

# **KOSOVO CREDIT GUARANTEE FUND**

**Independent Auditors' Report and  
Financial Statements for the year  
ended December 31, 2017**

## CONTENTS

	Page
Independent Auditors' Report	1
Statement of Financial Position	3
Statement of Comprehensive Income	4
Statement of Changes in Funds balance	5
Statement of Cash Flows	6
Notes to the Financial Statements	7 - 21



## INDEPENDENT AUDITORS' REPORT

To the Board of Directors of Kosovo Credit Guarantee Fund

Report on the Audit of the Financial Statements

### Opinion

We have audited the financial statements of Kosovo Credit Guarantee Fund (the "Fund" or "KCGF"), which comprise: the statement of financial position as at December 31, 2017, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion the accompanying financial statements present fairly, in all material respects, the financial position of the Fund as at December 31, 2017, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

### Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Fund in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRSs, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Fund's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Fund or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Fund's financial reporting process.



## Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Fund's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Fund to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

BDO KOSOVA L.L.C.

BDO Kosova L.L.C.

June 12, 2018

Str. Perandori Justinian, No.120

10 000 Pristina, Kosovo



Kosovo Credit Guarantee Fund  
Statement of Financial Position  
As at December 31, 2017

	Notes	As at December 31, 2017 (EUR)	As at December 31, 2016 (EUR)
<b>ASSETS</b>			
<b>Current assets</b>			
Cash and cash equivalents	4	7,567,694	7,379,611
Deposits	5	8,500,000	-
Receivables and other receivables	6	151,665	8,209
<b>Total current assets</b>		<b>16,219,359</b>	<b>7,387,820</b>
<b>Non-current assets</b>			
Property, plant and equipment	7	25,939	-
Intangible assets	8	52,600	-
<b>Total non-current assets</b>		<b>78,539</b>	<b>-</b>
<b>TOTAL ASSETS</b>		<b>16,297,898</b>	<b>7,387,820</b>
<b>EQUITY AND LIABILITIES</b>			
<b>Current liabilities</b>			
Deferred Guarantee Fees		166,635	35,609
Provision losses for loan guarantees		88,514	10,219
Deferred revenues from donated assets	9	72,716	-
Accrued expenses		3,244	-
<b>Total current liabilities</b>		<b>331,109</b>	<b>45,828</b>
<b>EQUITY</b>			
Capital	10	15,790,921	7,345,141
Accumulated profit/(loss)		175,868	(3,149)
<b>Total equity</b>		<b>15,966,789</b>	<b>7,341,992</b>
<b>TOTAL EQUITY AND LIABILITIES</b>		<b>16,297,898</b>	<b>7,387,820</b>

Authorized for issue by the management and signed on its behalf on June 12, 2018.

  
Besnik Berisha  
Managing Director



  
Vjosa Balaj  
Senior Finance Manager

The accompanying notes on pages 7 to 21 form an integral part of these financial statements

Kosovo Credit Guarantee Fund  
Statement of Comprehensive Income  
For the year ended December 31, 2017

	Notes	Year ended 31 December 2017 (EUR)	Year ended 31 December 2016 (EUR)
Guarantee fees	11	134,165	7,070
Other income	12	269,364	-
<b>Total income</b>		<b>403,529</b>	<b>7,070</b>
Personnel expenses	13	(87,043)	
Depreciation	7,8	(20,415)	
Operative expenses	14	(38,759)	
Net provision losses for guarantees	15	(78,295)	(10,219)
<b>Profit/(Loss) for the year</b>		<b>179,017</b>	<b>(3,149)</b>
Other comprehensive income		-	-
<b>Total comprehensive profit / loss for the year</b>		<b>179,017</b>	<b>(3,149)</b>

The accompanying notes on pages 7 to 21 form an integral part of these financial statements.

Kosovo Credit Guarantee Fund  
Statement of Changes in Funds balance  
For the year ended December 31, 2017

	Capital (EUR)	Accumulated (loss)/profit (EUR)	Total (EUR)
As at January 1, 2016	-	-	-
Paid in capital	7,345,141	-	7,345,141
Loss for the year	-	(3,149)	(3,149)
As at December 31, 2016	<u>7,345,141</u>	<u>(3,149)</u>	<u>7,341,992</u>
Addition paid in capital	8,445,780	-	8,445,780
Profit for the year	-	179,017	179,017
As at December 31, 2017	<u>15,790,921</u>	<u>175,868</u>	<u>15,966,789</u>

The accompanying notes on pages 7 to 21 form an integral part of these financial statements.

