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

I N F O R M A T I O N

ON THE BANKING SYSTEM
OF THE FEDERATION OF BOSNIA AND HERZEGOVINA
30. 09. 2016

Sarajevo, December 2016

The Banking Agency of the Federation of B&H, as a regulatory institution conducting banking supervision, has prepared the Information on the Banking System of the Federation of B&H (as of 30.09.2016) based on financial statements and other information and data provided by banks. This also encompasses results and information obtained during on-site examinations in banks and off-site financial analyses in the Agency.

I INTRODUCTION 1

II BUSINESS PERFORMANCE OF BANKS IN THE FEDERATION OF B&H 2

1. BANKING SECTOR STRUCTURE
1.1. Status, Number and Network of Branches 2
1.2. Ownership Structure 3
1.3. Human Resources 6

2. FINANCIAL PERFORMANCE INDICATORS
2.1. Balance Sheet 7
2.1.1. Liabilities 12
2.1.2. Capital – Strength and Adequacy 17
2.1.3. Assets and Asset Quality 22
2.2. Profitability 33
2.3. Weighted Nominal and Effective Interest Rates 38
2.4. Liquidity 42
2.5. FX Risk 50

III CONCLUSIONS AND RECOMMENDATIONS 52

ANNEXES 55

I INTRODUCTION

For a long period of time, operations of the banking sector have been taking place in an unfavourable environment and conditions of stagnating economic growth and development in countries of the EU zone. Insufficient economic growth, the difficult situation in the real sector and numerous domestic problems caused by the political situation in the country, limited access to stable sources of financing have all adversely reflected upon the condition and prospects in the banking sector. In the first three quarters of 2016, the banking sector saw an increase in the balance sheet total, deposits and loans, while capital is up on the basis of an increase in the financial result (profit) and recapitalisation in two banks. Liquidity, profitability and capitalisation of the sector can be deemed satisfactory, and it can be concluded that the banking sector remains stable and secure.

As of 30.09.2016, there were 16 licenced banks in the Federation of B&H. The headcount amounted to 6 680. The number of banks is down by one bank compared to the end of 2015 (17 banks) because of a merger.

The balance sheet total of the banking sector at the end of the third quarter of 2016 amounted to KM 17.8 billion, which is up by 3.8% or KM 651 million compared to the end of 2015. Two key items in the assets structure: loans and cash funds, recorded a slight change, i.e. an increase in the share of loans from 67.7% to 68.1%, while the share of cash funds decreased from 28.3% to 27.1%.

Cash funds in the first nine months of 2016 decreased slightly by 0.5% or KM 26 million and amounted to KM 4.8 billion as of 30.09.2016.

Loans, as the largest assets item of banks, recorded an increase in the amount of 4.5% or KM 517 million in the first three quarters of 2016, thus amounting to KM 12.1 billion as of 30.09.2016. In the first three quarters of 2016, positive trends were recorded in the segment of sector lending, i.e. increased lending to private companies compared to retail lending. Loans to private companies recorded a growth rate of 6% or KM 305 million in the first nine months of 2016, so that loans to this sector reached the amount of KM 5.6 billion and had a share of 46.5% as of 30.09.2016. In the same period, retail loans recorded a growth rate of 3% or KM 189 million, while their share decreased slightly from 49.1% to 48.6%, with them amounting to KM 5.9 billion as of 30.09.2016.

Total non-performing loans as of 30.09.2016 amounted to KM 1.45 billion and decreased by 3% or KM 51 million compared to the end of 2015. The share of non-performing loans, as a key indicator of loan quality, dropped from 12.9% to 12%. The improvement of this indicator was positively impacted by the recorded credit growth, in addition to a permanent write-off. Out of the total loans to legal entities, non-performing loans make up 15.3% or KM 953 million, down by 1.4 percentage points compared to the end of 2015. For the retail sector, the aforementioned amount to 8.4% or KM 498 million, down by 0.6 percentage points compared to the end 2015.

Investments in securities recorded an increase of 7.4% or KM 78 million (in 2015, the increase amounted to 31% or KM 249 million), which primarily refers to securities issued by the Government of the FB&H. The securities portfolio amounted to KM 1.1 billion at the end of the third quarter of 2016, thus having a 6.3% share in assets.

In the structure of banks' sources of funding, deposits in the amount of KM 13.6 billion and with a share of 76.4% continued to be the dominant source of funding for banks in the Federation of B&H. Total deposits were up by 3.9% or KM 508 million in the first nine months of 2016. On the other hand, savings deposits, as the most important segment of the deposit and financial potential of banks, increased by 4.6% or KM 331 million in the first nine months of 2016. As of 30.09.2016, they amounted to KM 7.6 billion.

The long-standing trend of reduced loan commitments continued in the first three quarters of 2016 as well, with a rate of 7.9% or KM 71 million, to the level of KM 833 million and a share of 4.7% in the structure of banks' liabilities. In the last seven years, due to the impact of the financial and economic crisis, banks borrowed significantly less from abroad, and by paying receivables due these sources were significantly reduced. Thus, it is evident that credit growth in the FB&H will be based more on an increase in domestic sources of funding in the period to come.

In the first three quarters of 2016, total capital increased by 7.5% or KM 193 million, amounting to KM 2.8 billion as of 30.09.2016.

As of 30.09.2016, regulatory capital amounted to KM 2.4 billion and was up by 9% or KM 196 million compared to the end of 2015, with slight changes in its structure.

The capital adequacy ratio of the banking system, as one of the most important indicators of the strength and capital adequacy of banks, was 16% as of 30.09.2016, which is up by 0.9 percentage points compared to the end of 2015. The capital adequacy ratio is significantly above the legal minimum (12%) and represents a satisfactory capitalisation of the overall system for the existing level of risk exposure as well as a strong foundation and basis for preserving its security and stability. The financial leverage ratio amounted to 9.8% at the level of the banking system as of 30.09.2016.

According to data from the income statement, a positive financial result, profit in the amount of KM 172.4 million, was recorded at the level of the banking system in the Federation of B&H in the first nine months of 2016. A positive financial result in the amount of KM 210.8 million was recorded by 14 banks, while two banks posted a loss in the amount of KM 38.4 million.

II BUSINESS PERFORMANCE OF BANKS IN THE FEDERATION OF B&H

1. BANKING SECTOR STRUCTURE

1.1. Status, Number and Network of Branches

As of 30.09.2016, there were 16 banks with a banking licence in the Federation of B&H. The number of banks is lower following the merger of Moja banka d.d., Sarajevo with the Investment and Commercial Bank d.d., Zenica as of 31.07.2016. A special law from 01.07.2008 regulates the establishment and operations of the Development Bank of the FB&H Sarajevo, a legal successor of the Investment Bank of the FB&H dd Sarajevo.

In the first three quarters of 2016, there was no major expansion of the banks' network of organisational units, chiefly attributable to the financial crisis and the reduced volume of the bans' business activities.

Banks have reorganised their networks of organisational units by changing the organisational form, membership or address of their organisational parts. This also entailed mergers and closings of some organisational parts, all for the purpose of business rationalisation and operating costs reduction. There was a total of 78 such changes among banks in the Federation of B&H (73 on the territory of the

Federation of B&H, and 5 in Republika Srpska): 13 new organisational units were established, 10 organisational units were closed, and 55 underwent changes.

Subsequent to such changes, banks in the Federation of B&H had a total of 561 organisational units as of 30.09.2016, up by 0.7% compared to 31.12.2015.

The number of organisational units of banks from Republika Srpska in the Federation of B&H (23) is down by 13 since the banking licence of one bank in Republika Srpska was revoked and thus her organisational units in the Federation of B&H also ceased operations.

As of 30.09.2016, seven banks from the Federation of B&H had 51 organisational units in Republika Srpska, and nine banks had 11 organisational units in Brčko District. Three banks from Republika Srpska had 23 organisational units in the Federation of B&H.

As of 30.09.2016, all banks had licences to effect interbank transactions within the domestic payment system, and 15 banks had secured deposits.

1.2. Ownership Structure

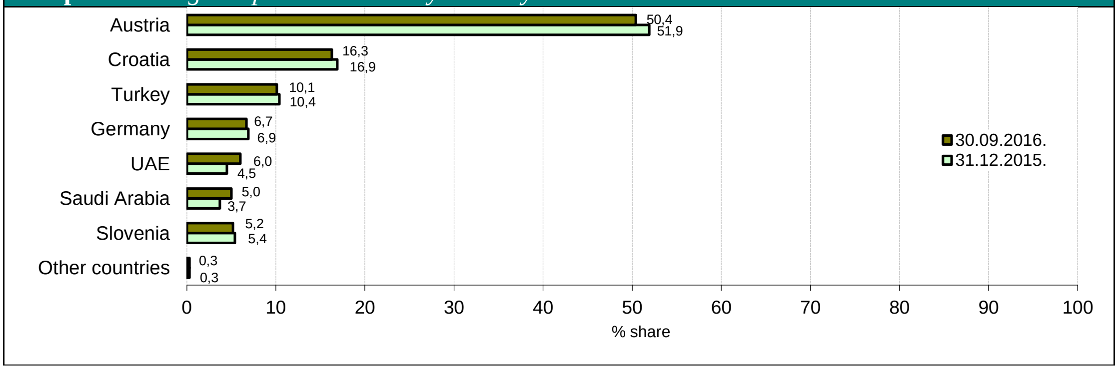
The ownership structure of banks[1] as of 30.09.2016, assessed on the basis of available information and reviews conducted in the banks themselves, is as follows:

- In private or mostly private ownership 15 banks
- In state or mostly state ownership[2] 1 bank.

Out of the 15 banks in mostly private ownership, five banks are in majority ownership of local legal entities and natural persons (residents), while 10 banks are in majority foreign ownership.

If observed solely from the perspective of foreign capital, using the criterion of the shareholders' home country, the conditions as of 30.09.2016 are slightly different compared to those at the end of 2015: the largest share of foreign capital in the amount of 50.4% (-1.5 percentage points) still refers to shareholders from Austria, followed by shareholders from Croatia with 16.3% (-0.6 percentage points) and Turkey with 10.1% (-0.3 percentage points). Other countries hold individual shares below 7%.

Graph 1: *Foreign Capital Structure by Country*

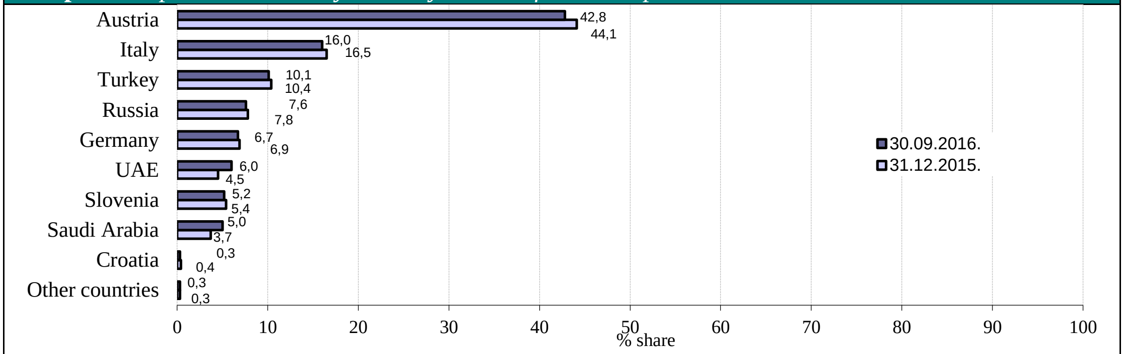


However, if taking into account capital relations, the structure of foreign capital can also be observed using the criterion of the home country of the parent bank or parent group having majority ownership

[1] The criterion for this particular bank classification is ownership of share capital in banks.
[2] State ownership refers to domestic state capital of B&H.

(direct or indirect via group members) of banks in the Federation of B&H. According to this criterion, the conditions are also slightly different compared to the end of 2015: the share of banking groups and banks from Austria amounts to 42.8% (-1.3 percentage points), followed by Italian banks with a share of 16.0% (-0.5 percentage points), while the share of capital from Turkey amounts to 10.1% (-0.3 percentage points) and from Russia to 7.6% (-0.2 percentage points). Other countries held individual shares below 7%.

Graph 2: *Capital Structure by Country – Seat of the Group* [3]



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

- in KM 000 -

Table 1: *Ownership Structure by Total Capital*

BANKS	31.12.2014		31.12.2015 [4]		30.09.2016		INDEX	
1	2		3		4		5 (3/2)	6 (4/3)
State-owned banks	51 929	2%	52 319	2%	52 316	2%	101	100
Private banks	2 367 574	98%	2 517 669	98%	2 710 734	98%	108	108
T O T A L	2 419 503	100%	2 569 988	100%	2 763 050	100%	108	108

In the first three quarters of 2016, total capital was up by 8% or KM 193 million. The current financial result – profit in the amount of KM 172 million – and a recapitalisation in the amount of KM 83 million in two banks had the largest positive impact on capital, while a decrease due to the transfer of the payment of dividends in the amount of 62 KM million to Liabilities had the largest negative impact.

If observed from the perspective of the share of state-owned, private and foreign capital in the banks' share capital, it results in a more detailed picture of the capital ownership structure of banks in the Federation of B&H.

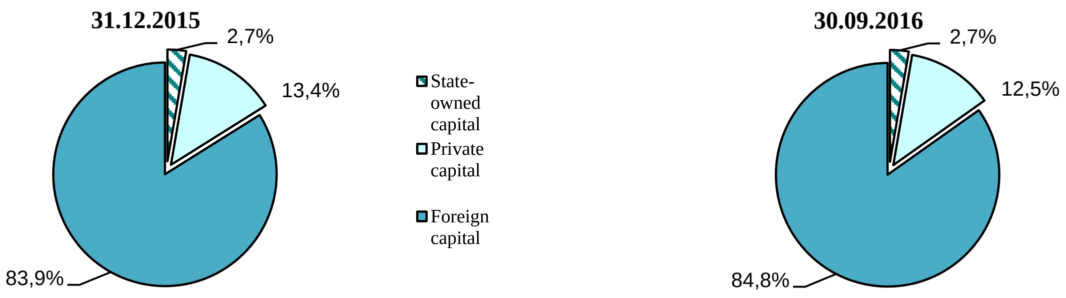
- in KM 000 -

Table 2: *Ownership Structure by Share of State-Owned, Private and Foreign Capital*

SHARE CAPITAL	31.12.2014		31.12.2015		30.09.2016		INDEX	
	Amount	Share %	Amount	Share %	Amount	Share %	4/2	6/4
1	2	3	4	5	6	7	8	9
State-owned capital	32 364	2.6	31 647	2.7	31 647	2.7	98	100
Private capital (residents)	162 354	13.2	156 574	13.4	147 964	12.5	96	95
Foreign capital (non-residents)	1 038 832	84.2	979 271	83.9	1 007 471	84.8	94	103
T O T A L	1 233 550	100.0	1 167 492	100.0	1 187 082	100.0	95	102

[3] In addition to home countries of parent groups whose members are banks from the Federation of B&H, the graph also outlines countries of all other foreign shareholders of banks in the Federation of B&H.
[4] All data in the Information related to 31.12.2015 are from the banks' audited financial statements.

Graph 3: *Ownership Structure (by Share Capital)*



As of 30.09.2016, share capital of banks in the Federation of B&H was up by KM 19.6 million compared to 31.12.2015, amounting to KM 1.2 billion. Share capital increased as a result of a KM 30 million recapitalisation in one bank and decreased by KM 10 million following the merger of one bank with another due to the share exchange ratio.

An analysis of the ownership structure of banks from the aspect of the share capital shows changes and trends in the banking system of the Federation of B&H, namely changes in the ownership structure, in a more detailed manner.

As of 30.09.2016, the share of state-owned capital in total share capital amounts to 2.7% and is the same compared to 31.12.2015, according to both relative and absolute indicators

The 12.5% share of private capital (of residents) in total share capital is down by 0.9 percentage points compared to 31.12.2015, according to relative indicators. According to absolute indicators, the share is down by KM 9 million net after trade with non-residents and the merger of one bank with another.

The share of private capital (of non-residents) in total share capital is up by 0.9 percentage points (84.8%), according to relative indicators. According to absolute indicators, the share is up by KM 28 million net after trade with residents and recapitalisation in one bank.

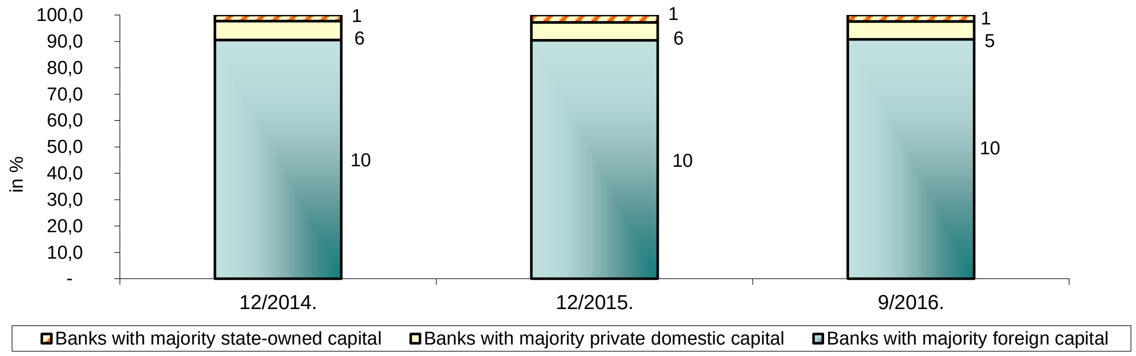
The market share of banks according to the ownership criterion has been almost unchanged for a long time, i.e. has seen only minor changes. The market share of banks in majority foreign ownership as of 30.09.2016 stood at a high 90.8%, while banks with majority domestic private capital had a 6.8% share and one bank with majority state-owned capital had a 2.4% share.

- in % -

Table 3: *Market Shares of Banks by Ownership Type (Majority Capital)*

BANKS	31.12.2014			31.12.2015			30.09.2016		
	No. of banks	Share in total capital	Share in total assets	No. of banks	Share in total capital	Share in total assets	No. of banks	Share in total capital	Share in total assets
1	2	3	4	5	6	7	8	9	10
Banks woth majority state-owned capital	1	2.1	2.3	1	2.0	2.8	1	1.9	2.4
Banks with majority private domestic capital	6	7.8	7.1	6	7.0	6.8	5	6.5	6.8
Banks with majority foreign capital	10	90.1	90.6	10	91.0	90.4	10	91.6	90.8
TOTAL	17	100.0	100.0	17	100.0	100.0	16	100.0	100.0

Graph 4: *Market Shares by Ownership Type*



1.3. Human Resources

As of 30.09.2016, banks in the Federation of B&H had a headcount of 6 680 employees, 3% of which were employed in banks with majority state-owned capital and 97% of which were employed in private banks.

Table 4: *Employees in Banks of the Federation of B&H*

BANKS	HEADCOUNT						INDEX	
	31.12.2014		31.12.2015		30.09.2016		3/2	4/3
1	2		3		4		5	6
State-owned banks	202	3%	181	3%	191	3%	90	106
Private banks	6 758	97%	6 502	97%	6.489	97%	96	100
TOTAL	6 960	100%	6 683	100%	6.680	100%	96	100
Number of banks	17		17		16		100	100

Table 5: *Qualification Structure of Employees*

LEVEL OF QUALIFICATION	HEADCOUNT						INDEX	
	31.12.2014		31.12.2015		30.09.2016		4/2	6/4
1	2	3	4	5	6	7	8	9
University degree	3 775	54.2%	3 757	56.2%	3 839	57.5%	99	102
Two-year post-secondary school qualification	587	8.5%	551	8.3%	550	8.2%	94	100
Secondary school qualification	2 571	36.9%	2 360	35.3%	2 277	34.1%	92	96
Other	27	0.4%	15	0.2%	14	0.2%	55	93
TOTAL	6 960	100.0%	6 683	100.0%	6 680	100.0%	96	100

The headcount at the end of the third quarter of 2016 was almost the same as at the end of 2015.

Slight changes in the qualification structure (a further increase in the share of employees with university degrees to 57.5%) are the result of a drop in the number of employees with secondary school qualifications by 4% or 83.

One of the indicators affecting the performance assessment of individual banks and the banking system as a whole is staff efficiency, expressed as a ratio of assets over the number of employees, i.e. assets per employee. A higher ratio is an indicator of better efficiency of both the bank's and the entire system's operations.

Table 6: *Assets per Employee*

BANKS	31.12.2014			31.12.2015			30.09.2016		
	Head-count	Assets (KM 000)	Assets per employee	Head-count	Assets (KM 000)	Assets per employee	Head-count	Assets (KM 000)	Assets per employee

State-owned	202	379 330	1 878	181	476 866	2 635	191	421 327	2 206
Private	6 758	15 771 200	2 334	6 502	16 684 859	2 566	6 489	17 391 254	2 680
TOTAL	6 960	16 150 530	2 320	6 683	17 161 725	2 568	6 680	17 812 581	2 667

At the end of the reporting period, there were KM 2.7 million of assets per employee at banking system level.

Table 7: *Assets per Employee – by Group*

Assets (KM 000)	31.12.2014 Number of banks	31.12.2015 Number of banks	30.09.2016 Number of banks
Up to 1 000	1	0	0
1 000 to 2 000	7	7	6
2 000 to 3 000	7	8	7
Over 3 000	2	2	3
TOTAL	17	17	16

Analytical indicators for individual banks range from KM 1.2 million to KM 4 million of assets per employee. There are five banks in which this ratio is better than the one at the banking sector level, while this ratio exceeds the amount of KM 2.8 million in the three largest banks in the system.

2. FINANCIAL PERFORMANCE INDICATORS OF BANKS

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

1) Balance sheet information for all banks submitted on a monthly basis, together with additional annexes 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 on the solvency of banks, information on capital and capital adequacy, asset classification, concentrations of certain risk types, liquidity position, FX risk exposure, interest rates on loans and deposits, all based on reports prescribed by the Agency,
3) Information on business results of banks (income statement according to the FBA model) and statements of cash flows, all submitted to the FBA on a quarterly basis.

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

In accordance with the provisions of the Law on Opening Balance Sheet of Banks, banks with majority state-owned capital are required to report to the Agency on the basis of the “full” balance sheet divided into: liabilities, neutral items and assets. In order to obtain more realistic indicators of the operations banks in the Federation of B&H, further analysis of the banking system will be based on indicators from the assets side of the balance sheet of banks with majority state-owned capital.[5]

2.1. Balance Sheet

The balance sheet total of the banking sector amounted to KM 17.8 billion at the end of the third quarter of 2016, up by 3.8% or KM 651 million compared to the end of 2015. Following a stagnation in the

[5] State-owned banks post the „full balance sheet“, meaning liabilities and neutral items, which the state will take over once the privatisation process gets finalised. As of 30.06.2016, these items amounted to KM 717 million in the case of one state-owned bank.

first quarter, positive trends from the second quarter continued in the third quarter as well, i.e. a slight increase in the balance sheet total and key balance sheet categories: deposits, total capital, and loans, which is a long-standing trend since the impact of the financial and economic crisis is still felt, i.e. the impact of the conditions of the environment in which the banks in the Federation of B&H, i.e. in B&H, operate.

- KM 000 -

Table 8: *Balance Sheet*

DESCRIPTION	31.12.2014 AMOUNT	Share %	31.12.2015 AMOUNT	Share %	30.09.2016 AMOUNT	Share %	INDEX	
1	2	3	4	5	6	7	8 (4/2)	9 (6/4)
ASSETS:								
Cash funds	4 560 234	28.2	4 857 483	28.3	4 831 706	27.1	107	99
Securities[6]	801 289	5.0	1 050 206	6.1	1 128 382	6.3	131	107
Facilities to other banks	50 836	0.3	78 420	0.5	128 726	0.7	154	164
Loans	11 170 277	69.2	11 610 744	67.7	12 127 524	68.1	104	104
Value adjustment	1 160 481	7.2	1 181 736	6.9	1 173 181	6.6	102	99
Net loans (loans minus value adjust.)	10 009 796	62.0	10 429 008	60.8	10 954 343	61.5	104	105
Business premises and other fixed assets	525 860	3.2	516 894	3.0	532 471	3.0	98	103
Other assets	202 515	1.3	229 714	1.3	236 953	1.4	113	103
TOTAL ASSETS	**16 150 530**	**100.0**	**17 161 725**	**100.0**	**17 812 581**	**100.0**	**106**	**104**
LIABILITIES:								
LIABILITIES								
Deposits	12 130 746	75.1	13 098 983	76.3	13 607 104	76.4	108	104
Borrowings from other banks	0	0.0	0	0.0	0	0.0	0	0
Loan commitments	1 026 503	6.4	904 050	5.3	832 620	4.7	88	92
Other liabilities	573 778	3.5	588 704	3.4	609 807	3.4	103	104
CAPITAL								
Capital	2 419 503	15.0	2 569 988	15.0	2 763 050	15.5	106	108
TOTAL LIABILITIES (LIABILITIES AND CAPITAL)	**16 150 530**	**100.0**	**17 161 725**	**100.0**	**17 812 581**	**100.0**	**106**	**104**

- KM 000 -

Table 9: *Banks' Assets by Ownership Structure*

BANKS	31.12.2014 No. of banks	Assets (KM 000)		31.12.2015 No. of banks	Assets (KM 000)		30.09.2016 No. of banks	Assets (KM 000)		INDEX	
1	2	3		4	5		6	7		8 (5/3)	9(7/5)
State-owned	1	379 330	2%	1	476 866	2.8%	1	421 327	2.4%	126	88
Private	16	15 771 200	98%	16	16 684 859	97.2%	15	17 391 254	97.6%	106	104
TOTAL	**17**	**16 150 530**	**100%**	**17**	**17 161 725**	**100%**	**16**	**17 812 581**	**100%**	**106**	**104**

A slight increase in the balance sheet total at system level is the result of a low to moderate growth rate with the majority of banks (12 banks), while the remaining banks recorded a decrease in assets.

