UNICREDIT BANK A.D., BANJA LUKA

Financial statements
Year ended December 31, 2013 and
Independent Auditors' Report

Translation of the Auditors' Report issued in the Serbian language

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Translation of the Auditors' Report issued in the Serbian language

INDEPENDENT AUDITORS' REPORT

To the Supervisory Board and Shareholders of UniCredit bank a.d., Banja Luka

We have audited the accompanying financial statements (page 2 to 70) of UniCredit bank a.d., Banja Luka (hereinafter the "Bank"), which comprise the statement of financial position as of December 31, 2013 and the related statement of comprehensive income, statement of changes in equity and statement of cash flow for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the International Financial Reporting Standards and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Bank's preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements of UniCredit bank a.d., Banja Luka present fairly, in all material respects, the financial position of the Bank as at December 31, 2013, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Deloitte doo

Deloitte d.o.o.,
Banja Luka
February 19, 2014

Statement of Comprehensive Income
For the year

	Note	2013. BAM '000'	2012. BAM '000'
Interest income	6	54,624	49,959
Interest expenses	7	(11,085)	(10,003)
Net interest income		**43,539**	**39,956**
Fee and commission income	8	12,549	11,801
Fee and commission expenses	9	(1,419)	(1,108)
Net fee and commission income		**11,130**	**10,693**
Dividend and equity interest income	10	**13**	-
Net foreign exchange gains / losses upon translation of monetary assets and liabilities	11	1,370	2,060
Total operating income		**56,052**	**52,709**
Personnel expenses	12	(13,627)	(13,522)
Depreciation and amortization	22,23	(4,525)	(4,476)
Other expenses	13	(10,938)	(10,850)
Total operating expenses		**(29,090)**	**(28,848)**
Profit before impairment and provisions		**26,962**	**23,861**
Net impairment losses and provisions for credit risk	14	(7,960)	(7,135)
Provisions for risks and charges	15	(572)	(333)
Impairment gains / losses on property and equipment	22	42	(919)
Profit before taxes		**18,472**	**15,474**
Income tax expense	16	(1,655)	(1,634)
Profit for the year		**16,817**	**13,840**
Other comprehensive income			
Net change in fair value reserves		(343)	69
Total comprehensive income for the year		**16,474**	**13,909**
Basic and diluted earnings per share (in BAM)	31	122.85	118.07

The financial statements were approved by the Bank Management as at February 6, 2014.

Signed on behalf of UniCredit Bank a.d., Banja Luka:

Dalibor Čubela
Director

Sandra Vojnović
CFO

Notes set out on pages 6 to 70 form an integral part of these financial statements

Translation of the Auditors' Report issued in the Serbian language

Statement of Financial Position
As at December 31,

	Note	2013 BAM '000	2012 BAM '000
Assets			
Cash and cash equivalents	*17*	41,412	47,177
Obligatory reserve with the Central Bank	*18*	40,975	36,854
Loans and receivables due from banks	*19*	97,659	135,765
Financial assets available for sale	*21a*	69,190	55,728
Loans and receivables from customers	*20*	671,932	607,855
Financial assets held to maturity	*21b*	105	170
Property and equipment	*22*	17,049	17,839
Intangible assets	*23*	3,039	4,658
Other assets	*24*	2,575	5,593
Deferred tax assets	*29*	54	19
Total assets		**943,990**	**911,658**
Liabilities			
Deposits and borrowings due to banks	*25*	252,028	289,399
Deposits and loans due to customers	*26*	532,881	482,805
Other liabilities	*27*	12,416	24,544
Provisions for liabilities and costs	*28*	2,088	1,473
Income tax payable		264	354
Deferred tax liabilities	*29*	0	243
Total liabilities		**799,677**	**798,818**
Equity and reserves			
Share capital	*30*	97,055	82,055
Share premium		373	373
Regulatory reserve for credit losses		12,007	9,288
Fair value reserve		(415)	(72)
Legal reserve		5,854	5,161
Retained earnings		12,622	2,195
Net profit for the year		16,817	13,840
Total equity and reserves		**144,313**	**112,840**
Total liabilities, equity and reserves		**943,990**	**911,658**

Notes set out on pages 6 to 70 form an integral part of these financial statements

Statement of Changes in Equity

	Share capital BAM '000	Share premium BAM '000	Regulatory reserve for credit losses BAM '000	Fair value reserve BAM '000	Legal reserve BAM '000	Revaluation reserve BAM '000	Retained earnings BAM '000	Profit for the year BAM '000	Total BAM '000
Balance as at January 1, 2012	**82,055**	**373**	**5,861**	**(141)**	**387**	**2,195**	**-**	**8,201**	**98,931**
Transfers among reserves	-	-	3,427	-	4,774	(2,195)	2,195	(8,201)	-
Net profit for the year	-	-	-	-	-	-	-	13,840	13,840
Other comprehensive income	-	-	-	-	-	-	-	-	-
Net gains from change in fair value of financial assets available for sale	-	-	-	69	-	-	-	-	69
Total other comprehensive income		-	-	69	-	-	-	-	69
	-	-	-	-	-	-	-	-	-
Total comprehensive income	-	-	-	69	-	-	-	13,840	13,909
Balance as at 31 December 2012	**82,055**	**373**	**9,288**	**(72)**	**5,161**	**-**	**2,195**	**13,840**	**112,840**
Balance as at January 1, 2013	82,055	373	9,288	(72)	5,161	-	2,195	13,840	112,840
Share capital increase	15,000	-	-	-	-	-	-	-	15,000
Transfer among reserves	-	-	2,719	-	693	-	10,427	(13,840)	(1)
Net profit for the year	-	-	-	-	-	-	-	16,817	16,817
Other comprehensive income	-	-	-	-	-	-	-	-	-
Net losses from change in fair value of financial assets available for sale	-	-	-	(343)	-	-	-	-	(343)
Total other comprehensive income	-	-	-	(343)	-	-	-	-	(343)
	-	-	-	-	-	-	-	-	-
Total comprehensive income	**-**	**-**	**-**	**(343)**	**-**	**-**	**-**	**16,817**	**16,474**
Balance as at December 31, 2013	**97,055**	**373**	**12,007**	**(415)**	**5,854**	**-**	**12,622**	**16,817**	**144,313**

Notes set out on pages 6 to 70 form an integral part of these financial statements

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Statement of Cash Flows
For the year

	Note	**2013 BAM '000**	**2012 BAM '000**
Cash flows from operating activities			
Profit before taxes		**18,472**	**15,474**
Adjustments:			
- depreciation and amortization	*22,23*	4,525	4,476
- net impairment gains / losses and provisions for credit risks	*14*	7,960	7,135
- net increases / decreases in provisions for liabilities and costs	*15*	572	333
- net foreign exchange gains / losses	*11*	(1,370)	(2,060)
- gains / losses on the sale of equipment		(42)	-
- impairment of property and equipment	*22*	-	919
Changes in operating assets and liabilities			
Increase / decrease in loans and advances to other banks		38,106	(97,637)
Increase / decrease in loans to customers		(70,769)	(78,784)
Increase / decrease in accrued interest and other assets		3,018	(1,019)
Increase / decrease in obligatory reserve with the Central Bank		(4,121)	(4,638)
Increase / decrease in deposits due to banks		(37,371)	94,712
Increase / decrease in deposits due to customers		50,076	85,224
Increase / decrease in other liabilities		(12,128)	14,680
Net cash generated by/used in operating activities before taxes		**(3,072)**	**38,815**
Income taxes paid		(2,179)	(2,015)
Net cash generated by/used in operating activities		**(5,251)**	**36,800**
Cash flows from investing activities			
Purchase of property, equipment and intangible assets	*22,23*	(2,117)	(3,472)
Increase / decrease in financial assets available for sale		(13,462)	(8,193)
Increase / decrease of financial assets held to maturity		65	30
Increase / decrease in share capital		15,000	-
Net cash generated by/used in investing activities		**(514)**	**(11,635)**
Net increase / decrease in cash and cash equivalents		**5,765**	**25,165**
Cash and cash equivalents at the beginning of the year	*17*	**47,177**	**22,012**
Cash and cash equivalents at the end of the year	*17*	**41,412**	**47,177**

NOTES TO THE FINANCIAL STATEMENTS

1. REPORTING ENTITY

UniCredit Bank a.d., Banja Luka (the „Bank") is a shareholding company registered in the Republic of Srpska for performance of payment transactions, credit and deposit operations in the country and abroad in accordance with the regulations of the Republic of Srpska.

History of the Bank is related to the beginning of the past century, i.e. to 1911 and establishment of the Monetary Institute which subsequently developed into the Bank for Trade and Crafts. In the next 60 years, numerous transformations and changes of names under which the Bank operated were made: in 1956, District – Communal Bank (Sreska komunalna banka), in 1961, Municipal Bank (Komunalna banka), and in 1966, Credit Bank.

By the reform of the banking system in 1971, the Credit Bank was merged by the Commerce Bank Sarajevo as its branch, and in 1976 it obtained a high degree of autonomy and was registered as the Basic Bank.

By the decision of the Founders Assembly meeting in December 1989 the Bank was spun off from the Commerce Bank Sarajevo system into an independent bank, under the name Banjalučka banka d.d. Banja Luka. From June 1998, it continued working as a shareholding company under the name Banjalučka banka a.d. Banja Luka.

In accordance with regulations on privatization of state-owned capital in the Republic of Srpska, in October 2000, shares of state-owned enterprises in the Bank were transferred to the management of the RS Ministry of Finance until the completion of privatization of the state-owned capital.

In early 2002, the Government of the Republic of Srpska sold the shares of the state to the company "Verano Motors" d.o.o., Belgrade. The first Shareholders' Meeting of the private Bank adopted a decision on the change of the name from Banjalučka banka into Nova banjalučka banka a.d., Banjaluka.

Since the end of 2002, the Bank's shares have been quoted on the Stock Exchange. Having purchased the package of shares in the end of 2005, Bank Austria Creditanstalt AG Vienna became the majority owner of the Bank with the equity interest of 83.3%. By further purchases of shares and increase in share capital, Bank Austria increased its share to 90.92% of the total capital of the Bank.

With the change in the ownership structure after the entry of Bank Austria as the majority shareholder, the Bank became the member of HVB Group, and after the change in the ownership structure of Bank Austria whose majority owner became UniCredit Bank Milan, the Bank became a member of UniCredit Group. In 2008, the name Nova banjalučka banka a.d. Banja Luka was changed, hence since June 1, 2008, the Bank has had the name UniCredit Bank a.d. Banja Luka.

As at December 31, 2013, the Bank consisted of the Head Office in Banja Luka with registered seat at no. 7, Marije Bursać Street, 32 branch offices and 7 agencies (December 31, 2012: 35 branch offices and 3 agencies). As at December 31, 2013, the Bank had 419 employees (2012: 426 employees).

The tax identification number of the Bank is 4400958880009, and its VAT code is 400958880009.

2. BASIS OF PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS AND ACCOUNTING CONVENTION

2.1. Statement of Compliance

The accompanying financial statements represent annual financial statements of the **UniCredit Bank a.d.,** Banja Luka, prepared in accordance with the International Financial Reporting Standards (IFRS).

2.2. Application and Impact of the New and Revised IFRS

Standards and Interpretations Effective in the Current Period

The following amendments to the existing standards issued by the International Accounting Standards Board and interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) have been effective over the current period:

- IFRS 10 "Consolidated Financial Statements" (effective for annual periods beginning on or after January 1, 2013);
- IFRS 11 "Joint Arrangements" (effective for annual periods beginning on or after January 1, 2013);

NOTES TO THE FINANCIAL STATEMENTS

2. BASIS OF PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS AND ACCOUNTING CONVENTION (Continued)

2.2. Application and Impact of the New and Revised IFRS (Continued)

Standards and Interpretations Effective in the Current Period (Continued)

- IFRS 12 “Disclosures of Involvement with Other Entities” (effective for annual periods beginning on or after January 1, 2013);
- IFRS 13 “Fair Value Measurement” (effective for annual periods beginning on or after January 1, 2013);
- IAS 27 (revised in 2011) “Separate Financial Statements” (effective for annual periods beginning on or after January 1, 2013);
- IAS 28 (revised in 2011) “Investments in Associates and Joint Ventures” (effective for annual periods beginning on or after January 1, 2013);
- Amendments to IFRS 1 “First-time Adoption of International Financial Reporting Standards” – Government Loans with a Below-Market Rate of Interest (effective for annual periods beginning on or after January 1, 2013);
- Amendments to IFRS 7 “Financial Instruments: Disclosures” – Offsetting Financial Assets and Financial Liabilities (effective for annual periods beginning on or after January 1, 2013);
- Amendments to IFRS 10 “Consolidated Financial Statements,” IFRS 11 “Joint Arrangements“ and IFRS 12 “Disclosures of Involvement with Other Entities“ - Transition Guidance” (effective for annual periods beginning on or after January 1, 2013);
- Amendments to IAS 1 “Presentation of Financial Statements” – Presentation of Items of Other Comprehensive Income (effective for annual periods beginning on or after July 1, 2012);
- Amendments to IAS 19 “Employee Benefits” – Improvements to the Accounting for Post-Employment Benefits (effective for annual periods beginning on or after January 1, 2013);
- Amendments resulting from Annual Improvements IFRS (2012issued on May 17, 2012 (IFRS 1, IAS 1, IAS 16, IAS 32, IAS 34), with a view to removing inconsistencies and clarifying wording (effective for annual periods beginning on or after January 1, 2013); and
- IFRIC 20 “Stripping Costs in the Production Phase of a Surface Mine” (effective for annual periods beginning on or after January 1, 2013).

Adoption of these standards, revisions and interpretations has not resulted in significant changes in the accounting policies of the Bank.

Standards and Interpretations in Issue not yet in Effect

At the date of authorization of these financial statements the following standards, revisions and interpretations were in issue but not yet effective:

- IFRS 9 “Financial Instruments” and subsequent amendments (effective date was not yet determined);
- Amendments to IFRS 9 “Financial Instruments” and IFRS 7 “Financial Instruments: Disclosures” – Mandatory Effective Date and Transition Disclosures (effective for annual periods beginning on or after January 1, 2015);
- Amendments to IFRS 10, IFRS 12 and IAS 27 - Exemption from Consolidation of Subsidiaries under IFRS 10 'Consolidated Financial Statements' (effective for annual periods beginning on or after January 1, 2014);
- Amendments to IAS 32 “Financial Instruments: Presentation” – Offsetting Financial Assets and Financial Liabilities (effective for annual periods beginning on or after January 1, 2014);
- Amendments to IAS 36 “Impairment of Assets” - Recoverable Amount Disclosures for Non-Financial Assets (effective for annual periods beginning on or after January 1, 2014);
- Amendments to IAS 39 “Financial Instruments:” Recognition and Measurement - Novation of Derivatives and Continuation of Hedge Accounting (effective for annual periods beginning on or after January 1, 2014);
- Amendments resulting from Annual Improvements 2010-2012 Cycle issued in December 2013 (IFRS 2, IFRS 3, IFRS 8, IFRS 13, IAS 16, IAS 24 and IAS 38) with a view to removing inconsistencies and clarifying wording (effective for annual periods beginning on or after July 1, 2014);
- Amendments resulting from Annual Improvements 2011-2013 Cycle issued in December 2013 (IFRS 1, IFRS 3, IFRS 13 and IAS 40) with a view to removing inconsistencies and clarifying wording (effective for annual periods beginning on or after July 1, 2014); and
- IFRIC 21 “Levies” (effective for annual periods beginning on or after January 1, 2014).

NOTES TO THE FINANCIAL STATEMENTS

2. BASIS OF PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS AND ACCOUNTING CONVENTION (Continued)

2.2. Application and Impact of the New and Revised IFRS (Continued)

Standards and Interpretations in Issue not yet adopted (Continued)

The Bank's management has elected not to adopt these standards, revisions and interpretations in advance of their effective dates. The management anticipates that the adoption of these standards, revisions and interpretations will have no material impact on the financial statements of the Bank in the period of initial application.

2.3. Basis of Preparation and Presentation of the Financial Statements

The accompanying financial statements have been prepared at cost (historical cost) principle except for certain financial instruments measured at fair value as explained in the accounting policies provided in the following passages.

In preparing the statement of cash flows for the year ended December 31, 2013, the Bank used direct cash flow reporting method.

In the preparation of the accompanying financial statements, the Bank has adhered to the accounting policies described in Note 3 to the financial statements.

2.4. Functional Currency and the Currency of the Presentation

Financial statements are presented in convertible marks ("BAM") which are also a functional currency. The values are rounded to the nearest thousand (if not otherwise stated).

The Central Bank of Bosnia and Herzegovina (the "Central Bank") implements the policy on FX rate in line with the principle of the Currency Board, according to which BAM is pegged to EUR at the rate of BAM 1 = EUR 0.51129, which was used for 2013 and 2012.

3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies presented hereinafter have been consistently applied for all years presented.

3.1. Interest Income and Expenses

Interest income and expenses are recognized in the statement of comprehensive income as they accrue for all interest-bearing instruments using the effective interest rate method, i.e. in accordance with the rate that discounts the estimated cash flows to their net present value during the respective contract term.

