BOSNIA AND HERZEGOVINA
FEDERATION OF BOSNIA AND HERZEGOVINA
FEDERATION OF BOSNIA AND HERZEGOVINA BANKING AGENCY

I N F O R M A T I O N

ON THE BANKING SYSTEM
OF THE FEDERATION OF BOSNIA AND HERZEGOVINA
31. 12. 2013

Sarajevo, March 2014

The Banking Agency of the Federation of B&H, as a regulatory institution conducting the bank supervision function, has prepared the Information on the Banking System of the Federation of B&H (as per final unaudited data as of 31.12.13) based on financial statements and other information and data provided by banks. This also encompassed results and information obtained over the course of on-site examinations in banks and their off-site financial analysis.

I INTRODUCTION

Operations of the banking sector in 2013 were also characterised by an unfavorable environment and conditions of stagnating economic development resulting from the global financial and mortgage crisis. Modest economic growth, difficult condition of the real sector and numerous domestic problems caused by the political situation in the country coupled with limited access to stable sources of financing have all adversely reflected upon the condition and perspectives in the banking sector. Despite all these negative factors, the banking sector remained stable and adequately capitalised, with Retail savings maintaining the upward trend and with still satisfactory liquidity

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As of 31.12.13, there were 17 licensed banks in the Federation of B&H. This number went down by one bank vs. the same period in 2012. More precisely, Postbank BH dd Sarajevo had its banking license revoked. Headcount at the FB&H banking sector level stood at 7,051 as of 31.12.13, down by 79 employees or 1% vs. the YE2012.

The balance sheet total of the banking sector as of 31.12.13 amounted KM 15.4 billion, thus posting an increase by3.1% or KM 458 million compared to the last two years. Loans, being the largest assets item in banks also show a slight growth of 1.7% or KM 186 million and reached an amount of KM 10.9 billion, thus representing 70% of the balance sheet total of banks in the FB&H. As for their structure, Retail and Corporate loans hold an equivalent share of 47.9% or KM 5.2 billion.

Total non-performing loans stand at KM 1.6 billion and hold a share of 14.6% among total loans. This share has risen by 1.4% vs. YE2012 when it was at 13.2% of total loans. The share of non-performing loans of corporate customers in total corporate loans is at concerning 18.8%, up by 3.2% vs. YE2012. The share of non-performing retail loans in total retail loans is 10%, down by 0.5% vs. YE2012.

Cash funds amount to KM 4.4 billion and represent 28.6% of the balance sheet total of banks in the FB&H, thus posting an increase of 11.5% or KM 455 million vs. YE2012. This increase is chiefly attributable to deposits going up by 5.1% or KM 563 million, but can also be seen to stem from a very modest credit growth.

Within the structure of sources of financing of banks, deposits amount to KM 11.5 billion and represent 74.6% of such sources, thus still being the key financing source for banks in the FB&H. Savings deposits are the main and the largest segment of deposit and financial potential of banks. They have maintained a positive growth trend and amounted to KM 6.2 billion as of YE2013. This is 7.7% or KM 445 million more than as at YE2012. Savings deposits amounted to KM 4 billion as of YE2008 and are higher by 54% or KM 2.2 billion in the period under review.

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Loan obligations of banks as of 31.12.13 amounted to KM 1.04 billion and represented 6.7% of total sources of financing. i.e. they went down by KM 102 million or 9% vs. the YE2012. During Y2013, we also saw a trend of reduction among foreign loan obligations of banks in the FB&H, especially towards their parent groups. In the past three years, these sources dropped by app. 50%

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Total capital of banks as of 31.12.13 amounted to KM 2.3 billion, up by 4.2% or KM 93 million vs. the YE2012. The largest positive effect on the capital refers to a capital increase and a reserves payment by one bank. Regulatory capital amounted to KM 2.3 billion, 6% or KM 128 million more than at the YE2012 (coupled with slight structural changes).

Capital adequacy rate of the banking system, as one of key indicators of strength and adequacy of the banks' capital, stood at 18.0% as of 31.12.13, which is 0.7% more than at YE2012. This is still much above the legally prescribed minimum (12%) and attests to satisfactory capitalisation rate of the overall banking system and provides sound grounds for preservation of its safety and stability.

According to unaudited income statement for YE2012, banks in the Federation of B&H have posted a loss of KM 228 ths. Out of all banks, 14 have achieved positive financial result of altogether KM 140 million, as was also the amount of total loss posted by three banks.

• ***Growth and development of the banking sector and its ownership structure:*** The table below provides an overview of changes regarding number and ownership structure of banks over the past five years.

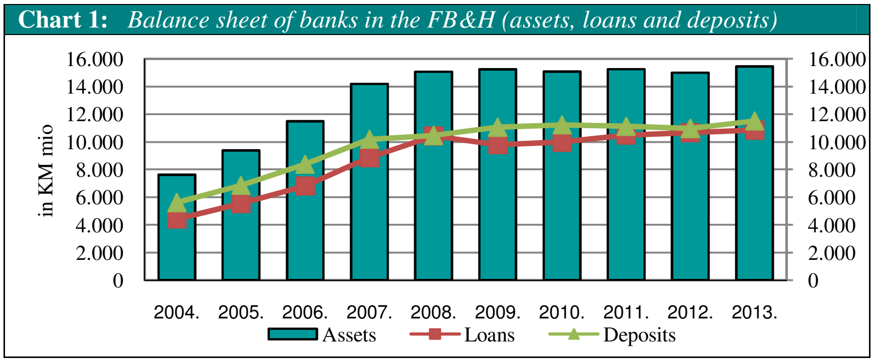
Table 1: *Overview of changes in the number and ownership structure of banks*

	State-owned banks	Private banks	TOTAL
31.12.2008	2	18	20
There were no changes in 2009			
31.12.2009.	2	18	20
Changes in 2010			
-revoked licenses	-1		-1
31.12.2010.	1	18	19
There were no changes in 2011			
31.12.2011.	1	18	19
Changes in 2012			
-revoked licenses		-1	-1
31.12.2012.	1	17	18
Changes in 2013			
-revoked licenses		-1	17
31.12.2013.	1	16	17

Balance Sheet

Over the past five years, as affected by the economic and financial crisis, the banking sector was characterised by stagnation, along with slight changed among key banking categories: balance sheet total, deposits, cash funds, loans and total capital. Still, as opposed to the last three years, the Y2013 saw some positive trends, i.e. growth of the balance sheet total as a result of a deposits increase, thus positively reflecting upon cash funds. Loans, as sources of financing, mostly refer to credit lines by foreign credit institutions and are steadily declining as a result of debt reduction, i.e. payment of liabilities due and weak inflow of new investments from abroad. The lending segment continues to display a positive trend of slight growth over the course of the past three years. Banks' assets posted a modest growth of 3.1% or KM 458 million, thus arriving to KM 15.4 billion. In the past five years, balance sheet total ranged between KM 15 billion and KM 15.4 billion, meaning it oscillated with +/- KM 460 million (the lowest level being KM 15 billion as at YE2012).

Chart 1: *Balance sheet of banks in the FB&H (assets, loans and deposits)*



The growth of the balance sheet total by 3.1% vs. the Y2012 results from the deposits increase of 5.1% or KM 563 million and the increase of total capital of 4.2% or KM 93 million. In 2013, the trend of reducing loan obligations continued, thus posting a rate of decrease of 9% or KM 102 million. As at YE2013, deposits amounted to KM 11.5 billion, total capital KM 2.3 billion and loan obligations KM 1 billion.

As for the banks' assets, a key item there refers to loans of 70.2%. Their share rose by 1.7% or KM 186 million, thus arriving to a figure of KM 10.9 billion. The most significant changes relate to two dominant sectors. Corporate loans rose by 1% or KM 61 million, thus amounting to KM 5.2 billion and representing 47.9% of total loans, while retail loans rose by 2% or KM 118 million and held the same share in total loans.

Cash funds saw a moderate growth of 11.5% or KM 455 million and amount to KM 4.4 billion, thus holding a share of 28.6% in assets
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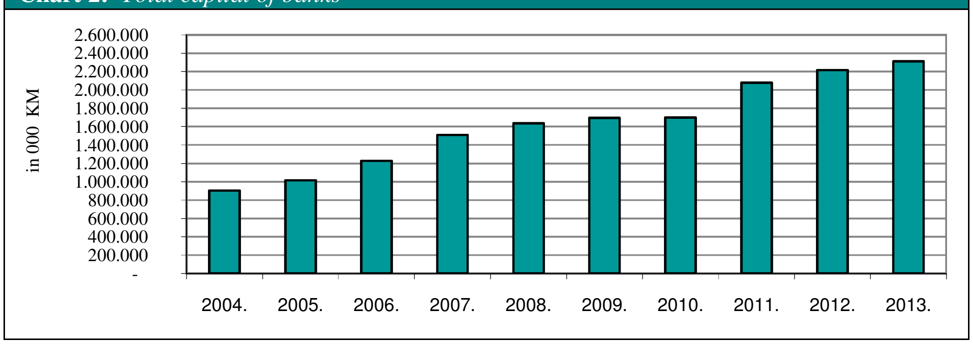
Deposits have a share of 74.6% and amount to KM 11.5 billion. Therefore, they are still the main source of financing for banks in the FB&H.

Total capital of banks equals KM 2.3 billion (shareholders capital being KM 1.2 billion), up by 4.2% or KM 93 million. The largest single positive effect on capital refers to the capital increase via new issue of shares and reserves payment of app. KM 130 million, while the negative effect was seen a profit reduction caused by a dividends disbursement (related to two banks in 2013) of KM 31 million.

Chart 2: *Total capital of banks*



Income Statement

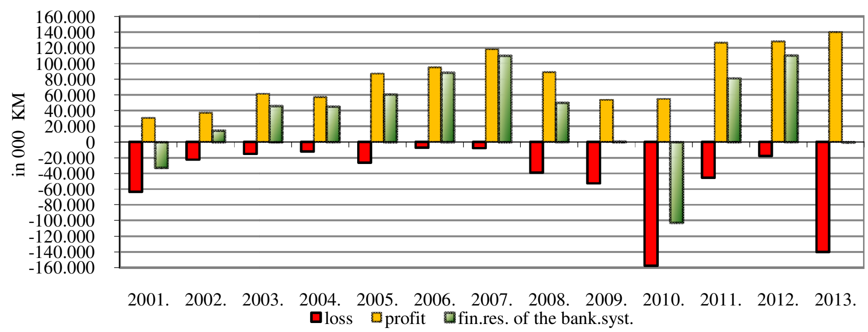
After 2001, when the banking system posted a loss figure of KM 33 million, we saw a positive trend of successful business operations. However, due to an expanding economic and financial crisis in Y2008, this trend came to a halt. Accordingly, this created major downturn in profitability of the overall banking system in the Federation of B&H. This profitability reduction was the most evident in 2010 and stemmed from the adverse crisis effect. However, in 2011 and 2012, the sector recognised some positive trends in the profitability segment, noting therein that the financial result at the banking system level in the past few years was subject to key positive influence of its two largest banks and to negative effect of one large bank.

According to the Y2013 income statement at the level of the FB&H banking sector, a loss figure was posted in an amount of KM 228 ths (as opposed to Y2012 that saw a profit of KM 110 million). –after 2001, the only case where the banking system also recognised a loss was in 2010 (KM 103 million).

Positive financial result was achieved by 14 banks of altogether KM 140 million, which is 9% or KM 12 million more than in the Y2012 (14 banks with KM 128 million), while three banks posted a loss of KM 140 million or app. eight times more or KM 123 million more than in 2012 (four banks, KM 18 million).

A reason behind the drastic fall of the financial result of the overall banking sector in 2013 rests mainly with an enormous loss by a single bank (KM 116 million), as resulting from major increase of costs of value adjustments due to extremely poor quality of its loan portfolio. Although most of banks have recognised better financial result (profit) than in the Y2012, the trend of deteriorating assets quality, albeit being slower, was still evident in 2013 among most of FB&H banks. This led to suspected underrated value adjustments and overrated financial result for some banks.

Chart 3: *Financial result of the FB&H banking sector*



Total income in 2013 amounted KM 859 million and is 1% or KM 10 million higher than in 2012, while net interest income was KM 542 million, which is nearly the same as in 2012 (with a share of 63% in total income). Operating income, as a second element of the total income, rose by 3% or KM 8 million to arrive to KM 317 million, which is almost the same as in YE2012 (37% share). On the expense side, value adjustment costs went up by significant 59% or KM 85 million vs. the Y2012 and amount to KM 230 million (representing 27% of total income), due to which total non-interest expenses went up by significant 17% or KM 120 million, i.e. they arrived to KM 841 million.

• Ownership structure*:* As at YE2013, ownership structure of banks in the Federation of B&H was as follows: one bank was mostly state-owned and 16 banks were mostly privately owned (of which 6 banks is under majority ownership of domestic legal entities and private individuals (residents), while 10 banks are under majority foreign ownership). According to the home country criteria for the owner-shareholder, i.e. criteria of direct or indirect majority ownership via group members, the largest share in 2013 refers to banking groups and banks from Austria (52.8%), followed by Italian banks (15.8%), while other countries hold respective shares below 6.3%.

In 2013, there were slight changes among shares of state-owned, foreign and private domestic (resident) capital in total shareholders capital which amounted to KM 1.2 billion as of 31.12.13. the share of state-owned capital was 2.7% and it dropped by 0.1%. Foreign capital, in nominal terms, rose by KM 14 million and arrived to KM 1 billion, thus bringing its share from 83.5% to 84.5%. private capital (of residents) declined by KM 11 million and arrived to KM 154 million, leading its share in the total shareholders capital from 13.7% to 12.8%.

• *Concentrations and competition:* As for the situation and occurrences in the FB&H banking sector, in the past few years, banks competed to achieve greater number of customers and greater market share and thus entered into mergers and acquisitions. However, over the course of last five years marked by the economic and financial crisis, banks refrained from any such mergers or acquisitions. Irrespective of the fact, three banks got their licenses revoked, thus reducing the number of banks in the banking sector. Of note, there were 17 banks in the FB&H as of YE2013. Financial experts opine that, once integration processes get finalised, there would be a total of 15 strong banks. More precisely, six to seven large banks in foreign ownership would control 90% of the market (as they already do, to some extent), while smaller banks would focus on becoming local or regional banks.
There are four banks still holding a dominant market share of 65.3% (vs. 68.1% as at YE2012) and their assets range from KM 1.2 billion to KM 3.8 billion. Most of banks (i.e. 9 of them) have assets

below KM 500 million and market share of 14, of which one bank has assets lower than KM 100 million and the market share of 0.5%. Four banks have assets ranging from KM 500 million and KM 1 billion and the market share of 20.7%.

One of indicators of concentrations at the banking system level is a market concentration ratio, i.e. a concentration rate [1] (hereinafter: the CR) indicating to a total share of five largest institutions in the system across relevant categories. CR5 as the market share indicator (assets) at the level of the FB&H banking system, stood at 71.6%, while this ratio for loans was at 71.1% and at 72.5% for deposits (2012: 74.2%, 73.5% and 74.5% respectively). However, two largest banks evidently dominate the system and hold 50% of the market in this sense.

As market players, banks use different instruments like interest rate policy, organisational improvements, HR enhancements, strong marketing approach, as well as branch network expansion, and financial support by the parent or member of the banking group.

In most of banks in the Federation of B&H, cards business represents a major business activity that is primarily of a lending character and is evident in an increasing number of credit cards and debit cards and in higher volume of non-monetary payments.

36 new ATMs were installed during 2013 and at the end of the same year their number totaled to 1,012. The number of POS terminals also rose (by 635 terminals), thus arriving to a number of 17,625 as at YE2013.

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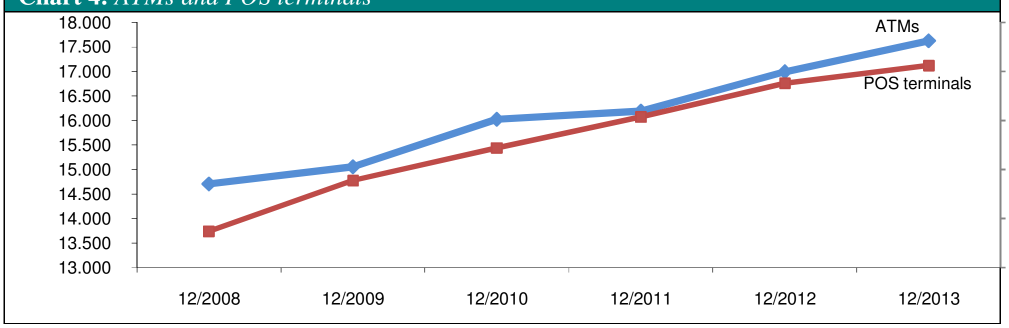
Chart 4: *ATMs and POS terminals*



[1] Concentration ratio (CR) is based on the number of institutions included in the calculation.

II BANKING SYSTEM SUPERVISION

1. BANKING AGENCY

The FB&H Banking Agency (hereinafter: the FBA) gave its fullest contribution to the banking sector reform although it frequently encountered lack of understanding for its actions. It was established in 2H of 1996 as an independent institution for bank supervision and licensing. From the very beginning, its operations were aimed towards creation of a strong and stable banking system that it market oriented and resting upon international business standards and international standards of bank supervision.

The FBA Law regulates its main duties that specifically relate to issuance of banking licenses, adoption of relevant regulations, and supervision of banks, micro credit organizations and leasing companies, as well as taking measures defined by the law (thus also including provisional administration and liquidation proceedings over banks, as well as initiation of a bankruptcy process over them).

According to local and foreign officials, over the past 17 years, FBA accomplished a high level of professionalism and formed a team with expertise and knowledge of the bank supervision area (gained through different training courses attended in the country and abroad)
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In 2013, FBA successfully invested its efforts for the banks in the Federation B&H to ensure sound risk management, especially when it comes to the credit risk. Resultantly, banks have managed to adhere to regulated minimum prudential criteria and consider therein interests of all stakeholders, as well as its financial health.

With a primarily objective of protecting interests of depositors, FBA imposed different measures over 27 banks in the period from its establishment until end of 2013 (this refers to provisional administration, liquidation and bankruptcy proceedings). One bank underwent provisional administration on basis of an order issued by the High Representative to B&H. Provisional administration was imposed over 25 banks.

Out of 27 banks being subject to these measures, the process was finalised with regards to 18 banks and there are 9 banks undergoing the process as of 31.12.13.

Out of 27 banks being subject to these measures:

- 10 banks underwent the bankruptcy proceedings before competent courts. This process was finalised with 5 banks and is still pending in 5 remaining banks.
- 10 banks underwent the liquidation process. This process was finalised in 6 banks (wherein, all liabilities to creditors and shareholders were settled in 4 banks and 2 banks were sold). The process is still pending in 4 remaining banks;
- 4 banks got merged to other banks;
- 3 banks recovered and resumed their operations. One bank underwent a capital increase and was privatised, the other also underwent the capital increase and the third one solved its status issues and nominated managing bodies, thus resuming regular course of business.

2. BANK SUPERVISION

Based on the needs for the global macroeconomic and financial stability, in 1997, the Basel Committee on Banking Supervision adopted 25 basic principles for efficient bank supervision that must be complied with in order to ensure such efficiency. These principles are in fact minimum standards for sound and prudential regulations and supervision over banks and the banking system as a whole

Since their last revision in October 2006 and taking into account major changes occurring in global financial markets and regulatory environments, as well as lessons learned from the crisis, the Basel Committee revisited these basic principles in September 2012. Resultantly, basic principles got combined with main methodology principles (assessment methodology) into a single comprehensive document. The number of basic principles went from 25 to 29 and they got reorganised into two groups: supervisory authorities, responsibilities and functions (principles 1-13) and prudential regulations and requirements (principles 14-29), all underlining importance of sound corporate governance, risk management and alignment with regulatory standards.

These principles represent minimum requirements and in many cases call for amendments in order to reflect specific conditions or regulate risks inherent with financial systems of individual countries. The principles refer to prerequisites to an efficient bank supervision, licensing, prudential regulations and requirements, supervisory approaches and methods for continuous bank supervision, information required, examiners' authorisations, cross-border banking, corporate governance, risk management processes, internal control and audit, as well as financial reporting and external audit.

FBA shows an increasing trend of comprehensive and consistent application of the generally accepted international principles, standards and practices of bank supervision. This is coupled with close attention on current and readily transferable causes of crisis situations. This was the major concern of FBA in relation to preparation and activation of available defense mechanisms and actions originating from own experience and lessons learned from much more developed and stronger banking systems suffering hard from the crisis.

FBA adopted regulations, worked on their improvement and upgrades, and enacted relevant operational decisions within its competency and taking therein all regulated steps with a primary objective for banks to ensure legality of its operations, full implementation of FBA regulations and all generally accepted principles and practices regarding their prudent and successful operations, especially under the conditions of all-present recession. In addition, all FBA efforts and persistent activities were aimed towards capital strengthening in banks, improvement of their credit policies and their consistent implementation in practice, along with the highest possible prudential approach to credit risk management still dominating our environment and liquidity risk management, plus reinforcing their capacities to handle a potential crisis situation. FBA constantly encouraged banks, especially those dominating the banking system, to strengthen their financial potentials by means of also obtaining additional special support from their parent banks abroad
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Bank supervision also included a continuous process of direct (on-site) and indirect (off-site) examinations of banks and direct communication with representatives of their managing bodies in order to synchronise and coordinate activities on stabilisation of the banking sector in the Federation of B&H. Following relevant report of examination, all examined banks were issued with orders for elimination of identified deficiencies. The examination noted that FBA orders were, in most part, properly and timely fulfilled by banks. Specific, technical and professional approach taken by an examination team strives towards further improvement of quality of banks' operations, their profitability, solvency and safety, which is also seen to be a mutual interest.

Activities related to adequate implementation of IAS/IFRS in banks were also in focus in 2013. Upon introduction and effect date of the FBA Instructions for Changed Manner of Forming, Recording and Reporting Provisions for Loan Losses (hereinafter: the Instructions) in 2012, i.e. upon the initial implementation of the IAS 39, all banks were subject to an examination of quality of methodologies applied by banks to calculate depreciation of financial assets according to IAS 39/37. The examinations revealed major weaknesses in this segment, as well as deviations in terms of quality and implementation of IAS/IFRS. Therefore, all banks were required to implement relevant corrective actions. Therefore, in 2013, FBA checked implementation status of such corrective actions and its relevant recommendations. This was done by means of targeted examinations of fulfillment of issued orders or targeted examinations of assets quality in banks.

In early 2012, FBA adopted resolutions related to information systems management and outsourcing risk in banks, while in 2013 it performed targeted examinations of the banks' process of bringing their operations in line with the said regulations.

Key changes introduced in 2013 regarding existing regulatory framework for banks' operations refer to enactment of new Decision on Temporary Measures for Dividends and Discretionary Bonus Disbursement and Repurchase of Own Shares by Banks, as well as to the corporate governance segment – decisions on the remuneration policy and practice for bank employees, suitability assessment of members of bank's bodies (fit & proper criteria) and duty of care by members of bank's bodies.

During 2013, activities continued regarding implementation of the Strategy that entailed a prudent and gradual transition to the new regulatory framework in B&H, starting from simple and going towards more complex approaches to calculating capital requirements to cover for risks inherent with bank operations. The strategy reflects a commitment to direct alignment with the regulatory framework of the EU, starting from the new global regulatory framework CRD IV/CRR, i.e. from the current reform of the entire system of financial supervision and regulations at the global level factoring therein local regulators' experience in such a process. In cooperation with the Banking Agency of the Republika Srpska (hereinafter: the ABRS) and the Association of Banks in B&H (ABB&H), as well as upon technical assistance provided by the USAID PARE, FBA has implemented a preliminary QIS encompassing a standardised approach to calculation of the credit risk capital requirement. A general conclusion after implementation of the QIS is that this would lead to an increased capital adequacy rate at the level of the FB&H banking system.

In 2013, FBA intensified its work with the International Monetary Fund, Central Bank of B&H and ABRS regarding establishment of capacities to collect and analyse a financial health indicator as one of preconditions to stronger and more efficient supervision over the entire financial system (banking sector included). Also, FBA continued with its efforts to develop a methodology for and implement relevant stress tests for the credit risk and their effect on the capital, as based on macroeconomic presumptions, as well as to inform banks of results of such stress tests. FBA also prepared a methodology to form a list of system-relevant banks in B&H.

As a part of requirements for the stand-by arrangement, FBA and IMF Mission representatives perform a regular quarterly review and analysis of effects of the global economic and mortgage crisis on the local banking and financial sector, trends in the banking sector, capitalisation rate of banks in gthe FB&H, stress test results for the banking system and for individual banks, current regulatory and banking framework, fulfillment of recommendations from previous IMF missions, as well as planned changes to the regulatory framework. Over the course of 2013, FBA also cooperated with three IMF projects of technical assistance to include: „Assistance to solving the issue of non-performing loans in the banking system and improvements to the framework for solving insolvency problems", „Contingency planning and readiness for solving unexpected crisis in the financial sector, strengthening of bank supervision function and stress testing in banks", as well as „Crisis Readiness and contingency planning".

FBA continued its cooperation with the ABRS and the B&H Deposit Insurance Agency by means of establishment of the regulatory framework, regular exchange of information and joint actions.

FBA's cooperation with the Association of Banks in B&H reflects in implementation of existing regulatory solutions and their proposed amendments, as well as in the process of enacting new regulations.

In 2013, FBA and ABRS chaired the BSCEE Group. Within these activities, FBA organised and chaired the BSCEE Group. Within these activities, FBA has organised and chaired the Annual Conference of the BSCEE Group held in mid-June 2013 in Sarajevo. The conference was attended by around 40 local and foreign participants, including representatives of 21 countries – members f the BSCEE Group, BSCEE Secretariat and international institutions (ECB, BCBS). At this two-day conference, attendees were presented with supervisory experiences regarding these issues: methods to solving non-performing loans and capital requirements within members of the BSCEE Group as opposed to Basel II, as well as latest information and regulatory news from banking systems of individual members.

In mid-November 2013, CBBH, ABRS and FBA have, with an assistance of IMF, organised the Forum on Cross-border Banking Cooperation. This high-level one-day forum gathered representatives of parent banks and their subsidiaries in B&H, banking supervision institutions of their home countries, representatives of supervisory and regulatory agencies in B&H, as well as key international financial institutions involved in the Vienna Initiative (WB, EBRD, ECB and EBA). Objectives of this forum were to promote constructive conversation on prospectives of the banking sector in B&H, challenges placed before banks (e.g. how to handle non-performing loans) and prospects of reviving the credit growth), as well as to ensure open exchange of opinions regarding challenges at the sector level and to contribute to improved cooperation between competent institutions of home countries and host countries and support by international organisations in solving these issues.

Due to the new wave of crisis in the Euro zone since end of 2011, signs of mortgage crisis and the process of debt reduction, i.e. reduction of indebtedness of banking subsidiaries towards parent banks, the so called Vienna Initiative 2.0 has been launched. An objective of the Vienna Initiative 2.0 is to manage the process of debt reduction of bank subsidiaries in a way to decrease the system risk for countries in which they operate and to establish better coordination between home countries of banking groups and their host countries in order to ensure that potential problems with cross-border financial stability are solved more quickly and to establish coordination of policies and actions, especially in relation to the supervision segment as this is in the best interest of both, home and host countries. Over the past period, activities related to fulfillment of obligations assumed by signing of this agreement were performed jointly by the FBA, ABRS and CBBH. During 2013, FBA showed its active involvement via the forum of the Vienna Initiative 2.0 and via regional meetings.

In line with requirements laid down in the Principle 3 (formerly Principle 25) of Key Principles for Efficient Bank Supervision issued by the Basel Committee, as at YE2013, FBA, CBBH and ABRS have signed a multilateral agreement with supervisory authorities of countries of Southeast Europe to include: Albania, Greece, Macedonia, Romania, Bulgaria, Serbia, Montenegro and Cyprus, as well as agreements on mutual cooperation with competent supervisory bodies of Slovenia, Croatia, Serbia, Montenegro and Turkey. The MoU closer defined the following: exchange of information, on-site examinations, information and examination requests, data protection, continued cooperation and other provisions.

In 2012, in cooperation with the ABRS and with technical assistance of USAD, FBA has conducted an analysis of the FB&H regulatory framework and its compliance with the EU directives regarding exchange of information and protection of data secrecy. In that sense, it launched an initiative to amend the Law on the FB&H Banking Agency. The amendments were approved by the FB&H Parliament in September 2012. These amendments laid foundations for signing multilateral agreements with supervisors of EU-member countries, especially Italy and Austria. Early in 2014, ECB provided their comments on amendments to the legal framework of entity-level banking agencies regarding the segment of exchange and confidentiality of information where it found that FB&H's framework is consistent with the relevant EU regulation regarding data confidentiality. As a West Balkan country, B&H will be kept appraised of forms of cooperation within the unified EU Supervisory Mechanism to be considered during 2014.

In 2013, FBA cooperated with regulatory institutions of countries where it already signed MoUs and also with other supervisory institutions of countries in local and wider region. Special forms of cooperation have been established with supervisory institutions through regional and bilateral meetings and regular exchange of information on issues concerning operations and condition of parent banks and their daughter banks, i.e. their subsidiaries.
In line with the FB&H Parliament's decision from 2006 and, later on, in line with the CARDS Program prepared by experts of the ECB and the group of central banks in Europe, FBA's activities in 2013 included support to the idea of consolidating the bank supervision function on the B&H state level since it realised that, along with many other pragmatic reasons, our country's accession to the European Union is not possible without this form of supervision over the main segment of the financial system. European experts have also confirmed that «the bank supervision function is in fact organised on a state level in EU countries, whether under the umbrella of the central bank or without it» and that «...EU membership entails establishment f a single banking marketplace leading towars a unified bank supervision».

An increasingly aggressive globalisation and development of the banking industry, as well as development and evolution of supervisory principles, rules and standards, as well as current painful lessons learned from the global financial and economic crisis by all affected parties, have shown that bank supervisory authorities must be constantly kept appraised of and develop their knowledge, skills and instruments to ensure their efficient actions towards achieving their mission. It is for these reasons, as well as for reasons of recruiting new, young staff, that the FBA took in to account these needs in 2013 and, independently and with the help of different international, highly qualified and specialised institutions, organised relevant local and international training of its employees. Also, FBA provided assistance in specialised training of other supervisory bodies and institutions in the FB&H.

3. ANTI-MONEY LAUNDERING AND COMBATING OF TERRORISM FINANCING

Based on bank situation over the past period, performed compliance examinations and reports banks deliver to the FBA, we find that the quality of risk management is still satisfactory and that there are no reasons for supervisory concern regarding managing the risk of money laundering and terrorism financing. The risk quantity is within the acceptable grids. The quality of risk management inherent with bank operations as a result of money laundering and terrorism financing (reputation risk, operational risk, legal risk, concentrations risk regarding assets and deposits) in the FB&H banking sector is satisfactory and at the sale level as in the previous period.

Customer Acceptance

Banks have adopted customer acceptance policies and defined which customers are acceptable for establishment of a business relationship. Based on this policy, banks have organised special customer profile registries. However, they encountered a difficulty with ensuring information updates for customers classified within the most risky groups. On the other hand, it is very important that banks have adopted and apply a kind of customer approach that rests on an analysis of risks that a particular customer brings to the bank, i.e. banks have precisely defined acceptable customers.

Customer Identification

Banks have adopted customer identification as a key element to the «know your customer» standard. The customer identification policy is being applied by banks upon establishment of a business relationship with a customer. However, the still-present problem is with ensuring updates to documentation used in the identification/verification regarding already established business relationships. In addition to difficulties with documentation updates, another problem concerns identification and verification of sources of funds used by customers to effect transactions related to payment of loan annuities.

Continuous Monitoring of Accounts and Transactions

This policy has been adhered to, thus further reducing the old practice of formal account and transaction monitoring of customers. In order to get to the essence of account and transactions monitoring, banks have applied the «know your customer» principle and defined transaction limits by account and transaction types and have built an information system enabling application of established limits for account and transactions monitoring. The defined limits have an increasing use in preventive account and transactions monitoring. However, certain problems appeared related to monitoring of transactions used for payment of loan installments and are directly caused by non-identification of sources of funds used for such payments.

Managing the Risk of Money Laundering and Terrorism Financing

Elements of the said policy are outlined in the banks' programs. They have defined reporting lines – internal and external alike.

Reporting: In 2013, banks have reported 243,721 transactions representing 0.3% of total transactions effected in the banking system of the Federation of B&H (71,435,220 of effected transactions, according to bank data) worth KM 12.2 billion, thus constituting 10.6% of total value of effected transactions in the FB&H banking system (KM 114.8 billion according to bank data). The number of transfers reported in 2013 is 1.3% higher than in the year before and their value is 2.4% higher.

The table below provides a comparative overview of the number and the value of reported transfers sorted by the reporting methods used (before transfer execution, within the defined deadline and upon expiry of this deadline):

Transfer value in 000 KM

Table 2: Comparative overview of number and value of reported transfers

No.	Description (transfer name)	Transfers in 2012		Transfers in 2013		%	
		Number	Value	Number	Value	Number	Value
1	2	3	4	5	6	7 (5/3)	8 (6/4)
1.	**Total reported transfers (2+3+4)**	**240.477**	**11.896.546**	**243.741**	**12.182.777**	**101,3**	**102,4**
2.	Transfers reported before their execution	7	3.993	13	5.380	185,7	134,7
3.	Transfers reported within 3 days	240.389	11.888.089	243.605	12.151.455	101,3	102,2
4.	Transfers reported after 3 days	81	4.464	123	25.942	151,8	581,1

The structure of reported transactions shows a major increase in number (by 85.7%) and value (by 34.7%) of transfers reported before their execution vs. the same transfers in 2012. This leads to a conclusion that banks act preventively regarding anti-money laundering and combating of terrorism financing. However, since the number and value of transfers reported after the deadline expiry have risen (by 50.8% and by 5.8x respectively), in 2014, banks would need to invest additional efforts to develop policies and procedures of preventive actions in order to maintain the achieved level of quality in managing the risk of money laundering and terrorism financing., i.e. to in order to eliminate risks of money laundering and terrorism financing in their operations. The number of transfers reported within the defined deadline followed the increase in number of total reported transfers (up by 1.3%), as is the case with their value (up by 2.2%).

