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. 06. 2014

Sarajevo, August 2014

The Banking Agency of the Federation of B&H, as a regulatory institution conducting bank supervision, has prepared the Information on the Banking System of the Federation of B&H (as of 30.06.14) based on financial statements and other information and data provided by banks. This also encompassed results and information obtained during on-site examinations in banks and off-site financial analyses in the Agency.

I INTRODUCTION

For quite some time, the operations of the banking sector in the Federation of B&H and B&H have been characterised by the effects of the economic and financial crisis, which also impacts most business segments of banks. The main characteristics of business operations in the first half of 2014 were: the stagnation of the growth and total development of the banking sector, the further decrease in the deposit base and foreign sources of funding in the form of credit lines, credit activities recorded a slight increase, and there is still a negative trend in the loan portfolio quality, which caused the key asset quality indicators to deteriorate as a result of past due receivables and non-performing loans. On the other hand, there is a continued increase in savings, and the liquidity, profitability and capitalisation of the banking sector can be assessed as satisfactory, and it can thus be concluded that the banking sector continues to be stable and safe.

It is to be expected that the natural disasters (floods and landslides) that hit the population and economic entities in Bosnia and Herzegovina in May 2014 will have negative effects on the banking system in Bosnia and Herzegovina in the second half of this year, primarily in terms of further deterioration of asset quality indicators and the increase in value adjustment costs and loan write-offs.

As of 30.06.14, there were 17 licensed banks in the Federation of B&H, and the headcount in banks of the Federation of B&H stood at 6 996, down by 0.8% or 55 employees compared to the end of 2013. The headcount in banks of the Federation of B&H has continuously decreased since the end of 2008, when the number of employees was 7 997, and is down by one thousand employees or 12.5% in the past 5.5 years.

The balance sheet total of the banking sector as of the first half of 2014 amounted to KM 15.4 billion, and is at approximately the same level as it was at the end of 2013. Even though the balance sheet total was down by 1.4% or KM 209 million in the first quarter of 2014, in the second quarter, it was up by 1.2% or KM 184 million compared to the end of the first quarter of 2014.

Asset structure underwent minor changes related to two key assets items: increase in loan shares from 70.3% to 71.9% and decrease in cash funds from 28.6% to 27.1%.

In the first half of 2014, cash funds were down by 5.5% or KM 242 million and amounted to KM 4.2 billion as of 30.06.2014. The recorded drop in cash funds is the result of the decrease in deposits, loan commitment payments and credit growth.

Loans recorded a slight increase of 2% or KM 238 million and amounted to KM 11 billion as of the end of the first half of 2014. Total non-performing loans amount to KM 1.7 billion as of 30.06.2014, up by 6.5% or KM 103 million compared to the end of 2013. The share of non-performing loans in total loans rose from 14.6%, to which it amounted at the end of 2013, to 15.2% as of the end of the first half of this year. Out of total corporate loans, 20.2% refer to non-performing loans, while their share in retail loans is 10%.

In the banks' liabilities structure, deposits in the amount of KM 11.4 billion and with a share of 74% are still a dominant source of funding for banks in the Federation of B&H. In the first half of 2014, total deposits were down by 1% or KM 111 million. On the other hand, savings deposits (being the key segment of the deposit and financial potential of banks) were up by 3% or KM 184 million in the same period and amounted to KM 6.4 billion as of 30.06.2014.

Loan commitments in the amount of KM 1 billion were down by 4.3% or KM 45 million in the first half of 2014 and their share in the liabilities structure was down from 6.7%, to which it amounted at the end of 2013, to 6.4% as of 30.06.2014. Over the past three years, due to the impact of the financial and economic crisis, banks incurred a much lower level of foreign debt, while the payment of receivables due decreased these sources by more than 50% (at the end of 2008, they amounted to KM 2.18 billion). Evidently, the financial support of parent banking groups was significantly reduced, so that credit growth in the Federation of B&H will probably be based on the growth of local sources of funding in the coming period.

In the first half of 2014, total capital was up by 3% or KM 72 million, largely prompted by current profit, but also as a result of the increase in share capital on the basis of recapitalisation. As of 30.06.2014, it amounted to KM 2.4 billion.

As of 30.06.2014, regulatory capital amounted to KM 2.3 billion and is at the same level as it was at the end of 2013.

In the first half of 2014, a positive financial result in the amount of KM 85.3 million was recorded at the level of the banking system in the Federation of B&H. A positive financial result in the amount of KM 94.7 million was recorded by 16 banks, while one bank recorded a loss in the amount of KM 9.4 million.

One of the key indicators of the banks’ capital strength and adequacy is the capital adequacy ratio. At the banking sector level, this ratio amounted to 17.7% as of 30.06.2014, which is lower by 0.3 percentage points compared to the end of 2013. However, this is still significantly above the legal minimum (12%) and represents a satisfactory capitalisation rate of the overall system.

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 30.06.2014, there were 17 banks with a banking licence in the Federation of B&H. The number of banks is the same as on 31.12.2013. 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 six months of 2014, there was no major expansion of the banks' network of organisational units. This is to say that the expansion trend continued, but in much lesser extent than before, chiefly attributable to the financial crisis. 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 were a total of 38 such changes among banks in the Federation of B&H (32 changes on the territory of the Federation of B&H and six changes on the territory of Republika Srpska): nine new organisational units were established, 15 were closed and 14 underwent changes.

Subsequent to such changes, banks in the Federation of B&H had a total of 573 organisational units as of 30.06.2014, down by 1.3% compared to 31.12.2013.

There were six banks from Republika Srpska with 32 organisational units in the Federation of B&H, which is an increase of 18.5% compared to 31.12.2013 (27).

As of 30.06.2014, seven banks from the Federation of B&H had 48 organisational units in Republika Srpska, and eight banks had 11 organisational units in Brčko District.

As of 30.06.2014, all banks had licences to effect interbank transactions within the domestic payment system, and 16 banks had secured deposits.

1.2. Ownership Structure

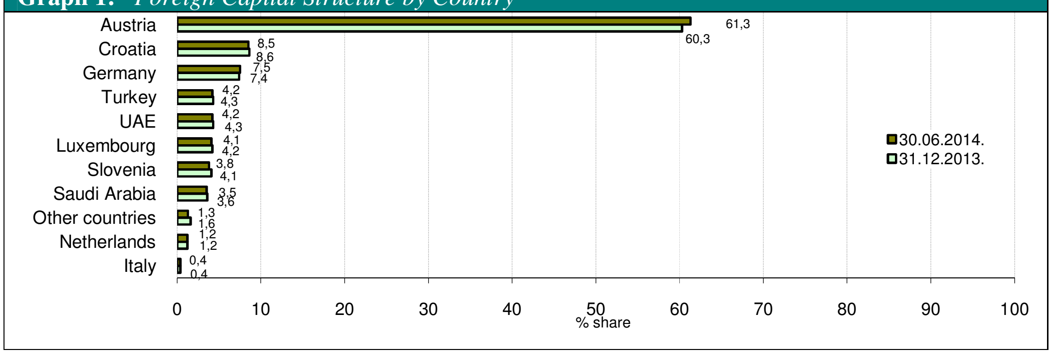
The ownership structure of banks[1] as of 30.06.2014, assessed on the basis of available information and reviews conducted in the banks themselves, is as follows:

- In private or mostly private ownership 16 banks (94.1%)
- In state or mostly state ownership[2] 1 bank (5.9%)

Out of the 16 banks in mostly private ownership, six 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 30.06.2014 changed only slightly compared to those as of 31.12.2013: the largest share of foreign capital in the amount of 61.3% refers to shareholders from Austria, followed by shareholders from Croatia with 8.5% and Germany with 7.5%. Other countries hold individual shares below 5%.

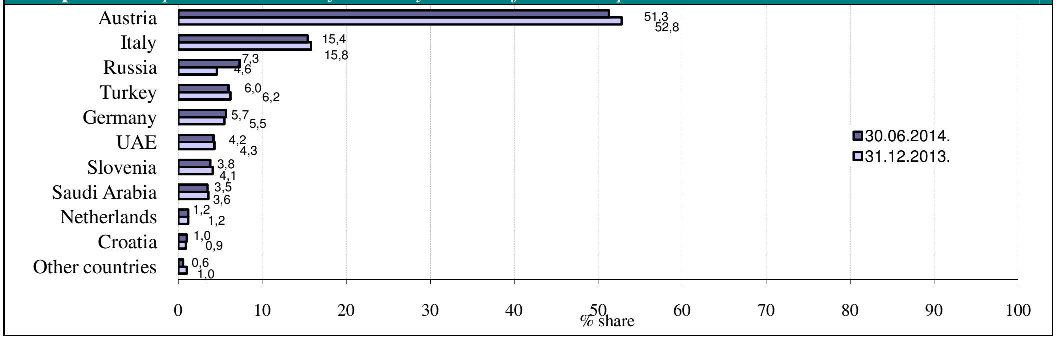
Graph 1: *Foreign Capital Structure by Country*



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 (direct or indirect via group members) of banks in the Federation of B&H. According to this criterion, the conditions also changed only slightly compared to the end of 2013: the share of banking groups and banks from Austria amounts to 51.3%, followed by Italian banks with a share of 15.4%, while Russia's share[3] in one bank in the Federation of B&H, following recapitalisation in the second quarter, increased from 4.6% to 7.3%, which is the most significant change in the reporting period. Other countries held individual shares below 7%.

[1] The criterion for this particular bank classification is ownership of share capital in banks.
[2] State ownership refers to local state capital of B&H.
[3] In 2012, the Russian bank Sberbank purchased Volksbank International from Austria, which also owned Volksbank BH d.d. Sarajevo.

Graph 2: *Capital Structure by Country – Seat of the Group*[4]



The ownership structure may also be observed from the aspect of financial ratios, i.e. according to the total capital value.[5]

-in KM 000-

Table 1: *Ownership Structure by Total Capital*

BANKS	31.12.2012		31.12.2013		30.06.2014		INDEX	
1	2		3		4		5 (3/2)	6 (4/3)
State-owned banks	51 114	2%	51 618	2%	52 029	2%	101	101
Private banks	2 166 261	98%	2 256 327	98%	2 327 675	98%	105	103
TOTAL	2 217 375	100%	2 307 945	100%	2 379 704	100%	105	103

In the first half of 2014, total capital was up by 3% or KM 72 million, largely based on current profit and recapitalisation in the amount of KM 29 million in one bank.

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.

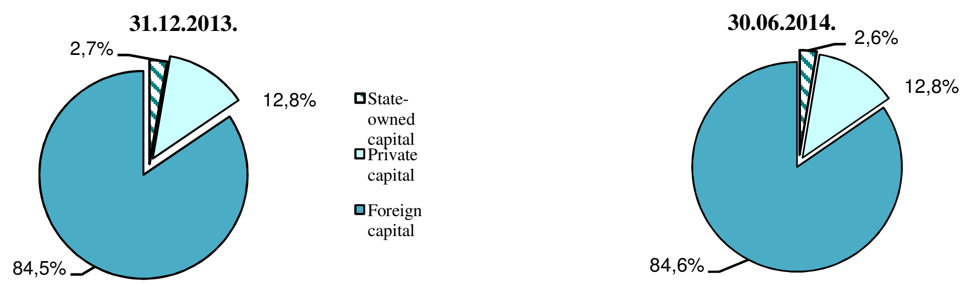
-in KM 000-

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

SHARE CAPITAL	31.12.2012		31.12.2013		30.06.2014		INDEX	
	Amount	Share %	Amount	Share %	Amount	Share %	4/2	6/4
1	2	3	4	5	6	7	8	9
State-owned capital	33 096	2.8	32 364	2.7	32 364	2.6	98	100
Private capital (residents)	164 603	13.7	153 549	12.8	158 623	12.8	93	103
Foreign capital (non-residents)	1 003 907	83.5	1 017 822	84.5	1 046 942	84.6	101	103
TOTAL	1 201 606	100.0	1 203 735	100.0	1 237 929	100.0	100	103

[4] 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.
[5] According to the balance sheet prepared on the basis of the FBA model: starting from 31.12.2011, loan loss provisions formed from profit were also included in total capital (in addition to share capital, issue premiums, retained profit and reserves and other capital (the financial resut of the current period)).

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



In the first six months of 2014, share capital of banks in the Federation of B&H was up by KM 34.2 million or 2.8% compared to 31.12.2013. Share capital rose by KM 4.9 million in one bank after the Agency withdrew its order for the exclusion of the aforementioned amount from capital as well as following recapitalisation in the amount of KM 29.3 million in another bank.

The analysis of the ownership structure of banks from the aspect of 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.

The share of state-owned capital in total share amounts to 2.6% as of 30.06.2014 and is lower by 0.1 index point compared to 31.12.2013.

The share of private capital (of residents) in total share capital amounts to 12.8% and is unchanged compared to 31.12.2013, according to relative indicators. According to absolute indicators, the share is up by KM 5.1 million net due to the revocation of the Agency's order for the exclusion of the amount of KM 4.9 million from one bank's capital as well as due to change and increase in structure after trade in the amount of KM 217 thousand net.

The share of private capital (of non-residents) in total share capital increased by 0.1 percentage points (from 84.5% to 84.6%), according to relative indicators. According to absolute indicators, the share is up by KM 29.3 million due to recapitalisation, and down by KM 217 thousand net due to change and increase in structure after trade.

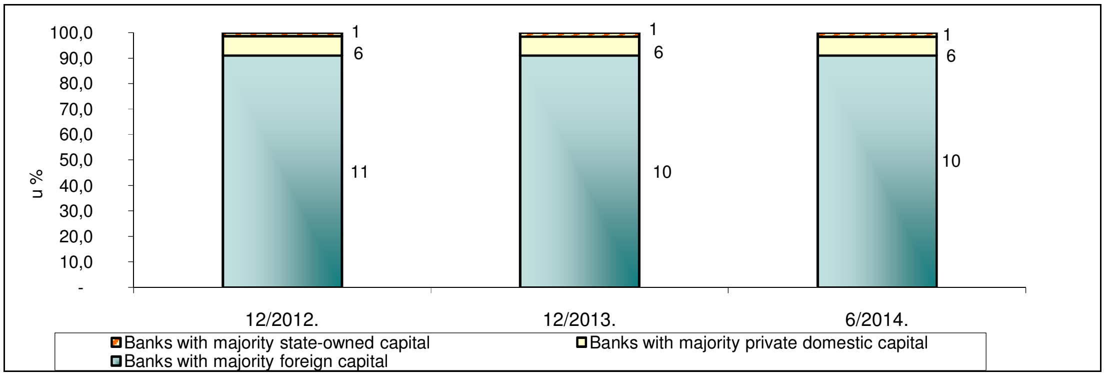
The market share of banks in majority foreign ownership as of 30.06.2014 stood at a high 91.0%, as was the case at the end of 2013, while banks with majority domestic private capital had a 7.3% share and banks with majority state-owned capital a 1.7% share.

- in % -

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

BANKS	31.12.2012			31.12.2013			30.06.2014		
	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 with majority state-owned capital	1	2.3	1.4	1	2.2	1.6	1	2.2	1.7
Banks with majority private domestic capital	6	10.5	7.6	6	9.2	7.4	6	8.6	7.3
Banks with majority foreign capital	11	87.2	91.0	10	88.6	91.0	10	89.2	91.0
TOTAL	18	100.0	100.0	17	100.0	100.0	17	100.0	100.0

Graph 4: *Market Shares by Ownership Type*



1.3. Human Resources

As of 30.06.2014, banks in the Federation of B&H had a headcount of 6 996 employees, 3% of which are employed in banks with majority state-owned capital and 97% of which are employed in private banks.

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

BANKS	HEADCOUNT						INDEX	
	31.12.2012		31.12.2013		30.06.2014		3/2	4/3
1	2		3		4		5	6
State-owned banks	183	3%	200	3%	195	3%	109	98
Private banks	6 947	97%	6 851	97%	6 801	97%	99	99
TOTAL	7 130	100%	7 051	100%	6 996	100%	99	99
Number of banks	18		17		17		94	100

Table 5: *Qualification Structure of Employees*

QUALIFICATION LEVEL	HEADCOUNT						INDEX	
	31.12.2012		31.12.2013		30.06.2014		4/2	6/4
1	2	3	4	5	6	7	8	9
University degree	3 479	48.8%	3 673	52.1%	3 710	53.0%	106	101
Two-year post-secondary school qualification	667	9.3%	601	8.5%	596	8.5%	90	99
Secondary school qualification	2 949	41.4%	2 750	39.0%	2 662	38.1%	93	97
Other	35	0.5%	27	0.4%	28	0.4%	77	104
TOTAL	7 130	100.0%	7 051	100.0%	6 996	100.0%	99	99

In the first half of 2014, the banks' headcount decreased slightly (by 55 employees or 0.8%).
The trend of an improved qualification structure by means of a larger share of employees with university degrees was continued in the first half of 2014 as well, mostly as a result of a reduction in the number of employees with secondary school qualifications by 1% or 88 employees.

One of the indicators affecting the performance assessment of individual banks and the banking system as a whole is staff efficiency, expressed 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	31.12.2012			31.12.2013			30.06.2014		
	Head-count	Assets (000 KM)	Assets per employee	Head-count	Assets (000 KM)	Assets per employee	Head-count	Assets (000 KM)	Assets per employee

State-owned	183	209 971	1 147	200	241 605	1 208	195	267 513	1 372
Private	6 947	14 780 795	2 128	6 851	15 204 945	2 220	6 801	15 154 130	2 228
TOTAL	7 130	14 990 766	2 102	7 051	15 446 550	2 191	6 996	15 421 643	2 204

At the end of the reporting period, there were KM 2.2 million of assets per employee at the banking system level which is almost the same as at the end of 2013.

Table 7: *Assets per Employee – by Group*

Assets (000 KM)	31.12.2012	31.12.2013	30.06.2014
	Number of banks	Number of banks	Number of banks
Up to 1.000	3	1	1
1.000 to 2.000	10	8	9
2.000 to 3.000	4	7	5
Over 3.000	1	1	2
TOTAL	18	17	17

Analytical indicators for individual banks range from KM 950 thousand to KM 3.7 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 2.4 million in the three largest banks in the system.

2. FINANCIAL PERFORMANCE INDICATORS OF BANKS

Off-site bank controls 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.[6]

2.1. Balance Sheet

The balance sheet total of the banking sector at the end of the first half of 2014 amounted to KM 15.4 billion, down by 0.2% or KM 25 million compared to the end of 2013. Changes in the balance sheet

[6] 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 30.06.2014, these items amounted to KM 644 million in the case of one state-owned bank.

total, as well as in key balance sheet categories (loans, deposits, loan commitments, capital, and consequently cash funds), are minor, so that it can be concluded that the situation has been stagnant for an extensive period of time due to the effects of the financial and economic crisis. Key performance indicators of the banking system have generally, with minor oscillations, maintained almost the same level as in the past two years.

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Table 8: *Balance Sheet*

DESCRIPTION	31.12.2012. AMOUNT	Share %	31.12.2013. AMOUNT	Share %	30.06.2014. AMOUNT	Share %	INDEX	
1	2	3	4	5	6	7	8 (4/2)	9 (6/4)
ASSETS:								
Cash funds	3 962 581	26.4	4 417 898	28.6	4 175 428	27.1	111	95
Securities[7]	548 467	3.7	562 513	3.6	590 501	3.8	103	105
Facilities to other banks	78 522	0.5	51 960	0.3	54 501	0.4	66	105
Loans	10 666 124	71.1	10 852 400	70.3	11 090 580	71.9	102	102
Value adjustment	1 007 459	6.7	1 165 928	7.5	1 202 319	7.8	116	103
Net loans (loans minus value adjust.)	9 658 665	64.4	9 686 472	62.8	9 888 261	64.1	100	102
Business premises and other fixed assets	521 493	3.5	512 985	3.3	508 649	3.3	98	99
Other assets	221 038	1.5	214 722	1.4	204 303	1.3	97	95
TOTAL ASSETS	**14 990 766**	**100.0**	**15 446 550**	**100.0**	**15 421 643**	**100.0**	**103**	**100**
LIABILITIES								
LIABILITIES								
Deposits	10 961 001	73.1	11 523 849	74.6	11 412 639	74.0	105	99
Borrowings from other banks	2 000	0.0	0	0.0	0	0.0	n/a	0
Loan commitments	1 141 561	7.6	1 039 381	6.7	994 186	6.5	91	96
Other liabilities	668 829	4.5	575 375	3.7	635 114	4.1	86	110
CAPITAL								
Capital	2 217 375	14.8	2 307 945	15.0	2 379 704	15.4	104	103
TOTAL LIABILITIES (LIABILITIES AND CAPITAL)	**14 990 766**	**100.0**	**15 446 550**	**100.0**	**15 421 643**	**100.,0**	**103**	**100**

-KM 000-

Table 9: *Banks' Assets by Ownership Structure*

BANKS	31.12.2012. No. of banks	Assets (000 KM)		31.12.2013. No. of banks	Assets (000 KM)		30.06.2014. No. of banks	Assets (000 KM)		INDEX	
1	2	3		4	5		6	7		8 (5/3)	9(7/5)
State-owned	1	209 971	1%	1	241 605	2%	1	267 513	2%	115	111
Private	17	14 780 795	99%	17	15 204 945	98%	16	15 154 130	98%	103	100
TOTAL	18	14 990 766	100%	18	15 446 550	100%	17	15 421 643	100%	103	100

In most banks (10), assets are up compared to the end of 2013, while other banks saw a decrease in assets. Two small and one large bank recorded a somewhat bigger increase in assets (10.7%, 12.7% and 7.1%), while a significant drop (13.2%) was recorded by one large bank.