The effective interest rate is the rate that precisely discounts the estimated future cash disbursement or payment through the expected duration of the financial instrument or, where appropriate, a shorter period, on the net carrying value of financial assets or financial liabilities. When calculating the effective interest rate, the Bank performs an assessment of cash flows, taking into consideration all conditions of the agreement related to the financial instrument, but not considering future loan losses.

The calculation includes all fees and commissions paid and received, which are a constituent part of the effective interest rate, transaction costs and all other premiums and discounts. Such income and expenses are presented as interest income and interest expenses in the statement of comprehensive income.

Interest income and expenses recognized in profit or loss include:

- Interest on financial assets and financial liabilities that are measured at amortized cost calculated using the effective interest rate method.
- Interest on debt securities available for sale calculated using the effective interest rate method.

3.2. Fee and Commission Income and Expense

Fee and commission income and expenses mainly comprise fees related to credit card transactions, the issue of guarantees and letters of credit, domestic and foreign payment transactions, foreign exchange trading, brokerage services, depository activities and other services and are recognized in the statement of comprehensive income upon performance of the relevant service.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

NOTES TO THE FINANCIAL STATEMENTS

3.3. Net Foreign Exchange Gains / Losses on Translation of Monetary Assets and Liabilities

Net FX gains / losses on translation of monetary assets and liabilities include non-realized and realized FX gains and losses of derivative financial instruments, and gains and losses upon translation of monetary assets and liabilities.

3.4. Foreign Currency

Transactions in foreign currency are translated into BAM at the exchange rate prevailing at the date of each transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated into BAM at the foreign exchange rate effective at that date. Foreign exchange differences arising on translation are recognized in the statement of comprehensive income, except in the case of differences arising on non-monetary available-for-sale financial assets, which are recognized in equity. Non-monetary assets and liabilities denominated in foreign currency measured at historical cost are translated into BAM using the exchange rate effective at the date of the transaction and are not retranslated at the reporting date.

3.5. Income Taxes

Income tax is based on taxable profit for the year and comprises current and deferred taxes.

Current Income Tax
Current income tax is the amount calculated according to the prescribed tax rate of 10% on the tax base determined in the tax return, which represents the amount of the profit before tax adjusted for the effect of reconciling income and expenses and any adjustments to the tax payable for prior years, in accordance with the tax legislation of the Republic of Srpska.

Deferred Income Taxes
Deferred taxes are calculated using the balance sheet liability method, for all temporary differences arising between the tax base of assets and liabilities and their carrying value for financial reporting purposes. Deferred tax assets and liabilities are measured by using the tax rates expected to apply to taxable profit in the years in which realization or settlement of the carrying value of the assets or liabilities is expected, and on the basis of the tax rate applicable at the statement of financial position date.

The measurement of deferred tax liabilities and assets reflects the tax effects that would follow from the manner in which the Bank expects, at the statement of financial position date, to recover or settle the book value of these assets and liabilities.

Deferred tax assets and liabilities are not discounted and are classified as non-current assets and/or liabilities in the statement of financial position. Deferred tax assets are recognized only to the extent that it is probable that they could be utilized as tax relief. At each reporting date, the Bank reassesses unrecognized potential deferred tax assets and tests the carrying value of recognized deferred tax assets for recoverability.

3.6. Financial Instruments

Classification
The Bank classifies its financial instruments in the following categories: loans and receivables, available-for-sale (AFS) financial assets, financial assets and liabilities at fair value through profit or loss (FVTPL), financial assets held to maturity and other financial liabilities. Management determines the classification of financial instruments upon initial recognition and re-evaluates initial classification at each reporting date.

Loans and receivables are non-derivative financial assets with fixed or determined payment that are not quoted on an active market. Loans and receivables arise when the Bank provides money to a debtor with no intention of trading with the receivable. Loans and receivables include loans approved to and receivables due from banks and customers.

AFS financial assets are non-derivative financial assets classified as available for sale or not classified in any other category. Financial assets classified as AFS are intended to be held for an indefinite period of time, but may be sold in response to a need for liquidity or a change in interest rates, foreign exchange rates or equity prices. Assets available for sale include debt and equity securities.

Financial assets and financial liabilities at fair value through the profit or loss have two sub-categories: financial assets held for trading (including derivatives) and those designated by management as FVTPL at inception. A financial instrument is classified in this category if it is acquired or incurred principally for the purpose of selling or repurchasing it in the near term, for the purpose of short-term profit-taking, or designated as such by management.

NOTES TO THE FINANCIAL STATEMENTS

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.6. Financial Instruments (Continued)

Classification (Continued)

Financial assets held to maturity comprise debt securities that the Bank intends to hold until their maturity.

Other financial liabilities comprise all financial liabilities which are not held for trading or designated at fair value through profit or loss and include current accounts, deposit accounts and borrowings.

Recognition

Loans and receivables and other financial liabilities are recognized when disbursed to borrowers or received from lenders.

Financial assets available for sale, financial assets held to maturity and financial assets and liabilities at fair value through profit or loss are recognized as at the trading date.

Financial assets and liabilities are initially recognized at fair value increased by financial assets and financial liabilities other than classified as at fair value through profit or loss and transaction costs that are directly attributable to the acquisition or issue of the financial instruments.

Measurement

(a) Loans and Receivables

Loans and receivables are initially recognized at fair value. After initial recognition, loans and receivables are measured at amortized cost using the effective interest method, less any impairment.

(b) Available-for-Sale Financial Assets

AFS financial assets are initially measured at fair value plus transaction costs that are directly attributable to the acquisition or issue of the financial asset. Subsequent to initial recognition all AFS financial assets are measured at fair value, except for equity instruments that do not have a quoted market price in an active market, or whose fair value cannot be reliably measured, which are stated at cost, including transaction costs, less impairment, if any.

(c) Financial Assets and Financial Liabilities at Fair Value through Profit or Loss

Financial assets and liabilities carried at fair value through profit or loss are initially recognized at fair value. All transaction costs are immediately expensed. Subsequent measurement is also at fair value.

(d) Financial Assets Held to Maturity

Financial assets held to maturity are initially recognized at fair value. After initial recognition, financial assets held to maturity are measured at amortized cost using the effective interest method, less any impairment.

(e) Other Financial Liabilities

Other financial liabilities are initially measured at fair value. Subsequent to initial recognition, other financial liabilities are measured at amortized cost using the effective interest method.

Recognition of Gains and Losses on Subsequent Measurement of Financial Instruments

Interest accrued using effective interest rate is recognized in profit or loss.

Gains and losses arising from a change in the fair value of financial assets or financial liabilities at fair value through profit or loss are recognized in profit or loss. Gains and losses arising from changes in the fair value of available-for-sale monetary assets are recognized directly in other comprehensive income, until cessation of recognition or permanent impairment of these financial assets, when the corresponding amount of the accumulated effect of change in fair market value, previously recognized in other comprehensive income, is transferred to profit or loss. Foreign exchange gains and losses on AFS equity instruments are part of the fair value of these instruments and are recognized in equity. Impairment losses, interest income and amortization of premium or discount using the effective interest method on AFS debt securities are recognized in profit or loss. Dividend income on AFS equity securities is recognized in the statement of comprehensive income when the right to receive payment has been established.

NOTES TO THE FINANCIAL STATEMENTS

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.6. Financial Instruments (Continued)

Impairment of Financial Assets

The Bank reviews financial assets at each reporting date to determine whether there is objective evidence of impairment. The impairment of financial assets or a group of financial assets is recognized if there is objective evidence of impairment as the result of one or more events occurring after initial recognition, which has an influence on estimated future cash flows from the financial assets or the group of financial assets, which can be reliably estimated.

1) Loans and Receivables

The Bank regularly reviews and monitors at each reporting date whether there is objective evidence of impairment of loans and receivables as well as other financial assets.

If there is objective evidence of impairment of loans and receivables on an individual basis, the impairment loss is determined as the difference between the carrying value of the assets and the present value of the expected future cash flows discounted by the original effective interest rate of the financial assets. The carrying value of the assets is decreased by the amount of loan loss provision, and the amount of the loss is recognized in profit or loss. If loans and receivables have a variable interest rate, the discount rate represents the current effective interest rate determined by an agreement at the moment when impairment has occurred.

Financial assets, for which no impairment was recognized on an individual basis, are grouped with other financial assets with similar characteristics, which are then assessed for impairment on a group basis for any impairment that has been incurred but not yet reported ("IBNR").

If a loan cannot be collected and all legal procedures have been completed and the final amount of the loss is known, the loan is directly written off. If, in the subsequent period, the amount of impairment loss decreases and the decrease can be directly linked to an event that has occurred after the write-off, the amount written-off or the loan loss provision is then reversed and shown as income in the profit or loss. Write-off of irrecoverable receivables is performed based on the relevant decision of the Credit Committee, and in accordance with court decisions, agreements between interested parties and the Bank's assessments.

In accordance with local regulations, the Bank also calculates loan loss provisions according to the Banking Agency of the Republic of Srpska ("BARS") regulations. Loans, placements and other financial assets of the Bank are classified into categories prescribed by BARS according to the expected recoverability determined on the basis of the number of days overdue, an assessment of the debtor's financial position and the quality of the collateral. The assessed amount of specific provisions for potential losses (regulatory reserve for credit losses) is calculated applying percentages prescribed by BARS. Generic provisions are calculated at the rate of 2% according to those regulations.

If the provisions calculated in accordance with BARS regulations are higher than the impairment allowances calculated in compliance with the IFRS and the balance of regulatory reserves within equity brought forward from the previous year-end, by the end of 2013 the aforesaid difference represented the shortfall in the regulatory reserve requirement for credit losses to be covered, and was absorbed from the prior years' unallocated profits, retained earnings or other reserves formed from profit. From 2010 to 2012 transfers to regulatory reserves were made directly within equity upon the approval by the shareholders in the General Assembly Meeting, in compliance with BARS instructions.

By the new change in the regulation which has been implemented since December 31, 2013, banks in the Republic of Srpska are not obligated to form the shortfall regulatory reserves from profit; however, they are obligated to include the reserves in the calculation of the capital adequacy ratio.

The shortfall regulatory reserves in the amount of BAM 8,511 thousand that the Bank has formed based on the decisions of the General Meeting according to the Annual Accounts for 2010, 2011 and 2012, will be transferred to the other reserves which do not refer to assessment of the assets quality on the based on the decision of the General Meeting which will be made upon adoption of the Audited Financial Statements for 2013.

Within the item of regulatory reserves, the amount of BAM 3,496 thousand will still remain representing the difference between the totally calculated regulatory reserves and the impairment allowances and provisions according to IAS and IFRS methodology upon the first-time adoption of these standards in the Republic of Srpska.

NOTES TO THE FINANCIAL STATEMENTS

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.6. Financial Instruments (Continued)

1) Loans and Receivables (Continued)

In accordance with the changed regulations and the instructions received from BARS, the Bank presented the change in equity within the BARS financial statements as at December 31, 2013, and the implementation of the change in the business books and IFRS financial statements will be performed upon making the Decision on distribution of 2013 profit and the transfer of a portion of regulatory reserves into the other reserves at the next General Assembly Meeting.

2) Available-for-Sale Financial Assets

At each reporting date, the Bank reviews whether there is objective evidence of impairment of individual financial assets or groups of financial assets.

In the case of equity investments classified as available for sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exist for the available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognized in profit or loss, is removed from other comprehensive income and recognized in profit or loss.

If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in profit or loss, the impairment loss is reversed through the statement of comprehensive income. However, any additional increase of the fair value of debt instruments available for sale, whose value was previously impaired, is recognized directly in other comprehensive income.

3) Financial Assets Held to Maturity

Impairment losses are recognized as the difference between the carrying value of the financial assets and the present value of expected future cash flows discounted by current market interest rates for similar financial assets. Impairment losses on these instruments, recognized in profit or loss, are not subsequently reversed through profit or loss.

Derecognition

A financial asset is derecognized (in full or in part) when the Bank loses control over the contractual rights over that financial asset which occurs when the rights are realized, surrendered or have expired.

Available-for-sale financial assets, financial assets and liabilities at fair value through profit or loss and financial assets held to maturity are derecognized on the trading date.

Loans and receivables and other financial liabilities are derecognized at the date that they are transferred by the Bank or when the liability ceases to exist.

The Bank derecognizes financial liabilities only when the financial liability ceases to exist, i.e. when it is discharged, cancelled or has expired. If the contractual terms of a financial liability change, the Bank will cease recognizing such a liability and will instantaneously recognize a new financial liability, with new terms and conditions.

Fair Value Measurement Principles

The fair value of derivatives traded in regulated markets is estimated at the amount of inflow / outflow that the Bank would receive or pay to terminate the contract at the statement of financial position date taking into account current market conditions and the current creditworthiness of the counterparties.

The fair value of government bonds classified as available for sale that are traded on an active market is based on closing bid prices at the reporting date for these securities. If the market for a financial asset is not active, the Bank determines the fair value by using internally adopted valuation techniques.

NOTES TO THE FINANCIAL STATEMENTS

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.6. Financial Instruments (Continued)

Specific Instruments

a) Financial Derivatives

The Bank uses derivative financial instruments to hedge economically its exposure to foreign exchange and interest rate risks arising from operating, financing and investing activities. The Bank does not hold or issue derivative financial instruments for speculative trading purposes.

Financial derivatives include foreign exchange forward and swap contracts, which are both initially and subsequently recognized at fair value. Market values are obtained by applying various assessment techniques, including discounted cash flow models.

All derivatives are presented as financial assets when their fair value is positive and as financial liabilities when it is negative. Changes in the fair value of financial derivatives are recorded as gains or losses.

b) Cash and Cash Equivalents

Cash and cash equivalents include: cash, cheques in the process of collection and cash deposited with the Central Bank (in excess of the amount of the obligatory reserve).

c) Obligatory Reserve with Central Bank

The minimum obligatory reserve with Central Bank is presented separately and represents the amount of the funds that the Bank is obligated to realize during each decade as the average daily balance on the reserves account, and which is determined based on the prescribed percentages from the average daily balance of the appropriate type of deposits in the previous decade (Note 17).

d) Loans and Advances to Banks are measured at amortized cost less impairment losses. Funds on held accounts of the other banks are also included in the loans and advances to banks.

e) Loans to Customers

Loans to customers are presented net of impairment allowances to reflect the estimated recoverable amounts.

f) Equity Securities

Equity securities are classified as available-for-sale financial assets and are carried at fair value, unless there is a reliable measure of the fair value, in which case they are stated at cost, less any impairment.

g) Debt Securities

Debt securities are classified as available-for-sale financial assets and financial assets held to maturity depending on the purpose for which those debt securities were acquired.

h) Current Accounts and Deposits from Banks and Customers

Current accounts and deposits are classified as other liabilities and are initially measured at fair value less transaction costs and subsequently stated at their amortized cost using the effective interest method.

i) Borrowings

Interest-bearing borrowings are classified as other liabilities and are recognized initially at fair value less transaction costs and subsequently stated at amortized cost on an effective interest rate basis.

j) Financial Guarantees and Loan Commitments

Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss incurred because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. Financial guarantee liabilities are initially recognized at their fair value, and the initial fair value is amortized over the life of the financial guarantee. The guarantee liability is subsequently carried at the higher of this amortized amount and the present value of any expected payment (when a payment under the guarantee has become probable).

Loan commitments are firm commitments to approve loans under pre-specified terms and conditions.

NOTES TO THE FINANCIAL STATEMENTS

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.6. Financial Instruments (Continued)

Offsetting of Financial Instruments

Financial assets and liabilities are offset and the net amount is reported in the statement of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted by the accounting regulations, or for gains and losses arising from a group of similar transactions such as within the Bank's trading activity.

3.7. Property and Equipment

(a) *Recognition and Measurement*

Property and equipment are tangible assets that are held for use in the supply of services or for other administrative purposes. Property and equipment are presented at historical or assumed purchase cost less accumulated depreciation and impairment losses. The historical cost includes the costs directly related with property acquisition.

Equipment is measured at cost less accumulated depreciation and impairment.

Subsequent Costs

Cost includes the invoiced amount of purchased assets increased by all costs incurred until the moment of placing the new assets into use. Subsequent costs are included in the book value of the asset or recognized as a separate asset, as appropriate, only when it is probable that the Bank will have future economic benefits from this asset and the value of this asset can be reliably measured. All other repair and maintenance costs are charged to the statement of comprehensive income during the period in which they are incurred.

(b) *Depreciation*

Depreciation is calculated for all assets, except land and assets not yet placed into use, on a straight line basis in order to write off the acquisition cost tover their estimated useful life.

The remaining value of assets and estimated useful life are reviewed at each reporting date.

Profit or loss on the disposal of assets is determined as the difference between the sales proceeds and net book value and is recorded within other operating income or other operating expenses.

