BANKA SLOVENIJE

BANK OF SLOVENIA

EUROSYSTEM

FINANCIAL STABILITY REVIEW

MAY 2010

Published by:
Bank of Slovenia
Slovenska 35

1505 Ljubljana

Tel: +3861 47 19 000
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The Financial Stability Review is based on figures and information available at the end of March 2010, except where otherwise stated.

This publication is also available in Slovene.

ISSN 1581-9752 (print version)
ISSN 1581-9760 (internet version)

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Abbreviations:

AJPES	Agency of the Republic of Slovenia for Public Legal Records and Related Services
AMC	Association of Management Companies
APP	Agency for Payment Transactions, Supervision and Information
AUP	Average unit price of mutual fund
BoS	Bank of Slovenia
BRIC	Brazil, Russia, India and China
CCBM	Correspondent Central Banking Model
CEIOPS	Committee of European Insurance and Occupational Pensions Supervisors
CSCC	Central Securities Clearing Corporation ECB European Central Bank
ECBC	European Covered Bond Council
EMU	Economic and Monetary Union
EMU16	Members of the euro area other than Slovenia
EONIA	Euro OverNight Index Average (weighted average interest rate for overnight credit)
ESCB	European System of Central Banks
EU8	New EU Member States not in the euro area
EU25	EU Member States prior to the inclusion of Bulgaria and Romania
EU27	EU Member States
EU3	EU Member States prior to enlargement of 1 May 2004 not in the euro area
EURIBOR	Interbank interest rate at which representative banks in the euro area offer deposits to one another
EUROSTAT	Statistical Office of the European Communities
IC	Investment company
IF	Investment fund
IFRS	International Financial Reporting Standards.
IMF	International Monetary Fund
ISA	Insurance Supervision Agency
Leaseurope	European Federation of Leasing Company Associations
LJSE	Ljubljana Stock Exchange
LTI	Loan-to-income ratio
LTV	Loan-to-value ratio
MCs	Management companies
MF	Mutual fund
OECD	Organisation for Economic Co-operation and Development
OFIs	Other financial institutions
P/E	The P/E ratio is the ratio of the share price to the most recent annual net earnings per share.
PDII	Pension and Disability Insurance Institute
PIX	Investment funds index
RTGS	Real-Time Gross Settlement
SAS	Slovenian Accounting Standards
SBI 20	Leading Slovenian stock market index
SI O/N	Interest rate for unsecured interbank overnight deposits in euros between Slovenian credit institutions and euro area credit institutions
SKD	Standard classification of economic activities
SLA	Slovenian Leasing Association
SLONEP	Slovenian real estate portal (www.slonep.net)
SMA	Securities Market Agency
SORS	Statistical Office of the Republic of Slovenia
S&P	Standard and Poor's
TARS	Tax Administration of the Republic of Slovenia
TR	Turnover ratio
Vzajemci.com	Portal of Slovenian mutual funds (www.vzajemci.com)

CONCLUSIONS

Despite the gradual recovery in the Slovenian economy, which has been reflected in low but unstable current rates of GDP growth since the second quarter of last year, the dimensions of the consequences of the economic crisis for the banking system are still being observed. The contraction of 7.8% in economic activity in the last year is being reflected in a stagnation in lending to non-financial corporations and a deterioration in the quality of the banking system's credit portfolio. Here Slovenia is no different from the majority of other euro area countries.

The restructuring of Slovenian banks' funding is an unfinished process. In the last year the banks primarily obtained short-term funding, which is not a stable basis for the beginning of a new credit cycle. Liabilities to foreign banks declined by a fifth last year, and could only be replaced by an increase in liabilities to the Eurosystem and by government deposits at banks. The government deposits were the proceeds of bond issues in the rest of the world. There was thus no decline in the Slovenian economy's dependence on foreign funding. It remains at the level of 37% of GDP; it was merely that private external debt was mostly converted into public debt. Slovenia remains highly sensitive to a change in funding conditions on the international financial markets, particularly in the circumstances of rising debt problems in certain euro area countries.

The low growth in loans is not merely the result of a change in the structure of the banking system's funding, but also of the inappropriate sectoral breakdown of GDP that arose in the period of expansion and the relatively high corporate indebtedness. The decline in economic activity, which was accompanied by a pro-cyclical tightening of credit standards at banks, did not merely affect corporates in their financing via bank channels. Trade credits also declined sharply. All of this increased corporate financial needs. This was exacerbated by poor corporate responsiveness to the altered circumstances and by expectations that bank financing would compensate for their own lack of response. In this situation errors related to business decisions made during the boom were quick to reveal themselves. All these elements together, in certain sectors in particular, are today leading to worse corporate liquidity and payment indiscipline.

The slow pace of the economic recovery, which is the result of global uncertainties, and also of poor business judgement during the period of expansion, has been reflected in an increase in funding costs and rising credit risk at the banks, in the context of an inadequate funding structure. The structural problems on the banks' balance sheets and the rise in credit risk led to a rise in premiums on market interest rates, thus widening the spread between Slovenian interest rates and average lending rates in the euro area. Alongside the increase in non-interest income, this was an important source of income for the banks for covering the sharp increase in impairment and provisioning costs.

Credit risk has been the most significant risk for the banks in the last year, alongside refinancing risk. The slow pace of the economic recovery and the tightened corporate liquidity situation led to an increase in loan repayment arrears. In certain sectors the proportion of loan repayments that were more than 90 days in arrears last year was significantly higher than in 2008, and the figure has continued to rise in 2010. The quality of the banking system's credit portfolio will therefore deteriorate further this year. The proportion of classified claims accounted for by non-performing claims and their coverage by impairments reached 2.3% and 3.9% respectively in February, and will increase further. The banks will therefore have to devote significantly more attention this year to the recovery of unsettled liabilities from obligors, and not merely to the more aggressive creation of impairments and provisions. As a result of rising impairment and provisioning costs, the deterioration in the banking system's income position, which last year was the result of low lending growth and a decline in the net interest margin, will be reflected this year in a worse operating result. A decline in the amount of relatively cheap funding, liabilities to the Eurosystem and the government in particular, and a probable rise in market interest rates will result in a rise in the banks' funding costs. All of this will increase income risk at the banks, and the significance, currently low, of interest-rate risk.

Bank solvency last year remained at almost the same level as in 2008, an indication of the change in the banks' business priorities. Attending to the maintenance of capital adequacy has become more important than lending growth. The surplus of regulatory capital over capital requirements, which at 30% last year reflected a satisfactory risk-bearing capacity on the part of the banks, will be difficult to maintain at the same level in the context of an increase in credit risk and a decline in income. A decline in the overall surplus in risk-bearing capacity, which varies from bank to bank, could trigger a defensive reaction to maintain its level by means of undesirable balance sheet contractions. This would hinder corporate participation in the recovery process. In addition, the banks must also consider the balance sheet consequences of the measures drafted as part of Basel III, which is now imminent. Deliberations of capital increases in these circumstances are becoming part of the process of the banking system's adjustments to the new situation. This is one of the key factors in demonstrating the financial stability of the Slovenian banking system, and it is therefore vital that bank management boards and owners promptly embark on the process of capital increases, thereby accepting responsibility for repairing past decisions concerning the take-up of credit risk.

The Financial Stability Review finds that certain risks increased in 2009. The sensitivity of the banking system and other financial intermediaries to potential shocks also remains relatively high in 2010.

Marko Kranjec, Ph.D.
Governor

EXECUTIVE SUMMARY

Developments in the Slovenian financial system in 2009 were influenced by the progress of the international financial turmoil and the profound effects of the adverse macroeconomic developments, which were reflected in a real decline of 7.8% in GDP.

The importance of monetary financial institutions in the Slovenian financial system has increased sharply in the last two years. Their total assets increased by EUR 9.2 billion, the ratio of their total assets to GDP rising to 149% as a result of the decline in GDP. After declining in 2008, by the end of 2009 the total assets of the non-monetary financial institutions had not reached the level seen two years earlier, despite rising to 46% of GDP. However, the increase in growth in non-monetary financial institutions in the circumstances of the recovery of the financial markets after the large fall in 2008 is an indication that the adverse impact of the financial turmoil on non-monetary financial institutions is diminishing. Isolated cases of consolidation between non-monetary financial institutions are an indication of the gradual adjustment to the modified circumstances, while there was a rise to 25 in the number of monetary financial institutions in Slovenia last year. Market concentration increased slightly in the banking sector. The market share of the five largest banks in terms of total assets amounted to 60%.

There were three main processes in the banking system last year. The first was the restructuring of funding as a result of the repayment of due liabilities to the rest of the world. The banks repaid liabilities in the amount of EUR 3.2 billion in 2009, and a further EUR 650 million in the first quarter of 2010. The banks carried out the restructuring in three ways. The Eurosystem provided euro area banks with the requisite liquidity at a fixed interest rate with full allotment in the context of a further extension of the maturity of refinancing, thereby providing banks with funding of maturity of up to 1 year. The refinancing rate was cut to 1%. The excess liquidity meant that interest rates on the money market were at record lows. The Slovenian banks remained net lenders to the rest of the world on the euro area interbank market for unsecured loans in the context of a decline in volume, while mostly securing the requisite funding of maturity of up to 1 year from the Eurosystem. Of this, the banks secured EUR 1.9 billion in three 1-year longer-term refinancing operations between June and December. At the same time the government invested a portion of the proceeds of EUR 4.0 billion from bond issues in 2009 in the form of bank deposits in Slovenia. The stock of government deposits at banks averaged EUR 3.5 billion last year, up EUR 2.1 billion on 2008. The third way in which the commercial banks restructured was the issue of 3-year bonds with a government guarantee with a total nominal value of EUR 2 billion. This was followed in April 2010 by the issue of 5-year bonds with a total nominal value of EUR 750 million by SID banka. The net increase of EUR 0.6 billion in household deposits contributed significantly less to the restructuring of bank funding than in previous years.

The second process seen over the last year and a half in the Slovenian banking system was a standstill in bank lending. One factor was the decline in creditworthy demand for loans. Lower economic growth, relatively high corporate indebtedness and a lack of adequate forms of collateral were factors in the decline in demand in the corporate sector, while the main factors in the household sector were the uncertain situation on the labour market and the anticipated fall in prices of residential real estate. Other factors in the standstill in lending were related to the supply of loans. The banking system responded to the increased credit risk from borrowers under the influence of the notable deterioration in the performance of individual sectors of the economy and rising financial indiscipline by tightening credit standards until the end of the year. At the same time the caution in lending was also the result of the uncertainty on the financial markets and the uncertainty relating to the timely provision of the requisite funding to restructure bank liabilities. The government mitigated the standstill in lending by means of guarantee schemes for corporate and household bank loans. Growth in total assets was down 4.5 percentage points on 2008 at 8%.

The third, and key, process for the banks was an increase in impairments and provisioning as a result of the sharp deterioration in the quality of the banking system’s investment portfolio and the realisation of credit risk. A deterioration in performance could not be prevented by increased income from trading, or by a slight decline in operating costs. As a result the banking system’s pre-tax profit was halved compared with 2008, while ROE declined to 3.83%. There was considerable realisation of credit risk in the Slovenian banking system in 2009.

Corporates operated in conditions of relatively low demand, limited financing, diminished liquidity and increased payment indiscipline in 2009. The flow of corporate financing was down drastically on 2008, at banks and non-bank financial institutions, from the rest of the world and inside the corporate sector. Business-to-business financing was able to mostly compensate for the decline in other financial resources the previous year. Corporate borrowing in the rest of the world declined last year more than domestic borrowing, primarily in the form of trade credits and loans raised at foreign corporates. This was one of the reasons for the increase in lending demand for short-term resources at Slovenian banks. The banks tightened their credit standards in 2009. One of the reasons for this was the structure of corporate financing. Corporates in Slovenia are over-indebted, the debt-to-equity ratio standing at 147%, compared with 105% in the euro area overall. Their dependence on the domestic banking system is high. Only in rare cases do they have the size and creditworthiness to access bank resources or the capital market at the European level. The basic problems of the domestic banks’ balance sheets are reflected in the financing needs of Slovenian corporates. These include a shortening of average funding maturity, which is cramping the space for investment activity. All of this is having an adverse impact on corporate liquidity, increasing the need for refinancing, and making financial intermediation in the circumstances of increased restriction of resources more difficult and more expensive. Because Slovenian corporates only finance themselves via securities issues in exceptional cases, they are even more dependent on bank loans. Interest rates for corporate loans fell in Slovenia last year, but more slowly than in the euro area overall. At the same time the banks increased their premiums over reference interest rates, in the context of primarily lending to clients at variable interest rates. This type of lending increased the risk related to corporate performance last year, their debt servicing burden increasing as the reference interest rates rose. The debt servicing burden had already risen last year, primarily as a result of increased borrowing in previous years. The largest increases were at non-financial holding companies, and in real estate activities and construction. The deterioration in corporate liquidity is the reason for the increase in arrears in loan repayment. The proportion of corporate liabilities to banks that are being settled more than 90 days in arrears doubled last year to 6.6%, and rose further in the first quarter of 2010. Prominent among the increasing arrears are non-financial holding companies, accommodation and food service activities, and, since the beginning of 2010, construction and real estate activities.

Households responded to the increased uncertainty and adverse situation on the labour market by slowing their borrowing. Other factors were high real interest rates and the tightening of credit standards. Despite the relatively low number of transactions on the residential real estate market, housing lending was solid, while consumer lending stalled. As a result the average maturity of household loans lengthened. The fall in interest rates on newly approved variable-rate loans, which accounted for three-quarters of the total, acted to encourage household borrowing. Household indebtedness and the debt servicing burden on household income increased last year. The household sector in Slovenia nevertheless remains relatively less-indebted compared with the euro area overall: at 34% of GDP its total financial liabilities at the end of the third quarter of 2009 were just under a half of the average financial liabilities of the household sector in the euro area overall. In the coming period of further deterioration in the situation on the labour market, it is the more-indebted low-income households that in particular will be more exposed to an increase in risk. The key increase in risk related to households and its possible spread into the banking system is the exposure to the risk of a change in market interest rates. For the moment they remain relatively low, but when they rise the household debt servicing burden will increase as a result of the prevalence of variable-rate loans and the lengthening of the average maturity of household loans.

The real estate market has been extremely exposed to the consequences of the economic crisis over the last year and a half. Inventories of unsold housing increased, while volume on the real estate market declined by more than a half. The construction sector, which was profoundly indebted even before the financial turmoil, borrowed sharply from banks last year primarily to refinance due loans. At the same time construction companies deferred or cancelled the settlement of liabilities to sub-contractors and suppliers, and delayed a cut in sales prices. The available figures for real estate prices in Slovenia indicate a decline of between 4.7% and 7.3% last year. The number of recorded transactions on the real estate market declined by 24%. Housing affordability increased last year, on the basis of the figures for Ljubljana. Sales prices are nevertheless still higher than fundamental prices, and the delay in purchases by households and the expectation of further price falls therefore come as no surprise. That the total value of new contracts for housing in 2009 was down almost three-quarters in 2008, with higher inventories of unsold housing, is an indication that the price adjustment of supply to the low level of demand is exceptionally slow. There remains the problem on the Slovenian real estate market that the construction companies are often also the investors.

The realisation of credit risk at the banks was expected in 2009 given the deterioration in the macroeconomic situation, corporate performance, and household behaviour. The decline in the quality of the banks' investment portfolio in 2009 was reflected in a rise of 30% on the previous year in non-performing claims, and year-on-year growth of 78% in impairment and provisioning costs. Further corroboration came from the acceleration in the downgrading of claims from the A and B ratings to the C rating, with the likelihood that a portion of these claims will be classed as non-performing. The proportion of non-performing claims rose from 1.8% to 2.2% in 2009. The large domestic banks were the most prominent in downgrading claims to the C rating, while the small domestic banks were the most conservative in classing claims as non-performing. The smallest deterioration in portfolio quality was at the banks under majority foreign ownership, partly as a result of their less conservative way of assessing the credit ratings of debtors and the rising proportion of their credit portfolio accounted for by household loans. Non-financial holding companies, and corporates in the sectors of construction, wholesale and retail trade, and accommodation and food service activities are prominent in the increase in the banks' non-performing claims against non-financial corporations. Impairments and provisioning for construction companies are above-average. Arrears of more than 90 days in the settlement of liabilities to banks rose sharply, non-financial corporations, non-residents and sole traders recording above-average increases. The position for the last of these and for SMEs will deteriorate further, as the adverse liquidity situation and financial indiscipline continue. An increase in the number of bankruptcies is very likely, and the banks will further increase their impairments and provisioning on the balance sheet, thereby reducing net profits.

Given the increase in credit risk, the banks have begun to reduce the proportion of newly approved loans that are unsecured. Overall 40% of newly approved loans were unsecured in 2009. The proportion of unsecured corporate loans declined to 35%. The proportion of secured corporate loans accounted for by loans with real estate collateral increased sharply. The proportion of claims against construction companies more than 90 days in arrears that are unsecured varies between the groups of banks, from 20% at the large domestic banks to almost 40% at the banks under majority foreign ownership. The risk pertaining to claims secured by real estate is being increased for the banks by the possibility that claims of several banks are secured by a single item of real estate, so that the actual value of the real estate collateral is lower. The banks' classified claims against holding companies declined in 2009. Claims against holdings varied between the groups of banks, from 3.5% to 5.5% of total classified claims. The proportion of claims against holding companies more than 90 days in arrears had increased to a quarter by February 2010, of which 60% were unsecured.

The banking system's capital adequacy was almost unchanged in 2009, the overall ratio ending the year at 11.6%. Growth in regulatory capital and capital requirements was low. The large domestic banks had the highest capital adequacy, slightly higher than the overall capital adequacy of comparable banks in the EU. The banks under majority foreign ownership and the small domestic banks have lower capital adequacy than comparable banks in the EU. For the former, it is the case that in the adverse situation they can no longer count on support from their parent banks as they did previously. For the small domestic banks it is the case that they are the most vulnerable group of banks according to certain other solvency criteria. The banking system's original own funds amounted to EUR 4.1 billion at the end of 2009. The quality of the banking system's own funds increased as the proportion of own funds before deductions accounted for by original own funds increased, but only as a result of changes at the large domestic banks. With the halving of the banking system's pre-tax profit, and further realisation of income risk expected, the impact of retained earnings as a resource for increasing original own funds is diminishing. The banks' dependence on the readiness and ability of owners to inject capital has increased. In January 2010 the Bank of Slovenia called on the banks to assess their need to increase capital. According to the available survey data, seven banks are planning capital increases in the next three years, but at the same time it is estimated that the banking system has the potential to increase subordinated debt by EUR 1.4 billion. The banking system has maintained a 30% surplus in regulatory capital over the capital requirements. A decline in the overall surplus in risk-bearing capacity, which varies from bank to bank, could trigger a defensive reaction to maintain its level by means of undesirable balance sheet contractions. This would hinder corporate participation in the recovery process. The banks must also consider the balance sheet consequences of the measures drafted as part of Basel III, which is about to come into effect. Deliberations of capital increases in these circumstances are becoming part of the process of the banking system's adjustments to the new situation. Capital requirements increased to EUR 3.2 billion in 2009. The deterioration in the credit portfolio has been reflected in a doubling of the capital requirements for past-due items. The breakdown of the capital requirements for credit risk is least favourable at the small domestic banks.

Interest-rate risk as measured by the difference between the average repricing periods for asset and liability interest rates has been increasing since the middle of last year. The likelihood of a rise in interest rates is growing, and with it the likelihood of the realisation of interest-rate risk. Currency risk has increased, but remains low. The proportion of items in foreign currency declined, and stood at around 5% on the asset side and around 3.5% on the liability side at the end of 2009. As a result of the decline in lending to non-banking sectors in Swiss francs, the proportion of the banking system's balance sheet accounted for by Swiss francs declined.

Insurers performed solidly in 2009, despite claims increasing sharply for the second consecutive year. Some insurers declared losses. Net insurance technical provisions and their coverage by the assets covering technical provisions increased. The latter increased to EUR 4.1 billion, more than the increase in total assets, thereby increasing insurers' robustness against any shocks. The insurers' total assets increased by a relatively high 10.9% to EUR 5.1 billion. The insurers' ROE rose to 3%, higher than the average ROE at insurers in the euro area. Six insurers carried out capital increases in 2009. In contrast to the aforementioned instances of positive performance, last year's gross written premium was the lowest since 2000. It is cause for concern that its largest decline was in pension insurance. In addition, the number of policyholders covered by voluntary supplementary pension insurance and the amount of premium both declined. After increasing sharply in 2008, the ratio of gross claims paid to gross premium written remained at the same level, primarily as a result of an increase in natural disasters. The size of the insurance sector in Slovenia remains relatively low, as total premium in the amount of 6.3% of GDP or EUR 954 per person is just 38% of the average premium per person in the euro area. It is encouraging that the investment structure of Slovenian insurers remains relatively conservative: at just over 60%, the proportion accounted for by the safest investments (deposits, government debt securities, other debt securities) is 6 percentage points higher than the comparable euro area average. The amount of credit insurance declined last year as a result of the standstill in lending. The sum insured for export loans declined particularly sharply. The claims ratio for credit insurance also deteriorated, primarily because of export insurance.

After seeing a decline of more than 50% in assets under management in 2008, the investment funds recorded an increase of almost 17% last year, and also increased the return on their investments. Banks manage 41% of the domestic mutual funds' assets as a result of their co-ownership of management companies. The proportion of investment fund assets accounted for by mutual funds stood at 84% at the end of March 2010, equivalent to EUR 1,969 million. Equity funds are prevalent in Slovenia, and in contrast to other EU countries there was no change worthy of note in the structure of the sector during the financial turmoil. Last year's increase in investment funds assets in Slovenia was large relative to the euro area average. However, the ratio of investment fund assets to GDP in Slovenia is almost six times lower than the euro area average at 6.4%. The proportion of investment fund assets accounted for by investment companies stood at

16% at the end of March, but they are diminishing in importance as they have to convert into mutual funds by the end of 2011.

The financial turmoil hit the leasing sector particularly hard, the volume of business declining by 46% in 2009. Real estate leasing declined by more than a half, in line with the rapid decline in construction activity, and demand and the number of transactions on the real estate market. The banks' exposure to leasing companies declined. The decline in the volume of leasing business was partly the result of the leasing companies' response to the adverse business situation and uncertain position of potential lessees. The leasing companies increased their requirements for participation by lessees, required additional collateral, increased their margins and shortened the average maturity in real estate leasing. The leasing companies limited their exposure to corporates by restructuring equipment leasing business in favour of car leasing at the expense of leasing of commercial vehicles and equipment. The debt-to-equity ratio is also deteriorating at leasing companies, although the banks' exposure to leasing companies accounted for just 4% of loans to non-banking sectors.

The financial infrastructure is ensuring the reliable, timely and cost-effective settlement of financial claims and liabilities. The functioning of the TARGET2-Slovenija and SEPA internal credit transfers payment systems is important to financial stability in Slovenia. The latter retail payment system replaced the Bank of Slovenia's Giro Clearing system at the end of July 2009. The two systems recorded availability of more than 99.8% last year, thereby demonstrating that operational risk is being managed adequately.

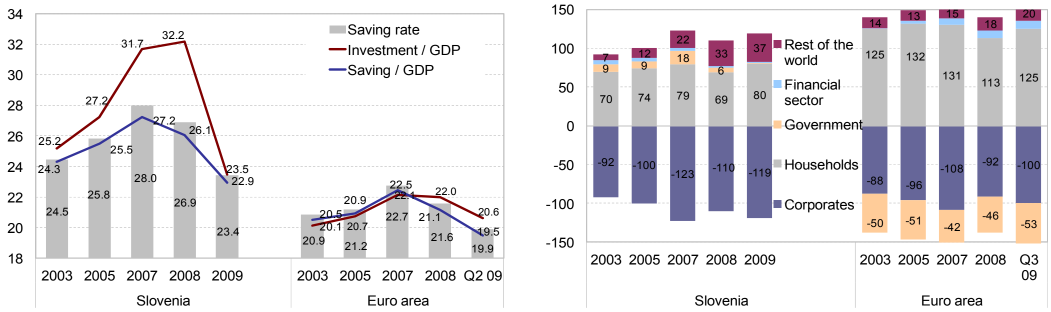
Financial stability in Slovenia will be adversely affected over the next one to two years by corporate under-capitalisation, the continuing realisation of credit risk at banks and the uncertain situation in the international environment caused by the most-indebted euro area countries. The financial system can only mitigate the problem of corporate under-capitalisation, but cannot reduce it, while it is powerless to affect factors in the international environment. Given the circumstances, the Slovenian financial system is functioning relatively well, albeit in a much more uncertain situation. Any shocks could impact it significantly faster than in previous years. The degree to which the financial system is capable of at least maintaining its to date satisfactory robustness against any shocks is becoming the key. In the banking system it is vital that the continuing process of creating adequate impairments and provisioning is supported by constant adjustments in the banks' capital adequacy to the risks that they have already taken up.

1 INTER-SECTOR FINANCIAL CLAIMS AND LIABILITIES

The ratio of investment to GDP fell sharply because of the adverse economic situation.

From the point of view of a surplus in financial assets, households remain nationally the most important institutional sector, providing money to finance the investments of other sectors. Despite a decline in economic activity, non-financial corporations recorded an increase of 9 GDP percentage points in their negative position as a result of lower revenues and debt repayments. They obtained most financial assets via the domestic banking sector, which during this period was funded primarily by government assets. These were obtained via bond-based borrowing. For this reason dependence on foreign resources increased to 37% of GDP, despite the decline in economic activity. The national saving rate stood at 23.4%, down 3.5 percentage points on 2008. The ratio of saving to GDP declined by 3.2 percentage points, as a result of a larger decline in GDP than in final consumption expenditure. The ratio of investment to GDP also declined simultaneously, by fully 8.7 percentage points. This was the result of a standstill in demand and in foreign trade, and limited access to financial resources.

Figure 1.1: Saving rate,[1] percentage ratios of investment and saving to GDP, and net financial position of individual economic sectors



Sources: Bank of Slovenia, SORS, ECB, Eurostat

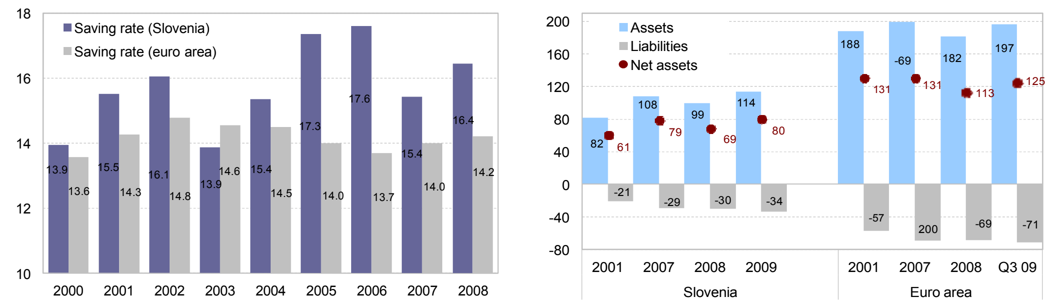
Given Slovenia's involvement in international financial flows, the recovery in foreign markets, which is uncertain and varies from sector to sector, will have a more significant impact on domestic economic growth this year. Other factors in the recovery of domestic economic activity will be the accessibility and price of financial resources, and an improvement in competitiveness.

Households

The household saving rate in 2008 was again higher than the euro area average at 16.4%.

Households increased their saving rate to 16.4% in 2008, 2.2 percentage points higher than the euro area average. The increase was the result of the impact of the economic crisis on the uncertain position faced by households, who thus opted to defer major purchases. The deterioration in the situation on the labour market means that no increase in saving is expected to have occurred in 2009.

Figure 1.2: Saving rate, financial assets and liabilities, and net financial position (net assets) of households as a percentage of GDP



Sources: Bank of Slovenia, SORS, ECB

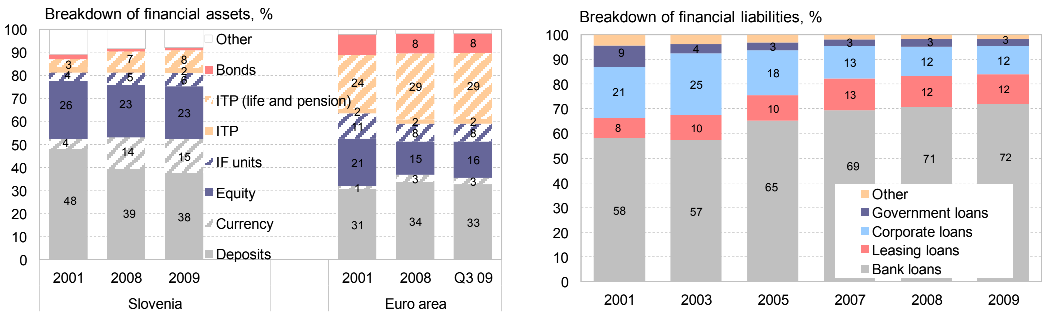
[1] The saving rate is an indicator calculated from sectoral accounts, and is the ratio of gross saving to gross disposable income. In addition to employee compensation and social security benefits it also includes gross operating surplus from manufacturing, other current transfers (such as compensation from non-life insurance, and ownership-related income such as interest and corporate profit distributions), but does not include changes in value or capital gains.

Structural reforms to pension insurance to ease the burden of contributions would help to increase household assets. At 114% of GDP, household assets in Slovenia are 58% of the average figure in the euro area. The convergence process is slow, primarily as a result of high labour taxation, i.e. high social contributions, and as a result of the prevalence of the manufacturing of products with low value-added, where employee earnings are relatively low.

The net assets of Slovenian households remain 45 GDP percentage points down on the euro area average.

The indebtedness of Slovenian households is increasing significantly more quickly than that of the average household in the euro area, primarily via loans from the financial sector. However, at 34%, the total financial liabilities of Slovenian households at the end of 2009 were still just under half of the financial liabilities of the average euro area household. Households' net assets at the end of 2009 were up on 2007 at 80% of GDP, although the gap by which the figure trails that of the euro area is only diminishing slowly.

Figure 1.3: Breakdown of financial assets of households in Slovenia and the euro area (left), and breakdown of financial liabilities of households in Slovenia (right)



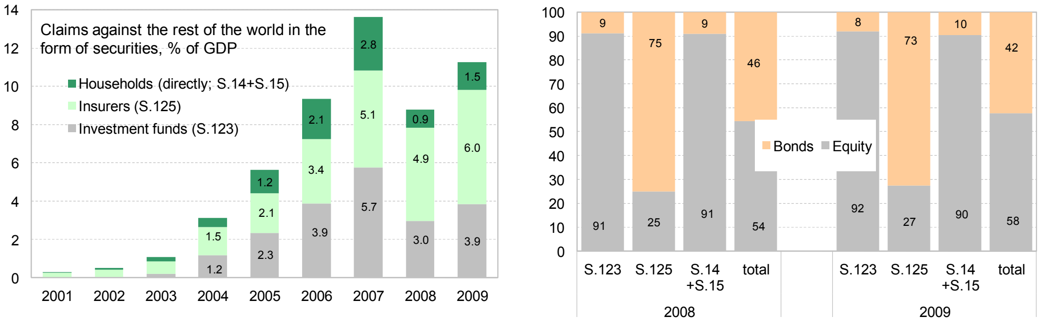
Note: ITP: insurance technical provisions; IF: investment funds. Includes the household sector (S.14) and non-profit institutions serving households (S.15).
Sources: Bank of Slovenia, ECB

There remains a high proportion of high-risk investments in household assets, and insufficient pension insurance and life insurance.

Despite the crisis Slovenian households have not actively restructured their financial assets. The proportion accounted for by bank deposits, which was higher in 2008 as a result of the inflow of money from the sale of financial instruments on the capital markets, was down 1 percentage point at the end of 2009 at 38%. The decline was conditioned by the weaker economic position of households, total earnings from net wages having declined while social security benefits increased, which do not enable saving. The lack of appetite for bond-based saving can be attributed to a lack of financial information on the part of investors. This form of saving is negligible in Slovenia compared with the euro area, despite the past losses realised on the capital markets. Some 29% of assets are invested in equity and investment fund units, primarily higher-risk funds. The most significant structural discrepancy is the shortfall in Slovenian households' saving for a secure future in the form of life insurance and pension insurance, which is 21 percentage points lower than the equivalent euro area average. Financial assets earmarked for saving for the third age remain low because of the current high burden placed on household income by social contributions, which do not encourage additional saving, while the existing pension system is becoming inadequate over the long term.

Bank loans are prevalent among households' financial liabilities, accounting for 72% of the total, followed by loans from leasing companies and loans from corporates at 12% each. Growth in household borrowing had slowed to 5% by the end of 2009, having stood at 24% in 2007 and 11% in 2008.

Figure 1.4: Breakdown of household claims against the rest of the world by intermediary as a percentage of GDP (left), and by foreign equity / debt securities (right) in percentages



Note: S.123: Other financial intermediaries, except insurance corporations and pension funds; S.125: Insurance corporations and pension funds; S.14 and S.15: Households and non-profit institutions serving households. The figures include a simplification: the total investments of sectors S.123 and S.125 in foreign securities are treated as household assets, although a specific proportion include intra-sectoral investments and corporate investments.

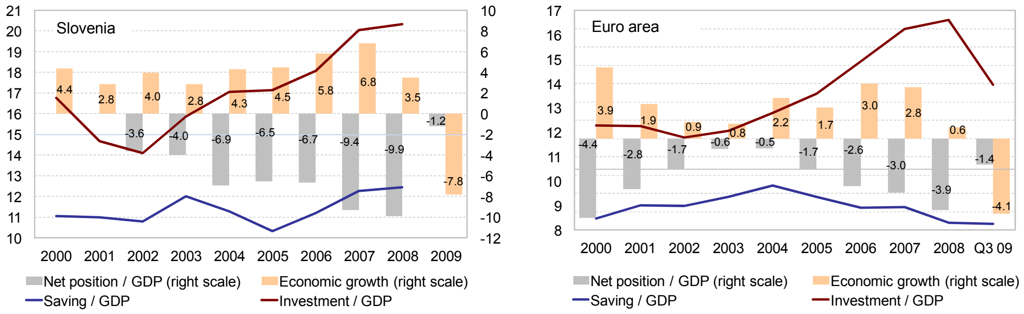
Sources: Bank of Slovenia, SORS

Last year households held 11% of their assets invested in foreign securities, 2.4 percentage points less than the figure before the outbreak of the financial turmoil. Of these, 58% were in equity, down 13 percentage points on the pre-crisis figure. This proportion declined in 2008 as a result of capital losses. Direct demand for foreign securities was low last year. The rise in direct investments by households to 1.5% of GDP in 2009 is a reflection of revaluation, in addition to net purchases. Of those held indirectly via institutional investors, the largest proportion of claims against the rest of the world in the form of securities were recorded by insurers, at 6% of GDP. This was a consequence of investments in unit-linked insurance, which are long-term in nature and are less sensitive to the financial turmoil.

Slovenian households' claims for foreign securities were down 2.4 percentage points on the pre-crisis period at 11% of GDP.

Non-financial corporations

Figure 1.5: Investment, saving and net position in transactions of non-financial corporations as a percentage of GDP, and real economic growth in Slovenia and the euro area in percentages



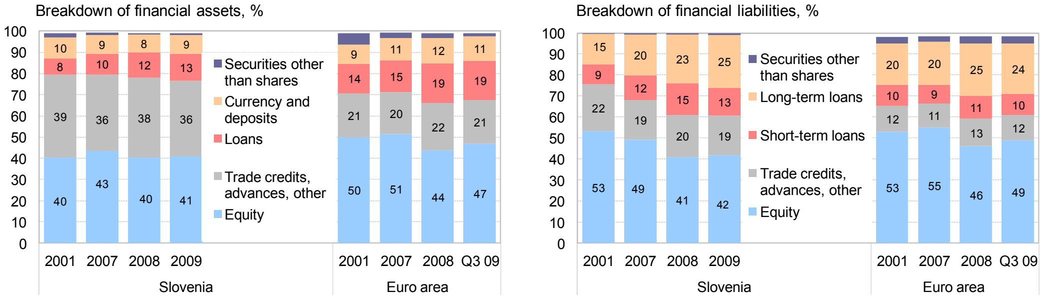
Note: The Q3 2009 figure for the euro area is the total for the preceding four quarters. The net financial position represents the difference between financial transactions from assets and liabilities in the period in question.

Sources: Bank of Slovenia, SORS, ECB, Eurostat

Non-financial corporations' net negative financial position from transactions had declined to 1.2% of GDP at the end of last year as a result of a large decline in investment activity. The decline in aggregate demand brought a decline in corporate borrowing. In addition to the tightened conditions and the decline in lending at the domestic banks, there was also a decline in loans raised in the rest of the world. According to financial accounts figures, the stock of foreign loans to Slovenian corporates increased by 32.2% in 2008, but declined by 5.1% in 2009 to reach EUR 4.7 billion, as a result of higher net repayments in the final quarter. The crisis forced non-financial corporations to consider borrowing via the bond market, which was larger than in previous years, but was still negligible compared with the euro area.

Lower corporate borrowing as a result of low economic activity and tighter loan conditions.

Figure 1.6: Breakdown of financial claims and liabilities of non-financial corporations in percentages



Sources: Bank of Slovenia, ECB

The breakdown of financial assets at the end of 2009 was similar to that a year earlier. Despite the purchase opportunities, there was no increase in the proportion accounted for by equity as a result of the lack of funds for investment. The proportion accounted for by trade credits, advances and other remained high compared with the euro area average. This was a result of the high business-to-business financing in Slovenia.

No major capital increases again last year despite corporate difficulties.

Although corporates needed fresh capital to stay competitive and to survive on the market, there were no major capital increases in 2009. The proportion accounted for by equity thus remained 7 percentage points lower than the euro area average at 42%. As a result of the low level of equity and the lack of financing via debt instruments, Slovenian corporates had difficulties in refinancing loans, which account for 38% of their total liabilities.

Financial sector

The financial sector increased domestic borrowing and made net repayments to the rest of the world.

After the outbreak of the financial turmoil, Slovenian banks sharply reduced their borrowing in the rest of the world, by means of which they had previously financed the economy during the period of high economic growth. For this reason the banks took up the 1-year liquidity allocated by the ECB, and increased government deposits invested after the issue of long-term debt securities, household deposits, and issued securities. In the Slovenian banking system there is not yet an active mortgage bond market, which fulfilled an important role in the euro area during the crisis.

In 2009 the financial sector[2] increased its domestic liabilities by 27 GDP percentage points. It increased its liabilities in the rest of the world from debt securities by 4.7 percentage points, while simultaneously reducing its liabilities from currency, deposits and loans.

General government sector

The government sector increased its domestic net assets to 19.4% of GDP, while increasing its net debt to the rest of the world to 19% of GDP.

After recording a large decline in net financial position in 2008, the general government sector reduced it by a further 5.2 percentage points in 2009 to 0.4% of GDP. The largest increase in government claims in the form of deposits was recorded by the financial sector, as a result of the investment of the proceeds of borrowing on the capital market. The large increase in liabilities to the rest of the world and to the Slovenian financial sector from debt securities was the result of the issue of three bonds with a total nominal value of EUR 4 billion. The largest increase on the liability side was recorded by the proportion accounted for by debt securities, which accounted for more than half of financing. Short-term loans were also a major resource, accounting for 14% of the total.

Rest of the world

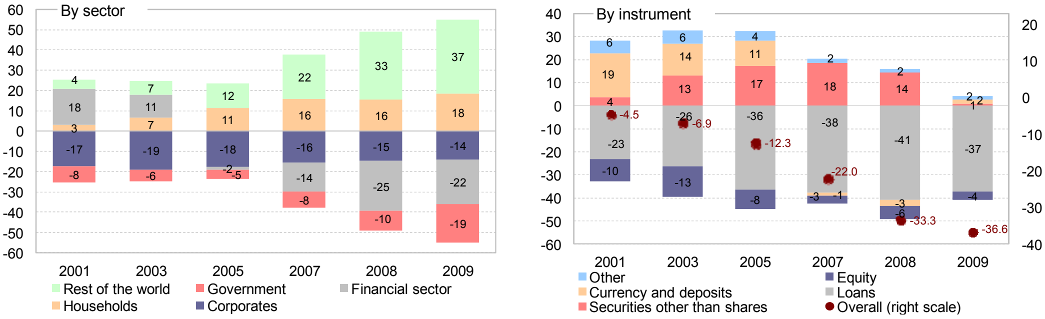
A rise in the net financial position against the rest of the world as a result of high government borrowing.

In 2009 the Slovenian economy increased its net financial liabilities to the rest of the world to 37% of GDP. The household sector's net surplus against the rest of the world increased slightly by 2 percentage points to 18% of GDP. The financial sector's net negative position declined by 3 percentage points to 22% of GDP. The most evident change was recorded by the general government sector, whose negative financial position increased by 9 percentage points to 19% of GDP. This was the result of the response to

[2] Includes the entire financial sector (S.12) in accordance with the classification of the system of financial accounts.

the situation on the financial markets, which required a change in the methods of financing.

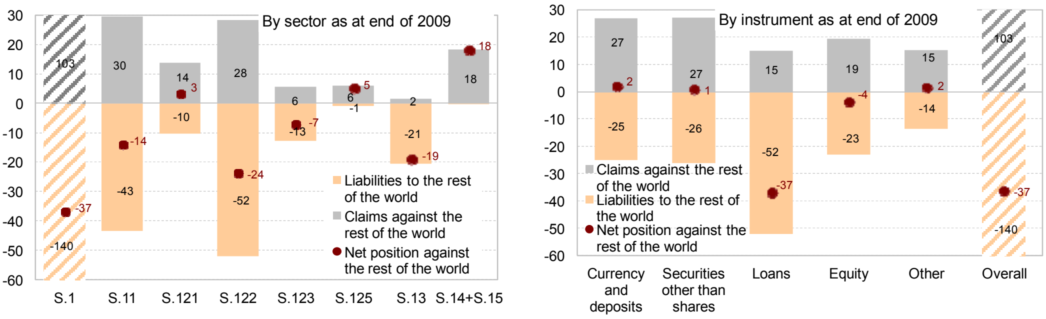
Figure 1.7: Net financial position against the rest of the world as a percentage of GDP, by sector and financial instrument



Source: Bank of Slovenia

As funding from the rest of the world declined, the commercial banks' debt repayments in the rest of the world were larger than their increase in liabilities to the ECB. For the purpose of financing the budget and general financing, last year the government issued a large amount of bonds, whose purchasers were mostly non-residents. As a result the net financial position against the rest of the world in the form of securities other than shares declined by 13.6 percentage points, although it remained positive at 0.8% of GDP. Net financial liabilities to the rest of the world in the form of loans raised declined last year, as a result of the lack of interbank lending and reduced corporate borrowing in the rest of the world.

Figure 1.8: Financial claims, liabilities and net position against the rest of the world as a percentage of GDP, by sector and financial instrument at the end of 2009



Note: S.1: Slovenian economy; S.11: Non-financial corporations; S.121: Central bank; S.122: Other monetary financial institutions (includes commercial banks and savings banks); S.123: Other financial intermediaries, except insurance corporations and pension funds (includes investment funds and leasing companies); S.125: Insurance corporations and pension funds; S.13: General government; S.14 + S.15: Households and non-profit institutions serving households.

Source: Bank of Slovenia

2 ECONOMIC TRENDS IN SLOVENIA

2.1 Economic activity and inflation

A sharp decline in GDP in 2009.

Real GDP declined sharply in Slovenia in 2009, by 7.8%. The negative economic growth was the result of the global decline in gross investment, which was down 30.2% last year, inventories accounting for almost half of the this decline. Household consumption also declined last year, by 1.4%, while government spending rose by 3.1%. The decline in foreign demand meant that exports were down 15.6% last year, while imports were down 17.9%, mitigating the contribution to the decline in GDP made by net trade by 2.1 percentage points. The deepening of the recession ceased in the second quarter of last year, GDP recording a current increase of 0.3%. In terms of the GDP output structure, last year there was a sharp contraction in activities in the manufacturing sector (16.5%), although the year-on-year decline slowed in the final quarter to 4.3%. Last year also saw a sharp decline in activity in the construction sector (15.9% annually), where growth remained strongly negative even in the final quarter, at -18.2% (source: SORS).

Figure 2.1: GDP growth (left) and inflation indices in Slovenia and the euro area in percentages

Source: Bank of Slovenia

The decline in economic activity in 2009 also brought a fall in average inflation.

Average inflation in Slovenia as measured by the HICP stood at 0.9% in 2009, down 4.6 percentage points on the average in 2008. The sharp decline in economic activity was the major factor in the significant fall in inflation in 2009. During the first seven months of last year another factor in the fall in year-on-year inflation was a base effect, namely the high growth in energy prices in the same period of the previous year.

The current account deficit was much smaller than in previous years.

Having widened rapidly between 2006 and 2008 to reach 6.2% of GDP in 2008, the current account deficit declined to just EUR 0.2 billion or 0.6% of GDP in 2009. Merchandise imports having declined more rapidly in year-on-year terms than exports, the trade deficit also declined, to just a fifth of that recorded in the previous year.

2.2 Country risk

Ratings of country risk

Slovenia's country risk rating was unchanged last year.

There was no change in Slovenia's ratings of country risk, which continue to reflect its stable position among the AA-rated countries.

Moody's held Slovenia at Aa2, with a stable outlook. In its most recent country risk rating issued in October 2009, the agency stated that there were four major factors in the aforementioned rating: a) the country's economic strength, which is based on high income and a small economy, although there is a lack of economic diversification; b) high institutional strength, which reflects the effectiveness of the government, the strength of laws and membership of the EU; c) the financial strength of the government, the agency emphasising the government's access to financing on the domestic and foreign markets, its capacity to repay its debts, and the medium-to-high fiscal flexibility; and d) the country's low sensitivity to a downgrading for reason of political, economic or financial shocks. In its report the agency states that the government's anti-crisis programme has been reasonably effective, despite a rigid labour market, and that the government responded swiftly with measures to protect the banking system.

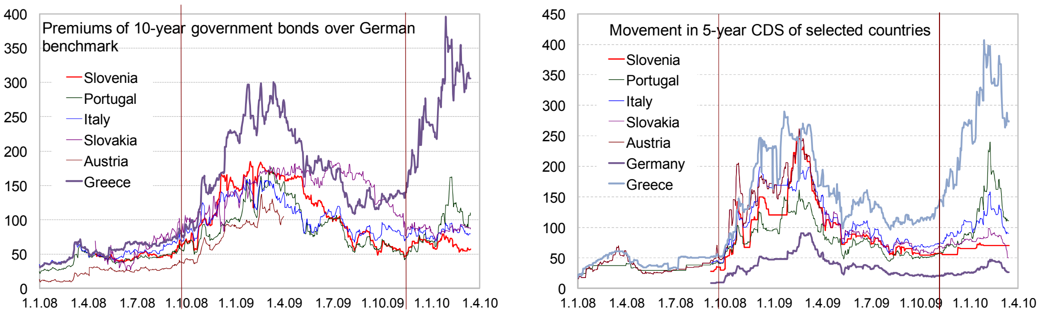
S&P made no change to its Slovenia rating last year (AA/A-1+). S&P cited the government's medium-term and long-term commitment to fiscal prudence and the stable outlook as factors holding the rating up. The agency cited the low level of welfare compared with other AA-rated countries and reticence in certain structural reforms as factors reflecting the country's weakness. It also nominated the continuation of economic restructuring as a key factor in a long-term upgrading.

Risk premium on Slovenian government securities

The risk premiums for Slovenian government securities over the German benchmarks fell in 2009 and early 2010.

The premiums on 3-year and 10-year Slovenian government bonds over the benchmark German bonds showed a clear rising trend after the worsening of the financial turmoil in autumn 2008. By March 2009 they had reached 170 basis points on 3-year Slovenian government bonds, and 167 basis points on the 10-year bonds. The premiums over the German bonds had fallen to 50 basis points on 3-year bonds and 88 basis points on 10-year bonds by the beginning of April 2010. The premiums on the 3-year bonds over the comparable German bonds were lower than those on the comparable Portuguese, Irish and Spanish bonds, and slightly higher than those on the comparable Italian bonds.

Figure 2.2: Premiums on 10-year government bonds of Slovenia and selected countries over the comparable German bonds in basis points (left), and 5-year credit default swap rates in basis points



Note: The vertical lines on the two figures mark the worsening of the financial turmoil in September 2008 (left) and the outbreak of the Greek debt crisis in autumn 2009 (right).
Source: Bank of Slovenia

Similar movements have been exhibited by credit default swap rates. The spread between 5-year CDSs for Slovenia and Germany stood at 96 basis points in March of last year, but had fallen to 40 basis points by the first half of this March.

Potential risk to the Slovenian financial system from the debt problems of certain euro area countries

The Greek sovereign debt crisis had an impact on borrowing costs in the rest of the world.

Countries whose fiscal situation is sustainable have also felt the indirect consequences of the Greek debt crisis, in the form of raised risk premiums. The adverse impact on the cost of borrowing for euro area countries with lower credit ratings could significantly increase in the event of a further deterioration in the Greek debt crisis, and its possible spread to other countries. In this event the consequences for Slovenian banks would also be indirect, as during the outbreak of the financial turmoil in 2007. Exposure to Greek, Spanish and Portuguese sovereign debt stood at EUR 270 million at the end of March 2010. In the rising uncertainty investors have migrated to government bonds of higher-rated euro area countries, which is raising Slovenia's borrowing costs. Higher costs of servicing sovereign debt also entail higher borrowing costs in the rest of the world for the Slovenian financial and non-financial sectors. The worsening of the sovereign debt crisis in Greece and its spread could make funding significantly more expensive, given the high proportion of foreign funding of the Slovenian financial sector, the banking system in particular. The financial sector would pass increased borrowing costs through to the real sector in the form of higher interest rates on loans and other forms of financing. It is therefore vital for Slovenia to consistently follow the European Council recommendations designed to eliminate the excessive general government deficit, and to ensure the long-term sustainability of its public finances by carrying out the planned structural reforms (labour market, pension system, healthcare). Only in this way will it retain the credit credibility that is has achieved on international financial markets, and ensure the long-term sustainability of financing for its economic development.

Downgradings for Greece, Spain and Portugal triggered additional investor migration to safer investments.

At the end of April S&P downgraded Greece, Spain and Portugal. Greek sovereign debt is now classed as junk, and the premiums on 10-year Greek government bonds over the benchmark German bonds reached record highs. Risk aversion therefore increased, and there was increased migration to safer government debt securities. The premiums on 10-year Slovenian government bonds over the benchmark German bonds had risen to 99 basis points by the end of April 2010.

3 HOUSEHOLD SECTOR

3.1 Household borrowing

A significant slowdown in the pace of household borrowing in 2009.

Growth in household borrowing slowed sharply in 2009. The household sector's financial liabilities increased by just 5.4% last year. The fall in GDP meant that they rose by 3 percentage points as a proportion of GDP to 33.5%. The slowdown in growth in household income and the rise in unemployment increased the debt servicing burden, which will continue to increase this year. This will lead to an increase in the systemic risk to the financial sector presented by the household sector.

There was almost no change in the breakdown of household debt by creditor sector in 2009. Households are most indebted in the form of loans from banks and other financial intermediaries, and in the form of trade credits from corporates.

Table 3.1: Stock of household financial liabilities by instrument

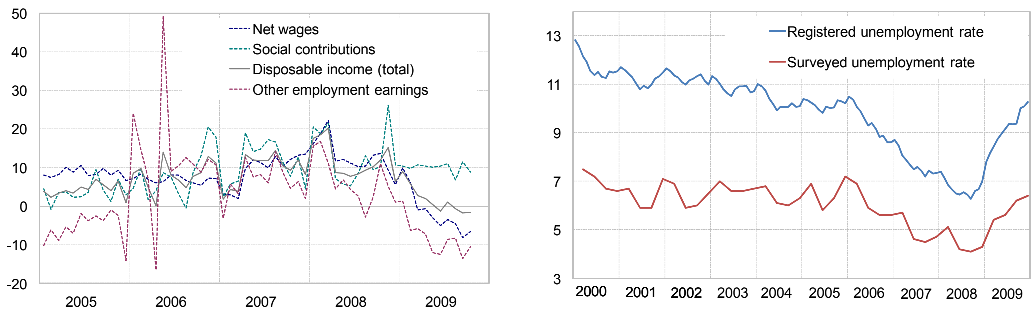
	2005	2006	2007	2008	2009
			(EUR million)		
Total	6,882	8,093	10,054	11,204	11,805
growth, %	19.7	17.6	24.2	11.4	5.4
as % GDP	24.0	26.1	29.2	30.2	33.5
			Breakdown, %		
Loans	79.7	83.7	85.7	86.6	87.3
Corporates	5.1	4.2	3.8	3.1	3.4
Banks	62.5	67.8	68.9	70.6	71.9
Other financial intermediaries	10.0	10.0	12.2	11.6	10.9
Government	1.3	1.0	0.8	1.4	1.2
Rest of the world	0.8	0.7	0.0	0.0	0.0
Trade credits and advances	12.4	11.7	10.4	9.9	9.3
Other	7.9	4.6	3.8	3.5	3.4

Source: Bank of Slovenia

Lower demand for loans is the result of negative expectations on the part of households.

The rise in real interest rates and the tightening of credit standards were supply-side factors in the increase in household debt. Major factors in the reduced demand for loans were rising unemployment and the slowdown in growth in household income, which were reflected in the low value of the consumer confidence indicator (consumer expectations regarding their economic position in the next 12 months).[3]

Figure 3.1: Year-on-year growth in monthly household income (left) and unemployment rate (right) in percentages



Sources: SORS, PA

Household borrowing at banks

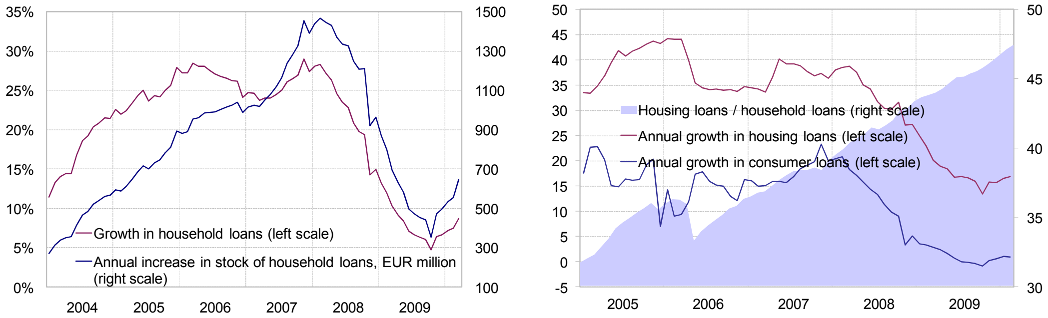
Growth in bank loans to households fell to 6.7% in 2009.

Growth in household loans from banks declined by 8.2 percentage points in 2009 to 6.7%. Growth in housing loans declined to 15.7%, while growth in consumer loans declined to 0.6%. Growth in household loans was declining until the end of October 2009, when there

[3] The indicator is calculated and published by the SORS as part of its Consumer Opinion Survey.

was a reversal. This was not merely the result of a base effect, as there was also a reversal in the annual increase in the stock of household loans.

Figure 3.2: Growth in household loans in percentages and EUR million

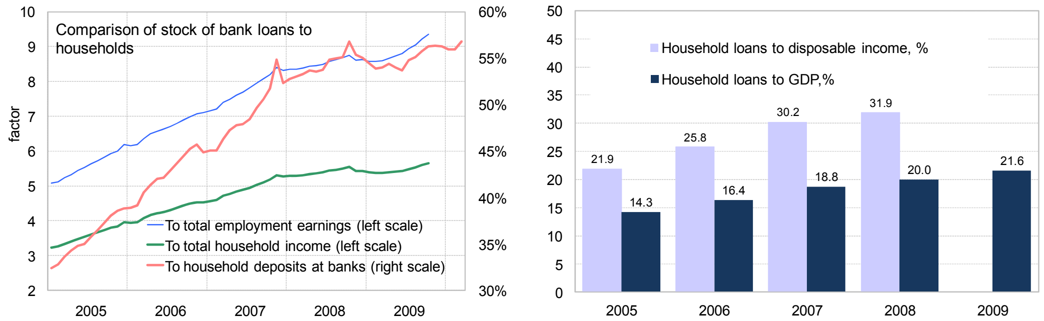


Source: Bank of Slovenia

A deterioration in indicators of household indebtedness.

Despite the slowdown in household borrowing, indicators of household indebtedness continued to deteriorate. This is particularly evident in the ratios of household loans to total employment earnings and to GDP. A factor in the deterioration in the indicators was the slowdown in total employment earnings, which was more pronounced than the slowdown in total household income (including social security benefits). The ratio of household loans to monthly employment earnings increased from 8.6 to 9.3 in 2009. During a period of slowing growth in earnings and rising unemployment, low-income households and households with higher debt levels whose active members are employed in the private sector will be more exposed to an increase in risk. The macroeconomic indicator of household indebtedness increased by 1.6 percentage points to 21.6%, primarily as a result of negative GDP growth.

Figure 3.3: Indicators of household indebtedness at banks



Source: Bank of Slovenia

Bank surveys reveal a slight increase in the household debt servicing burden.

The average household debt servicing burden for bank loans is estimated on the basis of data from bank surveys and statistics. The ratio of loan repayments to household employment earnings rose by 0.6 percentage points in 2009 to 22.2%.[4] Household loan repayments actually declined in 2009 in absolute terms, as a result of the slowdown in lending growth, the lengthening of the average maturities of household loans and, in particular, the fall in interest rates. The ratio of paid interest to employment earnings fell by 0.7 percentage points to 3.6%. Despite the negligible increase in the household debt servicing burden, households' arrears in repaying loans increased. According to the survey data, the proportion of household loan repayments more than 30 days in arrears rose by 1.2 percentage points in 2009 to 5.1%, while the proportion more than 90 days in arrears rose by 0.7 percentage points to 2.8%.

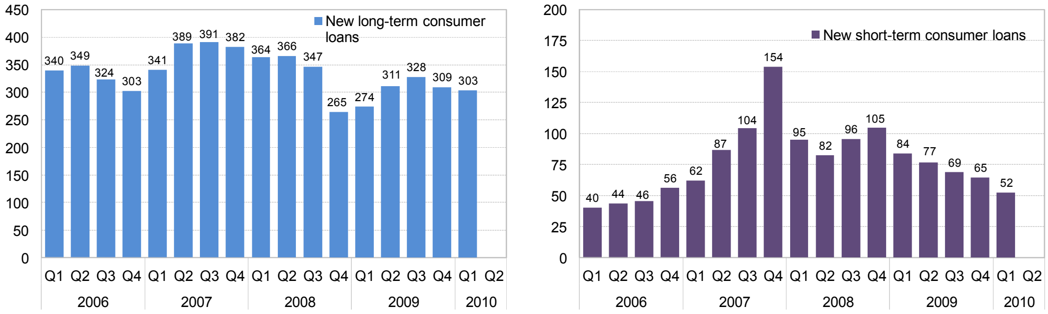
Lengthening of maturities of housing and consumer loans approved in 2009.

The volume of newly approved household loans in 2009 was down on 2008, but the average maturity increased. Analysis of quarterly figures reveals that the volume of newly approved housing loans and long-term consumer loans increased each quarter, but that of short-term consumer loans declined. The average maturity of housing loans had lengthened by 1.1 years by the end of 2009, primarily as a result of an increase in the proportion accounted for by loans with an original maturity of more than 15 years. The average maturity of consumer loans had lengthened by 0.7 years by the end of 2009,

[4] The figure used for employment earnings in 2009 was the sum of monthly household earnings between November 2008 and October 2009.

primarily as a result of an increase in the proportion accounted for by new consumer loans with an original maturity of more than 10 years.

Figure 3.4: Volume of newly approved long-term (left) and short-term (right) consumer loans in EUR million



Source: Bank of Slovenia

Table 3.2: Maturity breakdown of new housing loans in percentages

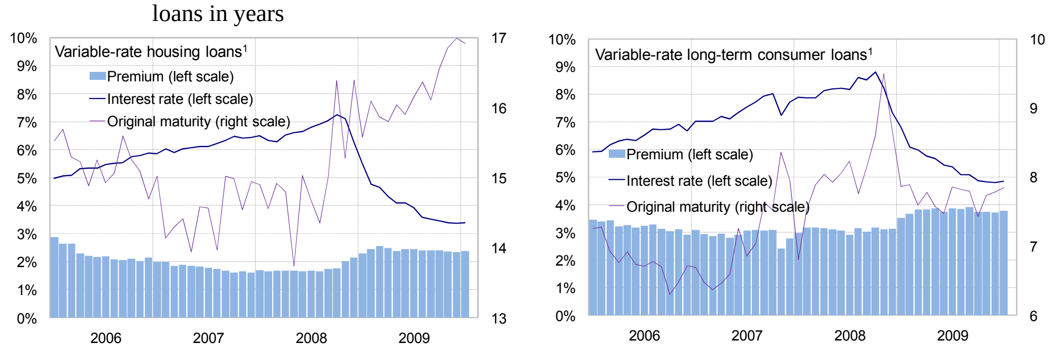
(%)	Up to 5 years	5 to 10 years	10 to 15 years	15 to 20 years	More than 20 years
2005	3.2	18.6	46.7	20.8	10.6
2006	2.2	13.0	35.0	24.2	25.6
2007	3.1	14.4	22.0	21.6	38.9
2008	3.9	13.6	19.0	20.0	43.6
2009	2.7	12.5	17.9	22.8	44.0

Note: The figures up to 2005 relate to loans by the eight largest banks, while the figures from 2006 cover all banks.
Source: Bank of Slovenia

A sharp fall in interest rates on new household loans.

The interest rates on new household loans fell in 2009, most notably on loans with a variable interest rate. The average interest rate on variable-rate housing loans had fallen by 2.9 percentage points by the end of January 2010, while that on variable-rate consumer loans had fallen by 2.5 percentage points. The fall in variable interest rates on household loans was slightly less than the fall in the reference interest rates, as the banks raised their premiums over the reference interest rates. These were significantly higher in 2009 than in 2008. In a period of rising reference interest rates this will be reflected in a higher debt servicing burden on household income, and a consequent greater likelihood of default.

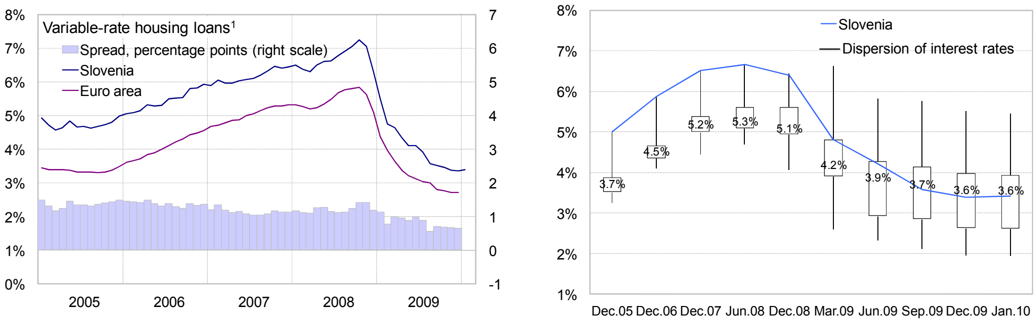
Figure 3.5: Premiums over the EURIBOR and average maturity on newly approved loans in years



Note: [1] Includes loans on which the agreed interest rate is variable or fixed for up to one year; the EURIBOR is the reference interest rate.
Source: Bank of Slovenia

In 2009 Slovenian interest rates on housing loans fell faster than the euro area average, which was reflected in a narrowing of the spread to 0.65 percentage points. In the euro area the dispersion of interest rates between countries widened, as a result of the variation in the tightening of credit standards at banks from different euro area countries.

Figure 3.6: Comparison of Slovenian interest rates with the euro area average, and dispersion in interest rates between countries for housing loans

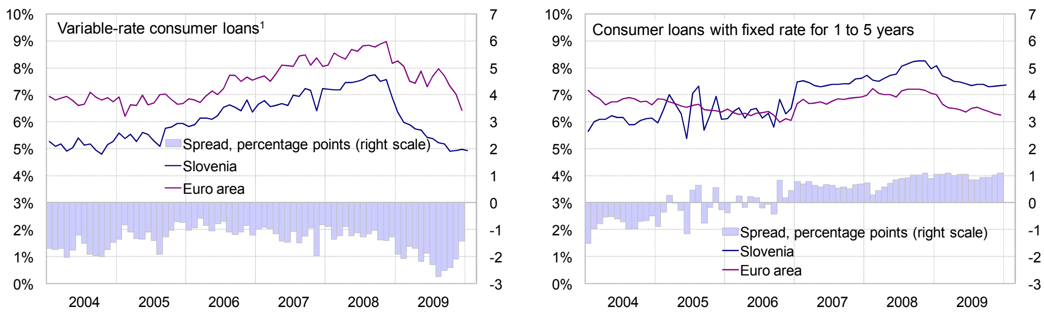


Note: [1] Includes loans in which the agreed interest rate is variable or fixed for up to one year. The columns in the right graph represent the dispersion of interest rates by quartile. The thick part of the column represents the second and third quartiles.
Sources: Bank of Slovenia, ECB

Interest rates on variable-rate consumer loans remain higher than the euro area average, while those on fixed-rate loans were lower.

Slovenian interest rates on variable-rate consumer loans were again well below the euro area average in 2009. They began to fall more quickly than average euro area interest rates, and by December were 1.4 percentage points below the euro area average. On consumer loans with the interest rate fixed for a period of 1 to 5 years, the spread was positive, at its level from the end of 2008.

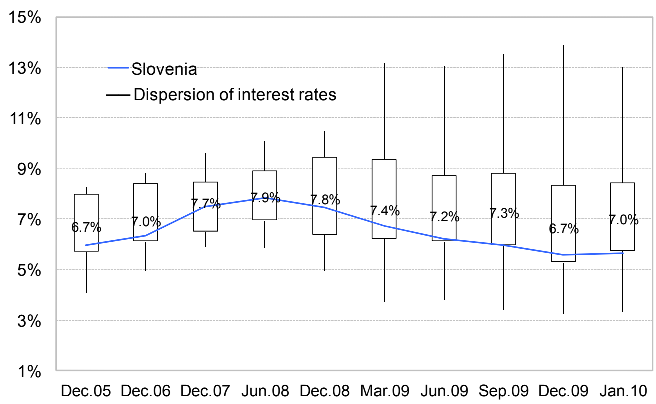
Figure 3.7: Comparison of interest rates on consumer loans in Slovenia with those in the euro area, by type of remuneration in percentages



Note: [1] Includes loans in which the agreed interest rate is variable or fixed for up to one year.
Sources: Bank of Slovenia, ECB

The dispersion between countries of interest rates on consumer loans widened even more than those on housing loans in 2009.

Figure 3.8: Dispersion of interest rates on consumer loans in the euro area in percentages



Note: The columns in the graph represent the dispersion of interest rates by quartile. The thick part of the column represents the second and third quartiles.
Source: ECB

In 2009 variable-rate loans were more attractive than fixed-rate loans, because of the low reference interest rates. The proportions of loans remunerated with a variable interest rate increased to 96% among housing loans, 62% among consumer loans, and 75% among all household loans. As a result the proportion of the stock of household loans accounted for by variable-rate loans increased to 77%. In the short term, during a period of low reference interest rates, the repayment of this type of loan entails a lower burden on the borrowers' income. In the long term households are exposed to significant uncertainty regarding the movement of reference interest rates, and thereby to interest-rate risk.

The proportion of new household loans with a variable interest rate increased in 2009.

Figure 3.9: Breakdown of household loans by type of interest rate in percentages

Source: Bank of Slovenia

3.2 Forms of household financial assets

Households' financial assets increased by 8% in 2009. Renewed growth in prices on the majority of world stock exchanges after March 2009 accounted for 31% of the increase of EUR 2.9 billion in the value of households' financial investments.

Household financial assets increased by 8% in 2009.

In 2009 households channelled their current financial investments into more conservative forms, particularly deposits, and life insurance and pension insurance tied to long-term contracts concluded in the past. They favoured investments in shares and mutual funds less frequently, despite the high growth in share prices after February 2009. This was the result of past bad experiences on the capital markets, and uncertainty surrounding the future economic position. The stock of assets in shares and mutual funds increased primarily as a result of positive value changes in the amount of EUR 0.8 billion.

Table 3.3: Stock of household financial investments by instrument

	2005	2006	2007	2008	2009
	(EUR million)				
Total	28,272	31,979	37,404	36,881	39,817
growth, %	8.8	13.1	17.0	-1.4	8.0
as % GDP	98.5	103.1	108.5	99.3	114.1
	Breakdown, %				
Monetary gold	0.0	0.0	0.0	0.0	0.0
Currency and deposits	50.4	48.5	45.9	53.0	52.3
bank deposits	40.2	37.9	35.5	39.4	37.6
Securities other than shares	1.8	1.6	1.3	1.3	1.3
Loans	3.1	2.6	2.3	2.5	2.4
Shares and other equity	24.4	25.4	27.5	23.1	22.8
Investment fund shares/units	6.5	7.7	9.2	5.1	5.9
Life insurance	4.0	4.5	4.5	4.7	5.2
Pension insurance	1.8	2.0	2.2	2.5	2.7
Other technical reserves	2.2	2.0	1.7	1.9	1.9
Other claims	5.7	5.6	5.3	5.8	5.5

Source: Bank of Slovenia

Having increased in 2008, the proportion of total household investments accounted for by bank deposits declined slightly in 2009, but was nevertheless higher than the figure from 2007. The main factors in this were value changes in investments in shares and mutual funds, and relatively high current investments in life insurance and pension insurance, which do not yet account for a significant proportion of household financial assets.

Table 3.4: Stock of net household investments at banks in EUR million

	2005	2006	2007	2008	2009
			(EUR million)		
Liabilities	4,480	5,558	6,965	7,938	8,514
growth, %	23.8	24.1	25.3	14.0	7.3
Investments	10,798	11,611	12,931	13,924	14,567
growth,%	6.0	7.5	11.4	7.7	4.6
Net investments	6,318	6,053	5,967	5,986	6,054
as % GDP	22.0	19.5	17.3	16.1	17.2

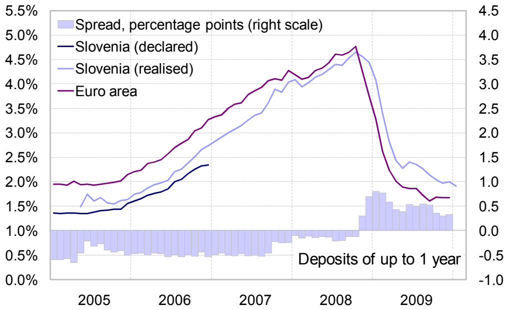
Source: Bank of Slovenia

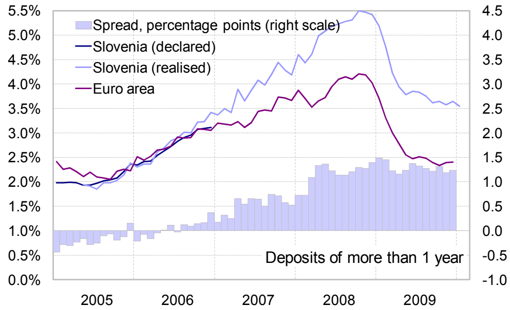
Interest rates on household deposits at banks

A fall in interest rates on household deposits.

Interest rates on household deposits at Slovenian banks fell significantly in 2009. Interest rates on new deposits with an original maturity of up to 1 year fell by 2.5 percentage points to 2%, halving the spread by which they exceeded the euro area average. Banks cut interest rates on long-term deposits by 1.8 percentage points to 3.6%, although the spread with the euro area average remained high.

Figure 3.10: Comparison of Slovenian interest rates on new household deposits of up to 1 year (left) and more than 1 year (right)



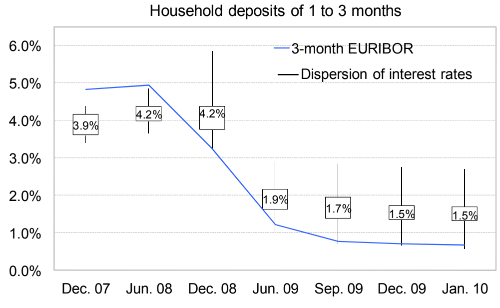


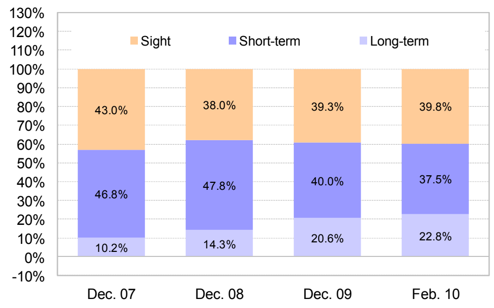
Source: Bank of Slovenia

Lengthening of the average maturity of household deposits.

The average maturity of household deposits continues to lengthen. The proportion of long-term deposits increased by just over 6 percentage points to 20.6%. This was the result of an increase in the spread between interest rates on long-term and short-term deposits, and a reduced appetite for risk when investing. The increase in deposits has not tracked the favourable changes in average maturity, having declined since February 2009, as a result of the slowdown in household income and the fall in deposit rates.

Figure 3.11: Dispersion of Slovenian interest rates on household deposits (left) and maturity breakdown of deposits (right) in percentages



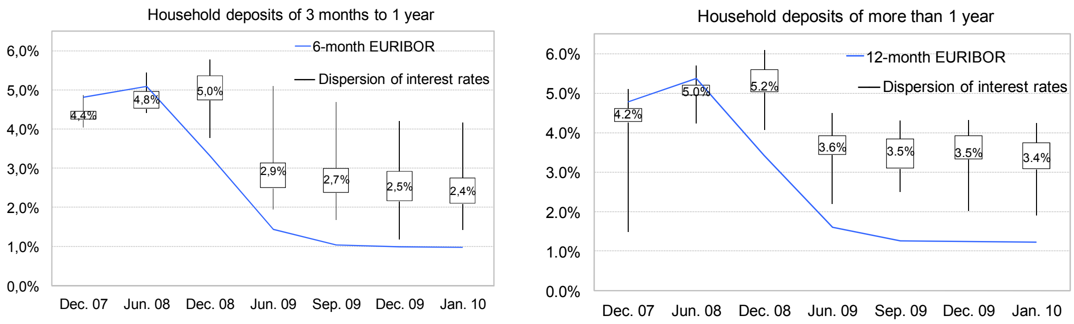


Note: The columns in the left graph represent the dispersion of interest rates by quartile. The thick part of the column represents the second and third quartiles.
Source: Bank of Slovenia

The dispersion of interest rates on household deposits between banks in Slovenia widened.

The dispersion of interest rates between banks in Slovenia widened in the second half of 2008, and remained highest in the segment of deposits with an original maturity of 3 months to 1 year, where competition between the banks to attract household deposits is greatest. Interest rates on deposits with an original maturity of more than 3 months are still sharply in excess of the EURIBOR, having stood at below the reference interest rate before the worsening of the financial turmoil.

Figure 3.12: Dispersion of Slovenian interest rates on household deposits in percentages

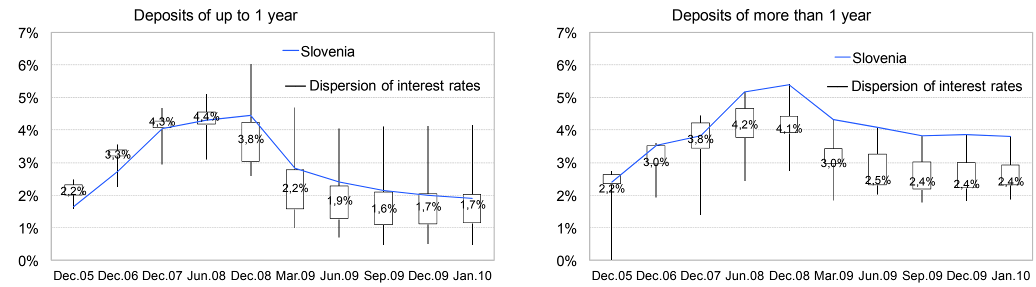


Note: The columns in the graph represent the dispersion of interest rates by quartile. The thick part of the column represents the second and third quartiles.
Source: Bank of Slovenia

The dispersion of interest rates on household deposits also increased between euro area countries.

As it did between banks in Slovenia, the dispersion of interest rates on household deposits also increased between individual euro area countries in the final quarter of 2008, particularly on short-term deposits. Slovenian interest rates on short-term deposits ranged in the third quartile in 2009 (deposit rates were higher in a quarter of euro area countries). On long-term deposits Slovenian banks offer some of the highest interest rates in the euro area, an indication of the fierce competition between Slovenian banks to attract long-term deposits since the worsening of the financial turmoil in 2008.

Figure 3.13: Dispersion of euro area interest rates on household deposits in percentages



Note: The columns in the graph represent the dispersion of interest rates by quartile. The thick part of the column represents the second and third quartiles.
Source: Bank of Slovenia

3.3 Real estate market

Prices of residential real estate in Slovenia peaked at the end of the first half of 2008, when the number of transactions had fallen for the third consecutive quarter. This was followed by a gradual fall in prices until the end of last year. Prices are also expected to fluctuate this year, as despite individual opportunities the decision to purchase housing is uncertain given the impact of the deterioration in the economy on household consumption, expectations of larger falls in housing prices and the anticipated rise in the key interest rate at the end of the year.

The accessibility of financial resources for major construction investors will have a significant impact on the future movement of real estate prices. Financial resources will enable them to settle their due liabilities to subcontractors. Financial institutions are renewing loans to construction companies, who are targeting an appropriate profit in sale, but they are also lending to the final purchasers. This generates a cash flow that ensures that liabilities are settled on the investor side, while a new claim arises on the part of the financial institution against the purchaser of the housing, which is generally less risky.

Given the large inventories of completed and unfinished dwellings on the balance sheets of construction companies, their solvency difficulties and low demand, no major housing projects can be expected to be planned. Many projects as realised were impractically conceived in the past as a result of a desire to catch up with surplus demand, and it is very difficult to sell the surplus supply on the market in the present situation. Volume on the real estate market has more than halved. The coming quarters will reveal the level of real demand. In the absence of expectations of major short-term rises in prices, and given the demographics, this is certain to be lower than in the last few years, when speculative demand was also encouraged. The real estate market will become even more segmented. Unsold housing also presents an opportunity to create housing funds, given an appropriate change in legislation, to help regulate the rental market in Slovenia. Difficulties that remain on the Slovenian real estate market are that construction companies are also investors, while abroad investors in residential and commercial real estate are generally investment companies and financial institutions. In this way construction companies in Slovenia take up the risk of incorrect investment decisions that would otherwise be taken up by investors.