The concentration indicator used for three key segments of banking operations (assets, loans and deposits) is the Herfindahl index.[7]

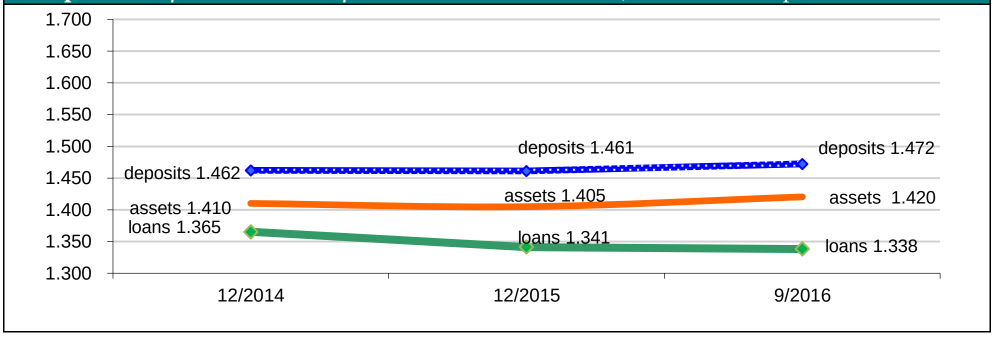
---

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

[7] 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 shares of specific elements (e.g. assets, deposits, loans) of all market participants in the system. It should be noted that this index does not grow linearly and that the value of e.g. 3 000 does not mean that the concentration in the system is 30%. Hypothetically, if there were just one bank in the entire system, the HHI would be 10 000 at most.

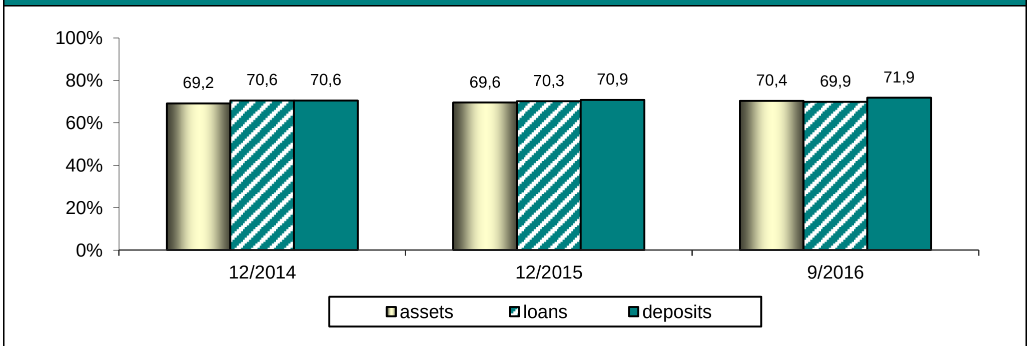
Graph 5: *Herfindahl Indeks of Concentrations in Assets, Loans and Deposits*



In the first nine months of 2016, the Herfindahl index of concentrations in all three relevant categories (assets, loans and deposits) changed slightly, so that it amounted to 1 420 units for assets (+15), 1 338 units for loans (-3), and 1 472 units for deposits (+11) as of 30.09.2016, which is indicative of a moderate concentration.[8]

The second concentration indicator for the banking system is the ratio of market concentrations, i.e. the concentration rate[9] (hereinafter: the CR) showing the total share of the largest institutions in the system in selected relevant categories: assets, loans and deposits. Like Herfindahl's index of concentrations, the CR5 also changed only slightly and amounted to 70.4% for market share, 69.9% for loans, and 71.9% for deposits. For a long period of time, the value of the CR5 saw slight changes across all three categories, but the domination of the five largest banks in the system, which hold approximately 70% of the market, loans and deposits, is still evident.

Graph 6: *Concentration Rates for the 5 Largest Banks – CR5: Assets, Loans and Deposits*



The banking sector can also be analysed on the basis of the criterium of belonging to groups formed according to asset size.[10] Changes in share percentage compared to the end of 2015 are minor, which is the result of slight changes the assets of most banks. The number of banks is lower by one due to the status change (merger) of two banks.

The banking system is dominated by the two largest banks (I group with assets in the amount of over KM 2 billion) with a share of 47.3%, followed by the share of the II group (three banks with assets in the amount ranging from KM 1 billion to KM 2 billion) of 23.0%, while the III group has a somewhat lower share of 18.4% (four banks with assets ranging from KM 500 million to KM 1 billion). The share of the IV and largest group (six banks with assets ranging from KM 100 million to KM 500 million)

---

[8] If the value of the HHI is below 1 000, this shows no presence of the concentration on the market, while an index value between 1 000 and 1 800 shows moderate concentration, and a HHI value above 1 800 shows high concentration on the market.
[9] The concentration ratio (CR) rests on the number of institutions included in the calculation.
[10] Banks are divided into 5 groups depending on asset size.

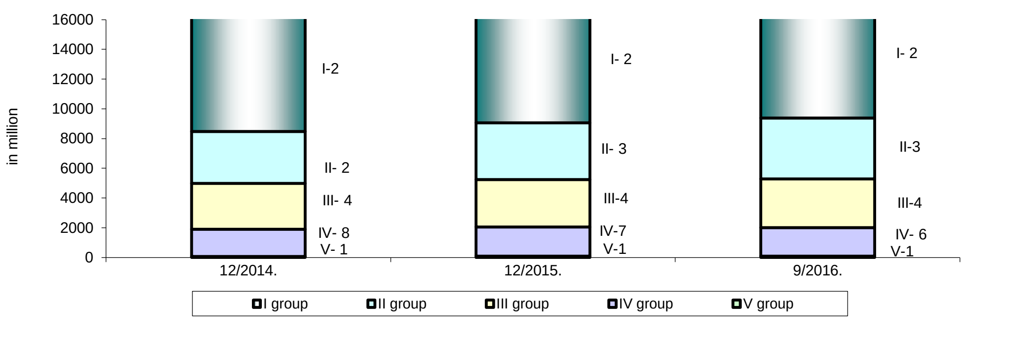
amounts to 10.8%, while one bank in the V and last group (with assets below KM 100 million) has a share of a negligible 0.5%.

The table below provides an overview of the amounts and shares of individual groups of banks in total assets by period (in KM million).

Table 10: *Share of Individual Banking Groups in Total Assets by Period*

ASSETS	31.12.2014			31.12.2015			30.09.2016		
	Amount	Share %	No. of banks	Amount	Share %	No. of banks	Amount	Share %	No. of banks
I- Over 2 000	7 685	47.6	2	8 121	47.3	2	8 432	47.3	2
II- 1000 to 2000	3 488	21.6	3	3 822	22.3	3	4 101	23.0	3
III- 500 to 1000	3 077	19.0	4	3 172	18.5	4	3 268	18.4	4
IV- 100 to 500	1 823	11.3	7	1 963	11.4	7	1 922	10.8	6
V- Below 100	78	0.5	1	84	0.5	1	90	0.5	1
TOTAL	16 151	100.0	17	17 162	100.0	17	17 813	100.0	16

Graph 7: *Share of Individual Banking Groups in Total Assets by Period*



In the first nine months of 2016, as was the case in previous years, the balance sheet total had a slight upward trend in the amount of 3.8% or KM 651 million, amounting to KM 17.8 billion as of 30.09.2016. Deposits recorded almost the same growth rate in the amount of 3.9% or KM 508 million, thus amounting to KM 13.6 billion, while total capital amounted to KM 2.8 billion following a moderate increase in the amount of 7.5% or KM 193 million. The downward trend of loan commitments continued, with a rate of 7.9% or KM 71 million, i.e. to the level of KM 833 million.

Cash funds in the amount of KM 4.8 billion remained at almost the same level as at the end of 2015, which is the result of a slight drop in the amount of 0.5% or KM 26 million.

Due to the stagnation of loan facilities, some banks approved short-term excess liquidity to domestic and foreign banks, which brings additional interest income. Facilities to other banks increased by 64% or KM 50 million, amounting to KM 129 million as of 30.09.2016.

In the reporting period of 2016, credit growth in the amount of 4.5% or KM 517 million was recorded and loans amounted to KM 12.1 billion as of 30.09.2016.

The increase in investments in securities continued in the first nine months of 2016 as well, with a rate of 7.4% or KM 78 million (in 2015, the increase amounted to 31.1% or KM 249 million), which primarily refers to securities issued by the Government of the FB&H. The securities portfolio amounted to KM 1.1 billion at the end of the reporting period, thus having a 6.3% share in assets.

The portfolio of securities available for sale (a small part thereof refers to the trading portfolio), up by 10.5% or KM 93 million, amounted to KM 1 billion, while the securities held to maturity decreased by 8.9% or KM 15 million, i.e. to KM 152 million. Both portfolios include securities issued by the Federation of B&H[11] in the total amount of KM 593 million, as well as securities issued by Republika Srpska in the amount of KM 139 million. Also, the trading portfolio includes shares issued by local companies totaling KM 2 million. The remaining portion of the securities portfolio amounts to KM 394 million and refers mostly to bonds of EU countries, and to a lesser extent to corporate bonds, primarily those of EU banks. The increase in investments in securities in the first three quarters of 2016 is primarily the result of an increase in the exposure to the Federation of B&H on the basis of the purchase of treasury bills.

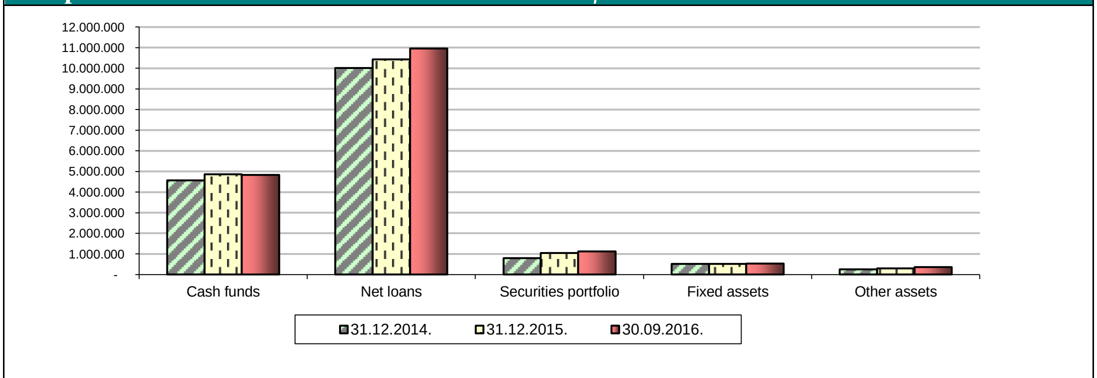
As of 30.09.2016, the balance and book value of treasury bills issued by the Federation of B&H amounted to KM 110 million (KM 100 million as of 31.12.2015) and KM 109.9 million, respectively.

In addition to treasury bills, the securities portfolios of banks also include market bonds issued by the Federation of B&H. The balance of the nominal amount of bonds as of 30.09.2016 amounted to KM 459 million (31.12.2015: KM 419 million). The majority of the treasury bills and market bonds with a book value of KM 550 million was classified in the portfolio of securities available for sale, while the rest in the amount of KM 20 million is classified in the portfolio of securities held to maturity.

When analysing the overall securities portfolio (KM 1.1 billion) from the aspect of exposure by country, the largest share is that of B&H (65.0%) (63.6% at the end of 2015) as a result of an increase in the amount of 10% or KM 66 million, i.e. to the level of KM 734 million at the end of the third quarter of 2016, followed by Romania (8.9%), Austria (7.4%), Belgium (3.0%), etc.

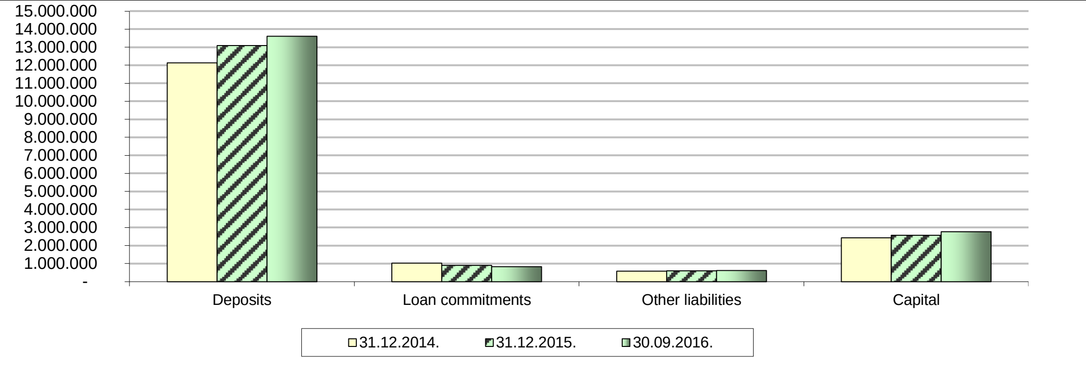
The graphs below show the structure of the key items of the banks' balance sheet.

Graph 8: *Assets Structure within the Balance Sheet of Banks*



[11] All types of securities issued by the Federation of B&H.

Graph 9: *Liabilities Structure within the Balance Sheet of Banks*



Within the liabilities structure of the banks' balances sheets, deposits still represent a dominant source of funding for banks in the Federation of B&H (with an amount of KM 13.6 billion and a 76.4% share). The long-standing trend of decrease of loan commitments continued in the first nine months of 2016 as well, which resulted in the share dropping to 4.7% (-0.6 percentage points). Capital continued to increase in 2016 as well. As of 30.09.2016 capital amounted to KM 2.8 billion, with a share of 15.5% (+0.5 percentage points).

Two key items in the structure of assets: loans and cash funds, saw minor changes, i.e. an increase in the loan share from 67.7% to 68.1%, while the share of cash funds decreased from 28.3% to 27.1%.

- in KM 000 -

Table 11: *Cash Funds of Banks*

CASH FUNDS	31.12.2014		31.12.2015		30.09.2016		INDEX	
	Amount	Share %	Amount	Share %	Amount	Share %	4/2	6/4
1	2	3	4	5	6	7	8	9
Cash	456 750	10.0	581 152	12.0	701 558	14.5	127	121
RR at the CB B&H	2 854 559	62.6	3 181 721	65.5	3 218 964	66.6	111	101
Accounts at deposit institutions in B&H	22 759	0.5	2 100	0.0	10 544	0.2	9	502
Accounts at deposit institutions abroad	1 225 850	26.9	1 092 273	22.5	900 503	18.7	89	82
Cash funds in the process of collection	316	0.0	237	0.0	137	0.0	75	58
TOTAL	4 560 234	100.0	4 857 483	100.0	4 831 706	100.0	107	99

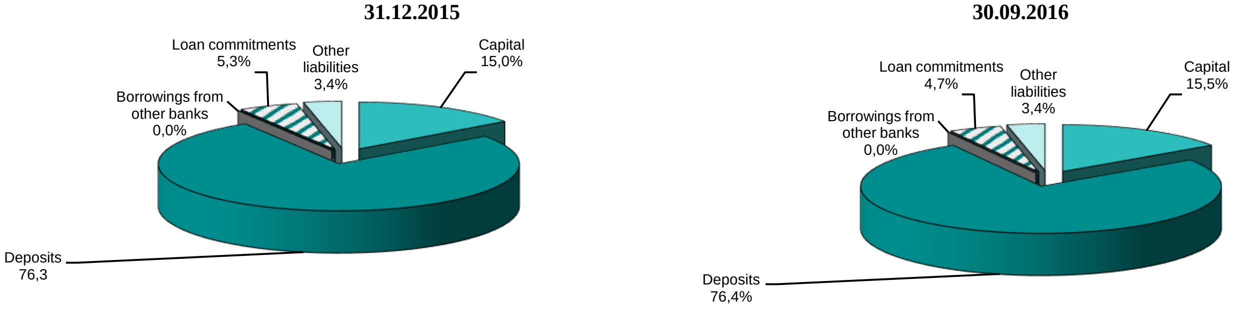
The banks' cash funds in the CBBH reserves account were up by 1% or KM 37 million in the first three quarters of 2016 and amounted to KM 3.2 billion or 66.6% of total cash funds as of 30.09.2016 (65.5% at the end of 2015). The continuous drop in banks' funds in accounts of deposit institutions abroad continued in 2016 as well. They decreased by 18% or KM 192 million and amounted to KM 0.9 billion or 18.7% of total cash funds (22.5% at the end of 2015). Following their increase in the amount of 21% or KM 120 million, banks held cash funds in the amount of KM 702 million in vaults and treasuries as of 30.09.2016, which represents 14.5% of total cash funds.

These trends prompted a change in the currency structure of cash funds: in the reporting period, the share of local currency increased from 73.1% to 77.8%, while cash in foreign currency decreased by the same percentage.

2. 1. 1. Liabilities

The total liabilities structure (liabilities and capital) within the banks' balance sheet as of 30.09.2016 is provided in the graph below:

Graph 10: *Liabilities Structure of Banks*



In the first nine months of 2016, the share of deposits (76.4%), as the most significant source of funding of banks, remained almost unchanged (+0.1 percentage points), while the continuous trend of decrease in the share of loan commitments, the second largest source of funding, continued in 2016 as well (by 0.6 percentage points, i.e. to the level of 4.7%).

As of 30.09.2016, deposits amounted to KM 13.6, million, thus still being the largest source of funding of banks in the Federation of B&H.

The second-largest source of funding are loans in the amount of KM 0.8 billion and with a share of 4.7%, which banks received mostly by borrowing from foreign financial institutions. In the past few years, due to the effect of the financial and economic crisis, as well as reduced lending activities, banks incurred significantly fewer loans abroad and, coupled with the payment of receivables due, reduced these sources of funding by app. 60% (at the end of 2008, deposits amounted to KM 2.18 billion), with them being down by 7.9% or KM 71 million in the first nine months (in 2015, the decrease amounted to 11.9% or KM 122 million). If subordinated loans in the amount of KM 112 million, which the banks withdrew in the interest of strengthening the capital base and improving capital adequacy, were added to loan commitments, total loan funds would hold a share of 5.3% in total sources of funding.

As of 30.09.2016, banks held the largest amount of liabilities towards the following creditors (6 out of a total of 25 creditors), accounting for 81% of total loan commitments: TC ZIRAAT BANKASI A.S. (Turkey), European Investment Bank (EIB), the World Bank, UniCredit Bank Austria AG, the European Bank for Reconstruction and Development (EBRD), and the European Fund for Southeast Europe (EFSE).

Capital amounted to KM 2.8 billion at the end of the third quarter of 2016, thus having recorded an increase in the amount of 7.5% or KM 193 million compared to the end of 2015, as a result of an increase on the basis of the financial result (profit) in the first nine months of 2016 (KM 172 million), recapitalisation (two banks, KM 83 million), and a decrease due to the payment of dividends from profit recorded in 2015 being transferred to Liabilities (two banks, KM 62 million).

According to the information submitted by banks, out of the total deposit amount at the end of the reporting period, only 5.9% relates to deposits collected in organisational units of banks from the Federation of B&H, which are doing business in Republika Srpska and Brčko District.

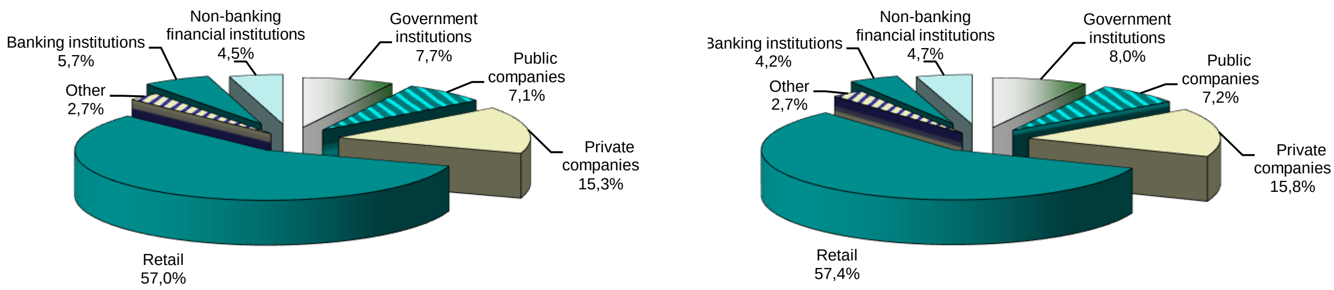
- in KM 000 -

Table 12: *Deposit Structure by Sector* [12]

SECTORS	31.12.2014 Amount	31.12.2014 Share %	31.12.2015 Amount	31.12.2015 Share %	30.09.2016 Amount	30.09.2016 Share %	INDEX 4/2	INDEX 6/4
1	2	3	4	5	6	7	8	9
Government institutions	795 985	6.6	1 002 438	7.7	1 087 223	8.0	126	108
Public companies	883 463	7.3	927 692	7.1	984 614	7.2	105	106
Private companies and enterprises	1 821 094	15.0	2 008 364	15.3	2 146 794	15.8	110	107
Banking institutions	886 007	7.3	752 217	5.7	576 459	4.2	85	77
Non-banking financial institutions	517 110	4.2	583 387	4.5	636 874	4.7	113	109
Retail	6 863 296	56.6	7 465 252	57.0	7 814 293	57.4	109	105
Other	363 791	3.0	359 633	2.7	360 847	2.7	99	100
TOTAL	12 130 746	100.0	13 098 983	100.0	13 607 104	100.0	108	104

Graph 11: *Deposit Structure by Sector*

31.12.2015 30.09.2016



A slight increase in deposits in the first three quarters of 2016 in the amount of 3.9% or KM 508 million, i.e. to the level of KM 13.6 billion, resulted in minor changes in the deposit structure by sector, namely due to an increase in all sectors with the exceptions of deposits of banking institutions, which still have a downward trend.

The continuous growth of retail deposits continued in 2016 as well, with a rate of 5% or KM 349 million, thus amounting to KM 7.8 billion as of 30.09.2016., while the share rose from 57% to 57.4%, so that this sector's deposits are still the largest source of funding for banks. Analytical data by bank indicate that the share ranges from 13% to 83%, the share of this sector’s deposits is the largest in 14 out of 16 banks, and it is above 50% in eight banks.

The second largest sector source in terms of amount and share are deposits of private companies. After a slight decrease in the amount of 2% in the first six months of 2016, a 9% increase was recorded in the third quarter, which resulted in a cumulative growth rate of 7% or KM 138 million and a share of 15.8% in nine months (+ 0.5 percentage points). As of 30.09.2016, they amounted to KM 2.1 billion.

Deposits of government institutions, following an increase in the amount of 8% or KM 85 million, amounted to KM 1.1 billion at the end of the third quarter of 2016, which is a share of 8%.

Deposits of public companies recorded an increase in the amount of 6% or KM 57 million and amounted to KM 1 billion, which is a share of 7.2%.

[12] Information from the auxiliary BS-D form, which banks submit on a quarterly basis in addition to the balance sheet (as based on the FBA model).

It should be noted that the trend of long-standing decrease in deposits of banking institutions due to the effects of the crisis, the reduced volume of lending and high liquidity continued in 2016 as well. From the end of 2009 to 31.12.2015, deposits of this sector dropped by app. 65% or KM 1.4 billion. Negative trends in previous years (related to these funds at sector level) are mostly the result of debt reduction, i.e. the repayment of funds to groups that own the banks in the Federation of B&H.

In the first nine months of 2016, deposits of the aforementioned sector fell by 23% or KM 176 million, to the level of KM 576 million, with the share dropping from 5.7% to 4.2%, mostly as a result of deposits that some banks had received from banking groups at the end of 2015 having been withdrawn immediately in early 2016. Based on the aforementioned information, it can be concluded that the foreign debt level of banks from the Federation of B&H is much lower, especially in terms of deposit funds of parent groups. It should be noted that maturity has changed singificantly in favour of short-term deposits, which have the function of maintining the maturity adjustment within the prescribed limits and/or improving certain indicators (structural balance, growth of certain categories, e.g. assets, deposits, followed by liquidity indicators, etc.). The aforementioned is also indicated by the fact that KM 118 million or 27% of term deposits of the group mature by the end of 2016, while KM 63 million or 14% mature in 2017, and KM 134 million or 30% mature in 2018. Considering that the same trend of decrease is present with respect to loan commitments, a number of banks have been facing the problem of maintaining their maturity adjustment for quite some time, with this being caused by the unfavourable maturity of local deposit funds, due to which they must continuously work on securing better quality sources in terms of maturity in order to intensify the increase in approved loans.

It is worth noting that 80% or KM 464 million of deposits of banking institutions relate to deposits of banks from the group (mostly shareholders). Financial support by parent groups is present with respect to nine banks in the Federation of B&H, wherein such financing is still concentrated in three large banks (86%). In this way, banks in majority foreign ownership had financial support and secured inflows of new funds by their foreign groups in previous periods. If these funds are coupled with loan commitments and subordinated debt, the financial support of banks from the group is higher (with respect to 11 banks) and amounts to KM 808 million as of 30.09.2016 (or 4.5% of total liabilities of the banking sector, which is lower compared to the end of 2015 (KM 932 million or 5.4% of liabilities)). In total deposits, the funds of banking groups hold a share of 3.4% (4.5% at the end of 2015), while loan commitments to the group account for 29.2% of total loan commitments (this share is up by 3%). In the first three quarters of 2016, these funds dropped by 13.3% or KM 124 million, largely based on regular maturities (deposits fell by 22% or KM 131 million, loan commitments are up by 2.8% or KM 7 million, while subordinated loans remained at the same level of KM 100 million).

Considering that lending activities of banks got significantly reduced due to the economic crisis, thus resulting in high liquidity and a good capitalisation rate of most of foreign-owned banks in the Federation of B&H, the trend of the past couple of years is still present when it comes to reduced exposures to the group. This primarily relates to the segment of both deposit sources and loan sources, largely on the basis of regular repayments of matured liabilities. It is evident that the financial support of parent banking groups got significantly reduced, so that credit growth in the Federation of B&H will have to rely more on local sources of funding in the period to come. It is especially important to underline that deposit funds that certain banks received from their parent groups over the past two years are mostly of short-term maturity (most often one to two months) and mainly serve the purpose of maintaining maturity adjustment within the prescribed limits, and therefore do not constitute a quality source of long-term funding.

