



1999

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# BANKING SUPERVISION

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## Methodological note

All data used in this publication are for banks with valid licences as of 31 December 1999, unless stated otherwise in the chapter heading or relevant passage. Data are always taken for the bank as a whole, i.e. including its foreign branches, with the exception of the data on the structure of credits and deposits by sector and industry, which comprise only bank transactions in the Czech Republic.

The data for 1999 partly reflect the results of external audits, so they may differ from data previously published by the CNB. There may be additional partial changes to the data given in this publication; however, they should not significantly affect the trends indicated.

## Foreword

Banking Supervision in 1999 is a periodical published by the Czech National Bank aimed at providing basic information on supervisory activities and the results of the banking sector in individual years. This publication, which focuses on facts, endeavours to present all users from among the professional and lay public with information on the present extent of banking supervision and the state of the banking sector from the point of view of its performance and compliance with the prudential rules. It is, therefore, the Czech National Bank's contribution to the transparency of banking business.

The publication is divided into four parts. The first part concentrates on the regulations of the Czech National Bank aimed at limiting the risks of banking business. Compliance with these rules considerably curtails the potential problems of banks and contributes to the stability of the banking sector. In addition to giving a basic overview of the provisions (regulations) banks had to adhere to in the course of 1999, this part focuses on the improvements to these provisions that were implemented in 1999. All the amendments to the prudential rules have been induced not only by the endeavour to attain full harmonisation with European Union regulations, but also by the endeavour to cover all risk areas in banking business, which in many cases are specific to the Czech Republic. In the first part you can also find a survey of the CNB banking supervisory authority's activities, especially the information gained from the performance of banking supervision in practice, the extent of international co-operation and a summary of all the steps taken by the Czech National Bank for the banking sector's successful transition into the year 2000. The second part contains up-to-date information on the products and services which banks operating in the Czech Republic offer to their clients. The third part provides basic data on the state of the banking sector in the Czech Republic. It deals with all areas of banking business and with the performance of the banking sector, devoting special attention to compliance with the prudential rules for banks. The primary aim of this part is to present in a clear form information characterising the basic trends in the banking sector in terms of structure of assets and liabilities, off-balance-sheet activities, foreign exchange transactions, banks' activities vis-à-vis non-residents and so on. The appendices contain detailed information in tabular form which the reader can use to conduct further analyses from other angles than those provided in this publication.

# A.

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## BANKING SUPERVISION IN 1999

In 1999 the CNB banking supervisory authority concentrated on further fulfilment of its basic objectives in accordance with the medium-term conception for its development approved by the CNB Bank Board in 1998. These objectives consist primarily in further harmonising the regulatory framework, methods and procedures with the prudential principles of the European Union and with best international practices. The basic aim is to establish a comprehensive, standardised and transparent system of regulation of the banking sector from both the methodological and practical points of view, in harmony with the Core Principles for Effective Banking Supervision defined by a working group of banking supervision experts from selected countries under the auspices of the Basle Committee on Banking Supervision.

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### 1. THE PRUDENTIAL RULES FOR BANKS IN THE CZECH REPUBLIC

The activities of banks in the Czech Republic are governed above all by Act No. 21/1992 Coll. on Banks, as amended, which contains the basic principles for granting a banking licence and provides for the structure of the bank's governing bodies, the procedure for acquiring holdings in banks, the operational requirements for banks, the basic procedures of banking supervision (including conservatorship and banking licence revocation), the system of insurance of deposits, etc. The Act on Banks states in general the obligation of a bank to proceed with prudence when performing its activities, and especially to conduct its business in a manner which is not detrimental to the interests of its depositors as regards the safety of their deposits, and which does not endanger the safety and soundness of the bank. This Act also authorises the Czech National Bank to issue "provisions" in the form of prudential rules stipulating the detailed requirements for the activities of banks. The purpose of these rules is to limit the exposure of banks to the risks inherent in all banking business and thus to maintain, or to enhance, the stability of the banking sector.

In 1999, the banks and foreign bank branches operating in the Czech Republic observed the following Czech National Bank provisions governing the rules for prudential business:

- CNB Provision No. 3 of 5 October 1995 on the Capital Adequacy of Banks. This stipulates the minimum limit for capital adequacy – expressed as the ratio of the bank's capital to the volume of its risk-weighted assets – which banks are obliged to maintain. This capital adequacy ratio temporarily included credit risk only (the capital adequacy ratio also incorporating market risk was introduced in April 2000). The minimum ratio has been set at 8%. This provision superseded a previous one in force since 1993 and has been partially amended several times during subsequent years.
- CNB Provision No. 4 of 5 October 1995 on the Credit Exposure of Banks. This stipulates the maximum limits for credit exposure – the ratio of credit exposure to the bank's capital – as follows: towards non-bank clients 25%, towards entities with close links to the bank 20%, and towards banks 125%. The same limits are also applied to groups of economically linked entities. This provision, which superseded a provision in force since 1993, has been partially amended several times during subsequent years.
- CNB Provision No.11 of 20 December 1996 on Bank Liquidity Rules. This does not stipulate any binding limits, but lays down the basic principles for managing liquidity, for example the obligation of banks to monitor residual maturity of assets and liabilities, to maintain a certain volume of funds in the form of quick assets, to formulate contingency plans for cases of unexpected outflow of funds, etc. This provision superseded a provision in force since 1993.

- CNB Provision No.193/1998 Coll. Stipulating the Principles for Classifying Loan Receivables and for Provisioning for these Receivables. This contains a detailed specification of the classification rules, according to which banks must break down all their loan receivables into five groups by the level of risk that these receivables will not be repaid in time and to a sufficient extent and will thus represent a real loss for the bank. It also stipulates the extent of obligatory classification-related provisioning required to cover any losses arising from these receivables. A provision governing this area has been in force since 1994. Owing to the problems with enforcing collateral, the present provision stipulates mandatory additional provisioning for loss loans secured by real estate which are more than one year past due.
- CNB Provision No. 6 of 8 December 1995 Stipulating the Restrictions and Conditions for the Open Foreign Exchange Positions of Banks and Foreign Bank Branches. In addition to defining individual terms, this sets the limits for open foreign exchange positions in relation to the bank's capital for individual freely convertible currencies (15%), for other currencies individually (2%) and for all remaining currencies overall (4%), for the open foreign exchange position (20%) and for the overall koruna position (15%). This provision superseded a previous one in force since 1993. Its main effect was to switch from an approach consisting in the limitation of groups of currencies to an individual approach towards individual currencies.
- CNB Provision No. 3 of 9 June 1997 on the Principles for Creating Portfolios of Securities and Holdings by Banks and for Covering the Risk of Devaluation of Securities and Holdings through Provisioning. This regulation focuses on laying down the rules for valuing securities in banks' trading and investment portfolios. Using these valuations, it stipulates mandatory provisioning to cover the difference between the market value and the purchase price of the individual securities in the trading portfolio and of the overall securities portfolio in the case of the investment portfolio. This provision, which superseded a previous one from 1996, thus ensures a realistic valuation of the securities and to a certain extent substitutes for the principle of market valuation, which is not yet recognised in Czech accounting.
- CNB Provision No. 8 of 22 September 1997 Stipulating the Restrictions and Conditions for Banks for Certain Types of Credits and Investments in Ownership Interests. This provision was induced by the need to restrict certain undesirable activities of banks in relation to persons linked with the bank and to curb the interconnections between banks and other economic agents. It superseded a provision in force since 1994.
- CNB Provision No. 4 of 29 September 1998 Stipulating the Requirements for the Bank Performance Report. This contains a description of the system for managing the bank's risks in all areas. It also requires banks to have external auditors verify whether the information given by the bank is true and whether its risk management system is commensurate with the scope of its activities. A provision governing this area has been issued annually since 1994 with the aim of updating the required content of the report.
- CNB Provision No. 2 of 29 June 1998 Stipulating the Minimum Requirements for the Disclosure of Information by Banks and Foreign Bank Branches. This requires banks to publish, on a quarterly basis, specific information on their premises so that it might be available to the public. The information relates on the one hand to indicators characterising the bank's performance – for example its capital adequacy ratio, profitability, classified credits, basic structure of its assets and liabilities – and on the other to data on the structure of the bank's shareholders, its management, etc.
- CNB Provision No. 6 of 29 December 1998 Stipulating the Requirements for Ensuring the Safe Operation of Banks and Foreign Bank Branches with respect to the Year 2000 Risk. This sets down the framework for the safe transition of the automated systems of banks, including foreign bank branches, into the year 2000 and the elimination of the Y2K effect.

The Act on Banks itself supplements the prudential rules in the area of banks' interconnections with other legal entities and in other areas. In particular

- it prohibits banks from exercising control over another legal entity which is not a bank, a financial institution or an ancillary banking services undertaking;

- it prohibits, with some minor exceptions, the acquisition of qualifying holdings in legal entities other than banks, financial institutions or ancillary banking services undertakings which would exceed 15% of the bank's capital in the case of a single legal entity, or 60% of the bank's capital with regard to its total qualifying holdings in all legal entities;
- it prohibits members of the statutory body of a bank from simultaneously being a member of the statutory body or supervisory board of another legal entity and also prohibits bank employees from being in the statutory body of such a legal entity – with certain exceptions in the case of financial institutions controlled by the bank, legal entities authorised to organise the demand and supply of securities and ancillary banking services undertakings;
- it obliges the bank to create conditions in its organisational, management and control systems to ensure the separation of lending and investment transactions and the separation of investment transactions for the bank's own account and those for account of clients;
- it sets down the duty to carry on securities transactions for own account only under the most advantageous conditions that can be attained while exercising due diligence; the same duty applies when carrying on investment transactions for account of clients etc.

The CNB provisions and the Act on Banks cover all critical areas of the bank's performance. Even though the degree of their harmonisation with internationally recognised standards is relatively high, the CNB banking supervisory authority is paying continuous attention to improving them in order that they may be fully comparable with the rules applied in countries with advanced banking sectors and that their potential shortcomings may not have a negative impact on the perception of the soundness of the Czech banking sector.

## 2. CHANGES TO THE REGULATIONS IN 1999

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The consistent endeavour of the CNB banking supervisory authority to adjust the system of regulation of the banking sector in the Czech Republic to the international standards expressed in the Core Principles for Effective Banking Supervision and in the directives of the European Union was reflected in 1999 in a further improvement and expansion of the prudential rules for banks.

The gradual development of bank activities containing elements of market risk, especially securities trading and derivatives transactions gave rise to the need to improve the **capital adequacy rules**, which until then had encompassed credit risk only. In 1998, therefore, work was begun on a new provision on capital adequacy encompassing both credit and market risks, which was approved in July 1999 (CNB Provision No. 3 of 28 June 1999 on the Capital Adequacy of Banks Incorporating Credit and Market Risks). The date of its entry into force was set at 1 April 2000.

The new capital adequacy provision signifies a new approach towards the stipulation of capital requirements. Its core element is the breakdown of all banking activities into trading and banking portfolios. The provision then defines for both portfolios the rules for determining the required level of capital to cover the credit risk in the banking portfolio and the market risks (interest rate risk, exchange rate risk, equity risk and commodity risk) in the trading portfolio. The provision contains the basic rules of the standard method for determining the capital requirements, in particular for determining both the general and the specific risk for the individual types of market risks and the level of the capital requirements for their coverage. It also defines the structure of the bank's capital, the structure of risk-weighted assets in the banking portfolio and so on. It also includes a **new calculation of credit exposure** and its limits in relation to the bank's capital and **limits for open foreign exchange positions**. Thus the existing provisions on capital adequacy, credit exposure and open foreign exchange positions were merged into a single provision, in which they logically belong. The new capital adequacy provision also enables banks to use their own models to calculate the individual risks from which the capital requirements are derived, provided they meet certain minimum requirements defined in this provision.



The determination of capital adequacy incorporating both credit and market risks is a relatively complicated process which requires detailed knowledge of all financial instruments, not only in terms of their application, but also with regard to determining the level of risk involved. A methodological aid has been prepared to help orient both banks and the individual banking supervisors whose responsibility it is to check compliance with the correct procedure for determining market risks. This aid contains a description of the method for valuing the individual financial instruments which are exposed to market risks.

Another provision which was prepared in the course of 1999 is the provision on **consolidated supervision** (CNB Provision No. 2 of 8 July 1999 Stipulating the Terms and Conditions for Performing Supervision of Banks on a Consolidated Basis), which has been in force since July 1999. The prudential rules which had been in force until then applied only to banks and did not regulate the overall position of a bank within the framework of its group. At the beginning of the development of the banking sector, this approach was not necessary, as the involvement of banks in other areas of activity was minimal. In the course of time, however, financial groups began to be formed in which banks in a number of cases play the decisive role. Thus it became apparent that it was necessary to speedily adopt measures to regulate the banking sector on a consolidated basis.

The aforementioned provision is the first step towards consolidated supervision according to the standards of European legislation. Owing to the limitations of the present Act on Banks, consolidated supervision applies only to those groups which are headed by a bank and which comprise other financial entities and insurance companies. In other cases, i.e. where a group is not headed by a bank but by some other legal entity, the Act on Banks does not yet empower the CNB banking supervisory authority to request information or to adopt any measures that might be necessary. The provision sets down the rules for determining a consolidated group and the methods a bank is obliged to use for consolidation. It also stipulates the obligation to maintain capital adequacy – for the time being containing credit risk only – for the entire group at 8% at minimum, and the limits for credit exposure and the maximum limits for holdings in non-bank and non-financial entities on a consolidated basis equal to those which are applied to the bank itself.

Banks will be obliged to implement consolidation for the first time when preparing their financial statements for 1999. As the banks will be consolidating audited data, the first reports monitoring adherence to the requirements enacted by this provision will be submitted as late as September 2000. An amendment to this provision will be prepared under which capital adequacy will also include the calculation of capital requirements with respect to market risks and which at the same time will set forth the obligation to consolidate with quarterly periodicity. The further development of consolidated supervision will focus on extending the scope of consolidation to include financial groups headed by entities other than banks, i.e. financial and mixed-activity holding companies. This, however, will be only possible after amendment of the present Act on Banks.

1999 also saw the replacement of the provision stipulating the principles for creating securities portfolios and for provisioning for these securities (with the present CNB Provision No. 5 of 30 December 1999 on the Principles for Covering the Losses from Depreciation of Securities and Holdings through Provisioning). This change, however, was of purely technical character, as it only replaced certain terms and definitions in order that they might correspond to the terms and definitions used in the new Provision on Capital Adequacy Incorporating Credit and Market Risks, with which it is closely linked.

A response to the amendment to the Act on Banks which came into force in September 1998 was the elaboration of CNB Decree No. 32/1999 Stipulating the Essentials for an Application for Prior Consent from the Czech National Bank to Acquire Voting Shares in a Bank and the Essentials of Notification about Decreasing a Holding of Voting Shares in a Bank. The amendment to the Act on Banks of September 1998 has unified the conditions for the acquisition of holdings in a bank for all investors, regardless of whether they are domestic or foreign, and for cases of new acquisitions of holdings or increases in existing ones. According to the Act on Banks and in line with European Union practice, every person whose holding in a bank would exceed 10%, 20%, 33% or 50% must ask the Czech National Bank for consent to such an acquisition or increase. The CNB decree then sets down the technical procedure, i.e. the format of the application for consent, the extent of the information the investor is obliged to submit and the course of the administrative proceedings. The Czech National Bank therefore has the possibility of evaluating every potential major shareholder of a bank and thus also of steering the shareholder structure of the banking sector towards inclusion of responsible and well-established entities which will contribute to its stability. The decree also stipulates the format for reporting a decrease in a holding in a bank.

In 1999, work was begun on an amendment to the Act on Banks, the main purpose of which is full compatibility with European Community directives. This amendment, which has already been approved by the Government of the Czech Republic, is expected to enter into force on 1 January 2001. The draft amendment includes important aspects of the regulation and exercise of banking supervision. Above all it creates a comprehensive framework for supervision on a consolidated basis, comprising also financial and mixed-activity groups not headed by banks, and facilitates effective co-operation with foreign partner supervisors, including the conducting of on-site examinations in foreign banks operating in a partner country by the domestic supervisor. It also contains a complete formal harmonisation of the criteria for granting a banking licence and for the entry of shareholders into existing banks; incorporation of the principle of a unified banking licence for foreign bank branches, which will enter into force upon accession of the Czech Republic to the European Union; a modification to the evaluation of the competence of bank managers; harmonisation of the rules for the exchange of information between the Czech National Bank and other bodies; an extended modification to the system for the insurance of deposits, etc.

### 3. LEGISLATION AFFECTING BANK ACTIVITIES

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In addition to the "classic" regulations of banking law such as the Act on Banks and the Act on the CNB, the activities of banks are fundamentally influenced by a large number of other norms of general effect. The most important of these is the Commercial Code, which stipulates the basic conditions for the activities of joint-stock companies, which is the only form in which banks in the Czech Republic are allowed to operate (except for one state financial institution). They also include, *inter alia*, a group of acts regulating the possibility of recovering debts from defaulting debtors (the Code of Civil Procedure, the Act on Public Auctions and the Act on Bankruptcy and Settlement) and a group of acts stipulating the basic legal framework for maintaining trustworthy documentation and information on business activities (the Act on Accounting and the Act on Auditors).

All these regulations will be either substantially revised or completely replaced during the course of 2000. The main reason for these amendments is the harmonisation of Czech law with European legislation – linked to the Czech Republic's interest in accession to the European Union – and with international standards, especially in the accounting and auditing areas. Apart from this, the amendments to the acts regulating debt recovery are necessitated by the problems with applying the existing regulations in practice. These problems consist above all in the low recovery rate and the protracted process of debt recovery and of turning to the law in general; in the weakening of the position of creditors; and in the undermining of the trust of society in general that the law will be respected.

#### 3.1 The Act on Public Auctions

Act No. 26/2000 Coll. on Public Auctions is a new act which entered into force on 1 May 2000. It is expected above all to improve and simplify the manner in which creditors can achieve satisfaction of their past-due claims through realisation of collateral, by streamlining the process of the sale of items on the basis of executory court rulings and realisation of bankruptcy assets.

The auctions will be organised by auctioneers – persons with the appropriate trade licence – who will be subject to inspection by the Ministry for Local Development. Each auction will be conducted only on the basis of a contract between the person proposing the auction and the auctioneer. The mandatory particulars of such contracts are defined by the Act. Participants in the auction, i.e. persons arriving intending to make a bid and to acquire the subject of the auction, may not, *inter alios*, be bankrupts, which could apply to several former banks. The ownership of the subject of the auction is transferred as of the moment of knockdown to the highest bidder, provided that he pays the auction price in time. The rights of any easement beneficiaries, however, remain intact. Under this Act, it is possible to auction both movables and immovables, businesses or organisational parts thereof and transferable rights which have property value, but it is not possible to auction securities.

The Act distinguishes between two types of auctions – voluntary and involuntary, depending on the person at whose proposal the auction is conducted. A voluntary auction is conducted at the proposal of the owner of the subject of the auction. The owner of the subject of the auction is also the receiver and the bankruptcy trustee. The Act on Bankruptcy and Settlement has been amended in such a way that realisation of the bankruptcy assets by public auction at the proposal of the trustee is now considered the priority manner of such realisation.

The important consequences of a voluntary auction are as follows:

- a) in the case of auctioning a business or organisational part thereof, the person proposing the auction (i.e. the original owner) guarantees fulfilment of the obligations which were transferred to the highest bidder with the ownership of the business or organisational part thereof;
- b) any liens on the subject of the auction (e.g. real estate) do not expire and remain in effect with respect to the highest bidder, and any claims secured by these rights, if they are not yet due, do not fall due as of the day of transfer of ownership.

The situation is different in the case of an involuntary auction, which is conducted at the proposal of an auction creditor whose claim has been acknowledged by an executory court ruling or an executory arbitration award or is documented by an executory notarial record. Of great importance for banks is the provision of Article 36(2) of the Act stating: "If a lien on real estate was inserted or registered in the Real Estate Cadastre before this Act entered into force or if a lien on a movable object arose on the basis of a valid lien agreement before this Act entered into force, and if the person who proposed the auction made an affidavit in the form of a notarial record to the effect that it has a claim on the debtor which is payable and has not been paid and which is secured by the said lien, then the auction conducted at the proposal of the auction creditor whose claim is secured by the said lien is also an involuntary auction". This provision establishes the right of the auction creditor to propose an auction even if the lien arose before the Act entered into force, provided that he makes an affidavit in respect of the aforementioned facts in the presence of a notary.

The auctioneer is obliged first of all to notify the debtor and pledger of the intended exercise of the proposer's right to conduct an auction. The Civil Code and the Commercial Code have been also amended to this effect. Any legal acts implemented by the owner or pledger upon receipt of the aforementioned notification in writing by which the subject of the auction would be illegally transferred or encumbered or which would similarly decrease its value in some other way are invalid under the law. If the subject of the auction is real estate registered in the Real Estate Cadastre, the auctioneer must also send a notification of the auction to the Cadastral Office in order that it might enter a note in the relevant record.

Upon transfer of ownership of the subject of auction, any liens encumbering this subject that secure claims predating the earliest claim registered for the auction do not expire. Any other liens expire and the claims secured by them become payable to the extent to which they are satisfied in the auction.

After the auction, its costs are settled and the registered claims of auction creditors are satisfied. In addition to pledgees and lienees, the auction creditors include tax administrators and administrators of social security and health insurance companies involved in public health insurance. If it is not possible to satisfy all the registered claims from the proceeds of the auction, the proposal breaks down the claims into four groups, which are satisfied progressively. The important point for banks is that the second group includes registered claims arising from mortgage credits serving to cover the nominal value of mortgage bonds, and that the third group comprises registered claims secured by a lien and by restraint of conveyance of real estate; if there several such claims, they are satisfied in order of their origination. Taxes, fees, insurance premiums and the like come after any claims of the bank and are classified in the fourth group.

A new bill on judicial distrainers and distraining activities (the Distrain Code), which has already been passed by the Chamber of Deputies, proposes, however, that Part Three of the Act on Public Auctions, which relates to involuntary auctions, should be repealed. According to this bill, the sale of pledges without the debtor's consent and out of court would henceforth be carried out only by authorised distrainers and essentially only on the basis of an express authorisation of the court and of an executory power of distraintment, which as a rule would be an executory court ruling only.

### 3.2 The Act on Bankruptcy and Settlement

Act No. 328/1991 Coll. on Bankruptcy and Settlement has been revised several times. The latest amendment to this Act entered into force on 1 May 2000. It is expected to speed up the bankruptcy process and to yield greater proceeds, and therefore also greater satisfaction of creditors' claims, in the event of bankruptcy (insolvency, overindebtedness) of the debtor, and to strengthen the position of the bankrupt's employees and former third-class creditors. The bankruptcy law in practice has a bearing on banks primarily as the bankrupt's creditors. The amendment provides for new obligations upon bankrupts and trustees, including penalties and responsibility for any breach of these obligations, and confers greater rights upon creditors. Of the numerous changes, only the most important are mentioned here.

In the event of bankruptcy, the debtor need not file for bankruptcy provided that he files a petition for settlement, which ought to ensure wider use of this institute. However, in order that debtors should not groundlessly file petitions for settlement – which from their point of view is a “softer” solution – so as to defer the declaration of bankruptcy, the Act stipulates that unless settlement is permitted or confirmed by the court the debtor will have to file for bankruptcy. Wilful failure to observe this duty will be then judged a criminal offence.

The debtor must submit to the court a list of his assets and liabilities signed in his own hand and must declare that this list is correct and complete. This had previously been the duty of the bankruptcy trustee. The list should help both the courts in forming an opinion on the economic situation of the debtor and the trustee in compiling a list of the bankrupt's estate.

The bankruptcy trustee may newly be, in addition to a natural person, a public company, provided that it performs the activities of trustee through partners who themselves fulfil the conditions laid down for bankruptcy trustees. A completely new and fundamental right of the creditor will henceforth be the possibility of asking the court to remove the trustee from his function and to appoint a new one. Another new feature is the institute of a “preliminary trustee”, whom the court may appoint immediately upon the filing of the bankruptcy petition for the purpose of securing and ascertaining the debtor's assets and reviewing the debtor's accounting, if the circumstances suggest that the debtor is bankrupt. The debtor will then be able to dispose of his assets only with the consent of the preliminary trustee.

Banks are affected by the obligation to notify without undue delay the trustee or the preliminary trustee at his written request of the numbers of the debtor's accounts and the balances of his accounts and changes thereto; to give him information on any objects deposited by the debtor in their safekeeping and information on the debtor's deposit books; and to provide him with any other data necessary to ascertain the debtor's assets – to the same extent as they would provide them to the debtor (bankrupt) himself.

The amendment expressly states that the inventory of assets belonging to the bankrupt's estate is a deed that authorises the trustee to realise the assets contained therein. Under the Act, bankruptcy relates not only to the debtor's assets, but also to the assets of other persons, especially if such assets were transferred to them by the debtor during the period immediately preceding the declaration of bankruptcy in order that they would not be included in the bankrupt's estate. As soon as an object or other asset is entered in this inventory, only the trustee or a person authorised by him may dispose of it.

Consent to operating the bankrupt's business will henceforth not be given to the trustee by the court, but instead by the creditors or the creditors' committee. This means that it will be entirely down to them to decide whether such a measure will be effective.

The most important change from the point of view of banks is the provision according to which separate (secured) creditors – as a rule entities whose claims are secured by pledges, transfers of rights or claims, or by liens – will be paid only 70% of the proceeds from realisation of the security falling to their share.

According to the amendment, it is not possible within the framework of bankruptcy to realise any items securing the claims of separate (secured) creditors (i.e. as a rule pledges) by public auction; such items may only be realised in the manners provided for by judicial distraint. By contrast, the property of the bankrupt may be realised by public auction.

There is one provision which should enable creditors to gain quicker access at least to a part of their money. This is the provision enabling the court to permit a partial repartition even before approval of the final report, provided that it is clear that the execution of the repartition after its approval will not be endangered.

As to the order in which creditors' claims will be satisfied from the bankruptcy proceeds, an important positive change for the bankrupt's employees is the fact that it will be possible to satisfy all their wage claims arising not more than three years prior to the declaration of bankruptcy at any time during the course of the bankruptcy and that they will not have to wait for the repartition. Until now this had applied essentially only to their work claims arising after the declaration of bankruptcy. An advantage for "ordinary" (unsecured) creditors is the fact that the claims of the state (taxes, fees, public insurance, etc.) arising not more than three years prior to the declaration of bankruptcy will no longer be given priority over their claims and that 70% of the proceeds of the realisation of the bankrupt's estate left after the satisfaction of those claims which can be satisfied at any time in the course of the bankruptcy proceedings must be set aside for the satisfaction of their claims. In the event of bankruptcy of a bank, the priority order of the claims of owners of mortgage bonds remains unchanged.

In the event of settlement, the threshold for satisfaction of creditors has been decreased from 45% to 30% (and in the event of compulsory settlement from one third to 15%), which should also be conducive to wider use of this institute. Another innovation is the possibility of offering settlement or compulsory settlement in the form of a new issue of shares or other securities by the debtor, or even in non-monetary form.

Several other acts were also amended along with the Act on Bankruptcy and Settlement. The most important of these revisions are the new *res gestae* for criminal offences committed in connection with bankruptcy and settlement proceedings (breach of duty in bankruptcy proceedings, overindebtedness) in the Penal Code. There is also a new provision in the Commercial Code which prohibits a person from becoming a member of the statutory body or other body of a legal entity if this person was acting as the statutory body or other body of the legal entity against whose assets bankruptcy has been declared or a bankruptcy petition has been rejected owing to lack of assets at the time when that legal entity became bankrupt. This prohibition applies for a period of three years from the cancellation of the bankruptcy or the rejection of the bankruptcy petition owing to lack of assets, unless such person acted in the "bankrupt" business with due diligence (in case of doubt, the burden of proof shall be borne by this person) or the legal entity went bankrupt as a result of a criminal offence committed by a third person or the person in question was the liquidator who filed for bankruptcy.

### **3.3 The Act on Accounting**

The Act No. 563 /1991 Coll. on Accounting, as amended, stipulates the basic duties of businesses for presenting a true and fair view of their financial performance. Since 1999, the Ministry of Finance, in close co-operation with the Czech National Bank, has been preparing an amendment to this Act, which, in its conception, links up with the proposed amendments to the Commercial Code, the Act on Securities and the Act on Bonds. All these regulations should enter into force on 1 January 2001.

The proposed amendment stipulates the basic elements of accounting and tightens the requirements for the keeping, extent and conclusiveness (trueness and fairness) of accounts. It envisages that the individual elements will be elaborated further in a series of operating regulations of the Ministry of Finance. The Ministry has also been newly entrusted with publishing the Czech accounting standards, which will not constitute a legal regulation and which will contain a description of accounting methods and procedures.

Among the most interesting of the proposed amendments to the Act that are likely to effect banks are the following changes. The accounting period need no longer be the calendar year, but with the consent of the tax administrator could alternatively be a business year beginning on the first day of a month other than January. Banks controlled by foreign banks could make use of this provision, provided such foreign banks already use the business-year concept in their accounting.

Also of importance is the new rule stating that provisions, reserves and technical reserves for foreign currency assets and liabilities shall also be expressed in foreign currency and shall subsequently be converted to CZK using the spot exchange rate of the CNB. Another change which is very important for banks is the newly adopted breakdown of assets and liabilities into short-term and long-term ones. Long-term assets and liabilities are those whose life, or maturity, exceeds one year; all others are short term. This enables banks to regard securities in their trading portfolio (both assets and liabilities) as short-term ones and securities in their banking portfolio as long-term ones, in accordance with the CNB capital adequacy provision.

Henceforth, the annual report is to include besides the financial statements for the given accounting period also the financial statements for the two preceding accounting periods. The financial statements of a bank, together with its annual report, must be published; this obligation is considered fulfilled with their delivery to the registration court. Banks must prepare consolidated financial statements encompassing all entities in relation to which it is, in accordance with the Commercial Code, the controlling or governing entity or in which it exerts a substantial influence.

