REPORT ON FINANCIAL MARKET DEVELOPMENTS IN 2008

May 2009

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SUMMARY

Economy

The Czech economy found itself in a declining phase of the economic cycle during 2008, and in the fourth quarter it entered into recession. GDP grew by 3.2% for the entire year. The slowing growth of real GDP was affected at the end of the year by the weakening of global demand.

Entities in the financial market

The numbers of entities in critical sectors of the financial market did not change more markedly year on year. The process of gradual market concentration through acquisitions and mergers has continued. On the insurance market, the first universal reinsurance company obtained a trade licence.

Banking sector

The volumes of accepted deposits and of loans grew to new record values. The Czech banking sector was not immediately affected by the global financial crisis. The Czech banking sector particularly benefited from its more rigorous assessment of loan applicants' creditworthiness, absence of securitisation processes, minimal investment into problematic assets, and the significant role of client deposits for bank financing. The ratio of client deposits to loans is among the highest within the entire EU.

Interest rates

In 2008's second half, CNB immediately proceeded to reduce the 2T repo rate three times. Nevertheless, interest rates for consumer loans and residential financing increased slightly. In the second half of the year, an increasing risk premium thus became more apparent as entities in the financial market adjusted their approach to risk.

Deposits and loans

The total volumes of deposits and loans increased. The household sector also recorded the highest absolute year-on-year growth in the volume of deposits (by CZK 142.8 bn) during this period.

Household indebtedness

Total household indebtedness to banks and non-banking financial institutions rose by 16% and exceeded CZK 1 trillion as at the end of the year. It can be regarded as a relatively healthy sign that households continue to take out loans primarily to answer housing needs.

Building societies

The total number of contracts in the savings phase at the end of 2008 fell year on year to nearly 5.1 mn. This represents a continuing trend, as the vast majority of so-called old contracts with state support in the amount of CZK 4,500 have been terminated. The change in the structure of buildings savings contracts was positively projected in the amount of state support disbursed.

Mortgage loans

The volume of mortgage loans provided to the population as at the end of the year reached nearly CZK 400 bn. Growth dynamics significantly decreased during 2008 with regard to the volume of mortgage loans. Despite the decrease of CNB rates, mortgage loan rates did not drop. This reflects the fact that banks have become more strict in assessing the risks in the mortgages provided.

Credit unions

As at the end of 2008, the total assets in this sector had grown by a third and exceeded CZK 12 bn. The main factor was the increase in deposits.

Regulated markets

The PSE's main index recorded the steepest drop in its 15-year history during 2008. Compared to the end of 2007, it lost 52.7%. In 2008, the company Wiener Börse became the exchange's majority owner.

Collective investments

In 2008, for the first time, invested funds declined year on year by almost 23%. The volume of assets in foreign funds surpassed the volume of assets in domestic funds.

Insurance companies

The insurance market registered relatively positive results, despite a reduction in year-on-year dynamics. The gross premiums written indicator rose especially thanks to non-life insurance.

Supplementary pension insurance

Even in the past year the number of supplementary pension insurees continued to increase, rising to nearly 4.21 mn participants. Employers currently comprise 21.8% of that number. In total, participants' funds under the management of pension funds reached CZK 186.7 bn.

Government sector

The state budget ended 2008 with a deficit of CZK 20 bn. Revenues surpassed expectations especially due to a rise in so-called non-tax and other revenues. As at the end of 2008, non-consolidated state debt was recorded in the amount of CZK 999.8 bn.

Foreign exchange market

In 2008's first half, the Czech currency became one of the fastest strengthening currencies in the world. This was primarily due to the relatively lower impact of the financial crisis on the Czech economy. In August, however, the Czech crown began to weaken rapidly.

Financial crisis

The financial crisis became the main topic worldwide during the first half of the year. Among those most significantly affected was the investment banking sector, which ceased to exist in its traditional form.

Considering the extent of the crisis and its results, a series of measures was adopted that included nationalisation of affected institutions, extensive guarantees and provision of funding. Czech financial institutions have not been directly affected by the crisis, and confidence in the banking sector in the Czech Republic is high.

The Czech Republic has a small, export-oriented economy. For the Czech Republic, therefore, it is not the world financial crisis but the economic crisis that is relevant. The effects of this crisis spill over into the Czech Republic from abroad due to the drop in demand for Czech goods from the economies of its trading partners.

In connection with the development of economies in the region of Central and Eastern Europe (hereinafter referred to as "CEE"), the Czech Republic has been misleadingly included into a vaguely defined group of countries within this region. Thus, a mistaken impression could arise that the Czech economy is undergoing similar problems as are certain other countries in the CEE region.

Czech Presidency of the Council of the EU

In the first half of 2009, the Czech Republic occupied the Presidency of the Council of the European Union. The role of the Ministry of Finance in the area of financial services consisted on the one hand in ensuring an adequate response to the current financial crisis, and on the other in efforts to move ahead in the process of adopting a range of legislative proposals. The MoF's active approach in the legislative sphere was rounded out by a series of achievements, among which the most significant include a revision of capital requirements directives (CRD), a regulation on credit rating agencies (CRA), and the Solvency II directive, which governs the insurance sector.

Consumer protection in the financial market

The harmonisation of distribution and requirements as to the expertise of distributors became the central theme. In the autumn of 2008, a public consultation was held on revising the existing system of out-of-court resolution of consumer disputes on the financial market. The main outcome was a recommendation to expand the authority of the financial arbiter to other sectors of the financial market and to modify the method of its financing.

1. MACROECONOMIC SITUATION

The Czech economy found itself in a declining phase of the economic cycle during 2008, and in the fourth quarter it entered into recession. The slowing growth of real gross domestic product (GDP) was affected at the end of the year by the weakening of global demand and of demand from the country's largest trading partners. Annual real GDP growth continued to be supported by high contributions from household consumption and foreign trade, even though foreign trade's contribution to GDP in the fourth quarter was a negative 1.8 percentage points. The drop in real gross capital formation, due especially to a slowdown in the increase of inventories and valuables, had the opposite effect.

Table 1.1: GDP growth rates[1]

(annual, %)	2003	2004	2005	2006	2007	2008
Czech Republic	3.6	4.5	6.3	6.8	6.0	3.2
EU-27	1.3	2.5	2.0	3.1	2.9	0.9
Eurozone	0.8	1.9	1.8	3.0	2.6	0.8
Japan	1.4	2.7	1.9	2.0	2.4	-0.6
USA	2.5	3.6	2.9	2.8	2.0	1.1

Source: Eurostat

The average inflation rate (measured by the CPI increase) reached a significantly higher level in 2008 than in previous years. The swift upswing in world energy and food prices (especially in the first half of 2008), rise in administrative (regulated) prices, and increase in the reduced VAT rate from 5% to 9% in particular were behind the rising inflation rate.

Table 1.2: Macroeconomic indicators of the Czech economy

	2005	2006	2007	2008
GDP growth (%, constant prices)	6.3	6.8	6.0	3.2
Household consumption (change, %, constant prices)	2.5	5.4	5.3	2.8
Government consumption (change, %, constant prices)	2.9	-0.7	0.4	0.9
Gross fixed capital formation (change, %, constant prices)	1.8	6.5	6.7	3.1
Inflation (CPI, average for period, %)	1.9	2.5	2.8	6.3
Unemployment rate (MLSA, average for period, %)	7.9	7.1	5.3	4.4
Current account balance for GDP (%, current prices)	-1.3	-2.6	-3.2	-3.1
Balance of trade for GDP (%, current prices)	2.0	2.0	3.4	2.8

Source: CZSO

The unemployment rate fell in 2008's first half but subsequently began to rise due to slowing exports and economic activity. Compared to the previous year, unemployment registered lower levels primarily thanks to a greater offering of jobs and worker retirements. In the second half of the year, the impacts of the global crisis already began to appear. Total employment (as defined domestically) also responded accordingly to GDP development. Although still continuing to grow, it was doing so as at the end of the year at a slower rate.

The external economic balance (measured by the current account balance as a ratio of GDP) did not change much in 2008 compared to 2007. Its slight improvement can be attributed to a better result in the services balance and balance of current transfers. The positive balance of trade decreased especially owing to the development in the fourth quarter.

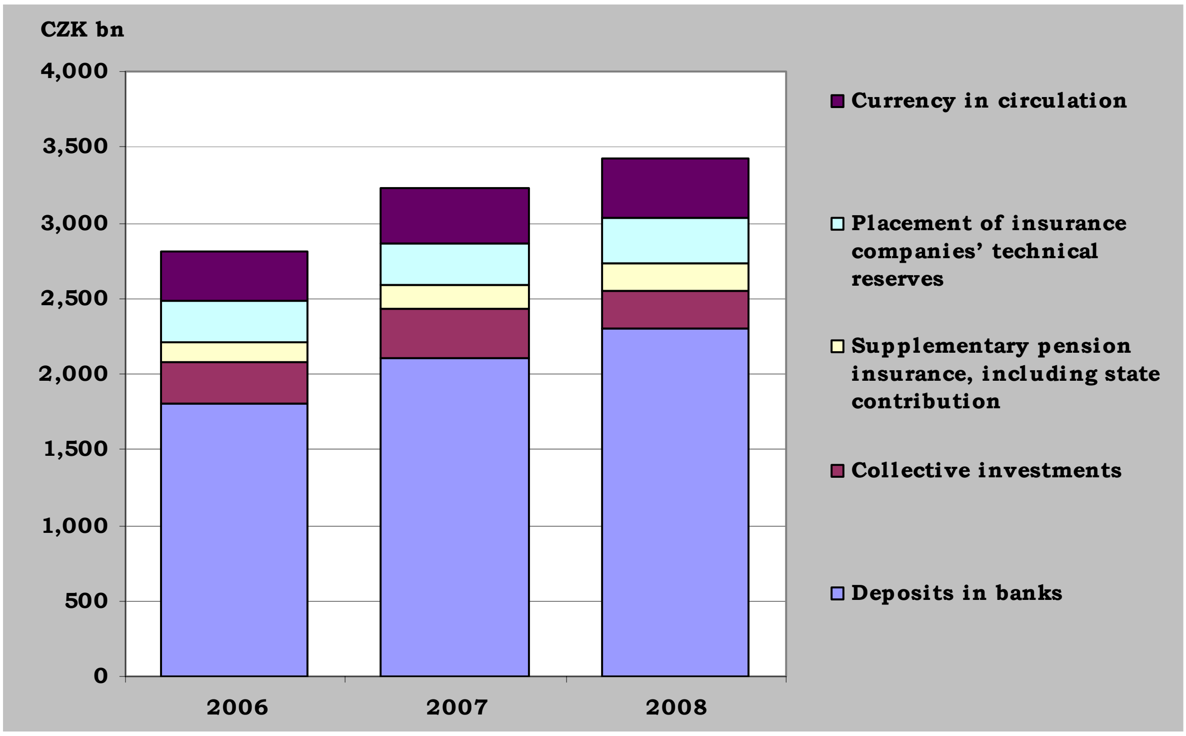
[1] Data published as at 7 March 2009.

2. FUNDS FOR USE IN THE FINANCIAL MARKET

Although the Czech economy showed signs of slowing in the second half of the year, all categories monitored that comprise funds for use in the financial market grew in 2008 with the exception of collective investments. The following graph displays a summary of the funds that financial institutions could theoretically use for financial market operations. From the data for 2008, it can be seen that the volume of these funds reached CZK 3,428 bn,[2] which represents an increase of 6.4% year on year. The year-on-year growth thus slowed by 8.5 percentage points.

The most important item, deposits in banks, recorded the largest absolute increase by more than CZK 191 bn year on year. In comparison with 2007, however, this represents an appreciable slowdown in the dynamics of year-on-year relative growth from 16.7% to 9.1%. On the other hand, the growth dynamics for the volume of currency in circulation increased from 10% to 12.9%, which represented a rise of CZK 45.5 bn in 2008.

Graph 2.1: Funds for use in the financial market



Source: MoF, CNB, AKAT

The category "supplementary pension insurance, including state contribution" achieved the highest growth rate (by 14.9%, or CZK 24.3 bn). The volume of funds within the item "placement of insurance companies' technical reserves" rose at a rate of 5.5% year on year. On the other hand, the development on financial markets, subsequent nervousness of clients and retraction of investments contributed to the decrease in funds within collective investments. This category diminished by CZK 71.4 bn, or 22.6%, year on year.[3]

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[2] Funds available in the financial market for the purposes hereof are calculated as the sum of money in bank deposits, collective investment funds, supplementary pension insurance, placement of technical reserves of insurance companies and currency in circulation available for use in the financial market. Therefore, they comprise a particular segment of the total balance of financial sources formation and use.

[3] See Chapter 4.3.4. Collective investments.

Table 2.1: Funds for use in the financial market[4]

As at 31 Dec (CZK bn)	2007	2008	Year-on-year change	
			Abs.	**(%)**
Deposits in banks[5]	2,109.8	2,301.0	191.2	9.06
of which: building savings schemes	384.8	401.3	16.5	4.29
Collective investments	315.2	243.9	-71.3	-22.63
Supplementary pension insurance, including state contribution	162.5	186.7	24.3	14.93
Placement of insurance companies' technical reserves	281.8	297.4	15.6	5.52
Currency in circulation	353.7	399.2	45.5	12.86
Total	3,223.0	3,428.1	205.2	6.37

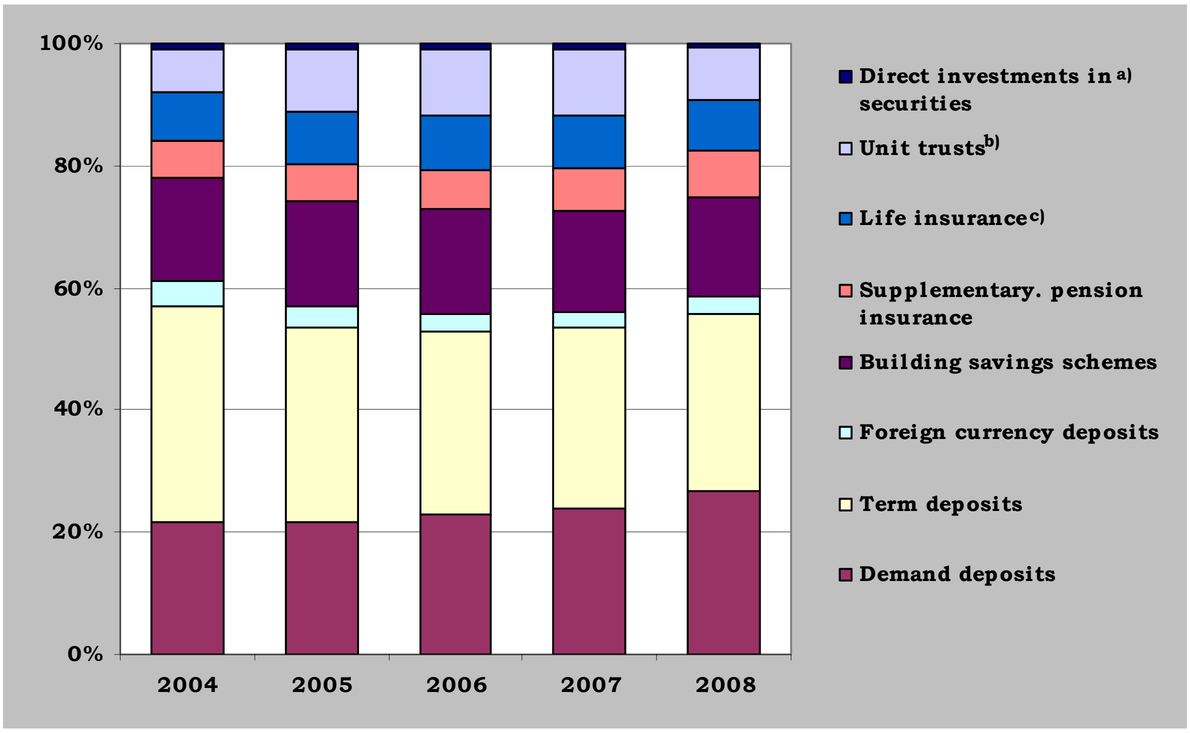
Source: MoF, CNB – ARAD, CNB, AKAT

[4] Data published as at 30 April 2008.
[5] Including CZK deposits of clients according to sector.

3. STRUCTURE OF HOUSEHOLD SAVINGS

Total household savings[6] increased by 7.4% year on year and came to just under CZK 2.5 trillion as at the end of 2008. Demand deposits achieved the highest year-on-year increase (almost 19%). In addition, life insurance and foreign currency deposits rose at double-digit rates. Sharp drops in the values of securities on capital markets due to the financial crisis were reflected in the year-on-year decline in funds invested into unit trusts.

Graph 3.1: Development of the structure of private savings in the Czech Republic[7]



Source: CNB, MoF

The structure of household savings scarcely changed in 2008. Households entrusted over 70% (CZK 1.8 trillion) of their savings to banks and building societies. Czech households thus continue to be very conservative. The financial crisis, which led Czech households to transfer a portion of their savings from high-risk products to insured bank deposits, also certainly had its own impact on the distribution of households' savings.

[6] Total household savings for the purposes hereof is calculated as the sum of bank term and demand deposits, foreign currency deposits, building savings schemes, supplementary pension insurance, life insurance, unit trusts, and direct investments in securities. Therefore, it is comprised of funds that are used by households to invest or save.

[7] Notes to Graph 3.1:

a) Qualified estimate by MoF.
b) Value of assets in open-ended unit trusts and investment funds is for individuals in the estimated amount of 85% of those funds' total assets.
c) According to the value of insurance companies' technical reserves.

4. FINANCIAL MARKET ENTITIES

The numbers of entities in critical sectors of the financial market did not change more markedly year on year. The process of gradual market concentration through acquisitions and mergers has continued, especially in the banking sector, among pension funds, and in the insurance business. Generally, the numbers of entities in the capital market slightly increased, primarily in the area of collective investments. The drop in the number of investment intermediaries results from new legislation that transposes MiFID and newly introduces the institution of a tied agent. On the insurance market, the first universal reinsurance company obtained a trade licence. Growth in the number of insurance intermediaries also continued in 2008.

In the banking sector, the trend from the past several years of rather marked growth in branches of foreign banks while maintaining the total number of entities was confirmed. This trend stems from, among other things, the efforts of some banks' foreign subsidiaries to take the form of branches in order to reduce administrative demands with respect to external requirements.

Table 4.1: Numbers of selected entities providing services in the financial market[8]

As at 31 Dec	2004	2005	2006	2007	2008
Banks	35	36	37	37	37
of which: foreign banks' branches	9	12	13	14	16,
of which: building societies	6	6	6	6	5
Credit unions	33	20	20	19	17
Investment firms	58	51	46	44	38
Investment funds	2	0	0	7	16 [9]
Investment companies	9	9	13	18,	19
Open-ended unit trusts	62	65	77	121	142
of which: special OEUT	0	41	41	51	101
standard OEUT	0	24	24	26	41
Foreign funds/sub-funds	911	1,038	1,282	1,499	1,596
of which: based on common European licence	0	1,025	1,271	1,479	1,569
of which: special funds	0	13	11	20	27
Investment intermediaries (000's)	5.70	8.40	10.60	13.37	12.87
Pension funds	11	11	11	11	10
Insurance companies	40	45	49	52	53
of which: branches of foreign insurance companies	7	12	16	18	17
Reinsurance companies	0	0	0	0	1
Insurance intermediaries (000's)[10]	43.60	35.30	50.10	67.50	86.23

Source: CNB

Entities operating in the Czech Republic on the basis of the so-called single European passport also have increased the competition on the financial market. Their impact on strengthening competition is limited, as the majority of these entities seem to develop their operations only minimally or are narrowly specialised. Instead, they complement the main

[8] Only active entities (not in liquidation) are included.
[9] Of this number, two investment funds were not yet entered into the Commercial Register as at 31 December 2008.
[10] Qualified estimate until 2004.

market players and potentially can gain importance should an unsatisfied gap in the existing offering of financial services become apparent.

Table 4.2: Number of entities operating in the Czech Republic under the single European passport

As at 31 Dec	Banks	Insurance companies	Funds	Investment companies	Non-banking providers of investment services
2007	198	478	1,479	37	518
2008	252	554	1,569	40	840

Source: CNB

The consequences of the turbulence on foreign financial markets are partly reflected in the economic results of financial institutions. Although employment continued to increase in all sectors, profit generation markedly declined. The sector comprised of leasing companies, pension funds and insurance companies strengthened in terms of capital.

Table 4.3: Economic results of financial institutions (year-on-year comparison)

		Banking financial institutions	**Non-banking financial institutions[11]**	**Insurance companies**	**Pension funds**	**Financial leasing companies**	**Investment companies[12]**
Average headcount[13]	**as at 31 Dec 2006**	36,644	12,000	14,214	450	2,738	207
	as at 31 Dec 2007	37,817	13,353	14,449	466	2,907	272
	change (%)	3.20	11.28	1.65	3.56	6.17	31.40
Profit/loss before tax (CZK bn)	**as at 31 Dec 2006**	59.3	24.7	16.2	4.3	4.8	3.1
	as at 31 Dec 2007	54.1	5.4	13.0	0.7	2.4	-18.5
	change (%)	-8.69	-78.27	-19.58	-83.88	-49.37	-694.23

Source: CZSO

4.1. Business sector

Non-financial undertakings with 250 or more employees slightly increased their indebtedness despite declining demand in the economy. The share of bonds in the total indebtedness of non-financial undertakings again decreased – from 16.8% in 2007 to 16.2% last year. Non-financial undertakings continue to use primarily bank loans for financing their activities and development.

Table 4.4: Financial resources of companies with no less than 250 employees[14]

As at 31 Dec (CZK bn)		2006	2007	2008
Money and bank accounts		199.5	207.9	189.6
Credits and loans (received)	**short-term**	150.4	193.4	212.3
	long-term	207.7	213.1	229.1
	total	358.2	406.4	441.4
Bonds incl. bills of exchange (liabilities)	**short-term**	10.2	12.8	7.8

[11] Institutions in categories 652 and 67 under the OKEČ methodology.
[12] Investment companies and the unit trusts and investment funds managed by those companies.
[13] Average headcount (full-time equivalent) of individual employees for the year ending on the stated date.
[14] The stated data include all credits, loans, bonds and bills of exchange (not only those newly acquired or issued).

	long-term	67.0	69.1	77.3
	total	77.2	81.9	85.1

Source: CZSO

Again in 2008, the number of non-financial enterprises with 250 or more employees increased. As the following table shows, companies managed last year to increase revenues per employee, but at the same time efficiency decreased. Expenditure items, particularly labour costs, grew faster than revenues. Thus, pressure has increased for stricter control over expenditures.

Table 4.5: Financial indicators of companies with no less than 250 employees

As at 31 Dec	2007	2008	Change	
			Abs.	**(%)**
Number of active entities	1,653	1,702	49	2.96
Number of employees (average, individuals)	1,213,654	1,232,434	18,780	1.55
Total assets (CZK bn)	3,701.5	3,966.1	264.6	7.15
Equity (CZK bn)	1,984.6	2,106.0	121.5	6.12
Total inventories	348.8	365.9	17.1	4.91
Total revenues	4,226.6	4,420.7	194.1	4.59
Revenues from sale of goods	954.9	1,013.4	58.5	6.13
Revenues from sale of own products	2,467.8	2,524.4	56.6	2.29
Revenues from sale of services	803.8	882.9	79.1	9.83
Wages	333.0	370.1	37.2	11.16
Cost of goods sold	805.1	860.6	55.5	6.90
Cost of sales	2,529.5	2,659.3	129.8	5.13
Accounting value added	945.8	958.6	12.8	1.36

Source: CZSO

4.2. Banking sector

The net income before tax in the banking sector for 2008 exceeded CZK 54 bn.[15] Compared to the record year 2007, this represents an 8.7% decline. While annual profits grew for the majority of institutions, ČSOB, whose profit fell by nearly 90% year on year and was just over CZK 1 bn, reported just the opposite. One reason for this was a one-time dramatic revaluation of investments into collateralised debt obligations (CDOs) and of investments connected with problematic Icelandic banks and the Lehman Brothers investment bank in the amount of approximately CZK 10 bn. After adjusting for this operation, the profit of the Czech banking sector would once again increase year on year.

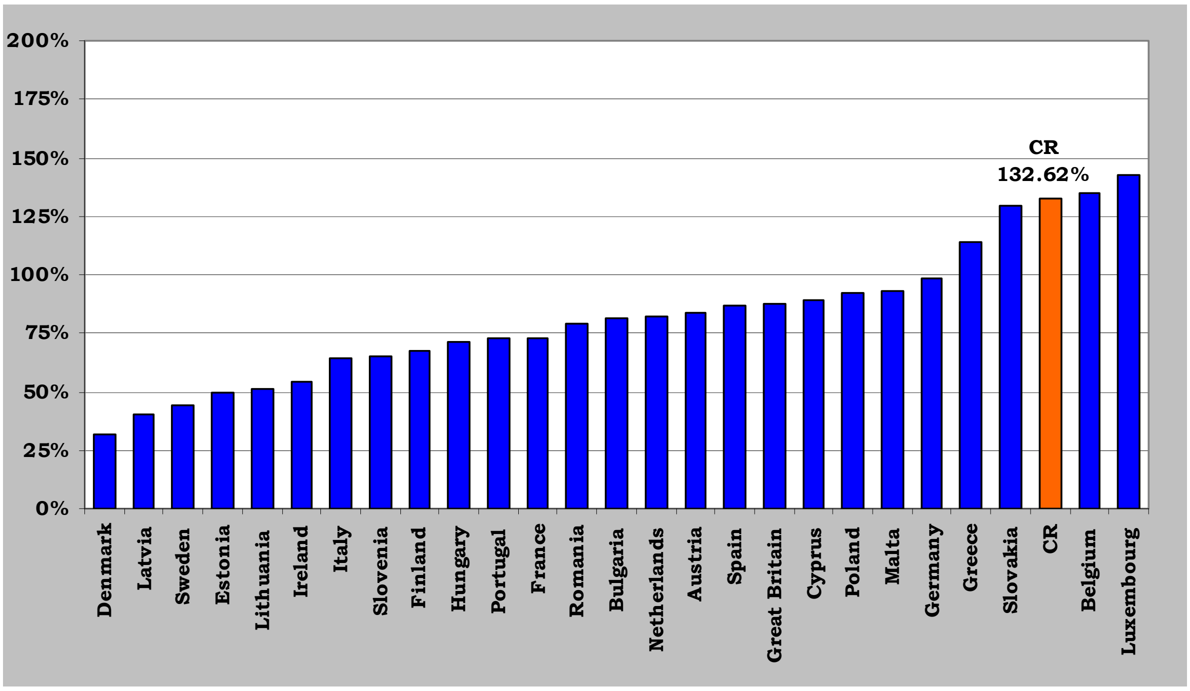
The volumes of deposits taken and of loans made rose to new record levels. This confirms that the Czech banking sector was not immediately affected by the global financial crisis that began with problems on the market for American mortgage-backed assets.[16] Banking institutions on the Czech market, the overwhelming majority of which are subsidiaries of foreign banks, earn profits for their owners primarily through local retail operations. Thus, they did not own derivatives or other assets tied to problematic mortgages to a similar extent as did certain foreign banks. In contrast to American banks, Czech banks also investigated and evaluated loan applicants' creditworthiness far more thoroughly. At the

[15] Data from CZSO.
[16] See Chapter 7. Financial and Economic Crisis.

same time, the Czech banking system is void of such processes for securitising assets that enabled banks in the USA to hold potentially problematic loans off their balance sheets.

