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 AS OF 30. 09. 2011.

Sarajevo, December 2011.

Information on banking system of the Federation of BiH (as of 31.09.2011., based on final, unaudited data) is prepared by the Banking Agency of the Federation of BiH, as a regulatory authority conducting supervision of banks, based on reports of banks, and other information and data submitted by banks. Findings and data from on-site examinations and analysis performed at the Agency (off-site financial analysis) have also been included.

# I INTRODUCTION

The growth and development of the banking sector has already been stopped for a longer period, although the negative trends, from the period after the commencement of the crises, that had been mirrored in the decline of the aggregate balance sheet, credit portfolio, profitability and employment, had been stopped, and the trends of the deterioration of loans though the incline of the poor performing loans are present in a significantly smaller volume than last year. It is obvious that the recovery of the economy, and the banking system itself, will take longer than previously planned.

As of 30.09.2011., there were 19 banks with banking license issued in the Federation of BiH, of which 2 banks were under provisional administration (Hercegovačka bank d.d. Mostar and Postanska bank BH d.d. Sarajevo). As of 30.09.2011., the number of employees in the banking sector was 7.400, which is by 0,2% more than at the end of 31.12.2010. The trend of the decreasing of the number of employees, as one of the negative effects of the economic crises on the banking sector, evident in 2009 and 2010, has been stopped in the second and third quarter of 2011.

The aggregate balance sheet of the banking sector, as of 30.09.2011., amounted to 15,25 billion KM, and is by 180 million KM or 1,2% lower that at the end of 2010. After the recorded decline in 2010., and in the first quarter of 2011, the aggregate balance sheet of the banking sector in the second and third quarter recorded a growth, primarily due to the growth of the gross balance of the banks.

In 2011, the assets structure had changes related to two key property items: increase of the credit participation from 66,2% to 67,5% and decrease of the cash funds from 29,5% to 27,3%.

As of 30. 09. 2011., the loan portfolio was 10,3 billion KM increasing by 3,2% or 323 million KM in comparison to the end of 2010. The slight credit growth from the last three quarters of 2010., continued in the first two quarters in 2011. (in the I quarter by 1,4% or 140 million KM and II by 1,5% or 151 million KM ), which was an encouraging indicator of the intensifying of the banks' credit activities. However, in the third quarter the credit growth again slowed down and is 0,3% or 32 million KM.

The cash funds in the assets are 4,2 billion KM decreasing by 6% or 282 million KM in comparison to the end of 2010., mostly due to the increase of the loan placements. The decline of the cash funds was recorded in the first quarter of this year, and in the second and third quarter they recorded a slight growth.

The most important liability items: deposits, credit liabilities and total capital as of 30. 09. 2011., had minimal changes in comparison to the end of the previous year: the growth was realized in deposits 1% (or 160 million KM) and total capital of 3% (or 53 million KM), while the credit liabilities decreased by 4% or 59 million KM.

In the financing sources structure, the deposits with the amount of 11,4 billion KM and participation of 74,7% are still a dominant source of banks financing in the Federation of BiH. The credit funds are the second highest source in the amount of 1,34 billion KM (or 8,8% liabilities), which the banks got mostly through borrowings from foreign financial institutions.

Savings deposits, as the most significant segment of deposit and financial potential of banks, maintained the positive growth trend in the first three quarters of 2011, and as of 30.09.2011 they were 5,26 billion KM – higher by 5,8% in comparison to the end of 2010, which is the highest up to date.

As 30.09.2011, the regulatory and net capital was two billion KM, decreasing by 2% in comparison to 2010. As of 30.09.2011., the banking system capital adequacy rate, as one of the most important indicators of strength and adequacy of banks' capital, is 15,3%, which is still far above the legal minimum (12%) and it presents a satisfactory capitalization of the overall system and a strong base and foundation for maintaining its security and stability. However, it declined by 0,9% in comparison to the end of 2010, when it was 16,2%.

At the level of the banking system of F BiH in the three quarters of 2011, positive financial result was realized in the total amount of 41,4 million KM. Positive financial result of 100 mill.KM was realized by 13 banks, while 6 banks realized losses in performance in the amount of 58,6 mill. KM.

# II BUSINESS PERFORMANCES OF BANKS IN THE FEDERATION OF BIH

## 1. STRUCTURE OF THE BANKING SECTOR

### 1.1. Status, number and business network

As of 30.09.2011., there were 19 banks with the banking license issued in the Federation of BiH. Number of banks is the same as of 31.12.2010. There is a special law regulating establishment and work of the Development Bank of the Federation of BiH, Sarajevo which is a legal successor of the Investment Bank of the Federation of BiH d.d., Sarajevo, as of 01.07.2008.

As of 30.09.2011., there were two banks under provisional administration (Hercegovačka banka d.d. Mostar and Postanska banka BH d.d. Sarajevo).

In nine months of 2011., there was no significant expansion of the banks' organizational units' network. There were established ten new organizational units. Simultaneously, some banks closed their organizational units, that is they performed reorganization and merger of their organizational parts with an aim to rationalize their expenses, so as of 30. 09. 2011., the banks from the Federation of BiH have a total of 611 organizational units. In relation to 31. 12. 2010 when the banks had 600 organizational units, the listed presents an increase of 1,8%.

As of 30.09.2011., seven banks from the Federation of BiH had 56 organizational units in the Republic Srpska and nine banks had 12 organizational units in District Brcko. Five banks from the Republic Srpska had 21 organizational units in the Federation of BiH. The only change was in the number of organizational units of banks from Federation of BiH on the territory of the Federation of BiH.

As of 30.09.2011., all the banks had the license for inter-bank transactions in the internal payment system and 15 banks were under the deposit insurance program.

## 1.2. Ownership structure

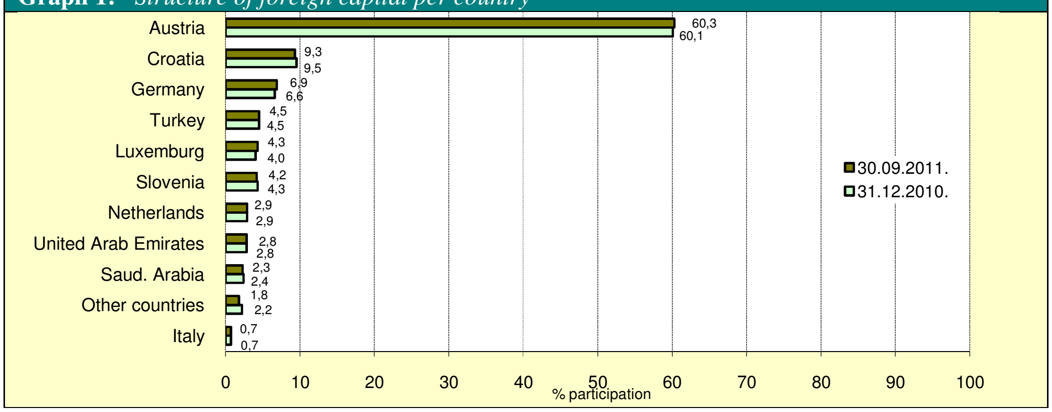
As of 30.09.2011., ownership structure in banks[1] based on the available information and on-site visits to banks[2] is the following:

- Private and majority private ownership 18 banks (94,7%)
- State and majority state ownership[3] 1 banks (5,3%)

Seven banks, of 18 banks with majority private ownership, are majority owned by domestic legal entities and individuals (residents), while 11 banks have majority foreign ownership.

If only foreign capital is analyzed based on the criteria of the shareholders' home country, as of 30.09.2011., the condition is the same as at the end of 2010: shareholders from Austria owned 60,3% of foreign capital, the shareholders from Croatia owned 9,3% of foreign capital, while other countries participated less than 7%.

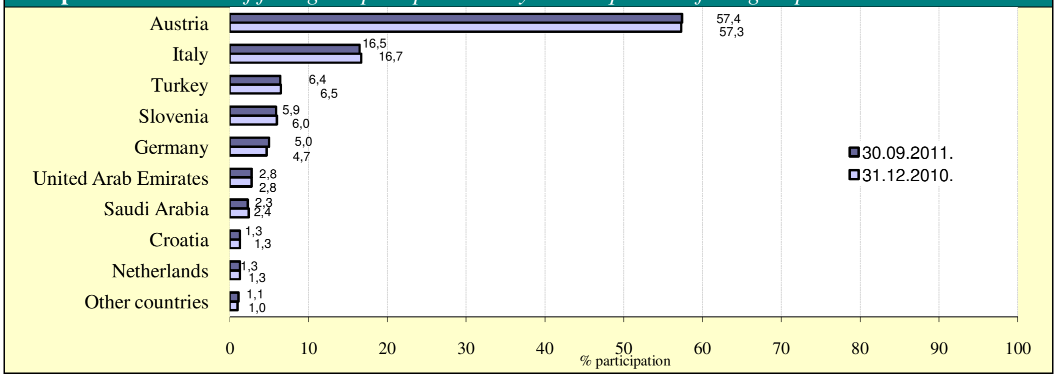
**Graph 1:** *Structure of foreign capital per country*




However, if capital correlations are taken into account the structure for foreign capital could be viewed according to the criteria of the parent-bank or the group's headquarter that has majority ownership (directly or indirectly through the group members) of the bank in the Federation of BiH. According to these criteria, the situation also just slightly changed in relation to the end of 2010: banking group and banks from Austria with participation of 57,4%, banks from Italy with participation of 16,5%, while other countries participate below 6,5%.

[1] A bank classification criterion is ownership over banks' share capital.
[2] The ownership structure of banks in the FBiH, as of 30.09.2011., resulted from received documentation and registrations at authorized courts (changes in capital and shareholders structure).
[3] State ownership refers to domestic state capital of BiH.

**Graph 2:** *Structure of foreign capital per country – headquarter of the group*[4]



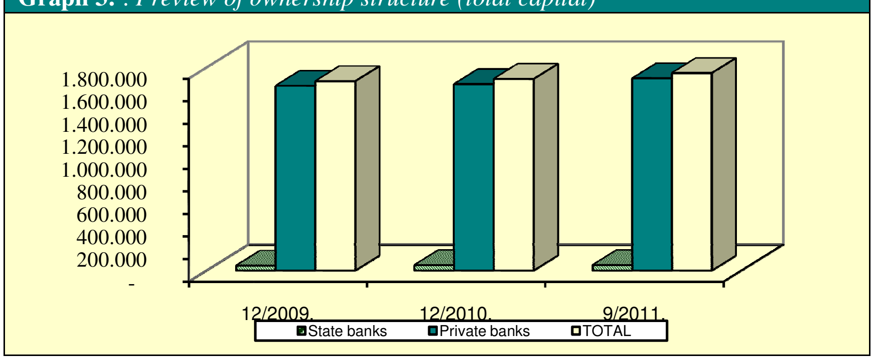

The ownership structure could be viewed from the aspect of financial indicators, which is based on the value of total capital[5].

-in 000 KM-

**Table 1:** *Ownership structure by total capital*

| BANKS | 31.12.2009. | | 31.12.2010 | | 30.09.2011. | | RATIO | |
|---|---|---|---|---|---|---|---|---|
| | | | | | | | 3/2 | 4/3 |
| 1 | 2 | | 3 | | 4 | | 5 | 6 |
| State banks | 41.736 | 2% | 46.586 | 3% | 47.054 | 3% | 112 | 101 |
| Privates banks | 1.635.962 | 98% | 1.650.039 | 97% | 1.702.128 | 97% | 101 | 103 |
| TOTAL | 1.677.698 | 100% | 1.696.625 | 100% | 1.749.182 | 100% | 101 | 103 |

**Graph 3:** : *Preview of ownership structure (total capital)*




Analysis of participation by state, private and foreign capital in the share capital of banks shows more precise picture of the capital ownership structure in banks of the Federation of BiH.

- in 000 KM-

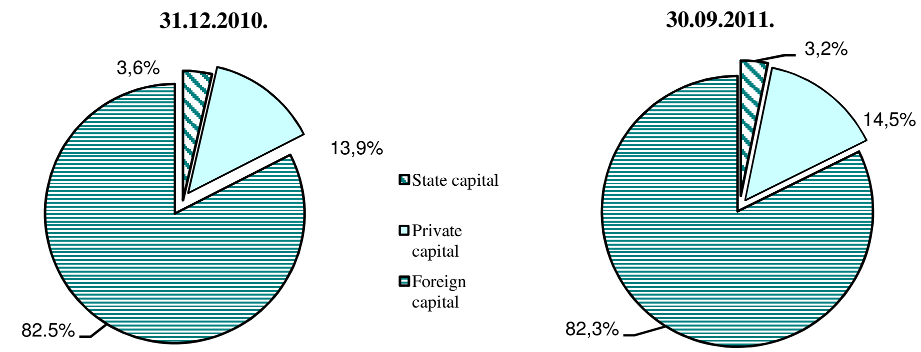
**Table 2:** *Ownership structure by participation of state private and foreign capital*

| SHARE CAPITAL | 31.12.2009. | | 31.12.2010. | | 30.09.2011. | | INDEX | |
|---|---|---|---|---|---|---|---|---|
| | Amount | Participation % | Amount | Participation % | Amount | Participation % | 5/3 | 7/5 |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| State capital | 41.860 | 3,6 | 41.860 | 3,6 | 38.072 | 3,2 | 100 | 91 |
| Private capital (residents) | 153.365 | 13,1 | 163.074 | 13,9 | 173.662 | 14,5 | 106 | 106 |

[4] Apart from the country of the headquarters of the parent-group whose members are the banks from the F BiH, the countries of all other shareholders of the banks from the F BiH are also included.
[5] Information from balance sheet – FBA schedule: shareholder's capital, premium issue, undistributed profit and reserves, and other capital (financial results of current period).

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Foreign capital (nonresident) | 975.943 | 83,3 | 968.363 | 82,5 | 981.838 | 82,3 | 99 | 101 |
| TOTAL | 1.171.168 | 100,0 | 1.173.297 | 100,0 | 1.193.572 | 100,0 | 100 | 102 |

**Graph 4**: *Ownership structure (share capital)*




The share capital of banks in the Federation of BiH, in nine months of 2011., was higher by 20,3 million KM or 1,7% in relation to 31.12.2010. The structure of the shareholder's capital slightly changed: the state capital decreased by 3,8 million KM, private capital (resident) increased by 10,6 million KM, and private (nonresident) capital increased by 13,5 million KM.

Analysis of the banks' ownership structure shows, in more details, from the aspect of share capital, the changes and trends in the banking system of the FBiH, and especially the changes of the ownership structure.

Participation of the state capital in total share capital, as of 30.09.2011., was 3,2%, and it decreased by 0,4% in relation to 31.12.2010.

Participation of private capital (residents) in total share capital of 14,5% is representing a 0,6 per cent increase in comparison to the end of 2010. Nominal increase of 10,6 million KM was based on the increase in trading with state owned capital in banks, and slightly due to trading with non-residents, in seven banks in the net amount of 5,7 million KM, while the shareholders capital of one bank increased by 2,3 million KM, and in another bank the capital (residents) increased by 2,6 million KM through emission of common shares.

Participation of foreign capital (nonresidents) in total share capital has increased by 13,5 million KM or 0,2% percent points in comparison to 31.12.2010. This increase was due to the new emissions of the shares in three banks, and in small part based on the turnover with residents in nine banks.

As of 30.09.2011., the market share of banks with majority foreign ownership was a high 91,1%, of banks with majority domestic private capital was 7,6%, and the share of banks with majority state capital was 1,3%.

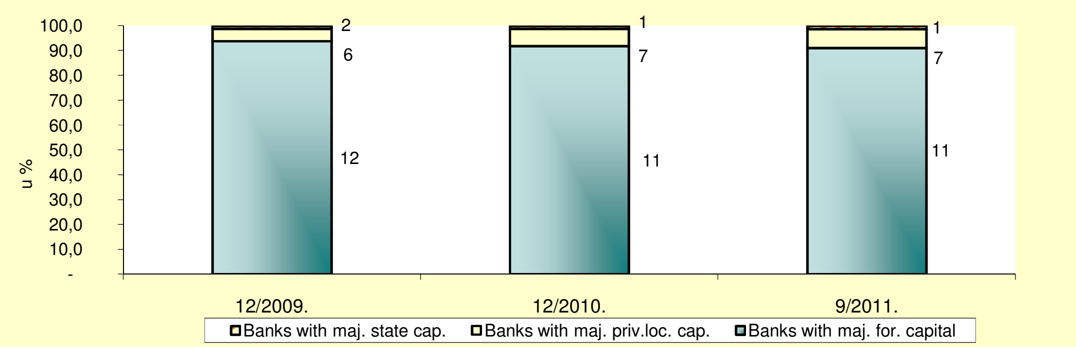
- in %-

**Table 3:** *Market share of banks per ownership type (majority owned capital)*

| BANKS | 31.12.2009. | | | 31.12.2010. | | | 30.09.2011. | | |
|---|---|---|---|---|---|---|---|---|---|
| | No. of banks | Partic. in total capital | Partic. in total assets | No. of banks | Partic. in total capital | Partic. in total assets | No. of banks | Partic. in total capital | Partic. In total assets |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Banks with majority state capital | 2 | 2,5 | 1,1 | 1 | 2,7 | 1,1 | 1 | 2,7 | 1,3 |
| Banks with majority private domestic capital | 6 | 10,7 | 5,0 | 7 | 12,2 | 7,0 | 7 | 11,9 | 7,6 |
| Banks with majority foreign capital | 12 | 86,8 | 93,9 | 11 | 85,1 | 91,9 | 11 | 85,4 | 91,1 |
| TOTAL | 20 | 100,0 | 100,0 | 19 | 100,0 | 100,0 | 19 | 100,0 | 100,0 |

**Graph 5:** *Market share per ownership type*




## 1.3. Employees

As of 30.09.2011., there were a total of 7.400 employees in the banks of the Federation of BiH, of that number 2% is in the banks with a majority state capital and 98% in private banks.

**Table 4:** *Bank employees in the FBiH*

| B A N K S | NUMBER OF EMPLOYEES | | | | | | INDEX | |
|---|---|---|---|---|---|---|---|---|
| | 31.12.2009. | | 31.12.2010. | | 30.09.2011. | | 3/2 | 4/3 |
| 1 | 2 | | 3 | | 4 | | 5 | 6 |
| State banks | 231 | 3% | 180 | 2% | 178 | 2% | 78 | 98 |
| Private banks | 7.425 | 97% | 7.208 | 98% | 7.222 | 98% | 97 | 100 |
| TOTAL | 7.656 | 100% | 7.388 | 100% | 7.400 | 100% | 97 | 100 |
| Number of banks | 20 | | 19 | | 19 | | 95 | 100 |

The decreasing trend of the numbers of employees as one of the consequences of the adverse effects of the economic crisis on the banking sector in the second and third quarter of 2011., was stopped, recorded was an increase in the number of employees in the second quarter by 14, in the third by 35, which is in total, for the nine months of 2011., an increase of 0,2% or 12 employees.

**Table 5:** *Qualification structure of employees*

| EDUCATION | NUMBER OF EMPLOYEES | | | | | | INDEX | |
|---|---|---|---|---|---|---|---|---|
| | 31.12.2009. | | 31.12.2010. | | 30.09.2011. | | 4/2 | 6/4 |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| University qualifications | 3.104 | 40,5% | 3.234 | 43,8% | 3.366 | 45,5% | 104 | 104 |
| Two-year post secondary school qualifications | 774 | 10,1% | 696 | 9,4% | 700 | 9,5% | 90 | 101 |
| Secondary school qualifications | 3.719 | 48,6% | 3.406 | 46,1% | 3.294 | 44,5% | 92 | 97 |
| Other | 59 | 0,8% | 52 | 0,7% | 40 | 0,5% | 88 | 77 |
| TOTAL | 7.656 | 100,0% | 7.388 | 100,0% | 7.400 | 100,0% | 97 | 100 |

The trend of improvement of the qualification structure of employees through the increase of participation of employees with higher education also continued in the three quarters of 2011., and the negative of the decrease of the number of employees, mostly with high school diploma, had a positive impact on the change of the qualification structure.

One of the indicators influencing an evaluation of performance of a respective bank and the banking system, and the banking system, is effectiveness of employees and it is shown as a ratio of the assets and the number of employees, that is, the amount of assets per an employee. The higher ratio, the better the performance effectiveness of both the bank and the entire system

**Table 6:** *Assets per employee*

| BANKS | 31.12.2009. | | | 31.12.2010. | | | 30.09.2011. | | |
|---|---|---|---|---|---|---|---|---|---|
| | No. of empl. | Assets (000 KM) | Assets per empl. | No. of empl. | Assets (000 KM) | Assets per empl. | No. of empl. | Assets (000 KM) | Assets per empl. |
| State | 231 | 161.619 | 700 | 180 | 167.263 | 929 | 178 | 198.683 | 1.116 |
| Private | 7.425 | 15.074.741 | 2.030 | 7.208 | 14.908.434 | 2.068 | 7.222 | 15.056.677 | 2.085 |
| TOTAL | 7.656 | 15.236.360 | 1.990 | 7.388 | 15.075.697 | 2.041 | 7.400 | 15.255.360 | 2.062 |

At the end of the reviewed period, there was a two million KM assets per employee on the level of the banking system. The slight increase of the indicators for the majority private capital is a consequence of the increase of assets in 2011.

**Table 7:** *Assets per employee by groups*

| Assets (000 KM) | 31.12.2009. | 31.12.2010. | 30.09.2011. |
|---|---|---|---|
| | Number of banks | Number of banks | Number of banks |
| Up to 500 | 1 | 0 | 0 |
| 500 to 1.000 | 8 | 7 | 4 |
| 1.000 to 2.000 | 5 | 6 | 9 |
| 2.000 to 3.000 | 5 | 5 | 5 |
| Over 3.000 | 1 | 1 | 1 |
| TOTAL | 20 | 19 | 19 |

The analytical indicators for individual banks are within the range from 602 thousand KM to 3,6 million KM of assets per employee. Six banks have this indicator better than what it is for the sector, and for three largest banks in the system it is over the amount of 2,4 million KM.

## 2. FINANCIAL INDICATORS OF BANKS' PERFORMANCES

Examination of banks based on reports is performed through using the reports prescribed by the FBA and the reports of other institutions creating a database constructed from three sources of information:

1. Information on balance sheet for all banks submitted monthly, including quarterly attachments, containing more detailed information on funds, loans, deposits and off-balance sheet items, and some general statistic information,
2. Information on bank solvency, data on capital and capital adequacy, asset classification, concentrations of certain types of risks, liquidity position, foreign exchange exposure, based on the reports prescribed by the FBA,
3. Information on performance results of banks (income statement – FBA format) and cash flow reports submitted to the FBA quarterly.

Aside from the mentioned standardized reports, the database includes the information obtained from additional reporting requirements prescribed by the FBA in order to have the best conditions for monitoring and analysis of banks' performance in the Federation of BiH. The database also includes audit reports of financial statements of banks prepared by independent auditor, as well as all other information relevant to the assessment of performances of individual banks and the entire banking system.