Suspicious transactions: In their reports, banks have tagged 67 transfers as suspicious and they all relate to potential money laundering. There were no reported transfers suspected of terrorism financing. The number of reported suspicious transactions went up by 59.5% vs. the year before. The value of such transfers was KM 44 million, which is 5 times more than in 2012.

The table below provides a comparative overview of the number and the value of reported suspicious transfers sorted by the reporting methods used ((before transfer execution, within the defined deadline and upon expiry of this deadline).

Transfer value in 000 KM

Table 3: Comparative overview of number and value of reported suspicious transfers

No.	Suspicious transfers	Transfers in 2012		Transfers in 2013		%	
		Number	Value	Number	Number	Value	Number
1	2	3	4	5	6	7 (5/3)	8(6/4)
1.	**Total reported transfers**	**42**	**8.802**	**67**	**43.828**	**159,5**	**497,9**
2.	Transfers reported before their execution	6	3.876	13	5.380	216,7	138,8
3.	Transfers reported within 3 days	21	3.035	30	16.469	142,8	542,6
4.	Transfers reported after 3 days	15	1.891	24	21.979	160,0	1.162,3

The structure of reported suspicious transfers, as well as the structure of total reported transfers, confirms earlier conclusions regarding the quality of risk management of money laundering and terrorism financing and absence of reasons for a supervisory concern. There are 13 cases of preventive actions by banks, where they delivered their suspicious transfer reports to the Financial Intelligence Unit prior to actual execution of such transfers. There are 30 cases of quality monitoring, where banks have detected suspicious transfers and reported of them within 3 days, while remaining 24 cases refer to corrective actions in line with FBA orders.

III OPERATIONS OF BANKS IN THE FEDERATION OF B&H

1. BANKING SECTOR STRUCTURE

1.1. Status, Number and Network of Branches

As of 31.12.13, there were 17 banks holding the banking license in the Federation of B&H. This number is lower than as at 31.12.12 considering a revocation of the banking license and initiation of liquidation proceedings over Postbank BH dd Sarajevo on 20.06.13. A special law was enacted on 01.07.08 to regulate operations of the Development Bank of the FB&H, a legal successor f the Investment Bank of the FB&H dd Sarajevo.

In 2013, there was no major expansion of the banks' branch network. This is to say that the expansion trend continued, but in lesser extent than before, as chiefly attributable to the financial crisis. Banks have re-organised their branch networks in a way to have changed organisational form, membership or address of their organisational parts. This also entailed mergers and closures of some organisational parts, all for purpose of business rationalisation and operating cost reduction. There were a total of 111 such changes among banks in the FB&H (107 changes within the FB&H territory and 4 changes within the RS territory): 13 new organisational units were established, 22 were closed and 76 changed their form.

Subsequent to such changes, banks in the FB&H had a total of 580 organisational parts as of 31.12.13, down by 0.8% vs. 31.12.12.

There were 5 banks from the Republika Srpska with 27 organisational parts in the Federation of B&H, which is an increase compared to 31.12.12 (25).

As of 31.12.13, 9 banks from the Federation of B&H had 51 organisational parts in the Republika Srpska and 8 banks had 11 organisational parts in the Brcko District.

As of 31.12.13, all banks had licenses to effect inter-bank transactions within the domestic payment system and 16 banks were covered by deposit insurance.

1.2. Ownership Structure

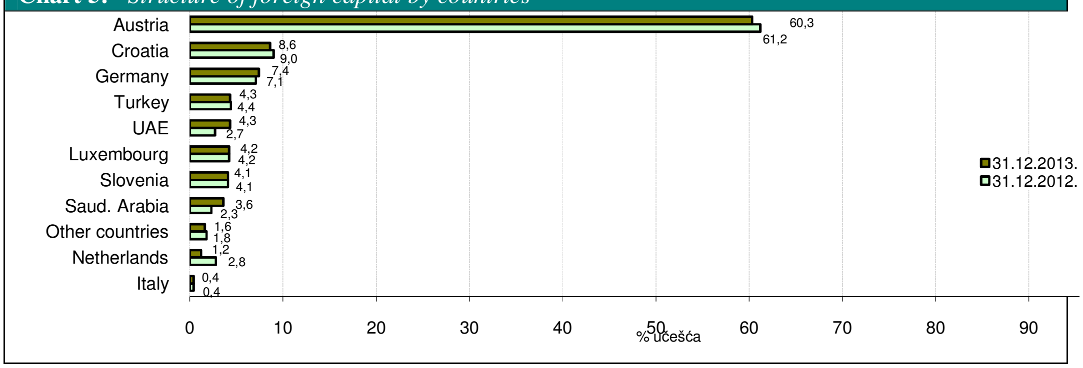
Find below is the ownership structure of banks[2] as of 31.12.13 that was analysed on basis of available information and reviews conducted in banks:

- In private or mostly private ownership: 16 banks (94.1%)
- In state or mostly state ownership[3]: 1 bank (5.9%)

Out of 16 banks in mostly private ownership, 6 are under majority ownership of local legal entities and private individuals (residents) and 10 are under majority foreign ownership.

If observed solely from the perspective of capital, using the criteria of home country of shareholders, the conditions as of 31.12.13 changed only slightly compared to the one as of 31.12.12: the largest share of foreign capital of 60.3% refers to shareholders from Austria, followed by shareholders from Croatia with 8.6% and Germany 7.4%. Other countries hold individual share below 5%.

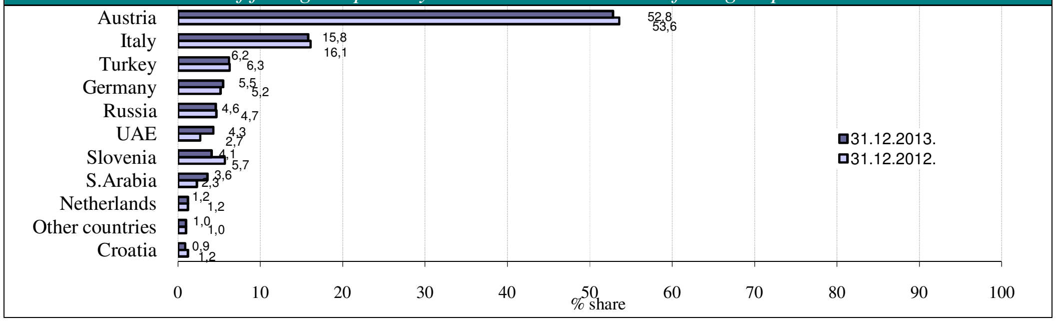
Chart 5: *Structure of foreign capital by countries*



However, if we account for capital relations, the structure of foreign capital may also be observed using the criteria of the home country of the parent bank or parent group holding ownership (direct or indirect) in banks in the Federation of B&H. According to this criteria, the condition has also changed only slightly vs. the one in late 2012: share of banking groups and banks from Austria was 52.8%, followed by Italian banks with the share of 15.8% and other countries with individual shares below 7%, plus the share of Russian[4] banks of 4.6% (appearing in the marketplace in 2012 for the first time.

[2] Criteria for this particular bank classification is ownership over shareholders capital in banks.
[3] State ownership refers to local state capital of B&H.
[4] In 2012, Sberbank from Russia purchased Volksbank International from Austria (under which ownership was also Volksbank BH d.d. Sarajevo).

Chart 6: *Structure of foreign capital by home countries – seat of the group*[5]



The ownership structure may also be observed from the aspect of financial ratios, i.e. according to the total capital value[6].

-in 000 KM-

Table 4: *Ownership structure according to total capital*

BANKS	31.12.2011		31.12.2012		31.12.2013		INDEX	
1	2		3		4		5 (3/2)	6 (4/3)
State-owned banks	50.499	2%	51.114	2%	51.668	2%	101	101
Private banks	2.029.566	98%	2.166.261	98%	2.269.387	98%	107	105
TOTAL	2.080.065	100%	2.217.375	100%	2.321.056	100%	107	105

In 2013, total capital rose by 5% or KM 104 million. The largest positive effect on capital refers to capital increase through a new issue of hares and reserves payment of app. KM 130 million and the negative effect refers to a reduction based on a transfer to liabilities for dividends (from Y2012 profit, with regards to 2 banks) of KM 31 million.

If observed from the perspective of the share of state-owned, private and foreign capital in shareholders capital of banks, the resulting picture of the capital ownership structure in FB&H banks is as follows.

- in 000 KM-

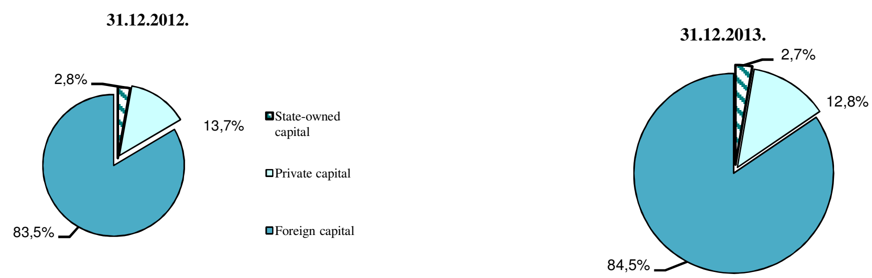
Table 5: *Ownership structure according to the share of state-owned, private and foreign capital*

Shareholders capital	31.12.2011		31.12.2012		31.12.2013		INDEX	
	Amount	% share	Amount	% share	Amount	% share	4/2	6/4
1	2	3	4	5	6	7	8	9
State-owned capital	38.072	3,2	33.096	2,8	32.364	2,7	87	98
Private capital (residents)	174.088	14,6	164.603	13,7	153.549	12,8	95	93
Foreign capital (non-residents)	981.412	82,2	1.003.907	83,5	1.017.822	84,5	102	101
TOTAL	1.193.572	100,0	1.201.606	100,0	1.203.735	100,0	101	100

[5] In addition to home countries of parent groups whose members are banks from the FB&H, the chart also outlines countries of all other shareholders of banks in the FB&H.

[6] According to the balance sheet prepared on basis of the FBA model: starting from 31.12.11, loan loss provisions formed against profit became a part of the equity structure (in addition to shareholders capital, issue premiums, retained profit and reserves and other capital (financial resut of the current period)).

Chart 7: *Ownership structure (by equity)*



In 2013, shareholders capital of banks in the Federation of B&H went up by KM 2.1 million or 0.2% vs. 31.12.12. Shareholders capital rose by KM 34 million related to the capital increase-issue of shares in two banks. Also, the capital increase against profit in one bank was KM1.4 million, while in the other the capital figure went down by KM 4.9 million following the FBA order for exclusion of this amount from the capital. Postbank BH had its capital reduced by 28.4 million and resultantly had its banking license revoked, thus being subject to a liquidation process.

Equity-based analysis of the banks' shareholders capital shows more details of changes and trends in the FB&H banking system, i.e. changes to its structure.

The share of state-owned capital in total shareholders capital as of 31.12.13 is 2.7%, down by 0.1% vs. 31.12.12 (as based on relative indicators). In absolute terms, the share of state-owned capital went down by KM 0.7 million, which was actually the amount of state-owned capital in Postbank BH following revocation of the banking license and initiation of the liquidation process.

The share of private capital (of residents) in total shareholders capital is 12.8%, down by 0.95 vs. 31.12.12, i.e. it amounts to KM 11.1 million net. The share of private capital (residents) dropped by KM 4.9 million following the FBA order to one bank for exclusion of the said amount from its capital. Also, it dropped by additional KM 11.4 million of private capital (residents) of Postbank subsequent to revocation of its banking license and opening of the liquidation process. This capital's figure went up based on the capital increase against profit in one bank by KM 1.4 million and by KM 3.8 million based on share issue in another bank.

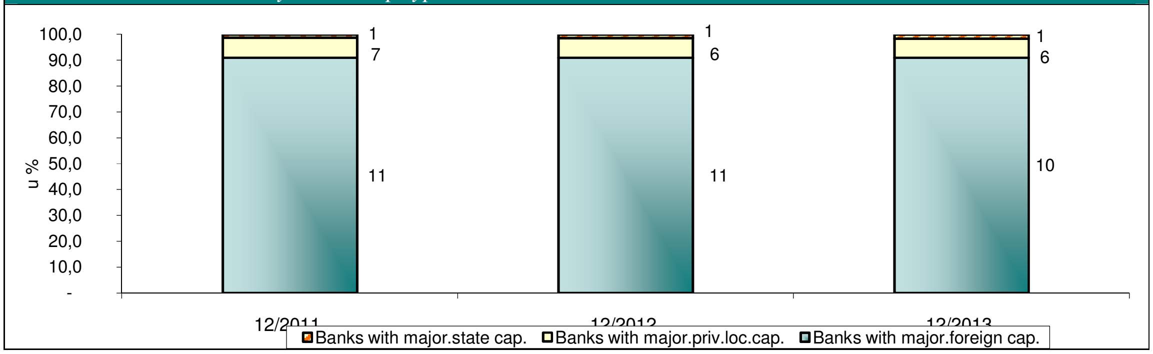
The share of private capital (non-residents) in total shareholders capital rose by 1.0% (i.e. from 83.5% to 84.5%). In absolute terms, the share of private capital (non-residents) climbed by KM 13.9 million net. We have also considered herein a reduction by KM 16.3 million of foreign capital in Postbank BH (after revocation of its banking license and initiation of the liquidation process), an increase of KM 34 million related to capital increases in two banks and a reduction by KM 3.8 million based on sale of shares.

The market share of banks with majority foreign ownership as of 31.12.13 stood at high 91.0%, while banks with majority domestic private capital had the share of 7.4% and banks with majority state-owned capital 1.6% share.

- in % -

Table 6: *Market shares of banks according to ownership type (majority capital)*									
BANKS	31.12.2011			31.12.2012			31.12.2013		
	Number of banks	Share in equity	Share in total assets	Number of banks	Share in equity	Share in total assets	Number of banks	Share in equity	Share in total assets
1	2	3	4	5	6	7	8	9	10
Bank with majority state-owned capital	1	2,4	1,3	1	2,3	1,4	1	2,2	1,6
Banks with majority private domestic capital	7	10,3	7,7	6	10,5	7,6	6	9,2	7,4
Banks with majority private foreign capital	11	87,3	91,0	11	87,2	91,0	10	88,6	91,0
TOTAL	19	100,0	100,0	18	100,0	100,0	17	100,0	100,0

Chart 8: *Market shares by ownership type*



1.3. Human Resources

As of 31.12.13, banks in the FB&H had a headcount of 7,051 employees, of which 3% are employed with state-owned banks and 97% in private banks.

Table 7: *Employees of FB&H banks*								
B A N K S	HEADCOUNT						INDEX	
	31.12.2011		31.12.2012		31.12.2013		3/2	4/3
1	2		3		4		5	6
State-owned banks	177	2%	183	3%	200	3%	103	109
Private banks	7.192	98%	6.947	97%	6.851	97%	97	99
TOTAL	7.369	100%	7.130	100%	7.051	100%	97	99
Number of banks	19		18		17		95	94

Table 8: *Qualification structure of employees*								
QUALIFICATIONS	HEADCOUNT						INDEX	
	31.12.2011		31.12.2012		31.12.2013		4/2	6/4
1	2	3	4	5	6	7	8	9
University qualifications	3.401	46,1%	3.479	48,8%	3.673	52,1%	102	106
Two-year post secondary school qualifications	706	9,6%	667	9,3%	601	8,5%	94	90
Secondary school qualifications	3.218	43,7%	2.949	41,4%	2.750	39,0%	92	93
Others	44	0,6%	35	0,5%	27	0,4%	80	77
TOTAL	7.369	100,0%	7.130	100,0%	7.051	100,0%	97	99

In 2013, banks' headcount dropped by 79 or 1%, as largely attributable to a banking license being revoked from one bank.

A trend of improved qualification structure by means of larger share of employees with university qualifications has continued in 2013 as well. On one hand, this is a result of an increase in number of this group of employees by 194 or 6% and, on the other hand, this is a result of a reduction in number of employees with secondary school qualifications by 199 or 7%.

One of indicators affecting the performance evaluation of individual bank and banking system as a whole is staff efficiency expressed as a ratio between assets and headcount, i.e. assets per employee. Higher ratio means better efficiency of operations of banks and of the entire banking system.

Table 9: *Assets per employee*

BANKS	31.12.2011			31.12.2012			31.12.2013		
	Headcount	Assets (000 KM)	Assets per employee	Headcount	Assets (000 KM)	Assets per employee	Headcount	Assets (000 KM)	Assets per employee
State-owned	177	191.881	1.084	183	209.971	1.147	200	241.605	1.208
Private	7.192	15.071.438	2.096	6.947	14.780.795	2.128	6.851	15.207.099	2.220
TOTAL	7.369	15.263.319	2.071	7.130	14.990.766	2.102	7.051	15.448.704	2.191

As at YE2013, there was KM 2.2 million of assets per employee at the banking system level and this is much better than at the end of 2012.

Table 10: *Assets per employee – by groups*

Assets (000 KM)	31.12.2011	31.12.2012	31.12.2013
	Number of banks	Number of banks	Number of banks
Up to 1.000	4	3	1
1.000 to 2.000	9	10	8
2.000 to 3.000	5	4	7
Over 3.000	1	1	1
TOTAL	19	18	17

Analytical indicators for individual banks range from KM 910 ths to KM 3.9 million of assets per employee. There are 5 banks where this ratio is better than the one at the banking sector level, while 3 largest banks in the system have this ratio surpassing the figure of KM 2.4 million.

2. FINANCIAL RATIOS OF BANKS' OPERATIONS

Off-site bank examinations are performed by means of reports defined by the FBA and reports of other institutions, thus constituting a database resting on three sources of information:

1) Balance sheet information for all banks provided on a monthly basis and together with additional attachments on a quarterly basis. This information contains details of cash funds, loans, deposits and off-balance sheet items, as well as basic statistical data;
2) Information of solvency of banks, information on capital and capital adequacy, assets classification, concentrations of certain risk types, liquidity position, FX risk exposure, interest rates on loans and deposits, all based on reports prescribed by the FBA;
3) Information on business results of banks (income statement according to the FBA model) and statement of cash flows, all delivered to the FBA on a quarterly basis.

In addition to these standardised reports, the reporting database also consists of information obtained on basis of additional reporting requests by the FBA for purpose of ensuring quality monitoring and analysis of banks' operations, as well as reports on audit of financial statements of banks prepared by external audit firms and any other information of relevance for performance evaluation of individual bank and the banking system as a whole.

In line with provisions of the Law on Opening Balance Sheet of Banks, a bank under majority state ownership is required to report to the FBA on basis of the «full» balance sheet divided into: liabilities, neutral items and assets. In order to obtain more realistic indicators of banks' operations in the Federation of B&H, indicators from the assets side of the balance sheet of banks with majority state ownership[7].

2.1. Balance Sheet

The balance sheet total of the banking sector as at YE2013 stood at KM 15.4 billion, up by 3.1% or KM 458 million vs. YE2012. Negative trends from the 1H 2013 (assets drop by 0.8%, drop f deposits by 0.9%, loans by 9.7% and cash funds by 3.7%) have stopped in the third and fourth quarter of the year, mainly due to growth of deposits by 6% or KM 661 million, which in turn positively reflected upon other mentioned segments. On the other hand, due to effects of the financial and economic crisis, the loan quality worsened, uncollectible receivables have risen and actual loan growth remained at the same rate as in the year before (2%). Still, we find that negative trends from the previous and this year have slowed down, so changes have been moderate and key business indicators of the banking system have mostly stagnated and, with minor oscillations, have maintained almost the same level as in the past two years.

- 000 KM-

Table 11: *Balance sheet*

DESCRIPTION	31.12.2011		31.12.2012		31.12.2013		INDEX	
	AMOUNT	% share	AMOUNT	% share	AMOUNT	% share		
1	2	3	4	5	6	7	8 (4/2)	9 (6/4)
ASSETS:								
Cash funds	4.378.076	28,8	3.962.581	26,4	4.417.898	28,6	91	111
Securities[8]	458.465	3,0	548.467	3,7	562.513	3,6	120	103
Loans to other banks	79.940	0,5	78.522	0,5	51.960	0,3	98	66
Loans	10.487.671	68,7	10.666.124	71,1	10.852.400	70,2	102	102
Value adjustment	931.946	6,1	1.007.459	6,7	1.163.530	7,5	108	115
Loans- net (loans minus value adjust.)	9.555.725	62,6	9.658.665	64,4	9.688.870	62,7	101	100
Business premises and other fixed assets	540.749	3,5	521.493	3,5	512.985	3,4	96	98
Other assets	250.364	1,6	221.038	1,5	214.478	1,4	88	97
TOTAL ASSETS	**15.263.319**	**100,0**	**14.990.766**	**100,0**	**15.448.704**	**100,0**	**98**	**103**
LIABILITIES:								
LIABILITIES								
Deposits	11.124.675	72,9	10.961.001	73,1	11.523.849	74,6	99	105
Borrowings from their banks	2.000	0,0	2.000	0,0	0	0,0	100	n/a
Liabilities under loans taken	1.319.299	8,6	1.141.561	7,6	1.039.381	6,7	87	91
Other liabilities	737.280	4,9	668.829	4,5	575.087	3,7	91	86
EQUITY								
Equity	2.080.065	13,6	2.217.375	14,8	2.310.387	15,0	107	104
TOTAL LIABILITIES (LIABILITIES AND EQUITY)	**15.263.319**	**100,0**	**14.990.766**	**100,0**	**15.448.704**	**100,0**	**98**	**103**

[7] State-owned banks post the «full balance sheet», meaning liabilities and neutral items that are to be taken over by the state once their privatisation proces gets finalised. As of 31.12.13,unted to KM 639 million with regards to one bank.

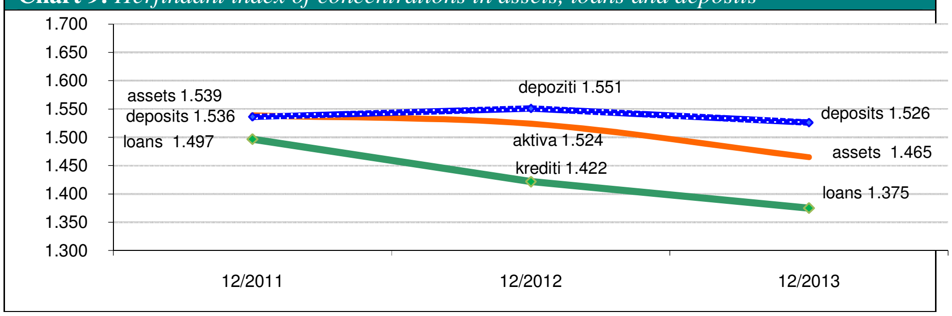
[8] Trading securities, securities available for sale and held to maturity securities.

Table 12: *Banks' assets according to ownership structure*											
BANKS	**31.12.2011**			**31.12.2012**			**31.12.2013**			**INDEX**	
	Number of banks	**Assets (000 KM)**		**Number of banks**	**Assets (000 KM)**		**Number of banks**	**Assets (000 KM)**			
1	2	3		4	5		6	7		8 (5/3)	9(7/5)
State-owned	1	191.881	1%	1	209.971	1%	1	241.605	2%	109	115
Private	18	15.071.438	99%	17	14.780.795	99%	16	15.207.099	98%	98	103
TOTAL	19	15.263.319	100%	18	14.990.766	100%	17	15.448.704	100%	98	103

There are 12 banks with assets exceeding the level from YE2012, while remaining 5 had their assets reduced and the rate of decrease ranged from 1% to 23%. The negative effect to the balance sheet total of banks is attributable to a drop by KM 50 million related to the banking license revocation from one bank in June 2013.

Concentrations indicator we used for the three key segments of the banking operations (assets, loans and deposits) is the Herfindahl index[9].

Chart 9: *Herfindahl index of concentrations in assets, loans and deposits*



In 2013, the Herfindahl index of concentrations in all three relevant categories (assets, loans and deposits) was reduced: for assets to 59, loans to 47 and deposits to 25 units, so its level in 2013 for assets stood at 1,465, for loans at 1,375 and for deposits at 1,526 units, which is indicative to a moderate concentration[10].

The second concentrations indicator for the banking system is a ratio of market concentrations, i.e. concentration rate[11] (hereinafter: the CR) showing a total share of largest institutions in the system and selected relevant categories: assets, loans and deposits. CR5 dropped in relation to the market share from 74.2% to 71.6%, it dropped for loans from 73.5% to 71.1% and for deposits it went from 74.5% to 72.5%. Over the past two years, the value of CR5 wend down slightly across all three

[9] This index is also called Hirschmann-Herfindahl index or HHI and is calculated according to this formula:

$$HI = \sum_{j=1}^{n} (S)_j^2 ,$$

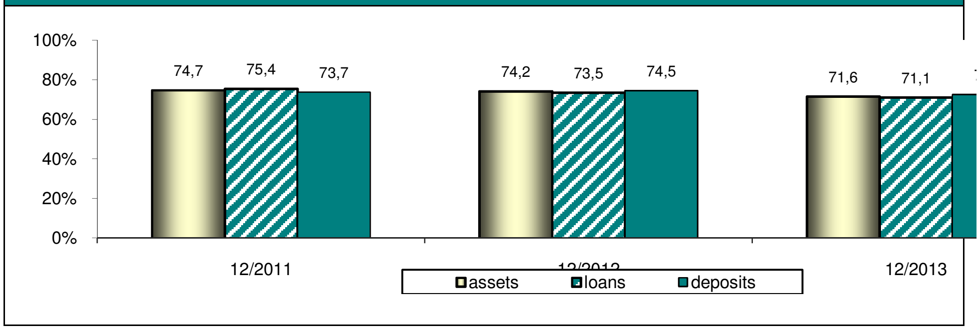
It represents a sum of squares of percentage share of specific element (e.g. assets, deposits, loans) of all market participants in the system. Of note, this index does not grow linearly and the value of e.g. 3,000 does not mean that the concentration within the system is 30%. Hypothetically, if there would be just one bank in the entire system HHI would be at maximum 10,000.

[10] If the value of HHI is below 1,000, this shows no presence of the concentration in the marketplace, while the index value between 1,000 and 1,800 shows moderate concentration and HHI value above 1,800 means high concentration in the market.

[11] Concentration ratio (CR) rests on the number of institutions included in the calculation.

categories, but there is still evident domination of five largest banks in the system holding app. 74% of the market, loans and deposits.

Chart 10: *Concentration rates for 5 largest banks-CR5: assets, loans and deposits*



The banking sector may also be analysed from the aspect of several groups formed according to the assets size[12]. Changes in the percentage share vs. the Y2012 were evident in relation to all groups, as a result of changeable assets with most of banks and revocation of the banking license from one bank (from the group of small banks, i.e. Group V).

The share of four largest banks has dropped: I group (two largest banks in the system with assets over KM 3 billion) from 49.8% to 48.8% and II group (two banks with assets amounting between KM 1 billion and KM 2 billion) from 18.3% to 16.5%. The share of the III group (four banks with assets between KM 500 million and KM 1 billion), after transfer of one bank to the IV group, rose by 4.8 percentage points, i.e. by 20.7%, thus affecting the reduction of share in the IV group of eight banks (with assets ranging from KM 100 million and KM 500 million) by 1.7 percentage points, i.e. 13.5%. Share of the last V group (assets below KM 100 million), after reduction from two to one bank (due to banking license revocation), dropped to 0.5%

Despite minor changes in shares of individual groups, evidently four largest banks still hold high market share of 65%.

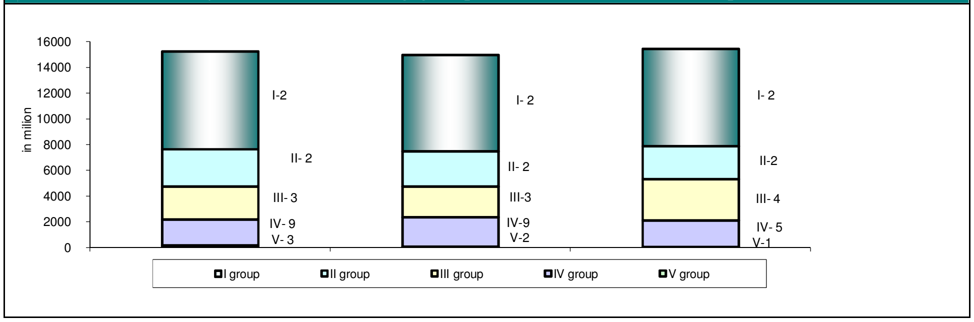
The table below provides an overview of amounts and shares of individual groups of banks in total assets – across periods (in KM million).

Table 13: *Share of individual banking groups in total assets – across periods*

ASSETS	31.12.2011			31.12.2012			31.12.2013		
	Amount	**% share**	**Number of banks**	**Amount**	**% share**	**Number of banks**	**Amount**	**% share**	**Number of banks**
I- Over 2.000	7.596	49,7	2	7.476	49,8	2	7.545	48,8	2
II- 1000 to 2000	2.894	19,0	2	2.741	18,3	2	2.556	16,5	2
III- 500 to 1000	2.545	16,7	3	2.379	15,9	3	3.195	20,7	4
IV- 100 to 500	2.030	13,3	9	2.280	15,2	9	2.080	13,5	8
V- Below 100	198	1,3	3	115	0,8	2	73	0,5	1
TOTAL	15.263	100,0	19	14.991	100,0	18	15.449	100,0	17

[12] Banks are divided into 5 groups depending on the assets size.

Chart 11: *Share of individual banking groups in total assets – across periods*



The balance sheet total growth by 3.1% or KM 458 million, i.e. to the level of KM 15.4 billion as at YE2013 is mostly a result of the deposit growth by 5.1% or KM 563 million, coupled with a reduction of loans by 9% or KM 102 million. Equity also rose by 4.2% or KM 93 million, as originating mostly from a capital increase via new issue of shares and reserve payment related to three banks of app. KM 130 million, as well as from a reduction based on transfer to liabilities for dividends (from Y2012 profit with regards to two banks) of KM 31 million. At the end of 2013, equity amounted to KM 2.3 billion.

After their decrease of 3.7% in the first two quarters of 2013, cash funds rose by 16% in the 2H 2013, thus resulting in a growth rate of 11.55 or KM 455 million on an annual level. As of 31.12.13, this amount stood at KM 4.4 billion. This growth results from the said increase of deposits, as well as from a very modest loan growth.

This is to say that growth rate of loans in 2013 and 2012 was the same 1-7% or KM 186 million. As of 31.12.13, loan portfolio stood at KM 10.9 billion.

Unlike the growth of app. 20% achieved in the previous two years, investments in securities in 2013 posted a modest increase of 2.6% or KM 14 million, while their figure as at YE2013 was KM 563 million, thus having a share in assets of mere 3.6%.

Portfolio of securities available for sale (where small part thereof refers to trading portfolio) rose slightly by KM 7 million and arrived to KM 382 million and value of securities held to maturity rose from KM173 million to KM 181 million. Both portfolios include securities issued by the FB&H Government[13] of altogether KM 217 million as of 31.12.13. Also, trading portfolio includes shares issued by local companies totaling to KM 3 million. The remaining portion of the securities portfolio amounts to app. KM 302 million and refers mostly to bonds of EU countries.

In 2013, the FB&H Government issued three trenches of treasury bills: one in March 2013 of nominal value of KM 30 million maturing in September 2013 and the other two in September 2013 in respective amounts of KM 30 million (maturing in March 2014) and KM 20 million (maturing in June 2014). As of 31.12.13, treasury bills amounted to KM 50 million, i.e. their book value was KM 49.7 million. Also, securities portfolios of banks also include bonds issued by the FB&H Government (issued in 2012: first issue in May 2012 of KM 80 million maturing within 3 years, the second one in June and August of KM 30 million in total that mature within 5 years and the third issue in September of KM 20 million maturing within 2 years, as well as fourth issue from December 2013 of KM 40 million maturing within 3 years-where the total value of bonds purchased by banks was KM 17.5 million) of total nominal value of KM 140 million. Most of treasury bills and bonds with book value

[13] All types of securities of the FB&H Government as the issuer.

of KM 157 million were classified into the portfolio of securities available for sale, while the rest of KM 33 million is classified within the portfolio of securities held to maturity.

If we look at the overall securities portfolio (KM 563 million) from a perspective of exposures by countries, the largest share is with B&H (46.4%), followed by Romania (15.3%), Austria (8.5%), France (7.9%), etc.

The charts below show the structure of key items of the banks' balance sheet.

Chart 12: *Structure of assets within the balance sheet of banks*

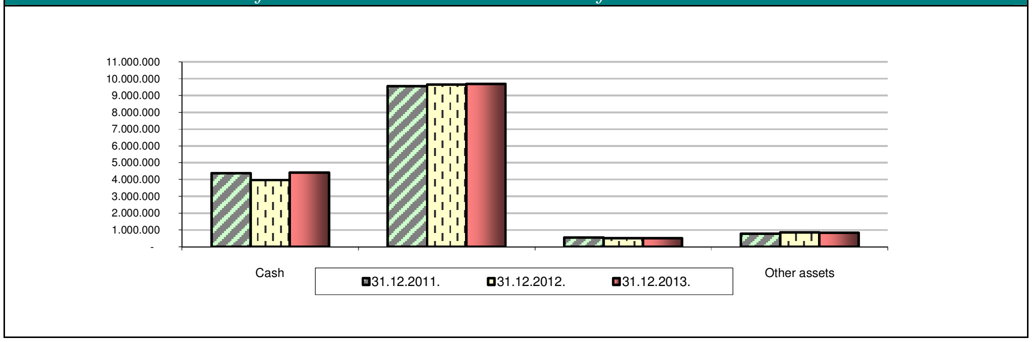
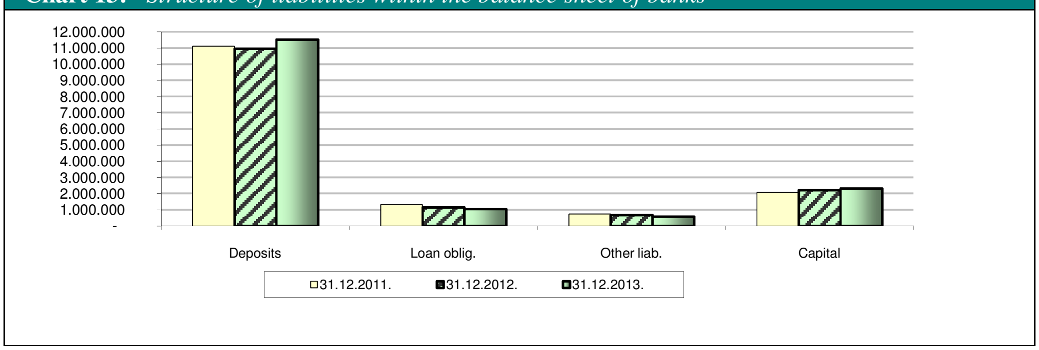


Chart 13: *Structure of liabilities within the balance sheet of banks*



Within the liabilities structure of the banks' balances sheets, deposits still represent a dominant source of financing for banks in the FB&H (with an amount of KM 11.5 billion or 74.6% share). After the decrease of 9%, the share of loan obligations of KM 1.04 billion dropped from 7.6% to 6.7%, while the share of capital rose from 14.8% to 15.0% (wherein, it amounted to KM 2.3 billion as of 31.12.13).