For the future, however, it should be expected that in connection with the slowing of the Czech economy the value of the loan portfolio will need to be adjusted according to how the decrease in foreign demand and employment affects the ability of non-financial undertakings and households to settle their obligations. Only shareholders should eventually feel these impacts in the form of a drop in profitability, however, and not depositors.

Graph 4.1: Client deposits to loans ratio at the end of 2008



Source: ECB

4.2.1. Interest rates development

In the first half of 2008, the strengthening of the Czech crown[17] combined with its consequences for export and economic performance did not provide CNB very much room for responding to inflation pressures by raising interest rates. CNB also was not obliged to react to the inflation growth, as the sources of price growth were rather temporary and partially administrative in nature. Following an increase on 8 February 2008 by 0.25 percentage points, CNB kept the 2T repo rate at 3.75% for the majority of the year's first half. Later easing of inflationary pressures in connection with slowing economic growth allowed CNB to reduce its rates further. In the second half of the year, the 2T repo rate was quickly reduced three times, from 3.75% to 2.25%.[18] The pace of reduction was less dramatic than in the cases of the ECB,[19] Bank of England or US Federal Reserve.

[17] See Chapter 6. Foreign Exchange Market.
[18] In February and May 2009, CNB proceeded with two further reductions to 1.50%.
[19] With effect from May 2009, ECB reduced its base rate to 1%.

Table 4.6: CNB interest rates

(%)	30 Jun 2006	31 Dec 2006	30 Jun 2007	31 Dec 2007	30 Jun 2008	31 Dec 2008
2T Repo	2.00	2.50	2.75	3.50	3.75	3.25
Discount	1.00	1.50	1.75	2.50	2.75	1.25
Lombard	3.00	3.50	3.75	4.50	4.75	3.75

Source: CNB

After declining in recent years, the APR[20] for consumer lending rose above 14%, which represents an appreciable increase compared to 12.1% in April 2007.

Table 4.7: APR of CZK loans provided by banks in the CR

New loans (%)	I-08	II-08	III-08	IV-08	V-08	VI-08	VII-08	VIII-08	IX-08	X-08	XI-08	XII-08
Consumer credit	13.9	13.6	14.0	14.0	14.0	13.8	14.2	14.3	14.3	14.5	14.6	14.2
For residential real estate	5.6	5.6	5.6	5.7	5.7	5.7	5.8	5.9	5.8	5.8	5.8	5.9

Source: CNB

APR on the purchase of residential real estate continued to increase and reached 5.9%. In 2008, however, it increased by only 0.29 percentage points. Compared to the previous year, when it rose by 0.7 percentage points, this shows a clear slowing of growth dynamics.

Several factors influenced the rise in interest rates for consumer and housing finance loans. In the first half of the year, the CNB's earlier rate increase had the greatest effect. In the second half, on the other hand, when CNB had reduced its rates, an increase in the risk premium was seen as entities in the financial markets changed their approach to risk.

4.2.2. Deposits and loans

The total deposits volume grew during 2008 by 9.1%. The growth dynamics in the volume of loans was even higher, and their volume expanded in the same period by 14.8%.

Most sectors recorded volume growth in the lending area. In absolute terms, the households sector recorded the greatest increase (by CZK 143.6 bn), while the "other" sector had the fastest growth in relative terms (by 24.7%). An exception was the government sector, which fell in absolute terms by CZK 3.3 bn and relatively by 6.4%.

[20] APR denotes the percent share of the amount owed that the client must pay within a period of one year in connection with instalments, administration fees and other costs connected with drawing a loan. This refers to the APR for loans denominated in Czech crowns and provided by banks in the Czech Republic (new transactions).

Table 4.8: Breakdown of CZK deposits and loans with banks by sectors

As at 31 Dec / Sector[21]	Bank deposits (CZK bn)				Loan beneficiaries (CZK bn)			
	2007	**2008**	**Change**	**Change (%)**	**2007**	**2008**	**Change**	**Change (%)**
Non-financial companies	485.9	465.9	-20.1	-4.13	616.6	692.2	75.6	12.25
Households	1,231.1	1,373.8	142.8	11.60	707.0	850.7	143.6	20.32
Government institutions	207.8	287.0	79.2	38.12	51.4	48.1	-3.3	-6.40
Financial institutions	110.3	97.0	-13.3	-12.05	128.5	130.4	1.9	1.46
Other[22]	74.7	77.3	2.6	3.47	50.2	62.5	12.4	24.69
Total	2,109.8	2,301.0	191.2	9.06	1,553.7	1,783.9	230.2	14.81

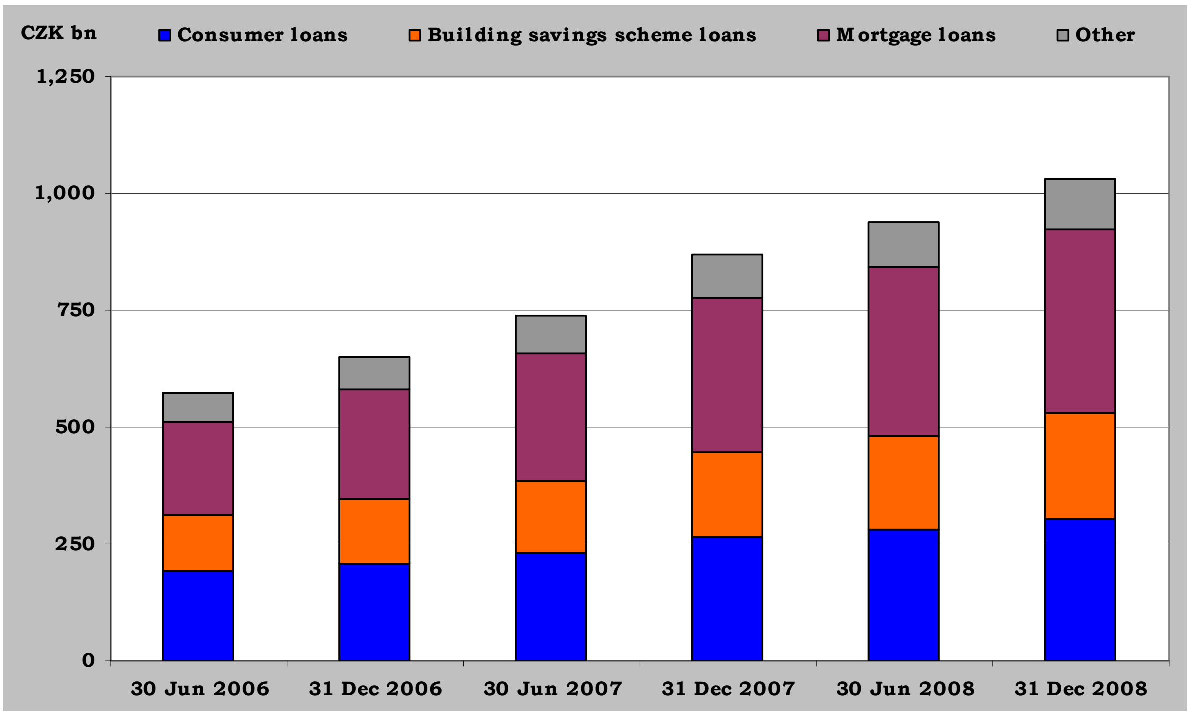
Source: CNB - ARAD

In this period, the household sector recorded the highest absolute increase year on year in the volume of deposits (by CZK 142.8 bn). The general government sector achieved the highest growth dynamics (by 38.1%). The largest absolute decrease in deposit volumes, on the other hand, was recorded by non-financial companies (by 4.1%, or CZK 20.1 bn). The financial institutions sector recorded the largest relative decrease as volumes fell by 12.1%, or CZK 13.3 bn.

Total household indebtedness to banks and non-banking financial institutions increased year on year by 16% and reached CZK 1,009.5 bn as at the end of 2008.[23] It can be regarded as a relatively healthy sign that households continue to take out loans primarily to meet their housing needs. These loans comprise 60% of household indebtedness. In absolute terms, housing loans increased in 2008 by CZK 104.0 bn while consumer loans grew by CZK 37.6 bn. Both categories, however, recorded decrease in their year-on-year growth rates in 2008. In the case of housing loans, the growth rate fell by 17.3 percentage points to 20.2%. The dynamics of consumer loans decreased by 12.9 percentage points to 14.1% in 2008.

[21] Client CZK accounts and loans based on ARAD banking statistics, broken out by sectors and including both residents and non-residents.
[22] This category includes non-profit organisations and non-residents.
[23] This data includes CZK and foreign currency loans to households (residents) and non-profit organisations serving households as well as funds provided to non-banking institutions.

Graph 4.2: Total household indebtedness

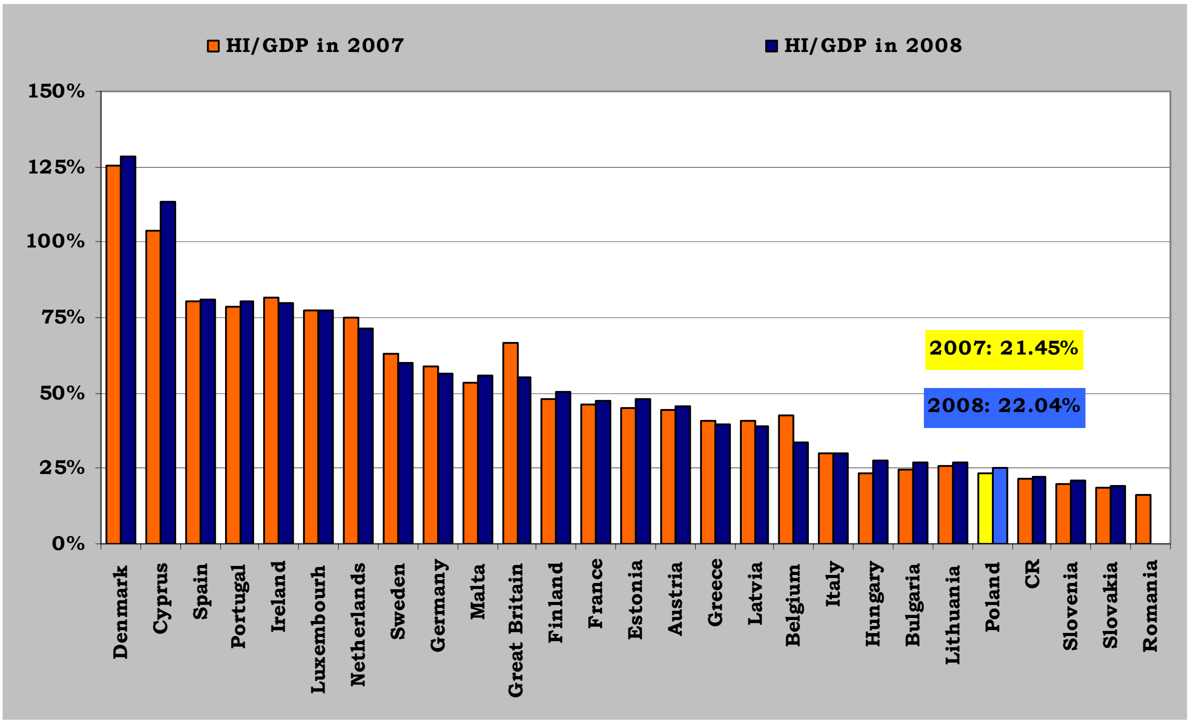


Source: CNB - ARAD

Compared to the rest of Europe, the level of household indebtedness relative to economic output remains relatively low (at 27.2% of GDP). Caution is in order, too, considering the economic slowdown and possible worsening of households' ability to repay loans. Greater attention thus must be given to the growth dynamics of households' obligations. The ratio of household debts to domestic GDP rose by 2.6 percentage points year on year. The current low level of household indebtedness as a proportion of GDP will serve as a factor alleviating the impact of the economic slowdown on Czech households. The greatest repayment problems thus threaten especially the most endangered groups such as, for example, low-income households that must spend more or less the majority of their income to service their debts.

As measured by the household indebtedness indicator, calculated as the ratio of total debt in the household sector to GDP, the Czech Republic is among the least indebted of EU Member States. As seen in Graph 4.3, other new Member States from Central Europe, which, like the Czech Republic, because of their recent transformation to market economies, have so far not managed to accumulate the relative volumes of loans common in West European countries, also show low household indebtedness.

Graph 4.3: Comparison of household indebtedness in the EU[24]



Source: ECB, Eurostat

4.2.3. Building societies

In 2008, over 705,000 new building savings contracts were concluded in a total amount of approximately CZK 218 bn.[25] The number of newly concluded contracts thus increased in comparison with the previous year by nearly 22%. One of the motives leading clients to significant year-on-year growth in newly concluded contracts could be the fact that building savings schemes are perceived by the population as a relatively secure and profitable savings instrument. The average target value for individuals reached almost CZK 303,000, which represents a more than 6% increase year on year. In 2008, the target amount was increase by ca CZK 94 bn for ca 336,000 total contracts, which represents a year-on-year increase of approximately 54,000 contracts.

Of course, the absolute number of concluded contracts is always higher than the number of newly concluded contracts, and that leads to a steady decline in their overall number. The total number of contracts in the savings phase thus fell at the end of 2008 by ca 62,000 year on year to almost 5.1 mn. This represents the continuation of a trend, as the vast majority of those contracts being terminated are so-called old contracts[26] with state support in the amount of CZK 4,500. The share of so-called new contracts amounted to 43% of all contracts as at the end of 2008. This represents a year-on-year increase of 11.9 percentage points. The change in the structure of building savings contracts was positively projected in the amount of state support distributed. In 2008, state support to building savings schemes was distributed in the total amount of CZK 14.2 bn. That is about CZK 760 mn less than in 2007.

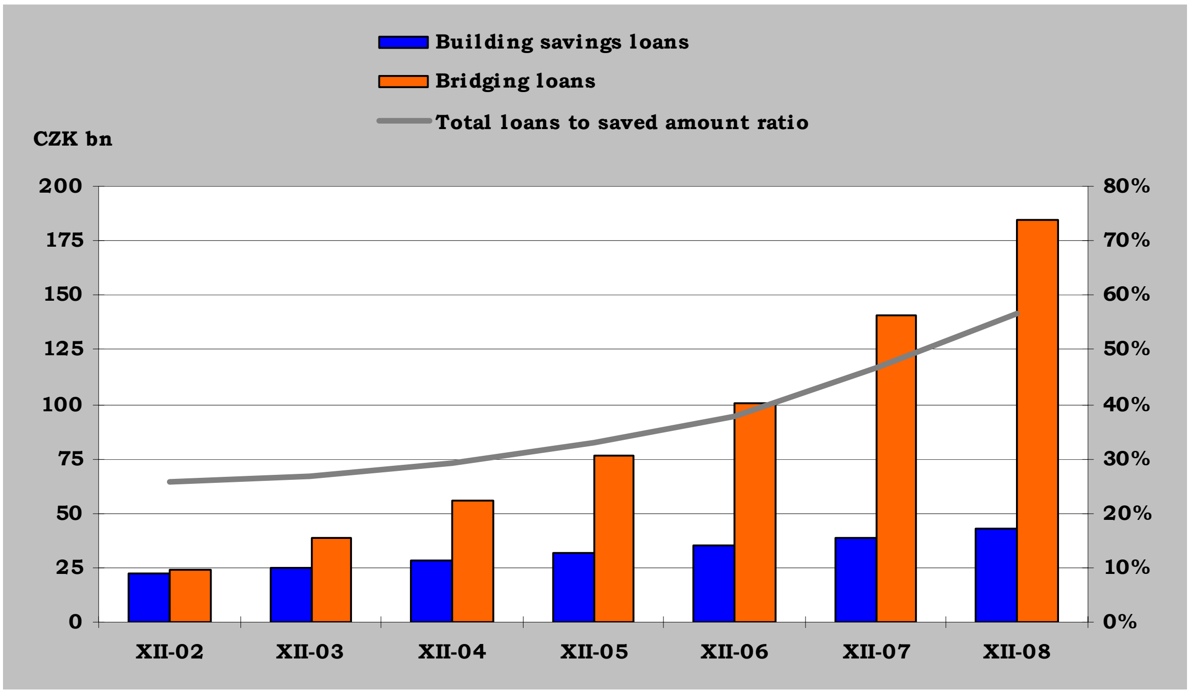
The total number of loans increased year on year to 971,000 along with the simultaneous increase in their total volume to CZK 227.4 bn. This fact was reflected in the repeated

[24] MoF's own calculations based on data from ECB and Eurostat, which differs from CNB and CZSO data.
[25] See Table 8.3 in Appendix 2.
[26] Contracts concluded by 31 December 2003.

growth in the ratio of the loans volume to the saved amount (56.7%), which thus increased year on year by 10.1 percentage points.

While the growth rate for the total number of loans decreased in 2008 compared to previous years (to 3.0% versus 4.7% in 2007), the year-on-year absolute increase in their volume continues to be very high (CZK 28 bn).

Graph 4.4: Development of loans in building savings schemes sector



Source: MoF

Since 2002, the structure of building savings loans has changed. Although building savings loans are increasing, they are far from catching up to the growth dynamics for bridging loans, as seen in the graph above.

The following table presents the growth in building savings loans and mortgage loans provided to the population. Although mortgage loans grew by a larger absolute amount than building savings loans, building savings loans increased at a higher rate. The ratio of these increases illustrates this fact. This points to the relative slowing of the dynamics of mortgage loans in the monitored period. The reasons for this can be seen, on the one hand, in the fall in the number of mortgage loans agreed and, on the other, in the interest in building savings loans attracted by an offer of loans with stable interest rates.

Table 4.9: Development of loans

As at 31 Dec (CZK bn)	2006	2007	2008
Growth of building savings loans	27.4	43.9	48.1
Growth of ML to population	71.6	95.3	63.6
Growth ratio (without units)	2.61	2.17	1.32

Source: CNB, MoF

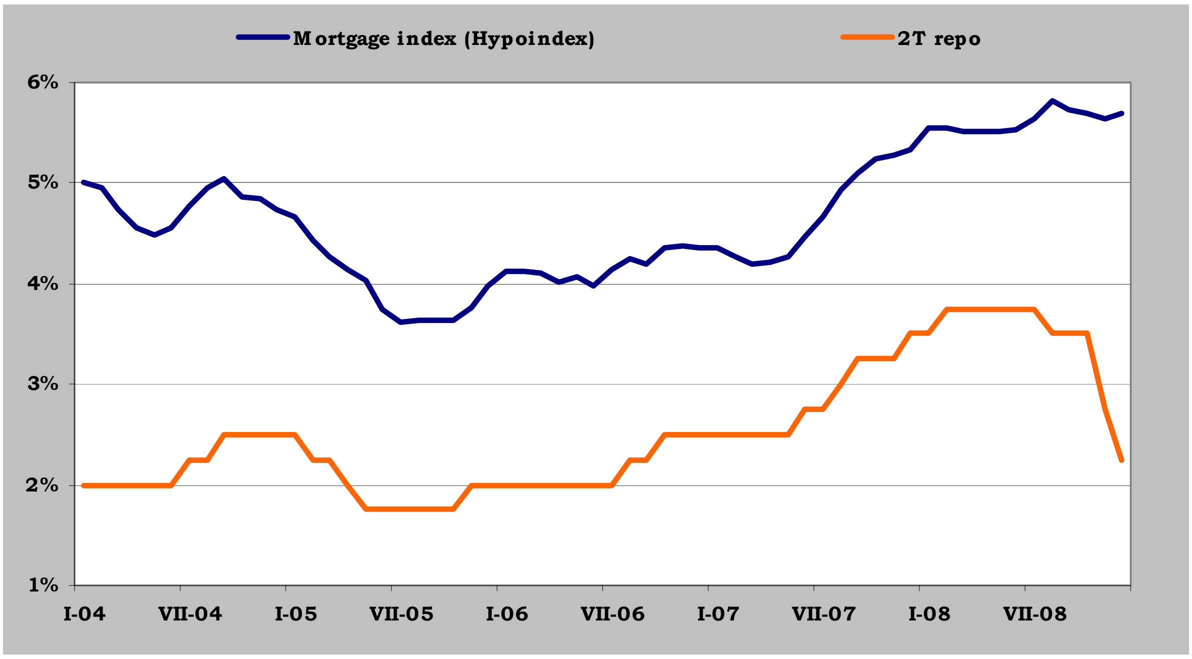
At the end of July 2008, a decision by which the CNB approved the merger of HYPO stavební spořitelna and Raiffeisen stavební spořitelna became legally valid. The number of building societies thereby decreased to five.

4.2.4. Mortgage market

The volume of mortgage loans provided to the population (hereinafter referred to as the "volume of mortgage loans") as at 31 December 2008 reached CZK 397.1 bn. A subject of debate is the slowing in the growth dynamics for mortgage loans. In 2008, the volume of mortgage loans grew by CZK 63.6 bn, which represents a 33.3% year-on-year decline in additions. An explanation for this development can be seen in the high growth in the volume of mortgage loans during the fourth quarter of 2007 (a year-on-year gain of 69.6%). This could have been influenced by an anomaly in the form of a forward buying effect, as entities acted to avoid the consequences of tax reforms by executing transactions before 1 January 2008, and thus before the increase of VAT for construction work. Among other factors that may weaken the dynamics of mortgage loans are modest growth in interest rates, slowing of real income growth, subsiding of speculative interest in purchasing apartments for rental purposes, as well as psychological influences on potential buyers from the developments on certain markets such as the USA or Spain or due to the uncertain impacts upon particular individuals due to developments in the Czech economy.

In the case of residential real estate in the Czech Republic, a key issue is the price bubble especially for older apartments in panel-block apartment buildings. On the demand side, access to mortgage loans, the development of employment and real incomes, the development of the inflation rate and of inflation expectations should influence prices development. On the supply side, the construction activities and financial health of developers as well as the number of housing units ready for sale should be influential. Further continuation in the process of gradually deregulating rents may also affect price changes. Price developments in individual segments of the market can move with varying intensity in various directions. Price stagnation and decline in certain segments, however, are important scenarios for calculating future development.

Graph 4.5: Selected interest rates' development[27]



Source: Fincentrum, CNB

The rates on the Czech mortgage market depicted by means of the Hypoindex mortgage index rose in 2008 by 0.35 percentage points. Compared to 2007, when the rates increased by roughly 1 percentage point, this represents a clear slowing of growth dynamics.

[27] The FINCENTRUM HYPOINDEX indicator is a weighted average interest rate applied to new mortgage loans to individuals in the given calendar month. The graph above depicts a time series of this interest rate.

More interesting, however, is comparison of the mortgage index rate with CNB's repo rate. Until August 2008, a clear connection could still be seen between the developments of the two rates. The spread between the mortgage index rate and the repo rate hovered (as it mostly had since 2005) around 2 percentage points. Nevertheless, since September an increase in this spread can be observed owing to the combination of CNB's rate reductions and the stagnation of the mortgage index rate. In December 2008, the difference between the two rates had reached 3.44%. The rise of the spread reflects the fact that banks are more strictly assessing the risks that result from providing mortgage loans and consequently they are demanding a higher risk premium.

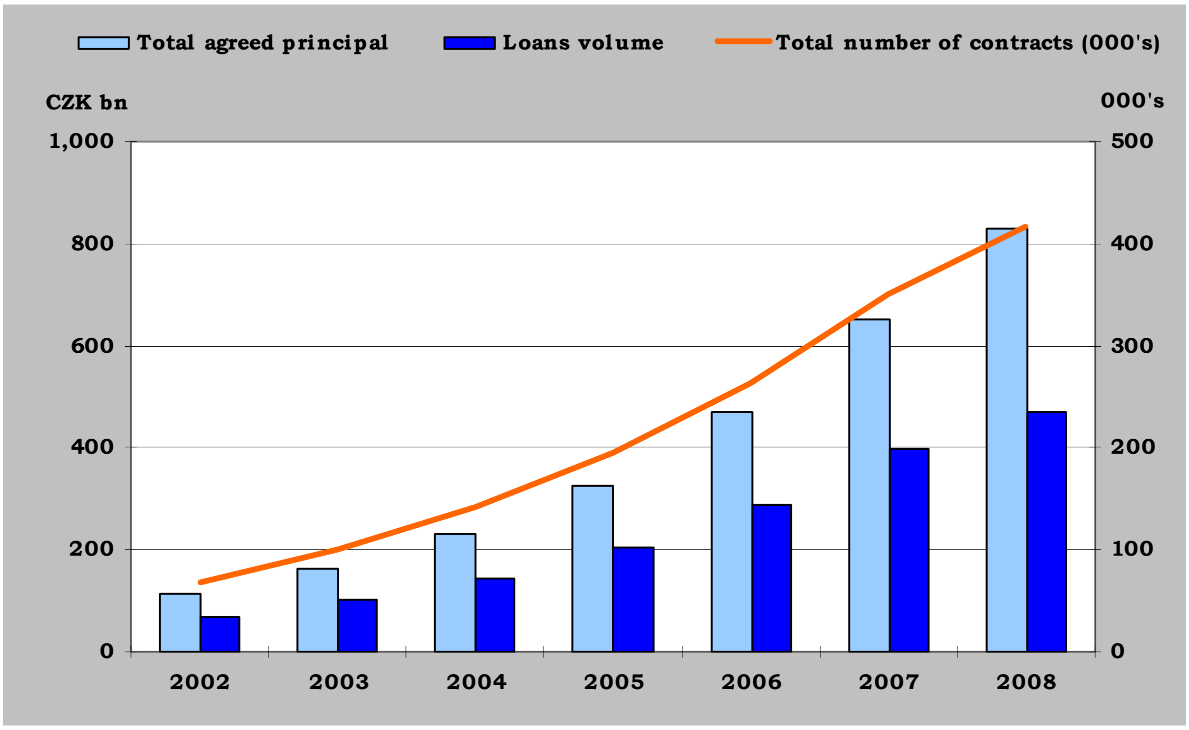
Table 4.10: Mortgage loan (ML) balances

As at 31 Dec		2006	2007	2008	Year-on-year change	
					Abs.	(%)
Individuals	**total (in thousands)**	255.7	339.0	403.5	64.5	19.03
	total agreed principal (CZK bn)	327.3	469.6	583.5	113.9	24.26
Business entities	**total (in thousands)**	7.4	9.8	11.7	1.9	19.71
	total agreed principal (CZK bn)	132.9	174.4	238.6	64.2	36.82
Municipalities	**total (in thousands)**	0.8	0.8	0.9	0.0	2.38
	total agreed principal (CZK bn)	8.0	8.3	8.5	0.2	1.96
Total	**total (in thousands)**	263.9	349.6	416.1	66.4	19.01
	total agreed principal (CZK bn)	468.3	652.3	830.6	178.3	27.34
Loans volume(CZK bn)		288.7	398.2	468.1	69.8	17.54

Source: MRD, CNB - ARAD

Table 4.10 illustrates the balance of mortgage loans provided to households. The number of mortgage loans increased by over 64,000, or 19%, and the total volume of loans grew at a similar rate.