With regard to the valuation of assets and liabilities, another important aspect for banks is the manner of valuation of short-term securities and derivatives at their real value; this means either their market value, a valuation resulting from a qualified estimate or expert opinion, or a valuation according to special legal regulations – in that order.

### **3.4 The Act on Auditors**

The present Czech National Council Act No. 524/1992 Coll. on Auditors and the Chamber of Auditors of the Czech Republic was adopted as a follow-up to the issuance of the Commercial Code and the Act on Accounting, which extended the obligation to carry out an audit to joint-stock companies and under stipulated conditions also to limited-liability companies and to co-operatives. This Act was amended by Act No. 63/1996 Coll. (which repealed the provision on mandatory reviewing of all auditors) and by Act No. 165/1998 Coll. (which relieves the auditor of his obligation to maintain confidentiality in cases where the auditor, with the bank's knowledge, informs the Czech National Bank about any material facts which might have a negative impact on the bank's finances).

The present Act defines the auditor as a natural or legal entity qualified by registration in the list of auditors maintained with the Chamber of Auditors to perform auditing activities. It also stipulates the conditions for passing the professional examination and for performing auditing activities, and regulates the position of assistants to the auditor. The Act establishes the Chamber of Auditors of the Czech Republic as a self-governing professional organisation grouping all auditors and assistants to auditors registered in the list maintained with the Chamber. Under the Act, all powers in the auditors' profession appertain to the Chamber, from entry into the profession through to imposition of the disciplinary measures stipulated by law.

Under this legal arrangement, the state has fully transferred its participation to the organisation it established for this purpose and has defined in detail the conditions of its operation. The only way in which the state (the Ministry of Finance) participates is that the Minister of Finance nominates a representative of the Ministry as a member of the examining boards. The ministry representative is always the chairman of the examining board and has the casting vote there.

The new draft Act on Auditors, which is expected to enter into force on 1 January 2001, should ensure full compatibility with European legislation in this area. In contrast with the present arrangement, it proposes more

exact definitions of the auditing activities and other services provided by auditors and auditing firms, a change in the system of examinations, more extensive regulation of the obligations of auditors and auditing firms, and a new delineation of the competencies of the Chamber of Auditors as the self-governing professional organisation of all auditors and of the Ministry of Finance as the body of state oversight. The authority of the state is likely to be greater than it has been to date, especially as regards entry into the profession (auditors' examinations) and oversight of the lawfulness of the professional regulations.

Also necessary is the rapid removal of "discrimination" whereby under the present Act the Chamber can only register in the list of auditors a legal entity in which at least 60% of the shares or voting rights belong to auditors who are citizens of the Czech Republic.

One of the most important changes with regard to the banking sector is the extension of the auditor's obligations to include the duty to notify the body of state oversight or banking supervision without delay whenever the auditor believes that there has been a breach of the special legal regulations governing the activities of the accounting units in question or if the auditor uncovers any information which has or may have a negative effect on their finances or may lead to a statement other than "without reservations". This duty also applies in the event of uncovering any information concerning the relations between consolidated accounting units. The auditor is also obliged to notify without delay the statutory and supervisory body of the accounting unit in writing of any such information and of cases where he believes that an economic criminal offence, a criminal offence of bribery or any other criminal offence against property has been committed. In the aforementioned cases, the auditor's obligation to maintain confidentiality does not apply to notifying the bodies of state oversight and banking supervision.

#### 4. CO-OPERATION WITH OTHER FINANCIAL MARKET REGULATORS

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In keeping with the worldwide trend, financial groups headed mainly by banks are gradually beginning to form in the Czech Republic. These groups offer products comprising numerous instruments of the present financial market. Financial banking groups have a controlling share of the building savings market and also of the mortgage loan market. They have also gained a major share in the area of collective investment and pension insurance. They also participate to a significant extent in the leasing, factoring and insurance markets and in the real estate market. Likewise, the foreign banks operating in the Czech Republic are part of the financial groups of their parent banks, which in many cases have considerable international reach.

These trends are generating the need for consolidated supervision, which cannot be done without close co-operation with the other regulators of the financial market, both at the domestic and international level.

***In the international area***, the Czech National Bank focuses primarily on co-operation with the supervisors of those countries the banks of which have subsidiaries or branches on the territory of the Czech Republic or with those countries where, conversely, subsidiaries or branches of Czech banks operate.

In 1999 an agreement on co-operation was signed with the National Bank of Slovakia. This agreement concentrates primarily on the exchange of information on entities which intend to establish a new bank, with regard to proceedings for the granting of banking licences, on major changes in shareholder structure, serious shortcomings in activities, preliminary measures, remedial measures and penalties against those banks which have branches or subsidiaries in the second country. Besides this, the agreement also contains provisions relating to co-operation in the area of methodology – in the form of exchange of information on the prudential rules for banks and on the laws which affect the business activities of banks. As part of its inspection activity, one central bank may in well-founded cases ask the other to carry out an on-site examination in a foreign bank branch or subsidiary in the area in question. The bank must be informed about the performance of the examination and its outcome without undue delay.

Similar agreements are gradually being prepared with other, primarily European, countries. In 1999 an informal agreement was concluded with the German Federal Banking Supervisory Office. The conclusion of a formal agreement is debarred by the fact that under the present wording of the Act on Banks, foreign supervisors cannot perform on-site examinations in foreign bank branches or subsidiaries. This restriction will be lifted in the amendment to the Act on Banks currently under preparation. Official negotiations on potential co-operation have been also opened with the banking regulators of Austria, the Netherlands, the United Kingdom, France and Belgium.

**Within the Czech Republic**, the Czech National Bank co-operates closely with the Ministry of Finance, which is responsible for supervising the activities of insurance companies and pension funds, and the Securities Commission, which from the point of view of regulation supervises securities dealers, investment companies and investment funds. This co-operation is developing on the basis of a tripartite agreement concluded in 1998. The agreement concentrates chiefly on exchange of information, both in licensing activity and with respect to oversight of individual entities. The system of banking and other confidentiality is generating certain problems in this area, as the different practices of the individual regulators are restricting the scope of possible co-operation.

On the practical level, co-operation between the regulators at both the domestic and international level focused on Year 2000-related activities. There was a relatively frequent exchange of information between regulators regarding the Y2K preparedness of subsidiaries, foreign bank branches and other financial market participants.

International co-operation is not oriented solely on specific activities connected with the operation of foreign entities on the individual banking markets, but is evolving to an ever greater extent in the **methodological area** as well. Thanks to the advanced stage of development it has attained in recent years, the CNB banking supervisory authority is now invited to participate in various international working groups engaged in further improving the regulations, the practical exercise of banking supervision and so on.

Since 1997, for example, the CNB banking supervisory authority has been participating in the activities of the BIS "Core Principles Liaison Group", which is currently engaged in further elaborating the basic principles of banking supervision. Observance of these principles should guarantee the effective functioning of banking supervision in individual countries. Uniform evaluation of these principles among individual countries should reflect the quality of the banking supervisor and therefore also its reliability in regulating the relevant banking sector, which is of great importance given the present international scope of operation of financial entities. Another working group in which the CNB banking supervisory authority is involved is the "Transparency Group". This focuses on standardising the accounting regulations for the banking sector and on the disclosure of information on the activities of individual banks. The CNB banking supervisory authority contributes to the work of both the aforementioned groups by commenting on the documents of the Basle Committee on Banking Supervision. It actively participates in the meetings of the Core Principles Liaison Group.

In 1999 a new group – the "New Capital Accord Group" – was established. This focuses on further improving the regulations relating to capital adequacy, especially in the area of more accurate measurement of credit risk, recognition of a wider range of hedging instruments and regulation of residual and operational risks. Great emphasis is placed not only on the regulation of capital adequacy, but also on overseeing its observance and on market discipline.

The frequency of international contacts is increasing further, especially in connection with the preparations for the **accession of the Czech Republic to the European Union**. Last year, the CNB banking supervisory authority actively participated in screening the Czech legal and regulatory framework in the area of free movement of services and in comparing it with the relevant EU directives. The harmonisation requirements, however, relate not only to the legislative area, but also to other aspects, especially in the area of practical implementation of banking supervision. This is why in 1999, under the sponsorship of Phare, a twinning project was launched. The aim of this project is to check the methods and practical procedures used in the individual areas of banking supervision and to ensure their further development in line with international practice, with the help of experts from EU member countries. As part of this project, two foreign experts have been working at the



Czech National Bank since December 1999, one from Germany and one from Greece. The main areas this project is concentrating on are market risk, supervision on a consolidated basis, capital requirements based on the risk profiles of individual banks, financial analyses of banks, and on-site examinations. The project includes not only verification of the level of harmonisation with international practice, but also a number of training courses, seminars, consultations and internships for the staff of the CNB banking supervisory authority, which will raise their level of qualification in these areas.

The CNB banking supervisory authority also actively participates in the activities of the **Regional Group of Banking Supervisors from Central and Eastern Europe**. In 1999, the Group organised several seminars, with the Czech National Bank hosting one on capital adequacy incorporating market risk. The Group's annual conference was held in Ljubljana, Slovenia in May 1999. The subject of the conference was the evaluation of fulfilment of the Core Principles and the conditions for the operation of foreign bank branches on the domestic market and the supervision of such branches. The Czech Republic took over the chair of the Group for the year 2000 and was the host of its 13th Conference held in Prague in May 2000.

## 5. THE EXERCISE OF BANKING SUPERVISION

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The CNB's "Conception for the further development of banking supervision" concentrates in the practical area on strengthening on-site supervisory activities in banks, on gradually supplementing the "static" evaluation of banks with "dynamic" aspects and on standardising the procedures for both off-site surveillance and on-site examinations.

### 5.1 Off-site surveillance

Off-site surveillance chiefly involves regular evaluation of the positions of individual banks from the point of view of their observance of the prudential rules and their current financial situation. It also involves assessing all matters relating to the organisation of the bank, its shareholder structure, its management, its ownership links with other entities in both the financial and non-financial areas, external auditing and so on. The Act on Banks requires in a number of cases the prior consent or opinion of the Czech National Bank, especially in cases of acquisition of holdings in a bank upon reaching certain thresholds, amalgamation or merger of banks, extension of the banking licence to include additional activities and sale of a part of a bank. The CNB banking supervisory authority also gives recommendations to newly proposed members of banks' management and confirms the external auditors selected. Off-site surveillance in the Czech Republic also includes the assessment of banking licence applications.

The financial position of the bank and its compliance with the prudential rules are evaluated by individual inspectors in monthly analyses prepared in a standardised format. Any substantial changes in the bank compared with the previous period are contained in a system of signal information comprising proposals for further action to be taken against banks displaying negative trends. Such action may consist in the imposition of remedial measures, the performance of an on-site examination, the initiation of discussions with the bank's representatives or its major shareholders, etc. A rating of banks is prepared with quarterly periodicity. This rating evaluates in a uniform manner the situation in the bank from the point of view of prudential business and breaks down the banks into five groups according to the intensity of the problems the banks have to resolve in their activities.

In 1999, an automated information system was established. This is used chiefly for off-site surveillance. Its main component is the banking supervision information centre, which is a database for the regular evaluation of the banking sector and individual banks. In addition to the basic data, it contains a number of standard outputs and

calculated indicators which facilitate the necessary standardised approach towards evaluation and which bolster the effectiveness of off-site surveillance. The register of banks comprises basic, generally "non-numerical", information on each bank (for example its shareholder structure, the names of its managers, its holdings, etc.). The new register of banks allows supervisors *inter alia* to monitor changes over time and to check adherence to certain provisions of the Act on Banks. The ancillary products of the system are the register of the decisions of the CNB banking supervisory authority, which includes basic information on the individual actions of the supervisory authority vis-à-vis banks (i.e. on-site examinations, any measures imposed on the bank, penalties, any consents granted in accordance with the Act on Banks and the results of any interviews with the bank's managers), and the methodological support of the CNB banking supervisory authority, which comprises centralised interpretations of the prudential rules for banks. This enables efficient access to the methodological regulations and, in particular, ensures uniform interpretation of the individual provisions of these regulations.

The system currently provides a comprehensive database which significantly helps the CNB banking supervisory authority to fulfil its tasks. The entire system is conceived as an open one and will be further supplemented not only in terms of extending the database, but also as regards introducing further elements into the system.

Off-site surveillance also involves the imposition of measures on banks if they do not comply with the stipulated rules or display any other shortcomings in their activities. In 1999, standard remedial measures were applied in relation to eleven banks. In the event of more serious problems, documents were prepared for the CNB Bank Board containing proposals for the adoption of fundamental measures against banks. These measures consisted chiefly in banking licence revocations (e.g. Universal banka and Moravia banka).

In the course of 1999, the CNB's banking supervisory authority issued 17 administrative decisions. These chiefly involved extensions to banks' licences and acquisitions of holdings in banks. It also issued around another 90 decisions outside administrative proceedings. These consisted in the approval of banks' auditors, their shareholder structures ahead of general meetings, the inclusion of subordinated debt in their capital, and of consolidated bank entities in connection with the new CNB provision on supervision on a consolidated basis. The opinion of the CNB banking supervisory authority on persons proposed for managerial positions in banks was issued in 44 cases.

## **5.2 On-site examinations**

Examinations carried out directly in banks are an integral part of banking supervision in the Czech Republic. The aim of these is to discern the quality of the bank's management systems, its internal audit system, information systems and so on, i.e. those parts of the bank's activities which cannot be monitored by off-site surveillance. Given the risky environment prevailing in the Czech Republic, great attention is paid to checking the bank's credit portfolio, as credit risk is currently the biggest risk in banking.

The reorganisation of the CNB's Banking Supervision Group carried out towards the end of 1997 created the prerequisites for improving the quality of supervisory activities by forming special supervisory teams fully dedicated to this activity. Since mid-1999, three supervision teams have been operating, each composed of a head of team and six inspectors. The fourth supervision team has yet to be formed owing to a lack of quality staff. To ensure a uniform approach to on-site examinations, the most experienced inspectors have focused on updating and completing the methodology for the organisation of inspections and on the individual specialised areas on which the comprehensive on-site examinations in banks concentrate. During July and August 1999, the first version of this methodology was drafted. It comprises general on-site examination procedures, inspection of the assets and liabilities management system (paying special attention to the bank's system of financial management), management of market risks and any risks connected with trading on the financial markets, the bank's credit activities and its internal audit system. In addition, a test program environment was prepared for maintenance of the database for checking credit risk. This speeds up and improves work in the area of checking banks' credit portfolios.

Inspection activities in banks are carried out in three forms. Comprehensive on-site examinations focus on all the bank's areas of activity. Their number is generally limited by the number of inspection teams, as such examinations are time consuming and labour intensive, especially in the case of large banks. Partial examinations are selected in cases where it is necessary on the basis of certain negative signals – for example from off-site surveillance – to carry out a quick check of a specific activity which might be the source of problems. The last type of examination is the information visit, which involves a discussion with the bank's management about basic issues relating to the bank's activities, its development, envisaged changes and so on. These information visits take place either regularly between comprehensive on-site examinations in order to maintain continuity of contact with the bank, or, conversely, before a comprehensive on-site examination with the aim of clarifying certain organisational, technical and other matters and thus to ensure that the examination itself proceeds smoothly.

In 1999, the CNB banking supervisory authority carried out five comprehensive and two partial on-site examinations. Information visits took place in 26 banks and foreign bank branches, and in some of them repeatedly. Many of the checks implemented were still focused on evaluating the quality of the credit portfolio, as credit risk continues to be the biggest risk for banks. In keeping with international trends, however, the focus of the checks is gradually shifting towards assessment of the bank's risk management systems and its internal audit system.

In addition, emphasis was placed in 1999 on checking compliance with the reporting duty of banks in the extent stipulated by CNB Provision No. 2 of 29 June 1998 Stipulating the Minimum Requirements for the Disclosure of Information by Banks and Foreign Bank Branches. First, at the beginning of the year, the CNB banking supervisory authority conducted information visits, then in May, it conducted partial inspections at 154 locations in 29 banks. These controls focused exclusively on ascertaining whether the information on the banks was complete, up-to-date and accessible to the public.

Another important banking supervision tool is discussions with bank management. During 1999, a number of discussions were held with the top management of individual banks, and in the case of problem banks these discussions took place at regular intervals. Following the publication of financial statements and auditors' statements, the matters at issue were discussed at bipartite or tripartite meetings (depending respectively on whether the subject of the discussion was professional problems of general character or the specific situation of the bank in question). Likewise, meetings with the auditor, sometimes also attended by the bank, were organised upon assessment of the bank's performance report, which contains a description and evaluation of the bank's risk management system and its internal audit system. In connection with these meetings, certain problems, especially those relating to the role of the auditor in evaluating the risk management system and the internal audit system, were discussed in the specialised Chamber of Auditors group for the auditing of financial institutions.

## 6. THE YEAR 2000 ISSUE

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In view of its statutory responsibility for supervision of banking activities and care for the safe operation and purposeful development of the banking system in the Czech Republic, the Czech National bank also set about the task of helping ensure a problem-free transition into the year 2000 in the banking sector. From the outset, however, responsibility for the specific resolution of the Year 2000 (Y2K) issue and minimisation of the associated risks rested exclusively with the banks themselves, their owners and their management. The CNB banking supervisory authority actively participated in dealing with these problems, especially as regards the methodology for and stipulation of the individual steps that had to be taken in order to address the Y2K risk and as regards monitoring the progress of the preparations and the Y2K transition itself directly in banks.

When launching the work on initialising and monitoring the problem-free transition of the banking sector into the year 2000, it was necessary, as early as in 1997, to prepare a methodological procedure which later, in 1998

and 1999, would ensure achievement of the set target. This chiefly concerned the regulatory base, as well as the procedure for checking the preparedness of individual banks on site.

To address the Y2K issue, the following official regulations were prepared, approved and issued:

- Official CNB Communication of 5 June 1998 on Adjusting Information Systems and Other Automated Bank Systems to the Year Change from 1999 to 2000, containing instructions and recommendations on how to proceed in preparing bank systems for the year 2000 and a specimen declaration of the bank's Year 2000 compliance;
- Official CNB Communication of 2 September 1998 on the Year 2000 Issue, which focused on defining the Y2K problem;
- CNB Provision No. 4 of 29 September 1998 Stipulating the Requirements for the Bank Performance Report; this contained many adjustments for the year 2000, *inter alia* the obligation of external auditors to assess the bank's progress in dealing with the Y2K issue;
- CNB Provision No. 6 of 29 December 1998 Stipulating the Requirements for Ensuring the Safe Operation of Banks and Foreign Bank Branches with respect to the Year 2000 Risk; this focused on the range of obligations of banks in their Y2K preparations, including disclosure of their preparedness and a schedule of individual Y2K preparatory measures,
- Official CNB Communication of 14 December 1999 on Safeguarding the Smooth Transition of Banks into the Year 2000; this contained instructions for supplying banks with cash and the reporting duty of banks towards the CNB on any problems arising.

Most of the methodological preparation, as is evident from the dates of effect of the individual regulations, was implemented in 1998. By the end of 1998, the necessary regulatory base for the Y2K issue had been laid down and it was only in the fourth quarter of 1999 that the need for an additional official regulation became apparent. This document regulated the actions of the Czech National bank and the banking sector during the period of transition into the year 2000 itself, i.e. the period immediately before and after the change of year.

The following methods were selected for verifying the Y2K preparedness of banks:

- questionnaires addressing all banks, with their content updated and amended according to the current state of preparedness of the Czech banking sector, international experience and recommendations;
- on-site informative interviews in banks, with the aim being to visit all banks operating in the Czech Republic by 30 June 1999 and subsequently, up to the end of the year, to visit only the "critical" banks found to be insufficiently prepared.

In January 1998, a preparatory investigation into the banks' state of preparedness took place. This investigation consisted in sending out an initial questionnaire with 21 questions to all banks. Its purpose was to conduct a basic mapping of the problem. In the autumn of 1999, the first round of informative interviews took place in 23 banks, which were selected according to the results of the preparatory investigation. The aim of these visits was primarily to find out whether the banks were devoting sufficient attention to this issue and how far they had progressed in implementing the individual steps of the Y2K compliance programme. At the same time, a detailed questionnaire was sent to all banks. This questionnaire supplemented the necessary information from the banks which until that time had not been visited and updated the information from the banks which had been visited. This first questionnaire, containing 71 questions altogether, broken down into ten subject groups, expanded and updated the previous enquiries. It also included further suggestions of the Basle Committee on Banking Supervision, adjusted to the situation in the Czech banking sector.

In the second quarter of 1999, a second round of informative interviews took place. Its orientation was similar to that of the first round, but this time special emphasis was placed on the preparation of contingency plans. The interviews were conducted in 31 banks, with selection priority being given to those banks which until then had not been visited and, of the visited banks, to those which were of major significance to the Czech banking sector. The remaining 12 banks, which were visited in the first round, were sent a second questionnaire with 88 questions, the wording of which was further updated. During the third and fourth quarters of 1999, the activity of the CNB banking supervisory authority in this area was focused on the "critical" banks, i.e. those whose evaluation was lower than the overall average for the banking sector. In this third and final round, another 21 informative interviews took place. These concentrated on individual and specific problems of the preparedness of selected banks. All supervisory activities were concluded at the beginning of December 1999.

By the end of June 1999, the banks had also fulfilled their obligation to inform the public of the Y2K compliance of their automated systems. Most banks used their websites for this purpose, and a number of them also published paid advertisements in the daily and trade press or made their declaration available to the Czech Press Agency (CTK). The public was thus well informed as early as at the beginning of July 1999 about the advanced stage of Y2K preparedness of the banking sector.

Altogether, 75 on-site interviews were conducted in banks during 1998 and 1999. Every active bank in the Czech banking sector was visited at least once. The results of the questionnaires and informative interviews were evaluated on a regular basis and discussed with the banking community at joint meetings organised in co-operation with the Banking Association.

The Czech National Bank also organised Y2K compliance tests of the connections between the CNB Clearing Centre and individual banks. These tests proved to be a kind of culmination of the Y2K preparations of the entire Czech banking sector. All banks participated in these tests and the results were evaluated as satisfactory. Similar tests, in which the Czech banking sector took an active part, were also organised by the Prague Stock Exchange and by the international organisations VISA and SWIFT.

In addressing the Y2K issue, the CNB banking supervisory authority co-operated closely with other institutions on both the domestic and international level. The main line of co-operation was established with the Banking Association, with which targeted seminars on this issue were organised for the banking sector. The Banking Association also began to release Y2K information on the Internet and made contact with the associations of various financial institutions in order to co-ordinate individual activities.

During 1998 and 1999, there was also co-ordination and mutual exchange of information with the Securities Commission and the National Co-ordination Centre (ÚSIS). The CNB banking supervisory authority addressed the home country supervisors of banks operating in the Czech Republic and the host country supervisors of Czech banks in order to gain information on their approach to this issue and to set the role of "lead supervisor" for foreign bank branches operating in the Czech Republic and for branches of Czech banks operating abroad.

In December 1999, it was possible to state, on the basis of concrete results, that the banking sector had come close to the highest tier of predicted Y2K preparedness. The banks' Y2K contingency plans and business continuity plans covered any residual risk. The concluding event was the verification of the course of the Y2K transition itself, using a special questionnaire to monitor any potential problems. No bank, however, recorded any difficulties with its information systems on the critical day or during the following days, so it was possible to state that **the transition into the year 2000 in the Czech banking sector proceeded without any problems.**

# B.

## THE DEVELOPMENT OF BANKING PRODUCTS AND SERVICES IN THE CZECH REPUBLIC

The banks operating in the Czech Republic are universal banks providing a full range of banking products and services. At the beginning of the 1990s, when the Czech banking sector started to form, the circle of products and services it provided was very narrow, concentrating only on the classic forms, especially in the deposit and credit areas. Over time, however, the banks began to improve their services. The entry of foreign banks and foreign bank branches into the Czech banking sector has contributed significantly to this process.

### 1. BANKING PRODUCTS AND INNOVATIONS

The structure of banking products and services depends to a great extent on the type of clientele the bank intends to serve. Ensuring maximum client satisfaction becomes the decisive element in the competition for clients. Only those banks which provide a full range of banking services and other services within the framework of a financial group can expect to attract new clients.

#### 1.1 Services for the public

Banks are currently focusing to an ever greater extent on small clients, who are less risky than corporate clients, especially under the present economic conditions in the Czech Republic.

In the Czech Republic, deposit books continue to be the traditional product in the area of deposits. However, the banks are beginning to orient themselves increasingly towards registered deposit books. This is in keeping with the alignment of the Czech legislation with European Community law, which requires elimination of anonymous banking accounts. Anonymous deposit books are still offered by eight banks, while twelve provide registered deposit books and eight intend to introduce this service. Savings accounts, which combine some of the advantages of current accounts with higher interest rates approaching the level of interest rates on time deposits, are offered by 14 banks.

With regard to retail banking, the banks are endeavouring to offer some new and better products for clients. For example, as regards maintaining current accounts, 23 banks are now able to transfer funds on a koruna account to an account with better interest rate if the balance exceeds a set limit. A total of 15 banks offer this possibility on current foreign currency accounts as well. Preferential forms of saving for selected groups of clients, especially children, young people and students, are also gradually expanding. Six banks offer this service, and another six intend to introduce it in the future.

**TABLE 1** SELECTED PRODUCTS AND SERVICES FOR THE PUBLIC  
for banks with licences as of 31 Dec. 1999

| SERVICE OR PRODUCT                                 | YEAR OF LAUNCH |         | DEGREE OF UTILISATION | DEGREE OF FURTHER DEVELOPMENT | NUMBER OF BANKS | BANKS INTENDING TO INTRODUCE THE SERVICE OR PRODUCT |
|--|----------------|---------|-----------------------|-------------------------------|-----------------|---|
|  | FIRST          | AVERAGE |                       |                               |                 |   |
| Savings accounts                                   | 1991           | 1994    | 2.6                   | 2.7                           | 14              | 2   |
| Registered deposit books                           | 1991           | 1994    | 2.8                   | 2.3                           | 12              | 8   |
| Preferential saving for selected groups of people  | 1993           | 1996    | 2.8                   | 2.7                           | 6               | 6   |
| Intelligent CZK account                            | 1991           | 1995    | 2.7                   | 2.5                           | 23              | 2   |
| CZK account with overdraft facility                | 1990           | 1993    | 2.9                   | 2.5                           | 30              | 8   |
| Spot payments in CZK                               | 1990           | 1994    | 2.5                   | 2.4                           | 32              | 6   |
| Intelligent foreign currency account               | 1991           | 1995    | 2.6                   | 2.5                           | 15              | 3   |
| Foreign currency account with overdraft facility   | 1990           | 1993    | 2.7                   | 2.3                           | 20              | 2   |
| Spot payments in foreign currencies                | 1990           | 1994    | 2.5                   | 2.3                           | 25              | 3   |
| Credit lines for natural persons                   | 1992           | 1996    | 2.6                   | 2.6                           | 11              | 3   |
| Consumer cash loans                                | 1959           | 1994    | 2.6                   | 2.7                           | 14              | 2   |
| Preferential credits for selected groups of people | 1993           | 1996    | 2.4                   | 2.7                           | 6               | 3   |

Degree of utilisation = 1 to 4, where 1 represents minimum utilisation and 4 maximum utilisation

Degree of further development = 1 to 3, where 1 represents a winding down, 2 the present state and 3 further improvement and development

New products are also emerging in the credit area. Consumer cash loans are offered by 14 banks. There are also preferential credits for specific groups of people, for example student credits, which are offered by six banks, while another three intend to become involved in this area in the future. Since as early as 1992, some banks have also been allowing natural persons to draw credits operatively on the basis of an approved credit line. Eleven banks currently provide this service, and another three intend to introduce it in the near future.

## 1.2 Services for the business sector

The business sector continues to be the primary type of client for the banking sector in the Czech Republic. In addition to the basic products connected with classic lending and administration of deposits, banks are to an ever greater extent beginning to develop special banking products and services for businesses.

In the area of investment banking, banks arrange new issues of securities for companies. A much used and frequently offered (by 25 banks) standard product in the area of deposit products and services continues to be deposit bills of exchange, which thanks to their exceptional tax status represent an advantageous deposit instrument, especially for profit-making legal entities.

**TABLE 2** SELECTED PRODUCTS AND SERVICES FOR THE BUSINESS SECTOR  
for banks with licences as of 31 Dec. 1999

| SERVICE OR PRODUCT                                   | YEAR OF LAUNCH |         | DEGREE OF UTILISATION | DEGREE OF FURTHER DEVELOPMENT | NUMBER OF BANKS | BANKS INTENDING TO INTRODUCE THE SERVICE OR PRODUCT |
|--|----------------|---------|-----------------------|-------------------------------|-----------------|---|
|  | FIRST          | AVERAGE |                       |                               |                 |   |
| Trading in securities for clients on foreign markets | 1994           | 1997    | 2.4                   | 2.8                           | 16              | 3   |
| Trading in T-bills or CNB bills for clients          | 1990           | 1995    | 2.6                   | 2.5                           | 20              | 1   |
| Trading in financial derivatives for clients         | 1991           | 1995    | 2.2                   | 2.7                           | 18              | 2   |
| Management of asset portfolios                       | 1993           | 1996    | 2.7                   | 2.8                           | 12              | 3   |

Degree of utilisation = 1 to 4, where 1 represents minimum utilisation and 4 maximum utilisation

Degree of further development = 1 to 3, where 1 represents a winding down, 2 the present state and 3 further improvement and development

Trading in securities on foreign markets on behalf of clients is arranged by 16 banks. Trading in T-bills is offered by 20 banks, while 18 banks trade for their clients in financial derivatives and 12 banks offer their clients comprehensive asset portfolio management. Trading in T-bills for bank clients was introduced on average at the beginning of 1995 and trading in financial derivatives at the end of the same year, whereas trading on foreign markets appeared on average later, only in the second half of 1997, even though some banks had been offering this service to selected clients since 1994. Management of individual asset portfolios for clients was introduced onto the market in 1993.

