NLB Banka d.d., Sarajevo

Financial Statements
For the year ended December 31, 2017

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Ernst & Young d.o.o. Sarajevo
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# Independent auditor's report

To the Shareholders of NLB Banka d.d., Sarajevo

## Report on the audit of the financial statements

### Opinion

We have audited the financial statements of NLB Banka d.d., Sarajevo (the Bank), which comprise the statement of financial position as at 31 December 2017, statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank as at 31 December 2017 and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

### Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report. We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

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

### Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the Auditor's responsibilities for the audit of the financial statements section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying financial statements.

1. Impairment of Loans

The carrying amount of loans to customers amounts to BAM 651 million (or 63% of total assets) as at 31 December 2017. Impairment is a highly subjective area due to the high level of judgment applied by the management in determining provisions. Experience from previous years has shown that banks can face serious losses in periods of recession and financial crisis, which can have material impact on the financial statements and pose threat to the going concern assumption. Mainly, the highest risk is related to assessment of individual provisions for loans.

We understood and evaluated the processes and controls for identifying impairment events within the loan portfolios, as well as the impairment assessment processes for loans.

We assessed the criteria for determining whether an impairment event had occurred and therefore whether there was a requirement to calculate an impairment provision. We tested a sample of performing loans with characteristics that might imply an impairment event had occurred to assess whether impairment events had been identified by management.

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| | |
|---|---|
| For further information, refer to Note 4.2. of the accompanying financial statements. | For a sample of individually impaired loans, we understood the latest developments at the borrower and the basis of measuring the impairment provisions and considered whether key judgments were appropriate given the borrowers' circumstances. We also re-performed management's impairment calculation. In addition, we tested key inputs to the impairment calculation including the expected future cash flows and their timing and valuation of collateral held, and discussed with management as to whether valuations were up to date, consistent with the strategy being followed in respect of the particular borrower and with the regulatory guidelines.<br><br>We assessed the adequacy of the disclosures included in Note 4.2. of the accompanying financial statements. |

## Responsibilities of management and Audit Committee for the financial statements

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

In preparing the financial statements, management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Audit Committee is responsible for overseeing the Bank's financial reporting process.

## Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

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# Independent auditor's report *(continued)*

**Auditor's responsibilities for the audit of the financial statements *(continued)***

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.
We also provide Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.
From the matters communicated with Audit Committee, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

DRUŠTVO ZA REVIZIJU
ERNST & YOUNG
SARAJEVO, d.o.o.

Zvonimir Madunić, Director

Tarik Alijagić

Tarik Alijagić, Licensed auditor

30 March 2018

Ernst & Young d.o.o. Sarajevo
Fra Anđela Zvizdovića 1
71000 Sarajevo

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*(All amounts are given in thousand BAM unless otherwise stated)*

| | Note | 2017 | 2016 |
|---|---|---|---|
| Income Statement | | | |
| Interest Income | 5a | 43,419 | 43,523 |
| Interest Expense | 5b | (8,166) | (10,413) |
| Net Interest Income | 5 | 35,253 | 33,110 |
| Impairment provisions for general credit risk and contingent credit and other losses (net) | 8 | (4,844) | (8,451) |
| Net Interest Income after provision for impairment | | 30,409 | 24,659 |
| Fee and commission income | 6a | 20,680 | 18,713 |
| Fee and commission expense | 6b | (7,045) | (6,225) |
| Foreign exchange gains | 7 | 697 | 1,135 |
| Other operating income | | 849 | 1,008 |
| Employees' expenses | 9a | (15,771) | (15,500) |
| General and administrative expenses | 9 | (11,755) | (11,431) |
| Other operating expenses | | (573) | (590) |
| Profit before income tax | | 17,491 | 11,769 |
| Income tax | 10 | (2,305) | (1,256) |
| Net profit for the year | | 15,186 | 10,513 |
| Other comprehensive income/loss: | | | |
| Profit/loss from financial assets available-for-sale | | 99 | 313 |
| Loss/Profit from provisions for severances (IAS 19) | | (84) | (113) |
| Other comprehensive Income/( loss) for the year | | 15 | 200 |
| Total comprehensive income for the year | | 15,201 | 10,713 |
| Earnings per Share (in BAM) | 23 | 39.68 | 27.47 |

Notes on pages 10 through 82 form an integral part of these financial statements.

*(All amounts are given in thousand BAM unless otherwise stated)*

| | Note | December 31, 2017 | December 31, 2016 |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and balances with the Central Bank of BiH | 11 | 238,335 | 230,214 |
| Placements with banks | 12 | 49,774 | 47,827 |
| Loans to customers | 13 | 651,423 | 611,800 |
| Financial assets available-for-sale | 14 | 74,989 | 62,263 |
| Tangible assets | 15 | 21,139 | 20,087 |
| Intangible assets | 16 | 552 | 438 |
| Other assets | 17 | 3,188 | 2,493 |
| **Total assets** | | **1,039,400** | **975,122** |
| **LIABILITIES** | | | |
| Banks' deposits | 18 | 10,317 | 17,190 |
| Customers' deposits | 19 | 836,961 | 795,915 |
| Borrowings | 20 | 43,222 | 32,720 |
| Other liabilities | 22 | 10,573 | 6,921 |
| Other provisions | 23 | 4,891 | 4,141 |
| **Total liabilities** | | **905,964** | **856,887** |
| **EQUITY** | | | |
| Share capital | 24 | 53,605 | 53,605 |
| Statutory reserves | | 64,934 | 54,421 |
| Revaluation reserves - financial assets available-for-sale | | 384 | 285 |
| Other revaluation reserves | | (673) | (589) |
| Retained earnings | | 15,186 | 10,513 |
| **Total equity** | | **133,436** | **118,235** |
| **Total equity and liabilities** | | **1,039,400** | **975,122** |

Notes on pages 10 through 82 form an integral part of these financial statements.

The Management has authorized these financial statements on 30 March 2018 and signed them accordingly:

| | | |
|---|---|---|
| Jure Peljhan | Denis Hasanić | Lidija Žigić |
| MB member | MB member | CEO |

*(All amounts are given in thousand BAM unless otherwise stated)*

| | Share capital | Statutory reserves | Revaluation reserves Financial assets AFS | Other revaluation reserves | Retained earnings | Total |
|---|---|---|---|---|---|---|
| Balance as of December 31, 2015 | 53,605 | 46,730 | (28) | (476) | 7,691 | 107,522 |
| Allocation of profit for 2015 | - | 7,691 | - | - | (7,691) | - |
| *Net profit for the year* | - | - | - | - | *10,513* | *10,513* |
| *Other comprehensive income* | - | - | *313* | *(113)* | - | *200* |
| Total comprehensive income | - | - | 313 | (113) | 10,513 | 10,713 |
| Balance as of December 31, 2016 | 53,605 | 54,421 | 285 | (589) | 10,513 | 118,235 |
| Allocation of profit for 2016 | - | 10,513 | - | - | (10,513) | - |
| *Net profit for the year* | - | - | - | - | *15,186* | *15,186* |
| *Other comprehensive income* | - | - | *99* | *(84)* | - | *15* |
| Total comprehensive income | - | - | 99 | (84) | 15,186 | 15,201 |
| Balance as of December 31, 2017 | 53,605 | 64,934 | 384 | (673) | 15,186 | 133,436 |

Notes on pages 10 through 82 form an integral part of these financial statements.

*(All amounts are given in thousand BAM unless otherwise stated)*

| | Note | 2017 | 2016 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Interest income from loans | | 37,660 | 37,849 |
| Fees and commission income from loans and commission from foreign exchange business | | 28,353 | 26,030 |
| Interest paid on deposits to customers | | (9,680) | (11,036) |
| Cash payments to employees and suppliers | | (33,200) | (32,488) |
| Payments upon off-balance contracts | | (107) | (34) |
| Incoming and outgoing payments under extraordinary items | | 429 | 614 |
| *(Increase)/Decrease in operating assets:* | | - | - |
| (Increase) in loans to customers | | (38,901) | (25,909) |
| *Increase/(Decrease) in operating liabilities:* | | | |
| Increase in clients' deposits and other liabilities from ordinary business activities | | 33,884 | 43,379 |
| Paid income tax | | (1,852) | (1,368) |
| Net cash from operating activities: | | 16,586 | 37,037 |
| **Cash flows from investing activities** | | | |
| Interest received from placements to financial institutions | | 985 | 872 |
| Dividends received | | 10 | 12 |
| (Purchase) of AFS financial assets, net | | (12,626) | (7,377) |
| (Purchase) of intangible assets | | (468) | (260) |
| (Purchase) of property and equipment | | (2,498) | (1,721) |
| Disposal of other assets | | 39 | 49 |
| Net cash (used in) investing activities | | (14,558) | (8,425) |
| **Cash flows from financing activities** | | | |
| Proceeds from issuance of shares | | - | - |
| Interest paid on borrowings | | (2,368) | (2,059) |
| Borrowings received | | 21,709 | - |
| Repayment of borrowings | | (11,251) | (13,837) |
| Payment of dividends | | - | (2) |
| Net cash used in financing activities: | | 8,090 | (15,898) |
| Net (decrease) increase in cash and cash equivalents: | | 10,118 | 12,714 |
| Cash and cash equivalents at the beginning of the year: | | 277,574 | 264,866 |
| Effects of changes in foreign exchange currency rates: | | 6 | (6) |
| Cash and cash equivalents at the end of the year: | | 287,698 | 277,574 |

Cash and cash equivalents include cash in hand and balances on accounts with the Central Bank of BiH (*Note 11*), and cash on accounts with other banks (Note 12) without placements to banks with maturity more than 30 days (*Note 4*), without related accrued due and not due interests and commissions

| | Note | 2017 | 2016 |
|---|---|---|---|
| Cash and balances with the Central Bank of BiH | 11 | 238,335 | 230,214 |
| Placements with banks | 12 | 49,774 | 47,827 |
| *Less:* | | | |
| Cash equivalent with maturity more than 30 days | | (411) | (467) |
| Total | | 287,698 | 277,574 |

Notes on pages 10 through 82 form an integral part of these financial statements.

## 1. General information

NLB Banka d.d., Sarajevo (hereinafter: the Bank) is a bank of universal type that has constantly operated through different ways of organization for over a hundred years. The Bank became a separate legal entity, a shareholders' company, on April 1, 1990.

The Bank was initially registered with the Registry of Companies with the Cantonal Court in Tuzla, and today at the Municipal Court in Sarajevo, and with the Registry of the Securities Commission of the Federation of BiH, with all relevant data and permissions issued by the Banking Agency of the Federation of BiH (hereinafter: FBA and other relevant bodies.

The Meeting of Bank Shareholders on September 16, 2015 issued the Decision to change the seat address and the name of the Bank, pursuant to which the Bank's headquarters was relocated from Tuzla to Sarajevo, to the address Džidžikovac 1. Following the above change, the name of the Bank was also changed from NLB Banka d.d., Tuzla to NLB Banka d.d., Sarajevo.
On November 5, 2015 the Municipal Court in Sarajevo issued a Decision on changes in the data, by which the change in the name and headquarters of the Bank were entered in the Company Register.
Upon a decision by the Supervisory Board adopted on November 8, 2016, new Bank Management was appointed, pursuant to which on January 4, 2017 the Municipal Court in Sarajevo passed the Decision on change of information, under which a change of persons authorized to represent the Bank as of January 1, 2017 was made.

The Bank operates directly or through its organisational units:
a) Branch Office Tuzla with its Sub-Branch Office in Lukavac and Business Offices Centar, Slatina, Irac, and Sjenjak
b) Branch Office Sarajevo with its Sub-Branch Office in Goražde and Business Offices Centar, Pofalići, Ilidža, Markale, Alipašino Polje, Ferhadija and Dobrinja,
c) Branch Office Mostar with its Sub-Branch Offices in Čapljina, Široki Brijeg and Ljubuški and Business Offices Centar and Rondo,
d) Branch Office Živinice with its Sub-Branch Offices Banovići and Kladanj,
e) Branch Office Kalesija with its Sub-Branch Offices Sapna and Teočak,
f) Branch Office Gradačac with Sub-Branch Offices Srebrenik, Brčko, Čelić, Orašje and Odžak,
g) Branch Office Gračanica with Sub-Branch Doboj Istok and Business Office Klokotnica,
h) Branch Office Zenica with Sub-Branch Offices Travnik, Vitez and Tešanj,
i) Branch Office Bihać with its Sub-Branch Office Cazin.

Through its Head Office in Sarajevo and well-developed network the Bank provides a wide range of financial and consulting services as follows:
1. Receiving of all types of money deposits and other monetary assets;
2. Granting and taking loans and financial leasing;
3. Issuing guarantees and all forms of guarantees;
4. services in internal and international payments and money transfers, in accordance with special regulations;
5. Buying and selling of foreign currencies and precious metals;
6. Issuing and managing means of payment (including credit cards, travel and bank cheques);
7. Financial leasing;
8. Buying, selling and collecting receivables (factoring, forfitting and others);
9. Purchase and sale of money market instruments and capital for its own or somebody else's account;
10. Purchase and sale of securities (brokering-dealership);
11. Managing portfolio of securities and other valuables;
12. Securities market support operations, agent operations and issuance of shares, in accordance with regulations governing the securities market;
13. Investment consulting and custody operations;
14. Financial management and consulting services;
15. Data collection services, preparing analysis and providing information on the creditworthiness of legal and natural persons who independently carry out the registered business activity;
16. Safe deposit box lease;
17. Insurance intermediary services in accordance with regulations governing insurance intermediary services; except liability insurance for motor vehicles;
18. other operations that support concrete banking activities.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 1. General information *(continued)*

### Bank's shareholders

| | December 31, 2017 | | December 31, 2016 | |
|---|---|---|---|---|
| | Amount in BAM | % | Amount in BAM | % |
| Nova Ljubljanska banka d.d., Ljubljana, Slovenia | 52,177,300 | 97.34 | 52,177,300 | 97.34 |
| Others | 1,427,860 | 2.66 | 1,427,860 | 2.66 |
| Total | 53,605,160 | 100.00 | 53,605,160 | 100.00 |

The headquarters of the Bank is at Džidžikovac 1, 71000 Sarajevo, Bosnia and Herzegovina.
The majority owner of the Bank is Nova Ljubljanska banka d.d., Ljubljana, with 97.34% of share capital as of December 31, 2017, which is also ultimate owner of the Bank.

### Employees

As of December 31, 2017, NLB Banka d.d., Sarajevo had 459 employees (in 2016: 444 employees).

*(All amounts are given in thousand BAM unless otherwise stated)*

## 1. General information *(continued)*

### The Supervisory Board

| | | |
|---|---|---|
| President | Blaž Brodnjak | 1.1.2017-29.5.2017 |
| Deputy President | Andreas Burkhardt | 1.1.2017-29.5.2017 |
| Member | Aleksander Kovač | 1.1.2017-29.5.2017 |
| | | 30.5.2017-5.10.2017 |
| Member | Ayda Šebić | 1.1.2017-29.5.2017 |
| Member | Suzana Žigon | 1.1.2017-29.5.2017 |

31/12/2017:

| | | |
|---|---|---|
| President | Blaž Brodnjak | 30.5.2017-29.5.2021 |
| Deputy President | Boštjan Kovač | 30.5.2017-29.5.2021 |
| Member | Igor Zalar | 6.10.2017-29.5.2021 |
| Member | Ayda Šebić | 30.5.2017-29.5.2021 |
| Member | Dragan Kovačević | 30.5.2017-29.5.2021 |

### Audit Committee

| | | |
|---|---|---|
| President | Tatjana Jamnik Skubic | 1.1.2017-1.6.2018 |
| Member | Nikolina Lilek | 1.1.2017-31.10.2017 |
| Member | Marko Jerič | 1.1.2017-31.10.2017 |
| Member | Barbara Deželak | 1.1.2017-1.6.2018 |
| Member | Nataša Simčič | 1.1.2017-1.6.2018 |

31/12/2017:

| | | |
|---|---|---|
| President | Tatjana Jamnik Skubic | 1.1.2017-1.6.2018 |
| Member | Suzana Žigon | 1.11.2017-1.6.2018 |
| Member | Barbara Deželak | 1.1.2017-1.6.2018 |
| Member | Nataša Simčič | 1.1.2017-1.6.2018 |
| Member | Zoran Blagojević | 1.11.2017-1.6.2018 |

### The Board of Directors

| | | |
|---|---|---|
| President of the Board | Lidija Žigić | 1.1.2017-31.12.2020 |
| Board member | Denis Hasanić | 1.1.2017-31.12.2020 |
| Board Member | Jure Peljhan | 1.1.2017-31.12.2020 |

| | |
|---|---|
| Head internal auditor | Elma Spahović |
| Secretary of the Bank | Amela Dizdarević-Bulja |

## 1. General information *(continued)*

### Memberships of members of Supervisory Board and Board of Directors of the Bank in other affiliated and unaffiliated entities

Blaž Brodnjak, President of the Supervisory Board
1. NLB d.d., Ljubljana, CEO
2. NLB Banka a.d., Banja Luka, President of the Supervisory Board
3. NLB Banka a.d., Skopje, President of the Supervisory Board
4. NLB Vita d.d., member of the Supervisory Board
5. Bank Association of Slovenia, President of the Supervisory Board

Boštjan Kovač, Deputy President of the Supervisory Board
1. NLB Banka a.d., Banja Luka, Deputy President of the Supervisory Board
2. NLB Leasing d.o.o. Sarajevo, Deputy President of the Supervisory Board

Igor Zalar, Member of the Supervisory Board
1. NLB Banka a.d., Banja Luka, member of the Supervisory Board

Ayda Šebić, Member of the Supervisory Board
1. NLB Banka a.d., Banja Luka, member of the Supervisory Board

Dragan Kovačević, member of the Supervisory Board
1. NLB Banka a.d., Banja Luka, member of the Supervisory Board

Jure Peljhan, Board member
1. Member of The Board of Directors of NLB Banka d.d. Priština (within which he is also the Chairman of the Risk Committee)

## 1. General information *(continued)*

### 1.1. Macroeconomic environment

In the first quarter of 2017, annual growth of nominal GDP was recorded, for the tenth quarter in a row. However, the significant growth of economic activity lacks due to the relatively weak infrastructure investment and slower implementation of structural reforms. The slowdown of industrial output growth on an annual level in the second quarter, compared to the previous quarter, suggests that no significant growth in economic activity can be expected in the second quarter.

GDP deflator points to a strong rise in prices of domestically produced goods and services in the first quarter of 2017. Inflationary pressures, measured by consumer price index, continued in the second quarter, but in somewhat lower intensity (the latest available data from the Statistics Agency show that the CPI for November 2017 was higher by 5.1 index points compared to the same month of the previous year).

Administrative data show a continuing trend of declining unemployment rate and increasing employment rate. The marked decline in unemployment can be explained, among other things, by the growth of the number of pensioners as well as by negative demographic changes. Employment growth is the result of higher economic activity of individual businesses, and increased control of the employee's working status. According to the Labour Force Survey, conducted in accordance with the recommendations of the International Labour Organization (ILO), the unemployment rate was 20.5% at the end of 2017. Although modest, the annual average net nominal wage growth is also recorded.

External debt of the government sector continued to decline, and in the second quarter it has been at its lowest level since the mid 2014. The collection of indirect tax revenues, which constitute the main source of funds for external debt servicing, continues to grow at the annual level in the first half of the year.[1]

As a result of its analysis, on September 8, 2017 the rating agency Standard & Poor's confirmed the sovereign credit rating "B with stable outlook" to Bosnia and Herzegovina. In February 2016, the agency Moody's Investors Service confirmed Bosnia and Herzegovina's sovereign credit rating "B3 with stable outlook". [2]

In the first three quarters of 2017, the banking sector in the Federation BiH recorded growth in the balance sum, deposit and loan, as continuation of positive trends reflected in the growth of household savings, capital, profit and fall of non-performing loans in total loans. At the system level, a positive financial result has been recorded, and it can be concluded from all that the banking sector remains stable, adequately capitalized, and liquidity remains satisfactory.
The balance sheet of the banking sector at the end of the third quarter of 2017 amounted to KM 19.6 billion and was by 6.5% or KM 1.2 billion higher than at the end of 2016. The growth of the balance sum on the source side (liabilities) is mainly due to the growth of deposits, as well as of total capital and liabilities on borrowed loans, while the structure of assets had smaller changes related to key asset items: decrease of loan participation from 66.8% to 66.2% and the increase in participation of cash resources from 28.3% to 29.4%.
The credit quality indicators have improved in the first three quarters of 2017, as well as in the previous two years, which has particularly reflected in the legal sector. The growth of the credit portfolio, significantly lower inflow of new non-performing loans, as well as permanent write-offs, had a positive effect on the coefficient of participation of non-performing loans in total loans, which was reduced from 11.7% at the end of 2016, to 10.5% as at 30/09/2017.

Capital adequacy ratio of banking system as at 30/09/ 2017 is 15.4%, which is by 0.3 percentage points lower than at the end of 2016, but is still much higher than the statutory minimum (12%).
According to data from the balance sheet, in the Federation of BiH, in nine months of 2017, a positive financial result-profit of KM 232 million was achieved at the banking system level.[3]

The Bank Management believes that it has taken all necessary measures to support the sustainability and growth of Bank business in the present circumstances.

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[1] Bulletin 2 CBBiH 2017
[2] www.cbbh.ba
[3] Information on the banking system of the Federarion of Bosnia and Herzegovina September 30, 2017

## 1. General information *(continued)*

### 1.2. Impact on liquidity

Until the outbreak of the global financial and economic crisis, under the banks' normal operating conditions and a stable environment, liquidity risk was of secondary importance, i.e. credit risk was in the foreground. After the transfer of the global crisis and its negative influence on the financial and economic system in BiH, there was an increase in liquidity risk.
In order to overcome financial issues and to maintain liquidity, the Bank has continued with increased monitoring of liquidity risk, and it has regularly updated and adjusted liquidity plans in accordance with the market situation. The Bank is also constantly monitoring the deposits of major depositors, their maturity dates, and it communicates with such depositors on a regular basis.