In accordance with the provisions of Law on Opening Balance Sheet of Banks, banks with majority state owned capital have to report to the FBA "full" balance sheet divided into: passive, neutral and active sub-balance sheet. In order to obtain realistic indicators of banks' performance in the Federation of BiH, all further analysis of the banking system will be based on the indicators from the active sub-balance sheet of banks with majority state owned capital[6].

## 2.1. Balance Sheet

Aggregate balance sheet of the banking sector, as of 30.09.2011., amounted to 15,26 billion KM, which is by 1% or 180 million KM more than at the end of 2010. It is evident that the impact of the financial crises on the banking sector in FBiH is still strong, the development and growth of the overall sector has been stopped for a longer period of time, however the slight growth in the nine months of 2011., can still be evaluated as positive, since the negative trends from the period after the crises up to the first half of 2010 have been significantly alleviated.

**Table 8:** *Balance Sheet*

| DESCRIPTION | AMOUNT ( IN 000 KM ) | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 31.12.2009. | | 31.12.2010. | | 30.09.2011. | | RATIO | |
| | AMOUNT | Partic. % | AMOUNT | Partic. % | AMOUNT | Partic. % | 3/2 | 4/3 |
| 1 | 2 | | 3 | | 4 | | 5 | 6 |
| **ASSETS:** | | | | | | | | |
| Cash funds | 4.782.301 | 27,9 | 4.443.614 | 29,5 | 4.161.321 | 27,3 | 93 | 94 |
| Securities[7] | 119.157 | 0,1 | 375.252 | 2,4 | 461.074 | 3,0 | 315 | 123 |
| Placements to other banks | 111.019 | 0,6 | 145.007 | 1,0 | 278.418 | 1,8 | 131 | 192 |
| Loans | 9.796.800 | 69,2 | 9.981.911 | 66,2 | 10.304.969 | 67,5 | 102 | 103 |
| Loan loss provisions (LLP) | 458.803 | 2,5 | 635.792 | 4,2 | 716.029 | 4,7 | 139 | 113 |
| Loans – net value (loans minus LLP) | 9.337.997 | 66,7 | 9.346.119 | 62,0 | 9.588.940 | 62,8 | 100 | 103 |
| Business premises and other fixed assets | 528.910 | 3,1 | 552.764 | 3,7 | 543.997 | 3,6 | 105 | 98 |
| Other assets | 356.976 | 1,6 | 212.941 | 1,4 | 221.610 | 1,5 | 60 | 104 |
| **TOTAL ASSETS** | **15.236.360** | **100,0** | **15.075.697** | **100,0** | **15.255.360** | **100,0** | **99** | **101** |
| **LIABILITIES** | | | | | | | | |
| **LIABILITIES** | | | | | | | | |
| Deposits | 11.045.868 | 69,4 | 11.232.830 | 74,5 | 11.392.516 | 74,7 | 102 | 101 |
| Borrowings from other banks | 3.089 | 0,0 | 7.000 | 0,0 | 2.000 | 0,0 | 227 | 29 |
| Loan Commitments | 1.771.978 | 14,4 | 1.403.451 | 9,3 | 1.344.522 | 8,8 | 79 | 96 |
| Other liabilities | 737.727 | 5,3 | 735.791 | 4,9 | 767.140 | 5,0 | 100 | 104 |
| **CAPITAL** | | | | | | | | |
| Capital | 1.677.698 | 10,9 | 1.696.625 | 11,3 | 1.749.182 | 11,5 | 101 | 103 |
| **TOTAL LIABILITIES (LIABILITIES AND CAPITAL)** | **15.236.360** | **100,0** | **15.075.697** | **100,0** | **15.255.360** | **100,0** | **99** | **101** |

**Table 9:** *Assets of banks based on the ownership structure*

[6] Some state banks in their "full balance sheet" report passive and neutral items, which will be taken over by the state upon finalization of the privatization process. As of 30.09.2011., these items amounted to KM 654 million.

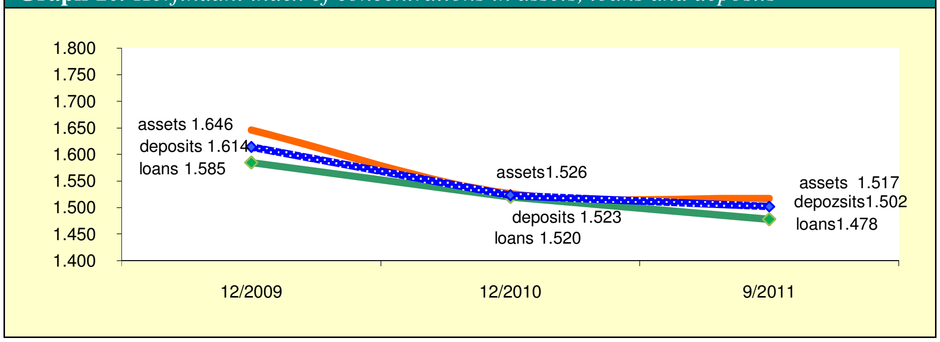
[7] Trading securities and securities held to maturity.

| BANKS | 31.12.2009. | | | 31.12.2010. | | | 30.09.2011. | | | RATIO | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | No. banks | Assets (000 KM) | | No. banks | Assets (000 KM) | | No. banks | Assets (000 KM) | | 5/3 | 7/5 |
| 1 | 2 | 3 | | 4 | 5 | | 6 | 7 | | 8 | 9 |
| State | 2 | 161.619 | 1% | 1 | 167.263 | 1% | 1 | 198.683 | 1% | 103 | 119 |
| Private | 18 | 15.074.741 | 99% | 18 | 14.908.434 | 99% | 18 | 15.056.677 | 99% | 99 | 101 |
| TOTAL | 20 | 15.236.360 | 100% | 19 | 15.075.697 | 100% | 19 | 15.255.360 | 100% | 99 | 101 |

The analytical data on the fluctuations of the banks' assets indicate that 12 realized growth, while in the remaining nine banks the level of assets declined, and the decreasing rates were between 1% and 5%.

Indicator of concentrations in the three most significant segments of banking performance, in assets, loans and deposits is the value of the Herfindahl index[8].

**Graph 10:** *Herfindahl index of concentrations in assets, loans and deposits*




At the end of the ninth month of 2011, the Herfindahl index in all three relevant categories (loans, deposits and assets) recorded insignificant changes in value: assets 1.517 units, loans 1.478 and deposits 1.502, indicating a moderate concentration[9]. In comparison to the end of 2010, all three indicators decreased: for assets nine, and for deposits 21 and loans 42 units.

Another indicator of concentration in the banking system is the ratio of market concentration, that is the concentration rate[10] (hereinafter: CR), which indicates the total market participation of the largest institutions in the system per relevant chosen categories: assets, loans and deposits. The CR5 decreased for all three categories: market participation from 75,5 to 75,2%, for loans from 77,6% to 76,7%, and for deposits from 75,8 to 74,6%. In the past two years the CR value has slightly declined in all three categories, but there is still an evident dominance of five largest banks in the system that "hold" approximately 75% of the market, loans and deposits

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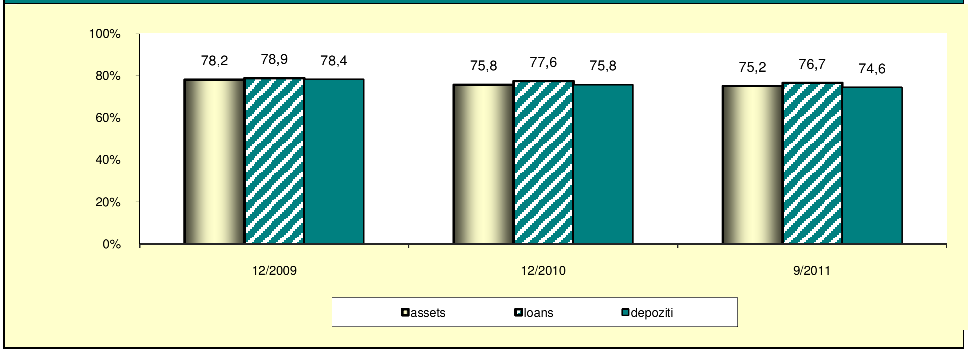
[8] It is also called the Hirschmann-Herfindahl index or HHI as calculated in the formula $HI = \sum_{j=1}^{n} (S)_j^2$, representing the sum of square of percentage shares of concrete values (e.g. assets, deposits, loans,…) of all market participants in the system. We should mention that the index is not linearly increasing, and the value of e.g. 3000 does not mean the concentration in the system is 30%. Hypothetically, if there is only one bank in the system, the HHI would be maximum at 10000.

[9] If the HHI value is below 1000, the opinion is that there is no concentration in the market; for the index value between 1000 and 1800 units, concentration in the market is moderate; and if the HHI value exceeds 1800, it indicates high concentration.

[10] Engl.: concentration ratio (CR), assigned to the number of institutions inlcuded in the calculation.

**Graph 7:** *Concentration rates for the five largest banks-CR5: assets, loans and deposits*




The banking sector could be analyzed from the aspect of several groups established according to the asset size[11]. The minor changes in relation to the end of 2010 refer to the number of banks and participation of certain groups which is a result of changes of assets in several banks.

Two banks from Group I (assets higher than three billion KM) still have a high market participation of almost 50%, and if included are two banks from the group II (with assets between one and two billion) the participation of four largest banks is 69,2%. The remaining 15 banks 'hold' 30% of the market, of which three banks from the group III (assets between 500 million KM and one billion KM) have a participation of 16,3%, while the group IV, with the biggest number of banks – nine (assets between 100 and 500 million KM) recorded the biggest change – its participation increased from 12,3% to 13,2%. The last V group (three banks with asses lower than 100 million KM), maintained the low participation of 1,3%.

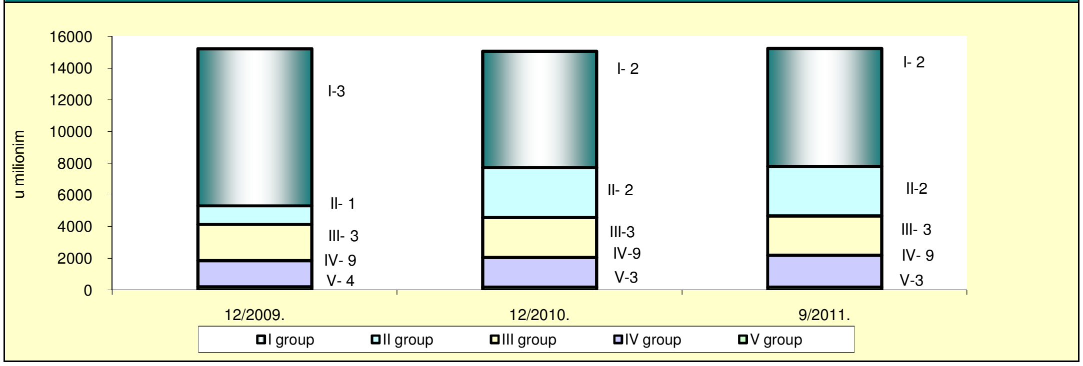
The following table presents a preview of amounts and participations of individual groups of banks in total assets by periods (amounts presented in KM millions).

**Table 10:** *Participation of individual groups of banks in total assets through periods*

| ASSETS | 31.12.2009. | | | 31.12.2010. | | | 30.09.2011. | | |
|---|---|---|---|---|---|---|---|---|---|
| | Amount | Partic. % | No. of banks | Amount | Partic. % | No. of banks | Amount | Partic. % | No. of banks |
| I- Over 2.000 | 9.912 | 65,1 | 3 | 7.348 | 48,8 | 2 | 7.443 | 48,8 | 2 |
| II- 1000 to 2000 | 1.165 | 7,6 | 1 | 3.146 | 20,9 | 2 | 3.122 | 20,4 | 2 |
| III- 500 to 1000 | 2.293 | 15,1 | 3 | 2.521 | 16,7 | 3 | 2.483 | 16,3 | 3 |
| IV- 100 to 500 | 1.648 | 10,8 | 9 | 1.862 | 12,3 | 9 | 2.008 | 13,2 | 9 |
| V- Under 100 | 218 | 1,4 | 4 | 199 | 1,3 | 3 | 199 | 1,3 | 3 |
| TOTAL | 15.236 | 100,0 | 20 | 15.076 | 100,0 | 19 | 15.255 | 100,0 | 19 |

[11] Banks are divided into five groups depending on the assets size.

**Graph 8:** *Participation of individual groups of banks in total assets by periods*



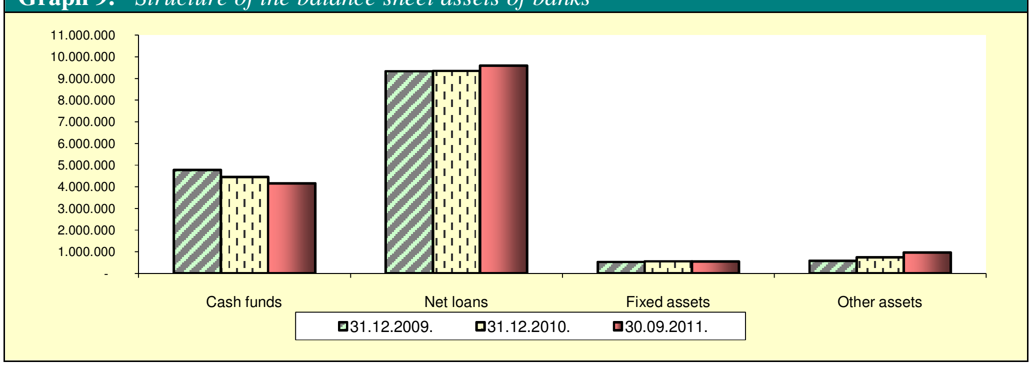

In the three quarters of 2011, the aggregate balance sheet realized a growth of 1% or 180 million KM. The most important liability items: deposits, credit liabilities and total capital had minimal changes, that is the deposits realized a growth (1% or 160 million KM) and total capital (3% or 53 million KM), while the loan liabilities decreased by 4% or 59 million KM.

In the assets, cash funds (in the amount of 4,2 billion KM) are lower by 6% or 282 million than in comparison to the end of 2010, mostly due to increase of loan placements by 3% or 323 million KM.

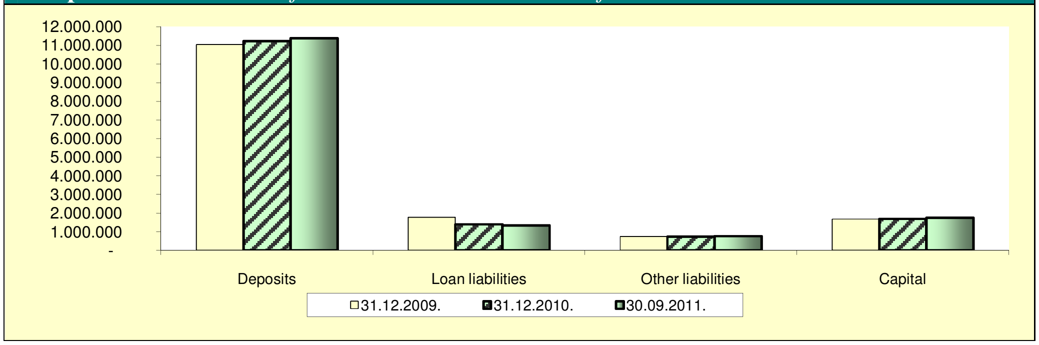
A slight credit growth from the last three quarters of 2010., and two quarters of 2011., continued in the third quarter, which is encouraging and it is an indicator of intensifying the credit activities of banks. After the increase of 3% or 323 million KM, the loans as of 30.09.2011 reached the amount of 10,3 billion KM.

The following table and graph present the structure of the most significant balance sheet positions of banks.

**Graph 9:** *Structure of the balance sheet assets of banks*



**Graph 10: :** *Structure of the balance sheet liabilities of banks*




In the structure of banks' balance sheet, deposits in the amount of 11,4 billion KM and participation of 74,7% are still the dominant source of financing for banks in the Federation of BiH. After a decrease of 4%, the loan obligations, in the amount of 1,34 billion KM, decreased its participation from 9,3% to 8,8%, while the capital participation, which as of 30.09.2011 was 1,75 billion KM, increased from 11,3% to 11,5.

The structure of assets, as well as the structure of sources, had slight changes related to two key assets items: increased participation of loans from 66,2% to 67,5% and a decrease of cash funds from 29,5% to 27,3%

- in 000 KM-

**Table 11:** *Banks' cash funds*

| CASH FUNDS | 31.12.2009. | | 31.12.2010. | | 30.09.2011. | | INDEX | |
|---|---|---|---|---|---|---|---|---|
| | Amount | Partic. % | Amount | Partic. % | Amount | Partic. % | 4/2 | 6/4 |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| Cash | 355.419 | 7,4 | 370.414 | 8,3 | 347.082 | 8,3 | 104 | 94 |
| Reserve accounts with CBBiH | 2.455.505 | 51,4 | 2.592.920 | 58,4 | 2.335.361 | 56,1 | 106 | 90 |
| Accounts with deposit institutions in BiH | 441 | 0,0 | 670 | 0,0 | 11.699 | 0,3 | 152 | 1746 |
| Accounts with deposit institutions abroad | 1.970.473 | 41,2 | 1.479.322 | 33,3 | 1.466.789 | 35,3 | 75 | 99 |
| Cash funds in collection process | 463 | 0,0 | 288 | 0,0 | 390 | 0,0 | 62 | 135 |
| TOTAL | 4.782.301 | 100,0 | 4.443.614 | 100,0 | 4.161.321 | 100,0 | 93 | 94 |

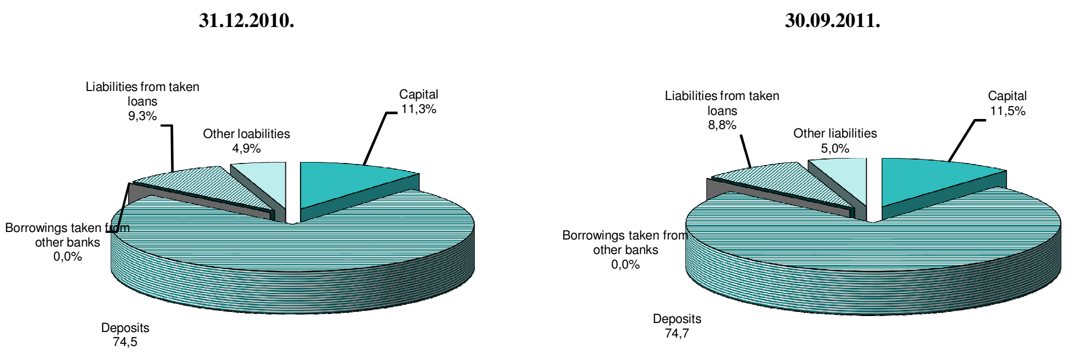
Cash funds of the banks on the reserve accounts of CBBiH, in the nine months of 2011, decreased by 10% or 258 million KM, and were 2,34 billion KM or 56,1% of total cash funds as of 30.09.2011., representing the participation decrease of 2,3 per cent in relation to the end of 2010. Banks' funds on the accounts with the depository institutions abroad have decreased by 1% or 13 million KM, amounting to 1,47 billion KM or 35,3% of total cash funds (33,3% at the end of 2010). As of 30.09.2011., the banks have had cash on hand and in vaults in the amount of 347 million KM, representing 8,3% of total cash funds.

The listed fluctuations had a significant impact on the change of the currency structure of the cash funds: the domestic currency participation in the reviewed period decreased from 63,7% to 62,3%, while the participation of funds in foreign currency has increased by the same amount of change.

## 2. 1. 1. Liabilities

Structure of liabilities (liabilities and capital) in the balance sheet of banks, as of 30.09.2011. is presented in the following graph:

**Graph 11:** *Liabilities structure of banks*




In the three quarters of 2011, there were minor changes in participation of the two most important banks' financing sources: deposits and credit obligations, that is an increase of deposit participation from 74,5% to 74,7%, and decrease of credit liabilities from 9,3% to 8,8%.

Deposits participating with 74,7% or 11,39 billion KM still represent the most significant funding source of banks in the Federation of BiH. Second source, per its size are credit funds in the amount of 1,34 billion KM obtained by banks mostly through the debt with foreign financial institutions. During the last two years, due to the impact of the financial and economic crises, the banks had far less lending from abroad, and with the payment of the past due liabilities these sources decreased significantly. In the reviewed period of 2011., the downfall was 4% or 59 million KM. If subordinate debts of 142 million KM, which were withdrawn by banks to strengthen capital base and capital adequacy, are added to credit liabilities, then the participation of total credit funds in the sources would be 9,8% .

Capital, as of 30.09.2011, was 1,75 billion KM, which is by 3% or 53 million KM higher than at the end of 2010, and the growth was realized exclusively on the basis of the current financial result-profit and additional capitalization of three banks.

As of 30.09.2011., the highest bank commitments were towards the following creditors (seven of total 40), representing 71% of total credit commitments: European Investment Bank (EIB), Central Eastern European Finance Agency (CEEFA), EBRD, European fund for Southeast Europe (EFSE), UniCredit Bank Austria AG, ComercBank AG Frankfurt, Council of Europe Development Bank.

According to the data submitted by banks, out of total deposits as of 30.09.2011., only 6,3% were deposits collected by organizational units of banks from the Federation of BiH operating in Republic Srpska and Brcko District.

- in 000 KM-

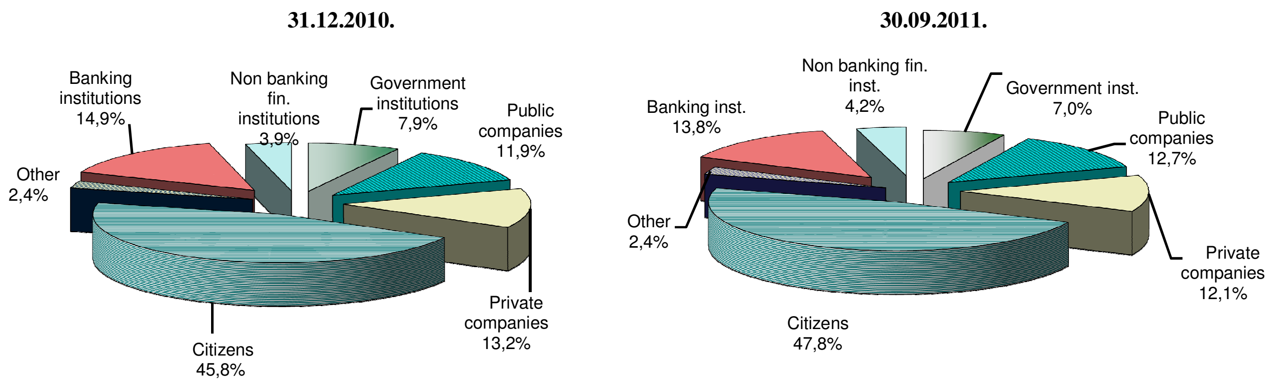
**Table 12:** *Deposit structure by sectors*[12]

| DEPARTMENTS | 31.12.2009. | | 31.12.2010. | | 30.09.2011. | | RATIO | |
|---|---|---|---|---|---|---|---|---|
| | Amount | Partic. % | Amount | Partic. % | Amount | Partic. % | 4/2 | 6/4 |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| Governmental institutions | 839.926 | 7,6 | 891.638 | 7,9 | 800.312 | 7,0 | 106 | 90 |

[12] Information from the attached form BS-D, submitted by banks with balance sheet - FBA format each quarter.

