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

INFORMATION

ON BANKING SYSTEM IN THE FEDERATION OF BOSNIA AND HERZEGOVINA As of 12/31/02

Sarajevo, March 2003

Banking Agency of the Federation of BiH, as regulatory institution performing supervision of banks, have completed Information on the Banking System of the Federation of BiH as of December 31st 2002 based on the reports of banks, and other reports and information submitted by banks. The information includes also findings and information attained during on-site examinations and analysis performed in the Agency (off-site control).

I INTRODUCTION

In last year, banking sector of the Federation of BiH was distinguished by further growth, consolidation and stabilization of the system, stronger competition, new services and products offers and adoption of changes and additions to regulations. In short, the transition is in the final phase. In future period we can expect more complete implementation of international standards in operations and establishment of modern market environment.

Based on the non-audited balance sheet from banks, at the end of last year, total balance sheet in banks in the Federation of BiH was KM 4.6 billion which is larger by 828 million or 22% in comparison to the end of 2001. Satisfying growth ratio in the system was achieved thankfully to expansion of private banking. Privately owned banks recorded assets growth of 25% and at the same time, state owned banks recorded reduction of eight percent. If we observe that from another perspective, the growth of balance sheet resulted from increased depository potentials by 628 million or 22% and, which is very significant, growth of capital by 124 million or 25%. The capital increased out of cash payments of KM 114.3 million, 110 million out of that amount was paid by foreign investors. Part of those assets was spent for settling earlier losses (83.7 million) and it resulted in decrease of remaining unsecured losses from 93 to 9.3 million of KM, that is, the losses decreased by 90%, if we do not include losses from 2002 in the calculation.

The whole banking system, consist of 29 banks, attained positive financial results. As it was recorded by banks, 20 bank closed previous year with profit of 39.7 million of KM, and eight banks had loss of total KM 22.3 million. Therefore, the whole system earned profit of KM 17.4 million. These indicators do not include Hercegovacka Bank that is under Provisional administration by the order of the High Representative.

Although maturity adjustment of assets and liabilities is not satisfactory yet (75.9% were short term), especially in comparison to the loan maturity adjustment, it is necessary to emphasize that this structure is continuously changed and long-term loans increased from 9.5% (in 2000) to 14.7% (in 2001) and in 2002 they were 24.1%). Participation of deposits in total liabilities was 76.8%t thus that makes our banks almost in line with international average that is 80%.

After boom in 2001, citizens' savings recorded growth in 2002 as well. Total deposits given by citizens to banks were KM 1.44 billion which is 10% more in comparison to the end of 2001, and in comparison to 2000 savings were more than tripled!

Loan portfolio in banks increased during last year by 967 million of KM or by 56%. The major operations were borrowings to citizens. That activity recorded growth of KM 637 million or 102%! Borrowings to privately owned enterprises increased by 40% or KM 308 million. Maturity adjustment of assets and liabilities was not satisfactory and it can have negative impact to banks' liquidity in future period.

Together with satisfactory financial results, banking sector recorded further consolidation and stabilization of the system in last year. After impetuous changes in previous years, the last year there was not need or cause for instituting provisional administration in any bank. The FBA started a liquidation procedure (ICB) after request of the bank's owner. The regulator capital of KM 15 million was successfully attained. Majority of banks timely provided additional capital, and 10 banks merged in order to adjust to this regulation. That additionally helped increasing of large banks and decreasing number of small banks.

Although banks' capital base strengthened in last year, it is obvious that this sector still has weaknesses, which can affect safety in some banks and system in whole. Capitalization of banks (capital to assets ratio) decreased. In 2001 it was 16.2% and it decreased to 15.4% in 2002. Also, capital adequacy ratio for the whole system reduced from 26.3% in 2000, to 22.4% in 2001 and at the end of last year it was 19.8%. Essentially, capital growth, especially in large banks did not follow the growth of risk assets. According to its legal authorities, the FBA will implement corrective actions in order to resolve these weaknesses as soon as possible.

Significant results were achieved in the field of introduction of new banking products. That is mainly related to the credit card operations. 6 banks in the Federation of BiH have established their own data processing center and have already issued over 8,000 credit cards locally. At the same time, 12 banks issued international debit and credit cards. Banks should devote their full attention to non-monetary payment system, but this should be also helped by other institutions in the system.

Certain number of banks, very few so far, started electronic (on-line) banking. Some banks announced SMS banking, ATM network is still expanding, but it is still not expanded enough. Banks introduced savings for housing loans, etc.

Banks have, successfully and in the short period of time, taken over the entire internal payment system, which functions without any problems. However, that introduced increased danger of banks "being involved" in money laundering and terrorism financing. Few such attempts were registered and banks undertook actions to eliminate it. As supervisory institution, the FBA cooperated with banks to prevent money laundering and terrorism financing, and also coordinated its actions with the Financial Police, Ministry of Internal Affairs (MUP), Tax Administration, Prosecutor's Office, etc. After 12 target examinations performed in banks and their branches, and after findings in full scope examinations, the FBA ordered actions for correcting identified weaknesses and/or informed authorized institutions on their findings.

In August last year, Law on Changes and Additions to the Law on Banks was passed as continuation of system reforms: prudential principles are more severe, public revenues were protected, new actions for prevention of money laundering and terrorism financing were instituted etc. After all these changes and additions, the FBA have passed new, that is complied old, regulations to the new Law as of December 24th 2002, which was done within the regulated time frame.

II BANKING SYSTEM REFORM

A key element of financial stability in every country and one of the important preconditions for success of an overall economic reform of any country is strength and stability of the banking sector, which were goals established for reform and restructuring efforts in the Federation of BiH. The starting points for those plans were:

- elimination of problems inherited from previous system and induced by the war,
- transformation of ownership through the capital privatization in state banks and its sale in mainly privately owned banks,
- attraction of foreign investors and stronger competition,
- improvement of efficiency and objectivity of banking operations, strengthening capital base, introduction of international standards and new products, accepting worldwide organizational systems, operations and supervision.

1. PRECONDITIONS FOR REFORM

The amount and complexity of inherited problems is presented in the best way by information that at the beginning of the reform, negative net capital in banks amounted around 4 billion KM. If we include inappropriate, socialistic and insufficient regulatory framework, interference of the state, nonexistent market, lack of staff and other inadequacies, we can picture the complexity of the reform process, and its time consuming character.

Five years later, it is possible to conclude that significant progress and results were achieved. Net capital in banks is positive today, that is, it reached 697 million KM. The system became more stable, there are more larger banks now and all banks were strengthened. The new regulatory framework was developed and statutory regulations were designed displaying that we are leaving transition period and entering phase of creating true market environment.

Unfortunately, successful transformation of banking industry was not followed by changes in other sectors, especially in the real economy sector, which is still stagnating and, unless rate of reform becomes higher, this can become an impediment to further development of the banking sector. It is necessary to provide additional development of regulatory framework for any further progress, mainly by passing more adequate procedures for judgments and implementation of courts' executive orders, that is, to improve legal protection of the creditors.

2. PRIVATIZATION AND RESTRUCTURING

Bank privatization process should be finalized in 2003 by change of capital owners or by liquidation procedures.

We are expecting that number of banks in the Federation of BiH will decrease and will continue to do so, although that process will slow down in comparison to the previous period. New minimum capital requirement of KM 15 million (paid-in shareholders' capital and net capital) resulted in several mergers of banks in last year – Vakufska Bank and Depozitna Bank, Central Profit Bank and Travnicka Bank, Raiffeisen Bank BH and Reiffeisen HPB, ABS Bank and Seh-in Bank, Gospodarska Bank Sarajevo and LT Komercijalna Bank Livno.

If we observe this by size of assets, there were radical changes in the system. Only two largest banks, with over 500 million in assets, have a concentration of 35.9% of total assets in the system. In next three largest banks, with assets between 300 and 500 million, have a concentration of 25.5% of total assets. On the other hand, 8 banks in the Federation of BiH had assets under KM 50 million. Foreign investors own 67.3% of shareholders capital in the system.

3. THE BANKING AGENCY

The Banking Agency of the F BiH, as independent institution for supervision and licensing of banks, was founded at the end of 1996. From the very beginning, its activities were designed to create strong and stable banking system, market oriented and adjusted to international business and supervision standards in banks. The Law on the Banking Agency established its main duties of the Agency which, in short, are licensing banks for inception and operations, passing regulations, supervising banks and undertaking actions as regulated by the Law (this includes provisional administration and liquidation in banks).

In implementing reform process in the banking system, the FBA gave its full contribution, although it often faced disagreements.

Since the leading objective of the Agency is to protect money and interests of depositors, the Banking Agency of the FBiH initiated provisional administration in 19 banks in period between foundation of the Agency until end of 2002, while the High Representative initiated provisional administration in one bank. Out of this number, there are 3 banks that are still under provisional administration. Provisional administration was successfully resolved in three cases by mergers of those banks, liquidation process was initiated in 8 banks, out of that number, two liquidations were completed without negative outcome for depositors and shareholders, and one resulted in merger. The Agency filed requests for bankruptcy process in 6 banks, and this process is still pending with courts. Liquidation process is currently going on in 4 banks. In 2002, the FBA did not initiate liquidation in any bank, and in one bank the liquidation procedure was established upon the request of the owner.

International experience and international rules that banks are the most often destroyed "from inside" has been confirmed by examples in the Federation of BiH. Analysis performed during and after provisional administration and liquidation procedures displayed that main sources of problems in those banks were operations with related entities, disregarding regulations and laws passed by the FBA and criminal actions. Responsibility for that laws with managing and governing bodies of banks.

4. BANK SUPERVISION

Since 1975, the Basel Committee for Bank Supervision explores methods and declares actions to strengthen financial stability all over the world.

In order to promote and provide for an overall macroeconomic and financial stability, in 1997 the Basel Committee adopted 25 core principles, which should be respected in order to have efficient supervisory system.

These core principles are minimum requirements to be implemented and in many cases it is necessary to supplement them with other actions in order to comply with specific conditions and to regulate risks of financial systems of individual countries. The principles are related to preconditions for effective supervision of banks, licensing, prudential regulations and requirements, methods for continued supervision of banks, necessary information, official authorization of supervisors and cross-border banking.

Although they are, to certain extent, adjusted to actual conditions in our country, legal and regulatory framework for bank operations in FBiH is mostly consistent with international standards. Certainly, the degree of compliance of local regulatory framework to Basel Principles will be improved in the future period, all the more so since the Law on Changes and Additions to the Law on Banks that was declared in August 2002 provides in Article 69 that "The regulations passed by the Agency… are based on the core principles for supervision of banks as regulated by the Basel Committee for Bank Supervision."

5. CORE (BASEL) PRINCIPLES FOR EFFECTIVE BANK SUPERVISION AND IMPLEMENTATION OF THOSE PRINCIPLES IN FEDERATION OF BiH

Conditions for effective supervision

Principle 1: An effective system of banking supervision will have clear responsibilities and objectives for each agency involved in the supervision of banks. Each such agency should possess operational independence and adequate resources. A suitable legal framework for banking supervision is also necessary, including provisions relating to authorization of banking establishments and their ongoing supervision; powers to address compliance with laws as well as safety and soundness concerns; and legal protection for supervisors. Arrangements for sharing information between supervisors and protecting the confidentiality of such information should be in place.

Implementation: The principle consists of six parts. It is possible to say that regulations in FBiH are adjusted and applied related to each part of the principle. Supervisory functions have a clear definitions of duties and roles. There is regulatory framework which ensures provisioning independence and self-funding of the Agency. Full compliance to the Basel Principles was attained in 2002 when the High Representative imposed the Law on Changes and Additions to the Law on Banks which provides "limited immunity" to the FBA, Managing Board of the Agency and employees of the Agency. The role and the position of the Agency in the community is not clarified, so there is opinion that single bank can not fail if the Agency operates properly. Core principles determine that any bank can fail regardless of the degree of supervision. The responsibility for banks' operational results is exclusively a duty of bank's management, and risk is with customers who select the bank in which they would entrust their deposits.

Licensing and Ownership Structures

Principle 2: The permissible activities of institutions that are licensed and subject to supervision as banks must be clearly defined, and the use of the word "bank" in names should be controlled as far as possible.

Implementation: Law on Banks defines banking activities and limits the use of the word "bank". The existing regulation is fully complied with this principle.

Principle 3: The licensing authority must have the right to set criteria and reject applications for establishments that do not meet the standards set. The licensing process, at a minimum, should consist of an assessment of the banking organization's ownership structure, directors and senior management, its operating plan and internal controls, and its projected financial condition, including its capital base; where the proposed owner or parent organization is a foreign bank, the prior consent of its home country supervisor should be obtained.

Implementation: As the Law on Banks regulates, the FBA is authorized to establish criteria and reject applications for establishment of banks. The Agency has passed Guidelines for issuing licenses and other approvals of the Banking Agency of FBiH. The Guidelines are fully complied with this principle.

Principle 4: Banking supervisors must have the authority to review and reject any proposals to transfer significant ownership or controlling interests in existing banks to other parties.

Implementation: By the law, significant ownership rights in the bank with over 10%, 33%, 50% and 66.7% can not be acquired or increased without approval from the FBA, which has sufficient authority and which instituted procedures necessary to implement the law and this principle, and that is regulated with special Guidelines that are being strictly applied.

Principle 5: Banking supervisors must have the authority to establish the criteria for reviewing major acquisitions or investments by a bank and ensuring that corporate affiliations or structures do not expose the bank to undue risks or hinder effective supervision.

Implementation: The Law on Banks and FBA Decisions provide elaboration of this principle and different regulations and practice are complied with it.