When it comes to other sectors, with a low share in total deposits, it should be noted that the increase in deposits of non-banking financial institutions continued in 2016 as well, with rate amounting to 9%

or KM 53 million. The share increased from 4.5% to 4.7%, so that deposits of this sector in the amount of KM 637 million rank fifth in terms of amount and share and are higher than deposits of banking institutions for the first time (KM 576 million, 4.2% share).

The currency structure of deposits as of 30.09.2016 has slightly changed: deposits in local currency, after a moderate increase in the amount of 8.5% or KM 592 million, increased their share to 55.5% (+2.4 percentage points) and amounted to KM 7.6 billion, while deposits in foreign currency (with a dominant share of EUR currency), following a decrease in the amount of 1.4% or KM 84 million, amounted to KM 6.1 billion, thus holding a share of 44.5%.

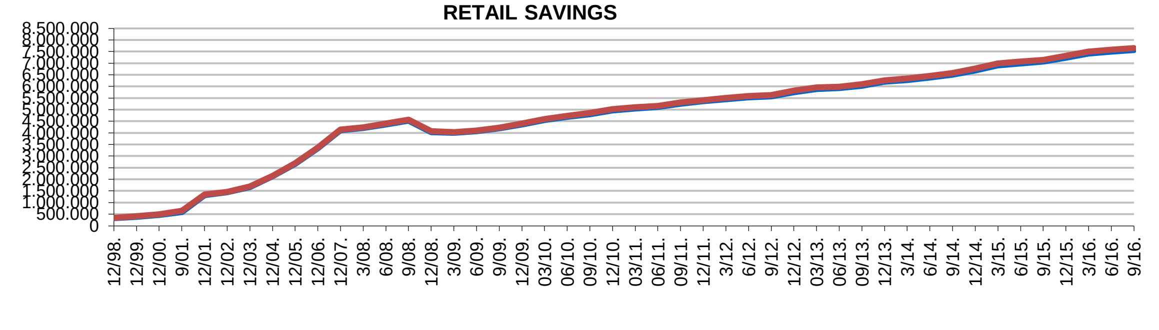
At the end of the third quarter of 2016, the structure of deposits by domicile status of depositors also changed slightly: resident funds amounted to KM 12.7 billion and had a share of 93.6% (+1.6 percentage points), while non-resident deposits amounted to KM 0.9 billion and represented 6.4% of total deposits. The increase in the share of resident deposits is, on the one hand, the result of their nominal increase in the amount of 5.7% or KM 684 million, and, on the other hand, the result of the drop in non-resident deposits by 16.9% or KM 176 million. Over the past few years, non-resident deposits continuously decreased as a result of the withdrawal, i.e. return of deposits to the parent bank or member of the banking group to which non-resident funds mostly refer.

The long-standing trend of increase in savings deposits, as the most significant segment of the deposit and financial potential of banks, continued in the first three quarters of 2016 as well, with a rate of 4.6% or KM 331 million. As of 30.09.2016, they amounted to KM 7.6 billion.

Table 13: *New Retail Savings By Period*

BANKS	AMOUNT (in KM 000)			INDEX	
	31.12.2014	31.12.2015	30.09.2016	3/2	4/3
1	2	3	4	5	6
State-owned	73 072	78 771	85 092	108	108
Private	6 618 891	7 156 178	7 480 757	108	105
TOTAL	6 691 963	7 234 949	7 565 849	108	105

Graph 12: *New Retail Savings by Period*



The two largest banks hold 57% of savings, while six banks hold individual shares of less than 2%, which amounts to 6.6% of total savings at system level.

Out of the total amount of savings, 42% refer to saving deposits in local currency and 58% to savings deposits in foreign currency.

Table 14: *Maturity Structure of Retail Savings Deposits by Period*

BANKS	AMOUNT (in KM 000)			INDEX	
	31.12.2014	31.12.2015	30.09.2016	3/2	4/3
1	2	3	4	5	6

Short-term savings deposits	3 129 098	46.8%	3 537 982	48.9%	3 792 841	50.1%	113	107
Long-term savings deposits	3 562 865	53.2%	3 696 967	51.1%	3 773 008	49.9%	104	102
TOTAL	6 691 963	100.0%	7 234 949	100.0%	7 565 849	100.0%	108	105

Compared to the end of 2015, the maturity structure of savings deposits changed slightly through an increase in short-term deposits by 7% or KM 255 million, while long-term deposits rose by 2% or KM 76 million, thus resulting in the share of long-term deposits being down from 51.1% to 49.9%.

Long-standing continuous growth and positive trends in the savings segment of banks in the Federation of B&H are the result of, on the one hand, better safety and stability of the overall banking system (as chiefly attributable to the functional, effective and efficient banking supervision implemented by the Agency) and, on the other hand, the existence of the deposit insurance system, the primary objective of which is increased stability of the banking, i.e. financial sector and the protection of savers. In order to preserve and strengthen the trust of citizens in the safety and stability of the banking system in B&H, the deposit insurance level rose following the onset of the financial crisis, and according to the latest decision by the Management Board of the Deposit Insurance Agency of B&H from December 2013, the insured deposit limit increased from the KM 35 000 to KM 50 000, effective as of 01.01.2014. All these actions are aimed towards limiting the effect of the global economic crisis on the banking and the overall economic system in the Federation of B&H and B&H.

As of 30.09.2016, there was a total of 15 banks from the Federation of B&H included in the deposit insurance program (i.e. holding licences issued by the Deposit Insurance Agency of B&H).

2.1.2. Capital – Strength and Adequacy

The capital[13] of banks in the Federation of B&H as of 30.09.2016 amounted to KM 2.4 billion.

It should be noted that the FBA, in order to comply with international standards of regulatory capital, adopted a new Decision on Minimum Standards for Bank Capital Management and Capital Hedge (hereinafter: the Decision) in mid-2014, which constitutes an innovated concept of capital, in which the previously prescribed and applied minimum standards in capital management are supplemented by additional measures for strengthening and preserving capital. New and amended provisions have influenced the form and content of regulatory reports in the segment of capital, with them having to be applied as of 30.09.2014.

- in KM 000 -

Table 15: *Regulatory Capital*

DESCRIPTION	31.12.2014		31.12.2015		30.09.2016		INDEX	
1	2		3		4		5 (3/2)	6 (4/3)
1.a.Core capital before reduction	1 991 385		2 010 634		2 223 921		101	111
1.1. Share capital – common and permanent non-cumulative shares	1 230 459		1 164 402		1 186 873		95	102
1.2. Issue premiums	136 485		132 667		132 667		97	100
1.3. Reserves and retained profit	624 441		713 565		904 381		114	127
1.b. Deductible items	219 589		183 755		207 191		84	113
1.1. Uncovered losses from previous years	122 705		28 371		119 789		23	422
1.2. Current year loss	50 868		102 108		40 752		201	40
1.3. Treasury shares	81		102		599		126	587
1.4.. Intangible assets	41 873		49 837		43 594		119	87
1.5. Deferred tax assets	2 780		1 641		1 441		59	88
1.6. Negative revalorised reserves	1 282		1 696		1 016		132	60
1. Core capital (1a-1b)	**1 771 796**	**81%**	**1 826 879**	**85%**	**2 016 730**	**86%**	103	110
2. Supplementary capital	**412 922**	**19%**	**330 784**	**15%**	**336 526**	**14%**	80	102
2.1. Share capital – common and permanent cumulative shares	3 091		3 090		209		100	7
2.2. General loan loss reserves	229 895		208 619		217 765		91	104

[13] Regulatory capital is defined in Articles 7, 8 and 9 of the Decision on Minimum Standards for Capital Management in Banks and Capital Hedge („Official Gazette of the Federation of B&H", No. 46/14).

2.3. Positive revalorised reserves	23 703		9 735		12 110		41	124
2.4. Amount of audited profit	N/a		N/a		N/a		N/a	N/a
2.5. Subordinated debt	154 814		107 918		105 020		70	97
2.5. Hybrid items and other instruments	1 419		1 422		1 422		100	100
3. Capital (1 + 2)	**2 184 718**	**100%**	**2 157 663**	**100%**	**2 353 256**	**100%**	99	109
4. Deductible items from capital	**203 077**		**206 321**		**204 446**		102	99
4.1. Bank's shares in capital of other legal entities above 5% of core capital	1 678		1 007		0		60	N/a
4.2. Loan loss reserves shortfall at regulatory request	199 890		204 559		203 689		102	100
4.3. Other deductible items	1 509		755		757		50	100
5. Net capital (3- 4)	**1 981 641**		**1 951 342**		**2 148 810**		98	110

In the first three quarters of 2016, capital[14] went up by 9% or KM 196 million compared to the end of 2015, with slight changes in its structure (86% core capital, 14% supplementary capital). Core capital increased by 10% or KM 190 million, and supplementary capital by 2% or KM 6 million.

The increase in core capital is primarily based on inclusion (transfer from supplementary to core capital) of profit recorded for 2015. After implementing legal procedures to adopt decisions by the general assembly of banks, recorded profit (15 banks) in the amount of KM 220 million was distributed as follows: 63% or KM 138 million to core capital (retained profit and reserves), two banks decided on dividend payment (KM 62 million total), while one bank distributed part of the profit of KM 20 million to retained profit, although the aforementioned is not an item of core capital.
The recapitalisation of two banks in the amount of KM 83 million also had an impact on the increase in core capital. At the same time, the status change of the integration (merger) of two smaller banks had a negative effect on core capital in the amount of app. KM 3 million, while one bank strengthened core capital through a conversion of cumulative preference shares (Supplementary Capital item) into ordinary shares and through a reduction of negative revalorised reserves (transfer to Costs), the effect of which was an increase in the amount of KM 4 million.

Deductible items (which decrease core capital) increased by 12% or KM 23 million, mostly as a result of an increase in current loss in the amount of KM 41 million and a partial reduction of uncovered losses in the amount of KM 10 million.

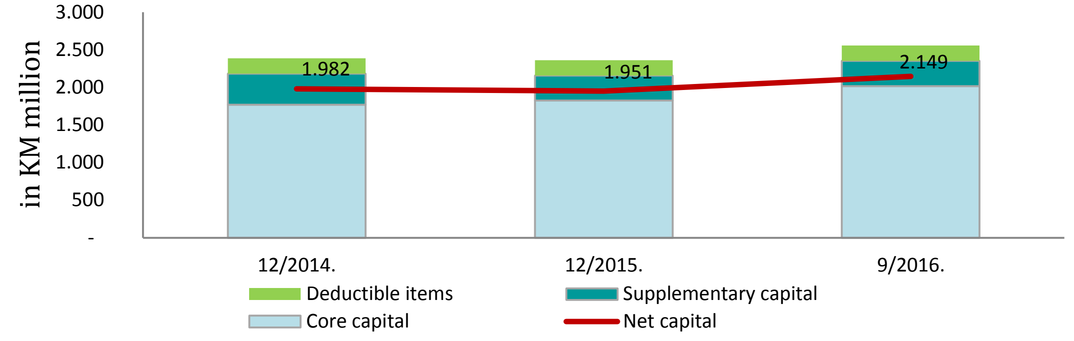
Supplementary capital increased by a slight 2% or KM 6 million, which is the net effect of an increase in general loan loss provisions (GLLP) and positive revalorised reserves, on the one hand, and a decrease on the basis of conversion of cumulative preference shares into ordinary shares and subordinated debt on the basis of depreciation, on the other hand.

According to regulatory changes in late 2011, deductible items from capital include a new accounting item: the shortfall of loan loss reserves upon regulator's request (i.e. a difference between required regulatory loan loss reserves according to balance sheet and off-balance sheet items and loan loss reserves formed from profit). As of 30.09.2016, this item amounted to KM 204 million, which is almost the same level as at the end of 2015 (this item was up by 2% or KM 5 million in 2015).

The graph below shows the regulatory capital structure.

[14] Source of information: quarterly Report on Capital Condition in Banks (Form 1-Table A).

Graph 13: *Regulatory Capital Structure*



As a result of the aforementioned changes, net capital increased by 10% or KM 197 million and amounted to KM 2.1 billion as of 30.09.2016.

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

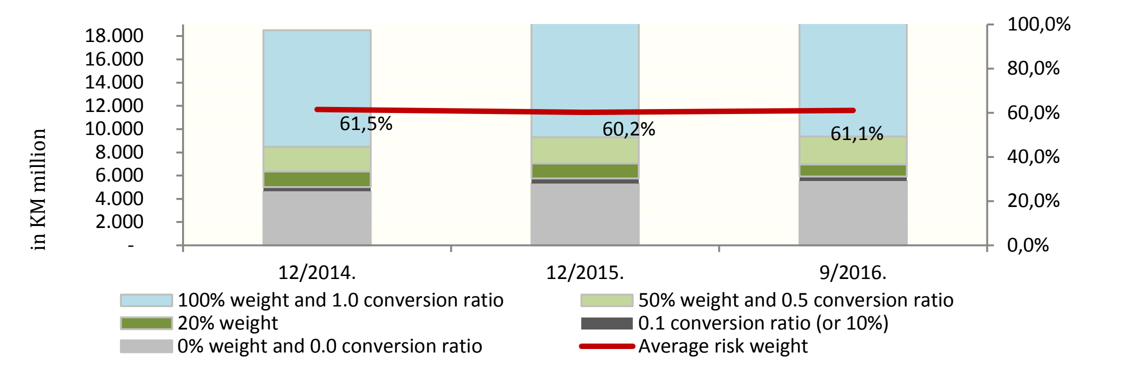
The table below provides a structure of the net exposure of banks by credit risk weight, i.e. conversion ratio for off-balance sheet items.

- in KM 000 -

Table 16: *Structure of Net Exposure of Banks by Credit Risk Weight*

DESCRIPTION	31.12.2014	31.12.2015	30.09.2016	INDEX	
1	2	3	4	5 (3/2)	6 (4/3)
TOTAL EXPOSURE (1+2):	**18 518 813**	**19 799 548**	**20 372 662**	107	103
1 Balance sheet assets	15 627 474	16 635 188	17 291 488	106	104
2. Off-balance sheet items	2 891 339	3 164 360	3 081 174	109	97
DISTRIBUTION BY RISK WEIGHT AND CONVERSION RATIO					
0% weight	4 598 235	5 255 223	5 487 461	114	104
20% weight	1 361 199	1 279 029	1 066 016	94	83
50% weight	54 096	52 241	120 587	97	231
100% weight	9 613 944	10 048 695	10 617 424	105	106
0.0 conversion ratio	52 453	51 199	49 078	98	96
0.1 conversion ratio	356 611	456 896	371 525	128	81
0.5 conversion ratio	2 073 404	2 227 852	2 269 154	107	102
1.0 conversion ratio	408 871	428 413	391 417	105	91
RISK-BEARING BALANCE SHEET AND OFF-BALANCE SHEET ASSETS	**11 394 469**	**11 918 650**	**12 454 066**	**105**	**104**
Average risk weight	**61.5%**	**60.2%**	**61.1%**	**98**	**102**

Graph 14: *Structure of Net Exposure of Banks by Credit Risk Weight*



In the reporting period of 2016, total net exposure of banks (before being weighted) increased slightly (3%). As of 30.09.2016, risk-bearing balance sheet and off-balance sheet items (after being weighted) amounted to KM 12.5 billion, with a 4% growth rate, which was primarily influenced by an increase in items with a 100% weight (mostly refers to the loan portfolio being up). As a result of the aforementioned, the average risk weight increased from 60.2% to 61.1%.

The same trend was seen with respect to the weighted operational risk (WOR), which rose slightly (2%) and amounted to KM 1 billion as of 30.09.2016. All of this resulted in an increase in total risk-bearing assets (4% or KM 560 million), i.e. to the level of KM 13.5 billion.

As of 30.09.2016, the share of risk-bearing balance and off-balance sheet assets exposed to credit risk amounted to 93% and to 7% on the basis of operational risk.

The banks' capitalisation rate, expressed as a ratio between capital and assets, amounted to 12.4% as of 30.09.2016, which is up by 0.7 percentage points compared to the end of 2015.

One of the key indicators of capital strength and adequacy[15] of banks is the capital adequacy ratio, which constitutes a ratio between net capital and risk-weighted assets. At the banking sector level, this ratio stood at 16.0% as of 30.09.2016, up by 0.9 percentage points compared to the end of 2015 as a result of a 10% increase in net capital and despite the negative impact of the implementation of certain provisions of the new Decision, starting with 31.12.2015.

Also, the indicator of capital strength and quality is the ratio of the core capital (Tier I) and total risk assets, which amounted to 15.0% at the level of the banking sector as of 30.09.2016. An important provision of the new Decision is the obligation of banks to intend part of the core capital above 8% (in application since 31.12.2015) of total risk assets to cover the risks related to preventive protection from potential losses in times of crisis or stressful situations through a protective layer for preserving the capital that has been prescribed in the amount of 2.5% of the amount of total risk assets under this Decision. Two other protective layers were introduced – a countercyclical protective layer and a protective layer for systemic risk, which the FBA would determine by a special resolution, if necessary.

Banks are also, according to the new Decision, obligated to establish and maintain the financial leverage ratio as an additional security and a simple capital hedge, at least in the amount of 6%, starting as of 31.12.2015. The financial leverage ratio at the level of the banking sector amounted to 9.8% as of 30.09.2016.

[15] The legally defined minimum capital adequacy ratio is 12%.

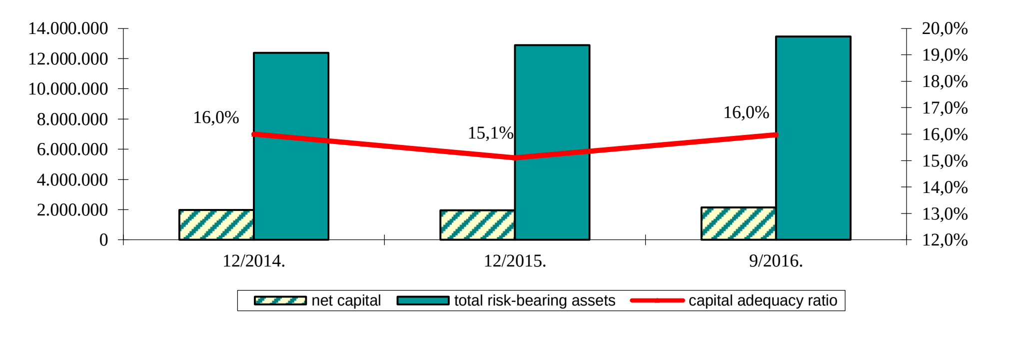
Although banking sector operations have been strongly affected by the economic crisis for the past few years, the capital adequacy of the banking sector has been continuously maintained at the level above 16% until 2015, when, for the aforementioned reasons, it decreased to 15.1%, only to increase slightly again and amount to 16.0% as of 30.09.2016, which is still a satisfactory capitalisation rate at system-level. The reason for this is, on the one hand, modest credit growth and a decrease of total risk-bearing assets in previous years (until 2013, after which gradual growth was recorded), and, on the other hand, the fact that banks have retained the largest share of profit from previous years within their capital and several banks have also improved their capitalisation rate by means of additional capital injections. However, problems related to non-performing loans and items not covered by loan loss reserves (net non-performing assets) may significantly impact and cause weakening of the capital base in several banks in the period to come. This is illustrated by the following information: at the end of 2008, net non-performing assets amounted to KM 197 million and its ratio (vs. core capital) was 13.2%. At the end of 2013, net non-performing assets amounted to KM 474 million, which is 25.5% of core capital, while dropping to the amount of KM 431 million in 2014, with a ratio of 24.3% (this is the result of a decrease on the basis of the sale of a part of non-performing loans in one bank, but also of an increase in loan loss reserves, i.e. greater coverage of non-performing facilities). In 2015, net non-performing had a further trend of decrease (mostly on the basis of a significant write-off in one bank) and amounted to KM 399 million, with a ratio of 21.5%. In 2016, the downward trend continued, net non-performing assets amounted to KM 360 million as of 30.09.2015, having a 17.8% ratio, which is still a high level and indicator. Also, according to existing regulations, banks do not calculate the capital requirement for market risks, due to which the capital adequacy rate is higher.

- KM 000 -

Table 17: *Net Capital, Total Weighted Risks and Capital Adequacy Ratio*

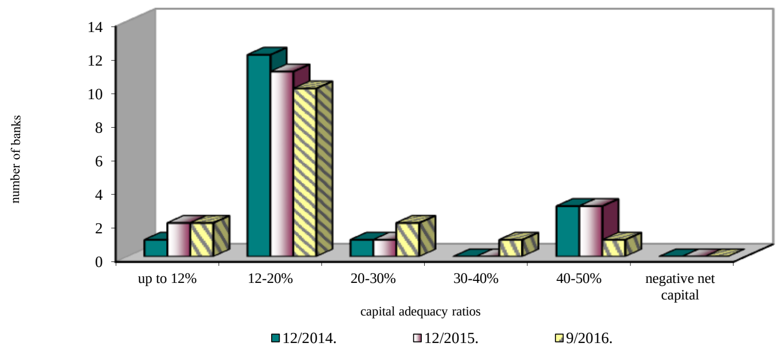
DESCRIPTION	31.12.2014	31.12.2015	30.09.2016	INDEX	
1	2	3	4	5(3/2)	6(4/3)
1. NET CAPITAL	1 981 641	1 951 342	2 148 810	98	110
2. RISK-BEARING BALANCE SHEET AND OFF-BALANCE SHEET ASSETS	11 394 469	11 918 650	12 454 066	105	104
3. WOR (WEIGHTED OPERATIONAL RISK)	982 250	976 734	1 001 009	99	102
4. TOTAL RISK-BEARING ASSETS (2+3)	12 376 719	12 895 384	13 455 075	104	104
5. NET CAPITAL RATIO (CAPITAL ADEQUACY) (1/ 4)	16.0%	15.1%	16.0%	94	106

Graph 15: *Net Capital, Total Weighted Risks and Capital Adequacy Ratio*



The capital adequacy rate of the banking system as of 30.09.2016 was 16.0%, which is still quite above the legal minimum (12%) and represents a satisfactory capitalisation rate of the overall system considering the existing level of risk exposure and it represents a strong basis and foundation for the preservation of its safety and stability.

Graph 16: *Capital Adequacy Ratios of Banks*



Out of a total of 16 banks in the Federation of B&H as of 30.09.2016, 14 banks had capital adequacy ratios that were above the legal minimum of 12%, while two banks had a ratio that was below the legal minimum, with it being noted that one bank's status change process (merger with another bank) was completed as of 30.09.2016. According to analytical data, 6 banks had a capital adequacy ratio below the one at the end of 2015, while 10 banks had improved this ratio.

Below is an overview of capital adequacy ratios of banks compared to the legal minimum of 12%:

- 2 banks had a ratio below 12%,
- 5 banks had a ratio between 13.5% and 14.8%,
- 4 banks had a ratio between 15.3% and 17.4%,
- 3 banks had a ratio between 18.8% abd 22.4%,
- 2 banks had a ratio between 39.4% and 41.1%.

By supervising the operations and financial condition of banks in the Federation of B&H in accordance with its legal competences and for the purpose of improving the safety of both individual banks and the banking system as a whole, the Agency instructed banks to take appropriate measures to strengthen their capital base and ensure capital adequacy in terms of the level and profile of the existing and potential exposure to all risks inherent to banking operations, primarily credit risk, as the most significant risk banks are exposed to in their business operations.

As has been the case before, 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 Federation of B&H, actions caused by and negative effects of the global financial and economic crisis on our country, the banking sector and the overall economy in B&H. Also, the focus is on troubled banks whose total business operations are under increased supervision and in which it is necessary to strengthen the capital base, as the basic prerequisite for the resolution of these banks and their exiting the zone of unsafe and unsound business operations. The capital of banks with adverse trends regarding asset quality, which negatively reflects on the capital and represents a realistic possibility for additional weakening of the capital base, is also under special supervision. Under conditions of economic crisis and credit risk growth caused by the downfall of the loan portfolio quality (due to an increase in uncollectable receivables), this requirement has a high priority and the capital segment is therefore under a continuous reinforced supervision in order to prevent the impairment of the banks' stability and the erosion of the capital base to a level that might jeopardise not only the banks' operations, but also impact the stability of the entire banking system.

2.1.3. Assets and Asset Quality

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

With the Law on Accounting and Audit in the Federation of Bosnia and Herzegovina entering into force on 31.12.2011, banks are required to prepare and present financial statements in accordance with the International Accounting Standards (IAS) and the International Financial Reporting Standards (IFRS), with recognition and measurement of financial assets and liabilities being subject to the IAS 39 – Financial instruments, recognition and measurement and the IAS 37 – Provisioning, contingent liabilities and contingent assets. Therefore, during the assessment of banks' exposure to credit risk, banks are required to continue calculating loan loss reserves in accordance with the criteria from the Decision on Minimum Standards for Credit Risk Management and Asset Classification in Banks, thereby considering already formed value adjustments of balance sheet assets and loss provisions for off-balance sheet items recorded in the banks' books, as well as loan loss reserves formed from profit (found on capital accounts).

- in KM 000 -

Table 18: *Assets (BS and off-BS), Loan Loss Reserves according to the Regulatory Body and Value Adjustments according to IAS)*

DESCRIPTION	31.12.2014	31.12.2015	30.09.2016	INDEX	
1	2	3	4	5(3/2	6(4/3)
1. Risk-bearing assets[16]	14 119 056	14 850 813	15 475 203	105	104
2. Calculated regulatory reserves for loan losses	1 551 075	1 507 523	1 503 548	97	100
3. Value adjustment and reserves for off-balance sheet items	1 253 270	1 269 548	1 269 910	101	100
4. Required regulatory reserves formed from profit for assessed	447 920	408 247	407 997	91	100
5. Formed regulatory reserves from profit for assessed losses	315 734	315 734	315 734	100	100
6. Shortfall of regulatory reserves formed from profit for assessed	199 889	204 558	203 689	102	100
7. Non-risk bearing items	6 217 740	6 797 824	6 732 575	109	99
8. TOTAL ASSETS (1+7)	20 336 796	21 648 637	22 207 778	106	103

Total assets with off-balance sheet items (assets)[17] of banks in the Federation of B&H amounted to KM 22.2 billion as of 30.09.2016 and up by 3% or KM 559 million compared to the end of 2015. Risk-bearing assets amount to KM 15.5 billion and are up by 4% or KM 624 million.