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Public enterprises | 1.400.839 | 12,7 | 1.332.748 | 11,9 | 1.443.800 | 12,7 | 95 | 108 |
| Private enterprises and assoc. | 1.403.465 | 12,7 | 1.487.509 | 13,2 | 1.381.692 | 12,1 | 106 | 93 |
| Non-profit. organizations | 2.120.143 | 19,2 | 1.674.576 | 14,9 | 1.574.508 | 13,8 | 79 | 94 |
| Banking institutions | 509.769 | 4,6 | 432.045 | 3,9 | 483.661 | 4,2 | 85 | 112 |
| Citizens | 4.506.881 | 40,8 | 5.144.607 | 45,8 | 5.433.301 | 47,8 | 114 | 106 |
| Other | 264.845 | 2,4 | 269.707 | 2,4 | 275.242 | 2,4 | 102 | 102 |
| TOTAL | 11.045.868 | 100,0 | 11.232.830 | 100,0 | 11.392.516 | 100,0 | 102 | 101 |

**Graph 12:** *Deposit structure by sectors*




In the reviewed period of 2011, there were minor changes in the deposit sector structure, which on one side, are a result of decrease of funds of private companies, government and banking institutions, and on the other hand, growth of deposits of citizens and public companies.

Deposits of the citizens sector continued their increase in 2011., and realized a growth rate of 6% or 289 million KM, with a note that in the third quarter the growth was 157 million KM. The deposits of this sector with the amount of 5,43 billion KM and participation of 47,8% in total deposits still are the largest financing source for banks in F BiH

The deposits of the banking institutions, which are the second highest source in the deposit potential of the sector, in the observing period decreased by 6% or 100 million KM and as of 30.09.2011., were 1,57 billion KM, which is 13,8% of total deposits. These funds are by 230 million KM higher than the credit liabilities (at the end of 2010 the difference was 271 million KM), which, after the deposits are the second most important financing source for banks in FBiH. From the listed data it can be concluded that the debt abroad of the banks in FBiH significantly decreased, especially the deposit funds of the parent groups. Since the same decreasing trend is present with the loan liabilities, the banks are again faced with the problem of maintaining the maturity match, which is due to the unfavorable maturity of the local deposit funds, therefore the banks have to find and secure a better quality sources of funds in regard to maturity, in order to continue the growth of the loan placements from the last several months.

It should be emphasized that 96% or 1,51 billion KM of banking institutions' deposits refers to deposits of banks-members of groups (primarily shareholders). Financial support of the groups is present in nine banks in the Federation of BiH, with a concentration on three large banks (81%), with only one bank representing 40% of total deposits received from the group. In this manner, the domestic banks-members of the groups receive financial support and have secured inflow of new funding sources by the group whose members they are. Under the times of crisis and more difficult access to money market and new funds, as well as the increase of liquidity risk as result of deterioration in collection of loans and increase of nonperforming claims as well as the unsatisfactory maturity structure of local deposit sources, of special importance is support and willingness of the ‘parent’ to secure further financing of the ‘daughter’ bank in the volume necessary for the planned volume of operations, especially growth of the credit placements, as well as maintaining satisfactory liquidity positions of the bank. If credit liabilities and subordinate debts items in supplementary capital) are added to these funds, the financial support the banks receive from their groups becomes higher (in ten banks), amounting to 2,12 billion KM or 13,9% of total liabilities of the banking sector as of 30.09.2011 (in the total deposits the group funds have a participation of 13,3%, and in total liabilities 33,1% are loan liabilities towards the group). In comparison to the end of 2010, these funds were reduced by 160 million KM or 7% (deposits decreased by 104 million KM or 6,3%, credit liabilities by 8% or 40 million KM and subordinated loans by 10% or 18 million KM).

Under the support of IMF and other financial institutions, the FBA has been involved in activities related to signing of the Memorandum of Understanding with parent-banks from the European Union countries whose daughter-banks operate in the territory of BiH, the so-called “Vienna Initiative”, by which the parent banks have taken the obligation to maintain the exposure in Bosnia and Herzegovina at the level from 31.12.2008., during the IMF program ( 2009 -2012), taken into account the availability of adequate credit possibilities in BiH within the defined good practices for managing the credit risk, capital and liquidity. Since, due to the economic crises, the banks’ credit activities have significantly decreased, which resulted with high liquidity, as well as the good capitalization of almost all banks in FBiH which parent banks signed the “Vienna Initiative”, in 2011 the trend of the decreasing exposure from the previous year continued in the deposit sources segment on the basis of the return of portions of deposit funds before the maturity. Once again emphasized should be the importance of the continuing financial support of the group, primarily the “parent”, especially in the banks which core sources were deposits and credit funds from the “parent” bank or the group.

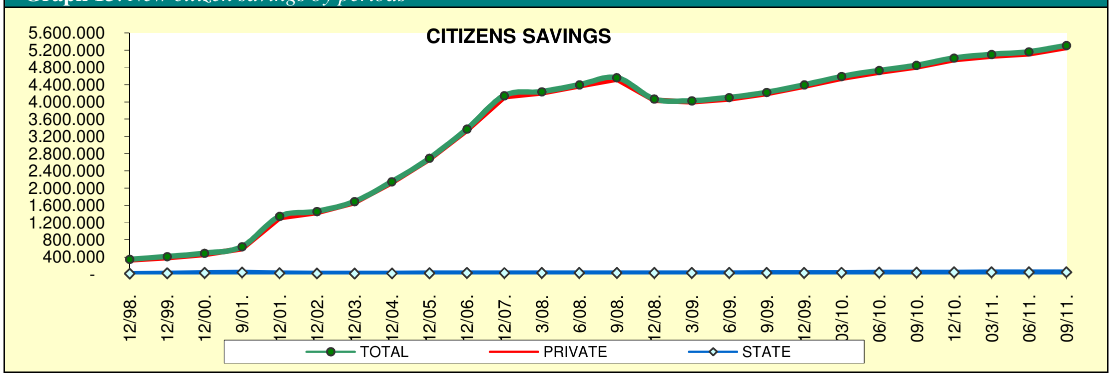
Deposits of other sectors had minor changes: the private enterprises' deposits, after the growth of 8% or 111 million KM, as of 30.09.2011, amounted to 1,44 billion KM, while the participation increased from 11,9% to 12,7%. The deposits of private companies, after the significant decline in the first two quarters of 2011, of 11%, which is a high 169 million KM, in the third quarter recorded an incline of 5% or 63 million KM. Thus, the deposits of this sector, for the nine months decreased by 7% or 106 million KM and as of 30.09.2011., with the amount of 1,38 billion KM had a participation of 12,1% which presents a decrease by 1,1%. Deposits of government institutions, after a decline of 10% or 91 million KM, at the end of the third quarter of 2011 were 800 million KM, which is 7,0% of total deposits. Relatively significant changes in the deposits of the government institutions (the downfall) and public companies (the growth) are the result of separation and transfer of funds of around 90 million KM from the account of the Federal Ministry of finance to the account of one public company.

Currency structure of deposits, at the end of observing period remained unchanged: deposits in foreign currencies (with the dominant participation of EURO) in the amount of 6,4 billion KM participated with 56% and deposits in domestic currency in the amount of five billion KM participated with 44%.

Saving deposits, as the most significant segment of deposits and financial potential of banks, maintained the positive growth trend and in the three quarters of 2011 with a growth rate of 5,8% or 287 million KM (just in the third quarter the growth was 144 million KM< which is 50% of the total growth for the nine months of 2011), amounted to 5,26 billion KM as of 30.09.2011., which is the highest amount so far and by 731 million KM or 16% higher than the level of savings as of 30.09.2008., which was the highest amount up to the crises.

| **Table 13:** *New citizen savings by periods* | | | | | |
|---|---|---|---|---|---|
| **BANKS** | **AMOUNT ( IN 000 KM )** | | | **RATIO** | |
| | **31.12.2009.** | **31.12.2010.** | **30.09.2011.** | **3/2** | **4/3** |
| 1 | 2 | 3 | 4 | 5 | 6 |
| State | 35.275 | 47.148 | 51.147 | 134 | 108 |
| Private | 4.325.928 | 4.926.361 | 5.209.168 | 114 | 106 |
| TOTAL | 4.361.203 | 4.973.509 | 5.260.315 | 114 | 106 |

**Graph 13**: *New citizen savings by periods*




The largest three banks hold 71% of savings, while participation of six banks has an individual participation of less than 1%, representing only 2,5% of total savings in the system.

Savings deposits in local currency represent 31% and in foreign currency 69% of total savings amount.

| **Table 14: :** *Maturity structure citizen saving deposits by periods* | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **BANKS** | **AMOUNT ( IN 000 KM )** | | | | | | **RATIO** | |
| | **31.12.2009.** | | **31.12.2010.** | | **30.09.2011.** | | **3/2** | **4/3** |
| 1 | 2 | | 3 | | 4 | | 5 | 6 |
| Short term saving deposits | 2.054.197 | 47,1% | 2.581.767 | 51,9% | 2.570.753 | 48,9% | 126 | 100 |
| Long term saving deposits | 2.307.006 | 52,9% | 2.391.742 | 48,1% | 2.689.562 | 51,1% | 104 | 112 |
| TOTAL | 4.361.203 | 100,0 % | 4.973.509 | 100,0 % | 5.260.315 | 100,0 % | 114 | 106 |

The maturity structure of the savings deposits slightly improved. The participation of the long term deposits, after the growth of 12% or 298 million KM, increased from 48,1% to 51,1%, while the short term decreased from 51,9% to 48,9%.

Long term continuous growth and positive trends in the savings segment of banks in the F BiH are a result, on one hand, of the strengthening of safety and stability of the overall banking system, giving the key importance to the existence of functional, effective and efficient banking supervision conducted by the FBA, and, on the other hand, deposit insurance system with the main purpose to increase stability of the banking, that is, financial sector and protection of depositors. In December 2008, with purpose to preserve citizens' trust in safety and stability of the banking system in BiH, the amount of insured deposit increased to KM 20.000. After that there was an initiative to increase the amount of the insured deposit, so as of 01.04.2010., it was increased to 35.000 KM, and all taken measures were directed to decrease the impact of the global economic crises on the banking and economic system of the Federation of BiH and BiH.

As of 30.09.2011., there are 15 banks included in the deposit insurance program in the Federation of BiH (they have a license by the Deposit Insurance Agency in BiH), and according to the submitted data 96,5% of total deposits and 98,4% of total savings are in these banks.

Of the remaining four banks three can not apply to be admitted since they do not qualify with the criteria prescribed by the Deposit Insurance Agency: one due to the existing composite rating, and two because they are under provisional administration. One bank , which upon receiving the new composite rang fulfilled this criterion, should start the procedure of entering the deposit insurance program.

### 2.1.2. Capital – strength and adequacy

**2.1.3.** Capital[13] of banks in the Federation of BiH, as of 30.09.2011., amounted to two billion KM

-in 000 KM-

**Table 15:** *Regulatory capital*

| DESCRIPTION | | 31.12.2009. | | 31.12.2010. | | 30.09.2011. | | RATIO | |
|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | | 3/2 | 4/3 |
| 1 | | 2 | | 3 | | 4 | | 5 | 6 |
| **STATE BANKS** | | | | | | | | | |
| 1. | Core capital before reduction | 44.906 | | 45.431 | | 46.457 | | 101 | 102 |
| 2. | Offsetting items | 3.796 | | 97 | | 77 | | 3 | 79 |
| a) | Core capital (1-2) | 41.110 | 97% | 45.334 | 98% | 46.380 | 98% | 110 | 102 |
| b) | Supplementary capital | 1.294 | 3% | 1.046 | 2% | 1.144 | 2% | 81 | 109 |
| c) | **Capital ( a + b)** | 42.404 | 100% | 46.380 | 100% | 47.524 | 100% | 109 | 102 |
| **PRIVATE BANKS** | | | | | | | | | |
| 1. | Core capital before reduction | 1.708.796 | | 1.839.728 | | 1.908.210 | | 108 | 104 |
| 2. | Offsetting items | 195.208 | | 313.224 | | 368.315 | | 160 | 118 |
| a) | Core capital (1-2) | 1.513.588 | 75% | 1.526.504 | 76% | 1.539.895 | 78% | 10 | 101 |
| b) | Supplementary capital | 506.458 | 25% | 488.940 | 24% | 430.544 | 22% | 101 | 88 |
| **c)** | **Capital ( a + b)** | 2.020.046 | 100% | 2.015.444 | 100% | 1.970.439 | 100% | 97 | 98 |
| | | | | | | | | 100 | |
| **Total** | | | | | | | | | |
| 1. | Core capital before reduction | 1.753.702 | | 1.885.159 | | 1.954.667 | | 108 | 104 |
| 2. | Offsetting items | 199.004 | | 313.321 | | 368.392 | | 157 | 118 |
| a) | Core capital (1-2) | 1.554.698 | 75% | 1.571.838 | 76% | 1.586.275 | 79% | 101 | 101 |
| b) | Supplementary capital | 507.752 | 25% | 489.986 | 24% | 431.688 | 21% | 97 | 88 |
| **c)** | **Capital ( a + b)** | 2.062.450 | 100% | 2.061.824 | 100% | 2.017.963 | 100% | 100 | 98 |

In the three quarters of 2011, capital[14] declined by 2% or 44 million KM in comparison to 2010, while the changes in core and supplementary capital influenced the changes in the structure of regulatory capital. The core capital increased by 1% or 14 million KM, and supplementary capital decreased by 12% or 58 million KM.

The core capital growth is a result in most part of the inclusion of the realized profit for 2010 in the amount of 49 million KM in the retained profit and reserves. After implementation of the legal procedure for adopting and implementing decisions on allocation of the revised profit by the banks' Assembly, the realized profit for 2010 in the amount of 49 million KM (14 banks) was 90% allocated into core capital (one bank directed the profit for a partial coverage of

[13] Regulatory capital as defined by Article 8 and 9 of Decision on Minimum Standards for Capital Management in Banks (Official Gazette of the Federation of BiH, 3/03, 18/03, 53/06, 55/07, 81/07, 6/08).
[17] Data source is the quarterly Report on Capital Positions of Banks (Form 1-Schedule A) regulated by the Decision on Minimum Standards for Managing Capital in Banks.

previous losses) Three banks had allocated a part of profit in the amount of 4,8 million KM into repayment of dividends, and one bank adopted a decision to pay a dividend from the retained earnings in the amount of 157,9 million KM.

In the second and third quarter of 2011, after in the first quarter there was no additional capital from external sources, three banks had additional capital in the amount of 17,6 million KM (10 million KM, four million KM and 3,6 million KM). One bank had increased its shareholders capital by 2,6 million KM through internal additional capitalization (from reserves).

Deductable items (which decrease the core capital) increased by 55 million KM mostly from increase of the current loss (which is 59 million KM), with a simultaneous decrease of intangible property by 3,5 million KM.

Supplementary capital decreased by 58 million KM, with major changes in the structure: the 2010 profit of 52 million KM that was included in the additional capital at the end of 2010, was moved to the core capital,  the subordinate debt (regular payments of the past due liabilities) and items of permanent character decreased by 16,9 million KM, while items of general loan loss provisions increased by 10,5 million KM. During the year the current unaudited profit does not go into the accrual of capital, which also influenced the decrease of supplementary capital.

The noted changes influenced the structure of the regulatory capital, thus the participation of the core capital increased from 76% to 79%, and the supplementary capital decreased from 24% to 21%.

Net capital, as well as regulatory capital, decreased by 2% or 46 million KM, amounting to two billion KM as of 30.09.2011.

The banks' capital level rate is expressed as a ratio of capital and assets and as of  30. 09. 2011., it was 12,6%, by 0,5% less that at end of 2010.

One of the most significant indicators of capital strength and adequacy[15] of banks is capital adequacy ratio calculated as a ratio of net capital and risk weighted assets. As of 30.09.2011., this ratio at the banking system level was 15,3% which is lower by 0,9% than at the end of 2010., due to the decrease of net capital by 2% or 46 million KM and increase of the total risk weighted risks by 3% or 407 million KM. The risk of the risk weighted assets and credit equivalents increased by 383 million KM (from 11,71 billion KM to 12,09 billion KM) mostly due to slight increase of credit activities, off-balance sheet items and placements to other banks, which are items that have risk weight with higher risk level (of 20% - 100%) with a simultaneous decrease of cash funds which the banks have in CBBiH and cash funds, and which risk weight is zero. On the other hand, the risk weighted operating risk (POR) increased by 23 million KM (966 million KM), which all together resulted with the noted increase of the total risk weighted risk. Apart from the listed, not including the current earnings in the accrual of capital during the year has a significant effect. If the current unrevised profit would be included in the  accrual, the capital adequacy ratio would be 15,6%.

At the end of the third quarter of 2011, the participation of risk-weighted assets exposed to credit risk was 93%, and to operating risk 7%.

In process of conducting supervision of operations and financial positions of banks in the FBiH, as regulated by the Law, the FBA issues orders to banks to undertake actions for strengthening

[15] The Law prescribes minimum capital adequacy rate of 12%.

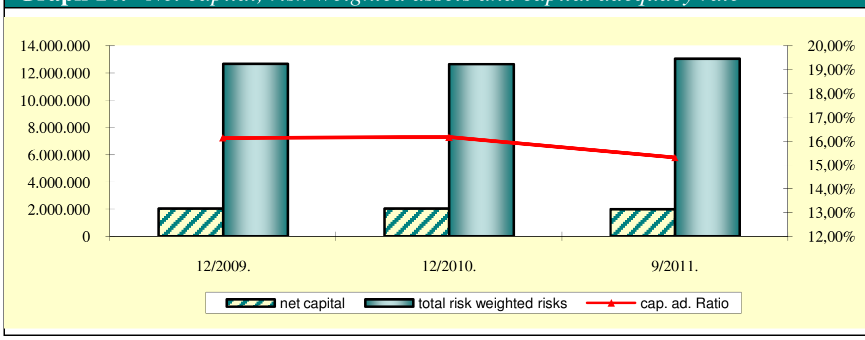
of capital base and provision of adequate capital in order to improve safety of both banks individually and the entire banking system, according to the level and profile of existing and potential exposure to all risks relevant to the banking operations. Under the conditions of economic crisis and the increase of the loan risk caused by the decline of the credit portfolio quality, this request has a priority and that is why the segment of capital is under a continuous enhanced supervision. One of the measures is also a requirement imposed on banks not to distribute the 2010 profit they generated to pay out dividends, but to rather strengthen their capital base, which was accepted by almost all banks.

- 000 KM-

**Table 16:** *Net capital, risk-weighted assets and capital adequacy rate*

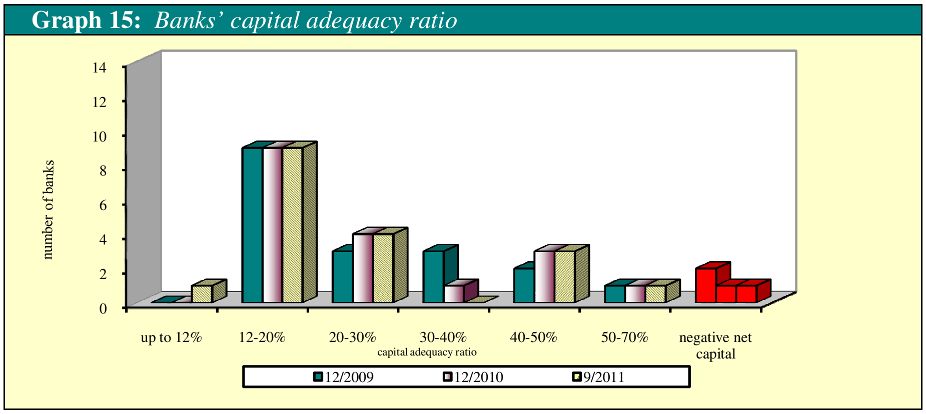
| DESCRIPTION S | 31.12.2009. | 31.12.2010. | 30.09.2011. | RATIO 3/2 | RATIO 4/3 |
|---|---|---|---|---|---|
| 1 | 2 | 3 | 4 | 5 | 6 |
| 1. NET CAPITAL | 2.046.414 | 2.045.886 | 1.999.425 | 100 | 98 |
| 2. RISK WEIGHTED ASSETS AND CREDIT EQUIVALENTS | 11.790.234 | 11.713.116 | 12.096.510 | 99 | 103 |
| 3. POR (RISK WEIGHTED OPERATING RISK) | 882.928 | 942.707 | 965.932 | 107 | 102 |
| 4. TOTAL RISK WEIGHTED RISKS (2+3) | 12.673.162 | 12.655.823 | 13.062.442 | 100 | 103 |
| 5. NET CAPITAL RATE (CAPITAL ADEQUACY) (1/ 4) | 16,1% | 16,2% | 15,3% | 101 | 94 |

**Graph 14:** *Net capital, risk-weighted assets and capital adequacy rate*




Capital adequacy rate of the banking system, as of 30.09.2011., was 15,3%, which is still much more than the minimum prescribed by the law (12%), representing satisfactory capitalization of the entire system and very strong basis and foundation to preserve its safety and stability.

**Graph 15:** *Banks' capital adequacy ratio*



Of total 19 banks in the FBiH, as of 30.09.2011., capital adequacy rate of 17 banks was higher than minimum prescribed by the law of 12%, one bank has the capital adequacy rate under the minimum (10,3%), while another bank, under provisional administration, recorded capital adequacy rate below 12% that is a negative adequacy rate. According to analytical data at the end of the reviewing period in 2011, 11 banks recorded the capital adequacy rate lower than prior year, in the range from 0,5 to 8,6%, seven banks recorded better rate.

Review of capital adequacy rates of 17 banks in comparison to the minimum prescribed by the law of 12% is the following:
- nine banks had the rate between 12,5% and 19,4%
- seven banks had the rate between 20,8% and 41,8%,
- One bank had the rate between of 59,0%.

Further strengthening of capital base will be priority task in majority of banks as it has been the case so far, especially in the largest banks of the system, which is necessary to strengthen stability and safety of both banks and the entire banking system, especially due to changes in business and operating environment under which banks in the Federation operate, because of the global financial crisis expansion to the area of our country and adverse effects this crisis may have on the banking sector and the entire economy of BiH. After the beginning of the crises, due to the deterioration of the loan portfolio and increase of the reserve expenses for loan losses, which had a significant impact on the downfall of the profitability of all banks in the system, the bank's capital has been under increased supervisory review, in order to avoid the endangering the banks' stability and capital base erosion to the level that would jeopardize not only the operations of the banks, but also impact the stability of the total banking system.

### 2.1.3. Assets and asset quality

Decision on Minimum Standards for Loan Risk Management and Assets Classification of Banks determines the criteria for evaluation of bank's exposure to loan risk based on evaluation of their assets quality and adequacy of reserves for loan and other losses according to the risk of placements and balance sheet and off-balance sheet items.

