BOR BANKA D.D. SARAJEVO

FINANCIAL STATEMENTS FOR THE YEAR ENDED
31 DECEMBER 2011
TOGETHER WITH INDIPENDENT AUDITOR’S REPORT

RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The Management Board is responsible for ensuring that financial statements are prepared for each financial period in accordance with International Financial Reporting Standards (IFRS), as published by the International Accounting Standards Board (IASB), which give a true and fair view of the state of affairs and results of BOR Banka d.d. Sarajevo („the Bank“) for that period.

After making enquiries, the Management Board has a reasonable expectation that the Bank has adequate resources to continue in operational existence for the foreseeable future. For this reason, the Management Board continues to adopt the going concern basis in preparing the financial statements.

In preparing those financial statements, the responsibilities of the Management Board include ensuring that:

- suitable accounting policies are selected and then applied consistently;
- judgments and estimates are reasonable and prudent;
- applicable accounting standards are followed, subject to any material departures disclosed and explained in the financial statements; and
- the financial statements are prepared on the going concern basis unless it is inappropriate to presume that the Bank will continue in business.

The Management Board is responsible for keeping proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Bank and must also; ensure that the financial statements comply with the Federation of Bosnia and Herzegovina Accounting and Audit Law. The Management Board is also responsible for safeguarding the assets of the Bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Signed on behalf of the Management Board

Hamid Pršeš, Director

BOR Banka d.d. Sarajevo

Obala Kulina bana br. 18
71 000 Sarajevo
Bosna i Hercegovina

27 January 2012

Accountants &
business advisers

Independent Auditor´s report

To the shareholders of BOR Banka d.d., Sarajevo:

We have audited the accompanying financial statements of BOR Banka d.d. Sarajevo („the Bank"), set out on pages 3 to 37 which comprise of the balance sheet (statement of financial position) as at 31 December 2011, and the income statement (statement of comprehensive income), statement of changes in equity and cash flow statement 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 International Financial Reporting Standards and modified by the regulatory requirements prescribed by the Federal Banking Agency in Bosnia and Herzegovina. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's 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 entity's preparation and fair presentation 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 entity'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 present fairly, in all material respects, the financial position of the Bank as of 31 December 2011, and the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Tel 387 33 552 150, 552 153, 218 829 | Fax 387 33 552 152
E-mail info@pkf-re-opinion.ba | www.pkf-re-opinion.ba
PKF Re Opinion d.o.o. Sarajevo | Grbavička 4 | 71000 Sarajevo | Bosna i Hercegovina (BiH)
JIB 4200960550009 | PDV 200960550009 | Raiffeisen Bank d.d. BiH 1610000045270008

Emphasis of matter

We draw your attention to Note 3.1.1 – First-time adoption of IFRS, where it is explained that Bank prepared its financial statements for the year that ended as of 31 December 2011 in accordance with International Financial Reporting Standards. Effects of changes in accounting policy had been registered as regulatory reserves for credit loss (within equity) as transaction in year 2011. In previous periods, the Bank prepared its financial statements in accordance with regulations issued by Banking Agency of the Federation of Bosnia and Herzegovina. In preparing its comparative balances the Bank did not restate its financial statements for the year that ended as of 31 December 2010 and 1 January 2010. This represents departure from request of IFRS 1 – First-time adoption of International Financial Reporting Standards, where restatement of comparative financial statements is expected.

PKF Re Opinion d.o.o.

Nihad Fejzić, Director and Certified Auditor

Lejla Kaknjo, Certified Auditor

Sarajevo, 27 January 2012

INCOME STATEMENT – STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2011

	Note	2011 KM 000	2010 KM 000
Interest income	6	9,373	7,164
Interest expense	7	(3,055)	(2,302)
NET INTEREST INCOME		**6,318**	**4,862**
Fee and commission income	8	1,302	1,436
Sale of financial assets available for sale		244	-
Fee and commission expense		(102)	(71)
NET FEE AND COMMISSION INCOME		**1,444**	**1,365**
Other gain/(losses) - exchange rates differences, net)		194	(63)
Other operating income	9	175	242
PROFIT FROM OPERATIONS		**8,131**	**6,406**
Personnel expenses	10	(2,021)	(2,027)
Depreciation expense	23	(470)	(399)
Other administrative expenses	11	(1,326)	(1,194)
PROFIT BEFORE IMPAIRMENT LOSSES, PROVISIONS AND TAXATION		**4,314**	**2,786**
Impairment of receivables and provisions	12	(2,680)	(1,284)
Income from collected written off receivables	13	-	102
PROFIT BEFORE TAX		**1,634**	**1,604**
Income tax expense	14	(255)	(188)
NET PROFIT FOR THE YEAR		**1,379**	**1,416**
Profit per ordinary share	15	**6.59**	**6.82**

Statement of comprehensive income can be presented as follow:

	2011 KM 000	2010 KM 000
Net profit for the year	1,379	1,416
Other comprehensive income:		
(Loss)/profit of investments in financial assets available for sale	(278)	180
Subtotal:	***(278)***	***180***
Total comprehensive income for the year	**1,101**	**1,596**

The accompanying accounting policies and notes form an integral part of these financial statements.

BOR BANKA D.D. SARAJEVO
BALANCE SHEET – STATEMENT OF FINANCIAL POSITION
AS OF 31 DECEMBER 2011

	Note	31/12/2011 KM 000	31/12/2010 KM 000
Assets			
Cash and balances with banks	16	6,655	15,178
Obligatory reserve with Central Bank	17	9,300	7,237
Placements with other banks	18	25,854	14,861
Loans to customers, net	19	150,803	94,472
Financial assets available for sale	20	2,473	1,767
Financial assets held to maturity	21	2,030	-
Other assets, net	22	151	216
Tangible and intangible assets	23	19,105	19,157
Total assets		**216,371**	**152,888**
Liabilities			
Due to other banks and financial institutions	24	42,056	22,010
Liabilities toward Government of FB&H („Fund“)	25	32,123	31,784
Liabilities toward customers	26	93,421	51,782
Long term accruals	27	2,388	2,634
Other liabilities	28	346	873
Provisions for contingent liabilities	29	339	264
Total liabilities		**170,673**	**109,347**
Shareholder´s equity and reserves			
Shareholders’ equity	30	29,166	26,515
Revaluation reserves		12,976	13,134
Investments revaluation reserve		67	441
Other reserves		10	10
Regulatory reserves for credit loss		1,465	-
Accumulated profit		2,014	3,441
Total shareholder´s equity		**45,698**	**43,541**
Total liabilities and equity		**216,371**	**152,888**

The accompanying accounting policies and notes form an integral part of these financial statements.

Signed on behalf of the Bank on 27 January 2012

Hamid Pršeš, Director

Enisa Hulusić, Executive director for accounting, analysis and IT

BOR BANKA D.D. SARAJEVO
STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2011

	Share capital KM 000	Revaluation reserves KM 000	Fair value adjustment reserves KM 000	Other reserves KM 000	Regulatory reserves for credit loss KM 000	Accumulated profit KM 000	Total KM 000
Balance as of 31 December 2009	**26,515**	**13,294**	**261**	**10**	**-**	**2,175**	**42,255**
Transfer from/to	-	(160)	-	-	-	160	-
Other comprehensive income	-	-	180	-	-	-	180
Dividend paid	-	-	-	-	-	(310)	(310)
Net result for 2010	-	-	-	-	-	1,416	1,416
Balance as of 31 December 2010	**26,515**	**13,134**	**441**	**10**	**-**	**3,441**	**43,541**
Transfer of regulatory reserves for credit loss*	-	-	-	-	1,465	-	1,465
Adjustment	-	-	-	-	-	(2)	(2)
Paid in capital**	2,651	-	-	-	-	(2,651)	-
Transfer from/to	-	(158)	-	-	-	158	-
Other comprehensive income	-	-	(278)	-	-	-	(278)
Sale of financial assets available for sale	-	-	(96)	-	-	-	(96)
Dividend paid***	-		-	-	-	(311)	(311)
Net result for 2011	-		-	-	-	1,379	1,379
Balance as of 31 December 2011	**29,166**	**12,976**	**67**	**10**	**1,465**	**2,014**	**45,698**

* As described in Note 3.1.1. as of 31 December 2011 the Bank disclosed as regulatory reserves for credit loss amount of KM 1,465 which represents effect of change in accounting policy on opening balance as of 1 January 2011. As of 31 December 2011 Bank estimated impairment in accordance with FBA regulation in amount of KM 1,150 thousand for loan portfolio. Considering that effect is lower comparing with already recorded regulatory reserves, difference of KM 262 thousand had not been registered (in accordance with Minutes upon changes of forming, registering and disclosing reserves for credit loss).

Furthermore, adopted Methodology for calculation of impairment for loan losses is established on adequately determined principles and fulfils requests from International Accounting Standard 39.

** As of 31 March 2011 Bank Assembly issued decision number S - 9/11 upon increase of share capital for amount of KM 2,651,460. Paid in capital had been registered as increase of nominal share value from previous KM 100 to KM 110 per share. As of 31 December 2011, registered share capital amounts to KM 29,166,060 which consists of 265,146 shares (shares with voting rights amounts to 162,014 shares).

Securities Exchange Commission in Federation B&H approved paid in capital (increase in share value from KM 100 to KM 110) with its decision no. 03/1-19-130/11 issued on 11 May 2011.

