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

INFORMATION

ON BANKING SYSTEM OF
THE FEDERATION OF BOSNIA AND HERZEGOVINA
As of 03/31/2005

Sarajevo, May 2005

Banking Agency of the Federation of BiH, as regulatory institution performing supervision of banks, completed the Information on the banking system of the Federation of BiH (as of March 31st 2005) based on the reports of banks, and other information and data submitted by banks. The information also includes findings and data attained during on-site examinations and analysis performed in the Agency (off-site examination).

CONTENTS

I INTRODUCTION

In the first quarter of 2005, some general indicators of banks' performance confirmed that positive changes have continuity and stabilized growth trend, including strengthening and consolidation of the sector. Total balance sheet sum was KM 7.8 billion at the end of first quarter, which is higher by KM 156 million or 2% in comparison to the end of 2004. If we observe balance sheet positions in their resources, it is visible that the highest growth was recorded in loans of KM 84 million or 10%, capital increased by KM 16 million or 2% while deposit potential slightly increased by KM 24 million or 0.4%.

In the observed period, banks increase loans by KM 206 million or 5%, while cash assets recorded minimum increase of KM 17 million or 1%. Banks maintained last year trend of faster growth of loans originated to enterprises (5%) in comparison to loans originated to citizens (4%). At the same time, short-term loans increased by 6% and long-term loans by 4%, which indicated improved maturity adjustment between assets and liabilities, resulted from actions implemented by FBA in banks.

If we observe the structure through the participation of balance sheet categories in assets and liabilities, we can see there are some insignificant changes in comparison to the previous period. The major source of financial potential was still deposits that represented 72.4%, although they continued with slight decreasing trend. Savings maintained growing trend and reached amount of KM 2.26 billion, which is higher by 6.1% in comparison to the end of 2004.

According to the information from income statement, on the system level banks reported positive financial result – profit of KM 16.3 million in the first quarter, which is higher by 59% in comparison to same period last year. The profit of 21.7 million was reported by 15 banks, while nine banks reported loss of total KM 5.4 million.

The ROAA (Return on Average Assets) was 0.85% and ROAE (Return on Average Equity) 8.57% for the whole system, which is better in comparison to the last year, and it is slightly worse than the international practice standards.

In the structure of total income it was visible that interest income increased and it was 68.8%, and at the same time operational income decreased from 35% to 31.2%. Interest expenses increased and were 26.4% and non-interest expenses were 73.6% out of total expenses.

As for market share and its reallocation, it is possible to make conclusion that there were no significant changes in the first quarter, and four banks with assets over KM 500 million held 68% of total banking assets. On the other hand, participation of 10 banks with assets below KM 100 million was only 6.4%.

Capitalization rate and capital adequacy remains still one of the key segments of the system's activity, especially due to fact that largest banks in the system have capital adequacy ratios just slightly over regulatory minimum (12%) by 1% to 2.6%. It is obvious that strengthening of capital base in banks represents priority in future, especially in the largest banks. That is necessary in order for banks to develop their operations and adjust them to their strategic plans.

II OPERATIONAL PERFORMANCE OF BANKS IN THE FBiH

1. STRUCTURE OF BANKING SECTOR

1.1. Status, Number and Operational Network

As of 03/31/05, there were 24 banks[1] in the Federation of BiH with banking license granted. Number of banks was unchanged in comparison to the 12/31/04.

Provisional administrator was instituted in five banks as of 03/31/05 (Hercegovačka Bank dd Mostar, UNA Bank dd Bihać, Ljubljanska Bank dd Sarajevo, Poštanska Bank BiH dd Sarajevo and Privredna Bank dd Sarajevo).

In first quarter of 2005, banks tried to further expand their organizational network. Banks in the Federation of BiH have founded 10 new organizational parts, out of which three in Republic of Srpska. In comparison to 12/31/04, when banks constituted of 439 organizational parts, this represents a growth of 2.3%.

As of 03/31/05, 11 banks from the Federation of BiH had 24 organizational parts in Republic of Srpska and 10 in Brčko District. Number of organizational parts of banks from Republic of Srpska in the Federation of BiH remained unchanged in comparison to 12/31/2004, that is, three banks from Republic of Srpska had nine organizational parts in the Federation of BiH.

License to perform inter-bank transactions in the internal payment system was granted to 24 banks as of 03/31/2005. There were 15 banks with deposit insurance program.

1.2. Ownership structure

As of 03/31/05, ownership structure in banks[2] was evaluated upon available information and insight in banks[3] as follows:

- Private and predominately privately owned 18 banks (75%)
- State and predominately state owned 6 banks (25%).

Ownership structure can be observed from the aspect of financial indicators, which is by the value of total capital[4].

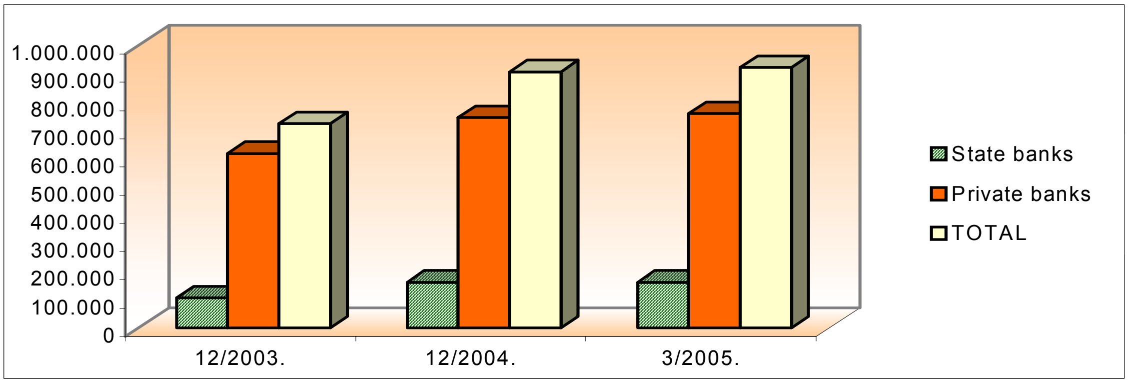
[1] Starting form 09/30/04, financial indicators include information from Hercegovačka Bank d.d. Mostar (in period from April 2001 when Provisional Administrator was instituted in Hercegovačka Bank until 09/30/04 information for the whole banking system did not include the data from this bank).
[2] Criteria for dividing banks by type of ownership is the ownership of shareholder capital in banks.
[3] General overview of ownership structure of banks in the F BiH as of 03/31/05 resulted from received reports, and registration in authorized courts (changes in capital and bank shareholders).
[4] Information from balance sheet - FBA schedule: share capital, value over the issue shares, undistributed profit and reserves and other capital (financial results from the current period).

Schedule 1: *Ownership Structure by Total Capital*

-In 000 KM-

BANKS	12/31/03		12/31/04		03/31/05		RATIO	
							3/2	4/3
1	2		3		4		5	6
State banks	106,105	15%	161,915	18%	161,942	18%	153	100
Private banks	607,430	85%	744,741	82%	759,776	82%	123	102
TOTAL	713,535	100%	906,656	100%	921,718	100%	127	102

Graph 1: *Schedule of Ownership Structure (total capital)*



More detailed picture on capital ownership structure of banks in the Federation of BiH can be viewed by analysis of participation of state, private and foreign capital in share capital of banks.

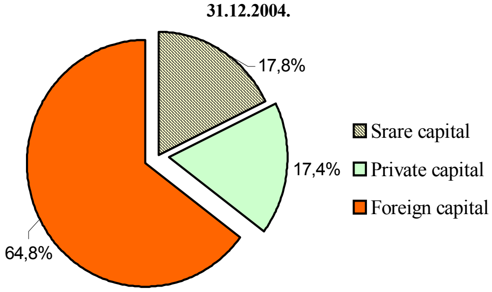
Schedule 2: *Ownership structure by participation of state, private and foreign capital*

-In 000 KM-

SHARE CAPITAL	12/31/03		12/31/04		03/31/05		RATIO	
	Amount	Participation %	Amount	Participation %	Amount	Participation %	5/3	7/5
1	3	4	5	6	7	8	9	10
State capital	75,636	12.6	135,350	17.8	135,350	17.8	179	100
Private capital (residents)	115,411	19.2	132,785	17.4	129,031	16.9	115	97
Foreign capital (non-residents)	408,882	68.2	493,227	64.8	496,982	65.3	121	101
TOTAL	540,612	100.0	598,574	100.0	672,415	100.0	111	112

Graph 2: *Ownership Structure (share capital)*

31.12.2004.



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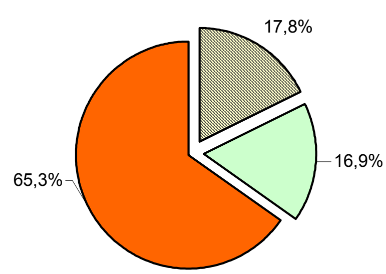


Analysis of ownership structure in banks from the aspect of shareholders capital is the best indicator of changes and trends in the banking system of the F BiH, especially in the segment of ownership structure changes.

Participation of state capital in total share capital of banks as of 03/31/05 was 17.8% and it is the same as of 12/31/04. Participation of remaining, state owned capital in privately owned banks was below 1% or KM 1.2 million.

In comparison to 31/12/04, participation of privately owned capital (residents) in total capital of the whole banking sector decreased from 17.4% to 16.9%, and participation of foreign capital increased from 64.8% to 65,3%.