Kosovo Credit Guarantee Fund  
Statement of Cash Flows  
For the year ended December 31, 2017

	Notes	Year ended 31 December 2017 (EUR)	Year ended 31 December 2016 (EUR)
<b>Cash flow from operating activities:</b>			
Profit/(Loss) for the year		179,017	(3,149)
<b>Adjustments for:</b>			
Depreciation	7,8	20,415	-
		<u>199,432</u>	<u>(3,149)</u>
<b>Movements in working capital:</b>			
Increase in receivables		(143,456)	(8,209)
Increase in deferred guaranty fees		131,026	35,609
Increase in provision losses for loan guarantees		78,295	10,219
Increase in deferred revenues from donated assets		72,715	-
Increase in accruals		<u>3,244</u>	<u>-</u>
<b>Net cash generated in operating activities</b>		<u>341,256</u>	<u>34,470</u>
<b>Cash flow from investing activities:</b>			
Additional assets		(98,953)	-
Deposits		<u>(8,500,000)</u>	<u>-</u>
<b>Net cash used in investing activities</b>		<u>(8,598,953)</u>	<u>-</u>
<b>Cash flow from financing activities:</b>			
Paid in capital		<u>8,445,780</u>	<u>7,345,141</u>
<b>Net cash generated in financing activities</b>		<u>8,445,780</u>	<u>7,345,141</u>
<b>Net increase in cash and cash equivalents during the year</b>		<b>188,083</b>	<b>7,379,611</b>
Cash and cash equivalents at the beginning of the year		<u>7,379,611</u>	<u>-</u>
<b>Cash and cash equivalents at the end of the year</b>	4	<u><u>7,567,694</u></u>	<u><u>7,379,611</u></u>

The accompanying notes on pages 7 to 21 form an integral part of these financial statements.



## 1. GENERAL

The Kosovo Credit Guarantee Fund is an independent and sustainable institution that issues guarantee to financial institutions to cover the risk for MSME loans.

KCGF was established, as a result of joint initiative between International Donors in Kosovo (mainly USAID and KfW) and Government of Kosovo, in January 2016, based on the Law on Establishment of the Kosovo Credit Guarantee Fund.

Through "Law on Establishment of the Kosovo Credit Guarantee Fund" Law No. 05/L -057 established the KCGF as an independent, not-for-profit, public institution, autonomous, legal entity and determined its authority, structure, governance, operations, scope, and policies and procedures for the issuance of Credit Guarantees.

The founding law of the KCGF was initiated by MTI, while USAID in Kosovo, through the EMPOWER Credit Support Program (ECS) supported the institution on becoming operational. The law entered into force on 23 January 2016. KCGF capital consists of funds donated by MTI, USAID and KfW.

KCGF is created to help meet the need for increased access to finance for micro, small and medium enterprises in Kosovo, in order to create jobs, increase local production and value added services, and improve the trade balance and enhance financing opportunities for MSMEs.

KCGF is an independent, autonomous, legal entity established by Law, with full legal personality, and a legal identity that is separate and distinct from the KCGF Management Board and Executives.

KCGF is governed by a Board of Directors composed of seven members who collectively combine years of experience in financial management, risk management, commercial or financial law and auditing. The Board provides leadership and oversight for all KCGF's activities.

KCGF is established for the purpose of providing partial risk credit guarantees to financial institutions on loans to MSMEs up to the coverage amount prescribed by the LKCGF and the Guarantee Agreement between KCGF and the financial institution.

For the purpose of its main function, KCGF is responsible for:

- a. Issuing Credit Guarantees in accordance with the LKCGF and internal policies approved by the Board of Directors;
- b. Setting the conditions for registering qualified Kosovo Financial Institutions in the KCGF reflected in the Policy on the Registration of Financial Institutions;
- c. Setting the conditions for issuing Credit Guarantees by the KCGF.
- d. Setting the Guarantee Fees of the KCGF.
- e. Depositing or investing directly or through delegation of authority the assets of KCGF within the limitations of the LKCGF.
- f. Paying Payable Amounts on Credit Guarantees to Registered Financial Institutions pursuant to the provisions of the LKCGF and the Guarantee Agreement, in accordance with the provisions of the LKCGF and the Policy on Handling Claims.

## **1. GENERAL (CONTINUED)**

KCGF's minimum capital is 300,000.00 Euros as defined in the Article 10 of the LKCGF. KCGF's governing bodies are the Board of Directors and the Managing Director. The Board of Directors shall be the highest governance body of KCGF. The KCGF's fiscal identification number is 601642061.

