



**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 December 31st, 2009**

Sarajevo, March 2010

Information on banking system of the Federation of BiH (as of December 31st, 2009 upon the final non-audited 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	1
II	SUPERVISION OF BANKING SYSTEM	6
	1. BANKING AGENCY	6
	2. BANKING SUPERVISION	7
	3. COMBAT AGAINST MONEY LAUNDERING AND TERRORISM FINANCING	9
III	BUSINESS PERFORMANCE OF BANKS IN THE FEDERATION OF BIH	11
	1. STRUCTURE OF THE BANKING SECTOR	
	1.1. Status, number and business network	11
	1.2. Ownership structure	12
	1.3. Employees	15
	2. FINANCIAL INDICATORS OF THE PERFORMANCE	
	2.1. Balance sheet	17
	2.1.1. Liabilities	22
	2.1.2. Capital – strength and adequacy	26
	2.1.3. Assets and asset quality	30
	2.2. Profitability	37
	2.3. Risk-weighted nominal and effective interest rates	41
	2.4. Liquidity	45
	2.5. Foreign exchange risk	50
IV	CONCLUSION	52
	ATTACHMENTS	55

I INTRODUCTION

As affected by general alert and the global economic and financial crisis in the real sector, the banking sector in the Federation of BiH, in 2009, displayed a level of stagnation, which, apart from other things, is reflected through the decrease of credit activities, increase of outstanding loans, lack of good quality lending projects, and decreased profitability.

However, in spite of all difficulties, banks were quite successful in managing the crisis. They have realized the performance that enabled a solid stability of this sector and preserved confidence of their customers, along with the increased concern and focus on liquidity and credit risk. In this process, along with decreasing overall number of organizational units, and increasing number of ATMs, number of employees in banks decreased by over 4%.

With an aim to hinder the adverse effects of the economic crisis, the Management board of Banking Agency of the Federation of BiH adopted the Decision on temporary renegotiation of citizens and legal entities' credit liabilities in the banks in order to extend the final maturity date for credit repayment and resulting decrease of credit installments.

Encourages the fact that majority of banks in BiH, that are in the ownership of the foreign groups, while implementing the "Vienna Initiative", that is the agreement for the continuation of financing the citizens and economy of Bosnia and Herzegovina, maintained their financial support on the level of 31.12.2008. This is of great importance for the overall performance security of the banking sector in the FBiH.

At the end of 2009, there were 20 banks with banking license issued in the Federation of BiH, of which 18 majority private owned and 2 majority state owned. The banks under provisional administration were UNA bank d.d. Bihać and Hercegovacka bank d.d. Mostar.

The aggregate balance sheet of banks, at the end of 2009, was 15,2 billion KM (by 1% or 163 million KM higher than at the end of 2008) with obvious domination of five largest banks in the system, holding approximately 80% of the market, loans, deposits and capital. The increase of the aggregate balance sheet in the sources was mainly supported by the increase of deposits of 6% or 584 million KM, while the same was significantly annulled by the decrease of loans taken (credit indebtedness of banks).

Fourteen banks have higher assets when compared to the end of 2008, while the remaining 6 banks recorded a downfall

Regulatory capital of banks in the FBiH, as of 31.12.2009., as well as net capital, amounted to two billion KM, whereas its structure was significantly improved, since supplementary capital was decreased, but core capital was increased for the most part from distribution of profit generated in 2008 to capital and the new additional capitalization.

The most significant change in the assets of banks was the increase of cash funds by 14% or 575 million KM (from 4,2 billion KM to 4,8 billion KM), primarily as an effect and result of the restrictive credit policy of banks and decreased lending activities in 2009, with simultaneous growth of deposits and inflow of cash funds from the first tranche of the stand-by arrangement with the IMF.

In 2009, credit placements decreased by 6% or 638 million KM. As of 31.12.2009., the mentioned items amounted to 9,8 billion KM.

Deposits with participation of 72,5% and amount of 11 billion KM still represent the most significant source of funding for banks in the FBiH. Positive movements are of special importance for citizen, which apart from the adverse economic circumstances in 2009, were increased by 8% or 325 million KM, amounting to 4,51 billion KM at the end of 2009. On contrary, in the sector of private enterprises, deposits amount to 1,4 billion KM, and in total, at the end of 2009, they decreased by 87 million KM.

Maintaining confidence in banks and safety and stability of the banking sector is confirmed with the data that savings as of 31.12.2009., following slight downfall in the first quarter, reached the amount of 4,36 billion KM.

The banking system in the Federation of BiH, in 2009, generated minimum profit of nine thousand KM, while the profit in 2008 was 50 million KM. Positive financial result of 52.975 thousand KM was generated by 13 banks, which is lower by 41% or 36 million KM than in 2008, and the loss of 52.966 thousand KM was reported by seven banks, that is, 36% or 14 million KM was higher than in 2008.

Reasons to decline of the entire sector's success in 2009 were credit activities deterioration along with unemployed cash funds increase, as well as the significant increase of loan loss provisioning due to asset quality deterioration.

And finally, we could conclude that in 2009 adverse movements from the last quarter of 2008 were stopped in the segment of liquidity risk, while the general liquidity indicators were improved.

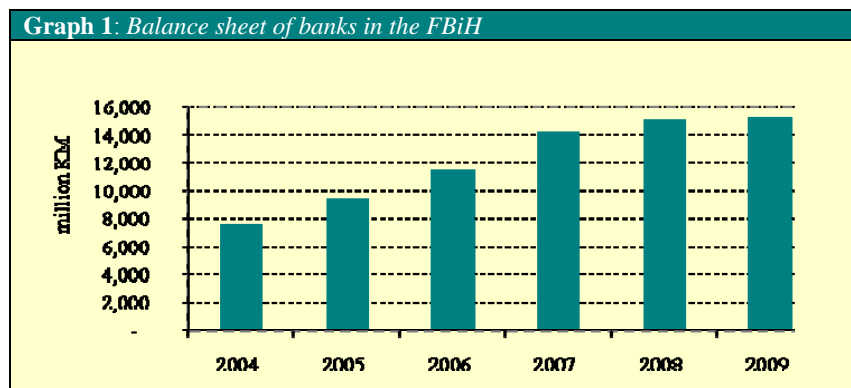
• **Growth and development of the banking sector and ownership structure:** The following table presents changes in the number and ownership structure of banks over the last five years.

Table 1: Review of changes in the number and ownership structure of banks			
	State banks	Private banks	TOTAL
31.12.2004.	6	18	24
No changes in 2005.			
31.12. 2005.	6	18	24
Changes in 2006:			
-licenses revoked	-1		-1
- new licenses		+1	+1
-merger with/integration into		-1	-1
31.12.2006.	5	18	23
Changes in 2007:			
- merger with/integration into		-1	-1
- ownership str.changes	-2	+2	
31.12.2007.	3	19	22
Changes in 2008:			
- merger with/integration into		-1	-1
- licenses revoked ¹	-1		-1
31.12.2008.	2	18	20
No changes in 2009.			
31.12.2009.	2	18	20

¹ Development Bank of the F BiH, as of 01.07.2008., became a legal successor of the Investment Bank of the F BiH d.d. Sarajevo.

Balance sheet

As affected by the global economic and financial crisis and adverse effects to the overall economy, the banking sector in was characterized by stagnation, that is, minimum growth of the aggregate balance sheet and decline of credit activities. The assets of banks recorded an insignificant growth of 1% or 163 million KM, reaching the amount of 15,2 billion KM. Over the past five years or in the period since the beginning of 2005 to the end of 2009, the aggregate balance sheet of the system increased by more than 2 times.



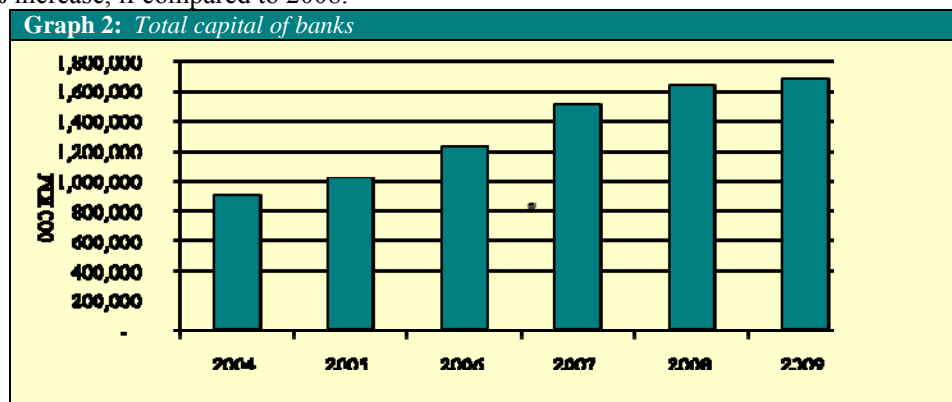
The minimum growth of the aggregate balance sheet of only 1%, in comparison to 2008, in the sources was realized through the increase of deposits by 584 million KM or 6%, capital by 37 million KM or 2%, while loans taken were decreased by 405 million KM or 19%.

In the assets of banks, the most significant item were credit placements with participation of 64,3% that in 2009 were decreased by 638 million KM or 6%, amounting to 9,8 billion KM. Most part of the decrease (567 million KM) referred to two dominant sectors, private enterprises and citizens, participating with 96,6% as of 31.12.2009.

Cash funds increased by 14% or 575 million KM, as result of the credit portfolio decrease, amounting to 4,8 billion KM, representing participation of 31,4% in the assets.

Deposits, with participation of 72,5%, amounting to 11 billion KM, still represent the most significant source of funding for banks in the FBiH.

Total capital of banks amounted to 1,7 billion KM (shareholders' was 1,17 billion KM), representing an increase of 2%. The mentioned capital increase was primarily caused by the inflow of new, green capital – additional capitalization in six banks of KM 43,5 million, which is 20% increase, if compared to 2008.



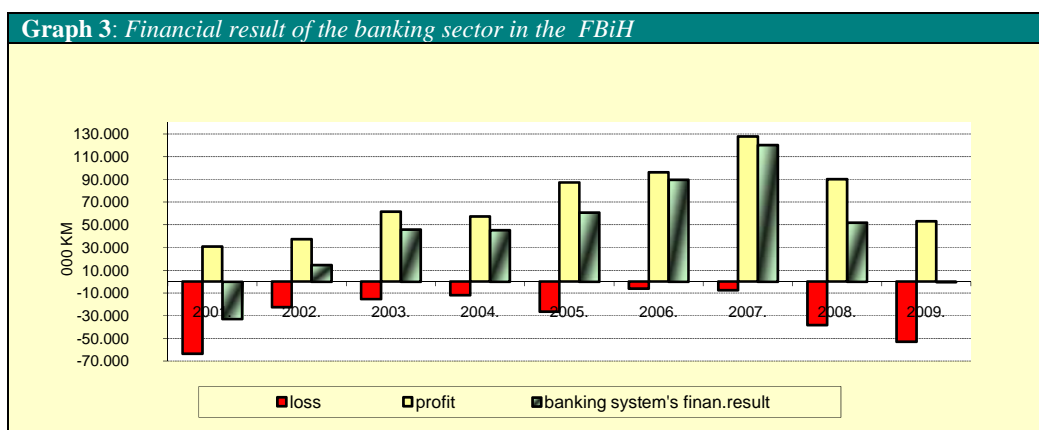
Income statement

Since 2001, when the banking system reported loss of KM 33 million, a positive trend of the successful performance had begun that due to the global economic and financial crisis spreading was stopped in 2008, so there was the significant deterioration of profitability recorded in the entire banking system of the Federation of BiH. In 2009, as affected by an adverse influence of the crisis, profitability decline was even more present.

According to the final non-audited data for 2009, the banks in the Federation of BiH reported positive financial result-profit in the amount of only nine thousand KM, while the profit reported in 2008 was 50 million KM.

Positive financial result was reported by 13 banks in total amount of 52.975 thousand KM, representing a decline of 41% or 36 million KM in comparison to 2008 (15 banks), while seven banks reported loss in the amount of 52.966 thousand KM, representing an increase of 36% or 14 million KM in comparison to prior years.

Reason to deterioration of the entire sector's success in 2009 is that generally in the system, and especially with large banks that carry the profitability, the reported profit significantly declined as result of the total income decrease and significant loan loss provisioning increase due to the asset quality deterioration.



Total income in 2009 amounted to 815 million KM, which was lower by 3% in comparison to 2008, while loan loss provisioning increased by 43% or 68 million KM, amounting to high 226 million KM.

Net interest income increased by only 1% or 3,1 million KM, as result of higher decline in interest expenses than in interest income, so there was slight increase of net interest income in the structure of total income from 62,0% to 64,1%, while participation of operating income decreased from 38% to 36%.

• **Ownership structure:** At the end of 2009, ownership structure of banks in the Federation of BiH was the following: two banks with majority state ownership, and of 18 banks with majority private ownership, six banks were majority owned by domestic legal entities and individuals (residents), and 12 banks were majority foreign owned.

Based on the criteria of the owner-shareholder's home country, that is the criteria of direct or indirect majority ownership through the group members, at the end of 2009, the largest

participation was recorded of banking groups and banks from Austria (56,7%), followed by Italian banks (16,6%), while other countries participated below 6,4%.

In 2009, participation of state, foreign and private domestic (resident) capital in total share capital changed. Participation of state capital decreased from 4,1% to 3,6%. Foreign capital nominally increased by 46,5 million KM, primarily based on additional capitalization (43,5 million KM), while the participation was increased from 83,1% to 83,3%. Private capital (residents) increased by 10,9 million KM, and relative participation in total share capital increased from 12,8% to 13,1%.

• **Concentration and competition:** As for opportunities in the banking market of the Federation of BiH, where in order to compete for customers and greater market share banks enter into acquisitions and integration processes through mergers, upon finalization of such processes in the system, as estimated by some financial experts, will remain 15 to 20 strong banks. However, five to six large foreign owned banks will control 90% of the market, in which they already sovereignty rule, while smaller banks will profile as local character banks.

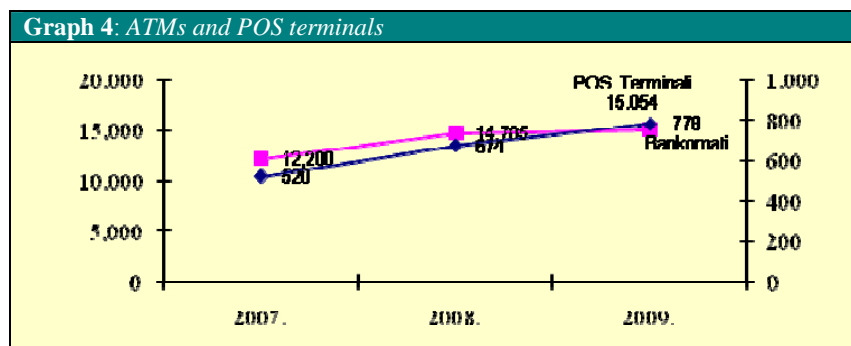
Three banks that still have dominant participation of 65,1% hold the assets that exceed two billion KM. Majority of banks (13) hold the assets bellow 500 million KM, of which four banks have the assets bellow 100 million KM. Three banks hold the assets between 500 million KM and one billion KM, while the assets of one bank were slightly higher than one billion KM.

One of the indicators of concentration in banking system is the ratio of market concentration, that is, the concentration rate² (hereinafter: CR), which indicates total market participation of the largest institutions in the system. The CR5 is an indicator of assets participation of the five largest banks, which at the end of 2009 in the banking system of the Federation of BiH amounted to 78,2% (79% as of 31.12.2008.), but there is still dominant participation of the three largest banks in the system that „hold“ 65,1% of the market.

In the market „game“, banks use various instruments, from interest rate policy, organization improvement, personnel strengthening, to strong marketing approach and business network expansion, financial support by "parent" bank or group member banks.

Card-based operations of majority of banks in the Federation of BiH represent a significant business activity, primarily of credit character, which is reflected through more massive use of credit and debit cards and increased volume of non-cash payments.

During 2009, 104 new ATMs were installed, and, at the end of the same year, their number was 778. Number of POS terminals has also increased by 349, so there was total of 15.054 POS terminals at the end of 2009 with possibility to pay commodities by cards.



² Engl.: Concentration Ratio (CR), assigned according to the number of institutions included in the calculation.

II. SUPERVISION OF BANKING SYSTEM

1. BANKING AGENCY

Banking Agency of the FBiH (FBA) has given its full contribution to the banking sector reform, although there have often been lack of understanding for the measures that were taken. As an independent and sovereign authority for bank supervision and licensing, the Agency was established in the second half of 1996 and its work, since the very beginning, has been directed towards a strong and stable banking system, as market-oriented and based on the international standards of performance and supervision of banks.

Law on Banking Agency sets out the main tasks of the Agency, such as issuance of banking license, adoption of regulations, supervision of banks, microcredit organizations and leasing companies and measures to be taken in accordance with the Law, including initiation of provisional administration and liquidation in banks, that is, initiation of bankruptcy procedure over banks.

Based on the assessments conducted by domestic and international officials, the FBA has, over the past 13 years, achieved the high professional level, and its staff has obtained expertise and skills in the area of supervision through various educations in country and overseas.

The FBA has, over the past year, successfully acted towards banks in the Federation of BiH to better manage especially credit risk, and banks have been doing so in compliance with the prescribed minimum prudential criteria, taking into account the interests of all „stakeholders“, including their financial „soundness“.

The FBA, with the main purpose being protection of funds and interests of depositors, has introduced measures in 26 banks (provisional administrations, liquidations or bankruptcies), since its initiation to the end of 2009, while provisional administration in one bank was introduced pursuant to the order of the High Representative of BiH. Provisional administration was introduced in 23 banks.

Of 26 banks in which the measures were taken, the procedure was finalized in 14 banks. As of 31.12.2009., there were 12 banks under the measures.

Of 26 banks with the measures initiated:

- Bankruptcy process at the authorized courts was initiated in seven banks,
- Liquidation process was initiated in ten banks. Liquidation process was finalized in six banks (four banks paid out all liabilities towards their creditors and shareholders, and one bank was sold out),
- Four banks were integrated into other banks,
- Three banks were rehabilitated and continued operating. First banks was additionally capitalized and privatized, second bank one was additionally capitalized, and third bank was resolved, the bank management bodies were elected and the bank continued operating,
- Provisional administration process in two banks is still pending.

2. BANKING SUPERVISION

Starting with the overall need of the macroeconomic and financial stability, in the year 1997, the Basel Committee for Bank Supervision adopted the twenty five core principles to be met in order for any supervisory system in banking to be efficient. The same principles were revised and published in the new form in 2006. By this revision, the Basle Committee has brought the core principles up to date, made them more clear and concise, additionally developed some already existing and added some new ones, and generally made them closer to the new international capital framework for banks – Basel II.

The principles set minimum requirements to be fulfilled and, in many cases, they need to be supplemented by other measures in order to satisfy specific conditions or regulate risks of the financial system of a respective country. The principles refer to the prerequisites for effective bank supervision, issuance of banking licenses, prudential regulations and requirements, on-going bank supervision methods, necessary information, authorizations of supervisors and cross-border banking.

Generally acceptable international principles, standards and practices for banking supervision that are being more broadly and consistently applied by the Agency, alongside with permanently intensified attention to striking and easily contagious causes of crisis situations, were major concern of the Agency for preparation and initiation of the available defense activities and measures as result of its own experiences, as well as “lessons learned” by many more developed and stronger, especially hit by the crisis, banking systems.

Regulations, their upgrading and extensibility, and operating decisions within the scope of its work, the Agency has been making, following all steps that were prescribed with main purpose that banks to maximum extent enable rule of law in their work, full implementation of the Agency's regulations and of all generally acceptable principles and practices for their prudent and successful work, especially under the circumstances of more present recession. Apart from the mentioned, the main focus of all of the Agency's efforts have been directed towards capital strengthening of banks, improvement of their credit policies and their consistent implementation in practice, raising prudency at maximum possible level in terms of credit risk management that is still very dominant in our environment, as well as liquidity risk, as well as to strengthen capacities for potential crisis management. Along with the mentioned, the Agency has been continuously giving incentives to banks, especially those that are dominant in the system to strengthen their financial potentials and through additional special support by their foreign parent-banks.

Bank supervision - on site and off site bank examinations was conducted upon the plan and program for 2009. Upon preparation of the examination reports, all banks subject to examination received orders to execute and eliminate determined deficiencies. The examinations determined that all banks were regularly and generally meeting the orders in a timely manner. Concrete, competent and professional approach by the supervision in the examination of banks has its purpose to further improve quality of banks performance, their profitability, solvency and safety in the performance, which is the mutual interest.

In 2009, the Agency continued and intensified its work with the International Monetary Fund and the Central Bank of BiH, along with initiation of concrete analytical activities, aimed at developing the skills for collection and analysis of „Financial Soundness Indicators“, as one of preconditions for strengthening and higher effectiveness of supervision over the entire financial, and not just banking sector. This work resulted with the first overall scenarios of real situation and supposed potentially possible crisis situations, or more specifically only crisis stroke of

systemic nature that have for the first time shown boundaries of the problems and stress those banks in the system of the Federation of BiH could be exposed to without any major consequences.

The USAID's Project of technical assistance to the financial sector of Bosnia and Herzegovina was initiated in 2008 under the name „Partnership for Advancing Reforms in Economy – „PARE“. In 2009, according to the Strategy developed by the Agency for introduction of „International Convergence of Capital Measurement and Capital Standards“– Basel II and action plans, the Agency has implemented the activities for the most part of Phase 1. of the mentioned Strategy; certain number of working drafts of the future regulations has been prepared in order to regulate the management of three core banking risks (credit risk, market risk and operating risk), as well as the preliminary steps for preparation of supervisory approach preparation to include wide range of prudential instruments as essential improvements to the successful management of the mentioned risks.

As equal counterpart, the Agency participated in all activities implemented by the Group of Banking Supervisors for Central and Eastern Europe – „BSCEE“ that comprises supervisory institutions from 20 transition countries and Austria that receives special support from the Basel Committee for Banking Supervision.