Changes in the ownership structure are significantly reflected through the participation, that is, market share and position of banks grouped by major ownership of share capital. Integration of individual institutions was made in order to achieve better market positioning, and they resulted in concentration of larger banks in banking sector, decreased number of banks, and more severe competition.

Schedule 3: *Market chare of banks by type of ownership*[5]

- In % -

BANKS	12/31/03			12/31/04			12/31/05		
	Part. in total capital	Part. in total assets	Number of banks	Part. in total capital	Part. in total assets	Number of banks	Part. in total capital	Part. in total assets	Number of banks
1	2	3	4	5	6	7	8	9	10
Banks with predominantly state capital	14.9	6.4	7	17.9	4.9	6	17.6	4.9	6
Banks with predominantly private domestic capital	19.7	14.7	7	16.8	15.8	8	16.7	16.0	8
Banks with predominantly foreign capital	65.4	78.9	12	65.3	79.3	10	65.8	79.1	10
TOTAL	100.0	100.0	26	100.0	100.0	24	100.0	100.0	24

1.3. Staff

There were total 5,737 employees as of 03/31/05 in banks of the Federation BiH. Out of total number, 9% worked in banks with predominantly state capital and 91% in privately owned banks.

Schedule 4: *Staff in banks of the F BiH*

BANKS	NUMBER OF EMPLOYEES						RATIO	
	12/31/03		12/31/04		03/31/05		3:2	4:3
1	2		3		4		5	6
State banks	549	10%	490	9%	487	9%	89	99
Private banks	4.845	90%	5.197	91%	5.250	91%	107	101
TOTAL	5.394	100%	5.687	100%	5.737	100%	105	101
Number of banks	26		24		24			

[5] By predominant ownership (over 50%).

In the first quarter of 2005, number of employees increased by 1% or 50 persons and the growth relates only to privately owned banks.

Schedule 5: *Educational structure of staff*

EDUCATION	NUMBER OF EMPLOYEES			RATIO	
	12/31/03	12/31/04	03/31/05	3:2	4:3
1	2	3	4	5	6
Graduate Study	1,847	2,016	2,052	109	102
Under Graduate Study	546	596	608	109	102
High school	2,825	2,962	2,967	105	100
Other	176	113	110	64	97
TOTAL	5,394	5,687	5,737	105	101

In comparison to the end of 2004, the structure of employees did not change in terms of educational structure, therefore, the major participation of 52% is with high school education.

One of the indicators of the success in the banking sector and any bank individually, is ratio between assets and number of staff, that is, assets against an employee. The higher ratio, the better position of banks' operations and the system in whole.

Schedule 6: *Assets per an employee*

BANKS	12/31/03			12/31/04			03/31/05		
	Number of staff	Assets (000 KM)	Assets/ Employee	Number of staff	Assets (000 KM)	Assets/ employee	Number of staff	Assets (000 KM)	Assets/ employee
State	549	369,974	674	490	373,064	766	487	378,244	777
Private	4,845	5,402,076	1,115	5,197	7,240,657	1,393	5,250	7,391,944	1,408
TOTAL	5,394	5,772,050	1,070	5,687	7,613,721	1,339	5,737	7,770,188	1,354

At the end of first quarter of 2005, for individual employee there was approximately KM 1.35 million of assets for whole banking system. The ratio was much better in privately owned banks, which is to be expected since operations in state owned banks were stagnating or decreasing.

Schedule 7: *Assets per an employee by groups*

Assets (000 KM)	12/31/03	12/31/04	03/31/05
	Number of banks	Number of banks	Number of banks
Up to 500	9	7	7
500 to 1.000	5	5	6
1.000 to 1.500	9	4	3
1.500 to 2.000	3	7	7
Over 2.000	1	1	1
TOTAL	26	24	24

Individual analytical results for banks were between KM 172 thousands up to KM 2.8 millions of assets per an employee. With nine banks this ratio was better then the ratio for whole banking sector, and four largest banks in the system had it over KM 1.8 millions. Other banks had way worse indicators because seven banks had assets per an employee under KM 500 thousands, which implies that they have excessive number of staff in comparison to assets. That results in larger operational costs and has negative impact to profitability in those banks.

2. FINANCIAL INDICATORS OF BANKING OPERATIONS

Examination of banks through analysis of banks' reports is conducted by review of reports regulated by the Agency and reports of other institutions. Those reports represent database of three groups of information:

1. Information on balance sheet set for all banks submitted monthly, including quarterly attachments to balance sheet containing more detailed information on cash assets, loans, deposits and off balance sheet items, and some basic statistical information,
2. Information on solvency of banks, information on capital and capital adequacy, assets classification, concentrations of various types of risk, liquidity position, exposure to foreign exchange risk, and based on the reports regulated by the FBA (quarterly) and
3. Information on operating results of banks (income statement - FBA format) and reports on cash flows, submitted to FBA quarterly.

Aside from the above standardized reports, data base includes information from additional reports requested by the FBA from banks in order to have the best quality monitoring and analysis of banks' operations in the Federation of BiH. Also, database includes reports on audit of financial statements prepared by independent auditor, and all other information relevant to the assessment of operational results for banks individually and banking system in whole.

As it is regulated by the Law on Opening Balance Sheet of Banks, banks with predominantly state capital have to report to the Agency "full" balance sheet, which would be divided into: passive, neutral and active sub-balance sheet. In order to have realistic indicators of banks' operational results in Federation of BiH, all further analysis of banking system will be based on information from active sub-balance for banks with predominantly state capital[6].

2.1. Balance sheet

Based on the balance sheets submitted by banks as of 03/31/05, total balance sheet of banks in the Federation of BiH was KM 7.8 billion, which is higher by 2% or KM 156 million in comparison to 12/31/04. In the same period last year, the growth ratio was 8%.

[6] Some state owned banks reported passive and neutral items in their "full" balance sheet, which will be taken over by the state upon the finalization of privatization process.

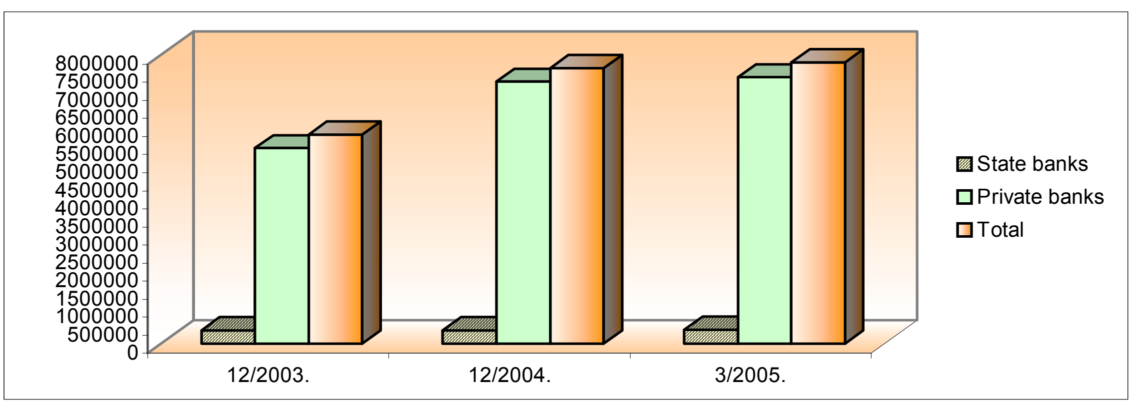
Schedule 8: *Balance Sheet*

DESCRIPTION	AMOUNT (in 000 KM)			RATIO	
	12/31/03	12/31/04	03/31/05	3/2	4/3
1	2	3	4	5	6
ASSETS:					
Cash assets	2,059,285	2,859,489	2,875,974	139	101
Securities	25,017	19,430	25,213	78	130
Placements to other banks	36,369	81,624	22,057	224	27
Loans – net value	3,238,270	4,185,522	4,385,194	129	105
Premises and other fixed assets	304,680	298,566	296,380	98	99
Other assets	108,429	169,090	165,370	156	98
TOTAL ASSETS	**5,772,050**	**7,613,721**	**7,770,188**	**132**	**102**
LIABILITIES:					
PAYABLES					
Deposits	4,292,709	5,602,238	5,626,451	131	100
Borrowings from other banks	3,779	3,329	3,328	88	100
Loan payables	589,012	850,833	935,012	144	110
Other liabilities	173,015	250,665	283,679	145	113
CAPITAL					
Capital	713,535	906,656	921,718	127	102
TOTAL LIABILITIES (PAYABLES AND CAPITAL)	**5,772,050**	**7,613,721**	**7,770,188**	**132**	**102**

Schedule 9: *Assets in Banks by Ownership Structure*

BANKS	12/31/03		12/31/04		03/31/05		RATIO	
							3/2	4/3
1	2		3		4		5	6
State Banks	369,974	6%	373,064	5%	378,244	5%	101	101
Private Banks	5,402,076	94%	7,240,657	95%	7,391,944	95%	134	102
TOTAL	5,772,050	100%	7,613,721	100%	7,770,188	100%	132	102

Graph 3: *Assets in Banks by Ownership Structure:*



Analysis of analytical data by banks shows that six banks (three under provisional administration) recorded decreased assets, while remaining 18 banks experienced increase in assets from 1% to 6%. Only two banks had increase of approximately 11%.

If we analyze banking system from the aspect of assets size and particular groups within this frame, it is possible to make conclusion that there were insignificant changes in banks by groups and number of banks.