KCGF operations and all administrative activities since June 10, 2017 are independent and under the management of the Fund backed by technical assistance from USAID.

On December 6, 2017 The Kosovo Credit Guarantee Fund (FKGK) signed the Guarantee Agreement with the Swedish International Development Cooperation Agency (Sida), represented by the Embassy of Sweden in Pristina.

The support of the guaranteed portfolio of KCGF by Sida, will further enhance the ability of the Fund to ensure a higher level of credit guarantees, while at the same time increasing the financial sustainability of the sector. The sustainability will reflect the facilitation of financial intermediation hence increase of access to finance of micro, small and medium size enterprises, in order to promote economic growth and job creation for woman, man and youth of all ethnicities in Kosovo.

## **2. SIGNIFICANT ACCOUNTING POLICIES**

### **2.1 Basis of preparation and statement of compliance**

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (IASB). The financial statements have been prepared using the measurement bases specified by IFRS for each type of asset, liability, income and expense. The measurement bases are more fully described within the Note below.

The preparation of these financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Fund's accounting policies.

### **2.2 New standards, interpretations and amendments effective from 1 January 2017**

A number of new standards issued by International Accounting Standards Board, interpretations and amendments issued by the International Financial Reporting Interpretations Committee are effective for the first time for periods beginning on (or after) 1 January 2017.

Note: not all new standards and interpretations effective for the first time for periods beginning on (or after) 1 January 2017 effect the Fund financial statements.

IAS 8:28 - The effect of the initial application of an IFRS on the Fund's accounting policies.

## 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### 2.2 New standards, interpretations and amendments effective from 1 January 2017 (continued)

The following new standards, amendments and interpretations are effective for the first time for periods beginning on or after 1 January 2017:

- Annual Improvements to IFRSs (2014 - 2016 Cycle): IFRS 12 Disclosure of interests in other entities
- IAS 12 Income Taxes (Amendment - Recognition of Deferred Tax Assets for Unrealized Losses)
- IAS 7 Statement of Cash Flows (Disclosure Initiative Amendments).

The scope of IFRS 12 was clarified to make it clear that the disclosure requirements in this Standard, except for those in paragraphs B10 - B16, apply to interests irrespective of whether they are classified as held for sale, as held for distribution to owners or as discontinued operations in accordance with IFRS 5.

The amendment to IAS 12 Income Taxes clarifies the accounting for deferred tax assets related to debt instruments measured at fair value but are not deemed to be impaired (for example, an investment in a fixed rate bond where the fair value has declined due to changes in interest rates, but the asset is not considered to have become impaired in value). Specifically it clarifies that deferred taxes should be recognized for deductible temporary differences arising from unrealized losses on debt instruments measured at fair value if all other recognition criteria for deferred taxes are met, regardless of whether it is planned to recover the instrument through sale or by holding it to maturity.

The amendment to IAS 7 aims to improve information about changes in liabilities arising from financing activities. One way to provide this disclosure would be to provide a reconciliation of the opening and closing carrying amounts for each item for which cash flows have been or would be classified as financial activities. The reconciliation would include:

- Changes from financing cash flows;
- Changes arising from obtaining or losing control of subsidiaries or other businesses;
- Other non-cash exchanges (e.g. changes in foreign exchange rates, new finance leases and changes in fair value);

There were no new standards or interpretations effective for the first time for periods beginning on or after 1 January 2017 that had a significant effect on the financial statements.

### 2.3 New standards, interpretations and amendments effective in periods after year end December 31, 2017

There are a number of standards and interpretations which have been issued by the International Accounting Standards Board that are effective in future accounting periods that the Fund has decided not to adopt early. The most significant of these are:

- IFRS 9 Financial Instruments (mandatorily effective for periods beginning on or after 1 January 2018); and
- IFRS 16 Leases (mandatorily effective for periods beginning on or after 1 January 2019).

## 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### 2.3 New standards, interpretations and amendments effective in periods after year end December 31, 2017 (continued)

#### IFRS 9 Financial Instruments

The Fund has identified that the adoption IFRS 9, which replaces IAS 39 Financial Instruments:

The Fund will need to apply from 1 January 2018 an expected credit loss model when calculating impairment losses on its trade and other receivables (both current and non-current). This will result in increased impairment provisions and greater judgement due to the need to factor in forward looking information when estimating the appropriate amount of provisions. In applying IFRS 9 the Fund must consider the probability of a default occurring over the contractual life of its trade receivables and contracts asset balances on initial recognition of those assets.