In compliance with the requirements of Principle 25 from the list of „Core principles for effective bank supervision“ issued by the Basle Committee, the Agency, in 2009, together with the Central Bank of BiH and Banking Agency of RS finalized negotiations regarding signing of two memorandums on mutual cooperation with the Banking Regulation and Supervisory Agency of the Republic of Turkey that was signed in June 2009, and with the Banca d'Italia, whose call for signing a similar document is expected to happen soon.

In 2009, the Agency realized cooperation not only with the regulatory authorities of the countries-signatories of the memorandums of understanding, but with all other supervisory authorities of the countries in the closer and wider region. In addition, special forms of concrete work cooperation were realized through so called „colleges“ and information exchange regarding performance and condition of parent-banks and their „daughters“, that is, subsidiaries.

Based on the decision of the Parliament of the Federation of BiH in 2006, and later on „CARDS Program“ that was prepared by the European Central Bank experts and group of the European central banks, in 2009 the Agency was, in all occasions, supportive of the idea to consolidate banking supervision at state level, since it has recognized, with many pragmatic reasons, such organization of supervision over the main segment of the financial system, on the path to the European Union, would not be viable. The European experts also confirmed that: „banking supervision is actually organized at state level in the European countries under the roof of the central bank or outside of it“and that: „ ... membership to the European Union implies the establishment of a single banking market that leads to a single (consolidated) supervision“.

Growing aggressive globalization and banking industry development, the enhancement and evolution of supervisory principles, rules and standards, as well as more recent painful reflection of the global financial and economic crisis that „taught“ many lessons to everything and everyone it had influenced, has demonstrated that especially banking supervisors have to be constantly updated and should keep developing their knowledge, skills and instruments for more effective action when realizing their mission. For the same reasons, and in order to hire new, especially young people, in 2009 the Agency was taking care of such needs, and on its own and with assistance of many international and highly qualified and specialized institutions, it applied necessary education of its employees, that was conducted in the country and overseas. At the

same time, the Agency offered assistance, through specialized education, to other authorities and institutions in the Federation of BiH.

3. COMBAT AGAINST MONEY LAUNDERING AND TERRORISM FINANCING

The banking system assessment for 2009 was based on the assessment of banks as result of supervisory examinations conducted in terms of banks' compliance to the standards for prevention of money laundering and terrorism financing, follow-up examinations of orders being met, and analysis of banks' reports submitted to the Agency (Form no. 6, Tables A to E).

1. The banks' condition

In full-scope and targeted examinations, and based on the banks' reports submitted to the Agency, it was determined no reasons for supervisory concern in terms of the management of risk from money laundering and terrorism financing. Risk management quality that in banks' performance could arise as result of money laundering and terrorism financing (reputation risk, operating risk, legal risk, assets and deposits concentrations risk), in the banking sector of the Federation of Bosnia and Herzegovina, is satisfactory and it has increasing trend. Risk quantity has maintained within the limits of moderate, and, during the year, it started recording the decreasing trend. Additional reason for such supervisory rating is the rating of compliance of the legislation of Bosnia and Herzegovina to the standards on prevention of money laundering and terrorism financing (40+9 FATF recommendations and the European Parliament and Council Directives) performed by the European Council's MONEYVAL Committee in May-December 2009. Namely, in the Report of this Committee, it was stated that, apart from many incompliance in the financial system of BiH, the banking sector was largely compliant and it could present a good example to other financial institutions to achieve this compliance.

- 1.1 Customer Acceptance Policy:* Banks have established special registries of their customer profiles. Certain issue in regard to functioning of such registries appeared in terms of updating the data of customers that banks classify in different categories. However, it is especially important that banks have established and are applying the approach towards customers that is based on risk analysis that customers have for the bank, that is, that they define what type of customers are acceptable for the bank.
- 1.2 Customer Identification Policy:* Banks have adopted customers' identification as core element of the «know your customer» standard. The customer identification policy is applied by banks when establishing business relationship with customers. However, there is still this problem of records updating that is used to document the establishment of such relationships with already established business relationships.
- 1.3 Account and Transaction Permanent Monitoring Policy:* This policy is applied and there is fewer formal monitoring of the customers' accounts and transactions. In order to achieve the essential monitoring of the customers' accounts and transactions, and based on implementation of the «know your customer» policy, banks have defined the transaction limits per certain types of accounts and transactions; developed information systems to apply limits set in monitoring of accounts and transactions, so in cases of any suspicion raised about money laundering and terrorism financing, the defined limits start to serve in their preventive and not just subsequent monitoring of accounts and transactions.
- 1.4 Money Laundering and Terrorism Financing Risk Management Policy:* The elements of the mentioned policy are defined in the banks' programs. Reporting lines, both external and internal, are also defined.

Reporting: In 2009, banks reported of 303.822 transactions, representing 0,47% of total transactions realized in the banking system of the Federation of Bosnia and Herzegovina (64.729.831 transactions realized, upon the banks' data) with the value of 11.067.457 h/KM, representing 10,60% of total value of the transactions realized in the banking system of the Federation of Bosnia and Herzegovina (104.217.534 h/KM upon the banks' data). Number of reported transactions in 2009 decreased by 0,12%, in comparison to the prior year, while their value increased by 1,65%.

The following table presents the comparative schedule of number and value of reported transactions based on the transfer reporting method (prior to conducting, within deadline prescribed and after deadline prescribed):

Transfer value in 000 KM

Table 2: Comparative schedule of number and values of reported transfers							
Ord. no.	Description (of transfer)	Transfers in 2008		Transfers in 2009		%	
		Number	Value	Number	Value	Number	Value
1	2	3	4	5	6	7 (5/3)	8 (6/4)
1.	Total reported transfers (2+3+4)	304.178	10.886.870	303.822	11.067.457	99,88	101,65
2.	Transfers reported prior to conducting	9	6.150	32	28.646	355,55	465,78
3.	Transfers reported within deadline of 3 days	303.958	10.869.257	303.637	11.030.046	99,89	101,48
4.	Transfers reported following deadline of 3 days	211	11.463	153	8.765	72,51	76,46

In the structure of reported transactions, there is a notable increase of the number (355,55%), in comparison to the prior year, and the value (465,78%) of reported transactions prior to their conducting. This leads to the conclusion that account and transaction monitoring based on the established limits has become the primary factor of banks' conclusions that were made in terms of suspicious or unusual transfers. The number and value of transfers reported within deadline prescribed has the same trend as the number and value of total reported transfers. The number and value of reported transfers following deadline prescribed for reporting supports the conclusion made in the segment: the Account and Transaction Permanent Monitoring Policy that banks applied the „know your customer policy“ in the account and transaction monitoring, so the number and value of transfers reported following deadline prescribed for their reporting has significantly decreased. However, monitoring still serves as corrective (subsequent) action of banks to prevention of money laundering and terrorism financing. This also means the Agency, in 2009, determined in its supervision that number of non-reported transactions has considerably decreased, resulting with quite reduced number of orders issued to subsequently report of such transactions.

Suspicious transactions: In their reports, banks marked 86 transfers as suspicious (85 transfers due to suspicion of money laundering and 1 transfer due to suspicion of terrorism financing), representing 215% in comparison to prior year. The value of those transfers is 36.865 h/KM, representing 150,84% in comparison to prior year.

The following table presents the comparative schedule of the number and value of reported suspicions transactions based on the transfer reporting method (prior to conducting, within deadline prescribed and after deadline prescribed):

Transfer value in 000 KM

Table 3: Comparative schedule of number and value of suspicious transfers reported							
Ord. No.	Suspicious transfers	Transfers in 2008		Transfers in 2009		%	
		Number	Value	Number	Value	Number	Value
1	2	3	4	5	6	7 (5/3)	8(6/4)
1.	Total reported transfers	40	24.439	86	36.895	215,00	150,84
2.	Transfers reported prior to conducting	7	6.108	32	28.646	457,14	469,00
3.	Transfers reported within deadline of 3 days	7	15.653	42	6.287	671,42	40,16
4.	Transfers reported following deadline of 3 days	26	2.678	12	1.960	46,15	73,18

The structure of reported suspicious transfers, as well as the structure of total reported transfers, supports above mentioned conclusions. However, significant increase of the number (457,14%) and value (469%) of suspicious transactions reported prior to conducting was noted. This adds to the meaning of the account and transaction monitoring based on the „know your customer“ principle and defined transaction limits as one of core instruments to identify some transaction being related to money laundering and terrorism financing. Decreased number (46,15%), in comparison to prior year, and value (73,18%) of transfers reported following deadline for reporting indicates that banks have developed adequate policies and procedures for monitoring so there is less transactions that banks themselves or upon the Agency's order, report after deadlines defined for reporting.

III BUSINESS PERFORMANCE OF BANKS IN THE FEDERATION OF BIH

1. STRUCTURE OF THE BANKING SECTOR

1.1. Status, number and business network

As of 31.12.2009., there were 20 banks with the banking license issued in the Federation of BiH. Number of banks remained the same as of 31.12.2008. 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 31.12.2009., there were two banks under provisional administration (UNA bank d.d. Bihac and Hercegovacka banka d.d. Mostar).

In 2009, the banks continued expanding the network of their organizational units, but at a significantly lower level. At the same time, some banks had to close their organizational units, that is, they reorganized and merged their organizational units for purpose of cost cutting. Consequently, as of 31.12.2009., the banks from the Federation of BiH had a total of 635 organizational units. This represents a downfall of 2,3% when compared to 31.12.2008., as of which date the banks had 650 organizational units.

As of 31.12.2009., seven banks from the Federation of BiH had 53 organizational units in the Republic Srpska and nine banks had 14 organizational units in District Brcko. Five banks from the Republic Srpska had 13 organizational units in the Federation of BiH (three organizational unit were opened, and nine were closed).

As of 31.12.2009., all the banks had the license for inter-bank transactions in the internal payment system and 14 banks were under the deposit insurance program.

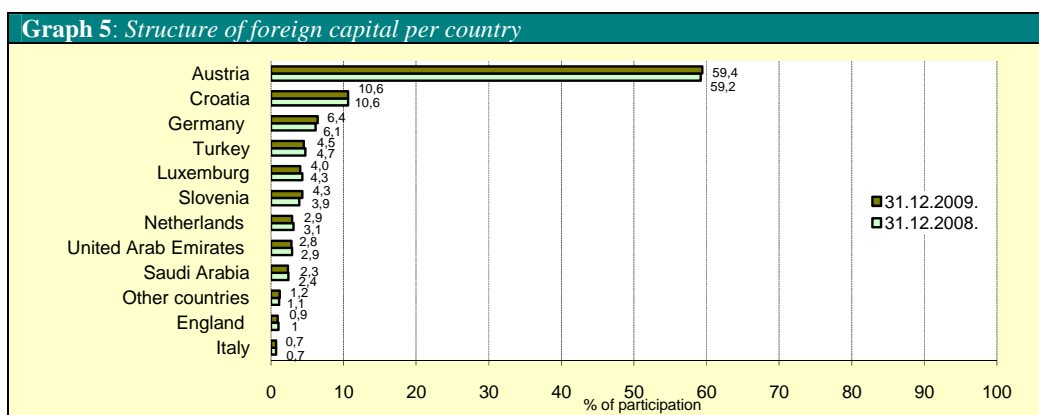
1.2. Ownership structure

As of 31.12.2009., ownership structure in banks³ based on the available information and on-site visits to banks⁴ is the following:

- Private and majority private ownership 18 banks (90%)
- State and majority state ownership⁵ 2 banks (10%)

Six banks, of 18 banks with majority private ownership, are majority owned by domestic legal entities and individuals (residents), while 12 banks have majority foreign ownership.

If only foreign capital is analyzed to the criteria of the shareholders' home country, as of 31.12.2009., the shareholders from Austria owned 59,4% of foreign capital, which is higher by 0,2 per cent than at the end of 2008. The shareholders from Croatia owned 10,6% of foreign capital, while other countries participated less than 7%.

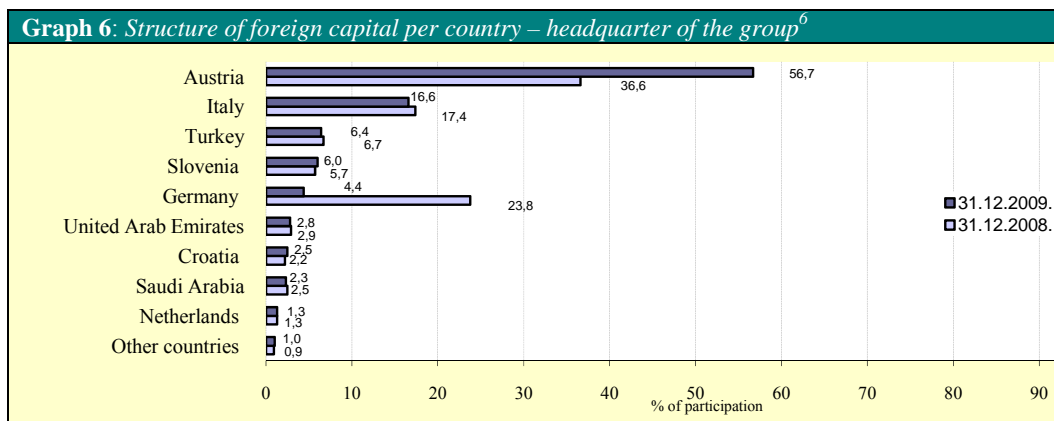


However, if capital correlations are taken into account the structure for foreign capital could be viewed according to the criteria of the parent-bank or the group's headquarter that has majority ownership (directly or indirectly over the group members) of the bank in the Federation of BiH. According to these criteria, situation as of 31.12.2009. has significantly changed in relation to the end of 2008, through the increase of participation of banking groups and banks from Austria from 36,6% to 56,7%, and reason to this were changes in the ownership structure of Hypo Alpe Adria Group, that is, Austria has taken over this banking group, followed by the Italian banks with participation of 16,6%. Other countries participate below 6,4%.

³ Bank classification criteria is ownership over banks' share capital.

⁴ The ownership structure of banks in the FBiH as of 31.12.2009., resulted from received documentation and registrations at authorized courts (changes in capital and shareholders structure).

⁵ State ownership refers to domestic state capital of BiH.

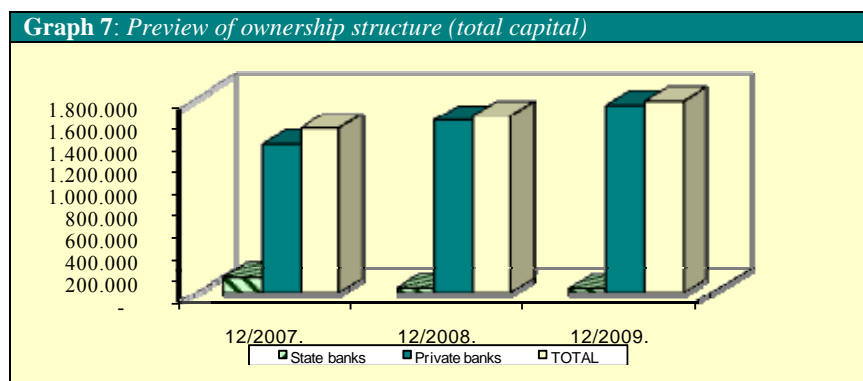


The ownership structure could be viewed from the aspect of financial indicators, which is based on the value of total capital⁷.

-in 000 KM-

Table 4: Ownership structure by total capital

BANKS	31.12.2007.		31.12.2008.		31.12.2009.		RATIO	
	1	2	3	4	5	6	3/2	4/3
State banks	147.022	10%	42.593	3%	41.736	3%	29	100
Private banks	1.363.020	90%	1.594.261	97%	1.632.391	97%	117	102
TOTAL	1.510.042	100%	1.636.854	100%	1.674.127	100%	108	102



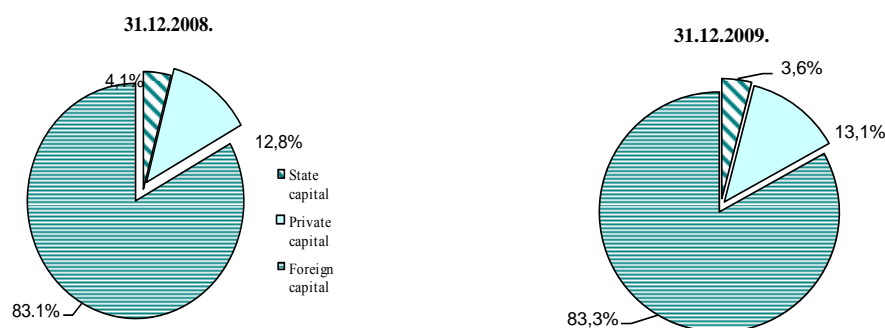
Analysis of participation by state, private and foreign capital in the share capital of banks shows more precise picture of the capital ownership structure in banks of the Federation of BiH.

⁶ Apart from the country of the headquarter 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.

⁷ Information from balance sheet – FBA schedule: shareholder's capital, premium issue, undistributed profit and reserves, and other capital (financial results of current period).

- in 000 KM-

Table 5: Ownership structure by participation of state private and foreign capital								
SHARE CAPITAL	31.12.2007.		31.12.2008.		31.12.2009.		RATIO	
	Amount	Participation %	Amount	Participation %	Amount	Participation %	5/3	7/5
1	2	3	4	5	6	7	8	9
State capital	133.582	12,8	46.100	4,1	41.860	3,6	35	91
Private capital (residents)	135.728	13,0	142.469	12,8	153.365	13,1	105	108
Foreign capital (nonresident)	775.912	74,2	929.447	83,1	975.943	83,3	120	105
TOTAL	1.045.222	100,0	1.118.016	100,0	1.171.168	100,0	107	105

Graph 8: Ownership structure (share capital)

The share capital of banks in the Federation of, in 2009, increased by 4,7% or 53,2 million KM, of which 46,5 million KM relates to nonresidents, and 10,9 million KM to residents, while state capital decreased by 4,2 million KM.

Analysis of the banks' ownership structure shows in the most explicit way, 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 31.12.2009., was 3,6%, lower by 0,5 per cent in comparison to 31. 12. 2008. Nominal decrease was 4,2 million KM based on the share trading with residents.

Participation of private capital (residents) in total share capital of 13,1% is representing a 0,3 per cent increase in comparison to 31.12.2008. Nominal increase of 10,9 million KM was based on the share trading among residents, nonresidents and state capital in the amount of 1,7 million KM net value, purchase of shares from additional capitalization of 3,2 million KM, and increase from the own funds of 6,0 million KM.

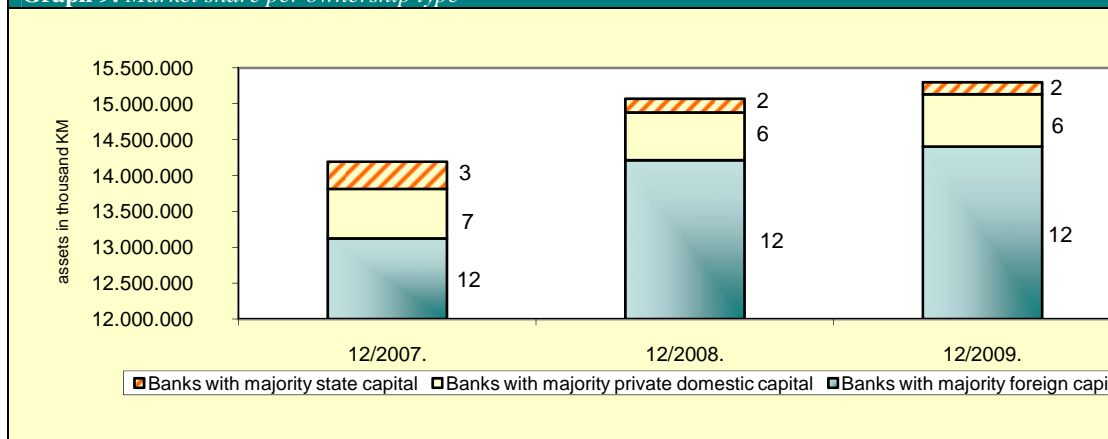
Participation of foreign capital (nonresidents) in total share capital has increased by 0,2 per cent in comparison to 31.12.2008. In absolute amount, the increase was 46,5 million KM based on additional capitalization of 40,2 million KM, based on increase of the own funds of 3,7 million KM, and mentioned share trading between residents and nonresidents of 2,6 million KM.

As of 31.12.2009., the market share of banks with majority foreign ownership was a high 93,9%, of banks with majority domestic private capital was 5,0%, and the share of banks with majority state capital was 1,1%.

- in %-
14

Table 6: Market share of banks per ownership type (majority owned capital)

BANKS	31.12.2007.			31.12.2008.			31.12.2009.		
	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	3	9,7	2,7	2	2,6	1,3	2	2,5	1,1
Banks with majority private domestic capital	7	10,9	4,9	6	10,5	4,4	6	10,5	5,0
Banks with majority foreign capital	12	79,4	92,4	12	86,9	94,3	12	87,0	93,9
TOTAL	22	100,0	100,0	20	100,0	100,0	20	100,0	100,0

Graph 9: Market share per ownership type

1.3. Employees

As of 31.12.2009., there was a total of 7.656 employees in the banks of the Federation of BiH, of that number 3% is in the banks with a majority state capital and 97% in private banks.

Table 7: Bank employees in the FBiH

BANKS	NUMBER OF EMPLOYEES						RATIO	
	31.12.2007.		31.12.2008.		31.12.2009.		3:2	4:3
1	2	3	4	5	6	7	8	
State banks	342	5%	234	3%	231	3%	68	99
Private banks	7.019	95%	7.763	97%	7.425	97%	111	96
TOTAL	7.361	100%	7.997	100%	7.656	100%	109	96
Number of banks	22		20		20		91	100

One of the consequences of the adverse effects of the economic crisis on the banking sector of the Federation of BiH is the decrease in the number of employees in 2009 by 4% or 341 employees. While in the first six months of 2009 the decrease represented only 1% or 108 employees, in the second six months, under stronger influence of the crisis and its adverse effects, the decreasing rate increased to 3% or 233 employees. It should be emphasized this number was not equally present in banks, but it primarily referred to one bank where the number of employees in 2009 decreased by 226 or 25%.