*** Furthermore, dividend for 2010 was paid for preferential cumulative shares in amount of KM 157 thousand, and for noncumulative preferential shares in amount of KM 154 thousand, based on Bank Assembly decision issued on 31 March 2011.

The accompanying accounting policies and notes form an integral part of these financial statements.

CASH FLOW STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2011

	2011 KM 000	2010 KM 000
Operating activities		
Profit before tax	1,634	1,604
Adjustments for:		
Depreciation	470	399
Net increase in impairment of receivables	2,680	1,284
Collected written off receivables	-	(102)
Loss on disposal of assets and adjustments	40	21
Changes in assets and liabilities:		
Increase of receivables from Central bank B&H	(2,063)	(130)
Net (increase)/decrease of placements at banks	(10,982)	312
Net increase of loans to customers, before impairment	(57,531)	(25,507)
Decrease of other receivables	76	235
Net increase of liabilities toward customers	41,639	24,269
Net changes in long term accruals	(246)	1,213
Decrease of other liabilities	(596)	(136)
Cash (used in)/from operating activities	**(24,879)**	**3,462**
Income tax paid	(188)	(117)
Net cash (used in)/provided from operating activities	**(25,067)**	**3,345**
Investing activities		
Increase of assets available for sale	(1,042)	-
Increase in assets held to maturity	(2,030)	-
Purchase of tangible and intangible assets	(458)	(756)
Net cash used in investing activities	**(3,530)**	**(756)**
Financing activities		
Proceeds from borrowings	20,046	2,632
Increase of liabilities toward Government of B&H	339	8,142
Dividend paid	(311)	(310)
Net cash provided from financing activities	**20,074**	**10,464**
Net (decrease)/increase in cash and cash equivalents	**(8,523)**	**13,053**
Cash and cash equivalents at the beginning of year	**15,178**	**2,125**
Cash and cash equivalents at the end of year	**6,655**	**15,178**

The accompanying accounting policies and notes form an integral part of these financial statements.

1. GENERAL

BOR Banka d.d. Sarajevo ("Bank") is registered 1995 in Federation of Bosnia and Herzegovina with address Obala Kulina Banka no. 18, 71000 Sarajevo, with a goal to support development and recovery process in Bosnia and Herzegovina.

The principal activity of the Bank is:
- Receiving and placing of deposits,
- Other services in accordance with Law,
- Foreign and foreign-currency payment transaction,
- Purchase and selling of securities,
- Emission of securities and cash cards,
- Issuing of guarantees, bill of exchange securities and other form of assurances,
- Performance of certain payment transactions,
- Maintenance and managing with assets and securities,
- Financial engineering transactions,
- Managing of finances,
- Expertise, diagnosis and restructuring,
- Receiving and placing loans,
- Other activities in accordance with registration.

In previous periods Bank had a ban on collection of deposits by the Federal Banking Agency due to specific contract with Kuwait Fund and outstanding capital ownership structure. Pursuant to the Law on Amendments to the Law on deposit insurance in B&H banks („Gazette of B&H No.: 75/09") the Bank has made amendments and changes of the Bank's Statute. By Decision No. 04-772/09 dated 30 March 2009 the Banking Agency of the FB&H approved Statute in part of deposit collection and based on it the Bank has submitted request to the Agency for Deposit Insurance of B&H on 3 September 2009 (No. I-2224/09). After the inspection and received ranking status performed by FBA Agency the Bank received permission and association member status from Agency of deposit insurance of FBiH as of 1 November 2011.

As of 31 December 2011 the Bank had 57 employees (2010 – 55).

Supervisory Board

Aziz Šunje	Chairman (Since 31 March 2011)
Esad Hrvačić	Chairman (Up to 31 March 2011)
Ademir Abdić	Member (Since 31 March 2011)
Hasan Đozo	Member (Since 31 March 2011)
Hasen Mašović	Member (Since 31 March 2011)
Hajrudin Hadžimehanović	Member
Denis Lasić	Member (Up to 31 March 2011)

Audit Committee

Tihomir Ćurak	Chairman
Senad Herenda	Member (Since 12 April 2011)
Elma Oković	Member (Since 12 April 2011)
Denis Lasić	Member (Since 12 April 2011)
Senaid Zajimović	Member (Since 12 April 2011)
Ahmet Alibašić	Member (Up to 12 April 2011)
Edin Tokić	Member (Up to 12 April 2011)

1. GENERAL /CONTINUED)

Management Board

Hamid Pršeš	Director of Bank
Adela Zorlak	Executive director of Individuals management department /Executive director od sales department (Since 1 November 2011)
Bedina Jusičić Musa	Executive director of legal entities management department/ Risks management department (Since 1 November 2011)
Enisa Hulusić	Executive director for accounting, analyze and IT department/ accounting and treasury (Since 1 November 2011)
Muhamed Šehbajraktarević	Executive director for legal, personnel and general services/ lehal and general services (Since 1 November 2011)
Ajna Šehović	Executive director of treasury department and internal payment transactions (Up to 1 November 2011)

Internal auditor of the Bank is Šefika Kreso.

2. ADOPTION OF NEW AND REVISED STANDARDS

In the current year, the Company has adopted IFRS's which were effective for annual reporting period: (Effective for periods beginning on 1 January 2011 or after):

IFRS 1 First time adoption of International financial reporting standards (Annual amendments to IFRS)
IFRS 7 Financial instruments: disclosures (Amendments of standards resulting of comprehensive review of balance sheet activities, in application since 1 January and 1 July 2011);
IAS 1 Presentation of financial statements (Annual amendments to IFRS)
IAS 24 Related party disclosures (Provide a partial exemption from related party disclosures, clarify the definition of the related party, included and explicit requirements to disclose commitments involving related parties)
IFRIC 14 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction
IAS 34 Interim financial reporting (Annual amendments to IFRS)

2.2 Standards and Interpretations in issue not yet adopted

At the date of authorisation of these financial statements, the following Standards and Interpretations were in issue but not yet effective:

IFRS 9 Financial instrument (Applicable from 1 January 2015)
IFRS 10 Consolidated financial statements (Applicable from 1 January 2013)
IFRS 11 Joint arrangements (Applicable from 1 January 2013)
IFRS 12 Disclosure of interest in other entities (Applicable from 1 January 2013)
IFRS 13 Fair value measurements (Applicable from 1 January 2013)
IAS 1 Presentation of financial statements (Presentation of other comprehensive income in application since July 1 of year 2012)
IAS 12 Income taxes (Applicable from 1 January 2013)
IAS 19 Employee benefits (pensions and other post retirement benefits, in application since January 1 2013)
IAS 27 Separate financial statements (Applicable from 1 January 2013)
IAS 28 Investments in associates and joint ventures (Applicable from 1 January 2013)

Bank will not adopt these standards, amendments and interpretations in advance, before the date they enter into force. Management anticipates that the adoption of these standards and interpretations in future periods will not significantly affect Bank's financial statements.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

3.1 Basis of preparation

As required by changes within local legislation the Bank prepared its financial statements in accordance with IFRS for the first time. Previous financial statements had been prepared in accordance with regulatory requirements of Federal Banking Agency ("FBA"), central regulatory organization of banking system in Federation of Bosnia and Herzegovina. Bank is using IFRS for the first time and in accordance with such IFRS 1:"*First time adoption of International financial reporting standards*" had been applied.

Explanation of transition to IFRS and effects on financial statements and financial result had been described in Note 3.1.1. – First-time adoption of IFRS.

The financial statements have been prepared on the historical cost basis except for the revaluation of certain noncurrent assets and financial instruments. The principal accounting policies are set out below. The financial statements are presented in thousands of Convertible mark (KM'000) which is the functional currency of the Bank. The financial statements are prepared on an accrual basis of accounting, under the going concern assumption.

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and their reported amounts of revenues and expenses during the reporting period. These estimates are based on the information available as at the reporting period date and actual results could differ from those estimates.

The Bank considers that it operates in a single business segment, and a single geographical segment, that is the provision of banking services in Bosnia and Herzegovina.

3.1.1. First-adoption of IFRS

As previously mentioned in the Statement of compliance, these are the first statements of the Bank prepared in accordance with IFRS. In previous periods, the Bank prepared financial statements in accordance with the accounting regulations of the Banking Agency of Federation of Bosnia and Herzegovina.

The basic differences between IFRS and the previous accounting framework relate to the following:

- The assessment of specific impairment allowance for financial instruments, in particular regarding loans and receivables, in accordance with relevant regulations of FBA is not in line with the requirements of IAS 39 *„Financial instruments: Recognition and Measurement"* which requires that impairment allowances on loan losses and provisions should be estimated based on discounted expected future cash flows by using the original effective interest rate.
- FBA requires banks to recognize impairment loss in the income statement for assets not individually identified for impairment by using the prescribed rate of 2%. Such a policy results in deviation from the methodology for measurement of the total impairment allowance on a portfolio basis, which is based n IFRS, and which assumes recognition only of losses which have occurred but have not yet been reported („IBNR"). INBR represents a situation where the losses have been incurred but it is not yet evident which financial asset is impaired and is calculated by applying an estimated loss rate for an estimated emergence period to the balance of unimpaired loans.
- Suspended interest represents the accrued but uncollected interest payments on assets which are classified as impaired assets (assets classified as substandard assets, doubtful assets and losses). Upon reclassification from interest earning to impaired assets, the Bank reverses the full amount of the accrued uncollected interest in the income statement, and ceases to accrue any further interest in the balance sheet (suspended interest is recorded off balance sheet) until collected in cash from the borrower. The only exception to this rule may occur where an impaired asset is covered by first class or good quality collateral and at the same time is in the process of collection. This policy is not in accordance with IAS 18 "Revenue" or IAS 39 "Financial Instruments: Recognition and Measurement" which require interest income on impaired financial assets to be calculated using the effective interest rate method.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.1.1. First-adoption of IFRS (Continued)
The accounting policies stated in this report have been applied in preparing the financial statements for the year ended 31 December 2011 with attention to the fact that the Bank had departed from request of IFRS 1 – Presentation of financial statements (Paragraph 39) where is stated that the Bank should restate its comparative financial statements for the year that ended on 31 December 2010. Also, based on Bank Management, restatement was not conducted due to explanation received from FBA no. 03-3-99-1/12 dated on 13 January 2012.