Graph 4.6: Aggregate mortgage market indicators



Source: MRD, CNB - ARAD

Graph 4.6 presents general indicators for the mortgage market. Data on the total number of contracts and agreed principal amounts includes not only households but also entrepreneurs and municipalities. The volume of loans thus includes mortgage loans for residential and non-residential real estate. The volume of loans grew slower year on year (by 17.5%) than the number of contracts (by 19.0%).

Table 4.11: Balance of mortgage loans (ML) to households

As at 31 Dec	2005	2006	2007	2008	Year-on-year change	
					Abs.	(%)
Number of ML (000s)	188.3	255.6	339.0	403.5	64.5	19.03
Agreed principal (CZK bn)	226.5	327.3	469.6	583.5	113.9	24.26
Volume of loans (CZK bn)	166.7	238.2	333.6	397.1	63.6	19.06

Source: MRD, CNB - ARAD

4.2.5. Credit unions

Despite the beginning world financial crisis and slowing of the domestic economy, the past year was favourable overall for the credit union sector. Though this segment is not comparable in size to the banking system, credit unions again found their niche in the field of providing services to their own clients and to members of cooperatives, especially in the areas of accepting deposits, payment systems and provision of loans. As at the end of 2008, 17 credit unions were operating in this sector with total assets exceeding CZK 12 bn (representing intense year-on-year assets growth of 34.8%). The main factor behind this growth was the increase in the volume of deposits, which rose by 46.2% year on year to some CZK 10.3 bn. This development can be attributed to interest-rate and fee policies oriented to retail clients and to the long-term strengthening of depositor confidence. Higher depositor confidence is promoted by the fact that the funds deposited by savers at credit unions, as with bank deposits, are insured by the Deposit Insurance Fund. Therefore, the same quantitative limits on deposit insurance apply for these deposits. Credit unions, just like banks, have been subject to the uniform supervision of CNB since 1 April 2006. At the same time, the supervisory rules for credit unions in recent years have become closer to those for banking supervision due to, for example, implementation of the Basel II regime.

The volume of loans provided increased significantly. Receivables from clients (i.e. credit union members) rose year on year by 29.15% to a total of CZK 6.7 bn. As regards the quality of the loan portfolio, the share of standard receivables in total receivables fell by nearly 3 percentage points year on year to 93.41%. The share of watch receivables, on the other hand, increased by 2.9 percentage points to 4.73%, while the share of the highest risk category of loss receivables grew by 0.09 percentage points to 1.86%.

Table 4.12: Credit unions – selected indicators

As at 31 Dec	2006	2007	2008
Number of members of credit unions	36,395	44,789	35,921
Total assets (CZK mn)	6,856.4	8,946.9	12,058.9
Receivables from clients (CZK mn)	4,117.6	5,196.2	6,711.0
Payables to clients (CZK mn)	5,216.3	7,032.3	10,282.9
Share of standard receivables (%)	98.30	96.39	93.41

Source: CNB

Credit unions' profits declined year on year by 9.6% to CZK 74.8 mn, while their total assets grew. Return on assets[28] thus fell from 9.2% in 2007 to 6.2% a year later.

[28] The ratio of the annual profit and total assets as at 31 December.

The divergent size of individual entities, and consequently the level of concentration in this sector, is remarkable. The four most prominent players control over 82% of the assets in the entire sector. The two largest entities, moreover, hold nearly 66% of total assets.

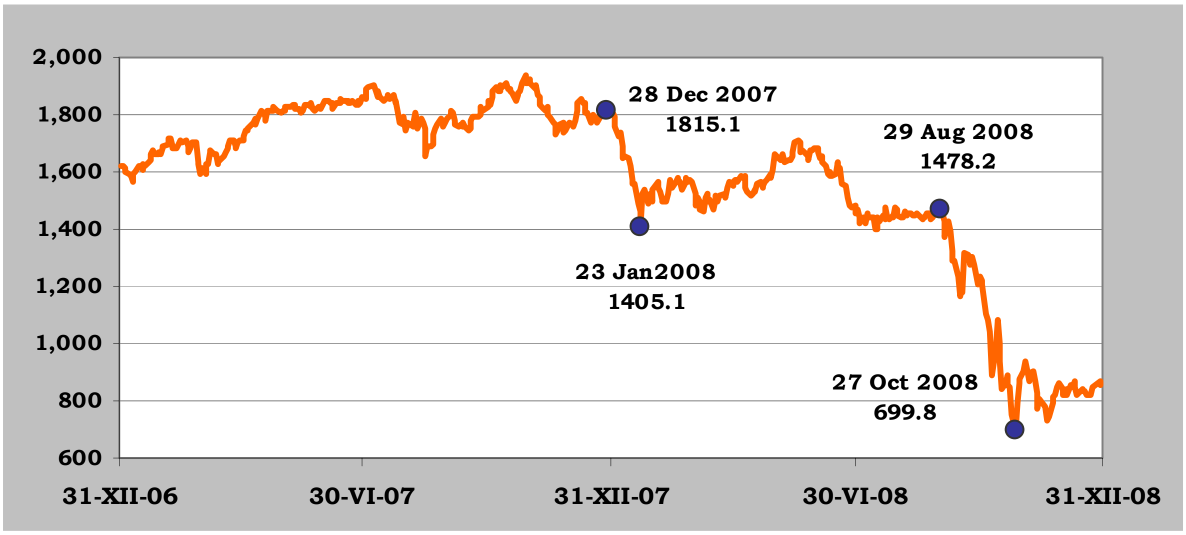
4.3. Capital market

The worsening situation of the global and Czech economies was reflected on capital markets. With the gathering recession, investors' pessimism also grew.

4.3.1. Regulated markets

In 2008, the main index of the Prague Stock Exchange recorded the steepest drop of its 15-year history. Compared to the end of 2007, when it was hovering near its historic maximum, the index fell to 858 points, thus losing 52.7%. It last touched such values in the second half of 2004.

Graph 4.7: PX index development



Source: PSE

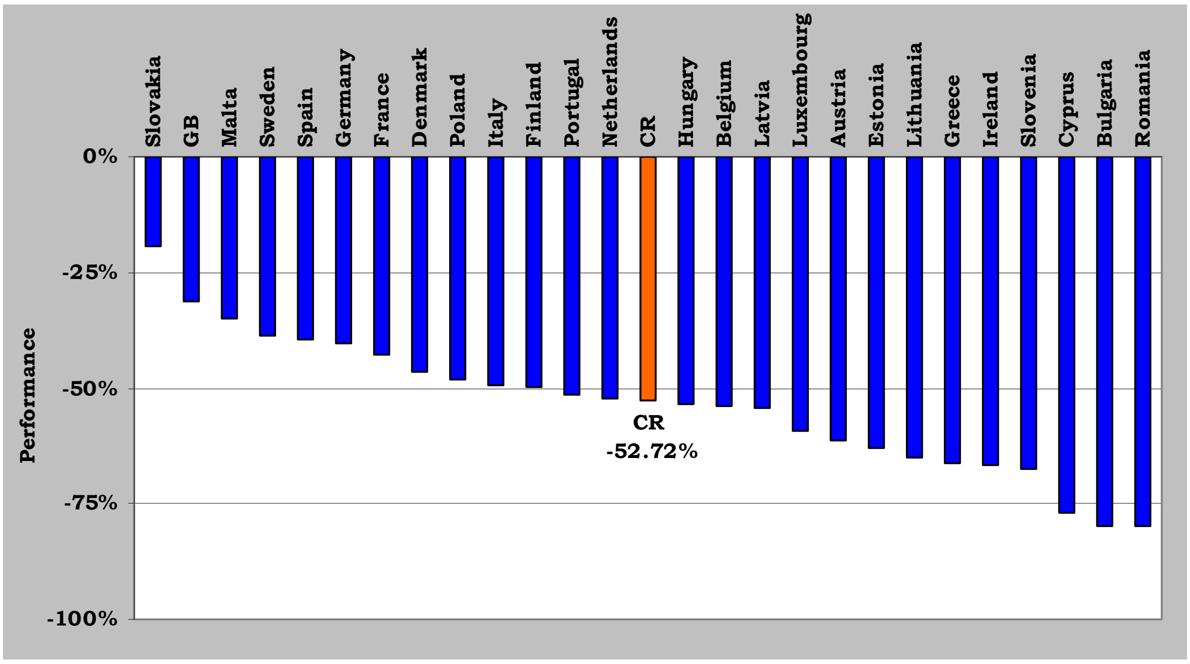
Table 4.13: PX index development

Year		2002	2003	2004	2005	2006	2007	2008
PX	As at 31 Dec	460.7	659.1	1,032.0	1,473.0	1,588.9	1,815.1	858.2
	Change (%)	16.75	43.06	56.58	42.73	7.87	14.24	-52.72

Source: PSE

The main cause of the drop in share prices on the PSE was the financial crisis. This was most markedly evident in trading on the PSE during January, when the PX index lost 22.6%, and in September and October, at which time the PX index had taken back 52.7% and dropped to as low as 699.8 points. For various reasons, the real estate developers ORCO Property Group (ORCO) and ECM Real Estate Investments (ECM) along with Central European Media Enterprises (CETV) and AAA Auto Group (AAA) registered the greatest losses.

Graph 4.8: Performance of significant stock exchange indexes in EU Member States in 2007[29]



Source: FESE

From the graph above it is evident that the sharp drop in share prices on the PSE was not among the largest recorded by the main exchanges of EU Member States.

Table 4.14: Trade value

Annual (CZK bn)			2005	2006	2007	2008	Year-on-year change (%)
PSE	**Shares and units**		1,041.2	848.9	1,013.0	852.0	-15.89
	Bonds		533.2	598.9	508.9	643.2	26.39
	Derivatives	**Futures**	0.0	0.0	1.9	0.6	-68.71
		Certificates and warrants	0.0	0.0	1.2	0.5	-62.00
		Total	0.0	0.0	3.1	1.1	-66.06
	Total		1,574.4	1,447.9	1,525.0	1,496.2	-1.88
RM-S			6.6	3.9	7.7	6.9	-10.38
Total			1,581.0	1,451.8	1,532.6	1,503.1	-1.93

Source: PSE, RM-S

The drops in share prices and uncertainty regarding future development of the economy and capital markets also were reflected in a decrease in the volume of shares trading on the PSE. A similar situation can be seen for the RM-S, upon which trading occurs almost exclusively in shares. The decrease in share trading volumes was compensated by increased interest in bonds, which is a common phenomenon in a time of crisis and uncertainty. The total volume of trading thus decreased only slightly.

[29] Austria-ATX, Belgium-BEL 20, Bulgaria-SOFIX, Cyprus-FTSE/CySE 20, Czech Republic-PX, Denmark-OMXC 20, Estonia–OMXT, Finland-OMXH 25, France-CAC 40, Germany-DAX, Greece-FTSE/ATHEX 20, Hungary-BUX, Ireland-ISEQ20, Italy-MIB, Latvia-OMXR, Lithuania-OMXV, Luxembourg-LuxX, Malta-MSE, Netherlands-AEX, Poland-WIG 20, Portugal-PSI 20, Romania-BET, Slovakia-SAX, Slovenia-SBI 20, Spain-IBEX-35, Sweden-OMXS 30, United Kingdom-FTSE 100.

Table 4.15: Number of registered issues[30]

	As at 31 Dec	2004	2005	2006	2007	2008
Shares	**Main market**	6	8	10	21	17
	Secondary market	29	19	11	-	-
	Free market	20	12	11	11	11
	Total	55	39	32	32	28
Bonds	**Main market**	24	27	28	41	38
	Secondary market	20	15	15	-	-
	Free market	35	54	67	91	83
	Total	79	96	110	132	121
Derivatives and other products	**Futures**	-	-	2	6	6
	Investment certificates	-	-	7	39	46
	Warrants	-	-	0	2	2
	Total	0	0	9	47	54
Total						

Source: PSE

The number of share issues decreased again last year.[31] The mining company New World Resources (NWR) and the Vienna Insurance Group (VIG) entered the market and thereby expanded the spectrum of titles quoted on the PSE. The number of certificates increased, but the volume of trades in these securities and derivatives continue to be negligible as compared to those for shares and bonds.

During the first quarter of 2009, the number of share issues decreased further. At the end of February, the French multinational company Sanofi-Aventis became the majority owner of Zentiva. In its takeover offer, the company paid CZK 1,150 per share and obtained a shareholding of more than 95%. As at 28 April 2009, the shares were delisted from trading on the PSE. Meanwhile, Sanofi-Aventis has taken steps to buy out minority shareholders.

In 2005, an amendment to the Commercial Code making it easier for majority owners to buy out shares from small shareholders came into take effect. According to data from the Czech Capital Information Agency (Čekia), more than 340 companies have proceeded to buy out minority shareholders since that time. By the end of the first quarter of 2009, majority owners had paid more than CZK 14 bn for these shares. The most costly buyout took place in Československá obchodní banka (CZK 2.6 bn). Other shareholders receiving more than CZK 1 bn for their minority interests include those of Česká pojišťovna (not quite CZK 1.5 bn), Severočeské doly (more than CZK 1.1 bn) and Plzeňský Prazdroj (not quite CZK 1.1 bn).

In 2008, the PSE's shareholder structure radically changed. The company Wiener Börse (Vienna Stock Exchange), the organiser of the regulated market in Austria that also operates exchanges in Slovenia and Hungary, became the majority owner with an approximately 93% share.

4.3.2. Energy exchange

Although the Prague Energy Exchange began operating only at the start of July 2007, the volume of trades for all of 2008 was only one third higher. The financial crisis, which

[30] On 1 July 2007, the main and the secondary markets merged.
[31] The shares of the companies Jihomoravská plynárenská, Pražská plynárenská, Středočeská plynárenská and Setuza were withdrawn from the primary market. Two issues were transferred from the main market to the free market.

dampened trading, was manifested here as well. In 2008, 9,130 contracts were concluded on the exchange.

Table 4.16: Main indicators of trading on PEE

Indicator	Market	2007	2008	Change	
				Abs.	(%)
Trade value (EUR mn)	**Futures**	1,897.8	2,441.0	543.2	28.62
	Spot[32]	-	7.1	-	-
	Total	1,897.8	2,448.0	550.2	28.99
Number of products (at end of period)	**Futures**	26	54	28	107.69

Source: PXE

4.3.3. Investment firms and asset management

Again in 2008, the roles of entities in the investment firms sector were distinctly distributed. Banking-segment investment firms dominate in terms of trading volumes for their own account, procurement trades and volumes of client assets. Non-banking investment firms, together with investment companies managing clients' assets, on the other hand, concentrate on managing their clients' assets. This also accounts for their predominance in the volume of management trades and managed funds. In 2008, investment companies significantly strengthened their position, as, in contrast to non-banking investment firms, they increased the volume of both management trades as well as managed assets.

[32] Trading on the spot market was launched in February 2008.

Table 4.17: Selected indicators of investment firm sector (by segment) in 2008[33]

As at 31 Dec (excl. derivatives, CZK bn)	2008			Change (%)		
	Banking IF	Non-banking IF	Investment companies[34]	Banking IF	Non-banking IF	Investment companies
Total number of licensed entities	25	30	6	4.17	-11.76	0.00
Total transactions value[35]	99.1	15.2	1.8	14.91	-20.64	141.81
of which: for own account	63.7	5.7	0.0	5.71	-14.77	-100.00
management	0.2	2.8	1.8	6.56	0.57	142.81
procurement	35.2	6.7	0.0	36.51	-30.91	-80.95
Value of managed funds	52.3	408.0	78.6	30.98	-57.85	15.55
Value of clients' assets	1,167.2	418.0	172.8	-20.51	6.33	25.66
Number of clients (according to contracts, 000's)	1,315.5	114.6	2.0	5.73	53.34	119.70
of which: active clients (000's)[36]	190.1	48.8	2.0	9.56	51.41	120.61

Source: CNB

Asset management

Three financial groups, whose market share decreased during 2008 by 1.9 percentage points to 62.9%, continue to dominate the asset management sector. The total volume of funds increased in 2008 by almost 1% to CZK 723 bn. Due to the financial crisis, a number of companies recorded drops in the total volume of assets under management, and in some cases even in double-digit percentages, while others were able to increase managed assets at similar rates. Generali PPF Asset Management, which increased its assets under management by nearly 14%, had the largest volume of assets under management as at the end of 2008.

[33] Because a derivatives contract's value is available only at the underlying asset value, derivatives are not included in the table.
[34] Investment companies managing customer assets.
[35] All trades (purchase and sale) concluded at PSE, RM-S, foreign markets and direct trading; accumulated for shares, unit certificates and bonds; average per daily base excl. derivatives trading.
[36] An active customer is a customer, to which a investment firm has provided an investment service during the last 6 months.

Table 4.18: Financial groups by value of assets under management

As at 31 Dec (CZK bn)	Value of assets under management		
	2007	2008	Change (%)
Generali PPF Asset Management + ČP Invest	145.7	166.0	13.96
ČSOB (Group)	164.4	156.3	-4.97
Česká spořitelna (Group)	154.0	132.4	-14.03
ING (Group)	85.8	85.8	0.01
Komerční banka (Group)	69.2	77.5	11.97
AXA investiční společnost	36.8	38.2	3.73
UniCredit Bank, a.s. + Pioneer Investments	17.0	14.9	-12.35
CREDIT SUISSE ASSET MANAGEMENT investiční společnost	13.0	14.2	9.09
BNP Paribas Asset Management	-	11.7	-
Conseq Investment Management	12.4	10.5	-15.35
Others	17.4	15.3	-12.48
Total	715.8	722.7	0.97

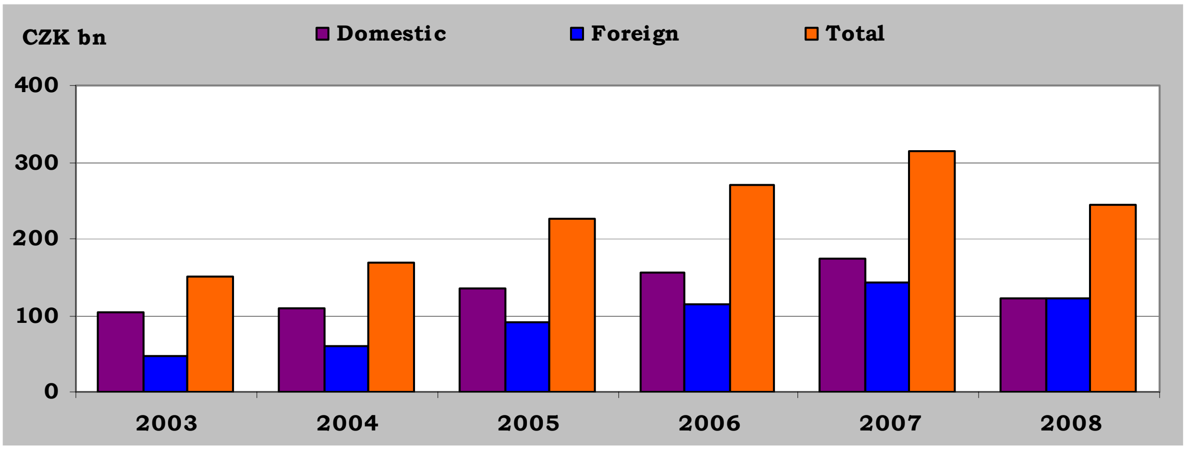
Source: AKAT

Investment intermediaries
The number of investment intermediaries increased again in the first half of the year, reaching nearly 15,000 at the end of June. In the second half, however, the number of investment intermediaries dropped below 13,000. This decrease was due to an amendment to the Act on Capital Market Undertakings as a result of which a portion of investment intermediaries became tied agents, replacing the so-called second-level investment intermediaries. These tied agents are no longer listed in the register of investment intermediaries, the number of which was reduced by this administrative intervention. Following this amendment, an investment intermediary can employ only its own personnel or tied agents. Investment intermediaries are directly accountable for their activities to CNB, which only registers the tied agents. Investment intermediaries are now entitled to provide not only intermediation but also investment advisory concerning investment securities and collective investment securities.

4.3.4. Collective investments

After many years of rising interest in investing in unit trusts and the associated continuous growth in the volume of resources managed by these funds, the year 2008 represents a significant turning point. A year-on-year drop (by CZK 71.4 bn) was recorded for the first time, falling to a total of nearly CZK 244 bn. The decrease in the volume of assets under management by nearly 23% thus returned the volume of funds in collective investments to approximately the same level as 3 years prior.

Graph 4.9: Development of investments in unit trusts



Source: AKAT

The ratio of assets invested into domestic and foreign funds also changed significantly. Over the past several years, the two categories have gradually levelled out, as the sale of foreign funds showed more dynamic growth. In 2008, there was a fundamental turning point as the volume of assets in foreign funds (CZK 123 bn) surpassed those in domestic funds (CZK 120.9 bn) due especially to the smaller drop in the former (by 13.5%) compared to the latter (by 30.1%).

Table 4.19: Assets in individual types of unit trusts by domicile

As at 31 Dec (CZK bn)	2007			2008			Year-on-year change (%)		
Unit trust type	**Domestic**	**Foreign**	**Total**	**Domestic**	**Foreign**	**Total**	**Domestic**	**Foreign**	**Total**
Money market	77.0	30.9	107.8	55.9	32.2	88.1	-27.4	4.3	-18.3
Bond	20.8	15.4	36.2	14.0	12.5	26.5	-32.8	-18.7	-26.8
Equity	16.6	31.5	48.0	7.3	16.1	23.5	-55.9	-48.7	-51.2
Mixed	28.8	9.7	38.5	19.4	6.7	26.1	-32.7	-31.1	-32.3
Funds of funds	18.4	0.3	18.7	12.7	0.2	12.9	-31.0	-20.5	-30.9
Guaranteed	10.3	54.5	64.7	9.9	55.2	65.1	-3.3	1.3	0.6
Real estate	1.2	0.0	1.2	1.8	0.0	1.8	45.2	-	45.2
Total	173.0	142.2	315.2	120.9	123.0	243.9	-30.1	-13.5	-22.6

Source: AKAT

The ongoing crisis, however, affected more than just the performance of funds or the volume of assets under management. The number of standard foreign open-ended unit trusts in the Czech Republic reached 1,569 at the end of 2008, which is 90 more than at the end of 2007 but 5 less than at the half-year mark. The number of domestic open-ended unit trusts, meanwhile, has increased especially due to special funds (101 compared to 83 a year earlier). The increase in standard funds was less (41 compared to 38 a year earlier). The number of investment funds also increased in 2008 to a total of 16 entities (compared to 7 at the end of 2007). These funds, however, are focused mainly on qualified investors.

Table 4.20: Unit sales and redemptions in 2008

(CZK bn)	Equity	Bond	Money market	Funds of funds	Mixed	Real estate	Total
Sales	4.0	1.8	20.0	5.4	3.3	0.9	35.4
Redemptions	3.9	8.6	39.3	7.0	5.5	0.5	64.8
Net sales	0.1	-6.7	-19.3	-1.7	-2.2	0.4	-29.4

Source: AKAT

The volume of investments in domestic funds decreased by CZK 52.1 bn. Of this, approximately CZK 29.5 bn was due to negative net sales. The drop in the volume of managed funds, however, does not in itself show whether the cause was more due to change in the number of units or to developments in the value of the equity per unit.

Table 4.21 shows that unfavourable price development for shares in the portfolios of these funds was practically the sole contributor to the more than 55% decrease in the volume of assets in equity funds. Through the continuing decline in fund values, people actually purchased these funds more than they sold them (in three quarters out of four). In contrast, most investors, relatively speaking, sold bond funds, the prices of which decreased by 2.45% on average during the year. Investors withdrew nearly a third of the volume of bond funds through redemptions. The largest redemptions in absolute terms involved money market funds (CZK -19.3 bn) and thus redemptions were the primary contributor to the decrease in the volume of assets in this category by CZK 21.1 bn. Investors in equity funds, meanwhile, showed stronger mettle in the face of declining equity markets. In contrast, the volatility in the performance of money market funds was sufficient to drive those investors to wide-scale selling.

Looking at the weighted average development in the prices of money market funds (-3.8%), however, it is no wonder that investors withdrew their assets. Money market funds had always been regarded as a secure refuge for conservative investors. The financial crisis became evident here, too, and the slump in the value of these securities, and especially those from endangered foreign banks that had found their way even into the portfolios of domestic money market funds, decreased the value of assets in the funds. From a fourth-quarter summary, it is evident that it was at this time that funds experienced the greatest run of redemptions. These funds will now need to battle for the lost confidence of investors with banks, whose offerings of savings and term-deposit accounts present great competition for investment funds considering the bank products' interest rates, deposit insurance, liquidity and often minimal fees. Guaranteed funds, too, must face up to such problems and competition. The returns of these funds will most likely follow a negative scenario characterised by zero appreciation for several years during which investors will receive "only" their principal upon maturity.

Price and redemption factors contributed almost equally to the drop in the volume of assets in the "funds of funds" and "mixed funds" categories, although redemptions contributed slightly less.

Table 4.21: Influence of development of shareholders' equity and net sales of units on the value of assets in domestic open-ended funds

(%)		Equity	Bond	Money market	Funds of funds	Mixed	Real estate
Number of funds[37]		17	14	8	26	31	3
NAV change	**1Q**	-17.24	-13.67	-5.46	-6.72	-6.83	14.94
	2Q	-1.78	-6.16	-0.78	-0.27	-3.06	8.28
	3Q	-18.73	-5.02	-1.86	-5.43	-7.52	13.23
	4Q	-32.27	-13.78	-23.79	-16.17	-12.98	-6.94
	year	-55.25	-33.65	-29.84	-26.24	-27.31	31.14
Change in number of units (weighted average)	**1Q**	0.26	-12.56	-5.32	-1.59	-0.35	13.79
	2Q	1.21	-6.55	-1.86	1.06	-1.46	8.34
	3Q	-1.27	-6.50	-1.67	-2.40	-3.06	10.54
	4Q	0.60	-11.12	-21.09	-9.30	-4.55	-7.70
	year	0.59	-32.08	-27.99	-11.92	-9.11	25.78
Rate change (weighted average)	**1Q**	-17.49	-1.32	-0.17	-5.22	-6.58	1.01
	2Q	-3.02	0.42	1.12	-1.30	-1.62	-0.07
	3Q	-17.73	1.70	-0.23	-3.08	-4.56	2.43
	4Q	-32.76	-3.09	-3.74	-7.64	-8.81	0.82
	year	-55.82	-2.45	-3.77	-16.24	-19.57	4.22

Source: AKAT, MoF

The newest category of real estate funds,[38] which was the only category during 2008 to record growth in the value of assets, a positive appreciation and positive net sales, is a quite distinctive category. Upon a closer look at individual quarters, however, it can be seen that the positive double-digit growth in the volume of assets under management lasted only through the first three quarters of 2008. In the fourth quarter, a volume decrease in the amount of nearly 7% was already evident due to redemptions. Nervousness regarding the general situation and the development in the same segment abroad thus had arrived to the Czech Republic as well.

Despite the continuing difficult situation on financial markets, it should not be forgotten that the declines on exchanges also create foundations for future profit opportunities on those same markets. It remains to be seen, however, how specific investors, and particularly those whose accounts saw negative returns, will perceive general axioms of this sort. Stable invest flows into funds thus can be expected in this period primarily from investors who have established programmes for regular investing, whether directly into funds or indirectly through, for example, unit linked insurance.