Depreciation rates for property and equipment are set out below:

	2013	**2012**
Buildings	2% - 5%	2% - 5%
Electronic equipment	15.5% - 25%	15.5% - 25%
Office furniture and equipment	12.5% - 20%	12.5% - 20%
Other	12.5% - 25%	12.5% - 25%
Leasehold improvements	16.7% - 20%	16.7% - 20%

3.8. Intangible assets

Intangible assets are measured at cost less accumulated amortization and impairment. Cost includes all costs directly attributable to the acquisition of the asset.

Intangible assets, with the exception of intangible assets in progress, are amortized on a straight line basis over their estimated useful economic life. Useful life is reviewed and adjusted, if necessary, at each reporting date.

Amortization rates for intangible assets are set out below:

	2013	**2012**
Intangible investments – software and licenses	20%-25%	20%-25%

NOTES TO THE FINANCIAL STATEMENTS

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.9. Impairment of Non-Financial Assets

The net carrying values of intangible assets in progress and intangible assets with an indefinite useful life, are tested for impairment and their recoverable amounts are estimated whenever there are indications that their carrying amounts may not be recoverable, or at least annually.

The net carrying value of other non-financial assets of the Bank (other than deferred tax assets) are tested for impairment at each statement of financial position date in order to determine whether there are circumstances indicating impairment. If the existence of such indications is established, the recoverable amount is estimated. An impairment loss is recognized in the statement of comprehensive income whenever the carrying amount of an asset exceeds its recoverable amount.

The recoverable amount of a non-financial asset is the higher of the asset’s fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

For assets not generating mostly independent cash flows, their recoverable amount is determined together with that of cash generating assets, with which those assets are linked.

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset’s carrying amount does not exceed the carrying amount that would have been determined, considering amortization, if no impairment loss had been recognized.

3.10. Provisions

Provisions are recognized when the Bank has a present legal or constructive obligation as a result of past events, if it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made, or as required by law in the case of provisions for unidentified losses on off-balance-sheet credit risk exposures in accordance with regulations.

Provisions for liabilities and charges are maintained at the level that the Bank's management considers sufficient for absorption of losses. The management determines the sufficiency of provisions on the basis of insight into specific items, current economic circumstances, risk characteristics of certain transaction categories, as well as other relevant factors. Provisions are released only for such expenditure in respect of which provisions were recognized at inception. If the outflow of economic benefits to settle the obligations is no longer probable, the provision is reversed.

3.11. Equity

Share Capital

Share capital comprises ordinary shares and is stated in BAM at nominal value.

Statutory Reserves

Statutory reserves are derived from the distribution of net profit from prior years.

According to the Companies Act, upon allocation of profit according to the annual accounts, shareholding companies in the Republic of Srpska are required to allocate a minimum of 5% of their annual profit to statutory reserves, until the amount of such reserves reaches the level of 10% of the shareholding company’s share capital. The Law has not defined the deadline until which the shareholding companies are supposed to form the amount of reserves of at least 10% of the share capital.

Share Premium

Share premium represents the accumulated positive difference between nominal value of the issued shares and the paid-in amount.

Regulatory Reserve for Credit Losses

As explained in Note 3.6, in the future, regulatory reserve for loan losses will represent the positive difference between the general and special provisions calculated in accordance with BARS regulations and the value impairment and provisions calculated in accordance with the IFRS requirements as at January 1,.2010, i.e. the initial balance as at the date of the first-time adoption of IFRS in the Republic of Srpska.

NOTES TO THE FINANCIAL STATEMENTS

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.11. Equity (Continued)

Regulatory Reserve for Credit Losses (Continued)

Positive difference between the calculated regulatory reserves and the impairment and provisions calculated in accordance with the IFRS requirements and the initial balance of regulatory reserves as at future reporting dates, will represent the shortfall regulatory reserves that will not be formed, however, they will be included as the deductible item from net capital when calculating the capital adequacy ratio.

Fair Value Reserve

The fair value reserve represents the change in the fair value of AFS financial assets, net of related deferred taxes.

Dividends

Dividends on ordinary shares are recognized as a liability in the period in which they are approved by the Bank's shareholders.

Retained Earnings and Revaluation Reserves

Retained earnings include retained and unallocated earnings that can be allocated in the ensuing future period.

3.12. Off-Balance-Sheet Commitments and Contingent Liabilities

In the ordinary course of business, the Bank enters into credit-related commitments which are recorded off balance sheet and primarily comprise guarantees, letters of credit, undrawn frame loan commitments and credit card limits. Such financial commitments are recorded in the Bank's statement of financial position if and when they become payable.

3.13. Managed Funds

The Bank manages funds for and on behalf of third parties. These amounts do not constitute part of the Bank's assets, and, therefore, they are excluded from the statement of financial position. The Bank receives fee income for providing these services and does not bear any credit risk.

3.14. Segment Reporting

A business segment represents a part of assets, liabilities and business activities (products and services) which is subject to risks and benefits different from those in other business segments. A geographic segment generates products or services within a specific economic environment which are subject to risks and benefits different from those operating in other economic environments.

The Bank has identified three main segments: Retail, Corporate and Investment Banking and Other.

Basic information per segment is based on the internal reporting structure for business segments. Segment results are measured applying an internal funding price (Note 5).

3.15. Employee Benefits

a) Employee Salaries

Gross salary costs and mandatory social security contributions are charged to profit or loss as incurred. For defined contribution plans, the Bank pays contributions in the prescribed amounts to obligatory pension funds managed by state-owned management companies. These contributions are recognized as personnel costs in profit or loss as they accrue.

b) Jubilee Awards

The Bank pays out jubilee awards to its employees. The liabilities thereof are estimated using the projected unit credit method. The projected unit credit method takes into consideration each year of sevice with the Bank, where the sum of all the particular units is the final liability which is measured individually for each unit. Liabilities are measured at present values of estimated future cash flows discounted at an econometrically modelled interest rate, which is more adequate in the existing market conditions than the interest rate on Government long-term debt securities. Jubilee awards are paid out in the amount of one average salary paid bythe Bank in the month preceding the payment for the completion of 20 years of service, or two average salaries of the Bank for the completion of 30 years of service with the Bank.

NOTES TO THE FINANCIAL STATEMENTS

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.15. Employee Benefits (Continued0

c) Retirement Benefits

In accordance with internal regulations on salaries, the Bank pays retirement benefits to employees upon retirement in the amount of two average monthly salaries of the vesting employee. Calculation of long-term provisions for employee retirement benefits is performed annually by a certified actuary using the projected unit credit method. The projected unit credit method takes into consideration each year of employment with the Bank, where the sum of all the particular units is the final liability which is measured individually for each unit. Liabilities are measured at present values of estimated future cash flows discounted at an econometrically modeled interest rate, which is more adequate in the existing market conditions than the interest rate on Government long-term debt securities.

3.16. Dividend Income

Dividend income is recognized in the profit or loss when the right to receive dividends has been established.

3.17. Earnings per Share

The Bank publishes basic and diluted earnings per share (EPS) data. Basic EPS are calculated by dividing the profit or loss attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the period.

3.18. Leases

Leases in terms of which the Bank as a lessee assumes substantially all the risks and rewards of ownership are classified as finance leases. At the reporting date, the Bank had no finance leases. All other leases are classified as operating leases. Payments made under operating leases are recognized in the profit or loss on a straight-line basis over the term of the lease.

3.19. New Standards and Interpretations

Several new and amended standards and interpretations issued by the International Accounting Standards Board (IASB) and its International Financial Reporting Interpretations Committee (IFRIC) have been authorized for issue but are not applicable to entities reporting under IFRS for period ended December 31, 2013, and have not been applied in preparation of these financial statements.

IFRS 9 *Financial Instruments* (the final version of which has not yet been adopted and IASB has an active ongoing project in respect of certain changes related to classification and measurement as well as inclusion of certain new requirements related to impairment and hedge accounting), which replaces IAS 39 *Financial Instruments: Recognition and Measurement*, is effective for annual periods beginning on January 1, 2015; early adoption is permitted. This standard introduces significant changes with respect to the classification and measurement of financial assets. The Bank has not yet decided on the date of the initial application of the new standard nor has it analyzed the effects of its application.

IFRS 13 Fair Value Measurement is mandatory for financial statements for periods beginning on January 1, 2013, and represents the unique source of fair value measurement guidelines contained currently in various standards. Apart for certain limited exceptions, IFRS 13 is used whenever fair value measurement or fair value disclosure are either required or permitted in accordance with the other IFRSs. The Bank has applied IFRS 13 since January 1, 2013 and presented the effects thereof in these statements (Note 37).

4. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGMENTS

The Bank makes estimates and assumptions about uncertain events, including estimates and judgments about the future. Such accounting assumptions and estimates are regularly evaluated and based on historical experience and other factors such as: expected course of future events that can be realistically assumed in the existing circumstances, but in spite of this, necessarily represent sources of uncertainty.

The estimation of impairment losses in the Bank's loan portfolio represents the major source of estimate uncertainty. This and other key sources of estimate uncertainty that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are described below.

a) Impairment Losses on Loans and Receivables

The Bank monitors the creditworthiness of its customers on an ongoing basis. The need to impair the Bank's on and off-balance sheet exposure to credit risk is assessed on a monthly basis.

NOTES TO THE FINANCIAL STATEMENTS

4. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGMENTS (Continued)

a) Impairment Losses on Loans and Receivables (Continued)

Impairment losses are recognized mainly against the carrying value of loans to corporate and retail customers (Note 20) and as provisions for liabilities and costs arising from off-balance sheet exposure to customers, mainly in the form of guarantees and letters of credit (Note 27).

Impairment losses are also considered for credit risk exposures to banks and for other assets not carried at fair value, where the primary risk of impairment is not credit risk.

Financial Assets Carried at Amortized Cost

The Bank assesses impairment on an individual basis for all exposures where there is objective evidence of impairment. Assets which are not significant are assessed on a group (portfolio) basis for impairment.

The Bank estimates impairment losses in cases where it estimates that the observable data indicates the likelihood of a measurable decrease in the estimated future cash flows of the asset or portfolio of assets. Evidence includes irregular repayment or other indications of financial difficulties of borrowers, unfavorable changes in economic conditions in which the borrowers operate, and changes in the value or collectability of collateral instruments when these changes can be linked to the above-mentioned breach of terms.

	Note	**2013 BAM '000**	**2012 BAM '000**
Breakdown of impairment allowances (IFRS)			
Impairment allowance for loans to customers	*20b*	54,550	47,654
Provisions for off-balance sheet contingent liabilities	*27*	711	959
		55,261	**48,613**
Impairment allowance for interest and fee receivables		3,481	3,940
Impairment allowance for other assets	*24*	827	843
Impairment of available-for-sale financial assets		631	277
Total loans and receivables		**60,200**	**53,673**

In addition to impairment allowance calculated and recognized in accordance with IFRS, the Bank also calculates impairment in accordance with BARS regulations where the difference in relation to IFRS impairment is recognized as reserve for credit losses within equity and reserves.

The following table summarizes impairment allowances calculated in accordance with BARS regulations:

	2013 BAM '000	**2012 BAM '000**
Breakdown of impairment allowances (BARS)		
Impairment allowance for loans to customers	65,922	57,878
Provisions for off-balance sheet contingent liabilities	2,135	2,305
	68,057	**60,183**
Impairment allowance for interest and fee receivables	3,549	3,959
Impairment allowance for other assets	904	1,538
Total loans and receivables	**72,510**	**65,680**

NOTES TO THE FINANCIAL STATEMENTS

4. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGMENTS (Continued)

a) Impairment Losses on Loans and Receivables (Continued)

Regulatory reserve for credit risk requirement as of December 31:

	2013 BAM '000	2012 BAM '000
Impairment allowances under BARS	72,510	65,680
Impairment allowances under IFRS	60,200	53,673
Difference at period end	12,310	12,007
Shortfall regulatory reserves before change in regulations	(303)	
Shortfall regulatory reserves after the change in regulations		
Regulatory reserves within equity	3,496	3,496
Shortfall regulatory reserves for calculation of capital adequacy ratio	**8,814**	**8,511**

The Bank takes into consideration the combined effect of several events when assessing impairment and uses its experience in making judgments in cases where the observable data required to estimate impairment is limited.

At year-end, the gross value of specifically impaired loans and receivables (non-performing loans – NPL) and the rates of impairment loss recognized were as follows:

	2013 BAM '000			2012 BAM '000		
	Corporate	Retail	Total	Corporate	Retail	Total
Gross exposure	54,294	20,453	**74,747**	57,836	18,191	**76,027**
Impairment	30,858	16,071	**46,929**	23,009	14,821	**37,830**
Impairment rate	56.8%	78.6%	**62.8%**	39.8%	81.5%	**49.8%**

An increase in the impairment rate of 1 percentage point of the gross non-performing exposure presented above as at December 31, 2013, would lead to the recognition of an additional impairment loss of BAM 747.5 thousand (2012: BAM 760.3 thousand).

In addition to separately identified losses for NPLs on an individual and portfolio basis, as explained in the paragraph above, the Bank also recognizes impairment losses which are known to exist at the reporting date, but which have not yet been specifically recognized (IBNR, portfolio impairment).

The amount of IBNR as at December 31, 2013 assessed on a portfolio basis amounted to BAM 7,621 thousand (2012: BAM 9,824 thousand) of the relevant on and off-balance sheet exposure. Total IBNR provision amounted to 1.2% (2012: 1.7%) of net loans to customers.

b) Taxation

The Bank provides for tax liabilities in accordance with the tax regulations of the Republic of Srpska and Bosnia and Herzegovina. Tax returns are subject to the approval of the tax authorities which are entitled to carry out subsequent inspection of taxpayers' records.

NOTES TO THE FINANCIAL STATEMENTS

4. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGMENTS (Continued)

c) Regulatory Requirements

The Banking Agency of the Republic of Srpska is authorized to perform regulatory inspection of the Bank's operations and to request adjustments to the carrying values of assets and liabilities, in accordance with the underlying regulations.

d) Litigation

The Bank performs an individual assessment of all court cases and creates provisions in accordance with the assessment. The assessment is carried out by a special Commission of three members, two of whom are employed in the Bank's Legal Affairs, and one in the Workout Department. Proposals on provisions after the assessment are verified by the managers of Legal Affairs and Risk Management, and the decision on creating the provisions is made by the Bank's Management Board.

28 lawsuits were instigated against the Bank with damage claims filed. According to decision of the Bank Management Board, at the proposal of the Commission for risk assessment of liabilities for litigations against the Bank, for the suits that the Bank believes could be lost or significant costs may be incurred thereof, provisions were formed in the total amount of BAM 1,796 thousand (2012: BAM1,239 thousand) , out of which, the amount of BAM 299 thousand (2012: BAM 210 thousand) is related to labor suits, and BAM 1,497 thousand (2012: BAM 1,029 thousand) to other legal suits.(Note 28).

f) Comparative Financial Information

In order to achieve consistency of the disclosures in the current reporting period, certain reclassifications of comparative financial information were made for 2012, as explained below. The stated reclassifications do not affect the result and equity of the Bank.

Statement of Comprehensive Income

- The realized FX changes in the amount of BAM 1,877 thousand were transferred from "Fee and commission income" (Note 8) to the position: "Net foreign exchange gains / losses upon translation of monetary assets and liabilities (Note 10).

NOTES TO THE FINANCIAL STATEMENTS

5. SEGMENT REPORTING

Segments recognized for the purposes of segment reporting comprise the following:

1. “Retail”: private individuals and small entrepreneurial businesses
2. “Corporate and Investment Banking”: large and medium-sized companies, state and public sector
3. “Other”: capital and reserves, Assets and Liability Management, other centralized services and other assets and liabilities not associated with other segments.

Segmental information is presented in accordance with management reports.

When measuring business results internal funding prices are applied based on specific prices, reflecting currencies and maturities with embedded additional adjustments.

The methodology for allocation of revenues and costs to segments is consistent with the previous year.