As previously described the Bank recognized effects of impairment for financial instruments (loans and receivables) in accordance with relevant regulations of FBA that is not in accordance with the requirements of relevant standards. Mentioned impairment, in accordance with relevant standards, resulted in decrease of previously disclosed amounts of impairment of loan portfolio in amount of KM 1,397 thousand as of 31 December 2010.

Furthermore, in accordance with application of relevant standards on impairment for other assets, previously disclosed amounts of impairment of other assets decreased in amount of KM 53 thousand, as of 31 December 2010. Similar to previous, application of relevant standards also effected provision for contingent liabilities as of 31 December 2010 and resulted in decrease in provision in amount of KM 15 thousand.

Total effects of transition to IFRS resulted in net increase of opening balance in equity and reserves as of 1 January 2011 in amount of KM 1,465 thousand.

3.2 Interest income and expense
Interest income and expenses are recognized in the income statement (the statement of comprehensive income) for all interest yielding/bearing instruments on the accrued basis by the application of the effective interest rate method, i.e. according to the rate that discounts the estimated cash flows to the net present value during the term of the agreement. Such income and expenses are presented as interest and similar income and interest and similar expenses in the income statement (the statement of comprehensive income). Interest income and expenses also include income and expenses from loan fees and commissions and receivables from customers, or borrowings from banks, recognized on the basis of the effective interest rate.

The effective interest rate method is the method of calculation of amortized cost of the financial assets or financial liabilities and distribution of interest income or expenses in the appropriate time period. 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 the future loan losses. The calculation includes all fees and commission that the contractual sides have paid and received, and which are a constituent part of the effective interest rate, transaction costs and all other premiums and discounts.

3.3 Fee and commission income and expense
Fees and commissions consist mainly of fees earned on domestic and foreign payment transactions, and fees for loans and other credit instruments issued by the Bank. Fees for payment transactions are recognized in the period when services are rendered. Loan origination fees, after approval and drawdown of loans, are deferred (together with related direct costs) and recognized as an adjustment to the effective yield of the loan over its life.

3.4 Employee benefits
On behalf of its employees, the Bank is paying pension and health insurance on and from salaries, as well as taxes. The Bank is paying the above contributions into the Pension and health funds of the Federation of Bosnia and Herzegovina, as per the set legal rates during the course of the year on the gross salary paid. In addition, meal allowances, transport allowances and vacation bonuses are paid in accordance with the local legislation. These expenses are recorded in the income statement in the period in which the salary expense is incurred.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.5 Retirement severance payments

In accordance with local legislation, Bank allow severance payments as minimum six salaries paid in past months or six average salaries in Federation of Bosnia and Herzegovina for past month, depending on what is suitable for employee.

The cost of providing benefits is determined using the Projected Unit Credit Method. Past service cost is recognized immediately to the extent that the benefits are already vested, and otherwise is amortized on a straight-line basis over the average period until the benefits become vested. The retirement benefit obligation recognized in the balance sheet represents the present value of the defined benefit obligation as adjusted for unrecognized past service cost.

3.6 Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax. The tax expense is based on taxable income for the year. Taxable income differs from net income as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Bank‘s liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the reporting period date.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax basis used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognized for all taxable temporary differences and deferred tax assets are recognized to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilized.

The carrying amount of deferred tax assets is reviewed at each reporting period date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the asset to be recovered. Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realized. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the Bank has the ability and intention to settle on a net basis. The Bank is subject to various indirect taxes which are included in administrative expenses.

3.7 Cash and cash equivalents

For the purpose of reporting cash flows, cash and cash equivalents are defined as cash, balances with the Central Bank („CBBH‘), current accounts with other banks and cash at hand.

Cash and cash equivalents excludes the compulsory minimum reserve with the Central Bank as these funds are not available for the Bank‘s day to day operations. The compulsory minimum reserve with the CBBH is a required reserve to be held by all commercial banks licensed in Bosnia and Herzegovina.

3.8 Financial assets

Financial assets are classified into the following specified categories: available-for-sale‘(AFS), held-to-maturity investments‘, and loans and receivables‘. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Loans and receivables are non-derivative financial assets with fixed or determinable payment that are not quoted in an active market. Mentioned assets appear where Bank transfers cash towards debtor without attention of active trade with receivables. Loan and receivables includes bank and other client’s loans and receivables.

Available for sale financial assets are any non-derivative financial assets designated on initial recognition as available for sale or any other instruments that are not classified in other category of financial instruments.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.8 Financial assets (Continued)

Available for sale financial assets represents assets that are acquired with intention of holding assets for indefinite time and possibility of sale in case of liquidity requirements, changes in interest rates, foreign exchange rates and prices of equity securities. Available for sale financial assets includes debt and equity securities. Other financial liabilities represent all financial liabilities that are not classified as financial liabilities through profit and loss, including current and deposit accounts and borrowings.

Recognition
Loans and receivables and other financial liabilities are recognized when advanced to borrowers or received from lenders. The Bank recognizes available for sale financial assets at the trade date.

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 rate method, less any impairment.

(b) Available for sale financial assets
Available for sale 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 available for sale financial assets are measured at fair value, except for equity securities 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.

(c) Other financial liabilities
Other financial liabilities are initially measured at fair value. Subsequent to initial recognition, other financial liabilities are measured at amortised cost using the effective interest rate method.

Recognition of gains and losses on subsequent measurement of financial instruments
Gains and losses from a change in the fair value of available-for-sale financial assets are recognised directly in the fair value reserve within equity until derecognition or impairment, when the cumulative amount previously recognised in equity is transferred to the statement of comprehensive income. Interest income calculated using the effective interest rate method is recognised in the statement of comprehensive income.

Foreign exchange gains and losses on available for sale equity securities represent a part of the fair value of these instruments and are recognized in equity. Dividend income on available for sale equity securities is recognized in the statement of comprehensive income when the right to receive payment has been established.

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 (“an event that causes the impairment“).

1) Loans and receivables
The Bank regularly reviews and monitors loans and receivables as well as other financial assets at each reporting date to determine whether there is objective evidence of impairment. 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 impairment allowance, and the amount of the loss is recognized in the statement of comprehensive income.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.8 Financial assets (Continued)

1) Loans and receivables (Continued)
If loans and receivables have a variable interest rate, the discount rate for determining impairment allowance represents the current effective interest rate determined by an agreement at the moment when impairment has occurred.

Financial assets for which no impairment was recognised on an individual basis, is grouped with other financial assets with similar characteristics, which are then reviewed for impairment on a group basis. Group impairment also includes impairment on a portfolio basis (IBNR) in cases where the (on an individual or group basis) determines that there is no objective evidence of impairment. If the 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 impairment allowance is then shown as income in the statement of comprehensive income. Write-off of uncollectible receivables is performed based on the decision of the Supervisory Board, and in accordance with court decisions, agreements between the interested parties and the Bank's assessments. In accordance with local regulations the Bank also calculates impairment loss in accordance with FBA Regulations.

Loans, placements and other financial assets of the Bank are classified into categories prescribed by the 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 the reserve for potential losses is calculated by applying percentages prescribed by the FBA. If the specific provision for potential losses calculated in accordance with BARS regulations is higher than the impairment allowance calculated in accordance with IFRS requirements, this difference is presented as a regulatory reserve for credit losses within equity based on a decision of the Bank's General Assembly and in accordance with accounting regulations of the Federation of Bosnia and Herzegovina.

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 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 recognised in profit or loss – is removed from other comprehensive income and recognised in profit or loss. Impairment losses recognised in the statement of comprehensive income on equity instruments are not reversed through the statement of comprehensive income at any point thereafter. 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 recognised in profit or loss, the impairment loss is reversed through the statement of comprehensive income.

Derecognition
A financial asset is derecognised (in full or in part) when the Bank loses control over the contractual rights on the asset. This occurs when the rights are realised, expire or are surrendered.

Available for sale financial assets are derecognized on the trade 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 derecognises financial liabilities only when the financial liability ceases to exist, i.e. when it is discharged, cancelled or has expired. If the terms of a financial liability change, the Bank will cease recognising that liability and will instantaneously recognise a new financial liability, with new terms and conditions.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.8 Financial assets (Continued)

Fair value measurement principles
The fair value of non-exchange-traded derivatives is estimated at the amount that the Bank would receive or pay to terminate the contract at the balance sheet date taking into account current market conditions and the current creditworthiness of the counterparties.