In accordance with guidelines of the ALM Board of the NLB Group, the Bank is obligated to maintain target limits which are mandatory for all banks in the NLB Group:

- The share of non-banking liabilities in the balance sheet total (non-banking liabilities / total assets) - the limit is min 70% and the realization as at December 31, 2017 is 82.44%,
- Gross loans to non-banking sector / deposits of non-banking sector - should have a maximum coefficient of 110% (as of December 31, 2017 the gross loans and deposits ratio was 86.10% - the Bank fulfils the given limit),
- Net non-banking loans / non-banking deposits – the limit of max 100% was fulfilled with 77.71%.
- Liquidity coverage ratio (LCR) – internal limit of min 120% was fulfilled with 345.31%
- Net stable Funding ratio - internal limit of minimum 105% was fulfilled with 165.33%
- The share of non-pledged liquid reserves in unstable liabilities – internal limit of min 25% was fulfilled with 269.73%
- Excess of non-pledged liquid reserves in relation to the potential outflows in strong stress test (3 months) internal limit of minimum 100% was fulfilled with 138.22%.
- Capital adequacy ratio should be maintained at 13% (as of December 31, 2017 capital adequacy ratio was 15.20% - the Bank fulfils the given limit).

### Impact on borrowers

The transfer of the global economic crisis onto the territory of BiH has also influenced the core bank business, which is the granting of loans. The limiting factor of credits growth is, on the one hand, the availability of new resources, namely their increase, and on the other hand the increasing influence of the crisis on the whole of the BiH economy and the deterioration of the situation in the real economy.

### Impact on collaterals (especially on real estates)

In determining the amount of impairment for impaired loans, cash flows from collateral are taken into account in addition to regular cash flows. The calculation of cash flows from collateral is made for loans where no more than seven years has passed from the moment of initiating the court proceedings.

The market in the Federation of Bosnia and Herzegovina for many types of collaterals, especially real-estate property, has been severely affected by the recent turbulent volatility in global financial markets, resulting in a low level of liquidity for certain types of assets. As a result the actual realizable value of collaterals may differ from assessed during impairment assessment.

One of the most frequent types of security for the Bank in its operations is the mortgage on real property and pledge on movable property. Collateral eligibility ratios with reference to the value of exposure are defined under the Loan granting policy for non-financial enterprises of NLB dd and NLB Group, Collateral policy and Manual for exposure security, depending on investment maturity and on the credit rating of the customer.

The Bank regularly monitors the market value trend of collaterals.

## 1. General information *(continued)*

### 1.3. Fair value of financial assets and liabilities

The fair value of securities in the active market is based on current prices of supply and demand for financial assets or financial liabilities. When there is no active market for financial instruments the Bank has established fair value using various valuation techniques. The valuation techniques include the use of present independent market transactions between informed and acquainted parties, the analysis of discounted cash flows, and other valuation techniques commonly used by market participants. The valuation models reflect current market conditions at the measurement date which may not be representative of market conditions either before or after the measurement date.

## 2. Adoption of new and revised standards

### 2.1. Standards and interpretations in effect over the current period

The adopted accounting policies are in accordance with those from the previous financial year, except for the following changed IFRS adopted by the Bank as of January 1, 2017:

· IAS 12 Income Taxes (Amendments): Recognition of Deferred Tax Assets for Unrealised Losses
The objective of the Amendments is to clarify the requirements of deferred tax assets for unrealized losses in order to address diversity in practice in the application of IAS 12. The specific issues where diversity in practice existed relate to the existence of a deductible temporary difference upon a decrease in fair value, to recovering an asset for more than its carrying amount, to probable future taxable profit and to combined versus separate assessment. It is not expected that amendments to this standard will affect financial statements of the Bank.

· IAS 7 Statement of Cash Flows (Amendments): Disclosure
The objective of the Amendments is to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. The Amendments specify that one way to fulfil the disclosure requirement is by providing a tabular reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities, including changes from financing cash flows, changes arising from obtaining or losing control of subsidiaries or other businesses, the effect of changes in foreign exchange rates, changes in fair values and other changes. It is not expected that amendments to this standard will affect financial statements of the Bank.

· The IASB has issued the Annual Improvements to IFRSs 2014 – 2016 Cycle , which is a collection of amendments to IFRSs. It is not expected that amendments to this standard will affect financial statements of the Bank.

Ø IFRS 12 Disclosure of Interests in Other Entities: The amendments clarify that the disclosure requirements in IFRS 12, other than those of summarized financial information for subsidiaries, joint ventures and associates, apply to an entity's interest in a subsidiary, a joint venture or an associate that is classified as held for sale, as held for distribution, or as discontinued operations in accordance with IFRS 5.

### 2.2. Standards and interpretations published but not yet adopted

· IFRS 9: Financial instruments: Classification and Measurement

The standard is effective for annual periods beginning on or after January 1, 2018, with early application permitted. The final version of IFRS 9 Financial Instruments Recognition and Measurement, connects all three aspects of accounting of the financial instruments: classification and measurement, impairment, and hedge accounting, and replaces IAS 39. Except for hedge accounting, retroactive application is necessary, while providing comparative information is not mandatory. For hedge accounting, requirements are generally applied prospectively, with some limited exceptions. The Bank's Board of Directors has carried out an assessment of the effects of the first application of the standard as explained below.

Taking into account the scope of requirements of IFRS 9 and its effect on the overall banking system, the implementation of the standard was centrally managed by the parent bank. The Bank applied the new standard on January 1, 2018. In accordance with the requirements for transition to IFRS 9, the comparative data is not adjusted. Adjustment resulting from the adoption of IFRS 9 is recognized in retained earnings and other comprehensive income as of January 1, 2018.

## 2. Adoption of new and revised standards *(continued)*

### 2.2. Standards and interpretations published but not yet adopted *(continued)*

Classification and Measurement under IFRS 9

From the perspective of classification and measurement, the IFRS 9 requires that all debt financial assets are evaluated based on the combination of the business model of the Bank for asset management and contractual cash flow characteristics of instruments. Under IAS 39, measurement categories of financial assets are replaced with:
- Financial assets measured at amortized cost (AC),
- Financial assets at fair value through other comprehensive income (FVOCI),
- Financial assets not intended for trading, required at fair value through profit or loss (FVPL).

Financial assets are measured at amortized cost (AC) if they are held within the business model for the purpose of collection under contracted cash flows ("held for collection") and cash flows refer only to payment of principal and interest to the remaining debt per share.

Financial assets are measured by other comprehensive income (FVOCI) if they are held in the business model for the purpose of collection and trade under contractual cash flows ("held for collection and trade") and cash flows refer only to payment of principal and interest on the remainder of the principal debt. Effects of Financial Assets at Fair Value through Other Comprehensive Income (FVOCI) are recognized at fair value through the balance sheet and at the amortized cost (AC) in the income statement. Gains and losses, other than expected credit losses and foreign exchange conversions, are recognized in other comprehensive income, until the financial asset is discontinued. At the end of the recognition of a financial asset, cumulative gains and losses previously recognized in other comprehensive income are reclassified to the income statement.

All other financial assets are measured at fair value through profit or loss (FVPL), including financial assets within other business models such as financial assets managed at fair value or held for trading and financial assets with contractual cash flows which are not solely the payment of principal and interest on the remaining debt per principal.

Like IAS 39, IFRS 9 also includes the option of determining financial assets at fair value through profit or loss if this eliminates or significantly reduces the measurement or recognition inequalities that would otherwise arise from measuring assets or liabilities or recognizing gains or losses on a different bases.

Non-trading capital instruments may be irrevocably designated as FVOCI, without subsequent reclassification of gains or losses in the income statement.

The calculation of financial liabilities remains the same as in the application under IAS 39, except for the treatment of gains or losses arising from its own credit risk related to the obligations set forth in the FVPL. Such movements are shown in other comprehensive income (OCI) without subsequent reclassification in the income statement.

Assessment of business model of NLB Bank d.d., Sarajevo

The Business Model Assessment is based on reasonably expected scenarios without taking into account the "worst case" and "stressful" scenarios and can be summarized as follows:

- Given loans and deposits are included in the "held for collection" business model as the Bank's primary purpose for credit portfolio is to collect the contracted cash flows.

- The Bank manages debt securities under the "held for collection and trade" business model for the purpose of collection for contractual cash flows and the sale of financial assets, and forms part of the Bank's liquid reserves.

## 2. Adoption of new and revised standards *(continued)*

### 2.2. Standards and interpretations published but not yet adopted *(continued)*

Overview of instruments with the characteristics of contracted cash flows (SPPI test - exclusive payment of principal and interest on the remaining debt per share).

The second step in the classification of financial assets in "held for collection" and "held for collection and trade" portfolios refers to the estimate of whether the contracted cash flows are in accordance with the SPPI test. The amount of principal reflects fair value at initial recognition, reduced by subsequent changes, for example due to repayment. The interest rate must take into account only the time value of money, credit risk, other basic lending risks and a profit margin that is consistent with the basic lending characteristics.
The Bank measures the debt securities at fair value through other comprehensive income.
If cash flows introduce more than the minimum risk or volatility exposure that does not comply with the core credit characteristics, the financial asset is recognized at fair value through profit or loss (FVPL).

The Bank has reviewed the portfolio within the "held up to collection" and "held for collection and trade" model for standardized products at the product sample level and for non-standardized products at the level of individual exposure. The Bank has established a procedure for identifying SPPI as part of a regular investment process with defined responsibilities for primary and secondary control. A special emphasis has been put on new and non-standardized credit contract characteristics.

Upon transition to IFRS 9, as of January 1, 2018, the Bank has identified only one exposure that has not passed the SPPI test and is therefore required to be measured at fair value through profit or loss.

Impairment of financial instruments

IFRS 9 requires movement from incurred losses into the model of expected losses, demanding that the Bank should recognise not only credit losses incurred but also losses expected to incur in the future. Decrease for expected credit losses (ECL) is required for all loans and other debt financial assets, except financial assets held at fair value through profit or loss, together with loan liabilities and guarantee contracts.

Corrections are based on expected credit losses related to deterioration probability in the upcoming 12 months, except in case of a significant increase in credit risk from initial recognition, in case of which the corrections are based on deterioration probability during lifetime expected credit losses (LECL). When deciding whether the deterioration risk has significantly increased since the initial recognition, the Bank takes into consideration reasonable information that is relevant and available without unnecessary costs or efforts. This also includes quantitative and qualitative information and analyses based on historical information, experience and estimates of credit experts, also taking into account information on future events

Classification into stages:
The methodology for the ECL criteria definition for classification into STAGEs, criteria for transfer between stages, the calculation of risk indicators and model validation. Financial instruments are classified into stage 1, stage 2 and stage 3, based on the methodology for value decrease as described below:

- stage 1– performing portfolio: no significant increase of credit risk from initial recognition. The Bank would recognise corrections based on ECL for 12 months,
- stage 2 – unsatisfactory portfolio: significant increase of credit risk from initial recognition. The Bank would recognise corrections based on LECL, and
- stage 3 - poor portfolio: The Bank would recognise LECL for these financial instruments. The default definition ("default") is aligned with the FBA regulation.

## 2. Adoption of new and revised standards *(continued)*

### 2.2. Standards and interpretations published but not yet adopted *(continued)*

A significant increase in credit risk is assumed:

- when credit rating is decreased on the date of reporting compared to the credit rating of initial recognition,
- when financial assets have substantial arrears exceeding 30 days (days in arrears are also included in the credit risk assessment),
- if the Bank is expected to approve a postponing to the Borrower or
- if a credit item is on the "watch list".

ECL for stage 1 of financial instruments is calculated based on 12-month PD (probability of default) or shorter PD period, if financial assets reach maturity in less than 1 year. The 12-month PD already includes the macroeconomic shock effect. Losses from a value decrease in phase 1 are designed to reflect losses from value decreases incurred in the portfolio but not yet identified.

LECL for stage 2 of financial instruments is calculated based on PD during the lifetime (LPD), because their credit risk is significantly increased as of the moment of their initial recognition. This calculation is based on assessment of future events and takes into account several economic scenarios to identify potential losses related to macroeconomic forecasts.

For financial instruments in stage 3 are observed in accordance with Methodology of individual value adjustments and provisions. Exposures below the threshold of materiality receive collective booking using PD of 100%. The financial instrument will be transferred out of stage 3 if it no longer meets the criteria of decreased value credit after the interim period.

Group provisioning is calculated by multiplying the EAD (exposure in default) at the end of each month with corresponding PD and LGD (specify loss). Default Exposure (EAD) is defined as the sum of balance exposure and off-balance exposure multiplied by CCF (credit conversion factor). The results obtained for each month are discounted to the present time. For Exposure at Stage 1 Expected Credit Loss (ECL) takes only 12-month periods into account, while Stage 2 includes all potential losses up to the maturity date.

For purposes of estimating the LGD parameter, the Bank uses collateral HC (haircut) at each collateral level and URR (unsecured recovery rate) at the level of each segment of the client.

Information with reference to the future
The Bank will include information on the future both in the assessment of significant increase in credit risk and in the measurement of expected credit loss (ECL). Information being considered include macroeconomic factors (e.g. unemployment rate, GDP growth, interest rates and housing prices) and economic forecasts.
A recalculation of all parameters is performed once a year or more frequently, if the macro environment changes more frequently than in previous forecasts, in that case, all parameters are recalculated in line with new forecasts.

The Bank has evaluated the effects of measurement of the value of a financial asset in accordance with IFRS 9 in relation to IAS 39 under the assumptions that apply to the Agency's guidance for the application of IAS 39 in determining the occurrence of loss events, calculation of days past due as well as other assumptions. In accordance with this, the Bank has not identified significant effects on the Bank's capital or on key indicators.

## 2. Adoption of new and revised standards *(continued)*

### 2.2. Standards and interpretations published but not yet adopted *(continued)*

- IFRS 15 Revenue from Contracts with Customers

The standard is effective for annual periods beginning on or after January 1, 2018. IFRS 15 establishes a five- step model that will apply to revenue earned from a contract with a customer (with limited exceptions), regardless of the type of revenue transaction or the industry. The standard's requirements will also apply to the recognition and measurement of gains and losses on the sale of some non-financial assets that are not an output of the entity's ordinary activities (e.g., sales of property, plant and equipment or intangibles). Extensive disclosures will be required, including disaggregation of total revenue; information about performance obligations; changes in contract asset and liability account balances between periods and key judgments and estimates. It is not expected that amendments to this standard will affect financial statements of the Bank.

The Clarifications apply for annual periods beginning on or after January 1, 2018 with earlier application permitted. The objective of the Clarifications is to clarify the IASB's intentions when developing the requirements in IFRS 15 Revenue from Contracts with Customers, particularly the accounting of identifying performance obligations amending the wording of the "separately identifiable" principle, of principal versus agent considerations including the assessment of whether an entity is a principal or an agent as well as applications of control principle and of licensing providing additional guidance for accounting of intellectual property and royalties. The Clarifications also provide additional practical expedients for entities that either apply IFRS 15 fully retrospectively or that elect to apply the modified retrospective approach. It is not expected that amendments to this standard will affect financial statements of the Bank.

- IFRS 16 Leases

The standard is effective for annual periods beginning on or after January 1, 2019. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer ('lessee') and the supplier ('lessor'). The new standard requires lessees to recognize most leases on their financial statements. Lessees will have a single accounting model for all leases, with certain exemptions. Lessor accounting is substantially unchanged. It is not expected that amendments to this standard will affect financial statements of the Bank.

- IFRS 10 Consolidated Financial Statements and IAS 28 Investments in Associates: Sale of Assets between an Investor and its Associate or Joint Venture (Amendment)

The amendments address an acknowledged inconsistency between the requirements in IFRS 10 and those in IAS 28, in dealing with the sale or contribution of assets between an investor and its associate or joint venture The main consequence of the amendments is that a full gain or loss is recognized when a transaction involves a business, whether it is housed in a subsidiary or not. A partial gain or loss is recognized when a transaction involves assets that do not constitute a business, even if these assets are housed in a subsidiary. In December 2015 the IASB postponed the effective date of this amendment indefinitely pending the outcome of its research project on the equity method of accounting. It is not expected that amendments to this standard will affect financial statements of the Bank.

- IFRS 2: Classification and Measurement of Share-based Payment Transactions (Amendments)

The Amendments are effective for annual periods beginning on or after January 1, 2018 with earlier application permitted. The Amendments provide requirements on the accounting for the effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments, for share-based payment transactions with a net settlement feature for withholding tax obligations and for modifications to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled. It is not expected that amendments to this standard will affect financial statements of the Bank.

## 2. Adoption of new and revised standards *(continued)*

### 2.2. Standards and interpretations published but not yet adopted *(continued)*

- IFRS 4: Application of IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (Amendments)

The Amendments are effective for annual periods beginning on or after 1 January 2018. The amendments address concerns arising from implementing the new financial instruments Standard, IFRS 9, before implementing the new insurance contracts standard that the Board is developing to replace IFRS 4. The amendments introduce two options for entities issuing insurance contracts: a temporary exemption from applying IFRS 9 and an overlay approach, which would permit entities that issue contracts within the scope of IFRS 4 to reclassify, from profit or loss to other comprehensive income, some of the income or expenses arising from designated financial assets. It is not expected that amendments to this standard will affect financial statements of the Bank.

- IAS 40: Transfers of Investment Property (Amendments)

The Amendments are effective for annual periods beginning on or after January 1, 2018 with earlier application permitted. The Amendments clarify when an entity should transfer property, including property under construction or development into, or out of investment property. The Amendments state that a change in use occurs when the property meets, or ceases to meet, the definition of investment property and there is evidence of the change in use. A mere change in management's intentions for the use of a property does not provide evidence of a change in use. It is not expected that amendments to this standard will affect financial statements of the Bank.

- IFRS 9: Negative compensation subscription function (amendment)

The Amendments are effective for annual periods beginning on or after January 1, 2019 with earlier application permitted. Amendments allow for financial assets with a subscription function that allows or requires a contractual party to contract or to pay or receive reasonable compensation for earlier termination of the contract (so that from the perspective of the asset owner it can be "negative compensation") to be valued by at amortized cost or at fair value through other comprehensive income. It is not expected that amendments to this standard will affect financial statements of the Bank.

- IAS 28: Investments in Associates: Sale of Assets between an Investor and its Associate (Amendments)

The Amendments are effective for annual periods beginning on or after January 1, 2019 with earlier application permitted. Amendments relate to the measurement, specifically the impairment (value adjustment), long-term investments in affiliated companies and joint ventures, which essentially make up a "net investment" item in an associate or joint venture, should be governed by IFRS 9, IAS 28 or a combination of both. Amendments state that the Bank should apply IFRS 9 Financial Instruments, before applying IAS 28, to long-term investments for which the capitalization method does not apply. In applying IFRS 9, an entity does not take into account any adjustments to the carrying amount of long-term investments arising from the application of IAS 28. It is not expected that amendments to this standard will affect financial statements of the Bank.

- IFRIC interpretation 22: Foreign Currency Transactions and Advance Consideration

The Intepretation is effective for annual periods beginning on or after January 1, 2018 with earlier application permitted. The Interpretation clarifies the accounting for transactions that include the receipt or payment of advance consideration in a foreign currency. The Interpretation covers foreign currency transactions when an entity recognizes a non-monetary asset or a non-monetary liability arising from the payment or receipt of advance consideration before the entity recognizes the related asset, expense or income. The Interpretation states that the date of the transaction, for the purpose of determining the exchange rate, is the date of initial recognition of the non-monetary prepayment asset or deferred income liability.

## 2. Adoption of new and revised standards *(continued)*

### 2.2. Standards and interpretations published but not yet adopted *(continued)*

If there are multiple payments or receipts in advance, then the entity must determine a date of the transactions for each payment or receipt of advance consideration. It is not expected that amendments to this standard will affect financial statements of the Bank.

· The IASB has issued the Annual Improvements to IFRSs 2014 – 2016 Cycle, which is a collection of amendments to IFRSs. Standard amendments are applicable for periods beginning on or after January 1, 2018 for IFRS 1 First-time Adoption of International Financial Reporting Standards and IAS 28 Investments in Associates. Earlier application is permitted for IAS 28 Investments in Associates. It is not expected that amendments to this standard will affect financial statements of the Bank.

Ø IFRS 1 First-time Adoption of International Financial Reporting Standards: This improvement deletes the short-term exemptions regarding disclosures about financial instruments, employee benefits and investment entities, applicable for first time adopters

Ø IAS 28 Investments in Associates: The amendments clarify that the election to measure at fair value through profit or loss an investment in an associate or a joint venture that is held by an entity that is venture capital organization, or other qualifying entity, is available for each investment in an associate or joint venture on an investment-by-investment basis, upon initial recognition.

· IFRIC Interpretation 23: Uncertainty regarding the treatment of personal income tax
The Interpretation is effective for annual periods beginning on or after January 1, 2019, with earlier application permitted. Interpretation refers to accounting treatment of income tax, in circumstances where tax treatment involves uncertainty affecting the application of IAS 12. Interpretation provides guidance for the consideration of uncertain tax treatment (individually or in combination), potential tax examinations as well as appropriate methods for uncertainty and accounting coverage due to changes in circumstances and facts.

· The IASB has issued the Annual Improvements to IFRSs 2015 – 2017 Cycle, which is a collection of amendments to IFRSs. Amendments are applicable for the annual period beginning on or after January 1, 2019. It is not expected that amendments to this standard will affect financial statements of the Bank.

Ø IFRS 3 Business Combinations and IFRS 11 Joint Arrangements: The amendments to IFRS 3 clarify that when an entity obtains control of a business that is a joint operation, it remeasures previously held interests in that business. The amendments to IFRS 11 clarify that when an entity obtains joint control of a business that is a joint operation, the entity does not remeasure previously held interests in that business.

Ø IAS 12 Income Taxes: The amendments clarify that the income tax consequences of payments on financial instruments classified as equity should be recognized according to where the past transactions or events that generated distributable profits has been recognized.

