

BANK OF ALBANIA

BANKING SUPERVISION

ANNUAL REPORT 2003

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<p>The financial entities, not licensed by the Bank of Albania for conducting their activities pursuant to the Bank of Albania Supervisory Council Decision No. 26, dated 29.03.2000, "On exemption of some entities from the application of the provisions of Law No. 8365, dated 02.07.1998, "On banks in the Republic of Albania", are:</p>	
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I. PREFACE

Dear reader,

During 2003 the Supervision Department - an integral part of the Bank of Albania - aimed at fulfilling its mission of monitoring the banking system performance in order to maintain its stability.

The year we left behind marked structural and institutional developments in our department, and they had a positive impact on upgrading information flow, communication within and outside the department, professionalism and ethics during work process, improving supervision, on-site and off-site inspection skills, the legal framework and the supervising capacities in general.

We are happy that the previous year marked quantitative and qualitative developments in the country's banking industry. The banking system is now closer to the public through a greater presence of banks all over the country, a wider spectrum of banking services and satisfactory profitability. These positive developments are, first of all, the product of a serious commitment of the Albanian banking system in playing a vital role towards supporting the country's economic development.

We believe that supervision has played and plays a primary role in all these developments; it has been careful to warn ahead against unpleasant situations and trends in the banking system, encourage banks to implement useful identification and survey systems of transactions bearing significant perils in the daily activities so that the banking system can operate adequately. One of the priorities of our work has always been and remains the equilibrium between the banking business scope to augment its incomes and the need to identify and manage risks during our activity.

We assume that bank's governing structures, including the executive board and the audit committee, are now aware of the importance their commitment has and the responsibility they have in completing the framework of policies and procedures, as well as closely and continuously monitoring the bank's performance in order for the bank to have a safe daily business. What the managing structures in banks should strongly press on in their work is the identification, evaluation and management of risks that banks undertake in order to avoid financial difficulties and unexpected losses.

Finally, the banking system in Albania moved to a new and faster development phase with the privatization of the Savings Bank. The Bank of Albania and the Supervision Department aim at responding promptly to such developments in order to precede potential unwanted developments. Using this opportunity, I reinforce our commitment in this respect, and invite the whole banking industry to establish a stable and productive dialogue in order to upgrade relations among institutions in banking supervision. I invite the public to be more attentive to banking system developments, where we have invested our funds and savings. In this way, banking activity management would be more transparent and the responsibility of the system's actors would be bigger. Hoping towards a good banking activity performance this year, I thank you for your kind attention.

*Klodion Shehu
Director
Supervision Department*

Banking Supervision Mission

The banking supervisory function is exercised by the Bank of Albania, the central bank of the country, according to the Law “On the Bank of Albania”, No. 8269, dated 23.12.1997 and Law “On the banking system in the Republic of Albania”, No. 8365, dated 02.07.1998.

Banking supervision mission means exercising a careful, continuous and independent supervision on all financial institutions licensed by the Bank of Albania, so as to guarantee the progress of their business. Banking supervision represents a unique and anticipatory role with regard to problems that may emerge in the institutions licensed by the Bank of Albania in order to prevent these problems from becoming a potential threat to the financial industry and especially to the banking system stability. If such a thing happened, inter alia, the public image and reputation of these institutions, as well as that of the Bank of Albania, would be damaged, bearing negative impacts on the soundness and growth of the Albanian economy.

In compliance with its mission, the Bank of Albania being the supervisory authority of banks and other financial entities licensed by it, intends to:

- Ensure a sound banking activity that is in good harmony with the Bank of Albania laws, rules and regulations in order to prevent financial crises.
- Safeguard the banking system stability by monitoring and recommending adequate measures for the administration of banks, as well as by putting out of market mismanaged banks that do not offer qualitative, on-license banking services.
- Safeguard and strengthen banking system credibility, promote a trustworthy administration and take care of the depositors' and shareholders' assets.
- Contribute to the enhancement of the banking system transparency by enforcing the market discipline and intensifying the public pressure on banks.
- Provide a fair competition in the banking system and beyond, and ensure equal treatment of entities licensed by the Bank of Albania including their clients, too.
- Contribute in establishing an efficient banking system that would supply the public needs of a high quality service at a reasonable cost.
- Regulate the banking system activity by implementing policies and a legal framework in compliance with the best international standards and practices, and with the country's specific conditions, too.
- Undertake necessary steps in avoiding the criminal activities throughout the banking system (money laundering, frauds, etc.), co-operating with respective state authorities in the case being.

Principles of the Bank of Albania mission as a supervisory authority

The Bank of Albania, in compliance with its main objective, encourages the protection of settlement, liquidity and normal functioning of the banking system relying on market economy. The scope of the Bank of Albania mission - as a supervisory authority - is based on certain principles, which include:

- Establishment and continuous improvement of the supervisory regulative framework, which does not affect competition terms and does not discriminate financial institutions under supervision, is in harmony with the best international principles, and applicable;
- Implementation of policies targeting a development-oriented banking system;
- Strict implementation of legal and regulative, professional and ethical requirements in licensing financial institutions and examining also their executive bodies and shareholders;

- Continuous supervision through on-site inspections and analysis of licensed institutions and identification of problems, undertaking corrective measures and observing their realization and impacts;
- Increase of transparency in activities exercised by licensed institutions.
- Co-operation with financial institutions under supervision and with supervisory authorities of other countries;
- Continuous enhancement of the Bank of Albania's supervisory capacities.

These principles are applied by the Supervision Department in the following aspects:

- a. Regulating the activity of commercial banks and other licensed institutions, as well as continuous supervision (banking regulation, inspection and analysis).

Banking regulation of commercial banks and licensed financial institutions aims at determining an equal field of activity for all the participants licensed by the Bank of Albania, establishing certain limits in reducing risk and a framework of specified indicators, which would assess the activity of these financial institutions. Thus, the correct implementation of the regulative framework is assessed through on-site inspections and off-site supervision of quantitative and qualitative indicators of the activity. The Supervision Department, in compliance with the authority given by respective laws, inspects every bank and foreign exchange bureau, every bank account and documents of banks and other on-license entities conducting banking activity.

- b. Supervising the entry of new banks and other non-bank financial institutions in the market (through the licensing process).

Based on the legal framework determined mainly (however, not only) by the Law "On the Bank of Albania" and the Law "On the banking system in the Republic of Albania", the Bank of Albania is exclusively responsible for licensing and supervising all banks in the Republic of Albania.

According to relevant by-laws and acts, the Bank of Albania has set minimum requirements on entities willing to apply for a license of a bank, non-bank, saving-crediting agency, etc.

Applications for license are examined based on the Law "On the banking system in the Republic of Albania", on transparent procedures, as well as on the international licensing practice and experience.

By observing the legal, operational, financial and administrative independence of banks, the Bank of Albania – in conformity with law – examines banks' applications and gives either preliminary approval or rejects demands on: termination of twinning agreements, additional financial activities, capital enlargement through non-liquid assets, capital diminution, repurchase of shares from the bank, appointment of one or more than one administrator, so that the bank unites, divides, merges or sells assets, etc.

- c. Examining and approving the executive bodies of banks and the continuous assessment of their role in the bank's performance;

This is a moment of paramount importance, since the bank's well-administering determines its performance. The supervision process, apart from establishing the main moral, professional and ethical criteria, recognizes the responsibility and merits of bank's administrators with regard to its performance, and it continuously assesses their banking activity.

- d. Supervising the bank and banking system financial performance (the process of banking and banking system analysis);

Financial performance indicators of a bank or banking system in general are continuously analyzed by the Supervision Department, through financial reports and indicators sent to the Bank of Albania. Based on the information provided, conclusions on different indicators performance are drawn, problems are identified and expectations are made on their future performance, as well as respective recommendations are given.

- e. Supervising the process of taking actions on banks and other licensed financial institutions that create problems (from corrective actions to license revocation).

Financial institutions licensed by the Bank of Albania, which pose problems to themselves and/or the entire system (violation to the Bank of Albania's legislation, violation to license terms, to credibility, conducting unsafe and unstable activity, etc.), corrective actions are recommended pursuant to the legal and regulative framework. Penalties to the licensed financial institution and/or to the administrator are also provided for. This could go as far as putting the bank under custody for a certain period of time. If necessary, corrective actions could also include license revocation and its liquidation.

- f. Establishing co-operation and information exchange relations with financial institutions of the country.

In compliance with the supervision activity, co-operative relations are established with licensed financial institutions (executive bodies and their shareholders) and other financial institutions, the activity field of which is related to the financial institutions licensed by the Bank of Albania. Here are included government institutions, supervisory authorities of financial institutions not licensed by the Bank of Albania, certified accountant agencies, institutions supervising various instruments and their markets, etc.

- g. Establishing relations of co-operation and information exchange with supervisory authorities of other countries.

The Supervision Department, in compliance with its function, relies on the co-operation with the supervisory authorities of other countries, where head-companies of financial institutions, or branches or affiliates of banks and other financial institutions licensed to conduct their business activity in Albania, are established. This co-operation is institutionalized through understanding and co-operation memorandums (or other documents) between respective authorities of the two countries.

- h. Enhancing supervisory capacities.

This is an ongoing principle of the banking supervision function. It is a process aiming at promoting human resources and enhancing their abilities in supervision. It enables also the adoption of the best supervisory practices of international standards.

2. BANKING ACTIVITY AND SUPERVISION

The activity of the financial and banking system in Albania takes place in an open economy, which is being more and more integrated into the European and world economy. Consequently, significant international developments – particularly the influential ones in international financial markets – are expected to bring about changes in our economy, as well as in financial markets and its actors. Under these conditions, it is important to follow and analyze them constantly in order to identify the developments that could bear negative impacts on our financial system, and take therefore adequate measures to protect it.

2.1 A few words about the economic climate in the USA, euro area and Albania

During 2003 the European Central Bank and the Federal Reserve pursued their easing monetary policy, encouraging thus the development of their economies.

Thus, the Fed cut the core interest rate in the June's meeting, bringing them down to the lowest level of the last 40 years, 1 per cent (versus 1.5 per cent at the beginning of the year). The cut of interest rates reflected the central bank's concern regarding deflationary risks in the American economy. However, the cut of interest rates along with underpinning fiscal policies gave their results in invigorating the American economy in the second half of the year, when it reached a 4 per cent growth.

During 2003 the European Central Bank cut the core interest rate in economy twice bringing it down to 2.00 per cent versus 2.75 per cent it was at the beginning of the year. The first cut was made in March (2.50 per cent) and in June (2.00 per cent) in order to spur the economic growth. However, the euro area economy marked again low growth rates. The quarterly growth rates were respectively 0.0 per cent, -0.1 percent, 0.4 per cent and 0.3 per cent.

In the fourth quarter of 2003, the euro area economic growth was below expectations of 0.4 per cent. The negative impact on the economic growth was the result of the reduction of net exports and a weak domestic demand. The economies of the main euro area countries had lower economic growth than expected. Thus, Germany's growth was only 0.2 per cent, France 0.5 per cent and Italy presented the same level of GDP as in the previous quarter.

Developments in the euro area and in the USA had their impact also on some developments of the banking system in Albania, in USD and euro interest rate policies, as well as on the exchange rates performance. The fall of interest rates in the most important areas of the world economy made the lending activity in foreign currency much more attractive. At the same time, the appreciation trend of lek exchange rate against USD and euro – this having reflected mainly the developments in international markets – gave negative impacts on the core capital of banks. In addition, the appreciation of lek influenced negatively the growth of total assets of the banking system, while most of the resources of the system are reflected in foreign currency.

The economic figures of 2003 in Albania reassured the economic growth and the realization of the main macroeconomic objectives. The real growth of the gross domestic product was 6 per cent or 1.3 per cent higher than in 2002. This growth is mainly attributed to the growth in construction, services and transport; however, figures in industry and agriculture remain quite modest.

By the end of December, inflation rate was 3.3 per cent, within the two-to-four per cent targeted range projected in the Bank of Albania's monetary program. Keeping these inflation rates suggests that there is a satisfactory equilibrium between the Bank of Albania's monetary policy and the fiscal policy applied by the government of Republic of Albania. Inflation trends and their forecasts in economy, as well as the necessity to maintain the country's financial stability, led to a smoother monetary policy in 2003. Hence, the Bank of Albania cut several times the core interest rate by 0.5 percentage point, respectively in April, July, October and December, bringing thus the core interest rate (interest rate being applied to Repo auctions) to 6.5 per cent by the end of the year.

In 2003 the domestic currency was featured by an appreciation trend versus the two main currencies. This was rather stronger by the second half of the year, respectively 3.8 per cent versus euro and 7.8 per cent versus USD.

Incomes and current expenditures soared in the foreign sector due to a growing activity of this sector. Although the current account reached a deficit of 6.7 per cent of GDP or 2 percentage points lower than the one of 2002, it marked however an increase of this deficit in absolute terms. This is grounded on the rise of consumption of the Albanian economy; it dictates the need

to increase the production and competition capacities. Nevertheless, there is an overall positive position of the balance of payments and a rising level of foreign reserves, which reached USD 1 million by the end of the year.

2.2 Banking system analysis

The banking market presented significant developments during 2003, well-supported by a good macroeconomic environment. The entry of two new banks and the Savings Bank's privatization from a strong investor in the Central and East Europe, set the ground for a higher productivity and competition in the system.

2.2.1. Banking system assets, their structure and quality.

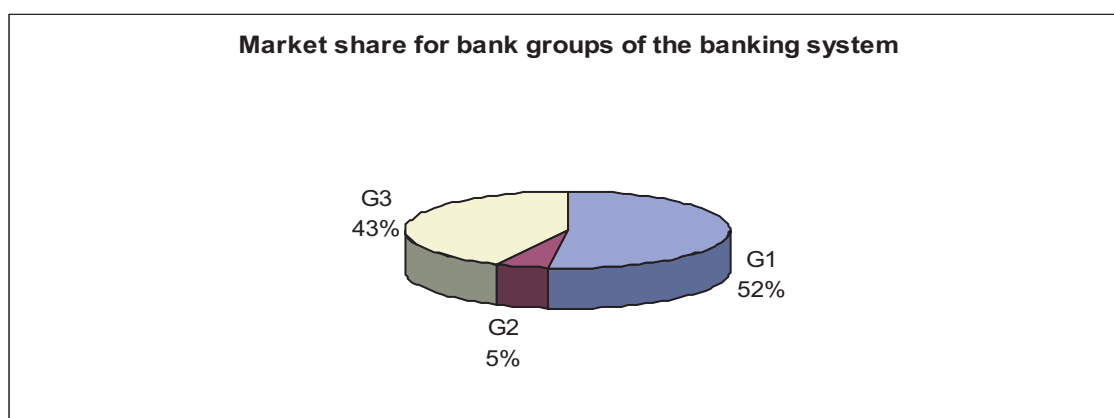
Total assets of the banking system totaled up to lek 34.3 billion or 10.1 per cent compared to the end of 2002. This growth is attributed not only to the "treasury and interbank transactions" but also to the "lending activity", as well as to "investments in Treasury Bills". "Treasury and interbank transactions" increased by lek 12.3 billion. "Lending activity" increased by lek 11.9 billion, whereas "investments in Treasury Bills" increased by lek 3.4 billion. The higher contribution of the last two items shows that banking transactions are expanding towards more effective activities.