#### IFRS 16 Leases

Adoption of IFRS 16 will result in the Fund recognizing right of use assets and lease liabilities for all contracts that are, or contain, a lease. For leases currently classified as operating leases, under current accounting requirements the Fund does not recognize related assets or liabilities, and instead spreads the lease payments on a straight-line basis over the lease term, disclosing in its annual financial statements the total commitment.

#### Other

The Fund does not expect any other standards issued by the IASB, but not yet effective, to have a material impact on the Fund.

The following is a list of other new and amended standards which, at the time of writing, had been issued by the IASB but which are effective in future periods. The amount of quantitative and qualitative detail to be given about each of the standards will, much like the amount of detail to be given about IFRSs 9, 15 and 16, depend on each Fund's own circumstances.

- IFRIC 22 Foreign Currency Translations and Advance Consideration (effective 1 January 2018)
- Amendments to IFRS 2 classification and Measurement of Share-based payment Transactions (effective 1 January 2018)
- Amendments to IFRS 4: Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (effective 1 January 2018)
- Amendments to IAS 40: Transfers of Investment Property (effective 1 January 2018)
- Annual Improvements to IFRS Standards 2014-2016 cycle dealing with matters in IFRS 1 First-time Adoption and IAS 28 Investments in Associates and Joint Ventures (effective 1 January 2018)
- IFRIC 23 Uncertainty over Income Tax Positions (effective 1 January 2019)
- Amendments to IFRS 9 Prepayment Features with Negative Compensation (effective 1 January 2019)
- Amendments to IAS 28: Long-term Interests in Associates and Joint Ventures (effective 1 January 2019)
- IFRS 17 Insurance Contracts (effective 1 January 2021)

## **2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

### **2.4 Financial assets**

The Fund classifies its financial assets in the following categories: financial assets at fair value through profit or loss, loans and receivables, held to maturity and available - for - sale financial assets. Management determines the classification of its investments at initial recognition.

#### **Financial assets at fair value through profit or loss**

Financial assets at fair value through profit or loss are financial assets held-for-trading. A financial asset is classified in this category if acquired principally for the purpose of selling in the short-term. Assets in this category are classified as current assets. The Fund has no assets classified in this category.

#### **Receivables**

Receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets. As of the reporting date this category includes cash and cash equivalents.

### **2.5 Cash and cash equivalents**

Cash and cash equivalents include cash in hand and balances with banks. The Fund has a bank account opened with Central Bank of the Republic of Kosovo and a current account with Banka për Biznes.

### **2.6 Funds balance**

Funds Balance provided by the Government of the Republic of Kosovo and USAID as a grant. During December 2017, grant agreements are signed in amount of 7.450 million EUR between the German Development Bank (KfW) and the Ministry of Finance, dedicated to increasing the KCGF Capital for 7.0 million EUR, whereas 450 thousand EUR is for technical assistance.

### **2.7 Current and deferred income taxes**

According to LKCGF, the Fund is exempt from Corporate Income Tax, VAT, and tax on dividends, interest or investment income earned from funds on credit guarantees or investments, and any other levy, withholding or tax to any aspect of the operations of the Fund.

### **2.8 Revenue recognition**

Revenue from services is recognized when all the following conditions are satisfied:

- the amount of revenue can be measured reliably;
- it is probable that the economic benefits associated with the transaction will flow to the entity;
- the stage of completion of the transaction at the statement of financial position date can be measured reliably; and
- the cost incurred for the transaction and the cost to complete the transaction can be measured reliably

## 2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### 2.8 Revenue recognition (continued)

The Fund's revenues are:

- (i) revenues from guarantee fees
- (ii) interest from investment

#### *Guarantee Fees*

Once the loan is accepted and put under guarantee, the guarantee fee is also calculated. The guarantee fee is calculated based on the actual guarantee fee percentage specified for a Guarantee Agreement multiplied by the Approved Amount of the guarantee. The income from the guarantee fee is recognized on accrual basis for a period of 12 months. The guarantee fees are recognized as revenues in statement of comprehensive income at the end of each month by debiting Accrual Guarantee Fee and credit Guarantees Fees Income.

#### *Interest from investment*

Investment mean investments of surplus funds where the over-riding principle guiding the investment of surplus funds is to ensure that the primary objectives of safeguarding KCGF's assets and limiting its risk are balanced with the achievement of a satisfactory return.