The concentration indicator used for three key segments of banking operations (assets, loans and deposits) is the Herfindahl index.[8]

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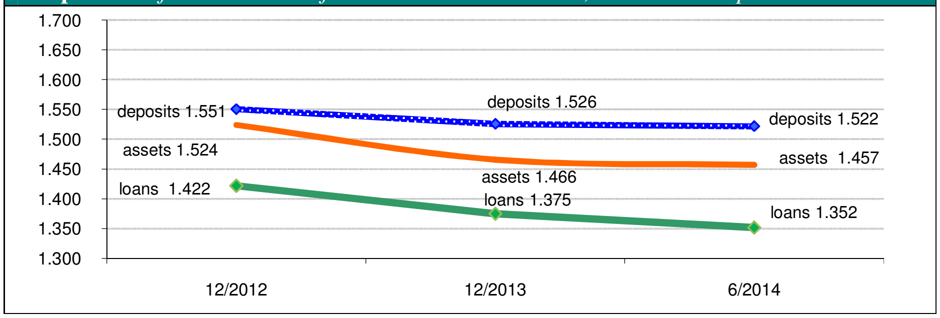
[7] Trading securities, securities available for sale and held to maturity securities.

[8] 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.

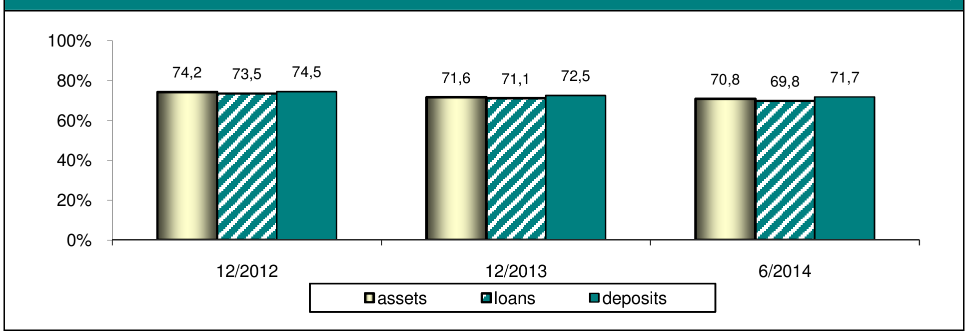
Graph 5: *Herfindahl Indeks of Concentrations in Assets, Loans and Deposits*



In 2014, the Herfindahl index of concentrations in all three relevant categories (assets, loans and deposits) remained almost the same as at the end of 2013, so that it amounted to 1 457 units for assets, 1 352 units for loans, and 1 522 units for deposits as of 30.06.2014, which is indicative of a moderate concentration.[9]

The second concentration indicator for the banking system is the ratio of market concentrations, i.e. The concentration rate[10] (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 70.8% for market share, 69.8% for loans and 71.7% for deposits. Over the past two years, the value of the CR5 went down slightly across all three categories, but the domination of the five largest banks in the system, which hold between 70% and 72% 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 from the aspect of several groups formed according to asset size.[11] Changes in share percentage compared to the end of 2013 are minor, which is the result of slight changes in the assets of most banks.

The banking system is still dominated by the four largest banks with a share of 64.4%, of which the I group (the two largest banks in the system with assets in the amount of over KM 3 billion) has a share of 48.7% and the II group (two banks with assets in the amount ranging from KM 1 billion to KM 2 billion) has a share of 15.7%. The share of the III group (four banks with assets ranging from KM 500 million to KM 1 billion) increased by 0.6 percentage points, i.e. to 21.3%, while the share of the IV

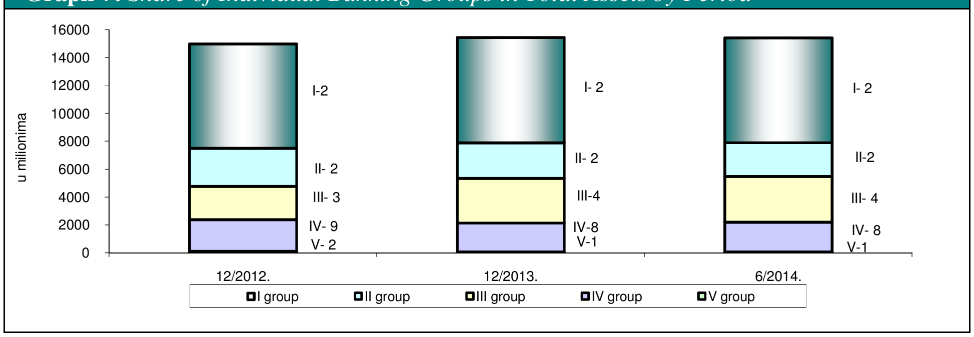
[9] If the value of the HHI is below 1 000, this shows no presence of the concentration on the market, while an index value between 1 000 and 1 800 shows moderate concentration, and a HHI value above 1 800 shows high concentration on the market.
[10] The concentration ratio (CR) rests on the number of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

and largest group (eight banks with assets ranging from KM 100 million to KM 500 million) is 13.8%. 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	31.12.2012. Amount	Share %	No. of banks	31.12.2013. Amount	Share %	No. of banks	30.06.2014. Amount	Share %	No. of banks
I- Over 2.000	7 476	49.8	2	7 546	48.8	2	7 514	48.7	2
II- 1000 to 2000	2 741	18.3	2	2 556	16.5	2	2 415	15.7	2
III- 500 to 1000	2 379	15.9	3	3 195	20.7	4	3 289	21.3	4
IV- 100 to 500	2 280	15.2	9	2 078	13.5	8	2 130	13.8	8
V- Below 100	115	0.8	2	73	0.5	1	74	0.5	1
TOTAL	14 991	100.0	18	14 991	100.0	17	15 422	100.0	17

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



The slight balance sheet total decrease of 0.2% or KM 25 million, i.e. to the level of KM 15.4 billion at the end of the reporting period is mostly a result of the drop in deposits of 1% or KM 111 million, i.e. a drop to the level of KM 11.4 billion, coupled with a drop in loan commitments of 4.3% or KM 45 million, which amounted to KM 1 billion as of 30.06.2014. On the other hand, total capital rose by 3.1% or KM 72 million, originating mostly from profit of the current period and, to a lesser degree, from recapitalisation in one bank. At the end of the first half of 2014, total capital amounted to KM 2.4 billion.

Due to the aforementioned decrease in deposits and loan commitments, coupled with the increase of the securities portfolio and modest credit growth, cash funds dropped by 5.5% or KM 242 million and amounted to KM 4.2 billion as of 30.06.2014.

The slight credit growth from the first quarter of 2014 (1% or KM 104 million) was continued in the second quarter as well (1% or KM 135 million), which cumulatively resulted in a growth rate of 2.2% or KM 238 million for six months of 2014, although it should be noted that the credit growth rate amounted to 1.7% in the past two years. At the end of the first half of 2014, loans amounted to KM 11.1 billion KM.

Investments in securities recorded an increase of 5.0% or KM 28 million (in 2013, their growth was 2.6% or KM 14 million) and amount to KM 591 million as of 30.06.2014, thus having a share in assets of a mere 3.8%.

The portfolio of securities available for sale (a small part thereof refers to the trading portfolio), up by

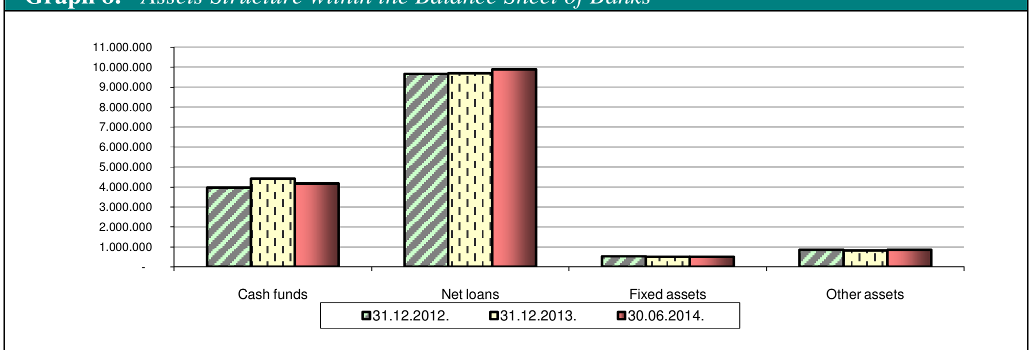
6.5% or KM 25 million, amounted to KM 407 million, and the securities held to maturity increased from KM 181 million to KM 184 million. Both portfolios include securities issued by the Government of the Federation of B&H[12] in the total amount of KM 241 million as of 30.06.2014, as well as securities issued by the Government of Republika Srpska in the amount of KM 25 million. Also, the trading portfolio includes shares issued by local companies totaling KM 3 million. The remaining portion of the securities portfolio amounts to app. KM 322 million and refers mostly to bonds of EU countries.

In the first half of 2014, the Government of the Federation of B&H issued seven tranches of treasury bills in the total amount of KM 130 million: one of the nominal value of KM 20 million in February 2014 (maturing in May 2014), two tranches in March 2014 in the amount of KM 20 million each (maturing in June 2014), two tranches in April in the amount of KM 15 million each (maturing in October 2014), one tranche in May in the amount of KM 20 million (maturing in November 2014), and one tranche in June in the amount of KM 20 million (maturing in June 2015). As of 30.06.2014, treasury bills amount to KM 70 million, i.e. their book value is KM 69.8 million. Also, the securities portfolios of banks also include bonds issued by the Government of the Federation of B&H (issued in 2012: the first issue in May 2012 in the amount of KM 80 million, maturing within 3 years, the second one in June and August in the total amount of KM 30 million, maturing within 5 years, and the third issue in September in the amount of KM 20 million, maturing within 2 years, as well as the fourth issue in December 2013 in the amount of KM 40 million, maturing within 3 years – with the total value of bonds purchased by banks being KM 17.5 million) of total nominal value of KM 140 million. The majority of the treasury bills and bonds with a book value of KM 175 million was classified in the portfolio of securities available for sale, while the rest in the amount of KM 35 million is classified in the portfolio of securities held to maturity.

When analysing the overall securities portfolio (KM 591 million) from the aspect of exposure by country, the largest share is that of B&H (45.6%) (46.4% at the end of 2013), followed by Romania (14.6%), Austria (11.8%), Belgium (9.4%), etc.

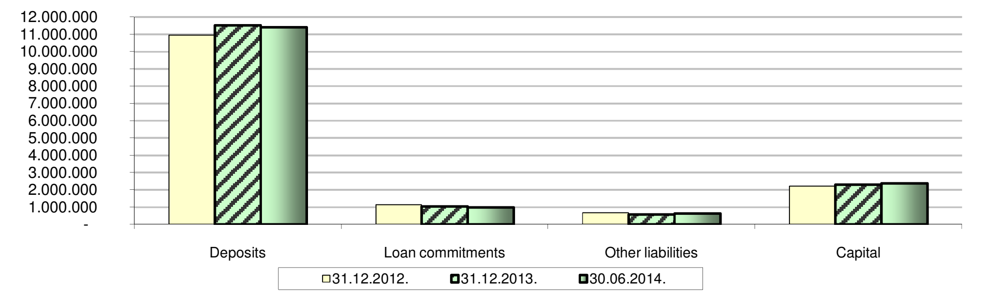
The graphs below show the structure of the key items of the banks' balance sheet.

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



[12] All types of securities issued by the Government of 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 11.4 billion and a 74.0% share). Following a further slight decrease of 4.3%, the share of loan obligations in the amount of KM 1.0 billion decreased from 6.7% to 6.4%, while the share of capital, which amounted to KM 2.4 billion as of 30.06.2014, increased from 15.0% to 15.4%.

The structure of assets, as well as the structure of sources of funding, saw minor changes related to two key assets items: increase in the loan share from 70.3% to 71.9% and decrease in cash funds from 28.6% to 27.1%.

- in KM 000-

Table 11: *Cash Funds of Banks*

CASH FUNDS	31.12.2012		31.12.2013		30.06.2014		INDEX	
	Amount	Share %	Amount	Share %	Amount	Share %	4/2	6/4
1	2	3	4	5	6	7	8	9
Cash	411 726	10.4	431 592	9.8	425 916	10.2	105	99
RR at the CB B&H	2 130 626	53.8	2 622 277	59.4	2 518 829	60.3	123	96
Accounts at deposit institutions in B&H	1 930	0.0	25 181	0.5	62 292	1.5	1305	247
Accounts at deposit institutions abroad	1 417 857	35.8	1 338 347	30.3	1 168 178	28.0	94	87
Cash in the process of collection	442	0.0	501	0.0	213	0.0	113	43
TOTAL	3 962 581	100.0	4 417 898	100.0	4 175 428	100.0	111	95

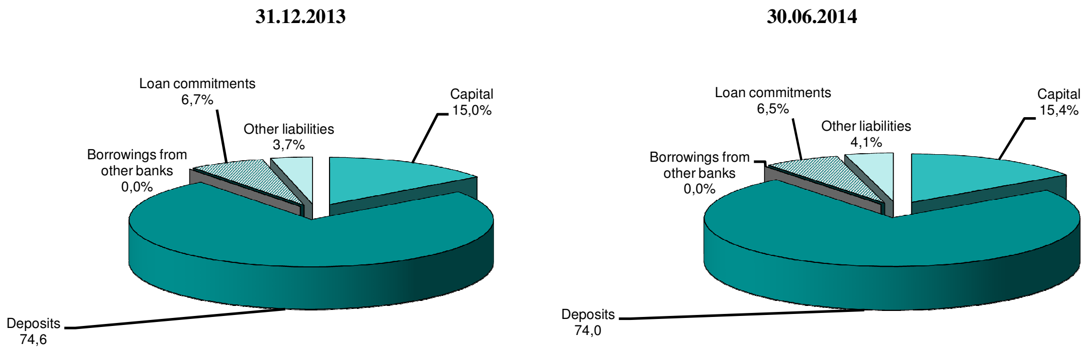
The two main changes related to cash funds are as follows: in the first half of 2014, the reserve account balance at the CBBH and the balances on the banks' accounts abroad recorded a decrease. The banks' cash funds in the CBBH reserves account fell by 4% or KM 103 million and amounted to KM 2.5 billion or 60.3% of total cash funds as of 30.06.2014 (59.4% at the end of 2013). The banks' funds in accounts of deposit institutions abroad recorded a decrease of 13% or KM 170 million and amounted to KM 1.2 billion or 28.0% of total cash funds (30.3% at the end of 2013). Following their decrease of 1% or KM 6 million, banks held cash funds in the amount of KM 426 million, which represents 10.2% of total cash funds, in vaults and treasuries as of 30.06.2014.

These trends prompted a change in the currency structure of cash funds: in the reporting period, the share of local currency increased from 66.4% to 69.0%, 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 30.06.2014 is provided in the graph below:

Graph 10: *Liabilities Structure of Banks*



During the reporting period, the share of deposits (74.0%), as the most significant source of funding of banks, fell by 0.6 percentage points, while the share of loan commitments, the second largest source of funding, fell by 0.2 percentage points (6.5%).
The decrease in the share of deposits is the result of their drop by 1% or KM 111 million in the first half of 2014. As of 30.06.2014, they amounted to KM 11.4 billion and are still the largest source of funding for banks in the Federation of B&H. it should be noted that, in January 2014, B&H received the VI tranche of funds based on the stand-by arrangement with the IMF in the amount of KM 61.7 million (B&H received app. KM 163 million in 2013 and KM 153 million in 2012).

The second-largest source of funding are loans in the amount of KM 1.0 billion, which banks received mostly by borrowing from foreign financial institutions. In the past 3 years, due to the effect of the financial and economic crisis, banks incurred significantly fewer loans abroad and, coupled with the payment of matured liabilities, reduced these sources of financing by over 50% (at the end of 2008, deposits amounted KM 2.18 billion). In 2012, the decrease amounted 13.5% or KM 178 million, in 2013, these sources dropped by 9% or KM 102 million, while in the first half of 2014, they dropped by 4.3% or KM 45 million. If subordinated loans in the amount of KM 167 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 7.5% in total sources of funding.

As of 30.06.2014, banks held the largest amount of liabilities towards the following creditors (6 out of a total of 33 creditors), accounting for 76% of total loan commitments: European Investment Bank (EIB), TC ZIRAAT BANKASI A.S. (Turkey), UniCredit Bank Austria AG, European Fund for Southeast Europe (EFSE), EBRD and the World Bank.

As of 30.06.2014, capital amounted to KM 2.4 billion, up by 3.1% or KM 72 million compared to the end of 2013. This primarily relates to the financial result (profit) recorded in the first half of 2014 as well as the recapitalisation in one bank (KM 29.3 million).

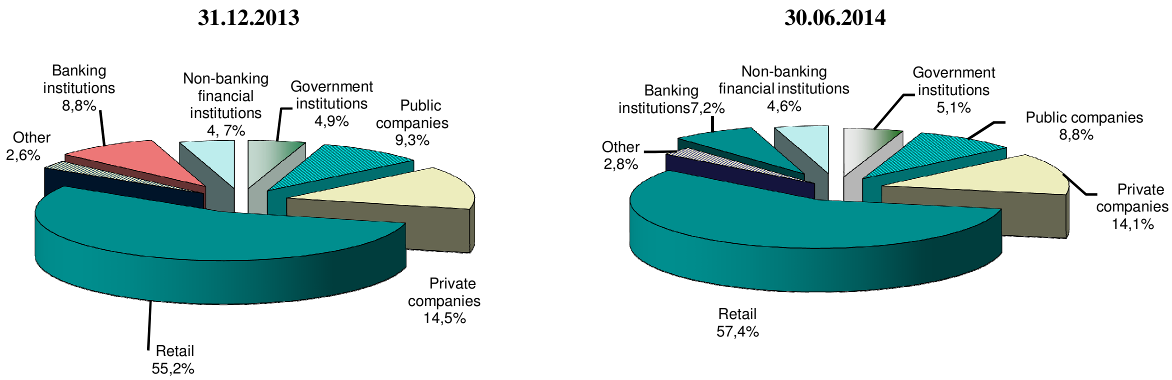
According to the information submitted by banks, out of the total deposit amount at the end of the reporting period, only 5.9% relates to deposits collected in organisational units of banks from the Federation of B&H, which are doing business in Republika Srpska and Brčko District.

- in KM 000-

Table 12: *Deposit Structure by Sector*[13]

SECTORS	31.12.2012		31.12.2013		30.06.2014		INDEX	
	Amount	Share %	Amount	Share %	Amount	Share %	4/2	6/4
1	2	3	4	5	6	7	8	9
Government institutions	682 313	6.2	565 533	4.9	575 882	5.1	83	102
Public companies	1 090 870	10.0	1 076 527	9.3	1 006 664	8.8	99	94
Private companies and enterprises	1 501 232	13.7	1 668 034	14.5	1 612 847	14.1	111	97
Banking institutions	981 562	9.0	1 012 274	8.8	815 501	7.2	103	81
Non-banking financial institutions	493 689	4.5	535 915	4.7	529 623	4.6	109	99
Retail	5 933 071	54.1	6 366 218	55.2	6 552 483	57.4	107	103
Other	278 264	2.5	299 348	2.6	319 639	2.8	108	107
TOTAL	10 961 001	100.0	11 523 849	100.0	11.412.639	100.0	105	99

Graph 11: *Deposit Structure by Sector*



In the first half of 2014, minor changes occurred in the deposit structure by sector and they are mostly the result of a decrease in deposits of banking institutions, private and public companies, as well as the increase in retail deposits.

Retail deposits displayed continuous growth over the past few years and they rose by 3% or KM 186 million in the first half 2014, while their share in total deposits rose from 55.2% to 57.4%, so that retail deposits are still the largest source of funding for banks. Analytical data indicates that the share of this sector's deposits is the largest in 15 out of 17 and it ranges from 33% to 88%.

The second largest source of funding (based on amount and share) are deposits of private companies. After their increase of 11% or KM 167 million in 2013, they fell by 3% or KM 55 million in the first half of 2014, while their share dropped to 14.1% (-0.4 percentage points) and they amounted to KM 1.6 billion.

Deposits of public companies recorded a decrease of 6% or KM 70 million and amounted to KM 1.0 billion or 8.8% of total deposits as of 30.06.2014.