As with structure of assets, financing sources included slight changes related to two key assets items: reduction of loan share from 71.1% to 70.2% and decrease of cash from 26.4% to 28.6%.

- in 000 KM-

Chart 14: *Cash funds of banks*

CASH FUNDS	31.12.2011		31.12.2012		31.12.2013		INDEX	
	Amount	% share	Amount	% share	Amount	% share	4/2	6/4
1	2	3	4	5	6	7	8	9
Cash	371.309	8,5	411.726	10,4	431.592	9,8	111	105
RR with CB B&H	2.351.811	53,7	2.130.626	53,8	2.622.277	59,4	91	123
Accounts with deposit inst. in B&H	20.618	0,5	1.930	0,0	25.181	0,6	9	1305
Accounts with deposit inst. abroad	1.633.479	37,3	1.417.857	35,8	1.338.347	30,3	87	94
Cash in process of collection	859	0,0	442	0,0	501	0,0	51	113
TOTAL	4.378.076	100,0	3.962.581	100,0	4.417.898	100,0	91	111

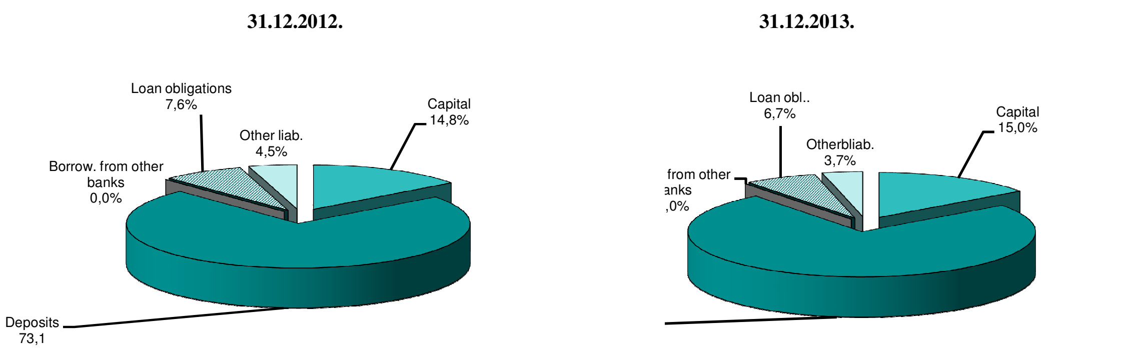
Two main changes related to cash funds are as follows: balances on the reserve account with CBBH and balances on banks' accounts abroad had a different trend. After the decrease of 9% in 2012, cash funds of banks at the CBBH reserves account rose by significant 23% or KM 492 million in 2013, hence their amount as of 31.12.13 was KM 2.6 billion or 59.4% of total cash funds (vs. 53.8% in 2012). On the other hand, banks' funds on accounts with deposit institutions abroad posted a lower decrease rate of 6% or KM 79 million in 2013 vs. 2013 when they posted a drop of 13%. Resultantly, as of 31.12.13, their amount equaled KM 1.3 billion KM or 30.3% of total cash funds (vs. 35.8% as at YE2012). As for the cash funds held in vault and cash desks, after their growth of 5% or KM 20 million, banks posted an amount of KM 432 million of such cash as of 31.12.13, which represented 9.8% of total cash funds.

These trends prompted a change of the currency structure of cash funds: in the observed period, the share of local currency rose from 60.4% to 66.4%, while cash in foreign currency declined by the same percentage..

2. 1. 1. Liabilities

Total liabilities structure (liabilities and equity) within the banks' balance sheet as of 31.12.13 is provided in the chart below:

Chart 14: S*tructure of banks' liabilities*



During the observed period, the share of deposits (74.6% as the most significant source of financing of banks rose by 1.5%, while the share of ST loans, the second largest source of financing, declined from 7.6% to 6.7%.

The deposits increase is a result of their increase in 2'13 by 5.1% or KM 563 million. Hence, as of 31.12.13 they arrived to KM 11.5 billion and are still the largest source of financing for banks in the Federation of B&H. Of note, in May 2013, Federation o B&H received the3rd tranche of funds based on the stand-by arrangement with the IMF of KM 50.5 million, the 4th tranche in the equivalent amount was received on 01.07.2013 and the 5th tranche of KM61.7 million was received in late October 2013 (in 2012, FB&H received a total of app. KM 163 million, where the first and second tranche totaled to KM 153 million).

The second largest source of financing are loans of KM 1.04 billion that banks received mostly from foreign financial institutions. In the past 3 years, due to the effect of the financial and economic crisis, banks incurred lesser loans abroad and, coupled with payment of matured deposits, reduced these sources of financing by app. 50% (YE208, deposits amounted KM 2.18 billion). In 2012, the decrease amounted 13.5% or KM 178 million, while in 2013 these sources dropped by 9% or KM 102 million.

If we add subordinated debts of KM 165 million to loans, total loan funds holds a share in total sources of financing of 7.8%. The subordinated debt was incurred by banks to strengthen their capital base and improve capital adequacy.

As of 31.12.13, banks held the largest amount of liabilities towards the following creditors (6 out of total of 36 creditors) taking up 72% of their total loan obligations: European Investment Bank (EIB), TC ZIRAAT BANKASI A.S. (Turkey), UniCredit Bank Austria AG, European Fund for Southeast Europe (EFSE), EBRD and Council of Europe Development Bank.

As of 31.12.13, capital position stood at KM 2.3 billion and was by 4.2% or KM 93 million higher than as at YE2012. This growth was mostly achieved as a net result of a capital increase of three banks, thus receiving fresh money from external sources (new issue of shares and reserve payment) of KM 130 million and as a result of the reduction due to the transfer to liabilities for dividends from Y2012 profit (KM 31 million).

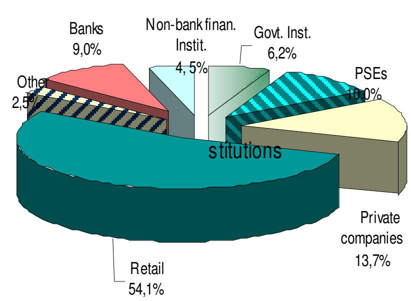
According to information provided by banks, out of the total deposit amount as of the observed period in 2013, only 6.6% relates to deposits collected in organisational parts of FB&H banks doing business in the Republika Srpska and the Brcko District.

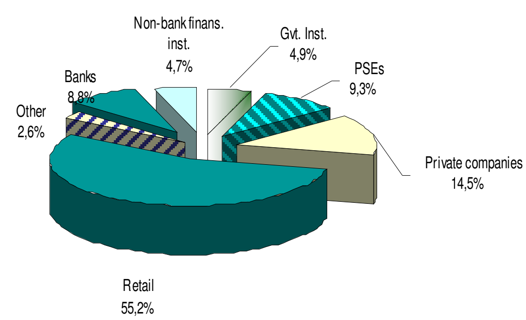
- in 000 KM-

Table *Deposit structure by industry sectors*[14]

SECTORS	31.12.2011		31.12.2012		31.12.2013		INDEX	
	Amount	% share	Amount	% share	Amount	% share	4/2	6/4
1	2	3	4	5	6	7	8	9
Government institutions	705.805	6,3	682.313	6,2	565.533	4,9	97	83
Public sector entities	1.413.686	12,7	1.090.870	10,0	1.076.527	9,3	77	99
Private companies and enterprises	1.462.767	13,1	1.501.232	13,7	1.668.034	14,5	103	111
Banking institutions	1.280.463	11,5	981.562	9,0	1.012.274	8,8	77	103
Non-banking finan.institutions	483.504	4,3	493.689	4,5	535.915	4,7	102	109
Retail	5.530.461	49,7	5.933.071	54,1	6.366.218	55,2	107	107
Other	247.989	2,4	278.264	2,5	299.348	2,6	112	108
TOTAL	11.124.675	100,0	10.961.001	100,0	11.523.849	100,0	99	105

Chart 15: *Deposit structure by industry sectors*





[14] Information originate from the auxiliary form BS-D to the balance sheet that banks deliver on a quarterly basis to the FBA (as based on the FBA model).

31.12.2012. **31.12.2013.**

In 2013, minor changes occurred in the deposit structure by sectors that, on one hand, mostly relate to the deposit increase of retail segment, private companies and banks and, on the other hand, to reduced level of funds of government institutions and public sector entities.

Although the effect of economic and financial crisis has been present for five years now and its adverse effects are evident with most of business segments of banks, it should be noted that retail deposits displayed a continuous growth in that same time period, i.e. they rose from KM 4.18 billion inYE2008 to KM 6.4 billion as of 31.12.13 (i.e. up by significant 52% or KM 2.2 billion). In 2013, as in the previous two years, the growth rate was 7% or KM 433 million, while their share in total deposits rose from 54.1% to 55.2%, so the retail deposits are still the largest source of financing for banks. Analytical data indicate that 16 out of 17 banks have the largest share of retail deposits that ranges from 33% to 88%.

The second largest source of financing of the banking sector (based on the amount and the share) is with deposits of private companies. In the period from 2008-2012 (along with periodical oscillations), their amount was app. KM 1.5 billion (the lowest amount of KM 1.4 billion was posted at the end of 2009). In 2013, deposits of this industry sector had a solid growth of 11% or KM 167 million, i.e. they arrived to a total amount of KM 1.7 billion, while their share rose by 0.8% to 14.5% of total deposits.

On the other hand, PSEs deposits in the past five years underwent significant oscillations. After major drop by 23% or KM 323 million in 2012, they posted a only a slight drop in 2013 of 1% or KM 14 million. As at YE2013, they amounted to KM 1.1 billion and held a share of 9.3% in total deposits (thus being the third largest source of financing for the banking sector). However, analytical data show that five banks use them as the second largest source of financing, where this share is between 14% and 28%.

From the end of 2007 until 3Q 2011, deposits of banking institutions were the second largest source among the deposit potential of banks. The growth trend was maintained by mid-2009 when they reached its peak of KM2.3 billion and a share of 21.4% in total deposits. After that, due to the crisis, reduced volume of lending and high liquidity, parent groups withdrew their deposits, thus resulting in the reduced share of these funds. Also, their decrease in 4Q 2011 of 19% or KM 294 million caused a decrease in their share in total deposits to 11.5% (which was the fourth largest share in total deposits of the sector as at YE2011). In 2012, the trend of decrease continued with a rate of 23% or KM 299 million and in 2013 this adverse trend was brought to a halt solely as a result of net increase of deposits in late December 2013 of app. KM 70 million. This related to ST deposits of parent groups (1 month term) towards two banks for purpose of maintaining maturity and FX position within the defined limits. Hence, in 2013, a slight increase was seen of 3% or KM 31 million. Negative trends of prior years (related to these funds at the sector level) are mostly a result of debt reduction, i.e. repayment of funds to groups – owners of banks in the FB&H.

At the end of 2013, deposits of banking institutions stood at KM 1.01 billion which represents 8.8% of all deposits. These funds are by KM 27 million smaller than loans, which are the second largest source of funds in the FB&H, just after deposits. Based on mentioned information, we find that foreign debt level of FB&H banks is much lower, especially in terms of deposit funds of parent groups. Considering that the same reduction trend is present with regards to loan obligations, banks are once again facing the problem of maintaining their maturity matching, as caused by an unfavorable maturity of local deposit funds, due to which they are forced to obtain quality sources of funds in the period ahead in order to uphold the trend of increase in loans approved.

Also worth noting is that 91% or KM 923 million of deposits of banking institutions relates to deposits of banks from the group (shareholders mostly). Financial support by parent groups is present with regards to nine banks in the FB&H, wherein such financing is still concentrated among five large banks (95%). In this way, banks under majority foreign ownership had financial support and secured inflows of new funds by their foreign groups. If these funds are coupled with loan obligations and subordinated debts (items posted within the supplementary capital), the financing of banks from the group would still be higher (with regards to 11 banks) and amounted to KM1.3 billion as of 31.12.13 (or 8.6% of total liabilities of the banking sector (vs. KM 1.4 billion or 9.3% of liabilities as at YE2012). Within total deposits, funds of banking groups hold a share of 8% (vs. 8.4% as at YE2012), while loan obligations to the group represent 26.1% of total loan obligations (this share went down by 3%). Compared to the end of 2012, these funds dropped by 4.3% or KM 60 million (vs. 21.7% or KM 387 million in 2012), as largely based on regular maturities (deposits rose by 0.3% or KM 3 million and loan obligations dropped by 18.6% or KM 62 million, as well as subordinated debts by 1% or KM 1 million).

Considering that lending activities of banks got reduced significantly due to the economic crisis, thus resulting in high liquidity and good capitalisation rate of most of foreign-owned banks in the FB&H, the trend of the previous two years, where exposures towards groups got reduced, has halted in late 2013. This primarily relates to the segment of deposit sources, while loan sources are reducing largely on basis of regular repayments of liabilities due. For reasons of unfavorable occurrences in the economies of home countries of owners of banks from the FB&H, problems these countries are facing and resultantly problems of their financial systems and banking groups, as well as measures taken in Austria to strengthen and ensure sustainability of business models of their large internationally active banking groups and to preserve its country credit rating[15], the financial support of parent banking groups got significantly reduced, so the loan growth in the following period in the FB&H will have to rely more on local sources of funds.

At times of crisis and difficulties with accessing money markets and new funds, increase of liquidity risk as a result of impaired collection rate of loans and growth of uncollectable receivables, unsatisfactory maturity structure of local deposit sources and expected further reduction of foreign sources of financing, the problem with unfavorable maturity structure of sources of financing (deposits primarily) and their growth will be in focus of most of banks in the period ahead.

Deposits of other sectors also went under minor changes in terms of their amount and share and the biggest change refers to deposits of government institutions that displayed a continuous trend of decrease over the past three years. In 2013, they got reduced by 17% or KM 117 million. This decrease would have been even greater if the FB&H had not received funds based on the 4th tranche of the stand-by arrangement with the IMF of altogether KM 163 million (KM 50.5 million in May and July 2013 respectively, while funds of the 5th tranche of KM 61.7 million were received in late October 2013, noting therein that first two tranches were drawn in 2012: KM 79 million in September and KM74 million in December 2012). As of 31.12.13, deposits of this sector amounted to KM 566 million and represented 4.9% of total deposits.

The currency structure of deposits as of 31.12.13 has slightly changed: deposits in foreign currency (with a dominant share of EUR currency) amount to KM 6 billion and their share dropped from 53.7% to 51.9% and deposits in local currency amount to KM 5.5 billion and hold the share of 48.1%.

At the end of 2013, the structure of deposits by domicile status of depositors was the same as at the end of 2012: resident funds amounted to KM 10.2 billion and had a share of 88.7% while non-resident deposits stood at KM 1.3 billion and represented 11.3% of total deposits. Resident deposits rose by 5.2% or KM 502 million, while non-resident deposits increased from 4.9% or KM 61 million. Over the past four years, non-resident deposits had continuously dropped, as a result of withdrawal, i.e. return of deposits to the parent bank or member of the banking group (where nonresident funds

[15] In essence, these measures mean that lending activities of subsidiaries of Austrian banks in the Central, Eastern and Southeastern Europe (CESEE) will be conditioned by stronger and sustainable financing from local sources.

mostly refer to these entities). Non-resident deposits had the largest share of 22.1% and nominal amount of KM 2.31 billion at the end of 2008.

In 2013, savings deposits, as the most significant segment of deposit and financial potential of banks posted an increase of 7.7% or KM 445 million and amounted to KM 6.2 billion as of 31.12.13.

Table 16: *New retail savings by periods*

BANKS	AMOUNT (IN 000 KM)			INDEX	
	31.12.2011	31.12.2012	31.12.2013	3/2	4/3
1	2	3	4	5	6
State-owned	50.259	58.050	65.179	116	112
Private	5.311.178	5.698.300	6.135.693	107	108
TOTAL	5.361.437	5.756.350	6.200.872	107	108

Chart 16: *New retail savings by periods*

Two largest banks hold 58% of savings, while eight banks hold individual share of 2%, thus representing 8.7% of total savings at the level of the banking system.

Out of the total amount of savings, 37% refers to saving deposits in local currency and 63% in foreign currency.

Table 17: *Maturity structure of retail savings deposits by periods*

BANKS	AMOUNT (IN 000 KM)						INDEX	
	31.12.2011		31.12.2012		31.12.2013		3/2	4/3
1	2		3		4		5	6
ST savings deposits	2.606.732	48,6%	2.656.934	46,2%	2.911.809	47,0%	102	110
LT savings deposits	2.754.705	51,4%	3.099.416	53,8%	3.289.063	53,0%	113	106
TOTAL	5.361.437	100,0 %	5.756.350	100,0 %	6.200.872	100,0 %	107	108

Compared to the end of 2012, maturity structure of savings deposits changed slightly through an increase of short term deposits by 10% or KM 255 million, while long term deposits grew by 6% or KM 190 million, thus resulting in slightly changed share of LT deposits from 53.8% to 53.0%.

Long standing continuous growth and positive trends in the savings segment of banks in the FB&H have resulted, on one hand, from better safety and stability of the overall banking system (as chiefly attributable to the functional, effective and efficient banking supervision implemented by the FBA) and, on the other hand, from existence of the deposit insurance segment whose primary objective is increased stability of the banking, i.e. financial sector, and protection of savers. In order to preserve and strengthen trust of citizens in safety and stability of the banking system in B&H, the deposit insurance level rose to KM 20,000 in 2008. After that, an initiative was taken to increase the insured deposit level. Accordingly, on 01.04.10, this level climbed to KM 35,000. According to the latest decision by the management board of the B&H Deposit Insurance Agency from December 2013, the insured deposit limit rose from the present KM 35,000 to KM 50,000, with the effect date starting from 01.01.14. All these actions are aimed towards limiting the effect of the global economic crisis in the banking and the overall economic system in the FB&H and B&H.

As of 31.12.13, there were a total of 16 banks from the FB&H that are included in the deposit insurance program (i.e. holding licenses issued by the B&H Deposit Insurance Agency). There is one bank that is not eligible for this program as it does not meet the criteria defined by the B&H Deposit Insurance Agency (due to existing composite rating).

2.1.2. Capital – strength and adequacy

Capital position[16] in FB&H banks as of 31.12.13 stood at KM 2.3 billion.

-in 000 KM-

Table 18: *Regulatory capital*

DESCRIPTION	31.12.2011		31.12.2012		31.12.2013		INDEX	
1	2		3		4		5 (3/2)	6 (4/3)
1.a.**Core capital before reduction**	2.008.081		1.913.841		2.155.188		95	113
1.1. Shareholders capital –common and permanent non-cumulative shares	1.190.482		1.198.516		1.200.644		101	100
1.2. Issue premiums	136.485		136.485		136.485		100	100
1.3.Reserves and retained profit	681.114		578.840		818.059		85	141
1.b.Deductible items	353.960		191.304		294.514		54	154
1.1. Uncovered losses from previous years	251.187		120.740		112.610		48	93
1.2. Current year loss	45.512		17.818		140.330		39	788
1.3. Treasury shares	81		156		156		192	100
1.4.. Intangible assets	57.180		52.590		41.418		92	79
1. Core capital (1a-1b)	**1.654.121**	**78%**	**1.722.537**	**79%**	**1.860.674**	**80%**	104	108
2. Supplementary capital	**466.968**	**22%**	**467.100**	**21%**	**457.047**	**20%**	100	98
2.1. Shareholders capital-permanent preferred cumulative shares	3.090		3.090		3.091		100	100
2.2. General loan loss provisions	212.248		211.433		215.083		100	102
2.3Amount of audited profit	62.564		67.243		71.984		107	107
2.4. Subordinated debt up to 50% of the core capital	139.754		120.264		165.473		86	138
2.5. Permanent items	49.312		65.070		1.416		132	2
3. Equity (1 + 2)	**2.121.089**	**100%**	**2.189.637**	**100%**	**2.317.721**	**100%**	103	106
4. Deductible items from the capital	**37.794**		**98.848**		**161.703**		261	164
4.1. Bank's share in capital of other legal entities above 5% of core capital	18.408		3.043		2.844		17	93
4.2. LLP shortfall at the regulator's request	19.386		95.720		158.859		494	166
4.3. Other deductible items	-		85		0		N/a	N/a
5. Net capital (3- 4)	**2.083.295**		**2.090.789**		**2.156.018**		100	103

In 2013, capital[17] rose by 6% or KM 128 million, thus including a minor change in its structure (80% core capital and 20% supplementary capital). Core capital increased by 8% or KM 138 million, while supplementary capital dropped by 2% or KM 10 million.

The core capital increase mostly refers to the transfer of one part of profit earned in 2012 from supplementary to core capital, as well as to the capital increase of two banks of altogether KM 34 million, reserve payment by one bank of KM 97 million and posting of audited profit earned in 2013 regarding one bank.

Core capital changes were also affected by the following: liquidation of one bank (reduction by KM 4 million) and exclusion from capital of one bank of an amount of KM 5 million (as per the FBA order).

Deductible items (from the core capital) rose by KM 103 million, as largely due to current loss of KM 140 million (of which KM 116 million refers to one bank), while, on the other hand, uncovered losses

[16] Regulatory capital is defined in Article 8 and 9 of the Decision on Minimum standards for Capital Management in –anks (Official Gazette of the FB&H No. 3/03, 18/03, 53/06, 55/07, 81/07, 6/08, 86/10, 70/11).

[17] Source of information: quarterly Report on Capital Condition in Banks (Form 1-Table A), as defined by the Decision on Minimum Standards for Capital Management in Banks.

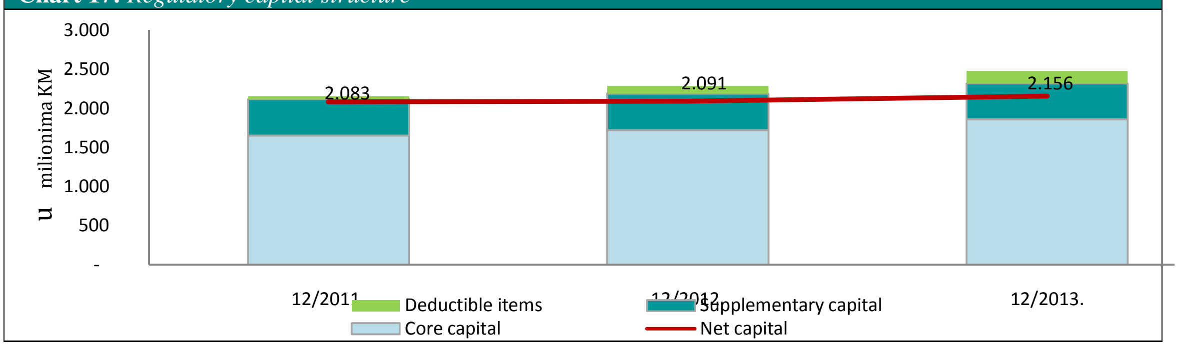
rose by KM 26 million (of which KM 24 million refers to one bank whose banking license has been revoked in June 2013), as well as due to partial coverage of the uncovered loss regarding three banks of altogether KM 2 million and reduction of intangible assets by KM 11 million.

Supplementary capital dropped by 2% or KM 10 million, thus including significant changes to its structure: one part of Y2012 profit of KM 67 million was transferred into the core capital, subordinated debts rose by KM 45 million (mostly with regards to one bank of KM 40 million), general LLP rose by KM 4 million, while permanent items dropped by KM 64 million (they got converted into core capital with regards to one bank). There are eight banks that included the current audited profit into its core capital (of altogether KM 72 million).

According to regulatory changes in late 2011, deductible items from capital include also LLP shortfall upon regulator's request (i.e. a difference between required regulatory loan loss provisions according to balance sheet and off-balance sheet items[18] and loan loss provisions formed against profit). As of 31.12.13, this item amounted to KM 159 million, up by 66% or KM 63 million than as at YE2012.

The chart below shows the regulatory capital structure.

Chart 17: *Regulatory capital structure*



As a result of the said changes, net capital rose by 3% or KM 65 million and amounted to KM 2.2 billion as of 31.12.13.

Capital adequacy of individual banks, i.e. the overall system, depends, on one hand, from the net capital level, and, on the other, from total risk weights (risk weighted assets and weighted operational risk).

[18] Banks recognise required regulatory reserves when the value adjustment (according to IAS) is below calculated regulatory reserves, as determined at the level of individual debtor. This methodology is in application since 30. 06. 2012.

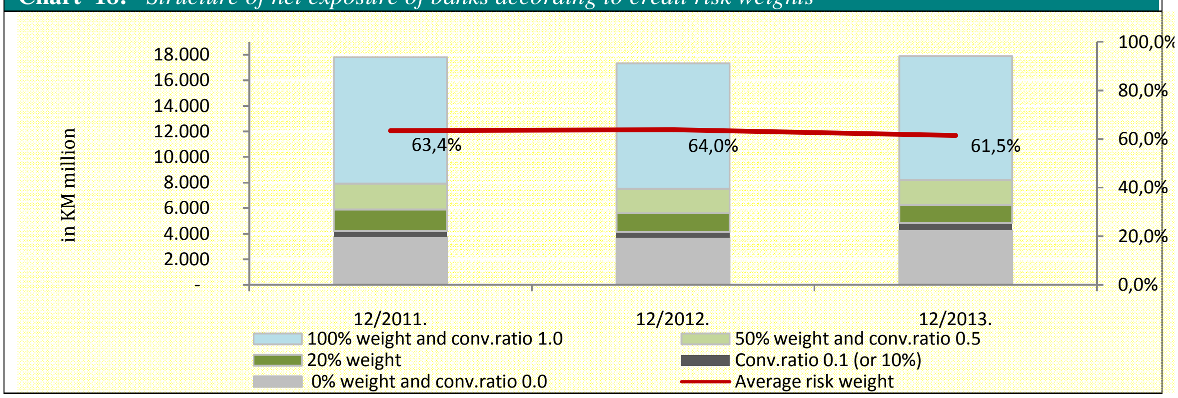
The table below provides a structure of net exposures of banks according to credit risk weights, i.e. conversion ratios for off-balance sheet items.

-in 000 KM-

Table 19: *Structure of net exposure of banks according to credit risk weights*

DESCRIPTION	31.12.2011	31.12.2012	31.12.2013	INDEX	
1	2	3	4	5 (3/2)	6 (4/3)
TOTAL EXPOSURE (1+2):	**17.814.140**	**17.310.579**	**17.894.350**	97	103
1 Balance sheet assets	14.987.978	14.568.957	14.969.857	97	103
2. Off-bal.sheet items	2.826.162	2.741.622	2.924.493	97	107
DISTRIBUTION BY RISK WEIGHTS AND CONVERSION RATIOS					
0% weight	3.721.678	3.647.306	4.198.260	98	115
20% weight	1.674.585	1.460.689	1.424.069	87	97
50% weight	83.165	53.155	33.110	64	62
100% weight	9.508.550	9.407.807	9.314.418	99	99
0,0 conversion ratio	54.529	51.131	86.947	94	170
0,1 conversion ratio	445.006	449.627	550.966	101	123
0,5 conversion ratio	1.938.361	1.867.703	1.916.110	96	103
1,0 conversion ratio	388.266	373.161	370.470	96	99
RISK WEIGHTED ASSETS AND LOAN EQUIVALENTS	**11.286.997**	**11.078.498**	**10.999.406**	**98**	**99**
Average risk weight	**63,4%**	**64,0%**	**61,5%**	**101**	**96**

Chart 18: *Structure of net exposure of banks according to credit risk weights*



Total net exposure of banks being weighted is higher by 3% or KM 584 million vs. the end of 2012, as mostly affected by the growth of balance sheet items with the risk weight 0% (cash funds), i.e. with their growth of 15% or KM 551 million. Since these items have no effect on the level of risk weighted assets and since other items with risk weights of 20%, 50% and 100% went down slightly, the risk weighted assets and loan equivalents dropped by 1% or KM 79 million and stands at KM 11 billion, while the average weight went down from 64.0% to 61.5%.

Contrary to the trend of risk weighted assets and loan equivalents, weighted operational risk (WOR) rose by 1% and stand at KM 981 million.

All of this has resulted in a slight decrease of total weighted risks. As of 31.12.13, the share of weighted assets exposed to credit risk was 92% and to operational risk was 8%.

As of 31.12.13, banks' capitalisation rate, expressed as a ratio between capital and assets, amounted 13.9%, up by 0.3% vs. YE2012.
One of key indicators of the capital strength and adequacy[19] of banks is the capital adequacy ratio representing a ratio between net capital and risk weighted assets. At the banking sector level, this ratio stood at 18.0% as of 31.12.13, up by 0.7% vs. YE2012. Out of the total profit of KM 140 million generated as of 31.12.13, the capital adequacy calculation accounted for KM 128 million.

Although operations of the banking sector have been affected by the economic crisis for five years now, i.e. have been affected by adverse macroeconomic and financial trends in both, Euro one countries and countries of the region, as well as due to the poor economic recovery of the real sector and overall economy in B&H, the capital adequacy of the banking sector has been continuously maintained at the level above 16% and above 17% in the past three years. Reason to this is, on one hand, in the credit growth stagnation and in the decrease of overall weighted risks, and, on the other, in the fact the banks have maintained the largest share of profit from previous years within their capital and several banks have improved their capitalization rate by means of additional capital injections. However, problems related to the increase of non-performing loans and items not covered by loan loss provisions (net non-performing assets) may, in the period ahead, significantly impact and cause weakening of the capital base with several banks. This is conditioned by continued negative trends regarding the assets quality and by worsening and increase of non-collectable loans. This is illustrated by the following information: at the end of 2008, net non-performing assets stood at KM197 million and its ratio (vs. core capital) was 13.2%. At the end of 2013, net non-performing assets reached an amount of KM 474 million and the ratio was 25.5%. Also, according to the existing regulations, banks to not calculate the capital requirement for market risks, due to which the capital adequacy rate is higher.

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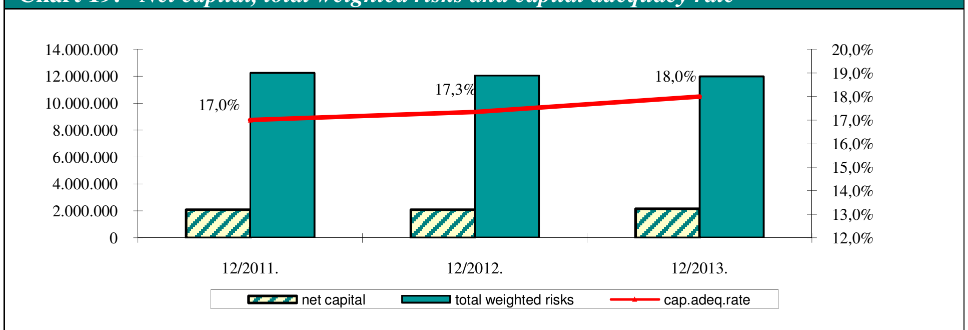
Table 20: *Net capital, total weighted risks and capital adequacy rate*

DESCRIPTION	31.12.2011	31.12.2012	31.12.2013	INDEX	
1	2	3	4	5(3/2)	6(4/3)
1. NET CAPITAL	2.083.295	2.090.789	2.156.018	100	103
2. RISK WEIGHTED ASSETS AND LOAN EQUIVALENTS	11.286.997	11.078.498	10.999.406	98	99
3. WOR (WEIGHTED OPERATIONAL RISK)	965.932	974.201	981.318	101	101
4. TOTAL WEIGHTED RISKS (2+3)	12.252.929	12.052.699	11.980.724	98	99
5. NET CAPITAL RATE (CAPITAL ADEQUACY) (1/ 4)	17,0%	17,3%	18,0%	102	104

Chart 19: ***Net capital, total weighted risks and capital adequacy rate***

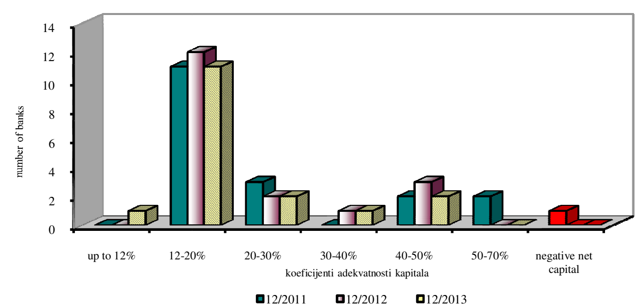


Capital adequacy rate of the banking system as of 31.12.13 was 18.0%, which is still quite above the legal minimum (12%) and represents a satisfactory capitalization rate of the overall system

[19] Legally defined minimum capital adequacy rate is 12%.

considering the existing level of risk exposure and poses strong basis and foundation for preservation of its safety and stability.