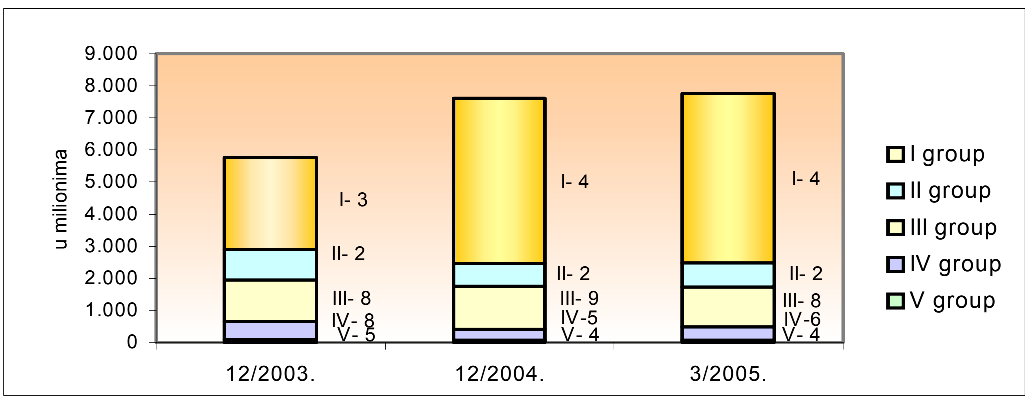
One bank switched from group III to group IV due to decreased assets, which reflected through participation of those groups in the total assets in the banking sector. The largest banks (group I and II) preserved trend of assets growth, and at the end of first quarter it was 77.9%.

Following schedule presents amount and participation of particular groups of banks[7] in time line (amounts are in millions of KM):

Schedule 10: *Participation of particular groups of banks in total assets through periods*

AMOUNT OF ASSETS	12/31/03			12/31/04			03/31/05		
	Amount	Particip. %	Number of banks	Amount	Particip. %	Number of banks	Amount	Particip. %	Number of banks
I- Over 500	2,882	49.9	3	5,166	67.9	4	5,300	68.2	4
II- 300 to 500	945	16.4	2	701	9.2	2	752	9.7	2
III- 100 to 300	1,293	22.4	8	1,335	17.5	9	1,222	15.7	8
IV- 50 to 100	554	9.6	8	342	4.5	5	424	5.5	6
V- Less then 50	98	1.7	5	70	0.9	4	72	0.9	4
TOTAL	5,772	100.0	26	7,614	100.0	24	7,770	100.0	24

Graph 4: *Participation of particular groups of banks in total assets through periods*



The growth of balance sheet mainly resulted from growth of borrowings (by 10% or KM 84 million), subordinated debts (by 12% or KM 10 million) and capital (by 2% or KM 16 million from current profit), while deposits increased by insignificant 0.4% or KM 24 million.

Within assets (property) of banks, loans[8] increased by 5% or KM 206 million, while cash assets had minimum growth of 1% or KM 17 million.

[7] Banks are divided into five groups, by size of assets.
[8] Gross loans (information from balance sheet).

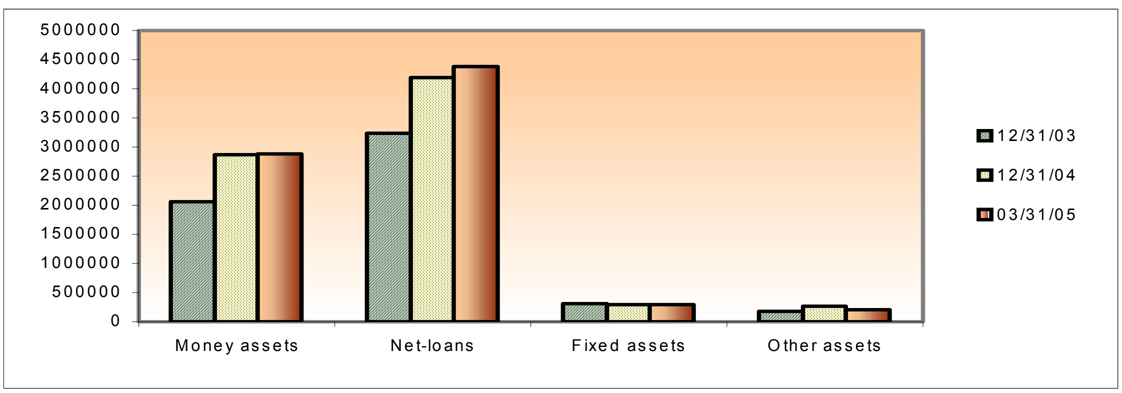
Following schedule and graphs show the structure of the most significant balance sheet assets and liabilities positions of banks through periods:

Schedule 11: *Balance sheet structure*

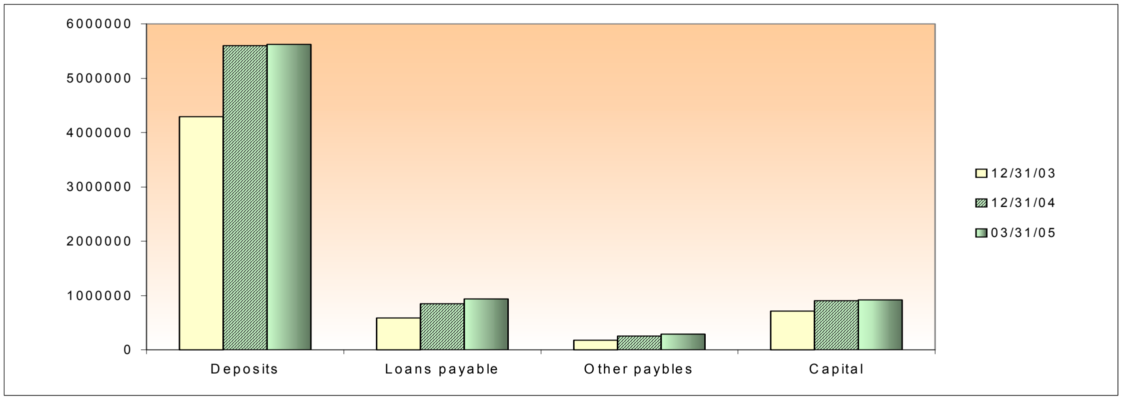
- In % -

DESCRIPTION	PARTICIPATION		
	12/31/03	**12/31/04**	**03/31/05**
ASSETS:			
Cash assets	35.7	37.6	37.0
Securities	0.4	0.2	0.3
Placements to other banks	0.6	1.1	0.3
Loans – net value	56.1	55.0	56.4
Premises and other fixed assets	5.3	3.9	3.9
Other assets	1.9	2.2	2.1
TOTAL ASSETS	100.0	100.0	100.0
LIABILITIES:			
PAYABLES			
Deposits	74.4	73.6	72.4
Borrowings from other banks	0.1	0.1	0.1
Loan payables	10.2	11.2	12.0
Other liabilities	2.9	3.2	3.6
CAPITAL			
Capital	12.4	11.9	11.9
TOTAL LIABILITIES (PAYABLES AND CAPITAL)	100.0	100.0	100.0

Graph 5: *Assets Structure in Balance Sheet of Banks*



Graph 6: *Liabilities Structure in Balance Sheet of Banks*



Changes in structure of liabilities in banks and participation of the most significant balance sheet items in financial potential remained the same as in the previous period. Participation of deposits is still decreasing slowly, but with ratio of 72.4% they are still predominant part. On the other hand, liabilities increased due to growth of loan payables from 11.2% to 12%.

Assets structure in banks did not change significantly: loans increased by 1.4%, while cash assets decreased by 0.3 percent.

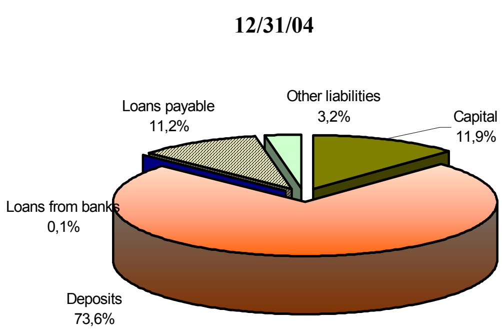
At the end of first quarter of 2005, banks in the Federation of BiH had deposits at depository institutions abroad of KM 1.5 billion (mainly in EURO) or 52% of total cash assets. That is more by 2.5% or KM 77 millions in comparison to the end of 2004. That resulted in decreased participation of cash assets at reserve accounts at the Central Bank of BiH (from 41.2% to 38.7%), which as of 03/31/2005 amounted to KM 1.1 million and this is lower by six percent or KM 66 million. Banks held 7.7% or KM 223 million of cash assets in cash at their vaults and tellers.

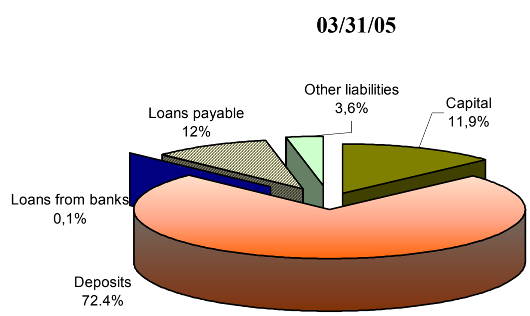
This resulted in changed currency structure of cash assets and growth of participation in foreign currencies from 54% to 56.2%, that is, domestic currency participation decreased from 46% to 43.8%.