Non-risk bearing items amount to KM 6.7 billion or 30% of total assets with off-balance sheet items, thus being down by 1% or KM 65 million compared to the end of 2015.

Total calculated loan loss reserves based on regulatory requirements are at the same level of KM 1.5 billion, with the following items also remaining unchanged: formed value adjustments for balance sheet assets and provisions for losses in the amount of KM 1.3 billion, required regulatory reserves[18] (KM 408 million), formed regulatory reserves from profit (KM 316 million), and the shortfall of regulatory reserves[19] (KM 204 million).

Table 19: *Total Assets, Gross Balance Sheet Assets, Risk-Bearing and Non-Risk-Bearing Assets Items*

	31.12.2014	31.12.2015	30.09.2016	INDEX

[16] Does not include amount of facilities and contingent liabilities of KM 226 million that is secured with a cash deposit.

[17] Assets, as defined in Article 2 of the Decision on Minimum Standards for Credit Risk Management and Asset Classification in Banks („Official Gazette of the Federation of B&H", No. 85/11 – consolidated text and 33/12 – correction, 15/13).

[18] Required regulatory reserves represent a positive difference between calculated loan loss reserves and value adjustments (calculated loan loss reserves are higher than value adjustments).

[19] Shortfall of regulatory reserves represents a positive difference between required and formed loan loss reserves.

DESCRIPTION	Amount	Struct. %	Amount	Struct.%	Amount	Struct.%		
1.	2	3	4	5	6	7	8 (4/2)	9 (6/4)
Loans	9 725 304[20]	84.1	10 186 613	84.1	10 716 292	84.2	105	105
Interest	74 573	0.6	71 680	0.6	70 005	0.6	96	98
Past due receivables	1 184 588	10.2	1 161 853	9.6	1 155 754	9.1	98	99
Receivables on paid guarantees	26 218	0.3	24 648	0.2	25 949	0.2	94	105
Other facilities	194 440	1.7	139 457	1.1	155 547	1.2	72	111
Other assets	361 666	3.1	526 871	4.4	602 452	4.7	147	114
1. RISK-BEARING BALANCE SHEET ASSETS	11 566 789	100.0	12 111 122	100.0	12 725 999	100.0	105	105
2. NON-RISK BEARING BALANCE SHEET ASSETS	5 806 579		6 289 910		6 318 485		108	100
3. GROSS BALANCE SHEET ASSETS (1+2)	17 373 368		18 401 032		19 044 484		106	103
4. RISK-BEARING OFF-BS ITEMS	2 552 267		2 739 691		2 749 204		107	100
5. NON-RISK BEARING OFF-BS ITEMS	411 161		507 914		414 090		124	81
6. TOTAL OFF-BS ITEMS (4+5)	2 963 428		3 247 605		3 163 294		110	97
7. RISK-BEARING ASSETS WITH OFF-BS ITEMS (1+4)	14 119 056		14 850 813		15 475 203		105	104
8. NON-RISK BEARING ITEMS (2+5)	6 217 740		6 797 824		6 732 575		109	99
9. ASSETS WITH OFF-BS ITEMS (3+6)	20 336 796		21 648 637		22 207 778		106	103

Gross balance sheet assets[21] amount to KM 19 billion and are up by 3% or KM 643 million compared to the end of 2015. Risk-bearing balance sheet assets amount to KM 12.7 billion or 67% of gross balance sheet assets (thus being up by 5% or KM 615 million in the first three quarters of 2016). Non-risk bearing balance sheet assets amount to KM 6.3 billion and are at the same level as at the end of 2015.

Off-balance sheet risk-bearing items in the amount of KM 2.7 billion remained unchanged, while non-risk bearing items amount to KM 414 million and are down by 19% or KM 94 million compared to the end of 2015.

The effects of the economic crisis on the overall economy and industry in B&H are still pronounced, which is reflected in the key business segment of banks – the lending segment. In the first nine months of 2016, banks recorded credit growth in the amount of 4.5% or KM 517 million (4% or KM 440 million in 2015). As of 30.09.2016, loans amounted to KM 12.1 billion, with a share of 68.1% (+0.4 percentage points).

In the first three quarters of 2016, a total of KM 6.6 billion of new loans was approved, up by 14% or KM 829 million compared to the same period of the previous year. Out of the total loans approved, 71% relate to the corporate segment and 26% to the retail segment (at the end of 2015: 68% corporate, 27% retail). The maturity structure of the newly-approved loans: 45% long-term loans, 55% short-term loans (at the end of 2015: 47% long-term loans, 53% short-term loans).

The three largest banks in the Federation of B&H have an aggregate amount of approved loans of KM 6.6 billion, thus holding a share of 54.4% in total loans at the banking system level.

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

- in KM 000 -

Table 20: *Loan Structure by Sector*

SECTORS	31.12.2014		31.12.2015		30.09.2016		INDEX	
	Amount	Share %	Amount	Share %	Amount	Share %		
1	2	3	4	5	6	7	8(4/2)	9(6/4)
Government institutions	190 401	1.7	250 805	2.2	307 536	2.5	132	123

[20] This does not include the loan amount of KM 183 million covered by a cash deposit (included in non-risk bearing assets of the balance sheet).

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

Public companies	253 057	2.3	269 507	2.3	237 480	2.0	106	88
Private companies and enterprises	5 216 068	46.7	5 328 591	45.9	5 633 731	46.5	102	106
Banking institutions	10 449	0.1	5 701	0.0	4 060	0.0	55	71
Non-banking financial institutions	43 424	0.3	41 542	0.4	39 701	0.3	96	96
Retail	5 448 307	48.8	5 705 684	49.1	5 895 108	48.6	105	103
Other	8 571	0.1	8 914	0.1	9 908	0.1	104	111
TOTAL	11 170 277	100.0	11 610 744	100.0	12 127 524	100.0	104	104

In the loan structure by sector, there are two dominant sectors: retail and corporate, while lending to other sectors is negligible. In the first three quarters of 2016, positive trends in the segment of sectoral lending were recorded, i.e. increased lending to private companies compared to retail. Unlike 2015, when loans to private companies increased modestly by 2% or KM 112 million, the growth rate in the first nine months of 2016 was 6% or KM 305 million, so that this sector's loans amounted to KM 5.6 billion and had a share of 46.5% as of 30.09.2016 (+0.6 percentage points). On the other hand, banks performed more lending to the retail sector in 2015, which is much less risky, and an increase in the amount of 5% or KM 257 million was recorded. In the first nine months of 2016, loans to this sector continued to increase, but to a lesser extent, with the rate amounting to 3% or KM 189 million, while the share decreased slightly from 49.1% to 48.6% and amounted to KM 5.9 billion as of 30.09.2016.

According to information submitted by the banks (as of 30.09.2016) regarding the retail loan structure by purpose: consumer loans[22] hold a share of 80%, followed by housing loans with 18%, while the remaining 2% refer to loans to small crafts, small businesses and agriculture (at the end of 2015: 78.5% consumer loans, 19% housing loans, and 2.5% small crafts, small businesses and agriculture).

Tri najveće banke u sistemu plasirale su stanovništvu 61,4%, a privatnim preduzećima 45% ukupnih kredita datih ovim sektorima (na kraju 2015. godine: stanovništvo 62%, privatna preduzeća 45,6%).

The three largest banks in the system have approved 61.4% of retail loans and 45% of loans to private companies out of the total number of loans approved to these segments (at the end of 2015: 62% retail, 45.6% private companies).

The currency structure of loans: the largest share of 59.2% or KM 7.2 billion refers to currency clause loans (EUR: KM 7 billion or 98%, CHF: KM 131 million or 1.8%), followed by local currency loans with a share of 40.3% or KM 4.9 billion, while the smallest share of just 0.5% or KM 62 million refers to foreign currency loans (almost the entire amount thereof refers to EUR: KM 57 million or 92%). The total amount of loans with a currency clause in CHF of KM 131 million has a 1.1% share in the total loan portfolio and refers almost entirely to one bank in the banking system (1.7% at the end of 2015).

Since loans are the highest risk category of banks' assets, their quality represents one of key factors determining the stability and success of the banks' operations. Asset quality assessment is in fact an evaluation of credit risk exposure of the banks' loans, i.e. the 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 by classification category.

Table 21: *Asset Classification, General Credit Risk (GCR) and Potential Loan Losses (PLL)*

Classification category	31.12.2014			31.12.2015			30.09.2016			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)

[22] Including card business

A	11 494 730	81.4	229 895	12 316 066	82.9	246 321	13 080 442	84.5	261 607	107	106
B	955 518	6.8	83 031	950 153	6.4	76 023	861 567	5.6	68 619	99	91
C	272 134	1.9	64 168	301 862	2.0	75 796	242 809	1.6	59 703	111	80
D	523 939	3.7	301 942	426 025	2.9	252 682	437 860	2.8	261 041	81	103
E	872 735	6.2	872 039	856 707	5.8	856 701	852 525	5.5	852 578	98	99
Risk-bearing assets (A-E)	14 119 056	100.0	1 551 075	14 850 813	100.0	1 507 523	15 475 203	100.0	1 503 548	105	104
Classified (B-E)	2 624 326	18.6	1 321 180	2 534 747	17.1	1 261 202	2 394 761	15.5	1 241 941	97	94
Non-performing (C-E)	1 668 808	11.8	1 238 149	1 584 594	10.7	1 185 179	1 533 194	9.9	1 173 322	95	97
Non-risk bearing assets [23]	6 217 740			6 797 824			6 732 575			109	99
TOTAL (risk-bearing and non-risk bearing)	20 336 796			21 648 637			22 207 778			106	103

The first indicator and a warning sign of potential problems with loan repayment is an increase in past due receivables and their share in total loans. As of 30.09.2016, past due receivables amounted to KM 1.2 billion, which is the same level as at the end of 2015 (the aforementioned went down by 2% or KM 24 million in 2015), while the share decreased from 10.2% to 9.7%.

When analysing the quality of risk-bearing assets through trends and changes of key indicators, it can be concluded that key indicators of asset quality improved slightly in the first nine months of 2016 compared to the end of 2015. In some banks, these indicators showed slight oscillations (upgrade or downgrade), i.e. there were eight banks with ratios of the share of classified (compared to risk-bearing assets) below the level of the banking sector, while there were seven banks with ratios of the share of non-performing assets (compared to risk-bearing assets) below the level of the banking sector.

As of 30.09.2016, classified assets amounted to KM 2.4 billion and non-performing assets to KM 1.5 billion.

Classified assets (B-E) decreased by 6% or KM 140 million compared to the end of 2015 (in 2015, there was a drop of 3% or KM 90 million). Category B decreased by 9% or KM 89 million, while non-performing assets (C-E) went down by 3% or KM 51 million, largely on the basis of permanently written-off assets in the amount of KM 61 million (in 2015, non-performing decreased by 5% or KM 84 million).

The ratio expressed through the share of classified assets in risk-bearing assets is 15.5%, and the 1.6% drop compared to the end of 2015 is mostly the result of an increase in risk-bearing assets by 4% or KM 624 million as well as the aforementioned decrease in classified assets.

The most significant indicator of asset quality is the ratio between non-performing assets and risk-bearing assets, amounting to 9.9%, which is down by 0.8% compared to the end of 2015. However, this should be taken with a grain of salt due to the share of category B being 5.6% and due to the suspicion that a part of the loans classified in 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 two key sectors: corporate and retail. The two aforementioned indicators for these sectors show major deviation and point to a higher exposure to credit risk and consequently to potential loan losses regarding the corporate segment.

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

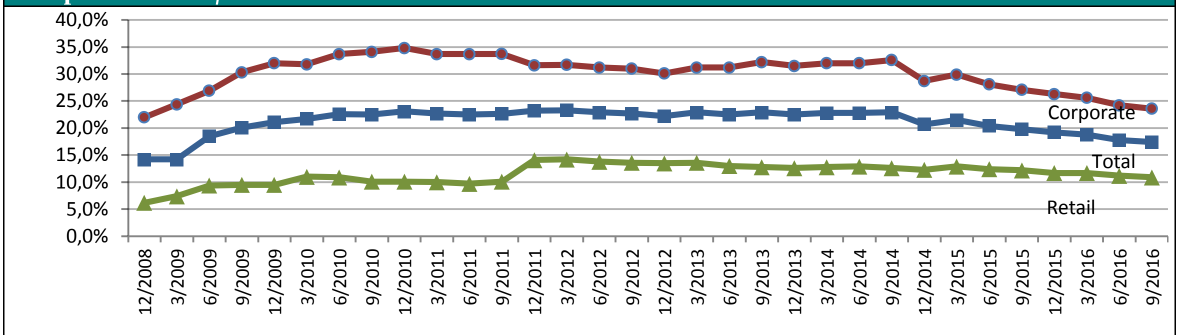
Table 22: *Classification of Corporate and Retail Loans*

Classification category	31.12.2015						30.09.2016						
	Retail	Share %	Corporate	Share %	TOTAL Amount	TOTAL Share	Retail	Share %	Corpo-rate	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	5 036 775	88.3	4 349 749	73.7	9 386 524	80.8	5 252 751	89.1	4 763 456	76.4	10 016 207	82.6	107
B	154 179	2.7	568 108	9.6	722 287	6.2	144 457	2.5	515 560	8.3	660 017	5.4	91
C	71 098	1.3	223 704	3.8	294 802	2.5	67 104	1.1	164 009	2.6	231 113	1.9	78
D	87 497	1.5	324 282	5.5	411 779	3.6	82 592	1.4	346 470	5.6	429 062	3.5	104
E	356 132	6.2	439 220	7.4	795 352	6.9	348 204	5.9	442 921	7.1	791 125	6.5	99
TOTAL	5 705 681	100.0	5 905 063	100.0	11 610 744	100.0	5 895 108	100.0	6 232 416	100.0	12 127 524	100.0	104
Class. loans. B-E	668 906	11.7	1 555 314	26.3	2 224 220	19.2	642 357	10.9	1 468 960	23.6	2 111 317	17.4	95
Non-perf. loans C-E	514 727	9.0	987 206	16.7	1 501 933	12.9	497 900	8.4	953 400	15.3	1 451 300	12.0	97
		49.1		50.9		100.0		48.6		51.4		100.0	
Individual sector's share in classified loans, non-performing loans and category B:													
Categories B-E		30.1		69.9		100.0		30.4		69.6		100.0	
Non-performing C-E		34.3		65.7		100.0		34.3		65.7		100.0	
Category B		21.3		78.7		100.0		21.9		78.1		100.0	

Loan quality indicators improved slightly in the first nine months of 2016 compared to the end of the previous year and the share of classified loans dropped to a still high 17.4% (-1.8 percentage points), due to a decrease in the aforementioned in the amount of 5% or KM 113 million, with the corporate segment being down by 6% or KM 86 million and the retail segment being down by 4% or KM 26 million.

The share of non-performing loans, as a key indicator of loan quality, decreased from 12.9% to 12.0%. Total non-performing loans are down by 3% or KM 51 million compared to the end of 2015 (with it being noted that the permanent write-off amounted to KM 58 million), as a result of a decrease in non-performing corporate loans by 3% or KM 34 million and non-performing retail loans by 3% or KM 17 million. Credit growth in the amount of 4.5% or KM 517 million also had a positive effect on the improvement of this indicator.

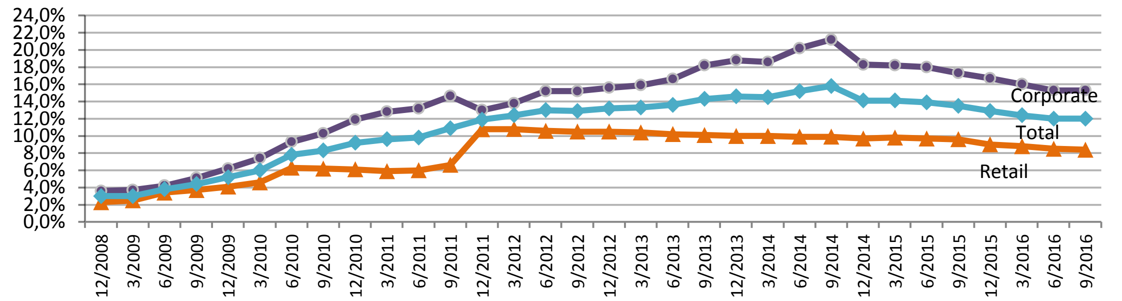
Graph 17: *Classified Loans*



Out of the total approved corporate loans in the amount of KM 6.2 billion as of 30.09.2016, there was still an alarmingly high 23.6% or KM 1.5 billion of loans classified within categories B to E, which is a 2.7% decrease compared to the end of 2015 (in 2015, this share went down by 2.4 percentage points). This indicator is much better for the retail segment. Out of the total approved retail loans in the amount of KM 5.9 billion, there were KM 642 million or 10.9% of loans classified in the aforementioned categories, down by 0.8 percentage points compared to the end of 2015 (in 2015, this share went down by 0.6 percentage points).

These trends are the result of the condition in the real sector and the effects of the economic crisis on the overall economy in B&H, due to which the corporate loan portfolio has a significantly lower quality than loans of the retail segment.

Graph 18: *Non-Performing Loans*



The most significant indicator of the loan portfolio quality is the share of non-performing loans. Out of total non-performing loans, corporate loans hold a share of 66% and retail loans a share of 34%, as was the case at the end of 2015. In the reporting period of 2016, the share of non-performing loans in both the retail and the corporate segment dropped. Out of total approved corporate loans, non-performing loans hold a share of 15.3% or KM 953 million, which is down by 1.4 percentage points compared to the end of 2015 (this share fell by 1.6 percentage points in 2015). The aforementioned amounts to 8.4% or KM 498 million in the retail segment, down by 0.6 percentage points (the share dropped by 0.7 percentage points in 2015).

A more detailed and comprehensive analysis is based on information on loan concentration by industry sector for the corporate segment (by sector) and for the retail segment (by purpose).

Table 23: *Concentration of Loans by Industry Sector*

DESCRIPTION	31.12.2015				30.09.2016				INDEX	
	Total loans		Non-performing loans		Total loans		Non-performing loans			
	Amount	Share %	Amount	Share %	Amount	Share %	Amount	Učešće %		
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)	121 964	1.1	20 754	17.0	124 997	1.0	19 446	15.6	102	94
Production (IND)	1 662 318	14.3	352 021	21.2	1 743 039	14.4	334 316	19.2	105	95
Construction (CON)	437 853	3.8	116 850	26.7	415 181	3.4	76 459	18.4	95	65
Trade (TRD)	2 298 963	19.8	303 715	13.2	2 353 250	19.4	297 249	12.6	102	98
Catering (HTR)	196 355	1.7	24 929	12.7	240 208	2.0	23 959	10.0	122	96
Other[24]	1 187 610	10.2	168 937	14.2	1 355 741	11.2	201 971	14.9	114	120
TOTAL 1.	5 905 063	50.9	987 206	16.7	6 232 416	51.4	953 400	15.3	106	97
2. Retail loans for:										
General consumption	4 503 904	38.8	301 755	6.7	4 710 211	38.8	308 177	6.5	105	102
Housing	1 088 139	9.3	181 511	16.7	1 057 849	8.7	163 124	15.4	97	90
Business activities (small business owners)	113 638	1.0	31 461	27.7	127 048	1.0	26 599	20.9	112	85
TOTAL 2.	5 705 681	49.1	514 727	9.0	5 895 108	48.6	497 900	8.4	103	97
TOTAL (1. + 2.)	**11 610 744**	**100.0**	**1 501 933**	**12.9**	**12 127 524**	**100.0**	**1 451 300**	**12.0**	**104**	**97**

[24] 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.

The largest share in total corporate loans refers to the trade sector (19.4%) and the production sector (14.4%), while the retail segment is dominated by general consumption loans (38.8%) and housing loans (8.7%), which is approximately the same level as at the end of 2015.

For an extensive period of time, the negative and strong effect of the economic crisis is especially pronounced in several key sectors, which is evident from the indicator of the share of non-performing loans. The construction sector, which has a low share of merely 3.4% in total loans, still has a high share of non-performing loans in the amount of 18.4%, with a further downward trend: in the first nine months of 2016, it dropped by as much as 8.3 percentage points (in 2015, it dropped by 2.4 percentage points). Also, the agricultural sector, despite the lowest share of 1%, has a high share of non-performing loans in the amount of 15.6%, which fell by 1.4 percentage points compared to the end of the previous year.

However, the focus is on the two sectors with the highest share in total loans – the trade sector (19.4%) and the production sector (14.4%). The amount of loans to the production sector (KM 1.7 billion) was up by 5% or KM 81 million, while non-performing loans decreased by 5% or KM 18 million in the first nine months of 2016, i.e. to the level of KM 334 million, which affected the drop in the share from 21.2% to 19.2% (in 2015, the drop amounted to 7% or KM 25 million, and the share amounted to 21.2%, down by 2.4 percentage points). On the other hand, trade sector lending was up by 2% or KM 54 million in the first nine months of 2016, i.e. to the level of KM 2.4 billion. Non-performing loans in this sector went down by 2% or KM 6 million, amounting to KM 297 million as of 30.09.2016, while the share amounted to 12.6%, down by 0.6 percentage points (in 2015, a drop of 13% or KM 46 million was recorded and the share dropped from 15.4% to 13.2%), which is a significantly better indicator compared to that of the production sector.

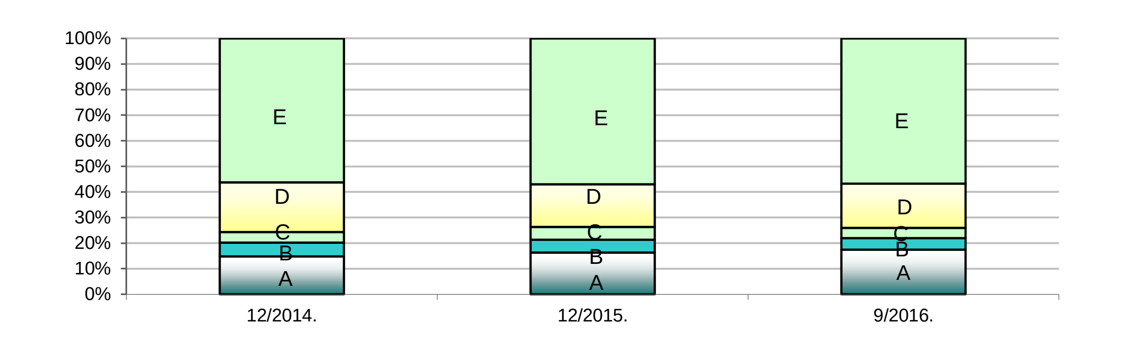
The retail segment is dominated by general consumption loans, which also have the largest share in total loans (38.8%). In the first nine months of 2016, these loans recorded an increase in the amount of 5% or KM 206 million, but the largest relative increase was recorded by small business owners (12% or KM 13 million), while housing loans went down by 3% or KM 30 million. The poorest indicator of the non-performing loans share in the amount of 20.9% (at the end of 2015: 27.7%) refers to loans to small business owners whose share in total loans is a low 1%. A relatively high share of non-performing loans in the amount of 15.4% refers to housing loans (at the end of 2015: 16.7%), while general consumption loans hold the lowest share of non-performing loans in the amount of 6.5% (at the end of 2015: 6.7%).

The general credit risk level and estimated potential loan losses by classification category, as determined in accordance with the criteria and methodology defined by the decisions of the Agency, along with their trend and structure at the banking sector level, is provided in the table and graph below.

Table 24: *Structure and Trend of General Credit Risk and Potential Loan Losses*

Classification category	AMOUNT (in KM 000) AND STRUCTURE (in %)						INDEX	
	31.12.2014		31.12.2015		30.09.2016			
1	2	3	4	5	6	7	8 (4/2)	9 (6/4)
A	229 895	14.8	246 321	16.3	261 607	17.4	107	106
B	83 031	5.4	76 023	5.0	68 619	4.6	92	90
C	64 168	4.1	75 796	5.0	59 703	4.0	118	79
D	301 942	19.5	252 682	16.7	261 041	17.3	84	103
E	872 039	56.2	856 701	57.0	852 578	56.7	98	99
TOTAL	1 551 075	100.0	1 507 523	100.0	1 503 548	100.0	97	100

Graph 19: *Structure and Trend of General Credit Risk and Potential Loan Losses*



Based on an analysis of the calculated loan loss reserves (in aggregate terms and by classification category) compared to the end of 2015, the reserves for general credit risk (category A) and potential loan losses are at the same level of KM 1.5 billion. The reserves for general credit risk are up by 6% or KM 15 million, while the reserves for potential loan losses are down by 1% or KM 19 million compared to the end of 2015. The reserves for category B are down by 10% or KM 7 million and amount to KM 67 million, while the reserves for non-performing assets are down by 1% or KM 12 million, i.e. amount to KM 1.2 billion, mostly on the basis of the reserves for category C and E being down by 21% or KM 16 million and 1% or KM 4 million, respectively.

One of the key indicators of asset quality is the ratio between potential loan losses (PLL) and risk-bearing assets with off-balance sheet items. This ratio amounts to 8% and is down by 0.5% compared to the end of 2015.

As of 30.09.2016, banks had an average calculated reserves in the amount of 8% for category B, 25% for category C, 60% for category D and 100% for category E (at the end of 2015: 8% B, 25% C, 59% D, and 100% E).[25]

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 reserves).

An overview of total assets items (balance sheet and off-balance sheet) and default items, as well as relevant value adjustments and provisions (defined in accordance with the banks' internal methodologies, the minimum contents of which are regulated by decisions of the Agency) is provided in the table below.