### 2.9 Provisions

Provisioning policy specifies the process of setting aside certain reserves for all credits that are placed under guarantees that are expected or have incurred credit loss. The provisioning policy is made in accordance with IFRS 9. The impairment of credit guarantees is done in three stages, based on changes in credit quality since initial recognition. The information provided by RFI regarding credit classification will be the key trigger for moving credit guarantee into stages and for measuring credit risk. Impairment in first stage is accounted for all credit guarantees irrespective of the credit quality, on the basis of expected loss over a period of 12 months. The credit guarantee will move to second stage (or from second to third) if there is a significant deterioration in the credit quality, if the contractual cash flows on the financial asset are not fully recoverable in the event of default. In both these stages, the impairment allowance is recognized based on the lifetime expected losses. The transfer of financial assets from one stage to another is symmetrical, which means that any financial asset can move back, if there is a significant improvement in the credit quality.

### 2.10 Commitments contingencies

Contingent liabilities are not recognized in the financial statements. They are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote. A contingent asset is not recognized in the financial statements but disclosed when an inflow of economic benefits is probable. The amount of a contingent loss is recognized as a provision if it is probable that future events will confirm that, a liability incurred as at the statement of financial position date and a reasonable estimate of the amount of the resulting loss can be made.



### **3. FINANCIAL RISK MANAGEMENT**

#### **3.1 Introduction and overview**

Risk is defined as effect of uncertainty events and their outcomes that may have a significant effect on KCGF operations. Risk management is the process of evaluating and responding to risks for the purpose of reducing those risks to acceptable levels. The evaluation of risk is based on identification of threats, as well as the likelihood of the threats being realized and the potential impact on the KCGF. Risk management uses the results of risk assessments to make decisions and to coordinate activities to direct and control an organization with regard to risk.

The KCGF Risk Management Policy sets out the key principles which in order to establish an appropriate system of risk oversight and management. The key principles for risk management are implemented in Guarantee Agreement, in existing policies and procedures as well as methodologies and tools for risk measuring, monitoring and reporting. Together these form the KCGF risk management framework.

#### **3.2 Risk Governance Structure**

The KCGF risk governance structure emphasizes oversight and control of risk and defines the processes and mechanisms by which decisions about risks are taken and implemented. KCGF's risk management governance structure begins with oversight by the Board of Directors. The Board receives regular updates on the key risks of KCGF - including a comprehensive summary of KCGF's risk profile and performance of the portfolio against defined goals, presented quarterly to the Board. The Board set forth risk appetites for credit risk and liquidity risk and approves key risk policies, limits, strategies. The Board also ensures that KCGF is taking appropriate measure to achieve prudent balance between risk and reward.

The Board of Directors has established two committees to supervise specific areas and to prepare topics for consideration by the Board: Risk Management Committee and Audit Committee.

Risk Management Committee - the committee reviews and submits recommendations to the Board of Directors regarding KCGF risk appetites, risk policies, risk instructions, capital, leverage, liquidity, products and services from a risk perspective, and loan portfolio credit quality.

Audit Committee -the committee operates as a preparatory committee for the Board of Directors with respect to accounting and auditing matters, including related risk matters.

In general, both committees assist the Board of Directors in ensuring strict risk management within KCGF and in ensuring that risk management and risk reporting are always compliant with law and the KCGF general principles.

### 3. FINANCIAL RISK MANAGEMENT (CONTINUED)

#### 3.3 Credit risk

Credit risk is the risk of loss resulting from the failure of a borrower to honor its financial or contractual obligations to a bank. KCGF's risks lies, correspondingly, with the banks. Should impaired loans at a particular bank increases, putting their portfolio at risk, this will in turn increase KCGF's, in the sense that KCGF may be called on the guarantees issued. This will have an impact on KCGF's capital position and expected fee incomes. Therefore, KCGF's counterparties' (RFI) credit assessment and their policies will influence the quality of KCGF's guaranteed portfolio.