2.1.1. Liabilities

As of 03/31/05, structure of balance sheet liabilities of banks can be overviewed from the following graph:

Graph 7: *Structure of liabilities in banks:*





Structure of liabilities was not significantly changed in comparison to the end of 2004. Deposit potential, as primary source of funding, still has major participation of 72.4%, while participation of loan payables increased as earlier and in the reviewed period it was 0.8%. Participation of capital remained unchanged with 11.9%.

In 2005, banks continued borrowing abroad. Long-term credit lines resulted in improved maturity adjustment of funds, and at the same time, banks ensured new long-term funds for financing their clients. Analytical data by banks displayed that approx. 49% of those funds were borrowed to banks by their owners (banks shareholders), and remaining assets were provided by borrowing from international financial market by using credit lines approved by international and domestic financial institutions. Four major creditors, with 60% out of total borrowings were: Raiffeisen Zentralbank Osterreich A.G. (RZB), Bank Polska OPIEKI, European Bank for Reconstruction and Development (EBRD) and Kreditanstalt fur Wiederaufbau (KfW).

In reporting period, deposits increased by insignificant 0.4% or KM 24 million. This growth was recorded only in privately owned banks (growth ratio of 0.4% or KM 27 million), while in state banks deposits were reduced by 2% or KM 3 million.

Participation of deposits in liabilities in privately owned banks was 74% and in state banks 36%.

Based on information reported by banks, out of total deposits only 4.9% were deposits accepted in Federal banks' organizational parts operating in Republic Srpska and Brcko District as of 03/31/05.

Maturity adjustments of deposits were slightly changed in two basic maturity groups. Demand deposits increased by 0.5 percent, while structure of long-term deposits improved and deposits with maturity over three years increased by 0.9%.

Schedule 12: *Maturity adjustment of deposits*

In 000 KM

DEPOSITS	12/31/03		12/31/04		03/12/05		RATIO	
	Amount	Particip .%	Amount	Particip. %	Amount	Particip %	4/2	6/4
1	2	3	4	5	6	7	8	9
Savings and demand deposits	2,215,925	51.6	2,663,052	47.5	2,699,380	48.0	120	101
Up to 3 months	303,203	7.1	389,396	7.0	412,834	7.3	128	106
Up to 1 year	447,952	10.4	490,685	8.8	447,807	8.0	110	91
1. Total short-term	2,967,080	69.1	3,543,133	63.3	3,560,021	63.3	119	101
Up to 3 years	715,648	16.7	1,367,882	24.4	1,321,738	23.5	191	97
Over 3 years	609,981	14.2	691,223	12.3	744,692	13.2	113	108
2. Total long-term	1,325,629	30.9	2,059,105	36.7	2,066,430	36.7	155	100
TOTAL (1 + 2)	4,292,709	100.0	5,602,238	100.0	5,626,451	100.0	131	100

Schedule 13: *Structure of deposits by depositors*[9]

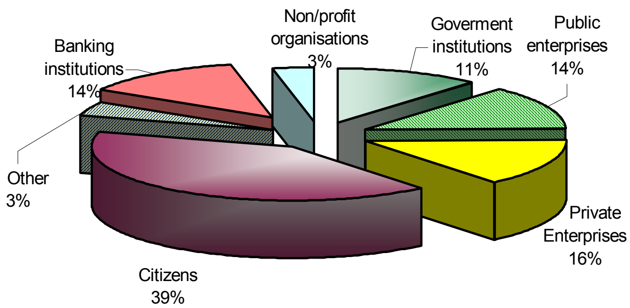
In 000 KM

DEPOSITS BY	12/31/02		12/31/03		09/30/04		RATIO	
	Amount	Particip .%	Amount	Particip. %	Amount	Particip %	4/2	6/4
1	2	3	4	5	6	7	8	9
Governmental institutions	498,132	11.6	599,060	10.7	587,265	10.5	120	98
Public enterprises	567,677	13.2	783,256	14.0	773,602	13.8	138	99
Private enterprises and assoc.	607,046	14.1	877,731	15.7	876,922	15.6	145	100
Non-profit. Organizations	147,606	3.5	180,204	3.2	169,389	3.0	122	94
Banking institutions	557,166	13.0	808,112	14.4	734,149	13.0	145	91
Citizens	1,737,238	40.5	2,173,228	38.8	2,308,830	41.0	125	106
Other	177,844	4.1	180,647	3.2	176,294	3.1	102	98
TOTAL	4,292,709	100.0	5,602,238	100.0	5,626,451	100.0	131	100

[9] Information from attached form BS-D submitted by banks each quarter with Balance sheet - FBA format.

Graph 8: *Structure of deposits by depositors*

12/31/04



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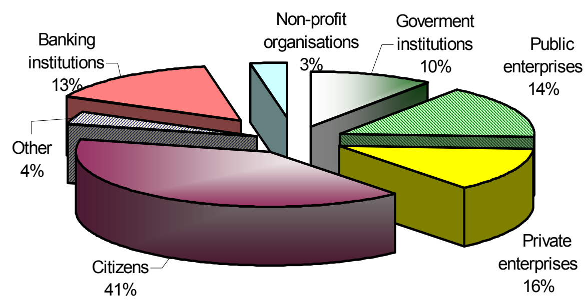


If we make analysis by sectors in first quarter of 2005, it is visible that citizens' deposits increased by 6% or KM 136 million, and at the same time their participation increased by 2.2 percent. Private enterprises deposits remained same at the end of 2004, while deposits from other sectors decreased nominally and their participation decreased in total deposits. The major drop of 9% or KM 74 million was recorded with deposits of banking institutions, and that resulted from withdrawal of those assets by banks-depositors "mother banks" and their reinvestment in credit lines.

Out of total deposits, 42% or KM 2,348 million were in domestic currency and 58% or KM 3,278 million were in foreign currencies. This is same as at the end of 2004.

Savings, as the most significant part of deposit and financial potential in banks maintained growing trend in first quarter of 2005. Savings increased by 6% or KM 130 million. Only one bank had minor decrease of savings, and other banks recorded growth. In five banks, growth ratio was between 10% and 20%, while remaining banks had savings ratio under 10%. Out of total growth of savings, 70% or KM 91 million was with four largest banks in the system.

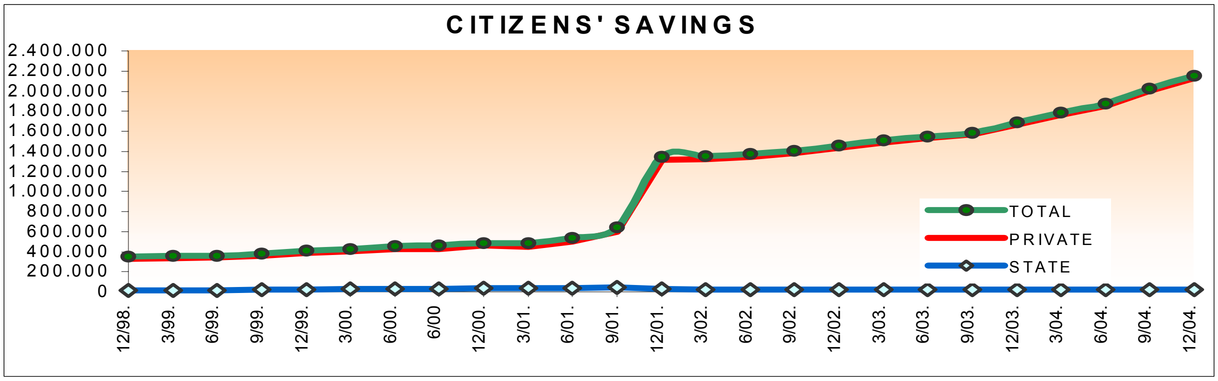
If we observe by sectors, almost all savings were in private banks, that is, only 1.1% out of total savings was at the accounts of five state owned banks.

Schedule 14: *New citizens' savings in time line*

-000 KM-

BANKS	AMOUNT (IN 000 KM)			RATIO	
	12/31/03	12/31/04	03/31/05	3/2	4/3
1	2	3	4	5	6
State	20,758	22,342	24,049	108	108
Private	1,645,991	2,105,167	2,233,474	128	106
TOTAL	1,666,749	2,127,509	2,257,523	128	106

Graph 9: *New citizens' savings in time line*



As in other segments, we should emphasize a strong concentration of savings with few banks, since 71% of total savings was with three largest banks, that is, 94.3% of total savings is deposited with ten private banks.

Out of total savings, 29.5% were savings in domestic currency and 70.5% were in foreign currency.

Schedule 15: *Citizens' savings maturity adjustments in time line*

BANKS	AMOUNT (IN 000 KM)						RATIO	
	12/31/03		12/31/04		03/31/05		3/2	4/3
1	2		3		4		5	6
Short-term savings	1,228,261	73.7%	1,360,285	63.9%	1,391,166	61.7%	111	102
Long-term savings	438,489	26.3%	767,224	36.1%	866,357	38.3%	175	113
TOTAL	1,666,749	100.0%	2,127,509	100.0%	2,257,523	100.0%	128	106

Maturity adjustment of savings, as well as total deposits, recorded positive trend, mainly due to continuing improvement of banking sector in whole, and regained trust in banks and that resulted in faster growth of long-term savings. We should especially mention stability and large growth ratio of long-term savings. That is good indicator for positive future trends.

