
# Addiko Bank

## Financial statements

for the year ended 31 December 2019 and Independent auditor’s report

This version of the report is a translation from the original, which was prepared in Serbian language. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our financial reports and the accompanying audit report takes precedence over this translation.

# Key data based on the financial statements

| | | | BAM ths |
|---|---|---|---|
| **Selected items of the Profit or Loss statement** | **YE19** | **YE18** | **Change (%)** |
| Net banking income | 37,555 | 37,634 | -0.2% |
| Net interest income | 25,035 | 25,244 | -0.8% |
| Net fee and commission income | 12,520 | 12,390 | 1.0% |
| Net result on financial instruments | 317 | 91 | >100% |
| Other operating result | (2,270) | (880) | >100% |
| Operating expenses | (28,355) | (28,508) | -0.5% |
| **Operating result before change in credit loss expense** | 7,247 | 8,337 | -13.1% |
| Credit loss expenses on financial assets | (543) | (5,059) | -89.3% |
| Tax on income | 16 | 7 | >100% |
| **Result after tax** | 6,720 | 3,285 | **>100%** |
| | | | |
| **Performance ratios** | **YE19** | **YE18** | **Change (pts)** |
| Net interest income/total average assets | 3.1% | 3.4% | -0.3 |
| Return on tangible equity | 4.4% | 2,2% | 2.2 |
| Cost/income ratio | 79.6% | 77.4% | 2.2 |
| Cost of risk ratio | 0.1% | 0.3% | -0.2 |
| | | | |
| **Selected items of the Statement of financial position** | **Dec19** | **Dec18** | **Change (%)** |
| Loans and receivables to customers | 564,206 | 506,896 | 11.3% |
| o/w gross performing loans | 567,090 | 507,320 | 11.8% |
| Deposits of customers | 557,561 | 540,245 | 3.2% |
| Equity | 161,201 | 154,461 | 4.4% |
| Total assets | 842,177 | 795,663 | 5.8% |
| Risk-weighted assets | 683,958 | 591,536 | 15.6% |
| | | | |
| **Balance sheet ratios** | **Dec19** | **Dec18** | **Change (pts)** |
| Loan to deposit ratio | 101.2% | 93.8% | 7.4 |
| NPE ratio | 9.1% | 9.8% | -0.7 |
| NPE coverage ratio | 86.5% | 84.3% | 2.2 |
| Liquidity coverage ratio | 324% | 307% | 17 |
| Common equity tier 1 ratio | 21.5% | 23,4% | -1.9 |
| Total capital ratio | 21.9% | 24,5% | -2.6 |

# Letter from the CEO

Dear All,

Addiko Bank ad Banja Luka ended 2019 successfully, in line with its plans. Simplicity in communication, focus on essentials and efficiency continue to be our drivers that help us to be a bank, focusing on consumer lending in the retail segment and the SME sector lending. We continued to make progress in both these segments at growth rates above market average and moved one step closer to our goal of profiling the bank as the first specialist bank in the country.

In 2019 we have maintained the stability of our business, with key business parameters recording a positive upward trend and doubling our profit compared to the previous year. We grew our lending business by 11.8%, indicating stronger growth than market average while deposits grew by 3.2%. Both demonstrate trust of our customers in our business model.

Our nonperforming exposures were further reduced, while maintaining strong provisions coverage, implying very small credit risk in the bank's books.  We maintained control over our cost, while parallel investing in digital developments and supporting responsibly our growth with the same cost base through various efficiency improvements.

These improved trends in all business aspects, with a strong capital and liquidity base, give us comfort that we will continue successfully on the path to implement our strategy and serve the needs of our customers.

After successful listing of the shares of our Group on the Vienna Stock Exchange in 2019, Addiko shares attracted the investment of many international investors, demonstrating confidence in our strategy and business model and providing us with credible and international recognition that we are on the right path.

As we are continuing our journey, I would like to take the opportunity to express gratitude to our clients and partners for trust and cooperation. And last, but not least, to emphasize the appreciation to all employees of Addiko Bank for their remarkable results and motivation throughout 2019 on behalf of entire Management and Supervisory board.

Mario Ivanković
President of the Management Board of Addiko Bank ad Banja Luka

# The board of Addiko Bank ad Banja Luka

From left to right: Boštjan Pečenko, board member, Žaklina Dimitrijević, board member and Mario Ivanković, CEO.

# Annual Report 2019

## Contents

# Management Report

## 1. Overview of Addiko Bank

Addiko Bank is part of Addiko group which is a consumer and small and medium-sized enterprises (SME) specialist banking group in Central and South Eastern Europe (CSEE). Addiko Bank services as of 31 December 2019 approximately 129 tousands customers, using a well-dispersed network of 31 branches and modern digital banking channels.

Based on its focussed strategy, Addiko Bank repositioned itself as a specialist consumer and SME banking group with a focus on growing its Consumer and SME lending activities as well as payment services (its "focus areas"), offering unsecured personal loan products for consumers and working capital loans for its SME customers funded largely by retail deposits. Addiko Bank's Mortgage lending, Public lending and Large Corporate lending portfolios (its "non-focus areas") have been gradually reduced over time, thereby providing liquidity and capital for the gradual growth in its Consumer and SME lending.

Addiko Bank delivers a modern customer experience in line with its strategy of providing straightforward banking - "focus on essentials, deliver on efficiency and communicate simplicity". Banking products and services have been standardised, especially in the Consumer segment and the SME segment, to improve efficiency, reduce risks and maintain asset quality, and have, particularly in the Large Corporates segment, been further tailored to better meet customer needs.

## 2. General economic environment

Growth momentum remains quite strong by post-crisis standards and has even picked up in Croatia recently. However, the growth rates in excess of 4% recorded in 2018 in three of the countries of operation (Slovenia, Serbia and Montenegro) could not be sustained last year, albeit for varying reasons. Using an unweighted average, the pace of expansion across the five countries of operation slowed down from 4% in 2018 to an estimated 3.1% last year. Growth was strongest in Serbia (3.4%) and Montenegro (3.3%) and weakest in Bosnia and Herzegovina (2.7%), while the economies of Croatia and Slovenia grew by an estimated 3.0% and 2.9%, respectively.

Over the next two years, growth in the five countries of operation (unweighted average) is projected to slow down further – albeit only marginally, to 2.8% in both 2020 and 2021. There are two key reasons for this: (i) the weakening external demand, not least reflecting protectionist risks, and (ii) in some cases domestic capacity constraints, such as skills and labour shortages. Although most Addiko countries of operation continue to have quite high unemployment rates, these have fallen considerably in recent years, reflecting robust economic growth and consequently higher labour demand, as well as in many cases continued outward migration. These trends are highly likely to continue in the next 2-3 years, which will add further positive impetus to wage and private consumption growth. At the same time, in those countries where the labour shortages have been most pronounced, such as Slovenia and Croatia, they started subsiding recently thanks to increased hiring of foreign labour.

Monetary conditions remain very loose, reflecting subdued inflation trends across most of Europe and ultra-loose ECB policy. Supply side factors in particular, such as depressed energy prices, indicate that inflationary pressure will not emerge anytime soon. Across all countries of operation, inflation has picked up somewhat from 2014-16 levels (when many countries experienced a period of deflation) but will remain at historically low levels. The main determining factor for credit growth in the next 2-3 years in Addiko countries will be the stance of the ECB. This makes sense, considering the very strong trade and investment integration between Addiko countries and the bloc and their fixed exchange rate regimes (except in Serbia). Slovenia is in fact part of the euro area, and Montenegro uses the euro as a legal tender. To this end, the signs for credit growth are quite positive. In September 2019, the ECB cut its deposit rate into negative territory (to -0.5%) and restarted its asset purchase programme in the volume of EUR 20 billion per month, while keeping its refinancing rate unchanged at 0%.

All five countries of operation are at a fairly positive point in the credit cycle: lending growth to the non-financial private sector was firmly positive in all countries of operation last year. The strongest growth was observed in Serbia (8.9% year-on-year), followed by Bosnia and Herzegovina (6.7%), Montenegro (6.6%), Slovenia (4.6%) and Croatia (3.2%). In all countries of operation, credit demand from households has been stronger than that from companies, which supported private consumption growth.

In Croatia, real GDP growth accelerated to an estimated 3% last year (from 2.7% in 2018), not least thanks to tourism season surprising on the upside. However, for 2020-2021 wiiw projects a growth deceleration to 2.7% per year on account of the weakening external demand. The Croatian government aims to join the ERM 2 by January 2021 at the latest, paving the way for euro accession two years later. To this end, the country committed itself to implement reforms in six policy areas, three of which are in the banking sector. The assessment of the country's progress in its application to join the ERM 2 (and the European Banking Union) by the ECB and the European Commission is expected in June-July of this year. Credit growth in Croatia has been sustained exclusively thanks to borrowing by households, whereas loans to the corporate sector have been declining slightly (by 1.7% as of November 2019, year-on-year).

In Slovenia, the very high real GDP growth from 2018 (4.1%) could not be repeated last year, but at an estimated 2.9% was still reasonably solid. However, wiiw expects growth to subside further going forward, to 2.6% in 2020 and 2.4% in 2021, mostly on account of the weakening external demand. The recent economic weakness in Germany has already affected Slovenian exports and the country's car production has suffered, but the performance of the important pharmaceuticals industry has remained strong. Following severe consumer loan restrictions imposed by the Central Bank in late 2019, household credit has started decelerating from the high growth rate of around 6% per year recorded last year.

In Serbia, growth slowdown has been not as pronounced as initially expected: real GDP still grew by an estimated 3.4% last year, partly thanks to the construction of the Serbian part of Turk Stream gas pipeline. For 2020 and 2021, the wiiw growth forecast has been revised upwards as well, to 3.4% and 3.2% respectively. This is partly due to the recent favourable international political developments, including improved Serbia-Kosovo relations and the related abolition of Kosovo's 100% import tariff on goods from Serbia and Bosnia and Herzegovina (which had been in place since late 2018). FDI inflows should continue to support investment, while rising wages and generous social policies will underpin private consumption growth. Credit growth picked up strongly in 2018 on the back of higher confidence, and although the current growth rate of around 9% per year may not be sustained, the outlook for the next two years is positive.

In Bosnia and Herzegovina, economic growth slowed down by nearly 1 pp last year (to an estimated 2.7%), mainly because of the disappointing export performance, with the weakness in the euro area increasingly spilling over. Growth is projected to subside further this year, to 2.5%, but should rebound to 2.8% in 2021, with the economy benefitting from remittance inflows and increased tourism exports. After more than a year of political deadlock, the formation of the new government should facilitate economic reforms this year, although the country's prospects of obtaining EU candidate status in the near future remain questionable and would require a major constitutional reform. Credit growth has picked up pace somewhat recently and has approached nearly 8% year-on-year in the case of the household sector.

In Montenegro, growth slowdown has been particularly sharp, from 5.1% in 2018 to an estimated 3.3% last year, mainly on account of the fiscal consolidation in the face of high public (and foreign) debt, with spending cuts falling mostly on public investment projects. Growth is projected to subside further going forward, to 3.0% this year and 2.9% in 2021, reflecting weakening investment activity as well as a slump in private and public consumption. The current government strategy is to ensure a fiscal surplus in 2020-2022, which should help bring down the public debt to 62% of GDP. Given the already high levels of corporate and private debt, the pace of credit expansion may weaken from its current rather high rate in excess of 6% per year.

## 3. Significant events in 2019

### 3.1. Addiko Group goes public

On 12 July 2019, the shares of Addiko Bank AG were admitted to the Official Market of the Vienna Stock Exchange and started trading in the ATX Prime market segment.

Based on the total number of 19,500,000 shares and the offering price of EUR 16.0 per share, reflecting a market capitalization of EUR 312.0 million. This IPO was the third and at that time largest listing in the top segment of the Vienna Stock Exchange this year and was the largest listing in the European financial sector in 2019. On its second trading day, 15 July 2019, Addiko Bank AG was admitted to the ATX (Austrian Traded Index) Prime market.

As announced on 12 August 2019 by Citigroup Global Markets Limited, acting as Stabilization Manager, the Greenshoe Option was exercised in full (975,000 shares) herewith confirming the free float of ca. 55% after the stabilization period of 30 days.

### 3.2. Rating agency Moody's assigns first-time ba2 Baseline Credit Assessment to Addiko Bank AG

On 4 April 2019, Moody's Investors Service assigned for the first-time a ba2 Baseline Credit Assessment (BCA) and Adjusted BCA and a Ba2(cr)/NP(cr) Counterparty Risk Assessments to Addiko Bank AG. Concurrently, the rating agency assigned a Ba3 long-term and NP short-term deposit ratings and counterparty risk ratings to Addiko. The outlook on Addiko's long-term deposit rating is stable.

On 11 October 2019, Moody's assigned a Ba3 long-term local currency rating to Addiko's planned issuance of Subordi-nated Tier 2 Notes and placed the rating on review for upgrade. Concurrently, the rating agency placed on review for upgrade Addiko's long- and short-term Ba3/NP deposits ratings, as well as the bank's long- and short-term Ba2(cr)/NP(cr) Counterparty Risk Assessments (CR Assessments) and Ba3/NP Counterparty Risk Ratings analysis. On 6 December 2019 Moody's confirmed Addiko Bank AG's ratings (outlook stable) concluding the rating review for Addiko opened on 11 October 2019 to reflect Addiko Bank's announcement on 19 November 2019 to postpone a planned issuance of subordinated debt.

## 3.3. Transformation towards out-of-branch sales and digital development

### 3.3.1. Great customer experience with efficient distribution transformation

Addiko Bank is dedicated to delivering the straightforward banking promise and ensuring great customer experience. An important part of this goal is further development and seamless integration of the Bank's digital channels across all customer touchpoints.

Accordingly, Addiko Bank has started a process of transforming its distribution model to keep close to the market's continuously evolving needs.

A target mix of channels was planned and is currently being executed in line with the convenience and simplicity promises that Addiko Bank makes to its customers. The changes are visible on several levels: customers have more options in terms of cash handling by having access to more self-service machines, inside Addiko Bank's branches or in stand-alone locations. The Bank's digital capabilities are being continuously developed with the mission to improve and enrich the user experience on the mobile app and the internet banking platform as well as to offer customers and non-customers end-to-end digital solutions for obtaining a loan.

The Bank is also capitalizing on one of its best capabilities: transforming the classic branch employee role into a more complex one, empowering them to go outside the branch and serve customers at their workplace. Under the Bank@Work label, a team comprised of Addiko Bank's sellers using mobile technology is continuously delivering the convenience promise to thousands of customers every month, throughout the whole Addiko Bank. Customers are receiving advice regarding their financial needs, they can open current accounts, order debit cards, apply for loans or credit cards, obtaining credit approval on the spot.

### 3.3.2. Digital transformation

Addiko Bank's successes over the past years were to a great extent made possible due to digital strategy being an essential part of the business strategy and both driving and supporting the change to reflect the transformation in banking business and customer expectations.

Therefore, Addiko Bank is continuously working on modernizing, improving and digitally transforming its business on all levels-process, procedural, operational, production, service with these reflecting the Bank's dedication to providing the straightforward banking service.

In November, Addiko Bank's Virtual branch was recognized as the "Best Product Innovation" in whole of Europe and received the "Retail Banking Europe Award 2019". The Retail Banking Europe Awards are presented to the most innovative banking institutions and are considered recognition for the best retail banking practices.

Digital transformation by creating new digital capabilities remains one of the strategic focus points of the Bank. Addiko continues to invest in digital solutions as an essential foundation to delivering on the business boosting, convenience and speed-based value proposition. For the Consumer segment the share of consumer loans sold digitally improved to 5.2% in 2019 (2.25% for 2018) and the contribution of Bank@Work to 31% (15% for 2018).

### 3.3.3. Branches

At year end 2019 Addiko Bank operates a total in 31 branches. This physical distribution is optimally sized to deliver the Addiko Bank's Consumer and SME focused strategy, in the context of the increasing customers' preference for digital channels.

## 3.4. Continuous cost management and efficiency gains

With a continued focus on process optimisation and establishing a lean, efficient and integrated organisation, further initiatives have been initiated.

Addiko Bank expects that its operating expenses for 2020 demonstrate a continuation of the 2019 performance.

# 4. Financial development of the Bank

## 4.1. Analysis of the reported result

BAM ths

| | 1.1.-31.12.2019 | 1.1.-31.12.2018 | Change (%) |
|---|---|---|---|
| Net banking income | 37,555 | 37,634 | -0.2% |
| Net interest income | 25,035 | 25,244 | -0.8% |
| Net fee and commission income | 12,520 | 12,390 | 1.0% |
| Net result on financial instruments | 317 | 91 | >100% |
| Other operating result | (2,270) | (880) | >100% |
| **Operating income** | **35,602** | **36,845** | **-3.4%** |
| **Operating expenses** | **(28,355)** | **(28,508)** | **-0.5%** |
| **Operating result before change in credit loss expense** | **7,247** | **8,337** | **-13.1%** |
| Credit loss expenses on financial assets | (543) | (5,059) | -89.3% |
| **Operating result before tax** | **6,704** | **3,278** | **>100%** |
| Tax on income | 16 | 7 | >100% |
| **Result after tax** | **6,720** | **3,285** | **>100%** |

The result after tax of BAM 6,720 thousand, mainly driven by the continued execution of Addiko's focus strategy reflected in a further increased share of the two focus segments Consumer and SME.

**Reported net interest income** decreased in 2019 from BAM 25,244 thousand at YE18, by BAM 209 thousand, or -0.8%, to BAM 25,035 thousand at YE19. This was primarily due to a decrease in interest income in 2019 from BAM 32,295 thousand at YE18, by BAM 542 thousand, to BAM 31,753 thousand, also decrease interest expenses from BAM -7,051 thousand at YE18, by BAM 333 thousand, to BAM -6,718 thousand at YE19, predominantly resulting from lower interest expenses for customer deposit to lower yield current deposits. This development is reflecting an increase of regular interest income within the focus areas Consumer and SME lending which over-compensated the decrease within the non-focus areas i.e. Mortgage and Public Finance. Moreover, interest income from NPEs reduced by BAM 316 thousand compared to YE18 given the successful reduction of NPEs during 2019. The **net interest margin** amounts to 310bp at YE19, compared to 340bp YE18. mainly due to decreased average interest rate for living loans of customers from 5.72% at YE18, by 0.23% to 5.49% at YE19.

**Reported net fee and commission income** increased from BAM 12,390 thousand in 2018, by BAM 130 thousand, or 1%, to BAM 12,520 thousand in 2019. This was primarily due to the increase of fee and commission income from BAM 15,225 thousand at YE18, by BAM 548 thousand, to BAM 15,773 thousand at YE19, which was mainly driven by stronger income from Securities&brokerage, FX and, dynamic currency conversion as well as roll out of further functionalities for guarantee and trade finance products in the SME segment.

**Reported net result on financial instruments** amounts to BAM 317 thousand, mainly driven by the sale of debt instruments.

On a reported basis, the **other operating result** as sum of other operating income and other operating expense changed in 2019 from BAM -880 thousand at YE18, by BAM 1,390 thousand, to BAM -2,270 thousand at YE19. The development was driven by the following significant items:

- net increase in BAM -812 thousand provision expenses mainly driven by the development in relation to legal matters
- the deposit guarantee costs in the amount of BAM -160 thousand

**Reported operating expenses** decreased from BAM -28,508 thousand in 2018, by BAM 153 thousand, or -0.5% to BAM -28,355 thousand at the current reporting date:

- **Personnel expenses** reduced compared to the previous period from BAM -12,639 thousand at YE18 to BAM -12,172 thousand at YE19. The number of employees expressed in full-time equivalent ('FTE') at 31 December 2019 was 334, which constitutes, as a result of efficiency and right sizing programs, a decrease of 7,5 FTEs from 31 December 2018
- **Other administrative expenses** decreased from BAM -13,347 thousand at YE18, by BAM 777 thousand, or 5.8% to BAM -12,570 thousand at YE19. This development was mainly driven by the implementation of the new leasing standard (IFRS 16, starting from 1.1.2019) and the related decrease in rental expenses. An increase in the administrative expenses can be seen in IT expenses, which is primarily reflecting

investments to grow the business and enhance the digital capabilities of the Bank.

- Depreciation and amortisation increased from BAM -2,522 thousand at YE18, by BAM -1,091 thousand, to BAM -3,613 thousand at YE19. This development was predominantely driven by depreciation in the amount of BAM -525 thousand for the right of use assets recognised in the course of the first-time implementation of the new leasing standard IFRS 16 and the corresponding decrease in rental expenses.

**The reported credit loss expenses** on financial assets amount to EUR -543 thousand (YE18: EUR -5,059 thousand).

The allocation of provisions is mainly caused by unsecured portfolio due to higher NPE inflows as well as migration of clients from STAGE 1 to STAGE 2 (caused by PD shift). Releases within the other portfolios was caused by repayments and re-migrations to a lower risk portfolio in the non-focus segment Mortgage and Corporate. In 2018, higher amount of reported credit loss compared to 2019 occurred mainly due to unsecured PI segment for followig reasons: a) recalibration of the historical internal models to more recent data trends b) implementation of stricter definition for NPL, both of which did not change significantly during 2019 afer its initial effects in 2018.

## 4.2. Analysis of the statement of financial position

BAM ths

| | 31.12.2019 | 31.12.2018 | Change (%) |
|---|---|---|---|
| Cash reserves | 169,528 | 188,393 | -10.0% |
| Financial assets held for trading | 1 | - | |
| Loans and receivables | 567,432 | 509,678 | 11.3% |
| Loans and advances to credit institutions | - | - | - |
| Loans and advances to customers | 567,432 | 509,678 | 11.3% |
| Investment securities | 62,176 | 55,128 | 12.8% |
| Tangible assets | 28,174 | 29,080 | -3.1% |
| Intangible assets | 6,561 | 5,874 | 11.7% |
| Tax assets | 1,424 | 1,395 | 2.1% |
| Current tax assets | 1,424 | 1,395 | 2.1% |
| Deferred tax assets | - | - | - |
| Other assets | 6,289 | 5,570 | 12.9% |
| Non-current assets and disposal groups classified as held for sale | 592 | 545 | 8.6% |
| **Total assets** | **842,177** | **795,663** | **5.8%** |

The statement of financial position of Addiko Bank shows the simple and solid interest-bearing asset structure: more than 54.9% of the assets are represented by customer loans, most of which belong to the focus area. In addition, a substantial part of the residual assets is represented by cash reserves and high rated bonds. With regard to the statement of financial positions, Addiko's strategy continued to change the business composition from lower margin Mortgage lending and Public Finance towards higher value-added Consumer and SME lending. This is shown by the increased share of these two segments of 75.9% of the gross performing loan book (YE18: 69%). The performance in new disbursements, which outperformed the market growth, in these focus segments over the last 12 months clearly highlights that Addiko is delivering on its business strategy, with an increase in the volumes of gross performing loans of +13.8% in Consumer lending and +42.6% in the SME loan books.

As of YE19 the total assets of Addiko Bank in the amount of BAM 842,177 thousand rise above the level as of YE18 of BAM 795,663 thousand, corresponding to a increase of BAM 46,514 thousand or 5.8%. The total risk, i.e. risk-weighted assets including credit, market and operational risk, (Banking Agency of Republic of Srpska) increased to BAM 683,958 thousand (YE18: BAM 591,536 thousand) reflecting the increases of volumes in the focus segments.

**Cash reserve** decreased by BAM 18,865 thousand to BAM 169,528 thousand as of 31 December 2019 (YE18: BAM 188,393 thousand). This was primarily driven by an increase in lending activity.

Overall **loans and receivables** increased to BAM 567,432 thousand from BAM 509,678 thousand at year end 2018:

Loans and receivables to customers (net) increased by BAM 57,754 thousand to BAM 567,432 thousand (YE18: BAM 509,678 thousand). In line with the Bank's strategy, within the loans and receivables to customers, the business composition continued to change during the reporting period, with an increased share of higher value adding Consumer and SME lending, which was partly offset by the decrease in the Mortgage Business.

The **investment securities** increased from BAM 55,128 thousand to BAM 62,176 thousand in YE19. They are largely invested in high rated government or bank bonds and have a maturity of less than five years. To ensure high levels of liquidity and transparency in securities portfolios, all investments are “plain vanilla” without any embedded options or other structured features.

**Tangible assets** decreased to BAM 28,174 thousand compared to BAM 29,080 thousand at YE18, mainly as result of external assesment of bank's property. This decrease is partially compensated with the first-time implementation of IFRS 16, leading to the recognition of a right of use asset in the amount of BAM 1,239 at the 1. January 2019

**Tax assets** slightly increased to BAM 1,424 thousand (YE18: BAM 1,395 thousand).

**Other assets** increased to BAM 6,289 thousand (YE18: BAM 5,570 thousand), mainly due to increase of receivables from insurance companies for damages (BAM 317 thousand) and increase of advance payments in relation to IT projects aimed to increase operational efficiency.