Prudential and Safety Regulations and Requirements

Principle 6: Banking Supervisors must set minimum capital adequacy requirements for banks that reflect the risks that the bank undertakes, and must define the components of capital, bearing in mind its ability to absorb losses. For internationally active banks, these requirements must not be less than those established in the Basel. Capital Accord.

Implementation: The Law and FBA's Decision on Minimum Standards for Managing Capital in Bank regulate components of the capital and how capital should be managed. In general, the requirements are consisted with the Basel Principles, but we lack correlation with market, liquidity and foreign currency risks. The regulatory framework is mainly complied with this principle. The regulations should be improved in the future period in order to adjust them completely with the principles.

Principle 7: As essential part of any supervisory system is the independent evaluation of a bank's policies, practices, and procedures related to the granting of loans and making of investments and the ongoing management of the loan and investment portfolio.

Implementation: The Decision on Minimum Standards for Managing Credit Risk and Assets Classification and Decision on Minimum Standards for Internal and External Audit Systems, passed by the FBA, are the most complex regulations with detailed classification of assets including quality of collateral as key element. By these decisions, banks have to execute an audit of all risk areas and that is where we experience problems. On one hand, it is not rare that internal auditors are not independent (influenced by members of managing boards or members of bank management) so in some cases banks have good policies, but they do not respect them. On the other hand, it happens that external audit firms do not perform their job properly. Although there are good regulatory frameworks for evaluation of credit and investment risk, the problem is in the implementation of those regulations. Therefore, it is possible to say that practices are quite inadequately adjusted to Principle 7. The FBA will monitor operation of internal controls and external audits, and if necessary, apply corrective actions.

Principle 8: Banking supervisors must be satisfied that banks establish and adhere to adequate policies, practices, and procedures for evaluating the quality of assets and the adequacy of loan loss provisions and reserves.

Implementation: The regulatory frameworks are in place for adequate policies, practices and procedures in banks. From that point of view, there is full compliance to this principle. The problem is in the realization: banks are not fully adhered to laws and decisions, there are staffing constraints, there are transactions with related entities and other critical situations which narrow possibilities for resolving weaknesses in banks. In the previous period, the FBA has aggressively applied authorities and corrective actions in this area. The Agency will continue to implement those actions until the full compliance of this principle.

Principle 9: Banking supervisors must be satisfied that banks have management information system that enable management to identify concentrations within the portfolio and supervisors must set prudential limits to restrict bank exposures to single borrowers or groups of related borrowers.

Implementation: By the Law, FBA's Decision on Minimum Standards for Managing Risk Concentrations regulates in detail limits to exposure to credit risk and defines related entities of the bank. The FBA insists on application of the Decision although banks objected definition of related entity (they think that it is too broad) established in the Changes and Additions to the Law on Banks, referenced in this Decision.

Principle 10: In order to prevent abuses arising from connected lending, banking supervisors must have in place requirements that banks lend to related companies and individuals on an arm's-length basis, that such extensions of credit are effectively monitored, and that other appropriate steps are taken to control or mitigate the risks.

Implementation: Implementation of existing FBA regulations and laws is sufficient to prevent abuses from connected lending. However, there is still lack of basic credit culture and many shareholders still believe that the bank exists only in order to meet their needs. As a rule, these situations end in provisional administration, liquidation or bankruptcy of banks. In order to ensure full compliance to this principle, it is necessary to perform more frequent examinations in banks where such situation is identified.

Principle 11: Banking supervisors must be satisfied that banks have adequate policies and procedures for identifying, monitoring and controlling country risk and transfer risk in their international lending and investment activities, and for maintaining appropriate reserves against such risks

Implementation: The Law on Banks does not regulate precisely what is country risk. The only limitation is in the FBA's Decision on Minimum Standards for Managing Credit Risk. There is no regular process for assessing this risk. Although, for now, there are no banks in the FBiH that issue loans or make investments abroad in larger amounts, still it is necessary to gradually prepare appropriate regulations for future situations. The FBA is working on this.

Principle 12: Banking supervisors must be satisfied that banks have in place systems that accurately measure, monitor and adequately control market risks; supervisors should have powers to impose specific limits and/or a specific capital charge on market risk exposures, if warranted.

Implementation: Neither the Law on Banks nor FBA decisions currently address all aspects of market risk, that is, risk associated with securities or financial derivatives. There are no explicit requirements for banks to develop policies and procedures for identifying, measuring, monitoring and controlling market risk, outside of foreign currency risk. The Changes and Additions to the Law on Banks and appropriate FBA decisions created a possibility to establish certain limits and establish more severe capital requirements in relation to the discovered risk exposure level. Even though our financial market is still establishing, it is necessary to work on additional regulations and prepare for the future.

Principle 13: Banking supervisors must be satisfied that banks have in place a comprehensive risk management process (including appropriate board and senior management oversight) to identify, measure and control all other material risks and where appropriate, to hold capital against these risks.

Implementation: Since the banking system was predominantly faced with traditional types of risks, FBA has been primarily concerned with credit risk, fraud and related entity abuse. In general all those risks are related to credit functions. However, losses may occur in area of non-traditional banking operations and, from now, further development of banking industry will frequently result in those situations. It is necessary to provide risk management in all areas of operations in supervised institutions. FBA will prepare a special decision on that.

Principle 14: Banking supervisors must determine that banks have in place internal controls that are adequate for the nature and scale of their business. These should include clear arrangements for delegating authority and responsibility; separation of the functions that involve committing the bank, paying away its funds, and accounting for its assets and liabilities; reconciliation of these processes; safeguarding its assets; and appropriate independent internal or external audit and compliance functions to test adherence to these controls as well as applicable laws and regulations.

Implementation: Internal control and audit functions in all banks, but it is very often under the influence of bank management. By the Law, FBA has passed the Decision on Minimum Standards for Internal Control in Banks and Decision on Minimum Standards for Internal and External Audit in Banks. The FBA will monitor implementation of these decisions and apply appropriate corrective actions.

Principle 15: Banking supervisors must determine that banks have adequate policies, practices and procedures in place, including strict "know-your-customer" rules, that promote high ethical and professional standards in the financial sector and prevent the bank being used, intentionally or unintentionally, by criminal elements.

Implementation: FBA has passed the Decision on Minimum Standards for Banks' Activities on Prevention of Money Laundering and Terrorism Financing. Basically, that is the rule "know-your-customer". Banks have started implementation of this decision, and examiners of the FBA need additional training and new knowledge for detecting financial crime. Although the FBA cooperated with other institutions and provided some help in implementation of actions against money laundering and other criminal activities in banks, due to slow and weak court procedures, those efforts gave partial results. All the more so until recently "money laundering" was not even a criminal act. Law should be amended and examiners should receive additional training.

Methods of Continued Bank Supervision

Principle 16: An effective banking supervisory system should consist of some from of both on-site and off-site supervision.

Implementation: There are both types of supervision (on-site and off-site) and their activities are coordinated. FBA developed procedures for assessment of risk in banks. The procedures are fully complied with this principle.

Principle 17: Banking supervisors must have regular contact with bank management and a thorough understanding of the institutions' operations..

Implementation: FBA maintains contact with banks, but there is no program of regular meetings with banks. The institution of Bankers' Association would provide more efficient and better communication. Unfortunately, the FBA inherited too many duties from past, therefore in previous period it was preoccupied with implementation of provisional administrations, monitoring implementation of ordered actions, liquidation procedures etc. Decreased number of banks, that is, "elimination" of problem banks from the system opened possibilities for better application of this principle.

Principle 18: Banking supervisors must have a means of collecting, reviewing and analyzing prudential reports and statistical returns from banks on a solo and consolidated basis.

Implementation: Information gathered by the FBA are sufficient and complete, except in the area of review of consolidated balance sheets. This issue will be resolved in the first six months of 2003.

Principle 19: Banking supervisors must have a means of independent validation of supervisory information either through on-site examinations or use of external auditors.

Implementation: FBA can examine banks completely and that represents major part of its activities. It is necessary to continue promoting international accounting and audit standards in order to eliminate discrepancies and inaccuracies in banks' reports. External audit firms should implement them as well.

Principle 20: An essential element of banking supervision is the ability of supervisors to supervise the banking group on a consolidated basis.

Implementation: Since this issue is raised in our banking system, it is necessary to pass certain regulations in order to implement this principle adequately.

Necessary Information

Principle 21: Banking supervisors must be satisfied that each bank maintains adequate records drawn up in accordance with consistent accounting policies and practices that enable the supervisor to obtain a true and fair view of the financial condition of the bank and the profitability of its business, and that the bank published on a regular basis financial statements that fairly reflect its condition.

Implementation: The Law on Changes and Additions to the Law on Banks extended banks' duties to publish shortened version of the report of external audit of annual financial statements in media. Also, it is obligatory for banks to publish unaudited semi annual report including balance sheets (and Off-Balance Sheet), income statement, statement of cash flow and names of supervisory board members, management and shareholders (with over 5% of voting shares). This significantly improved transparency of banking industry and that will result in strengthening of financial discipline and further strengthening of confidence in banks.

Official supervisory authorities

Principle 22: Banking supervisors must have at their disposal adequate supervisory measures to bring about timely corrective action when banks fail to meet prudential requirements (such as minimum capital adequacy ratios), when there are regulatory violations, or where depositors are threatened in any other way. In extreme circumstances, this should include the ability to revoke the banking license or recommend its revocation.

Implementation: The Law provides necessary authorities to the FBA. The focus should be on a proactive approach that would anticipate crisis situations that, as we could see from foreign experience, can not be fully avoided, regardless of the frequency and quality of supervision.

Cross-border Banking

Principle 23: Banking supervisors must practice global consolidated supervision over their internationally active banking organizations, adequately monitoring and applying appropriate prudential norms to all aspects of the business conducted by these banking organizations worldwide, primarily at their foreign branches, joint ventures and subsidiaries.

Principle 24: A key component of consolidated supervision is establishing contact and information exchange with the various other supervisors involved, primarily host country supervisory authorities.

Principle 25: Banking supervisors must require the local operations of foreign banks to be conducted to the same high standards as are required of domestic institutions and must have powers to share information needed by the home country supervisors of those banks for the purpose of carrying out consolidated supervision.

Implementation: Federation BiH does not have actual banking institutions that are "internationally active", but in future period we can expect expansion of some banks to neighboring markets. Until now, these principles are not applicable to our country. We have undertaken activities for implementation of the principles by signing a memorandum of cooperation with the Bank of Slovenia and by preparing similar documents to be signed with authorized supervisory institutions from Austria and Croatia.

Exchange of information has been agreed with the Bank of Slovenia, and similar arrangements should be established with Austria and Croatia. In the Federation BiH there are banks from Malaysia, Turkey, Italy, and Arab countries and we should prepare official agreements on exchange of information with supervisors of those countries.

III OPERATIONAL PERFORMANCE OF BANKS IN THE FEDERATION OF BiH

As of 12/31/02, there were 29 banks in the FBiH holding banking licenses issued by the FBA. All banks have been performing banking operations and had a duty to report to the FBA, except Hercegovacka Bank dd Mostar, and information related to operations of that bank was not included to this information. The FBA reviewed reports (off-site review) and performed on-site examinations as regulated by law.

1. STRUCTURE OF THE BANKING SECTOR

1.1. Licenses for inception and establishment of bank operations and other approvals

In 2002, the FBA revoked five banking licenses from the following banks: Depozitna Bank dd Sarajevo, which merged to Vakufska bank d.d. Sarajevo, Šeh in Bank dd Zenica which merged to ABS Bank d.d. Sarajevo, Mostarska Bank d.d. Mostar due to merger with Gospodarska Bank Mostar, International Commerce Bank p.l.c. Sarajevo that was under liquidation procedure as requested by the Bank Assembly and Travnicka Bank dd Travnik due to status change (merger to Central Profit Bank dd Sarajevo). In the same period, the FBA issued one license for inception and operation of HVB Bank BiH d.d. Sarajevo.

At the end of 2002, FBiH banks had 7 organizational units in the Republika Srpska and 6 RS banks opened their organizational units in the FBiH.

As of 12/31/02, three banks were under provisional administration:

- Gospodarska Bank dd Mostar
- Hercegovačka Bank dd Mostar and
- UNA Bank dd Bihać.

Aside from Hercegovacka Bank dd Mostar (Provisional administration was initiated by the decision of the High Representative in BiH), the reason for initiation of Provisional Administration in other banks was failure to meet operating conditions required by law.

The license for internal payment operations was given to 28 banks as of 12/31/02, which is related to inter-bank transactions. In comparison to the end of 2001, the license for inter-bank transactions were approved to HVB Bank BiH dd Sarajevo. Applications for license for internal payment system operations are still accepted by the FBA.

1.2. Ownership Structure

As of 12/31/02, ownership structure in banks[1] was evaluated upon available information and bank examinations[2] and is was as follows:

Private and majority privately owned 25 banks (79.3%)

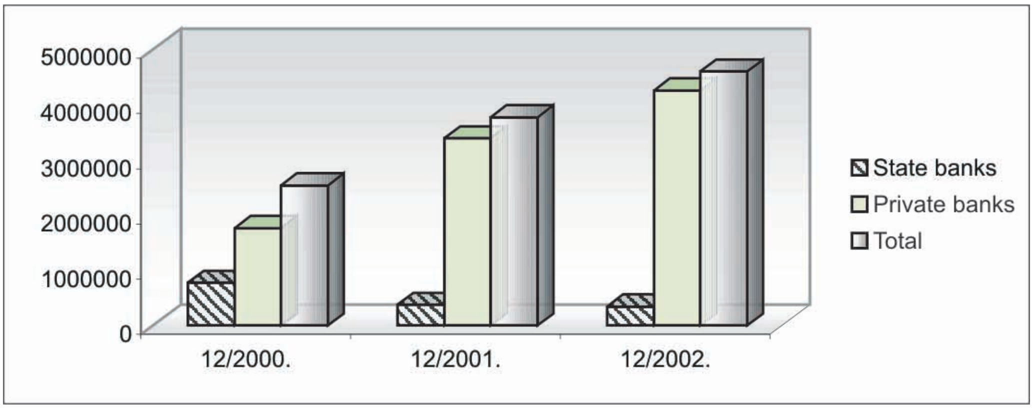
State and majority state owned 6 banks (20.7%).