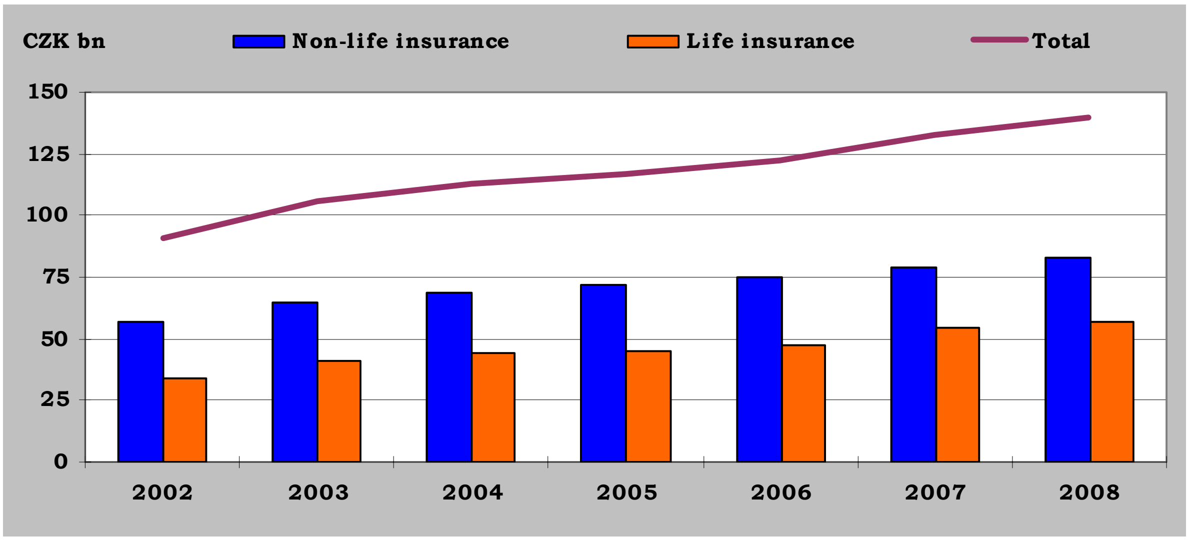
4.4. Insurance companies

In the past year, insurance companies operating on the Czech insurance market did not need to involve themselves any more significantly in resolving property losses caused by

[37] Due to data availability, 98 domestic funds denominated in CZK were used for the analysis. These 98 funds cover 95% of the total volume of assets under management in domestic funds.
[38] After one of three funds terminated its activities, only two real estate funds remained as at the end of 2008. One of these accounts for 95% of the assets in this category.

natural disasters. Insurance claims due to adverse impacts of extreme climatic effects were recorded only regionally and concerned especially damages from strong winds and flooding. In this regard, the past year thus can be assessed as unproblematic.

Graph 4.10: Development of gross premiums written



Source: CNB

Despite a decrease in dynamics by 3.6 percentage points year on year, the insurance market recorded relatively positive results. Considering the negative events on financial markets, and especially the worsening economic environment at the close of the year, this slight slowdown can be regarded as confirming the relative stability of the sector even in comparison with the extraordinarily prosperous 2007.

The indicator of gross premiums written rose by 5.2% to reach CZK 139.9 bn. Non-life insurance, which increased by 5.3% to CZK 82.9 bn, contributed most to that outcome. Its total volume represents almost two thirds (59.3%) of the total selected gross premiums written. Life insurance increased by 5.2% to total CZK 56.9 bn. Life insurance’s usually higher growth dynamics seen in previous periods were not sustained in 2008. The deficit in one-off premium payments, which fell by ca 1.5%, was especially responsible for the reduced dynamics in life insurance. The nearly 8% increase in regular premium payments provided life insurance an element of stability.

Table 4.22: Results of insurance companies[39]

As at 31 Dec	2006	2007	2008	Year-on-year change	
				Abs.	(%)
Number of policies (000's)	22,216	23,241	25,204	1,963	8.45
of which: non-life insurance	15,456	16,317	18,222	1,905	11.67
life insurance	6,760	6,924	6,982	58	0.84
Number of newly concluded policies (000's)	8,024	9,016	10,414	1,398	15.51
of which: non-life insurance	7,238	8,102	9,470	1,368	16.88
life insurance	786	914	944	30	3.28
Total gross premiums written (CZK bn)	122.1	132.9	139.9	7.0	5.23
of which: non-life insurance	74.9	78.8	82.9	4.2	5.31
life insurance	47.2	54.1	56.9	2.8	5.11
Total insurance penetration (%)	3.80	3.70	3.77	0.07	-

Source: CNB

The number of insurance contracts concluded corresponds to the trend in the development of insurance premiums. The number of contracts for life insurance stagnated, and almost the entire increase in concluded contracts occurred in non-life insurance. The life insurance portfolio was more affected by the unfavourable situation in the real economy. Due to an increased level of uncertainty, preferences were directed more toward insurance products compensating loss of employment, illness or injury. Life insurance contracts were not cancelled, but rather a slight diversion away from unit linked insurance in favour of traditional capital products was recorded. The savings component of unit linked insurance is typically invested into guaranteed funds or funds that lock in returns. At the same time, clients prefer products with a higher measure of flexibility, i.e. with the possibility to reduce or postpone premium payments in case their incomes should fall short.

In connection with the increasing business volumes, insurance companies have appropriately strengthened their capital facilities (by 3.3%) as well as the total amount of technical reserves (by 5.5%). This bears witness to a cautious approach with regard to an accumulating measure of risks. The financial placement structure of assets, the source of which is technical reserves, adheres to a conservative approach. The share of state guaranteed bonds or similar low-risk securities guaranteed by multinational institutions comprises over 50% of the total financial placement.

This sector's profitability in contrast to the extraordinary profits of recent years dropped by approximately 22%. Considering the current situation on the financial market, where returns from financial placement are decreasing, this amount still can be regarded as adequate and to not pose a threat to the sector's future development. The slight rise in employment (2.2%) also can be regarded as an indication of the sector's relative stability.

Despite the increased volatility of interest rates on financial markets, the maximum amount of the technical interest rate remained at 2.4%. For policyholders, this level represents the guaranteed share in returns from financial placement in the case of life insurance.

Increasing pressure from reinsurance companies, with which insurance companies are themselves insured, also has a considerable influence on insurance companies' business. Insurance companies, however, have not fully reflected the price increase for reinsurance

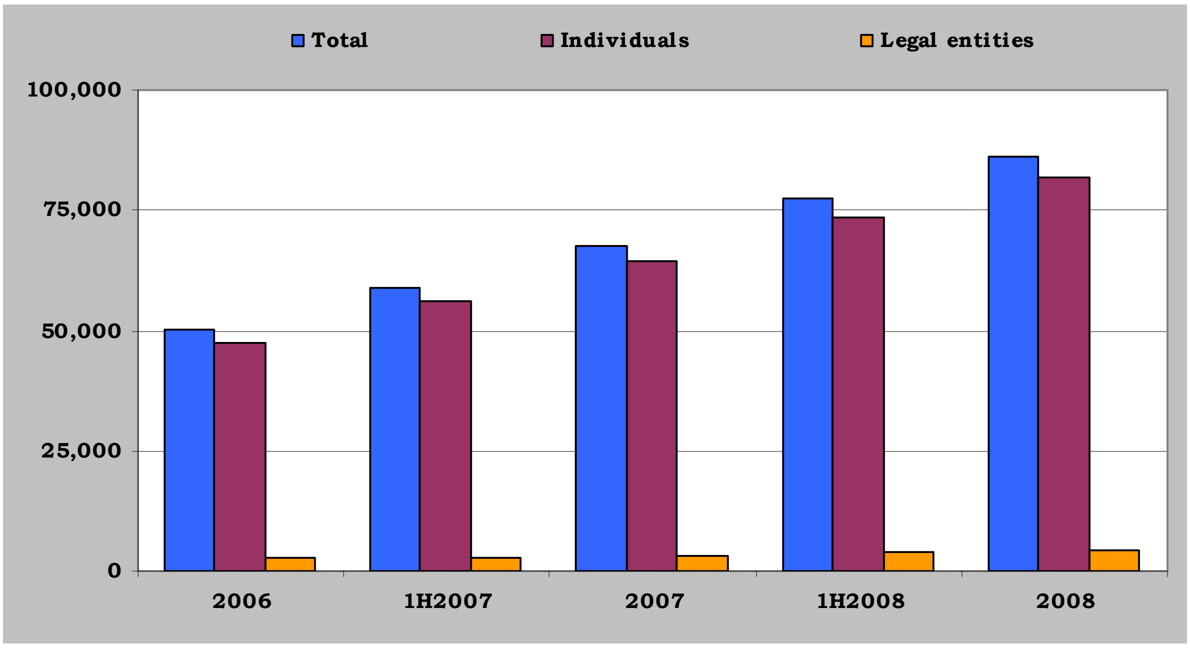
[39] The number of policies in life insurance does not include policies for additional insurance. The data does not include the Czech Insurers' Bureau (a professional organisation of insurance companies granted licence to operate liability insurance for operation of a vehicle).

premiums into the insurance rates for clients. Insurance companies are trying to partially compensate for the increased insurance claims by reducing their own margins.

In the insurance sector, 53 entities in total, of which 35 were domestic insurance companies and 18 were branches of foreign insurance companies (of which 17 were from EU countries), were in operation as at the end of 2008. As many as 554 insurance companies could operate in the Czech Republic under the so-called single European passport. A significant event for the institutional structure of the Czech insurance market was the founding of the first reinsurance company. VIG RE zajišťovna obtained a licence for reinsurance activities relating to both life and non-life insurance. The reinsurance company announced that it will provide reinsurance throughout the region of Central and Eastern Europe.

In connection with the troubles in the real economy, it is assumed that efforts could increase to offset unfavourable financial performance by unauthorised drawing of insurance claims. Insurance companies, therefore, are orienting their policies ever more distinctively toward verification in the liquidation of insurance claims for the purpose of detecting insurance frauds. In the past year, insurance companies invested large sums into systems to facilitate the detection of insurance frauds and for their prevention. Nevertheless, it is estimated that the proportion of fraudulent activity, especially regarding property insurance, is considerable. Estimates for motor vehicle insurance fluctuate in the neighbourhood of 35% of insurance settlements.

Graph 4.11: Development of the number of insurance intermediaries



Source: CNB

The increase in the number of insurance intermediaries continued, and their number exceeded 86,000 (an increase of 27.7%). At the same time, however, 7,252 entities had their licences to conduct intermediary activities withdrawn—in the overwhelming majority of cases at the intermediary's own request. Findings in practice indicate that a number of intermediaries do not perform this activity or they do so only occasionally. The majority of intermediaries are registered in the category "subordinated insurance intermediaries" (53.4%) or "exclusive insurance agents" (23.9%). Of the total number of foreign intermediaries, more than half are entities from Slovakia.

Table 4.23: Insurance intermediaries by position (category)[40]

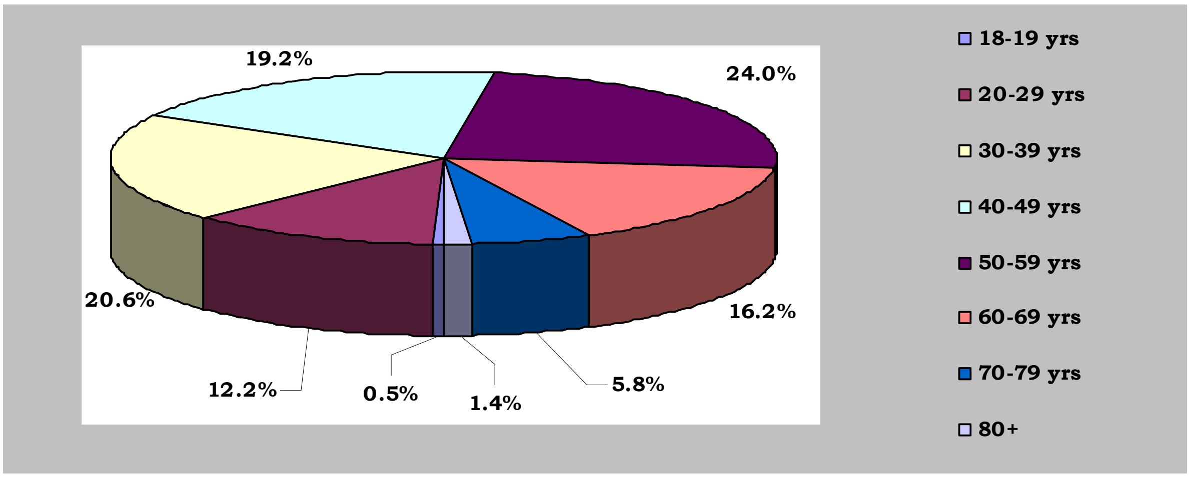
Entity registered as at 31 Dec	2006			2007			Year-on-year change (%)		
	IN	LE	Total	IN	LE	Total	IN	LE	Total
TIE	8,589	236	8,825	10,201	264	10,465	18.77	11.86	18.58
SII	33,726	1,126	34,852	44,692	1,375	46,067	32.51	22.11	32.18
EIA	16,726	89	16,815	20,477	124	20,601	22.43	39.33	22.52
IA	486	581	1,067	509	649	1,158	4.73	11.70	8.53
IB	146	453	599	161	497	658	10.27	9.71	9.85
ILA	55	91	146	62	103	165	12.73	13.19	13.01
FII	4,512	714	5,226	5,819	1,299	7,118	28.97	81.93	36.20
Total	64,240	3,290	67,530	81,921	4,311	86,232	27.52	31.03	27.69

Source: CNB

4.5. Supplementary pension insurance

The number of supplementary pension insurance participants continued to increase in the past year. Altogether, nearly 4.21 mn participants were registered in pension funds as at 31 December 2008. As annual growth dynamics slowed from 9.5% to 6.9%, the absolute increase in the number of participants reached 270,879. In total, then, participants' assets under management in pension funds reached CZK 186.7 bn.

Graph 4.12: Age structure of participants in supplementary pension insurance



Source: MoF

Looking at the age distribution of the year-on-year increase in participants, it is clear that the highest double-digit percentage increases were achieved in the highest age categories. In practice, the relationship between higher age category and higher relative growth in the number of participants is directly proportional. It can be expected here, however, that a considerable portion of the increase in participants in these categories is simply due to the transfer of participants into higher categories (i.e. their aging). Nevertheless, the number of participants aged 60 and older that save is relatively higher and this bears upon the setting of the product. After reaching the 60-year mark, supplementary pension insurance becomes a secure short- or medium-term savings tool with a state contribution. Among working-age participants, only the 30s category recorded more pronounced growth.

[40] Explanation: TII = tied insurance intermediary, SII = subordinated insurance intermediary, EIA = exclusive insurance agent, IA = insurance agent, IB = insurance broker, ILA = independent loss adjuster, FII= foreign insurance intermediary, IN = individual and LE = legal entity.

Table 4.24: Participants in supplementary pension insurance by age

As at 31 Dec	2005	2006	2007	2008	Year-on-year change	
					Abs.	(%)
18–19 yrs	12,522	16,513	21,461	22,526	1,065	4.96
20–29 yrs	368,952	420,387	475,887	512,496	36,609	7.69
30–39 yrs	601,614	686,156	786,781	867,574	80,793	10.27
40–49 yrs	705,074	735,250	777,167	807,665	30,498	3.92
50–59 yrs	931,001	966,952	996,474	1,010,509	14,035	1.41
60–69 yrs	452,878	530,932	610,778	682,601	71,823	11.76
70–79 yrs	173,965	196,484	218,919	245,558	26,639	12.17
80+	33,721	40,971	48,890	58,307	9,417	19.26
Total	3,279.7	3,593.6	3,936.4	4,207.2	270.9	6.88

Source: MoF

The number of supplementary pension insurance policies with employer's contribution has also increased. As at 31 December 2008, this category comprised a total 916,398 contracts, i.e. 21.8% of the total number of contracts. The number of contracts with managed employer contributions, of course, is still higher, having reached 1,635,722 contracts as at the same date.[41]

The number of contracts with currently paid employer's contribution increased by 6.3% year on year. In 2008, the volume of contributions paid by employers reached CZK 6.128 bn and thus significantly exceeded state contributions credited (CZK 4.920 bn). The average monthly employer's contribution thus stands around CZK 575.

Table 4.25: Share of policies with employer's contribution by age group and gender[42]

Age	2005	2006	2007	2008
18–19	358	344	459	461
20–29	76,948	81,412	83,203	86,224
30–39	178,118	200,425	218,108	238,090
40–49	214,432	230,051	242,993	257,048
50–59	249,926	267,726	279,464	290,310
60–69	22,452	29,757	37,468	43,315
70–79	489	658	756	907
80+	20	22	28	43
Total	742,743	810,395	862,479	916,398

Source: MoF

Table 4.26 shows a slight drop in the value of average monthly contributions of supplementary pension insurance participants to CZK 488 (not including employers' contributions), which represents a year-on-year decrease of 1.6%. In contrast, the average amount of the state contribution increased further to CZK 105.4. This is clearly caused by increase in the number of participants in the category with the lowest (i.e. zero) contribution (growth from 251,000 to 292,000 participants), who use supplementary insurance especially for employer contributions, and by a relative decrease in the number of

[41] Supplementary pension insurance policies with employer's contribution represent the current number of contracts to which employer contribute. The number of contracts with managed employer contributions cumulatively records the number of contracts under which an employer's contribution is sometimes paid.
[42] Data as at 31 December of the given year.

contributions in categories over CZK 500 per month (especially over CZK 2,500 per month), which increase the value of the average contribution but do not increase the average state contribution. It can be assumed that after introduction of the uniform income tax rate for individuals in the amount of 15% the tax deduction for contributions ranging above CZK 500 per month ceased to be attractive for certain participants falling under the previously upper tax bracket of 32%.

Table 4.26: Breakdown of average monthly contributions amount

CZK/month	2004	2005	2006	2007	2008
Contribution for old-age pension	385.3	399.3	406.4	414.1	394.9
Contribution for early-retirement pension	153.3	162.1	171.3	181.4	187.7
Participant's contribution	435.6	459.1	474.8	495.9	488.0
State contribution	99.6	100.8	103.6	104.0	105.4

Source: MoF

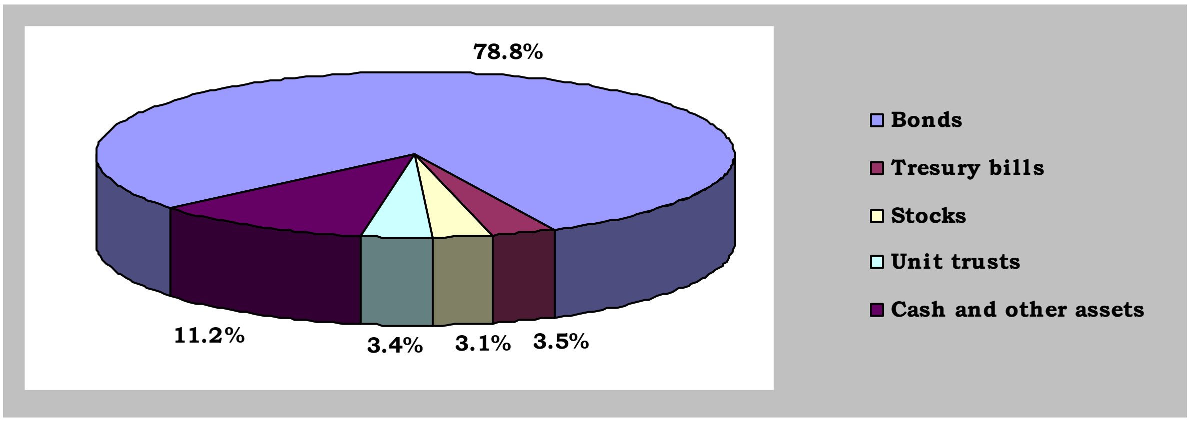
As in the case of collective investment funds, the pressure from developments on financial markets weighed on pension funds as well. Because of the accounting rules used in the supplementary pension insurance sector,[43] it still is possible to speak of appreciation gains in this area – even in a situation where practically all available assets recorded sharp drops in their values. Only the newest pension fund, which entered the market later and under different market conditions than other funds, declared a financial loss. In comparing the financial results of other funds with the previous period, two funds show a profit below CZK 10 mn, i.e. very much lower than in the previous year. The same picture can be seen on an aggregate level. While in 2007 the ten pension funds showed annual profit of CZK 4.3 bn, for 2008 they showed only CZK 718 mn.

The valuation differences, of course, sharply increased. While in 2007 they amounted to CZK -4.3 bn, as at 31 December 2008 they were CZK -8.2 bn. Four pension funds decided to increase their registered capital through shareholder contributions by a total of CZK 856 mn, and one did so repeatedly. According to data from The Association of Pension Funds of the Czech Republic, pension fund shareholders increased capital by a total of CZK 8.5 bn. As at the end of April 2009, only one pension fund had made public the amount of attributed appreciation in participants' funds for 2008.

The development of assets' prices was projected also into their structure within pension funds' portfolios. Compared to the end of 2007, the proportions decreased for shares (from 6.1% to 3.1%) and investment certificates (from 4.7% to 3.4%). The share in treasury bills diminished slightly (from 3.9% to 3.5%), while the share in bonds increased (from 73.7% to 78.8%).

[43] Pension funds value assets in fair values, but not through profit and loss statements. Revaluation is performed in the balance sheet using valuation differences (a component of shareholders' equity).

Graph 4.13: Allocation of assets of pension funds as at 31 December 2008[44]



Source: APF Czech Republic

[44] See table 8.5 in Appendix 2.

5. RELATION OF THE GOVERNMENT SECTOR TO THE FINANCIAL MARKET

5.1. General government balance

In 2009, as compared to 2008, the general government balance as a proportion of GDP will worsen significantly – from -1.5% to -4.5%. The cause of this negative development will be in unfavourable macroeconomic parameters, especially the slowdown of economic growth. The economy is especially influenced by negative external factors. The year-on-year decline in retail sales, marked year-on-year drop in foreign trade, and steep growth in unemployment also are gradually being reflected in the development of the government sector's income and spending. The anticipated temporary worsening of the general government balance is also caused by the government's extensive proposed or already implemented counter-crisis measures.

Upon a closer look at the structure of the general government balance, we find that the central government balance ended 2008 with a deficit (CZK -81.8 bn, i.e. -2.2% of GDP) while local government balances and social security funds, on the other hand, achieved surpluses (CZK 17.5 bn, i.e. 0.5% of GDP, and CZK 10.3 bn, i.e. 0.3% of GDP, respectively). The general government debt totalled CZK 1,105.8 bn (29.8% of GDP) at the end of 2008.

It is anticipated that in 2009 all government subsectors will be in deficits. The greatest deficit is predicted for the central government balance (CZK 144.9 bn, i.e. 3.9% of GDP), and deficit also is expected for the local government balance (CZK 21.6 bn, i.e. 0.6% of GDP). The social security funds will be almost in balance (CZK -0.5 bn). The fiscal results of the central government balance already reflect the aforementioned slowdown in economic growth, which is evidenced by a slump in all kinds of tax revenues.

In addition to the worsening economic development, the changes in tax legislation are projected on the revenue side of the general government sector. The changes were made in relation to implementing public finance reform that had begun in 2007 and also in relation to the so-called counter-crisis measures. The first group of measures includes the cancellation of limitations on the eligibility of financing costs and narrowing of the corporate income tax basis, which occurred by means of a tax exemption on the so-called manipulation fees collected by companies operating fixed-odds betting. With regard to the personal income tax, further reduction of rates was abandoned (remained at 15%), but this step was nevertheless more than compensated by decreasing the social security rate by 1.5 percentage points for employees (CZK 18.4 bn). For self-employed persons, this rate has been decreased by 0.4 percentage points.

On the expenditures side, these reform measures include in particular an amendment to the Pension Insurance Act decreasing the amount of the price growth criterion for valorisation of pensions and a change in the Health Insurance Act.

The second group of measures related to the so-called first counter-crisis package includes especially steps on the expenditures side in the form of one-time increases in the capital of the Czech Export Bank, Export Guarantee and Insurance Corporation, Czech-Moravian Guarantee and Development Bank (CZK 2 bn),[45] and the Support and Guarantee Agricultural and Forestry Fund (CZK 0.3 bn); an increase in investment incentives for technology centre projects (CZK 0.6 bn); support to projects co-financed using EU funds and focused on improving the environment (CZK 0.5 bn); maintaining the contribution for construction and modernisation of transport infrastructure realised by the State Fund for Transport Infrastructure in the amount of CZK 14.4 bn; and increasing the salaries of state employees (CZK 2.3 bn). The total impact of these measures on the general government balance in 2009 is expected to be CZK 37.2 bn.

[45] Due to the nature of this financial operation (increase in ownership interest), the government balance is not affected.

Another group of realised measures was approved by the government in January this year. The most important of these aims to decrease the budget deficit and includes the involvement of funds from unrealised expenditures of previous years, in the amount of ca CZK 32 bn, that are transferred to the revenues of the state budget as compensation for anticipated tax shortfalls. Due to the fact that this only involves a transfer of funds that the general government received in the previous years, these funds are not regarded as income under the ESA 95 methodology. The funds are intended for financing budget expenditures. At the same time, this package of measures contained expenditure cuts in the amount of CZK 6.5 bn. These cuts, however, are compensated by the transfer of remaining funds from reserve funds. Beyond the framework of the approved state budget expenditures, the government also approved expenditures for providing subsidies to the Support and Guarantee Agricultural and Forestry Fund (CZK 2 bn), covering currency losses from EIB tranches for construction of the Masaryk University in Brno (CZK 0.3 bn), and financing of direct payments to farmers (CZK 0.5 bn).

Furthermore, the prediction takes into account the so-called second counter-crisis package which contains a decrease in taxation of selected services with a high labour content. More specifically, this concerns the inclusion of restaurant services into the reduced VAT rate or keeping renovations and repairs of private apartments and residential buildings at that rate (impact of CZK 3.2 bn). The most important measure considered in the prediction, however, is that of the amendment to the act on social security which introduces discounts on social security premiums and a contribution to the state employment policy for employees whose income is less than 1.15 times the average salary (CZK 18 bn).

In 2009, income from privatisation (income from sale of shares and other ownership interests) is anticipated in the total amount of CZK 5.6 bn. This includes especially income from the sale of ownership interests in the joint-stock companies ČSA, Strojimport and Technoexport. The privatisation of Prague Airport cannot be considered as the legislative steps are currently ongoing. Another source of revenues associated with the state ownership interests are represented by dividends, which in the current forecast are considered in the amount of CZK 15.3 bn (CZK 15 bn – ČEZ, CZK 0.1 bn – ČEPRO, CZK 0.1 bn – MERO ČR). The revenues from privatisation in 2009 should be used especially for fixing environmental damages and losses caused by coal mining, for flood-protection measures, and for a subsidy to the State Fund for Transport Infrastructure and to Hyundai Motor Company.

In 2009, the general government debt will total CZK 1,228.3 bn, which represents 33.3% of GDP and thus means a year-on-year increase by 3.5 percentage points. Its growth dynamics hence have begun to accelerate after quite a long period of stable development. Included into the government debt are state guarantees, the purchase of Grippen fighter planes, and the imputation associated with the toll-gates and purchase of shares in ČEPS in the amount of approximately CZK 33.1 bn (i.e. 2.7% of government debt).

The greatest part of the government debt is in the form of debt securities, and the process of securitising the debt is ongoing. The portion of loans in the government debt has recorded a continuous decrease since 2001.