Table 25: *Assessment and Valuation of Risk-Bearing Items According to IAS 39 and IAS 37*

Description	AMOUNT (in KM 000) AND SHARE (in %)				INDEX
	31.12.2015		30.09.2016		
	Amount	Share	Amount	Share	
1	2	3	4	5	6 (4/2)
1. RISK-BEARING ASSETS (a+b)	**14 850 813**	**100.0%**	**15 475 203**	**100.0%**	104
a) Default items	**1 681 006**	11.3%	**1 628 181**	10.5%	97
a.1. BS-items in default	1 662 958		1 609 847		97
a.2. off-BS items in default	18 048		18 334		102
b) Performing assets	**13 169 807**	88.7%	**13 847 022**	89.5%	105
1.1 TOTAL VALUE ADJUSTMENTS FOR RISK-BEARING ASSETS (a+b)	**1 269 548** **100.0%**	**100.0%**	**1 269 910**	**100.0%**	100

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

a) Value adjustments for default	**1 117 269**	88.0%	**1 102 302**	86.8%	97
a.1. Value adjustment for BS-items in default	1 110 757		1 091 803		98
a.2. reserves for off-BS items in default	6 512		10 499		161
b) Value adjustments for performing assets (IBNR[26])	152 279	12.0%	167 608	13.2%	110
2. TOTAL LOANS (a+b)	**11 610 744**	**100.0%**	**12 127 524**		104
a) Defaulted loans (non-performing loans)	1 605 754	13.8%	1 552 735	12.8%	97
b) Performing loans	10 004 990	86.2%	10 574 789	87.2%	106
2.1. VALUE ADJUSTMENT FOR LOANS (a+b)	**1 181 736**	**100.0%**	**1 173 181**	**100.0%**	99
a) Value adjustments for defaulted loans	1 061 476	89.8%	1 042 818	88.9%	98
b) Value adjustments for performing loans (IBNR loans)	120 260	10.2%	130 363	11.1%	108
Coverage rate of default items	**66.5%**		**67.7%**		
Coverage rate of performing assets	**1.2%**		**1.2%**		
Coverage rate of risk-bearing assets with total value adjustments	**8.5%**		**8.2%**		

In the first three quarters of 2016, default loans went down by 3% or KM 53 million (in 2015: down by 7% or KM 115 million), while non-performing loans decreased by 3% or KM 51 million. The share of default loans in total loans is down by 1.0 percentage point and amounts to 12.8% and the share of non-performing loans amounts to 12%. The share of all default items in total risk-bearing assets is down by 0.8 percentage points and amounts to 10.5%.

The coverage rate of default items with value adjustments is up and amounts to 67.7% (at the end of 2015: 66.5%) due to the nominal drop in the amount of default (KM 53 million) being larger than the drop in value adjustments for default (KM 15 million). The coverage rate of non-performing assets with loan loss reserves is slightly up and amounts to 76.5% (at the end of 2015: 74.8%).

The coverage rate of performing assets remains the same and amounts to 1.2%, while the coverage rate of risk-bearing assets with total value adjustments is slightly down and amounts to 8.2% (at the end of 2015: 8.5%). The coverage ratio of risk-bearing assets with total calculated regulatory reserves for loan losses (reserves for general credit risk and special reserves for loan losses) decreased from 10.2% to 9.7%.

In order to mitigate the negative effects of the natural disaster, on 30.06.2014, the Agency adopted the Decision on Provisional Measures for Treatment of Loan Commitments of Bank Clients Affected by Natural Disasters.[27]

Acting in accordance with the aforementioned Decision, in the second half of 2014, banks in the Federation of B&H approved moratoriums on loan commitments in the amount of KM 34 million. As of 30.09.2016, the balance of the aforementioned loans amounts to KM 6 million, KM 4 million of which refer to legal entities and KM 2 million of which refer to natural persons.

Also, in accordance with the aforementioned Decision, in the second half of 2014, banks in the Federation of B&H approved restructurings of loan commitments in the total amount of KM 39 million. As of 30.09.2016, the balance of the restructured loans amounts to KM 37 million, KM 36 million of which refer to legal entities and KM 1 million of which refer to natural persons. Restructured loans also include loans with a grace period following the expiration of the moratorium.

As of 30.09.2016, loans approved in accordance with the aforementioned Decision have a very low share in relation to total loans: moratorium 0.05% and restructuring 0.30%.

[26] IBNR (identified but not reported) – latent losses.
[27] "Official Gazette of the Federation of B&H", No. 55/14.

The upward trend of uncollectable receivables, i.e. customer defaults in the payment of past due loan commitments, has caused the activation of the guarantor's obligation in a certain number of defaulted loans (with this form of security). As of 31.12.2009, the Agency has prescribed a report on the repayment of loans by guarantors in order to collect, monitor and analyse information on loans being repaid by guarantors. According to the reports filed by banks in the Federation of B&H as of 30.09.2016, there was a total of 1 152 990 loan accounts, 1 078 of which were being repaid by guarantors (1 243 guranators). The share of loans and number of loan accounts being repaid guarantors in relation to information for the overall system is low and amounts to a mere 0.23% and 0.1%.

An analysis of asset quality, i.e. the quality of the loan portfolio of individual banks, as well as on-site controls in the banks themselves, indicate that credit risk is the dominant risk in most banks and the fact that some banks have inadequate practices for managing, i.e. assessing, measuring, monitoring and controlling credit risk and for classifying assets is worrisome, which our on-site examinations determined on the basis of major amounts related to the shortfall of loan loss reserves (which were later on adequately formed as per the Agency's orders). Also, the analysis of asset quality in banks grouped according to ownership structure revealed that ratios of banks in majority ownership of residents (5 "local" private banks) were worse than those of banks in majority foreign ownership (10 banks).

The share of non-performing loans in banks that are in majority foreign ownership amounts to 11% (12/15: 11.7%), while it amounts to 26% (12/15: 30.4%) in "local banks". This is the result of inadequate and weak systems for credit risk management, especially in relation to the key stage – loan approval, as well as the result of an underdeveloped risk function. Major weaknesses and inefficient practices were also identified in the preventive actions stage, i.e. in the early recognition of problems in loan settlement (servicing), as well as when handling non-performing assets in the interest of reducing such assets through collection or sound restructuring.

Banks, in which the Agency identified (through bank examinations) low asset quality and poor practices of credit risk management and/or which displayed adverse trends, i.e. decrease in asset quality, were ordered to apply corrective actions in the sense of drafting an operational program for the management of non-performing assets, which had to contain an action plan for the improvement of existing practices of credit risk management, i.e. asset quality management, for the reduction of existing concentrations and for solving the problem of non-performing assets and preventing their further impairment, as well as for strenghtening the risk function, i.e. its significance and quality. Compliance with the Agency's orders is being continuously monitored through an intensified post-control process based on reports and other documentation submitted by banks, as well as through targeted on-site controls. The supervision of this segment of operations has been intensified due to evident negative trends significantly affecting and causing the deterioration of the banks' profitability and the weakening of the capital base of certain banks, due to which banks need to take timely actions to obtain capital from external sources.

Transactions with Related Entities

In their business operations, banks are exposed to different risks, with the risk of transactions with their related entities being especially significant.

In accordance with the Basel Committee standards, the Agency has established prudential principles and requirements for bank transactions with related entities, as regulated by the Decision on Minimum Standards for Banks' Operations with Related Entities, which defines the conditions and manner of the banks' business operations with related parties. Based on this Decision and the Law on Banks, a bank's Supervisory Board (acting on the Director's proposal) is required to adopt special bank policies for operations with related entities and to monitor their implementation.

The Agency's Decision also prescribes a special set of reports on transactions with one part of related entities, encompassing loans and contingent and assumed off-balance sheet liabilities (guarantees, letters of credit, assumed loan commitments) 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 approved 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.

- KM 000 -

Table 26: *Transactions with Related Entities*

Description	LOANS APPROVED[28]			INDEX	
	31.12.2014	31.12.2015	30.09.2016	3/2	4/3
1	2	3	4	5	6
To shareholders with over 5% voting rights, subsidiaries and other related entities	160 135	89 014	115 257	56	129
To members of the Supervisory Board and Audit Board	409	446	627	109	141
To the Management of the bank	1 994	3 023	2 864	152	95
TOTAL	162 538	92 483	118 748	57	128
Contingent and assumed off-balance sheet liabilities	21 826	9 326	11 343	43	122

During the reporting period, loan exposures to related entities increased by 28%, while contingent liabilities increased by 22% due to increased exposure with respect to two banks. Based on the presented information, it can be concluded that the volume of loans and guarantees with related entities is still low, as is the level of risk. However, it is evident that this risk is significantly higher in banks that have a dispersed ownership structure, i.e. in „local banks" owned by residents. The Agency pays special attention (during its on-site controls) to the banks' operations with related entities, especially in terms of assessing their system of identification and monitoring of risk exposure in transactions with related entities. The Agency's examiners give on-site orders for eliminating identified omissions within certain time frames and also initiate violation proceedings, the integral part being monitoring and overseeing the compliance with the issued orders in the post-control procedure. This has reflected positively on this segment of their operations since banks have significantly improved the quality of their risk management in this segment.

2.2. Profitability

According to data from the income statement, a positive financial result – profit in the amount of KM 172 million (down by 1% or KM 2 million compared to the same period of the previous year and up by 45% or KM 55 million compared to profit recorded in 2015[29]) was recorded at the level of the banking system in the Federation of B&H in the first nine months of 2016. The positive effect on the financial result at system level is particularly due to 13 banks that had operated positively in the same period of the previous year as well having recorded higher profit (effect KM 32 million). On the other hand, a negative effect in the amount of KM 34 million is primarily the result of a significant loss recorded by one bank (KM 32 million) as well as lower profit recorded by one bank (app. KM 2 million). Compared to the same period of the previous year, the number of banks is lower by one due to a merger, the financial result of which was capitalised following the completion of the status change process (as of

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

[29] After the completed audit of financial statements for 2015, a financial result – profit (after taxes) in the amount of KM 117 million was recorded at the level of the banking system.

31.07.2016).

The key effect on the improved profitability of most banks is still primarily the result of the application of a new methodological approach (implementation of IAS 37/39 starting from 31.12.2011), which led to lower value adjustment costs. A decrease in interest income is still being compensated for by a significantly greater decrease in interest expenses, resulting in an increase in net interest income, which, together with the still good operating profitability (increase in operating income on the basis of fees and the efficient management of operating expenses), had an affect on higher profit being recorded compared to the same period of the previous year when it comes to the majority of banks.

A positive financial result in the amount of KM 211 million was recorded by 14 banks and it is up by 16% or KM 30 million compared to the same period of the previous year. At the same time, an operating loss in the amount of app. KM 38 million was recorded by two banks.

More detailed data is shown in the following table.

- KM 000 -

Table 27: *Recorded Financial Result: Profit/Loss*

Description	30.09.2014		30.09.2015		30.09.2016	
	Amount	Number of banks	Amount	Number of banks	Amount	Number of banks
1	2	3	4	5	6	7
Loss	-29 423	2	-7 088	2	-38 439	2
Profit	153 395	15	180 998	15	210 821	14
Total	**123 972**	**17**	**173 910**	**17**	**172 382**	**16**

As in other segments, this segment also shows some concentrations: out of the total profit (KM 211 million), 64% or KM 135 million refer to the two largest banks in the system with an assets share of 47% in the banking sector, while the total loss in the amount of KM 38 million mostly refers to one bank (99%). Analytical data indicates that a total of 14 banks has a better financial result (by KM 32 million), while 2 banks have a poorer financial result (by KM 34 million).

Based on analytical data as well as on indicators for the assessment of profitability quality (i.e. the level of the recorded 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 the overall profitability of the system has deteriorated slightly with respect to one bank due to a large loss, while it has improved for the majority of banks, especially with respect to larger banks that recorded greater profit compared to the same period of the previous year. This is primarily the result of the new implemented methodological approach and, in the case of the largest banks, also the result of an increase in income based on service fees. However, a profitability assessment that is based solely on the recorded financial result would not be an adequate assessment since other important factors that affect sustainability and quality of earnings, i.e. profit, should also be taken into account. In that sense, it is of outmost importance to emphasise credit risk and negative trends in asset quality over the past few years through the increase in non-performing and uncollectable loans, with it being noted that a downward trend in terms of non-performing loans has been present since the second half of 2015 (both in accordance with IAS and the regulatory definition of NPL), primarily as a result of the significant amount of the permanent write-off, which does not correlate with the reduction of value adjustment costs (following the implementation of IAS 39 and 37), this being the most important factor affecting the improvement of the financial result in most banks over the past four years. Although the coverage of loans in the status of default with value adjustments (in accordance with IAS 39) at system level has increased since the second half of 2015 (it amounted to 61.5% as of 30.06.2015 and to 67.2% as of 30.09.2016), the aforementioned leads to the conclusion and suspicion that value adjustments are underestimated and not at an adequate level in some banks.

At system level, total income amounted to KM 711 million, up by 5% or KM 32 million compared to the same period of the previous year, primarily as a result of increased operating income. Total non-interest bearing expenses amounted to KM 538 million, with a growth rate of 7% or KM 33 million compared to the same period of the previous year, which had a negative impact on the total financial result of the sector.

Despite the increase in average interest-bearing loans (in the majority of banks) by 3.8% as well as the fact that the increase in non-performing loans was halted (mostly on the basis of write-offs), the reduced average interest rate on loans, which is the result of a decrease in active interest rates resulted in a slight decrease in terms of interest income. Although a number of banks recorded an increase in interest income as a result of increased credit activity compared to the same period of the previous year, significantly lower interest income in the case of two large banks mainly influenced the decrease at system level. Interest income amounts to KM 563 million, which is down by 2% or KM 9 million compared to the previous year, with the share in the structure of total income being down from 84.3% to 79.3%. The largest share refers to loan interest income, which amounts to KM 503 million and recorded a drop of 2% or KM 13 million, with the share in total income dropping from 75.9% to 70.7%, which was partially depreciated by an increase in other interest income, mostly on the basis of investments in securities.

The long-standing downward trend with respect to interest expenses was continued in 2016 as well. Compared to the same period of the previous year, interest expenses had a significantly higher rate of decrease (-16%) compared to the rate of decrease of interest income (-2%). In nominal terms, interest expenses are down by KM 24 million and interest income by KM 9 million. Interest expenses amounted to KM 126 million, and their share in the structure of total income went down from 22% to 17.7%. In the structure of interest expenses, it should be noted that interest expenses on deposits in the amount of KM 109 million, despite the increase in average interest-bearing deposits by 6%, are down by 17% or KM 22 million as a result of the structure of the deposit base (i.e. a larger share of deposits with a lower interest rate), but also as a result of the banks' interest rate policy and the continuous decrease in interest rates on deposits, which ultimately led to average interest rates on deposits for the parallel period being down from 1.88% to 1.48%. Interest expenses on loans taken and other borrowings, as well as subordinated debt, recorded a decrease of 18% or KM 3 million compared to the same period of the previous year, with the share in total income dropping from 2.6% to 2%, which correlates with the continuous decrease in this source of funding for banks.

As a result of the decrease in interest expenses (-16%) being significantly higher than the decrease in interest income (-2%), net interest income went up by 3% or KM 15 million and amounts to KM 438 million, with its share in the total income structure dropping from 62.3% to 61.6%.

Operating income amounts to KM 273 million and is up by 7% or KM 17 million compared to the same period of the previous year, with its share in the total income structure increasing to 38.4% (+0.7 percentage points). Within operating income, the largest share refers to service fees, with them also having recorded an increase of 11% or KM 18 million. It can be concluded that banks are compensating for the drop in interest income with a continuous increase in service fees.

Total non-interest expenses amount to KM 538 million and are up by 7% or KM 33 million compared to the same period of the previous year, which is, despite business and direct expenses being down (exclusively value adjustment costs), the result of higher operating expenses. Their share in the total income structure increased from 74.4% to 75.8%. Value adjustment costs amount to KM 64 million and are down by 18% or KM 14 million compared to the same period of the previous year (a significant KM 10 million decrease in one large bank had the largest impact on this), which is positively reflected in their share in the total income structure being down from 11.5% to 9.1%.

On the other hand, operating expenses in the amount of KM 402 million and with a share of 56.5% in total income are up by 11% or KM 38 million, mostly on the basis of an increase in other operating expenses, which are up by 52% or KM 38 million (largely as a result of one bank having recorded an increase in the amount of KM 33 million). Salary and contribution costs, as the largest item of operating expenses, went slightly down by 0.8%, amounting to KM 180 million or 25.4% of total income, while costs of fixed assets went up by 2%, amounting to KM 109 million and thus having a share of 15.4% in total income. After the crisis emerged, banks took numerous measures to rationalise costs of operations, primarily to reduce operating expenses, which has partly mitigated adverse effects of the interest income decrease caused by the lower volume of lending activities and decrease in loan portfolio quality.

The trend and structure of total income and total expenses is provided in the tables and graphs below.

- in KM 000 -

Table 28: *Total Income Structure*

Total income structure	30.09.2014		30.09.2015		30.09.2016		INDEX	
	Amount	%	Amount	%	Amount	%		
1	2	3	4	5	6	7	8 (4/2)	9 (6/4)
I Interest income and similar income								
Interest-bearing deposit accounts at deposit institutions	3 069	0.4	1 065	0.1	1 354	0.2	35	127
Loans and leasing facilities	519 657	63.5	515 294	62.2	502 582	60.1	99	98
Other interest income	55 066	6.7	55 964	6.8	59 423	7.1	102	106
TOTAL	577 792	70.6	572 323	69.1	563 359	67.4	99	98
II Operating income								
Service fees	176 261	21.6	187 459	22.6	206 479	24.7	106	110
Income from FX deals	33 836	4.1	36 716	4.4	38 580	4.6	109	105
Other operating income	30 465	3.7	31 674	3.9	27 848	3.3	104	88
TOTAL	240 562	29.4	255 849	30.9	272 907	32.6	106	107
TOTAL INCOME (I + II)	818 354	100.0	828 172	100.0	836 266	100.0	101	101

Graph 20: *Total Income Structure*

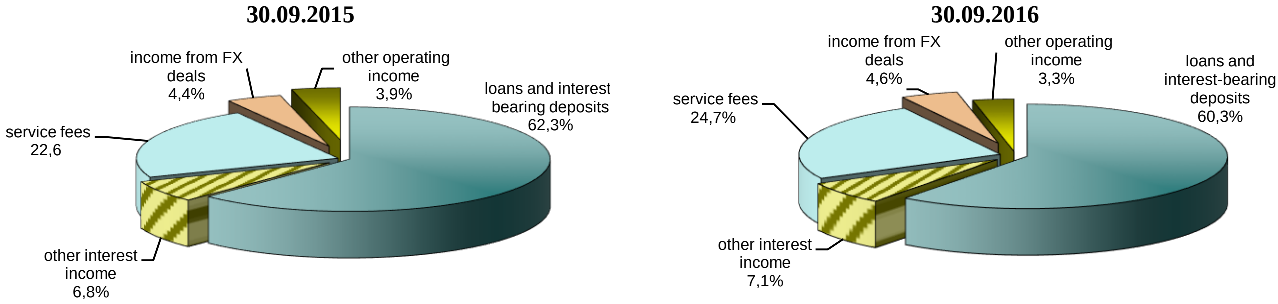
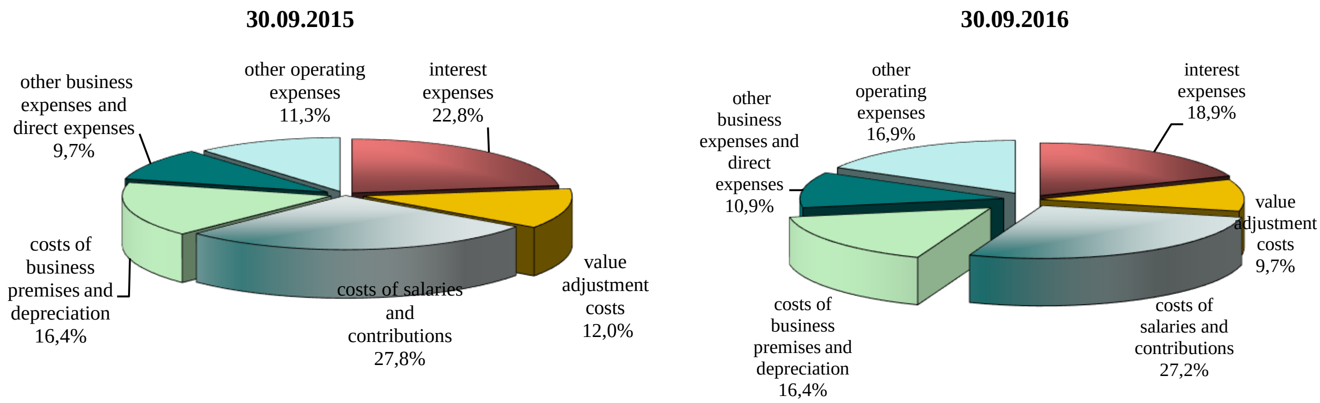


Table 29: *Total Expenses Structure*

Total expenses structure	30.09.2014		30.09.2015		30.09.2016		INDEX	
	Amount	%	Amount	%	Amount	%		
1	2	3	4	5	6	7	8 (4/2)/	9 (6/4)
I Interest expenses and similar expenses								
Deposits	145 632	21.0	130 556	20.0	108 927	16.4	90	83
Liabilities based on loans and other borrowings	14 694	2.1	11 401	1.7	8 854	1.3	78	78
Other interest expenses	10 177	1.5	7 213	1.1	7 775	1.2	71	108
TOTAL	170 503	24.6	149 170	22.8	125 556	18.9	87	84
II Total non-interest bearing expenses								
Costs of value adjustment of risk-bearing assets and provisions for contingent liabilities and other value	104 641	15.0	78 303	12.0	64 455	9.7	75	82

adjustments								
Costs of salaries and contributions	184 319	26.5	181 956	27.8	180 480	27.2	99	99
Costs of business premises and depreciation	108 389	15.6	107 437	16.4	109 094	16.4	99	102
Other business expenses and direct expenses	58 772	8.5	63 570	9.7	72 274	10.9	108	114
Other operating expenses	67 758	9.8	73 788	11.3	112 025	16.9	109	152
TOTAL	523 879	75.4	505 054	77.2	538 328	81.1	96	107
TOTAL EXPENSES (I + II)	694 382	100.0	654 224	100.0	663 884	100.0	94	101

Graph 21: *Total Expenses Structure*



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

- in % -

Table 30: *Profitability, Productivity and Efficiency Ratios by Period*

RATIOS	30.09.2014	30.09.2015	30.09.2016
Profit from average assets	0.8	1.1	1.0
Profit from average total capital	5.2	6.9	6.4
Profit from average share capital	10.1	13.8	14.8
Net interest income/average assets	2.6	2.6	2.5
Operating income/average assets	1.5	1.6	1.6
Total income/average assets	4.2	4.2	4.1
Business expenses and direct expenses[30]/average assets	1.1	0.9	0.8
Operating expenses/average assets	2.3	2.2	2.3
Total non-interest bearing expenses/average assets	3.4	3.1	3.1

An analysis of key ratios for the assessment of profitability shows that they have changed only slightly, with the exception of the ROAE (return on average equity), which improved from 13.8% to 14.8% as a result of reduced average share capital (largely due to significant loss coverage in one bank). The ROAA (return on average assets) amounted to 1.0% and the banks' productivity indicator, measured as a ratio between total income and average assets, amounted to 4.1%. Reduced value adjustment costs resulted in a slight improvement of the business expenses and direct expenses/average assets ratio (from 0.9% to 0.8%).

In negative conditions of the banks' operations and prompted by effects of the economic and financial crisis on the banking sector of the Federation of B&H, the profitability of banks will continue to be mostly affected by and will depend on two key factors: a) the further trend of assets quality, i.e. the level of loan losses and credit risk, and b) the efficiency of management and control over operating income and operating expenses. On the other hand, it is necessary to maintain the upward trend of credit

[30] Expenses also include value adjustment costs.

growth in order to increase the banks' profitability, along with applying and strictly observing prudent lending standards when it comes to loan approval. Also, the banks' profit, i.e. their financial result, will be largely affected by the price and interest rate risk in terms of both sources of funding and an interest margin sufficient enough to cover all non-interest bearing expenses and thus eventually ensure satisfactory profit related to capital invested by bank owners. Therefore, a key factor for the efficiency and profitability of every bank is the quality of management and business policies, as well as the quality and efficiency of risk management systems, since this directly affects its performances.

2.3. Weighted Nominal and Effective Interest Rates

In the interest of greater transparency and easier comparability of banks' loan approval terms and deposit taking terms, as well as in the interest of customer protection by means of introducing transparent disclosure of loan approval costs, i.e. deposit income, all in accordance with international standards, criteria and practices in other countries, on 01.07.2007, the Agency prescribed a uniform manner of calculating and disclosing the effective interest rate[31] for all banks seated in the Federation of B&H as well as the organisational units of banks from Republika Srpska operating on the territory of the Federation of B&H. The effective interest rate represents an actual loan price, i.e. income earned on a deposit, expressed as an annual percentage.

The effective interest rate is a decursive interest rate calculated on an annual level by applying complex interest calculation in such a manner that discounted cash receipts are brought to an equivalent level with discounted cash expenditures related to the approved loans, i.e. related to the received deposits.