Total assets with off-balance sheet items (assets)[16] of banks in the FBiH as of 30.09.2011., amounted to 18,5 billion KM, and gross assets[17] in the amount of 16 billion KM which is by 2% higher than at the end of 2010.

-in 000 KM-

**Table 17:** *Assets off-balance sheet items and potential loan losses*

| DESCRIPTION | AMOUNT ( in 000 KM ) | | | | | | RATIO | |
|---|---|---|---|---|---|---|---|---|
| | 31.12.2009. | Struct. % | 31.12.2010. | Struct. % | 30.09.2011. | Struct. % | 4:2 | 6:4 |
| 1. | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| Loans | 9.442.600 | 60,1 | 9.414.729 | 59,8 | 9.664.175 | 60,4 | 100 | 103 |
| Interests | 61.797 | 0,4 | 51.348 | 0,3 | 51.096 | 0,3 | 83 | 100 |
| Past due claims | 352.580 | 2,2 | 566.629 | 3,7 | 640.423 | 4,0 | 161 | 113 |
| Claims for paid guarantees | 1.620 | 0,0 | 553 | 0,0 | 371 | 0,0 | 34 | 67 |
| Other placements | 276.693 | 1,8 | 410.797 | 2,6 | 453.938 | 2,9 | 148 | 110 |
| Other assets | 5.581.877 | 35,5 | 5.292.854 | 33,6 | 5.188.271 | 32,4 | 95 | 98 |
| TOTAL ASSETS | 15.717.167 | 100,0 | 15.736.910 | 100,0 | 15.998.274 | 100,0 | 100 | 102 |

[16] Assets defined by Article 2 of Decision on Minimum Standards for Loan Risk Management and Assets Classification of Banks („Official Gazzette of FBiH", number 3/03, 54/04, 68/05).
[17] Data source: Report on classification of balance sheet assets and off-balance sheet items of banks.

| | | | | | |
|---|---|---|---|---|---|
| OFF-BALANCE SHEET | 2.271.512 | 2.352.092 | 2.507.612 | 104 | 107 |
| ASSETS WITH OFF-BALANCE SHEET | 17.988.679 | 18.089.002 | 18.505.886 | 101 | 102 |
| RISK ASSETS WITH OFF-BALANCE SHEET | 12.583.315 | 13.053.738 | 13.613.172 | 104 | 104 |
| General loan risk and Potential loan losses | 534.721 | 717.713 | 805.264 | 134 | 112 |
| General and Special loan loss reserves already established | 534.749 | 717.768 | 804.941 | 134 | 112 |

Non-risk items amount to 4,9 KM or 26% of total assets with off-balance sheet, and they are by 3% less than as of the end of 2010. On the other hand, risk assets with off-balance sheet items amount to 13,6 billion KM, and they increased by 4% or 559 million KM. Off-balance sheet risk items amounted to 2,5 billion KM.

After the negative trends in the previous periods in the segment of lending as a key activity of the banks due to the impact of the global financial and economic crises, in the nine months of 2011, the positive trend from the second half of 2010 continued, that is a slight growth of loans of 3% or 323 million KM. As of 30. 09. 2011., the loans were 10,3 billion KM, with participation in the assets of 67,5%, which is 1,3 percent in relation to the end of 2010.

In the nine months of 2011, granted was a total of 4 billion KM of new loans, which is by 16% or 546 million KM more than for the same period in 2010. Of the total granted loans 69% refers to economy and 29,3% to citizens. The maturity structure of the newly granted loans is as at the end of 2010, the participation of the long term loans and short long term loans is the same 50%.

The most significant limiting factor to the credit growth in the last two years is adverse impact of the crisis to the entire economy in BiH and deterioration of condition in the real sector, then decreased citizen’s spending, as well as more restrictive and prudent lending policies of banks. Although a slight growth of loans is evident, which has a positive impact on the asset quality indicators, there is still a deteriorating trend for loans through increase of nonperforming loans, but in a significantly lower volume than last year. The level of the poor placements is still relatively high and as a consequence the loan losses are, too, which in 2011 will have negative effect on the banks’ financial results. In 2010 the banks significantly increased the provisioning for loan losses, due to the increase of the poor performing loans, and a part was used for write off of unpaid receivables and transfer of the off-balance records. The established reserves for loan losses will be a good amortization for potential loan losses in the following period

The FBA has been involved in the activities aimed at signing of the Memorandum of Understanding with parent-banks from the European Union countries whose daughter-banks operate in the territory of BiH, so called „Vienna Initiative“, which will secure additional financial funds for lending to the real sector, since any deterioration of the economy could adversely reflect to the rating of daughter-banks, and consequently weaken the rating of parent banks.

Three largest banks in the FBiH with credit amount of 6,3 billion KM have participation of 60,8% in total loans at the system level.

From the aspect of sectors to which banks originate their loans, the movements in the first half of 2011, can be evaluated as positive due to increase of loans originated to private companies, as well as a slight increase of placements to citizens, after in 2010, and in the first quarter of 2011 they recorded a decline of 1%. In comparison to the end of 2010, the loans to private companies are higher by 5% or 228 million KM, and they amount to five billion KM or 48,9% of total loans (48,2% at the end of 2010). Loans to citizens increased by 2% or 89 million KM, and they amount to 4,8 billion KM, with a participation of 46,8% ( 47,4% at the end of 2010). The data submitted by banks, as of 30.09.2011., in the aspect of loan structure originated to citizens (based on the purpose), record an increase of loans granted to finance consumer goods[18] from 72 to 74, while housing loans declined from 25% to 23, and the remaining 3% have loans for SMEs and agriculture.

Three largest banks in the system financed 65% of total loans originated to citizens, and to private companies 56% of total loans to all sectors (for citizens sector 65,4% at the end of 2010, and 59% for private companies).

Trend and changes in participation of individual sectors in the overall structure of loans are presented in the following table:

- in 000 KM -

**Table 18:** *Loan structure through departments*

| DEPARTMENTS | 31.12.2009. | | 31.12.2010. | | 30.09.2011. | | RATIO | |
|---|---|---|---|---|---|---|---|---|
| | Amount | Partic% | Amount | Partic % | Amount | Partic % | 4/2 | 6/4 |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| Government institutions | 74.609 | 0,8 | 126.328 | 1,3 | 125.347 | 1,2 | 169 | 99 |
| Public enterprises | 184.005 | 1,9 | 238.105 | 2,4 | 254.309 | 2,5 | 129 | 107 |
| Private enterprises and assoc. | 4.696.276 | 47,9 | 4.815.426 | 48,2 | 5.043.297 | 48,9 | 103 | 105 |
| Banking institutions | 6.755 | 0,1 | 10.975 | 0,1 | 11.624 | 0,1 | 162 | 106 |
| Non-banking financial instit. | 51.255 | 0,5 | 37.235 | 0,4 | 34.571 | 0,4 | 73 | 93 |
| Citizens | 4.765.656 | 48,6 | 4.733.198 | 47,4 | 4.822.700 | 46,8 | 99 | 102 |
| Other | 18.244 | 0,2 | 20.644 | 0,2 | 13.121 | 0,1 | 113 | 66 |
| TOTAL | 9.796.800 | 100,0 | 9.981.911 | 100,0 | 10.304.969 | 100,0 | 102 | 103 |

Currency structure of loans has also been unchanged for longer period: loans financed with currency clause had the highest participation of 70% or 7,2 billion KM (EUR: 6,823 million KM or 95%, CHF: 387 million KM or 5%), loans in domestic currency of 29% or 3 billion KM, while loans in foreign currency had the lowest participation of only 1% or 98 million KM (EUR: 74 million KM or 75%, CHF: 16 million KM or 16%). The total amount of loans in CHF currency of 403 million KM is 4% of the total loan portfolio and almost the whole amount refers to one bank in the system.

Since placements, that is, loans represent the most risky portion of banks' assets, their quality represents one of the most significant elements of stability and successful performance. Evaluation of assets quality is actually evaluation of exposure to loan risk of banks' placements, that is, identification of potential loan losses that are recognized as loan loss provisioning.

Quality of assets and off-balance sheet risk items, general loan risk, potential loan losses by classification categories[19] and off-balance sheet items are presented in the following table:

**Table 19:** *Asset classification, general loan risk (GLR),potential loan losses (PLL) and off-balance sheet items (charged off assets and suspended interest)*

| Classification category | AMOUNT (in 000 KM ) AND PARTICIPATION ( in% ) | | | | | | | | | RATIO | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | 31.12.2009. | | | 31.12.2010. | | | 30.09.2011. | | | | |
| | Assets classif. | Partic. % | GLR PLL | Assets classif. | Partic. % | GLR PLL | Assets classif. | Partic. % | GLR PLL | 5/2 | 8/5 |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 | 12 |
| A | 10.260.601 | 81,5 | 205.228 | 10.477.329 | 80,3 | 209.555 | 11.020.457 | 81,0 | 220.392 | 102 | 105 |
| B | 1.804.767 | 14,4 | 136.973 | 1.645.750 | 12,6 | 132.048 | 1.449.818 | 10,7 | 120.919 | 91 | 88 |

18 Credit cardoperations included.

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

| | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **C** | 307.892 | 2,5 | 72.970 | 471.505 | 3,6 | 113.962 | 577.522 | 4,2 | 142.870 | 153 | 122 |
| **D** | 206.201 | 1,6 | 115.703 | 455.303 | 3,5 | 258.297 | 561.102 | 4,1 | 316.810 | 221 | 123 |
| **E** | 3.854 | 0,0 | 3.847 | 3.851 | 0,0 | 3.851 | 4.273 | 0,0 | 4.273 | 100 | 111 |
| **Risk assets (A-E)** | 12.583.315 | 100,0 | 534.721 | 13.053.738 | 100,0 | 717.713 | 13.613.172 | 100,0 | 805.264 | 104 | 104 |
| **Classified (B-E)** | 2.322.714 | 18,5 | 349.493 | 2.576.409 | 19,7 | 508.158 | 2.592.715 | 19,0 | 584.861 | 111 | 101 |
| **Non perform. (C-E)** | 517.947 | 4,1 | 119.550 | 930.659 | 7,1 | 376.110 | 1.142.897 | 8,4 | 463.942 | 180 | 123 |
| **No risk assets[20]** | 5.405.364 | | | 5.035.264 | | | 4.892.714 | | | 93 | 97 |
| **TOTAL (risk and no risk)** | 17.988.679 | | | 18.089.002 | | | 18.505.886 | | | 101 | 102 |
| **OFF BALANCE SHEET** | | | | | | | | | | | |
| **Written Off** | 505.632 | 89,7 | | 622.990 | 89,6 | | 680.843 | 89,7 | | 123 | 109 |
| **Susp. Interest** | 57.957 | 10,3 | | 72.251 | 10,4 | | 78.517 | 10,3 | | 125 | 109 |
| **TOTAL:** | 563.589 | 100,0 | | 695.241 | 100,0 | | 759.360 | 100,0 | | 123 | 109 |

Risk assets with off-balance sheet items (A-E) amounted to 13,6 billion KM, and, as of 30.09.2011., these items increased by 4% or 559 million KM. Non-risk items amounted to 4,9 billion KM, decreasing by 3% or 142 million KM in comparison to the end of 2010.

If an analysis of the risk assets quality is performed, it could be concluded, that in the three quarters of 2011, the negative trend of the downfall of asset quality and its deterioration from the previous period had significantly improved, special mentioned assets (category B) decreased, poor performing assets slightly increased, and that there was a significant decrease of write off into the off-balance sheet. It must be noted that the highest impact on the significant deterioration of the indicators of the overall system had one bank, which in the previous periods intensified "cleaning" of its credit portfolio, which as a result had a significantly more poor asset quality indicators of this bank and the overall banking system. While the credit portfolio participation of that bank as of 30.09.2011., was 15,2%, the participation of its classified and non performing assets was 34% and 60%, and of the realized increase of the non-performing loans (207 million KM) the largest part refers to the bank (167 million KM or 81%). In the other banks the indicators has slight oscillations (deterioration or improvement), that is: five banks have indicators of the classified in relation to the risk assets more poor than the banking sector, and only one bank (in provisional administration ) has participation of non-performing in relation to risk asses also more poor than the banking sector.

Classified assets (B – E) is by 1% higher than last year, the category B was decreased by 12% or 196 million KM, and nonperforming assets (C-E) increased by 23% or 212 million KM. In the nine months of 2011 performed was the write off of the assets and interest (transferred to off balance sheet) in the amount of 124 million KM (in 2010 the write off was 218 million KM) . While in 2010, due to poor collection and increase of due days of the past due receivables, the banks had to perform a reclassification and a significant amount of loans were moved from B category to nonperforming category (for nine months in 2010., the poor performing assets increased by a high 60% or 310 million KM, that is for 2010 80% or 413 million KM) resulting in the high increase of the loan loss provisioning expenses and having a significant negative impact on the financial results of the banks in 2010., in the nine months of 2011, due to a significantly lower growth of poor performing loans, recorded is a decline of reserves for loan losses, which had a positive reflection on the financial result of the banking system.

The classified assets as of 30.09.2011 were 2,6 billion KM, and nonperforming one 1,1 billion KM (31.12.2010: 2,6 billion KM and 931 million KM).

As result of the mentioned, the indicators of asset quality expressed as ratio, that is, participation of individual categories in risky assets have insignificantly changed in comparison to the end of

[20] Assets items that are not, according to Article 22, Paragraph 7 of Decision on Minimum Standards for Bank Credit Risk and Assets Classification Management, subject to accrual of general loan loss provisions of 2%.

2010. The classified assets to risky assets ratio has improved by 0,7% due to the increase of classified assets (4%) in comparison to the end of 2010, which is representing 19,0%.

If an analysis is performed of only the ratio and trend of nonperforming assets and risk assets, as of 30.09.2010., this ratio was 8,4%, which is still relatively low ratio, and, if compared to the end of 2010, it is higher by 1,3 per cent. If we take into account the category E (the written off placements) the noted ratio is significantly higher and is 13,2% (in some banks up to three times higher due to significant write offs). However, it should be taken with reserve, taken that the participation of category B in the risk assets is 10,7%, and the doubt that portion of placements reported under this category deteriorated in quality and should be categorized as nonperforming assets, in other words that some banks still practice not to timely establish adequate loan loss provisioning which was confirmed in the on-site examinations and resulted in insufficient provisioning for loan losses. That's why it is crucial that the banks rate the quality of their placements as realistically as possible, especially due to the fact that performing under a crises increases the delays in collection of the due receivables, the reserve expenses grow, and the earnings of the bank decline.

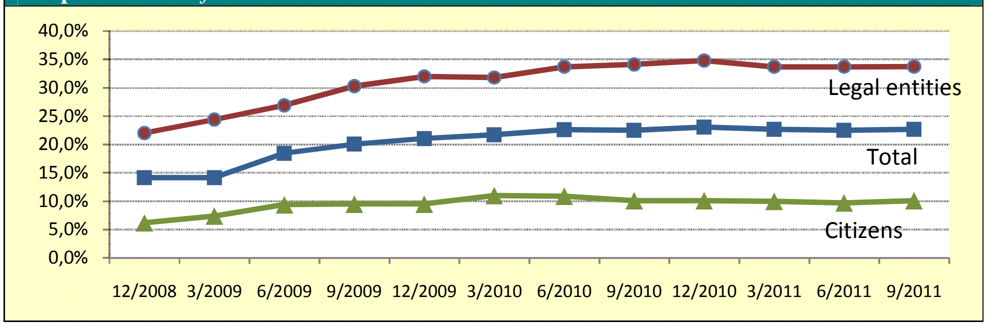
The analysis of data by sectors is based on the indicators of the quality of loans granted to the two most significant sectors: private companies and citizens. The two mentioned indicators for these sectors are significantly different and indicate higher loan risk exposure, and also the exposure to potential loan losses with the loans originated to legal entities.

**Table 20:** *Classification of loans originated to citizens and legal entities*

| Classification category | AMOUNT (in 000 KM )AND PARTICIPATION (in% ) | | | | | | | | | | | | RATIO |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 31.12.2010. | | | | | | 30.09.2011. | | | | | | |
| | Citizens | Partic. % | Legal entities | Partic. % | TOTAL Amount | TOTAL Partic. | Citizens | Partic. % | Legal entities | Partic. % | TOTAL Amount | TOTAL Partic. | 12/6 |
| 1 | 2 | 3 | 4 | 5 | 6 (2+4) | 7 | 8 | 9 | 10 | 11 | 12 (8+10) | 13 | 14 |
| **A** | 4.257.408 | 89,95 | 3.422.650 | 65,21 | 7.680.058 | 76,94 | 4.336.205 | 89,91 | 3.633.163 | 66,27 | 7.969.368 | 77,34 | 104 |
| **B** | 185.851 | 3,93 | 1.201.981 | 22,94 | 1.387.832 | 13,90 | 166.544 | 3,45 | 1.047.696 | 19,11 | 1.214.240 | 11,78 | 87 |
| **C** | 125.114 | 2,65 | 336.038 | 6,36 | 461.152 | 4,62 | 137.166 | 2,85 | 429.598 | 7,84 | 566.764 | 5,50 | 123 |
| **D** | 164.826 | 3,47 | 288.042 | 5,49 | 452.868 | 4,54 | 182.617 | 3,79 | 371.812 | 6,78 | 554.429 | 5,38 | 122 |
| **E** | 1 | 0,00 | 0 | 0,00 | 1 | 0,00 | 168 | 0,00 | 0 | 0,00 | 168 | 0,00 | 0 |
| **TOTAL** | 4.733.200 | 100,0 | 5.248.711 | 100,0 | 9.981.911 | 100,00 | 4.822.700 | 100,0 | 5.482.269 | 100,0 | 10.304.969 | 100,00 | 103 |
| **Class.loans B-E** | 475.792 | 10,05 | 1.826.061 | 34,79 | 2.301.853 | 23,06 | 486.495 | 10,08 | 1.849.106 | 33,73 | 2.335.601 | 22,66 | 101 |
| **TOTAL** | 289.941 | 6,13 | 624.080 | 11,89 | 914.021 | 9,16 | 319.951 | 6,63 | 801.410 | 14,62 | 1.121.361 | 10,88 | 123 |
| | | 47,42 | | 52,58 | | 100,00 | | 46,80 | | 53,20 | | 100,00 | |
| **Participation by sectors in classified loans, nonperforming loans and category B** | | | | | | | | | | | | | |
| **Classification B-E** | | 20,67 | | 79,33 | | 100,00 | | 20,83 | | 79,17 | | 100,00 | |
| **NPL C-E** | | 31,72 | | 68,28 | | 100,00 | | 28,53 | | 71,47 | | 100,00 | |
| **Category B** | | 13,39 | | 86,61 | | 100,00 | | 13,72 | | 86,28 | | 100,00 | |

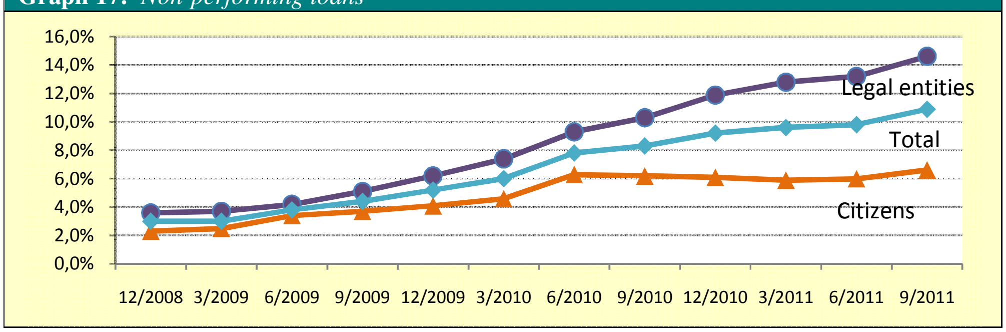
The indicators of the quality of loans deteriorated in the first three quarters of 2011, especially the participation of the poor performing loans, primarily as a result of the growth of the total poor quality loans by 23% or 207 million KM (only in the third quarter 111 million KM), legal entities by around 177 million KM or 28%, and to citizens by 30 million or 10%, which lead to increase of the participation of the poor performing loans from 9,16% to 10,88%, and had a negative impact on other indicators for these two sectors and total loan portfolio. However, again should be noted the impact of the indicators of one bank on the total banking system, especially on the growth indicator and participation of the non-performing loans, since if that bank is excluded, it can be concluded that the listed indicator slightly increased in comparison to 31.12.2010 (from 4,87 to 5,11%).

**Graph 16:** *Classified loans*




As of 30.09.2011., of total loans originated to legal entities in the amount of 5,5 billion KM, 1,8 billion KM or 33,73% was classified in categories B to E (1,8 billion KM or 34,79% at the end of 2010), while of total loans originated to citizens in the amount of 4,8 billion KM, classification categories B to E represent 486 million KM or 10,08% (476 million KM or 10,05% at the end of 2010).

**Graph 17:** *Non-performing loans*




Of loans finance to legal entities, 801 million KM was classified as nonperforming loans or 14,62% of total loans originated to this sector (as of 31.12.2010., these items amounted to 624 million KM or 11,89%). Nonperforming loans, in the sector of citizens, amounted to 320 million KM or 6,63% (as of 31.12.2010., these items amounted to 290 million KM or 6,13).

Due to poor performing receivables trend that is the delays in collecting the past due loan liabilities from clients, there were activated some guarantees in a number of delinquent loans that had this type of insurance, so the burden of payment of such loans fell on the guarantors. As of 31.12.2009., the FBA requires a report about the loans being repaid by the guarantor, in order to collect, monitor and analyze the data on loans that are being repaid by the guarantors. According to the banks' reports in F BiH as of 30. 09. 2011., 3.493 guarantors in total repaid 13 million KM of the total granted amount of loans of 85 million KM (3.022 credit party), which is by 11% less in comparison to the amount of the payment by the guarantors as of 31. 12. 2010. (15 million KM paid by 3.767 guarantors, while the amount of the total loans was 101 million KM – 3.192 credit parties). The amount of the remaining debt is 59 million KM (31. 12. 2010.: 63 million KM). From the listed data it can be concluded that in the nine months of 2011, the amount of loans paid by guarantors decreased, the balance of the remaining debt, as well the amount of payments on the account of guarantors, which was mostly influenced by the return of the significant amount of repayment of loans of around 16 million by principal debtor. The participation of loans and the number of credit parties being repaid by the guarantors in relation to the data for the entire system is low and amounts to only 0,57% and 0,28%.

With an aim to defer the negative effects of the global financial and economic crises, and taking care of maintaining the stability of the banking sector, the FBA at the end 2009, issued a Decision on temporary measures for reconstruction of loan liabilities of individuals and legal entities[21].

The main goal for issuing these temporary measures was to stimulate the banks to „revive“ credit activities, and restructuring the existing receivables, without increasing the price of the loan and expenses for the existing creditors, to help both the individuals and the legal entities to overcome the situation in which they are because of the effects of the economic crises (decrease in the repayment capability, for individuals due to the loss of jobs, late salaries, decrease in income etc., and for legal entities due to increased lack of liquidity, significant decrease of business activities, very difficult conditions in the real sector in general etc.).