5.2. State budget

The state budget for **2008** was approved with a deficit of CZK 70.8 bn. Total expenditures were expected in the amount of CZK 1,107.3 bn and revenues in the amount of CZK 1,036.5 bn. The actual expenditures totalled CZK 1,083.9 bn and revenues CZK 1,063.9 bn. The state budget balance thus resulted in a deficit of CZK 20 bn.

The higher-than-expected **revenues** were due especially to increase in so-called non-tax and other revenues that reflect, among other things, transfers from reserve funds which reached CZK 55.6 bn in 2008. Tax revenues fell short by CZK 8.5 bn compared to the approved budget. Expectations for indirect taxes remained unfulfilled (VAT by CZK 14.1 bn and excise taxes by CZK 9.3 bn), as did social security insurance (by CZK 1.6 bn). By contrast, a better-than-budgeted collection was achieved in income taxes (PIT by CZK 4.8 bn and CIT by CZK 9.3 bn). Under the methodology for compiling the state budget, state budget revenues include transfers from reserve funds, which totalled CZK 55.5 bn in 2008. Moreover, the state budget revenues include a transfer from the state guarantee fund in the amount of CZK 4.9 bn. Under international methodologies, these cannot be regarded as revenues for the current year because they were already recorded as revenues in the past. Therefore, after their exclusion, the revenues side of the state budget developed more poorly than anticipated by the approved budget. The pension insurance system, however, finished the year with a surplus of CZK 9.9 bn, which was transferred to the reserve account for pension reform. The negative trend in drawing transfers from the EU continues, amounting to CZK 34.5 bn (including transfers from the National Fund), which is only 45.7% of the amended budgeted amount. The state budget revenues also include transfer of the liquidation balance of the Czech Collection Company in the amount of CZK 2 bn. The total state budget revenues net of these transfers amounted to CZK 993.1 bn.

Unrealised revenues from the EU also caused a considerable decrease of subsidy and transfer payments from the state budget. The structure of **expenditures** divided into current and capital remained almost unchanged in a year-on-year comparison. The proportion of mandatory expenditures relative to total expenditures grew by 2.9 percentage points. The total volume of state budget expenditures is greatly influenced under the state budget compilation methodology by the discontinuation of transferring undrawn funds for budgeted expenditures into reserve funds. The state organisation units now are able to claim the unspent expenditures of the previous year in the current year, thus exceeding the expenditures budgeted for the current year. This change significantly complicates the comparability of the year-on-year data published on the state budget results in the state budget compilation methodology. In 2007, transfers of unspent expenditures into the reserve funds of state organisational units totalled CZK 79.2 bn, and these expenditures were fully reflected in the state budget expenditures under the state budget compilation methodology. Nevertheless, the state budget expenditures, following the aforementioned change in the budgetary rules, are not affected by the transfer in the amount of CZK 72 bn (the amount of claims). In 2008, furthermore, the state guarantee fund was cancelled.

The **total state budget balance** net of transfers from/to state organisational units' own funds amounted to CZK 80.4 bn.

The state budget proposal for **2009** was submitted to the Parliament with a deficit of CZK 38.1 bn (i.e. by CZK 32.7 bn less than was anticipated in the approved budget for 2008). The budget was drawn up to have total revenues of CZK 1,114.0 bn (i.e. 7.5% more compared to the approved budget for the previous year) and total expenditures of CZK 1,152.1 bn (i.e. a year-on-year increase of 4%). State budget revenues and expenditures were proposed so as to enable the achievement of a general government balance at 1.6% of GDP (under the ESA 95 methodology).

Currently, state budget revenues and expenditures are expected in the amount of CZK 974.6 bn (i.e. by CZK 139.4 bn less), being influenced by the aforementioned measures, while under the state budget compilation methodology they are expected in the amount of CZK 1,142.8 bn (i.e. by CZK 9.3 bn less).

Most of the aforementioned measures are reflected on the revenues and expenditures sides of the state budget. The expected tax shortfalls, however, have a fundamental influence on the development of the state budget. In comparison to the approved budget, lower tax collections will probably be realised: value added tax by CZK 21.1 bn, excise taxes by CZK 16.7 bn, corporate income taxes by CZK 30.7 bn, and personal income taxes by CZK 36.7 bn. The budgeted revenues from property taxes, too, are likely to be under-fulfilled (by CZK 1.4 bn).

Table 5.1: Development of state budget revenues, expenditures and balance[46]

As at 31 Dec (CZK bn)	2004	2005	2006	2007	2008	2009	Year-on-year change (%)
Revenues incl. repayments	763.2	819.7	865.4	965.3	993.2	974.6	763.2
Expenditures incl. gross borrowings	832.2	880.7	972.8	1,013.9	1,073.6	1,142.8	832.2
Balance	-69.0	-61.1	-107.4	-48.6	-80.4	-168.2	-69.0

Source: MoF

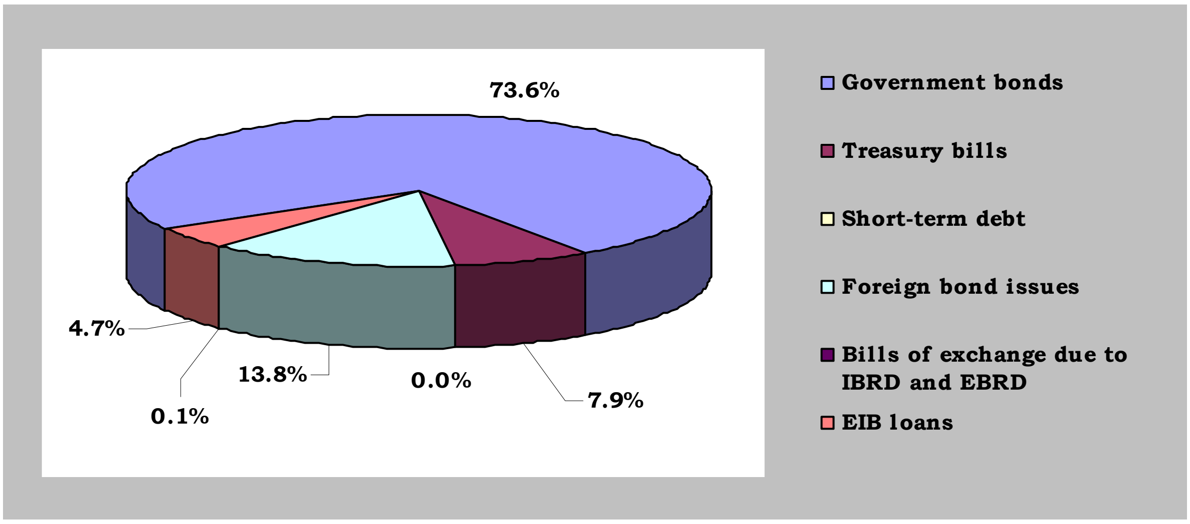
5.3. Government debt and state guarantees

At the end of **2008**, the unconsolidated state debt was recorded in the amount of CZK 999.8 bn, and it is anticipated to rise to CZK 1,108.8 bn as at the end of 2009. Its proportion of GDP will reach 30.0%. The volume of internal state debt will grow to CZK 860.2 bn (77.6%), while the volume of external state debt will reach CZK 248.6 bn (22.4%).

The rise in government debt is especially due to the state budget deficit, though its growth dynamics have slowed gradually since 2003. From 2009, however, they will begin to accelerate once again.

In the first quarter of the year, in the area of foreign financing, two tranches of EIB loans were drawn in a total amount of CZK 0.7 bn (i.e. 4.4% of this type of financing approved by the State Budget Act). In the area of domestic issuance activity in this period, medium-term and long-term bonds were issued in the nominal value of CZK 66.0 bn, of which CZK 17.7 bn was sold on the secondary market (using of 52.8% of the approved annual maximum limit for domestic issuance activity). In the given period, the remaining part of the principal amount of the 42nd issue of medium-term government bonds (CZK 37.9 bn) was paid and government bonds (CZK 10.6 bn) were redeemed. The net issuance of government bonds in the first quarter thus was CZK 17.5 bn.

Graph 5.1: Government debt by type of instrument as at 31 December 2008



Source: MoF

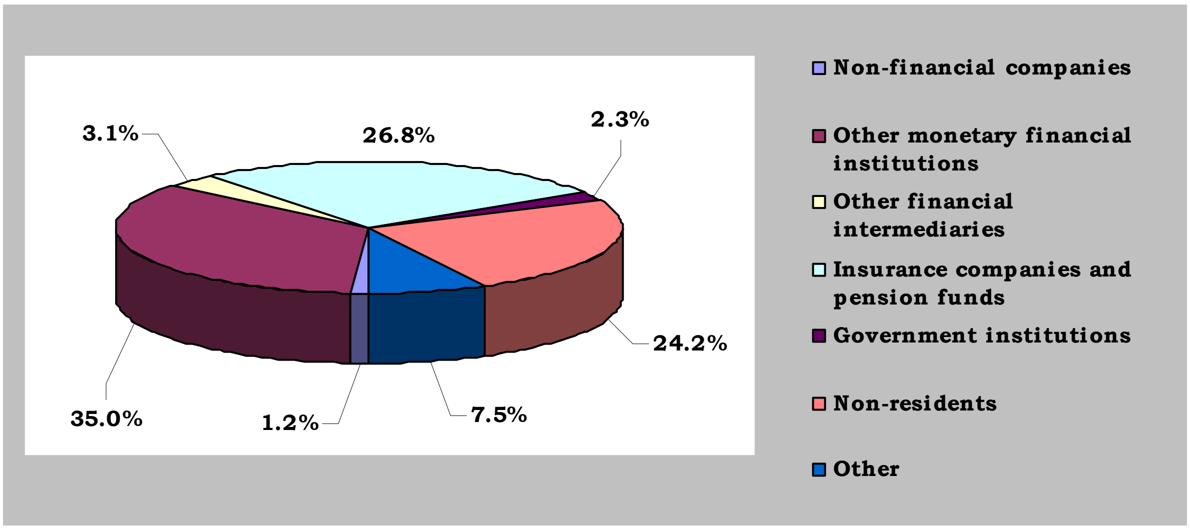
[46] In contrast to the budget documentation, the revenues and expenditures in this time line are reduced by interest income and premiums from the government debt (i.e. the consolidation of the costs of debt service). This operation does not affect the government budget balance.

The average maturity of the government debt thus recorded an increase to 6.8 years as at the end of the first quarter. Net costs of servicing the government debt amounted to CZK 7.3 bn for the same period.

As at the end of the first quarter, of the total value of government debt, CZK 952.2 bn was in the form of tradable debt and CZK 48.3 bn in untradeable debt. The proportion of foreign currency debt was 4.9%. The proportion of short-term government debt decreased as compared to the previous year by 6.5 percentage points to 11.2%.

In 2009, the value of the portfolio of high-risk state guarantees, which are refinanced within the state budget expenditures, has decreased further. Their significance in relation to the value of the state debt fell below 6%, and their structure therefore cannot more significantly skew the monitored quantitative criteria away from the announced target values.

Graph 5.2: Government debt by creditor as at 31 December 2008

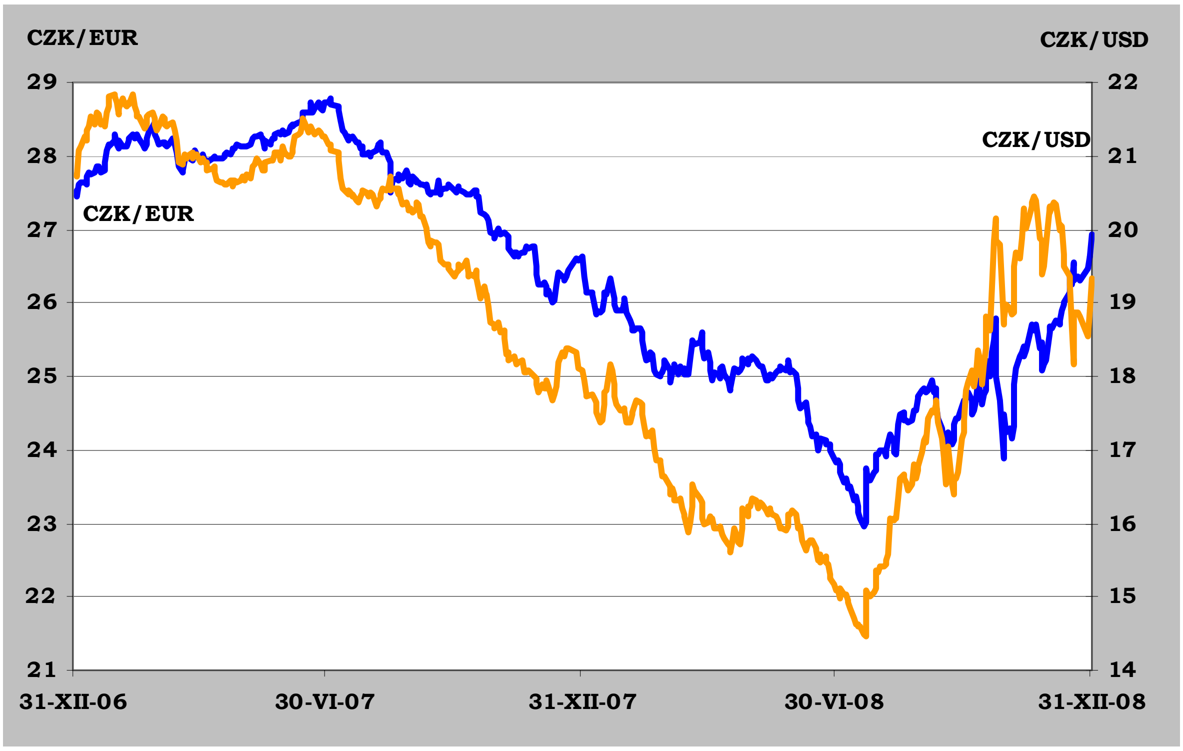


Source: MoF

6. FOREIGN EXCHANGE MARKET

From the start of the year, the Czech currency strengthened rapidly to 22.97 CZK/EUR and 14.45 CZK/USD, primarily due to the relatively lower influence of the financial crisis on the Czech economy. From August, however, when the crisis spilled over into Central and Eastern Europe, the Czech crown began to weaken rapidly. At the end of the year, it was trading at 26.93 CZK/EUR and 19.35 CZK/USD.

Graph 6.1: CZK exchange rates relative to major currencies



Source: CNB

In the first half of 2008, the Czech crown became one of the most rapidly strengthening currencies in the world, increasing in value by 10.2% against the euro and by 16.2% against the US dollar. In the second half of the year, on the other hand, it sharply weakened, losing 12.7% in value against the euro and 27.6% against the US dollar at the end of the year compared to the middle of the year.

Table 6.1: CZK exchange rates relative to major currencies

	Average exchange rate					
	2004	**2005**	**2006**	**2007**	**2008**	**Year-on-year change (%)**
CZK/EUR	31.90	29.78	28.34	27.76	24.94	-10.16
CZK/USD	25.70	23.95	22.61	20.31	17.04	-16.12
	Exchange rate as at the end of					
	2004	**2005**	**2006**	**2007**	**2008**	**Year-on-year change (%)**
CZK/EUR	30.47	29.01	27.50	26.62	26.93	1.16
CZK/USD	22.37	24.59	20.88	18.08	19.35	7.01

Source: CNB, CZSO

The cause of these significant changes was in the responses of investors to the developing financial crisis. In the first half of 2008, the Czech currency was sought after by investors because the Czech economy, like Central and Eastern Europe in general, was less affected by the impacts of the financial crisis. After the Baltic states as well as Hungary and

Romania encountered difficulties in the middle of the year, however, the view of investors changed for the entire region. Due to the fact that a great number of investors regarded Central and Eastern Europe as an integrated whole and did not distinguish between individual countries, the entire region lost their confidence. They thus began to sell regional currencies, and that was reflected in a sharp and unsubstantiated weakening of the Czech currency.

Table 6.2: External financial relations

Anual (CZK bn)	2004	2005	2006	2007	2008
Trade balance	-13.4	59.4	65.1	117.5	103.2
Payment balance – current account	-147.5	-48.5	-100.8	-89.0	-113.9
Payment balance – capital account	-14.2	4.7	8.5	19.7	31.0
Payment balance – financial account	177.3	154.8	104.9	104.5	151.2

Source: CNB - ARAD

Albeit with high exchange rate volatility in 2008, the local currency strengthened on average by 10.2% to the euro and by 16.1% to the US dollar. Despite the local currency's strengthening exchange rate, the trade balance surplus approached the record-breaking level of 2007. The rise in the price level gradually slowed during the year. The central bank's interest rate was decreased more slowly than in the USA (where it was reduced similarly as in the eurozone). Such data, which usually leads to strengthening of the local currency, still could not reverse investors' negative attitude toward the Czech crown in the second half of the year.

Table 6.3: Comparison of economic indicators

(%)	Inflation (year-on-year)			Key interest rate of central bank[47]		
	Czech Republic	Eurozone	USA	Czech Republic	Eurozone	USA
January 08	7.5	3.2	4.3	3.50	4.00	4.25
February 08	7.5	3.3	4.0	3.75	4.00	3.00
March 08	7.1	3.6	4.0	3.75	4.00	2.25
April 08	6.8	3.3	3.9	3.75	4.00	2.25
May 08	6.8	3.7	4.2	3.75	4.00	2.00
June 08	6.7	4.0	5.0	3.75	4.00	2.00
July 08	6.9	4.0	5.6	3.75	4.25	2.00
August 08	6.5	3.8	5.4	3.50	4.25	2.00
September 08	6.6	3.6	4.9	3.50	4.25	2.00
October 08	6.0	3.2	3.7	3.50	3.75	1.50
November 08	4.4	2.1	1.1	2.75	3.25	1.50
December 08	3.6	1.6	0.1	2.25	2.50	0.25

Source: CZSO, CNB, Eurostat, ECB, Fed

[47] CR – 2T repo rate of CNB, eurozone – ECB's main refinancing operations (minimum bid rate, or fixed rate), and USA – the Fed's intended federal funds rate.

7. FINANCIAL AND ECONOMIC CRISIS

The first problems in the USA appeared on the mortgage market in March 2007.[48] Their immediate cause was mortgages for less-creditworthy clients (the so-called subprime market) and an overly benevolent approach by banks in providing loans to these clients. After a period of relatively low interest rates, however, the Fed began to raise rates due to increasing inflationary pressures. This led to a rise in interest rates on mortgages and, therefore, on their payments. The less-creditworthy debtors thus got into repayment difficulties.

Securitisation of assets became a transfer mechanism for spreading the losses and uncertainty to the global financial market.[49] Securitisation enabled credit institutions to remove risk from their balance sheets at a time of surplus liquidity on world markets through the sale of securities using financial innovations. However, the risk was thereby only transferred onto the balance sheets of financial institutions worldwide across all financial market sectors. Due to the decrease in the credit quality of the portfolio and the revaluation of risk, however, the value of the securities tied to problematic assets (for example, mortgage loans) decreased dramatically.

The increasing uncertainty as to who had suffered which losses subsequently contributed to the decline in mutual trust among banks. Mutual distrust began to spread among them, they lost confidence in one another, and they stopped lending to each other (liquidity crisis in the interbank sector). In an extreme case, this situation could have led to a collapse of not only the entire banking sector but also of the financial market. To avert this threat, central banks worldwide released the equivalent of hundreds of billions of US dollars for commercial banks to borrow if they needed temporarily to increase their liquidity. The central banks thus are trying to substitute for the liquidity function of the interbank market.

A liquidity crisis may have negative impacts on the economy, as even healthy (solvent) banks can encounter difficulties due to a loss of liquidity. Moreover, there is a danger that the problems will spill over into the commercial sphere if otherwise long solvent firms were unable to obtain loans for financing their regular activity or to cover their existing maturing loans with new loans in a standard way.

What was originally only a financial market crisis over time became a crisis of the entire US economy. The related drop in consumption by US households also was projected into the demand for imported goods. The countries that are the main trading partners of the USA thus encountered problems in their export sectors. Due to the importance of the US economy for the development of the global economy, the problems in the USA were transferred to other countries as well. Economic growth gradually slowed, or in some cases fell, in the eurozone as well as in the rest of Europe, in Russia, and in China. The IMF in its April report for 2009 estimates the rate of GDP decrease for the world economy at -1.3%.

Considering the aforementioned risks threatening the very functioning of the world financial and economic system, and due to other impacts on the real economy, numerous monetary and economic policy measures were taken.

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[48] Certain important events of the current financial crisis happened before and also after the period under review in this report. Due to their complexity and interconnection, however, it is useful to monitor this development in a wider time frame beyond just the year 2008.

[49] In carrying out securitisation, mortgage institutions (primary providers of loans) sold huge packages of mortgage loans whereby they also got rid of the risks associated with these loans. The financial institutions (mostly large investment banks) that purchased these packages of mortgage loans then issued securities whose value and returns were covered by the cash flows from the aforementioned mortgages. After transforming the mortgage loans into securities, these were bought by various investors from all over the world also for the high ratings that these securities obtained from credit rating agencies.

7.1. Monetary and economic policy measures

Major central banks all over the world began to **decrease their interest rates**. ECB cut its key interest rate to 1% (in May 2009), the Fed (the American central bank) to the 0.00–0.25% range (in December 2008), and the Bank of England to 0.5% (in March 2009). After the rates of certain central banks almost reached zero, some central banks began to implement **less conventional measures**. The Fed as well as the Bank of England started buying up their countries' government securities. This results in a similar approach to that applied by the Japanese central bank within its policy of so-called quantitative easing. If the current tendency toward deflation persists, these steps may be taken without significant proinflationary impacts.

Liquidity support to financial market entities aims to renew confidence in the banking sector and thus prevent a shock-induced drop in credit activity. At the same time, many of the measures contribute to maintaining the solvency of viable or systemic financial market entities. To support liquidity, the types of assets accepted as collateral by central banks to finance commercial banks and other financial market entities were expanded. Government loans to banks and government guarantees on loans provided on the interbank market are other means to calm markets and restore confidence. In addition, central banks (especially the American Fed) introduced programmes for purchasing specific assets to support activity in the areas of lending to households and non-financial enterprises.

Another measure focuses on **removing impaired assets from banks' balance sheets**, as the losses from these assets, which are difficult to estimate, may sustain the persisting uncertainty in the banking sector and thus limit credit issuance. In relation to this, two basic procedures are discussed. The first involves the purchase of toxic assets by the state into a special institution (*bad bank*), which in the Czech context can be compared to the former Czech Consolidation Agency. The second alternative is a programme for mitigating the impacts of impaired assets (*asset protection scheme*), which represents a form of government insurance against potential high losses resulting from these problematic assets. A form of partnership between the private and public sectors was selected in the USA whereby the state will encourage private entities to purchase the impaired assets.

State ownership of banks is an approach taken especially in situations when it is necessary to quickly boost the capital of the affected institutions and this recapitalisation cannot be performed by private entities. The so-called nationalisation, i.e. the injection of cash into an affected bank in exchange for obtaining an ownership interest, was carried out for example by governments in the USA, Belgium, Great Britain, and Iceland. The possibility to subsequently sell the ownership interest in a stabilised financial institution provides a potential for compensating previous public expenditures that may not exist, for example, in the case of purchasing impaired assets. On the other hand, there is a risk of inappropriate state interference in the business activities of these entities.

Increasing government guarantees for bank deposits aims to increase depositors' confidence in the banking system and to prevent mass withdrawals of deposits. Nevertheless, and especially in the eurozone, the steps taken by individual states led to avalanche-like announcements of unlimited government guarantees under the threat of deposits flowing out to economies with higher guarantees. The political motives rather than actual necessity behind these measures are often debatable in certain economies. Subsequently, the EU Member States ultimately agreed on a coordinated measure in this area.

In implementing the measures, it may be **difficult to distinguish** between unhealthy entities and those that were affected by the crisis only in a secondary way. Moreover, the risk of **moral hazard** increases, as there is the danger that entities may take greater risks in future because they will not expect to fully bear the potential losses. This results in the privatisation of previous banking profits and subsequently to the socialisation of losses. The expenditures necessary to perform these state measures in the end are always paid by the taxpayer. In cases of certain economies, the transfer of risks and losses from the balance sheets of private entities into public budgets also may result in rapid growth of public debt as a proportion of GDP. Recommendations for fiscal prudence should be taken into consideration also for the reason that even with a constant rate of indebtedness problems may occur in relation to refinancing the government debt of economies considered by investors as more risky.

Systemic risk, i.e. a situation in which a fundamental **weakening of the functioning of the financial system could threaten the real economy**, may represent **an argument for** the aforementioned **interventions**. Therefore, the potential losses from government support to banks may pay off for taxpayers by supporting economic performance.

Fiscal spending programmes comprise a tool intended only to support the real economy rather than the financial sector. The conditions for their success are their optimum targeting on the most appropriate areas and subsequently their successful implementation. The impacts of these measures on the financial sector are rather indirect, and these effects take the form of a (potential) boost to the real economy and the resulting improved abilities of banks' clients to fulfil obligations from loans that have been provided. A direct impact on the financial sector can be seen in the increased need to market the government securities issued to finance these programmes.

7.2. Situation in financial markets

Nevertheless, the aforementioned measures were not sufficient to avert the panic that affected financial markets worldwide, taking its most intensive form from September 2008. Collapse of the most important investment banks set off the problems of the entire US banking sector and led to fundamental change in the financial market. Five of the largest investment banks ceased to exist in their original form. Bear Stearns and Lehman Brothers collapsed, Merrill Lynch was saved by being taken under the wings of Bank of America, and Goldman Sachs and Morgan Stanley requested the Fed that they be transformed into bank holdings. Washington Mutual, the largest US savings company, collapsed and the Fed took over control of the AIG insurance company. Important government support was also directed to other key entities, such as Citibank, Royal Bank of Scotland (Great Britain), and Hypo Real Estate (Germany).

Subsequently, the problems spread all across Europe. The governments of Great Britain, the Benelux countries, Sweden, and other countries acquired interests in the problematic banks. Iceland nationalised all large banks and is on the verge of state bankruptcy. Hungary received international credit assistance to avert difficulties in the private as well as government sectors that are dependant on foreign loans. Decisive steps were taken to allow Latvia and Romania to receive assistance.

Thus, stock market titles from the financial sector (banks, insurance companies) came under selling pressure first. The worsening of the economic situation, especially in the USA and eurozone, caused the prices of other titles also to decline. The slowdown of economic growth reduced the demand for commodities (the price of oil had fallen markedly below USD 50 per barrel as at the end of the year). The markets continued to be highly volatile in the first quarter of 2009. Losses recorded by investors during the first months of the year were nevertheless compensated to a great extent by later increases in the values of the exchange indices.

After the market shock in the autumn of 2008 in relation to the collapse of the investment bank Lehman Brothers, the situation on monetary markets calmed down due to the interventions. The TED spread, an indicator of nervousness on interbank markets that is calculated as the difference between the money market rate and the yields of US government bonds, has stabilised around 100bp since February 2009. In October 2008, the spread had reached record-breaking values, exceeding 450bp in the short term.

However, the adverse effects associated with the slowdown of the real global economy and the related worsening in the quality of credit portfolios will continue to be apparent. World financial institutions, therefore, are (and will be) affected by additional waves of losses. In April 2009, the International Monetary Fund estimated these losses to reach USD 4.1 trillion.