From the end of 2007 until the third quarter of 2011, deposits of banking institutions were the second-largest source in the deposit potential of banks. The growth trend was maintained by mid-2009, when they reached their peak of KM 2.3 billion and a share of 21.4% of total deposits. After that, due to the

[13] 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).

effects of the crisis, the reduced volume of lending and high liquidity, parent groups withdrew their deposits, thus resulting in the reduced share. Deposits of this sector dropped over the past 4.5 years (from the end of 2009 to 30.06.2014) by app. 60% or KM 1.3 billion. Negative trends in previous years (related to these funds at sector level) are mostly a 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 half of 20¸14, deposits of banking institutions fell by a high 19% or KM 197 million, thus amounting to KM 816 million as of 30.06.2014. This resulted in their share in total deposits dropping from 8.8% to 7.1%. These funds are lower than loan commitments by KM 179 million, which are the second-largest source of funding in banks from the Federation of B&H, just after deposits. 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 app. KM 180 million or 24% of term deposits of the group mature by the end of 2014. Considering that the same reduction trend is present with respect to loan commitments, banks are once again facing the problem of maintaining their maturity adjustment, with this being caused by the unfavourable maturity of local deposit funds, due to which they are forced to obtain quality sources of funding in the period to come in order to uphold the trend of increase in approved loans.
It is worth noting that 93% or KM 760 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 five large banks (94%). 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 obligations and subordinated debts, the financial support of banks from the group is higher (with respect to 11 banks) and amounts to KM 1.15 billion as of 30.06.2014 (or 7.4% of total liabilities of the banking sector, which is lower compared to the end of 2013 (KM 1.3 billion or 8.6% of liabilities). In total deposits, the funds of banking groups hold a share of 6.7% (8.0% at the end of 2013), while loan commitments to the group account for 24.3% of total loan obligations (this share is down by 1.8%). Compared to the end of 2013, these funds dropped by 14.1% or KM 188 million, largely based on regular maturities (deposits fell by 17.6% or KM 163 million, loan commitments by 10.9% or KM 29 million, while subordinated loans rose by 3.0% or KM 4 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 deposit sources, while loan sources are reduced largely on the basis of regular repayments of matured liabilities. For reasons of unfavourable occurrences in the economies of the home countries of the owners of banks from the Federation of B&H, the problems these countries are facing and consequently, the problems of their financial systems and banking groups, as well as measures taken in Austria to strengthen and ensure the sustainability of the business models of large internationally active Austrian banks and thereby preserve the country's credit rating[14], 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 (from one month to one year) and serve the purpose of maintaining maturity adjustment within the prescribed limits, and therefore do not constitute a quality source of long-term funding.

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[14] In essence, these measures mean that the lending activity of subsidiaries of Austrian banks in the Central, Eastern and Southeastern Europe (CESEE) is conditioned by stronger and sustainable funding from local sources.

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

Deposits of other sectors saw slight changes in terms of both amount and share.

The currency structure of deposits as of 30.06.2014 has slightly changed: deposits in foreign currency (with a dominant share of EUR currency) in the amount of KM 5.9 billion increased their share from 51.9% to 51.6% and deposits in local currency amounted to KM 5.5 billion and hold a share of 48.4%.

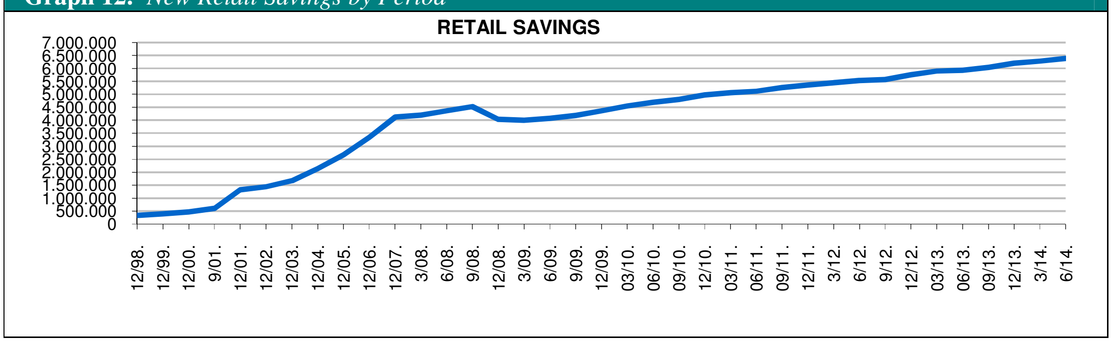
At the end of first half of 2014, the structure of deposits by domicile status of depositors changed slightly: resident funds amounted to KM 10.3 billion and had a share of 90.3% (+1.6%) while non-resident deposits amounted to KM 1.1 billion and represented 9.7% of total deposits. Resident deposits rose by 0.8% or KM 85 million, while non-resident deposits fell by 15.1% or KM 197 million. Over the past four 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. Non-resident deposits had the largest share of 22.1% and nominal amount of KM 2.31 billion at the end of 2008.

In 2014, savings deposits, as the most significant segment of the deposit and financial potential of banks, recorded an increase of 3.0% or KM 184 million and amounted to KM 6.4 billion as of 30.06.2014.

Table 13: *New Retail Savings by Period*

BANKS	AMOUNT (u 000 KM)			INDEX	
	31.12.2012	31.12.2013	30.06.2014	3/2	4/3
1	2	3	4	5	6
State-owned	58 050	65 179	65 475	112	100
Private	5 698 300	6 135 693	6 319 231	108	103
TOTAL	5 756 350	6 200 872	6 384 706	108	103

Graph 12: *New Retail Savings by Period*



The two largest banks hold 58% of savings, while nine banks hold individual shares of less than 2%, which amounts to 10.7% of total savings at system level.

Out of the total amount of savings, 38% refers to saving deposits in local currency and 62% to savings deposits in foreign currency.

Table 14: *Maturity Structure of Retail Savings Deposits by Period*								
BANKS	**I Z NO S (u 000 KM)**						**INDEX**	
	31.12.2012		**31.12.2013**		**30.06.2014**		**3/2**	**4/3**
1	2		3		4		5	6
Short-term savings deposits	2 656 934	46.2%	2 911 827	47.0%	2 966 975	46.5%	110	102
Long-term savings deposits	3 099 416	53.8%	3 289 063	53.0%	3 417 731	53.5%	106	104
TOTAL	5 756 350	100.0 %	6 200 890	100.0%	6 384 706	100.0%	108	103

Compared to the end of 2013, the maturity structure of savings deposits changed slightly through an increase in short-term deposits by 2% or KM 55 million, while long-term deposits rose by 4% or KM 129 million, thus resulting in a slightly higher share of long-term deposits from 53.0% to 53.5%.

Long standing continuous growth and positive trends in the savings segment of banks in the Federation of B&H are the result of, on 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 to KM 20 000 in 2008. After that, an initiative was started to increase the insured deposit level. Accordingly, on 01.04.2010, this level rose to KM 35 000. 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 present 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 30.06.2014, there was a total of 16 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). There is one bank that is not eligible for this program because it does not meet the criteria defined by the Deposit Insurance Agency of B&H (due to existing composite rating).

2.1.2. Capital – Strength and Adequacy

The capital[15] of banks in the Federation of B&H as of 30.06.2014 amounted to KM 2.3 billion.

-in KM 000-

Table 15: *Regulatory Capital*								
DESCRIPTION	**31.12.2012**		**31.12.2013**		**30.06.2014**		**INDEX**	
1	2		3		4		5 (3/2)	6 (4/3)
1.a.Core capital before reduction	1 913 841		2 155 188		2 120 463		113	98
1.1. Share capital – common and permanent non-cumulative shares	1 198 516		1 200 644		1 234 838		100	103
1.2. Issue premiums	136 485		136 485		136 485		100	100
1.3.Reserves and retained profit	578 840		818 059		749 140		141	92
1.b.Deductible items	191 304		294 629		195 501		154	66
1.1. Uncovered losses from previous years	120 740		112 610		144 924		93	129
1.2. Current year loss	17 818		140 445		9 362		788	7
1.3. Treasury shares	156		156		81		100	52
1.4. Intangible assets	52 590		41 418		41 134		79	99
1. Core capital (1a-1b)	**1 722 537**	**79%**	**1 860 559**	**80%**	**1 924 962**	**83%**	108	103
2. Supplementary capital	**467 100**	**21%**	**457 047**	**20%**	**390 870**	**17%**	98	86
2.1. Share capital – permanent preferred cumulative shares	3 090		3 091		3 091		100	100
2.2. General loan loss reserves	211 433		215 083		221 019		102	103
2.3. Amount of audited profit	67 243		71 984		0		107	N/a
2.4. Subordinated debt up to 50% of the core capital	120 264		165 473		165 344		138	100

[15] Regulatory capital is defined in Articles 8 and 9 of the Decision on Minimum Standards for Capital Management in Banks („Official Gazette of the Federation of B&H", No. 3/03, 18/03, 53/06, 55/07, 81/07, 6/08, 86/10, 70/11).

2.5. Permanent items	65 070		1 416		1 416		2	100
3. Capital (1 + 2)	**2 189 637**	**100%**	**2 317 606**	**100%**	**2 315 832**	**100%**	106	100
4. Deductible items from capital	**98 848**		**159 710**		**191 513**		162	120
4.1. Bank's shares in capital of other legal entities above 5% of core capital	3 043		2 844		2 909		93	102
4.2. Loan loss reserves shortfall at regulatory request	95 720		156 866		188 604		164	120
4.3. Other deductible items	85		0		0		N/a	N/a
5. Net Capital (3- 4)	**2 090 789**		**2 157 896**		**2 124 319**		103	98

In the first half of 2014, capital[16] remained at the same level, and the changes in core and supplementary capital affected the changes in the structure of the regulatory capital. Core capital increased by 3% or KM 64 million, while supplementary capital dropped by 14% or KM 66 million.

The core capital increase is mostly based on the inclusion (the transfer of one part of profit from supplementary to core capital) of profit earned in 2013. After the implementation of the legal procedure of adopting decisions by the banks' assemblies, the recorded profit in the amount of KM 138 million was distributed as follows: 99% or KM 136 million KM into core capital (retained profit and reserves), two banks distributed a part of the profit in the amount of 1.2 million to partly cover previous losses, while two banks made the decision to pay dividends (a total of KM 44 million). The increase in core capital was also influenced by the recapitalisation of two banks in the amount of KM 34 million.

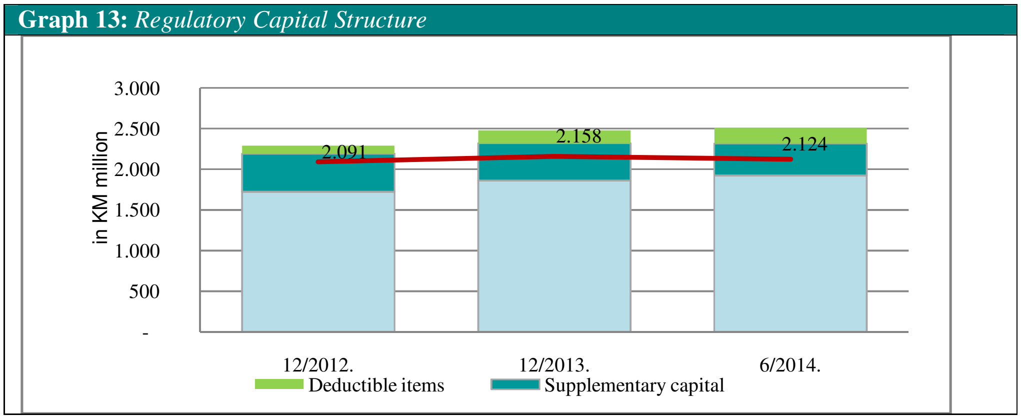
Deductible items (which decrease core capital) decreased by KM 99 million, as a result of the decrease on the basis of partial coverage of uncovered losses in three banks in the amount of KM 108 million (KM 107 million of which apply to one bank) and the increase on the basis of the current loss of KM 9 million.

Supplementary capital dropped by 14% or KM 66 million, and was mostly affected by the aforementioned transfer of audited profit to the core capital, while general loan loss reserves were increased by KM 6 million.

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[17] and loan loss reserves formed from profit). As of 30.06.14, this item amounted to KM 189 million, up by 20% or KM 32 million compared to the end of 2013 (this item was up by 64% or KM 61 million in 2013).

The graph below shows the regulatory capital structure.

Graph 13: *Regulatory Capital Structure*



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

[17] Banks declare required regulatory reserves when the value adjustment (according to IAS) is below calculated regulatory reserves, as determined at the level of the individual debtor. This methodology is in application since 30.06.2012.

As a result of the aforementioned changes, especially due to the negative effect of the increase of the shortfall of loan loss reserves (20% or KM 32 million), net capital fell by 2% or KM 34 million and amounted to KM 2.1 billion as of 30.06.2014.

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

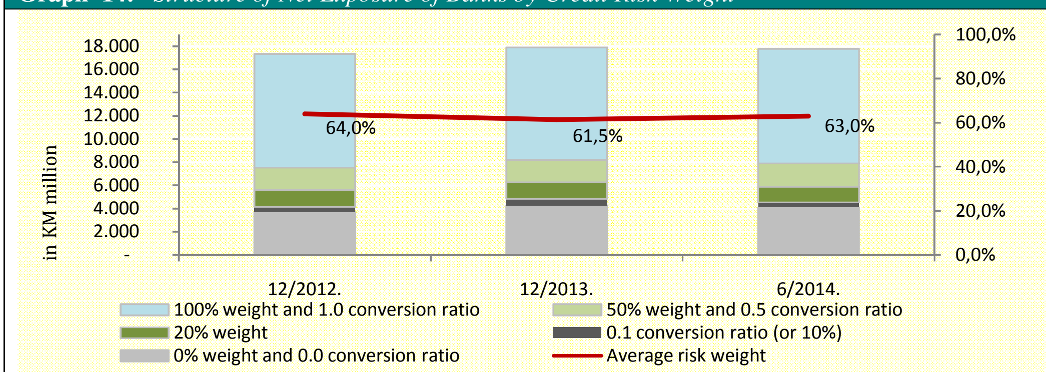
The table below provides a structure of the net exposure of banks by credit risk weight, i.e. conversion ratio for off-balance sheet items.

-in KM 000-

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

DESCRIPTION	31.12.2012.	31.12.2013.	30.06.2014.	INDEX	
1	2	3	4	5 (3/2)	6 (4/3)
TOTAL EXPOSURE (1+2):	**17 310 579**	**17 893 904**	**17 751 800**	103	99
1 Balance sheet assets	14 568 957	14 969 445	14 913 490	103	100
2. Off-balance sheet items	2 741 622	2 924 459	2 838 310	107	97
DISTRIBUTION BY RISK WEIGHT AND CONVERSION RATIO					
0% weight	3 647 306	4 198 260	4 068 153	115	97
20% weight	1 460 689	1 424 069	1 341 781	97	94
50% weight	53 155	33 110	21 978	62	66
100% weight	9 407 807	9 314 006	9 481 578	99	102
0.0 conversion ratio	51 131	86 947	53 515	170	62
0.1 conversion ratio	449 627	550 966	414 952	123	75
0.5 conversion ratio	1 867 703	1 916 076	1 993 212	103	104
1.0 conversion ratio	373 161	370 470	376 631	99	102
RISK WEIGHTED ASSETS AND LOAN EQUIVALENTS	**11 078 498**	**10 998 977**	**11 175 653**	**99**	**102**
Average risk weight	**64.0%**	**61.5%**	**63.0%**	**96**	**102**

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



In the first half of 2014, total net exposure of banks (before being weighted) is lower by 1% or KM 142 million. This was influenced more by the decrease in off-balance sheet items (mostly items weighted with 0 and 0.1 conversion ratios) than balance-sheet items (mostly item weighted with 20% risk weight, receivables from banks from countries belonging to zone A). Although asset items being weighted with 0%, 20% and 50% have decreased, asset items being weighted with 100% have increased slightly (2%), which has caused risk weighted assets and loan equivalents to increase (2%) along with the average risk weight, which rose from 61.5% na 63%.

The same direction was seen with respect to the weighted operational risk (WOR), which also rose slightly and amounts to KM 982 million. All of this has resulted in a slight increase in total risk weights (1.5%).

As of 30.06.2014, the share of risk weighted assets exposed to credit risk amounted to 92% and to operational risk 8%.

The banks' capitalisation rate, expressed as a ratio between capital and assets, amounted 13.9% as of 30.06.2014, which is the same as at the end of 2013.

One of the key indicators of capital strength and adequacy[18] 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 17.5% as of 30.06.2014, down by 0.5% compared to the end of 2013.

Although operations of the banking sector have been 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% and above 17% in the past three years. The reason for this is, on the one hand, the credit growth stagnation and decrease of overall weighted risks, and, on the otherhand , the fact the banks have retained the largest share of profit from previous years within their capital and several banks have improved their capitalisation rate by means of additional capital injections. However, problems related to the increase in 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 conditioned by continued negative trends regarding asset quality and the worsening of and increase in non-collectable loans. 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 the first half of 2014, net non-performing assets reached an amount of KM 508 million and the ratio was 26.4%. Also, according to existing regulations, banks do not calculate the capital requirement for market risks, due to which the capital adequacy rate is higher.

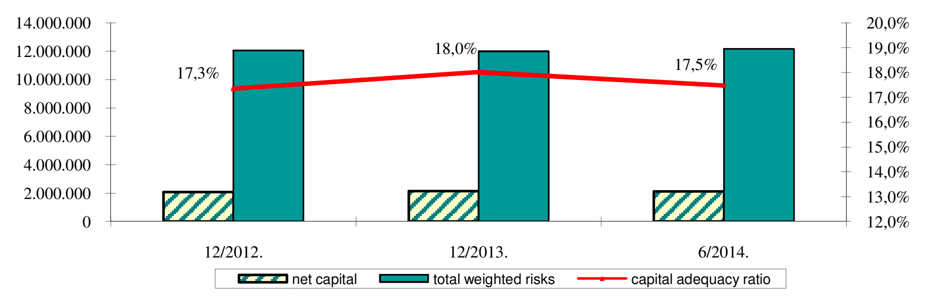
- KM 000 -

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

DESCRIPTION	31.12.2012	31.12.2013	30.06.2014	INDEX	
1	2	3	4	5(3/2)	6(4/3)
1. NET CAPITAL	2 090 789	2 157 896	2 124 319	103	98
2. RISK WEIGHTED ASSETS AND LOAN EQUIVALENTS	11 078 498	10 998 977	11 175 653	99	102
3. WOR (WEIGHTED OPERATIONAL RISK)	974 201	981 318	982 260	101	100
4. TOTAL WEIGHTED RISKS (2+3)	12 052 699	11 980 295	12 157 913	99	101
5. NET CAPITAL RATE (CAPITAL ADEQUACY) (1/ 4)	17.3%	18.0%	17.5%	104	97

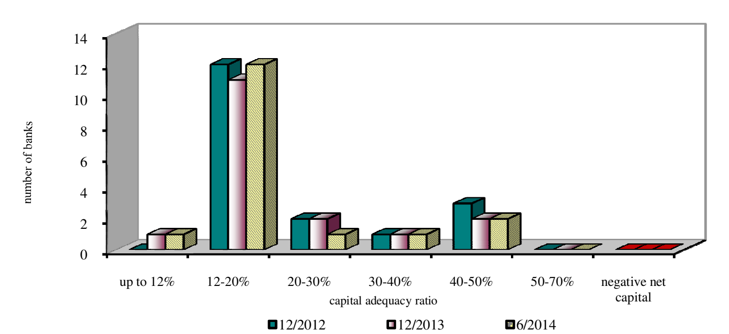
18 The legally defined minimum capital adequacy rate is 12%.

Graph 15: *Net Capital, Risk Weighted Assets and Capital Adequacy Rate*



The capital adequacy rate of the banking system as of 30.06.2014 was 17.5%, 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 17 banks in the Federation of B&H as of 30.06.2014, 16 banks had capital adequacy ratios that were above the legal minimum of 12%, while one bank had a ratio that was below the legal minimum. According to analytical data, 12 banks had a capital adequacy ratio below the one at the end of 2013 (ranging from 0.3 to 5.4 percentage points), 4 banks had improved this ratio and 1 bank had the same ratio as at the end of 2013.

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

- 1 bank had a ratio below 12% (8,2%),
- 6 banks had a ratio between 13.1% and 15.1%,
- 6 banks had a ratio between 16.4% and 19.5%,
- 1 bank had a ratio of 20,4%,
- 3 banks had a ratio between 35.3% and 47.3%.

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 level and profile of the existing and potential exposure to all risks inherent to banking 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 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. 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	31.12.2012	31.12.2013	30.06.2014	INDEX	
1	2	3	4	5(3/2	6(4/3)
1. Risk-bearing assets[19]	13 286 676	13 517 944	13 918 233	102	103
2. Calculated regulatory reserves for loan losses	1 370 669	1 504 174	1 587 669	110	106
3. Value adjustment and reserves for off-balance sheet items	1 092 535	1 255 162	1 295 691	115	103
4. Required regulatory reserved formed from profit for assessed losses	411 077	411 515	463 672	100	113
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 losses	111 565	156 866	188 603	141	120
7. Non-risk-bearing items	5 579 911	6 145 092	5 674 627	110	92
8. TOTAL ASSETS (1+7)	18 866 587	19 663 036	19 592 860	104	100

Total assets with off-balance sheet items (assets) [20] of banks in the Federation of B&H amounted to KM 19.6 billion as of 30.06.2014 and at the same level as at the end of 2013. Risk-bearing assets amount to KM 13.9 billion and are up by 3% or KM 400 million.