Table 8: Qualification structure of employees								
EDUCATION	NUMBER OF EMPLOYEES						RATIO	
	31.12.2007.		31.12.2008.		31.12.2009.		4:2	6:4
	1	2	3	4	5	6	7	8
University qualifications	2.725	37,0%	3.007	37,6%	3.104	40,5%	110	103
Two-year post secondary school qualifications	799	10,8%	861	10,8%	774	10,1%	108	90
Secondary school qualifications	3.759	51,1%	4.054	50,7%	3.719	48,6%	108	92
Other	78	1,1%	75	0,9%	59	0,8%	96	79
TOTAL	7.361	100,0%	7.997	100,0%	7.656	100,0%	109	96

Although, over a longer period of time the employees' qualification structure has recorded a slight trend of improvement through an increase of the number of employees with university qualifications, the negative trends of decrease of employees in 2009, mostly of those with secondary school qualifications, have also had a positive effect on the qualification structure.

One of the indicators influencing an evaluation of performance of a respective bank, 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 9: Assets per employee									
BANKS	31.12.2007.			31.12.2008.			31.12.2009.		
	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	342	381.036	1.114	234	187.157	800	231	161.619	700
Private	7.019	13.814.886	1.968	7.763	14.882.747	1.917	7.425	15.071.121	2.030
TOTAL	7.361	14.195.922	1.929	7.997	15.069.904	1.884	7.656	15.232.740	1.990

At the end of 2009, there was a 1,99 million KM assets per employee on the level of the banking system. This indicator is significantly better with the private bank sector, as expected taken the stagnation or the decreased volume of activities of state banks and their consequent excessive number of employees.

Table 10: Assets per employee by groups						
Assets (000 KM)	31.12.2007.		31.12.2008.		31.12.2009.	
	Number of banks		Number of banks		Number of banks	
Up to 500	2		2		1	
500 to 1.000	7		9		8	
1.000 to 2.000	7		3		5	
2.000 to 3.000	4		5		5	
Over 3.000	2		1		1	
TOTAL	22		20		20	

Analytical indicators of respective banks range from 253 thousand KM to 3,7 million KM of assets per an employee. Six banks have a better indicator than the one for the whole banking sector, and three banks in the system have one that exceeds 2,4 million KM.

Finally, we can say that the banks have made a significant progress in improving the quality and conditions in which they offer their services to clients, legal entities and individuals, as well as the conditions under which they offer services and finance clients.

2. FINANCIAL INDICATORS OF BANKS' PERFORMANCE

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 of 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 (quarterly),
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 capital⁸.

2.1. Balance sheet

The impact of the global economic crisis and its negative effects on the overall economy of BiH from the last quarter of 2008 continued in 2009, especially over the second six months, resulting by further deterioration of the condition of the real sector. All of this has also adversely affected the banking sector and the key performance indicators. General characteristic of the banking sector's performance under strong effect of the crisis is growth stagnation as the result of the restricted access to funding sources, both deposit and credit, while structural changes in the assets are only due to banks' new business strategies that are adopted for more difficult performance conditions and the state of the environment characterized by restricted or minimum growth, strengthened focus on liquidity and credit risk, implementation of restrictive credit policies resulting in decrease of credit portfolio and has as an aim decrease of risk assets and maintenance of adequate levels of capital. On the other hand, the result is an increase in liquid funds and good liquidity of the banking sector.

Aggregate balance sheet of the banking sector, as of 31.12.2009., amounted to 15,2 billion KM, 1% or 163 million KM higher than at the end of 2008. After slight quarterly oscillations in the 2009, and with assets that the end of the first six months of 2009 was close to the level of 2008, the third quarter the condition displayed a positive change due to the funds received from the first payment of proceeds from the agreement IMF approved for BiH in July of 2009. An amount of about 270 million KM was allocated to the Federation of BiH from the total amount of the

⁸ 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 31.12.2009., these items amounted to KM 618 million.

first proceeds. In the last quarter, negative rate was recorded of 0,4% or 65 million KM, so on the annual, minimum of 1% was recorded. Taken the crisis impact and condition of the real sector, as well as situation and state in the economy and financial sector of the owners' home countries of the banks in the FBiH, such movements and trends in the banking sector have been expected.

Table 11: Balance sheet								
DESCRIPTION	AMOUNT (in 000 KM)							
	31.12.2007.		31.12.2008.		31.12.2009.		RATIO	
	AMOUNT	Partic. %	AMOUNT	Partic. %	AMOUNT	Partic. %	3/2	4/3
1	2	3	4	5	6	7	8	9
ASSETS:								
Cash funds	4.894.973	34,5	4.207.559	27,9	4.782.301	31,4	86	114
Securities ⁹	48.565	0,3	18.814	0,1	119.157	0,8	39	633
Placements to other banks	69.314	0,5	90.415	0,6	111.019	0,7	130	123
Loans	8.874.984	62,5	10.434.377	69,2	9.796.800	64,3	118	94
Loan loss provisions (LLP)	334.139	2,4	381.215	2,5	458.803	3,0	114	120
Loans – net value (loans minus LLP)	8.540.845	60,1	10.053.162	66,7	9.337.997	61,3	118	93
Business premises and other fixed assets	405.116	2,9	467.507	3,1	525.220	3,4	115	112
Other assets	237.109	1,7	232.447	1,6	357.046	2,4	98	154
TOTAL ASSETS	14.195.922	100,00	15.069.904	100,00	15.232.740	100,00	106	101
LIABILITIES:								
LIABILITIES								
Deposits	10.190.977	71,8	10.461.850	69,4	11.045.868	72,5	103	106
Borrowings from other banks	3.289	0,0	3.089	0,0	3.089	0,0	94	100
Loan Commitments	1.856.471	13,1	2.176.594	14,4	1.771.978	11,6	117	81
Other liabilities	635.143	4,5	791.517	5,3	737.678	4,9	125	93
CAPITAL								
Capital	1.510.042	10,6	1.636.854	10,9	1.674.127	11,0	108	102
TOTAL LIABILITIES (LIABILITIES AND CAPITAL)	14.195.922	100,00	15.069.904	100,0	15.232.740	100,00	106	101

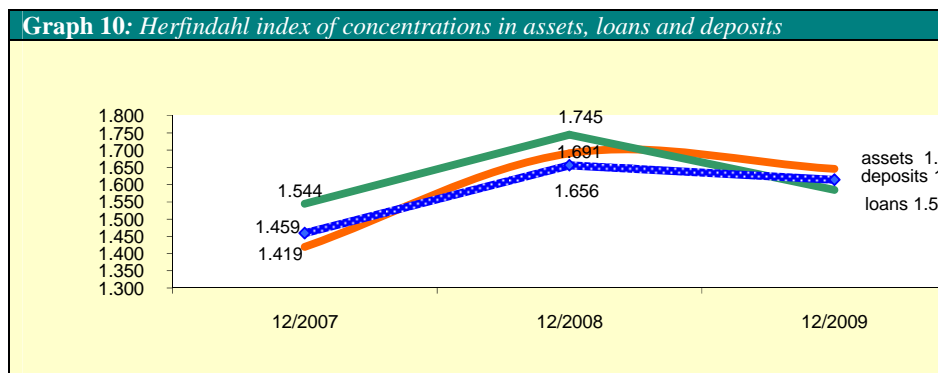
Table 12: Assets of banks based on the ownership structure											
BANKS	31.12.2007.			31.12.2008.			31.12.2009.			RATIO	
	No. banks	Assets (000 KM)		No. banks	Assets (000 KM)		No. banks	Assets (000 KM)		5/3	7/5
	1	2	3	4	5	6	7	8	9		
State	3	381.036	3%	2	187.157	1%	2	161.619	1%	49	86
Private	19	13.814.886	97%	18	14.882.747	99%	18	15.071.121	99%	108	101
TOTAL	22	14.195.922	100%	20	15.069.904	100%	20	15.232.740	100%	106	101

The assets of majority of banks (14) were higher than at the end of 2008, ranging from 1% to 51,2%. The remaining six banks recorded the aggregate balance sheet decline from 2% to 27,7%. Three largest banks in the system recorded minimum assets changes, that is, the largest bank and the third bank per the level of assets recorded the decline of 2% and 7,8%, while the second listed bank recorded growth of 4,5%.

Indicator of concentrations in the three most significant segments of banking performance, in assets, loans and deposits is the value of the Herfffindahl index¹⁰.

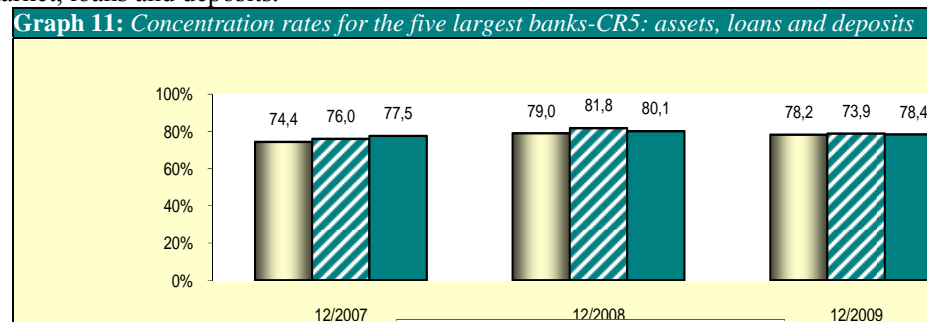
⁹ Trading securities and securities held to maturity.

¹⁰ It is also called the Hirschmann-Herfindahl index or HHI as calculated in the formula $HI = \sum_{j=1}^n (S_j)^2$,



In 2009, the Herfindahl index in all three relevant categories (loans, deposits and assets) recorded a slight downfall, of which the highest downfall was in loans of 160 units, in assets of 45, and deposits of 42 units. Their value, as of 31.12.2009., was 1.646 for assets, 1.585 for loans and 1.614 units for deposits, indicating a moderate concentration¹¹.

Another indicator of concentration in the banking system is the ratio of market concentration, that is the concentration rate¹² (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 for market participation, loans and deposits of the five largest banks in the system, at the end of 2009, was 78,2%, 78,9% and 78,4% respectively which is slightly lower in comparison to the end of 2008. The situation has almost not changed over the past several years, and dominant is the position of five largest banks in the system that 'hold' approximately 80% of the market, loans and deposits.



The banking sector could be analyzed from the aspect of several groups established according to the asset size¹³. The minor changes in relation to the end of 2008 refer to the participation of certain groups which is a result of changes of assets of the larger number of banks.

Three largest banks (Group I) still maintain the highest participation of 65,1%, that has been decreased by 1,5 per cent in comparison to the end of 2008. One bank (Group II) increased its participation from 6,7% to 7,6%, while the participation of 15,1 % of three banks in Group III

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.

¹¹ 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.

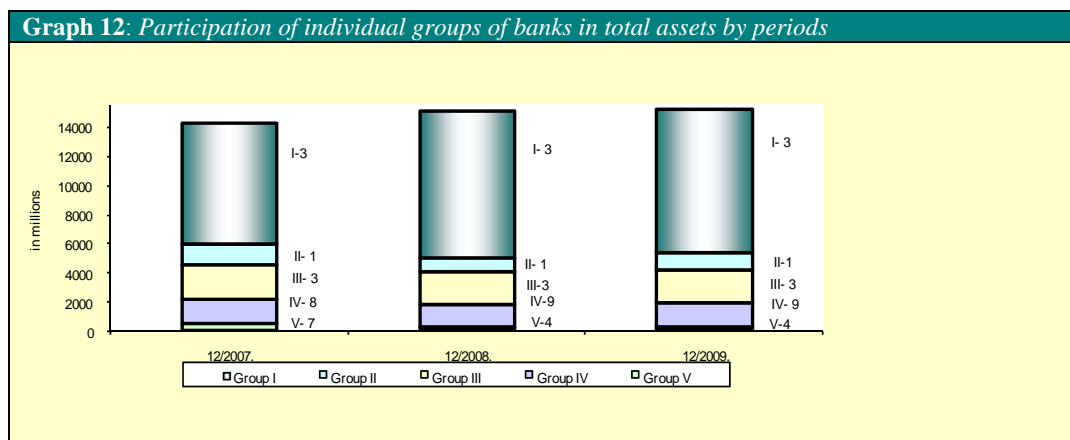
¹² Engl.: concentration ratio (CR), assigned to the number of institutions included in the calculation.

¹³ Banks are divided into five groups depending on the assets size.

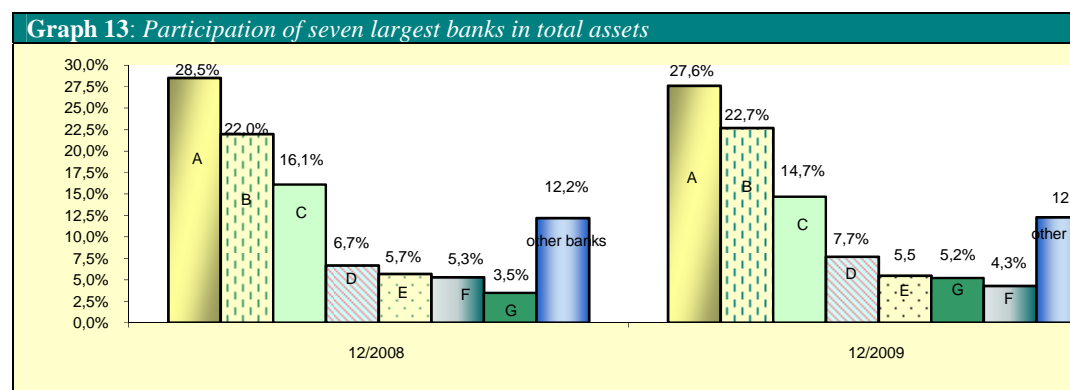
(assets between 500 million KM and one billion KM) increased by 0,6 per cent. The largest group IV consisting of nine banks with assets between 100 and 500 million KM, had unchanged participation of 10,8%, and the last Group V (four banks) still has the lowest participation of 1,4%.

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).

ASSETS	31.12.2007.			31.12.2008.			31.12.2009.		
	Amount	Partic. %	No. of banks	Amount	Partic. %	No. of banks	Amount	Partic. %	No. of banks
I- Over 2.000	8.203	57,8	3	10.036	66,6	3	9.912	65,1	3
II- 1000 to 2000	1.409	9,9	1	1.017	6,7	1	1.165	7,6	1
III- 500 to 1000	2.392	16,8	3	2.180	14,5	3	2.293	15,1	3
IV- 100 to 500	1.741	12,3	8	1.627	10,8	9	1.645	10,8	9
V- Bellow 100	451	3,2	7	210	1,4	4	218	1,4	4
TOTAL	14.196	100,0	22	15.070	100,0	20	15.233	100,0	20



The following graph presents the structure and participation trend of the seven largest banks¹⁴ in the banking system of the Federation of BiH.

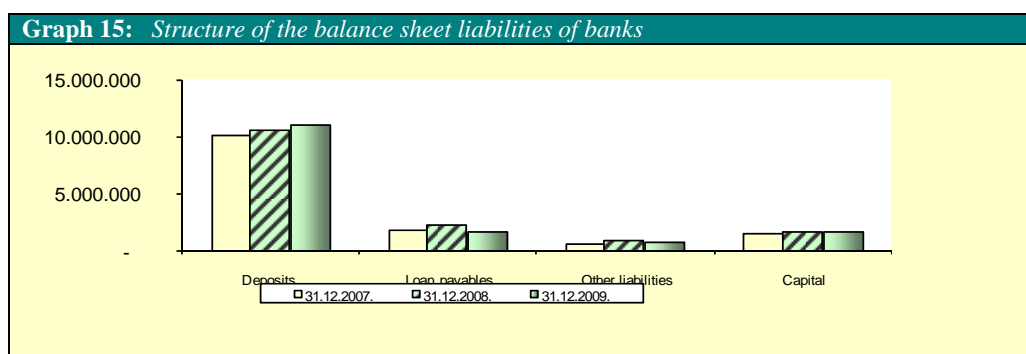
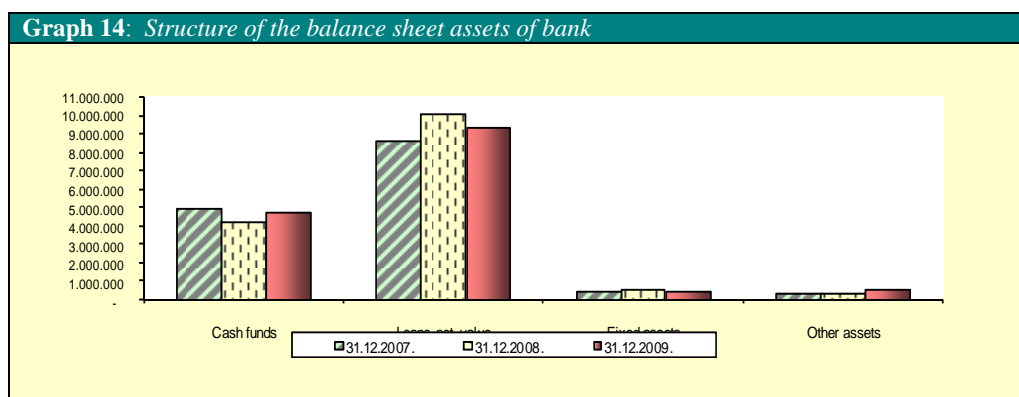


¹⁴ Banks are marked with letters from A to I.

The slight increase of the aggregate balance sheet amount in 2009 of 1% or 163 million has been financed from the increase of deposits of 6% or 584 million KM. However, it has to be emphasized that of that amount around 270 million KM refers to funds received through the first payment of proceeds from IMF, 200 million is the result of replacement of loan liabilities with deposits at one of the banks, while the remaining amount is the realistic increase of deposits for only 114 million KM or 1%. Loan liabilities decreased by 19% or 405 million, of that 200 million were transferred to deposits, and the remaining amount of 205 million KM presents the realistic decrease of 9%. As of 31.12.2009., deposits were 11 billion KM, and loan liabilities 1,8 billion KM. In the observed period, the capital of banks increased by 2% or 37 million KM and it was 1,7 billion KM.

The most significant change in the assets of banks is the increase of cash funds by 14% or 575 million KM (from 4,2 billion KM to 4,8 billion KM). Such movements are mostly the consequence and the result of the banks' restrictive loan policies and the decrease of loan activities in 2009, as well as due to the inflow of the cash funds from the first payment of proceeds from the agreement with IMF. In 2009, loans decreased by 6% or 638 million KM amounting to 9,8 billion KM as of 31.12.2009.

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



In the structure of banks' balance sheet liabilities from the aspect of the most significant balance sheet categories, deposits in the amount of 11 billion KM and participation of 72,5% are still the dominant source of financing for banks in the Federation of BiH. Participation of credit liabilities has decreased from 14,4% to 11,6%, and participation of capital increased from 10,9% to 11,0%.

The structure of assets, as well as the structure of sources, had relatively significant changes related to two key assets items: further decreased participation of loans from 69,2% to 64,3% and an increase of cash funds from 27,9% to 31,4%.

CASH FUNDS	31.12.2007.		31.12.2008.		31.12.2009.		RATIO	
	Amount	Partic. %	Amount	Partic. %	Amount	Partic. %	4/2	6/4
1	2	3	4	5	6	7	8	9
Cash	311.436	6,4	344.618	8,2	355.419	7,4	111	103
Reserve accounts with CBBiH	2.805.568	57,3	2.228.687	53,0	2.455.505	51,4	79	110
Accounts with deposit institutions in BiH	12.304	0,3	12.341	0,3	441	0,0	100	4
Accounts with deposit institutions abroad	1.764.757	36,0	1.621.449	38,5	1.970.473	41,2	92	122
Cash funds in collection process	908	0,0	464	0,0	463	0,0	51	100
TOTAL	4.894.973	100,0	4.207.559	100,0	4.782.301	100,0	86	114

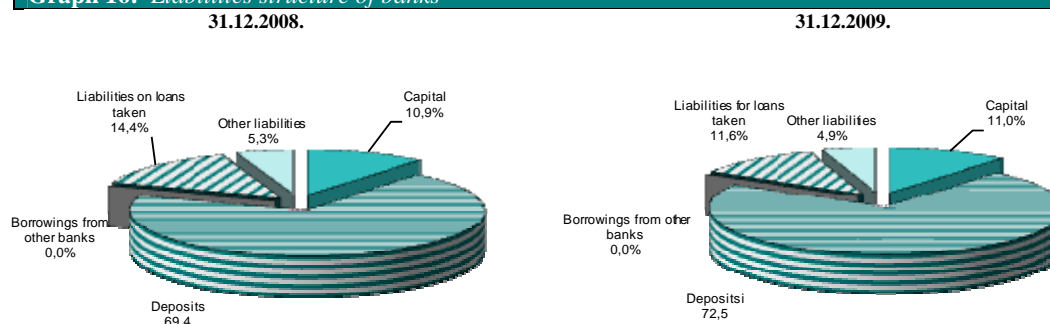
Cash funds of the banks on the reserve accounts of CBBiH, over the observing period of 2009, increased by 10% or 227 million KM, amounting to 2,46 billion KM or 51,4% of total cash funds as of 31.12.2009., representing the participation decrease of 1,6 per cent in relation to the end of 2008. Banks' funds on the accounts with the depository institutions abroad have also increased by 22% or 349 million KM, amounting to 1,97 billion KM or 41,2% of total cash funds as of 31.12.2009., (38,5% at the end of 2008). The banks have increased their cash on hand and in vaults by 3% or 11 million KM. At the end of the observing period, those funds amounted to 355 million KM, representing 7,4% of total cash funds (8,2 at the end of 2008.).

The participation of domestic currency in the currency structure of cash funds, over the observing period, has decreased from 57,9% to 55,8%, 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 31.12.2009. is presented in the following graphs:

Graph 16: Liabilities structure of banks



In 2009, participation of the two most significant funding sources of banks (deposits and credit liabilities), has changed primarily due to the business transaction of replacing credit sources with the deposit in one bank (these are the funds of parent bank granted as financial support to its subsidiary in the FBiH), then also due to the growth of deposits with the payment of the proceeds from the agreement with IMF, as well as due to the decrease of credit liabilities through

collection of past due loans. Deposit participation increased from 69,4% to 72,5%, and the credit liabilities have decreased from 14,4% to 11,6%.