Statement of Comprehensive Income by Segment

2013	**Corporate and Investment Banking BAM ’000**	**Retail BAM ’000**	**Other BAM ’000**	**Total BAM ’000**
Net interest income	13,774	21,319	8,446	43,539
Net fee and commission income	3,137	8,385	(393)	11,130
Dividend and equity income	-	-	13	13
Net foreign gains / losses on translation of monetary assets and liabilities	614	756	-	1370
Total operating income	**17,525**	**30,461**	**8,066**	**56,052**
Total operating expenses	**(5,451)**	**(23,639)**	**-**	**(29,090)**
Profit before impairment and provisions	**12,074**	**6,822**	**8,066**	**26,962**
Net impairment losses / gains and provisions for credit risk	(7,749)	(211)	-	(7,960)
Provisions for risks and costs	(450)	(97)	(25)	(572)
Impairment losses on property and equipment	-	-	42	42
Profit before tax	**3,875**	**6,514**	**8,083**	**18,472**
Income tax expense	-	-	(1,655)	(1,655)
Profit for the year	**3,875**	**6,514**	**6,428**	**16,817**
Other comprehensive income				
Net change in fair value reserves	-	-	(343)	(343)
Total comprehensive income for the year	**3,875**	**6,514**	**6,085**	**16,474**

NOTES TO THE FINANCIAL STATEMENTS

5. SEGMENT REPORTING (Continued)

Statement of Comprehensive Income by Segment

2012	Corporate and Investment Banking BAM '000	Retail BAM '000	Other BAM '000	Total BAM '000
Net interest income	10,007	22,841	7,108	39,956
Net fee and commission income	2,935	8,011	(253)	10-693
Dividend and equity income	-	-	-	-
Net foreign exchange gains / losses on translation of monetary assets and liabilities	1,208	852	-	2,060
Total operating income	**14.150**	**31.704**	**6.855**	**52.709**
Total operating expenses	**(5.466)**	**(23.382)**	**-**	**(28.848)**
Profit before impairment and provisions	**8.684**	**8.322**	**6.855**	**23.861**
Net impairment losses / gains and provisions for credit risk	(3,819)	(3,316)	-	(7,135)
Provisions for risks and costs	-	-	(333)	(333)
Impairment losses on property and equipment	-	-	(919)	(919)
Profit before tax	**4,865**	**5,006**	**5,603**	**15,474**
Income tax expense	-	-	(1,634)	(1,634)
Profit for the year	**4,865**	**5,006**	**3,969**	**13,840**
Other comprehensive income				
Net change in fair value reserves	-	-	69	69
Total comprehensive income for the year	**4,865**	**5,006**	**4,038**	**13,909**

NOTES TO THE FINANCIAL STATEMENTS

5. SEGMENT REPORTING (Continued)

Statement of Financial Position by Segment

2013	Corporate and Investment Banking BAM '000	Retail BAM '000	Other BAM '000	Total BAM '000
Assets				
Cash and cash equivalents	-	-	41,412	41,412
Obligatory reserve with the Central Bank	-	-	40,975	40,975
Loans and receivables due from banks	-	-	97,659	97,659
Financial assets available for sale	53,868	-	15,322	69,190
Loans and receivables from customers	333,869	338,063	-	671,932
Financial assets held to maturity	105	-	-	105
Property and equipment	-	-	17.049	17.049
Intangible assets	-	-	3.039	3.039
Other assets	-	-	2.575	2.575
Deferred tax assets	-	-	54	54
Total assets	**387,842**	**338,063**	**218,085**	**943,990**
Liabilities				
Deposits and loans due to banks	-	-	252,028	252,028
Deposits and loans due to customers	286,256	246,625	-	532,881
Other liabilities	-	-	-	-
Provisions for liabilities and costs	-	-	12,416	12,416
Current income tax expense	-	-	2,088	2,088
Deferred income tax expense	-	-	264	264
Total liabilities	**286,256**	**246,625**	**266,796**	**799,677**
Share capital and reserves	-	-	127,496	127,496
Net profit for the year	3,874	6,514	6,429	16,817
Total equity	**3,874**	**6,514**	**133,925**	**144,313**
Total liabilities and equity	**290,129**	**253,139**	**400,722**	**943,990**

NOTES TO THE FINANCIAL STATEMENTS

5. SEGMENT REPORTING (Continued)

Statement of Financial Position by Segment

2012	Corporate and Investment Banking BAM '000	Retail BAM '000	Other BAM '000	Total BAM '000
Assets				
Cash and cash equivalents	-	-	47,177	47,177
Obligatory reserve with the Central Bank	-	-	36,854	36,854
Loans and receivables due from banks	-	-	135,765	135,765
Financial assets available for sale	46,007	-	9,721	55,728
Loans and receivables due from customers	277,347	330,508	-	607,855
Financial assets held to maturity	170	-	-	170
Property and equipment	-	-	17,839	17,839
Intangible assets	-	-	4,658	4,658
Other assets	-	-	5,593	5,593
Deferred tax assets	-	-	19	19
Total assets	**323,524**	**330,508**	**257,626**	**911,658**
Liabilities				
Deposits and loans due to banks	-	-	289,399	289,399
Deposits and loans due to customers	262,309	220,496	-	482,805
Other liabilities	-	-	-	-
Provisions for liabilities and costs	-	-	24,544	24,544
Current income tax expense	-	-	1,473	1,473
Deferred income tax expense	- -	- -	354 243	354 243
Total liabilities	**262,309**	**220,496**	**316,013**	**798,818**
Share capital and reserves	-	-	99,000	99,000
Net profit for the year	4,866	50,116	3,963	13,840
Total equity	**4,866**	**50,116**	**102,963**	**112,840**
Total liabilities and equity	**267.175**	**270.612**	**418.976**	**911.658**

Notes set out on pages 6 to 70 form an integral part of these financial statements

NOTES TO THE FINANCIAL STATEMENTS

6. INTEREST INCOME

a) Analysis by source:

	2013 BAM '000	2012 BAM '000
Retail customers	26,884	27,441
Corporate customers and entrepreneurs	14,572	15,174
Banks and financial institutions	52	160
Public sector	13,116	7,184
	54,624	**49,959**

b) Analysis by product

	2013 BAM '000	2012 BAM '000
Loans to customers	50,288	46,321
Loans and advances to banks	32	135
Obligatory reserve with the Central Bank	20	25
Debt securities	4,284	3,478
	54,624	**49,959**

7. INTEREST EXPENSES

a) Analysis by recipient:

	2013 BAM '000	2012 BAM '000
Retail customers	3,490	2,842
Corporate customers and entrepreneurs	2,517	2,274
Banks and other financial institutions	2,501	3,080
Public sector	1,019	925
Other organizations	1,558	882
	11,085	**10,003**

b) Analysis by product:

	2013 BAM '000	2012 BAM '000
Current accounts and deposits - retail	3,490	2,842
Current accounts and deposits - corporate	2,178	1,709
Current accounts and deposits - banks	2,016	2,093
Borrowings	1,843	2,477
Other	1,558	882
	11,085	**10,003**

NOTES TO THE FINANCIAL STATEMENTS

8. FEE AND COMMISSION INCOME

	2013 BAM '000	2012 BAM '000
Domestic payment transactions	4,775	4,647
Foreign payment transactions	1,444	1,423
Payment of foreign pensions and remittances of individuals	1,493	1,670
Issuance of guarantees and other sureties	1,084	1,077
Card operations	1,035	853
Loan origination fees	426	275
Foreign exchange spot trading gains and cash operations	777	546
Other	1,515	1,310
	12,549	**11,801**

9. FEE AND COMMISSION EXPENSES

	2013 BAM '000	2012 BAM '000
Domestic payment transactions	192	192
Foreign payment transactions	71	67
Guarantees and letters of credit received	17	16
Card operations	546	506
Loan fees payable	14	24
Cash operations	498	298
Other	81	5
	1,419	**1,108**

10. DIVIDEND AND EQUITY INTEREST INCOME

	2013 BAM '000	2012 BAM '000
Dividend income	13	-
	13	**-**

11. NET FOREIGN EXCHANGE GAINS / LOSSES UPON TRANSLATION OF MONETARY ASSETS AND LIABILITIES

	2013 BAM '000	2012 BAM '000
Foreign exchange gains	103,354	38,680
Foreign exchange losses	(101,984)	(36,620)
	1,370	**2,060**

NOTES TO THE FINANCIAL STATEMENTS

12. PERSONNEL EXPENSES

	2013 BAM ’000	2012 BAM ’000
Fixed payments – gross salaries	11,296	11,249
Variable payments - bonuses	1,000	1,000
Other personnel costs	581	490
Severance and retirement benefits	592	593
Other costs	158	190
Total personnel expenses	**13,627**	**13,522**

Personnel expenses include contributions for pension and disability insurance paid in 2013 in the amount of BAM 2,361 thousand (2012: BAM 2,320 thousand).

13. OTHER EXPENSES

	2013 BAM ’000	2012 BAM ’000
IT and telecommunications	3,148	3,285
Sundry operational expenses	1,980	1,995
Utilities	1,727	1,809
Security and money transportation	1,200	1,323
Production services	1,044	1,056
Cost of materials	487	487
Advertising, marketing & promotions	695	332
Indirect taxes and contributions	303	244
Other operating expenses	354	319
	10,938	**10,850**

14. NET IMPAIRMENT LOSSES AND PROVISIONS FOR CREDIT RISK

	2013 BAM ’000	2012 BAM ’000
Loans and receivables due from customers (Note 20)	8,213	6,704
Other assets (Note 24)	(5)	(1)
Off-balance sheet items (Note 27)	(248)	432
	7,960	**7,135**

NOTES TO THE FINANCIAL STATEMENTS

15. PROVISIONS FOR RISKS AND CHARGES

	2013 BAM '000	2012 BAM '000
Costs of provisions for litigations	572	333
	572	**333**

16. INCOME TAXES

Income tax charged to the profit and loss comprises current and deferred taxes.

a) Income tax expense recognized within the profit and loss

	2013 BAM '000	2012 BAM '000
Current income tax expense	1,899	1,634
Deferred income tax expense (Note 29)	(244)	-
Total	**1,655**	**1,634**

b) Reconciliation of income tax expense

	2013 BAM '000	2012 BAM '000
Profit before tax	18,472	15,474
Income tax at the rate of 10%	1,847	1,547
Income not subject to taxation	(455)	(415)
Impairment losses on loans and other assets and other expenses not deductible for tax purposes	643	829
Incremental effect of impairment losses on loans and other assets deductible for tax purposes at 20% of the adjusted tax base	(380)	(327)
Income tax expense	**1,655**	**1,634**
Average effective income tax rate	**9.0%**	**10.6%**

Tax regulations stipulate that for the purpose of calculation of the tax base, a maximum of 20% of the adjusted tax base (result for the period), which represents the difference between adjusted income and expenses before impairment of loans and other assets, may be taken as a taxable deductible expense in respect of charges for the impairment of loans and other assets.

Tax liabilities are recognized in accordance with the tax return prepared by the Bank. However, the tax position of the Bank is subject to subsequent inspection by the tax authorities in the five year period following the year for which the tax return was issued. The Bank's Management Board is not aware of any circumstances which may give rise to a potential material liability in this respect.

NOTES TO THE FINANCIAL STATEMENTS

17. CASH AND CASH EQUIVALENTS

	2013 BAM '000	2012 BAM '000
Cash in domestic currency	10,724	8,608
Funds with the Central Bank – gyro account	22,724	34,570
Cash in foreign currency	7,964	3,999
	41,412	**47,177**

18. OBLIGATORY RESERVE WITH THE CENTRAL BANK

	2013 BAM '000	2012 BAM '000
Obligatory reserve with the Central Bank in domestic currency	**40,975**	**36,854**

The Central Bank of Bosnia and Herzegovina (the "Central Bank") has prescribed a method for calculating and holding obligatory reserves, as well as the amount and manner of payment of fees on the amount of obligatory reserve and on the amount of funds in excess ofthe obligatory reserve held on the account with the Central Bank.

The basis for the calculation of the obligatory reserve is the average amount of deposits and borrowed funds in BAM and foreign currencies (denominated in BAM, at the exchange rate of the Central Bank valid over the calculation period).

The basis for calculation of obligatory reserve excludes:

- borrowed funds from non-residents,
- deposits and loans from governments and entities (residents) intended for development projects.

The Bank is obligated to hold at least 10% of deposits and borrowed funds with an agreed maturity date up to one year, and 7% of the deposits and borrowed funds with an agreed maturity date of over one year, with the Central Bank.

The Central Bank calculates interest on reserves as follows

- for the amount of obligatory reserves: 70% of the rate which is determined based on the weighted average interest rates earned by the Central Bank at the same period on funds invested up to one month (in 2013 this rate ranged from 0.004% to 0.128%);

- for the amount of funds above obligatory reserves requirement: 90% of the rate which is determined based weighted average interest rates earned by the Central Bank at the same period on funds invested up to one month (in 2013 this rate ranged from 0.050% to 0.165%).

19. LOANS AND RECEIVABLES DUE FROM BANKS

	2013 BAM '000	2012 BAM '000
- foreign banks	97,657	132,824
- domestic banks	2	2,941
	97,659	**135,765**

Loans to and receivables from banks include BAM 55,451 thousand (2012: BAM 77,472 thousand) of loans to and receivables from related banks.

NOTES TO THE FINANCIAL STATEMENTS

20. LOANS AND RECEIVABLES DUE FROM CUSTOMERS

a) Breakdown by product

	2013 BAM '000	2012 BAM '000
Corporate		
- in BAM	184,167	149,976
- in foreign currency	122,332	93,085
- with foreign currency clause	104,931	102,935
Total gross	**411,430**	**345,996**
Impairment allowance	(35,915)	(25,559)
	375,515	**320,437**
Retail		
- in BAM	77,834	105,335
- in foreign currency	94	102
- with foreign currency clause	238,762	206,616
Total gross	**316,690**	**312,053**
Impairment allowance	(18,635)	(22,095)
	298,055	**289,958**
Net loans	**673,570**	**610,395**
Interest receivables matured	1,308	1,370
Deferred fee income	(2,946)	(3,910)
Loans and receivables due from customers	**671,932**	**607,855**

b) Movements on impairment allowance

	Loans to corporate BAM '000	Loans to retail BAM '000	Total loans BAM '000
Balance as at January 1, 2012	**23,668**	**20,992**	**44,660**
Net loss recognized in the profit or loss (Note 14)	5,523	1,181	**6,704**
Write-offs	(3,632)	(78)	**(3,710)**
Balance as at December 31, 2012	**25,559**	**22,095**	**47,654**
Net loss recognized in the profit or loss (Note 14)	11,672	(3,459)	**8,213**
Write-offs	(1,316)	(1)	**(1,317)**
Balance as at December 31, 2013	**35,915**	**18,635**	**54,550**

NOTES TO THE FINANCIAL STATEMENTS

20. LOANS AND RECEIVABLES DUE FROM CUSTOMERS (Continued)

c) Geographic concentration of credit risk

Geographic credit risk concentration relates entirely to companies, individuals and other entities located in Bosnia and Herzegovina.

d) Concentration of credit risk by industry

The Bank's loan portfolio as at December 31, 2013 is analyzed by industry in the table below:

	2013 BAM '000	2012 BAM '000
Loans to corporate customers		
Mining and energy	3,414	3,522
Agriculture	16,894	16,767
Civil engineering	26,861	20,797
Industry	50,169	50,136
Trade	128,511	132,998
Services	3,014	3,210
Transport	11,702	8,767
Finance	1,142	1,173
Public Sector (Central Institutions)	111,500	82,500
Local self-government	53,600	20,044
Non-profit institutions	4,623	6,082
	411,430	**345,996**
Retail loans	316,690	312,053
Total gross loans	**728,120**	**658,049**
Impairment allowance	(54,550)	(47,654)
Total net loans	**673,570**	**610,395**

The structure of the loan portfolio is regularly monitored by the Risk Management Department in order to recognize potential events that could have a significant impact on the loan portfolio (usual risk factors) and, if needed, mitigate the Bank's exposure to certain industry sectors.

NOTES TO THE FINANCIAL STATEMENTS

21. FINANCIAL ASSETS

21. a) Financial assets available for sale

	2013 BAM '000	2012 BAM '000
Equity securities, quoted		
Dunav osiguranje a.d. Banja Luka	15	15
Krajina Osiguranje d.d. Banja Luka	13	13
Debt securities, quoted		
Bonds of the Municipality of Šamac	11	10
RS bonds issued by public offer	53,348	45,811
RS for verified frozen FX savings	3,676	4,598
RS Ministry of Finance Treasury Bills	11,781	4,935
Total quoted securities	**68,844**	**55,382**
Equity securities, unquoted		
Banja Luka Stock Exchange a.d., Banja Luka	237	237
Central Registry of Securities	101	101
SWIFT	8	8
Total unquoted securities	**346**	**346**
Total financial assets available for sale	**69,190**	**55,728**

Breakdown of financial assets available for sale according to fair value levels:

December 31, 2013	**Level 1 BAM 000**	**Level 2 BAM 000**	**Level 3 BAM 000**	**Total BAM 000**
Bonds of the Municipality of Šamac	-	11	-	**11**
RS bonds issued by public offer	-	53,348	-	**53,348**
RS for verified old FX savings	-	3,676	-	**3,676**
RS Ministry of Finance Treasury Bills	-	11,781	-	**11,781**
Total	**-**	**68,816**	**-**	**68,816**
December 31, 2012				
Bonds of the Municipality of Šamac	-	-	10	**10**
RS bonds issued by public offer	-	45,811	-	**45,811**
RS for verified frozen FX savings	-	4,598	-	**4,598**
RS Ministry of Finance Treasury Bills	-	4,935	-	**4,935**
Total	**-**	**55,344**	**10**	**55,354**

In 2013, Bonds of Šamac Municipality were transferred from level 3 to level 2 of fair value hierarchy.

NOTES TO THE FINANCIAL STATEMENTS

21. FINANCIAL ASSETS (Continued)

21. a) Financial assets available for sale (Continued)

External rating of debt securities

To the external rating of debt securities, the external credit rating of the state of Bosnia and Herzegovina was applied, which according to the Agency for Credit Rating Standard & Poor's was "B / stable", and according to Moody's Investors Service was "B3 / stable ."