Table 1. Total assets, its trend in years

Indicator in billion Lek	December '99	December '00	December '01	December '02	December '03
Total assets	249.5	270.8	318.5	339.3	373.6
In % of the GDP	49.2	50.2	53.5	51.6	50.2 ¹

In the analysis as to the bank groups of the system², compared to the end of 2002, the state-owned capital banks group (G1) marked a rise of about lek 10.4 billion of total assets; the group of banks of joint capital (G2) had a rise of lek 0.86 billion and the group of banks of private capital (G3) had a rise of lek 23.1 billion. The satisfactory growth of the private banks group, the growth of which surpasses twice as much that of the two other groups, shows the private management efficiency even in the banking industry.

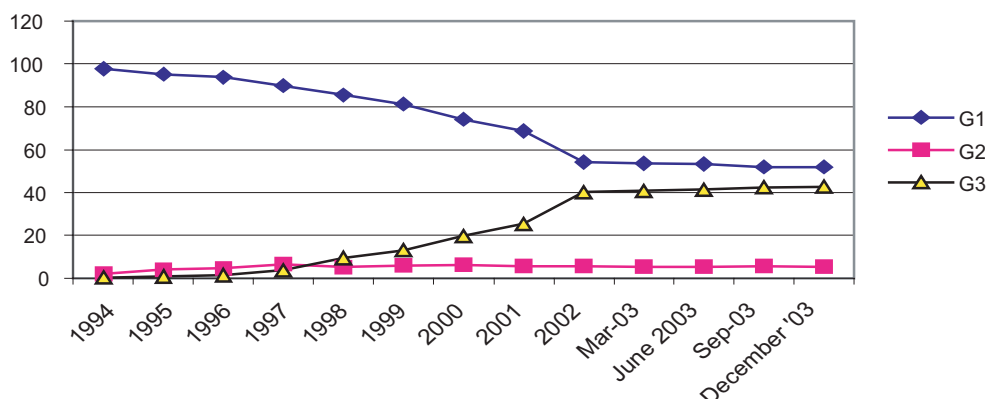
**Chart 1 Market share for bank groups of the banking system, by the end of '03
(according to total assets).)**



¹ The lower weight is explained through the application of the new calculating method of the estimated GDP.

² While the privatization of the Savings Bank is now *de facto*, its capital is still state-owned and *de jure* under transfer process.

**Chart 2 Market share for bank groups of the banking system, over the years
(according to total assets)**



The above graphic affirms the downward trend of the G1 weight in the market, the positive performance of the G3 and the static situation of the joint capital banks group. Year 2003 brought even closer to comparative levels the G1 and G3 respective weights. The Savings Bank's privatization is expected to enhance competition in the market; however, its impacts on the banking system structure are difficult to forecast. If other small-size banks do not find other ways to rapidly expand their activity, they will encounter significant hardships, which might lead to even lower weights.

2.2.2 Assets structure

The assets structure, as to the main items was, presented as follows by the end of 2003:

"Treasury and interbank transfers" show since the beginning of 2002 a lower growth rate than the one of total assets, which explains their downward weight. Although there was an increase of 4.5 per cent in 2003, much higher than the increase of 0.3 per cent in 2002, the downward trend of its weight versus the total assets, reflects an expansion of the banking industry and portfolio diversification.

"Dealings with central bank" item shows an irregular trend with regard to change momentum. In 2001 this item increased by 12.2 per cent; in 2002 it dropped by 5.1 per cent, whereas in 2003 it toted up by 9.9 per cent. Nevertheless, its weight versus the total assets has been kept at the same level of 8.7 per cent in the two last years.

"Treasury Bills investments" item continues to keep a significant weight in the assets structure of banking system, of about 49.6 per cent. However, this indicator has been going downward since its growth rate is lower than total assets growth.

"Dealings with other banks" item represents mainly the settlement of banks into other banks. The expansion of the banking system towards other prospects (lending and Treasury Bills investments) was followed by the fall of its weight versus total assets.

Lending³, despite its limited weight (only 13.5 per cent of the total assets) represents a growing activity in the Albanian banking system (30.7 percentage points versus the end of 2002).

"Operations with securities" are ever more important in the assets structure of banking system. There were about 7 banks having such a portfolio by the end of 2003, from 3 they were in the previous year. Worth mentioning is that two-year government bonds play a significant role in widening this portfolio.

³ In table 2, it matches the item "Operations with clients"

Table 2 . Main items trend of the banking system assets

Indicators (in Lek billion):	December 2000		December 2001			December 2002			December 2003		
	Amount	Weight	Amount*	Weight**	Difference**	Amount	Weight	Difference	Amount	Weight	Difference
1. Interbank operations and with the treasury. From these:	239.5	88.4	272.9	85.7	13.9	273.6	80.6	0.3	286	76.5	4.5
- Central bank dealings	27.9	10.3	31.3	9.8	12.2	29.7	8.7	-5.1	32.6	8.7	9.9
- Treasury bills	150.2	55.5	164.6	51.7	9.6	174.9	51.6	6.3	185.4	49.6	5.9
- Dealings with other banks	55.8	20.6	59.9	18.8	7.3	62.1	18.3	3.7	60.4	16.2	-2.8
2. Operations with clients (gross)	28.2	10.4	28.3	8.9	0.4	38.7	11.4	36.7	50.6 ⁴	13.5	30.7
3. Operations with securities	7.7	2.9	10.6	3.3	37.7	16.9	5.0	59.4	20.3	5.4	20.1
4. Other assets	1.5	0.6	1.2	0.4	-20.0	3.2	0.9	166.7	3	0.8	-5.2
5. Fixed assets	5.1	1.9	5.6	1.8	9.8	6.4	1.9	14.3	5.7	1.5	-9.2
Total assets	270.8	100.0	318.5	100.0	17.6	339.3	100	6.5	373.6	100.0	10.1

* in Lek billion

** in percentage

*** in percentage

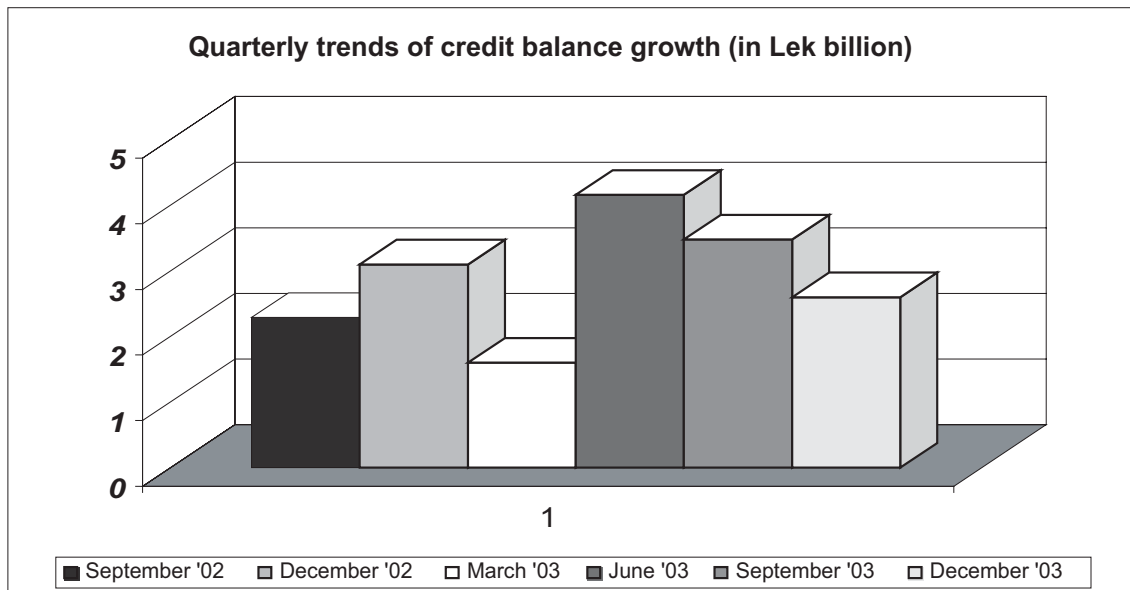
2.2.3 Lending activity

Compared to 2002, the new extended credit during 2003 mounted to lek 92.7 billion, or about 1.5 times higher, while the credit balance rose by lek 11.9 billion (or 30.5 per cent).

The weight of short-term loans has been going down since mid-term and long-term loans increased; however, extension rate of short-term loans remains still high.

The credit balance in lek has a lower weight versus the total credit, a performance that differs from that of 2002.

Chart 3 Gross credit balance, cumulative quarterly trend (in lek billion)



⁴ This is the gross credit balance without the calculated interests. Together with these latter ones, the gross credit balance was Lek 50.8 billion by the end of 2003.

Chart 4 Quarterly trends of credit balance growth

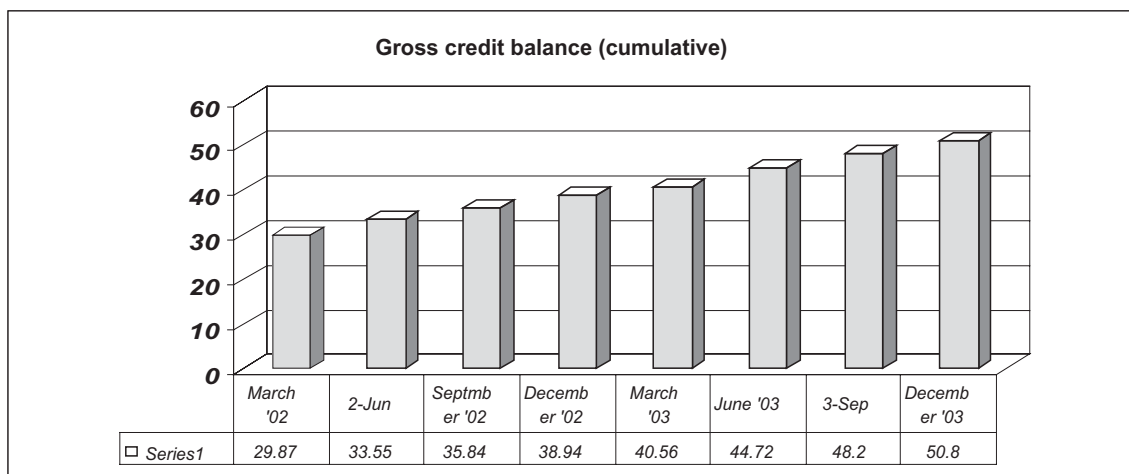
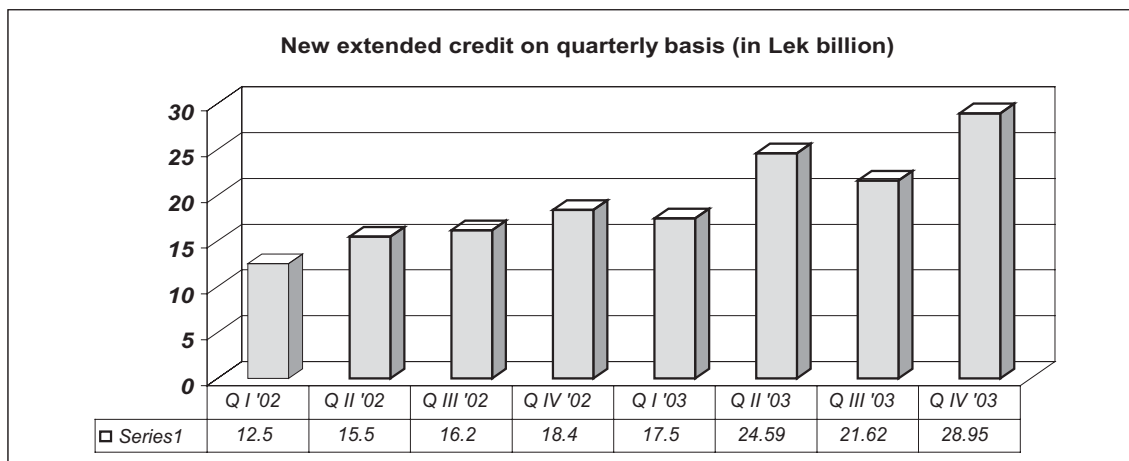


Chart 5 New extended credit from the banking system (in lek billion)



2.2.4 Assets quality

The indicator “bad loans/credit balance (gross), considered as the main indicator of the quality of this portfolio, was in a downward trend during 2003. The decline of this indicator is due to a lower growth rate of bad loans versus credit balance. Thus, credit balance increased by 30.5 per cent by the end of 2002; bad loans increased only by 8.2 per cent compared to the same period. The credit classification performance as presented in the following table, shows an enhanced portfolio quality by the end of 2003.

Table 2. Credit classification

Credit classification (in % versus credit balance).	First quarter '03.	Second quarter '03.	Third quarter '03.	Fourth quarter '03.
Standard credits	90.3	91.8	91.6	92.3
Special mention credits	3.6	3.0	3.2	3.1
Sub-standard credits	2.5	2.3	2.4	1.9
Doubtful credits	0.2	0.2	0.3	0.5
Lost credits	3.4	2.6	2.5	2.1

The indicator “bad loans/credit balance” on net basis⁵ shows the size of banking system exposure to credit risk. The low and declining values of this ratio indicate a generally limited exposure to this risk.

2.3 Deposits and current accounts

The level of funds from third parties – deposits and current accounts – in the overall/total funds of the banking system is 87.5 per cent from 84.6 it was by the end of 2002.

A stable growth of deposits was evidenced in 2003. Compared to the end of 2002, deposits increased by 14.7 per cent of lek 42.4 billion. We can say that the growth from 2001 to 2002 was quite modest, 4 per cent or lek 11.2 billion.

Table 3. Deposits and current accounts

Indicator in Lek billion	December 2002	March 2003	June 2003	September 2003	December 2003
Total deposits and current accounts	289.0	302.4	315.2	329.7	331.4

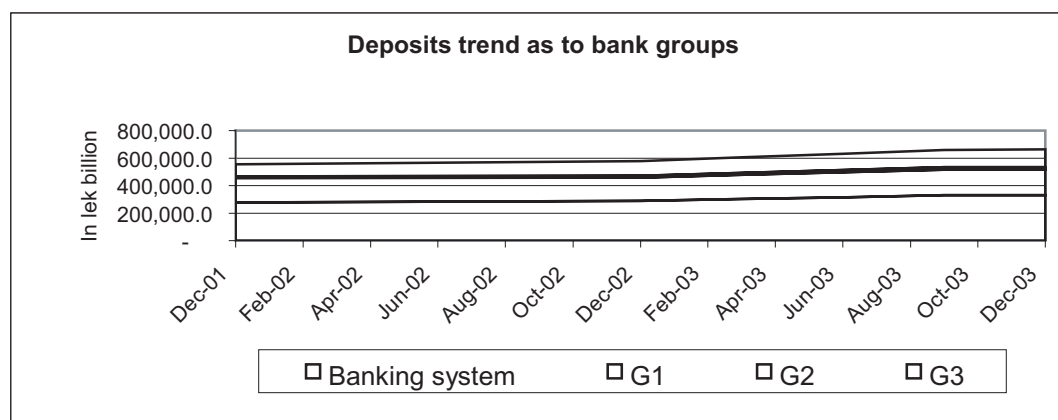
Private banks gave the biggest impact on the growth of deposits by lek 21.6 billion. The Savings Bank gave a contribution of about lek 18.9 billion; the contribution of banks with joint capital is still quite modest of about lek 2 billion.