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[19] Does not include amount of facilities and contingent liabilities of KM 246 million that is secured with a cash deposit.

[20] 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).

Non-risk bearing items amount to KM 5.7 billion or 29% of total assets with off-balance sheet items, thus being down by 8% or KM 470 million compared to the end of 2013.

Total calculated loan loss reserves based on regulatory requirements amount to KM 1.6 billion and formed value adjustments for balance sheet assets and provisions for losses under off-balance sheet items amount to KM 1.3 billion. Required regulatory reserves[21] amount to KM 464 million and are up by 13% or KM 52 million. Formed regulatory reserves from profit amount to KM 316 million and are at the same level as a result of changes in regulations, i.e. the shortfall of loan loss reservess being recorded at the end of the business year (starting from 31.12.2012) is not covered by profit, but still represents a deductible item from the capital and affects the calculation of the capital adequacy ratio. The shortfall of regulatory reserves[22] as of 30.06.2014 amounts to KM 189 million, with a growth rate of 20% or KM 32 million compared to the end of 2013, which is the result of the continuous deterioration of the loan portfolio quality.

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

DESCRIPTION	31.12.2012		31.12.2013		30.06.2014		INDEX	
	Amount	Struct. %	Amount	Struct.%	Amount	Struct.%		
1.	2	3	4	5	6	7	8 (4/2)	9 (6/4)
Loans	9 347 370	85.2	9 396 444	84.3	9 513 147[23]	82.9	101	101
Interest	86 650	0.8	81 456	0.7	82 427	0.7	94	101
Past due receivables	1 049 891	9.5	1 144 042	10.3	1 279 959	11.2	109	112
Receivables based on paid guarantees	24 360	0.2	31 783	0.3	33 399	0.3	130	105
Other facilities	172 479	1.6	201 786	1.8	222 200	1.9	117	110
Other assets	292 440	2.7	294 623	2.6	350 144	3.0	101	119
1.RISK-BEARING BALANCE SHEET ASSETS	10 973 190	100.0	11 150 134	100.0	11 481 276	100.0	102	103
2. NON-RISK-BEARING BALANCE SHEET ASSETS	5 084 000		5 523 506		5 207 091		109	94
3.GROSS BALANCE SHEET ASSETS (1+2)	16 057 190		16 673 640		16 688 367		104	100
4.RISK-BEARING OFF-BS ITEMS	2 313 486		2 367 810		2 436 957		102	103
5.NON-RISK-BEARING OFF-BS ITEMS	495 911		621 586		467 536		125	75
6.TOTAL OFF-BS ITEMS (4+5)	2 809 397		2 989 396		2 904 493		106	97
7.RISK-BEARING ASSETS WITH OFF-BS ITEMS (1+4)	13 286 676		13 517 944		13 918 233		102	103
8. NON-RISK-BEARING ITEMS (2+5)	5 579 911		6 145 092		5 674 627		110	92
9. ASSETS WITH OFF-BS ITEMS (3+6)	18 866 587		19 663 036		19 592 860		104	100

Gross balance sheet assets[24] amount to KM 16.7 billion and are at the same level as at the end of 2013, while risk-bearing balance sheet assets amount to KM 11.5 billion or 69% of gross balance sheet assets (thus being up by 3% or KM 331 million compared to the end of 2013). Non-risk bearing balance sheet assets amount to KM 5.2 billion and are down by 6% or KM 316 million. Off-balance sheet risk-bearing items amount to KM 2.4 billion and are up by 3% or KM 69 million, while non-risk bearing items amount to KM 467 million and are down by 25% or KM 154 million compared to the end of 2013.

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 six months of

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

22 Shortfall of regulatory reserves represents a positive difference between required and formed loan loss reserves.

23 This does not include the loan amount of KM 194 million covered by a cash deposit (included in non-risk bearing assets of the balance sheet).

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

2014, banks recorded a moderate loan increase of 2% or KM 238 million. As of 30.06.2014, loans amounted to KM 11.1 billion, with their share in assets rising by 1.6% and amounting to 71.9%.

However, based on analytical data, it can be concluded that this credit growth was largely generated by an increase of past due, uncollected receivables (default receivables). In the first half of 2014, the growth rate was a high 11% or KM 130 million, same as for all of 2013 (overall past due, uncollected receivables amounted to KM 1.1 billion, while they rose by 11% or KM 110 million) and amounted to KM 1.3 billion as of 30.06.2014. This results in the real credit growth in six months of 2014 amounting to 1% (app. 0.7% in 2013).

In the first half of 2014, a total of KM 3.6 billion of new loans was approved, up by 12% or KM 369 million compared to the same period of the previous year. Out of the total loans approved, 67% relate to the corporate segment and 30% to the retail segment (as of 31.12.2013: 67% corporate segment, 28% retail segment). The maturity structure of newly approved loans: 47% long-term loans, 53% short-term loans (as of 31.12.2013: 44% long-term loans and 56% short-term loans.

The three largest banks in the Federation of B&H have an aggregate amount of approved loans of KM 6.1 billion, thus holding a share of 55% 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	31.12.2012		31.12.2013		30.06.2014		INDEX	
	Amount	Share %	Amount	Share %	Amount	Share %		
1	2	3	4	5	6	7	8(4/2)	9(6/4)
Government institutions	132 525	1.2	142 010	1.3	151 574	1.4	107	107
Public companies	251 233	2.4	259 769	2.4	293 222	2.6	103	113
Private companies and enterprises	5 141 359	48.2	5 202 269	47.9	5 258 866	47.4	101	101
Banking institutions	11 177	0.1	6 671	0.1	5 835	0.1	60	87
Non-banking financial institutions	41 661	0.4	37 791	0.3	35 759	0.3	91	95
Retail	5 076 679	47.6	5 194 971	47.9	5 336 818	48.1	102	103
Other	11 490	0.1	8 919	0.1	8 506	0.1	78	95
TOTAL	10 666 124	100.0	10 852 400	100.0	11 090 580	100.0	102	102

In the first half of 2014, loan structure by industry sector changed slightly compared to the end of 2013. Retail loans and loans to private companies amount to KM 5.3 billion (at the end of 2013: KM 5.2 billion). Retail loans are up by 3% or KM 142 million, while loans to private companies rose by 1% or KM 57 million. Retail loans recorded an increase in their share from 47.9% to 48.1%, while the share of private company loans dropped from 47.9% to 47.4%.

According to information submitted by the banks (as of 30.06.2014) regarding the retail loan structure by purpose, consumer loans[25] hold a share of 75%, followed by housing loans with 21%, while the remaining 4% refer to loans to small crafts, small businesses and agriculture (at the end of 2013: 75% consumer loans, 22% housing loans, and 3% small crafts, small businesses and agriculture).

The three largest banks in the system have approved 63% of retail loans and 47% of private company loans (31.12.2013: 63% retail, 48% private companies).

[25] Including cards business.

The currency structure of loans: the largest share of 65% or KM 7 billion refers to currency clause loans (EUR: KM 7 billion or 97%, CHF: KM 230 million or 3%), followed by local currency loans with a share of 34% or KM 3.8 billion, while the smallest share of just 1% or KM 87 million refers to foreign currency loans (almost the entire amount thereof refers to EUR: KM 79 million or 90%). The total amount of loans with a currency clause in CHF of KM 230 million amounts to 2.1% of the total loan portfolio and refers almost entirely to one bank in the banking system.

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	31.12.2012.			31.12.2013.			30.06.2014.			INDEX	
	Classified assets	Share %	GCR PLL	Classified assets	Share %	GCR PLL	Classified assets	Share %	GCR PLL		
1	2	3	4	5	6	7	8	9	10	11(5/2)	12(8/5)
A	10 571 555	79.6	211 433	10 754 079	79.6	215 083	11 051 072	79.4	221 019	102	103
B	1 227 301	9.3	108 313	1 094 361	8.1	93 547	1 086 040	7.8	93 404	89	99
C	334 226	2.5	87 874	356 646	2.6	90 541	406 134	2.9	98 920	107	114
D	443 500	3.3	252 970	502 803	3.7	295 224	482 399	3.5	282 159	113	96
E	710 094	5.3	710 079	810 055	6.0	809 779	892 588	6.4	892 167	114	110
Risk-bearing assets (A-E)	13 286 676	100.0	1 370 669	13 517 944	100.0	1.504.174	13 918 233	100.0	1 587 669	102	103
Classified (B-E)	2 715 121	20.4	1 159 236	2 763 865	20.4	1.289.091	2 867 161	20.6	1 366 650	102	104
Non-performing (C-E)	1 487 820	11.2	1 050 923	1 669 504	12.4	1.195.544	1 781 121	12.8	1 273 246	112	107
Non-risk-bearing assets[26]	5 579 911			6 145 092			5 674 627			110	92
TOTAL (risk-bearing and non-risk-bearing)	18 866 587			19 663 036			19 592 860			104	100

The first indicator and a warning sign of potential problems with loan repayment is the growth of past due receivables and their share in total loans. In the first half of 2014, past due receivables had a relatively high increase of 12% or KM 137 million (in 2013: 9% or KM 102 million) and their share rose by 1 percentage point, i.e. to 11.8%.

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 have deteriorated compared to the end of 2013. In some banks, these indicators showed slight oscillations (upgrade or downgrade), i.e. there were eight banks with ratios of the share of both classified assets and non-performing assets (compared to risk-bearing assets) below the level of the banking sector.

As of 30.06.2014, classified assets amounted to KM 2.9 billion and non-performing assets to KM 1.8 billion.

Classified assets (B-E) went up by 4% or KM 103 million and non-performing assets (C-E) went up by 7% or KM 112 million (i.e. in 2013, it went up by 12% or KM 182 million), half of which relates

[26] 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).

to one large bank in the system. Category B is down by 1% or KM 8 million (in 2013: down by 11% or KM 133 million).

The ratio expressed through the share of classified assets in risk-bearing assets is 20.6%, which is an increase of 0.2% compared to the end of 2013.

The most significant indicator of asset quality is the ratio between non-performing assets and risk-bearing assets, which rose by 0.4 percentage points compared to the end of the previous year and now amounts to 12.8% (in 2013 this ratio rose by 1.2 percentage points) as a result of the increase in non-performing assets by KM 112 million. However, this should be taken with a grain of salt due to the share of category B being 7.8% (end of 2013: 8.1%) 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.

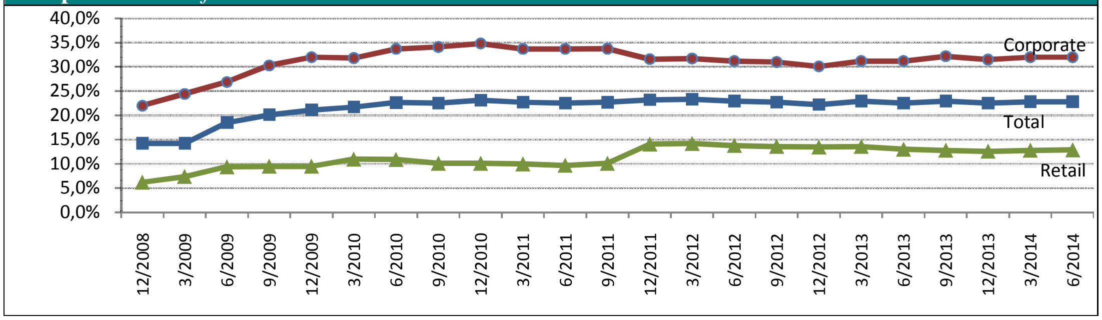
Sector-level data analysis is based on loan quality indicators for two key sectors: corporate and retail. The two aforementioned indicators for these sectors show major deviation and point to a higher exposure to credit risk and consequently to potential loan losses regarding the corporate segment.

Table 22: *Classification of Corporate and Retail Loans*

Classification category	31.12.2013.						30.06.2014.						INDEX
	Retail	Share %	Corporate	Učešće %	TOTAL Amount	TOTAL Share	Retail	Share %	Corpo-rate	Share %	TOTAL Amount	TOTAL Share	
1	2	3	4	5	6 (2+4)	7	8	9	10	11	12 (8+10)	13	14(12/6)
A	4 538 704	87.4	3 874 012	68.5	8 412 716	77.5	4 649 419	87.1	3 912 547	68.0	8 561 966	77.2	102
B	135 873	2.6	717 004	12.7	852 877	7.9	158 124	3.0	680 567	11.8	838 691	7.6	98
C	70 012	1.3	272 940	4.8	342 952	3.2	68 615	1.3	320 225	5.6	388 840	3.5	113
D	128 351	2.5	361 163	6.4	489 514	4.5	92 783	1.7	378 035	6.6	470 818	4.2	96
E	322 031	6.2	432 310	7.6	754 341	6.9	367 876	6.9	462 389	8.0	830 265	7.5	110
TOTAL	5 194 971	100.0	5 657 429	100.0	10 852 400	100.00	5 336 817	100.0	5 753 763	100.0	11 090 580	100.00	102
Class. loans B-E	656 267	12.6	1 783 417	31.5	2 439 684	22.5	687 398	12.9	1 841 216	32.0	2 528 614	22.8	104
Non-perf. loans C-E	520 394	10.0	1 066 413	18.8	1 586 807	14.6	529 274	9.9	1 160 649	20.2	1 689 923	15.2	107
		47.9		52.1		100.0		48.1		51.9		100.0	
Individual sector's share in classified loans, non-performing loans and category B:													
Categories B-E		26.9		73.1		100.0		27.2		72.8		100.0	
Non-performing C-E		32.8		67.2		100.0		31.3		68.7		100.0	
Category B		15.9		84.1		100.0		18.9		81.1		100.0	

After the first quarter, when loan quality indicators remained almost the same as at the end of 2013, non-performing loans went up again in the second quarter, and loan quality indicators deteriorated compared to the end of the previous year. At the end of the first half of 2014, the share of non-performing loans, following an increase of 0.6 percentage points, amounted to 15.2% (in 2013, the share went up by 1.4 percentage points) as a result of the increase in total non-performing loans by 7% or KM 103 million, with corporate loans increasing by 9% or KM 94 million, and retail loans by 2% or KM 9 million (in 2013, total non-performing loans rose by 13% or KM 180 million, with corporate loans being up by 22.3% or KM 194 million, and retail loans being down by 2.7% or KM 14 million). The share of classified loans increased to 22.8%, i.e. by 0.3. percentage points.

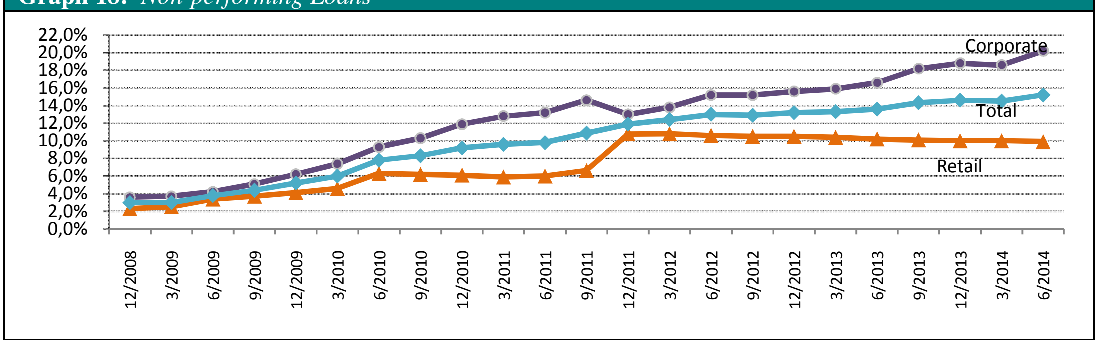
Graph 17: *Classified Loans*



Out of the total approved corporate loans in the amount of KM 5.7 billion as of 30.06.2014, there was an alarmingly high 32% or KM 1.8 billion of loans classified within categories B to E, which is an increase of 0.5 percentage points compared to the end of 2013 (in 2013, this share went up by 1.4 percentage points). This indicator is much better for the retail segment. Out of the total approved retail loans in the amount of KM 5.3 billion, there were 12.9% or KM 687 million of loans classified in the aforementioned categories (at the end of 2013: 12.6%; at the end of 2012: 13.5%), which is also high.

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 69% and retail loans a share of 31% (at the end of 2013: 67% corporate loans, 33% retail loans). In the first half of 2014, the share of non-performing loans in the corporate segment increased as a result of the aforementioned increase of 9%, while retail non-performing loans remained the same. Out of total approved corporate loans, non-performing loans hold a share of 20.2% or KM 1.2 billion, which is up by 1.4% compared to the end of 2013 (in 2013, this share rose by 3.2 percentage points). This increase rate in the retail segment amounts to KM 529 million, with almost the same share of 9.9% as at the end of 2013 (in 2013, the share dropped by 0.5%).

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	31.12.2013		30.06.2014		INDEX
	Total loans	Non-performing loans	Total loans	Non-performing loans	

	Amount	Share %	Amount	Share %	Amount	Share %	Amount	Share %		
1	2	3	4	5 (4/2)	6	7	8	9 (8/6)	10 (6/2)	11(8/4)
1. Corporate loans for:										
Agriculture (AGR)	112 695	1.0	30 608	27.2	114 819	1.0	29 678	25.8	102	97
Production (IND)	1 547 431	14.3	333 666	21.6	1 550 812	14.0	372 024	24.0	100	111
Construction (CON)	394 706	3.6	121 971	30.9	413 827	3.7	124 892	30.2	105	102
Trade (TRD)	2 298 260	21.2	392 161	17.1	2 366 600	21.4	430 519	18.2	103	110
Catering (HTR)	162 102	1.5	29 970	18.5	153 650	1.4	28 974	18.9	95	97
Other[27]	1 142 235	10.5	158 037	13.8	1 154 055	10.4	174 562	15.1	101	110
TOTAL 1.	5 657 429	52.1	1 066 413	18.8	5 753 763	51.9	1 160 649	20.2	102	109
2. Retail loans for:										
General consumption	3 906 142	36.0	310 450	7.9	4 072 673	36.7	316 342	7.8	104	102
Housing	1 148 230	10.6	170 282	14.8	1 124 009	10.1	173 085	15.4	98	102
Business activities (small business owners)	140 599	1.3	39 662	28.2	140 135	1.3	39 847	28.4	100	100
TOTAL 2.	5 194 971	47.9	520 394	10.0	5 336 817	48.1	529 274	9.9	103	102
TOTAL (1. +2.)	**10 852 400**	**100.0**	**1 586 807**	**14.6**	**11 090 580**	**100.0**	**1 689 923**	**15.2**	**102**	**106**

The largest share in total corporate loans refers to the trade sector (21.4%) and the production sector (14.0%), while the retail segment is dominated by general consumption loans (36.7%) and housing loans (10.1%), with these shares being almost the same as at the end of the previous year.

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 highest share of non-performing loans in the amount of 30.2% is held by the construction sector, which is down by 0.7 percentage points (in 2013, it rose by 5 percentage points), while its share in total loans stands at a mere 3.7%. In the first half of 2014, this sector recorded a slight increase in non-performing loans of 2% or KM 3 million. Also, agricultural sector, despite the lowest share of 1%, has a high share of non-performing loans in the amount of 25.8% (12/13: 27.2%), with there being a slight drop of 3% in non-performing loans in the first half of 2014.

However, the focus is on the two sectors with the highest share in total loans – the trade sector (21%) and the production sector (14%). In the first half of 2014, especially in the second quarter, there was a relatively significant increase in non-performing loans in both sectors: by 11% or KM 38 million in the production sector, with the share increasing from 21.6% to 24% (in 2013, the increase amounted to a high 37% or KM 90 million, and the share amounted to 21.6%, up by 5.7 percentage points); in the trade sector, non-performing loans recorded an increase in the amount of 10% or KM 38 million, while the share amounted to 18.2%, up by 1.1 percentage point (in 2013, a high increase of 27% or KM 82 million was recorded and the share rose from 13.3% to 17.1%).

The retail sector displays no major changes, its indicators are approximately the same as at the end of the previous year. The lowest indicator of the non-performing loans share in the amount of 28.4% (at the end of 2013: 28.2%) refers to loans to small business owners whose share in total loans is a low 1.3%. A relatively high share of non-performing loans in the amount of 15.4% refers to housing loans (at the end of 2013: 14.8%), while consumer loans (with the highest share of 36.7% in total loans) hold a lower share of 7.8% (at the end of 2013: 7.9%).

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,

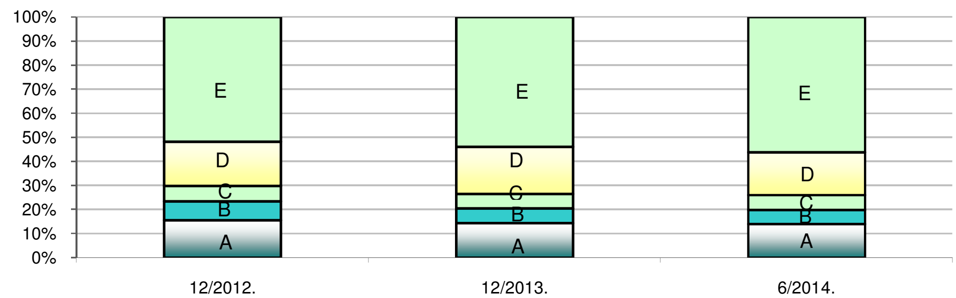
[27] This includes the following sectors: traffic, warehouse and communications (TRC); financial mediation (FIN); real estate, renting and business services (RER); public administration and defence, mandatory social insurance (GOV) and other.