BAM ths

| | 31.12.2019 | 31.12.2018 | Change (%) |
|---|---|---|---|
| Financial liabilities held for trading | 3 | - | - |
| Financial liabilities measured at amortised cost | 672,644 | 632,787 | 6.3% |
| Deposits of credit and financial institutions | 47,992 | 31,350 | 53.1% |
| Deposits of customers | 557,561 | 540,245 | 3.2% |
| Borrowings liabilities | 56,196 | 52,512 | 7.0% |
| Other financial liabilities | 10,895 | 8,680 | 25.5% |
| Provisions | 3,841 | 3,849 | -0.2% |
| Tax liabilities | 440 | 582 | -24.4% |
| Current tax liabilities | - | - | - |
| Deferred tax liabilities | 440 | 582 | -24.4% |
| Other liabilities | 4,048 | 3,984 | 1.6% |
| Equity | 161.201 | 154.461 | 4.4% |
| **Total equity and liabilities** | **824,177** | **795,663** | **5.8%** |

On the liabilities' side, **financial liabilities measured at amortised cost** increased to BAM 672,644 thousand compared to BAM 632,787 thousand at year end 2018:

- Deposits of credit and financial institutions increased from BAM 31,350 thousand to BAM 47,992 thousand as of YE19.
- Deposits of customers increased to BAM 557,561 thousand (YE18: BAM 540,245 thousand).
- Borrowings liabilities increased from BAM 52,512 thousand at YE18 to BAM 56,196 thousand at YE19.
- Other financial liabilities increased from BAM 8,680 thousand at YE18 to BAM 10,895 thousand at YE19, which can be traced back to the first-time implementation of IFRS 16 regulations.

**Provisions** slightly decreased by BAM 8 thousand in 2019. This was primarily influenced by release of provision and off-court settlement for legal matters on CHF loans.

**Tax liabilities** slightly decreased to BAM 440 thousand (YE18: BAM 582 thousand)

**Other liabilities** slightly increased from BAM 3,984 thousand to BAM 4,048 thousand and include accruals for services received but not yet invoiced as well as liabilities for salaries and salary compensations not yet paid.

The development of equity from BAM 154.461 thousand to BAM 161.201 thousand is reflecting the net impact in the amount of BAM 6,740 thousand for the year 2018 and the 2019 total comprehensive income, which includes the profit for the reporting period in the amount of BAM 6,720 thousand as well as changes in other comprehensive income in the amount of BAM 20 thousand.

The capital base of Addiko Bank is solely made up of CET1 and stands at 26.1% (YE18: 27.3%), well above the Overall Capital Requirements of 14.5% based on currently valid Banking Agency decision.

The return on tangible equity with 4.4% for 2019 compared to 2.2% for YE18 is reflecting the stable Bank's performance.

# 5. Internal Control System for accounting procedures

Addiko Bank has an internal control system (ICS) for accounting procedures, in which suitable structures and processes are defined and implemented throughout the organisation.

The aim of the internal control system of Addiko Bank is to ensure effective and efficient operations, adequate identification, measurement and mitigation of risks, prudent conduct of business, reliability of financial and non-financial information reported, both internally and externally, and compliance with laws, regulations, supervisory requirements and the institution's internal rules and decisions.

The Internal Control System (ICS) consists of a set of rules, procedures and organisational structures which aim to:

- ensure that corporate strategy is implemented,
- achieve effective and efficient corporate processes,
- safeguard the value of corporate assets,
- ensure the reliability and integrity of accounting and management data,
- ensure that operations comply with all relevant rules and regulations.

The particular objectives with regard to Addiko Group accounting procedures are that the ICS ensures that all business transactions are recorded immediately, correctly and in a uniform way for accounting purposes. The implementation of the internal control system in relation to the financial reporting process is also set out in the internal rules and regulations.

The internal control system of Addiko Group is built on a process-oriented approach. Addiko Group deploys control activities through process documentation which incorporates the tracking and documentation of each process, including the information about process flow according to the internally set up guidelines for process management.

The overall effectiveness of the internal controls is monitored on an ongoing basis. Monitoring of key risks is part of daily activities of Addiko Group as well as periodic evaluations by the business lines, internal control functions, risk management, compliance and internal audit.

Regular internal control system monitoring and promptly reporting on internal control deficiency and escalation to relevant stakeholders (e.g. committees) is established. Internal control deficiencies, whether identified by business line, internal audit, or other control functions are reported in a timely manner to the appropriate management level for further decision and addressed promptly.

Internal Audit performs independent and regular reviews of compliance with legal provisions and internal rules.

The internal control system itself is not a static system but is continuously adapted to the changing environment. The implementation of the internal control system is fundamentally based on the integrity and ethical behavior of the employees. The Management Board and the leadership team actively and consciously embrace their role of leading by example by promoting high ethical and integrity standards and establishing a risk and control culture within the organisation that emphasizes and demonstrates to all levels of personnel the importance of internal controls.

# 6. Research & Development

Addiko Bank does not conduct any research and development activities.

# 7. Mid-Term Targets and Outlook

## 7.1. Mid-Term Targets

Addiko Group was able in 2019 to successfully continue its progress towards achieving mid-term target levels and we are convinced that the continuous focus on Consumer and SME lending activities as well as payment services ("focus areas") in the CSEE region and a rigorous commitment to digital transformation, will enable a continuation of the established track record and a visible result of this strategy.

While the banking industry continued to experience a challenging low interest rate environment and continued pricing pressure in the financial year 2019, Addiko Group managed to further improve the adjusted net interest margin, towards its mid-term target to reach a NIM of approximately 4%. The continuous shift of the loan book from the "non-focus" to the "focus areas" in line with the mid-term target of 80% (75.9% as of YE19), complemented by a further optimization of the funding position towards the mid-term targeted LDR of ~100% (101.2% as of YE19) will support Addiko Group's efforts for further improvement in the upcoming years.

Addiko Bank further expects its operating expenses for 2020 to continue the developments in 2019, largely as a result of additional cost reduction initiatives which have been implemented during the second half of 2019. The related impact resulting from predominantly back office optimisation, branch opimization and a further shift to digital channels, in combination with the positive impact of our focus strategy on net banking income are expected to allow for further significant improvement of the cost-income ratio and to achieve in the medium term a cost-income ratio of below 50% (77.4% as of YE19).

Amid a stable low interest rate environment, cost of risk is expected to increase slightly along with the loan book shifting toward the focus areas unsecured consumer and SME lending. While precise forecasts are difficult in the current environment, Addiko Bank projects a cost of risk (net loans) in its mid-term target of approximately 1.6%.

### 7.2. Outlook 2019

The global measures to counter contagion of the coronavirus (COVID-19) have resulted in subdued social and economic activity in various regions across the world that will have adverse effects on global economic growth. In addition, uncertainty on the further development of the situation has resulted in a significant deterioration in market confidence. The degree of the impact on the global economy and financial markets is yet to be seen. Central banks including the ECB, the United States Federal Reserve and the Bank of England have implemented further expansionary monetary policy such as interest rate cuts, asset purchases and generous liquidity facilities for commercial banks. Additionally, governments are expected to implement stimulus measures and support the hardest hit sectors of the economy.

At the same time, developments in the European banking sector are expected to continue. On the one hand, the sector is facing challenges in the form of a low interest rate environment, general price pressure due to excess liquidity in the markets, and steadily increasing regulatory requirements, which are having a negative impact on the profitability of banks. Furthermore, these activities of regulatory authorities, such as the implementation of consumer protection mechanisms limiting loan growth in the consumer sector, will in turn also have a negative influence on private consumption, further affecting the profitability. On the other hand, the pressure on market participants to innovate is increasing, and with it the need to make comprehensive investments.

In view of these challenges, but also these opportunities, the Addiko Group has continued to push ahead with its digital transformation and was thus able to take further significant steps towards achieving its medium-term goals. The locally operating banks have successfully positioned themselves as innovative and targeted specialist lenders in the areas of unsecured consumer loans and loans for small and medium-sized enterprises. This will enable them to continue to expand their growth and margins profitably in the coming year, while maintaining a balanced risk/return profile and a balance sheet financed primarily by deposits with a good equity base.

On the back of this Addiko remains with the expectation of a moderately slower growth outlook on the back of very loose monetary condition, increased complexity of regulations and overall geopolitical uncertainties. The main risk factors influencing the banking industry include worsened interest rate outlooks, political or regulatory measures against banks as well as geopolitical and global economic uncertainties. Addiko Group will continue to execute its focused strategy as a consumer and SME specialist lender in the CSEE region, and further drive digital transformation along the value proposition convenience and speed. Rigorously managed risk-return profile and self-funding principle in each entity will remain strong anchors in the strategy. Cost of risk is expected to increase slightly along with the loan book shifting toward the focus areas unsecured consumer and SME lending.

# ADDIKO BANK A.D. BANJA LUKA

## Financial Statements Year Ended December 31, 2019 and Independent Auditors' Report

Deloitte d.o.o. Banja Luka
Braće Mažar i majke Marije 58 i 60
78000 Banja Luka
Republic of Srpska
Bosnia and Herzegovina

Tel: +387 (0)51 223 500
Fax: +387 (0)51 224 990
www.deloitte.com

# Independent Auditors' Report

**To the Supervisory Board and Shareholders of Addiko banka a.d. Banja Luka**

***Opinion***

We have audited the financial statements of Addiko banka a.d. Banja Luka (hereinafter: the "Bank"), which comprise the statement of financial position as at December 31, 2019, and the related statement of profit or loss, statement of other comprehensive income, statement of changes in equity and reserves 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, in all material respects, give a true and fair view of the financial position of Addiko banka a.d. Banja Luka as at December 31, 2019, and of its financial performance and its cash flows for the year then ended, in accordance with the accounting regulations of the Republic of Srpska and regulations of the Banking Agency of the Republic of Srpska, governing the financial reporting of banks.

***Basis for Opinion***

We conducted our audit in accordance with the International Standards on Auditing (ISA) and the Law on Accounting and Auditing of the Republic of Srpska. 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 Co*de) together with the ethical requirements that are relevant to our audit of the financial statements in the Republic of Srpska, and we have fulfilled our other ethical responsibilities in accordance with these requirements and IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

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 most significant in our audit of the financial statements for 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.

(Continued)

*Key Audit Matters (Continued)*

<table>
<tr><th>Key audit matter</th><th>Responsive audit procedure</th></tr>
<tr><td colspan="2">Expected credit losses per loans and provisions for guarantees</td></tr>
<tr><td>As of December 31, 2019, the Bank's loans and receivables due from customers totaled BAM 652,273 thousand (December 31, 2018: BAM 597,566 thousand), whereas the total impairment allowance amounted to BAM 86,216 thousand as of December 31, 2018 (December 31, 2018: BAM 89,106 thousand).<br><br>Measurement of the impairment losses for loans and provisions per guarantees is deemed a key audit matter because definition of assumptions used in expected credit loss calculation is subjective due to the extent of judgment used by the Bank's management.<br><br>The most significant judgements refer to:<br>• Assumptions used within the expected credit loss models applied in estimates of credit risk of the customer exposure and expected future cash flows;<br>• Timely identification of exposures with a significant increase in credit risk; and<br>• Collateral valuation and assumptions of the future cash flows per individually assessed credit exposures.<br><br>The Bank's management disclosed additional information on the impairment losses on loans and provisions for guarantees in Notes 2, 3, 6.1, 14, 18 and 28 to the financial statements.</td><td>Based on our risk assessment and knowledge of the industry, we examined the losses on impairment of loans and provisions for guarantees, and evaluated the methodology applied by the Bank, and the assumptions used in accordance with the key audit matter description.<br><br>Our testing encompassed the following elements:<br>• Evaluation of the key controls over the assumptions used in the expected credit loss models for assessing the credit risk of the customer exposure and expected future cash flows;<br>• Obtaining and detailed testing of the evidence supporting the assumptions used in the expected credit loss models for staging, assumptions used to calculate 12-month and life-cycle probability of default (PD) parameters and methods applied in arriving at the loss given default (LGD) parameter;<br>• Obtaining and detailed testing of the evidence supporting appropriate definition of assumptions on impairment losses on loans and provisions per guarantees, including collateral valuation and assumptions of the future cash flows per individually assessed credit exposures;<br>• Estimates of the key trends in the Bank's previous year's high-risk portfolio against the industry standards and historical data;<br>• Evaluation of the methodologies applied by the Bank using our knowledge of and experience with the industry;<br>• We involved our IT experts and credit risk specialists in the work in areas that required specific expertise;<br>• Evaluation of the accuracy and completeness of the disclosures made in the financial statements.</td></tr>
</table>

***Responsibilities of Management and the Supervisory Board for the Financial Statements***

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the accounting regulations of the Republic of Srpska and regulations of the Banking Agency of the Republic of Srpska, governing the financial reporting of banks, 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.

The Supervisory Board is responsible for overseeing the Bank’s financial reporting process.

(Continued)

***Auditors' Responsibility 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 auditors' 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 the International Standards on Auditing 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 the International Standards on Auditing, 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.
- 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 those in charge of governance 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 those in charge of governance with a statement that we have complied with relevant ethical requirements regarding independence, and that we will communicate to them all relationships and other matters that may reasonably be thought to bear on our independence, and, where applicable, the related safeguards.

From the matters communicated to those in charge of governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore key audit matters. We describe those matters in our auditors' report unless an applicable law or a 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 adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The Engagement Partner on the audit resulting in this independent auditors' report is Mr. Mirko Ilić, Certified Auditor.

Banja Luka, March 23, 2020

DELOITTE D.O.O. 1 BANJA LUKA

Mirko Ilić
Certified Auditor

## Statement of Profit or Loss
**Year Ended December 31**
**(Thousands of BAM)**

| | Note | 2019 | 2018 |
|---|---|---|---|
| *Statement of profit or loss* | | | |
| Interest income calculated using the effective interest method | 7.1 | 31,743 | 32,285 |
| Other interest income | 7.1 | 10 | 10 |
| Interest expenses | 7.2 | (6,718) | (7,051) |
| **Net interest income** | 7 | **25,035** | **25,244** |
| Fee and commission income | 8.1 | 15,773 | 15,225 |
| Fee and commission expenses | 8.2 | (3,253) | (2,835) |
| **Net fee and commission income** | 8 | **12,520** | **12,390** |
| Net profit from financial instruments | 9 | 317 | 91 |
| Other operating income | 10 | 2,367 | 2,819 |
| Other operating expenses | 11 | (4,637) | (3,699) |
| **Total operating income** | | **35,602** | **36,845** |
| Personnel expense | 12 | (12,172) | (12,639) |
| Depreciation/amortization charge | 20, 21 | (3,613) | (2,522) |
| Other administrative costs | 13 | (12,570) | (13,347) |
| **Total operating expenses** | | **(28,355)** | **(28,508)** |
| **OPERATING PROFIT BEFORE CREDIT RISK PROVISIONS** | | **7,247** | **8,337** |
| Credit loss expense on financial assets | 14 | (543) | (5,059) |
| **PROFIT BEFORE TAXES** | | **6,704** | **3,278** |
| Tax on income | 15 | **16** | **7** |
| **NET PROFIT FOR THE YEAR** | | **6,720** | **3,285** |
| Earnings per share (in BAM) | 27 | 0,044 | 0,021 |

## Statement of Other Comprehensive Income
**Year Ended December 31**
**(Thousands of BAM)**

| | 2019 | 2018 |
|---|---|---|
| **NET PROFIT FOR THE YEAR** | **6,720** | **3,285** |
| **Other comprehensive income** | | |
| ***Items that may subsequently be reclassified to the profit or loss:*** | | |
| Net gains on the fair value adjustment of financial assets at fair value through other comprehensive income (FVtOCI) | 1,145 | 102 |
| ***Items that cannot subsequently be reclassified to the profit or loss:*** | | |
| Losses on revaluation of property and equipment | (1,253) | - |
| Gains on changes in actuarial assumptions | 2 | 3 |
| Income tax on items of other comprehensive income that cannot be reclassified to profit or loss | 126 | - |
| **Other comprehensive income, net** | **20** | **105** |
| **TOTAL POSITIVE COMPREHENSIVE INCOME** | **6,740** | **3,390** |

These financial statements were approved for issuance by Management of Addiko Bank a.d., Banja Luka on March 18, 2020.

Signed on behalf of the Bank by:

ADDIKO BANK AD BANJA LUKA

Mario Ivanković
Chairman of the Management Board

Žaklina Dimitrijević
Member of the Management Board

# Statement of Financial Position
As of December 31
(Thousands of BAM)

| | Note | 2019 | 2018 |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and balances held with the Central bank | 16 | 126,008 | 129,946 |
| Balances held with other banks | 17 | 43,520 | 58,447 |
| Financial assets held for trading | 19.2 | 1 | - |
| Loans and receivables | 18 | 567,432 | 509,678 |
| Loans and receivables due from customers | 18.1 | 564,206 | 506,896 |
| Other financial assets | 18.2 | 3,226 | 2,782 |
| Investments in securities | 19.1 | 62,176 | 55,128 |
| Property and equipment | 20 | 28,174 | 29,080 |
| Land, buildings and equipment | 20.1 | 25,673 | 26,679 |
| Investment property | 20.2 | 2,501 | 2,401 |
| Intangible assets | 21 | 6,561 | 5,874 |
| Tax assets | | 1,424 | 1,395 |
| Receivables for prepaid income taxes | | 1,424 | 1,395 |
| Assets held for sale | 22 | 592 | 545 |
| Other assets | 23 | 6,289 | 5,570 |
| **Total assets** | | **842,177** | **795,663** |
| **LIABILITIES** | | | |
| Financial liabilities held for trading | 19.2 | 3 | - |
| Financial liabilities at amortized cost | 24 | 672,644 | 632,787 |
| Deposits due to banks and financial institutions | 24.1 | 47,992 | 31,350 |
| Deposits due to customers | 24.2 | 557,561 | 540,245 |
| Borrowings | 24.3 | 56,196 | 52,512 |
| Other financial liabilities | 24.4 | 10,895 | 8,680 |
| Other provisions | 28 | 3,841 | 3,849 |
| Tax liabilities | | 440 | 582 |
| Deferred tax liabilities | 15c) | 440 | 582 |
| Other liabilities | 25 | 4,048 | 3,984 |
| **Total liabilities** | | **680,976** | **641,202** |
| **EQUITY** | | | |
| Issued (share) capital | 26 | 153,094 | 153,094 |
| Regulatory reserves for credit losses | 26 | - | 4,532 |
| Other reserves from profit | 26 | 61,351 | 56,819 |
| Revaluation and fair value reserves | | 2,102 | 2,235 |
| Accumulated losses | | (55,346) | (62,219) |
| **Total equity** | | **161,201** | **154,461** |
| **Total liabilities and equity** | | **842,177** | **795,663** |
| **Contingent liabilities and commitments** | 29 | **119,473** | **114,429** |

# Statement of Changes in Equity and Reserves
**Year Ended December 31**
**(Thousands of BAM)**

| | Share capital | Regulatory reserves for credit losses | Other reserves from profit | Revaluation reserves | Accumulated losses | Total |
|---|---|---|---|---|---|---|
| **Balance as at 31 December 2017** | **153,094** | **61,826** | **-** | **2,189** | **(65,563)** | **151,546** |
| Transfers within reserves (Note 27) | - | (56,819) | 56,819 | - | - | **-** |
| IFRS 9 first-time adoption effect | - | (475) | - | - | - | **(475)** |
| Net profit for 2018 | - | - | - | - | 3,285 | **3,285** |
| **Other comprehensive income** | | | | | | |
| *Items that may be reclassified to the income statement:* | | | | | | |
| Gains on the fair value adjustment of securities at FVtOCI | - | - | - | 102 | - | **102** |
| Net effect of changes in the deferred taxes | - | - | - | - | - | **-** |
| *Items that cannot be reclassified to the profit or loss* | | | | | | |
| Revaluation of property and investment property | - | - | - | (66) | 66 | **-** |
| Gains on changes in actuarial assumptions | - | - | - | 3 | - | **3** |
| Net effect of changes in the deferred taxes | - | - | - | 7 | (7) | **-** |
| **Total other comprehensive income** | **-** | **-** | **-** | **46** | **59** | **105** |
| **Total comprehensive income** | **-** | **-** | **-** | **46** | **3,344** | **3,390** |
| **Balance as at 31 December 2018** | **153,094** | **4,532** | **56,819** | **2,235** | **(62,219)** | **154,461** |

| | Share capital | Regulatory reserves for credit losses | Other reserves from profit | Revaluation reserves | Accumulated losses | Total |
|---|---|---|---|---|---|---|
| **Balance as at 31 December 2018** | **153,094** | **4,532** | **56,819** | **2,235** | **(62,219)** | **154,461** |
| Transfers within reserves | - | (4,532) | 4,532 | - | - | **-** |
| Net profit for 2019 | - | - | - | - | 6,720 | **6,720** |
| **Other comprehensive income** | | | | | | |
| *Items that may be reclassified to the income statement:* | | | | | | |
| Gains on the fair value adjustment of securities at FVtOCI | - | - | - | 1,145 | - | **1,145** |
| Net effect of changes in the deferred taxes | - | - | - | - | - | **-** |
| *Items that cannot be reclassified to the profit or loss* | | | | | | |
| Revaluation of property and investment property | - | - | - | (1,422) | 169 | **(1,253)** |
| Gains on changes in actuarial assumptions | - | - | - | 2 | - | **2** |
| Net effect of changes in the deferred taxes | - | - | - | 142 | (16) | **126** |
| **Total other comprehensive income** | **-** | **-** | **-** | **(133)** | **153** | **20** |
| **Total comprehensive income** | **-** | **-** | **-** | **(133)** | **6,873** | **6,740** |
| **Balance as at 31 December 2019** | **153,094** | **-** | **61,351** | **2,102** | **(55,346)** | **161,201** |

## Statement of Cash Flows
### Year Ended December 31
### (Thousands of BAM)

| | Note | 2019 | 2018 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Interest, fees and commissions received | | 45,481 | 47,665 |
| Interest paid | | (8,712) | (9,317) |
| Collection of loans previously written off | | 497 | 163 |
| Cash paid to employees and suppliers | | (28,141) | (28,939) |
| Off-balance sheet contractual payments | | | |
| Receipts and payments on extraordinary items | | 402 | 508 |
| Disbursement of loans extended to customers | | (58,634) | 7,439 |
| Customer deposits | | 34,525 | 62,876 |
| Income taxes paid | | (28) | (183) |
| **Net cash/(used in)/generated by operating activities** | | (14,610) | **80,212** |
| | | | |
| **Cash flows from investing activities** | | | |
| Interest received | | 1,990 | 122 |
| Dividend received | | 10 | 10 |
| Investments in securities at fair value through other comprehensive income | | (6,892) | (52,862) |
| Purchases of intangible assets | | (2,672) | (3,060) |
| Purchases of tangible assets | | (310) | (197) |
| **Net cash (used in) investing activities** | | (7,874) | **(55,987)** |
| | | | |
| **Cash flows from financing activities** | | | |
| Interest paid on borrowings | | (921) | (1,076) |
| Increase in borrowings | | 11,567 | 30,426 |
| Repayment of borrowings | | (7,906) | (6,300) |
| **Net cash generated by financing activities** | | **2,740** | **23,050** |
| | | | |
| **Net (decrease)/increase in cash and cash equivalents** | | **(19,744)** | **47,275** |
| | | | |
| **Cash and cash equivalents at the beginning of year** | | **189,246** | **141,287** |
| Foreign exchange gains | | 160 | 684 |
| **Cash and cash equivalents at the end of year** | | **169,662** | **189,246** |
| | | | |
| **Cash and cash equivalents comprise the following statement of financial position items:** | | | |
| Cash and balances with the Central Bank | 16 | 126,008 | 129,946 |
| Balances held with other banks | 17 | 43,520 | 58,447 |
| Interest accrued and provisions | | 134 | 853 |
| | | **169,662** | **189,246** |

# Notes to the Financial Statements
**December 31, 2019**
**(Thousands of BAM)**

## 1. GENERAL INFORMATION

Addiko Bank a.d. Banja Luka (the "Bank") is a legal successor of Kristal Banka a.d., Banja Luka which was initially registered as a separate legal entity as at September 30, 1992, and subsequently transformed into a shareholders' company as at May 16, 1997. Prior to its establishment as an independent bank, the Bank operated as a main branch of Jugobanka Jubanka d.d., Sarajevo, a related party of Jugobanka d.d., Beograd.

Under Decision of the district Commercial court of Banja Luka (no. 057-0-Reg-16-002147) dated October 28, 2016, the Bank changed its name to the current legal name. The Bank's owner is Addiko Bank AG, a member of Addiko Group, holding a 99.86% equity interest therein. More details on ownership structure of the Bank are provided in Note 26.