The Savings Bank continues to hold the highest level of deposits, despite the rising contribution of private banks. Privatization of the Savings Banks, as the biggest bank with state-owned capital, though not expected to shake the level of its deposits, is expected to have a more efficient deposit investment.

Table 4. Depositing activity of the Savings Bank

Indicator in % versus the banking system	December 2001	December 2002	March 2003	June 2003	September 2003	December 2003
Total deposits and current accounts	63.7	58.3	58.1	58.0	56.5	56.5

Chart 6 Deposits trend as to bank groups



⁵ Having subtracted the provisions.

By the end of 2003, the structure of deposits was as follows: lek deposits 70 per cent, time deposits 82 per cent, households deposits 86 per cent. Analyzing the three bank groups in the system, the tendency is quite the same where a significant rise comes from time deposits and lek deposits from households. The cut of core interest rate from the Bank of Albania, despite its interaction in cutting the interest rate for lek deposits in the second half of the year, did not bring about the fall of deposits level. Actually, deposits in lek totted up by 15.7 per cent to lek 36.4 billion, whereas those in foreign currency only 6 per cent or lek 6 billion⁶. The growth of deposits in lek and foreign currency shows a consolidation of public confidence and a higher tendency towards depositing one's savings in the banking system.

Chart 7 Deposits trend in the system
Chart 7a. According to availability

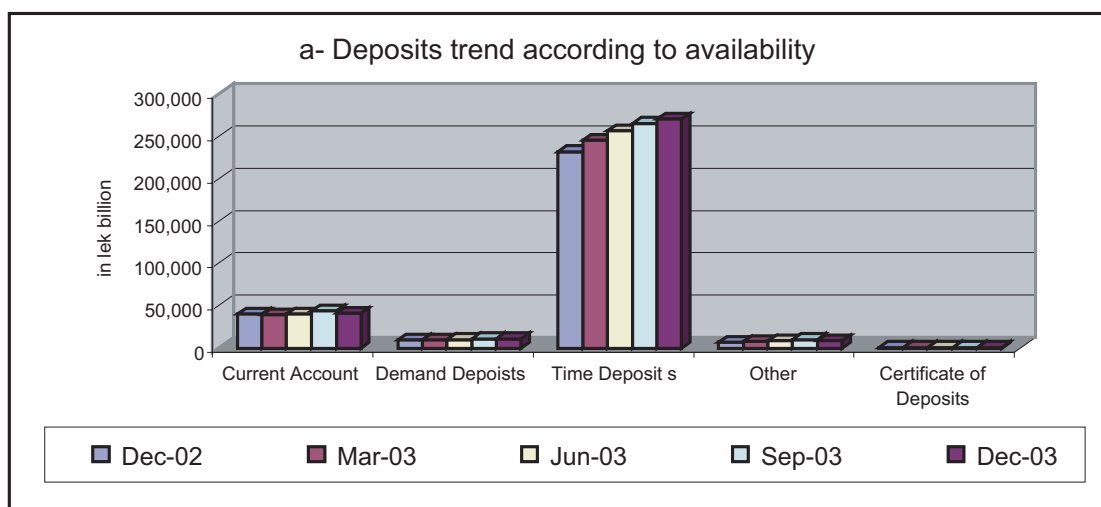
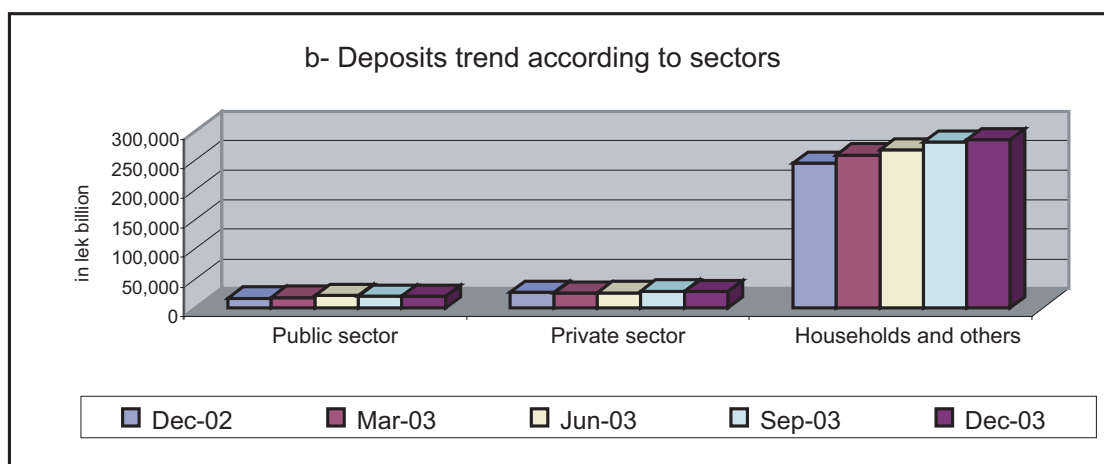
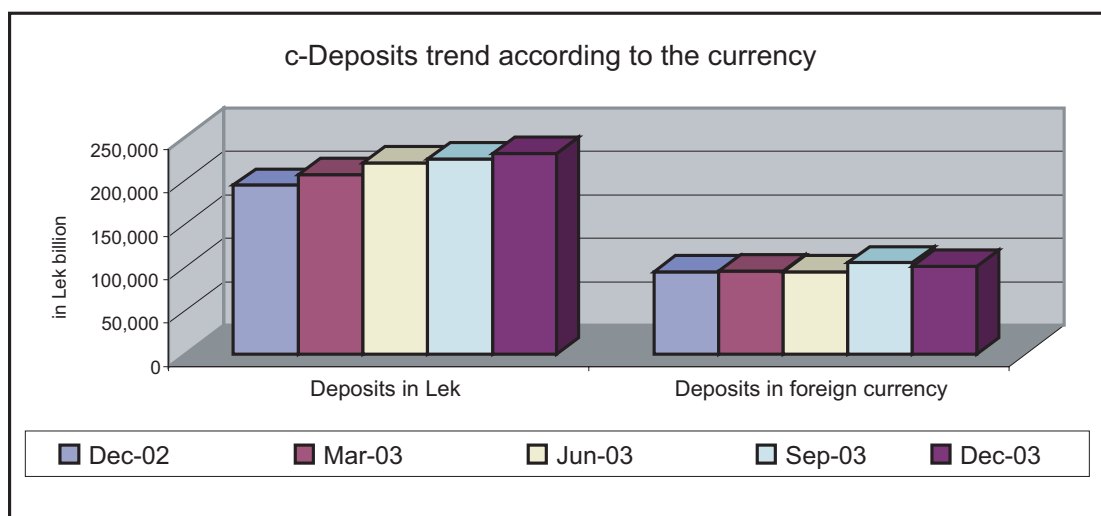


Chart 7b. According to sectors



⁶ Interest rates of deposits in euro and usd dropped over 2003 following their fall in international markets.

Chart 7c. According to the currency



2.4 Efficiency

The financial result of the banking system was positive and satisfactory by the end of 2003. Net incomes were about lek 4.45 billion or 0.6 per cent of GDP. Compared to the end of 2002, net incomes are lek 0.6 billion or 14.4 per cent higher (in real terms, this rise is estimated to be 11.4 per cent)⁷.

Table 5. Trend of financial incomes and expenditures, financial result

Indicator in Lek billion	December '99	December '00	December '01	December '02	December '03
Total incomes	39.1	31.0	29.2	28.0	32.0
Total expenditures	37.9	25.7	24.9	24.1	27.6
Net incomes (earnings)	1.2	5.3	4.3	3.9	4.4

Net incomes from the main activity of the banking system were lek 13.3 billion. Compared to the end of 2002, net incomes increased by lek 2.1 billion or 18.8 per cent. From these, 84 per cent belong to net incomes from interests, which still are the main contributors in net incomes. The rest comes mainly from commissions and foreign exchange.

Table 6. Trend of incomes and expenditures from the main activity, net incomes

Indicator in Lek billion	December '99	December '00	December '01	December '02	December '03
Incomes	37.5	27.0	26.1	26.9	31.1
Expenditures	31.1	17.1	15.0	15.7	17.8
Net incomes	6.4	9.9	11.1	11.2	13.3
Out of this : net incomes accrued	5.2	7.7	8.7	8.8	11.2

The general expenditures⁸ were lek 6.1 billion, that is lek 0.6 billion more than in 2002. Such an increase is due to the expansion of net banking investments, information technology systems, etc. Expenses on provisions fell by lek 155 billion.

⁷ The real decline (growth) is calculated: $1 + \text{nominal rate} = 1 + \text{real rate} + \text{inflation rate}$

⁸ General expenditures include expenses on: staff, business abroad, amortization and reserve fund for the devaluation of fixed assets.

Table 7. Efficiency ratio.

Indicator in Lek billion	December '99	December '00	December '01	December '02	December '03
General expenditures of the activity (1)	3.2	4.0	4.8	5.5	6.1
Gross incomes from the activity (2)	4.8	11.5	10.4	10.2	12.4
Efficiency ratio (1)/(2)*100	65.9	34.5	46.3	54.5	49.2 ⁹

The outcome of policies and bank management decisions is reflected in profitability indicators. The positive value of ROA of about 1.24 per cent shows the banking system ability to operate generally with profit; the high level of ROE of about 19.5 per cent shows the possibility of investments to rise. These indicators were within normal ranges¹⁰.

Table 8. Profit ratio over the years

Indicator in %	December '99	December '00	December '01	December '02	December '03
ROA*	0.5	2.1	1.5	1.2	1.24
ROE**	15.7	20.6	21.6	19.2	19.5

*Return on assets

**Return on equity

2.5 Capital adequacy

By the end of 2003, the system's shareholder capital was lek 22 billion, or lek 0.4 billion more than in 2002. A detailed analysis of its elements highlights their contribution.

Table 9. Structure of shareholder capital

	December	2001	December	2002	December	2003
Indicator	In Lek billion	in %	In Lek billion	in %	In Lek billion	In %
Shareholder capital	18,760.0	100.0	21,592.2	100.0	21,984.9	100.0
Paid-in capital ¹¹	14,052.2	74.3	14,516.6	65.6	18,512.3	69.3
Reserves	3,274.7	17.4	4,199.6	19.4	4,517.5	20.5
Re-estimation gaps	-117.7		-354.6		-3,285.8	
Retained earnings (loss) ¹²	88.8	0.5	536.7	2.5	-180.9	
Earnings (loss) in the current year	1,462.0	7.8	2,693.9	12.5	2,422.0	10.2

Paid-up capital, which constitutes the main element of the shareholder's capital, had a considerable growth of 27.5 per cent or about lek 4 billion¹³. This element is most influential in the shareholder's capital apart from earnings over the year. However, the re-estimation gaps due to USD depreciation versus lek had significant negative impact.¹⁴

Capital adequacy ratio¹⁵ was 28.5 per cent by the end of 2003, from 31.6 per cent it was in 2002. The level of regulatory capital and that of risk-classified assets rose respectively by 1.2 per cent (lek 207 billion) and 12.2 per cent (lek 6.8 billion). Precisely, the higher growth rates of risk-classified assets explain the fall of capital adequacy ratio.

⁹ The lower efficiency ratio is the result of a higher growth rate of incomes compared to expenditures.

¹⁰ The normal ROA range is considered 0.5 – 1.6 %; the ROE one is 10 – 20%.

¹¹ Weights in percentage of the paid-in capital are calculated by taking into consideration even the re-estimation gaps.

¹² The weight in percentage of the 2003 profit is calculated taking in consideration the retained loss of the previous year.

¹³ The augmentation of paid-in capital is due to the entrance of two new banks in the system, and the rise of the capital of some other banks.

¹⁴ Debit differences of capital re-assessment in 2003 had negative impacts on some of the banks, the core capital level of which was lower than the minimum required capital.

¹⁵ Capital adequacy ratio is the ratio of regulatory capital versus total assets average weighted with risk.

The capital adequacy ratio analysis as to bank groups shows a decline of the ratio in the private banks group and in the group of banks with joint capital, while the ratio is quite high in the Savings Bank. Hence, capital adequacy ratio in private banks is 24.4 per cent; 32.7 per cent in banks with joint capital and 54.9 per cent in state-owned capital banks. The high levels of capital adequacy indicators in the Savings Bank are expected to fall after privatization, since it will engage in lending and other investments activities.