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	
	31.12.2012		31.12.2013		30.06.2014			
1	2	3	4	5	6	7	8 (4/2)	9 (6/4)
A	211 433	15.4	215 083	14.3	221 019	13.9	102	103
B	108 313	7.9	93 547	6.2	93 404	5.9	86	100
C	87 874	6.4	90 541	6.0	98 920	6.2	103	109
D	252 970	18.5	295 224	19.6	282 159	17.8	117	96
E	710 079	51.8	809 779	53.9	892 167	56.2	114	110
TOTAL	1 370 669	100.0	1 504 174	100.0	1 587 669	100.0	110	106

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 2013, the reserves for general credit risk (category A) and potential loan losses went up by 6% or KM 83 million and stand at KM 1.6 billion. The reserves for general credit risk are up by 3% or KM 6 million and amount to KM 221 million, while the reserves for potential loan losses went up by 6% or KM 78 million. The reserves for category B remained the same and amount to KM 93 million. Due to the increase in non-performing assets by 7% or KM 112 million, the reserves for non-performing assets are up by 6% or KM 78 million, i.e. amount to KM 1.3 billion. The largest relative and nominal growth of 10% or KM 82 million refers to reserves for category E, while reserves for category C are up by 9% or KM 8 million, while the reserves for category D are down by 4% or KM 13 million. This trend of loan loss reserves points to a constant deterioration of the loan portfolio, which is the result of further effects of the economic crisis on the real sector.

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 9.8% and is higher by 0.3% compared to the end of 2013.

As of 30.06.2014, banks had an average calculated reserves in the amount of 8.6% for category B, 24.4% for category C, 58.5% for category D and 100%for category E (at the end of 2013: 8.5% for B, 25.4% for C, 58.7% for D and 100% for E).[28]

[28] 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%.

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) a 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 000 KM) AND SHARE (u%)				INDEX
	31.12.2013		30.06.2014		
	Amount	Share	Amount	Share	
1	2	3	4	5	6 (4/2)
1. RISK-BEARING ASSETS (a+b)	**13 517 944**	**100.0%**	**13 918 233**	**100,0%**	103
a) Default items	**1 886 251**	14.0%	**1 966 435**	14.1%	104
a.1. BS-items in default	1 863 530		1 946 079		104
a.2. off-BS items in default	22 721		20 356		90
b) Performing assets	**11 631 693**	86.0%	**11 951 798**	85.9%	103
1.1 TOTAL VALUE ADJUSTMENTS FOR RISK-BEARING ASSETS (a+b)	**1 255 162**	**100.0%**	**1 295 691**	**100.0%**	103
a) Value adjustments for default	**1 110 375**	88.5%	**1 152 809**	89.0%	104
a.1. Value adjustments for BS items in default	1 105 059		1 146 264		104
a.2. Reserves for off-BS items in default	5 316		6 545		123
b) Value adjustments for performing assets (IBNR[29])	144 787	11.5%	142 882	11.0%	99
2. TOTAL LOANS (a+b)	**10 852 400**	**100.0%**	**11 090 580**	**100.0%**	102
a) Defaulted loans (non-performing loans)	1 799 777	16.6%	1 882 845	17.0%	105
b) Performing loans	9 052 623	83.4%	9 207 735	83.0%	102
2.1. VALUE ADJUSTMENT FOR LOANS (a+b)	**1 165 928**	**100.0%**	**1 202 319**	**100.0%**	103
a) Value adjustments for defaulted loans	1 052 412	90.3%	1 092 139	90.8%	104
b) Value adjustments for performing loans (IBNR loans)	113 516	9.7%	110 180	9.2%	97
Coverage rate of default items	**58.9%**		**58.6%**		
Coverage rate of performing assets	**1.2%**		**1.2%**		
Coverage rate of risk-bearing assets with total value adjustments	**9.3%**		**9.3%**		

In the first half of 2014, default loans rose by 5% or KM 83 million (in 2013: up by 9% or KM 155 million). For comparison purposes, non-performing loans rose by 6% or KM 103 million compared to the end of 2013. The share of default loans in total loans increased by 0.4 percentage points and amounts to 17% and the share of non-performing loans amounts to 15.2%. The share of all default items in total risk-bearing assets is 14.1%, which is the same as at the end of 2013.

The coverage rate of default items with value adjustments fell from 58.9% to 58.6%, while the coverage rate of non-performing assets with loan loss reserves is approximately the same (71.5%). The coverage rate of performing assets remains the same and amounts to 1.2%, along with the coverage rate of risk-bearing assets with total value adjustments (9.3%). 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) improved slightly and amounts to 11.4% (12/13: 11.1%).

On the basis of the aforementioned, it can be concluded that the economic crisis and conditions in the real sector still negatively affect the banks' loan portfolio, past due receivables of debtors, primarily legal entities, which results in the increase in non-performing loans. However, it should be noted that the negative effects the natural disasters from May 2014 had on natural persons and legal entities on territories affected by the flood in B&H, i.e. the effect of the banks' debtors' meeting loan

[29] IBNR (identified but not reported) – latent losses.

commitments, has yet to be recorded in the reports submitted to banks as of 30.06.2014, due to the short period of time since the disasters' occurrence. 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[30].

The aforementioned Decision determined that the Bank can approve the following, either individually or in combination:

- *a moratorium on loan commitments*, i.e. the deferral of the payment of loan commitments with a maximum duration of 12 months, the deadline being 30.09.2015, and at an interest rate that can amount to at most 50% of the previously agreed on interest rate, and
- *a restructuring of loan commitments* which can include an extension of the deadline for principal and/or interest repayment, a lowering of the interest rate, a write-off of a portion of receivables, the capitalisation of interest, the approval of new loan funds in order to repair damages or continue the business process or other significant changes to facilitate the client's position.

The Agency has also prescribed special reporting tables, with the banks' first quarterly data being submitted as of 30.09.2014.

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), so that the loan repayment fell on the guarantors. 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 30.06.2014, there was a total of 1 931 guarantors that repaid KM 12.2 million of the total approved loan amount of KM 64 million (1 697 loan accounts), which is the same as the amount repaid by guarantors as of 31.12.2013 (KM 12.2 million repaid by 2 032 guarantors, while the amount of approved loans was KM 66 million and encompassed 1 785 loan accounts). The remaining debt amounts to KM 42 million (31.12.2013: KM 43 million).

Based on the aforementioned information, it can be concluded that the loan amount repaid by guarantors decreased in the first half 2014, as well as the balance of remaining debt, while the amount of repayments by guarantors remained the same. The share of loans and number of loan accounts being repaid by guarantors compared to information at the overall system level is low and amounts to a mere 0.37% and 0.15%.

For the purpose of mitigating the adverse effects of the global financial and economic crisis and considering the preservation of the banking sector's stability, in late 2009, the Agency adopted the Decision on Temporary Measures for Rescheduling of Loan Commitments of Natural Perons and Legal Entities[31].

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

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[30] "Official Gazette of the Federation of B&H", No. 55/14.
[31] "Official Gazette of the Federation of B&H", No. 2/10, 1/12, 111/12 and 1/14.

Acting upon the said Decision, in the first half of 2014, banks in the Federation of B&H have received a total of 223 requests for loan restructuring and approved 201 requests in the total amount of KM 39 million or 90%, which higher by 13% compared to the same period in 2013. Out of the total amount of approved restructured liabilities, KM 38 million refer to legal entities and KM 1 million to natural persons.

The net effect of loan loss reserves based on performed restructurings is an increase of KM 376 thousand. It is worth noting that there were also contrary trends in sense that there were both increases and decreases in loan loss reserves on this basis, which finally resulted in the aforementioned net effect.

According to the aforementioned Decision of the Agency, restructured loans represented only 0.3% of total loans as of 30.06.2014 (i.e. corporate restructured loans represented 0.7% of total corporate loans and retail restructured loans represented 0.01% of total retail loans).

Based on this information, it can be concluded that the result of restructured loans is relatively modest considering both their number and amount, when compared to the total loan portfolio and sector-level portfolio (for legal entities and natural persons).

Although the results and effects of the Decision's implementation are not significant, the adoption of such a regulation was particularly important, i.e. such temporary measures were truly necessary in the conditions of the financial and economic crisis and their effects on the real sector in the Federation of B&H and had positive effects on debtors (both corporate and retail) by facilitating debt servicing in accordance with their payment capacities. Therefore, the validity prolongation of the Decision to 2014 was justified, especially due to the fact that the effects of the crisis are still evident.

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 examiners 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 (6 "local" private banks) were worse than those of banks in majority foreign ownership (10 banks).

After the significant increase in non-performing loans in "local" banks by 45% in 2013, the first half of 2014 saw a slight increase of 1%, but there is a relatively high increase of 7% in banks that are in majority foreign ownership (the increase in non-performing loans in 2013 was 9%). The share of non-performing loans in banks that are in majority foreign ownership amounts to 14.3%, while it amounts to 26.2% 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. 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. 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 target 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.

-000 KM-

Table 26: *Transactions with Related Entities*

Opis	LOANS APPROVED[32]			INDEX	
	31.12.2012	31.12.2013	30.06.2014	3/2	4/3
1	2	3	4	5	6
To shareholders with over 5% voting rights, subsidiaries and other related entities	156 861	123 889	156 915	79	127
To members of the Supervisory Board and Audit Board	617	570	495	92	87
To the Management of the bank	2 574	2 507	2 159	97	86
TOTAL	160 052	126 966	159 569	79	126
Contingent and assumed off-balance sheet liabilities	21 800	16 046	13 380	74	83

During the reporting period, loan exposures to related entities increased by 26%, while contingent liabilities decreased by 17% due to reduced exposure related to one large bank. 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. 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

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

operations since banks have significantly improved the quality of their risk management in this segment.

2.2. Profitability

According to information from the income statement, a positive financial result – profit in the amount of KM 85 million was recorded at the level of the banking system in the Federation of B&H in the first half of 2014. This is a slight increase of 3% or KM 3 million compared to the same period of the previous year. The key contributor to this positive financial result at system level is higher profit recorded by 8 banks that also recorded positive figures in the same period of the previous year, with the positive effect being KM 10 million. This especially relates to one bank belonging to a group of banks highly profitable banks as well as to profit recorded by two banks that operated at a loss in the previous year (the positive effect is KM 4 million). On the other hand, a negative effect of KM 11 million is primarily the result of a bigger loss recorded by one bank as well as lower profit recorded by a few banks.

The key effect on improved profitability of most banks is primarily the results of the application of the new methodological approach (implementation of IAS 37/39 starting from 31.12.2011), which led to smaller value adjustment costs.

Not posting the profit tax (KM 3.5 million), despite the increase in non-interest bearing expenses being greater than the increase in total income, resulted in a better financial result compared to the same period of the previous year.

A positive financial result in the amount of KM 94.7 million was recorded by 16 banks and it is up by 7% or KM 6 million compared to the same period of the previous year. At the same time, an operating loss in the amount of KM 9.4 million was recorded by one bank, which, along with two other banks, operated at a loss last year as well, and it is significantly higher by 61% compared to the same period of the previous year.

Detailed information is provided in the table below.

- KM 000 -

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

Description	30.06.2012		30.06.2013		30.06.2014	
	Amount	Number of banks	Amount	Number of banks	Amount	Number of banks
1	2	3	4	5	6	7
Loss	-5 744	3	-5 813	3	-9 362	1
Profit	75 988	16	88 504	14	94 701	16
Total	**70 244**	**19**	**82 691**	**17**	**85 339**	**17**

As in other segments, this segment also shows some concentrations: out of the total profit (KM 95 million), 71% or KM 67 million refers to the two largest banks in the system with an assets share of 49% in the banking sector, while the total loss of KM 9 million refers to one small bank with a low assets share in the system. Analytical data indicates that a total of 10 banks has a better financial result (by KM 14 million), while 6 banks have a poorer financial result (by KM 11 million).

Based on analytical data as well as 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 improved slighty compared to the previous year, especially in relation to large banks that recorded greater profit compared to the same period of the previous year. This is primarily a result of the implementation of a new methodological approach.

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 five years, which is evident from the increase in non-performing and uncollectable loans and which does not corelate 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 three years. This leads to the conclusion, as well as suspicion, that value adjustments are underestimated and not at an adequate level in some banks.

At system level, total income amounted to KM 429 million, up by 2% or KM 9 million compared to the samle period of the previous year. Total non-interest bearing expenses amount to KM 343 million, with a growth rate of 3% or KM 9 million compared to the same period of the previous year. This has negatively affected the total finacial result of the banking sector.

Despite the increase in average interest-bearing loans in most of banks by 2.8%, a decrease in the average interest rate on loans (as a result of a slight decrease in active loan interest rates and the increase in non-performing loans) led to the further reduction of interest-bearing income. Although some banks recorded higher interest income compared to the same period of the the previous year (as a result of intensified lending activities), much lower interest income of one large bank has caused the reduction at system level. Interest income amounted to KM 386 million, down by 1% or KM 3 million compared to the same period of the previous year, with the share in the structure of total income being down from 92.7% to 90.2%. The largest share refers to loan interest income, which also recorded the biggest nominal drop of KM 4 million or 1%, with the share in total income being down from 83.6% to 80.9%.

Compared to the same period of the previous year, positive trends were recorded with respect to interest expenses as their rate of decrease was higher (-5%) than the rate of decrease of interest income (-1%). Nominal interest expenses decreased by KM 7 million, and interest income by KM 3 million. Interest expenses amount to KM 115 million, and their share in the total income structure decreased from 29% to 26.9%. Average interest-bearing deposits increased by 2.4% and interest expenses related to deposit accounts amount to KM 98 million and are the biggest item, in both relative and nominal terms, in total interest expenses. This item went down by 6% or KM 4 million, as a result of the deposit base structure (higher share of deposits with lower interest rate), which resulted in a decrease in average interest rates on deposits from 1.16% to 1.07% vs. the comparable period. Interest expenses on loans and other borrowings amount to KM 10 million and are down by 12% compared to the same period of the previous year, with their share going from 2.8% to 2.4%.

As a result of the larger decrease in both interest expenses (-5%) and interest income (-1%), net interest income rose by 1% or KM 4 million and amounts to KM 271 million, but with their share in the total income structure being down from 63.6% to 63.2%.

Operating income amounts to KM 158 million and is up by 3% or KM 5 million compared to the same period of the previous year, and their share in total income structure rose from 36.4% to 36.8%. Within operating income, the largest share refers to service fees, with an increase of 7% or KM 7 million. Other operating income increased by 3% or KM 5 million, 23% or KM 1 million of which relate to income based on reduced provisions (three banks).

Total non-interest bearing expenses amount to KM 343 million and increased by 3% or KM 9 million compared to the same period of the previous year, which is mainly the result of higher value adjustment costs. At the same time, their share in the total income structure increased from 79.5% to 80.1%. The value adjustment costs amount to KM 66 million and are up by 21% or KM 12 million (KM 6 million of which relate to one small bank) compared to the same period of the previous year.

This has negatively affected the increase of their share from 12.9% to 15.4% in the total income structure.

On the other hand, operating expenses in the amount of KM 240 million and a share of 56% in total income also recorded a decrease of 2% or KM 4, although it should be noted that the costs of salaries and contributions, as the largest item in operating expenses, are up by 1% or KM 1 million and amount to KM 123 million (thus representing 28.6% of total income), while fixed assets expenses amount to KM 72 million (thus representing 17% of total income), following a decrease of 5% or KM 4 million. Other operating expenses also dropped by 3% or KM 1 million. 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.

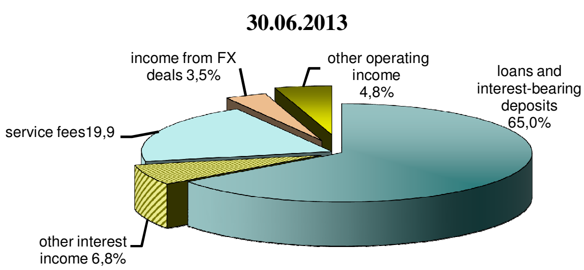
The trend and structure of total income and total expenses is provided in tables and graphs below.

-in KM 000-

Table 28: *Total Income Structure*

Struktura ukupnih prihoda	30.06.2012		30.06.2013		30.06.2014		INDEX	
	Iznos	%	Iznos	%	Iznos	%		
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 institution	2.789	0,5	1.026	0,2	2.489	0,5	37	243
Loans and leasing facilities	366.570	66,0	351.026	64,8	346.714	63,7	96	99
Other interest income	36.719	6,6	37.225	6,8	37.272	6,8	101	100
TOTAL	406.078	73,1	389.277	71,8	386.475	71,0	96	99
II Operating income								
Service fees	104.172	18,8	107.733	19,9	114.775	21,1	103	107
Income from FX deals	21.294	3,8	19.106	3,5	19.405	3,6	90	102
Other operating income	23.742	4,3	26.000	4,8	23.408	4,3	110	90
TOTAL	149.208	26,9	152.839	28,2	157.588	29,0	102	103
TOTAL INCOME (I + II)	555.286	100,0	542.116	100,0	544.063	100,0	98	100

Graph 20: *Total Income Structure*



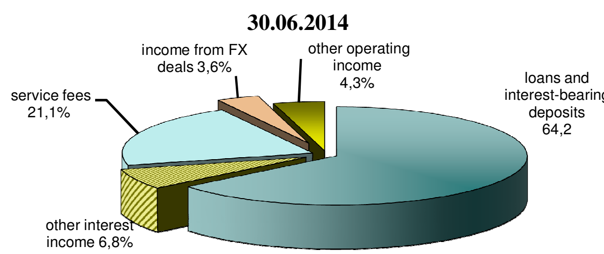


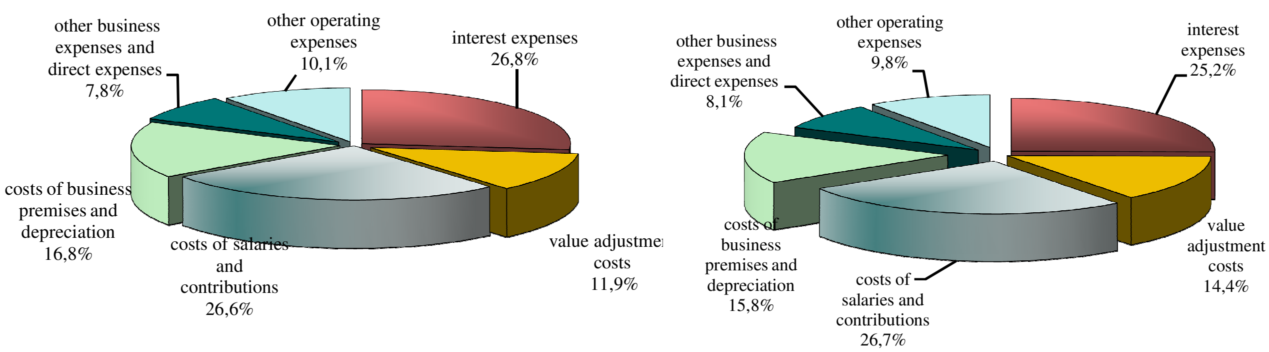
Table 29: *Total Expenses Structure*

Total expenses structure	30.06.2012		30.06.2013		30.06.2014		INDEX	
	Amount	%	Amount	%	Amount	%		
1	2	3	4	5	6	7	8 (4/2)/	9 (6/4)
I Interest expenses and similar expenses								
Deposits	108 378	22.4	104 333	22.9	98 178	21.4	96	94
Liabilities based on loans and other borrowings	20 484	4.2	11 719	2.6	10 183	2.2	57	87
Other interest expenses	7 744	1.6	5 932	1.3	7 045	1.6	77	119
TOTAL	136 606	28.2	121 984	26.8	115 406	25.2	89	95
II Total non-interest-bearing expenses								
Costs of value adjustment of risk-bearing assets and provisions for contingent liabilities and other value	64 070	13.2	54 397	11.9	66 088	14.4	85	121

adjustments								
Costs of salaries and contributions	124 146	25.7	121 419	26.6	122 503	26.7	98	101
Costs of business premises and depreciation	79 630	16.5	76 433	16.8	72 377	15.8	96	95
Other business expenses and direct expenses	35 403	7.3	35 501	7.8	37 371	8.1	100	105
Other operating expenses	44 175	9.1	46 276	10.1	44 979	9.8	105	97
TOTAL	347 424	71.8	334 026	73.2	343 318	74.8	96	103
TOTAL EXPENSES (I + II)	484 030	100.0	456 010	100.0	458 724	100.0	94	101

Graph 21: *Total Expenses Structure*

30.06.2013. **30.06.2014.**



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	30.06.2012	30.06.2013	30.06.2014
Profit from average assets	0.5	0.6	0.6
Profit from average total capital	3.3	3.7	3.6
Profit from average share capital	5.8	7.0	7.0
Net interest income/average assets	1.8	1.8	1.8
Operating income/average assets	1.0	1.0	1.0
Total income/average assets	2.8	2.8	2.8
Business expenses and direct expenses[33]/average assets	0.7	0.6	0.7
Operating expenses/average assets	1.7	1.7	1.6
Total non-interest-bearing expenses/average assets	2.3	2.3	2.2

An analysis of key ratios for the profitability quality assessment has shown that, due to approximately the same growth and average assets and amount of recorded profit, the ROAA (return on average assets) remained the same (0.6%), while the ROAE (return on average equity), due to approximately the same growth and average share capital and amount of recorded profit, also remained the same (7%). The banks' productivity indicator, measured as a ratio between total income and average assets (2.8%), remained the same vs. the end of the comparable period of the previous year. Other ratios showed slight changes: due to higher value adjustment costs, the business expenses and direct expenses ratio/average assets deteriorated from 0.6% to 0.7%, and the operating expenses/average assets ratio improved from 1.7% to 1.6% as a result of lower operating expenses, along with a simultaneous increase in average assets.