Ownership structure can be observed from aspect of financial results, which is by the value of total capital[3].

Schedule 1: Ownership Structure by Total Capital ***-In 000 KM-***

BANKS	12/31/00		12/31/01[4]		12/31/02		RATIO	
							3/2	4/3
1	2		3		4		5	6
State banks	240,139	48%	90,800	18%	88,834	14%	38	97
Private banks	255,135	52%	413,691	82%	542,664	86%	162	131
TOTAL	495,274	100%	504,491	100%	628,498	100%	102	122

Graph 1: Ownership Structure (total capital)



More detailed picture on ownership structure[5] of banks in the Federation of BiH can be viewed by analysis of participation of state, private and foreign capital in shareholders; capital in banks.

Schedule 2: Ownership structure by participation of state, private and foreign capital -In 000 KM-

SHARE CAPITAL	12/31/00		12/31/01		12/31/02		RATIO	
	Amount	Participa-tion %	Amount	Participa-tion %	Amount	Participa-tion %	5/3	7/5
1	3	4	5	6	7	8	9	10
State capital	220,847	42.9	65,862	14.4	64,875	12.7	30	105
Private capital (residents)	159,325	30.9	102,943	22.4	110,605	20.5	65	107
Foreign capital (non-residents)	135,201	26.2	289,951	63.2	360,758	66.8	215	124
TOTAL	515,373	100.0	458,756	100.0	540,238	100.0	89	118

1 Criteria for classification of banks by type of ownership refers to shareholders capital in banks.

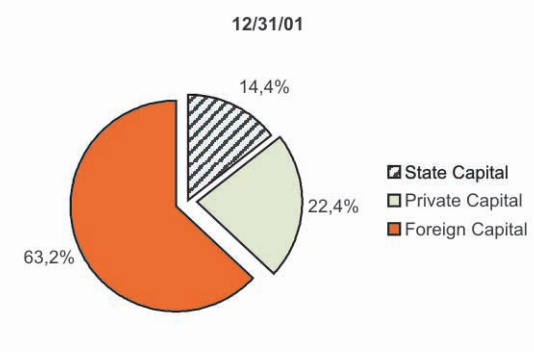
2 General overview of ownership structure in banks in the F BiH as of 12/31/02 resulted from received reports, and registration at authorized courts (changes in capital and shareholders structure).

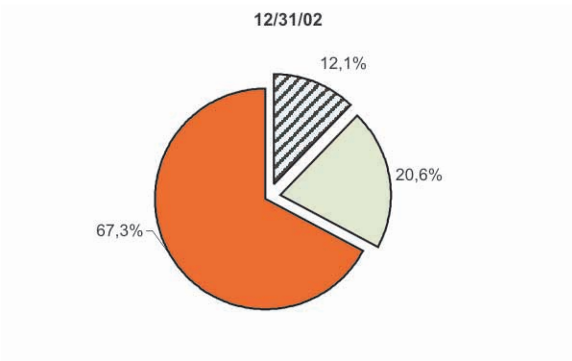
3 Information from Balance sheet - FBA schedule.

4 All schedules contain information as of 12/31/01 were included after audit of financial reports (after external audit).

5 Ownership structure - shareholders' capital (excluding capital related to apartments) as reported by banks.

Graph 2: Ownership Structure (shareholders' capital)





Analysis of ownership structure in banks, from the aspect of shareholders' capital, shows in the best way changes and trends that occurred in the banking system in the Federation of BiH and it is visible in two segments: privatization of existing state capital in mainly privately owned banks and further inflow of foreign capital (mainly from foreign banks).

Participation of state capital in the total shareholders' capital in banks as of 12/31/02 is lower by 1.7% in comparison to 12/31/01. This resulted from increase of (absolute amount and in percentage) of foreign capital. As of 12/31/02, participation of remaining, state owned capital in privately owned banks was only 1% or KM 6.4 million.

Major changes in the ownership structure in 2002 were related to participation of private (national) and foreign capital.

In comparison to 12/31/01, participation of privately owned capital (residents) in total capital for whole banking sector was decreased from 22.4% to 20.5%, while at the same time, participation of foreign capital increased from 63.2% to 66.8%. These changes relate mainly to privately owned banks, and it resulted from two components: foreign capital coming into the system through purchase of shares (trading with shares) from earlier owners (residents - institutions and citizens), and additional capitalization of 2 banks owned by foreigners.

Progress made in reform efforts and stabilization of banking system led to a larger inflow of foreign capital, mainly from foreign banks. Positive trend of increase of foreign capital investments in banks in the Federation will probably continue in the future period.

1.3. Staff

There is a total of 5,101 employees as of 12/31/02 in banks in the Federation BiH. Out of this total number, 11% worked in banks with predominantly state capital and 89% in privately owned banks.

Schedule 3: Staff in banks in the F BiH

BANKS	NUMBER OF EMPLOYEES			RATIO	
	12/31/00	12/31/01	12/31/02	3:2	4:3
1	2	3	4	5	6
State banks	1,253	554	558	44	101
Private banks	3,036	4,056	4,543	134	112
TOTAL	4,289	4,610	5,101	107	111
Number of banks	37	32	28		

In comparison to 12/31/01, number of employees increased by 11% or 491 persons mainly in privately owned banks.

Increased number of employees in banks was caused by new operations, that is, extended scope of operations, expansion of network of operational units of banks and inception of one new bank.

Schedule 4: Educational structure of staff

EDUCATION	NUMBER OF EMPLOYEES			RATIO	
	12/31/00	12/31/01	12/31/02	3:2	4:3
1	2	3	4	5	6
University degree	1,334	1,434	1,683	107	117
Two-year post secondary school degree	405	467	533	115	114
High school degree	2,331	2,483	2,665	107	107
Other	219	226	220	103	97
TOTAL	4,289	4,610	5,101	107	111

In the observed period, the major ratio growth of 17% was recorded in the group of staff with university degree, while number of staff with a two-year post secondary school degree increased by 14%.

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

Schedule 5: Assets/employees

BANKS	12/31/00			12/31/01			12/31/02		
	Number of staff	Assets (000 KM)	Assets/ employee	Number of staff	Assets (000 KM)	Assets/ employee	Number of staff	Assets (000 KM)	Assets/ employee
State	1,253	772,559	616	554	378,256	684	558	345,592	619
Private	3,036	1,766,760	582	4,056	3,390,231	836	4,543	4,250,496	936
TOTAL	4,289	2,539,319	592	4,610	3,768,487	818	5,101	4,596,088	901

At the end of 2002, for each employee there were KM 901,000 in assets for the whole banking system, which is better in comparison to the end of 2001. The ratio in state banks was worse in comparison to ratio for privately owned banks, or banking system in whole.

Analytical indicators for banks individually were between KM 280,000 up to KM 1,989,000 of assets per an employee. 12 banks had assets per an employee under KM 500,000 which implies that they have excess number of staff in comparison to assets. That results in larger operational costs and has negative impact to profitability in those banks. On the other hand, the same ratio in 11 banks was over 1 million KM.

2. FINANCIAL INDICATORS OF BANKS' OPERATIONS

Bank examination through analysis of banks' reports is performed through a review of reports regulated by the Agency and reports of other institutions. Those reports represent database of three groups of information:

Balance sheet information for all banks (by IMF and FBA format) submitted monthly, including quarterly attachments to balance sheet by the FBA format containing more detailed information on cash funds, loans, deposits and off balance sheet items.

Information on solvency of banks, information on capital and capital adequacy, assets classification, risk concentrations, liquidity, exposure to foreign currency risk, all based on the reports regulated by the FBA (quarterly) and Information on operational results of banks (income statement - FBA format) and statement of cash flows, submitted to FBA quarterly.

Aside from above listed standardized reports, data base includes information from additional report requirements of the FBA from banks in order to have the best conditions for monitoring banks' operations in the Federation of BiH. Also, database includes reports on audit prepared by independent auditor, and all other information relevant for evaluation of operational results of every bank individually and banking system in whole.

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

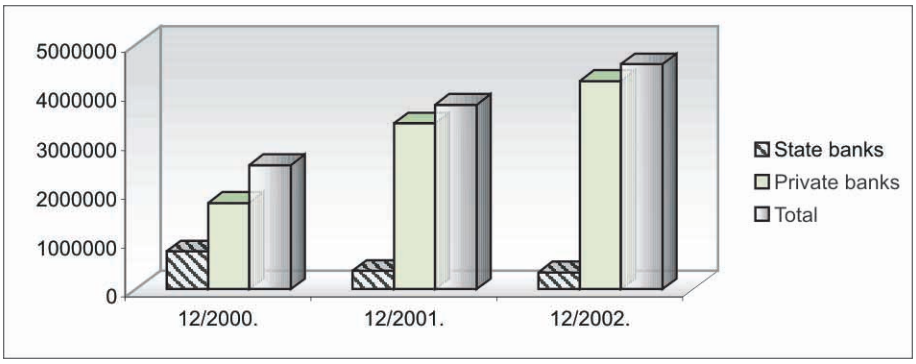
2.1. Balance Sheet

Based on the balance sheets submitted by banks as of 12/31/02, total balance sheet for the Federation of BiH was KM 4.6 billion, which is more by 22% or KM 828 million in comparison to 12/31/01.

Schedule 6: Balance Sheet

DESCRIPTION	AMOUNT (in 000 KM)			RATIO	
	12/31/00	12/31/01	12/31/02	3/2	4/3
1	2	3	4	5	6
ASSETS:					
Cash funds	1,025,813	1,783,234	1,595,153	174	90
Securities	4,352	51,436	73,150	1.182	142
Placements in other banks	20,311	25,355	19,952	125	76
Loans – net	1,142,650	1,572,159	2,503,585	138	159
Premises and other fixed assets	283,436	273,981	299,250	97	110
Other assets	62,757	62,322	104,998	99	165
TOTAL ASSETS	**2,539,319**	**3,768,487**	**4,596,088**	**148**	**122**
LIABILITIES:					
PAYABLES					
Deposits	1,763,000	2,900,613	3,528,209	165	122
Borrowings from other banks	6,761	5,550	3,352	82	60
Loan payables	188,448	253,269	313,010	134	124
Other liabilities	85,836	104,564	123,019	122	118
CAPITAL					
Capital	495,274	504,491	628,498	102	125
TOTAL LIABILITIES (PAYABLES AND CAPITAL)	**2.539,319**	**3,768,487**	**4,596,088**	**148**	**122**

Graph 3: Banks' Assets by Ownership Structure:



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

In comparison to 2001 when banks accomplished large growth ratio of balance sheet of 48% (the most significant factors were: improvement of the banking sector in whole, introduction of deposit insurance system, transfer of internal payments to banks, and conversion of other currencies to Euro at the year end) it is possible to conclude that in 2002 banks achieved moderate growth ratio. But, these achievements relate only to privately owned banks (growth of 25% or KM 860 million) while in state owned banks (as part of sector had assets reduced by 9% or KM 33 millions at the end of 2002.

Although ratio for balance sheet for the whole system continued with growth, analysis of individual data in banks displayed that assets in eight banks (four state and four privately owned banks) was less assets in comparison to previous year, year 2001. At the same time, assets growth ratio in ten banks (all private) increased by over 20% (in three banks this resulted from merging). We should emphasize that out of total growth of balance sheet assets in 2002, about 67% of the KM 552 million is with three largest banks in the system.

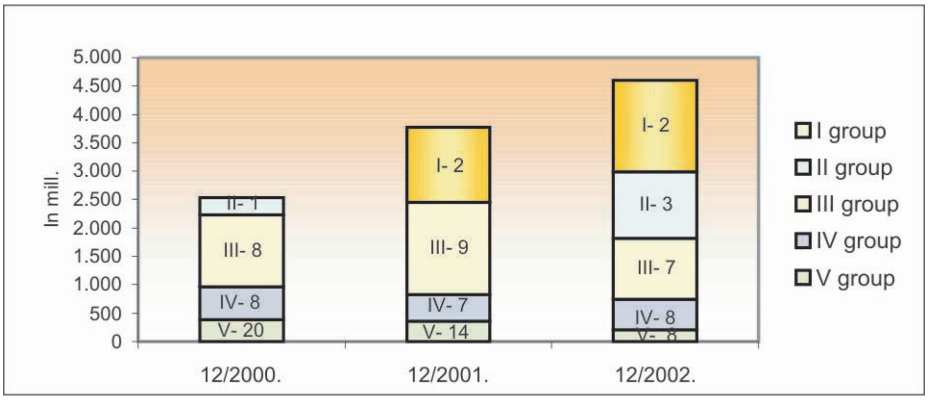
If we analyze banking system from the aspect of assets size and particular groups within this frame, it is possible to make conclusion that banks from first three groups, (with assets of over KM 100 million) still have increasing trend. On the other hand, 16 banks had assets under KM 100 million, and total number of those banks is continuously decreasing, as well as total assets in those banks, and relatively - participation of their assets in total assets for the whole banking system. This can be considered as positive trend in the growing and developing process of the banking sector.