Ø IAS 23 Borrowing Costs: The amendments clarify paragraph 14 of the standard that, when a qualifying asset is ready for its intended use or sale, and some of the specific borrowing related to that qualifying asset remains outstanding at that point, that borrowing is to be included in the funds that an entity borrows generally.

## 3. Summary of significant accounting policies

### 3.1. Statement of compliance

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by International Accounting Standards Board.

Accounting regulations applicable in the Federation are based on the provisions of the Law on accounting and auditing ("Law") (Official Gazette 83/09). Companies prepare and present their financial statements in accordance with International Accounting Standards ("IAS"), their amendments and interpretations ("Standard interpretations"), International Financial Reporting Standards ("IFRS") and their amendments and interpretations ("International Financial Reporting Interpretations") issued by International Accounting Standard Board ("IASB"), as translated and published by Association of accountants, auditors and financial employees in Federation (by the authorization of Accounting Commission of Bosnia and Herzegovina number 2-11/06). The decisions on publishing Standards number O-1/2-2017 dated 13 January 2017 and O-1/7- 2017 dated 24 May 2017 are binding for the periods starting 1 January 2017. Those decisions include IAS, IFRS and interpretations published by IFRS foundation in Blue book (2016 edition) chapter A and include all amendments and improvements published in 2016. Any subsequently standards or new or amended IFRS and IFRIC interpretations issued by the IASB subsequent to December 2016 have not yet been translated and published.

In preparation of these IFRS financial statements for the year ended December 31, 2017 the Bank has considered whether application of standards that have been issued by the IASB subsequent to and applicable for the current accounting period, but which were not translated and published in FBiH, results in a material departure from relevant applicable local accounting regulation.

The Bank has concluded that this is not the case and therefore in the opinion of the management these IFRS financial statements also satisfy the Bank's legal statutory requirement to publish financial statements in accordance with relevant applicable local accounting regulations.

### 3.2. Going concern basis

The financial statements are based on the assumption of going concern, which implies that the Bank will be able to continue as a going concern for the foreseeable future and will be capable of collecting receivables and covering liabilities in the ordinary course of business.

### 3.3. Basis for the preparation and presentation of financial statements

These statements have been prepared using the historical cost basis, except for financial assets and liabilities measured and presented at fair value.
Business activities are recorded on the date of their occurrence.

Fair value is the price which may be achieved by sale of an asset or would be paid for a transfer of a liability in the ordinary transaction between parties on the primary (or on the most favourable) market on the measurement date, regardless of whether the price is directly observed or estimated by application of the other techniques for value measurement. While estimating the fair value of assets or liabilities the Bank takes into consideration characteristics of assets or liabilities that the participants in the market would have taken into account when determining the price of assets or liabilities on the date of measurement. Fair value for measurement and/or for the purpose of disclosure in these financial statements is estimated on such a basis (apart for measurements which have some similarity to fair value measurement i.e. net realisable value according to IAS 2 or value in use according to IAS 36.

## 3. Summary of significant accounting policies *(continued)*

### 3.3. Basis for the preparation and presentation of financial statements *(continued)*

Furthermore, for the financial reporting purposes fair value indicators are divided into levels 1, 2 or 3, based on the degree to which the measurement of fair value can be viewed according to the importance of evaluating fair value in its entirety, as follows:

- Level 1 inputs are (unadjusted) quoted prices in active markets for identical assets or liabilities that the Bank can access at the measurement date;
- Level 2 inputs are inputs other than quoted market prices included within Level 1 which are observable for assets or liabilities, either directly or indirectly; and
- Level 3 inputs are unobservable input data for assets or liabilities.

The valuation techniques used for the measurement of fair value maximise the use of relevant observable inputs, while the use of unobservable inputs is minimised.
In cases where input data which is used for measurement of fair value of assets or liabilities can be classified in different levels of the fair value hierarchy, the measurement of fair value is classified fully in the appropriate level according to the lowest level inputs which are important for the overall measurement considered.

The Bank performs transfers or reclassifications among different fair value levels of hierarchy when input data used for the determination of the fair value of assets or liabilities are classified in a different level than the level in which the input data used for the previous measurement of fair value of that asset or liability are classified.
Reclassification from one level of hierarchy of fair value to another is required in cases when, during the measurement of fair value, inputs from one level are replaced by inputs from another level.

### 3.4. Functional and presentation currency

Financial statements are presented in Convertible Marks (KM or BAM). The Convertible Mark has a fixed exchange rate linked to the Euro (EUR 1 = KM 1.95583).

### 3.5. Use of estimates and judgments

The preparation of financial statements in accordance with IFRS requires the Board to use judgements, estimates and assumptions which have influence on the application of accounting policies and disclosed amounts of assets, liabilities, income and expenses. Actual results may differ from those estimates.

Estimates and related assumptions are reviewed on a regular basis. Changes in accounting estimates are recognized in the period in which these estimates were changed, and possibly in future periods, if affected by them.
Information on areas of significant uncertainty related to estimates and judgements used in the application of accounting policies, which have a significant influence on amounts disclosed in these financial statements, are disclosed in *Note 3.31.*

Accounting policies listed below were applied consistently to all periods presented in these financial statements.

### 3.6. Foreign Currencies

Assets and liabilities in foreign currencies are translated into the local currency using the exchange rate set by the Central Bank of Bosnia and Herzegovina on the last day of the reporting period.

Monetary items denominated in foreign currencies are translated using the closing exchange rate as at the reporting date. If several exchange rates are available, the forward rate is used at which the future cash flows represented by the transaction or balance could have been settled if those cash flows had occurred. Non-monetary items measured at historical cost denominated in foreign currency are disclosed using the exchange rate which was valid on the date of initial recognition.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 3. Summary of significant accounting policies *(continued)*

### 3.6. Foreign currencies *(continued)*

Foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the year-end translation of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of profit or loss.

All foreign exchange gains and losses recognised in the statement of profit or loss are presented in net amount within appropriate items.

Exchange rates used in financial statements are the official rates determined by the Central Bank of Bosnia and Herzegovina. On December 31, the average exchange rates were as follows:

| | 2017 | 2016 |
|---|---|---|
| Exchange rate | | |
| | BAM | BAM |
| USD | 1.63081 | 1.85545 |
| EUR | 1.95583 | 1.95583 |

### 3.7. Interest income and expense

Interest income and expense are recognized in the statement of comprehensive income for all interest bearing instruments on an accrual basis. Penalty interest income is accounted for on an accrual basis.
Calculation of interest for non-performing loans, i.e. for the loans which are overdue over 90 days in a materially significant amount, is suspended on the date when the loan becomes default, and all further calculations of such positions are recorded in off-balance sheet.

In accordance with IAS 39, the increase in the recoverable amount of non-performing receivables as a result of time passing by, in case there have been no changes in assessment of future cash flows, is recorded in the statement of profit or loss as interest income using the effective interest rate method (unwinding – *Note 5)*.

Interest is calculated in accordance with the regulations in force or in accordance with the contract between creditor and debtor. If stipulated by the contract, interest for deposits is added to the principal.

Loan origination fee income is deferred throughout the duration of the loan using the effective interest rate method. Income from loan origination fees is presented within the Interest income position.

### 3.8. Fee and commission income and expense

Fees and commissions are generally recognized on an accrual basis when the service has been provided. Fee and commission income are recognized for all services provided to the Bank's clients.

Fee and commission income includes fees for local and international payment operations, income from off-balance sheet operations, brokerage and dealing operations.

Fee and commission expenses relate to fees paid to the Central Bank of Bosnia and Herzegovina for local payments operations, SWIFT costs and costs of card operations.

Fee and commission expenses are recognized in the period in which they occurred.

### 3.9. Dividend Income

Dividends are recognised in the statement of profit or loss within the other income item when the shareholders' rights to receive dividends are established.

## 3. Summary of significant accounting policies *(continued)*

### 3.10. Employee compensations

In its regular operations, the Bank pays taxes and contributions on and from salaries, calculated from the gross salary, as well as meal allowances, transport allowances, and vacation bonuses in accordance with local legislation for its employees. These expenses are recorded in the statement of profit or loss in the period to which the salaries relate.

Employee benefits represent amounts the employer has to pay to the employees in accordance with laws, rulebooks and contracts, which also represents a basis for recording provisions in accordance with IAS 19
In accordance with NLB Group policies, every three years the Bank engages an external actuary for the employee benefits calculation, and furthermore, twice a year it has to perform an analysis of underlying information used in the calculation of provisions for employee benefits. Additional provisions are recorded in the following cases:

- when the number of employees increases by more than 10%,
- the amount of jubilee benefits or severance payments increases by more than 5%,
- when there is a significant decline in interest rates whose discount factor is used in calculations of the present value of provisions,
- when there have been changes in the legislation related to employee benefits.

The following benefits are recognised in the other comprehensive income/loss:

- empirical adjustments, i.e. differences between the prior actuarial assumptions and what was actually realized, and
- the effects of changes in actuarial assumptions referring to demographical (fluctuations of employees, mortality, etc.) and financial assumptions (e.g. changes in the discount rate, an increase in wages).

The effects of the recognition of benefits in other comprehensive income are presented in the statement of changes in equity within the position other comprehensive income / loss (other revaluation reserves

The Bank has made provisions for unused vacation days in 2017 using the Bank's average hourly rate method for each unused vacation day, and released the excess provisions in favour of income from impairment for unused vacation.

### 3.11. Taxation

Taxes are calculated in accordance with the laws and regulations of the Federation of Bosnia and Herzegovina, on the basis of profit or loss recognized in the profit or loss statement prepared in accordance with accounting standards.
Corporate income tax (current tax) for the reporting period is calculated in accordance with the Income Tax Law using the prescribed rate of 10% on taxable income for the reporting period.

The corporate income tax charge is an aggregate amount of current and deferred taxes.

For the purposes of financial reporting, any deferred tax is recognized on the temporary differences between the tax base of assets and liabilities and their financial reporting book values using the balance sheet method and the applicable tax rates in force. Deferred tax liabilities are fully recorded. Deferred tax assets are recognized to the extent that it is probable that they will be available for offset against the current tax liability in the future.

The book value of deferred tax assets is reviewed on every balance sheet date and decreased to the extent to which it is not certain anymore that the available amount of taxable income will be available to fully or partially utilise the balance of deferred tax assets. Deferred tax is calculated using the tax rates which will probably be applicable in the period when liability is settled or asset realized. Deferred tax is recorded as debit or credit in the income statement and in other comprehensive income except when it refers to items which directly credit or debit the principal, in which case the deferred tax is presented as part of the principal.
Deferred tax assets and liabilities are offset if they relate to items imposed by the same tax authorities and if the Bank intends to settle its current tax assets and liabilities on a net basis.

## 3. Summary of significant accounting policies *(continued)*

### 3.11. Taxation *(continued)*

The amount of deferred tax assets and liabilities is not material for financial statements as a whole.

The Bank is obliged to pay several indirect taxes which are presented within the other operating expenses in the statement of profit or loss.

### 3.12. Earnings per share

The Bank discloses basic and diluted earnings per share.

Basic earnings per share are calculated by dividing net profit or loss of the current period attributable to the ordinary shareholders of the Bank by the weighted average number of ordinary shares for the period.

During 2016 and 2017 there have been no dilution impacts.

### 3.13. Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with a maturity of less than 30 days, including cash and non-restricted balances with the Central Bank as well as other eligible securities and loans and advances to banks.

### 3.14. Due from other banks

Amounts due from other banks are recorded when the Bank places funds to counterparty banks, with no intention of trading with such non-derivative, non-quoted receivables, which become due on a fixed or subsequently determinable date.

### 3.15. Financial Assets

Financial assets originate from lending operations, foreign exchange related operations, deposits, and payments operations; they are also used in securities trading, the purchase and collection of receivables, and they are the result of other banking services.

Financial assets are recognized as of the date of settlement (settlement date) determined for that financial asset.

*Transaction costs* are incremental costs that are directly attributable to the acquisition, issue or decrease in financial instruments. An incremental cost is incurred upon rendering a transaction. Transaction costs include fees and commissions paid to agents (including employees acting as selling agents), advisers, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs.

*Amortised cost* is the amount at which the financial instrument was recognised at initial recognition less any principal repayments, plus accrued interest, and the amount at which the financial instrument was recognised less any write-down for incurred impairment losses. Accrued interest includes amortisation of transaction costs deferred at initial recognition and amortization of all premiums or discounts up to the maturity date by applying the effective interest rate. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discounts or premiums (including fees deferred at origination, if any), are not presented separately and are included in the carrying values in the statement of financial position (balance sheet).

3. Summary of significant accounting policies *(continued)*

3.15. Financial assets *(continued)*

*The effective interest rate method is a method*of calculation of the amortised cost of a financial asset or financial liability, and the allocation of interest income or interest expenditures over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, if appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. The effective interest rate discounts cash flows of variable interest instruments until the next interest re-pricing date, except for the premium or discount which reflects the credit spread over the floating rate specified in the instrument, or other variables that are not reset to market rates. Such premiums or discounts are amortised over the entire expected life of the instrument. The present value calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate.

The Bank classifies financial assets in following categories:
- Financial assets available-for-sale and
- Loans and receivables.

The basic difference between these categories is the approach to financial assets' measurement and recognition of fair value in financial statements.

*Financial assets available-for-sale*

Available-for-sale financial assets include assets that the Bank intends to hold for an indefinite period of time, which could be sold in response to needs for liquidity or changes in interest rates, exchange rates or funding prices, or share prices; these are assets that are not classified as loans and receivables, held-to-maturity investments or financial assets at fair value through profit or loss.

In this group are also classified financial assets that do not fulfil conditions to be classified as financial assets for trading.

Financial assets available for sale are initially recognized at cost on trading date.
These assets are subsequently measured at fair value and the difference is recognized as revaluation reserve in equity. Changes in the fair value of securities classified as available-for-sale are recognised in other comprehensive income.
In case of sale of assets available-for-sale, the accumulated gain or loss recognized in equity is transferred to the Bank's profit or loss as realised gain or loss.

Financial assets available for sale include investments in capital of separate legal entities (equity instruments) which, in absence of active market for these instruments, are recorded at the purchase cost (acquisition cost).

*Loans to customers*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

All loans and receivables are initially measured at fair value at the loan disbursement date and are recognized when the borrower receives cash.

Loans are initially measured in the statement of financial position to the amount of approved placements less principal paid and any value adjustment, and they are increased by accrued uncollected interest. After initial recognition loans are subsequently measured at amortized cost using the effective interest rate.

## 3. Summary of significant accounting policies *(continued)*

### 3.15. Financial assets *(continued)*

#### 3.15.1. Restructured financial resources

A restructured financial asset is a financial asset on which restructuring measures were taken.
Measures of restructuring include "concessions" to a debtor caused by economic and financial situations of the customer and his inability to service the debt under initially agreed terms and conditions.

Types of restructuring, i.e. possible changes in contractual terms and conditions which may appear individually, or in combination, are as follows:
- prolongation of maturity date or postponing the debt repayment;
- interest rate and/or other expenses reduction;
- decrease of debt as a result of agreement with the debtor and of owner's restructuring,
- conversion of debt in placement in debtor's capital,
- taking over of other assets (including cashing in per collaterals) for partial or full repayment of debt;
- other activities.

In case of debt restructuring, a part of the debt can be reduced or written off following the decision of a competent authority, as follows:
- in case of amendment to loan conditions, when the book value is higher than the present value of the restructured receivable;
- in case of decrease of the receivable, the difference between the initial book value of the receivable and the new, lower value of the receivable is recorded;
- in case of repossession of tangible assets in exchange for the receivable subject to restructuring, the difference between the higher book value of the restructured receivable and the fair value of the repossessed asset is recorded;
- in case of taking over of securities, capital investments, loans and other receivables in exchange for receivables which are subject to restructuring, the difference between the book value of restructured receivables and the purchase value or fair value of new receivables is recorded, whichever is lower.

### 3.16. Property and equipment

Property and equipment items are stated at historical cost less accumulated depreciation. Depreciation is calculated on a straight-line basis to write down the cost of such assets to their residual values over their estimated useful lives. Land and assets in construction are not depreciated. Applied depreciation rates are set for 2017 and 2016 as follows:

| | % |
|---|---|
| Buildings | 1.3% |
| Computers | 25% |
| Transport means | 15% |
| Furniture and other office equipment | 7-15% |

The period and amortisation method is reviewed once per year at the end of each business year. When the expected useful life significantly differs from the previous estimation, the corresponding change in the period of depreciation is required. This represents the change in accounting estimate and such change should be adequately accounted for in the financial statements.

For tangible assets the Bank periodically estimates whether there are indicators of impairment. Within such estimation process the Bank considers a number of indicators from internal and external sources. When the Bank finds that there are indicators of impairment in tangible assets, then the Bank initiates the process of estimation of recoverable value. Recoverable value is the value in use or the fair value reduced by cost of sale, whichever is higher.

## 3. Summary of significant accounting policies *(continued)*

### 3.16. Property and equipment *(continued)*

After assessing the value of the property owned by the Bank in 2017, for two business buildings it was estimated that their carrying values were higher than the recoverable amount and that their cost reduction was reduced in the total amount of 209 thousand BAM. On other tangible assets there were no indicators indicating change in value, and management believes that the fair value of this asset is approximately equal to the carrying amount.

In 2017 and 2016 there were no impairment indicators and the management believes that the fair value of these assets is close to their book value.

The overview of tangible assets in 2017 and 2016 is presented in *Note 15.*

*Leasehold improvements.* Leasehold improvements are capitalized and amortised by linear method during its life or during the lease period depending on whichever is shorter.

### 3.17. Intangible assets

*(a) Licences*
Acquired licences for computer software are measured at historical cost.
Amortisation is calculated using the straight-line method to allocate the cost of licences over their estimated useful lives.

*(b) Computer software*
Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised over their estimated useful lives.

Costs associated with developing or maintaining computer software programmes are recognised as an expense as incurred. Costs that are directly associated with the development of identifiable and unique software products controlled by the Bank are recognised as intangible assets insofar as they are expected to generate economic benefits that exceed costs within the time period beyond one year. Direct costs include the costs of the software development team that has developed the software and an appropriate portion of relevant overheads.
Computer software development costs recognised as assets are amortised over their estimated useful lives (5 years).

The overview of intangible assets in 2017 and 2016 is presented in *Note 16.*

### 3.18. Repossessed financial and non-financial assets

Repossessed assets represent financial and non-financial assets acquired by the Bank through the settlement of overdue loans. These assets are initially recognised at fair value when acquired (and they are recorded in other assets, other financial assets or inventories within other assets, depending on their nature and the Bank's intention in respect of recovery of these assets), and are subsequently re-measured and accounted for in accordance with the accounting policies for these categories of assets.

Assets classified for sale acquired by the Bank through the settlement of overdue loans is classified either as an IFRS 5 non-current asset held for sale - if it is a long term asset (mostly real estate), if it is available for immediate sale and if the sale in the next 12 months is probable; or it is classified in accordance with IAS 2 - if the short-term asset is acquired for the purpose resale in a short period (up to 12 months).

In accordance with the Decision of the Banking Agency of the Federation of BiH on minimum standards for credit risk management and the classification of bank’s assets, the Bank applies the concept of fair value, or realistic value when assessing repossessed assets received in exchange for full or partial debt repayment. For tangible assets for which a stable and active market exists, the fair value represents a value equal to the market value for such assets.

## 3. Summary of significant accounting policies *(continued)*

### 3.18. Repossessed financial and non-financial assets *(continued)*

In the absence of such a market, the fair value has to be established by an independent, formal and professional assessment. When it is not possible to reliably determine the fair value, i.e. uncontested and stable value of the acquired tangible assets, for bookkeeping purposes the Bank will apply only the technical value of BAM 1.
Receivables per repossessed assets remain in the balance sheet until sale proceeds are realised or until a permanent write-off is recorded provided there are no sufficient funds from the sale or other additional security. Repossessed tangible assets are classified as risk assets unless they are sold within one year.

Assets acquired in lieu of uncollected receivables may be used for regular Bank operations in accordance with the decision - such assets are recorded in the fixed assets register and depreciated.

The assets acquired through the collection of receivables, and let to third parties, are first recorded in own fixed assets and the same are subject to depreciation, and afterwards, based on contracts signed with lessees, income from the lease is generated.

### 3.19. Liabilities for guarantees

The Bank issues financial guarantees. Financial guarantees represent an irrevocable payment guarantee in case of a customer not being able to meet its liabilities to a third party, and they carry the same credit risk as loans. Financial guarantees are initially recognised at their fair value, usually in the amount of received fees. This amount is amortised on a straight line basis over the commitment period.

### 3.20. Deposits of clients, banks and other deposits

At initial recognition, received deposits are valued in accordance with corresponding documents which support the initial receipt of funds.
For a vista deposits and deposits without a defined maturity fair value is an amount payable on the reporting date. Estimated fair value of deposits with a fixed maturity is based on cash flows discounted by use of the currently offered interest rates on deposits with a similar remaining maturity date.

### 3.21. Liabilities for received loans, subordinated debts and other borrowings

Liabilities for received loans, subordinated debts and other borrowings are recognised initially at contracted value, which represents the amount received.
These liabilities are subsequently measured at amortised cost by application of the effective interest rate method; incurred transaction costs are recognised in the profit or loss of the current period.

### 3.22. Impairment of financial assets and off-balance sheet contingent liabilities

*a) Assets carried at amortised cost*

At each balance sheet date the Bank assesses whether there is objective evidence that a financial asset or groups of financial assets should be impaired.
It is considered that financial assets or group of financial assets are impaired when there is objective evidence of impairment which arises as a consequence of one or more loss events arising after the initial recognition of assets and if said events (losses) will surely impact on future estimated cash flows.
In accordance with the adopted methodology, the process of assessment of receivables' impairment is as follows:

3. Summary of significant accounting policies *(continued)*

3.22. Impairment of financial assets and off-balance sheet contingent liabilities *(continued)*

The Bank is individually assessing:
- Banks and exposure to central level of government,
- all clients with exposure on calculation date exceeding the threshold (BAM 100,000),
- all clients past due over 90 days,
- clients in default status.