The Bank is licensed in the Republic of Srpska to perform banking operations related to payment transfers, credit and deposit activities in the country and abroad, and in accordance with the Republic of Srpska banking legislation, it is obligated to operate based on the principles of liquidity, solvency and profitability.

The Bank's registered Head Office is located at no. 13, Aleja Svetog Save St., Banja Luka, Republic of Srpska. As of December 31, 2019, besides the Head Office located in Banja Luka, the Bank had 31 branch offices situated throughout Bosnia and Herzegovina (BH) (December 31, 2018: the Head Office located in Banja Luka and 33 branch offices).

Up to September 7, 2017 the Bank was the sole owner of Hypo Alpe Adria Leasing d.o.o. Banja Luka, when the liquidation procedure was instigated over Hypo Alpe-Adria-Leasing d.o.o. Banja Luka, which comprised the Group along with the Bank. On February 7, 2019, Decision on Closure of the Liquidation Procedure over Hypo Alpe Adria Leasing d.o.o. Banja Luka became effective.

As of December 31, 2019, the Bank had 362 employees (December 31, 2018: 372 employees).

| | |
|---|---|
| **Management of the Bank** | |
| Chairman, Executive Director | Mario Ivanković |
| Member | Boštjan Pečenko |
| Member | Žaklina Dimitrijević |
| | |
| **Supervisory Board** | |
| Chairman | Hans-Hermann Anton Lotter |
| Deputy | Biljana Rabitsch |
| Member | Razvan Munteanu |
| Member | Meliha Povlakić |
| Member | Damir Karamehmedović |
| | |
| **Audit Committee** | |
| President | Đorđe Lazović |
| Member | Siniša Radonjić |
| Member | Jelena Mažuranić |

## 2. BASIS FOR PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS AND ACCOUNTING METHOD

### 2.1. Statement of Compliance

The accompanying financial statements comprise annual stand-alone financial statements of Addiko Bank a.d. Banja Luka (the “Bank”) for 2019.

These financial statements have been prepared in accordance with the International Financial Reporting Standards (“IFRS”) in keeping with the Law on Accounting and Auditing or the Republic of Srpska and regulations of the Banking Agency of the Republic of Srpska governing the financial reporting of banks and finance lessors.

### 2.2. Basis of Measurement and Preparation of the Financial Statements

The accompanying financial statements of the Bank have been prepared on the historical cost basis unless otherwise stated in the summary of accounting policies hereunder.

Historical cost is generally based on the fair value of consideration paid in exchange for goods and services

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between the market participants at the measurement date under current market conditions regardless of whether that price is directly observable or estimated using another valuation technique. Upon estimating the fair value of assets or liabilities, the Bank takes into account characteristics of assets or liabilities that other market participants would also consider upon determining the price of assets or liabilities at the measurement date.

In preparing the statement of cash flows for the year ended December 31, 2019, the Bank used direct cash flow reporting method.

### 2.3. Functional and Presentation Currency

Amounts in the accompanying financial statements are stated in thousands of convertible marks (“BAM”), BAM being the functional and official presentation currency in the Republic of Srpska and Bosnia and Herzegovina.

The Central Bank of Bosnia and Herzegovina (the “Central Bank”) implements the policy on FX rate in line with the principle of the Currency Board, according to which BAM is fix pegged to EUR at the rate of BAM 1 = EUR 0.51129, which was used for 2019 and 2018.

### 2.4. Application and Impact of the New and Revised International Financial Reporting Standards (“IFRS”) and International Accounting Standards (“IAS”)

The accompanying financial statements have been prepared in accordance with the International Accounting (“IAS”) and International Financial Reporting Standards (“IFRS”), effective since January 1, 2014 and accounting regulations of the Republic of Srpska based on those standards as well as regulations of the Banking Agency of the Republic of Srpska governing financial reporting of banks and finance lessors.

Namely, in accordance with the provisions of the newly adopted Law on Accounting and Auditing of the Republic of Srpska (Official Gazette of RS no. 94/15), all legal entities situated on the territory of the Republic of Srpska are under an obligation to fully apply IAS, IFRS and the International Financial Reporting Standard for Small and Medium-Sized Entities ("IFRS for SMEs"), International Public Sector Accounting Standards ("IPSAS"), International Valuation Standards ("IVS"), International Standards for the Professional Practice of Internal Auditing, Conceptual Framework for Financial Reporting, Code of Ethics for Professional Accountants and the pronouncements, interpretations and guidelines of the International Accounting Standards Board (“IASB”) and all pronouncements, interpretations and guidelines of the International Federation of Accountants (“IFAC”).

In addition, in accordance with the previously effective Law on Accounting and Auditing of the Republic of Srpska, on October 4, 2017, the Management Board of AAARS enacted “Decision on Determining and Issuing the Conceptual Framework for Financial Reporting and Basic Texts of the International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS)“.

Under the aforesaid Decision, translations of the Standards and interpretations issued by the International Accounting Standards Board (“IASB”) up to December 31, 2014 are defined and published on AAARS website, which shall be effective in the Republic of Srpska and applicable to the financial statements prepared as of December 31, 2018.

## 2. BASIS FOR PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS AND ACCOUNTING METHOD (Continued)

### 2.4. Application and Impact of the New and Revised International Financial Reporting Standards ("IFRS") and International Accounting Standards ("IAS") (Continued)

In addition, the Banking Agency of the Republic of Srpska ("BARS"), as the regulator of the banking market in the Republic of Srpska, in its memo to the Association of Banks of Bosnia and Herzegovina no. 05-500-1572-3/17 dated October 16, 2017, ordered that additional three standards not yet officially translated in the Republic of Srpska or published on AAARS website, shall be applied:

- IFRS 9 "Financial Instruments" (effective for annual periods beginning on or after January 1, 2018);
- IFRS 15 "Revenue from Contracts with Customers" (effective for annual periods beginning on or after January 1, 2018); and
- IFRS 16 "Leases" (effective for annual periods beginning on or after January 1, 2019).

***New Standards and Amendments to the Existing Standards and Interpretations Effective for the Current Reporting Period but not yet Officially Translated and Issued in the Republic of Srpska***

As of these financial statements' approval date, the following new standards and amendments to the existing standards were effective:

- Amendments to IFRS 9 "Financial Instruments" - Prepayment Features with Negative Compensation (effective for annual periods beginning on or after January 1, 2019);
- Amendments to various standards due to "Improvements to IFRSs (cycle 2015-2017)" resulting from the annual improvement project of IFRS (IFRS 3, IFRS 11, IAS 12 and IAS 23) primarily with a view to removing inconsistencies and clarifying wording (amendments should be effective for annual periods beginning on or after January 1, 2019);
- Amendments to IAS 19 "Employee Benefits" - Plan Amendment, Curtailment or Settlement (effective for annual periods beginning on or after January 1, 2019);
- Amendments to IAS 28 "Investments in Associates and Joint Ventures" - Long-term Interests in Associates and Joint Ventures (effective for annual periods beginning on or after January 1, 2019);
- IFRIC 23 "Uncertainty over Income Tax Treatments" (effective for annual periods beginning on or after January 1, 2019); and

The Bank's management analyzes the amendments to the standards and interpretations in effect as well as the newly adopted standards and interpretations issued after December 31, 2014, and, once the standards and interpretations relevant for the Bank have been determined, intends to implement those in preparation of the financial statements, if they are not in conflict with any of the regulations of Republic of Srpska and Bosnia and Herzegovina, after they have been officially translated and published in the Republic of Srpska.

***New Standards and Amendments to the Existing Standards Issued but not yet Effective***

- IFRS 17 "Insurance Contracts" (effective for annual periods beginning on or after January 1, 2021);
- Amendments to IFRS 10 "Consolidated Financial Statements" and IAS 28 "Investments in Associates and Joint Ventures" - Sale or Contribution of Assets between an Investor and its Associate or Joint Venture and further amendments (effective date deferred indefinitely until the research project on the equity method has been concluded;
- Amendments to IFRS 3 "Business Combinations" - Definition of a Business (effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 January 2020 and to asset acquisitions that occur on or after the beginning of that period);
- Amendments to IAS 1 "Presentation of Financial Statements" and IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors" - Definition of Material (effective for annual periods beginning on or after 1 January 2020); and
- Amendments to References to the Conceptual Framework in IFRS Standards (effective for annual periods beginning on or after 1 January 2020).

## 2. BASIS FOR PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS AND ACCOUNTING METHOD (Continued)

### 2.4. Application and Impact of the New and Revised International Financial Reporting Standards ("IFRS") and International Accounting Standards ("IAS") (Continued)

***New Standards and Amendments to the Existing Standards Issued but not yet Effective (Continued)***

It is the Bank's policy to adopt the new standards and amendments to the existing standards and apply them as from their effective date. The Bank's management anticipates that the adoption of these standards, amendments to existing standards and new interpretations will have no material impact on the financial statements of the Bank in the period of initial application.

### 2.5. Departures of the Local Regulations from the Requirements of IAS and IFRS

The only departure of the statutory accounting regulations for banks, in accordance with which these financial statements have been prepared, refers to the acquired assets received as partial or full payment of debts, where the difference in the net realizable value of such assets calculated under the local regulations and their net realizable value calculated under the requirements of IAS/IFRS amounted to BAM 110 thousand as of December 31, 2019 (December 31, 2018: BAM 274 thousand).

### 2.6. Effects of First-Time Adoption of IFRS 16 - Leases

As from January 1, 2019, the Bank has been applying IFRS 16 – Leases. IFRS 16 is applicable to all leases, including subleases and sale and lease-back transactions, except the contracts on leases to explore for or use minerals, oil, natural gas and similar non-regenerative resources, leases of biological assets, service concession arrangements and certain rights within the scope of IFRS 15 – Revenues from the Contracts with Customers and IAS 38 – Intangible Assets.

IFRS 16 defines the following exceptions from its application:
- short-term leases and leases with low-value underlying assets; and
- expedients for portfolios of leases with similar characteristics for both the lessees and lessors.

**Short-term leases**
Lessees may elect whether or not to recognize assets (right-of-use assets) and liabilities (lease liabilities) for short-term lease arrangements. Short-term leases are those with a lease term of 12 months or less, containing no purchase options.

**Leases with low-value underlying assets**
Lessees may elect to treat as exceptions form recognition under IFRS 16 leases where the underlying asset has a low value when new. Although the standard itself does not specify the value threshold above which assets cannot be classified as low-value assets, it does provide some examples such as IT equipment or office equipment. Automobiles are not in the category of low-value assets.

**Definition of a lease**
At the commencement of the lease contract, an entity is to assess whether the contract or a part thereof is a lease. A contract is, or contains, a lease if it conveys the right to control the use of an identified asset for a period of time in exchange for consideration. Control is conveyed where the customer has both the right to direct the identified asset's use and obtain substantially all the economic benefits from that use.
Under IFRS 16, a lease contract transfers the right of use of the identified asset to the lessee if the following two criteria are met:
- the lessee will obtain real economic benefits from the use of the asset during the period of usage (the lessee shall have the exclusive right of use of the asset; and
- the lessee will have the right to make decisions about how the asset will be used during the lease term.

**Accounting for the lease**
Following the commencement of the lease contract, IFRS 16 requires that lessees recognize all the leases within the balance sheet (statement of financial position). Accordingly:
- the lessee shall recognize depreciation of right-of-use assets during the lease term (mostly on a straight-line basis), along with the amortized cost of the lease liability; and
- the annual leasing costs should represent the depreciation charge of the right-of-use assets and interest on lease liabilities (the leasing costs will be dropping during the lease term due to lower interest on the decreasing principal amount).

## 2. BASIS FOR PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS AND ACCOUNTING METHOD (Continued)

### 2.6. Effects of First-Time Adoption of IFRS 16 – Leases (Continued)

**Initial recognition and measurement of the right-of-use assets**
At the inception of a lease (e.g., on a date when the lessor places certain assets to the disposition of the lessee), the lessee should recognize and measure the right-of-use assets using the cost method, as follows:

- an amount equal to the lease liability;
- plus any amounts prepaid by the lessee on the date or prior to the date of the lease commencement, less any discounts granted by the lessor;
- plus any direct lease costs (costs that would not have been incurred had there been no lease, e.g., lease commissions); and
- plus estimated costs of dismantling, removal and/or restoration of assets to the specified condition.

**Initial recognition and measurement of the lease liability**
At the inception of a lease, lessees recognize lease liabilities in the amount of the present value of the minimum future lease payments (discounted value). IFRS 16 was issued in January 2016 and is effective for the reporting periods beginning on or after January 1, 2019.

**First-time adoption impact**
Upon initial measurement, the new standard application resulted in increase in right-of-use assets by BAM 1,239 thousand and the lease liabilities (the aggregate principal amount) increased by BAM 1,181 thousand. In addition, the application of IFRS 16 will lead to reallocation of the previous leasing costs to the depreciation charge and costs of interest on the lease liabilities. The costs will be higher in the first years of the lease term, and they will decrease in the later periods in comparison to the previously effective IAS 17, due to the calculation of interest on the decreasing lease liability principal.

Upon transition to IFRS 16 it is possible to select one of the following two approaches:

1. a full retrospective approach, where IFRS 16 is applied to all prior reporting periods with due restatement of comparative figures; and
2. a cumulative catch-up approach, where IFRS 16 is applied retrospectively with a cumulative effect recognized as an adjustment of retained earnings as of January 1, 2019, without restatement of comparative data.

The Bank has opted for the cumulative catch-up approach and measured right-of-use assets based on the information available as of the IFRS 16 first-time adoption date. In other words, the Bank recorded its lease liabilities at the present value of the remaining lease payments, discounted using its incremental borrowing interest rate as of the IFRS 16 first-time adoption date. The value of the assets leased will be presented within assets as the right-of-use (ROU) assets under the line item of the Bank's property, plant and equipment, while the corresponding lease liabilities will be presented within liabilities in the statement of financial position.

Recognition of lease liabilities upon initial recognition:

| Undiscounted lease liabilities (under IAS 17) at December 31, 2018 | 1,669 |
|---|---|
| (-) discounting effects | (41) |
| **Discounted lease liabilities (under IAS 17)** | **1,628** |
| (-) exemption for short-term leases | (37) |
| (-) exemption for leases with low-value underlying assets | (36) |
| (+/-) lease contract extension and renewal/termination options likely to occur | (11) |
| (-) guaranteed residual values | (305) |
| (+/-) other | (58) |
| **Lease liabilities at January 1, 2019** | **1,181** |

Recognition of right-of-use (ROU) assets upon initial recognition:

| Unadjusted right-of-use assets at January 1, 2019 | 1,181 |
|---|---|
| (+) prepaid amounts | 58 |
| **Right-of-use assets at January 1, 2019** | **1,239** |

## 2. BASIS FOR PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS AND ACCOUNTING METHOD (Continued)

### 2.6. Effects of First-Time Adoption of IFRS 16 – Leases (Continued)

### 2.7. Going Concern

The accompanying financial statements have been prepared on a going concern basis, which entails that the Bank will continue to operate in the foreseeable future.

Throughout 2019 the Bank performed its operations in compliance with the effective legislation.

As of December 31, 2019, the Bank's regulatory capital ratio equaled 21.89%, while the ratio of the regular core capital was 21.47%. Based on the foregoing ratios, it is evident that the Bank had a solid capital position and that it meets the requirements and criteria for maintaining capital buffers.

During the year, the Bank's liquidity levels ranged within the limits prescribed by the Banking Agency of the Republic of Srpska. It should be noted that, after the milestone of 2017, and after positive performance in 2018, in 2019 the Bank continued to operate profitably, with the net profit of BAM 6,720 thousand.

Given the Bank's solid capital position, and its focus on straightforward banking with attractive credit product mix, along with improvements in service digitalization, the Bank's management concluded that these financial statements may be prepared on a going concern basis, which entails that the Bank will continue to operate in the foreseeable future.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.1. Interest Income and Expenses

Interest income and expenses are recognized in the statement of comprehensive income as they accrue for all interest-bearing instruments using the effective interest method. Interest income and expenses are accounted for on an accrual basis. The effective interest method is a method that calculates the costs of repayment of financial assets or financial liabilities and the costs of recognition of interest income or interest expense over a period. The effective interest rate is the rate that precisely discounts the estimated future cash disbursements or payments over the expected life of a financial instrument or, as appropriate, a shorter period, to the net carrying value of the financial asset or liability. When calculating the effective interest rate, the Bank estimates cash flows, taking into consideration all contractual terms related to the financial instrument (e.g. advance payments) but not considering future credit losses. The calculation includes all fees and commissions paid or received, which are a constituent part of the effective interest rate, transaction costs and all other premiums and discounts.

Interest income and expenses also include fee and commission income and expenses relating to loan origination and other differences between the initial carrying value of a financial instrument and its value at maturity, which are recognized using the effective interest rate.

### 3.2. Fee and Commission Income and Expenses

Fees and commissions are generally recognized on an accrual basis when due for collection i.e. when the relevant service has been rendered. Such fees and commissions relate to domestic and foreign payment transactions, off-balance sheet operations (issuance of guarantees), broker-dealer operations and the like.

Fee and commission expenses relate to fees paid to the Central Bank of Bosnia and Herzegovina for the local payments operations, SWIFT costs, costs of payment card operations and other fees (Note 8).

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.2. Fee and Commission Income and Expenses (Continued)

***IFRS 15 – Revenue from Contracts with Customers***

New IFRS 5 – *Revenue from Contracts with Customers* defines the timeframes and amounts for recognition of revenues from contracts with customers. The standard's basic principle is that a reporting entity should recognize revenue when the contractual performance obligation has been fulfilled, i.e., control over the goods or services transferred to the customer. IFRS 15 is not applicable to the following types of contracts:

- leases within the scope of IAS 17;
- insurance contracts within the scope of IFRS 4;
- financial instruments and other contractual rights or obligations within the scope of IFRS 9 *Financial Instruments*, IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements*, IAS 27 *Separate Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures;* and
- non-monetary exchanges between entities in the same line of business to facilitate sales to customers or potential customers.

Accordingly, the interest income and dividend income are no longer within the scope of the standard for revenue recognition. Instead, they are covered by IFRS 9 – Financial Instruments. Since the Bank earns revenues primarily from the financial instruments that are excluded from the scope of IFRS 15, application of the standard will not result in significant changes within the Bank.

Adoption of IFRS 15 did not affect the time or amount of recognized income from fees and commissions from the contracts with customers and related assets. IFRS 15 supersedes clauses on current income recognition pf IAS 11, IAS 18 and the relating interpretations.
IFRS 15 is effective for period beginning on or after January 1, 2018.

### 3.3. Foreign Exchange Translation

Transactions denominated in foreign currencies are translated into the functional currency at official rates effective at the date of each transaction. Assets and liabilities denominated in foreign currencies on the statement of financial position date are translated into BAM by applying official rates of exchange effective on that date. Contingent liabilities denominated in foreign currencies are translated into BAM at official exchange rates effective at the statement of financial position date.

Foreign exchange effects arising from translation are credited or charged to the profit or loss statement. The Bank has no monetary securities denominated in foreign currencies.

Exchange rates used in these financial statements are official rates established by the Central Bank of Bosnia and Herzegovina (“CBBH”).

### 3.4. Employee Benefits

Short-Term Employee Benefits

Short-term benefits include employee salaries and benefits and all the related taxes and contributions payable to the Republic of Srpska social security and pension funds, calculated by applying the specific percentage rates which are stipulated by the relevant regulations. Short-term employee benefits are recognized as expenses in the period in which they are incurred.

Retirement Benefits and Annual Leave (Vacation) Entitlements

According to the Labor Law of the Republic of Srpska and the Bank’s Rules of Procedure, employees are entitled to receive benefits upon retirement. The retirement benefit liability costs recognized in the statement of profit or loss represent the present value of the defined benefit liabilities as determined by actuarial calculations.

Provisions for retirement benefits and annual leave (vacation) entitlements are disclosed in the statement of financial position within “other liabilities.”

Retirement benefits provisions are based on actuarial reports and are used only for the purposes they are intended for. At each year-end, accuracy and adequacy of the amounts of provisions for retirement benefits and annual leave entitlements are assessed. In accordance with amendments to IAS 19, changes in retirement benefits are included in “personnel expense” within the statement of profit or loss unless they relate to actuarial gains or losses. Otherwise, such changes are immediately recognized in other comprehensive income. Benefits falling due more than 12 months after the statement of financial position date are discounted to their present value.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.5. Income Taxes

***Current Income Tax***

Current income tax relates to the amount calculated and paid in accordance with the Corporate Income Tax Law. Current income tax is payable at the rate of 10% applied to the tax base determined in the taxa statement and reported in the annual corporate income tax return, being the amount of profit before taxation net of income and expense adjustment effects pursuant to the tax regulations of the Republic of Srpska.

The tax regulations in the Republic of Srpska do not envisage that any tax losses of the current period be used to recover taxes paid within a specific carryback period. However, current period tax losses stated in tax return may be used to reduce or eliminate taxes to be paid in future periods but only for duration of no longer than five ensuing years.

***Deferred Income Taxes***

Deferred income taxes are calculated on all temporary differences between tax base of assets and liabilities and their carrying amounts stated in financial statements of the Bank. Deferred tax liabilities are recognized for all taxable temporary differences between the tax base of assets and liabilities at the statement of financial position date and carrying values reported in the financial statements, which will result in future period taxable amounts.

Deferred tax assets are generally recognized for all deductible temporary differences, unused tax assets and unused tax losses to the extent that it is probable that taxable profits will be available against which those deductible temporary differences, unused tax credits and unused tax losses can be utilized.

Deferred tax assets are only recognized to the extent that it is probable that there will be sufficient taxable profits against which to utilize the benefits of the temporary differences against profits earned.

### 3.6. Cash and Cash Equivalents

For purposes of the cash flow statement, cash on hand, balances on the accounts held with the Central Bank, foreign currency accounts with foreign and domestic banks and short-term deposits with maturities of up to 30 days held with foreign and domestic banks are all considered to be cash equivalents.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.7. Financial Instruments

### 3.7.1. IFRS 9 - Financial Instruments – Business Model

***Business Model***

In order to classify financial assets in accordance with IFRS 9, the Bank needed to do the following two steps:
(i) assess the characteristics of the contractual cash flows of assets, i.e., perform the so-called SPPI test (whether the cash flows of an asset represent solely payments of principal and interest on the principal amount outstanding), and
(ii) assess the business model the assets are held within.

By its business model, the Bank demonstrates in what manner it manages its financial assets in order to generate cash flows, in other words, whether it will generate the cash flows from collection of the instruments' contractual cash flows, by selling the financial assets or both. The model assessment is conducted based on the scenario the Bank can reasonably anticipate. This means that the assessment does not include the so-called "worst case scenario" or the "stress case scenario".

Taking into account analyses of the historical cash flow generation and anticipated sales for the future, the Bank has the following business models:

- **Held-to-Collect model,** which includes loans due from customers;
- **Held-to-Collect-and-Sale model**, which includes a portfolio of debt securities available for sale; and
- **Other business model,** which includes a trading securities' portfolio**.**

Under 9.4.1.1(a), financial assets are classified according to the business model for managing those assets except in cases to which paragraph IFRS 9.4.1.5 is applicable. The Bank assesses whether its financial assets meet the condition defined in paragraph IFRS 9.4.1.2(a) or paragraph IFRS 9.4.1.2A(a) based on the business model defined by the Bank's key management (as defined by IAS 24 – *Related Party Disclosures*).

A business model is determined at the level reflecting the manner in which groups of financial assets are jointly managed to achieve a certain business goal. The business model does not depend on management's intentions for an individual instrument. Accordingly, this condition is not an instrument-by-instrument approach to classification and should be determined on a higher level of aggregation. However, there may be more than one business model for managing the financial instruments. Therefore, classification is determined at the cash-generating unit level.

For example, an entity may hold a portfolio of investments that it manages in order to collect contractual cash flows and another portfolio of investments that it manages in order to trade to realize gains on the fair value changes. Similarly, an entity may decide that it is appropriate to divide a portfolio of financial assets into sub-portfolios in order to present the level at which the entity manages its financial assets. This may be the case, for instance, when the entity creates or purchases a portfolio of mortgage loans and manages some of these loans in order to collect the contractual cash flows and the other loans are intended for sale.

The Bank shows by way of its business model the manner in which it manages its financial assets in order to generate cash flows, i.e., the business model demonstrates whether the Bank will generate the cash flows from (i) collection of the contractual cash flows, (ii) sales of the financial assets, or (iii) both these sources. This is why the business model assessment is not made based on the so-called "worst case scenario" or the "stress case scenario".