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

Schedule 7: Participation of particular groups of banks in total assets in periods

AMOUNT OF ASSETS	12/31/00			12/31/01			12/31/02		
	Amount	Particip. %	Number of banks	Amount	Particip. %	Number of banks	Amount	Particip. %	Number of banks
Over 500	-	-	-	1,315	34.9	2	1,606	34.9	2
300 to 500	309	0.1	1	-	-	-	1,171	25.5	3
100 to 300	1,272	50.2	8	1,632	43.3	9	1,072	23.3	7
50 to 100	576	22.7	8	460	12.2	7	543	11.8	8
Less then 50	382	15.0	20	362	9.6	14	204	4.5	8
TOTAL	2,539	100.0	37	3,769	100.0	32	4,596	100.0	28

Graph 4: Participation of particular groups of banks in total assets in timeline



The evidence that growth of assets is concentrated with small group of banks is data that participation of 12 largest banks in total assets of the banking system was approximately 84% or KM 3,849 million at the end of 2002 (at the end of 2001 it was 78.2% or KM 2,947 million). The significant progress was made in the last group (banks with assets under KM 50 million). In that group number of banks was decre-

7 Banks are divided into five groups, by size of assets.

ased (at the end of 2001 there were 14 banks and at the end of 2002 it was 8) and participation of their assets (from 9.6% to 4.5%). This mainly resulted from reconstruction of banking sector in 2002 accomplished by status changes (merging in four banks) and liquidation process in one bank. The process of further reduction of banks with assets under KM 50 million will continue in 2003 as this group contains four state banks (two under provisional administration) and one bank completed merging process to the bank from fourth group in February 2003.

The growth of balance sheet mainly resulted from growth of deposits (by 22% or KM 628 million) and capital (by 25% or KM 124 million).

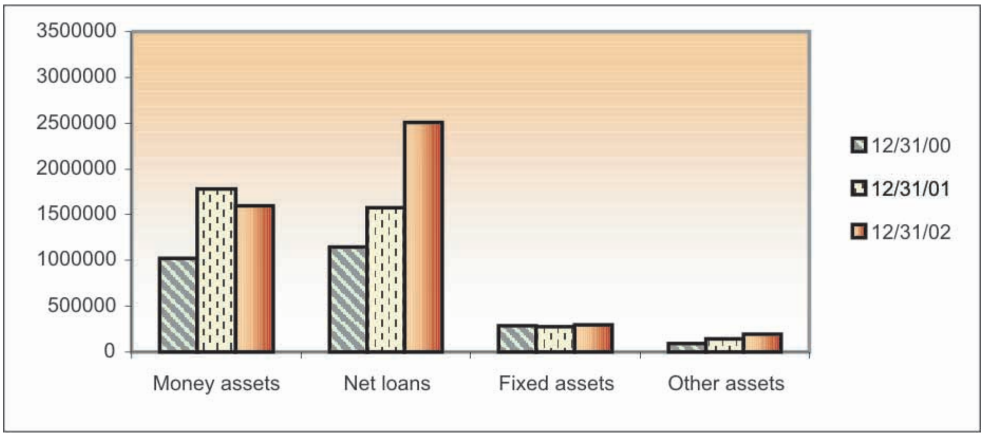
On the other hand, within assets (property) of banks, the major growth was recorded with loans[8] of 56% or KM 967 million, while money assets decreased by 11% or KM 188 million.

Following schedule and graphs display comparable schedule of essential balance sheet positions in assets and liabilities in balance sheet of banks:

Schedule 8: Balance sheet structure ***- In % -***

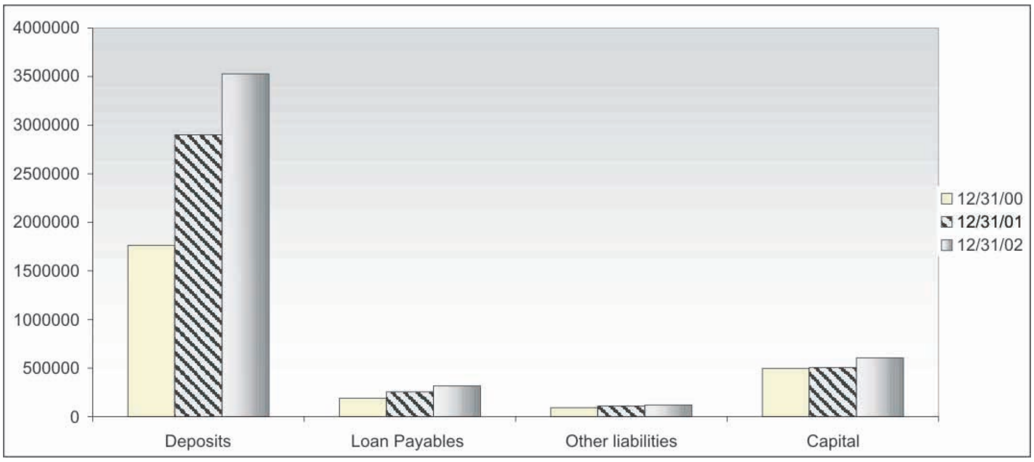
DESCRIPTION	PARTICIPATION		
	12/31/00	**12/31/01**	**12/31/02**
ASSETS:			
Money assets	40.4	47.3	34.7
Securities	0.2	1.4	1.6
Placements in other banks	0.8	0.7	0.4
Loans – net	45.0	41.7	54.5
Premises and other fixed assets	11.2	7.2	6.5
Other assets	2.4	1.7	2.3
TOTAL ASSETS	100.0	100.0	100.0
LIABILITIES:			
PAYABLES			
Deposits	69.4	77.0	76.8
Loans from other banks	0.3	0.2	0.1
Loan Payables	7.4	6.7	6.8
Other liabilities	3.4	2.7	2.6
CAPITAL			
Capital	19.5	13.4	13.7
TOTAL LIABILITIES (PAYABLES AND CAPITAL)	100.0	100.0	100.0

Graph 5: Assets Structure in Balance Sheet in Banks



8 Gross loans (information from balance sheet).

Graph 6: Liabilities Structure in Balance Sheet in Banks



The liabilities structure in banks did not change significantly and deposit total, with participation of 76.8%, is still predominant in the financial potential of banks.

The most significant change of assets structure in banks is with participation of loans that increased by approximately 13%, so as of 12/31/02 net loans were 54% of assets in banks. At the same time, participation of money assets was decreased by same percentage (from 47% to 35%). This change in the assets structure in banks is good from the aspect of profitability, because assets are placed in order to earn interest income. But further growth of risk assets, primarily loans will result in increased credit risk and it should be followed by appropriate growth of capital. Also in that situation management in banks have to establish efficient systems for identifying, measuring, controlling and monitoring of all risks that bank, during its performance, is exposed to.

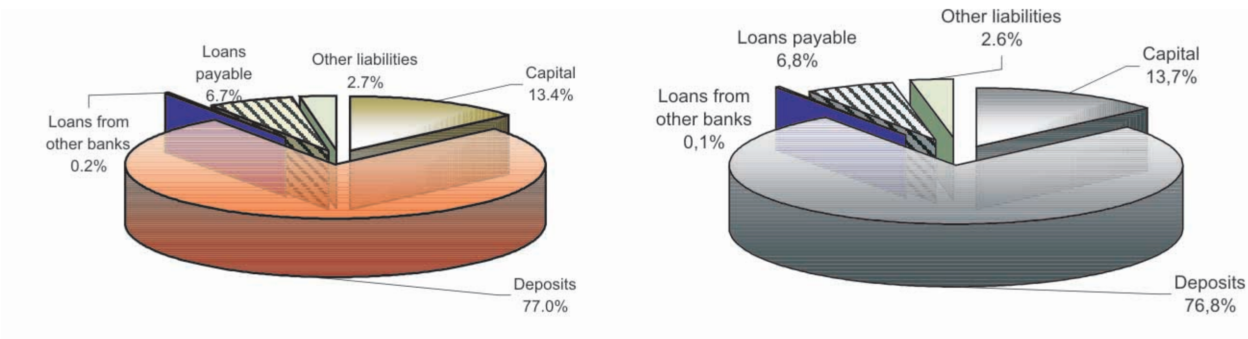
Banks in the Federation of BiH still had significant amount of money assets deposited at depository institutions abroad. At the end of 2002, those deposits were 64% or KM 1.0 billion out of total cash items. In comparison to the end of 2001, the growth of this participation is by 20%. Participation of assets deposited at the reserve account at Central Bank of BiH and in vaults of banks decreased in comparison to the last year (from 36% to 23%, 20% to 13% respectively), which is in direct connection with the increase of credit placements in 2002.

2.1.1. Liabilities (Payables and Capital)

Structure of payables and capital in balance sheet of banks as of 12/31/02 can be overviewed from the following graph:

Graph 7: Structure of liabilities in banks:

12/31/2001 *12/31/2002*



Liabilities structure was not significantly changed; therefore, major participation of 76.8% is still with deposits as primary source of funding.

In 2002, deposits increased by 22% or KM 628 million only in privately owned banks (by 25% or KM 655 million), while in state banks deposits were reduced by 11% or KM 27 million in comparison to the end of 2001. That reflected to participation of those sectors in total deposits, so at the end of 2002 94% of total deposits were with private banks (this was 91% at the end of 2001) and with state banks only 6% (in 2001 it was 9%). Participation of deposits in liabilities in privately owned banks was 78% and in state banks 65%.

The trend of concentration of deposits in banks, which are at the same time banks with largest assets, is continued, so as of 12/31/02 only five largest banks had held 67% of total deposits or KM 2,374 million. Also, the indicator of deposits concentration is fact that 85% of total deposits is placed in only ten banks.

Positive trend of deposit structure maturity adjustment is continued in 2002 as well, although not satisfactory yet. In comparison to the end of 2001, participation of long-term deposits increased by nine percent (from 15% to 24%), and at the same time, participation of short-term deposits decreased. It is possible to overview the situation in the following schedule:

Schedule 9: Maturity adjustment of deposits ***- in 000 KM -***

DEPOSITS	12/31/00		12/31/01		12/31/02	
	Amount	Participation %	Amount	Participation %	Amount	Participation %
Savings and demand deposits	1,277,824	72.5	1,779,672	61.4	2,010,579	57.0
Up to 3 months	168,255	9.5	413,465	14.2	317,862	9.0
Up to 1 year	149,578	8.5	280,243	9.7	349,586	9.9
1. Total short-term	1,595,657	90.5	2,473,380	85.3	2,678,027	75.9
Up to 3 years	113,605	6.4	242,924	8.4	416,323	11.8
Over 3 years	53,738	3.1	184,309	6.3	433,859	12.3
2. Total long-term	167,343	9.5	427,233	14.7	850,182	24.1
TOTAL (1 + 2)	1,763,000	100.00	2,900,613	100.0	3,528,209	100.0

Maintaining adequate maturity adjustment between sources and placements is one of the most significant segments in risk management, that is, exposure of banks to liquidity risk. Any disorder in maturity adjustments represents danger for future liquidity position, and finally, it can endanger financial condition of the bank and question its further solvency and operations.

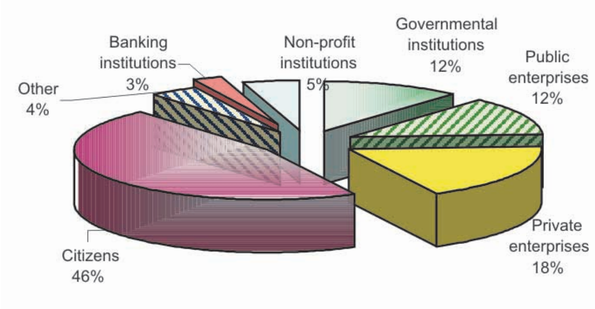
Schedule 10: Structure of deposits by depositors[9] ***- u 000 KM-***

DEPOSITORS	12/31/00		12/31/01		12/31/02	
	Amount	Participation %	Amount	Participation %	Amount	Participation %
Governmental institutions	168,194	9.5	339,364	11.7	440,383	12.5
Public enterprises	370,562	21.0	359,390	12.4	388,271	11.0
Private enterprises and assoc.	374,834	21.3	536,324	18.5	661,292	18.7
Non-profit. Organizations	164,748	9.3	132,452	4.6	135,849	3.9
Banking institutions	32,225	1.8	77,272	2.7	296,217	8.4
Citizens	482,340	27.4	1,334,337	46.0	1,482,313	42.0
Other	170,017	9.7	121,474	4.1	123,884	3.5
TOTAL	1,763,000	100.0	2,900,613	100.0	3,528,209	100.0

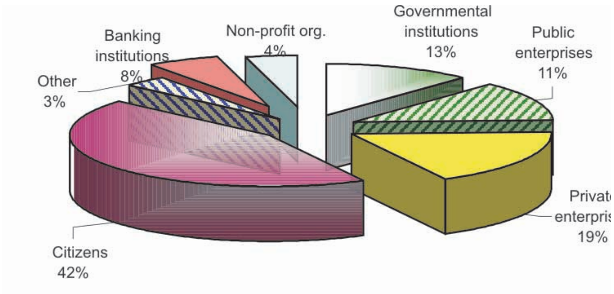
9 Information from the form BS-D submitted by banks each quarter with Balance Sheet - FBA schedule.

Graph 8: Structure of deposits by depositors

12/31/01



12/31/02



If we make analysis and deposits participation by sectors, it is possible to conclude that all sectors recorded deposit growth in 2002, the majority of growth (absolute amount and relative ratio) relates to growth of banking institutions almost completely associated with three banks mainly owned by foreign investors. Out of total deposits growth of approximately KM 628 million in 2002, deposits of banking institutions increased by approximately KM 219 million, which resulted from support of founder-shareholders (foreign banks) in order to provide for additional source of funding mainly for citizens and private enterprises sections. It is very significant that growth was with long-term deposits (over three years), which is used by banks to mitigate maturity inadjustment between assets and liabilities.

In comparison to the end of 2001, the most significant change was with the sector structure of deposits - increased participation of banking institutions from three percent to eight percent and reduction of citizens' participation by four percent.