Impairment (value decrease) is recorded in cases where the Bank has information on events which represent the objective evidence of the impairment of financial asset, or a group of assets, including:
- financial difficulties of the borrower,
- borrower's breach of contractual liabilities,
- restructuring of financial assets due to financial difficulties of the borrower; extension of principal and/or interest repayment period, postponing of principal and/or interest repayment, decrease in interest rate and/or other costs, partial write-off of receivable (principal and/or interest past due), repossession of other assets for purposes of partial or full repayment of receivable, introduction of grace period and other similar activities.
- possibility of bankruptcy or financial reorganisation of the borrower,
- measurable decrease of expected cash flows from the group of financial assets, occurred since the initial recognition of these financial assets, even when the decrease cannot be allocated to individual assets in the group, including: negative changes in debt repayment, worsening of economic conditions in industry branch, or negative economic conditions which influence the repayment of financial assets.

For off-balance sheet liabilities, provisions are recorded in the following cases:
- the occurrence of the past event which triggers Bank's present liability for payment (payment call and similar),
- there is more than 50% probability that the Bank will have to settle the liability, and
- when it is possible to adequately measure the amount of the liability representing loss and to form provisions in the same amount.

Receivables from clients, for which no evidence of impairment exists, or who the Bank considers will settle its liabilities in accordance with contractual amounts and deadlines, are included in the groups for collective assessment of impairment or provision.

The fully 100% collectable receivables group consists of receivables secured with first-class collaterals and for them it is not necessary to record impairment, or provisions either on an individual or collective level.

Newly approved receivables from clients that have active liabilities towards the Bank are treated in the following manner:

a. when the existing receivables have been individually assessed, the newly approved receivables shall also be individually assessed,
b. when the existing receivables have been collectively assessed, the newly approved receivables shall also be collectively assessed (provided that the total exposure is not higher than the individual assessment limit).

For receivables from clients, for which evidence of impairment exists, assessment is performed on individual level.

Individual assessment of impairment comprises the following steps:
- the review of contractual cash flows from the repayment plan,
- an estimate of the actual collection of receivables by amounts and time periods (i.e. future cash flows),
- the discounting of estimated future cash flows on present value is performed by applying the effective interest rate method (EIR),
- the calculation of the receivables collection rate, equal to the ratio of the present value of estimated cash flows and the present value of future cash flows,
- the amount of impairment is calculated on the basis of the receivables collection rate.

## 3. Summary of significant accounting policies *(continued)*

### 3.22. Impairment of financial assets and off-balance sheet contingent liabilities *(continued)*

For receivables which are examined collectively, the impairment assessment is carried out according to the following stages:

1. Forming groups of clients

For the purpose of forming a group allowance for impairment and provisions, risk assets and commitments by off-balance sheet items, which does not represent individually significant exposure, is divided into groups with similar characteristics with respect to credit risk exposure, as follows:

   1. groups of companies and private entrepreneurs,
   2. groups of private individuals.

Both groups of clients are further divided into five rating subgroups, based on their credit rating (A, B, C, D and E).

2. Group impairment percentages are applied for receivables sorted into different rating groups.

The loss is calculated as the difference between the book value and recoverable amount. . The recoverable amount represents the present value of expected cash flows from the collection of receivables based on contracts.

*b) Assessment of potential losses of financial assets in accordance with requirements of the Federal Banking Agency of the Federation of Bosnia and Herzegovina*

In accordance with the Instruction on the amended method of recording, documenting and reporting of provisions for credit losses, brought by the Banking Agency of the Federation of Bosnia and Herzegovina, the Bank continues to manage adequate internal records (off-balance evidence) which is in accordance with the Decision of Banking Agency of the Federation of Bosnia and Herzegovina on minimum standards for credit risk management and the classification of banks' assets.

The Bank is required to classify loans, placements and other balance and off-balance sheet exposures to risk into categories A, B, C, D and E in accordance with the assessment of collectability of loans and other placements, based on the regularity of repayment of debtors' liabilities, the debtor's financial position and collateral. The estimated amount of provisions for potential losses is calculated using the following percentages: 2% for loans classified into category A, 5% - 15% for the loans in category B, 16% - 40% on loans in category C, 41 - 60% on loans in category D and 100% on E category loans.

If the amount of loan loss provisions calculated in accordance with the Decision on minimum standards for credit risk management and classification of banks' assets is higher than the sum of IFRS provisions for total assets and loan provisions for off-balance items and previously formed loan loss provisions, the Bank shall treat such a difference as a missing balancing figure in loan loss provisions in accordance with the Decision. The determined amount of missing loan loss provisions, as per regulatory requirements, represents a deductible item in the Bank's capital adequacy calculation (Note 4.9.)

If the amount of provisions and the amount of loss provisions for off-balance items under IFRS is higher than the calculated amount of loan loss provisions per Decision, the Bank is not required to form special reserves for loan losses. The excess of provisions for certain clients cannot be used for offsetting the missing provisions for other clients.

In accordance with the Decision, the Bank cannot decrease the amount of previously formed loan loss provisions.

## 3. Summary of significant accounting policies *(continued)*

### 3.22. Impairment of financial assets and off-balance sheet contingent liabilities *(continued)*

#### c) *Assets carried at fair value*

At each reporting date the Bank assesses whether there is objective evidence that impairment indicators exist for a financial asset.

The fair value of financial assets available for sale is its quoted bid market price at the balance sheet date, without any deductions for selling costs.

If the market for a financial asset is not active (for unquoted securities also), or if, for any other reason, the fair value cannot be reliably measured using market price, the Bank determines fair value by using valuation techniques. These include the use of prices achieved in recent arm's length transactions between informed and willing parties, reference to other similar instruments and discounted cash flow analysis, with maximal use of market inputs and relying as little as possible on entity-specific inputs.

Where discounted cash flows are used, estimated future cash flows are based on the management's best estimate and the discount rate is a market rate valid as at balance sheet date for financial instruments with similar terms and conditions. Where a pricing model is used, inputs are based on market observable measures at the balance sheet date.

The effects of subsequent measurements of available for sale financial assets are presented in equity.

In case there is a significant and prolonged decrease in fair value below purchase prices for these assets, this is an indication that the financial asset has become impaired. If there is evidence of impairment of financial assets available for sale, the cumulative loss - measured as the difference between the acquisition cost and current fair value - is recognized in the profit or loss.
In case there is a subsequent increase in the fair value of an available for sale debt instrument and the increase can be objectively related to an event occurring after the initial impairment loss is recognized in the profit or loss, the impairment loss is reversed in the profit or loss, but only up to the amount of previously recognized impairment.
In the case of equity securities subsequent correction of impairment in the profit or loss is not permitted.

### 3.23. Other provisions

Provisions for legal claims are recognized when:
- the Bank has a present legal or constructive obligation as a result of past events,
- it is more likely that an outflow of resources will be required to settle the obligation,
- the amount of liability can be reliably estimated.

When there are a number of similar liabilities, the probability that an outflow will be required in a settlement is determined by considering the type of the entire pool of liabilities. A provision is recognized even if there is a low probability of an outflow with respect to the individual item included in the same class of liabilities.

Provisions are measured at the present value of the expected cash outflows required to settle the liability.

When the outflow of assets is not probable anymore, provisions are cancelled.

### 3.24. Share capital and reserves

Share capital consists of ordinary and preference shares and it is stated in BAM at nominal value. Reserves are being formed based on the decision of the Bank's Assembly on the adoption of an annual calculation and profit distribution.

## 3. Summary of significant accounting policies *(continued)*

### 3.25. Statutory reserves

Statutory reserves have been created in accordance with the Company Law of the FBiH, which requires 10% of the profit for the year to be transferred to this reserve until statutory reserves reach 25% of the issued share capital. If the statutory reserves do not reach 25% of issued share capital within five business years, a public limited company is required to increase its transfer to the statutory reserve to 20% of its annual profit for fifth and subsequent business years until capital reserves reach 25% of issued share capital. The statutory reserve can be used for covering current and prior year losses. The Bank was increasing its share capital by redirecting its earnings into statutory reserves, so that as at December 31, 2015, the statutory reserves of the Bank amounted to 87% of the share capital.
The statutory reserves include the reserves for loan losses formed from profit, which are recognized in accordance with regulations (FBA), and are not distributable.

The Bank's legal reserves as of December 31, 2017 amounted to 64,934 thousand BAM, out of which 13.401 thousand BAM relate to the legally prescribed 25% of the share capital, the loan loss reserves formed from profit amount to 3,748 thousand BAM, and 47,785 thousand BAM relate to the amount exceeding the statutory reserve.

### 3.26. Revaluation reserves

Revaluation reserves include changes in the fair value of financial assets available for sale and other re-valuation reserves which relate to the actuarial gains/losses recognised in accordance with IAS 19 and which are the result of an increase or decrease in the present value of a liability for defined employee benefits, due to changes in actuarial assumptions and adjustments based on experience.

### 3.27. Off-balance sheet commitments and contingent liabilities

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

### 3.28. Funds managed for and on behalf of third parties

Assets and revenues from operating activities, where the Bank acts as an agent, including holding or keeping assets on behalf of individuals, trustees and other institutions, are included in the Bank's financial statements, in positions Other liabilities (*Note 21a*) and Fee and commission income (*Note 6a*).

### 3.29. Related party transactions

According to the definition of IAS 24, related parties are:
- parties which directly or indirectly through one or more intermediaries control the reporting party or are being controlled or jointly controlled by the reporting entity,
- associates over which the Bank has a significant influence which are neither related parties nor joint investment,
- individuals with direct or indirect voting power in the Bank which gives them significant influence over the Bank's operations, or over any other subject which is influenced by a related party in performing transactions with the Bank,
- members of the key management personnel i.e. individuals with authorizations and responsibility for planning, managing and controlling the Bank's operations, including directors and key management.

While considering transactions with a related party, attention is focused on the substance and basis of relationship, not just on the legal form.

## 3. Summary of significant accounting policies (*continued*)

### 3.30. Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns which are different from those of other business segments.

A geographical segment relates to products or services within a particular economic environment which are subject to risks and returns different than those of segments operating in other economic environments.

The Bank is monitoring and disclosing its performance by business segments (public, retail, corporate) and by geographical segments (branch offices).

### 3.31. Critical accounting estimates and assumptions

The Bank makes estimates and assumptions with respect to effects which influence reported amounts of assets and liabilities in the next financial year. Estimates and judgements are continually evaluated and based on historical experience and other factors, including expectations of future events which are considered to be reasonable under the circumstances.

#### Impairment losses on loans, deposits with other banks and other assets and off-balance sheet items exposed to risk

The Bank reviews its loan portfolio and other assets and off-balance sheet items to assess the level of impairment at least on a monthly basis. The Bank determines whether a portfolio impairment loss should be recorded in the profit or loss, and assesses whether there is any observable data indicating that there will be a decrease in the estimated future cash flows from a portfolio of loans and guarantees before the decrease can be identified with individual loans in that portfolio.

#### Severance payments and unused vacation days accruals

Expenses for long-term provisions related to the future outflows regarding the retirement of employees are assessed based on the actuarial calculation done in accordance with IAS 19. For the purposes of the assessment, the Bank engages a certified actuary, who performs the calculation based on the data from the HR department of the Bank. . The present value of these future liabilities is calculated by applying a discount rate. These provisions are only used to settle expenses that they have originally been formed for. At the end of each business year the Bank re-assesses the value of these provisions. If the amount recorded is higher or lower than estimated amount, the difference is released or expensed through profit or loss.

In 2017, the authorised actuary has made a calculation of provisions for severances for 2017 and 2018 in accordance with IAS 19 and the Bank has made the required adjustments. For periods when the authorised actuary makes no calculations, the Bank conducts its own reviews of necessary provisions, in accordance with Instructions of the NLB Group.

An assessment of short-term provisions for unused vacation days is done in accordance with the number of days of unused annual holidays as of balance sheet date and the Bank's average net per diem in 2017.

#### Litigations

The Bank's management assesses the amount of provisions for outflows based on litigation; the assessment is based on the estimated probability of the future cash outflows, arising from past contractual or legal obligations. More details on ongoing litigations are found in *Note 25*.

## 3. Summary of significant accounting policies (*continued*)

### 3.31. Critical accounting estimates and assumptions (*continued*)

#### Income tax

The Bank is subject to income taxes in the Federation of Bosnia and Herzegovina and in the Brčko District of Bosnia and Herzegovina. The Bank recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be paid. If the final outcome is different than the amounts that were initially recorded, such differences will impact the current income tax and deferred tax.
The average effective tax rate of the bank as published in *Note 10*.

## 4. Bank's financial risk management

### 4.1. Risk management strategy

Risk management strategy represents part of the overall risk management system for risks to which the Bank is exposed in its operations, and is in line with the business policy and strategy of the Bank.
The Strategy includes guidelines from the Risk Management Strategy of NLB Group. The main purpose of the Strategy is to define key risks while achieving the defined medium-term strategic objectives of the Bank as well as meeting all requests, both of the local regulator, and as directed by NLB d.d., including the requirements of the Bank of Slovenia and ECB at the level of the NLB Group.
The Strategy defines the kind of risks the Bank is willing to assume, those that are not acceptable to the Bank, as well as the strategic guidelines for taking and managing risks at the Bank (including Risk Profile, ICAAP, ILAAP, Budgeting and Equity Planning Process).

Based on the Business Strategy and Risk Appetite, the Risk Management Strategy defines in more detail the key risk taking principles that relate to the type of risk (and related segments or types of activities) that the Bank is prepared to take and which are not eligible/are only acceptable in a very limited extent.

Key principles of the Risk Management Strategy are:
- taking into account the criteria set out in the Risk Appetite;
- inclusion of risk analysis in the decision-making process at strategic and operational level;
- focus on diversification to avoid large concentration at portfolio level;
- optimal use of capital;
- price determination in accordance with appropriate risk;
- full compliance with internal policies / procedures and applicable regulations.

The main risks include: credit risk, liquidity risk, market risk (including currency risk and interest rate risk exposure), operational risk and equity risk).
Standards for risk management of the NLB Group represent the basis for implementation, organization and activities related to the Bank's risk management as a member of NLB Group. The described guidelines, or "minimal standards" in the area of management of credit, non-credit and operating risks, represent basic starting points to all members of the NLB Group which need to adapt their business policies, organization, operating activities and reporting systems.
Standards define basic guidelines, as well as specific short-term and long-term tasks, implementation deadlines and persons/departments in charge of such activities.
The guidelines of the standards for risk management of the NLB Group, are incorporated in the following acts:
- Criteria and procedures for placement approval in the NLB Group (with Attachments);
- Loan Policy for Non-financial Companies in NLB d.d. and NLB Group;
- Program for credit risk management;
- Program for foreign currency risk management;
- Policies and procedures for monitoring interest rate risk exposure;
- Policies for operating risk management;
- Policies and procedures for liquidity risk management;
- Policies for debt securities management;
- Methodology of credit rating - general methodology.

### 4.2. Credit risk management

The Bank is exposed to credit risk, which is the risk of loss due to debtors inability to settle its money commitments towards the Bank. Through the categorisation of placements, loan takers into appropriate risk groups, the Bank identifies and determines the possible level of credit losses, i.e. general credit risk and potential credit loss.
The Bank makes an assessment of credit losses for both individual borrowers and groups of related-party borrowers. The Bank monitors such risks on a continuous basis and reviews them in accordance with internal programs and policies, as well as Banking Agency of the Federation of Bosnia and Herzegovina decisions.
Determination of imapairment includes significant level of management's assessment. Prior years experience show that banks can face significant losses during the crisis which can have significant effect on financial statements and even affect the continuance of business.

*(All amounts are given in thousand BAM unless otherwise stated)*

## *4.* Bank's financial risk management *(continued)*

### 4.2. Credit risk management *(continued)*

The Bank manages credit risk through regular analysis of the ability of lenders and potential lenders to meet interest and principal repayment obligations and by changing these lending limits where appropriate but in accordance with set procedures for credit approval, additional lending, investment activities, and assumption of potential out-of-balance liabilities. Exposure to credit risk is also managed in part by reduction of all forms of possible risk sources related to quality, concentration, guarantees of payment (most credits are insured through attainment of collateral, such as guarantees, mortgages and other collaterals), maturity and currency.

The department for risk management produces a Proposition for credit rating classification and the determination of the upper limit of exposure if the Bank's exposure to credit risk with respect to an individual user or a group of related parties (loans, guarantees and letters of credit and other) exceeds 0.05% of the Bank's core capital.

For exposure to individuals or groups of related parties up to the amount of BAM 200 thousand, the decision on creditworthiness, classification and approval of the limit is usually decided upon by the credit committee of the Retail Centre.

The Credit Board of the Corporate Centre passes decisions on credit limits and sets the upper indebtedness limits for loans from BAM 200 thousand to BAM 400 thousand, while Credit Board of the Bank passes decision on risk exposure for amounts exceeding BAM 400 thousand.

Credit rating and setting up the upper limit of indebtedness ("ULI") in accordance with the Methodology of credit rating for legal persons and groups of related entities is performed, not only for materially important clients (exposure over EUR 5.0 million) and those customers whose loan approval is the competence of the Supervisory Board of the NLB Group (exposure over 10% of the Bank's core capital), but also for all clients of the NLB Group and for clients who are exclusively within the jurisdiction of a member of the NLB Group. By the end of 2017, activities were initiated to accommodate the so-called "GGZ" system for a risk assessment at the level of the transaction, all with the aim of applying the same in early 2018.

| Total exposure to credit risk | 2017 | 2016 |
|---|---|---|
| Cash and balances with the Central Bank of BiH (CBBiH) | 238,335 | 230,214 |
| Placements with banks | 49,774 | 47,827 |
| Loans to customers | 651,423 | 611,800 |
| Financial assets available-for-sale | 74,989 | 62,263 |
| Other financial assets (*Note 17*) | 2,301 | 1,816 |
| | 1,016,822 | 953,920 |

*(All amounts are given in thousand BAM unless otherwise stated)*

## 4. Bank's financial risk management *(continued)*

### 4.2. Credit risk management *(continued)*

The following table shows the maximum exposure to credit risk

| *Financial assets* | Total book value | Impairment provisions | Total net book value |
|---|---|---|---|
| December 31, 2017 | | | |
| Cash and balances with the CBBH (*Note 11*) | 238,335 | - | 238,335 |
| Placements to Banks (*Note 12*) | 49,774 | - | 49,774 |
| Loans to Customers (*Note 13*) | 724,684 | (73,261) | 651,423 |
| Financial assets available-for-sale (*Note 14*) | 75,005 | (16) | 74,989 |
| Other financial assets (*Note 17*) | 4,424 | (2,123) | 2,301 |
| | 1,092,222 | (75,400) | 1,016,822 |
| Contingent Liabilities (*Note 25*) | 130,128 | (3,261) | 126,867 |
| Total | 1,222,350 | (78,661) | 1,143,689 |
| December 31, 2016 | | | |
| Cash and balances with the CBBH (*Note 11*) | 230,214 | - | 230,214 |
| Placements to Banks (*Note 12*) | 47,827 | - | 47,827 |
| Loans to Customers (*Note 13*) | 688,684 | (76,884) | 611,800 |
| Financial assets available-for-sale (*Note 14*) | 62,263 | - | 62,263 |
| Other financial assets (*Note 17*) | 3,843 | (2,027) | 1,816 |
| | 1,032,831 | (78,911) | 953,920 |
| Contingent Liabilities (*Note 25)* | 116,486 | (2,637) | 113,849 |
| Total | 1,149,317 | (81,548) | 1,067,769 |

The Bank performs regular formal asset reviews, separately for each client, and the estimate of the credit risk is performed on a monthly basis based on the following criteria:

1. Client's regularity in settlement of obligations;
2. Estimate of client's business, including financial and capital strength;
3. Estimate of client's business position within the economic sector in which he operates;
4. Management's estimate;
5. Quality of business relations with the client;
6. Estimate of quality and marketability of insurance instruments in order to collect receivables.

Exposure to credit risk from loans to customers, net and due from other banks per rating is as follows:

*(All amounts are given in thousand BAM unless otherwise stated)*

## 4. Bank's financial risk management *(continued)*

### 4.2. Credit risk management *(continued)*

| | Banks | | Loans to customers | | Total | |
|---|---|---|---|---|---|---|
| December 31, 2017 | Gross | Risk provisions | Gross | Risk provisions | Gross | Risk provisions |
| A | 19,733 | - | 389,365 | 3,892 | 409,098 | 3,892 |
| B | 30,041 | - | 215,520 | 4,667 | 245,561 | 4,667 |
| C | - | - | 49,131 | 7,058 | 49,131 | 7,058 |
| D | - | - | 23,138 | 15,300 | 23,138 | 15,300 |
| E | - | - | 47,530 | 42,344 | 47,530 | 42,344 |
| Total | 49,774 | - | 724,684 | 73,261 | 774,458 | 73,261 |
| Total (net) | | 49,774 | | 651,423 | | 701,197 |

| | Banks | | Loans to customers | | Total | |
|---|---|---|---|---|---|---|
| December 31, 2016 | Gross | Risk provisions | Gross | Risk provisions | Gross | Risk provisions |
| A | 21,252 | - | 371,298 | 1,029 | 392,550 | 1,029 |
| B | 26,575 | - | 181,745 | 4,227 | 208,320 | 4,227 |
| C | - | - | 44,000 | 6,939 | 44,000 | 6,939 |
| D | - | - | 44,622 | 23,133 | 44,622 | 23,133 |
| E | - | - | 47,015 | 41,552 | 47,015 | 41,552 |
| Total | 47,827 | - | 688,680 | 76,880 | 736,507 | 76,880 |
| Total (net) | | 47,827 | | 611,800 | | 659,627 |

#### Provisions for impairment and provisioning policy

Impaired loans and securities are those loans and securities for which the Bank determines that it is not likely it will be able to collect all principal and accrued interest under the provisions of the loan agreement /securities agreement. An individually significant exposure is the total exposure to credit risk to a single client or group of related entities that exceeds the amount of BAM 100,000. An individual assessment of credit risk is performed for individually significant exposures and exposures for which there is evidence of impairment. Receivables from clients who do not show signs of impairment exist, or for which the assessor thinks they will be fully repaid according to contractually agreed amounts and terms, are marked as no evidence of impairment of receivables and included in the group for collective assessment of impairment or provisions.