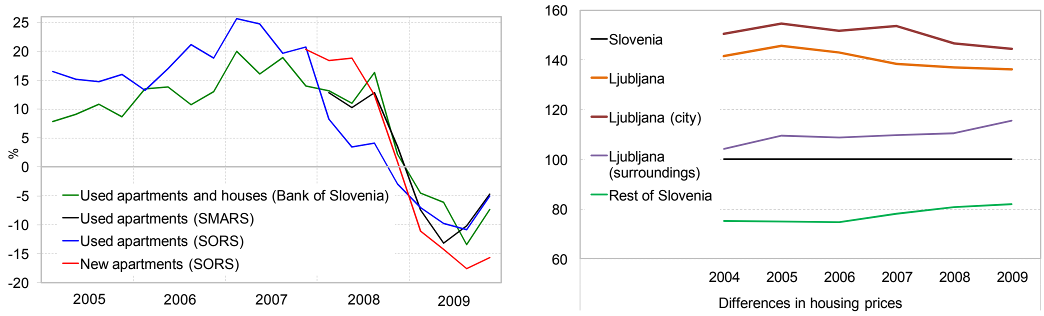
Published growth in real estate prices in Slovenia

The fall in real estate prices in Slovenia in 2009 ranged from 4.7% to 7.3% according to price indices. with various methodologies.

According to Surveying and Mapping Authority (SMARS) figures, housing prices at the end of 2009 were down 4.7% on the beginning of the year, and down 11% on their peak in the second quarter of 2008. The fall in housing prices in Ljubljana was slightly larger, at 6.6% in 2009, which left them down 12.6% on the aforementioned peak.

The same trend in housing prices was seen in figures published by the SORS. Using a hedonic index it recorded price falls in 2009 of 5% nationally, and 8.2% in Ljubljana. Its statistical research illustrated the movement in prices of new housing, which fell by 15.7% last year, and were down 17.4% on their peak in the third quarter of 2008.

Figure 3.14: Year-on-year growth in prices of used and new residential real estate (left) and regional differences in transaction prices of housing (right) in percentages



Note: The regional differences in price levels are calculated from the weighted average of transaction prices in each year.
Sources: Bank of Slovenia, TARS, SMARS, SORS

Transaction prices of housing and growth calculated from the Fischer index

The fall in the transaction prices of flats and houses in 2009 amounted to 7.3% according to Bank of Slovenia calculations on the basis of the Fischer index. The largest fall in prices was in the Ljubljana urban region, prices in the past having been more than 50% higher than the average for Slovenia as a whole. During the reversal in the business cycle on the real estate market the prices of both small and large flats fell.

Table 3.5: Year-on-year growth in transaction prices of flats and houses calculated using the Fischer index in percentages

(v %)	Ljubljana urban region	Ljubljana city	Ljubljana surroundings	Rest of Slovenia	Euro area[1]
2005	8.8	10.6	4.5	11.1	7.3
2006	13.5	14.0	12.2	14.3	6.5
2007	15.6	17.4	12.5	26.5	4.4
2008	4.3	2.8	7.4	5.1	1.8
2009	-12.4	-11.6	-14.0	-6.9	-2.5

Note: [1] The 2009 figure is the annual growth in Q2 2009.
Sources: Bank of Slovenia, TARS, ECB, SMARS, own calculations

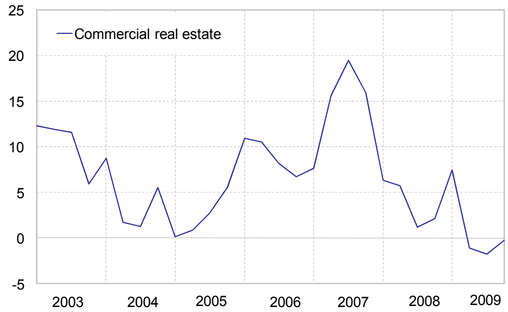
Advertised prices of housing

The average advertised prices of housing in Ljubljana fell in 2009. The smallest falls were in prices of three- and four-room flats, which were down 2.6% and 3% on average respectively. Prices of smaller flats fell by just over 4%. The differences between the advertised prices of flats in Ljubljana and its surroundings widened on average, particularly for larger flats.

Prices of commercial real estate remained almost unchanged in 2009.

After falling by 1.7% in the third quarter of 2009, prices of commercial real estate rose again and ended the year almost unchanged, down just 0.2%. However, given the availability of commercial premises, the sharp decline in economic activity last year and corporate efforts to cut costs, there can be no expectation of higher growth in prices of commercial real estate.

Figure 3.15: Year-on-year growth in advertised prices of housing (left) and commercial real estate[5] (right) in Ljubljana in percentages

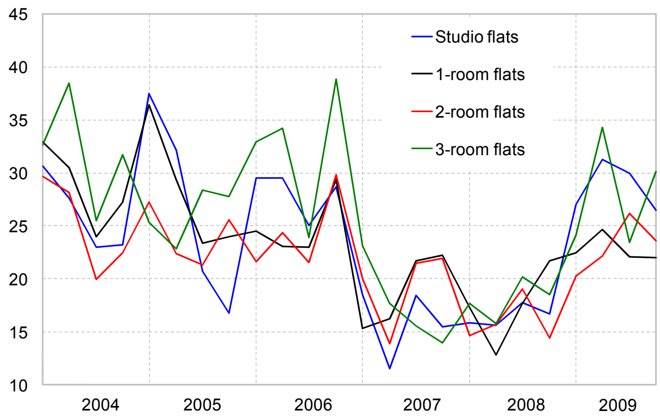


Sources: SLONEP, own calculations

The gap between advertised prices and transaction prices widened again.

The gap by which advertised prices exceeded transaction prices widened again. This was the result of the situation on the market, which allowed purchasers to obtain larger discounts. In addition, advertised prices are delayed in tracking the fall in transaction prices.

Figure 3.16: Gaps by which advertised prices exceed realised prices per square metre in Ljubljana in percentages



Sources: TARS, SMARS, SLONEP

Housing affordability in Ljubljana

Housing affordability improved according to certain indicators, but actual prices are nevertheless higher than fundamental housing prices.

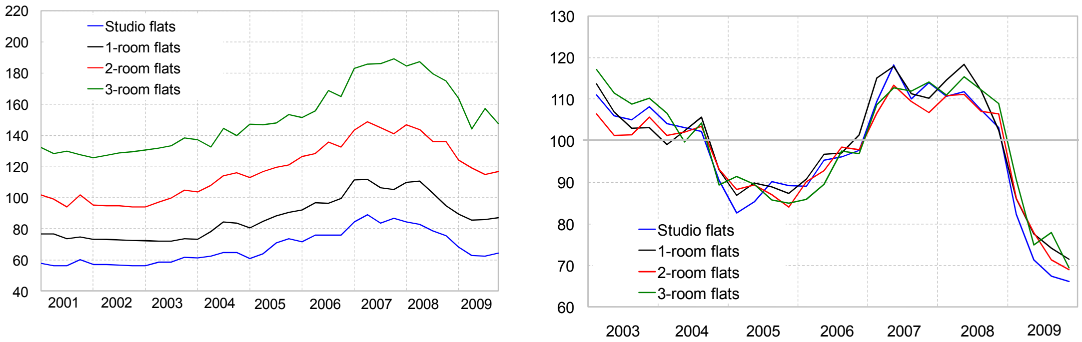
Housing affordability, which is expressed as the ratio of the price of housing to the annual moving average of net monthly wages in Ljubljana, increased slightly in 2009 as a result of falls in real estate prices. The rise of 3.8% in the average net wage in Ljubljana in terms of the annual moving average was a factor. The cost of studio flats and one-room flats in Ljubljana was down the equivalent of 7.4 and 11.5 average monthly wages respectively on the final quarter of 2008. The saving for two-room flats was 20 average monthly wages. Actual prices nevertheless remain higher than the fundamental housing prices[6] that should be sustainable in the long term.

Given the rise in the minimum cost of living and the planned rise in the minimum wage, the housing affordability index is expected to improve further in the future, although this would not necessarily entail any improvement in actual affordability. Evidence of the

[5] Prices for office space in Ljubljana were used to calculate the growth rates.
[6] Fundamental prices: see Note 9.

limitations of the index is that growth in the average net wage is not necessarily equal to growth in the income of housing purchasers, who when addressing their housing issues are usually concentrated in younger age groups. The size of the household also has an impact on affordability. The indicator also fails to take account of rising unemployment, which has an adverse impact on housing affordability.

Figure 3.17: Ratio of housing prices to annual moving average of net monthly wages in Ljubljana[7] (left) and housing affordability index[8] (2004 = 100) (right)



Sources: Bank of Slovenia, SLONEP, SORS, own calculations

The average maturity of housing loans lengthened, while variable interest rates fell.

Relatively low interest rates also mean that housing affordability is improving, as it still takes account of lending terms. Interest rates on variable-rate housing loans fell by 2.9 percentage points in 2009. In addition to the aforementioned factors, the ratio of the housing loan repayment annuity to net wages also declined as a result of the lengthening of maturities of new loans, which lengthened by just over 13 months in 2009. The ratios of housing loan annuities to net wages at the end of 2009 stood at 42% for studio flats, 57% for one-room flats, 76% for two-room flats and 102% for three-room flats.

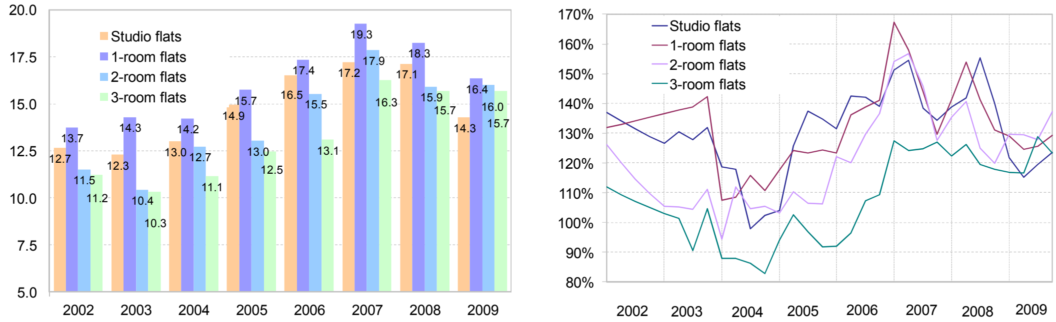
The P/E ratio for real estate improved.

Rents for smaller flats fell by less on average in 2009 than housing prices, while the fall in rents for larger flats was more pronounced. This was reflected in a decline in the P/E ratio for studio flats and one-room flats, an indication of a decline in the overvaluation of smaller housing units. The ratio effectively remained unchanged for larger flats. From an investment point of view, buy-to-let purchasers receive an annual return of 6.1% to 7% on their investment.

7 Advertised prices minus 10% until 2004, transaction prices since 2004. In the calculation of the ratio of housing prices to the average monthly net wage, differences between advertised prices and transaction prices may vary from quarter to quarter, as a result of which the calculated affordability may differ from the actual affordability.

8 It is assumed in the calculation that the full value of the real estate is financed via a housing loan from a bank. In the calculation of the index, the quarterly annuity for a loan in the amount of the housing value is first computed on the basis of the interest rates and the weighted average maturity of new housing loans in a particular quarter. The next step is to calculate the ratio of the quarterly annuity to the 12-month moving average of net quarterly wages in Ljubljana, from which the base index is then calculated. A rise in the index reflects a decline in housing affordability.

Figure 3.18: Ratio of housing prices to rents (P/E) (left), and ratio of actual prices to fundamental prices of housing in Ljubljana calculated on this basis[9] (right)

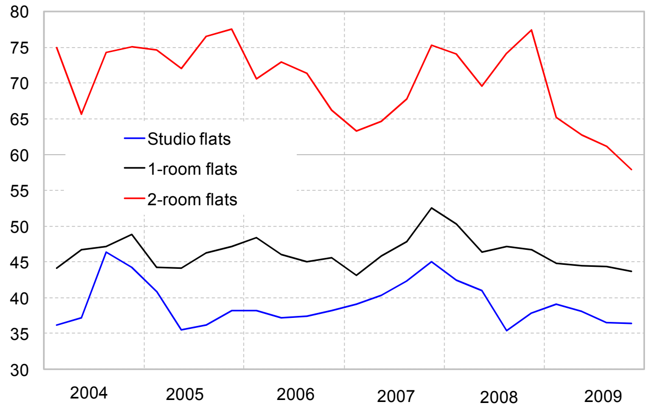


Sources: SLONEP, TARS, SMARS, own calculations

Last year actual prices remained significantly above fundamental prices for all housing. With housing prices falling by more than rents, the aforementioned ratio declined most for smaller flats. At the end of 2009 actual prices of studio flats, one-room flats and three-room flats exceeded fundamental prices by 23% to 29%, while the overvaluation of two-room flats had increased to 37%.

Rents excluding current housing expenses in Ljubljana in 2008 averaged 39% of the average net wage for studio flats, 48% for one-room flats and 74% for two-room flats. The figures fell slightly last year, to 37% for studio flats, 44% for one-room flats and 62% for two-room flats.

Figure 3.19: Percentage ratio of housing rents excluding current expenses to average net monthly wage in Ljubljana



Note: Given the lack of available data for actual agreed rents, average advertised rents for Ljubljana are used in the calculation. The average net monthly wage is calculated from the annual moving averages of net monthly wages for Ljubljana.

Sources: SLONEP, TARS, SMARS, SORS, own calculations

Supply and demand factors in real estate prices

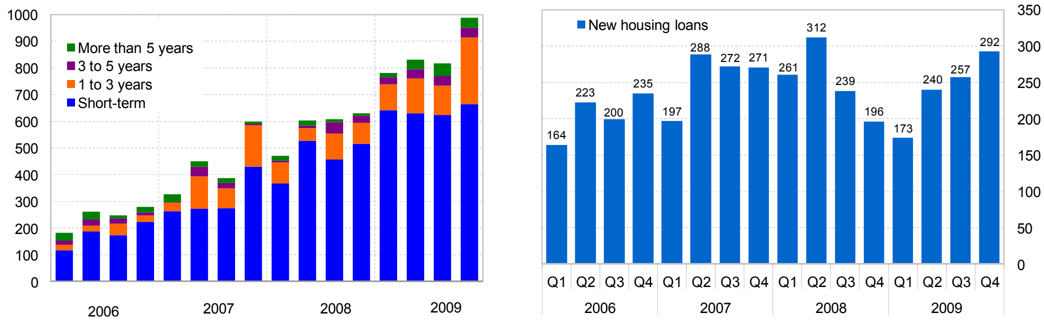
Purchasers' expectations surrounding price movements will be a factor in demand for housing in the months ahead.

Housing prices will remain subject to downward pressure from purchasers in the coming months. The main reasons are to be found in the psychological expectation of a significant further fall in housing prices and deferrals of purchases, and in the weaker economic position of households as a result of the economic crisis. Household consumption of durables fell by 8.3% last year, further evidence of considerable circumspection in making purchase decisions. However, arrears in loan repayments by investors to banks and in the settlement of liabilities to subcontractors are increasing. Because bankruptcy proceedings for construction companies and the repossession of real estate by banks is a lengthy

[9] The calculation of fundamental housing prices on the basis of the ratio of housing prices to housing rents (P/E) takes into consideration the average P/E value between 1995 and 2003. A more accurate calculation of the fundamental price would require the calculation of the average P/E ratio over a longer, more stable period of at least 10 or 15 years. The short time in which the Slovenian housing market has functioned normally makes this impossible. These limitations must be borne in mind during interpretation, although over a longer timeframe a lower average P/E ratio would be anticipated, and housing would appear to be even more overpriced according to this indicator.

process subject to delays, the prompt adjustment of housing prices to actual demand would have a beneficial impact on liquidity in the construction sector. The project of the mass valuation of real estate and way in which the real estate tax is introduced will also have an impact on price formation.

Figure 3.20: Newly approved loans to the construction sector (left) and newly approved housing loans to households (right) in EUR million

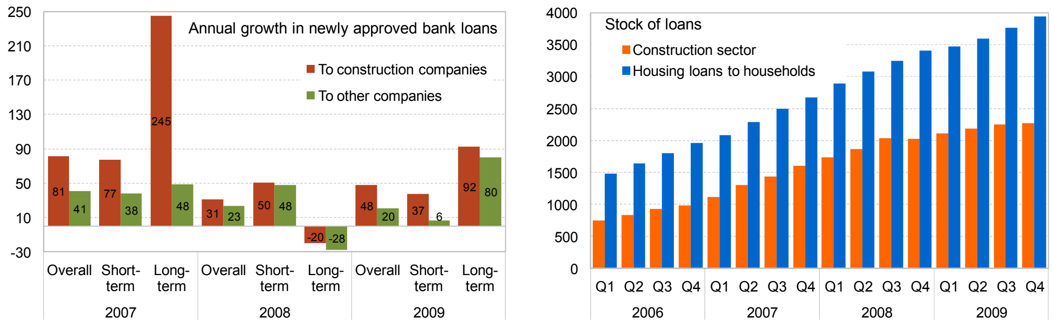


Source: Bank of Slovenia

Growth in newly approved loans to the construction sector stood at 48% in 2009.

New loans approved to the construction sector in 2009 were up 48% on 2008. Given the slow pace of real estate sales and the cancellation or deferral of many infrastructure projects, it is predicted that a large proportion of the newly approved loans are renewals. The increased turnover of short-term loans is a reflection of the increased importance of bank loans in ensuring liquidity for construction companies. The average weighted maturity of all new loans to the construction sector has fallen from 21 months to 14 months over the last three years. The proportion of the total accounted for by long-term loans was again up on the previous year, by 6 percentage points to 25%. Growth in construction loans stood at 11.7% in 2009, down 15 percentage points on the previous year.

Figure 3.21: Growth in newly approved bank loans to construction companies and other companies in percentages (left) and stock of loan to the construction sector and stock of housing loans to households in EUR million (right)



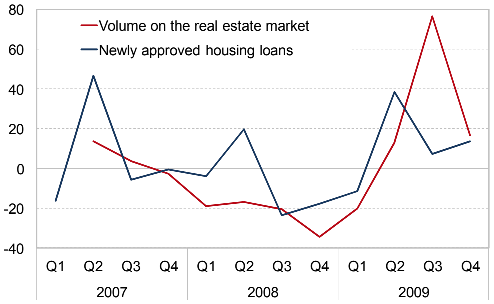
Source: Bank of Slovenia

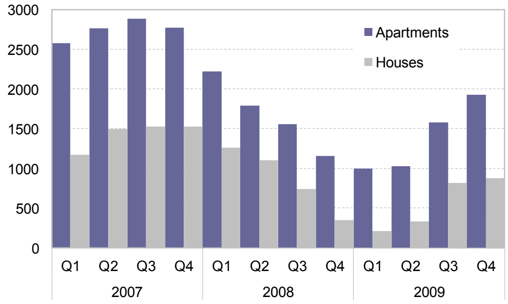
Newly approved housing loans were down 4.4% last year, negligible compared with the decline of 24% in recorded transactions.

Recorded transactions in flats and houses on the real estate market fell by 39% in 2008, and by a further 24% in 2009. There was a gradual decline in newly approved housing loans in the final quarter in 2008, and in the first quarter of 2009 in particular, but newly approved loans in the remaining quarters were higher than the average over the last four years. The annual volume of newly approved housing loans in 2009 was up 17% on 2006, when there were incomparably more transactions on the real estate market.

Leasing business in 2009 was down 59% in terms of the value financed. The decline was especially large for retail facilities (down 79.6%) and commercial buildings (down 49%).

Figure 3.22: Quarterly growth in volume on the real estate market and newly approved housing loans in percentages (left) and number of recorded transactions in flats and houses (right)





Sources: Bank of Slovenia, SMARS, own calculations

Discrepancies between lending activity and transactions on the real estate market are possible, given the incomplete capture of recorded transactions. An extremely small number of new build sales are included, as investors are not legally obliged to report the sale. At the same time households are also opting to modify existing housing. The stock of housing loans increased to EUR 3.9 billion or 11.3% of GDP in 2009.

Table 3.6: Breakdown of non-residents' purchases of real estate by tax office

	Breakdown, %								No. of purchases by NRs	Proportion of total (%)
	Celje	Koper	Kranj	Ljubljana	Maribor	Murska Sobota	Nova Gorica	Other		
Jul–Dec 2004	6.5	26.0	11.1	5.9	7.7	21.4	10.8	10.6	443	-
2005	4.0	16.4	18.5	6.1	6.7	18.4	14.3	15.6	642	3.9
2006	5.5	20.7	12.8	4.7	4.2	16.9	20.3	14.9	740	4.2
2007	7.0	22.5	11.5	4.2	4.9	19.5	16.6	13.8	730	4.4
2008	7.0	25.8	7.2	8.5	4.7	19.7	15.7	11.4	472	4.6
2009	3.5	36.7	8.4	5.2	6.3	15.7	12.9	11.2	286	3.7

Sources: TARS, SMARS, own calculations

Neither was there any contribution to higher volume on the real estate market last year from demand for housing from non-residents, which like domestic demand was down significantly, at just under half of its average over the last five years. Non-residents accounted for 3.7% of all purchases.

Capital losses for the investment of money in housing in Ljubljana last year.

Other factors in the reduced demand for housing were the capital losses realised from speculative purchases of real estate. Speculative real estate purchases were relatively less attractive in 2009 than in the past. In contrast to previous years, residential real estate is no longer a predictably high-yielding investment, given the uncertainty of future developments. A gradual recovery on the capital markets encouraged price rises, which offered the highest return among financial investments. Here consideration should also be given to the volatility of the capital markets, which entails higher risk. The government guarantee meant that deposits were the most attractive and safest form of saving, despite the lower return. At the end of the third quarter of 2009 they accounted for 37% on household financial assets.

Table 3.7: Return on investments in housing in Ljubljana allowing for loan repayment, and comparison of return on investments in housing with other forms of financial investment in percentages

	Purchase of housing	Investment of own funds			
		Housing	Shares	Mutual funds	Deposit rate[1]
(%)	with loan		SBI 20	MF AUP	
2006	6.8	14.1	30.3	15.1	2.7
2007	6.0	13.9	62.5	22.4	3.4
2008	-3.0	5.4	-67.5	-42.8	4.3
2009	-15.7	-9.5	8.3	19.2	3.3
	Average annual return				
2006–2009	-1.5	6.0	8.4	3.5	3.4

Note: Return is calculated post tax. Capital gains (on real estate, securities, investment coupons) are subject to a final tax. A 20% tax applies after the first year of disposal. Rental income is included in the annual taxable base for personal income tax. In the calculation it is subject to the middle personal income tax rate of 27% (a 33% rate has been applied to the figures for 2006 under the ZDoh-1 then valid). The amount of money invested in shares, investment coupons and bank deposits is equal to the money invested in purchasing housing. The return is calculated on the basis of capital market indices and the average annual interest rates on time deposits of more than 1 year.
[1]Average annual interest rate for deposits of more than 1 year.

Sources: Bank of Slovenia, SMARS, SORS, LJSE, SMA, own calculations

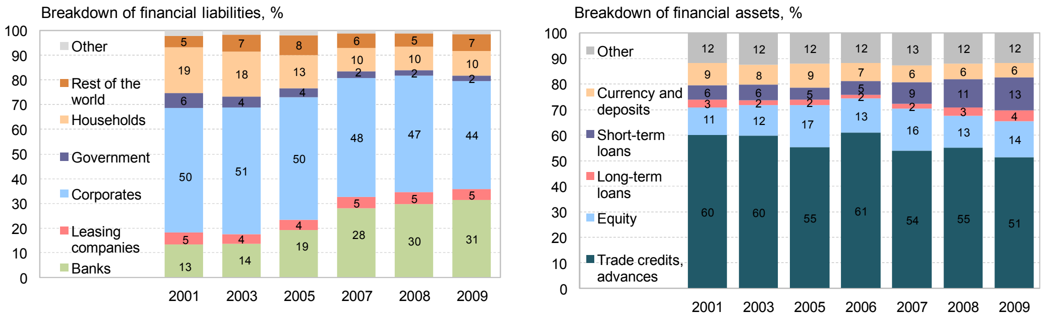
The available data suggests that there is negligible migration of household financial assets between various investments, primarily as a result of the passive asset management seen in recent years.

Table 3.8: Changes in households' time deposits and alternative financial investments, volume of transactions on the real estate market, and changes in the stock of housing loans

	2005	2006	2007	2008	2009
	(EUR million)				
Change in stock of household time deposits excluding sight deposits	-424	163	1,177	1,301	177
Change in stock of household financial assets	2,151	3,685	5,369	-531	2,927
Volume of trading in shares on capital market	941	1,451	3,035	953	720
Volume of trading on real estate market	1,348	1,559	1,900	1,818	1,105
Change in stock of housing loans	439	504	712	727	532
	Growth, %				
Household time deposits excluding sight deposits	-7.1	2.9	20.6	18.9	2.2
Household financial assets	8.4	13.2	17.0	-1.4	8.1
Volume of trading in shares on capital market	1.0	54.3	109.1	-68.6	-24.4
Volume of trading on real estate market	25.4	15.7	21.9	-4.4	-39.2

Sources: Bank of Slovenia, TARS, LJSE, own calculations

Figure 3.23: Breakdown of financial liabilities (left) and assets (right) of construction companies



Sources: Bank of Slovenia, own calculations

The financial accounts figures reveal construction companies' high dependence on bank resources in the last three years. The proportion of total liabilities accounted for by liabilities to banks in 2009 was up 12 percentage points on 2005, primarily at the expense of a decline in liabilities to corporates and households. The proportion accounted for by loans increased to stand at 44% at the end of 2009, while the proportion of construction companies' financing accounted for by equity fell to 19%.

Table 3.9: Completed dwellings, building permits issued and gross investment in housebuilding

	2002	2003	2004	2005	2006	2007	2008	2009
	Estimate of housing stock							
Number of dwellings[1]	730,064	736,420	743,133	750,355	757,522	765,552	775,199	
Number of dwellings per 1,000 inhabitants	366	369	372	375	377	378	381	
	New build, including extensions and change of purpose							
Number of new dwellings	7,265	6,567	7,004	7,516	7,538	8,357	9,971	
Number of new dwellings per 1,000 inhabitants	3.6	3.3	3.5	3.8	3.7	4.1	4.9	
Floor area (m2)	824,608	746,517	761,430	807,607	860,537	928,941	1,100,436	
	Building permits issued							
Number of dwellings	5,080	6,122	7,002	7,235	8,463	10,204	8,376	5,940
Floor area (m^2)	597,366	711,385	793,200	880,751	1,028,024	1,127,420	970,034	740,390
	Supply of the Housing Fund of the Republic of Slovenia (HFRS)							
Number of dwellings delivered	76	59	160	353	453	685	35	120
proportion of new dwellings, %	1.0	0.9	2.3	4.7	6.0	8.2	0.4	
	Gross investment in housebuilding							
Growth, %	5.9	-0.1	20.8	26.3	11.6	20.6	16.8	-17.5
As % GDP	3.1	2.9	3.2	3.8	3.9	4.3	4.6	4.1
	Growth, %							
Construction costs - new housing[2]	4.9	6.3	11.8	3.4	4.5	4.5	5.0	-1.7
material costs	3.8	4.7	14.6	1.1	5.2	3.2	4.5	-3.6
labour costs	7.5	10.9	5.1	9.1	2.4	8.0	5.9	2.7

Notes: [1] The housing stock includes occupied and temporarily unoccupied dwellings for permanent use.
[2] Costs of construction, finishing work, and fixtures on new housing, excluding land costs.

Sources: SORS, HFRS, own calculations

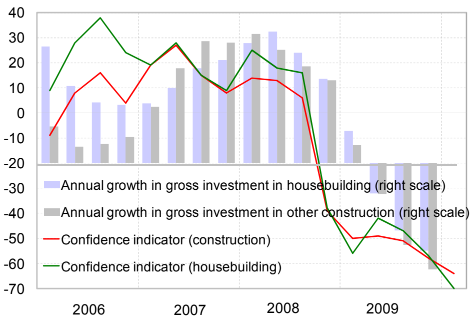
The decline in construction activity was reflected in the number of building permits issued, which in 2009 was down 23.4% on the previous year. Gross investment in housebuilding also declined as expected, by 17.5%.

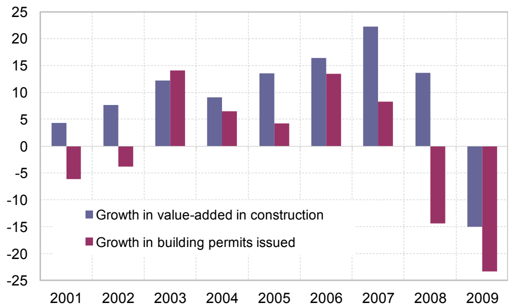
A decline in construction activity.

Despite a rise in labour costs in the construction sector, costs of work on new housing excluding land costs declined by 1.7%, as a result of falling material prices.

Projected developments in the construction sector

Figure 3.24: Business trends and annual growth in gross investment in construction (left) and annual growth in value-added in construction and building permits issued (right) in percentages





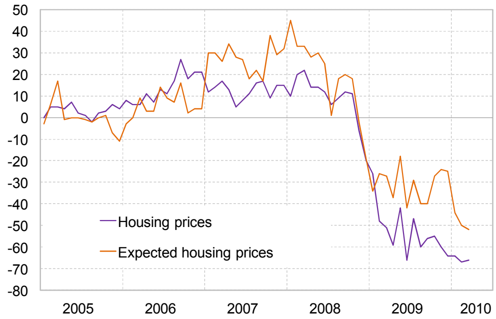
Sources: SORS, own calculations

The construction confidence indicator,[10] which is the average of the balances for current total orders and employment expectations, had reached a record low by the end of 2009, and declined further during the first quarter of 2010. Among the factors cited by construction companies as limiting their business, insufficient demand was cited by 62% and fierce competition in the sector by 56%. High labour costs are faced by 30% of the companies, while slightly fewer face high financial costs and difficulties in obtaining loans. Expected housing prices[11] are at their lowest level of the last eight years.

The price expectations indicator fell sharply in 2009, and deteriorated further in the first quarter of 2010.

[10] Source: SORS
[11] Price expectations are expressed by means of an indicator for the next three months.

Figure 3.25: Business situation of construction companies (left) and housing prices (right) from survey of business trends[12]



Note: In the determination of the business situation, companies answer in writing whether it is better than, the same as or worse than the previous month.

Source: SORS

According to SORS figures, the value of construction work performed in housebuilding in 2009 was down a half on 2008, while the value of new contracts concluded for housebuilding was down 73% over the same period.

[12] Original data.

4 CORPORATE SECTOR

Corporate performance in 2009 was marked by a decline in economic activity, as financial resources were severely limited and corporate liquidity positions deteriorated. All the major forms of corporate financing declined: both at banks and non-monetary financial institutions, and within the corporate sector. There was also a decline in financing in the rest of the world corresponding to the decline in foreign trade. After corporates successfully compensated for the loss of financing at the domestic banks in 2008 by means of financing in the rest of the world, with banks and with their commercial partners, these financial resources shrank in 2009. Financing at owners in the rest of the world, who used it to support their own companies in Slovenia, also dried up, and an additional burden on subsidiaries was debt repayment to the parent companies and disbursement via loans in the opposite direction.

Debt financing prevails in corporate financing in Slovenia: the proportion that it accounts for is above the euro area average. Further evidence of the inadequacy of the structure of financing and the differences with the euro area comes from the proportion accounted for by short-term financing and the negligible proportion accounted for by financing via alternative forms, such as corporate bonds.

Interest rates on corporate loans fell in 2009, but significantly less than in the euro area overall. The debt servicing burden will rise in the future, particularly in sectors that have recorded above-average increases in indebtedness. The proportion of new borrowing accounted for by fixed-rate borrowing is increasing rapidly, but variable-rate loans remain the prevalent form of borrowing. Given the prevalence of variable interest rates, high corporate indebtedness means that corporates will be burdened with debt servicing costs in the event of the anticipated rise in interest rates, which will also lead to slower economic recovery.

4.1 Corporate financing and net debt

Corporate financing flows

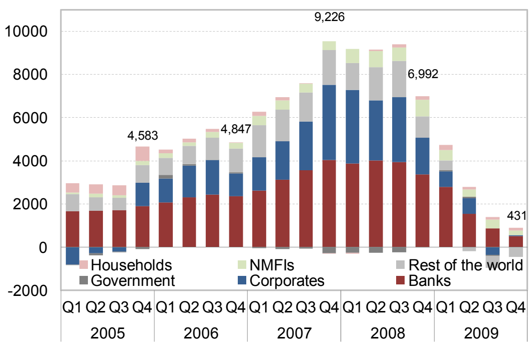
Corporate financing flows in 2009 declined to just 6% of the level in 2008.

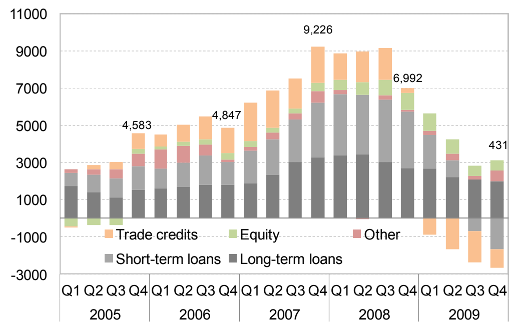
The impact of the financial turmoil was also reflected in a contraction in financing flows, not just via bank loans, but also in other forms of financing. The flow of financing in the final quarter of 2008 fell to a fifth of its average flow in 2007 and 2008. The decline in economic activity only led to an escalation in corporate financing difficulties. Financing flows amounted to merely EUR 431 million in 2009, just 6% of the flows in 2008. Debt repayments exceeded new financing in some forms of financing and at some creditors.

Corporate financing is declining both at banks, and at other sectors.

The flow of corporate financing at banks declined in 2009 to just 15% of its level in 2008, while the flow of corporate financing at non-monetary financial institutions was 30% of that in the previous year. Business-to-business financing, which in previous years was the second-largest source of corporate financing immediately behind the domestic banks, fell in 2009 to just 3.4% of its level in 2008. Corporates made net debt repayments to the rest of the world.

Figure 4.1: Corporate borrowing by sector (left) and instrument (right), annual moving total of flows in EUR million





Source: Bank of Slovenia

Business-to-business financing: the flow of financing declined and corporate liquidity position deteriorated in 2009.

The decline in business-to-business financing is the result of the reduced need for financing as a result of the decline in corporate activity, and also of the deterioration in the corporate liquidity position, which limits corporates' ability to engage in this financing. Corporate liquidity is being undermined by insufficient demand, payment indiscipline, and the lengthening of payment terms of corporates. The daily volume of unpaid past-due liabilities of legal entities increased by 75% to reach EUR 257 million in December 2009, although the actual amount is probably even higher.[13]

Lower financing via trade credits is the result of the decline in economic activity and, in relation to the rest of the world, the sharp decline in imports.

Financing between corporates via trade credits is particularly closely tied to the decline in turnover; financing provided by foreign partners reflects the sharp decline in foreign trade. This segment of corporate financing contracted sharply: trade credits received from foreign partners were down 14% in year-on-year terms, in line with the large decline in imports by Slovenian corporates.

In 2008, when corporates were first faced with greater limitations on borrowing from banks and the loss of partial compensation from other sectors, there was a pronounced increase in lending within the corporate sector. The proportion of the total flow of financing via loans accounted for by business-to-business loans in Slovenia exceeded 15% during that year. In 2009 the lack of liquidity in the context of the low economic activity also limited this source of financing.

Table 4.1: Flows of corporate financing (total, via loans and via trade credits) in EUR million

	Flows			Stock		Growth
	2007	2008	2009	2008	2009	2009
	(EUR million)					(%)
Total	9,226	6,992	431	86,959	87,320	
growth, %	90.3	-24.2	-93.8	-1.1	0.4	0.4
	of which:					
Loans	6,223	5,742	331	33,348	33,431	0.2
business-to-business	538	864	330	3,377	3,590	6.3
from banks	4,514	3,128	211	20,704	20,908	1.0
from NMFIs	612	722	150	3,149	3,188	1.2
from rest of the world	514	960	-404	4,972	4,718	-5.1
of which: from corporates	224	331	-478	1,443	1,040	-27.9
Trade credits	1,930	270	-1,013	13,378	12,425	-7.1
business-to-business	1,179	335	-488	7,817	7,401	-5.3
from rest of the world	613	-107	-592	4,519	3,878	-14.2

Source: Bank of Slovenia

Financing from the rest of the world: a decline in borrowing at foreign corporates.

Corporate borrowing in the rest of the world declined more than borrowing in Slovenia. This is particularly the case for trade credits and loans raised at foreign corporates. Even in the second half of 2008, the worsening of the financial turmoil, which affected foreign economies before Slovenia, began to be reflected in this source of financing drying up as there were large increases in repayments of loans raised earlier. The proportion of all loans from the rest of the world accounted for by loans raised at foreign corporates was down 7 percentage points at the end of 2009 at 22%.

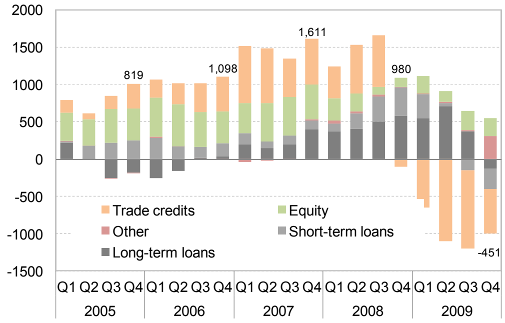
[13] The available figures only include non-payments on the basis of tax debt and those that acquire an epilogue in the form of court orders of enforcement, not all remaining unsettled mutual corporate claims and liabilities. The data source is the AJPES.

Table 4.2: Corporate financing in the rest of the world, stock in EUR million and breakdown in percentages

	Stock at year end			
	2006	2007	2008	2009
Total, EUR million	12,633	14,490	15,619	15,177
growth, %	7.0	14.7	7.8	-2.8
	Breakdown, %			
Securities[1]	0.2	0.2	0.1	1.9
Loans	24.2	26.0	31.8	31.1
of which: at foreign banks	10.2	9.0	10.7	12.5
at IFIs[2]	8.4	9.6	10.9	11.2
at foreign corporates	5.0	6.6	9.2	6.8
Equity	44.3	42.9	38.3	39.8
Trade credits and other	31.3	30.9	29.7	27.2

Notes: [1] Securities other than shares; [2] International financial institutions.
Source: Bank of Slovenia

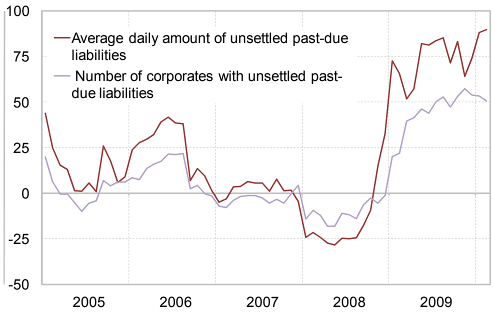
Figure 4.2: Corporate financing flows in the rest of the world in EUR million

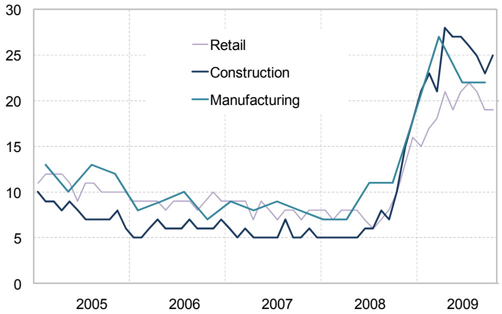


Financing at banks: corporates are faced with tightened lending terms at banks.

The deterioration in the corporate liquidity position and corporates' high indebtedness made it more difficult to access bank resources. Corporates are faced with tough requirements from the banks for collateral and for evidence of good prospects for projects, which is lacking in the existing economic structure. In 2009 an average of 22% of corporates in the manufacturing sector and 25% of corporates in the construction sector cited limitations in financing as one of the most important adverse factors of business.[14] The retail sector, which is mostly financed via shorter-maturity loans, is less exposed to these difficulties, but even there around 20% of corporates face major difficulties with financing.

Figure 4.3: Growth in unsettled past-due corporate liabilities in percentages (left) and proportion of corporates citing financing difficulties as a limiting factor in percentages (right)





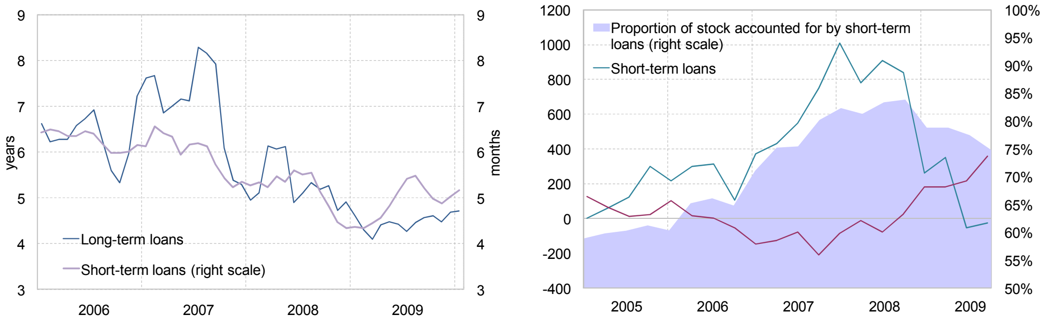
Sources: AJPES, SORS

The limited financing at banks primarily affected current corporate financing.

Corporate financing via bank loans in 2009 was just 6.7% of the flow of loans in 2008. In contrast to 2008, when the impact of the crisis on corporate financing conditions at banks was reflected primarily via a shortening of loan maturities, the main feature of 2009 was a sharp decline in bank lending activity. The problem of obtaining long-term loans worsened. As a result of repayments of short-term loans, which were not renewed in the same volume as before, the proportion of long-term loans in the maturity breakdown began to increase again. A similar trend in loan maturities can be seen in business-to-business loans.

[14] Source: SORS surveys.

Figure 4.4: Average maturity of newly approved corporate loans at banks (left) and flows of loans between non-financial corporations, annual moving totals in EUR million (right)

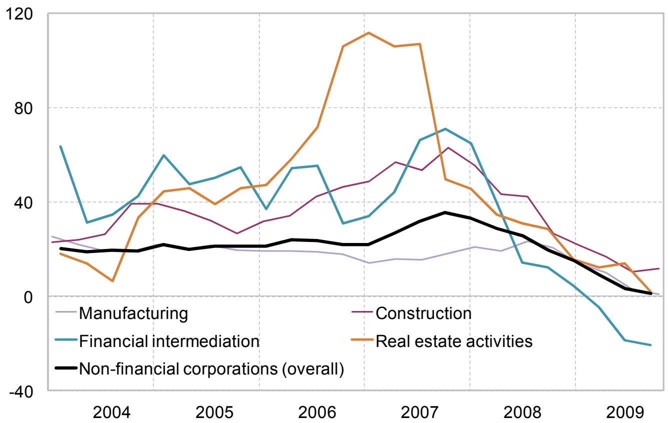


Sources: AJPES, SORS

The loss of financing at banks varied from sector to sector.

In the previous years of good economic climate, the sectors that recorded high growth were also notably financed via bank loans. Construction, real estate activities and activities of holding companies (majority of financial and insurance activities) were prominent for their high growth in bank loans. The period of heavy financing of holding companies ended in 2009 with negative rates of growth (partly as a result of the liquidation of banks' non-performing claims). Given the slowdown in construction activity and the real estate market, real estate activities also recorded a sharp decline in the volume of loans raised at banks. Certain other sectors again increased their borrowing at banks in 2009. The construction and transportation sectors each succeeded in increasing their borrowings from banks in the amount of the entire increase in bank loans to non-financial corporations.[15] In the last six years of above-average growth in loans to the construction sector, which averaged 28% annually, the proportion of the stock of loans to non-financial corporations accounted for by the sector has risen by 5.5 percentage points to 10.8%. At the same time the proportion accounted for by manufacturing declined by 5.3 percentage points to 26.7%. The reason for the divergence in the financing of individual sectors during the financial turmoil can be found in the shorter business cycles of manufacturing and other sectors, which allow them to respond more quickly to reduced demand through lower demand for bank loans, in contrast to construction, where the completion of projects of many years' duration requires extended financing.

Figure 4.5: Growth in bank loans to individual sectors in percentages



Source: Bank of Slovenia

Only in exceptional cases do Slovenian corporates finance themselves via bonds. This form of financing increased slightly in 2009 to account for 1.1% of total corporate financing, compared with 3.4% in the euro area overall.

Corporate financial liabilities

Despite the absence of new financing, corporates saw an increase in the ratio of their indebtedness to GDP, as a result of the latter's decline in 2009.

The stock of non-financial corporations' financial liabilities increased by EUR 361 million in 2009 to EUR 87.3 billion, equivalent to 250% of GDP. Other factors in addition to current borrowing have contributed to the change in the ratio of non-financial corporations' debts to GDP in the last two years. In 2008 falls on the stock markets

[15] See the section on credit risk.

devalued the portion of liabilities deriving from equity, and thus contributed to a smaller increase in corporates' total financial liabilities, despite relatively high borrowing. In 2009, while the increase in corporate borrowing was modest compared with the years before the financial turmoil, the sharp decline in GDP meant that the ratio of total corporate financial liabilities to GDP rose again, by 14 percentage points.

Table 4.3: Stock and breakdown of financial liabilities by instrument, and corporate debt in EUR million and percentages

	2005	2006	2007	2008	2009
	(EUR million)				
Total liabilities	62,984	71,305	87,946	86,959	87,320
growth, %	11.4	13.2	23.3	-1.1	0.4
as % GDP	219.4	230.0	254.4	234.2	250.3
Debt[1]	18,972	21,403	27,928	33,830	34,258
growth, %	19.0	12.8	30.5	21.1	1.3
as % GDP	66.1	69.0	80.8	91.1	98.2
	Breakdown, %				
In Slovenia	81.2	82.3	83.5	82.0	82.6
corporates	31.1	29.9	30.0	29.9	29.5
banks	18.0	19.4	20.9	24.9	25.3
bank loans	16.7	18.0	19.9	23.8	23.9
NMFIs	6.6	6.8	7.4	6.2	6.2
government	11.9	12.5	12.2	9.0	8.9
households	13.6	13.5	13.0	12.0	12.6
In rest of the world	18.8	17.7	16.5	18.0	17.4
loans at foreign banks	2.3	1.7	1.5	1.9	2.2

Note: [1] Debt includes loans, debt securities (excluding derivatives) and insurance technical provisions, and in the Slovenian corporate sector practically consists solely of loans raised.

Source: Bank of Slovenia

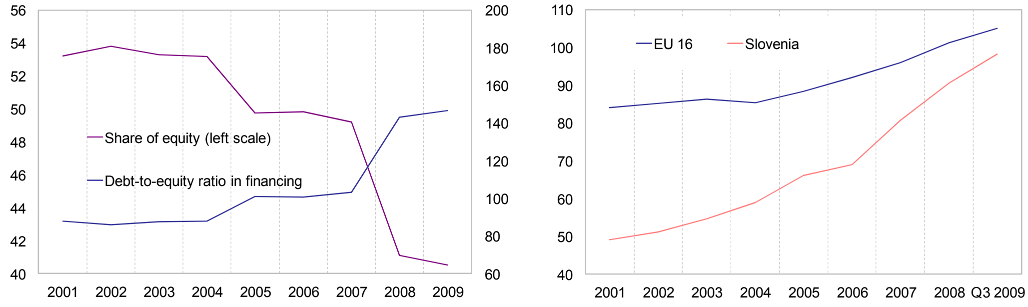
High corporate indebtedness is limiting the acquisition of new financing at banks.

Equity accounts for 42% of corporate financial liabilities, 6 percentage points less than the in the euro area overall. Corporate indebtedness as measured by the debt-to-equity ratio is significantly higher in Slovenia than in the euro area overall (147%, compared with 105% in the euro area), and indicates a problem with corporate under-capitalisation in a situation of economic crisis. High indebtedness is a significant limiting factor in obtaining loans from banks, which have begun assessing borrowers' credit risk more prudently. To improve the structure of financing, corporates must be more active in attracting fresh equity instead of debt-based resources. Growth in equity from retained earnings will be limited, given the low profits expected in the coming years. Profits will be lower because of the anticipated slow pace of the recovery in the coming years, and also because of the high debt servicing burden faced by corporates, particularly those who borrowed with high inbuilt premiums in the loan price.

The proportion accounted for by short-term financing is higher than in the euro area overall.

Another significant factor in the inadequate corporate financing structure is the high proportion accounted for by short-term financing, which has led to a deterioration in liquidity. This is reflected indirectly in corporates' short-term focus on current performance, but also in the spread of structural banking problems to corporate financing. The proportion of total bank loans accounted for by short-term loans is 36%, significantly more than the overall euro area figure of 25%. The proportion of total corporate financial liabilities accounted for by short-term resources (loans and trade credits) is also higher than in the euro area overall at 32%, compared with 22%. The short-term nature of the resources also entails a greater need for refinancing on the part of corporates, which in the conditions of the financial turmoil is hindered by the limitations on resources, and as a result entails higher total corporate financing costs.

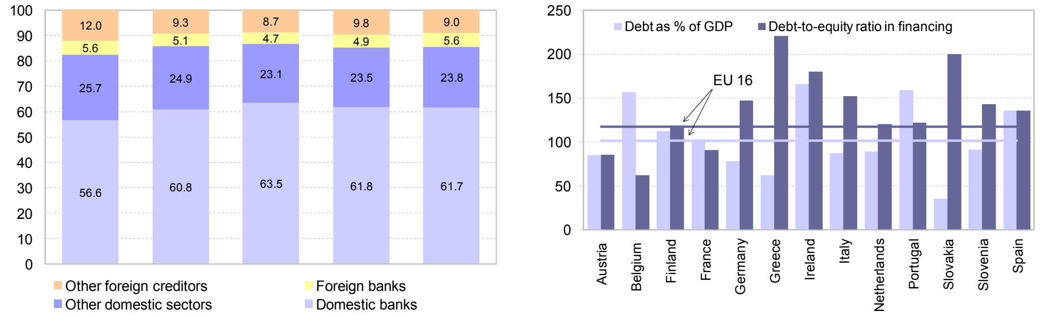
Figure 4.6: Debt-to-equity ratio in corporate financing (left) and increase in ratio of corporate debt to GDP in Slovenia and the euro area (right)



Source: Bank of Slovenia

The ratio of corporate debt to GDP stood at 98.2% in 2009. Corporate indebtedness in the euro area as measured by this indicator was 10 percentage points higher, but the gap has narrowed extremely sharply in recent years.

Figure 4.7: Structure of Slovenian corporate debt in percentages (left) and comparison of corporate indebtedness in the euro area in 2008 in percentages (right)



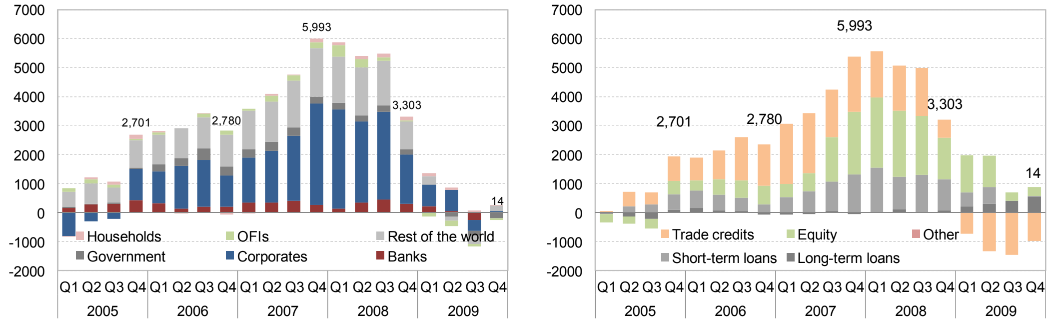
Source: Bank of Slovenia

Corporate financial assets and net financial position

Corporates are reducing their financial investments.

Corporates have been reducing their financial investments since the final quarter of 2008. The flow of corporate financial investments between the final quarter of 2008 and the end of 2009 was negative in the amount of EUR 817 million. By the end of 2009 the stock of investments had returned to its level at the end of 2007. The largest decline was recorded by inter-corporate investments, which are prevalent in the breakdown of corporate investments. The flow of loans between corporates was just 38% of its level in 2008. Having been a major means of promoting sales between corporates in previous years, trade credits recorded net repayments. Corporate investments in the household sector declined by two-thirds. In the context of the low total financing of households, there was a change in the breakdown: the flow of loans to households increased slightly, while trade credits as a means of promoting sales to the household sector dried up entirely, households actually making net repayments.

Figure 4.8: Corporate investments by sector (left) and instrument (right), annual moving total of flows in EUR million



Source: Bank of Slovenia

There was a slight change in the breakdown of investments in the rest of the world, which include the financing of business partners and related corporates in the rest of the world. Trade credits to the rest of the world, which in previous years accounted for 30% to 60% of all corporate investments in the rest of the world, shared the fate of Slovenia's foreign trade in 2009 and declined by 10%.

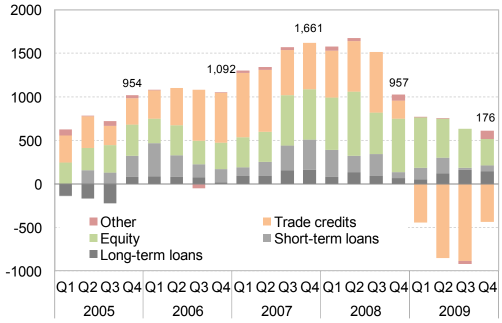
Corporates increased their financing of the rest of the world via loans in 2009.

Table 4.4: Corporate investments in the rest of the world, stock in EUR million and percentages

	Stock at year end			
	2006	2007	2008	2009
Total, EUR million	7,501	9,076	10,146	10,312
growth, %	10.8	21.0	11.8	1.6
	Breakdown, %			
Securities other than shares	0.5	0.6	0.5	0.6
Loans	7.7	12.9	13.5	15.6
Equity	30.3	30.2	32.2	35.0
Trade credits and other	60.1	54.2	52.1	47.2

Source: Bank of Slovenia

Figure 4.9: Corporate financing flows in the rest of the world in EUR million



The net flow of corporate loans to the rest of the world in 2009 was the second-largest of the last five years, three times in excess of that of 2008. Financing of the rest of the world via loans was aimed primarily at supporting corporates' own exports and supporting the operations of subsidiaries in the rest of the world. In contrast, in 2009 foreign owners of Slovenian corporates were prevalent among loan recipients. At the same time Slovenian corporates made net repayments of debts received from foreign owners. The overall effect was that corporates significantly financed their foreign owners in the amount of EUR 581 million. Net loans from the rest of the world (loans received minus loans approved), which in 2008 were a significant additional source of corporate financing, were exhausted in 2009 as a result of the financing of parent companies in the rest of the world, an indication of the instability of debt financing via loans from the rest of the world during the conditions of the financial turmoil.

A high net outflow of loans from corporates as a result of financing of owners in the rest of the world.

Table 4.5: Loans to and from the rest of the world with regard to ownership links, transactions in EUR million

	Loans from rest of the world				Loans to rest of the world				
	From foreign investors in Slovenia	From Slovenian corporates in rest of the world	Without ownership links	TOTAL	To foreign investors in Slovenia	To Slovenian corporates in rest of the world	Without ownership links	TOTAL	Net loans granted
2005	-3	18	-202	-187	120	23	59	201	389
2006	46	-5	50	91	-50	33	103	86	-4
2007	127	58	319	503	124	297	68	489	-15
2008	371	14	570	955	-80	134	45	100	-855
2009	-465	20	48	-397	116	111	91	318	715
	From EU	From ex-YU	From other countries	TOTAL	To EU	To ex-YU	To other countries	TOTAL	
2005	-190	0	2	-187	119	18	64	201	389
2006	5	0	86	91	15	78	-7	86	-4
2007	64	19	421	503	277	188	24	489	-15
2008	392	51	512	955	-64	76	88	100	-855
2009	-177	-16	-204	-397	151	137	30	318	715

Source: Bank of Slovenia

As on the liability side, the ratio of the stock of corporate investments to GDP rose by several percentage points as a result of the sharp decline in GDP in 2009. The ratio of corporates' net financial liabilities to GDP was up 9 percentage points at 119%. The net debt position of corporates in the euro area rose by a similar amount, but is lower at 99.5% of GDP. This provides further evidence of the relatively higher dependence of Slovenian corporates on debt financing than that of euro area corporates overall.

The net corporate debt position increased to 119% of GDP.

Table 4.6: Net corporate financial liabilities, stock at year end in EUR million and percentages

	2005	2006	2007	2008	2009
			(EUR million)		
Total	28,798	33,696	42,382	40,900	41,641
growth, %	7.5	17.0	25.8	-3.5	1.8
as % GDP	100.2	108.5	122.6	110.1	119.3
			Breakdown, %		
In Slovenia	82.5	84.8	87.2	86.6	88.3
banks	25.8	28.5	32.6	41.3	41.5
NMFIs	10.3	9.9	10.3	9.2	9.3
government	21.2	21.4	20.6	14.0	14.4
households	25.3	25.1	23.9	22.3	23.3
In rest of the world	17.5	15.2	12.8	13.4	11.7

Source: Bank of Slovenia

The ratio of loans to deposits at banks improved after several years.

The corporate sector's net debt position against the banking system was up slightly on the end of 2008 as a ratio to GDP, but declined in absolute terms. Corporate deposits at banks have increased at very low rates during the last two years, which were marked primarily by liquidity problems, while the stock of loans actually declined slightly last year (impairments were deducted from the stocks). After several years of rapid increase, the ratio of loans to deposits recorded its first decline in 2009.

Table 4.7: Corporate loans from and deposits at banks, stock at year end in EUR million and percentages

	Corporate borrowing at banks		Corporate	Net corporate borrowing at banks		
	Corporate loans		deposits			
	(EUR million)	(as % GDP)	(EUR million)	(EUR million)	Ratio	(as % GDP)
	(1)	(2)=(1)/BDP	(3)	(4)=(1-3)	(5)=(1/3)	(6)=(4)/GDP
2005	9,907	34.5	3,128	6,779	3.2	23.6
2006	12,364	39.8	3,341	9,023	3.7	29.1
2007	17,039	49.3	3,674	13,365	4.6	38.7
2008	20,245	54.5	3,712	16,533	5.5	44.5
2009	20,009	56.5	3,796	16,213	5.3	45.8

Source: Bank of Slovenia

4.2 Interest rates and interest-rate risk for corporates

Lending rates

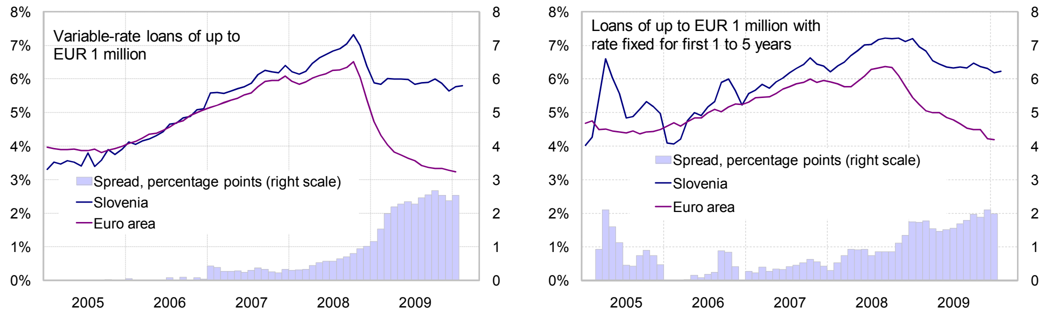
Interest rates on corporate loans have been falling since October 2008, the gap with the euro area is widening.

Interest rates on corporate loans at Slovenian banks fell in 2009. On the most common type, variable-rate loans of up to EUR 1 million, interest rates had fallen by 0.7 percentage points by the end of 2009, and by 3.2 percentage points from their peak in October 2008.

The fall in interest rates was slower than in the euro area overall, where lending rates for corporate tracked the market reference interest rates more than in Slovenia, falling by 2.1 percentage points in 2009. The spread between variable interest rates on loans at banks in Slovenia and those in the euro area overall widened to 2.5 percentage points. The reasons for the widening of the spread in interest rates with the euro area were the decline in all forms of financing for Slovenian corporates and the high dependence on bank loans. In the decline in the supply of loans, both at the domestic banks and in the rest of the world, the banks saw an increase in their ability to set the financing conditions.

The spread between banks in Slovenia and those in the euro area on fixed-rate loans was lower, although euro area interest rates also declined more rapidly in this segment. That fixed interest rates are higher than variable rates is a reflection of expectations of interest rate rises in the future.

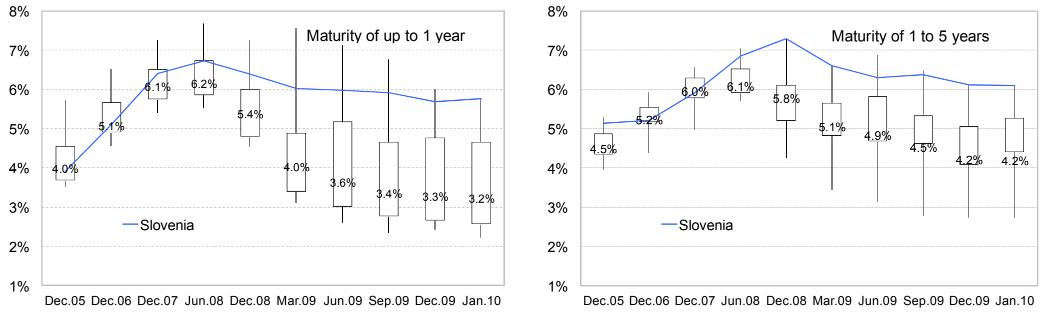
Figure 4.10: Comparison of interest rates on loans of up to EUR 1 million at banks in Slovenia and in the euro area, and interest rate spread in percentage points



Sources: ECB, Bank of Slovenia

Spreads in lending rates between euro area countries have been widening since the second half of 2008. The flow of capital between banks declined sharply in the financial turmoil. Given the lack of funding, banks are more likely to set interest rates with regard to the quality of the individual clients or projects than during a period of high loan supply, the variation between banks thereby increasing, and likewise the variation between countries.

Figure 4.11: Dispersion of interest rates on corporate loans of up to EUR 1 million in the euro area in percentages

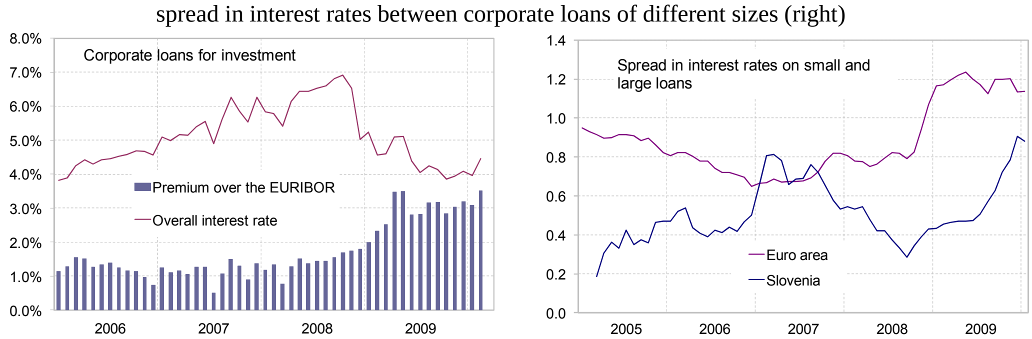


Sources: ECB, Bank of Slovenia

The difference in interest rates is increasing at the Slovenian banks with regard to loan size.

The dispersion of interest rates is particularly high in the segment of low-value loans with a maturity of up to 1 year. On loans with a maturity of 1 to 5 years the dispersion of interest rates in the euro area is notably lower, the Slovenian banks overall demanding the highest interest rates of all euro area countries. The fall in the price of low-value corporate loans at Slovenian banks in 2009 was slightly less than that of larger loans. The average spread between interest rates on these loan segments had widened from 0.4 percentage points at the end of 2008 to 0.9 percentage points by the end of 2009. Slovenian banks thereby narrowed the difference with the euro area, where the average spread stood at 1.1 percentage points at the end of 2009. The more favourable interest rates on larger loans are a reflection of the greater credit capacity of larger clients, and their better credit ratings, which are based on their relatively greater stability.

Figure 4.12: Increase in premiums over the EURIBOR for corporate loans (left) and spread in interest rates between corporate loans of different sizes (right)



Sources: ECB, Bank of Slovenia

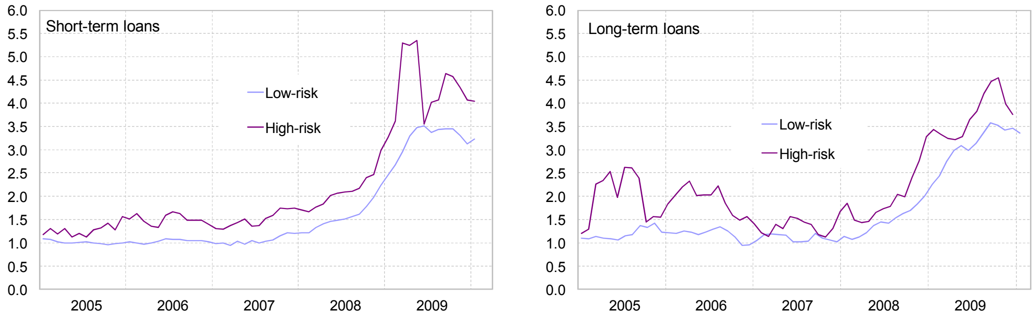
Premiums over the EURIBOR are rising in the context of falling interest rates.

The banks' premiums over the reference interest rates are increasing even as interest rates fall. This is partly the result of stricter credit standards at the banks and the increase in credit risk, and partly the result of the banks' maintenance of profits in the context of declining lending activity, or at least the prevention of continuing falls in profits. The premiums over the EURIBOR for newly approved corporate loans between the end of 2008 and February 2010 were up to 3.7 percentage points for short-term loans and up to 3.5 percentage points for long-term loans for investment.

Risk premiums on loans with regard to debtor's credit rating

The premiums over the EURIBOR for each client category reflect the banks' assessments of each client's level of credit risk. On newly approved short-term loans the risk premium for high-risk loans increased more than that of low-risk loans. The average spread between these loan segments widened from an average of 0.5 percentage points in 2008 to 1.1 percentage points in 2009. The spread between the risk premiums on high-risk and low-risk long-term loans widened from 0.4 percentage points in 2008 to 0.7 percentage points in 2009, an indication of the banks' reduced propensity to take up additional credit risks, or to evaluate credit risks more conservatively than before the financial turmoil.

Figure 4.13: Premiums over the EURIBOR for short-term (left) and long-term (right) euro-denominated corporate loans, by client credit rating, 3-month moving average in percentage points



Source: Bank of Slovenia

Interest-rate risk for corporates (proportions of fixed and variable remuneration)

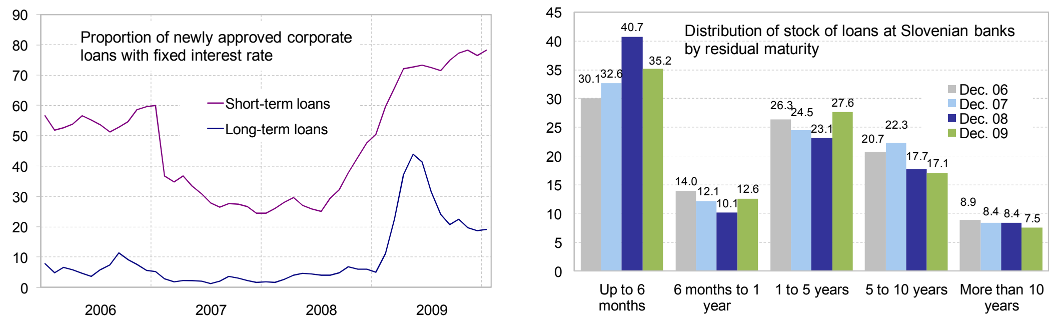
High premiums over the EURIBOR entail high interest-rate risk for corporates.

Corporates mostly borrow at banks at variable interest rates. Loans with variable-rate (including all loans with fixed interest rates for period shorter than one year) accounted for 97.4% of existing loans in 2009. The most frequently used reference interest rate is the EURIBOR. The high premium levels represent the invariable portion of the interest rate, and represent the high interest-rate risk for corporates, particularly on loans of longer maturities. Given the anticipated rise in reference interest rates, servicing these loans will place a heavy burden on corporate revenue.

The proportion of newly approved loans with a fixed interest rate is increasing.

In 2009 the financing conditions for corporates at banks changed in the direction of increased fixed-rate borrowing. The proportion of newly approved long-term corporate loans accounted for by fixed-rate loans exceeded 25% over the year, up significantly on the previous year's figure of just 4%. The equivalent figure for short-term loans was 70%, compared with 32% in 2008.

Figure 4.14: Proportion of loans with a fixed interest rate (left) and distribution of loans by maturity (right) in percentages



Source: Bank of Slovenia

The proportion of loans with a fixed interest rate is approaching the euro area average.

The increase in the proportion of fixed-rate loans among newly approved loans moved the breakdown of corporate loans at banks by type of remuneration in 2009 closer to the average breakdown in the euro area. Up to and including 2008 the proportion of variable-rate loans in Slovenia was a tenth higher than the euro area average. In 2009 the gap narrowed to just under 2 percentage points. The increase in fixed-rate remuneration was particularly pronounced among larger loans, which in the past were almost entirely variable-rate.

Table 4.8: Proportion of new corporate loans with a variable interest rate[1]

	2006	2007	2008	2009
	(%)			
Euro area	87.1	87.6	90.2	90.7
up to EUR 1 million	85.9	85.5	86.0	86.0
over EUR 1 million	87.6	88.4	91.5	92.1
At domestic banks	97.2	99.2	99.2	92.5
up to EUR 1 million	97.3	98.1	98.4	94.9
over EUR 1 million	97.1	99.6	99.4	91.9

Note: [1] For comparability with ECB methodology, variable-rate loans include loans on which the agreed interest rate is fixed for a period of less than one year (the table includes all short-term loans otherwise shown as fixed-rate loans in the separate disclosure of short-term loans).
Sources: ECB, Bank of Slovenia

Corporate loan repayment burden

The breakdown of loans falling due for repayment is more favourable than a year earlier.

The breakdown of loans falling due for repayment in 2009 was slightly more favourable than in the previous year. At the end of 2009 almost half of corporate debt to banks had a maturity of up to 1 year. The sharp increase in the maturing of loans with the shortest maturities in 2008 eased slightly in 2009. The proportion of loans with a maturity of less than 6 months declined by 5 percentage points to 35%, although the proportion is still higher than before the financial turmoil. The proportion of loans with a longer maturity of 1 to 5 years was slightly higher than in 2008.

The debt servicing burden is rising at corporates, particularly in the sectors of real estate activities, activities of holding companies, and construction.

The heavy borrowing in the years before the financial turmoil began to be reflected in corporate balance sheets via a rising debt servicing burden. The ratio of interest paid to revenue rose from an average of 0.8% between 2005 and 2007 to 1.1% in 2008. In 2009 the ratio declined slightly, as a result of the sharp fall in interest rates during the year, and the prevalence of variable-rate remuneration. The decline in corporate revenue in 2009 meant that this positive effect was not reflected in full.

According to bank surveys, despite the smaller level of interest paid, the corporate debt servicing burden increased, as a result of the previous heavy borrowing and the amount of debt falling due for repayment.

Table 4.9: Selected indicators of the corporate interest repayment burden in percentages

	2005	2006	2007	2008	2009
Ratio of interest paid to income	0.8	0.7	0.8	1.1	1.0
Ratio of net interest paid to income	0.5	0.5	0.6	0.7	0.7
agriculture, forestry, fishing, mining, quarrying	1.0	0.7	0.9	0.8	0.9
manufacturing	0.4	0.5	0.5	0.7	0.6
electricity, gas, water; remediation	0.2	0.3	0.1	0.1	0.0
construction	0.7	0.6	0.7	0.9	1.0
wholesale and retail trade	0.3	0.3	0.4	0.4	0.3
transportation and storage	0.5	0.6	0.6	0.8	0.8
accommodation and food service activities	1.2	0.9	1.0	1.6	1.7
information and communication activities	0.8	0.2	0.1	0.5	0.8
financial and insurance activities	5.1	5.0	4.7	6.9	9.7
real estate activities	2.1	2.6	3.0	5.9	5.4
professional, scientific and technical activities	0.7	0.7	0.8	1.3	1.0
public services	0.5	0.6	0.6	1.0	0.8
Ratio of net interest paid to net profit	16.8	13.2	13.8	36.4	70.7

Sources: AJPES, own calculations

The sharp increase in borrowing was reflected in certain sectors in a larger increase in the debt servicing burden. The ratio of net interest paid to revenue rose sharply over the last two years in financial and insurance activities (non-financial holding companies) and real estate activities, i.e. in sectors that recorded growth in borrowing of 70% and 110% respectively in 2007. The interest repayment burden also increased sharply in the accommodation and food service activities sector, which has operated at a loss in the last two years. In the construction sector the increase in this indicator was lower, most likely as a result of the longer average maturity of its borrowing. Given the poor forecasts of recovery for the sector, and its ongoing borrowing during the time of the credit crunch, its debt servicing burden can be expected to increase sharply.

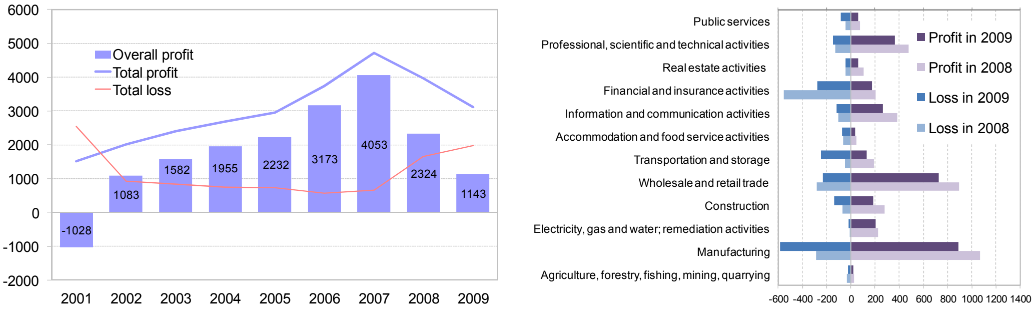
The debt servicing burden will also increase in the future at those corporates that in 2009 raised long-term loans at variable interest rates, with high premiums over the current low market reference interest rates.

4.3 Corporate performance and risk by sector

The effects of the financial turmoil on corporate performance were seen in a fall in profits and a rise in losses in 2008 and 2009.

The initial effects of the financial turmoil on corporate performance were seen in annual reports for 2008, in a fall in profits and rising losses. The deeper effects of the crisis were revealed in the reports for 2009, when the decline in economic activity had a more profound impact on corporate financial positions. In 2009 there were sharp declines in value-added in manufacturing and construction, while that in wholesale and retail trade was also above-average. In contrast to other sectors, where the positive expectations for the future are gradually strengthening, pessimism is deepening in the construction sector.

Figure 4.15: Total profit and loss by year (left) and by sector (right) in EUR million



Sources: AJPES, Bank of Slovenia

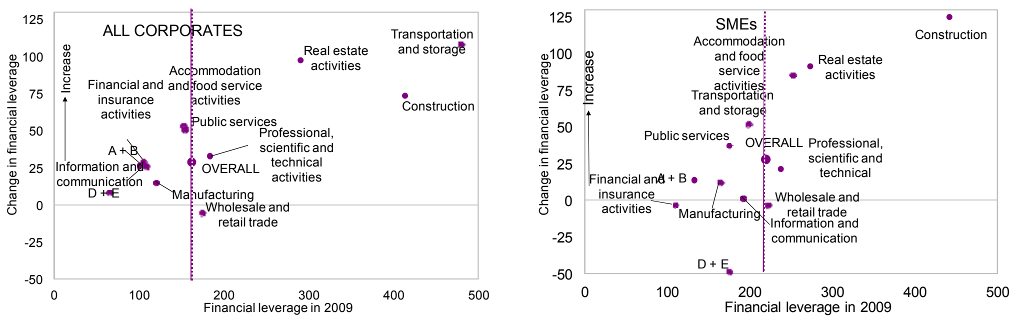
A decline in net profit in 2009 to the level seen in 2002.

Net corporate profit fell over 2008 and 2009 to reach EUR 1.1 billion, its level in 2002. The total corporate profit generated was down a third on 2007, while losses were up 200%. The sectors of accommodation and food service activities, financial and insurance activities, and agriculture, forestry and fishing recorded a net loss in 2008, while in 2009 they were joined by the sectors of transportation and public services.

Corporate financial leverage rose sharply during the years of rapid borrowing, reaching 165% in 2008.

Corporates were highly indebted as they entered the financial turmoil. Financial leverage rose rapidly between 2006 and 2008, reaching 165% in 2008. As a result of the almost complete standstill in all sources of corporate financing, there was no significant change in financial leverage overall in 2009, although its movement in certain sectors was dependent on corporates' success in obtaining financial resources in the harsher conditions.

Figure 4.16: Financial leverage by sector and change in the last three years



Note: A+B: agriculture, forestry, fishing, mining and quarrying; D+E: electricity, gas and water supply, environmental remediation.
Sources: AJPES, Bank of Slovenia

SMEs are more indebted than large enterprises.

Debt capital was more than four times higher than equity in the construction sector at the end of 2009, while it was almost three times as high in the related sector of real estate activities. The highest level of indebtedness was recorded by corporates in the transportation and storage sector (480%), primarily because of the sector's large enterprises. Transportation is the only sector where the SMEs are significantly less indebted than the large enterprises. The indebtedness of the SMEs in the accommodation and food service activities sector increased considerably in 2009, significantly more than that of the sector's large enterprises. Corporate indebtedness is extremely high in the sectors of construction and real estate activities, irrespective of size. The boom in construction encouraged high activity supported by borrowing, even in the mass of smaller enterprises, which remained highly indebted after the decline in activity. The financial leverage of SMEs stood at 219% at the end of 2009, 57 percentage points higher than the average figure for all non-financial corporations.

Short-term liquidity in 2009 was at a similar low level to 2008.