Although participation of citizens section in total deposits was decreased by four percent, savings still have increasing trend, so growth ratio amounted to 10 percent or KM 125 million in 2002. Observed in sector structure, savings were decreased by 24% or KM seven million in state banks, while in privately owned banks growth was by 10% or KM 132 million.

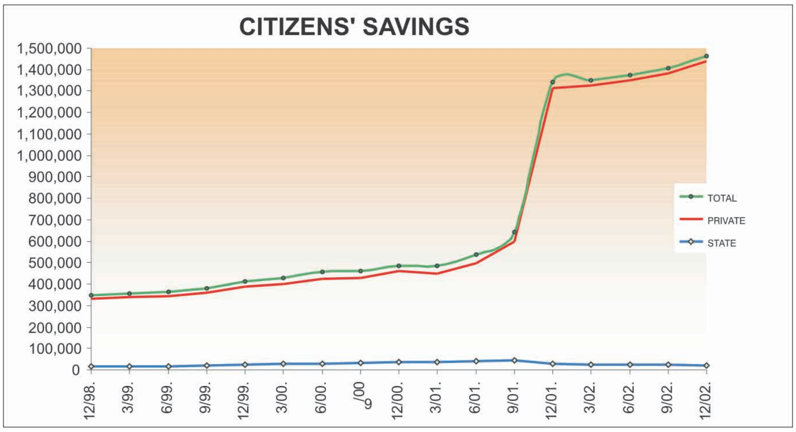
As in other sectors, it is necessary to stress that there is large concentration of savings in few banks, since 61% of total savings are placed in three largest banks in the Federation of BiH (as of 12/31/01 this amount was 45%), that is, 86% of total savings is placed in eight private banks.

Schedule 11: New citizens' savings in time line

BANKS	AMOUNT (IN 000 KM)			RATIO	
	12/31/00	12/31/01	12/31/02	3/2	4/3
1	2	3	4	5	6
State	34,841	28,787	22,072	83	76
Private	427,166	1,285,803	1,417,847	301	110
TOTAL	462,007	1,314,590	1,439,919	285	110

The growth of savings in banks in the Federation of BiH resulted from the activities implemented by the FBA and implementation of deposit insurance system starting from January 2001 when Deposit Insurance Agency in the F BiH started its operations, and in August 2002 the Law on Deposit Insurance in Banks in BiH set up foundation of Deposit Insurance Agency in Bosnia and Herzegovina. Until the end of 2002, 10 banks in the Federation of BiH took part in the deposit insurance program and were given certificates. Analytical data on size of deposits showed growth in those banks. The participation of those deposits in total deposits was 68% as of 12/31702 and same data for savings was 76%. Deposits' safety is a guaranty and motive for further growth of savings in those banks, but in all other banks in the system.

Graph 9: New citizens' savings in time line



2.1.2. Assets and Asset Quality

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

Gross assets[10] in the balance sheet in banks in the Federation of BiH as of 12/31/02 was KM 4,803 million, which is higher by 22% or KM 857 million in comparison to end of 2001, while off-balance sheet risk items were KM 673 million and they increased by 36% or KM 178 million.

Total assets, including off-balance sheet items (assets)[11], were 5.5 billion of KM and they increased by 23% in comparison to the year 2001.

Schedule 12: Assets, off-balance sheet items and potential loan losses in active balance sheet *In 000 KM*

DESCRIPTION	AMOUNT (in 000 KM)						RATIO	
	12/31/00	Structure %	12/31/01	Structure %	12/31/02	Structure %	4:2	6:4
1.	2.	3.	4.	5.	6	7	8	9
Loans	1,128,493	41.4	1,526,178	38.7	2,525,337	52.6	135	165
Interest	17,644	0.6	17,646	0.4	25,697	0.6	100	146
Past due receivables	168,567	6.2	189,630	4.8	158,084	3.3	113	84
Receivables on paid guarantees	10,913	0.4	7,853	0.2	7,110	0.1	72	91
Other placements	29,151	1.1	28,083	0.7	70,300	1.4	96	250
Other assets	1,372,554	50.3	2,177,185	55.2	2,016,606	42.0	159	93
TOTAL ASSETS	2,727,322	100.0	3,946,575	100.0	4,803,107	100.0	145	122
OFF BALANCE SHEET	435,095		495,029		673,498		106	139
BALANCE SHEET AND OFF BALANCE SHEET	3,162,417		4,441,604		5,476,605		140	123
General credit risk and Potential loan losses	212,669		201,778		228,385		95	113
Allocated general and special reserves for loan losses	201,198		198,234		224,987		99	113

10 Information from the report on Assets Classification in balance and off-balance sheet.

11 Assets, as defined in the Article 2 of the decision on Minimum Standards for Managing Credit Risk and Assets Classification in banks

The most significant change in assets in banks occurred in 2002 that indicated increase of banks' exposure to credit and liquidity risk. Loans[12] had significant growth ratio of 56% or KM 967 million. At the same time, money assets decreased by 11% or KM 188 million. This resulted in changed structure of assets, that is increase of loan participation from 46% to 59% at the end of 2002, while participation of money assets decreased from 47% to 35%.

Analytical data provided by banks displayed that this sector recorded the same trends as in other operational areas of banks. The major growth of loans from 62% to 136% was with three largest banks in the system, and 11 banks increased their placements by over 50% in 2002. Negative growth ratio, that is, decreased loan activity was recorded in six banks, and those were mainly banks from group of small banks (assets under KM 50 million).

Analysis of the sector structure of loans showed that major growth was with loans approved to citizens that increased by 102% or KM 637 million in 2002, therefore almost half of total loans (47%) was approved to citizens and 40% was approved to private enterprises in 2002. Citizens loans in three largest banks participated in total loans with approximately 57% that is even higher for the whole banking sector. In those banks and in few other large banks it is obvious that they are implementing strategy of increased loans to citizens and that is related to opinion that those loans bear less risk if they are supported with adequate loan policy regulating a good quality collateral.

Schedule 13: Structure of loans by sectors

SECTORS	12/31/00		12/31/01		12/31/02		RATIO	
	Amount	Participation %	Amount	Participation %	Amount	Participation %	4/2	6/4
1	2	3	4	5	6	7	8	9
Governmental institutions	20,428	1.5	26,033	1.5	30,368	1.2	127	117
Public enterprises	285,448	21.8	246,437	14.3	248,852	9.2	87	101
Private enterprises and assoc.	568,773	43.5	770,703	44.7	1,078,651	40.1	135	140
Non-profit. Organizations	4,995	0.4	6,370	0.4	2,834	0.1	128	44
Banking institutions	62,592	4.8	42,480	2.5	46,439	1.7	68	109
Citizens	362,370	27.7	623,219	36.2	1,259,816	46.8	172	202
Other	3,652	0.3	8,422	0.4	23,571	0.9	230	280
TOTAL	1,308,258	100.0	1,723,663	100.0	2,690,531	100.0	132	156

Regarding maturity adjustments, we should emphasize that increase of long-term loans remained (70% out of total loans) and especially loans approved to citizens (as of 12/31/02, 92% of those loans were long-term), while 56% of total loans approved to private enterprises were long-term.

Schedule 14: Maturity Structure of Loans ***-In 000 KM-***

LOANS	12/31/00		12/31/01		12/31/02		RATIO	
	Amount	Participation %	Amount	Participation %	Amount	Participation %	4/2	6/4
1	2	3	4	5	6	7	8	9
Past due Receivables	179,714	13.7	197,633	11.4	158,084	6.2	110	80
Short-term Loans	440,568	33.7	459,617	26.7	650,570	24.8	104	142
Long-term Loans	687,976	52.6	1,066,560	61.9	1,904,767	69.0	155	179
TOTAL LOANS	1,308,258	100.0	1,723,663	100.0	2,690,531	100.0	132	156

Past due receivables reduced by 20% or KM 39.5 million and that partially resulted from collection and restructuring, and from the fact that those receivables were problem assets for longer period of time, hence banks had to record those as loss and record in off-balance sheet. In 2002, banks wrote off (removed from balance sheet and recorded in off-balance sheet) KM 79.8 million of receivables. Out of that, permanent write off was KM 13.6 million of loans approved to enterprises, especially in fourth quarter. At the same time, management in banks put effort to collect those receivables, therefore banks collected and recorded as income KM 22.4 million in 2002. At the end of 2002, total write off (potential assets of banks) was KM 266 million, and major participation of those receivables are under litigation for longer time.

12 Gross loans with past due receivables and receivable on guarantees paid.

Certain banks did not adjust maturity of financial assets and liabilities, that is, long-term loans were financed from short-term sources. This is the first warning sign that those banks could have liquidity problems in future, especially if they experience deterioration of assets quality. Therefore majority of banks now face the problem of providing long-term source of funds, including primary (deposits) and secondary (loans) source of funds and capital.

Since placements, that is, loans represent part of assets with highest risk in banks, the quality of loans indicates one of the most significant constituents for stability and success of banking operations. Therefore, the rating of assets quality is rating of credit placements in banks, that is, identification of potential loan losses and allocation of reserves for loan losses.

Assets quality of banks and off-balance sheet risk items as of 12/31/02 and potential loan losses by classification categories are presented in the following schedule:

Schedule 15: Classification of Assets and Off-Balance Sheet Risk Items in Active Balance Sheet -000 KM-

RECEIVABLES	CLASSIFICATION					
	A	B	C	D	E	TOTAL
Placements[13]	2,092,929	402,104	128,648	132,061	5,089	2,760,831
Interest	17,197	5,438	848	2,214	0	25,697
Total Placements	2,110,126	407,542	129,496	134,275	5,089	2,786,528
Other Assets	2,001,074	9,062	2,054	2,279	2,110	2,016,579
TOTAL ASSETS	4,111,200	416,604	131,550	136,554	7,199	4,803,107
OFF-BALANCE SHEET RISK ITEMS	599,689	66,736	3,725	2,843	505	673,498
BALANCE AND OFF-BALANCE RISK ITEMS	4,710,889	483,340	135,275	139,397	7,704	5,476,605
General credit risk and potential loan losses	60,296	42,537	35,977	81,871	7,704	228,385
Allocated general and special reserves for loan losses	60,461	42,750	36,114	83,047	2,615	224,987
Structure of allocated reserves by classification category	26.9	19.0	16.0	36.9	1.2	100.0

If we make analysis of assets quality with off-balance sheet items included, it is possible to notice that participation of non-performing assets (C to E) decreased from 5.9% to 5.2%, although it increased nominally by KM 19.6 million. The reduction is related to growth of balance sheet and off-balance sheet assets in 2002 by 23% or KM 1,035 million.

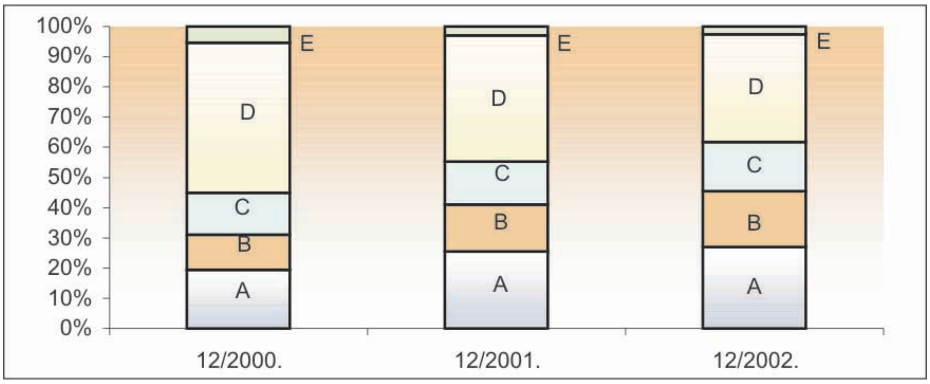
Level of general loan risk and potential loss by classification categories, determined upon criteria and methodology regulated by the FBA's decisions, their trends and structure for the whole banking sector are presented in the following schedule and graph:

Schedule 16: Structure and Trend of General Credit Risk and Potential Loan Losses

Classification	AMOUNT (in 000 KM) and STRUCTURE (in %)						RATIO	
	12/31/00		12/31/01		12/31/02		4/2	6/4
1	2	3	4	5	6	7	8	9
A	41,521	19.5	51,377	25.5	60,296	26.4	124	119
B	24,357	11.5	31,339	15.5	42,537	18.6	130	136
C	29,822	14.0	28,852	14.3	35,977	15.8	97	125
D	105,597	49.7	84,429	41.8	81,871	35.8	79	97
E	11,372	5.3	5,781	2.9	7,704	3.4	51	133
TOTAL	212,669	100.0	201,778	100.0	226,839	100.0	95	113

13 Placements include loans, past due receivables, receivables on paid guarantees and other placements.

Graph 10: Structure and Trend of General Credit Risk and Potential Loan Losses



General credit risk and potential loan losses in banks were KM 228 million at the end of 2002 (4.2% of total assets including off-balance sheet), which is higher by 13% in comparison to the end of 2001. The major changes in the structure of loan losses were with categories A, B and C, which increased, and participation of category D decreased from 42% to 36%. Individual analysis of assets quality, that is, loan portfolio, in banks and on-site examination in banks displayed that key risk in banks is with credit risk. There are still problem loans mainly approved earlier, mainly to legal entities (enterprises). The FBA set up corrective actions in those banks by which the banks have to prepare plan of activities for improvement of practices for managing credit risk, that is, assets quality. Also, they have to decrease existing concentrations, resolve problems related to non-performing assets and prevent any further deterioration of assets. FBA findings are performed according to the determined schedule.