The Bank assesses impairment of receivables as incurred losses in the credit portfolio.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 4. Bank's financial risk management (*continued*)

### 4.2. Credit risk management (*continued*)

The classification of receivables is based on an analysis of overdue settlements of liabilities and indicators of return. In the case of a single loan impairment, future estimated cash flows are discounted in accordance with the requirements of IAS 39, to arrive at an appropriate amount of provision.

#### Collaterals

For the majority of placements granted to clients, the Bank requires collateral.

Collaterals usually include one or a combination of following items:
- Cash deposits,
- Securities deposits,
- Pledge of property, including first line mortgage over property,
- Pledge of precious metals,
- Pledge of movable assets,
- Irrevocable guarantees,
- Insurance with an insurance company,
- Bills of exchange.

In addition to the above mentioned guarantees, the Bank also uses the following elements as placement guarantees:

- Co-guarantors,
- Cessions and assignations,
- Administrative order to monthly salary payments, or agreement on seizure,
- Exceptional guarantees by physical persons and legal entities,

The Bank reserves the right to request any other type of instrument (or variations of the instruments stated above) it deems necessary.

Assessment of fair value of impaired assets is based on the value of the collateral at the time of loan approval which is updated periodically in accordance with the relevant credit policy.

Credit exposure and collaterals before discounting for loans to clients and financial assets with other banks:

| | Maximum credit risk exposure | Fair value of collaterals |
|---|---|---|
| December 31, 2017 | | |
| Credit exposure, net | 701,197 | 1,065,232 |
| Off-balance sheet exposure, net | 126,867 | 67,224 |
| Total | 764,144 | 1,132,456 |
| December 31, 2016 | | |
| Credit exposure, net | 659,627 | 1,039,390 |
| Off-balance sheet exposure, net | 113,849 | 74,827 |
| Total | 773,476 | 1,114,217 |

## 4. Bank's financial risk management (*continued*)

### 4.2. Credit risk management (*continued*)

Out of the total value of collateral, as at December 31, 2017, business and housing premises amounted to BAM 472,936 thousand, while the rest of the collaterals are deposits, movable property, guarantees, administrative orders, assurances, and bills of exchange.
As at December 31, 2016, out of the total value of collaterals, business and housing premises amounted to BAM 523,312 thousand.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 4. Bank's financial risk management *(continued)*

### 4.2. Credit risk management *(continued)*

Maturity dates and impairment of loan liabilities which include loans to customers and placements to banks may be presented as follows:

| | Receivables not due not value adjusted | Overdue receivables not value adjusted | Receivables not due with individual value adjustment | Overdue receivables with individual value adjustment | Receivables not due with group value adjustment | Overdue receivables with group value adjustment | Individual value adjustment | Group value adjustment | Total |
|---|---|---|---|---|---|---|---|---|---|
| December 31, 2017 | | | | | | | | | |
| Governments | - | - | - | - | 5,284 | - | - | (90) | 5,194 |
| Companies | 9,936 | 220 | 20,836 | 36,441 | 257,624 | 456 | (38,123) | (7,867) | 279,523 |
| Banks | 49,774 | - | - | - | - | - | - | - | 49,774 |
| Non-banking financial institutions | - | - | - | - | 3,493 | - | - | (58) | 3,435 |
| Retail | 1,708 | 8 | 10,400 | 18,852 | 358,430 | 996 | (22,151) | (4,972) | 363,271 |
| Total | 61,418 | 228 | 31,236 | 55,293 | 624,831 | 1,452 | (60,274) | (12,987) | 701,197 |
| December 31, 2016 | | | | | | | | | |
| Governments | - | - | - | - | 412 | - | - | (8) | 404 |
| Companies | 10,202 | 25 | 21,929 | 50,231 | 248,889 | 684 | (47,400) | (9,017) | 275,543 |
| Banks | 47,826 | - | 1 | - | - | - | - | - | 47,827 |
| Non-banking financial institutions | - | - | - | - | 3,118 | - | - | (45) | 3,073 |
| Retail | 1,878 | 8 | 10,760 | 18,555 | 321,135 | 858 | (19,323) | (1,091) | 332,780 |
| Total | 59,906 | 33 | 32,690 | 68,786 | 573,554 | 1,542 | (66,723) | (10,161) | 659,627 |

*(All amounts are given in thousand BAM unless otherwise stated)*

## 4. Bank's financial risk management (*continued*)

### 4.2. Credit risk management (*continued*)

An aging analysis of due and not due, impaired and not impaired balance sheet items as at 31 December (including loans to customers and placements to banks) is presented in the following table:

| | Receivables not due not value adjusted | Overdue receivables not value adjusted | Receivables not due with individual value adjustment | Overdue receivables with individual value adjustment | Receivables not due with group value adjustment | Overdue receivables with group value adjustment | Individual value adjustment | Group value adjustment | Total |
|---|---|---|---|---|---|---|---|---|---|
| December 31, 2017 | | | | | | | | | |
| Without delay | 61,418 | 3 | 31,236 | - | 624,831 | - | (13,446) | (12,912) | 691,130 |
| Up to 30 days | - | 5 | - | 115 | - | 1,093 | (38) | (33) | 1,142 |
| From 30 to 90 days | - | - | - | 575 | - | 337 | (328) | (38) | 546 |
| Over 90 days | - | 220 | - | 54,603 | - | 22 | (46,462) | (4) | 8,379 |
| Total | 61,418 | 228 | 31,236 | 55,293 | 624,831 | 1,452 | (60,274) | (12,987) | 701,197 |
| December 31, 2016 | | | | | | | | | |
| Without delay | 59,906 | - | 32,690 | - | 573,554 | - | (14,956) | (10,098) | 641,096 |
| Up to 30 days | - | 33 | - | 3,288 | - | 1,189 | (1,657) | (36) | 2,817 |
| From 30 to 90 days | - | - | - | 4,801 | - | 345 | (3,188) | (24) | 1,934 |
| Over 90 days | - | - | - | 60,697 | - | 8 | (46,922) | (3) | 13,780 |
| Total | 59,906 | 33 | 32,690 | 68,786 | 573,554 | 1,542 | (66,723) | (10,161) | 659,627 |

*(All amounts are given in thousand BAM unless otherwise stated)*

## 4. Bank's financial risk management *(continued)*

### 4.2. Credit risk management *(continued)*

Loan portfolio per industrial sector is presented in the table below. Calculated interests and fees which increase the balance of loan receivables and bank placements, as well as accrued income (IAS 18), deducted from loan receivables and bank placements, are presented within the separate positions in the table below.

| | 2017 | | 2016 | |
|---|---|---|---|---|
| | BAM | % | BAM | % |
| Retail | 388,648 | 50.25 | 351,611 | 47.77 |
| Trade | 165,965 | 21.46 | 167,319 | 22.73 |
| Mining and industry | 98,745 | 12.77 | 101,186 | 13.75 |
| Financial institutions | 54,192 | 7.01 | 51,173 | 6.95 |
| Building construction industry | 16,069 | 2.08 | 23,530 | 3.20 |
| Transportation and communications | 20,472 | 2.65 | 14,722 | 2.00 |
| Trading in real estate | 5,670 | 0.73 | 5,417 | 0.73 |
| Services, tourism, catering | 6,301 | 0.81 | 8,780 | 0.19 |
| Agriculture, forestry and fishing | 6,996 | 0.90 | 7,476 | 1.01 |
| Other | 10,380 | 1.34 | 4,901 | 0.67 |
| | 773,438 | 100.00 | 736,115 | 100.00 |
| Interests and fees | 3,450 | | 3,524 | |
| Delimitation of charges collected in advance for loans processing (IAS 18) | (2,430) | | (3,128) | |
| | 774,458 | | 736,511 | |
| Less: Impairment allowance | (73,261) | | (76,884) | |
| | 701,197 | | 659,627 | |

*Non-Performing Loans*

Non-Performing Loans (NPL) are the Bank's loans classified into categories D and E. NPL management is done in the Department for Collection and NPL Management. For all Corporate and SME customers in Categories D and E whose total exposure to a client or group of related entities is over EUR 1,000, immediately after the fulfilment of these criteria a procedure is initiated to transfer the customer from the business component to the Department for Collection and NPL Management.
As of 01 June 2017, Sector is divided into two organizational units, the Corporate Collection Department and Retail Collection Department, where the process of early, late and court collection of claims from problematic clients is being run and monitored.
The process of collecting claims for retail is centralized and is in charge of the Retail Collection Department.
All activities for collecting claims for retail clients are undertaken solely by the Retail Collection Department and start from the first day of the client's delay through early collection and continue through late collection activities and initiation of court proceedings until the claims are closed or the client recovered.

In the collection process for corporate entities, the Corporate Collection Department is involved with collection activity starting from a 31st day of delay, which implies customer interaction, meeting, defining collection strategy for the client along with the Corporate Sector. With the classification of a client in a credit rating class D and E, the client enters into the jurisdiction of the Corporate Collection Department, where the collection strategy is defined individually for each client (restructuring, settlement, collateral, collection from collaterals, initiation and conducting court proceedings).

If clients who are under the jurisdiction of the Department for Collection and NPL Management establish a continuity in payment without delays and come out of financial difficulties after the recovery period, then as recovered they return to the Performing portfolio under the responsibility of the Corporate Department and Retail Department.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 4. Bank's financial risk management (*continued*)

### 4.2. Credit risk management (*continued*)

*Reprograms and restructuring*

Measures for restructuring debt include a "concession" to a debtor which is caused by economic and financial situation of the customer and his inability to service the debt under previously agreed terms and conditions. The "concession" may take the form of an amendment to conditions of the initial agreement (annex) or a new agreement (refinancing).

Restructuring the debt has the aim to adjust the repayment to be in line with the client's real capabilities, ensuring more efficient and safer collection of the Bank's receivables. In this sense restructuring the debt represents a change in the terms agreed during loan approval (prolonged repayment period, decrease in interest rate, etc.). The decision on restructuring is made by the competent body of the Bank in accordance with the Decision on responsibilities in the lending process. Loans to clients rated in group E cannot be refinanced/reprogrammed.

Restructured exposure may be identified as both in the uncollectable (NPE) and in collectable (PE) part of the portfolio.

| | Number of restructured loans (number of transactions) | Gross loan exposures |
|---|---|---|
| December 31, 2017 | | |
| Corporate | 78 | 29,680 |
| Retail and SME | 45 | 541 |
| Total | 123 | 30,221 |
| December 31, 2016 | | |
| Corporate | 105 | 52,626 |
| Retail and SME | 60 | 699 |
| Total | 165 | 53,295 |

*Intensive monitoring of clients*

The Bank introduces intensive monitoring for clients that require careful treatment and monitoring. Such clients are placed on the intensive monitoring list, due to different operating elements (large placement volumes, acutely negative operating trends, an increase in debt and establishment of the capital adequacy, the non-payment or irregular payment of liabilities). The initiative for placing a specific client on the intensive monitoring list may come from, apart from the competent business administrator, the WLC (Watch Loan Committee), the Centre of risk management of the Bank during the creditworthiness classification and setting the upper indebtedness limit, the members of the Bank's Credit committee, and Bank management. Reasons which initiated placing the client on the intensive monitoring list must be stated.

Client monitoring on ICL contributes to reducing credit risk and transition to NPL, as by adopting measures and further activities to be undertaken towards the client, it tries to achieve:

- Reduction of Bank's exposure to client
- possible acquisition of additional security instruments (collateral),
- Consideration of various workout options (restructure, repossession, recovery)
- Discussion on client' key business issues
- verification of the adequacy of the credit rating of the client.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 4. Bank's financial risk management *(continued)*

### 4.2. Credit risk management *(continued)*

Intensive client monitoring is terminated in following cases:

- Due to the dismissal of all placements of the Bank (by collection or write-off),
- Due to an improvement of the client's status and rating into higher rating class (if the client accomplishes main values of indicators or other given goals),
- Due to the transfer of a client into the categories D or E,
- By initiating insolvency proceedings over the client,
- In all other cases when the Bank's management brings the decision on the termination of intensive client monitoring.

The decision to classify a client into the intensive monitoring list falls within the competence of the Watch Loan Committee.

Off-balance sheet items

*(a) Loan liabilities*

The timings of contractual amounts of the Bank's off-balance sheet financial instruments committing it to extend loans to customers are summarized in the table below.

| | Up to 1 year | From 1 to 5 years | Over 5 years | Total |
|---|---|---|---|---|
| As of December 31, 2017 | | | | |
| Loan liabilities | 81,476 | 485 | 40 | 82,001 |
| As of December 31, 2016 | | | | |
| Loan liabilities | 62,645 | 109 | - | 62,754 |

*(b) Other financial liabilities - guarantees*

Other financial liabilities are also included in the table below, based on the earliest contractual maturity date.

| | Up to 1 year | From 1 to 5 years | Over 5 years | Total |
|---|---|---|---|---|
| As of December 31, 2017 | | | | |
| Other financial facilities | 35,758 | 12,364 | 5 | 48,127 |
| As of December 31, 2016 | | | | |
| Other financial facilities | 38,911 | 14,821 | - | 53,732 |

*Risk measurement*

The measurement of exposure to market risk is performed in accordance with regulations and the methodology for measuring the quantity of risk exposure on the level of the NLB Group, by using standard forms. The NLB Group has relatively conservative policy for market risk management, which includes certain limitations and procedures in policies and other documents of the NLB Group.

## 4. Bank's financial risk management *(continued)*

### 4.3. Market risk

*General requirements*

The Bank takes on exposure to market risks, which is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risks arise from open positions in interest rates, foreign currency and equity products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, foreign exchange rates and equity prices. The Management Board sets limits and guidelines for monitoring and mitigating market risks, which is regularly monitored by the Bank's ALCO Committee.

When it comes to market risk management, the key factor is the separation of responsibilities between the monitoring and management of market risks Non-credit risks are regularly monitored by the Risk department, which analyses whether all positions for certain types of risk are within the defined limits. Open positions are managed by the Asset liability management department of the Bank which keeps them within the given limits.

*Risk mitigation*

The department for trading daily currency conversions maintains the foreign exchange position within legally and internally established limits. The asset liability management department of the Bank conducts different activities in order to reduce market risks to the lowest level.

*Risk controlling and monitoring*

Risk controlling is used to monitor compliance with certain legal and internal limits. Market risk controlling and monitoring is supported by internal methodologies adjusted to Basel Standards. In accordance with the requirements of the Bank of Slovenia, the NLB Group provides the necessary level of capital for covering potential unexpected losses due to exposure to currency and other market risks.

### 4.4. Foreign currency risk management

Currency risk is the Bank’s exposure to the possible impact of changes in exchange rates and the risk that adverse changes result in losses for the Bank in BAM (local currency). The level of risk represents a function of level and the size of exposure to possible changes of exchange rates for the Bank, depending on the amount of bank’s foreign debt and the level of Bank’s open balance sheet and off-balance FX positions, i.e. the degree of compliance of its currency flows.
Foreign currency exposure arises from loans, deposits, and investment and trading activities. It is monitored daily in accordance with legislation and internally set limits for each currency and for the total balance sheet denominated or linked to a foreign currency. Throughout the year open currency positions were maintained in accordance with the regulations set by the Banking Agency and internal limits defined by the Methodology of the NLB Group.
Since BAM has a fixed exchange rate to EUR, in accordance with the Currency Board arrangement, the Bank was not exposed to changes in EUR exchange rate. Fluctuations in other currencies did not have a significant influence to exposure of the Bank to foreign currency risk since the open foreign exchange position was reduced to a minimum.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 4. Bank's financial risk management (*continued*)

### 4.4 Foreign currency risk management (*continued)*

The Bank had the following currency position

| As of December 31, 2017 | EUR | USD | BAM | Other currencies | Total |
|---|---|---|---|---|---|
| Financial assets | | | | | |
| Cash and balances with the CBBiH | 3,986 | 287 | 233,011 | 1,051 | 238,335 |
| Placements to banks and loans to customers | 109 | 6,966 | 199,030 | 4,467 | 210,572 |
| Placements to banks and loans to customers with foreign currency clause | 490,625 | - | - | - | 490,625 |
| Financial assets available-for-sale | 54 | - | 69,094 | - | 69,148 |
| Financial assets available-for-sale with foreign currency clause | 5,841 | - | - | - | 5,841 |
| Other financial assets | 703 | 1 | 1,597 | - | 2,301 |
| | 501,318 | 7,254 | 502,732 | 5,518 | 1,016,822 |
| Financial Commitments | | | | | |
| Financial liabilities at amortized cost | 304,496 | 7,091 | 392,982 | 4,965 | 709,534 |
| Financial liabilities at amortized cost with FX clause (EUR) | 180,966 | - | - | - | 180,966 |
| Other financial liabilities | 1,903 | 46 | 8,405 | 114 | 10,468 |
| | 487,365 | 7,137 | 401,387 | 5,079 | 900,968 |
| Foreign exchange position, net | 13,953 | 117 | 101,345 | 439 | 115,854 |

| As of December 31, 2016 | EUR | USD | BAM | Other currencies | Total |
|---|---|---|---|---|---|
| Financial assets | | | | | |
| Cash and balances with the CBBiH | 3,987 | 380 | 224,643 | 1,204 | 230,214 |
| Placements to banks and loans to customers | 37,395 | 5,677 | 190,333 | 4,668 | 238,073 |
| Placements to banks and loans to customers with foreign currency clause | 421,554 | - | - | - | 421,554 |
| Financial assets available-for-sale | 3,969 | - | 57,273 | - | 61,242 |
| Financial assets available-for-sale with foreign currency clause | 1,021 | - | - | - | 1,021 |
| Other financial assets | 498 | - | 1,317 | 1 | 1,816 |
| | 468,424 | 6,057 | 473,566 | 5,873 | 953,920 |
| Financial Commitments | | | | | |
| Financial liabilities at amortized cost | 289,179 | 5,953 | 371,896 | 5,653 | 672,681 |
| Financial liabilities at amortized cost with FX clause (EUR) | 173,144 | - | - | - | 173,144 |
| Other financial liabilities | 3,895 | 9 | 2,867 | 39 | 6,810 |
| | 466,218 | 5,962 | 374,763 | 5,692 | 852,635 |
| Foreign exchange position, net | 2,206 | 95 | 98,803 | 181 | 101,285 |

Financial liabilities at amortised cost include liabilities to banks, clients, borrowings and subordinated debt.

## 4. Bank's financial risk management (*continued*)

### 4.5. Interest rate risk management

The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest earning assets and interest bearing liabilities mature or re-price at different times or in different amounts.

In the case of floating rates, the Bank's assets and liabilities are also exposed to base risk, which is the difference in the re-pricing characteristics of the various floating rate indices, such as savings rates, the six months EURIBOR, and different types of interest. Risk management activities are consistent with the Bank's business strategies and they are aimed at optimizing net interest income given the market interest rate levels.

The Bank produced Policies and procedures for monitoring of market risk management, whose goal is to manage and limit the potential losses of the Bank, due to changes in foreign and domestic interest rates that affect the economic and market value of the Bank.

In order to achieve the Policies' goals for monitoring interest rate risk exposure, the Bank identifies positions that are sensitive to change in interest rates, prepares data for the calculation of interest-sensitive positions, establishes methods for risk measurement, establishes control mechanisms and limits, determines authorizations and responsibilities, and prepares reports.

The purpose of interest rate risk management, as one segment of assets and liabilities management, is to determine the optimal interest rate, and with that, the Bank's income, taking into account market conditions and the competitive environment, and to adjust the interest rate in line with the Bank's assets and liabilities. Considering this objective, it is extremely important to assess the sensitivity of revenues towards abrupt changes in the market interest rate.

As a protection from interest rate risk exposure, the Bank contracts the variable interest rate, adjusts the structure of interest-bearing assets and liabilities subject to interest payment, and uses other interest rate risk management instruments.
The Bank manages the interest rate risk in the following manner:

- By adequately determining the level of the interest margin, by adjusting the interest rates on positions of interest-sensitive assets and liabilities to be within the same maturity and time intervals within which the re-establishment of the interest rate is being performed; and/or
- By securing maturity alignment of interest-sensitive assets and liabilities (when the fixed interest rate is used), or by adjusting the deadline (time interval for re-establishment of the interest rates in cases where variable interest rate is being used).

The Bank is exposed to risks that affect its financial position and cash flows, through the effects of change in interest rates on the market. The table below shows the Bank's exposure to interest rate risk.