Deposits participating with 72,5% or 11 billion KM still represent the most significant funding source of banks in the Federation of BiH. In comparison to 31.12.2008, these items increased by 6% or 584 million KM. Second source, per its size are credit funds obtained by banks through the debt with foreign financial institutions. In 2009, credit funds have decreased by 19% or 405 million KM, of which 200 million KM had been withdrawn and replaced by deposit, and the remaining amount refers to payment of past due liabilities. If subordinate debts of 184 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 12,8% (15,8% at the end of 2008.).

Capital, in 2009, has increased by 2% or 37 million KM, of which the amount of 43,5 million KM refers to the inflow of new capital from additional capitalization of six banks.

As of 31.12.2009., the highest bank commitments were towards the following creditors (eight of total 47), representing 73% of total credit commitments: Raiffeisen Zentralbank Osterreich A.G. (RZB), European Investment Bank (EIB), Central Eastern European Finance Agency (CEEFA), ComercBank AG Frankfurt, European fund for Southeast Europe (EFSE), Steirmarkische Sparkasse, EBRD and Council of Europe Development Bank.

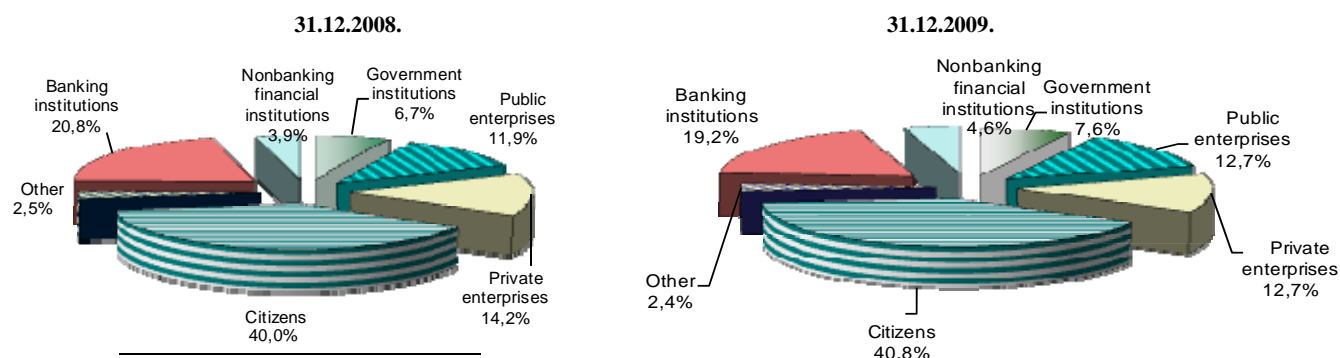
According to the data submitted by banks, out of total deposits as of 31.12.2009., only 5,7% were deposits collected by organizational units of banks from the Federation of BiH operating in Republic Srpska and Brcko District.

- in 000 KM-

Table 15: Deposit structure by sectors¹⁵

SECTORS	31.12.2007.		31.12.2008.		31.12.2009.		RATIO	
	Amount	Partic. %	Amount	Partic. %	Amount	Partic. %	4/2	6/4
1	2	3	4	5	6	7	8	9
Governmental institutions	1.171.095	11,5	701.520	6,7	839.926	7,6	60	120
Public enterprises	1.126.838	11,1	1.245.793	11,9	1.400.839	12,7	111	112
Private enterprises and assoc.	1.554.693	15,3	1.490.139	14,2	1.403.465	12,7	96	94
Non-profit. organizations	1.548.619	15,2	2.172.860	20,8	2.120.143	19,2	140	98
Banking institutions	334.575	3,3	403.295	3,9	509.769	4,6	121	126
Citizens	4.202.161	41,2	4.181.882	40,0	4.506.881	40,8	100	108
Other	252.996	2,4	266.361	2,5	264.845	2,4	105	99
TOTAL	10.190.977	100,0	10.461.850	100,0	11.045.868	100,0	103	106

Graph 17: Deposit structure by sectors



¹⁵ Information from the attached form BS-D, each quarter submitted by banks with balance sheet - FBA format.

The positive movements in the segment of deposit sources are visible in the majority of sectors, and it is especially significant for citizen deposits which in 2009, increased by 8% or 325 million KM. At the end of 2009, citizen deposits, with the amount of 4,51 billion KM and participation of 40,8% in total deposits, still represent the largest funding source of banks in the Federation of Bosnia and Herzegovina.

Deposits of banking institutions are the second largest of the sector sources in deposit potential of banks. During 2009, there were oscillations of such deposits, and in the first six months of the year, they recorded an increase of 6% or 120 million KM, while in the second six months of the year, they had decreasing trend, so total decrease in 2009 was 53 million KM or 2%. At the end of 2009, they amounted to 2,12 billion KM, representing 19,2% of total deposits. Deposits of banking institutions, as of 31.12.2009., were higher by 348 million KM than credit liabilities, representing, after deposits, the second most significant funding source of banks in the FBiH.

It should be emphasized that 97% or 2,06 billion KM of banking institutions' deposits refers to deposits of banks-members of groups (primarily shareholders). Financial support of the groups (banking and nonbanking financial institutions) through deposits in the amount of 2,10 billion KM is present in nine banks in the Federation of BiH, with a concentration on four large banks (86%), with one bank representing 45% 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. On the other hand this is creating higher concentrations in the sources, which is directly correlated with the increase of liquidity risk and reliance on risk management at the level of the bank's group, as well as an impact on the profitability as these are expensive sources. If credit liabilities and subordinate debts (loans and deposits in supplementary capital) are added to these funds, the financial support the banks received from their groups becomes higher, amounting to 3,04 billion KM or 20% of total liabilities of the banking sector as of 31.12.2009. In comparison to the end of 2008, these funds were reduced by 399 million KM or 11,6%, of which loans represented 360 million KM based on servicing matured liabilities per loans in repayment.

As part of the activities taken to mitigate the impact of the global financial crisis, the FBA (in October 2008), in addition to other measures, asked the banks-members of the groups to submit a confirmation from their owners that the existing sources of funds received from their groups (loans and deposits) would not be withdrawn and the financial support would still be provided, as well as an information on planning, measures and activities from their owners related to subsiding the pressure on liquidity and safeguarding their banks liquidity in the Federation of BiH.

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".

Moderate growth was recorded by the government institutions sector of 20% or 138 million KM and public enterprises of 12% or 155 million KM, noting that these two sectors recorded significant downfall of deposits in the last quarter of the prior year. Deposits of government institutions, at the end of 2009, amounted to 840 million KM or 7,6% of total deposits (0,9 per cent higher than at the end of 2008), and deposits of public enterprises were 1,4 billion KM, representing 12,7% of total deposits (increase by 0,8 per cent).

Deposits of nonbanking financial institutions, during 2009, had increasing trend and increase of 26% or 107 million KM. At the end of 2009, they amounted to 510 million KM, but still have low participation in total deposits of only 4,6%.

The biggest impact and adverse consequences of 2009 were present in the real sector, which is the sector of private companies. One of the negative effects of the economic crisis in the segment of deposits in the first half of the year was the decrease of 6% or 94 million KM, while minimum increase of seven million KM was realized in the second half of the year, so the overall decrease in 2009 was 6% or 87 million KM. The nominal deposits of this sector amounted to 1,4 billion KM, while the participation in total deposits was decreased from 14,2% to 12,7%.

Currency structure of deposits, at the end of 2009, was the following: deposits in foreign currencies (with the dominant participation of EURO) in the amount of 6,6 billion KM participated with 59,6% (60% at the end of 2008) and deposits in domestic currency in the amount of 4,4 billion KM participated with 40,4% (40% at the end of 2008).

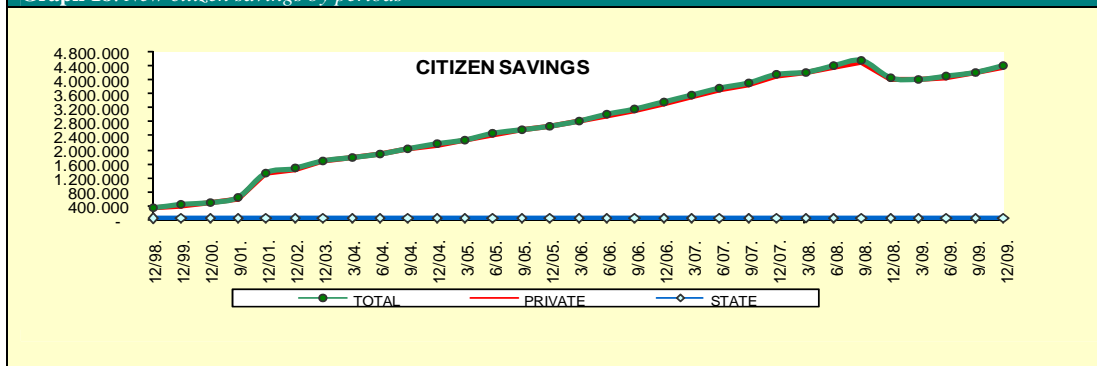
Saving deposits, as the most significant segment of deposits and financial potential of banks, following many years of a stable and continuous growth, with the first signs of the economic and financial crisis in the fourth quarter of 2008, decreased by 11% or 494 million KM. The most critical withdrawal was recorded in October. After this period, the condition stabilized, shaken confidence in banks retrieved, resulting by majority of deposits being placed back on bank accounts in 2009.

Following a slight downfall of savings in the first quarter of 2009, of 0,9% or 38 million KM, the saving deposits recorded an increasing trend in the next three quarters, resulting in an increase of 8 or 326 million KM in 2009. The savings as of 31.12.2009., amounted to 4,36 billion KM, which was almost the same as the level as of 30.06.2008. (savings were higher by only six million KM), and if compared to 30.09.2008. (amount of 4,53 billion KM), it was 96,3% or 3,7% lower that confirms the confidence in the banks and the security and stability of the banking sector have been preserved.

Table 16: New citizen savings by periods

BANKS	AMOUNT (in 000 KM)			RATIO	
	31.12.2007.	31.12.2008.	31.12.2009.	3/2	4/3
1	2	3	4	5	6
State	30.469	32.481	35.275	107	109
Private	4.086.820	4.003.184	4.325.926	98	108
TOTAL	4.117.289	4.035.665	4.361.201	98	108

Graph 18: New citizen savings by periods



The largest three banks hold 72,6% of savings, while participation of eleven banks has an individual participation of less than 1%, representing only 4,8% of total savings in the system.

Savings deposits in local currency represent 29% and in foreign currency 71% of total savings amount.

Table 17: Maturity structure citizen saving deposits by periods

BANKS	AMOUNT (in 000 KM)				RATIO			
	31.12.2007.		31.12.2008.		31.12.2009.			
1	2		3		4	5	6	
Short term saving deposits	2.174.863	52,8%	2.119.669	52,5%	2.054.196	47,1%	97	97
Long term saving deposits	1.942.426	47,2%	1.915.996	47,5%	2.307.005	52,9%	99	120
TOTAL	4.117.289	100,0 %	4.035.665	100,0 %	4.361.201	100,0 %	98	108

The savings maturity structure changed, that is, the trend of the participation increase of long-term savings is continuing. Such changes are a result of the growth of the long-term savings of 20% or 391 million KM, and the decrease of the short-term savings by 3% or 65 million KM. As of 31.12.2009., their participation was 52,9% and 47,1% respectively.

Long term continuous growth and positive trends in the savings segment of banks in the F BiH result, on the one hand, from 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. There is total 14 banks from the Federation of BiH that were accepted to the deposit insurance program, and according to the submitted data, there is total 96,5% of total deposits and 98% of total savings deposited in these banks.

Upon the change of the Law on the deposit insurance in the banks in BiH¹⁶ and elimination of the ownership criteria (participation of private and state capital), of the remaining banks four can not apply to be admitted since they do not qualify with the criteria prescribed by the Deposit Insurance Agency: two banks due to the existing composite rating, two (one private and one state) are under provisional administration, while there are two more banks that can apply for the admission to the insurance program (one was admitted in February 2010). At the same time, there is an initiative made to raise the insured deposit to 50.000 KM, and all the activities undertaken have been directed to reduce an impact of the global economic crisis on the banking and the entire economic system of the FBiH and BiH

2.1.2. Capital – strength and adequacy

Capital¹⁷ of banks in the Federation of BiH, as of 31.12.2009., amounted to 2,06 billion KM.

¹⁶ „Official Gazette of BiH“ No.75/09.

¹⁷ 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).

¹⁶ 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.

-in 000 KM-

Table 18: Regulatory capital						
DESCRIPTION	31.12.2007.	31.12.2008.	31.12.2009.	RATIO		
				3/2	4/3	
1	2	3	4	5	6	
STATE BANKS						
1. Core capital before reduction	145.802	44.852	44.906	31	100	
2. Offsetting items	2.018	2.752	3.796	136	138	
a) Core capital (1-2)	143.784	42.100	41.110	29	98	
b) Supplementary capital	6.017	1.335	1.294	22	97	
c) Capital (a + b)	149.801	43.435	42.404	29	98	
PRIVATE BANKS						
1. Core capital before reduction	1.316.424	1.610.692	1.706.023	122	106	
2. Offsetting items	124.137	170.042	195.208	137	115	
a) Core capital (1-2)	1.192.287	1.440.650	1.510.815	121	105	
b) Supplementary capital	531.057	574.370	506.390	108	88	
c) Capital (a + b)	1.723.344	2.015.020	2.017.205	117	100	
Total						
1. Core capital before reduction	1.462.226	1.655.544	1.750.929	113	106	
2. Offsetting items	126.155	172.794	199.004	137	115	
a) Core capital (1-2)	1.336.071	1.482.750	1.551.925	111	105	
b) Supplementary capital	537.074	575.705	507.684	107	88	
c) Capital (a + b)	1.873.145	2.058.455	2.059.609	110	100	

In 2009, capital¹⁸ remained almost at the same level, that is, it increased by only 1 million KM in comparison to 2008, while the changes in core and supplementary capital reflected on the structure of regulatory capital. The core capital increased by 5% or 69 million KM, and supplementary capital decreased by 12% or 68 million KM.

The core capital growth is primarily based on a distribution of the 2008 profit to the capital. Following the implementation of the legal procedure related to adoption of a decision by the assembly of banks concerning distribution of an audited profit (five banks reported loss of 39 million KM), the profit generated in 2008 in the amount of 89 million KM (15 banks) was distributed 94,3% to the core capital (reserves or retained-undistributed profit of 88,6% and 5,7% to cover losses). Four banks made a decision to pay out dividends in total amount of five million KM, representing approximately 5,7% of the profit generated.

The core capital growth, aside from the mentioned, has been influenced by the new additional capitalization, that is, the inflow of green capital in the amount of 43,5 million KM in six banks.

Offsetting items (that reduce the core capital) have increased by 26 million KM, primarily based on the increase of the current loss (53 million KM), along with a decrease due to partial coverage of the uncovered losses of 30 million KM.

Supplementary capital decreased by 68 million KM, with major changes in the structure: the 2008 profit of 75 million KM moved to the core capital, current audited profit amounted to 49 million KM, general loan loss reserves have decreased by 25 million KM, and subordinate debts by 27 million KM, while the permanent character items increased by 10 million KM.

The mentioned changes influenced the structure of the regulatory capital, so participation of core capital has increased from 72% to 75%, while the supplementary capital has decreased from 28% to 25%.

Net capital has increased by 4,6 million KM amounting to 2,04 billion KM as of 31.12.2009.

Capitalization rate of banks, expressed as a capital to assets ratio, as of 31.12.2009., was 13,1%, representing a decrease of 0,2 per cent compared to the end of 2008.

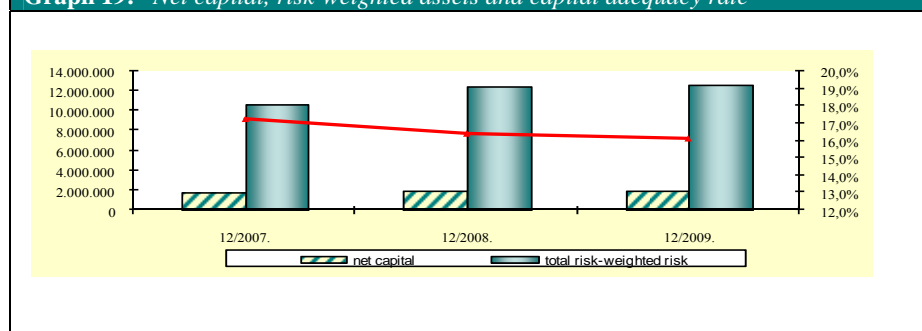
One of the most significant indicators of capital strength and adequacy¹⁹ of banks is capital adequacy ratio calculated as a ratio of net capital and risk weighted assets. As of 31.12.2009., this ratio at the banking system level was 16,1% which is lower by 0,3 per cent than at the end of 2008. The reason was the increase of total risk weighted risk by 2% or 237 million KM. Although the risk of risk-weighted assets and credit equivalents decreased from 12,3 billion KM to 11,8 billion KM due to the decline of credit activities of banks in 2009 and consequently the entire credit portfolio, as well as decrease of risk off-balance sheet items, there was, on the other hand, significant increase of²⁰ risk-weighted operating risk (POR) (from 131 million KM to 883 million KM). As result, the increase of total risk-weighted risks was noted. At the end of 2009, structural 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 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 profit they generate to pay out dividends, but to rather strengthen their capital base.

- 000 KM-

DESCRIPTION	31.12.2007.	31.12.2008.	31.12.2009.	RATIO	
				3/2	4/3
				5	6
1. NET CAPITAL	1.857.109	2.038.997	2.043.573	110	100
2. RISK WEIGHTED ASSETS AND CREDIT EQUIVALENTS	10.740.880	12.301.441	11.786.614	115	96
3. POR (RISK WEIGHTED OPERATING RISK)	-	130.975	882.928	-	674
4. TOTAL RISK WEIGHTED RISKS (2+3)	10.740.880	12.432.416	12.669.542	116	102
5. NET CAPITAL RATE (CAPITAL ADEQUACY) (1/ 4)	17,3%	16,4%	16,1%	95	98

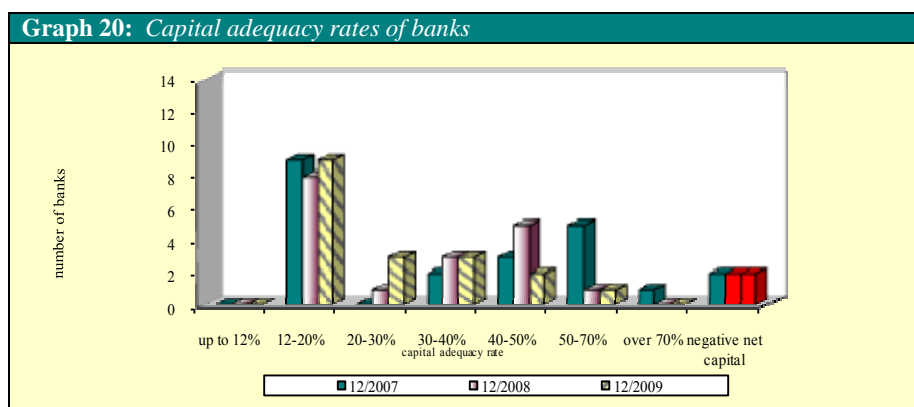
Graph 19: Net capital, risk-weighted assets and capital adequacy rate



¹⁹ The Law prescribes minimum capital adequacy rate of 12%.

²⁰ In accordance with Decision on Changes and Amendments to Decision on Minimum Standards for Operating Risk Management in Banks (Official Gazette of the FBiH, number 40/09) as of 31.12.2009. the new methodology of the capital requirements calculation for operating risk is in effect.

The global financial crisis effects are also evident in the segment of capital, that is, in the capital adequacy rate, mostly due to the profitability decline in almost all banks in the system (profit decline, that is, loss increase), so the net capital remained at almost the same level as at the end of 2008 (2,04 billion KM), as well as the increase of risk assets by 2%. Capital adequacy rate of the banking system, as of 31.12.2008., was reduced by 0,3 per cent, amounting to 16,1% as of 31. 12. 2009., which is still significantly above 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.



Of total 20 banks in the FBiH, as of 31.12.2009., capital adequacy rate of 18 banks was higher than minimum prescribed by the law of 12%, while two banks, under provisional administration, recorded capital adequacy rate below 12%, that is, negative adequacy rate. According to analytical data at the end of 2009, 14 banks recorded the capital adequacy rate lower than prior year, four banks recorded better rate, while two banks under provisional administration recorded negative rate. Three largest banks in the system succeeded to improve their capital adequacy, which is especially important for systemic significance of those banks and their impact to stability of the entire banking sector.

Preview of capital adequacy rates of 18 banks in comparison to the minimum prescribed by the law of 12% is the following:

- Nine banks had the rate between 12,5% and 20%, and the three largest banks from 13,7% to 15,3%,
- Eight banks had the rate between 21% and 50%,
- One bank had the rate between 51% and 70%.

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. Following bank expansion and performing regular supervision of this segment, when acting towards banks, depending on the evaluation of their capital adequacy and risk profile, the FBA takes different corrective and supervisory measures, such as: adoption of strategy to maintain certain level of capital and plan which will provide for quantity and quality (structure) of that capital in accordance with the nature and complexity of bank's present and future business activities and the undertaken and potential risk, then intensified supervision and monitoring of bank, request to supply additional capital in order to strengthen capital base, and elimination of excessive credit risk concentrations

and related limitation and decrease of credit risk exposure related to certain types of concentrations, monitoring of implementation and realization of adopted capital plans, especially for additional capital supplied from external resources, supervision of compliance and implementation of the ordered measures, etc.

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)²¹ of banks in the FBiH as of 31.12.2009., amounted to 18 billion KM, the same as at the end of 2008. Gross assets²² in the amount of 15,7 billion KM are higher by 2% or 242 million KM than the previous year.

Off-balance sheet risk items amounted to 2,3 billion KM and are lower by 12% or 311 million KM.