Corporate liquidity has declined in the last few years. The decline in liquidity in 2008 was greater than in the previous years, as it fell from 76.3% to 68.6%. A major factor in the decline was the large increase in short-term financing at banks during the year. At the same time the slowdown in economic activity meant that short-term claims began to decline, a process that continued in an even greater scope in 2009. The proportion of long-term investments on the investment side of the corporate balance sheet is increasing, partly as a result of the aforementioned decline in short-term claims, and partly as a result of an increase in long-term financial investments, in particular investments in shares and interests, and the financing of related corporates in the rest of the world. As a result of the simultaneous decline in short-term claims and liabilities, there was no significant change in the current liquidity indicator in 2009.

Table 4.10: Maturity breakdown of financial and operating claims and liabilities in percentages

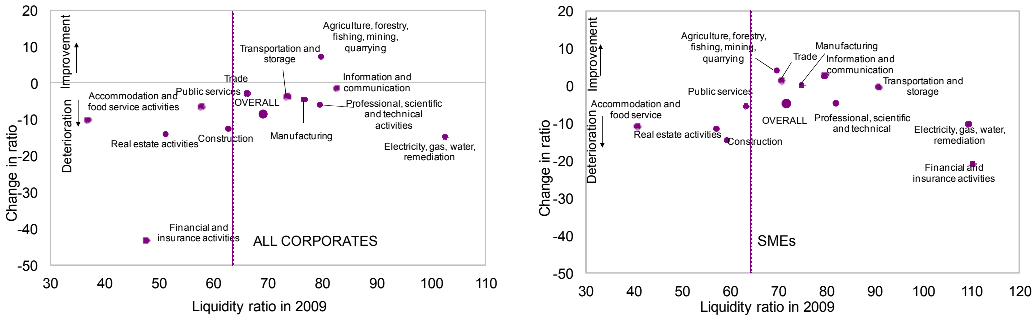
	2005	2006	2007	2008	2009
	Breakdown, %				
Financial and operating claims					
long-term	42.4	39.3	39.1	41.3	43.1
short-term	57.6	60.7	60.9	58.7	56.9
Financial and operating liabilities					
long-term	41.2	41.2	40.0	38.8	41.7
short-term	58.8	58.8	60.0	61.2	58.3
	Ratio of claims to liabilities, %				
Overall	81.3	75.2	75.2	71.5	70.9
long-term	83.7	71.7	73.6	76.1	73.3
short-term	79.6	77.6	76.3	68.6	69.1

Sources: AJPES, own calculations

The largest declines in liquidity were recorded by non-financial holding companies, real estate activities, and construction.

Compared with 2007, the largest decline in liquidity in 2009 was recorded by corporates in the sector of financial and insurance activities, which mostly comprises non-financial holding companies. In 2007 and 2008 they recorded borrowing heavily above the average, banks assessing their ability to service the debts on the basis of their relatively low indebtedness at the time, while the aspect of liquidity during harsher economic conditions was underestimated. Holding companies that were established to acquire companies repaid their debts from the profits of the acquired companies, which in addition to servicing their own indebtedness by paying out dividends also supported their owners' debt servicing.

Figure 4.17: Liquidity ratios by sector and change in percentage points in the last three years



Sources: AJPES, Bank of Slovenia

Liquidity also declined significantly in real estate activities, and by slightly less in construction. Figures for unsettled past-due liabilities indicate that corporate liquidity problems increased sharply in these two sectors. By December 2009 the stock had reached two or three times the level at the end of 2008.

Arrears in the settlement of liabilities at banks increased sharply in 2009.

The deterioration in corporate liquidity was reflected in growing arrears in the settlement of liabilities to banks. The proportion of corporates in arrears in settling their liabilities to banks rose from 14.2% at the end of 2008 to 17.9% in February 2010. The proportion of corporates whose arrears were in excess of 90 days in February was 11.4%. The average number of days in arrears increased more than the number of corporates in arrears, an indication of the lengthening of existing arrears and the deepening liquidity problems at these corporates. The proportion of corporate liabilities to banks being settled by corporates more than 90 days in arrears rose from 3.5% at the end of 2008 to 6.6% at the end of 2009. By February 2010 the proportion of corporate liabilities to banks being settled by corporates more than 90 days in arrears had risen to 7.5%.

Table 4.11: Days in arrears at banks at the end of 2009

	Number of corporates in arrears	% of total number of corporates at banks in arrears: total	% of total number of corporates at banks in arrears: of which, more than 90 days in arrears		Average number of days in arrears	% of classified claims in bank portfolio in arrears: total	% of classified claims in bank portfolio in arrears: of which, more than 90 days in arrears	
		Dec. 09	Dec. 08	Dec. 09		Dec. 09	Dec. 08	Dec. 09
Agriculture, forestry, fishing, mining, quarrying	36	16.0	12.0	12.0	803	6.5	6.2	5.5
Manufacturing	673	17.2	9.7	11.0	355	11.5	3.8	6.3
Electricity, gas, water; remediation	22	8.9	3.0	3.7	66	2.7	1.3	0.8
Construction	655	22.7	10.3	15.2	203	19.5	3.0	7.7
Wholesale and retail trade	1140	17.3	11.5	13.1	561	9.0	5.1	5.1
Transportation and storage	283	21.6	10.6	15.0	136	6.7	2.6	1.9
Accommodation and food service activities	239	23.6	14.3	16.9	416	12.2	3.6	7.9
Information and communication activities	122	9.6	4.6	6.0	130	13.7	1.4	1.8
Financial and insurance activities	29	21.0	4.8	13.8	233	29.1	1.5	21.6
Real estate activities	119	18.6	7.5	10.8	189	13.3	2.1	4.8
Professional, scientific and technical activities	499	10.2	5.8	6.9	379	12.9	5.1	7.6
Public services	112	9.3	5.0	6.1	209	6.7	1.2	2.2
Overall	3,930	16.1	9.1	11.1	311	12.6	3.5	6.6

Sources: AJPES, own calculations

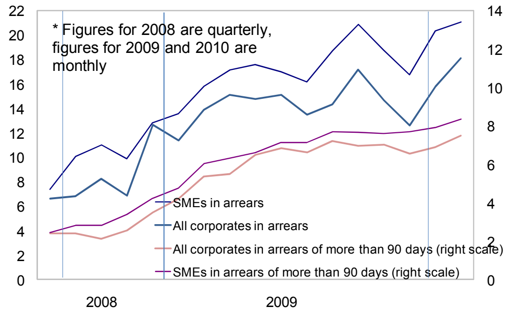
A large proportion of longer arrears at non-financial holding companies, accommodation and food service activities, construction and professional, scientific and technical activities.

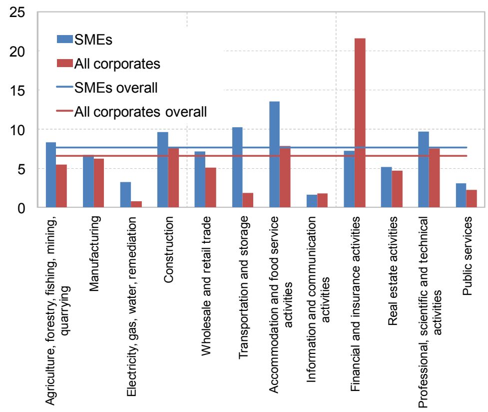
The problem of lengthening arrears became very significant in 2009 at corporates in the sector of financial and insurance activities (non-financial holding companies), where almost 22% of the banking system's classified claims in this sector recorded longer arrears, and every fifth corporate disclosed longer arrears. The sectors of accommodation and food service activities (7.9%) and professional, scientific and technical activities (7.6%) also recorded a high proportion of longer arrears. In the early months of 2010 the problem of longer arrears worsened in the sectors of construction (an increase to 10.3%) and real estate activities (7.5%), both sectors recording an increase in the figure of 2.7 percentage points on the end of 2009.

Arrears at banks are higher at SMEs.

SMEs are more exposed to liquidity problems because of their small size, which reduces their economic and negotiating power in relation to business partners and to the commercial banks. Larger enterprises are partly succeeding in passing their liquidity problems onto SMEs, where the problems are intensifying. Average arrears in the settlement of liabilities to banks are longer at SMEs, while the proportion of corporates in arrears is higher than for large enterprises. Almost 17% of SMEs' liabilities to banks were in arrears at the end of 2009, 4.2 percentage points higher than the figure for corporates overall. The proportion of liabilities to banks more than 90 days in arrears at SMEs was an average of 0.5 percentage points higher than for corporates overall for the majority of 2009. Towards the end of the year the gap widened to 1 percentage point, and remained at this level in the first two months of 2010.

Figure 4.18: Comparison of arrears at banks for SMEs and all corporates: overall (left) and by sector for arrears of more than 90 days (right) as percentage of total liabilities to banks





Source: Bank of Slovenia

SMEs disclose longer arrears in all sectors other than financial and insurance activities and information and communication activities. In the accommodation and food service activities sector more than 13% of SMEs' liabilities were settled with longer arrears in December 2009 (compared with 7.9% of those of all corporates). Corporates in the sectors of wholesale and retail trade and professional, scientific and technical activities are also more exposed with regard to size.

Risk premium at banks by sector

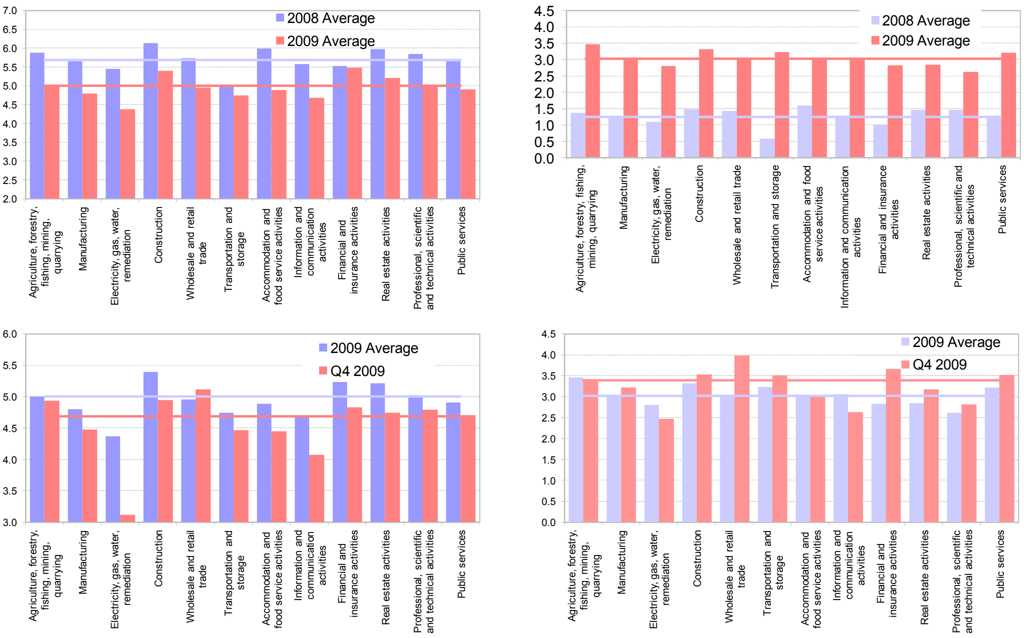
The realised interest rates tied to the EURIBOR on newly approved long-term corporate loans average 5% in 2009, down 0.7 percentage points on 2008. The premiums over the EURIBOR on these loans have been rising since the outbreak of the financial turmoil in autumn 2007. They averaged 3 percentage points in 2009, compared with 1.2 percentage points in 2008.

High increase in premiums over the EURIBOR in 2009.

The spread in the premiums in lending rates between sectors ranged from 2.6 to 3.5 percentage points, the spread between the highest and lowest premiums remaining unchanged from 2008. In 2009 the premiums over the EURIBOR shifted upwards in the sectors of construction, transportation and storage, agriculture and public services. The premiums on new long-term loans in the majority of sectors rose in the final quarter, most notably in the sectors of wholesale and retail trade and financial and insurance activities.

The highest risk premiums are in construction, transportation, agriculture and public services.

Figure 4.19: Overall interest rate (left) and premiums over the EURIBOR (right) on long-term bank loans, by sector in percentages

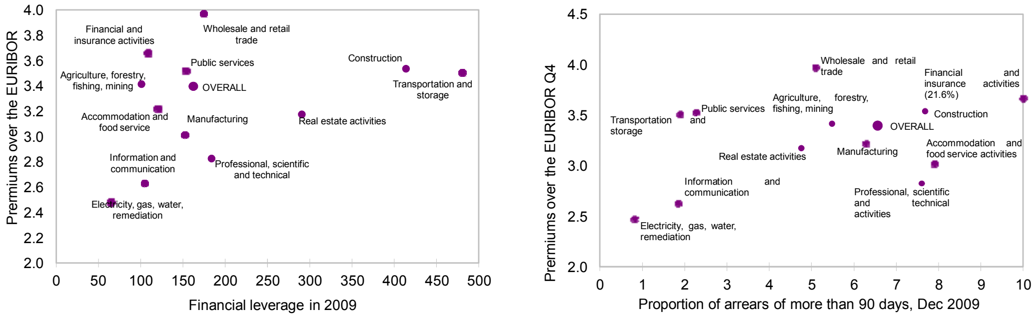


Note: Interest rates on long-term bank loans; only loans tied to the EURIBOR are included in the premium figures.
Source: Bank of Slovenia

The link between the risk premium and a corporate's financial situation is not evident in all activities.

The size of the premium for a particular corporate depends on its financial position; during the harsher financing conditions the importance of a corporate's liquidity position during the loan repayment period rose. A comparison of the premiums on newly approved loans and the indicators of the financial position of the sector does not show this dependence in full, because loans are mostly approved for corporates with higher creditworthiness that to a greater or lesser extent stand above the average for the sector.

Figure 4.20: Average premium over the EURIBOR on new bank loans to corporates in relation to corporate financial indicators by sector



Sources: AJPES, Bank of Slovenia

In 2009 the banks set their highest premiums over the EURIBOR for corporates in the sectors of agriculture, forestry, fishing, mining and quarrying, which are notable for their average length of arrears of more than 90 days, while in terms of the proportion of liabilities more than 90 days in arrears and indebtedness they are lower-risk. The risk premiums were also higher for corporates in the construction sector, which are notable for their high indebtedness and the above-average proportion of longer arrears. Transportation and storage was notable in 2008 for its extremely low premiums, primarily as a result of certain larger loans. In 2009 the banks also set higher risk premiums for these corporates, which were highly indebted on average.

Table 4.12: Selected financial performance indicators by sector, and premiums over the EURIBOR on new loans at the domestic banks

	Debt ratio 2009	Financial leverage 2009	Liquidity ratio 2009	% more than 90 days in arrears dec. 09	Overall rank	Premium over EURIBOR 2009	Rank
Agriculture, forestry, fishing, mining, quarrying	46.6	101.1	79.8	5.5	3	3.5	12
Manufacturing	52.0	119.5	76.5	6.3	4	3.0	7
Electricity, gas, water; remediation	36.7	64.1	102.4	0.8	1	2.8	2
Construction	77.7	413.6	62.7	7.7	12	3.3	11
Wholesale and retail trade	62.2	173.8	65.9	5.1	6	3.0	6
Transportation and storage	81.4	479.7	73.3	1.9	9	3.2	10
Accommodation and food service activities	57.6	151.4	36.6	7.9	10	3.0	5
Information and communication activities	48.9	104.0	82.5	1.8	2	3.1	8
Financial and insurance activities	51.1	107.0	47.2	21.6	7	2.8	3
Real estate activities	73.1	290.5	51.1	4.8	10	2.8	4
Professional, scientific and technical activities	62.6	183.7	79.6	7.6	7	2.6	1
Public services	58.5	153.0	57.5	2.2	5	3.2	9
Overall	59.8	162.2	69.1	6.6		3.0	

Note: For the liquidity ratio, a higher ratio represents better liquidity, while for all the other indicators a higher value is less favourable. The overall ranking is calculated from the individual rankings for each indicator, where a higher ranking indicates higher risk. The premiums refer to those on long-term loans tied to the EURIBOR.

Sources: AJPES, Bank of Slovenia, own calculations

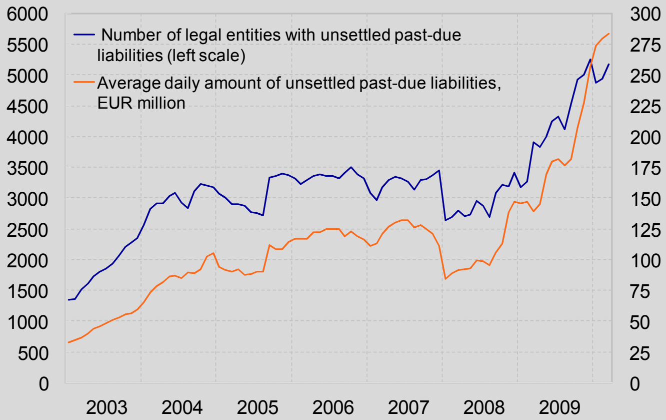
Box 4.1: Payment indiscipline

Slovenian corporates state that the key problems that they have faced in recent times are:
- a decline in orders, primarily at home, and to a lesser extent in the rest of the world;
- short loan maturities, and the provisions of sufficient loan collateral;
- payment indiscipline.

The vast majority of surveyed corporates (74%) state that the payment deadlines by which they are being paid by customers have been extended. They have been extended past the deadlines by which the corporates are paying their suppliers. The mismatch between the payment of claims and liabilities is thus increasing, which is reducing corporate liquidity.

Further evidence of the problem of payment indiscipline comes from the AJPES figures for unsettled past-due liabilities, although these only include the figures from court enforcement orders or from official tax debts, not the remaining unsettled liabilities from unpaid invoices between creditors and debtors. The number of legal entities with unsettled past-due liabilities almost doubled from its lowest point in August 2008 (2,693 legal entities) to reach 5,182 at the end of March 2010 (an increase of 92%). The average daily amount of unsettled past-due liabilities increased even more, rising by 198% over the same period.

Figure 4.21: Number of legal entities with unsettled past-due liabilities and average daily amount of unsettled past-due liabilities



Source: AJPES

The largest increases in the number of legal entities (53.8% in year-on-year terms) and in the average daily amount of unsettled past-due liabilities (74.3% in year-on-year terms) were recorded in 2009. The number of legal entities with unsettled liabilities began to decline in 2010, while the average daily amount of unsettled liabilities has continued to increase.

The worst situation is in the construction sector, which in 2009 recorded the largest increase in the number of legal entities and the average amount of unsettled liabilities. At the end of 2009 the average daily amount of unsettled past-due liabilities in the construction sector was almost three times higher than a year earlier. In 2010 the number of legal entities and the average daily amount of unsettled liabilities remained highest in the construction sector. In addition, in 2010 there was a significant increase in the average daily amount of unsettled liabilities in the manufacturing sector. However, this is likely to mostly comprise existing debtors, as the number of legal entities with unsettled past-due liabilities in the manufacturing sector remains at its level of the end of 2009.

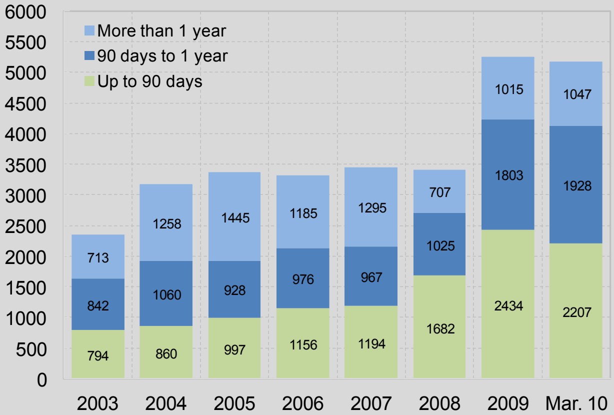
Table 4.13: Number of legal entities with unsettled past-due liabilities and average daily amount of unsettled past-due liabilities, total and largest sectors

	Number of legal entities			Average daily amount, EUR million		
	Dec. 08	Dec. 09	Mar. 10	Dec. 08	Dec. 09	Mar. 10
Total	3414	5252	5182	147.3	256.7	283.7
Construction	732	1288	1247	27.0	78.2	73.9
Financial and insurance activities	41	55	52	24.1	46.2	48.3
Manufacturing	431	662	674	18.5	28.9	44.9
Wholesale and retail trade	806	1083	1075	32.2	38.1	44.0
Professional, scientific and technical activities	354	537	539	17.6	20.8	21.5
Other	1050	1627	1595	27.9	44.5	51.1

Source: AJPES

The number of legal entities with unsettled past-due liabilities in an unbroken period of up to 1 year increased by 1,530 in 2009, in an approximately equal amount in the categories of unsettled liabilities in an unbroken period of up to 90 days, and those in an unbroken period of 90 days to 1 year. In the first three months of 2010 there was a notable increase in the number of legal entities with an unbroken period of unsettled past-due liabilities of 91 to 180 days.

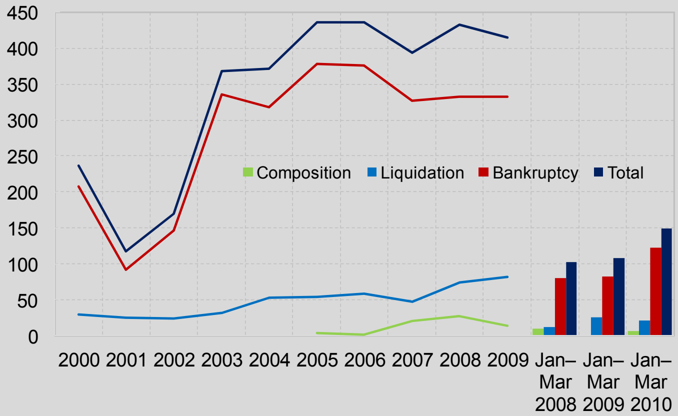
Figure 4.22: Number of bankruptcy, composition and liquidation proceedings initiated



Source: AJPES

An increase in the amount of unsettled liabilities and the lengthening of the period of illiquidity can make a corporate insolvent. Bankruptcy proceedings were initiated 332 times in 2009. The number was at the same level as the previous two years. The number of liquidations initiated increased considerably over the last two years. The were 82 liquidation proceedings initiated in 2009, compared with just 47 in 2007. A feature of the early months of 2010 was the rapid increase in the number of bankruptcies. During the first quarter of 2010 there were 122 bankruptcy proceedings initiated, equivalent to 37% of the total during the whole of 2009.

Figure 4.23: Number of legal entities according to the unbroken period of unsettled past-due liabilities



Source: AJPES

Further evidence of declining payments comes from the figures for the number and value of transactions in the SEPA ICT system, which is the main system for settling retail payments, which mostly involve payments between bank clients. The value of transactions reached EUR 44.9 billion in 2009, down 8.6% on 2008. The number of transactions in 2009 was also down, by 1.4%. However, the decline in the number and value of transactions is primarily a reflection of the decline in economic activity, and only to a lesser extent or indirectly is it an indication of lower payments because of payment indiscipline.

Table 4.14: Number and value of transactions in the Giro Clearing / SEPA ICT system

	2003	2004	2005	2006	2007	2008	2009	Q1 2009	Q1 2010
Value, EUR billion	18.8	20.2	21.0	22.9	45.7	49.1	44.9	10.8	10.5
Year-on-year growth, %	1.0	7.5	3.8	9.3	99.3	7.5	-8.6	-5.9	-2.2
Number of transactions, million	46.6	48.6	49.4	52.1	53.6	55.9	55.1	13.2	13.3
Year-on-year growth, %	-7.7	4.3	1.7	5.4	2.9	4.3	-1.4	-0.3	0.5

Source: Bank of Slovenia

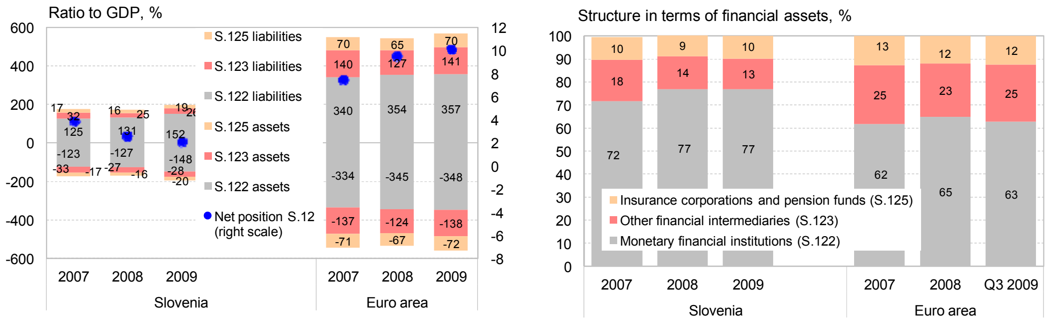
5 FINANCIAL SYSTEM

5.1 Structure of the financial system

The relative size of the financial system increased to 199% of GDP last year.

As a result of the decline in GDP and the growth in the total assets of monetary financial institutions, the ratio of the financial system (excluding the central bank) to GDP increased by 26 percentage points in 2009 to 199% of GDP,[16] equivalent to 35% of the depth of the financial system in the euro area overall.[17]

Figure 5.1: Ratio of financial assets, liabilities and net position to GDP by financial sub-sector (left) and structure of the financial sector in terms of financial assets (right) in percentages



Note: Excludes the central bank. S.122: Other monetary financial institutions (includes commercial banks and savings banks); S.123: Other financial intermediaries, except insurance corporations and pension funds (includes investment funds and leasing companies); S.125: Insurance corporations and pension funds.

Sources: Bank of Slovenia, ECB, Eurostat, SORS

The most notable feature of the breakdown of financial assets in Slovenia between 2007 and 2009 is the increase in the proportion accounted for by monetary financial institutions and the simultaneous decline in the proportion accounted for by other financial intermediaries. The importance of monetary financial institutions has increased sharply over the last two years, their total assets increasing by EUR 9.2 billion. The total assets of non-monetary financial institutions at the end of 2009 were still down almost EUR 360 million on two years earlier. Other financial intermediaries were hit strongly by movements on the capital markets in 2008, although the easing of the situation last year has been reflected in a stabilisation of the structure.

Table 5.1: Overview of the Slovenian financial sector in terms of total assets

	Assets, EUR million		Structure, %		As % GDP		No. of institutions	
	2008	2009	2008	2009	2008	2009	2008	2009
Monetary financial institutions¹	47,948	51,824	76.3	76.4	129.1	148.5	24	25
NMFIs	14,925	16,030	23.7	23.6	40.2	45.9		
insurers²	5,151	5,680	8.2	8.4	13.9	16.3	17	17
pension companies/funds³	1,041	1,296	1.7	1.9	2.8	3.7	10	10
investment funds	1,912	2,234	3.0	3.3	5.1	6.4	131	132
leasing companies⁴, ⁵	6,144	6,144	9.8	9.1	16.5	17.6	22	21
BHs, MCs, others⁵	676	676	1.1	1.0	1.8	1.9	-	-
Total	62,872	67,854	100.0	100.0	169.3	194.5	-	-

Notes: Figures for financial institutions that are not banks, insurers, pension companies or pension and investment funds are obtained from the AJPES database of annual accounts based on the SKD 2008 classification.
[1] Monetary financial institutions do not include the central bank.
[2] The latest figure for the total assets of reinsurance companies is for the end of the third quarter of 2009.
[3] The First Pension Fund is included among pension funds.
[4] Total assets in 2009 according to the figures for the end of 2008.

Sources: Bank of Slovenia, ISA, SMA, AJPES

[16] Owing to revisions to financial accounts figures, GDP and figures for the performance of financial institutions, the values in this section may differ from those previously published.
[17] The figure is not comparable with the figures published in the past because of the ECB's switch to publishing unconsolidated figures instead of consolidated figures.

Last year's growth in the total assets of monetary financial institutions was lower than in 2008, but higher than the growth in the total assets of non-monetary financial institutions. Among the non-monetary financial institutions, the renewed positive growth in investment funds is important from the point of view of financial stability. Although investment funds only replaced just over 14% of their large decline in total assets recorded in 2008, together with the increased rate of growth at insurers and pension companies and funds this indicates that the pressure exerted by the crisis on this part of the financial system eased last year.

The increase in the total assets of pension funds was considerable in 2009. Growth in the pension funds is nevertheless too low given the demographic developments. Low returns mean that supplementary pension insurance is not competitive against other forms of investment.

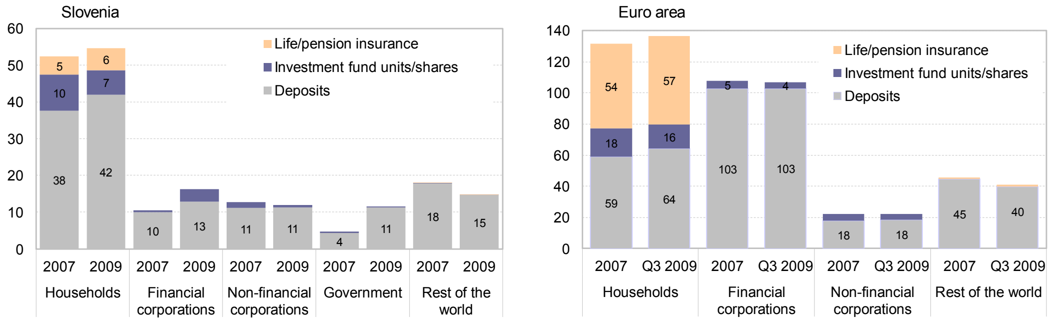
Comparison of financial institutions in terms of intermediation of savings

The lack of development of pension-based saving is strongly exposing households to the consequences of adverse demographic developments.

The breakdown of household financial assets reflects the relative lack of development of pension-based saving and the investment of savings in life insurance instruments. During the financial turmoil the household sector increased the proportion of its total assets held in bank deposits, given the negative experiences from investing in the capital markets and the unlimited government guarantee for deposits. That the value of the household sector's financial assets held in the form of life insurance and pension insurance in Slovenia is just 6% of GDP or just 8% of total financial assets is of concern from the point of view of demographic developments and in comparison with the euro area, where the household sector holds almost 29% of its financial assets in the form of life insurance and pension insurance.

The changes in the breakdown of the government sector's financial assets in Slovenia are a reflection of the issuance of government securities. After issuing bonds the government placed a portion of the proceeds in bank deposits, thereby assisting banks in the relatively rapid process of restructuring their funding while making net repayments of liabilities to foreign banks. With the repayment of debts to banks in the rest of the world, the value of deposits by the rest of the world declined by 3% of GDP over the last two years.

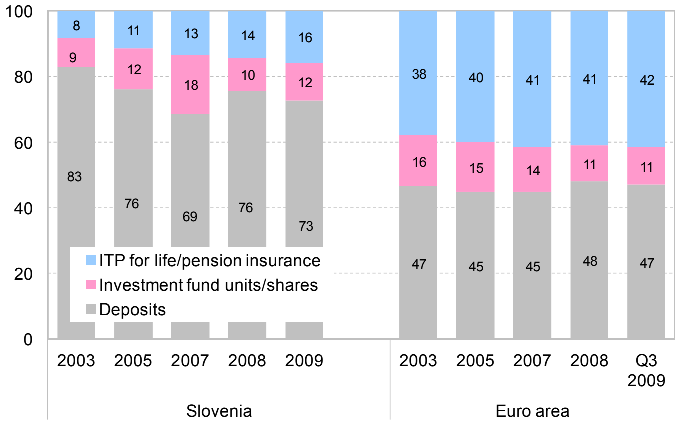
Figure 5.2: Value of financial assets by instrument owned by individual sectors as a percentage of GDP in Slovenia (left) and the euro area (right)



Note: The central bank is not included in the figures for Slovenia, and only sector S.14 is included.
Sources: Bank of Slovenia, ECB, Eurostat, SORS

The proportion of household financial assets in Slovenia accounted for by insurance technical provisions for life insurance and pension insurance has doubled since 2003, but the gap with the euro area remains considerable. The rapid increase in the proportion of financial assets held in the form of shares and investment funds before the reversal on the capital markets was the result of rapid growth in prices and investments. The virtual halving of the proportion in 2008 is a reflection of capital losses. The reversal on the markets in the spring of 2009 was a positive change in the direction of the better-balanced breakdown of household financial assets seen in the euro area.

Figure 5.3: Breakdown of households' financial assets from intermediation in Slovenia and the euro area in percentages



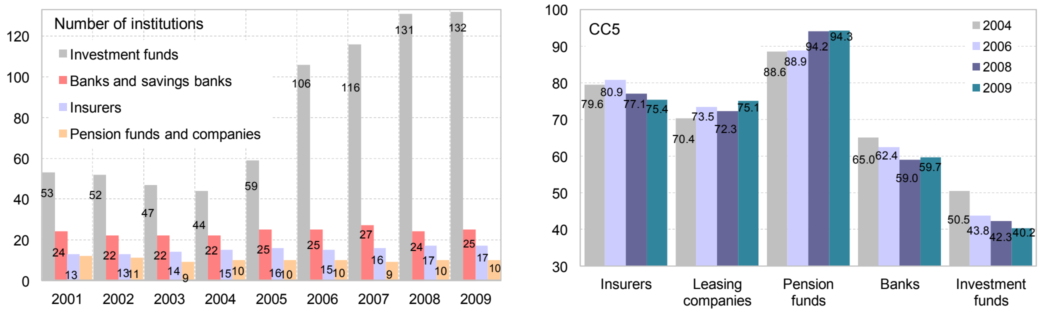
Note: Transferable and other deposits are included among the euro area figure for deposits.
Sources: Bank of Slovenia, ECB

Market concentration in the financial sector

Ownership consolidation proceeded between brokerage houses, but not between banks.

There was almost no change in the number of financial institutions in Slovenia last year. Market concentration stagnated or declined for three of the five categories of financial institution. Given the prevalent role of the banking sector in the financial system, the end of the fall in concentration in banking is not a positive development. At the same time it is the result of changes in the rates of growth at individual banks, and not consolidation between the largest banks. This process in the banking system was not encouraged either by last year's halving of the banking system's profits, or the continuing increase in impairments and provisioning in early 2010. The reasons were the banks' stable solvency, the successful curbs on growth in operating costs, and the lack of a feeling among bank owners that consolidation would make their business more efficient, in the context of the continuing profit-making. The decline in bank profits could increase their owners' motivation to decide themselves in favour of ownership consolidation, or the poor bank performance could force them into it. The portion of the financial system that was primarily hit by the developments on the capital markets in 2008 began making adjustments in this way last year. The three largest brokerage houses announced a merger in July, which went through in March 2010.

Figure 5.4: Number of financial institutions of different type (left), and market concentration of the five largest (CC5; right, in percentages)



Note: The CC5 index is calculated in terms of total assets, with the exception of leasing companies, for which it is calculated in terms of volume of business (transactions concluded). Insurers includes two reinsurance companies, whose total assets relate to the end of the third quarter of 2009. Pension funds does not include the First Pension Fund, as this is a closed fund that does not envisage any more contributions.
Sources: Bank of Slovenia, ISA, SMA, BAS, SLA

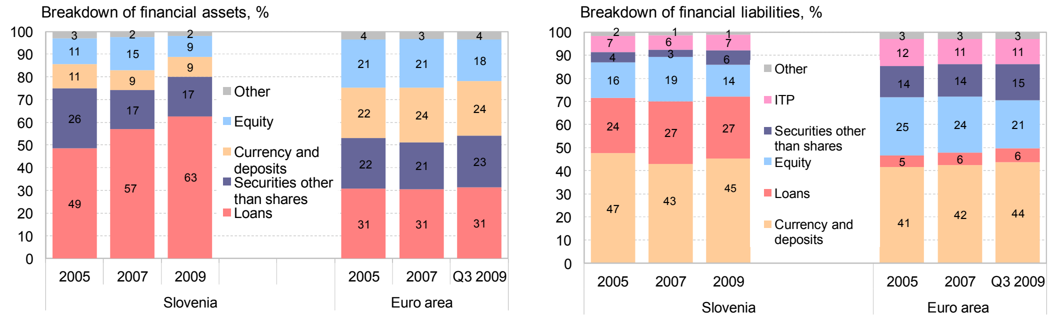
Concentration in the insurance sector is gradually declining for the third consecutive year. The potential adverse impact on the banking sector of possible problems in the insurance sector is limited by the banking system's relatively low level of exposure to insurers. The long years for which a small number of insurers have been established on the Slovenian market, the competitiveness of their services, and the well-developed business network and ownership structure of the largest insurer[18] are all slowing the process of deconcentration more than in the banking sector. The stagnation in concentration among pension funds remains at a high level, and is merely a reflection of the insufficient level of development in this part of the financial services market.

Comparison of the breakdown of the financial sector's financial assets and liabilities with the euro area

The proportion of the Slovenian financial sector's financial assets accounted for by loans is increasing, but in the euro area overall there is no change in the breakdown.

The fundamental difference between the breakdown of the financial assets of the Slovenian financial sector and that of the euro area financial sector is the increase in the proportion accounted for by loans at the expense of other types of financial asset. The change represents a return to the traditional behaviour of financial intermediaries, while the sharp decline in the proportion accounted for by equity is not encouraging the development of the capital market and the integration of the financial sector. Despite the crisis, there was no significant change in the breakdown of the financial assets of the euro area financial sector. The proportion accounted for by forms of financial assets other than loans remains around 70%, but fell below 40% in Slovenia.

Figure 5.5: Breakdown of the financial sector's financial assets (left) and liabilities (right) in percentages



Note: Excludes the central bank.
Sources: Bank of Slovenia, ECB

The breakdown of the financial sector's financial liabilities in Slovenia and in the euro area was relatively stable. The decline in the proportion accounted for by equity during the crisis is an indication of the Slovenian financial sector's relatively larger exposure to capital losses compared with the euro area financial sector. This change has been seen throughout the euro area since 2007, but in Slovenia it could act more adversely, as the proportion of the financial sector's liabilities accounted for by equity is a third lower than that of the euro area overall.

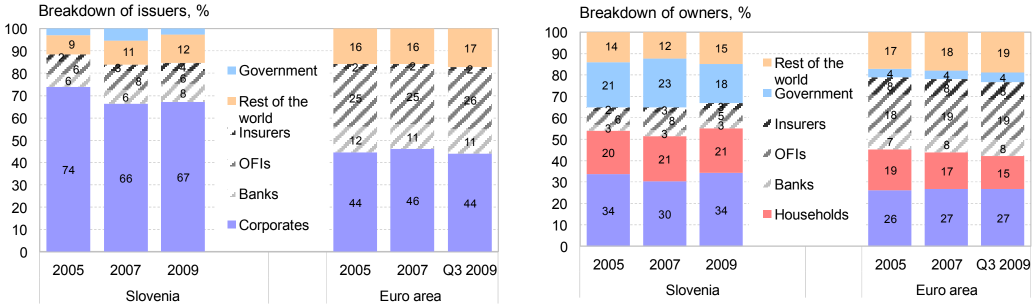
The low proportion of issuers' capital accounted for by banks means their greater dependence on other funding.

The breakdown of the issuers of equity in Slovenia had stabilised before the outbreak of the crisis, and remained almost unchanged until last year. Two-thirds of equity pertains to the corporate sector. Financial institutions remain very restrained issuers of equity, accounting for just 18%. The effect is negative because of the maintenance of the financial institutions' relatively high dependence on other resources, while it is also not encouraging the development of an already-shallow capital market. The proportion accounted for by the government, government-owned corporates and quasi-governmental funds as issuers of equity in Slovenia declined last year to the level seen in 2005, although even this is unusual compared with the euro area.

In the breakdown of owners of equity, the government sector is also notable in Slovenia compared with the euro area overall, despite the decline in its proportion during the last two years as a result of the decline in capital investments. The level of cross-ownership integration of financial institutions is significantly weaker in Slovenia than in the euro area overall. The low and stagnating proportion accounted for by financial institutions is in accordance with the relatively low sophistication of the capital market.

[18] The Pension and Disability Insurance Institute and the Slovenian Indemnity Corporation held 62.6% of the equity of Zavarovalnica Triglav d.d. in the middle of 2009.

Figure 5.6: Breakdown of equity issuers (left) and owners (right) in percentages



Note: Equity: instrument F.5 (shares and other equity) under the ESA 95 definition. It includes issued share capital, units in investment funds and ownership in other corporate forms such as limited liability companies and unlimited partnerships. At the end of 2009 issued share capital (irrespective of whether listed on a stock exchange) accounted for 47.9% of total equity.

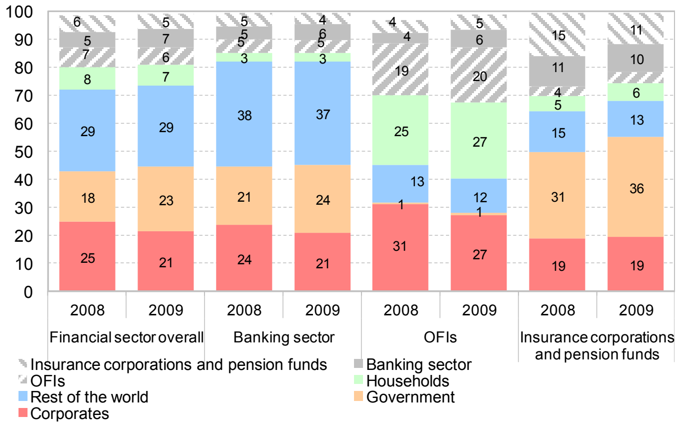
Sources: Bank of Slovenia, ECB

Capital links in the financial sector

Cross-ownership in the financial sector is not increasing.

Cross-ownership between domestic financial institutions is low at 18%, and was unchanged during 2009. Capital links are a relatively limited channel for the possible transfer of risks in the financial system. One change seen last year was the increase in the proportion of government ownership. In the banking sector the capital increase at SID banka was a factor in this. From the point of view of capital links, the process of integrating the financial system into the international economic environment was unchanged last year, the rest of the world's proportion remaining at 29%.

Figure 5.7: Ownership structure of financial sectors in percentages



Note: Includes direct ownership only.

Sources: CSCC, own calculations

Risk in the financial system

The banks' investment exposure to other financial intermediaries is relatively low.

The decline in economic growth in 2009 increased caution in decision-making, and delayed decisions regarding investments in the corporate sector and purchases by the household sector. The situation on the real estate market acted to further discourage the latter. The excess supply and the related expectations of price falls on the real estate market sharply reduced the number of transactions. The household sector nevertheless maintained a solid level of creditworthy demand at the banks, while the gap between demand and creditworthy corporate demand widened. A portion of the risks realised in the corporate sector began to be transferred to the banks via increased financial indiscipline and low demand. The banks restricted the transfer of risks to their own balance sheets by restricting corporate lending, particularly the banks under majority foreign ownership. Certain domestic banks restricted the take-up of risks by transferring a portion of the credit risk to the government by participating in the guarantee scheme for corporates.

The banks' exposure to other financial intermediaries was just 4.6% of the banking system's total financial assets at the end of 2009, lower than in 2007. When the relative exposure to insurance corporations and pension funds is also taken into consideration, the banking system's exposure to investment risk in the non-banking financial sector is relatively limited. Given the prevalence of loans, it is concentrated primarily in form of credit risk.

Table 5.2: Investment links between Slovenian financial institutions

	2005	2007	2008	2009		2005	2007	2008	2009
	Domestic banks' exposure to[1]								
	other fin. intermediaries (S.123)					insurance cor. & PFs (S.125)			
Value, EUR million	867	2,124	2,502	2,459		57	94	166	158
bank investments in debt securities[3]	2	0	0	0		14	14	19	15
bank loans granted	685	1,840	2,328	2,234		0	0	54	27
bank capital investments	180	284	174	225		42	79	94	116
As % of:									
total bank financial assets	2.9	4.9	5.1	4.6	5.1	0.2	0.2	0.3	0.3
bank investments in debt securities	0.0	0.0	0.0	0.0	0.1	0.2	0.2	0.3	0.2
bank loans granted	4.1	6.1	6.4	5.9	6.4	0.0	0.0	0.1	0.1
bank capital investments	15.3	15.9	11.0	12.0	12.9	3.6	4.5	5.9	6.2
	Exposure to domestic banks of[2]								
	other fin. intermediaries (S.123)					insurance cor. & PFs (S.125)			
Value, EUR million	590	930	603	581		816	983	1,288	1,433
investments in bank deposits	408	602	321	318		384	495	687	732
investments in bank debt securities	132	132	105	73		359	383	421	530
investments in bank capital	51	196	178	191		72	106	181	171
As % of:									
total financial assets of S.123 / S.125	8.7	8.3	6.6	6.3		20.9	16.5	21.8	21.4
investments in bank deposits	93.8	99.1	98.2	98.2		99.4	93.6	98.0	99.1
investments in debt securities	28.6	37.2	38.9	29.9		15.1	12.2	12.9	14.3
capital investments	1.8	3.7	6.2	6.5		9.7	5.8	12.9	10.5

Notes: The table shows the investment links between the banking sector, and both the sector of other financial intermediaries (including investment funds and leasing companies) and the sector of insurance corporations and pension funds.
[1] Investments by domestic banks in the other two sectors, via equity, debt securities and loans granted. The proportion of total bank financial assets accounted for by the aforementioned investments, and the ratio of exposure to the two aforementioned sectors via a particular instrument to the total value of the instrument are illustrated.
[2] Investments by other financial intermediaries and insurers in bank equity, debt securities and deposits. The proportion of the total assets of these two sectors accounted for by these investments and the proportion of exposure to banks via a particular instrument are also given.
[3] Debt securities.
Sources: Bank of Slovenia, SORS

Insurance corporations and pension funds hold more than a fifth of their investments at banks.

In contrast to the banks' low exposure to non-banking financial institutions, insurance corporations and pension funds are more exposed to banks. The transfer of risks from the banking system to this sector can be considerable, as their investments of EUR 1,433 million at the banks accounted for just over a fifth of their financial assets at the end of 2009. Deposits at banks are prevalent in the heterogeneous investment structure. Given the banks' increased need for funding of longer maturity because of the anticipated decline in government deposits and Eurosystem funding, an increase in pension saving would also be a positive development from the point of view of bank funding. Compared with 2007 and 2008, insurance corporations and pension funds recorded a sharper increase last year in their investments in bank debt securities. Should pension saving increase, this positive change could help the banks in attracting the necessary funding, and ease their acquisition of additional own funds.

5.2 Domestic financial markets

5.2.1 Money market

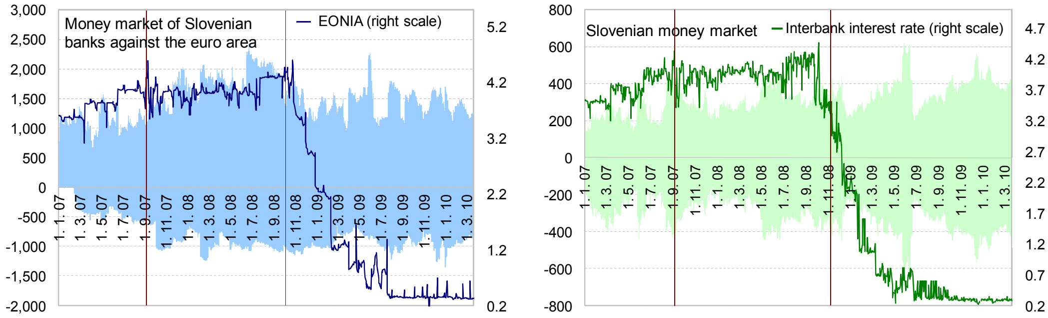
High surplus liquidity was a feature of the euro area money market in 2009.

The situation on the euro area money market improved in 2009. By providing unlimited liquidity at a fixed interest rate, the ECB continued to supplement the role of the money market in 2009 in reallocating liquidity between banks. Last year the ECB's low interest rate and the surplus liquidity reduced the market interest rates to historical lows. The surplus liquidity was reflected in a low EONIA, which fell below the ECB key interest rate, and in the use of the marginal deposit facility at the ECB. Volume on the Slovenian interbank market declined last year, and the average maturity of the transactions lengthened.

A sharp fall in interest rates in 2009.

The EONIA and the SI/ON fell sharply last year. The fall in the two interest rates matched and coincided with the fall in the ECB's interest rates. The levels of the SI/ON and the interbank interest rates on the Slovenian money market were lower than the EONIA again last year. The latter averaged 0.71% in 2009, compared with an average of 0.58% for the SI/ON and an average of 0.62% for the interbank interest rates on the Slovenian money market.

Figure 5.8: Stock of unsecured deposits of Slovenian banks placed and received on the euro area money market (left) and the Slovenian money market (right) in EUR million, and movement of the EONIA and the interbank interest rate on the Slovenian money market in percentages



Source: Bank of Slovenia

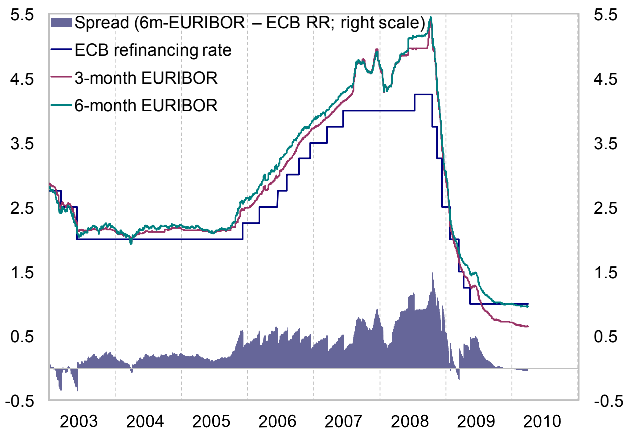
Slovenian banks' net claims against the rest of the world on the international market for unsecured interbank deposits declined last year.

Slovenian banks have been net creditors of the rest of the world on the euro area money market for unsecured interbank loans since Slovenia introduced the euro, but their net claims against the rest of the world declined in 2009 and 2010. Volume on the interbank deposit market was down by just under a half last year, although Slovenian banks remained net lenders to the rest of the world in 2009 in the amount of EUR 516 million (compared with EUR 748 million in 2008).

A decline in volume on the Slovenian interbank market, and lengthening of maturities of loans between banks in Slovenia.

Last year the banks traded with a slightly longer average loan maturity than in the previous year, the average maturity having lengthened by 8 days. The average weighted loan maturity was 18 days. The maturities of loans between Slovenian banks or from Slovenian banks to foreign banks were shorter than the maturities of loans received from foreign banks, having averaged 16 days and 14 days respectively. The proportion of the interbank deposit market accounted for by overnight deposits halved from 60% in 2008 to 34% last year. The proportion of the total volume on the money market accounted for by transactions between banks in Slovenia increased by 8 percentage points in 2009 to 30%, an indication that in Slovenia too the banks are trading more within national boundaries.

Figure 5.9: Comparison of the EURIBOR market rate with the ECB refinancing rate in percentages

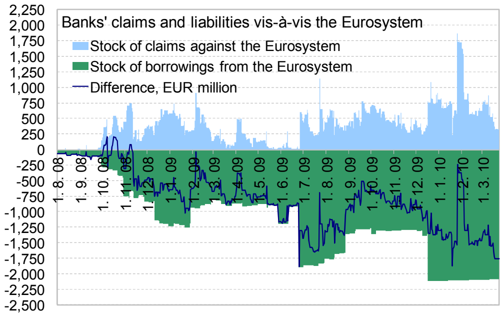


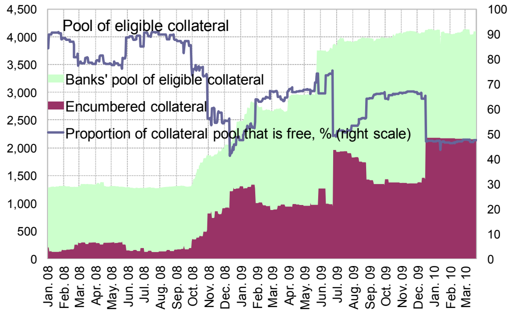
Source: Bank of Slovenia

Interest rates on the financial markets began falling in November and December 2008, simultaneously with the cuts in the ECB's interest rates. After the outbreak of the financial turmoil and several cuts in the ECB's key interest rate, the spread between the EURIBOR and the ECB's key interest rate declined sharply. The spread between the 6-month EURIBOR and the ECB interest rate has even been negative since last November.

The EURIBORs have been slightly below the ECB's key interest rate since November 2009.

Figure 5.10: Commercial banks' claims, liabilities and net position vis-à-vis the Eurosystem in EUR millions (left), and pool of eligible collateral at the Eurosystem in EUR millions (right)





Source: Bank of Slovenia

By the autumn of 2008 the banks had begun simultaneously increasing their borrowing from the Eurosystem and the pool of eligible collateral for Eurosystem operations. This comprises securities and loans banks can pledge as collateral for liabilities to the Eurosystem. The size of the pool had reached EUR 2.5 billion by the end of 2008, and EUR 3.8 billion by the end of June 2009, when the ECB conducted its first 12-month longer-term refinancing operations. By October 2009 the pool had increased to more than EUR 4 billion, and it remained at this level in the first quarter of 2010.

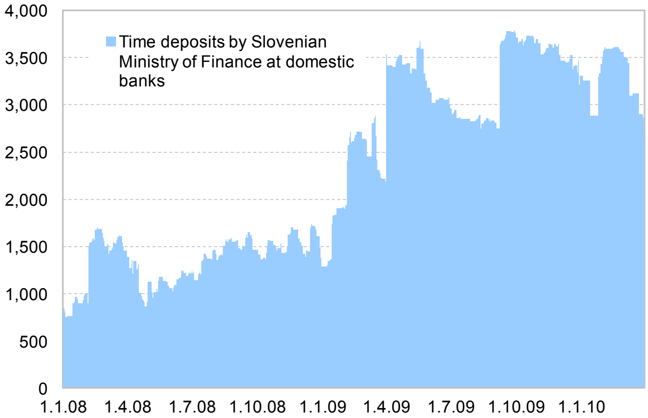
The pool of eligible collateral for Eurosystem operations increased in size in 2009.

The proportion of the pool of eligible collateral for Eurosystem operations that is free stood at a relatively high 62% last year. After the third and final 12-month LTRO at the ECB the proportion of the pool of eligible collateral that is free fell below a half. The banks' borrowings from the Eurosystem on this account rose to EUR 2.1 billion.

The Ministry of Finance held several auctions for short-term deposits of government money at banks during 2009. At EUR 3.5 billion, the average stock of the Ministry of Finance's deposits at the banks was significantly in excess of the stock of deposits in 2008, when the average amount stood at EUR 1.4 billion.

The average stock of government deposits at banks in 2009 was 2.5 times that in 2008.

Figure 5.11: Stock of short-term deposits by the Slovenian Ministry of Finance at banks in EUR million



Source: Bank of Slovenia

5.2.2 Capital market

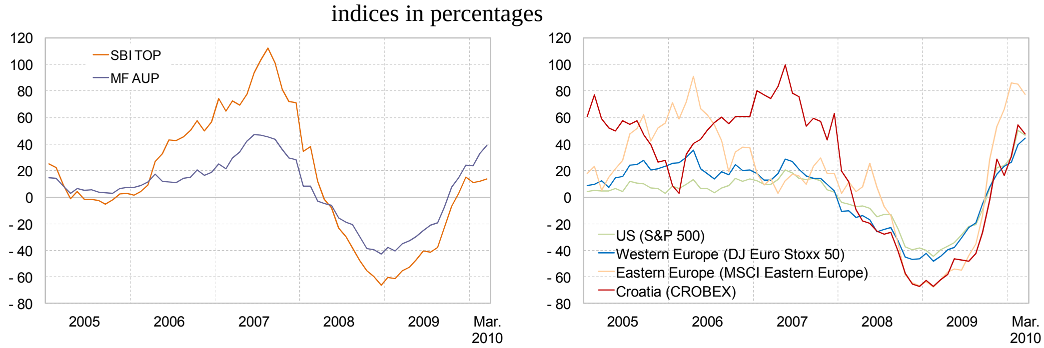
The Ljubljana Stock Exchange's SBI TOP ended 2009 up 15.0% on a year earlier. The index rose steeply between March and June, but then stagnated and even fell slightly until March 2010. There was similar movement in the overall index for Ljubljana Stock

The SBI TOP rose by 15.0% in 2009.

Exchange shares, the LJSEX,[19] which rose by 10.4% in 2009. This volatility is primarily a reflection of the uncertain economic situation.

The majority of global market indices rose from March 2009 until February's temporary downward correction. The American S&P 500 rose by 23.5%, and the European DJ EuroStoxx 50 by 23.3% in 2009. Investors also demonstrated a renewed appetite for risk, the indices of the less-developed markets rising sharply in 2009 (the MSCI Eastern Europe rose by 66.2%, while the Chinese Hang Seng rose by 82.7%). The movements were not as pronounced on less-liquid markets (Croatia's CROBEX rose by 16.4% in 2009, while Serbia's BELEX 15 rose by 17.4%). The Slovenian capital market also belongs to the group of illiquid markets.

Figure 5.12: Annual growth in domestic (left) and foreign (right) stock exchange indices in percentages



Sources: LJSE, Bloomberg

The P/E[20] ratios for shares on the Ljubljana Stock Exchange, which in 2007 were significantly higher than the similar indicators for leading global indices, have gradually declined over the last two years. They were more moderate at the end of 2009, but still higher than the values for leading global indices. This means that Slovenian shares were relatively more expensive, and thus less attractive to investors.

Table 5.3: P/E ratios for the Ljubljana Stock Exchange's prime market and standard market, and selected global indices

	LJSE Prime	LJSE Standard	DJ EURO STOXX 50	S&P 500	DAX	MSCI EM EASTERN EUROPE
Dec 06	28.5	23.5	12.6	17.7	14.5	12.0
Dec 07	33.8	32.6	12.2	17.3	13.7	12.6
Dec 08	10.6	8.3	9.2	13.6	10.4	3.7
Dec 09	19.4	23.0	16.5	18.0	60.2	16.0
Mar 10	19.8	37.1	15.4	18.7	21.6	15.8

Sources: LJSE, Bloomberg

The market capitalisation of bonds on the Ljubljana Stock Exchange increased by 60.7% in 2009, while the market capitalisation of shares remained unchanged.

The market capitalisation of shares[21] on the Ljubljana Stock Exchange remained at the same level as at the end of 2008, despite the rise in its indices at the end of 2009. Several securities were delisted in 2009, the corporates in question having cut costs at all levels. Shares in eight corporates were removed from trading and listing in 2009 (of which MIP and Infond Holding were delisted because bankruptcy proceedings were initiated, and the others because of a delisting resolution passed by the general meeting). The turnover ratio nevertheless increased as a result of the delisting of predominantly illiquid shares. The volume of trading was again low in 2009: it averaged EUR 60.0 million each month, down 24.4% on 2008.

An improvement in the turnover ratio for equities.

The market capitalisation of bonds rose by 60.2% in 2009, primarily as a result of new issues of government bonds. The issues of RS64, RS65 and RS66 bonds with a total nominal value of EUR 4 billion alone accounted for 37.9% of the total market capitalisation of bonds at the end of 2009. There was no proportionately large increase in the volume of trading on the Ljubljana Stock Exchange, as the majority of trading in these

[19] In March the Ljubljana Stock Exchange changed the names of its indices and their methodology of calculation. The SBI 20 was renamed the LJSE Composite (LJSEX), becoming an index for the entire share market at the Ljubljana Stock Exchange, while the SBI TOP remains the Ljubljana Stock Exchange's blue-chip index, and is also used as the benchmark index.
[20] The P/E ratio is the ratio of the share price to the most recent annual net earnings per share.
[21] Investment company shares are not included in the values of the market capitalisation of shares or the volume of trading in shares.

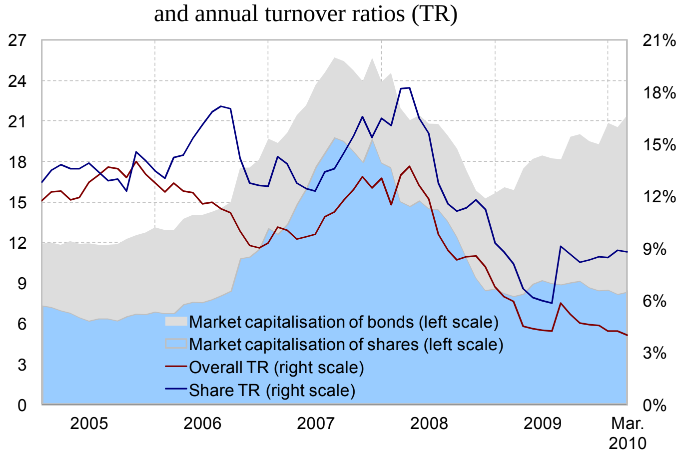
securities were conducted outside of the exchange's regulated market (via the MTS Slovenia system). The volume of trading in bonds was again low in 2009. The average monthly volume was EUR 13.0 million, down 39.2% on 2008. The heaviest volume was recorded in the months when the RS64 and RS65 bonds were issued.

Table 5.4: Overview of Slovenia's regulated capital market

	2005	2006	2007	2008	2009	Mar. 2010
			Shares			
Market capitalisation						
amount, EUR billion	6.7	11.5	19.7	8.5	8.5	8.4
as % GDP	24.2	38.7	58.7	22.8	24.2	23.9
annual growth, %	-5.9	72.0	71.5	-57.1	-0.1	-1.3
% held non-residents	3.3	4.8	5.9	7.1	7.2	9.0
Volume						
amount, EUR billion	0.94	1.45	3.03	0.95	0.72	0.04
as % GDP	3.4	4.9	9.0	2.6	2.1	0.1
annual growth, %	1.0	54.3	109.1	-68.6	-24.4	-93.8
Annual growth in SBI TOP, %	2.8	56.6	71.0	-66.1	15.0	13.6
P/E (prime)	21.3	28.5	33.8	10.6	19.4	19.8
Dividend return (prime), %	1.4	1.2	1.0	3.9	2.1	2.0
			Bonds			
Market capitalisation						
amount, EUR billion	6.0	6.6	5.9	6.8	10.8	13.1
as % GDP	21.9	22.3	17.6	18.3	30.9	37.4
annual growth, %	31.0	9.6	-10.5	14.5	59.2	20.8
Volume						
amount, EUR billion	0.75	0.19	0.17	0.26	0.16	0.02
as % GDP	2.7	0.6	0.5	0.7	0.4	0.1
annual growth, %	58.1	-74.9	-11.8	54.9	-39.2	-87.5

Note: Excludes listed investment companies and mutual funds. The volume includes block trades.
Sources: LJSE, SORS

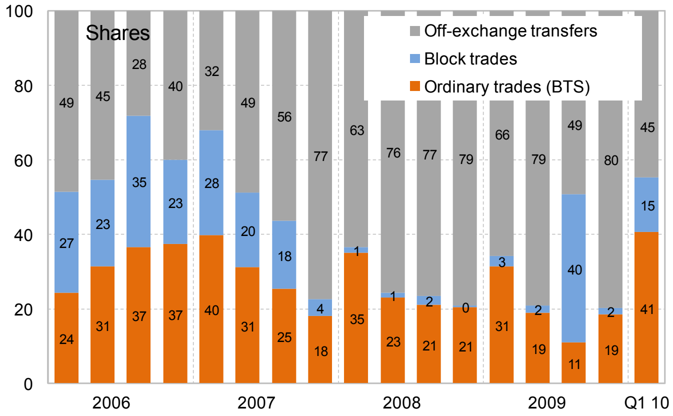
Figure 5.13: Market capitalisation on the Ljubljana Stock Exchange in EUR billion, and annual turnover ratios (TR)



Note: Excludes listed investment companies and mutual funds. The turnover ratio (TR) is the ratio of annual volume to market capitalisation at the end of the year. The volume includes block trades.
Source: LJSE

While on more sophisticated markets there was a trend during the crisis of investors migrating from off-exchange markets to regulated markets, in Slovenia there was no such trend. Of the total volume of trading in securities listed on the Ljubljana Stock Exchange, 93.2% was conducted outside the regulated market in 2009. The figure was 81.6% in 2008, and 59.8% in 2007. The majority of off-exchange trading in bonds was conducted in government bonds via the MTS Slovenia system. The ratio of off-exchange transfers of shares to exchange transactions (ordinary trades and block trades) remains relatively high. It stood at 67.2% in 2009, down 7.9 percentage points on 2008, but nevertheless up 5.8 percentage points on 2007.There were no major changes of ownership of shares in the prime market or standard market.

Figure 5.14: Breakdown of trading in shares listed on the Ljubljana Stock Exchange by transaction type



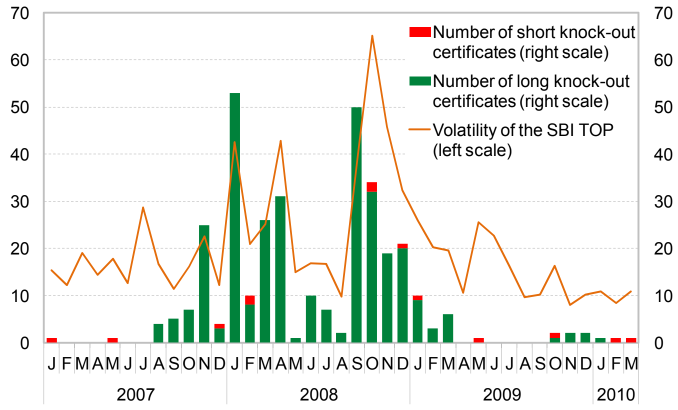
Source: LJSE

Foreign banks' retail certificates on Slovenian corporate shares

The majority of retail certificates issued by foreign banks on shares in Slovenian corporates expired prematurely between the outbreak of the crisis in August 2007 and March 2009.

Trading in foreign banks' retail certificates on shares in Slovenian corporates was a major factor in the movement of prices on the Slovenian capital market in previous years. The low liquidity of the market and the falling prices in the period to March 2009 led to the majority of these instruments reaching the knock-out barrier, and also to extra caution on the part of issuers in issuing such products and on the part of investors in purchasing them. Another major factor was the entry into force of the Gains on the Disposal of Derivative Financial Instruments Act in July 2008, which further reduced the liquidity of the Slovenian capital market.

Figure 5.15: Number of expiring knock-out certificates issued on Slovenian shares or indices incorporating Slovenian shares, and volatility of the SBI TOP



Note: The volatility of the index is calculated as the standard deviation in the daily percentage changes in the closing values of the index in a month multiplied by the square root of the number of trading days in a year (WFE and FESE reporting methodology).
Sources: LJSE, FESE, Boerse Stuttgart

Because the majority of retail certificates issued on Slovenian shares were long, the largest proportion expired between the outbreak of the crisis in August 2007 and March 2009. The stock of short retail certificates issued on shares in Slovenian corporates is presently still low, as a result of the lack of eligible hedging instruments. The stock of long retail certificates, both investment certificates and leverage certificates, declined sharply as a result of ordinary expiry and knock-outs. There were no large-scale replacements of expired certificates with new issues.

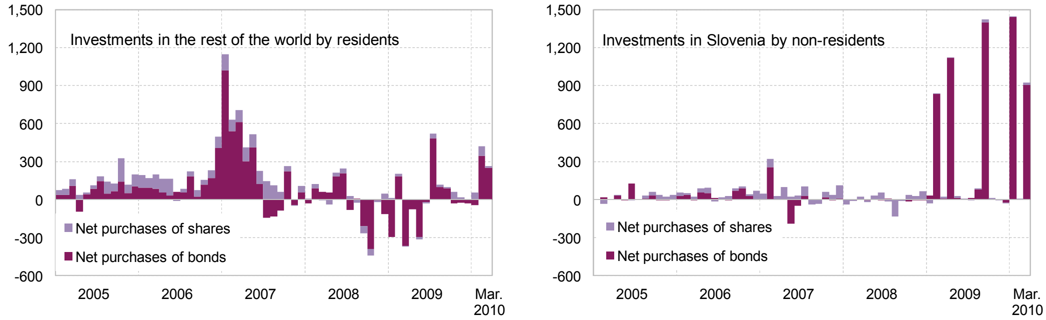
The correlation coefficient between the number of retail certificates reaching the knock-out barrier and the volatility of the SBI TOP between 2007 and 2009 was 0.77. It is more common for certificates to reach the knock-out barrier during a period of high volatility, as it is harder for the issuer to set a knock-out barrier that the price will not exceed in such conditions. However, the expiry of the certificate alone and the consequent closure of the issuer's position in a situation of low liquidity also causes an additional increase in price volatility.

Investment links with the rest of the world

Increased demand for Slovenian debt securities from non-residents.

Non-residents' investments in Slovenian securities in 2009 increased significantly on 2008. Non-residents' net purchases of shares in Slovenian issuers were up 24.0% on 2008 at EUR 31.0 million. However, this was down 84.1% on the net purchases made in the period before the sharp growth in prices in 2002 to 2005. Non-residents' net purchases of Slovenian bonds also increased sharply: last year's net purchases of EUR 3,403.6 million were almost three times those in 2008.

Figure 5.16: Monthly net investments by residents in the rest of the world (left) and by non-residents in Slovenia (right) in EUR million

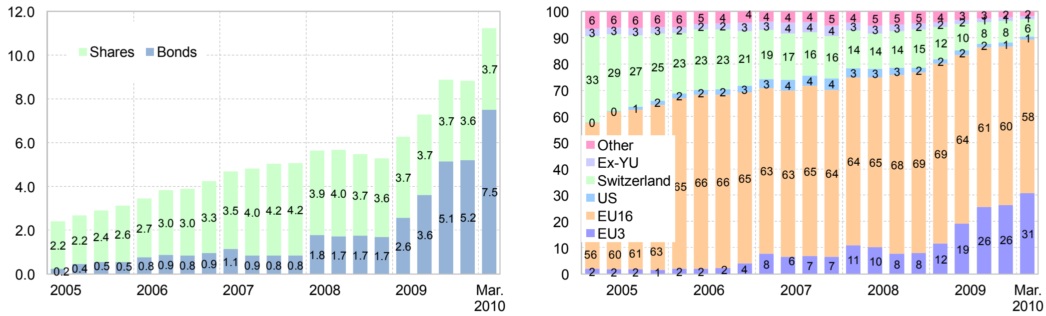


Note: The RS63 government bond issued on the MTS Slovenia system is not included among the net purchases of bonds made by non-residents in 2008.
Sources: CSCC, Bank of Slovenia, own calculations

RS64, RS65, RS66 and RS67 government bonds attracted the greatest demand.

The proportion of the market capitalisation of shares on the Ljubljana Stock Exchange accounted for by non-residents remained low. It increased from 7.06% to 7.18% in 2009. The proportion of all equities of Slovenian issuers held by non-residents increased from 14.7% to 15.6%. In 2009 non-resident investors primarily purchased debt securities, their holding increasing from 23.8% to 43.3% of the total. The greatest demand was during the issues of the RS64, RS65, RS66 and RS67 government bonds. The largest purchasers were residents of the UK, Luxembourg and Austria. There was thus a significant change in the breakdown of foreign owners of Slovenian securities last year. Last year was the first year when the proportion of equities held by non-residents was lower than the proportion of debt securities, an indication of a change in investment policy by foreign investors.

Figure 5.17: Stock of non-residents' investments in securities of Slovenian issuers in EUR billion (left), and regional percentage breakdown (right)



Note: Includes investments in listed shares and bonds, and in those not listed on the exchange.
EU3: UK, Denmark, Sweden
EU16: euro area
Ex-YU: former Yugoslav republics
Sources: CSCC, own calculations

Withdrawal of investments from the rest of the world in the first half of 2009, followed by renewed outward investment in the second half of the year and in early 2010.

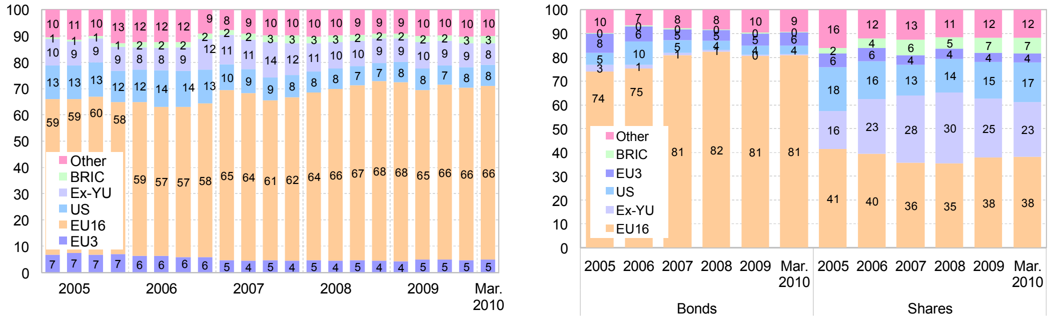
Residents made net purchases of EUR 151.1 million in foreign shares last year. The largest net purchases of foreign equities last year were made by the insurance sector, primarily in the euro area (EUR 48.1 million) and in the former Yugoslav republics (EUR 29.6 million). The banks made net purchases of shares from the former Yugoslav republics (EUR 32.4 million) and sold securities from the US (EUR 10.0 million). Other financial intermediaries made net purchases of shares from the US (EUR 23.0 million), the euro area (EUR 16.6 million) and Switzerland (EUR 8.4 million), while making net sales primarily in shares from the BRIC[22] countries (EUR 14.5 million). A trend of increasing investment in the rest of the world by residents was evident in the second half of 2009 and the early part of 2010. The largest increases were in the stock of investments in the euro area, the US and the BRIC countries, the last primarily as a result of rises in share prices.

The banking sector and the public sector were the largest net sellers of debt securities in 2009: the banks recorded net sales of EUR 336.3 million, and the public sector net sales of EUR 62.1 million. Net purchases were made by the insurance sector, the corporate sector and the household sector, but the amounts were relatively low. The trend of a withdrawal of funds from the rest of the world continued in the first half of 2009, particularly at the banks. As the situation normalised, a trend of renewed placement of bank funds in foreign securities was evident in the second half of 2009 and the early part of 2010.

An increase in investments in the euro area, the US and the BRIC countries.

Euro area bonds were particularly prevalent in the portfolio of foreign bonds, accounting for over 80% of the portfolio of debt securities. Greater diversification was seen in the management of the portfolio of foreign shares, in keeping with good practice in asset management. The proportion of the total investment portfolio accounted for by the former Yugoslav republics declined from 30% to 25% in 2009. The proportions accounted for by the BRIC countries, the US and the euro area increased. This is an indication of the varying dynamics in prices on these markets, and the partial withdrawal from the markets of the former Yugoslav republics, where the economic recovery is uncertain and growth in stock market prices is relatively slow.

Figure 5.18: Regional breakdown of investments by residents in foreign securities overall (left), and bonds and shares separately (right) in percentages



Note: EU3: UK, Denmark, Sweden
EU16: euro area
BRIC: Brazil, Russia, India, China
Ex-YU: former Yugoslav republics

Source: Bank of Slovenia

[22] Brazil, Russia, India and China.

Table 5.5: Overview of investment links with the rest of the world

	2005	2006	2007	2008	2009	Mar. 2010
	Residents' investments in rest of the world					
Shares						
stock, EUR billion	1.5	2.6	4.1	2.3	2.9	3.1
as % GDP	6.3	11.0	11.7	6.2	8.3	8.8
annual growth, %	192.8	73.7	55.9	-43.2	25.5	-16.8
as % of total stock of ISEs	8.0	10.7	11.9	9.4	12.4	13.3
net purchases, EUR billion	0.76	0.83	1.04	0.00	0.15	0.14
Bonds						
stock, EUR billion	1.5	2.9	5.7	5.3	5.2	5.8
as % GDP	6.4	12.1	16.4	14.4	14.9	16.6
annual growth, %	89.2	89.7	95.2	-5.7	-2.6	124.9
as % of total stock of ISDSs	20.6	37.5	87.3	74.6	43.2	42.7
net purchases, EUR billion	0.77	1.38	2.87	-0.22	-0.27	0.55
	Non-residents' investments in Slovenia					
Shares						
stock, EUR billion	2.5	3.2	4.2	3.6	3.6	3.7
as % GDP	8.3	10.7	12.2	9.7	10.4	10.7
annual growth, %	13.0	28.5	30.6	-14.8	1.2	0.3
as % of total stock of ISEs	13.5	13.3	12.3	14.7	15.6	16.0
net purchases, EUR billion	0.13	0.28	0.48	0.02	0.03	0.03
Bonds						
stock, EUR billion	0.5	0.9	0.8	1.7	5.2	7.5
as % GDP	1.6	3.0	2.4	4.6	14.9	21.6
annual growth, %	172.8	85.2	-7.4	103.2	205.1	192.5
as % of total stock of ISDSs	6.7	11.8	12.9	23.8	43.2	55.5
net purchases, EUR billion	0.15	0.38	0.11	0.89	3.40	2.35

Note: The 2010 figures are for net purchases in the first three months of the year only. Includes all investments in Slovenia by non-residents, in both listed and unlisted securities. ISDSs: issued Slovenian debt securities; ISEs: issued Slovenian equities.
Sources: CSCC, Bank of Slovenia, SORS, own calculations

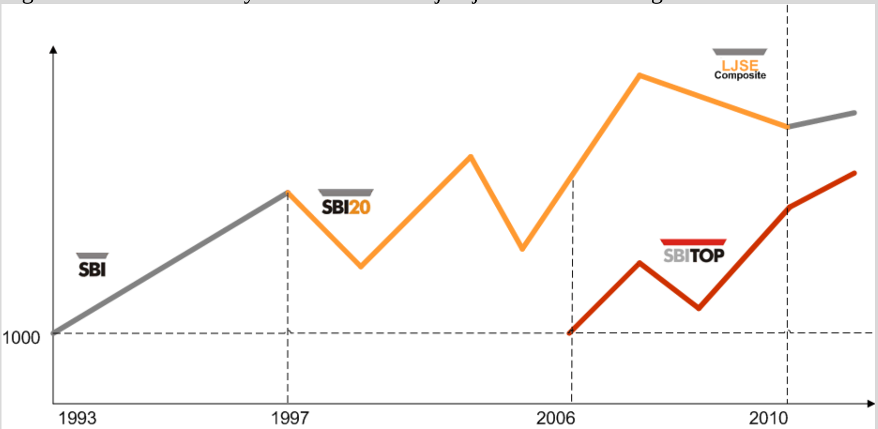
Box 5.1: Ljubljana Stock Exchange, the CEESEG and changes in the Slovenian regulated capital market

Vienna Stock Exchange took an 81% holding in the Ljubljana Stock Exchange on 20 June 2008. With their incorporation in the CEE Stock Exchange Group (CEESEG), the Ljubljana Stock Exchange and the Slovenian capital market have become part of the regional market of central and eastern Europe, thereby gaining new possibilities for development and growth. By the end of 2009, the CEESEG comprised the stock exchanges in Vienna, Ljubljana, Budapest and Prague.