The positions of assets and liabilities with the balance as at 31 December 2017 and 2016 are shown in the table at the book value and in accordance with the agreed interest rate and the date of repircing.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 4. Bank's financial risk management *(continued)*

### 4.5. Interest rate risk management *(continued)*

| | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Non-interest bearing | Total |
|---|---|---|---|---|---|---|---|
| December 31, 2017 | | | | | | | |
| Financial assets | | | | | | | |
| Cash and balances with the CBBiH | 196,819 | - | - | - | - | 41,516 | 238,335 |
| Placements with banks | 49,364 | - | - | 410 | - | - | 49,774 |
| Loans to customers | 391,743 | 75,271 | 162,399 | 13,209 | 3,742 | 5,059 | 651,423 |
| Financial assets available-for-sale | - | 4,985 | 50,404 | 18,189 | 1,266 | 175 | 74,989 |
| Other financial assets | 2,301 | - | - | - | - | - | 2,301 |
| Non-financial assets | | | | | | | |
| Tangible and intangible assets | - | - | - | - | - | 21,691 | 21,691 |
| Other non-financial assets | 887 | - | - | - | - | - | 887 |
| | 641,114 | 80,256 | 212,803 | 31,778 | 5,008 | 68,441 | 1,039,400 |
| Financial liabilities | | | | | | | |
| Banks' deposits | 4,312 | - | 5,858 | 147 | - | - | 10,317 |
| Customers' deposits | 351,200 | 6,660 | 21,157 | 58,271 | 455 | 399,218 | 836,961 |
| Borrowings | 9 | 1,627 | 12,195 | 28,659 | 732 | - | 43,222 |
| Other financial liabilities | 10,440 | 6 | 22 | - | - | - | 10,468 |
| Non-financial liabilities | | | | | | | |
| Other provisions | 3,311 | - | 1,160 | 208 | 212 | - | 4,891 |
| Deferred income | - | - | - | 105 | - | - | 105 |
| | 369,272 | 8,293 | 40,392 | 87,390 | 1,399 | 399,218 | 905,964 |
| Exposure to interest rate risk, net | 271,842 | 71,963 | 172,411 | (55,612) | 3,609 | (330,777) | 133,436 |

*(All amounts are given in thousand BAM unless otherwise stated)*

## 4. Bank's financial risk management *(continued)*

### 4.5. Interest rate risk management *(continued)*

| | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Non-interest bearing | Total |
|---|---|---|---|---|---|---|---|
| December 31, 2016 | | | | | | | |
| Financial assets | | | | | | | |
| Cash and balances with the CBBiH | 189,879 | - | - | - | - | 40,335 | 230,214 |
| Placements with banks | 47,360 | - | - | 467 | - | - | 47.827 |
| Loans to customers | 348,544 | 55,039 | 185,192 | 3,605 | 2,626 | 16,794 | 611,800 |
| Financial assets available-for-sale | - | - | 36,726 | 24,120 | 1,235 | 182 | 62,263 |
| Other financial assets | 1.816 | - | - | - | - | - | 1,816 |
| Non-financial assets | | | | | | | |
| Tangible and intangible assets | - | - | - | - | - | 20,525 | 20,525 |
| Other non-financial assets | 677 | - | - | - | - | - | 677 |
| | 588,276 | 55,039 | 221,918 | 28,192 | 3,861 | 77,836 | 975,122 |
| Financial liabilities | | | | | | | |
| Banks' deposits | 3,510 | 1 | 13,679 | - | - | - | 17.190 |
| Customers' deposits | 362,912 | 5,100 | 36.119 | 29.594 | - | 362,190 | 795,915 |
| Borrowings | 662 | 706 | 7,982 | 19,998 | 3,372 | - | 32,720 |
| Other financial liabilities | 6,777 | 7 | 25 | - | 112 | - | 6,921 |
| Non-financial liabilities | | | | | | | |
| Other provisions | 2,643 | 102 | 547 | 220 | 629 | - | 4,141 |
| Deferred income | - | - | - | - | - | - | - |
| | 376,504 | 5,916 | 58,352 | 49,812 | 4,113 | 362,190 | 856,887 |
| Exposure to interest rate risk, net | (211,772) | 49,123 | 163,566 | (21,620) | (252) | (284,354) | 1,118.235 |

In its management of interest rate risk, the Bank uses a simulation of expected and extreme changes in interest rates and the influence of these changes on the profit or loss.

## 4. Bank's financial risk management (*continued*)

### 4.5. Interest rate risk management (*continued*)

The following table presents the impact of expected changes in interest rates to the Bank's profit, while all other variables remain unchanged:

Profit or loss sensitivity to change in interest rates as at December 31, 2017

| Increase in interest rates | Impact on profit or loss in BAM | Decrease in interest rates | Impact on profit or loss in BAM |
|---|---|---|---|
| +100 bp | 1,699 | -100 bp | (765) |

Profit or loss sensitivity to change in interest rates as at December 31, 2016

| Increase in interest rates | Impact on profit or loss in BAM | Decrease in interest rates | Impact on profit or loss in BAM |
|---|---|---|---|
| +100 bp | 1,361 | -100 bp | (846) |

Interest rate sensitivity as a result of changes in market interest rates affects two categories:
- The amount of net interest income,
- The market value of certain financial instruments (interest-sensitive investments and sources), which consequently affects the market value of the Bank's capital

The sensitivity of the income statement in the table shows how changes in market interest rates, applied to the existing interest sensitive open position, would reflect on the financial result. The limit for the income aspect of credit risk, presented as a decrease in net interest income in case of a parallel change in interest rates by 100 bp, is 3% of capital. The effect of interest rate decrease by 100 bp, as at 31/12/2017 was 0.65% of capital.

In line with the Policies and procedures for the monitoring of interest rate risk exposure, the Bank must meet the criteria of impact of a parallel shift in interest rates by 200 basis points, which is applied to the existing open interest rate position in accordance with certain time intervals. The effects of the simulation, calculated based on core deposit starting 2016, cannot exceed 10% of the Bank's capital. Core deposits are deposits presumed to remain with the Bank regardless of a change in market interest rates. They are calculated based on the movements of corporate and retail demand deposits over a period of several years.

Sensitivity of the market value of financial instruments on December 31, 2017

| Change of interest rates | Effect of simulation in 000 BAM | Effect of simulation in relation to capital |
|---|---|---|
| 200 bp | 659 | 0.56% |

Sensitivity of the market value of financial instruments on December 31, 2016

| Change of interest rates | Effect of simulation in 000 BAM | Effect of simulation in relation to capital |
|---|---|---|
| 200 bp | 552 | 0.46% |

## 4. Bank's financial risk management (*continued*)

### 4.6. Liquidity risk management

*Definition*

Liquidity risk is probability that the Bank will not have sufficient cash assets for the normal course of its business activities in the future.
Liquidity risk arises in the general funding of the Bank's activities and in the management of positions. It includes both the risk of being unable to fund assets at appropriate maturities and rates and the risk of being unable to liquidate an asset at a reasonable price and in an appropriate time frame.

*General requirements*

The Bank has access to a diverse funding base. Funds are raised using a broad range of instruments including various types of retail and corporate deposits, borrowings and share capital and through emission of bonds. This enhances funding sources flexibility, limits dependence on one source of funds and generally lowers the cost of funds.
The Bank strives to maintain a balance between the continuity of funding and flexibility through the use of liabilities with a range of maturities. The Bank continually assesses liquidity risk by identifying and monitoring changes in funding, required to meet business goals and targets set in terms of the overall strategy of the Bank. Furthermore, the Bank keeps a portfolio of liquid assets as part of its strategy for liquidity risk management.

*Risk measurement*

The measurement of liquidity risk is performed through reporting on structural liquidity and liquidity gaps that show the long term aspects of securing the Bank's liquidity (in relation to assets, liabilities, the relationship between assets and liabilities and financing source structure).
The Bank conducts liquidity stress tests on a regular basis.
Measurement of liquidity risk is also performed through the Scoring model.

*Risk controlling*

The Bank adjusts its business activities in compliance with liquidity risk according to legislation and internal policies for the maintenance of liquidity reserves, the matching of liabilities and assets, limits, and preferred liquidity ratios. The Bank's Treasury manages liquidity reserves daily, also ensuring that the Bank satisfies all customer needs.

*Monitoring liquidity risk exposure*

In accordance with Risk Management Standards in the NLB Group, a monthly report is made on structural liquidity, in which the following ratios are monitored:

- Share of NLB resources in the total balance sheet sum,
- Amount of NLB resources in relation to the Bank’s equity,
- Share of non-bank liabilities in the balance sum,
- Share of resources of 30 largest non-banking depositors in total balance sheet sum,
- The ratio of loans and deposits (“Loan to deposit ratio”) (gross loans to non-banking sector/deposits of non-banking sector),
- The ratio of net loans (gross loans decreased for impairments) and deposits (net loans to non-banking sector/deposits of non-banking sector),
- Liquidity coverage ratio (LCR) – supplies of high-quality liquid assets / net outflows in the next 30 days,
- Net Stable Funding Ratio (NSFR) - available amount of funds for stable funding / required amount of funds for stable funding,
- The share of unmortgaged liquid reserves in total assets,

*(All amounts are given in thousand BAM unless otherwise stated)*

## 4. Bank's financial risk management (*continued*)

### 4.6. Liquidity risk management (*continued*)

- The share unmortgaged liquid reserves in unstable liabilities,
- Unmortgaged liquid reserves in relation to the potential outflows in strong quarterly stress test,
- Stable demand deposits.

The Bank prepares monthly LGST (Liquidity Gap Stress Test) reports that are also used to monitor the maturity structure of assets and liabilities per periods of remaining maturity, and influence of stress scenarios on the static liquidity gap structure (cash flows from contracted activities) that is within the responsibility of the Risk Management Department. A dynamic projection is added to the static one, and it includes the plan of future inflows and outflows for the following year (dynamic projection is the responsibility of the Bank's Asset/Liability Management Department). Established Stress scenarios are applied to static projection, and taking into account the future inflows and outflows, the level of necessary liquid assets needed for the Bank to be able to continue the normal course of its operations under special circumstances, resulting from possible increased outflows, is calculated.

The Bank monitors the exposure to liquidity risk through Scoring models. Scoring models are composed of 22 indicators divided to six groups: regulatory indicators, internal liquidity and financing source indicators, indicators of assets, capital indicators, stress test and systemic risks.

The final result is determined by the percentage that shows in which group of risk the Bank is:

| | | |
|---|---|---|
| 1. | Low liquidity risk | 0% - 20% |
| 2. | Acceptable liquidity risk | 20% - 40% |
| 3. | Moderate liquidity risk | 40% - 60% |
| 4. | High liquidity risk | 60% - 80% |
| 5. | Extremely high liquidity risk | 80% - 100% |

The Bank's exposure to liquidity risk as of December 31, 2017 is low as a result of a Scoring model result of 15.85%.

In case of exposure to high liquidity risk, the Bank would activate the Plan for liquidity risk management in exceptional circumstances.

The following table presents analysis of assets and liabilities per maturity based on remaining period from balance sheet date to agreed due date.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 4. Bank's financial risk management *(continued)*

### 4.6. Liquidity risk management *(continued)*

| December 31, 2017 | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Without maturity date | Total |
|---|---|---|---|---|---|---|---|
| *Financial assets* | | | | | | | |
| Cash and balances with the CBBiH | 196,819 | - | - | - | - | 41,516 | 238,335 |
| Placements with banks | 49,367 | - | - | 411 | - | - | 49,778 |
| Loans to customers | 45,612 | 61,302 | 204,168 | 308,809 | 136,874 | 2,301 | 759,066 |
| Financial assets available-for-sale | 76 | 4,999 | 50,438 | 18,185 | 1,269 | 83 | 75,050 |
| Other financial assets | - | - | - | - | - | - | - |
| *Non-financial assets* | | | | | | | |
| Tangible and intangible assets | - | - | - | - | - | 21,691 | 21,691 |
| Other non-financial assets | - | - | - | - | - | 887 | 887 |
| Total | 291,874 | 66,301 | 254,606 | 327,405 | 138,143 | 66,478 | 1,144,807 |
| *Financial liabilities* | | | | | | | |
| Banks' deposits | 4,312 | - | 5,859 | 147 | - | - | 10,318 |
| Customers' deposits | 384,375 | 29,230 | 97,902 | 223,831 | 1,496 | 108,585 | 845,419 |
| Borrowings | 38 | 1,685 | 12,423 | 29,213 | 742 | - | 44,101 |
| Other financial liabilities | - | - | - | - | - | 10,468 | 10,468 |
| *Non-financial liabilities* | | | | | | | |
| Other provisions | - | - | - | - | - | 4,891 | 4,891 |
| Deferred income | - | - | - | - | - | 105 | 105 |
| Total | 388,725 | 30,915 | 116,184 | 253,191 | 2,238 | 124,049 | 915,302 |
| Exposure to liquidity risk, net | (96,851) | 35,386 | 138,422 | 74,214 | 135,905 | (57,571) | 229,505 |

*(All amounts are given in thousand BAM unless otherwise stated)*

## *4.* Bank's financial risk management *(continued)*

### 4.6. Liquidity risk management *(continued)*

| December 31, 2016 | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Without maturity date | Total |
|---|---|---|---|---|---|---|---|
| Financial assets | | | | | | | |
| Cash and balances with the CBBiH | 189,879 | - | - | - | - | 40,335 | 230,214 |
| Placements with banks | 47,362 | - | - | 467 | - | - | 47,829 |
| Loans to customers | 51,166 | 52,681 | 209,223 | 284,729 | 110,387 | - | 708,186 |
| Financial assets available-for-sale | 73 | 3 | 36,736 | 24,157 | 1,244 | 122 | 62,335 |
| Other financial assets | 0 | - | - | 160 | - | 1,656 | 1,816 |
| Non-financial assets | | | | | | | |
| Tangible and intangible assets | - | - | - | - | - | 20,525 | 20,525 |
| Other non-financial assets | | - | - | - | - | 677 | 677 |
| Total | 288,480 | 52,684 | 245,959 | 309,513 | 111,631 | 63,315 | 1,071,582 |
| Financial liabilities | | | | | | | |
| Banks' deposits | *166* | *1* | *13,679* | - | - | *3,346* | *17,192* |
| Customers' deposits | 363,610 | 27,123 | 113,709 | 200,784 | 1,477 | 99,363 | 806,066 |
| Borrowings | 712 | 804 | 8,386 | 20,951 | 3,404 | - | 34,257 |
| Other financial liabilities | - | - | - | - | | 6,810 | 6,810 |
| Non-financial liabilities | | | | | | | |
| Other provisions | - | - | - | - | - | 4,141 | 4,141 |
| Deferred income | - | - | - | - | - | 111 | 111 |
| Total | 364,488 | 27,928 | 135,774 | 221,735 | 4,881 | 113,771 | 868,577 |
| Exposure to liquidity risk, net | (76,008) | (24,756) | 110,185 | 87,778 | 106,750 | 50,456 | 203,005 |

## 4. Bank's financial risk management *(continued)*

### 4.7. Fair value of financial assets and liabilities

*Placements with banks*

Deposits with other banks include inter-banking placements. The fair value of placements with the fluctuating interest and fixed interest represents their carrying value (the Bank has a limited portfolio of placements to banks with a fixed interest rate and usually these placements have a short maturity date).

*Loans and advances to customers*

The fair value of loans and advances given to clients represents a discounted amount of expected future cash flows from principal and interest. After initial recognition, loans are subsequently measured at amortized cost using the effective interest rate method. At each balance sheet date the Bank assesses whether there is objective evidence that a financial asset or groups of financial assets should be impaired. It is considered that financial assets or group of financial assets are impaired when there is objective evidence of impairment which arises as a consequence of one or more loss events arising after the initial recognition of assets and if said events (losses) will surely impact on future estimated cash flows.

The fair value of a loan with a fixed interest rate is estimated by discounting of cash flows applying the interest rates currently valid on loans with similar terms and characteristics. Since the Bank has a limited portfolio of loans and receivables with a fixed interest rate and longer maturity, the management believes that the fair value of loans and receivables do not differ significantly from their carrying value. Fair value of loans with variable yield whose price is reviewed on a regular basis (with no significant changes in credit risk) are generally close to their book values and are calculated on the basis of discounted cash flows by applying interest rates increased by the credit risk margin, in order to recognize the impact of specific credit risk of the counterpart.

*Deposits of other banks, clients, other deposits, other borrowings and subordinated liabilities*

For a vista deposits and deposits without a defined maturity fair value is an amount payable on the reporting date. The estimated fair value of deposits with fixed maturity and variable interest rate is close to the book value on the date of reporting and it is based on cash flows discounted at currently offered interest rates on deposits with a similar remaining maturity. The value of long-term relationships with depositors is not taken into account for the assessment of fair value. Since most deposits with the Bank have a variable interest rate (which is at the same time the market interest rate), and since long-term deposits with a fixed interest rate represent a smaller portion of deposits, the management believes that there is no significant difference between the fair value of those deposits and their carrying value.

The fair value of received loans is calculated by discounting the future cash flows (the remaining debt and future interest rates) to their present value. Future interest rates are calculated by applying the current value of EURIBOR and on the reporting date there is no significant difference between the fair value of received loans and their carrying value.

*Financial assets available-for-sale*

Debt securities and equity securities are measured at fair value in the Bank's balance sheet (Bank's investments in equity of other legal entities). Re-measurement at fair value is performed at the end of each month and the difference compared to the purchased value is credited/debited to equity. As of December 31, 2016 the total market value of securities, including accrued interest, amounts to BAM 62,262 thousand.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 4. Bank's financial risk management *(continued)*

### 4.7.1. Fair value of financial assets and financial liabilities of the Bank which are measured at fair value on a recurring basis, from period to period

The following table presents information on how the fair value of securities available for sale is measured (valuation techniques and input data used, in particular). Re-measurement at fair value is performed at the end of each month and the difference compared to the purchased value is credited/debited to equity.

| Fair value as of | | Fair value hicherarchy |
|---|---|---|
| December 31, 2017 | December 31, 2016 | |
| Debt securities | Debt securities:<br>· Ministry of Finance treasury bills of Republic of Slovenia BAM 3,918 thousand | Level 1 |
| Debt securities:<br>· Ministry of Finance FBiH (long-term bonds) – BAM 26,628 thousand<br>· Ministry of Finance FBiH (short-term treasury bills) – BAM 34,492 thousand<br>· Ministry of Finance RS (long-term bonds) – BAM 2,893 thousand<br>· Ministry of Finance RS (short-term treasury bills) – BAM 9,977 thousand<br>· Canton Sarajevo (long-term bonds) – BAM 916 thousand | Debt securities:<br>• Ministry of Finance FBiH (long-term bonds) – BAM 27,417 thousand<br>• Ministry of Finance FBiH (short-term treasury bills) – BAM 30,805 thousand | Level 2 |
| Equity securities:<br>· Registry of securities of FBiH – BAM 14 thousand<br>· UBBIH – BAM 14 thousand<br>· SWIFT Belgium – BAM 55 thousand | Equity securities:<br>· Registry of securities of FBiH – BAM 14 thousand<br>· UBBIH – BAM 14 thousand<br>· Privredna banka Sarajevo – BAM 44 thousand<br>· SWIFT Belgium – BAM 50 thousand | Level 3 |

As of December 31, 2017 all securities are classified as available for sale (AFS) and serve as secondary liquidity reserves. Measurements under fair value are in compliance with IAS and IFRS. Effects of valuation are disclosed in the Statement of changes in equity within the item Other comprehensive income/loss (Revaluation reserves).

(All amounts are given in thousand BAM unless otherwise stated)

## 4. Bank's financial risk management *(continued)*

### 4.7.2. Fair value of financial assets and financial liabilities of the Bank which are not measured at fair value on a recurring basis

Fair value of loans and deposits is calculated on different segments, products, type of interest rate rebate and remaining maturities. Calculations are based on the net value of the loan increased by future interest rates. All future cash flows from equity and interest are discounted to the present value. Fair value reflects the price at which an individual financial instrument could be sold, but it does not affect the balance sheet and income statement of the Bank.

| | | December 31, 2017 | | December 31, 2016 | |
|---|---|---|---|---|---|
| *Financial assets* | Fair value hicherarchy | Book value | Fair value | Book value | Fair value |
| Placements with banks | Level 3 | 49,774 | 49,745 | 47,827 | 47,792 |
| Loans to clients | Level 3 | 651,423 | 640,048 | 611,800 | 617,232 |
| Total | | 701,197 | 689,793 | 659,627 | 665,024 |
| *Financial liabilities* | | | | | |
| Banks' deposits | Level 3 | 10,317 | 10,325 | 17,190 | 17,203 |
| Deposits of parties that are not banks | Level 3 | 836,961 | 835,179 | 795,915 | 774,402 |
| Borrowings | Level 3 | 43,222 | 44,788 | 32,720 | 31,085 |
| Total | | 890,500 | 890,292 | 845,825 | 822,690 |

### 4.8. Operational risk management

Operational risk management as an important part of the Bank's business activities enables the Bank to operate with its activities successfully and to preserve its reputation.

The Bank performs the following activities with regards to operational risk:
- Permanent identification and risk assessment activities, the identification of all operational risks in business activities in the Bank, in new processes, new products, as well as operating risks related to hiring external suppliers,
- Activities of regular re-identification on an annual basis, review of previously identified operating risks,
- Semi-annual reporting to the Operational risk management board on the maximum limit of risk tolerance, important operational risks of categories A and B (with proposals for their overcoming), as well as important damage events,
- Annual calculation of the Bank's risk profile and comparative overview with risk profile for the previous year and reporting to NLB d.d. and the Operational risk management board,
- Monthly data collection and reporting on negative events,
- Reporting on follow-up and suppressing operational risks on quarterly basis.

## 4. Bank's financial risk management *(continued)*

### 4.8. Operational risk management

In order to improve processes for operational risk management, the Bank performed the following activities:

- Regular activities related to adequate operational risk management for all processes, new projects, outsourcing,and the development of new products, processes and systems, as well as projects being implemented,
- Continuous activities on the identification of operational risks related to "cyber" crime, inadequate software operations, risks of data incorrectly entered into the software, natural disasters risks, risks of noncompliance with legislation, rules, regulations, agreements, prescribed practices, ethical standards and other operational risks that have a little chance of occurrence but may have a very high financial effect, or they represent a very high risk to the reputation of the Bank, and other specific operational risks to which they would like to draw attention,
- Special emphasis on compliance risk (risk of loss due to legal sanctions), risk of conduct (risk of loss due to deliberate deception of customers in the presentation of products and services, and inadequate treatment of clients in resolving their complaints), risks arising from potential adverse events occurred, and the risk of terrorist attacks,
- Permanent support of audit recommendations in assessing the adequacy of system of controls in certain business areas,
- Preparation of analyses of operational risk within the most important business processes for the Bank,
- Establishing and monitoring of adequacy of formed provisions to cover operational risk in accordance with the Federal Banking Agency regulations, and guidelines of the Group, with the purpose of creating consolidated reports, and reporting to Bank authorities, the Operating risks department, and NLB,
- Holding meetings of the Operational risk management board on a quarterly basis,
- Continuous education of employees on processes of identification of operational risks and reporting on recorded damage events, potential damage events and increasing awareness on the presence of such risks in the working environment of all Bank employees.