21. b) Financial assets held to maturity

	2013 BAM '000	2012 BAM '000
Bonds of Atlantik doo Banja Luka, quoted	105	170
Total financial assets held to maturity	**105**	**170**

NOTES TO THE FINANCIAL STATEMENTS

22. PROPERTY AND EQUIPMENT

	Land and buildings BAM '000	Equipment and other assets BAM '000	Leasehold improvements BAM '000	Investment in progress BAM '000	Total property and equipment BAM '000
Cost or appraised value					
Balance as at January 1, 2012	26,640	16,157	1,645	317	44,759
Additions	-	-	-	2,004	2,004
Transfers	27	1,864	-	(1,891)	-
Disposals and write-offs	(219)	(886)	(5)	-	(1,110)
Balance as at December 31, 2012	**26,448**	**17,135**	**1,640**	**430**	**45,653**
Balance as at January 1, 2013	26,448	17,135	1,640	430	45,653
Additions	-	-	-	1,028	1,028
Transfers	96	912	117	(1,125)	-
Disposals and write-offs	-	(325)	-	-	(325)
Balance as at December 31, 2013	**26,544**	**17,722**	**1,757**	**333**	**46,356**
Accumulated depreciation					
Balance as at January 1, 2012	10,866	13,416	1,384	-	25,666
Charge for the year	303	1,892	159	-	2,354
Impairment of assets	757	82	80	-	919
Disposals and write-offs	(238)	(881)	(6)	-	(1,125)
Balance as at December 31, 2012	**11,688**	**14,509**	**1,617**	**-**	**27,814**
Balance as at January 1, 2013	11,688	14,509	1,617	-	27,814
Charge for the year	499	1,308	11	-	1,818
Impairment of assets	-	-	-	-	-
Disposals and write-offs	-	(325)	-	-	(325)
Balance as at December 31, 2013	**12,187**	**15,492**	**1,628**	**-**	**29,307**
Net book value:					
Balance as at December 31, 2012	**14,760**	**2,626**	**23**	**430**	**17,839**
Balance as at December 31, 2013	**14,357**	**2,230**	**129**	**333**	**17,049**

Investments in progress as of December 31, 2013 in the amount of BAM 333 thousand (2012: BAM 430 thousand) represent equipment not yet placed into use.

There are no mortgage or pledge liens instituted over the Bank's property and equipment. The Bank tested the property for impairment as at December 31, 2013, and concluded that there were no reasons for recognition of impairment losses.

NOTES TO THE FINANCIAL STATEMENTS

23. INTANGIBLE ASSETS

	Software BAM '000	Other BAM '000	Investments in progress BAM '000	Total BAM '000
Cost				
Balance as at January 1, 2012	13,593	3,434	15	17,042
Additions	-	-	1,468	1,468
Transfers	201	498	(699)	-
Balance as at December 31, 2012	**13,794**	**3,932**	**784**	**18,510**
Balance as at January 1, 2013	13,794	3,932	784	18,510
Additions	-	-	1,089	1,089
Transfers	281	542	(823)	-
Sale and write-offs	-	(1)	-	(1)
Balance as at December 31, 2013	**14,075**	**4,473**	**1,050**	**19,598**
Accumulated amortization				
Balance as at January 1, 2012	8,399	3,314	-	11,713
Charge for the year	1,787	335	-	2,122
Write-offs	12	5	-	17
Balance as at December 31, 2012	**10,198**	**3,654**	**-**	**13,852**
Balance as at January 1, 2013	10,198	3,654	-	13,852
Charge for the year	2,249	458	-	2,707
Write-offs	-	-	-	-
Balance as at December 31, 2013	**12,447**	**4,112**	**-**	**16,559**
Net book value:				
Balance as at December 31, 2012	**3,596**	**278**	**784**	**4,658**
Balance as at December 31, 2013	**1,628**	**361**	**1,050**	**3,039**

Investments in progress as of December 31, 2013 in the amount of BAM 1,050 thousand (2012: BAM 784 thousand) relate to software and other intangible assets not yet placed into use.

As of December 31, 2013, the Bank had no internally generated intangible assets.

NOTES TO THE FINANCIAL STATEMENTS

24. OTHER ASSETS

	2013 BAM '000	2012 BAM '000
Accrued interest not matured	552	498
Receivables for fees in local currency	153	117
Receivables for salaries of employees from the Group	636	1 038
Receivables for salaries of employees from RS Health Insurance Fund	278	253
Receivables from card operations	1,264	929
Receivables based on cheques	268	120
Receivables from Escrow accounts for the performed payments related to out-of-court settlements	-	2,735
Other receivables	251	746
Impairment allowance	(827)	(843)
Total other assets	**2,575**	**5,593**

Movements on impairment allowance for other assets:

	Total BAM '000
Balance as at January 1, 2012	**844**
Net gains / losses recognized in P&L (Note 14)	(1)
Write-offs and transfers	-
Balance as at December 31, 2012	**843**
Net gains / losses recognized in P&L (Note 14)	(5)
Write-offs and transfers	(11)
Balance as at December 31, 2013	**827**

NOTES TO THE FINANCIAL STATEMENTS

25. DEPOSITS AND LOANS DUE TO BANKS

	2013 BAM '000	2012 BAM '000
Demand deposits		
- in BAM	15	40
- in foreign currencies	1	1
	16	**41**
Term deposits		
- in BAM	23,000	37,960
- in foreign currencies	185,022	211,230
	208,022	**249,190**
Total deposits	**208,038**	**249,231**
Loans obtained		
- Fund for Italian Participation in the Stabilization, Reconstruction and Development of the Balkans - "MCI Fund"	691	760
- European Investment Bank	43,299	39,408
Total loans	**43,990**	**40,168**
Total deposits and loans from banks	**252,028**	**289,399**

Deposits and loans due to banks include BAM 208,023 thousand due to related parties (2012: BAM 249,179 thousand).

NOTES TO THE FINANCIAL STATEMENTS

26. DEPOSITS AND LOANS UE TO CUSTOMERS

	2013 BAM '000	2012 BAM '000
Corporate		
Demand deposits		
- in BAM	115,867	124,050
- in foreign currencies	50,063	46,564
	165,930	**170,614**
Term deposits		
- in BAM	12,888	6,689
- with foreign currency clause	50,307	28,314
- in foreign currencies	10,315	12,281
	73,510	**47,284**
Total corporate	**239,440**	**217,898**
Retail		
Demand deposits		
- in BAM	75,584	69,321
- in foreign currencies	46,985	42,178
	122,569	**111,499**
Term deposits		
- in BAM	16,935	10,321
- with foreign currency clause	-	11
- in foreign currencies	77,026	71,400
	93,961	**81,732**
Total retail	**216,530**	**193,231**
Total deposits	**455,970**	**411,129**
Loans from customers		
- IRB RS Housing Fund of The Republic of Srpska	30,571	30,537
- IRB RS Fund for the Development of the Eastern Part of RS	9,663	8,314
- IRB RS Development and Employment Fund	15,485	20,339
- IRB RS World Bank Funds	1,634	2,707
- Green for Growth Fund (GGF) Amsterdam	19,558	9,779
Total loans from customers	**76,911**	**71,676**
Total deposits and loans from customers	**532,881**	**482,805**

Deposits and loans from customers include BAM 325 thousand due to related parties (2012: BAM 360 thousand).

NOTES TO THE FINANCIAL STATEMENTS

27. OTHER LIABILITIES

	2013 BAM '000	2012 BAM '000
Accrued interest, not matured	3,840	2,777
Liabilities to employees	1,455	1,343
Liabilities to suppliers	1,376	2,340
Provisions for off-balance-sheet contingent liabilities	711	959
Provisions for jubilee awards	170	198
Subscribed not paid in share capital liability	-	15,000
Liabilities for realization of payment orders in the country	197	787
Liabilities for realization of payment orders abroad	752	-
Liabilities based on brokerage operations	138	178
Liabilities based on derivative transactions	945	-
Liabilities based on deposits that were not nominated	915	-
Accruals and deferred income	999	-
Other liabilities	918	962
	12,416	**24,544**

Movements on provisions were as follows:

	Off-balance-sheet contingent liabilities BAM '000	Jubilee awards BAM '000	Total BAM '000
Balance as at January 1, 2012	**527**	**198**	**725**
Net gain / loss recognized in profit or loss	432	-	432
Balance as at December 31, 2012	**959**	**198**	**1.157**
Net gain / loss recognized in profit or loss	(248)		(248)
Provisions released during the period and transfers	-	(28)	(28)
Balance as at December 31, 2013	**711**	**170**	**881**

Charges and reversals in provisions for off-balance-sheet exposures are recognized as net impairment losses and provisions for credit risks (Note 14) and for jubilee awards as personnel expenses (Note 12) within the statement of comprehensive income.

NOTES TO THE FINANCIAL STATEMENTS

28. PROVISIONS FOR LIABILITIES AND COSTS

	2013 BAM '000	2012 BAM '000
Provisions for retirement benefits	292	234
Provisions for litigations	1,796	1,239
	2,088	**1,473**

Movements on provisions were as follows:

	Litigations BAM '000	Retirement benefits BAM '000	Total BAM '000
Balance as at January 1, 2012	**1,080**	**517**	**1,597**
Net gain / loss recognized in profit or loss (Note 15)	333	-	333
Provisions released during the period and transfers	(174)	(283)	(457)
Balance as at December 31, 2012	**1,239**	**234**	**1,473**
Net gain / loss recognized in profit or loss (Note 15)	572	58	630
Provisions released during the period and transfers	(15)	-	(15)
Balance as at December 31, 2013	**1,796**	**292**	**2,088**

29. DEFERRED TAX ASSETS AND LIABILITIES

Net deferred tax liabilities

Deferred taxes are calculated for temporary differences according to the balance sheet method using the effective tax rate of 10 % (2012: 10%). Changes in temporary differences and components of deferred tax liabilities are recognized in equity and reserves or in comprehensive income as follows:

	2013 BAM '000	2012 BAM '000
Deferred tax assets		
Fair value reserve	54	19
Deferred tax liabilities		
Fair value reserve	-	-
Reserves	-	(243)
Net deferred tax liabilities	**54**	**(224)**

NOTES TO THE FINANCIAL STATEMENTS

29. DEFERRED TAX ASSETS AND LIABILITIES (Continued

Movements on deferred taxes were as follows:

	Deferred tax assets	Deferred tax liabilities	Net deferred tax liabilities
	BAM '000	BAM '000	BAM '000
Balance as at January 1, 2012	**19**	**(247)**	**(228)**
Decrease inf deferred tax liabilities	-	(3)	(3)
Changes in fair value of financial assets available for sale recognized in equity and reserves	-	7	7
Balance as at December 31, 2012	**19**	**(243)**	**(224)**
Balance as at January 1, 2013	**19**	**(243)**	**(224)**
Decrease in deferred tax liabilities	-	243	243
Changes in fair value of financial assets available for sale recognized in equity and reserves	35	-	35
Balance as at December 31, 2013	**54**	**-**	**54**

30. SHARE CAPITAL

	Ordinary shares BAM '000
Balance as at January 1, 2012	82,055
Balance as at December 31, 2012	**82,055**
Increase in share capital through the 9th issue of shares	15,000
Balance as at December 31, 2013	**97,055**
Nominal value (BAM)	700
Number of shares	138,650

NOTES TO THE FINANCIAL STATEMENTS

30. SHARE CAPITAL (Continued)

The shareholders of the Bank as at December 31, 2013 comprise 73 domestic and foreign legal entities and individuals. As of the reporting date there wass only one shareholder holding more than 1% of the total shares:

	% of equity interest
UniCredit Bank Austria AG, Vienna	**98.37%**
Other shareholders	1.63%
	100.00%

As at December 31, 2013, members of Supervisory Board, Audit Committee and Management Board did not possess any shares in the Bank.

All the Bank shares were quoted on Banjaluka Stock Exchange. As at December 31, 2013, the price on Banjaluka Stock Exchange amounted to BAM 515 (December 31, 2012: BAM 501).

31. EARNINGS PER SHARE

	2013	2012
Total number of shares	138,650	117,221
Weighted average number of shares	136,889	117,221
Net profit in BAM '000	16,817	13,840
Basic and diluted earnings per share in BAM	122.85	118.07

32. COMMITMENTS AND CONTINGENT LIABILITIES

	2013 BAM '000	2012 BAM '000
Performance guarantees:		
- in BAM	19,508	16,881
- in foreign currencies	3,789	9,861
Other guarantees:		
- in BAM	13,902	8,494
- in foreign currencies	8,358	3,858
Contingent liabilities based on unused loans and guarantees :		
- in BAM	60,516	59,253
- in foreign currencies	152	25,020
Letters of credit in foreign currencies	355	372
Other sureties	-	2,900
Total	**106,580**	**126,639**

As at December 31, 2013, impairment allowances in respect of commitments and contingencies amounted to BAM 711 thousand (2012: BAM 959 thousand). The movements on impairment allowances are presented in Note 27.

33. TRANSACTIONS WITH RELATED PARTIES

In accordance with the effective regulations, parties related to the Bank are:

- the major shareholder and its related parties (banks and the other legal entities included in consolidated financial statements – UniCredit Group members).
- members of the Supervisory Board and Management Board of the Bank, and the members of their families, and
- legal entities under the control or significant influence of the members of the Supervisory Board and Management Board of the Bank, or members of their families.

Additionally, the Bank discloses the transactions with key management personnel, in accordance with IAS 24.

Amounts of assets and liabilities with UniCredit Group members are presented below:

	2013 BAM '000	2012 BAM '000
Assets:		
Foreign currency current accounts:		
- UniCredit Bank Austria AG, Vienna	4,084	1,689
- UniCredit Bank Serbia A.D., Belgrade	14	19
- Zagrebačka banka d.d., Zagreb	281	1,148
- UniCredit Bank AG, Munich	470	48,997
- Unicredito Italiano SpA, Milan	153	3,134
- UniCredit Bank d.d. Mostar	2	27
	5,004	**55,014**
Short term deposits:		
- UniCredit Bank Austria AG, Vienna	50,447	19,558
- UniCredit Bank d,d., Mostar	-	2,900
	50,447	**22,458**
Total assets	**55,451**	**77,472**
Liabilities:		
Short-term deposits:		
- UniCredit Bank Austria AG, Vienna	185,023	211,241
- UniCredit d.d., Mostar	23,000	37,938
Paid in share capital not subscribed		
- UniCredit Bank Austria AG, Vienna	0	15,000
Liabilities due for services delivered		
- UBIS (UniCredit Business Integrated Solutions), Vienna	62	66
- UniCredit d.d., Mostar	-	68
- Zagrebačka banka d.d., Zagreb	-	32
- UBIS (UniCredit Business Integrated Solutions), Prague	5	-
Total liabilities	**208,090**	**264,345**
Net liabilities	**(152,639)**	**(186,873)**

NOTES TO THE FINANCIAL STATEMENTS

33. TRANSACTIONS WITH RELATED PARTIES (Continued)

Amounts of income and expenses with related parties are presented below:

	2013 BAM '000	2012 BAM '000
Items included in the statement of comprehensive income:		
Interest income:		
-UniCredit Bank Austria AG, Vienna	14	100
-UniCredit bank d.d., Mostar	14	25
Total interest income	**28**	**125**
Fee and commission income:		
-UniCredit Bank Austria AG, Vienna	3	42
-UniCredit bank d.d., Mostar	6	11
Total fee and commission income	**9**	**53**
Interest expenses:		
-UniCredit Bank Austria AG, Vienna	1,817	1,925
-UniCredit bank d.d., Mostar	199	436
-ZAO UniCredit Bank, Moscow	-	136
Total interest expense	**2,016**	**2,497**
Fee and commission expenses:		
-UniCredit Bank Austria AG, Vienna	5	8
-Unicredito Italiano SPA, Milan	4	3
-Zagrebačka banka d.d., Zagreb	2	88
-UniCredit bank d.d., Mostar	-	39
- UniCredit Bank AG Munich	1	-
Total fee and commissions expenses	**12**	**138**
Software maintenance costs:		
-BTS – Banking Transaction services s.r.o., Prague	59	59
-UBIS (ex, UGIS; WAVE, BAGIS), Vienna	1,286	1,400
-UniCredit bank d.d., Mostar	240	235
Total software maintenance costs	**1,585**	**1,694**
Expenses, net	**(3,576)**	**(4,151)**

NOTES TO THE FINANCIAL STATEMENTS

33. TRANSACTIONS WITH RELATED PARTIES (Continued)

The remuneration of members of the Supervisory and Management Boards, and other key management are presented below:

	2013 BAM '000	2012 BAM '000.
Supervisory Board		
Management Board		
Short term remuneration		
Gross salaries disbursed in the current year for the current year	669	647
Bonuses disbursed in the current year for the previous year - gross	79	77
Long term remuneration		
Insurance policies paid in the current year - gross	29	30
Disbursements in the current year based on previous years - gross	29	0
Total	**807**	**754**
Other key management personnel		
Short term remuneration		
Gross salaries disbursed in the current year for the current year	914	801
Bonuses disbursed in the current year for previous year - gross	149	123
Total	**1,063**	**924**

Other key management personnel comprise 14 employees of the Bank (2012: 14 employees of the Bank).