One of the Ljubljana Stock Exchange's most important activities in 2010 is the introduction of the Xetra trading platform, which is scheduled for September. Xetra is an international trading platform used by more than 250 financial corporations with more than 4,800 brokers. Investors can access Xetra directly from 18 European countries and from the Middle East. Xetra, which will be launched in conjunction with stock exchange members, provides further impetus for convergence with internationally established practice on the capital markets, and is expected to give the market a higher profile and better functioning primarily as a result of increased interest from international investment firms and banks, an influx of new foreign portfolio investors, the possibility of listing new financial products, and, later, access to other markets for Slovenian stock exchange members.

In March 2010 the Ljubljana Stock Exchange changed the names of its indices and their methodology of calculation. The purpose of the changes was to increase the market focus of the indices and to harmonise with the standards of the CEESEG. At the same time the methodology of calculating the indices was also changed, to simplify it and adapt it to the needs of market products. The SBI 20 was renamed the LJSE Composite (LJSEX), and has become an index of the entire share market at the Ljubljana Stock Exchange, measuring the return on the entire Slovenian regulated market in shares.. The SBI TOP remains the Ljubljana Stock Exchange's blue-chip index, and is also used as a measurement of the movement in the prices of only the largest and most-liquid shares on the regulated market.

Figure 5.19: Continuity of indices at the Ljubljana Stock Exchange



Source: LJSE

The Ljubljana Stock Exchange drew up a plan for the future development and growth of the Slovenian capital market, which is expected in future years, by means of a change in the corporate financing model, to support the restructuring of the Slovenian economy in order to achieve new growth and higher value-added. In conjunction with market participants the Ljubljana Stock Exchange will set out a new capital market strategy, establish new business models, services and products, and provide a trading and settlement infrastructure to international standards.

The key problems of corporate financing by means of capital market instruments are primarily related to tax legislation and settlement infrastructure. The issuers of financial products cite unfavourable treatment in the taxation of derivative financial products and withholding tax in particular. Foreign investors cite the overly complex procedures in the existing settlement process and a lack of alternative settlement arrangements that recognise fiduciary accounts (indirect clearing, net settlement), as is established practice in the rest of the world. The Ljubljana Stock Exchange is also endeavouring to implement the exit strategy via IPOs on the exchange, as this would revive the Slovenian regulated capital market, increase liquidity, and carry out the sale of government holdings in the commercial sector in a transparent and orderly fashion. The Ljubljana Stock Exchange is also committed to the introduction of the third pillar of pension reform, the introduction of personal accounts, and stimulus for investments in Slovenian securities to help the capital market to flourish.

The new role and strategy for the capital market will be presented to the public in June 2010, and will take account of the need to restructure the Slovenian economy while exploiting the new opportunities opening up with the Ljubljana Stock Exchange's incorporation in the CEESEG.

Box 5.2: Eurosystem and government anti-crisis measures

1. Eurosystem measures

In the middle of 2009 the Eurosystem added five non-standard measures to its package of instruments: an increase in the number and frequency of main refinancing operations, expansion of the list of eligible collateral, full allotment in all main refinancing operations and longer-term refinancing operations in fixed-rate tenders, lending in foreign currency (US dollars and Swiss francs), and a programme of outright purchases of covered bonds.

2. Guarantee for retail deposits

a) The unlimited guarantee for deposits at banks and savings banks established in Slovenia, which was introduced in November 2008, applies until 31 December 2010. The coverage for the payout of deposits to investors that by law are entitled to the payout of guaranteed deposits is provided by the banks up to the basic limit for a guaranteed deposit, and above this limit is provided by the government. Where the banks are unable to secure sufficient funds, the government also guarantees these deposits. The Act Amending the Banking Act (the ZBan-1D), which entered into force on 5 December 2009, changed the limit for a guaranteed deposit from EUR 22,000 to EUR 50,000, which does not entail any changes for investors, given the unlimited guarantee applying until 31 December 2010. It only affects the obligations of banks and savings banks, which in the event of the bankruptcy of any of them would guarantee the payout of deposits to an individual investor that meets the prescribed conditions, up to the increased amount.

b) The increased amount of the guaranteed deposit is the result of the adoption of Directive 2009/14/EC of the European Parliament and of the Council of 11 March 2009 amending Directive 94/19/EC on deposit-guarantee schemes as regards the coverage level and the payout delay. The directive stipulates that governments should raise the minimum coverage level for deposits to at least EUR 50,000 in order to maintain investor confidence and to attain greater stability on the financial markets. In order to protect consumers, to ensure financial stability in the Community and to avoid distortions of competition between Member States, the coverage of aggregate deposits should be increased to a standardised amount of EUR 100,000 by 31 December 2010. The directive also stipulates that the three-month period generally allowed for the payout of guaranteed deposits should be reduced to 20 working days, requires credit institutions to accordingly inform investors, and requires Member States to ensure the conditions for cross-border cooperation and agreements between deposit-guarantee schemes.

3. Issuance of government bonds, the public debt and government deposits at banks

a) Issuance of bonds: in 2009 and the first quarter of 2010 the government borrowed a total of EUR 6.5 billion via the issue of five bonds, mostly to foreign investors.

Table 5.6: Issued government bonds, January 2009 to March 2010

Bond	Issue date[1]	Nominal value, EUR billion	Maturity, years	Coupon rate, %
RS64	5 February 2009	1.0	3	4.250
RS65	2 April 2009	1.5	5	4.375
RS66	9 September 2009	1.5	15	4.625
RS67	26 January 2010	1.5	10	4.125
RS68	17 March 2010	1.0	5	2.750

Note: The date of issue is the date of registration with the CSCC or the first accrual date.
Source: Ministry of Finance

b) The public debt:[1] the changes in public finances in the last year reflect the government's response to the profoundly adverse macroeconomic developments. The government tried to mitigate adverse developments on the demand side, raising its final consumption by 3.1%, while the decline in GDP sharply reduced tax revenues. The deterioration in the public finance position was unavoidable and considerable: the general government deficit increased to above the Maastricht ceiling at 5.5% of GDP, while the general government debt rose by 13 GDP percentage points to 35.9% of GDP. At the same time the stock of government guarantees increased from EUR 4.7 billion to EUR 7.1 billion, which would further increase the general government debt were they to be redeemed.

c) Government deposits at banks: the government obtained considerable proceeds from issuing bonds over a relatively short period and in the uncertain situation on the financial markets. A portion of the proceeds was earmarked for and spent on the repayment of debt, a portion went to finance current spending, and a portion with various maturities was invested in the form of deposits at Slovenian banks.

4. Government guarantees for the issue of bank bonds

Only in the second half of the year did the banks make use of the possibility of obtaining funding by issuing government-guaranteed securities. The government having adopted a resolution issuing a guarantee to NLB d.d. on 5 March 2009, it was on 23 July when the aforementioned bank completed its issue of a 3-year bond with a nominal value of EUR 1.5 billion, a fixed interest rate of 3.25% and a yield at issue in the amount of 105 basis points over the benchmark swap rate. This was followed in the middle of September by Abanka Vipa d.d., which sold an issue of 3-year government-guaranteed bonds with a nominal value of EUR 0.5 billion and a yield of 100 basis points over the 3-month EURIBOR on the international capital market. The considerable demand on the market demonstrated that at the aforementioned price major Slovenian banks could use the government guarantee to secure long-term funding on the international markets in the requisite amount. The change in tax regulations in the early months of 2010 increased the banks' uncertainty, and by delaying bond issues at certain banks that were otherwise ready it hindered the banking system in ensuring an optimal structure of funding.

5. Activities of SID banka d.d.

The government mitigated the standstill in lending through the activities of SID banka, which it owns. In the early part of 2009 SID banka sold its second consecutive issue of S101 bonds to investors, mostly banks, with a nominal value of EUR 250 million, and earmarked EUR 229 million of the proceeds for the commercial banks in the form of long-term loans. At the same time SID banka obtained a total of EUR 1.5 billion of funding by means of issues of debt securities on international markets and by borrowing on the interbank market. The intensity of government intervention via SID banka is also reflected in last year's increase of EUR 937 million or 45% in SID banka's total assets. In keeping with its specific role in the system, the bank directed the majority of the assets into long-term loans to banks, while a smaller portion went into direct corporate lending. Then in April SID banka issued a 5-year bond with a nominal value of EUR 750 million and a yield at issue of 63 basis points above the benchmark swap rate.

5.1 Guarantee scheme for corporate loans

a) Basic facts: between 19 June 2009 and 24 February 2010, SID banka organised ten auctions for banks on behalf of the government at which they were able to obtain shares in the government guarantee quota for corporate bank loans. A total of 13 banks participated in at least one of the auctions, and 11 of them approved loans on the basis of the guarantee scheme.

Table 5.7: Attributes of the auctions, and number and value of corporate loans approved (as at 24 March 2010)

Auction		Maximum	Government guarantee quota, EUR million			Proportion of quota	Loans approved	
No.	Date	government risk, %	tendered	allocated	utilised	utilised, %	number	value, EUR million
1.	19. 6. 2009	50	60.0	60.0	2.7	4.5	19	7.4
2.	24. 6. 2009	40	150.0	149.8	37.9	25.3	48	119.1
3.	9. 7. 2009	35	100.0	100.0	32.7	32.7	76	107.6
4.	9. 9. 09	35	50.0	49.8	36.5	73.3	71	108.1
5.	26. 10. 2009	50	50.0	49.8	30.8	61.8	46	62.1
6.	26. 10. 2009	35	50.0	49.7	41.5	83.5	85	122.3
7.	21. 12. 2009	35	50.0	49.9	23.6	47.3	55	67.9
8.	14. 1. 2010	50	50.0	49.7	6.2	12.5	18	12.4
9.	24. 2. 2010	35	50.0	31.8	8.8	27.7	8	25.1
10.	24. 2. 2010	35	50.0	31.7	0.5	1.6	5	1.6
Total			660.0	622.2	221.3	35.6	431	633.7

Note: The figures in the table are final for the first seven auctions. The difference between the ninth and tenth auctions is that banks with guarantees from the ninth auction can lend to C-rated corporates.
Source: SID banka d.d.

b) Response to the guarantee scheme between July 2009 and February 2010: the guarantee scheme actually began operating with the signing of the first agreements between SID banka and a commercial bank, and between the commercial bank and a corporate in the middle of July. Corporates responded to the banks' offer in the summer, after the second and third auctions. The government then cut the tendered quotas at the subsequent auctions, thereby increasing the utilisation of the guarantee quotas allocated to the banks. The response by banks and corporates was largest in September, and particularly in the two auctions in late October, while the number and value of loans at the seventh auction in December were lower. Borrowers receive the money after a certain delay, and may also receive the money in several tranches. On the basis of the first three auctions, corporates obtained resources that were mostly disbursed between August and October, before responding more strongly again to the banks' offer in the fifth and sixth SID banka auctions in late October. Applying a simplification that by the end of February 2010 the corporates had been disbursed all the money approved on the basis of the loans from the first seven auctions, a total of EUR 594.6 million in new loans was received between last July and the end of this February on the basis of the guarantee scheme.

c) Responsiveness of each group of banks and loan ratings: the large domestic banks approved three-quarters of all loans approved to corporates on the basis of the guarantee scheme. At the same time the ratings structure of the corporates that received loans from the guarantee scheme from the large domestic banks was significantly worse than that at the banks under majority foreign ownership. The banks under majority foreign ownership provided more guarantees at the first two auctions than in the next eight together, although they were extremely conservative in their lending. Participating in the guarantee scheme brought a deterioration in the quality of the large domestic banks' portfolio, but had a positive impact on their lending growth. Their risk was most concentrated in the 67 loans in a total amount of EUR 91.6 million that they approved to C-rated corporates. The banks under majority foreign ownership have clearly targeted their business policy on maintaining market share by focusing on household lending, and are restricting their corporate lending to the highest-quality clients. Further evidence of this can be seen in a comparison of the ratings structure of their loans on the basis of the guarantee scheme, and their overall loans to corporates.

Table 5.8: Ratings of borrowers by group of banks in the first ten auctions in the guarantee scheme as at 24 March 2010

Group of banks	Rating	Guarantee scheme loans				Breakdown of loans, %	
		Number	% of total	Value, EUR million	% of total	to corporates	to all clients
Large domestic banks	A	83	25.2	160.3	33.3	52.5	68.1
	B	180	54.5	229.9	47.7	39.7	26.6
	C	67	20.3	91.6	19.0	4.2	2.6
Total		330	100.0	481.8	100.0	96.4	97.3
Small domestic banks	A	9	36.0	8.7	41.5	60.4	71.2
	B	8	32.0	8.4	40.2	30.5	22.5
	C	8	32.0	3.8	18.2	4.7	3.2
Total		25	100.0	20.8	100.0	95.6	96.9
Banks under majority foreign ownership	A	24	31.6	98.0	74.8	77.1	81.4
	B	44	57.9	25.2	19.3	18.0	14.5
	C	8	10.5	7.8	6.0	3.2	2.0
Total		76	100.0	131.0	100.0	98.2	97.8
All participating banks	A	116	26.9	267.0	42.1	61.8	72.6
	B	232	53.8	263.5	41.6	31.3	22.4
	C	83	19.3	103.2	16.3	3.9	2.4
OVERALL		431	100.0	633.7	100.0	96.9	97.5

Note: For substantive reasons the figures for the banking system's loans comprise all loans, and not classified claims, which are usually the basis for calculating the ratings structure. They have been calculated for the situation as at November 2009, approximately half of the period to which the figures for loans on the basis of the guarantee scheme relate. The remainder up to 100% consists of loans rated D and E.

Sources: SID banka d.d., own calculations

d) Loans by sector: almost three-quarters of the value of the approved loans were obtained by corporates in the manufacturing and construction sectors. The former were hit harder by the decline in demand. Borrowing by corporates in the construction sector is more related to the specifics of the sector, with low exposure to foreign competition, and to the business decisions by the corporates in the last few years. It seems that the guarantee scheme was one of the factors that in the construction sector in the last year was delaying the establishment of a sustainable price balance on the residential real estate market and a balance between equity and debt capital at construction firms. Although the proportion of loans received by corporates in the wholesale and retail trade sector and the transportation and storage sector was relatively low, one thing in common at all four of the aforementioned sectors was their above-average financial leverage before the launch of the guarantee scheme.

Table 5.9: Breakdown of approved corporate loans by sector

Sector	Corporate loans approved in government guarantee scheme				Financial leverage
	Value, EUR million	% of total	Number	% of total	in 2008, %
Manufacturing	317.7	50.1	207	48.0	126.0
Construction	146.9	23.2	67	15.5	419.5
Wholesale and retail trade; repair of motor vehicles	61.6	9.7	66	15.3	188.8
Transportation and storage	58.9	9.3	26	6.0	450.3
Other	48.6	7.7	65	15.1	
Total	633.7	100.0	431	100.0	164.8

Sources: SID banka d.d., AJPES

e) Purpose of the loans: the loans on the basis of the guarantee scheme primarily satisfied the corporate need for financing working capital; less than 10% of the loans were earmarked for financing investments.

Table 5.10: Breakdown of loans on the basis of the guarantee scheme by purpose

Purpose of loan	Corporate loans approved in government guarantee scheme			
	Value, EUR million	% of total	Number	% of total
a) Working capital	572.7	90.4	403	93.5
financing	452.9	71.5	322	74.7
reprogramming	119.8	18.9	81	18.8
b) Investments	61.0	9.6	28	6.5
new	35.9	5.7	12	2.8
in progress	20.4	3.2	15	3.5
reprogramming	4.7	0.7	1	0.2
Total (a+b)	633.7	100.0	431	100.0

Source: SID banka d.d.

e) Total lending potential: in the auctions the banks obtained a total of EUR 622.2 million of government guarantee quota, based on which they themselves take up risks for lending a maximum of EUR 1,355 million in line with the guarantee percentages agreed in the auctions. The total lending potential of the corporate guarantee scheme after the tenth auction was EUR 1,977 million, three times the amount of the approved loans.

Table 5.11: Lending potential and value of approved bank loans on the basis of the corporate guarantee scheme by group of banks as at 24 March 2010 in EUR million

Group of banks	Auctions: lending potential (total of government guarantee and bank guarantee)												Government	Banks'	Approved
	1.	2.	3.	4.	5.	6.	7.	8.	9.	10.	Total	%	guarantee	share	loans
Large domestic	0.0	123.5	148.8	98.2	98.1	74.8	115.2	50.6	76.5	59.3	845.0	42.7	293.7	551.3	481.8
Small domestic	0.0	31.1	12.5	35.6	1.7	6.1	0.0	4.4	5.3	2.4	98.9	5.0	30.9	68.0	20.8
Foreign	219.9	442.4	163.3	15.3	3.1	65.8	30.5	50.3	10.0	32.7	1,033.3	52.3	297.6	735.7	131.0
Total	219.9	597.1	324.6	149.0	102.9	146.7	145.7	105.3	91.8	94.4	1,977.2	100.0	622.2	1,355.0	633.7

Sources: SID banka d.d., own calculations

f) With almost EUR 600 million of loans disbursed on the basis of the guarantee scheme between July and February, the banks would in many cases have approved the loans even if there had been no guarantee scheme, primarily to clients rated A (42% of the value of the loans approved on the basis of the guarantee scheme) and B. What the value of the loans would have been in this event it is impossible to estimate, and an assessment of the guarantee scheme therefore cannot be perfect. At the same time, it could worsen if the quality of the portfolio of loans approved to corporates on the basis of the guarantee scheme were to begin to deteriorate more than in just a few unavoidable cases.

5.2 Guarantee scheme for household loans

a) The purpose of the guarantee scheme for household loans is to mitigate the effects of the economic crisis on households. In the scheme the government allows banks to transfer to it 50% or 100% of the loans that the banks will approve by the end of 2010, or until the quota of EUR 350 million for this purpose is exhausted. The banks obtain the guarantee quotas for approving liabilities at auctions organised by SID banka, with descending bids for the overall effective interest rate at which they will approve the loans. Those eligible for the scheme are Slovenian citizens and foreign citizens with permanent residence in Slovenia, provided that they meet one of the following conditions:[2]
- they are temporarily employed;
- they are purchasing their first home;
- they are part of a young family;
- they have had their employment terminated since 1 October 2008 on business grounds.

Table 5.12: Guarantee scheme for household loans as at 19 March 2010

Auction	Date	Tendered quota, EUR million	Maximum interest rate, %	Size of guarantee, %	Allocated quota, EUR million	Approved loans value, EUR million	Approved loans number	Issued guarantees, EUR million
1.	25. 9. 2009	50.0	8	50				
2.	25. 9. 2009	10.0	9	100				
a) Total		60.0			38.4	14.7	484	8.2
3.	28. 1. 2010	50.0	7	50				
4.	28. 1. 2010	20.0	5	100				
b) Total		70.0			33.9	4.5	107	2.3
Total a + b		130.0			72.3	19.2	591	10.5

Source: SID banka d.d.

b) The guarantee scheme for household loans is an instrument of low effectiveness, judging simply by the 14.5% utilisation of the issued guarantees in the assigned quota. The banks were reluctant to accept it, with only six banks, one branch of a foreign bank and one savings bank participating, and the concentration of approved loans between them was considerable. It could be concluded that the banks were able to meet their needs without utilising the guarantee scheme, partly by making adjustments for specific potential guarantee scheme beneficiaries. This was one of the reasons for certain banks not participating in the guarantee scheme for household loans. Nevertheless, with 591 loans and approximately this number of borrowers, the guarantee scheme for household loans has shown the scale of the need for such an instrument, and has proven justified.

6. Exit strategy and bank funding

The one-year funding from the Eurosystem falls due for payment for Slovenian banks in the second half of 2010. The funding of the banks is therefore redirecting towards deposits and other resources that the banks can obtain on the market. A feature of 2009 was that the banks required funding to repay liabilities to the rest of the world as lending stalled. A period is coming when the banks will increasingly need long-term funding to gradually increase lending. The importance of government deposits as funding will diminish as a result of the normalisation of the functioning of the financial markets and the restriction of the increase in government debt. The government’s exit strategy adopted in February 2010 sets out the gradual withdrawal of anti-crisis measures in the financial sector, and the consolidation of public finances, which is aimed at cutting the general government deficit to below 3% of GDP by 2013. Even in 2009 the banks began obtaining funding on the market by issuing government-guaranteed bank securities. Two banks successfully issued bonds, while some made preparations to do so, but delayed the issue because of changes in tax regulations that would have made the funding more expensive for these banks. The two banks were able to issue bonds on the basis of government guarantees already obtained, while the others have until the end of 2010 to obtain a guarantee. This will allow them to use the government guarantee to secure long-term funding in early 2011. By issuing securities the banks could obtain foreign funding, but they should also try to make better use of the domestic capital market, and to attract institutional investors.

[1] Source: Price Stability Report, Bank of Slovenia, April 2010.
[2] The conditions are cited in abbreviated form. They are set out in full by the Article 6 of the Republic of Slovenia Guarantee Scheme for Natural Persons Act.

6 BANKING SECTOR

6.1 Structural features of the banking sector

Banking sector size and changes of status

The number of banks rose to 22 in 2009.

There were 19 banks, three savings banks and three branches of foreign banks operating in Slovenia at the end of 2009. The total number of credit institutions was up one on the previous year, as KD banka commenced trading as a newly established bank on 2 March 2009.

By 31 December 2009 the Bank of Slovenia had received notifications of the direct provision of banking services and other mutually recognised financial services for a total of 284 credit institutions and special financial institutions, primarily from Austria, the United Kingdom and Germany.

The banking system's total assets stood at 147% of GDP at the end of 2009.

Banks remain by far the most important financial intermediaries, while the proportion of savings banks is negligible. The banks had total assets of EUR 51.4 billion in December 2009, while those of savings banks stood at EUR 396.7 million. The banking system’s total assets thus stood at 147.4% of GDP. The total assets of banks and savings banks as a percentage of GDP were up relatively sharply in 2009, as a result of the relatively high growth in total assets and the real decline in GDP last year.

Growth in total assets was 8% in 2009, down 4.5 percentage points on 2008. The highest growth, of nearly 45%, was recorded by SID banka, as a result of government-guaranteed borrowing on the international financial market, and on account of lending to the banking and household sectors.

The ratio of the Slovenian banks’ total assets to GDP has increased from year to year, but is nevertheless still significantly lower than the EU average, which stood at 337% at the end of 2008.

Table 6.1: Total assets of banks compared with GDP

	2004	2005	2006	2007	2008	2009
Total assets, EUR million	23,691	29,287	33,868	42,343	47,628	51,427
GDP (current prices), EUR million	27,073	28,704	31,050	34,569	37,136	34,892
Total assets as % of GDP	87.5	102.0	109.1	122.5	128.3	147.4
Ratio of growth in total assets to GDP growth	1.6	3.9	2.0	2.2	1.7	-1.3
No. of bank employees	11,534	11,632	11,707	11,868	12,046	11,935

Source: Bank of Slovenia

Bank ownership

Ten banks were under majority domestic ownership at the end of 2009.

There were eight subsidiary banks and three branches of foreign banks operating in Slovenia at the end of 2009. One bank was under full domestic ownership, while nine banks were under majority domestic ownership. The proportion of equity held by non-residents was down 1.6 percentage points on 2008 to stand at 36.6%, of which the proportion held by non-residents with equity holdings exceeding 50% stood at 26.8%. The proportion of the Slovenian banking system held by non-residents in terms of total assets at the end of 2009 was 2.9 percentage points higher that that in terms of equity. Government ownership as measured by equity rose slightly last year, to stand at 20.45%, primarily as a result of a capital increase at SID banka in August 2009.

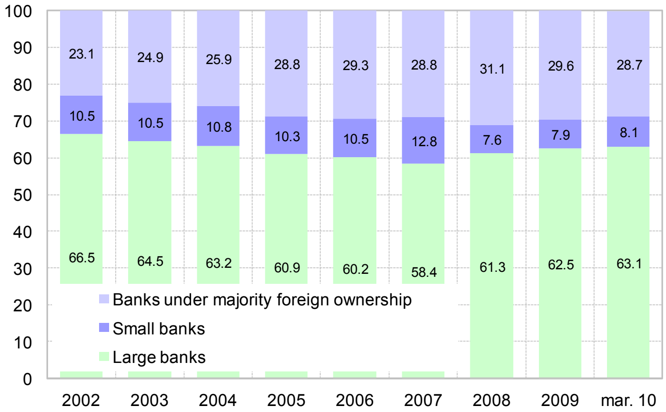
Table 6.2: Ownership structure of the banking sector (in terms of equity)

(%)	2004	2005	2006	2007	2008	2009
Central government	19.1	18.2	17.9	15.1	17.7	20.5
Other domestic entities	48.6	46.9	44.4	47.2	44.1	43.0
Non-residents	32.4	34.9	37.7	37.8	38.2	36.6
non-residents (over 50% control)	16.5	19.4	27.7	26.8	27.6	26.8
non-residents (under 50% control)	15.9	15.5	10.0	11.0	10.6	9.8

Source: Bank of Slovenia

In the subsequent analysis, the banks are divided into three groups: the large and small domestic banks, and the banks under majority foreign ownership. Each bank is classified into one group only. The size of the bank is determined by its total assets. All the banks under majority foreign ownership are placed in the same group, regardless of size, owing to differences in their behaviour and operational methods. Despite this division for analytical purposes, all euro area banks are treated the same irrespective of ownership.

Figure 6.1: Market shares of banks under majority foreign ownership and under majority domestic ownership in terms of total assets in percentages



Source: Bank of Slovenia

Concentration in the banking sector

There was no significant change in market concentration in 2009 in the most important market segments.

There were no significant changes in the market concentration in the Slovenian banking sector in 2009. There was a slight decrease in the concentration of loans to non-financial corporations and households. Market concentration as measured by the Herfindahl-Hirschman index has been prominent for some time with regard to household deposits in particular. This was further increased by the aquisition of three banks by Nova Ljubljanska banka in May 2008.

Table 6.3: Market concentration of the Slovenian banking market as measured by the Herfindahl-Hirschman index, and market share of the top three/five banks

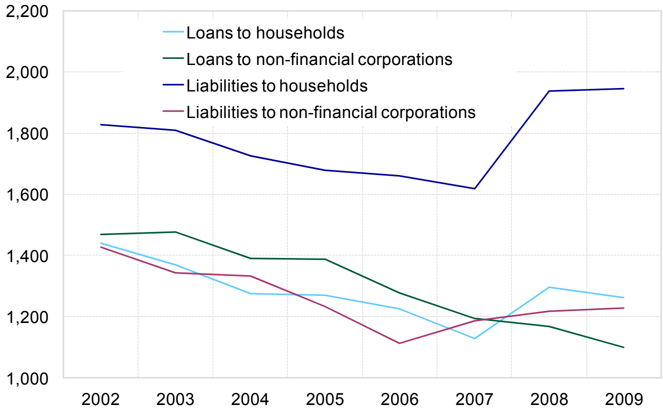
	2004	2005	2006	2007	2008	2009	Change 2009/2008
	Herfindahl-Hirschman index						
Total assets	1,472	1,395	1,342	1,313	1,282	1,269	-13
Total assets (euro area)	599	642	630	655	687		
unweighted	997	1,029	996	1,006	1084		
Loans to non-banking sectors	1,310	1,307	1,232	1,214	1,123	1,164	41
Liabilities to non-banking sectors	1,570	1,462	1,434	1,477	1,616	1,627	11
Liabilities to banks	1,278	1,339	1,236	1,170	1,034	1,042	8
	Market share of top 3 banks, %						
Total assets	52.0	50.6	50.0	49.0	48.0	47.9	-0.1
Loans to non-banking sectors	50.5	49.2	48.0	47.0	46.6	46.0	-0.6
Liabilities to non-banking sectors	55.3	54.1	54.0	54.2	56.6	56.5	-0.1
Liabilities to banks	49.0	49.7	48.0	41.4	36.4	46.2	9.8
	Market share of top 5 banks, %						
Total assets	65.1	63.6	62.7	59.9	59.4	60.1	0.7
Total assets (euro area)	41.6	42.6	42.8	44.1	44.7		
unweighted	54.2	54.9	54.4	54.7	57.1		
Loans to non-banking sectors	64.2	62.6	61.3	58.4	59.3	58.7	-0.6
Liabilities to non-banking sectors	68.9	67.3	66.7	65.8	65.7	68.8	3.1
Liabilities to banks	62.0	62.9	61.4	50.9	51.2	61.3	10.1

Sources: Bank of Slovenia, ECB: Report on EU Banking Structures

Concentration in the Slovenian banking system is higher than in the euro area.

Concentration in Slovenia is higher than the euro area average, although the gap is diminishing, as reflected in the market share of the five largest banks, which in 2009 was just 3 percentage points higher than the unweighted euro area average for 2008.

Figure 6.2: Market concentration in bank operations with non-banking sectors as measured by the Herfindahl-Hirschman index



Source: Bank of Slovenia

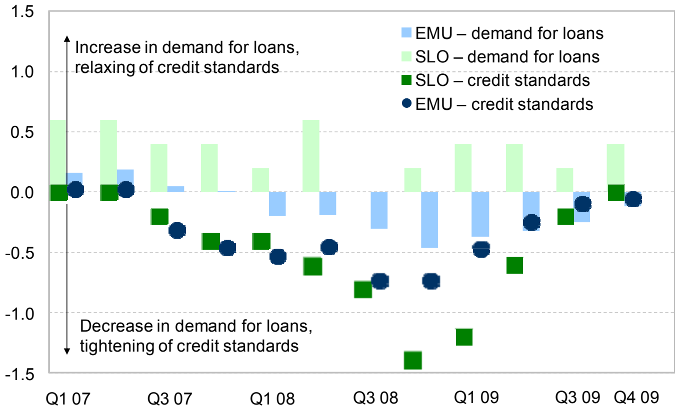
6.2 Banks' assessment of changing demand for loans and changing credit standards[23]

6.2.1 Demand for corporate loans and credit standards

A period of further tightening of credit standards came to an end last year.

Demand for corporate loans was up last year, primarily owing to the needs for working capital and the restructuring of debt. Loan demand was driven by tightened corporate financing. A portion of loan demand derived from corporates that were not creditworthy. There was also a notable convergence with the euro area, where corporate demand for loans declined in each quarter.

Figure 6.3: Demand for corporate loans and credit standards



Source: ECB, Bank of Slovenia

At the same time, the banks were increasingly reluctant to further tighten credit standards[24] for corporate loans. These standards, however, remain significantly tighter than in the period prior to the financial turmoil. The end of 2009 saw an end to the period of tightening standards, which began in the middle of 2007. Several risk factors (e.g. expectation regarding general economic activity, risks associated with individual sectors and risks associated with securing claims) had a significant impact on the tightening of

[23] The ESCB supplements the prevailing quantitative information with its Bank Lending Survey. The ECB publishes the results for the euro area on its website. Methodological limitations mean that the results for Slovenia (for the five banks included in the sample) and for the euro area as a whole are not directly comparable, and the substantive conclusions are less solid than in quantitative analyses.

[24] Credit standards are defined in the survey as internal guidelines or criteria that reflect the bank's lending policy. Lending terms are specific contractual obligations or elements of an agreement between bank and borrower.

credit standards in the first quarter of 2009, while difficulties in accessing financing had a lesser effect. In contrast to the first half of the year, improved access to market sources in the second half of the year actually prevented the further tightening of credit standards, while the effect of the risk factors diminished. Changes in lending terms included a sharp increase in premiums over the reference interest rate for higher-risk loans and required collateral in the first half of the year while, to a lesser degree, the banks increased non-interest expenses and limited the size and maturity of approved loans. Certain banks merely increased premiums for higher-risk loans at the end of the year.

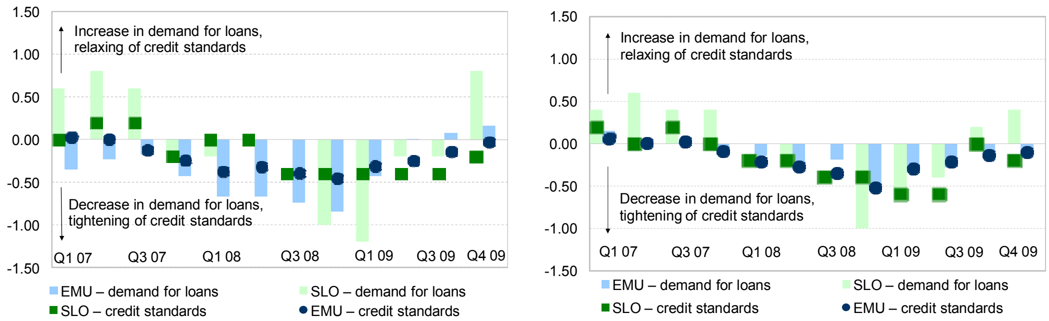
6.2.2 Household demand for housing loans and consumer loans, and changes in credit standards

Housing loans

Demand for housing loans was up for the first time in two years.

Demand for housing loans fell sharply at the beginning of the year, owing to expected developments on the housing market and declining consumer confidence. The impact of the aforementioned factors then diminished and stimulated demand towards the end of the year. The moderate tightening of credit standards for housing loans at the beginning of the year was a result of risks associated with the general economic conditions and expectations on the real estate market and, to a lesser degree, with the costs of bank funding. The impact of the latter had diminished by the end of the year, while the negative effect of economic conditions and the state of the real estate market was also less pronounced. The banks tightened lending terms for housing loans in the first quarter of last year, primarily by raising their premiums over the reference interest rates. At the same time, they also tightened loan collateral terms and increased their LTV ratios. The banks stopped raising their premiums in the second half of the year, and also stopped tightening other lending terms in the final months.

Figure 6.4: Household demand for housing loans (left) and consumer loans (right), and changes in credit standards



Source: ECB, Bank of Slovenia

Consumer loans

Demand for consumer loans began to rise slightly in the second half of the year.

Demand for consumer loans was down in the first half of year, although the decline lessened from quarter to quarter. The declining demand was a result of diminishing needs for financing (owing to a drop in spending on durables), lower consumer confidence and declining interest in the purchase of securities. A slight rise in consumption is expected to trigger growing demand in the second half of the year. The tightening of credit standards in the first half of the year was a result of risks associated with expected economic activity, the creditworthiness of borrowers, loan collateral and, to a lesser extent, limitations on bank funding. The banks primarily adjusted lending terms by raising premiums and tightening loan collateral requirements. The tightening of credit standards came to a halt in the third quarter.

6.3 Changes in balance sheet structure

Declining growth in the banks' total assets.

Average growth in the banking system’s total assets stood at 9.1% last year, down 10.8 percentage points on the growth recorded in 2008. While the decline in total assets in 2008 was relatively closely tied to declining growth in lending, that trend came to an end last year, when the drop in lending was significantly sharper. Contributing most to growth in total assets was the increase in government deposits at banks as a result of several government bond issues, the additional issues of bank securities and increased borrowing at the ECB. In the context of weak growth in household deposits, which was down on the growth recorded in previous years, the three aforementioned sources compensated for dried-up funding in the form of loans from the rest of the world. Nearly the whole of last year was marked by continuous net repayments to banks in the rest of the world. The same was true for the first quarter of this year. Liabilities to banks in the rest of the world were down one-fifth at the end of last year. The ratio of this funding to the banks' total liabilities fell from one-third at the end of 2008 to one-quarter at the end of 2009.

A sharp decline in growth in loans to non-banking sectors.

The most prominent feature of last year was the standstill in the banks' lending activity. At 18.5%, growth in loans to non-banking sectors was still relatively high at the end of 2008, but had fallen to almost zero by the end of last year. The trend of declining bank investments in securities came to an end last year. The banks once again increased the proportion of total assets accounted for by securities, resulting in a decline in the proportion of total assets accounted for by loans to non-banking sectors. The increase in the proportion of total assets accounted for by claims against banks also stood out among other forms of investment.

Table 6.4: Market shares and growth in total assets and loans to non-banking sectors by bank group in percentages

(%)	Market shares					Growth				
	2006	2007	2008	2009	Mar. 10	2006	2007	2008	2009	Mar. 10
Total assets										
large banks	60.2	61.5	61.3	62.5	63.1	13.9	26.5	7.7	10.1	7.0
foreign banks	29.3	28.8	31.1	29.6	28.7	17.9	22.7	21.8	2.6	-0.3
small banks	10.5	9.8	7.6	7.9	8.1	22.6	22.0	18.2	12.8	8.6
overall	100	100	100	99	100	15.6	25.0	12.5	8.0	4.9
Loans to non-banking sectors										
large banks	56.5	56.4	56.7	56.5	56.6	21.7	37.5	13.9	0.3	1.7
foreign banks	33.8	34.1	36.2	35.7	35.6	33.7	40.0	25.7	-0.5	-0.1
small banks	9.8	9.5	7.1	7.7	7.7	35.9	42.0	22.0	9.0	6.6
overall	100	100	100	99	100	26.4	38.6	18.5	0.6	1.4

Source: Bank of Slovenia

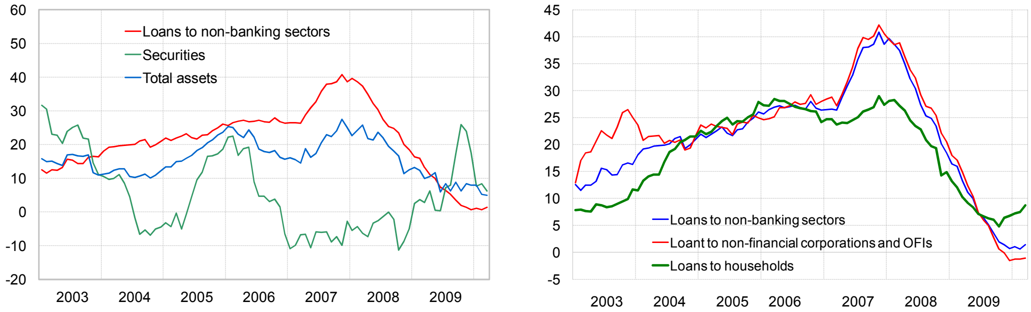
6.3.2 Major factors in the decline in lending growth

Tightened lending terms contributed to a decline in lending growth.

Lending growth began to decline back in 2008 as a result of the tightening of terms on bank funding in the rest of the world, rising real interest rates and a base effect from the previous year when lending growth was sharply above average. Further contributing to the decline in lending growth, which was merely 0.6% at the end of last year, was the tightening of the banks' policies regarding loan collateral and higher premiums over the reference interest rates.

A decline in lending growth was characteristic of all bank groups last year. The banks under majority foreign ownership limited their lending to non-financial corporations most notably, while increasing lending to households.

Figure 6.5: Year-on-year growth in bank investments and loans to non-banking sectors in percentages



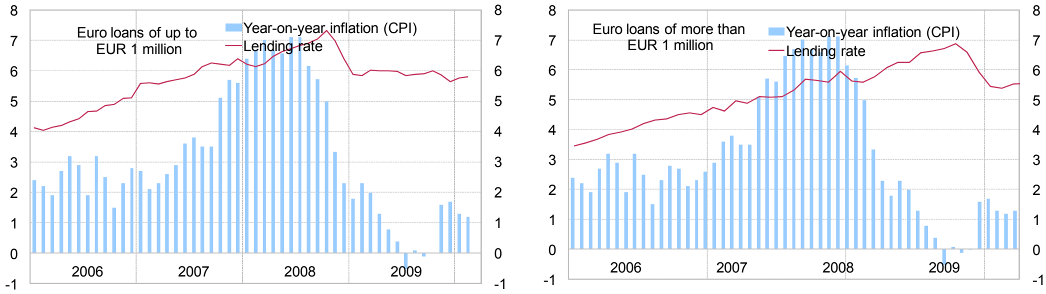
Source: Bank of Slovenia

Movement of interest rates and inflation as a factor of demand for loans

The real interest rate on corporate loans rose.

The real interest rate rose rapidly in the context of falling inflation and the maintenance of the nominal level of interest rates, which contributed to the decline in corporate demand for loans.

Figure 6.6: Interest rates on corporate loans of up to EUR 1 million (left) and more than EUR 1 million (right) and annual inflation in percentages



Source: Bank of Slovenia

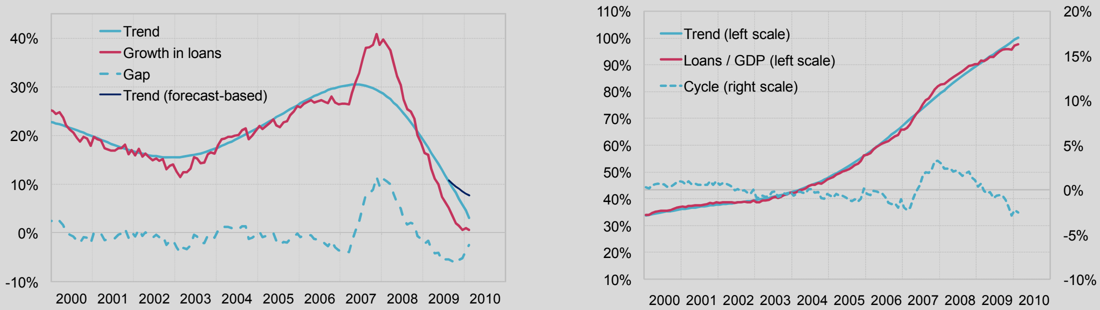
Box 6.2: Indicators of balanced lending growth

Balanced lending growth and the deviation of actual lending growth from balanced growth represent important data in analysing the dynamics of lending. One method used to assess balanced lending growth is the Hodrick-Prescott filter (HP-filter). It is a smoothing method used for assessing a component of a longer time series. We used the HP filter to assess the long-term trend of growth in loans on the basis of seasonally adjusted growth in loans to non-banking sectors, non-financial corporations and households. We used the same filter to assess the long-term trend of the ratio of the volume of loans to GDP for specific sectors on the basis of a seasonally adjusted ratio.

Owing to the methodological shortcomings of the HP-filter, we extended the basic data series of growth in loans with estimates of growth in loans until the end of 2011, seasonally adjusted them, and then assessed the long-term trend. Since the ratio of the volume of loans to GDP is less volatile over time, we did not extend basic data series with estimates when assessing the long-term trend.

Actual growth in loans to non-banking sectors was below the long-term average in 2009. The negative gap widened until October, and then began to close. Actual growth in loans to non-banking sectors in February 2010 was 2.5 percentage points below the long-term trend estimated on the basis of growth in loans until the end of February 2010, and 7.1 percentage points below the long-term trend of growth in loans estimated on the basis of growth in loans extended until the end of 2011 using estimates. The ratio of the volume of loans to non-banking sectors to GDP was 2.5 percentage points below the long-term trend in February 2010.

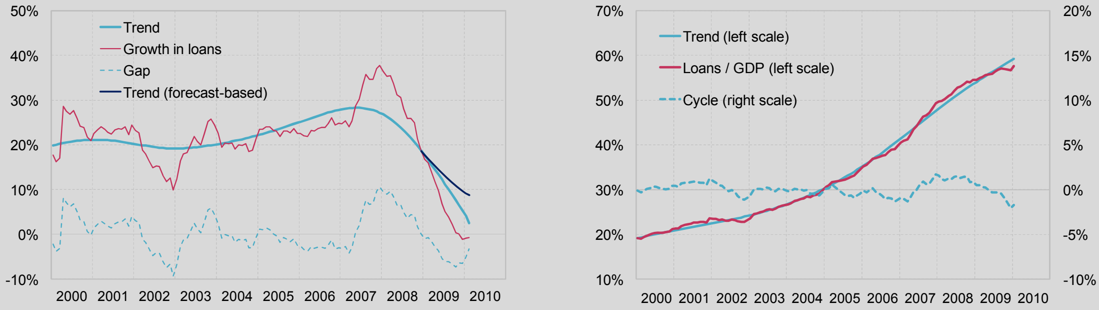
Figure 6.7: Growth in loans to non-banking sectors (left) and the ratio of the volume of loans to GDP (right)



Source: Bank of Slovenia

Actual growth in loans to non-financial corporations was below the long-term trend last year. This negative gap also widened until October, and then began to close. Actual growth in loans to non-financial corporations in February 2010 was 3.2 percentage points below the long-term trend estimated on the basis of growth in loans until the end of February 2010, and 9.4 percentage points below the long-term trend of growth in loans estimated on the basis of growth in loans extended until the end of 2011 using estimates. The ratio of the volume of loans to non-financial corporations to GDP was 1.7 percentage points below the long-term trend in February 2010.

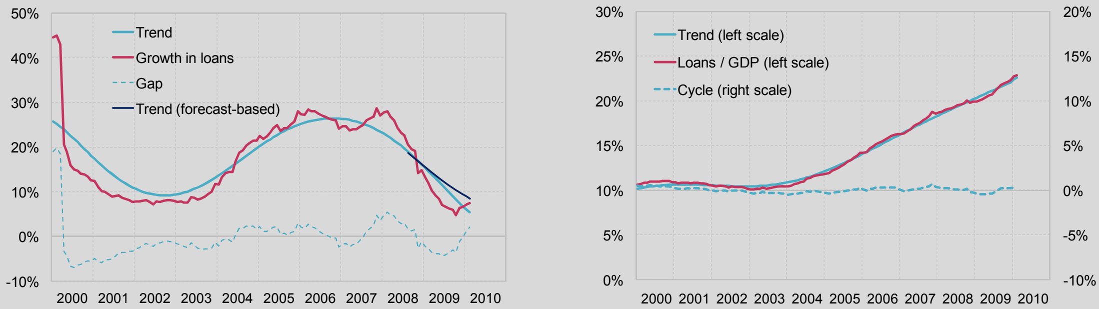
Figure 6.8: Growth in loans to non-financial corporations (left) and the ratio of the volume of loans to GDP (right)



Source: Bank of Slovenia

Actual growth in loans to households was below the long-term trend in 2009, but considerably less than loans to non-financial corporations and non-banking sectors. The negative gap widened until the middle of last year, and then began to close, and became positive in 2010. Actual growth in loans to households in February 2010 was 2.1 percentage points above the long-term trend estimated on the basis of growth in loans until the end of February 2010, and 1 percentage point below the long-term trend of growth in loans estimated on the basis of growth in loans extended until the end of 2011 using estimates. The ratio of the volume of loans to households to GDP was at the level of the long-term trend in February 2010.

Figure 6.9: Growth in loans to households (left) and the ratio of the volume of loans to GDP (right)



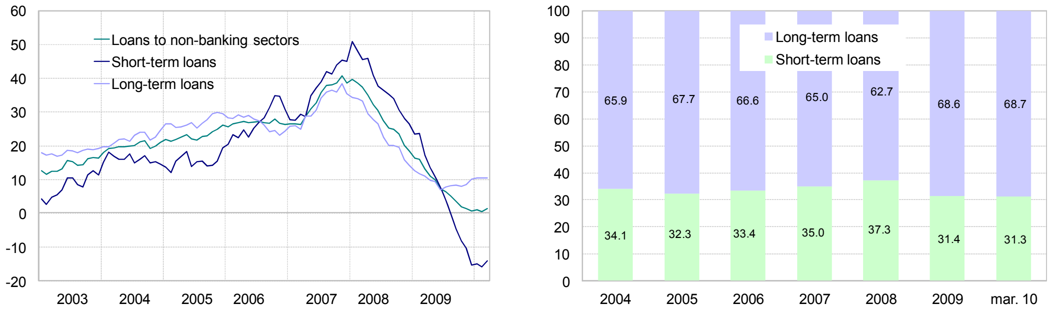
Source: Bank of Slovenia

Despite the narrowing of the negative gaps, significant differences between growth in lending to households and non-financial corporations remain, as a result of the more procyclical rate of growth in loans to non-financial corporations compared with loans to households.

6.3.3 Structure of assets

The maturity breakdown of loans changed significantly last year, the proportion of loans to non-banking sectors accounted for by long-term loans having increased from 62.7% to 68.6%.

Figure 6.10: Year-on-year growth in loans to non-banking sectors by maturity, and percentage breakdown of loans to non-banking sectors by maturity



Source: Bank of Slovenia

Loan maturities changed.

The banks mainly approved short-term corporate loans, although maturing loans exceeded the volume of newly approved loans. Also contributing to the decline in the stock of short-term loans is the fact that the banks have converted a portion of revolving short-term loans to long-term loans. The change in the breakdown is partly a result of an increase in bank loans to households, which are predominantly long-term in nature.

Growth in foreign currency loans to non-banking sectors fell rapidly last year, and was negative from May on. Foreign currency loans accounted for less than 5% of all loans at the end of the year. The proportion accounted for by foreign currency loans is highest in household loans, the figure standing at 10.5% at the end of the first quarter of this year.

A decline in the proportion of loans to non-banking sectors in bank balance sheets and an increase in the proportion accounted for by securities and claims against banks.

The trend of a decline in the proportion of the banking system's total assets accounted for by securities came to an end last year. The stock of securities on bank balance sheets was up EUR 1.6 billion, to reach 16.1% of total assets. The banking system's claims against banks were also up, by EUR 1.9 billion. In the context of stagnating growth in lending, the proportion of total assets accounted for by loans to non-banking sectors was down 4.8 percentage points, as a result of the aforementioned increase in the proportion of securities and claims against banks in bank balance sheets.

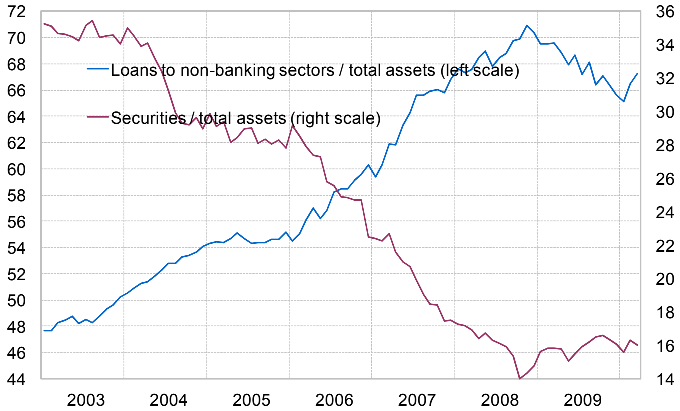
Table 6.5: Structure of and growth in balance sheet items in the banking sector at year-end in percentages

						Growth, %				
	2006	2007	2008	2009	Mar. 2010	2006	2007	2008	2009	Mar. 2010
Total assets, EUR million	33,868	42,343	47,628	51,427	50,655	15.6	25.0	12.5	8.0	4.9
Assets	Structure, %									
Cash	3.1	1.4	2.6	2.8	2.1	76.3	-42.9	105.9	17.0	38.0
Loans to banks	9.1	9.6	8.5	11.1	10.0	6.8	32.8	-1.0	41.2	18.3
Loans to non-banking sectors	60.3	66.8	70.4	65.6	67.3	26.4	38.6	18.5	0.6	1.4
corporate loans	36.5	40.2	42.5	38.9	40.0	24.8	37.8	18.8	-1.2	-0.2
household loans	14.9	15.2	15.5	15.3	15.9	24.1	27.1	14.9	6.8	8.7
loans to government	1.7	1.1	1.1	1.4	1.5	-13.8	-18.9	8.9	45.1	36.7
loans to others	7.1	10.3	11.3	10.0	9.9	61.3	80.7	23.4	-5.1	-6.2
Financial assets/securities	23.3	18.2	15.3	17.3	17.2	-5.7	-2.2	-5.7	21.9	9.7
of which government	8.0	10.1	8.6	9.9	9.4	0.5	57.5	-4.8	24.9	3.2
Capital investments	1.3	1.5	1.3	1.4	1.4	19.9	43.9	2.0	11.0	11.0
Other assets	3.0	2.4	1.9	1.9	2.0	8.0	2.5	-11.1	5.1	-2.2
Liabilities										
Liabilities to banks	31.9	38.0	40.7	34.7	34.1	28.6	49.0	20.4	-7.8	-5.8
to foreign banks	29.9	34.0	33.8	25.0	24.1	28.1	42.5	11.7	-20.0	-19.4
Liabilities to non-banking sectors	51.7	45.8	43.3	45.8	45.8	9.3	10.7	6.4	14.3	6.0
to corporates	14.1	11.4	10.0	9.6	9.9	10.3	0.7	-1.0	3.4	4.5
to households	33.4	29.2	28.4	27.4	28.2	7.4	9.3	9.2	4.3	3.2
to government	3.3	3.6	3.9	7.8	6.7	28.5	35.6	22.9	114.9	21.0
to others	0.8	1.6	1.0	1.0	1.1	6.9	139.0	-30.7	13.8	14.0
Liabilities from securities	2.9	2.3	2.6	6.7	6.9	-1.6	-1.3	30.6	172.9	130.1
Other liabilities	4.6	3.9	3.9	7.8	8.1	3.3	6.3	14.1	112.5	82.9
Provisions	0.5	0.5	0.4	0.3	0.3	2.2	12.6	-15.4	-1.3	0.7
Subordinated liabilities	2.9	3.5	3.4	3.0	3.1	40.0	48.1	8.6	-2.9	-2.6
Capital	8.4	8.4	8.4	8.4	8.6	14.3	25.2	12.4	7.5	7.2

Note: The category of financial assets is wider than securities in methodological terms, and also includes available-for-sale loans and certain available-for-sale securities with the function of capital investments.

Source: Bank of Slovenia

Figure 6.11: Percentage of total assets accounted for by loans to non-banking sectors and securities



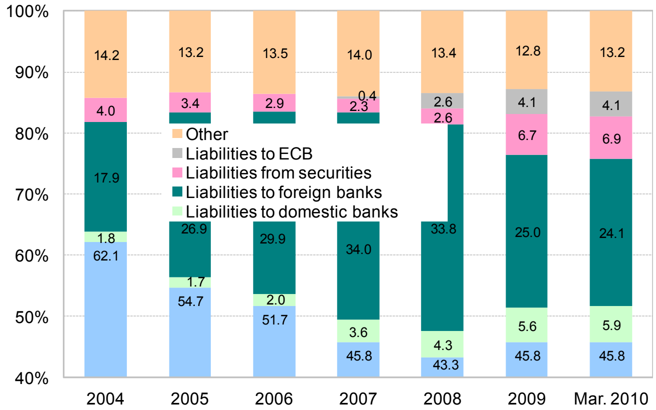
Source: Bank of Slovenia

6.3.4 Bank funding

Restructuring of the banks' liabilities in 2009.

The banks made debt repayments to the rest of world of EUR 3.2 billion last year, and an additional EUR 650 million in the first quarter of this year. For this reason the banks were forced to restructure their liabilities. The banks compensated for the drop in funding in the form of loans from the rest of the world with government deposits. An even more important long-term source of funding for two banks was the issue of government-guaranteed bonds in the total amount of EUR 2 billion. Funds raised at the ECB have grown further in importance.

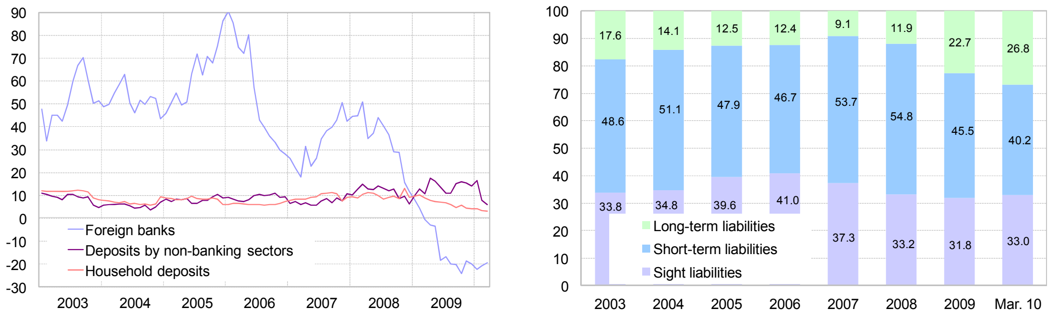
Figure 6.12: Structure of bank funding in percentages



Source: Bank of Slovenia

Last year's net increase in household deposits of EUR 592 million was half of that recorded in previous years. Restrictions on funding at foreign banks and a sharp increase in economic uncertainties forced the banks to ease their pace of lending to non-banking sectors last year.

Figure 6.13: Growth in funding (left), and breakdown of banks' sight, short-term and long-term liabilities to non-banking sectors (right) in percentages

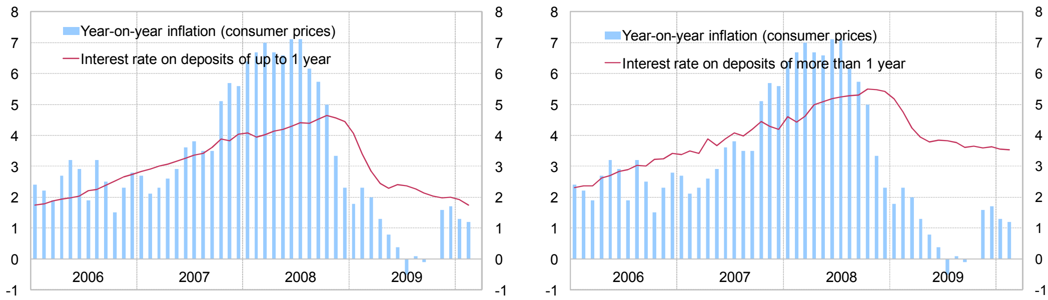


Sources: Bank of Slovenia

The proportion of deposits by non-banking sectors accounted for by long-term deposits was up.

The increase in the proportion of deposits by non-banking sectors accounted for by long-term deposits is partly a result of an increase in long-term government deposits. Likewise, the proportion of household deposits accounted for by long-term deposits was up from just over 15% at the beginning of last year to 20% in the first quarter of this year, as a result of higher interest rates on long-term deposits.

Figure 6.14: Interest rates on deposits of up to 1 year (left) and on deposits of more than 1 year (right), and inflation rate in percentages



Sources: Bank of Slovenia

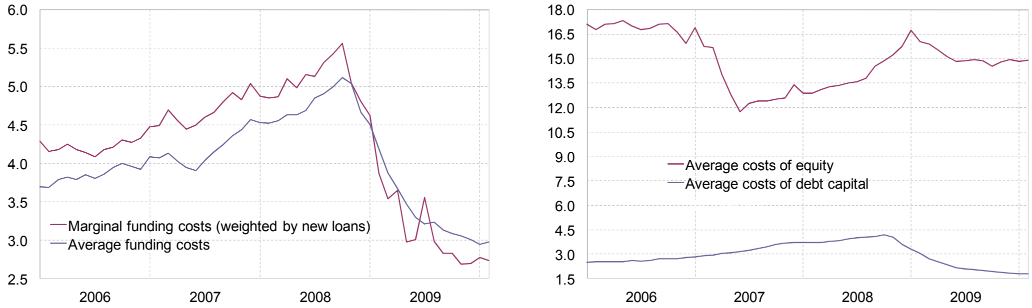
Ex post real interest rates rose in the first half of 2009 owing to the more rapid fall of inflation than in deposit interest rates. That gap has narrowed however, particularly on short-term deposits, in conjunction with rising growth in prices in the second half of last year and the first months of this year. This affected savers' decisions regarding deposit maturities.

6.3.5 Costs of bank funding

Bank funding costs were down notably in 2009.

The decline in the banks' average and marginal funding costs, which began in at the end of 2008, continued last year,[25] and was primarily a result of the falling costs of debt and, to a lesser degree, the falling costs of equity (i.e. a rise in bank share prices). We assess that the decline in bank funding costs will end soon owing to the expected rise in market interest rates. The banks' average funding costs fell 166 basis points in 2009 to 3%, and remained at approximately that level in the first two months of 2010. The banks' marginal funding costs were down 211 basis points in 2009 at 2.7%, but have risen slightly in 2010.

Figure 6.15: Average and marginal funding costs of banks (left), and average costs of equity and debt capital (right) in percentages



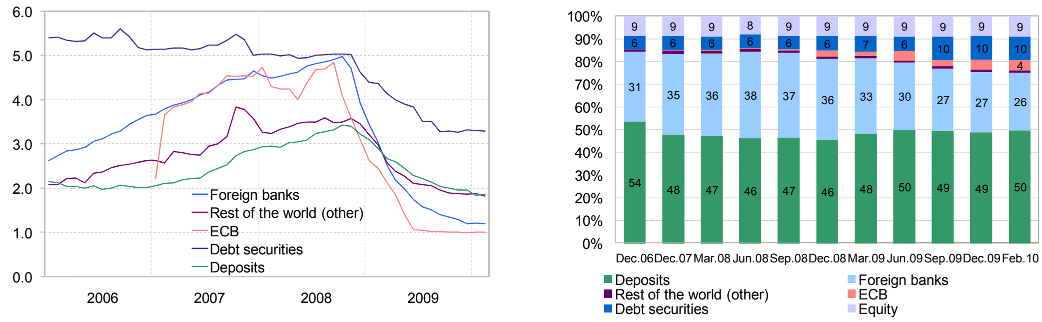
Sources: Bank of Slovenije, LJSE

Average costs of debt capital

Falling interest rates on deposits by non-banking sectors and on liabilities to foreign banks contributed most to declining debt capital costs.

Declining debt capital costs are a result of falling interest rates, particularly on liabilities to foreign banks and on deposits by non-banking sectors. Contributing further to lower average costs was less expensive funding obtained via ECB auctions and significantly shorter maturities on funding obtained at foreign banks. Interest rates on short-term deposits by non-banking sectors recorded the sharpest drop between the end of 2008 and February 2010 (down 248 basis points), followed by lesser falls for interest rates on long-term deposits (down 135 basis points) and interest rates on sight and overnight deposits (down 29 basis points). Recording the sharpest decline over the same period were interest rates on liabilities to foreign banks, which at the end of 2009 were sharply lower than interest rates on deposits by non-banking sectors. The interest rate on funds raised at the ECB was also down significantly in the first half of 2009, but was unchanged over the remainder of the period observed. A similar trend was seen in interest rates on debt securities issued by banks.

Figure 6.16: Average costs of banks' debt financing (left) and the structure of banks' new sources of funding used in the calculation of average funding costs (right) in percentages



Source: Bank of Slovenia

The proportion of funding accounted for by the most expensive sources increased.

Changes in the structure of funding had an adverse impact on associated costs, without which the decline in average costs of debt capital would be considerably more pronounced. Between the end of 2008 and February 2010, the proportion of deposits by non-banking sectors accounted for by short-term deposits fell 11 percentage points, while

[25] The banks' funding costs are calculated on a pre-tax basis. Costs of debt are calculated on the basis of the movement of interest rates on deposits by non-banking sectors, liabilities to the rest of the world (e.g. to banks in the form of loans and deposits, to the ECB and to other sectors) and debt securities (including subordinated debt securities). The costs of equity are estimated using a two-stage dividend discounting model for banks whose shares are listed on the Ljubljana Stock Exchange.

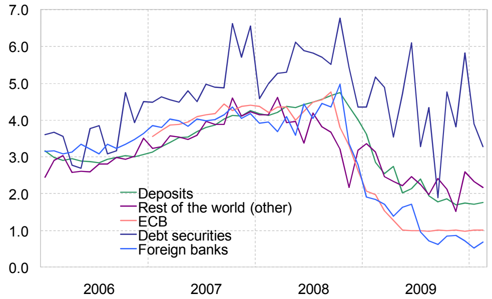
the proportion accounted for by sight and overnight deposits was down 2 percentage points. The proportion of long-term deposits was up 13 percentage points. The changing maturity of deposits by non-banking sectors was conditioned by the banks' relatively aggressive interest-rate policy in the final quarter of 2008 and in early 2009. In the absence of these changes, the decline in the overall interest rate would have been sharper.

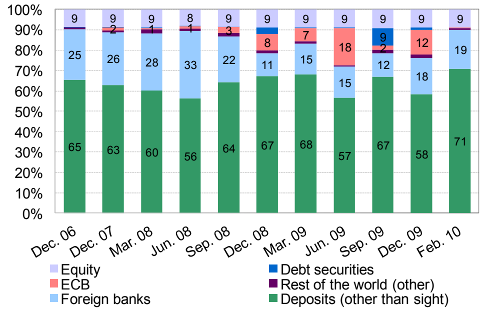
Marginal costs of debt capital

The decline in the costs of banks' most important new sources of funding came to a halt in the second half of 2009.

Contributing most last year to the lower marginal costs of debt capital were lower interest rates on new deposits by non-banking sectors and liabilities to foreign banks and the ECB. Interest rates on short-term and long-term deposits fell until February 2010. The overall interest rate on new deposits has remained virtually unchanged since the middle of 2009 owing to the lengthening of deposit maturities. Falling interest rates on new liabilities to foreign banks were heavily influenced by the shortening of maturities on this funding. Interest rates on liabilities to foreign banks have remained relatively stable since the middle of 2009. Liabilities to the ECB and foreign banks were most favourable in terms of costs, while the issue of debt securities (including subordinated instruments) was least favourable.

Figure 6.17: Marginal costs of banks' debt financing (left) and the structure of banks' new sources of funding used in the calculation of average funding costs (right) in percentages





Source: Bank of Slovenia

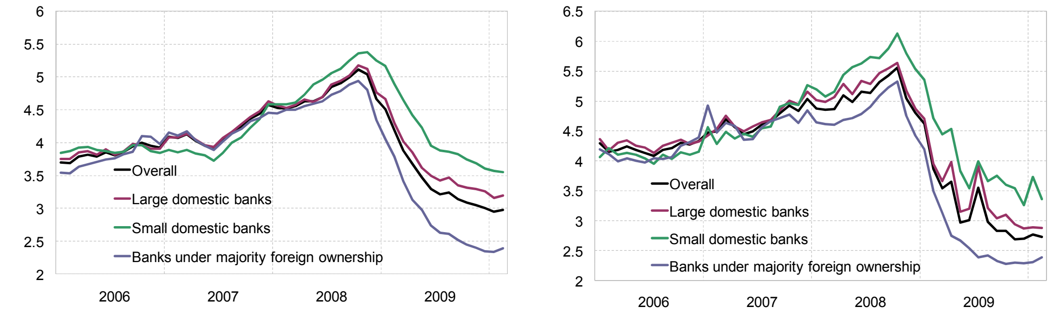
Difference in funding costs between bank groups

Significant differences in funding costs between individual bank groups.

The differences in funding costs between individual bank groups increased last year.[26] The spread in average funding costs between individual bank groups rose from 90 basis points at the end of 2008 to 126 basis points in 2009, before closing to 116 basis points by the end of February 2010. This is due to a sharper decline in average funding costs at the banks under majority foreign ownership than at the banks under majority domestic ownership. The spread in marginal costs fell by 13 basis points until the end of 2009, to stand at 97 basis points. This was due to the fact that the decline in marginal funding costs at the small domestic banks outstripped the decline recorded at the banks under majority foreign ownership and at the large domestic banks by 15 basis points. The reason the banks under majority foreign ownership recorded the lowest average and marginal costs lies in the difference in the costs and structure of funding by individual bank group. Alongside the lowest costs associated with individual forms of funding, the banks under majority ownership also have the most favourable structure of funding in terms of costs.

[26] The estimate of costs of equity is the same for all groups of banks owing to the limited number of bank shares listed on the Ljubljana Stock Exchange. The differences in bank funding costs arise solely due to differences in the costs of debt capital and the proportions of funding accounted for by equity by individual bank group.

Figure 6.18: Average (left) and marginal bank funding costs (right) in percentages

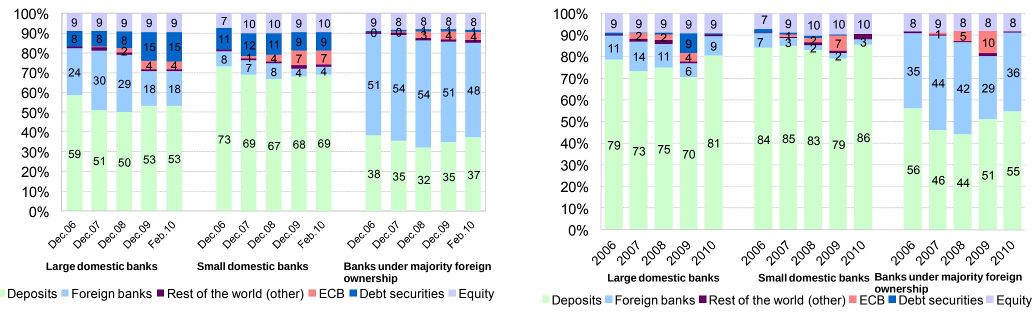


Sources: Bank of Slovenije, LJSE

The impact of the structure of funding on funding costs.

The structure of funding and the associated rate of change have a significant impact on total funding costs by individual bank group. The banks under majority foreign ownership have by far the largest proportion of the cheapest sources of funding (e.g. liabilities to the ECB and foreign banks). That proportion has fallen slightly over the last year on account of an increase in the proportion of deposits by non-banking sectors, both in terms of the stock and new transactions. In terms of the stock and new transactions, the small domestic banks have the highest proportion of the most expensive sources of funding (e.g. deposits by non-banking sectors and debt securities). The proportion of new funding accounted for by the cheapest sources (e.g. liabilities to the ECB) was up last year for this group of banks. At the large domestic banks, in 2009 there was a notable shift from one of the currently cheapest forms of funding (liabilities to foreign banks) to debt securities and funding from the ECB.

Figure 6.19: Structure of the stock of (left) and new (right) funding taken into account in the calculation of bank funding costs in percentages

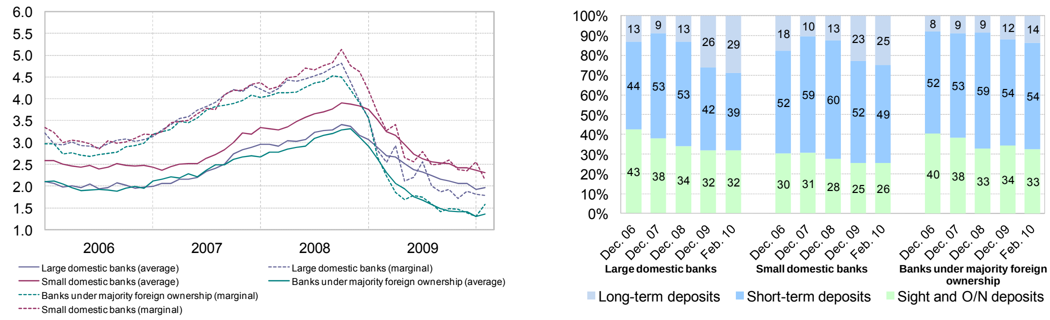


Source: Bank of Slovenia

The fall in interest rates on deposits by non-banking sectors was sharpest at the banks under majority foreign ownership.

Interest rates for the most important component of funding, i.e. deposits by non-banking sectors, fell sharply in all bank groups. From the end of 2008 until February 2010, interest rates on deposits fell by 177 basis points at the banks under majority foreign ownership, by 152 basis points at the small domestic banks and by 120 basis points at the large domestic banks. There was a shift to longer maturities in the maturity breakdown of deposits, which slowed the fall in the average interest rate in all bank groups.

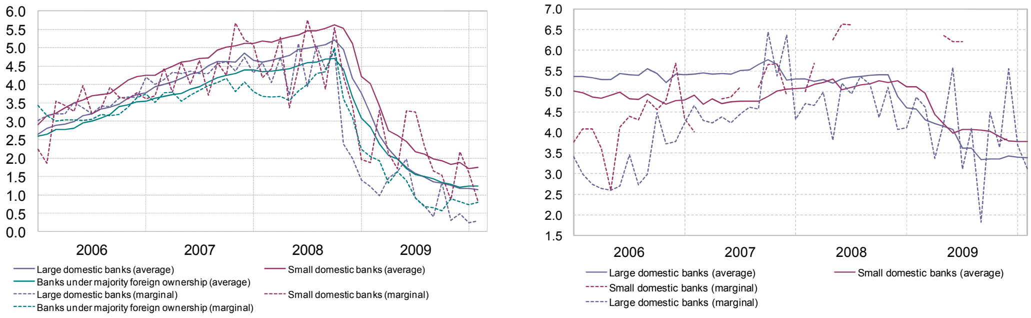
Figure 6.20: Average and marginal funding costs for deposits by non-banking sectors (left) and the maturity breakdown of deposits (right) by individual bank group



Source: Bank of Slovenia

Between the end of 2008 and February 2010, interests rates on existing liabilities to foreign banks recorded the sharpest fall (by 336 basis points) at the small domestic banks, followed by the large domestic banks (by 303 basis points) and the banks under majority foreign ownership (by 241 basis points). The interest rates on existing liabilities to foreign banks at the large domestic banks have been lower than those at the banks under majority foreign ownership since November 2008. This is due to shorter original maturities for liabilities to foreign banks at the domestic banks, and the fact that the domestic banks were obliged to repay mature liabilities to foreign banks. The banks under majority foreign ownership were able to refinance mature liabilities, albeit at a higher premium over reference interest rates.

Figure 6.21: Average and marginal funding costs for liabilities to foreign banks (left) and for debt securities[27] (right) by group of banks



Source: Bank of Slovenia

Interest rates on debt securities fell in the first half of 2009, in part owing to guarantees issued by the government. The banks under majority foreign ownership do not issue debt securities.

A rise in bank funding costs and the need to adjust the structure of bank funding to new conditions are expected.

The trend of declining bank funding costs will reverse in the near future. The costs of bank funding will gradually rise in line with the expectations of market participants regarding future movements in market interest rates and data from futures contracts. ECB funding will likely have shorter maturities, while the government is expected to reduce its stock of bank deposits. In line with an expected rise in market interest rates, the costs of other funding, particularly liabilities to foreign banks, will begin to rise. Slovenian banks will compete with foreign banks in obtaining new funding on the financial markets. A significant portion of foreign banks' debt securities and liabilities to the ECB and governments will mature this year, with governments issuing bonds to finance budget deficits. In such conditions, banks will be forced to optimise the structure of their funding in line with their size and majority ownership. In addition to relying on parent banks for funding, the banks under majority foreign ownership will also give increasing attention to attracting deposits by non-banking sectors. Funding from foreign banks will be less important for the large domestic banks than in previous year. Owing to the limited amount of domestic savings, debt securities will represent an important source of new funding for this bank group. These will be a comparably more expensive source owing to the relatively small size of Slovenian banks and the expected high supply of debt securities on the international financial markets.

[27] Debt securities include subordinated debt.

Table 6.6: Forms of funding as a proportion of total assets by individual bank group

(%)	Large domestic banks	Small domestic banks	Banks under majority foreign ownership	Banking system overall
	Liabilities to foreign banks			
2007	29.0	6.2	52.3	34.0
2008	27.7	6.8	52.3	33.8
2009	16.5	3.5	48.9	25.0
Mar. 2010	16.4	2.8	47.3	24.1
	Deposits by non-banking sectors			
2007	49.3	59.0	34.6	45.8
2008	47.8	56.7	31.1	43.3
2009	49.8	59.2	33.7	45.8
Mar. 2010	49.4	59.6	34.1	45.8
	Household deposits			
2007	31.9	30.6	20.8	28.6
2008	32.0	30.6	18.6	27.7
2009	30.5	30.3	18.2	26.8
Mar. 2010	30.9	31.0	19.5	27.6
	Government deposits			
2007	4.3	5.3	1.5	3.6
2008	4.3	6.6	2.5	3.9
2009	8.8	10.9	4.7	7.8
Mar. 2010	7.7	10.2	3.7	6.7
	Issued debt securities			
2007	2.8	6.5	0.0	2.3
2008	3.5	6.4	0.0	2.6
2009	10.0	5.2	0.0	6.7
Mar. 2010	10.2	5.1	0.0	6.9
	Liabilities to Eurosystem			
2007	0.3	0.8	0.5	0.4
2008	2.1	3.0	3.3	2.6
2009	4.0	6.4	3.7	4.1
Mar. 2010	3.9	6.1	3.9	4.1

Source: Bank of Slovenia

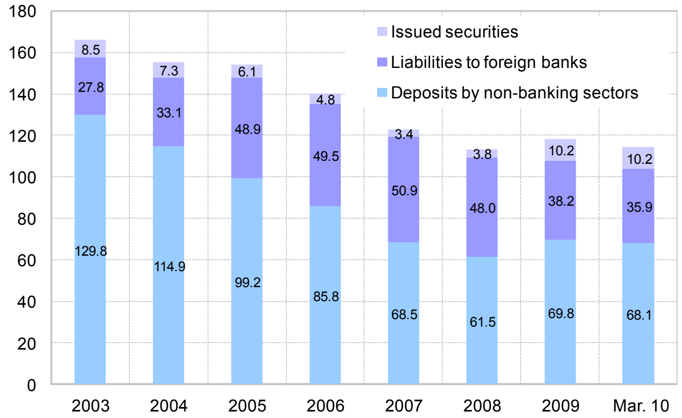
The differences in funding costs between individual bank groups are expected to narrow in the future. Interest rates on liabilities to foreign banks will rise in line with a rise in interbank interest rates, while the rise in interest rates on deposits by non-banking sectors will be slower.

6.3.6 Coverage of bank loans by sources of funding

Increase in coverage of loans by deposits owing to an increase in government deposits.

The trend of declining coverage of loans by deposits by non-banking sectors came to an end last year due to the increase in government deposits and lower lending growth. Coverage stood at 70% at the end of last year. The coverage of loans by deposits by non-banking sectors was up more than 8 percentage points on 2008. Excluding government deposits, the coverage of loans by deposits in October 2009 was more comparable with that recorded at the end of 2008.

Figure 6.22: Coverage of loans to non-banking sectors by liabilities to foreign banks and deposits by non-banking sectors in percentages



Source: Bank of Slovenia

There are large differences in the coverage of loans by forms of funding between individual bank groups owing to various funding structures.

Relatively large differences by individual bank group with regard to the coverage of loans to non-banking sectors by individual forms of funding persist. In December last year, the small domestic banks achieved the highest coverage of loans by deposits by non-banking sectors at 92.7%, followed by the large domestic banks at 83.9% and the banks under majority foreign ownership with the lowest coverage, at 42.5%.

Table 6.7: Coverage of loans by various forms of funding by bank group

(%)	Large domestic banks	Small domestic banks	Banks under majority foreign ownership	Banking system overall
	Coverage by deposits by non-banking sectors			
2007	80.0	92.2	43.7	68.5
2008	73.4	85.8	38.1	61.5
2009	83.9	92.7	42.5	69.8
Mar. 2010	81.8	93.3	40.9	68.1
	Coverage by household deposits			
2007	51.7	47.8	26.2	42.8
2008	49.2	46.3	22.7	39.4
2009	51.4	47.4	22.9	40.9
Mar. 2010	51.2	48.6	23.3	41.1
	Coverage by deposits by non-banking sectors other than government deposits			
2007	73.1	83.9	41.8	63.1
2008	66.8	75.8	35.0	55.9
2009	69.1	75.6	36.5	58.0
Mar. 2010	69.1	77.4	36.5	58.1
	Coverage by liabilities to foreign banks			
2007	47.0	9.7	66.0	50.9
2008	42.6	10.3	63.9	48.0
2009	27.8	5.5	61.6	38.2
Mar. 2010	27.1	4.3	56.7	35.9
	Coverage by issued debt securities			
2007	4.6	10.1	0.0	3.4
2008	5.4	9.7	0.0	3.8
2009	16.9	8.1	0.0	10.2
Mar. 2010	17.0	8.0	0.0	10.2

Source: Bank of Slovenia

Off-balance-sheet items and fiduciary operations

At 30.2%, last year's growth in off-balance-sheet items significantly outstripped growth in total assets (of 8%), the ratio of off-balance-sheet items to total assets having exceeded 200% at the end of 2009. Guarantees received accounted for more than two-thirds of the increase in off-balance-sheet items, while derivatives accounted for slightly less than 12%.