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

[33] Expenses also include value adjustment costs.

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, the evident slowdown and downward trend of economic activities caused lower demand for loans and a more restrictive approach on the supply side (banks). This will directly affect the profitability of the entire banking sector in the period to come. 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[34] for all banks seated in the Federation of B&H as well as their organisational units operating on the territory of the Federation of B&H. the effective interest rate represents an actual relative 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[35].

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 2012, March, June, and December 2013, and March and June 2014.

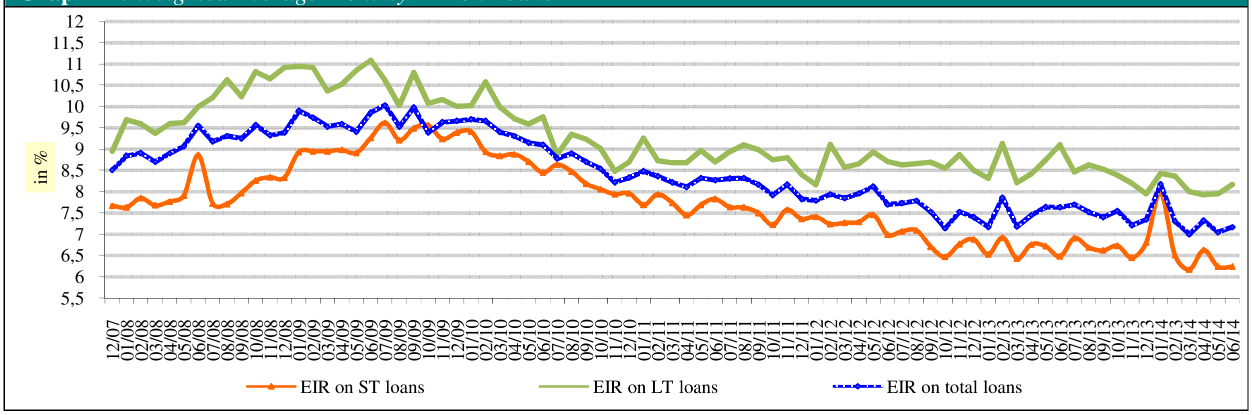
Table 31 : *Weighted Average NIR and EIR on Loans*

DESCRIPTION	12/2012		03/2013		06/2013		12/2013		03/2014		06/2014	
	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	6.39	6.88	6.06	6.44	6.04	6.48	6.18	6.81	5.81	6.17	5.70	6.24
1.1. Corporate	6.39	6.86	6.12	6.46	6.09	6.47	6.21	6.79	5.77	6.06	5.64	6.13
1.2. Retail	8.46	10.89	8.58	10.90	7.92	10.91	6.42	8.51	8.27	11.80	8.32	11.72
2. Weighted IR on long-term loans	7.66	8.50	7.48	8.21	8.07	9.10	7.31	7.95	7.22	8.00	7.54	8.17
2.1. Corporate	6.73	7.22	6.40	6.72	6.94	7.40	6.83	7.17	6.72	7.18	6.03	6.30

[34] 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. 27/07).
[35] Instructions for Implementation of the Decision on Uniform Method of Calculation and Disclosure of Effective Interest Rate on Loans and Deposits and Instructions for Calculation of Weighted and Effective Interest Rate.

2.2. Retail	8.48	9.59	8.37	9.47	8.52	9.79	7.93	8.95	7.64	8.64	8.90	9.83
3. Total weighted IR on loans	6.80	7.40	6.66	7.18	6.93	7.63	6.72	7.35	6.45	7.00	6.59	7.17
3.1. Corporate	6.45	6.93	6.20	6.53	6.26	6.66	6.41	6.92	5.99	6.32	5.76	6.18
3.2. Retail	8.47	9.69	8.38	9.55	8.49	9.83	7.84	8.92	7.65	8.74	8.88	9.89

Graph 22: *Weighted Average Monthly EIR on Loans*



When analysing interest rate trends, it is important to monitor trends of the weighted EIR, with the difference between this interest rate and the 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 half of 2014, the weighted EIR on loans amounts to 7.17% and saw oscillations ranging within a high 1.18 percentage points, with the highest rate being recorded in January (8.18%) and the lowest in March (7%). This rate is lower by 0.18 percentage points compared to the one in December 2013.

Weighted interest rates on short-term loans in the first half of 2014 saw higher oscillations (within the range of 1.81 percentage points) compared to those on long-term loans (ranging within 0.50%).

In June 2014, the weighted EIR on short-term loans amounted to 6.24%, down by 0.57 percentage points compared to December 2013. The weighted EIR on long-term loans amounted to 8.17% in June 2014, up by 0.22 percentage points compared to December 2013.

Interest rates on loans approved to two key customer segments: corporate and retail , saw a decrease in the reporting period in 2014. The weighted EIR on corporate loans (which is still lower than the EIR on retail loans) went down from 6.92% in December 2013 to 6.18% in June 2014. This downward trend of weighted EIRs on corporate loans was also seen with respect to short-term loans (from 6.79% to 6.13%) and long-term loans (from 7.17% to 6.30%).

In June 2014, the EIR on retail loans amounted to 9.89%, up by 0.97 percentage points compared to December 2013. The EIR on long term-loans of this segment went from 8.95% in December 2013 to 9.83% in June 2014. The EIR on short-term loans amounted to 11.72% in June 2014, up by 3.21 percentage points compared to December 2013.

Compared to December 2013, the most significant decrease of the EIR was recorded in June 2014 with respect to long-term retail loans – small businesses (from 13.77% to 9.26%), while the most significant increase was seen in relation to short-term retail loans – general consumption (from 8.16%

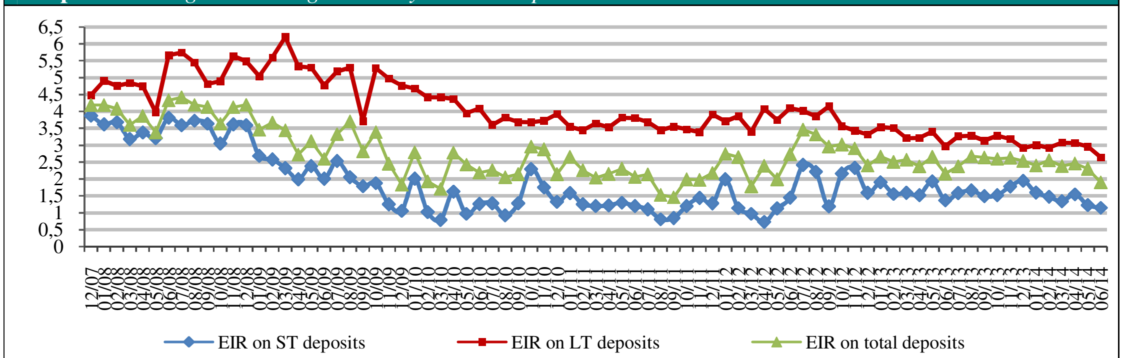
to 11.64%).

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

Table 32 : *Weighted Average NIR and EIR on Deposits*

O P I S	12/2012		03/2013		06/2013		12/2013		03/2014		06/2014	
	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	1.59	1.59	1.57	1.59	1.35	1.37	1.94	1.95	1.31	1.34	1.13	1.15
1.1. up to three months	1.28	1.28	1.26	1.26	1.01	1.01	1.92	1.92	1.06	1.07	0.94	0.95
1.2. up to one year	2.53	2.55	1.98	2.02	1.80	1.86	1.99	2.01	1.60	1.65	1.59	1.62
2. Weighted IR on long-term deposits	3.30	3.32	3.18	3.21	2.95	2.97	2.89	2.92	3.04	3.08	2.61	2.64
2.1. up to three years	3.17	3.19	3.03	3.06	2.64	2.66	2.58	2.61	2.68	2.72	2.55	2.58
2.2. more than three years	4.42	4.46	4.01	4.04	4.32	4.33	4.24	4.28	3.94	3.98	2.80	2.82
3. Total weighted IR on deposits	2.39	2.40	2.55	2.57	2.14	2.16	2.50	2.53	2.34	2.38	1.87	1.90

Graph 23: *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 2013, the weighted EIR on total term deposits in June 2014 is down by 0.63 percentage points (from 2.53% to 1.90%).

The weighted EIR on short-term deposits has decreased. In June 2014, it amounted to 1.15%, down by 0.80 percentage points compared to December 2013.

The weighted EIR on long-term deposits also saw a decrease in the second quarter of 2014 and amounts to 2.64%, down by 0.28 percentage points compared to December 2013 (12/2013: 2.92%).

In the period from the second half of 2012 to the second quarter of 2014, new corporate deposits decreased, especially those of short-term nature. This has resulted in a significant increase in short-term interest rates of the corporate segment and eventually to average interest rates of the corporate segment being higher than average interest rates of the retail segment in the reporting period. As of June 2014, despitethe still evident trend of low increase in new corporate deposits, weighted EIRs of the corporate segment amount to 2.98%, which is similar to December 2013, when they amounted to 3%. EIRs of the corporate segment in relation to both short-term (as of 12/2013: from 1.41% to 1.40%) and long-term deposits (as of 12/2013: from 3.35% to 3.25%) saw minimal oscillations.

The weighted EIR on retail deposits amounts to 2.34%, slightly down compared to December 2013 (2.65%), with a recorded drop of the EIR on long-term deposits (from 3.03% to 2.64%) and a stagnation in relation to short-term deposits (from 1.64% to 1.67%).

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

DESCRIPTION	31.12.2012		30.06.2013		31.12.2013		31.03.2014		30.06.2014	
	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 overdraft facilities	8.43	8.57	8.37	8.53	8.25	8.42	8.09	8.26	8.14	8.31
2. Weighted IR on call deposits	0.19	0.19	0.18	0.18	0.15	0.15	0.14	0.14	0.13	0.13

As a rule, the EIR on these assets and liabilities items is equal to the nominal interest rate. The weighted EIR on total overdraft facilities for the banking sector in June 2014 amounted to 8.31% (down by 0.11 percentage points compared to December 2013) and to 0.13% on call deposits (slightly lower compared to December 2013).

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.

In 2009, negative trends from the last quarter of 2008 were halted and basic liquidity indicators improved (mostly thanks to reduced lending activity). 2010 saw a slight deterioration of these indicators, continuing in 2011, but in lesser intensity. A somewhat greater deterioration of these indicators was again seen in the first quarter of 2012 as a result of reduced cash funds related to a slight increase in lending activities and investments in securities, reduced deposits, payment of loan commitments due as well as the increase in outstanding receivables. This was a trend that, with minor oscillations, continued until the end of 2012. The first half of 2013 was characterised by the continued mild worsening of these indicators, caused by the outflow of deposits, payment of loan commitments due and the continued growth of past due outstanding receivables, while the second half of 2013 saw a slight improvement of the indicators, caused by an increase in deposits and cash funds.

The banks' efforts to achieve better profitability through better allocation of financial assets, changes in the structure of deposit sources, as well as the long-present trend of reducing loan commitments and liabilities under subordinated debt, influenced by the mortgage crisis and recession in the Eurozone, have all led to a faster decrease in liquid assets compared to the reduction of short-term financial liabilities, a decrease in the share of liquid assets in total assets and the deterioration of the ratio of loans to deposits, loans taken and subordinated debt.

However, despite the evident negative trends, 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, with a trend of moderate improvement since the end of 2010. Still, due to the still present effect and impact of the global financial crisis as well as mortgage crisis in the Eurozone (that has adversely affected the banking systems of certain European countries and parent banks of FB&H banks), 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 30.06.2014, the largest share of 74.0% still refers to deposits, followed by loans taken (including subordinated debts[36]) with a share of 7.5%. 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[37]. After a longer period of improvement (the period before the crisis), it worsened slightly in 2010 and this trend (with minor oscillations) continued in 2011 and the first quarter of 2012, after which it stopped and the structure modestly improved in late 2012, which continued in 2013 and the first half of 2014.

- in KM 000-

[36] Subordinated debts: loans taken and permanent items.

[37] As per remaining maturity.

DEPOSITS	31.12.2012		31.12.2013		30.06.2014		INDEX	
	Amount	Share %	Amount	Share %	Amount	Share %		
1	2	3	4	5	6	7	8(4/2)	9(6/4)
Savings and call deposits	4 805 480	43.8	5 233 356	45.4	5 237 688	45.9	109	100
Up to 3 months	267 199	2.5	365 229	3.2	244 086	2.1	137	67
Up to 1 year	709 620	6.5	668 142	5.8	624 090	5.5	94	93
1. Total short-term deposits	5 782 299	52.8	6 266 727	54.4	6 105 864	53.5	108	97
Up to 3 years	3 576 903	32.6	3 541 354	30.7	3 408 096	29.9	99	96
More than 3 years	1 601 799	14.6	1 715 768	14.9	1 898 679	16.6	107	111
2. Total long-term deposits	5 178 702	47.2	5 257 122	45.6	5 306 775	46.5	102	101
TOTAL (1 + 2)	10 961 001	100.0	11 523 849	100.0	11 412 639	100.0	105	99

Table 34: *Maturity Structure of Deposits by Contractual Maturity*

Compared to 31.12.2013, total deposits fell by 1% or KM 111 million, largely as a result of a decrease in deposits of banking institutions by 19% or KM 197 million and deposits of private companies by 7% or KM 70 million and, on the other hand, by an increase in retail deposits by 3% or KM 186 million and deposits of non-profit organisations by 9% or KM 23 million. The maturity structure of deposits with contractual maturity is relatively good, with short-term deposits holding a share of 53.5% and long-term deposits a share of 46.5%, which is somewhat better compared to 31.12.2013.

Changes in maturity structure stem from a decrease in short-term deposits by 3% or KM 161 million, largely related to a decrease in deposits of banking institutions (with a term up to 3 months) by KM 133 million and deposits of private companies by KM 49 million, as well as an increase in terms of public companies by KM 17 million. Long-term deposits rose slightly by 1% or KM 50 million, as a result the increase in deposits with a term over three years by 11% (mostly retail deposits), while deposits up to three years recorded a 4% decrease (mostly deposits of public companies and banking institutions). It should be noted that long-term deposits are still dominated by two segments: retail, with the share increasing from 63.6% to 65.4%, and banking institutions, with the share decreasing slightly from 12.3% to 11.8%, although deposits of public companies are also a significant long-term source, with a decrease from 9.2% to 7.5%. In deposits with a term from one to three years, the largest share of 70.6% is held by retail deposits (slightly up by 3.2 percentage points), followed by deposits of public companies with 10.6% (down by 2.6 percentage points). Deposits over three years mostly consist of retail deposits (56.1%, slightly down by 0.3 percentage points) and deposits of banking institutions with a share of 25.3% (having a trend of stagnation after a long trend of reduction) (at the end of 2013: 25.6%, at the end of 2012: 33.0%; at the end of 2011: 46.9%, at the end of 2010: 60.9%).

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 35: *Maturity Structure of Deposits by Remaining Maturity*

DEPOSITS	31.12.2012.		31.12.2013.		30.06.2014.		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)	4 941 325	45.1	5 343 263	46.4	5 336 063	46.8	108	100
7- 90 days	908 834	8.3	920 951	7.9	920 788	8.0	101	100
91 days to one year	2 278 639	20.8	2 126 249	18.5	1 963 498	17.2	93	92
1. Total short-term deposits	8 128 798	74.2	8 390 463	72.8	8 220 349	72.0	103	98
Up to 5 years	2 609 727	23.8	3 002 846	26.1	3 044 739	26.7	115	101
More than 5 years	222 476	2.0	130 540	1.1	147 551	1.3	59	113
2. Total long-term deposits	2 832 203	25.8	3 133 386	27.2	3 192 290	28.0	111	102
TOTAL (1 + 2)	10 961 001	100.0	11 523 849	100.0	11 412 639	100.0	105	99

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 72.0%. However, there is a trend of moderate improvement compared to the end of 2013. Short-term deposits fell by 2% or KM 170 million, with its share decreasing by 0.8 percentage points, while long-term deposits increased by 2% or KM 59 million and their share went up from 27.2% to 28%. Looking at the structure of long-term deposits, it is evidently dominated by deposits with remaining maturity of up to 5 years (95.4% of long-term deposits and 26.7% of total deposits), while the negative trend constitutes a major reduction of deposits with remaining maturity of over 5 years (when observing the period of the past two years). This is despite a moderate increase of 13% or KM 17 million in the first half of 2014. When comparing information on deposit maturities by contractual and residual maturity, it can be concluded that out of the KM 5.3 billion of total long-term contracted deposits, there were approximately KM 2.2 billion, i.e. slightly above 41%, of long-term contracted deposits with the remaining maturity of one year as of 30.06.2014.

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.

Moreover, supervisory concern is increased 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 the regulated minimum limits.

-in KM000 -

Table 36: *Maturity Structure of Loans*

LOANS	31.12.2012		31.12.2013		30.06.2014		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	1 074 251	10.1	1 175 825	10.8	1 313 358	11.8	109	112
Short-term loans	2 472 571	23.2	2 360 832	21.8	2 345 253	21.2	95	99
Long-term loans	7 119 302	66.7	7 315.743	67.4	7 431 969	67.0	103	102
TOTAL LOANS	10 666 124	100.0	10 852 400	100.0	11 090 580	100.0	102	102

In the first half of 2014, long-term loans increased by 2% or KM 116 million, short-term loans recorded a slight drop in the amount of 1% or KM 16 million, while past due receivables significantly increased by 12% or KM 138 million, which is yet another indicator of the deterioration of the collection rate of loans due and difficulties that debtors have in servicing liabilities towards banks in the light of the economic crisis. In the structure of past due receivables, 68% refers to private companies, 30% to the retail sector and 2% to other sectors.

An analysis of maturities of two key sectors shows that 84.4% of retail loans are long-term loans, while 48.7% of total approved loans refers to private companies.

In the structure of assets, loans, as the key category, still hold the largest share of 71.9%, up by 1.6% compared to the end of 2013. Loans themselves recorded a slight increase of 2.0%. Cash funds dropped by 5% or KM 242 million and their share decreased from 28.6% to 27.1% compared to the end of 2013.

An overview of the main liquidity ratios is provided in the table below. Banks have transitioned to new regulations as of 31.12.2011, which led to a major increase in total assets, thus causing a deterioration of the ratios: loans/deposits and loans taken (if observed across periods). In 2012, liquidity ratios further deteriorated, as prompted by a reduction of cash funds through increased lending activities and the settlement of loan commitments due, while the ratio of short-term financial liabilities/total financial liabilities improved slightly due to the better maturity structure of sources of funding. This also continued in the first half of 2013. The increase in deposits and cash funds in the second half of 2013 led to a modest improvement of the ratios compared to 31.12.2012. In the first half of 2014, ratios deteriorated slightly again as a consequence of the decrease in deposits and increase in oustanding receivables.

- in % -

Table 37: *Liquidity Ratios*

Ratios	31.12.2012	31.12.2013	30.06.2014
1	2	3	4
Liquid assets[38]/total assets	26.8	28.9	27.2
Liquid assets /short-term financial liabilities	46.2	50.6	47.9
Short-term financial liabilities/total financial liabilities	68.9	67.9	67.9
Loans/deposits and loans taken[39]	88.1	86.4	89.4
Loans/deposits, loans taken and subordinated debt[40]	86.8	85.3	88.2

In 2012, the ratio of loans/deposits and loans taken deteriorated. The same trend continued in the first half of 2013, but was halted in the second half of 2013. In the first half of 2014, this ratio worsened slightly again. As of 30.06.2014, the ratio was above 85% (critical level) with respect to 11 banks. On the one hand, this was the result of their liabilities structure (relatively significant share of capital) and, on the other hand, a 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 and practices of sources of funding management in order to ensure a satisfactory liquidity position.

In 2014, banks have duly fulfilled the requirement of maintaining the defined level of the required reserve at the Central Bank of B&H. 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

[38] In narrow terms, liquid assets are: cash and deposits and other financial assets with remaining maturity of less than 3 months (excluding interbank deposits).
[39] Empirical standards are: below 70% - very sound, 71%-75% - satisfactory, 76%-80% - marginally satisfactory, 81%-85% - insufficient, over 85% - critical.
[40] The previous ratio was expanded and sources now include subordinated debts, thus being a more realistic indicator.