Specific instruments
a) Financial derivatives
Financial derivatives include foreign exchange forward and swap contracts. Financial derivatives are initially recognized and subsequently measured at their fair value in the statement of financial position. Fair values are obtained by application of various assessment techniques, including discounted cash flow models. All derivatives are presented as financial assets at fair value through profit or loss when their fair value is positive and as financial liabilities at fair value through profit or loss 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 sent for collection, current accounts with other banks and cash deposited with the Central Bank (not including the amount of the obligatory reserve).

c) Placements with and loans to banks
Placements with and loans to banks are classified as loans and receivables and are carried at amortization cost less any impairment losses.

d) Loans to customers
Loans to customers are presented net of impairment allowance to reflect the estimated recoverable amounts.

e) Equity securities
Equity securities are classified as assets available for sale and are carried at fair value, unless there is no reliable measure of the fair value, in which case they are stated at acquisition cost, less any impairment.

f) Debt securities
Debt securities are classified as available for sale financial assets and carried at fair value.

g) Transaction accounts and deposits from banks and customers
Transaction accounts and deposits are classified as other liabilities and are initially recognized at fair value less transaction costs, and subsequently stated at their amortised cost using the effective interest rate method.

h) Borrowings
Interest bearing borrowings are classified as other financial liabilities and are initially measured at fair value less transaction costs, and subsequently stated at their amortised cost using the effective interest rate method.

3.9 Financial liabilities and equity instruments issued by Bank

Classification as debt or equity
Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

Equity instruments
An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Bank are recorded at the proceeds received, net of direct issue costs.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.9 Financial liabilities and equity instruments issued by Bank (Continued)

Financial guarantee contract liabilities
Financial guarantee contract liabilities are measured initially at their fair values and are subsequently measured at the higher of:

- the amount of the obligation under the contract, as determined in accordance with IAS 37: „Provisions, Contingent Liabilities and Contingent Assets";
- and the amount initially recognized less, where appropriate, cumulative amortization recognized in accordance with the revenue recognition policies set out at above.

Financial liabilities
Financial liabilities are classified as either financial liabilities at FVTPL or other financial liabilities. The Bank creates one category of financial liabilities, for which basis of accounting is disclosed below.

Other financial liabilities
Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognized on an effective yield basis. The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

Derecognition of financial liabilities
The Bank derecognizes financial liabilities when, and only when, the Bank‘s obligations are discharged, cancelled or they expire.

3.10 Property and equipment
Property and equipment are stated at cost or its revalue amount less accumulated depreciation and any accumulated impairment losses. Revaluations are performed with sufficient regularity such that the carrying amount does not differ materially from that which would be determined using fair values at the balance sheet date.

Any revaluation increase arising on the revaluation of such land and buildings is credited to the property revaluation reserve, except to the extent that it reverses a revaluation decrease for the same asset previously recognised as an expense, in which case the increase is credited to the income statement to the extent of the decrease previously charged. A decrease in carrying amount arising on the revaluation of such land and buildings is charged as an expense to the extent that it exceeds the balance, if any, held in the properties revaluation reserve relating to a previous revaluation of that asset.

Initially, property and equipment are stated at cost less accumulated depreciation and any accumulated impairment losses. Cost includes the purchase price and directly associated cost of bringing the asset to a working condition for its intended use. Maintenance and repairs, replacements and improvements of minor importance are expensed as incurred. Significant improvements and replacement of assets are capitalised. Gains or losses on the retirement or disposal of property, plant and equipment are included in the income statement in the period they occur.

Properties in the course of construction are carried at cost, less impairment loss, if any. Depreciation commences when the assets are ready for their intended use. Depreciation is calculated on a straight-line basis over the estimated useful life of the applicable assets

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.10 Property and equipment (Continued)
Estimated depreciation rates were as follows:

Buildings	1.3% (till 77 years)
Computers	33% (till 3 years)
Furniture and other office equipment	7% - 20% (from 5 to14 years)

3.11 Intangible assets
Intangible assets are measured initially at purchase cost and are amortised on a straight-line basis over their estimated useful lives.

3.12 Foreign currency translation
Transactions in currencies other than Bosnia and Herzegovina KM are initially recorded at the rates of exchange prevailing on the dates of the transactions. Monetary assets and liabilities are translated at the rates prevailing on the reporting period date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated. Profits and losses arising on translation are included in the income statement for the year. The Bank values its assets and liabilities by middle rate of Central Bank of Bosnia and Herzegovina valid at the date of balance sheet, which approximate market rates. The principal rates of exchange set forth by the Central Bank and used in the preparation of the Bank‘s balance sheet at the reporting dates were as follows:

31 December 2011 EUR 1 = KM 1.95583 USD 1 = KM 1.511577
31 December 2010 EUR 1 = KM 1.95583 USD 1 = KM 1.472764

For the financial assets and liabilities denominated in KWD, the Bank use Kuwait National Bank rate.

31 December 2011 KWD 1 = 5.359 KM
31 December 2010 KWD 1 = 5.182754 KM

3.13 Provisions
Provisions are recognized when the Bank has a present obligation as a result of a past event, and it is probable that the Bank will be required to settle that obligation. Management Board estimates the provisions based at the best estimate of expenditure to settle the Bank‘s obligation. Provisions are discounted to present value where the effect is material.

4. CRITICAL ACCOUNTING JUDGMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the Bank‘s accounting policies, which are described in Note 4, the directors are required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Key sources of estimation uncertainty
The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the reporting period date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

4. CRITICAL ACCOUNTING JUDGMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY (CONTINUED)

Useful lives of property and equipment
As described at Note 3 above, the Bank reviews the estimated useful lives of property and equipment at the end of each annual reporting period.

Fair value of derivatives and other financial instruments
As described in Note 34. the Management use their judgement in selecting an appropriate valuation technique for financial instruments not quoted in an active market. Valuation techniques commonly used by market practitioners are applied. Financial instruments, other than loans, are valued using a discounted cash flow analysis based on assumptions supported, where possible, by observable market prices or rates. The estimation of fair value of unlisted shares includes some assumptions not supported by observable market prices or rates.

5. GLOBAL MARKET CRISIS

The Bank was impacted by the recent financial crisis and deteriorating economic conditions. Due to the current global crisis in the market and its effects on the local market in Bosnia and Herzegovina, the Bank will probably still operate in more difficult and uncertain economic environment in 2011. The impact of this crisis on the Bank‘s business operations is currently not possible to fully predict and therefore there is an element of general uncertainty.

So far, the ongoing financial crisis has had some impact on the financial position and performance of the Bank, mainly in the amount of additional loan provisions recognized in the income statement for the year ended 31 December 2011. The Bank monitors closely the credit, liquidity, interest rate and foreign exchange risks on a regular basis. The deteriorating economic situation in the country will probably impact the position of certain industries and the abilities of some clients to meet their loan obligations. This may consequently influence the amount of the Bank‘s provisions for impairment losses in 2012 and other areas that require estimates to be made by management, including the valuation of collateral and of securities.

These financial statements contain significant estimates with respect to impairment charges, collateral valuation and the fair value of securities. Actual results may differ from these estimates. The key priorities of the Bank in 2012 will be attention to the resolution of regulatory capital issue, management of the financial portfolio adjusting to the changing economic environment and maintaining the Bank‘s market share.

6. INTEREST INCOME

	2011 KM 000	2010 KM 000
Legal entities (legal entities)	7,739	6,018
Individuals	928	688
Interests on impaired loans (penalty interest)	309	191
Amortization of discount (Note 27)	246	187
Placement with domestic banks	56	39
Placement with foreign banks	48	24
The Central bank of B&H (on compulsory reserve)	35	17
Interest from financial assets held to maturity	12	-
Total	**9,373**	**7,164**

7. INTEREST EXPENSE

	2011 KM 000	2010 KM 000
Interest on deposits from companies	1,664	1,346
Interests on Government funds	631	518
Interests on other credit assets	570	365
Interest on deposits from individuals	190	73
Total	**3,055**	**2,302**

8. FEE AND COMMISSION INCOME

	2011 KM 000	2010 KM 000
Fees from payment transactions	816	472
Fees from off balance sheet transactions	256	274
Commission transactions	173	673
Fees from conversion transactions	53	17
Other fees	4	-
Total	**1,302**	**1,436**

9. OTHER OPERATING INCOME

	2011 KM 000	2010 KM 000
Income from heating services and rent	149	188
Other income	26	54
Total	**175**	**242**

10. PERSONNEL EXPENSES

	2011 KM 000	2010 KM 000
Net salaries	1,041	1,045
Taxes and contributions	643	644
Meal allowance and transportation costs	201	200
Other	136	138
Total	**2,021**	**2,027**

11. OTHER ADMINISTRATIVE EXPENSES

	2011 KM 000	2010 KM 000
Professional services	273	234
Advertising and entertaining	213	154
Supervisory Board and Audit Ccommittee fees	141	140
Energy costs	122	163
Material and small inventories costs	113	91
Court and administrative taxes	84	72
Maintenance	77	47
Other costs	303	293
Total	**1,326**	**1,194**

12. IMPAIRMENT OF RECEIVABLES AND PROVISIONS

	2011 KM 000	2010 KM 000
Impairment of loan receivables (Note 19)	2,597	1,269
Increase in provision for possible losses in commitments and contingencies (Note 29)	90	17
Decrease in impairment for possible losses on other assets (Note 22)	4	(4)
Decrease in impairment for possible losses on placements in banks (Note 18)	(11)	(1)
Increase in impairment for financial assets available for sale	-	3
Total	**2,680**	**1,284**