Chart 20: *Capital adequacy ratios of banks*



Out of the total of 17 banks in the FB&H as of 31.12.13, 16 banks had the capital adequacy ratio above the legal minimum of 12%, while one bank had this ratio below the legal minimum. According to analytical data, 10 banks had the capital adequacy rate below the rate as at YE2012 (ranging from 0.3% to 15.6 percentage points) and seven banks had this rate above the one at the end of 2012. Two largest banks in the system increased their capital adequacy rate vs. the one at the end of 2012 and it exceeds 18%.

Find below is an overview of capital adequacy rates of banks vs. the legal minimum of 12%:

- 1 bank had the rate below 12% (8.1%),
- 7 banks had the rate between 12.5% and 15.5%,
- 3 banks had the rate between 17.9% and 19.3%,
- 3 banks had the rate between 20.0% and 21.7% and
- 3 banks had the rate between 35.9% and 49.3%.

By performing supervision of operations and financial condition of banks in the FB&H in line with its legal competencies and for purpose of improving safety of individual banks and the banking system as a whole, FBA instructed banks to take appropriate measures to strengthen their capital base and ensure capital adequacy in terms of level and profile of the existing and potential exposure to all risks inherent with the banking operations. One of measures taken by the FBA to preserve and strengthen capital base and safety and stability of banks is to adopt actions[20] on temporary restrictions and minimum requirements for dividends and discretionary bonus disbursement and repurchase of own shares by banks (with 31.12.12 as the effect date).

As insofar, the priority task of most of banks in the system is to further strengthen the capital base, wherein the focus is placed on large banks in the system, especially due to changes in the business and operating environment of the FB&H, actions caused by and negative effects of the global financial and economic crisis to our country, banking sector and the overall economy in B&H. Also, the focus is on banks with adverse trends regarding assets quality, which further negatively reflects upon the capital and represents a realistic possibility for additional weakening of the capital base. Under conditions of economic crisis and credit risk growth caused by the downfall of the loan portfolio quality (due to an increase of uncollectible receivables), this requirement has a high priority and the capital segment is therefore under a continuous reinforced supervision in order to prevent impaired stability of banks and erosion of the capital base to the level that may jeopardize bank operations and impact the stability of the entire banking system.

[20] Decision on Temporary Restrictions and Minimum Requirements for Dividends and Discretionary Bonus Disbursement and Repurchase of Own Shares by Banks (FB&H Official Gazette No. 15/13).

2.1.3. Assets and Assets Quality

The Decision on Minimum Standards for Credit Risk Management and Assets Classification in Banks defines criteria for an assessment of banks' exposure to credit risk by means of the assets quality assessment and assessment of adequacy of reserves for loan and other losses as per risk level of loans and balance sheet and off-balance sheet assets items.

With the effect date of the Law on Accounting and Audit in the FB&H, i.e. starting from 31.12.11, banks are required to prepare and present financial statements in line with the International Accounting Standards (IAS) and the International Financial Reporting Standards (IFRS), whereas recognition and measurement of financial assets and liabilities is subject to the IAS 39 – Financial instruments, recognition and measurement and the IAS 37 – Provisioning, contingent liabilities and contingent assets. This is to say that, during the assessment of banks' exposure to the credit risk, banks are required to continue calculating loan loss provisions in line with the criteria from the Decision on Minimum Standards for Credit Risk Management and Assets Classification in Banks, considering therein already formed value adjustments of balance sheet assets and loss provisions for off-balance sheet items carried on banks' books, as well as loan loss provisions formed against profit (found on capital accounts).

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Table 21: Assets *(BS and off-BS), LLP according to the regulatory body and value adjustments according to IAS*

DESCRIPTION	31.12.2011	31.12.2012	31.12.2013	INDEX	
1	2	3	4	5(3/2	6(4/3)
1. Risk-bearing assets[21]	13.376.110	13.286.676	13.517.944	99	102
2. Calculated regulatory reserves for loan losses	1.294.757	1.370.669	1.504.174	106	110
3. Value adjustment and reserves for off-balance sheet items	1.039.529	1.092.535	1.252.464	105	115
4. Required regulatory reserves formed against profit for assessed losses	255.228	411.077	413.508	161	101
5. Formed regulatory reserves for against profit for assessed losses	292.225	315.734	315.734	108	100
6. Shortfall of regulatory reserves formed against profit for assessed losses	19.386	111.565	158.859	575	142
7. Non-risk bearing items	5.787.457	5.579.911	6.144.833	96	110
8. TOTAL ASSETS (1+7)	19.163.567	18.866.587	19.662.777	98	104

Total assets with off-balance sheet items (assets)[22] of banks in the FB&H amounted to KM 19.7 billion as of 31.12.13 and are higher by 4% or KM 796 million vs. YE2012. Risk-bearing assets amount to KM 13.5 billion and are up by 2% or KM 231 million.

Non-risk bearing items stand at KM 6 billion or 31% of total assets with off-balance sheet items, thus being up by 10% or KM 565 million vs. the YE2012.

Total calculated LLP based on regulatory requirements amount to KM 1.5 billion and formed value adjustments for balance sheet assets and provisions for losses under off-balance sheet items amount to KM 1.3 billion. Required regulatory reserves[23] amount to KM 414 million and went up by 1% or KM 2 million. Formed regulatory reserves against profit amount to KM 316 million and they remained at the same level as a result of changes in regulations, i.e. LLP shortfall being posted at the end of the business year (starting from 31.12.12) is not covered against profit, but still represents a deductible

[21] Does not include amount of facilities and contingent liabilities of KM 274 million that is secured with a cash deposit.
[22] Assets, as defined in Article 2 of the Decision on Minimum Standards for Credit Risk Management and Assets Classification in Banks (FB&H Official Gazette Nos. 3/03, 54/04, 68/05, 86/10, 6/11, 70/11, 85/11; 85/11-consolidated text; 15/13).
[23] Required regulatory reserves represent a positive difference between calculated LLP and value adjustments (calculated LLP are higher than value adjustments).

item from the capital and affects the capital adequacy calculation. Regulatory reserves shortfall [24] as of 31.12.13 stand at KM 159 million and posted a high growth rate of 42% or KM 47 million vs. YE2012, as a result of continuous worsening of the loan portfolio quality.

Table 22: *Total assets, gross balance sheet assets, risk-bearing and non-risk bearing assets items*

DESCRIPTION	31.12.2011		31.12.2012		31.12.2013		INDEX	
	Amount	Struct. %	Amount	Struct. %	Amount	Struct. %		
1.	2	3	4	5	6	7	8 (4/2)	9 (6/4)
Loans	9.364.121	85,4	9.347.370	85,2	9.396.444[25]	84,3	100	101
Interest	109.696	1,0	86.650	0,8	81.456	0,7	79	94
Past due receivables	937.899	8,5	1.049.891	9,5	1.144.042	10,3	111	109
Receivables based on paid guarantees	24.808	0,2	24.360	0,2	31.783	0,3	98	130
Other facilities	171.052	1,5	172.479	1,6	201.786	1,8	101	117
Other assets	371.127	3,4	292.440	2,7	294.623	2,6	79	101
1.RISK-BEARING BALANCE SHEET ASSETS	10.978.703	100,0	10.973.190	100,0	11.150.134	100,0	100	102
2. NON-RISK BEARING BALANCE SHEET ASSETS	5.290.275		5.084.000		5.523.247		96	109
3.GROSS BALANCE SHEET ASSETS (1+2)	16.268.978		16.057.190		16.673.381		99	104
4.RISK-BEARING OFF-BAL.SHEET ITEMS	2.397.407		2.313.486		2.367.810		96	102
5.NON-RISK BEARING OFF-BAL.SHEET ITEMS	497.182		495.911		621.586		100	125
6.TOTAL OFF-BAL.SHEET ITEMS (4+5)	2.894.589		2.809.397		2.989.396		97	106
7.RISK-BEARING ASSETS WITH OFF-BAL.SHEET ITEMS (1+4)	13.376.110		13.286.676		13.517.944		99	102
8. NON-RISK BEARING ITEMS (2+5)	5.787.457		5.579.911		6.144.833		96	110
9. ASSETS WITH OFF-BAL.SHEET ITEMS (3+6)	19.163.567		18.866.587		19.662.777		98	104

Gross balance sheet assets[26] amount to KM 16.7 billion and it went up by 4% or KM 616 million, while risk-bearing balance sheet assets stand at KM 11.2 billion or 67% of gross balance sheet assets (thus being by 2% or KM 177 million higher than at the end of 2012). Non-risk bearing balance sheet assets amount to KM 2.4 billion and are by 2% or KM 54 million higher, while non-risk bearing items amount to KM 662 million and are 25% or KM 126 million higher than at the YE2012.

The economic crisis effect on the total economy and industry in B&H is still pronounced, as significantly impacting the key business segment of banks – the lending segment. In 2012, banks posted a minimal loan increase of 2% or KM 178 million and this trend continued in 2013 where the growth level was 2% or KM 186 million. As of 31.12.13, loans stood at KM 10.9 billion and their share in assets dropped by 1 percentage point and equals 70.2%.

However, based on analytical data, we find that this loan growth was largely generated from an increase of past due, uncollected receivables (default receivables). In 2012, their increase rate was 15% or KM 135 million, i.e. their overall amount was KM 1 billion, while they rose by 11% or KM 110 million in 2013 and achieved an amount of KM 1.1 billion as of 31.12.13. This leads to a conclusion that the real loan growth in the past two years was negligible (0.4% in 2012 and app. 0.7% in 2013).

In 2013, a total of KM 6.7 billion of new loans was approved, which is 12% or KM 717 million higher than in the year before. Out of the total loans approved, 67% relates to the corporate segment and 28% to the retail segment (as of 31.12.12: 71% corporate segment, 25% retail segment). The maturity structure of newly approved loans: 44% long term and 56% short term loans (as of 31.12.12: 41% long term and 59% short term).

[24] Shortfall of regulatory reserves represents a positive difference between required and formed LLP.

[25] This does not include the loan amount of KM 204 million secured with a cash deposit (included in non-risk bearing assets of the balance sheet).

[26] Data source: Report on classification of balance sheet assets and off-balance sheet items of banks.

Three largest banks in the FB&H have an aggregate amount of approved loans of KM 6.1 billion, thus holding a share of 56% in total loans at the banking system level.

The table below provides an overview of the trend and changes in shares of individual sectors regarding the total loan structure:

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Table 23: *Loan structure by industry sectors*

SECTORS	31.12.2011		31.12.2012		31.12.2013		INDEX	
	Amount	% share	Amount	% share	Amount	% share		
1	2	3	4	5	6	7	8(4/2)	9(6/4)
Government institutions	125.827	1,2	132.525	1,2	142.010	1,3	105	107
PSEs	257.547	2,4	251.233	2,4	259.769	2,4	98	103
Private companies and enterprises	4.989.796	47,6	5.141.359	48,2	5.202.269	47,9	103	101
Banks	16.411	0,2	11.177	0,1	6.671	0,1	68	60
Non-bank. finans.institutions	40.978	0,4	41.661	0,4	37.791	0,3	102	91
Retail	5.043.634	48,1	5.076.679	47,6	5.194.971	47,9	101	102
Other	13.478	0,1	11.490	0,1	8.919	0,1	85	78
TOTAL	10.487.671	100,0	10.666.124	100,0	10.852.400	100,0	102	102

In 2013, loan structure by industry sectors has slightly changed compared to 2012. Retail loans went up by 2% or KM 118 million and arrived to KM 5.2 billion (vs. YE2012: KM 5.1 billion) and loans to private companies posted a moderate increase of 1% or KM 61 million and stand at KM 5.2 billion (vs. KM 5.1 billion at the end of 2012). Retail loan growth also caused the increase of their share from 47.6% to 47.9%, while the share of private company loans dropped from 48.2% to 47.9%.

According to information delivered by banks (as of 31.12.13) regarding the retail loan structure by their purpose, the largest share of 75% is with consumer loans[27] (12/12: 74%), followed by housing loans of 22% (12/12: 23%), while the rest of 3% refers to loans to small crafts, small businesses and agriculture.

Three largest banks in the system have approved 63% of retail loans and 49% of private company loans (31.12.12: 62% retail, 52% private companies).

Currency structure of loans: the largest share of 66% or KM 7.2 billion refers to currency clause loans (EUR: KM 7 billion or 97%, CHF: KM 240 million or 3%), followed by local currency loans with the share of 33% or KM 3.5 billion, while the smallest share of 1% or KM 93 million refers to FCY loans (thereof, almost entire amount refers to EUR: KM 84 million or 90%). Total amount of loans with the currency clause in CHF of KM 240 million or 2.2% of total loan portfolio refers almost entirely to one bank within the banking system.

Since loans are the highest risk category of banks' assets, their quality represents one of key factors determining stability and success of their operations. Assets quality assessment is in fact an evaluation of credit risk exposure for banks, i.e. identification of potential loan losses.

The table below provides an overview of the quality of assets and off-balance sheet risk-bearing items, general credit risk and potential loan losses per classification categories.

[27] Including cards business.

Table 24: *Assets classification, general credit risk (GCR) and potential loan losses (PLL)*											
Classification category	**31.12.2011**			**31.12.2012**			**31.12.2013**			**INDEX**	
	Classified assets	**% share**	**GCR PLL**	**Classified assets**	**% share**	**GCR PLL**	**Classified assets**	**% share**	**GCR PLL**		
1	2	3	4	5	6	7	8	9	10	11(5/2)	12(8/5)
A	10.612.528	79,3	212.248	10.571.555	79,6	211.433	10.754.079	79,6	215.083	100	102
B	1.419.030	10,6	118.847	1.227.301	9,3	108.313	1.094.361	8,1	93.547	86	89
C	282.847	2,1	67.999	334.226	2,5	87.874	356.646	2,6	90.541	118	107
D	375.980	2,8	209.936	443.500	3,3	252.970	502.803	3,7	295.224	118	113
E	685.725	5,2	685.727	710.094	5,3	710.079	810.055	6,0	809.779	103	114
Risk-bear.assets (A-E)	13.376.110	100,0	1.294.757	13.286.676	100,0	1.370.669	13.517.944	100,0	1.504.174	99	102
Classified (B-E)	2.763.582	20,7	1.082.509	2.715.121	20,4	1.159.236	2.763.865	20,4	1.289.091	98	102
Non-performing (C-E)	1.344.552	10,1	963.662	1.487.820	11,2	1.050.923	1.669.504	12,4	1.195.544	111	112
Non-risk bear.assets[28]	5.787.457			5.579.911			6.144.833			96	110
TOTAL (risk and non-risk)	19.163.567			18.866.587			19.662.777			98	104

The first indicator and a warning sign of potential problems with loan repayment is the growth of past due receivables and their share in total loans. In 2013, past due receivables had a relatively high increase of 9% or KM 102 million (vs. 2012: 12% or KM 112 million) and their share rose by 0.7 percentage points, i.e. by 10.8%.

If we look into the quality of risk-bearing assets through trends and changes of key indicators, we can conclude that adverse trends from previous periods have continued in 2013 as well. This primarily refers to the increase of non-performing assets and impairment of its structure and migration of items to worse classification categories. Also, key indicators of assets quality have worsened compared to the YE2012. As for some banks, these indicators showed slight oscillations (upgrade or downgrade), i.e. there were eight banks with the ratio of classified assets and risk-bearing assets below the level of the overall banking sector, while six banks had the share of non-performing assets vs. risk-bearing assets below the level of the banking sector.

As of 31.12.13, classified assets amounted to KM 2.8 billion and non-performing assets stood at KM 1.7 billion.

Classified assets (B-E) went up by 2% or KM 49 million: category B is by 11% or KM 133 million lower and non-performing assets (C-E) rose by 12% or KM 182 million.

The ratio between classified assets and risk-bearing assets is 20.4%, which is equivalent to the one from YE2012.

The most significant indicator of assets quality is the ratio between non-performing assets and risk-bearing assets, which rose by 2.1 percentage points vs. YE2012 and now stands at 12.4% (whereas this increase in 2012 was 1.1 percentage points). The main reasons for this rests with the increase of non-performing assets by 12% or KM 182 million (vs. 2012: 11% or KM 143 million). However, this should not be taken lightly since the share of category B is 8.1% and since we doubt that a part of loans classified within this category are of poor quality and need to be classified as non-performing assets.

Sector-level data analysis is based on loan quality indicators for the two key sectors: corporate and retail. Two indicators for the said sectors show major deviation and point to higher exposure to credit risk, hence to potential loan losses regarding the corporate segment.

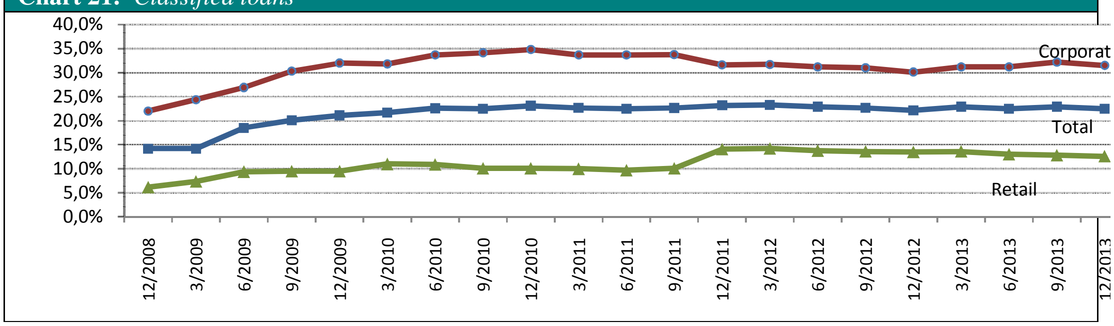
[28] In line with Article 2, Paragraph 2 of the Decision on Minimum Standards for Credit Risk Management and Assets Classification in Banks, not classified assets items and items for which no general loan loss provisions of 2% are being calculated (as per Article 22, Paragraph 8 of the same Decision).

Table 25: *Classification of corporate and retail loans*

Classification category	31.12.2012						31.12.2013						
	Retail	% share	Corporate	% share	TOTAL Amount	TOTAL Share	Retail	% share	Corporate	% share	TOTAL Amount	TOTAL Share	INDEX
1	2	3	4	5	6 (2+4)	7	8	9	10	11	12 (8+10)	13	14(12/6)
A	4.391.603	86,5	3.905.862	69,9	8.297.465	77,8	4.538.704	87,4	3.874.012	68,5	8.412.716	77,5	101
B	150.247	3,0	811.742	14,5	961.989	9,0	135.873	2,6	717.004	12,7	852.877	7,9	89
C	97.021	1,9	225.405	4,0	322.426	3,0	70.012	1,3	272.940	4,8	342.952	3,2	106
D	162.781	3,2	268.663	4,8	431.444	4,1	128.351	2,5	361.163	6,4	489.514	4,5	113
E	275.027	5,4	377.773	6,8	652.800	6,1	322.031	6,2	432.310	7,6	754.341	6,9	116
TOTAL	5.076.679	100,0	5.589.445	100,0	10.666.124	100,0	5.194.971	100,0	5.657.429	100,0	10.852.400	100,00	102
Class. loans-E	685.076	13,5	1.683.583	30,1	2.368.659	22,2	656.267	12,6	1.783.417	31,5	2.439.684	22,5	103
Non-perf. Loans C-E	534.829	10,5	871.841	15,6	1.406.670	13,2	520.394	10,0	1.066.413	18,8	1.586.807	14,6	113
		47,6		52,4		100,00		47,9		52,1		100,0	
Individual sector's share in classified loans, non-performing loans and category B:													
Categories B-E		28,9		71,1		100,0		26,9		73,1		100,0	
Non-performing C-E		38,0		62,0		100,0		32,8		67,2		100,0	
Category B		15,6		84,4		100,0		15,9		84,1		100,0	

Loan quality indicators worsened vs. YE2012, where the share of non-performing loans rose by 1.4 percentage points and stood at 14.6% as a result of growing total non-performing loans by 13% or KM 180 million (to include increase by 22.3% or KM 195 million for corporate loans, while retail non-performing loans dropped by 2.7% or KM 14 million. The share of classified loans rose to 22.5%, i.e. it rose by 0.3 percentage points.

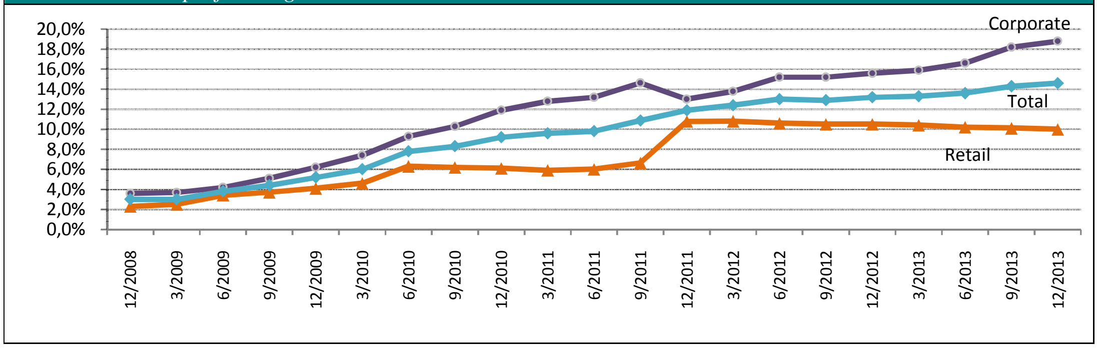
Chart 21: *Classified loans*



Out of the total loans approved to corporate customers of KM 5.7 billion as of 31.12.13, there was significantly high percentage of 31.5% or KM 1.8 billion of loans classified within categories B to E, which is an increase of 1.4 percentage points vs. YE2012 (in 2012, this share went down by 1.5 percentage points). Also, this indicator is much better for the retail segment. This is to say that out of the total approved retail loans of KM 5.2 billion, there was 12.6% or KM 656 million of loans classified in the said categories (vs. YE2012 when this share was 13.5% or YE2011 when it was KM 14.1%), but this is also high.

These trends result from the condition in the real sector and the economic crisis, due to which the corporate loan portfolio displays significantly lower quality than loans of the retail segment..

Chart 22: *Non-performing loans*



The most important indicator of the loan portfolio quality is the share of non-performing loans. Out of the total non-performing loans, corporate loans hold a share of 67% (vs. YE2012: 62%) and retail loans a share of 33% (vs. YE2012: 38%). In 2013, the share of non-performing loans of the corporate segment continued to grow (by 22.3%), while retail non-performing loans dropped their share. Out of the total corporate loans approved, non-performing loans take up a share of 18.8% or KM 1.1 billion, which is 3.2 percentage points more than at the end of 2012 (in 2012, this share rose by 2.6 percentage points). This increase rate in the retail segment equals 10% or KM 520 million, which is by 0.5 percentage points less than as of 31.12.12 (vs. YE2011: 10.8%).

More detailed and comprehensive analysis is based on information on loan concentrations by industry sectors for corporate segment (by sectors) and for retail segment (by purpose).

Table 26: *Concentration of loans by industry sectors*

DESCRIPTION	31.12.2012				31.12.2013				INDEX	
	Total loans		Non-performing loans		Total loans		Non-performing loans			
	Amount	% share	Amount	% share	Amount	% share	Amount	% share		
1	2	3	4	5 (4/2)	6	7	8	9 (8/6)	10 (6/2)	11(8/4)
1. Corporate loans for:										
Agriculture (AGR)	109.873	1,0	31.431	28,6	112.695	1,0	30.608	27,2	103	97
Production (IND)	1.537.147	14,4	244.138	15,9	1.547.431	14,3	333.666	21,6	101	137
Construction (CON)	408.753	3,8	106.553	26,1	394.706	3,6	121.971	30,9	97	114
Trade (TRD)	2.318.167	21,7	309.230	13,3	2.298.260	21,2	392.161	17,1	99	127
Catering (HTR)	166.485	1,6	23.453	14,1	162.102	1,5	29.970	18,5	97	128
Other[29]	1.049.020	9,8	157.036	15,0	1.142.235	10,5	158.037	13,8	109	101
TOTAL 1.	5.589.445	52,4	871.841	15,6	5.657.429	52,1	1.066.413	18,8	101	122
2. Retail loans for:										
General consumption	3.738.550	35,1	312.682	8,4	3.906.142	36,0	310.450	7,9	104	99
Housing	1.186.437	11,1	177.177	14,9	1.148.230	10,6	170.282	14,8	97	96
Business activities (small entrepreneurs)	151.692	1,4	44.970	29,6	140.599	1,3	39.662	28,2	93	88
TOTAL 2.	5.076.679	47,6	534.829	10,5	5.194.971	47,9	520.394	10,0	102	97
TOTAL (1. +2.)	**10.666.124**	**100,0**	**1.406.670**	**13,2**	**10.852.400**	**100,0**	**1.586.807**	**14,6**	**102**	**113**

The largest share among total corporate loans refers to the trade sector (21.2%) and the production sector (14.3%), while the retail segment is dominated by general consumption loans (36%) and housing loans (10.6%), wherein these shares are almost the same as the year before.

For an extensive period of time, negative and strong effect of the economic crisis is especially pronounced within several key sectors (as evident from the indicator of the share of non-performing

[29] This includes the following sectors: traffic, warehouse and communications (TRC); financial mediation (FIN); real estate, renting and business services (RER); public administration and defence, mandatory social insurance (GOV) and other.

loans). As of YE2012, the agriculture sector, although holding the lowest share among total loans of 1%, had the poorest indicator of 28.6%. However, at the end of 2013, the situation changed, so the highest share in non-performing loans of 30.9% was with the construction sector (in 2012, it rose by 5.9 percentage points and in 2013 by 4.8 percentage points), while its share in total loans stands at mere 3.6%. In 2013, this sector posted a rise of its non-performing loans of 14% or KM 15 million.

However, the focus is on the two sectors with the highest share in total loans – trade sector (21%) and production sector 14%). Based on the data analysis, we find that these two sectors are still exposed to the strong effect of the crisis and the quality of loans approved to these two sectors in continuously decreasing. In 2013, the trend of non-performing loan increase continued regarding the production sector (up by 37% or KM 90 million), i.e. their share rose from 15.9% to 21.6% (vs. 2012, when their increase was 22% or KM 45 million and their share rose by 3.1 percentage points and reached the level of 15.9%). As for the trade sector, non-performing loans also posted a high growth rate of 27% or KM 83 million and their share rose by 3.8 percentage points and arrived to 17.1% (vs. 2012 when their growth was 24% or KM 60 million and their share rose from 11.2% to 13.3%).

Also, the catering sector with the low share in loans of 1.5% underwent major impairment of their loans quality in 2013, meaning NPLs rose by 28% or KM 7 million, while their share increased from 14.1% to 18.5%.

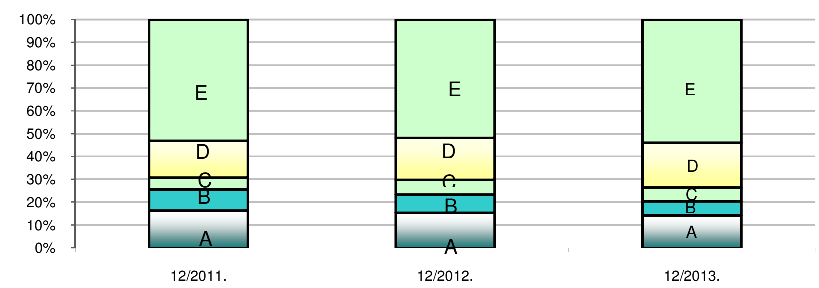
As opposed to the agriculture, the retail sector displays a positive trend, meaning it shows a slight improvement of its indicators, all as a result of reduced level of non-performing loans. The lowest indicator of the NPL share of 28.2% (vs. 29.6% in YE2012) refers to loans to small entrepreneurs whose share in total loans is quite low 1.3%. Relatively high share of NPLs of 14.8% refers to housing loans (which is almost the same as in 2012), while consumer loans have lower share of 7.9%, down by 0.5 percentage points vs. YE2012.

General credit risk level and estimated potential loan losses by classification categories, as determined in line with the criteria and methodology defined by the FBA decisions, plus their trend and structure at the banking sector level, is provided in the table and the chart below:

Table 27: *Structure and trend of general credit risk and potential loan losses*

Classification category	AMOUNT (in 000 KM) AND STRUCTURE (in%)						INDEX	
	31.12.2011		31.12.2012		31.12.2013			
1	2	3	4	5	6	7	8 (4/2)	9 (6/4)
A	209.555	29,2	211.433	15,4	215.083	14,3	100	102
B	132.048	18,4	108.313	7,9	93.547	6,2	91	86
C	113.962	15,9	87.874	6,4	90.541	6,0	129	103
D	258.297	36,0	252.970	18,5	295.224	19,6	120	117
E	3.851	0,5	710.079	51,8	809.779	53,9	104	114
TOTAL	717.713	100,0	1.370.669	100,0	1.504.174	100,0	106	110

Chart 23: *Structure and trend of general credit risk and potential loan losses*



Based on an analysis of the calculated LLP (in aggregate terms and by classification categories) vs. YE2012, reserves for general credit risk (category A) and potential loan losses went up by 10% or KM 134 million and stand at KM 1.5 billion. The reserves for general credit risk are 2% or KM 3.6 million higher and amount to KM 215 million, while for potential loan losses went up by 11% or KM 130 million. Reserves for the category B dropped by 14% or KM 15 million (they are 2x lower as of the last quarter alone) due to its reduction by 11% or KM 133 million and now stand at KM 94 million. Prompted by the increase of non-performing assets (categories C, D and E) by 12% or KM 182 million, relevant reserves also rose by 14% or KM 145 million, i.e. they reached the level of KM 1.2 billion. The largest relative growth of 17% or KM 42 million refers to reserves for the category D, while the highest nominal growth is with the category E of 4% or KM 3.5 million (due to the transfer of loans to worse classification categories D and E). In the last quarter 2013, they rose by KM 6.2 million (transfer from category B to category C), hence the growth rate for the entire 2013 is 3% or KM 2.7 million. This trend of loan loss provisions indicates to a constant worsening of the loan portfolio, as stemming from further effect of the economic crisis on the real sector.

One of key indicators of assets quality is a ratio between potential loan losses (PLL) and risk-bearing assets with off-balance sheet items. This ratio stands at 9.5% and is higher by 0.8 percentage points than in the end of 2012.
As of 31.12.13, banks had an average calculated reserves for the category B of 8.5%, for the category C of 25.4%, for the category D 58.7% and for the category E 100% (vs. YE2012: 8.8% for B, 26.3% for C, 57% for D and 100% for E).[30]

In accordance with the IAS/IFRS, banks are required to book assets depreciation through expenses by forming value adjustments for balance sheet items and provisions for risk-bearing off-balance sheet items (previously called costs of loan loss provisions).

An overview of total assets items (balance sheet and off-balance sheet) and default items, as well as related value adjustments and provisions (defined in line with banks' internal methodology whose minimum contents are regulated by the FBA decisions) at the banking sector level is provided in the following table.

[30] According to the Decision on Minimum Standards for Credit Risk Management and Assets Classification in Banks, banks are required to calculate loan loss provisions by classification categories bearing the following percentages: A-2%, B 5-15%, C 16-40%, D 41-60% and E 100%.

Table 28: *Assessment and valuation of risk-bearing items according to IAS 39 and IAS 37*

Description	AMOUNT (in 000 KM) AND SHARE (in %)				INDEX
	31.12.2012.		31.12.2013.		
	Amount	Share	Amount	Share	
1	2	3	4	5	6 (4/2)
1. RISK-BEARING ASSETS (a+b)	**13.286.676**	**100,0%**	**13.517.944**	**100,0%**	102
a) Default items	**1.729.182**	13,0%	**1.886.251**	14,0%	109
a.1. on balance default items	1.708.152		1.863.530		109
a.2. off-balance default items	21.030		22.721		108
b) Performing assets	**11.557.494**	87,0%	**11.631.693**	86,0%	101
1.1 TOTAL VALUE ADJUSTMENTS FOR RISK-BEARING ASSETS (a+b)	**1.092.535 100,0%**	**100,0%**	**1.252.464**	**100,0%**	115
a) Value adjustments for default	**953.904**	87,3%	**1.109.531**	88,6%	116
a.1. Value adjustments for BS items in default	950.344		1.104.215		116
a.2. Reserves for off-BS items in default	3.560		5.316		149
b) Value adjustments for performing assets (IBNR[31])	138.631	12,7%	142.933	11,5%	103
2. TOTAL LOANS (a+b)	**10.666.124**	**100,0%**	**10.852.400**	**100,0%**	102
a) Defaulted loans (non-performing loans)	1.645.072	15,4%	1.799.777	16,6%	109
b) Performing loans	9.021.052	84,6%	9.052.623	83,4%	100
2.1. VALUE ADJUSTMENTS FOR LOANS (a+b)	**1.007.459**	**100,0%**	**1.163.530**	**100,0%**	115
a) Value adjustments for defaulted loans	898.737	89,2%	1.052.412	90,4%	117
b) Value adjustments for performing loans (IBNR loans)	108.722	10,8%	111.118	9,6%	102
Coverage rate of default items	**55,2%**		**58,8%**		
Coverage rate of performing assets	**1,2%**		**1,2%**		
Coverage rate of risk bearing assets with total value adjustments	**8,2%**		**9,3%**		

In 2013, default loans rose by 9% or KM 155 million. For comparison purposes, non-performing loans grew by 12.8% or KM 180 million. The share of defaulted loans in total loans increased by 1.2 percentage points and stands at 16.6% and the share of non-performing loans stands at 14.6%. The share of all default items in total risk-bearing assets is 14%, which is 1 percentage point higher than at the end of 2012.

Coverage rate of default items with value adjustments rose from 55.2% to 58.8% due to high increase of value adjustments by 16% or KM 156 million (the increase rate has doubled in the last quarter), while the coverage rate of nonperforming assets with provisions for loan losses for this asset type has only slightly risen from 70.6% to 71.6%. The coverage rate of performing assets remained at the same level of 1.2% and the coverage rate of risk-bearing assets with total value adjustments equals 9.3%, up by 1 percentage point vs. YE2012. The coverage ratio of risk-bearing assets with total calculated regulatory reserves for loan losses (for general credit risk and special reserves for loan losses) has improved and amounts to 11.1% (vs. 12/12: 10.3%).