Transactions with Related Entities

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

The FBA has set up, in accordance with Basle Principles, certain prudential principles and requirements regulating operations with related entities of the bank[14]. That is also regulated by the Decision on Minimum Standards for Bank Operations with Related Entities that regulated in detail modes and conditions operations with related entities. The Decision and the Law on Banks regulate the duty of the Supervisory Board of the Bank, which has to adopt, upon the proposal of the General Manager, special policies regulating operations with related entities and to monitor their implementation.

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

• shareholders with more than 5% of voting rights,

• members of the Supervisory Board and senior management in the bank and

• Subsidiaries and other enterprises related to the bank through capital.

But, information reported by banks to the FBA should be taken with certain skepticism, since true state of the mentioned transactions is possible to determine only by review of reporting data in the bank, that is, by on-site examination.

14 Article 39, item 2 of the Law on Changes and Additions to the Law on Banks defines term "entities related to the bank". Now it excludes staff of the bank.

Schedule 17: Transactions with Related Entities **-000 KM-**

Description	APPROVED LOANS 12/31/00	12/31/01	12/31/02
Shareholders with over then 5% of voting rights, Subsidiaries and other enterprises related through capital	70,677	46,071	59,241
Members of the Supervisory Board	1,164	48	315
Management and employees of the bank	4,537	3,580	2,699[15]
TOTAL	76,378	49,699	62,255
POTENTIAL AND ACCEPTED OFF-BALANCE SHEET LIABILITIES	21,243	4,906	6,684

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

2.1.3. Capital -Strength and Adequacy

Total capital[16] in banks in the Federation of BiH was KM 740,387,000 as of 12/31/02.

Schedule 18: Regulatory capital **-In 000 KM-**

DESCRIPTION	12/31/00		12/31/01		12/31/02		RATIO 3/2	RATIO 4/3
1	2		3		4		5	6
STATE BANKS								
a) Core Capital	238,314	95%	83,505	93%	101,783	96%	35	122
b) Additional Capital	12,613	5%	6,206	7%	3,925	4%	49	63
c) Total capital (a + b)	250,927	100%	89,711	100%	105,708	100%	36	118
PRIVATE BANKS								
a) Core Capital	317,290	85%	475,845	86%	536,203	84%	150	113
b) Additional Capital	54,669	15%	74,881	14%	98,476	16%	137	132
c) Total capital (a + b)	371,959	100%	550,726	100%	634,679	100%	148	115
Total								
a) Core Capital	555.604	89%	559,350	87%	637,986	86%	101	114
b) Additional Capital	67,282	11%	81,087	13%	102,401	14%	121	126
c) Total capital (a + b)	622,886	100%	640,437	100%	740,387	100%	103	116

Total capital[17] increased during 2002 by KM 100 million or 16% in comparison to 2001. The core capital was increased by KM 78.6 million, and additional capital by KM 21.3 million.

Within core capital, share capital paid in money increased by KM 84 million and share capital as investment of rights and properties is higher by KM 10 million.

The increase of share capital in 2002 was mainly influenced by banks compliance with the new minimum capital requirement (share capital in cash of KM 15 million) obligatory by the end of 2002. Also it resulted from additional capitalization in cash in few banks in order to cover loss from previous year. Eleven banks provided additional capital of approximately KM 109 million, out of that, foreign investors (shareholders of banks predominantly owned by foreign investors) provided for KM 105.1 million. Also, two banks provided reserves of KM 5.3 million. Share capital increased due to distribution of income after year-end statements for 2001 and inception of new bank with founders' capital of KM 15 million.

15 Excluding loans approved to employees of banks, as it is regulated in the changes to the Law on Banks.

16 Regulatory capital as defined by Article 8 and 9 in the Decision on Minimum Standards for Capital Management

17 Source of information is quarterly Report on Capital Position in Banks (Form 1-Table A) regulated by the Decision on Minimum Standards for Capital Management in Banks.

In 2002, seven banks covered losses from previous years of KM 83.7 million from share capital and reserves (11 banks had uncovered losses from previous years of total KM 93 million). Based on that, the reserves were decreased by KM 30 million. In addition, one bank performed coverage of losses made in 2002[18] of KM 4.1 million. Due to closing of one bank with accumulated losses from previous years of KM 1.1 million, the core capital was decreased by 10 million of KM.

At the same time, four banks increased core capital from the income gained in 2002 (confirmed by the external audit) in total amount of KM 17.7 million. Additional capital was increased by KM 21.3 million based on subordinated debt included from additional capital in two banks of approximately KM 16 million, and increase of general reserves (2% for performing assets) by KM 8.5 million[19]

Aside from significant additional capitalization and increased core capital, the structure of regulatory capital was changed in favor of additional capital.

Above-mentioned changes had positive effect to net capital that was increased by 29% or KM 156 million in 2002. Therefore as of 12/31/02 it totaled to KM 691 million (KM 607 million in private banks and KM 84 million in state banks).

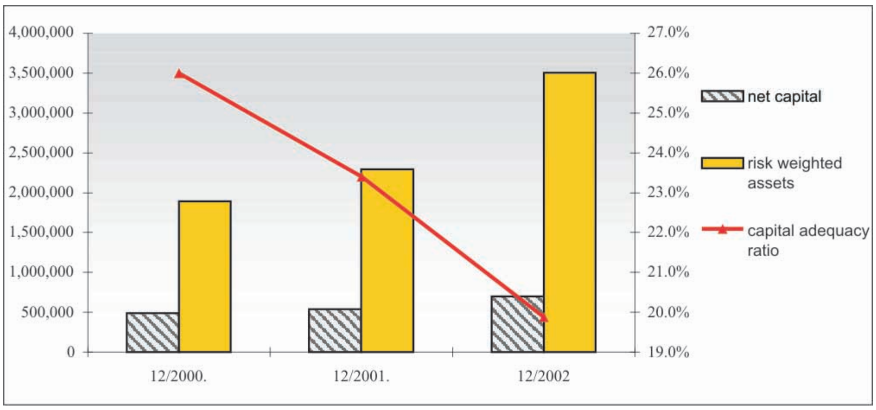
Ratio between capital and assets, that is capitalization rate in banks as of 12/31/02, was 15.4%, which is less by 0.8% in comparison to the end of 2001. Faster growth of assets than capital can be considered as negative trend in general overview of safety of bank operations and banking sector in whole. That suggests that banks should strengthen capital, especially those banks that experienced large growth of assets in previous period. According to its authority stated in the Law, the FBA will insist on further capitalization of banks.

Above presented findings are confirmed by capital adequacy ratio, calculated as ratio of net capital and risk weighted assets. For the whole banking sector it was 19.8%, which is less by 2.6% then as of 12/31/01. Substantial growth of credit activities resulted in increased risk and it was not followed by appropriate growth of net capital. Consequently this ratio recorded reduction in past two years.

Schedule 19: Net capital, Risk Weighted Assets and Capital Adequacy Ratio

DESCRIPTION	12/31/00	12/31/01	12/31/02	RATIO	
				3/2	4/3
1	2	3	4	5	6
NET CAPITAL	497,768	535,505	691,674	108	129
RISK WEIGHTED ASSETS AND CREDIT EQUIVALENTS	1,890,040	2,388,921	3,492,170	126	146
NET CAPITAL RATIO (CAPITAL ADEQUACY)	26.3%	22.4%	19.8%	85	88

Graph 11: Net capital, Risk Weighted Assets and Capital Adequacy Ratio

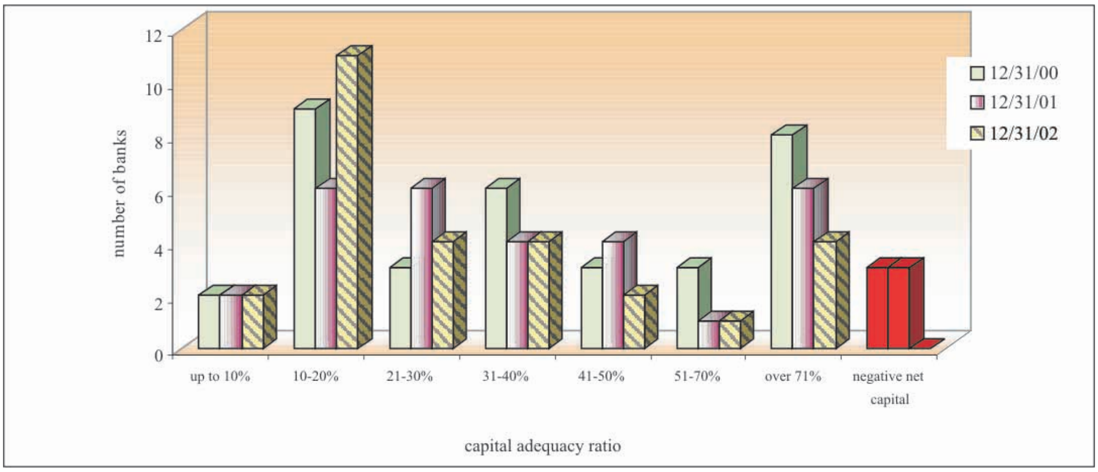


18 Loss made for the interval period from 01/01-08/31/2002.

19 By new Decision on Minimum Standards for Credit Risk and Assets Classification Management (adopted at the end of 2002), banks do have obligation to establish general loan loss reserves (ORKG-2%) for cash items held with foreign banks rated by investment rating. Based on this, in the fourth quarter of 2002, those reserves were decreased by KM 16 million.

Out of total 28 banks in the F BiH, as of 12/31/02, 26 banks had capital adequacy ratio higher than 10% (four banks over 100%) while two banks had capital adequacy ratio under regulatory minimum[20]. But, the concern is with five largest banks (by size of assets) which had capital adequacy ratio between 10% and 15% and they will have immediately to provide additional capital. That should not present any problem since their founders are capable of providing additional capital.

Graph 12: Capital adequacy ratio in banks



We should emphasize that capital adequacy ratio is significantly higher in small banks, mainly due to fact that small banks did not completely develop their operations, primarily credit activities (there is stagnation or poor growth of balance sheet total with major participation of cash assets) and that resulted in decreased risk in assets in those banks.

At the end of 2002, private banks had to comply with the new requirement for minimum share capital paid in cash of KM 15 million. Based on information as of 12/31/02 (for private banks), out of four banks which did not comply with the new requirement, three banks resolved that problem in first two months of 2003 by status changes of assumption/merger (process completed), while one bank with special status is excluded from this compliance until the end of 2003.

Although banking system in the Federation experienced strengthening of capital through the period, there are still too many small banks, some banks are undercapitalized, that is, they do not have strong capital base which would guarantee absorption of all potential losses in performance and a full safety for creditors. Also, we can make conclusion that number of banks in the Federation will continue decreasing, and that is necessary and positive trend from the aspect of strengthening of banking system of the F BiH. The strengthening of capital base will be priority task in majority of banks in 2003, especially large banks in the system. That is necessary for the stability and safety of banks, as well as the whole banking system. Consequently, the FBA's duty will be to establish regulations that would require strengthening of capital base in banks that would guarantee stability and safety of banks.

2.2. Profitability

At the end of 2002, banks in the Federation of BiH showed positive financial results of KM 17,448,000. This indicator is much better in comparison to the one in same period in 2001, when banks had showed loss of KM 32,798,000.

Positive financial result of KM 39,748,000 was reported by 20 banks, while eight banks showed loss of KM 22,300,000. Since one bank in 2002 covered its losses made in the same year[21] of KM 4.1 million against its share capital (at the same time, there was additional capitalization made), in 2003, total uncovered losses from 2002 will be transferred in the amount of KM 18 million. More detailed information is presented in the following schedule:

20 The Law on Changes and Additions to the Law on Banks (Official gazette F BiH, no. 41/02) regulates new capital adequacy ratio of minimum 12%. Banks' duty was to adjust their operations to new regulatory minimums within six months starting from the date of adoption of the Law, that is, until 02/24/03).

21 See Footnote18.

Schedule 20: Income/Loss - *000 KM-*

Date/Description	Whole system Amount	Whole system Number of banks	Private banks Amount	Private banks Number of banks	State banks Amount	State banks Number of banks
12/31/00						
Loss	-76,702	10	-71,100	7	-5,602	3
Income	26,606	27	20,272	23	6,334	4
Total	-50,096	37	-50,828	30	732	7
12/31/01						
Loss	-63,493	10	-63,399	7	-1,094	3
Income	30,695	22	27,024	19	3,671	3
Total	-32,798	32	-35,375	26	2,577	6
12/31/02						
Loss	-22,300	8	-15,502	6	-6,798	2
Income	39,748	20	36,667	16	3,081	4
Total	17,448	28	21,165	22	-3,717	6

Individual analytical information from banks lead to conclusion that profitability in majority of banks is not satisfactory, due to that and to the amount of financial results (income/loss) and to ratios used to determine profitability, productivity and efficiency of operations in banks. As in the other operational segments, this one also includes concentrations: few banks have good profitability, while few banks showed losses in their performance. Out of total income, two private banks showed 60%, while 64% of total loss was shown in three banks (one state and two private banks).

In the structure of total income, net interest margin participates with 45% (for the same period in 2001, it was 40%), and operating income (banking services fee income and other income, including collection of risk placements previously written off) participates with 55% (for the same period in 2001, it was 59%).

Total expenses of banks participate with 95% in total income (for the same period in 2001, it was 108%). In the structure of total expenses, operating expenses have the highest participation of 58% (salary and contribution expenses of 28%, business premises expenses and other fixed assets and overhead of 15%, other operating expenses of 14%), while provisions for general loan risk and potential loan losses participate with 32%. Provisions for general loan risk and potential loan losses have significant decreasing trend in comparison to the previous year (18% less) and decreased participation in the structure of total expenses, which has a positive reflection to the decrease of participation of expenses in total income.