13. INCOME FROM COLLECTED WRITTEN OFF RECEIVABLES

	2011 KM 000	2010 KM 000
Principal	-	61
Interest	-	41
Total	**-**	**102**

14. INCOME TAX

	2011 KM 000	2010 KM 000
Income before tax	**1,634**	**1,604**
Non-deductible expenses	916	276
Taxable income	**2,550**	**1,880**
Tax at the domestic income tax rate of 10%	255	188
Tax expense for the year	**255**	**188**
Effective tax rate	**15.60**	**11.72**

15. EARNINGS PER SHARE

	2011 KM 000	2010 KM 000
Net profit	1,379	1,416
Less: Dividends on preferred shares	(311)	(310)
Subtotal:	*1,068*	*1,106*
Weighted average number of ordinary shares outstanding (000)	162	162
Basic earnings per ordinary share in KM	**6.59**	**6.82**

16. CASH AND BALANCES WITH BANKS

	31/12/2011 KM 000	31/12/2010 KM 000
Current account with the Central Bank of Bosnia and Herzegovina	6,167	14,792
Cash on hands in domestic currency	331	180
Cash on hands in foreign currency	157	206
Total	**6,655**	**15,178**

17. OBLIGATORY RESERVE WITH THE CENTRAL BANK

	31/12/2011 KM 000	31/12/2010 KM 000
Obligatory reserve	7,934	5,944
Specific reserve by Banking Law, article 42 a.(Note 26)	1,366	1,293
Total	**9,300**	**7,237**

Minimum obligatory reserve is calculated as a percentage of the average amount of total deposits and borrowings for each working day during 10 calendar days following the period of maintaining the obligatory reserve. The rates of minimum obligatory reserve were 10% of total short-term deposits and borrowings and 7% of total long-term deposits and borrowings.

17. OBLIGATORY RESERVE WITH THE CENTRAL BANK (CONTINUED)

In accordance with Law on banks (article 42 a.), the Bank is obliged to hold 50% of daily balance of received payments from public funds, deposits and transactions for budgetary and off budgetary funds in cash as specific reserve in Central Bank. This refers to funds and transactions of customer Agencija za vodno područje rijeke Save and Stari Grad and 50% of these funds amounted to KM 1,366 thousand as of 31 December 2011.

Average interest rate on assets kept up to minimum obligatory reserve within the Central Bank was 0.11%, and for the amount held at accounts of Central Bank of Bosnia and Hezregovina above the obligatory reserve interest rate was 0.14%. Cash held at the obligatory reserve account with the Central Bank of Bosnia and Herzegovina is not available for daily operations without specific approval from the Central Bank of Bosnia and Herzegovina and FBA.

18. PLACEMENTS WITH OTHER BANKS

	31/12/2011 KM 000	31/12/2010 KM 000
Loans:		
Balkan Investment Bank a.d. Banja Luka	4,000	-
Una banka d.d. Bihać	-	1,818
Subtotal:	**4,000**	**1,818**
Demand deposits in foreign currency:		
National Bank of Kuwait	3,992	2,447
Deutsche Bank AG, Germany	3,414	4,026
Raiffeisen Zentralbank AG, Austria	2,987	674
Zagrebačka banka, Croatia	1,845	111
Nova Ljubljanska banka, Slovenia	1,444	170
KBC Brussels, Belgium	130	303
AHLI United Bank London, United Kingdom	37	17
Subtotal:	**13,849**	**7,748**
Term deposits in foreign currency:		
AHLI United Bank London, United Kingdom	4,555	3,628
Zagrebačka banka, Croatia	1,992	-
Nova Ljubljanska banka, Slovenia	1,538	1,760
Subtotal:	**8,085**	**5,388**
Term deposits in domestic currency:		
ABS Banka d.d. Sarajevo	-	-
Total placements before provision	**25,934**	**14,954**
Impairment for bank placements:	**(80)**	**(93)**
Total	**25,854**	**14,861**

Annual interest rates for foreign currency placements can be presented as follows:

	2011 KM 000	2010 KM 000
	In % annually	**In % annually**
Placements in EUR	0.10 – 0.80	0.03 – 0.70
Placements in USD	0.08 – 0.20	0.01 – 0.05
Placements in KWD	0.14 – 0.50	0.20 – 0.63

18. PLACEMENTS WITH OTHER BANKS (CONTINUED)

Changes in impairment for placements with banks can be presented as follows:

	2011 KM 000	2010 KM 000
Balance at beginning of the year	**93**	**94**
Increase in impairment (Note 12)	80	-
Effects of changes in accounting policy (Note 3.1.1)	(2)	-
Decrease in impairment (Note 12)	(91)	(1)
Total	**80**	**93**

19. LOANS TO CUSTOMERS, NET

	31/12/2011 KM 000	31/12/2010 KM 000
Short-term loans:		
Legal entities	36,163	14,086
Individuals	293	45
Current portion of long-term loans	10,312	15,573
Subtotal:	***46,768***	***29,704***
Long-term loans:		
Legal entities	114,772	76,305
Individuals	15,505	9,817
Current portion of long-term loans	(10,312)	(15,573)
Subtotal:	**119,965**	**70,549**
Total loans before provisions	166,733	100,253
Provision for loans	(15,930)	(5,781)
Total	**150,803**	**94,472**

Bank signed two purchase contracts with Privredna Banka Sarajevo d.d. Sarajevo and Ministry of Finance of FB&H. Discount that represent difference between nominal value of portfolio and cashless reconciliation (payments); will be recognized as interest income at maturity, on individual basis repayment of separate loans (Note 27). Short-term loans are approved on period from 1 till 365 days. Majority of short-term loans in domestic currency have been authorised to customers for working capital. Long-term loans mostly have been approved to legal entities for different investment activities and for working capital.

Changes in provisions can be presented as follows:

	2011 KM 000	2010 KM 000
Balance at beginning of the period	**5,781**	**5,712**
Increase of provisions (Note 12)	4,784	3,671
Decrease of provisions (Note 12)	(2,187)	(2,402)
Effects from accounting policy changes (Note 3.1.1)	(1,397)	-
Transfer from off balance sheet (written off receivables)	8,747	-
Write off	(352)	(1,615)
Exchange rate differences	554	415
Total	**15,930**	**5,781**

19. LOANS TO CUSTOMERS, NET (CONTINUED)

Analysis of loans before provisions for impairment by industry:

	31/12/2011 KM 000	31/12/2010 KM 000
Agriculture, forestry, mining and energetic	52,830	30,238
Trade	46,467	30,209
Individuals	15,798	9,871
Services, finances, sport and tourism	14,675	8,058
Transportation and telecommunications services	11,911	6,086
Building industry	8,069	5,264
Administrative and other public institution	6,259	5,346
Other	11,615	5,762
Less: Deferred fees	(891)	(581)
Total	**166,733**	**100,253**

Weighted average interest rate is presented as follows:

	31/12/2011		31/12/2010	
	KM 000	Annual interest rate %	KM 000	Annual interest rate %
Legal entities	150.935	6,9 – 12	90,391	6 – 10
Individuals	15.798	5,95 – 7,99	9,862	5.45 – 10.5
Total:	**166.733**		**100,253**	

20. FINANCIAL ASSETS AVAILABLE FOR SALE

	% ownership	31/12/2011 KM 000	31/12/2010 KM 000
Privredna banka Sarajevo d.d. Sarajevo	8.14	2,470	1,800
Bamcard d.o.o. Sarajevo	0.10	3	3
		2,473	1,803
Provisions for impairment		-	(36)
Total		**2,473**	**1,767**

Shares are estimate at fair value because of its trading on Sarajevo stock exchange d.d. Sarajevo from 2008. In accordance with Board statement, the Bank has accomplished all contracted liabilities from purchase contract between Privredna banka d.d Sarajevo and Ortačka grupa X-25, related to paid in capital in amount of KM 30 millions. With its investment, Bank participated with 6.9% in partnership.

20. FINANCIAL ASSETS AVAILABLE FOR SALE (CONTINUED)

Changes on provisions for assets available for sale can be presented as follows:

	2011 KM 000	2010 KM 000
Balance at beginning of the period	**36**	**33**
Increase of provisions (Note 12.)	-	3
Effects of accounting policy changes (Note 3.1.1)	(36)	-
Total	**-**	**36**

21. FINANCIAL ASSETS HELD TO MATURITY

On 30 September 2011, the Bank purchased 203 treasury notes of Federal Ministry of Finance with total value of KM 2,030 thousand (increased for interest in amount of KM 25 thousand). Nominal value of treasury notes is 10 thousand while 98.77% of nominal values was sales price. Estimated maturity date is 28 March 2012.