For the purpose of Registering Financial Institutions, KCGF has implemented a Registration Policy which is aimed at ensuring registration of only financial institutions that are responsive and transparent and provide evidence of their ability to comply with KCGF requirements. The registration policy sets the key principles that financial institutions should have in order to be registered in KCGF:

- A sound capital base and financial position
- A good reputation in the market
- A willingness to further penetrate the MSME segment
- A willingness to reduce collateral requirements as a quid pro quo for KCGF's partial loan guarantees
- Sound loan underwriting policies and procedures

For ensuring the guarantee commitments that KCGF is taking within its risk bearing capacity and that its portfolio is well diversified, KCGF has adopted an Allocation Policy. This policy determines the risk appetite that KCGF is willing to take and sets the methodology for evaluating RFI exposure. The policy also sets the methodology for assessing RFI and allocating limits to RFI. The methodology defines that the main criteria for allocating an initial limit are market share and risk profile. However, exposure limits may be adjusted by the KCGF. Reasons for adjustment would include failure to use the allocated limit significantly or at all, poor quality of loans submitted for guarantee, or safety and soundness issues in the overall condition of the bank.

### 3. FINANCIAL RISK MANAGEMENT (CONTINUED)

#### 3.4 Liquidity risk

Effective liquidity risk governance is essential in order to maintain the confidence of donors and RFI, and to enable the core business to continue to generate revenue, even under adverse circumstances. Reliable arrangements, analysis of liquidity requirements, and contingency planning (for example, a stand-by line of credit, or counter guarantee arrangement) are crucial elements of strong liquidity.

KCGF acknowledges that capital that it is holding as liquid assets should provide support towards the achievement of its objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable performance measurement techniques that balance risk and reward, within the context of effective risk management.

For the purposes of optimizing potential returns within acceptable risk parameters, KCGF has prepared an investment policy that clearly sets out an investment framework consistent with KCGF mandate and its strategic objectives.

31 December 2017				
	Current			
	Up to 1 year (EUR)	1 to 2 years (EUR)	2 to 5 years (EUR)	Over 5 years (EUR)
<b>Financial assets</b>				
Cash and cash equivalents	7,567,694	-	-	-
Deposits	-	8,500,000	-	-
<b>Total financial asset</b>	<b>7,567,694</b>	<b>8,500,000</b>	<b>-</b>	<b>-</b>
<b>Financial liabilities</b>				
Payables and other liabilities	258,393	-	-	-
<b>Total financial liabilities</b>	<b>258,393</b>	<b>-</b>	<b>-</b>	<b>-</b>

31 December 2016				
	Current			
	Up to 1 year (EUR)	1 to 2 years (EUR)	2 to 5 years (EUR)	Over 5 years (EUR)
<b>Financial assets</b>				
Cash and cash equivalents	7,379,611	-	-	-
<b>Total financial asset</b>	<b>7,379,611</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Financial liabilities</b>				
Payables and other liabilities	45,828	-	-	-
<b>Total financial liabilities</b>	<b>45,828</b>	<b>-</b>	<b>-</b>	<b>-</b>

#### 3.5 Operational Risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Operational risk can be created by a wide range of different external events ranging from power failures to floods or earthquakes.

### 3. FINANCIAL RISK MANAGEMENT (CONTINUED)

#### 3.5 Operational Risk (continued)

Similarly, operational risk can arise due to internal events such as the potential for failures or inadequacies in any of the KCGF's processes and systems, or those of its outsourced service providers. Operational risk arising from human resources management may refer to a range of issues such as mismanaged or poorly trained employees; the potential of employees for negligence, willful misconduct; conflict of interests; fraud; rogue trading; and so on. The KCGF's operational risk management focuses on proactive measures in order to ensure business continuity as well as the accuracy of information used internally and reported externally, a competent and well-informed staff, and its adherence to established rules and procedures as well as on security arrangements to protect the physical and ICT infrastructure of the KCGF.

##### *KCGF's Operational Risk Management Framework:*

- I) Clear strategies adopted by the Board of Directors and oversight exercised by Senior Management;
- II) Strong internal operational risk culture (Internal operational risk culture is taken to mean the combined set of individual and corporate values, attitudes, competencies and behavior that determine an institution's commitment to and style of operational risk management) and internal control culture, emphasizing on dual controls;
- III) High standards of ethics and integrity, and
- IV) Commitment to effective corporate governance, including, among others, segregation of duties, avoidance of conflicts of interest, and clear lines of management responsibility, accountability and reporting, as reflected in the KCGF's governance documents. All levels of staff shall understand their responsibilities with respect to operational risk management.

Insurance policies may be used to confront losses which may occur as a result of events such as third-party claims resulting from errors and omissions, employee or third-party fraud, and natural disasters.