Acting in accordance with the mentioned Decision, the banks in the Federation of BiH in the three quarters of 2011, of total received 367 requests for reconstruction of credit liabilities granted 340 requests in the total amount of 55 million KM or 93% which is twice as low as in the same period in 2010. Of the total amount of granted reconstructed liabilities 53 million KM refers to legal entities, and two million to individuals.

Net effect on the loan loss reserves (in further reading LLR), based on the performed reprogramming is an increase of 463 thousand KM. It should be noted that there were opposite movements, that is increases and declines of the LLR on these basis, which at the end resulted in the noted net effect. The banks were performing very prudently, mostly maintaining the LLR on the same level, with which they were able to avoid short term and long term increases of the income, which in reality presents a true and responsible banks' attitude in implementing the provisions of the Decision that relate to this segment.

In the three quarters of 2011., the reconstructed loans in the total loans as of 30.09.2011., have a participation of only 0,53% (for the sector of legal entities in the portfolio of legal entities this per cent is 0,96%, while the citizens sector is 0,04%).

From the listed data it can be concluded that both in the number and the amount of the reconstructed loan liabilities the result is relatively modest, if compared with the total loan portfolio and through sectors (for legal entities and individuals).

Although the results and the effects of implementation of the Decision are not significant, it is estimated that development of such a regulation was very important, such measures of temporary character under the conditions of extreme financial and economic crises were necessary for the financial and real in FBiH, and had a positive effect on debtors (individuals and legal entities), facilitating debt servicing in compliance with their repayment ability. That is why the prolonging of the amendments of the Decision to the end of 2011 is justifiable, especially due to the fact that the impact of the crises is still evident, and that the positive movements and economic recovery are to be expected next year.

For more realistic assessment, it should take into account the amount of loans that banks, during the observing period, charged off to the off-balance sheet, as presented in the following table.

-000 KM-

[21] "Official Gazette F BiH", No.2/10.

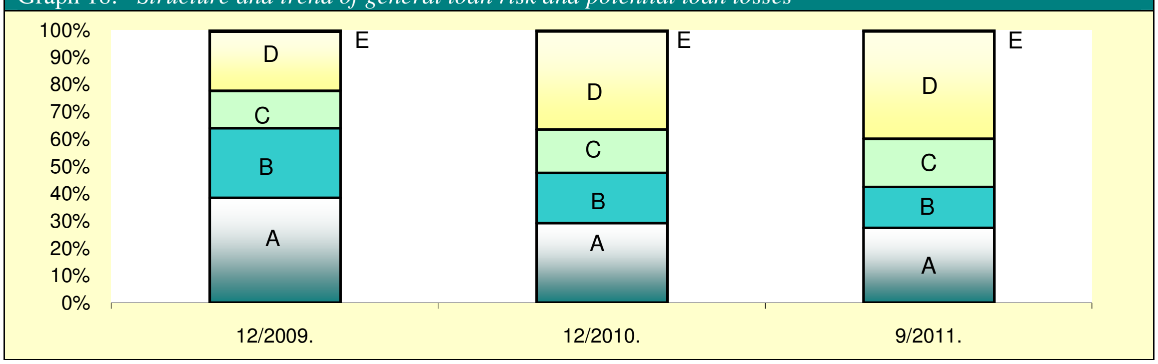
| **Table 21:** *Off-balance sheet records: charged off assets and suspended interest* | | | | | | |
|---|---|---|---|---|---|---|
| **DESCRIPTION** | **CITIZENS** | | **LEGAL ENTITIES** | | **TOTAL** | |
| | **Charged off assets** | **Suspended interest** | **Charged off assets** | **Charged off assets** | **Suspended interest** | **Charged off assets** |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 |
| Opening balance as of 31.12.2010. | 216.721 | 16.759 | 406.269 | 55.529 | 622.990 | 72.288 |
| *Changes in 2011:* | | | | | | |
| - new charge offs (current year) | 47.731 | 5.432 | 59.381 | 11.906 | 107.112 | 17.338 |
| - payments made in the current year | 20.837 | 4.739 | 15.174 | 5.711 | 36.011 | 10.450 |
| - *permanent charge off* | 562 | 65 | 12.686 | 594 | 13.248 | 659 |
| Balance as of 30.09.2011. | 243.053 | 17.387 | 437.790 | 61.130 | 680.843 | 78.517 |

Balance of the charged off assets, as of 30.09.2011., (681 million KM), and the suspended interest (78 million KM) increased by 9% in comparison to 2010. In the third quarter of 2011., recorded is an incline of 5% due to larger write off and smaller collection in comparison to the first two quarters in 2011.

Level of general loan risk and estimated potential loan losses in the classification categories, as determined in accordance with the criteria and methodology prescribed by the FBA's decisions, their trend and structure at the level of the banking sector are presented in the following tables and graphs.

| **Table 22:** *Off-balance sheet records: charged off assets and suspended interest* | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **Classification category** | **AMOUNT (in 000 KM) and STRUCTURE (in%)** | | | | | | **RATIO** | |
| | **31.12.2009.** | | **31.12.2010.** | | **30.09.2011.** | | **4/2** | **6/4** |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| **A** | 205.228 | 38,4 | 209.555 | 29,2 | 220.392 | 27,4 | 102 | 105 |
| **B** | 136.973 | 25,6 | 132.048 | 18,4 | 120.919 | 15,0 | 96 | 92 |
| **C** | 72.970 | 13,7 | 113.962 | 15,9 | 142.870 | 17,7 | 156 | 125 |
| **D** | 115.703 | 21,6 | 258.297 | 36,0 | 316.810 | 39,4 | 223 | 123 |
| **E** | 3.847 | 0,7 | 3.851 | 0,5 | 4.273 | 0,5 | 100 | 111 |
| **TOTAL** | 534.721 | 100 | 717.713 | 100 | 805.264 | 100 | 134 | 112 |

Graph 18: *Structure and trend of general loan risk and potential loan losses*




As reported, banks have established loan loss provisions in accordance with the regulations and level of the estimated credit risk.

Based on an analysis of the established provisions, in total amount and by classification categories, if compared to the end of 2010, general loan risk (for category A) and potential loan loss provisions have increased by 12%, or 87 million KM amounting to 805 million KM. Due to an increase of the poor performing assets, the banks had to increase the reserves for these poorest quality loans by 23,4%, from 376 million KM to 464 million KM and the largest growth was recorded in the third quarter 13% or 53 million KM. The reserves for general credit risk (A category) increased by an insignificant 5% or 11 million KM, while for category B, due to its decrease by 174 million KM, mostly generated by the reclassification into more poor categories, the reserves decreased by 8% or 11 million KM. One of the most significant indicators of the asset quality is the relation of the potential loan losses and the risk assets with the off-balance sheet, which is 4,3% and is higher by 0,4% in comparison to the previous year (3,89%). However, if we take into consideration the E category, the listed ratio is two times higher and is 9,4%. As of 30.09.2011., banks in average allocated for category B 8,3%, for category C 24,7%, category D 56,5% and E 100% (at the end of 2010: B 8%, C 24,2%, D 56,7% and E 100%).

The asset quality analysis, that is, the loan portfolio analysis of individual banks, as well as on-site examinations at banks, indicate loan risk as dominant risk with majority of banks, raising a concern that some banks still have inadequate management practices, that is, evaluation, measuring, monitoring, and control of loan risk and assets classification, which was determined in on-site examinations through significant amount of insufficient loan loss reserves that banks have established based on the orders issued by the FBA. However, this is not adding to an essential resolution of the problem.

The FBA has ordered corrective measures to those banks whose assets quality was rated poor by the examination in sense of preparation of the operating program that has to contain action plan aimed to improve existing practices for loan risk management, that is, assets quality management, decrease of existing concentrations and resolution of the nonperforming assets issue, and prevention of their further deterioration. Implementation of the FBA's orders is continuously monitored through an intensified follow-up procedure based on reports and other documentation submitted by banks, as well as their verification in targeted on-site examinations. Supervision of this segment has been intensified due to obvious adverse trends, which has a significant impact through deterioration of banks' profitability and declining of their capital base, which is a reason for banks to timely take actions to raise capital from external sources.

### *Transactions with related entities*

While operating, banks are exposed to different types of risks, of which the most significant is the risk of transactions with related entities of banks.

In accordance with the Basle Standards, the FBA has established certain prudential principles and requirements related to transactions with related entities of banks, as regulated in Decision on Minimum Standards for Bank's Operations with Related Entities, prescribing requirements and method of operations with related entities. The Decision and Law on Banks regulate the duty of Supervisory Board of a bank, which has to adopt, upon the proposal of the General Manager, special policies regulating operations with related entities and to monitor their implementation.

The FBA Decisions prescribe a special set of reports, including transactions with one segment of related entities, such as loans, and potential and undertaken off-balance sheet liabilities (guarantees, letters of credit, undertaken loan commitments), as the most frequent and the most riskiest form of transactions between a bank and related entities.

The set of prescribed reports include data on loans originated to the following categories of related entities:
- Bank's shareholders over 5% of voting rights,
- Supervisory Board members and bank management and
- Subsidiaries and other enterprises related to a bank.

-000 KM-

**Table 23:** *Transactions with related entities*

| Description | GRANTED LOANS[22] | | | RATIO | |
|---|---|---|---|---|---|
| | 31.12.2009. | 31.12.2010. | 30.09.2011. | 3/2 | 4/3 |
| 1 | 2 | 3 | 4 | 5 | 6 |
| Shareholders over 5% of voting rights, subsidiaries and other related enterprises | 29.191 | 84.600 | 79.570 | 290 | 94 |
| Supervisory Board and Audit Board members | 470 | 375 | 410 | 80 | 109 |
| Bank Management | 2.193 | 2.239 | 2.141 | 102 | 96 |
| TOTAL | 31.854 | 87.214 | 82.121 | 274 | 94 |
| Potential and undertaken off-balance sheet liabilities | 5.137 | 22.653 | 30.063 | 441 | 133 |

In the observed period, credit exposures to persons related to banks decreased by 6%, and potential liabilities increased by 33%. Based on the presented data, it can be concluded that it is still a question of a small amount of loans-guarantees operations with related entities, and the level of risk is low. The FBA pays special attention (in on-site examinations) to banks' operations with related entities, especially in assessing identification system and monitoring of risk exposure to related entities operations. The FBA on-site examiners issue orders for elimination of determined weaknesses within certain deadlines and initiate violation procedures. Part of these activities is also to monitor and supervise implementation of the issued orders in the follow up procedure. This has had a positive influence on this segment of operations, since the risk management quality in this segment has improved.

## 2.2. Profitability

For the nine months of 2011, according to the income statements, the banks in the Federation of BiH realized a positive financial result – profit in the amount of 41,5 million KM, while in the same period in 2010, there was loss generated on the level of the banking sector in the amount of 58,7 million KM. The biggest effect on the realization of the positive result on the level of the banking system had the significant increase of profit in banks that had positive performance in the same period last year (for about 61 million KM), especially in two largest banks in the system which carry the profitability, as well as decrease of a high loss in one bank (by around 29 million KM) which in the same period last year was by 25 million KM higher than the loss on the level of the system, as well as decrease of losses in other banks that previously had a negative performance.

The biggest influence on improvement of profitability in a number of banks is the increase of net interest exclusively due to the decline of the interest expenses, growth of the operating income in almost all banks in the system, as well as decrease of loan loss provisions in a number of banks.

Positive financial result of 100,1 million KM was generated by 13 banks, which is more than two times higher or by 60 million KM than in the same period in 2010. At the same time, six banks reported loss of 59 million KM, which declined by 41% or 40 million KM in comparison to the same period in 2010

Detailed data is shown in the following table.

-000 KM-

[22] Apart from loans, it includes other claims, deposited funds and the placements to shareholders (financial institutions) exceeding 5% of voting rights.

| **Table 24:** *Financial result reported: profit/loss* | | | | | | |
|---|---|---|---|---|---|---|
| **Date/Description** | **At the system level** | | **State banks** | | **Private banks** | |
| | **Amount** | **No. of banks** | **Amount** | **Amount** | **No. of banks** | **Amount** |
| **30.09.2009.** | | | | | | |
| Loss | -37.396 | 9 | -870 | 1 | -35.809 | 8 |
| Profit | 58.286 | 11 | 629 | 1 | 57.657 | 10 |
| **Total** | **20.890** | **20** | **-241** | **2** | **21.848** | **18** |
| **30.09.2010.** | | | | | | |
| Loss | -98.836 | 7 | -316 | 1 | -98.520 | 6 |
| Profit | 40.095 | 13 | 817 | 1 | 39.278 | 12 |
| **Total** | **-58.741** | **20** | **501** | **2** | **-59.242** | **18** |
| **30.09.2011.** | | | | | | |
| Loss | -58.594 | 6 | - | - | -58.594 | 6 |
| Profit | 100.066 | 13 | 597 | 1 | 99.469 | 12 |
| **Total** | **41.472** | **19** | **597** | **1** | **40.875** | **18** |

Similar to other segments, this segment has also encountered concentrations: of total profit generated (100 million KM), 75,5% was generated by two largest banks in the system, whose participation in the banking system assets was 48,8%. In the total loss of 59 million KM, 55 million KM or 93,3% refers to only one bank with asset participation of 11,8%, third in the system (in the same period last year that bank's loss was 83,7 million KM). Analytical data indicate that a total of 15 banks have a much better financial result (by a high 102 million KM), and four banks have worse results (the effect is 3 million KM).

Based on the analytical data and the indicators for the quality evaluation of the profitability (the amount of the generated financial result – profit/loss and ratios used for evaluation of profitability productivity and efficiency of operation as well as other parameters related to evaluation of operation) it can be concluded that the total profitability of the system had improved in comparison to the previous year, and especially at larger banks that are carriers of profitability which generated significantly higher profit that in the same period last year.

At the system level, total income was realized in the amount of 676 million KM with an increasing rate of 9% or 57 million KM in relation to the comparing period in the previous year. Total noninterest bearing expenses were 635 million KM, with the decrease rate of 6% or 44 million KM which had a positive reflection to the overall financial result of the sector.

In spite the slight increase of the average loans by 3,8%, the growth of the poor performing assets, and consequently the suspended interest, as well as the slight decline of average interest rate on loans, influenced the still present, but slower, declining trend of the interest income of 1% or four million KM. The interest income was 637 million KM with a decreased participation in the total income from 103,3% to 94,1%. In the interest income structure the largest participation belongs to the interest income from loans, which are 567 million KM or 83,8% of the total income, with a decline of 3% or 17 million KM in comparison to the same period last year, which is a result of the decrease of average interest rate on loans for the observed period from 5,96% to 5,58%. Interest bearing accounts in deposit institutions had a significant growth of 89%, and their participation increased from 1,6% to 2,8%.

On the other hand, continued is the positive trend of decline of interest expenses, which had a significantly higher decline rate (12%) in comparison to the declining rate of interest income (1%). The interest expenses are 220 million KM, with a change in participation in the total income from 40,2% to 32,5%. Interest expenses on deposits, as a structurally largest item of the interest expenses, declined by 16% or 33 million KM, primarily as a result of the decrease of average interest bearing deposits by 1,4% as well as interest rates on short term and long term deposits. The average interest rate on deposits declined from 1,99% to 1,69%, and as of 30.09.2011 it was 2,35%. In 2011, after the significant decline of the interest expenses on taken loans and other borrowings in the last year (43%), which was due to regular payments, and in part due to payments before the due date (which the banks were performing in order to decrease the expenses caused by high liquidity), they recorded a growth of 8% or three million, with an insignificant decrease in participation from 5,3% to 5,2%.

Net interest income is 417 million KM and in comparison to the same period last year increased by 7% or 26 million KM, with a declined participation in the total income from 63,1% to 61,7%.

Operating income was 259 million KM and in relation to the comparing period recorded a growth of 13% or 30 million KM with a change in the participation in the total income from 36,9% to 38,3%.

Total noninterest expenses were 635 million KM and in comparison to the same period of last year decreased by 6% or 44 million KM, primarily based on the downfall of loan loss provisions. At the same time, their participation in the structure of total income declined from 109,5% to 93,9%.

After a significant increase in the same period in 2010, in comparison to the same period in 2009 (63%), in the nine months of 2011 the reserve expenses for loan losses nominally and relatively had a significant decline of 22% or 59 million KM, and were 206 million KM, and their participation in the structure of the total income significantly declined from 42,7% to 30,5%. The operating expenses had the opposite trend and movements with a growth rate of 3% or 12,2 million KM, of which the fixed asset had a growth of 6% and are 119 million KM, and salary expenses and contributions a growth of 3% and are 187 million KM (average number of employees in this period of 2011., decreased by 2% in comparison to the same period in 2010).

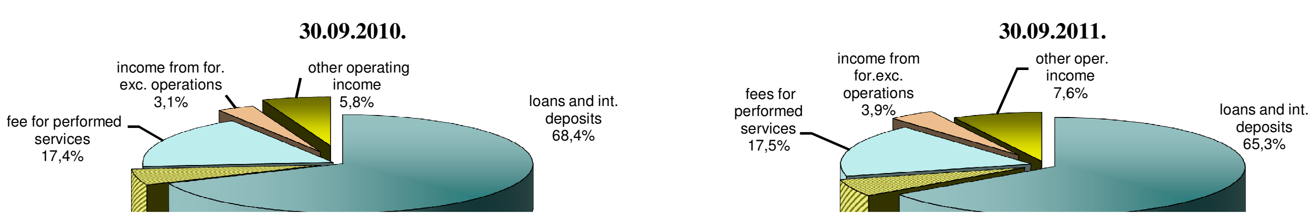
Trend and structure of total income and expenses is presented in the following tables and graphs:

- in 000 KM-

**Table 25:** *Structure of total income*

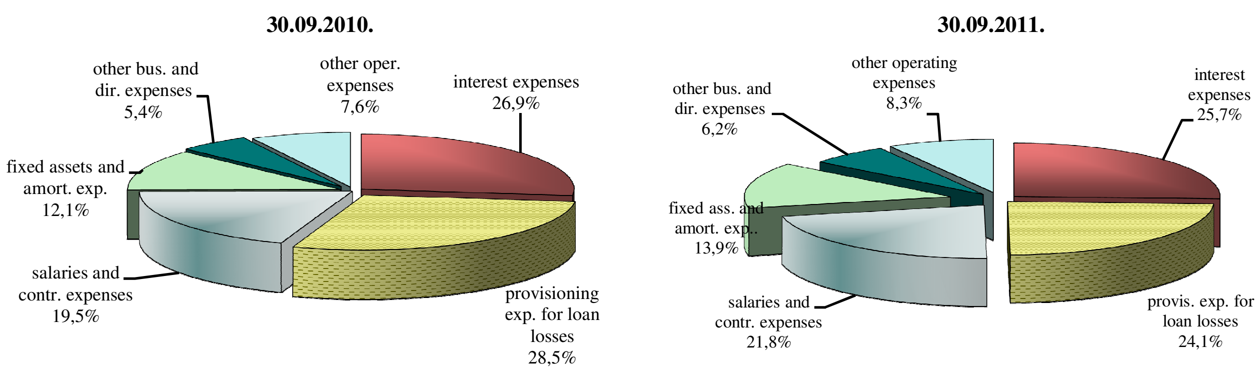
| Structure of total income | 30.09.2009. | | 30.09.2010. | | 30.09.2011. | | RATIO | |
|---|---|---|---|---|---|---|---|---|
| | Amount | % | % | % | Amount | % | 4/2 | 6/4 |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| **I Interest income and similar income** | | | | | | | | |
| Interest bearing deposit accounts with depository institutions | 19.974 | 2,2 | 10.117 | 1,2 | 19.119 | 2,1 | 51 | 189 |
| Loans and leasing | 640.202 | 70,5 | 584.168 | 67,2 | 567.062 | 63,2 | 91 | 97 |
| Other interest income | 35.607 | 3,9 | 46.669 | 5,3 | 51.115 | 5,7 | 131 | 110 |
| **TOTAL** | 695.783 | 76,6 | 640.954 | 73,7 | 637.296 | 71,1 | 92 | 99 |
| **II Operating income** | | | | | | | | |
| Service fees | 138.627 | 15,3 | 150.973 | 17,4 | 156.605 | 17,5 | 109 | 104 |
| Foreign exchange income | 25.667 | 2,8 | 27.097 | 3,1 | 34.870 | 3,9 | 106 | 129 |
| Other operating income | 48.668 | 5,3 | 50.831 | 5,8 | 67.911 | 7,6 | 104 | 134 |
| **TOTAL** | 212.962 | 23,4 | 228.901 | 26,3 | 259.386 | 28,9 | 107 | 113 |
| **TOTAL INCOME ( I + II )** | 908.745 | 100,0 | 869.855 | 100,0 | 896.682 | 100,0 | 96 | 103 |

**Graph 19:** *Structure of total income*



| **Table 26:** *Structure of total expenses* | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **Structure of total expenses** | **30.09.2009.** | | **30.09.2010.** | | **30.09.2011.** | | **RATIO** | |
| | **Amount** | **%** | **Amount** | **%** | **Amount** | **%** | **4/2** | **6/4** |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| **I Interest expenses and similar expenses** | | | | | | | | |
| Deposits | 229.884 | 26,0 | 205.259 | 22,1 | 172.150 | 20,1 | 89 | 84 |
| Liabilities for borrowings | 57.003 | 6,4 | 32.669 | 3,5 | 35.184 | 4,1 | 57 | 108 |
| Other interest expenses | 16.009 | 1,8 | 11.614 | 1,3 | 12.453 | 1,5 | 73 | 107 |
| **TOTAL** | 302.896 | 34,2 | 249.542 | 26,9 | 219.787 | 25,7 | 82 | 88 |
| **II Total non-interest bearing expenses** | | | | | | | | |
| General loan risk and potential loan losses Provisioning | 162.847 | 18,4 | 264.900 | 28,5 | 206.140 | 24,1 | 163 | 78 |
| Salary expenses | 188.083 | 21,2 | 181.300 | 19,5 | 186.587 | 21,8 | 96 | 103 |
| Business premises and depreciation expenses | 115.612 | 13,1 | 111.980 | 12,1 | 118.515 | 13,9 | 97 | 106 |
| Other business and direct expenses | 49.802 | 5,6 | 50.400 | 5,4 | 53.318 | 6,2 | 101 | 106 |
| Other operating expenses | 66.585 | 7,5 | 70.435 | 7,6 | 70.843 | 8,3 | 106 | 101 |
| **TOTAL** | 582.929 | 65,8 | 679.015 | 73,1 | 635.403 | 74,3 | 116 | 94 |
| **TOTAL EXPENSES ( I + II )** | 885.825 | 100,0 | 928.557 | 100,0 | 855.190 | 100,0 | 105 | 92 |

**Graph 20:** *Structure of total expenses*




The following tables give the most significant ratios for evaluation of profitability, productivity and efficiency of banks:

- in %-

| **Table 27:** *Ratios of profitability, productivity and effectiveness by periods* | | | |
|---|---|---|---|
| **RATIOS** | **30.09.2009.** | **30.09.2010.** | **30.09.2011.** |
| **Return on Average Assets** | 0,14 | -0,39 | 0,28 |
| **Return on Average Total Capital** | 1,26 | -3,54 | 2,39 |
| **Return on Average Equity** | 1,85 | -5,03 | 3,51 |
| **Net Interest Income/Average Assets** | 2,59 | 2,57 | 2,77 |
| **Fee Income/Average Assets** | 1,41 | 1,50 | 1,72 |
| **Total Income/Average Assets** | 4,00 | 4,07 | 4,49 |

| | | | |
|---|---|---|---|
| **Operating and Direct Expanses23/Average Assets** | 1,40 | 2,07 | 1,72 |
| **Operating Expenses/Average Assets** | 2,44 | 2,38 | 2,50 |
| **Total Non-interest Expanses/Average Assets** | 3,85 | 4,45 | 4,22 |

-in %-

**Table 28:** *Ratios of profitability, productivity and effectiveness as of 30.09. 2011.*

| RATIOS | 30.09. 2011. | | |
|---|---|---|---|
| | **STATE BANKS** | **PRIVATE BANKS** | **AVERAGE IN FBiH** |
| **Return on Average Assets** | 0,34% | 0,27% | 0,28% |
| **Return on Average Total Capital** | 1,27% | 2,42% | 2,39% |
| **Return on Average Equity** | 1,75% | 3,56% | 3,51% |
| **Net Interest Income/Average Assets** | 1,86% | 2,78% | 2,77% |
| **Fee Income/Average Assets** | 2,90% | 1,71% | 1,72% |
| **Total Income/Average Assets** | 4,76% | 4,49% | 4,49% |
| **Operating and Direct Expanses/Average Assets** | 0,43% | 1,74% | 1,72% |
| **Operating Expenses/Average Assets** | 3,99% | 2,48% | 2,50% |
| **Total Non-interest Expanses/Average Assets** | 4,41% | 4,22% | 4,22% |

Based on the analyses of the core parameters for profitability quality evaluation, it can be concluded that the profitability of the overall system is much better, the profit realized in comparison to the high loss reported on the level of the system, resulted with positive key profitability indicators: ROAA (Return on Average Assets) is 0,28% and ROAE (Return on Average Equity) is 3,51% (the same indicators in the same period last year were negative due to the reported loss on the level of the system in the amount of 58,7 million KM) . Productivity of banks, measured as ratio of total income and average assets (4,49%) was improved in comparison to the same period last year (4,07%) due to growth of the total income (9%) while the average total assets slightly declined (2%). It should be emphasized that the business and direct expenses per average assets decreased (from 2,07% to 1,72%), which is related to the decline of loan loss provisions expenses.