7.3. Implications for the Czech Republic

Czech financial institutions have not been directly affected by the financial crisis. Their exposures to products containing securitised subprime mortgages and other impaired assets are very low, on the order of tenths of a percentage point of assets. Nevertheless, in the context of the globalised world economy, the real economy of the Czech Republic still has experienced indirect impacts.

The Czech Republic has a small, export-oriented economy. The Czech economy thus was affected by the decrease in foreign demand from its main trading partners. In its analysis from April 2009, the IMF estimates a decrease in GDP for 2009 by 4.2% in the EU, and in Germany even by an unprecedented 5.6%. For the Czech Republic, therefore, it is not the world financial crisis but primarily the economic crisis that is relevant as it spills over into the Czech Republic through the drop in demand for Czech goods from the ailing economies of its trading partners. Thus, we see that some industries show decreases in production and employment. This is subsequently reflected in the reduced ability of certain non-financial enterprises and households to fulfil their obligations and in a moderate worsening in the quality of banks' credit portfolios. Nevertheless, these represent secondary impacts of the overall economic slowdown and not a direct financial crisis. Subsequently, the worsening of the economic situation will also be projected through this channel into the financial sector by a decline in profitability. This development should not impact depositors, but it may affect the amount of dividends paid to owners.

Confidence in the banking sector, which is high in the Czech Republic, was further supported by the increase in deposit insurance (100% for the equivalent amount of up to EUR 50,000, which at the current exchange rate corresponds to ca CZK 1.25 mn). To support liquidity in the banking sector, the Czech National Bank introduced so-called liquidity-providing repo operations on 15 October 2008. This monetary policy tool aims to enable commercial banks to obtain liquidity from the central bank using government securities as collateral. To date, however, commercial banks have not shown substantial interest in this instrument.

Like stock exchanges worldwide, the Prague Stock Exchange also was affected by a wave of selling. By the middle of October 2008, the PX index had lost more than 50% of its value from the beginning of the year. The development on the financial markets also has a strong influence on the yields of pension funds and collective investment funds.

The tightening of conditions and the increased costs of bank financing were first felt by real estate developers whose activities greatly depend on such financing. This has been reflected in the entire construction industry. Subsequently, as the financial crisis deepened, companies in other industries began to experience similar difficulties. The economic problems of major trading partners are reflected also in the demand for imported goods, and the export industries are thus also experiencing problems. The Czech economy in the second quarter of 2008 slowed, expanding by "only" 4%. In the following quarters, the growth rate continued to decelerate, reaching 2.9% in the third quarter and 0.7% in the fourth quarter year on year. For 2009, GDP is expected to decrease by 2.3%.[50]

[50] Macroeconomic Forecast (April 2009).

7.4. Misleading inclusion of the Czech Republic into CEE region

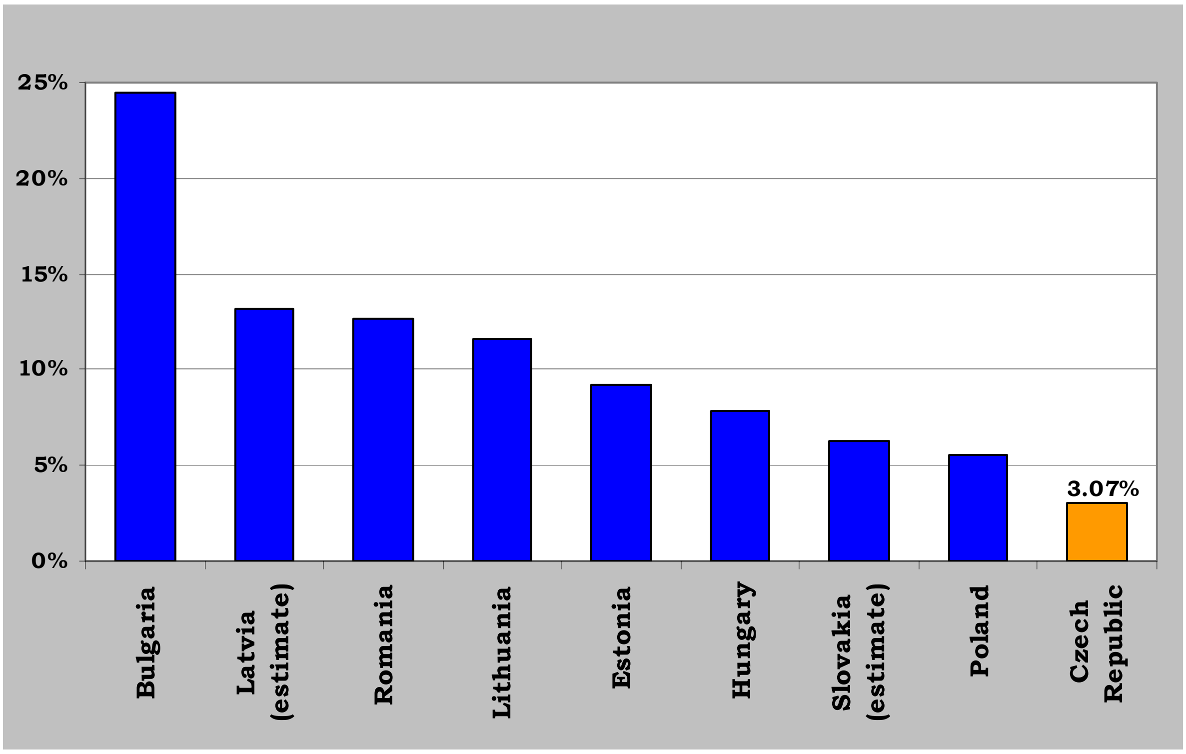
In relation to the development of economies in Central and Easter Europe (especially in spring 2009), the Czech Republic's economy and financial markets were misleadingly lumped into a vaguely defined group of countries in Central and Eastern Europe, or Central, Eastern and Southern Europe (hereinafter just "CEE"). Such inclusion thus could give the incorrect impression that the Czech economy suffers from similar problems, or problems in similar intensity, as certain other countries included in CEE.

Potential risks can be divided into several groups whereby it can be illustrated that **it is not appropriate to include the Czech Republic into this broadly defined CEE region**:

1. problems of external imbalance due to decreased availability of cross-border financing in foreign currencies,
2. problems due to decreased liquidity on interbank markets, and
3. problems due to a spread of foreign exchange-denominated borrowing among domestic entities.

(1) **Problems of external imbalance** concern other countries in the region much more so than the Czech Republic. **The Czech economy records more favourable results for the current account payment balance** and is therefore less dependent on the relatively volatile means of financing through debt financing flows. Additionally, some economies in the region have based the financing of their payment balances on the inflow of direct foreign investments in a cyclically very unfavourable structure which, in Bulgaria for example, resulted in an unprecedented construction and real estate boom. For the aforementioned reasons, the Czech Republic is less prone to be inflicted by economic problems through this channel. Graph 7.1 below shows the already mentioned low level of the current account deficit relative to GDP in the Czech Republic in comparison to other countries in the region.

Graph 7.1: Current account deficit relative to GDP in 2008



Source: International Monetary Fund

(2) Similarly, the situation in the Czech banking sector differs from that in other countries of the region. **Czech banks finance their activities mainly through deposits from clients** and **do not depend to such extent** as in other countries **on interbank loans**. This is consequently reflected in a greater stability of the banking system during more volatile times. This situation can be illustrated using the ratio of the volume of client deposits to that of client loans, which is extremely high in the Czech Republic. As can be seen from Graph 4.1, as at 31 December 2008 client loans were covered by deposits in the Czech Republic by more than 130%. By contrast, in Latvia for example, this ratio was only some 41%.

(3) Another advantage of the Czech Republic and the Czech banking sector is the **low significance of indebtedness** (especially of households) **denominated in foreign currencies**. At the end of 2008, the total share of loans in foreign currencies comprised 14.1% and **household indebtedness in foreign currencies** was only **0.1%**. Any weakening of the local currency permits Czech exporters to increase their competitiveness on world markets without burdening households, due to their low level of debts in foreign currencies.

Hence, the situation in the Czech economy and Czech financial sector differs very significantly from the situation in the rest of the region. Inclusion of the Czech Republic into a broadly defined **"high-risk" CEE region** is therefore a practice that is **very inaccurate and misleading from an economic perspective**.

8. FINANCIAL MARKET ACTIVITIES OF MOF

8.1. Ministry of Finance's activities on an international level

A well-functioning financial services sector and efficient markets are among the basic preconditions for a healthy economy on a national, European, as well as global level. An internal market with well-regulated financial services that is sufficiently stabilised by the legal framework but nevertheless dynamic provides entrepreneurs easier access to the capital needed for further investments and, at the same time, enables consumers to safely earn returns on their savings. It is precisely the financial services area, however, that remains highly fragmented on the European level, and so harmonisation of the respective legislation has commenced in this area within the European Union.

In this context, one of the most important tasks of the Ministry of Finance in relation to the development of the financial market was to prepare for and then perform its role within the Czech Presidency of the Council of the European Union in the area of financial services. Currently, the activity of the Ministry of Finance in this area significantly exceeds its regular activities, especially those related to creating primary supporting documents for the Prime Minister in relation to summits of the heads of the Member States or to the Czech delegation's participation in G20 meetings.

8.1.1. Czech Presidency of the Council of the European Union[51]

In the course of the Czech Presidency, the financial services sector became one of the key areas of interest for the European Communities, especially with regard to the ongoing financial and economic crisis that has resulted in a great number of legislative and non-legislative activities. These European Commission proposals, often politically sensitive, evoked great expectations from entities operating on the financial market and from the individual Member States. Moreover, the negotiations were carried out under time pressure caused by the concluding election period of the European Parliament and concluding term of office of the European Commission, as well as by the effort to respond to the financial crisis as soon as possible.

Legislative acts

During 2008, the Ministry of Finance monitored and closely cooperated on discussions about the agendas for individual sectors within the EU.[52] At the close of 2008, in the context of the status of discussions about these agendas, the priorities were set for the Czech Presidency in the first half of 2009.

The financial services sector represents one of the prominent areas in the main programme of the Czech Presidency, defined as a competitive and open Europe. The current as well as

[51] In 2008, the preparations for the Czech Presidency of the Council of the European Union were carried out, culminating in the presidency during the first half of 2009. With respect to the importance of the topic, this document discusses the preparation phase as well as the actual course of the presidency and the results it has achieved to date.

[52] The Ministry of Finance supports such initiatives that allow for easier provision of retail financial services and facilitate development of the European market in these services, while ensuring adequate consumer protection. In mid-2008, the priorities were the following: a directive on intermediating insurance, legislation related to intermediaries of loans, harmonisation in providing mortgage loans, revision of the directive on collective investment in transferable securities, increasing the efficiency of the functioning of the supervisory framework, the Solvency II project, revision of directives concerning capital requirements, regulatory dialogue with the USA, and revision of the markets in financial instruments directive. Moreover, roadmaps approved by the Economic and Financial Affairs Council (ECOFIN) in 2007 set the course to strengthening financial stability and ensuring efficient supervision over financial markets.

future planned European initiatives in this area focus on creating an open and secure internal market for retail consumers, further integration of certain non-retail financial services, and creating a corresponding regulatory framework. In this context, the Czech Republic strived to complete discussions at the European level especially about those legislative acts that are urgent in the European context, and especially with regard to the ongoing financial and economic crisis.

A main objective in the first half of the Czech Presidency in terms of legislation, therefore, was to reach an agreement between the Council and the European Parliament in three priority areas: regulation on credit rating agencies (CRA), a directive on the adequate solvency of insurance companies, and a revision of capital requirements directives (CRD).

The most complicated problem, with both European and global impacts, consisted in the regulation on credit rating agencies. As the presiding country, our aim was to contribute to legislation that will function properly in view of this field's global character. The contents of the regulation include especially conditions for registering the credit rating agencies in the European Union and rules for issuing ratings, for preventing conflicts of interests and for increasing the transparency of credit rating agencies. Rules for credit rating agencies from countries outside the EU that issue ratings used by financial institutions in the EU have now been introduced. A fundamental innovation is supervision over the activities of credit rating agencies in the EU based on creating colleges of competent supervisors which should allow for better coordination of supervision over rating agencies. The agreement reached in relation to the compromise text of the regulation is a significant step towards strengthening the transparency of financial markets.

The Solvency II directive was a clear challenge and a great opportunity to set international standards for insurance sector regulation. Following demanding and difficult negotiations within the EU Council as well as with the European Parliament, the Czech Presidency managed to complete the negotiations on this directive, which had been discussed at the European Union level for the past two years.

A high priority of the Czech Presidency was also the revision of CRD, which is a very good example of a concrete legislative response to the crisis. The amendment to the stated directive represents the first significant contribution to a thorough revision of the banking regulatory system with the aim to remove its main deficiencies revealed during the financial crisis. The amendment introduces stricter rules for large exposures (limits for receivables due from a single client) and greater harmonisation of hybrid capital instruments, and it substantially revises the regulatory framework in the securitisation area. Achieving the compromise regarding this document can also be regarded as a great success of the Czech Presidency.

Other important legislation discussed in 2009's first half includes a directive concerning e-money (regulates the issuing of electronic money and supervision over electronic money institutions) and a regulation concerning cross-border payments in euros. The existing regulation of electronic money did not allow for fully utilising the potential that electronic money has as an alternative payment method. In the negotiations on the e-money directive, therefore, the Czech Presidency aimed especially to remove the high regulatory barriers that hinder development of the electronic money market in the European Union and to establish adequate conditions for electronic money institutions to conduct their business activities. The Czech Presidency managed to achieve this objective. The new regulation concerning cross-border payments in euros will strengthen protection of consumer rights and support development of a modern and efficient payment system within the EU.

The agreed compromise texts of the mentioned legislative proposals have already been approved by the European Parliament, and following the necessary technical and linguistic adaptations they can be officially approved by the EU Council. The Czech Presidency thus succeeded to fulfil all the objectives established at the end of last year in the financial services area.

In January of this year, the European Commission submitted a proposal for implementing the Community Programme to support specific activities in the field of financial services, financial reporting and auditing aimed at supporting the EU policies in the respective areas. The Czech Presidency managed to achieve a compromise regarding this proposal, too. It has already been approved by the European Parliament, and, following the necessary technical and linguistic adaptations, it needs only to be officially approved by the EU Council.

Non-legislative initiatives

In the non-legislative area, at the beginning of its term of office the Czech Presidency focused on following up the measures adopted during 2008 to restore proper functioning of the financial systems and the confidence of economic entities. An urgent task of the Czech Presidency was to execute additional steps to strengthen the transparency and stability of the financial markets. Already at the first meeting of the ECOFIN Council gathered under the Czech Presidency, conclusions regarding banking capital were successfully adopted.

In 2008, as well as in the first quarter of 2009, the entire EU worked actively to adopt a coordinated response to the financial crisis. As a part of the strategy for ensuring financial stability agreed in October 2008, a common approach to impaired assets was discussed at the EU level. With regard to the complexity of this matter, it was necessary to closely cooperate with the European Commission and the European Central Bank to find an optimum approach for valuing the impaired assets and authorising institutions to participate in rescue schemes. In all the aforementioned cases, the Czech Presidency endeavoured to facilitate and accelerate the ongoing discussions in order to achieve maximum consistency in stabilising the economic and financial situation and to prevent negative secondary impacts. The ECOFIN Council agreed in February 2009 on common principles for dealing with impaired assets.

In the second half of the Czech Presidency, the main priority regarding the financial services sector has been reform of the structure of supervision over the financial market. The first discussion attended by the ministers of finance and governors of central banks of all 27 Member States was held at the beginning of April at an informal meeting of the ECOFIN Council in Prague. The ministers and governors agreed on the main principles for reforming financial market supervision in the European Union, especially on the necessity to strengthen supervision over macrofinancial stability at the EU level. For that purpose, they supported the creation of a new body – the European Systemic Risk Council (ESRC). As regards the reform on the supervision over individual financial market institutions, the ministers and governors acknowledged the necessity to harmonise the European supervisory framework. Among the tasks for the upcoming period thus will be to harmonise the powers of supervisory authorities and to strengthen their independence; to harmonise rules, standards and sanction powers among Member States; and also to strengthen and transform the Level 3 Lamfalussy Committees (CEBS, CESR and CEIOPS)[53] into new agencies with legal personality.

International coordination

Considering that financial markets and economies are ever more interconnected, the only possible solution for the current difficult economic situation is global coordination. During 2008, the financial and subsequently economic crisis became a truly global problem. The best possible platform for the aforementioned coordination became the G20. At their first meeting in November 2008 in Washington, the representatives of the G20 countries agreed on an action plan containing short-term as well as long-term measures to improve international financial regulations. The preparation works for the next meeting, which was held in London on 2 April 2009, were very intensive in the first quarter of 2009. Four working groups were established which dealt with such topics as the regulation and supervision of the global market in financial services.

[53] For more information on third-level Lamfalussy Committees, see Chapter 8.1.2. European and other international institutions.

The Czech Presidency sought to find a common position of all EU Member States at all levels for the negotiations within the G20. Decisive for the final agreement on a common EU position were the meeting of the ECOFIN Council on 10 March 2009 and the meeting of the European Council on 19 March 2009 at which the European mandate for the London summit of G20 countries was approved.

Tasks before the end of the Czech Presidency

Under the Czech Presidency, the Ministry of Finance takes a responsible, Europe-wide approach to the current crisis situation both in relation to legislation as well as in forming the approach for the coming years. It is therefore necessary to continue intensively in the remaining weeks of the Czech Presidency with the work already commenced. The Ministry will do everything that is needed to coordinate further steps, both at the EU level and globally, and to restore the confidence in financial markets that is necessary in order to stabilise the financial situation.

At the end of April, the European Commission presented a proposal for a directive concerning managers of alternative investment funds. The proposal relates to, among others, managers of hedge funds, private equity funds, commodity funds, and real estate funds. Since May, therefore, the Czech Republic has moderated the Council's work group discussing this legislative proposal with the aim of finding a common position among the Member States.

Nevertheless, the main topic discussed at all levels within the EU will be the reform of financial market supervision based upon the communication from the Commission expected to be issued in May. The goal of the June meeting of the ECOFIN Council will be to prepare, in the form of conclusions of the Council, a contribution for the European Council meeting in June regarding the future structure of supervision in the EU. In June, ECOFIN will further deal with procyclical effects of the financial system and will assess the implementation of those measures taken to support the financial sector.

The issue of distribution on the financial market will also be emphasised as an initiative of the Czech Presidency of the Council of the EU in the non-legislative area. The Czech Presidency aims to emphasise the importance of distribution and the pressure to extend the activities of the European Commission with respect to the distribution of a small group of investment products to all financial market products through the conclusions of the Council adopted for distribution by the ECOFIN Council in June.

8.1.2. European and other international institutions

The Financial Services Committee and the Economic and Financial Committee

The Financial Services Committee (FSC) and the Economic and Financial Committee (EFC) are among the expert committees of the ECOFIN Council. FSC is a forum for preliminary discussions about issues associated with financial services at an expert level, and, together with EFC, it participates in preparing the meetings of the ECOFIN Council. Representatives of the ministries of finance of the EU Member States and representative of the Commission, the European Central Bank and Level 2 and Level 3 Lamfalussy Committees participate in the FSC's work. EFC was established on the basis of Article 114 of the EC Treaty and performs especially the advisory and preparatory tasks stipulated by that Article of the Treaty or assigned directly by the Council. EFC activities focus especially on monitoring the economic and financial situation of the Member States and the Communities, reporting to the ECOFIN Council and the Commission, and contributing to the preparation of activities of the Council in the economic and financial sectors. EFC includes representatives of ministries of finance of the EU Member States and representatives of the Commission, European Central Bank, as well as national central banks.

The Ministry of Finance regularly attends and actively participates in the meetings of both committees. In preparing opinions for the meetings of both committees, the Ministry cooperates with the Czech National Bank. Neither of the aforementioned committees is chaired by the representatives of the Czech Republic during the Czech Presidency, as both have a permanent chairperson. Nevertheless, the presence of the Ministry's representatives at both committees is very constructive and the Ministry of Finance cooperates closely with the respective secretariats in preparing the agendas for individual meetings as well as materials for each item on the agenda.

In 2008, and especially in the second half, the topics associated with the current financial crisis and related responses were discussed at the meetings of the committees. The discussions concerned, in particular:

- evaluating the current development of the financial markets and the impacts of the financial crisis on individual sectors;
- assessing the implementation of action plans adopted by the ECOFIN Council in October and December 2007 and updated in May 2008 (action plan in response to financial turmoil, action plan to review the Lamfalussy process, and action plan to strengthen financial stability);
- preparation for the Washington summit of G20 countries (November 2008) and the subsequent implementation of the adopted measures;
- setting the rules for support to financial institutions in order to be in accordance with the EU rules for providing public support;
- reform of the supervisory structure in the EU;
- limiting the potential procyclical effect of financial regulation;
- changes in accounting rules which would make it possible to value financial instruments at fair value while taking into account the fact that the markets are not liquid.

During 2008, in addition to topics directly related to the financial crisis, the two aforementioned committees also dealt with the following topics: increasing efficiency of deposit insurance systems; issues concerning non-cooperating jurisdictions; increase in efficiency of crisis prevention, crisis management and recovery; issues associated with an increase in banking mobility; support to the SEPA project; strengthening of financial education; integration of the mortgage loan market; preparation of the Memorandum of Understanding on Cross-border Financial Stability; and an increase of efficiency in cross-border settlement of securities transactions.

During 2008, the Ministry of Finance also responded to two questionnaires sent by FSC. The first concerned the availability of crisis management tools; the second was related to inclusion of the so-called European dimension into mandates of the national supervisory authorities. During the first two months of 2009, the Ministry of Finance sent its response to two questionnaires from EFC concerning measures intended to strengthen the stability of the financial system.

This year, the priority topic of both committees continues to be the current financial crisis, including the mitigation of its impacts and preparation of such measures that would help to prevent a crisis of a similar extent in future. In this context, the main issues discussed in the past months of this year were: reforming the supervisory structure in the EU; decreasing the procyclical impacts of the financial system (especially adjustments to accounting policies to mitigate the procyclical effects of fair value measurement); dealing with impaired assets; and overall evaluation of the efficiency of measures adopted to support financial institutions. The two committees also prepared the common position of the EU for the G20 summit in April.

In the coming months, FSC and EFC will continue especially to address reform of the European supervisory framework, distribution on the financial market, and issues associated with the financial and economic crisis.

ECOFIN Council

During 2008, in relation to the financial market and financial services, the ECOFIN Council addressed the topics outlined above in the section about the Financial Services Committee (FSC) and Economic and Financial Committee (EFC).

Particularly in the second half of 2008, the ECOFIN Council devoted considerable attention to the financial crisis and the response to it. The ECOFIN Council:

- regularly discussed the current development of the financial markets situation.
- determined the priority areas upon which it should focus (in particular, increasing transparency on the markets, improving valuation standards, strengthening the prudential framework for the banking sector, reviewing the role of credit rating agencies) (4 March 2008).
- determined the future direction for review of the Lamfalussy process and for strengthening financial stability by adopting the reviewed action plans addressing these issues. Furthermore, the ECOFIN Council adopted the updated action plan in response to the financial turmoil (14 May 2008) and emphasised the necessity for its full implementation (2 December 2008).
- supported the reform of IASB (International Accounting Standard Board) (8 July 2008).
- determined the main principles of the common response to the financial crisis and the main steps that need to be taken, agreed on increasing the guarantee provided to depositors for their deposits to a minimum of EUR 50,000, and called for a review of the practices concerning executive remuneration (7 October 2008).
- prepared the groundwork (4 November 2008) for an informal summit of the heads of state and prime ministers which was held at the beginning of November and at which the Member States agreed on a common position for the G20 summit. After the November summit, the ECOFIN Council supported continuing the close cooperation among Member States in preparing the next international summit (2 December 2008).
- approved the provision of a loan to Hungary in the amount of EUR 6.5 bn (4 November 2008).
- approved an increase in funds for providing medium-term financial aid in cases of imbalanced payment balance for Member States outside the eurozone to double the previous amount (from EUR 12 bn to EUR 25 bn) (2 December 2008).

In addition to addressing the issues related to the financial crisis, the ECOFIN Council did the following during 2008:

- supported the implementation of SEPA, which should result in an integrated, competitive market for EUR payments by 2010 (22 January);
- supported the increase in transparency of sovereign wealth funds (4 March);
- adopted the Memorandum of Understanding on Cross-border Financial Stability (4 April);
- highlighted the importance of financial education and its improvement (14 May);
- supported further integration of the mortgage loans market (14 May);
- supported further removal of barriers to cross-border settlement of securities trades (3 June) and creation of a European central counterparty for OTC derivatives (2 December);
- reached an agreement (general approach) in relation to proposals for the Solvency II directive and the revision of capital requirements directives, the directive concerning the deposit insurance systems and the UCITS directive (2 December);
- embraced the obligation of the banking sector to introduce common principles for banking mobility (2 December).

As is evidenced by the aforementioned decisions and measures, in 2008 the ECOFIN Council had numerous achievements to which, in the second half of 2008 and especially at the close of the year, the representatives of the Ministry of Finance, who at that time cooperated closely with the French representatives and participated greatly in negotiating the compromises in preparation for the Czech Presidency of the Council of the EU, also contributed.

The Czech Republic took over the presidency of the EU Council as at 1 January 2009. During the following months, the priority topics of the ECOFIN Council continued to be the financial crisis, reform of the EU supervisory framework, and preparation for the G20 summit in April.

Already at the first meeting of the ECOFIN Council under the Czech Presidency, the Council managed to approve financial aid to Latvia in the amount of EUR 3.1 bn and to adopt conclusions in relation to banking capital. These steps were the first great success of the Czech Presidency in coordinating the EU's common response to the crisis. At their subsequent meetings, the ministers of finance of the Member States supported a faster transition to the SEPA system and agreed on the common principles for dealing with impaired assets. The ECOFIN Council also supported the CESR (Committee of European Securities Regulators) in its continued work to review the impacts of short selling on the stability of financial markets. Last but not least, the ministers agreed on the common position of the EU for the G20 summit held in early April.

At the beginning of April 2009, informal meetings of ministers of finance and governors of central banks from the EU Member States were held in Prague. As regards financial services, the main topic discussed was reform of the European supervisory framework. The ministers and governors agreed on the main principles for reforming supervision over the financial market in the EU, especially on the necessity to strengthen supervision over macrofinancial stability, and they confirmed the need to harmonise the European supervisory framework.

At the ECOFIN Council's meeting in May 2009, the political agreement between the Council and the European Parliament was confirmed within the first reading of the co-decision process in relation to the following legislative acts: regulation on credit rating agencies, Solvency II directive, e-money directive, and regulation on cross-border payments in the Communities. The political agreement on the review of directives on capital requirements and the Community's programme to support specific activities in the field of financial services, financial reporting and auditing will be confirmed at the meeting of the ECOFIN Council in June. The process of adopting these acts, which represents an important achievement of the Czech Presidency in relation to financial services, will thereby be completed.

At the meeting of the ECOFIN Council in May, the ministers of finance also agreed on doubling the funds for providing medium-term assistance to Member States outside the eurozone that face payment balance problems (i.e. an increase to EUR 50 bn). Furthermore, the ministers also supported providing medium-term assistance in the amount of EUR 5 bn to Romania for its payments imbalance.