Table 6.8: Structure of and growth in off-balance sheet items in the banking sector at year-end in percentages

						Growth, %				
	2006	2007	2008	2009	Mar. 10	2006	2007	2008	2009	Mar. 10
Off-balance sheet items, EUR million	49,465	68,843	80,746	99,189	100,290	24.3	39.2	10.7	30.2	24.2
	Structure, %									
Letters of credit	0.3	0.3	0.1	0.1	0.1	-13.9	19.5	-37.1	-10.8	-6.0
Guarantees and assets pledged as collateral	5.4	4.6	4.1	3.6	3.6	10.8	17.8	10.1	2.5	8.2
Assumed financial liabilities	8.1	7.6	5.1	4.4	4.3	6.9	30.1	-15.1	-0.6	4.5
Derivatives	13.0	16.2	15.0	14.0	13.5	32.0	73.1	0.6	24.4	12.1
Depo and other securities records	13.4	12.0	8.2	6.4	5.7	24.7	24.2	-29.8	10.1	-13.8
Records of written-off claims	0.2	0.2	0.2	0.2	0.2	1.2	18.6	34.4	-1.2	0.8
Other off-balance sheet items	59.5	59.3	67.3	71.2	72.7	27.3	38.5	25.1	38.5	34.1
warranties received	36.9	36.8	45.0	49.3	51.1	26.3	38.7	31.1	47.3	41.1
guarantees and government sureties received	2.3	2.0	3.0	3.3	3.4	-3.3	21.1	65.2	42.5	40.7
other	20.4	20.5	19.4	18.7	18.2	33.9	40.0	10.3	19.1	16.9

Source: Bank of Slovenia

6.4 Profitability and performance indicators

The banking system's 2009 profit was down one half on 2008.

According to unaudited figures, the banks generated a pre-tax profit of EUR 160 million in 2009, down 48% on 2008. The main factors in the decline in income were the increase in impairment and provisioning costs and a decline in net interest. The banks were unable to compensate for the loss of income through higher non-interest income and by cutting operating costs.

Table 6.9: Banking sector income statement

	Amount, EUR million				Growth, %				Ratio to gross income, %			
	2007	2008	2009	Mar. 10	2007	2008	2009	Mar. 10	2007	2008	2009	Mar. 10
Net interest	816.4	944.6	924.7	255.8	18.3	15.7	-2.1	25.7	57.0	69.4	65.3	71.9
Net non-interest income	616.7	415.6	492.2	100.0	17.3	-32.6	18.4	-0.3	43.0	30.6	34.7	28.1
of which net fees and commissions	336.3	339.7	334.7	83.7	9.0	1.0	-1.5	4.7	23.5	25.0	23.6	23.5
of which net gain/loss on financial assets and liabilities held for trading	135.7	-114.6	41.5	-25.5	39.7	-184.4	-136.2	-238.2	9.5	-8.4	2.9	-7.2
Gross income	1433.0	1360.2	1417.0	355.8	17.9	-5.1	4.2	17.1	100	100	100	100
Operating costs	755.9	776.0	761.6	180.3	7.7	2.7	-1.9	0.1	52.7	57.1	53.7	50.7
labour costs	401.8	412.1	413.4	102.6	9.4	2.6	0.3	-0.5	28.0	30.3	29.2	28.8
Net income	677.1	584.2	655.4	175.5	31.9	-13.7	12.2	41.8	47.3	42.9	46.3	49.3
net impairments and provisioning	163.0	277.9	495.8	111.7	36.0	70.5	78.5	58.1	11.4	20.4	35.0	31.4
Pre-tax profit	514.2	306.3	159.5	63.8	30.6	-40.4	-47.9	20.2	35.9	22.5	11.3	17.9
Taxes	102.5	58.6	38.3	12.0	12.8	-42.8	-34.7	6.7	7.1	4.3	2.7	3.4
Net profit	411.7	247.7	121.3	51.8	36.0	-39.8	-51.1	23.8	28.7	18.2	8.6	14.6

Source: Bank of Slovenia

Net interest income, interest margin and net non-interest income

Declining proportion of the banks' gross income accounted for by net interest.

The proportion of gross income accounted for by net interest declined to 65.3% last year, while the proportion accounted for by net non-interest income was up. The negative growth in interest income was a result of weak lending activity, loans generally bearing higher interest rates than other forms of assets. Higher non-interest income resulted in positive growth in banks' gross income last year. The interest margin on interest-bearing assets fell to 1.98%.

Table 6.10: Average effective asset and liability interest rates calculated from interest income and expenses, interest spread and net interest margin in percentages

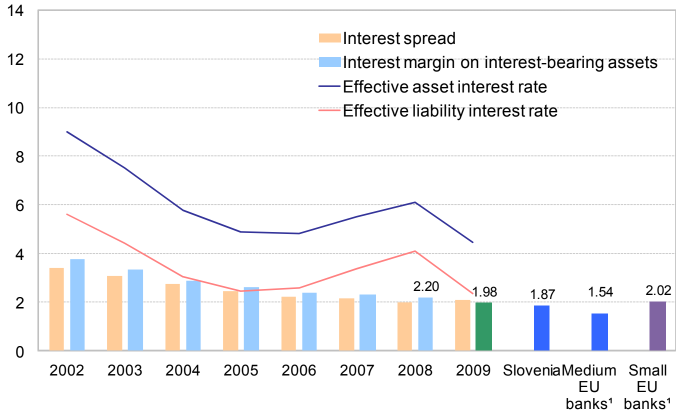
(%)	2002	2003	2004	2005	2006	2007	2008	2009
Average asset interest rate	9.01	7.52	5.78	4.90	4.81	5.51	6.09	4.45
Average liability interest rate	5.62	4.44	3.04	2.44	2.59	3.37	4.11	2.61
Effective interest rate spread	3.39	3.08	2.74	2.46	2.22	2.14	1.98	1.84
Net interest margin on interest-bearing assets	3.76	3.35	2.87	2.62	2.37	2.33	2.20	1.98

Source: Bank of Slovenia

The interest spread and net interest margin declined again last year.

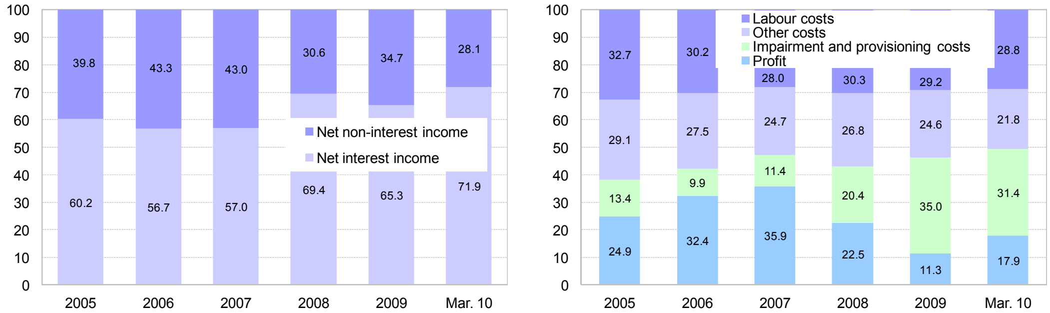
The main factors in the 1.6 percentage point fall in effective asset interest rates were a change in the structure of interest-bearing assets (as a result of a decline in the proportion of loans) and the fall in interest rates on the financial markets. The restructuring of liabilities in favour of relatively less expensive, but unstable, funding resulted in a fall in effective liability interest rates of 1.5 percentage points.

Figure 6.23: Average effective asset and liability interest rates calculated from interest income and expenses, interest spread and interest margin in percentages



Note: [1] The separate figures for the interest margin are for 2009 in Slovenia and for 2008 for EU Member States reporting under international accounting standards, and were calculated as the ratio of net interest income to total assets. The interest margin for EU banks was taken as the net interest margin for medium-sized banks and small banks.
Sources: ECB, EU Banking Sector Stability, August 2009.

Figure 6.24: Proportion of banks' gross income accounted for by net interest and non-interest income (left) and disposal of gross income (right) in percentages



Source: Bank of Slovenia

Bank operating costs

A decline in the proportion of the banks' gross income accounted for by operating costs.

The banks' operating costs were down 2% last year. The large domestic banks were the most effective at cost control, and succeeded in reducing costs. Growth in labour costs also fell throughout the year, but remained positive. The importance of controlling operating costs for banks' performance will increase further this year. The success of improving banks' cost effectiveness will depend largely on whether higher impairment and provisioning costs will result in a lower return on equity over the longer term.

A sharp increase in impairment and provisioning costs in 2009.

The impairments and provisions created last year by the banks exceeded those created in 2008 by EUR 218 million or 78%. This is a reflection of the deteriorating credit portfolio in the harsh economic conditions. The ratio of impairment and provisioning costs to gross income, which nearly doubled in 2008, rose further last year to reach 35%. The banks under majority foreign ownership recorded the sharpest growth in impairment and provisioning costs, but recorded a lower ratio of impairment and provisioning costs to gross income than the other bank groups last year. The movement of impairment and provisioning costs in the coming years is largely dependent on the development of the economic crisis.

Table 6.11: Loans, and impairment and provisioning costs

(%)	Large banks	Small banks	Foreign banks	Banking system
Growth in loans to non-banking sectors in 2009	0.3	9.0	-0.5	0.6
Growth in capital requirements	6.3	5.8	-0.5	4.3
Growth in impairments and provisioning in 2009	72.8	51.9	120.4	78.5
Ratio of impairments and provisioning to gross income in 2009, %	39.4	36.1	25.1	35.0
Ratio of impairments and provisioning to gross income in 2008, %	23.7	27.6	11.6	20.4

Source: Bank of Slovenia

Bank performance indicators

Bank performance indicators deteriorated in 2009.

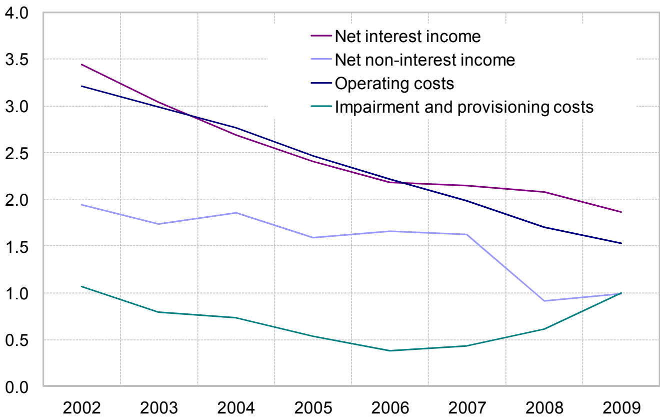
The banking system's ROE declined by 4.3 percentage points last year to just 3.83%. The main factors in the decline were the significant fall in interest income and the increase in impairment and provisioning costs. In the future the banking system's ROE is also expected to be sharply lower than that achieved prior to the outbreak of the financial turmoil.

Table 6.12: Bank performance indicators in percentages

(%)	2003	2004	2005	2006	2007	2008	2009
ROA	1.00	1.06	1.00	1.25	1.36	0.68	0.32
ROE	11.89	12.72	12.72	15.07	16.29	8.14	3.83
Costs / gross income	63.28	62.32	61.74	57.76	52.75	57.05	53.75
Interest margin on interest-bearing assets	3.35	2.94	2.62	2.37	2.33	2.21	1.98
Interest margin on total assets	3.05	2.70	2.42	2.19	2.16	2.09	1.87
Non-interest margin	1.63	1.72	1.60	1.67	1.64	0.91	0.99
Gross income / average assets	4.68	4.42	4.02	3.86	3.80	3.00	2.86

Source: Bank of Slovenia

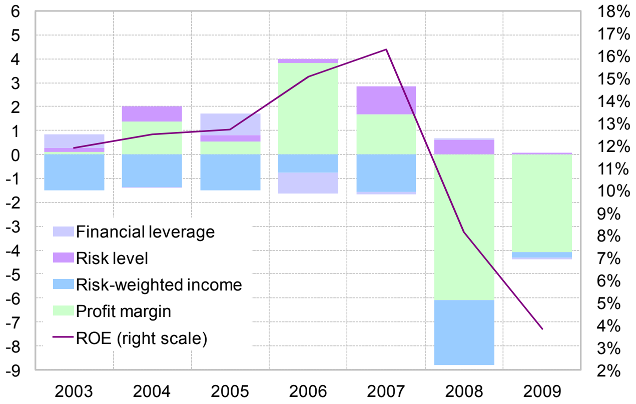
Figure 6.25: Net interest income, net non-interest income, operating costs and net provisioning as a percentage of average assets



Source: Bank of Slovenia

The movement of the banks' ROE can be analysed by breaking down profitability into four components: profit margin, risk-weighted income, risk level and financial leverage.

Figure 6.26: Movement in ROE, and impact of four factors on the direction of the movement in ROE



Source: Bank of Slovenia

A decline in the profit margin acted to reduce the banks' profitability in 2009, while the contribution of risk-weighted income declined compared with 2008.[28] The risk level acted to increase profitability, albeit minimally.

The profit margin had a pronounced impact in reducing the banking system's profitability considerably, as pre-tax profit was down sharply in 2009 in the context of an increase in gross income.

Table 6.13: Breakdown of ROE into four factors

Year	Profit margin: pre-tax profit / gross income	*	Risk-weighted income: gross income / risk-weighted assets	*	Risk level: risk-weighted assets / total assets	*	Financial leverage: total assets / capital	=	Profitability: ROE
2005	0.25		0.06		0.65		12.82		0.127
2006	0.32		0.06		0.66		12.12		0.151
2007	0.36		0.05		0.71		12.05		0.163
2008	0.23		0.04		0.77		12.17		0.081
2009	0.11		0.04		0.78		11.92		0.038

Source: Bank of Slovenia

6.5 Risks in the banking sector

Survey of major risks

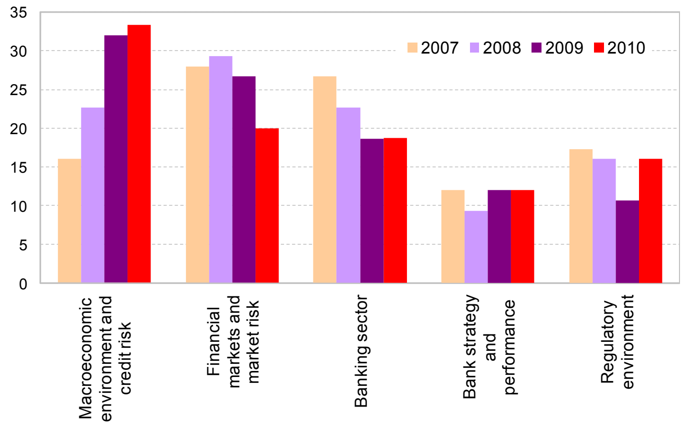
According to the banks, risks associated with the macroeconomic environment will be highest in the future, particularly risks associated with the regulatory environment.

Every year selected banks use a survey to assess their exposure to five types of risk over the next 12 month period. According to these banks, risks associated with the macroeconomic environment increased sharply in the years following the outbreak of the financial turmoil, while in the future they primarily expect increased risks associated with the regulatory environment. In this regard, the two responses most frequently given by banks from possible survey responses were international regulatory changes and risks associated with corporate governance and the reporting burden.

The banks were more adamant than ever in their expression of risks associated with the macroeconomic environment for the period to March 2011, and were nearly united with regard to three key reasons. The first is credit risk and developments in the credit cycle, including the deteriorating credit ratings of borrowers, relatively high indebtedness and the deteriorating quality of collateral. The second are changes on the real estate market, while the third is low economic growth and economic conditions in Europe. The majority of banks assess that credit risk and the risk of unfavourable changes on the real estate market will increase. The banks do not consider domestic public debt as one of the three most important factors of macroeconomic risk.

[28] Owing to the inclusion of operational risks in capital requirements, the introduction of Basel II in 2008 reduces the comparability of capital requirements with risk-weighted assets for periods prior to 2008.

Figure 6.27: Results of 2007 to 2010 surveys on main origins of risk for the coming year in percentages[29]



Sources: Bank of Slovenia, annual bank surveys

Banks expect the pressure of risks associated with the financial markets to be moderate. Movements in interest rates, developments on the capital markets, and access to and the costs of funding are expected to have an adverse impact on banks, while changes in exchange rates will be of less importance. Risks associated with business strategies and business models are expected to remain unchanged. Risks associated with the functioning of the interbank market and competitive pressures owing to the large number of banks and the range of products and services on the market are expected to have a moderate impact on the former. The reasons behind risks associated with business strategies and banks' operations are heterogeneous, while risks associated with penetrating new markets, operational risks and fluctuations in profit are insignificant. Increased risk associated with the regulatory environment is an important warning, as it is the only risk that, according to banks, is expected to increase notably in the future. It can be concluded from the banks' response that international regulatory changes are the underlying reason for this expected increase that this involves the introduction of measures in the scope of Basel III. The other reason, i.e. risks associated with corporate governance and the reporting burden, reflects the increased complexity of bank governance in the uncertain conditions and the banks' expectations of a response to these conditions from supervisors.

6.6 Liquidity risk and refinancing risk

The continuing turmoil on the international financial markets last year had a significant impact on Slovenian banks that borrowed heavily in the rest of the world prior to the financial turmoil. The tightening of funding conditions on the international financial markets was reflected in the shortening of funding maturities and, in the context of less favourable funding conditions, primarily in a contraction in refinancing in the rest of the world, which resulted in net debt repayments to the rest of the world in the amount of EUR 3.2 billion.

In the context of debt repayments to banks in the rest of the world and after the replacement of foreign funding with government deposits and funding at the ECB, the banks are more exposed to refinancing risk, as these forms of funding have shorter maturities. Moreover, these short-term, temporary sources cannot ensure quality lending growth.

The increase in bank funding last year was only reflected in an increase in the banks' secondary liquidity. Growth in household deposits in 2009 was down sharply on growth in previous years owing to the unstable economic conditions, and led to a significant increase in the proportion of bank funding via the government. The increase in government deposits contributed to nearly three-quarters of the overall increase in deposits by non-banking sectors last year, and to more than half of the increase in total assets.

[29] The sum of the columns for each year is 100%.

The banking system's liquidity position normalised last year, as was reflected in liquidity ratios. The average values of these ratios exceeded those achieved in 2008, but fluctuated. The coverage of loans to non-banking sectors by deposits by non-banking sectors did not change significantly last year, while the coverage of loans to non-banking sectors by funding from banks in the rest of the world declined owing to debt repayments by banks.

6.6.1 Impact of the instability on the financial markets on the funding conditions in the rest of the world

Debt repayments to banks in the rest of the world

The banks made significant debt repayments in the rest of the world in 2009. The proportion of total assets accounted for by liabilities to foreign banks was down from nearly one-third to one-quarter.

The banks began operating in conditions of significantly limited foreign funding following the escalation of the financial turmoil in autumn 2008. The stock of newly raised loans in the rest of the world was down sharply. The banks made net debt repayments in 2009 due to the maturing of loans. They were able to compensate for a portion of lost funding by issuing debt securities, through government deposits and with funds raised at the ECB. By the end of February 2010 liabilities to foreign banks were down 19.4% in year-on-year terms to stand at 24% of the banking system's total assets, after standing at nearly 31.4% in March last year. In 2009 the large domestic banks made the largest debt repayments to foreign banks at EUR 2.8 billion, followed by the banks under majority foreign ownership at EUR 317 million and the small domestic banks at EUR 103 million. The banks under majority foreign ownership made the highest net debt repayments in the first quarter of this year.

Funding in the rest of the world was down on the previous year.

Liabilities to foreign banks stood at EUR 13.9 billion in February 2010.[30] The majority of net funding in the rest of the world was generated by the banks under majority foreign ownership (58%) in the form of new transactions, despite the fact that these banks account for a significantly smaller proportion of banking transactions than the domestic banks. It was again easier last year for the banks under majority foreign ownership, which primarily borrow from their parent banks, to access funding in the rest of the world. However, the stock of newly raised loans in this bank group was down on the stock prior to the financial turmoil. Similar to 2008, the majority of loans raised were short-term.

The proportion of short-term liabilities was comparable to last year, while the breakdown of maturities of up to 1 year changed.

At 23.5%, the proportion of short-term liabilities to foreign banks in February 2010 was down on last February's figure of 27.5%. There was a change in the maturity breakdown over the course of one year. The proportion accounted for by liabilities with a maturity of up to 6 months decreased, while the proportion accounted for by liabilities with a maturity of between 6 months and 1 year was up. The proportion of debt with a maturity of up to 1 year in February 2010 was highest at the banks under majority foreign ownership (29.5%), and was practically unchanged with respect to February 2008. That same proportion was down more than 10 percentage points at the large domestic banks, at 16.8%, primarily owing to higher repayments in the first half of last year. The small banks face the highest proportion of liabilities to foreign banks maturing over the next 12 months, at 77.8%.

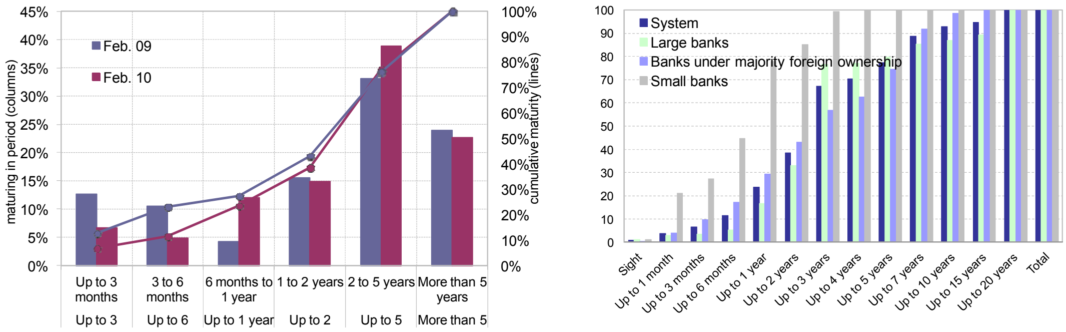
The decline in debt to the rest of the world is fastest at the small domestic banks; however, the proportion of this type of funding is negligible in this bank group.

Hence the decline in debt to the rest of the world is fastest at the small banks. This type of funding however represents less than 3% of all liabilities in this bank group.

There are also significant differences between the bank groups in the segment of maturities of 2 to 3 years, where the banks under majority foreign ownership held merely 14% of their liabilities to foreign banks as at the end of February 2010, and the large banks a high proportion of 43.5%. This high proportion of liabilities in the segment of 2 to 3 years at the large domestic banks is a result of last year's debt securities issues. In February 2010 the vast majority (76.4%) of banks' total liabilities to banks in the rest of the world had maturities of more than 1 year, and more than one-fifth (22.7%) had maturities of more than 5 years.

[30] In addition to liabilities to the rest of the world from loans raised and deposits at foreign banks, the figure includes debt securities issued by banks in the rest of the world.

Figure 6.28: Maturing of liabilities to foreign banks by maturity interval (left) and bank group (right) in percentages



Source: Bank of Slovenia

Table 6.14: Maturing of liabilities to foreign banks and maturity breakdown as at 28 February 2010 for the banking system and by bank group in percentages

	Cumulative maturing of liabilities to foreign banks				Breakdown of liabilities by maturity			
	System	Large domestic banks	Banks under majority foreign ownership	Small domestic banks	System	Large domestic banks	Banks under majority foreign ownership	Small domestic banks
Total, EUR million	13,922	6,975	6,812	134				
	Breakdown, %							
Overnight, sight	0.8	1.2	0.5	1.3	0.8	1.2	0.5	1.3
Up to 1 months	3.6	2.8	4.1	21.1	2.8	1.7	3.6	19.9
1 to 3 months	6.7	3.4	9.7	27.2	3.1	0.6	5.6	6.1
3 to 6 months	11.6	5.3	17.3	44.7	4.9	1.9	7.6	17.5
6 months to 1 year	23.6	16.8	29.5	77.8	12.0	11.5	12.2	33.1
1 to 2 years	38.4	33.1	43.0	85.2	14.9	16.3	13.5	7.4
2 to 3 years	67.2	76.6	56.9	99.3	28.7	43.5	13.9	14.1
3 to 4 years	70.3	77.2	62.7	100.0	3.1	0.6	5.8	0.7
4 to 5 years	77.3	79.7	74.5		7.0	2.5	11.8	
5 to 7 years	88.7	85.3	92.0		11.4	5.6	17.5	
7 to 10 years	92.8	87.0	98.6		4.1	1.7	6.6	
10 to 15 years	94.6	89.2	100.0		1.7	2.2	1.4	
15 to 20 years	100.0	100.0	100.0		5.4	10.8	0.0	
More than 20 years								
Total					100.0	100.0	100.0	100.0

Source: Bank of Slovenia

The continuing financial turmoil was reflected in a decline in new loans raised in the rest of the world, at both the banks under majority domestic ownership and at the banks under majority foreign ownership. The latter more than halved their newly raised loans in the rest of the world, from EUR 2.5 billion to EUR 1.25 billion. The banks under majority foreign ownership reduced their stock of newly raised loans in the rest of the world by 26%, from EUR 2.35 billion to EUR 1.74 billion.

Table 6.15: New loans of banks raised at banks in the rest of the world, by maturity and currency

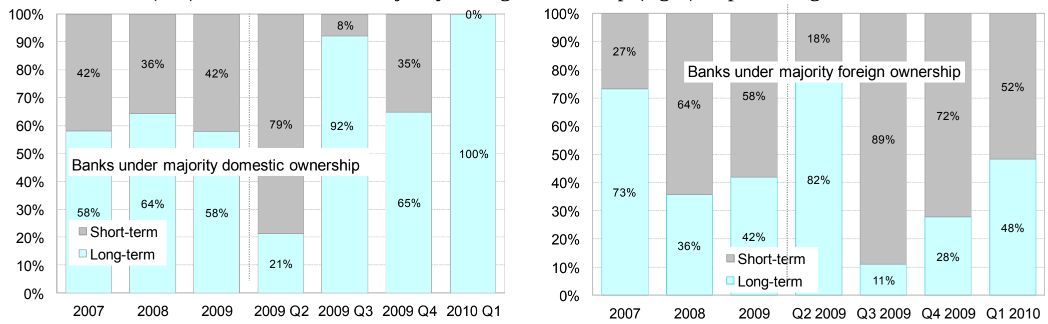
	Loans by maturity, EUR million			Breakdown by currency, %			
	Total	Short-term	Long-term	CHF	EUR	SIT	USD
2006	1,904.2	539.2	1,365.0	6.8	87.8	5.4	0.0
2007	5,304.8	1,877.8	3,426.9	8.2	91.5	-	0.3
2008	4,862.0	2,408.8	2,453.2	5.2	93.5	-	1.3
2009	2,984.8	1,536.4	1,448.5	11.2	88.8	-	0.0
Q1 2009	320.8	318.3	2.5	21.0	79.0	-	0.0
Q2 2009	1,253.1	543.4	709.7	5.1	94.9	-	0.0
Q3 2009	911.7	385.4	526.3	7.8	92.2	-	0.0
Q4 2009	499.2	289.2	209.9	26.4	73.6	-	0.0
Q1 2010	292.1	145.9	146.1	25.9	74.1	-	0.0

Source: Bank of Slovenia

The ratio of new short-term loans to long-term loans raised in the rest of the world was unchanged in 2009. The stock of new loans raised in the rest of the world was down sharply, by 36.2% for short-term loans and by 40.9% for long-term loans. The domestic banks reduced their new short-term borrowings in the rest of the world by EUR 366 million to EUR 526 million, and their long-term borrowings by EUR 893 million to EUR 721 million. The situation was similar for the banks under majority foreign ownership. They reduced their new short-term borrowings in the rest of the world by EUR 506 million to EUR 1,010 million, and their new long-term borrowings by EUR 111 million to EUR 728 million. The banks under majority foreign ownership, which last year raised 58% of all new loans in the rest of the world, were primarily funded by raising new short-term loans.

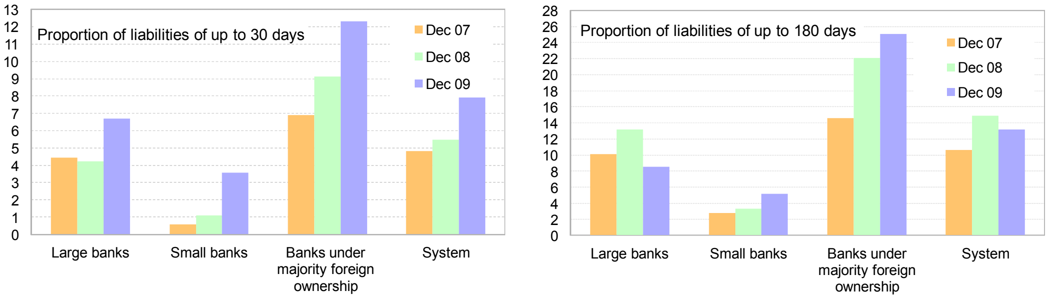
The maturity breakdown of newly raised loans was similar to 2008.

Figure 6.29: Maturity breakdown of new loans for banks under domestic ownership (left) and banks under majority foreign ownership (right) in percentages



Source: Bank of Slovenia

Figure 6.30: Liabilities to foreign banks as a proportion of total liabilities with a residual maturity of up to 30 days (left) and up to 180 days (right), by bank group

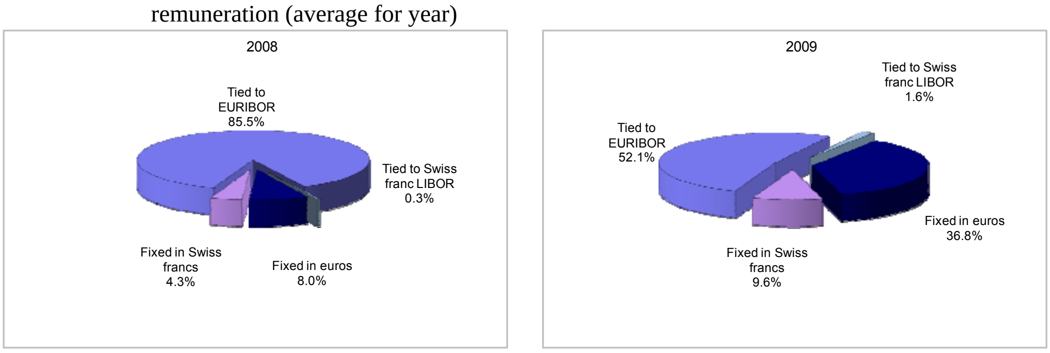


Source: Bank of Slovenia

The breakdown of borrowing from the rest of the world by type of remuneration also changed last year. The proportion of all new loans accounted for by euro loans raised by banks with a fixed interest rate increased to 36.8%, while half of all new loans are still raised with a variable interest rate (tied to the EURIBOR).

The proportion of loans with a fixed interest rate increased.

Figure 6.31: Breakdown of banks' new loans in the rest of the world by type of remuneration (average for year)



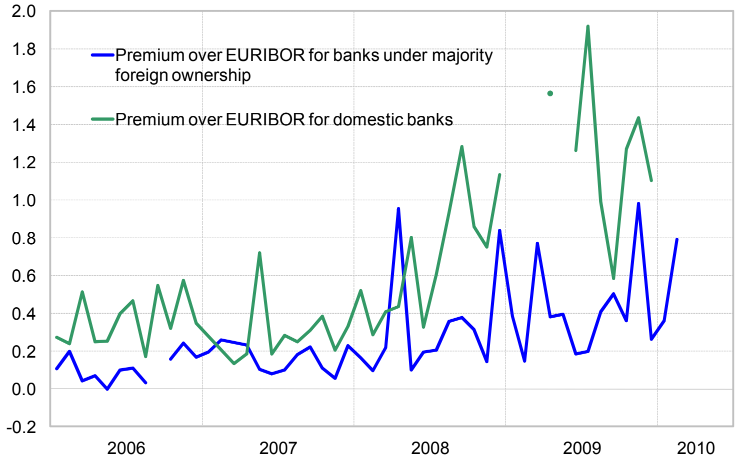
Source: Bank of Slovenia

The continuing financial turmoil and economic crisis were reflected in higher risk premiums over reference interest rates on loans raised in the rest of the world. In their

Risk premiums on bank borrowing from the rest of the world increased.

borrowing from the rest of the world, the banks under majority foreign ownership achieved an average premium over the EURIBOR of 0.41 percentage points in 2009, compared with 0.33 percentage points in 2008, while the domestic banks achieved a premium of 1.27 percentage points, compared with 0.69 percentage points in 2008. The banks under majority domestic ownership thus borrowed at less favourable terms from the rest of the world.

Figure 6.32: Premium over the EURIBOR for banks' loans raised in the rest of the world, with regard to majority ownership, in percentage points



Source: Bank of Slovenia

Banks' increased dependence on government deposits and Eurosystem instruments, and the impact of refinancing risk

The banks compensated for last year's drop in funding from the rest of the world by issuing debt securities, through government deposits and via funds raised at the Eurosystem.

The banks made cumulative debt repayments to the rest of world in the amount of EUR 3.2 billion last year, and an additional EUR 650 million in the first quarter of this year. The banks only partially compensated for the drop in this form of funding with other longer-term sources, such as bond issues by three banks in the nominal amount of EUR 2.1 billion.[31] The drop in funding in 2009 was compensated for primarily by government deposits. The net increase in government deposits totalled EUR 2.1 billion in 2009, accounting for nearly 73% of the total increase in deposits by non-banking sectors and 56% of the increase in the banking system's total assets. The importance of bank funding obtained at the ECB increased back in the final quarter of 2008, immediately following the outbreak of the financial turmoil. The banks' liabilities to the ECB stood at EUR 2.1 billion at the end of 2009, equivalent to more than 4% of the banking system's total assets. Last year's net increase in household deposits was down on the growth recorded in previous years.

Given the short-term nature of funds raised last year, which do not represent a stable source of funding, banks are exposed to relatively high refinancing risk. A portion of funding that cannot be rolled over and the banks' inability to compensate for government deposits and liabilities to the ECB with more sustainable funding can lead to a contraction in total assets. The contraction in the banking system's total assets in the first quarter of 2010 is already the consequence of declining government deposits placed at banks.

In 2009 banks funded nearly four-fifths of the increase in total assets via predominantly short-term sources. The increase in this type of funding was not reflected in an increase in lending activity, but in an increase in investments in securities and an increase in claims against banks.

Bank borrowing and the maturity of their debt from ECB operations

According to figures from the first quarter of 2010, Slovenian bank are faced with maturing liabilities to the Eurosystem of EUR 2.1 billion and maturing deposits by the Slovenian Ministry of Finance in the amount of EUR 1.2 billion by the end of 2010. Maturing debt accounts for nearly nine-tenths of last year's net increase in total assets.

[31] In July 2009 NLB issued a 3-year bond in the nominal amount of EUR 1.5 billion. Abanka Vipa issued a 3-year bond in the nominal amount of EUR 500 million in September, while SID banka generated funds in the amount of EUR 126 million in December through the issue of notes.

Maturing bank debt to the rest of the world, which continues this year, must also be taken into account. EUR 3.3 billion in liabilities to the rest of the world could mature by February 2011.

Last year the banks borrowed at the ECB via LTROs.

The banks borrowed in the total amount of EUR 1.05 billion after the ECB first offered a refinancing instrument at the end of June 2009 with a maturity of 12 months and full allotment at an interest rate of 1%. A second 12-month LTRO was executed under the same conditions at the end of September 2009, but the demand by Slovenian banks was merely EUR 122 million. Bank borrowing was up sharply again during the last of three 12-month LTROs in mid-December last year, when the banks borrowed a total of EUR 728 million. Total bank borrowing from the ECB increased to EUR 2.1 billion.

Table 6.16: Maturing of the banking system's liabilities to the ECB

	Cumulative maturing of liabilities to Eurosystem				Breakdown of liabilities by maturity			
	Large domestic banks	Small domestic banks	Banks under majority foreign ownership	System	Large domestic banks	Small domestic banks	Banks under majority foreign ownership	System
Total, EUR million	1,250	272	542	2,065				
	Breakdown, %							
Up to 3 months	52.8	39.9	82.1	58.8	52.8	39.9	82.1	58.8
3 to 6 months	56.0	52.8	90.8	64.7	3.2	12.9	8.7	5.9
By 23 December 2010	100.0	100.0	100.0	100.0	44.0	47.2	9.2	35.3
Total					100.0	100.0	100.0	100.0

Source: Bank of Slovenia

The proportions of the banking system's total liabilities accounted for by liabilities to the ECB do not vary significantly by bank group. At the end of March 2010 these liabilities accounted for 6.1% of the total liabilities of the small domestic banks, and for 3.9% of the total liabilities of both the large domestic banks and the banks under majority foreign ownership.

Bank borrowing in the form of government deposits and their maturity

The stock of government deposits at banks was down EUR 0.6 billion in the first half of this year, and is expected to fall a further EUR 1.2 billion by the end of the year.

The main source for last year's increase in the banking system's deposits was the issue of bonds. In 2009 the Slovenian government issued three bonds with a total nominal value of EUR 4 billion and several treasury bills with a total nominal value of EUR 1.06 billion. The government issued two additional bonds in the first quarter of 2010 with a total nominal value of EUR 2.5 billion. Despite last year's improvement in the maturity breakdown of deposits by non-banking sectors in favour of long-term deposits, the breakdown is gradually turning less favourable given the residual maturity of government deposits. The stock of government deposits placed at banks was down EUR 0.6 billion in the first quarter of 2010, which, alongside the banks' debt repayments to the rest of the world, was the main reason for the contraction in total assets.

Table 6.17: Maturing of banks' liabilities from deposits by the Slovenian Ministry of Finance placed at banks

	Cumulative maturing of Ministry of Finance deposits				Breakdown of liabilities by maturity			
	Large domestic banks	Small domestic banks	Banks under majority foreign ownership	System	Large domestic banks	Small domestic banks	Banks under majority foreign ownership	System
Total, EUR million	2,035	304	403	2,742				
	Breakdown, %							
Up to 3 months	10.5	18.8	60.3	18.8	10.5	18.8	60.3	18.8
3 months to 1 year	41.4	35.9	88.8	47.7	30.8	17.1	28.5	29.0
1 to 2 years	45.4	47.4	100.0	53.7	4.1	11.5	11.2	5.9
More than 2 years	100	100		100	54.6	52.6	0.0	46.3
Total					100.0	100.0	100.0	100.0

Source: Bank of Slovenia

There were relatively large differences between the bank groups at the end of the first quarter of 2010 in terms of the proportion of the banks' liabilities accounted for by government deposits. The proportion of government deposits was highest at the small domestic banks (10.2%), followed by the large domestic banks (7.7%) and the banks under majority foreign ownership (4.1%).

Box 6.2: Assessment of the banks' funding needs in 2010

In 2010 the banks will face the maturing of certain sources of funding obtained during the financial turmoil. These primarily include funds raised in LTROs at the ECB and via government deposits. Moreover, a significant portion of liabilities to foreign banks will also mature. Hence the question arises as to how banks will replace these forms of funding or whether the availability of funding will become a key limiting factor in lending growth and growth in total assets.

Current forecasts of lending growth indicate growth in loans to non-banking sectors of around 4% at the end of 2010 and of around 10% the following year. According to these assumptions, growth in loans would amount to EUR 1.3 billion in 2010 and EUR 3.5 billion in 2011. The banks should not face major funding difficulties in 2010, if they achieve projected growth in household deposits of 7.9%. Alongside growth in household deposits, the banks would have to secure an additional increase in other funding of slightly less than EUR 250 million. Taking into account the growth recorded in the first quarter, banks would have to ensure merely an additional EUR 100 million in other funding by the end of the year. In 2011 banks would have to fund an increase in loans to non-banking sectors of EUR 1.86 billion via other sources. We expect however that the conditions on the international financial markets will stabilise by 2011. We also assess that the majority of the restructuring of the banking system's liabilities will be carried out in 2010. We thus expect more uncertainty this year in securing sufficient funding.

Table 6.18: Requisite increase in funding with respect to forecasts of growth in loans to non-banking sectors and household deposits

	Stock, EUR million		Growth forecast, %		Stock forecast, EUR		Increase, EUR million	
	2009	Mar. 10	2010	2011	2010	2011	2010	2011
Loans to non-banking sectors	33,744	34,074	4.0	10.2	35,087	38,662	1,343	3,575
Household deposits	13,801	13,988	7.9	11.5	14,898	16,611	1,096	1,713
Requisite increase in other funding							247	1,862

Source: Bank of Slovenia

According to figures for March 2010, the banks will be required to compensate for up to EUR 6.2 billion in expired funding merely to maintain total assets at their current level. Should banks achieve growth forecasts for specific assets items (e.g. growth in loans to non-banking sectors of 4%, total growth in other asset items of 2.6% and growth in total assets of 3.5%), they would need to secure additional funding of EUR 2.6 billion by the end of the year.

The latest figures do not take into account government-guaranteed bank bonds already issued in 2010 and secured guarantees for bonds not yet issued, totalling EUR 1.1 billion. If in the future banks roll over the same percentage (63%) of mature liabilities to foreign banks, the stock of these liabilities will decline by a maximum of EUR 930 million and not by the projected EUR 2.5 billion. This means that banks could compensate for a decline in liabilities to foreign banks with funds raised via the issue of debt securities. Banks will still be able to refinance maturing liabilities to the ECB, should they not be able to renew these liabilities on the interbank market. Assuming 7.9% growth in household deposits and 6% growth in corporate deposits (non-financial corporations and NMFIs) in 2010, banks will be able to compensate for maturing government deposits of around EUR 1.15 billion by the end of the year.

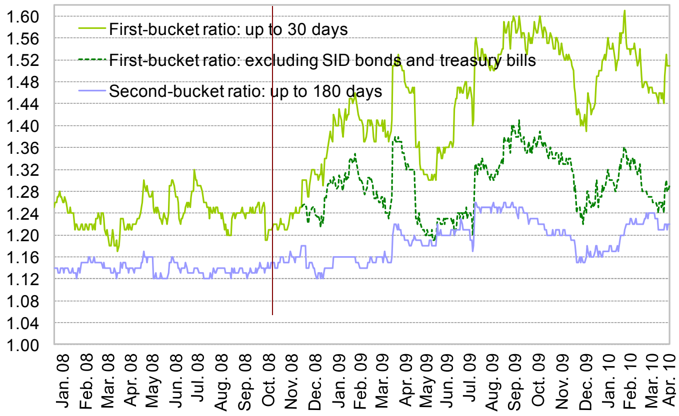
The current conditions indicate that banks will be able to compensate for funding maturing this year by restructuring their liabilities. Should refinancing be successful, this year banks would require an additional EUR 247 million to fund lending growth, but considerably more (EUR 1.86 billion) next year. If however the domestic and international interbank markets do not recover significantly and banks refrain from issuing bonds owing to withholding tax, growth in total assets could be negative in 2010. Banks will also close gaps in their balance sheets by reducing claims against the ECB and foreign banks and by reducing investments in securities.

6.6.2 Liquidity ratios

The first bucket liquidity ratio was up in 2009.

The first-bucket liquidity ratio averaged 1.46 in 2009, up 0.22 on the previous year. The increase was the result of bank operations related to the issue of SID banka d.d. bonds and the issue of Slovenian treasury bills, and deposits placed at banks by SID banka and the government.

Figure 6.33: Daily liquidity ratios for first and second buckets of liquidity ladder



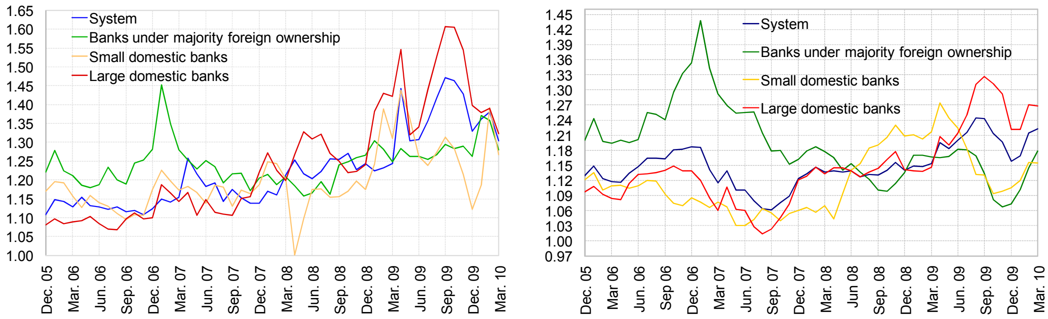
Source: Bank of Slovenia

The values of ratios fluctuated sharply last year.

The value of the first-bucket liquidity ratio fluctuated sharply in 2009 owing to the substantial increase in government deposits at banks, the increase in the banks' liabilities to the ECB, the issue of bank securities and the repayment of liabilities to the rest of the world.

The large domestic banks recorded the highest average ratio in 2009 of 1.46. The small banks recorded an average ratio of 1.29, while that of the banks under majority foreign ownership was slightly lower at 1.27), although the value of ratio did not change significantly with respect to 2008.

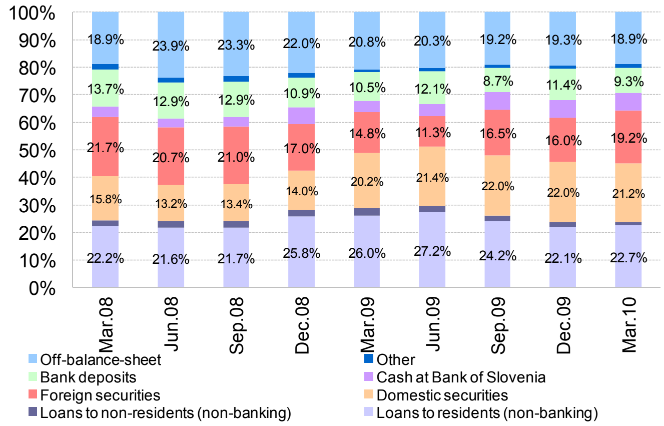
Figure 6.34: Liquidity ratios for first bucket (left) and second bucket (right) of liquidity ladder by individual bank group, monthly averages



Source: Bank of Slovenia

In the formation of the average first-bucket liquidity ratio there were again structural changes last year in investments included in the coverage of the ratio. There was a decrease in the proportion of short-term loans and an increase in the proportion of foreign securities.

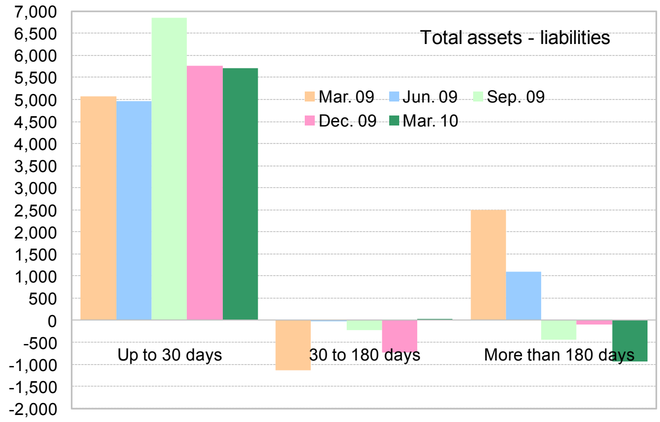
Figure 6.35: Structure of assets taken into account in the calculation of the first-bucket liquidity ratio (with a residual maturity of up to 30 days) in percentages



Source: Bank of Slovenia

The liquidity gap, calculated as the difference between total assets and liabilities defined in the liquidity ladder methodology, was extremely long for the bucket with a residual maturity of up to 30 days. Last year's sharp increase in the gap was primarily due to an increase in the banks' secondary liquidity and an increase in investment-grade investments in government securities and foreign marketable securities rated BBB or higher.

Figure 6.36: Liquidity gap as the difference between total assets and total liabilities defined in the liquidity ladder methodology in EUR million



Source: Bank of Slovenia

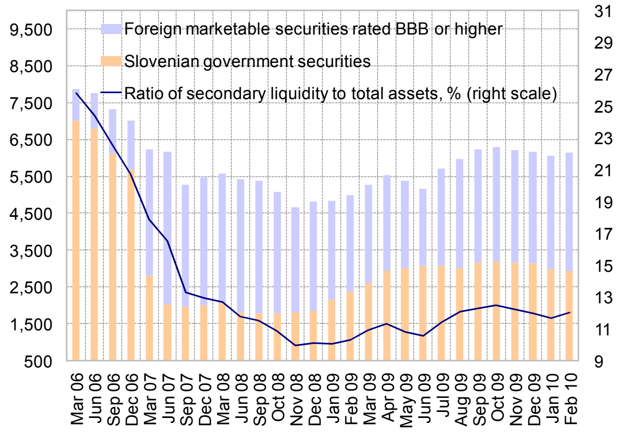
6.6.3 Other structural liquidity indicators

The proportion of total assets accounted for by secondary liquidity rose.

The proportion of total assets accounted for by secondary liquidity rose again last year owing to the more rapid growth in secondary liquidity than total assets. The figure fluctuated at slightly less than 12% in the first quarter of 2010. The stock of structural liquidity averaged EUR 6.1 billion over the same period, and was up more than EUR 1 billion on the first quarter of 2009.

There are relatively large differences in the proportions of secondary liquidity between the banks under majority domestic ownership and those under majority foreign ownership. The large domestic banks recorded the highest proportion at 15.4%, followed by the small domestic banks (12.6%), while the proportion recorded by the banks under majority foreign ownership is significantly lower owing to the relatively low proportion of total assets accounted for by securities in this bank group.

Figure 6.37: Changes in the amount of secondary liquidity (monthly averages in EUR million) and as a proportion of total assets in percentages



Note: Secondary liquidity is calculated from liquidity ladder data as the sum of the monthly average of Slovenian government securities (taking into account Bank of Slovenia bills up to March 2007 inclusive) and foreign marketable securities rated BBB or higher.

Source: Bank of Slovenia

Changes in structural liquidity indicators last year reflect deposits by non-banking sectors (the government) as the prevailing form of bank funding, stalled lending activity, debt repayments to banks in the rest of the world and an increase in the banks' most liquid investments.

Last year's increase in coverage of loans by deposits by non-banking sectors was a reflection of an increase in deposits by non-banking sectors and stalled lending activity.

The ratio of deposits by non-banking sectors and loans to non-banking sectors rose to nearly 70% in 2009. However, last year's increase in this ratio was a result of a temporary increase in government deposits and stalled lending activity. The coverage of short-term loans by short-term deposits increased again last year, but fell again in the first quarter of this year to approach the level recorded at the end of 2008 owing to the decline in deposits. The coverage of loans by deposits improved at all bank groups last year. At 93%, the small banks stood out in terms of coverage at the end of the first quarter of 2010, followed by the large domestic banks at 82% and the banks under majority foreign ownership at merely 41%. The increase in the proportion of total assets accounted for by debt securities and the ECB liquidity indicator, which shows the ratio of the sum of cash and claims against banks to liabilities to banks, was primarily the result of an increase in the banks' liabilities last year in the context of a simultaneous increase in the banking system's secondary liquidity in the form of securities and in the most liquid forms of the banks' assets. The decline in the indicator, which shows the ratio of liabilities to foreign banks to loans to non-banking sectors, reflects debt repayments to the rest of the world.

Table 6.19: Selected ratios in balance sheet items defining bank liquidity in percentages

(%)		Large domestic banks	Small domestic banks	Banks under majority foreign ownership	Overall
Ratio of deposits by non-banking sectors to loans by non-banking sectors	2005	110.9	136.6	69.1	99.2
	2006	99.5	122.5	54.2	85.8
	2007	80.0	92.2	43.7	68.5
	2008	73.4	85.8	38.1	61.5
	2009	83.9	92.7	42.5	69.8
	Mar. 10	81.8	93.3	40.9	68.1
Ratio of short-term deposits to short-term loans to non-banking sectors	2005	154.8	121.4	138.4	146.9
	2006	122.1	111.3	117.6	119.8
	2007	113.3	94.3	89.5	105.1
	2008	93.2	86.3	84.7	90.3
	2009	99.4	89.8	112.9	101.2
	Mar. 10	85.9	83.4	94.1	87.5
Ratio of liabilities to foreign banks to loans to non-banking sectors	2005	38.3	14.3	76.1	48.9
	2006	40.4	13.2	72.9	49.5
	2007	47.0	9.7	66.0	50.9
	2008	42.6	10.3	63.9	48.0
	2009	27.8	5.5	61.6	38.2
	Mar. 10	27.1	4.3	56.7	35.9
Ratio of liabilities to foreign banks to total assets	2005	20.3	7.1	46.6	26.9
	2006	22.9	7.2	50.6	29.9
	2007	29.0	6.2	52.3	34.0
	2008	27.7	6.8	52.3	33.8
	2009	16.5	3.5	48.9	25.0
	Mar. 10	16.4	2.8	47.3	24.1
Ratio of debt securities to total assets	2005	29.5	28.9	19.4	26.5
	2006	24.8	20.3	13.5	21.2
	2007	19.9	17.0	7.2	16.0
	2008	17.2	14.8	5.8	13.5
	2009	18.1	18.9	7.2	15.0
	Mar. 10	17.8	18.8	7.2	14.9
ECB liquidity indicator (ratio of cash and claims against banks to liabilities to banks)	2005	48.4	98.7	30.3	41.3
	2006	45.5	116.0	25.1	38.2
	2007	37.3	48.8	16.9	29.4
	2008	39.2	55.8	14.8	29.1
	2009	72.9	61.3	18.7	45.3
	Mar. 10	68.8	62.7	10.5	40.4

Source: Bank of Slovenia

6.7 Credit risk

The banks faced a sharp deterioration in the financial positions of their clients in 2009, as a direct consequence of declining economic activity, resulting in the deterioration in the credit portfolio. The banks tightened collateral requirements and applied stricter criteria regarding the justification of projects they intend to finance.

Arrears in the settlement of liabilities to banks are lengthening due to rising illiquidity in the economy. The banks are downgrading their clients. They have intensified the creation of impairments and provisions, partly as a result of the insufficient creation of impairments in the previous period of high economic growth. Given the significant discrepancies between longer arrears and previously created impairments and provisions in certain sectors, growth in impairments at banks can be expected to continue in the future, as the quality of collateral deteriorates in the uncertain economic conditions.

Credit risk at banks has increased, in particular with regard to non-financial corporations, sole traders and non-residents. Holding companies, which stand out in terms of the length of arrears and very low coverage of claims by collateral, also represent significant credit risk. Uncertainty on the real estate market is also resulting in rising credit risk vis-à-vis the construction sector and associated activities. The small banks are exposed to additional credit risk owing to the high concentration of exposures to SMEs in their portfolios. The liquidity of SMEs has tightened further due to their position at end of the cash flow chain.

6.7.1 Credit standards

Alongside declining demand for financing at banks as a result of declining economic activity, the low lending growth in 2009 was also affected by banks' tightened credit standards, which are more difficult to meet by weakened corporates. The tightening of banks' credit standards was primarily seen in the stricter assessment of clients and projects. The scope and quality of required collateral were both increased. Long-term loans are conditional on the prospects of projects. Short-term loans to finance current operations are also not as accessible as they were prior to the financial turmoil.

Loan-to-income (LTI) ratio

There was no change in the banks' highest LTI ratio in 2009.

In 2009 the banks saw no change in their average, internally-defined LTI ratio on loans to households. Banks take into account several factors in determining this ratio: in addition to the level of wages, additional income and loan maturity, employment security is gaining in importance during the period of rising unemployment. The LTI ratio fluctuates between individual banks in a range from one-third to two-thirds of the borrower's monthly income.

There were no significant changes in the terms of household borrowing at banks in loan agreements concluded in 2009. The proportion of new consumer loans on which the LTI ratio exceeds 33% was down slightly on 2008, while the proportion of consumer loans on which the LTI ratio exceeds 50% was up. There were also minor changes in the proportion of housing loans on which the LTI exceeded the aforementioned thresholds. It is not however possible to draw conclusions on the tightening of approval terms for loans to households in 2009.

Table 6.20: Loan-to-income (LTI) ratio

	Average maximum LTI under bank's business policy	Actual proportion of newly approved housing loans with		Actual proportion of newly approved consumer loans with	
		LTI >= 33%	LTI >= 50%	LTI >= 33%	LTI >= 50%
2008	53.3	57.8	15.4	47.5	9.2
2009	53.5	57.1	14.8	44.0	10.4

Note: LTI is the ratio of the loan instalment to the borrower's income.
Source: Bank survey

Loan-to-value (LTV) ratio

Tightening of the LTV ratio on loans with real estate collateral.

In 2009 the banks further tightened their collateral terms for loans to both households and corporates. The maximum LTV ratio on corporate and household loans with real estate collateral allowed by internal bank standards averaged 63%. The actual LTV ratios on new household loans in 2009 were lower than the internal standards, particularly on non-housing loans to households, where the LTV ratio was down 3.7 percentage points on 2008 at 42%. The LTV ratio on housing loans with real estate collateral averaged 55.5%. A more favourable LTV ratio was seen on new corporate loans in 2009, but tightened with respect to 2008. Given the risk to which banks are exposed owing to developments on the real estate market, they are expected to apply stricter criteria on real estate collateral.

Table 6.21: Average loan-to-value (LTV) ratio for loans with real estate collateral

	LTV for real estate collateral	
	2008	2009
Corporate loans	68.7	63.8
Non-housing loans to households	45.5	41.8
Housing loans	56.3	55.5

Note: LTV – ratio of loan to value of pledged collateral.
Source: Bank survey

Additional requirements by banks on loans with securities collateral.

In 2009 the banks further tightened their requirements regarding the LTV ratio on loans with securities collateral. This ratio is higher than the LTV ratio on loans with real estate collateral, but this is a result of banks' demands for additional collateral, which is not included in the calculation of the LTV ratio, in addition to securities.

Having risen sharply in 2008 as a result of the fall in stock market prices, the amount of loans on which the LTV ratio exceeded internal requirements began to decline again in 2009. Such loans, in the amount of EUR 290 million, represented 1.3% of the stock of corporate loans in 2009, compared with 2.9% in 2008. Banks obtained additional collateral for the majority of such loans in 2009.

Table 6.22: Average loan-to-value (LTV) ratio for loans with securities collateral

	LTV for securities / mutual funds units collateral, %		Loans whose LTV rose above the internally defined LTV in 2009		Loans for which banks obtained additional collateral in 2009	
	2008	2009	value, EUR million	proportion of all corporate loans, %	value, EUR million	proportion of all corporate loans, %
Corporate loans	88.3	82.0	290.0	1.3	246.0	1.1
Non-housing loans to households	62.1	57.4	13.7	0.4	6.7	0.2
Housing loans	102.7	78.9	0.5	0.0	0.0	0.0

Note: LTV – ratio of loan to value of pledged collateral.
Source: Bank survey

6.7.2 Portfolio quality

The banks began downgrading their risk assessments of the credit portfolio owing to the escalation of the financial turmoil in the final quarter of 2008 and the deteriorating financial position of clients. Declining lending growth and the resulting decline in access to new clients via newly concluded transactions to which banks assign lower risk assessments contributed further to the falling average quality of bank portfolios.

High growth in banks' non-performing claims in 2009.

At the end of 2009 non-performing claims were up 30% on the end of 2008 in the context of 5.6% growth in classified claims. By the end of 2009 the stock of impairments and provisions was up 30% in year-on-year terms at EUR 1.8 billion. The coverage of classified claims by impairments was up 0.7 percentage points on the previous year at 3.7%.

The high increase in non-performing claims, and in impairments and provisions is an unavoidable consequence of insufficiently critical risk assessments during the period of high lending growth prior to the outbreak of the financial turmoil. The increase in impairments and provisions could have been lower if banks had focused less on the current financial positions of their clients during the favourable climate and period of high lending growth, and focused more on assessing clients' debt servicing capacity over the entire period of exposure. The deepening of the corporate sector's liquidity problems indicate that the banking system's credit portfolio will continue to deteriorate.

Figure 6.38: Year-on-year growth in classified and non-performing claims (left) and the breakdown of claims by credit rating (right) in percentages

Source: Bank of Slovenia

In 2009 the banks downgraded 1.9% of classified claims from less risky claims (rated A and B) to higher-risk claims. The proportion of C rated claims in particular was up, by 1.6 percentage points to 2.6%. A portion of this portfolio is likely to be downgraded in the coming period to high-risk ratings. The proportion of non-performing claims (rated D and E) rose by 0.4 percentage points during the year to stand 2.2% at the end of 2009, before rising further in February 2010 to reach 2.3% of classified claims.

Table 6.23: Breakdown of classified claims and coverage of claims by impairments and provisions

	31 December 2008			31 December 2009			28 February 2010		
	Classified claims	Impairments	Coverage of claims by impairments, %	Classified claims	Impairments	Coverage of claims by impairments, %	Classified claims	Impairments	Coverage of claims by impairments, %
Total, EUR million	47,129	1,403	3.0	49,757	1,827	3.7	48,679	1,882	3.9
	Breakdown, %			Breakdown, %			Breakdown, %		
A	74.4	8.8	0.4	70.7	7.0	0.4	69.6	7.0	0.4
B	22.7	34.4	4.5	24.5	30.8	4.6	25.4	30.8	4.7
C	1.0	8.7	24.8	2.6	16.2	23.2	2.6	16.2	24.1
D	1.0	20.8	62.3	1.4	24.7	62.9	1.5	25.5	63.9
E	0.8	27.2	100.0	0.8	21.2	100.0	0.8	20.5	100.0

Source: Bank of Slovenia

By bank group: the risk assessment of the quality of the credit portfolio deteriorated most at the large domestic banks in 2009.

The most significant shift in the structure of the credit portfolio in 2009 occurred at the large domestic banks. This bank group's proportion of lower-risk claims (rated A and B) was down by an average of 2.4 percentage points on the end of 2008 to stand at 94.6%. The majority of this change (1.9 percentage points) was on account of claims downgraded to the C rating, while the proportion of non-performing claims rose to 2.3% of classified claims. Accordingly, the coverage of classified claims by impairments and provisions was up 0.7 percentage points on the end of 2008 at 4%.

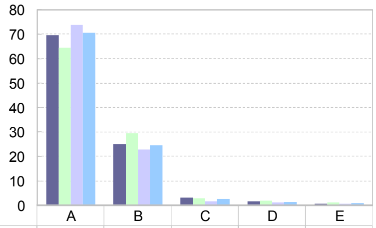
The small banks are most conservative in assessing clients.

In the context of the deteriorating economic and financial conditions in 2008, the small banks responded quickest by increasing the proportion of the overall portfolio accounted for by non-performing claims (rated D and E). That proportion rose to 3.1% by the end of 2009, the highest among the three bank groups. The small banks were also more conservative in the past in their assessments of clients and in the creation of impairments and provisions. Their coverage of classified claims by impairments is highest at 4.8%. In addition to the small banks' greater prudence in assessing the quality of clients, the structure of their portfolio also contributes to the higher level of impairments. Compared with the other bank groups, a relatively larger portion of the small banks' portfolio is accounted for by domestic corporates, which have been hit harder by the economic crisis than other groups of clients.

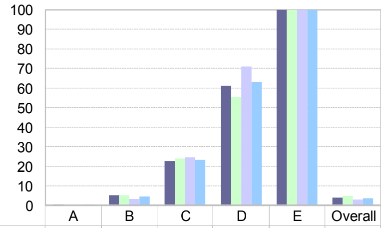
Deterioration in the quality of the credit portfolio was least notable at the banks under majority foreign ownership.

Among all bank groups, the proportion of the portfolio accounted for by the highest-rated claims is highest at the banks under majority foreign ownership, at 96.5%. Even the deterioration in the quality of this bank group's portfolio was below the banking system's average: the proportion of non-performing claims was up merely 0.1 percentage points, while the other two groups recorded a rise of 0.5 percentage points. The below-average deterioration in the portfolio of the banks under majority foreign ownership is a result of more optimistic risk assessments at these banks, and also owing to the more favourable structure of clients in terms of credit risk, with a relatively high and growing proportion of claims against households.

Figure 6.39: Breakdown of classified claims (left) and average coverage of classified claims by impairments (right) by bank group for the end of 2009 in percentages



	A	B	C	D	E
Large domestic banks	69.5	25.1	3.0	1.6	0.7
Small domestic banks	64.5	29.4	3.0	1.9	1.2
Banks under majority foreign ownership	73.8	22.8	1.6	1.1	0.8
Overall	70.7	24.5	2.6	1.4	0.8



	A	B	C	D	E	Overall
Large domestic banks	0.4	5.2	22.7	61.2	100.0	4.0
Small domestic banks	0.5	5.1	24.0	55.3	100.0	4.8
Banks under majority foreign ownership	0.3	3.2	24.7	70.9	100.0	2.9
Overall	0.4	4.6	23.2	62.9	100.0	3.7

Source: Bank of Slovenia

Non-financial corporations: the portfolio accounted for by non-financial corporations is deteriorating, particularly with respect to holding companies.

The proportion of non-performing claims against non-financial corporations reached 2.6% at the end of 2009, up one-third on a year earlier. The deterioration of the portfolio accounted for by non-financial corporations is most evident in the financial and insurance activities sector (non-financial holding companies), which banks continued to assess as largely low-risk as late as 2008, with a proportion of non-performing claims of merely 0.1%. During the course of the year, the liquidity problems faced by holding companies led to the partial repayment of claims from collateral and a sharp increase in impairments and provisions.

High growth in non-performing claims was evident in the sectors of construction, wholesale and retail trade, accommodation and food service activities, and other business activities.

High growth in non-performing claims was also evident in the sectors of construction, wholesale and retail trade, accommodation and food service activities, and other business activities. The proportion of non-performing claims in the portfolio of construction companies remained below the overall average for non-financial corporations. Banks downgraded a high proportion of these companies to C-rated claims, which could lead to further downgrading to non-performing claims (rated D and E) in the future. Impairments and provisions for construction companies are above-average, reflecting banks' awareness of the rising credit risk to which they are exposed in this sector.

In terms of the low coverage of claims by impairments, banks classify electricity, gas and water supply, and transportation and storage as notably low-risk sectors.

Table 6.24: Proportions of non-performing claims of non-financial corporations by sector

	Impairments of classified claims, EUR million		Coverage of classified claims by impairments, %		Classified claims rated D and E		
					value, EUR million	as % of total classified claims	
	2008	2009	2008	2009		2008	2009
Agriculture, forestry, fishing, mining	24	23	8.0	7.0	16.9	6.2	4.9
Manufacturing	287	342	4.5	5.2	220.9	2.8	3.4
Electricity, gas, water; remediation	8	10	1.1	1.0	1.9	0.2	0.1
Construction	105	154	3.6	4.9	71.9	1.2	2.2
Wholesale and retail trade	203	222	4.0	4.6	157.9	2.4	3.2
Transportation and storage	24	40	1.1	1.7	13.9	0.3	0.6
Accommodation and food service activities	22	28	3.7	4.0	20.9	2.0	2.9
Information and communication activities	14	27	2.0	4.0	8.9	0.9	1.2
Financial and insurance activities	50	133	2.2	7.5	46.9	0.1	2.6
Real estate activities	31	46	2.6	3.8	19.9	0.9	1.6
Professional, scientific and technical activities	83	123	4.0	5.8	82.9	2.4	3.9
Public services	11	14	2.9	3.1	4.9	0.9	0.8
Overall	862	1,162	3.5	4.6	657.9	1.8	2.6

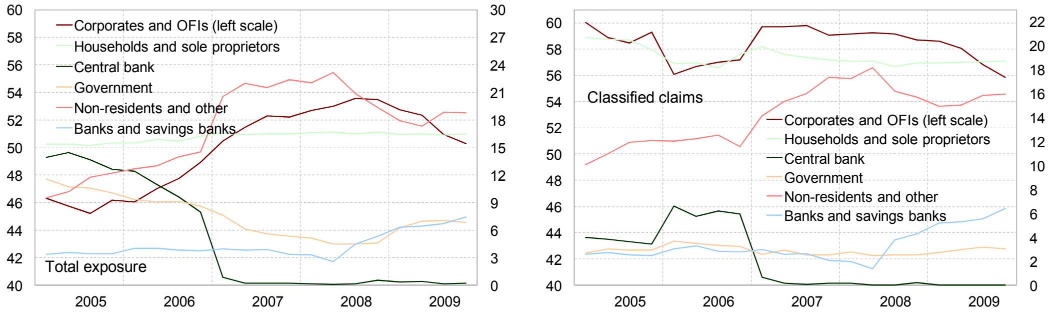
Source: Bank of Slovenia

6.7.3 Portfolio diversification

The proportion of total exposure accounted for by corporates was down.

The decline in the banks' lending activity in 2009 varied by sector, and was reflected in the structure of the banking system's credit portfolio. Non-financial corporations, as a proportion of both total bank exposure and classified claims, recorded the sharpest drop, of around 3 percentage points. The proportion of the banking system's portfolio accounted for by loans to households was up in line with the higher growth in these loans. There was no significant change in the banks' exposure to non-residents, although there were structural shifts. The proportion of the banking system's portfolio accounted for by foreign non-financial corporations was down 1 percentage point, while the proportion accounted for by foreign financial institutions was up by a similar amount. The proportion of investments in domestic banks and savings banks has increased since the middle of 2008. The higher proportions of the banking system's portfolio accounted for by the government and the domestic and foreign financial sectors is a reflection of the banks' prudence in the context of the simultaneous need for the most liquid assets and net debt repayments to the rest of the world.

Figure 6.40: Percentage breakdown of total bank exposure (left) and classified claims (right) by sector



Source: Bank of Slovenia

The proportion of the banking system's credit portfolio accounted for by the sectors of manufacturing and wholesale and retail trade declined.

The largest portion of the banking system's portfolio of non-financial corporations is accounted for by corporates from the sectors of manufacturing and wholesale and retail trade. Owing to the shorter business process in these sectors, growth in borrowing by these companies adjusted quicker to declining demand. In the case of wholesale and retail trade, it actually led to debt repayments. In the context of a slowdown in financing, the proportion accounted for by these sectors has fallen in recent years, in contrast to the sectors of construction, transportation and storage and real estate activities, which actually increased their borrowing at banks during the credit crunch. At the end of 2009 these three sectors accounted for 26.7% of classified claims against non-financial corporations, up 4 percentage points on the last year prior to the crisis (2006).

Table 6.25: Banks' classified claims against non-financial corporations by sector, structure and year-on-year growth, in EUR million and percentages

	Loans to non-financial corporations[1]			Classified claims against non-financial corporations					
	total	breakdown, %		total	breakdown, %	change in breakdown, percentage points		year-on-year growth, %	
	2009	2008	2009	2009	2009	2008	2009	2008	2009
Agriculture, forestry, fishing, mining	284	1.2	1.4	327	1.3	0.1	0.1	28.9	11.7
Manufacturing	5,611	26.7	26.7	6,533	26.0	-0.2	0.2	12.9	1.9
Electricity, gas, water; remediation	615	2.5	2.9	974	3.9	0.0	0.7	12.2	25.3
Construction	2,267	9.8	10.8	3,160	12.6	0.1	0.7	15.2	7.0
Wholesale and retail trade	4,008	20.2	19.1	4,844	19.3	-0.1	-1.1	13.2	-4.3
Transportation and storage	2,102	9.0	10.0	2,327	9.3	0.4	0.8	19.9	11.0
Accommodation and food service activities	624	2.7	3.0	697	2.8	0.1	0.4	18.7	15.6
Information and communication activities	500	2.3	2.4	684	2.7	-0.1	0.0	8.3	0.1
Financial and insurance activities	1,674	10.1	8.0	1,767	7.0	-0.4	-2.1	9.6	-22.0
Real estate activities	1,117	5.3	5.3	1,218	4.9	0.2	0.1	19.1	2.4
Professional, scientific and technical activities	1,825	8.4	8.7	2,125	8.5	-0.3	0.0	9.5	1.3
Public services	399	1.8	1.9	439	1.7	0.2	0.2	28.2	10.7
Total	21,026	100.0	100.0	25,096	100.0			13.8	1.1

Note: [1] Loans are in gross amounts, excluding impairments.
Source: Bank of Slovenia

Negative growth in claims against foreign non-financial institutions.

At 5.6%, growth in classified claims in 2009 was slightly more than one-third of the growth recorded in 2008. After recording the highest growth in the years prior to the financial turmoil, growth in the financing of foreign non-financial institutions was negative in 2009. Last year the banks maintained high growth in the financing of less-risky sectors, such as electricity, gas and water supply and public services.

Table 6.26: Increases in loans by sector in EUR million

	Manufacturing	Construction	Trade	Transportation and storage	Accommodation and food service	Financial and insurance	Real estate activities	Professional, scientific and technical	Non-financial corporations overall
2005	542.9	141.2	489.6	135.3	62.0	296.5	87.1	145.6	1,844.9
2006	591.0	312.7	182.9	236.4	53.3	256.6	292.6	231.9	2,321.0
2007	713.4	618.8	719.1	350.1	84.3	774.8	283.2	554.7	4,541.4
2008	942.5	426.5	721.4	320.3	118.0	238.2	242.1	165.2	3,415.6
2009	50.5	236.9	-186.3	228.4	72.9	-433.4	23.0	68.7	237.9

Note: [1] Loans are in gross amounts, excluding impairments.
Source: Bank of Slovenia

By bank group: high growth in claims against households at the banks under majority foreign ownership.

The proportion of classified claims against the household sector, which is already high, was up nearly 2 percentage points at the banks under majority foreign ownership, to reach 22.5%. At the same time, the proportion accounted for by this client segment was down 0.4 percentage points at the large domestic banks and down 0.7 percentage points at the small domestic banks.

All bank groups increased their impairments in the majority of sectors and client segments.

All the bank groups increased their coverage of claims by impairments in almost all sectors, with minor exceptions in sectors that previously had above-average impairments. The banks under majority foreign ownership have the lowest coverage by impairments, which is valid for the portfolio overall and for individual sectors and client segments. The coverage of claims by impairments at this bank group is also below average in sectors where these banks are more exposed than the other bank groups, which confirms that the banks under majority foreign ownership are generally less conservative when assessing the quality of clients. These banks only created relatively high impairments for foreign non-financial institutions, to which their exposure is below average, at 2.8% compared with 8.2% of classified claims for the entire banking system.

Table 6.27: Breakdown and average risk (coverage of claims by impairments) of rated claims in 2009 by bank group in percentages

	Breakdown, %				Coverage of classified claims by impairments, %			
	Banking sector	Large domestic banks	Small domestic banks	Banks under majority foreign ownership	Banking sector	Large domestic banks	Small domestic banks	Banks under majority foreign ownership
Agriculture, forestry, fishing, mining	0.7	0.7	0.8	0.7	6.9	7.4	13.3	4.3
Manufacturing	13.6	13.5	12.9	14.0	5.4	6.4	6.5	3.1
Electricity, gas, water; remediation	2.0	1.7	1.2	2.7	1.0	1.0	2.7	0.9
Construction	6.7	7.1	8.5	5.4	5.0	5.4	5.7	3.9
Wholesale and retail trade	10.0	8.3	13.5	12.5	4.7	5.6	5.9	3.4
Transportation and storage	4.9	4.9	1.5	5.8	1.9	2.2	4.1	1.3
Accommodation and food service activities	1.6	1.5	1.0	1.9	4.7	5.4	7.9	3.2
Information and communication activities	1.4	1.6	0.6	1.3	4.1	4.7	2.5	2.9
Financial and insurance activities	15.5	18.2	13.6	10.6	2.6	2.5	3.9	2.4
Real estate activities	2.5	2.0	3.1	3.4	3.8	4.9	4.4	2.5
Professional, scientific and technical activities	4.5	3.7	8.7	4.9	5.9	6.8	7.6	3.9
Public services	3.8	3.0	7.0	4.5	1.1	1.4	0.8	0.7
Households	16.7	14.8	8.0	22.5	3.6	3.5	6.0	3.5
Sole proprietors	0.2	0.1	1.1	0.1	10.4	18.8	4.7	8.5
Foreign non-financial institutions	8.2	10.6	11.4	2.8	4.7	4.6	3.5	6.1
Foreign financial institutions	7.7	8.2	6.9	6.8	0.6	0.6	0.7	0.6
Other	0.03	0.03	0.0	0.0	8.0	9.6		5.8
Overall	100.0	100.0	100.0	100.0	3.7	4.0	4.8	2.9

Note: Sole proprietors with a registration number are included in individual sectors. Only sole proprietors operating without a registration number are included in the item "sole proprietors".
Source: Bank of Slovenia

6.7.4 Arrears in loan repayment

Arrears in the repayment of liabilities to banks lengthened in 2009.

There was an increase in clients' arrears in the settlement of liabilities to banks in 2009. The proportion classified claims in arrears was up slightly on the end of 2008, while there was sharp increase in the proportion of total classified claims more than 90 days in arrears, to 5.4% at the end of 2009. The proportion of non-financial corporations' classified claims that were more than 90 days in arrears rose significantly to reach 6.6% at the end of the year. In the context of a continuing increase in corporate illiquidity in early 2010, the proportion of longer arrears in this client segment rose further to 7.5% by February.

Table 6.28: Breakdown of classified claims by client segment in terms of number of days in arrears in the settlement of liabilities to banks in EUR million and percentages

	Classified claims			Proportion of claims in arrears for group of clients						
					all arrears			arrears of more than 90 days		
	Dec. 08	Dec. 09	Feb. 10		Dec. 08	Dec. 09	Feb. 10	Dec. 08	Dec. 09	Feb. 10
Total, EUR million	47,129	49,757	49,493		4,347	5,108	6,761	1,532	2,690	2,801
							(%)			
Corporates	52.6	50.4	50.7	100.0	12.6	12.6	18.1	3.5	6.6	7.5
OFIs	5.8	5.2	5.1	100.0	3.2	6.6	11.2	0.5	2.2	4.7
Households[1]	18.8	19.0	19.3	100.0	13.2	11.9	-	2.9	3.8	-
sole traders	2.2	1.9	1.9	100.0	16.9	22.9	21.8	9.3	13.1	11.8
other households[1]	16.6	17.1	17.4	100.0	12.7	10.7	-	2.1	2.8	-
Non-residents	15.5	15.7	15.0	100.0	12.2	18.9	17.5	7.3	10.9	9.0
Government	2.5	3.1	3.4	100.0	3.3	2.3	19.8	0.6	0.1	0.1
Banks and savings banks	4.4	6.5	6.4	100.0	0.9	1.4	2.5	0.9	0.4	0.4
Central bank	0.3	0.0	0.0	100.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	0.1	0.1	0.1	100.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	100.0	100.0	100.0	100.0	9.2	10.3	13.7	3.3	5.4	5.7

Note: [1] The figures for 2008 and 2009 for households are estimated on the basis of figures from the spring 2010 bank survey. The assessment is also taken into account in the aggregate of households.