Aside from activities implemented by FBA, growth of savings in banks of the FBiH resulted from deposit insurance system, which was implemented in January 2001, immediately after the inception of the Deposit Insurance Agency of F BiH. The Law on Deposit Insurance in Banks of BiH was passed in August 2002 and shortly after that the Deposit Insurance Agency of BiH was founded. 15 banks from the Federation of BiH became part of the deposit insurance program and received certificate on deposit insurance. Analytical information displayed that participation of deposits in those banks out of total deposits was 94% and 97% out of total savings was with those banks as well. The admission of banks in the deposit insurance system for the Federation of BiH is entering the closing phase because within nine remaining banks which don't have certificate, six are state banks and they can apply for certificate (they don't have appropriate ownership structure) because of regulations set up by the Deposit Insurance Agency. The safety of deposits is guaranty and incentive for further growth of savings, not only in those banks but also in all other banks.

2.1.2. Capital -Strength and Adequacy

Total capital[10] in banks of the Federation of BiH was KM 1,053 million as of 03/31/05.

Schedule 16: *Regulatory capital*

-In 000 KM-

DESCRIPTION	12/31/03		12/31/04		03/31/05		RATIO	
							3/2	4/3
1	2		3		4		5	6
STATE BANKS								
1.Core Capital before Reduction	122,937		163,061		163,868		133	100
2. Off-setting items	17,687		2,607		3,263		15	125
a) Core Capital (1-2)	105,250	97%	160,454	98%	160,605	98%	153	100
b) Additional Capital	3,061	3%	3,639	2%	3,334	2%	119	92
c) Total capital (a + b)	108,311	100%	164,093	100%	163,939	100%	152	100
PRIVATE BANKS								
1. Core capital before reduction	584,221		743,860		790,242		127	106
2. Of-setting items	34,311		87,071		92,860		254	107
a) Core Capital (1-2)	549,910	75%	656,789	75%	697,382	78%	119	106
b) Additional Capital	183,681	25%	214,478	25%	191,584	22%	117	89
c) Total capital (a + b)	733,591	100%	871,267	100%	888,966	100%	119	102
Total								
1. Core Capital before Reduction	707,158		906,921		954,110		128	105
2. Off-setting items	51,998		89,678		96,123		172	107
a) Core Capital (1-2)	655,160	78%	817,243	79%	857,987	81%	125	105
b) Additional Capital	186,742	22%	218,117	21%	194,918	19%	117	89
c) Capital (a + b)	841,02	100%	1,035,360	100%	1,052,905	100%	123	102

New capital accrual method was set up as of 12/31/03[11], core and net capital were reported on more realistic bases. That is very important for estimation of risk exposure, especially for estimation of banks' exposure to risks, primarily loan risk concentrations.

In the first quarter of 2005, total capital[12] increased by 2% or KM 17.5 million in comparison to year 2004. This resulted from growth of core capital by KM 40.8 million, and reduction of additional capital by KM 23.2 million.

The growth of core capital mainly resulted from transfer of income from 2004 (KM 36.8 million to retained undistributed income, that is, allocation of KM 10.4 million to reserve account).

Off-setting capital items (influenced reduction of core capital) increased by KM 6.4 million due to growth of uncovered losses from previous years by KM 1.5 million and current losses of KM 5.4 million. This was influenced by decreased intangible assets in banks by 0.5 million.

Decreased additional capital of KM 23 million mainly resulted from transfer of the profit from 2004 to core capital (KM 39 million), increased subordinated debts of KM 10 millions in one bank and increased general reserves for loan loses of KM 5.7 million.

These changes influenced structure of regulatory capital, that is, participation of core capital increased from 79% to 81%.

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[10] Regulatory capital as defined by Article 8 and 9 in the Decision on Minimum Standards for Bank Capital Management

[11] The Decision on Changes and Additions to the Decision on Minimum Standards for Bank Capital Management ("Official Gazette F BiH", no. 18/03).

[12] Source of information is quarterly Report on Capital Positions in Banks (Form 1-Schedule A) regulated by the Decision on Minimum Standards for Bank Capital Management.

Above-mentioned changes had positive effect to net capital that was increased by 2% or KM 17.5 million in first quarter of 2005. Therefore, as of 03/31/05, total net capital was KM 1,034 million (KM 870 million in private banks and KM 164 million in state banks).

Ratio between capital and assets, that is capitalization rate in banks as of 03/31/05, was 13.1%, and in comparison to 2004 (13.2%) it records slight change due to proportional growth of capital and assets.

Capital adequacy ratio calculated as net capital against risk weighted assets was 18% for the whole banking sector, which is less by 0.6% in comparison to the end of 2004.

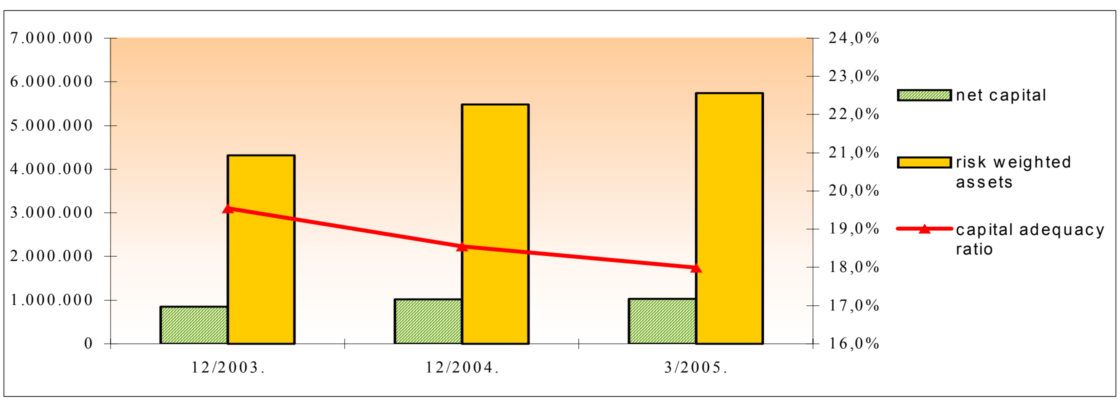
Drop of ratio for the whole system resulted also from drop of capital adequacy ratio in state banks from 59.1% (year 2004) to 56.3% and continuing drop of this ratio in private banks from 16.4% (year 2004) to 16%.

While performing supervision of performance and financial positions of banks in the F BiH, as regulated by the Law, FBA issues orders towards banks to undertake actions for strengthening of capital base and provision of adequate capital in order to strengthen safety in banks individually and in the banking system in whole.

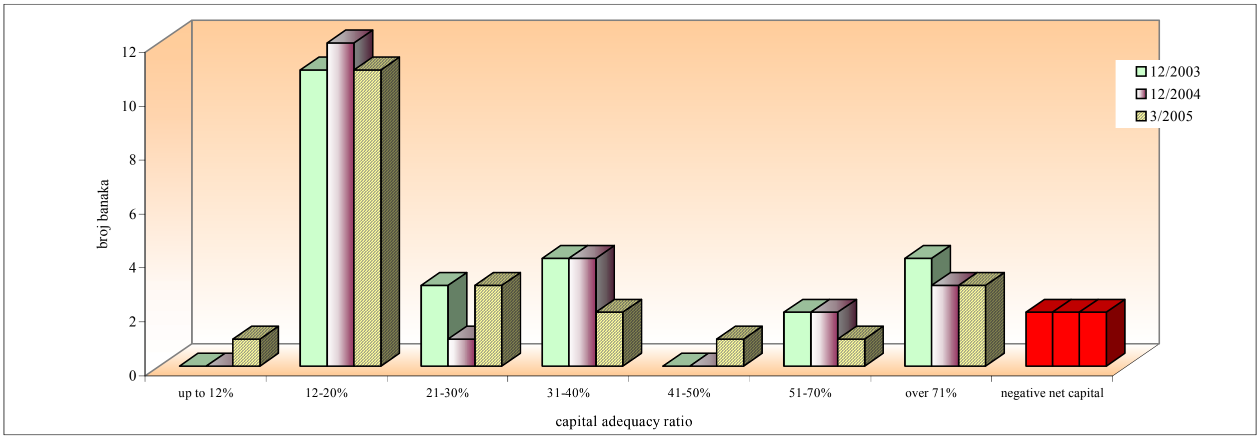
Schedule 17: *Net Capital, Risk Weighted Assets and Capital Adequacy Ratio*

DESCRIPTION	12/31/03	12/31/04	03/31/05	RATIO	
				3/2	4/3
1	2	3	4	5	6
NET CAPITAL	840,605	1,016,333	1,033,878	121	102
RISK WEIGHTED ASSETS AND CREDIT EQUIVALENTS	4,306,774	5,478,655	5,741,606	127	105
NET CAPITAL RATE (CAPITAL ADEQUACY)	19.5%	18.6%	18.0%	95	97

Graph 10: *Net Capital, Risk Weighted Assets and Capital Adequacy Ratio*



Graph 11: *Capital adequacy ratio in banks*



Out of total 24 banks in F BiH, as of 03/31/05, 21 bank had capital adequacy ratio higher than minimum prescribed by the Law of 12% (four banks over 50%), while two banks (under provisional administration) had negative capital adequacy ratio.

In the second group (ratio between 12% and 20%) there were 11 banks, while there were five banks with ratio between 21% and 40%. But, four largest banks by size of assets (which participate with 68% in total assets of the banking sector) had capital adequacy ratio slightly over the minimum prescribed by the Law (between 13.0% and 14.6%).

Any further growth of risk assets has to be followed by adequate growth of capital, and in that sense banks are required to pass program for managing capital and to monitor implementation of the program in order to maintain size and quality of capital at least within the minimum standards prescribed by the Law.

Further strengthening of capital base will be priority task in majority of banks, especially after implementation of new capital recording format. This is especially important for the largest banks in the system in order to preserve stability and safety of all banks in the whole banking system. FBA will pass appropriate decision necessary to strengthen capital base in banks and that will guaranty their stability and safety.