The banks are intending to develop this relatively young area of banking services. Other banks are considering adding these services to the range they offer, especially as regards comprehensive portfolio management. For all the investment banking and money market products and services under review, more and more banks are intending to offer them to their clients.

## 1.3 Other companies' products offered by banks

Another way in which banks can retain their market share and gain a competitive edge is to offer non-banking financial products on their premises, a phenomenon which has started to become widespread in the Czech economy. In most cases, the products and services concerned are provided by the subsidiaries and associated companies of the bank. However, the products and services of independent contractual partners are by no means the exception, either.

**TABLE 3** OTHER COMPANIES' PRODUCTS OFFERED BY BANKS  
for banks with licences as of 31 Dec. 1999

| SERVICE OR PRODUCT                                | YEAR OF LAUNCH |         | DEGREE OF UTILISATION | DEGREE OF FURTHER DEVELOPMENT | NUMBER OF BANKS | BANKS INTENDING TO INTRODUCE THE SERVICE OR PRODUCT |
|---|----------------|---------|-----------------------|-------------------------------|-----------------|---|
|   | FIRST          | AVERAGE |                       |                               |                 |   |
| Building savings                                  | 1993           | 1995    | 2.6                   | 2.4                           | 13              | 2   |
| Supplementary pension insurance                   | 1994           | 1996    | 2.4                   | 2.6                           | 9               | 8   |
| Life insurance                                    | 1994           | 1995    | 2.3                   | 2.8                           | 5               | 6   |
| Other insurance                                   | 1994           | 1997    | 2.6                   | 2.7                           | 9               | 3   |
| Leasing   | 1991           | 1995    | 2.3                   | 2.4                           | 6               | 2   |
| Sale and repurchase of participation certificates | 1991           | 1995    | 3.2                   | 2.8                           | 10              | 3   |

Degree of utilisation = 1 to 4, where 1 represents minimum utilisation and 4 maximum utilisation

Degree of further development = 1 to 3, where 1 represents a winding down, 2 the present state and 3 further improvement and development

Banks of all groups have been offering building savings as a parallel product since 1993, when this product was launched in the Czech Republic. Six building savings banks focus on this activity in the Czech Republic and co-operate with other banks on the Czech banking market. Building savings products are intermediated by thirteen banks (in addition to the building savings banks) and another two banks are preparing to launch this service within the short term.

Banks began to broker supplementary pension insurance with state contribution in 1994; at present, nine banks provide this service, while another eight are planning to introduce it. Insurance brokering first appeared as part of the range of banking services in 1994. Nine banks offer non-life insurance, while only five currently offer life insurance, although another six intend to become involved in this area. Leasing intermediation was launched as early as 1991; today it is offered by six banks, while another two are planning to introduce it. Sale and purchase of participation certificates (unit trust units) also began in 1991; ten banks currently offer this service. Together with building savings, intermediation of open-end mutual funds is thus becoming another of the most frequently offered intermediated services.

Some banks are now considering how to get as close to the client as possible in the places where the client really needs them, in the form of financial kiosks located, for example, in department stores. A continuation of this trend may be the possibility of direct co-operation between banks and retailers, with the latter arranging credit lines for their customers. The conditions for this shift towards the client have been created above all by the development of the Internet, through which retailers and other non-traditional providers of financial services will be able to verify the financial status and credit history of the client.

Some banks see another way to enlarge their range of services in switching from the present trend whereby they try to sell clients their existing products and services, to a new trend whereby banks will adapt to their clients' needs, helping them to address their specific needs and advising on all the specific options for so doing.

## 1.4 Operations linked with receivables, collateral and hedging

Credit transactions are the most widely used service in the Czech banking sector. Associated with these is a whole range of operations relating to their collateralisation, appraisal and recovery. One of the most widespread solutions to problem credits is the sale, purchase and recovery of debt; the sale of debt is undertaken by thirteen banks, the purchase of debt by twelve banks and debt recovery by ten banks. The first of these transactions to be launched was debt recovery – in 1990. A year later the banks started to sell and purchase debt. Only three banks appraise their receivables themselves at present; the others co-operate in these areas with specialised entities.

**TABLE 4** OPERATIONS LINKED WITH RECEIVABLES, COLLATERAL AND HEDGING  
for banks with licences as of 31 Dec. 1999

| SERVICE OR PRODUCT       | YEAR OF LAUNCH |         | DEGREE OF UTILISATION | DEGREE OF FURTHER DEVELOPMENT | NUMBER OF BANKS | BANKS INTENDING TO INTRODUCE THE SERVICE OR PRODUCT |
|--------------------------|----------------|---------|-----------------------|-------------------------------|-----------------|---|
|                          | FIRST          | AVERAGE |                       |                               |                 |   |
| Appraisal of receivables | 1993           | 1996    | 3.3                   | 3.0                           | 3               | 1   |
| Sale of debt             | 1991           | 1995    | 2.5                   | 2.4                           | 13              | 1   |
| Purchase of debt         | 1991           | 1994    | 2.0                   | 2.1                           | 12              | 2   |
| Debt recovery            | 1990           | 1993    | 3.4                   | 2.8                           | 10              | 0   |
| Credit derivatives       | 1992           | 1995    | 1.3                   | 2.4                           | 3               | 3   |

Degree of utilisation = 1 to 4, where 1 represents minimum utilisation and 4 maximum utilisation

Degree of further development = 1 to 3, where 1 represents a winding down, 2 the present state and 3 further improvement and development



Gradually, however, new forms of hedging and administering of credit transactions are beginning to appear. These chiefly concern primary securitisation, whereby the importance of refinancing through traditional credit contracts is decreasing and the volume of funds allocated through securities is increasing. In 1999, some operations relating to secondary securitisation of assets were also initiated; these involve converting credits into securities. Unlike the classic securitisation of high quality assets, however, these operations were intended to solve the problem credits granted by some banks. Another possibility is credit derivatives, which, like credit insurance, minimise credit risk even before the credit is granted by transferring it to a third person, i.e. to the partner in the credit-derivative contract. Only three banks currently use credit derivatives; three others intend to implement this type of transaction in the near future.

## 2. COMPUTER AND TELECOMMUNICATIONS TECHNOLOGY AND ELECTRONIC BANKING

A necessary prerequisite for the rationalisation and streamlining of banking activities is the continuous development of computer and telecommunications technology. The banks' aim is to maintain and further develop the quality of the services they provide. Modern technology is used very actively by all participants in the banking market, not only for their own trading, settlement, processing of information and management, but also to save time and increase the convenience of their products and services for their clients. It is also used in the supervision and regulation of the banking sector. The unceasing innovations on the banking product market and the globalisation of banking markets are also conditioned by the state of the art in computer and communications technology.

### 2.1 Payment cards

The most widespread products in electronic banking are payment cards. These have various forms and functions, starting with identification cards, through electronic purses and debit cards to credit cards valid not only in the Czech Republic, but also abroad. Some banks also issue cards usable only upon entering a personal identification number (PIN); even though the possibilities for using these cards are limited, they have better protection against fraud. This type of card is offered mainly in programmes for children and young people. Clients may choose cards from several international payment systems, the most common in the Czech Republic being the cards of the two banking systems EuroPay/MasterCard and Visa.

**TABLE 5** ATMs AND PAYMENT CARDS  
for banks with licences as of 31 Dec. 1999

|                      | 1997      | 1998      | 1999      |
|----------------------|-----------|-----------|-----------|
| Number of ATMs       | 1 285     | 1 366     | 1 447     |
| Payment cards, total | 1 484 484 | 1 852 765 | 2 791 024 |
| <i>of which:</i>     |           |           |           |
| credit cards         | 594       | 3 250     | 5 851     |
| cards valid abroad   | 115 990   | 202 549   | 858 937   |
| electronic purses    | 2 892     | 21 215    | 236 089   |
| cards using PIN only | 580 545   | 523 019   | 481 404   |

As of 31 December 1999, the banks operated 1,447 ATMs, an increase of 81 on the previous year. The rapid development of automated banking is particularly visible in the growth in the number of payment cards issued. As of 31 December 1999, this number was 2.8 million, 50.6% higher than a year earlier. By type, payment cards that can be used outside the Czech Republic predominate. As of 31 December 1999, this type of card accounted for 30.8% of the overall volume of payment cards. This type of card has also shown the greatest development in comparison with the previous year. A similar trend was seen for electronic purses, the number of which had reached around 236,000 as of 31 December 1999. The structure of payment cards by type overlaps in certain aspects, as for example both credit cards and certain PIN cards can be used abroad, and all cards are equipped with a security system, which many cases is similar to a PIN.

The number of credit cards is also steadily rising. As of 31 December 1999, it had reached around 5,800. The volume of credits on credit cards amounted to CZK 207.3 million as of 31 December 1999, compared with only CZK 35.7 million a year earlier. Further growth in the volume of credits granted in this way can be expected, in spite of the fact that some banks grant credits on credit cards only on a monthly basis and require repayment of the credit as of the last day in the month.

**TABLE 6** USE OF PAYMENT CARDS  
for banks with licences as of 31 Dec. 1999

|  | 1997   | 1998   | 1999   |
|--|--------|--------|--------|
| Number of withdrawals from ATMs per year in thousands                      | 44 173 | 55 515 | 65 682 |
| Average withdrawal amount in CZK   | 2 167  | 2 249  | 2 794  |
| Number of direct payments for goods and services per year in CZK thousands | 1 087  | 1 788  | 4 071  |
| Average CZK payment amount   | 2 697  | 2 402  | 2 457  |

The most common form of use of payment cards in the Czech Republic continues to be cash withdrawals from ATMs. In 1999 there was a total of 65.7 million withdrawals, 18.3% more than in 1998 and almost 50% more than in 1997. The average amount withdrawn through ATMs is also on the increase; since 1997 this amount has gone up by CZK 627 to CZK 2,794. The average amount for direct payments for goods and services by payment card is somewhat lower; in 1999 this was just under CZK 2,500, a decrease of more than CZK 200 compared with 1997. This decrease is connected with the expansion in the network of shops and services which accept these cards and allow payment by card even for minor items. In 1997, payment by card was rather an exceptional and exclusive matter, which is also evidenced by the growth in the number of payments. Over the last two years, this number has almost quadrupled to more than 4 million. Nevertheless, the number of direct payments is only about 6% of the number of ATM withdrawals.

## 2.2 Electronic banking

The development of electronic banking is currently one of the main new trends in world banking. The Czech Republic, too, is witnessing a great upsurge in these services, which allow clients to gain quick access to their accounts without having to visit the bank. An obvious advantage for banks is the possibility of reducing their operating expenses.

The simplest form of direct banking close to electronic banking is callbanking. This involves the client communicating by telephone with a bank employee, who on the basis of his instructions executes the relevant operations. In the Czech Republic, this banking service began to develop in 1996. As of 31 December 1999, twelve banks operated such a service, and another five planned to introduce one in the near future. Clients use callbanking relatively extensively, so the banks are planning further developments and improvements to this service.

**TABLE 7** ELECTRONIC BANKING  
for banks with licences as of 31 Dec. 1999

| SERVICE OR PRODUCT | YEAR OF LAUNCH |         | DEGREE OF UTILISATION | DEGREE OF FURTHER DEVELOPMENT | NUMBER OF BANKS | BANKS INTENDING TO INTRODUCE THE SERVICE OR PRODUCT |
|--------------------|----------------|---------|-----------------------|-------------------------------|-----------------|---|
|                    | FIRST          | AVERAGE |                       |                               |                 |   |
| Callbanking        | 1996           | 1998    | 3                     | 2.7                           | 12              | 5   |
| Homebanking        | 1990           | 1995    | 3.2                   | 2.8                           | 27              | 2   |
| GSM banking        | 1998           | 1999    | 3.3                   | 3                             | 3               | 9   |
| Internet banking   | 1998           | 1999    | 3.6                   | 2.9                           | 3               | 17  |

Degree of utilisation = 1 to 4, where 1 represents minimum utilisation and 4 maximum utilisation

Degree of further development = 1 to 3, where 1 represents a winding down, 2 the present state and 3 further improvement and development

Homebanking, which involves a fixed link or ordinary telephone link between the client's personal computer and the bank's system and allows selected operations to be performed without the assistance of the bank's employees, was introduced by the first bank in 1990. In the Czech Republic, 27 banks allow their clients to use such a service, and another two plan to introduce it. This type of electronic banking is currently the most widespread and the banks envisage further development of this product.

Internet banking and GSM banking are the latest trend in electronic banking. Internet banking and GSM banking involve the client becoming a part of the bank's information system through a personal computer or mobile

telephone connected to the Internet or the GSM network. All operations are entered into the system directly, without the participation of the bank's employees. Czech banks only recently began to offer these services, which are dependent to a considerable extent on the development of the Internet and the mobile telephone networks, which is why they are not widely used yet. As of 31 December, three banks were offering Internet banking and three banks GSM banking. However, 17 banks plan to introduce Internet banking and nine banks GSM banking in the near future, and these services have marked priority in the development of banking services.

As of 31 December 1999, around 293,600 clients were using some form of electronic banking. In comparison with 1998, their number had quadrupled, and it can be expected to continue rising thanks to the foreseen development of electronic banking.

# C.

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## BASIC TRENDS IN THE BANKING SECTOR

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### 1. THE ECONOMIC AND LEGAL ENVIRONMENT IN 1999

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In 1999, the activities of the banking sector were significantly influenced by the real economy, where, starting in 1997, there occurred a slowdown in economic growth. Even though certain signs of recovery emerged, especially towards the end of 1999, most of the year was characterised by continuing recession with a knock-on effect on the business sector and thus also on the activities of the banking sector.

Gross domestic product decreased in 1999 by 0.2% in comparison with 1998. Most of the decrease occurred during the first half of the year, whereas in 1999 Q4, GDP showed a year-on-year increase of 1%. The upturn in GDP was largely due to domestic demand, which contributed 1.2 percentage points to the growth.

Inflation was 2.1% in 1999. The favourable development of inflation factors made possible a further decrease in basic interest rates. The discount rate was reduced from 7.5% as of 23 December 1998 to 5% as of 27 October 1999. The two-week repo rate was lowered in the same period from 9.5% to 5.25% as of 26 November 1999. The Lombard rate, which stood at 12.5% at the end of 1998, was 7.5% from 27 October 1999 onwards. In 1999, there was also a major reduction in the reserve requirement, which was 7.5% at the end of 1998 and, after two decreases in January and October, only 2% at the end of 1999.

From 1999 Q2 onwards, the Czech koruna gradually appreciated against the euro. This trend was connected with the continuing inflow of foreign direct investment and with the expectation of further inflow of capital owing to the Government's decision to speed up the privatisation process. The appreciation pressures were interrupted at the beginning of Q4 by the CNB's foreign exchange market interventions. From mid-October onwards, however, the koruna's nominal appreciation trend against the euro resumed.

The unfavourable trend in the business sector continued into 1999. This showed up in a decrease in industrial production and construction output, leading to a deterioration of the situation in a number of businesses, which were unable to generate sufficient funds to repay the credits granted to them. This strongly affected the activities of the banking sector, which responded primarily by adopting a tighter approach towards lending in an effort to eliminate potential future problems with poor quality assets.

In addition to economic influences, the legal environment significantly affects the activities of the banking sector. In 1999, there was no significant shift towards improving the legislative framework, especially as regards the position of creditors, enforcement of collateral, inflexibility of bankruptcy proceedings and so on. However, amendments to the appropriate acts were prepared in an effort to solve these problems. These entered into force in 2000. Their contribution towards increasing the stability of the banking sector will thus not be felt until 2000.

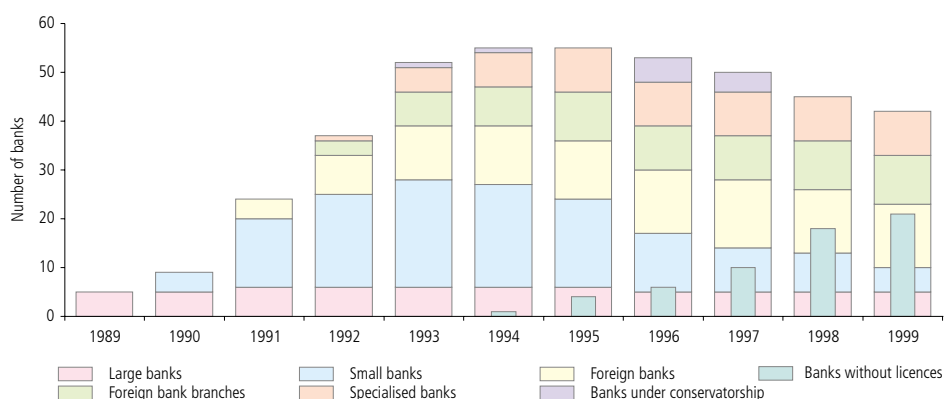
## 2. THE STRUCTURE OF THE BANKING SECTOR IN THE CZECH REPUBLIC<sup>1)</sup>

### 2.1 Number of banks

As of 31 December 1999, the Czech banking sector consisted of 42 banks and foreign bank branches. During the course of 1999, three banks from the group of small banks had their banking licences revoked. The revocation of the licences of Universal banka and Moravia banka was due to their non-compliance with the prudential rules. After transferring most of its activities to another bank, Foresbank decided not to continue its banking activities and asked for revocation of its banking licence. As of 31 December 1999, no banks were operating under conservatorship. No new banking licences were granted in 1999.

**CHART 1** NUMBER OF BANKS BY GROUP

for banks which had started client operations as of 31 Dec. of the given year



Since 1990, there have been major changes in the number of banks operating actively on the market. Many of the newly established banks, especially those with private Czech capital, were unable to cope with the risky conditions of the economic transformation and were forced to terminate their activities. The tightening of the conditions for granting licences to new banks after 1996 restricted the entry of new entities into the sector. The structure of the banking sector has recently also been affected by mergers of individual banks, leading to concentration of the banking sector.

Between 1989 and the end of 1999, a total of 63 banking licences were granted, of which 21 were later revoked. Of this number, 16 were revoked because of the poor financial situation of the bank in question and its non-compliance with the prudential rules. Four licences were revoked owing to mergers or sales, and one bank failed to start operating within the deadline stipulated by law.

### 2.2 Ownership structure

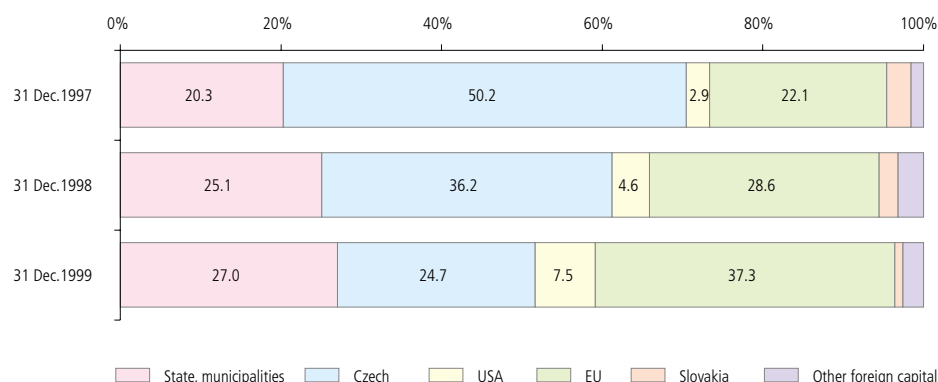
(for banks with licences as of the given date)

According to the Act on Banks, the only permissible legal form of a bank of the commercial type in the Czech Republic is the joint-stock company, unless the bank concerned is a foreign bank branch – which does not have legal entity status – or a state financial institution. The ownership structure is expressed as the share in the equity capital of the joint-stock company. Both legal and natural entities may become shareholders of a bank, regardless of their country of residence or domicile. If, however, their share exceeds 10% of the capital of the bank, they must meet the conditions stipulated by the Czech National Bank in accordance with the Act on Banks.

1) In order to record the different developments in individual segments of the banking sector, the banks are divided into five groups according to the amount of their total assets, origin of their capital and their specialisation. A detailed survey of the groups by individual bank is given in the Appendix.

**CHART 2** BANK OWNERSHIP STRUCTURE

for banks with licences as of the given date



The changes in ownership structure<sup>2)</sup> over time reflect the differing intensity of equity capital increases with respect to domestic and foreign investors. Other important factors in the changes in ownership structure include sales and purchases of holdings, among the most important of which are the sales of state stakes in the large banks within the privatisation process, and also changes in the number of banks. In the latter case, licence revocations due to non-fulfilment of the prudential requirements led to a decrease in the ownership share of Czech private capital. This chiefly concerned small banks.

In 1999, the **banking sector privatisation process** continued. The sale of the state stake and CNB stake in Československá obchodní banka (CSOB) to KBC Bank of Belgium was completed in mid-1999. Intensive preparatory work also continued for the sale of the state's majority in Česká spořitelna to Erste Bank Sparkassen of Austria. This sale took place at the beginning of 2000. Work also began on the privatisation of the state stake in Komerční banka. This institution is expected to be sold by the end of 2000. The privatisation of Komerční banka should essentially complete the privatisation of the banking sector; the state will retain its stakes only in a number of specialised banks specifically oriented towards financing government programmes in the areas of export, support for small businesses, administration of poor quality assets, etc. A specific solution has been selected for the sole state financial institution in the Czech banking sector, Konsolidační banka, which concentrates on the administration of poor quality assets transferred to it from other banks as part of the consolidation of the banking sector. These transfers took place mainly at the beginning of the formation of this sector, and more recently in connection with the privatisation of the large banks.

In spite of the ongoing privatisation process, the share of the state and municipalities in the total equity capital of the banking sector increased by 1.9 percentage points to 27.0% in 1999. This is the result of increases in equity capital at the large banks ahead of their privatisation. The impact of these increases on the total volume of the state share was, however, reduced by the completion of the privatisation of Československá obchodní banka, which was sold to a foreign investor; conversely, this was reflected in a marked increase in the proportion of foreign ownership. Czech private capital saw the largest reduction in share in 1999, falling from 36.2% at the end of 1998 to 24.7% as of 31 December 1999. The reasons for this were the revocation of the banking licences of more banks with predominantly Czech private capital and the smaller contribution of these entities to the equity capital increases at other banks.

The share of foreign entities in the total equity capital of the banking sector was 48.4% as of 31 December 1999, 9.6 points higher than a year earlier. By country, European Union member states accounted for the largest proportion, with a 77.2% share of the total volume of foreign equity capital, followed by the USA with 15.5%. European Union states had 37.3% of the total equity capital of the banking sector as of 31 December 1999, which represents annual growth of 8.7 points, and the USA had 7.5%, up 2.9 points on a year earlier. A further

2) In 1999, the methodology for monitoring holdings in banks was tightened. This methodology now allows all shareholders to be registered. Until 1998, only shareholders whose shares exceeded the stipulated limits, taking into account both the percentage share of the equity capital or voting rights and the amount of the equity capital invested, were monitored. The change in the methodology may affect the exactness of the figures, but not the basic trends.

increase in the share of foreign capital in the banking sector will occur in 2000 upon completion of the privatisation of the state stakes, as these banks either have been or are to be sold to major foreign banks.

### 2.3 Employees and banking units

(for banks with licences in the given year)

Since 1995, a marked tendency towards increased efficiency has been seen in the Czech banking sector. A reflection of this tendency is the dramatic decrease in the workforce and banking units serving bank clientele in recent years. This development has been facilitated, *inter alia*, by the gradual development of banking services which do not require a large amount of human labour, especially the various forms of electronic banking, payment cards and so on.

As of 31 December 1999, 49,355 people were working in the banking sector, 5.9% fewer than a year earlier and 18.8% fewer than in 1995, when the workforce in the banking sector peaked. The number of banking units decreased by 9.6% to 2,006 in 1999, and was down by 42.1% in comparison with 1994, when the number of banking units peaked.

**TABLE 8** NUMBER OF EMPLOYEES AND BANKING UNITS IN THE BANKING SECTOR  
for banks with licences as of the given date

|                                       | 31 DEC. 1994 | 31 DEC. 1995 | 31 DEC. 1996 | 31 DEC. 1997 | 31 DEC. 1998 | 31 DEC. 1999 |
|---------------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Number of employees                   | 58 755       | 60 819       | 59 959       | 53 785       | 52 475       | 49 355       |
| Number of banking units               | 3 465        | 3 411        | 3 172        | 2 467        | 2 220        | 2 006        |
| Number of employees per bank          | 1 068        | 1 106        | 1 131        | 1 076        | 1 166        | 1 175        |
| Number of employees per banking unit  | 17           | 18           | 19           | 22           | 24           | 25           |
| Number of population per bank         | 187 876      | 187 661      | 194 512      | 205 983      | 228 658      | 244 717      |
| Number of population per banking unit | 2 982        | 3 026        | 3 250        | 4 175        | 4 635        | 5 124        |
| Number of population per employee     | 176          | 170          | 172          | 191          | 196          | 208          |

The most marked changes occurred in the group of large banks, which in 1999 accounted for 64.7% of the overall drop in the number of employees and for 53.9% of the decrease in banking units. The number of employees in foreign banks and foreign bank branches was 6,489 as of 31 December 1999, 2.4% lower than a year earlier. Conversely, the number of banking units decreased during the same period by 6.3% to 343. Growth in the number of employees and expansion of the branch network was also recorded for specialised banks, including building societies, where between 1995 and the end of 1999 the workforce increased by 67.3% to 2,249 and the number of banking units rose by 75% to 70.

The differences between the personnel and organisational structure of the individual groups of banks stem primarily from their different focuses of activity. Foreign banks orient themselves chiefly towards wholesale banking, which is less demanding as regards both personnel and organisation. This is reflected above all in the comparison of total assets per employee. In foreign banks and foreign bank branches, this ratio is almost 2.5 times higher than in the group of large banks. A similar difference can be seen when comparing the networks of banking units and the total assets managed. For the large banks the average amount per banking unit was CZK 1.1 billion, whereas for foreign banks and foreign bank branches it was CZK 2.0 billion.

The more substantial decrease in the number of banking units in comparison with the number of staff is related to the liquidation of small workplaces and the gradual concentration of banking services into larger organisational units. In 1995 there had been 18 employees per banking unit, whereas at the end of 1999 the number was 25. The rationalisation of branch networks has been facilitated to a considerable extent by the development of automated banking services, and above all by the growth and interlinking of the ATM networks and the gradual replacement of classic counter banking in some financial institutions with electronic banking services. Automation will be a significant factor in the further rationalisation of banking services.

The number of citizens per bank, banking unit and employee has been constantly increasing in recent years. This is due to the decrease in the number of active banks, the downsizing of branch networks and the reductions in

bank workforces amid a stagnant population level in the Czech Republic. The reduction in the number of workplaces and in the number of bank staff has been fully offset by the development of automated forms of banking, which offer clients a higher level of convenience and saving of time. Czech banks first offered payment cards eleven years ago. At the end of 1999, the number of bank-administered ATMs in operation in the Czech Republic was 1,447 and the total number of active payment cards was 2.8 million. In 1999, there were around 4,000 cash withdrawals per ATM per month.

The banks operating on the Czech banking market have yet to focus on other countries in any significant way. As of 31 December 1999, five banks had foreign workplaces, in the form of branches or representative offices, and 840 employees worked in these banking units as of that date. The weight of the foreign network expressed as the ratio of the number of staff registered at workplaces abroad to the total number of staff remained at the 1997 and 1998 level, i.e. around 2%, with the large banks accounting for the major part of this.

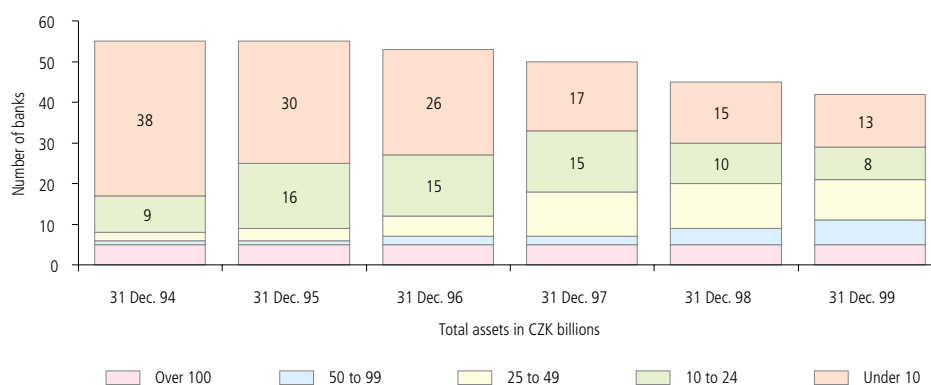
## 2.4 Concentration and competition

Concentration is a characteristic feature of today's financial world. The main motive for concentration is the efficiency gain given by decreasing costs amid a rising volume of business deals. Another element is the endeavour to cope with the ever greater competition on the domestic market and, in particular, on the international scale.

In the Czech Republic, the concentration in the banking sector is particularly visible in the intensive development of medium-sized banks which are gradually beginning to form. The significant fall in the number of banks managing total assets of less than CZK 10 billion, which as recently as 1995 made up the lion's share of the banking sector in terms of the number of banks, is related primarily to the winding up of some of these banks owing to their unfavourable financial situation. On the other hand, certain foreign banks and foreign bank branches, which initially only monitored the development of the incipient market economy, have begun to expand their activities with great intensity, and the growth in the total assets they manage reflects this. The concentration of the banks operating in the Czech Republic also reflects the amalgamation of certain foreign banks following the mergers of their parent banks.