The increase trend among uncollectable receivables, i.e. posting of customer defaults in settlement of past due loan obligations has caused activation of guarantees with certain number of defaulted loans (having this form of security), so the loan repayment went against guarantors. As of 31.12.09, FBA has defined a report on repayment of loans by guarantors in order to collect, monitor and analyse information on loans repaid by guarantors. According to the reports filed by banks in the FB&H as of 31.12.13, there was a total of 2,032 guarantors that repaid KM 12 million of total loans approved of KM 66 million (1,785 loan accounts), which is 1% more than as of 31.12.12 (KM 12 million repaid by 2,823 guarantors, while the amount of approved loans was KM 70 million and encompassed 2,479 loan accounts). The remaining debt amounts to KM 43 million (31.12.12: KM 41 million).

[31] IBNR (identified but not reported)-latent losses.

Based on mentioned information, we find that loan amount repaid by guarantors has dropped in 2013, while the balance of remaining debt and the amount of repayments by guarantors rose. The share of loans and number of loan accounts being repaid by guarantors vs. information at the overall system level is low and stand at mere 0.40% and 0.15%.

For purpose of mitigating adverse effects of the global financial and economic crisis and considering preservation of the banking sector's stability, in late 2009, FBA has adopted the Decision on Temporary Measures for Rescheduling of Credit Liabilities of Legal Entities and Private Individuals in Banks[32].

The primary objective of these temporary measures is to encourage banks to "boost" lending activities and restructure existing receivables without having to increase prices on loans and raise costs for existing debtors, as well as to help private individuals and legal entities to overcome the situation they have come to due to the economic crisis (lower payment capacity of private individuals due to loss of a job, late salaries, salary reductions, etc. and, with regards to legal entities - higher illiquidity, major reduction of business volume, very difficult condition in the real sector in general, etc.).

Acting upon the said Decision, in 2013, FB&H banks have received a total of 599 requests for loan restructuring and approved 571 requests in a total amount of KM 76 million or 95%, which is by 4% higher than in 2012. Out of the total amount of approved restructured liabilities, KM 74 million refers to legal entities and KM 2 million to private individuals.

The net effect of loan loss provisions based on performed restructurings is an increase of KM 279 ths. Of note, there were also contrary trends in sense that there were both, increases and decreases if loan loss provisions on this basis, which finally resulted in the said net effect.

According to the said FBA Decision, restructured loans represented only 0.7% of total loans as of 31.12.13 (i.e. corporate restructured loans represented 1.3% of total corporate loans and retail restructured loans represented 0.04% of total retail loans).

Based on such information, we find that the result of restructured loans is relatively modest considering both, their number and amount, and even if compared against total loan portfolio and sector-level portfolio (for corporate and private individuals).

Although results and effects of the Decision are not that significant, we find that enactment of such a regulation was particularly important, meaning these temporary measures were truly necessary under conditions of the financial and economic crisis and their effects on the real sector in the FB&H and had positive effects for debtors (corporate and retail alike) by facilitating debt servicing in line with their payment capacities. Therefore, validity prolongation of the said Decision to 2014 was justified, especially due to the fact that the crisis effects are still evident.

An analysis of the assets quality, i.e. quality of the loan portfolio of individual banks, as well as on-site examinations in banks, have led to a conclusion that the credit risk is dominant risk with most of banks and another concerning fact is that some banks have inadequate practices for managing, i.e. assessing, measuring, monitoring and controlling credit risks and for classifying assets, which our on-site examiners determined on basis of major amounts related to shortfall of loan loss reserves (which was later on adequately formed as per FBA orders). Also, our analysis of the assets quality in banks grouped according to the ownership structure revealed that relevant ratios of banks in majority ownership of residents (6 local private banks) wore worse than those in banks under majority foreign ownership (10 banks). Moreover, the significant increase of non-performing loans in local banks equaled 76.2% in 2012 and 45% in 2013, while this increase with foreign-owned banks was 7.6% in 2012 and 9% in 2013. This is a result of inadequate and weak systems for credit risk management, especially in relation to the key stage of the process – at the time of loan approval. Major weaknesses and inefficient practices were also identified within the preventive actions stage, i.e. within the early

[32] FB&H Official Gazette Nos. 2/10, 1/12, 111/12 and 1/14.

recognition of problems with non-performing assets whose objective was to reduce such assets through collection or sound restructuring.
.
With regards to banks where the FBA identified (through bank examinations) low level of assets quality and poor practices of credit risk management and/or where banks displayed adverse trends, meaning reduction of assets quality, such banks were ordered to apply corrective actions in sense of preparation of an operational program for management of non-performing assets to contain an action plan for improvement of existing practices of credit risk management, i.e. assets quality management, for reducing existing concentrations and for solving problems with non-performing assets and preventing their further impairment. Fulfillment of FBA orders is being continuously controlled through intensified follow-up process based on reports and other documentation delivered by banks, as well as through target on-site examinations. Supervision of this segment of operations has been intensified due to evident negative trends significantly affecting and causing deterioration of banks' profitability and weakening of capital base of certain banks, due to which banks need to take timely measures to obtain capital from external sources.

Transactions with Related Entities

In their operations, banks are exposed to different risks, of which special relevance is seen with the risk of transactions with their related entities.

In accordance with the Basel Committee standards, FBA has established prudential principles and requirements for bank transactions with related entities, as regulated by its Decision on Minimum Standards for Banks' Operations with Related Entities defining conditions and manner of banks' operations with related parties. Based on this Decision and the Law on Banks, a bank's supervisory board (acting upon the CEO proposal) is required to adopt special policies for operations with related entities and to ensure their implementation.

The FBA Decision also prescribes a special set of reports on transactions with one part of related entities, encompassing therein loans and contingent and assumed off-balance sheet liabilities (guarantees, letters of credit, assumed loan obligations) as the most frequent and most risky form of transactions between banks and their related entities.

The regulated set of reports includes information on loans extended to the following types of related entities:
- Bank shareholders with over 5% of voting rights,
- Members of the bank's supervisory board and management board, and
- Subsidiaries and other companies related to the bank.

-000 KM-

Table 29: *Transactions with related entities*					
Description	**LOANS APPROVED[33]**			**INDEX**	
	31.12.2011	**31.12.2012**	**31.12.2013**	**3/2**	**4/3**
1	2	3	4	5	6
To shareholders with over 5% voting rights, subsidiaries and other related entities	131.962	156.861	123.889	119	79
Members of supervisory board and audit board	400	617	570	154	92
Management board of the bank	2.170	2.574	2.507	119	97
TOTAL	134.532	160.052	126.966	119	79
Contingent and assumed off-bal.sheet liabilities	29.818	21.800	16.046	73	74

During the observed period, loan exposures to related entities were reduced by 21%, while contingent off-balance sheet liabilities dropped by 26% due to reduced exposure related to one large bank. Based on presented information, we find that the volume of loans and guarantees with related entities is still low, as is also the level of inherent risk. FBA pays special attention (during its on-site examinations) to banks' operations with related entities, especially in terms if assessing their system of identification and monitoring of risk in transactions with related entities. FBA examiners give on-site orders for elimination of identified omissions within certain deadlines and also initiate violation proceedings, their integral part being monitoring and overseeing implementation of issued orders within the follow up examinations. This has positively reflected upon this segment of their operations since banks have significantly improved the quality of their risk management in this segment.

2.2. Profitability

According to information from financial statements showing business results of banks, i.e. based on the Y2013 income statement, negative financial result – loss of KM 228 ths was posted at the level of the banking system in the FB&H, while Y2012 saw a profit of KM 110 million at the same level. The main reason for this poor financial result rests with high loss figure of two banks of altogether KM 135 million, which is KM 120 million more than the Y2012. Still, it should be noted that this primarily refers to an enormous loss by one bank (KM 116 million), that is by KM 105 million higher than in 2012. Also, the negative effect of app. KM 5 million refers to a loss by one small bank that posted minimal profit in Y2012, as well as almost identical amount of lower profit posted by four banks. On the other hand, the largest positive effect of app. KM 17 million is based on higher profit posted by nine banks. Looking into individual banks and their data by quarters in the Y2013, we noted positive trend in 1H 2013 in sense of profit recognized by most banks, while the 2H 2013 (especially last quarter of 2013) this profit is much lower, particularly related to large banks, along with major increase of losses with banks that posted negative financial result.

Key effect on improved profitability of most banks refers to results of applied new methodological approach (implementation of IAS 37/39 starting from 31.12.11), which led to smaller level of value adjustment costs. However, as opposed to Y2012 when the total income decrease (4% or KM 39 million) was amortised by more extensive decrease of non-interest bearing expenses (9% or KM 69 million, of which value adjustment costs went down by 24% or KM 46 million), in 2013 this total income drop has stopped, i.e. a slight increase was posted (1% or KM 10 million), while further deterioration of the loan portfolio quality caused high growth of non-interest bearing expenses of 17% or KM 120 million (noting therein that value adjustments among these costs rose by 59% or KM 85 million). It should also be noted that these are largely (app. 80% of total increase of value adjustment

[33] In addition to loans, this includes other receivables, deposits and facilities to shareholders (financial institutions) with over 5% of voting rights.

costs) related to just one bank, thus affecting the negative financial result at the banking system level.

Positive financial result of KM 140 million was posted by 14 banks and it is by 9% or KM 12 million higher than in 2012. At the same time, operating loss of KM 140 million was seen with regards to three banks and is eight times higher or KM 123 million higher than in 2012, all as a result of negative effect the credit risk and trends related to assets quality.

Relevant details are provided in the table below.

-000 KM-

Table 30: *Achieved financial result: profit/loss*

Description	31.12.2011		31.12.2012		31.12.2013	
	Amount	Number of banks	Amount	Number of banks	Amount	Number of banks
1	2	3	4	5	6	7
Loss	-45.512	3	-17.817	4	-140.330	3
Profit	126.754	16	128.173	14	140.102	14
Total	**81.242**	**19**	**110.356**	**18**	**-228**	**17**

As in other segments, this segment also shows some concentrations: out of the total profit (KM 140 million), 70% or KM 98 million refers to two largest banks in the system with assets share in the banking sector of 49%, while out of the total loss of KM 140 million, 83% or KM 116 million refers to just one bank with somewhat higher assets share in the system. Analytical data indicate that a total of ten banks have better financial result (by KM 19 million), while seven banks have poor financial result (by KM 131 million).

Based on analytical data, as well as indicators for assessment of the profitability quality (i.e. level of achieved financial result – profit/loss and ratios used in evaluating profitability, productivity and efficiency of operations, as well as other parameters related to business result assessment), it is evident that total profitability of the system has worsened in relation to the previous year, solely as a result of an enormous loss posted by one bank. Higher profitability, especially in relation to the largest banks achieving higher profit than the year before, is chiefly the result of implementation of a new methodological approach for measuring value impairment of financial assets. However, a profitability assessment that is based solely on achieved financial result would not be an adequate assessment since one should consider other important factors to sustainability and quality of earnings, i.e. profit. Here, an outmost importance rests on the credit risk and negative trends within assets quality over the past five years, as evident from growth of non-performing and uncollectable loans that is not co-related with the level of value adjustment costs (subsequent to implementation of IAS 39 and 37), being the most important factor to improvement of the financial result in most banks in the past three years. This leads to a conclusion, as well as doubt, that value adjustments with some banks are underestimated and not at an adequate level, although banking system displayed significant increase of value adjustment costs in the 2H of 2013, especially in 4Q 2013. We should once again emphasise that this mostly relates to just one bank.

As already mentioned, after the decrease of 4% or KM 39 million in 2012, total income in 2013 had a minimal growth of 1% or KM 10 million, i.e. total income at the system level amounted KM 859 million. Total non-interest bearing expenses amounted to KM 841 million, with a growth rate of even 17% or KM 120 million (vs. 2012: down by 9% or KM 69 million), which has adversely reflected upon the overall financial result of the banking sector.

Despite the increase of average interest-bearing loans with most of banks by 1.4%, a slight decrease of loan interest and growth of non-performing loans resulted in further reduction of interest-bearing income and lower average interest rates on loans from 6.90% to 6.56%. Although some banks posted higher interest income vs. the previous year (as a result of intensified lending activities), lower interest income of large banks (that are mostly leaders in the profitability segment) has caused the reduction at the system level. Interest income amounted to KM 781 million, down by 4% or KM 28 million than in the Y2012, also leading to its lower share in the structure of total income from 95.4% to 91%. Still, we find that the negative trend was mitigated since the interest income decrease in 2012 was at 7% or KM 57 million. The largest share among interest income refers to loan interest income that also posted the biggest nominal drop of 4% or KM 26 million and reduced share in total income from 86% to 81.9%. The structure of loan interest income is mostly (56%) consisting of interest income based on retail loans that went down by 1.4% against the year and their share in total loan portfolio was at 47.9%. They are followed by interest income based on corporate loans with the share of 41%, thus being down by 6% vs. the year before and the share of 47.9% in the total loan portfolio. Based on the just said, we find that the retail loan portfolio is still more profitable for banks and bears lesser risk considering the level of non-performing loans in the loan structure, as well as due to higher interest rates on retail loans that were by app. 30% higher than the interest rates of the corporate segment in 2013.

As in previous four years, positive trends were evident with regards to interest expenses as their rate of decrease was higher (-11%), but the nominal difference is not too high: interest expenses dropped by KM 30 million and interest income by KM 28 million. Interest expenses amount to KM 239 million, and their share in total income went down from 31.8% to 27.9%. Average interest-bearing deposits decreased by 3.5% and interest expenses related to deposit accounts amount to KM 205 million and is the biggest item in both, relative and nominal terms, in total interest expenses. This item went down by 6% or KM 13 million, thus resulting in a slight reduction of average interest rates on deposits vs. the comparable period from 2.32% to 2.26%. Although interest expenses on loans and other borrowings, as the second largest item among interest expenses with an amount of KM 21 million, holds a low share, its decrease rate was significant as it dropped from 42% or KM 15 million. This is seen as significant positive effect than the reduction of interest expenses on deposits.

As a result of decrease of both, interest income (-4%) and interest expenses (-11%), net interest income maintained nearly the same level (up by KM 2 million) and stands at KM 542 million, but with lower share in the total income structure from 63.6% to 63.1%.

Operating income amounts KM 317 million and went up by slight 3% or KM 8 million vs. the Y2012 and their share in total income rose from 36.4% to 36.9%. Within operating income, the largest share refers to service fees going up by 5% or KM 10 million.

After two years of a downward trend (2011: down by 17% or KM 163 million; 2012: 9% or KM 69 million), total non-interest bearing expenses amounted to KM 841 million in 2013 and had a growth rate of 17% or KM 120 million, plus their share in total income went from 85% to 98%, which is mainly a result of higher value adjustment costs. The value adjustment costs also dropped significantly over the past two years. In 2011, upon implementation of the new methodological approach, i.e. IAS 37/39, the decrease was 51% or KM 196 million and in 2012, they went further down by 24% or KM 46 million. In 2013, value adjustment costs amounted KM 230 million and had significant growth rate of 59% or KM 85 million, thus negatively reflecting upon the increase of their share in total income from 17.1% to 26.8%.

On the other hand, operating expenses of KM 536 million and the share of 62.3% in total income also posted a rise of 7% or KM 35 million (2012: down by 4% or KM 23 million). Thereof, costs of salaries and contributions, as the largest item among operating expenses, rose by slight 1% or KM 3 million and stand at KM 246 million, thus representing 28.7% of total income. Costs of fixed assets, after their increase by 6% or KM 10 million, amount to KM 169 million and represent 19.7% of total income, while other operating expenses rose by 23% or KM 22 million, as largely a result of costs of reserves for court disputes related to one bank. After the crisis emerged, banks took numerous measures to rationalise costs of operations, primarily to reduce operating and interest expenses, as has partly mitigated adverse effect of the interest income decrease caused by lower volume of lending activity and decrease of loan portfolio quality.

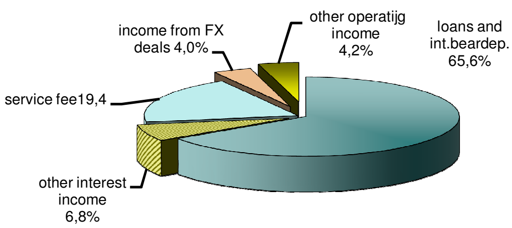
Trend and structure of total income and total expenses is provided in tables and charts below.

- in 000 KM-

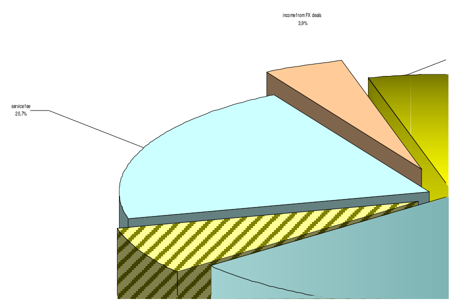
Table 31: *Structure of total income*

Structure of total income	31.12.2011. Amount	%	31.12.2012. Amount	%	31.12.2013. Amount	%	INDEX 8 (4/2)	9 (6/4)
1	2	3	4	5	6	7	8 (4/2)	9 (6/4)
I Interest and similar income								
Interest-bear.deposit accts. with dep.inst.	23.545	2,0	3.991	0,4	2.461	0,2	17	62
Loans and leasing facilities	769.774	65,1	729.602	65,2	703.462	64,1	95	96
Other interest income	73.365	6,2	75.831	6,8	75.122	6,8	103	99
TOTAL	866.684	73,3	809.424	72,4	781.045	71,1	93	96
II Operating income								
Service fees	210.795	17,8	216.711	19,4	227.150	20,7	103	105
Income from FX deals	48.198	4,1	45.081	4,0	42.695	3,9	94	95
Other operating income	56.049	4,8	47.181	4,2	47.377	4,3	84	100
TOTAL	315.042	26,7	308.973	27,6	317.222	28,9	98	103
TOTAL INCOME (I + II)	1.181.726	100,0	1.118.397	100,0	1.098.267	100,0	95	98

Chart 24: *Structure of total income*



31.12.2012.

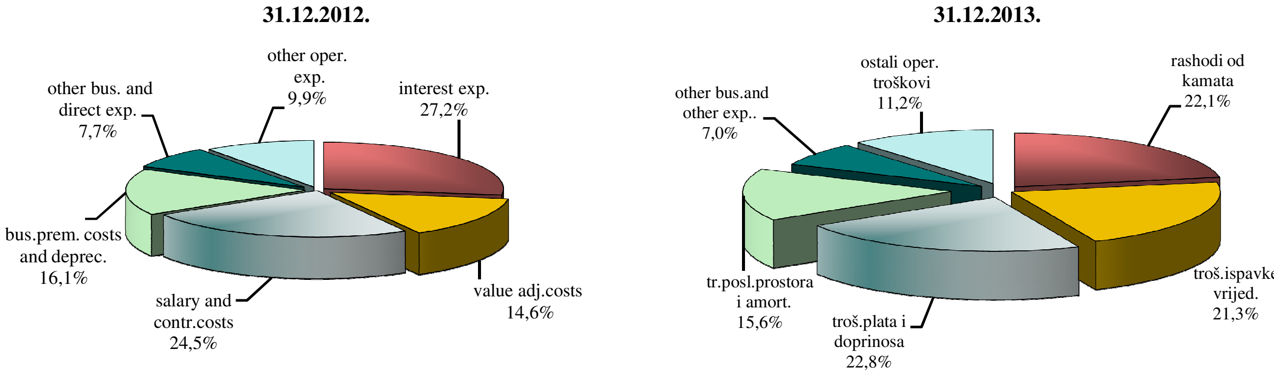


31.12.2013.

Table 32: *Structure of total expenses*

Structure of total expenses	31.12.2011 Amount	%	31.12.2012 Amount	%	31.12.2013 Amount	%	INDEX 8 (4/2)/	9 (6/4)
1	2	3	4	5	6	7	8 (4/2)/	9 (6/4)
I Interest and similar expenses								
Deposits	230.224	21,2	218.614	22,0	205.187	19,0	95	94
Liabilities under loans and other borrowings	47.831	4,4	36.520	3,7	21.253	2,0	76	58
Other interest expenses	16.502	1,5	14.635	1,5	12.862	1,1	89	88
TOTAL	294.557	27,1	269.769	27,2	239.302	22,1	92	89
II Total non-interest bearing expenses								
Costs of value adjustment of risk.bear.assets and Provisions for conting.liab. and other value adjustments	190.499	17,6	144.750	14,6	230.103	21,3	76	159
Costs of salaries and contributions	250.783	23,1	243.133	24,5	246.087	22,8	97	101
Costs of bus.premises and depreciation	166.075	15,3	158.933	16,1	168.794	15,6	96	106
Other business and direct expenses	76.209	7,0	76.181	7,7	75.621	7,0	100	99
Other operating expenses	106.998	9,9	98.441	9,9	120.634	11,2	92	123
TOTAL	790.564	72,9	721.438	72,8	841.239	77,9	91	117
TOTAL EXPENSES (I + II)	1.085.121	100,0	991.207	100,0	1.080.541	100,0	91	109

Chart 25: *Structure of total expenses*



The table below provides an overview of key ratios relative to assessment of profitability, productivity and efficiency of banks.

- in %-

Table 33: *Ratios of profitability, productivity and efficiency by periods*

RATIOS	31.12.2011	31.12.2012	31.12.2013
Profit vs. average assets	0,5	0,7	n/a
Profit vs. average equity	4,6	5,1	n/a
Profit vs. average shareholders capital	6,9	9,3	n/a
Net interest income / average assets	3,8	3,6	3,6
Fee income/ average assets	2,1	2,1	2,1
Total income/ average assets	5,9	5,7	5,7
Business and direct expenses[34]/average assets	1,8	1,5	2,0
Operating expenses/ average assets	3,5	3,4	3,6
Total non-interest bear.expenses/ average assets	5,2	4,8	5,6

The loss figure posted at the level of the banking system resulted also in the negative key ratios of profitability: ROAA (return on average assets) and ROAE (return on average equity).

Banks' productivity indicator, measured as a ratio between total income and average assets (5.7%), maintained the same level as a result of higher total income by 1% (based on increase of fee income by 5%), along with a simultaneous increase of average assets by 1%. Higher costs of value adjustments also resulted in impaired ratio of business and direct expenses vs. average assets, i.e. it worsened from 1.5% to 2.0%.

Under negative conditions of banks' operations and prompted by effects of the economic and financial crisis on the FB&H banking sector, profitability of banks will continue to be mostly affected by and will depend on two key factors: a) further trend of the assets quality, i.e. level of loan losses and credit risk, and b) efficiency of management and control over operating income and operating expenses. On the other hand, evident slowdown and downward trend of economic activities caused lower demand for loans and more restrictive approach on the supply side (banks). This will directly reflect upon profitability of the entire banking sector in the period ahead. Also, profit of banks, i.e. their financial result, will be largely affected by the price and interest rate risk in terms of both, sources of financing and interest margin sufficient enough to cover for all non-interest bearing expenses and thus finally ensure satisfactory profit related to capital invested by bank owners. Therefore, a key factor to efficiency and profitability of every bank is the quality of management and business policies since this directly reflects upon its performances.

[34] Expenses also include value adjustment costs.

2.3. Weighted Nominal and Effective Interest Rates

For purpose of greater transparency and easier comparability of banks' loan approval terms and deposit taking terms, as well as for purpose of customer protection by means of introducing transparent disclosure of loan approval costs, i.e. income earned of deposits, all in line with international standards, criteria and practices of other countries, on 01.07.07, FBA has prescribed a unified manner of calculation and disclosure of effective interest rate[35] for all banks seated in the Federation of B&H. Effective interest rate represents an actual relative loan price, i.e. income earned on a deposit, expressed as an annual percentage.

Effective interest rate is a decursive interest rate calculated on an annual level by applying complex interest calculation in a manner where discounted cash receipts are brought to an equivalent level with discounted cash expenditures related to the approved loan, i.e. related to the received deposit (breakeven point).

Banks are required to report to the FBA on a monthly level regarding weighted nominal and effective interest rates on loans and deposits approved/received within particular reporting month, all in line with regulated methodology[36].

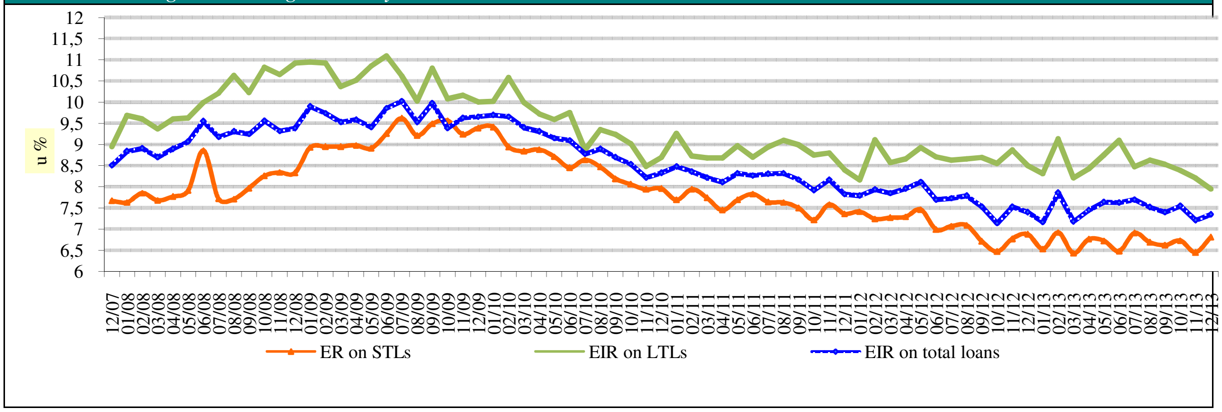
The table below shows an overview of weighted nominal and effective interest rates (hereinafter: NIR and EIR) for loans at the banking sector level and for two key customer sectors (corporate and retail) for December 2011, June and December 2012 and June and December 2013.

Table 34 : *Weighted average NIR and EIR for loans*

DESCRIPTION	12/2011		6/2012		12/2012		6/2013		12/2013	
	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR
1	2	3	4	5	6	7	8	9	10	11
1. Weighted IR on ST loans:	6,78	7,36	6,31	6,99	6,39	6,88	6,04	6,48	6,18	6,81
1.1. Corporate	6,74	7,28	6,29	6,93	6,39	6,86	6,09	6,47	6,21	6,79
1.2. Retail	8,66	11,89	7,73	10,88	8,46	10,89	7,92	10,91	6,42	8,51
2. Weighted IR on LT loans:	7,57	8,40	7,71	8,71	7,66	8,50	8,07	9,10	7,31	7,95
2.1. Corporate	6,96	7,59	6,82	7,41	6,73	7,22	6,94	7,40	6,83	7,17
2.2. Retail	8,25	9,31	8,39	9,54	8,47	9,59	8,52	9,79	7,93	8,95
3. Total weighted IR on loans:	7,14	7,83	6,91	7,70	6,80	7,40	6,93	7,63	6,72	7,35
3.1. Corporate	6,81	7,38	6,41	7,03	6,45	6,93	6,26	6,66	6,41	6,92
3.2. Retail	8,27	9,44	8,36	9,61	8,47	9,69	8,49	9,83	7,84	8,92

[35] Decision on Uniform Method of Calculation and Disclosure of Effective Interest Rate on Loans and Deposits (Official Gazette of FB&H No. 27/07).
[36] Instructions for Implementation of the Decision on Uniform Method of Calculation and Disclosure of Effective Interest Rate on Loans and Deposits and Instructions for Calculation of Weighted and Effective Interest Rate.

Chart 26: *Weighted average monthly EIR on loans*



During an analysis of interest rate trends it is important to monitor trends of the weighted EIR, wherein the difference between this interest rate and NIR represents a fee and commission paid to the bank for an approved loan (and this is factored in the loan price calculation). This is why EIR represents an actual price of a loan.

During 2012, there was an evident trend of moderate decrease of weighted EIR as a result of implementation of a business policy of lower interest rates by some banks, due to pronounced competition in the FB&H banking market, as well as due to low demand for loans and related restrictive lending policy of banks in the process of analyzing credit standing of potential borrowers.

This trend of slight decrease of weighted EIR on loans continued in 2013 as well.

In December 2012, weighted EIR stood at 7.40% and in December 2013 at 7.35%, while the lowest rate (7.17%) was in January 2013.

During 2013, weighted interest rates on short term loans posted minor oscillations within 0.48 percentage points, while interest rates on long term loans were within 1.18 percentage points.

In December 2013, weighted EIR on short term loans was 6.81%, down by 0.07 percentage points than in December 2012.

In December 2013, weighted EIR on long term loans was 7.95%, down by 0.55 percentage points than in December 2012.

In 2012, interest rates on loans approved to two key customer segments: corporate and retail[37] took two contrary directions, meaning interest rates on corporate loans were on a slight decrease and interest rates on retail loans were on the slight rise. During 2013, weighted EIR of corporate loans, despite present oscillations within 0.78 percentage points, was still lower than EIR on retail loans and in December 2013 this rate was at the same level of 6.92% as in December 2012. EIR on long term corporate loans in December 2013 was slightly lower than in December 2012 and stood at 7.17% (12/2012: 7.22%), which is also the case with EIR on short term loans (12/2012: 6.86%; 12/2013: 6.79).

In 2013, EIR on retail loans ranged from 8.92% to 9.83%. In December 2013, this rate was 8.92%, down by 0.77 percentage points than in December 2012.

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[37] According to the industry sector classifications, small entrepreneurs belong to the retail segment.

Also, over the period of the past five years, there is an evident moderate, but continuous decrease of weighted average EIR on loans (calculated on an annual level), primarily related to the corporate segment. However, continuous decrease of EIR in the retail segment was stopped in 2013, which is when interest rates had slightly higher values (as evident from the table below).

Table 35 : *Weighted average NIR and EIR on loans on annual level*

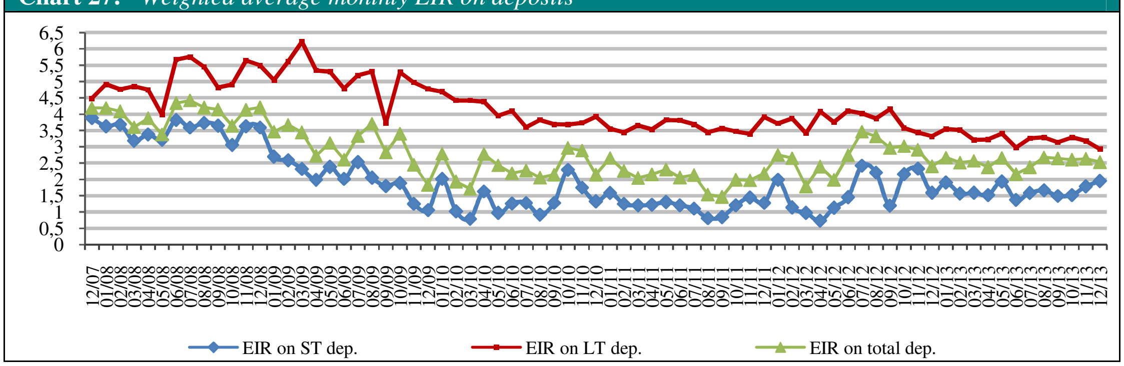
DESCRIPTION	2009		2010		2011		2012		2013	
	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR
1	2	3	4	5	6	7	8	9	10	11
1. Weighted IR on ST loans:	8,52	9,21	7,94	8,49	7,04	7,61	6,61	7,19	6,17	6,66
1.1. Corporate	8,52	9,11	7,92	8,35	6,97	7,45	6,42	6,93	6,22	6,66
1.2. Retail	10,00	13,15	9,07	12,79	9,08	12,41	8,40	11,50	8,09	11,08
2. Weighted IR on LT loans:	9,51	10,55	8,46	9,35	7,97	8,84	7,82	8,74	7,66	8,48
2.1. Corporate	8,29	9,17	7,90	8,35	7,39	7,89	6,98	7,65	6,64	7,12
2.2. Retail	10,68	11,97	9,12	10,48	8,45	9,62	8,44	8,73	8,35	9,40
3. Total weighted IR on loans:	8,90	9,73	8,20	8,92	7,49	8,21	7,11	7,83	6,82	7,46
3.1.Corporate	8,46	9,12	7,92	8,35	7,09	7,58	6,55	7,10	6,33	6,78
3.2. Retail	10,62	12,06	9,11	10,60	8,49	9,77	8,43	8,88	8,33	9,48

Weighted NIR and EIR on term deposits (calculated on basis of monthly reports) at the banking sector level are provided in the following table.

Table 36 : *Weighted average NIR and EIR on deposits*

DESCRIPTION	12/2011		06/2012		12/2012		6/2013		12/2013	
	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR
1	2	3	4	5	6	7	8	9	10	11
1. Weighted IR on ST deposits:	1,28	1,28	1,44	1,45	1,59	1,59	1,35	1,37	1,94	1,95
1.1. up to three months	0,91	0,91	0,48	0,48	1,28	1,28	1,01	1,01	1,92	1,92
1.2. up to one year	2,74	2,74	3,15	3,18	2,53	2,55	1,80	1,86	1,99	2,01
2. Weighted IR on LT deposits:	3,88	3,91	4,07	4,10	3,3	3,32	2,95	2,97	2,89	2,92
2.1. up to three years	3,73	3,75	4,01	4,03	3,17	3,19	2,64	2,66	2,58	2,61
2.2. over three years	4,56	4,61	4,57	4,76	4,42	4,46	4,32	4,33	4,24	4,28
3. Total weighted IR on deposits	2,17	2,18	2,72	2,74	2,39	2,40	2,14	2,16	2,50	2,53

Chart 27: *Weighted average monthly EIR on deposits*



As opposed to loans, where actual price is affected by costs related to approval and servicing of loans (on condition such costs are known at the time of approval), deposits almost show no difference between the nominal and effective interest rate.

Compared to December 2012, weighted EIR on total term deposits rose by 0.13 percentage points in December 2013 (i.e. from 2.40% to 2.53%). Weighted EIR on short term deposits in 2013 was within 0.58 percentage points, wherein the largest rate was seen in December of 1.95% and the lowest in June of 1.37%.