Banks are required to report to the Agency on a monthly basis regarding weighted nominal and effective interest rates on loans and deposits approved/received in the reporting month in question, all in accordance with regulated methodology.[32]

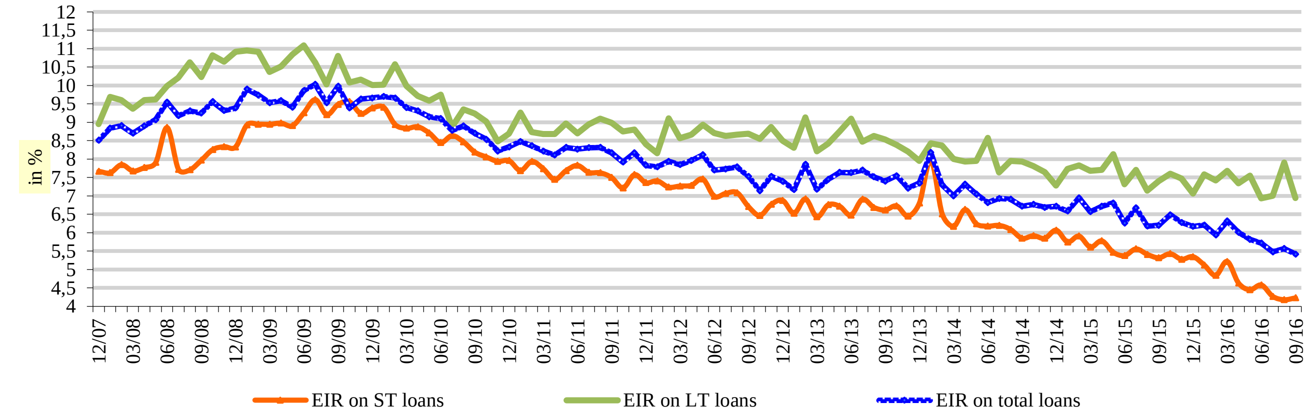
The table below shows an overview of weighted nominal and effective interest rates (hereinafter: NIR and EIR) on loans at the banking sector level and for two key customer segments (corporate and retail) for December 2014, June, September, and December 2015, as well as June and September 2016.

Table 31: *Weighted Average NIR and EIR on Loans*

DESCRIPTION	12/2014		06/2015		09/2015		12/2015		06/2016		09/2016	
	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR
1	2	3	4	5	6	7	8	9	10	11	12	13
1. Weighted IR on short-term loans	5.58	6.07	5.01	5.35	4.94	5.33	4.89	5.35	4.15	4.58	3.89	4.23
1.1. Corporate	5.55	5.99	4.99	5.26	4.9	5.23	4.84	5.25	4.08	4.42	3.92	4.21
1.2. Retail	6.57	8.90	7.66	11.47	7.86	11.94	8.21	11.74	8.05	14.68	8.25	15.0
2. Weighted IR on long-term loans	6.00	7.28	6.49	7.24	6.51	7.4	6.18	7.06	5.93	6.93	5.88	6.94
2.1. Corporate	5.29	6.76	5.47	5.84	5.45	5.8	5.31	5.67	4.66	4.97	4.93	5.31
2.2. Retail	7.50	8.60	7.35	8.44	7.32	8.65	7.1	8.55	7.15	8.82	7.02	8.78
3. Total weighted IR on loans	5.80	6.72	5.69	6.21	5.6	6.2	5.51	6.17	5.01	5.72	4.76	5.42
3.1. Corporate	5.43	6.32	5.13	5.43	5.02	5.36	4.99	5.38	4.26	4.59	4.18	4.48
3.2. Retail	7.44	8.62	7.36	8.53	7.34	8.75	7.13	8.64	7.17	8.98	7.05	8.96

[31] Decision on Uniform Method of Calculation and Disclosure of Effective Interest Rate on Loans and Deposits („Official Gazette of the Federation of B&H", No. 48/12 – consolidated text and 23/14).
[32] 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 Nominal and Effective Interest Rate.

Graph 22: *Weighted Average Monthly EIR on Loans by Maturity*



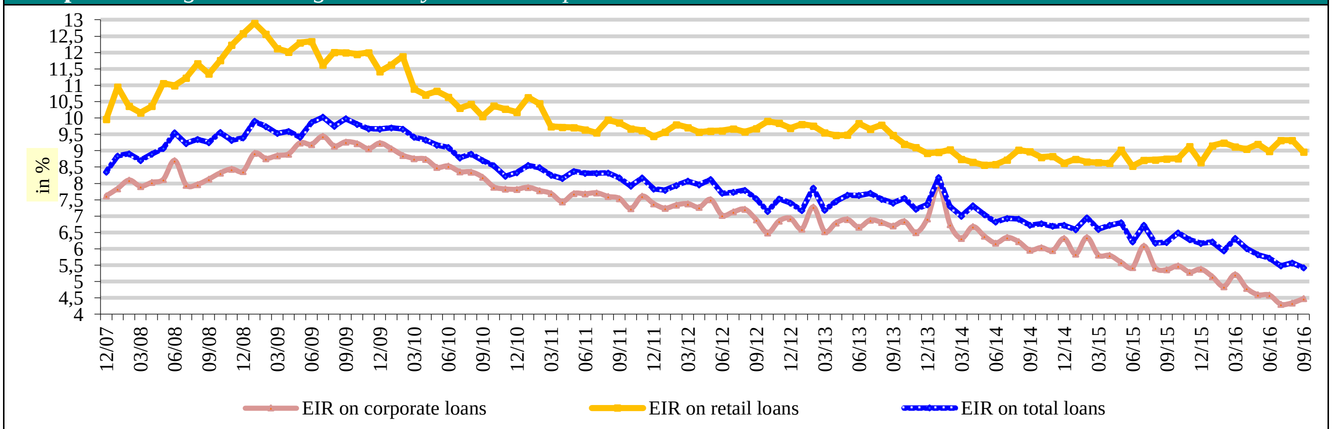
When analysing interest rate trends, it is important to monitor trends of the weighted EIR, with the difference between this interest rate and the weighted NIR representing a fee and commission paid to the bank for an approved loan (and this is factored in the loan price calculation). This is why the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

In the first three quarters of 2016, the weighted EIR on loans recorded oscillations within the range of 0.9 percentage points, with the highest rate having been recorded in March (6.32%) and the lowest in September (5.42%). Weighted interest rates on short-term loans recorded oscillations within the range of 1.12 percentage points, while those on long-term ones were within the range of 0.98 percentage points.

The weighted EIR on short-term loans stood at 4.23% in September 2016, which is down by 1.12 percentage points compared to December 2015, while the weighted EIR on long-term loans amounted to 6.94%, down by 0.12 percentage points compared to December 2015.

Interest rates on loans to the two most important sectors: corporate and retail[33], had opposite trends in the reporting period of 2016. Interest rates on corporate loans recorded a further slight downward trend, while the weighted EIR on retail loans were generally somewhat higher compared to the previous year, as shown in the graph below.

Graph 23: *Weighted Average Monthly EIR on Corporate and Retail Loans*



[33] According to the methodology of sector classification, small business owners are included in the retail sector.

The weighted EIR on corporate loans is still significantly lower than the EIR on retail loans, having amounted to 4.48% in September 2016 (12/2015: 5.38%). In the case of long-term corporate loans, the EIR dropped from 5.67% to 5.31%, while the EIR on short-term loans saw a decrease in the amount of 1.04 percentage points (from 5.25% to 4.21%).

The EIR on retail loans was 8.96% in September 2016, which is up by 0.32 percentage points compared to the level in December 2015. The EIR on short-term loans to this sector increased from the level of 11.74% in December 2015 to 15.0%, with it being noted that such a high effective interest rate level has been recorded since March 2016 at the monthly level, whereas the EIR was below 11% in January and February 2016. The EIR on long-term retail loans recorded a slight increase, having amounted to 8.78% in September 2016, which is up by 0.23 percentage points compared to December 2015.

When observing the period of the last five years, it is evident that there is a moderate, but continuous decrease in the weighted average EIR on loans calculated on an annual basis, primarily in the corporate sector, while the retail sector's continuous decrease from previous years was halted in 2015. Following that, a slight increase was recorded in the first three quarters of 2016 (although nominal interest rates on retail loans have a slight downward trend, the EIR is up due to increased fees and other related loan costs), as can be seen in the following table.

Table 32: *Weighted Average NIR and EIR on Loans per Annum and for Three Quarters of 2016*

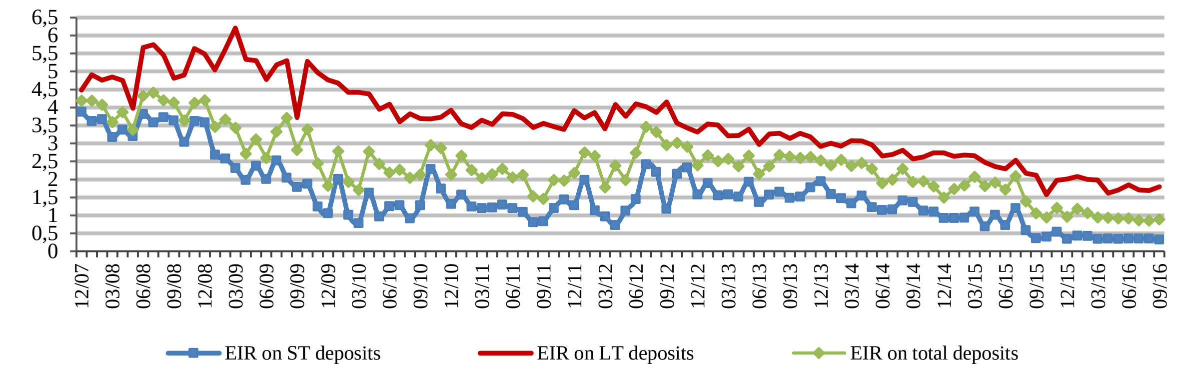
DESCRIPTION	2012		2013		2014		2015		Three quarters of 2016	
	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR
1	2	3	4	5	6	7	8	9	10	11
1. Weighted IR on short-term loans	6.45	7.01	6.17	6.66	5.72	6.25	5.10	5.50	4.14	4.58
1.1. Corporate	6.43	6.94	6.22	6.66	5.70	6.17	5.07	5.42	4.10	4.45
1.2. Retail	8.41	11.52	8.09	11.08	7.98	11.39	7.84	11.37	7.89	13.61
2. Weighted IR on long-term loans	7.78	8.70	7.66	8.48	6.98	7.80	6.60	7.57	6.23	7.33
2.1. Corporate	6.86	7.51	6.65	7.12	6.19	6.81	5.63	6.20	4.98	5.29
2.2. Retail	8.44	9.57	8.35	9.40	7.66	8.66	7.36	8.65	7.25	8.99
3. Total weighted IR on loans	6.99	7.70	6.82	7.46	6.32	6.98	5.81	6.48	5.07	5.81
3.1. Corporate	6.52	7.07	6.33	6.78	5.84	6.35	5.23	5.64	4.33	4.68
3.2. Retail	8.44	9.68	8.33	9.48	7.68	8.77	7.37	8.74	7.28	9.14

Weighted NIR and EIR on term deposits for the banking sector, calculated on the basis on monthly reports, are shown in the table below.

Table 33: *Weighted Average NIR and EIR on Deposits*

DESCRIPTION	12/2014		06/2015		09/2015		12/2015		06/2016		09/2016	
	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR
1	2	3	4	5	6	7	8	9	10	11	12	13
1. Weighted IR on short-term deposits	0.92	0.93	0.72	0.73	0.37	0.37	0.34	0.35	0.36	0.36	0.33	0.33
1.1. up to three months	0.42	0.42	0.27	0.27	0.13	0.13	0.21	0.21	0.25	0.25	0.28	0.28
1.2. up to one year	1.94	1.97	1.26	1.28	1.04	1.06	1.18	1.25	0.72	0.76	0.66	0.67
2. Weighted IR on long-term deposits	2.67	2.74	2.25	2.29	2.12	2.12	1.92	2.01	1.81	1.85	1.79	1.80
2.1. up to three years	2.40	2.48	2.21	2.26	1.82	1.83	1.67	1.68	1.65	1.70	1.43	1.44
2.2. more than three years	3.41	3.43	2.33	2.33	2.88	2.89	2.46	2.72	2.23	2.21	2.51	2.52
3. Total weighted IR on deposits	1.47	1.50	1.69	1.72	1.05	1.06	0.92	0.96	0.90	0.92	0.89	0.89

Graph 24: *Weighted Average Monthly EIR on Deposits*



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

Compared to December 2015, weighted EIR on short-term, long-term and total term deposits recorded only slight changes, i.e. their slight downward trend continued. The weighted EIR on total term deposits amounted to 0.89%, which is down by 0.07 percentage points compared to December 2015.

The weighted EIR on short-term deposits stood at 0.33% in September 2016, slightly down compared to December 2015. The highest one was recorded in January 2016, when it amounted to 0.44%. The weighted EIR on long-term deposits recorded slight oscillations within the range of 0.46 percentage points, amounting to 1.80% (December 2015: 2.01%).

When analysing the trends of interest rates on short-term deposits by maturity, the EIR on term deposits up to three months increased slightly by 0.07 percentage points and amounted to 0.28%. On the other hand, the interest rate on term deposits up to one year recorded a slightly larger drop and amounted to 0.67% (12/2015: 1.25%).

The weighted EIR on long-term deposits up to three years is 1.44%, which is a slight drop in the amount of 0.24 percentage points compared to the level in December 2015. The EIR on term deposits over three years was 2.52% in September 2016, down by 0.2 percentage points compared to December 2015, when the aforementioned amounted to 2.72%.

The average EIR on retail deposits is down by 0.17 percentage points compared to December 2015 and amounts to 1.57%. In the corporate sector, the average EIR stood at 1.60% in September 2016 (December 2015: 1.81%).

When analysing the trends of weighted average interest rates on deposits per annum in the last five years, a continuous decrease in interest rates on long-term deposits is evident, while interest rates on short-term deposits are also at the lowest level in the last five years, with present oscillations, as can be seen in the table below.

Table 34: *Weighted Average NIR and EIR on Deposits per Annum and for Three Quarters of 2016*

DESCRIPTION	2012		2013		2014		2015		Three quarters of 2016	
	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 short-term deposits	1.45	1.47	1.65	1.67	1.20	1.23	0.60	0.61	0.36	0.37

1.1. up to three months	0.86	0.88	1.47	1.47	0.79	0.80	0.27	0.28	0.28	0.28
1.2. up to one year	2.55	2.57	1.85	1.87	1.72	1.76	1.25	1.28	0.71	0.73
2. Weighted IR on long-term deposits	3.78	3.81	3.20	3.23	2.79	2.82	2.20	2.23	1.80	1.82
2.1. up to three years	3.69	3.71	2.97	3.00	2.61	2.64	2.08	2.10	1.60	1.63
2.2. more than three years	4.44	4.50	4.15	4.18	3.32	3.34	2.48	2.52	2.36	2.37
3. Total weighted IR on deposits	2.61	2.64	2.51	2.53	2.04	2.07	1.41	1.43	0.94	0.95

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

Table 35: *Weighted Average NIR and EIR on Overdraft Facilities and Call Deposits*

DESCRIPTION	12/2014		06/2015		09/2015		12/2015		06/2015		09/2015	
	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR
1	2	3	4	5	6	7	8	9	10	11	12	13
1. Weighted IR on overdraft facilities	8.05	8.22	7.91	8.08	7.96	8.16	7.81	8.01	7.26	7.45	7.16	7.35
2. Weighted IR on call deposits	0.13	0.13	0.11	0.11	0.09	0.09	0.09	0.09	0.08	0.08	0.07	0.07

The weighted EIR on total overdraft facilities for the banking sector in September 2016 amounted to 7.35% (down by 0.66 percentage points compared to December 2015) and to 0.07% on call deposits (slightly lower compared to December 2015). As a rule, the EIR on these assets and liabilities items is equal to the nominal interest rate.

2.4. Liquidity

Along with credit risk management, liquidity risk management is one of the most important and most complex segments of banking operations. Liquidity maintenance within the market economy is a permanent liability of the bank and the basic premise for its sustainability on the financial market, along with being a key precondition to establishing and preserving trust in the banking system of any country as well as in the banking system's stability and safety.

Until the onset of the global financial and economic crisis, in normal operating conditions of banks and a stable environment, the liquidity risk was of secondary importance to banks, 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 for the purpose of being improved and upgraded.

When financial markets got disrupted due to the effect of the global crisis, liquidity risk suddenly gained importance and managing this risk became a key factor for smooth operations, the timely handling of liabilities due and the preservation of the long-term position of the bank in terms of its solvency and capital base. In addition, it is worth noting that the interdependence of all risks the bank is or may be exposed to in its operations has also come to light with the onset of the crisis.

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

The banking sector in the FB&H also maintained good performances in the area of liquidity risk in the following years, basic indicators of liquidity, largely thanks to reduced lending activities, have improved, and the biggest changes took place in the maturity structure of sources, primarily deposits, due to the continuous reduction of the exposure to parent groups, whose deposits in several banks in majority foreign ownership were the main source of funding for the aggressive credit growth that was recorded in the years leading up to the crisis. Also, there is a continuous trend of reduced liabilities to foreign financial institutions-creditors, which is also part of the deleveraging process and the banks' strategic orientation toward domestic deposits as the main source of funding credit growth.

The 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 a very good maturity adjustment of financial assets and liabilities. Still, due to the still present effect and impact of the economic crisis, it was found that the liquidity risk should still be kept under close supervision. Also, it should be kept in mind that the effect of the crisis on the real sector is still present, with its negative consequences reflected in the overall industrial and economic environment in which banks in B&H operate, thus resulting in defaults in terms of the settlement of loan obligations and increases in uncollectable receivables, i.e. reductions of inflows of liquid funds to banks and the conversion of credit risk into liquidity risk. In that sense, one of key influences on the liquidity position of banks in the period to come will be their capacity to adequately manage their assets, which encompasses obtaining assets with good performances and the quality of which ensures that bank loans (and interest) are repaid in accordance 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 the development and implementation of the liquidity policy that ensures the bank’s capacity to meet its obligations on the maturity date fully and without a delay.

This regulation represents a framework for 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 compared to short-term sources of funds, as well as minimum limits of the maturity adjustment of instruments of financial assets and financial liabilities (up to 180 days).

In the structure of the sources of funding of FB&H banks as of 30.09.2016, the largest share of 76.4% still refers to deposits, followed by loans taken (including subordinated debt[34]) with a share of 5.4%. Loans taken have longer maturities and represent a quality source for the approval of long-term loans, while also improving the maturity adjustment of assets and liabilities items, although a downward trend of the aforementioned has been evident for an extensive period of time.

On the other hand, the maturity structure of deposits is much more unfavourable,[35] with changes in the direction of trends in the past few years being present. After improving and an increase in the share of long-term deposits in the period from 2011 to 2013, 2014 saw a stagnation, while a slight deterioration was recorded in 2015, which continued in 2016 as well.

- in KM 000 -

Table 36: *Maturity Structure of Deposits by Contractual Maturity*

DEPOSITS	31.12.2014		31.12.2015		30.09.2016		INDEX	
	Amount	Share %	Amount	Share %	Amount	Share %		
1	2	3	4	5	6	7	8(4/2)	9(6/4)
Savings and call deposits	5 771 888	47.6	6 645 840	50.8	7 280 623	53.5	115	110
Up to 3 months	279 332	2.3	266 464	2.0	171 408	1.3	95	64
Up to 1 year	701 041	5.8	679 876	5.2	632 412	4.6	97	93
1. Total short-term deposits	6 752 261	55.7	7 592 180	58.0	8 084 443	59.4	112	106
Up to 3 years	3 437 563	28.3	3 502 798	26.7	3 449 015	25.3	102	98

[34] Subordinated debt: loans taken and permanent items.

[35] As per remaining maturity.

More than 3 years	1 940 922	16.0	2 004 005	15.3	2 073 646	15.3	103	103
2. Total long-term deposits	5 378 485	44.3	5 506 803	42.0	5 522 661	40.6	102	100
TOTAL (1 + 2)	12 130 746	100.0	13 098 983	100.0	13 607 104	100.0	108	104

Compared to the end of 2015, total deposits recorded an increase in the amount of 4% or KM 508 million, with changes in their sectoral structure, which is mostly due to deposits of all sectors being up (in nominal terms, retail deposits and deposits of private companies saw the largest increase by 5% or KM 349 million and 7% or KM 138 million, respectively), with the exception of deposits of banking institutions, which still have a downward trend (down by 23% or KM 176 million). With a share of 57.4%, retail deposits are the largest sectoral source of funding of banks in the FB&H.

The maturity structure of deposits with contractual maturity has had a continuous slight downward trend since 2012. In the reporting period of 2016, the share of short-term deposits increased from 58.0% to 59.4%, while the share of long-term deposits decreased from 42.0% to 40.6%.

Changes in the maturity structure stem from an increase in short-term deposits by 6% or KM 492 million as a result of an increase in retail deposits by KM 273 million, deposits of private companies by KM 153 million, deposits of fovernment institutions by KM 70 million, deposits of public companies by KM 59 million, deposits of non-banking financial institutions by KM 39 million, while deposits of banking institutions recorded a drop in the amount of KM 107 million. Long-term deposits are slightly up by KM 16 million as a result of deposits up to three years being down by 1.5% or KM 54 million, mostly those belonging to the sector of private companies and banking financial institutions, while deposits with a term over three years went up by 3.5% or KM 70 million, primarily on the basis of retail deposits, deposits of non-banking financial institutions, and deposits of private companies being up. It should be noted that long-term deposits are still dominated by two segments: retail, with the share increasing from 68.4% to 69.6%, and public companies, with an unchanged share of 9%. In deposits with a term from one to three years, the largest share of 72.6% (+1.0 percentage point) is held by retail deposits, followed by public companies (12.7%, +0.1 percentage points). Deposits over three years mostly consist of retail deposits (64.6%, +1.6 percentage points), while deposits of banking institutions, with a long-lasting trend of decrease that has slowed down somewhat, have a share of 13.0% (at the end of 2015: 15.9%).

Although the 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).

- in KM 000 -

Table 37: *Maturity Structure of Deposits by Remaining Maturity*

DEPOSITS	31.12.2014		31.12.2015		30.09.2016		INDEX	
	Amount	Share %	Amount	Share %	Amount	Share %		
1	2	3	4	5	6	7	8(4/2)	9(6/4)
Savings and call deposits (up to 7 days)	5 874 183	48.4	6 852 863	52.3	7 394 522	54.3	117	108
7- 90 days	898 335	7.4	770 687	5.9	786 362	5.8	86	102
91 days to one year	2 054 981	17.0	2 080 342	15.9	2 015 390	14.8	101	97
1. Total short-term deposits	8 827 499	72.8	9 703 892	74.1	10 196 274	74.9	110	105
Up to 5 years	3 150 040	26.0	3 190 290	24.3	3 211 663	23.6	101	101
More than 5 years	153 207	1.2	204 801	1.6	199 167	1.5	134	97
2. Total long-term deposits	3 303 247	27.2	3 395 091	25.9	3 410 830	25.1	103	100
TOTAL (1 + 2)	12 130 746	100.0	13 098 983	100.0	13 607 104	100.0	108	104

Based on the data above, it can be concluded that the maturity structure of deposits by remaining maturity is much worse due to a high share of short-term deposits in the amount of 74.9%, with a trend of slight deterioration in 2016. Compared to the end of 2015, short-term deposits increased by 5% or KM 492 million, with the share being up by 0.8 percentage points, while there is a trend of stagnation when it comes to long-term deposits, with the share in total deposits dropping from 25.9% to 25.1%.

When analysing the structure of long-term deposits, it is evidently dominated by deposits with remaining maturity of up to 5 years (94.2% of long-term deposits and 23.6% of total deposits). Although the reduction of deposits with remaining maturity of over 5 years was halted in 2014, when a moderate increase of 17% or KM 23 million was recorded, with an increase in the amount of 34% or KM 52 million recorded in 2015, there was a decrease in the amount of 3% or KM 5.6 million in 2016. When comparing information on deposit maturities by contractual and residual maturity, it can be concluded that out of the KM 5.5 billion of total long-term contracted deposits, there were approximately KM 2.1 billion, i.e. 38%, of long-term contracted deposits with the remaining maturity of up uo one year as of 30.09.2016.

The existing maturity structure of deposits (being the largest source of funding of banks in the Federation of B&H) has become an increasingly limiting factor of credit growth in relation to most banks since they incline more towards approving long-term loans. Therefore, banks are faced with the problem of finding ways to obtain quality sources of funding in terms of maturity, especially due to the considerably reduced inflow of financial assets (borrowings) from abroad, i.e. both from parent groups and financial institutions-creditors, while local sources of funding are mostly short-term. In June 2014, the FBA amended the existing regulations on liquidity.[36] Having previously met the prescribed requirements and obtained the approval of the FBA, banks have the opportunity to use a certain amount (i.e. a corrective amount) of retail call deposits for loans with longer maturities. As of 30.09.2016, five banks are using a corrective amount (KM 383 million) after being granted approval by the FBA, with it being noted that one more bank was granted approval for the use of a corrective amount in October 2016, while another one that has applied for the use of the corrective amount is undergoing an assessment process related to whether or not it meets the requirements. The objective of the regulation amendment is primarily aimed at stimulating credit growth, mostly real sector lending, and positive effects have already been recorded.

However, supervisory concern is also present due to to the fact that banks, due to the lack of quality long term-sources of funding and for the purpose of ensuring compliance with legally defined limits related to maturity adjustment, resort to approving revolving short-term loans, i.e. settling existing ones with new short-term facilities, which basically means long-term lending from short-term sources of funding. In such a way, the real loan maturity and its adjustment with sources of funding is being kept hidden. This may become a serious problem in the period to come as well as a potential threat to the bank's liquidity position.

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

- in KM 000 -

Table 38: *Maturity Structure of Loans*

LOANS	31.12.2014		31.12.2015		30.09.2016		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	1 210 806	10.8	1 186 501	10.2	1 181 703	9.7	98	100
Short-term loans	2 256 837	20.2	2 283 316	19.7	2 425 589	20.0	101	106

[36] Decision on Amending the Decision on Minimum Standards for Liquidity Risk Management in Banks („Official Gazette of the Federation of B&H", No. 46/14)

Long-term loans	7 702 634	69.0	8 140 927	70.1	8 520 232	70.3	106	105
TOTAL LOANS	11 170 277	100.0	11 610 744	100.0	12 127 524	100.0	104	104

In the first three quarters of 2016, long-term loans were up by 5% or KM 379 million, amounting to KM 8.5 billion, and short-term loans were up by 6% or KM 142 million, amounting to KM 2.4 billion, while past due receivables amounted to KM 1.2 billion, slightly down by KM 5 million, primarily as a result of a permanent write-off in the amount of KM 58 million, which is yet another indicator of the deterioration of the collection rate of past due loan commitments and the difficulties that debtors have in servicing their debt towards banks in light of the effects of the economic crisis. In the structure of past due receivables, 64.5% refers to private companies, 33.3% to the retail sector and 2.2% to other sectors.