**CHART 3** BANKS BY TOTAL ASSETS

for banks with licences as of the given date



The group of large banks with total assets exceeding CZK 100 billion comprises five financial institutions; this number has remained constant in the long term. On the other hand, the number of banks managing total assets in the CZK 50-99 billion range has increased by five since 1995 to six. A similar increase has occurred in the number of banks with total assets of CZK 25-49 billion. As of 31 December 1999, this group comprised ten banks, i.e. seven more than at the end of 1995. At the same time, the gap between the large and medium-sized banks is gradually narrowing. In 1995 the sixth-largest bank had been CZK 62 billion short of the CZK 100 billion threshold, whereas in 1999 it was only CZK 9 billion short.



The development of medium-sized banks, which are forming mainly in the groups of foreign banks and foreign bank branches, is gradually eroding the predominance of the large banks. The share of the latter in the total volume of assets was 7.9 points lower than at end-1995 at 65.1%, while the share of foreign banks and foreign bank branches was up by 11.2 points in the same period to 27.1%. Specialised banks are also undergoing rapid development. This is particularly true of the building societies, which, thanks to the state contribution to building savings, are attracting a large part of the population. The share of small banks in the total assets of the banking sector was negligible; in 1995 it had been on a par with foreign banks.

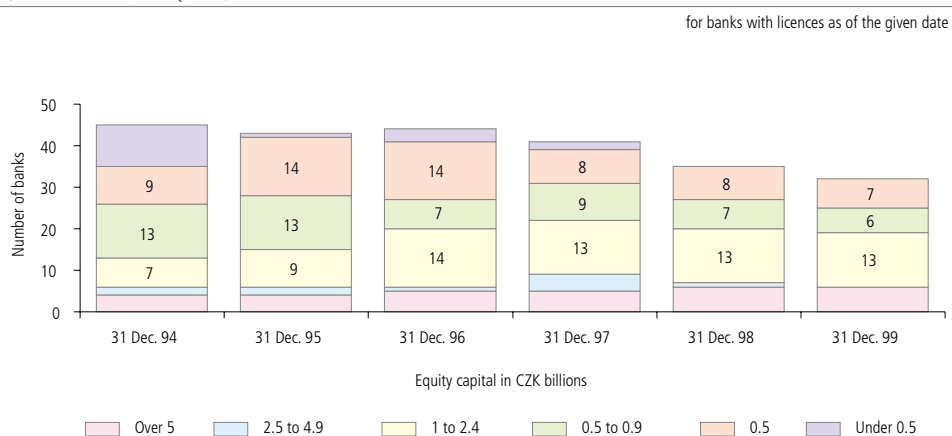
**TABLE 9** SHARE OF INDIVIDUAL BANK GROUPS IN TOTAL ASSETS IN %  
for banks with licences as of the given date

|                             | 31 DEC. 1994 | 31 DEC. 1995 | 31 DEC. 1996 | 31 DEC. 1997 | 31 DEC. 1998 | 31 DEC. 1999 |
|-----------------------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Banking sector, total       | 100.00       | 100.00       | 100.00       | 100.00       | 100.00       | 100.00       |
| <i>of which:</i>            |              |              |              |              |              |              |
| large banks                 | 77.48        | 72.99        | 68.11        | 65.63        | 65.96        | 65.07        |
| small banks                 | 9.73         | 9.06         | 6.22         | 4.70         | 3.55         | 1.57         |
| foreign banks               | 7.05         | 9.92         | 12.19        | 14.58        | 15.56        | 15.67        |
| foreign bank branches       | 4.05         | 5.99         | 6.44         | 7.72         | 9.48         | 11.44        |
| specialised banks           | 1.40         | 2.04         | 3.06         | 4.31         | 5.46         | 6.25         |
| banks under conservatorship | 0.28         | 0.00         | 3.99         | 3.07         | 0.00         | 0.00         |

Similar trends can also be seen for equity capital and for the other indicators characterising the main activities of the Czech banking sector, i.e. the total volume of credits and primary deposits.

Thanks to the winding up of small banks with low levels of capital, coupled with the capital increases in other banks, the capital situation of the banking sector is gradually improving. The average level of equity capital per bank (excluding foreign bank branches) had increased from CZK 1.5 billion at the end of 1995 to CZK 2.7 billion as of 31 December 1999. The breakdown of banks by equity capital has in recent years shown a steady decrease in the number of banks having equity capital of less than CZK 1 billion. In 1995 this group had included 28 banks, whereas at the end of 1999 it comprised only 13. The minimum equity capital level has been set at CZK 500 million. Of the total number of 32 banks, only seven operated with this equity capital level in 1999. In the period under review, a fall below the minimum equity capital level occurred in several banks, on which conservatorship was imposed.

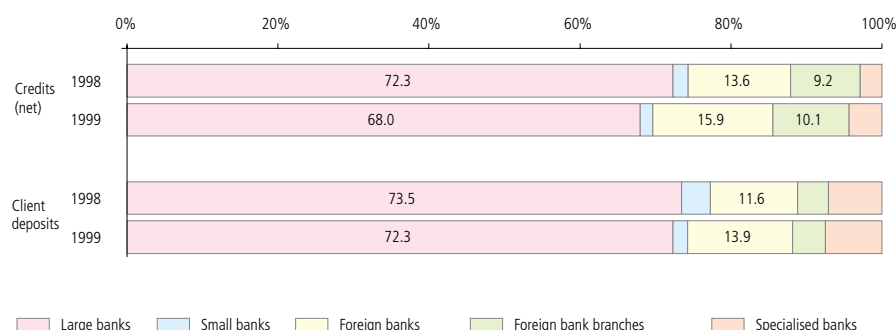
**CHART 4** BANKS BY EQUITY CAPITAL



The differences in the market shares of the individual groups of banks as regards the main banking products result primarily from their orientation towards specific client segments. The changes in market share also correspond to the varying rates of expansion of the banks' activities and to the growing competition on the market related to the rising number of clients and to product innovations.

**CHART 5 MARKET SHARES OF BANK GROUPS IN SELECTED PRODUCTS IN %**

for banks with licences as of 31 Dec. 1999



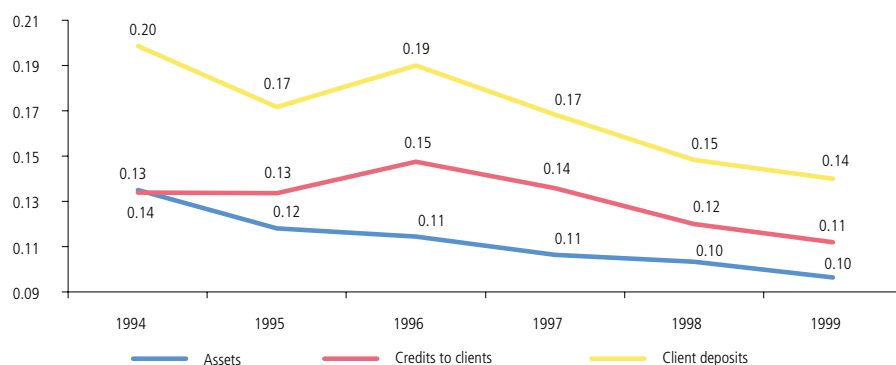
The group of large banks still retains the dominant share in the main banking products, namely credits granted and client deposits. The high pace of development of foreign banks and foreign bank branches, however, is leading to a continuous decline in the shares of the large banks, especially as regards the total volume of credits, which in 1999 decreased by 4.3 points to 68%. On the other hand, the share of foreign banks and foreign bank branches in the total volume of credits increased in the same period by 2.3 points and 0.9 points to 15.9% and 10.1% respectively. Specialised banks also recorded further growth on the credit market, mainly as a result of the higher volume of credits and interim credits granted by building societies. Their share had reached 4.3% of the total market as of 31 December 1999.

The deposit structure saw similar development. For deposits, however, the share of large banks decreased by only 1.2 points to 72.3% in 1999, owing to continuing depositor inertia and the reduced involvement of foreign banks and, in particular, foreign bank branches in retail banking. Nevertheless, a number of foreign banks are gradually launching programmes focusing on this area of banking. This was reflected in a relatively sizeable increase in their primary deposits in 1999 and thus also in their share in the total volume of deposits, which rose by 2.3 points to 13.9%, mainly to the detriment of the group of small banks. The expansion in building savings led to a 0.4 point increase in the share of specialised banks in the total volume of client deposits to 7.7%, although in comparison with previous years the pace of growth in primary deposits in this group slowed. For all products the share of small banks is negligible.

The level of competition can be measured using Herfindahl indices. These take a value in the range of 0 to 1, where 1 represents a non-competitive, monopoly-controlled environment and a value approaching 0 denotes a market wide open to competition. At present, the strongest competition is in the area of assets (0.10) and on the credit market (0.11). Competition has been steadily increasing since 1994, the only partial exception being 1996. In spite of growth in competition in the area of deposits, confirmed by a 0.06 point decrease in the Herfindahl index in 1994-1999, the competitive environment continues to be weakest in this area (0.14).

**CHART 6 HERFINDAHL INDICES OF MARKET COMPETITION**

for banks with licences in the given year



The steady increase in competition on the Czech banking market is a positive element showing up mainly in an improvement in the range of good quality products on offer, by means of which banks intend to expand their clientele at the expense of their competitors. For clients, therefore, the increasing competition in the banking sector means an improvement in the services provided, and this applies not only to business clients, but also to small depositors.

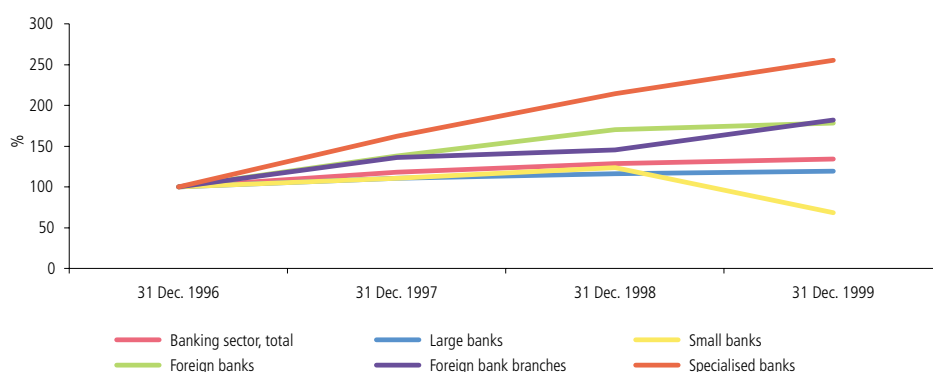
### 3. BANK ASSETS

(for banks with licences as of 31 December 1999)

As of 31 December 1999, the total assets of the banking sector stood at CZK 2,533.9 billion, which is 4.5% higher than a year earlier. The rate of growth in total assets slowed by 4.6 points in comparison with 1998 and by 13.3 points in comparison with 1997. In the group of large banks, total assets were only 19.2% higher than in 1996, while foreign banks and foreign bank branches during the same period increased their total assets by around 80% and building societies, which make up the majority of specialised banks, almost tripled theirs. Since 1996 there has been an absolute decline in the group of small banks. This is related to the winding up of certain banks in this group.

**CHART 7** GROWTH OF TOTAL ASSETS

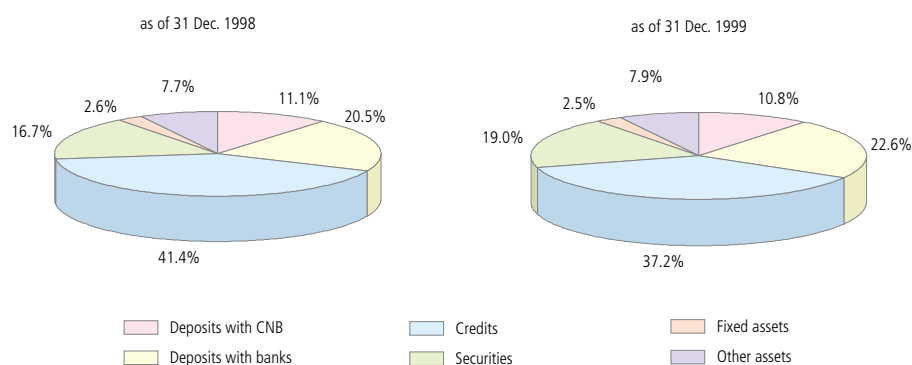
for banks with licences as of 31 Dec. 1999



Most of the growth in total assets occurred prior to 1998; in 1999 the growth slowed, owing to the overall stagnation of the economy and increased prudence of banks. This was also reflected in the changes in the structure of the assets side of the banking sector's balance sheet.

**CHART 8** ASSET STRUCTURE

for banks with licences as of 31 Dec. 1999



The reduced lending activity resulted in a further decrease in the share of credits in total assets – of 4.2 points to 37.2%. The increases in the shares of securities (especially T-bills and CNB bills) of 2.3 points to 19.0% and of deposits with other banks of 2.1 points to 22.6% are related to the banks' giving preference to locating their free funds in safe forms of business rather than using them in the credit area. The 0.3 point decrease in the share of deposits with the CNB to 10.8% is also connected with the decrease in the required reserves ratio for primary deposits from 7.5% to 2.0% in 1999.

### 3.1 Credit activities<sup>3)</sup>

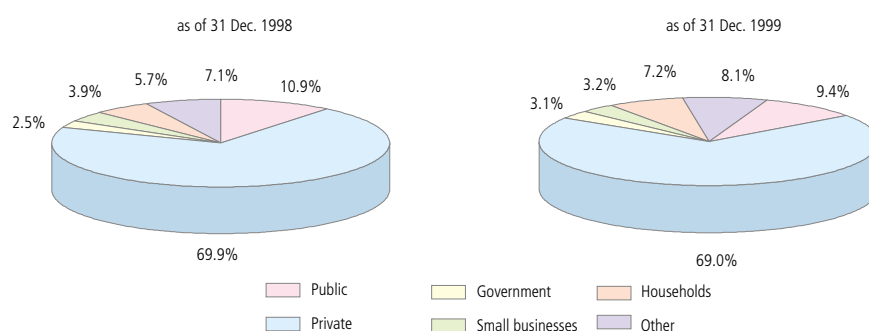
The unfavourable economic development during 1998 and 1999 led banks to curtail their new credit activities in an endeavour to decrease the risk of incurring any new losses. At present, the banks are developing new activities linked chiefly with off-balance-sheet transactions, to the detriment of classic banking services and therefore also credits. Although the reduction of the reserve requirement increased the disposable funds of banks, it did not foster any growth of their credit portfolios, as fears prevailed of potential problems with the repayment of newly granted loans.

The total volume of credits as of 31 December 1999 was CZK 1,085.7 billion, which is 3.2% less than a year earlier. Credits accounted for around 78% of GDP in constant prices.

The decrease in lending activity occurred largely in the group of large banks, where in 1999 the total volume of credits granted dropped by 7.5% to CZK 770.2 billion. The volumes of credits granted by foreign banks and foreign bank branches were 12.0% higher and 4.7% higher respectively than a year earlier. Even these growth rates, however, are below the 1998 level (16.9% for foreign banks and 7.8% for foreign bank branches). For the second year in a row, building societies registered an enormous rise in lending, with annual growth of 44.9% (and 144.1% in 1998). This situation, however, is given by the fact that building societies, owing to legal restrictions, had begun to provide the first credits to their clients only after two years' saving, i.e. from around 1997 onwards. The greatest upsurge in building society lending activity occurred in 1998; in 1999, the growth was less dynamic, and a further slowdown can be expected in the future.

**CHART 9** CREDIT STRUCTURE BY SECTOR

for banks with licences as of 31 Dec. 1999



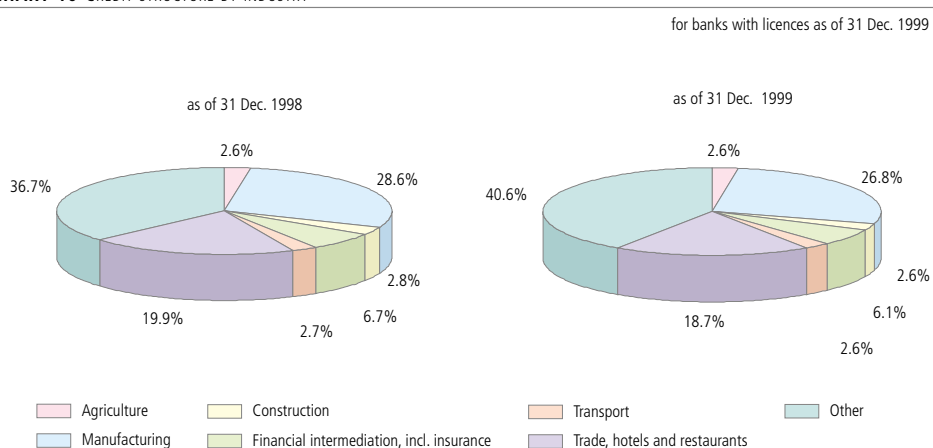
Note: Credits granted in the Czech Republic only

The banking sector granted the largest volume of credits to the private sector, which accounted for 69.0% of the overall volume of credits as of 31 December 1999. Compared with the previous year, however, this share was down by 0.9 points, chiefly in favour of credits granted to households. The same tendency was seen in the public sector, the share of which in the overall volume of credits decreased in 1999 by 1.5 points to 9.4%, and in the small business sector, whose share fell by 0.7 points to 3.2%. All the aforementioned economic sectors also registered an absolute year-on-year decrease in the volume of credits drawn. The absolute decreases in the

3) All data in this chapter refer to gross credits, i.e. credits irrespective of provisions

volume of credits granted to the business sector confirm the unfavourable economic situation in the Czech Republic and the increased prudence of banks in granting new credits. There has been continuous growth in the volume of credits granted to households, the share of which in the overall volume of credits increased in 1999 by 1.5 points to 7.2%, and by 22.6% in absolute terms. Thus, the growing orientation of some banks towards small clients and the increased availability of consumer credits, already signalled in the previous year, have been confirmed; specific-purpose credits granted by building societies and mortgage loans make up a substantial part of these credits. Credits to the government sector and credits to other entities also registered growth; the share of the former increased by 0.6 points to 3.1% and the share of the latter by 1 point to 8.1%.

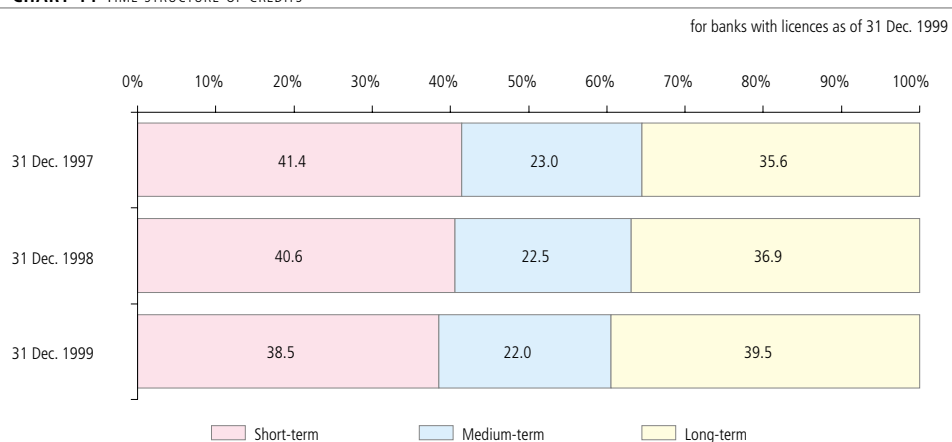
**CHART 10** CREDIT STRUCTURE BY INDUSTRY



The industry structure of the credits granted corresponds to the industry structure of the Czech economy. The largest volume of credits was channelled into manufacturing (26.8% as of 31 December 1999), followed by trade and hotels and restaurants (18.7%). In comparison with 1998, however, these shares decreased by 1.8 and 1.2 points respectively owing to the high level of risk in these industries. Of the other industries, credits granted to the financial intermediation and insurance industry had a sizeable share (6.1%). The other industries, which have shares of less than 3%, are of no great significance in the structure of credits granted.

As regards the time structure of credits, 1999 saw the continuation of the moderate shift towards long-term credits (i.e. those with maturities of over four years). Their share was the only one to show a year-on-year increase – of 2.6 points to 39.5%. Long-term credits thus for the first time occupied first place in terms of their share in the overall volume of credits granted.

**CHART 11** TIME STRUCTURE OF CREDITS



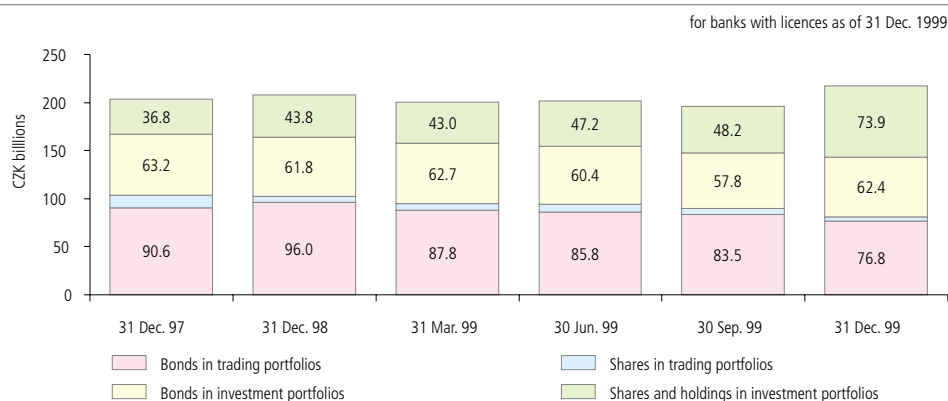
Short-term credits, like medium-term credits, decreased in both absolute and relative terms in 1999 – by 2.1 points and 0.6 points respectively. The time structure of credits reflects the structure of disposable funds of the banking sector, where funds with shorter maturities also predominate.

### 3.2 Securities operations

The net value of the total volume of securities, i.e. T-bills and CNB bills, trading portfolio securities and long-term financial investments, was CZK 480.4 billion as of 31 December 1999, an increase of 18.8% on a year earlier. Securities accounted for 19.0% of total assets, which is 2.3 points more than at the end of 1998.

T-bills and CNB bills had the highest share in the structure of securities – 58.8%. These were also the main source of growth in the total volume of securities in 1999. For banks, these securities are a good way in which to invest free funds, because, in addition to their minimal level of risk, they have the advantage of high liquidity. Their volume was 31.3% higher than a year earlier.

**CHART 12** STRUCTURE OF SECURITIES IN BANK PORTFOLIOS



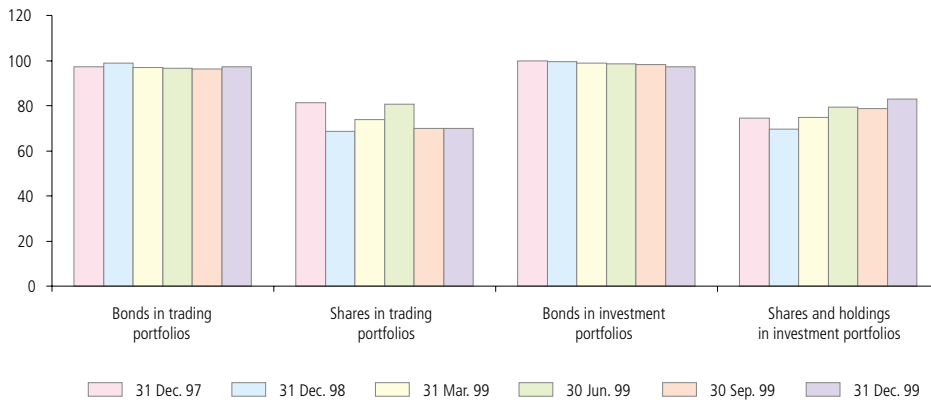
Other securities, i.e. securities designed for active trading on the capital markets and long-term financial investments, developed differently. Owing to the continuing relatively unstable situation on the capital market, banks are not engaging in these activities to any large extent. The total volume of securities excluding T-bills and CNB bills was 4.7% higher than a year earlier, accounting for 7.8% of the total volume of assets as of 31 December 1999.

When assessing the level of risk in a securities portfolio, an important aspect is its breakdown by type of security. The low level and volatility of market valuations, especially with respect to equity securities, result from the developments on the Czech capital market. On the other hand, in the case of debt securities the situation is much more favourable. The structure of the securities trading portfolio reflects this situation; fixed-yield securities account for around 95% of this portfolio. In the investment portfolio, where banks lodge their strategic investments and bonds held until maturity in order to support liquidity, variable-yield securities and equity interests predominate. As of 31 December 1999, these types of securities accounted for 54.2% of the total volume of the investment portfolio, 12.7 points higher than a year earlier.

The market value/purchase price ratio for equity securities in both trading and investment portfolios has long been fluctuating at the 60%-80% level. In the case of debt securities, the ratio has been fluctuating just below 100%, regardless of portfolio.

**CHART 13** SECURITIES - RATIO OF MARKET VALUE TO PURCHASE PRICE

for banks with licences as of 31 Dec. 1999



The ratio of the market value of the total banking sector securities portfolio excluding T-bills and CNB bills to its purchase price was 91.9% as of 31 December 1999, which was essentially the same as at end-1998. In the case of the trading portfolio, the ratio of market value to purchase price was 95.8% (1.4 points higher than a year earlier) and in the case of the investment portfolio it was 89.7% (2.4 points higher).

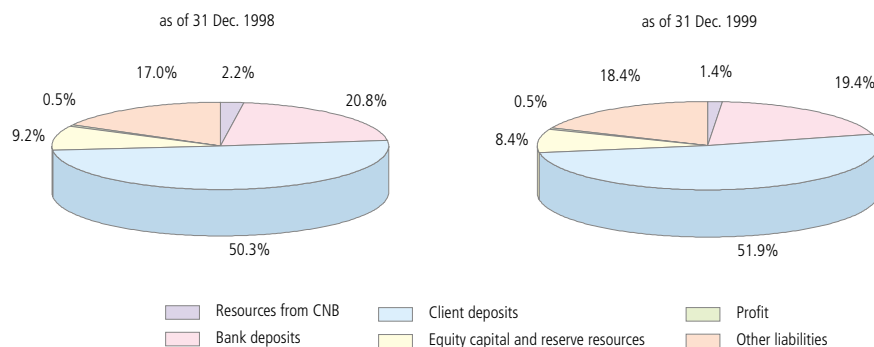
## 4. BANK LIABILITIES

(for banks with licences as of 31 December 1999)

The structure of liabilities of the Czech banking sector reflects the level and structure of the banks' own funds and of the various forms of their external funds, the volume of which depends on the extent of the banks' asset operations and their ability to obtain them. The most important liabilities item is client deposits, the share of which has been fluctuating in the long term around 50% of total assets. As of 31 December 1999, the share of client deposits was 51.9%, which is 1.6 points higher than at the end of 1998. The persisting trend towards lodging free funds in bank accounts is related to a certain distrust, especially on the part of households, of other forms of investing. At present, however, even in the Czech Republic the process of decline in the intermediation of financial services by banks is intensifying, in favour of other financial institutions such as insurance companies, pension funds and collective investment institutions, which are gradually taking over a part of household savings.

**CHART 14** LIABILITIES STRUCTURE

for banks with licences as of 31 Dec. 1999



Deposits from other banks were the second most important external funds item in 1999, accounting for one fifth of the total volume of liabilities. In comparison with the end of 1998, their share was up by 1.4 points to 19.4% as of 31 December 1999 owing to the reduced need of banks for additional funds in connection with their subdued lending in that year. Equity capital and reserve resources have been fluctuating in the long term at the level of 8%-9% of total liabilities.

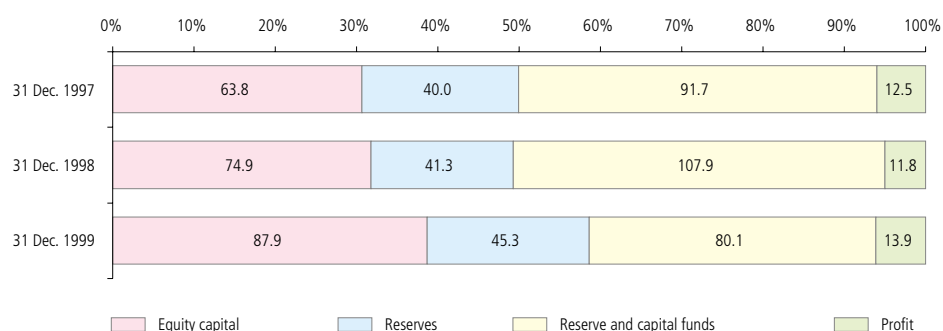
#### 4.1 Own funds

The own funds of the banking sector, i.e. equity capital, reserve and capital funds, general reserves and current and retained profits, amounted to CZK 227.2 billion as of 31 December 1999, 3.6% lower than a year earlier. The main cause of this decline was a 25.8% fall in reserve and capital funds to CZK 80.1 billion. These funds were used to write off accumulated losses and for the accounting settlement of operations linked with the sale of certain banks.

The equity capital of the banking sector amounted to CZK 87.9 billion as of 31 December 1999, CZK 13.0 billion higher than a year earlier. Most of the increase occurred in the group of large banks, in connection with their privatisation, and in the group of foreign banks. The reasons for the increases in equity capital in the individual groups differ. In small banks and basically also in large banks, the increases were intended to enhance stability by covering real or forecast losses, whereas in the case of foreign banks such increases are primarily intended to stimulate the development of new activities, which need to be covered by capital in order to maintain a satisfactory level of capital adequacy.

**CHART 15** DEVELOPMENT AND STRUCTURE OF BANKS' OWN FUNDS

for banks with licences as of 31 Dec. 1999



Note: The data in the chart are in CZK billions

Reserves are a bank's own funds used mainly to cover its losses arising from the credit portfolio. Over recent years, their volume has been relatively stable, mainly because the banks have preferred to cover their losses with provisions relating to specific asset items. As of 31 December 1999, reserve and capital funds accounted for 35.2% of total own funds. The creation of reserve funds depends on the level of the profit attained, which is the basic source for these funds. Those banks in the Czech banking sector which make a profit currently prefer to create funds rather than pay out dividends, in the interests of maximum strengthening of their capital base.