Chart 8 Trend of regulatory capital, risk-classified assets and capital adequacy ratio

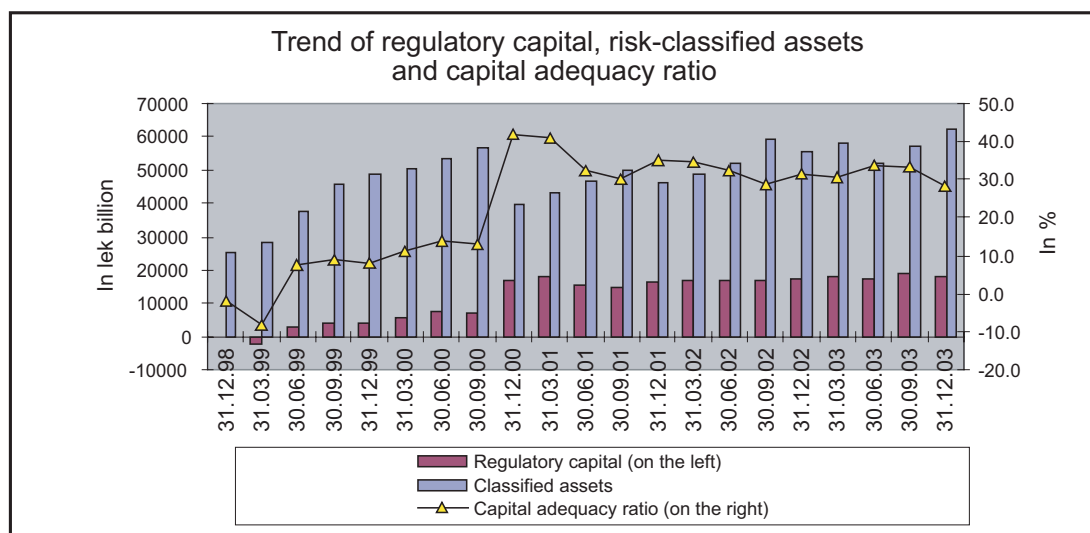
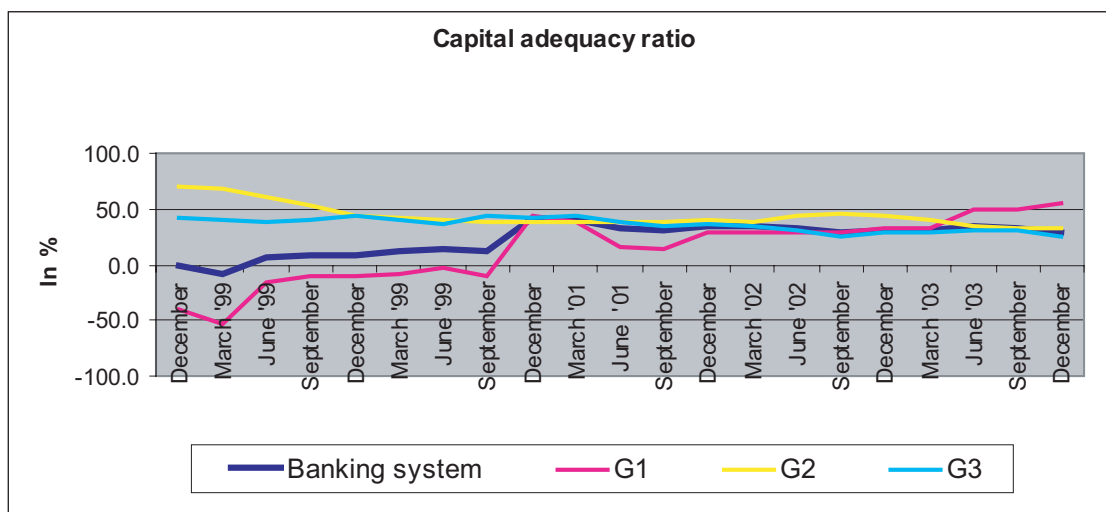


Chart 9 Capital adequacy ratio according to bank groups (in %)



The high levels of capital adequacy show that banks are capitalized. Although the levels of the core capital are below the minimum required levels, the shareholders are committed to make up for these differences in the future.

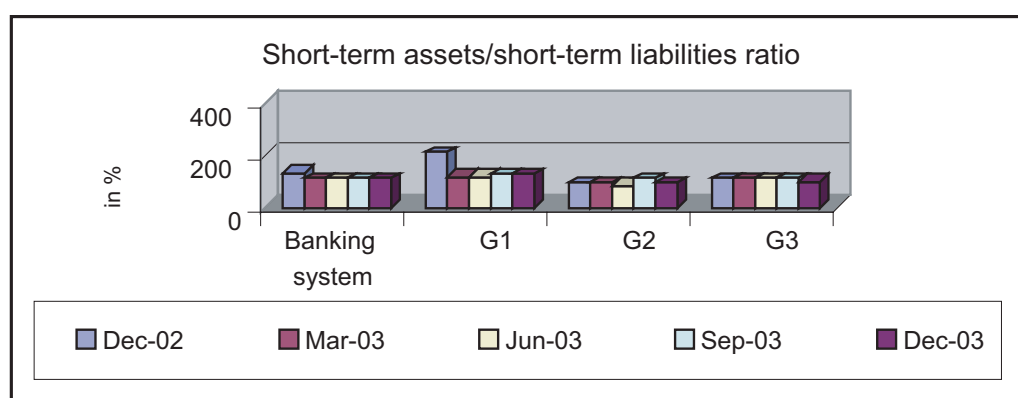
2.6 Liquidity

Liquidity analysis is based on the analysis of its main indicators¹⁶: liquidity, maturity gaps and credit/deposit ratio.

By the end of 2003, liquid assets ratio¹⁷ in total assets of the banking system resulted at a satisfactory level, over 30 per cent.

The above-mentioned indicator is backed up also by (2) the “short-term assets/short-term liabilities” ratio, which in the banking system resulted 107.1 per cent, or 25.8 percentage points lower than the end of 2002. This is considered a satisfactory indicator in the banking system, however in decline because of the high growth rates of short-term liabilities (26.4 per cent or lek 29.5 billion) compared to short-term assets (1.9 per cent or lek 2.8 billion).

Chart 10 Short-term assets/short-term liabilities ratio for the system and bank groups



Maturity gap between assets and liabilities of remaining maturity up to one-month shows considerable negative values in two banks of the system. However, thanks to the satisfactory level of their liquid assets, they are not exposed to liquidity risk.

Regarding the net credit balance/average deposits ratio - as an indirect indicator of the liquidity in the system – some banks were found to have a high level of credit/deposit ratio (over 70 per cent)¹⁸. Nevertheless, adequate capital levels were noticed in these banks, and no alarming indicators of credit portfolio quality were evident.

In a wider prospect, operative data on the interbank market and application of crediting facilities of the Bank of Albania suggest a system in liquidity surplus. The satisfactory levels of liquidity indicators do not expose the system and its banks to liquidity risk.

The above-mentioned indicators speak in general for a good situation from the financial indicators prospect in 2003.

¹⁶ These ratios are liquid assets versus total assets and short-term assets versus short-term liabilities.

¹⁷ Under “liquid assets” are included: monetary assets, dealings BoA-other accounts, treasury bills, dealings with banks, credit and other financial institutions and securities (net).

¹⁸ Following, licensed, financial institutions (LFI)

2.7 On-site examinations

The Bank of Albania is entitled by law to perform the role of a regulatory and supervisory institution of the Albanian banking system, a function that it has diligently carried out during 2003. Apart from the banking system, other financial institutions licensed by the Bank of Albania, such as non-bank financial institutions, saving-crediting agencies and foreign exchange bureaus have been consistently regulated and supervised¹⁹.

Supervision has been carried out through complete and/or partial inspections at licensed financial institutions (LFI), as well as through off-site analysis and examinations. Each bank is thoroughly inspected at least once a year. Partial inspections were constantly made on LFIs in order to assess the performance of their business activity, risk management, well-functioning of internal control system, etc.

The reporting system, through which banks report the main elements of their business activity to the Bank of Albania, is the main instrument of off-site analysis. Conclusions interesting the public on the banking system situation and the trend of its performance are drawn based on aggregation and analysis of these data.

The CAMELS system is employed in on-site examinations. It provides a qualitative analysis of some of the elements of the bank activity, including capital, assets quality, bank management, incomes, liquidity, sensitivity of payments balance items to interest rates and exchange rates mobility, etc. Based on these elements, this system provides an overall assessment of the bank's financial situation. According to this system, the overall financial situation of the banking system in the last year is considered "satisfactory", or ranked "2" (CAMELS ranking varies from "1", top performance, to "5", poor performance).

Compared to the overall average situation of 2002, it is observed the same ranking. However, some banks that ranked "1" in 2002, shifted to "2" in 2003. Some others have kept the same ranking but they shifted in separate elements of CAMELS, mainly in the negative direction.

The deterioration in these banks is due to some problems that might have been present even earlier. This shows that banking supervision is gaining ground, but at the same time it proves that management in some banks did not have the adequate insight and commitment to recognize and correct the weak points of their activity, and it did not show full seriousness in applying the recommendations given by the Bank of Albania.

During 2003, banks were quite active in expanding their network and activity through new branches. At the same time, there have been positive deployments in enhancing banking services and introducing new products. The positive outcome of such developments is expected to be even greater in the near future, since competition in the market is getting stronger.

The banking system performance throughout 2003 could be summarized as follows:

- Banking system earnings have been going upward, since their generation sources have been quite stable.
- Banking system assets have augmented being thus an indicator of public approach and the ability to find new financial sources. This growth was underpinned also by an aggressive marketing policy from banks, by expansion with new branches and agencies, and by technical, regulative and human infrastructure.
- Capital adequacy indicator is above the minimum level required by the Bank of Albania. However, in some banks this indicator is very high, indicating thus a conservatory policy and lack of efficiency in banking activity. Banks' shareholders expressed their commitment to raise the capital when necessary; however, their reaction must be faster and in due

¹⁹ In cases when the core capital was under the minimum paid-in capital, as to the level defined in the license.

course. We deem that bank management must provide a deeper insight to shareholders on the respective regulative framework and the importance of its comprehensive enforcement.

- Banks' administrators have been positive and responsible in regard to the objections and recommendations suggested in the examination reports. Nevertheless, there have been inadequate reactions, or weaknesses in diligently fulfilling the recommendations and orders given by the Bank of Albania, in compliance with the legal and regulative framework and principles on performing a safe banking activity.

Problems encountered by banks are briefly presented as follows:

- Diligent implementation of the Law "On banks in the Republic of Albania", regarding audit committee and its well-functioning, Albanian language usage, appointment of well-qualified persons in leading functions; completing credit files with all the required documentation, etc.
- Observance of the Bank of Albania's regulation "On credit risk management". In some banks, bad loans classification has not been made in conformity with the regulation, and consequently no provisions fund has been set up.
- Observance of the regulation "On foreign exchange activity", regarding relevant documentation to be attached to bank transfers.
- Completing and improving bank policies and procedures.
- Effective functioning of internal control and strengthening its independence.
- Enhancement of security elements in Technology Information systems, increasing security measures to prevent outside interventions, firewall locations, to control and filter information traffic, application of encryption on information not only during transmission but also during back-ups, back-ups at adequate frequency, design and implementation of a recovery plan in emergency situations, etc.
- Diligent implementation of regulative framework on preventing money laundering.

The Bank of Albania provided recommendations to each bank and set also respective deadlines. Administrative measures are often taken towards banks that have not fulfilled or solved identified deficiencies. Despite improvements, the Supervision Department should strengthen its surveillance capacities in order for the banks to follow and implement relevant recommendations given by the Bank of Albania.

We believe that in 2003 examinations quality and compilation of reports have improved because of a stronger hierarchy and greater responsibility not only within the On-site Examinations Office but also in the entire Supervision Department. Findings and draft-reports have been intensively discussed by examiners team, as part of the training process, and by division chiefs and the director and vice director of the department, especially in the second half of the year. In addition, a special attention has been given to the co-operation with certified accountants, aiming thus at a deeper insight on their reports, and especially on findings in "Management Letter". In the following year, this co-operation will focus on designing Co-operation Agreements with these institutions as well as with pre-established or occasional discussions on issues concerning both parties.

Of crucial importance in banking supervision, in examination and follow-up of recommendations in every bank, is co-operation among all structures of the Supervision Department, especially between On-site Examinations Office and Off-site Examinations and Analyses Office. Although co-operation exists, we believe that there is still a need to enhance mutual information exchange and debates.

In the past year, a great attention was given to strengthening human and professional capacities in the Supervision Department. Hence, the department is now under the direct dependence of

the Governor. Also, the structure of the department has changed, the number of personnel increased, internal training policies were complied, etc. We believe in the efficiency of all these measures which will soon lead to a better supervision by the Bank of Albania.

2.8. Changes and developments in legal and regulatory framework

2.8.1 Regulations

Changes effected in this direction were aimed at improving the existing regulatory framework in terms of applying the Basel Principles for an effective supervision and implementing the Development Plan of Supervision Department drafted in cooperation with the World Bank.

Aiming at their improvement, changes have taken place in the following regulatory acts:

- The Regulation “On certified experts of banks” approved with the Supervisory Council Decision No. 06, dated 29.01.2003, was changed with the Supervisory Council Decision No. 102, dated 10.12.2003. The changes aim at increasing the role of the Audit Committee on selecting the certified accounting experts and evaluating its report, defining the competencies for approval or refusal of certified accounting experts by the Bank of Albania, creating the possibility of the Bank of Albania to request from the certified accounting experts to audit and evaluate certain directions of the Bank’s activity where larger risk or inconsistencies are noticed, and requiring the experts to draft at any case the “Management Letter”, which shall be delivered also to banking supervision inspectors.
- The Guideline “On bank’s liquidity”, where the changes are intended to increase the flexibility of banks so that they calculate additional liquidity ratios and the accuracy of defining liquid assets.
- The Regulation “On licensing the savings-credit associations”, where the changes were imposed to precede the new tendency of micro-finance institutions for consolidation or transformation through merging. Such changes require licensing procedures in the event the savings-credit associations merge, thus creating a new association or a continuation of activity in an extended form in the event of an association being absorbed by another one.
- The Regulation “On licensing the non-bank financial institutions to conduct financial activity in the Republic of Albania”, where the changes have improved the stipulations on documentation and the way it is fulfilled, and have made accurate stipulations on the paid-up capital, when the entity requires to carry out more than one permitted activity. At the same time, the changes are intended to comply this Regulation with the Regulation “On granting a license to conduct banking business in the Republic of Albania”.
- The Regulation “On capital adequacy ratio”, where the change aimed at including explicitly all loans guaranteed by the EX-IM Bank of the United States of America into the items of the balance sheet weighed by a zero per cent coefficient, for purposes of capital adequacy.
- The Regulation “On foreign exchange operations”, where the changes aimed at gradually liberalizing the capital account operations, thus evolving in terms of fulfilling the obligations arising from Albania’s membership to World Trade Organization, and from the Association-Stability Agreement with the European Union. The substantive change has to do with omitting the restriction of the Bank of Albania’s preliminary approval on capital account operations and the assignment of the right, in this case, to the banks themselves to verify the documentation. Also, changes included the accuracy of documentation that should be filled in while carrying out the operations, and the clarification of some operations

- required by the regulation, based on its application in practice.
- The Regulation “On licensing the foreign exchange bureaus”, approved by the Supervisory Council Decision No. 65, dated 30.07.2003, which has derived from the previous guideline included in the old regulation “On foreign exchange operations”. The changes in this case were aimed at making the processing and fulfillment of documentation as accurate as possible. At the same time, the Regulation requires that an officer of the Security Division of the Bank of Albania shall also be employed in inspecting the foreign exchange bureau premises, as part of the process of granting a license.
- The Guideline “On reporting the foreign exchange operations”, where, for analytical and statistical purposes, the foreign exchange market operators, banks and exchange bureaus are required to report to the Bank of Albania on their foreign exchange operations. Therefore, a reporting system is also approved, being composed of some forms where reporting terms are stipulated.
- The Regulation “On requirements to be met by bank’s administrators” where the changes stipulated that the appointment of administrations, for whom preliminary approval by the Bank of Albania is needed, should be subject to requirements of the regulation. This regulation, unlike the previous one, prescribes the requirements with regard to reputation, education and experience needed for the persons that would become administrators of banks or foreign bank branches. This regulation solves even the problem of decision-making and auditing bodies for a foreign bank branch. Also, to the effect of preserving the decision-making and auditing independence of various bodies of the bank, some restrictions are defined regarding being an administrator in two or more than two leading and auditing bodies of the bank.
- Regulation “On bank’s relations with related persons”, which is drafted to supplement the regulatory framework. The purpose of drafting this regulation is to reduce the bank’s risk arising from conducting operations with related persons. The stipulation here takes into consideration relations with related persons to the effect of ownership and with its administrators. This regulation has also stipulated the limits of these relations regarding the extension of credit and other transactions. Related persons are considered as a sole counterparty and to prudent effect, their weighted coefficient is unified with the larger coefficient of each of them. The Regulation stipulates the supervision terms on the related persons and makes a differentiation in the event the related person is a bank. Such terms are adjusted with the supervision terms on large risks.