### 4.9. Capital risk management

In accordance with the Law on Banks, the minimum amount of the Bank's subscribed founding capital cannot be less than BAM 15,000 thousand. Bank's equity includes core capital less core capital deductible items and supplementary capital.

The Bank's core capital comprises paid-in share capital, the Bank's reserves and retained unallocated earnings from previous years. Deductible items of core capital are: intangible assets, uncovered losses from previous years and from the current year, the carrying amount of the Bank's shares owned by the Bank and the amount of negative revaluation reserves from the change in the fair value of assets.
Supplementary capital of the Bank comprises: the general provision for risk for balance sheet items classified in category A, revaluation reserves resulting from a change in the fair value of assets, subordinated debts in accordance with the FBA decision, and other equity instruments.

Regarding capital management the Bank aims to:

- Ensure compliance with the Federal Banking Agency requirements,
- Ensure compliance with NLB Group standards,
- Ensure a solid equity base as support for the further development of Bank operations,
- Ensure the possibility of long-term business continuation while at the same time providing an adequate yield to shareholders.

The Bank is obliged to maintain a capital adequacy ratio at a minimum of 12%, and it has to adjust the scope and structure of its operations to business indicators as defined by the FBA, i.e. in the Decision on minimum standards for bank capital management (Official Gazette of FBiH, No. 03/03, 18/03, 53/06, 55/07, 81/07, 6/08, 86/10, 48/12 and 46/14) and other decisions of FBiH relating to supervision and control of banks' performance and in the Law on Banks FBiH (Official Gazette of FBiH, No. 39/98, 32/00, 48/01, 27/02, 41/02, 58/02, 13/03, 19/03, 28/03, 66/13).

*(All amounts are given in thousand BAM unless otherwise stated)*

## 4. Bank's financial risk management (*continued*)

### 4.9. Capital risk management (*continued*)

Within the scope of regulatory activities and harmonisation with international standards on regulatory capital, the FBA Board of Directors brought a Decision on minimum standards for banks' capital management and capital protection on May 30, 2014 which includes an innovated concept of regulatory capital in comparison to the previously valid regulatory framework. When this decision became effective, the Decision on minimum standards for bank capital management (Official gazette of the FBiH No. 48/12, revised text) and the Decision on temporary limitation and minimum conditions for payment of dividends, discretionary bonuses and redemption of own shares by banks (Official gazette of the FBiH No. 15/13) were placed out of force.
The application of the new Decision for reporting to the FBA has been compulsory since September 30, 2014.

The Bank's Management monitors capital adequacy indicators and other business indicators monthly, and reports on indicators' actual values are delivered to the FBA quarterly in a prescribed form.

The Bank manages its capital and aligns capital management goals in accordance with the Program implemented by the Supervisory Board, market changes and risks specific to the Bank's operations. Depending on the primary goal, the Bank adjusts the capital structure, i.e. increases capital in following ways:

- By adjusting the dividend paid to shareholders, or by increasing share capital arising from retained earnings,
- By increasing capital reserves from realised profit,
- By issuing new shares which can be private and public,
- By increasing additional capital items.

On December 31, 2017 all the Bank's capital indicators were in compliance with all valid regulations.

| | December 31, 2017 (estimate) | December 31, 2016 |
|---|---|---|
| Core Capital | 113,666 | 103,315 |
| Supplementary Capital | 9,725 | 9,042 |
| Missing reserves for losses from loans per regulatory requirements | (5,359) | (10,148) |
| Net capital | 118,032 | 102,209 |
| | | |
| Total risk-weighted assets | 654,415 | 604,482 |
| Total risk-weighted off-balance sheet items | 68,635 | 67,045 |
| Total risk-weighted assets and off-balance sheet items | 723,050 | 671,527 |
| | | |
| Weighted operating risk | 52,970 | 49,797 |
| | | |
| Capital adequacy ratio as of 31 December | 15.2% | 14.2% |

Data presented on December 31, 2017 at the time of preparation of these reports have not yet been reviewed given that the regulatory audit deadline is May 31, 2018.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 5. Net Interest Income

### *a. Interest Income*

| | 2017 | 2016 |
|---|---|---|
| Loans | 42,088 | 42,233 |
| Placements with banks | 58 | 24 |
| Unwinding (*Note 13*) | 443 | 363 |
| Other interest and similar income | 857 | 873 |
| Interest Income | 43,446 | 43,493 |
| Net impairment cost during the year (*Note 13*) | (27) | 30 |
| Net Interest Income | 43,419 | 43,523 |

### *b. Interest Expense*

| | 2017 | 2016 |
|---|---|---|
| Deposits | 6,848 | 8,870 |
| Loan liabilities | 889 | 1,085 |
| Discount amount of provision under IAS 19 (*Note 22a*) | 70 | 88 |
| Other interest expenses | 359 | 370 |
| Interest Expense | 8,166 | 10,413 |
| Net Interest Income | 35,253 | 33,110 |

## 6. Net fee and commission income

### *a. Fee and commission income*

| | 2017 | 2016 |
|---|---|---|
| Income from domestic and international payment transactions | 17,113 | 15,360 |
| Income from guarantees and letters of credit | 1,150 | 1,188 |
| Income from other activities | 2,417 | 2,165 |
| Fee income | 20,680 | 18,713 |

### *b. Fee and commission expense*

| | 2017 | 2016 |
|---|---|---|
| Payment transactions and other banking services expenses | 5,263 | 4,500 |
| Deposit insurance expenses | 1,782 | 1,725 |
| Fee Expense | 7,045 | 6,225 |
| Net fees | 13,635 | 12,488 |

## 7. Foreign exchange gains

| | 2017 | 2016 |
|---|---|---|
| Fee income from foreign exchange transactions | 1,166 | 1,231 |
| Fee expense from foreign exchange transactions | (141) | (201) |
| | 1,025 | 1,030 |
| Foreign exchange differences, net | (328) | 105 |
| | 697 | 1,135 |

*(All amounts are given in thousand BAM unless otherwise stated)*

## 8. Impairment provisions for general credit risk and contingent credit and other losses (net)

| | 2017 | 2016 |
|---|---|---|
| Loans to Customers (*Note 13*) | 3,936 | 9,244 |
| Financial assets available-for-sale (*Note 14*) | 16 | (1) |
| Other assets (*Note 17*) | 252 | 492 |
| Commitments and contingent liabilities (*Note 22c*) | 640 | (1,372) |
| Provisions for legal cases (*Note 22b*) | - | 88 |
| | 4,844 | 8,451 |

## 9. General and administrative expenses

| | 2017 | 2016 |
|---|---|---|
| Rent | 1,871 | 1,776 |
| Amortization of tangible and intangible asset | 1,588 | 1,487 |
| Maintenance | 1,183 | 1,175 |
| Security costs | 1,127 | 1,127 |
| Services | 1,016 | 1,044 |
| Marketing costs | 850 | 917 |
| Postal and telecommunications services cost | 1,016 | 866 |
| Utilities | 727 | 706 |
| Fees to FBA | 634 | 596 |
| Office supplies and small inventory | 606 | 542 |
| Cleaning costs | 277 | 321 |
| Insurance of property and employees | 292 | 278 |
| Other taxes and contributions | 243 | 262 |
| Legal expenses and other administrative expenses | 185 | 228 |
| Other employees' expenses | 140 | 106 |
| | 11,755 | 11,431 |

## 9.a. Employees' expenses

| | 2017 | 2016 |
|---|---|---|
| Net salaries | 8,584 | 8,393 |
| Taxes and contributions | 5,270 | 5,177 |
| Unpaid bonuses from the previous year | (224) | - |
| Meal and transport | 1,080 | 1,120 |
| Holiday allowance | 510 | 515 |
| Other | 478 | 484 |
| | 15,698 | 15,689 |
| Provisions for jubilee awards, released provisions for jubilee awards, provisions for regular severance payments, provisions for unused vacation (*Note 22a*) | 73 | (189) |
| | 15,771 | 15,500 |

Provisions for regular severance payments in 2017 amounted to KM 50 thousand, provisions for unused annual vacations KM 23 thousand and unpaid bonuses from the previous year KM 224 thousand.

The average number of employees by calculated hours in 2017 was 442 (in 2016: 427).

*(All amounts are given in thousand BAM unless otherwise stated)*

## 10. Income tax

| | 2017 | 2016 |
|---|---|---|
| Profit before income tax | 17,491 | 11,769 |
| Non-deductible expenses | 5,529 | 782 |
| Taxable profit | 23,020 | 12,551 |
| Income tax at the prescribed rate of 10% | 2,302 | 1,255 |
| Income tax in Brčko District not recognised under the regulations of the Federation BiH | 3 | 1 |
| Total calculated income tax | 2,305 | 1,256 |
| Effective tax rate | 13,18% | 10,67% |

In 2017, there was a significant increase in tax non-deductible expenses compared to 2016, of which the largest part refers to expense on the basis of value adjustments that are estimated on a group basis and based on historical cost, where there is no objective evidence of impairment, then the part refers to the sale of receivables, and the part for value impairment of two real estates (Note 3.16.).

## 11. Cash and balances with the Central Bank of BiH

| | 2017 | 2016 |
|---|---|---|
| Cash in hand | 41,516 | 40,335 |
| Balances with the Central Bank of Bosnia and Herzegovina | 196,819 | 189,879 |
| - Obligatory reserve | 90,584 | 85,323 |
| - Liquidity reserves in excess of obligatory reserve | 106,235 | 104,556 |
| | 238,335 | 230,214 |

The obligatory reserve represents amounts required to be deposited with the Central Bank of Bosnia and Herzegovina. According to the Law on the Central Bank of Bosnia and Herzegovina, starting from 1. July 2016 the obligatory reserve requirement represents 10% of average ten-day deposits and borrowings in BAM. The obligatory reserve is maintained through average account balances with the Central Bank of Bosnia and Herzegovina.

## 12. Placements with banks

| | 2017 | 2016 |
|---|---|---|
| Current accounts with banks | 45,286 | 42,720 |
| Items in the course of collection | - | 1 |
| Interest-bearing deposits | 4,488 | 5,106 |
| | 49,774 | 47,827 |

## 13. Loans to customers

| | Short-term loans | | Long-term loans | | Total | |
|---|---|---|---|---|---|---|
| | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 |
| Retail loans | 31,631 | 32,195 | 358,763 | 320,999 | 390,394 | 353,194 |
| Corporate loans | 176,932 | 180,887 | 157,358 | 154,603 | 334,290 | 335,490 |
| | 208,563 | 213,082 | 516,121 | 475,602 | 724,684 | 688,684 |
| Less: Allowance for impairment losses | (28,810) | (33,377) | (44,451) | (43,507) | (73,261) | (76,884) |
| | 179,753 | 179,705 | 471,670 | 432,095 | 651,423 | 611,800 |

*(All amounts are given in thousand BAM unless otherwise stated)*

## 13. Loans to Customers (*continued)*

Movement in allowance for impairment losses per loans is as follows:

| | 2017 | 2016 |
|---|---|---|
| 1 January | 76,884 | 73,092 |
| Charge for the year | 43,477 | 34,710 |
| Decrease in provisions | (39,541) | (25,466) |
| Charge for the year, net (*Note 8*) | 3,936 | 9,244 |
| Decrease in provisions on the basis of unwinding (*Note 5a*) | (443) | (363) |
| Net impairment of interest receivables(*Note 5a*) | (27) | (30) |
| Write-offs | (7,089) | (5,059) |
| 31 December | 73,261 | 76,884 |

During the year 2017, and in particular in December, the Department for Collection and NPL Management, through the implementation of the collection activities, had a direct impact on the significant reduction of NPL and low-quality assets.

Although loans grew in 2017 compared to 2016, there was a lower net impairment compared to 2016, largely as a result of the collection of NPL loans, which was realized in a more significant amount in the last month of 2017.

## 14. Financial assets available-for-sale

| | 2017 | 2016 |
|---|---|---|
| Debt securities | | |
| Government of Federation of BiH – Federal Ministry of Finance | 61,120 | 58,222 |
| Republic of Srpska - Ministry of Finance | 12,870 | - |
| Republic of Slovenia - Ministry of Finance | - | 3,918 |
| Canton Sarajevo | 932 | - |
| Equity securities | | |
| Privredna banka Sarajevo d.d., Sarajevo | - | 44 |
| S.W.I.F.T., Belgium | 55 | 51 |
| Registry of Securities of FBiH, Sarajevo | 14 | 14 |
| Banks' Association of BiH, Sarajevo | 14 | 14 |
| | 75,005 | 62,263 |
| Less: Value adjustment | 16 | - |
| | 74,989 | 62,263 |

Movement in value adjustment:

| | 2017 | 2016 |
|---|---|---|
| 1 January | - | 1 |
| Increase for the year, net (*Note 8*) | 16 | (1) |
| 31 December | 16 | - |

*(All amounts are given in thousand BAM unless otherwise stated)*

14. Financial assets available-for-sale *(continued)*

| Structure of investments | Activity | % of ownership | Country of business |
|---|---|---|---|
| Banks' Association of BiH | Activity of other member organisations | 4.18 | Bosnia and Herzegovina |
| Registry of Securities of FBiH | Registering and maintenance of securities' data | 0.687 | Bosnia and Herzegovina |
| S.W.I.F.T. | Payment transactions | 0.0054 | Belgium |
| Master Card Incorporated | Card services | 0.0614 | USA |

The Bank has the following debt securities in its portfolio:

| Debt securities | 31/12/2017 | 31/12/2016 |
|---|---|---|
| Bonds of Government of the Federation of BiH - war claims | 796 | 713 |
| Bonds of the Ministry of Finance FBiH | 25,832 | 26,704 |
| Bonds of the Ministry of Finance RS | 2,893 | - |
| Bonds of the Ministry of Finance of Canton Sarajevo | 916 | - |
| Treasury bills of the Republic of Slovenia | - | 3,918 |
| Treasury bills of Ministry of Finance of FBiH | 34,492 | 30,805 |
| Treasury bills of Ministry of Finance of RS | 9,977 | - |
| Total | 74,906 | 62,140 |

In 2017, the Bank bought the following securities:

- Bonds issued based on war claims by Government of the Federation of Bosnia and Herzegovina with nominal value of BAM 1.18 million. Interest rate on purchased bonds is 2.5% per annum, maturity date June 30, 2023.
- Bonds of the Ministry of Finance of RS with nominal value of BAM 2.8 million. Interest rate on purchased bonds is 3.5% per annum, maturity date May 5 and November 3, 2022.
- Bonds of the Ministry of Finance of Canton Sarajevo with nominal value of BAM 0.9 million. Interest rate on purchased bonds is 2.85% and 3.5% per annum, maturity date June 2, 2020 and September 28, 2022.
- Treasury bills of the Federation of BiH, with nominal value of BAM 48 million, with yields until maturity ranging 0% to 0.25%.
- Treasury bills of the Republic of Srpska, with nominal value of BAM 12.2 million, with yields until maturity ranging 0.45% to 0.75%.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 14. Financial assets available-for-sale *(continued)*

In 2017, the following securities became due:

- Bonds of the Federation of BiH with nominal value of BAM 2 million. became due on December 3, 2017;
- Treasury bills of the Republic of Slovenia, with nominal value of BAM 3.9 million. became due on October 5, 2017;
- The treasury bills of the Federation of Bosnia and Herzegovina with nominal value and maturity are given as follows: BAM 15 million – July 19, 2017, BAM 1 million –July 26, 2017, BAM 6.5 million – August 9, 2017, BAM 12.8 million – November 22, 2017, BAM 4 million –December 6, 2017, and BAM 5 million – December 13, 2017.

Treasury bills of the Republic of Srpska, with nominal value of BAM 2.2 million became due on December 8, 2017;

Overview of securities per fair value hierarchy levels as of December 31, 2017:

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Debt securities | - | 74,906 | - | 74,906 |
| Equity securities | - | - | 83 | 83 |
| Total | - | 74,906 | 83 | 74,989 |

Overview of securities per fair value hierarchy levels as of December 31, 2016:

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Debt securities | 3,918 | 58,222 | - | 62,140 |
| Equity securities | - | - | 123 | 123 |
| Total | 3,918 | 58,222 | 123 | 62,263 |

In 2017, long-term treasury bills the Ministry of Finance of the Republic of Slovenia with a nominal value of EUR 2,000 thousand matured, that were listed in Level 1.

The portfolio of debt securities at level 2 consists of long-term bonds of the Federal Ministry of Finance worth BAM 26,628 thousand, short-term treasury bills of the Federal Ministry of Finance worth BAM 34,492 thousand, long-term bonds of the Ministry of Finance of the Republic of Srpska worth BAM 2,893 thousand, short-term treasury bills of the Ministry of Finance of the Republic of Srpska in the amount of BAM 9,977 thousand, and long-term bonds of Canton Sarajevo worth BAM 916 thousand.

In level 3 are included equity securities. The fall in the value of the previous year was due to the sale of shares of Privredna banka Sarajevo by BAM 35 thousand and an increase in share value of Swift by BAM 5 thousand.

*(All amounts are given in thousand BAM unless otherwise stated)*

15. Tangible assets

| | Land and buildings | Vehicles | Computer equipment | Other equipment | Assets in the course of construction | Total |
|---|---|---|---|---|---|---|
| Cost | | | | | | |
| At January 1, 2016 | 28,246 | 991 | 6,363 | 6,127 | - | 41,727 |
| Additions | - | - | - | - | 1,805 | 1,805 |
| Transfers | 505 | 239 | 518 | 348 | (1,610) | - |
| Disposals | | | | | | |
| - Write-offs | - | - | (782) | (728) | - | (1,510) |
| - Sale of tangible assets | - | (404) | - | - | - | (404) |
| At December 31, 2016 | 28,751 | 826 | 6,099 | 5,747 | 195 | 41,618 |
| *At January 1, 2017* | 28,751 | 826 | 6,099 | 5,747 | 195 | 41,618 |
| Additions | - | - | - | - | 2,653 | 2,653 |
| Transfers | 180 | 243 | 458 | 305 | (1,186) | - |
| Disposals | | | | | | |
| - Write-offs | - | - | (262) | (470) | - | (732) |
| - Disposal under IAS 36 | (255) | | | | | (255) |
| - Sale of tangible assets | - | (126) | - | - | - | (126) |
| At December 31, 2017 | 28,676 | 943 | 6,295 | 5,582 | 1,662 | 43,158 |
| Accumulated depreciation | | | | | | |
| At January 1, 2016 | 11,696 | 566 | 4,782 | 4,880 | - | 21,924 |
| Depreciation charge for the year | 369 | 87 | 572 | 319 | - | 1,347 |
| - Write-offs | - | | (782) | (714) | - | (1,496) |
| - Sale of tangible assets | - | (244) | - | - | - | (244) |
| At December 31, 2016 | 12,065 | 409 | 4,572 | 4,485 | - | 21,531 |
| *At January 1, 2017* | 12,065 | 409 | 4,572 | 4,485 | - | 21,531 |
| Depreciation charge for the year | 373 | 110 | 582 | 324 | - | 1,389 |
| - Write-offs | - | - | (260) | (469) | - | (729) |
| - Disposal under IAS 36 | (46) | - | - | - | - | (46) |
| - Sale of tangible assets | - | (126) | - | - | - | (126) |
| At December 31, 2017 | 12,392 | 393 | 4,894 | 4,340 | - | 22,019 |
| Net book value at December 31, 2017 | 16,284 | 550 | 1,401 | 1,242 | 1,662 | 21,139 |
| Net book value at December 31, 2016 | 16,686 | 417 | 1,527 | 1,262 | 195 | 20,087 |

In 2017 and 2016, items of real estate and equipment were not pledged as collateral (pledge) for the Bank's liabilities. The total cost of fully depreciated assets still in use amounts to BAM 6,577 thousand as at December 31, 2017, while as at December 31, 2016 it was BAM 6,957 thousand.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 16. Intangible assets

| | Licenses and software |
|---|---|
| **Cost** | |
| At January 1, 2016 | *4,655* |
| Additions | 175 |
| Disposals-Write-offs | (20) |
| At December 31, 2016 | 4,810 |
| *At January 1, 2017* | *4,810* |
| Additions | 310 |
| Disposals-Write-offs | |
| At December 31, 2017 | 5,120 |
| | |
| **Accumulated depreciation** | |
| At January 1, 2016 | 4,253 |
| Depreciation | 139 |
| Disposals-Write-offs | (20) |
| At December 31, 2016 | 4,372 |
| *At January 1, 2017* | 4,372 |
| Depreciation | 196 |
| Disposals-Write-offs | |
| At December 31, 2017 | 4,568 |
| | |
| Net book value at December 31, 2017 | 552 |
| Net book value at December 31, 2016 | 438 |

The total cost of fully depreciated intangible assets still in use amounts to BAM 4,047 thousand as at December 31, 2017, while as at December 31, 2016 it was BAM 4,039 thousand.

## 17. Other assets

| | 2017 | 2016 |
|---|---|---|
| *Other financial assets* | | |
| Service fees accrued | 474 | 457 |
| Other assets | 3,950 | 3,386 |
| | 4,424 | 3,843 |
| Less: Impairment allowance | (2,123) | (2,027) |
| | 2,301 | 1,816 |
| *Other assets* | | |
| Acquired tangible assets | 1,598 | 1,084 |
| Prepaid costs | 188 | 170 |
| Small inventory | 17 | 116 |
| Advance for corporation tax | - | 119 |
| | 1,803 | 1,489 |
| Less (impairment/value adjustment): | | |
| Acquired tangible assets | (914) | (808) |
| Other non-financial assets | (2) | (4) |
| Other non-financial assets | 887 | 677 |
| | 3,188 | 2,493 |

Movement in value adjustment:

| | 2017 | 2016 |
|---|---|---|
| 1 January | 2,839 | 2,451 |
| Increase for the year, net (*Note 8*) | 252 | 492 |
| Write-offs | (52) | (104) |
| 31 December | 3,039 | 2,839 |

*(All amounts are given in thousand BAM unless otherwise stated)*

## 17. Other assets *(continued)*

Repossessed tangible assets are presented within Other assets of the Bank in the amount of BAM 1,598 thousand as at December 31, 2017, and they relate to real estate repossessed for unsettled debts.