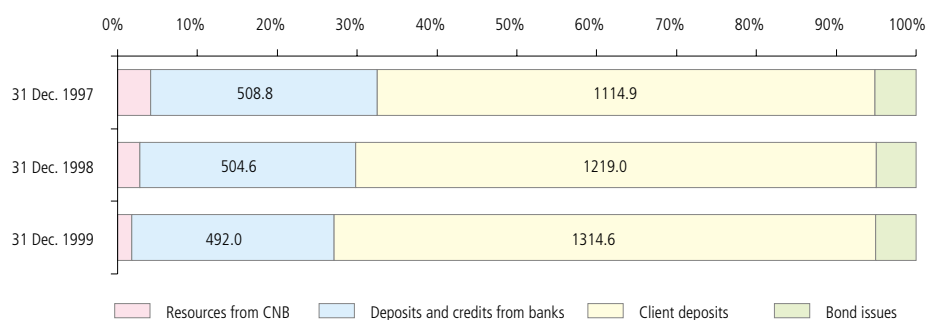
#### 4.2 External funds

The overall volume of external funds amounted to CZK 1,938.9 billion as of 31 December 1999, i.e. 3.7% higher than a year earlier. Client deposits accounted for the highest share in the structure of external funds, with their share increasing by 2.6 points to 67.8% in 1999. Deposits and credits from banks made up around one quarter of the external sources of financing; their share in the overall volume of external funds fell slightly during the course of 1999. The importance of bank bonds as a source of bank financing continues to be minimal; their share in total external funds was around 5%.



**CHART 16** DEVELOPMENT AND STRUCTURE OF BANKS' EXTERNAL FUNDS

for banks with licences as of 31 Dec. 1999



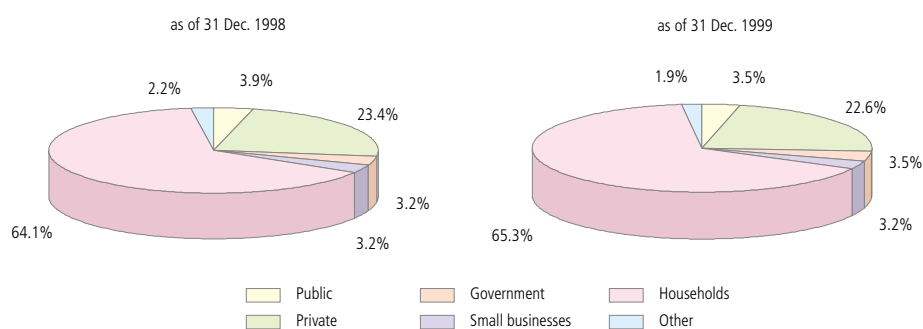
Note: The data in the chart are in CZK billions

### 4.2.1 Primary funds

The overall volume of client deposits was CZK 1,314.6 billion as of 31 December 1999, i.e. 7.8% higher than a year earlier. In comparison with 1998, their rate of growth slowed by 1.5 points. Households' deposits amounted to CZK 762.0 billion as of 31 December 1999, up 3.2%. Their growth rate, however, was 12.8 points slower than in 1998. Business sector deposits accounted for 26.1% of the total volume of client deposits, 1.2 points less than a year earlier. During the course of 1999, there was an absolute decrease in private and public sector deposits of CZK 9.3 billion to CZK 304.8 billion.

**CHART 17** DEPOSIT STRUCTURE BY SECTOR

for banks with licences as of 31 Dec. 1999



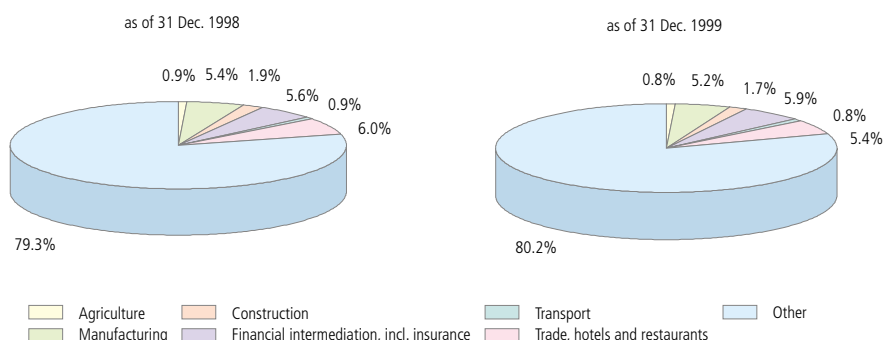
Note: Deposits accepted in the Czech Republic only

1999 saw moderate growth in small businesses' deposits – of 0.8% to CZK 37.0 billion – and in the government sector – of 10.8% to CZK 41.0 billion. Nevertheless, government sector deposits and small business deposits are the smallest in terms of volume and have only a minimal influence on overall client deposits.

The industry structure of primary deposits reflects the large share of household deposits, which in this context are included under other industries. Of the specific industries, financial intermediation and insurance had the highest share in total deposits (5.9%), followed by trade and hotels and restaurants (5.4%) and by manufacturing (5.2%).

**CHART 18 DEPOSIT STRUCTURE BY INDUSTRY**

for banks with licences as of 31 Dec. 1999

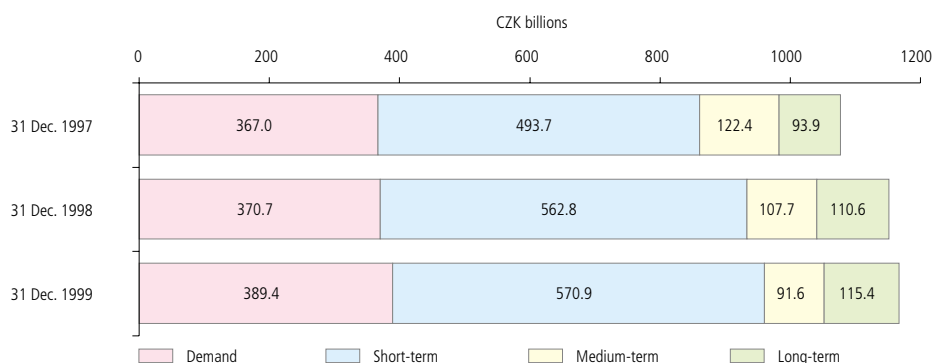


Note: Deposits accepted in the Czech Republic only

The deposits of both last-named industries showed a decrease in their share of the total compared with a year earlier. The deposits of the other industries under review, i.e. agriculture, construction, transport and travel, represent altogether only 3.3% of total client deposits and are therefore negligible from the point of view of the development of deposits.

**CHART 19 TIME STRUCTURE OF DEPOSITS**

for banks with licences as of 31 Dec. 1999



Note: Deposits accepted in the Czech Republic only

Short-term time deposits with maturities of up to one year continued to predominate in the deposit time structure. The reasons for demand deposits still occupying second place as regards the volume of deposits are the need for liquid funds, the relatively low interest rates on time deposits and the as yet not quite rational investment decision-making in the Czech Republic. The total volume of demand deposits and short-term time deposits increased by 5.1% to CZK 389.4 billion and by 1.4% to CZK 570.9 billion respectively. These two types of deposits accounted for 82.3% of the total volume of primary deposits, with short-term time deposits alone accounting for almost one half of total deposits.

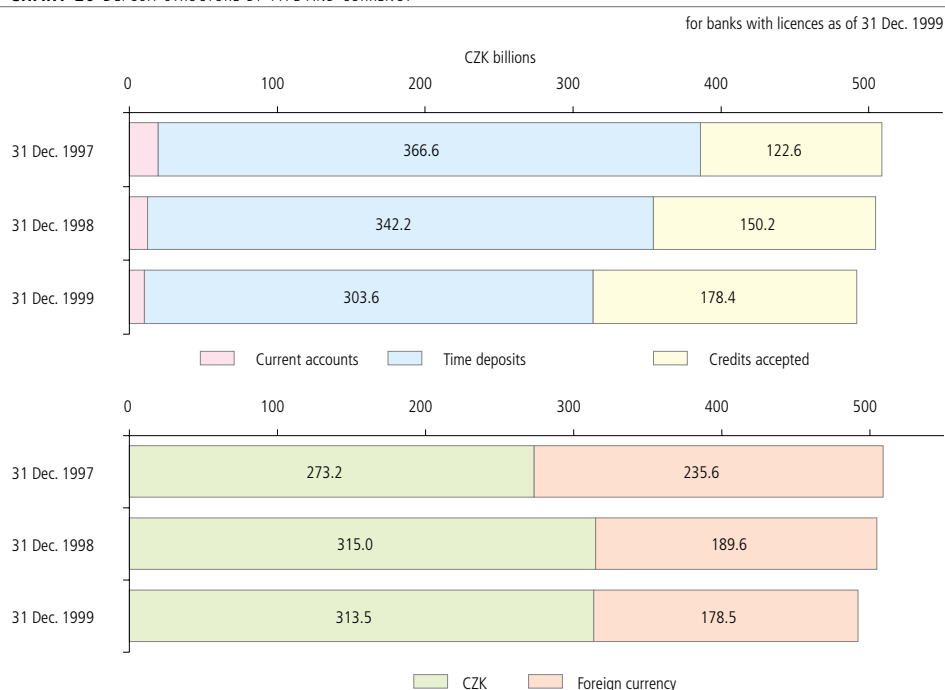
The trend towards a moderate increase in the share of long-term time deposits continued into 1999; this share increased by 0.3 points compared with 1998 to 9.9%. This shift, however, was largely due to a decrease in the share of medium-term time deposits. These deposits, with maturities of one to four years, are the least popular at present, accounting for just 7.8% of primary deposits.

## 4.2.2 Secondary funds

The total volume of deposits and credits from banks was CZK 492.0 billion at the end of 1999, i.e. 2.5% less than a year earlier. By type, time deposits (61.7%) and credits accepted (36.3%) predominate in the structure of secondary funds.

As of 31 December 1999, koruna funds accounted for 63.7% of the secondary funds of banks, up 1.3 points on a year earlier. The overall decrease in secondary funds reflects the decrease in foreign currency deposits, i.e. deposits from non-resident banks in particular. The main reason for the decline in banks' secondary funds is the reduced need for funding for asset transactions, owing to the basic trend towards lower bank lending activity in 1999.

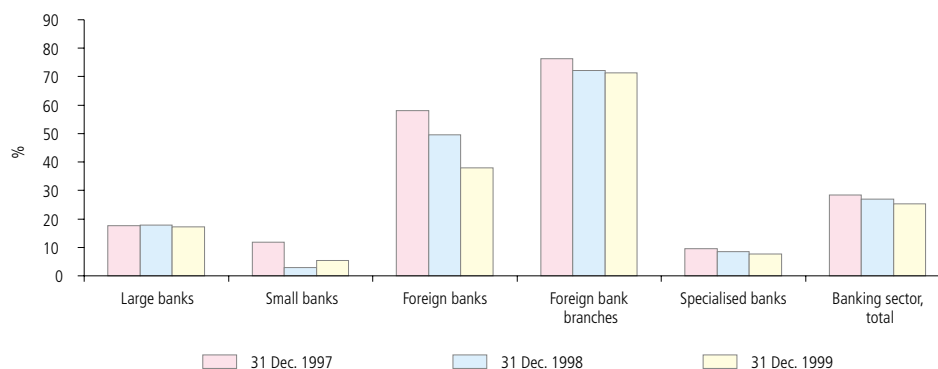
**CHART 20** DEPOSIT STRUCTURE BY TYPE AND CURRENCY



Financing through the interbank market is particularly characteristic of foreign bank branches and foreign banks. Even in these groups, though, there has been a modest shift towards primary deposits. During the course of 1999, the share of secondary deposits in the total volume of external funds decreased by 0.8 points in the case of foreign bank branches and by 11.6 points in the case of foreign banks. The lower use of interbank financing by foreign banks and foreign bank branches is related not only to their new activities in retail banking, but also to the slower growth of their involvement in lending which was also apparent for these banks in 1999. Small and specialised banks in practice finance their activities fully from their primary funds, while large banks have maintained a stable level of financing from secondary funds at 17%-18%.

**CHART 21** SHARE OF SECONDARY FUNDS IN EXTERNAL FUNDS

for banks with licences as of 31 Dec. 1999



## 5. OFF-BALANCE-SHEET ACTIVITIES

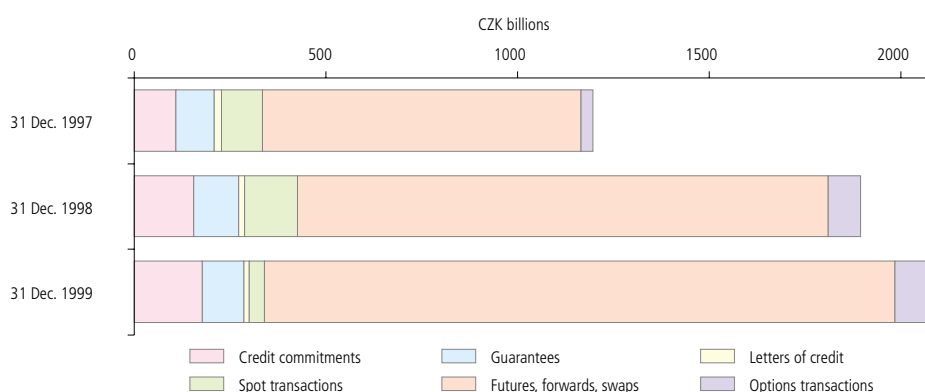
(for banks with licences as of 31 December 1999)

In terms of both volume and innovation, the development of off-balance-sheet operations is, together with the development and introduction of various forms of electronic banking, one of the two most important worldwide trends in the provision of banking services. The same is also true for the Czech banking sector.

As of 31 December 1999, off-balance-sheet assets had reached CZK 2,069.4 billion, an increase of 9.2% on a year earlier. At the end of 1999, off-balance-sheet activities accounted for 81.7% of total assets. Most of the growth in off-balance-sheet activities occurred during 1997 and 1998. In comparison with the end of 1996, the volume of off-balance sheet assets had risen by more than 250% and their share in the total assets by 50.7 points.

**CHART 22** STRUCTURE OF OFF-BALANCE-SHEET ASSETS

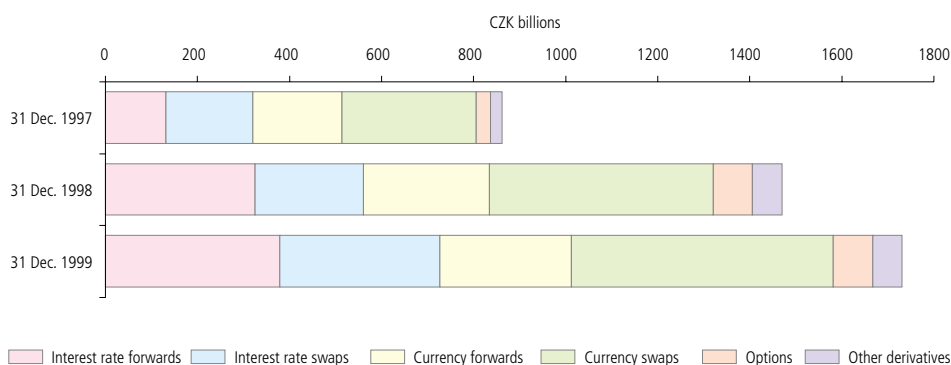
for banks with licences as of 31 Dec. 1999



The growth in off-balance-sheet activities is a consequence of the development of derivatives operations, i.e. futures, forwards, swaps and options. The importance of off-balance-sheet activities relating to classic banking, such as credit commitments, guarantees and letters of credit, is on the decrease, as evidenced by the 0.7 point decrease of their share in the total volume of off-balance-sheet assets to 14.5% compared with the end of 1998. Since 1996, derivatives operations have increased almost five fold, and as of 31 December represented 83.6% of all off-balance-sheet activities. Futures, forwards and swaps predominate in derivatives operations; banks are much less involved in options operations, which account for around 5% of the overall volume of derivatives operations.

**CHART 23** STRUCTURE OF DERIVATIVES BY TYPE

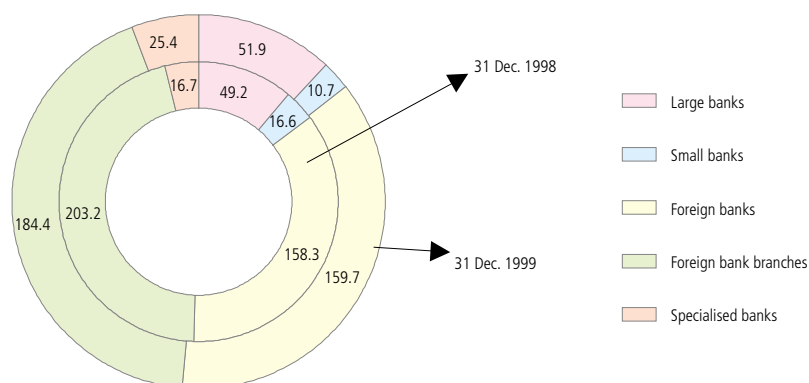
for banks with licences as of 31 Dec. 1999



Operations in currency and interest rate instruments predominate in the structure of derivatives operations. Trading in equity derivatives and especially in commodity derivatives is much less frequent, or even minimal. Currency swaps consistently account for the lion's share of derivatives trading; during the course of 1999 they increased by 17.1% to CZK 569.5 billion. Interest rate forwards grew during 1999 with approximately the same intensity (by 16.6% to CZK 379.2 billion as of 31 December 1999). A very high level and sharp upsurge is also visible for interest rate swaps and currency forwards.

**CHART 24** SHARE OF OFF-BALANCE-SHEET ASSETS IN TOTAL ASSETS IN %

for banks with licences as of 31 Dec. 1999



The individual groups of banks engaged in off-balance-sheet transactions with varying intensity. The highest ratios of off-balance-sheet items to total assets were registered for foreign bank branches (184.4% as of 31 December 1999) and foreign banks (159.7%). In the group of large banks, off-balance-sheet assets constitute around one half of their total assets. The involvement of small banks and specialised banks in this area is minimal. The structure of off-balance-sheet activities in the individual groups of banks also differs. Derivatives operations are predominant in the case of foreign banks and foreign bank branches (86.9% and 91.0% of the total volume of off-balance-sheet assets respectively as of 31 December 1999), whereas items relating to classic banking are of greatest importance for small banks and specialised banks (81.2% and 68.6% respectively).

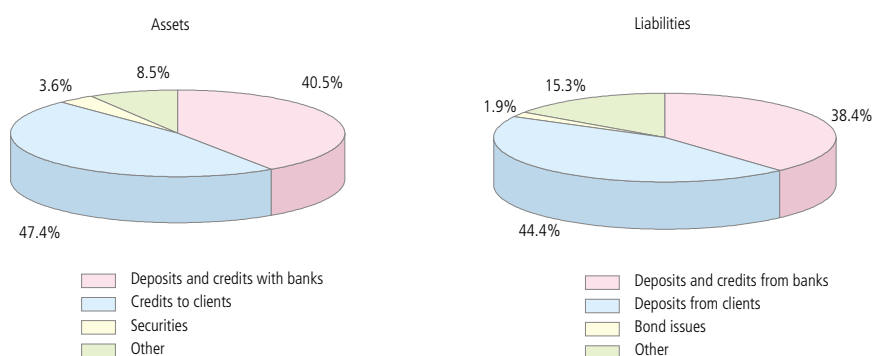
## 6. FOREIGN EXCHANGE ACTIVITIES

(for banks with licences as of 31 December 1999)

Banks operating on the Czech banking market are allowed to perform foreign currency operations on the basis of a foreign exchange licence. As of 31 December 1999, foreign exchange assets amounted to CZK 545.5 billion and foreign exchange liabilities to CZK 465.4 billion. These volumes were 12.3% and 5.4% higher respectively than a year earlier. Foreign exchange activities accounted for around one fifth of the total volume of assets. The highest share of foreign exchange operations in total assets was attained in 1997. Following a decrease in 1998, the volume of foreign exchange assets and liabilities began to increase again in 1999, but has yet to return to the 1997 level. Foreign exchange assets are growing faster than foreign exchange liabilities. This is linked with the current credit trend whereby banks require a lower volume of additional funds to finance their activities, and conversely are depositing their free funds to a greater extent with foreign banks.

**CHART 25** STRUCTURE OF FOREIGN EXCHANGE ASSETS AND LIABILITIES AS OF 31 DEC. 1999

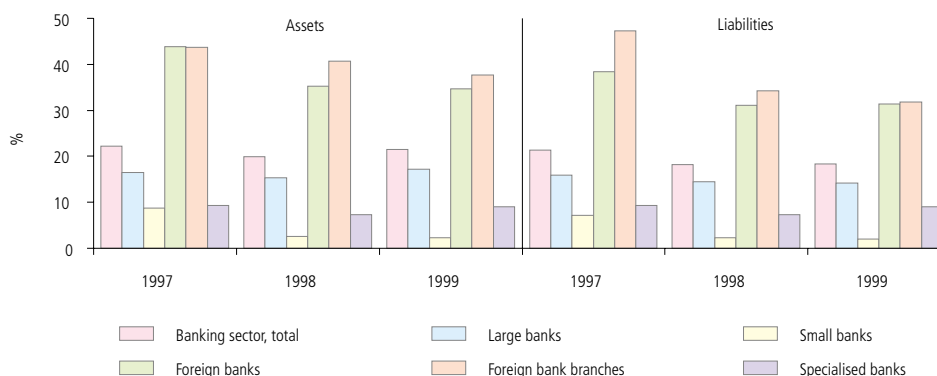
for banks with licences as of 31 Dec. 1999



Credits to clients accounted for the largest proportion of foreign exchange assets – 47.4% as of 31 December 1999, which roughly corresponds to the end-1998 level. This share is 10.2 points higher than the share of total client credits in total assets. Foreign exchange deposits and credits with banks account for 40.5% of the foreign exchange assets of the banking sector; this share is 17.9 points higher than the share of total deposits and credits with banks in total assets. The percentage of securities denominated in foreign currency (3.6%) is substantially (15.4 points) lower than the share of total securities in total assets. Client deposits accepted formed the major part of foreign exchange liabilities in 1999, with 44.4%, while interbank financing accounted for 38.4%.

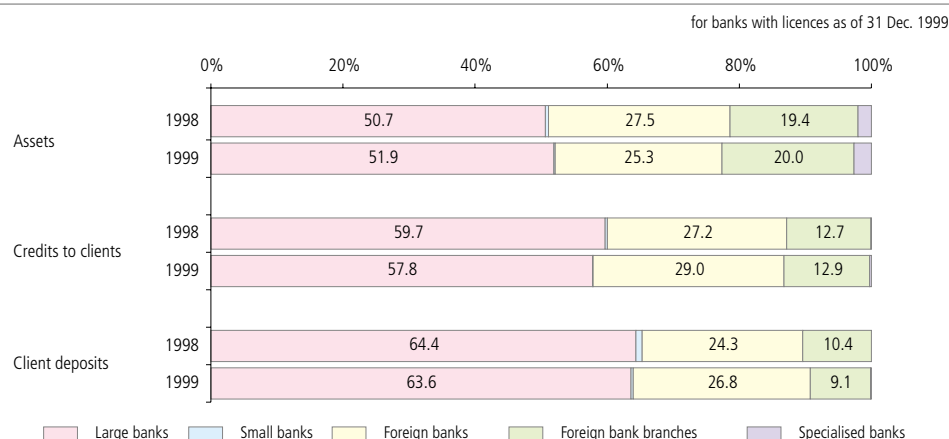
**CHART 26** SHARE OF FOREIGN EXCHANGE ASSETS AND LIABILITIES IN TOTAL ASSETS

for banks with licences as of 31 Dec. 1999



Foreign currency transactions are activities in which foreign banks and foreign bank branches in particular engage; in 1999 the share of foreign exchange assets and liabilities in their total assets fluctuated at the 30%-40% level. The involvement of small banks and building societies in foreign exchange transactions continued to be minimal.

**CHART 27** MARKET SHARES OF BANK GROUPS IN SELECTED FOREIGN CURRENCY PRODUCTS IN %



The market shares of the individual bank groups in selected balance sheet items in foreign currencies show certain differences in comparison with their total market shares. In particular, there is a change in proportions between large banks and foreign banks. Comparing foreign exchange activities, the percentage participation of large banks in the products under review decreases by 10% to 20% in favour of foreign banks. Large banks retain the highest proportion of client deposits accepted (63.6% as of 31 December 1999), although this figure was 0.8 points lower than a year earlier. Conversely, the share of foreign banks in deposits accepted rose in the same period by 2.5 points to 26.8%. The share of large banks in foreign exchange credits was 57.8% as of 31 December 1999; but this share, too, was lower than a year earlier in favour of foreign banks and foreign bank branches.

## 7. ACTIVITIES VIS-À-VIS NON-RESIDENTS

(for banks with licences as of 31 December 1999)

The openness of the Czech economy enables banks to do business with foreign entities, both banks and non-banks. The involvement of the banking sector with non-residents has been increasing recently, especially on the asset side of the balance sheet. The volume of assets vis-à-vis non-residents was CZK 498.7 billion as of 31 December 1999 and accounted for 18.2% of the total volume of assets. Non-resident assets were 39.2% higher than a year earlier. This rate of growth is more than triple that in 1998.

The biggest non-resident assets item is deposits with banks, which represented 59.7% of total assets as of 31 December 1999. Deposits with non-resident banks accounted for more than 50% of the total volume of deposits with banks, 12.3 points higher than a year earlier. This growth is due to the reduced lending activity of banks, which deposited their free funds to a larger extent abroad. The share of client credits, which are the second-biggest non-resident assets item, was 6.5 points lower than a year earlier, reaching 19.3% as of 31 December 1999. In comparison with the total volume of credits, however, their share was up by 0.7 points to 9.1%.

**TABLE 10** STRUCTURE OF ACTIVITIES OF THE BANKING SECTOR VIS-À-VIS NON-RESIDENTS  
for banks with licences as of 31 Dec. 1999

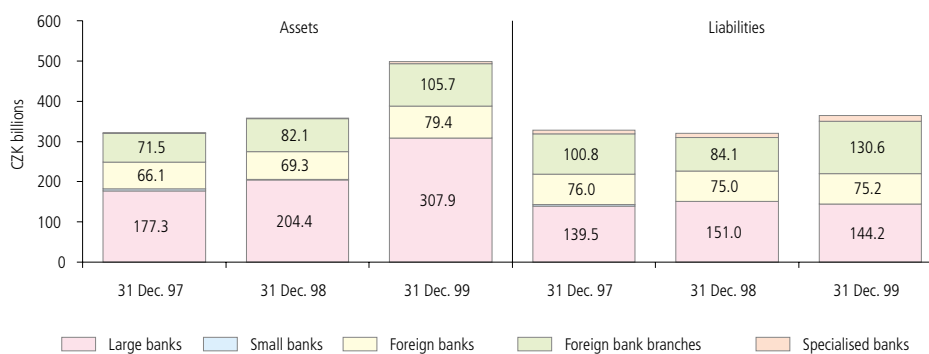
|   | 31 Dec. 1997 | 31 Dec. 1998 | 31 Dec. 1999 | SHARE OF THE TOTAL IN % |       |
|---|--------------|--------------|--------------|-------------------------|-------|
|   |              |              |              | 1998                    | 1999  |
| Total assets in CZK millions              | 320 834      | 358 238      | 498 695      | 13.72                   | 18.24 |
| <i>of which in %:</i> deposits with banks | 63.06        | 55.11        | 59.69        | 39.67                   | 51.96 |
| credits to clients                        | 19.42        | 25.77        | 19.25        | 8.44                    | 9.12  |
| securities for trading                    | 4.43         | 3.61         | 2.84         | 4.08                    | 3.90  |
| long-term financial investments           | 3.50         | 4.83         | 9.04         | 16.40                   | 33.09 |
| Total liabilities in CZK millions         | 328 433      | 319 583      | 364 150      | 13.18                   | 14.37 |
| <i>of which in %:</i> deposits from banks | 68.94        | 65.22        | 62.13        | 41.31                   | 45.98 |
| client deposits                           | 18.96        | 17.64        | 18.48        | 4.84                    | 5.34  |
| subordinated debt                         | 1.67         | 3.28         | 3.63         | 54.05                   | 60.31 |

As regards liabilities items, the growth in activity is not so robust, although the share of these items in total assets also increased – by 1.2 points to 14.4%. The overwhelming majority of non-resident liabilities are concentrated in deposits from banks (62.1%). Owing to the lower need for additional sources of funding for asset transactions, however, this proportion is gradually decreasing. The share of client non-resident deposits has not changed significantly during recent years and has been fluctuating around 18%.

The faster growth of non-resident assets relative to non-resident liabilities in 1999 has substantially opened the international position of the banking sector. In 1998, relations towards non-residents on the assets and liabilities side of the balance sheet were practically balanced (13.7% versus 13.2%), whereas in 1999 the share of assets vis-à-vis non-residents in total assets was 3.9 points higher than the share of non-resident liabilities in total liabilities. This testifies to the relative advantageousness of depositing bank capital in this way. There are no comparable alternatives in the domestic economy, not only in terms of yield, but also, in particular, as regards the returnability of the funds provided.

**CHART 28** STRUCTURE OF ACTIVITIES VIS-À-VIS NON-RESIDENTS BY BANK GROUP

for banks with licences as of 31 Dec. 1999



Large banks registered the fastest growth in asset transactions vis-à-vis non-residents, with a 51.5% increase in volume. This growth was mainly due to an increase in deposits with non-resident banks, where banks deposit free funds that they are unable to use for effective lending. On the liabilities side, conversely, the group of large banks recorded an 8% decrease in total liabilities vis-à-vis non-residents. The largest drop – of 19.3% – was in deposits from banks, whereas client deposits increased by 16.5%.