Sources: Bank of Slovenia, bank survey

High growth and the lengthening of the arrears of non-residents and sole traders.

Banks are less exposed to sole traders in terms of the proportion of the credit portfolio accounted for by this client group, which demonstrates an exceptionally high level of claims paid in arrears. Non-residents and sole traders saw a sharp increase in overall arrears and arrears of more than 90 days in 2009. Non-residents, who account for a relatively high proportion of the banks' classified claims (15.7%), settle almost one-fifth of classified claims in arrears and nearly 11% with arrears of more than 90 days. Even greater risk in terms of longer arrears can be seen at sole traders, who account for a relatively low proportion of the banking system's credit portfolio. In contrast to non-financial corporations, the total arrears of non-residents and sole traders have risen significantly faster than arrears of more than 90 days, which indicates the expanding circle of clients in arrears from this segment, and forebodes the further lengthening of arrears in the future. For sole traders, this development is likely due to an increase in payment indiscipline, which is being transferred from larger to smaller corporates through a chain of effects.

Household arrears have risen, but mostly with respect to shorter maturities.

The proportion of households' total arrears is relatively high, at 10.7%, but down slightly on the previous year. The fluctuation is a result of the large proportion of the shortest arrears of up to 30 days. The proportion of longer arrears is low in this client group (2.8%), and did not show any sign of a major increase last year. Given the low proportion of longer arrears and the relatively high coverage of claims by collateral, the household sector represents low credit risk for banks.

The credit risk of the banks under majority foreign ownership is lower owing to the proportion of the credit portfolio accounted for by households.

The banks under majority foreign ownership, which have the highest proportion of households in their portfolio, are less exposed to the risk of default than the other bank groups. Contributing further to lower credit risk at these banks is the significantly lower proportion of foreign non-financial institutions, where the problem of non-payment of liabilities is more pronounced. The banks under majority foreign ownership have begun targeting their business policy on further increasing their exposure to households at the expense of other client segments, which will further improve the structure of clients in terms of credit risk.

Table 6.29: Breakdown of classified claims as at 31 December 2009 by individual bank group in terms of number of days in arrears in the settlement of liabilities to banks in EUR million and percentages

	Classified claims	No arrears	Up to 30 days	31 to 90 days	91 to 180 days	More than 180 days
Total, EUR million	49,757.3	44,649.2	1,511.8	906.5	735.4	1,954.4
			Breakdown, %			
Small domestic banks	100.0	82.8	9.8	1.5	1.5	4.3
Banks under majority foreign ownership	100.0	92.6	2.2	0.9	0.8	3.5
Large domestic banks	100.0	89.0	2.7	2.4	1.9	4.1
Overall	100.0	89.7	3.0	1.8	1.5	3.9

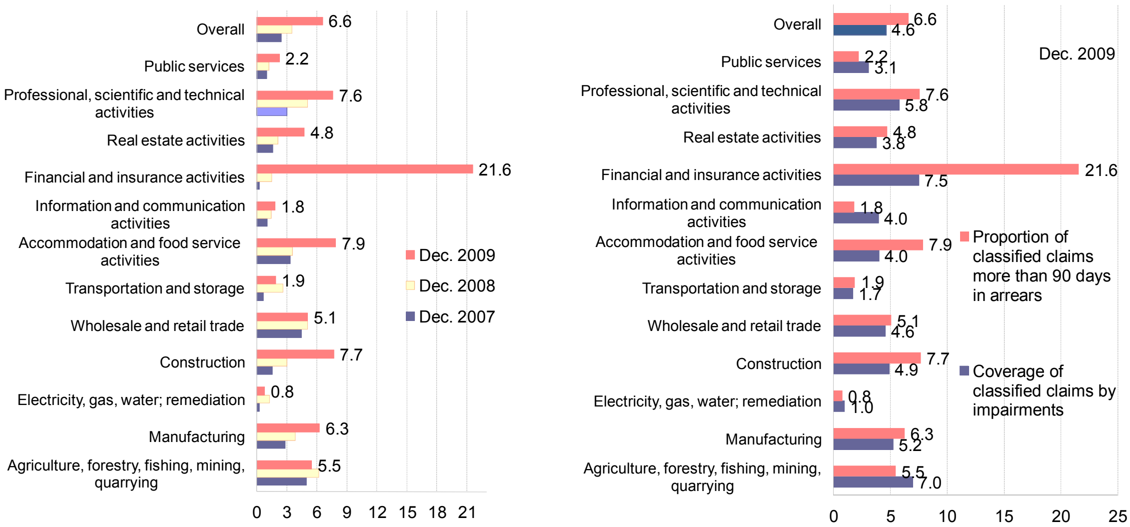
Source: Bank of Slovenia

The length of arrears represents one of the most important criteria for downgrading clients' ratings and creating additional impairments. The banks have responded faster in specific sectors to the increase in arrears by creating additional impairments. In professional, scientific and technical activities, where arrears of more than 90 days were up 50% in 2009, coverage of claims by impairments was up by a similar amount. In contrast, there was no significant increase in impairments for corporates from the accommodation and food service activities sector, where longer arrears more than doubled in 2009.

Significant variation between longer arrears and impairments created in certain sectors.

Figures regarding longer arrears and impairments for individual sectors indicate that banks will likely increase their impairments in the future, at least in those sectors where these variations are highest and total arrears have risen notably in recent times.

Figure 6.41: Arrears of more than 90 days as a proportion of banks' classified claims (left) and comparison of arrears of more than 90 days with impairments and provisions as a proportion of classified claims in percentages, December 2009



Source: Bank of Slovenia

The small domestic banks are more exposed to SMEs, which disclose higher arrears than large corporates.

Arrears at banks are longer for SMEs. The proportion of arrears of more than 90 days at SMEs stood at 7.7% in December, compared with 6.6% for all corporates. The small domestic banks are more exposed to SMEs than the other bank groups. SMEs account for nearly 54% of classified claims against non-financial corporations, while the figure is 36% and 40% for the other bank groups.

At the small banks, there is a high concentration of SMEs from the sectors of accommodation and food service activities, information and communication activities, construction, real estate activities, other business activities and agriculture, fishing and forestry. The proportion of SMEs exceeds 70% in all of the aforementioned sectors. The majority of these sectors also disclose above-average arrears.

All the bank groups assign SMEs an above-average risk assessment. Alongside the small banks, which are more prudent in the creation of impairments, the large domestic banks also created higher impairments for SMEs. The coverage of claims by impairments for

SMEs was 6.7% for both bank groups, the difference being that the large domestic banks assess SMEs as relatively more risky than larger corporates, compared with the other two bank groups.

Table 6.30: Proportion of banks' classified claims accounted for by SMEs and coverage of claims by impairments in percentages

	Large domestic banks	Small domestic banks	Banks under majority foreign ownership	Overall
Proportion of classified claims accounted for by SMEs	36.2	53.9	40.2	39.1
Coverage of classified claims by impairments				
against all non-financial corporations	5.4	6.1	3.0	4.6
against SMEs	6.7	6.7	3.5	5.6

Source: Bank of Slovenia

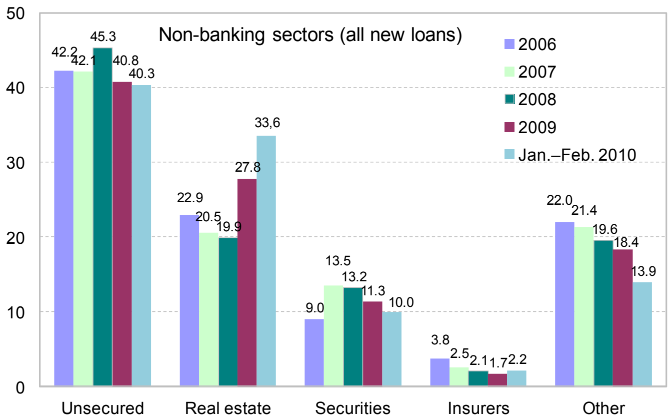
6.7.5 Loan collateral

Breakdown of collateral for newly approved loans

Banks tightened their loan collateral standards in 2009.

Owing to the deterioration of the existing credit portfolio, banks have become more prudent in approving new loans with regard to assessing the quality of individual clients and the required loan collateral. The tightening of collateral standards was reflected in a decline in the proportion of unsecured newly approved loans. An average of 40% of newly approved loans to non-banking sectors was unsecured in 2009. The high proportion of newly approved unsecured loans is a result of the high proportion of newly approved short-term loans, which rose in particular in 2008, resulting in an increase in the proportion of unsecured loans in the same period.

Figure 6.42: Breakdown of collateral of new loans to non-banking sectors in percentages



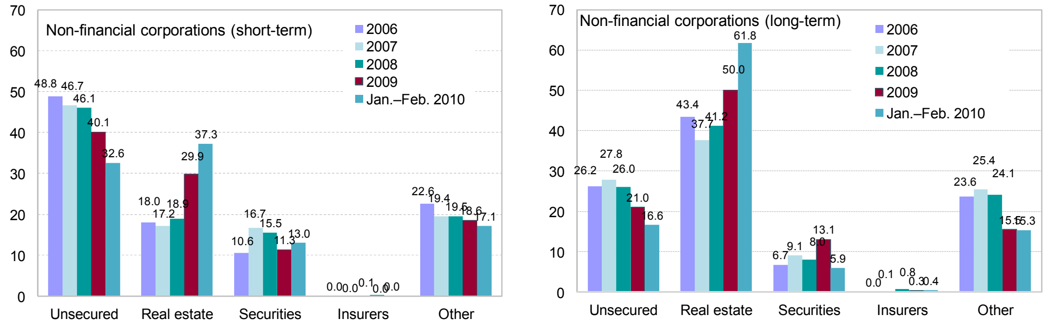
Source: Bank of Slovenia

Collateral on corporate loans: the proportion of unsecured loans was down at the expense of an increase in the proportion of real estate collateral.

The terms for raising new loans with respect to collateral tightened most notably in loans to non-financial corporations. The proportion of unsecured loans in this client segment stood at 35% in 2009, down 7 percentage points on the average in the period from 2006 to 2008. Unsecured long-term loans accounted for 21% of newly approved loans in 2009, while that figure was nearly double for short-term loans, at 40%. Having lost a great deal of value in 2008, the importance of securities collateral has diminished in the overall breakdown of collateral for new loans. The banks have also begun to require additional loan collateral alongside securities collateral.

The proportion of new loans to non-financial corporations with real estate collateral increased notably as a result of the relatively more stable value of this form of collateral and its availability, given the high proportion of bank loans accounted for by the construction sector. In 2009 the banks received real estate collateral for half of newly approved long-term loans and 30% of short-term loans to non-financial corporations. The proportion of this form of collateral continued to increase in early 2010.

Figure 6.43: Breakdown of collateral for new short-term loans (left) and long-term loans (right) to non-financial corporations in percentages

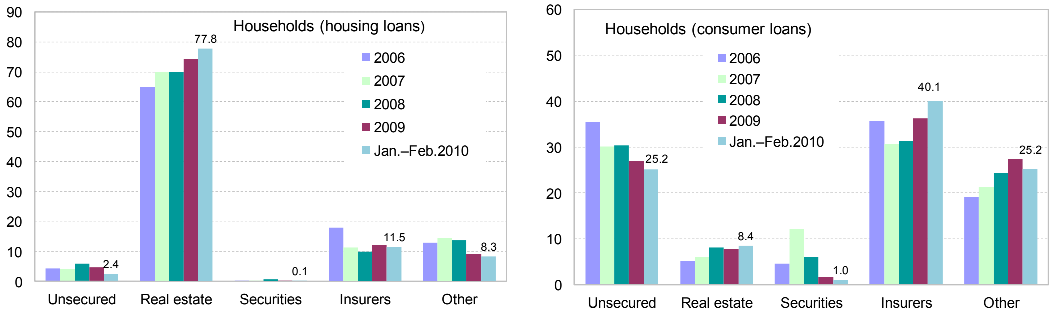


Source: Bank of Slovenia

Collateral on household loans: the proportion of loans secured with real estate is rising, as is the proportion of consumer loans secured with insurers.

Newly approved household loans were most frequently secured with real estate and with insurers, depending on the type of loan. The proportion of other forms of collateral (e.g. bank guarantees, deposits, sureties and other forms) and the proportion of unsecured loans were down. Housing loans have remained relatively well-covered by collateral, while a notable decrease in the proportion of unsecured consumer loans was not seen until recent years. The proportion of housing loans secured by real estate rose to 74% in 2009, while the proportion secured with insurers is stable, but relatively low. At 36% and rising, insurers represented the prevailing form of collateral for consumer loans in 2009. The proportion accounted for by insurers had already reached 40% in early 2010.

Figure 6.44: Breakdown of collateral of new housing loans (left) and consumer loans (right) to households in percentages



Source: Bank of Slovenia

Coverage of the credit portfolio by collateral

The proportion of unsecured bank loans was highest among non-residents and lowest among households.

At the end of 2009 the unsecured portion of the banks' credit portfolio overall was slightly higher than for newly approved loans, where a portion of existing bank portfolios was secured according to the looser bank standards that were valid prior to the outbreak of the financial turmoil. Nearly half of the banks' classified assets were unsecured at the end of 2009 owing to lower standards in the past and the high proportion of loans with the shortest maturities.[32] The highest proportion of the banks' unsecured claims is against the government and the banking sector, which is in line with the short maturities of these assets and the low level of risk. Non-residents stand out among other client segments, with the highest proportion of unsecured loans, of 70%. Claims against foreign financial institutions, which mostly bear a low level of risk and the shortest maturities, account for close to half of these claims. At 32%, households represent the lowest proportion of banks' unsecured claims.

[32] The figure includes unsecured claims and claims secured with forms of collateral that are not taken into account in banks' calculation of impairments and provisions (e.g. collateral in the form of bills of exchange).

Table 6.31: Collateral of classified claims by client segment at the end of 2009 in percentages

		Comparison of collateral[2] with classified assets, %						
			Secured					
	Classified claims, EUR million	Unsecured[1]	Shares, equity and mutual funds units as collateral	Real estate as collateral[3]	Housing as collateral[3]	At insurer	Other	Total value of collateral[3]
Corporates	25,078	40.6	9.4	60.3	4.8	0.1	31.1	105.7
OFIs	2,566	53.9	25.7	6.4	0.3	0.0	28.6	61.1
Households	9,440	32.3	1.3	13.5	58.5	18.1	14.1	105.4
Non-residents	7,833	70.1	3.3	15.6	1.9	0.0	22.2	43.1
Government	1,555	83.3		2.6	0.2		12.0	14.8
Banks and savings banks	3,219	96.6	0.2		0.0		2.5	2.7
Overall	49,757	49.4	6.8	35.8	13.8	3.5	23.9	83.8

Notes: [1] The figure includes unsecured claims and claims secured with forms of collateral that are not taken into account in banks' calculation of impairments and provisions (e.g. collateral in the form of bills of exchange).
[2] Collateral is stated at fair value.
[3] With regard to collateral in the form of real estate, several banks may enter a mortgage on the same property. In such cases, the value of the mortgage at each successive bank is reduced by the value of banks' claims with priority in the possible redemption of the collateral. Consequently, the value of these forms of collateral is multiplied both for these forms of collateral and as an aggregate.

Source: Bank of Slovenia

The coverage of claims against households and corporates with real estate was high.

The majority of the banks' classified claims were secured by real estate, which, measured at fair value, covers nearly 50% of the value of classified assets. The banks had the highest coverage of classified claims by real estate (both residential and commercial property) for their claims against corporates (65.1%) and their claims against households (72%). In these two segments, the total value of collateral was around 5% higher than the total value of claims against these clients, including unsecured claims.[33]

Standing out among other forms of collateral in terms of importance were credit insurance with insurers for claims against households at 18.1%, and collateral in the form of securities or mutual fund units for claims against non-monetary financial institutions at 25.7%. Given the rising trend of collateral in the form of real estate for newly approved loans, we can also expect the proportion of the overall credit portfolio accounted for by this form of collateral to increase in the future.

Claims more than 90 in arrears were better secured than the total credit portfolio, primarily with real estate, shares and participating interests.

The banks' claims more than 90 days in arrears were slightly better secured on average than total claims. The proportion of secured claims with longer arrears was 60% at the end of 2009, up 10 percentage points on total classified claims. Claims against non-monetary financial institutions stand out in terms of coverage by collateral, the proportion of unsecured claims with longer arrears having stood at just 8.1% at the end of 2009. In contrast, non-residents stand out in terms of poor collateral, their proportion of unsecured claims with longer arrears having stood at 42.1%.

[33] With regard to collateral in the form of real estate, several banks may enter a mortgage on the same property. In such cases, the value of the mortgage at each successive bank is reduced by the value of banks' claims with priority in the possible redemption of the collateral. Consequently, the value of these forms of collateral is multiplied both for these forms of collateral and as an aggregate.

Table 6.32: Collateral of classified claims more than 90 days in arrears by client segment at the end of 2009 in percentages

	Classified claims, EUR million	Comparison of collateral[2] with classified assets, %							
		Unsecured[1]	Secured: Shares, equity and mutual funds units as collateral	Real estate as collateral[3]	Housing as collateral[3]	At insurer	Other	Total value of collateral[3]
Corporates	1,645.5	41.0	7.4	65.6	7.1	0.1	27.2	107.3
OFIs	55.4	8.1	73.4	18.9	1.3		26.3	119.9
Households[4]	121.6	37.5	0.0	82.0	27.8	0.7	18.4	128.9
Non-residents	853.5	42.1	8.3	35.9	1.3		26.7	72.2
Government	1.6	100.0						
Banks and savings banks	12.0	100.0						
Overall	2,689.8	40.8	8.7	55.6	6.0	0.1	26.5	96.9

Notes: [1,2,3] The same notes from the previous table apply. [4] Only sole traders are included. No figures regarding arrears are available for households.
Source: Bank of Slovenia

There is a notable gap for claims with longer arrears between the high proportion of unsecured claims (40.8%) and the coverage of these claims by impairments and provisions (28.8%). This gap can arise owing to the short maturity of claims for which impairments were not (or have not yet been) created, or due to claims against banks' best clients for which collateral was not required when a loan agreement was concluded.

The majority of claims with longer arrears were secured by real estate and collateral in the form of shares and participating interests, while the coverage of claims by credit insurance with insurers was negligible.

Table 6.33: Collateral of classified claims more than 90 days in arrears by bank group at the end of 2009 in percentages

	Classified claims, EUR million	Comparison of collateral[2] with classified assets, %						
		Unsecured[1]	Shares, equity and mutual funds units as collateral	Real estate as collateral[3]	Housing as collateral[3]	At insurer	Other	Total value of collateral[3]
Savings banks	0.6	70.0	10.1		25.4	0.9	12.2	47.7
Small domestic banks	208.6	44.1	5.6	69.9	9.9	0.2	16.5	101.6
Foreign banks	675.1	42.7	8.5	42.1	7.7	0.1	18.2	91.6
Large domestic banks	1,805.5	39.7	9.1	59.0	5.0	0.0	25.8	98.3
Overall	2,690	40.8	8.7	55.6	6.0	0.1	26.5	96.9

Note: 1,2,3 The same notes from the previous table apply.
Source: Bank of Slovenia

The large domestic banks had the lowest proportion of unsecured claims with longer arrears at just under 40%. In the context of a higher proportion of unsecured claims, the small domestic banks created higher impairments and provisions for this category of claims than the other bank groups. The small banks also stood out with the highest relative proportion of collateral for claims more than 90 days in arrears in the form of real estate.

Redemption of loan collateral

In the current uncertain conditions on the capital markets and in the context of price instability on the real estate market, loan collateral in the form of real estate and securities represents an additional risk factor in the banks' credit portfolio. The LTV ratio on loans secured by mortgages deteriorated due to falling real estate prices. According to figures from the spring 2010 bank survey, in 2009 banks addressed the problem of a deteriorating LTV ratio with respect to the contractually agreed ratio by requiring additional collateral or the partial repayment of debt. They took a similar approach to claims with collateral in the form of securities and mutual funds units.

The redemption of collateral in the form of real estate was limited in 2009.

In 2009 banks redeemed collateral by selling real estate in only a few cases of default by clients. In the majority of instances, debtors were able to agree on a way to settle their liabilities. Alongside the low liquidity of the real estate market, another major factor in decisions not to redeem these forms of collateral was the long-term nature of such procedures, for the most part owing to long court proceedings. In practice, the procedure of redeeming real estate collateral can last several years (e.g. during bankruptcy proceedings against a debtor).

Owing to legal restrictions, banks are also limited with regard to increasing their investments in equities obtained on the basis of debtors' failure to settle liabilities. The Banking Act set out limits on banks' investments in qualifying holdings in entities from the non-financial sector. The value of a bank's qualifying holding in an individual legal entity from the non-financial sector may not exceed 15% of the bank's capital, while sum of all qualifying holdings of a bank in entities from the non-financial sector may not exceed 60% of the banks capital. The investments that a bank obtains temporarily in lieu of the settlement of a debtor's financial liabilities are not taken into account when calculating the aforementioned limitations for the first three years following the receipt of pledged property. A bank may exceed these limitations if it secures additional capital as coverage for this purpose.

Construction

In the context of the developments on the real estate market and in the construction sector, the high proportion of collateral in the form of real estate represents a significant risk factor for banks. Corporates in the construction sector in particular have secured a large portion of their debt with real estate. Banks partly hedge against a fall in the value of real estate with a low LTV ratio. The risk is relatively higher for that portion of banks' claims that are secured by yet-to-be-constructed real estate or real estate whose completion is uncertain.

The small domestic banks were the most exposed to corporates from the construction sector, and also created the highest impairments in relative terms for them.

Last year classified claims against corporates from the construction sectors accounted for 6.4% of the banking system's total classified assets. At 8.3%, the small domestic banks were most exposed to this sector, while the banks under majority foreign ownership were least exposed, at 5.1%. The highest proportion of claims against the construction sector more than 90 days in arrears was seen at the small banks. Impairments of claims against the construction sector were also highest at these banks.

A large portion of claims against the construction sector were unsecured. At the end of 2009 one-third of claims against the construction sector were unsecured at the domestic banks, and fully 60% at the banks under majority foreign ownership. The proportion of unsecured claims more than 90 days in arrears was also very high: the figure ranged from 20% at the large domestic banks to nearly 40% at the banks under majority foreign ownership. The prevailing form of collateral for claims against the construction sector was pledged real estate, the assessed value of which at the end of 2009 only exceeded claims against this sector at the large banks. Here it should be noted that one item of real estate can serve as collateral for the claims of several banks, making the actual value of the real estate collateral lower.

Table 6.34: Impairments and provisions of claims against the construction sector, December 2009

	Classified claims against corporates					Classified claims more than 90 days in arrears			
			Coverage by impairments						
	Claims, EUR million	Proportion of total claims of group	Dec. 08	Dec. 09	Proportion unsecured	Proportion of total claims against corporates in sector	Coverage by impairments	Proportion unsecured	Real estate collateral / classified claims
	Construction								
Large domestic banks	2,060.0	6.8	3.6	5.3	33.9	7.2	26.4	19.8	104.7
Small domestic banks	298.9	8.3	4.3	5.6	32.9	9.4	24.2	25.6	93.6
Banks under majority foreign ownership	800.5	5.1	3.3	3.7	60.2	8.2	25.9	39.0	78.8
Overall	3,160.3	6.4	3.6	4.9	40.4	7.7	26.0	25.7	96.4
	Real estate activities								
Large domestic banks	591.0	2.0	3.4	5.0	15.5	3.4	37.2	11.5	126.2
Small domestic banks	109.2	3.0	3.8	4.3	29.9	9.3	22.1	25.7	97.2
Banks under majority foreign ownership	517.1	3.3	1.4	2.3	41.3	5.3	26.9	16.1	142.0
Overall	1,217.8	2.4	2.6	3.8	27.8	4.8	29.7	16.2	128.6
	Non-financial corporations in sectors of construction and real estate activities								
Large domestic banks	2,651.0	8.8	3.5	5.2	29.8	6.4	27.7	18.8	107.3
Small domestic banks	408.1	11.3	4.2	5.3	32.1	9.4	23.6	25.6	94.6
Banks under majority foreign ownership	1,317.6	8.4	2.6	3.2	52.8	7.1	26.2	32.3	97.4
Overall	4,378.1	8.8	3.3	4.6	36.9	6.9	26.7	23.8	102.6

Source: Bank of Slovenia

Non-residents

High credit risk for the domestic banks with respect to foreign non-financial institutions.

Exposure to non-residents was high primarily at the domestic banks, where it reached 18% of their credit portfolio. The differences between the bank groups were significant, particularly with regard to exposures to foreign non-financial institutions, the figure standing at slightly less than 3% at the banks under majority foreign ownership, and at 11% at the domestic banks. The high risk associated with these claims was seen in a high 14.1% proportion of claims more than 90 days in arrears, and in their rapid growth in the last year, of 6 percentage points. Claims against foreign non-financial institutions represent high credit risk, particularly at the large domestic banks, where the proportion of claims with longer arrears reached 15.6%, while the coverage of these claims by impairments was relatively low compared with the lower-risk client segment.

The coverage of claims against foreign financial institutions with longer arrears by impairments was exceptionally low at the small domestic banks, at merely 4.3%. The low amount of impairments created at these banks was partially offset with collateral, by which the small banks covered nearly the entire amount of non-performing claims against this client segment. The prevailing form of collateral at all the bank groups for claims against foreign financial institutions was real estate.

The large domestic banks' exposure to credit risk is above-average with respect to foreign non-financial institutions.

The relative exposure to foreign financial institutions was approximately the same in all bank groups; only at the large domestic banks did these claims represent increased credit risk owing to their exposure to subsidiary banks in the rest of the world. More than one-tenth of the large banks' claims against foreign financial institutions disclosed longer arrears, a large proportion of which were also unsecured. Only 13% of such claims of the large domestic banks were secured by irrevocable guarantees, while other forms of collateral were negligible.

Table 6.35: Impairments and provisions of claims against non-residents, December 2009

	Classified claims against non-residents					Classified claims more than 90 days in arrears			
			Coverage by impairments						
	Claims against non-residents, EUR million	Proportion of total claims of group	Dec. 08	Dec. 09	Proportion unsecured	Proportion of total claims against corporates in sector	Coverage by impairments	Proportion unsecured	Collateral / classified claims
	Foreign non-financial institutions								real estate
Large domestic banks	3,182.9	10.6	3.7	4.6	46.5	15.6	15.6	17.5	57.3
Small domestic banks	412.4	11.4	2.3	3.5	29.4	6.8	4.3	4.7	99.8
Banks under majority foreign ownership	442.4	2.8	3.9	6.1	44.5	9.6	52.0	50.0	10.2
Overall	4,037.7	8.1	3.5	4.7	44.5	14.1	17.8	19.3	55.9
	Foreign financial institutions								irrevocable guarantees
Large domestic banks	2,472.0	8.2	0.7	0.6	97.2	11.3	4.2	86.9	13.0
Small domestic banks	249.9	6.9	0.8	0.7	98.7	0.0	-	-	-
Banks under majority foreign ownership	1,073.1	6.8	0.8	0.6	97.2	0.7	89.9	100.0	0.0
Overall	3,795.0	7.6	0.7	0.6	97.3	7.5	6.3	87.2	12.7

Source: Bank of Slovenia

Holding companies

The banks classify holding companies among higher-risk clients, both in terms of impairments created, and the highest relative increase in 2009. Classified claims against holding companies declined in the last year, in part owing to the maturing of short-term loans and also due to the closing of non-performing claims in autumn 2009 and their repayment from collateral.

Arrears of more than 90 days and impairments of claims against holding companies recorded the fastest growth.

Claims against holding companies varied between the bank groups, from 3.5% to 5.5% of total classified claims. These claims are among the highest-risk claims in the banks' portfolios. At the end of 2009 nearly one-fifth of claims against holding companies were more than 90 days in arrears. The figure had already risen to one-quarter by February 2010.

Table 6.36: Impairments and provisions of claims against holding companies, December 2009

	Classified claims against holding companies					Classified claims more than 90 days in arrears			
			Coverage by impairments						
	Claims against holding companies, EUR million	Proportion of total claims of group	Dec/ 08	Dec/ 09	Proportion unsecured	Proportion of total claims against holding companies in sector	Coverage by impairments	Proportion unsecured	Shares and equity collateral
	Holding companies								
Large domestic banks	1,382.8	4.6	2.8	8.0	35.3	14.8	27.3	77.3	19.7
Small domestic banks	200.2	5.5	2.2	6.6	60.0	14.3	28.0	99.1	0.0
Banks under majority foreign ownership	553.2	3.5	0.4	5.4	40.7	33.4	13.7	32.6	5.4
Overall	2,160.3	4.3	2.1	7.1	38.6	19.3	21.3	59.0	12.0

Source: Bank of Slovenia

Given the high illiquidity of holding companies, the banks created relatively low impairments, although they were higher than in other sectors. At the banks under majority foreign ownership, claims with longer arrears accounted for one-third of all claims against holding companies, while coverage by impairments of this portion of the portfolio was just 13.7%. The risk associated with claims against holding companies is further exacerbated by the fact that the majority of these claims are unsecured. The proportion of unsecured claims against holding companies more than 90 days in arrears was alarmingly high: 60% of claims more than 90 days in arrears were unsecured, and fully 99% were unsecured at the small banks. The prevailing forms of collateral for claims against holding companies were shares and participating interests, which covered merely 12% of classified claims, and real estate covering 2.5%.

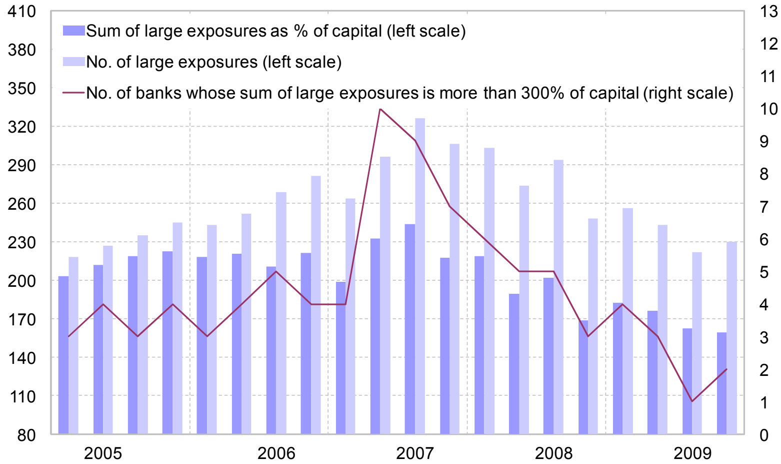
Given the high illiquidity of holding companies, claims against them are poorly covered, despite the increase in impairments.

Large exposures

There was a decline in the number and sum of large exposures in 2009.

The number and sum of large exposures both declined in 2009. The number of large exposures fell by 18 to 230. The sum of large exposures also fell, from 169% to 159% of the banking system's capital. At the end of 2009 the sum of large exposures exceeded 300% of capital at only two banks.

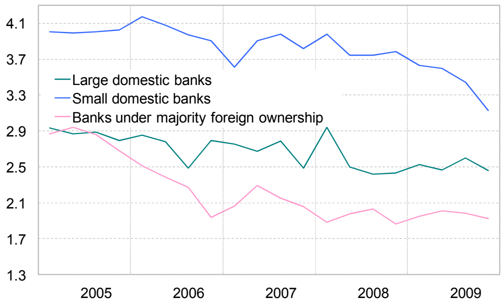
Figure 6.45: Sum and number of the banking sector's large exposures

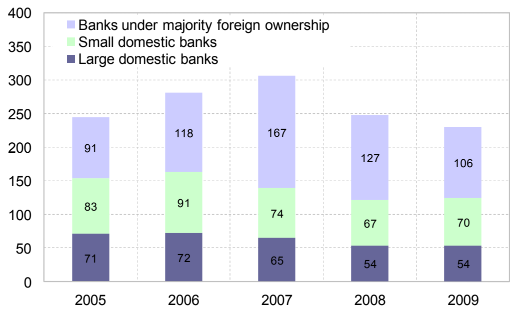


Source: Bank of Slovenia

Exposure to credit risk as measured by large exposures declined for all the bank groups in 2009. The average size of large exposures fell by 0.7 percentage points at the small domestic banks to 3.1% of regulatory capital, and was unchanged at the large domestic banks. The average size of large exposures was up 0.1 percentage points at the banks under majority foreign ownership to 1.9% of regulatory capital.

Figure 6.46: Average size of large exposures as a percentage of regulatory capital (left) and number of large exposures (right) by bank group





Source: Bank of Slovenia

Box 6.3: Assessment of the potential increase in non-performing claims and impairments

The proportion of non-performing claims (rated D and E)[3] was up 0.4 percentage points in 2009. At 1.6 percentage points, the increase in the proportion of C-rated claims was more significant.[4] Despite the gradual economic recovery, the proportion of non-performing claims is expected to rise further. There are several reasons for this.

First, credit growth stagnated in 2009. Very low growth in loans to non-banking sectors is also forecast for 2010. The average credit rating structure of new loans is better than that of existing loans, and is improving the quality of the credit portfolio. The quality of existing loans deteriorates in periods of stagnating or very low credit growth. Hence, the credit rating structure of the entire credit portfolio also deteriorates.

Second, in 2009 the deteriorating quality of the credit portfolio was seen primarily in an increase in the proportion of C-rated claims. In the context of a slow economic recovery, periods of arrears will further lengthen for certain loans, resulting in downgrading to D and E ratings. By contrast, the quality of some collateral, and hence the ratings of claims, also deteriorates in conditions where no growth in real estate prices is expected and the ability to redeem such collateral is questionable owing to the low volume of transactions.

Third, we assess that the banks are also reluctant to downgrade claims. The ability of the banks to create additional impairments from current earning has also diminished owing to declining profitability. In the background there is also the assumption that the recession was merely short-term in nature and that economic conditions will improve rapidly and with them the solvency of clients.

Fourth, there are loans that are still being repaid regularly, but that nevertheless have a risk of becoming problematic in the future. This group includes those borrowers for which a speedy economic recovery is crucial. It also includes loans that could become problematic in the context of an external shock, such as a rise in interest rates. Finally, this group includes loans for which only interest is paid regularly, while the principal is repaid at maturity. Borrowers will be forced to repay the principal in economic conditions that will be entirely different from those that existed when the loans were approved.

An assessment of the potential increase in the proportion of non-performing claims, coverage by impairments and the costs of impairments for the banking system are presented below. Assessments are based on figures available at the end of November 2009.[5] The impact of a reduction in the differences between banks in the creation of impairments and an acceleration in the downgrading of claims is illustrated first. This is followed by assessments for 2010, using three approaches: a transition matrix, an aggregate equation and a credit risk model based on panel data.

Adjusting the percentages of impairments of the same customers at different banks

On the basis of approximately one-quarter of clients, we can estimate the amount of additionally required impairments if we took into account the conservative assessments of banks in the percentages of impairments. The maximum percentage of impairments that an individual bank creates for the claims against the same client is taken into account. The maximum percentage, reduced by the actual percentage of created impairments, is applied to the unsecured portion of classified claims. On the basis of figures from the end of November 2009, the banks would be required to create additional impairments in the amount of EUR 490 million according to this assessment. By limiting the assessment to only those clients for which an individual bank classified its related claims as non-performing, with other banks then following suit, additional impairments in the amount of EUR 174 million would be required. This would mean an increase in the coverage of classified claims by impairments of 0.4 percentage points to 4% for the banking system overall. If all such claims were downgraded to non-performing, the proportion of non-performing claims would increase by 1.7 percentage points to 4%.

A comparison by sector indicates that 60% of the additional impairments of EUR 174 million would be required for the sectors of financial and insurance activities, and manufacturing. Coverage by impairments in these two sectors would increase by 0.9 percentage points to 3.5% in financial and insurance activities and by 0.6 percentage points to 5.9% in manufacturing. The high amount of additional impairments required in the financial and insurance activities sector, which primarily includes holding and leasing companies, indicates that certain banks have already identified claims against these corporates as bad and created the necessary impairments, while other banks continue to maintain a relatively low percentage of impairments. More problematic is the construction sector, where potential deviations are to be expected. The banks however continue to give corporates from the construction sector relatively good assessments. Since the quality of claims against the construction sector is linked to the market value of real estate and the actual ability to redeem collateral in this form, more stringent requirements for additional impairments can be expected if the situation on the real estate market deteriorates.

Assessments for 2010

Three approaches are used to assess expected changes in impairments and non-performing claims in 2010. The assessment based on a transition matrix assumes that the transition matrix for 2010 is the same as that for 2009. The aggregate equation assesses the proportion of non-performing claims, depending on GDP, interest rates and lending growth. The credit model based on panel data[6] assesses the credit rating of corporates, depending on microeconomic variables (capital, cash flow, liquidity, indebtedness and demand) that are characteristic for a specific corporate, and on macroeconomic factors (economic growth, interest rates and loans to non-banking sectors as a proportion of GDP) that are common to all clients. It is assumed that the variables relating to specific corporates remain unchanged, and that only macroeconomic factors change.

On the basis of these three approaches, the proportion of non-performing claims increases by between 0.2 and 1 percentage points in 2010, and the coverage of classified claims by impairments increases by between 0.3 and 0.9 percentage points. The proportion of non-performing claims could rise to 3.3% in 2010, and coverage of classified claims by impairments to 4.5%.

Estimated net impairment costs for 2010 range from EUR 300 million to EUR 600 million. In 2009 the banks disclosed net impairment costs (relating to financial assets at amortised cost) of EUR 428 million, which is at the same level assessed for 2010 assuming no change in the transition matrix. At this level of impairment costs, the banks would have recorded a pre-tax profit of EUR 160 million in 2009. Assuming the same gross income and operating expenses as in 2009, the banking system’s operating result would be marginally positive, if impairment costs were close to the assessed upper limit of EUR 600 million. This does not preclude the possibility of a negative operating result for individual banks in 2010.

The estimated impairment costs ranging from EUR 300 million to EUR 600 million take into account macroeconomic factors and the unchanged probability of the downgrading of claims. The banking system's impairment costs would increase further in the event of an external shock, such as a rise in market interest rates.

Table 6.37: Proportion of non-performing claims, impairment costs and coverage of classified claims by impairments in 2009 (figures available at the end of November)

	Classified claims, EUR million	Impairments, EUR million	Proportion of claims rated D and E, %	Impairment costs, EUR million	Coverage of classified claims by impairments, %
Nov. 2009	48,732	1,763	2.3%	428	3.6%

Source: Bank of Slovenia

Table 6.38: Estimated increase in impairment costs, the proportion of non-performing claims and coverage of classified claims by impairments taking into account various calculation methods

	Classified claims, EUR million	Proportion rated D and E, %	Change in proportion rated D and E, percentage points	Impairment costs, EUR million	Increase in impairments excluding write-offs, EUR million	Coverage of classified claims by impairments, %	Change in coverage, percentage points
1. Adjustments in assessments of same clients at different banks (maximum impairment level)							
- All clients in debt at several banks	48,732	4.0%	1.7	490	490	4.6%	1.0
- Clients against whom individual banks have non-performing claims		4.0%	1.7	174	174	4.0%	0.4
2. Baseline scenario for 2010							
- Aggregate equation for claims rated D and E	51,618	2.5%	0.2	307	260	3.9%	0.3
- Transition matrix		2.8%	0.5	436	401	4.2%	0.6
- Panel model		3.3%	1.0	598	557	4.5%	0.9

Sources: Bank of Slovenia, own calculations

High impairment costs in 2009, which can be expected this year as well, are a result of the pro-cyclical behaviour by banks. Past lending growth strengthened in line with high economic growth and high returns on the capital and real estate markets. The more expansionary the lending policies pursued by the banks in a positive economic climate, the more restrictive and risk-oriented they become in deteriorating economic conditions. The deterioration in economic conditions brought a decrease in demand for loans and the creditworthiness of borrowers. An important factor in the context of the difficulty in accessing fresh capital is the banks' desire to reduce financial leverage with the aim of maintaining capital adequacy at a sufficiently high level. The latter is also true in light of unrealised, but expected, needs to create impairments owing to the deterioration in the quality of the credit portfolio. The banks' ability to generate revenue in the future is diminished in the context of currently low lending growth. Their ability to create impairments is also diminishing in line with the expected decline in their profitability. This raises expectations regarding the need to cover unexpected losses with capital.

It is important that the banks more actively monitor their credit portfolio. Special attention is being given to the success of claims recovery, which could also ease the burden on income and capital in the long term. It would be highly unusual to intervene via extraordinary measures in a banking system with relatively well-capitalised and liquid banks with a satisfactory level of profitability and quality of investments. Owing to the rate of deterioration of the credit portfolio's quality and the rising impairment and provisioning costs, banks' management boards and supervisory boards must be ready to carry out timely capital increases. The Bank of Slovenia specifically called on banks in January 2010 to make the relevant assessments and preparations, and to effect capital increases in a timely manner.

[3] These are classified claims with a percentage of impairments exceeding 40%.
[4] Percentage of impairments of between 15% and 40%.
[5] Banks and savings banks are taken into account, excluding subsidiaries, which are not obliged to meet requirements regarding the creation of impairments.
[6] An ordinal probit model of random effects is used for panel data.

6.8 Interest-rate risk

The banks remain exposed to rising interest rates in the context of an increased likelihood of the realisation of interest-rate risk.

Interest-rate risk as measured by the difference between the average repricing periods for asset and liability interest rates declined overall in 2009, despite rising in the second half of the year. An analysis of interest-rate gaps indicates that exposure to a rise in interest rates rose in buckets where a sharper rise in interest rates is expected. Net long positions in key interest rates have decreased, but this remains favourable in the context of an expected rise in interest rates.

An analysis by bank group reveals that exposure to a rise in interest rates, as measured by the difference between the average repricing periods for asset and liability interest rates, only decreased at the large domestic banks, while it increased at the banks under majority foreign ownership and the small domestic banks. According to this indicator, we assess that the decrease in interest-rate risk in the Slovenian banking system is merely temporary, as confirmed by its dynamic from the middle of 2009 on.

Varying levels of exposure to interest-rate risk between banks groups.

On the basis of movements in interest rates on futures contracts, we assess that the likelihood of a rise in interest rates has increased, and hence the realisation of interest-rate risk.

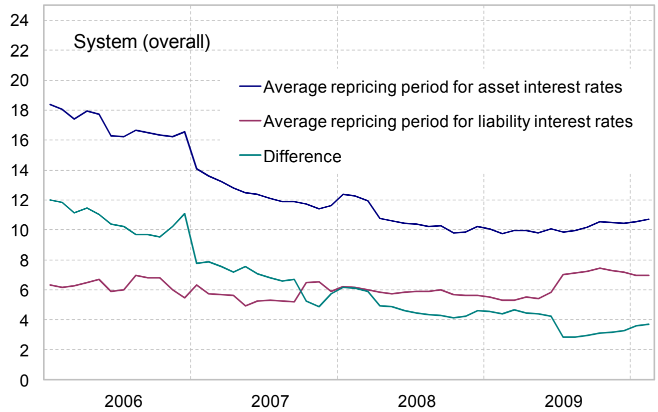
6.8.1 Average repricing periods for interest rates

Interest-rate risk, as measured by the difference between the average repricing periods for asset and liability interest rates, fell sharply in the middle of 2009 with the issue of government-guaranteed bank bonds with a fixed coupon rate, and then began to rise again gradually. In February 2010 the average repricing period for asset interest rates was 3.7 months longer than the average repricing period for liability interest rates, down 0.9 months on the difference at the end of 2008. The difference was 3.1 months at the large domestic banks, 4.8 months at the banks under majority foreign ownership and 5.2 months at the small domestic banks.

The difference between the average repricing period for asset and liability interest rates narrowed.

The trend of a decline in the average repricing period for asset interest rates came to a halt in 2009, the average repricing period having reached 10.7 months by the end of February 2010, up 0.4 months on December 2008. The average repricing period for liability interest rates lengthened by 1.3 months over the same period, to reach 7 months. The lengthening of the average repricing period for liability interest rates in 2009 can only be temporary in nature, particularly if the banks are unable to substitute maturing short-term sources with fixed rate sources with longer maturities. Consequently exposure to interest-rate risk may rise.

Figure 6.47: Average repricing period for interest rates by bank group in months



Source: Bank of Slovenia

A comparison between the bank groups reveals significant differences in the dynamic of interest-rate risk measured by the difference between the average repricing period for asset and liability interest rates. According to this indicator, interest-rate risk decreased notably at the large domestic banks in 2009 owing to the issue of bonds with a fixed coupon rate. Exposure to interest-rate risk increased at the banks under majority foreign ownership due to the shortening of the average repricing period for liability interest rates. Interest-rate risk increased at the small domestic banks due to the lengthening of the average repricing period for asset interest rates.

6.8.2 Interest-rate gap

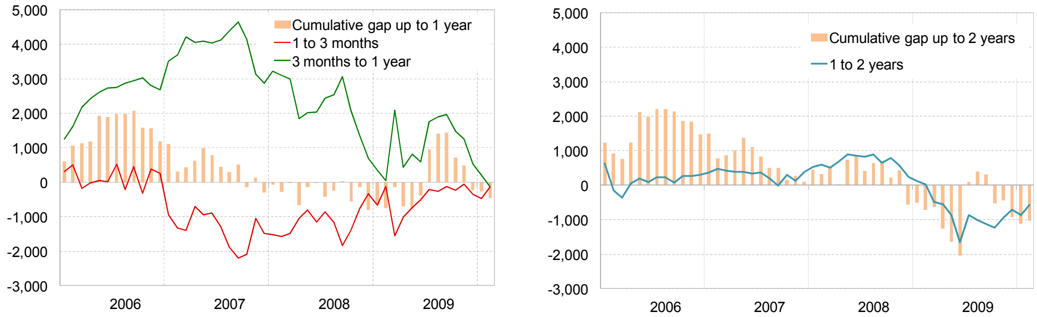
An analysis of cumulative interest-rate gaps indicates that exposure to a rise in interest rates decreased in the interval of up to 1 year, but increased in the interval of up to 2 years. The negative cumulative interest-rate gap of up to 1 year closed by slightly more than two-thirds in 2009, but widened again slightly in the first two months of 2010. The negative cumulative interest-rate gap of up to 2 years widened by 64% in 2009, and by an additional 11% by February 2010.

The negative cumulative interest-rate gap of up to one 1 closed, while the gap of up to 2 years turned from positive to negative.

The banks' interest-rate gap of 1 to 2 years is sharply negative where interest rates are expected to rise more notably.

The negative interest-rate gap of 1 to 3 months was affected by a decline in assets and liabilities in this bucket. Assets declined more rapidly than liabilities in the first half of the year, which led to the widening of the negative gap. This was followed by liabilities declining faster than assets, the interest-rate gap in this bucket hence returning to the level recorded at the end of 2008. Having previously lengthened, in 2009 the interest-rate gap of up to 3 months returned to the level seen at the end of 2008. The interest-rate gap of 1 to 2 years remained sharply negative. Banks are exposed to a rise in interest rates in this bucket. On the basis of interest rates in interest rate futures[34] and the expectation of market participants regarding changes in the ECB's interest rate,[35] we can expect interest rates to rise.

Figure 6.48: Gap between interest-sensitive assets and liabilities by individual bucket in EUR million



Source: Bank of Slovenia

6.8.3 Basis risk

Interest-rate gaps by currency

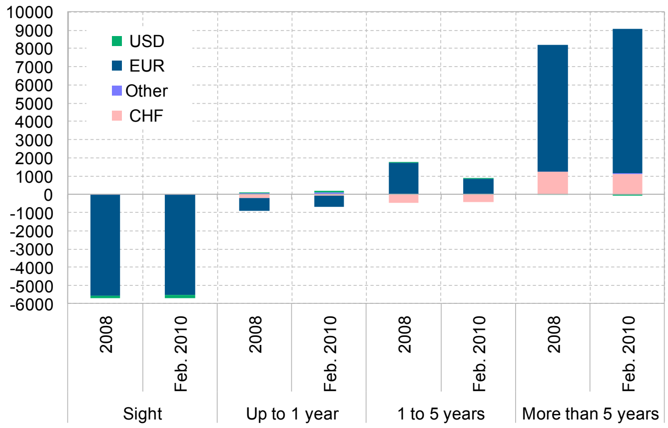
Growth in interest-sensitive assets and liabilities was 8.6% and 8.8% respectively.

Interest-sensitive assets exceeded interest-sensitive liabilities by EUR 3.4 billion in February 2010. Interest-sensitive assets were up 8.6% in 2009, to EUR 49.4 billion, and then fell to EUR 48.9 billion by the end of February 2010. Interest-sensitive liabilities recorded a similar dynamic, having risen by 8.8% in 2009 to EUR 46.2 billion, before declining to EUR 45.5 billion over the first two months of 2010.

The already-high proportion of interest-sensitive items accounted for by the domestic currency increased further.

There were no major changes in the currency breakdown of interest-sensitive items in 2009. The proportion of interest-sensitive items accounted for by the domestic currency was up slightly on account of a decrease in the proportion accounted for by Swiss franc items. The proportion of interest-sensitive items accounted for by the domestic currency was up 1.5 percentage points to 94.7% on the asset side in 2009, and up 1.7 percentage points to 95.8% on the liability side.

Figure 6.49: Currency breakdown of net interest-rate positions by individual bucket of residual maturity in EUR million



Source: Bank of Slovenia

[34] Figures from futures contacts as of 26 March 2010. Source: Bloomberg.
[35] Expectations regarding the ECB's key interest rate. Source: Reuters survey.

The banks are primarily exposed to a rise in interest rates in the domestic currency and in Swiss francs. There is also some exposure in shorter maturities in US dollars.

Gaps by type of reference interest rate

An additional source of interest-rate risk is mismatching in the structure of interest-sensitive assets and liabilities in relation to the type of reference interest rate, although mismatching decreased in 2009.

The proportion of interest-sensitive items tied to reference interest rates declined.

The proportion of items tied to reference interest rates was down 12 percentage points in 2009 to 53% on the asset side, and down 6 percentage points to 33% on the liability side. The gap between the proportion of interest-sensitive assets and liabilities tied to reference interest rates thus decreased to 20 percentage points.

Table 6.39: Structure of interest-sensitive assets and liabilities by reference interest rate

	Interest-sensitive assets				Interest-sensitive liabilities			
	Dec. 07	Dec. 08	Dec. 09	Feb. 10	Dec. 07	Dec. 08	Dec. 09	Feb. 10
Stock, EUR million	40,173	45,440	49,368	48,883	37,919	42,426	46,168	45,520
	Breakdown, %							
Reference interest rates	59.6	65.4	53.0	53.9	38.3	39.2	33.2	33.6
TOM	1.4	0.8	0.5	0.4	0.9	0.4	0.2	0.2
Other	39.0	33.8	46.5	45.6	60.8	60.4	66.6	66.3
	Proportion of tied items accounted for by individual reference rates, %							
EURIBOR								
1 month	19.6	17.4	8.2	7.7	23.2	18.6	10.7	10.1
3 month	23.0	24.0	29.3	29.3	24.7	28.2	31.3	28.2
6 month	45.7	47.0	51.7	52.2	41.1	41.4	46.9	47.2
1 year	2.2	1.9	2.1	2.1	1.3	1.6	0.4	0.4
Swiss franc LIBOR								
1 month	1.1	0.7	0.5	0.5	0.2	0.4	0.3	0.2
3 month	1.8	2.2	1.8	1.8	2.5	3.0	3.3	3.3
6 month	2.5	3.2	3.1	3.1	1.6	3.2	2.4	2.4
1 year	1.5	1.6	1.6	1.6	1.9	1.6	1.2	1.1
Central bank interest rate	0.1	0.1	0.2	0.2	0.0	0.0	2.6	2.6
Other	2.4	1.9	1.5	1.6	3.5	2.1	1.1	4.5

Source: Bank of Slovenia

More than 90% of interest-sensitive items are tied to the EURIBOR of varying maturities.

The most frequently used reference interest rate on the asset side remains the EURIBOR, accounting for 91.3% of the total. The proportion of items tied to the 3- and 6-month EURIBOR was up in 2009 at the expense of a decrease in the proportion of items tied to the 1-month EURIBOR. Hence the structure of interest-sensitive assets tied to EURIBOR maturities moved closer to the structure of interest-sensitive liabilities. The 6-month EURIBOR remains the most common reference interest rate used for interest-sensitive items. The second most important reference interest rate remains the Swiss franc LIBOR. However, its proportion began to decline owing to repayments and a halt in the approval of new loans tied to the Swiss franc. The proportion of interest sensitive assets tied to the Swiss franc was down 0.7 percentage points in 2009 to 7%, while the proportion of interest-sensitive liabilities was down 1 percentage point to 7.1%.

The banks closed their long positions in key reference interest rates in 2009.

The banks closed their long positions in key reference interest rates in 2009, but remain exposed to a rise in interest rates, which is favourable in the context of an expected rise in reference interest rates.

Table 6.40: Structure of interest-sensitive assets and liabilities by reference interest rate

	Total net position				Net position by bucket, Feb. 2010			
	Dec. 07	Dec. 08	Dec. 09	Feb. 10	Sight	Up to 1 year	1 to 5 years	More than 5 years
EURIBOR								
1 month	3.3	4.6	1.0	1.0	0.3	0.1	-1.0	1.5
3 month	4.8	5.4	5.8	7.0	2.8	0.1	0.9	3.2
6 month	12.4	15.6	12.8	13.4	2.7	-0.1	5.2	5.6
1 year	0.9	0.7	1.0	1.0	0.1	0.0	0.1	0.9
LIBOR								
1 month	0.6	0.3	0.2	0.2	0.1	0.0	0.0	0.1
3 month	0.2	0.3	-0.1	-0.1	0.2	0.0	-0.5	0.2
6 month	0.9	0.9	0.9	0.9	-0.3	0.0	-0.2	1.4
1 year	0.2	0.5	0.5	0.5	-0.1	0.0	-0.1	0.7
TOM	0.5	0.4	0.3	0.3	0.0	0.0	0.1	0.1

Source: Bank of Slovenia

6.9 Currency risk

Currency risk rose in 2009, but remains low.

Currency risk rose in 2009, but remains relatively low in terms of importance among other types of risk. The net open foreign exchange position as a proportion of regulatory capital stood at 0.9% at the end of 2009. The banks opened their positions in the currencies of the former Yugoslav republics and in the currencies of new EU Member States, and mostly closed their positions in major global currencies.

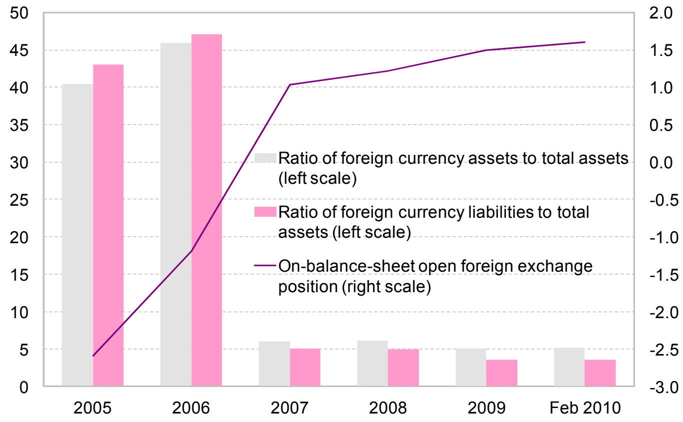
The large domestic banks are most exposed to currency risk, having held a net long foreign exchange position in the amount of 1.4% of regulatory capital at the end of 2009.

6.9.1 Currency breakdown of banks' balance sheets

The proportion of the banks' total assets accounted for by foreign currency items was down in 2009.

The proportion of the banks' total assets accounted for by foreign currency items in 2009 was down on the end of 2008. At the end of 2009 the proportion of foreign currency assets fluctuated at a level of 5%, while foreign currency liabilities accounted for 3.5% of total assets. The on-balance-sheet foreign exchange position remained long in 2009, at 1.5% of total assets.

Figure 6.50: Ratio of foreign currency assets and liabilities to total assets, and on-balance-sheet open foreign exchange position in percentages



Source: Bank of Slovenia

At the end of 2009 year-on-year growth in foreign currency assets and liabilities was -16.2% and -22.6% respectively. The reason for the negative growth lies in the banks' debt repayments to the rest of the world (in non-euro currencies) and a decrease in foreign currency lending, particularly in Swiss francs. A similar trend continued at the beginning of 2010.

There was a notable change in the currency breakdown, as the proportion of foreign currency assets and liabilities accounted for by Swiss francs was down, while the proportion accounted for by US dollars was up. The proportion accounted for by the currencies of new EU Member States and the former Yugoslav republics was up on the asset side, albeit at just 3.9% of foreign currency assets.

Table 6.41: Currency breakdown of assets and liabilities

	Dec. 2008		Dec. 2009		Feb. 2010	
	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities
Total foreign currency excluding euros, EUR million	3,108	2,528	2,605	1,957	2,644	1,960
year-on-year growth, %	14.3	11.5	-16.2	-22.6	-13.4	-19.2
Breakdown of currencies other than euros			(%)			
global currencies	98.1	99.5	94.9	99.3	95.3	99.0
Swiss franc	80.1	75.6	76.0	71.3	76.2	71.4
pound sterling	0.7	0.8	0.8	1.2	0.8	1.3
US dollar	16.0	22.0	16.7	25.5	16.7	24.9
Canadian dollar	0.4	0.4	0.5	0.6	0.6	0.7
yen	0.7	0.1	0.6	0.1	0.5	0.1
Australian dollar	0.2	0.4	0.5	0.6	0.5	0.6
new EU Member States	1.3	0.0	2.8	0.0	2.8	0.1
Scandinavia	0.2	0.3	0.5	0.5	0.5	0.4
former Yugoslav republics	0.3	0.2	1.3	0.2	1.1	0.2
other	0.0	0.0	0.3	0.0	0.3	0.3

Source: Bank of Slovenia

6.9.2 Open foreign exchange position

The net open foreign exchange position was long in the amount of EUR 41.4 million or 0.9% of regulatory capital at the end of 2009.

The net open foreign exchange position rose in 2009, but remains low. It was long and amounted to EUR 41.4 million or 0.9% of regulatory capital at the end of 2009. The majority of long net foreign exchange positions at the end of 2009 were those in investment fund units and in less significant currencies, while the banks held short net foreign exchange positions in major global currencies. This means that the banks are exposed to the risk of appreciation in major global currencies against the euro on the one hand, and to the risk of depreciation in other currencies on the other. The currencies of the former Yugoslav republics account for the majority of other currencies. The currencies of these countries have depreciated for the most part in the last year owing to the deteriorating macroeconomic conditions. There is no expectation of a reversal in this trend in the short term, as most of the former Yugoslav republics run large current account deficits. Nevertheless, currency risk for the Slovenian banks is low owing to the low values of open foreign exchange positions.

Table 6.42: Open foreign exchange positions by currency in EUR million

	Net position			Greater of sum of long and short positions		
	Dec. 08	Jun. 09	Dec. 09	Dec. 08	Jun. 09	Dec. 09
Global currencies	-39.5	-33.0	-28.9	49.5	42.8	37.1
US dollar	-22.9	-17.1	-14.7	26.8	22.0	19.1
Swiss franc	-19.2	-14.4	-12.3	19.6	17.6	14.6
Other (GBP, CAD, AUD, JPY)	2.6	-1.5	-1.8	5.7	3.2	3.4
EEA currencies	1.1	0.0	4.9	4.4	2.8	5.0
Other currencies	9.9	34.5	17.2	10.1	34.7	25.2
CIU	38.0	41.3	48.2	38.0	41.3	48.2
Total	9.5	42.8	41.4	62.6	88.6	86.6
As % of regulatory capital	0.2	1.0	0.9	1.5	2.0	1.9

Note: EEA: European Economic Area, i.e. the EU, Iceland and Norway; CIU: foreign exchange position in investment fund units.
Source: Bank of Slovenia

The open foreign exchange position according to the definition from capital requirements (i.e. the greater of the sum of all long positions and the sum of all short positions in individual currencies) stood at EUR 86.6 million or 1.9% of regulatory capital in 2009.

Table 6.43: Open foreign exchange positions by bank group in EUR million, December 2009

	Large domestic banks	Small domestic banks	Banks under majority foreign ownership	Overall
Global currencies	-25.1	1.2	-5.3	-28.9
US dollar	-14.1	0.6	-1.3	-14.7
Swiss franc	-8.5	0.3	-4.3	-12.3
Other (GBP, CAD, AUD, JPY)	-2.5	0.3	0.3	-1.8
EEA currencies	4.5	0.2	0.3	4.9
Other currencies	14.2	2.3	0.6	17.2
CIU	47.9	0.2	0.1	48.2
Total	41.6	3.9	-4.4	41.4
As % of regulatory capital	1.4	1.0	-0.4	0.9

Note: EEA: European Economic Area, i.e. the EU, Iceland and Norway; CIU: foreign exchange position in investment fund units.
Source: Bank of Slovenia

The domestic banks hold a long position, while the banks under majority foreign ownership hold a short net foreign exchange position.

The large domestic banks, which held a long net foreign exchange position in the amount of 1.4% of regulatory capital at the end of 2009, are most exposed to currency risk, followed by the small domestic banks with a long net position in the amount of 1% and the banks under majority foreign ownership with a short net position of 0.4% of regulatory capital.

6.9.3 Borrowing in Swiss francs

Negative growth in Swiss franc borrowing by non-banking sectors.

Growth in lending to non-banking sectors in Swiss francs or with a currency clause tied to the Swiss franc declined by 21.3% in 2009. Negative year-on-year growth continued at the beginning of 2010. The reasons for this lie primarily in the narrowing of the spread between the EURIBOR and Swiss franc LIBOR, the trend of appreciation in the Swiss franc, which was particularly pronounced at the beginning of 2010, and the banks' high premiums on Swiss franc loans.

Table 6.44: Stock and year-on-year growth of loans in Swiss francs or with a Swiss franc currency clause

	Non-banking sectors	Non-financial corporations	OFIs	Government	Households: All loans	Households: Housing loans
	Stock of loans, EUR million					
2008	2,403.8	743.6	226.6	7.4	1,426.2	1,125.8
2009	1,891.4	464.8	173.3	6.4	1,246.9	1,034.9
Feb. 10	1,879.4	459.6	174.7	6.4	1,238.7	1,033.1
	Year-on-year growth, %					
2008	21.1	-5.1	34.7	-0.2	39.1	46.3
2009	-21.3	-37.5	-23.5	-13.5	-12.6	-8.1
Feb. 10	-18.9	-33.1	-18.0	-20.4	-12.1	-7.7

Source: Bank of Slovenia

At the end of 2009 the proportion of the total stock of loans to non-banking sectors tied to the Swiss franc or with a Swiss franc currency clause was 4.9%, down 2.3 percentage points on the end of 2008.

Table 6.45: Loans tied to the Swiss franc exchange rate by bank group

	Year-on-year growth, %		Proportion of all loans to non-banking sectors tied to Swiss franc, %		Proportion of loans at particular bank group, %	
	2008	2009	2008	2009	2008	2009
Large domestic banks	22.8	-19.5	31.0	31.7	4.0	2.6
Small domestic banks	-17.7	-7.1	0.9	1.1	0.9	0.7
Banks under majority foreign ownership	21.1	-21.4	68.1	67.2	13.5	9.8
Overall	21.1	-21.3	100.0	100.0	7.2	4.9

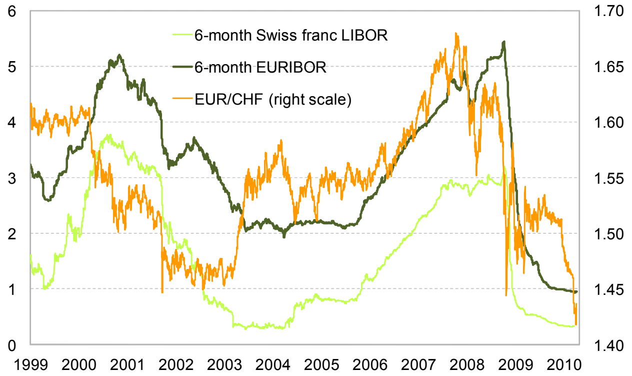
Source: Bank of Slovenia

The Swiss franc appreciated by 3.8% against the euro in the first three months of 2010.

The Swiss franc was virtually unchanged against the euro at the end of 2009 in year-on-year terms, but rose by 3.8% against the euro in the first three months of 2010. The main reasons for the Swiss franc's appreciation against the euro were encouraging forecasts regarding growth in the Swiss economy, its current account surplus and the adverse impact of Greece's public finance problems on the value of the euro. Nevertheless, a more pronounced appreciation in the Swiss franc in the short term is unlikely, as the Swiss central bank continues to implement an expansionary monetary policy and is dampening growth in the Swiss franc through interventions on the currency market.

The 6-month Swiss franc LIBOR is still lower than the 6-month EURIBOR, but the spread had narrowed significantly to 0.62 percentage points by the end of March 2010. The low value of the Swiss franc LIBOR is acting to ease the debt servicing burden on borrowers and, to a limited degree, is offsetting the effect of the Swiss franc's appreciation against euro.

Figure 6.51: LIBOR reference interest rate for Swiss francs and the EURIBOR, and changes in the euro / Swiss franc exchange rate



Source: Bank of Slovenia

6.10 Bank solvency

The banking system's capital adequacy was unchanged in 2009. Growth in regulatory capital and capital requirements was low. Owners are less willing to increase capital in the adverse economic conditions. The banks' ability to increase subordinated debt is assessed as sufficient. Capital requirements reflect the banks' diminishing readiness to take up additional credit risk and the deteriorating quality of the credit portfolio.

The small banks are most vulnerable. Their capital requirements for regulatory high-risk items account for the highest proportion of total capital requirements for credit risk, while they record the highest growth in capital requirements for past-due items among all three bank groups. Thus the small banks have the lowest capital adequacy and Tier 1 capital adequacy, and lag most behind comparable EU banks in terms of capital adequacy. The small banks recorded the sharpest decline in original own funds as a proportion of capital prior to deductions in 2009, which indicates the deteriorating quality of their regulatory capital.

The capital adequacy of the banks under majority foreign ownership is below the EU average. This bank group also recorded a decline in the proportion of original own funds in 2009. The prevailing sentiment in the past was that the banks under majority foreign ownership received strong support from their parent banks, where they can raise additional capital. The soundness of this assumption has waned given the problems faced by certain parent banks during the financial turmoil. Therefore, greater attention is also required at the banks under majority foreign ownership.

The small banks and the banks under majority foreign ownership will soon find it difficult to make up the gap with comparable European banks in terms of the level of capital adequacy. Tier 1 capital adequacy, which also effects banks' credit ratings and their funding costs, is becoming an increasingly important indicator for all banks. In line with amended banking regulations, banks that include innovative instruments in original own funds will be forced to replace these instruments with higher-quality forms of capital over the longer term. At a time when it is difficult to carry out capital increases, it is not possible to counter the contraction in financial intermediation by reducing or slowing growth in investments. The banks under majority foreign ownership recorded a decline in capital requirements in 2009. In this context, we can also expect a reduction in deduction items, which are primarily linked to capital investments, at the banks under domestic ownership.

At the banks requiring capital increases, it is not enough that owners search merely for appropriate returns; they must assume responsibility with management boards for past business decisions and provide sufficient capital. During periods of economic growth, owners took up additional risk, supported expansionary lending policies and reaped the associated returns. The capital required by the banks today is partly a result of poor lending decisions from the period of high growth, and partly a result of requirements deriving from the international environment for improving the quality of capital.

6.10.1 Capital adequacy

Capital adequacy remained at the level achieved in 2008.

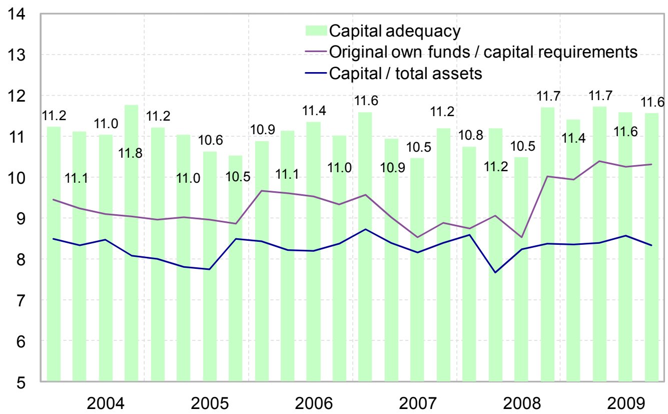
The banking system's capital adequacy remained at the level achieved in 2008 throughout 2009. Capital adequacy was up 1.2 percentage points to 11.7% in the final quarter of 2008 owing to the abolition of the prudential filter and capital increases. Capital adequacy and Tier 1 capital adequacy stood at 11.6% and 9.3% respectively at the end of 2009. Despite the financial turmoil, the banking system's capital adequacy did not decline significantly in 2009. The banks instead reduced their financial leverage. The ratio of the book value of capital to total assets was up 0.2 percentage points to 8.6%, a reflection of stagnating lending growth. Consequently, growth in capital requirements was also low. The latter was most evident in the final quarter of 2009, when capital requirements were up merely EUR 8 million, compared with an increase of EUR 42 million over the previous three quarters.

Table 6.46: Basic indicators of the banking system's capital adequacy in percentages

	2004	2005	2006	2007	2008	2009
Capital adequacy	11.8	10.5	11.0	11.2	11.7	11.6
Original own funds / capital requirements	9.0	8.9	9.3	8.9	10.0	10.3
Tier 1 capital / capital requirements	8.1	7.6	8.3	7.8	9.2	9.3
Book value of capital / total assets	8.1	8.5	8.4	8.4	8.4	8.6

Note: Tier 1 – original own funds less deduction items.
Source: Bank of Slovenia

Figure 6.52: Basic indicators of the banking system's capital adequacy in percentages



Source: Bank of Slovenia

The large domestic banks achieve the highest capital adequacy.

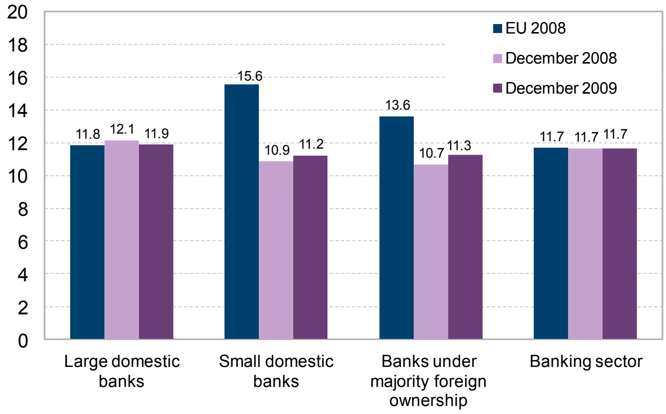
The large domestic banks achieve the highest capital adequacy. The capital adequacy of the large banks was down in 2009 owing to significantly lower growth in regulatory capital (1.4%) than in capital requirements (6.3%). It was down 0.6 percentage points to stand at 11.8%. Capital adequacy improved in the other two bank groups with respect to 2008. The small banks recorded the highest year-on-year growth in regulatory capital of all bank groups, at 10.1%. The capital requirements of the banks under majority foreign ownership were down on 2008 in nominal terms.

Table 6.47: Capital adequacy by bank group on an individual basis in percentages

	2004	2005	2006	2007	2008	2009
Large domestic banks	12.0	10.5	11.0	11.9	12.3	11.8
Small domestic banks	11.7	10.8	10.9	12.1	10.8	11.1
Banks under majority foreign ownership	11.3	10.5	11.1	9.3	10.6	11.2
Slovenian banking sector	11.8	10.5	11.0	11.2	11.7	11.6

Source: Bank of Slovenia

Figure 6.53: Capital adequacy by bank group on a consolidated basis in comparison with the EU average in percentages



Sources: Bank of Slovenia, EU Banking Sector Stability, ECB, August 2009.

The small banks lag most behind the EU average in terms of capital adequacy.

Taking into account the EU average for 2008, the capital adequacy of the large domestic banks is at the same level as comparable EU banks, while the small banks lag most behind the EU average. Their capital adequacy is 4.4 percentage points below the average for small EU banks. The capital adequacy of the banks under majority foreign ownership is 2.3 percentage points below that of comparable EU banks. In the context of unchanged capital requirements, the small banks would need to increase regulatory capital by EUR 168 million or 39% to reach the same average level of capital adequacy on a consolidated basis as comparable EU banks. The banks under majority foreign ownership would require additional capital of EUR 261 million, an increase of 21%.

The lowest Tier 1 capital adequacy is achieved by the small banks, which again lag most behind the EU average.

There was no significant change in Tier 1 capital adequacy by individual bank group with respect to 2008. The exception were the banks under majority foreign ownership, where Tier 1 capital adequacy also improved owing to a reduction in capital requirements. The small domestic banks still record the lowest Tier 1 capital adequacy.

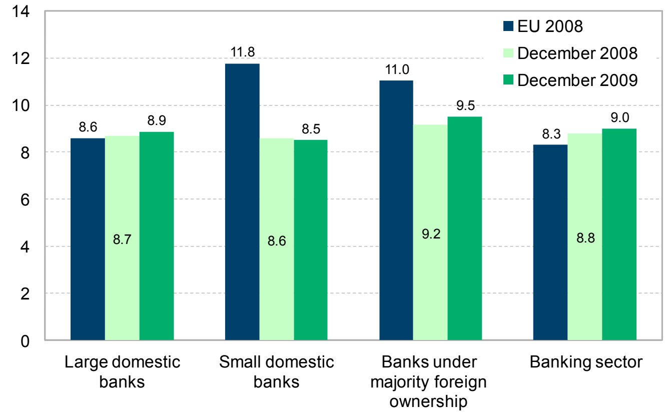
The small banks also lag behind the average of comparable EU banks in terms of Tier 1 capital adequacy. To reach the EU average, the small banks would have to increase original own funds on a consolidated basis by EUR 126 million or 38%. The banks under majority foreign ownership would require a relative increase in original own funds of 16% or EUR 170 million. The Tier 1 capital adequacy of the large domestic banks exceeds the average of comparable EU banks.

Table 6.48: Tier 1 capital adequacy by bank group on an individual basis in percentages

	2004	2005	2006	2007	2008	2009
Large domestic banks	7.4	6.8	7.4	7.3	9.3	9.4
Small domestic banks	9.2	8.1	8.6	9.6	8.5	8.5
Banks under majority foreign ownership	9.0	9.4	10.2	8.1	9.1	9.5
Slovenian banking sector	8.1	7.6	8.3	7.8	9.2	9.3

Source: Bank of Slovenia

Figure 6.54: Tier 1 capital adequacy by bank group on a consolidated basis in comparison with the EU average in percentages

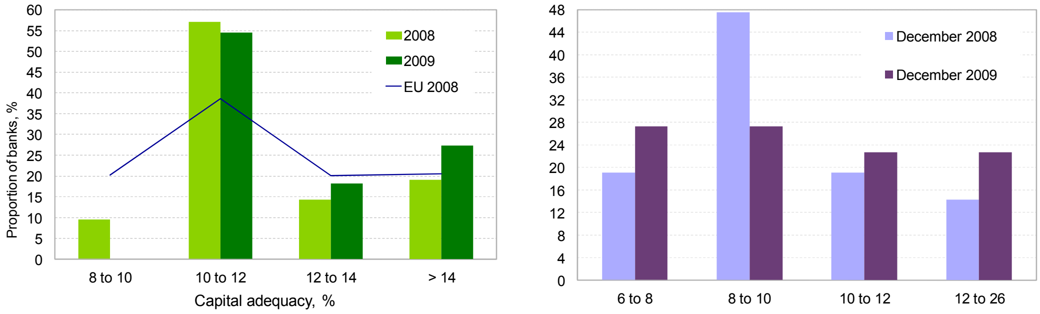


Source: Bank of Slovenia, EU Banking Sector Stability, ECB, August 2009

No bank had a capital adequacy of less than 10% at the end of 2009.

There was a positive shift towards higher intervals in the distribution of banks in terms of capital adequacy. No bank had a capital adequacy of less than 10% at the end of 2009. The proportion of banks with a capital adequacy exceeding 12% was up.

Figure 6.55: Distribution of banks' capital adequacy (left) and Tier 1 capital adequacy in percentages



Source: Bank of Slovenia, EU Banking Sector Stability, ECB, August 2009

The distribution of Tier 1 capital adequacy flattened.

The distribution of Tier 1 capital adequacy flattened with respect to 2008. The proportion of banks where Tier 1 capital adequacy exceeds 10% was up, while the proportion of banks with a Tier 1 capital adequacy of less 8% also increased. The increase in the proportion of banks with a low Tier 1 capital adequacy reflects declining capital adequacy and the deteriorating capital structure of individual banks. At the overall banking system level, the Tier 1 capital adequacy of nine banks declined in 2009, by an average of 0.6 percentage points. The structure of capital at certain small banks and banks under majority foreign ownership deteriorated.

6.10.2 Capital

Original own funds increased on account of share capital and retained earnings.

At the end of 2009 the banking system's original own funds stood at EUR 4.1 billion, up EUR 282 million on the end of 2008. The increase derives from in increase in share capital in the amount of EUR 165 million, and an increase in reserves and retained earning of EUR 131 million.

Table 6.49: Regulatory capital and its components, stock and increase in EUR million, year-on-year growth in percentages

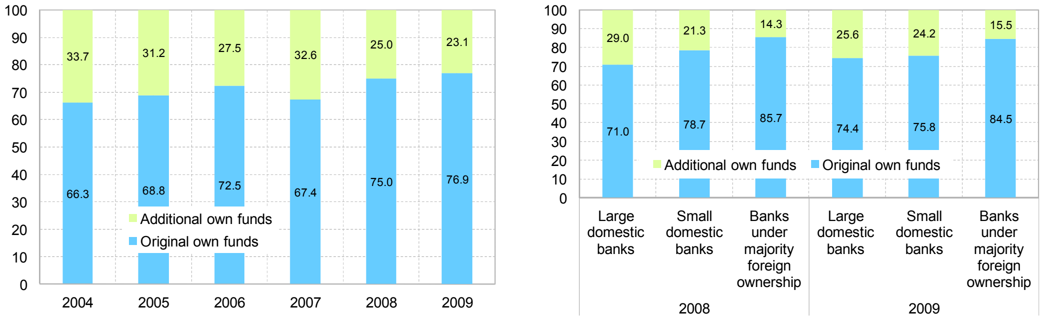
	2008	2009		
	Stock	Stock	Increase	Growth
Regulatory capital	4,475	4,616	141	3.1%
Original own funds	3,835	4,116	282	7.3%
Tier I additional own funds	1,277	1,239	-38	-3.0%
Deduction items	636	739	103	16.2%
Original own funds for capital adequacy calculation	3,501	3,722	220	6.3%
Tier I additional own funds for capital adequacy calculation	974	894	-80	-8.2%
Tier II additional own funds	0	0	0	

Source: Bank of Slovenia

The large banks improved their capital structure.