#### 3.6 Financial instruments presented at fair value

The financial assets measured according to the fair value in the statement of financial position in accordance with the hierarchy of the fair value are shown in the next table. This hierarchy groups the financial assets and liabilities into three levels that are based on the significance of the incoming data used during the measurement of the fair value of the financial assets. Fair value hierarchy is as follows:

- **Level 1:** quoted prices (not adjusted) on the active markets for identical assets or liabilities;
- **Level 2:** other incoming data, aside from the quoted prices, included in Level 1 which are available for asset or liability observing, directly (i.e. as prices), or indirectly (i.e. made of prices) and
- **Level 3:** incoming data on the asset or liability that are not based on data available for market observing

As of 31 December 2017, the Fund has no financial assets measured at fair value.

### 3. FINANCIAL RISK MANAGEMENT (CONTINUED)

#### 3.7 Financial instruments that are not presented at fair value

The following table summarizes the carrying amounts and fair values to those financial assets and liabilities that are not presented in the Statement of financial position at their fair value:

	Carrying value 2017 (EUR)	Fair value 2017 (EUR)
<b>Financial assets</b>		
Cash and cash equivalents	7,567,694	7,567,694
Deposits	8,500,000	8,500,000
<b>Total financial assets</b>	<b>16,067,694</b>	<b>16,067,694</b>
<b>Financial liabilities</b>		
Payables and other liabilities	258,393	258,393
<b>Total financial liabilities</b>	<b>258,393</b>	<b>258,393</b>

### 4. CASH AND CASH EQUIVALENTS

	As at December 31 2017 (EUR)	As at December 31 2016 (EUR)
Cash at Central Bank of Kosovo	7,542,060	7,379,611
Current Accounts	25,224	-
Petty cash	410	-
<b>Total cash and cash equivalents</b>	<b>7,567,694</b>	<b>7,379,611</b>

### 5. DEPOSITS

The total deposits invested during 2017 are in amount of 8,500,000 EUR. The investments, which should have a maximum maturity of 5 years, are limited to organizations that meet the criteria as approved by KCGF's Board of Directors.

### 6. ACCOUNTS RECEIVABLE AND OTHER RECEIVABLES

	As at December 31 2017 (EUR)	As at December 31 2016 (EUR)
Receivable from clients	65,495	8,209
Accrual interest of bank deposits	69,493	-
Advances	16,677	-
<b>Total receivables</b>	<b>151,665</b>	<b>8,209</b>

**7. PROPERTY, PLANT AND EQUIPMENT**

	Equipment	IT Equipment	Office furniture	Total
	(EUR)	(EUR)	(EUR)	(EUR)
<b>Historical cost</b>				
As at January 1, 2016	-	-	-	-
Additions during the period	-	-	-	-
<b>As at December 31, 2016</b>	-	-	-	-
Transfer	1,972	50,431	19,947	72,350
Additions during the period	-	-	-	-
<b>As at December 31, 2017</b>	<b>1,972</b>	<b>50,431</b>	<b>19,947</b>	<b>72,350</b>
<b>Accumulated depreciation</b>				
As at January 1, 2016	-	-	-	-
Depreciation for the period	-	-	-	-
<b>As at December 31, 2016</b>	-	-	-	-
Transfer	1,100	16,901	15,890	33,891
Depreciation for the period	369	9,441	2,710	12,520
<b>As at December 31, 2017</b>	<b>1,469</b>	<b>26,342</b>	<b>18,600</b>	<b>46,411</b>
<b>NET VALUE</b>				
As at December 31, 2017	<b>503</b>	<b>24,089</b>	<b>1,347</b>	<b>25,939</b>
As at December 31, 2016	-	-	-	-

After June 10, 2017 KCGF has been transferred all the competencies related to KCGF, also transferring the assets that were managed until then under USAID management.



## 8. INTANGIBLE ASSETS

	Software (EUR)	Total (EUR)
Historical cost		
As at January 1, 2016	-	-
Additions during the period	-	-
As at December 31, 2016	-	-
Transfer	66,825	66,825
Additions during the period	5,922	5,922
As at December 31, 2017	72,747	72,747
Accumulated depreciation		
As at January 1, 2016	-	-
Depreciation for the period	-	-
As at December 31, 2016	-	-
Transfer	12,252	12,252
Depreciation for the period	7,895	7,895
As at December 31, 2017	20,147	20,147
NET VALUE		
As at December 31, 2017	52,600	52,600
As at December 31, 2016	-	-

## 9. DEFERRED REVENUES FROM DONATED ASSETS

	As at December 31 2017 (EUR)	As at December 31 2016 (EUR)
Equipment	503	-
IT Equipment	24,090	-
Office furniture	1,346	-
Software	46,777	-
Total in kind contributions	72,716	-

## 10. CAPITAL

Funds provided to the KCGF by the Government of the Republic of Kosovo and USAID as a grant.