For example, the Bank expects to sell a certain portfolio of financial assets within the stress case scenario. Such a scenario does not affect the assessment of the Bank's business model for those particular assets if the Bank reasonably anticipates that such a scenario will not occur.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.7. Financial Instruments (Continued)

#### 3.7.1. IFRS 9 - Financial Instruments – Business Model (Continued)

***Business Model (Continued)***

If the cash flows were realized in a manner different form the Bank's expectation as of the business model assessment date (e.g., more or less financial assets are sold than anticipated upon classification of those assets), that will not be the cause of the previous period misstatement in the Bank's financial statements (refer to IAS 8), or change the classification of the remaining financial assets within the business model (assets recognized by the Bank in prior periods and still held) on condition that, in assessing the business model, the Bank has taken into account of the relevant information available at the time of assessment. However, when the Bank assesses the business model for newly originated or purchased financial assets, it must consider the information on the historical cash flows along with all the other relevant information.

This means that there is no concept which is the same as that for treatment of the financial assets held to maturity under IAS 39. Rather, the manner of realizing the cash flows changes and it affects classification of the new assets upon initial recognition.

The Bank's business model is a fact and not a mere representation. It may usually be monitored through the activities taken by the Bank to achieve the objective defined by the business model. The Bank assesses the business model for management of its financial assets based on the evaluation, based not only upon a single factor or activity but on all the relevant evidence available as of the model assessment date.

***Held-to-Collect Model***

The Bank manages financial assets held within the business model whose objective is to hold the assets in order to collect the contractual cash flows so as to generate cash flows from collection of particular contractual cash flows over the instrument’s life. This means that the Bank manages the assets held in the portfolio to collect the contractual cash flows (rather than manage the overall turnover per such a portfolio by holding and selling the assets). Upon determining whether the cash flows will be generated from the collection of the contractual cash flows of the financial assets, the Bank considers the frequency, volume and timing of sales in prior periods, the reasons for such sales and expectations about future sales activity. The sale activity is not to be considered in isolation since the business model cannot be determined solely based on the sales. Instead, the Bank needs to consider both the historical sale information as well as the expectations of the future sales as part of an overall assessment on how the Bank´s stated objective for managing the financial assets is achieved and how the cash flows are realized. However, the information on the historical sales need to be regarded within the context of the particular sale and conditions prevailing at that time, which are to be compared and contrasted to the current conditions.

Although the objective of the Bank’s business model may be to hold financial assets in order to collect contractual cash flows, the Bank need not hold all of those instruments until maturity, so that the business model can be to hold financial assets to collect contractual cash flows even when sales of financial assets occur or is expected to occur in the future.

The objective of the Bank’s business model may be to hold financial assets in order to collect contractual cash flows even if the Bank sells the financial assets, which may be:

- If there has been a **significant increase in the credit risk** of those assets. When determining whether the credit risk (i.e., risk of default) on a financial instrument has increased significantly since initial recognition, the Bank will consider reasonable and supportable information, including forward-looking information. Irrespective of the frequency and volume of sales of financial assets due to significant increase in the credit risk of those assets, such sales are not deemed **inconsistent** with the business model whose objective is to hold financial assets to collect the contractual cash flows since it is the quality of the financial assets that is relevant to the Bank's ability to collect the contractual cash flows. An integral part of such a business model are activities of credit risk management aimed at minimizing potential credit losses due to the credit quality deterioration. An example of the sales due to a significant credit risk increase is a sale of financial assets because the assets no longer meet the credit quality criteria defined by the Bank's documented investment policy. However, if the Bank has no such policy in place, the Bank may otherwise present that the sale was made due to the increase in the credit risk.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.7. Financial Instruments (Continued)

### 3.7.1. IFRS 9 - Financial Instruments – Business Model (Continued)

***Held-to-Collect Model (Continued)***

- Sales for other reasons, such as **credit concentration risk management** (without an increase in the credit risk of financial assets), may also be consistent with the Bank's business model whose objective is to hold financial assets to collect the contractual cash flows. Such sales may particularly be consistent with the business model whose objective is to hold financial assets to collect the contractual cash flows if the sales are not frequent (even if the volume, i.e., amounts of such sales are significant) or if the value of an individual sale or of the aggregate sales is immaterial (even if the number of such sales is large).
  If multiple sales are made within the portfolio (the number of which is higher than the immaterial number) and if the value of such sales is higher than the immaterial value (individually or in the aggregate), the Bank needs to assess whether and how such sales are consistent with the objective to collect the contractual cash flows.
  For such an assessment, the information whether the sales are imposed on the Bank by a third party or the Bank has decided to sell the assets on its own is irrelevant. Increase in the frequency or value of the sales over the specific period is not necessarily inconsistent with the objective of holding the financial assets to collect the contractual cash flows if the Bank can provide a rationale for such sales and demonstrate why such sales do not mean a change of the business model.

- Further, a sale may be consistent with the objective of holding the financial assets to collect the contractual cash flows if the sale occurs **shortly before maturity of the financial assets** and if the gain on the sale approximate the amount of collection of the remaining cash flows.

***Transferred Financial Assets not Derecognized***

In various circumstances the Bank may sell financial assets yet such assets still remain within its statement of financial position, for example, in “repo” transactions, when the Bank sells debt securities and at the same time agrees to repurchase them at a fixed price. In such instances, the seller retains substantially all the risks and rewards of the ownership of such assets and does not derecognize the financial assets in accordance with the requirements of IFRS 9. For the purpose of the business model assessment, it is the accounting treatment rather than the legal form of the transaction that determines whether the entity has stopped holding the financial assets to collect the contractual cash flows.

***Held-to-Collect-and-Sale Model***

The Bank may manage financial assets within the business model whose objective achieved by both collection of the contractual cash flows and sales of the financial assets. In such a business model, the senior management has decided that the achievement of the business model objective requires both the collection of the contractual cash flows and sales of the financial assets. Various objectives may consistent with this type of the business model. For example, the objective may be to manage daily liquidity requirements, maintain a certain interest income profile or match the maturities of assets with the maturities of liabilities covered with those assets. In order to achieve such an objective, the Bank will collect the contractual cash flows and sell the financial assets.

Compared to the held-to-collect business model, this model normally entails higher frequency and value of the sales due to the fact that the sale of financial assets is an integral part of achieving the business model’s objective and not just a side effect.

However, there is no threshold for the frequency or value of sales that must be performed within this business model for both collection of the contractual cash flows and sales of the financial assets are elements of achieving the business model’s objective.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.7. Financial Instruments (Continued)

#### 3.7.1. IFRS 9 - Financial Instruments – Business Model (Continued)

***Other Business Model***

Financial assets are measured at fair value through profit or loss (FVtPL) if not held within the business model whose objective is to collect the contractual cash flows or within the model whose objective is achieved by both collection of the contractual cash flows and sales of the financial assets (para. 5.7.5). The business model resulting in the measurement of the financial assets at FVtPL is a model in which the Bank manages the financial assets in order to generate the cash flows through the sales of assets. The Bank makes decision based on the fair value of assets and manages the assets in order to realize the fair value thereof. In such a case, the Bank’s goal is usually achieved through active sales and purchases. Although the Bank collects the contractual cash flows while holding the financial asset, the objective of this model is not achieved by both collecting the contractual cash flows and selling the assets, because the collection of the contractual cash flows is not an element of achieving the objective of the model but simply represents a side effect.

Upon initial recognition, the Bank may make an irrevocable election to classify the instruments at FVtOCI, in order to present all subsequent changes in the fair value of investment in an equity instruments belonging to the scope of IFRS 9, which is not held for trading or is subject to a consideration recognized by the acquirer in a business combination to which IFRS 3 is applicable.

The portfolio of financial asset managed or resulting in assessment at fair value (as described in IFRS 9.4.2.2(b)) is held neither to collect the contractual cash flows nor to collect the contractual cash flows and sell the assets. Here the Bank is primarily focused on the information on fair value, which is used for assessment of the performance of the financial assets and decision making. In addition, the Bank's portfolio of financial assets meeting the criteria of definition of the financial assets held for trading, is held neither to collect the contractual cash flows nor to collect the contractual cash flows and sell the assets. In such portfolios, collection of the contractual cash flows is simply a side effect in achieving the business model's objective and that is why such portfolios must be measured at fair value through profit or loss.

#### 3.7.2. IFRS 9 - Financial Instruments – Recognition

The Bank recognizes loans and receivables and other financial liabilities at the date of occurrence, i.e., when disbursed to customers or received from the creditors.

Regular way purchases and sales of financial instruments are recognized on the trading date, i.e., the date when the Bank has become a party to the contractual terms of a particular instrument.

#### 3.7.3. IFRS 9 - Financial Instruments – Classification

The Bank classifies its financial assets into the following categories;
- Financial assets subsequently measured at amortized cost (AC);
- Financial assets measured at fair value through other comprehensive income (FVtOCI); and
- Financial assets measured at fair value through profit or loss (FVtPL).

The Bank may, at initial recognition, irrevocably designate a financial asset that would otherwise have to be measured at amortized cost or fair value through other comprehensive income to be measured at fair value through profit or loss if doing so would eliminate or significantly reduce a measurement or recognition inconsistency (‘accounting mismatch’) that would otherwise arise from measuring assets or liabilities or recognizing the gains and losses on them on different bases.

In addition, the Bank may, at initial recognition, irrevocably designate certain investments in equity instruments as financial assets at FVtOCI.

Classification of the financial assets is made based on:
- The business model for management of the financial assets; and
- characteristics of the contractual cash flows of the instruments.

The Bank's management classifies financial assets upon initial recognition.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.7. Financial Instruments (Continued)

#### 3.7.3. IFRS 9 - Financial Instruments – Classification (Continued)

As of December 31, 2019, the Bank had financial assets subsequently measured at amortized cost (AC), financial assets held for trading and financial assets measured at fair value through other comprehensive income (FVtOCI).

***Financial Assets Measured at Amortized Cost (AC)***

Financial assets measured at AC are financial assets that meet both of the following two criteria:
- the asset is held within a business model whose objective is to hold assets in order to collect contractual cash flows (Held-to-Collect model); and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest (SPPI) on the principal amount outstanding.

***Loans and Receivables***

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

***Financial Assets Measured at Fair Value through Other Comprehensive Income (FVtOCI)***

Financial assets measured at FVtOCI are financial assets that meet both of the following two criteria:
- the asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest (SPPI) on the principal amount outstanding.

***Financial Assets and Liabilities Measured at Fair Value through Profit or Loss (FVtPL)***

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

The Bank classifies financial assets and liabilities as financial instruments at fair value through profit or loss when:

- the assets and liabilities are managed, evaluated and reported internally at fair value;
- such designation eliminates or significantly reduces an accounting mismatch that would otherwise arise;
- the asset or liability contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.7. Financial Instruments (Continued)

### 3.7.3. IFRS 9 - Financial Instruments – Classification (Continued)

***Fair Value Measurement***

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Group has access at that date. The fair value of a liability reflects its non-performance (default) risk.

The fair value of securities quoted in an active market are based on current bid prices. If the market for a financial asset (and the market of unlisted securities) is not active, the Group establishes fair value by valuation techniques. These involve the application of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis and other valuation techniques.

### 3.7.4. IFRS 9 - Financial Instruments – Derecognition

The Bank derecognizes financial assets (in full or partially) when the rights to receive cash flows from the financial instrument have expired or when it loses control over the contractual rights on those financial assets. This occurs when the Bank transfers substantially all the risks and rewards of ownership to another business entity or when the rights are realized, ceded or have expired.

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

### 3.7.5. Impairment of Financial Assets

#### *3.7.5.1. Financial Assets Measured at Amortized Cost*

Under IFRS 9, impairment covers the following exposures (IFRS 9.5.5.1):
- financial assets that comprise debt instruments such as loans, debt securities, bank balances and deposits and trade receivables, which are measured at amortized cost (AC);
- financial assets measured at fair value through other comprehensive income (FVtOCI);
- Lease receivables within the scope of IAS 17;
- Contractual assets under IFRS 15;
- Borrowings other than those measured at fair value through profit or loss (FVtPL) under IFRS 9 (borrowings designated as FVtPL are excluded);
- Financial guarantee contracts other than those measured at fair value through profit or loss (FVtPL) under IFRS 9 (financial liabilities arising when the transfer of financial assets does not meet the derecognition criteria or when there is continuing involvement are excluded).

At each reporting date, the Bank assesses whether there is objective evidence that a financial asset or group of financial assets has suffered impairment.

A financial asset or a group of financial assets is considered to be impaired and impairment losses are incurred only if there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the asset (a ‘loss event’), the estimated future cash flows of the financial asset or group of financial assets have been affected by the event or events, and that the amount of the loss incurred can be reliably estimated. The criteria that the Bank uses to determine that there is objective evidence of an impairment loss are described in its Credit Risk Provisioning Policy – Methodology for measurement of Impairment and Provisions.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.7. Financial Instruments (Continued)

### 3.7.5. Impairment of Financial Assets (Continued)

#### *3.7.5.1. Financial Assets Measured at Amortized Cost (Continued)*

For the assessment of the impairment allowances and credit loss expense on financial assets may be allocated to Stage 1, Stage 2, Stage 3) and POCI assets (purchased or originated credit impaired assets):

- Stage 1 – includes financial assets where no significant increase of credit risk has been identified since initial recognition or those with low credit risk level at the reporting date. For such assets, provisions based on the 12-month expected credit losses are recognized and interest income is calculated on the gross carrying value of the assets. 12-month expected credit losses (ECL) are expected credit losses arising from default that may occur within 12 months from the reporting date.

- Stage 2 – includes financial assets where a significant increase of credit risk has been identified since initial recognition (unless they have low credit risk level at the reporting date and this option is elected by the Bank), however, there is no objective evidence of impairment and those are not POCI assets. For such assets, provisions based on the lifetime expected credit losses are recognized but interest income is still calculated on the gross carrying value of the assets. Lifetime expected credit losses (ECL) are expected credit losses arising from all possible defaults over the maximum contractual term over which the Bank is exposed to credit risk. Such an expected credit loss is a default-risk-weighted average credit loss. The expected credit loss will be discounted at the reporting date using the effective interest rate or a rate approximating the effective interest rate.

- Stage 3 can be divided into:
  - Stage 3 ii – individual (special) risk provisions – individual imapirment: includes financial assets with objective evidence of impairment at the reporting date. For such assets, provisions based on the lifetime expected credit losses are recognized but interest income is calculated on the net carrying value of the assets.
  - Stage 3 ci – individual (special) risk provisions – collective imapirment: includes financial assets with objective evidence of impairment at the reporting date. For such assets, provisions based on the lifetime expected credit losses are recognized but interest income is calculated on the net carrying value of the assets.

- POCI assets –purchased or originated credit-impaired financial assets are financial assets whose value was impaired upon acquisition, i.e., at the time of purchase or origination, due to significant credit risk (IFRS 9.5.5.13). If a financial asset is deemed to be credit impaired at initial recognition, the Bank ought to recognize such asset as a POCI asset unless it is measured at FVtPL.

Loss identification period (LIP) is assessed by the management, separately for each portfolio type. This period generally ranges between 3 and 12 months. Exceptionally, it may exceed 12 months.

In accordance with IFRS, the Bank first assesses individually whether there is objective evidence of imapirment of individually significant financial assets and, either individually or collectively, of financial assets that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognized are not included in a collective assessment of impairment.

**3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**3.7. Financial Instruments (Continued)**

**3.7.5. Impairment of Financial Assets (Continued)**

***3.7.5.1. Financial Assets Measured at Amortized Cost (Continued)***

If there is objective evidence of the impairment of financial assets carried at amortized cost, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognized in the income statement. If a financial asset has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

When a loan is irrecoverable it is written off by derecognition of both the relevant loan and the related allowance for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined.

If a loan is written off without the Bank waiving the receivables due from the customer (the so-called internal or accounting write-off), the amount of the receivable written off is at the same time recorded on-balance, within the internal write-off adjustment accounts, and off-balance, within off-balance sheet items. The aforedescribed internal write-off of receivables represents a partial or full write-off when the Bank no longer reasonably expects recovery of the financial assets. The customer's gross debt toward the Bank remains the same and is communicated to the customer as such, while the internal write-off represents an adjustment to the customer gross exposure and serves for the purposes of accounting and reporting under IFRS 9. internal write-offs are commonly performed for receivables allocated to Stage 3ii and Stage 3ci.
If an internally written-off receivable is subsequently recovered, it is recorded within income, as the recovery of the receivables previously written off.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be objectively related to an event occurring after the impairment was recognized (such as an improvement in the debtor's credit rating), the previously recognized impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognized in the profit or loss as the income from reversal of impairment allowance/provision.
Whenever possible, the Bank seeks to restructure loans rather than foreclose collaterals securing loan repayment. If the terms of the financial assets are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, an assessment is made of whether the financial asset should be derecognized. If the cash flows of the renegotiated assets are substantially different, then the contractual rights to cash flows from the original financial assets are deemed to have expired. Once the terms have been renegotiated any impairment is measured using the original effective interest rate as calculated before the modification of terms and the loan is no longer considered past due. Management continually reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. Rescheduled loans will be subject to individual or group-level assessment for impairment and provisioning using the original effective interest rate.

***3.7.5.2. Financial Assets Measured at Fair Value through Other Comprehensive Income (FVtOCI)***

At each reporting date, the Bank assesses whether there is objective evidence that a financial asset or a group of financial assets is impaired. In case of securities classified as measured at FVtOCI, a significant or prolonged decline in the fair value of the security below its cost is objective evidence of impairment resulting in the recognition of an impairment loss. If any such evidence exists for these financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value – is recognized in the statement of other comprehensive income.
If, in a subsequent period, the fair value of a debt instrument classified as at FVtOCI increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in the profit or loss, the increase will be recognized within equity, under fair value reserves until such security is sold.

Interest on debt instruments and foreign exchange gains/losses are recognized directly in the profit or loss. Credit risk provisions for debt instruments are recognized within the statement of profit or loss and other comprehensive income, while their net carrying values remain equal to the fair values within assets, i.e., they are not decreased by the credit risk provisions.
Impairment of financial assets classified as measured at FVtOCI is made in the same manner as the impairment of financial assets measured at AC.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.7. Financial Instruments (Continued)

### 3.7.5. Impairment of Financial Assets (Continued)

#### *3.7.5.3. Estimation of Potential Losses for Financial Assets in Accordance with the Requirements of the Banking Agency of the Republic of Srpska*

In accordance with the Decision of the Banking Agency of the Republic of Srpska on Classification of Assets and Off-Balance Sheet Items according to the Degree of Collectability, the Bank is required to classify loans, investments and other balance sheet and off-balance sheet risk exposures into categories A, B, C, D and E in accordance with the assessment of recoverability of loans and other investments based on regularity and timeliness in liability settlement on the part of the debtor, debtor's financial position and collaterals securitizing collection of receivables. The estimated amount of reserves for potential losses is calculated by applying the following percentages: 2% to loans classified as category A, 5% - 15% to the loans in category B, 16% - 40% to loans in category C, 41% - 60% to loans in category D and 100% to investments in category E.

The difference between impairment allowances determined in accordance with IFRS 9 and estimated provisions for potential losses on loans classified into categories, when negative, is presented as a deductible item in calculation of the capital adequacy.

In 2019, the Banking Agency of the Republic of Srpska (“BARS”) enacted the Decision on Managing Credit Risk and Determining Expected Credit Losses (the “Decision”) to prescribe the minimum requirements for credit risk management. The effects of the initial application of the said Decision represent the difference between the expected credit losses determined in line with the stipulations of the Decision and those determined and accounted for in accordance with the Bank’s internal methodology. When the expected credit losses determined in such a manner, they are recorded within equity.

The total effect of adjusting the carrying values of financial instruments due to the application of the Decision will be recognized within the Bank’s equity as of January 1, 2020 in the amount of BAM 4,511 thousand, with the capital adequacy ratio estimated at about 21.23% before addition of the net profit for FY 2019, i.e., about 22.22% with the net profit for FY 2019 added.

### 3.7.6. Offsetting of the financial instruments

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

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

### 3.7.7. Derivative Financial Instruments

Derivative financial instruments are initially recognized in the statement of financial position in accordance with the policy for initial recognition of financial instruments and subsequently remeasured at their fair value. Fair values are obtained from quoted market prices, dealer price quotations, discounted cash flow models and options pricing models.

All derivatives are carried as assets when their fair value is positive and as liabilities when negative. Changes in the fair value of derivatives are included in the profit or loss statement under “net profit on financial instruments”. All derivatives are classified as held for trading.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.7. Financial Instruments (Continued)

### 3.7.7. Derivative Financial Instruments (Continued)

Some hybrid contracts contain both a derivative and a non-derivative component. In such cases, the derivative component is termed an embedded derivative. When the economic characteristics and risks of embedded derivatives are not closely related to those of the host contract and when the hybrid contract is not itself carried at fair value through profit or loss, the embedded derivative is treated as a separate derivative and classified at fair value through profit or loss with all unrealized and realized gains and losses recognized in the profit or loss unless there is no reliable measure of their fair value.

Derivative financial instruments include currency forward contracts and currency swaps.

### 3.8. Managed Funds - Custody Operations

Assets and income arising from operating activities, where the Bank performs custody operations, which include holding or keeping the funds for the benefit of individuals, creditors and other institutions are included in Bank's financial statements.

### 3.9. Property and Equipment

***Land, Buildings and Equipment***

Property and equipment are carried at their fair value, as periodically determined by certified appraisers, subsequently decreased by the accumulated depreciation and impairment, if any.

Subsequent expenditures are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. All other repair and maintenance costs are charged to the statement of comprehensive income during the financial period in which they are incurred.

Increases in the carrying amount arising on revaluation of buildings and equipment are credited to equity as revaluation reserve. The increase is recognized in the profit or loss statement only to the extent that it reverses a revaluation decrease of the same asset previously recognized as an expense in the profit or loss. If an asset's carrying amount is decreased as a result of a revaluation, the decrease is recognized as an expense in the profit or loss statement. The decrease is debited directly to revaluation reserve within equity to the extent of any credit balance existing in the revaluation surplus in respect of that asset.

Revaluation reserves included in equity in respect of property and equipment are transferred directly to retained earnings successively (annually) or when the asset is derecognized. This may involve transferring the entire revaluation reserves when the asset is retired or disposed of.

Land is not depreciated. Depreciation of other assets is calculated based on their cost or previously revalued amounts using the straight-line method to allocate their cost or revalued amounts to the residual value of the assets over their estimated useful lives:

| | Depreciation Rate | Useful Life (years) |
|---|---|---|
| Buildings | 0.62% - 3.33% | 30 - 85 |
| Computer equipment | 20.00%-33.33% | 3 - 5 |
| Furniture and other equipment | 6.67% - 33.3% | 3 - 14 |

Management believes that depreciation rates applied fairly reflect the economic useful lives of property and equipment.

Gains and losses on disposal of assets are determined as the difference between the proceeds from the disposal and the carrying amounts of assets and are recognized in the profit or loss statements within gains or losses on the sale of disposal of property and equipment.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.9. Property and Equipment (Continued)

***Investment Property***

Investment property is property held either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business, use in supply of goods or services or for administrative purposes. Investment property is initially measured at cost increased by transaction costs. Subsequent to initial recognition, investment property is stated at fair value. Gains or losses arising from changes in the fair value are included in the profit or loss statement in the period in which they arise. When the use of a property changes from owner-occupied to investment property, the property is remeasured to fair value and reclassified as investment property.

Investment properties are derecognized when either they have been disposed of or when the investment property is permanently retired from use and no future economic benefit is expected from its disposal. The difference between the net disposal proceeds and the carrying amount of the asset is recognized in the income statement in the period of derecognition.

### 3.10. Intangible Assets

Intangible assets are stated at fair value as periodically determined by valuation, net of accumulated amortization. Intangible assets include computer software and licenses.

The Bank recognizes an intangible asset only if it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. Such investments are capitalized at cost.

Revaluations of intangible assets are conducted regularly so that the carrying amounts do not differ significantly from the amounts that would be recognized by determining the fair values of assets at the statement of financial position date. If the carrying amount of an intangible asset is increased as a result of revaluation, the increase is directly recorded as an increase in the revaluation reserves within equity.
If the carrying amount of an intangible asset is reduced as a result of revaluation, the decrease should be recognized as an expense unless the revaluation reserve has not been previously formed or directly charged to the revaluation reserve.

Intangible assets are derecognized when they are sold or when there are no future economic benefits expected from their use. Gains or losses arising from the retirement or disposal of an intangible asset are determined as the difference between the net disposal proceeds and the carrying amount of the asset and recognized as income or expenses in the profit or loss statement.

The estimated useful lives of intangible assets are as follows:

| | Amortization Rate | Useful Life (years) |
|---|---|---|
| Intangible assets | 9.83% - 33.33% | 3 - 10 |

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.11. Leases – Policy Applicable until December 31, 2018

Leases in which the Bank, as the lessee, assumes all the risks and rewards of ownership, are classified as finance leases. All other leases are operating leases.