-in 000 KM-

Table 20: Assets off-balance sheet items and potential loan losses								
DESCRIPTION	AMOUNT (in 000 KM)						RATIO	
	31.12.2007.	Struct. %	31.12.2008.	Struct. %	31.12.2009.	Struct. %	4:2	6:4
1.	2	3	4	5	6	7	8	9
Loans	8.660.761	59,6	10.200.134	66,0	9.442.600	60,1	118	93
Interests	53.512	0,4	59.564	0,4	61.797	0,4	111	104
Past due claims	210.585	1,4	231.890	1,5	352.580	2,2	110	152
Claims for paid guarantees	3.638	0,0	2.353	0,0	1.620	0,0	65	69
Other placements	61.910	0,4	39.393	0,2	276.693	1,8	64	702
Other assets	5.552.875	38,2	4.937.976	31,9	5.578.188	35,5	89	113
TOTAL ASSETS	14.543.281	100,0	15.471.310	100,0	15.713.478	100,0	106	102
OFF-BALANCE SHEET	2.453.214		2.582.093		2.271.512		105	88
ASSETS WITH OFF-BALANCE SHEET	16.996.495		18.053.403		17.984.990		106	100
RISK ASSETS WITH OFF-BALANCE SHEET	11.624.445		13.304.610		12.579.883		114	95
General loan risk and Potential loan losses	409.833		461.839		534.652		113	116
General and Special loan loss reserves already established	409.895		461.687		534.681		113	116

Non-risk items amount to 5,4 billion KM or 30% of total assets with off-balance sheet, and they increased by 14% in comparison to the end of 2008. On the other hand, risk assets with off-balance sheet items amount to 12,6 billion KM, and they decreased by 5% or 725 million KM.

In 2009, the impact and negative consequences of the global financial and economic crisis in BiH, are increasingly more apparent in banks operations, as a result of the transfer of crisis from real to the banking sector, with the largest impact on banks' key operation and that is the segment of lending and asset quality. In the last quarter of 2008, banks significantly decreased and limited growth of new placements, which was continued in 2009, so credit placements recorded a significant downfall of 6% or 638 million KM in 2009. As of 31.12.2009., these items amounted to 9,8 billion KM and their participation in the assets was 64,3%. In 2009, there

²¹ 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).

²² Data source: Report on classification of balance sheet assets and off-balance sheet items of banks.

were 31% less placements when compared to the same period last year and the new placements were mainly financed through repayment of the previous placements. The most significant limiting factor to the credit growth 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. It is certain that in the forthcoming period there will be further deterioration in quality of the credit portfolio, increase of bad placements and consequently credit losses, which will have an adverse reflection to the financial result of banks.

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.

Although an impact of the crisis to the credit portfolio of banks in the Federation was less obvious in the first months of 2009, it could be stated it was more expressed due to a deepening of the crisis and deterioration of entire economic condition in BiH. This was primarily reflected through an increase of past due claims by 52% and their participation in total loans from 2,3% to 3,6%.

Although, a significant downfall of loans was realized on the level of the system of 6% or 637 million KM, the analytical data from the banks indicate that this is mainly due to decrease of loans by 17% or 496 million KM in the largest bank in the system. Seven other banks recorded a smaller downfall in loan portfolio and ten banks had an increase in loans of 339 million KM.

Three largest banks in the FBiH with credit amount of 6,3 billion KM have participation of 65% in total loans at the system level.

In the aspect of sectors to which banks originate their loans, as of 31.12.2009., loans originated to private companies decreased by 185 million KM amounting to 4,7 billion KM or 47,9% of total loans. Loans originated to citizens have decreased by 7% or 381 million KM, amounting to 4,8 billion KM, representing participation of 48,6%. The data submitted by banks, as of 31.12.2009., in the aspect of loan structure originated to citizens (based on the purpose), do not record any change over longer period of time, that is, the highest participation of approx. 72% have loans originated to finance consumer goods²³, 25% have housing loans, and remaining 3% have loans for SMEs and agriculture.

As for other sectors, with total participation of 3%, major change has been recorded with non-banking financial institutions, where the loans decreased from 105 million Km to 51 million KM.

Three largest banks in the system financed 66,4% of total loans originated to citizens, and to private companies 63,2% of total loans to all sectors, which for citizens sector remains at the same level as at the end of 2008, and the other sector recorded six per cent lower than the previous year.

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

²³ Short- term operation included.

-in 000 KM-

SECTORS	31.12.2007.		31.12.2008.		31.12.2009.		INDEKS	
	Amount	Partic. %	Amount	Partic. %	Amount	Partic. %	4/2	6/4
1	2	3	4	5	6	7	8	9
Government institutions	32.556	0,4	76.964	0,7	74.609	0,8	236	97
Public enterprises	211.465	2,4	175.424	1,7	184.005	1,9	83	105
Private enterprises and assoc.	3.998.141	45,0	4.881.526	46,8	4.696.276	47,9	122	96
Banking institutions	26.768	0,3	5.805	0,1	6.755	0,1	22	116
Non-banking financial instit.	114.084	1,3	105.352	1,0	51.255	0,5	92	49
Citizens	4.461.965	50,3	5.146.963	49,3	4.765.656	48,6	115	93
Other	30.005	0,3	42.343	0,4	18.244	0,2	141	43
TOTAL	8.874.984	100,0	10.434.377	100,0	9.796.800	100,0	118	94

Currency structure of loans has also been unchanged for longer period: loans financed with currency clause had the highest participation of 76% or 7,4 billion KM, loans in domestic currency of 23% or 2,3 billion KM, while loans in foreign currency had the lowest participation of only 1% or 125 million KM.

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 categories²⁴ and off-balance sheet items are presented in the following table:

Classification category	AMOUNT (in 000 KM) and PARTICIPATION (in %)									RATIO	
	31.12.2007.			31.12.2008.			31.12.2009.			5/2	8/5
	Assets classif.	Partic. %	GLR PLL	Assets classif.	Partic. %	GLR PLL	Assets classif.	Partic. %	GLR PLL		
1	2	3	4	5	6	7	8	9	10	11	12
A	9.876.208	85,0	197.719	11.534.783	86,7	230.749	10.257.169	81,5	205.159	117	89
B	1.478.711	12,7	105.446	1.446.503	10,9	103.385	1.804.767	14,3	136.973	98	125
C	143.658	1,2	35.717	165.309	1,2	40.558	307.892	2,4	72.970	115	186
D	122.003	1,1	67.086	154.168	1,2	83.300	206.201	1,6	115.703	126	134
E	3.865	0,0	3.865	3.847	0,0	3.847	3.854	0,0	3.847	99	100
Risk assets (A-E)	11.624.445	100,0	409.833	13.304.610	100,0	461.839	12.579.883	100,0	534.652	114	95
Nonrisk assets²⁵	5.372.050			4.748.793			5.405.107			88	114
TOTAL	16.996.495			18.053.403			17.984.990			106	100
OFFBALANCE SHEET ITEMS											
	430.069	90,1		429.419	89,0		506.041	89,4		100	118
Susp. Interest	46.929	9,9		54.479	11,0		59.760	10,6		116	110
TOTAL	476.998	100,0		483.898	100,0		565.801	100,0		101	117

²⁴ 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%.

²⁵ 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%.

Risk assets with off-balance sheet items (A-E) amounted to 12,6 billion KM, and, as of 31.12.2009., these items decreased by 5% or 725 million KM. Non-risk items amounted to 5,4 billion KM. These items increased by 14% in comparison to the end of 2008.

If an analysis of the risk assets quality is performed, it could be concluded, over the observing period, there was a stronger downfall of asset quality and its deterioration as an impact of the economic crisis and an increase of non-payable claims, that is, delinquency of customers to pay past due loan liabilities. Classified assets (B – E), in comparison to the end of 2008, recorded a significant growth of 31,2% or 553 million KM, primarily due to an increase of special mentioned placements (category B) of 25% or 358 million KM, while nonperforming assets (C-E) increased by 60% or 195 million KM. Furthermore, over the same period, the assets were charged off (write off to the off-balance sheet) in the amount of 136 million KM. Classified assets, as of 31.12.2009., amounted to 2,3 billion KM, and nonperforming assets were 518 million KM. Due to decreased lending activities of banks and loan placements, good assets (category A) decreased by 11% or 1,3 billion KM, amounting to 10,3 billion KM at the end of 2009.

As result of the mentioned, the indicators of asset quality expressed as ratio, that is, participation of individual categories in risky assets have deteriorated in comparison to the end of 2008. This is raising a concern, especially since more adverse effects are expected to happen over the upcoming quarters. The classified assets to risky assets ratio has deteriorated by 5,2 per cent due to an increase of classified assets (31,2%) and downfall of risky assets (5%) in comparison to the end of 2008, which is currently representing 18,5%.

If an analysis is performed of only the ratio and trend of nonperforming assets and risk assets, as of 31.12.2009., this ratio was 4,1%, which is still relatively low ratio, and, if compared to the end of 2008, it is higher by 1,7 per cent. However, if we take into account that participation of category B in the risk assets is 14,3% (10,9% at the end of 2008), and the increasing 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 (as confirmed through on-site examinations, resulting by insufficient loan loss reserves), it could be concluded that the assets quality still has a decreasing trend. That is why it is of key importance that banks more realistically evaluate quality of their placements and establish adequate loan loss reserves, especially due to the fact that under an impact of the crisis delinquency concerning payment of past due claims increase, provisioning increases, and the earnings of banks decrease, and therefore a portion of bad loans hides through the highest increase of category B.

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 23: Classification of loans originated to citizens and legal entities

Classification category	AMOUNT (in 000 KM) and PARTICIPATION (in%)												RATIO
	31.12.2008.						31.12.2009.						
	Citizens	Partic. %	Legal entities	Partic. %	TOTAL Amount	Partic. %	Citizens	Partic. %	Legal entities	Partic. %	TOTAL Amount	Partic. %	
1	2	3	4	5	6 (2+4)	7	8	9	10	11	12 (8+10)	13	14
A	4.825.699	93,76	4.125.628	78,03	8.951.327	85,79	4.311.231	90,46	3.421.255	68,00	7.732.486	78,93	86
B	203.799	3,96	971.259	18,37	1.175.058	11,26	260.509	5,47	1.298.642	25,81	1.559.151	15,91	133
C	71.580	1,39	84.803	1,60	156.383	1,50	108.969	2,29	193.570	3,85	302.539	3,09	193
D	45.885	0,89	105.724	2,00	151.609	1,45	84.947	1,78	117.677	2,34	202.624	2,07	134
E	0	0,00	0	0,00	0	0,00	0	0,00	0	0,00	0	0,00	0
TOTAL	5.146.963	100,00	5.287.414	100,00	10.434.377	100,00	4.765.656	100,0	5.031.144	100,0	9.796.800	100,00	94
Class.loans B-E	321.264	6,24	1.161.786	21,97	1.483.050	14,21	454.425	9,53	1.609.889	32,00	2.064.314	21,07	139
NPL C-E	117.465	2,28	190.527	3,60	307.992	2,95	193.916	4,07	311.247	6,19	505.163	5,16	164
Loans structure	49,33		50,67		100,00		48,64		51,36		100,00		
Participation by sectors in classified loans, nonperforming loans and category B:													
Classification B-E	21,66		78,34		100,00		22,02		77,98		100,00		
NPL C-E	38,14		61,86		100,00		38,39		61,61		100,00		
Category B	17,34		82,66		100,00		16,71		83,29		100,00		

As of 31.12.2009., of total loans originated to legal entities in the amount of 5,03 billion KM, 1,6 billion KM or 32% was classified in categories B to E (1,2 billion KM or 22% at the end of 2008), while of total loans originated to citizens in the amount of 4,8 billion KM, classification categories B to E represent 454 million KM or 9,5% (321 million KM or 6,2% at the end of 2008).

Of loans finance to legal entities, 311 million KM was classified as nonperforming loans or 56,2% of total loans originated to this sector (as of 31.12.2008., these items amounted to 191 million KM or 3,6%). Nonperforming loans, in the sector of citizens, amounted to 194 million KM or 4,1% of total loans originated to this sector (as of 31.12.2008., these items amounted to 117 million KM or 2,3%), as result of high growth rate of 65% over the observing period.

The observed indicators of the quality of loans originated to legal entities and citizens, as well as already stated indicators of the quality of total risky assets, show a decreasing trend in 2009, especially in the third and fourth quarter, which is primarily a result of growth in categories B and C in both sectors, especially in the sector of legal entities (in the sector of citizens category B 28%, category C 52%, and the legal entities 34% and 128% respectively), resulting by an increase of participation , primarily of category B (in citizens from 4,0% to 5,5%, and in legal entities from 18,4% to 25,8%), as well as other indicators for those two sectors and the entire loan portfolio have deteriorated. 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-

Table 24: 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 31.12.2008.	95.693	8.860	333.170	43.456	428.863	52.316
<i>Changes in 2009:</i>						
- new charge offs (current year)	72.677	9.888	63.771	11.231	136.448	21.119
- payments made in the current year	20.055	5.743	20.609	3.591	40.664	9.334
- permanent charge off	1.657	232	16.949	4.109	18.606	4.341
Balance as of 31.12.2009.	146.658	12.773	359.383	46.987	506.041	59.760

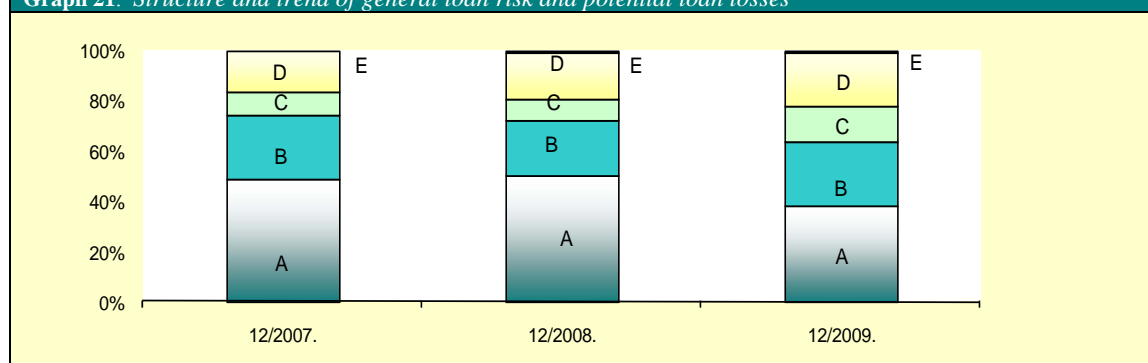
Balance of the charged off assets, as of 31.12.2009., (506 million KM), and the suspended interest (59,8 million KM) generated an increase of 18% in comparison to the end of 2008. There was a significant assets charge-off in the second six months and it is by 2,8 times higher than the charge off for the first two quarters of 2009.

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 25: Structure and trend of general loan risk and potential loan losses

Classification category	AMOUNT (in 000 KM) and STRUCTURE (in%)						RATIO	
	31.12.2007.		31.12.2008.		31.12.2009.		4/2	6/4
	2	3	4	5	6	7	8	9
A	197.719	48,2	230.749	50,0	205.159	38,4	117	89
B	105.446	25,7	103.385	22,4	136.973	25,6	98	132
C	35.717	8,7	40.558	8,8	72.970	13,7	113	180
D	67.086	16,4	83.300	18,0	115.703	21,6	124	139
E	3.865	1,0	3.847	0,8	3.847	0,7	100	100
TOTAL	409.833	100,0	461.839	100	534.652	100	113	116

Graph 21: 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 2008, general loan risk and potential loan loss provisions have increased by 16%, amounting to 535 million KM, while relative ratio of risky assets and off-balance sheet items have increased from 3,47% to 4,25%, if compared to the end of 2008. As of 31.12.2009., banks in average allocated for category B 7,6%, for category C 23,7%, category D 56,1% 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 still 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-

Description	ORIGINATED LOANS ²⁶			RATIO	
	31.12.2007.	31.12.2008.	31.12.2009.	3/2	4/3
	1	2	3	4	5
Shareholders over 5% of voting rights, subsidiaries and other related enterprises	26.083	26.823	29.191	103	109
Supervisory Board and Audit Board members	145	304	470	210	155
Bank Management	2.355	2.315	2.193	98	95
TOTAL	28.583	29.442	31.854	108	108
Potential and undertaken off-balance sheet liabilities	1.936	10.304	5.137	532	50

While level of transactions with the mentioned categories of related entities that are subject to reporting had increased in 2008, especially of potential and undertaken liabilities based on guarantees issued for "sister" leasing companies in BiH (two banks), in 2009, credit exposures to persons related to banks increased by 8%, while potential liabilities were significantly decreased, primarily due to expiration of the mentioned guarantees and loans that were originated. Based on

²⁶ Apart from loans, it includes other claims, deposited funds and the placements to shareholders (financial institutions) exceeding 5% of voting rights.

the presented data, we could conclude that it is 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

According to the final non-audited data in the financial statements that present the success of banks' performance, that is, in the income statement for 2009, at the banking system level in the Federation of BiH, there was minimum profit reported of only nine thousand KM, while in 2008, the profit was 50 million KM. Main reason to this dramatic downfall of the financial result is simultaneous decrease of profit in banks that had positive performance and increase of losses in banks that reached the amount of the generated profit, resulting by the mentioned amount of profit for the entire system level. Major influence to deterioration of profitability of almost all banks had increase of loan loss provisions, as result of considerable decline in quality of loan repayments, that is, increased loan delinquency, as well as downfall in interest income on loans and other placements.

High oscillations in the reported financial result at the sector level, if compared to the periods over the past three years, were mainly under influence of the events in stock exchanges related to price changes in securities trading, such as high income in 2007, that is, high expenses in 2008, while in 2009, the main reason of such bad financial result, as already mentioned, was decline in loan portfolio quality and consequently increased loan loss provisions.

Positive financial result of KM 52.975 thousand KM was generated by 13 banks, which is less by 41% or KM 36 million than in the same period in 2008. At the same time seven banks reported loss of KM 52.966 thousand KM, which is higher by 36% or KM 14 million than in the same period of last year.

Detailed data is shown in the following table:

-000 KM-

Date/Description	At the system level		State banks		Private banks	
	Amount	Number of banks	Amount		Amount	Number of banks
31.12.2007.						
Loss	-8.156	4	-420	1	-7.736	3
Profit	118.092	18	3.182	2	114.910	16
Total	109.936	22	2.762	3	107.174	19
31.12.2008.						
Loss	-38.938	5	-761	1	-38.177	4
Profit	88.977	15	464	1	88.513	14
Total	50.039	20	-297	2	50.336	18
31.12.2009.						
Loss	-52.966	7	-964	1	-52.001	6
Profit	52.975	13	518	1	52.457	12
Total	9	20	-447	2	456	18

Similar to other segments, this segment has also encountered concentrations: of total profit generated (53 million KM), 71% or 37,7 million relates to two largest banks in the system, with

participation in the assets of the banking sector is 50,3%, while in total loss of the same amount as profit, two foreign owned banks, of which one has participation in the assets of 14,7% in the system and 3rd rated in the system, represent 63,7% or 33,7 million KM. Analytical data indicate that total of 13 banks reported worse financial result (by 53,7 million KM), while seven banks reported slightly better result (by 3,7 million KM).

The financial result of state owned banks does not have any significant influence to the overall profitability of the banking sector. Of two state owned banks, one reported the 2009 year end positive financial result, and the other one operated with loss.

Based on the analytical data and the indicators of 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 overall profitability of the system has considerably declined in comparison to the past years. Generally in the system, and especially in large banks that generate profitability, the actual generated income is smaller as a result of the total income at minimum rate by majority of banks due to decreased total income and considerable increase of loan loss provisions, which was to expect under the environment of stronger effect of the economic crisis.

At the system level, total income was realized in the amount of 815 million KM with decreasing rate of 3% or 21 million KM in comparison to 2008. Total noninterest bearing expenses were 809 million KM, and growth rate was 6% or 46 million KM which had negative reflection to the overall financial result of the sector.

Total interest income amounts to 919 million KM, and, if compared to the last year, it shows a decrease of 3% or 27 million KM. In the structure of total income, their participation decreased from 113,1% to 112,7%. Although credit placements in 2009 were lower by 6%, interest income on loans increased by 3% and their participation in total income, in comparison to the past year, increased from 97,6% to 103,6%. In the structure of interest income, highest participation of 54,8% was realized by interest income on credit placements of citizens that in total credit portfolio have participation of 48,6%. The next in line are interest income on loans originated to private companies with participation of 42,7% and participation in credit portfolio of 47,9%. Based on the mentioned, it can be concluded that credit portfolio of citizens is still more profitable for banks and less risky in terms of lower level of nonperforming assets in the structure of credit placements, and because of much higher interest rates on loans originated to citizens, which at the end of 2009, in average, were higher by 20% to 30% than the interest rates on loans to companies.

Positive changes were recorded in interest expenses that in comparison to prior year recorded downfall of 7% or 31 million KM, amounting to 397 million KM in 2009, while their participation in the structure of total income was decreased from 51,1% to 48,7%.

In the structure of interest expenses, interest expenses on deposits realized growth of 4% or 10,7 million KM as result of the increase of interest-bearing deposits by 6%, as part of which the increase of term deposits was 4,5%. Their participation in the structure of total income was increased from 34,9% to 37,1%. Decrease of long term credit indebtedness of banks, primarily with foreign financial institutions (“parent” banks or related banks from the group and in the financial markets with other creditors) of 19%, followed by the funds of subordinate debt of 6% resulted by decrease of interest expenses based on loans taken of 34% or 38 million KM.

Net interest income in the amount of 522 million KM increased by only 1% or 3,1 million KM with insignificant increase of participation in the structure of total income from 62,0% to 64,1%.

Operating income amounts to 293 million KM, and, if compared to the prior year, it records a downfall of 8% or 24,5 million KM, and their participation in the structure of total income decreased from 38,0% to 36%. As part of operating income, there was nominal and percentage growth of 2,4 million KM or 1% realized based on fees. Decrease of operating income is mainly related to a downfall of other operating income.

Total noninterest expenses had a faster growth (6%) than the net interest income (1%) and they amount to 809 million KM as of 31.12.2009., which represents an increase of 46 million KM if compared to the same period last year. At the same time, their participation in the structure of total income has increased from 91,3% to 99,3%.