Large banks, foreign banks and branches of foreign banks have the largest share in operations with non-residents. Small banks and specialised banks have virtually no involvement in this area. The share of large banks in asset transactions with non-residents was 61.7% as of 31 December 1999. A slightly different situation exists with respect to liability transactions with non-residents, where a marked predominance of foreign banks and branches of foreign banks can be seen. As of 31 December 1999, 56.5% of all the transactions were concentrated in foreign banks and foreign bank branches, whereas only 39.6% lay with large banks.



## 8. BANKING SECTOR PERFORMANCE

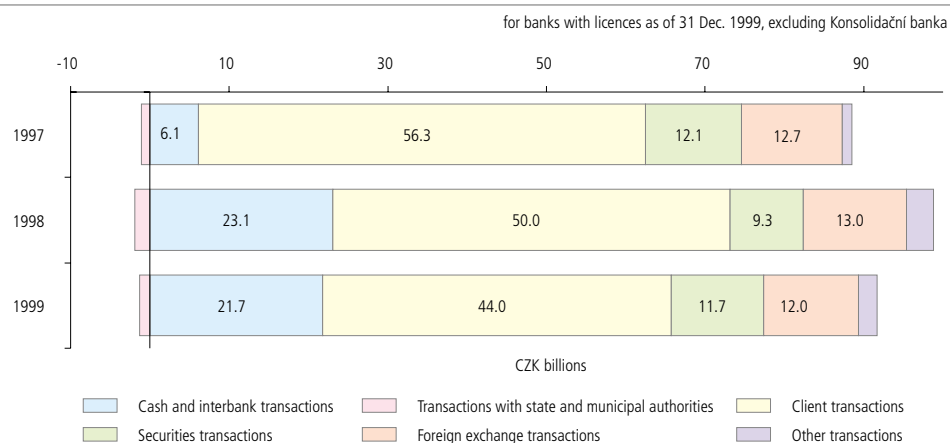
(for banks with licences as of 31 December 1998, excluding Konsolidační banka)

### 8.1 Profit from banking activities

Profit from banking activities was CZK 90.3 billion for 1999, which is 6.7% less than in 1998. The main reason for the lower level is a decrease in interest profit, which constitutes the major part of profit from banking activities.

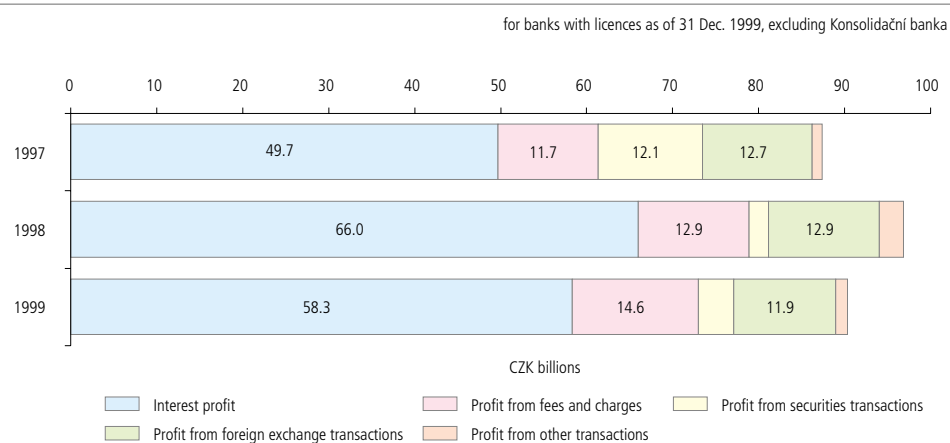
Client transactions, i.e. classic banking connected with accepting deposits and granting credits, remained the most important area of profit from banking activities. Their share in the overall structure of profit from banking activities, however, gradually decreased in favour of other transactions and towards the end of 1999 dropped below one half of the profit from banking activities for the first time, to 48.7%. Profit from cash and interbank transactions decreased less rapidly; its share in the total profit from banking activities, however, increased by 0.2 points to 24.1% in 1999. The developments in these two profit areas are conditional on interest rates, as interest profit is of crucial importance in this respect.

**CHART 29** STRUCTURE OF PROFIT FROM FINANCIAL ACTIVITIES BY TYPE OF ACTIVITY



Despite an absolute fall of CZK 1.0 billion, profit from foreign exchange operations maintained its share of profit from financial activities approximately at the 1998 level, i.e. 13.3%. Following a moderate decrease in 1999, securities transactions in 1999 registered renewed profit growth to CZK 11.7 billion, which, however, is below the 1997 level. Profit from securities transactions, nevertheless, considerably reinforced its importance as regards the profit from banking activities; its percentage share rose by 3.3 points to 12.9%.

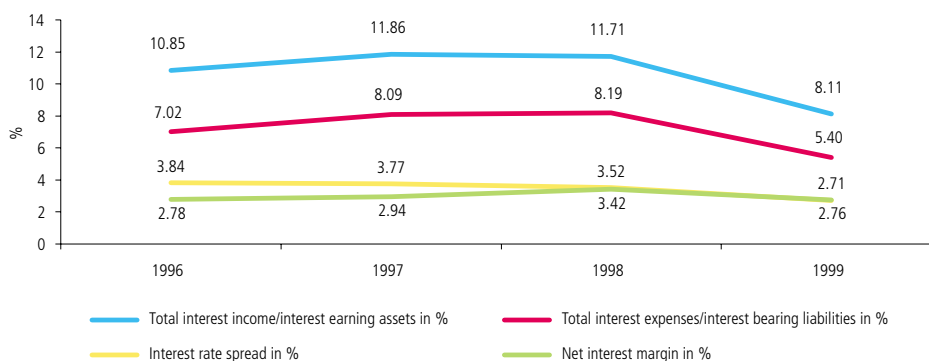
**CHART 30** STRUCTURE OF PROFIT FROM FINANCIAL ACTIVITIES BY TYPE OF PROFIT



With respect to the type of profit, interest profit has biggest influence on the level of profit from banking activities. This amounted to CZK 58.3 billion in 1999, i.e. 11.6% lower than a year earlier. Its share in profit from financial activities for 1999 dropped by 3.6 points to 64.6%. Profit from fees and charges, connected primarily with interbank and off-balance-sheet transactions, increased further in comparison with 1998, by 13.3% to CZK 14.6 billion. This fed through into a 2.9 point increase of its share in profit from banking activities to 16.2%.

**CHART 31** SELECTED PROFITABILITY INDICATORS

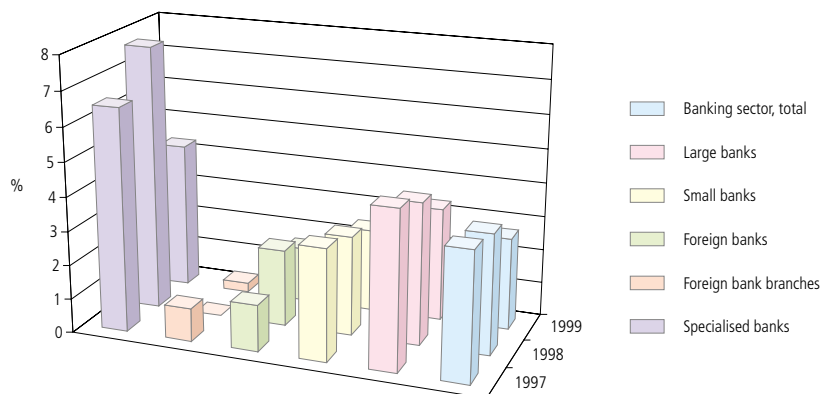
for banks with licences as of 31 Dec. 1999, excluding Konsolidační banka



The continuing decrease in basic interest rates was also reflected in the ratios of interest income/interest earning assets and interest expenses/interest bearing liabilities. In 1999, the former was 8.11% and the latter 5.4%, i.e. 3.6 points lower and 2.8 points lower respectively than a year earlier. This fed through into a narrowing of the interest rate spread by 0.8 points to 2.71%.

**CHART 32** INTEREST RATE SPREAD BY BANK GROUP

for banks with licences as of 31 Dec. 1999, excluding Konsolidační banka



Specialised banks, and especially building societies, are achieving the highest levels of interest rate spread. In 1999, however, the interest rate spread in this group narrowed by 3.5 points to 4.31%, owing the gradual development of credit activities in the area of housing support. A relatively high level of interest rate spread is also visible in the groups of large and small banks, which are obliged to maintain such levels because of the need to create provisions and reserves. In these groups, too, however, there were decreases in comparison with 1998, of 0.8 points to 3.33% and of 0.5 points to 2.43% respectively. In foreign banks, the interest rate spread was 1.61% and in branches of foreign banks 0.27%.

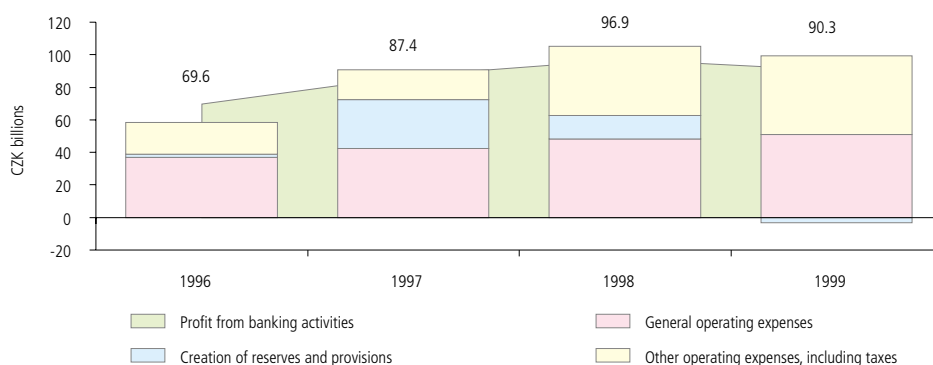
The return on assets, expressed as the ratio of profit from banking activities to average assets in a given year, decreased by 0.5 points to 4.01% in 1999. Only small banks and foreign banks registered a rise in their return on assets. The highest figure was attained by specialised banks – 5.26%.

## 8.2 Net profit

The banking sector ended 1999 with a loss of CZK 5.6 billion. Profit was registered in 1999 by foreign banks (CZK 1.8 billion) and by specialised banks, including building societies (CZK 1.9 billion). The group of large banks, on the contrary, showed a loss of CZK 7.9 billion, down CZK 4.9 billion on a year earlier. Small banks and foreign bank branches also recorded a loss in 1999 (CZK 0.5 billion and CZK 0.9 billion respectively).

**CHART 33** NET PROFIT FROM BANKING ACTIVITIES

for banks with licences as of 31 Dec. 1999



The resulting level of net profit is influenced above all by the level of operating expenses and by the creation of provisions and reserves. General operating expenses in 1999 were CZK 51.1 billion, a rise of 6.4% compared with 1998. Their share in the profit from banking activities, which in the long term has been fluctuating around 50%, increased during the same period by 6.9 points to 56.6%, largely thanks to the lower volume of profit from banking activities.

Net creation of provisions and reserves in 1999 amounted to CZK -3.4 billion, as the provisions created were used to write off receivables totalling CZK 25.3 billion and because part of these provisions were used in connection with the transfers of certain large bank receivables to Konsolidační banka ahead of their privatisation. The receivables written off and the costs connected with the transfer of the receivables are reflected in other operating expenses.

## 8.3 Efficiency and productivity

The optimisation of workforce and branch networks continued into 1999, the aim being to boost productivity while improving or maintaining the quality of services. One of the major innovations facilitating parallel growth in both the efficiency of banking activities and the quality of the services offered is the automation of certain operations. This reduces the active participation of individual bank employees using state-of-the-art computer and communications technology and the active involvement of the clients themselves. The various forms of electronic banking, from payment cards to trading via the Internet, are being used to an ever greater extent by banks in the Czech Republic.

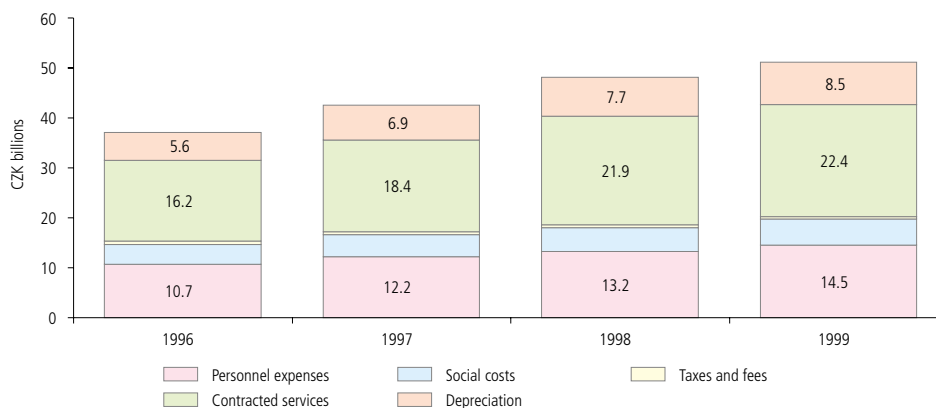
The gradual reduction in the number of employees in the banking sector over the last few years is passing through into a growing volume of total assets per employee. In comparison with the end of 1998, this volume had increased by 10.1% to CZK 51.3 billion as of 31 December 1999. The amount of profit from banking

activities per employee, which was CZK 1.8 million as of 31 December 1999, remained at the end-1998 level, owing to the overall decrease in profit from banking activities.

General operating expenses, which are of key importance for the efficiency of bank business, grew 6.7 points more slowly in 1999 than in 1998. Compared with 1997, their rate of growth was 8.3 points slower. The ongoing growth in operating expenses is *inter alia* a consequence of the shift to modern forms of electronic banking, which, even though they are labour saving, require higher initial acquisition costs. Their introduction also requires qualified staff, which is being reflected in the level of personnel expenses.

**CHART 34** STRUCTURE OF GENERAL OPERATING EXPENSES

for banks with licences as of 31 Dec. 1999, excluding Konsolidační banka

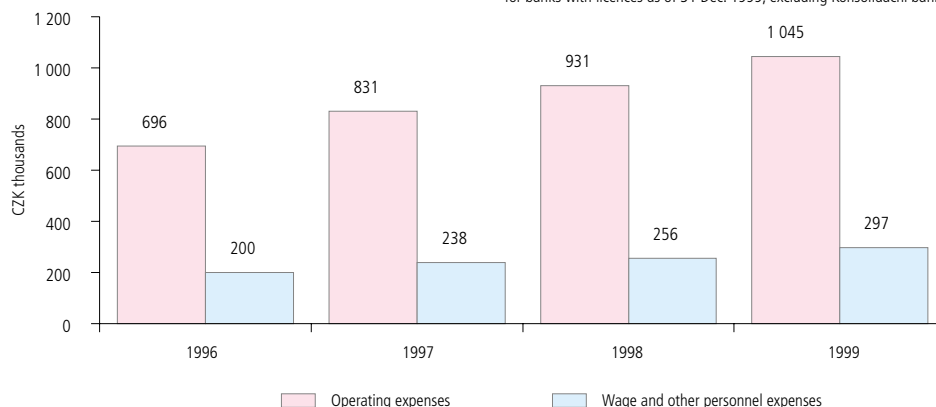


The structure of general operating expenses has not varied significantly over time. The most important item in these expenses is contracted services, where banks account for the costs of the services provided to them, as well as materials, travelling expenses, etc. In 1999 contracted services accounted for 43.9% of the total volume of general operating expenses, 1.6 points lower than in 1998. The share of personnel expenses in the structure of general operating expenses increased by 0.9 points in 1999 to 28.4%. Depreciation of tangible and intangible assets also increased, by 0.7 points to 16.7%.

Wage and other personnel expenses rose by 9.7% in 1999 to CZK 14.5 billion. The rate of growth was 1.2 points higher than a year earlier, largely because of the higher level of qualification of the staff operating the more sophisticated products and information systems.

**CHART 35** COSTS PER EMPLOYEE

for banks with licences as of 31 Dec. 1999, excluding Konsolidační banka



The different development of personnel expenses and other operating expenses, together with the downsizing of the workforce, is being reflected in different evolution of these expenses when recalculated per employee. Growth in operating expenses per employee has been gradually slowing, from just under 20% in 1997 to around 12% in 1998 and 1999, whereas growth in wage and other personnel expenses gradually decreased from just under 20% in 1997 to around 8% in 1998 then picked up again to 16% in 1999.

General operating expenses accounted for 2.27% of the average total assets of the banking sector in 1999. In comparison with the end of 1998, this represents an increase of 0.04 points, due to the faster growth in general operating expenses relative to the growth in total assets.

## 9. THE BANKING SECTOR WITH RESPECT TO THE PRUDENTIAL RULES

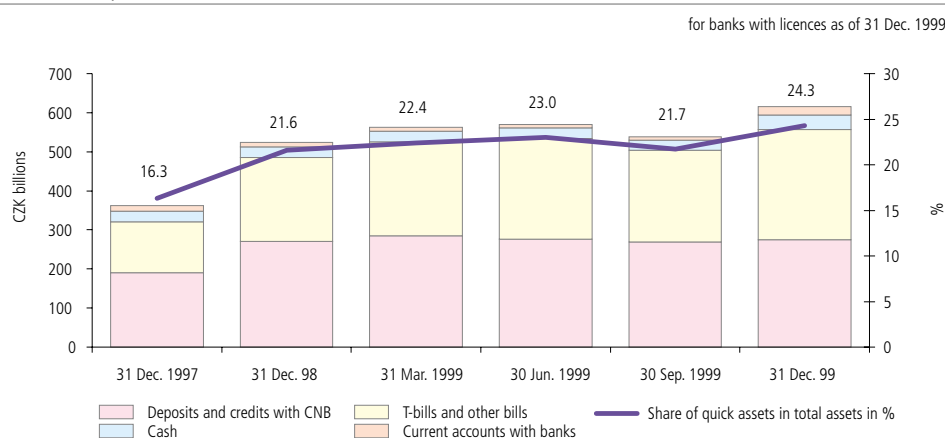
The level of risk present in the economic environment within which banks operate in the Czech Republic necessitates great emphasis on compliance with the prudential rules. The aim of these rules is to minimise the risks connected with banking activities. The most significant of the risks to which banks are currently exposed is credit risk. This is the major factor influencing the activities and financial results of banks. In contrast, other risks are not so significant as yet in the Czech banking sector, as banks are primarily engaged in the credit area and their involvement in trading in securities and derivatives, in spite of its relatively fast growth, is not very high.

### 9.1 Liquidity

(for banks with licences as of 31 December 1999)

As of 31 December 1999 the total volume of quick assets<sup>4)</sup> was CZK 615.6 billion, i.e. 17.7% higher than a year earlier. In comparison with 1998, however, their growth rate slowed by 26.8 points. If the securities included in banks' trading portfolios are also considered liquid, the volume of liquid assets rises to CZK 691.4 billion as of the end of 1999, which represents 27.3% of the overall volume of assets.

CHART 36 QUICK ASSETS



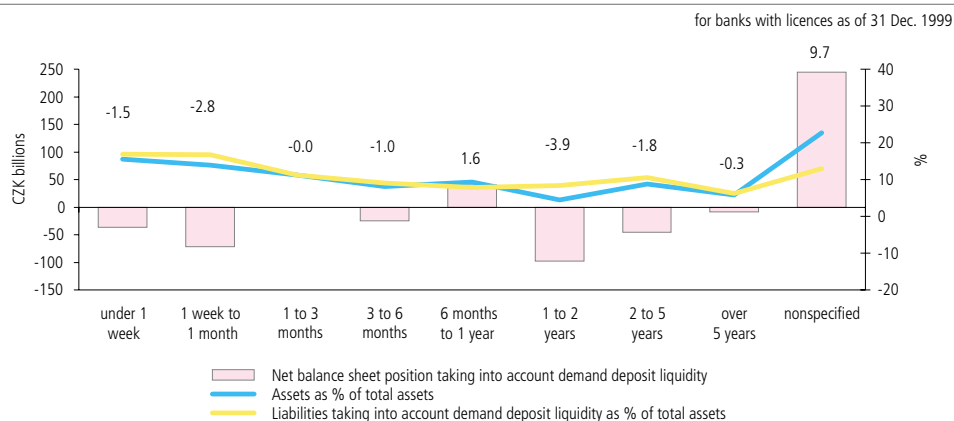
The high growth rate of quick assets is not due to a high risk of liquidity problems, but is a consequence of banks' preference for placing their free funds in quick assets, which have a low level of risk relative to credit transactions. The share of quick assets in total assets was 24.3% as of 31 December 1999, i.e. 2.7 points higher than in 1998 and 8 points higher than in 1997.

The most important item in the structure of quick assets are T-bills and CNB bills, which accounted for 45.9% of the overall volume of quick assets and stood at CZK 282.4 billion as of 31 December 1999. Of similar importance

4) Quick assets comprise cash, current accounts with banks, deposits and credits with the Czech National Bank, T-bills and CNB bills.

are deposits and credits with the central bank, including required reserves, which as of 31 December 1999 amounted to CZK 274.2 billion and accounted for almost 45% of the total volume of quick assets. Cash and current accounts maintained with other commercial banks are an insignificant component in the volume of quick assets.

**CHART 37** STRUCTURE OF ASSETS AND LIABILITIES BY RESIDUAL MATURITY AS OF 31 DEC. 1999



An important aspect of liquidity management is the balancing of maturities between the asset and liability items of the balance sheet. It is necessary to take into account, especially on the liabilities side, the stable volumes of deposits which, even though declared as demand deposits, are basically of a constant nature. Taking into account the certain degree of constancy of demand deposits, the structure of assets and liabilities in the banking sector as a whole is relatively balanced in the long term. In relation to total assets, the absolute value of the difference between the volume of balance sheet assets and liabilities with maturities of up to three months has lain within the 2%-5% range in the long term; if off-balance sheet items are included, the situation is even more favourable.

## 9.2 Quality of assets

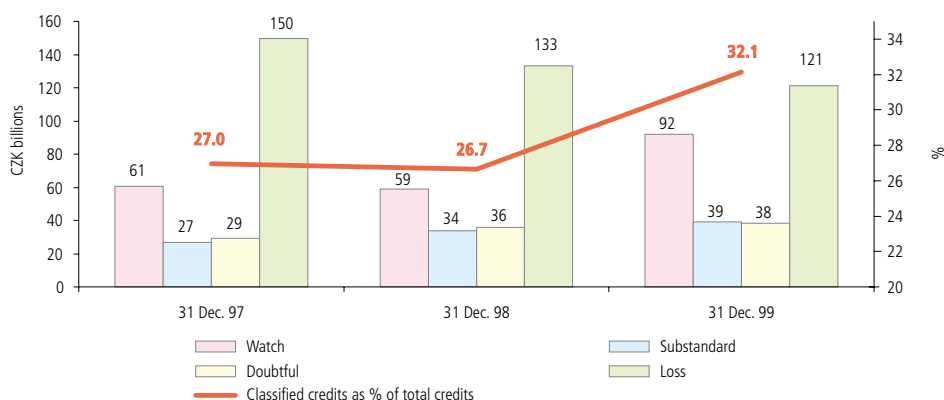
(for banks with licences as of 31 December 1998, excluding Konsolidační banka)

The high volume of classified credits in bank portfolios dates for the most part from the early period of transformation and privatisation of the economy. Although banks, particularly during the last two years, have improved their methods for granting loans, especially with respect to assessing the creditworthiness of clients, which has led to a reduction of their lending activities, the quality of credit portfolios continues to be one of the main problems of the Czech banking sector. Most recently, classified credits have also begun to be affected by the current recession in the economy.

The overall volume of classified credits was CZK 291.1 billion as of 31 December 1998, which represented 32.1% of the total credits granted and was 11.2% higher than a year earlier. This unfavourable development occurred despite the comparatively high level of write-offs of loss receivables against provisions and is related to the large share of watch credits in newly granted credits.

**CHART 38** STRUCTURE OF CLASSIFIED CREDITS

for banks with licences as of 31 Dec. 1999, excluding Konsolidační banka



Loss loans constitute the major part of classified credits. Even though in 1999, owing to write-offs and transfers of receivables to Konsolidační banka, their share decreased by 9.2 points, they still represent 41.6% of the total volume of classified credits. At the end of 1999, substandard and doubtful credits had an almost equal share in the overall volume of classified credits – 13.5% and 13.2% respectively. In 1999, the biggest growth was registered in the volume of watch credits, i.e. those with the lowest level of risk. The volume of these credits increased in absolute terms by 55.9%, which meant that their share in the structure of classified credits rose by 9.1 points to 31.7%. The rapid growth in watch credits is largely connected with the ever more frequent practice of classifying all new clients in this category until they verify their creditworthiness by repaying their debts.

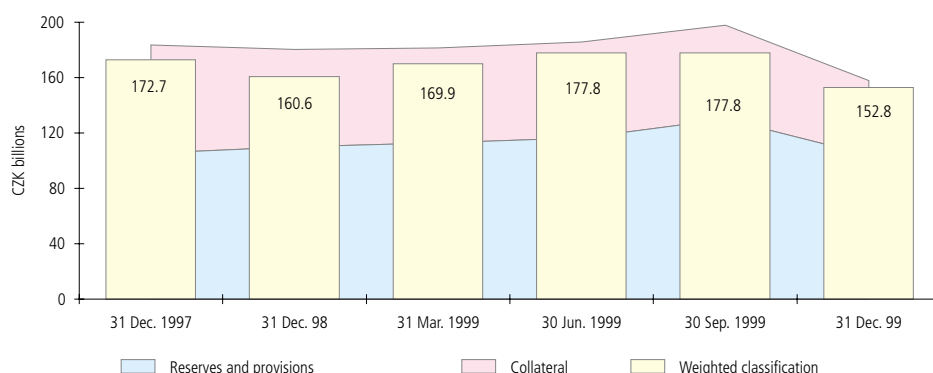
As of 31 December 1999, classified credits represented 32.1% of the overall volume of credits, i.e. 5.5 points more than at the end of 1998. Even though the growth in this share is to a certain extent due to the decreasing volume of total credits, the main growth factor is the increase in classified credits. The least favourable situation is in the group of small banks, where classified credits as of 31 December 1999 accounted for 51.4% of the total volume of credits, and in the group of large banks, where they constituted 41.3% of total credits (which is 9.6 points more than a year earlier). In contrast, the lowest volume of classified loans was registered in building societies (2.8%) and foreign bank branches (5.9%). In foreign banks, the ratio of classified credits to total credits was 18.0% at the end of 1999, 2.9 points higher than a year earlier.

The high proportion of classified credits in bank portfolios ensues from the still relatively low extent of writing off receivables against provisions and, in particular, from the difficulties in realising collateral under the present legislation. This situation ought to improve to some extent in 2000, when new legal regulations enter into force.

The favourable trend in the structure of classified credits by the degree of risk involved in the individual categories of classified receivables is reflected in a decrease in the weighted classification of the credit portfolio. In comparison with the end of 1998, the volume of this classification dropped by 4.9% to CZK 152.8 billion, which is the lowest value for the past three years.

**CHART 39** COVERAGE OF POTENTIAL LOSSES FROM THE CREDIT PORTFOLIO

for banks with licences as of 31 Dec. 1999, excluding Konsolidační banka

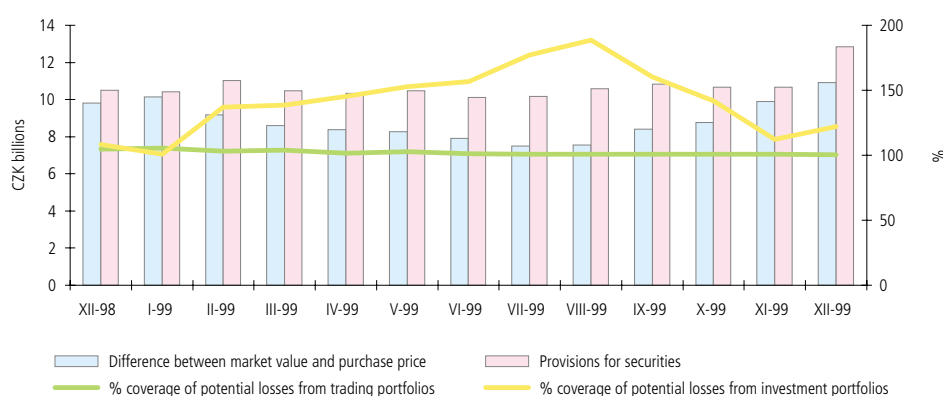


Banks create provisions and reserves to cover potential losses from their credit portfolios. As of 31 December 1999, these provisions and reserves amounted to CZK 103.8 billion, down 5.8% compared with a year earlier. The decrease in provisions and reserves occurred because CZK 25.3 billion worth of them were used for direct write-offs of loss receivables and because part of them were dissolved following the transfer of certain large bank receivables to Konsolidační banka as part of the preparation of these banks for privatisation. As of 31 December 1999, reserves and provisions covered 67.9% of the total volume of the weighted classification. The remainder was covered by high-quality collateral, which exceeded the volume required by around CZK 5 billion.

Owing to the relative instability of the capital market, the securities in banks' portfolios may go down in value. Banks are obliged to cover this devaluation with provisions. Banks provision for the securities in their investment portfolios and in their trading portfolios separately and under different rules.

**CHART 40** COVERAGE OF POTENTIAL LOSSES FROM THE SECURITIES PORTFOLIO

for banks with licences as of 31 Dec. 1999, excluding Konsolidační banka



Banks create provisions for the individual securities in their trading portfolios in order to cover the negative difference between the market value of a given security and its purchase price on a daily basis. In the case of investment portfolios, they are obliged to cover the overall difference between the market value and purchase price always at the year-end. As of 31 December 1999, the potential losses from the trading portfolio were 100% covered, while the provisions created for the investment portfolio exceeded the volume required by 22%. The overall volume of provisioning for securities as of 31 December was CZK 12.9 billion and exceeded the devaluation of the securities portfolio by CZK 2 billion.