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 exceed the defined minimum of the 10-day average of 10% (20% until 10.06.2014) in relation to short-term sources of funding and the daily minimum of 5% (10% until 10.06.2014) in relation to the same basis, as illustrated in the table below.

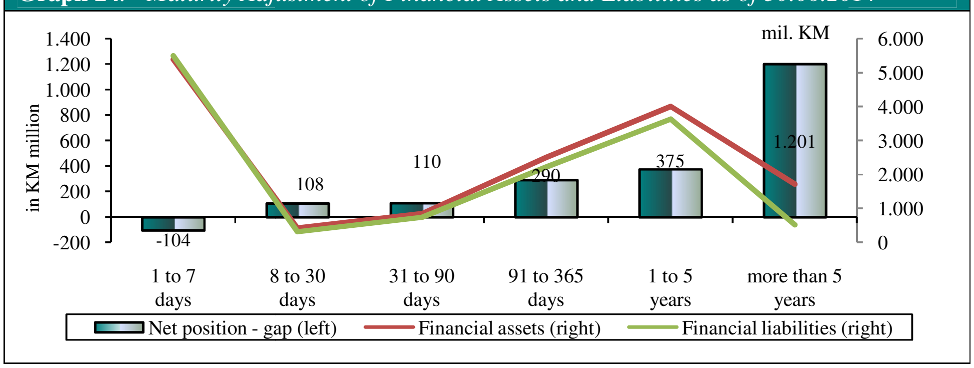
- in KM 000 -

Table 38: *Liquidity Position – 10-Day Average and Daily Minimum*

	31.12.2012	31.12.2013	30.06.2014	INDEX	
	Amount	Amount	Amount		
1	2	3	4	5(3/2)	6(4/3)
1. Average daily balance of cash	3 408 958	3 722 887	3 714 664	109	100
2. Lowest total daily cash balance	3 149 188	3 423 657	3 484 154	109	102
3. Short-term sources of funding (calculation basis)	5 631 431	5 887 967	5 977 556	105	102
4.Amount of liabilities[41] :					
4.1. 10-day average 20% of the amount under item 3	1 126 286	1 177 593	597 756	105	51
4.2. daily minimum 10% of the amount under item 3	563 143	588 798	298 878	105	51
5. Performance of liabilities: 10-day average[42]					
Surplus = no.1 – item no. 4.1.	2 282 672	2 545 294	3.116 908	112	122
6. Performance of liabilities: daily minimum					
Surplus = no.2 – item no. 4.2.	2 586 045	2 834 859	3 185 276	110	112

When observing the maturity adjustment of remaining maturities of total financial assets[43] and liabilities, it can be concluded that the adjustment rate is good, although somewhat lower compared to 31.12.2012.

Graph 24*: Maturity Adjustment of Financial Assets and Liabilities as of 30.06.2014*



In the first half of 2014, short-term financial assets of banks were higher than short-term financial liabilities by KM 404 million. Compared to the end of 2013, when the positive gap amounted to KM 522 million, this represents a decrease of KM 118 million or 22.6%, which also led to the deterioration of the coverage ratio of short-term liabilities from 105.9% to 104.6%.

[41] According to Article 1 of the 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), the percentage of maintaining the 10-day average liquidity minimum and the daily average cash funds minimum was reduced from 20% to 10% and from 10% to 5%, respectively.

[42] Promjene u indexima na pozicijama 4.1., 4.2., 5. i 6. su rezultat izmjene navedene u prethodnoj napomeni.

[43] Finansijska aktiva iskazana je na neto osnovi (umanjena za ispravke vrijednosti).

Short-term financial assets dropped by 1.9% and short-term financial liabilities by 0.6%. In the structure of short-term financial assets, an increase in net loans (up by 1.7% or KM 70 million), trading assets (up by 6.5% or KM 25 million) and cash borrowings to other banks (up by 4.6% or KM 2 million) was recorded, while a decrease in cash funds (down by 5.5% or KM 243 million), securities held until maturity (down by 24.1% or KM 20 million) and other financial assets (down by 5.2% or KM 8 million) was also posted. Financial assets with remaining maturity of over one year rose by 2.8% or KM 154 million, mostly as a result of the increase in loans by 2.4% or KM 131 million)

As for liabilities with maturity of up to one year, which have dropped slightly by 0.6% or KM 55 million, the largest increase refers to the increase in other financial liabilities up (by 41.4% or KM 73 million), loan commitments (up by 13.3% or KM 28 million) and subordinated debts (up by 53.6% or KM 14 million), coupled with a decrease in deposits in the amount of 2% or KM 170 million. Liabilities with maturity of over one year decreased slightly by 0.6% or KM 26 million, which is mostly the result of an increase in deposits by 1.9% or KM 59 million and a decrease in loan commitments by 8.9% or KM 73 million and liabilities under subordinated debts by 9.8% or KM 14 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[44].

- in KM 000-

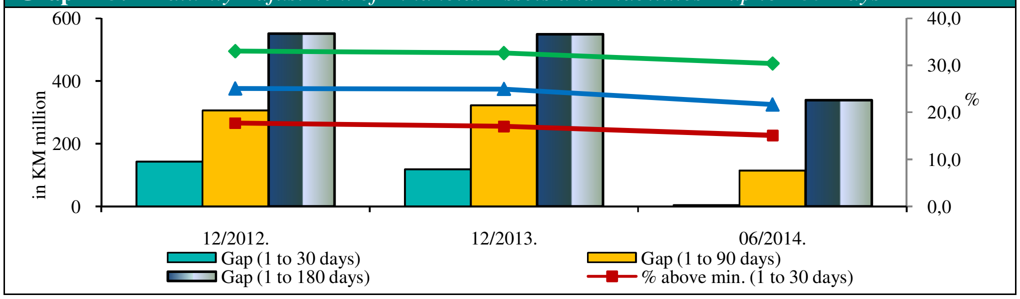
Table 39: *Maturity Adjustment of Financial Assets and Liabilities – up to 180 Days*

Description	31.12.2012 Amount	31.12.2013 Amount	30.06.2014 Amount	INDEX	
1	2	3	4	5 (3/2)	6(4/3)
I. 1- 30 days					
1. Financial assets	5 490 582	5 924 526	5 805 798	108	98
2. Financial liabilities	5 346 703	5 806 822	5 802 075	109	100
3. Difference (+ or -) = 1-2	143 879	117 704	3 723	82	3
Calculation of prescrib. requirement in %					
a) Actual %= no.1/no.2	102.7%	102.0%	100.1%		
b) Prescribed minimum %	85.0%	85.0%	85.0%		
Plus (+) or minus (-) = a - b	17.7%	17.0%	15.1%		
II. 1-90 days					
1. Financial assets	6 355 017	6 809 340	6 652 024	107	98
2. Financial liabilities	6 048 777	6 485 914	6 538 046	107	101
3. Difference (+ or -) = 1-2	306 240	323 426	113 978	106	35
Calculation of prescrib. requirement in %					
a) Actual %= no.1/no.2	105.1%	105.0%	101.7%		
b) Prescribed minimum %	80.0%	80.0%	80.0%		
Plus (+) or minus (-) = a - b	25.1%	25.0%	21.7%		
III. 1-180 days					
1. Financial assets	7 454 731	7 812 974	7 626 778	105	98
2. Financial liabilities	6 903 027	7 263 293	7 238 052	105	100
3. Difference (+ or -) = 1-2	551 704	549 681	388 726	100	71
Calculation of prescrib. requirement in %					
a) Actual %= no.1/no.2	108.0%	107.6%	105.4%		
b) Prescribed minimum %	75.0%	75.0%	75.0%		
Plus (+) or minus (-) = a - b	33.0%	32.6%	30.4%		

[44] 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 30.06.2014, banks have adhered to prescribed limits and achieved a better maturity adjustment of financial assets and liabilities in relation to the prescribed limits.

Graph 25: *Maturity Adjustment of Financial Assets and Liabilities – up to 180 Days*



Over the past two years, there is an evident trend of improvement in terms of maturity adjustment. As of 31.12.2012, financial assets surpassed financial liabilities accross all three periods of time, along with a somewhat greater improvement of liquidity positions in the period of up to 90 and up to 180 days. The positive gap in the period of up to 30 days was slightly lower compared to 31.12.2011. Maturity adjustment percentages were above the prescribed minimum by 17.7% in the first period, 25.1% in the second period and 33.0% in the third period.

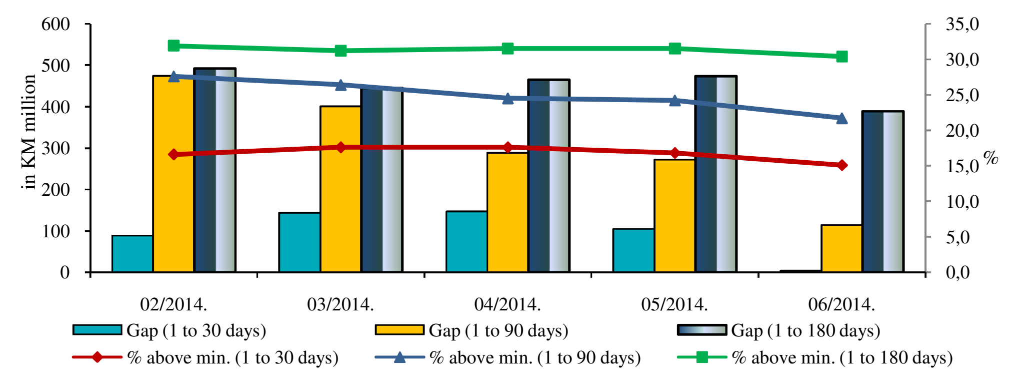
As of 31.12.2013, the maturity adjustment percentage for all three periods of time is somewhat lower compared to the end of 2012, but it is still well above the prescribed minimum (by 17.0% in the first period, 25.0% in the second period and 32.6% in the third period).

In the first half of 2014, the recorded maturity adjustment percentages were somewhat lower compared to the end of 2013. In all periods of time, primarily in the period of up to 30 days, the gap between financial assets and liabilities decreased due to reduced cash funds, while financial liabilities remained almost the same.

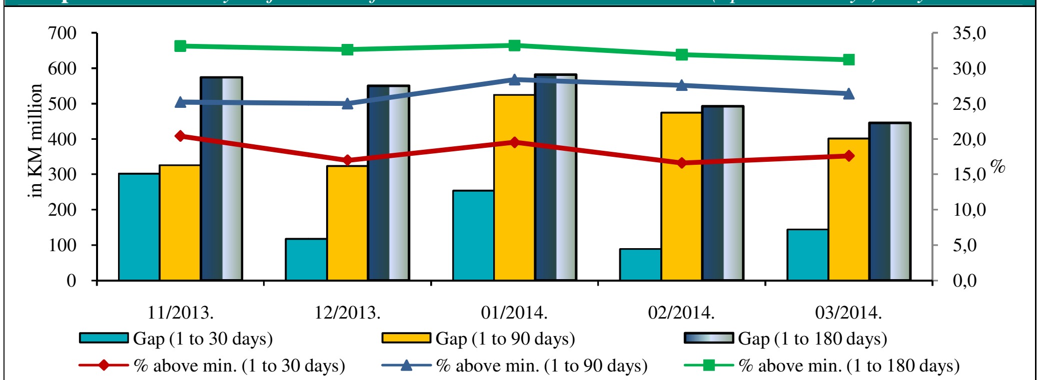
As a result of the aforementioned, the recorded maturity adjustment percentages in all three periods of time were somewhat lower compared to the end of 2013. However, all of them are still well above the prescribed minimum (by 15.1% in the first period, 21.7% in the second period and 30.4% in the third period).

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

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



Graph 26: *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[45], which regulates minimum standards for adopting and implementing the programme, 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[46].

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 EUR, banks are not exposed to FX risk in their daily operations with EUR as the key currency.

As of 30.06.2014, the currency structure of banks' assets included 11.4% or KM 1.8 billion of foreign currency items (at the end of 2013, these items amounted 12.6% or KM 1.9 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 45.8% or KM 7.1 billion (at the end of 2013, this share was 46.7% or KM 7.2 billion).

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

-in KM million-

Table 40: *FC Adjustment of Financial Assets and Liabilities (EUR and Aggregate)*[47]

Description	31.12.2013				30.06.2014				INDEX	
	EURO		TOTAL		EURO		TOTAL		EURO	TOTAL
	Amount	Share %	Amount	Share %	Amount	Share %	Amount	Share %	6/2	8/4
1	2	3	4	5	6	7	8	9	10	11
I. Financial assets										
1. Cash	996	13.0	1 516	18.0	820	10.9	1 299	15.8	82	86
2. Loans	40	0.5	44	0.5	36	0.5	39	0.5	90	89
3.Loans with a currency clause	6 285	82.2	6 465	76.9	6 316	84.0	6 485	78.7	100	100
4. Other	332	4.3	386	4.6	347	4.6	418	5.0	105	108
Total (1+2+3+4)	7 653	100.0	8 411	100.0	7 519	100.0	8 241	100.0	98	98
II. Financial liabilities										
1. Deposits	5 345	72.6	5 990	74.7	5 257	73.4	5 894	75.4	98	98
2. Loans taken	986	13.4	994	12.4	928	12.9	935	12.0	94	94
3. Deposits and loans with a currency clause	798	10.9	798	9.9	736	10.3	736	9.4	92	92
4. Other	226	3.1	237	3.0	244	3.4	249	3.2	108	105
Total (1+2+3+4)	7 355	100.0	8 019	100.0	7 165	100.0	7 814	100.0	97	97
III. Off-balance sheet										
1. Assets	80		80		39		41			

[45] "Official Gazette of the Federation of B&H", No. 48/12 – consolidated text.
[46] 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.
[47] Source: Form 5 – FX position.

2. Liabilities	255	359	206	269
IV. Position				
Long (amount)	122	113	187	198
%	6.6%	6.1%	9.7%	10.3%
Short				
%				
Allowed	30%	30%	30%	30%
Lower than the allowed level	23.4%	23.9% 23.9%	20.3%	19.7%

In terms of the structure of foreign currencies, the dominant share among financial assets[48] is held by EUR with 68.5%, which is somewhat lower compared to 31.12.2013 (70.3%) due to the lower nominal amount (from KM 1.36 billion to KM 1.20 billion). The share of EUR in liabilities is 90.8%, which is the same as at the end of 2013, coupled with a decrease of the nominal amount by KM 128 million.

However, FX risk exposure calculation also includes the amount of indexed assets items (loans) and liabilities items[49], which is quite significant on the assets side (78.7% or KM 6.5 billion) and, in nominal terms, remained almost the same as on 31.12.2013 (76.9% or KM 6.5 billion). Other FX items on the assets side hold a share of 21.3% or KM 1.8 billion and have the following structure: items in EUR 14.6% or KM 1.2 billion and other currencies 6.7% or KM 0.6 billion (at the end of 2013, loans with a currency clause amounted to KM 6.5 billion and held a share of 76.9%, while other items in EUR held a share of 16.3% or KM 1.4 billion). Out of total net loans (KM 9.9 billion), app. 65.6% have a currency clause (mostly pegged to EUR – 97.4%).

As for the sources of funding, financial liabilities determine the structure of financial assets items for every currency. The largest share in FX liabilities (KM 7.8 billion) is 82.3% or KM 6.4 billion and refers to items in EUR (deposits mostly), while the share and amount of indexed liabilities is minimal and amounts to 9.4% or KM 0.7 billion (at the end of 2013, the share of liabilities in EUR was 81.8% or KM 6.5 billion, while the share of indexed liabilities was 9.9% or KM 0.8 billion).

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 the first half of 2014 was within the defined limits. As of 30.06.2014, the long FX position was recorded with 14 banks and the short position with 3 banks. At system level, there is a long FX position of 10.3% of the total core capital of banks, which is 19.7% below the allowed limit. The individual FX position for EUR was 9.7%, which is 20.3% below the allowed limit, with financial assets items being larger than financial liabilities (net long position).

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

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[48] 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

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

III 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 targets 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.

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

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

- take measures and actions within its competences to overcome and mitigate the effects of the global financial crisis on the banking sector in the Federation of B&H;
- continue with activities within its competences to consolidate the supervision function at state level;
- maintain continuous supervision of banks through on-site and off-site controls, 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,
  - continued banking supervision that is of system relevance for the development of lending activities where large savings and other deposits are concentrated (all for the purpose of protecting depositors),
  - continued 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,
  - working on upgrades to legal regulations as based on Basel Principles, Basel Capital Accord and European Banking Directives, as has been the case so far, all as part of the preparations for B&H joining the European Union,
  - changing capital regulations for the purpose of ensuring the qualitative and structural strengthening of capital and harmonisation with the capital requirements of Basel II/III,
  - preparing and adopting a contingency plan (as a part of the crisis preparation process),
  - developing and implementing 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,

  - establishing and expanding cooperation with supervisory authorities in home countries of investors in the banking sector of the Federation of B&H, as well as in other countries – all for the purpose of ensuring more efficient bank supervision,
  - improving cooperation with the B&H Banks' Association across all segments of the banking business, 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, introducing new products, collection of receivables and ensuring full involvement in the development and functioning of a unified registry of non-performing clients – legal entities and natural persons (ensuring daily updates of information).
- continue with efforts to improve the information system that would enable 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, as per Management Board conclusions.

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

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

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

- full commitment to quality and prudent operations and to combating the crisis effects presently posing the biggest threat to banks, the real sector of the economy and the general population;
- the preparation of and updates to their contingency plans;
- further capital strengthening and ensuring a solvency level proportional to an increase in assets and risk, greater profitability, more consistent implementation of adopted policies and procedures to prevent money laundering and the financing of terrorism, the security and protection of money

in the bank and in transit, all in accordance with laws and by-laws;
- 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;
- regular, timely and accurate submission of information to the Central Loans Registry and the Uniform Central Registry of Accounts at the Central Bank of B&H.

No.: U.O.-62-2/14.
Sarajevo, 02.09.2014

A N N E X E S

ANNEX 1

Banks in the Federation of Bosnia and Herzegovina - 30.06.2014

No.	BANK	Adress		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	Interim director - DRAGAN KOVAČEVIĆ
4	INTESA SANPAOLO BANKA D.D. BOSNA I HERCEGOVINA	Sarajevo	Obala Kulina bana 9a.	033/497-555, fax:497-589	ALMIR KRKALIĆ
5	INVESTICIONO-KOMERCIJALNA BANKA dd - ZENICA	Zenica	Trg B&H 1	032/448-400, fax:448-501	SUVAD IBRANOVIĆ
6	KOMERCIJALNO-INVESTICIONA BANKA DD V.KLADUŠA	V.Kladuša	Ibrahima Mržljaka 3	037/771-253, fax:772-416	HASAN PORČIĆ
7	MOJA BANKA dd - SARAJEVO	Sarajevo	Trg međunarodnog prijateljstva br. 25.	033/586-870, fax:586-880	MIRZA HUREM
8	NLB BANKA dd - TUZLA	Tuzla	Maršala Tita 34	035/259-259, fax:250-596	ALMIR ŠAHINPAŠIĆ
9	PRIVREDNA BANKA SARAJEVO dd - SARAJEVO	Sarajevo	Alipašina 6	033/277-700, fax:664-175	ADNAN BOGUNIĆ
10	PROCREDIT BANK dd - SARAJEVO	Sarajevo	Franca Lehara bb	033/250-950, fax:250-971	EDIN HRNJICA
11	RAIFFEISEN BANK dd BiH - SARAJEVO	Sarajevo	Zmaja od Bosne bb.	033/755-010, fax: 213-851	MICHAEL MÜLLER
12	RAZVOJNA BANKA FEDERACIJE BIH	Sarajevo	Igmanska 1	033/724-930, fax: 668-952	RAMIZ DŽAFEROVIĆ
13	SBERBANK BH dd - SARAJEVO	Sarajevo	Fra Anđela Zvizdovića 1	033/295-601, fax:263-832	EDIN KARABEG
14	SPARKASSE BANK dd - SARAJEVO	Sarajevo	Zmaja od Bosne br. 7.	033/280-300, fax:280-230	SANEL KUSTURICA
15	UNICREDIT BANK dd - MOSTAR	Mostar	Kardinala Stepinca bb	036/312-112, fax:312-121	IVAN VLAHO
16	UNION BANKA dd - SARAJEVO	Sarajevo	Dubrovačka 6	033/561-000, fax: 201-567	SENAD REDŽIĆ
17	VAKUFSKA BANKA dd - SARAJEVO	Sarajevo	M. Tita 13.	033/280-100, fax: 663-399	Interim director - MIRZET RIBIĆ
18	ZIRAATBANK BH dd - SARAJEVO	Sarajevo	Dženetića Čikma br. 2.	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 OUTLINE OF THE FBA
ACTIV SUB-BALANCE

in 000 KM

No.	D E S C R I P T I O N	31.12.2012	31.12.2013	30.06.2014
	A S S E T S			
1.	Cash and deposit accounts with deposit-taking institutions	3 962 581	4 417 898	4 175 428
1a	Cash and non-interest bearing deposit accounts	625 188	627 016	509 875
1b	Interest-bearing deposit accounts	3 337 393	3 790 882	3 665 553
2.	Trading securities	375 032	381 909	406 553
3.	Loans to other banks	78 522	51 960	54 501
4.	Loans, receivables based on leasing facilities and past due receivables	10 666 124	10 852 400	11 090 580
4a	Loans	9 591 819	9 676 527	9 777 177
4b	Receivables based on leasing facilities	54	48	45
4c	Past due receivables based on loans and leasing facilities	1 074 251	1 175 825	1 313 358
5.	Held to maturity securities	173 435	180 604	183 948
6.	Business premises and other fixed assets	491 370	476 199	468 995
7.	Other real estate	30 123	36 786	39 654
8.	Investments in unconsolidated related companies	24 756	23 762	24 003
9.	Other assets	255 247	252 122	244 704
10.	LESS: value adjustment	1 066 424	1 227 090	1 266 723
10a	Value adjustments for Item 4. of the Assets	1 007 459	1 165 928	1 202 319
10b	Value adjustments for Assets items, except for the Item 4	58 965	61 162	64 404
11.	**TOTAL ASSETS**	**14 990 766**	**15 446 550**	**15 421 643**
	L I A B I L I T I E S			
12.	Deposits	10 961 001	11 523 849	11 412 639
12a	Interest-bearing deposits	9 281 938	9 363 284	9 186 872
12b	Non-interest bearing deposits	1 679 063	2 160 565	2 225 767
13.	Borrowings - liabilities due	1 752	1 577	1 594
13a	Past due liabilities			
13b	Past due - invoked off-balance sheet liabilities	1 752	1 577	1 594
14.	Borrowings from other banks	2 000		
15.	Liabilities to the Government			
16.	Loan commitments and other borrowings	1 141 561	1 039 381	994 186
16a	with remaining maturity of up to one year	244 160	212 485	240 645
16b	with remaining maturity of more than one year	897 401	826 896	753 541
17.	Subordinated debt and subordinated bonds	186 675	166 889	166 760
18.	Other liabilities	480 402	406 909	466 760
19.	**TOTAL LIABILITIES**	**12 773 391**	**13 138 605**	**13 041 939**
	E Q U I T Y			
20.	Permanent preferred shares	26 059	11 959	11 959
21.	Common shares	1 175 547	1 196 633	1 225 970
22.	Issue premiums	136 485	136 485	136 485
22a	over permanent preferred shares	8 420	8 420	88
22b	over common shares	128 065	128 065	136 397
23.	Undistributed profit and capital reserves	453 269	649 879	604 217
24.	Foreign exchange rate differences			
25.	Other capital	110 281	-2 745	85 339
26.	Loan loss provisions formed from profit	315 734	315 734	315 734
27.	**TOTAL EQUITY (20. do 25.)**	**2 217 375**	**2 307 945**	**2 379 704**
28.	**TOTAL LIABILITIES AND EQUITY (19 +26)**	**14 990 766**	**15 446 550**	**15 421 643**