At the June meeting of the ECOFIN Council, which is also the last meeting of this formation of the Council planned to be held before the end of the Czech Presidency, the ministers of finance will further address especially those issues related to procyclical effects of the financial system. They will revisit the questions as to the future supervisory structure in the EU and evaluate the implementation of measures taken to support the financial sector. It is also anticipated that the ministers of finance will express their opinions regarding distribution on the financial market.

It can be expected that the priority topics for the rest of the year will continue to be the issues associated with the financial crisis and reform of the supervisory structure in the EU.

ECOFIN Council's Working Party on Financial Services (WP D3)

The D3 Working Party on Financial Services handles legislative proposals with the aim to find compromise among Member States within the Council, enabling the subsequent negotiation of compromise between the Council (represented by the presiding country), the European Parliament and the European Commission, and thus reaching a political agreement that will allow their adoption.

One of the priorities of the Czech Presidency in this area was to complete negotiations on the proposal for the **Solvency II** directive. The proposal combines 13 existing directives regulating the insurance area into one document and introduces a new solvency regime for insurance and reinsurance companies, as the existing legislation is considered to be no longer suitable. The proposal regulates all aspects of insurance and reinsurance, and its objective is the overall modernisation of legislation and deepening integration of the insurance and reinsurance markets. After complicated negotiations, the compromise proposal does not include the so-called group support regime governing supervision over groups of insurance companies that was included in the Commission's original proposal.

Another priority proposal was the **review of capital requirements directives** (2006/48/EC and 2006/49/EC, the so-called **CRD**). This review aims primarily to modernise the prudential rules for supervision over credit institutions and to remove their main shortcomings, which have become evident during the financial crisis. The main changes that this amendment brings consist in establishing colleges of supervisory bodies for cooperation in supervising cross-border groups of credit institutions. Furthermore, the proposal aims to prevent the risks associated with large exposures by adjusting the limits for receivables due from a single client and introducing regulatory legislation for securitisation.

Another proposal discussed under the Czech Presidency was the proposal for a **regulation on credit rating agencies**. The agencies issuing credit ratings came into focus in the context of the current financial crisis, as they were identified as one of its causes. This resulted in the prevailing opinion that credit rating agencies' activities should be regulated and supervised in some way in future. The regulation introduces compulsory registration and supervision of credit rating agencies. In particular, the regulation establishes conditions for registering credit rating agencies in the EU, rules for issuing ratings, preventing conflicts of interest, and improving the transparency of credit rating agencies. The regulation also newly introduces rules for credit rating agencies from countries outside the EU whose ratings are used by financial institutions operating in the EU.

A review of the regulation on cross-border payments in euros (2560/2001/EC) was also discussed during the Czech Presidency.[54] The currently valid regulation ensures that the costs of cross-border payments (transfers, ATM withdrawals, electronic payments) for the consumer are the same as in the case of a corresponding payment in euros made within his or her Member State. The amendment extends the force of the regulation to cover the collection of payments and is important especially for further developing the SEPA project.

Another proposal discussed under the Czech Presidency is the **review of the directive on electronic money institutions** (2000/46/EC, EMD). The review of the directive is intended to remove legal uncertainty consisting in the problematic definition of electronic money and to reduce the excessive regulation hindering the development of this market in the EU. Furthermore, the amendment aims to harmonise this legislation with the adopted directive on payment services on the internal market.

Under the Czech Presidency, the European Commission submitted a **proposal for implementing the Community Programme to support specific activities in the field of financial services, financial reporting and auditing** which aims to support the EU policies in these areas.

[54] The proposal that was eventually approved by the ECOFIN Council is known as the Regulation on Cross-border Payments in the Community.

For all the aforementioned legislative proposals, a consensus was successfully reached among the Member States in the Council (general approach) and subsequently also between the Council, the European Parliament and the Commission. In the case of the capital requirements directive and the Solvency II directive, the general approach was approved by the Council at the end of the French Presidency. In all other cases, however, the negotiations in the Council's respective working parties for the individual legislative proposals were led by representatives of the Ministry of Finance, and, therefore, the agreement was achieved thanks to the Czech Presidency. Reaching agreement between the Council, the European Parliament and the Commission, which was already approved officially by the European Parliament for all aforementioned legislative proposals, is solely the success of the Czech Presidency. Thus, following the necessary technical and linguistic adaptations, nothing will prevent the EU Council from officially approving the agreed compromise texts, whereby the whole legislative process would be completed. The Czech Presidency thus managed to fulfil all the objectives it resolved to achieve in this area.

Under the Czech Presidency, the negotiations on the proposal for review of the directive on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (85/611/EEC, known as **UCITS**) were completed. This proposal was approved at the meeting of the European Parliament in January and, following the necessary technical and linguistic adaptations, will be officially approved by the EU Council in June.

One of the legislative proposals that was expected to be discussed during the Czech Presidency was also the **review of the directive on deposit-guarantee schemes** (94/19/EC, so-called **DGS**). Nevertheless, thanks also to the intensive work of the representatives of the Ministry of Finance, agreement on this review was reached with the European Parliament already before the end of the French Presidency (December 2008). Similarly, negotiations on **review of the directive on settlement finality in payment and securities settlement systems** (98/26/EC) and the **directive on financial collateral arrangements** (2002/47/EC) were completed already under the French Presidency and, after their necessary technical and linguistic adaptations, these directives were officially approved by the EU Council in April.

On 30 April 2009, the European Commission submitted a legislative **proposal for the directive on alternative investment fund managers**. The proposal concerns, among other things, managers of hedge funds, private equity funds, commodity funds and real estate funds. Thus, the Ministry of Finance has chaired a working party of the Council since May to negotiate this proposal and which aims to find a compromise among Member States.

From the beginning, the Czech Presidency of the Council of the EU during the first half of 2009 has been substantially influenced by the ongoing financial and economic crisis to which it has responded flexibly with certain changes in the originally planned agenda. At the same time, the Czech Presidency has had, and will continue to need, to cope with the great pressure it faces due to the situation in financial markets and the approaching end of the election period of the European Parliament and of the term of office of the European Commission. Nevertheless, the Czech Presidency has shown in the field of financial services that even a small country is able to lead the Union at difficult times and achieve important successes.

European Council

The European Council is the most important political body of the Communities and is represented by the top political leaders of the Member States (heads of state and prime ministers) and the President of the European Commission. The European Council meets at least four times a year and determines the general policy direction of the European Union.

The Ministry of Finance participated in preparing the supporting documents for the Prime Minister concerning the current financial crisis for the meetings in both 2008 and 2009.

Furthermore, it also prepared the common position of the EU for the G20 summits (April 2009).

Level 2 Committees of the Lamfalussy process

In July 2000, on the basis of a decision of the EU Council, a working party chaired by Baron Alexander Lamfalussy was established to prepare an analysis of the mechanisms of capital markets regulation and to propose possibilities for their adaptation to the conditions on the global financial markets. The result of this party's work was a proposal for a four-level mechanism of adopting, approving and controlling the implementation of regulatory legislation concerning financial markets at the EU level. This became common as the Lamfalussy process.

Level 1 includes legal norms, especially directives and regulations, adopted in accordance with the co-decision procedure of the Council and the European Parliament. The primary legislation regulates the character and scope of the implementing measures to be approved at Level 2, on the basis of a proposal of the European Commission. Level 2 includes implementing measures for the primary legislation adopted by the European Commission. The Level 2 committees include the European Banking Committee (EBC), the European Insurance and Occupational Pensions Committee (EIOPC), and the European Securities Committee (ESC). The representatives of the Ministry of Finance are members of the Level 2 committees and participate in the meetings of EBC, EIOPC and ESC.

Level 3 is intended to ensure that the primary and secondary legislation is reflected properly and on schedule by strengthening the cooperation of supervisory bodies. Level 3 committees within the Lamfalussy process are the following: Committee of European Banking Supervisors (CEBS), Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS), and Committee of European Securities Regulators (CESR). Level 4 seeks to strengthen the enforcement of the European legislation by ensuring cooperation among the European Commission, Member States and supervisory institutions. The enforcement of EU law is an exclusive competence of the European Commission.

European Banking Committee (EBC)

EBC is an advisory committee of the European Commission, consisting of the top political leaders of the Member States and representatives of the European Commission. It closely cooperates with CEBS and performs two basic functions:

- advisory – in formulating proposals for legislation of the European Communities in the area of banking and in fulfilling tasks of the European Commission, it ensures proper implementation of European legislation in the legal orders of the Member States; and
- regulatory (comitology).

Generally, the main topics of EBC for 2008 were the situation on the financial markets and, more specifically, the review of CRD, banking deposit insurance schemes, reporting and settlement of derivatives on OTC markets.

The work of the Ministry of Finance in the committee has continued in 2009. The negotiations to date have included issues related to the G20 summit, the report of the de Larosière Group, regulation and supervision over the financial market within the EU, review of CRD, and procyclicity. It can be expected that evaluation of the situation in the financial markets, establishing cooperation of domestic and host supervisory bodies, and work on the structure of supervision over financial markets (including discussion about the counter-cyclical effects of various measures) will continue.

European Insurance and Occupational Pensions Committee (EIOPC)

EIOPC, the Commission's advisory committee, deals with expert as well as policy issues connected with insurance, including pension funds. It consists of top political leaders of Member States and representatives of the European Commission. Its mission is to consider any issues concerning the application of regulations of the Communities in insurance and in the area of occupational pension insurance and to closely cooperate with CEIOPS.

During 2008, at the meetings of EIOPC, the representatives of the Ministry of Finance addressed especially the Solvency II project, the directive on institutions for occupational retirement provisions (IORP), motor vehicle insurance, the Insurance Mediation Directive (IMD), and retail investment products.

Moreover, in 2009 the committee dealt with the G20 recommendations in the field of financial markets, the financial crisis and evaluation of the Solvency I directive. By the end of 2009, the committee will have covered especially the Solvency II directive, in relation to which five working party meetings are planned due to the adoption of implementing measures for this directive. Through the end of 2009, the preparatory works plus identification of problems and proposals for their solutions will also affect decisions on introducing and establishing guarantee schemes in insurance, on a new approach to risk management and capital requirements in connection with IORP, and on the future direction of IMD.

European Securities Committee (ESC)

ESC is also an advisory and regulatory body of the European Commission. It discusses and votes on proposals of the Commission that are intended to increase efficiency in regulating the European securities market. It provides advice on policy issues concerning the capital market and issues implementing regulations for framework legislation in this area. It consists of top political leaders from the Member States and representatives of the European Commission.

The Ministry of Finance participated in all meetings of the committee in 2008. Members dealt especially with the overall situation in financial markets and, more specifically, with the UCITS Directive, Market Abuse Directive, mutual recognition with third countries in the area of capital markets, credit rating agencies, Markets in Financial Instruments Directive (MiFID), non-harmonised funds, Prospectus Directive, market infrastructure, and Directive on Deposit Guarantee Schemes.

In 2009, the Ministry of Finance continues its active participation in the committee's meetings. The issues discussed to date include market infrastructure, transparency, Prospectus Directive, Directive on Deposit Guarantee Schemes, UCITS Directive, MiFID in the area of derivatives, and Market Abuse Directive. The committee also discussed the European Economic Recovery Plan, regulation of hedge funds and private equity funds, retail investment products, and the future structure of supervision over the financial market in the EU.

OECD

Committee on Financial Markets under OECD (CMF under OECD)

CMF is the main OECD body dealing with issues related to financial markets. It monitors and studies measures intended to improve the operation of national financial markets and the international financial and exchange market and discusses conceptual and strategic trends. It is included in the international network of bodies which execute oversight on developments in the financial system and foster international cooperation and coordination and greater compatibility of financial market regulation. Its members are representatives of the ministries of finance and central banks of the OECD member states. Each meeting of the committee is special and exceptional in that it is attended by representatives from the international private financial sector who take part in addressing important issues of common interest for both the public and privates sectors.

A representative of the Ministry of Finance participated in all meetings of the committee in 2008, which dealt with general issues as to the situation and future direction of financial markets. More specifically, the committee dealt especially with deposit insurance systems, state investment funds, the efficiency and usefulness of the regulation in the financial sector and the need to reform it, financial education, and the financial indicators project. The committee also organised a seminar on the payment phase of the retirement system at which it covered political issues and new challenges that the retirement system sector must currently face.

In 2009 to date, the Ministry of Finance attended a single meeting at which the CMF members exchanged their experiences in relation to measures adopted to address the current financial and economic crisis and the possibility to cancel these (especially in the context of excessive deposits insurance). Topics often discussed on an ongoing basis include the efficiency of regulation in financial markets, financial education, and consumer protection in financial markets. A major discussion about the influence of the crisis on the insurance sector is anticipated before the end of the year.

Insurance and Private Pensions Committee (IPPC under OECD)

IPPC is a committee under the Directorate for Financial and Enterprise Affairs (DAF) and is the main OECD body dealing with issues concerning the insurance market, oversight of the insurance sector, and private pensions, i.e. non-public pension insurance sector (issues related to private pensions are dealt with by the Working Party for Private Pensions under IPPC). IPPC fosters international cooperation, coordination and greater compatibility of regulation in the said financial market sectors. Its members are representatives of the ministries of finance and central banks of OECD member states.

In 2008 IPPC gathered twice at its permanent meetings in Paris. The sessions' main agenda was comprised of the efficiency of oversight in the insurance sector, review of the so-called Core Principles in the area of occupational pension insurance, corporate management, as well as financial education, the annuities market and the payment phase in private pension insurance, insurance against large-scale disasters, review of the Codes of Liberalisation and, last but not least, the accession processes of new member states. Other conferences also were organised under the auspices of this committee. One of them was a conference in Washington which sought to improve dialogue in the area of financial education on an international level and enable the sharing of experiences and best practices. A similar event was a conference organised in cooperation with IOPS in Nairobi, Kenya, which was intended to develop political and expert discussion about savings for old age among the developed countries of OECD and developing countries in Africa.

G20

The G20 brings together ministers of finance and governors of central banks of 19 countries[55] and the EU (represented by the currently presiding country and ECB). It was established in 1999 to provide a forum for the exchange of opinions of the world's most important economies on key issues concerning the global economy.

The seriousness of the current economic crisis and its impacts on the real economy led to the extraordinary summit of heads of state and prime ministers of the G20 countries held in Washington in November 2008. At this summit, the representatives of the G20 countries agreed on an action plan to combat the unfavourable situation in the world economy and financial markets, including both short-term and long-term goals. The G20 representatives agreed especially that they would proceed in a coordinated way and on the necessity to improve the regulation in financial markets and to reform international financial

[55] The member states are Argentina, Australia, Brazil, Canada, China, France, Germany, Great Britain, India, Indonesia, Italy, Japan, Mexico, Republic of South Africa, Russia, Saudi Arabia, South Korea, Turkey and USA.

institutions. At the same time, they rejected any forms of protectionism and undertook to maintain an open market economy.

Great Britain, which presided over the G20 during the first half of this year, subsequently established four working groups to monitor fulfilment of the agreed measures and to prepare proposals for main reform for the summit in April.

1. A working group to strengthen regulation and transparency – This group focused on issues associated with accounting, disclosing information, prudential supervision and risk management.
2. A working group to strengthen international cooperation and the integrity of financial markets – This group's main topics included questions concerning management of cross-border financial crises and recovery measures, protection of the international system against risks resulting from the existence of non-cooperating jurisdictions, and strengthening of cooperation between international organisations.
3. A working group toward reform of the International Monetary Fund (IMF) – This group focused especially on reforming the role, administration, management and resources of IMF.
4. A working group regarding the World Bank and other multilateral development banks – This group examined the mandates, management and administration, financing, and tools used by these institutions.

At the April summit in London, the G20 countries agreed that there is a need in the area of financial services for a strategy on terminating the current extraordinary temporary measures. Furthermore, they agreed on reform of the Financial Stability Forum and on the foundations for regulatory reform of the financial markets.

By virtue of the Czech Republic's occupying the Presidency of the EU, the Ministry of Finance took part in both the November summit (as an observer) and the April summit, at which it represented the interests of the entire EU. The ministry also participated in the activities of the working group for strengthening regulation and transparency as well as the negotiations among the ministers of finance and their representatives.

We regard it as important that for all negotiations the Czech Presidency managed to reach an agreement on a common position among the member states, the so-called European mandate, which it afterwards defended successfully.

Other selected platforms of the European Commission

European Financial Conglomerates Committee (EFCC)

EFCC engages in expedient supervision over financial conglomerates[56], covering an area that is important for the individual Member States as well as for the EU as a whole due to the systemic importance of these companies. Directive 2002/87/EC, the Financial Conglomerates Directive (hereinafter just "FCD"), aims to improve the prudent and efficient supervision over financial conglomerates; supports convergence between national supervisory authorities and financial sectors; enhances financial stability; and is a significant improvement in the protection of depositors, shareholders and investors.

The Interim Working Committee on Financial Conglomerates (IWCFC), an expert working party that takes a coherent view of the role of supplementary supervision over financial conglomerates, presented in April 2008 the conclusions of the response to the Call for Advance that it made in cooperation with CEBS in assessing whether comparable supervision is conducted over the banking groups and financial conglomerates in the USA and Switzerland. The European Commission organised a round table discussion for all concerned parties in September 2008. The participants agreed that the decision concerning the review of FCD may be published only after Solvency II and the conclusions regarding

[56] Large financial groups operating in various financial sectors, often providing cross-border services.

the CRD review are approved. The legislative changes to FCD thus will be considered only after issue of the Review Report that will be completed by the end of 2009.

European Financial Integration Report (EFIR)

Another working group of the European Commission that participates in creating the annual report on the development of integrating financial markets in the European Union is known as the European Financial Integration Report (EFIR). The report is a successor of the two previously issued publications (the Financial Integration Monitor and the Single Market in Financial Services Progress Report). The main part of the report deals with an economic analysis of European financial integration and its impacts on the structure, competitiveness, efficiency, innovation and stability of financial markets. At the same time, the report strives to monitor the ways in which financial instability could spread across the entire EU.

Government Expert Group on Retail Financial Services (GEGRFS)

GEGRFS is an expert group of the European Commission that is engaged in issues relating to retail financial services. The work of this group is based especially on the Green Paper on Retail Financial Services in the Single Market published in May 2007. Specific legislative and non-legislative proposals of the European Commission as well as topics in the phase of expert discussion are submitted at the meetings of this group. Representatives of the Ministry of Finance participate in all meetings of this group.

The main topic under discussion in GEGRFS in 2008 was the legislative proposal of the European Commission for regulation of so-called switching, i.e. the conditions that arise during a change of bank that maintains a client's current account. GEGRFS became the first platform including representatives of all Member States upon which this proposal was under expert discussion. On the basis of numerous critical objections and the subsequent will of market representatives to resolve the problem by means of self-regulation, the legislative proposal was withdrawn in the autumn of 2008.

Another essential topic became the initiative of the European Commission concerning so-called substitute retail investment products. The initiative aims to harmonise the conditions for distribution of these products. The group also discussed issues related to credit registers and the possibility to integrate them within a single market, the out-of-court settlement of disputes in the financial market, and financial inclusion.

Government Expert Group on Mortgage Credit (GEGMC)

GEGMC is another expert group of the European Commission that in contrast to the rather general GEGRFS has a more specific orientation. The group was established in 2005 as an advisory body assisting the European Commission in defining and developing policies in the area of mortgage loans. In addition to its meetings, the group serves as a network for obtaining information on the situations in national markets through surveys on specific topics.

The main item on the 2008 agenda became the text of the White Paper on the Integration of EU Mortgage Credit Markets (issued in December 2007) and subsequently the fulfilment of the objectives set down in that document.

In the course of the year, the first surveys were conducted and the European Commission discussed their results at the GEGRFS meetings. Responsible borrowing, in relation to which the Commission mapped out the situation on the European markets and proposed specific solutions emphasising especially the evaluation of consumers' ability to repay their loans, became the most important issue. Another important initiative discussed at the GEGMC meetings was the draft Recommendation on Land Registration, Foreclosure and Property Valuation.

Early Intervention Working Group (EIWG)

The EIWG, a working group of the European Commission, held its first meeting on 31 October 2008. In its work, the group aims to prepare a draft directive that would regulate the procedure of Member States in the case that a particular bank faces problems (especially in terms of liquidity) and which therefore does not concern resolving a systemic crisis. A wide spectrum of issues was under focused discussion, including, for example, the timing of when to start interventions, measures of supervisory bodies, and financing. The issue relating to the removal of legal barriers on the transferability of assets within banking groups and the possibility to finance interventions using funds from deposit insurance systems can arguably be regarded as the most serious and politically very sensitive.

8.2. Financial markets legislation

8.2.1. Community law

In 2008, community-level negotiations were held in relation to several important changes in regulations on financial markets. The Ministry of Finance, which is responsible in the Czech Republic for the directives concerning the financial market, participated in these negotiations both through the personal attendance of its representatives and by sending remarks and comments to individual materials.

As certain important legislation (Solvency II, CRD review, CRA regulation) were not completed under the Slovenian and French presidencies (2008), this work was taken over in the first half of 2009 by the Czech Presidency represented by the Ministry of Finance. This included negotiations on other legislation to which the preceding presidencies did not devote much attention, such as the new directive regulating e-money issuers and the regulation on cross-border payments in euros. Their completion represents a considerable success of the Czech Republic.[57]

The Ministry of Finance contributed through its presentations to the negotiations on the proposal of the new directive on the activity of standard collective investment funds (the so-called UCITS IV directive), which regulates certain new institutions within the regulation of standard collective investment funds (e.g., cross-border mergers, free movement in providing services of investment management companies, a new concept of information for investors, new investment strategies of master-feeder funds). The process of negotiations was essentially brought to a conclusion by the French Presidency.

In 2008, and specifically in the second half, brief amendments also were negotiated in relation to the directive on deposit insurance that responds to the crisis in the banking sector of some states and in relation to the directive on settlement finality in securities transactions and directive on financial collateral arrangements. The Ministry of Finance also contributed actively in these cases through certain substantial comments.

Soon after the adoption of Directive 2008/48/EC of the European Parliament and Council on credit agreements for consumers, a joint working group of the Ministry of Finance and the Ministry of Industry and Trade (main coordinator) was established with the aim of transposing this directive. With the aim to obtain opinions, especially from professionals, a public consultation was held at the end of 2008, focusing questions especially on those areas of the directive in which a Member State has a certain leeway for its own legal provisions. After assessing the responses, the working group began preparing the wording of the law itself.

[57] For more information, see Chapter 8.1. Ministry of Finance’s activities on an international level.

8.2.2. National legislation

The Ministry of Finance is a coordinator for the preparation of legislation regulating the financial market. In this regard, it prepared proposals for several important regulations in 2008. During this process, the Ministry regularly cooperates with the Czech National Bank and associations of financial market participants.

The Parliament of the Czech Republic discussed and approved an amendment to the Act on Capital Market Undertakings, transposing the directive on markets in financial instruments known as MiFID. The amendment took effect on 1 July 2008 and brought many substantial changes for investment firms (both banking and non-banking), regulated markets and the entire capital market in general. Due to, among other things, the intensive consultancy activity of the Ministry of Finance with market participants during the preparation of the law, these changes do not present unknown obligations for the subjects to this law.

Furthermore, a transposition amendment to the Motor Third Party Liability Insurance Act prepared by the Ministry of Finance during 2007 took effect in the first half of 2008.

The Ministry of Finance also prepared and submitted to the government a proposal for a wholly new Insurance Act that would introduce especially the implementation of new European reinsurance rules. The government approved this draft act in July 2008 and submitted it to the Czech Parliament which, however, did not discuss it during the second half of the year. Discussions on the proposal, therefore, are expected to be held before the end of 2009's first half.

In October 2008, the government approved the legislative intent of the Financial Market Supervision Act prepared by the Ministry of Finance, which is intended to regulate supervision in such a way that certain parts of providing supervision over the financial market are concentrated into a single aggregate law. This idea follows up the institutional integration of supervision over the financial market that was carried out in 2006 by merging the supervisory authorities into the Czech National Bank.

The Ministry of Finance prepared and submitted to the government the so-called Theses of the new act on pension savings which should regulate separation of the assets of pension institution managers from those of the insurees within the 3rd (optional) pension pillar currently represented by pension funds. In approving the Theses in October, the government requested the Ministry of Finance to prepare the regulation for the new pension savings system while preserving the current system of pension funds in parallel with the existing systems. This extensive law, adopting modern regulatory elements from the area of financial markets, was prepared by the Ministry of Finance in the autumn of 2008 and submitted for the interdepartmental notice and comment procedure. The bill on pension savings was approved by the government on 20 April 2009.

In the first half of 2008, the consultancy process with market participants was completed as part of the transposition works on the directive on payment services on the internal market. Afterwards, the act on the payment system was prepared and was submitted for the interdepartmental notice and comment procedure at the end of 2008. This law is also expected to be submitted to the government at the end of 2009's first half.

Throughout 2008, the Ministry worked on the amendment transposing the so-called transparency directive on the information duty of issuers of listed securities, the directive on the assessment of acquisitions of qualified holdings in financial institutions, and the directive on assets suitable for investment by standard collective investment funds. Following the interdepartmental notice and comment procedure, the draft act was approved by the government in November 2008 and submitted to the Czech Parliament. It is expected to be approved in the middle of 2009.

At the end of 2008, over the course of several weeks, the Ministry of Finance prepared a draft amendment to the Act on Banks. The government and the Parliament later approved the amendment, which was then published in the Collection of Laws. The upper limit of insurance on deposits in banks was thereby increased to EUR 50,000. The draft act responds to similar measures in other countries, although the Czech banking market is stabilised.

As for regulations not prepared by the Ministry of Finance, the Ministry actively gave its opinion especially on draft decrees of the Czech National Bank, which is authorised under draft acts prepared by the Ministry of Finance to issue implementing regulations.

Furthermore, the Ministry of Finance participated, within the notice and comment procedure as well as within its regular work, in commenting on laws that in some way relate to the financial market. These included especially laws prepared by the Ministry of Justice: a draft act transposing the directive on the exercising of voting rights by shareholders of listed companies; a new draft of the Civil Code; and a new act on business companies, and especially regarding issues related to securities law and shares law.

In 2009, legislative activity can be expected not only in completing the draft acts already being prepared by the Ministry of Finance, but also in beginning work on laws transposing new EU regulations that respond especially to the financial markets crisis.

8.3. Consumer protection in the financial market

In 2008, the Ministry of Finance continued its activities in the field of financial market development and especially realisation of the Framework Policy in the area of consumer protection. The central topic became the harmonisation of distribution and requirements on the expertise of distributors. Further to last year's public consultation, the Ministry established a Working Group on Financial Market Distribution at the beginning of 2009. The group aims to evaluate the possibilities and suggest solutions for future harmonisation of the distribution regulation, especially in the following areas:

- provisions for originating authorisations to operate on the financial market and defining the distributors' responsibility to clients,
- registration of distributors of financial services,
- requirements for their expert qualification.

The group brings together representatives of the Ministry of Finance, Czech National Bank, professional associations and consumer associations. Its mandate includes defining recommendations for the regulation of as yet unregulated sectors of the financial market, especially providers of consumer lending. The group should formulate its conclusions by September 2009.