2.8.2 Licensing

Year in year out, the number of entities licensed by the Bank of Albania increased. During 2003 the Bank of Albania approved the granting of license to conduct banking business to “Credins Bank” Jnt.Stk, which is the first bank established by Albanian legal entities and individuals, a domestically owned bank. The Bank was established meeting the minimum capital required by the Bank of Albania to carry out banking business. It is licensed to conduct banking business according to first level of the license.

This development was followed by the application of another group of Albanian entrepreneurs to create a bank with fully Albanian private capital. After the examination of the application submitted by 23 shareholders, the Bank of Albania Supervisory Council approved the granting of preliminary license to the Popular Bank, Jnt.Stk.

During this year the Bank of Albania provided the consent for the opening of a branch outside the country, requested by the American Bank of Albania intending to receive a license for opening a branch of the bank in Athens, Greece, whereas the Savings Bank was given the consent to open a branch in Pristine.

Also, the number of non-bank institutions increased with two new entities “Albacredit Ltd.”, licensed to conduct services of payments and receipts and mediation in monetary transactions (including foreign currency), and “AK - Invest Jnt. Stk.”, licensed to conduct services of payments and receipts and mediation in monetary transactions (including foreign currency), as well as acting as an agent and financial advisor.

The number of savings-credit associations licensed by the Bank of Albania increased with 20 new associations, which are respectively members of the two existing unions of savings –credit associations, “Jehona” and “Albanian Union of Savings and Credit Associations”. At the same time, an association established as a separate association not included in the unions, was revoked the license, since the inspection revealed that this association had not conducted its activity in compliance with the license granted. At the end of 2003 the phenomenon of merging the savings-credit associations started to take place.

The number of foreign exchange bureaus licensed during 2003 was reduced, compared to 2002 during which 20 foreign exchange bureaus were licensed, due to some administrative actions taken by the state on the entities that operated without license at an informal market. During this year, three new foreign exchange bureaus were licensed, three other foreign exchange bureaus were revoked the license, and an agency of a foreign exchange bureau holding two such agencies was closed.

For the first time during 2003, pursuant to the Regulation “On granting a license to conduct banking business in the Republic of Albania”, the first license was given to a foreign bank, Popular Puglia Bank, to establish a representative office in Tirana. This representative office aims at studying the market and preparing for establishing a bank or a branch of this bank later on. According to the license, it is not permitted to this bank to conduct banking and financial activity.

Table 10. List of entities licensed by the Bank of Albania

No.	Entities	Year 2000	Year2001	Year 2002	Year 2003
1	Banks and foreign bank branches	13	13	14	15
2	Non-bank financial institutions	2	4	5	7
3	Foreign exchange bureaus	19	38	57	57
4	Savings-Credit Associations			113	131
5	Unions of Savings – Credit Associations			2	2

During 2003 the consent was given for changes in some banks’ names. So, the Arab Albanian Islamic Bank changed its name into United Bank of Albania, FEFAD Bank changed its name into “ProCredit” Bank, and Commercial Bank of Greece (Albania) is still under the process of changing its name into EMPORIKI Bank.

For the first time during 2003, the Bank of Albania approved “Bank Licensing Principles”, as an important document on the licensing process of banks. This document stipulates the main principles of this process, including the equal right for application, equal treatment of applications, preserving of public confidence, protection of competitiveness, transparency of decision-making and licensing process, etc.

3. IMPORTANT DEVELOPMENTS

3.1 The Savings Bank's privatization and expectations

The preparation and implementation of an action plan for the restructuring of the bank, during December 2002 - September 2003, drafted by the Ministry of Finance, intensified the privatization process of the Savings Bank.

This plan consisted in further developing the information and telecommunication of the bank, reducing the staff number and improving its quality, transferring fiscal services, restructuring the bank's network, improving the payment system, regionally extending the bank, reducing the bank's prevalence in the market and performing a better marketing about the bank's activity.

The Supervision Department has attended to the implementation of this plan in the process of supervision and has noticed that it has been applied with due attention by the Savings Bank and its leading bodies.

Pursuant to the privatization process of the Savings Bank and in order for the supervision to meet its main target, i.e., the maintenance of the financial system stability, the Supervision Department contributed to the campaign undertaken by the Bank of Albania for making the public aware of the importance of the Savings Bank's privatization, of the security and prosperity of the SB and of the whole banking system in the future. This purpose was carried out through direct contacts with the media and through publishing various relevant articles in the press.

After completing the above-mentioned process at the end of 2003, with the decision of the Council of Ministers of the Republic of Albania, the Savings Bank was privatized at a 100 per cent of the value of its shares. The new and the only owner of the bank, Raiffeisen Zentralbank, Austria, a financial group well-known to the European Union and distinguished for important investments in the banking sector of Central and Eastern European countries is expected to undertake all steps necessary for continuing the Savings Bank's restructuring, with a view to fostering the overall banking infrastructure.

Expectations

The Savings Bank's privatization is deemed to have important effects on the Albanian banking system. First, the new owner of the Savings Bank is expected to start the lending activity, of which this bank was restricted while it was a state-owned bank. The commitment to lending activity will be undertaken through establishing and organizing the necessary structures within the bank so that they might be able to carry out and monitor this activity, and be acquainted with the market in general. The bank may orient its lending by assigning a significant importance to lending in lek. The structure of its resources and the possibility of the bank to move faster towards lending, the potential of which is not made use of so far, may impose this.

Upon the release of considerable funds to lending, the banking system capacities will be raised to provide this service to customers, but at the same time the market competition will also be increased significantly. Some banks may try the competition by reducing the interests and profit margins, while some others may notice the customers alienate the banks. This growing pressure, in those banks where the audit systems and the framework of policies and procedures still need improvements, may be associated with the increasing risk that banks will be ready to take, thus requiring a closer and more prudent supervision.

The gradual passing to lending is not expected to bring about significant pressures on treasury bill interest rates, under the conditions when the new owner of the Savings Bank is expected to show the appropriate care in managing the portfolio of the Albanian Government's treasury bills being under its possession.

The new owner is expected to bring its own experience in the market development of new products, which are related mainly with the customer payment instruments. Other banks that are not active in this direction are expected to attend to these developments and establish their respective strategies.

The origin from a member country of European Union will have its own impact in bringing a new mentality into the market concerning the bank management, the so-called corporate governance. Wherever they go, the institutions of such magnitude decide such an organization of work that aims at implementing best standards in new investments. The policies of decision-making, transparency, staff organization, etc., aim at creating an efficient undertaking, thus creating confidence to customers. Soon these features are expected to be evidenced even at the Savings Bank and through it in the whole banking system. Simultaneously, the new owner is bringing the culture and the obligation to implement best international principles based on accounting and supervision international standards. According to the Directives of the European Union, the implementation of these standards is obligatory. This would be a very good experience for the whole banking system in Albania and for all the other operators in the financial area, under the conditions when the earliest implementation of these standards is required as a common target.

The Savings Bank's privatization would impact also on the way the monetary policy is carried out by the Bank of Albania, especially through fostering an important monetary (lending) transmission channel. In addition, the decisions made in monetary policy area should reflect to a larger extent the banking system expectations and its most important actors of macroeconomic developments. Only in this way, the decisions made may be entirely effective. So far, the efforts made by the Bank of Albania for considering the commercial banks' opinions in its decisions, as well as for orienting them in line with macroeconomic objectives are significant, but the banks' commitment in this respect, albeit increased, might have been even larger.

Important impacts are foreseen even on theoretical discussion and research about financial phenomena that may impact on the performance of the banking system and financial market in general. Institutions of such magnitude cannot be passive to economic events. On the contrary, they try to foresee and precede them through necessary operations. That is why their investments in terms of research are significant. Presently, the financial institutions and big private businesses in the world offer a more qualified economic opinion and frequently determine the trends through which a country's economy passes. This would be a very useful element for our banking system, where the public opposition of the private business and the banking sectors to economic decisions, or research work on our financial system tendencies and phenomena, should be much more active. Contribution to research area and study of the phenomena by the Savings Bank (already privatized), are expected to have an impact even on the growth of transparency for the country's economic developments, to regional and European economic-research centers. This is because such powerful financial groups possess the infrastructure necessary to present various economic data and build market opinions about them.

The privatization of the Savings Bank may be regarded as a successful event because it may be associated with the attraction of important foreign investors to Albanian economy. This is a common practice, when the entry of a well-known financial institution into a certain market serves as a catalyst to draw the attention of other investors towards this market. In this case the effects would be very positive and no long comments would be needed. The Savings Bank would presently be totally integrated into the international market, under the conditions when its owner represents a bank, a financial group with universal interests.

We deem that the Savings Bank's privatization is raising the quality of our banking system to a higher level. It represents, at the same time, an important challenge for the supervisory function of the Bank of Albania, particularly under the conditions when the products and instruments to be employed by banks will be complicated and increased. Thus, improvement of composition, raising

of staff quality, raising of training qualities, establishment of close links with supervisory authorities of the foreign countries the financial institutions come from, application of principles of consolidated supervision, etc., would be needed. The cooperation in these areas with the supervisory authorities of other financial institutions that operate in our country (for example, insurance companies), certified accounting experts, etc., is indispensability.

3.2 Preventing money laundering and terrorism financing

Year 2003 has marked some important developments in this direction, the most important of which is the changing of the Law “On money laundering prevention”, as well as other changes made to “Penal Code” and “Penal Procedure Code”. These changes were aimed mainly at extending the entities being subject to the Law “On Money Laundering Prevention” and at determining the activity of money laundering and terrorism financing as a penal offence. Further on, the obligation for confiscating tools and products that finance or derive from this penal offence are defined:

More specifically, the change of the Law “On Money laundering Prevention” consists in:

- Defining more clearly the “Money Laundering” term;
- Adding entities being subject to law, including non-profitable associations, construction associations, travel agencies, non-government associations, stock-exchange, National Privatization Agency, etc;
- Reducing the limit amount of transaction to be reported to the Responsible Authority from lek 70 million to lek 20 million.
- Setting a lower limit, by lek 200 thousand, on transactions of such entities as travel agencies, insurance associations and fortune games associations;
- Detailing the reporting of customs duties, banking and financial bodies;
- etc.

The changes in Law dictated necessary changes in the Bank of Albania Regulation “On Money Laundering Prevention”. The changing of the Regulation was based not only on the changes in law, but also on the remarks made by the Group of European Commission Experts on the fight against money laundering and terrorism, 40 recommendations of Financial Action Task Force (FATF) and 8 recommendations added currently to the effect of the fight against terrorism, and the Directive of the European Commission, No. 2001/97EC, changed with the directive No. 91/308/EEC “On preventing the use of financial system for money laundering”. The foreign assistance offered by the International Monetary Fund was also made use of changing the regulation.

This regulation, unlike the previous guideline, makes a better stipulation of:

- Cases when the customer identification should be effected;
- Types of documents that the customer should submit at any case to the bank for identification;
- Way of managing the documentation. Pursuant to Law, the identification shall be effected by means of the original documentation, while pursuant to the regulation, it should be photocopied, sealed by the bank and kept at the customer’s file;
- Cases of operating with an e-banking account;
- How does the bank proceed when suspicious transactions are identified;
- The bank’s internal procedures approved by the executive board regarding money laundering prevention;

- The role of the Bank of Albania as the supervisory authority for preventing money laundering;
- The requirement that reports on suspicious transactions should be sent not only to the Responsible Authority but also to the Bank of Albania;
- Some amendments are made to Annex I of the Regulation, involving even other activities not included before;
- A new annex is added (Annex 2), listing all types of transactions on which the banks should inform the Responsible Authority, etc.

Along with the legal and regulatory changes, a significant progress was marked even in terms of the whole process conception. A better dialogue exists between the Directorate of the Fight against Money Laundering and other institutions, which play the role of the supervisory authority on the entities of law. The cooperation between the supervisory authorities themselves is also enhanced. Numerous joint meetings and training courses have been organized, being aimed at clarifying the responsibilities and the exchange of experience. Information has been exchanged about certain entities of law.

However, we deem that much needs to be done yet in this direction. A more stable and open dialogue is needed to be held between the Responsible Authority and the supervisory authorities on the entities of law. This requirement is particularly real in the case of banks, which represent the entities of law with a better quality and quantity of reporting and cooperating in the framework of money laundering prevention. The Banks request a larger level of their participation in decision-making with regard to defining the regulatory framework of money laundering prevention, more accurate procedures wholly applicable in preserving the confidentiality of exchanged information, etc.

Pursuant to Law requirements, the Bank of Albania has conducted, through the Supervision Department, controls on entities licensed by the Bank in the framework of money laundering prevention. Such controls are part of the overall examinations in banks and other institutions licensed, or are considered as specific examinations. During such controls, assessment is based on the compliance of the bank's activity with the relevant legal and regulatory requirements, and the adequacy of the bank's structure that follows up the prevention of money laundering, various practices of payments and receivables are verified, the way of reporting of the entity to General Directorate of Money Laundering Prevention at the Ministry of Finance as the responsible authority is considered, etc. In cases when the findings are essential, they are made known to the responsible authority and special recommendations are stipulated for the bank. Generally speaking, the situation is presented as good, but inconsistencies are observed in terms of:

- Full reporting to the responsible authority;
- Accurate filling in of the relevant forms;
- Accurate definition of internal procedures of the entity regarding the drafting of relevant regulations or the assignment of responsible persons with the required hierarchy.

This notwithstanding, generally 2003 highlighted the indispensability for applying the legal and regulatory requirements for preventing money laundering and terrorism financing.

3.3 Development Plan of the Supervision Department

Since 2001, the Supervision Department has been committed to implement a development plan, which is designed in cooperation with the World Bank. The main object of this development plan is the standardization of the supervisory process and its procedures, the shifting of the

supervision into a continuous and proactive process and its orientation to risk identification, implementation of corrective actions and verification of their implementation.

The elements of this plan are extended in four main directions interacting between them, mentioning improvement of decision-making; transparency and communication; revising of the regulatory framework; and implementation of necessary instruments for monitoring and following up the implementation of recommendations.

Regarding the improvement of decision-making, some steps undertaken relate to:

- The accurate defining of decision-making competencies as far as concerns either the responsible unit or the object on which it is making decisions;
- Necessary structural changes, staff quality improvement, defining of training priorities, etc;
- Improvement of research process and necessary legal support, impacting on the quality of decision-making.