Looking into interest rates trends regarding short term deposits by their maturity periods, EIR on term deposits up to three months rose by 0.64 percentage points vs. its level in December 2012 and stands at 1.92%. The decrease is evident with regards to loans on deposits with a term of up to one year, that amounted to 2.91% in December 2013, which are 0.54 percentage points less than in December 2012. Short term deposits are mostly considered to be unstable sources of financing due to the nature of their maturity. As such, they are subject to high oscillations, even within a one year period due to banks' efforts to manage their assets and liabilities, i.e. their sources of financing, as efficiently as possible. One of their instruments used herein is the interest rate policy.

Weighted EIR on long term deposits in December 2013 stood at 2.92% (12/2012: 3.32%), which is also the lowest rate during 2013, while the largest rate was identified in January of 3.54%. If observed across several past periods, weighted EIR on long term deposits, except for sporadic and minor oscillations, was solely within the range of 3% and 4%.

Weighted EIR on long term deposits up to three years was 2.61%, thus representing a decrease of 0.58 percentage points vs. December 2012. EIR on deposits with a term of over three years was 4.28% in December 2013, which is 0.18 percentage points lower than in December 2012 when this rate was at 4.46%.

Average EIR on retail deposits in December 2013 was at 2.65% and is 0.33 percentage points lower than in December 2012. The lowest rate identified in 2013 was in October of 2.27%, while the highest was seen in September 2.83%. As for the corporate segment, rates have higher values and in December 2013 they stood at 3%, 1 percentage point below the rate in December 2012. During 2013, the lowest level of 2.39% was seen in November and the highest of 4.16% in February.

Starting from the 2H 2012, new corporate deposits decreased, especially those of short term nature. During the said period, they were at their lowest level over the past four years. This has resulted in significant increase of interest rates on short term corporate deposits. Although the Y2013saw a decrease of corporate interest rates for both, short term and long term deposits, in December 2013 average interest rates of the corporate segment (3%) were still higher than average interest rates of the retail segment (2.65%).

Our analysis of trends of weighted average interest rates of deposits on an annual level for the past two years has revealed an increase of interest rates on short term deposits, while long term deposits (after a moderate increase in 2012) dropped significantly in 2013 (down by 0.58 percentage points). Banks use their interest rate policies to manage profitability and plan an optimal sector-level and maturity structure of deposit sources, all in line with the strategy of financing and lending.

Table 37 : *Weighted average NIR and EIR on deposits on an annual level*										
DESCRIPTION	**12/2009**		**12/2010**		**12/2011**		**12/2012**		**12/2013**	
	NIR	**EIR**	**NIR**	**EIR**	**NIR**	**EIR**	**NIR**	**EIR**	**NIR**	**EIR**
1	2	3	4	5	6	7	8	9	10	11
1. Weighted average IR on ST deposits:	2,02	2,04	1,31	1,31	1,16	1,16	1,45	1,47	1,65	1,67
1.1. up to 3 months	1,59	1,60	0,60	0,60	0,87	0,87	0,86	0,88	1,47	1,47
1.2. up to 1 year	3,76	3,79	2,79	2,79	2,53	2,53	2,55	2,57	1,85	1,87
2. Weighted average IR on LT deposits:	4,77	4,80	4,00	4,02	3,59	3,63	3,78	3,81	3,20	3,23
2.1. up to 3 years	5,25	5,29	3,90	3,92	3,47	3,50	3,69	3,71	2,97	3,00
2.2. over 3 years	3,09	3,09	4,56	4,60	4,9	4,29	4,44	4,51	4,15	4,18
3. Total weighted average IR on deposits	2,97	2,99	2,33	2,34	1,99	2,00	2,61	2,64	2,51	2,53

Weighted interest rates on loans, i.e. transaction account overdraft facilities, and demand deposits, as calculated on basis of monthly reports, are provided in the table below.

Table 38 : *Weighted average NIR and EIR on overdraft facilities and demand deposits*										
DESCRIPTION	**12/2011**		**6/2012**		**12/2012**		**6/2013**		**12/2013**	
	NIR	**EIR**	**NIR**	**EIR**	**NIR**	**EIR**	**NIR**	**EIR**	**NIR**	**EIR**
1	2	3	4	5	6	7	8	9	10	11
1. Weighted average IR on overdraft facilities	8,73	8,86	8,40	8,53	8,43	8,57	8,37	8,53	8,25	8,42
2. Weighted IR on demand deposits	0,18	0,18	0,22	0,22	0,19	0,19	0,18	0,18	0,15	0,15

As a rule, EIR on these assets and liabilities items is equal to the nominal interest rate. Weighted EIR on total overdraft facilities for the banking sector in December 2013 stood at 8.42% (down by 0.15 percentage points vs. December 2012) and at 0.15% on demand deposits (down by 0.04 percentage points than in December 2012).

2.4. Liquidity

Along with credit risk management, the liquidity risk management is one of the most important and the most complex segments of banking operations. Liquidity maintenance within the market economy is one of key preconditions to establishing and preserving trust in the banking system of any country. The same stands for its stability and safety.

Until emergence of the global financial and economic crisis, under normal operating conditions of banks and within a stable environment, the liquidity risk for banks was of a secondary importance, i.e. credit risk was the focal point and established management systems, i.e. systems for identification, measurement and control of this risk were under continuous supervision in order to improve and upgrade such systems.

When financial markets got disrupted due to the effect of the global crisis, the liquidity risk suddenly gained importance and management of this risk became a key factor to smooth operations, as well as timely reporting of liabilities due and preservation of long term position of the bank in sense of its solvency and capital base. In addition, it is worth noting that interdependence of all risks the bank is or may b exposed to in its operations has also came to light upon rising of the crisis.

During the last quarter of 2008, after expansion of the global crisis and its negative effect to the financial and economic system of B&H, the liquidity risk of banks in the FB&H has risen. Although one part of savings deposits got withdrawn and trust in banks got impaired, we find that liquidity of the banking system was never at stake since banks in the FB&H (due to regulatory requirements and defined limits based on a conservative approach) had significant liquid assets and good liquidity position.

In 2009, negative trends from the last quarter of 2008 have come to a halt and basic liquidity indicators improved (thanks mostly to reduced lending activity). In 2010, we saw a slight impairment of these indicators, continuing in 2011, but in lesser intensity. Somewhat greater impairment of these indicators was seen in again in 1Q 2012, as a result of reduced cash funds related to slight increase of lending activity and investments in securities, reduced deposits, payments of loan obligations due and increase of uncollected receivables. This was a trend that, with minor oscillations, continued until the end of 2012. The first half of 2013 was characterized by continued mild worsening of these indicators, caused by the deposits outflow, payment of loan obligations due and continued growth of past due uncollected receivables, while the 2H 2013 was displaying slight improvement of indicators, as caused by an increase of deposits and cash funds.

Banks' efforts to achieve better profitability through better allocation of financial assets, changes in the structure of deposit sources, as well as long-present trend of reduction of loan obligations and obligations under subordinated debt, as well as effects of the mortgage crisis and recession in the Euro zone, have all led to faster decrease of liquid assets vs. the reduction of short term financial liabilities, decrease of share of liquid assets in total assets and worsened ratio of loans to deposits, loans taken and subordinated debt.

However, despite the evident negative trends, liquidity of the banking system in the Federation of B&H is still seen as sound, having satisfactory share of liquid assets in total assets, as well as very good maturity matching of financial assets and financial liabilities, plus a trend of moderate improvement starting from the end of 2010. Still, due to still present effect and impact of the global financial crisis, as well as mortgage crisis in the Euro zone (that has adversely reflected upon banking systems of certain European countries and parent banks of FB&H banks, we find that the liquidity risk should still be kept under close supervision. Also, we should bear in mind the still present effect of the crisis on the real sector, whose negative consequences reflected upon the overall industrial and economic environment in which FB&H banks operate, thus resulting in defaults with settlement of loans and increase of uncollectable receivables, i.e. reduction of inflows of liquid funds to banks and conversion of credit risk into liquidity risk. In that sense, one of key effects of the liquidity position of banks in the period ahead is seen with their capacity to adequately manage their assets, thus entailing obtaining assets with good performances and whose quality ensures that bank loans (and interest) are repaid in line with maturity dates.

The Decision on Minimum Standards for Liquidity Risk Management defines minimum standards that a bank is required to ensure and maintain in the liquidity risk management process, i.e. minimum standards for development and implementation of the liquidity policy that ensures bank's capacity to fully and without a delay meet its obligations on the maturity date.

This regulation represents a framework for the liquidity risk management and encompasses qualitative and quantitative provisions and requirements for banks. It also defines limits that banks are to meet in relation to the average 10-day minimum and daily minimum of cash funds vs. short term sources of funds, as well as minimum limits for maturity matching of instruments of financial assets and financial liabilities (up to 180 days).

Within the structure of financing sources of banks in the FB&H as of 31.12.13, the largest share of 74.6% still refers to deposits, followed by loans taken (including subordinated debts[38]) of 7.8%. Loans taken bear longer maturities and represent quality source for approval of long term loans and improve maturity matching of assets and liabilities, although their reduction trend has been evident for an extensive period of time.

[38] Subordinated debts: loans taken and permanent items

On the other hand, maturity structure of deposits is much more unfavorable[39]. After a longer period of improvement, in 2010 it slightly worsened and this trend (with minor oscillations) continued in 2011 and 1Q 2012, after which it still stopped and the structure modestly improved in late 2012 and continued to improve in 2013.

- in 000 KM-

Table 39: *Maturity structure of deposits by contractual maturity*

DEPOSITS	31.12.2011		31.12.2012		31.12.2013		INDEX	
	Amount	% share	Amount	% share	Amount	% share		
1	2	3	4	5	6	7	8(4/2)	9(6/4)
Šavings and demand deposits:	4.983.292	44,8	4.805.480	43,8	5.233.356	45,4	96	109
Up to 3 months	433.030	3,9	267.199	2,5	365.229	3,2	62	137
Up to 1 year	756.332	6,8	709.620	6,5	668.142	5,8	94	94
1. Total ST deposits	6.172.654	55,5	5.782.299	52,8	6.266.727	54,4	94	108
Up to 3 years	3.272.641	29,4	3.576.903	32,6	3.541.354	30,7	109	99
Over 3 years	1.679.380	15,1	1.601.799	14,6	1.715.768	14,9	95	107
2. Total LT deposits	4.952.021	44,5	5.178.702	47,2	5.257.122	45,6	105	102
TOTAL (1 + 2)	11.124.675	100,0	10.961.001	100,0	11.523.849	100,0	99	105

As opposed to 31.12.12, total deposits rose by 5% or KM 563 million, as largely resulting from an increase of retail deposits by 7% or KM 433 million, deposits of private companies by 11% or KM 167 million and deposits of banking institutions by 3% or KM 31 million and, on the other hand by a decrease of deposits of government institutions by 17% or KM 117 million and deposits of PSEs by 1.3% or KM 14 million. Maturity structure of deposits with contractual maturity is relatively good, wherein short term deposits hold a share of 54.4% and long term deposits a share of 45.6%, which is somewhat below the condition as of 31.12.12.

Changes in the maturity structure stem from an increase of short term deposits by 8% or KM 484 million, as largely related to the increase of retail deposits by KM 249 million (sight deposits mostly), deposits of private companies by KM 136 million, PSEs by KM 129 million and deposits with a term of up to 3 months with regards to banking institutions. Long term deposits rose slightly by 2% or KM 78 million, as a result of 7% rise of deposits with a term over three years (i.e. retail deposits mostly), while deposits up to three years posted 1% decrease (PSEs mostly). Of note, long term deposits are still dominated by two segments: retail with a share increase from 61.0% to 63.6% and banking institutions with a share reduction from 13.2% to 12.3%, although deposits of PSEs also hold the significant share - however, going slightly down from 12.1% to 9.2%. Within deposits with a term from one to three years, the largest share of 67.4% is with retail deposits (slightly up by 1.8 percentage points), followed by PSE deposits of 13.2% (down by 4.0 percentage points). Deposits over three years mostly consist of retail deposits (55.8%, up by 5.0 percentage points) and deposits of banking institutions with a share of 25.6% resulting from several years long trend of reduction (vs. YE2012: 33.0%, YE2011: 46.9%, 2010: 60.9%).

Although maturity structure of deposits with contractual maturity is relatively good, residual maturity of deposits is of greater relevance for the liquidity risk analysis since it includes deposit balances from the reporting period to the due date (as presented in the table below).

[39] As per remaining maturity.

- in 000 KM-

Table 40: *Maturity structure of deposits by remaining maturity*

DEPOSITS	31.12.2011 Amount	% share	31.12.2012 Amount	% share	31.12.2013 Amount	% share	INDEX	
1	2	3	4	5	6	7	8(4/2)	9(6/4)
Savings and demand deposits (up to 7 days)	5.184.070	46,6	4.941.325	45,1	5.343.263	46,4	95	108
7- 90 days	917.917	8,3	908.834	8,3	920.951	7,9	99	101
91 days to one year	2.219.322	19,9	2.278.639	20,8	2.126.249	18,5	103	93
1. Total short term deposits	8.321.309	74,8	8.128.798	74,2	8.390.463	72,8	98	103
up to 5 years	2.404.179	21,6	2.609.727	23,8	3.002.846	26,1	109	115
over 5 years	399.187	3,6	222.476	2,0	130.540	1,1	56	59
2. Total long term deposits	2.803.366	25,2	2.832.203	25,8	3.133.386	27,2	101	111
TOTAL (1 + 2)	11.124.675	100,0	10.961.001	100,0	11.523.849	100,0	99	105

Based on the data above, we find that the maturity structure of deposits by remaining maturity is much worse due to high share of short term deposits of 72.8%. However, there is a trend of moderate improvement vs. YE2012. Short term deposits rose by 3% or KM 262 million, thus its share decreased by 1.4 percentage point, while long term deposits increased by 11% or KM 301 million and its share going up from 25.8% to 27.2%. Looking into the structure of long term deposits, it is dominated by deposits with remaining maturity of up to 5 years (with a share of 95.8% in long term deposits and 26.1% in total deposits), while the negative trend is seen with regards to major reduction of deposits with remaining maturity of over 5 years (if observing the period of the past two years). We have compared information on deposit maturities by contractual and residual maturity and found that out of the total long term contracted deposits of KM 5.3 billion, there was KM 2.1 billion or somewhat above 40% of these deposits as of 31.12.13 that had the remaining maturity of one year.

Existing maturity structure of deposits (being the largest source of financing of banks in the FB&H) has become an increasingly limiting factor to the credit growth regarding most banks since they incline more towards approving long term loans. Therefore, banks are facing a problem of finding ways to obtain quality sources of funds in sense of maturity, especially because of considerable reduced inflow of financial assets (borrowings) from abroad, i.e. from parent groups and financial institutions-creditors, while local sources of funds are mostly of short term character.

In addition, supervisory concern is pronounced in relation to the fact that banks, due to lack of quality long term sources of funds and for purpose of ensuring compliance with legally defined limits related to maturity matching, resort to approving revolving short term loans, i.e. settlement of existing with new short term facilities, which basically means long term lending from short term sources of funds. In this way, they are not providing the real picture as to the loan maturity and its matching with sources of funds. This may pose a serious problem in the period ahead, as well as a potential threat to the banks' liquidity position.

For purpose of planning the required level of liquid assets, banks need to account for both, their sources of funds and the structure of an adequate liquidity potential, which is also tied to plans for their credit policy. Loan maturity, i.e. maturity of the loan portfolio, is in fact determined by maturity of sources of funds. Since maturity transformation of funds in banks is inherently related to functional characteristics of banking operations, banks are required to continuously control and maintain maturity mismatches between sources of funds and extended loans within the regulated minimum limits.

-in 000 KM-

Table 41: *Maturity structure of loans*								
LOANS	**31.12.2011**		**31.12.2012**		**31.12.2013**		**INDEX**	
	Amount	**% share**	**Amount**	**% share**	**Amount**	**% share**		
1	2	3	4	5	6	7	8(4/2)	9(6/4)
Past due receivables and paid off-balance liabilities	962.707	9,2	1.074.251	10,1	1.175.825	10,8	112	109
Short term loans	2.287.597	21,8	2.472.571	23,2	2.360.832	21,8	108	95
Long term loans	7.237.367	69,0	7.119.302	66,7	7.315.743	67,4	98	103
TOTAL LOANS	10.487.671	100,0	10.666.124	100,0	10.852.400	100,0	102	102

In 2013, long term loans rose moderately by 3% or KM 196 million, short term loans fell by 5% or KM 112 million, while past due receivables climbed by 9% or KM 102 million, which is yet another indicator of impaired collection rate of loans due and difficulties that debtors have in servicing liabilities towards banks (in the light of the economic crisis). Within the structure of past due receivables, 71% refers to private companies, 27% to the retail sector and 2% to other sectors.

An analysis of maturities of two key sectors shows that 85.7% of retail loans are of long term character, while this percentage among corporate loans equals 48.0%.

As the key assets category, loans still hold the largest share of 70.2%, down by 1.0 percentage point vs. YE2012 (although loans themselves have posted a slight increase by 1.7%). Cash funds rose by 11% or KM 455 million and their share climbed from 26.4% to 28.6% vs. YE2012.

An overview of main liquidity ratios is provided in the table below. Banks have transitioned to new regulations as of 31.12.11, which led to a major increase of total assets, thus causing impairment of ratios: loans vs. deposits and loans taken (if observed across periods). In 2012, liquidity ratios got further impaired, as prompted by a reduction of cash funds through increased lending activity and settlement of loan obligations due, while the ratio of short term financial liabilities/total financial liabilities improved somewhat, as based on better maturity structure of sources of funds. This also continued in the 1H 2013. The increase of deposits and cash funds in 2H 2013 led to a moderate improvement of the ratios vs. 31.12.12.

- in % -

Table 42: *Liquidity ratios*			
Ratios	**31.12.2011**	**31.12.2012**	**31.12.2013**
1	2	3	4
Liquid assets[40] / total assets	28,9	26,8	28,9
Liquid assets / ST finan.liabilities	49,0	46,2	50,6
ST finan.liabilities/ total finan. Liabilities	69,1	68,9	67,9
Loans / deposits and loans taken[41]	84,3	88,1	86,4
Loans / deposits, loans taken and subordinated debts[42]	82,9	86,8	85,3

In 2012, the ratio of loans vs. deposits and loans taken has worsened. The same trend continued in 1H 2013, but was stopped in the 2H 2013. As of 31.12.13, this ratio was above 85% (critical level) with regards to 12 banks. On one hand, this was a result of their liabilities structure (relatively significant share of capital) and, on the other hand, a result of high share of loans in assets. FBA paid special attention in its on-site examinations to banks with identified weaknesses in this segment and

[40] In more narrow sense, liquid assets are: cash and deposits and other financial assets with remaining maturity below 3 months (excluding interbank deposits).

[41] Empirical standards are: below 70%-very sound, 71%-75%-satisfactory, 76%-80%-marginally satisfactory, 81%-85%-insufficient, over 85%-critical.

[42] Previous rato was expanded, sources now include subordinadet debts, thus providing a more realistic picture.

instructed them to take actions and measures to improve the liquidity level and practices of sources of financing management in order to ensure satisfactory liquidity position.

In 2013, banks have duly fulfilled the requirement of maintaining the defined level of mandatory reserve with the Central Bank of B&H. The mandatory reserve, being the key instrument of the monetary policy in B&H under conditions of the Currency Board and financially undeveloped market, is the only instrument of the monetary policy that ensures monetary control in sense of prevention of rapid growth of loans and reduced multiplication, as well as increased liquidity in banks under conditions of the crisis and higher outflow rate of funds from banks (as compared to the situation in B&H as of 01.10.08). On the other hand, implementation of FC risk regulations and maintenance of currency matching within the defined limits has also significantly impacted the amount banks hold at their reserve accounts with the Central Bank of B&H (in LCY), thus ensuring high liquidity of banks individually and at the banking sector level.

All banks have been continuously meeting and exceeding the defined minimum of 10-day average of 20% of ST sources of financing and daily minimum of 10% of the same sources, as illustrated from the table below.

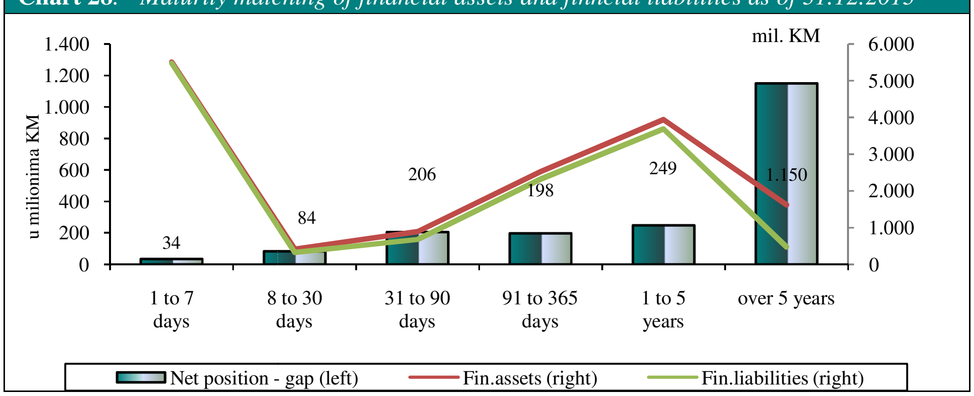
- in 000 KM-

Table 43: *Liquidity position—10-day average and daily minimum*

Description	31.12.2011	31.12.2012	31.12.2013	INDEX	
	Amount	Amount	Amount		
1	2	3	4	5(3/2)	6(4/3)
1. Average daily balance of cash	3.759.486	3.408.958	3.722.887	91	109
2. Lowest total daily cash balance	3.550.990	3.149.188	3.423.657	89	109
3. ST sources of funds (calculation basis)	6.013.102	5.631.431	5.887.967	94	105
4.Amount of liabilities:					
4.1. 10-day average 20% of the amount under item 3	1.202.620	1.126.286	1.177.593	94	105
4.2. daily minimum 10% of the amount under item No. 3	601.310	563.143	588.798	94	105
5.Performance of liabilities:10-day average					
Surplus = Item No. 1 – Item No. 4.1	2.556.866	2.282.672	2.545.294	89	112
6. Performance of liabilities : daily minimum					
Surplus = Item No. 2 – Item no. 4.2	2.949.680	2.586.045	2.834.859	88	110

Observing the maturity matching of remaining maturities of total financial assets[43] and liabilities, we find that the maturity rate is good, although somewhat lower than as of 31.12.12.

Chart 28: *Maturity matching of financial assets and fincial liabilities as of 31.12.2013*



[43] Financial assets are posted on a net basis (deducted by value adjustments).

At the end of 2013, short term financial assets of banks were higher than short term financial liabilities by KM 522 million. If compared to the YE2012 when the positive gap was KM 276 million, this represents an increase by KM 246 million or 89.1%, thus also leading the coverage ratio of ST liabilities going from 103.2% to 105.9%.

Short term financial assets rose by 4.1% and short term financial liabilities by 1.4%. Within the structure of ST financial assets, this increase referred to cash funds (up by 11.% or KM 455 million), securities held to maturity (up by 18.9% or KM 13 million) and trading assets (up by 1.8% or KM 7 million), while a decrease was seen in relation to net loans (down by 1.9% or KM 80 million), cash borrowings to other banks (down by 33.6% or KM 26 million) and other financial assets (down by 2.3% or KM 3.5 million). Financial assets with remaining maturity over one year rose by 1.9% or KM 104 million as a result of loans going up by 2.1% or KM 111 million and securities held to maturity going down by 5.5% or KM 6 million.

As for liabilities with maturity up to one year, they have risen by slight 1.4% or KM 119 million, wherein the largest increase refers to deposits (+3.2% or KM 261 million) coupled with reduction of other financial liabilities by 34.4% or KM 93 million, liabilities under loans by 13% or KM 32 million, subordinated debt by 38.2% or KM 16 million and borrowings from other banks by 100% or KM2 million. Liabilities with maturity over one year rose by 6% or app. KMM235 million, as a result of an increase of deposits by 10.6% or KM 301 million and other financial liabilities by 16.1% or KM 9 million, coupled with a reduction of liabilities under loans by 7.9% or KM71 million and liabilities under subordinated debt by 2.8% or KM 4 million.

In addition to the said prescribed minimal standard, a very important aspect of this increase and the analysis of the liquidity position is maturity matching of remaining maturities of financial assets and financial liabilities according to the time scale created to capture a time horizon of 180 days in line with the prescribed minimum limits[44].

[44] The Decision on Minimum Standards for Liquidity Risk Management in Banks defines these percentages for maturity matching of financial assets and financial liabilities: min. 85% of sources of financing with maturity up to 30 days must be used for facilites with maturity up to 30 days, min. 80% of sources of financing with maturity up to 90 days must be used fr facilities with maturity up to 90 days, and min. 75% of sources of financing with maturity up to 180 days must be used for facilities with maturity up to 180 days.

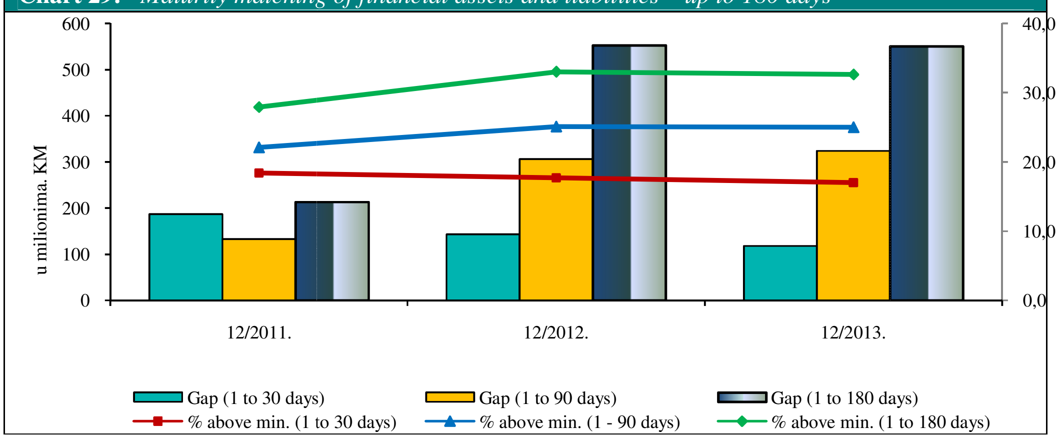
- in 000 KM -

Table 44: *Maturity matching of financial assets and liabilities (up to 180 days)*

Description	31.12.2011 Amount	31.12.2012 Amount	31.12.2013 Amount	INDEX 5 (3/2)	INDEX 6(4/3)
1	2	3	4	5 (3/2)	6(4/3)
I. 1- 30 days					
1. Financial assets	5.748.473	5.490.582	5.924.581	96	108
2. Financial liabilities	5.561.192	5.346.703	5.806.538	96	109
3. Difference (+ or -) = 1-2	187.281	143.879	118.043	77	82
Calculation of prescrib.requirement in %					
a) Actual %= No. 1 / No. 2	103,4%	102,7%	102,0%		
b) Prescribed minimum %	85,0%	85,0%	85,0%		
Plus (+) or minus (-) = a - b	18,4%	17,7%	17,0%		
II. 1-90 days					
1. Financial assets	6.511.798	6.355.017	6.809.401	98	107
2. Financial liabilities	6.378.807	6.048.777	6.485.630	95	107
3. Difference (+ or -) = 1-2	132.991	306.240	323.771	230	106
Calculation of prescrib.requirement in %					
a) Actual %= No. 1 / No. 2	102,1%	105,1%	105,0%		
b) Prescribed minimum %	80,0%	80,0%	80,0%		
Plus (+) or minus (-) = a - b	22,1%	25,1%	25,0%		
III. 1-180 days					
1. Financial assets	7.522.305	7.454.731	7.813.043	99	105
2. Financial liabilities	7.308.881	6.903.027	7.263.009	94	105
3. Difference (+ or -) = 1-2	213.424	551.704	550.034	259	100
Calculation of prescrib.requirement in %					
a) Actual %= No. 1 / No. 2	102,9%	108,0%	107,6%		
b) Prescribed minimum %	75,0%	75,0%	75,0%		
Plus (+) or minus (-) = a - b	27,9%	33,0%	32,6%		

Based on presented information, we find that, as of 31.12.13, banks have adhered to prescribed limits and achieved better maturity matching of financial assets and financial liabilities vs. such prescribed limits

Chart 29: *Maturity matching of financial assets and liabilities – up to 180 days*



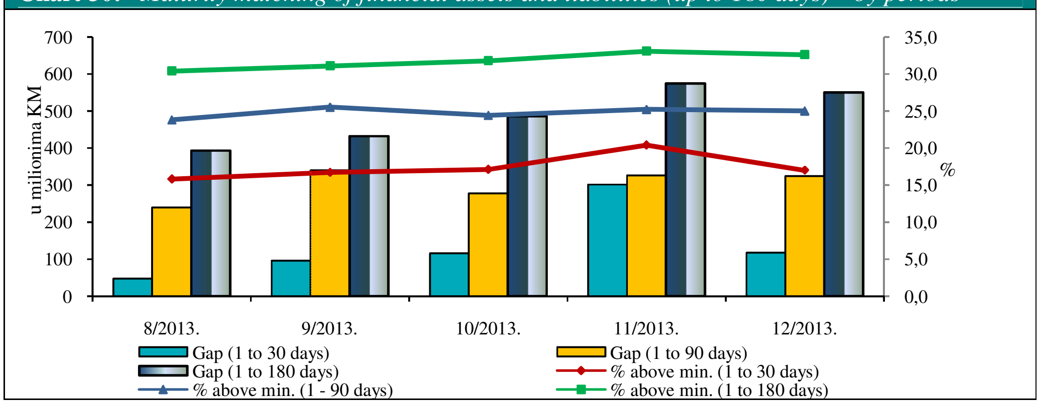
As of 31.12.10, financial liabilities exceeded financial assets across all three time intervals up to 180 days, but the Y2011 saw an improvement of the maturity matching. This is to say that as at YE2011, financial assets were above financial liabilities during all three time intervals and percentages of maturity matching were above the prescribed minimum by 18.4% in the first time interval, by 22.1% in the second and by 27.9% in the third time interval. The trend of improvement of the maturity matching continued in 2012 as well, so financial assets surpassed financial liabilities as of 31.12.12 in

all three maturity intervals, coupled with somewhat better liquidity position within the intervals of 90 days and 180 days, while the positive gap within the interval of 30 days was still somewhat lower than as of 31.12.11. As at YE2011, the maturity matching percentages were above the defined minimum: by 17.7% in the first time interval, by 25.1% in the second and by 33.0% in the third time interval.
As of 31.12.13, the maturity interval of 30 days saw a reduction of the positive gap due to the increase of financial liabilities (mainly deposits and other financial liabilities) being higher than the increase of financial assets (cash funds and securities held to maturity). A slight reduction was also seen with regards to the time interval of 90 days due to equivalent growth rate of 7.2% of financial assets (primarily cash funds and securities held to maturity) and financial liabilities (mostly deposits, liabilities under loans and other liabilities). Somewhat lower positive gap was also seen with the time interval of 180 days, due to high growth rate of financial liabilities caused by an increase of deposits and other financial liabilities (that was compensated by a decrease of liabilities under loans), while financial assets posted a smaller growth rate due to reduction of loans (increase of cash funds and reduction of loans and borrowings to other banks).

All of this resulted in the maturity matching percentage for all three time intervals being somewhat lower than as at YE2012. However, this is still considerably above the defined minimum: for the first interval by 17.0%, for the second by 25.0% and for the third time interval by 32.6%.

The chart below shows the trend of maturity matching of financial assets and financial liabilities in the period from August to December 2013 (by time intervals and maturity matching percentages vs. the legally defined minimal standards).

Chart 30: *Maturity matching of financial assets and liabilities (up to 180 days) – by periods*



Based on all presented ratios, liquidity of the banking sector in the FB&H is still deemed satisfactory. However, since this business segment and the exposure level to the liquidity risk correlate with the credit risk and considering also effects of the financial crisis to B&H and the FB&H banking sector (primarily in sense of increased pressure to the banks' liquidity), we should underline that banks should pay even more attention to the liquidity risk management by means of establishing and implementing liquidity policies that would ensure timely performance of all liabilities due, as based on continuous planning of future liquidity needs factoring therein changes in operating, economic, regulatory and other conditions of the banks' business environment. On one hand, this rests on poor maturity structure of deposits, repayment of past due loans and much smaller debt rate with financial institutions (thus being the best source of financing for banks from the maturity perspective) and, on the other hand, on poor inflow of liquid funds due to declined collection rate of loans.
Through its off-site and on-site examinations, FBA will continue to monitor and oversee the manner in which banks manage their risk and whether they act in accordance with adopted policies and programs.

2.5. FX Risk – Foreign Currency Matching of BS and Off-BS Assets and Liabilities

Banks' operations are exposed to major risks originating from possible losses related to balance sheet and off-balance sheet items, as incurred due to market price changes. one of these risks is a foreign currency risk arising as a result of changes in exchange rates and/or mismatches between assets, liabilities and off-balance sheet items denominated in the same currency – individual FX position or all currencies of the bank's operations together – total FX position of the bank.

In order to ensure implementation and realisation of prudent principles related to FX activities of banks and to reduce FX risk effects on their profitability, liquidity and capital, the FBA has adopted the Decision on Minimum Standards for FX Risk Management in Banks[45] that regulates FX risk assumption, monitoring, control and management, as well as limits for the open individual and total FX position (long or short) calculated in relation to the core capital of the bank. [46]

In order for the FBA to monitor banks' compliance with the regulated limits and their exposure level to the FX risk, banks are required to perform daily reporting to the FBA. Based on a review, monitoring and analysis of delivered reports, we find that banks adhere to regulated limits and perform their FX activities within such limits.

Since the Central Bank of B&H functions as a currency board pegged to EUR, banks are not exposed to FX risk in their daily operations with EUR.

As of 31.12.13, the currency structure of banks' assets included 12.6% or KM 1.9 billion of foreign currency items (as at YE2012, these items stood at 13.4% or KM 2 billion). On the other hand, currency structure of liabilities is quite different since the share of FC liabilities is much higher and equals 46.7% or KM 7.2 billion (as at YE2012, this share was 48.2% or KM 7.2 billion).