2.1.3. Assets and Asset Quality

The Decision on Minimum Standards for Managing Credit Risk and Assets Classification in Banks (the Decision) determines criteria for assessment of banks' risk exposure by means of evaluating their assets' quality and adequacy of their reserves for loan and other losses by placements and balance sheet and off-balance sheet risk item.

Gross assets[13] in the balance sheet of banks in the Federation of BiH as of 03/31/05 was KM 8 billion, which is higher by 2% or KM 160 million in comparison to end of 2004. Off-balance sheet risk items were KM 1,148 million and they increased by 10% or KM 101 million.

[13] Information from the Report on Assets Classification in balance sheet and off-balance sheet.

Total assets, including off-balance sheet items (assets)[14], were 9.2 billion of KM and they increased by 3% in comparison to end year 2004.

Schedule 18: *Assets, off balance sheet items and potential loan losses*

In 000 KM

DESCRIPTION	AMOUNT (in 000 KM)						RATIO	
	12/31/03	Structure %	12/31/04	Structure %	03/31/05	Structure %	4:2	6:4
1.	2.	3.	4.	5.	6	7	8	9
Loans	3,272,569	54.5	4,209,441	53.5	4,391,478	54.7	129	104
Interests	26,395	0.4	29,856	0.4	32,436	0.4	113	109
Past due receivables	171,821	2.9	209,218	2.7	232,489	2.9	122	111
Receivables on paid guarantees	5,353	0.1	5,026	0.1	4,940	0.1	94	98
Other placements	50,906	0.9	40,811	0.4	31,766	0.4	80	78
Other assets	2,468,073	41.2	3,377,845	42.9	3,339,004	41.5	137	99
TOTAL ASSETS	5,995,117	100.0	7,872,197	100.0	8,032,113	100.0	131	102
OFF BALANCE SHEET	749,382		1,046,809		1,147,531		140	110
BALANCE SHEET AND OFF BALANCE SHEET	6,744,499		8,919,006		9,179,644		132	103
General credit risk and potential loan losses	247,369		282,586		290,501		114	103
Allocated general and special reserves for loan losses	247,411		285,270		290,771		115	102

Out of total assets with off-balance sheet, non-risk assets participate with KM 3.1 billion or 34%. This is less by one percent in comparison to the end of 2004.

The growth of credit placements (by 5%) resulted in changed risk assets structure and increased participation of credit placements from 58.1% to 59.6%. We should emphasize that past due receivables increased by 11% and that reflected to their participation, which increased by 0.2 percent.

Analysis of assets structure changes in banks displayed that six banks (three under provisional administration) reported reduction of credit placements, eight banks reported credit growth ratio over 5%, while in other banks the growth ratio was between 0.2% and 4%. Three largest banks in the F BiH increased credit placements by KM 120 million, which represents 59% out of total growth for the whole banking sector.

Analysis of credit structure by industries brings conclusion that placements decreased in sector of government institutions, public enterprises and bunking institutions, while placement to other sectors increased. The major growth of KM 125 million or 5% was recorded with placements approved to private enterprises and that reflected to participation of those placements in total sector structure of loans from 43.7% to 44.4%. Loans approved to citizens increased by 4% or KM 90 million, and at the same time their participation in total loans decreased by 0.2%.

Changed structure of industries participation in total structure of loans is presented in the following schedule:

[14] Assets, as defined by the Article 2 of the Decision on Minimum Standards for Managing Credit Risk and Assets Classification in banks

Schedule 19: *Structure of loans by sectors*

-In 000 KM-

SECTORS	12/31/03		12/31/04		03/31/05		RATIO	
	Amount	Participation %	Amount	Participation %	Amount	Participation %	4/2	6/4
1	2	3	4	5	6	7	8	9
Governmental institutions	24,526	0.7	34,348	0.8	31,353	0.7	140	91
Public enterprises	217,587	6.3	203,697	4.6	196,226	4.2	94	96
Private enterprises and assoc.	1,439,009	41.7	1,932,203	43.7	2,057,158	44.4	134	105
Non-profit. Organizations	3,015	0.1	3,619	0.1	4,310	0.1	120	119
Banking institutions	33,281	1.0	34,082	0.7	32,568	0.7	102	96
Citizens	1,676,325	48.6	2,139,700	48.4	2,229,311	48.2	128	104
Other	55,999	1.6	76,036	1.7	77,981	1.7	136	103
TOTAL	3,449,742	100.0	4,423,685	100.0	4,628,907	100.0	128	105

As with deposits, we should emphasize that maturity adjustments of loans maintained positive growth trend with short-term loans which increased by 6%. Long-term had growth ratio of 4% and analysis by sectors displayed that 91% of loans approved to citizens and 56% to private enterprises are long-term.

Schedule 20: *Maturity Adjustments of Loans*

-In 000 KM-

LOANS	12/31/03		12/31/04		03/31/05		RATIO	
	Amount	Participation %	Amount	Participation %	Amount	Participation %	4/2	6/4
1	2	3	4	5	6	7	8	9
Past due receivables and off-balance sheet liabilities paid	177,174	5.1	214,244	4.8	237,429	5.1	121	111
Short-term loans	776,014	22.5	991,183	22.4	1,054,432	22.8	128	106
Long-term loans	2,496,554	72.4	3,218,258	72.8	3,337,046	72.1	129	104
TOTAL LOANS	3,449,742	100.0	4,423,685	100.0	4,628,907	100.0	128	105

Above reported changes had positive effect to maturity adjustment of assets and liabilities, that is, had positive effect to imbalance in maturity adjustments of particular items of assets and liabilities. This mainly resulted from activities and actions implemented by banks requested by FBA. Anyhow, some banks still have maturity mismatch of remaining past due financial assets and liabilities. FBA issued an order to resolve this by the end of the prescribed deadline.

Since placements, that is loans, are the part of assets with highest risk, the quality of loans represents one of the most significant factors of stability and success of performance. Rating of assets quality is actually estimation of credit risk in banks, that is, identification of potential loan losses that are recognized as loan loss provisions.

Quality of assets and off-balance sheet risk items, general credit risk and potential loan losses are presented, by classification categories[15], in the following schedule:

[15] As it is regulated in the Article 22 of the Decision on Minimum Standards for Managing Credit Risk and Assets Classification in Banks, banks have to allocate and maintain reserves for general and special loan losses in percentages according to classification of loans: A 2%, B 5% to 15%, C 16% to 40%, D 41% to 60% and E 100%.

Schedule 21: *Classification of Assets, General Credit Risk (GCR) and Potential Loan Losses (PLL) and Off-Balance Sheet Items (write offs and suspended interest)*

Classification category	AMOUNT (in 000 KM) AND PARTICIPATION (in %)									RATIO	
	12/31/03			12/31/04			03/31/05				
	Asses Classif.	Particip. %	GCR PLL	Asses Classif.	Particip. %	GCR PLL	Asses Classif.	Particip. %	GCR PLL	5/2	8/5
1	2	3	4	5	6	7	8	9	10	11	12
A	5,881,803	87.2	70,974	7,880,355	88.4	94,492	8,115,773	88.4	99,981	134	103
B	563,498	8.4	46,657	730,737	8.2	53,633	759,981	8.3	55,508	130	104
C	152,581	2.3	44,593	144,732	1.6	42,287	141,488	1.5	39,595	95	98
D	139,311	2.0	77,839	162,299	1.8	91,294	161,858	1.8	94,876	117	98
E	7,306	0.1	7,306	883	0.0	880	544	0.0	541	12	62
TOTAL	6,744,499	100.0	247,369	8,919,006	100.0	282,586	9,179,644	100.0	290,501	132	103
OFF-BALANCE SHEET											
E	341,166	79.8		342,565	83.3		357,727	84.7		100	104
Susp. interest	86,205	20.2		68,680	16.7		64,837	15.3		80	94
TOTAL	427,371	100.0		411,245	100.0		422,564	100.0		96	103

If we make analysis of assets quality with off-balance sheet items included, it is possible to notice that there was growth of classified assets (B to E) by 2% or KM 25 million, at the same time poor quality assets decreased by 1% or four million KM. In first quarter of 2005, banks charged off from balance sheet to off-balance sheet, that is, wrote off receivables of KM 18 million and suspended interest of total two million KM. In same period banks performed permanent write offs of assets of KM 1.9 million, and permanent write offs of suspended interest was KM 0.5 million. Banks collected earlier written off assets of total KM six million and collected suspended interest was KM 1.6 million in this period. This had positive influence to banks' profitability.

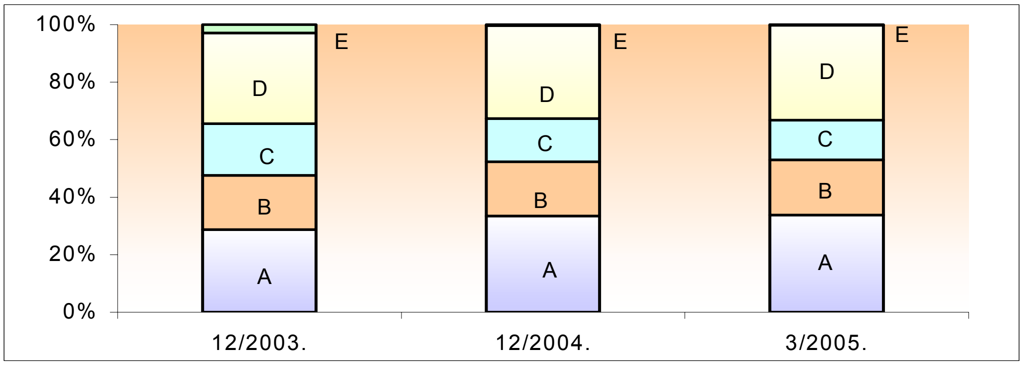
At the end of first quarter of 2005, balance of written off assets was KM 358 million which is more by 4% in comparison to the end of 2004. While suspended interest was KM 65 million or less by KM four million or 6% in comparison to the end of last year.