22. OTHER ASSETS, NET

Structure of other receivables is:

	31/12/2011 KM 000	31/12/2010 KM 000
Prepaid expenses	127	61
Assets available for sale (acquired collaterals)	-	153
Other assets	32	21
	159	235
Provisions for potential losses	(8)	(19)
Total	**151**	**216**

Changes in provisions for potential losses can be presented as follows:

	31/12/2011 KM 000	31/12/2010 KM 000
Balance at beginning of the period	**19**	**23**
Increase of provisions (Note 12.)	8	13
Decrease of provisions (Note 12.)	(4)	(17)
Effects of accounting policy changes (Note 3.1.1)	(15)	-
Total	**8**	**19**

23. TANGIBLE AND INTANGIBLE ASSETS

	Land KM 000	Building KM 000	Equipment KM 000	Software KM 000	Investments in progress KM 000	Total KM 000
Cost						
At 1 January 2010	**425**	**17,748**	**1,234**	**679**	**297**	**20,383**
- additions	-	-	215	38	503	756
- disposals	-	-	(117)	-	-	(117)
- transfer from/to	-	144	401	-	(545)	-
At 31 December 2010 - changed	**425**	**17,892**	**1,733**	**717**	**255**	**21,022**
- additions	-	94	86	44	234	458
- disposals	-	-	(7)	-	(39)	(46)
- disposals from/to	-	104	143	8	(255)	-
- adjustments	-	-	(5)	-	-	(5)
At 31 December 2011	**425**	**18,090**	**1,950**	**769**	**195**	**21,429**
Accumulated depreciation						
At 31 December 2010	**-**	**173**	**853**	**536**	**-**	**1,562**
- depreciation for 2010	-	232	130	37	-	399
- adjustments	-	-	11	-	-	11
- disposals	-	-	(107)	-	-	(107)
At 31 December 2010 – changed	**-**	**405**	**887**	**573**	**-**	**1,865**
- depreciation for 2011	-	233	195	42	-	470
- adjustments	-	-	(5)	-	-	(5)
- disposals	-	-	(6)	-	-	(6)
At 31 December 2011	**-**	**638**	**1,071**	**615**	**-**	**2,324**
Net carrying amount						
31 December 2010	**425**	**17,452**	**879**	**154**	**195**	**19,105**
1 January 2011	**425**	**17,487**	**846**	**144**	**255**	**19,157**

24. DUE TO OTHER BANKS AND FINANCIAL INSTITUTIONS

	Interest rate (p.a.)	31/12/2011 KM 000	31/12/2010 KM 000
Ministry of Finance FB&H (Foundation for sustainable development)	6-month. Euro LIBOR+1%	26,586	3,805
Kuwait Fund for Arabian economic development (KFAED)	2%	15,470	18,205
Maturity of liabilities is as follows:			
In first year		5,541	3,698
In second		6,794	3,748
In period from 3-5 years		19,087	11,589
After 5 years		10,634	2,975
Total		**42,056**	**22,010**

On 30 April 1997, Bank signed loan Agreement with Kuwait fund for Arabic economic development (KFAED) in amount of KWD 6,100,000 with interest rate 1.5% and 0.5% other costs annually. Since 31 December 2008, Bank has signed 4 amendments on loan agreement. The purpose of loans is financing of small and medium legal entities with maturity up to 7 years and with interest rate from 7.5% to 9.5% till 30 June 2006 and after that date from 7% - 9% annually. Government of Federation of Bosnia and Herzegovina is guarantor of executing Bank liabilities toward KFAED in accordance with guarantee contract approved by Federal Parliament, Decision number 20/99 dated on 21 July 1999 („Official Gazette FB&H“, number 38/99). As disclosed in Note 1, any change within the Bank ownership structure that is concerning percentage of ownership of Federation of Bosnia and Herzegovina, has to be approved by KFAED.

24. DUE TO OTHER BANKS AND FINANCIAL INSTITUTIONS (CONTINUED)

Supervisory Board and KFAED Board of directors had approved Memorandum of understanding dated on 14 November 2008, under which Bank started with accelerated repayments of loan 516, and new loan aprovement from Kuwait credit line have been suspended. Principal should be repaid in KWD in 14 unequal semi-annual instalments beginning on 15 January 2009 and with maturity on 15 January 2016.

On 27 September 2010 the Bank signed subordinated contract with Federal Ministry of Finance in B&H and Sustainable Development Foundation (ODRAZ). Initially, funds have been approved by World Bank for project of improving finance accessibility to small and medium legal entities. Repayment of funds is reconciled with collection of approved loans to final customers (maximum granted period of 120 months). During 2011 the Bank registered significant proceeds of approved assets from ODRAZ.

25. LIABILITIES TOWARD GOVERNMENT OF FB&H („FUND“)

Based on agreement from 1 March 2005, between Council of Ministry of B&H and the Entity's Governments, the Bank signed on 22 August 2005 „Agreement for permanent fund managing“ with Ministry of Finance of Federation of Bosnia and Herzegovina (Ministry) that is amended on 31 August 2007. In accordance with Agreement, Bank suffers credit risk for loans granted from fund and calculates annual interest rate of 2%. As of the date of this report, no actual interest payments have been made. So, the credit balance is increased because of accrued interest. In accordance with the Contract, the value of the Fund is increased till 28 February next year, for the amount of accrued interest. Under the Contract, the same is lasting until Bank has FBA licence and is doing its business in accordance with regular banks procedures. On 18 January 2012 proposal of Government decision, for increase of fund for approximately KM 3 millions from budget FB&H (payments for Japanese grant), have been adopted.

26. LIABILITIES TOWARD CUSTOMERS

	31/12/2011 KM 000	31/12/2010 KM 000
Demand deposits:		
Individuals:		
In domestic currency	1,274	765
In foreign currency	450	132
	1,724	897
Legal entities:		
In domestic currency	23,698	8,483
In foreign currency	3,959	9,749
	27,657	18,232
	29,381	***19,129***
Term deposits:		
Individuals:		
In domestic currency	1,767	615
In foreign currency	4,877	1,801
	6,644	2,416
Legal entities:		
In domestic currency	46,639	29,136
In foreign currency	10,757	1,101
	57,396	30,237
	64,040	**32,653**
Total	**93,421**	**51,782**

26. LIABILITIES TOWARD CUSTOMERS (CONTINUED)

Interest rate on demand deposits in domestic currency is 0.3% (2010-0.3%), respectively 0.2% (2010-0.2%) on demand deposits in foreign currency, unless otherwise stipulated by the contract. Interests on short-term deposits in 2011 had been from 0.3% till 6.00% (in 2010 2.2%-5.00%). In 2011, interest rates on long-term term deposits and deposits used as collaterals had been from 2.5% till 5.7%, respectively during 2010 from 3% till 6%.

Interest rates on demand deposits in KM and in foreign currency for individuals are 0.35%. Interest rates on short-term deposits for individuals and in EUR currency had been from 1.70% till 4% and for USD currency from 1.20% till 2.20%. In 2010 interest rates on long-term deposits in KM and EUR currency are 4.20% to 5.90% and for USD currency 2.50% till 3.10%. During 2010, on long-term deposits for individuals in all currencies (on period of 50 months) Bank agreed special interest rate of 5.75% annually.

On 1 November 2011, the Bank acquired licence from Agency for deposit insurance of FB&H.

27. LONG TERM ACCRUALS

	31/12/2011 KM 000	31/12/2010 KM 000
Accrued income from repurchased loans (discount) – Ministry of Finance of FB&IH (Željezara Zenica)	1,259	1,304
Accrued income from repurchased loans (discount) – PBS	1,079	1,271
Accrued income – Fenix d.o.o. Kladanj	50	59
Total	**2,388**	**2,634**

28. OTHER LIABILITIES

	31/12/2011 KM 000	31/12/2010 KM 000
Liabilities for employee benefits	103	-
Differed income	86	113
Income tax liability	67	71
Trade payables	47	124
Provisions (IAS 19)	19	-
Managed funds difference (Note 34)	22	411
Deferred income – repossessed collaterals (Note 23)	-	142
Other liabilities	2	12
Total	**346**	**873**

29. PROVISIONS FOR COMMITMENTS AND CONTINGENT LIABILITIES

	2011 KM 000	2010 KM 000
Balance at the beginning of the period	**264**	**247**
Increase of provisions (Note 12)	292	476
Decrease of provisions (Note 12)	(202)	(459)
Effects on accounting policy changes (Note 3.1.1)	(15)	-
Balance at the end of the period	**339**	**264**

30. SHARE CAPITAL

Share capital structure can be presented as follows:

	31/12/2011 KM 000		31/12/2010 KM 000	
	Number of shares	Ownership in %	Number of shares	Ownership in %
Ordinary shares:				
Ministry of Finance FB&H	23,100	14,26	23,100	14,26
ZIF “Naprijed” d.d. Sarajevo	15,718	9,70	-	-
Pobjeda – Rudet d.d. Goražde	10,716	6,61	8,220	5,07
Hamid Pršeš	8,545	5,27	6,990	4,3
Fond “Bošnjaci”	8,496	5,24	8,496	5,24
Koprom Handelsgesellschaft M.B.H.	5,766	3,56	16,176	9,98
Other (under 5% of ownership)	89,673	55,36	99,032	61,15
Total:	**162,014**	**100.00**	**162,014**	**100.00**
Preferred shares:				
RTM – TV1 d.o.o. Mostar	23,490	-	-	-
Ministry of Finance FB&H	22,136	-	64,536	-
ZIF CROBIH FOND d.d. Mostar	12,400	-	-	-
Others	45,106	-	38,596	-
Total:	**103,132**	**-**	**103,132**	**-**
Total share capital of the Bank:	**265,146**	**100.00**	**265,146**	**100.00**

On 31 December 2011 the nominal value of all shares is KM 100 (on 31 December 2010: KM 100). The owners of preferred shares do not have guaranteed right to dividends. However, if dividend is declared, they have priority in actual receipt of dividend payments over ordinary shareholders. Preference shareholders also have preferential rights to return capital in case of liquidation.

The Bank considers that it operates in a single business segment, and a single geographical segment, that is the provision of banking services in Bosnia and Herzegovina. The Bank’s shares are traded at the Sarajevo stock exchange (SASE).

31. COMMITMENTS AND CONTINGENT FINANCIAL LIABILITIES

Within regularly business activities, the Bank is participant in several court proceedings under refund of assets based on insurance instruments or not collected loan receivables, that includes interests and doubtful receivable costs from bank customers, as the other banks. The Management believes that pending court proceedings on 31 December 2011 will not have any significant losses for the Bank as consequence.