The table below provides the structure and trend of financial assets and liabilities and FX positions for EUR as the key currency and for the total position.

[45] Official Gazette of the FB&H Nos. 3/03, 31/03, 64/03, 54/04.

[46] Article 8 of the Decision on Minimum Standards for Managing Banks' Capital defines the following limits: for the individual FX position – up to 30% of the core capital for EUR and up to 20% for other currencies and for the total bank position – up to 30%.

- in KM million-

Table 45: *FC matching of financial assets and liabilities (EUR and aggregate)*[47]

Description	31.12.2012				31.12.2013				INDEX	
	EUR		TOTAL		EUR		TOTAL		EUR	TOTAL
	Amount	Share %	Amount	Share %	Amount	Share %	Amount	Share %	6/2	8/4
1	2	3	4	5	6	7	8	9	10	11
I. Financial assets										
1. Cash	1.050	13,8	1.568	18,6	996	13,0	1.516	18,0	95	97
2. Loans	39	0,5	57	0,7	40	0,5	44	0,5	103	77
3.Loans with a currency clause	6.202	81,4	6.435	76,2	6.285	82,2	6.465	76,9	101	100
4. Other	325	4,3	383	4,5	332	4,3	386	4,6	102	101
Total (1+2+3+4)	7.616	100,0	8.443	100,0	7.653	100,0	8.411	100,0	100	100
II. Financial liabilities										
1. Deposits	5.220	70,1	5.888	72,3	5.345	72,6	5.990	74,7	102	102
2. Loans taken	1.058	14,2	1.079	13,3	986	13,4	994	12,4	93	92
3.Dep. & loans with curr.clause	915	12,3	915	11,2	798	10,9	798	9,9	87	87
4. Other	250	3,4	259	3,2	226	3,1	237	3,0	90	92
Total (1+2+3+4)	7.443	100,0	8.141	100,0	7.355	100,0	8.019	100,0	99	99
III. Off-balance sheet										
1.Assets	153		153		80		80			
2.Liabilities	235		349		255		359			
IV.Position										
Long (amount)	90		106		122		113			
%	5,2%		6,2%		6,6%		6,1%			
Short										
%										
Allowed	30%		30%		30%		30%			
Less than the allowed level	24,8%		23,8%		23,4%		23,9%			

In terms of the structure of foreign currencies, dominant share among financial assets [48] is held by EUR with 70.3%, which is somewhat lower than as of 31.12.12 (70.4%) due to lower nominal amount (from KM 1.41 billion to KM 1.36 billion). The share of EUR in liabilities is 90.8%, up by 0.5% vs. YE2012, coupled with a slight increase of the nominal amount to KM 29 million.

However, FX risk exposure calculation also includes an amount of indexed assets items (loans) and liabilities items[49], which is quite significant on the assets side (76.9% or KM 6.5 billion) and, in nominal terms, remained almost the same as on 31.12.12 (76.2% or KM 6.4 billion). Other FX items on the assets side hold a share of 23.1% or KM 1.9 billion and bear the following structure: items in EUR 16.3% or KM 1.4 billion and other currencies 6.9% or KM 0.6 billion (at YE2012, loans with a currency clause amounted KM 6.4 billion and had a share of 76.2%, while other items in EUR had a share of 16.8% or KM 1.4 billion). Out of the total net loans (KM 9.7 billion), app. 66.7% have the currency clause (mostly pegged to EUR – 97.2%).

As for the sources of financing, financial liabilities determines the structure of financial assets for every currency respectively. The largest share among financial liabilities (KM 8.0 billion) is 81.8% or KM 6.5 billion and refers to EUR (deposits mostly), while the share and amount of indexed

[47] Source: Form 5-FX position.

[48] Source: Form 5-FX position: one part of financial assets (FCYs denominated in KM). According to the calculation methodology, financial assets were posted according to the net principles until 31.12.2011 (i.e. after deductions for loan loss reserves), after which the new methodology entailed depreciation of fixed assets according to IAS, i.e. after deductions for value adjustments and reserves for contingent liabilities.

[49] In order to protect against foreign exchange rate changes, banks arrange certain assets items (loans) and liabilities items with a currency clause (regulations allow only for a two-way currency clause).

liabilities is at minimal 9.9% or KM 0.8 billion (at YE2012, share of liabilities in EUR was 80.2% or KM 6.5 billion, while share of indexed liabilities was 11.2% or KM 0.9 billion).

If observed by banks and at the FB&H banking sector level, we find that FX risk exposure of banks and of the banking system in 2013 was within the defined limits. As of 31.12.13, the long FX position was seen with 14 banks and the short position with 3 banks. At the system level, there is a long FX position of 6.1% of the total core capital of banks, which is by 23.9% below the allowed limit. Individual FX position for EUR was 6.6%, which is 23.4% below the allowed limit, wherein financial assets items were greater than financial liabilities (net long position).

Although the currency board protects banks from the FX risk exposure related to EUR, they are required to adhere to regulated limits for all currencies, as well as for the total FX position, and to perform daily risk management activities in line with the adopted programs, policies, procedures and plans.

IV CONCLUSIONS AND RECOMMENDATIONS

During the reform period, the banking sector of the Federation of B&H achieved an enviable level of its development and it represents the most developed and the strongest part of the financial and the overall economic system in the FB&H. Future activities should be aimed towards preservation of its stability, meaning this should be a priority under present stressful conditions and considering therein the banking system's future progress and development. These targets are conditioned by a continuous and committed involvement of all elements of the system, as well as legislative and executive authorities, thus forming grounds for more favorable economic environment for banks and the real sector of the economy, as well as for the general population.

In order to further strengthen resilience of banks in the Federation of B&H to potentially more severe crisis situation, in early 2013, the FBA has adopted the Decision on Temporary Measures for Dividends and Discretionary Bonus Disbursement and Repurchase of Own Shares by Banks. This meant that disbursement of dividends is tied to existence of a capital buffer of 2.5% of the prescribed minimum capital adequacy rate and core capital rate of banks vs. risk-bearing assets. As a part of activities regarding implementation of the Strategy, i.e. Revised Strategy for introducing the International Convergence of Capital Measurement and Capital Standards (Basel II), the FBA has coordinated the matter with the Republika Srpska Banking Agency and USAID (providing technical assistance) to preparing the following draft papers: Decision on the Remuneration Policy and Practice for Bank Employees, Decision on Suitability Assessment of Bank's Bodies and Decision on Diligent Behavior of Members of Bank's Bodies. These decisions were adopted in August 2013 (Official Gazette of the FB&H No. 60/13).

In the following period, the FB&H Banking Agency intends to:

- take measures and actions within its competencies to overcome and mitigate effects of the global financial crisis on the banking sector in the FB&H;
- continue with activities within its competencies to consolidate the supervision function on a state level;
- maintain continuous supervision of banks through on-site and off-site examinations, placing an emphasis therein on dominant risk segments of the banking business and aiming to improve efficiency by means of:
    - further insisting on capital strengthening in banks, especially for those banks with an above average assets growth and reduction of capital adequacy rate.

- continued banking supervision mainly from the perspective of system relevance for the development of lending activities where large savings and other deposits are concentrated (all for purpose of depositors' protection).
- continued system-based monitoring of banks' activities on prevention of money laundering and terrorism financing and improving of cooperation with other supervisory and regulatory institutions,
- as so far, working on upgrades to legal regulations as based on Basel Principles, Basel Capital Accord and European Banking Directives, all as a part of preparations for B&H joining the European Union,
- changing capital regulations for purpose of ensuring qualitative and structural strengthening of capital and alignment with capital requirements of the Basel II/III;
- preparing and adopting a contingency plan (as a part of crisis preparations),
- developing and implementing Early Warning System tool (EWS) for purpose of an early identification of financial and operational inefficiencies and/or adverse trends in banks' operations,
- establishing and expanding cooperation with supervisory authorities in home countries of investors in the FB&H banking sector, as well as in other countries – all for purpose of ensuring more efficient bank supervision function,
- improving cooperation with the B&H Banks' Association across all segments of the banking business, organising consultations and providing professional assistance in implementation of banking laws and regulations, improving cooperation in sense of professional training, proposing amendments to all laws or regulations that have become a limiting factor to banks' development, introducing new products, collection of receivables and ensuring full involvement in development and functioning of a unified registry of non-performing customers – legal entities and private individuals (ensuring therein daily updates to relevant information).

* Continue with efforts on improving the information system that would enable early warning and preventive actions with respect to elimination of weaknesses in banks' operations;
* Continue with an on-going training and professional education of its staff;
* Accelerate actions regarding finalisation of liquidation processes, as per Management Board conclusions.

Further strong engagement of other institutions and bodies of Bosnia and Herzegovina and the Federation of Bosnia and Herzegovina is also necessary with regards to the following:

* implementation of the Program of measures to mitigate results of the global economic crisis and improve the business environment (as accepted by the FB&H Economic-Social Council in December 2008 and in line with relevant FB&H Government paper;
* implementation of conclusions reached by the FB&H Parliament regarding establishment of a state-level bank supervision function;
* creating and upgrading regulations pertaining to the financial sector that refer to actions, status and operations of banks, micro credit organisations, leasing companies, insurance companies, etc.;
* accelerated implementation of economic reforms in the real sector of the economy in order to ensure faster alignment with the level achieved in the monetary and banking sector;
* preparation and adoption of the new Law on Banks/Law on Credit Institutions;
* preparation and adoption of the Law on Asset Management Companies;
* preparations for drafting legal regulations of relevance for the banking sector and financial system based on Basel Principles, Basel Capital Accord and European Banking Directives;
* establishment of special commercial departments within courts;
* establishment of more efficient enforcement proceedings against pledged property;
* adoption of regulations of protection of financial service users and full liability of debtors;
* enactment of laws or improvement of existing legal regulations defining the segment of security and protection of money in the bank and in transit, etc.

As key segments of the banking system, banks should concentrate their efforts on the following activities:

- full commitment to quality and prudent operations and to combating the crisis effects presently posing the biggest threat to banks, real sector of the economy and general population;
- preparation of and updates to their contingency plans;
- further capital strengthening and ensuring solvency level proportional to an increase of assets and risk, greater profitability, more consistent implementation of adopted AML and CTF policies and procedure, security and protection of money in the bank and in transit, all in line with laws and regulations;
- strengthening the internal controls system and the internal audit function as segments that are fully independent in performance of their duties and roles;
- regular, timely and accurate delivery of information to the Central Loans Registry and the Uniform Registry of Accounts with the Central Bank of B&H.

No. U.O.-57-3/14
Sarajevo, 31.03.2014

ATTACHMENTS

ATTACHMENT 1

Banks in the Federation of Bosnia and Herzegovina - 31.12.2013

No.	BANK	Address		Phone	CEO
1	BOR BANKA dd - SARAJEVO	Sarajevo	Obala Kulina bana 18	033/278-520, fax:278-550	HAMID PRŠEŠ
2	BOSNA BANK INTERNATIONAL dd - SARAJEVO	Sarajevo	Trg djece Sarajeva bb	033/275-100, fax:203-122	AMER BUKVIĆ
3	HYPO ALPE-ADRIA-BANK dd - MOSTAR	Mostar	Kneza Branimira 2b	070/340-341, fax:036/444-235	ALEXANDER PICKER
4	INTESA SANPAOLO BANKA D.D. BOSNA I HERCEGOVINA	Sarajevo	Obala Kulina bana 9a	033/497-555, fax:497-589	ALMIR KRKALIĆ
5	INVESTICIONO-KOMERCIJALNA BANKA dd - ZENICA	Zenica	Trg B&H 1	032/448-400, fax:448-501	SUVAD IBRANOVIĆ
6	KOMERCIJALNO-INVESTICIONA BANKA DD V.KLADUŠA	V.Kladuša	Ibrahima Mržljaka 3	037/771-253, fax:772-416	HASAN PORČIĆ
7	MOJA BANKA dd - SARAJEVO	Sarajevo	Trg međunarodnog prijateljstva 25	033/586-870, fax:586-880	MIRZA HUREM
8	NLB BANKA dd - TUZLA	Tuzla	Maršala Tita 34	035/259-259, fax:250-596	ALMIR ŠAHINPAŠIĆ
9	PRIVREDNA BANKA SARAJEVO dd - SARAJEVO	Sarajevo	Alipašina 6	033/277-700, fax:664-175	ADNAN BOGUNIĆ
10	PROCREDIT BANK dd - SARAJEVO	Sarajevo	Franca Lehara bb	033/250-950, fax:250-971	EDIN HRNJICA
11	RAIFFEISEN BANK dd BiH - SARAJEVO	Sarajevo	Zmaja od Bosne bb.	033/755-010, fax: 213-851	MICHAEL MÜLLER
12	RAZVOJNA BANKA FEDERACIJE BIH	Sarajevo	Igmanska 1	033/724-930, fax: 668-952	RAMIZ DŽAFEROVIĆ
13	SBERBANK BH dd - SARAJEVO	Sarajevo	Fra Anđela Zvizdovića 1	033/295-601, fax:263-832	EDIN KARABEG
14	SPARKASSE BANK dd - SARAJEVO	Sarajevo	Zmaja od Bosne 7	033/280-300, fax:280-230	SANEL KUSTURICA
15	UNICREDIT BANK dd - MOSTAR	Mostar	Kardinala Stepinca bb	036/312-112, fax:312-121	IVAN VLAHO
16	UNION BANKA dd - SARAJEVO	Sarajevo	Dubrovačka 6	033/561-000, fax: 201-567	SENAD REDŽIĆ
17	VAKUFSKA BANKA dd - SARAJEVO	Sarajevo	M. Tita 13.	033/280-100, fax: 663-399	AMIR RIZVANOVIĆ
18	ZIRAATBANK BH dd - SARAJEVO	Sarajevo	Dženetića Čikma 2	033/252-230, fax: 252-245	ALI RIZA AKBAŞ

ATTACHMENT 2

LEGAL FRAMEWORK FOR OPERATIONS OF THE FB&H BANKING AGENCY, BANKS, MICRO CREDIT ORGANISATIONS AND LEASING COMPANIES IN THE FEDERATION OF B&H

I. REGULATIONS RELATED TO ORGANISATION OF THE FB&H BANKING AGENCY

- Law on the Banking Agency of the Federation of Bosnia and Herzegovina (Official Gazette of the FB&H Nos. 9/96, 27/98, 20/00, 45/00, 58/02, 13/03, 19/03, 47/06, 59/06, 48/08, 34/12 and 77/12),
- Articles of Association of the Banking Agency of the Federation of B&H (Official Gazette of the FB&H No. 42/04),
- Rules of Internal Organisation of the Banking Agency of the Federation of B&H (Official Gazette of the FB&H Nos. 46/09, 32/10 , 65/12, 88/12, 60/13).

II. REGULATIONS RELATED TO THE AGENCY'S COMPETENCIES

Laws

1. Law on Banks (Official Gazette of the FB&H Nos. 39/98, 32/00,48/01, 27/02, 41/02, 58/02, 13/03, 19/03 and 28/03, 66/13),
2. Law on Micro Credit Organisations (Official Gazette of the FB&H No. 59/06),
3. Law on Associations and Foundations (Official Gazette of the FB&H No. 45/02)
4. Leasing Law (Official Gazette of the FB&H Nos 85/08 and 39/09, 65/13),
5. Law on the Development Bank of the Federation of B&H (Official Gazette of the FB&H No. 37/08),
6. Law on Deposit Insurance in B&H (Official Gazette of B&H Nos. 20/02, 18/05, 100/08 and 75/09, 57/13),
7. Law on Foreign Currency Operations (Official Gazette of the FB&H No. 47/10),
8. Law on Prevention of Money Laundering and Terrorism Financing (Official Gazette of B&H No. 53/09).

Decisions and instructions of the Banking Agency related to operations of banks

1. Decision on Minimum Standards for Managing Information Systems in B&H Banks (Official Gazette of the FB&H No. 1/12),
2. Decision on Minimum Standards for Outsourcing Management (Official Gazette of the FB&H No. 1/12),
3. Decision on Reporting Forms Banks Deliver to the Banking Agency of the FB&H (Official Gazette of the FB&H No. 110/12 and 15/13),
4. Decision on Minimum Standards for Managing Risk Concentrations in Banks (Official Gazette of the FB&H No. 48/12-consolidated text) ,
5. Decision on Minimum Standards for Managing Capital in Banks (Official Gazette of the FB&H No. 48/12-consolidated text),
6. Decision on Minimum Standards for Managing Foreign Currency Risk in Banks (Official Gazette of the FB&H No. 48/12-consolidated text),
7. Decision on Minimum Scope, Form and Contents of the Program and the Report on Economic-Financial Audit of Banks (Official Gazette of the FB&H No. 48/12-consolidated text),
8. Decision on Uniform Method of Calculation and Disclosure of Effective Interest Rate on Loans and Deposits (Official Gazette of the FB&H No. 48/12-consolidated text),

9. Decision on Determination of the Fee Tariff of the Banking Agency of the Federation of B&H (Official Gazette of the FB&H No. 48/12-consolidated text),
10. Decision on Minimum Standards for Banks' Activities on Prevention of Money Laundering and Terrorism Financing (Official Gazette of the FB&H No. 48/12) ,
11. Decision on Minimum Standards for Managing Liquidity Risk in Banks (Official Gazette of the FB&H No. 48/12-consolidated text and No. 110/12) ,
12. Decision on Minimum Standards for Managing Credit Risk and Assets Classification in Banks (Official Gazette of the FB&H No. 85/11-consolidated text and No. 33/12-correction and No. 15/13),
13. Decision on Conditions and Manner of Customer Complaints Management in Banks (Official Gazette of the FB&H No. 32/10),
14. Decision on Temporary Measures for Rescheduling of Credit Liabilities of Legal Entities and Private Individuals in Banks (Official Gazette of the FB&H Nos. 2/10, 86/10, 1/12 and 111/12 and 1/14),
15. Decision on Minimum Standards for Managing Operational Risk in Banks (Official Gazette of the FB&H Nos. 6/08 and 40/09),
16. Criteria for Internal Rating of Banks by the Banking Agency of the Federation of B&H (Official Gazette of the FB&H Nos. 3/03 and 6/03 correction),
17. Decision on Reporting on Non-performing Customers Considered to be of Special Credit Risk for Banks (Official Gazette of the FB&H No. 3/03),
18. Decision on Conditions when the Bank is Considered Insolvent (Official Gazette of the FB&H No. 3/03),
19. Decision on Minimum Standards for Documenting Lending Activities of Banks (Official Gazette of the FB&H No. 3/03),
20. Decision on Minimum Standards for Banks' Operations with Related Entities (Official Gazette of the FB&H No. 3/03),
21. Decision on Bank Supervision and Actions of the Banking Agency of the Federation of B&H (Official Gazette of the FB&H No. 3/03),
22. Decision on Minimum Standards for Internal and External Audit in Banks (Official Gazette of the FB&H No. 3/03),
23. Decision on the Process of Determination of Receivables and Allocation of Assets and Liabilities during the Liquidation Process (Official Gazette of the FB&H No. 3/03),
24. Decision on Minimum Standards of the Internal Controls System in Banks (Official Gazette of the FB&H No. 3/03),
25. Decision on Interest and Fee Calculation for Dormant Accounts (Official Gazette of the FB&H No. 7/03),
26. Decision on Level and Conditions for Loan Approval to Bank Employees (Official Gazette of the FB&H Nos. 7/03 and 83/08),
27. Decision on Property Statement (Official Gazette of the FB&H No. 3/03),
28. Decision on Minimum Standards for Managing Market Risks in Banks (Official Gazette of the FB&H Nos. 55/07, 81/07, 6/08, 52/08 and 79/09).
29. Decision on Temporary Restrictions and Minimum Requirements for Dividends and Discretionary Bonus Disbursement and Repurchase of Own Shares by Banks (Official Gazette of the FB&H No.15/13),
30. Instructions for Licensing and Other Approvals of the FB&H Banking Agency (Official Gazette of the FB&H No. 1/14 – consolidated text),
31. Instructions for Changed Manner of Forming, Recording and Reporting Loan Loss Provisions (12/2011, 01/2013),
32. Instructions on Manner of Provisional Administrator's Reporting on Operations of the Bank Placed under Provisional Administration (19.07.2013),
33. Instructions on Form and Manner of Additional Reporting of Banks Placed under Provisional Administration (19.07.2013),

34. Instructions on Manner of Liquidation Administrator's Reporting on the Bank Liquidation Process (19.07.2013),
35. Decision on Diligent Behavior of Members of Bank's Bodies (Official Gazette of the FB&H No. 60/13),
36. Decision on Suitability Assessment of Bank's Bodies (Official Gazette of the FB&H No. 60/13),
37. Decision on the Remuneration Policy and Practice for Bank Employees (Official Gazette of the FB&H No. 60/13),
38. Decision on Minimum Standards for Currency Exchange Operations (Official Gazette of the FB&H Nos. 95/13 and 99/13),
39. Decision on Minimum Standards for Examination of Currency Exchange Operations (Official Gazette of the FB&H No. 95/13),
40. Decision on Conditions and Manner of Executing International Payments (Official Gazette of the FB&H No. 95/13),
41. Decision on Examination of Foreign Currency Operations in Banks – Payment Transactions (Official Gazette of the FB&H No. 95/13).

Decisions and Instructions of the Banking Agency related to operations of micro credit organisations

1. Decision on Conditions and Process of Issuance and Revocation of Operating License and Other Approvals to/from Micro Credit Organisations (Official Gazette of the FB&H Nos. 27/07 and 46/11),
2. Decision on Conditions and Process of Issuance of Operating License and Other Approvals for Acquiring Ownership Share by Investing and Transferring Assets of the Micro Credit Foundation (Official Gazette of the FB&H No. 27/07),
3. Decision on Conditions and Process of Issuance of Operating License and Other Approvals for Micro Credit Foundation Resulting from Changed Organisational form of a micro credit organisation (Official Gazette of the FB&H No. 27/07),
4. Decision on Supervision of Micro Credit Organisations (Official Gazette of the FB&H No. 27/07),
5. Decision on Form and Contents of Reports that Micro Credit Organisations Deliver to the Banking Agency of the FB&H and on Reporting Deadlines (Official Gazette of the FB&H Nos. 27/07 and 110/12 and 15/13),
6. Decision on Level and Manner of Forming and Maintaining Reserves for Loan Losses of Micro Credit Organisations (Official Gazette of the FB&H No. 27/07),
7. Decision on Other General Conditions for Operations of Micro Credit Organisations (Official Gazette of the FB&H No. 27/07),
8. Decision on Uniform Manner of Calculation and Disclosure of Interest Rate on Loans and Deposits (Official Gazette of the FB&H Nos. 27/07, 46/09 , 46/11, 48/12-consolidated text),
9. Decision on Conditions and Manner of Customer Complaints Management by Micro Credit Organisations (Official Gazette of the FB&H No. 32/10),
10. Decision on Fees that Micro Credit Organisations Pay to the FB&H Banking Agency (Official Gazette of the FB&H No. 46/11),
11. Decision on Minimum Standards for Activities of Micro Credit Organisation on Prevention of Money Laundering and Terrorism Financing (Official Gazette of the FB&H No. 48/12),
12. Instructions for Calculation of Weighted and Effective Interest Rate,
13. Instructions for Calculation of Adjusted Return on Assets,
14. Instructions for Calculation of Efficiency Ratios
15. Instructions for MCO Reporting.

Decisions of the Banking Agency related to operations of leasing companies

1. Decision on Form and Contents of Reports that Leasing Companies Deliver to the FB&H Banking Agency and on Reporting Deadlines (Official Gazette of the FB&H Nos. 46/09, 48/12 and 110/12),
2. Decision on Conditions and Process of Issuance of Operating License to Leasing Companies (Official Gazette of the FB&H No. 46/09),
3. Decision on Conditions and Process of Issuance and Revocation of Approvals to/from Leasing Companies (Official Gazette of the FB&H Nos. 46/09 and 46/11),
4. Decision on Uniform Manner and Method of Calculation and Disclosure of Effective Interest Rates for Financial Leasing Agreements (Official Gazette of the FB&H No. 46/09),
5. Decision on Uniform Manner and Method of Calculation and Disclosure of Leasing Fees under the Operational Leasing Agreement (Official Gazette of the FB&H No. 46/09 and 48/12),
6. Decision on Minimum Level and Manner of Forming, Managing and Maintaining Loss Reserves and Risk Management in Leasing Companies (Official Gazette of the FB&H No. 46/09),
7. Decision on Supervision of Leasing Companies (Official Gazette of the FB&H No. 46/09),
8. Decision on Fees that Leasing Companies Pay to the FB&H Banking Agency (Official Gazette of the FB&H Nos. 46/09 and 46/11),
9. Decision on Conditions and Manner of Customer Complaints Management by Leasing Companies (Official Gazette of the FB&H No. 48/12),
10. Decision on Minimum Standards for Activities of Leasing Companies on Prevention of Money Laundering and Terrorism Financing (Official Gazette of the FB&H No. 48/12),
11. Instruction on Reporting by Leasing Companies (31.01.2013).

Other regulations:

Development Bank of the FB&H

1. Decree on Criteria and Manner of Supervision of the FB&H Development Bank (Official Gazette of the FB&H Nos. 57/08, 77/08 and 62/10),
2. Decision on Determination of Supervision Fee for the FB&H Development Bank (Official Gazette of the FB&H No. 65/09).

Foreign currency operations

1. Rulebook on the Process of Opening and Maintaining FC Accounts and FC Savings of Resident Customers of Banks (Official Gazette of the FB&H No. 56/10),
2. Rulebook on Conditions and Manner for Opening, Maintaining and Closing of Non-resident Accounts in Banks (Official Gazette of the FB&H No. 56/10),
3. Rulebook on Manner, Deadlines and Forms of Reporting on International Lending Business (Official Gazette of the FB&H No. 79/10),
4. Decision on Withdrawing of Foreign Cash and Cheques (Official Gazette of the FB&H No. 58/10),
5. Decision on Conditions and Manner of Conducting Foreign Exchange Operations (Official Gazette of the FB&H Nos. 58/10 and 49/11),

6. Decision on Conditions for Issuing Approvals for Opening FC Accounts Abroad (Official Gazette of the FB&H No. 58/10),
7. Decision on Payment, Collection and Transfer of Foreign Currency and Foreign Cash (Official Gazette of the FB&H No. 58/10),
8. Decision on Manner and Conditions for Residents to Receive or Perform Payment in FCY and LCY cash in their operations with Non-residents (Official Gazette of the FB&H No. 58/10),
9. Instructions for the Structure and Use of the International Bank Number (IBAN) (Official Gazette of the FB&H No. 4//07).

Anti-money Laundering

1. Rulebook on Risk Assessment, Information, Data, Documentation, Identification Methods and Other Minimum Indicators for an Efficient Implementation of the Law on Prevention of Money Laundering and Terrorism Financing (Official Gazette of B&H No. 93/09),
2. Instructions for Manner of Populating Forms and Electronic Data Entry for Reporting Cash Transactions by the Payer (Official Gazette of B&H No. 22/11).

III. OTHER LAWS AND REGULATIONS IN THE FB&H

1. Law on Obligations (Official Gazette of the RB&H Nos. 2/92, 13/93 and 13/94, Official Gazette of the FB&H Nos. 29/03 and 42/11),
2. Law on Payment Transactions (Official Gazette of the FB&H Nos. 32/00 and 28/03),
   - 2.1. Instructions on Manner in which Banks Report to Customers – Treasuries and Non-Budget Funds (Official Gazette of the FB&H Nos. 55/00 and 2/01),
   - 2.2. Instructions on Form and Contents of Payment Orders and Procedures for Performing Payment Transactions (Official Gazette of the FB&H Nos. 55/00, 2/01, 45/02, 7/04 and 11/04),
   - 2.3. Instructions on Opening and Closing of Transaction Accounts and Recording Keeping (Official Gazette of the FB&H Nos. 55/00, 61/05 and 62/11),
   - 2.4. Instructions on Banks' Obligations regarding Domestic Transaction Account Opening (Official Gazette of the FB&H Nos. 56/00, 9/01, 28/01 and 46/03),
   - 2.5. Instructions for Establishment of Unified Registry of Account Holders in Commercial Banks and Contents and Manner of Keeping the Account Registry in the Federation of B&H (Official Gazette of the FB&H No. 14/01),
   - 2.6. Instructions on the Structure of Transaction Accounts (Official Gazette of the FB&H No. 52/00),
   - 2.7. Instructions for Manner of Payment to and from Blocked Accounts maintained with the FB&H Payments Bureau (Official Gazette of the FB&H No. 2/01 and 46/03),
3. Law rendering ineffective the Law on Domestic Payments (Official Gazette of the FB&H No. 56/04),
4. Law on Cheques (Official Gazette of the FB&H No. 32/00),
5. Law on Promissory Notes (Official Gazette of the FB&H Nos. 32/00 and 28/03),
6. Law on Default Interest Rate Level (Official Gazette of the FB&H Nos. 27/98 and 51/01, 28/13),
7. Law on Level of Default Interest on Unsettled Debts (Official Gazette of the FB&H Nos. 56/04, 68/04, 29/05 and 48/11, 28/13),
8. Law on the Default Interest Level for Public Revenues (Official Gazette of the FB&H Nos. 48/01, 52/01 and 42/06),
9. Company Law (Official Gazette of the FB&H Nos. 23/99, 45/00, 2/02, 6/02, 29/03, 68/05, 91/07, 84/08, 88/8-correction, 7/09-correction and 63/10, 75/13),
10. Stock Companies Take-Over Law (Official Gazette of the FB&H No. 7/06),

11. Law on Registration of Legal Entities in the FB&H (Official Gazette of the FB&H Nos. 27/05, 68/05 and 43/09),
12. Law on Public Sector Companies (Official Gazette of the FB&H Nos. 8/05, 81/08, 22/09 and 109/12),
13. Liquidation Proceedings Law (Official Gazette of the FB&H No. 29/03),
14. Bankruptcy Law (Official Gazette of the FB&H Nos. 29/03, 32/04 and 42/06),
15. FB&H Law on Debt, Debt Raising and Guarantees (Official Gazette of the FB&H Nos. 86/07, 24/09 and 44/10) ,
    - 15.1. Rulebook on Foreign Debt Recording in the FB&H (Official Gazette of the FB&H No. 14/08),
    - 15.2. Rulebook on Required Documentation for Prior Approvals to the Canton, Municipality or City for Debt Raising and Issuance of Guarantees based on Domestic Debt (Official Gazette of the FB&H No. 14/08),
    - 15.3. Rulebook on Accompanying Documents and Information relevant for the Decision-Making on Issuance of FB&H Guarantee and Percentage of Premium and Fee for Guarantee Issuance (Official Gazette of the FB&H No. 14/08),
    - 15.4. Rulebook on Recording of Guarantees in the FB&H (Official Gazette of the FB&H No. 14/08),
    - 15.5. Decision on Conditions and Procedure for Issuing FB&H Bonds (Official Gazette of the FB&H No. 31/12),
    - 15.6. Decision on Conditions and Procedures for Issue of FB&H Treasury Bills (Official Gazette of the FB&H No. 88/12),
16. Law on Accounting and Audit in the FB&H (Official Gazette of the FB&H No. 83/09),
17. FB&H Business Classification Law (Official Gazette of the FB&H Nos. 64/07 and 80/11),
18. Law on Classification of Professions in the FB&H (Official Gazette of the FB&H No. 111/12),
    - 18.1. Decision on Standard Classification of professions in the FB&H (Official Gazette of the FB&H Nos. 40/04, 26/09 and 40/09),
19. Law on Securities' Market (Official Gazette of the FB&H Nos. 85/08 and 109/12),
20. Law on the Securities Register (Official Gazette of the FB&H Nos. 39/98, 36/99 and 33/04),
21. Law on the Securities Commission (Official Gazette of the FB&H Nos. 39/98, 36/99 and 33/04),
22. Labor Law (Official Gazette of the FB&H Nos. 43/99, 32/00 and 29/03),
23. Law on the Employees' Council (Official Gazette of the FB&H No. 38/04),
24. Law on Employment of Foreign Citizens (Official Gazette of the FB&H No. 111/12),
25. Law on Investment Funds (Official Gazette of the FB&H No. 85/08),
26. Law on Fund Management Companies and Investment Funds (Official Gazette of the FB&H Nos. 41/98, 36/99, 36/00, 27/02, 44/02, 50/03 and 70/04) ,
27. Law on Private Insurance Companies (Official Gazette of the FB&H Nos. 24/05 and 36/10) ,
28. Law on Private Insurance Agency (Official Gazette of the FB&H Nos. 22/05 and 8/10),
29. Law on the FB&H Tax Authority (Official Gazette of the FB&H Nos. 33/02, 28/04, 57/09, 40/10, 29/11 and 27/12, 7/13),
30. Law on Profit Tax (Official Gazette of the FB&H Nos. 97/07, 14/08-correction and 39/09),
31. Law on Personal Income Tax (Official Gazette of the FB&H Nos. 10/08, 9/10 and 44/11, 7/13, 65/13),
32. Law on Contributions (Official Gazette of the FB&H Nos. 35/98, 54/00, 16/01, 37/01, 1/02, 17/06 and 14/08),
33. Law on Collection and Partial Write off of Overdue Social Insurance Contributions (Official Gazette of the FB&H Nos. 25/06 and 57/09),

34. Law on Unified System of Registration of Control and Collection of Contributions (Official Gazette of the FB&H Nos. 42/09 and 109/12),
35. Law on Opening Balance Sheet of Companies and Banks (Official Gazette of the FB&H Nos. 12/98, 40/99, 47/06, 38/08 and 65/09),
36. Law on Audit of Privatisation of State-owned Capital in Companies and Banks (Official Gazette of the FB&H No. 55/12),
37. Law on Identifying and Realising Claims of Citizens in the Privatisation Process (Official Gazette of the FB&H Nos. 27/97, 8/99, 45/00, 54/00, 7/01, 32/01, 27/02, 57/03, 44/04, 79/07, 65/09, 48/11 and 111/12),
38. Law on Identification and Manner of Settlement of Domestic Debt of FB&H (Official Gazette of the FB&H Nos. 66/04, 49/05, 5/06, 35/06, 31/08, 32/09, 65/09 and 42/11, 91/13),
39. Law on Settlement of Liabilities based on Pre-War FC Savings in the FB&H (Official Gazette of the FB&H Nos. 62/09 and 42/11, 91/13),
40. Law on Associations and Foundations (Official Gazette of the FB&H No. 45/02),
41. Law on Trade and Related Businesses (Official Gazette of the FB&H Nos. 35/09 and 42/11),
42. Expropriation Law (Official Gazette of the FB&H Nos. 70/07, 36/10 and 25/12),
43. Law rendering ineffective the Law on Construction (Official Gazette of the FB&H Nos. 55/02, 34/07),
44. Law on Construction Land in the FB&H (Official Gazette of the FB&H No. 67/05),
45. Law on Temporary Restriction over Disposing with State Property in the FB&H (Official Gazette of the FB&H Nos. 20/05, 17/06, 62/06, 40/07, 70/07, 94/07 and 41/08),
46. Law on Free Access to Information in the FB&H (Official Gazette of the FB&H Nos. 32/01 and 48/11),
47. FB&H Regulatory Offence Law (Official Gazette of the FB&H Nos. 31/06 and 37/10-correction),
48. Law on Public Notaries (Official Gazette of the FB&H No. 45/02),
49. Law on Court Appraisers (Official Gazette of the FB&H Nos. 49/05 and 38/08),
50. Law on Property Rights (Official Gazette of the FB&H Nos. 06/9 and 29/03, 66/13),
51. Law on Agencies and Internal Departments for Personal and Property Protection (Official Gazette of the FB&H Nos. 78/08, 67/13),
52. Law on Land Books in the FB&H (Official Gazette of the FB&H Nos. 58/02, 19/03 and 54/04),
53. Foreign Investments Law (Official Gazette of the FB&H Nos. 61/01 and 50/03),
54. Mediation Law (Official Gazette of the FB&H No. 49/07),
55. Law on FB&H Treasury (Official Gazette of the FB&H Nos. 58/02, 19/03 and 79/07),
56. Law on the FB&H Government (Official Gazette of the FB&H Nos. 1/94, 8/95, 58/02, 19/03, 2/06 and 8/06),
57. Law on the FB&H Prosecutor's Office (Official Gazette of the FB&H Nos. 42/02 and 19/03),
58. Law on FB&H Courts (Official Gazette of the FB&H Nos. 38/05, 22/06, 63/10 and 72/10-correction),
59. Law on Enforcement Proceedings (Official Gazette of the FB&H Nos. 32/03, 52/03, 33/06, 39/06- correction., 39/09, 74/11 and 35/12),
60. Law on Temporary Postponment of Fulfillment of Receivables based on Executive Decisions Issued in relation to the FB&H Budget (Official Gazette of the FB&H Nos. 9/04 and 30/04),
61. Law on Administrative Proceedings (Official Gazette of the FB&H Nos. 2/98 and 48/99),
62. Law on Administrative Disputes (Official Gazette of the FB&H No. 9/05),
63. Law on Civil Proceedings (Official Gazette of the FB&H Nos. 53/03, 73/05 and 19/06),

64. Law on Non-civil Proceedings (Official Gazette of the FB&H Nos. 2/98, 39/04 and 73/05),
65. FB&H Criminal Code (Official Gazette of the FB&H Nos. 36/03, 37/03, 21/04, 69/04, 18/05, 42/10 and 42/11),
66. Law on Criminal Proceedings in the FB&H (Official Gazette of the FB&H Nos. 35/03, 37/03, 56/03, 78/04, 28/05, 55/06, 27/07, 53/07, 9/09 and 12/10, 8/13),
67. FB&H Regulatory Offence Law (Official Gazette of the FB&H Nos. 44/98, 42/99, 12/09 and 42/11),
68. Law on Conflict of Interest in FB&H Government Bodies (Official Gazette of the FB&H No. 70/08),
69. Law on Financial-Information Agency (Official Gazette of the FB&H No. 80/11),
70. Law on Fiscal Systems (Official Gazette of the FB&H No. 81/09),
71. Law on Privatisation of Banks (Official Gazette of the FB&H Nos. 12/98, 29/00, 37/01 and 33/02),
72. Law on Archive Materials of the FB&H (Official Gazette of the FB&H No. 45/02),
    72.1. Decree of Organisation and Manner of Archiving by Legal Entities in the FB&H (Official Gazette of the FB&H Nos. 12/03, 22/03),
73. Law on Recognition of Public Identification Documents in the FB&H Territory (Official Gazette of the FB&H No. 4/98),
74. Law on Strike (Official Gazette of the FB&H No. 14/00),
75. Collective Employment Agreement for the Financial Sector (Official Gazette of the FB&H No. 48/00),
76. Law on Protection of Guarantors in the FB&H (Official Gazette of the FB&H No. 100/13),
77. Property Law (Official Gazette of the FB&H Nos. 66/13 and 100/13),
78. Law on FB&H Budgets (Official Gazette of the FB&H No. 102/13).