In terms of transparency and communication, this plan aims at:

- Better communicating within the departments and structures of the Bank of Albania on various decisions;
- Implementing the self-control program for unifying the supervisory standards used in examining the commercial banks;
- Establishing a stable communication bridge between banking supervision and banking industry, with the purpose to discuss the issues that may represent a threatening to the banking system stability in general and certain banks in particular, as well as to strengthen the capacities in terms of identifying the problems and causes of their existence;
- Establishing a stable communication bridge between banking supervision and other institutions that have supervisory and auditing functions on the financial system, inside and outside the country, aiming at regulating this communication with legal instruments and ensuring the exchange of information rapidly and making the first steps towards consolidated supervision;
- Enhancing transparency on the supervisory decisions, aiming at raising accountability within the supervision on reasons having motivated certain decisions and at the same time bringing to banks' attention their more acute problems that need immediate solution.

In terms of revision to regulatory framework through implementation of development plan requirements, it is aimed mainly at:

- Fulfillment of supervisory regulations under the conditions of introducing new products into the banking market;
- Revision to existing regulations to present the necessary changes when required by the level the banking system has reached at;
- Introduction of necessary regulatory and legal changes to bring our supervisory regulative framework as close as possible to international standards and Basel Committee principles;
- Introduction of necessary changes in the supervisory regulatory and legal framework to enhance its flexibility in treating specific supervisory issues and to better clarify the treatment of particular problems and the responsibilities of each party for its implementation.

Regarding the implementation of the required instruments for following up and applying the recommendations, work is done mainly in terms of:

- Making accurate the procedures for carrying out the banking supervision through on-site inspections and off-site analysis, as well as the cooperation between the units conducting the supervision;
- Stipulation of some documents and their drafting methodology to ensure constant follow-up of the bank as well as to orient the supervision to main risks the bank faces;
- Implementation of these requirements in practice.

During 2003, as well as previously, the Supervision Department has been committed to application of the requirements of this plan. With the purpose to attend and evaluate its performance, a continuous communication has existed between the Supervision Department and the World Bank, being materialized, inter alia, even through direct discussions in the framework of the missions authorized by the World Bank for this purpose. The orienting of discussions and the defining of the further platform to be developed has been based on the basic matrix of the work plan, aiming at a further qualitative improvement of practices, procedures, approaches and the materials compiled or being compiled, deriving from the requirements of this plan.

We regard the supervision development plan as a primary instrument in the quality improvement of banking supervision. During 2004 work will be done for implementing its main requirements in practice.

4. ISSUES REQUIRING SPECIAL ATTENTION AND CONCLUSIONS

We would highlight three main directions, in which we deem that the banks and their leading structures should give maximum attention.

Lending represents a primary direction of the banking activity, which has currently entered into its stable extension stage. This development is due to banks' sufficient experience in managing the banking activity, the social situation improvement in the country, the legislative improvements that regulate this activity, as well as an improved public culture for using effectively this banking service. This profitable direction of the banking system represents simultaneously even the main source of its risk, especially in the cases of focusing the business towards this activity.

We deem that the level of credit risk may be increasing due to some objective developments, including the strengthening of competition upon the Savings Bank's privatization and its commitment to lending, the large spaces for increasing the lending activity in the whole banking system, as well as the focusing of lending in foreign currency.

These developments may be transformed into a real risk on banks, if their leading structures do not fulfil the internal framework of policies and procedures duly and delay the establishment of structures needed to identify and evaluate the risk of this activity. In this regard, we deem that the banks should:

- Strengthen the units of their structure that are responsible for managing the lending process with staff and technological infrastructure;
- Subject the process of approving the lending to a vast discussion within the relevant structures of the bank, being prudential in decision-making;
- Improve their internal policies and procedures of managing the lending process, imposing the linking of credit to other banking services that strengthen the relation between the bank and the borrower and raise the degree of recognizing the credit risk;
- Strengthen the requirements for a close pursuit of the financial situation of the borrower, and apply rigorously the requirements for a periodic review of the credit portfolio quality by informing the higher leading structures on this;

- Strengthen the cooperation between them for exchanging information on certain borrowers, who are present in some banks, but without infringing the data confidentiality;
- Establish right ratios in the credit portfolio composition according to economy sectors, preserving the diversification of this portfolio;
- Establish right ratios between the lending activity and some other directions of banking business, preserving the diversification of their business and preventing the risk sources as much as possible;
- Observe rigorously the credit limits for a sole borrower or a group of related borrowers;
- Diversify the credit portfolio composition according to foreign currencies and maturity terms, taking into account the composition and structure of their sources.

We believe that the establishment of Credit Information Bureau, albeit in a not much advanced technological level, is a necessity on which the banking system has rising demands. The Bank of Albania, encouraging and supporting every effort made in this regard, deems that it is the due time for concrete developments in implementing projects undertaken by the Banks' Association. If there are problems delaying the implementation, it is necessary to make them known so that joint effective work takes place for their solution.

Given that the prevailing part of credit is extended in foreign currency by the banking system, the concern is growing on the performance of this credit under the conditions of unfavorable development of the exchange rate. Observing the limits for the open foreign currency position is an instrument which would protect against the effects of unfavorable developments of exchange rate in the balance sheet of banks. However, the exchange rate risk may be associated with the credit risk, when the borrower suffers from the exchange rate fluctuation, too. This is true when the incomes of the borrower are generated in a different monetary unit from that in which the credit is extended, which is depreciated. Therefore, we deem necessary that the bank should strengthen its procedures for deepening the financial analysis of the customer regarding income source and form of the source. We deem that the banks should create a specific database to this end, which, in turn, should serve its credit portfolio testing about the unfavorable fluctuations of exchange rate. At the same time, it may be necessary that security elements concerning the preserving of credit value in such cases be included in the loan contract.

The competition is a feature of the banking system expected to be significantly stronger due to the Savings Bank's privatization but even due to a better activation of other private banks in the market. Some banks may suffer more from this fact than the others would do. It has to do with small banks, which seek to expand their market share. Effects may be felt even in larger banks, particularly in terms of clientele movement. To be protected from the reduction of their market share, some banks may consider the extending of their network as a way out. If these decisions are taken hurriedly, except the effect on reduction of incomes of short-term activity, they could result even in non-effective investments in the longer run. Other banks may choose to be more risk-oriented, which, according to them, could help them to maintain the margin levels of profit and ensure their good performance in the future. In both cases, reduction of short-term incomes and an increased risk of their activity may take place in a number of banks. If these phenomena last, inter alia, this may be an indicator of "saturation" of the banking market, or the existence of a greater number of banks compared to the banking business potential currently offered by the Albanian banking system. We deem that in such a case other ways of strengthening certain banks should also be taken into account, mentioning merging between banks, purchasing of separate branches, etc. At the same time, the discouraging of the entry into the market of new banks, not expected to bring about special positive developments, may be necessary. As supervision, we will be closer to banks that may face difficulties in the short run so that problems they face are better identified and possible ways out are suggested.

The third element, on which we would require the bank's leading structures, including the executive board and the audit committee, to focus their attention is the adequacy of risk control and monitoring systems. It is time for the banks to treat rapidly and definitely some problems that may be encountered in terms of:

- Setting up a leading and operational structure, which totally ensures the independence of internal audit unit and the effectiveness of exercising its functioning, delegating the responsibilities according to abilities and competencies and preventing their concentration, defining the elements that ensure a supported decision-making and responsibility and accountability on such decisions, observing the ethical requirements in the customer relations, defining the links that ensure dual control on delicate activities of banks, etc;
- Relations with related persons and preventing of interest conflicts in selecting the leading structures;
- Establishment of specific structures for monitoring risks, particularly in terms of foreign exchange activities and securities investments. Here the separation of the functions of concluding agreements from the function of executing them is of importance. The control on the communication systems is of special importance, for example on SWIFT;
- Preserving of their information technology systems through implementing best security standards, documenting the way of use, may be preferential use and treatment of the relevant staff, duplicating and keeping the data in safe places, establishing plans for developing the bank's basic business under extraordinary conditions and their testing, etc.

It should be stressed that the senior management of the bank has the responsibility of applying these requirements. As supervision, we are going to try to play our role in making the bank's senior management aware as concerns the above, through direct communication and implementation of instruments provided by law. We will also try to reinforce their implementation.

Finally, we may conclude that the banking system situation during 2003 was stable. The financial result of the system was positive and increased in comparison with the past years. The banking system is capitalized well, while certain banks have experienced reduction of the base capital value under the minimum value required by the license level, mainly due to the appreciation of the lek exchange rate and business insolvency.

The Bank of Albania through the Supervision Department closely supervises the banking system. The supervision process has undergone improvements thanks to a better conceiving of the cooperation with the banking industry, and to the implementation of some steps provided in the framework of supervision development plan. However, these efforts should continue so as to be turned into an accepted supervision standard.

Establishment of a communication bridge between the banking industry and supervision is an indispensable element, which improves the supervision function by increasing the degree of comprehending various phenomena and by making banks and their management more responsible of the role they have in the final and stable solution of various problems.

This is the main element on which the efforts of the Supervision Department will be focused. We believe that there would be room even for other actors, such as external audit associations, supervisory institutions of other actors of financial market in the country, etc., in this regular communication line.

We have deemed to further treat a brief presentation of the new Basel Accord in this report, representing the new standard to which the new banking industry and supervision is moving.

Further on, discussions around this issue will be raised and enriched with the substantial contribution of the banking industry in the country.

5. OTHERS

5.1. New Basel Accord, preliminary assessment

The new Basel Accord on capital, known as Basel II, is an initiative of the Basel Committee launched in 1999, and it will take final form during 2004. The contribution rendered by banking business in improving this accord since its start is significant. Its main purpose consists in revising risks in the banking activity. In fact, the new accord is a consequence of advancement in information technology area, of the use of such systems in financial risk assessment, especially in banks and largest financial groups worldwide.

The new accord is designed into three main pillars:

Pillar I: Minimum capital requirement

In this light, the new accord has some changes from the existing one, mainly regarding the revision to credit risk and effects of its assessment on the bank's capital adequacy, as well as on the presentation of a supplementary requirement on capital attributed only to operational risk.

In a more detailed way, the material changes relating to credit risk have to do with:

- a) Omitting the concept "member state of OECD and non-member state of OECD", for assessing the credit risk of the debt of various countries or of companies coming from these countries;
- b) Supporting the international agencies of rating, such as Standard&Poor, Moody's, etc., for assessing the credit risk;
- c) Introducing a new category, which requires the weighting of some exposures with the purpose to assess the credit risk, with the coefficient of 150 per cent. This element is included in the Standardized Approach of Credit Risk Assessment, which is supposed to be applicable to the vast majority of banks. Alongside this approach, the new accord allows banks to use even their internal credit risk assessment approaches, and their adjustment is considered to be subject to evaluation by the supervisor (as part of stipulation in the second pillar).

The approach of credit risk assessment through internal assessment systems is deemed appropriate for the following main reasons:

First, the process of risk assessment is dynamic, always in process of development. Therefore, the new accord has created necessary space for adopting the changes in the future with respect to risk management approach by the banking industry. Hence, banks are given some possibilities to calculate capital requirements depending on their "appetite" to risk, thus increasing at the same time the degree of accord acceptance.

Second, to encourage banks to develop and refine techniques and internal risk management approaches, under the conditions when this may be associated with the reduction of the bank's capital requirements.

Therefore, it is understandable that the internal assessment approach is more applicable for a certain category of banks, which have made headway in investments and in the employment of information technology systems on risk assessment. Generally, they are strong and active banks in the international markets. The standard approach will be preferable for a category of banks which are less advanced in risk management techniques and are bound to be based on external risk assessments (for example, by rating companies).

Regarding the operational risk, the change presented in the new accord relates to the fact that the capital requirement for covering this risk will not be implied (included within the ratio of 8 per cent of adequacy), but it will be supplementary and calculated according to one of the approaches provided in the regulatory practice.

Pillar 2: Supervisory role

The substance of this pillar stands in the responsibility given to the supervisors for evaluating the suitability of the approaches used in risk assessment, the systems and quality of data included in the calculation. In this framework, not only the meeting of capital adequacy by the bank but also its ability to foresee and evaluate its own needs for additional capital, arising from its risk profile, will be evaluated.

This element is a real challenge in the supervisory function, since it requires the building of necessary human and financial capacities, so that appropriate level of banks' risk is acceptably achieved and necessary interventions are carried out to raise the capital level in accordance with the re-assessed risk profile.

Pillar 3: Market discipline.

Both the public and the market will play an important role in evaluating the adequacy of banks' capital. This pillar outlines the requirements for a larger transparency of the main risk elements and its management at banks, which would represent an important information to investors and competitors. This would provide a complete view of the bank's risk profile and would increase pressures on it for managing its risks prudentially. In a more general view, this development would raise the market discipline and would contribute to the overall financial stability.

Pursuant to this pillar, the type of information to be disclosed should meet some requirements, highlighting:

The information should be material, which according to International Accounting Standards means that omissions or misinterpretations of this information could change or influence the assessment or decision-making of its public user. Regarding this issue, given the difficulty, the Basel Committee did not set forth definitions or specific thresholds for classifying the information to be disclosed as material, believing that the "reasonable investor will be the one that will determine the necessary information and will impose an adequate level of transparency".

The information should not be confidential, since in such a case the disclosure may damage the competitive position of the bank and its relations with the customers.

According to this pillar, some ways of selecting the disclosure of information depending on its destination, administrators' judgement, type of information and various requirements of international standards are provided, IAS being the most important ones.

Also, this pillar provides orientation with regard to the frequency of reporting to public, which varies according to type of information. Definitely, the banks should have their own formal policies approved for the public disclosure of information and transparency, including the frequency of disclosure.

It is expected that the New Basel Accord requirements will be included and approved in the form of an European Directive, until mid 2005. If this is implemented, its requirements will become obligatory to all banks with headquarters in the European Union, as of year-start 2008.

In our country's case, implementation of the New Basel Accord requirements may result to be earlier than what is deemed at present. It may be imposed by the considerable presence of foreign capital investments to our banking system with origin from the European Union. Under such conditions, the recognition of its requirements by all the banks operating in the country and all other financial institutions interacting with the banking system is necessary.

The Bank of Albania has currently set up a work team to this end, intending to initiate a process of large discussion with the banking industry, for getting acquainted with the requirements of the New Basel Accord and its impacts on the banking system of the country.

6. ANNEXES*

6.1. Annex. I : List of entities licensed by the Bank of Albania

6.1.1 Banks and foreign bank branches

1. ITALIAN-ALBANIAN BANK

License No. 1/1996, dated 17.07.1998.

Approved with the Bank of Albania Supervisory Council Decision No. 89, dated 18.06.1998.

Certificate No. 1 "On deposit insurance".

Director: Adrian FULLANI

Address: Rruga "Barrikadave", No. 70, Tirana, Albania.

Tel: 04 23 56 97, 04 23 56 98, 04 22 62 62.

Fax: 04 23 30 34.

2. SAVINGS BANK

License No. 2/1998, dated 11.01.1999.

Approved with the Bank of Albania Supervisory Council Decision No. 163, dated 11.12.1998.

Certificate No. 2 "On deposit insurance".