	31/12/2011 KM 000	31/12/2010 KM 000
Contingent liabilities		
Payable guarantees	9,017	4,358
Obligation guarantees	2,765	2,529
Total contingent liabilities	**11,782**	**6,887**
Commitments		
Unutilized approved loans	2,545	3,445
Framework agreements (risk free assets)	16,713	8,251
Total commitments	**19,258**	**11,696**
Total commitments and contingent financial liabilities	**31,040**	**18,583**

32. RELATED-PARTY TRANSACTIONS

Related parties, as defined by IAS 24, are those counter parties that represent:

- enterprises that directly, or indirectly through one or more intermediaries, control, or are controlled by, or are under common control with, the reporting enterprise. (This includes holding companies, subsidiaries and fellow subsidiaries);
- associates – enterprises in which the Bank has significant influence and which is neither a subsidiary nor a joint venture of the investor;
- individuals owning, directly or indirectly, an interest in the voting power of the Bank that gives them significant influence over the Bank, and anyone expected to influence, or be influenced by, that person in their dealings with the Bank;
- key management personnel, that is, those persons having authority and responsibility for planning, directing and controlling the activities of the Bank, including directors and officers of the Bank and close members of the families of such individuals; and
- enterprises in which a substantial interest in the voting power is owned, directly or indirectly, by any person described in (c) or (d) or over which such a person is able to exercise significant influence.

This includes enterprises owned by directors or major shareholders of the Bank and enterprises that have a member of key management in common with the Bank. In considering each possible related party relationship, attention is directed to the substance of the relationship, and not merely the legal form.

During analysing of each possible transaction with related party, attention is on essence of relationships not only on legal form.

	31/12/2011 KM 000	31/12/2010 KM 000
Receivables		
Loans approved to personnel and their familiarity members	1,688	1,365
Loans approved to shareholders with over 5% of ownership	562	589
Loans approved to Supervisory Board and Audit Committee and their familiarity members	50	130
	2,300	2,084
Investments		
Privredna banka Sarajevo d.d. Sarajevo	2,470	-
Treasury notes (Ministry of finance FBiH)	2,030	-
	4,500	-
Liabilities		
Ministry of Finance FB&H	34,321	35,589
Deposits of persons associated with the Bank and their family members (Management, Supervisory Board and partners)	585	500
	34,906	36,089
Income		
Income from approved loans to shareholders with 5%	23	35
Interest income from key personnel of Management and their familiarity members	15	22
Interest income (treasury notes Ministry of Finance FB&H)	12	-
Interest income from Supervisory Board and Audit Committee and their familiarity members	2	11
	52	68
Expenses		
Interest expense Ministry of Finance FB&H	631	518

During regularly business activities it had realized several bank transactions with related parties. These transactions have been performed under commercial conditions and terms with using market rates.

32. RELATED-PARTY TRANSACTIONS (CONTINUED)

Fees paid to Management members on key positions are:

	2011 KM 000	2010 KM 000
Salaries to directors and other key personnel of Management	335	310
Taxes and contributions	231	214
Fees to Supervisory Board	81	101
Fees to Audit Committee	29	39
Bonuses	-	2
Subtotal	**676**	**666**

33. MANAGED FUNDS

Funds managed by the Bank on behalf of individuals, trusts and other institutions are not assets of the Bank and, therefore, are not included in its balance sheet.

	2011 KM 000	2010 KM 000
Liabilities		
Goverment of Federacije Bosnia and Herzegovina	10,084	10,385
Goverment of Bosnia and Herzegovina	500	893
Međunarodni MG	141	210
Fond za izgradnju Kantona Sarajevo	116	123
Kanton Sarajevo	45	60
Total	**10,886**	**11,671**
Assets		
Loans approved to legal entities	9,781	9,970
Loans approved to individuals	1,083	1,290
Total	**10,864**	**11,260**
Current liabilities from managed funds activities (Note 28)	**22**	**411**

The Bank does not bear the risk for these placements and charges a fee for its services

34. FINANCIAL INSTRUMENTS

Capital risk management

The Bank‘s objectives when managing capital, which is a broader concept than the equity on the face of balance sheets are:

- To comply with the capital requirements set by the regulators of the banking markets;
- To safeguard the Bank‘s ability to continue as a going concern so that it can continue to provide returns for shareholders and benefits for other stakeholders; and
- To maintain a strong capital base to support the development of its business.

34. FINANCIAL INSTRUMENTS (CONTINUED)

Capital risk management (continued)

The Bank expects to maintain its debt to capital ratio. Solvency indicators were as follows:

	31/12/2011 KM 000	31/12/2010 KM 000
Debt (i)	167,600	105,576
Cash and cash equivalents	(15,955)	(22,415)
Net debt	151,645	83,161
Capital (ii)	45,698	43,541
Net debt to equity ratio	**3.32**	**1.91**

Debt (i) is defined as liabilities to banks and clients presented in detail in Notes 24, 25 and 26. Capital (ii) includes total share equity, share premium and accumulated gain. Capital adequacy and the use of regulatory capital are monitored daily by the Bank‘s management, employing techniques based on the guidelines developed by Banking Agency of Federation of Bosnia and Herzegovina (FBA) for supervisory purposes. The required information is filed with the FBA on a quarterly basis.

Banking Agency request from all banks: (a) to maintain minimum amount paid share capital of the bank in amount of KM 15 million; and (b) to maintain ratio net-capital and weighted assets risk as minimum 12%.

The Bank‘s net capital is divided into two tiers:

- Tier 1 capital or Core Capital: share capital (net of any book values of the treasury shares), share premium, retained earnings and reserves created by appropriations of retained earnings; and
- Tier 2 capital or Supplementary Capital: qualifying subordinated loan capital, other share capital, general reserves for credit losses and net profit of current year.

The risk-weighted assets are measured by means of a hierarchy of four weights classified according to the nature of – and reflecting an estimate of credit, market and other risks associated with – each asset and counterparty, taking into account any eligible collateral or guarantees. A similar treatment is adopted for off-balance sheet exposure, with some adjustments to reflect the more contingent nature of the potential losses.

The table below summarizes the composition of regulatory capital and the ratios of the Bank for the years ended 31 December.

34. FINANCIAL INSTRUMENTS (CONTINUED)

During those two years the Bank complied with all of the externally imposed capital requirements related to capital:

	2011 KM 000	2010 KM 000
Tier 1 capital		
Share capital	26,285	23,895
Legislative reserves	13,053	13,585
Accumulated profit	635	2,025
Intangible assets	(154)	(144)
Total qualifying Tier 1 Capital	***39,819***	***39,361***
Tier 2 capital		
Other share capital	2,882	2,620
General reserves	2,657	1,614
Net profit of the current year	1,379	1,416
Total qualifying Tier 2 Capital	***6,918***	***5,650***
Debit balances - investments	***(2,470)***	**-**
Total net-capital	**44,267**	**45,011**
Risk weighted assets	**162,862**	**127,745**
On Balance sheet	151,644	117,919
Off Balance sheet	11,218	9,826
Weighted operating risk	**6.956**	**-**
Capital adequacy ratio	**26.07%**	**33.52%**

Significant accounting policies

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognized, in respect of each class of financial asset, financial liability and equity instrument are disclosed in Note 3 to the financial statements.

Categories of financial instruments

	31/12/2011 KM 000	31/12/2010 KM 000
Financial assets		
Cash and cash equivalents (including Obligatory reserves with Central Bank)	15,955	22,415
Placements with other banks	25,854	14,861
Loans and advances, net	150,803	94,472
Financial assets available for sale	2,473	1,766
	195,085	**133,514**
Financial liabilities		
At amortized cost	170,160	108,210

34. FINANCIAL INSTRUMENTS (CONTINUED)

Financial risk management objectives

The Bank's Treasury function provides services to the business, co-ordinates access to domestic and international financial markets, monitors and manages the financial risks relating to the operations of the Bank through internal risk reports which analyse exposures by degree and magnitude of risks. These risks include market risk (including currency risk and fair value interest rate risk), credit risk, liquidity risk and cash flow interest rate risk.

Market risk

The Bank's activities expose it primarily to the financial risks of changes in foreign currency exchange rates and interest rates (see below). Market risk exposures are supplemented by sensitivity analysis. There has been no change to the Bank's exposure to market risks or the manner in which it manages and measures the risk.

Foreign currency risk management

The Bank undertakes certain transactions denominated in foreign currencies. Hence, exposures to exchange rate fluctuations arise. Exchange rate exposures are managed within approved policy parameters utilizing forward foreign exchange contracts. The carrying amounts of the Bank's foreign currency denominated monetary assets and monetary liabilities at the reporting date are as follows:

	Assets		Liabilities	
	31/12/2011 KM 000	31/12/2010 KM 000	31/12/2011 KM 000	31/12/2010 KM 000
EUR	51,864	27,091	50,164	18,917
KWD	15,690	13,370	15,505	18,245
USD	6,545	6,597	2,155	1,849
Other	61	15	-	-

Foreign currency sensitivity analysis
The Bank is mainly exposed to EUR. Since Convertible Mark (KM) is pegged to EUR, the Bank is not exposed to risk of change of EUR exchange rate EUR 1 = KM 1.95583). Change in the exchange rate would require the amendments of the law and approval by Parliamentary Assembly of Bosnia and Herzegovina. The following table details the Bank's sensitivity to a 10% increase and decrease in KM against USD and KWD. 10% is the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the reasonably possible change in foreign exchange rates.