***a) Finance Leases***

Finance lease is a lease that, substantially, transfers all the risks and rewards incidental to ownership of the leased item. After the expiry of the lease period, the right of ownership can but need not be transferred.

Upon initial recognition, the Bank as the lessor recognizes the funds given to finance lease in the statement of financial position as long-term financial investments equal to the amount of the purchase value of the leased asset plus future interest.

Gross investment in the lease represents the total amount of all minimum lease payments and any non-guaranteed residual value attributable to the lessor. Net investment in the lease equals gross investment in the lease as decreased by the unearned finance income calculated at an interest rate defined by the relevant lease contract. Investments in the lease stated in the statement of financial position as long-term financial investments are subsequently measured at amortized cost less the assessed allowance for impairment.

Finance income, i.e. interest income based on the finance lease operations is recognized based on a pattern reflecting a constant periodic rate of return on the lessor's net investment in the finance lease.

***b) Operating Leases***

*The Bank as the Lessor*

Leases are classified as operating leases if the terms of the lease do not transfer substantially all risks and rewards of ownership to the lessee.

Assets used for operating lease are recognized within the statement of financial position of the lessor at cost and are depreciated in accordance with the depreciation policy applied to the lessors own assets. Lease income from operating leases (rentals) is recognized as income in the period it refers to.

Initial direct costs incurred by lessors in negotiating and arranging an operating lease may be recognized as expenses of the period when incurred or be added to the carrying amount of the leased asset, deferred and recognized as an expense over the lease term on the same basis as the rental income.

*The Bank as the Lessee*

Lease payments under an operating lease are recognized as an expense on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit. Contingent fees arising from operating lease are recognized as expenses of the period when incurred.

In the event that lease incentives are received to enter into operating leases, such incentives are recognized as a liability. The aggregate benefit of incentives is recognized as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

### 3.12. IFRS 16 - Leases – Policy Applicable as from January 1, 2019

As from January 1, 2019, the Bank has been applying IFRS 16 – *Leases*. IFRS 16 is applicable to all leases, including subleases and sale and lease-back transactions, except the contracts on leases to explore for or use minerals, oil, natural gas and similar non-regenerative resources, leases of biological assets, service concession arrangements and certain rights within the scope of IFRS 15 – *Revenues from the Contracts with Customer*s and IAS 38 – *Intangible Assets*.

IFRS 16 defines the following exceptions from its application:
- short-term leases and leases with low-value underlying assets; and
- expedients for portfolios of leases with similar characteristics for both the lessees and lessors.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.12. IFRS 16 - Leases – Policy Applicable as from January 1, 2019 (Continued)

**Short-term leases**
Lessees may elect whether or not to recognize assets (right-of-use assets) and liabilities (lease liabilities) for short-term lease arrangements. Short-term leases are those with a lease term of 12 months or less, containing no purchase options.

**Leases with low-value underlying assets**
Lessees may elect to treat as exceptions form recognition under IFRS 16 leases where the underlying asset has a low value when new. Although the standard itself does not specify the value threshold above which assets cannot be classified as low-value assets, it does provide some examples such as IT equipment or office equipment. Automobiles are not in the category of low-value assets.

**Definition of a lease**
At the commencement of the lease contract, an entity is to assess whether the contract or a part thereof is a lease. A contract is, or contains, a lease if it conveys the right to control the use of an identified asset for a period of time in exchange for consideration. Control is conveyed where the customer has both the right to direct the identified asset's use and to obtain substantially all the economic benefits from that use.

Under IFRS 16, a lease contract transfers the right of use of the identified asset to the lessee if the following two criteria are met:

- the lessee will obtain real economic benefits from the use of the asset during the period of usage (the lessee shall have the exclusive right of use of the asset; and
- the lessee will have the right to make decisions about how the asset will be used during the lease term.

**Accounting for the lease**
Following the commencement of the lease contract, IFRS 16 requires that lessees recognize all the leases within the balance sheet (statement of financial position). Accordingly:

- the lessee shall recognize depreciation of right-of-use assets during the lease term (mostly on a straight-line basis), along with the amortized cost of the lease liability; and
- the annual leasing costs should represent the depreciation charge of the right-of-use assets and interest on lease liabilities (the leasing costs will be dropping during the lease term due to lower interest on the decreasing principal amount).

**Initial recognition and measurement of the right-of-use assets**
At the inception of a lease (e.g., on a date when the lessor places certain assets to the disposition of the lessee), the lessee should recognize and measure the right-of-use assets using the cost method, as follows:

- an amount equal to the lease liability;
- plus any amounts prepaid by the lessee on the date or prior to the date of the lease commencement, less any discounts granted by the lessor;
- plus any direct lease costs (costs that would not have been incurred had there been no lease, e.g., lease commissions); and
- plus estimated costs of dismantling, removal and/or restoration of assets to the specified condition.

**Initial recognition and measurement of the lease liability**
At the inception of a lease, lessees recognize lease liabilities in the amount of the present value of the minimum future lease payments (discounted value).

IFRS 16 was issued in January 2016 and is effective for the reporting periods beginning on or after January 1, 2019.

**First-time adoption impact**
Upon initial measurement, the new standard application resulted in increase in right-of-use assets by BAM 1,239 thousand and the lease liabilities (the aggregate principal amount) increased by BAM 1,181 thousand. In addition, the application of IFRS 16 will lead to reallocation of the previous leasing costs to the depreciation charge and costs of interest on the lease liabilities. The costs will be higher in the first years of the lease term, and they will decrease in the later periods in comparison to the previously effective IAS 17, due to the calculation of interest on the decreasing lease liability principal.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.13. Tangible Assets Acquired in Lieu of Debt Collection

The Bank occasionally acquires real estate and movable property in lieu of collection of certain loans and receivables.

In accordance with the relevant IAS and IFRS such assets are initially recognized at cost. After the initial recognition, these assets are stated at the lower of the following two values - cost and net realizable value. An impairment loss is recognized whenever the carrying amount of an asset exceeds its net realizable value. Impairment losses are recognized in the profit or loss statement for the year.

Gains and losses on the sales of such assets are recognized in the profit or loss statement for the year.

### 3.14. Impairment of Non-Financial Assets

All assets that are subject to depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Intangible assets that have an indefinite useful life are not subject to amortization and are tested for impairment whenever there are indications that these may be impaired or at least annually.

An impairment loss is recognized in the amount by which the carrying amount exceeds its recoverable amount. The recoverable amount is the higher of fair value less costs to sell and value in use.

Non-financial assets that are impaired are assessed at each reporting date for possible reversal of the impairment. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reduced up to the amount of the carrying value of the assets which does not exceed the carrying amount that would have been determined, net of accumulated depreciation/amortization, had the impairment loss not been accounted for.

### 3.15. Financial Liabilities Measured at Amortized Cost

***Deposits***

Transaction accounts and deposits are initially recognized at fair value, net of transaction costs. Subsequently, they are stated at their amortized cost, using the effective interest rate, and any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the profit or loss statement over the period of their utilization using the effective interest method.

***Borrowings***

Borrowings are initially recognized at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortized cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the profit or loss statement over the period of utilization using the effective interest method.

### 3.16. Provisions

Provisions for liabilities and charges are maintained at the level that the Bank's management considers sufficient for absorption of losses. The management determines the sufficiency of provisions based on considerations of into specific items, current economic circumstances, risk characteristics of certain transaction categories, as well as other relevant factors.

Provisions are released only for the expenditures for which they were initially recognized. If an outflow of economic benefits to settle the obligations is no longer probable, the provision is reversed.

Provisions for restructuring and damage claims/losses per legal suits filed are recognized when:

- the Group has a present legal or constructive obligation as a result of past events;
- it is more likely than not that an outflow of resources will be required to settle the obligation; and
- a reliable estimate can be made of the amount of the obligation.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 3.17. Issued (Share) Capital

Share capital consists of ordinary (common stock) shares. Share capital is stated at nominal value.

### 3.18. Dividends

Dividends are recognized as liabilities in the period wherein a decision on dividend disbursement is made by the Bank's shareholders.

### 3.19. Revaluation and Fair Value Reserves

***For Property, Equipment and Intangible Assets***

Revaluation surpluses are credited to revaluation reserves. When the carrying amount of an asset increases due to revaluation, such increase is to be included in equity as revaluation surplus (reserve). However, the increase is recognized in profit and loss to the extent that it reverses a revaluation decrease of the same asset previously recognized in profit or loss.

When an asset's carrying value decreases due to revaluation, such decrease is to be recognized as an expense. However, the decrease is to be charged within equity up to the amount of the existing (previously recorded) revaluation surplus relating to the asset.

***For Financial Assets at Fair Value through Other Comprehensive Income (FVtOCI)***

Reserves for financial assets at FVtOCI include fair value adjustments of such financial assets net of deferred taxes.

### 3.20. Earnings per Share

The Bank presents basic earnings per share. Basic earnings per share is calculated by dividing the profit or loss for the current period intended for ordinary shareholders by the weighted average number of ordinary shares outstanding during the year.

Since the Bank has no potentially dilutive ordinary shares such as convertible debt and options on shares, the Bank does not calculate diluted earnings per share.

### 3.21. Off-Balance Sheet Commitments and Contingent Liabilities

In the ordinary course of business, the Bank enters into off-balance sheet contingent liabilities recorded on the off-balance sheet accounts, which primarily include guarantees, letters of credit, undrawn loans and loans per credit cards. Such financial commitments are recorded in the statement of financial position, if and when they become payable.
Financial guarantees are contracts that require the Bank to undertake specific payments per guarantees to reimburse to the guarantee beneficiaries for the losses incurred due to inability of certain debtors to make the due payments in accordance with the terms of debt instruments.
Liabilities per guarantees issued are initially recognized at fair value, which is amortized over the validity period of the guarantee. Liabilities per guarantees are subsequently measured at amortized amount or the present value of expected payments (when a payment under the guarantee is likely), whichever is higher.

### 3.22. Segment Reporting

An operating segment represents a group of assets and business activities engaged in providing products or services that are subject to risks and returns that are different from those of other operating segments.

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

The Bank monitors its performance per operating segments and per geographical segments (branches) for the purposes of consolidated reporting. The geographical segment was not published due to the fact that the Bank's operations are concentrated in Bosnia and Herzegovina. Detailed information on the segments, as well as the structure and the result on each of the segments, is provided in Note 5.

## 4. KEY ACCOUNTING ESTIMATES AND ASSUMPTIONS

In the normal course of business, the Bank makes estimates and assumptions about uncertain events, including estimates and assumptions about the future. Such accounting assumptions and estimates are regularly reviewed and are based on historical experience and other factors such as the expected flow of future events that can be reasonably assumed in existing circumstances, but nevertheless necessarily represent sources of estimation uncertainty. The estimation of impairment losses in the Bank's credit risk portfolio represents the major source of estimation uncertainty. This and other key sources of estimation uncertainty, that have a significant risk of causing a possible material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below.

### 4.1 Impairment Losses on Loans and Receivables

The Bank monitors the credit rating of its customers on an ongoing basis. The need for impairment of the Bank's on-balance and off-balance sheet exposures to credit risk is assessed on a monthly basis, using available data. Impairment losses are made mainly against the carrying value of loans to corporate and retail customers and as provisions for contingent liabilities and commitments arising from off-balance exposure to customers, mainly in the form of undrawn framework loans, guarantees, letters of credit and other assets.

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

The Bank first assesses whether objective evidence of impairment exists individually for assets that are individually significant and collectively for assets that are not individually significant. However, assets assessed individually as unimpaired are then included in groups of assets with similar credit risk characteristics and then assessed collectively for impairment.

The Bank estimates impairment losses in cases where it judges that the observable data indicates the likelihood of a measurable decrease in the estimated future cash flows of the asset or a portfolio of assets. Such evidence includes delinquency in payments or other indications of financial difficulty of borrowers and adverse changes in the economic conditions in which borrowers operate or in the value or marketability of collateral, where these changes can be correlated with defaults.

Expected credit losses are calculated using the following formula:

$$ECL = \sum_{t=1}^{T} (PD_t \cdot EAD_t \cdot LGD_t)$$

(ECL = expected credit loss, PD = probability of default, LGD = loss given default).

Expected credit losses are calculated separately for each scenario used, where forward-looking information is taken into account and represent probability-weighted numbers. Thereafter, aggregation is performed.

- Loss Given Default (LGD)

The Bank estimates LGD value based on the difference between the contractual cash flows and the cash flows it expects to receive through recovery, including recovery from the collateral foreclosure cash flows. LGD is usually expressed as a percentage.

LGD is best modelled using individual elements (recovery rate percentage, collateral value, and the like).

- Probability of Default (PD)

Probability of default is a probability that a loan/receivable will default within a specific time period. Several approaches are used in modelling PDs for ECL calculation.

- Exposure at Default (EaD)

This is an estimate of the outstanding exposure at the time of default on a future date, where expected changes in the exposure after the reporting date are taken into account, including payments of principal and interest, as well as expected drawdowns of funds.

The first and foremost criterion for defining the type of impairment is determining whether an impairment trigger has occurred, as defined in the Bank's default and workout policy.

## 4. KEY ACCOUNTING ESTIMATES AND ASSUMPTIONS (Continued)

### 4.1 Impairment Losses on Loans and Receivables (Continued)

Loans of the borrowers that are not in the default status will be subject to portfolio (collective) impairment while the default-status loans will be subject to either individual or collective impairment and provisioning depending on the significance of the exposure at default (EaD) to their group of related entities. Special risk provisions represent impairment allowances of assets for the amounts expect not be collected upon contractually agreed maturity. The loss amount for which the remaining exposure is adjusted is a result of the gross exposure (on-balance and/or off-balance sheet) decreased by expected future cash flows discounted to their present value. Impairment losses on financial assets carried at amortized cost is calculated as the difference between the carrying value of assets and the present value of the expected future cash flows from such assets discounted at the original effective interest rate.
Stage3CI/STAGE3II represent a risk measure of identified losses (default on the obligation to make the payment) and can always be allocated to the individual loan facility.

### 4.2. Taxation

The Bank records tax liabilities in accordance with the tax laws of the Republic of Srpska. Tax returns are subject to the approval of the tax authorities who are entitled to carry out subsequent inspections of taxpayers' records. The interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Bank may not coincide with that of the management. As a result, transactions may be challenged by tax authorities and the Bank may be assessed additional taxes, penalties and interest, which can be significant. In accordance with the Law on the Tax Administration of the Republic of Srpska, expiration period of the tax liability is five years. This virtually means that tax authorities could determine payment of outstanding liabilities in the period of five years from the origination of the liability.

### 4.3. Regulatory Requirements

The Banking Agency of the Republic of Srpska is authorized to carry out regulatory inspections of the Bank's operations and to request changes to the carrying values of assets, liabilities and equity, in accordance with the underlying regulations.

### 4.4. Litigation

The Bank makes individual assessment of all court cases and makes the related provisions based on professional legal advice received.
As disclosed in Note 28, the Bank made provisions of BAM 2,568 thousand for litigations in 2019 (2018: BAM 1,863 thousand), which the management estimated as sufficient. In 2019, the number of lawsuits involving the Bank was further reduced as a result of the Bank's intensified activities of the legal risk management (adequate defense at court, and amicable settlement of disputes where possible, etc.).

### 4.5. Tangible Assets Acquired in Lieu of Debt Collection

The Bank occasionally acquires real estate in lieu of debt collection per certain loans and receivables. Real estate is stated at the lower of the net recoverable value of the related loan receivable and the current fair value of such assets less costs to sell. Gains or losses arising on disposal of such assets are recognized in the statement of profit or loss.

### 4.6. Employee Retirement Benefits

Long-term provisions related to the future outflows for retirement benefits are formed based on the actuarial calculation performed in accordance with IAS 19. For the purposes of the assessment, the Bank engages a certified actuary to perform the calculation based on the data from the Bank's HR Department records according to the estimated time of employees' retirement. The present value of the future liabilities is calculated by applying a discount rate. These provisions are only used to settle the expenses that the provisions have originally been made for. At each year-end, the Bank re-assesses these provisions. If the amount recorded is higher/lower than estimated amount, the difference is reflected through profit and loss, except in the event that such a difference is a result of actuarial assumptions, when it is presented within equity as actuarial gain or loss.

In December 2018, a certified actuary performed a new actuarial calculation as of December 31, 2018 in accordance with IAS 19. Following the new calculation, the Bank recorded a decrease in the previously recognized provisions by crediting actuarial gains within equity. An assessment of short-term provisions for unused annual leaves (vacations) is performed based on the number of days of unused vacation as of the statement of financial position date and the average monthly gross salary per employee.

## 4. KEY ACCOUNTING ESTIMATES AND ASSUMPTIONS (Continued)

### 4.7. Impairment of Financial Assets at FVtOCI

The Bank determines that the equity investments available-for-sale are impaired when there has been a significant and prolonged decrease in their fair value below their cost. Determining a significant and prolonged decrease demands estimates. Among other factors, the Bank estimates normal fluctuations in the prices of shares.

In addition, impairment may be appropriate when there is evidence of the deterioration of the sound financial standing of the investor, deterioration of the success of the industry or the sector as well as changes in technology and operating and financing cash flows.

### 4.7. Fair Value of Property, Equipment and Investment Property

Fair value of property, equipment and investment property is regularly assessed based on the market value of similar property situated at similar locations by certified appraisers. Fair value is determined by means of capitalization valuation method (income approach) that takes into account actual or realizable annual income from the property under valuation relative to the value of the underlying investment. The actual annual income is then decreased by the costs of maintenance, depreciation, taxes and risk of rent payment default or failure to lease property. Factors applied in the assessment are specific for the market of Bosnia and Herzegovina.

## 5. SEGMENT REPORTING

Segments recognized for reporting purposes in accordance with IFRS 8 include the following:

- Operations with the Retail segment, within which the following two sub-segments are recognized:
  - sub-segment of private individuals (PI) and
  - sub-segment of micro entities;
- Operations with the Corporate segment, within which three sub-segments are recognized: small, medium, and large entities;
- Operations with the Public segment – segment of public enterprises; and
- Treasury.

Since the Bank operates mainly in Bosnia and Herzegovina, secondary (geographical) segments are not presented.

## 5. SEGMENT REPORTING (Continued)

The tables below show the overall breakdown of the Bank's statement of profit and loss per segment:

| | RET | COR | PUB | TRE | OTH | Total |
|---|---|---|---|---|---|---|
| **Year Ended December 31, 2019** | | | | | | |
| Interest income calculated using the effective interest method | 22,646 | 6,739 | 1,625 | 731 | 2 | 31,743 |
| Other interest income | - | 10 | - | - | - | 10 |
| Interest expenses | (4,547) | (556) | (513) | (1,102) | - | (6,718) |
| **Net interest income** | **18,099** | **6,193** | **1,112** | **(371)** | **2** | **25,035** |
| | | | | | | |
| Fee and commission income | 13,137 | 2,495 | 141 | - | - | 15,773 |
| Fee and commission expenses | (2,861) | (363) | (26) | (3) | - | (3,253) |
| **Net fee and commission income** | **10,276** | **2,132** | **115** | **(3)** | **-** | **12,520** |
| Net profit from financial instruments | - | - | 39 | 278 | - | 317 |
| Other operating income | - | - | - | - | 2,367 | 2,367 |
| Other operating expenses | - | - | - | - | (4,637) | (4,637) |
| **Total operating income** | **28,375** | **8,325** | **1,266** | **(96)** | **(2,268)** | **35,602** |
| | | | | | | |
| Personnel expense | (8,823) | (1,659) | (205) | (192) | (1,293) | (12,172) |
| Depreciation/amortization charge | (2,619) | (492) | (61) | (57) | (384) | (3,613) |
| Other administrative costs | (9,113) | (1,713) | (211) | (198) | (1,335) | (12,570) |
| **Total operating expenses** | **(20,555)** | **(3,864)** | **(477)** | **(447)** | **(3,012)** | **(28,355)** |
| **Operating profit/(loss) before credit risk provisions** | **7,820** | **4,461** | **789** | **(543)** | **(5,280)** | **7,247** |
| Credit loss expense on financial assets | (3,601) | 826 | 1,447 | 785 | - | (543) |
| **PROFIT/(LOSS) BEFORE TAXES** | 4,219 | 5,287 | 2,236 | 242 | (5,280) | 6,704 |
| Income tax expense | - | - | - | - | 16 | 16 |
| **Net profit/(loss) for the year** | **4,219** | **5,287** | **2,236** | **242** | **(5,264)** | **6,720** |

## 5. SEGMENT REPORTING (Continued)

| | RET | COR | PUB | TRE | OTH | Total |
|---|---|---|---|---|---|---|
| **Year Ended December 31, 2018** | | | | | | |
| Interest income calculated using the effective interest method | 22,968 | 6,960 | 2,163 | 287 | (93) | 32,285 |
| Other interest income | - | 10 | - | - | - | 10 |
| Interest expenses | (4,676) | (609) | (953) | (813) | - | (7,051) |
| **Net interest income** | **18,292** | **6,361** | **1,210** | **(526)** | **(93)** | **25,244** |
| Fee and commission income | 12,634 | 2,443 | 148 | - | - | 15,225 |
| Fee and commission expenses | (2,190) | (620) | (25) | - | - | (2,835) |
| **Net fee and commission income** | **10,444** | **1,823** | **123** | **-** | **-** | **12,390** |
| Net profit from financial instruments | - | - | - | 91 | - | 91 |
| Other operating income | - | - | - | - | 2,819 | 2,819 |
| Other operating expenses | - | - | - | - | (3,699) | (3,699) |
| **Total operating income** | **28,736** | **8,184** | **1,333** | **(435)** | **(973)** | **36,845** |
| Personnel expense | (9,097) | (1,671) | (212) | (212) | (1,447) | (12,639) |
| Depreciation/amortization charge | (1,816) | (333) | (42) | (42) | (289) | (2,522) |
| Other administrative costs | (9,607) | (1,764) | (225) | (223) | (1,528) | (13,347) |
| **Total operating expenses** | **(20,520)** | **(3,768)** | **(479)** | **(477)** | **(3,264)** | **(28,508)** |
| **Operating profit/(loss) before credit risk provisions** | **8,216** | **4,416** | **854** | **(912)** | **(4,237)** | **8,337** |
| Credit loss expense on financial assets | (8,105) | 1,710 | 1,299 | - | 37 | (5,059) |
| **PROFIT/(LOSS) BEFORE TAXES** | 111 | 6,126 | 2,153 | (912) | (4,200) | 3,278 |
| Income tax expense | - | - | - | - | 7 | 7 |
| **Net profit/(loss) for the year** | **111** | **6,126** | **2,153** | **(912)** | **(4,193)** | **3,285** |

The table below shows the Bank's total assets and liabilities per segment:

| | RET | COR | PUB | TRE | OTH | Total |
|---|---|---|---|---|---|---|
| **December 31, 2019** | | | | | | |
| Total assets | 310,362 | 225,807 | 58,334 | 247,674 | - | 842,177 |
| Total liabilities | 439,248 | 117,541 | 63,189 | 60,998 | - | 680,976 |
| **31 December 31, 2018** | | | | | | |
| Total assets | 293,238 | 183,757 | 50,119 | 268,549 | - | 795,663 |
| Total liabilities | 426,503 | 125,776 | 72,544 | 16,379 | - | 641,202 |

# 6. FINANCIAL RISK MANAGEMENT

The risk management strategy of the Bank is to maintain stable performance in the future. The Bank possesses an internal risk management model. The most significant tools and methods used in the model for internal risk management are: internal credit rating system (for corporate and retail segments and banks), collaterals, internal indicators in respect of provisions/bad debts, etc. The use of risk management tools has a great impact on asset quality, liquidity structure, efficiency, ratios and early warnings, and reduce the Bank's exposure to all types of risk.

The Bank is exposed to the following major risks: credit risk, market risk, liquidity risk, and operational risks.

## 6.1. Credit Risk Management

The Bank is exposed to credit risk which is the risk of their inability to collect due loans and other receivables with interest accrued thereon within contractually defined terms.

The Bank manages credit risk through an ongoing analysis of the creditworthiness of existing and potential borrowers to pay their liabilities for principal and interest, and changes in indebtedness limits where necessary. This is performed in in accordance with the loan approval, additional lending and investment activity procedures in place and assumptions regarding contingent off-balance sheet liabilities. In addition, the Bank also manages its exposure to credit risk by minimizing any form of risk related to quality, concentration, collection securitization, maturity and currency.

The Bank has formed separate organizational units in charge of managing and controlling credit risk and the collection of bad debts aligned with the organizational chart used within Addiko Group. The Bank approves loans in accordance with the defined loan approval process bases on the borrower creditworthiness, i.e., solely based on the estimates of the borrower's sustainable cash flows as the primary source of loan repayment.