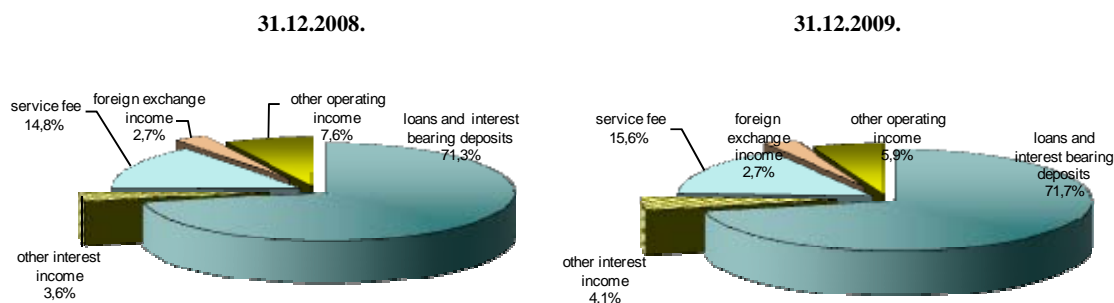
Within the noninterest expenses, only other operating expenses recorded a downfall of 26% or 38 million KM, and their participation in the structure of total income has decreased from 17,6% to 13,4%. An opposite trend and changes, that is, a significant growth of 43% or 68 million KM was recorded by loan loss provisions, which, at the end of the observing period, amounted to 225,9 million KM, with an increase in the structure of total income from 18,8% to 27,7%, followed by business premises and fixed assets expenses of 158,9 million KM with growth rate realized of 5% or 7,7 million KM, representing 19,5% of total income, as well as salary and contribution expenses with the growth rate of 2% or 5,6 million KM, amounting to 248,7 million KM to represent 30,5% of total income.

Trend and structure of total income and expenses is presented in the following tables and graphs:
- in 000 KM-

Table 28: Structure of total income

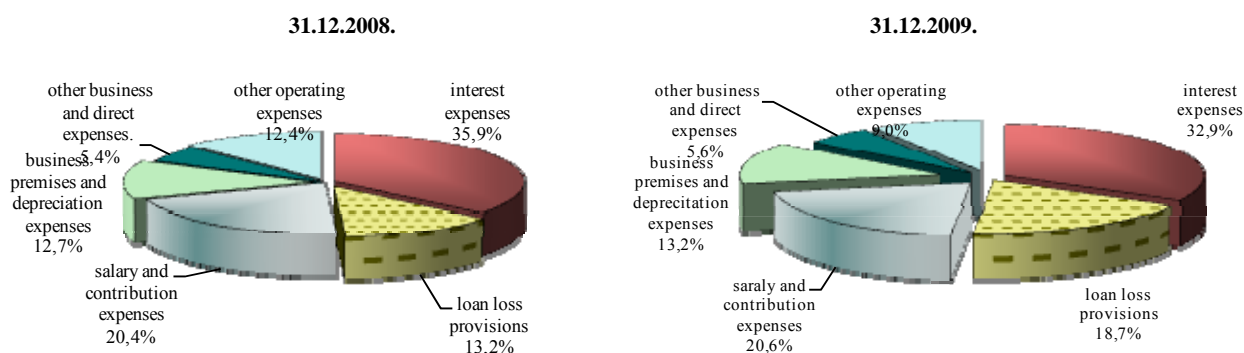
Structure of total income	31.12.2007.		31.12.2008.		31.12.2009.		RATIO	
	Amount	%	Amount	%	Amount	%	4/2	6/4
1	2	3	4	5	6	7	8	9
I Interest income and similar income								
Interest bearing deposit accounts with depository institutions	121.966	10,7	84.585	6,7	23.848	2,0	69	28
Loans and leasing	666.417	58,7	816.338	64,6	844.681	69,7	122	103
Other interest income	46.141	4,1	45.254	3,6	50.163	4,1	98	111
TOTAL	834.524	73,5	946.177	74,9	918.692	75,8	113	97
II Operating income								
Service fees	168.362	14,8	186.477	14,8	188.891	15,6	111	101
Foreign exchange income	33.054	2,9	35.063	2,7	33.129	2,7	106	94
Other operating income	99.404	8,8	95.970	7,6	70.990	5,9	96	74
TOTAL	300.820	26,5	317.510	25,1	293.010	24,2	106	92
TOTAL INCOME (I + II)	1.135.344	100,0	1.263.687	100,0	1.211.702	100,0	111	96

Graph 22: Structure of total income



- in 000 KM-

Structure of total expenses	31.12.2007.		31.12.2008.		31.12.2009.		RATIO	
	Amount	%	Amount	%	Amount	%	4/2	6/4
1	2	3	4	5	6	7	8	9
I Interest expenses and similar expenses								
Deposits	225.465	22,3	291.575	24,5	302.305	25,1	129	104
Liabilities for borrowings	83.192	8,3	112.074	9,4	73.593	6,1	135	66
Other interest expenses	15.139	1,5	23.664	2,0	20.804	1,7	156	88
TOTAL	323.796	32,1	427.313	35,9	396.702	32,9	132	93
II Total non-interest bearing expenses								
General loan risk and potential loan losses Provisioning	177.279	17,6	157.552	13,2	225.939	18,7	89	143
Salary expenses	219.730	21,8	243.089	20,4	248.716	20,6	111	102
Business premises and depreciation expenses	124.706	12,3	151.159	12,7	158.884	13,2	121	105
Other business and direct expenses	58.260	5,8	64.247	5,4	66.945	5,6	110	104
Other operating expenses	105.410	10,4	147.415	12,4	108.993	9,0	140	74
TOTAL	685.385	67,9	763.462	64,1	809.477	67,1	111	106
TOTAL EXPENSES (I + II)	1.009.181	100,0	1.190.775	100,0	1.206.179	100,0	118	101

Graph 23: Structure of total expenses

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

- in %-

RATIOS	31.12.2007.	31.12.2008.	31.12.2009.
Return on Average Assets	0,85	0,35	0,00
Return on Average Total Capital	8,07	3,33	0,00
Return on Average Equity	11,64	5,02	0,00
Net Interest Income/Average Assets	3,97	3,61	3,44
Fee Income/Average Assets	2,34	2,21	1,93
Total Income/Average Assets	6,31	5,82	5,37
Operating and Direct Expenses ²⁷ /Average Assets	1,83	1,54	1,93
Operating Expenses/Average Assets	3,50	3,77	3,40
Total Non-interest Expenses/Average Assets	5,33	5,31	5,34

²⁷ Expenses include provisions for potential loan losses.

-in %-

RATIOS	31.12. 2009.		
	STATE BANKS	PRIVATE BANKS	AVERAGE IN THE FBiH
Return on Average Assets	-0,26	0,00	0,00
Return on Average Total Capital	-1,06	0,03	0,00
Return on Average Equity	-1,31	0,04	0,00
Net Interest Income/Average Assets	2,27	3,45	3,44
Fee Income/Average Assets	5,46	1,89	1,93
Total Income/Average Assets	7,74	5,34	5,37
Operating and Direct Expenses/Average Assets	1,42	1,94	1,93
Operating Expenses/Average Assets	6,52	3,37	3,40
Total Non-interest Expenses/Average Assets	7,94	5,31	5,34

Further drastic downfall of profitability in 2009, at the system level, resulted by downfall of key profitability indicators (ROAA - Return on Average Assets and ROAE - Return on Average Equity) that as of 31.12.2009. were reduced to the level of 0,00%. Productivity of banks, measured as ratio of total income and average assets, continues with decreasing trend (from 5,82% to 5,37%) primarily due to decrease of total income, noting that downfall has slightly slower intensity, since on the other hand average total assets realized increase. It should be emphasized a high increase of business and direct expenses per average assets (from 1,54% to 1,93%), which is related to the increase of loan loss provisions. Banks tried to amortize downfall of income and increase of the mentioned expenses by decreasing operating expenses, so this ratio has improved by 0,37 per cent (from 3,77% to 3,40%).

All key financial indicators of profitability analyzed based on the ownership criteria in banks indicate that private banks operate more cost-effectively, productively and efficiently, which gives them competitive advantage if compared to state banks, emphasizing the need to finish privatization process in remaining state banks.

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. 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

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.,

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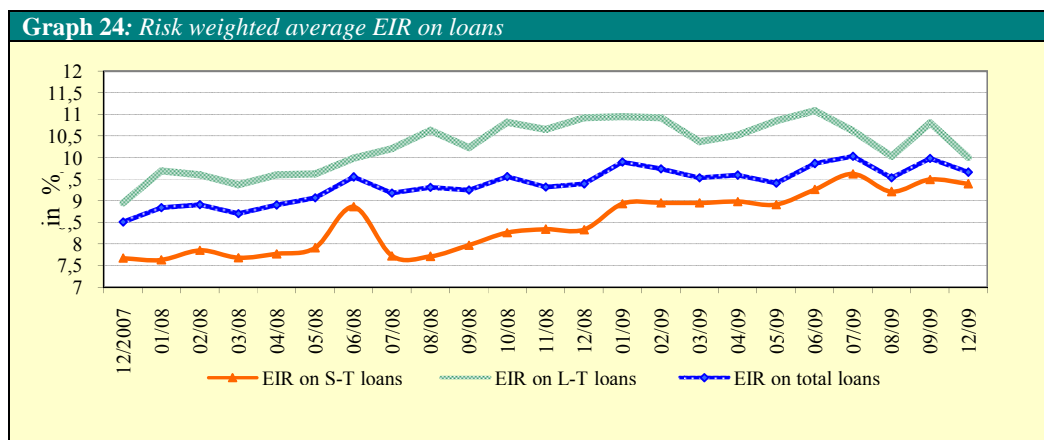
prescribed unified method of computation and disclosure of effective interest rate²⁸ for all banks that have their seat in the Federation of BiH, and their organizational units, regardless of the territory in which they operate, including organizational units of the banks operating in the Federation 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 decursive 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 prescribed²⁹.

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 2007, and, for June and December of 2008, and June and December of 2009:

DESCRIPTION	31.12.2007.		30.06.2008.		31.12.2008.		30.6.2009.		31.12.2009.	
	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR
1	2	3	4	5	6	2	3	4	5	6
1. Risk-weighted interest rates for short-term loans	7,34	7,67	7,51	8,86	7,82	8,33	8,41	9,26	8,55	9,39
1.1. Economy	7,19	7,45	7,39	8,76	7,74	8,19	8,4	9,1	8,51	9,27
1.2. Citizens	11,22	13,47	10,83	13,6	10,25	13,04	10,03	13,94	9,51	12,9
2. Risk-weighted interest rates for long-term loans	8,23	8,83	9,22	9,99	9,95	10,92	9,92	11,09	9,16	10
2.1. Economy	7,49	7,85	8,16	8,6	8,33	8,92	8,7	9,62	8,46	9,15
2.2. Citizens	8,93	9,75	9,91	10,88	11,16	12,54	10,82	12,2	10,21	11,31
3. Total risk-weighted interest rates for loans	7,86	8,51	8,56	9,55	8,69	9,39	8,91	9,86	8,82	9,66
3.1. Economy	7,31	7,62	7,7	8,7	7,88	8,37	8,45	9,19	8,50	9,23
3.2. Citizens	9,05	9,96	9,95	10,99	11,09	12,58	10,75	12,34	10,17	11,42



²⁸ Decision on unified method of computation and disclosure of effective interest rates on loans and deposits (“Official Gazette of the FBiH”, number 27/07).

²⁹ 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-weighted 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 a computation of the loan price. That is the reason why the EIR represents a real loan price.

The risk-weighted EIR for loans, as opposed to 2008, with major oscillations in changes of interest rates and an increasing trend recorded in the second half of the year, during 2009, there were slight interest rates changes in both directions, but staying within 0,62%, the highest level being in July of 2009, (10,03%), and the lowest in May of 2009 (9,41%). In December 2009, an average EIR was 9,66%, which was higher by 0,27 per cent than in December of 2008.

The risk-weighted EIR for short-term loans, in December 2009, was 9,39%, representing a significant 1,06 per cent higher than in December 2008.

The risk-weighted EIR for long-term loans, in December 2009, was 10%, which was lower by 0,92 per cent than in December 2008.

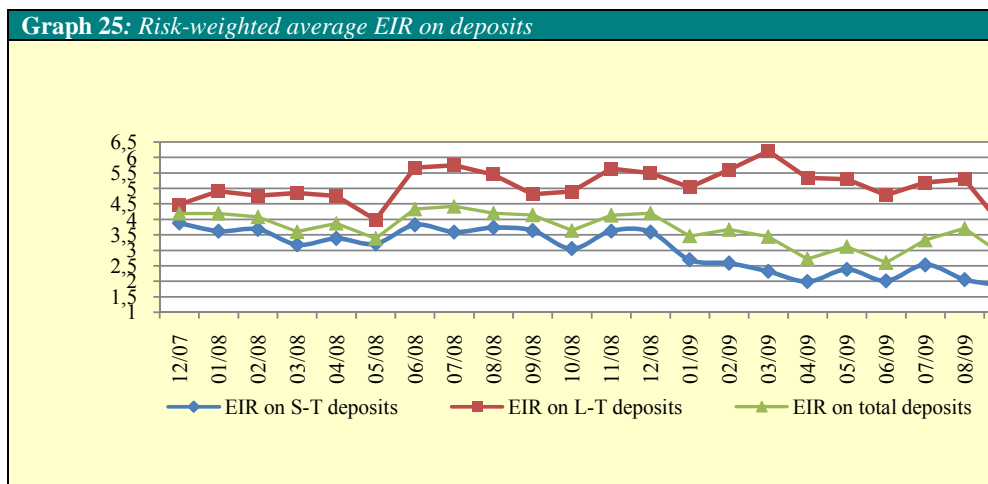
Interest rates for loans originated in the two most significant sectors: economy and citizens³⁰, over the observing period of 2009, have been changing in opposite directions. However, the risk weighted EIR for loans originated in the economy, although still much lower than the EIR for loans to citizens, had a growth trend, for both short-term and long-term loans. In comparison to December of 2008, EIR for short-term loans increased for 1,08 per cent (from 8,19 to 9,27), while the increase for the long term loans was 0,23 per cent, that is from 8,92% to 9,15%. The total interest rate for loans to the economy increased for 8,37% from December of 2008 to 9,23% in December of 2009.

EIR on short term loans to citizens in the first half of 2009, had a growth trend (from 13,04% in December 2008, to 13,94% in June 2009), but at the end of the year realized a decrease to 12,9%. In December of 2008, EIR for long term loans to the same sector was 12,54%, after downfall of 1,22 per cent, to 11,32% in December 2009. The total EIR for loans to citizens in the compared period, in December 2008 and December 2009, decreased from 12,58 to 11,42%.

Risk-weighted NIR and EIR for term deposits, computed based on monthly statements, for the banking sector are presented in the following table:

Table 33: Risk-weighted average NIR and EIR on deposits										
DESCRIPTION	31.12.2007.		30.06.2008.		31.12.2008.		30.06.2009.		31.12.2009.	
	NIR	EIR	NIR	EIR	NIR	NIR	EIR	NIR	EIR	NIR
1	2	3	4	5	6	2	3	4	5	6
1. Risk-weighted interest rates on short term deposits	3,87	3,88	3,82	3,82	3,59	3,59	1,99	2,01	1,06	1,06
1.1. up to 3 months	3,85	3,85	3,94	3,94	3,48	3,49	1,74	1,74	0,72	0,72
1.2. up to 1 year	3,92	3,92	3,6	3,6	4,13	4,14	3,8	3,95	2,90	2,91
2. Risk-weighted interest rates on long term deposits	4,48	4,48	5,67	5,67	5,48	5,49	4,72	4,78	4,75	4,77
2.1. up to 3 years	4,65	4,66	5,49	5,49	5,41	5,42	4,58	4,66	4,72	4,74
2.2. over 3 years	4,32	4,33	6,46	6,47	6,34	6,33	6,14	6,11	5,12	5,13
3. Total risk-weighted interest rates on deposits	4,18	4,19	4,33	4,33	4,2	4,2	2,57	2,6	1,82	1,83

³⁰ Based on the methodology of classification in sectors: entrepreneurs are included in the sector of citizens.



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 2008, risk-weighted EIR for total term deposits, in December 2009, decreased by 2,37 per cent (from 4,2% to 1,83%). The same changes were recorded in the EIR for short-term (from 3,59% to 1,06%) and long-term deposits (from 5,49% to 4,77%). In short term deposits, primary decrease comes from the EIR downfall on term deposits up to three months (from 3,49% to 0,72%). Banks in December 2009 paid to the economy lower interest rates on term deposits (1,10%) than to citizens (3,75%), and such interest rates were lower than in December 2008. Reason to this significant downfall of EIR on deposits to the economy is decrease of EIR on short term deposits, that is, changes in the maturity structure, since majority of short term deposits to the economy in December 2009 had the term to three months for which EIR was 0,33% (3,49% in December 2008). At the same time, EIR on term deposits to the economy from three months to one year was considerably increased, where the interest rate increased from 0,11% (December 2008) to 3,96% (December 2009).

The EIR for short-term citizen deposits has decreased from 2,84% (December 2008) to 2,38% in December 2009.

In December of 2009, the risk-weighted EIR for long-term economy deposits was 5,45%, and the citizens 4,64% (in December 2008, 6,13% and 5,31%).

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:

DESCRIPTION	31.12.2007.		30.06.2008.		31.12.2008.		30.06.2009.		31.12.2009.	
	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR	NIR	EIR
1	2	3	4	12	14	2	3	4	12	14
1. Risk-weighted interest rates for loans-overdrafts	8,89	9,01	8,59	8,58	8,62	8,81	8,56	9,00	8,96	8,96
2. Risk-weighted interest rates for demand deposits	0,37	0,37	0,41	0,41	0,40	0,40	0,40	0,40	0,41	0,41

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 December 2009, was 8,96% (an increase of 0,15 per cent in comparison to December 2008), and 0,41% for demand deposits, which was the same as in December 2008.

2.4. Liquidity

Liquidity risk management, along with credit risk, is one of the most compound and most important segments of banking operation. 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.

Over the last quarter of 2008, following a spillover of the global crisis and its adverse impact to the financial and economic system in BiH, the liquidity risk has increased. Although there was a withdrawal of some portion of saving deposits and undermined confidence to banks, an estimate was made that there was no time of the banking system's liquidity being harmed, since all banks in the FBiH, due to regulatory requirements and limits prescribed, had significant liquid assets and sound liquidity position.

The adverse changes from the last quarter of 2008 were stopped in 2009, and main liquidity indicators, primarily thanks to decreased lending activities, have improved, so the statement remains that liquidity of the banking system in the Federation of BiH is still sound, with a 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.

Additional concern is raised by the fact that an impact of the crisis is increasing to the real sector, and its adverse consequences will reflect to the entire economic environment in which banks in BiH operate.

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 31.12.2009., deposits still have the highest participation of 72,5% that have increased, over the observing period, by 6% or 584 million KM. The next item are loans taken (including the subordinated debt³¹) with participation of 13,2% 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, majority structure of deposits is considerably unfavorable, although it has been some time of an improving trend.

- in 000 KM-

Table 35: Maturity structure of deposits

DEPOSITS	31.12.2007.		31.12.2008.		31.12.2009.		RATIO	
	Amount	Partic. %	Amount	Partic. %	Amount	Partic. %	4/2	6/4
1	2	3	4	5	6	7	8	9
Savings and demand deposits	4.747.689	46,6	4.186.773	40,0	4.490.845	40,7	88	107
Up to 3 months	430.784	4,2	460.100	4,4	322.763	2,9	107	70
Up to 1 year	1.045.768	10,3	979.516	9,4	833.089	7,5	94	85
1. Total short term	6.224.241	61,1	5.626.389	53,8	5.646.697	51,1	90	100
Up to 3 years	2.722.927	26,7	3.018.766	28,9	3.292.619	29,8	111	109
Over 3 years	1.243.809	12,2	1.816.695	17,4	2.106.552	19,1	146	116
2. Total long term	3.966.736	38,9	4.835.461	46,2	5.399.171	48,9	122	112
TOTAL (1 + 2)	10.190.977	100,0	10.461.850	100,0	11.045.868	100,0	103	106

Analysis of maturity structure of deposits in two main groups, if compared to 2008, shows a decrease of short term deposits participation by 2,7 per cent, and by the same percentage an increase of long term deposits, so their participation, as of 31.12.2009., was 51,1% and 48,9% respectively. Major influence to this change was made by replacement of credit funds by long term deposit of one bank.

Total short term deposits, if compared to 2008, increased by 20,3 million KM or 0,4%, observing that in the fourth quarter of 2008, the decline was 634 million KM or 10%.

The increase was realized from increased demand deposits of 7%, while deposits up to three months were decreased by 30% along with decrease in participation from 4,4% to 2,9%, and deposits to 1 year that decreased by 15%, which is why their participation in total deposits decreased from 9,4% to 7,5%. Demand deposits still have the highest participation of 40,7% in total deposits, while deposits up to three months have the lowest participation of 2,9%. In total demand deposits, the highest participation is still recorded by citizen deposits (36%), which, in comparison to 2008, have decreased by 38 million KM or 2%.

Total long term deposits in 2009, in comparison to 2008, increased by 564 million KM or 12%. It should be emphasized that of long term deposits, two sectors show dominant participation: citizens of 43,8% and banking institutions of 34,6%. Citizen deposits in term deposits up to three years show the highest participation of 58,2% (51,8% at the end of 2008), while banking

³¹ Subordinated debt – loans taken and permanent liabilities.

institutions' deposits over three years show the highest participation of 72% (70% at the end of 2008).

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 36: Maturity structure of loans

LOANS	31.12.2007.		31.12.2008.		31.12.2009.		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	214.223	2,4	234.178	2,2	354.200	3,6	110	152
Short term loans	1.719.297	19,4	2.337.251	22,4	2.159.008	22,0	136	92
Long term loans	6.941.464	78,2	7.862.948	75,4	7.283.592	74,4	113	93
TOTAL LOANS	8.874.984	100,0	10.434.377	100,0	9.796.800	100,0	118	94

In 2009, long term loans, in comparison to 31.12.2008., have decreased by 7% or 579 million KM (since loans originated to citizens have the highest participation in the structure of long term loans, it should be pointed out that only a decrease in this segment represents 459 million KM), short term loans have also recorded a decrease of 8% or 178 million KM, while past due claims have increased by 52% or 121 million KM (private companies represent 92 million KM, citizens represent 32 million KM. In the structure of past due claims, 72% are private companies, 21% are citizens, and 7% are other sectors.