Director: Steven GRUNERUD

Address: Rr. "Dëshmorët e 4 Shkurtit", No.6, Tirana, Albania

Tel: 04 22 45 40, 04 22 26 69, 04 22 54 16.

Fax: 04 22 35 87, 04 22 36 95, 04 22 40 51.

3. UNITED BANK OF ALBANIA Jnt. Stk.

License No. 3/1998, dated 11.01.1999.

Approved with the Bank of Albania Supervisory Council Decision No. 165, dated 11.12.1998.

Certificate No. 3 "On deposit insurance".

Director: Abdul Waheed ALAVI

Address: Bulevardi "Dëshmorët e Kombit", No. 8, Tirana, Albania.

Tel: 04 22 84 60, 04 223 873, 04 227 408.

Fax: 04 22 84 60, 04 228 387.

4. DARDANIA BANK

License No. 5/1998, dated 11.01.1999.

Approved with the Bank of Albania Supervisory Council Decision No. 164, dated 01.12.1998.

Certificate No. 4 "On deposit insurance".

Director: Beqir MEZELXHIU

Address: Bulevardi "Zogu I" (pranë Fakultetit të Shkencave), Tirana, Albania.

Tel: 04 22 87 59, 04 25 9350, 04 25 93 51.

Fax: 04 230-566.

Telex: 2298 db banc ab

E-mail: db@albaniaonline.net ; dardaniabank@hotmail.com .

5. NATIONAL COMMERCIAL BANK

License No. 6/1998, dated 11.01.1999.

Approved with the Bank of Albania Supervisory Council Decision No. 162, dated 11.01.1999.

Certificate No. 5 "On deposit insurance".

Director: Seyhan PENCAPLIGIL

Address: Bulevardi "Zhan Dark", Tirana, Albania

* Data as of July 2004.

Tel: 04 25 09 55.
Fax: 04 25 09 56.

6. TIRANA BANK

License No. 07, dated 12.09.1996.
Approved with the Bank of Albania Supervisory Council Decision No. 9, dated 12.09.1996.
Certificate No. 6 "On deposit insurance".
Director: Dimitris KARAVIAS
Address: Bulevardi "Zogu I", No. 55/I, Tirana, Albania.
Tel: 04 233 441, 42, 43, 44, 45, 46, 47.
Fax: 04 233 417.

7. BRANCH OF NATIONAL BANK OF GREECE IN TIRANA Jnt. Stk.

License No. 08, dated 25.11.1996
Approved with the Bank of Albania Supervisory Council Decision No. 4, dated 14.03.1996.
Certificate No. 7 "On deposit insurance".
Director: Spiro BRUMBULLI (Local Director)
Address: Drejtoria administrative: Rruga e Durrësit, Godina Comfort, Tirana, Albania
Tel: 04 233 623 / 4
Fax: 04 233 613

8. INTERNATIONAL COMMERCIAL BANK Jnt. Stk.

License No.09, dated 20.02.1997.
Approved with the Bank of Albania Supervisory Council Decision No. 9, dated 30.04.1996.
Certificate No. 8 "On deposit insurance".
Director: Lee CHONG PA
Address: Rr. "Ded Gjo Luli", Tirana, Albania.
Tel: 04 237 567, 04 237 568, 04 237 569.
Tel/Fax: 04 237 570.

9. BRANCH OF ALPHA BANK IN TIRANA

License No. 10, dated 07.01.1998.
Approved with the Bank of Albania Supervisory Council Decision No. 01/03/96, dated 27.12.1997.
Certificate No. 9 "On deposit insurance".
Director: Andrea GALATOULAS
Address: Bulevardi "Zogu I", No.47, Tirana, Albania.
Tel: 04 233 532, 04 233 359, 04 340 476, 04 340 477.
Tel/Fax: 04 232 102.

10. AMERICAN BANK OF ALBANIA

License No.11, dated 10.08.1998.
Approved with the Bank of Albania Supervisory Council Decision No. 105, dated 10.08.1998.
Certificate No. 10 "On deposit insurance".
Director: Lorenzo RONCARI
Address: Rruga "Ismail Qemali" No.27, P.O. Box 8319 – Tirana, Albania.
Tel: 04 348 753/4/5/6.
Tel/Fax: 04 348 762.

11. PROCREDIT BANK Jnt. Stk

License No. 12, dated 15.03.1999.
Approved with the Bank of Albania Supervisory Council Decision No. 22, dated 03.03.1999.

Certificate No. 11 "On deposit insurance".

Director: Jasper MENKEN

Address: Rruga "Sami Frashëri", Tirana e Re, P.O. Box. 2395,
Tirana, Albania.

Tel: 04 230 499, 04 233 496.

Tel/Fax: 04 233 481.

12. FIRST INVESTMENT BANK – BRANCH IN TIRANA, Jnt. Stk

License No. 13, dated 16.04.1999.

Approved with the Bank of Albania Supervisory Council Decision No. 45, dated 13.04.1999.

Certificate No. 12 "On deposit insurance".

Director: Petar Gavrillov KRASTEV

Address: Bulevardi "Zogu I", No. 64, Tirana, Albania.

Tel: 04 356 423, 04 356 424.

Tel/Fax: 04 356 422.

13. COMMERCIAL BANK OF GREECE (ALBANIA) Jnt. Stk.

License No. 14, dated 28.10.1999.

Approved with the Bank of Albania Supervisory Council Decision No. 105, dated 19.10.1999.

Certificate No. 13 "On deposit insurance".

Director: George CARACOSTAS

Address: Rruga "Kavajës", "Tirana Tower", Tirana, Albania.

Tel: 04 587 55, 56, 57, 58, 59, 60.

Tel/Fax: 04 587 52.

14. CREDIT BANK OF ALBANIA Jnt. Stk.

License No. 15, dated 28.08.2002.

Approved with the Bank of Albania Supervisory Council Decision No. 66, dated 28.08.2002.

Certificate No. 14 "On deposit insurance".

Director: Kamal Adbel Moneim

Address: Rruga "Perlat Rexhepi", Al-Kharafi Group Administration Building, Kati 1&2, Tirana,
Albania.

Tel: 04 272 168; 04 272 162.

Tel/Fax: 04 272 162.

E-mail: creditbkalb@icc-al.org

15. "CREDINS" BANK, TIRANA, Jnt. Stk.

License No. 16, dated 28.03.2003.

Approved with the Bank of Albania Supervisory Council Decision No. 22, dated 26.03.2003.

Certificate No. 15 "On deposit insurance".

Director: Artan SANTO

Address: Rruga "Ismail Qemali", No.21, Tirana, Albania.

Tel: 04 222916; 04 234096.

16. POPULAR BANK, TIRANA, Jnt. Stk.

License No. 17, dated 16.02.2004.

Approved with the Bank of Albania Supervisory Council Decision No. 06, dated 11.02.2004.

Certificate No. 16 "On deposit insurance".

Director: Edvin LIBOHOVA

Address: Rruga "Donika Kastrioti", Pall. 11/1, Kati 1, Tirana, Albania

Tel: 04 272 788; 04 272789.

6.1.2 NON-BANK ENTITIES

1. FINANCIAL UNION OF TIRANA LTD, (FUT)

License No. 1, dated 08.12.1999, for conducting the following financial activities:

- Providing payment and receivable services;
- Mediating in the conduct of monetary transactions;
- Acting as a financial agent or advisor.

Director: Niko Leka, Edmond Leka
Address: Rruga "Reshit Çollaku", Pall. "Shallvareve", sh.2, n.18,
Tirana, Albania.
Tel: 04 250 653.

2. DINERS CLUB ALBANIA LTD.

License No. 2, dated 09.10.2000, for conducting the following financial activity:

- Mediating in the conduct of monetary transactions.

Director: Vebi Velia
Address: Rruga Bulevardi "Zogu I", Qendra e Biznesit VEVE,
Tirana, Albania

3. ALBANIAN POST-OFFICE JNT. STK.

License No. 3, dated 18.04.2001, for conducting the following financial activities:

- Providing payment and receivable services;
- Acting as a financial agent or advisor.

Type: State-owned
Director: Aleksandra Çollaku
Address: Rruga "Reshit Çollaku", No. 4, Tirana, Albania.

4. "CREDINS" TIRANA JNT. STK.

License No. 04, dated 13.06.2001, for conducting the following financial activities:

- Extending credit;
- Providing payment and receivable services;
- Mediating in the conduct of monetary transactions (foreign currency included);
- Offering guarantees;

Acting as a financial agent or advisor (excluding herein the services set forth in points 3/a and 3/b of Article 26 of the Law "On banks in the Republic of Albania").

Director: Monika Milo
Address: Rruga "Ismail Qemali" No.21, Tirana, Albania.
Tel: 04 222916; 04 234096.

5."MOUNTAIN AREA FINANCING FUND".

License No. 5, dated 29. 03.2002, for conducting the following financial activity:

- Extending credit;

Founded on the Decision of the Council of Ministers of Republic of Albania.

Director: Arben Jorgji
Address: Rruga "Mustafa Matohiti" Vila No.12, Tirana, Albania
Tel: 04 250633.

6. "ALBACREDIT LTD."

License No. 6, dated 18.04.2003, for conducting the following financial activities:

- Providing payment and receivable services;
- Mediating in the conduct of monetary transactions (foreign currency included);

Manager: Ermira Skënderi
Address : Rruga "Ded Gjon Luli", No.5, Tirana, Albania
Tel.: 04 230 956.
Fax: 04 228 929.

7. "AK- INVEST JNT. STK."

License No. 7, dated 03.12.2003, for conducting the following financial activities:

- Providing payment and receivable services;
- Mediating in the conduct of monetary transactions (foreign currency included);
- Acting as a financial agent or advisor.

Shareholders: Ilir Adili
Muharrem Kokona
General Manager: Ilir Adili
Address: Rruga Ded Gjo Luli, No.2/3, Tirana.
Tel: 04 24 01 47.

The financial entities, not licensed by the Bank of Albania for conducting their activities pursuant to the Bank of Albania Supervisory Council Decision No. 26, dated 29.03.2000, “On exemption of some entities from the application of the provisions of Law No. 8365, dated 02.07.1998, “On banks in the Republic of Albania”, are:

1. Rural Financing Fund

Founded by the Decision of the Council of Ministers of Republic of Albania No. 207, dated 28.04.1999.

Object of activity: Financing the rural areas.

Address: Rr.”Ismail Qemali”, P. 32, Tirana, Albania.

Director: Zana Konini.

Exempted with the official document of the Bank of Albania, No. 1843, dated 01.08.2000.

2. Besa Foundation

Founded by “Open Society Fund for Albania” (SOROS).

Object of activity: Financing small and medium size enterprises.

Address: Rr.”Asim Vokshi”, No. 35, Tirana, Albania.

Director: Bajram Muça

Exempted with the official document of the Bank of Albania, No. 2895/I, dated 19.01.2001.

3. Albanian Partner on Microcredit

Shareholder: “Opportunity International” (East Europe).

Object of activity: Lending.

Address: Rr. “Gjin Bue Shpata”, No. 7/I, Tirana, Albania.

Director: James Reiff.

Exempted with the official document of the Bank of Albania No. 828/I, dated 08.04.2002.

These entities are not licensed or supervised by the Bank of Albania but they are obliged to report to the Bank of Albania.

6.1.3 REPRESENTATIVE OFFICES OF FOREIGN BANKS

I. Representative Office of the Popular Puglia Bank in Albania

License No. I, dated 02.07.2003.

Representative: Dr. Giancarlo STASI

Address: Sheshi "Skënderbej" - pranë Pallatit të Kulturës - kati i tretë, Tirana, Albania.

Tel: 00 355 4 256 782

6.1.4 FOREIGN EXCHANGE BUREAUS

1. "JOARD" Foreign Exchange Bureau Ltd., Tirana

License : No. 1, dated 01.10.1999.
Address: Rruga "Ded Gjo Luli" No.2, Tirana, Albania.

2. "AMA" Foreign Exchange Bureau Ltd., Durrës

License : No. 2, dated 01.10.1999.
Address: Rruga "Tregtare", Lagjja 3, Durrës, Albania.

3. "ARIS" Foreign Exchange Bureau Ltd., Tirana

License : No. 3, dated 01.10.1999.
Address: Rruga "Luigj Gurakuqi", Tirana, Albania.

4. "UNIONI FINANCIAR TIRANË" Foreign Exchange Bureau Ltd.

License : No. 4, dated 01.10.1999.
Address: Rruga "Reshit Çollaku", Pall. Shallvare, Shk. 2/18, Tirana, Albania.

5. "AGLI" Foreign Exchange Bureau Ltd., Tirana

License : No. 5, dated 01.10.1999.
Address: Bureau 1: Rruga "Islam Alla" No.1, Tirana.
Bureau 2: Rruga "Kavajës", pranë pastičeri "Rinia", Tirana, Albania.

6. "ALBAKREDIT" Foreign Exchange Bureau Ltd., Tirana

License : No. 06, dated 24.11.1999.
Address: Rruga "Ded Gjo Luli" No.5, Tirana, Albania.

7. "EXCHANGE" Foreign Exchange Bureau Ltd., Tirana

License : No. 08, dated 24.11.1999.
Address: Rruga "Durrësit" No. 170, Tirana, Albania.

8. "UNISIX" Foreign Exchange Bureau Ltd., Korça

License : No. 09, dated 26.11.1999.
Address: Bulevardi "Republika", Pall.4, Korça, Albania.

9. "EKSPRES J & E" Foreign Exchange Bureau Ltd., Durrës

License : No. 10, dated 26.11.1999.
Address: Lagjja 11, Rruga "Prokop Meksi" (pranë Hotel "Durrësi"), Durrës, Albania.

10. "MI & CO" Foreign Exchange Bureau Ltd., Tirana

License : No. 11, dated 29.02.2000.
Address: Rruga "Ded Gjo Luli", No.2/3, Tirana, Albania.

11. "ILIRIA '98" Foreign Exchange Bureau Ltd., Tirana

License : No. 12, dated 25.02.2000.
Address: Sheshi "Skënderbej", Teatri i Kukullave, Tirana, Albania.

12. "SERXHIO" Foreign Exchange Bureau Ltd., Elbasan

License : No. 14, dated 07.04.2000.
Address: Lagjja "Luigj Gurakuqi", Rr. 11 Nëntori", Pall. 70, No.14, Elbasan, Albania.

13. "ALBTUR" Foreign Exchange Bureau Ltd., Tirana

License : No. 15, dated 07.04.2000.

Address: Bulevardi "Zogu I", Pall. 32, Shk. I (përballë Bankës Tirana), Tirana, Albania.

14. "R & M" Foreign Exchange Bureau Ltd., Tirana

License : No. 16, dated 22.05.2000.

Address: Rruga "Punëtorët e Rilindjes", Pall. 182, Tirana, Albania.

15. "TEUTA 2000" Foreign Exchange Bureau Ltd., Durrës

License : No. 17, dated 22.05.2000.

Address: Lagjja 4, Rruga "Skënderbej", Ap. 950, Durrës, Albania.