For every loan, there are several levels of authority for their approval, the highest of which is the Supervisory Board of the Bank. Loan approval decision are made (and the competent authority level determined) based on total liabilities/limits defined at the level of a group of related parties.

### 6.1.1 Management of Non-Performing Loans

NPL management is organized through the work of the Risk Management Department, i.e., through its two teams: Loan Restructuring and Workout, which is in charge of corporate (COR) and public sector (PUB) segments, and the Retail Collection Team in charge of the retail segment customers (including private individuals and entrepreneurs).

Non-performing (NPL status) loans are loans that over 90 days past due in repayment (materially significant past-due means that the liabilities exceed 2.5% of the total exposure and that the delay from entering the materially significant past-due status is longer than 90 days) or loans where borrowers have exhibited problems in business operations indicating borrowers' inability to discharge their liabilities from operations and evident risk of default. According to the local categorization these are exposures classified in C, D and E categories, or assets with special provisions in accordance with IFRS 9 (NPLs) with an internal rating of 5A or worse. Loans with internal ratings ranging from 4A to 4E (WL status) are additionally monitored with the active involvement of the Risk Management Department in order to minimize potential losses through active creation of the strategy for prevention of the customer transition to the default status.

The Loan Restructuring and Workout Team, is in charge of corporate and public segment clients (with all their related parties) with the status of over 90 days past due, with 5A or a worse rating and categories C, D and E within the local classification; transfer of customers from the Market Department is performed immediately upon fulfillment of these criteria. Prior to transfer to the Risk Management Department/Loan Restructuring and Workout Team, the Market Department prepares a Client Transfer Protocol and the credit committees are in charge of transfer approval. In addition, the Risk Management Department is entitled to assume other borrowing customers with ratings better than 5A in all instances where the Department estimates that the credit risk could deteriorate. The portfolio of credit rating 4 borrowers is monitored by the Monitoring Committee that considers the watch list status borrowers on a monthly basis and proposes measures for risk elimination and mitigation in order to prevent migrations to the NPL status.

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.1. Credit Risk Management (Continued)

#### 6.1.1 Management of Non-Performing Loans (Continued)

Upon identification of a client as a NPL client, the Risk Management Department/Loan Restructuring and Workout Team assumes competence and responsibility for the whole group of clients with the Bank as well as for defining collection strategy at the client group level.

Transfer of borrowing clients to the Risk Management Department is performed at the client group level, whereby all group members are allocated the credit rating of the worst group member. Exceptionally, the Department can assume on one group member or allocate different credit ratings to the group members; however, this must be explained, documented and approves by competent bodies.

After assuming clients, the Risk Management Department assumes functions of both the Market and Underwriting Departments, as it is responsible for borrowing client processing and monitoring, for proposing manners of resolution and manners of possible collection of the Bank's receivables to the competent Credit Committee, calculation of the credit risk at the client/loan facility levels under both local regulations and IFRS/IAS, for obtaining valid collateral appraisal, for borrower rating adjustments, for assessment and proposal of the amount of individually assessed loan loss provisions (the so-called SRP Stage 3), and for collection of receivables using all legal means available.

All the borrowers under the remit of the Risk Management Department/Loan Restructuring and Workout Functions are subject to the mandatory monitoring on a semi-annual basis in the form of a credit report, which is approved by the Credit Committees in line with their respective competences.

The Loan Restructuring and Workout Functions are parts of the Risk Management Department dealing with the early risk assessment, loan restructuring and all legal activities relating to enforced collection.

The Collection Department in charge of the retail clients – SMEs and individuals – whose liability settlement is one or more days past due and with debts matured amounting to EUR 10 (in BAM equivalent) in instances of private individuals (PI) and EUR 25 (in BAM equivalent) in instances of micro-sized entities.

The Collection Department “covers” all collection activities starting from the client's day 1 past due stats and includes late collection phases (90+, 180+ days past due), all legal procedures (including execution procedure) and repossession and re-sale of assets,

The process of collection from the Retail segment clients involves collection per all loan facilities with days past due, through the functions of:

- Client Recovery – while the client is in the category of up to 90 days past due it is considered recoverable, and all activities undertaken are focused on the recovery of the client and the return of the client back to the performing status; and
- Debt Collection – once the number of days past due per a single loan facility or a single borrower exceeds 90 days, client recovery is no longer deemed possible; accordingly, the focus shifts to minimizing the losses.

Early collection is the first and most important collection phase. The early collection strategy is based on the early and consistent contact with the borrowers.

The early collection procedure entails a combination of activities aimed at encouraging the borrower to settle liabilities immediately after their maturity: telephone calls and texting, delivery of written reminders, collateral activation, negotiations and attempts to find the best solution in the common interests of the Bank and the borrower. The goal of the restructuring activities here is to prevent new NPLs and contribute to the maintenance of the portfolio quality.

Late collection approach is intended to encourage and enable timely addressing of NPLs and set up a system for prevention of accumulation of NPLs. It is based on the following basic principles: more debt settlement, voluntary sales of assets preferred to the foreclosure of assets, avoidance of lawsuit instigation to claim smaller value debts, full outsourcing of unsecuritized receivables and minimum or (ideally) no instigation of lawsuits for debt collection, optimized use of resources with focus on the receivables with the highest possible recoveries, provision of a balance between the collection costs and the net present value of the collected amounts, clearing of the previous NPL portfolio, sales of assets acquired in lieu of debt collection through authorized real estate agencies, etc.

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.1. Credit Risk Management (Continued)

#### 6.1.2. Maximum Credit Risk Exposure

The table below shows the Bank's maximum exposure to credit risk, by the statement of the financial position items.

| Financial instruments at December 31, 2019 | Performing | | | Non-Performing | | | Total | | |
|---|---|---|---|---|---|---|---|---|---|
| | Exposure | S1 and S2 provisions | Net | Exposure | S3 provisions | Net | Exposure | Provisions | Net |
| Cash and balances held with the Central Bank[1)] | 77,935 | (25) | 77,910 | - | - | - | 77,935 | (25) | 77,910 |
| Balances held with other banks | 43,630 | (110) | 43,520 | - | - | - | 43,630 | (110) | 43,520 |
| **Loans and receivables** | **570,261** | **(14,235)** | **556,026** | **85,049** | **(73,643)** | **11,406** | **655,310** | **(87,878)** | **567,432** |
| Loans and receivables due from customers | 567,090 | (14,202) | 552,888 | 83,334 | (72,016) | 11,318 | 650,424 | (86,218) | 564,206 |
| Other financial assets | 3,171 | (33) | 3,138 | 1,715 | (1,627) | 88 | 4,886 | (1,660) | 3,226 |
| Investments in securities[2)] | 61,979 | (32) | 61,947 | - | - | - | 61,979 | (32) | 61,947 |
| **Total financial assets** | **753,805** | **(14,402)** | **739,403** | **85,049** | **(73,643)** | **11,406** | **838,854** | **(88,045)** | **750,809** |
| Off-balance sheet items | 119,350 | (771) | 118,579 | 123 | (82) | 41 | 119,473 | (853) | 118,620 |
| **Total credit risk exposure** | **873,155** | **(15,173)** | **857,982** | **85,172** | **(73,725)** | **11,447** | **958,327** | **(88,898)** | **869,429** |

| Financial instruments at December 31, 2018 | Performing | | | Non-Performing | | | Total | | |
|---|---|---|---|---|---|---|---|---|---|
| | Exposure | S1 and S2 provisions | Net | Exposure | S3 provisions | Net | Exposure | Provisions | Net |
| Cash and balances held with the Central Bank[1)] | 104,891 | (734) | 104,157 | - | - | - | 104,891 | (734) | 104,157 |
| Balances held with other banks | 58,568 | (121) | 58,447 | - | - | - | 58,568 | (121) | 58,447 |
| **Loans and receivables** | **510,127** | **(14,269)** | **495,858** | **89,926** | **(76,106)** | **13,820** | **600,053** | **(90,375)** | **509,678** |
| Loans and receivables due from customers | 507,320 | (14,214) | 493,106 | 88,682 | (74,892) | 13,790 | 596,002 | (89,106) | 506,896 |
| Other financial assets | 2,807 | (55) | 2,752 | 1,244 | (1,214) | 30 | 4,051 | (1,269) | 2,782 |
| Investments in securities[2)] | 55,017 | (118) | 54,899 | - | - | - | 55,017 | (118) | 54,899 |
| **Total financial assets** | **728,603** | **(15,242)** | **713,361** | **89,926** | **(76,106)** | **13,820** | **818,529** | **(91,348)** | **727,181** |
| Off-balance sheet items | 114,208 | (1,025) | 113,183 | 221 | (149) | 72 | 114,429 | (1,174) | 113,255 |
| **Total credit risk exposure** | **842,811** | **(16,267)** | **826,544** | **90,147** | **(76,255)** | **13,892** | **932,958** | **(92,522)** | **840,436** |

1) The line item does not include cash in the amount of BAM 25,789 thousand.
2) The line item does not include equity investments in the amount of BAM 229 thousand.

The maximum exposure is presented without deducting the value of any underlying collateral.

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.1. Credit Risk Management (Continued)

### 6.1.2. Loans and Receivables Due from Customers – the Rating System

The Bank's rating system is presented in accordance with the internal rating scale of Addiko Group (five rating classes and five levels within each class). The probability of default (PD) of a certain client, whose rating has been assigned within the internal Addiko Group's rating scale, is expressed through the internal ratings, as follows:

- Rating Class 1 (ratings of 1A - 1E), which includes customers from the best to the very good credit worthiness;
- Rating Class 2 (ratings of 2A - 2E), which includes clients from good to moderate credit worthiness;
- Rating Class 3 (ratings of 3A - 3E), which include clients from acceptable to insufficient creditworthiness;
- Rating Class 4 (ratings of 4A - 4E) comprising of customers under surveillance measures, as a result of short-term or long-term indicators of business difficulties, in a particular client or within a certain industry;
- Rating Class 5 (ratings of 5A - 5E), which includes clients where there is a significant delay in the payment obligations or a significant doubt about client's creditworthiness.

The Bank's credit risk exposure arising from loans and receivables due from customers and banks and balances with other banks, by category, is provided below:

| | December 31, 2019 | | | |
|---|---|---|---|---|
| | Exposure | S1 and S2 provisions | S3 provisions | Net |
| No rating | 1,349 | (16) | (16) | 1,317 |
| 1A-1E | 137,945 | (195) | - | 137,750 |
| 2A-2E | 261,412 | (1,369) | (32) | 260,011 |
| 3A-3E | 170,157 | (2,997) | (103) | 167,057 |
| 4A-4E | 40,721 | (9,733) | (631) | 30,357 |
| 5A-5E | 82,470 | (2) | (71,234) | 11,234 |
| **Total** | **694,054** | **(14,312)** | **(72,016)** | **607,726** |

| | December 31, 2018 | | | |
|---|---|---|---|---|
| | Exposure | S1 and S2 provisions | S3 provisions | Net |
| No rating | 2,708 | (72) | (151) | 2,485 |
| 1A-1E | 156,291 | (818) | - | 155,473 |
| 2A-2E | 219,315 | (2,719) | (11) | 216,585 |
| 3A-3E | 147,855 | (4,325) | (40) | 143,490 |
| 4A-4E | 40,592 | (6,384) | (532) | 33,676 |
| 5A-5E | 87,809 | (17) | (74,158) | 13,634 |
| **Total** | **654,570** | **(14,335)** | **(74,892)** | **565,343** |

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.1. Credit Risk Management (Continued)

### 6.1.3. Loans and Receivables Due from Customers – Performance Breakdown

| | 2019 | 2018 |
|---|---|---|
| Neither past due nor impaired | 565,094 | 504,722 |
| Past due but not impaired | 1,996 | 2,598 |
| Impaired (non-performing) | 83,334 | 88,682 |
| **Total, gross** | **650,424** | **596,002** |
| S3 provisions | (72,016) | (74,892) |
| S1 and S2 provisions | (14,202) | (14,214) |
| **Total, net** | **564,206** | **506,896** |

*Neither past-due nor impaired loans*

Neither past-due nor impaired loans and receivables based on the segment structure can be summarized as follows:

| | 2019 | 2018 |
|---|---|---|
| Public sector | 16,554 | 26,137 |
| Non-banking financial institutions | 14,433 | 15,880 |
| Corporate customers | 215,450 | 162,703 |
| Entrepreneurs | 9,809 | 11,057 |
| Retail - individuals | 308,720 | 288,786 |
| Other | 128 | 159 |
| | 565,094 | 504,722 |

*Past-due but not impaired loans*

Past due but not impaired loans and receivables, by the segment structure and days past due, can be summarized as follows:

| December 31, 2019 | Up to 30 days | 30 - 60 days | 60 - 90 days | 90 - 180 days | Over 180 days | Total |
|---|---|---|---|---|---|---|
| Public sector | - | - | - | - | - | - |
| Non-banking financial institutions | - | - | - | - | - | - |
| Corporate customers | 1 | - | - | - | - | 1 |
| Entrepreneurs | - | - | - | - | - | - |
| Retail - individuals | 1,520 | 361 | 114 | - | - | 1,995 |
| Other | - | - | - | - | - | - |
| | 1,521 | 361 | 114 | - | - | 1,996 |

| December 31, 2018 | Up to 30 days | 30 - 60 days | 60 - 90 days | 90 - 180 days | Over 180 days | Total |
|---|---|---|---|---|---|---|
| Public sector | - | - | - | - | - | - |
| Non-banking financial institutions | - | - | - | - | - | - |
| Corporate customers | 73 | - | - | - | - | 73 |
| Entrepreneurs | - | - | - | - | - | - |
| Retail - individuals | 1,983 | 298 | 244 | - | - | 2,525 |
| Other | - | - | - | - | - | - |
| | 2,056 | 298 | 244 | - | - | 2,598 |

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.1. Credit Risk Management (Continued)

### 6.1.3. Loans and Receivables Due from Customers – Performance Breakdown (Continued)

*Impaired loans*

Impaired loans with the fair value of related collateral, held by the Bank as security instruments, may be summarized as follows:

| | Public sector | Non-banking financial institutions | Corporate | Entrepre-neurs | Retail | Other | Total |
|---|---|---|---|---|---|---|---|
| **December 31, 2019** | | | | | | | |
| **Exposure** | 4,337 | - | 7,343 | 504 | 71,145 | 5 | 83,334 |
| Stage 3 provisions | (1,289) | - | (5,500) | (461) | (64,761) | (5) | (72,016) |
| **Net** | 3,048 | - | 1,843 | 43 | 6,384 | - | 11,318 |
| Collateral fair value | 2,096 | - | 3,857 | 154 | 23,778 | - | 29,885 |

| | Public sector | Non-banking financial institutions | Corporate | Entrepre-neurs | Retail | Other | Total |
|---|---|---|---|---|---|---|---|
| **December 31, 2018** | | | | | | | |
| **Exposure** | 4,886 | - | 12,154 | 525 | 71,112 | 5 | 88,682 |
| Stage 3 provisions | (1,674) | - | (9,589) | (474) | (63,152) | (3) | (74,892) |
| **Net** | **3,212** | **-** | **2,565** | **51** | **7,960** | **2** | **13,790** |
| Collateral fair value | 2,057 | - | 5,203 | 184 | 27,579 | - | 35,023 |

### 6.1.4. Rescheduled and Restructured Receivables

A restructured loan is a loan that is refinances, rescheduled or otherwise converted, i.e., a loan in which, due to the borrower's changed conditions and repayment capabilities, or its inability to make repayment in line with initially agreed repayment schedule or because of the revised (lower) current market rate, the previously agreed deadlines (period or repayment schedule) and/or other terms and conditions have subsequently been altered so that the Bank can allow the borrower easier (and for the Bank itself more secure) debt servicing.

Breakdown of the Bank's restructured and refinanced loans, at December 31, 2019 and 2018 is provided below:

| | Number of renegotiated loans | Amount |
|---|---|---|
| **December 31, 2019** | | |
| Corporate clients | - | - |
| Retail clients - individuals and entrepreneurs | 24 | 985 |
| **Total** | **24** | **985** |
| **December 31, 2018** | | |
| Corporate clients | - | - |
| Retail clients - individuals and entrepreneurs | 62 | 1,330 |
| **Total** | **62** | **1,330** |

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.1. Credit Risk Management (Continued)

#### 6.1.5. Loans and Receivables Due from Customers - Concentration per Industry

The breakdown of the Group's and the Bank's financial assets exposed to credit risk per industry on the gross and net bases (net of provisions) is shown in the following table:

| | 2019 Amount | 2019 % | 2018 Amount | 2018 % |
|---|---|---|---|---|
| Retail customers | 395,147 | 47.0% | 376,318 | 45.9% |
| Trade | 47,900 | 5.7% | 58,067 | 7.1% |
| Mining and industry | 77,830 | 9.2% | 70,105 | 8.5% |
| Services, tourism and catering business | 11,907 | 1.4% | 3,819 | 0.5% |
| Transport and communications | 11,637 | 1.4% | 4,179 | 0.5% |
| Real estate trade | 409 | 0.0% | 2,283 | 0.3% |
| Agriculture, forestry and fishing | 3,819 | 0.5% | 3,840 | 0.5% |
| Construction industry | 28,587 | 3.4% | 6,613 | 0.8% |
| Financial institutions | 169,125 | 20.1% | 220,590 | 26.9% |
| Power industry | 34,965 | 4.2% | 22,048 | 2.7% |
| Administration and other public services | 52,806 | 6.3% | 46,958 | 5.7% |
| Other | 6,541 | 0.8% | 5,155 | 0.6% |
| Allowance for impairment | (88,013) | | (91,230) | |
| Collected fees not recognized within income | (1,851) | | (1,564) | |
| | 750,809 | | 727,181 | |

The amounts presented in the table above do not include cash in the amount of BAM 48,098 thousand and equity securities of BAM 229 thousand (2018: BAM 25,789 thousand and BAM 229 thousand, respectively).

#### 6.1.6. Off-Balance Sheet Items

The contractual amounts of the Bank's off-balance sheet financial liabilities that it has committed to extend to customers are summarized in the table below:

| | Up to 1 year | 1 - 5 years | Over 5 years | Total |
|---|---|---|---|---|
| **December 31, 2019** | | | | |
| Irrevocable loan commitments | 23,008 | 36,204 | 17,578 | **76,790** |
| Payment and performance guarantees and letters of credit | 7,255 | 37,174 | 695 | **45,124** |
| | **30,263** | **73,378** | **18,273** | **121,914** |
| **December 31, 2018** | | | | |
| Irrevocable loan commitments | 25,710 | 28,899 | 16,975 | **71,584** |
| Payment and performance guarantees and letters of credit | 10,517 | 31,332 | 996 | **42,845** |
| | **36,227** | **60,231** | **17,971** | **114,429** |

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.2. Market Risk Management

The Bank is exposed to market risk which is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risks arise from open positions in interest rate, 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.

*General Requirements*

The Bank develops its market risk strategy on the basis of strategic discussions between the competent units of Treasury and Risk Controlling. Decisions on combined business and risk strategies are only made by the Asset and Liability Management Committee (ALCO).

As part of the daily reporting procedure, the management receives value-at-risk (VaR) and performance figures for trading transactions on a daily basis and figures on the banking book investments and market risk steering on a weekly basis. There is also a daily report to the Management in which the key risk and performance figures of the branches are communicated. In these, the value-at-risk at the branch level is compared to the defined limits. Limit breaches initiate defined escalation processes up to the Executive Board level.

*Risk Measurement*

The principal tool used to measure and control market risk exposure within the Bank's trading portfolio is value-at-risk (VaR). VaR of a trading portfolio is the estimated loss that will arise on the portfolio over a specified period of time (holding period) given an adverse movement with a specified probability (confidence level). The model is based upon a 99% confidence level, assumes a 1 day holding period and takes into account 250 historical scenarios. The use of a 99% confidence level means that losses exceeding the VaR figure should occur, on average, not more than once every 100 days.
The Bank uses VaR to measure the following market risks:

- general interest rate risk in the banking book;
- foreign exchange risk on the statement of financial position level (both trading and banking books);
- equity and debt securities risk in the trading book;
- credit spread risk.

The Bank's VaR per risk type for years 2019 and 2018:

| | Minimum | Maximum | Monthly average | December 31 |
|---|---|---|---|---|
| **2019** | | | | |
| Interest rate risk | 62 | 141 | 103 | 141 |
| Foreign currency risk | 2 | 16 | 10 | 10 |
| Price risk | - | - | - | - |
| Credit spread risk | 18 | 122 | 60 | 18 |
| **Total** | **82** | **279** | **173** | **169** |
| **2018** | | | | |
| Interest rate risk | 40 | 106 | 89 | 40 |
| Foreign currency risk | 3 | 16 | 7 | 16 |
| Price risk | - | - | - | - |
| Credit spread risk | - | 68 | 6 | 68 |
| **Total** | **43** | **190** | **102** | **124** |

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.3. Foreign Currency Risk

Foreign currency risk is the Bank's exposure to possible impact of change in foreign currency exchange rate and danger that unfavorable changes may result in loss denominated in BAM (local currency). The level of risk is a function of height and length of the Bank's exposure to possible changes in foreign exchange rates, and depends on the amount of the Bank's borrowing in foreign currencies and the degree of alignment of assets and liabilities of the Bank's balance sheet and off-balance sheet, i.e., the degree of matching of the foreign currency flows.

Foreign currency risk exposure arises from credit, deposit, investment and trading activities. It is controlled daily in accordance with legislation and the internally set limits for each currency and for the assets and liabilities denominated in foreign currencies. During the year open currency positions were maintained within the limits prescribed by the Decisions of the Banking Agency of the Republic of Srpska and the internal limits set according to the Addiko Group's methodology. Currency matching of the financial assets and financial liabilities is maintained by selling and purchasing all currencies, by contracting deposits and approving loans with currency clause index and by monitoring such loans. Foreign currency risk management activities and responsibilities are defined by the program, policies and procedures for foreign currency risk management.

*Sensitivity Analysis*

The following table indicates the currencies to which the Bank had significant exposures at December 31, 2018 and 2017. The position in euros was not analyzed since BAM is pegged to EUR.

| Currency | FX Open position, December 31, 2019 | 10% increase | 10% decrease | FX Open position, December 31, 2018 | 10% increase | 10% decrease |
|---|---|---|---|---|---|---|
| USD | 1,301 | 227 | (227) | 1,720 | 294 | (294) |
| CHF | 643 | 116 | (116) | 9 | 2 | (2) |

FX open position represents net exposure in a foreign currency. The analysis calculates the effect of a reasonably predictable movements of the currencies against BAM and their influence on the profit or loss, with all other variables held constant. Negative values in the table reflect a potential net reduction of the profit, while positive amounts reflect a net potential increase.

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.3. Foreign Currency Risk (Continued)

Loans and receivables extended in BAM with contracted currency clause are presented within the appropriate foreign currency buckets.