The following schedules show the most significant ratios for assessment of profitability, productivity and efficiency of banks:

Schedule 19: Profitability, Productivity and Efficiency Ratios by Periods

RATIOS	12/31/2000	12/31/2001	12/31/2002
Return on Average Assets	-2.04	-1.18	0.41
Return on Average Total Capital	-9.55	-5.62	3.04
Return on Average Equity Capital	-10.14	-6.15	3.56
Net Interest Income/Average Assets	5.72	5.26	4.50
Fee Income/Average Assets	8.02	7.64	5.50
Total Income/Average Assets	13.74	12.89	10.00
Operating and Direct Expenses[22]/Average Assets	8.98	6.54	3.73
Operating Expense/Average Assets	6.67	7.40	5.80
Total Non-interest Expanse/Average Assets	15.65	13.94	9.52

22 Expenses include provisions for potential loan losses.

Schedule 20: Profitability, Productivity and Efficiency Ratios as of 12/31/02 *-In %-*

RATIOS	12/31/02		
	STATE BANKS	PRIVATE BANKS	AVERAGE IN F BiH
Return on Average Assets	-1.02	0.55	0.41
Return on Average Total Capital	-4.25	4.36	3.04
Return on Average Share Capital	-5.44	5.02	3.56
Net Interest Income/Average Assets	4.51	4.50	4.50
Fee Income/Average Assets	6.87	5.37	5.50
Total Income/Average Assets	11.38	9.87	10.00
Operational and Direct Expenses[23]/ Average Assets	5.83	3.53	3.73
Operational Expense/Average Assets	6.22	5.75	5.80
Total Non-interest Expense/Average Assets	12.05	9.28	9.52

Banking system in 2002, in comparison to the same period from previous year, performed better indicators among which we should emphasize two the most significant indicators of profitability: ROA (return on assets) of 0.41% and ROE (return on equity) of 3.56% (the same indicators as of 12/31/2001, due to the loss shown for the whole system, were the following: -1.18% and –6.15%). But, this is still considerably below the international empirical standards[24].

By analysis of other indicators, we can conclude that in comparison to the end of 2001, productivity of banks expressed through smaller total return on assets is some worse due to further growth of assets in banks and their structure, that is, significant participation of non-interest-bearing assets. Besides, from one period to another, the structure of total income has slight trend of change in favor of net interest income, which is due to the increase in loan portfolio, although banks still gain 55% of total income from operating income.

A financial result shown in whole banking system as of 12/31/2002 is one of the indicators of positive changes in banking system. Profitability in banks in future period will mainly depend on assets quality, that is, loans approved and banks exposure to credit risk, and efficient management of operational costs.

In further restructuring and reform of banking system we should expect elimination of banks which did not comply their operations to the Law (mainly problem of minimum capital standards) and which have, at the same time, mainly operated with loss, through the processes of assumption/merger and liquidation. Other banks in the system should adopt new concept of operational policies which should be better complied with market oriented banking in order to achieve better profit, while maintaining stability of banks at the same time, and preserving managing and control of all risk to which a bank is exposed while operating, especially credit risk. By earning greater profit, through retained income as internal source, banks will strengthen their capital base.

23 Expanses include provisions for potential loan losses.

24 International standard for ROA is 1%, and for ROE is 12-18%.

III. CONCLUSION

Consolidation and stabilization of banking sector in the Federation of BiH in last year resulted in new development reflected in significant growth of assets and capital, decreasing number of small banks, introduction of new products, designing new regulative framework in order to provide stronger implementation of international operational standards.

Banks achieved better financial results in comparison to previous years, but still, seven banks showed operational loss.

In future period the main activities of the FBA will be stronger control of risk, before all, credit risk, and to insist on establishment of more harsh policies and procedures and their application in banks. At the same time, the FBA will undertake actions for strengthening internal control, external and internal audits and capital strengthening in banks.

Continuation of positive trends should include uninterrupted activities of all participants in the reform of banking system and implementation of actions that would lead to fast finalization of transition process.

Involvement of authorized institutions and entities in the Federation of BiH will effect further positive changes, such as:

- fastening of reform process in material sector, followed by progress in monetary and banking system;
- finalization of privatization process in state banks within expected deadlines;
- establishing regulatory framework to support process of increasing number of large banks;
- improvement of environment for bank operations in the area of whole Bosnia and Herzegovina;
- transfer of succession assets to development, through commercial banks;
- faster and more efficient implementation of Law on Collateral;
- accelerating court procedures, passing judgments and their implementation;
- establishing efficient procedure for performance of pledges;
- appointing law for protection of creditors and higher and more concrete responsibility of banks' debtors;
- further improvement of legal and institutional framework for the reform of banking system and whole financial system, with respect of Basle Principles and European guidelines;
- support to the initiative to allow the Central Bank to issue bonds and treasury bills, etc.

The duties of the Banking Agency of the Federation of BiH in future period are:

- continuous supervision of banks in order to provide for effective protection of depositors and eliminate weakness in banks;

- finalization of remaining provisional and liquidation administrations in banks;
- special supervision of banks with high amounts of savings (citizen savings) and banks with growth above average (fast expansion);
- special supervision of operations with related entities;
- control over implementation of new standards for banking operations regulated by laws and regulations;
- further development of regulations under authority of the Agency (FC risk, capital standards, etc.), in accordance with Basel Principles;
- further education and training of FBA staff;
- intensified activities for implementation of regulations for prevention of money laundry and financing of terrorism, and implementation of cooperation with other supervisory and control institutions;
- establishment of data base on non-performing clients which are considered special credit risk for banks;
- improvement and application of IT systems for early warning and prevention of weaknesses in banks;
- efficient cooperation with Association of Banks;
- establishment of cooperation with supervisory institutions in countries whose natives are investors in our banking system;
- advising on application and further development of regulations passed by the FBA, etc.

And, as the most important part of the system, banks have to undertake the following activities:

- further strengthening of capital in correlation with growth of assets and risk;
- improve quality of assets;
- strengthen internal control systems and establish internal audits, and provision of their independence;
- adopt and implement new principles for operations, policies and procedures in accordance with competitive market conditions;
- exchange of information on non-performing debtors, that is, reporting to the FBA on debtors that are considered special credit risk for banks which would provide for conditions to establish special data base;
- faster development of credit/debit card operations and electronic banking;
- development of procedures for control and improvement of IT;
- implement more strict criteria and their implementation in matter of competency and expertise of managerial staff in banks;
- improvement of staff and training in order to establish better relations with customers, especially small and middle-sized enterprises, hence, this includes new services, common all over the world, that is, banks should develop financial management operations;
- efficient participation in global process of preventing money laundering and terrorism financing, etc.

ATTACHMENTS

BASIC DATA ABOUT BANKS IN THE F BiH
12/31/2002

Red.broj	BANKA	Adresa		Telefon	Direktor
1	ABS BANKA dd - SARAJEVO	Sarajevo	Trampina 12/VI	722-400, 722-401	ISMET KUMALIĆ
2	BOSNA BANK INTERNATIONAL dd - SARAJEVO	Sarajevo	Trg djece Sarajeva bb	275-130	ANDRE VAN HOVE
3	BOR BANKA dd - SARAJEVO	Sarajevo	Obala Kulina bana 18	663-500, 472-487	HAMID PRŠEŠ
4	CENTRAL PROFIT BANKA dd - SARAJEVO	Sarajevo	Zelenih beretki 24	533-433; 533-688, 531-006,	FEHIM KAPID□IĆ
5	COMMERCEBANK, ban□na skupina NLB dd - SARAJEVO	Sarajevo	Džidžikovac 1.	204-119	FRANC VISENJAK
6	GOSPODARSKA BANKA dd - MOSTAR	Mostar	Ante Zuanića bb	036 / 318-424, 318-395	Privremeni upravnik - Senad Kazazić od 01.07.2002.
7	GOSPODARSKA BANKA dd - SARAJEVO	Sarajevo	Ferhadija 11	667-688; 670-660, 444-605	MIJO MIŠIĆ
8	HERCEGOVAČKA BANKA dd MOSTAR	Mostar	Kneza Domagoja bb.	036/320-555,324-346,	Privremeni upravnik - Toby Robinson od 06.04.2001.
9	HVB-BANKA BOSNA I HERCEGOVINA dd SARAJEVO	Sarajevo	Fra Anđela Zvizdovića 1	250-900, fax 250-924	FRANZ FRIEDL
10	HYPO ALPE-ADRIA-BANK dd - MOSTAR	Mostar	Kneza Branimira 2b	036/444-444, 444-445, 444-400	PETAR JURČIĆ
11	INVESTICIJSKA BANKA FEDERACIJE BIH	Sarajevo	Paromlinska bb	230-390; 277-900; 277-902	ASIM OMANIĆ
12	INVESTICIONO-KOMERCIJALNA BANKA dd - ZENICA	Zenica	Trg B&H 1	032 / 201-804; 417-022	HALIM ČABARAVDIĆ
13	KOMERCIJALNO-INVESTICIONA BANKA DD V.KLADUŠA	V.Kladuša	Ibrahima Mržljaka 3.	037/772-416, 771-654, 771-253	HASAN PORČIĆ
14	LJUBLJANSKA BANKA dd - SARAJEVO	Sarajevo	Kaptol 4	205-263, 205-264, 205-265,	ĆAMIL BAVČIĆ
15	LT KOMERCIJALNA BANKA dd - LIVNO	Livno	Gabrijela Jurkića bb	034/201-227, 201-414, 201-942,	IVICA BEKAVAC
16	MICRO ENTERPRISE BANK dd - SARAJEVO	Sarajevo	Sime Milutinovića 4.	232-172; 232-173, 232-546	FRIEDER WOEHRMANN
17	POŠTANSKA BANKA BiH dd - SARAJEVO	Sarajevo	Branilaca Sarajeva 20/XI	212-993, 210-007	MUFID LOJO
18	PRIVREDNA BANKA SARAJEVO dd - SARAJEVO	Sarajevo	Alipašina 6	277-700, 277-707, 277-718	MEVSUDIN DREKOVIĆ
19	RAIFFEISEN BANK dd - SARAJEVO	Sarajevo	Danijela Ozme 3	440-272; 442-964; 214-900;	EDIN MUFTIĆ
20	RAIFFEISEN BANK HPB dd - MOSTAR	Mostar	Kneza Domagoja bb	036 / 316-020;316-651, 316-010,	DAVOR ŠIMIĆ
21	TURKISH ZIRAAT BANK BOSNIA dd - SARAJEVO	Sarajevo	Ferhadija 29	440-040, 440-062, 440-573	OZNUR OZENIS
22	TUZLANSKA BANKA dd - TUZLA	Tuzla	Maršala Tita 34	035/251-200, 251-576, 251-197,	M. ABDURAHMANOVIĆ
23	UNA BANKA dd - BIHAĆ	Bihać	Bosanska 25	037 / 322-400, 322-402	Privremeni upravnik - Esad Kozar□anin od 07.05.2001.
24	UNION BANKA dd - SARAJEVO	Sarajevo	Dubrova□ka 6	219-471, 219-472, 219-473	SULEJMAN HOD□IĆ
25	UNIVERSAL BANKA dd - SARAJEVO	Sarajevo	Branilaca Sarajeva 20/V	214-594,214-587,664-139,668-239	D□ENAMIR ABAZA
26	UPI BANKA dd - SARAJEVO	Sarajevo	Obala Kulina bana 9a.	200-301, 200-309, 664-135	MIRSAD LETIĆ
27	VAKUFSKA BANKA dd - SARAJEVO	Sarajevo	Ferhadija 4	470-945, 200-598, 471-178,	AMIR RIZVANOVIĆ
28	VOLKSBANK BH dd - SARAJEVO	Sarajevo	Fra Anđela Zvizdovića 1	483-266, 483-264	REINHOLD KOLLAND
29	ZAGREBAČKA BANKA BH dd - MOSTAR	Mostar	Kardinala Stepinca bb	036/312-112,312-121,312-167,	BERISLAV KUTLE

LEGAL FRAMEWORK FOR BANKING AGENCY OF THE FEDERATION OF BIH AND BANKS IN THE FEDERATION OF BIH

1. Law on Banking Agency of the Federation of BiH ("Official Gazette of the F BiH", 9/96, 27/98, 20/00, 45/00 and 58/02),
2. Law on Central Bank of BiH ("Official Gazette of the F BiH", 1/97 and 29/02),
3. Law on Banks ("Official Gazette of the F BiH", 39/98,32/00, 48/01, 27/02, 41/02 and 58/02),
4. Law on Deposit Insurance in Banks of BiH("Official Gazette of BiH", 20/02),
5. Law on Financial Performance ("Official Gazette of the F BiH", 2/95, 13/00 and 29/00),
6. Law on Internal Payment System ("Official Gazette of the F BiH", 15/00-cleared version, 54/01 and 40/99),
7. Law on Foreign Exchange ("Official Gazette of the F BiH", 35/98),
8. Law on Securities ("Official Gazette of the F BiH", 39/98 and 36/99),
9. Law on Prevention of Money Laundering ("Official Gazette of the F BiH", 8/00),
10. Law on Notes ("Official Gazette of the F BiH", 32/00),
11. Law on Cheques ("Official Gazette of the F BiH", 32/00),
12. Law on Payment Transactions ("Official Gazette of the F BiH", 32/00),
13. Law on Obligations ("Official Gazette of the F BiH", 2/95),
14. Law on Commercial Enterprises ("Official Gazette of the F BiH", 23/99, 45/00 and 2/02),
15. Law on Bankruptcy and Liquidation ("Official Gazette of the F BiH", 23/98),
16. Labor Law ("Official Gazette of the F BiH", 43/99 and 32/00),
17. Law on Executive Procedure ("Official Gazette of the F BiH", 42/98),
18. Law on Procedure of Registration of Legal Entities into the Court Registry ("Official Gazette of the F BiH", 4/00, 19/00, 49/00, 32/02 and 58/01),
19. Law on Administrative Procedure ("Official Gazette of the F BiH", 2/98 and 48/99),
20. Law on Violations Representing a Breach of Federal Regulations ("Official Gazette of the F BiH", 9/96 and 29/00),
21. Law on Treasury of BiH Institutions ("Official Gazette of the F BiH", 27/00),
22. Law on Bank Privatization ("Official Gazette of the F BiH", 12/98, 29/00 and 37/01),
23. Law on Opening Balance Sheet of Enterprises and Banks ("Official Gazette of the F BiH", 12/98 and 40/99),
24. Law on Securities Registry ("Official Gazette of the F BiH", 39/98 and 36/99),
25. Law on Securities Commission ("Official Gazette of the F BiH", 39/98 and 36/99),
26. Law on Accounting ("Official Gazette of the F BiH", 2/95, 14/97 and 12/98).