The quality of the banking system's capital improved in 2009. The proportion of capital prior to deductions accounted for by original own funds was up 1.9 percentage points. A more detailed analysis indicates that this is only true for the large banks, while the proportion of original own funds at the small banks and the banks under majority foreign ownership was down. The proportion of original own funds was down by more than 5 percentage points at three banks.

Figure 6.56: Structure of capital prior to deductions for the banking system as a whole (left), and by bank group (right) in percentages



Source: Bank of Slovenia

The proportion of original own funds accounted for by earnings declined, thus increasing the banks' dependence on capital increases.

The proportion of original own funds accounted for by current and retained earnings was down. These items accounted for 47% of original own funds in 2009, compared with 60% in 2006 and 2007. In the past, retained earnings were considered a key source for increasing original own funds. Their importance is now diminishing. The reduction in financial leverage on the investment side, which is being seen in stagnating lending growth, means a decline in generated profits in the future as well. This increases the banks' dependency on owners and their willingness to carry out capital increases.

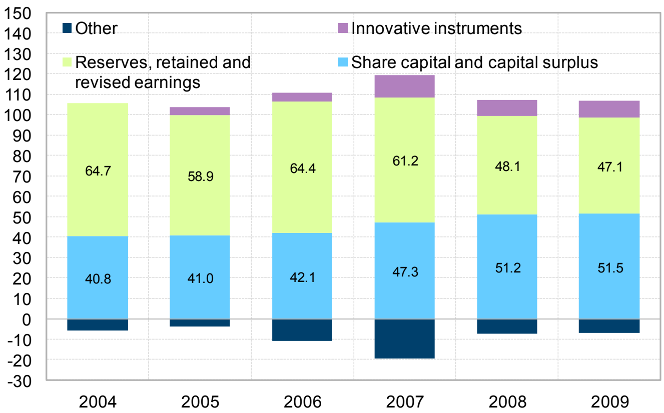
Five banks include innovative instruments, which they will be forced to replace, in original own funds.

Five banks include innovative instruments in original own funds. The total stock of these instruments stands at EUR 331 million, and was up EUR 26 million in 2009.[36] In line with amended regulations, the banks will be forced to replace these instruments with higher-quality forms of capital.

Seven banks are planning capital increases in the next three years, primarily owing to growth in turnover.

According to survey data, seven banks are planning capital increases in the next three years. It is primarily small banks that are planning capital increases. The total amount of planned capital increases is EUR 140 million. In addition to the desire to improve capital adequacy, the main reason for capital increases is the expected growth in turnover. According to survey data, banks are planning 7.3% growth in total assets in 2010. The lowest growth in total assets of 6.6% is planned by the large banks, while the highest growth of 7.9% is planned by the banks under majority foreign ownership. The banks intend to make the majority of capital increases via the subscription of share capital and, to a lesser degree, by increasing subordinated debt.

Figure 6.57: Components of original own funds in percentages



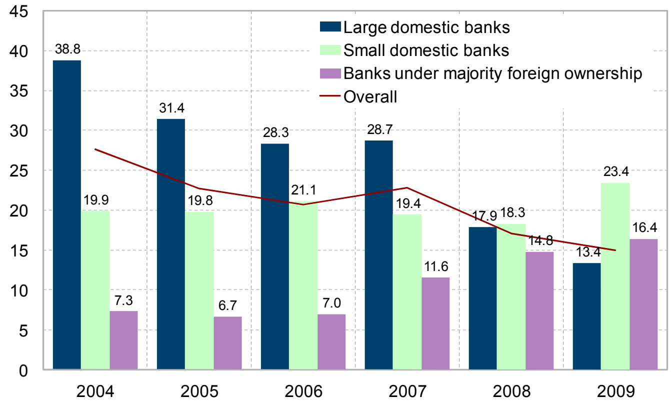
Source: Bank of Slovenia

36 These five banks may take into account innovative instruments in the amount of EUR 250 million in original own funds.

The large banks decreased their stock of subordinated debt. The banking system's potential for increasing subordinated debt stood at EUR 1.4 billion.

The stock of the banking system's subordinated debt was down EUR 40 million in 2009, at EUR 616 million. The large banks made the most significant reduction in subordinated debt, of EUR 83 million. The small banks and the banks under majority foreign ownership increased their stock of subordinated debt, each group by slightly more than EUR 20 million. Consequently, the ratio of subordinated debt to original own funds was up 5.1 percentage points at the small banks and up 1.6 percentage points at the banks under majority foreign ownership. The large banks also reduced their stock of hybrid instruments and surplus in innovative instruments, which is transferred to additional own funds. There was no significant change in the stock of these items at the other two bank groups. The ratio of subordinated debt to original own funds exceeded 40% at three banks, and was close to 40% at two others.[37]

Figure 6.58: Ratio of subordinated debt to original own funds by bank group in percentages



Source: Bank of Slovenia

According to figures at the end of 2009, the banking system's potential for increasing subordinated debt stood at EUR 1.4 billion, up EUR 180 million on the end of 2008. This figure was up EUR 194 million in the last year at the large banks, but down at the other two bank groups (by EUR 10.5 million at the small banks and by more than EUR 3 million at the banks under majority foreign ownership). Assuming growth in capital requirements equal to planned growth in total assets (i.e. 7.3% on the basis of the bank survey), the banking system's potential for increasing subordinated debt would be sufficient to cover the capital requirement of the next 9.1 years.

Deductions from original own funds were up EUR 103 million in 2009.

Deductions from original own funds and additional own funds deriving primarily from capital investments were up EUR 103 million in 2009, to EUR 739 million. Original own funds and additional own funds cover 53.4% and 46.6% of deduction items respectively.

Growth in regulatory capital lagged behind growth in capital requirements. The surplus of regulatory capital over capital requirements was 30.8%.

At the end of 2009 the banking system's regulatory capital stood at EUR 4.6 billion, up EUR 141 million or 3.1% on the previous year. On account of the large banks, the banking system's growth in regulatory capital lagged behind the growth in capital requirements of 4.4%. The banking system's surplus of regulatory capital over capital requirements, which reflects the banks' capacity to absorb risks, was down 0.8 percentage points in 2009, at 30.8% of regulatory capital, although it was up at the banks under majority foreign ownership and the small domestic banks.

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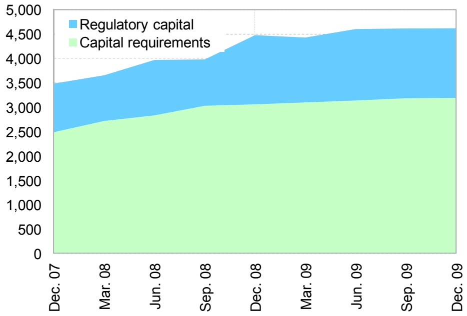
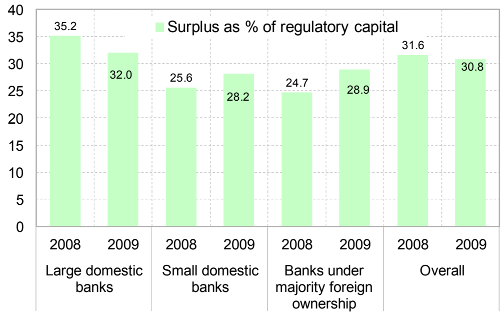
[37] The regulatory limit is 50%.

Figure 6.59: Regulatory capital and capital requirements in EUR million (left) and surplus of capital over capital requirements as percentage of regulatory capital (right)





Source: Bank of Slovenia

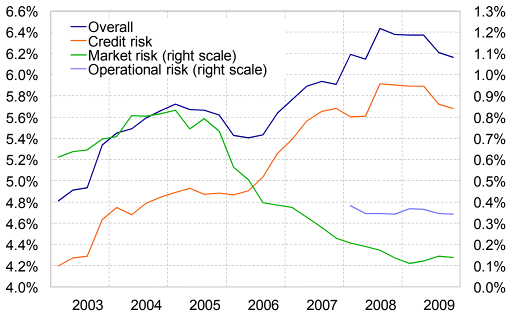
6.10.3 Capital requirements

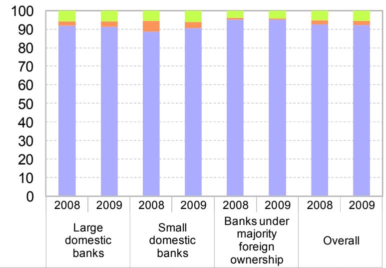
The banks are less willing to take up additional credit risks.

Capital requirements were up EUR 134 million in 2009 to stand at EUR 3.2 billion. The majority of capital requirements relate to credit risk. However, with the outbreak of the financial turmoil, the banks are less willing to take up additional credit risks. This is demonstrated by the ratio of capital requirements for credit risk to total assets, which was down 0.2 percentage points in 2009 at 5.7%. The majority of this decline was recorded by the banks in the third quarter of 2009. There was no change in the ratio of capital requirements for market and operational risk to total assets.

The proportion of the banking system's capital requirements for credit risk was down 0.3 percentage points, at 92.2%, the decline relating entirely to the large domestic banks. The small domestic banks recorded an increase in the proportion of capital requirements for credit risk of 1.9 percentage points in 2009. The large banks responded to the changing conditions in the context of the financial turmoil in the structure of both capital and capital requirements. This is not apparent at the small banks, which are still willing to take up additional credit risk.

Figure 6.60: Ratio of capital requirements to total assets (left) and structure of capital requirements by bank group (right) in percentages





	Large domestic banks 2008	Large domestic banks 2009	Small domestic banks 2008	Small domestic banks 2009	Banks under majority foreign ownership 2008	Banks under majority foreign ownership 2009	Overall 2008	Overall 2009
Operational risk	5.9	6.0	5.7	6.2	4.0	4.3	5.4	5.6
Market risk	2.2	2.9	5.7	3.3	0.8	0.4	2.1	2.2
Credit risk	91.8	91.1	88.6	90.6	95.2	95.2	92.5	92.2

Source: Bank of Slovenia

Shift from exposure to corporates to institutions and retail banking.

The decrease in the banking system's appetite to take up credit risk is reflected in the structure of capital requirements for credit risk as a reduction in capital requirements for corporate exposures of EUR 73 million. This reduction relates in an approximately equal amount to the large banks and the banks under majority foreign ownership. The large banks shifted their focus to institutions,[38] which resulted in an increase in their capital requirements of EUR 61 million or 43%. In contrast, the banks under majority foreign ownership focused their activities on retail banking, where they recorded the largest increase in capital requirements, in the amount of EUR 18.5 million or 8.1%.

Growth in capital requirements for past-due items is a reflection of the deteriorating quality of the credit portfolio.

The deteriorating quality of the credit portfolio is seen in a significant increase in capital requirements for past-due items. These doubled (by nearly EUR 50 million) for the banking system overall in 2009. The majority, or 60%, of the increase relates to the large banks. The highest year-on-year growth was recorded by the small banks, where total capital requirements for past-due items were nearly five times higher than at the end of

[38] Financial institutions, investment firms, clearing houses and stock exchanges.

2008. At the end of 2009 capital requirements for past-due items for all the bank groups accounted for more than 3% of capital requirements for credit risk.

The small banks are most vulnerable with respect to the structure of capital requirements.

The small banks are most vulnerable with respect to the structure of capital requirements for credit risk, as they have the smallest proportion of capital requirements for corporate and retail banking exposures. Their exposures secured by real estate account for 8.1% of capital requirements for credit risk, while this proportion is less than 1% for the other bank groups. The small banks apply lower weights and allocate less capital for exposures secured by real estate. The other bank groups classify these exposures as corporate and retail banking exposures. The weight taken into account in the calculation of capital requirements in these segments may be double the typical weight. Moreover, the small banks record the highest proportion of capital requirements for regulatory high-risk items, which is partly linked to the financing of M&A activities. Growth in capital requirements for past-due items is also highest at the small banks.

Table 6.50: Capital requirements for credit risk for the banking system and bank groups in EUR million

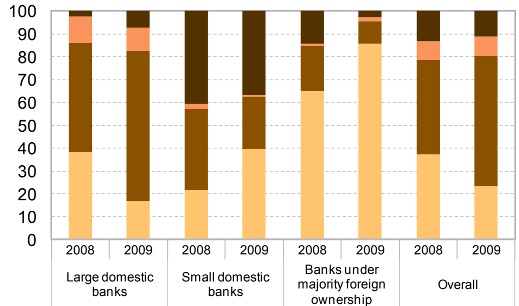
	2008				2009				Change			
	Large domestic banks	Small domestic banks	Banks under majority foreign ownership	Overall	Large domestic banks	Small domestic banks	Banks under majority foreign ownership	Overall	Large domestic banks	Small domestic banks	Banks under majority foreign ownership	Overall
Capital requirements for credit risk, EUR million	1741.6	253.5	835.0	2830.1	1837.3	275.4	831.6	2944.2	95.7	21.8	-3.5	114.1
	Breakdown in capital requirements for credit risk, %								Change, percentage points			
General government, international organisations	0.5	0.5	1.0	0.6	0.4	1.0	1.2	0.7	-0.1	0.5	0.2	0.1
Institutions	8.3	5.2	4.1	6.7	11.2	5.6	3.3	8.4	2.9	0.5	-0.8	1.7
Corporates	63.8	59.0	59.4	62.1	58.5	54.6	55.3	57.2	-5.3	-4.4	-4.2	-4.9
Retail banking	17.2	13.4	27.4	19.9	17.0	13.1	29.8	20.2	-0.3	-0.3	2.3	0.3
Exposures secured by real estate	0.0	5.6	0.6	0.7	0.0	8.1	0.6	0.9	0.0	2.5	0.0	0.3
Past-due items	1.9	0.6	1.7	1.7	3.4	3.1	3.2	3.3	1.5	2.5	1.5	1.6
Regulatory high-risk categories	5.8	10.3	3.8	5.6	5.5	9.5	3.9	5.5	-0.3	-0.9	0.1	-0.2
Other	2.4	5.4	2.0	2.6	4.0	5.0	2.7	3.7	1.5	-0.4	0.7	1.1

Source: Bank of Slovenia

Capital requirements for market risk were up at the large banks, but down at the other bank groups.

Capital requirements for market risks were up 10% in 2009. However, the increase related to the large banks, where capital requirements for equity instruments nearly doubled. The reason primarily lies in securities received by banks via the redemption of collateral for bad loans. There was a significant decrease in capital requirements for markets risks in the other bank groups, by 39% at the small banks and by 45% at the banks under majority foreign ownership. The main reason at the small banks was a decrease in capital requirements for equity instruments, and a decrease in capital requirements for both equity and debt instruments at the banks under majority foreign ownership.

Figure 6.61: Breakdown of capital requirements for market risks by bank group in percentages



	Large domestic banks 2008	Large domestic banks 2009	Small domestic banks 2008	Small domestic banks 2009	Banks under majority foreign ownership 2008	Banks under majority foreign ownership 2009	Overall 2008	Overall 2009
Other	2.5	7.4	40.7	36.8	14.4	2.8	13.3	11.2
Foreign currencies	11.6	10.0	1.9	0.8	0.8	1.7	8.0	8.3
Equity financial instruments	47.6	66.0	35.5	22.9	19.8	10.0	41.6	57.0
Debt financial instruments	38.3	16.7	21.9	39.6	65.0	85.6	37.1	23.5

Source: Bank of Slovenia

Capital requirements for operational risk increased at all bank groups.

Capital requirements for operational risk increased at all the bank groups in 2009, and amount to EUR 178 million for the banking system overall, up EUR 13.4 million or 8.2% on 2008. At 15%, the small banks recorded the largest increase in capital requirements for operational risk.

7 NON-BANKING FINANCIAL INSTITUTIONS

7.1 Insurers

7.1.1 Features of insurers' business and comparison with the EU

An increase in concentration in the voluntary pension insurance segment.

There were 15 insurance companies and two reinsurance companies operating in Slovenia at the end of 2009. Concentration in the insurance sector remains high. The market share of the largest insurance company in terms of written premium declined by 1 percentage point to 38%, while the largest market share in voluntary supplementary pension insurance was up 8 percentage points at 55%. The largest insurance company covers 37% of the non-life insurance market, and 42% of the life insurance market. The market share of the largest reinsurance company remains unchanged at 56%.

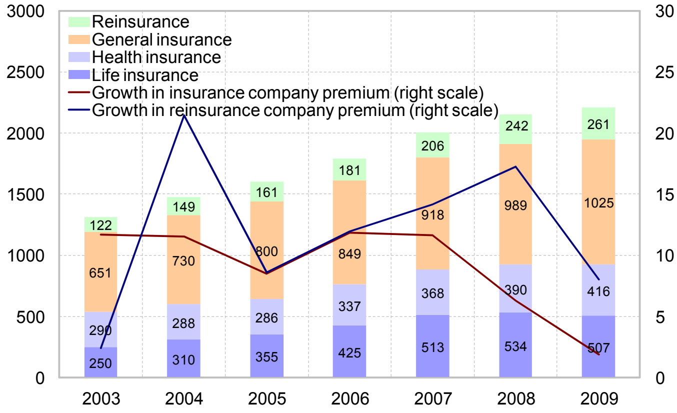
The insurers' performance in 2009 was affected by the uncertainty on the capital markets, which reduced the demand for insurance products with investment risk. The decline in economic activity meant that there was lower demand for bank loans, which reduced the demand for credit insurance at the insurers. Last year again saw several hailstorms and floods at the end of the year. The size of the claims was extremely high for the second consecutive year. In conjunction with the adverse market situation, this had an impact on the insurers' liquidity. They made use of credit lines at banks to settle their due liabilities on time, while a large insurance company issued a bond with a nominal value of EUR 30 million.

Insurers recorded an increase of 3.7% in general insurance premium and a decline of 5.1% in life insurance premium in 2009.

The insurers' gross written premium in 2009 was up a modest 1.9%, the lowest annual growth since 2000,[39] at EUR 1,948 million. Written premium was up 3.7% for general insurance and 6.8% for health insurance, but was down 5.1% for life insurance. The largest decline in written premium of 13.2% was recorded by pension insurance.

Net insurance technical provisions were up 14.2%, while coverage by the assets covering technical provisions was up 3.6 percentage points at 118.8%, a consequence of the short-term growth in the capital markets. The insurers' ROE[40] in 2009 was up slightly at 3%, an indication of improved performance compared with the previous year, but individual insurers nevertheless ended the year with a loss. The total value of capital increases made at Slovenian insurers last year was EUR 25 million, equivalent to an 11% increase in paid-up share capital. Last year there were capital increases at six insurance companies, while the two reinsurance companies are planning capital increases in 2010. The average ROE in the euro area was 2% at the end of the third quarter of 2009.[41]

Figure 7.1: Gross written premium by type of insurance in EUR million (left scale), and annual growth in percentages (right scale)



Source: ISA

[39] Figures are available from 2000.
[40] For insurance companies and reinsurance companies ROE and ROA are calculated from profits after tax.
[41] Source: ECB: Financial Stability Review, December 2009.

Despite the lower growth in the reinsurance companies' gross written premium, the increase of 8% to EUR 261 million is satisfactory. The increase was also the result of insurance companies opting for traditional reinsurance products aimed at improving solvency during conditions of financial uncertainty. Equity has been declining in value as a result of the negative operating result in the 2008 financial year, which continued at the end of the third quarter of 2009. Reinsurance companies' ROE averaged around 10% in the euro area at the end of the third quarter of 2009.

Slovenia's premium per person for life insurance is just 15% of the euro area average.

The proportions of written premium accounted for by general insurance and by health insurance each rose by 1 percentage point to 53% and 21% respectively, at the expense of a decline in that of life insurance to 26%. The insurers' total written premium in 2009 amounted to 5.6% of GDP, which is EUR 954 per person, just under 38% of the written premium per person in the euro area overall. Primarily as a result of high claims during natural disasters in the last two years, there has been a tendency to raise premiums for non-life insurance, or to opt for insurance with lower premiums that offers less coverage. At the same time the figure for written premium for life insurance is just 15%, which is additional motivation to promote sales.

Table 7.1: Total gross written premium and gross written life insurance premium of insurance companies expressed in various categories for Slovenia in 2009 and for selected countries in 2008

	Slovenia	EU15	EU27	Portugal	Austria	Germany	UK
Total premium, EUR billion	1.95	1,063.7	1,099.1	15.4	16.3	165.3	306.1
per person, EUR	954	2,534	2,081	1,443	1,949	1,985	4,663
as % GDP	5.6	8.7	8.3	9.2	5.8	6.6	15.7
Life insurance premium, EUR billion	0.51	662.0	678.9	11.1	7.4	75.7	233.0
per person, EUR	248	1,608	1,310	1,036	882	916	3,795
as % of total premium	26.0	62.2	61.8	71.7	45.3	45.8	76.1
as % GDP	1.5	5.5	5.2	6.6	2.6	3.0	12.8

Sources: ISA, Swiss Re, own calculations

Greater segmentation of insurance products is expected, with greater differentiation of policyholders.

The crisis situation offers an opportunity for insurers to reach price-sensitive groups of policyholders by means of advisory services and improvements in the quality and pricing of their products, thereby increasing market share. Competition will force insurers into greater segmentation of insurance products, and differentiation between low-risk and high-risk policyholders. However, the capital and financial solidity of the insurers take precedence over long-term growth and the generation of profits. The deterioration in the position of policyholders as a result of the weaker macroeconomic environment could lead to more fraudulent claims, particularly in non-life insurance, and to premature termination of long-term policies in life insurance.

Life insurance and contractual integration of insurers with banks

Investment-based life insurance declined in relative terms compared with traditional forms of life insurance.

The total assets of life insurance accounted for 54% of the total assets of the insurers at the end of 2009. As a result of the experience of heavy losses on the capital markets, written premium for unit-linked life insurance declined by 7.5%. Some policyholders had difficulties in settling their liabilities, and a portion of the concluded policies are therefore in a state of premium holiday or have even been terminated. Last year there were a quarter more cancellations of life insurance policies, equivalent to 6% of existing life insurance at the end of 2009. The proportion of total written life insurance premium accounted for by life insurance in which policyholders assume the investment risk declined slightly to 45.9%, in favour of traditional forms of life insurance. The relative importance of these investments in the life insurance portion of the insurers' balance sheet rose again, by 5.3 percentage points to 24.6%, compared with 21.4% in euro area countries in 2008.[42]

[42] Source: CEIOPS, Statistical annex 2008.

Table 7.2: Insurers' written premium in EUR million and number of policyholders for life insurance and pension insurance

	2006	2007	2008	2009	2006	2007	2008	2009
Life insurance total					Growth, %			
premium, EUR million	425	513	534	507	19.7	20.6	4.1	-5.1
number of policyholders	986,803	1,140,435	1,196,312	1,206,786	6.5	15.6	4.9	0.9
Unit-linked life insurance					Proportion of life insurance, %			
premium, EUR million	173	238	252	233	40.8	46.3	47.1	45.9
number of policyholders	216,122	309,009	361,639	432,509	21.9	27.1	30.2	35.8
Voluntary supplementary pension insurance								
premium, EUR million	16	44	57	49	3.8	8.6	10.7	9.8
number of policyholders	42,413	113,246	123,281	81,295	4.3	9.9	10.3	6.7

Source: ISA

The banks' ties with the insurers in marketing insurance products declined. The volume of transactions in terms of written premium was down 22% for life insurance at EUR 30.4 million, but was up 42% for non-life insurance, although the figure is relatively small at EUR 1.5 million. The banks' commission is around 9% of the value of marketing the insurance policies.[43]

A decline in written premium for insurance products marketed via banks.

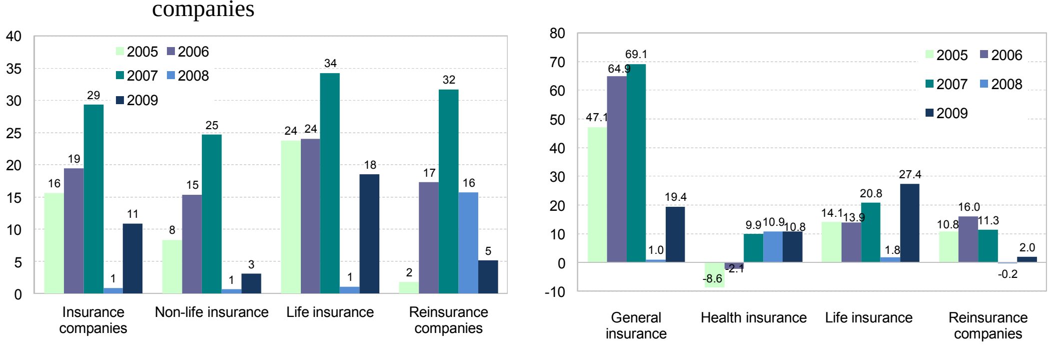
Financial statements of insurers

The insurers' total assets increased by a high 10.9% in 2009 to EUR 5.1 billion, only partly as a result of the increase in gross written premium. The total assets of non-life insurance were up 3.1%, while those of life insurance were up 18.5%. The total assets of the reinsurance companies were up 5.1% over the first three quarters of 2009 at EUR 590 million.

The insurers' total assets reached EUR 5.1 billion.

The increase was also the result of the gradual improvement on the capital markets after March 2009, which brought a rise in the value of investments in investment funds and shares. Prices of debt securities also rose, although the insurance sector is faced with the risk of yields on government bonds remaining low for a long time. Low yields have an adverse impact on the value of the insurers' liabilities, as they are used to discount future liabilities. The increase in the net present value of the liabilities is primarily of concern to life insurance companies, which have many policies with guaranteed returns. It is harder to generate satisfactory income from investments when yields are low. This situation could lead to a quest for investments to fill the gap between the guaranteed return and the risk-free interest rate. The crisis in the real sector has increased the risk in investing in corporate securities. In the event of any problems in the banking sector or other financial sectors, the problems could be transferred to the insurance sector via equity-debt links.

Figure 7.2: Growth in total assets in percentages (left) and result from ordinary activities in EUR million (right) of insurance companies and reinsurance companies



Note: The figures for reinsurance companies in 2009 relate to the end of the third quarter.
Source: ISA

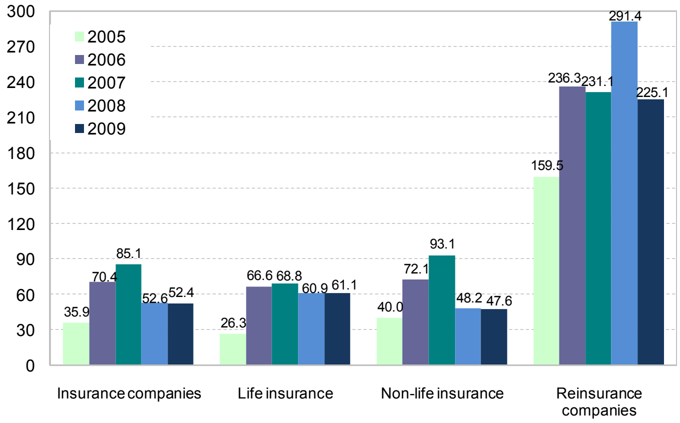
The insurers' net profit rose to EUR 23 million in 2009, just over half of the average in the five years before the financial and economic crisis. Despite the overall system-wide positive result, several insurers still made losses: four in general insurance, two in life insurance, and one in health insurance. The reinsurance companies declared a net loss of EUR 3 million at the end of the third quarter of 2009.

The insurance companies' net profit rose in 2009, while the reinsurance companies were still declaring a loss over the first three quarters of 2009.

[43] Source: Bank survey.

The insurers' surplus of available capital over the minimum capital requirement was almost unchanged at the end of 2009 at 52.4%. Neither were there any major changes in the breakdown between life insurance and non-life insurance. One insurer was still in a state of capital inadequacy in the non-life segment, which entails a ratio of 14.4% to gross insurance premium.

Figure 7.3: Surplus of available capital over minimum capital requirement at insurance companies and reinsurance companies in percentages



Note: The figures for reinsurance companies in 2009 relate to the end of the third quarter.
Source: ISA

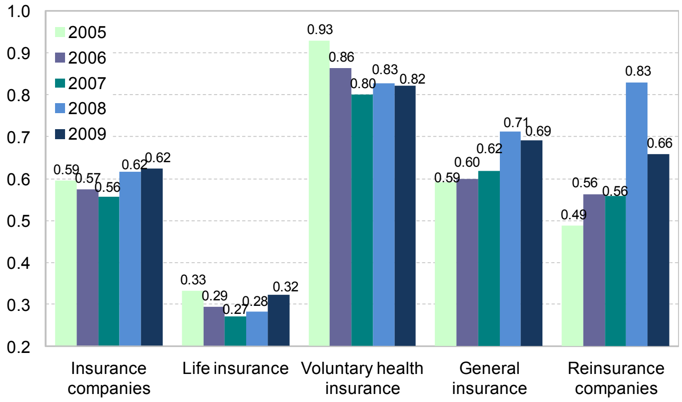
7.1.2 Stability of the insurance sector

Underwriting risk

A deterioration in the claims ratio for life insurance.

The claims ratio at insurers as measured by the ratio of gross claims paid to gross written premium remained at the same level last year, having increased sharply in 2008. This was the result of several natural disasters in the last two years. The claims ratio for life insurance deteriorated slightly last year, as a result of an increase of 8.8% in claims paid and a decline of 5.1% in written premium. Having risen in 2008, the insurers' level of retained risk in non-life insurance declined by 2.8 percentage points last year to 81%.

Figure 7.4: Claims ratio for major types of insurance



Source ISA

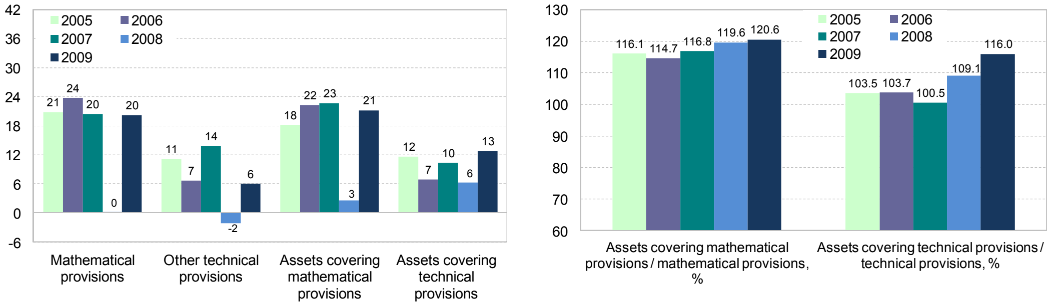
Investment risk

Assets covering technical provisions increased by 17.8% in 2009 to EUR 4,115 million, or 11.8% of GDP. In contrast to 2008, growth in life insurance investments last year was higher than growth in non-life insurance investments. The ratio of assets covering mathematical provisions to assets covering technical provisions thus rose to 1.6.

The coverage of insurance technical provisions by assets covering technical provisions increased to 118.8%.

The coverage of insurance technical provisions by assets covering technical provisions increased by 3.6 percentage points in 2009 to 118.8%. The largest factor in this was the improvement of 6.9 percentage points in the coverage of other insurance technical provisions by the assets covering technical provisions to 116%, while there was an improvement of 1 percentage point in the coverage of mathematical provisions by the assets covering mathematical provisions in life insurance and health insurance.

Figure 7.5: Growth in net insurance technical provisions and assets for life insurance and non-life insurance (left), and coverage of insurance technical provisions by assets covering technical provisions (right) in percentages



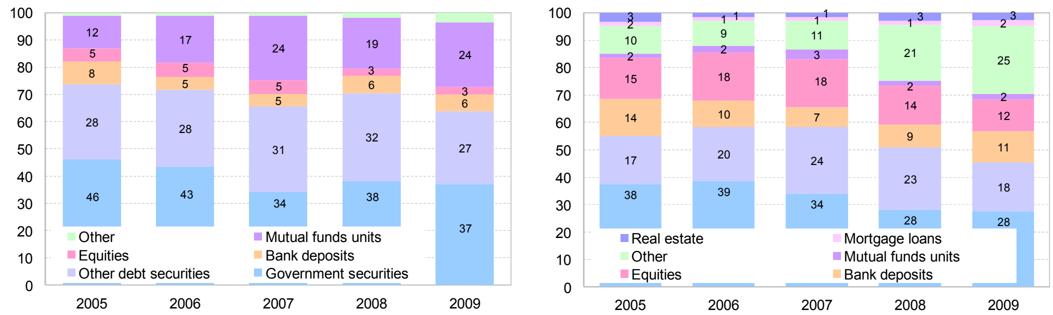
Sources: ISA, own calculations

Slovenian insurers remain more conservative than those of the euro area overall, although the gap in the level of safe investments narrowed by 10 percentage points during the crisis in 2008. The proportion accounted for by the safest forms of investment in deposits, government debt securities and other debt securities stood at 60.2% in Slovenia at the end of 2009, down just under 4 percentage points on a year earlier, partly as a result of investment value changes. The overall figure in the euro area was 54% at the end of 2008.[44]

Changes in value on the capital markets brought a change in investment structure.

The most notable change in the structure of life insurance investments was the rise of 4.8 percentage points in the proportion accounted for by mutual fund units to 23.6%. Given that demand for investment-based insurance was lower last year, this was the result of movements in securities prices. The proportion accounted for by non-government debt securities declined by 5.6 percentage points to 26.7%. Government securities still account for the largest proportion, at 37.1%.

Figure 7.6: Structure of insurers' assets covering mathematical provisions (left) and assets covering technical provisions other than mathematical provisions (right) in percentages



Source: ISA

The proportion of non-life insurance investments accounted for by bank deposits was up 2.8 percentage points, while that of debt securities was down 5.4 percentage points. The proportion accounted for by the safest forms of investment thus declined to 57%.

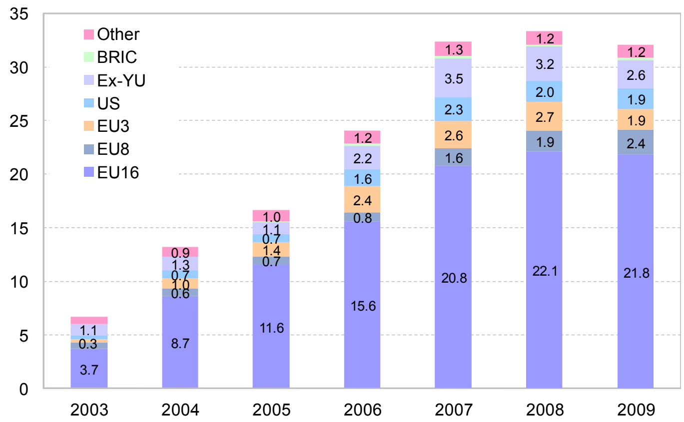
There was a slowdown in investments in foreign securities within the assets covering mathematical provisions. Growth in these investments was 15.1% in 2009, the proportion that they account for declining by 2.2 percentage points to 40.6%. Within assets covering technical provisions other than mathematical provisions, investments in foreign securities increased by just 1%. The proportion that they account for declined by 1.6 percentage points to 14.9%.

44 CEIOPS, Statistical annex 2008.

More than two-thirds of insurance investments in the rest of the world are in euro area countries, although ownership links mean that the proportion accounted for by former Yugoslav republics remains significant.

The entire insurance sector's investments in the rest of the world increased by 13.2% in 2009 to EUR 2,043 million. However, the proportion of total investments accounted for by investments in the rest of the world declined by 1.3 percentage points to 32.1%. There were net purchases of EUR 135.2 million last year, of which EUR 73 million comprised investments in shares, primarily in euro area countries and the former Yugoslav republics, partly as a result of capital increase at affiliated insurers. As a result, the proportion of investments in shares accounted for by the former Yugoslav republics is high at 29%. Insurers assess south-eastern Europe as a market with good prospects, where it would be possible to gain a higher market and generate profits, although the process is slow because of the low purchasing power and the need for greater awareness on the part of the public. Net purchases of debt securities in the amount of EUR 62 million were recorded primarily by issuers from the EU and Norway, while net sales were recorded by the former Yugoslav republics.

Figure 7.7: Proportion of life insurance investments accounted for by foreign investments in percentages



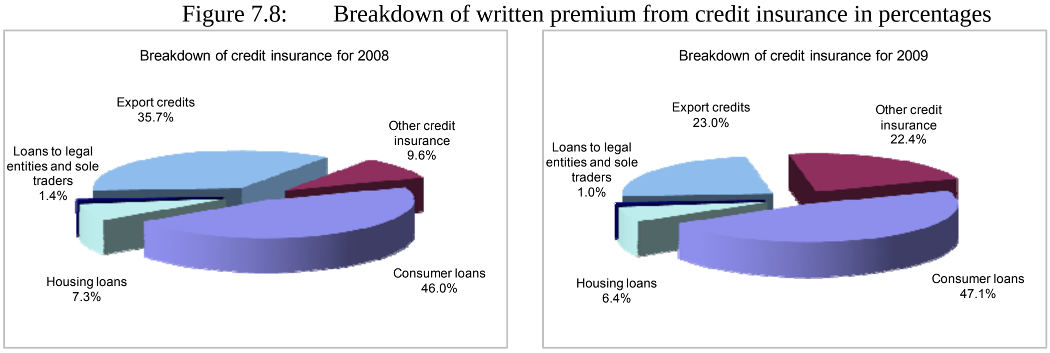
Source: Bank of Slovenia

7.1.3 Influence of insurers on the stability of the banking sector via credit insurance

Written premium for credit insurance declined as a result of the economic crisis.

The economic crisis reduced demand for credit insurance at insurers, which are indirectly dependent on the banks' lending activity. After a slowdown in growth in written premium in credit insurance between 2006 and 2008, the volume of transactions last year declined by 5.8%. The proportion of the insurers' total written premium accounted for by credit insurance declined to 2%, and the proportion of written non-life insurance premium to 2.7%. The ratio of the sum insured from credit insurance at Slovenian insurers to loans to non-banking sectors declined for the fourth consecutive year to 16.5%, equivalent to EUR 5,578 million. The ratio of the sum insured from credit insurance for housing and consumer loans and loans to sole traders to household loans declined slightly to 8.8%, equivalent to EUR 697 million. The sum insured for consumer loans increased by 10.1% last year. The largest decline was in the sum insured for export credits, at a large 41.6%, while the sum insured for housing loans declined by 20.2%.

Figure 7.8: Breakdown of written premium from credit insurance in percentages

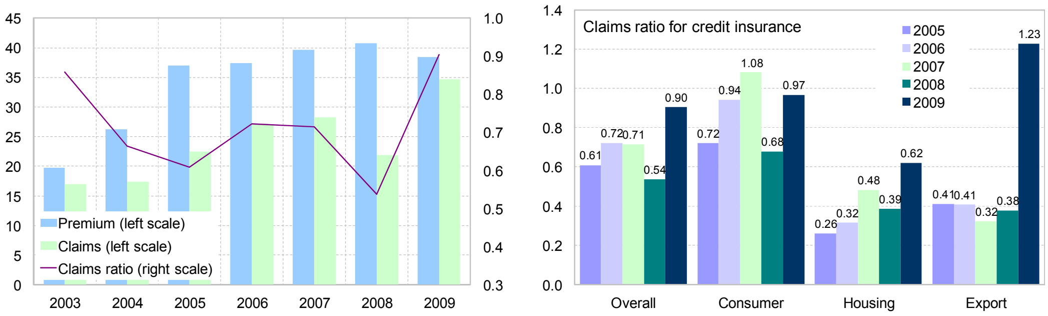


Source: ISA

A deterioration in the claims ratio for credit insurance.

The overall claims ratio for credit insurance deteriorated as expected in 2009 to 0.9. This was the result of the deterioration in corporate performance and the economic situation of households. There was a particularly pronounced deterioration in the claims ratio for export insurance to 1.23. Gross written premium for export insurance declined by 39.3%, while gross claims paid increased by 96.7%. Gross written premium for credit insurance for consumer loans declined by 3.6%, while gross claims paid increased by 37.5%. This was reflected in an increase in the claims ratio to 0.97. Although credit insurance premium accounts for a small proportion of the total, the deterioration in the claims ratios is having an adverse impact on performance, and these results will continue in light of the weakness of economic activity.

Figure 7.9: Written premium and claims paid in EUR million, and claims ratios for credit insurance



Source: ISA

7.2 Voluntary supplementary pension insurance

The number of voluntary supplementary pension insurance policyholders declined by 5.7%.

The number of policyholders covered by voluntary supplementary pension insurance declined by 5.7% in 2009. At the same time written premium declined by 3.6% to EUR 231 million; assets increased by 26.1% to EUR 1.5 billion, or 4.4% of GDP, as a result of favourable capital movements. Premium payments declined as a result of the deterioration in households' economic situation, which is a consequence of rising unemployment, lower net wages at certain companies and the introduction of reduced working hours.

Table 7.3: Voluntary supplementary pension insurance providers: number of policyholders, written premium and assets

	2004	2005	2006	2007	2008	2009
Number of policy holders	404,885	427,645	459,764	486,816	512,343	482,988
Breakdown, %						
mutual pension funds	50.7	49.3	48.0	47.4	46.6	51.1
insurers	9.5	9.3	9.2	23.3	24.1	16.8
pension companies	39.8	41.4	42.8	29.3	29.3	32.1
Written premium, EUR million	179	182	202	217	240	231
Breakdown, %						
mutual pension funds	51.6	46.3	44.6	43.7	42.6	45.9
insurers	8.3	8.3	7.9	20.2	23.7	21.4
pension companies	40.1	45.3	47.5	36.0	33.7	32.7
Assets, EUR million	398	592	783	956	1,212	1,528
Breakdown, %						
mutual pension funds	38.0	40.6	43.0	45.9	39.9	42.4
insurers	13.1	11.5	10.9	12.3	22.1	21.5
pension companies	48.9	47.8	46.1	41.8	38.0	36.1

Sources: ISA, SMA

The pressure on the fund of compulsory pension and disability insurance increased slightly as a result of the rise in unemployment, the ratio of policyholders at the Pension and Disability Insurance Institute to the number of pensioners declining to 1.6. Growth in the net average wage outpaced growth in the average pension by 0.5 percentage points. There was an increase of 0.3 years to 59.5 in the average age of pension claimants.

The bill for a new Pension and Disability Insurance Act envisages a gradual rise in the actual retirement age.

A bill for a new Pension and Disability Insurance Act was presented in March 2010 with the aim of modernising the pension system. The bill seeks to increase the proportion of active policyholders by gradually raising the actual retirement age for men to 65 and for women to 63, in the context of retirement with 40 or 38 years of service respectively. The aim is to establish the principle that the amount of benefits is based on the contributions paid, and the allowance for periods when social transfers are received, for example during studies or maternity leave, is abolished. The accounting period is also gradually extended to the 34 best years of insurance.

The average return on supplementary pension insurance improved.

The average annual return achieved by insurers and pension companies from voluntary supplementary pension insurance investments was 4.6% in 2009, while growth in the average unit value of mutual pension funds was 14%. The returns were better because of the improvement in the situation on the capital market compared with the previous year. Higher prices of debt securities also had a major impact. Greater motivation for saving in this form is being curbed by the legally prescribed minimum guaranteed return,[45] which stood at 1.69% annualised in December 2009. Because saving for the third age is a long-term enterprise, investments need to be more actively managed, risk management needs to be clearer, and various opportunities need to be exploited. Higher-risk investments are suitable in the early period of saving, but closer to retirement policyholders can opt for lower-risk investments.

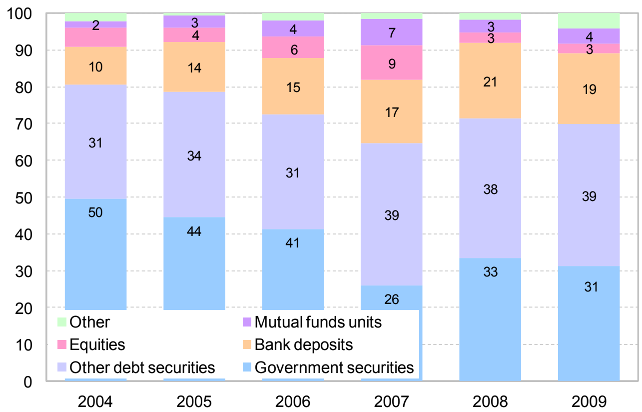
Table 7.4: Structure of pension funds' assets in Slovenia at the end of 2009 and in selected European countries at the end of 2008 in percentages

	Slovenia	Portugal	Austria	Germany	UK
Structure of investments, %					
currency and deposits	19.2	13.6	15.2	5.3	3.7
debt securities	69.9	52.2	49.0	38.3	27.1
shares	2.5	18.3	21.2	6.1	45.8
mutual funds units	4.2				
other	4.1	15.9	14.6	50.3	23.4

Note: OECD figures include investments in investment funds. Their investments are disclosed by type of security.
Sources: ISA, SMA, OECD Pension Markets in Focus, October 2009, Issue 6

Compared with certain European countries, the investment structure of Slovenian pension funds' assets is still relatively conservative, which has been reflected positively in the last two years. However, investment should also be adjusted to a period of high growth in the capital market, allowing for gains to be realised, while constantly upholding the fundamental principle of security.

Figure 7.10: Structure of voluntary supplementary pension insurance providers' investments in percentages



Sources: ISA, SMA

7.3 Investment funds

After a substantial withdrawal of money from funds in 2008, the situation stabilised in 2009.

The assets under management at the investment funds increased by 16.8% in 2009, an express reversal from 2008, when assets declined by 53.8%. Mass withdrawals and a significant fall in the value of investments were the main features of 2008. The situation

[45] The guaranteed annual return on pension saving is legally prescribed in the amount of at least 40% of the average annual interest rate on government securities with a maturity of more than 1 year.

normalised in 2009, and the funds again attracted small net inflows in the context of improved returns on investment. As a result of the investment fund conversion process the proportion of investment fund assets accounted for by mutual funds is continuing to increase. They accounted for 83.1% of the investment funds' total assets under management at the end of 2009, and 84.1% of the total at the end of March 2010.

Table 7.5: Overview of investment funds

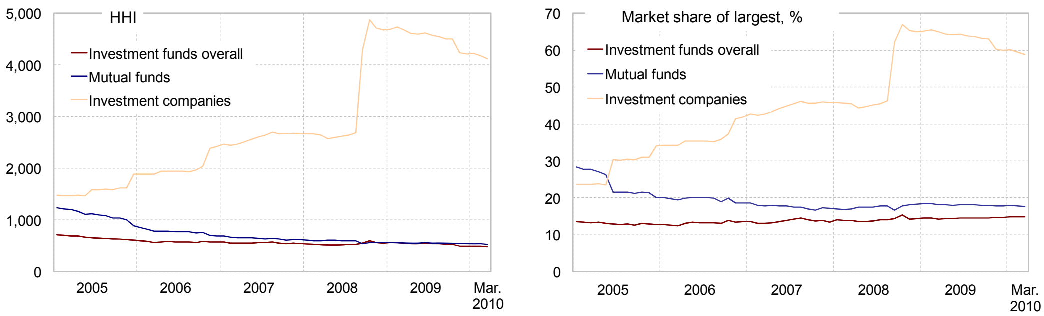
	2005	2006	2007	2008	2009	Mar. 2010
	Assets, EUR million					
Investment funds	2,220	2,845	4,138	1,912	2,234	2,341
Mutual funds	1,385	1,929	2,924	1,513	1,856	1,969
annual net inflows	138	163	470	-304	18	33
Investment companies	835	916	1,213	398	377	372
	Breakdown, %					
Mutual funds	62	68	71	79	83	84
Investment companies	38	32	29	21	17	16
	Growth, %					
Investment funds	6.4	28.1	45.4	-53.8	16.8	29.8
Mutual funds	57.9	39.3	51.6	-48.2	22.7	38.6
Investment companies	-30.9	9.7	32.4	-67.2	-5.3	-3.1
AUP	7.2	18.8	28.0	-42.8	24.0	39.0

Sources: SMA, LJSE, own calculations

The market concentration of investment funds remains low.

Given the crisis situation, there were no major changes in the ownership structure of the management companies. Their market shares also remained practically the same as at the end of 2008. The investment fund market was very dispersed: fewer than 5% of the funds had a market share of 5% or more, and only one of the 132 funds had a market share of more than 10% at the end of March 2010. Just under half of the funds are owned by banks. Foreign funds accounted for a lowly 9.5% of the market at the end of March 2010.

Figure 7.11: Market concentration of investment funds

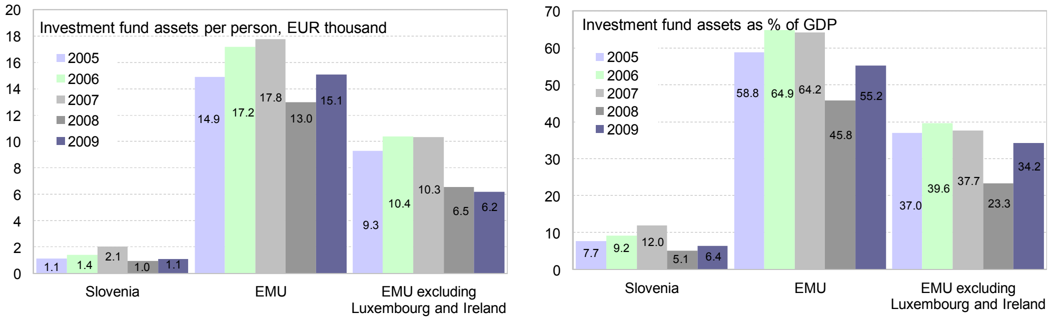


Note: HHI is the Herfindahl-Hirschman index. The market shares are determined on the basis of the amount of assets under management.
Source: SMA

Investment funds accounted for 5.9% of Slovenian households' financial assets at the end of 2009, up 0.8 percentage points on a year earlier. The figure was similar at the end of 2004. Before the outbreak of the financial turmoil the figure was almost twice as high (9.2% at the end of 2007). The figures are very low compared with the euro area overall. The total assets of the domestic investment funds per person stood at EUR 1,099 at the end of 2009, up 15.6% over one year. Assets per person in the euro area[46] declined by 5.1%. The ratio of assets to GDP increased by 24.4% to stand at 6.4% at the end of 2009. This was significantly lower than the euro area average of 34.2%. After a sharp decline in 2008, the assets of investment funds recorded a moderate increase last year in both Slovenia and the euro area overall.

[46] This figure does not include Luxembourg or Ireland, which have many registered funds marketed outside the euro area.

Figure 7.12: Comparison between Slovenia and the euro area in investment fund assets per capita in EUR thousand (left) and assets as a percentage of GDP (right)

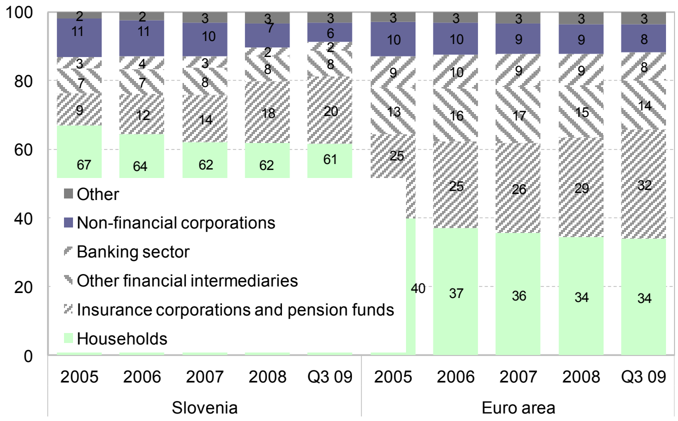


Sources: ECB, SMA, Eurostat, SORS

There is potential to increase investment in funds in the financial sector.

The ownership structure of investment fund units and shares revealed considerable potential for an increase in assets, particularly those of corporate investors. Compared with the euro area, the proportion of ownership accounted for by households at the end of September 2009 was above average, at 61.5%. The figure for households in the euro area overall was much lower at 34.0%. The financial sector in particular is a major investor in the euro area, accounting for more than 50% of ownership, while in Slovenia its proportion is less than 30%.

Figure 7.13: Breakdown of ownership of investment fund units/shares in percentages



Note: The units/shares of all investment funds (investment companies and mutual funds), both domestic and foreign, are taken into account.
Sources: Bank of Slovenia, ECB

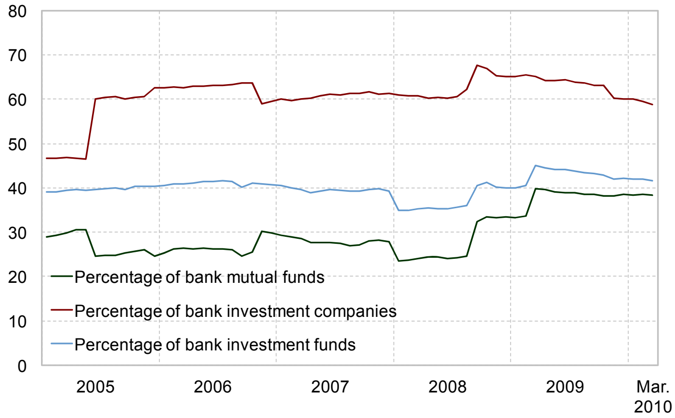
Interaction of investment funds and the banking sector

Management companies (MCs) under majority bank ownership accounted for 42.2% of the domestic mutual funds' total assets under management at the end of 2009. Because of the process of the conversion of investment companies into mutual funds, this figure is gradually approaching the proportion held by bank-owned mutual funds, which stood at 38.6% at the end of 2009.

Links between bank-owned management companies and non-bank management companies were not an issue in 2009.

Last year there was no incentive for the banks to link with other investment fund managers, as bank deposits were more attractive than investment funds for reasons of security. In addition, the banks are more cautious with regard to capital links during times of crisis. The banks nevertheless endeavoured to obtain alternative sources of funding by offering hybrid forms of bank deposit, thereby also attracting clients with greater appetite for risk.

Figure 7.14: Percentage of assets of investment funds, investment companies and mutual funds managed by management companies under majority bank ownership



Note: Deviation in March 2009 caused by change in reporting.
Source: SMA

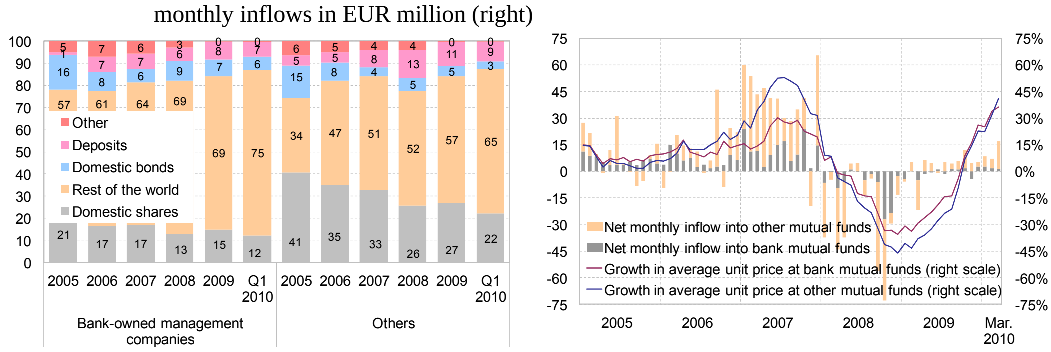
The volume of trading in mutual fund coupons amounted to EUR 132.5 million in 2009, generating a commission of EUR 2.0 million. The volume of trading was thus down almost a half, while commission was down 16.9%.

The mutual funds operated by management companies under majority bank ownership had a higher proportion of investments in the rest of the world. While only 14.9% of the total assets under management of bank-owned management companies was held in domestic shares, the figure for non-bank management companies was 26.7%. Foreign securities accounted for 69.3% of the assets under management at the bank-owned management companies, compared with 57.3% at the non-bank management companies. The reason for this gap is that the banks have a better investment policy with greater diversification and a larger trading portfolio.

The bank-owned management companies declared higher AUPs than the non-bank management companies.

The better-diversified portfolio of the bank-owned management companies led to a smaller decline in the average unit price at the bank-owned management companies in the second half of 2008 and the first half of 2009. By March 2010 the average unit prices at the bank-owned management companies were higher than during the most successful period of expansion in 2007, while those of the non-bank management companies were still below their record highs. Growth in the average unit price of the non-bank management companies nevertheless again overtook that of the bank-owned management companies in March, and was 4.9 percentage points ahead at the end of the month.

Figure 7.15: Comparison of mutual funds operated by management companies under majority bank ownership and others: investment structure in percentages (left), and annual growth in average unit prices in percentages and net monthly inflows in EUR million (right)



Sources: SMA, own calculations

Having recorded extremely high net outflows in 2008, the mutual funds recorded a low net inflow in 2009. The ratio of inflows and outflows at bank-owned management companies to total inflows did not reach the level that would be ascribed to them on the basis of the proportion of total investment fund assets that they account for. This is primarily a result of the specialised approach of the non-bank management companies, which are generating a larger response from investors.

The direct debt of the management companies at the domestic banks amounted to EUR 110 million at the end of 2009, down 14.5% on the end of 2008. The banks' total exposure to the management companies amounted to EUR 278.3 million at the end of 2009, down 11.5% on the end of 2008. After mass outflows in 2008, the management companies do not need such a quantity of liquid assets for their operations, and their indebtedness at banks is therefore declining.

7.3.2 Mutual funds

As a result of the investment company conversion process the proportion of mutual found in the structure of investment founds continued to increase. The mutual funds accounted for 84.1% of the total assets of the investment funds at the end of March 2010.

Table 7.6: Changes in the mutual funds' assets as a result of net inflows and other factors in EUR million

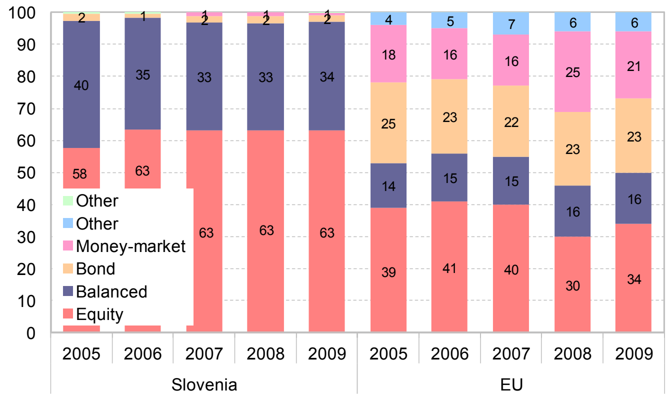
	Bond	Balanced	Equity	Money-market	Total
			2007		
Net inflows	-6	75	398	3	470
Capital gains	3	176	346	1	526
Assets, year end	40	1,019	1,855	11	2,924
			2008		
Net inflows	-5	-105	-200	6	-304
Capital gains	-3	-407	-698	0	-1,107
Assets, year end	32	507	957	18	1,513
			2009		
Net inflows	5	-20	36	-4	18
Capital gains	2	142	181	0	325
Assets, year end	39	628	1,173	14	1,856

Sources: SMA, own calculations

In Slovenia the majority of assets are shared between equity and balanced funds, which did not change during the crisis.

At the end of 2009 equity funds (63.2% of the total) and balanced funds (33.8%) were prevalent, while other types of fund accounted for a negligible proportion. In the EU the overall breakdown of funds is more balanced: no type of fund is particularly prominent. While Slovenian investors responded to the crisis primarily by reducing inflows and increasing outflows from funds, they did not alter their inclinations in investing in particular types of fund. The proportions accounted for by the various forms of fund (equity, bond, balanced, money-market, other) in Slovenia remained the same throughout the crisis period. The response was different in the EU overall, investors also responding to the changing situation in the economy in their choice of funds. There was a sharp increase in the proportion accounted for by money-market funds in 2008, while that of higher-risk equity funds declined sharply. In 2009 the proportions slowly returned to their pre-crisis levels.

Figure 7.16: Breakdown of funds by type, in terms of assets, in Slovenia and the EU overall in percentages



Sources: SMA, EFAMA

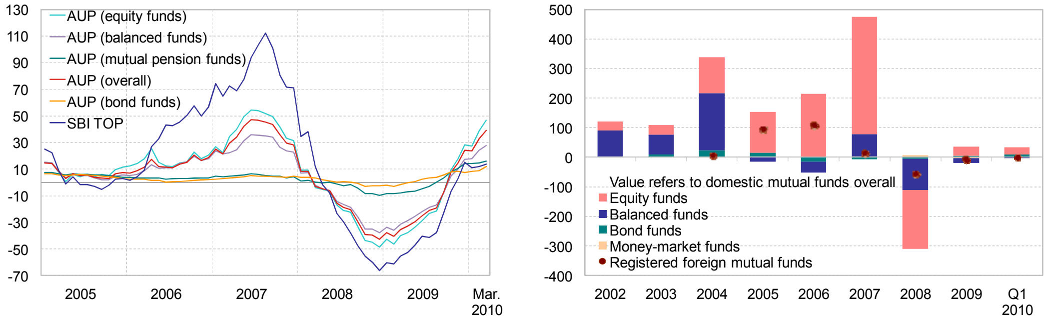
Net inflows of EUR 18.3 million in 2009 helped the mutual funds increase their assets by 22.7% to EUR 1,856.3 million. The majority of the increase can be ascribed to the change in the average unit price, which rose by 24.0%. A year of recovery followed the sharp decline in 2008. Given the movements in global stock markets, the largest gains last year were made by equity funds, and the smallest by bond funds.

Capital gains were the main engine of growth in the mutual funds' assets in 2009.

Despite the net inflows, the majority of the increase in the mutual funds' assets can be explained by capital gains, primarily as a result of rises in share prices.

Fund managers have adjusted their investment policies, and were no longer so consistent in tracking the make-up of the SBI TOP. The correlation coefficient for the daily percentage changes in the SBI TOP and the average unit price, which stood at 0.68 at the end of 2008, was just 0.35 at the end of 2009. This was partly the result of the higher correlation between stock market indices and the average unit price during the crisis than during the recovery.

Figure 7.17: Annual change in the average unit price of mutual funds and the SBI TOP in percentages (left) and amount of annual net inflows into mutual funds in EUR million (right)



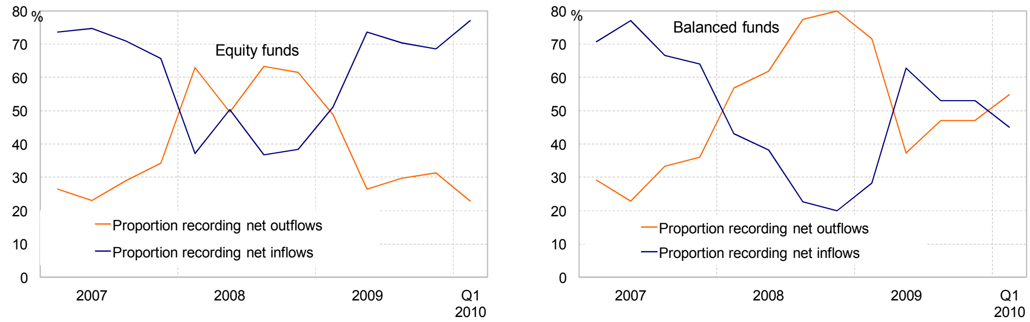
Sources: SMA, LJSE, Bank of Slovenia

Renewed net inflows into mutual funds in the second half of 2009.

Investors responded to the movement in the average unit price by withdrawing money from funds in 2008, and by reinvesting in 2009. While the mutual funds' management companies recorded net outflows of EUR 303.8 million in 2008, in 2009 they recorded net inflows of EUR 18.3 million, the majority in the second half of the year, when the trend of growth in the average unit price was more evident and attractive to investors.

Major differences had arisen between the mutual funds in 2007 as a result of their regional and sectoral focus. The varying returns led to different responses by investors in making payments into the funds. The majority of funds have recorded renewed net inflows since the second quarter of 2009. Net inflows were recorded by 77.1% of equity funds in the first quarter of 2010, compared with 45.1% of balanced funds.

Figure 7.18: Proportion of mutual funds recording net inflows and proportion of mutual funds recording net outflows, for equity funds (left) and balanced funds (right)



Source: SMA

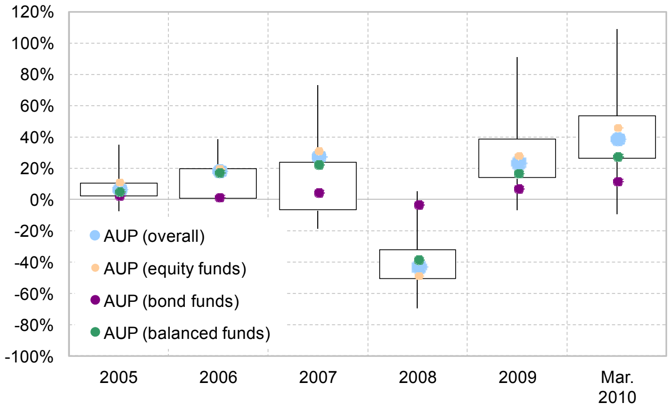
The differences in annual returns widened, but the majority were positive.

The standard deviation in annual returns on all mutual funds has increased each year, rising to 19.94 by the end of 2009. While almost all of the funds recorded a loss in 2008, almost all recorded a positive annual change in the unit price in 2009. With a rise of 28.4% in the average unit price, the best-performing funds were equity funds, particularly those with an investment policy focused on the BRIC[47] countries, eastern Europe and Latin America, while the money-market funds and bond funds were the worst-performing, with annual rises of 2.2% and 7.4% respectively. The mutual funds thus succeeded in

[47] Brazil, Russia, India and China.

increasing their assets as a result of turnaround on the global markets. Capital gains accounted for 98.5% of the increase in assets in 2009.

Figure 7.19: Classification of mutual funds in terms of annual return at year end in percentages



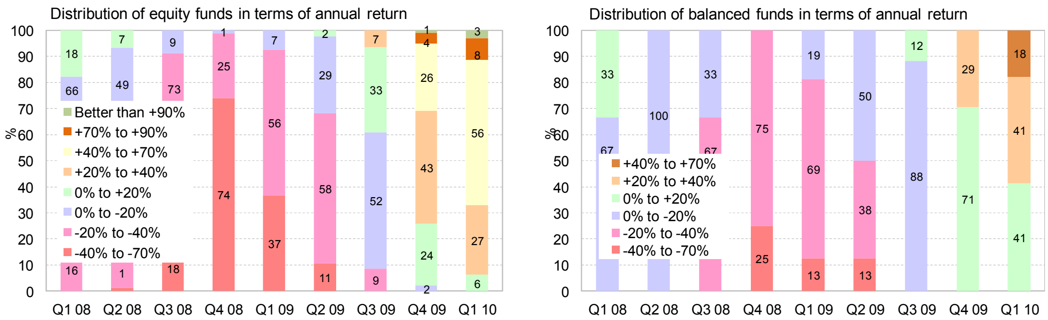
Note: As the funds have been ranked according to annual return at the end of the year, only those funds in existence for at least one year are included. The figure shows the variation in annual returns between funds, and the relative standing of particular types of fund compared with mutual funds overall. The rectangles represent the 50% of mutual funds whose annual returns are higher than the bottom quartile of the funds, and lower than the top quartile.

Sources: SMA, own calculations

The year-on-year change in AUPs changed from extremely negative to positive at the majority of equity and balanced funds.

The largest changes were in the returns on equity funds and balanced funds, as they had the highest-risk investment policy. There was a gradual decline in the proportion of loss-making equity funds in 2009, the figure standing at 2.1% at the end of the year. The balanced funds all recorded a positive return. Only two funds recorded an annual loss. Both had an investment policy focusing on the Balkans. Only one fund was disclosing an annual loss in March 2010. The proportion of funds recoding an annual return of more than 20% is increasing.

Figure 7.20: Relative distribution of domestic equity funds (left) and domestic balanced funds (right) in terms of annual change in average unit price



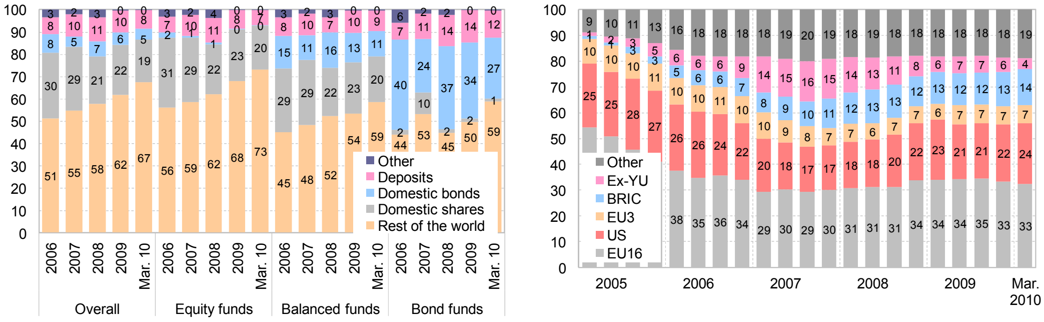
Source: SMA

In addition to rises in stock markets, the mutual funds' positive return was the result of a more appropriate investment policy. The proportion of the mutual funds' portfolio accounted for by domestic shares declined in 2009. Domestic shares accounted for just 19.2% of the mutual funds' investments in March 2010, while foreign shares accounted for 67.5%. This trend was not shaped by the financial turmoil, as it had been seen even before the crisis, and is a reflection of the anticipated evolution of the mutual funds, which are gradually gaining in knowledge and experience to upgrade their existing investment policies.

The portfolio is continuing to evolve in the quest for greater returns.

By contrast, the regional focus was rather dependent on global developments. The largest response to the restructuring of the portfolio was between 2006 and 2008, when the mutual funds entered the markets of the former Yugoslav republics en masse, then saw the value of the portfolio decline significantly during the crisis as a result of the large fall in prices in the region. The proportion of the mutual funds' assets accounted for by shares from the former Yugoslav republics gradually declined in 2009 to stand at just 5.7% at the end of the year (it had stood at more than 15% in 2007). The problems on these markets originate primarily in low liquidity, economic and political instability and currency risk. In contrast, the proportions accounted for by shares from the US, the euro area (these investments are primarily low-risk) and the BRIC countries (higher-risk, but better returns) all increased.

Figure 7.21: Breakdown of mutual fund investments (left) and regional breakdown of investments in foreign shares by the entire other financial intermediaries sector (right) in percentages



Note: BRIC: Brazil, Russia, India, China
EU3: UK, Denmark, Sweden
EU16: euro area
Ex-YU: former Yugoslav republics

Source: SMA

The proportion of liquid assets at the mutual funds declined again in the second half of 2009.

The largest number of withdrawal requests was in 2008. Operators were nevertheless increasing their liquid assets until June 2009, when the proportion of liquid assets stood at 14.0%. The increased redemption of fund units, which peaked in 2008 and gave operators an increased need to secure liquid assets, was also seen in the first half of 2009, for security reasons and for reason of investment uncertainty. The proportion of total assets accounted for by liquid assets had fallen to 11.4% by the end of the year, down 1.4 percentage points on the previous year. The decline in the proportion accounted for by liquid assets was the result of lower demand from investors for withdrawals from the funds.

Table 7.7: Liquid assets as a proportion of mutual funds' total assets at the end of the month

(%)	Bond	Balanced	Equity	Money-market	Total
Mar. 08	30.2	11.7	9.2	99.5	11.1
Jun. 08	36.8	10.7	8.9	99.2	10.5
Sep. 08	39.9	10.4	9.7	99.7	11.2
Dec. 08	37.1	11.4	11.1	99.5	12.8
Mar. 09	38.5	11.3	8.3	99.6	11.4
Jun. 09	39.6	18.3	9.0	99.8	14.0
Sep. 09	37.1	16.6	8.1	99.4	12.4
Dec. 09	36.2	15.3	7.4	99.3	11.4
Mar. 10	30.5	14.0	7.0	99.4	10.6

Notes: Liquid assets include cash, deposits, money-market instruments and government bonds.
Sources: SMA, own calculations

In addition to better returns on the funds, another factor in the decline in outflows was the Rules on the traceability of switching between sub-funds of the same umbrella fund, which since 25 October 2008 have allowed investment coupons in a sub-fund to be swapped tax-free for investment coupons of another fund of the same umbrella fund.

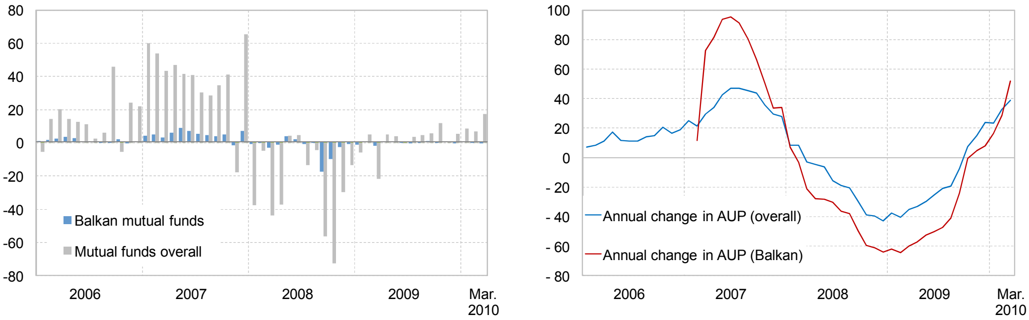
Mutual funds with an investment policy focusing on the Balkans

Outflows from the Balkan funds were lower than the decline in assets.

Funds with an investment strategy focusing primarily on the markets of former Yugoslav republics accounted for 5.7% of all the mutual funds' assets under management at the end of 2009. This figure has been gradually declining since its highs of 2007, when it exceeded 15%. This decline in the proportion can partly be explained by the outflows from the funds, but mainly by the sharp decline in asset values.

The period of above-average returns in 2007 was followed by a period of above-average losses from the second half of 2008 to the first half of 2009. Only at the end of 2009 and the beginning of 2010 did the mutual funds with an investment policy focused on the Balkans disclose positive annual returns. Of the seven Balkan mutual funds, two ended 2009 with a negative annual return.

Figure 7.22: Comparison of funds whose investment policy is focused on the Balkans with all domestic mutual funds in terms of net flows in EUR million (left) and annual changes in average unit price (right) in percentages

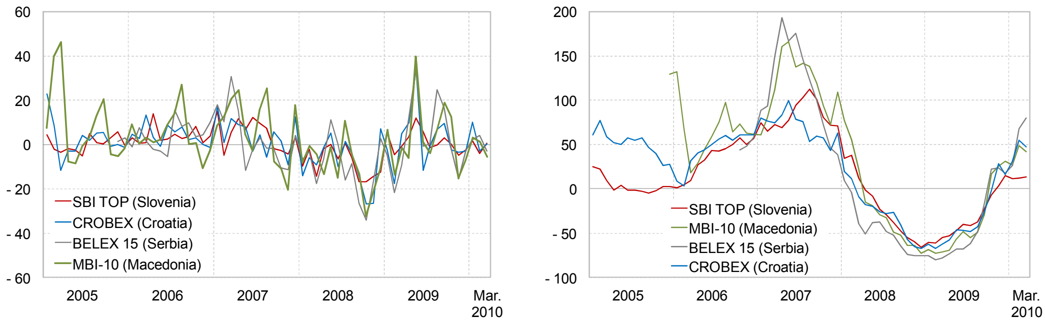


Sources: SMA, own calculations

Indices in the region have risen since March 2009.

Similar movements can be seen on the region's stock markets. Exceptional growth in 2007 was followed by a sharp fall in 2008 and early 2009. At the end of February 2009, the year-on-year change in Croatia's CROBEX was -67.3%, while Macedonia's MBI-20 was down 72.6% and Serbia's BELEX 15 was down fully 79.4%. The indices have risen since March 2009, and ended the year having recorded a positive change. The CROBEX was up 16.4% in 2009, the MBI-20 was up 31.3% and the BELEX 15 was up 17.4%. The indices had risen further by the end of March 2010.

Figure 7.23: Monthly (left) and annual (right) changes in selected stock market indices in the former Yugoslav republics



Sources: LJSE, Bloomberg, websites of stock exchanges of the former Yugoslavia

7.3.3 Investment companies

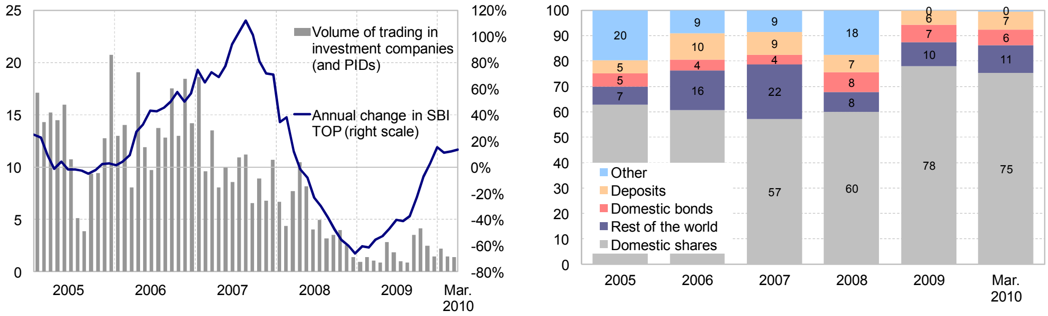
The remaining four investment companies must convert to mutual fund status by 2011.

The investment companies accounted for 15.9% of investment fund assets at the end of March 2010. The process of converting investment companies into mutual funds means that their importance is diminishing; investment company shares accounted for just 5.4% of the total volume of trading on the Ljubljana Stock Exchange in 2009. The figure was 10.1% in 2008, and 14.0% in 2007. The four remaining investment companies must convert to mutual fund status by 2011. The market capitalisation of the investment companies increased by 12.2% in 2009, no company having successfully converted into a mutual fund during the year.

The investment companies with less exposure to domestic shares disclosed higher returns in 2009.

Compared with the investment structure of the mutual funds, the investment companies' investment policies are strongly focused on domestic shares, which accounted for 78.0% of their assets at the end of 2009, compared with 22.4% at the mutual funds overall, and 23.2% at the equity funds. The two companies that outperformed the SBI TOP in 2009 were the least-exposed to shares in domestic issuers. Nevertheless domestic shares accounted for 58.0% and 40.0% of their assets, well above the average for the mutual funds. At the other two investment companies, whose share prices ended 2009 at almost the same level as at the end of 2008, the proportions of the investment portfolio accounted for by domestic shares stood at 94.1% and 77.4%.