An analysis of maturities of two key sectors shows that 86% of retail loans are long-term loans, while 53% of total approved loans refers to private companies.

In the structure of assets, loans, as the key category, still hold the largest share of 68.1%, up by 0.4 percentage points compared to the end of 2015, and recorded a slight increase of 4% in the first three quarters of 2016. Cash funds decreased by 1% or KM 26 million and their share dropped from 28.3% to 27.1% compared to the end of 2015.

An overview of the main liquidity ratios is provided in the table below.

- in % -

Table 39: *Liquidity Ratios*

Ratios	**31.12.2014**	**31.12.2015**	**30.09.2016**
1	2	3	4
Liquid assets[37]/total assets	28.5	28.4	27.3
Liquid assets/short-term financial liabilities	49.1	48.4	45.9
Short-term financial liabilities/total financial liabilities	69.3	70.0	71.3
Loans/deposits and loans taken[38]	84.9	82.9	84.0
Loans/deposits, loans taken and subordinated debt[39]	83.9	82.2	83.3

In the reporting period of 2016, the ratios deteriorated slightly due to a drop in cash funds, due to the increase in loans being larger than the increase in deposits, and due to a decrease in loans taken.

After deteriorating in 2012, the ratio of loans/deposits and loans taken improved in 2013 (from 88.1% to 86.4%), and the same trend continued in 2014 and 2015 as well. However, as of 30.09.2016, the ratio deteriorated to 84.0% (+1.1 percentage points) as a result of the increase in loans being larger than the increase in deposits. The ratio was above 85% (critical level) with respect to 7 banks. On the one hand, this was the result of their liabilities structure (relatively significant share of capital) and, on the other hand, the result of the high share of loans in assets. During its on-site controls, the Agency paid special attention to banks with identified weaknesses in this business segment and instructed them to take actions and measures to improve the liquidity level, as well as practices of managing sources of funding in order to ensure a satisfactory liquidity position.

[37] In narrow terms, liquid assets are: cash and deposits and other financial assets with remaining maturity of less than 3 months (excluding interbank deposits).

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

[39] The previous ratio was expanded and sources now include subordinated debt, thus being a more realistic indicator.

In 2016, banks have duly fulfilled the requirement of maintaining the defined level of the required reserve at the Central Bank of B&H.[40] The required reserve, being the key instrument of the monetary policy in B&H in relation to the Currency Board and the financially undeveloped market, is the only instrument of the monetary policy that ensures monetary control in sense of the prevention of rapid growth of loans and reduced multiplication, as well as increased liquidity in banks in conditions of crisis and a higher outflow rate of funds from banks (as compared to the situation in B&H as of 01.10.2008). On the other hand, the implementation of foreign currency risk regulations and the maintenance of currency adjustment to the defined limits has also significantly impacted the amount banks hold in their reserve accounts at the Central Bank of B&H (in local currency), thus ensuring a high liquidity of banks, individually and at the banking sector level.

All banks continuously meet and significantly exceed the defined minimum of the 10-day average of 10% in relation to short-term sources of funding and the daily minimum of 5% in relation to the same basis, as illustrated in the table below.

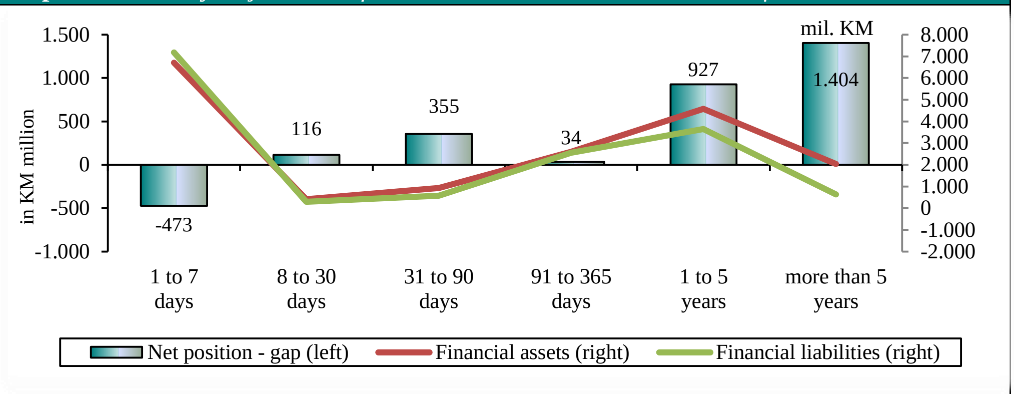
- in KM 000 -

Table 40: *Liquidity Position – 10-Day Average and Daily Minimum*

	31.12.2014 Iznos	31.12.2015 Iznos	30.09.2016 Iznos	INDEX	
1	2	3	4	5(3/2)	6(4/3)
1. Average daily balance of cash	4 060 671	4 592 752	4 740 689	113	103
2. Lowest total daily cash balance	3 797 970	4 310 524	4 546 157	114	105
3. Short-term sources of funding (calculation basis)	6 351 607	7 358 839	8 170 200	116	111
4. Amount of liabilities:					
4.1. 10-day average 10% of the amount under item 3	635 161	735 884	817 020	116	111
4.2. daily minimum 5% of the amount under item 3	317 580	367 942	408 510	116	111
5. Performance of liabilities: 10-day average					
Surplus = item no. 1 – item no. 4.1.	3 425 510	3 856 868	3 923 669	113	102
6. Performance of liabilities: daily minimum					
Surplus = item no. 2 – item no. 4.2.	3 480 390	3 942 582	4 137 647	113	105

When observing the maturity adjustment of remaining maturities of total financial assets[41] and liabilities, it can be concluded that the adjustment rate is good, although somewhat lower compared to 31.12.2015.

Graph 25: *Maturity Adjustment of Financial Assets and Liabilities as of 30.09.2016*



[40] The Decision on Establishing and Maintaining Required Reserves and Determining the Remuneration of the CBBH to Banks on the Reserve Amount was published in the "Official Gazette of B&H", No. 30/16 and is in application since 1 July 2016.
[41] Financial assets are posted on a net basis (after deductions for value adjustments).

As of 30.09.2016, short-term financial assets of banks in the amount of KM 10.6 billion were higher than short-term liabilities by KM 32 million. Compared to the end of 2015, when the positive gap amounted to KM 234 million, this represents a decrease of KM 202 million or 86.4%, which led to the coverage ratio for short-term liabilities deteriorating from 102.3% to 100.3%.

Short-term financial assets increased by 3.1% and short-term financial liabilities by 5.2%. In the structure of short-term financial assets, the largest increase in the amount of 4.8% or KM 205 million was recorded with respect to net loans, followed by trading assets (10.5% or KM 93 million), cash borrowings to other banks (89.0% or KM 56 million), and other financial assets (4.1% or KM 7 million), while a decrease was recorded with respect to cash funds (0.5% or KM 26 million) and securities held to maturity (14.8% or KM 10 million). Financial assets with remaining maturity of over one year increased by 4.9% or KM 306 million, mostly as a result of loans being up by 5.2% or KM 321 million.

Liabilities with maturity of up to one year (KM 10.6 billion) increased (+5.2%), with changes in the following items: an increase in deposits (up by 5.1% or KM 492 million), other financial liabilities (up by 16.0% or KM 33 million), and loan commitments (up by 0.3% or KM 0.5 million). Liabilities with maturity of over one year (KM 4.3 billion) recorded a slight drop in the amount of 1.3% or KM 56 million, primarily as a result of a decrease in loan commitments by 9.7% or KM 72 million.

In addition to the said prescribed minimum standard, a very important aspect of the monitoring and analysis of the liquidity position is the maturity adjustment of remaining maturities of financial assets and liabilities items in accordance with the time scale created to capture a time horizon of 180 days in line with the prescribed minimum limits.[42]

- in KM 000 -

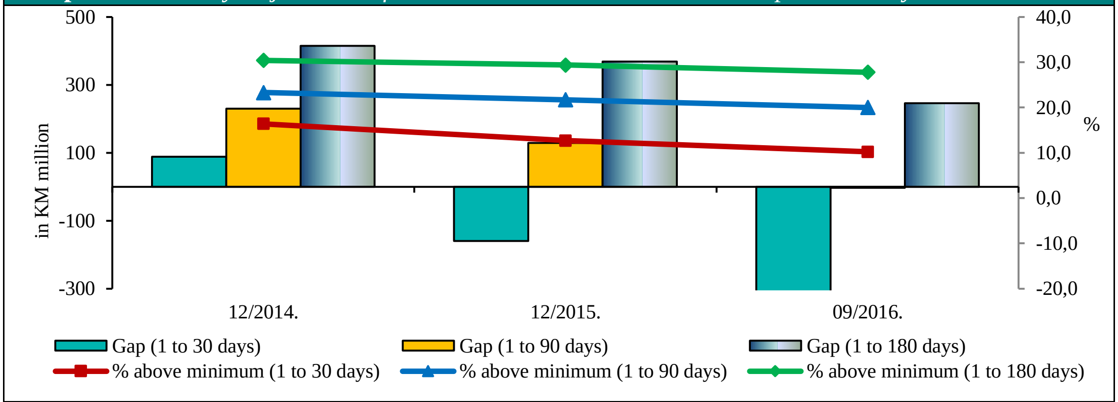
Table 41: *Maturity Adjustment of Financial Assets and Liabilities – up to 180 Days*

Description	31.12.2014 Amount	31.12.2015 Amount	30.09.2016 Amount	INDEX	
1	2	3	4	5 (3/2)	6(4/3)
I. 1- 30 days					
1. Financial assets	6 303 761	6 878 280	7 112 227	109	103
2. Financial liabilities	6 215 782	7 037 944	7 469 684	113	106
3. Difference (+ or -) = 1-2	87 979	-159 664	-357 457	n/a	n/a
Calculation of prescribed requirement in %					
a) Actual %= no. 1/no. 2	101.4%	97.7%	95.2%		
b) Prescribed minimum %	85.0%	85.0%	85.0%		
Plus (+) or minus (-) = a - b	16.4%	12.7%	10.2%		
II. 1-90 days					
1. Financial assets	7 132 287	7 750 227	8 035 999	109	104
2. Financial liabilities	6 901 893	7 621 496	8 038 524	110	105
3. Difference (+ or -) = 1-2	230 394	128 731	-2 525	56	n/a
Calculation of prescribed requirement in %					
a) Actual %= no. 1/no. 2	103.3%	101.7%	100.0%		
b) Prescribed minimum %	80.0%	80.0%	80.0%		
Plus (+) or minus (-) = a - b	23.3%	21.7%	20.0%		
III. 1-180 days					
1. Financial assets	8 062 506	8 735 123	9 013 934	108	103
2. Financial liabilities	7 647 885	8 365 780	8 768 424	109	105
3. Difference (+ or -) = 1-2	414 621	369 343	245 510	89	66
Calculation of prescribed requirement in %					
a) Actual %= no. 1/no. 2	105.4%	104.4%	102.8%		
b) Prescribed minimum %	75.0%	75.0%	75.0%		
Plus (+) or minus (-) = a - b	30.4%	29.4%	27.8%		

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

Based on the information presented, it is found that, as of 30.09.2016, banks have adhered to prescribed limits and achieved a better maturity adjustment of financial assets and liabilities in relation to the prescribed limits.

Graph 26: *Maturity Adjustment of Financial Assets and Liabilities – up to 180 Days*

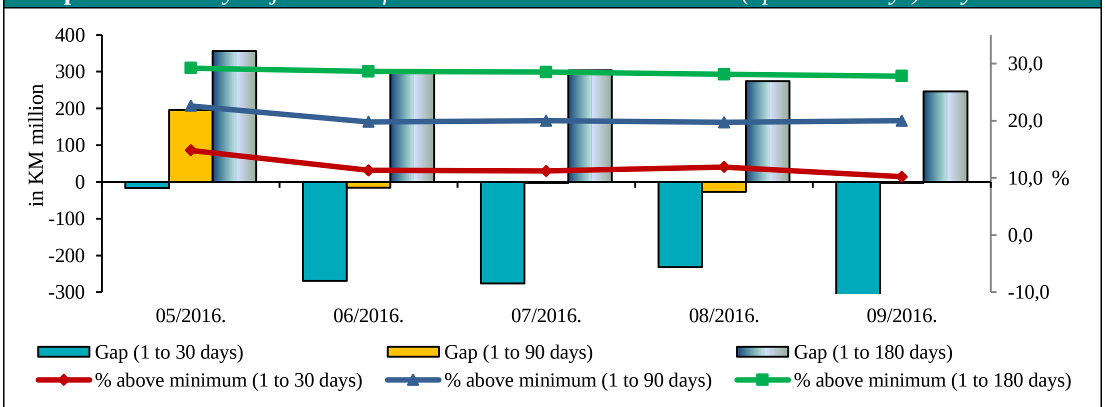


As of 30.09.2016, financial assets in the first and second period were lower than financial liabilities, due to the increase in financial liabilities, primarily deposits and other financial liabilities, being higher than the increase in financial assets (an increase in net loans, trading assets, borrowings to other banks, securities held to maturity, and other financial assets). Despite financial liabilities being up, financial assets surpassed financial liabilities in the third period, due to an increase in assets (primarily an increase in net loans, borrowings to other banks, and trading assets).

As a result of the aforementioned, the recorded maturity adjustment percentages in all three periods were somewhat lower than at the end of 2015, but still significantly above the prescribed minimum by 10.2% in the first period, 20.0% in the second period, and 27.8% in the third period.

The chart below shows the trend of the maturity adjustment of financial assets and liabilities in the period from May to September 2016 (by period of time and maturity adjustment percentages in relation to the legally defined minimum standards).

Graph 27: *Maturity Adjustment of Financial Assets and Liabilities (up to 180 Days) – by Period*



Based on all presented ratios, the liquidity of the banking system in the Federation of B&H is still deemed satisfactory. However, we should underline that banks should pay even more attention to liquidity risk management in the period to come by means of establishing and implementing liquidity policies that would ensure the settlement of all liabilities due in a timely manner and based on continuous planning of future liquidity needs while factoring in changes in operating, economic, regulatory and other conditions of the banks' business environment since this business segment and the exposure level to liquidity risk correlate with credit risk, and also considering the effects of the financial crisis on B&H and the banking sector of the Federation of B&H (primarily in the sense of increased pressure on the banks' liquidity). On the one hand, this rests on the poor maturity structure of deposits, the repayment of loan commitments due and a much smaller amount of borrowings from financial institutions (which, over the past few years, were the best source of funding for banks from a maturity perspective) and, on the other hand, of the poor inflow of liquid funds due to a decreased collection rate of loans.

Through its off-site and on-site controls of banks, the Agency will continue to monitor and oversee the manner in which banks manage this risk and whether they act in accordance with adopted policies and programmes.

2.5. FX Risk – Foreign Currency Adjustment of Balance Sheet and Off-Balance Sheet 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 the foreign currency risk arising as a result of changes in exchange rates and/or unadjusted levels of 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 the 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 Agency has adopted the Decision on Minimum Standards for Foreign Exchange Risk Management in Banks[43], which regulates minimum standards for adopting and implementing the programmes, policies and procedures for 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.[44]

In order for the Agency to monitor the banks' compliance with the regulated limits and their exposure level to FX risk, banks are required to report daily to the Agency. Based on the review, monitoring and analysis of the submitted reports, it can be concluded that banks adhere to regulated limits and conduct their FX activities within such limits.

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

As of 30.09.2016, the currency structure of banks' assets included 10.1% or KM 1.8 billion of foreign currency items (at the end of 2015, these items amounted 11.5% or KM 2 billion). On the other hand, the currency structure of liabilities is quite different since the share of foreign currency liabilities is much higher and equals 39.3% or KM 7 billion (at the end of 2015, this share was 41.6% or KM 7.1 billion).

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

---

[43] "Official Gazette of the Federation of B&H", No. 48/12 – consolidated text.

[44] Article 7 of the Decision on Minimum Standards for Foreign Exchange Risk Management in Banks defines the following limits: for the individual FX position – up to 30% of the core capital for EUR, up to 20% for other currencies and up to 30% for the total bank position.

- in KM million -

Table 42: *FX Adjustment of Financial Assets and Liabilities (EUR and Aggregate)* [45]

Description	31.12.2015				30.09.2016				INDEX	
	EURO		TOTAL		EURO		TOTAL		EURO	TOTAL
	Amount	Share %	Amount	Share %	Amount	Share %	Amount	Share %	Amount	Share %
1	2	3	4	5	6	7	8	9	10	11
I. Financial assets										
1. Cash	839	10.7	1 311	15.3	589	7.8	1 066	13.0	70	81
2. Loans	29	0.4	31	0.4	26	0.3	27	0.3	90	87
3. Loans with a currency clause	6 510	82.6	6 595	76.9	6 369	84.3	6 409	78.1	98	97
4. Other	500	6.3	636	7.4	407	5.4	539	6.6	81	85
5. Other financial assets with a currency clause[46]	N/a	N/a	N/a	N/a	168	2.2	169	2.0	N/a	N/a
Total (1+2+3+4)	7 878	100.0	8 573	100.0	7 559	100.0	8 210	100.0	96	96
II. Financial liabilities										
1. Deposits	5 498	72.8	6 153	74.9	5 438	72.8	6 056	74.8	99	98
2. Loans taken	810	10.7	812	9.9	745	10.0	745	9.2	92	92
3.Deposits and loans with a currency clause	1 076	14.2	1 076	13.1	1 102	14.7	1 102	13.6	102	102
4. Other	170	2.3	176	2.1	183	2.5	195	2.4	108	111
Total (1+2+3+4)	7 554	100.0	8 217	100.0	7 468	100.0	8 098	100.0	99	99
III. Off-balance sheet										
1. Assets	37		48		59		94			
2. Liabilities	129		208		170		218			
IV.Position										
Long (amount)	232		196							
%	12.7%		10.7%							
Short					20		12			
%					1.0%		0.6%			
Allowed	30%		30%		30%		30%			
Lower than the allowed level	17.3%		19.3% 23.9%		29.0%		29.4%			

In terms of the structure of foreign currencies, the dominant share among financial assets[47] is held by the EUR with 62.6% (31.12.2015: 69.2%), along with a drop in the nominal amount (from KM 1.4 billion to KM 1 billion). The share of the EUR in liabilities is at the same level (91.0%), coupled with a decrease in the nominal amount by KM 112 million.

However, FX risk exposure calculation also includes the amount of indexed assets items (loans and other financial assets) and liabilities items[48], which is quite significant on the assets side (80.1% or KM 6.6 billion) and which is at approximately the same level as at the end of 2015 (76.9% or KM 6.6 billion). Other FX items on the assets side hold a share of 19.9% or KM 1.6 billion and have the following structure: items in EUR 12.4% or KM 1.0 billion and other currencies 7.4% or KM 0.6 billion (at the end of 2015, other items in EUR held a share of 16.0% or KM 1.4 billion). Out of total net loans (KM 11.0 billion), app. 58.5% have a currency clause (mostly pegged to the EUR – 99.4%).

---

45 Source: Form 5 – FX position.

46 Items on this position as of 31.12.2015 are listed on position 3. Loans with a currency clause.

47 Source: Form 5 – FX position: one part of financial assets (foreign currencies denominated in KM). According to the calculation methodology, financial assets were posted in accordance with the net principle until 31.12.2011 (i.e. after deductions for loan loss reserves), after which the new methodology entailed the depreciation of fixed assets according to IAS, i.e. after deductions for value adjustments and reserves for contingent liabilities

48 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).

As for the sources of funding, financial liabilities condition and determine the structure of financial assets items for every currency. The largest share in FX liabilities (KM 8.1 billion) is 78.6% or KM 6.4 billion and refers to items in EUR, mostly deposits (at the end of 2015, the share of liabilities in EUR amounted to 78.8% or KM 6.5 billion). The share and amount of indexed liabilities in the last five years (with the exception of 2013, when a drop in the amount of 13% or KM 117 million was recorded) have had an upward trend from when they amounted to KM 661 million in 2011, thus having a share of 8%, to the level of KM 1.1 billion (with a 13.6% share) as of 30.09.2016. The increase in indexed liabilities (almost all relate to deposits) is conditioned, on the one hand, by the outflow of deposits and loan commitments in foreign currencies, which have been a source of loans approved with a currency clause, and, on the other hand, by the continuously high amount of loans with a currency clause. In order to maintain the FX adjustment, banks are increasing indexed liabilities items (deposits), with it being noted that most banks have a long FX position.

When observing banks and the banking sector level of the Federation of B&H, it can be concluded that FX risk exposure of banks and the banking system in 2016 was within the defined limits. As of 30.09.2016, the long FX position was recorded with 8 banks and the short position with the same number of banks. At system level, there is a short FX position of 0.6% of the total core capital of banks, which is 29.4% below the allowed limit. The individual FX position for the EUR, like the total position, was 1.0%, which is 29.0% below the allowed limit, with financial liabilities being larger than financial assets items (net short position).

Although the currency board protects banks from FX risk exposure related to the EUR, they are required to adhere to regulated limits for all currencies, as well as for the total FX position, and to conduct daily risk management activities in accordance with the adopted programmes, 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 Federation B&H. Future activities should be aimed towards the preservation of its stability, with this being a priority in present stressful conditions, and towards the banking system's future progress and development. These objectives are conditioned by a continuous and committed involvement of all elements of the system, the legislative and executive authorities, thus forming grounds for a more favourable economic environment for banks and the real sector of the economy, as well as for the general population.

The FBA adopted regulations, their improvement and upgrade, as well as operational decisions within its jurisdiction while taking all the prescribed steps whose main goal was for banks to fully ensure the legality, full implementation of the FBA's provisions and the generally accepted principles and practices for their, especially in terms of the ever-present recession, careful and successful work. Furthermore, the insistence and the objectives of the FBA's efforts were aimed at strengthening banks' capital, improving their credit policies and their consistent application in practice, raising caution to the highest level in the management of credit risk, which is still dominant in our environment, and liquidity risk, but also at strengthening the ability to manage a potential crisis situation.

In the period to come, the Banking Agency of the Federation of B&H will, within its competences:

- take measures and actions for more secure and stable banking operations and the banking system as a whole and its support to the economy and the population;
- continue with activities to consolidate the supervision function at state level;

- take measures and actions for the purpose of implementing measures from the Reform Agenda and the Economic Reforms Programme, which are related to the banking and financial sector;
- work to implement the recommendations of the FSAP Mission in order to improve the quality of banking sector supervision;
- continue with activities to draft a regulatory framework (by-laws) in accordance with the adopted Strategy and Annual Plan for the Drafting of Regulations in order to implement Basel II/III and EU directives and as part of the preparation for B&H's joining of the European Union;
- maintain continuous supervision of banks through on-site and off-site examinations, placing an emphasis on dominant risk segments of banking operations and aiming to improve efficiency by means of:
  - further insistence on capital strengthening in banks, especially in those banks with an above average increase in assets and reduction of the capital adequacy ratio,
  - continuing banking supervision that is of systemic importance for the development of lending activities where large savings and other deposits are concentrated (all for the purpose of protecting depositors);
  - continuing system-based monitoring of banks' activities to prevent money laundering and the financing of terrorism and the improvement of the cooperation with other supervisory and regulatory institutions;
  - reviewing and regularly updating the contingency plan as part of crisis preparations,
  - continuing to develop and implement the Early Warning System tool (EWS) for the purpose of an early identification of financial and operational inefficiencies and/or adverse trends in the banks' operations,
  - monitoring the compliance of banks' operations with laws and regulations and the practices employed in banks in the segment of protecting users of financial services and guarantors,
  - establishing and expanding cooperation with supervisory authorities in countries with investors in the banking sector of the FB&H, as well as with other countries in order to maintain effective supervision,
  - continuing the cooperation with the ECB and the EBA and the exchange of information on banking supervision, as well as with international financial institutions, the IMF, the WB, the EBRD, etc.;
  - improving cooperation with the B&H Banks' Association across all segments of the banking business (e.g. introduction of new products, collection of receivables, functioning of the Central Credit Registry of legal entities and natural persons, daily updating of data, etc.), organising consultations and providing professional assistance in the implementation of banking laws and regulations, improving cooperation in the sense of professional training, proposing amendments to all laws or regulations that have become a limiting factor to the banks' development;
- continue with efforts to improve the information system, as an important prerequisite for efficient and proactive banking supervision, i.e. IT support with the function of early warning and preventive actions with respect to the elimination of weaknesses in the banks' operations;
- continue with the on-going training and professional education of the staff;
- accelerate actions regarding the finalisation of the liquidation processes.

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:

- the implementation of activities from the Reform Agenda for Bosnia and Herzegovina for the period 2015-2018;
- the implementation of conclusions reached by the Parliament of the Federation of B&H regarding the establishment of state-level bank supervision;
- the implementation of the Economic Reforms Programme for 2016-2018 (ERP B&H 2016-2018);

- creating and upgrading legislation pertaining to the financial and banking sector, starting with the Basel Principles, Basel Capital Frameworks and European Banking Directives, which refer to the actions, status and operations of banks, and especially to the drafting and adoption of the new Banking Law and the legal framework for the resolution of banks;
- accelerating the implementation of economic reforms in the real sector of the economy in order for it to approach the level achieved in the monetary and banking sector more rapidly;
- the preparation and adoption of the Law on Asset Management Companies;
- the establishment of special commercial departments within courts;
- the establishment of more efficient enforcement proceedings;
- the establishment of a mechanism for out-of-court debt restructuring of companies;
- the creation and adoption of measures for resolving or mitigating the problem of over-indebted persons;
- the adoption of a law or the improvement of existing legislation regulating the area of safety and protection of money in banks and in transit, etc.

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

- increasing the volume of lending activities in order to support the economy, together with full commitment to quality and prudent operations and to combating the crisis effects presently posing the biggest threat to banks, the real sector of the economy and the general population;
- improvement of the risk management system and the system of early identification of loan portfolio deterioration and more effective measures for the resolution of non-performing loans;
- further capital strengthening and ensuring the level of solvency in proportion to the increase in assets and risk, greater profitability, strengthening of the internal control system and the internal audit function as segments that are fully independent in the performance of their duties and roles
- more consistent implementation of adopted policies and procedures to prevent money laundering and the financing of terrorism, the safety and protection of money in banks and in transit, all in accordance with laws and by-laws;
- the implementation of laws and by-laws in the segment of protecting users of financial services and guarantors;
- active participation in the implementation of measures for resolving the problem of individuals' over-indebtedness and the financial consolidation of companies;
- preparing and updating their contingency measures plans;
- regular, timely and accurate submission of information to the Central Credit Registry and the Uniform Central Registry of Accounts at the Central Bank of B&H.