### 9.3 Capital adequacy

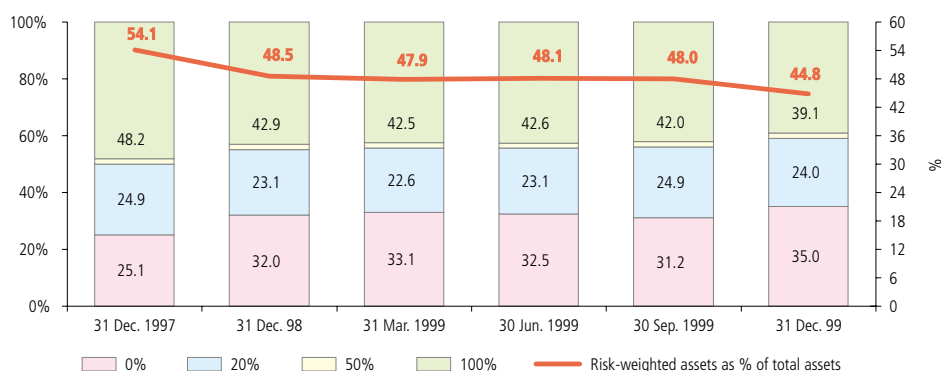
(for banks with licences as of 31 December 1999, excluding Konsolidační banka)

Capital adequacy is a measure of the real level of capital in individual banks. It reflects any positive and negative trends influencing the banking sector and has become a basic and internationally applied standard. The lower limit for acceptable capital adequacy, i.e. the minimum ratio of a bank's capital to its risk-weighted assets, has been set at 8%. Banks which operate in a higher-risk economic environment, i.e. an environment corresponding to the present situation in the Czech Republic, are recommended to maintain a minimum ratio of between 10% and 12% for safe operation

As of 31 December 1999, the overall volume of capital of the banking sector was CZK 133.8 billion, i.e. 5.3% higher than a year earlier. This increase was largely attributable to a CZK 13.1 billion overall increase in registered capital to CZK 81.8 billion and a CZK 2.6 billion increase in supplementary capital in the form of subordinated debt to CZK 26.1 billion.

**CHART 41** STRUCTURE OF ASSETS BY RISK WEIGHT

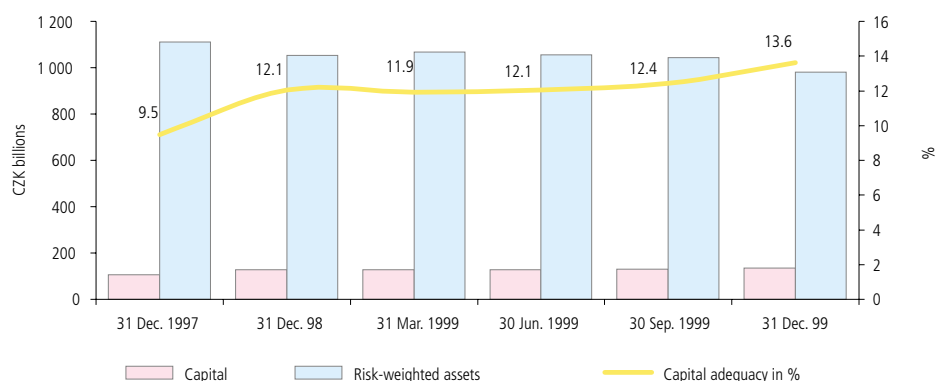
for banks with licences as of 31 Dec. 1999, excluding Konsolidační banka



The volume of risk-weighted assets decreased by 6.9% to CZK 981.1 million compared with the end of 1998, largely because of the curtailing of lending activities and the preference given to quick assets, which have a lower risk weight in the capital adequacy calculation. In 1999, the share of assets with zero risk weight increased by 3 points to 35.0% and the share of assets with 20% risk weight by 0.8 points to 23.9%. Conversely, the proportion of asset items with 100% risk weight dropped by 3.8 points to 39.1%; this represents an 8.2% absolute decrease to CZK 855.2 billion. The favourable developments in the asset risk structure were also reflected in the ratio of risk-weighted assets to total assets, which stood at 44.9%, i.e. 3.7 points lower than a year earlier and 9.2 points lower than at the end of 1997.

**CHART 42** CAPITAL ADEQUACY

for banks with licences as of 31 Dec. 1999, excluding Konsolidační banka

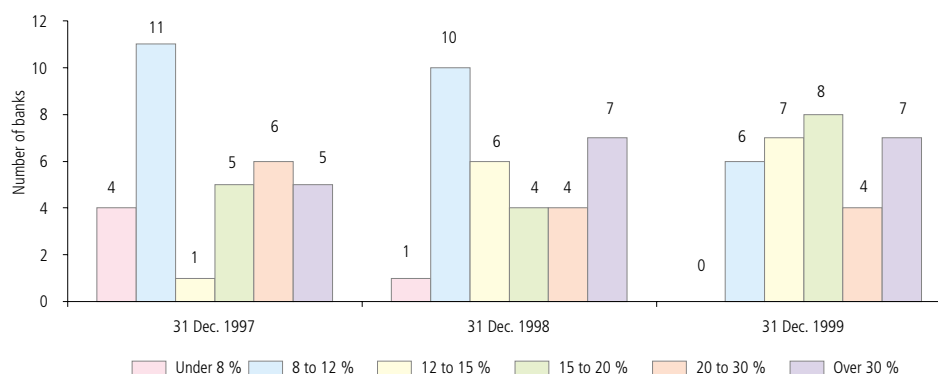


The positive developments in both components of capital adequacy, i.e. overall capital and risk-weighted assets, generated a 1.6 point increase in capital adequacy to 13.6% compared with a year earlier. This growth is attributable largely to the group of large banks, where capital adequacy rose by 1.7 points to 12.2%. The level of capital adequacy in the other bank groups did not show any major changes and considerably exceeded the required 8%.

As of 31 December 1999, all banks met the minimum capital adequacy requirement and only four had a capital adequacy ratio lower than 10%. The largest number of banks is concentrated in the group having capital adequacy of between 15% and 20%, whereas in previous years most banks had lain within the 8%-12% range. As of the end of 1999, 26 banks exceeded the 12% limit, five more than a year earlier.

**CHART 43** BREAKDOWN OF BANKS BY CAPITAL ADEQUACY

for banks with licences as of 31 Dec. 1999, excluding Konsolidační banka



The current pressure to set aside provisions and reserves is showing up negatively in the capital adequacy calculation, both in the form of growth in items deductible from the bank's capital and in the form of a lower volume of profit which may be used to boost the reserve funds or equity capital. The present capital adequacy calculation takes into account credit risk only. As from 1 April 2000, following the adoption of a new CNB banking supervision provision based on the relevant EU directive, capital adequacy will also be evaluated with regard to market risks.



**D.**

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APPENDICES

## Survey of banks and foreign bank branches as of 31 December 1999

### I. Banks

| Bank   | Start of operation | Equity capital in CZK millions | Number of banking units |                  | Number of employees |
|--|--------------------|--------------------------------|-------------------------|------------------|---------------------|
|  |                    |                                | in CR                   | abroad (country) |                     |
| Česká spořitelna, a.s.                             | 1 Jan. 1969        | 15 200                         | 876                     | 1                | 15 316              |
| Československá obchodní banka, a.s.                | 1 Jan. 1965        | 5 105                          | 48                      | 17               | 4 710               |
| INVESTIČNÍ A POŠTOVNÍ BANKA, a.s.                  | 1 Jan. 1990        | 13 383                         | 214                     | 5                | 5 083               |
| Komerční banka, a.s.                               | 1 Jan. 1990        | 9 502                          | 349                     | 5                | 13 433              |
| Konsolidační banka, s.p.ú.                         | 23 Feb. 1993       | 5 950                          | 0                       | 0                | 400                 |
| BANKA HANÁ, a.s.                                   | 11 Jan. 1991       | 1 020                          | 1                       | 0                | 31                  |
| PLZEŇSKÁ BANKA, a.s.                               | 1 Oct. 1993        | 1 000                          | 1                       | 0                | 41                  |
| První městská banka, a.s.                          | 1 Sep. 1993        | 850                            | 0                       | 0                | 96                  |
| Union banka, a.s.                                  | 15 Nov. 1991       | 2 444                          | 104                     | 0                | 1 220               |
| EXPANDIA BANKA, a.s.                               | 1 Jan. 1991        | 500                            | 0                       | 0                | 287                 |
| Bank Austria Creditanstalt Czech Republic a.s.     | 1 Apr. 1991        | 1 997                          | 17                      | 0                | 725                 |
| BNP-Dresdner Bank (ČR), a.s.                       | 12 May 1992        | 1 000                          | 1                       | 0                | 172                 |
| Citibank, a.s.                                     | 24 Jun. 1991       | 2 425                          | 5                       | 0                | 335                 |
| CREDIT LYONNAIS BANK PRAHA, a.s.                   | 12 Nov. 1992       | 500                            | 1                       | 0                | 120                 |
| Erste Bank Sparkassen (CR) a.s.                    | 1 Feb. 1993        | 700                            | 7                       | 0                | 257                 |
| GE Capital Bank, a.s.                              | 22 Jun. 1998       | 510                            | 246                     | 0                | 2 117               |
| HypoVereinsbank CZ a.s.                            | 1 Jul. 1992        | 5 047                          | 18                      | 0                | 460                 |
| IC Banka, a.s.                                     | 6 Apr. 1994        | 500                            | 1                       | 0                | 36                  |
| Interbanka, a.s.                                   | 1 Feb. 1991        | 1 709                          | 0                       | 0                | 101                 |
| J & T Banka, a.s.                                  | 18 Dec. 1992       | 501                            | 0                       | 0                | 37                  |
| Raiffeisenbank a.s.                                | 1 Jul. 1993        | 1 000                          | 15                      | 0                | 331                 |
| VOLKSBANK, a.s.                                    | 1 Jan. 1994        | 650                            | 8                       | 0                | 176                 |
| Živnostenská banka, a.s.                           | 1868               | 1 360                          | 11                      | 1                | 705                 |
| Raiffeisen stavební spořitelna a.s.                | 7 Sep. 1993        | 500                            | 0                       | 0                | 402                 |
| Českomoravská stavební spořitelna, a.s.            | 8 Sep. 1993        | 1 500                          | 5                       | 0                | 477                 |
| ČS-stavební spořitelna, a.s.                       | 1 Jul. 1964        | 750                            | 0                       | 0                | 253                 |
| HYPO stavební spořitelna, a.s.                     | 1 Oct. 1994        | 500                            | 3                       | 0                | 56                  |
| Všeobecná stavební spořitelna Komerční banky, a.s. | 16 Dec. 1993       | 500                            | 0                       | 0                | 323                 |
| Wüstenrot-Stavební spořitelna, a.s.                | 11 Nov. 1993       | 500                            | 0                       | 0                | 142                 |
| Českomoravská záruční a rozvojová banka, a.s.      | 1 Mar. 1992        | 1 100                          | 5                       | 0                | 224                 |
| Českomoravská hypoteční banka, a.s.                | 10 Jan. 1991       | 1 128                          | 57                      | 0                | 266                 |
| Česká exportní banka, a.s.                         | 1 Jul. 1995        | 1 500                          | 0                       | 0                | 106                 |

## II. Foreign bank branches

| Bank  | Start of operation | Home country  | Number of banking units |                  | Number of employees |
|---|--------------------|---------------|-------------------------|------------------|---------------------|
|   |                    |               | in CR                   | abroad (country) |                     |
| ABN AMRO BANK N.V.  | 6 May 1993         | Netherlands   | 1                       | 0                | 130                 |
| COMMERZBANK AG  | 1 Dec. 1992        | Germany       | 1                       | 0                | 176                 |
| Deutsche Bank Aktiengesellschaft Filiale Prag, organizační složka | 1 Dec. 1993        | Germany       | 0                       | 0                | 103                 |
| ING Bank N.V.   | 1 Sep. 1993        | Netherlands   | 0                       | 0                | 148                 |
| HSBC Bank plc - pobočka Praha                                     | 1 May 1997         | Great Britain | 0                       | 0                | 30                  |
| Raiffeisenbank im Stiftland Waldsassen AG, odštěpný závod Cheb    | 1 Jan. 1995        | Germany       | 1                       | 0                | 23                  |
| SOCIETE GENERALE, pobočka PRAHA                                   | 15 Apr. 1991       | France        | 2                       | 0                | 170                 |
| Sparkasse Mühlviertel - West banka, pobočka České Budějovice      | 20 Mar. 1995       | Austria       | 5                       | 0                | 49                  |
| Všeobecná úverová banka, a.s., pobočka Praha                      | 14 Jan. 1993       | Slovakia      | 1                       | 0                | 64                  |
| Waldviertler Sparkasse von 1842                                   | 1 May 1994         | Austria       | 2                       | 0                | 24                  |

## III. Banks in liquidation

| Bank                                   | Start of operation | Revocation of licence |
|--|--------------------|-----------------------|
| Agrobanka Praha, a.s. - in liquidation | 1 Jul. 1990        | 2 Sep. 1998           |
| Banka Bohemia, a.s. - in liquidation   | 1 Feb. 1991        | not revoked           |
| Baska a.s. - in liquidation            | 13 Dec. 1990       | 31 Mar. 1997          |
| Ekoagrobanka, a.s. - in liquidation    | 1 Nov. 1990        | 31 May 1997           |
| Evrobanka, a.s. - in liquidation       | 1 Oct. 1991        | 3 Jun. 1997           |
| COOP BANKA, a.s. - in liquidation      | 24 Feb. 1992       | 6 May 1998            |

## IV. Banks in bankruptcy proceedings

| Bank  | Start of operation | Revocation of licence | Beginning of bankruptcy proceedings |
|---|--------------------|-----------------------|-------------------------------------|
| AB Banka, a.s. - in liquidation                               | 1 Apr. 1991        | 15 Dec. 1995          | 18 Mar. 1999                        |
| Česká banka, akciová společnost Praha - in liquidation        | 28 Feb. 1992       | 14 Dec. 1995          | 28 Jun. 1996                        |
| Kreditní banka Plzeň, a.s. - in liquidation                   | 1 Jan. 1991        | 8 Aug. 1996           | 21 Dec. 1998                        |
| Kreditní a průmyslová banka, a.s. - in bankruptcy proceedings | 1 Apr. 1991        | 31 Aug. 1995          | 2 Oct. 1995                         |
| Realitbanka, a.s. - in bankruptcy proceedings                 | 1 Nov. 1991        | 17 Apr. 1997          | 24 Mar. 1997                        |
| Velkomoravská banka, a.s. - in bankruptcy proceedings         | 3 Nov. 1992        | 10 Jul. 1998          | 2 Jul. 1998                         |
| Pragobanka, a.s. - in bankruptcy proceedings                  | 1 Oct. 1990        | 24 Oct. 1998          | 19 Nov. 1998                        |
| První slezská banka a.s. - in liquidation                     | 12 Jan. 1993       | 13 May 1996           | 20 Nov. 1997                        |
| Moravia banka a.s.  | 2 Jul. 1992        | 9 Nov. 1999           | 8 Dec. 1999                         |
| UNIVERSAL BANKA, a.s.   | 15 Feb. 1993       | 10 Feb. 1999          | 12 Feb. 1999                        |

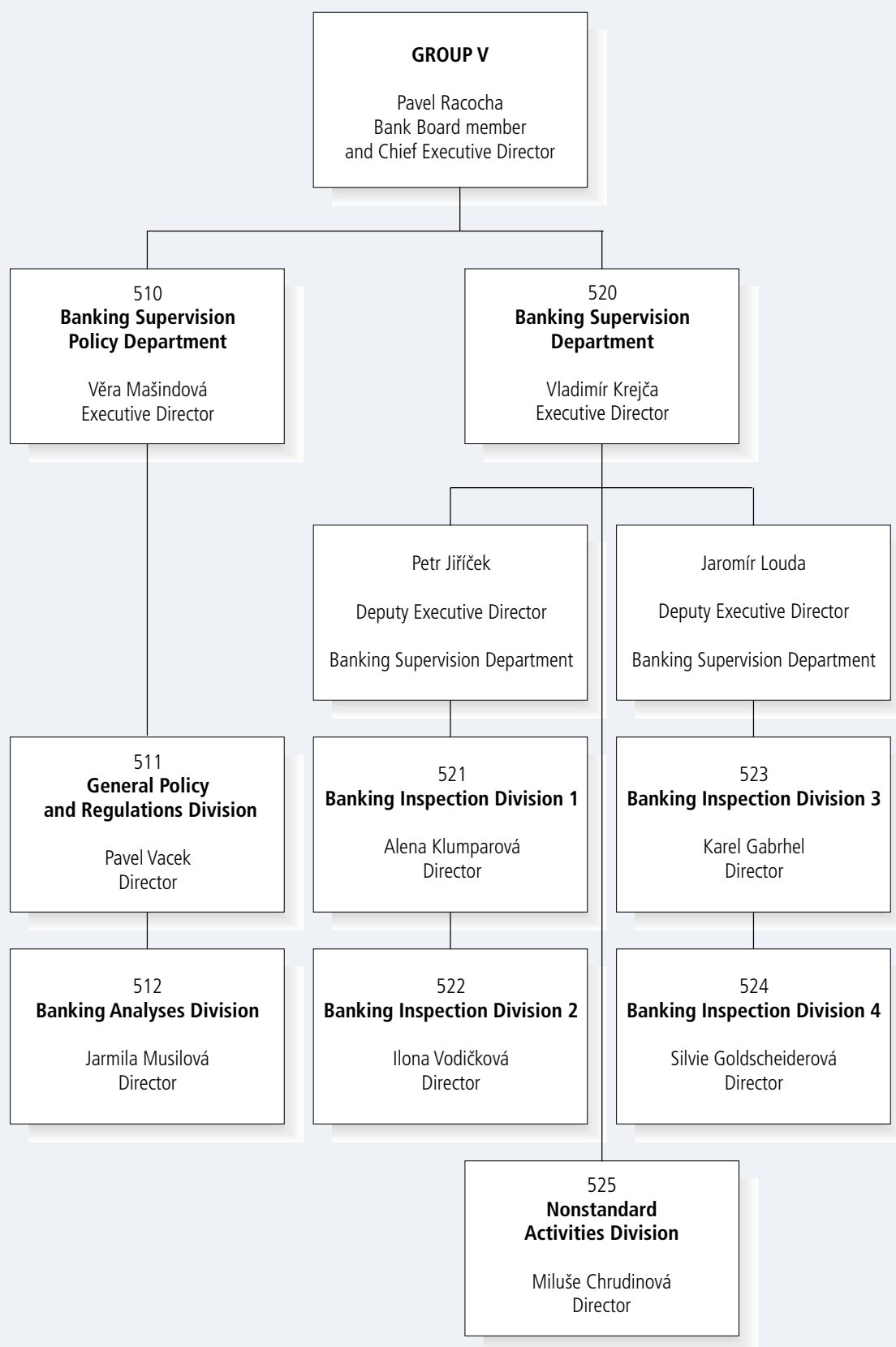
## V. Banks dissolved without liquidation

| Bank                               | Start of operation    | Termination of licence | Reason                |
|------------------------------------|-----------------------|------------------------|-----------------------|
| Poštovní banka, a.s.               | 1 Jan. 1991           | 1 Jan. 1994            | merger                |
| Bank Austria a.s.                  | 1 Jan. 1992           | 30 Jun. 1998           | merger                |
| Westdeutsche Landesbank (CZ), a.s. | operation not started | 20 Jan. 1998           | operation not started |
| HYPOT-BANK CZ a.s.                 | 26 Feb. 1992          | 31 Dec. 1998           | merger                |

## VI. Former banks operating at present as joint-stock companies only, without banking licence

| Bank            | Start of operation | Termination of licence |
|-----------------|--------------------|------------------------|
| Foresbank, a.s. | 7 Sep. 1993        | 1 Mar. 1999            |

## Organisational structure of the CNB Banking Supervision Group



## BREAKDOWN OF BANKS INTO GROUPS

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### I. Large banks

1. Česká spořitelna, a.s.
2. Československá obchodní banka, a.s.
3. INVESTIČNÍ A POŠTOVNÍ BANKA, a.s.
4. Komerční banka, a.s.
5. Konsolidační banka, s.p.ú.

### II. Small banks

1. BANKA HANÁ, a.s.
2. PLZEŇSKÁ BANKA, a.s.
3. První městská banka, a.s.
4. Union banka, a.s.
5. EXPANDIA BANKA, a.s.

### III. Foreign banks

1. Bank Austria Creditanstalt, a.s.
2. BNP- Dresdner Bank (ČR), a.s.
3. Citibank, a.s.
4. CREDIT LYONNAIS BANK PRAHA, a.s.
5. Erste Bank Sparkassen (CR) a.s.
6. GE Capital Bank, a.s.
7. HypoVereinsbank CZ a.s.
8. IC Banka, a.s.
9. Interbanka, a.s.
10. J & T Banka, a.s.
11. Raiffeisenbank a.s.
12. VOLKSBANK, a.s.
13. Živnostenská banka, a.s.

### IV. Foreign bank branches

1. ABN AMRO BANK N.V.
2. COMMERZBANK AG
3. Deutsche Bank Aktiengesellschaft Filiale Prag, organizační složka
4. ING Bank N.V.
5. HSBC Bank plc - pobočka Praha
6. Raiffeisenbank im Stiftland Waldsassen AG, odštěpný závod Cheb
7. SOCIETE GENERALE, pobočka PRAHA
8. Sparkasse Mühlviertel - West banka, pobočka České Budějovice
9. Všeobecná úverová banka, a.s., pobočka Praha
10. Waldviertler Sparkasse von 1842

### V. Specialised banks

1. Raiffeisen stavební spořitelna a.s.
2. Českomoravská stavební spořitelna, a.s.
3. ČS-stavební spořitelna, a.s.
4. HYPO stavební spořitelna, a.s.
5. Všeobecná stavební spořitelna Komerční banky, a.s.
6. Wüstenrot-Stavební spořitelna, a.s.
7. Českomoravská záruční a rozvojová banka, a.s.
8. Českomoravská hypoteční banka, a.s.
9. Česká exportní banka, a.s.



## Main indicators of monetary and economic developments in the Czech Republic

|   |                                     | 1996     | 1997     | 1998     | 1999     |
|---|-------------------------------------|----------|----------|----------|----------|
| Gross domestic product <sup>1), 2)</sup>                        | Value (in CZK billions)             | 1 447.7  | 1 432.8  | 1 401.3  | 1397.9   |
|   | Increase (%)                        | 4.8      | -1.0     | -2.2     | -0.2     |
| Output - increase in % <sup>2)</sup>                            | Industry                            | 2.0      | 4.5      | 1.6      | -3.1     |
|   | Construction                        | 5.3      | -3.9     | -7.0     | -6.5     |
|   | Inflation rate (%)                  | 8.8      | 8.5      | 10.7     | 2.1      |
| Prices  | Inflation rate (%)                  | 8.8      | 8.5      | 10.7     | 2.1      |
| Unemployment <sup>3)</sup>                                      | Unemployment rate (%)               | 3.5      | 5.2      | 7.5      | 9.4      |
| Foreign trade   | Exports (in CZK billions)           | 594.6    | 722.5    | 850.3    | 929.2    |
|   | Imports (in CZK billions)           | 752.3    | 870.7    | 928.9    | 997.3    |
|   | Balance (in CZK billions)           | -157.7   | -148.2   | -78.6    | -68.1    |
| Average wage <sup>2)</sup>                                      | Nominal (%)                         | 18.4     | 10.5     | 9.4      | 8.2      |
|   | Real (%)                            | 8.8      | 1.9      | -1.2     | 6.0      |
| Balance of payments   | Current account (in USD millions)   | -4 292.2 | -3 211.0 | -1 335.7 | -1 058.2 |
|   | Financial account (in USD millions) | 4 184.3  | 1 081.9  | 2 923.1  | 2 483.5  |
| Exchange rate <sup>4)</sup>                                     | CZK/USD                             | 27.14    | 31.71    | 32.27    | 34.60    |
|   | CZK/DEM                             | 18.06    | 18.28    | 18.33    | 18.90    |
| Average interbank deposit<br>rate (PRIBOR)<br>(%) <sup>4)</sup> | 7 day                               | 12.04    | 18.31    | 14.15    | 6.83     |
|   | 3 month                             | 12.01    | 15.97    | 14.33    | 6.84     |
|   | 6 month                             | 11.95    | 15.15    | 14.23    | 6.87     |
| Discount rate (%) <sup>3)</sup>                                 |                                     | 10.5     | 13.0     | 7.5      | 5.0      |
| Lombard rate (%) <sup>3)</sup>                                  |                                     | 14.0     | 23.0     | 12.5     | 7.5      |

1) In constant 1995 prices

2) Increase in % on a year earlier

3) End-of-period data

4) Annual averages

## Assets

(for banks with licences as of 31 December 1999)

|                                 | 31 Dec. 1997     | 31 Dec. 1998     | 1999             |                  |                  |                  |
|---------------------------------|------------------|------------------|------------------|------------------|------------------|------------------|
|                                 |                  |                  | 31 Mar.          | 30 Jun.          | 30 Sep.          | 31 Dec.          |
|                                 |                  |                  | in CZK millions  |                  |                  |                  |
| Cash                            | 26 685           | 27 016           | 27 280           | 27 920           | 27 145           | 36 903           |
| Deposits and credits with CNB   | 190 733          | 269 934          | 284 850          | 276 647          | 268 574          | 274 204          |
| of which: required reserves     | 86 279           | 86 827           | 62 204           | 51 645           | 68 189           | 28 019           |
| Deposits and credits with banks | 482 003          | 497 628          | 494 367          | 519 111          | 574 225          | 572 957          |
| of which: current accounts      | 18 725           | 18 112           | 19 162           | 22 676           | 13 830           | 23 210           |
| time deposits                   | 390 837          | 392 062          | 390 674          | 411 803          | 447 194          | 407 410          |
| credits granted                 | 72 441           | 87 453           | 84 531           | 84 632           | 113 201          | 142 337          |
| T-bills                         | 38 613           | 53 394           | 39 195           | 56 192           | 48 474           | 80 532           |
| CNB bills                       | 91 957           | 161 710          | 201 002          | 200 536          | 186 168          | 201 900          |
| Credits granted (net)           | 998 451          | 1 003 635        | 1 031 935        | 1 025 664        | 988 850          | 943 882          |
| of which: to clients            | 977 840          | 975 866          | 1 000 537        | 994 988          | 958 043          | 910 715          |
| to state and local authorities  | 20 612           | 27 769           | 31 398           | 30 676           | 30 807           | 33 167           |
| Trading securities              | 97 509           | 96 362           | 88 696           | 88 333           | 83 827           | 75 739           |
| of which: bonds                 | 87 887           | 92 177           | 83 531           | 81 884           | 79 538           | 72 812           |
| equity securities               | 9 621            | 4 184            | 5 164            | 6 449            | 4 289            | 2 927            |
| Long-term financial investments | 91 058           | 92 760           | 93 585           | 95 893           | 93 908           | 122 222          |
| Tangible and intangible assets  | 61 888           | 62 999           | 62 127           | 62 479           | 62 606           | 63 153           |
| Other assets                    | 143 416          | 158 798          | 190 365          | 126 664          | 149 193          | 162 405          |
| <b>Total assets</b>             | <b>2 222 313</b> | <b>2 424 235</b> | <b>2 513 401</b> | <b>2 479 439</b> | <b>2 482 972</b> | <b>2 533 895</b> |
|                                 | in %             |                  |                  |                  |                  |                  |
| Cash                            | 1.20             | 1.11             | 1.09             | 1.13             | 1.09             | 1.46             |
| Deposits and credits with CNB   | 8.58             | 11.13            | 11.33            | 11.16            | 10.82            | 10.82            |
| of which: required reserves     | 3.88             | 3.58             | 2.47             | 2.08             | 2.75             | 1.11             |
| Deposits and credits with banks | 21.69            | 20.53            | 19.67            | 20.94            | 23.13            | 22.61            |
| of which: current accounts      | 0.84             | 0.75             | 0.76             | 0.91             | 0.56             | 0.92             |
| time deposits                   | 17.59            | 16.17            | 15.54            | 16.61            | 18.01            | 16.08            |
| credits granted                 | 3.26             | 3.61             | 3.36             | 3.41             | 4.56             | 5.62             |
| T-bills                         | 1.74             | 2.20             | 1.56             | 2.27             | 1.95             | 3.18             |
| CNB bills                       | 4.14             | 6.67             | 8.00             | 8.09             | 7.50             | 7.97             |
| Credits granted (net)           | 44.93            | 41.40            | 41.06            | 41.37            | 39.83            | 37.25            |
| of which: to clients            | 44.00            | 40.25            | 39.81            | 40.13            | 38.58            | 35.94            |
| to state and local authorities  | 0.93             | 1.15             | 1.25             | 1.24             | 1.24             | 1.31             |
| Trading securities              | 4.39             | 3.97             | 3.53             | 3.56             | 3.38             | 2.99             |
| of which: bonds                 | 3.95             | 3.80             | 3.32             | 3.30             | 3.20             | 2.87             |
| equity securities               | 0.43             | 0.17             | 0.21             | 0.26             | 0.17             | 0.12             |
| Long-term financial investments | 4.10             | 3.83             | 3.72             | 3.87             | 3.78             | 4.82             |
| Tangible and intangible assets  | 2.78             | 2.60             | 2.47             | 2.52             | 2.52             | 2.49             |
| Other assets                    | 6.45             | 6.55             | 7.57             | 5.11             | 6.01             | 6.41             |
| <b>Total assets</b>             | <b>100.00</b>    | <b>100.00</b>    | <b>100.00</b>    | <b>100.00</b>    | <b>100.00</b>    | <b>100.00</b>    |