Level of general loan risk and estimated loss by classification categories, determined upon criteria and methodology regulated by the FBA's decisions, their trends and structure for the whole banking sector are presented in the following schedule and graph:

Schedule 22: *Structure and Trend of General Credit Risk and Potential Loan Losses*

Classification Category	AMOUNT (in 000 KM) and STRUCTURE (in %)						RATIO	
	12/31/03		12/31/04		03/31/05		4/2	6/4
1	2	3	4	5	6	7	8	9
A	70,974	28.7	94,492	33.4	99,981	34.4	133	106
B	46,657	18.9	53,633	18.9	55,508	19.1	115	103
C	44,593	18.0	42,287	15.0	39,595	13.6	95	94
D	77,839	31.5	91,294	32.4	94,876	32.7	117	104
E	7,306	2.9	880	0.3	541	0.2	12	61
TOTAL	247,369	100.0	282,586	100.0	290,501	100.0	114	103

Graph 12: *Structure and Trend of General Credit Risk and Potential Loan Losses*



Based on reports from banks, banks allocated reserves for loan losses as regulated by the regulations and estimated level of credit risk.

In comparison to the end of 2004, analysis of the reserves allocated, in general and by classification category, showed that reserves for general credit risk and potential loan losses increased by 3% and were KM 291 million or 3.2% of total assets, including off-balance sheet. In first quarter of 2005, banks allocated average reserves for category B of 7.3%, for C 28%, for D 58.6% and E 100%. This can be considered satisfactory.

Assets quality analysis, that is, analysis of loan portfolios in banks individually, as well as on site examinations in banks showed that key risk in majority of banks is still credit risk, that is, existence of problem loans originated to legal entities (enterprises).

The FBA ordered corrective actions to banks with poor quality assets, banks had to prepare program for amelioration of existing practices for managing credit risk, that is, assets quality. Also, they have to decrease existing concentrations, resolve poor quality assets and prevent any further deterioration of assets. FBA continuously monitors implementation of those actions through reports submitted by banks, as well as during on site examinations in banks.

Transactions with Related Entities

While operating, banks are exposed to different types of risks, among the most dangerous operations are transactions with related entities.

The Agency has determined, in accordance with the Basle Principles, certain prudential principles and requirements regulating operations with bank related entities[16]. That is also regulated by the Decision on Minimum Standards for Bank Operations with Related Entities that regulated in detail modes and conditions operations with related entities. The Decision and the Law regulate the duty of the Supervisory Board of the Bank, which has to adopt, upon the proposal of the General Manager, special policies regulating operations with related entities and to monitor implementation of those policies.

FBA Decisions regulate special set of reports showing transactions with one part of related entities, including loans and potential and accepted off-balance sheet liabilities (guarantees, letters of credit, accepted loan payables) since those represent the most frequent and the riskiest types of transactions between banks and their related entities. The set of reports includes information on loans approved to the following categories of related entities:

[16] Article 39, item 2 of the Law on Changes and Additions to the Law on Banks defines term “entities related to the bank”, excluding bank´s employees.

- Shareholders with more than 5% of voting shares,
- Members of the Supervisory Board and senior management in the bank and
- Subsidiaries and other enterprises related to the bank through capital

Schedule 23: *Transactions with Related Entities*

000 KM

Description	APPROVED LOANS			RATIO	
	12/31/03	12/31/04	03/31/05	3/2	4/3
1	2	3	4	5	6
Shareholders with over then 5% of voting shares, subsidiaries and other enterprises related to the bank through capital	37,050	40,084	41,860	108	104
Members of the Supervisory Board	388	141	162	36	115
Management and employees of the bank	1,670	2,392	2,298	139	96
TOTAL	39,108	42,617	44,320	109	104
POTENTIAL AND ACCEPTED OFF-BALANCE SHEET LIABILITIES	8,689	3,235	2,246	37	69

The Agency pays special attention (during on-site examinations) to banking operations with related entities. FBA examiners issue on-site orders for elimination of found oversights, determine deadlines and start legal procedures. Part of those activities is monitoring and supervision of execution of ordered corrective actions.

2.2. Profitability

According to the income statements for first quarter of 2005, banks in the Federation of BiH reported positive financial result – profit of KM 16.3 million. This result represents significant growth of 59% for the whole system in comparison to the same period of 2004 when the profit reported was KM 10.3 million. This amelioration resulted only from profit growth, while loss remained same as last year.

Positive financial result was reported by 15 banks of total KM 21.7 million, which is more by 39.8% or KM 3.2 million in comparison to same period 2004. At the same time, nine banks reported operating loss (four state and five privately owned) of KM 5.4 million, which is growth of only 3.1% in comparison to same period 2004.

More detailed information is presented in the following schedule:

Schedule 24: *Financial result realized: profit/loss*

- 000 KM-

Date/Description	Whole system		Private banks		State banks	
	Amount	Number of banks	Amount	Number of banks	Amount	Number of banks
03/31/03						
Loss	-6,713	9	-3,025	4	-3,688	5
Profit	20,664	17	20,118	15	546	2
Total	13,951	26	17,093	19	-3,142	7
03/31/04						
Loss	-5,261	9	-4,884	5	-377	4
Profit	15,541	17	13,895	14	1,646	3
Total	10,280	26	9,011	19	1,269	7
03/31/05						
Loss	-5,426	9	-4,725	5	-701	4
Profit	21,734	15	21,006	13	728	2
Total	16,308	24	16,281	18	27	6

As in other segments, this one is characterized by concentrations: out of total profit (KM 21.7 million), 73.3% or KM 15.9 million was with four largest banks in the system. It is same with total loss (KM 5.4. million) since 72.4% or KM 3.9 million was reported by two banks. Remaining state owned banks did not influence significantly the total profitability, and four banks under provisional administration operated with loss.

Individual analytical information from banks, as well as indicators for quality rating lead to conclusion that general profitability of the system is improving due to general improving trend and stabilization of banking sector, and fewer large banks hold the concentration (owner by foreign investors).

In the structure of total income, net interest income still has growing trend and it participates with 59.1% of total income (in the same period in 2004 it was 55.8%), while participation of operational income decreased from 44.2% to 40.9%.

Although net interest income was higher by 21% in comparison to same period last year, it did not follow growth of credit placements – interest-bearing assets (average growth of 25%). The main reason for that was drop of interest rates and interest margin, high participation of loan-term loans in the structure of loan portfolio, but also, growth of interest-bearing sources of financing (borrowings and term deposits) which influenced growth of interest expenses by 35%.

Operating income increased by 6% in comparison to the same period last year, while their participation in total income decreased by 4%, mainly due to decreased other operating income, which is mainly consisted of decreased reserves.

Total non-interest bearing expenses were higher by 10% in comparison to same period last year, which mainly resulted from growth of operating expenses of 14% and participation of those expenses in total income decreased from 91% to 87% in comparison to the observing period last year. From profitability aspect, we should make a conclusion that positive effect was recorded with reserves for potential losses, which were higher by only 2% in comparison to last year, and their participation decreased from 25% to 23% in the structure of expenses. Anyhow, prudential standards and growth of credit risk imply that banks, no mater to positive financial results, should allocate more through expenses and maintain adequate reserves for loan losses in order to depreciate future losses and protect capital.

The structure of other non-interest bearing expenses did not change significantly, and in comparison to previous year they increased by 13%.

Trend and structure of total income and expenses is presented in the following schedule:

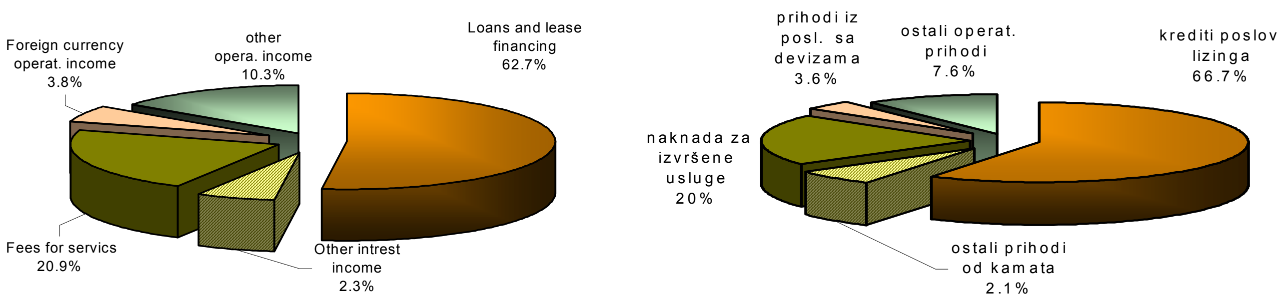
Schedule 25: *Structure of total income*