The amount of the remuneration disbursed to members of Management Board and key management includes the amount of BAM 346 thousand (2012: BAM 302 thousand) of contributions for pension and disability insurance with the prescribed amounts of contributions, which are paid to the mandatory pension funds.

Within the regular transactions, the transactions with related persons are performed according to fair market conditions, which we consider to be 'arm's length' transactions, and our estimate is that the Bank has no risk in respect of transfer prices.

NOTES TO THE FINANCIAL STATEMENTS

33. TRANSACTIONS WITH RELATED PARTIES (Continued)

Loans and deposits, and income and expenses arising from loans and deposits of the members of the Supervisory Board, Management Board and other key management are as follows:

	2013 BAM'000	2012 BAM '000
Supervisory Board	-	-
Management Board		
- Loans as at December, 31	228	12
- Interest income for the year	*3*	-
- Deposits as at December 31	31	121
- Interest expenses for the year	-	1
Other key management		
- Loans as at December, 31	593	638
- Interest income for the year	39	45
- Deposits as at December, 31	290	239
- Interest expenses for the year	1	3
Total key management		
- Loans as at December 31	***821***	***650***
- Interest income for the year	***42***	***45***
- Deposits as at December 31	***325***	***360***
- Interest expenses for the year	***1***	***4***

34. RISK MANAGEMENT

The Bank's risk management is conducted through a system of policies, programs, work procedures and determined limits, which are continuously upgraded in accordance with changes in legislation, changes in business activities based on market trends and development of new products, as well as through the adoption of risk management standards of UniCredit Group (the "Group"). The Group has a comprehensive risk management system based on defined risk appetite, risk strategies and operative policies and procedures and established risk limits.

The Supervisory Board and Management Board of the Bank prescribe overall risk management principles and adopt risk strategies and internal acts covering business areas. In accordance with Group requirements, the Bank has implemented a standard approach to the international Basel II standard, through an IT platform, which is aligned with the requirements of this standard.

Risk management is organized into organizational units within the competence of the Chief Risk Officer:

1. Underwriting, responsible *inter alia* for credit fraud prevention
2. Credit Risk Monitoring
3. Special Credit Management
4. Risk Controlling with the function of collateral management
5. Market Risk Management
6. Operational Risk Management

Within Special Credit Management there are three departments: Restructuring, Workout and Retail Collection Center.

The most significant types of risk to which the Bank is exposed are credit risk, market risk and operational risk.

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.1. Credit Risk

The Bank is exposed to credit risk that can be defined as the possibility that a debtor may default on the liabilities defined in its loan agreements, which results in financial loss for the Bank. The assumption of credit risk is managed in accordance with the specific rules and principles defined by the Group for areas of credit strategies, policies, models development, risk concentration, new products introduction, monitoring and reporting. Credit risk exposure is managed in accordance with the Bank's strategies and policies in force, as well as the other internal acts prescribed by the Supervisory Board and the Management Board. Credit risk strategies define the main strategic goals, and determine the limits of credit risk assumption within business operations with all client segments.

General principles and rules of credit risk management have been established by the Group through a general crediting policy, which the Bank applies in its business operations in accordance with the requirements of the local regulator, group standards and best practice. General rules and principles have been defined in more detail by specified special crediting policies.

a) Credit Risk Measurement

The following factors are taken into account in credit risk measurement: risk of loss resulting from insolvency of the debtor, risk of loss resulting from a change in client risk rating, credit exposure including balance sheet and off-balance-sheet positions of the Bank and the material value of collaterals.

Credit risk is measured at the level of individual users of loans/transactions and at the level of the total portfolio.

With the support of the Group, the Bank is developing and establishing both a system of credit risk measurement on the portfolio basis applying the Basel II basic parameters of credit risk for calculation of expected loss from the loan portfolio, and the calculation of the internal capital requirements to cover potential loss because of the credit risk on the basis of calculation of loan value at risk (VaR). As the measure of economic / internal capital, loan VaR is also the basic input for defining crediting strategies, analysis of credit limits and risk concentration.

The established system of reporting analyses the main triggers and components of credit risk and their dynamics in order to undertake corrective activities if necessary and in time. Reports contain the information about changes in the size and quality of the credit portfolio at the client segment level and for the Bank.

b) Risk Control Policies

The Bank manages, limits and controls credit risk concentrations, wherever such risk concentrations have been established, particularly with regard to specific clients and/or groups, and industry sectors.

The Bank sets the credit risk level, which it assumes by setting limits for the amount of risk accepted in relation to one borrower or group of borrowers, or industry segments. Such risks are monitored on a regular monthly basis through a report to the Credit Committee of the Bank on limits utilization.

The Credit Committee, Management Board and the Supervisory Board of the Bank are regularly informed of all significant changes in the value and quality of the portfolio.

Credit risk is also managed by the regular analysis of the ability of borrowers and potential borrowers to settle liabilities for principal repayment and interest payment, and change in credit limits where necessary.

In order to minimize the risks from lending activities, the Bank has set up policies for definition, assessment and treatment of collateral serving as security for claims collection, and as the collateral for the collection of its claims, it uses acceptable collateral. Acceptable collateral is a pledge over an asset which has a known active market and stable price, whose value is satisfactory relative to the Bank's receivables and which is sufficient to protect the Bank from possible loss of principal, interest, fees and collection costs.

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.1. Credit Risk (Continued)

34.1.1. Maximum exposure to credit risk for on and off-balance sheet items

	2013 BAM '000	2012 BAM '000
Balance sheet assets		
Cash and cash equivalents (Note 17)	41,412	47,177
Obligatory reserve with the Central Bank (Note 18)	40,975	36,854
Loans and receivables due from banks (Note 19)	97,659	135,765
Loans and receivables due from customers - corporate (Note 20)	375,515	320,437
Loans and receivables due from customers - retail (Note 20)	298,055	289,958
Accrued interest (Note 20)	1,308	1,370
Financial assets available for sale (Note 21a)	69,190	55,354
Financial assets held to maturity (Note 21b)	105	170
Other assets (Note 24)	2,575	5,593
Total balance sheet items exposed to credit risk	**926,794**	**880,071**
Off-balance sheet (Note 32)		
Guarantees and other sureties	45,912	42,366
Approved overdrafts, global loans and guarantees	60,668	84,273
Total off-balance-sheet exposure to credit risk	**105,580**	**126,639**
	1,032,374	**1,006,710**

The table represents the maximum exposure to credit risk of the Bank as at December 31, 2013 and 2012, without taking into consideration pledges or other loan security instruments. For balance sheet assets, the presented exposures are based on net carrying values. As shown in the table above, 65.2% of the total maximum exposure originates from loans to customers (2012: 60.6%), and 9.5% originates from loans to other banks (2012: 13.5 %). The Management Board believes in the Bank's ability to continue controlling and maintaining the exposure to credit risk.

The Bank takes collaterals for loans and receivables in the form of mortgages assigned over real estate, pledges liens assigned over other assets, and guarantees. Initial assessments of the value of collateral, or real estate, are performed upon loan approval, i.e., they are an integral part of the process of clients' loan request approval. Revaluations are performed in accordance with the principles and rules of the collateral management system. Collaterals are not taken in the case of loans and advances from other banks and financial assets available for sale.

In view of the impact of the general financial and economic crisis, there is considerable uncertainty related to the fair market value of such collaterals, along with the time needed to realize the sale thereof.

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.1. Credit Risk (Continued)

34.1.2. Credit risk management and policies for impairment and provisions

Impairment and impairment policies

At each reporting date, the Bank checks the existence of objective evidence of impairment of financial assets, as previously explained in Note 3.6.

For the purpose of determining impairment of loans and receivables, the Bank distinguishes two approaches

- Loans assessed on an individual basis
- Loans assessed on a group basis (generic IBNR and special provisions).

Loans assessed on an individual basis

Individually significant loans are assessed on an individual basis are all loans for objective evidence of impairment. Factors that can influence the ability and readiness of each individual debtor to fulfill their obligations toward the Bank, are as follows:

- failure to settle or delay in payment of interest or principal
- failure to comply with the contractual terms and conditions
- bankruptcy or instigation of bankruptcy proceedings
- any specific information about business difficulties (e,g, reflected in the insufficient liquidity of the customer)
- significant changes in the customer's market environment
- global economic situation.

Loans assessed on a portfolio basis ("IBNR" and special provisions)

In order to assess the impairment of loans that are not individually significant, such loans are grouped based on the similar credit risk characteristics. The Bank has segmented the loan portfolio into the risk groups based on the credit rating for corporate customers and number of days past-due for retail customers and, accordingly, applying parameters of credit risk (such as probability of default, loss given default, amount that the Bank requires in instances of non-performance of obligations) determined by Basel II and in conformity with IFRS requirements it impairs loans.

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.1. Credit Risk (Continued)

34.1.2. Credit risk management and policies for impairment and provisions (Continued)

For the purpose of credit monitoring and credit risk management, the Bank divides its credit portfolio into the following groups:

- Performing loans – loans that are neither due nor impaired
- Past due but not impaired loans
- Non-performing loans for which impairment has been recognized.

The breakdown of the loan portfolio according to the above-stated categories is presented below:

	2013			2012		
	BAM '000			BAM '000		
	Loans	**Provisions**	**%**	**Loans**	**Provisions**	**%**
Performing and past due but not impaired loans not specifically impaired						
- loans to corporate	357,136	5,057	1.4%	288,160	2,550	0.9%
- loans to retail	296,237	2,564	0.9%	293,862	7,274	2.5%
	653,373	**7,621**	**1.2%**	**582,022**	**9,824**	**1.7%**
Non-performing loans						
- loans to corporate	54,294	30,858	56.8%	57,836	23,009	39.8%
- loans to retail	20,453	16,071	78.6%	18,191	14,821	81.5%
	74,747	**46,929**	**62.8%**	**76,027**	**37,830**	**49.8%**
Total loans	**728,120**	**54,550**	**7.5%**	**658,049**	**47,654**	**7.2%**

Provision coverage of the non-performing portfolio amounts to 62.8% (2012: 49.8%).

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.1. Credit Risk (Continued)

34.1.2. Credit risk management and policies for impairment and provisions (Continued)

The table below presents the analysis of gross and net (net of impairment allowance) loans and receivables due from customers:

	2013 BAM '000	2012 BAM '000
Corporate		
Loans to customers that are neither due nor impaired	356,994	284,962
Past due but not impaired loans	142	3,198
Non-performing loans (impaired loans)	54,294	57,836
Gross exposure	**411,430**	**345,996**
***Less:* Impairment allowance:**		
- Portfolio (IBNR), individual and group impairment allowance	(35,915)	(25,559)
Net exposure	**375,515**	**320,437**

	2013 BAM '000	2012 BAM '000
Retail		
Loans to customers that are neither due nor impaired	296,174	293,802
Past due but not impaired loans	63	60
Non-performing loans (impaired loans)	20,453	18,191
Gross exposure	**316,690**	**312,053**
***Less:* Impairment allowance:**		
- Portfolio (IBNR), individual and group impairment allowance	(18,635)	(22,095)
Net exposure	**298,055**	**289,958**
Total gross exposure	**728,120**	**658,049**
Portfolio impairment allowance (IBNR)	(7,621)	(9,824)
Individual and group impairment allowance	(46,929)	(37,830)
Net exposure	**673,570**	**610,395**

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.1. Credit Risk (Continued)

34.1.2. Credit risk management and policies for impairment and provisions (Continued)

a*) Loans to customers that are neither due nor impaired*

The quality of the portfolio of loans to customers that are neither due nor impaired can be accessed through the internal standard monitoring system. Loans to customers are regularly monitored and systematically reviewed in order to identify any irregularities or warning signals. These loans are subject to constant monitoring with the aim of taking timely action based on improvement/deterioration of clients' risk profile.

An overview of gross exposure of loans to customers that are neither due nor impaired according to the type of loan is as follows:

	Retail loans				Corporate loans			
	Customer loans	Housing loans	Credit card loans and overdrafts	**Total**	Large	Medium	Small	**Total**
2013	BAM '000	BAM '000	BAM '000	**BAM '000**	BAM '000	BAM '000	BAM '000	**BAM '000**
Standard monitoring	211,942	64,634	19,598	**296,174**	268,674	54,455	33,865	**356,994**
2012								
Standard monitoring	213,738	61,626	18,438	**293,802**	204,897	49,245	30,820	**284,962**

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.1. Credit Risk (Continued)

34.1.2. Credit risk management and policies for impairment and provisions (Continued)

b) *Past due but not impaired loans*

Loans to and receivables from customers less than 90 days overdue are not considered as impaired, unless other information is available to indicate the contrary. Additionally, certain corporate loans overdue for over 90 days are also not considered impaired. The gross amount of loans to and receivables from customers that were past due but not impaired were as follows:

	Retail loans				**Corporate loans**			
2013	Customer loans	Housing loans	Credit card loans and overdrafts	**Total**	Large	Medium	Small	**Total**
Past due	BAM '000	BAM '000	BAM '000	**BAM '000**	BAM '000	BAM '000	BAM '000	**BAM '000**
Past due up to 30 days	22	-	-	22	-	12	27	39
Past due 30 – 60 days	29	-	-	29	-	-	24	24
Past due 60 – 90 days	12	-	-	12	-	-	79	79
Past due over 90 days	-	-	-	-	-	-	-	-
Total	**63**	**-**	**-**	**63**	**-**	**12**	**130**	**142**
Value of collateral								
2012								
Past due								
Past due up to 30 days	19	-	-	19	-	377	83	460
Past due 30 – 60 days	22	-	-	22	100	-	-	100
Past due 60 – 90 days	19	-	-	19	-	215	-	215
Past due over 90 days	-	-	-	-	-	2,309	114	2,423
Total	**60**	**-**	**-**	**60**	**100**	**2,901**	**197**	**3,198**
Value of collateral	1	-	-	**1**	-	2,357	113	**2,470**

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.1. Credit Risk (Continued)

34.1.2. Credit risk management and policies for impairment and provisions (Continued)

c) Non-performing loans (impaired loans)

The classification of loans to customers that are impaired, together with the allocated value of associated collateral instruments, is as follows:

	Retail loans				Corporate loans			
2013	Customer loans BAM '000	Housing loans BAM '000	Credit card loans and overdrafts BAM '000	**Total BAM '000**	Large BAM '000	Medium BAM '000	Small BAM '000	**Total BAM '000**
Non-performing loans	15,965	2,305	2,183	**20,453**	7,202	25,156	21,936	**54,294**
Value of collateral	2,497	2,292	-	**4,789**	7,167	20,468	15,474	**43,109**
2012								
Non-performing loans	14,401	1,769	2,021	**18,191**	6,568	27,651	23,617	**57,836**
Value of collateral	1,995	1,667	-	**3,662**	6,324	27,843	18,192	**52,359**

The data shown in the table above are presented in gross amounts.

As at December 31, 2013, assets acquired in settlement of non-performing loans amounted to BAM 81 thousand (2012: BAM 174 thousand), which are recorded off-balance.

d) Restructured loans and receivables

During the year, the Bank restructured certain loans to customers in order to improve their final recoverability. Restructuring is mainly performed in response to deterioration or for the prevention of further deterioration of the customer financial situation based on an analysis of the possibility of successful restructuring in order to remove difficulties in the client's operations within a defined time limit and return the client to the "performing" portfolio,

Restructured loans (exposure per all restructured loans irrespective of the remit they belong to) amounted to a total of BAM 28,228 thousand as at December 31, 2013 (2012: BAM 26,801 thousand).

	2013 BAM '000	**2012 BAM '000**
Restructured loans	28,228	26,801
Loan portfolio - gross	728,120	658,049
Restructured loans recorded as % of gross loan portfolio	3,9%	4,1%

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.2. Liquidity Risk

The liquidity risk represents the risk that the Bank will not be able to settle its financial liabilities fully and without any delay. In this sense, the main target of the Bank, when managing liquidity risk as the main risks present in banking operations, is to align its business activities and ensure optimal liquidity in accordance with minimum standards and limits prescribed by the Banking Agency of the Republic of Srpska, BH Central Bank and the Group.

The Bank has the access to different sources of financing which include different types of deposits of natural and legal persons, banks (within and out of the Group), and credit facilities. The aforesaid sources enable flexibility of funding sources and limit the dependence on any single source, thus providing a high level of their own sustainability in possible crises.

The Bank has implemented the liquidity policies of the Group, by which there are defined methods and procedures of liquidity parameters analysis, responsibilities of managing functions and reporting lines, which cover the short term, medium term and long term liquidity, as well as the liquidity stress tests. In accordance with Group guidelines, the exposure to liquidity risk is held at the level at which the Bank is able to observe its payment obligations on regular basis, and also in the crisis period, by ensuring the monitoring of short term and long term requirements for liquidity.

Short term liquidity maintenance requirements are planned each month for the period of the next six months. They are controlled and maintained daily. The Function of Assets and Liabilities Management manages the daily reserves of liquidity, providing the compliance with the clients' needs.