Sector analysis by maturity, in two most significant sectors, indicates that loans to citizens represent 90% of long term loans, and loans to private companies, of total originated loans, represent 59% of long term loans.

In the assets structure, as the most significant category, loans still have the highest participation of 64,3%, which has decreased by 4,9 per cent in comparison to the end of 2008 due to a decline of loans of 6% or 638 million KM. Cash funds have increased by 14% or 575 million KM, and their participation, in comparison to 31.12.2008., increased from 27,9% to 31,4%.

In 2009, 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%. 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 % -

Ratios	31.12.2007.	31.12.2008.	31.12.2009.
1	2	3	4
Liquid assets ³² / Total assets	34,5	28,3	31,9
Liquid assets / Short term financial liabilities	58,1	51,2	54,2
Short term financial liabilities / Total financial liabilities	67,3	62,9	66,9
Loans / Deposits and Borrowings ³³	73,7	82,6	76,4
Loans / Deposits, borrowings and subordinate debts ³⁴	72,2	80,9	75,0

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-

Description	31.12.2007.	31.12.2008.	31.12.2009.	RATIO	
	Amount	Amount	Amount	3/2	4/3
1	2	3	4	5	6
1. Average daily balance of cash assets	3.974.722	3.687.406	3.789.107	93	103
2. Minimum total daily balance of cash assets	3.686.972	3.310.173	3.341.965	90	101
3. Short term sources (accrual basis)	6.094.193	5.821.848	5.431.143	96	93
4. Liabilities:					
4.1. ten-day average 20% of Item 3	1.218.839	1.164.370	1.086.229	96	93
4.2. daily minimum 10% of Item 3	609.419	582.185	543.114	96	93
5. Meeting requirement :ten-day average					
Surplus = Item 1 – Item 4.1.	2.755.883	2.523.036	2.702.878	92	107
6. Meeting requirement :daily minimum					
Surplus = Item 2 – Item 4.2.	3.077.553	2.727.988	2.798.851	89	103

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 up to 180 days.³⁵

³² Liquidity assets in the narrow sense: cash and deposits and other financial assets with maturity below three months, except inter-banking deposits.

³³ Empiric standards: below 70%-very solid, 71%-75%-satisfactory, 76%-80%-marginal to satisfactory, 81%-85%-insufficient, over 85%-critical.

³⁴ Prior ratio has been modified. Subordinated debts are included in the sources, which gives more realistic indicator.

³⁵ 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.

- in 000 KM -

Table 39: Maturity match between financial assets and liabilities up to 180 days					
Description	31.12.2007.	31.12.2008.	31.12.2009.	RATIO	
	Amount	Amount	Amount	3/2	4/3
1	2	3	4	5	6
I. 1-30 days					
1. Financial assets	5.678.451	5.126.920	5.719.878	90	112
2. Financial liabilities	5.291.774	4.763.530	5.070.291	90	106
3. Difference (+ or -) = 1-2	386.677	363.390	649.587	94	179
<i>Accrual of requirement in %</i>					
a) Performed %= Item 1 / Item 2	107,3 %	107,6%	112,8%		
b) Required minimum %	100,0%	85,0 %	85,0 %		
Surplus (+) or shortage (-) = a - b	7,3%	22,6 %	27,8 %		
II. 1-90 days					
1. Financial assets	6.283.942	5.892.107	6.479.395	94	110
2. Financial liabilities	5.957.300	5.441.072	5.745.023	91	106
3. Difference (+ or -) = 1-2	326.642	451.035	734.372	138	163
<i>Accrual of requirement in %</i>					
a) Performed %= Item 1 / Item.2	105,5%	108,3%	112,8 %		
b) Required minimum %	100,0%	80,0%	80,0%		
Surplus (+) or shortage (-) = a - b	5,5%	28,3%	32,8%		
III. 1-180 days					
1. Financial assets	7.032.175	6.999.103	7.469.752	100	107
2. Financial liabilities	6.861.962	6.477.230	6.956.965	94	107
3. Difference (+ or -) = 1-2	170.213	521.873	512.787	307	99
<i>Accrual of requirement in %</i>					
a) Performed %= Item 1 / Item.2	102,5%	108,1 %	107,4%		
b) Required minimum %	95,0%	75,0 %	75,0 %		
Surplus (+) or shortage (-) = a - b	7,5%	33,1%	32,4%		

Based on the presented data, we may conclude that banks, as of 31.12.2009., 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.

Based on all of the above presented indicators, it may be concluded that the negative movements from the last quarter of 2008 have been stopped, and there is an apparent trend of improvement, so the liquidity of the banking system of the Federation of BiH is evaluated 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, through outflow of deposits and deterioration of deposit basis, and, on the other side, through a drained inflow of liquid funds due to the expected downfall of loan collection in 2009, 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.

2.3.2.5. 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.

In order to enable application and implementation of prudential principles in foreign exchange 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 Banks³⁶ 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.³⁷

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 31.12.2009., currency structure of banks' assets on the level of banking system recorded participation of items in foreign currencies of 17,1% or 2,6 billion KM (13,5% or 2 billion KM at the end of 2008). On the other hand, currency structure of liabilities is essentially different, since participation of liabilities in foreign currency is significantly higher of 56,7% or 8,6 billion KM (57,9% or 8,7 billion KM at the end of 2008).

The following table presents structure and trend of financial assets and liabilities and foreign currency position for EUR as the most significant currency³⁸ and total.

³⁶ “Official Gazette of F BiH”, Number. 3/03, 31/03, 64/03, 54/04.

³⁷ 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%.

³⁸ Source: Form 5-Foreign currency position.

-in million KM-

Table 40: Foreign currency adjustment of financial assets and liabilities (EUR and total)										
Description	31.12.2008.				31.12.2009.				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>I. Financial assets</i>										
1. Cash assets	1.213	14,2	1.738	18,2	1.697	19,4	2.150	22,2	140	124
2. Loans	149	1,8	185	1,9	90	1,0	124	1,3	60	67
3. Loans with currency clause	7.075	83,0	7.505	78,7	6.713	76,6	7.095	73,1	95	95
4. Other	83	1,0	110	1,2	269	3,0	336	3,4	324	305
Total (1+2+3+4)	8.520	100,0	9.538	100,0	8.769	100,0	9.705	100,0	103	102
<i>II. Financial liabilities</i>										
1. Deposits	5.333	65,5	6.292	68,7	5.704	68,9	6.585	71,5	107	105
2. Borrowings	2.045	25,1	2.095	22,9	1.689	20,4	1.727	18,7	83	82
3. Deposits and loans with currency clause	434	5,3	434	4,7	577	6,9	577	6,3	133	133
4. Other	332	4,1	338	3,7	313	3,8	322	3,5	94	95
Total (1+2+3+4)	8.144	100,0	9.159	100,0	8.283	100,0	9.211	100,0	102	101
<i>III. Off-balance sheet</i>										
1. Assets	71		73		50		57			
2. Liabilities	350		358		500		505			
<i>IV. Position</i>										
Long (amount)	96		94		36		46			
%	6,5%		6,4%		2,3%		3,0%			
Short										
%										
Limit	30%		30%		30%		30%			
Below limit	23,5%		23,6%		27,7%		27,0%			

If we analyze the structure of foreign currencies, we see a dominant participation of EUR in the financial assets³⁹, noticing increase of participation (from 71,1% to 78,8%) with increase of nominal amount from 1,4 billion KM to 2,1 billion KM. Participation of EUR in the liabilities has slightly increased from 88,4% to 89,3%, or almost the same level nominally of 7,7 billion KM.

However, calculation of the FX risk exposure also includes the amount of indexed items of assets (loans) and liabilities⁴⁰, which are especially significant in the assets (73,1% or 7,1 billion KM) this is slightly lower in relation to 31.12.2008. (78,7% or 7,5 billion KM). Other foreign currency assets items represent 26,9% or 2,6 billion KM, of which EUR items make 21,2% or 2,1 billion KM, and other currencies 5,7% or 0,5 billion KM (at the end of 2008, loans contracted with currency clause amounted to KM 7,5 billion with participation of 78,7%, and other items in EUR of 15,1% or 1,4 billion KM). Of total net loans (9,3 billion KM), 76% were contracted with currency clause, primarily tied to EUR (94,6%).

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 (9,2 billion KM)

³⁹ 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).

³⁹ 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).

items in EUR (primarily deposits) had the highest participation of 83,7% or 7,7 billion KM, while participation and amount of indexed liabilities was at minimum, amounting to 6,3% or 0,6 billion KM (at the end of 2008., participation of liabilities in EUR was 84,2% or 7,7 billion KM, while indexed liabilities were 4,7% or 0,4 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 2009, ranged within the prescribed limits.

As of 31.12.2009., there were 11 banks with long foreign currency position, and 9 with short position. At the system level, long foreign currency position represented 3% of banks' core capital, which is lower by 27% than the limit. Individual foreign currency position for EURO was 2,3%, with financial assets items being higher than financial liabilities (long position), representing a decline of 27,7% than the limit.

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 CONCLUSION AND RECOMMENDATIONS

Consolidation, development and stabilization of the banking sector of the Federation of BiH during reform implementation has reached an enviable level, so the upcoming activities should be aimed at preserving its stability as priority task in the current stressing 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 impact 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, emphasizing 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,
 - Continue permanent monitoring of banks, primarily those with systemic significance 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, etc.,
- 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;
- Accelerate finalization of the remaining provisional administrations and liquidations based on the conclusion made by the Management Board.

In addition, it is necessary to have further involvement of 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;
- Accelerate implementation of economic reform in the real sector in order to reach the level of the monetary and banking sector;
- Based on the proposal made by the Banks Association of BiH, and through the Ministry of Finance of the Federation of BiH, it is necessary to accelerate the activities in order to:
 - 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;
- Constant improvement of cooperation with the Banks Association in the area of professional development, change all laws and regulations which have become a limiting factor in bank development, introduction of new products, collection of claims and active involvement in the establishment of unified registry of irregular debtors – legal entities and individuals;

- 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.-19-3/10
Sarajevo, 30.03.2010.

ATTACHMENTS

ATTACHMENT 1..... General data about banks in the F BiH

**ATTACHMENT 2..... Legal Framework of the Banking Agency of
the FBiH and banks in the FBiH**

ATTACHMENT 3..... Balance sheet of banks, FBA Schedule

ATTACHMENT 4..... Citizen savings in banks of the F BiH

**ATTACHMENT 5..... Report on changes in balance sheet assets and
off-balance sheet risk items**

ATTACHMENT 6..... Income statement of banks

ATTACHMENT 7..... Report on capital balance and adequacy

ATTACHMENT 8..... Information about employees in banks of the F BiH

ATTACHMENT 1

Banks in the Federation of Bosnia and Herzegovina - 31.12.2009.

<i>No.</i>	<i>BANK</i>	<i>Address</i>		<i>Telephone</i>	<i>Director</i>
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	FIMA BANKA dd – SARAJEVO	Sarajevo	Kolodvorska br. 5.	033/720-070, fax:720-100	EDIN MUFTIĆ
4	HERCEGOVAČKA BANKA dd - MOSTAR	Mostar	Nadbiskupa Čule bb	036/332-901, fax:332-903	Prov.Admin. - Nikola Fabijanić - 16.04.2007.
5	HYPO ALPE-ADRIA-BANK dd - MOSTAR	Mostar	Kneza Branimira 2b	036/444-444, fax:444-235	PETAR JURČIĆ
6	INVESTICIONO-KOMERCIJALNA BANKA dd – ZENICA	Zenica	Trg B&H 1	032/448-400, fax:448-501	SUVAD IBRANOVIĆ
7	INTESA SANPAOLO BANKA D.D. BOSNA I HERCEGOVINA	Sarajevo	Obala Kulina bana 9a.	033/497-555, fax:497-589	ALMIR KRKALIĆ
8	KOMERCIJALNO-INVESTICIONA BANKA DD V.KLADUŠA	V.Kladuša	Ibrahima Mržljaka 3	037/771-253, fax:772-416	HASAN PORČIĆ
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	ADNAN ZUKIĆ
11	PRIVREDNA BANKA SARAJEVO dd – SARAJEVO	Sarajevo	Alipašina 6	033/277-700, fax:664-175	AZRA ČOLIĆ
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	Trampina 12/VI	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	KENAN BOZKURT
17	UNA BANKA dd – BIHAĆ	Bihać	Bosanska 25	037/222-400, fax: 222-331	Prov.Admin. - Stjepan Blagović - 01.05.2005.
18	UNICREDIT BANK dd – MOSTAR	Mostar	Kardinala Stepinca bb	036/312-112, fax:312-121	BERISLAV KUTLE
19	UNION BANKA dd – SARAJEVO	Sarajevo	Dubrovačka 6	033/561-000, fax: 201-567	ESAD BEKTEŠEVIĆ
20	VAKUFСКА BANKA dd – SARAJEVO	Sarajevo	M. Tita 13.	033/280-100, fax: 663-399	AMIR RIZVANOVIĆ
21	VOLKSBANK BH dd – SARAJEVO	Sarajevo	Fra Andela Zvizdovića 1	033/295-601, fax:295-603	REINHOLD KOLLAND

ATTACHMENT 2

LEGAL FRAMEWORK OF THE BANKING AGENCY OF THE FBiH, BANKS, MICROCREDIT ORGANIZATIONS AND LEASING COMPANIES IN THE FEDERATION OF BIH

Laws of the FBiH

Basic laws regulating work of the Banking Agency of the FBiH, banking, microcredit and leasing sectors

1. Law on Banking Agency of the Federation of BiH (“Official Gazette of the FBiH”, number 9/96, 27/98, 20/00, 45/00, 58/02, 13/03, 19/03, 47/06, 59/06, 48/08)
2. Law on Banks (“Official Gazette of the FBiH”, number 39/98,32/00, 48/01, 27/02, 41/02, 58/02, 13/03, 19/03 and 28/03)
3. Law on Microcredit organizations (“Official Gazette of the FBiH”, number: 59/06)
4. Law on Leasing („Official Gazette of the Federation of BiH number: 85/08 and 39/09)
5. Law on Development Bank of the Federation of BiH (“Official Gazette of the FBiH”, number: 37/08)
6. Decree on Criteria and Supervision Method of Development Bank of the FBiH, (“Official Gazette of the FBiH”, number: 57/08)

Other laws

1. Law on Enterprises (“Official Gazette of the FBiH” number 23/99, 45/00, 2/02, 6/02, 29/03 and 68/05, 91/07 and 84/08)
2. Law on Taking Over Public Limited Companies („Official Gazette of the FBiH“, number: 7/06)
3. Law on Financial Operations (“Official Gazette of the F BiH”, number 2/95, 14/97, 13/00 and 29/00)
4. Law on Foreign Exchange Operations (“Official Gazette of the F BiH”, number: 35/98)
5. Law on Bill of Exchange (“Official Gazette of the F BiH”, number 32/00, 28/03)
6. Law on Check (“Official Gazette of the F BiH”, number: 32/00)
7. Law on Obligations (“Official Gazette of RBiH” number 2/92, 13/93, Official Gazette of the FBiH number: 29/03)
8. Law on Opening Balance Sheet of Enterprises and Banks (“Official Gazette of the FBiH”, number 12/98, 40/99, 47/06, 38/08 and 65/09)
9. Law on Securities Market (“Official Gazette of the FBiH”, number: 85/08)
10. Law on Investment Funds (“Official Gazette of the FBiH”, number: 85/08)
11. Law on Securities Market (“Official Gazette of the FBiH”, number: 85/08)
12. Law on Securities Register (“Official Gazette of the FBiH”, number 39/98 and 36/99),
13. Law on Securities Commission (“Official Gazette of the FBiH” number 39/98 and 36/99)
14. Law on Payment Transactions (“Official Gazette of the FBiH”, number 32/00, 28/03)
15. Law on Termination of Law on Internal Payment System („Official Gazette of the FBiH“, number: 56/04)
16. Law on Accounting and Audit in the FBiH (“Official Gazette of the F BiH”, number: 83/09)

17. Law on Determination and Fulfillment Method of Internal Liabilities of the F BiH (“Official Gazette of the F BiH”, number 66/04, 49/05, 35/06, 31/08, 32/09 and 65/09)
18. Law on Determination and Fulfillment of Citizen Claims from Privatization Process (“Official Gazette of the F BiH”, number 27/97, 8/99, 45/00, 54/00, 7/01, 32/01, 27/02, 57/03, 44/04, 79/07 and 65/09)
19. Law on Debt, Indebtedness and Guarantees in the FBiH („Official Gazette of the FBiH“, number: 86/07)
20. Law on Treasury of the FBiH (“Official Gazette of the FBiH”, number: 19/03)
21. Law on Registration of Legal Entities in the FBiH (“Official Gazette of the FBiH”, number 27/05 and 68/05)
22. Law on Classification of Activities in the FBiH (“Official Gazette of the FBiH”, number: 64/07)
23. Law on Foreign Exchange Operations (“Official Gazette of the FBiH”, number: 35/98)
24. Law on Audit (“Official Gazette of the F BiH”, number: 32/05)
25. Law on Property-Legal Relationships (“Official Gazette of the FBiH”, number 06/9 and 29/03)
26. Law on Land Books in the F BiH (“Official Gazette of the F BiH”, number 19/03 and 54/04)
27. Law on Profit Tax (“Official Gazette of the F BiH”, number: 97/07)
28. Law on Salary Tax (“Official Gazette of the F BiH”, number: 10/08)
29. Law on Contributions (“Official Gazette of the F BiH”, number 35/98, 54/00, 16/01, 37/01, 1/02 and 17/06 and 14/08)
30. Law on Foreign Investments (“Official Gazette of the F BiH”, number 61/01 and 50/03)
31. Labor Law (“Official Gazette of the F BiH”, number 43/99, 32/00 and 29/03)
32. Law on Conflict of Interest in the Government Bodies in the F BiH (“Official Gazette of the F BiH”, number: 70/08)
33. Law on Violations of the FBiH (“Official Gazette of the F BiH”, number: 31/06)
34. Law on Courts in the F BiH (“Official Gazette of the F BiH”, number 38/95 and 22/06)
35. Law on Appraisers (“Official Gazette of the F BiH”, number 49/05 and 38/08)
36. Law on Free Access to Information in the FBiH („Official Gazette of the FBiH“, number: 32/01)
37. Law on Expropriation (“Official Gazette of the FBiH”, number: 70/07)
38. Law on Administrative Disputes („Official Gazette of the FBiH“, number: 9/05)
39. Law on Government of the F BiH („Official Gazette of the FBiH“, number 1/94, 8/95, 58/02, 19/03, 2/06 and 8/06)
40. Law on Bankruptcy Proceeding (“Official Gazette of the F BiH”, number 29/03, 32/04, 42/06),
41. Law on Liquidation Proceeding (“Official Gazette of the FBiH”, number: 29/03),
42. Law on Executive Proceeding (“Official Gazette of the F BiH”, number 32/03 and 33/06, 39/06-correction and 39/09),
43. Law on Civil Proceeding (“Official Gazette of the FBiH”, number 53/03, 73/05 and 19/06),
44. Law on Extrajudiciary Proceeding („Official Gazette of the FBiH“, number 2/98, 39/04, 73/05)
45. Law on Administrative Proceeding (“Official Gazette of the FBiH”, number: 2/98 and 48/99)
46. Law on Criminal Proceeding (“Official Gazette of the FBiH”, number 35/03, 37/03, 56/03, 78/04, 28/05, 55/06, 27/07, 53/07, and 9/09)
47. Law on Classification of Activities in the Federation of BiH (“Official Gazette of the FBiH”, number 64/07)
48. Law on Registration of Business Entities in the Federation of BiH (“Official Gazette of the FBiH”, number 27/05, 68/05, and 43/09)
49. Law on Tax Administration in the Federation of BiH (“Official Gazette of the FBiH”, number 33/02, 28/04, and 57/09)

50. Law on Implementation of Penal Sanctions in the Federation of BiH (“Official Gazette of the FBiH”, number 44/98, 42/99 and 12/09)
51. Law on Crafts and Similar Activities (“Official Gazette of the FBiH”, number 35/09)
52. Law on Tourist-Catering Activity (“Official Gazette of the FBiH”, number 19/09 and 28/03)
53. Law on Trading (“Official Gazette of the FBiH”, number 64/04)
54. Law on Unified System of Control Registry and Collection of Contributions (“Official Gazette of the FBiH”, number 42/09)
55. Law on Payment of Liabilities based on Old Foreign Currency Savings in the Federation of BiH (“Official Gazette of the FBiH”, number 62/09)
56. Law on Determination and Payment Method of Internal Liabilities of the Federation of BiH (“Official Gazette of the FBiH”, number 66/04, 49/05, 35/06, 31/08, 32/09 and 65/09)
57. Guidelines to Open and Close Accounts to Perform Payment Transactions and Records („Official Gazette of the FBiH“, number: 55/00, 61/05)
47. Guidelines on Conditions and Proceeding to Transporting Cash, Securities and Securities Registered as Foreign Currencies („Official Gazette of the FBiH“, number: 35/00)