	LIABILITIES AND NEUTRAL ITEMS	**661 321**	**638 913**	**644 339**
	BALANCE SHEET TOTAL OF BANKS	**15 652 087**	**16 087 617**	**16 065 982**

ANNEX 3

OVERVIEW OF ASSETS, LOANS, DEPOSITS AND FINANCIAL RESULTS OF BANKS IN THE FEDERATION OF B&H as of 30.06.2014

in 000 KM

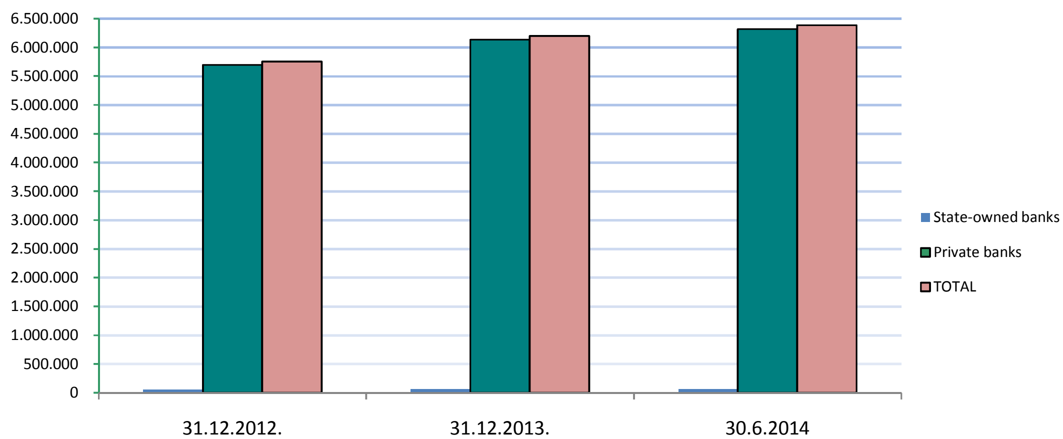
No.	BANK	Assets		Loans		Deposits		Financial result
		Amount	%	Amount	%	Amount	%	Amount
1	BOR Banka d.d. Sarajevo	234 194	1.52%	190 958	1.72%	119 932	1.05%	337
2	Bosna Bank International d.d. Sarajevo	541 318	3.51%	376 120	3.39%	351 147	3.08%	1 349
3	Hypo Alpe Adria Bank d.d. Mostar	1 060 073	6.87%	790 601	7.13%	696 152	6.10%	178
4	Intesa Sanpaolo banka d.d. Sarajevo	1 355 333	8.79%	1 137 760	10.26%	914 179	8.01%	10 356
5	Investiciono Komercijalna banka d.d. Zenica	191 549	1.24%	99 353	0.90%	135 378	1.19%	777
6	Komercijalno Investiciona banka d.d. Velika Kladuša	73 471	0.48%	39 279	0.35%	47 067	0.41%	548
7	Moja banka d.d.Sarajevo	187 978	1.22%	137 222	1.24%	156 295	1.37%	15
8	NLB banka d.d. Tuzla	836 079	5.42%	636 867	5.74%	668 585	5.86%	2 435
9	Privredna Banka d.d Sarajevo	154 319	1.00%	113 248	1.02%	123 873	1.09%	14
10	ProCredit Bank d.d. Sarajevo	362 918	2.35%	311 474	2.81%	241 560	2.12%	180
11	Raiffeisen Bank dd Bosna i Hercegovina	3 699 811	23.99%	2 323 993	20.95%	2 864 085	25.10%	35 833
12	Sberbank BH d.d. Sarajevo	924 317	5.99%	797 852	7.19%	675 637	5.92%	1 986
13	Sparkasse Bank d.d. Sarajevo	986 985	6.40%	820 622	7.40%	826 026	7.24%	5 796
14	Union banka d.d. Sarajevo	267 513	1.73%	122 171	1.10%	209 829	1.84%	412
15	UniCredit bank d.d. Mostar	3 814 143	24.73%	2 666 469	24.04%	2 878 112	25.22%	31 481
16	Vakufska banka d.d. Sarajevo	283 673	1.84%	192 874	1.74%	236 307	2.07%	-9 362
17	Ziraatbank BH d.d. Sarajevo	447 969	2.90%	333 717	3.01%	268 475	2.35%	3 004
	TOTAL	15 421 643	100%	11 090 580	100%	11 412 639	100%	85 339

ANNEX 4

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

in 000 KM

	31.12.2012	31.12.2013	30.06.2014
State-owned banks	58 050	65 179	65 475
Private banks	5 698 300	6 135 711	6 319 231
TOTAL	**5 756 350**	**6 200 890**	**6 384 706**



ANNEX 5

CLASSIFICATION OF BALANCE SHEET ASSETS AND OFF-BALANCE SHEET RISK-BEARING ITEMS as of 30.06.2014 - CLASSIFICATION OF BALANCE SHEET ASSETS ITEMS -

in 000 KM

No.	BALANCE SHEET ASSETS ITEMS	CLASSIFICATION					TOTAL
		A	B	C	D	E	
1.	Short-term loans	2 100 346	197 325	41 563	3 796	2 223	2 345 253
2.	Long-term loans	6 343 549	569 976	273 019	141 271	33 679	7 361 494
3.	Other facilities	216 724	2 321	149	1 044	1 962	222 200
4.	Accrued interest and fees	37 114	6 669	3 152	7 221	28 271	82 427
5.	Past due receivables	47 596	71 240	74 258	325 169	761 696	1 279 959
6.	Receivables based on paid guarantees		150		582	32 667	33 399
7.	Other balance sheet assets being classified	308 337	4 554	4 485	2.209	30 559	350 144
8.	**TOTAL BALANCE SHEET ASSETS BEING CLASSIFIED (sum of items 1 through 7 – calculation basis for regulatory loan loss provisions)**	**9 053 666**	**852 235**	**396 626**	**481 292**	**891 057**	**11 674 876**
9.	**CALCULATED REGULATORY RESERVES FOR LOAN LOSSES BASED ON BS ASSETS**	**177 201**	**79 314**	**96 895**	**281 527**	**890 636**	**1 525 573**
10.	**VALUE ADJUSTMENT FOR BS ASSETS**	**113 073**	**81 139**	**122 310**	**215 950**	**734 251**	**1 266 723**
11.	**REQUIRED REGULATORY RESERVES FORMED AGAINST PROFIT FOR PURPOSE OF ASSESSED LOSSES BASED ON BS ASSETS**	**101 888**	**42 978**	**24 293**	**96 575**	**158 974**	**424 708**
12.	**FORMEED REGULATORY RESERVES FORMED AGAINST PROFIT RELATED TO ASSESSED LOSSES BASED ON BS ASSETS**	**77 850**	**26 161**	**26 157**	**77 118**	**71 708**	**278 994**
13.	**SHORTFALL OF REGULATORY RESERVE FORMED AGAINST PROFIT RELATED TO ASSESSED LOSSES BASED ON BS ASSETS**						**183.630**
14.	**BALANCE SHEET ASSETS NOT BEING CLASSIFIED (gross book value)**						**5 013 491**
15.	**TOTAL BALANCE SHEET ASSETS (gross book value)**						**16 688 367**

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	2 945 266
14.b	Demand deposits and term deposits up to one month located on accounts of banks with defined investment rating	1 087 354
14.c	Tangible and intangible assets	487 964
14.d	Financial and tangible assets acquired in the process of collection of receivables (within one year upon such acquisition)	7 936
14.e	Own (treasury) shares	
14.f	Receivables based on overpaid taxes	13 232
14.g	Trading securities	131 843
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	339 896
	TOTAL Item 14	**5 013 491**
8a.	Facilities secured with a cash deposit	193 600

ANNEX 5A

CLASSIFICATION OF BALANCE SHEET ASSETS AND OFF-BALANCE SHEET RISK-BEARING ITEMS
as of 30.06.2014
- CLASSIFICATION OF OFF-BALANCE SHEET ITEMS -

in 000 KM

No.	OFF-BALANCE SHEET ITEMS	CLASSIFICATION					TOTAL
		A	B	C	D	E	
1.	Payment guarantees	349 830	44 761	3 276		1	397 868
2.	Performance guarantees	496 045	110 219	4 820	846	266	612 196
3.	Uncovered letters of credit	46 876	1 093	108			48 077
4.	Irrevocably approved, but undrawn loans	1 339 851	77 445	1 304	260	1 134	1 419 994
5.	Other contingent liabilities of the bank	10 996	287		1	130	11 414
6.	**TOTAL OFF-BALANCE SHEDET ITEMS BEING CLASSIFIED (sum of items 1 through 5 – calculation basis for regulatory loan loss provisions)**	**2 243 598**	**233 805**	**9 508**	**1 107**	**1 531**	**2 489 549**
7.	**CALCULATED REGULATORY RESERVES FOR LOAN LOSSES RELATED TO OFF-BALANCE SHEET ITEMS**	**43 818**	**14 090**	**2 025**	**632**	**1 531**	**62 096**
8.	**LOSS RESERVES FOR OFF-BALANCE SHEET ITEMS**	**20 282**	**4 741**	**2 430**	**302**	**1 213**	**28 968**
9.	**REQUIRED REGULATORY RESERVES FORMED AGAINST PROFIT RELATED TO ASSESSED LOSSED BASED ON OFF.BAL.SHEET ITEMS**	**26 539**	**10 771**	**893**	**445**	**316**	**38 964**
10.	**FORMED REGULATORY RESERVES FORMED AGAINST PROFIT RELATED TO ASSESSED LOSSED BASED ON OFF.BAL.SHEET ITEMS**	**23 954**	**9 916**	**1 130**	**1 336**	**404**	**36 740**
11.	**SHORTFALL OF REGULATORY RESERVES FORMED AGAINST PROFIT RELATED TO ASSESSED LOSSED BASED ON OFF.BAL.SHEET ITEMS**						**5 746**
12.	**OFF-BALANCE SHEET ITEMS NOT BEING CLASSIFIED**						**414 944**
13.	**TOTAL OFF-BALANCE SHEET ITEMS**						**2 904 493**
6a.	**Contingent liabilities secured with a cash deposit**						**52 592**

ANNEX 6

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

in 000 KM

No.		DESCRIPTION	31.03.2012	31.03.2013	30.06.2014
1.		**INTEREST INCOME AND EXPENSES**			
	a)	Interest income and similar income			
	1)	Interest-bearing deposit accounts with deposit-taking institutions	2 789	1 026	2 489
	2)	Loans to other banks	2 601	944	1 217
	3)	Loans and leasing facilities	366 570	351 026	346 714
	4)	Held to maturity securities	2 923	3 796	3 644
	5)	Equity securities	165	184	646
	6)	Receivables based on paid off-balance sheet liabilities	0	0	0
	7)	Other interest income and similar income	31 030	32 301	31 765
	8)	**TOTAL INTEREST INCOME AND SIMILAR INCOME**	**406 078**	**389 277**	**386 475**
	b)	Interest expenses and similar expenses			
	1)	Deposits	108 378	104 333	98 178
	2)	Borrowing from other banks	14	112	0
	3)	Borrowing taken – liabilities due	0	0	0
	4)	Liabilities based on loans and other borrowings	20 470	11 607	10 183
	5)	Subordinated debt and subordinated bonds	5 824	4 494	5 683
	6)	Other interest and similar expenses	1 920	1 438	1 362
	7)	**TOTAL INTEREST EXPENSES AND SIMILAR EXPENSES**	**136 606**	**121 984**	**115 406**
	c)	**NET INTEREST AND SIMILAR INCOME**	**269 472**	**267 293**	**271 069**
2.		**OPERATING INCOME**			
	a)	FX income	21 294	19 106	19 405
	b)	Loan fees	3 161	3 195	3 328
	c)	Fees based on off-balance sheet items	12 281	12 102	12 351
	d)	Service fees	88 730	92 436	99 096
	e)	Trading income	324	2 499	445
	f)	Other operating income	23 418	23 501	22 963
	g)	**TOTAL OPERATING INCOME a) to f)**	**149 208**	**152 839**	**157 588**
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	64 070	54 397	66 088
	2)	Other business and direct expenses	35 403	35 501	37 371
	3)	**TOTAL BUSINESS AND DIRECT EXPENSES 1) + 2)**	**99 473**	**89 898**	**103 459**
	b)	Operating expenses			
	1)	Costs of salaries and contributions	124 146	121 419	122 503
	2)	Costs of business premises, other fixed assets and utilities	79.630	76 433	72 377
	3)	Other operating expenses	44 175	46 276	44 979
	4)	**TOTAL OPERATING EXPENSES 1) to 3)**	**247 951**	**244 128**	**239 859**
	c)	**TOTAL NON-INTEREST BEARING EXPENSES**	**347 424**	**334 026**	**343 318**
4.		**PROFIT BEFORE TAXES**	**77 000**	**91 919**	**94 701**
5.		**LOSS**	**5 744**	**5 813**	**9 362**
6.		**TAXES**	**1 012**	**3 531**	**0**
7.		**PROFIT BASED ON INCREASE OF DEFERRED TAX FUNDS AD REDUCTION OF DEFERRED TAX LIABILITIES**	**0**	**116**	**0**
8.		**LOSS BASED ON REDUCTION OF DEFERRED TAX FUNDS AND INCREASE OF DEFERRED TAX LIABILITIES**	**0**	**0**	**0**
9.		**NET PROFIT 4. - 6.**	**75 988**	**88 504**	**94 701**
10.		**NET LOSS 4. - 6.**	**5 744**	**5 813**	**9 362**

11.	**FINANCIAL RESULT 9.-10.**	**70 244**	**82 673**	**85 339**

ANNEX 7

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

in 000 KM

No.	DESCRIPTION	31.12.2012	31.12.2013	30.06.2014
1	**BANK'S CORE CAPITAL**			
1.a.	Share capital, reserves and profit			
1.1.	Share capital – common and permanent preferred non-cumulative shares – cash payments	1 185 966	1 188 094	1 222 288
1.2.	Share capital – common and permanent preferred non-cumulative shares – investments in kind and in rights	12 550	12 550	12 550
1.3.	Amount of issue premiums earned upon payment of shares	136 485	136 485	136 485
1.4.	General mandatory reserves (reserves mandated by the law)	101 836	206 809	115 685
1.5.	Other reserves not related to the assets quality evaluation	309 179	362 349	367 052
1.6.	Retained – undistributed profit from previous years	167 825	248 901	266 403
1.a.	**TOTAL (1.1. to 1.6.)**	**1 913 841**	**2 155 188**	**2 120 463**
1.b.	Deductible items from 1.a.			
1.7.	Uncovered losses transferred from previous years	120 740	112 610	144 924
1.8.	Current year's loss	17 818	140 330	9 362
1.9.	Book value of own (treasury) shares of the bank	156	156	81
1.10.	Intangible assets	52 590	41 418	41 134
1.b.	**TOTAL (1.7. to 1.10.)**	**191 304**	**294 514**	**195 501**
1.	**CORE CAPITAL: (1.a.-1.b.)**	**1 722 537**	**1 860 674**	**1 924 962**
2	**SUPPLEMENTARY CAPITAL OF THE BANK**			
2.1.	Share capital – common and permanent preferred cumulative shares – cash payments	3 090	3 091	3 091
2.2.	Share capital – common and preferred cumulative shares – investments in kind and in rights			
2.3.	General loan loss provisions for the category A – performing assets	211 433	215 083	221 019
2.4.	Current year profit – audited and confirmed by an external audit	67 243	71 984	
2.5.	Profit amount for which the FBA issues an order restricting its disbursement			
2.6.	Amount of subordinated debts representing max. 50% of the core capital	120 264	165 473	165 344
2.7.	Hybrid convertible items max. 50% of the core capital			
2.8.	Permanent, non-refundable items	65 070	1 416	1 416
2.	**AMOUNT OF SUPPLEMENTARY CAPITAL: (2.1 to 2.8)**	**467 100**	**457 047**	**390 870**
3	**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			
3.2.	Capital contributions of other legal entities exceeding 5% of the bank's core capital	3 043	2 844	2 909
3.3.	Receivables from shareholders with significant voting rights – approved contrary to regulations	85		
3.4.	LCRE towards shareholders with significant voting rights in the bank (no FBA approval required)			
3.5.	LLP shortfall as per regulatory requirement	95 720	158 859	188 604
3.	**AMOUNT OF DEDUCTIBLE ITEMS FROM THE BANK'S CAPITAL: (3.1 to 3.5)**	**98 848**	**161 703**	**191 513**
A.	**NET CAPITAL OF THE BANK (1.+2.-3.)**	**2 090 789**	**2 156 018**	**2 124 319**
B.	**RISK WEIGHTED ASSETS AND LOAN EQUIVALENTS**	**11 078 498**	**10 999 406**	**11 175 653**

C.	**WEIGHTED OPERATIONAL RISK**	**974 201**	**981 318**	**982 260**
D.	**WEIGHTED MARKET RISK**			
E.	**TOTAL WEIGHTED RISKS B+C+D**	**12 052 699**	**11 980 724**	**12 157 913**
F.	**NET CAPITAL RATE (CAPITAL ADEQUACY) (A.:E.) X 100**	**17.3%**	**18.0%**	**17.5%**

ANNEX 8

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

No.	BANK	31.12.2012	31.12.2013	30.06.2014
1	BOR Banka d.d. Sarajevo	62	64	63
2	Bosna Bank International d.d. Sarajevo	247	279	292
3	Hypo Alpe Adria Bank d.d. Mostar	579	517	529
4	Intesa Sanpaolo banka d.d. Sarajevo	537	528	521
5	Investiciono Komercijalna banka d.d. Zenica	166	164	158
6	Komercijalno Investiciona banka d.d. Velika Kladuša	71	71	71
7	Moja banka d.d.Sarajevo	151	156	141
8	NLB banka d.d. Tuzla	456	442	445
9	Poštanska banka d.d. Sarajevo	85		
10	Privredna Banka d.d Sarajevo	179	177	163
11	ProCredit Bank d.d. Sarajevo	344	333	312
12	Raiffeisen Bank dd Bosna i Hercegovina	1 552	1 531	1 518
13	Sberbank BH d.d. Sarajevo	360	411	420
14	Sparkasse Bank d.d. Sarajevo	452	462	464
15	Union banka d.d. Sarajevo	183	200	195
16	UniCredit bank d.d. Mostar	1 305	1 262	1 239
17	Vakufska banka d.d. Sarajevo	230	225	231
18	Ziraatbank BH d.d. Sarajevo	171	229	234
	TOTAL	**7 130**	**7 051**	**6 996**