The following table shows the Profile of Structural Liquidity, which represents the analysis of assets and liabilities according to appropriate time baskets, based on the remaining period of the agreed maturity, with the following exceptions:

1) Current and demand savings accounts, and overdrafts on current accounts of legal and natural persons are mapped on the basis of their estimated stability, in accordance with Group standards.

2) Securities available for sale are mapped on the basis of the assessment of the period of marketability and possibility to pledge the securities with the Central Bank, in accordance with the Group Standards.

3) Non-performing loans, other assets, equity and reserves are also mapped according to the Group standard rules, for the longest term to maturity.

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.2. Liquidity Risk (Continued)

2013	Up to 1 month BAM '000	From 1 to 3 months BAM '000	From 3 to 12 months BAM '000	From 1 to 5 years BAM '000	Over 5 years BAM '000	Total BAM '000
Assets						
Cash and cash equivalents	41,412	-	-	-	-	41,412
Obligatory reserve with the Central bank	40,975	-	-	-		40,975
Loans and receivables due from banks	97,659	-	-	-	-	97,659
Financial assets available for sale	1	-	68,805	10	374	69,190
Loans and receivables due from customers	62,340	24,502	76,781	291,008	217,301	671,932
Financial assets held to maturity	-	-	69	36	-	105
Property and equipment					17,049	17,049
Intangible assets	-	-	-	-	3,039	3,039
Other assets	1,288	515	773	-	-	2,575
Deferred tax assets	-	-	54	-	-	54
Total assets	**243,674**	**25,017**	**146,482**	**291,054**	**237,763**	**943,990**
Liabilities, equity and reserves						
Deposits and loans due to banks	138,409	6,000	29,305	62,793	15,521	252,028
Deposits and loans due to customers	76,970	73,867	95,133	187,238	99,673	532,881
Other liabilities	3,206	3,117	3,727	2,366	-	12,416
Provisions for liabilities and costs	-	-	125	1,963	-	2,088
Income tax payable	-	264	-	-	-	264
Deferred tax liabilities	-	-	-	-	-	-
Equity and reserves	-	-	-	-	144,313	144,313
Total liabilities, equity and reserves	**218,585**	**83,248**	**128,290**	**254,360**	**259,507**	**943,990**
Liquidity gap	**25,089**	**(58,231)**	**18,192**	**36,694**	**(21,744)**	**-**

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.2. Liquidity Risk (Continued)

2012	Up to 1 month BAM '000	From 1 to 3 months BAM '000	From 3 to 12 months BAM '000	From 1 to 5 years BAM '000	Over 5 years BAM '000	Total BAM '000
Assets						
Cash and cash equivalents	47,177	-	-	-	-	47,177
Obligatory reserve with the Central bank	36,854	-	-	-	-	36,854
Loans and receivables due from banks	132,865	-	2,900	-	-	135,765
Financial assets available for sale	45,829	-	9,516	6	377	55,728
Loans and receivables due from customers	95,836	31,717	87,073	238,517	154,712	607,855
Financial assets held to maturity	-	-	64	106	-	170
Property and equipment	-	-	-	-	17,839	17,839
Intangible assets	-	-	-	-	4,658	4,658
Other assets	2,708	1,292	1,593	-	-	5,593
Deferred tax assets	-	-	19	-	-	19
Total assets	**361,269**	**33,009**	**101,165**	**238,629**	**177,586**	**911,658**
Liabilities, equity and reserves						
Deposits and loans due to banks	142,877	15,133	56,743	59,906	14,740	289,399
Deposits and loans due to customers	289,075	10,234	62,633	91,602	29,261	482,805
Other liabilities	3,727	669	4,327	748	15,073	24,544
Provisions for liabilities and costs	-	234	-	1,239	-	1,473
Income tax payable	-	354	-	-	-	354
Deferred tax liabilities	-	-	-	243	-	243
Equity and reserves	-	-	-	-	112,840	112,840
Total liabilities, equity and reserves	**435,679**	**26,624**	**123,703**	**153,738**	**171,914**	**911,658**
Liquidity gap	**(74,410)**	**6,385**	**(22,538)**	**84,891**	**5,672**	**-**

34. RISK MANAGEMENT (Continued)

34.3. Market Risk Management

Market risks result from general and specific trends and changes of specified market variables (interest rates, prices of securities, exchange rate changes) which can affect the economic value the Bank's portfolio in the trading book and in the banking book. The Bank is exposed to market risk mainly because of positions and business activities in the banking book.

Market risk exposure management includes the activities related to the operations of the Financial Markets and Assets and Liabilities Management function, and it has been organized through a system of internal acts and the setting of defined limits and warning signals which are supervised on a daily basis. Market risk measuring is based on the VaR ("Value at Risk") methodology. VaR is the appraised potential overnight loss which occurs at total and particular positions of balance sheet structure in a defined time period, based on numerous assumptions of changes in market conditions with a confidence level of 99%. The Group uses historic volatility simulation as an assessment model based on the last 500 daily return observations, VaR model quality is continuously monitored by back testing. Beside the VaR methodology, Market Risk Management also uses open FX position limits and base point calculation as a supplement to set VaR limits.

Factors which are also of importance for the assessment of market risk impact on the Banks' portfolio are stress-oriented warning levels and limits. The Bank performs stress liquidity tests within Risk Management in accordance with group parameters for:

- foreign currency,
- interest rate and
- liquidity risks,

and the results are included in regular ALCO reports.

The Bank performs activities on market risk limit review closely cooperating with UniCredit Bank Austria AG, Vienna. These activities are performed at least on annually, and if needed more often in accordance with business changes as a result of changes of legal regulations, business strategies goals development as well as targeted risk profile.

The set of documents with rules for operations performed by Financial Markets and Market Risk Management is made in the form of a Financial Markets Rule Book which is divided into three parts (General, Specific and Unit). Only the permitted risk bearers are enabled to enter into the risk-weighted items.

Overview of total VaR items of the Bank:

BAM '000	**2013 BAM '000**	**2012 BAM '000**
- average for the period	279	151
- maximum for the period	326	266
- minimum for the period	237	96

In addition to group market risk techniques, methods and measuring models, the Bank continuously works on the improvement of the business processes and data quality.

34.3.1. Currency risk

Currency risk is the risk of the possibility of occurrence of adverse effects on the financial results and net assets due to volatility in exchange rates. The Bank's exposure to foreign currency risk results from credit, deposit and trading activities and is controlled daily, according to legal and internal Group limits for particular payment currencies, and in total amount for all assets and liabilities denominated in foreign currency or indexed to a foreign currency.

Market Risk Management is responsible for daily monitoring of foreign exchange risk calculations in accordance with the Group guidelines in compliance with defined rules for trend monitoring through the conversion accounts for individual currencies.

The Bank intends to direct its business activities with a view to minimizing the mismatch between assets and liabilities denominated in the foreign currency or with the foreign currency clauses, keeping daily operations within set limits.

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.3. Market Risk Management (Continued)

34.3.1. Currency risk (continued)

All sensitivities stemming from positions in or linked to foreign currencies are covered by general daily VaR limit also, which among other risks, limits the maximum permitted loss of open positions in the foreign currencies.

Stress testing for currency risk is performed by the including appreciation and depreciation shocks for all the major currencies and currency buckets and the results are presented within regular ALCO reports.

Exposure to this risk is monitored on a daily basis in accordance with legally and internally determined limits for each currency and in the total amount for assets and liabilities denominated in foreign currencies or linked thereto with a foreign currency clause. According to local regulations the currency risk ratio is the proportion between the total open foreign currency items and the Bank's capital.

In accordance with the decision which regulates the minimum standards for currency risk management, the Bank is required to maintain relations between assets and liabilities in each individual currency so that its total open foreign currency position at the end of each working day is not higher than 30 % of its equity. According to internal regulations the Bank measures the risk of exposure to change in foreign currency rate through openness of positions in foreign currency in relation to limits defined in the absolute amounts.

	2013	**2012**
Currency risk ratios:		
- as at December 31	12.5%	0.13%
- maximum for the month of December	25.6%	25.5%
- minimum for the month of December	4.3%	0.13%

The major portion of business transactions exposes the Bank to the risk of change in the EUR exchange rate; however due to the Currency Board regime currently in place, according to which the ratio of the local currency to EUR is fixed, it can be deemed that there is no foreign exchange rate risk to the Bank.

The Bank protects itself from exposure to currency risk in foreign currencies other than EUR by managing foreign currency position, within the assets and liabilities management strategy, in such a manner that the positions opened through operations with customers are closed by opposite transactions, so that the open position of the Bank is reduced to the minimum.

The analysis of assets and liabilities shown in foreign currency amounts, as at December 31, 2013, is presented in the table below:

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.3. Market Risk Management (Continued)

34.3.1. Currency risk (continued)

	EUR BAM '000	EUR related items BAM '000	USD BAM '000	Other currencies BAM '000	Total currencies BAM '000	BAM BAM '000	Total BAM '000
2013							
Assets							
Cash and cash equivalents	6,606	-	236	1,122	7,964	33,448	**41,412**
Obligatory reserve with Central bank	-	-	-	-	-	40,975	**40,975**
Loans and receivables due from banks	88,648	-	6,476	2,535	97,659	-	**97,659**
Financial assets available for sale	-	11,791	-	-	11,791	57,399	**69,190**
Loans and receivables due from customers	112,347	332,634	-	-	444,981	226,951	**671,932**
Financial assets held to maturity	-	-	-	-	-	105	**105**
Property and equipment	-	-	-	-	-	17,049	**17,049**
Intangible assets	-	-	-	-	-	3,039	**3,039**
Other assets	111	126	220	12	469	2,106	**2,575**
Deferred tax assets	-	-	-	-	-	54	**54**
Total assets	**207,712**	**344,551**	**6,932**	**3,669**	**562,864**	**381,126**	**943,990**
Liabilities and equity							
Deposits and loans due to banks	229,012	-	1	-	229,013	23,015	**252,028**
Deposits and loans due to customers	185,746	107,770	8,956	9,246	311,718	221,163	**532,881**
Other liabilities	4,304	249	802	60	5,415	7,001	**12,416**
Provisions for liabilities and costs	292		-	-	292	1,796	**2,088**
Income tax payable	-	-	-	-	-	-	**-**
Net deferred tax liabilities	-	-	-	-	-	264	**264**
Equity and reserves	3,382	-	-	-	3,382	140,931	**144,313**
Total liabilities, equity and reserves	**422,736**	**108,019**	**9,759**	**9,306**	**549,820**	**394,170**	**943,990**
Net foreign currency position	**(215,024)**	**236,532**	**(2,827)**	**(5,637)**	**13,044**	**(13,044)**	**-**

The depreciation of foreign currencies (except for EUR) against BAM by 10%, with all other variables remaining unaltered, would result in an increase of profit for the year 2013 by the amount of BAM 846,4 thousand (2012: increase of BAM 855 thousand).

The appreciation of 10% in foreign currencies other than EUR against BAM would result in a decrease of profit for the year 2013 by the amount of BAM 846,4 thousand (2012: decrease of BAM 855 thousand).

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.3. Market Risk Management (Continued)

34.3.1. Currency risk (continued)

	EUR BAM '000	EUR related items BAM '000	USD BAM '000	Other currencies BAM '000	Total currencies BAM '000	BAM BAM '000	Total BAM '000
2012							
Assets							
Cash and cash equivalents	2,813	-	292	894	3,999	43,178	47,177
Obligatory reserve with Central bank	-	-	-	-	-	36,854	36,854
Loans and receivables due from banks	116,649	-	14,408	1,806	132,863	2,902	135,765
Financial assets available for sale	-	4,945	-	-	4,945	50,783	55,728
Loans and receivables due from customers	87,852	296,913	-	-	384,765	223,090	607,855
Financial assets held to maturity	-	-	-	-	-	170	170
Property and equipment	-	-	-	-	-	17,839	17,839
Intangible assets	-	-	-	-	-	4,658	4,658
Other assets	1,497	-	120	17	1,634	3,959	5,593
Deferred tax assets	-	-	-	-	-	19	19
Total assets	**208,811**	**301,858**	**14,820**	**2,717**	**528,206**	**383,452**	**911,658**
Liabilities and equity							
Deposits and loans due to banks	251,398	60	1	-	251,459	37,940	289,399
Deposits and loans due to customers	156,183	90,223	17,696	8,322	272,424	210,381	482,805
Other liabilities	3,061	-	32	36	3,129	21,415	24,544
Provisions for liabilities and costs	234	-	-	-	234	1,239	1,473
Income tax payable	-	-	-	-	-	354	354
Net deferred tax liabilities	-	-	-	-	-	243	243
Equity and reserves	3,382	-	-	-	3,382	109,458	112,840
Total liabilities, equity and reserves	**414,258**	**90,283**	**17,729**	**8,358**	**530,628**	**381,030**	**911,658**
Net foreign currency position	**(205,447)**	**211,575**	**(2,909)**	**(5,641)**	**(2,422)**	**2,422**	**-**

34. RISK MANAGEMENT (Continued)

34.3. Market Risk Management (Continued)

34.3.2. Interest rate risk

The Bank is exposed to risk from interest rate fluctuations which have an impact on the financial position of the Bank and its cash flows. The Bank's business operations are influenced by interest rates changes, to the extent that interest bearing assets and liabilities mature or their interest rates change at different times or in different amounts, Interest rate margins may grow as the result of those fluctuations however at the same time they may be reduced and cause losses in the event of unexpected fluctuations.

The main sources of interest rate risk are as follows:

- repricing risk resulting from unfavourable changes in the fair value of assets and liabilities during the remaining period until the next interest rate change (items with fixed interest rate are classified according to the remaining maturity);
- risk of change in inclination and shape of the yield curve (yield curve risk);
- risk of different changes in interest earned and interest paid (basis risk) of instruments having identical maturity and denominated in identical currency, where the interest rates are based on different reference rate types (e.g. EURIBOR vs. LIBOR).

Exposure to risk of interest rate changes is monitored by reports and in accordance with Group guidelines and it is in the domain of Market Risk Management. The methodology which is used for risk assessment of interest rate changes is based on the GAP analysis of time differences. Differences between interest-bearing assets and liabilities in different time "baskets" show how two sides of the balance sheet may react differently on the change of interest rates:

- in case of a positive GAP difference, the Bank is exposed to a risk of loss in the event that interest rates of given maturities for the relevant payment currency fall,
- in case of negative GAP difference the Bank is exposed to risk of loss in the event that interest rates of the given maturity for the relevant payment currency grow.

Risk is measured calculating the change in net present value of the portfolio in case of reference rate curve shift by 0.01% (1 base point) and it is limited by BPV limit (basis point value limit) as a sensitivity measure. BPV limits are defined in summary, per currency and per time baskets. BPV limits for daily operations matching are regulated by UniCredit Group. Interest risk is also monitored through the specified VaR model.

Stress testing conducted by the Bank in compliance with UniCredit Group parameters for interest rate risk category includes scenarios of various shocks on interest curves. Shocks include change in interest rate level (parallel shifts), curve rotations, change in curve inclination and jumps on specific segments of interest curves.

The Bank estimates the interest rate exposure also based on net interest income sensitivity analysis.

Economic capital sensitivity analysis

At the end of 2013 the Bank improved the methods of interest rate risk measurement by introducing economic capital sensitivity analysis in compliance with the Group and Basel II regulatory framework and the result thereof is included in the regular ALCO report.

An overview of the Bank's exposure to interest rate risk as at December 31, 2013 and 2012 is shown on the following pages.

The Bank is exposed to various risks which through the effects of fluctuations in the levels of market interest rates have an impact on its financial position and cash flows. The following table presents the Bank's estimate of the interest rate risk as at December 31, 2013 and 2012, as well as certain sensitivity of the Bank's earnings to movements in interest rates, which is not necessarily indicative for forthcoming periods.

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.3. Market Risk Management (Continued)

34.3.2. Interest rate risk (continued

a) Period of interest rate changes, interest risk analysis and amounts subject to fixed interest rates

Earnings will also be affected by the maturity structure of the Bank's assets and liabilities.