Under a more deteriorated performance conditions of banks, and due to adverse effects of the economic and financial crisis to the banking sector in the FBiH, profitability of banks, in the forthcoming period, will mostly depend on deterioration of asset quality, that is, permanent increase of loan losses and loan risk, and will depend on effective management and operating income and expenses control. With an aim to improve the profitability, the banks will have to increase the level of lending activities, not only to ensure increase of interest income, but to utilize their social core function of the collected financial assets allocation to the economic flows and the economy in compliance with the standards of prudent performance and sound practices of risk management, primarily of credit risk.

In addition, profit of banks, that is, financial result will mostly depend on price and interest rate risk, both in the sources and price changes in funding sources of banks, and possibility to realize interest rate margin sufficient to cover all non-interest bearing expenses, and, eventually, to provide for satisfactory profit on the invested capital for bank owners. That is why the key factor is effectiveness and profitability of each bank's management quality and its business policy since this is the most direct way to affect its performance.

## 2.3. Risk-weighted nominal and effective interest rates

23 Expenses include provisions for potential loan losses.

In order to increase transparency, and to make easy a comparability of conditions of banks in process of originating loans and accepting deposits and protection of customers through a transparent disclosure of loan expenses versus deposit income, and, in accordance with the international standards, criteria and practices in other countries, the FBA, as of 01.07.2007., prescribed unified method of computation and disclosure of effective interest rate[24]for all banks that have their seat in the Federation of BiH, and their organizational units, regardless of the territory in which they operate, including organizational units of the banks operating in the Federation of BiH. Effective interest rate represents a real relative price of a loan, that is, an income generated from a deposit, expressed as per cent at the annual level.

Effective interest rate is a discursive interest rate computed at the annual level. It applies a compound interest rate in a way to equal discounted cash inflows with discounted cash outflows for the originated loans, that is, accepted deposits.

Banks are obliged to monthly report to the FBA of risk-weighted nominal and effective interest rates on loans and deposits originated or accepted within the reporting month, in accordance with the methodology prescribed[25].

The following table presents risk-weighted nominal and effective interest rates (hereinafter: NIR and EIR) for loans on the banking system level for the two most important sectors (economy and citizens) for December of 2009, March, June, September and December of 2010, and June and September of 2011:

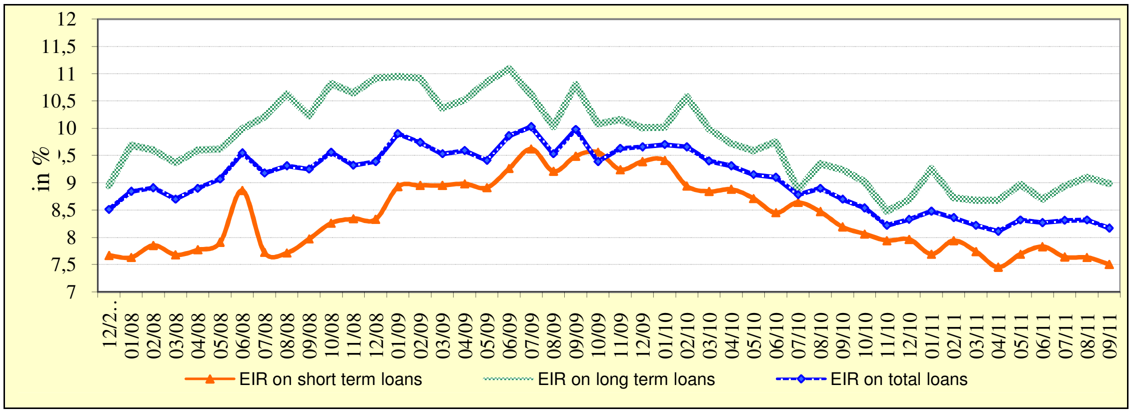
**Table 29** *Risk-weighted average NIR and EIR on loans*

| DESCRIPTION | 31.12.2009. | | 30.06.2010. | | 30.09.2010. | | 31.12.2010 | | 30.06.2011. | | 30.09.2011. | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | NIR | EIR | NIR | EIR | NIR | EIR | NIR | EIR | NIR | EIR | NIR | EIR |
| 1 | 2 | 3 | 6 | 7 | 6 | 7 | 8 | 9 | 10 | 11 | 12 | 13 |
| 1. Risk-weighted interest rates for short-term loans | 8,55 | 9,39 | 7,9 | 8,45 | 7,7 | 8,19 | 7,51 | 7,96 | 7,24 | 7,83 | 6,93 | 7,50 |
| 1.1. Economy | 8,51 | 9,27 | 7,86 | 8,34 | 7,69 | 8,08 | 7,47 | 7,82 | 7,19 | 7,68 | 6,87 | 7,34 |
| 1.2. Citizens | 9,51 | 12,9 | 8,97 | 12,28 | 8,42 | 12,57 | 8,67 | 12,65 | 8,74 | 12,64 | 8,38 | 12,07 |
| 2. Risk-weighted interest rates for long-term loans | 9,16 | 10,00 | 8,89 | 9,75 | 7,75 | 9,24 | 7,91 | 8,69 | 7,76 | 8,70 | 8,05 | 8,99 |
| 2.1. Economy | 8,46 | 9,15 | 8,4 | 8,9 | 8,07 | 8,45 | 7,34 | 7,82 | 7,17 | 7,67 | 7,54 | 8,08 |
| 2.2. Citizens | 10,21 | 11,32 | 9,35 | 10,56 | 7,48 | 9,93 | 8,79 | 10,05 | 8,16 | 9,39 | 8,46 | 9,71 |
| 3. Total risk-weighted interest rates for loans | 8,82 | 9,66 | 8,40 | 9,10 | 7,73 | 8,70 | 7,72 | 8,33 | 7,50 | 8,27 | 7,43 | 8,17 |
| 3.1. Economy | 8,50 | 9,23 | 8,04 | 8,53 | 7,81 | 8,19 | 7,42 | 7,82 | 7,68 | 7,18 | 7,06 | 7,54 |
| 3.2. Citizens | 10,17 | 11,42 | 9,34 | 10,64 | 7,53 | 10,05 | 8,78 | 10,18 | 9,54 | 8,19 | 8,46 | 9,85 |

**Graph 21:** *Risk weighted average EIR on loans*

[24] Decision on unified method of computation and disclosure of effective interest rates on loans and deposits ("Official Gazette of the FBiH", number 27/07).

[25] Guidelines for implementation of Decision on unified method of computation and disclosure of effective interest rates on loans and deposits and Guidelines for computation of risk-weigthed nominal and effective interest rate.




When analyzing the trend of interest rates, it is relevant to monitor risk-weighted EIR, while a difference in the risk-weighted NIR is exclusively the result of fees and provisions paid to banks for originated loans, which is included in the computation of the loan price. That is the reason why the EIR represents a real loan price.

The risk-weighted EIR for loans, in the first three quarters of 2011, recorded a slight declining trend. It is recording a continued decline in comparison to the level from December of 2010 of 8,33%, apart from a moderate increase in January (0,16%), May (0,21%), in July (0,04%), August (0,01%) and in September of 2011 was 8,17.

During the first nine months of 2011, higher oscillations are recorded by the EIR for long-term loans, within 0,58%, than the short term that oscillated within 0,51%.

The risk-weighted EIR for short-term loans, in September of 2011, was 7,50%, which was lower by 0,46 per cent in comparison to December 2010.

The risk-weighted EIR for long-term loans, in September 2011, was 8,99%, which was higher by a 0,3 per cent in comparison to December 2010.

Interest rates for loans originated in the two most significant sectors: economy and citizens[26], over the observing period of 2011, had the same slight decline, with slight oscillations. The risk weighted EIR for loans originated in the economy, although still much lower than the EIR for loans to citizens, decreased from 7,82% in December 2010 to the level of 7,54% in September 2011. In long term loans to economy, the oscillation was within 0,78% and in comparison to the December of 2010 it was higher by 0,26% amounting to 8,08%, while in short term oscillated within 0,53%, and recorded a decline of 0,48% in comparison to December of 2010 and is 7,34%.

In the first nine months of 2011., the total EIR on loans to citizens had a declining trend, it declined from 10,18% to 9,85%. EIR on long term loans from the level in December of 2919 (of 10,05%) decreased in September of 2011 to 9,71%. In September the EIR on short term loans was 12,07%, which is by only 0,58% less than in December of 2010, with present oscillations of 1,56% during the first nine months of 2011.

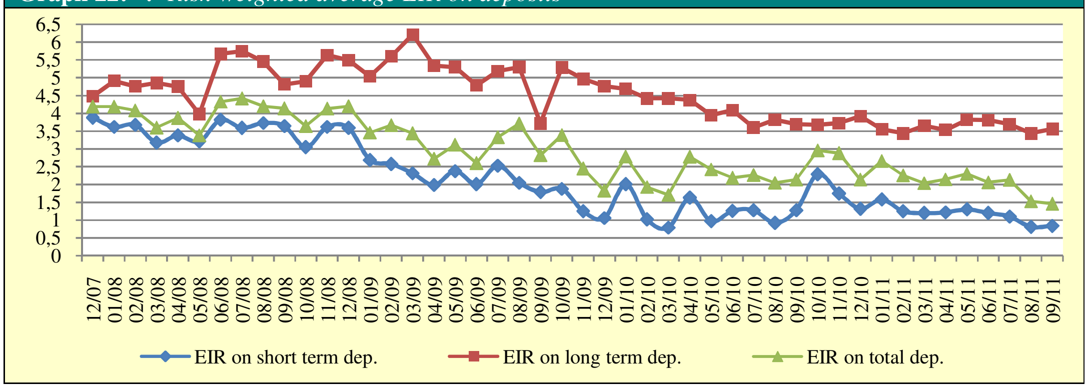
[26] Based on the methodology of classification in sectors: entrepreneurs are included in the sector of citizens.

Risk weighted NIR and EIR on time deposits accrued based on monthly reports are presented in the following table for the banking system:

**Table 30:** *Risk-weighted average NIR and EIR on deposits*

| DESCRIPTION | 31.12.2009. | | 30.06.2010. | | 30.09.2010. | | 31.12.2010. | | 30.06.2011. | | 30.09.2011. | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | NIR | EIR | NIR | EIR | NIR | NIR | EIR | NIR | EIR | NIR | NIR | EIR |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 | 12 | 13 |
| 1. Risk-weighted interest rates on short term deposits | 1,06 | 1,06 | 1,26 | 1,26 | 1,28 | 1,28 | 1,31 | 1,32 | 1,21 | 1,20 | 0,94 | 0,94 |
| 1.1. up to 3 months | 0,72 | 0,72 | 0,39 | 0,39 | 0,69 | 0,69 | 0,97 | 0,97 | 1,01 | 1,01 | 0,78 | 0,78 |
| 1.2. up to 1 year | 2,90 | 2,91 | 3,25 | 3,26 | 2,59 | 2,6 | 2,61 | 2,63 | 2,53 | 2,51 | 2,40 | 2,41 |
| 2. Risk-weighted interest rates on long term deposits | 4,75 | 4,77 | 4,08 | 4,09 | 3,65 | 3,69 | 3,89 | 3,92 | 3,78 | 3,81 | 3,54 | 3,56 |
| 2.1. up to 3 years | 4,72 | 4,74 | 3,86 | 3,87 | 3,44 | 3,47 | 3,78 | 3,80 | 3,64 | 3,65 | 3,44 | 3,45 |
| 2.2. over 3 years | 5,12 | 5,13 | 5,45 | 5,47 | 4,58 | 4,64 | 4,48 | 4,57 | 4,52 | 4,61 | 3,90 | 3,96 |
| 3. Total risk-weighted interest rates on deposits | 1,82 | 1,83 | 2,19 | 2,19 | 2,13 | 2,14 | 2,13 | 2,14 | 2,05 | 2,06 | 1,46 | 1,46 |

**Graph 22:** *: Risk-weighted average EIR on deposits*




As opposed to loans, where the real price is influenced by the expenses associated with loan origination and servicing (under condition they are known at the time of origination), deposits do not show almost any difference between nominal and effective interest rates.

If compared to December 2010, risk-weighted EIR for total term deposits, in September 2011, decreased by 0,68 per cent (from 2,14% to 1,46%). Risk-weighted EIR on short term deposits, had a slight declining trend and in September was 0,94 percent points (December 2010.: 1,32%). Risk-weighted EIR on long term deposits in comparison to December of 2010 recorded a downfall of 0,36 per cent and in September of 2011 is 3,56%.

In September of 2011., the banks paid interest at a significantly lower interest rates on economy deposits (0,73%) than citizens (2,96%). EIR on economy deposits are lower in comparison to December of 2010 by a significant 1,82% (from 2,55% to 0,73%), while the EIR on citizens deposits is on approximately the same level (2,94%). Significant downfall of the average EIR on economy deposits , up to three months, and these deposits carry much lower interest rates.

Risk-weighted interest rates for loans referring to the contracted overdraft and demand deposits, computed based on monthly statements, are presented in the following table:

**Table 31:** *Risk-weighted average NIR and EIR on loans-overdrafts and demand deposits*

| DESCRIPTION | 30.09.2009. | | 31.12.2009. | | 30.09.2010. | | 31.12.2010. | | 30.09.2011. | |
|---|---|---|---|---|---|---|---|---|---|---|
| | NIR | EIR | NIR | EIR | NIR | EIR | NIR | EIR | NIR | EIR |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 |
| 1. Risk-weighted interest rates for loans-overdrafts | 8,71 | 8,72 | 8,96 | 8,96 | 8,78 | 8,78 | 8,29 | 8,29 | 8,89 | 9,02 |
| 2. Risk-weighted interest rates for demand deposits | 0,42 | 0,42 | 0,41 | 0,41 | 0,23 | 0,23 | 0,22 | 0,22 | 0,22 | 0,22 |

The EIR for the above items of assets and liabilities, in general, should be equal to the nominal interest rate. The risk-weighted EIR for total loans in overdrafts for the banking sector, in September of 2011, was 9,02% (an increase of 0,73 per cent in comparison to December 2010), and 0,21% for demand deposits, which was lower by 0,01 per cent in comparison to December 2010.

## 2.4. Liquidity

Liquidity risk management, along with credit risk, is one of the most compound and most important segments of banking operations. Maintaining liquidity in market economy is a permanent task of a bank and main precondition for its sustainability in financial market. This is also one of the key preconditions for establishment and maintenance of the confidence in the banking system of any country, as well as its stability and safety.

Under normal circumstances of banks' performance and stable environment, until the global financial and economic crisis occurred, liquidity risk has had a secondary significance, that is, credit risk was first priority and management systems established, that is, identification, measurement, and control of such risks were under continuous supervision with purpose of its enhancement and improvement. It should be emphasized, however, that during the course of its performance, a correlation of all risks that any bank is or may be exposed to is very high.

Along with turbulences in the financial market due to the global crisis, liquidity risk has rapidly increased and the risk management has become a key factor for normal operating of a bank, as well as timely meeting of past due liabilities and maintenance of a long term position of a bank in regard of its solvency and capital base.

In the last quarter of 2008 the liquidity risk increased after the expansion of the global crises and its adverse impact on the financial and economic system in BiH. Although a part of the savings was withdrawn and the trust in banks was impaired, it was evaluated that the banking system liquidity was not in danger in any given moment, since the banks in FBiH, due to regulatory requirements and proscribed limits, based on a conservative approach, had significant liquid funds and a good liquidity position.

In 2009 the adverse movements from the last quarter of 2008 were stopped, and general liquidity indicators were improved thanks to primarily decreased lending activity, with a tendency of slight deterioration in the 2010., and during 2011., due to decrease of cash funds from slight increase of credit activities, investment in securities and payment of loan liabilities, as well as payment of the long term deposits in one bank during 2010, which had an impact on the deterioration of the maturity structure of the assets and liabilities items. The statement remains that liquidity of the banking system in the Federation of BiH is still good, with satisfactory participation of liquid assets in total assets and coverage of short term liabilities by liquid assets. However, since the financial crisis is still present worldwide which has an adverse reflection to the banking systems of certain European countries, and since majority of banks in FBiH are owned by the European banking groups that provide financial support to our banks through deposit and credit funding, it is estimated that liquidity risk still needs to be under enhanced supervision.

In addition, we should have in mind the fact that impact of the crisis is still present in the real sector, adverse consequences are being reflected to the entire economy environment under which banks operate in BiH, causing delinquency of debtors and increase of nonperforming claims, which is causing decrease in inflow of liquid assets of banks.

Decision on Minimum Standards for Liquidity Risk Management prescribes minimum standards a bank has to establish and maintain in the process of managing this risk, that is, minimum standards to create and implement liquidity policy, which assures bank's ability to fully and immediately perform its liabilities as they become due.

The mentioned regulation represents a framework for liquidity risk management and qualitative and quantitative provisions and requirements towards banks. It prescribes limits banks have to meet in regard to average ten-day minimum and daily minimum of cash assets in relation to short-term sources, as well as minimum limit of maturity adjustment of the instruments of financial assets and liabilities up to 180 days.

Liquidity risk is closely correlated with other risks and often has an adverse effect on banks' success and profitability.

In the structure of financing sources of banks in the Federation of BiH, as of 30.09.2011., deposits still have, although slightly increased, the highest participation of 74,7%, followed by loans taken (including the subordinated debt[27]) with participation of 10,2% with longer maturity, representing quality source for long term placements, and have made a significant contribution to maturity match between assets and liabilities.

On the other hand, the structure of deposits is considerably unfavorable, and after a long period of improvements, has a slight trend of deterioration in 2010, and in 2011., the negative trend was stopped and the maturity structure slightly improved.

- in 000 KM-

**Table 32:** *Maturity structure of deposits*

| DEPOSITS | 31.12.2009. | | 31.12.2010. | | 30.09.2011. | | INDEX | |
|---|---|---|---|---|---|---|---|---|
| | Amount | Partic. % | Amount | Partic. % | Amount | Partic. % | 4/2 | 6/4 |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| Savings and demand deposits | 4.490.845 | 40,7 | 5.054.335 | 45,0 | 5.011.801 | 44,0 | 113 | 99 |
| Up to 3 months | 322.763 | 2,9 | 344.926 | 3,1 | 392.509 | 3,4 | 107 | 114 |
| Up to 1 year | 833.089 | 7,5 | 1.085.115 | 9,6 | 722.974 | 6,4 | 130 | 67 |
| 1. Total short term | 5.646.697 | 51,1 | 6.484.376 | 57,7 | 6.127.284 | 53,8 | 115 | 94 |
| Up to 3 years | 3.292.619 | 29,8 | 2.832.507 | 25,2 | 3.218.688 | 28,2 | 86 | 114 |
| Over 3 years | 2.106.552 | 19,1 | 1.915.947 | 17,1 | 2.046.544 | 18,0 | 91 | 107 |
| 2. Total long term | 5.399.171 | 48,9 | 4.748.454 | 42,3 | 5.265.232 | 46,2 | 88 | 111 |
| TOTAL (1 + 2) | 11.045.868 | 100,0 | 11.232.830 | 100,0 | 11.392.516 | 100,0 | 102 | 101 |

The contracted maturity structure of deposits is relatively good, with the participation of short term loans with 53,8% and long term 46,2%. In comparison to the end of 2010, evident is a slight improvement in the maturity, due to a decrease in participation of short term deposits by 3,9 per cent, and by the same percentage a decrease of long term deposits for the same amount.

[27] Subordinated debt – loans taken and permanent liabilities.

The listed changes in the maturity structure are a result of the decrease of the short term deposits in the first quarter of 2011 by 6% or 357 million KM and a simultaneous increase of the long term deposits by 11% or 517 million KM.