All repossessed tangible assets are located on the territory of Bosnia and Herzegovina.

The Bank plans to sell repossessed assets taken over for unsettled debts in the period of one year after the date of acquiring of these assets. For assets not sold within one year, evaluation is made and adequate impairment is recognized.

## 18. Banks' deposits

| | 2017 | 2016 |
|---|---|---|
| Nova Ljubljanska banka d.d., Ljubljana | 7,060 | 14,524 |
| NLB Tutunska banka AD Skopje | 1,627 | 2,393 |
| NLB Montenegrobanka AD Podgorica | 5 | 120 |
| NLB Banka AD Banja Luka | 1,041 | - |
| Other banks | 584 | 153 |
| | 10,317 | 17,190 |

## 19. Customers' deposits

| | 2017 | 2016 |
|---|---|---|
| Companies: | | |
| Current accounts | | |
| - in BAM | 223,839 | 212,195 |
| - in foreign currencies | 28,259 | 27,016 |
| Term deposits | | |
| - in BAM | 47,412 | 48,646 |
| - in foreign currencies | 26,205 | 16,836 |
| | 325,715 | 304,693 |
| Citizens: | | |
| Current accounts | | |
| - in BAM | 165,120 | 151,219 |
| - in foreign currencies | 56,355 | 51,311 |
| Term deposits | | |
| - in BAM | 126,387 | 119,641 |
| - in foreign currencies | 163,384 | 169,051 |
| | 511,246 | 491,222 |
| | 836,961 | 795,915 |

## 20. Borrowings

| | 2017 | 2016 |
|---|---|---|
| Nova Ljubljanska banka d.d., Ljubljana | 23,955 | 7,858 |
| European Fund for South-East Europe (EFSE) | 9,791 | 9,777 |
| Slovenian bank for export and development d.d., Ljubljana | - | 2,061 |
| Federal Ministry of Finance | 9,476 | 13,024 |
| | 43,222 | 32,720 |

Long-term borrowings are used for alignment of maturity structure of financial assets and financial liabilities, as well as for placement of funds.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 20. Borrowings (*continued*)

Long-term loans from banks and non-banking financial institutions obtained from NLB d.d., Ljubljana and investment funds EFSE. Liabilities to other long-term loans relate to subsidiary financing from the World Bank funds through the Federal Ministry of Finance.

Interest rates on the entire portfolio of long-term credit lines from banks and non-banking financial institutions for the year ended December 31, 2016 were fixed interest rate of 2.92% per annum, while variable interest rates ranged from 6M EURIBOR + 1.65% to 6M EURIBOR + 3.90%. Interest rates on other long-term loans were 6M EUROLIBOR + 1.00%.
Interest rates on the entire portfolio of long-term credit lines from banks and non-banking financial institutions for the year ended December 31, 2017 were fixed interest rate ranging from 2.20% to 2.92% per annum, while variable interest rates ranged from 6M EURIBOR + 1.65% to 6M EURIBOR + 2.01%. Interest rates on other long-term loans were 6M EUROLIBOR + 1.00%.

In order to provide the Bank with access to diversified sources of assets, as at December 31, 2017 the Bank has the concluded a Credit Line Contract with Nova Ljubljanska banka d.d., Ljubljana to the amount of EUR 10 million; a Business Cooperation Contract with NLB Banka a.d. Banja Luka and Union banka d.d., Sarajevo to the maximum amount of EUR 5 million, and BAM 3 million respectively.
The funds from these credit lines have not been withdrawn by the Bank.

## 21. Other liabilities

| | 2017 | 2016 |
|---|---|---|
| *Other financial liabilities* | | |
| Paid amount for not due loan receivables | 2,782 | 2,774 |
| Unallocated payments received | 2,018 | 1,127 |
| Liabilities to employees | 750 | 573 |
| Liabilities to suppliers | 2,162 | 742 |
| Liabilities from commission operations | - | 12 |
| Liabilities for taxes and contributions | 55 | 40 |
| Liabilities for other banking fees | 16 | 48 |
| Other liabilities | 2,685 | 1,494 |
| | 10,468 | 6,810 |
| *Other non-financial liabilities* | | |
| Deferred income | 105 | 111 |
| | 105 | 111 |
| | 10,573 | 6,921 |

*(All amounts are given in thousand BAM unless otherwise stated)*

## 21. Other Liabilities (*continued*)

### 21.a. The management of assets in the name of and on behalf of clients

| | 2017 | 2016 |
|---|---|---|
| Corporate | 13,756 | 10,023 |
| Retail | 8,186 | 8,157 |
| Total placements | 21,942 | 18,181 |
| | | |
| Government of Tuzla Canton | 14,558 | 11,990 |
| Government of Sarajevo Canton | 4,215 | 3,810 |
| Other non-banking financial institutions | 3,169 | 2,393 |
| Total sources (liabilities) | 21,942 | 18,193 |
| Difference | - | 12 |

Funds managed by the Bank as an agent for and on behalf of third parties do not represent Bank assets, in the Bank balance.

The Bank manages certain assets on behalf of third parties by investing the funds in long-term loans granted to companies and individuals. The Bank does not bear the risk for these placements, and charges a fee for its services.

## 22. Other provisions

| | 2017 | 2016 |
|---|---|---|
| Provisions for employees | 1,527 | 1,378 |
| Provisions for litigations | 103 | 126 |
| Provisions for off-balance sheet exposures | 3,261 | 2,637 |
| | 4,891 | 4,141 |

### a. Movement of provisions in accordance with IAS 19

| | 2017 | 2016 |
|---|---|---|
| Opening balance as of January 1 | 1,378 | 1,442 |
| Expenses during the year | 73 | 107 |
| Release in provisions for unused vacation and jubilee awards | - | (296) |
| Increase for the year, net (*Note 9a*) | 73 | (189) |
| Discount amount of provision under IAS 19 (*Note 5b*) | 70 | 88 |
| (Additional provisions)/ Release through equity | 84 | 113 |
| Utilization | (78) | (76) |
| | 1,527 | 1,378 |

### b. Movement of provisions for litigations

| | 2017 | 2016 |
|---|---|---|
| Opening balance as of January 1 | 126 | 38 |
| Increase for the year, net (*Note 8*) | - | 88 |
| Utilization | (23) | - |
| | 103 | 126 |

### c. Provisions for off-balance

| | 2017 | 2016 |
|---|---|---|
| Opening balance as of January 1 | 2,637 | 4,004 |
| (Decrease)/Increase for the year, net (*Note 8*) | 640 | (1,372) |
| Foreign exchange differences, net | (16) | 5 |
| | 3,261 | 2,637 |

*(All amounts are given in thousand BAM unless otherwise stated)*

## 23. Share capital

| | 2017 | 2016 |
|---|---|---|
| Number of shares | 382,894 | 382,894 |
| -Ordinary shares | 382,712 | 382,712 |
| -Preference shares | 182 | 182 |

Preference shares were issued in 1991 bearing a dividend in an amount equal to the interest rate on retail term deposits with a maturity of over 3 years, applicable from the date on which the Shareholders' Assembly is held.

Ownership structure is presented within the Note 1.

### Earnings per share

Bank shares are traded on the Stock Market. The Bank calculates and discloses earnings per share in accordance with IAS 33. Basic earnings per share are calculated by dividing net profit attributable to ordinary shareholders by the weighted average number of ordinary shares for the period (amounts in absolute values). The Bank does not have instruments, such as convertible debt or share options, for which there could be diluted earnings per share. For this reason, the Bank does not calculate diluted earnings per share, meaning it is the same as the basic earnings per share.

| | 2017 | 2016 |
|---|---|---|
| Net profit of the Bank after tax (in BAM) | 15,186,577 | 10,513,537 |
| Weighted number of shares | 382,712 | 382,712 |
| Basic earnings per Share (in BAM) | 39.68 | 27.47 |

## 24. Transactions with related parties

Parties are considered to be related when one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions.

NLB d.d., Ljubljana is 100% owned by the Republic of Slovenia and therefore the Republic of Slovenia is considered a related party to the Bank. Transactions with the Bank management and members of their families have likewise been considered transactions with related parties in 2016 and 2017.

Transactions with related parties are a part of everyday operations. These transactions include loans, deposits, and borrowings, received and issued guarantees and other potential liabilities.

Memberships of members of the Supervisory Board and Bank Management in other affiliates and non-affiliates are specified in Note 1.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 24. Transactions with related parties (*continued*)

The scope of related party transactions and year-end balances are presented in the table below:

| | 2017 | 2016 |
|---|---|---|
| Owner | | |
| Assets: | | |
| Loans and other liabilities: | | |
| - Nova Ljubljanska banka d.d., Ljubljana | 5 | 1 |
| Accounts in foreign currency: | | |
| - Nova Ljubljanska banka d.d., Ljubljana | 3,965 | 4,309 |
| Accrued interests: | | |
| - Nova Ljubljanska banka d.d., Ljubljana | - | 2 |
| Liabilities: | | |
| A vista deposits: | | |
| - Nova Ljubljanska banka d.d., Ljubljana | 1,192 | 833 |
| Short-term deposits: | | |
| - Nova Ljubljanska banka d.d., Ljubljana | 5,867 | 13,691 |
| Long-term Loans: | | |
| - Nova Ljubljanska banka d.d., Ljubljana | 23,886 | 7,823 |
| Other liabilities: | | |
| - Nova Ljubljanska banka d.d., Ljubljana | 31 | 19 |
| Accrued interests: | | |
| - Nova Ljubljanska banka d.d., Ljubljana | 147 | 67 |

| Others | 2017 | 2016 |
|---|---|---|
| Assets: | | |
| Loans and other liabilities: | | |
| - NLB Banka a.d., Banja Luka | 186 | 188 |
| - Ministry of Finance of the Republic of Slovenia | - | 3,920 |
| - Individuals | 366 | 36 |
| Accounts in foreign currency: | | |
| - NLB Banka AD., Belgrade | 562 | 556 |
| - NLB Banka AD, Skopje | 441 | 338 |
| - NLB Banka AD, Podgorica | 465 | 484 |
| Term deposits: | | |
| - NLB Banka AD, Banja Luka | 410 | 467 |
| Accrued interests: | | |
| - Individuals | 1 | - |

*(All amounts are given in thousand BAM unless otherwise stated)*

24. Transactions with related parties (*continued*)

| | | |
|---|---|---|
| Liabilities: | | |
| A vista deposits: | | |
| - NLB Leasing d.o.o., Sarajevo | 907 | 158 |
| - Prvi faktor d.o.o., Sarajevo | 172 | 23 |
| - NLB Banka AD, Skopje | 1,627 | 2,393 |
| - NLB Banka AD, Banja Luka | 1,041 | - |
| -NLB Banka AD Belgrade | 286 | - |
| - NLB Banka AD, Podgorica | 5 | 120 |
| - CBS Invest d.o.o., Sarajevo | 96 | 14 |
| - BH-RE d.o.o. Sarajevo | 17 | 7 |
| - Individuals | 46 | 24 |
| Long-term deposits: | | |
| - NLB Leasing d.o.o., Sarajevo | 450 | 450 |
| - Individuals | 11 | 173 |
| Other liabilities: | | |
| - NLB Banka AD, Banja Luka | 27 | 24 |
| - Ministry of Finance of the Republic of Slovenia | - | 1 |
| - Individuals | 7 | 1 |
| Accrued interests: | | |
| - Individuals | 1 | 1 |

| Owner | 2017 | 2016 |
|---|---|---|
| Income and expenses: | | |
| Interest Income: | | |
| - Nova Ljubljanska banka d.d., Ljubljana | 5 | 1 |
| Income from fees: | | |
| - Nova Ljubljanska banka d.d., Ljubljana | 14 | 11 |
| Interest Expenses: | | |
| - Nova Ljubljanska banka d.d., Ljubljana | 381 | 396 |
| Expenses from fees: | | |
| - Nova Ljubljanska banka d.d., Ljubljana | 79 | 154 |
| Other expenses: | | |
| - Nova Ljubljanska banka d.d., Ljubljana | 28 | 47 |
| Others | | |
| Income and expenses: | | |
| Interest Income: | | |
| - Individuals | 10 | 3 |
| Income from fees: | | |
| - Prvi faktor d.o.o., Sarajevo | 1 | 13 |
| - NLB Razvojna banka a.d., Banja Luka | 157 | 145 |
| - NLB Leasing d.o.o., Sarajevo | 33 | 7 |
| - Individuals | 3 | 2 |

*(All amounts are given in thousand BAM unless otherwise stated)*

## 24. Transactions with related parties (*continued*)

| | | |
|---|---|---|
| Interest Expenses: | | |
| - NLB Leasing d.o.o., Sarajevo | 6 | 7 |
| - Ministry of Finance of the Republic of Slovenia | 2 | 1 |
| - Individuals | 1 | 1 |

Owner

| | | |
|---|---|---|
| Guarantees and other assurances: (Off-balance sheet exposure, i.e. granted loans basis | | |
| -Nova Ljubljanska banka d.d., Ljubljana | 3,000 | - |

Others

| | | |
|---|---|---|
| -Prvi faktor d.o.o., Sarajevo | 2 | 2 |
| -NLB Leasing d.o.o., Sarajevo | 4 | 5 |
| - Individuals | 27 | 19 |

### Management remuneration

| | 2017 | 2016 |
|---|---|---|
| Net salaries | 473 | 438 |
| Taxes and contributions | 289 | 267 |
| Other remunerations | 179 | 575 |
| Taxes and contributions | 112 | 340 |
| | 1,053 | 1,620 |

In other income the Bank has an increase of BAM 396 thousand, while taxes and contributions on other earnings increased by BAM 228 thousand compared to 2016.
In 2016, severance payments to two Bank management members were allocated to Bank expenses, which is not the case in 2017, and there are no taxes and contributions on severance payments.
In 2017 the Bank has not paid bonus for Bank management members.

### Remunerations of Bank's Supervisory and Audit Committees' members

| | 2017 | 2016 |
|---|---|---|
| Fees paid to SB and AC members | 18 | 8 |
| Taxes and contributions | 4 | 2 |
| | 22 | 10 |

During 2016 the fee was paid to one member of the Supervisory Board of the Bank.
During 2017 the fee was paid to two members of the Supervisory Board of the Bank and to one member of the Audit Committee of the Bank.

*(All amounts are given in thousand BAM unless otherwise stated)*

## 25. Contingencies and Commitments

The following table presents contractual amounts which refer to possible and assumed liabilities of the Bank:

| | 2017 | 2016 |
|---|---|---|
| Guarantees | | |
| - in BAM | 34,025 | 32,520 |
| - in foreign currencies | 13,740 | 18,944 |
| Letter of Credits | 362 | 2,268 |
| Granted loans not yet utilised | 82,001 | 62,754 |
| Less: Value adjustment for potential losses | (3,261) | (2,637) |
| | 126,867 | 113,849 |

*Operating leases*

The Bank leases business premises in the whole of Bosnia and Herzegovina.
Based on lease contracts, commitments are as follows:

| | 2017 | 2016 |
|---|---|---|
| Commitments for leases | 1,878 | 1,776 |
| | 1,878 | 1,776 |

| | 2017 | 2016 |
|---|---|---|
| Maturity up to 1 year | 413 | 495 |
| Maturity from 2 to 5 years | 1,175 | 959 |
| Maturity over 5 years | 290 | 322 |
| | 1,878 | 1,776 |

*Ongoing court cases*

As of December 31, 2017 there were 88 cases against the Bank for which assessment of legal risk is performed. The total value of these court cases against the Bank as at December 31, 2017 amounts to BAM 60,107 thousand; EUR 292 thousand; CHF 5 thousand, and USD 1 thousands.

In 2017 there were 14 new legal actions initiated against the Bank.

In the period from January 1 to December 31, 2017 the Bank won 11 cases.

The Bank continuously monitors the legal risk, estimates expected costs based on the legal risk and sets adequate provisions on that basis.

## 26. Operations by segments

Segment analysis is used for internal financial reporting of business results. Segments include Corporate and SME, Micro and Retail, Treasury and Collection. Interest income is allocated on segments applying the internal transfer prices (ITP) which are set by the Treasury centre depending on prevailing market conditions. Allocation of joint expenses, service and overhead costs is performed according to appropriate keys, i.e. based on the plan weighted indices.

*(All amounts are given in thousand BAM unless otherwise stated)*

26. Operations by segments (*continued*)

Statement of financial position per segments as of December 31, 2017:

| | Corporate and SME | Micro and Retail | Treasury | Collection | Other | Bank |
|---|---|---|---|---|---|---|
| ASSETS | | | | | | |
| Cash and balances with the CB BiH | - | 31,199 | 196,819 | - | 10,317 | 238,335 |
| Loans | 266,969 | 371,954 | 49,774 | 12,500 | - | 701,197 |
| Financial assets available-for-sale | - | - | 74,989 | - | - | 74,989 |
| Tangible and intangible assets | - | - | - | - | 21,691 | 21,691 |
| Other assets | 127 | 689 | 7 | 684 | 1,681 | 3,188 |
| Total assets | 267,096 | 403,842 | 321,589 | 13,184 | 33,689 | 1,039,400 |
| | | | | | | |
| LIABILITIES | | | | | | |
| Deposits | 187,504 | 647,721 | 10,166 | 1,735 | 152 | 847,278 |
| Borrowings | - | - | 43,222 | - | - | 43,222 |
| Other liabilities | 1,109 | 3,371 | 2,164 | 101 | 3,828 | 10,573 |
| Provisions for contingencies and commitments, for employees and legal risk | 2,154 | 879 | - | 329 | 1,529 | 4,891 |
| Total liabilities | 190,767 | 651,971 | 55,552 | 2,165 | 5,509 | 905,964 |

Statement of financial position per segments as of December 31, 2016:

| | Corporate and SME | Micro and Retail | Treasury | Collection | Other | Bank |
|---|---|---|---|---|---|---|
| ASSETS | | | | | | |
| Cash and balances with the CB BiH | - | 26,387 | 189,879 | - | 13,948 | 230,214 |
| Loans | 246,140 | 343,255 | 47,827 | 22,405 | - | 659,627 |
| Financial assets available-for-sale | - | - | 62,263 | - | - | 62,263 |
| Tangible and intangible assets | - | - | - | - | 20,525 | 20,525 |
| Other assets | 102 | 506 | 7 | 278 | 1,600 | 2,493 |
| Total assets | 246,242 | 370,148 | 299,976 | 22,683 | 36,073 | 975,122 |
| | | | | | | |
| LIABILITIES | | | | | | |
| Deposits | 184,102 | 611,420 | 17,037 | 395 | 151 | 813,105 |
| Borrowings | - | - | 32,720 | - | - | 32,720 |
| Other liabilities | 1,377 | 2,951 | 971 | 62 | 1,560 | 6,921 |
| Provisions for contingencies and commitments, for employees and legal risk | 1,889 | 557 | - | 315 | 1,380 | 4,141 |
| Total liabilities | 187,368 | 614,928 | 50,728 | 772 | 3,091 | 856,887 |

*(All amounts are given in thousand BAM unless otherwise stated)*

## 26. Operations by segments (*continued*)

Income statement by segments for the year 2017:

| | Corporate and SME | Micro and Retail | Treasury | Collection | Bank |
|---|---|---|---|---|---|
| Interest Income | 10,668 | 29,640 | 914 | 2,197 | 43419 |
| Interest Expense | (1,465) | (5,413) | (1,260) | (28) | (8,166) |
| Net Interest Income (before transfer prices) | 9,203 | 24,227 | (346) | 2,169 | 35,253 |
| Margin on assets | 6,735 | 19,571 | 336 | 1,731 | 28,373 |
| Margin on liabilities | 125 | 3,015 | (80) | (26) | 3,034 |
| ALM | - | - | 3,846 | - | 3,846 |
| Net Interest Income (by transfer prices) | 6,860 | 22,586 | 4,102 | 1,705 | 35,253 |
| Impairment provisions for general credit risk and contingent credit and other losses | 168 | (6,560) | (17) | 1,565 | (4,844) |
| Net Interest Income after provision for losses | 7,028 | 16,026 | 4,085 | 3,270 | 30,409 |
| Net non-interest income | 1,876 | 14,190 | 625 | 272 | 16,963 |
| Total operative income | 8,904 | 30,216 | 4,710 | 3,542 | 47,372 |
| Total expense | (3,740) | (22,572) | (1,826) | (1,743) | (29,881) |
| Profit before income tax | 5,164 | 7,644 | 2,884 | 1,799 | 17,491 |

Income statement by segments for the year 2016:

| | Corporate and SME | Micro and Retail | Treasury | Collection | Bank |
|---|---|---|---|---|---|
| Interest Income | 13,238 | 28,416 | 897 | 972 | 43,523 |
| Interest Expense | (2,258) | (6,688) | (1,467) | - | (10,413) |
| Net Interest Income (before transfer prices) | 10,980 | 21,728 | (570) | 972 | 33,110 |
| Margin on assets | 7,533 | 17,388 | 346 | 540 | 25,807 |
| Margin on liabilities | 292 | 2,780 | (249) | - | 2,823 |
| ALM | - | - | 4,480 | - | 4,480 |
| Net Interest Income (by transfer prices) | 7,825 | 20,168 | 4,577 | 540 | 33,110 |
| Impairment provisions for general credit risk and contingent credit and other losses | (3,143) | (2,031) | 7 | (3,284) | (8,451) |
| Net Interest Income after provision for losses | 4,682 | 18,137 | 4,584 | (2,744) | 24,659 |
| Net non-interest income | 1,716 | 11,754 | 978 | 183 | 14,631 |
| Total operative income | 6,398 | 29,891 | 5,562 | (2,561) | 39,290 |
| Total expense | (3,666) | (21,198) | (1,541) | (1,116) | (27,521) |
| Profit before income tax | 2,732 | 8,693 | 4,021 | (3,677) | 11,769 |

## 27. Events after the date of reporting

Since December 31, 2017, after the balance sheet date, until the date of submission of the report, there have been no events with a significant impact on the Bank's position or requiring an additional explanation.