	Up to 1 month	1 – 3 months	3 months to 1 year	1 – 5 years	Over 5 years	Non-interest bearing	Total	Fixed interest rate
	BAM '000	BAM '000	BAM '000	BAM '000	BAM '000	BAM '000	BAM '000	BAM '000
2013								
Assets								
Cash and cash equivalents	22,724	-	-	-	-	18,688	41,412	-
Obligatory reserve with the Central bank	40,975	-	-	-	-	-	40,975	-
Loans and receivables due from banks	97,659	-	-	-	-	-	97,659	97,659
Financial assets available for sale	-	8,318	6,542	53,956	-	374	69,190	68,816
Loans and receivables due from customers	194,060	345,765	106,086	20,287	5,734	-	671,932	34,521
Financial assets held to maturity	-	-	-	105	-	-	105	105
Property and equipment	-	-	-	-	-	17,049	17,049	-
Intangible assets	-	-	-	-	-	3,039	3039	-
Other assets	-	-	-	-	-	2,575	2,575	-
Deferred tax assets						54	54	-
Total assets	**355,418**	**354,083**	**112,628**	**74,348**	**5,734**	**41,779**	**943,990**	**201,101**
Liabilities and equity								
Deposits and loans due to banks	711	209,453	41,173	-	-	691	252,028	-
Deposits and loans due to customers	194,556	65,321	69,759	85,286	8,717	109,242	532,881	9,277
Other liabilities	-	-	-	-	-	12,416	12,416	-
Provisions for liabilities and costs	-	-	-	-	-	2,088	2,088	-
Income tax payable						264	264	
Deferred tax liabilities	-	-	-	-	-	-	-	-
Equity and reserves	-	-	-	-	-	144,313	144,313	-
Total liabilities, equity and reserves	**195,267**	**274,774**	**110,932**	**85,286**	**8,717**	**269,014**	**943,990**	**9,277**
Bank's interest rate mismatch	160,151	79,309	1,696	(10,938)	(2,983)	(227,235)	-	191,824

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.3. Market Risk Management (Continued)

34.3.2. Interest rate risk (continued

a) Period of interest rate changes, interest risk analysis and amounts subject to fixed interest rates (continued)

	Up to 1 month	1 – 3 months	3 months to 1 year	1 – 5 years	Over 5 years	Non-interest bearing	Total	fixed interest rate
	BAM '000	BAM '000	BAM '000	BAM '000	BAM '000	BAM '000	BAM '000	BAM '000
2012								
Assets								
Cash and cash equivalents	34,570	-	-	-	-	12,607	47,177	-
Obligatory reserve with the Central bank	36, 854	-	-	-	-	-	36,854	-
Loans and receivables due from banks	132,865	-	2,900	-	-	-	135,765	135,765
Financial assets available for sale	-	-	4,935	4,598	45,821	374	55,728	55,354
Loans and receivables due from customers	166,611	322,506	85,630	18,518	14,590	-	607,855	41.538
Financial assets held to maturity	-	-	-	170	-	-	170	170
Property and equipment	-	-	-	-	-	17,839	17,839	-
Intangible assets	-	-	-	-	-	4,658	4,658	-
Other assets	-	-	-	-	-	5,593	5,593	-
Deferred tax assets	-	-	-	-	-	19	19	-
Total assets	**370,900**	**322,506**	**93,465**	**23,286**	**60,411**	**41,090**	**911,658**	**232.837**
Liabilities and equity								
Deposits and loans due to banks	157,877	90,845	39,917	-	-	760	289,399	-
Deposits and loans due to customers	204,947	67,987	45,744	56,021	3,463	104,643	482,805	-
Other liabilities	-	-	-	-	-	24,544	24,544	-
Provisions for liabilities and costs	-	-	-	-	-	1,473	1,473	-
Income tax payable						354	354	-
Deferred tax liabilities	-	-	-	-	-	243	243	-
Equity and reserves	-	-	-	-	-	112,840	112,840	-
Total liabilities, equity and reserves	**362,824**	**158,832**	**85,661**	**56,021**	**3,463**	**244,857**	**911,658**	**-**
Bank's interest rate mismatch	8,076	163,674	7,804	(32,735)	56,948	(203,767)	-	232.827

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.3. Market Risk Management (Continued)

34.3.2. Interest rate risk (continued

Sensitivity analysis

Simulation is performed by measuring the impact of change in the interest rate by 1pp on the net interest income for the period of 12 months based on simultaneous growth or drop of interest rates against all positions in the Bank's statement of financial position sensitive to the interest rate change. Changes in net interest income due to changes in interest rates should not exceed 10% of the projected net interest income.

Taking into consideration discrepancies between assets and liabilities in the observed periods: up to one month, 1-3 months and 3-12 months, an assessment of the impact of interest rate change of +/-1pp was performed on the net interest income of the Bank for 2013 and for 2012.

It was estimated from the specified assumptions that an interest rate decrease by 1pp would cause a decrease in the interest rate income for 2013 in the amount of BAM 2,412 thousand, or 5.5% of the total net interest income. Simulation of the impact of interest rate change on net interest income in the previous year resulted in decrease by of approximately BAM 1796 thousand or 4.5%.of the total net interest income.

The estimated future cash flow for the Bank's interest bearing liabilities as at December 31, 2013 and 2012 are shown in the following table:

2013	**Up to 1 month**	**From 1 to 3 months**	**From 3 to 12 months**	**From 1 to 5 years**	**Over 5 years**	**Total**
	BAM '000	**BAM '000**	**BAM '000**	**BAM '000**	**BAM '000**	**BAM '000**
Liabilities						
Transaction accounts and deposits of banks	138,459	6,142	29,540	62,786	15,525	252,453
Transaction accounts and deposits of customers	66,192	60,836	104,919	204,144	111,472	547,562
Other liabilities	7,088	780	3,562	4,080	2,206	17,715
Total liabilities	211,739	67,758	138,021	271,010	129,202	817,730
2012						
Transaction accounts and deposits of banks	142,891	15,569	56,997	59,904	14,743	290,104
Transaction accounts and deposits of customers	65,830	52,053	110,185	171,237	97,757	497,062
Other liabilities	7,452	66	3,158	2,472	17,376	30,524
Total liabilities	**216,173**	**67,688**	**170,340**	**233,613**	**129,876**	**817,690**

b) Effective interest rates

The following table presents the effective interest rates calculated as the weighted average for the financial instruments in the reporting period:

	2013	**2012**
	%	**%**
Obligatory reserve with the Central Bank	0.05	0.03
Loans and advances to banks	0.04	0.20
Loans to customers	7.35	7.89
Debt securities available for sale	5.90	6.61
Transaction accounts and deposits of banks	1.00	1.16
Transaction accounts and deposits of customers	1.76	1.38
Borrowings	1.59	2.43

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.3. Market Risk Management (Continued)

34.3.3. Risk of changes in interest rate margin

Within market-risk-measuring techniques the Bank measures the impact of interest rate margin changes in securities with fixed yield. The risk of change in securities price due to issuer credit risk change (margin perceived by the market) is measured and limited by CPV limit -basis point credit margin value (Credit Point Value). This limit has been applied since 2013. CPV limit is similar to BPV (Basis Point Value) and limits the risk of change in the net present value of securities portfolio if the impact of interest margin change shifts by 0.01% (1 base point). BPV limit limits total sensitivity of the Bank's itemss to changes in interest rates and CPV limit additionally limits investments in securities with regard to the volume and duration.

34.4. Operational Risk

Operational risk is the risk of incurring a loss due to inadequate or poor internal processes, systems and procedures, as well as due to errors made by employees during their work or the result of externally caused events. Definition of operational risks includes legal risk; however it excludes strategic and reputational risk.

Operational risk events are events resulting from inadequate or failed internal processes, people and systems or from systemic or other external events: internal or external fraud, relations with employees and safety at workplace, customer complaints, distribution of products, fines and penalties for non-compliance with regulations, damage to tangible assets of the Bank, work disruptions and errors in the system and process management.

In accordance with rules and methodology of the Group as well as local regulations, the Bank has established and improved the operational risk management system. The system includes tools and mechanisms for continuous monitoring of damages that the Bank bears by operational risk and the Bank's exposure to operational risks, the assessment of operational risk within processes and products, and defining the ways to avoid, control or transfer operational risk to third parties, as well as a reporting system.

The Bank uses the Group tool ARGO to record data on operational risk loss; reporting and the data analysis related to the operational risks.

The Bank's management and the Group are regularly informed and receive reports in respect of the aforementioned processes and indicators which constitute the operational risk management system. In addition, the operational risk management system is aligned with the standards of the UniCredit Group and local and international regulations.

Given the significance of the reputational risk and the requirements and standards of the Group, the Bank has commenced the process of implementing reputational risk management by adopting and implementing special policies and procedures regulating the area of reputational risk management.

34.5. Capital Management

The Bank's objectives in capital management are:

- compliance with capital requirements set by regulators of banks and capital markets,
- maintenance of the Bank's ability to continue the business operations so that it could ensure the yields for shareholders and benefits for other interested parties, and
- maintenance of a strong capital basis to support the development of its business activities.

The Bank monitors capital adequacy using techniques based on the regulatory requirements of BARS. Minimum capital standards defined by the law and other regulations are: maintenance of minimum level of the net capital, maintenance of the ratio of the total net capital to risk weighted assets at the prescribed minimum of 12%.

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT (Continued)

34.5. Capital Management (Continued)

Net capital of the Bank, serving to calculate the Bank's capital adequacy ratio, represents the sum of tier 1 and tier 2 capital, decreased by deductible items consisting of, *inter alia,* the amount of additional loan loss provision for loans and other assets calculated in accordance with BARS regulations.

The core capital (tier 1) of the Bank consists of: the share capital (ordinary shares), share premium, revaluation reserves from financial assets available for sale, reserves from profit and retained earnings reduced by intangible assets.

Supplementary capital (tier 2) of the Bank consists of generic loan loss provision calculated according to the BARS methodology on Bank's assets classified in Category A (performing assets) and the calculated current year profit verified by an external auditor.

Core, supplementary, net capital and capital adequacy calculated pursuant to the BARS regulations, are presented in the following table:

	2013 BAM '000	**2012 BAM '000**
Tier 1 capital		
Ordinary shares	97,055	82,055
Share premium	373	373
General legal reserves	5,854	5,089
Other reserves not related to the quality of assets	8,511	-
Retained earnings and revaluation reserves	12,207	2,195
Intangible assets	(3,039)	(4,658)
Total tier 1 capital	**120,961**	**85,054**
Tier 2 capital		
General reserves	12,562	11,528
Audited profit	16,817	13,840
Total tier 2 capital	**29,379**	**25,368**
Additional loan loss provisions as per regulatory requirement *	**(8,814)**	**(2,719)**
Net capital	**141,526**	**107,703**
Risk-weighted assets		
Risk weighted assets and credit equivalents	570,840	556,182
Weighted operational risk	55,943	55,943
Total weighted risks	**626,783**	**612,125**
Capital adequacy ratio	**22.6**	**17.6**

Information on total weighted risk is as submitted to BARS and is not audited.

* Additional loan loss provisions as per regulatory requirement and the other reserves which are not related to assessment of asset quality for 2013 are presented in accordance with the changed BARS regulations as explained in Note 3.6.1), and for 2012 according to the regulations valid on the respective reporting date.

NOTES TO THE FINANCIAL STATEMENTS

35. MANAGED FUNDS

The Bank manages funds related to transactions for and on behalf of third parties; it records these funds off-balance sheet, separated from its own assets. The Bank charges a fee for managing funds for and on behalf of third parties. Income and expenses for these funds are posted as income or expense of the owner or user.

Placements related to the activities for and on behalf of third parties are presented in the table below:

	2013 BAM '000	2012 BAM '000
Commission placements – MCI	730	731

In 2013, the Bank earned revenues from fees related to transaction on behalf and for the account of the third parties in the amount of BAM 39 thousand (2012: BAM 61 thousand),

36. LIABILITIES FOR FUTURE PAYMENTS UNDER OPERATING LEASE

The Bank has commitments for future payments under operating lease contracts. The contracts are related to the lease of the Bank's branch premises and ATMs.

The future minimum lease payments under the aforesaid operating lease contracts are summarized in the table below:

	2013 BAM '000	2012 BAM '000
Up to 1 year	82	573
From 1 to 5 years	409	1,038
Over 5 years	426	79
	917	**1,690**

37. FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

Fair value represents the amount for which some assets can be exchanged or the liability settled between knowledgeable and willing parties in arm's length transactions. It can also be defined as the value at which it is possible to dispose of assets / liabilities, or the appraised value of the neutralization of the market risk which originates from the assets / liabilities in the appropriate time-frame.

Up to January 1, 2013, the Bank had calculated fair value only for loans and deposits with fixed interest rates. The Bank has applied IFRS 13 measurement of fair value for periods which started as at January 1, 2013.

Assumptions used in assessing and measuring the fair values of financial instruments, the Bank based on application of centralized calculation developed at the Group level which uses IFRS 13 as a unique source of guidelines to measure the fair value.

Financial instruments are considered as quoted on active market if the quoted prices are easily and regularly available and if the prices represent actual and regular market transactions according to common market conditions.

All financial instruments are classified in accordance with criteria for classification into the hierarchy levels of fair values which contain three different levels.

Hierarchy Level 1: Fair value determined on the basis of prices for identical assets or liabilities which can be accessed as at the measurement date, i.e. if the financial instruments are present on an active market.

NOTES TO THE FINANCIAL STATEMENTS

37. FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES (Continued)

Hierarchy Level 2: Fair value determined based on valuation model for which input data are taken from active market when option of inputs used in assessment of Hierarchy Level 1 is excluded.

Hierarchy Level 3: Fair value determined based on valuation model for which input data are not present on active market, i.e. when more significant adjustments are needed.

In the methodology, when determining hierarchy levels for performing loans and deposits of banks and clients, the Group uses the following additional criteria:

Hierarchy Level 2: (risk free rate i.e. FV risk free – adjusted rate for credit spread for the expected and unexpected loss i.e. FV risk adjusted) / risk free rate i.e. FV risk free < 10%

Hierarchy Level 3: (risk free rate i.e. FV risk free – adjusted rate for credit spread for expected and unexpected loss i.e. FV risk adjusted) / risk free rate i.e. FV risk free >= 10%

The Bank classifies defaulted loans in accordance with the Group Instructions in such a manner that it equas their carrying and fair values. All assets and liabilities of the Bank are classified into hierarchy level 2 and level 3.

The Bank classifies bonds into level 2 and the fair value adjustment is performed in accordance with the centralized calculation of the Group.

Fair value of Bank's assets and liabilities is presented in accordance with IFRS 13 in the table below:

	December 31, 2013				**December 31, 2012**			
	Fair value	**Carrying value**	**Variance**		**Fair value**	**Carrying value**	**Variance**	
	BAM '000	**BAM '000**	**BAM '000**	**%**	**BAM '000**	**BAM '000**	**BAM '000**	**%**
Held-to-maturity investments	105	105	-	0.0%	170	170	-	0.0%
Loans and receivables due from banks	138,633	138,633	-	0.0%	172,619	172,619	-	0.0%
Loans and receivables due from customers	755,343	671932	83,411	12.4%	609,411	607,855	1,556	0.3%
Total	**894,081**	**810,670**	**83,411**	10.3%	**782,200**	**780,644**	**1,556**	0.2%
Deposits and loans due to banks	250,969	252,028	(1,059)	(0.4%)	289,399	289,399	-	0.0%
Deposits and loans due to customers	536,504	532,881	3,623	0.7%	480,810	482,805	(1,995)	(0.4%)
Total	**787,473**	**784,909**	**2,564**	0.3%	**770,210**	**772,205**	**(1,995)**	(0.3%)

NOTES TO THE FINANCIAL STATEMENTS

37. FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES (Continued)

Levels of fair value of Bank's assets and liabilities are presented in accordance with IFRS 13 in the table below:

	December 31, 2013			December 31, 2012		
	Fair value levels			Fair value levels		
	L1 BAM '000	L2 BAM '000	L3 BAM '000	L1 BAM '000	L2 BAM '000	L3 BAM '000
Held-to-maturity investments	-	-	105	-	-	170
Loans and receivables due from banks	-	138,633	-	-	172,619	-
Loans and receivables due from customers	-	680,434	74,909	-	571,008	38,403
Total	**-**	**819,067**	**75,014**	**-**	**743,627**	**38,573**
Deposits and loans due to banks	-	250,969	-	-	289,399	-
Deposits and loans due to customers	-	536,504	-	-	480,810	-
Total	**-**	**787,473**	**-**	**-**	**770,210**	**-**

38. EVENTS AFTER THE REPORTING DATE

The New Mandate of the Bank's Supervisory Board

Since 18 January 2014, with the mandate of 4 years, the new convocation of the Supervisory Board of the Bank has come into office with the following composition: Mr. Franjo Luković, President, and the members: Ms. Sanja Rendulić, Mr. Marko Remenar, Mr. Guenther Stromenger, Mr. Helmut Haller, Mr. Martin Klauzer and Mr. Heinz Tschiltsch. The stated convocation also performed the function of Supervisory Board in previous mandate except for Mr. Heinz Tschiltsch who replaced Ms. Friederike Kotz in this capacity.

Regulations Related to Regulatory Reserves and Equity

As described in Note 3.6. of Significant Accounting Policies, 1) Loans and receivables, changes in BARS regulations related to regulatory reserves and equity, which have been applied since December 31, 2013, will influence the calculation of the core capital (increase in Tier 1) to which minimum business standards are related, and which are mainly related to concentrations of exposure to credit risk, FX risk, etc. The changes will not influence the capital adequacy ratio.

Other Events

After the reporting date, there were no events which would require adjustments to the financial statements (corrective events) until the date of their issuance.

39. EXCHANGE RATES

The official exchange rates applied in translation of the statement of financial position components in foreign currencies into BAM as at December 31, 2013 and 2012 for the following more significant currencies were:

	December 31, 2013	December 31, 2012
USD	1.419016	1.483600
CHF	1.595424	1.619065
EUR	1.955830	1.955830