The Bank had the following significant currency positions:

| | EUR | USD | CHF | Other currencies | FX Sub-total | BAM Sub-total | Total |
|---|---|---|---|---|---|---|---|
| **December 31, 2019** | | | | | | | |
| **ASSETS** | | | | | | | |
| Cash and balances held with the Central Bank | - | - | - | 24,051 | 24,051 | 101,957 | 126,008 |
| Balances held with other banks | (25) | 6,992 | - | 36,553 | 43,520 | - | 43,520 |
| Financial assets held for trading | - | - | - | - | - | 1 | 1 |
| Loans and receivables | 318,522 | (19) | 89,800 | 17 | 408,320 | 159,112 | 567,432 |
| Loans and receivables due from customers | 317,158 | - | 89,800 | 17 | 406,975 | 157,231 | 564,206 |
| Other financial assets | 1,364 | (19) | - | - | 1,345 | 1,881 | 3,226 |
| Investments in securities | 61,965 | - | - | - | 61,965 | 211 | 62,176 |
| Property and equipment | - | - | - | - | - | 28,174 | 28,174 |
| Land, buildings and equipment | - | - | - | - | - | 25,673 | 25,673 |
| Investment property | - | - | - | - | - | 2,501 | 2,501 |
| Intangible assets | - | - | - | - | - | 6,561 | 6,561 |
| Tax assets | - | - | - | - | - | 1,424 | 1,424 |
| Receivables for prepaid income taxes | - | - | - | - | - | 1,424 | 1,424 |
| Assets held for sale | - | - | - | - | - | 592 | 592 |
| Other assets | 361 | 32 | - | - | 393 | 5,896 | 6,289 |
| **Total assets** | **380,823** | **7,005** | **89,800** | **60,621** | **538,249** | **303,927** | **842,177** |
| **LIABILITIES** | | | | | | | |
| Financial liabilities held for trading | - | - | - | - | - | 3 | **3** |
| Financial liabilities measured at amortized cost | 126,873 | 9,568 | 153,933 | 85,112 | 375,486 | 297,158 | 672,644 |
| Deposits due to banks | 32,347 | - | - | 1 | 32,348 | 15,644 | 47,992 |
| Deposits due to customers | 33,188 | 9,568 | 152,602 | 85,111 | 280,469 | 277,092 | 557,561 |
| Borrowings | 56,196 | - | - | - | 56,196 | - | 56,196 |
| Other financial liabilities | 5,142 | - | 1,331 | - | 6,473 | 4,422 | 10,895 |
| Other provisions | 63 | 177 | - | - | 240 | 3,601 | 3,841 |
| Tax liabilities | - | - | - | - | - | 440 | 440 |
| Deferred tax liabilities | - | - | - | - | - | 440 | 440 |
| Other liabilities | 64 | - | - | 4 | 68 | 3,980 | 4,048 |
| **Total liabilities** | **127,000** | **9,745** | **153,933** | **85,116** | **375,794** | **305,182** | **680,976** |
| **Net foreign currency position** | **253,823** | **(2,740)** | **(64,133)** | **(24,495)** | **162,455** | **(1,255)** | **161,201** |

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.3. Foreign Currency Risk (Continued)

| | EUR | USD | CHF | Other currencies | FX Sub-total | BAM Sub-total | Total |
|---|---|---|---|---|---|---|---|
| **December 31, 2018** | | | | | | | |
| **ASSETS** | | | | | | | |
| Cash and balances held with the Central Bank | 9,067 | 554 | 585 | 1,092 | 11,298 | 118,648 | 129,946 |
| Balances held with other banks | 42,636 | 11,034 | 2,460 | 2,317 | 58,447 | - | 58,447 |
| Loans and receivables | 372,695 | - | 4,058 | 1 | 376,754 | 132,924 | 509,678 |
| Loans and receivables due from customers | 371,914 | - | 4,058 | 1 | 375,973 | 130,923 | 506,896 |
| Other financial assets | 781 | - | - | - | 781 | 2,001 | 2,782 |
| Investments in securities | 52,896 | - | - | - | 52,896 | 2,232 | 55,128 |
| Property and equipment | - | - | - | - | - | 29,080 | 29,080 |
| Land, buildings and equipment | - | - | - | - | - | 26,679 | 26,679 |
| Investment property | - | - | - | - | - | 2,401 | 2,401 |
| Intangible assets | - | - | - | - | - | 5,874 | 5,874 |
| Tax assets | - | - | - | - | - | 1,395 | 1,395 |
| Receivables for prepaid income taxes | - | - | - | - | - | 1,395 | 1,395 |
| Assets held for sale | - | - | - | - | - | 545 | 545 |
| Other assets | 263 | - | - | - | 263 | 5,307 | 5,570 |
| **Total assets** | **477,557** | **11,588** | **7,103** | **3,410** | **499,658** | **296,005** | **795,663** |
| **LIABILITIES** | | | | | | | |
| Financial liabilities measured at amortized cost | 343,698 | 9,868 | 7,093 | 2,196 | 362,855 | 269,932 | 632,787 |
| Deposits due to banks | 21,618 | 1 | - | - | 21,619 | 9,731 | 31,350 |
| Deposits due to customers | 263,265 | 9,867 | 7,086 | 2,191 | 282,409 | 257,836 | 540,245 |
| Borrowings | 52,512 | - | - | - | 52,512 | - | 52,512 |
| Other financial liabilities | 6,303 | - | 7 | 5 | 6,315 | 2,365 | 8,680 |
| Other provisions | 438 | 1 | - | - | 439 | 3,410 | 3,849 |
| Tax liabilities | - | - | - | - | - | 582 | 582 |
| Deferred tax liabilities | - | - | - | - | - | 582 | 582 |
| Other liabilities | 333 | - | - | - | 333 | 3,651 | 3,984 |
| **Total liabilities** | **344,469** | **9,869** | **7,093** | **2,196** | **363,627** | **277,575** | **641,202** |
| **Net foreign currency position** | **133,088** | **1,719** | **10** | **1,214** | **136,031** | **18,430** | **154,461** |

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.4. Interest Rate Risk Management

Interest rate risk represents the possibility of a decrease in planned or expected yield on interest-bearing or interest rate sensitive positions due to a change in interest rates and/or yield on the capital market.

Interest rate risks arise when assets or liabilities transactions are in a mismatch with the funds and/or capital investments when it comes to concordance rates and maturity dates. In case there is an excess of fixed interest rate on assets, an increasing interest rate would, for example, have a negative effect on the present value of the bank and/or on net interest revenue. The same consequences would happen if there was a decrease in the fixed interest rate on the liabilities side.

The following table shows the sensitivity of the current portfolio value to a reasonable change in interest rates (parallel movement), with all other variables constant. The amounts are stated in thousands of BAM.

| | Interest rates changes | Sensitivity | Interest rates changes | Sensitivity |
|---|---|---|---|---|
| **December 31, 2019** | | | | |
| BAM | +/-100 bp | 6,510/(7,092) | +/-200 bp | 12,494/(14,828) |
| EUR | +/-100 bp | (5,871)/6,339 | +/-200 bp | (11,317)/13,204 |
| CHF | +/-100 bp | (21)/22 | +/-200 bp | (42)/45 |
| USD | +/-100 bp | (1)/1 | +/-200 bp | (2)/2 |
| Other | +/-100 bp | -/- | +/-200 bp | (1)/1 |
| **Total** | | **617/(730)** | | **1,132/(1,576)** |
| **December 31, 2018** | | | | |
| BAM | +/-100 bp | 2,180/(2,380) | +/-200 bp | 4,181/(4,982) |
| EUR | +/-100 bp | (2,255)/2,534 | +/-200 bp | (4,267)/5,391 |
| CHF | +/-100 bp | (29)/30 | +/-200 bp | (57)/62 |
| USD | +/-100 bp | -/- | +/-200 bp | -/- |
| Other | +/-100 bp | -/- | +/-200 bp | -/- |
| **Total** | | **(104)/184** | | **(143)/471** |

### 6.5. Liquidity Risk Management

The Bank defines liquidity risk as the risk of not being able to meet due payment obligations on time or in full amount; or – in the event of a liquidity crisis – only being able to procure refinancing at increased market rates; or only being able to sell assets at a discount to market prices.

The main objective of liquidity risk management and control is to ensure that the Bank maintains the capacity to make payments and undertake refinancing activities at any time.

Monitoring of liquidity risk is carried out, on one hand, on the basis of the liquidity ratio and "time-to-wall" key indicators (maximum liquidity time horizon), under normal and stress conditions, and on the other hand, through the integration of the structural liquidity risk into overall Bank control (risk-bearing capacity).

Limits for short-term liquidity as well as for the limitation of long-term structural liquidity have been set, both at the Bank level and for the individual branches, and are monitored constantly. To ensure that existing liquidity gaps can be closed at any time through the mobilization of the liquidity potential, threshold values are being defined for all scenarios and if these are exceeded, measures must be introduced to reduce the identified liquidity risks.

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.5. Liquidity Risk Management (Continued)

*Maturity Analysis*

The following tables show the analysis of the Banks's assets and liabilities by maturity based on the remaining period from the statement of financial position date to the agreed due date:

| | Up to 1 month | 1 - 3 months | 3 - 12 months | Over 1 year | Total |
|---|---|---|---|---|---|
| **December 31, 2019** | | | | | |
| **ASSETS** | | | | | |
| Cash and balances held with the Central Bank | 126,008 | - | - | - | 126,008 |
| Balances held with other banks | 43,520 | - | - | - | 43,520 |
| Financial assets held for trading | 1 | - | - | - | 1 |
| Loans and receivables | **21,717** | **32,626** | **121,731** | **391,358** | **567,432** |
| Loans and receivables due from customers | 18,577 | 32,626 | 121,731 | 391,272 | 564,206 |
| Other financial assets | 3,140 | - | - | 86 | 3,226 |
| Investments in securities | 62,171 | - | - | 5 | 62,176 |
| Property and equipment | - | - | - | 28,174 | 28,174 |
| Land, buildings and equipment | - | - | - | 25,673 | 25,673 |
| Investment property | - | - | - | 2,501 | 2,501 |
| Intangible assets | - | - | - | 6,561 | 6,561 |
| Tax assets | - | - | - | 1,424 | 1,424 |
| Receivables for prepaid income taxes | - | - | - | 1,424 | 1,424 |
| Assets held for sale | - | - | 592 | - | 592 |
| Other assets | 4,098 | - | - | 2,191 | 6,289 |
| **Total** | **257,515** | **32,626** | **122,323** | **429,713** | **842,177** |
| **LIABILITIES** | | | | | |
| Financial liabilities held for trading | 3 | - | - | - | 3 |
| Financial liabilities measured at amortized cost | **274,527** | **35,997** | **197,133** | **164,987** | 672,644 |
| Deposits due to banks | 4,852 | 11,944 | 17,617 | 13,579 | 47,992 |
| Deposits due to customers | 258,421 | 21,879 | 171,729 | 105,532 | 557,561 |
| Borrowings | 359 | 2,174 | 7,787 | 45,876 | 56,196 |
| Other financial liabilities | 10,895 | - | - | - | 10,895 |
| Other provisions | 1,567 | 151 | 265 | 1,858 | 3,841 |
| Tax liabilities | - | - | - | 440 | 440 |
| Deferred tax liabilities | - | - | - | 440 | 440 |
| Other liabilities | 3,967 | - | - | 81 | 4,048 |
| **Total** | 280,064 | 36,148 | 197,398 | 167,366 | 680,976 |
| **Maturity mismatch** | **(22,549)** | **(3,522)** | **(75,075)** | **262,347** | **161,201** |

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.5. Liquidity Risk Management (Continued)

*Maturity Analysis (Continued)*

| | Up to 1 month | 1 - 3 months | 3 - 12 months | Over 1 year | Total |
|---|---|---|---|---|---|
| **December 31, 2018** | | | | | |
| **ASSETS** | | | | | |
| Cash and balances held with the Central Bank | 129,946 | - | - | - | 129,946 |
| Balances held with other banks | 58,447 | - | - | - | 58,447 |
| Loans and receivables | **40,714** | **31,731** | **88,674** | **348,559** | **509,678** |
| Loans and receivables due from customers | 38,003 | 31,731 | 88,674 | 348,488 | 506,896 |
| Other financial assets | 2,711 | - | - | 71 | 2,782 |
| Investments in securities | 53,121 | - | 2,002 | 5 | 55,128 |
| Property and equipment | - | - | - | 29,080 | 29,080 |
| Land, buildings and equipment | - | - | - | 26,679 | 26,679 |
| Investment property | - | - | - | 2,401 | 2,401 |
| Intangible assets | - | - | - | 5,874 | 5,874 |
| Tax assets | - | - | - | 1,395 | 1,395 |
| Receivables for prepaid income taxes | - | - | - | 1,395 | 1,395 |
| Assets held for sale | - | - | 545 | - | 545 |
| Other assets | 3,314 | - | - | 2,256 | 5,570 |
| **Total** | **285,542** | **31,731** | **91,221** | **387,169** | **795,663** |
| **LIABILITIES** | | | | | |
| Financial liabilities measured at amortized cost | **333,620** | **16,373** | **82,923** | **199,871** | **632,787** |
| Deposits due to banks | 10,549 | 1,500 | 4,900 | 14,401 | 31,350 |
| Deposits due to customers | 314,073 | 14,205 | 72,200 | 139,767 | 540,245 |
| Borrowings | 318 | 668 | 5,823 | 45,703 | 52,512 |
| Other financial liabilities | 8,680 | - | - | - | 8,680 |
| Other provisions | 912 | 578 | 474 | 1,885 | 3,849 |
| Tax liabilities | - | - | - | 582 | 582 |
| Deferred tax liabilities | - | - | - | 582 | 582 |
| Other liabilities | 3,898 | - | - | 86 | 3,984 |
| **Total liabilities** | **338,430** | **16,951** | **83,397** | **202,424** | **641,202** |
| **Maturity mismatch** | **(52,888)** | **14,780** | **7,824** | **184,745** | **154,461** |

The table below shows the remaining undiscounted maturities of the Bank's financial liabilities as at December 31, 2019 and 2018:

| | Up to 1 month | 1-3 months | 3-12 months | Over 1 year | Total | Net carrying value |
|---|---|---|---|---|---|---|
| **December 31, 2019** | | | | | | |
| Deposits due to banks | 4,919 | 24,660 | 4,901 | 13,579 | 48,059 | 47,992 |
| Deposits due to customers | 344,950 | 23,365 | 87,642 | 107,308 | 563,265 | 557,561 |
| Borrowings | 525 | 2,289 | 8,505 | 48,151 | 59,470 | 56,196 |
| Other financial liabilities | 10,895 | - | - | - | 10,895 | 10,895 |
| **Total** | **361,289** | **50,314** | **101,048** | **169,038** | **681,689** | **672,644** |

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.5. Liquidity Risk Management (Continued)

*Maturity Analysis (Continued)*

| | Up to 1 month | 1-3 months | 3-12 months | Over 1 year | Total | Net carrying value |
|---|---|---|---|---|---|---|
| **December 31, 2018** | | | | | | |
| Deposits due to banks | 10,591 | 1,500 | 4,900 | 14,401 | 31,392 | 31,350 |
| Deposits due to customers | 315,890 | 12,720 | 77,072 | 143,156 | 548,838 | 540,245 |
| Borrowings | 459 | 767 | 10,085 | 44,713 | 56,024 | 52,512 |
| Other financial liabilities | 8,680 | - | - | - | 8,680 | 8,680 |
| **Total** | **335,620** | **14,987** | **92,057** | **202,270** | **644,934** | **632,787** |

### 6.6. Fair Value of Financial Assets and Liabilities

The fair value of financial assets and financial liabilities that are traded in the active markets can be measured based on quoted market prices or dealer quotes. For all other financial instruments, the Bank determines fair value using other valuation techniques.

The Bank measures the fair value using the following fair value hierarchy that reflects the significance of input parameters, used in the measurement:

- Level 1 inputs: quoted market prices (unadjusted) in an active market for identical assets.
- Level 2 inputs: inputs other than quoted prices included in Level 1 that are based on observable inputs, either directly or indirectly for the relevant asset or liability. This category includes instruments measured using: quoted market prices in active markets for similar instruments, quoted prices for identical or similar instruments that are considered less than active or other measurement techniques, in which all of the significant inputs, directly or indirectly, are observable from market data.
- Level 3 inputs: unobservable inputs. This category includes all instruments for which measurement techniques are not observable and these parameters have a significant impact on the assessment of the value of the instruments. This category includes instruments that are measured based on quoted prices for similar products that require significant adjustments or assumptions to reflect differences between the instruments.

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.6. Fair Value of Financial Assets and Liabilities (Continued)

The fair values of the Bank's assets and liabilities, at levels in accordance with IFRS 13, can be summarized as follows:

| December 31, 2019 | Carrying value | Fair value total | Difference | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|---|---|
| ***Financial assets carried at fair value*** | | | | | | |
| Financial assets held for trading | 1 | 1 | - | 1 | - | - |
| Investments in securities | 62,176 | 62,176 | - | 61,942 | 5 | 229 |
| ***Financial assets other than carried at fair value*** | | | | | | |
| Cash and balances held with the Central Bank | 126,008 | 126,008 | - | - | - | 126,008 |
| Balances held with other banks | 43,520 | 43,520 | - | - | - | 43,520 |
| Loans and receivables | **567,432** | **622,856** | **55,424** | **-** | **-** | **622,856** |
| Loans and receivables due from customers | 564,206 | 619,630 | 55,424 | - | - | 619,630 |
| Other financial assets | 3,226 | 3,226 | - | - | - | 3,226 |
| Property and equipment | 28,174 | 28,174 | - | - | - | 28,174 |
| Intangible assets | 6,561 | 6,561 | - | - | - | 6,561 |
| Assets held for sale | 592 | 592 | - | - | - | 592 |
| **Total** | **834,464** | **889,888** | **55,424** | **61,943** | **5** | **827,940** |
| **LIABILITIES** | | | | | | |
| ***Financial liabilities carried at fair value*** | | | | | | |
| Financial liabilities held for trading | 3 | 3 | - | 3 | - | - |
| ***Financial liabilities other than carried at fair value*** | | | | | | |
| Financial liabilities at amortized cost | **672,644** | **681,199** | **8,555** | **-** | **-** | **681,199** |
| Deposits due to banks | 47,992 | 48,744 | 752 | - | - | 48,744 |
| Deposits due to customers | 557,561 | 563,569 | 6,008 | - | - | 563,569 |
| Borrowings | 56,196 | 57,991 | 1,795 | - | - | 57,991 |
| Other financial liabilities | 10,895 | 10,895 | - | - | - | 10,895 |
| **Total** | **672,647** | **681,202** | **8,555** | **3** | **-** | **681,199** |

| December 31, 2018 | Carrying value | Fair value total | Difference | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|---|---|
| ***Financial assets carried at fair value*** | | | | | | |
| Financial assets held for trading | - | - | - | - | - | - |
| Investments in securities | 55,128 | 55,128 | - | 52,872 | 2,027 | 229 |
| ***Financial assets other than carried at fair value*** | | | | | | |
| Cash and balances held with the Central Bank | 129,946 | 129,946 | - | - | - | 129,946 |
| Balances held with other banks | 58,447 | 58,447 | - | - | - | 58,447 |
| Loans and receivables | 509,678 | 523,662 | 13,984 | - | - | 523,662 |
| Loans and receivables due from customers | 506,896 | 520,880 | 13,984 | - | - | 520,880 |
| Other financial assets | 2,782 | 2,782 | - | - | - | 2,782 |
| Property and equipment | 29,080 | 29,080 | - | - | - | 29,080 |
| Intangible assets | 5,874 | 5,874 | - | - | - | 5,874 |
| Assets held for sale | 545 | 545 | - | - | - | 545 |
| **Total** | **788,698** | **802,682** | **13,984** | **52,872** | **2,027** | **747,783** |
| **LIABILITIES** | | | | | | |
| ***Financial liabilities carried at fair value*** | | | | | | |
| Financial liabilities held for trading | - | - | - | - | - | - |
| ***Financial liabilities other than carried at fair value*** | | | | | | |
| Financial liabilities at amortized cost | 632,787 | 644,304 | 11,517 | - | - | 644,304 |
| Deposits due to banks | 31,350 | 31,350 | - | - | - | 31,350 |
| Deposits due to customers | 540,245 | 551,762 | 11,517 | - | - | 551,762 |
| Borrowings | 52,512 | 52,512 | - | - | - | 52,512 |
| Other financial liabilities | 8,680 | 8,680 | - | - | - | 8,680 |
| **Total** | **632,787** | **644,304** | **11,517** | **-** | **-** | **644,304** |

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.6. Fair Value of Financial Assets and Liabilities (Continued)

By definition fair value is the value a third party is willing to pay for a contract in an arm's length transaction. In order to calculate the fair market value, the future cash flows must be discounted to their present value where there are cash flows clearly defined by the terms of the contract. The Investor is willing to assume the contract if the contract compensates fairly the price per all risks included in the contract. This means that the investor demands an adequate rate of return that covers all the risks. Accordingly, the investor will discount all future cash flows using this return rate to arrive at the present value that the investor is willing to pay for the contract. The present value arrived at in this manner guarantees the investor the required annual rate of return and represents the fair value:

$$FV_l = \sum_{i=1}^{T} \frac{CF_i}{(1 + RRR_i^l)^i}$$

$FV$ fair value of loan l
T maturity of the loan
$CF_n$ cash flows (principal and interest) as per loan agreement
$RRR_n^l$ rate of return per investor for the maturity n and loan l

The required rate of return:

$$RRR_n = r_n + s_n^l + (1 - cr_l)fc_n + cc_l \cdot ec^l$$

$r_n$ risk-free interest for the currency of the loan l and maturity of the cash flows
$s_n^l$ n- annual premium for idiosyncratic credit risk aligned with the risk of the country of debtor's origin
$fc_n$ funding spread
$ec^l$ pre-tax excess equity cost
$cr_l$ percentage share of the contract coverage by capital, which represents an economic capital requirement for each contract.

The following table presents movements in the financial assets carried at fair value within Level 3 of the fair value hierarchy:

| | Banja Luka Stock Exchange | Central Securities Register | S.W.I.F.T. | Total |
|---|---|---|---|---|
| Balance at January 1, 2019 | 175 | 30 | 24 | 229 |
| Increase in the year | - | - | - | - |
| Decrease in the year | - | - | - | - |
| Change in revaluation reserves | - | - | - | - |
| Sales | - | - | - | - |
| **Balance at December 31, 2019** | **175** | **30** | **24** | **229** |
| Balance at January 1, 2018 | 175 | 30 | 24 | 229 |
| Increase in the year | - | - | - | - |
| Decrease in the year | - | - | - | - |
| Change in revaluation reserves | - | - | - | - |
| Sales | - | - | - | - |
| **Balance at December 31, 2018** | **175** | **30** | **24** | **229** |

During 2019, there were no reclassifications between the Levels.

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.7. Operational Risks

Operational risk management is an important part of the Bank’s operations, which allows their long-term successful business and the preservation of reputation.

As part of operational risk framework, the Bank implements the following activities:

- definition and identification of operational risk;
- development and application of methods and systems for measurement, analysis, limitations and control of operational risks in accordance with regulatory and requirements of Addiko Group;
- measurement, analysis and supervision of operational risk in line with minimum standards for operational risk management;
- maintenance of database on losses from operational risks – regular data collection and reporting on loss events;
- regular updates of the existing and development of new policies, manuals and procedures in accordance with regulatory and requirements of Addiko Group;
- performing qualitative estimates (scenario analyses and risk assessment) in order to identify and assess risk in business processes;
- education of all employees in order to improve their knowledge and experience, awareness and skills in dealing with operational risk or specific processes (e.g. collection of data on losses, risk assessment);
- development of the internal control system through the process of mapping all the relevant SIK processes within the Bank, by definition of their owners, recognition of risks arising within a process, adequate alleviation of those risks and testing operating effectiveness of the controls in place;
- assessment and establishment of adequate operational risk management upon development of new products; and
- assessment of the risk of outsourcing and management of outsourced activities within the Bank in collaboration with organizational units that are owners of the outsourced activities.

### 6.8. Capital Risk Management

In accordance with the effective Law on Banks, the minimum amount of a bank’s paid-in capital to be maintained at all times must not be below BAM 15,000 thousand. The Bank’s subscribed capital amounted to BAM 153,049 thousand in line with these provisions.

Pursuant to the new Decision on Bank Capital Calculation enacted by the Banking Agency of the Republic of Srpska (“BARS”) in 2017, the Bank’s capital is comprised of regulatory capital as the sum of the Bank’s core capital and supplementary capital after the regulatory adjustments:
- The Bank's core capital is the sum of the regular core capital and additional core capital after regulatory adjustments;
- The Bank's supplementary capital is comprised of the equity instruments and subordinated debts, share premium accounts, general provisions for credit losses and other items after regulatory adjustments.

Regular core capital items include: equity instruments if the recognition criteria are met for them, share premium accounts relating to the equity instruments, retained earnings, other comprehensive income, other reserves and reserves for general banking risks.

The Bank deducts from the regular core capital items the following: loss for the current financial year, unabsorbed prior years' losses, intangible assets, deferred tax assets depending on the future profitability, all tax expenses relating to the regular core capital items predictable at the time of the item calculation, investments into the Bank's own equity instruments (e.g., redeemed treasury shares), the amount of the Bank's qualified interest in a non-FSI entity, and free delivery (settlement) risk and other legally prescribed items if they arise during the banking operations.

The Bank's additional core capital is comprised of additional core capital items less the regulatory adjustments and application of the temporary exemption of the regulatory capital deductibles.

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.8. Capital Risk Management (Continued)

The Bank deducts from the additional core capital items the following: the Bank's direct and indirect investments into own additional core capital instruments, including those instruments that would be subject to the Bank's purchase obligation under the existing contractual commitments, the Bank's direct and indirect investments in additional core capital instruments of a FSI entity if the entity has a reciprocal investment into the Bank, which the Agency believes to have been made with a view to artificial increase in the regulatory capital, the amount of direct or indirect Bank's investment into the additional core capital instruments of a FSI entity if the Bank holds a significant interest therein, the amount of direct or indirect Bank's investment into the additional core capital instruments of a FSI entity if the Bank holds no significant interest therein, excluding items that, as the issue underwriter, it has held for no more than five working days, the amount of items to be deducted from the supplementary capital that exceed the Bank's supplementary capital, tax liabilities relating to the additional core capital items predictable at the time of the item calculation, unless the Bank adequately adjusts the amount of the additional core capital items to the extent that such tax liabilities may reduce their amount

The Bank's supplementary capital is comprised of the supplementary capital items less the regulatory adjustments and application of the temporary exemption of the regulatory capital deductibles. The supplementary capital may not exceed a half of the core capital, and as from July 26, 2018 it may not exceed one third of the core capital

The supplementary capital items include: paid equity instruments and subordinated debts recognized as supplementary capital items, share issue premium accounts, and general provisions for credit losses maximum up to 1.25% of the amount of the risk-weighted exposures

Equity instruments and subordinated debts meeting the inclusion criteria may be included in the supplementary capital only after the Bank has obtained a prior approval from the Agency.