In autumn of 2008, a public consultation was held to review the existing system for out-of-court settlement of consumer disputes on the financial market. The Ministry of Finance published the results on its web site. The main conclusion is a recommendation to extend the powers of the financial arbiter to other sectors of the financial market and to change the method of its financing, using funds either from the state budget or from financial market entities. Since 2008, the Ministry has also been a member of the Platform for Alternative Dispute Resolution. The platform is an interdepartmental body and decides on basic issues of the Alternative Dispute Resolution Project that is under the Ministry of Industry and Trade.

In 2008, the Working Group for Financial Education continued its work. The group comprises representatives of the concerned ministries (in addition to the Ministry of Finance, also the Ministry of Industry and Trade and the Ministry of Education, Youth and Sports), Czech National Bank, professional associations operating on the financial market, representatives of entities providing educational projects, consumer associations and education professionals. This working group meets approximately twice a year. At these meetings, members discuss their projects and experiences and endeavour to find a common approach to increasing the financial literacy of the Czech population. Representatives of the Ministry of Finance also participated in preparing a systematic manual for financial literacy of teachers that was published in the autumn of 2008 by the Ministry of Education, Youth and Sports and its directly subordinated bodies (the National Institute of Professional Education and the Pedagogical Research Institute). The publication should help teachers at secondary and primary schools in their preparation for future teaching of financial education at schools. In autumn last year, the English version of the section dealing with financial education was launched on the Ministry of Finance's website.

The Ministry of Finance also actively presents its approaches to issues of retail financial services and consumer protection at an international level, especially in expert working groups of the European Commission and OECD. Within the Czech Presidency of the Council of the EU, the Czech Republic emphasised the need for harmonising conditions of distribution for the entire financial market, especially with respect to rules on negotiating with clients, providing information, expertise of distributors, and commission schemes.

LIST OF ABBREVIATIONS

Abs.	Absolute
AKAT	Asociace pro kapitálový trh (Capital Market Association)
APF CR	Asociace penzijních fondů České republiky (Association of Pension Funds of CR)
APR	Annual Percentage Rate
bp	Basis point
CNB	Czech National Bank
CR	Czech Republic
CZK	International currency code of the Czech crown
CZSO	Czech Statistical Office
EBRD	European Bank for Reconstruction and Development
EC	European Communities
ECB	European Central Bank
EIB	European Investment Bank
EU	European Union
EUR	International currency code of euro
Fed	Federal Reserve System (U.S. Central Bank)
FESE	Federation of European Securities Exchanges
GDP	Gross domestic product
IBRD	International Bank for Reconstruction and Development
KB	Komerční banka
MiFID	Markets in Financial Instruments Directive
ML	Mortgage loan
MoF	Ministry of Finance of the Czech Republic
MRD	Ministry for Regional Development
OECD	Organisation for Economic Co-operation and Development
OEUT	Open-ended unit trust
OKEČ	Branch Classification of Economic Activities (CZ_NACE)
PSE	Prague Stock Exchange
PXE	Prague Energy Exchange
RM-S	RM-Systém
USA	United States of America
USD	International currency code of the US dollar
VAT	Value added tax

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APPENDIX 1: FINANCIAL MARKET LEGISLATION

In 2008, the following changes were made in the legislation of the Czech Republic and European Communities in the financial market sphere:

1.1. Cross-sectoral regulations in the sphere of financial markets

1) European legislation and other initiatives published in 2008:

- **Directive 2008/48/EC** of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC. The Member States have 2 years to transpose the directive into their national legal orders, i.e. the directive will be applicable in 2010. The objective of this regulation is to create conditions for a single internal market in consumer lending, to ensure a high level of consumer protection, and to specify the communitary adjustments.
- **Commission Decision** of 30 April 2008 setting up a group of experts on financial education **(2008/365/EC)** (Official Journal, L 125, 9 May 2008, p. 36–38).
- **Directive 2008/52/EC** of the European Parliament and of the Council of 21 May 2008 on certain aspects of mediation in civil and commercial matters. The directive aims to allow access to alternative dispute resolutions by ensuring a balanced relationship between mediation and court proceeding. The directive may be applied to cross-border disputes concerning civil and commercial matters. It will not relate to tax, customs and administrative matters or responsibility of a state for its conduct in enforcing state powers.
- **Regulation (EC) No 593/2008** of the European Parliament and of the Council **on the law applicable to contractual obligations** (Rome I) shall be applicable from 17 December 2009, taking the place of the Convention on the Law Applicable to Contractual Obligations known as the Rome Convention (effective from 24 July 2008).

2) Pending European legislation (including legislation published after 31 December 2008) and other initiatives of the European Commission:

- **Draft directive** of the European Parliament and of the Council **on consumer rights**, which should replace the existing directives 99/44/EC, 93/13/EC, 97/7/EC and 85/577/EC (8 October 2008).

3) Acts that took effect in 2008:

- **Act No. 104/2008 Coll., on Takeover Bids and on Amendments to Certain Other Acts (effective from 1 April 2008).**
- **Act No. 126/2008 Coll., amending certain acts in connection with the enactment of the Act on the Restructuring of Companies and Cooperatives (effective from 1 April 2008).**
- **Act No. 253/2008 Coll., on Selected Measures against Legitimisation of Proceeds of Crime and Financing of Terrorism (effective from 1 September 2008).**
- **Act No. 254/2008 Coll., amending certain acts in connection with the enactment of the Act on Selected Measures against Legitimisation of Proceeds of Crime and Financing of Terrorism (effective from 1 September 2008).**
- **Act No. 36/2008 Coll., amending Act No. 634/1992 Coll., on Consumer Protection, as subsequently amended; Act No. 40/1995 Coll., on Advertising Regulation and the Amendment and Completion of Act No. 468/1991 Coll., on Operation of Radio and Television Broadcasting, as subsequently amended; Act No. 513/1991 Coll., the Commercial Code, as subsequently amended; and the transposition of Directive 2005/29/EC of the European Parliament and of the Council concerning unfair business-to-consumer commercial practices in the internal market, whereby Act No. 6/1993 Coll., on the Czech National Bank, as subsequently amended, was also amended. As a result, the Czech National**

Bank currently executes the supervision over adherence to the ban on using unfair commercial practices in the case that they are used by entities subject to CNB's supervision.

- **Act No. 344/2007 Coll.,** amending Act No. 513/1991 Coll., the Commercial Code, as subsequently amended, and Act No. 200/1990 Coll., on Violations, as subsequently amended, effective on 1 March 2008, introduced a change in the regulation of the financial security in the provisions of Section 323a et seq. of the Commercial Code. The main change is that the financial security regime shall newly apply to all legal entities if their counterparty is any of the listed institutions of the financial sector.

4) Pending Acts (including acts already adopted that have taken effect or will take effect after 31 December 2008):

- **Draft act on certain conditions in negotiating a consumer loan and on the amendment of certain acts**. The draft act is a full transposition of Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC.
- **Legislative intent of the Financial Market Supervision Act.** The main objective is a unified legal regulation for the procedures of the Czech National Bank in performing supervision over the financial market. It is another step following up the integration of supervision into the Czech National Bank that occurred in 2006. On 30 April 2008, the legislative intent of the act was published on the website of the Ministry of Finance for consultation. On 8 October 2008, the legislative intent of the act was approved by Government Resolution No. 1252.
- **Draft Act on the Czech National Bank.** This act becomes effective upon introduction of the euro as the currency of the Czech Republic.

5) Secondary legislation:

- Decree No. 280/2008 Coll. of the Czech National Bank of 31 July 2008 on bureau-de-change activity, non-cash foreign currency transactions and money services.

1.2. Legislation in the sphere of capital markets

1) European legislation and other initiatives published in 2008:

- **Expert report** of the European Securities Markets Expert Group (ESME) concerning commodity derivatives and related business activities (4 June 2008).
- **Expert report** of the European Securities Markets Expert Group (ESME) concerning the role of credit rating agencies and the relationship between Article 10 of Directive 2003/71/EC on the prospectus and Directive 2004/109/EC on transparency (8 July 2008).
- **European Commission's RIA in the area of private placement** (17 July 2008).
- **Second advice** of the Legal Certainty Group **on solutions to legal barriers related to post-trading** within the EU (August 2008). The European Commission will present a legislative proposal in 2009 on the basis of this advice.

2) Pending European legislation (including legislation published after 31 December 2008) and other initiatives of the European Commission:

- **Proposal of the European Commission for a new directive of the European Parliament and of the Council amending Directive 98/26/EC on settlement finality in payment and securities settlement systems and Directive 2002/47/EC on financial collateral arrangements in the case of linked systems and credit claims (23 April 2008).**
- **Proposal of the European Commission for an amendment to the Directive of the European Parliament and of the Council on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities – so-called UCITS IV (16 July 2008).**

- **Draft regulation on credit rating agencies (23 April 2009).**
- **Draft recommendation of the European Commission for improved procedures for receiving relief on tax withheld from gains on securities (13 November 2008).**

3) Acts that took effect in 2008:

- **Act No. 29/2008 Coll.,** amending **Act No. 256/2004 Coll., on Capital Market Undertakings**, as subsequently amended, in connection with an adjustment to claim for compensation from the Securities Brokers Guarantee Fund (effective from 12 February 2008).
- **Act No. 230/2008 Coll.**, amending **Act No. 256/2004 Coll., on Capital Market Undertakings**, as subsequently amended, **and other related acts** (effective from 1 July 2008).

4) Pending Acts (including acts already adopted that have taken effect or will take effect after 31 December 2008):

- **Act No. 7/2009 Coll.**, amending Act No. 99/1963 Coll., Civil Procedure Code, as subsequently amended, and other related acts (effective from 23 January 2009).
- **Amendment to Act No. 256/2004 Coll., on Capital Market Undertakings**, as subsequently amended, and **Act No. 189/2004 Coll., on Collective Investment**, as subsequently amended, **and other related acts** – transposition of Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market, Commission Directive 2007/14/EC of 8 March 2007 laying down detailed rules for the implementation of certain provisions of Directive 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market, Directive 2007/44/EC of the European Parliament and of the Council of 5 September 2007 amending Council Directive 92/49/EEC and Directives 2002/83/EC, 2004/39/EC, 2005/68/EC and 2006/48/EC as regards procedural rules and evaluation criteria for the prudential assessment of acquisitions and increase of holdings in the financial sector, and Commission Directive 2007/16/EC of 19 March 2007 implementing Council Directive 85/611/EEC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as regards the clarification of certain definitions. The amendment to the law was submitted to the Parliament on 15 January 2009. The law can be expected to take effect in July of this year.

5) Secondary legislation:

- Decree No. 234/2008 Coll., amending Decree No. 605/2006 Coll., on certain information duties of investment firms (effective from 1 July 2008).
- Decree No. 235/2008 Coll., on information duties of the settlement system administrator and the central securities depository (effective from 1 July 2008).
- Decree No. 236/2008 Coll., on information duties of the operator of the regulated market and the operator of a multilateral trading facility (effective from 1 July 2008).
- Decree No. 237/2008 Coll., on the details of certain rules in the provision of investment services (effective from 1 July 2008).
- Decree No. 238/2008 Coll., amending Decree No. 58/2006 Coll., on the manner of keeping separate records of investment instruments and records based on separate records of investment instruments (effective from 1 July 2008).
- Decree No. 255/2008 Coll., on forms for lodging applications pursuant to the Act on Capital Market Undertakings and the contents of their annexes (effective from 11 July 2008).
- Decree No. 282/2008 Coll., amending Decree No. 123/2007 Coll., stipulating the prudential rules for banks, credit unions and investment firms (effective from 1 September 2008).

- Decree No. 283/2008 Coll., amending Decree No. 347/2004 Coll., on the method of observing the rules for prudential business activities and the rules for organising internal operation of an investment company and investment fund (effective from 15 August 2008).

1.3. Legislation in the sphere of banking, building savings schemes and credit unions

1) European legislation and other initiatives published in 2008:

- none

2) Pending European legislation (including legislation published after 31 December 2008) and other initiatives of the European Commission:

- **Directive 2009/14/EC** of the European Parliament and of the Council, **amending Directive 94/19/EC on deposit-guarantee schemes as regards the coverage level and the payout delay**.
- Draft directive amending Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions and Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006 on the capital adequacy of investment firms and credit institutions.
- Draft directive on the taking up, pursuit and prudential supervision of the business of electronic money institutions, amending Directive 2005/60/EC and Directive 2006/48/EC and repealing Directive 2000/46/EC.
- Draft regulation of the European Parliament and of the Council on cross-border payments in the Communities.

3) Acts that took effect in 2008:

- **Act No. 433/2008 Coll., amending Act No. 21/1992 Coll., on Banks, as subsequently amended.** The act increases the limit for insurance of deposits to the equivalent of EUR 50,000 (effective from 15 December 2008).

4) Pending Acts (including acts already adopted that have taken effect or will take effect after 31 December 2008):

- Draft Payment Systems Act. Transposition of **Directive 2007/64/EC on payment services in the internal market**. Anticipated effectiveness from 1 November 2009.
- Draft act amending certain acts in connection with the enactment of the Payment Systems Act. Anticipated effectiveness from 1 November 2009.
- Draft act amending Act No. 256/2004 Coll., on Capital Market Undertakings, as subsequently amended, and other related acts (Parliamentary Print No. 705).
- Draft act amending Act No. 6/1993 Coll., on the Czech National Bank (Parliamentary Print No. 800).
- Draft act amending Act No. 21/1992 Coll., on Banks, concerning the introduction of instruments for the case of threatened stability of either an individual bank or the banking or financial system as a whole.

5) Secondary legislation:

- Decree No. 282/2008 Coll., amending Decree No. 123/2007 Coll., stipulating the prudential rules for banks, credit unions and investment firms (effective from 1 September 2008).
- Decree No. 358/2008 Coll., amending Decree No. 307/2004 Coll., concerning the submitting of information and documents to the Czech National Bank by entities that belong to the financial institutions sector, as amended by Decree No. 34/2006 Coll. (effective from 1 December 2008).
- Provision of the Czech National Bank No. 1/2008, amending Provision No. 3 of 25 June 2007 concerning the submitting of statements by credit unions to the

Czech National Bank, as amended by Provision of the Czech National Bank No. 8 of 13 December 2007, amending Provision No. 3 of 25 June 2007 concerning the submitting of statements by credit unions to the Czech National Bank.
- Provision of the Czech National Bank No. 2/2008 concerning the submitting of statements by banks and foreign bank branches to the Czech National Bank (effective from 1 January 2009).
- Provision of the Czech National Bank No. 3/2008 concerning the disclosure of information by electronic money institutions (effective from 1 January 2009).
- Provision of the Czech National Bank No. 4/2008 concerning the submitting of statements by electronic money institutions to the Czech National Bank (effective from 1 January 2009).

1.4. Legislation in the sphere of insurance and supplementary pension insurance

1) European legislation and other initiatives published in 2008:
- Increasing the insurance limits for insurance intermediaries.
- Increasing the minimum amount for a guarantee fund of insurance companies.
- Increasing the insurance limits for insurance intermediaries – **Communication of the European Commission**.
- Increasing the minimum amount for a guarantee fund of insurance companies – **Communication of the European Commission**.

2) Pending European legislation (including legislation published after 31 December 2008) and other initiatives of the European Commission:
- Draft directive on the approach to insurance and reinsurance activities and their performance – Solvency II (the proposal is a recodification of insurance-related directives and implements new rules for calculating solvency).

3) Acts that took effect in 2008:
- **Act No. 137/2008 Coll.** of 20 March 2008, amending Act No. 168/1999 Coll., on liability insurance for damage caused by operation of vehicle and on amendments to certain related acts (**Motor Third Party Liability Insurance**), as subsequently amended; Act No. 363/1999 Coll., on insurance and on amendment to some related acts (the Insurance Act), as subsequently amended; Act No. 56/2001 Coll., on the conditions for operation of vehicles on roadways and on amendment to Act No. 168/1999 Coll., on liability insurance for damage caused by operation of vehicle and on amendments to certain related acts (Motor Third Party Liability Insurance), as amended by Act. No. 307/1999 Coll., as subsequently amended; and Act No. 48/1997 Coll., on general health insurance and on changes and amendments of some related acts, as subsequently amended. The act became effective on 1 June 2008, with the exception of the provisions of Article I, clause 73, as regards Section 24, paragraph 1, and clause 89, as regards Section 24c, which become effective on 1 January 2009.
- **Act No. 248/2008 Coll. of 5 June 2008, amending Act No. 340/2006 Coll., on Activities of Occupational Pension Scheme Institutions from EU Member States in the Czech Republic** and on amendment to Act No. 48/1997 Coll., on general health insurance and on changes and amendments of some related acts, as subsequently amended. The act became effective upon its announcement on 4 July 2008.
- Full wording of Act No. 340/2006 Coll. was published in the Collection of Laws under No. 345/2008 Coll.

4) Pending Acts (including acts already adopted that have taken effect or will take effect after 31 December 2008):
- **Draft Insurance Act**, transposing Directive 2005/68/ES on reinsurance and Directive 2007/44/EC on acquisitions and increase of holdings in the financial

sector. The draft act is being discussed in the Parliament of the Czech Republic (Parliamentary Print No. 571). The proposed effective date is 1 January 2010.

- **Draft act on amendment of acts in connection with the enactment of the Insurance Act**. The draft act is being discussed in Parliament (Parliamentary Print No. 572). The proposed effective date is 1 January 2010.
- **Draft Pension Insurance Act** – phase II of the pension reform. The draft act is being discussed in Parliament (Parliamentary Print No. 825). The proposed effective date is 1 January 2010.
- **Draft act amending certain acts in connection with the enactment of the Pension Insurance Act**. The draft act is being discussed in Parliament (Parliamentary Print No. 826). The proposed effective date is 1 January 2010.

5) Secondary legislation:

- Decree No. 186/2008 Coll., amending Decree No. 205/1999 Coll. of the Ministry of Finance, implementing Act No. 168/1999 Coll., on liability insurance for damage caused by operation of vehicle and on amendments to certain related acts (Motor Third Party Liability Insurance), as amended by Decree No. 429/2002 Coll. and Decree No. 309/2004 Coll. The amendment to the Decree became effective on 1 June 2008.

APPENDIX 2: SUPPLEMENTARY TABLES

Table 8.1: Average interest rate

As at 31 Dec (%)		2004	2005	2006	2007	2008
Deposits	**households and small entrepreneurs**	1.33	1.24	1.23	1.34	1.55
	non-financial enterprises	1.14	0.99	0.97	1.17	1.80
Loans	**to households and small entrepreneurs**	8.09	7.53	7.46	8.06	6.81
	for consumption	14.86	14.36	14.26	14.99	13.40
	for real estate	6.15	5.57	5.51	6.11	5.05
	to non-financial enterprises	4.51	4.27	4.22	4.57	5.59

Source: CNB - ARAD

Table 8.2: Loans by type

As at 31 Dec (CZK bn)	2006	2007	2008	Year-on-year change	
				Abs.	(%)
Overdrafts and debit balances of current accounts	104.9	140.3	141.2	0.9	0.66
Consumer loans (excl. overdrafts and debit balances of current accounts)	101.7	128.9	161.8	32.9	25.51
Housing loans excl. mortgages	142.8	191.2	235.8	44.6	23.34
Mortgage loans for residential properties	288.7	398.2	468.1	69.8	17.54
Mortgage loans for non-residential properties	12.8	21.5	35.3	13.8	64.21
Other loans	236.0	271.3	281.3	10.0	3.68
Investment loans	292.3	363.3	423.2	59.9	16.49
Bridge loans	2.1	1.4	3.1	1.6	114.49
Trade receivables	40.2	37.5	34.1	-3.4	-9.12
Total	1,221.6	1,553.7	1,783.9	230.2	14.82

Source: CNB - ARAD

Table 8.3: Basic indicators of building savings development in the Czech Republic

As at 31 Dec			**2003**	**2004**	**2005**	**2006**	**2008**
New building savings contracts	**number**	2,097,338	314,650	430,233	516,385	579,730	705 463
	change (%)	62.1	-85.0	36.7	20.0	12.3	21.7
Average target value for new building s. contracts with private individuals	**value (CZK th.)**	201	223	228	236	285	303
	change (%)	36.7	11.1	2.3	3.5	20.8	6.3
Building savings contracts in savings phase[58]	**number**	6,300,831	5,899,300	5,573,874	5,297,522	5,132,595	5,070,510
	change (%)	29.4	-6.4	-5.5	-5.0	-3.1	-1.2
Awarded state contribution	**value (CZK th.)**	13.26	15.34	16.09	15.77	14.98	14.22
	change (%)	19.9	15.7	4.9	-2.0	-5.0	-5.0
Average state contribution awarded per building savings contract for the relevant year	**value (CZK th.)**	3,159	3,256	3,242	n/a	n/a	n/a
	change (%)	0.7	3.1	-0.4	0.0	n/a	n/a
Saved amount[58]	**value (CZK th.)**	237	287	329	360	385	401
	change (%)	31.4	21.2	14.6	9.4	6.9	4.2
Loans total [58]	**number**	685,740	786,483	857,875	900,653	942,944	971,176
of which: building saving schemes	**number**	488,850	549,698	582,867	587,501	580,352	569,870
bridging[59]	**number**	196,890	236,785	275,008	313,152	362,592	401,306
	change (%)	20.5	14.7	9.1	5.0	4.7	3.0
Loans total [58]	**value (CZK th.)**	63.6	84.2	108.1	135.5	179.3	227.4
of which: building saving schemes	**value (CZK th.)**	25.1	28.7	31.8	35.1	38.9	42.9
bridging[59]	**value (CZK th.)**	38.5	55.4	76.3	100.4	140.4	184.5
	change (%)	37.3	32.4	28.4	25.3	32.4	26.8
Loans total/saved amount	**ratio (%)**	26.9	29.3	32.8	37.6	46.6	56.7

Source: MoF

58 Closing balance of the period.
59 Loans under Section 5 (5) of Act No. 96/1993 Coll., on building savings schemes and state support for building savings schemes, as subsequently amended.

Table 8.4: Net assets in trusts domiciled abroad, by distributors

As at 31 Dec 2008	Net assets (CZK bn)	Share in total value (%)	Year-on-year change (%)
Československá obchodní banka	75.8	61.61	-4.83
Česká spořitelna	16.9	13.70	-14.11
ING Bank	12.9	10.47	-30.88
Conseq Investment Management	4.4	3.59	-27.96
Komerční banka	3.9	3.18	57.08
Raiffeisenbank	2.3	1.91	-25.22
HSBC Bank	2.0	1.63	-28.51
Pioneer Investments	1.8	1.43	-40.88
Citibank	1.2	0.95	-52.04
HVB Bank Czech Republic	0.6	0.49	-73.10
Československá obchodní banka	75.8	61.61	-4.83
Other	1.3	1.05	-35.11
Total	123.0	100.00	-13.42

Source: AKAT

Table 8.5: Net assets of domestic trusts, by management companies

As at 31 Dec 2008	Net assets (CZK bn)	Share in total value (%)	Year-on-year change (%)
Investiční společnost České spořitelny	49.8	41.14	-38.45
Investiční kapitálová společnost KB	36.1	29.79	-25.91
Pioneer česká investiční společnost	8.7	7.19	-20.99
ČSOB investiční společnost	6.9	5.69	-37.90
ČP INVEST investiční společnost	5.6	4.66	-11.19
AXA investiční společnost a.s.	2.2	1.84	84.78
REICO investiční společnost ČS, a.s.	1.7	1.37	37.70
J&T ASSET MANAGEMENT, IS	1.4	1.12	-20.56
AKRO investiční společnost	0.4	0.36	-48.41
AIG Funds Central Europe správ.spol.	0.0	0.00	-100.00
Other	8.3	6.83	-15.78
Total	121.1	100.00	-30.02

Source: AKAT

Table 8.6: Allocation of assets of pension funds

As at 31 Dec (market prices, CZK bn)		2004	2005	2006	2007	Share in 2007 (%)
Bonds	69.1	89.4	110.0	119.5	144.9	78.80
Treasury bills	18.1	9.7	5.5	6.4	6.4	3.49
Shares and unit certificates	6.4	9.2	14.6	17.5	11.9	6.47
Money and other assets	8.5	15.1	12.5	18.7	20.7	11.24
Total	102.1	123.4	142.5	162.1	183.9	100.00

Source: APF Czech Republic

Table 8.7: Placement of technical reserves

As at 31 Dec (CZK bn)	2007			2008			Abs. change			Year-on-year change (%)		
	LI	NLI	total	LI	NLI	total	LI	NLI	total	LI	NLI	total
Bonds issued by Member State or its central bank and bonds guaranteed by Member State	85.6	20.6	106.2	93.0	30.9	123.9	7.4	10.3	17.7	8.63	50.08	16.66
Bonds issued by banks and similar credit institutions of Member States	12.7	3.6	16.3	15.1	3.6	18.7	2.4	0.0	2.5	19.27	0.45	15.14
Listed bonds issued by commercial companies	17.1	6.3	23.4	16.2	5.2	21.4	-0.9	-1.1	-2.0	-5.46	-17.35	-8.68
Treasury bills	3.3	5.4	8.7	0.2	3.3	3.5	-3.1	-2.2	-5.2	-93.41	-39.90	-60.18
Listed municipal bonds	1.9	0.8	2.8	2.1	0.8	2.9	0.1	0.0	0.1	5.35	-1.11	3.40
Credits, loans and other receivables	0.0	0.2	0.2	0.0	0.0	0.0	0.0	-0.2	-0.2	70.40	-90.44	-89.43
Bills of exchange guaranteed by bank surety or bank aval	0.1	0.1	0.3	0.0	0.1	0.1	-0.1	0.0	-0.1	-88.14	3.35	-45.98
Real estate on the territory of Member States	0.9	1.9	2.8	0.7	2.4	3.1	-0.2	0.5	0.3	-25.44	25.83	9.37
Mortgage bonds	13.4	8.8	22.2	13.0	7.8	20.7	-0.4	-1.0	-1.4	-2.97	-11.63	-6.40
Listed shares of stock	8.5	4.7	13.2	8.8	4.2	13.0	0.4	-0.6	-0.2	4.31	-11.85	-1.50
Deposits and deposits confirmed by deposit certificate, deposit receipt or similar document	10.0	7.4	17.4	11.2	8.7	19.9	1.2	1.3	2.5	11.97	17.74	14.43
Works of art	0.0	0.1	0.1	0.0	0.1	0.1	0.0	0.0	0.0	-	-1.54	-1.54
Bonds issued by EIB, ECB, EBRD or IBRD	12.8	1.3	14.0	12.7	1.5	14.1	-0.1	0.2	0.1	-0.96	16.13	0.57
Securities issued by collective investment unit	26.0	2.9	28.8	23.5	1.9	25.4	-2.5	-0.9	-3.4	-9.59	-32.86	-11.91
Foreign securities traded on regulated market of OECD states	5.6	1.8	7.5	9.9	2.1	12.0	4.3	0.2	4.5	75.88	13.53	60.43
Loans to insured persons	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	-67.57	-	-67.57
Derivatives	0.0	0.0	0.0	0.2	0.0	0.2	0.2	0.0	0.2	-	-	-
Receivables from reinsurance companies	0.7	17.1	17.8	0.8	17.4	18.2	0.1	0.3	0.4	11.94	1.68	2.09
Other financial placement	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.00	0.00	0.00
Financial placements total	198.7	83.1	281.8	207.4	90.0	297.4	8.7	6.9	15.6	4.37	8.29	5.52

Source: CNB