It should be emphasized that in long term deposits, two sectors show dominant participation: citizens with an increased participation from 51,6% to 52,2% and banking institutions with a decrease in participation from 27,4 to 25,3%. In the deposits of up to three years similar the highest participation of 65,6% belongs to citizen deposits with a note that due to the slower increase of this type of deposits than total deposits up to three years, there happened a slight decline of the participation by 1,5%, while in the period over three years the largest participation belongs to banking institutions (at the end of 2010., 60,9%)

However, the remaining maturity is more important for the analyses of liquidity, since it reflects the balance of the deposits for the period from the reporting date to the maturity date, which is presented in the following table:

**Table 33:** *Maturity structure of loans based on the remaining maturity*

| DEPOSITS | 31.12.2009. | | 31.12.2010. | | 30.09.2011. | | RATIO | |
|---|---|---|---|---|---|---|---|---|
| | Amount | Partic. % | Amount | Partic. % | Amount | Partic. % | 4/2 | 6/4 |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| Savings and demand deposits | 4.597.259 | 41,7 | 5.377.075 | 47,9 | 5.185.327 | 45,5 | 117 | 96 |
| Up to 3 months | 819.715 | 7,4 | 776.732 | 6,9 | 795.409 | 7,0 | 95 | 102 |
| Up to 1 year | 2.654.201 | 24,0 | 2.240.255 | 19,9 | 2.360.641 | 20,7 | 84 | 105 |
| 1. Total short term | 8.071.175 | 73,1 | 8.394.062 | 74,7 | 8.341.377 | 73,2 | 104 | 99 |
| Up to 3 years | 2.427.463 | 22,0 | 2.214.874 | 19,7 | 2.464.967 | 21,6 | 91 | 111 |
| Over 3 years | 547.230 | 5,0 | 623.894 | 5,6 | 586.172 | 5,1 | 114 | 94 |
| 2. Total long term | 2.974.693 | 26,9 | 2.838.768 | 25,3 | 3.051.139 | 26,8 | 95 | 107 |
| TOTAL (1 + 2) | 11.045.868 | 100,0 | 11.232.830 | 100,0 | 11.392.516 | 100,0 | 102 | 101 |

Based on the data it can be concluded that the maturity structure of deposits in the remaining maturity is much more poor due to the high participation of the short term deposits of 73,2%. Nevertheless, in the observed period in 2011., there were some slight positive changes, short term deposits declined by 1% or 53 million KM, which resulted in the decline of their participation by 1,5%, while the long term deposits increased by 7% or 212 million KM, and participation from 25,3% to 26,8%. However, if we review the structure of the long term deposits, it is visible that deposits with the remaining maturity of up to 5 years are dominating (81% of long term deposits and 21,6% of total deposits). If maturity data are compared through contracted and remaining maturity, it is clear that around 2,2 billion long term contracted deposits as of 30.09.2011., had a remaining maturity of less than one year.

In the existing maturity structure of deposits, as the largest financing sources of banks in the F BiH, there are increasingly higher limiting factors for credit growth, since banks' biggest need are placements of long term loans. Due to that, the banks are faced with the issue how to secure better quality sources in regard to maturity, especially due to the fact that the inflow of financial funds (borrowings) from abroad had significantly declined, from parent groups as well as from financial institutions - creditors.

In the function of planning for the necessary level of liquid resources, banks have to plan for sources and structure of adequate liquidity potential, along with planning of credit policy. Maturity of placements, that is, credit portfolio is determined by maturity of sources. Since maturity transformation of assets in banks is inherently connected to the functional characteristics of banking performance, banks continuously control and maintain maturity imbalance between sources and placements within prescribed minimum limits.

-in 000 KM-

**Table 33:** *Maturity structure of loans*

| LOANS | 31.12.2009. | | 31.12.2010. | | 30.09.2011. | | RATIO | |
|---|---|---|---|---|---|---|---|---|
| | Amount | Partic. % | Amount | Partic. % | Amount | Partic. % | 4/2 | 6/4 |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| Past due claims and paid off-balance sheet liabilities | 354.200 | 3,6 | 567.182 | 5,7 | 640.794 | 6,2 | 160 | 113 |
| Short term loans | 2.159.008 | 22,0 | 2.129.184 | 21,3 | 2.250.108 | 21,8 | 99 | 106 |
| Long term loans | 7.283.592 | 74,4 | 7.285.545 | 73,0 | 7.414.067 | 72,0 | 100 | 102 |
| TOTAL LOANS | 9.796.800 | 100,0 | 9.981.911 | 100,0 | 10.304.969 | 100,0 | 102 | 103 |

In the observed period in 2011., the long term loans increased by 2% or 129 million KM, short term loans recorded an increase of 6% or 121 million KM, while past due claims increased by 13% or 74 million KM, of which the largest amount, 59 million KM, refers to private companies. In the structure of past due claims, 77% are private companies, 18% are citizens, and 5% are other sectors.

Sector analysis by maturity, in two most significant sectors, indicates that loans to citizens represent 88,8% of long term loans, and loans to private companies, of total originated loans, represent 55% of long term loans.

In the assets structure, as the most significant category, loans still have the highest participation of 67,5%, which has increased by 1,3 per cent in comparison to the end of 2010 due to a slight growth of loans of 3% or 323 million KM.  Cash funds decreased by 6% or 282 million KM and their participation, in comparison to the end of 2010., decreased from 29,5% to 27,3%.

In 2011, banks were regularly meeting a commitment to maintain required reserves with the Central Bank of BiH. The required reserve rate, as of 11.10.2008., decreased to 14% with purpose to enable additional liquidity for banks. In addition, with the same purpose, the CBBiH's decision has been to change basis of the required reserve's computation, so the funds borrowed from nonresidents, based on the contracts signed after 01.11.2008., would not be subject to the basis for computation. As of 01.01.2009., a differentiated required reserve rate has been introduced with regard to the maturity of sources (10% for long term and 14% for short term) and as of 01.05.2009., the rate for long term deposits and borrowings decreased to 7%, and as of 01.02.2011., the rate for short term deposits and borrowings decreased to 10%. Required reserve, as significant instrument of monetary policy in BiH, under the Currency Board and financially underdeveloped market, represents the only instrument of monetary policy used to realize monetary control, in sense of stopping fast credit growth from the past years, and decrease multiplications, as well as an increase of banks' liquidity under an impact of the crisis and intensified outflow of funds from banks that in BiH was experienced after 01.10.2008. On the other hand, implementation of regulation on foreign exchange risk and maintenance of currency adjustment within prescribed limits, also significantly influence the amount of funds banks maintain on the reserve account with the Central Bank in domestic currency, which provides for high liquidity of individual banks and the banking sector.

In liquidity analysis, we use several ratios, and preview of the most significant ones is presented in the following table:

- in %

-

| **Table 35:** *Liquidity ratios* | | | |
|---|---|---|---|
| **RATIOS** | **31.12.2009.** | **31.12.2010.** | **30.09.2011.** |
| 1 | 2 | 3 | 4 |
| Liquid assets[28] / Total assets | 31,9 | 30,2 | 28,5 |
| Liquid assets / Short term financial liabilities | 54,2 | 50,8 | 48,5 |
| Short term financial liabilities / Total financial liabilities | 66,9 | 68,1 | 67,5 |
| Loans / Deposits and Borrowings[29] | 76,4 | 79,0 | 80,9 |
| Loans / Deposits, borrowings and subordinate debts[30] | 75,0 | 77,6 | 79,6 |

All banks continuously meet, considerably above the prescribed minimum, their obligation of a ten-day average of 20% on a comparable basis with the short term funding sources, and daily minimum of 10%, on the same basis, as presented in the following schedule.

- in 000 KM-

| **Table 36:** *Liquidity position – ten-day average and daily minimum* | | | | | |
|---|---|---|---|---|---|
| | **31.12.2009.** | **31.12.2010.** | **30.09.2011.** | **RATIO** | |
| | **Amount** | **Amount** | **Amount** | 3/2 | 4/3 |
| 1 | 2 | 3 | 4 | 5 | 6 |
| 1. Average daily balance of cash assets | 3.789.107 | 3.887.490 | 3.719.202 | 103 | 96 |
| 2. Minimum total daily balance of cash assets | 3.341.965 | 3.585.319 | 3.498.737 | 107 | 98 |
| 3. Short term sources (accrual basis) | 5.431.143 | 6.128.941 | 6.084.404 | 113 | 99 |
| 4.Liabilities: | | | | | |
| 4.1. ten-day average 20% of Item 3 | 1.086.229 | 1.225.788 | 1.216.881 | 113 | 99 |
| 4.2. daily minimum 10% of Item 3 | 543.114 | 612.894 | 608.440 | 113 | 99 |
| *5.Meeting requirement :ten-day average* | | | | | |
| Surplus = Item 1 – Item 4.1. | 2.702.878 | 2.661.702 | 2.502.321 | 98 | 94 |
| *6. Meeting requirement :daily minimum* | | | | | |
| Surplus = Item.2 – Item 4.2. | 2.798.851 | 2.972.425 | 2.890.297 | 106 | 97 |

Apart from the mentioned prescribed minimum standards, monitoring of remaining maturity of financial assets and liabilities, according to the time scale, is of crucial significance for the liquidity position analysis. The time scale is from the aspect of prescribed minimum limits created based on time horizon of up to 180 days.[31]

- in 000 KM -

| **Table 37:** *Maturity of financial assets and liabilities up to 180 days* | | | | | |
|---|---|---|---|---|---|
| **Description** | **31.12.2009.** | **31.12.2010.** | **30.09.2011.** | **RATIO** | |
| | **Amount** | **Amount** | **Amount** | 3/2 | 4/3 |
| 1 | 2 | 3 | 4 | 5 | 6 |
| **I. 1- 30 days** | | | | | |
| 1. Financial assets | 5.719.878 | 5.674.836 | 5.612.631 | 99 | 99 |
| 2. Financial liabilities | 5.070.291 | 5.816.147 | 5.583.660 | 115 | 96 |
| 3. Difference (+ or -) = 1-2 | 649.587 | - 141.311 | 28.971 | N/a | N/a |
| *Accrual of requirement in %* | | | | | |

28 Liquidity assets in the narrow sense: cash and deposits and other financial assets with maturity below three months, except inter-banking deposits.

29 Empiric standards: below 70%-very solid, 71%-75%-satisfactory, 76%-80%-marginal to satisfactory, 81%-85%-insufficient, over 85%-critical.

30 Prior ratio has been modified. Subordinated debts are included in the sources, which gives more realistic indicator.

31 Decision on Changes and Amendments to Decision on Minimum Standards for Liquidity Risk Management in Banks (Official Gazette of the FBiH, number 88/07) dated of 01.01.2008. sets new percentages for maturity matching between financial assets and liabilities: minimum 85% of funding sources (used to be 100%) with maturity up to 30 days must be engaged in placements with maturity up to 30 days; minimum 80% of funding sources (used to be 100%) with maturity up to 90 days in placements with maturity up to 90 days and minimum 75% of funding sources (used to be 95%) with maturity up to 180 days in placements with maturity up to 180 days.

| | | | | | |
|---|---|---|---|---|---|
| a) Performed %= Item 1 / Item 2 | 112,8% | 97,6% | 100,5% | | |
| b) Required minimum % | 85,0 % | 85,0% | 85,0% | | |
| Surplus (+) or shortage (-) = a – b | 27,8 % | 12,6% | 15,5% | | |
| **II. 1-90 days** | | | | | |
| 1. Financial assets | 6.479.395 | 6.408.275 | 6.481.928 | 99 | 101 |
| 2. Financial liabilities | 5.745.023 | 6.450.887 | 6.226.980 | 112 | 97 |
| 3. Difference (+ or -) = 1-2 | 734.372 | - 42.612 | 254.948 | N/a | N/a |
| *Accrual of requirement in %* | | | | | |
| a) Performed %= Item 1 / Item.2 | 112,8 % | 99,3% | 104,1% | | |
| b) Required minimum % | 80,0% | 80,0% | 80,0% | | |
| Surplus (+) or shortage (-) = a – b | 32,8% | 19,3% | 24,1% | | |
| **III. 1-180 days** | | | | | |
| 1. Financial assets | 7.469.752 | 7.343.882 | 7.415.279 | 98 | 101 |
| 2. Financial liabilities | 6.956.965 | 7.509.597 | 7.084.618 | 108 | 94 |
| 3. Difference (+ or -) = 1-2 | 512.787 | - 165.715 | 330.661 | N/a | N/a |
| *Accrual of requirement in %* | | | | | |
| a) Performed %= Item 1 / Item.2 | 107,4% | 97,8% | 104,7% | | |
| b) Required minimum % | 75,0 % | 75,0% | 75,0% | | |
| Surplus (+) or shortage (-) = a – b | 32,4% | 22,8% | 29,7% | | |

Based on the presented data, we may conclude that banks, as of 30.09.2011., were able to meet the required limits, and have managed to realize better maturity match between financial assets and financial liabilities in relation to the limits prescribed. However, of concern is the fact that the maturity match reflect deterioration taken the significantly lower percentages of the surplus over the prescribed minimum, that is, as of 31.12.2010, for the first time in the last two years the amount of the financial liabilities is higher than the amount of the financial assets, in all three time intervals up to 180 days, which was significantly impacted by the return of the long term deposits of one bank to the parent bank before the maturity (just in the fourth quarter of 2010, about 219 million KM). During the first quarter of 2011 the amount of the financial liabilities in all three time intervals up to 180 days was higher than the amount of the financial assets, while in the second quarter there was a slight improvement and the financial assets in the interval up to 180 days were higher somewhat than the financial liabilities, mostly due to the increase of the items of loans and securities kept to maturity reported in the time interval up to 180 days, with a simultaneous decrease of the items of the financial liabilities, mostly liabilities from taken loans. Just in the third quarter (eighth and ninth month) the financial assets were somewhat higher in all three time intervals up to 180 days, mostly as a result of the increase of cash funds and placements to banks, while the financial liabilities up to 180 days remained at approximately the same level. Also, from the aspect of the remaining maturity there is a negative trend of increase of the participation of deposits with maturity up to seven days due to extensive growth of these deposits during 2010 (about 17%), which resulted in an increase of their participation with about 42% to around 48% in total deposits at the end of 2010., and as of 30.09.2011., their participation slightly decreased and was 45,5% and in compliance with the proscribed limits for the maturity match. In part, these funds finance the placements with longer maturities.

Based on all of the above presented indicators, it may be concluded that the negative movements from the last quarter of 2008 were stopped, that there was an improvement during 2009 and that there was a slight deterioration in 2010 that continued in 2011, so the liquidity of the banking system of the Federation of BiH is still assessed as satisfactory. Since this segment of performance and level of liquidity risk exposure correlates to credit risk, having in mind the effects of global financial crisis expansion in BiH and an impact to the banking sector of the FBiH (primarily through a stronger pressure on banks' liquidity), on one side, due to slower inflow of deposits and deterioration of the deposit maturity structure and, on the other side, poor inflow of liquid assets due to downfall in collection of loans and significantly lower borrowings from international financial institutions (which in the previous years was the best quality banks' funding source from the aspect of maturity) it should be emphasized that, in the forthcoming period, banks will have to pay more attention to the liquidity risk management by establishing and implementing liquidity policies, which will make sure that all matured liabilities of banks are timely realized, based on continuous planning of future liquidity needs, and taking into account changes in operating, economic, regulatory and other segments of business environment of banks.

The FBA will, both through reports and on-site examinations of banks, monitor how banks manage this risk, and whether they act in accordance with the adopted policies and programs

### 2.5. Foreign exchange risk – foreign currency matching between assets and liabilities from balance sheet and off-balance sheet items

In their operations, banks are exposed to significant risks coming from potential losses in balance sheet and off-balance sheet items created as a result of price changes in the market. One of those risks is foreign exchange risk (FX) created as a result of changes of exchange rates and/or the imbalance in assets, liabilities and off-balance sheet items of the same currency – individual foreign currency position or all currencies together used by a bank in its operations – overall foreign currency position of a bank.

activities of banks and to decrease influence of foreign exchange risk to their profitability, liquidity and capital, the FBA has issued Decision on Minimum Standards for Foreign Exchange Risk Management in Banks[32] that regulates minimum standards for adoption and implementation of programs, policies and procedures for undertaking, monitoring, control and management of foreign exchange risk, and restrictions prescribed for opened individual and overall foreign exchange position (long or short), calculated in relation to the amount of bank's core capital. [33]

The banks are obliged to report on daily basis to FBA so that FBA can monitor the banks compliance with the prescribed limits and the exposure to the foreign currency risk. Based on examination, monitoring and analysis of submitted reports on foreign currency position of banks, we can conclude that banks meet prescribe limits and perform their FX activities within these limits.

Since the Central Bank functions as the Currency Board and EUR is an anchor currency of the Currency Board, in practice banks are not exposed to foreign exchange risk in case of the most significant currency EUR.

According to the balance as of 30.09.2011., currency structure of banks' assets on the level of banking system recorded participation of items in foreign currencies of 15,1% or 2,3 billion KM (14,8% or 2,2 billion KM at the end of 2010). On the other hand, currency structure of liabilities is essentially different, since participation of liabilities in foreign currency is significantly higher and it amounts to 52,5% or 8,0 billion KM (53,6% or 8,1 billion KM at the end of 2010).

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[32] "Official Gazette of F BiH", Number. 3/03, 31/03, 64/03, 54/04.

[33] Article 8 of Decision on Minimum Standards for Capital Management of Banks determines limits for individual foreign currency position in EUR up to 30% of core capital, for other currencies up to 20% and foreign currency of a bank up to 30%.

The following table presents structure and trend of financial assets and liabilities and foreign currency position for EUR as the most significant currency[34] and total.

- In million KM-

**Table 38:** *Foreign currency adjustment of financial assets and liabilities (EUR and total*

| Description | 31.12.2010. | | | | 30.09.2011. | | | | RATIO | |
|---|---|---|---|---|---|---|---|---|---|---|
| | EURO | | TOTAL | | EURO | | TOTAL | | EURO | TOTAL |
| | Amount | Partic. % | Amount | Partic. % | Amount | Partic. % | Amount | Partic. % | 6/2 | 8/4 |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 |
| *I. Financial assets* | | | | | | | | | | |
| 1. Cash assets | 1.195 | 14,6 | 1.637 | 18,0 | 1.161 | 14,4 | 1.653 | 18,5 | 94 | 101 |
| 2. Loans | 72 | 0,9 | 104 | 1,1 | 67 | 0,8 | 90 | 1,0 | 82 | 87 |
| 3.Loans with currency clause | 6.508 | 79,6 | 6.868 | 75,5 | 6.362 | 78,7 | 6.667 | 74,3 | 99 | 97 |
| 4. Other | 401 | 4,9 | 489 | 5,4 | 491 | 6,1 | 559 | 6,2 | 122 | 114 |
| Total (1+2+3+4) | 8.176 | 100,0 | 9.098 | 100,0 | 8.081 | 100,0 | 8.969 | 100,0 | 99 | 99 |
| *II. Financial liabilities* | | | | | | | | | | |
| 1. Deposits | 5.552 | 71,6 | 6.424 | 74,1 | 5.566 | 71,9 | 6.408 | 74,3 | 100 | 100 |
| 2. Borrowings | 1.328 | 17,1 | 1.363 | 15,7 | 1.264 | 16,3 | 1.293 | 15,0 | 98 | 95 |
| 3.Deposits and loans with currency clause | 584 | 7,5 | 584 | 6,8 | 621 | 8,0 | 621 | 7,2 | 102 | 106 |
| 4.Other | 288 | 3,8 | 296 | 3,4 | 290 | 3,8 | 303 | 3,5 | 107 | 102 |
| Total (1+2+3+4) | 7.752 | 100,0 | 8.667 | 100,0 | 7.741 | 100,0 | 8.625 | 100,0 | 100 | 100 |
| *III. Off-balance sheet* | | | | | | | | | | |
| 1.Assets | 26 | | 28 | | 32 | | 32 | | | |
| 2.Liabilities | 435 | | 438 | | 179 | | 180 | | | |
| *IV.Position* | | | | | | | | | | |
| Long (amount) | 16 | | 21 | | 193 | | 196 | | | |
| % | 1,0% | | 1,3% | | 12,1% | | 12,3% | | | |
| Short | | | | | | | | | | |
| % | | | | | | | | | | |
| Limit | 30% | | 30% | | 30% | | 30% | | | |
| Below limit | 29,0% | | 28,7% | | 17,9% | | 17,7% | | | |

If we analyze the structure of foreign currencies in the financial assets[35] we see a dominant participation of EUR of 74,7, which increased somewhat in comparison to the participation as of 31.12.2010. (74,8%) with the same nominal amount of 1,7 billion KM. Participation of EUR in the liabilities has slightly increased from 88,7% to 89,0%, with a slight decline of the nominal amount from 7,2 to 7,1 billion KM.

However, calculation of the FX risk exposure also includes the amount of indexed items of assets (loans) and liabilities[36], which are especially significant in the assets (74,3% or 6,7 billion KM) this is slightly lower in relation to 31.12.2010. (75,5% or 6,9 billion KM). Other foreign currency assets items represent 25,7% or 2,3 billion KM, of which EUR items make 18,5% or 1,7 billion KM, and other currencies 6,5% or 0,6 billion KM (at the end of 2010, loans contracted with currency clause amounted to KM 6,9 billion with participation of 75,5%, and

[34] Source: Form 5-Foreign currency position.

[35] Source: Form 5-Foreign currency position: portion of financial assets (in foreign currencies denominated in KM). According to the methodology, financial assets are expressed based on net principle (reduced by loan loss reserves).

[37] In order to protect from changes of the exchange rate banks contract certain items of assets (loans) and liabilities with currency clause (regulation allow only two-way currency clause).

other items in EUR of 18,3% or 1,7 billion KM). Of total net loans (9,6 billion KM), 69,5% were contracted with currency clause, primarily tied to EUR (95,4%).

On the other hand, the structure of financial liabilities stipulates and determines the structure of financial assets, for each currency individually. In foreign currency liabilities (8,6 billion KM) items in EUR (primarily deposits) had the highest participation of 82,6% or 7,1 billion KM, while participation and amount of indexed liabilities was at minimum, amounting to 7,2% or 0,6 billion KM (at the end of 2010, participation of liabilities in EUR was 82,7% or 7,2 billion KM, while indexed liabilities were 6,8% or 0,6 billion KM).

Observed by banks and overall on the level of the banking system of the FBiH, we can conclude that foreign exchange risk exposure of banks and the system, in the past three quarters of 2011, ranged within the prescribed limits. As of 30.09.2011., there were 13 banks with long foreign currency position, and six banks with short position. At the system level, long foreign currency position represented 12,3% of banks' core capital, which is lower by 17,7% than the limit. Individual foreign currency position for EURO was at 12,1%, representing a decline of 17,9% than the limit, with financial assets items being higher than financial liabilities ( net long position).

Although in the environment of the Currency Board banks are not exposed to foreign exchange risk in the most significant currency EUR, they are still required to operate within prescribed limits for individual currencies and for total foreign currency position and to daily manage this risk in accordance with adopted programs, policies, procedures and plans.

# IV CONCLUSIONS AND RECOMMENDATIONS

Banking sector of the Federation of BiH during the period of implementation of the reform has reached an enviable level. The upcoming activities should be aimed at preserving its stability as priority task in the current stressful conditions, and its further progress and development. These goals require continuous and vigilant engagement of all parts of the system, legislative and executive authorities, which is a prerequisite to create the most favorable economic environment that would be stimulating to both banks and consequently to the real sector of the economy and citizens.

In the upcoming period, the Banking Agency of the Federation of BiH shall:

- Take measures and activities within its powers to overcome and mitigate adverse effects to the banking sector of the FBiH caused by the global financial crisis,
- Continue implementing activities, from the scope of its authority, to consolidate supervision on state level,
- Proceed with a continues supervision of banks through on-site and off-site examinations, focusing on targeted examination of dominant risk segments of banking operations, which will make supervision more effective, in regard to:

  - Persist on capital strengthening of banks, especially those recording outstanding assets growth and decrease of capital adequacy ratio,
  - Continue permanent monitoring of banks, primarily those with systemic importance to development of credit activities with the highest concentration of savings and other deposits in order to protect depositors,
  - Continue a systematic monitoring of banks' activities in prevention of money laundering

and terrorism financing and improve cooperation with other supervisory and examination institutions,
- Maintain continuity in payment system examinations,
- Continue working on further development of regulation based on the Basle Principles, the Basle Capital Accord, and the European Banking Directives, as part of BiH's preparation to join the European Union,
- Establish and expand cooperation with home country supervisors of the investors present in the banking sector of the FBiH, and other countries in order to have more effective supervision,
- Improve cooperation with the Banks Association in all banking performance segments, organization of counseling and professional assistance in the area of implementation of banking laws and regulations, advancement of cooperation in regard to professional development, proposed changes of all legislative regulations that have become a limiting factor to banks' development, introduction of new products, collection of claims and fully involve in building up and functioning of the unified registry of irregular debtors – legal entities and citizens, with daily data update.