	Effect USD ('000 KM)		Effect KWD ('000 KM)	
	31/12/2011	31/12/2010	31/12/2011	31/12/2010
Profit or (loss)	439	475	19	(488)

The analysis outlined above is used on open foreign currency position of the Bank, which includes all asset and liability items. If the currency position of a foreign currency is "long" (assets exceeding liabilities) and the exchange rate for this currency increases in relation to the KM, the Bank will experience a foreign exchange gain. If the currency position of a foreign currency is "long" (assets exceeding liabilities) and the exchange rate for this currency decreases in relation to the KM, the Bank will experience a foreign exchange loss. If the currency position of a foreign currency is "short" (liabilities exceeding assets) and the exchange rate for this currency increases in relation to KM, the Bank will experience a foreign exchange loss. If the currency position of a foreign currency is "short" (liabilities exceeding assets) and the exchange rate for this currency decreases in relation to KM, the Bank will experience a foreign exchange gain.

34. FINANCIAL INSTRUMENTS (CONTINUED)

Foreign currency risk management (continued)

The Bank takes on exposure to effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows.

The Bank monitors its foreign exchange (FX) position for compliance with the regulatory requirements of the Federal Banking Agency established in respect of limits on open positions. The Bank seeks to match assets and liabilities denominated in foreign currencies to avoid foreign currency exposures.

Interest rate risk management

The Bank is not exposed to interest rate risk because borrow assets by fixed interest rates. The risk is managed by the Bank by maintaining an appropriate mix between fixed and floating rate borrowings. The Bank‘s exposures to interest rates on financial assets and financial liabilities are detailed in the liquidity risk management section.

Interest rate sensitivity analysis
The sensitivity analyses below have been determined based on the exposure to interest rates for non-derivative instruments at the reporting period date. For floating rate liabilities, the analysis is prepared assuming the amount of liability outstanding at the reporting period date was outstanding for the whole year. A 50 basis point increase or decrease is used when reporting interest rate risk internally to key management personnel and represents management‘s assessment of the reasonably possible change in interest rates. If interest rates had been 50 basis points higher/lower and all other variables were held constant, the Bank ‘loss for the year ended 31 December 2011 would increase / decrease by KM 133 thousand (31 December 2010 for 12 thousand).

Credit risk management

The Bank takes on exposure to credit risk which is the risk upon credit approval and when counterparty will be unable to pay amounts in full when due. The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review. Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees.

Commitments arising from the issuance of letters of credit. Documentary letters of credit, which are written irrevocable undertakings by the Bank on behalf of a customer (mandatory) authorising a third party (beneficiary) to draw drafts on the Bank up to a stipulated amount under specific terms and conditions, are collateralised by the underlying shipments of goods to which they relate and therefore have significantly less risk. Cash requirements under open letters of credit are considerably less than the commitments under issued guarantees or stand-by letters of credit. However, the Bank records provisions against these instruments on the same basis as is applicable to loans.

Commitments to extend credit, unused loan commitments, unutilised overdrafts and approved overdraft loans. The primary purpose of commitments to extend credit is to ensure that funds are available to a customer as required. Commitments to extend credit represent unused portions of authorisations to extend credits in the form of loans, guarantees or stand-by letters of credit. Commitments to extend credit issued by the Bank represent issued loan commitments or guarantees, unused portions of and approved overdrafts loans. Commitments to extend credit or guarantees issued by the Bank, that are contingent upon customers maintaining specific credit standards (including the condition that a customer’s solvency does not deteriorate) are revocable commitments. Irrevocable commitments represent unused portions of authorised loans and approved overdraft facilities because they result from contractual terms and conditions in the credit agreements.

34. FINANCIAL INSTRUMENTS (CONTINUED)

Credit risk management (continued)

Financial assets

31 December 2011	Total gross carrying amount KM 000	Unimpaired assets KM 000	Individually impaired assets KM 000	Impairments for losses (individually) KM 000	Impairments for losses (collectively) KM 000	Total net carrying amount KM 000
Cash and balances with banks	6,655	6,655	-	-	-	6,655
Obligatory reserve with Central Bank	9,300	9,300	-	-	-	9,300
Placements with other banks	25,934	21,934	4,000	(80)	-	25,854
Loans and receivables	166,733	23,839	142,894	(11,704)	(4,226)	150,803
Financial assets available for sale	2,473	2,473	-	-	-	2,473
Financial assets held to maturity	2,030	2,030	-	-	-	2,030
	213,125	**66,231**	**146,894**	**(11,784)**	**(4,226)**	**197,115**
31 December 2010						
Cash and balances with banks	15,178	15,178	-	-	-	15,178
Obligatory reserve with Central Bank	7,237	7,237	-	-	-	7,237
Placements with other banks	14,954	13,136	1,818	(92)	(1)	14,861
Loans and receivables	100,253	72,134	28,119	(4,430)	(1,351)	94,472
Financial assets available for sale	1,802	1,802	-	-	(36)	1,766
	139,424	**109,487**	**29,937**	**(4,522)**	**(1,388)**	**133,514**

Credit exposure and collateral

31 December 2011	**Credit risk exposure**			
Description	**Loans KM 000**	**Unutilized credit assets and unutilized overdraft limits KM 000**	**Commitments / guarantees KM 000**	**Fair value of collateral KM 000**
Legal entities	150,935	2,545	11,782	
Individuals	15,798	-	-	
Total	**166,733**	**2,545**	**11,782**	**330,299**
31 December 2010				
Legal entities	92,209	3,445	6,887	303,839
Individuals	9,862	-	-	25,491
Total	**102,071**	**3,445**	**6,887**	**329,330**

Fair value of collateral

	31/12/2011 KM 000	**31/12/2010 KM 000**
Assets	313,941	306,430
Deposits	12,580	6,431
Guarantees	3,778	16,469
	330,299	**329,330**

34. FINANCIAL INSTRUMENTS (CONTINUED)

Liquidity risk management

Liquidity risk is a measure of the extent to which the Bank may be required to raise funds to meet its commitments associated with financial instruments. The Bank maintains its liquidity profiles in accordance with regulations laid down by regulatory bodies of Bosnia and Herzegovina. The table below provides an analysis of assets and liabilities into relevant maturity groupings based on the remaining period from the balance sheet date to the contractual maturity date. It is presented under the most prudent consideration of maturity dates where options or repayment schedules allow for early repayment possibilities.

The Bank is exposed to daily calls on its available cash resources from overnight deposits, current accounts, maturing deposits, loan drawdown's, guarantees and from margin and other calls on cash-settled derivatives. The Bank does not maintain cash resources to meet all of these needs as experience shows that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty. The Bank sets limits on the minimum proportion of maturing funds available to meet such calls and on the minimum level of interbank and other borrowing facilities that should be in place to cover withdrawals at unexpected levels of demand.

Liquidity and interest risk tables
The following tables detail the Bank's remaining contractual maturity for its non-derivative financial liabilities. The tables have been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest date on which the Bank can be required to pay. The table includes both interest and principal cash flows.

The table of financial assets have been drawn up based on the undiscounted contractual maturities of the financial assets including interest that will be earned on those assets except where the Bank anticipates that the cash flow will occur in a different period.

34. FINANCIAL INSTRUMENTS (CONTINUED)

Liquidity risk management (continued)

Financial liabilities	Weighted average effective interest rate	Less than 1 month KM 000	1-3 months KM 000	3 months till 1 year KM 000	1-5 years KM 000	5+ years KM 000	Total KM 000
31/12/2011	%						
Non-interest bearing	-	172	-	-	-	-	172
Fixed interest rate instruments	2.420	36,798	911	45,835	31,167	32,440	147,151
Variable interest rate instruments	2.504	51	513	2,148	15,581	11,190	29,483
		37,021	**1,424**	**47,983**	**46,748**	**43,630**	**176,,806**
31/12/2010							
Non-interest bearing	-	3,470	-	-	-	-	3,470
Fixed interest rate instruments	2.43	10,054	2,060	25,064	25,763	33,979	96,920
Variable interest rate instruments	1.57	7,510	14	372	2,644	1,055	11,595
		21,034	**2,074**	**25,436**	**28,407**	**35,034**	**111,985**
Financial assets							
31/12/2011							
Non-interest bearing	-	20,663	-	-	-	-	20,663
Fixed interest rate instruments	9,09	7,448	13,711	38,405	90,859	45,422	195,845
Variable interest rate instruments	0.43	16,631	1	757	-	-	17,389
		44,742	**13,712**	**39,162**	**90,859**	**45,422**	**233,897**
31/12/2010							
Non-interest bearing	-	22,553	-	-	1,766	-	24,319
Fixed interest rate instruments	8.5	4,773	8,479	23,641	69,495	38,029	144,417
Variable interest rate instruments	0.28	12,906	-	-	-	-	12,906
		40,232	**8,479**	**23,641**	**71,261**	**38,029**	**181,642**
Difference 31/12/2011		**7,721**	**12,288**	**(8,821)**	**44,111**	**1,792**	**57,091**
Difference 31/12/2010		**19,198**	**6,405**	**(1,795)**	**42,854**	**2,995**	**69,657**

35. APPROVAL OF THE FINANCIAL STATEMENTS

These financial statements were approved by the Management Board on 19 January 2011:

Signed on behalf of the Bank

Hamid Pršeš	Enisa Hulusić
Director	Executive director for accounting, analyse and IT