-In 000 KM-

Structure of total income	12/31/03		12/31/04		03/31/05		RATIO	
	Amount	%	Amount	%	Amount	%	4/2	5/6
1	2	3	4	5	6	7	8	9
I Interest income and similar types of income								
Interest bearing deposit accounts with depository institutions	7,071	5.5	6,119	4.3	9,806	5.8	87	160
Loans and lease financing	67,271	52.2	83,119	58.4	102,689	60.9	124	124
Other interest income	1,010	0.8	3,330	2.3	3,494	2.1	330	105
TOTAL	75,352	58.5	92,568	65.0	115,989	68.8	123	125
II Operating income								
Service Fees	27,511	21.4	29,591	20.9	33,643	20.0	108	114
Foreign Exchange Income	7,414	5.7	5,417	3.8	6,089	3.6	73	112
Other operating income	18,517	14.4	14,734	10.3	12,809	7.6	80	87
TOTAL	53,442	41.5	49,742	35.0	52,541	31.2	93	106
TOTAL INCOME (I+II)	128.794	100,0	142.310	100,0	168.530	100,0	111	118

Graph 13: *Structure of total income*

31.03.2004. **31.03.2005.**



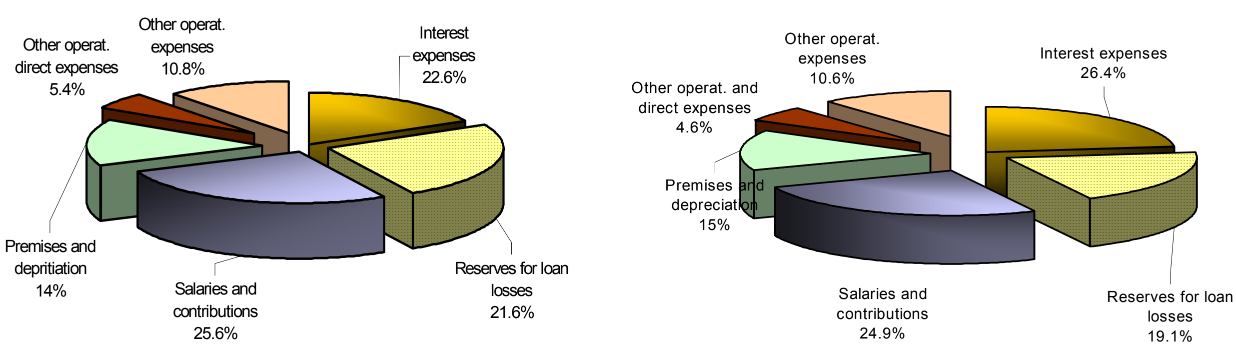
Schedule 26: *Structure of total expenses*

- In 000 KM-

	Structure of total expenses	12/31/02		12/31/03		09/30/04		RATIO	
		Amount	%	Amount	%	Amount	%	4/2	5/6
	1	2	3	4	5	6	7	8	9
I	**Interest expenses and other similar expenses**								
	Deposits	15,280	13.3	24,186	18.3	31,500	20.7	158	130
	Obligations based on loans and other borrowings	3,831	3.3	4,971	3.8	7,872	5.2	130	158
	Other interest expenses	1,048	0.9	651	0.5	799	0.5	62	123
	TOTAL	20,159	17.5	29,808	22.6	40,171	26.4	148	135
II	**II Total non-interest bearing expenses**								
	Provisions for general credit risk & potential loan and other losses	28,159	24.5	28,487	21.6	29,039	19.1	101	102
	Costs of salaries and benefits	30,501	26.6	33,754	25.6	37,940	24.9	111	112
	Costs of business premises and depreciation	16,980	14.8	18,527	14.0	21,973	14.4	109	119
	Other operating and direct expenses	5,988	5.2	7,169	5.4	7,027	4.6	120	98
	Other operating expenses	13,056	11.4	14,285	10.8	16,072	10.6	109	113
	TOTAL	94,684	82.5	102,222	77.4	112,051	73.6	108	110
	TOTAL EXPENSES (I + II)	114,843	100.0	132,030	100.0	152,222	100.0	115	115

Graph 14: *Structure of total expenses*

31.03.2004. **31.03.2005.**



Following schedules show the most significant ratios necessary to assess profitability, productivity and efficiency in banks:

Schedule 27: *Profitability, Productivity and Efficiency Ratios by Periods*

-In % -

RATIOS	03/31/03	03/31/04	03/31/05
Return on Average Assets	0.88	0.72	0.85
Return on Average Total Capital	6.76	5.75	7.11
Return on Average Share Capital	8.17	6.89	8.57
Net Interest Income/Average Assets	4.60	4.08	3.93
Fee Income/Average Assets	4.27	3.43	2.73
Total Income/Average Assets	8.88	7.51	6.66
Operating and Direct Expanses[17]/Average Assets	2.79	2.20	1.87
Operating Expenses/Average Assets	5.17	4.55	3.94
Total Non-interest Expanses/Average Assets	7.95	6.76	5.81

Schedule 28: *Profitability, Productivity and Efficiency Ratios as of 03/31/05*

-In % -

RATIOS	03/31/05		
	STATE BANKS	PRIVATE BANKS	AVERAGE IN F BiH
Return on Average Assets	0.03	0.89	0.85
Return on Average Total Capital	0.07	8.62	7.11
Return on Average Share Capital	0.08	10.53	8.57
Net Interest Income/Average Assets	3.25	3.97	3.93
Fee Income/Average Assets	5.31	2.59	2.73
Total Income/Average Assets	8.56	6.56	6.66
Operating and Direct Expanses[18]/Average Assets	3.63	1.79	1.87
Operating Expenses/Average Assets	4.90	3.89	3.94
Total Non-interest Expanses/Average Assets	8.53	5.68	5.81

Analysis of basic indicators of profitability showed that, although income was higher in comparison to the same period last year since ROAA (return on average assets) was 0.85% and ROAE (return on average equity/share capital) was 8.57%, anyhow, productivity in banks (total income against average assets) as well as net interest and operating income by one unit of average assets were lower due to, from one hand, faster growth of assets against total income (net interest and operating income) and from the other hand due to significant participation of assets which are not earning income.

Efficiency of banks' operations, measured as relation assets/employee, improved. This resulted from faster growth of average assets of 27% in comparison to growth of average number of employees 4%.

Profitability of banks in future period will mostly depend on assets' quality, that is, banks' exposure to credit risk and efficiency of managing operating expenses. Saying that key factor for efficiency and profitability in each bank is management quality and operational policy, since that has the most direct impact to bank's performance.

Also, new market conditions will force banks to adopt new concepts of operational policies adjusted to competitive banking striving for maximum profit, providing stability and adequate

[17] Expenses include reserves for potential credit losses.
[18] Expenses include reserves for potential credit losses.

management and control of all operational risks in the bank, and above all, credit risk. But, taking place in international financial business and market will expose banks to larger market risks: interest rate risk, foreign exchange risk and price risk. Earning more profit from retained income as internal source of funding in banks would provide stronger capital and increase base for further development and growth.

III. CONCLUSION

Consolidation and stabilization of banking sector in the Federation of BiH have reached satisfactory level and upcoming activities should provide further progress and development of the system. On that account, continuous engagement of all parts of the system, regulatory and administrative authorities in order to provide the most favorable environment in economy which would be stimulating to banks and vice versa to economy.

In other to achieve above-mentioned goals, further involvement of authorized institutions and entities in Bosnia and Herzegovina and the Federation of BiH will be necessary in order to:

- fastening reconstruction process in material sector in order to achieve level attained by monetary and banking system;
- finalization of privatization process in state banks, that is, resolving their status;
- conclusion and annexation of regulations for sector of finance, the regulations referring to operation or status of micro credit institutions, BOR and Investment Bank in the Federation of BiH d.d. Sarajevo etc;
- amelioration of environment for bank operations in whole Bosnia and Herzegovina;
- accelerating implementation of special court sections for economy;
- implementation of more efficient procedures for collection of collateral;
- passing the Law on Protection of Creditors and implementing greater and defined duties of debtors;
- further improvement of legal framework for banking system and sector of finance, starting from Basle Principles and European banking directives;
- Supporting activities for founding banking agency on the state level etc.

The Banking Agency of the Federation of BiH in future will:

- continuing supervision of banks, on-site and off-site;
- finalization of provisional and liquidation administrations in banks;
- insist on strengthening of capital in banks, especially those banks which have recorded growth above average;
- in order to protect depositors, implement special supervision in banks with large savings and other types of deposits;
- further development of regulations under authority of the Agency starting from Basle Principles and incorporating European Directives, as part of preparation process for becoming part of European Union;
- initiate further education of members in Supervisory Boards in banks;
- work on continuous education and training of Agency staff;
- maintain continuity of control of payment system;
- continue effective monitoring of banks activities for prevention of money laundry and financing of terrorism, and ameliorate cooperation with other supervisory and examiners institutions;
- provide effective operation of new informational system for early warning and prevention of weaknesses in banks;
- improve cooperation with Association of banks;

- establishment of cooperation with supervisory institutions in countries whose natives are investors in our country
- take active part in preparation for passing laws on banks for the whole state
- organize counseling and provide advising on application of regulations passed by the FBA etc

And, as the most important part of the system, banks have to concentrate their actions to:

- further strengthen capital in correlation with growth of assets;
- improve quality of assets;
- adopt and implement new principles for operations, policies and procedures adjusted to competitive market conditions;
- strengthen internal control systems and establish internal audits, and provision of their independence;
- faster development of credit/debit card operations and electronic banking;
- development of procedures for control and improvement of IT;
- training and staff improvement;
- maintaining prevention of money laundering and terrorism financing by implementation of adopted policies and procedures;
- improvement of Bankers Association etc.