## Liabilities

(for banks with licences as of 31 December 1999)

|                                  | 31 Dec. 1997 | 31 Dec. 1998 | 1999            |           |           |           |
|----------------------------------|--------------|--------------|-----------------|-----------|-----------|-----------|
|                                  |              |              | 31 Mar.         | 30 Jun.   | 30 Sep.   | 31 Dec.   |
|                                  |              |              | in CZK millions |           |           |           |
| Funds from CNB                   | 73 856       | 52 843       | 50 988          | 49 844    | 35 067    | 33 764    |
| Deposits and credits from banks  | 508 760      | 504 615      | 499 991         | 476 964   | 468 408   | 492 039   |
| of which: current accounts       | 19 551       | 12 198       | 15 942          | 17 423    | 12 145    | 10 017    |
| time deposits                    | 366 593      | 342 206      | 319 285         | 307 137   | 303 066   | 303 586   |
| credits received                 | 122 616      | 150 212      | 164 764         | 152 404   | 153 197   | 178 436   |
| Deposits received                | 1 114 915    | 1 219 014    | 1 234 757       | 1 260 934 | 1 294 428 | 1 314 557 |
| of which: from clients           | 1 062 325    | 1 161 974    | 1 178 939       | 1 199 728 | 1 211 504 | 1 256 725 |
| from state and local authorities | 51 204       | 55 062       | 53 804          | 59 107    | 80 331    | 54 590    |
| deposit certificates             | 1 386        | 1 978        | 2 014           | 2 099     | 2 594     | 3 242     |
| Bond issues                      | 92 724       | 92 588       | 99 800          | 99 166    | 102 019   | 98 495    |
| Reserves                         | 40 014       | 41 275       | 39 316          | 36 255    | 46 675    | 45 317    |
| Reserve funds                    | 72 328       | 73 938       | 75 065          | 66 935    | 67 232    | 67 111    |
| Capital funds                    | 19 369       | 33 967       | 34 478          | 12 893    | 12 723    | 12 958    |
| Equity capital                   | 63 819       | 74 855       | 75 443          | 76 814    | 84 914    | 87 934    |
| Retained profits                 | 1 332        | 2 110        | 10 653          | 4 236     | 3 050     | 3 123     |
| Current year profit              | 11 185       | 9 655        | 3 802           | 6 335     | 8 410     | 10 803    |
| Other liabilities                | 224 011      | 319 375      | 389 107         | 389 063   | 360 047   | 367 794   |
| Total liabilities                | 2 222 313    | 2 424 235    | 2 513 401       | 2 479 439 | 2 482 972 | 2 533 895 |
|                                  | in %         |              |                 |           |           |           |
| Funds from CNB                   | 3.32         | 2.18         | 2.03            | 2.01      | 1.41      | 1.33      |
| Deposits and credits from banks  | 22.89        | 20.82        | 19.89           | 19.24     | 18.86     | 19.42     |
| of which: current accounts       | 0.88         | 0.50         | 0.63            | 0.70      | 0.49      | 0.40      |
| time deposits                    | 16.50        | 14.12        | 12.70           | 12.39     | 12.21     | 11.98     |
| credits received                 | 5.52         | 6.20         | 6.56            | 6.15      | 6.17      | 7.04      |
| Deposits received                | 50.17        | 50.28        | 49.13           | 50.86     | 52.13     | 51.88     |
| of which: from clients           | 47.80        | 47.93        | 46.91           | 48.39     | 48.79     | 49.60     |
| from state and local authorities | 2.30         | 2.27         | 2.14            | 2.38      | 3.24      | 2.15      |
| deposit certificates             | 0.06         | 0.08         | 0.08            | 0.08      | 0.10      | 0.13      |
| Bond issues                      | 4.17         | 3.82         | 3.97            | 4.00      | 4.11      | 3.89      |
| Reserves                         | 1.80         | 1.70         | 1.56            | 1.46      | 1.88      | 1.79      |
| Reserve funds                    | 3.25         | 3.05         | 2.99            | 2.70      | 2.71      | 2.65      |
| Capital funds                    | 0.87         | 1.40         | 1.37            | 0.52      | 0.51      | 0.51      |
| Equity capital                   | 2.87         | 3.09         | 3.00            | 3.10      | 3.42      | 3.47      |
| Retained profits                 | 0.06         | 0.09         | 0.42            | 0.17      | 0.12      | 0.12      |
| Current year profit              | 0.50         | 0.40         | 0.15            | 0.26      | 0.34      | 0.43      |
| Other liabilities                | 10.08        | 13.17        | 15.48           | 15.69     | 14.50     | 14.51     |
| Total liabilities                | 100.00       | 100.00       | 100.00          | 100.00    | 100.00    | 100.00    |

## Off-balance-sheet assets

(for banks with licences as of 31 December 1999)

|   | 31 Dec. 1997     | 31 Dec. 1998     | 1999             |                  |                  |                  |
|---|------------------|------------------|------------------|------------------|------------------|------------------|
|   |                  |                  | 31 Mar.          | 30 Jun.          | 30 Sep.          | 31 Dec.          |
| in CZK millions                           |                  |                  |                  |                  |                  |                  |
| Credit commitments provided               | 108 719          | 154 910          | 136 195          | 156 763          | 162 060          | 177 425          |
| Receivables from guarantees               | 99 424           | 116 911          | 106 407          | 106 892          | 107 976          | 108 442          |
| Receivables from letters of credit        | 19 216           | 15 453           | 16 607           | 17 392           | 15 109           | 13 673           |
| Receivables from spot transactions        | 106 825          | 138 211          | 258 211          | 239 082          | 276 828          | 39 710           |
| Receivables from futures, forwards, swaps | 830 983          | 1 385 198        | 1 630 039        | 1 526 999        | 1 430 575        | 1 644 587        |
| Receivables from options transactions     | 30 932           | 84 508           | 131 515          | 140 365          | 135 524          | 85 578           |
| <b>Total off-balance-sheet assets</b>     | <b>1 196 100</b> | <b>1 895 191</b> | <b>2 278 975</b> | <b>2 187 495</b> | <b>2 128 072</b> | <b>2 069 415</b> |
| in %                                      |                  |                  |                  |                  |                  |                  |
| Credit commitments provided               | 9.09             | 8.17             | 5.98             | 7.17             | 7.62             | 8.57             |
| Receivables from guarantees               | 8.31             | 6.17             | 4.67             | 4.89             | 5.07             | 5.24             |
| Receivables from letters of credit        | 1.61             | 0.82             | 0.73             | 0.80             | 0.71             | 0.66             |
| Receivables from spot transactions        | 8.93             | 7.29             | 11.33            | 10.93            | 13.01            | 1.92             |
| Receivables from futures, forwards, swaps | 69.47            | 73.09            | 71.53            | 69.81            | 67.22            | 79.47            |
| Receivables from options transactions     | 2.59             | 4.46             | 5.77             | 6.42             | 6.37             | 4.14             |
| <b>Total off-balance-sheet assets</b>     | <b>100.00</b>    | <b>100.00</b>    | <b>100.00</b>    | <b>100.00</b>    | <b>100.00</b>    | <b>100.00</b>    |

## Off-balance-sheet liabilities

(for banks with licences as of 31 December 1999)

|  | 31 Dec. 1997     | 31 Dec. 1998     | 1999             |                  |                  |                  |
|--|------------------|------------------|------------------|------------------|------------------|------------------|
|  |                  |                  | 31 Mar.          | 30 Jun.          | 30 Sep.          | 31 Dec.          |
| in CZK millions                            |                  |                  |                  |                  |                  |                  |
| Credit commitments accepted                | 30 051           | 34 125           | 35 358           | 35 971           | 26 119           | 41 068           |
| Payables from guarantees                   | 217 559          | 250 195          | 273 585          | 281 816          | 282 715          | 287 869          |
| Payables from letters of credit            | 1 106            | 758              | 378              | 1 239            | 1 199            | 801              |
| Payables from spot transactions            | 103 691          | 137 892          | 255 497          | 234 987          | 275 513          | 41 240           |
| Payables from futures, forwards, swaps     | 822 929          | 1 357 361        | 1 633 764        | 1 527 801        | 1 420 341        | 1 640 391        |
| Payables from options transactions         | 31 293           | 83 136           | 131 050          | 141 190          | 133 152          | 83 478           |
| <b>Total off-balance-sheet liabilities</b> | <b>1 206 628</b> | <b>1 863 467</b> | <b>2 329 633</b> | <b>2 223 005</b> | <b>2 139 039</b> | <b>2 094 847</b> |
| in %                                       |                  |                  |                  |                  |                  |                  |
| Credit commitments accepted                | 2.49             | 1.83             | 1.52             | 1.62             | 1.22             | 1.96             |
| Payables from guarantees                   | 18.03            | 13.43            | 11.74            | 12.68            | 13.22            | 13.74            |
| Payables from letters of credit            | 0.09             | 0.04             | 0.02             | 0.06             | 0.06             | 0.04             |
| Payables from spot transactions            | 8.59             | 7.40             | 10.97            | 10.57            | 12.88            | 1.97             |
| Payables from futures, forwards, swaps     | 68.20            | 72.84            | 70.13            | 68.73            | 66.40            | 78.31            |
| Payables from options transactions         | 2.59             | 4.46             | 5.63             | 6.35             | 6.22             | 3.98             |
| <b>Total off-balance-sheet liabilities</b> | <b>100.00</b>    | <b>100.00</b>    | <b>100.00</b>    | <b>100.00</b>    | <b>100.00</b>    | <b>100.00</b>    |

## Income and expenses

(for banks with licences as of 31 December 1999, excluding Konsolidační banka, in CZK millions)

|  | 31 Dec. 1997 | 31 Dec. 1998 | 1999    |         |         |         |
|--|--------------|--------------|---------|---------|---------|---------|
|  |              |              | 31 Mar. | 30 Jun. | 30 Sep. | 31 Dec. |
| Interest income                            | 171 194      | 227 660      | 47 653  | 91 672  | 131 072 | 167 983 |
| Interest expenses                          | 121 510      | 161 666      | 33 003  | 62 789  | 87 973  | 109 649 |
| Interest profit                            | 49 684       | 65 994       | 14 650  | 28 883  | 43 099  | 58 334  |
| Income from fees and charges               | 13 273       | 17 067       | 4 287   | 9 085   | 13 985  | 19 959  |
| Expenses from fees and charges             | 1 594        | 4 151        | 1 423   | 2 077   | 3 563   | 5 320   |
| Profit from fees and charges               | 11 679       | 12 916       | 2 864   | 7 007   | 10 422  | 14 638  |
| Interest profit including fees and charges | 61 363       | 78 910       | 17 514  | 35 891  | 53 521  | 72 972  |
| Profit from securities                     | 12 110       | 2 270        | 981     | 285     | 2 062   | 4 141   |
| Profit from foreign exchange operations    | 12 733       | 12 856       | 2 846   | 5 380   | 8 711   | 11 858  |
| Profit from other banking operations       | 1 207        | 2 824        | 388     | 793     | 1 155   | 1 351   |
| Profit from banking activities             | 87 412       | 96 860       | 21 728  | 42 348  | 65 448  | 90 323  |
| General operating expenses                 | 42 519       | 48 094       | 10 836  | 23 456  | 35 295  | 51 149  |
| Creation of reserves and provisions (net)  | 29 726       | 14 673       | -284    | 2 112   | 18 025  | -3 376  |
| Other operating income (+) / expenses (-)  | -18 146      | -42 218      | -10 142 | -17 286 | -16 379 | -49 742 |
| Gross operating profit                     | -2 979       | -8 126       | 1 033   | -506    | -4 251  | -7 192  |
| Extraordinary income (+) / expenses (-)    | 702          | 2 958        | 201     | 689     | 1 069   | 2 700   |
| Pre-tax gross profit                       | -2 277       | -5 167       | 1 235   | 183     | -3 182  | -4 492  |
| Taxes                                      | 1 080        | 3 069        | 175     | 464     | 1 026   | 1 137   |
| Net profit                                 | -3 356       | -8 236       | 1 059   | -281    | -4 208  | -5 628  |

## Profitability and efficiency

(for banks with licences as of 31 December 1999, excluding Konsolidační banka)

|   | 31 Dec. 1997 | 31 Dec. 1998 | 1999    |         |         |         |
|---|--------------|--------------|---------|---------|---------|---------|
|   |              |              | 31 Mar. | 30 Jun. | 30 Sep. | 31 Dec. |
| Profit from banking activities/assets in %                | 4.54         | 4.49         | 4.29    | 3.91    | 3.96    | 4.01    |
| Gross profit/assets in %                                  | (0.12)       | (0.23)       | 0.24    | 0.02    | (0.19)  | (0.20)  |
| Net profit/assets in %                                    | (0.17)       | (0.36)       | 0.21    | (0.03)  | (0.25)  | (0.25)  |
| Net profit/core capital in %                              | (3.53)       | (8.26)       | 4.29    | (0.56)  | (5.43)  | (5.27)  |
| Total interest income/interest earning assets in %        | 11.86        | 11.71        | 10.31   | 9.05    | 8.46    | 8.11    |
| Total interest expenses/interest bearing liabilities in % | 8.09         | 8.19         | 7.05    | 6.08    | 5.58    | 5.40    |
| Interest rate spread in %                                 | 3.77         | 3.52         | 3.25    | 2.96    | 2.88    | 2.71    |
| Net interest margin in %                                  | 2.94         | 3.42         | 3.21    | 2.92    | 2.85    | 2.76    |
| Number of employees in banking sector                     | 51 170       | 51 650       | 50 681  | 50 791  | 50 103  | 48 955  |
| Per employee in CZK thousands:                            |              |              |         |         |         |         |
| total assets  | 40 692       | 43 926       | 46 411  | 45 753  | 46 210  | 47 761  |
| profit from banking activities                            | 1 708        | 1 875        | 1 715   | 1 668   | 1 742   | 1 845   |
| net profit  | -66          | -159         | 84      | -11     | -112    | -115    |
| operating expenses  | 831          | 931          | 855     | 924     | 939     | 1 045   |
| personnel expenses  | 238          | 256          | 61      | 132     | 202     | 297     |

## Credits

(for banks with licences as of 31 December 1999, credits granted in the Czech Republic, in CZK millions)

|   | 31 Dec. 1997 | 31 Dec. 1998 | 1999      |           |           |           |
|---|--------------|--------------|-----------|-----------|-----------|-----------|
|   |              |              | 31 Mar.   | 30 Jun.   | 30 Sep.   | 31 Dec.   |
| Total credits                             | 1 063 391    | 1 111 436    | 1 144 456 | 1 144 887 | 1 126 873 | 1 075 220 |
| of which: short-term                      | 440 287      | 451 512      | 462 244   | 471 457   | 445 364   | 414 472   |
| medium-term                               | 245 045      | 250 185      | 254 005   | 248 051   | 251 978   | 236 034   |
| long-term                                 | 378 059      | 409 739      | 428 207   | 425 380   | 429 531   | 424 714   |
| Total credits                             | 1 063 391    | 1 111 436    | 1 144 456 | 1 144 887 | 1 126 873 | 1 075 220 |
| of which: to public sector                | 145 998      | 120 590      | 119 321   | 117 896   | 112 590   | 100 521   |
| to private sector                         | 765 030      | 776 343      | 791 575   | 781 949   | 767 412   | 742 107   |
| to government sector                      | 15 378       | 28 272       | 31 532    | 30 765    | 30 841    | 32 970    |
| to small businesses                       | 54 226       | 43 567       | 42 881    | 42 337    | 40 243    | 34 884    |
| to households                             | 49 687       | 63 266       | 65 396    | 68 028    | 71 482    | 77 550    |
| other                                     | 33 072       | 79 399       | 93 751    | 103 912   | 104 307   | 87 189    |
| of which: agriculture and forestry        | 28 779       | 28 985       | 30 402    | 30 767    | 30 120    | 27 438    |
| manufacturing                             | 330 431      | 317 921      | 324 719   | 318 594   | 305 263   | 288 138   |
| construction                              | 32 038       | 31 538       | 34 172    | 32 283    | 31 500    | 28 266    |
| financial intermediation, incl. insurance | 63 386       | 74 118       | 69 811    | 81 850    | 68 454    | 65 377    |
| transport                                 | 31 961       | 29 567       | 32 117    | 30 598    | 29 941    | 27 983    |
| trade, hotels and restaurants             | 236 674      | 221 413      | 222 762   | 215 413   | 216 408   | 201 074   |
| other                                     | 340 122      | 407 894      | 430 473   | 435 383   | 445 187   | 436 944   |

## Deposits

(for banks with licences as of 31 December 1999, deposits accepted in the Czech Republic, in CZK millions)

|   | 31 Dec. 1997 | 31 Dec. 1998 | 1999      |           |           |           |
|---|--------------|--------------|-----------|-----------|-----------|-----------|
|   |              |              | 31 Mar.   | 30 Jun.   | 30 Sep.   | 31 Dec.   |
| Total deposits                            | 1 076 979    | 1 151 826    | 1 182 261 | 1 200 699 | 1 217 879 | 1 167 351 |
| of which: demand                          | 366 987      | 370 683      | 353 942   | 375 813   | 395 159   | 389 390   |
| time                                      | 709 992      | 781 143      | 828 319   | 824 886   | 822 720   | 777 961   |
| of which: short-term                      | 493 668      | 562 821      | 618 461   | 617 275   | 618 671   | 570 893   |
| medium-term                               | 122 424      | 107 734      | 98 914    | 93 189    | 91 011    | 91 621    |
| long-term                                 | 93 900       | 110 588      | 110 945   | 114 423   | 113 038   | 115 447   |
| Total deposits                            | 1 076 979    | 1 151 826    | 1 182 261 | 1 200 699 | 1 217 879 | 1 167 351 |
| of which: public sector                   | 54 697       | 44 582       | 47 203    | 47 350    | 46 834    | 41 126    |
| private sector                            | 283 634      | 269 550      | 260 113   | 270 857   | 276 393   | 263 703   |
| government sector                         | 30 772       | 37 051       | 43 374    | 48 943    | 60 330    | 41 038    |
| small businesses                          | 39 288       | 36 725       | 41 827    | 43 414    | 46 199    | 37 012    |
| households                                | 636 455      | 738 341      | 760 314   | 761 492   | 761 329   | 761 991   |
| other                                     | 32 133       | 25 577       | 29 430    | 28 643    | 26 794    | 22 480    |
| of which: agriculture and forestry        | 8 312        | 10 056       | 10 396    | 10 406    | 10 395    | 9 747     |
| manufacturing                             | 71 852       | 62 370       | 59 052    | 60 703    | 62 083    | 60 528    |
| construction                              | 20 768       | 22 049       | 17 717    | 17 853    | 19 291    | 19 317    |
| financial intermediation, incl. insurance | 69 187       | 63 997       | 61 880    | 67 729    | 62 219    | 68 296    |
| transport and storage                     | 11 390       | 10 562       | 11 816    | 13 033    | 12 466    | 9 745     |
| trade, hotels and restaurants             | 73 661       | 69 583       | 62 923    | 65 976    | 66 324    | 62 971    |
| other                                     | 821 809      | 913 209      | 958 477   | 964 999   | 985 101   | 936 748   |

## Capital, risk weighted assets and capital adequacy

(for banks with licences as of 31 December 1999, excluding Konsolidační banka)

|  | 31 Dec. 1997 | 31 Dec. 1998 | 1999      |           |           |           |
|--|--------------|--------------|-----------|-----------|-----------|-----------|
|  |              |              | 31 Mar.   | 30 Jun.   | 30 Sep.   | 31 Dec.   |
| Core capital in CZK millions           | 95 127       | 99 693       | 98 876    | 100 951   | 103 319   | 106 385   |
| Total capital in CZK millions          | 105 233      | 127 022      | 127 369   | 127 401   | 129 594   | 133 796   |
| Total assets in CZK millions           | 2 055 102    | 2 170 325    | 2 228 501 | 2 194 895 | 2 173 797 | 2 186 579 |
| of which by risk weight:               |              |              |           |           |           |           |
| 0%                                     | 515 304      | 695 128      | 736 746   | 713 507   | 677 483   | 765 593   |
| 20%                                    | 512 026      | 500 767      | 502 836   | 506 664   | 541 689   | 523 402   |
| 50%                                    | 37 116       | 42 656       | 42 676    | 38 884    | 40 692    | 42 336    |
| 100%                                   | 990 656      | 931 775      | 946 244   | 935 841   | 913 933   | 855 249   |
| Risk-weighted assets in CZK millions   | 1 111 619    | 1 053 256    | 1 068 149 | 1 056 615 | 1 042 617 | 981 097   |
| Risk-weighted assets/total assets in % | 54.09        | 48.53        | 47.93     | 48.14     | 47.96     | 44.87     |
| Core capital/risk-weighted assets in % | 8.56         | 9.47         | 9.26      | 9.55      | 9.91      | 10.84     |
| Capital/risk-weighted assets in %      | 9.47         | 12.06        | 11.92     | 12.06     | 12.43     | 13.64     |

## Reserve resources

(for banks with licences as of 31 December 1999, in CZK millions)

|                         | 31 Dec. 1997 | 31 Dec. 1998 | 1999    |         |         |         |
|-------------------------|--------------|--------------|---------|---------|---------|---------|
|                         |              |              | 31 Mar. | 30 Jun. | 30 Sep. | 31 Dec. |
| Provisions              | 98 573       | 118 814      | 123 587 | 130 812 | 149 161 | 142 137 |
| Reserves                | 40 014       | 41 275       | 39 316  | 36 255  | 46 675  | 45 317  |
| Reserve funds           | 72 328       | 73 938       | 75 065  | 66 935  | 67 232  | 67 111  |
| Capital funds           | 19 369       | 33 967       | 34 478  | 12 893  | 12 723  | 12 958  |
| Total reserve resources | 230 284      | 267 995      | 272 447 | 246 895 | 275 791 | 267 524 |

## Quick assets

(for banks with licences as of 31 December 1999, in CZK millions)

|                                   | 31 Dec. 1997 | 31 Dec. 1998 | 1999    |         |         |         |
|-----------------------------------|--------------|--------------|---------|---------|---------|---------|
|                                   |              |              | 31 Mar. | 30 Jun. | 30 Sep. | 31 Dec. |
| Cash                              | 26 685       | 27 016       | 27 280  | 27 920  | 27 145  | 36 903  |
| Deposits and credits with the CNB | 190 733      | 269 934      | 284 850 | 276 647 | 268 574 | 274 204 |
| of which: required reserves       | 86 279       | 86 827       | 62 204  | 51 645  | 68 189  | 28 019  |
| Current accounts with banks       | 14 189       | 11 193       | 10 514  | 9 132   | 8 487   | 22 084  |
| T-bills                           | 38 613       | 53 394       | 39 195  | 56 192  | 48 474  | 80 532  |
| CNB bills                         | 91 957       | 161 710      | 201 002 | 200 536 | 186 168 | 201 900 |
| Total quick assets                | 362 178      | 523 247      | 562 840 | 570 427 | 538 849 | 615 621 |
| Trading securities                | 97 509       | 96 362       | 88 696  | 88 333  | 83 827  | 75 739  |
| of which: bonds                   | 84 231       | 86 521       | 78 714  | 77 733  | 75 718  | 68 378  |
| equity securities                 | 9 621        | 4 184        | 5 164   | 6 449   | 4 289   | 2 927   |
| Total liquid assets               | 459 686      | 619 608      | 651 536 | 658 760 | 622 676 | 691 361 |
| Share in total assets in %        |              |              |         |         |         |         |
| quick assets                      | 16.30        | 21.58        | 22.39   | 23.01   | 21.70   | 24.30   |
| liquid assets                     | 20.69        | 25.56        | 25.92   | 26.57   | 25.08   | 27.28   |

## Assets and liabilities by residual maturity as of 31 December 1998

(for banks with licences as of 31 December 1999, in CZK millions)

|  | Total     | of which     |                   |               |               |                    |              |              |                   |               |
|--|-----------|--------------|-------------------|---------------|---------------|--------------------|--------------|--------------|-------------------|---------------|
|  |           | under 1 week | 1 week to 1 month | 1 to 3 months | 3 to 6 months | 6 months to 1 year | 1 to 2 years | 2 to 5 years | more than 5 years | non-specified |
| Total assets   | 2 424 232 | 399 003      | 263 171           | 243 531       | 187 154       | 217 082            | 165 129      | 198 144      | 143 160           | 607 857       |
| Total liabilities  | 2 424 232 | 780 259      | 329 457           | 201 237       | 145 618       | 162 071            | 132 961      | 188 962      | 107 097           | 376 570       |
| Net balance sheet position                               | x         | (381 255)    | (66 285)          | 42 294        | 41 536        | 55 010             | 32 168       | 9 182        | 36 063            | 231 287       |
| Cumulative net balance sheet position                    | x         | (381 255)    | (447 541)         | (405 247)     | (363 711)     | (308 701)          | (276 533)    | (267 350)    | (231 287)         | 0             |
| in % of total assets                                     | x         | (15.73)      | (18.46)           | (16.72)       | (15.00)       | (12.73)            | (11.41)      | (11.03)      | (9.54)            | 0.00          |
| Liabilities taking into account demand deposit liquidity | 2 424 232 | 376 863      | 369 796           | 241 577       | 226 297       | 222 581            | 193 471      | 249 471      | 167 606           | 376 570       |
| Net balance sheet position                               | x         | 22 140       | (106 625)         | 1 955         | (39 144)      | (5 499)            | (28 341)     | (51 327)     | (24 446)          | 231 287       |
| Cumulative net balance sheet position                    | x         | 22 140       | (84 485)          | (82 530)      | (121 673)     | (127 173)          | (155 514)    | (206 841)    | (231 287)         | 0             |
| in % of total assets                                     | x         | 0.91         | (3.49)            | (3.40)        | (5.02)        | (5.25)             | (6.41)       | (8.53)       | (9.54)            | 0.00          |

## Assets and liabilities by residual maturity as of 31 December 1999

(for banks with licences as of 31 December 1999, in CZK millions)

|  | Total     | of which     |                   |               |               |                    |              |              |                   |               |
|--|-----------|--------------|-------------------|---------------|---------------|--------------------|--------------|--------------|-------------------|---------------|
|  |           | under 1 week | 1 week to 1 month | 1 to 3 months | 3 to 6 months | 6 months to 1 year | 1 to 2 years | 2 to 5 years | more than 5 years | non-specified |
| Total assets   | 2 533 888 | 392 863      | 353 872           | 283 784       | 206 115       | 237 026            | 113 457      | 223 345      | 148 560           | 574 866       |
| Total liabilities  | 2 533 888 | 853 129      | 383 365           | 241 816       | 145 804       | 133 597            | 147 964      | 204 947      | 93 127            | 330 140       |
| Net balance sheet position                               | x         | (460 266)    | (29 492)          | 41 968        | 60 311        | 103 428            | (34 506)     | 18 397       | 55 433            | 244 727       |
| Cumulative net balance sheet position                    | x         | (460 266)    | (489 759)         | (447 790)     | (387 479)     | (284 050)          | (318 557)    | (300 159)    | (244 727)         | (0)           |
| in % of total assets                                     | x         | (18.16)      | (19.33)           | (17.67)       | (15.29)       | (11.21)            | (12.57)      | (11.85)      | (9.66)            | (0.00)        |
| Liabilities taking into account demand deposit liquidity | 2 533 888 | 429 503      | 425 727           | 284 179       | 230 529       | 197 141            | 211 507      | 268 491      | 156 671           | 330 140       |
| Net balance sheet position                               | x         | (36 641)     | (71 855)          | (394)         | (24 414)      | 39 885             | (98 050)     | (45 147)     | (8 111)           | 244 727       |
| Cumulative net balance sheet position                    | x         | (36 641)     | (108 496)         | (108 890)     | (133 304)     | (93 419)           | (191 469)    | (236 616)    | (244 727)         | (0)           |
| in % of total assets                                     | x         | (1.45)       | (4.28)            | (4.30)        | (5.26)        | (3.69)             | (7.56)       | (9.34)       | (9.66)            | (0.00)        |

## Classified credits

(for banks with licences as of 31 December 1999, excluding Konsolidační banka)

|   | 31 Dec. 1997 | 31 Dec. 1998 | 1999    |         |         |         |
|---|--------------|--------------|---------|---------|---------|---------|
|   |              |              | 31 Mar. | 30 Jun. | 30 Sep. | 31 Dec. |
| Classified credits in CZK millions  | 266 390      | 261 641      | 291 475 | 309 898 | 308 371 | 291 061 |
| in % of total credit volume   | 26.95        | 26.67        | 28.89   | 30.58   | 31.45   | 32.15   |
| of which: watch credits   | 60 595       | 59 093       | 77 590  | 86 480  | 82 675  | 92 124  |
| substandard credits   | 26 811       | 33 684       | 36 127  | 38 127  | 40 221  | 39 379  |
| doubtful credits  | 29 386       | 35 862       | 38 011  | 38 911  | 39 687  | 38 433  |
| loss credits  | 149 597      | 133 002      | 139 748 | 146 380 | 145 787 | 121 125 |
| Classified credits taking into account collateral, in CZK millions                  | 142 654      | 146 036      | 168 728 | 182 794 | 181 745 | 170 180 |
| in % of total credit volume   | 14.43        | 14.89        | 16.72   | 18.04   | 18.54   | 18.80   |
| Weighted classification in CZK millions   | 172 682      | 160 625      | 169 858 | 177 785 | 177 809 | 152 823 |
| in % of total credit volume   | 17.47        | 16.37        | 16.83   | 17.55   | 18.14   | 16.88   |
| Weighted classification taking into account collateral, in CZK millions             | 94 257       | 90 570       | 100 992 | 108 575 | 109 852 | 98 817  |
| in % of total credit volume   | 9.54         | 9.23         | 10.01   | 10.71   | 11.20   | 10.91   |
| Reserves and provisions in CZK millions   | 105 287      | 110 126      | 112 727 | 116 490 | 129 847 | 103 774 |
| Surplus (+) or shortfall (-) of reserves, provisions and collateral in CZK millions | 11 031       | 19 557       | 11 735  | 7 915   | 19 995  | 4 957   |
| in % of total credit volume   | 1.12         | 1.99         | 1.16    | 0.78    | 2.04    | 0.55    |



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