- Continuous operational development of the IT system for early warning and prevention in elimination of weaknesses in banks;
- Work on continuous education and training of staff;
- Make effort to accelerate finalization of the remaining provisional administrations and liquidations based on the conclusion made by the Management Board;
- Particularly, accelerate resolution of unsettled issues with the Government of BiH in relation to the Provisional Administration of Hercegovačka Bank d.d. Mostar related to terminal Dretelj.

In addition, it is necessary to have stronger involvement of other authorized institutions and bodies of Bosnia and Herzegovina and the Federation of BiH in order to:

- Realize Program of measures to mitigate effects of the global economic crisis and improve the business environment, as accepted by the Economic Social Council in the territory of the FBiH in December 2008, pursuant to the document issued by the FBiH Government;
- Realize the conclusion made by the Federation of BiH Parliament to establish banking supervision on state level;
- Form an opinion about status of banks owned by the Federation of BiH;
- Create and further develop the financial sector regulation related to the activity, status and performance of micro-credit organizations, leasing companies, insurance companies, etc.;
- Accelerate implementation of economic reform in the real sector in order to reach the level of the monetary and banking sector;
- Prepare for creation of legislative regulation for the banking sector and financial system based on the Basle Principles, the Basle Capital Accord, and the European Banking Directives,
- Establish specialized court departments for economy,
- Establish more efficient process for realization of pledges,
- Adopt law on protection of creditors and full responsibility of debtors,
- Adopt law or improve existing legislation regulating the area of safety and protection of money in banks and in transportation.

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

- Full dedication to good quality and prudent performance, and actions to cope with the crisis impact that presently represents the greatest danger for banks and the real sector of the economy and citizens;

- Further capital strengthening and level of solvency proportional to the growth of assets and risk, higher profitability, more consistent implementation of adopted policies and procedures in the area of prevention of money laundering and terrorism financing, and safety and protection of money in banks and in transportation, in accordance with laws and regulations;
- Strengthen internal control systems and internal audit functions as fully independent in performing their duties and roles;
- Regular, updated and accurate submission of data to the Central Loan Registry and Unified Central Account Registry with the Central Bank of BiH.

Number: U.O.- 35 - 2/11.
Sarajevo, 05.12.2011.

## ATTACHMENTS

**ATTACHMENT 1**

## Banks in the Federation of Bosnia and Herzegovina - 30.09.2011.

| No. | BANK | Address | | Telephone | Director |
|---|---|---|---|---|---|
| *1* | BOSNA BANK INTERNATIONAL dd - SARAJEVO | Sarajevo | Trg djece Sarajeva bb | 033/275-100, fax:203-122 | AMER BUKVIĆ |
| *2* | BOR BANKA dd - SARAJEVO | Sarajevo | Obala Kulina bana 18 | 033/663-500, fax:278-550 | HAMID PRŠEŠ |
| *3* | HERCEGOVAČKA BANKA dd - MOSTAR | Mostar | Nadbiskupa Čule bb | 036/332-901, fax:332-903 | Privr.upravitelj - Nikola Fabijanić - 16.04.2007. |
| *4* | HYPO ALPE-ADRIA-BANK dd - MOSTAR | Mostar | Kneza Branimira 2b | 036/444-444, fax:444-235 | MICHAEL VOGT |
| *5* | INVESTICIONO-KOMERCIJALNA BANKA dd - ZENICA | Zenica | Trg B&H 1 | 032/448-400, fax:448-501 | SUVAD IBRANOVIĆ |
| *6* | INTESA SANPAOLO BANKA D.D. BOSNA I HERCEGOVINA | Sarajevo | Obala Kulina bana 9a. | 033/497-555, fax:497-589 | ALMIR KRKALIĆ |
| *7* | KOMERCIJALNO-INVESTICIONA BANKA DD V.KLADUŠA | V.Kladuša | Ibrahima Mržljaka 3 | 037/771-253, fax:772-416 | HASAN PORČIĆ |
| *8* | MOJA BANKA dd - SARAJEVO | Sarajevo | Kolodvorska br. 5. | 033/720-070, fax:720-100 | OGNJEN SAMARDŽIĆ |
| *9* | NLB TUZLANSKA BANKA dd - TUZLA | Tuzla | Maršala Tita 34 | 035/259-259, fax:250-596 | ALMIR ŠAHINPAŠIĆ |
| *10* | POŠTANSKA BANKA BiH dd - SARAJEVO | Sarajevo | Put zivota 2. | 033/564-000, fax: 564-050 | Privr.upravitelj - Stjepan Jovičić - 05.10.2010. |
| *11* | PRIVREDNA BANKA SARAJEVO dd - SARAJEVO | Sarajevo | Alipašina 6 | 033/277-700, fax:664-175 | AZEMINA GOLO |
| *12* | PROCREDIT BANK dd - SARAJEVO | Sarajevo | Emerika Bluma 8. | 033/250-950, fax:250-971 | FRIEDER WOEHRMANN |
| *13* | RAIFFEISEN BANK dd BiH - SARAJEVO | Sarajevo | Zmaja od Bosne bb. | 033/755-010, fax: 213-851 | MICHAEL MÜLLER |
| *14* | RAZVOJNA BANKA FEDERACIJE BIH | Sarajevo | Igmanska 1 | 033/277-900, fax: 668-952 | RAMIZ DŽAFEROVIĆ |
| *15* | SPARKASSE BANK dd - SARAJEVO | Sarajevo | Zmaja od Bosne br. 7. | 033/280-300, fax:280-230 | SANEL KUSTURICA |
| *16* | TURKISH ZIRAAT BANK BOSNIA dd - SARAJEVO | Sarajevo | Dženetića Čikma br. 2. | 033/252-230, fax: 252-245 | Privremeni direktor - Ozcan Asanoglu |
| *17* | UNICREDIT BANK dd - MOSTAR | Mostar | Kardinala Stepinca bb | 036/312-112, fax:312-121 | BERISLAV KUTLE |
| *18* | UNION BANKA dd - SARAJEVO | Sarajevo | Dubrovačka 6 | 033/561-000, fax: 201-567 | ESAD BEKTEŠEVIĆ |
| *19* | VAKUFSKA BANKA dd - SARAJEVO | Sarajevo | M. Tita 13. | 033/280-100, fax: 663-399 | AMIR RIZVANOVIĆ |
| *20* | VOLKSBANK BH dd - SARAJEVO | Sarajevo | Fra Anđela Zvizdovića 1 | 033/295-601, fax:295-603 | REINHOLD KOLLAND |

**ATTACHMENT 2**

## BALANCE SHEET OF BANKS IN THE FBiH - FBA SCHEDULE
## ACTIVE SUB-BALANCE SHEET

in 000 KM

| No. | DESCRIPTION | 31.12.2009. | 31.12.2010. | 30.09.2011. |
|---|---|---|---|---|
| | **ASSETS** | | | |
| 1. | Cash funds and deposit accounts at depository institutions | 4.782.301 | 4.443.614 | 4.161.321 |
| 1a | Cash and non-interest deposit accounts | 490.171 | 452.188 | 408.868 |
| 1b | Interest deposit accounts | 4.292.130 | 3.991.426 | 3.752.453 |
| 2. | Trading securities | 12.884 | 233.178 | 285.374 |
| 3. | Placements in other banks | 111.019 | 145.007 | 278.418 |
| 4. | Loans, receivables in leasing and past due receivables | 9.796.800 | 9.981.911 | 10.304.969 |
| 4a | Loans | 9.442.455 | 9.414.597 | 9.664.052 |
| 4b | Receivables on leasing | 145 | 132 | 123 |
| 4c | Past due receivables - loans and leasing | 354.200 | 567.182 | 640.794 |
| 5. | Securities held until maturity | 106.273 | 142.074 | 175.700 |
| 6. | Premises and other fixed assets | 503.157 | 521.625 | 506.515 |
| 7. | Other real estate | 25.753 | 31.139 | 37.482 |
| 8. | Investments in non-consolidated related enterprises | 42.693 | 44.753 | 42.007 |
| 9. | Other assets | 336.287 | 193.609 | 206.488 |
| 10. | MINUS: Reserves for potential losses | 480.807 | 661.213 | 742.914 |
| 10a | Reserves on item 4 in Assets | 458.803 | 635.792 | 716.029 |
| 10b | Reserves on Assets except item 4 | 22.004 | 25.421 | 26.885 |
| **11.** | **TOTAL ASSETS** | 15.236.360 | 15.075.697 | **15.255.360** |
| | **LIABILITIES** | 0 | 0 | 0 |
| 12. | Deposits | 11.045.868 | 11.232.830 | 11.392.516 |
| 12a | Interest deposits | 10.180.008 | 10.134.101 | 10.365.208 |
| 12b | Non-interest deposits | 865.860 | 1.098.729 | 1.027.308 |
| 13. | Loans - past due | 2.744 | 1.723 | 1.826 |
| 13a | Balance of payable loans, unpaid | 0 | 0 | 0 |
| 13b | Unpaid - called for payment off-balance sheet items | 2.744 | 1.723 | 1.826 |
| 14. | Loans from other banks | 3.089 | 7.000 | 2.000 |
| 15. | Payables to Government | 0 | 0 | 0 |
| 16. | Payables on loans and other borrowings | 1.771.978 | 1.403.451 | 1.344.522 |
| 16a | payable within one year | 678.608 | 381.305 | 374.281 |
| 16b | payable longer than one year | 1.093.370 | 1.022.146 | 970.241 |
| 17. | Subordinated debts and subordinated bonds | 250.483 | 226.847 | 208.560 |
| 18. | Other liabilities | 484.500 | 507.221 | 556.754 |
| **19.** | **TOTAL LIABILITIES** | 13.558.662 | 13.379.072 | **13.506.178** |
| | **C A P I T A L** | 0 | 0 | 0 |
| 20. | Permanent priority shares | 25.028 | 25.028 | 26.059 |
| 21. | Common shares | 1.145.627 | 1.148.269 | 1.167.513 |
| 22. | Shares issued | 143.725 | 136.485 | 136.485 |
| 22a | Permanent priority shares | 8.420 | 8.420 | 8.420 |
| 22b | Common shares | 135.305 | 128.065 | 128.065 |
| 23. | Undistributed income and capital reserves | 358.480 | 489.557 | 377.157 |
| 24. | Currency rate difference | 0 | 0 | 0 |
| 25. | Other capital | 4.838 | -102.714 | 41.968 |
| **26.** | **TOTAL CAPITAL (20. TO 25.)** | 1.677.698 | 1.696.625 | **1.749.182** |
| **27.** | **TOTAL LIABILITIES AND CAPITAL (19+26)** | 15.236.360 | 15.075.697 | **15.255.360** |
| | **PASSIVE AND NEUTRAL SUB BALANCE** | **622.094** | **659.059** | |
| | **TOTAL BALANCE SHEET IN BANKS** | **15.859.732** | **15.734.756** | **15.764.546** |

**ATTACHMENT 3**

## NEW CITIZEN SAVINGS BY PERIODS IN THE BANKS IN FBiH

In ' 000 KM

| | 31.12.2009. | 31.12.2010. | 30.09.2011. |
|---|---|---|---|
| State banks | 35.275 | 47.148 | 51.147 |
| Private banks | 4.325.928 | 4.926.361 | 5.209.168 |
| **TOTAL** | **4.361.203** | **4.973.509** | **5.260.315** |

**ATTACHMENT 4**

## CLASSIFICATION OF ASSETS AND OFF-BALANCE SHEET RISK ITEMS IN BANKS IN FBiH
## As of 30.09.2011.

### - ACTIVE BALANCE SHEET -

in '000 KM

| No. | BALANCE SHEET ASSETS AND OFF-BALANCE SHEET ITEMS | C L A S I F I C A T I O N | | | | | TOTAL |
|---|---|---|---|---|---|---|---|
| | | A | B | C | D | E | |
| 1. | Short-term loans | 1.891.584 | 331.923 | 24.810 | 1.638 | 153 | 2.250.108 |
| 2. | Long-term loans | 6.010.558 | 809.279 | 382.706 | 211.513 | 11 | 7.414.067 |
| 3. | Other placements | 452.810 | 244 | 85 | 797 | 2 | 453.938 |
| 4. | Interest accrued | 39.827 | 11.251 | 13 | 2 | 3 | 51.096 |
| 5. | Past due receivables | 67.006 | 72.964 | 159.171 | 341.278 | 4 | 640.423 |
| 6. | Receivables on guarantees paid | 220 | 74 | 77 | 0 | | 371 |
| 7. | Other assets | 5.168.998 | 9.109 | 3.925 | 2.390 | 3.849 | 5.188.271 |
| **8.** | **TOTAL ACTIVE BALANCE SHEET** | **13.631.003** | **1.234.844** | **570.787** | **557.618** | **4.022** | **15.998.274** |
| | a) Guarantees payable | 356.052 | 60.387 | 1.177 | 231 | | 417.847 |
| 9. | b) Performing guarantees | 495.223 | 104.388 | 489 | 1.602 | | 601.702 |
| 10. | Unsecured LoC | 55.473 | 7.048 | | | | 62.521 |
| 11. | Irrevocable loans | 1.360.550 | 41.117 | 5.069 | 1.535 | 251 | 1.408.522 |
| 12. | Other potential liabilities | 14.870 | 2.034 | | 116 | | 17.020 |
| **13.** | TOTAL OFF-BALANCE SHEET | **2.282.168** | **214.974** | **6.735** | **3.484** | **251** | **2.507.612** |
| **14.** | TOTAL BALANCE AND OFF-BALANCE SHEET (8+13) | **15.913.171** | **1.449.818** | **577.522** | **561.102** | **4.273** | **18.505.886** |
| 15. | General credit risk and potential loan losses (#14 x % of loss) | 220.392 | 120.919 | 142.870 | 316.810 | 4.273 | 805.264 |
| 16. | Allocated general reserves (A) and special reserves (B, C, D, E) | 220.084 | 120.919 | 142.870 | 316.810 | 4.258 | 804.941 |
| **17.** | **MORE (LESS) of the allocated reserves (#16 - 15) +or -** | **-308** | **0** | **0** | **0** | **-15** | **-323** |

**ATTACHMENT 5**

# INCOME STATEMENT

in '000 KM

| ELEMENTS | PERFORMED **30.09. 2010.** | | PERFORMED **30.09.2011.** | | RATIO 4 : 2 |
|---|---|---|---|---|---|
| | Amount | Partic.in total income | Amount | Partic. in total income | |
| **INCOME** | | | | | |
| Interest income | 640.954 | 103% | 637.296 | 94% | 99 |
| Interest expenses | 249.542 | 40% | 219.787 | 32% | 88 |
| Net interest income | 391.412 | 63% | 417.509 | 62% | 107 |
| Fee income and other operating income | 228.901 | 37% | 259.386 | 38% | 113 |
| **TOTAL INCOME** | 620.313 | 100% | 676.895 | 100% | 109 |
| EXPENSES | | | | | |
| Reserves for potential losses | 264.900 | 43% | 206.140 | 30% | 78 |
| Salaries and contribution expenses | 181.300 | 29% | 186.587 | 28% | 103 |
| Fixed assets and overhead expenses | 111.980 | 18% | 118.515 | 18% | 106 |
| Other expenses | 120.835 | 19% | 124.161 | 18% | 103 |
| TOTAL EXPENSES (without interests) | 679.015 | 109% | 635.403 | 94% | 94 |
| NET INCOME BEFORE TAX | -58.702 | -9% | 41.492 | 6% | N/A |
| Income Tax | -39 | 0% | 20 | 0% | |
| **NET INCOME** | -58.663 | -9% | 41.472 | 6% | N/A |

ATTACHMENT 6

## COMPARATIVE SCHEDULE OF CAPITAL BALANCE AND ADEQUACY IN BANKS IN FBiH
## ACTIVE SUB-BALANCE SHEET

'000 KM

| No. | DESCRIPTION | 31.12.2009. | 31.12.2010. | 30.09.2011. |
|---|---|---|---|---|
| **1** | **BANK'S CORE CAPITAL** | | | |
| 1.a. | Share capital, reserves and income | | | |
| 1.1. | Share capital - common and perm. priority non-cumulat. shares - cash payments | 1.155.790 | 1.157.918 | 1.177.932 |
| 1.2. | Share capital - comm. and perm. prior. non-cumul. shares-invested posses. And rights | 12.550 | 12.550 | 12.550 |
| 1.3. | Issued shares income at share payments | 143.725 | 136.485 | 136.485 |
| 1.4. | General regulatory reserves (reserves as regulated by the Law) | 78.317 | 183.807 | 189.307 |
| 1.5. | Other reserves not related to assets quality assessment | 201.758 | 228.867 | 262.724 |
| 1.6. | Retained - undistributed income from previous years | 161.562 | 165.532 | 175.669 |
| **1.a.** | **TOTAL ( from 1.1. to 1.6.)** | **1.753.702** | **1.885.159** | **1.954.667** |
| 1.b. | Offsetting items from 1.a. | | | 0 |
| 1.7. | Uncovered losses transferred from previous years | 82.324 | 92.058 | 250.052 |
| 1.8. | Losses from current year | 52.966 | 157.933 | 58.594 |
| 1.9. | Book value of treasury shares owned by the bank | 595 | 81 | 81 |
| 1.10. | Amount of intangible assets | 63.119 | 63.249 | 59.665 |
| **1.b.** | **TOTAL (from 1.7.to 1.10.)** | 199.004 | 313.321 | 368.392 |
| **1.** | **AMOUNT OF CORE CAPITAL: ( 1.a.-1.b.)** | **1.554.698** | **1.571.838** | **1.586.275** |
| **2** | **BANK'S SUPPLEMENTARY CAPITAL** | | | |
| 2.1. | Share capital - common and perm. priority non-cumulat. shares - cash payments | 2.829 | 2.829 | 3.090 |
| 2.2. | Share capital - comm. and perm. prior. non-cumul. shares-invested posses. And rights | 0 | 0 | 0 |
| 2.3. | General reserves for losses on loans from class. A - performing assets | 205.254 | 209.612 | 220.084 |
| 2.4. | Accrued income for current year audited and confirmed by external auditor | 49.186 | 52.090 | 0 |
| 2.5. | Income under FBA's temporary restriction on distribution | 0 | 0 | 0 |
| 2.6. | Subordinated debts, the most 50% of core capital | 184.093 | 159.056 | 142.114 |
| 2.7. | Hybrid convertible items - the most 50% of core capital | 0 | 0 | 0 |
| 2.8. | Items-permanent liabilities without repayment duty | 66.390 | 66.399 | 66.400 |
| **2.** | **AMOUNT OF SUPPLEMENTARY CAPITAL: (from 2.1. to 2.8.)** | **507.752** | **489.986** | **431.688** |
| **3** | **OFFSETTING ITEMS FROM BANK'S CAPITAL** | | | |
| 3.1. | Part of invested share capital that according to FBA's assessment represents accepted and overestimated value | 0 | 0 | 0 |
| 3.2. | Investments in capital of other legal entities exceeding 5% of bank's core capital | 16.036 | 15.938 | 18.538 |
| 3.3. | Receivables from shareholders for significant voting shares - approved aside from regulations | 0 | 0 | 0 |
| 3.4. | VIKR to shareholders with significant voting shares in the bank without FBA's permission | 0 | 0 | 0 |
| **3.** | **AMOUNT OF OFFSETTING ITEMS FROM BANK'S CAPITAL (3.1. to 3.4.)** | **16.036** | **15.938** | **18.538** |
| **A.** | **AMOUNT OF BANK'S NET CAPITAL (1.+2.-3.)** | **2.046.414** | **2.045.886** | **1.999.425** |
| **B.** | **RISK FROM RISK-WEIGHTED ASSETS AND CREDIT EQUIVALENTS** | **11.790.234** | **11.713.116** | **12.096.510** |
| **C.** | **POR ( RISK-WEIGHTED OPERATING RISK )** | **882.928** | **942.707** | **965.932** |
| **D.** | **PTR ( RISK-WEIGHTED MARKET RISK )** | 0 | 0 | **0** |
| **E.** | **TOTAL RISK-WEIGHTED RISKS B+C+D** | **12.673.162** | **12.655.823** | **13.062.442** |
| **F.** | **NET CAPITAL RATE (CAPITAL ADEQUACY) (A.:B.) X 100** | **16,4%** | **16,2%** | **15,3%** |

**ATTACHMENT 7**

## NUMBER OF EMPLOYEES BY BANKS

| No. | BANK | 31.12.2009. | 31.12.2010. | 30.09.2011. |
|---|---|---|---|---|
| 1 | BOR BANKA dd SARAJEVO | 51 | 54 | 57 |
| 2 | BOSNA BANK INTERNATIONAL dd Sarajevo | 185 | 207 | 225 |
| 3 | HERCEGOVACKA BANKA dd MOSTAR | 77 | 75 | 74 |
| 4 | HYPO ALPE ADRIA BANK dd MOSTAR | 600 | 568 | 645 |
| 5 | INTESA SANPAOLO BANKA dd BiH | 514 | 519 | 525 |
| 6 | INVESTICIONO KOMERCIJALNA BANKA dd ZENICA | 174 | 178 | 172 |
| 7 | KOMERCIJALNO INVESTICIONA BANKA dd VELIKA KLADUŠA | 68 | 67 | 71 |
| 8 | MOJA BANKA dd SARAJEVO | 133 | 143 | 170 |
| 9 | NLB TUZLANSKA BANKA dd TUZLA | 473 | 474 | 475 |
| 10 | POŠTANSKA BANKA dd SARAJEVO | 111 | 91 | 88 |
| 11 | PRIVREDNA BANKA dd SARAJEVO | 195 | 211 | 189 |
| 12 | PROCREDIT BANK dd SARAJEVO | 662 | 501 | 449 |
| 13 | RAIFFEISEN BANK BH dd SARAJEVO | 1.669 | 1.630 | 1.590 |
| 14 | SPARKASSE BANK dd SARAJEVO | 426 | 426 | 430 |
| 15 | TURKISH ZIRAAT BANK dd SARAJEVO | 152 | 150 | 155 |
| 16 | UNA BANKA dd BIHAĆ | 56 | - | - |
| 17 | UNI CREDIT BANKA BH dd MOSTAR | 1.389 | 1.362 | 1.344 |
| 18 | UNION BANKA dd SARAJEVO | 175 | 180 | 178 |
| 19 | VAKUFSKA BANKA dd SARAJEVO | 212 | 222 | 229 |
| 20 | VOLKSBANK BH dd SARAJEVO | 334 | 330 | 334 |
| | **TOTAL** | **7.656** | **7.388** | **7.400** |