BANK REGULATIONS

1. Decision on Bank Supervision and Procedures of Banking Agency of the Federation of BiH ("Official Gazette of the F BiH", 3/03),
2. Decision on Minimum Standards for Bank Capital management ("Official Gazette of the F BiH", 3/03),
3. Decision on Minimum Standards for Bank Credit Risk and Assets Classification Management ("Official Gazette of the F BiH", 3/03),
4. Decision on Minimum Standards for Bank Risk Concentration Management ("Official Gazette of the F BiH", 3/03, ispr. 6/03),
5. Decision on Minimum Standards for Bank Internal and External Audit ("Official Gazette of the F BiH", 3/03),
6. Decision on Minimum Standards for Bank Internal Control System ("Official Gazette of the F BiH", 3/03),
7. Decision on Minimum Standards for Bank Liquidity Risk Management ("Official Gazette of the F BiH", 3/03),
8. Decision on Minimum Standards for Bank Foreign Exchange Risk Management ("Official Gazette of the F BiH", 3/03),
9. Decision on Minimum Standards for Operations with Bank Related Entities ("Official Gazette of the F BiH", 3/03),
10. Decision on Minimum Standards for Recording Bank Lending Activities ("Official Gazette of the F BiH", 3/03),
11. Decision on Reporting Non-Performing Clients Who are Considered Special Credit Risk ("Official Gazette of the F BiH", 3/03),
12. Decision on Minimum Scope, Form and Content of the Program and Report on Economic-Financial Audit of Banks ("Official Gazette of the F BiH", 3/03),
13. Decision on Reporting Forms Which Banks Submit to Banking Agency of the Federation of BiH ("Official Gazette of the F BiH", 3/03),
14. Decision on Conditions When Bank is Considered Insolvent ("Official Gazette of the F BiH", 3/03),
15. Decision on Minimum Requirements Bank has to Fulfill in Order to Perform Internal Payment System ("Official Gazette of the F BiH", 46/01),
16. Decision on Procedure to Determine Claims and Allocation of Assets and Liabilities in Bank Liquidation Process ("Official Gazette of the F BiH", 3/03),
17. Internal Rating Criteria by Banking Agency of the F BiH ("Official Gazette of the F BiH", 3/03, ispr. 6/03),
18. Decision on Minimum Standards to Issue License for Internal Payment System for Branches of Banks from Republic Srpska ("Official Gazette of the F BiH", 50/01),
19. Decision on Minimum Standards for Banks Activities on Prevention of Money Laundering and Terrorism Financing ("Official Gazette of the F BiH", 3/03),
20. Decision on Financial Disclosure ("Official Gazette of the F BiH", 3/03),
21. Decision on Calculation of Interest and Fees on Dormant Accounts ("Official Gazette of the F BiH", ...),
22. Decision on Amount and Conditions for Approving Loans to Bank Employees ("Official Gazette of the F BiH", ...),
23. Guidelines for Licensing and Other Consents from Banking Agency of the F BiH ("Official Gazette of the F BiH", 46/02).

ATTACHMENT 3

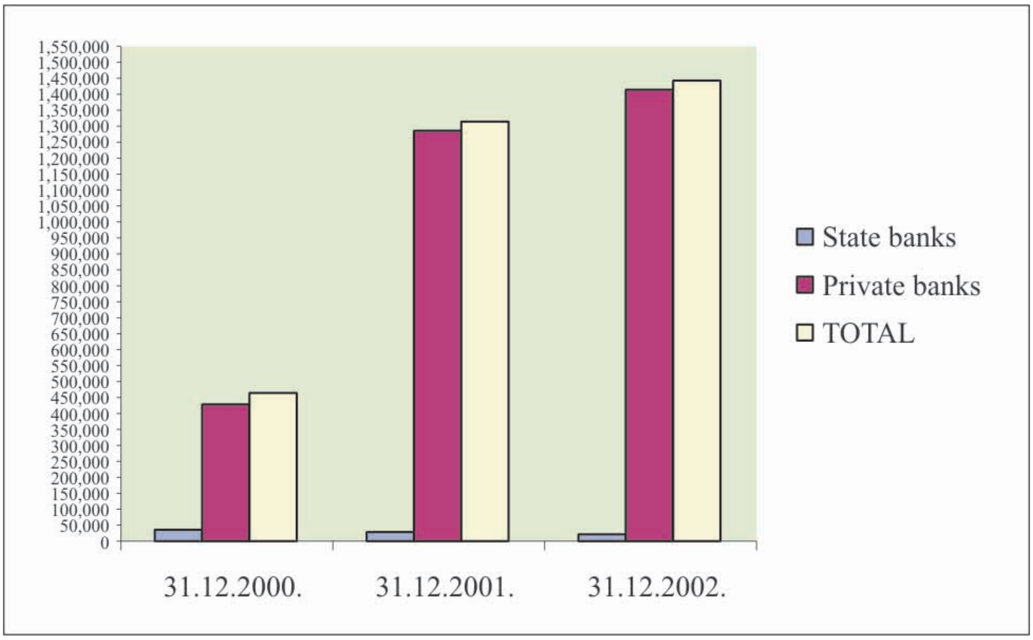
BALANCE SHEET OF BANKS IN THE FBiH (ACCORDING TO THE FBA SCHEDULE) ACTIVE SUB-BALANCE SHEET

No.	DESCRIPTION	12/31/00	12/31/01	12/31/02
	ASSETS			
1.	Cash Funds and Deposit Accounts with Deposit Institutions	1,025,813	1,783,234	1,595,153
1a	Cash and Non-Interest Bearing Deposit Accounts	369,061	1,039,914	587,969
1b	Interest-Bearing Deposit Accounts	656,752	743,320	1,007,184
2.	Trading Securities	3,912	47,192	50,459
3.	Placements to Other Banks	20,311	25,355	19,952
4.	Loans, Leasing Type Receivables and Past-due Receivables	1,308,259	1,723,663	2,690,531
4a	Loans	1,128,546	1,526,180	2,525,356
4b	Leasing Type Receivables	0	0	0
4c	Loans and Leasing Type Past-due Receivables	179,713	197,483	165,175
5.	Securities Held to Maturity	440	4,244	22,691
6.	Business Premises and Other Fixed Assets	272,979	263,547	284,233
7.	Other real-estate	10,457	10,434	15,017
8.	Investments to Non-Consolidated Related Companies	35,094	17,211	32,351
9.	Other Assets	50,377	71,689	90,635
10.	MINUS: Reserves for Potential Losses	188,324	178,082	204,934
10a	Reserves for the Items in Position 4 of the Assets	165,608	151,504	186,946
10b	Reserves for the Assets Items, Except for Position 4	22,716	26,578	17,988
11.	**TOTAL ASSETS**	**2,539,318**	**3,768,487**	**4,596,088**
	LIABILITIES			
12.	Deposits	1,763,000	2,900,613	3,528,209
12a	Interest-Bearing Deposits	1,064,739	1,999,170	2,871,780
12b	Non-Interest-Bearing Deposits	698,261	901,443	656,429
13.	Borrowings - Past-due Liabilities	8,662	7,637	5,295
13a	Past-due, Not Paid Liabilities	1,093	78	477
13b	Not Fulfilled - Called for Payment Off-Balance Sheet Liabiliti	7,569	7,559	4,818
14.	Borrowings from Other Banks	6,761	5,550	3,352
15.	Liabilities to Government	350	1,225	8,068
16.	Liabilities on Loans and Other Borrowings	188,448	253,269	313,010
16a	with remaining number of maturity days up to 1 year	13,940	36,072	61,615
16b	with remaining number of maturity days over 1 year	174,508	217,197	251,395
17.	Subordinated Debts and Subordinated Bonds	4,771	5,179	21,040
18.	Other Liabilities	72,051	90,523	89,337
19.	**TOTAL LIABILITIES**	**2,044,044**	**3,263,996**	**3,967,590**
	CAPITAL			
20.	Permanent Priority Shares	14,336	5,698	14,759
21.	Common Shares	491,075	452,788	524,002
22.	Surplus over per Value	0	5,565	4,766
22a	of permanent priority shares	0	0	0
22b	of common shares	0	5,565	4,766
23.	Undivided Profit and Capital Reserves	41,320	72,483	66,200
24.	Exchange Rate Differences	-840	0	0
25.	Other Capital	-50,616	-32,043	18,771
26.	TOTAL CAPITAL (20. to 25.)	495,275	504,491	628,498
27.	**TOTAL LIABILITIES AND CAPITAL (19 +26)**	**2,539,318**	**3,768,487**	**4,596,088**
	PASIVE AND NEUTRAL SUB-BALANCE SHEET	**1,187,175**	**859,296**	**102,934**
	TOTAL BALANCE SHEET SUM OF BANKS	**3,726,494**	**4,633,450**	**4,699,022**

NEW CITIZENS SAVINGS BY PERIODS

000 KM

	12/31/00	12/31/01	12/31/02
State Banks	34,841	28,787	22,072
Private Banks	427,166	1,285,803	1,417,847
TOTAL	462,007	1,314,590	1,439,919



PRILOG 5

INCOME STATEMENT

000 KM

ELEMENTS	PERFORMED Jan-Dec 2000		PERFORMED Jan-Dec 2001		PERFORMED Jan-Dec 2002		RATIO 4 : 2	RATIO 6 : 4
	Amount	participation in total income	Amount	participation in total income	Amount	participation in total income		
1	2	3	4	5	6	7	8	9
INCOME								
Interest income	192,782	57%	199,487	56%	267,925	63%	132	134
Interest expense	52,117	15%	52,882	15%	77,902	18%	157	147
Net interest income	140,665	42%	146,605	41%	190,023	45%	124	130
Fee income	197,074	58%	212,919	59%	231,572	55%	110	109
TOTAL INCOME	337,739	100%	359,524	100%	421,595	100%	114	117
EXPENSE								
Reserves for potential losses	179,733	53%	162,322	45%	133,403	32%	126	82
Salaries and payables with salary	84,898	25%	97,426	27%	118,685	28%	123	122
Fixed assets and overhead expense	38,140	11%	50,760	14%	64,574	15%	125	127
Other expense	82,141	24%	78,290	22%	84,661	20%	76	108
TOTAL EXPENSE	384,912	113%	388,798	108%	401,323	95%	110	103
NET INCOME BEFORE TAXES	-47,172		-29,274		20,272			
Taxes	2,924		3,524		2,824			
NET INCOME	-50,096		-32,798		17,448			

NUMBER OF EMPLOYEES BY BANKS

No.	BANK	12/31/00	12/31/01	12/31/02
1	ABS BANKA dd SARAJEVO	119	209	289
2	BOSNA BANK INTERNATIONAL dd Sarajevo		29	46
3	BOR BANKA dd SARAJEVO	34	31	36
4	CENTRAL PROFIT BANKA dd SARAJEVO	319	389	481
5	COMMERCEBANK dd SARAJEVO	52	71	93
6	GOSPODARSKA BANKA dd SARAJEVO	99	105	125
7	GOSPODARSKA BANKA dd MOSTAR	30	29	46
8	RAIFFEISEN BANK HPB dd MOSTAR	82	147	194
9	HYPO ALPE ADRIA BANK dd MOSTAR	168	203	248
10	HVB BANKA BiH dd SARAJEVO			44
11	INVESTICIJSKA BANKA FBiH SARAJEVO	69	67	71
12	INVESTICIONO KOMERCIJALNA BANKA dd ZENICA	205	210	201
13	KOMERCIJALNO INVESTICIONA BANKA dd VELIKA KL	24	36	40
14	LT KOMERCIJALNA BANKA dd LIVNO	64	60	61
15	LJUBLJANSKA BANKA dd SARAJEVO	82	91	90
16	MICRO ENTERPRISE BANK dd SARAJEVO	73	130	171
17	POŠTANSKA BANKA dd SARAJEVO	76	87	89
18	PRIVREDNA BANKA dd SARAJEVO	273	277	221
19	RAIFFEISEN BANK BH dd SARAJEVO	247	517	702
20	TURKISH ZIRAAT BANK dd SARAJEVO	48	47	50
21	TUZLANSKA BANKA dd TUZLA	349	374	374
22	UNA BANKA dd BIHAC	136	98	80
23	UNION BANKA dd SARAJEVO	163	182	182
24	UNIVERSAL BANKA dd SARAJEVO	152	265	301
25	UPI BANKA dd SARAJEVO	79	123	145
26	VAKUFSKA BANKA dd SARAJEVO	65	68	148
27	VOLKSBANK BH dd SARAJEVO	48	80	122
28	ZAGREBACKA BANKA BH dd MOSTAR	399	416	451
	OTHER BANKS *	834	269	-
	TOTAL	4,289	4,610	5,101

* Banks that had status changes (assumption/merger or liquidation)