IV. OTHER LAWS AND REGULATIONS IN B&H

1. Law on the Central Bank of B&H (Official Gazette of B&H Nos. 1/97, 29/02, 8/03, 13/03, 14/03, 9/05, 76/06 and 32/07),
2. Law on Consumer Protection in B&H (Official Gazette of B&H No. 25/06),
3. Law on B&H Market Supervision (Official Gazette of B&H Nos. 45/04, 44/07 and 102/09),
4. Competition Law (Official Gazette of B&H Nos. 48/05, 76/07 and 80/09),
5. Law on Direct Foreign Investment Policy in B&H (Official Gazette of B&H Nos. 4/98, 17/98, 13/03, and 48/10),
6. Law on Protection of Personal Data (Official Gazette of B&H Nos. 49/06, 76/11 and 89/11-correction),
7. Law on Protection of Data Secrecy (Official Gazette of B&H Nos. 54/05 and 12/09),
8. Law on Electronic Signature (Official Gazette of B&H No. 91/06),
    a. Decision on Use of Electronic Signature and Documents Certification Services (Official Gazette of B&H No. 21/09),
9. Business Classification Law in B&H (Official Gazette of B&H Nos. 76/06, 100/08 and 32/10),
10. B&H Law on Debt, Debt Raising and Guarantees (Official Gazette of B&H Nos. 52/05 and 103/09),
    a. Decision Approving Issuance of State Guarantees (Official Gazette of B&H No. 85/10),
11. Law on Settlement of Liabilities based on Pre-War FC Savings (Official Gazette of B&H Nos. 28/06, 76/06, 72/07 and 97/11, 100/13),
12. Law on Accounting and Audit in B&H (Official Gazette of B&H No. 42/04),

13. Law on Determination and Manner of Settlement of Domestic Debt in B&H (Official Gazette of B&H No. 44/04),
14. Framework Law on Pledges (Official Gazette of B&H Nos. 28/04 and 54/04),
15. Law on Value Added Tax (Official Gazette of B&H Nos. 9/05, 35/05 and 100/08),
16. Law on Public Procurements in B&H (Official Gazette of B&H Nos. 49/04, 19/05, 52/05, 94/05, 8/06, 24/06, 70/06, 12/09 and 60/10, 87/13),
17. Law on Customs Duties (Official Gazette of B&H No. 58/12),
18. Law on Customs Violations in B&H (Official Gazette of B&H No. 88/05),
19. Patent Law (Official Gazette of B&H No. 53/10),
20. Law on Free Access to Information in B&H (Official Gazette of B&H Nos. 28/00, 45/06, 102/09 and 62/11, 100/13),
21. Law on the national identification number (Official Gazette of B&H Nos. 32/01, 63/08 and 103/11),
22. Law on Associations and Foundations in B&H (Official Gazette of B&H Nos. 32/01, 42/03, 63/08 and 76/11),
23. Law on Temporary Restriction over Disposing with State-owned Property in B&H (Official Gazette of B&H Nos. 18/05, 29/06, 85/06, 32/07, 41/07, 74/07, 99/07 and 58/08),
24. Law on Use and Protection of the Name of B&H (Official Gazette of B&H Nos. 30/03, 42/04, 50/08 and 76/11),
25. Law on Fiscal Council of B&H (Official Gazette of B&H No. 63/08),
26. Law on the Treasury of the B&H Institutions (Official Gazette of B&H Nos. 27/00 and 50/08),
27. Mediation Law (Official Gazette of B&H No. 37/04),
28. Law on Transfer of Mediation Business to the Association of Mediators (Official Gazette of B&H No. 52/05),
29. Law on Enforced Collection of Indirect Taxes (Official Gazette of B&H Nos. 89/05 and 62/11),
30. Regulatory Offence Law (Official Gazette of B&H Nos. 41/07 and 18/12),
31. Law on B&H Courts (Official Gazette of B&H Nos. 49/09-consolidated text, 74/09-correction and 97/09),
32. Law on the High Judicial and Prosecutorial Council of B&H (Official Gazette of B&H Nos. 35/02, 39/03, 42/03, 10/04, 25/04, 93/05, 32/07 and 48/07),
33. Law on the B&H Prosecutor's Office (Official Gazette of B&H Nos. 49/09-consolidated text and 97/09),
34. Law on Administrative Proceedings (Official Gazette of B&H Nos. 29/02, 12/04, 88/07 and 93/09, 41/13),
35. Law on Administrative Disputes in B&H (Official Gazette of B&H Nos. 19/02, 88/07, 83/08 and 74/10),
36. Law on Civil Proceedings before the B&H Court (Official Gazette of B&H Nos. 36/04 and 84/07, 58/13),
37. Law on Enforcement Proceedings before the B&H Court (Official Gazette of B&H No. 18/03),
38. Law on Temporary Postponement of Fulfillment of Receivables based on Executive Decisions against the Budget of B&H Institutions and International Obligations of B&H (Official Gazette of B&H Nos. 43/03 and 43/04),
39. B&H Criminal Code (Official Gazette of B&H Nos. 3/03, 32/03, 37/03, 54/04, 61/04, 30/05, 53/06, 55/06, 32/07 and 8/10),
40. Law on Criminal Proceedings in B&H (Official Gazette of B&H Nos. 3/03, 32/03, 36/03, 26/04, 63/04, 13/05, 48/05, 46/06, 76/06, 29/07, 32/07, 53/07, 76/07, 15/08, 58/08, 12/09, 16/09 and 93/09, 72/13),
41. Law on Conflict of Interest in B&H Government Bodies (Official Gazette of B&H Nos. 13/02, 16/02, 14/03, 12/04, 63/08 and 18/12, 87/13),

42. Law on Archive Materials and Archives of B&H (Official Gazette of B&H No. 16/01).

ATTACHMENT 3

BALANCE SHEET OF BANKS IN THE FB&H ACCORDING TO THE FBA MODEL – ASSETS SIDE

in 000 KM

No.	DESCRIPTION	31.12.2011	31.12.2012	31.12.2013
	ASSETS			
1.	Cash and deposit accounts with deposit-taking institutions	4.378.076	3.962.581	4.417.898
1a	Cash and non-interest bearing deposit accounts	528.721	625.188	627.016
1b	Interest-bearing deposit accounts	3.849.355	3.337.393	3.790.882
2.	Trading securities	300.228	375.032	381.909
3.	Facilities to other banks	79.940	78.522	51.960
4.	Loans, receivables based on leasing facilities and past due receivables	10.487.671	10.666.124	10.852.400
4a	Loans	9.524.844	9.591.819	9.676.527
4b	Receivables based on leasing facilities	120	54	48
4c	Past due receivables based on loans and leasing facilities	962.707	1.074.251	1.175.825
5.	Held to maturity securities	158.237	173.435	180.604
6.	Business premises and other fixed assets	503.802	491.370	476.199
7.	Other real estate	36.947	30.123	36.786
8.	Investments in unconsolidated related companies	42.186	24.756	23.762
9.	other assets	281.891	255.247	251.863
10.	LESS: value adjustment	1.005.659	1.066.424	1.224.677
10a	Value adjustments for Item 4. of the Assets	931.946	1.007.459	1.163.530
10b	Value adjustments for Assets items, except for the Item 4	73.713	58.965	61.147
11.	**TOTAL ASSETS**	**15.263.319**	**14.990.766**	**15.448.704**
	LIABILITIES			
12.	Deposits	11.124.675	10.961.001	11.523.849
12a	Interest-bearing deposits	10.128.147	9.281.938	9.363.284
12b	Non-interest bearing deposits	996.528	1.679.063	2.160.565
13.	Borrowings - liabilities due	1.762	1.752	1.577
13a	Past due liabilities			
13b	Past due - invoked off-balance sheet liabilities	1.762	1.752	1.577
14.	Borrowings from other banks	2.000	2.000	
15.	Liabilities to the Government			
16.	Loan obligations and other borrowings	1.319.299	1.141.561	1.039.381
16a	with remaining maturity of up to one year	387.585	244.160	212.485
16b	with remaining maturity of over one year	931.714	897.401	826.896
17.	Subordinated debt and subordinated bonds	206.159	186.675	166.889
18.	Other liabilities	529.359	480.402	406.621
19.	**TOTAL LIABILITIES**	**13.183.254**	**12.773.391**	**13.138.317**
	EQUITY			
20.	Permanent preferred shares	26.059	26.059	11.959
21.	Common shares	1.167.513	1.175.547	1.196.633
22.	Issue premiums	136.485	136.485	136.485
22a	over permanent preferred shares	8.420	8.420	8.420
22b	over common shares	128.065	128.065	128.065
23.	Undistributed profit and capital reserves	376.102	453.269	649.879
24.	foreign exchange rate differences			
25.	Other capital	81.681	110.281	-303
26.	Loan loss provisions formed against profit	292.225	315.734	315.734
27.	**EQUITY (20 to 25)**	**2.080.065**	**2.217.375**	**2.310.387**
28.	**LIABILITIES AND EQUITY (19 +26)**	**15.263.319**	**14.990.766**	**15.448.704**
	LIABILITIES AND NEUTRAL ITEMS	**671.241**	**661.321**	**638.913**
	BALANCE SHEET TOTAL OF BANKS	**15.934.560**	**15.652.087**	**16.087.617**

ATTACHMENT 4

OVERVIEW OF ASSETS, LOANS, DEPOSITS AND FINANCIAL RESULTS OF BANKS IN THE FB&H as of 31.12.2013

in 000 KM

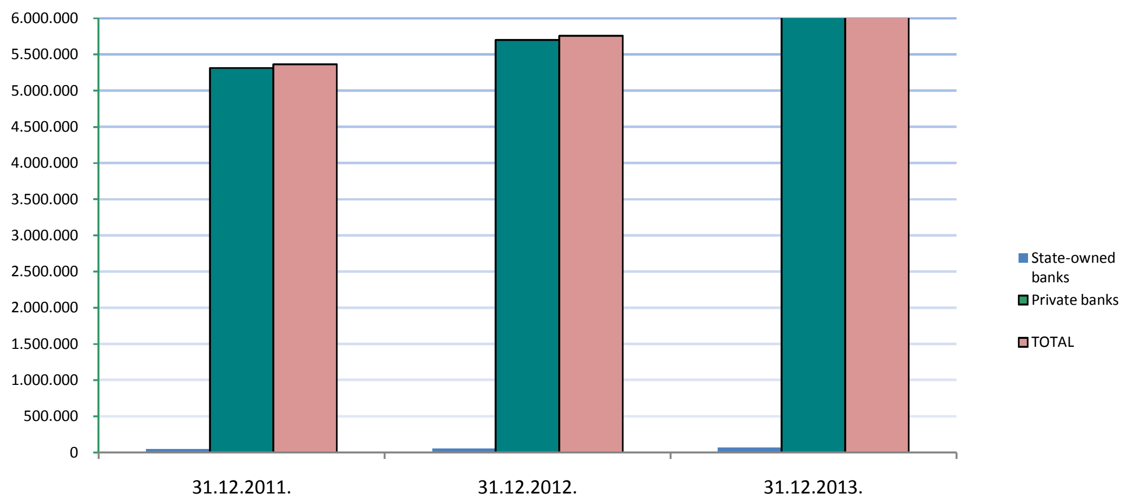
No.	BANK	Assets		Loans		Deposits		Financial result
		Amount	%	Amount	%	Amount	%	Amount
1	BOR BANKA dd SARAJEVO	246.051	1,6%	183.923	1,7%	133.254	1,2%	653
2	BBI BANKA dd SARAJEVO	563.297	3,6%	345.739	3,2%	391.117	3,4%	2.972
3	HYPO ALPE-ADRIA-BANK dd MOSTAR	1.221.519	7,9%	838.382	7,7%	848.461	7,4%	-116.142
4	INTESA SANPAOLO BANKA D.D. BOSNA I HERCEGOVINA	1.333.194	8,6%	1.114.492	10,3%	887.260	7,7%	13.429
5	INVESTICIONO-KOMERCIJALNA BANKA dd - ZENICA	186.545	1,2%	89.206	0,8%	131.468	1,1%	2.045
6	KOMERCIJALNO INVESTICIONA BANKA dd VELIKA KLADUŠA	72.761	0,5%	40.062	0,4%	46.972	0,4%	1.193
7	MOJA BANKA dd SARAJEVO	198.323	1,3%	137.352	1,3%	158.556	1,4%	220
8	NLB TUZLANSKA BANKA dd TUZLA	803.560	5,2%	621.282	5,7%	631.256	5,5%	4.262
9	PRIVREDNA BANKA dd SARAJEVO	160.732	1,0%	128.550	1,2%	130.044	1,1%	-18.950
10	PROCREDIT BANK dd SARAJEVO	362.473	2,3%	303.547	2,8%	246.144	2,1%	1.106
11	RAIFFEISEN BANK BH dd SARAJEVO	3.800.453	24,6%	2.372.660	21,9%	2.952.683	25,6%	42.505
12	SBERBANK BH dd - SARAJEVO	862.806	5,6%	697.101	6,4%	658.718	5,7%	2.725
13	SPARKASSE BANK dd - SARAJEVO	965.548	6,3%	805.878	7,4%	813.353	7,1%	8.725
14	UNION BANKA dd - SARAJEVO	241.605	1,6%	118.364	1,1%	184.675	1,6%	462
15	UNICREDIT BANKA dd - MOSTAR	3.745.178	24,2%	2.585.081	23,8%	2.848.070	24,7%	55.571
16	VAKUFSKA BANKA dd - SARAJEVO	285.126	1,8%	191.064	1,8%	229.127	2,0%	-5.238
17	ZIRAATBANK BH dd - SARAJEVO	399.533	2,6%	279.717	2,6%	232.691	2,0%	4.234
	TOTAL	**15.448.704**	**100,0%**	**10.852.400**	**100,0%**	**11.523.849**	**100,0%**	**-228**

ATTACHMENT 5

NEW RETAIL SAVINGS IN THE FB&H BANKS

in 000 KM

	31.12.2011	31.12.2012	31.12.2013
State-owned banks	50.259	58.050	65.179
Private banks	5.311.178	5.698.300	6.135.711
TOTAL	**5.361.437**	**5.756.350**	**6.200.890**



ATTACHMENT 6

CLASSIFICATION OF BALANCE SHEET ASSETS AND OFF-BALANCE SHEET RISK-BEARING ITEMS as of 31.12.2013

- CLASSIFICATION OF BALANCE SHEET ASSETS ITEMS -

in 000 KM

No.	BALANCE SHEET ASSETS ITEMS	CLASSIFICATION					TOTAL
		A	B	C	D	E	
1.	Short term loans	2.072.467	252.948	26.720	6.814	1.883	2.360.832
2.	Long term loans	6.223.898	572.880	262.288	166.647	13.726	7.239.439
3.	Other facilities	196.946	2.697	59	472	1.612	201.786
4.	Accrued interest and fees	37.241	4.862	3.378	8.420	27.555	81.456
5.	Past due receivables	39.979	27.049	53.547	315.711	707.756	1.144.042
6.	Receivables based on paid guarantees	67		397	342	30.977	31.783
7.	Other balance sheet assets being classified	257.855	4.240	5.446	1.909	25.173	294.623
8.	**TOTAL BALANCE SHEET ASSETS BEING CLASSIFIED (sum of items 1 through 7 – calculation basis for regulatory loan loss provisions)**	**8.828.453**	**864.676**	**351.835**	**500.315**	**808.682**	**11.353.961**
9.	**CALCULATED REGULATORY RESERVES FOR LOAN LOSSES BASED ON BS ASSETS**	**172.493**	**79.317**	**89.502**	**293.822**	**808.406**	**1.443.540**
10.	**VALUE ADJUSTMENT FOR BS ASSETS**	**116.660**	**74.845**	**111.452**	**221.471**	**700.248**	**1.224.676**
11.	**REQUIRED REGULATORY RESERVES FORMED AGAINST PROFIT FOR PURPOSE OF ASSESSED LOSSES BASED ON BS ASSETS**	**96.277**	**42.368**	**24.265**	**103.698**	**109.006**	**375.614**
12.	**FORMEED REGULATORY RESERVES FORMED AGAINST PROFIT RELATED TO ASSESSED LOSSES BASED ON BS ASSETS**	**79.660**	**30.719**	**23.019**	**84.390**	**61.315**	**279.103**
13.	**SHORTFALL OF REGULATORY RESERVE FORMED AGAINST PROFIT RELATED TO ASSESSED LOSSES BASED ON BS ASSETS**						**155.363**
14.	**BALANCE SHEET ASSETS NOT BEING CLASSIFIED (gross book value)**						**5.319.420**
15.	**TOTAL BALANCE SHEET ASSETS (gross book value)**						**16.673.381**

OVERVIEW OF BALANCE SHEET ASSETS NOT BEING CLASSIFIED AND FACILITIES SECURED WITH A CASH DEPOSIT

14.a	Cash in cash desk and vault and cash funds at the account with the Central Bank of B&H, gold and other precious metals	3.054.218
14.b	Demand deposits and term deposits up to one month located on accounts of banks with defined investment rating	1.274.497
14.c	Tangible and intangible assets	494.422
14.d	Financial and tangible assets acquired in the process of collection of receivables (within one yearupon such acquisition)	9.485
14.e	Own (treasury) shares	
14.f	Receivables based on overpaid taxes	14.260
14.g	Trading securities	134.414
14.h	Receivables from the B&H Government, FB&H Government and RS Government, securities issued by the B&H Government, FB&H Government and RS Government and receivables secured with unconditional guarantees payable upon the first call	338.124
	TOTAL Item 14	**5.319.420**
8a.	Facilities secured with a cash deposit	203.827

ATTACHMENT 6A

CLASSIFICATION OF BALANCE SHEET ASSETS AND OFF-BALANCE SHEET RISK-BEARING ITEMS as of 31.12.2013

- CLASSIFICATION OF OFF-BALANCE SHEET ITEMS -

in 000 KM

No.	OFF-BALANCE SHEET ITEMS	CLASSIFICATION					TOTAL
		A	B	C	D	E	
1.	Payment guarantees	351.161	47.545	942	471		400.119
2.	Performance guarantees	499.514	89.170	1.374	1.211	275	591.544
3.	Uncovered letters of credit	44.176	6.638	531			51.345
4.	Irrevocably approved, but undrawn loans	1.294.662	86.045	1.964	805	979	1.384.455
5.	Other contingent liabilities of the bank	10.565	287		1	119	10.972
6.	**TOTAL OFF-BALANCE SHEDET ITEMS BEING CLASSIFIED (sum of items 1 through 5 – calculation basis for regulatory loan loss provisions)**	**2.200.078**	**229.685**	**4.811**	**2.488**	**1.373**	**2.438.435**
7.	**CALCULATED REGULATORY RESERVES FOR LOAN LOSSES RELATED TO OFF-BALANCE SHEET ITEMS**	**42.590**	**14.230**	**1.039**	**1.402**	**1.373**	**60.634**
8.	**LOSS RESERVES FOR OFF-BALANCE SHEET ITEMS**	**20.146**	**4.256**	**1.406**	**955**	**1.025**	**27.788**
9.	**REQUIRED REGULATORY RESERVES FORMED AGAINST PROFIT RELATED TO ASSESSED LOSSED BASED ON OFF.BAL.SHEET ITEMS**	**25.439**	**10.801**	**493**	**816**	**345**	**37.894**
10.	**FORMED REGULATORY RESERVES FORMED AGAINST PROFIT RELATED TO ASSESSED LOSSED BASED ON OFF.BAL.SHEET ITEMS**	**23.313**	**10.837**	**737**	**1.345**	**399**	**36.631**
11.	**SHORTFALL OF REGULATORY RESERVES FORMED AGAINST PROFIT RELATED TO ASSESSED LOSSED BASED ON OFF.BAL.SHEET ITEMS**						**4.980**
12.	**OFF-BALANCE SHEET ITEMS NOT BEING CLASSIFIED**						**550.961**
13.	**TOTAL OFF-BALANCE SHEET ITEMS**						**2.989.396**
6a.	**Contingent liabilities secured with a cash deposit**						**70.625**

ATTACHMENT 7

INCOME STATEMENT OF BANKS IN THE FB&H ACCORDINF TO THE FBA MODEL

in 000 KM

No.		DESCRIPTION	31.12.2011	31.12.2012	31.12.2013
1.		**INTEREST INCOME AND EXPENSES**			
	a)	Interest income and similar income			
	1)	Interest-bearing deposit accounts with deposit-taking institutions	23.545	3.991	2.461
	2)	Loans to other banks	5.529	3.436	1.964
	3)	Loans and leasing facilities	769.774	729.602	703.462
	4)	Held to maturity securities	5.663	6.564	7.496
	5)	Equity securities	909	186	153
	6)	Receivables based on paid off-balance sheet liabilities		0	0
	7)	Other interest and similar income	61.264	65.645	65.509
	8)	**TOTAL INTEREST INCOME AND SIMILAR INCOME**	**866.684**	**809.424**	**781.045**
	b)	Interest expenses and similar expenses			
	1)	Deposits	230.224	218.614	205.187
	2)	Borrowing from other banks	4	276	436
	3)	Borrowing taken – liabilities due	0	0	0
	4)	Liabilities based on loans and other borrowings	47.831	36.520	21.253
	5)	Subordinated debt and subordinated bonds	12.086	10.997	10.050
	6)	Other interest and similar expenses	4.412	3.362	2.376
	7)	**TOTAL INTEREST EXPENSES AND SIMILAR EXPENSES**	**294.557**	**269.769**	**239.302**
	c)	**NET INTEREST AND SIMILAR INCOME**	**572.127**	**539.655**	**541.743**
2.		**OPERATING INCOME**			
	a)	FX income	48.198	45.081	42.695
	b)	Loan fees	6.918	7.674	6.986
	c)	Fees based on off-balance sheet items	24.933	24.781	24.902
	d)	Service fees	178.944	184.256	195.262
	e)	Trading income	368	1.139	3.210
	f)	Other operating income	55.681	46.042	44.167
	g)	**TOTAL OPERATING INCOME a) to f)**	**315.042**	**308.973**	**317.222**
3.		**NON-INTEREST BEARING EXPENSES**			
	a)	Business and direct expenses			
	1)	Costs of value adjustments, risk-bearing assets, provisions for contingent liabilities and other value adjustments	190.499	144.750	230.103
	2)	Other business and direct expenses	76.209	76.181	75.621
	3)	**TOTAL BUSINESS AND DIRECT EXPENSES 1) + 2)**	**266.708**	**220.931**	**305.724**
	b)	Operating expenses			
	1)	Costs of salaries and contributions	250.783	243.133	246.087
	2)	Costs of business premises, other fixed assets and utilities	166.075	158.933	168.794
	3)	Other operating expenses	106.998	98.441	120.634
	4)	**TOTAL OPERATING EXPENSES 1) to 3)**	**523.856**	**500.507**	**535.515**
	c)	**TOTAL NON-INTEREST BEARING EXPENSES**	**790.564**	**721.438**	**841.239**
4.		**PROFIT BEFORE TAXES**	**64.209**	**145.003**	**158.054**
5.		**LOSS**	**158.428**	**17.813**	**140.328**
6.		**TAXES**	**9.252**	**16.706**	**17.926**
7.		**PROFIT BASED ON INCREASE OF DEFERRED TAX FUNDS AD REDUCTION OF DEFERRED TAX LIABILITIES**	**495**	**60**	**147**
8.		**LOSS BASED ON REDUCTION OF DEFERRED TAX FUNDS AND INCREASE OF DEFERRED TAX LIABILITIES**	**0**	**188**	**175**
9.		**NET PROFIT 4. - 6.**	**54.957**	**128.173**	**140.102**
10.		**NET LOSS 4. - 6.**	**-157.933**	**17.817**	**140.330**
11.		**FINANCIAL RESULT 9.-10.**	**-102.976**	**110.356**	**-228**

REPORT ON CAPITAL CONDITION AND ADEQUACY OF BANKS IN THE FB&H
ASSETS SIDE OF THE BALANCE SHEET

in 000 KM

No.	DESCRIPTION	31.12.2011	31.12.2012	31.12.2013
1	**BANK'S CORE CAPITAL**			
1.a.	Shareholders capital, reserves and profit			
1.1.	Shareholders capital – common and permanent preferred non-cumulative shares – cash payments	1.177.932	1.185.966	1.188.094
1.2.	Shareholders capital – common and permanent preferred non-cumulative shares – investments in kind and in rights	12.550	12.550	12.550
1.3.	Amount of issue premiums earned upon payment of shares	136.485	136.485	136.485
1.4.	General mandatory reserves (reserves mandated by the law)	192.752	101.836	206.809
1.5.	Other reserves not related to the assets quality evaluation	262.501	309.179	362.349
1.6.	Retained – undistributed profit from previous years	225.861	167.825	248.901
1.a.	**TOTAL (1.1. to 1.6.)**	**2.008.081**	**1.913.841**	**2.155.188**
1.b.	Deductible items from 1.a.			
1.7.	Uncovered losses transferred from previous years	251.187	120.740	112.610
1.8.	Current year's loss	45.512	17.818	140.330
1.9.	Book value of own (treasury) shares of the bank	81	156	156
1.10.	Intangible assets	57.180	52.590	41.418
1.b.	**TOTAL (1.7. to 1.10.)**	353.960	191.304	294.514
1.	**CORE CAPITAL: (1.a.-1.b.)**	**1.654.121**	**1.722.537**	**1.860.674**
2	**SUPPLEMENTARY CAPITAL OF THE BANK**			
2.1.	Shareholders capital – common and permanent preferred cumulative shares – cash payments	3.090	3.090	3.091
2.2.	Shareholders capital – common and preferred cumulative shares – investments in kind and in rights	0	0	
2.3.	General loan loss provisions for the category A – performing assets	212.248	211.433	215.083
2.4.	Current year profit – audited and confirmed by an external audit	62.564	67.243	71.984
2.5.	Profit amount for which the FBA issues an order restricting its disbursement	0	0	0
2.6.	Amount of subordinated debts representing max. 50% of the core capital	139.754	120.264	165.473
2.7.	Hybrid convertible items max. 50% of the core capital	0	0	0
2.8.	Permanent, non-refundable items	49.312	65.070	1.416
2.	**AMOUNT OF SUPPLEMENTARY CAPITAL: (2.1 to 2.8)**	**466.968**	**467.100**	**457.047**
3	**DEDUCTIBLE ITEMS FROM THE BANK'S CAPITAL**			
3.1.	Portion of invested shareholders capital that, according to the FBA, represents a received, but over-appraised value	0	0	0
3.2.	Capital contributions of other legal entities exceeding 5% of the bank's core capital	18.408	3.043	2.844
3.3.	Receivables from shareholders with significant voting rights – approved contrary to regulations	0	85	0
3.4.	LCRE towards shareholders with significant voting rights in the bank (no FBA approval required)	0	0	0
3.5.	LLP shortfall as per regulatory requirement	19.386	95.720	158.859
3.	**AMOUNT OF DEDUCTIBLE ITEMS FROM THE BANK'S CAPITAL: (3.1 to 3.5)**	**37.794**	**98.848**	**161.703**
A.	**NET CAPITAL OF THE BANK (1.+2.-3.)**	**2.083.295**	**2.090.789**	**2.156.018**
B.	**RISK WEIGHTED ASSETS AND LOAN EQUIVALENTS**	**11.286.997**	**11.078.498**	**10.999.406**
C.	**WEIGHTED OPERATIONAL RISK**	**965.932**	**974.201**	**981.318**
D.	**WEIGHTED MARKET RISK**	**0**	**0**	**0**
E.	**TOTAL WEIGHTED RISKS B+C+D**	**12.252.929**	**12.052.699**	**11.980.724**
F.	**NET CAPITAL RATE (CAPITAL ADEQUACY) (A.:E.) X 100**	**17,0%**	**17,3%**	**18,0%**

ATTACHMENT 9

HEADCOUNT INFORMATION FOR BANKS IN THE FB&H

No.	BANK	31.12.2011	31.12.2012	31.12.2013
1	BOR Banka d.d. Sarajevo	57	62	64
2	Bosna Bank International d.d. Sarajevo	235	247	279
3	Hercegovačka banka d.d. Mostar	72		
4	Hypo Alpe Adria Bank d.d. Mostar	647	579	517
5	Intesa Sanpaolo banka d.d. Sarajevo	525	537	528
6	Investiciono Komercijalna banka d.d. Zenica	173	166	164
7	Komercijalno Investiciona banka d.d. Velika Kladuša	71	71	71
8	Moja banka d.d.Sarajevo	171	151	156
9	NLB banka d.d. Tuzla	471	456	442
10	Poštanska banka d.d. Sarajevo	90	85	
11	Privredna Banka d.d Sarajevo	191	179	177
12	ProCredit Bank d.d. Sarajevo	427	344	333
13	Raiffeisen BANK dd Bosna i Hercegovina	1.576	1,552	1.531
14	Sberbank BH d.d. Sarajevo	329	360	411
15	Sparkasse Bank d.d. Sarajevo	432	452	462
16	UNION banka d.d. Sarajevo	177	183	200
17	UniCredit bank d.d. Mostar	1.338	1,305	1.262
18	Vakufska banka d.d. Sarajevo	229	230	225
19	Ziraatbank BH d.d. Sarajevo	158	171	229
	TOTAL	**7.369**	**7.130**	**7.051**