As at 31 December 2016 Funds consist:

- Funds received from USAID in the amount of EUR 5,345,141.
- Funds received from Government of Republic of Kosovo (through Ministry of Trade and Industry) in the amount of EUR 2,000,000.

Additional grant funds during 2017:

- Funds received from KfW in the amount of EUR 7,000,000.
- Funds received from Government of Republic of Kosovo in the amount of EUR 1,000,000.
- Funds received from USAID in the amount of EUR 445,780.

**11. GUARANTEE FEES**

	Year ended December 31, 2017 (EUR)	Year ended December 31, 2016 (EUR)
Guarantee fees	134,165	7,070
<b>Total guarantee fees</b>	<b>134,165</b>	<b>7,070</b>

Once the loan is accepted and put under guarantee, the guarantee fee is also calculated. The guarantee fee is calculated based on the actual guarantee fee percentage specified for a Guarantee Agreement (2%) multiplied by the Approved Amount of the guarantee. The income from the guarantee fee is recognized on accrual basis for a period of 12 months. The guarantee fees are recognized as revenues in statement of comprehensive income at the end of each month by debiting Accrual Guarantee Fee and credit Guarantees Fees Income.

**12. OTHER INCOME**

	Year ended December 31, 2017 (EUR)	Year ended December 31, 2016 (EUR)
Funds for operative expenses	179,555	-
Depreciation on donated assets	20,316	-
Interest from deposits	69,493	-
<b>Total other income</b>	<b>269,364</b>	<b>-</b>

Funds for operative expenses are the purpose of the activity of USAID to support KCGF as it grows its nascent business of providing partial credit guarantees to facilitate expansion of local bank lending to the micro-, small-, and medium-enterprise (MSME) sector in Kosovo. The activity will cover KCGF's business operating costs (such as salaries, office rent, etc., for a limited time after the expiration of USAID's ECS project on June 10, 2017. Based upon KCGF's current and anticipated cost structure and burn rate, and detailed financial forecasts including growing utilization rates and revenues, the proposed amount of funding should be sufficient to enable KCGF to achieve financial self-sufficiency (positive cash-flow from operations) not later than the end of 2018. It is important to note that funds under this award will only be used for operating expense coverage, and not for loan losses. KCGF has a separate pool of funds (the KCGF capital account) dedicated to covering loan losses, which in any case are not expected to materialize until well after year-end 2018, the period covered by this award.

**13. PERSONNEL EXPENSES**

	Year ended December 31, 2017 (EUR)	Year ended December 31, 2016 (EUR)
Salaries	71,591	-
Pensional contribution	15,452	-
<b>Total personnel expenses</b>	<b>87,043</b>	<b>-</b>

**14. OPERATING EXPENSES**

	Year ended December 31, 2017 (EUR)	Year ended December 31, 2016 (EUR)
Office rent & utilities	11,267	-
Maintenance & Repair Exp.	7,380	-
Translator and other Professional services	6,090	-
Publications, Branding and Marketing	4,315	-
Phone and internet expenses	2,133	-
Training, Conferences and Seminars	1,385	-
Bank fees	807	-
Other expenses	5,382	-
<b>Total operating expenses</b>	<b>38,759</b>	<b>-</b>

**15. NET PROVISION EXPENSES**

	Year ended December 31, 2017 (EUR)	Year ended December 31, 2016 (EUR)
Provision expenses	128,223	10,219
Provision income	(49,928)	-
<b>Total net provision expenses</b>	<b>78,295</b>	<b>10,219</b>

Provisioning policy specifies the process of setting aside certain reserves for all credits that are placed under guarantees that are expected or have incurred credit loss. The provisioning policy is made in accordance with IFRS 9

**16. CONTINGENCIES AND COMMITMENTS**

	As at December 31, 2017
	Number of Guarantees
	Outstanding Guaranteed Amount (EUR)
<b>Total</b>	739
	11,657,827

Other than the ones disclosed above there are no contingencies or commitments in existence as at the balance sheet date.

**17. RELATED PARTY TRANSACTIONS**

Related parties consist of the directors of the Fund. Parties are considered related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions.

**18. EVENTS AFTER THE REPORTING DATE**

There are no significant subsequent events after the reporting date which requires adjustment or disclosure to these financial statements.