Figure 7.24: Monthly volume of trading in investment companies in EUR million, and annual growth in the SBI TOP in percentages (left), and breakdown of investment companies' investments in percentages (right)



Note: The figures before 2009 differ because of looser reporting methodology. Investments under the item "Other transferable securities and money-market instruments" have been more precisely defined, and divided among other categories (domestic shares, bonds, deposits, rest of the world, other).

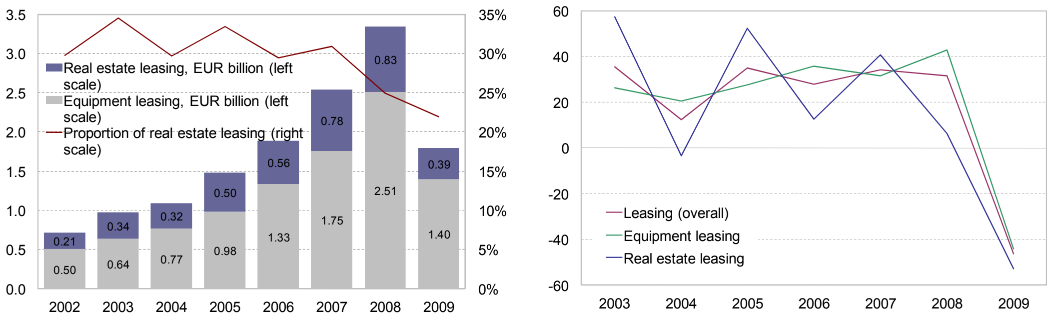
Sources: SMA, LJSE

7.4 Leasing companies

The volume of leasing business declined by 46.4% in 2009.

Like the banks, Slovenian leasing companies faced low demand in 2009. Their volume of leasing business declined by 46.4%, the stock of principal declining by 13.4% during 2009 to stand at EUR 4.4 billion at the end of the year. Of the members of the BAS's leasing committee, who had a market share of 88% in terms of total assets at the end of 2008, the market share of the largest leasing company in terms of volume of business declined by 4.4 percentage points to 33.1%.

Figure 7.25: Approved leasing business in EUR billion[48] and the proportion accounted for by real estate leasing (left), and annual growth in leasing business in percentages (right)



Sources: SLA, BAS

Real estate leasing business declined by 52.8%, and equipment leasing business by 44.2%.

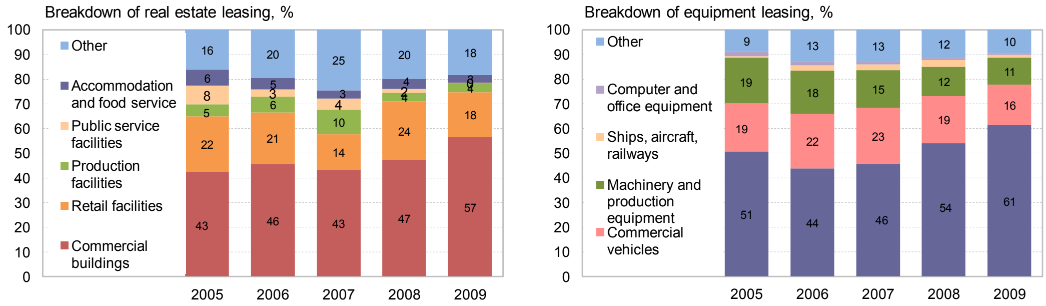
The proportion of leasing business accounted for by real estate leasing declined to 22%. Real estate leasing business declined by more than a half to EUR 394 million, simultaneous with the decline in construction activity and the decline in the number of transactions on the real estate market. Last year the proportion of the secondary real estate market[49] accounted for by leasing business fell by 7.6 percentage points to 26.7%. Despite the decline in economic activity leasing remains an important source of new corporate investment, particularly in commercial buildings.

The volume of equipment leasing declined by 44.2%, and accounted for 78% of total leasing business. In the breakdown of leasing services by types of equipment, cars and commercial vehicles remain at the forefront, with machinery and production equipment. Of these, the largest advance made over the last two years was by cars, whose proportion of the total increased by 15 percentage points to 61%, while the proportion accounted for by commercial vehicles declined to 16%, and that accounted for by machinery and equipment declined to 11%.

[48] Figures for the purchase and financed value of leasing business are available for the last two years. The purchase value is used in the analysis for the purpose of comparison over time.

[49] Includes legal entities and private individuals.

Figure 7.26: Breakdown of real estate leasing (left) and equipment leasing (right) in percentages



Sources: SLA, BAS

The requirements for the lessee's own participation increased.

In the purchase of equipment the average lessee's own participation declined by 1.5 percentage points to 16.2%, while own participation in real estate leasing declined by 13.1 percentage points to 22.9%. The most pronounced rise was in the requirement for the lessee's own participation in the leasing of retail facilities, which went from an average of 7.7% to 46%. Weakened circumstances led to lower credit ratings for lessees, who were irregular in settling their liabilities and had less possibility of refinancing. Leasing companies therefore raised their margins and required additional forms of collateral.

The average maturity of leasing agreements is shortening.

The average maturity in equipment leasing shortened significantly in 2009. The proportion of the total accounted for by agreements with a maturity of up to 2 years was up 9 percentage points at 45%. In real estate leasing there was an increase in business with a maturity of 5 to 10 years (31%), at the expense of a decline in business with a maturity of more than 10 years (46%).

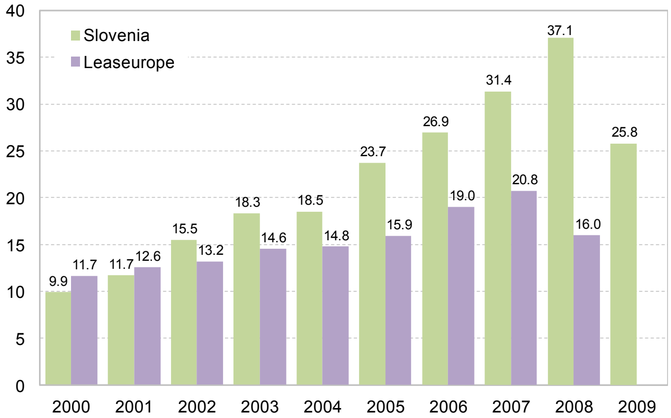
The European leasing market saw a decline of 1.6% in the volume of business in 2008, and a decline of 28% in 2009 according to provisional figures.

According to Leaseurope figures, the volume of European leasing business in 2008 declined by 1.6%, primarily as a result of a large decline of 21.6% in real estate financing, while equipment leasing recorded growth of 1.6%. As a result the proportion accounted for by equipment leasing rose to 89.1%, juts over 14 percentage points more than in Slovenia. The largest declines in the volume of business were recorded by the Baltic states, Spain, Italy and Greece.[50] Although the total volume declined, individual markets still recorded growth. The highest growth was in Bulgaria and Romania, followed by Denmark, Slovakia and Belgium.[51]

According to provisional figures for 2009, the volume of European leasing business declined by 28.4%, to a level below that more than six years ago. Real estate leasing declined by 23.4%, while equipment leasing was down a high 35.3%. The countries of central and eastern Europe recorded a decline of 44.2% in the volume of leasing business, while it was down 43.7% in the Mediterranean countries.[52] Only in 2011 is an improvement expected.

[50] Leaseurope figures for 2008: Latvia down 42.1%, Spain down 30.5%, Estonia down 22.4%, Italy down 18.5% and Greece down 10.3%.
[51] Bulgaria 58%, Romania 22.8%, Denmark 15.1%, Slovakia 14.6%, Belgium 10.8%.
[52] Central and eastern Europe: Bulgaria, Czech Republic, Estonia, Poland, Slovakia, Slovenia. Mediterranean: Spain, Portugal, Greece.

Figure 7.27: Ratio of leasing business to gross fixed capital formation in percentages



Note: The Leaseurope figures include all EU Member States with the exception of Luxembourg, Ireland, Lithuania, Cyprus and Malta, plus Norway, Russia, Switzerland and Serbia (the figures for 2008 are not yet available for the last two). Gross investment includes gross fixed capital formation other than investments in residential buildings for reason of comparability with the Leaseurope figures.
Sources: SLA, BAS, SORS, Leaseurope

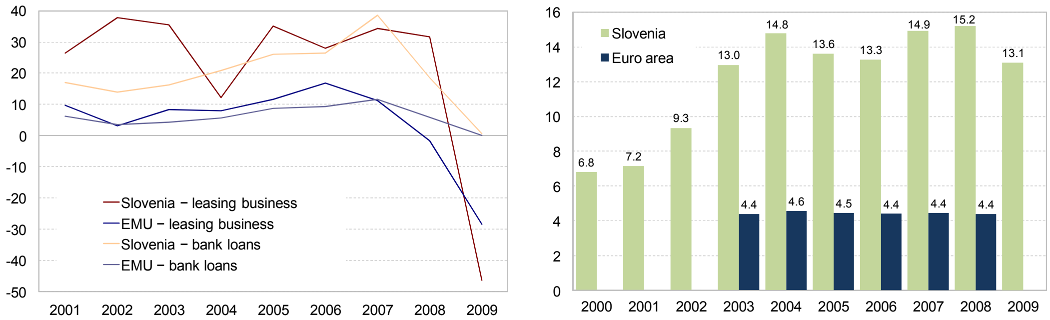
The ratio of leasing business to gross fixed capital formation declined by 11.3 percentage points to 25.8%.

The adverse impact of the crisis in the real sector was sharply reflected in leasing performance in 2009, as evidenced in the decline in the ratio of leasing business to gross fixed capital formation (other than investment in residential buildings). After growing for several years, the financing of investment other than residential buildings declined by 11.3 percentage points to reach 25.8%, a level seen before 2006.

The adverse economic situation forced leasing companies to cut costs in their business processes. Given the lack of liquidity, solvency was ensured by the optimal acquisition of long-term funding and the prudent placement of assets.

There was a deterioration in the quality of the leasing companies' portfolio, as a result of the problems experienced in their dealings with clients. Given the realisation of credit risk, the timely recovery of claims was a key in performance. The high indebtedness of clients, the uncertain economic situation and the rise in funding costs raised the costs of undertaking leasing business. In the case of consumer lending, according to the Consumer Credit Act the effective interest rate may be no more than 200% of the most recently reported average effective interest rate of banks and savings banks.

Figure 7.28: Annual growth in newly approved leasing business concluded and stock of bank loans to non-banking sectors (left) and ratio of leasing loans to bank loans (right) in percentages



Note: The figures for the volume of leasing business in the euro area do not include Luxembourg, Ireland, Cyprus or Malta. The figure for growth in European leasing business for 2009 is provisional.
Sources: SLA, BAS, Bank of Slovenia, Leaseurope, ECB

Leasing is more important to the economy in Slovenia than in the euro area overall according to the indicator of the ratio of leasing loans to bank loans. The future activities of the leasing companies will also be determined by the performance of the banks, with which most have ownership links. According to end-of-year accounts figures for 2008, banks account for 76% of leasing companies' total liabilities.

The leasing companies owned by banks had fewer problems in obtaining funding. However, should the European Commission's proposals to improve the robustness of the financial system be approved, their position will also worsen. The main impact would come from the proposed calculation of the liquidity ratio for legal entities and the amendments to the IFRS, which would also have an impact on the amount of financial leverage.

Performance of Slovenian leasing companies

The leasing companies' profit halved in 2008.

Even in 2008, when the leasing sector was still growing in terms of the volume of business, profits almost halved because of fierce competition, higher funding costs, repossessions and higher impairment costs. ROE consequently declined by just over 10 percentage points to 9.3%. Growth in total assets slowed to 15.3%.

Growth in the domestic banks' loans to leasing companies continued in 2008. At EUR 2.8 billion they accounted for around 46% of the leasing companies' total liabilities.[53] Given that financial liabilities rose significantly more than equity in 2008, the debt-to-equity ratio deteriorated. The proportion of total bank loans to non-banking sectors accounted for by loans to the leasing companies stood at just under 4%, and does not represent a systemic threat to the banking sector.

Table 7.8: Performance of leasing companies and sources of funding

						Growth, %				
	2004	2005	2006	2007	2008	2004	2005	2006	2007	2008
Total assets, EUR million	2,669	3,162	4,052	5,328	6,144	51.1	18.4	28.1	31.5	15.3
Capital, EUR million	177	212	287	318	324	46.2	19.5	35.5	10.7	1.9
Total profit/loss, EUR million	45	48	55	61	30	39.5	8.0	13.2	11.1	-50.7
ROA, %	2.0	1.7	1.5	1.3	0.5					
ROE, %	30.0	24.8	21.9	20.1	9.3					
Financial and operating liabilities, EUR million	2,468	2,934	3,738	4,976	5,777	32.4	18.9	27.4	33.1	16.1
liabilities to banks and companies in group,%	81	83	94	94	96	49.1	20.7	44.5	34.3	18.0
liabilities to the rest of the world, %	79	78	74	72	73	52.8	17.6	21.2	28.5	17.9
Liabilities to rest of the world / total liabilities, %	-72.9	-72.4	-68.5	-66.9	-68.4					

Note: The figures from financial statements include all companies included under K64.91 (Financial leasing) in the SKD 2008 classification (J65.21 in the SKD 2002). Since 2006 the final accounts of companies have been compiled in accordance with the new Slovenian Accounting Standards (SAS 2006).

Source: AJPES

[53] The ratio stood at 15% in 2005, 39% in 2006 and 43% in 2007.

8 FINANCIAL INFRASTRUCTURE

Payment systems, the clearing system and the settlement of financial instruments ensure the transfer of money and securities, while their secure and efficient functioning ensure that financial claims and liabilities are settled reliably, promptly and cost-effectively. They thus contribute to the general stability and efficiency of the functioning of financial systems, but their importance means that they can cause systemic shocks or become a channel of contagion.

8.1 Payment systems

Given the size of its total transaction value, the TARGET2-Slovenia system is the most important payment system for financial stability in Slovenia. As the national component of the centralised pan-European system for individual (gross) settlement of euro payments in real time (TARGET2), it is operated by the Bank of Slovenia. Because TARGET2 is technologically set up as a single shared platform of the Eurosystem, oversight of the system to ensure that it is functioning securely and effectively is centralised under the aegis of the ECB. The oversight in 2009 did not identify any major deviations from normal functioning. In response to the threat of a flu pandemic, the operators of the single shared platform adopted a crisis management plan for such an eventuality.

A changeover from the Giro Clearing system to the SEPA ICT system for retail payments.

Given the large number of transactions processed daily, the SEPA internal credit transfers (SEPA ICT) payment system operated by Bankart d.o.o. is also important to financial stability. It is designed to process retail credit transfers (up to EUR 50,000) in line with the rules of the single euro payments area (SEPA), according to the principles of calculating an individual member's net claims or net liabilities in the system vis-à-vis other members. All members other than the Bank of Slovenia are obliged to participate in the Settlement Guarantee Scheme (SGS), which was set up to manage financial risk (the inability to settle liabilities). The SEPA ICT system, which began operating on 4 March 2009, replaced the Bank of Slovenia' Giro Clearing system, the gradual migration of payments to the new payment system taking place between the establishment of the SEPA ICT system and the end of July 2009.

The value of transactions in the TARGET2-Slovenija retail payment system increased again in 2009.

The value and number of transactions in the TARGET2-Slovenija system increased in 2009, but declined in the SEPA ICT system (including Giro Clearing payments). The total value of transactions in the TARGET2-Slovenia and SEPA ICT systems were respectively 14.5 and 1.3 times Slovenia's GDP in 2009.

Table 8.1: Value and number of transactions in the RTGS/TARGET/TARGET2[54] and Giro Clearing / SEPA ICT systems

	Year					Year-on-year growth, %				
	2005	2006	2007	2008	2009	2005	2006	2007	2008	2009
RTGS / TARGET / TARGET2[1]										
Value, EUR billion	261.6	317.6	364.7	410.4	507.6	28.0	21.4	14.8	12.5	23.7
Number of transactions, million	1.40	1.57	0.73	0.66	0.67	2.4	11.6	-53.5	-9.6	1.2
Giro Clearing / SEPA ICT										
Value, EUR billion	21.0	22.9	45.7	49.1	44.9	3.8	9.3	99.3	7.5	-8.6
Number of transactions, million	49.42	52.11	53.62	55.91	55.13	1.7	5.4	2.9	4.3	-1.4

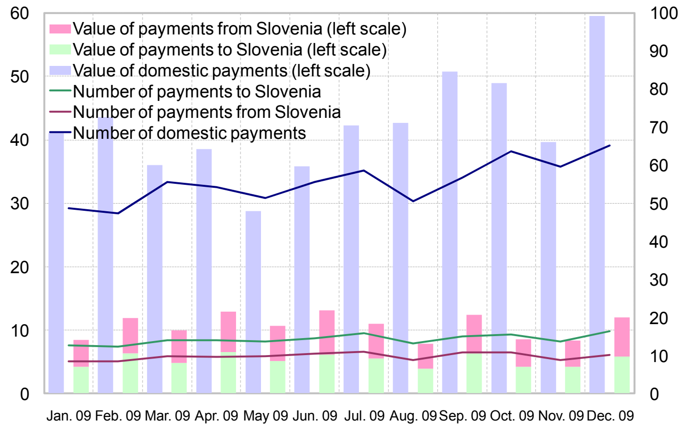
Note: [1] Transactions between members of the TARGET2-Slovenija system (domestic payments).
Source: Bank of Slovenia

The TARGET2-Slovenija system enables the settlement of transactions between members of the system, and cross-border transactions with members of the TARGET2 system outside Slovenia. The number and value accounted for by the latter are relatively small, which limits the possibility of cross-border transfer of risk. An average of 55,600 transactions with a total value of EUR 42.30 billion were settled each month in the TARGET2-Slovenija system in 2009. At the same time members of the TARGET2-Slovenija system received a monthly average of 14,300 inward payments (from members

[54] With the introduction of the euro on 1 January 2007, the Bank of Slovenia's real-time gross settlement (RTGS) system for high-value tolar payments was replaced by the TARGET system. The changeover to the TARGET2 system, the successor to TARGET, was made in November 2007.

outside Slovenia) with a total value of EUR 5.28 billion, and sent a monthly average of 9,770 outward payments with a total value of EUR 5.33 billion. The TARGET2-Slovenija system's 100% availability in 2009 ensured that members had no disruption in the use of Eurosystem instruments to mitigate the effects of the financial turmoil. That the realisation of operational risks in the system would entail disruption to the Eurosystem and at the same time would sharply increase the banks' exposure to liquidity risk is proof of the importance of adequate risk management in the system.

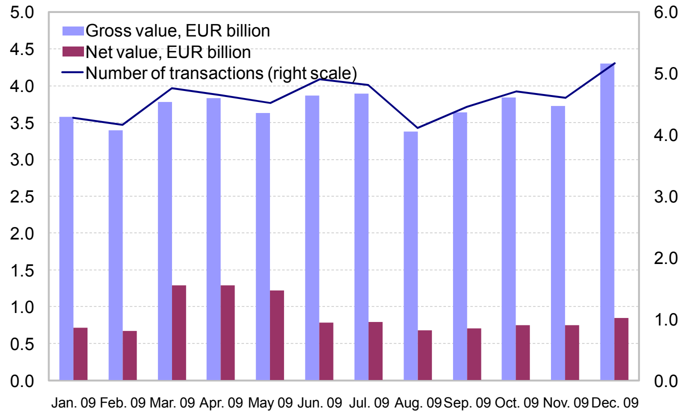
Figure 8.1: TARGET2-Slovenija: domestic and cross-border payments; value in EUR billion and number in thousand



Source: Bank of Slovenia

A monthly average of 4.59 million transactions with a total value of EUR 3.74 billion were processed in the Giro Clearing and SEPA ICT systems in 2009, while the average net monthly value of the settled transactions was EUR 0.88 billion. The offsetting rate thereby reached 76.6% (for settling the gross value of payments liquidity in the amount of 23.4% of the gross value was required). The ratio of net cash flow to the gross transaction value increased significantly between March and May 2009 as a result of the co-existence of two alternative system and the varying intensity of the migration of payments of individual members from the Giro Clearing system to the SEPA ICT system.

Figure 8.2: Giro Clearing and SEPA ICT (total): value in EUR billion and number in million



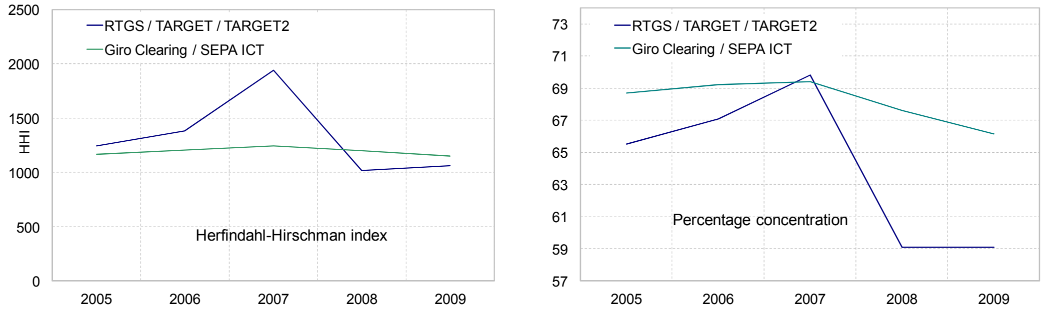
Source: Bank of Slovenia

There was again no need in 2009 to activate the Settlement Guarantee Scheme designed to manage financial risks in the event of illiquidity on the part of a member. With regard to operational risks, the Giro Clearing system (until ceasing to operate) ensured 100% availability, while the SEPA ICT system (from commencing operation in March 2009) ensured 99.85% availability.

There was no significant change in the TARGET2-Slovenija system's exposure to systemic risk.

Concentration in the TARGET2-Slovenija system as measured by the Herfindahl-Hirschman index was up slightly on 2008, although there was no change in the proportion of the number of transactions accounted for by the five largest system members. Concentration declined gently in the SEPA ICT system (including Giro Clearing). The proportion accounted for by the five largest members was down 1.5 percentage points on 2008.

Figure 8.3: Concentration of the number of transactions in the RTGS/TARGET/TARGET2 and Giro Clearing / SEPA ICT systems (Herfindahl-Hirschman Index; left) and proportion of total number of transactions accounted for by the five largest members (excluding the Bank of Slovenia; right)



Source:Bank of Slovenia

8.2 Securities clearing and settlement systems

The importance of risk management in settlement systems is increasing as a result of increased use of eligible securities to secure Eurosystem operations.

The services of securities clearing and settlement in Slovenia are provided by the Central Security Clearing Corporation (CSCC), which operates settlement systems to settle transactions concluded in the Ljubljana Stock Exchange, and to settle transactions concluded outside the regulated market. Operation is based on the principles of settlement versus payment and settlement free of payment. The Bank of Slovenia uses the latter for the needs of collateralising Eurosystem credit operations. On the basis of the statute of the European System of Central Banks, all credit operations of Eurosystem central banks must be fully secured by means of eligible collateral. This includes securities booked and settled in securities settlement systems that comply with Eurosystem requirements. In August 2009 the Governing Council of the ECB approved the CSCC's compliance as the operator of a system for the settlement of securities according to the principle of settlement free of payment as part of the assessment of the compliance of securities settlement systems in the euro area. The previous month, in an ad hoc assessment, the Governing Council had also confirmed the compliance of the CSCC's links with foreign securities settlement systems operated by Clearstream Banking Frankfurt and Clearstream Banking Luxembourg. The two assessments reflect the compliance of the management of settlement and operational risk at the CSCC from the point of view of the requirements and needs of the central banks of the Eurosystem.

The importance of risk management in settlement systems grew further as a result of the increasing use of eligible securities booked at the CSCC as collateral for Eurosystem central banking credit operations. Last year Slovenian banks and savings banks pledged a monthly average of EUR 2,135 million in eligible domestic securities as collateral, up 86.8% on 2008. The value rose sharply in the period to June 2009, then stabilised to reach EUR 2,369 million at end of the year. At the same time the use of the correspondence central banking model (which provides for the use of cross-border financial assets as collateral for Eurosystem credit operations) increased foreign banks' interest in using securities registered at the CSCC to a lesser extent in 2009. The average monthly value of Slovenian securities used as collateral for the credit operations of other central banks in the Eurosystem increased by 13.8% in 2009 to EUR 77 million.

STATISTICAL APPENDIX

1. Inter-sector financial claims and liabilities

Table 1.1: Inter-sector financial claims and liabilities of the institutional sectors of the Slovenian economy at the end of 2009 as a percentage of GDP

(As % GDP)	Claims						
	Domestic sectors					Rest of the world	Total
Liabilities	Corporates	Financial sector	Government	Households	Total		liabilities
Corporates	73.8	79.0	22.3	31.7	206.8	43.5	250.2
currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	
securities other than shares	0.3	1.5	0.1	0.1	2.0	0.8	
loans	10.3	69.1	0.4	2.5	82.3	13.5	
equity	38.8	6.8	17.2	24.1	87.0	17.3	
insurance technical provisions	0.0	0.0	0.0	0.0	0.0	0.0	
other	24.4	1.6	4.6	4.8	35.5	11.8	
Financial sector	18.5	40.6	20.3	61.9	141.3	75.9	217.2
currency and deposits	11.0	15.0	12.4	42.9	81.4	25.0	
securities other than shares	0.4	5.1	0.3	0.2	6.0	6.4	
loans	0.7	14.1	0.0	0.2	15.0	38.1	
equity	4.3	5.5	6.5	7.3	23.6	5.9	
insurance technical provisions	1.3	0.7	0.0	10.9	12.9	0.3	
other	0.8	0.2	1.0	0.4	2.4	0.3	
Government	5.1	17.0	15.6	2.1	39.7	20.5	60.3
currency and deposits	0.0	0.0	0.0	0.1	0.1	0.0	
securities other than shares	0.2	14.1	0.4	1.0	15.8	18.9	
loans	0.2	2.5	8.9	0.0	11.6	0.4	
equity	0.0	0.0	4.4	0.0	4.4	0.0	
insurance technical provisions	0.0	0.0	0.0	0.0	0.0	0.0	
other	4.7	0.4	1.9	1.0	7.9	1.2	
Households	3.9	28.9	1.0	0.0	33.8	0.0	33.8
currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	
securities other than shares	0.0	0.0	0.0	0.0	0.0	0.0	
loans	1.2	28.0	0.4	0.0	29.5	0.0	
equity	0.0	0.0	0.0	0.0	0.0	0.0	
insurance technical provisions	0.0	0.0	0.0	0.0	0.0	0.0	
other	2.7	0.9	0.6	0.0	4.3	0.0	
Total	101.4	165.4	59.1	95.7	421.6	140.0	561.6
currency and deposits	11.0	15.0	12.4	43.1	81.5	25.0	
securities other than shares	0.9	20.8	0.8	1.3	23.8	26.1	
loans	12.3	113.6	9.7	2.7	138.3	52.1	
equity	43.1	12.3	28.1	31.4	114.9	23.2	
insurance technical provisions	1.3	0.7	0.0	10.9	12.9	0.3	
other	32.7	3.1	8.1	6.3	50.1	13.3	
Rest of the world	29.6	53.9	1.5	18.4	103.4		103.4
currency and deposits	0.5	9.7	0.0	16.7			
securities other than shares	0.2	26.3	0.4	0.1			
loans	4.6	10.3	0.0	0.0			
equity	10.3	6.9	0.8	1.3			
insurance technical provisions	0.0	0.1	0.0	0.3			
other	13.9	0.6	0.3	0.0			
Total claims	130.9	219.3	60.7	114.1	525.0	140.0	665.0

Note: The table is based on financial accounts compiled by the Bank of Slovenia. The unconsolidated figures have been restructured into the form of a matrix with the aim of illustrating the underlying mutual financial ties between domestic institutional sectors and the rest of the world.

Source: Bank of Slovenia

Table 1.2: Inter-sector financial claims and liabilities of the institutional sectors of the Slovenian economy at the end of 2008 as a percentage of GDP

(% of GDP)	Claims						
	Domestic sector					Rest of	Total
Liabilities	Corporates	Financial sector	Government	Households	Total	the world	liabilities
Corporates	76.5	72.2	31.5	33.0	213.2	41.9	255.0
Cash and deposits	0.0	0.0	0.0	0.0	0.0	0.0	
Securities except shares	0.3	1.1	0.1	0.1	1.6	0.1	
Loans	7.5	57.9	0.8	2.3	68.5	10.3	
Equity	43.8	11.8	25.6	26.3	107.4	18.6	
Technical provisions	0.0	0.0	0.0	0.0	0.0	0.0	
Other	24.9	1.4	5.0	4.3	35.6	12.8	
Financial sector	19.9	26.2	13.1	56.6	115.8	73.3	189.1
Cash and deposits	10.8	7.1	5.7	36.1	59.7	28.3	
Securities except shares	0.6	3.0	0.4	0.1	4.2	1.2	
Loans	0.6	8.7	0.0	0.1	9.5	38.0	
Equity	5.8	6.6	5.5	10.8	28.7	5.4	
Technical provisions	1.1	0.5	0.1	8.9	10.6	0.2	
Other	1.0	0.3	1.4	0.5	3.1	0.3	
Government	5.6	12.7	17.1	1.9	37.4	9.6	46.9
Cash and deposits	0.0	0.0	0.0	0.1	0.1	0.0	
Securities except shares	0.3	10.6	0.5	0.9	12.3	8.2	
Loans	0.5	1.6	3.5	0.0	5.7	0.6	
Equity	0.0	0.0	10.3	0.0	10.3	0.0	
Technical provisions	0.0	0.0	0.0	0.0	0.0	0.0	
Other	4.7	0.5	2.8	0.9	8.9	0.8	
Households	3.7	24.4	0.7	0.0	28.8	0.0	28.8
Cash and deposits	0.0	0.0	0.0	0.0	0.0	0.0	
Securities except shares	0.0	0.0	0.0	0.0	0.0	0.0	
Loans	1.1	23.5	0.2	0.0	24.8	0.0	
Equity	0.0	0.0	0.0	0.0	0.0	0.0	
Technical provisions	0.0	0.0	0.0	0.0	0.0	0.0	
Other	2.6	0.9	0.6	0.0	4.1	0.0	
Total	105.8	135.7	62.5	91.5	395.5	124.8	520.2
Cash and deposits	10.8	7.1	5.7	36.2	59.8	28.3	
Securities except shares	1.3	14.8	1.0	1.1	18.1	9.5	
Loans	9.7	91.9	4.6	2.4	108.7	48.9	
Equity	49.6	18.4	41.4	37.1	146.5	24.0	
Technical provisions	1.1	0.5	0.1	8.9	10.6	0.2	
Other	33.3	3.0	9.8	5.7	51.8	13.9	
Rest of the world	26.0	59.3	1.6	15.7	102.5		102.5
Cash and deposits	0.5	13.9	0.0	12.5	26.9		
Securities except shares	0.2	27.1	0.5	0.2	28.0		
Loans	3.0	8.1	0.0	0.0	11.2		
Equity	8.3	8.9	0.7	2.7	20.5		
Technical provisions	0.0	0.1	0.0	0.3	0.3		
Other	14.0	1.2	0.4	0.0	15.6		
Total claims	131.8	195.0	64.1	107.2	498.0	124.8	622.8

Note: The table is based on financial accounts compiled by the Bank of Slovenia. The unconsolidated figures have been restructured into the form of a matrix with the aim of illustrating the underlying mutual financial ties between domestic institutional sectors and the rest of the world.

Source: Bank of Slovenia

Table 1.3: Inter-sector financial claims and liabilities of the institutional sectors of the Slovenian economy at the end of 2007 as a percentage of GDP

(As % GDP)	Claims						
	Domestic sectors					Rest of the world	Total
Liabilities	Corporates	Financial sector	Government	Households	Total		liabilities
Corporates	76.3	72.0	31.1	33.2	212.7	41.8	254.5
currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	
securities other than shares	0.3	1.1	0.1	0.1	1.6	0.1	
loans	7.4	57.8	0.8	2.3	68.4	10.8	
equity	43.7	11.8	25.5	26.4	107.4	17.9	
insurance technical provisions	0.0	0.0	0.0	0.0	0.0	0.0	
other	24.9	1.3	4.6	4.4	35.2	13.0	
Financial sector	19.8	26.2	14.1	57.4	117.4	73.1	190.5
currency and deposits	10.8	7.1	5.7	36.8	60.4	28.3	
securities other than shares	0.6	3.0	0.4	0.1	4.1	1.2	
loans	0.6	8.7	0.0	0.1	9.4	37.8	
equity	5.8	6.6	6.5	10.9	29.7	5.4	
insurance technical provisions	1.1	0.5	0.1	8.9	10.6	0.2	
other	1.0	0.3	1.4	0.5	3.1	0.3	
Government	5.8	12.7	17.3	1.9	37.7	9.5	47.3
currency and deposits	0.0	0.0	0.0	0.1	0.1	0.0	
securities other than shares	0.3	10.6	0.5	1.0	12.4	8.2	
loans	0.6	1.6	3.5	0.0	5.7	0.6	
equity	0.0	0.0	10.3	0.0	10.3	0.0	
insurance technical provisions	0.0	0.0	0.0	0.0	0.0	0.0	
other	4.9	0.5	3.0	0.8	9.2	0.8	
Households	3.8	24.5	0.8	0.0	29.1	0.0	29.1
currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0	
securities other than shares	0.0	0.0	0.0	0.0	0.0	0.0	
loans	1.1	23.6	0.2	0.0	24.9	0.0	
equity	0.0	0.0	0.0	0.0	0.0	0.0	
insurance technical provisions	0.0	0.0	0.0	0.0	0.0	0.0	
other	2.7	0.9	0.6	0.0	4.1	0.0	
Total	105.8	135.3	63.3	92.5	396.9	124.5	521.4
currency and deposits	10.8	7.1	5.7	37.0	60.5	28.3	
securities other than shares	1.2	14.7	1.0	1.3	18.2	9.4	
loans	9.7	91.7	4.6	2.5	108.4	49.2	
equity	49.5	18.3	42.3	37.3	147.5	23.3	
insurance technical provisions	1.1	0.5	0.1	8.9	10.6	0.2	
other	33.4	2.9	9.6	5.7	51.7	14.1	
Rest of the world	26.3	59.1	1.6	15.8	102.8		102.8
currency and deposits	0.6	13.8	0.0	12.7	27.1		
securities other than shares	0.2	27.0	0.5	0.2	27.9		
loans	3.4	8.1	0.0	0.0	11.5		
equity	7.9	8.9	0.7	2.6	20.1		
insurance technical provisions	0.0	0.1	0.0	0.3	0.3		
other	14.2	1.2	0.4	0.0	15.8		
Total claims	132.0	194.4	64.9	108.4	499.7	124.5	624.2

Note: The table is based on financial accounts compiled by the Bank of Slovenia. The unconsolidated figures have been restructured into the form of a matrix with the aim of illustrating the underlying mutual financial ties between domestic institutional sectors and the rest of the world.

Source: Bank of Slovenia

2. Financial system

Table 2.1: Structure of the financial system

	Total assets, EUR million		Structure, %		as % GDP		No. of institutions	
	2008	2009	2008	2009	2008	2009	2008	2009
Monetary financial institutions[1]	47,948	51,824	76.3	76.4	129.1	148.5	24	25
banks	47,628	51,427	75.8	75.8	128.3	147.4	21	22
privately owned	38,484	40,885	61.2	60.3	103.6	117.2	-	-
domestic	18,908	20,622	30.1	30.4	50.9	59.1	-	-
foreign	19,575	20,262	31.1	29.9	52.7	58.1	-	-
government-owned	9,145	10,543	14.5	15.5	24.6	30.2	-	-
savings banks	397	397	0.6	0.6	1.1	1.1	3	3
NMFIs	14,925	16,030	23.7	23.6	40.2	45.9	-	-
insurers[2]	5,151	5,680	8.2	8.4	13.9	16.3	17	17
pension funds[3]	1,041	1,296	1.7	1.9	2.8	3.7	10	10
investment funds	1,912	2,234	3.0	3.3	5.1	6.4	131	132
leasing companies[4, 5]	6,144	6,144	9.8	9.1	16.5	17.6	22	21
BHs, MCs, others[5]	676	676	1.1	1.0	1.8	1.9	-	-
Total	62,872	67,854	100.0	100.0	169.3	194.5	-	-

Notes: Figures for financial institutions that are not banks, insurers, pension companies or pension and investment funds are obtained from the AJPES database of annual accounts based on the SKD 2008 classification.
[1] Monetary financial institutions do not include the central bank. [2] The figures for the total assets of reinsurance companies are for the end of the third quarter of 2009. [3] The First Pension Fund is included among pension funds. [4] Includes leasing companies monitored by the BAS's leasing committee. [5] Total assets according to the figures for the end of 2008.

Sources: Bank of Slovenia, ISA, SMA, AJPES, BAS

Table 2.2: Market concentration of individual types of financial institution

		Banks		Insurers		Pension funds		Investment funds		Leasing companies	
		2008	2009	2008	2009	2008	2009	2008	2009	2008	2009
HHI	all companies	1,265	1,250	2,389	2,302	2,052	2,119	555	492	1,903	1,680
	five largest	1,121	1,109	2,329	2,233	2,042	2,109	464	403	1,801	1,600
Share, %	five largest	59	60	77	75	94	94	42	40	72	75
	largest	30	30	45	44	29	32	14	15	39	33

Note: The Herfindahl-Hirschman Index (HHI) is calculated in terms of total assets, with the exception of leasing companies, for which it is calculated in terms of volume of business. The figures for pension funds do not include the First Pension Fund, which is a closed pension fund that does not envisage further inflows.

Sources: Bank of Slovenia, ISA, SMA, AJPES, BAS

Table 2.3: Financial indicators for individual types of financial institution

	2004	2005	2006	2007	2008	2009
			Pre-tax profit, EUR million			
Banks	234.2	261.2	393.7	514.2	306.3	160.8
Insurers[1]	22.7	47.2	67.8	117.5	-2.8	19.7
Leasing companies	44.7	48.3	54.6	60.7	29.9	
Management companies	16.6	18.1	17.1	34.6	21.3	
			ROA, %			
Banks	1.06	1.00	1.25	1.36	0.68	0.32
Insurers[1]	0.79	1.45	1.74	2.63	-0.06	0.36
Leasing companies	2.07	1.66	1.51	1.29	0.52	
Management companies	25.86	14.01	11.64	15.98	9.83	
			ROE, %			
Banks	12.72	12.72	15.07	16.29	8.14	3.85
Insurers[1]	4.53	8.66	9.69	12.90	-0.28	2.05
Leasing companies	29.72	24.83	21.92	20.07	9.33	
Management companies	37.39	20.24	16.74	23.01	15.15	

Note: [1] Net profit for the accounting period (profit after tax) is taken into account for insurance companies and reinsurance companies. The figures for reinsurance companies are for the first three quarters of 2009.

Sources: Bank of Slovenia, ISA, AJPES

Table 2.4: Direct ownership structure of the Slovenian financial system (shares valued at market price or book value) in percentages

ISSUERS / HOLDERS	Banks	Other financial intermediaries	Insurance corporations and pension funds	Corporates	Total
	Ownership structure (%)				
	2005				
Non-financial corporations	24	30	14	31	29
Banks	8	8	7	3	4
Other financial intermediaries	2	9	1	11	10
Insurance corporations and pension funds	3	8	10	1	2
Government	23	8	54	23	23
Households	2	34	1	17	16
Non-residents	36	2	10	11	13
Others	2	2	0	3	2
Total	100	100	100	100	100
	2006				
Non-financial corporations	24	29	16	29	28
Banks	8	10	5	3	5
Other financial intermediaries	2	15	1	9	8
Insurance corporations and pension funds	3	6	9	2	3
Government	20	7	56	25	24
Households	2	30	4	18	16
Non-residents	39	1	8	11	15
Others	1	2	1	3	2
Total	100	100	100	100	100
	2007				
Non-financial corporations	17	33	22	32	30
Banks	7	8	6	2	3
Other financial intermediaries	5	16	1	10	9
Insurance corporations and pension funds	3	7	9	2	2
Government	26	1	47	24	23
Households	8	32	6	19	18
Non-residents	34	2	9	11	13
Others	1	2	1	1	1
Total	100	100	100	100	100
	2008				
Non-financial corporations	24	31	19	39	35
Banks	5	4	11	3	4
Other financial intermediaries	5	19	4	8	8
Insurance corporations and pension funds	5	4	15	1	3
Government	21	1	31	19	19
Households	3	25	5	15	13
Non-residents	38	13	15	13	17
Others	0	3	0	1	1
Total	100	100	100	100	100
	2010				
Non-financial corporations	21	27	19	38	33
Banks	6	6	10	4	5
Other financial intermediaries	5	20	4	7	7
Insurance corporations and pension funds	4	5	11	2	3
Government	25	1	36	20	21
Households	3	27	6	16	14
Non-residents	37	12	13	12	17
Others	0	1	1	1	1
Total	100	100	100	100	100

Sources: CSCC, own calculations

3. Banking sector

Table 3.1: Banking sector's balance sheet: amounts in EUR million and growth rates in percentages

	Value, EUR million					Growth, %				
	2005	2006	2007	2008	2009	2005	2006	2007	2008	2009
ASSETS	29,287	33,868	42,343	47,628	51,427	23.6	15.6	25.0	12.5	8.0
1) Cash	599	1,057	604	1,243	1,454	1.9	76.3	-42.9	105.9	17.0
2) Loans to banks (including BoS/Eurosystem)	2,872	3,067	4,072	4,031	5,694	35.6	6.8	32.8	-1.0	41.2
3) Loans to non-banking sectors	16,149	20,414	28,302	33,530	33,744	26.1	26.4	38.6	18.5	0.6
3.1 Currency breakdown										
domestic currency	8,757	9,095	26,669	31,506	32,110	4.9	3.9	193.2	18.1	1.9
foreign currency	7,392	11,320	1,633	2,024	1,634	65.7	53.1	-85.6	23.9	-19.3
3.2 Maturity breakdown										
short-term	5,219	6,821	9,893	12,515	10,597	19.5	30.7	45.0	26.5	-15.3
long-term	10,931	13,593	18,409	21,015	23,147	29.5	24.4	35.4	14.2	10.1
3.3 Sector breakdown										
corporate	9,908	12,364	17,039	20,245	20,006	22.5	24.8	37.8	18.8	-1.2
household	4,078	5,060	6,429	7,386	7,886	28.0	24.1	27.1	14.9	6.8
government	665	574	465	506	735	11.6	-13.8	-18.9	8.9	45.1
other	1,498	2,417	4,369	5,392	5,118	59.4	61.3	80.7	23.4	-5.1
4) Financial assets/securities	8,243	7,719	7,459	7,093	8,547	19.4	-6.4	-3.4	-4.9	20.5
4.1 Currency breakdown										
domestic currency	5,406	5,014	6,506	6,232	7,419	36.4	-7.2	29.7	-4.2	19.0
foreign currency	2,254	2,006	56	21	10	-11.5	-11.0	-97.2	-63.0	-49.7
4.2 Maturity breakdown										
short-term	3,595	2,101	1,192	1,107	1,869	7.8	-41.6	-43.3	-7.2	68.8
long-term	4,064	4,919	5,369	5,146	5,560	28.1	21.1	9.1	-4.2	8.0
4.3 Sector breakdown										
government	2,706	2,718	4,283	4,079	5,094	7.9	0.5	57.5	-4.8	24.9
Bank of Slovenia	3,501	1,789	0	0	0	9.5	-48.9	….	….	….
other	2,037	3,211	3,176	3,014	3,453	70.0	57.7	-1.1	-5.1	14.6
5) Capital investments	356	427	615	627	696	11.6	19.9	43.9	2.0	11.0
6) Other	931	1,006	1,031	917	964	-2.2	8.0	2.5	-11.1	5.1
LIABILITIES	29,287	33,868	42,343	47,628	51,427	23.6	15.6	25.0	12.5	8.0
1) Liabilities to banks (including BoS/Eurosystem)	8,397	10,797	16,086	19,372	17,870	80.0	28.6	49.0	20.4	-7.8
foreign banks	7,892	10,112	14,410	16,091	12,878	86.4	28.1	42.5	11.7	-20.0
2) Deposits by non-banking sectors	16,018	17,507	19,381	20,612	23,554	8.8	9.3	10.7	6.4	14.3
2.1 Currency breakdown										
domestic currency	10,716	11,653	18,848	20,127	23,103	11.4	8.7	61.7	6.8	14.8
foreign currency	5,300	5,853	532	485	450	4.1	10.4	-90.9	-8.9	-7.2
2.2 Maturity breakdown										
short-term	14,017	15,341	17,626	18,151	18,217	10.9	9.4	14.9	3.0	0.4
long-term	1,999	2,165	1,754	2,461	5,337	-3.5	8.3	-19.0	40.3	116.8
2.3 Sector breakdown										
corporate	4,340	4,787	4,819	4,770	4,934	11.6	10.3	0.7	-1.0	3.4
household	10,545	11,322	12,370	13,513	14,092	6.0	7.4	9.3	9.2	4.3
government	867	1,114	1,510	1,857	3,990	53.4	28.5	35.6	22.9	114.9
other	266	285	681	472	537	-15.6	6.9	139.0	-30.7	13.8
3) Securities	992	976	963	1,259	3,435	5.7	-1.6	-1.3	30.6	172.9
3.1 Currency breakdown										
domestic currency	973	969	962	1,259	3,435	5.5	-0.4	-0.7	30.8	172.9
foreign currency	19	7	1	0	0	17.6	-63.9	-85.1	-95.1	-100.0
3.2 Maturity breakdown										
short-term	21	8	11	108	8	-73.3	-63.0	49.4	845.6	-92.7
long-term	971	968	952	1,151	3,427	12.8	-0.3	-1.7	20.9	197.8
4) Provisions	180	184	208	176	173	-64.1	2.2	12.6	-15.4	-1.3
5) Subordinated debt	709	993	1,470	1,597	1,550	18.4	40.0	48.1	8.6	-2.9
6) Capital	2,486	2,841	3,556	3,996	4,295	29.6	14.3	25.2	12.4	7.5
7) Others	505	570	680	617	551	42.7	12.8	19.3	-9.3	-10.7

Notes: Converted to euros at the conversion rate.
The 2006, 2007, 2008 and 2009 figures are those reported under the IFRS, while those for 2005 are based on estimated values in accordance with the IFRS.

Source: Bank of Slovenia

Table 3.2: Banking sector's balance sheet: as proportion of total assets, and ratio to GDP in percentages

	As % of total assets					As % GDP				
	2005	2006	2007	2008	2009	2005	2006	2007	2008	2009
ASSETS	100.0	100.0	100.0	100.0	100.0	102.0	109.2	122.5	128.3	147.4
1) Cash	2.0	3.1	1.4	2.6	2.8	2.1	3.4	1.7	3.3	4.2
2) Loans to banks (including BoS/Eurosystem)	9.8	9.1	9.6	8.5	11.1	10.0	9.9	11.8	10.9	16.3
3) Loans to non-banking sectors	55.1	60.3	66.8	70.4	65.6	56.3	65.8	81.9	90.3	96.7
3.1 Currency breakdown										
domestic currency	29.9	26.9	63.0	66.1	62.4	30.5	29.3	77.1	84.8	92.0
foreign currency	25.2	33.4	3.9	4.2	3.2	25.8	36.5	4.7	5.4	4.7
3.2 Maturity breakdown						0.0	0.0	0.0	0.0	0.0
short-term	17.8	20.1	23.4	26.3	20.6	18.2	22.0	28.6	33.7	30.4
long-term	37.3	40.1	43.5	44.1	45.0	38.1	43.8	53.3	56.6	66.3
3.3 Sector breakdown										
corporate	33.8	36.5	40.2	42.5	38.9	34.5	39.9	49.3	54.5	57.3
household	13.9	14.9	15.2	15.5	15.3	14.2	16.3	18.6	19.9	22.6
government	2.3	1.7	1.1	1.1	1.4	2.3	1.9	1.3	1.4	2.1
other	5.1	7.1	10.3	11.3	10.0	5.2	7.8	12.6	14.5	14.7
4) Financial assets/securities	28.1	22.8	17.6	14.9	16.6	28.7	24.9	21.6	19.1	24.5
4.1 Currency breakdown										
domestic currency	18.5	14.8	15.4	13.1	14.4	18.8	16.2	18.8	16.8	21.3
foreign currency	7.7	5.9	0.1	0.0	0.0	7.9	6.5	0.2	0.1	0.0
4.2 Maturity breakdown						0.0	0.0	0.0	0.0	0.0
short-term	12.3	6.2	2.8	2.3	3.6	12.5	6.8	3.4	3.0	5.4
long-term	13.9	14.5	12.7	10.8	10.8	14.2	15.9	15.5	13.9	15.9
4.3 Sector breakdown										
government	9.2	8.0	10.1	8.6	9.9	9.4	8.8	12.4	11.0	14.6
Bank of Slovenia	12.0	5.3	0.0	0.0	0.0	12.2	5.8	0.0	0.0	0.0
other	7.0	9.5	7.5	6.3	6.7	7.1	10.4	9.2	8.1	9.9
5) Capital investments	1.2	1.3	1.5	1.3	1.4	1.2	1.4	1.8	1.7	2.0
6) Other	3.2	3.0	2.4	1.9	1.9	3.2	3.2	3.0	2.5	2.8
LIABILITIES	100	100	100	100	100	102.0	109.2	122.5	128.3	147.4
1) Liabilities to banks (including BoS/Eurosystem)	28.7	31.9	38.0	40.7	34.7	29.3	34.8	46.5	52.2	51.2
foreign banks	26.9	29.9	34.0	33.8	25.0	27.5	32.6	41.7	43.3	36.9
2) Deposits by non-banking sectors	54.7	51.7	45.8	43.3	45.8	55.8	56.5	56.1	55.5	67.5
2.1 Currency breakdown										
domestic currency	36.6	34.4	44.5	42.3	44.9	37.3	37.6	54.5	54.2	66.2
foreign currency	18.1	17.3	1.3	1.0	0.9	18.5	18.9	1.5	1.3	1.3
2.2 Maturity breakdown						0.0	0.0	0.0	0.0	0.0
short-term	47.9	45.3	41.6	38.1	35.4	48.8	49.5	51.0	48.9	52.2
long-term	6.8	6.4	4.1	5.2	10.4	7.0	7.0	5.1	6.6	15.3
2.3 Sector breakdown										
corporate	14.8	14.1	11.4	10.0	9.6	15.1	15.4	13.9	12.8	14.1
household	36.0	33.4	29.2	28.4	27.4	36.7	36.5	35.8	36.4	40.4
government	3.0	3.3	3.6	3.9	7.8	3.0	3.6	4.4	5.0	11.4
other	0.9	0.8	1.6	1.0	1.0	0.9	0.9	2.0	1.3	1.5
3) Securities	3.4	2.9	2.3	2.6	6.7	3.5	3.1	2.8	3.4	9.8
3.1 Currency breakdown										
domestic currency	3.3	2.9	2.3	2.6	6.7	3.4	3.1	2.8	3.4	9.8
foreign currency	0.1	0.0	0.0	0.0	0.0	0.1	0.0	0.0	0.0	0.0
3.2 Maturity breakdown										
short-term	0.1	0.0	0.0	0.2	0.0	0.1	0.0	0.0	0.3	0.0
long-term	3.3	2.9	2.2	2.4	6.7	3.4	3.1	2.8	3.1	9.8
4) Provisions	0.6	0.5	0.5	0.4	0.3	0.6	0.6	0.6	0.5	0.5
5) Subordinated debt	2.4	2.9	3.5	3.4	3.0	2.5	3.2	4.3	4.3	4.4
6) Capital	8.5	8.4	8.4	8.4	8.4	8.7	9.2	10.3	10.8	12.3
7) Others	1.7	1.7	1.6	1.3	1.1	1.8	1.8	2.0	1.7	1.6

Source: Bank of Slovenia

Table 3.3: Banking sector's income statement: amounts in EUR million and growth rates in percentages

	Value, EUR million					Growth, %				
	2005	2006	2007	2008	2009	2005	2006	2007	2008	2009
1. Net interest income	631	690	816	945	925	5.4	9.2	18.3	15.7	-2.1
1.1 Interest income	1,198	1,421	1,954	2,615	2,086	0.3	18.6	37.5	33.8	-20.2
1.2 Interest expenses	567	731	1,138	1,671	1,162	-4.8	29.0	55.6	46.8	-30.5
2. Net non-interest income	417	526	617	416	492	9.0	26.0	17.3	-32.6	18.4
2.1 Net fees and commissions	282	309	336	340	335	9.1	9.5	9.0	1.0	-1.5
2.2 Net financial transactions	71	97	136	-115	42	-15.7	37.2	39.7	-184.4	-136.2
2.3 Net other	65	120	145	191	116	60.0	85.7	20.5	31.8	-39.1
3. Gross income (1+2)	1,049	1,216	1,433	1,360	1,417	6.8	15.9	17.9	-5.1	4.2
4. Operating costs	647	702	756	776	762	5.8	8.5	7.7	2.7	-1.9
labour costs	342	367	402	412	413	5.0	7.3	9.4	2.6	0.3
5. Net income (3-4)	401	513	677	584	655	8.5	28.0	31.9	-13.7	12.2
6. Net provisions	140	120	163	278	496	3.2	-14.5	36.0	70.5	78.5
7. Total costs (4+6)	787	822	919	1,054	1,257	5.3	4.4	11.8	14.7	19.3
8. Pre-tax profit (3-7)	261	394	514	306	160	11.5	50.7	30.6	-40.4	-47.9
9. Taxes	52	91	102	59	38	-35.9	75.5	12.8	-42.8	-34.7
10 Net profit (8-9)	209	303	412	248	121	36.5	44.6	36.0	-39.8	-51.1

Notes: Converted to euros at the conversion rate.
The 2006, 2007, 2008 and 2009 figures are those reported under the IFRS, while those for 2005 are based on estimated values in accordance with the IFRS.

Source: Bank of Slovenia

Table 3.4: Banking sector's income statement: as proportion of gross income and as proportion of total assets in percentages

	As % of gross income					As % of total assets				
	2005	2006	2007	2008	2009	2005	2006	2007	2008	2009
1. Net interest income	60	57	57	69	65	2.2	2.0	1.9	2.0	1.8
1.1 Interest income	114	117	136	192	147	4.1	4.2	4.6	5.5	4.1
1.2 Interest expenses	54	60	79	123	82	1.9	2.2	2.7	3.5	2.3
2. Net non-interest income	39.8	43.3	43.0	30.6	34.7	1.4	1.6	1.5	0.9	1.0
2.1 Net fees and commissions	27	25	23	25	24	1.0	0.9	0.8	0.7	0.7
2.2 Net financial transactions	7	8	9	-8	3	0.2	0.3	0.3	-0.2	0.1
2.3 Net other	6	10	10	14	8	0.2	0.4	0.3	0.4	0.2
3. Gross income (1+2)	100	100	100	100	100	3.6	3.6	3.4	2.9	2.8
4. Operating costs	62	58	53	57	54	2.2	2.1	1.8	1.6	1.5
labour costs	33	30	28	30	29	1.2	1.1	0.9	0.9	0.8
5. Net income (3-4)	38	42	47	43	46	1.4	1.5	1.6	1.2	1.3
6. Net provisions	13	10	11	20	35	0.5	0.4	0.4	0.6	1.0
7. Total costs (4+6)	75	68	64	77	89	2.7	2.4	2.2	2.2	2.4
8. Pre-tax profit (3-7)	25	32	36	23	11	0.9	1.2	1.2	0.6	0.3
9. Taxes	5	7	7	4	3	0.2	0.3	0.2	0.1	0.1
10 Net profit (8-9)	20	25	29	18	9	0.7	0.9	1.0	0.5	0.2

Source: Bank of Slovenia

Table 3.5: Selected performance indicators for the banking sector

	2005	2006	2007	2008	2009
1) Profitability and margins, %					
ROA	1.0	1.3	1.4	0.7	0.3
ROE	12.7	15.1	16.3	8.1	3.8
CIR	61.7	57.8	52.7	57.1	53.7
financial intermediation margin	4.0	3.9	3.8	3.0	2.9
interest margin (per total assets)	2.4	2.2	2.2	2.1	1.9
non-interest margin (per total assets)	1.6	1.7	1.6	0.9	1.0
net interest margin (per interest-bearing assets)	2.6	2.4	2.3	2.2	2.0
interest spread[1]	3.8	3.8	2.3	2.3	2.3
2) Structure of assets and liabilities, %					
2.1 Maturity breakdown of loans to non-banking sectors					
short-term loans / loans	32.3	33.4	35.0	37.0	33.2
long-term loans / loans	67.7	66.6	65.0	63.0	66.8
2.2 Maturity breakdown of deposits by non-banking sectors					
short-term deposits / deposits	87.5	87.6	90.9	88.1	77.3
long-term deposits / deposits	12.5	12.4	9.1	11.9	22.7
2.3 Regional breakdown of loans					
to residents	95.4	94.4	92.2	92.5	93.0
to non-residents	4.6	5.6	7.8	7.5	7.0
2.4 Foreign currency sub-balance					
foreign currency assets / total assets	40.5	45.9	6.0	6.1	5.0
foreign currency liabilities / total assets	42.9	46.8	5.0	4.9	3.5
difference	-2.4	-0.8	1.1	1.2	1.5
foreign currency loans / loans	48.7	55.9	6.4	6.4	5.2
foreign currency deposits / deposits	49.4	53.3	5.9	6.0	4.5
foreign currency loans / loans (non-banking sectors)	45.8	55.4	5.8	6.0	4.8
foreign currency deposits / deposits (non-banking sectors)	33.1	33.4	2.7	2.4	1.9
2.5 Securities					
securities / loans to non-banking sectors	50.4	37.3	26.1	21.1	24.5
2.6 Sector breakdown					
corporate					
corporate loans / loans to non-banking sectors	65.9	66.7	67.7	68.6	67.3
foreign currency corporate loans / corporate loans	57.0	65.4	3.7	3.4	2.3
household					
household loans / loans to non-banking sectors	25.3	24.9	22.9	22.3	23.5
foreign currency household loans / household loans	11.8	23.2	10.2	12.9	10.6
government					
loans to government / loans to non-banking sectors	4.1	2.8	1.6	1.5	2.2
rest of the world					
liabilities to foreign banks / total assets	26.9	29.9	34.0	33.7	25.0
3) Asset quality					
impairments, EUR million	1,168.7	1,233.8	1,311.1	1,403.2	1,827.2
classified claims, EUR million	25,209.1	31,581.0	40,541.6	47,129.2	49,757.3
impairments / classified claims, %	4.6	3.9	3.2	3.0	3.7
non-performing claims / classified claims, %	2.5	2.5	1.8	1.8	2.2
impairments for non-performing claims / classified claims, %	80.6	84.3	86.4	79.3	75.9
non-performing claims / classified claims, %	30.8	31.0	20.8	19.1	18.3
non-performing classified claims / regulatory capital, %	6.0	4.9	2.8	4.0	5.8
sum of large exposures / capital, %	222.6	221.2	217.4	168.7	159.2
4) Interest-rate risk					
gap between interest-bearing assets and liabilities, percentage points	3.7	3.7	5.0	4.8	6.2
interest-bearing assets / assets, %	90.2	91.3	95.1	94.2	96.0
interest-bearing liabilities / liabilities, %	86.5	87.6	90.1	89.4	89.8
5) Currency risk					
open foreign exchange position / regulatory capital, %	21.7	25.8	0.9	0.2	0.9
6) Liquidity					
average liquid assets / average short-term deposits by non-banking sectors, %	9.5	9.7	8.37	34.33	36.16
average liquid assets / average total assets, %	4.8	4.5	3.6	13.78	13.82
first-bucket liquidity ratio	1.12	1.13	1.21	1.24	1.33
second-bucket liquidity ratio	1.11	1.15	1.13	1.14	1.17
debt securities / total assets, %	26.2	20.8	16.0	13.5	15.0
7) Solvency and capital structure, %					
capital adequacy (solvency ratio)	10.5	11.1	11.2	11.7	11.6
Tier I capital adequacy	8.9	9.3	8.9	10.0	10.3
additional own funds / original own funds	45.3	38.0	48.5	33.3	30.0

Notes: [1] Spread between the average effective tolar interest rate on loans to and deposits by non-banking sectors in the final quarter.
[2] The 2006, 2007, 2008 and 2009 figures are those reported under the IFRS, while those for 2005 are based on estimated values in accordance with the IFRS.

Source: Bank of Slovenia

4. Insurers

Table 4.1: Total assets and operating results of insurance companies and reinsurance companies

	2005	2006	2007	2008	2009	2006	2007	2008	2009
	Value, EUR million					Growth, %			
	Insurance companies								
Total assets	2,946	3,519	4,550	4,590	5,091	19.4	29.3	0.9	10.9
non-life insurance	1,565	1,806	2,251	2,265	2,335	15.4	24.6	0.7	3.1
life insurance	1,381	1,713	2,299	2,325	2,755	24.0	34.2	1.1	18.5
Results									
result from general insurance[1]	47.1	64.9	69.1	1.0	19.4	37.6	6.5	-98.6	1860.8
result from health insurance[1]	-8.6	-2.1	9.9	10.9	10.8	-75.7	-573.4	9.9	-0.7
result from life insurance[1]	14.1	13.9	20.8	1.8	27.4	-1.2	49.5	-91.5	1446.5
income from investments	78.0	74.6	118.7	104.0	99.1	-4.4	59.1	-12.4	-4.7
expenses from investments	18.7	13.1	21.2	86.9	69.9	-29.8	62.0	309.3	-19.6
net profit[2]	37.6	51.5	95.1	2.9	23.1	37.1	84.7	-97.0	696.9
ROE, %	8.70	9.93	12.42	0.34	2.99				
ROA, %	1.37	1.59	2.36	0.06	0.48				
	Reinsurance companies[3]								
Total assets	314	368	485	561	590	17.3	31.7	15.7	5.1
Results									
result from general insurance	10.8	16.0	11.3	-0.2	2.0	47.8	-29.1	-101.5	-1265.0
income from investments	14.4	15.6	31.3	27.0	13.2	8.2	101.2	-13.9	-51.2
expenses from investments	2.7	2.4	6.9	30.6	13.1	-11.4	184.6	343.0	-57.1
net profit	9.7	16.3	22.4	-5.7	-3.4	68.4	37.6	-125.6	-40.4
ROE, %	10.58	15.67	15.48	-3.16	-1.82				
ROA, %	3.11	4.77	5.25	-1.10	-0.59				

Notes: [1] Result from ordinary activities.
[2] Net profit for the accounting period is calculated after taxes.
[3] The figures for reinsurance companies in 2009 relate to the end of the third quarter.
Sources: ISA, own calculations

Table 4.2: Capital adequacy of insurance companies and reinsurance companies

						Growth, %			
	2005	2006	2007	2008	2009	2006	2007	2008	2009
	Insurance companies (overall)								
Minimum capital requirement, EUR million	200.7	220.1	261.0	275.2	286.6	9.7	18.6	5.5	4.1
Surplus, EUR million	72.0	155.0	222.2	144.8	150.1	115.3	43.4	-34.8	3.6
Surplus / minimum capital requirement, %	35.9	70.4	85.1	52.6	52.4	96.3	20.9	-38.2	-0.5
	Life insurance								
Surplus / minimum capital requirement, %	26.3	66.6	68.8	60.9	61.1				
Original own funds / net technical provisions, %	6.9	8.0	10.4	10.3	8.6				
	Non-life insurance								
Surplus / minimum capital requirement, %	40.0	72.1	93.1	48.2	47.6				
Original own funds / net written premium (%)	19.8	26.7	45.3	36.9	36.0				
	Reinsurance companies[1]								
Minimum capital requirement, EUR million	19.3	21.9	26.1	26.1	29.9	13.4	18.9	0.0	14.6
Surplus, EUR million	30.8	51.8	60.2	75.9	67.2	67.9	16.3	26.1	-11.5
Surplus / minimum capital requirement, %	159.5	236.3	231.1	291.4	225.1	48.1	-2.2	26.1	-22.7
Original own funds / net written premium (%)	83.6	73.8	107.0	105.6	124.8	-11.6	44.9	-1.3	18.2

Note: [1] The figures for reinsurance companies in 2009 relate to the end of the third quarter.
Sources: ISA, own calculations

Table 4.3: Claims ratios for major types of insurance

	2005	2006	2007	2008	2009
			Insurance companies		
Overall	0.59	0.57	0.56	0.62	0.62
Life insurance	0.33	0.29	0.27	0.28	0.32
Voluntary health insurance	0.93	0.86	0.80	0.83	0.82
General insurance	0.59	0.60	0.62	0.71	0.69
motor vehicle liability insurance	0.56	0.54	0.55	0.55	0.57
motor vehicle insurance	0.71	0.76	0.77	0.87	0.89
accident insurance	0.52	0.44	0.39	0.39	0.38
other property insurance	0.70	0.64	0.76	1.04	0.86
fire and natural disaster insurance	0.43	0.45	0.60	1.14	0.69
credit insurance	0.61	0.72	0.71	0.54	0.90
other general insurance	0.63	0.77	0.64	0.61	0.62
			Reinsurance companies		
Overall	0.49	0.56	0.56	0.83	0.66

Source: ISA

Table 4.4: Coverage of net insurance technical provisions by assets covering technical provisions

	2004	2005	2006	2007	2008	2009
Insurance technical provisions, EUR million	1,939	2,250	2,601	3,056	3,033	3,464
growth, %		16	16	18	-1	14
Assets covering technical provisions, EUR million	2,150	2,476	2,856	3,357	3,493	4,115
growth, %		15	15	18	4	18
Assets covering technical provisions / insurance technical provisions, %	110.9	110.1	109.8	109.8	115.2	118.8
Assets covering technical provisions / GDP, %	7.9	8.6	9.2	9.7	9.4	11.8
Mathematical provisions (EUR million)	971	1,173	1,452	1,748	1,752	2,105
growth, %		21	24	20	0	20
Assets covering mathematical provisions, EUR million	1,152	1,361	1,665	2,042	2,095	2,539
growth, %		18	22	23	3	21
Assets covering mathematical provisions / mathematical provisions, %	118.7	116.1	114.7	116.8	119.6	120.6
Assets covering mathematical provisions / GDP, %	4.3	4.7	5.4	5.9	5.6	7.3
Other technical provisions, EUR million	968	1,077	1,149	1,308	1,281	1,359
growth, %		11	7	14	-2	6
Assets covering technical provisions less assets covering mathematical provisions, EUR million	998	1,114	1,192	1,315	1,398	1,576
growth, %		12	7	10	6	13
Assets covering technical provisions less assets covering mathematical provisions / other technical provisions, %	103.0	103.5	103.7	100.5	109.1	116.0
Assets covering technical provisions less assets covering mathematical provisions / GDP, %	3.7	3.9	3.8	3.8	3.8	4.5

Sources: ISA, SORS, own calculations

Table 4.5: Selected indicators for compulsory and voluntary supplementary pension insurance

	2005	2006	2007	2008	2009	Growth, % 2005	2006	2007	2008	2009
	Compulsory pension insurance									
Average no. of policyholders at the PDII	845,643	857,922	879,090	904,084	894,886	1.1	1.5	2.5	2.8	-1.0
Average no. of pensioners[1]	531,075	536,887	543,473	551,258	560,428	1.4	1.1	1.2	1.4	1.7
Ratio	1.59	1.60	1.62	1.64	1.60	-0.3	0.4	1.2	1.4	-2.6
Average pension, EUR[2]	461	484	512	554	570	3.1	4.9	5.7	8.3	2.9
Average net wage, EUR	736	773	835	900	930	6.2	5.1	7.9	7.8	3.4
Ratio	0.63	0.63	0.61	0.62	0.61	-2.8	-0.2	-2.0	0.5	-0.5
Average age of new pension recipients	58.8	58.9	59.2	59.2	59.5	0.4	0.2	0.5	0.0	0.6
men	60.4	60.3	60.7	60.8	60.9	-0.3	-0.1	0.6	0.1	0.3
women	57.1	57.2	57.4	57.5	58.0	0.9	0.1	0.4	0.2	0.9
	Voluntary supplementary pension insurance									
No. of voluntary supplementary pension insurance policyholders	427,645	459,764	486,816	512,343	482,988	5.6	7.5	5.9	5.2	-5.7
Workforce in employment	813,558	833,016	864,361	880,252	844,655	0.8	2.4	3.8	1.8	-4.0
Ratio	0.53	0.55	0.56	0.58	0.57	4.8	5.0	2.0	3.3	-1.8
Assets, EUR million	592	783	956	1,212	1,528	48.7	32.3	22.0	26.9	26.1
assets as % of GDP	2.1	2.5	2.8	3.3	4.4	40.0	22.5	9.6	18.1	34.1
assets as % of household financial assets	2.1	2.5	2.6	3.3	3.9	38.0	16.4	3.5	28.1	18.0
Written premium, EUR million	182	202	217	240	231	2.0	10.6	7.8	10.3	-3.6
premium as % of PDII tax revenues	7.2	7.5	7.5	7.4	7.0	-3.9	5.5	-0.7	-1.6	-4.7

Notes: [1] Includes recipients of all types of pension: old-age, disability, family, widow's, military, farmer's, state.
[2] Includes old-age, disability, family and widow's pensions, less tax prepayment.

Sources: PDII, ISA, SMA, SORS, Bank of Slovenia

5. Investment funds

Table 5.1: Overview of investment funds: assets and net inflows of mutual funds in EUR million and year-on-year returns in percentages

	Mutual funds				(Authorised) investment companies – Assets				Investment funds (total)	
	Net inflows	Assets		AUP	PIDs		ICs		Assets	
	EUR million	EUR million	Growth	Growth	EUR million	Growth	EUR million	Growth	EUR million	Growth
2000	5	45	22%	4%	2,393	-4%	-	-	2,438	-
2001	7	61	37%	23%	2,287	-4%	-	-	2,348	-4%
2002	122	231	277%	54%	1,352	-41%	578	-	2,161	-8%
2003	107	389	68%	17%	550	-59%	894	55%	1,833	-15%
2004	339	877	126%	18%	-	-	1,209	35%	2,086	14%
2005	138	1,385	58%	7%	-	-	835	-31%	2,220	6%
2006	163	1,929	39%	19%	-	-	916	10%	2,845	28%
2007	470	2,924	52%	28%	-	-	1,213	32%	4,138	45%
2008	-304	1,513	-48%	-43%	-	-	398	-67%	1,912	-54%
2009	18	1,856	23%	24%	-	-	377	-5%	2,234	17%

Sources: AMC, SMA, LJSE, own calculations

Table 5.2: Assets of EU and Slovenian investment funds in EUR billion and in percentages

		Asset value	Annual growth	Breakdown by asset type, %				
		(EUR billion)	(%)	Equity	Bond	Balanced	Money-market	Other
EU	2005	5,170	23.3	39	25	14	18	4
	2006	5,974	15.1	41	23	15	16	5
	2007	6,203	4.2	40	22	15	16	7
	2008	4,593	-25.4	30	23	16	25	6
	2009	5,299	16.7	34	23	16	21	6
Slovenia	2005	1.4	57.9	58	2	40	0	0
	2006	1.9	39.3	63	1	35	0	0
	2007	2.9	51.3	63	2	33	1	0
	2008	1.5	-48.8	63	2	33	1	0
	2009	1.8	21.6	63	2	34	1	0

Sources: Bank of Slovenia, Eurostat

Table 5.3: Mutual funds: number, assets and net inflows in EUR million and returns in percentages

	2005	2006	2007	2008	2009	Growth, % 2005	2006	2007	2008	2009
Number										
overall	50	99	109	127	128	51.5	98.0	10.1	16.5	0.8
equity	26	72	80	96	98	116.7	176.9	11.1	20.0	2.1
bond	9	9	10	10	10	28.6	0.0	11.1	0.0	0.0
balanced	14	16	17	18	17	0.0	14.3	6.3	5.9	-5.6
money-market	1	2	2	2	2	-	-	0.0	0.0	0.0
other	-	-	-	1	1	-	-	-	-	0.0
Assets										
domestic mutual funds, EUR million	1,385	1,929	2,924	1,513	1,856	57.9	39.3	51.6	-48.2	22.7
equity, % of total	53	58	68	63	63	85.4	9.6	17.7	-6.8	0.0
bond, % of total	4	2	1	2	2	-18.6	-45.3	-47.4	78.6	-0.4
balanced, % of total	43	40	31	33	34	-35.5	-7.4	-23.0	9.4	1.0
bank, % of total	25	30	28	33	39	-13.4	20.8	-6.5	20.1	15.2
non-bank, % of total	75	70	72	67	61	5.3	-6.8	2.7	-7.8	-7.6
foreign mutual funds, EUR million	137	308	367	130	189	-	119.8	19.4	-64.7	45.773
Net annual in flows										
domestic mutual funds, EUR million	138	163	470	-304	18	-59.1	18.1	187.3	-164.6	-106.01
equity, % of total	100	130	84	-200	66					
bond, % of total	8	-9	-1	-5	2					
balanced, % of total	-11	-23	16	-105	35					
bank, % of total	52	44	31	28	52					
non-bank, % of total	48	56	69	72	48					
foreign mutual funds, EUR million	97	127	2	-55	-7					
Annual growth in AUP, %										
overall	7	19	28	-43	39					
equity	11	20	32	-48	47					
bond	3	2	5	-3	12					
balanced	5	18	23	-38	28					
bank	10	15	19	-35	26					
non-bank	6	20	31	-46	23					

Note: The figures for foreign mutual funds only include those officially marketed in Slovenia.
Sources: SMA, own calculations

Table 5.4: Breakdown of investment fund investments by type in percentages

(%)	2005	2006	2007	2008	2009
Mutual funds					
shares	36	30	29	21	22
bonds	15	8	5	7	6
bank deposits	6	8	10	11	10
foreign investments	39	51	55	58	62
other	4	3	2	3	0

Source: SMA

6. Leasing companies

Table 6.1: Comparison of the Slovenian leasing sector with European leasing companies in percentages

(%)	2003	2004	2005	2006	2007	2008	2009
Slovenian leasing companies							
Growth in business	35.6	12.3	35.5	28.0	34.3	31.7	-46.4
Leasing business / gross investment	18.3	18.5	23.7	26.9	31.4	37.1	25.8
Breakdown of business							
real estate leasing	34.5	29.7	33.5	29.5	30.9	25.0	22.0
equipment leasing	65.5	70.3	66.4	70.5	69.1	75.0	78.0
equipment and real estate leasing by individuals	20.2	22.2	20.9	19.2	19.5	20.9	23.8
European leasing companies							
Growth in business	8.3	8.0	11.6	16.9	11.2	-1.6	-28.4
Leasing business / gross investment	14.6	14.8	15.9	19.0	20.8	16.0	-
Breakdown of business							
real estate leasing	16.6	16.2	17.1	15.5	13.7	10.9	-
equipment leasing	83.4	83.8	82.9	84.5	86.3	89.1	-

Note: The Leaseurope figures include all EU Member States with the exception of Luxembourg, Ireland, Lithuania, Cyprus and Malta, plus Norway, Russia, Switzerland and Serbia (the figures for 2008 are not yet available for the last two). Gross investment includes gross fixed capital formation other than investments in residential buildings for reason of comparability with the Leaseurope figures. The figure for growth in European leasing business for 2009 is provisional.

Sources: Leaseurope, SORS, BAS, SLA

7. Capital market

Slovenian capital market

Table 7.1: Overview of the regulated securities market in EUR million and in percentages

	Market capitalisation (EUR million)	Market capitalisation (as % GDP)	Volume (EUR million)	Volume (as % GDP)	Turnover velocity	Annual change in SBI TOP, %
2001	5,759	27.9	1,454	7.0	0.252	-
2002	9,073	39.2	2,007	8.7	0.221	-
2003	10,190	40.6	1,420	5.7	0.139	-
2004	12,726	47.0	1,655	6.1	0.130	29.3
2005	13,395	46.7	1,840	6.4	0.137	2.8
2006	18,838	60.8	1,805	5.8	0.096	56.57
2007	26,696	77.4	3,324	9.6	0.125	70.97
2008	15,488	41.7	1,286	3.5	0.083	-66.09
2009	19,668	55.4	904	2.5	0.046	15.03

Sources: LJSE, SORS

Table 7.2: Number of issuers and issued securities on the Ljubljana Stock Exchange and number of registered securities at the CSCC

	2005	2006	2007	2008	2009	2005	2006	2007	2008	2009
LJSE										
number of issuers	148	130	119	107	97	-25	-18	-11	-12	-10
number of issued securities	227	205	188	187	174	-27	-22	-17	-1	-13
shares	112	102	89	86	86	-30	-10	-13	-3	0
bonds	95	93	89	90	85	-6	-2	-4	1	-5
investment companies	10	7	7	4	4	-1	-3	0	-3	0
number of members	27	24	24	23	25	0	-3	0	-1	2
CSCC										
number of issuers	827	810	803	764	742	18	16	15	14	13
number of issued securities	1043	1026	995	943	912	22	20	19	20	19
shares	910	889	877	821	795	12	11	10	10	11
bonds	123	115	112	111	107	77	81	79	81	79
investment companies	10	7	7	4	4	100	100	100	100	100

Sources: LJSE, CSCC

Investments by residents in the rest of the world

Table 7.3: Investments by residents in securities issued in the rest of the world in EUR million and in percentages

	2005	2006	2007	2008	2009
Growth in investments in rest of the world, %	130.5	81.5	77.7	-21.6	7.8
Total investments in rest of the world, EUR million	3,027	5,495	9,767	7,655	8,256
	Breakdown by sector, %				
Banks	39	41	47	55	47
Other financial intermediaries	21	21	19	12	15
Insurers	19	18	17	24	27
Households	11	12	10	4	6
Corporates	5	4	3	1	2
Other	5	4	4	4	3

Sources: CSCC, Bank of Slovenia, own calculations

Investments by non-residents in Slovenia

Table 7.4: Investments by non-residents in securities issued in Slovenia in EUR million and in percentages

	2005	2006	2007	2008	2009
Growth in investments by non-residents, %	24.9	38.6	22	5	65
Total investments by non-residents, EUR million	3,000	4,129	5,054	5,295	8,855
	Breakdown by domestic sector, %				
Corporates	57	52	55	36	21
Banks	25	24	26	29	18
Other financial intermediaries	1	0	1	3	1
Insurers	2	2	2	2	2
Government	16	22	16	30	58

Sources: CSCC, Bank of Slovenia, own calculations