16. "T & E" Foreign Exchange Bureau Ltd., Durrës

License : No. 18, dated 11.06.2000.

Address: Lagjja 4, Rruga "9 Maji", Durrës, Albania.

17. "SHIJAK 2000" Foreign Exchange Bureau Ltd., Shijak

License : No. 19, dated 24.11.2000.

Address: Lagjja "Popullore", Shijak, Albania.

18. "R & T" Foreign Exchange Bureau Ltd., Tirana

License : No. 20, dated 20.12.2000.

Address: Bulevardi "Zogu I", (pranë BPI-së), Tirana, Albania.

19. "DV-ALBA" Foreign Exchange Bureau Ltd., Tirana

License : No. 21, dated 11.01.2001.

Address: Sheshi "Skënderbej", Tirana Internacional Hotel, Tirana, Albania.

20. "MANUSHI" Foreign Exchange Bureau Ltd., Tirana

License : No. 22, dated 18.04.2001.

Address: Bulevardi "Zogu I", Qendra e Biznesit VEVE, Tirana, Albania.

21. "UNIONI SELVIA" Foreign Exchange Bureau Ltd., Tirana

License : No. 23, dated 21.05.2001.

Address: Në krah të Postës Qendrore, godina 2-katëshe, kati I, Tirana, Albania.

22. "KALENJA" Foreign Exchange Bureau Ltd., Tirana

License : No. 24, dated 29.06.2001.

Address: Rruga "Kavajës" (pranë Ambasadës Turke), Tirana, Albania.

23. "TILBA" Foreign Exchange Bureau Ltd., Elbasan

License : No. 25, dated 30.09.2001.

Address: Lagjja "Luigi Gurakuqi", Bulevardi "Qemal Stafa", Njësia No. 12, Elbasan, Albania.

24. "ANAGNOSTI" Foreign Exchange Bureau Ltd., Tirana

License : No. 26, dated 31.10.2001.

Address: Bureau I - Bulevardi "Zogu I", Pallati 97, shk.3.ap. 28, Tirana, Albania

Bureau 2- Rruga "Kajo Karafili", No. 11 Tirana, Albania.

25. "KO-GO" Foreign Exchange Bureau Ltd., Tirana

License : No. 27, dated 12.11.2001.

Address: Rruga "Vaso Pasha", Pall.16, Shk.2, Ap. 9, Tirana, Albania.

26. "ALB-FOREX" Foreign Exchange Bureau Ltd., Tirana

License : No. 28, dated 22.11.2001.

Address: Bureau 1- Rruga "Abdyl Frashëri No.3, Tirana, Albania.

Bureau 2- Rruga "Mine Peza", Pall. 102, Shk.1 (pranë Bar Grand), Tirana, Albania.

27. "L&N" Foreign Exchange Bureau Ltd., Tirana

License : No. 29, dated 22.11.2001.

Address: Rruga "Muhamet Gjollësia", ish-Gjelltorja tek sheshi Atatürk, Tirana, Albania.

28. "EXCHANGE ALOG" Foreign Exchange Bureau Ltd., Tirana

License : No. 31, dated 22.11.2001.

Address: Rruga "Mine Peza" (përballë selisë së Vatikanit), Tirana, Albania.

29. "EX-CHANGE BEBI&FLORI" Foreign Exchange Bureau Ltd., Fier

License : No. 32, dated 26.11.2001.

Address: Lagjja "Kongresi i Përmetit", Fier, Albania.

30. "BASHKIMI 2001" Foreign Exchange Bureau Ltd., Tirana

License : No. 35, dated 12.12.2001.

Address: Rr. "Kavajës" (pastiçeri "Rinia"), Tirana, Albania

31. "ARJON 2002" Foreign Exchange Bureau Ltd., Tirana

License : No. 36, dated 14.12.2001.

Address: Lagjja "Kongresi i Elbasanit", Bulevardi "Qemal Stafa", Pall.9-katësh, Elbasan, Albania

32. "ALAKTH" Foreign Exchange Bureau Ltd., Tirana

License : No. 42, dated 18.01.2002.

Address: Rruga e Dibrës, No.105/1, Tirana, Albania.

33. "FORMAT" Foreign Exchange Bureau Ltd., Tirana

License : No. 43, dated 21.01.2002.

Address: Rruga e Durrësit, Pall.85, shk.1,ap.1, Tirana, Albania.

34. "TRI URAT" Foreign Exchange Bureau Ltd., Elbasan

License : No. 44, dated 05.02.2002.

Address: Lagjja "29 Nëntori", pranë filialit të postës Elbasan, Albania.

35. "BESA 2001" Foreign Exchange Bureau Ltd., Tirana

License : No. 46, dated 15.02.2002.

Address: Rruga "Myslym Shyri", No.25, Tirana, Albania.

36. "MARIO" Foreign Exchange Bureau Ltd., Saranda

License : No. 47, dated 14.03.2002.

Address: Lagjja 1, pranë ish-Komitetit Ekzekutiv të rrethit Sarandë, Saranda, Albania.

37. "JAV" Foreign Exchange Bureau Ltd., Tirana

License : No. 48, dated 20.03.2002.

Address: Bulevardi "Zogu I" Godina e "Zërit të Popullit", Tirana, Albania.

38. "DROGU" Foreign Exchange Bureau Ltd., Tirana

License : No. 49, dated 23.04.2002.

Address: Rruga "Vaso Pasha" Kulla I, Kati I (pas pallateve Agimi), Tirana, Albania.

39. "HYSEN-C" Foreign Exchange Bureau Ltd., Laç

License : No. 50, dated 23.04.2002.

Address: Lagjja No.3, përballë Komisariatit të Policisë, Laç, Albania.

40. "UNIONI FIER" Foreign Exchange Bureau Ltd., Fier

License : No. 51, dated 08.05.2002.

Address: Lagjja "15 Tetori", Rruga "Kastriot Muça", Fier, Albania.

41. "TAXI EKSPRES" Foreign Exchange Bureau Ltd., Elbasan

License : No. 52, dated 20.05.2002.

Address: Rruga "Sami Frashëri", No. 11 (pranë Shkollës "Edit Durhan"), Elbasan, Albania.

42. "MERO" Foreign Exchange Bureau Ltd., Devoll

License : No. 53, dated 22.05.2002.

Address: Bureau 1 : Bulevardi "Fuat Babani", Bilisht, Albania.

Bureau 2 : Dogana Kapshticë, Albania.

43. "GLEAR" Foreign Exchange Bureau Ltd., Shijak

License : No. 55, dated 23.07.2002.

Address: Lagjja Kodër Shijak, Durrës, Albania.

44. "POSTA SHQIPTARE" Foreign Exchange Bureau Jnt. Stk. Tirana,

License : No. 56, dated 28.08.2002.

Address: Rruga "Reshit Çollaku", No. 4 Tirana, Albania.

45. "UNIONI BALLSH" Foreign Exchange Bureau Ltd., Ballsh

License : No. 57, dated 11.09.2002.

Address: Rruga "8 Nëntori", Ballsh, Albania.

46. "ESLULI" Foreign Exchange Bureau Ltd., Tirana

License : No. 58, dated 17.10.2002.

Address: Rr. "Reshit Çollaku", Pallati i Shallvareve, shkalla n.4/1, Tirana, Albania.

47. "AMERICAN GLOBAL CAPITAL FUND-WORLDWIDE INVESTMENT" Ltd. Tirana

License : No. 59, dated 26.11.2002.

Address: Rr. "Ismail Qemali", Parcela 167/187 "Euroapartment", Tirana, Albania.

48. "DENI&KRISTI-2002" Foreign Exchange Bureau Ltd., Tirana

License : No. 61, dated 02.06.2003.

Address: Rruga "Myslym Shyri", pallati 60, ap.3 Tirana, Albania.

49. “YLDON” Foreign Exchange Bureau Ltd., Tirana

License : No. 62, dated 03.06.2003.

Address: Rruga Qemal Stafa, pall. 382/2/2 Tirana, Albania.

50. “BILLI” Foreign Exchange Bureau Ltd., Tirana

License : No. 63, dated 16.02.2004.

Address: Sheshi “Wilson” , Tirana, Albania.

51. “REXHA F&E” Foreign Exchange Bureau Ltd.,Durrës

License : No. 64, dated 07.04.2004

Address: Rruga “Mujo Ulqinaku”, Lagja nr. 5, Pallati 619, Durrës, Albania

52. “ALBA&ARBËR” Foreign Exchange Bureau Ltd., Tirana

Licenca nr. No. 65, dated 06.05.2004

Adresa: Rruga “Kavajës”, pall. 3, kati i parë, Tirana.

53. “I.S.N.” Foreign Exchange Bureau Ltd.,Tirana

Licenca nr. No. 66, dated 06.05.2004

Adresa: Rruga “Kavajës”, pall. 3, kati i parë, Tirana.

54. “ARIABA” Foreign Exchange Bureau Ltd.,Tirana

Licenca nr. No. 67, dated 07.06.2004

Adresa: Rruga “Abdyl Frashëri”, kati i parë, shkalla 5, pranë Librit Universitar, Tirana.

55. “ALBACREDITS” Foreign Exchange Bureau Ltd., Tirana

License : No. 68, dated 13.07.2004.

Address: Rruga "Murat Toptani", pallati 12 katesh, kati përdhe, Tirana, Albania.

56. “ALB-KREDIT” Foreign Exchange Bureau Ltd., Tirana

License : No. 69, dated 19.07.2004.

Address: Rruga "Kongresi i Përmetit", nr.2, Tirana, Albania.

6.1.5 SAVINGS – CREDIT ASSOCIATION UNIONS

1. “JEHONA” Savings – Credit Associations Union, Tirana

License : No.1, dated 27.06.2002.

Chairman of the Executive Board: Vojsava Rama

Members of this union are 41 Savings – Credit Associations, licensed also as separate associations. They rely on the technical assistance given by the foundation “Movement for the savings-credit associations development”.

2. “ALBANIAN SAVINGS-CREDIT UNION” Savings–Credit Associations Union, Tirana

License : No.2, dated 09.08.2002.

Address: Rruga “Ismail Qemali”, No.32, Tirana, Albania.

Chairman of the Executive Board: Zana Konini

Tel: 04 25 19 10

E-mail : ffrural@albaniaonline.net

Members of this union are 91 Savings–Credit Associations licensed also as separate associations. They rely on the technical assistance given by Rural Financing Fund.

6.2 Annex 2: List of banking supervision regulations in force as of July 2004

- 1- Regulation "On granting a license to conduct banking activity in the Republic of Albania", approved by the Supervisory Council Decision No. 71, dated 11.09.2002.
- 2- Regulation "On banks and branches of foreign banks' administrators", approved by the Supervisory Council Decision No. 120, dated 30.12.2003.
- 3- Regulation "On licensing the non-bank financial institutions", approved by the Supervisory Council Decision No. 96, dated 26.11.2003.
- 4- Regulation "On credit risk management", approved by the Supervisory Council Decision No. 12, dated 21.02.2001, revised by the Supervisory Council Decision No. 32, dated 08.05.2002.
- 5- Regulation "On the size and completion of minimum initial capital for activities permissible to banks and branches of foreign banks", approved by the Supervisory Council Decision No. 51, dated 22.04.1999.
- 6- Guideline "On regulatory capital", approved by the Supervisory Council Decision No. 57, dated 05.05.1999, revised by the Supervisory Council Decision No. 21, dated 24.03.2004.
- 7- Regulation "On capital adequacy ratio", approved by the Supervisory Council Decision No. 82, dated 08.10.2003, revised by the Supervisory Council Decision No. 22, dated 24.03.04.
- 8- Regulation "On foreign currency open positions", approved by the Supervisory Council Decision No. 59, dated 05.05.1999, revised by the Supervisory Council Decision No. 118, dated 01.12.1999.
- 9- Regulation "On foreign currency operations", approved by the Supervisory Council Decision No. 64, dated 30.07.2003, revised by the Supervisory Council Decision No. 101, dated 10.12.2003.
- 10- Guideline "On banks' liquidity", approved by the Supervisory Council Decision No. 04, dated 19.01.2000, revised by the Supervisory Council Decision No. 08, dated 12.02.2003.
- 11- Regulation "On market risks", approved by the Supervisory Council Decision No. 72, dated 02.06.1999, revised by the Supervisory Council Decision No. 98, dated 19.12.2001.
- 12- Regulation "On controlling the large risks", approved by the Supervisory Council Decision No. 78, dated 07.07.1999, revised by the Supervisory Council Decision No. 119, dated 01.12.1999, revised by the Supervisory Council Decision No. 92, dated 05.12.2001.
- 13- Guideline "On internal control of banks", approved by the Supervisory Council Decision No. 107, dated 03.11.1999.
- 14- Regulation "On investments in the capital of commercial companies by banks", approved by the Supervisory Council Decision No. 42, dated 06.06.2001.
- 15- Regulation "On cooperative banks", approved by the Supervisory Council Decision No. 25, dated 29.03.2000.
- 16- Guideline "On interest rate risk management", approved by the Supervisory Council Decision No. 61, dated 05.07.2000.

17- The Supervisory Council Decision No. 26, dated 29.03.2000 “On exemption of some entities from the application of the provisions of Law “On banks in the Republic of Albania”.

18- Regulation “On supervision terms over non-bank entities conducting financial activity”, approved by the Supervisory Council Decision No. 60, dated 05.07.2000.

19- Regulation “On certified accounting experts of banks”, approved by the Supervisory Council Decision No. 06, dated 29.01.2003, revised by the Supervisory Council Decision No. 102, dated 10.12.2003.

20- The reporting system of the savings-credit associations, approved by the Supervisory Council Decision No. 75, dated 05.09.2001.

21- Guideline “On certificates of deposits”, approved by the Supervisory Council Decision No. 79, dated 03.10.2001.

22- Regulation “On money laundering prevention”, approved by the Supervisory Council Decision No. 10, dated 25.02.2004.

23- Regulation “On licensing the savings-credit associations”, approved by the Supervisory Council Decision No. 11, dated 27.02.2002, revised by the Supervisory Council Decision No. 09, dated 12.02.2003.

24- Guideline “On banks’ custody and liquidation”, approved by the Supervisory Council Decision No. 45, dated 12.06.2002.

25- The Supervisory Council Decision No. 58, dated 24.07.2002, approved to add in the permitted banking activities the “banking activity in relation to gold and precious metals”.

26- Regulation “On supervision of the savings – credit associations”, approved by the Supervisory Council Decision No. 67, dated 28.08.2002, revised by the Supervisory Council Decision No. 83, dated 13.11.2002.

27- Regulation “On licensing the foreign exchange bureaus”, approved by the Supervisory Council Decision No. 65, dated 30.07.2003.

28- Guideline “On reporting the foreign exchange operations”, approved by the Supervisory Council Decision No. 69, dated 30.07.2003.

29- Regulation “On bank’s relations with related persons”, approved by the Supervisory Council Decision No. 100, dated 10.12.2003.