No.: U.O-90-4/16.
Sarajevo, 08.12.2016

ANNEXES

ANNEX 1…………………….. Basic Information on Banks in the Federation of B&H

ANNEX 2…………………..… Balance Sheet of Banks in the Federation of B&H According to the FBA Model

ANNEX 3……………………. Overview of Assets, Loans, Deposits and Financial Results of Banks in the Federation of B&H

ANNEX 4…………………..… Retail Savings in Banks in the Federation of B&H

ANNEX 5…………………..… Report on Classification of Assets and Off-Balance Sheet Risk-Bearing Items in Banks in the Federation of B&H

ANNEX 6……………………. Income Statement of Banks in the Federation of B&H According to the FBA Model

ANNEX 7……………………. Report on Capital Condition and Adequacy of Banks in the Federation of B&H

ANNEX 8……………………. Data on Employees in Banks in the Federation of B&H

ANNEX 1

Banks in the Federation of Bosnia and Herzegovina – 30.09.2016

No.	BANK	Address		Telephone	Director
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	SANELA PAŠIĆ
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	SAMIR MUSTAFIĆ
6.	KOMERCIJALNO-INVESTICIONA BANKA DD V.KLADUŠA	V.Kladuša	Tone Hrovata bb	037/771-253, fax:772-416	HASAN PORČIĆ
7.	NLB BANKA dd - SARAJEVO	Sarajevo	Džidžikovac 1.	033/720-300, fax:035/302-802	SENAD REDŽIĆ
8.	PRIVREDNA BANKA SARAJEVO dd - SARAJEVO	Sarajevo	Alipašina 6	033/277-700, fax:664-175	ADNAN BOGUNIĆ
9.	PROCREDIT BANK dd - SARAJEVO	Sarajevo	Franca Lehara bb	033/250-950, fax:250-971	EDIN HRNJICA
10.	RAIFFEISEN BANK dd BiH - SARAJEVO	Sarajevo	Zmaja od Bosne bb.	033/755-010, fax: 213-851	KARLHEINZ DOBNIGG
11.	SBERBANK BH dd - SARAJEVO	Sarajevo	Fra Anđela Zvizdovića 1	033/295-601, fax:263-832	EDIN KARABEG
12.	SPARKASSE BANK dd BOSNA I HERCEGOVINA- SARAJEVO	Sarajevo	Zmaja od Bosne br. 7.	033/280-300, fax:280-230	SANEL KUSTURICA
13.	UNICREDIT BANK dd - MOSTAR	Mostar	Kardinala Stepinca bb	036/312-112, fax:312-121	DALIBOR ĆUBELA
14.	UNION BANKA dd - SARAJEVO	Sarajevo	Dubrovačka 6	033/561-000, fax: 201-567	VEDRAN HADŽIAHMETOVIĆ
15.	VAKUFSKA BANKA dd - SARAJEVO	Sarajevo	M. Tita 13.	033/280-100, fax: 663-399	Interim director DAMIR SOKOLOVIĆ
16.	ZIRAATBANK BH dd - SARAJEVO	Sarajevo	Zmaja od Bosne 47c	033/252-230, fax: 252-245	ALI RIZA AKBAŞ

ANNEX 2

THE BALANCE SHEET OF BANKS IN THE FEDERATION OF B&H ACCORDING TO THE FBA MODEL
ACTIVE SUB-BALANCE

in KM 000

No.	DESCRIPTION	31.12.2014	31.12.2015	30.09.2016
	ASSETS			
1.	Cash and deposit accounts with deposit-taking institutions	4 560 234	4 857 483	4 831 706
1a	Cash and non-interest bearing deposit accounts	618 460	1 058 837	2 276 743
1b	Interest-bearing deposits accounts	3 941 774	3 798 646	2 554 963
2.	Trading securities	586 704	882 829	975 925
3.	Loans to other banks	50 836	78 420	128 726
4.	Loans, receivables based on leasing facilities and past due receivables	11 170 277	11 610 744	12 127 524
4a	Loans	9 959 429	10 424 207	10 945 790
4b	Receivables based on leasing facilities	42	36	31
4c	Past due receivables based on loans and leasing facilities	1 210 806	1 186 501	1 181 703
5.	Held to maturity securities	214 585	167 377	152 457
6.	Business premises and other fixed assets	491 740	482 817	489 869
7.	Other real estate	34 120	34 077	42 602
8.	Investments in unconsolidated related companies	23 135	22 114	18 615
9.	Other assets	241 737	265 171	277 060
10.	LESS: value adjustments	1 222 838	1 239 307	1 231 903
10a	Value adjustments for Item 4. of the Assets	1 160 481	1 181 736	1 173 181
10b	Value adjustments for Assets items, except for the Item 4.	62 357	57 571	58 722
11.	**TOTAL ASSETS**	**16 150 530**	**17 161 725**	**17 812 581**
	LIABILITIES			
12.	Deposits	12 130 746	13 098 983	13 607 104
12a	Interest-bearing deposits	9 360 082	9 935 353	9 954 741
12b	Non-interest bearing deposits	2 770 664	3 163 630	3 652 363
13.	Borrowings – liabilities due	150	150	150
13a	Past due liabilities			
13b	Past due – invoked off-balance sheet liabilities	150	150	150
14.	Borrowings from other banks			
15.	Liabilities to the Government			
16.	Loan commitments and other borrowings	1 026 503	904 050	832 620
16a	With remaining maturity of up to one year	359 866	161 356	161 882
16b	With remaining maturity of more than one year	666 637	742 694	670 738
17.	Subordinated debt and subordinated bonds	156 233	119 835	119 715
18.	Other liabilities	417 395	468 719	489 942
19.	**TOTAL LIABILITIES**	**13 731 027**	**14 591 737**	**15 049 531**
	CAPITAL			
20.	Permanent preferred shares	11 959	11 709	8 828
21.	Common shares	1 221 591	1 155 783	1 178 254
22.	Issue premiums	136 485	132 667	132 667
22a	Over permanent preferred shares	88	88	88
22b	Over common shares	136 397	132 579	132 579
23.	Undistributed profit and capital reserves	618 214	836 609	955 185
24.	Foreign exchange rate differences			
25.	Other capital	115 520	117 486	172 382
26.	Loan loss provisions formed from profit	315 734	315 734	315 734
27.	**TOTAL EQUITY (20. to 25.)**	**2 419 503**	**2 569 988**	**2 763 050**
28.	**TOTAL LIABILITIES AND EQUITY (19 +26)**	**16 150 530**	**17 161 725**	**17 812 581**
	PASSIVE AND NEUTRAL SUB-BALANCE	**638 913**	**713 765**	**715 293**
	BALANCE SHEET TOTAL OF BANKS	**16 789 443**	**17 875 490**	**18 527 874**

ANNEX 3

OVERVIEW OF ASSETS, LOANS, DEPOSITS AND FINANCIAL RESULTS OF BANKS IN THE FEDERATION OF B&H as of 30.09.2016

in KM 000

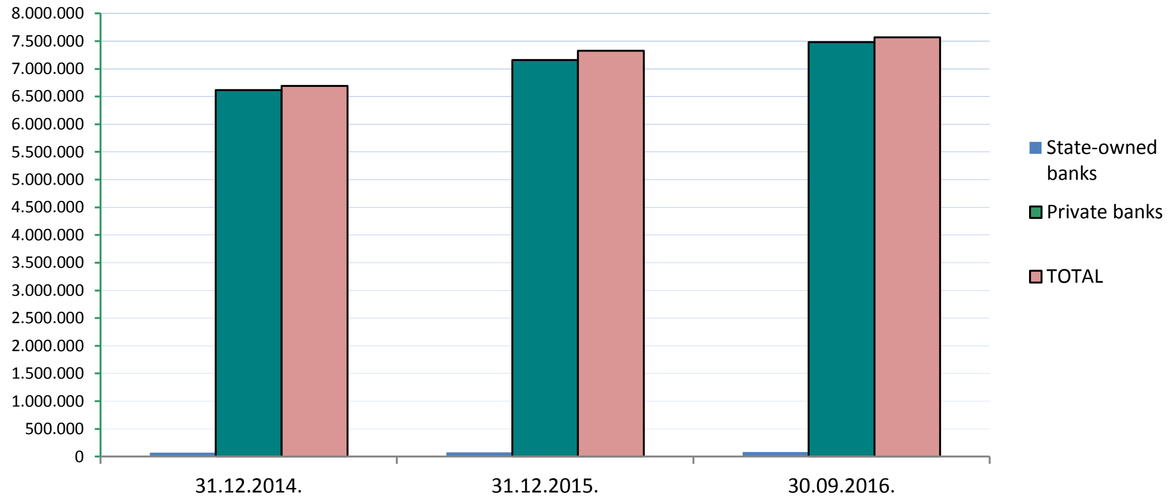
No.	BANK	Assets		Loans		Deposits		Fin. result
		Amount	%	Amount	%	Amount	%	Amount
1.	BOR Banka d.d. Sarajevo	253 432	1.4%	177 331	1.5%	151 412	1.1%	110
2.	Bosna Bank International d.d. Sarajevo	739 381	4.2%	538 436	4.4%	474 572	3.5%	4 661
3.	Hypo Alpe Adria Bank d.d. Mostar	821 609	4.6%	561 223	4.6%	586 576	4.3%	-37 894
4.	Intesa Sanpaolo banka d.d. Sarajevo	1 774 137	10.0%	1 251 202	10.3%	1 307 733	9.6%	22 538
5.	Investiciono Komercijalna banka d.d. Zenica	415 930	2.3%	260 764	2.2%	329 509	2.4%	1 786
6.	Komercijalno Investiciona banka d.d. Velika Kladuša	89 484	0.5%	50 065	0.4%	61 900	0.5%	1 167
7.	NLB banka d.d. Sarajevo	943 227	5.3%	683 034	5.6%	769 371	5.7%	9 586
8.	Privredna Banka d.d Sarajevo	154 132	0.9%	97 514	0.8%	128 003	0.9%	651
9.	ProCredit Bank d.d. Sarajevo	382 257	2.1%	310 185	2.6%	252 834	1.9%	-545
10.	Raiffeisen Bank dd Bosna i Hercegovina	3 837 623	21.5%	2 269 974	18.7%	3 094 555	22.7%	65 606
11.	Sberbank BH d.d. Sarajevo	1 144 727	6.4%	950 758	7.8%	889 198	6.5%	8 948
12.	Sparkasse Bank d.d. Sarajevo	1 182 168	6.6%	929 400	7.7%	966 333	7.1%	18 632
13.	Union banka d.d. Sarajevo	421 327	2.4%	150 803	1.2%	352 576	2.6%	214
14.	UniCredit bank d.d. Mostar	4 594 766	25.8%	3 079 357	25.4%	3 530 455	25.9%	69 032
15.	Vakufska banka d.d. Sarajevo	294 785	1.7%	212 442	1.8%	251 502	1.8%	1 058
16.	Ziraatbank BH d.d. Sarajevo	763 596	4.3%	605 036	5.0%	460 575	3.4%	6 832
	TOTAL	**17 812 581**	**100%**	**12 127 524**	**100%**	**13 607 104**	**100%**	**172 382**

ANNEX 4

NEW RETAIL SAVINGS IN BANKS IN THE FEDERATION OF B&H

in KM 000

	31.12.2014	31.12.2015	30.09.2016
State-owned banks	73 072	78 771	85 092
Private banks	6 618 891	7 156 178	7 480 757
TOTAL	**6 691 963**	**7 234 949**	**7 565 849**



ANNEX 5

CLASSIFICATION OF BALANCE SHEET ASSETS AND OFF-BALANCE SHEET RISK-BEARING ITEMS
as of 30.09.2016
- CLASSIFICATION OF BALANCE SHEET ASSETS ITEMS –

in KM 000

No.	BALANCE SHEET ASSETS ITEMS	CLASSIFICATION					TOTAL
		A	B	C	D	E	
1.	Short-term loans	2 242 078	163 632	8 072	8 700	1 007	2 423 489
2.	Long-term loans	7 675 849	472 758	201 999	109 620	15 492	8 475 718
3.	Other facilities	151 944	1 482	24	182	1 915	155 547
4.	Accrued interest and fees	36 672	3 539	1 698	4 345	23 751	70 005
5.	Past due receivables	51 666	23 627	20 992	309 815	749 654	1 155 754
6.	Receivables based on paid guarantees			50	927	24 972	25 949
7.	Other balance sheet assets being classified	559 882	3 841	838	2 464	35 427	602 452
8.	**TOTAL BALANCE SHEET ASSETS BEING CLASSIFIED (sum of items 1 through 7 – calculation basis for regulatory loan loss provisions)**	**10 718 091**	**668 879**	**233 673**	**436 053**	**852 218**	**12 908 914**
9.	**CALCULATED REGULATORY RESERVES FOR LOAN LOSSES BASED ON BS ASSETS**	**210 702**	**56 714**	**56 474**	**260 037**	**852 271**	**1 436 198**
10.	**VALUE ADJUSTMENT FOR BS ASSETS**	**133 207**	**42 942**	**83 779**	**246 386**	**725 589**	**1 231 903**
11.	**REQUIRED REGULATORY RESERVES FORMED AGAINST PROFIT FOR PURPOSE OF ASSESSED LOSSES BASED ON BS ASSETS**	**120 963**	**36 021**	**14 954**	**60 999**	**133 515**	**366 452**
12.	**FORMEED REGULATORY RESERVES FORMED AGAINST PROFIT RELATED TO ASSESSED LOSSES BASED ON BS ASSETS**	**86 908**	**29 783**	**23 383**	**81 922**	**57 255**	**279 251**
13.	**SHORTFALL OF REGULATORY RESERVE FORMED AGAINST PROFIT RELATED TO ASSESSED LOSSES BASED ON BS ASSETS**						**195 517**
14.	**BALANCE SHEET ASSETS NOT BEING CLASSIFIED (gross book value)**						**6 135 570**
15.	**TOTAL BALANCE SHEET ASSETS (gross book value)**						**19 044 484**

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	3 921 082
14.b	Demand deposits and term deposits up to one month located on accounts of banks with defined investment rating	776 011
14.c	Tangible and intangible assets	507 938
14.d	Financial and tangible assets acquired in the process of collection of receivables (within one year upon such acquisition)	14 057
14.e	Own (treasury) shares	
14.f	Receivables based on overpaid taxes	19 061
14.g	Trading securities	110 729
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	786 692
	TOTAL Item 14	**6 135 570**
8a.	Facilities secured with a cash deposit	182 915

ANNEX 5A

CLASSIFICATION OF BALANCE SHEET ASSETS AND OFF-BALANCE SHEET RISK-BEARING ITEMS
as of 30.09.2016
- CLASSIFICATION OF OFF-BALANCE SHEET ITEMS -

in KM 000

No.	OFF-BALANCE SHEET ITEMS	CLASSIFICATION					TOTAL
		A	B	C	D	E	
1.	Payment guarantees	382 840	28 801	3 961	1 006	3	416 611
2.	Performance guarantees	602 932	88 815	3 888	632		696 267
3.	Uncovered letters of credit	39 696	234	108			40 038
4.	Irrevocably approved, but undrawn loans	1 551 211	74 687	1 179	168	154	1 627 399
5.	Other contingent liabilities of the bank	12 127	151		1	150	12 429
6.	**TOTAL OFF-BALANCE SHEDET ITEMS BEING CLASSIFIED (sum of items 1 through 5 – calculation basis for regulatory loan loss provisions)**	**2 588 806**	**192 688**	**9 136**	**1 807**	**307**	**2 792 744**
7.	**CALCULATED REGULATORY RESERVES FOR LOAN LOSSES RELATED TO OFF-BALANCE SHEET ITEMS**	**50 905**	**11 905**	**3 229**	**1 004**	**307**	**67 350**
8.	**LOSS RESERVES FOR OFF-BALANCE SHEET ITEMS**	**30 537**	**1 870**	**4 713**	**631**	**256**	**38 007**
9.	**REQUIRED REGULATORY RESERVES FORMED AGAINST PROFIT RELATED TO ASSESSED LOSSED BASED ON OFF-BALANCE SHEET ITEMS**	**29 787**	**10 777**	**436**	**494**	**51**	**41 545**
10.	**FORMED REGULATORY RESERVES FORMED AGAINST PROFIT RELATED TO ASSESSED LOSSED BASED ON OFF-BALANCE SHEET ITEMS**	**24 000**	**10 028**	**688**	**1 619**	**148**	**36 483**
11.	**SHORTFALL OF REGULATORY RESERVES FORMED AGAINST PROFIT RELATED TO ASSESSED LOSSED BASED ON OFF-BALANCE SHEET ITEMS**						**10 739**
12.	**OFF-BALANCE SHEET ITEMS NOT BEING CLASSIFIED**						**370 550**
13.	**TOTAL OFF-BALANCE SHEET ITEMS**						**3 163 294**
6a.	**Contingent liabilities secured with a cash deposit**						**43 540**
6b.	**Approved undisbursed loans with a clause on unconditional cancellation**						**512 172**

ANNEX 6

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

in KM 000

No.		D E S C R I P T I O N	30.09.2014	30.09.2015	30.09.2016
1.		**INTEREST INCOME AND EXPENSES**			
	a)	Interest income and similar income			
	1)	Interest-bearing deposit accounts with deposit-taking institutions	3 069	1 065	1 354
	2)	Loans to other banks	1 705	1 352	1 543
	3)	Loans and leasing facilities	519 657	515 294	502 582
	4)	Held to maturity securities	5 352	4 971	3 926
	5)	Equity securities	651	49	37
	6)	Receivables based on paid-off balance sheet liabilities	6	2	2
	7)	Other interest income and similar income	47 352	49 590	53 915
	8)	**TOTAL INTEREST INCOME AND SIMILAR INCOME**	**577 792**	**572 323**	**563 359**
	b)	Interest expenses and similar expenses			
	1)	Deposits	145 632	130 556	108 927
	2)	Borrowings from other banks	0	0	0
	3)	Borrowings taken – liabilities due	0	0	0
	4)	Liabilities based on loans and other borrowings	14 694	11 401	8 854
	5)	Subordinated debt and subordinated bonds	8 512	6 093	5 435
	6)	Other interest and similar expenses	1 665	1 120	2 340
	7)	**TOTAL INTEREST EXPENSES AND SIMILAR EXPENSES**	**170 503**	**149 170**	**125 556**
	c)	**NET INTEREST AND SIMILAR INCOME**	**407 289**	**423 153**	**437 803**
2.		**OPERATING INCOME**			
	a)	FX income	33 836	36 716	38 580
	b)	Loan fees	4 939	5 954	7 087
	c)	Fees based on off-balance sheet items	18 672	18 018	18 194
	d)	Service fees	152 650	163 487	181 198
	e)	Trading income	178	132	232
	f)	Other operating income	30 287	31 542	27 616
	g)	**TOTAL OPERATING INCOME a) to f)**	**240 562**	**255 849**	**272 907**
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	104 641	78 303	64 455
	2)	Other business and direct expenses	58 772	63 570	72 274
	3)	**TOTAL BUSINESS AND DIRECT EXPENSES 1) + 2)**	**163 413**	**141 873**	**136 729**
	b)	Operating expenses			
	1)	Costs of salaries and contributions	184 319	181 956	180 480
	2)	Costs of business premises, other fixed assets and utilities	108 389	107 437	109 094
	3)	Other operating expenses	67 758	73 788	112 025
	4)	**TOTAL OPERATING EXPENSES 1) to 3)**	**360 466**	**363 181**	**401 599**
	c)	**TOTAL NON-INTEREST BEARING EXPENSES**	**523 879**	**505 054**	**538 328**
4.		**PROFIT BEFORE TAXES**	**153.395**	**181 036**	**210 821**
5.		**LOSS**	**29.423**	**7 088**	**38 439**
6.		**TAXES**	**0**	**38**	**0**
7.		**PROFIT BASED ON INCREASE OF DEFERRED TAX FUNDS AD REDUCTION OF DEFERRED TAX LIABILITIES**	**0**	**0**	**0**
8.		**LOSS BASED ON REDUCTION OF DEFERRED TAX FUNDS AND INCREASE OF DEFERRED TAX LIABILITIES**	**0**	**0**	**0**
9.		**NET PROFIT 4. - 6.**	**153 395**	**180 998**	**210 821**
10.		**NET LOSS 4. - 6.**	**29 423**	**7 088**	**38 439**
11.		**FINANCIAL RESULT 9.-10.**	**123 972**	**173 910**	**172 382**

ANNEX 7

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

in KM 000

No.	DESCRIPTION	31.12.2014	31.12.2015	30.09.2016
	CORE CAPITAL OF THE BANK			
1.a.	Share capital, reserves and profit			
1.1.	Share capital – common and permanent preferred non-cumulative shares – cash payments	1 217 909	1 151 971	1 174 442
1.2.	Share capital – common and permanent preferred non-cumulative shares – investments in kind and in rights	12 550	12 431	12 431
1.3.	Amount of issue premiums earned upon payment of shares	136 485	132 667	132 667
1.4.	General mandatory reserves (reserves mandated by the law)	106 051	163 794	234 179
1.5.	Other reserves from profit after tax based on the decision of the Bank's assembly	409 634	427 706	529 124
1.6.	Retained, undistributed profit from previous years and current year's profit	108 756	122 065	141 078
1.a.	**TOTAL (1.1 to 1.6)**	**1 991 385**	**2 010 634**	**2 223 921**
1.b.	Deductible items from 1.a			
1.7.	Uncovered losses from previous years	122 705	28 371	119 789
1.8.	Current year's loss	50 868	102 108	40 207
1.9.	Book value of own (treasury) shares of the bank	81	102	599
1.10.	Intangible assets in accordance with the applicable accounting framework	41 873	49 837	43 594
1.11.	Amount of deferred tax assets	2 780	1 641	1 441
1.12.	Amount of negative revalorised reserves based on the effect of the change in the fair value of assets	1 282	1 696	1 016
1.b.	TOTAL (1.7. to 1.10)	219 589	183 755	206 646
1.	**AMOUNT OF CORE CAPITAL: (1.a. - 1.b.)**	**1 771 796**	**1 826 879**	**2 017 275**
	SUPPLEMENTARY CAPITAL OF THE BANK			
2.1.	Share capital – common and permanent preferred non-cumulative shares – cash payments	3 091	3 090	209
2.2.	Share capital – common and permanent preferred non-cumulative shares – investments in kind and in rights	0	0	0
2.3.	General loan loss provisions for the category A – performing assets	229 895	208 619	217 765
2.4.	Amount of positive revalorised reserves based on the effect of the change in the fair value of assets	23 703	9 735	12 110
2.5.	Current year profit – audited and confirmed by an external audit	0	0	0
2.6.	Profit amount for which the FBA issues an order restricting its disbursement	154 814	107 918	105 020
2.7.	Amount of subordinated debt	0	0	0
2.8.	Amount of hybrid convertible items – capital instruments	1 419	1 422	1 422
2.	**AMOUNT OF SUPPLEMENTARY CAPITAL: (2.1 to 2.8)**	**412 922**	**330 784**	**336 526**
	DEDUCTIBLE ITEMS FROM THE BANK'S CAPITAL			
3.1.	Portion of invested share 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	1 678	1 007	0
3.3.	Receivables from shareholders with significant voting rights – approved by the bank contrary to Law provisions, FBA regulations and the bank's work policy	1 509	755	757
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	199 890	204 559	203 689
3.	**AMOUNT OF DEDUCTIBLE ITEMS FROM THE BANK'S CAPITAL: (3.1 to 3.5)**	**203 077**	**206 321**	**204 446**
A.	**NET CAPITAL OF THE BANK (1.+2.-3.)**	**1 981 641**	**1 951 342**	**2 149 355**
B.	**RISK OF BALANCE AND OFF-BALANCE ASSETS**	**11 394 469**	**11 918 650**	**12 454 066**
C.	**WEIGHTED OPERATIONAL RISK**	**982 250**	**976 734**	**1 001 009**
D.	**WEIGHTED MARKET RISK**	**0**	**0**	**0**
E.	**TOTAL ASSETS RISK B+C+D**	**12 376 719**	**12 895 384**	**13 455 075**
F.	**NET CAPITAL RATE (A/E) (% 1 dec.)**	**16,0%**	**15,1%**	**16,0%**

ANNEX 8

DATA ON EMPLOYEES IN BANKS IN THE FEDERATION OF B&H

No.	BANK	31.12.2014	31.12.2015	30.09.2016
1	BOR Banka d.d. Sarajevo	64	66	63
2	Bosna Bank International d.d. Sarajevo	312	341	361
3	Hypo Alpe Adria Bank d.d. Mostar	513	490	449
4	Intesa Sanpaolo banka d.d. Sarajevo	521	537	555
5	Investiciono Komercijalna banka d.d. Zenica	164	125	216
6	Komercijalno Investiciona banka d.d. Velika Kladuša	75	77	77
7	Moja banka d.d.Sarajevo	142	133	
8	NLB banka d.d. Sarajevo	430	424	447
9	Privredna Banka d.d Sarajevo	164	142	112
10	ProCredit Bank d.d. Sarajevo	291	248	216
11	Raiffeisen Bank dd Bosna i Hercegovina	1 478	1 355	1 326
12	Sberbank BH d.d. Sarajevo	435	420	424
13	Sparkasse Bank d.d. Sarajevo	475	471	508
14	Union banka d.d. Sarajevo	202	181	191
15	UniCredit bank d.d. Mostar	1 216	1 208	1 230
16	Vakufska banka d.d. Sarajevo	231	200	202
17	Ziraatbank BH d.d. Sarajevo	247	265	303
	TOTAL	6 960	6 683	6 680