Laws of BiH

1. Law on Prevention of Money Laundering (“Official Gazette of BiH“, number: 53/09)
2. Law on Deposit Insurance in BiH („Official Gazette of BiH“, number 20/02, 18/05, 100/08, and 75/09)
3. Law on Central Bank of BiH (“Official Gazette of BiH”, number 1/97, 29/02, 8/03, 13/03, 14/03, 9/05, 76/06)
4. Law on Competition („Official Gazette of the FBiH“, number 48/05, 76/07, and 80/09)
5. Law on Consumer Protection in BiH („Official Gazette of BiH“, number: 25/06)
6. Law on Protection of Personal Data („Official Gazette of BiH“, number: 49/06)
7. Law on Electronic Signature („Official Gazette of BiH“, number: 91/06)
8. Law on Classification of Activities in BiH („Official Gazette of BiH“, number 76/06 and 100/08)
9. Law on Meeting Liabilities for Old Foreign Currency Savings („Official Gazette of BiH“, number 28/06, 76/06 and 72/07)
10. Law on Temporary Postponement of Execution of Claims from Executive Decision against Budget of the Institutions of Bosnia and Herzegovina and International Liabilities of Bosnia and Herzegovina (“Official Gazette of BiH“, number 43/03 and 43/04)
11. Law on Accounting and Audit of Bosnia and Herzegovina (“Official Gazette of BiH“, number: 42/04)
12. Law on Temporary Suspension of Disposal of State Property of BiH (“Official Gazette of BiH“, number: 32/07)
13. Law on Supervision over the Markets in BiH (“Official Gazette of BiH“, number 45/04 and 44/07)
14. Law on Central Records and Data Exchange (“Official Gazette of BiH“, number 16/02 and 32/07)
15. Law on Indirect Taxation (“Official Gazette of BiH“, number 52/04 and 32/079)
16. Law on Treasury of Institutions of BiH («Official Gazette of BiH», number 27/00)
17. Law on Violations (“Official Gazette of BiH“, number: 41/07)
18. Roof Law on Pledges (“Official Gazette of BiH“, number 27/04 and 54/04)
19. Law on Value Added Tax (“Official Gazette of BiH“, number 9/05 and 35/05 and 100/08)
20. Law on Electronic Legal and Business Turnover (“Official Gazette of BiH“, number: 88/07)

21. Law on Conflict of Interest in the Government Institutions of Bosnia and Herzegovina (“Official Gazette of BiH“, number 16/02,12/04 and 63/08)
22. Law on Courts of Bosnia and Herzegovina (“Official Gazette of BiH“, number 29/00, 16/02, 24/02, 3/02, 37/03, 4/04 and 9/04, 32/07)
23. Law on High Court and Judicial Council (“Official Gazette of BiH“, number 15/02, 26/02, 35/02, 42/03, 10/04 and 32/07)
24. Law on Judiciary of Bosnia and Herzegovina (“Official Gazette of BiH“, number 42/03, 9/04 and 35/04)
25. Criminal Law of BiH (“Official Gazette of BiH“, number 37/03, 61/04, 30/05, 53/06, 55/06 and 32/07)
26. Law on Administrative Disputes of BiH (“Official Gazette of BiH“, number 19/02, 83/08 and 88/07)
27. Law on Criminal Proceeding of Bosnia and Herzegovina (“Official Gazette of BiH“, number 36/03, 26/04, 76/06, 32/07, 76/07, 15/08 and 58/08)
28. Law on Administrative Proceeding (“Official Gazette of BiH“, number 29/02 and 12/04, 88/07)
29. Law on Civil Proceeding before the Courts of Bosnia and Herzegovina (“Official Gazette of BiH“, number 36/04, 84/07);
30. Law on Civil Proceeding („Official Gazette of BiH“, number: 53/03);
31. Law on Mediation (“Official Gazette of BiH“, number: 37/04);
32. Law on Public Supplies of BiH („Official Gazette of BiH“, number 49/04, 19/05, 52/05, 8/06, 24/06 and 70/06)
33. Guidelines on Data, Information, Records, Identification Methods and Minimum Other Indicators for Effective Implementation of the Provisions of the Law on Prevention of Money Laundering („Official Gazette of BiH“, number: 17/05)
34. Conclusion on Authentic Interpretation of Laws, Other Regulations and General Acts (“Official Gazette of BiH“, number: 24/04)
35. Law on Customs Tariffs (“Official Gazette of BiH“, number 1/98, 5/98, 7/98, 22/98, 31/02, 32/04, 48/05, 76/06, and 39/09)

DECISION OF THE BANKING AGENCY OF THE FEDERATION OF BIH REGULATING WORK OF BANKS

1. Decision on Bank Supervision and Actions of the Banking Agency of the Federation of BiH (“Official Gazette of the F BiH“, number 3/03)
2. Decision on Minimum Standards for Capital Management in Banks (“Official Gazette of the F BiH“, number 3/03, 18/03, 53/06, 55/07, 81/07, 6/08)
3. Decision on Minimum Standards for Loan Risk and Assets Classification Management in Banks (“Official Gazette of the F BiH“, number 3/03, 54/04, 68/05)
4. Decision on Minimum Standards for Risk Concentration Management in Banks (“Official Gazette of the F BiH“, number 3/03, 6/03 correct., 18/03, 64/03, 1/06)
5. Decision on Minimum Standards for Liquidity Risk Management in Banks (“Official Gazette of the F BiH“, number 3/03, 12/04, 88/07, 6/08)
6. Decision on Minimum Standards for Foreign Exchange Risk Management in Banks (“Official Gazette of the F BiH“, number 3/03, 31/03, 64/03, 54/04)
7. Decision on Minimum Standards for Activities of Banks in Prevention of Money Laundering and Terrorism Financing (“Official Gazette of the F BiH“, number 3/03, 18/04, 5/05, 13/05)
8. Decision on Financial Disclaimer (“Official Gazette of the F BiH“, number 3/03)
9. Decision on Minimum Standards for Operations with Related Entities in Banks (“Official Gazette of the F BiH“, number 3/03)

10. Decision on Minimum Standards for Documenting Loan Activities in Banks (“Official Gazette of the F BiH”, number 3/03)
11. Decision on Minimum Standards for Internal Control System in Banks (“Official Gazette of the F BiH”, number 3/03)
12. Decision on Minimum Standards for Internal and External Audit in Banks (“Official Gazette of the F BiH”, number 3/03)
13. Decision on Conditions when Bank is Considered Insolvent (“Official Gazette of the F BiH”, number 3/03)
14. Decision on Procedure for Determination of Claims and Distribution of Assets and Liabilities in Liquidation of Banks (“Official Gazette of the F BiH”, number 3/03)
15. Decision on Reporting Forms Submitted by Banks to the Banking Agency of the Federation of BiH (“Official Gazette of the F BiH”, number 3/03, 18/03, 52/03, 64/03 correct., 6/04, 14/04, 54/04, 5/05, 43/07, 55/07, 81/07, 88/07, 6/08)
16. Decision on Reporting about Non-performing Customers Considered a Special Loan Risk (“Official Gazette of the F BiH”, number 3/03)
17. Decision on Minimum Scope in Form and Content of Program and Reporting about Economic-Financial Audit in Banks (“Official Gazette of the F BiH”, number 3/03, 64/03)
18. Internal Rating Criteria of Banks performed by the Banking Agency of the Federation of BiH (“Official Gazette of the F BiH”, number 3/03, 6/03 correct.)
19. Decision on Interest and Fee Accrual for Dormant Accounts (“Official Gazette of the F BiH”, number 7/03)
20. Decision on Amount and Conditions for Origination of Loans to Bank Employees (“Official Gazette of the F BiH”, number 7/03 and 83/08)
21. Guidelines for Licensing and Other Approvals Issued by the Banking Agency of the Federation of the F BiH”, 6/08 cleaned text)
22. Decision on Minimum Standards for Market Risks Management in Banks (“Official Gazette of the Federation of BiH“, number: 55/07, 81/07, 6/08 and 52/08 and 79/09)
23. Decision on Unified Accrual and Declaration of Effective Interest Rate on Loans and Deposits (“Official Gazette of the Federation of BiH“, number 27/07 and 46/09)
24. Decision on Minimum Standards for Operating Risk Management in Banks („Official Gazette of the F BiH“, number: 6/08 and 40/09).
25. Decision on Temporary Measures for Renegotiation of Citizen and Legal Entities’ Credit Liabilities (“Official Gazette of the F BiH”, number 02/10)
26. Decision on Determining Level of Fees to Conduct Supervision of Development Bank of the Federation of BiH (“Official Gazette of the F BiH”, 65/09)

DECISIONS OF THE BANKING AGENCY OF THE FEDERATION OF BIH REGULATING WORK OF MICROCREDIT ORGANIZATIONS

1. Decision on Requirements and Procedure for Issuance of License to Microcredit Foundations Created as a Result of Changed Form of Microcredit Organizations („Official Gazette of the Federation of Bah“, number: 27/07)
2. Decision on Requirements and Procedure for Issuance and Revoking of License and Other Approvals to Microcredit Organizations („Official Gazette of the Federation of BiH“, number: 27/07)
3. Decision on Requirements and Procedure for Issuance of License and Consent to Acquire Ownership Share by Investing and Transferring Property of Microcredit Foundation („Official Gazette of the Federation of BiH“, number: 27/07)

4. Decision on Supervision of Microcredit Organizations („Official Gazette of the Federation of BiH“, number: 27/07)
5. Decision on Form and Content of Reports Microcredit Organizations Submit to the Banking Agency of the Federation of BiH and Reporting Deadlines („Official Gazette of the Federation of BiH“, number: 27/07)
6. Decision on Level and Method of Establishing and Maintaining Loan Loss Reserves of Microcredit Organizations („Official Gazette of the Federation of BiH“, number: 27/07)
7. Decision on Other General Requirements for Microcredit Organizations („Official Gazette of the Federation of BiH“, number: 27/07)
8. Decision on Fees Microcredit Organizations Pay to the Banking Agency of the Federation of BiH („Official Gazette of the Federation of BiH“, number: 27/07)
9. Decision on Unified Method of Accrual and Declaration of Effective Interest rate on Loans and Deposits („Official Gazette of the Federation of BiH“, number: 27/07).

ATTACHMENT 3

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

in 000 KM

Ord. No.	DESCRIPTION	31.12.2007.	31.12.2008.	31.12.2009.
	ASSETS			
1.	Cash funds and deposit accounts at depository institutions	4.894.973	4.207.559	4.782.301
1a	Cash and non-interest deposit accounts	349.241	417.601	490.171
1b	Interest deposit accounts	4.545.732	3.789.958	4.292.130
2.	Trading securities	44.361	11.184	12.884
3.	Placements in other banks	69.314	90.415	111.019
4.	Loans, receivables in leasing and past due receivables	8.874.984	10.434.377	9.796.800
4a	Loans	8.660.593	10.199.978	9.442.455
4b	Receivables on leasing	168	221	145
4c	Past due receivables - loans and leasing	214.223	234.178	354.200
5.	Securities held until maturity	4.204	7.630	106.273
6.	Premises and other fixed assets	363.270	442.739	499.440
7.	Other real estate	41.846	24.768	25.780
8.	Investments in non-consolidated related enterprises	34.390	40.471	42.693
9.	Other assets	215.938	212.167	336.288
10.	MINUS: Reserves for potential losses	347.358	401.406	480.738
10a	Reserves on item 4 in Assets	334.139	381.215	458.803
10b	Reserves on Assets except item 4	13.219	20.191	21.935
11.	TOTAL ASSETS	14.195.922	15.069.904	15.232.740
	LIABILITIES			
12.	Deposits	10.190.977	10.461.850	11.045.868
12a	Interest deposits	9.368.121	9.586.215	10.180.008
12b	Non-interest deposits	822.856	875.635	865.860
13.	Loans - past due	7.376	3.025	2.744
13a	Balance of payable loans, unpaid	0	0	
13b	Unpaid - called for payment off-balance sheet items	7.376	3.025	2.744
14.	Loans from other banks	3.289	3.089	3.089
15.	Payables to Government	0	0	
16.	Payables on loans and other borrowings	1.856.471	2.176.594	1.771.978
16a	payable within one year	357.425	793.837	678.608
16b	payable longer than one year	1.499.046	1.382.757	1.093.370
17.	Subordinated debts and subordinated bonds	242.791	267.737	250.483
18.	Other liabilities	384.976	520.755	484.451
19.	TOTAL LIABILITIES	12.685.880	13.433.050	13.558.613
	CAPITAL			
20.	Permanent priority shares	26.224	26.136	25.028
21.	Common shares	1.018.997	1.091.879	1.145.627
22.	Shares issued	94.739	152.892	143.725
22a	Permanent priority shares	8.332	8.420	8.420
22b	Common shares	86.407	144.472	135.305
23.	Undistributed income and capital reserves	260.146	307.465	355.707
24.	Currency rate difference	0		
25.	Other capital	109.936	58.482	4.040
26.	TOTAL CAPITAL (20. TO 25.)	1.510.042	1.636.854	1.674.127
27.	TOTAL LIABILITIES AND CAPITAL (19+26)	14.195.922	15.069.904	15.232.740
	PASSIVE AND NEUTRAL SUBBALANCE	606.788	626.468	622.094

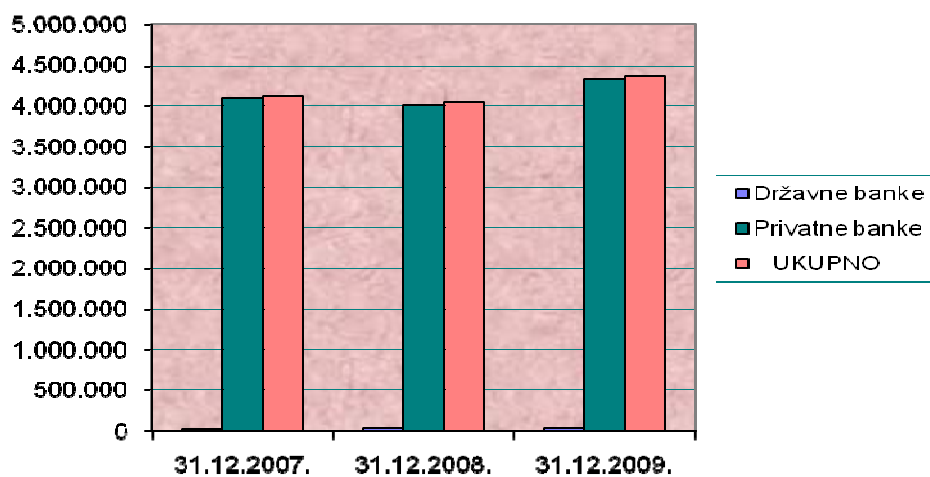
TOTAL BALANCE SHEET IN BANKS	14.802.710	15.696.372	15.854.834
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ATTACHMENT 4

NEW CITIZEN SAVINGS BY PERIODS

IN 000 KM

	31.12.2007.	31.12.2008.	31.12.2009.
State banks	30.469	32.481	35.275
Private banks	4.086.820	4.003.184	4.325.926
TOTAL	4.117.289	4.035.665	4.361.201



ATTACHMENT 5

**CLASSIFICATION OF ASSETS AND OFF-BALANCE SHEET RISK ITEMS
As of 31.12.2009.**

- ACTIVE BALANCE SHEET -

in 000 KM

Ord. No.	BALANCE SHEET ASSETS AND OFF-BALANCE SHEET ITEMS	CLASSIFICATION					TOTAL
		A	B	C	D	E	
1.	Short-term loans	1.709.155	430.652	13.586	5.615	0	2.159.008
2.	Long-term loans	5.946.822	1.018.083	223.655	95.032	0	7.283.592
3.	Other placements	272.736	3.894	29	34	0	276.693
4.	Interest accrued	41.869	19.924	4	0	0	61.797
5.	Past due receivables	76.092	110.275	64.236	101.977	0	352.580
6.	Receivables on guarantees paid	417	141	1.062	0	0	1.620
7.	Other assets	5.546.897	24.501	2.279	664	3.847	5.578.188
8.	TOTAL ACTIVE BALANCE SHEET	13.593.988	1.607.470	304.851	203.322	3.847	15.713.478
	a) Guarantees payable	313.383	56.709	861	570	0	371.523
9.	b) Performing guarantees	465.329	80.139	953	1.723	0	548.144
10.	Unsecured LoC	31.147	11.013	0	0	0	42.160
11.	Irrevocable loans	1.245.393	49.336	1.077	586	7	1.296.399
12.	Other potential liabilities	13.036	100	150	0	0	13.286
13.	TOTAL OFF-BALANCE SHEET	2.068.288	197.297	3.041	2.879	7	2.271.512
14.	TOTAL BALANCE AND OFF-BALANCE SHEET (8+13)	15.662.276	1.804.767	307.892	206.201	3.854	17.984.990
15.	General credit risk and potential loan losses (#14 x % of loss)	205.159	136.973	72.970	115.703	3.847	534.652
16.	Allocated general reserves (A) and special reserves (B, C, D, E)	205.186	136.973	72.972	115.703	3.847	534.681
17.	MORE (LESS) of the allocated reserves (#16 - 15) +or -	27	0	2	0	0	29

INCOME STATEMENT

in 000 KM

ELEMENTS	PERFORMED 31.12. 2008.		PERFORMED 31.12.2009.		RATIO 4 : 2 Amount
	Amount	Partic.in total income	Amount	učešće u ukupnom prihodu	
INCOME					
Interest income	946.177	113%	918.692	113%	97
Interest expenses	427.313	51%	396.702	49%	93
Net interest income	518.864	62%	521.990	64%	101
Fee income and other operating income	317.510	38%	293.010	36%	92
TOTAL INCOME	836.374	100%	815.000	100%	97
EXPENSES					
Reserves for potential losses	157.552	19%	225.939	28%	143
Salaries and contribution expenses	243.089	29%	248.716	31%	102
Fixed assets and overhead expenses	151.159	18%	158.884	20%	105
Other expenses	211.662	25%	175.938	22%	83
TOTAL EXPENSES (without interests)	763.462	91%	809.477	99%	106
NET INCOME BEFORE TAX	72.912	9%	5.523	1%	8
Income Tax	22.873	3%	5.514	1%	24
NET INCOME	50.039	6%	9		

ATTACHMENT 7

COMPARATIVE SCHEDULE OF CAPITAL BALANCE AND ADEQUACY

ACTIVE SUB-BALANCE SHEET

IN 000

KM

Ord. No.	DESCRIPTION	31.12.2007.	31.12.2008.	31.12.2009.
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	1.029.756	1.102.636	1.155.790
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	94.739	152.892	143.725
1.4.	General regulatory reserves (reserves as regulated by the Law)	65.945	84.319	78.317
1.5.	Other reserves not related to assets quality assessment	128.882	168.927	198.985
1.6.	Retained - undistributed income from previous years	130.354	134.220	161.562
1.a.	TOTAL (from 1.1. to 1.6.)	1.462.226	1.655.544	1.750.929
1.b.	Offsetting items from 1.a.			
1.7.	Uncovered losses transferred from previous years	65.908	73.464	82.324
1.8.	Losses from current year	8.156	38.938	52.966
1.9.	Book value of treasury shares owned by the bank	2	81	595
1.10.	Amount of intangible assets	52.089	60.311	63.119
1.b.	TOTAL (from 1.7.to 1.10.)	126.155	172.794	199.004
1.	AMOUNT OF CORE CAPITAL: (1.a.-1.b.)	1.336.071	1.482.750	1.551.925
2	BANK'S SUPPLEMENTARY CAPITAL			
2.1.	Share capital - common and perm. priority non-cumulat. shares - cash payments	2.917	2.829	2.829
2.2.	Share capital - comm. and perm. prior. non-cumul. shares-invested posses. And rights	0	0	
2.3.	General reserves for losses on loans from class. A - performing assets	197.782	230.596	205.186
2.4.	Accrued income for current year audited and confirmed by external auditor	93.945	74.543	49.186
2.5.	Income under FBA's temporary restriction on distribution	0	0	0
2.6.	Subordinated debts, the most 50% of core capital	191.575	211.360	184.093
2.7.	Hybrid convertible items - the most 50% of core capital	0	0	0
2.8.	Items-permanent liabilities without repayment duty	50.855	56.377	66.390
2.	AMOUNT OF SUPPLEMENTARY CAPITAL: (from 2.1. to 2.8.)	537.074	575.705	507.684
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	16.036	16.036
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	3.422	0
3.	AMOUNT OF OFFSETTING ITEMS FROM BANK'S CAPITAL (3.1. to 3.4.)	16.036	19.458	16.036
A.	AMOUNT OF BANK'S NET CAPITAL (1.+2.-3.)	1.857.109	2.038.997	2.043.573
B.	RISK FROM RISK-WEIGHTED ASSETS AND CREDIT EQUIVALENTS	10.740.880	12.301.441	11.786.614
C.	POR (RISK-WEIGHTED OPERATING RISK)		130.975	882.928
D.	PTR (RISK-WEIGHTED MARKET RISK)		0	0
E.	TOTAL RISK-WEIGHTED RISKS B+C+D	10.740.880	12.432.416	12.669.542
F.	NET CAPITAL RATE (CAPITAL ADEQUACY) (A.:B.) X 100	17,3%	16,4%	16,1%

NUMBER OF EMPLOYEES BY BANKS

Ord. No.	BANK	31.12.2007.	31.12.2008.	31.12.2009.
1	BOR BANKA dd SARAJEVO	42	45	51
2	BOSNA BANK INTERNATIONAL dd Sarajevo	145	171	185
3	FIMA BANKA dd SARAJEVO	101	149	133
4	HERCEGOVACKA BANKA dd MOSTAR	93	87	77
5	HVB CENTRAL PROFIT BANKA dd SARAJEVO	465		
6	HYPO ALPE ADRIA BANK dd MOSTAR	550	626	600
7	INTESA SANPAOLO BANKA dd BiH	479	501	514
8	INVESTICIJSKA BANKA FBiH SARAJEVO	104		
9	INVESTICIONO KOMERCIJALNA BANKA dd ZENICA	154	179	174
10	KOMERCIJALNO INVESTICIONA BANKA dd VELIKA KLADUŠA	65	67	68
11	NLB TUZLANSKA BANKA dd TUZLA	472	507	473
12	POŠTANSKA BANKA dd SARAJEVO	97	119	111
13	PRIVREDNA BANKA dd SARAJEVO	163	175	195
14	PROCREDIT BANK dd SARAJEVO	831	888	662
15	RAIFFEISEN BANK BH dd SARAJEVO	1.543	1.745	1.669
16	SPARKASSE BANK dd SARAJEVO	326	379	426
17	TURKISH ZIRAAT BANK dd SARAJEVO	129	149	152
18	UNA BANKA dd BIHAĆ	59	59	56
19	UNI CREDIT BANKA BH dd MOSTAR	840	1.418	1.389
20	UNION BANKA dd SARAJEVO	179	175	175
21	VAKUFСКА BANKA dd SARAJEVO	184	204	212
22	VOLKSBANK BH dd SARAJEVO	340	354	334
	TOTAL	7.361	7.997	7.656