The Bank deducts from the supplementary capital items the following: the Bank's direct or indirect investments in its own supplementary capital instruments, including its own supplementary capital instruments subject to a potential purchase obligation under the existing contractual commitments, the Bank's investments in the supplementary capital instruments of a FSI entity if the entity has a reciprocal investment into the Bank, which the Agency believes to have been made with a view to artificial increase in the regulatory capital, the Bank's direct or indirect investments in the supplementary capital instruments of a FSI entity if the Bank holds a significant interest therein, the amount of direct or indirect Bank's investment into the supplementary capital instruments of a FSI entity if the Bank holds no significant interest therein, excluding items that, as the issue underwriter, it has held for no more than five working days.

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.8. Capital Risk Management (Continued)

The table below provides the Bank's capital structure for the purpose of calculation of the Bank's capital adequacy ratio in accordance with the Decision on Bank Capital Calculation enacted by the Banking Agency of the Republic of Srpska (“BARS”):

| | 2019 | 2018 |
|---|---|---|
| ***Core capital*** | | |
| Equity instruments recognized as the regular core capital | 153,094 | 153,094 |
| Retained earnings | (62,220) | (65,564) |
| Other comprehensive income | 1,209 | 63 |
| (-) Other intangible assets | (6,560) | (5,874) |
| Other reserves | 61,351 | 56,819 |
| **Regular core capital** | **146,874** | **138,538** |
| **Additional core capital** | **-** | **-** |
| **Total core capital** | **146,874** | **138,538** |
| ***Supplementary capital*** | | |
| **Total supplementary capital** | 2,872 | 6,404 |
| **Total regulatory capital** | **149,746** | **144,942** |
| ***Risk exposures*** | | |
| Risk-weighted exposures for credit risk, financial derivatives exposure to credit risk and free delivery (settlement) risk | 568,710 | 512,299 |
| Total exposures to the position risk, currency and commodity risks | 38,432 | 4,507 |
| Total operational risk exposure | 76,816 | 74,730 |
| **Total risk exposures** | **683,958** | **591,536** |
| Ratio of the regular core capital | 21.47% | 23.42% |
| Regular core capital surplus | 100,707 | 98,609 |
| Core capital ratio | 21.47% | 23.42% |
| Core capital surplus | 85,318 | 85,300 |
| Regulatory capital ratio | 21.89% | 24.50% |
| Regulatory capital surplus | 67,671 | 73,958 |

As of December 31, 2019 and 2018 all the Bank's capital ratios were in compliance with the regulatory requirements. From the foregoing it is evident that the Bank has a solid capital position.

With regard to capital risk management, the Bank aims to:
- provide compliance with BARS requirements;
- provide compliance with Addiko Group standards;
- provide solid capital basis as a support for further development of Bank’s operations;
- provide possibilities of long-term business operation while ensuring profit for shareholders.

The Bank’s management monitors adequacy ratios and other performance indicators on a regular basis. Reports on indicators are submitted to the Banking Agency of the Republic of Srpska quarterly in the prescribed form.

## 6. FINANCIAL RISK MANAGEMENT (Continued)

### 6.8. Capital Risk Management (Continued)

The Bank manages capital and performs reconciliations in accordance with its goals, market changes and risks typical for Bank's operations.

Up to 2010, the Bank calculated and recorded provisions for credit risks in accordance with the regulatory rules prescribed by BARS.

In 2010, with the mandatory implementation of the newly adopted IAS 39, the regulatory rules were amended. The new rules required lower amounts of provisions compared to the previous (regulatory) methodology. As a result of the new standard implementation, the Bank credited reversal of the said provisions to the account of other reserves as "shortfall provisions from profit for estimated losses" in the amount of BAM 61,826 thousand.

On January 1, 2018, upon first-time adoption of IFRS 9 (wit mandatory implementation as from January 1, 2019), the aforesaid amount was reduced by BAM 475 thousand, which led to a decrease in the balance of the reserves for credit losses as per regulatory requirements by BAM 61,351 thousand.

On December 19, 2018, BARS issued the Decision on the Conditions for Inclusion of the Formed Reserves for Credit Losses into the Regular Core Capital of Banks (Official Gazette of RS no. 117/2018), whereby conditions are prescribed that banks need to fulfill in order to recognize the reserves for credit losses as the regular core capital item in accordance with the Decision on Bank Capital Calculation.

The aforesaid BARS Decision dated December 19, 2018 prescribes two conditions the Bank must fulfill:

- Submit to BARS a decision of the Bank's Shareholder Assembly on inclusion of the formed reserves for credit losses into the Bank's regular core capital, i.e., a decision on the allocation of the formed reserves to an appropriate item of its regular core capital in accordance with Article 6, para. 1 of the Decision on Bank Capital Calculation;
- Previously reduce the amount of the formed reserves for credit losses by any predictable costs in accordance with the effective tax legislation.

The Bank believes that the remaining balance of BAM 61,351 thousand on the account of the reserves for credit losses per regulatory requirement is tax exempt given the fact that, in years prior to the implementation of the Decision on the Minimum Standards for Credit Risk Management and Classification of Assets in Banks, these reserves for credit losses increased the Bank's taxable income so, unless tax exempt, there would be double taxation.

Considering all the aforesaid, on December 27, 2018, the Bank's Shareholder Assembly enacted Decision no. 01-1-22786/2018 on inclusion of the formed reserves for credit losses into the other reserves.

Due to the inclusion of the formed reserves for credit losses into the other reserves the Bank's regulatory capital increased by BAM 56,819 thousand as BAM 4,532 thousand remained as the balance of the reserves for credit losses as per regulatory requirements.

On April 30, 2019, the Bank's Shareholder Assembly enacted Decision no. S-9/2019 on inclusion of the remaining reserves for credit losses amounting to BAM 4,532 thousand into the other reserves.

Capital management entails ongoing monitoring and the measures that the Bank may take to maintain the legally prescribed ratios and limits include the following:
- adjustments of dividend payments to shareholders, i.e., increase of the share capital from profit allocation;
- increase of the capital reserves from profit allocation;
- new issues of shares, which can be private and public;
- increase of the supplementary capital items.

Given the Bank's rather high capital adequacy ratio, the Bank does not anticipate the need to increase the capital, but in the event that the Bank needs to take measures in order to comply with the effective regulations, the Bank's owner demonstrated the willingness to support the Bank.

## 7. INTEREST INCOME AND EXPENSES

| | Year Ended December 31, 2019 | 2018 |
|---|---|---|
| **Interest income calculated using the effective interest method** | **31,743** | **32,285** |
| Financial assets at FVtOCI | 564 | 148 |
| Financial assets at amortized cost (AC) | 31,179 | 32,137 |
| **Other interest income** | **10** | **10** |
| Dividend income | 10 | 10 |
| **Total interest income** | **31,753** | **32,295** |
| Financial liabilities at amortized cost (AC) | (6,447) | (6,836) |
| Other liabilities | (25) | - |
| Negative interest on financial assets | (246) | (215) |
| **Total interest expenses** | **(6,718)** | **(7,051)** |
| **Net interest income** | **25,035** | **25,244** |

### 7.1. Interest Income

*a) Interest Income - Breakdown per Source*

| | Year Ended December 31, 2019 | 2018 |
|---|---|---|
| **Bonds** | **564** | **148** |
| Public sector (Government) | 40 | 121 |
| Banks | 524 | 27 |
| **Loans and receivables** | **31,025** | **32,011** |
| Public sector (Government) | 1,222 | 1,764 |
| Public companies | 1,043 | 944 |
| Non-banking financial institutions | 533 | 357 |
| Corporate customers - private companies | 5,545 | 5,962 |
| Entrepreneurs | 359 | 396 |
| Retail customers - individuals | 22,296 | 22,548 |
| Non-residents | - | - |
| Other entities | 27 | 40 |
| Cash and balances held with the Central Bank | - | - |
| Balances held with other banks | 154 | 126 |
| Dividend income | 10 | 10 |
| | **31,753** | **32,295** |

*b) Interest Income - Breakdown per Product*

| | Year Ended December 31, 2019 | 2018 |
|---|---|---|
| Loans and receivables due from customers | 30,504 | 31,390 |
| Credit cards | 521 | 621 |
| Bonds | 564 | 148 |
| Balances held with other banks | 154 | 126 |
| Cash and balances held with the Central Bank | - | - |
| Dividend income | 10 | 10 |
| | **31,753** | **32,295** |

## 7. INTEREST INCOME AND EXPENSES (Continued)

### 7.2. Interest Expenses

*a) Interest Expenses – Breakdown per Source*

| | Year Ended December 31, 2019 | 2018 |
|---|---|---|
| **Deposits** | **5,337** | **5,912** |
| Public sector (Government) | 63 | 356 |
| Public companies | 70 | 120 |
| Banks | 36 | 164 |
| Non-banking financial institutions | 373 | 438 |
| Corporate customers - private companies | 181 | 176 |
| Entrepreneurs | - | 1 |
| Retail customers – individuals | 4,530 | 4,636 |
| Non-residents | - | - |
| Other entities | 84 | 21 |
| Negative interest on financial assets | 246 | 215 |
| Interest per lease liabilities | 25 | - |
| Other liabilities | - | - |
| Borrowings | **1,110** | **924** |
| Banks | 343 | 260 |
| Non-banking financial institutions | 767 | 664 |
| | **6,718** | **7,051** |

*b) Interest Expenses – Breakdown per Product*

| | Year Ended December 31, 2019 | 2018 |
|---|---|---|
| Current accounts and deposits of customers | 5,301 | 5,748 |
| Current accounts and deposits of banks | 36 | 164 |
| Negative interest on financial assets | 246 | 215 |
| Borrowings | 1,110 | 924 |
| Other liabilities | 25 | - |
| | **6,718** | **7,051** |

## 8. FEE AND COMMISSION INCOME AND EXPENSES

### 8.1. Fee and Commission Income

| | Year Ended December 31, 2019 | 2018 |
|---|---|---|
| Fee income arising from domestic payment transfers | 6,592 | 6,411 |
| Fees earned on VISA card operations | 2,923 | 3,341 |
| Fee income arising from international payment transfers | 1,851 | 1,686 |
| Fee income from currency conversion operations | 1,656 | 1,325 |
| Charges for early loan repayment, reminders and other loan fees | 752 | 739 |
| Commission from issued guarantees, letters of credit and other sureties | 623 | 597 |
| Brokerage commissions | - | 1 |
| Insurance fees and commissions | 964 | 733 |
| Other fee and commission income | 412 | 392 |
| | **15,773** | **15,225** |

## 8. FEE AND COMMISSION INCOME AND EXPENSES (Continued)

### 8.1. Fee and Commission Income (Continued)

In accordance with the requirements of IFRS 15, fee and commission income may be presented as follows:

| | Year Ended December 31, 2019 | 2018 |
|---|---|---|
| Account maintenance fees | 5,702 | 5,541 |
| Transaction processing fees and commissions | 3,002 | 2,974 |
| Card operation fees and charges | 2,061 | 2,313 |
| Lending operation fees | 731 | 706 |
| Fees for issue of guarantees, letters of credit and other sureties | 634 | 595 |
| Fees per securities | - | - |
| Insurance fees | 964 | 739 |
| Currency conversion operation fees and commissions | 2,645 | 2,076 |
| Other fees and commissions | 34 | 281 |
| | **15,773** | **15,225** |

### 8.2. Fee and Commission Expenses

| | Year Ended December 31, 2019 | 2018 |
|---|---|---|
| Fee expenses incurred on payment card operations | 1,628 | 1,722 |
| Fees for loans, issued guarantees and other fees | 264 | 296 |
| Fee expenses incurred on domestic payment transfers | 362 | 312 |
| Fee expenses incurred on international payment transfers | 348 | 145 |
| Fee expenses incurred on stock exchange operations and Central Register fees | 96 | 74 |
| Fee expenses per funds available for liquidity maintenance | 44 | 44 |
| Other fee and commission expenses | 511 | 242 |
| | **3,253** | **2,835** |

In accordance with the requirements of IFRS 15, fee and commission expenses may be presented as follows:

| | Year Ended December 31, 2019 | 2018 |
|---|---|---|
| Account maintenance fees | 337 | 242 |
| Transaction processing fees and commissions | 625 | 321 |
| Card operation fees and charges | 1,628 | 1,687 |
| Fees per securities – customer bonuses | 122 | 108 |
| Other fee and commission expenses | 541 | 477 |
| | **3,253** | **2,835** |

## 9. NET PROFIT FROM FINANCIAL INSTRUMENTS

| | Year Ended December 31, 2019 | 2018 |
|---|---|---|
| Profit on the financial assets held for trading (FVtPL) | (19) | (23) |
| Profit on the financial assets at FVtOCI | 364 | - |
| Foreign exchange gains/(losses) | (28) | 114 |
| | **317** | **91** |

## 10. OTHER OPERATING INCOME

| | Year Ended December 31, 2019 | 2018 |
|---|---|---|
| Reversal of provisions for litigations | 525 | 812 |
| Gains on the sales and value adjustments of tangible assets acquired in lieu of debt collection | 502 | 826 |
| Rental income | 385 | 405 |
| Write-off of liabilities | 136 | 543 |
| Write-off of liabilities due to close of dormant accounts | 2 | - |
| Gains on appraisal | 305 | - |
| Sales of consultancy services | 44 | 5 |
| Capital gains on the sales of acquired tangible assets, property and equipment | 7 | - |
| Other income | 461 | 228 |
| | **2,367** | **2,819** |

## 11. OTHER OPERATING EXPENSES

| | Year Ended December 31, 2019 | 2018 |
|---|---|---|
| Fees payable to the Deposit Insurance Agency of RS costs | 1,299 | 1,138 |
| Provisions for litigations | 1,292 | 767 |
| Fees payable to the Banking Agency of RS | 644 | 604 |
| Litigation costs and court fees | 191 | 405 |
| Fees payable to the other regulatory institutions | 555 | 385 |
| Losses on appraisal | 191 | - |
| Disposals and write-offs of property and equipment | 20 | 19 |
| Other expenses | 445 | 381 |
| | **4,637** | **3,699** |

## 12. PERSONNEL EXPENSE

| | Year Ended December 31, 2019 | 2018 |
|---|---|---|
| Net salaries | 7,087 | 7,064 |
| Payroll taxes and contributions | 4,318 | 4,351 |
| Other employee benefits | 538 | 649 |
| Reversal of provisions for retirement benefits/unused annual leaves | (365) | (11) |
| Provisions for employee bonuses | 594 | 586 |
| | **12,172** | **12,639** |

Other employee benefits include the cost of employee commuting allowances, paid recreation hours, insurance and other forms of employee benefits.

## 13. OTHER ADMINISTRATIVE EXPENSES

| | Year Ended December 31, 2019 | 2018 |
|---|---|---|
| Software maintenance costs | 2,360 | 3,842 |
| Property insurance and security | 1,040 | 1,036 |
| Telecommunications | 1,201 | 1,266 |
| Cost of materials, fuel, energy and services | 1,051 | 951 |
| Indirect taxes and contributions | 941 | 887 |
| Advertising, marketing and entertainment | 1,169 | 1,084 |
| Rental costs | 731 | 1,392 |
| Maintenance | 2,711 | 1,236 |
| Non-material costs | 234 | 165 |
| Intellectual services rendered by related banks | 253 | 246 |
| Consulting services | 143 | 58 |
| Membership fees and commissions | - | 116 |
| Per diems and other travel costs | 185 | 239 |
| Sponsorship and humanitarian aid projects | 99 | 141 |
| Other expenses | 452 | 688 |
| | **12,570** | **13,347** |

## 14. CREDIT LOSS EXPENSE ON FINANCIAL ASSETS

| | Year Ended December 31, 2019 | 2018 |
|---|---|---|
| Cash and balances held with the Central Bank (Note 16) | 709 | 234 |
| Balances held with other banks (Note 17) | 11 | (102) |
| Loans and receivables due from customers (Note 18.1) | (1,284) | (4,465) |
| Other financial assets (Note 18.2) | (428) | (322) |
| Investments in securities (Note 19) | 86 | (26) |
| Contingent liabilities and commitments (Note 28) | 323 | 85 |
| Recovery of the receivables previously written off | 496 | 164 |
| Write-offs | (456) | (627) |
| | **(543)** | **(5,059)** |

## 15. INCOME TAXES

### *a) Components of Income Taxes*

| | 2019 | 2018 |
|---|---|---|
| Current tax on income | - | - |
| Deferred tax benefits | (16) | (7) |
| | **(16)** | **(7)** |

### *b) Reconciliation between tax expense and profit before taxes multiplied by the applicable tax rate*

| | 2019 | 2018 |
|---|---|---|
| Profit before taxes | 6,705 | 3,278 |
| Income taxes at the statutory tax rate of 10% | 671 | 328 |
| ***Adjustments*** | | |
| Tax effects of expenses not recognized for tax purposes | 248 | 152 |
| Tax effects of income not recognized for tax purposes | (185) | (198) |
| Tax effects of recognized credit loss expense on financial assets | (63) | 314 |
| Non-deductible entertainment costs | 1 | 1 |
| Non-deductible default interest | 11 | 3 |
| Tax effects of non-deductible depreciation charge | 39 | (80) |
| Tax effects of provisions for employee benefits | (31) | (21) |
| Utilization of tax losses carried forward | (691) | (499) |
| Reversal of deferred tax (liabilities)/assets | (16) | (7) |
| **Income tax expense** | **(16)** | **(7)** |
| ***Effective tax rate*** | **0.24%** | **0.21%** |

## 15. INCOME TAXES (Continued)

### *b) Reconciliation between tax expense and profit before taxes multiplied by the applicable tax rate (Continued)*

The Bank's taxable income amounted to BAM 6,912 thousand for FY 2019. The Bank eliminated the taxable income amount using the same amount of the tax losses carried forward from prior periods. The remaining gross tax losses of BAM 228 thousand will be available for elimination or reduction of the Bank's taxable profits in the ensuing years. A tax loss is available for carryforward within five years from inception (the aforesaid amount can be used up to December 31, 2021).

### *c) Deferred Taxes*

The following table shows items for which deferred tax assets and liabilities were formed:

| | 2019 | 2018 |
|---|---|---|
| **Deferred tax liabilities** | | |
| Revaluation reserves from property and equipment | (100) | (242) |
| Property and equipment - different tax and accounting depreciation rates | (340) | (340) |
| | (440) | **(582)** |
| **Deferred tax liabilities, net** | (440) | **(582)** |

Movements on the Bank's deferred taxes were as follows:

| | January 1, 2019 | Recognized in the profit or loss | Recognized in other comprehensive income | December 31, 2019 | Deferred tax assets | Deferred tax liabilities |
|---|---|---|---|---|---|---|
| Revaluation reserves from property and equipment | (242) | 16 | 126 | (100) | - | (100) |
| Property and equipment - different tax and accounting rates | (340) | - | - | (340) | - | (340) |
| | **(582)** | **16** | **126** | **(440)** | **-** | **(440)** |

| | January 1, 2018 | Recognized in the profit or loss | Recognized in other comprehensive income | December 31, 2018 | Deferred tax assets | Deferred tax liabilities |
|---|---|---|---|---|---|---|
| Revaluation reserves from property and equipment | (249) | 7 | - | (242) | - | (242) |
| Property and equipment - different tax and accounting rates | (340) | - | - | (340) | - | (340) |
| | **(589)** | **7** | **-** | **(582)** | **-** | **(582)** |

## 16. CASH AND BALANCES HELD WITH THE CENTRAL BANK

| | 2019 | 2018 |
|---|---|---|
| Cash funds | | |
| - in local currency | 24,047 | 14,491 |
| - in foreign currencies | 24,051 | 11,298 |
| Balances with the Central Bank (BAM) | | |
| - obligatory reserve | 15,352 | 45,137 |
| - gyro account | 62,583 | 59,754 |
| *Less:* Impairment allowance | (25) | (734) |
| | **126,008** | **129,946** |

## 16. CASH AND BALANCES HELD WITH THE CENTRAL BANK (Continued)

The obligatory reserve represents amounts required to be deposited with the Central Bank of Bosnia and Herzegovina. Pursuant to the Decision of the Central Bank of Bosnia and Herzegovina, starting from August 31, 2016, the required reserve represents 10% of average balance of liabilities per deposits and borrowings irrespective of their maturities.

The required reserve is maintained as the average balance on the current account with the Central Bank of Bosnia and Herzegovina. This reserve is available for liquidity purposes. The Bank pays a fee of 5% on the required reserve surplus funds held on the account with the Central Bank.

Movements on the Bank's gross exposure in 2019 and 2018 were as follows:

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Gross exposure at January 1, 2019** | 130,680 | - | - | - | 130,680 |
| Change in the gross exposure | (4,647) | - | - | - | (4,647) |
| of which, increase | 22,309 | - | - | - | 22,309 |
| of which, decrease | (26,956) | - | - | - | (26,956) |
| of which, transfers among Stages | - | - | - | - | - |
| Write-offs | - | - | - | - | - |
| Originated or purchased assets | - | - | - | - | - |
| Derecognized assets | - | - | - | - | - |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Gross exposure at December 31, 2019** | **126,033** | **-** | **-** | **-** | **126,033** |

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Gross exposure at January 1, 2018** | 121,863 | - | - | - | 121,863 |
| Change in the gross exposure | 8,817 | - | - | - | 8,817 |
| of which, increase | 82,776 | - | - | - | 82,776 |
| of which, decrease | (73,959) | - | - | - | (73,959) |
| of which, transfers among Stages | - | - | - | - | - |
| Write-offs | - | - | - | - | - |
| Originated or purchased assets | - | - | - | - | - |
| Derecognized assets | - | - | - | - | - |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Gross exposure at December 31, 2018** | **130,680** | **-** | **-** | **-** | **130,680** |

## 16. CASH AND BALANCES HELD WITH THE CENTRAL BANK (Continued)

Movements on the impairment allowance/provisions in 2019 and 2018 were as follows:

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Provisions at January 1, 2019** | (734) | - | - | - | (734) |
| Change in the provisions | 709 | - | - | - | 709 |
| of which, transfers among Stages | - | - | - | - | - |
| of which, increase | - | - | - | - | - |
| of which, decrease | 709 | - | - | - | 709 |
| of which, effects on the interest income | - | - | - | - | - |
| Write-offs | - | - | - | - | - |
| Modification effect not resulting in derecognition of assets | - | - | - | - | - |
| Originated or purchased assets | - | - | - | - | - |
| Derecognized assets | - | - | - | - | - |
| Model/parameter changes | - | - | - | - | - |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Provisions at December 31, 2019** | **(25)** | **-** | **-** | **-** | **(25)** |

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Provisions at January 1, 2018** | (968) | - | - | - | (968) |
| Change in the provisions | 234 | - | - | - | 234 |
| of which, transfers among Stages | - | - | - | - | - |
| of which, increase | - | - | - | - | - |
| of which, decrease | 234 | - | - | - | 234 |
| of which, effects on the interest income | - | - | - | - | - |
| Write-offs | - | - | - | - | - |
| Modification effect not resulting in derecognition of assets | - | - | - | - | - |
| Originated or purchased assets | - | - | - | - | - |
| Derecognized assets | - | - | - | - | - |
| Model/parameter changes | - | - | - | - | - |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Provisions at December 31, 2018** | **(734)** | **-** | **-** | **-** | **(734)** |

## 17. BALANCES HELD WITH OTHER BANKS

| | 2019 | 2018 |
|---|---|---|
| Foreign currency accounts held with foreign and domestic banks | 36,637 | 51,223 |
| Short-term deposits placed for periods of up to 7 days | 6,993 | 7,345 |
| Foreign currency cheques in the course of collection | - | - |
| **Total** | **43,630** | **58,568** |
| *Less:* Impairment | (110) | (121) |
| | **43,520** | **58,447** |

As of December 31, 2019, the amount of BAM 6,993 thousand relates to the foreign currency term deposits a 7-day maturity, placed with Erste Group Bank AG Austria at an interest rate of 1.55%.

Foreign currency accounts held with foreign and domestic banks accrue interest depending on the terms of respective contracts executed with those banks for various currencies.

Movements on the Bank's gross exposure in 2019 and 2018 were as follows:

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Gross exposure at January 1, 2019** | 58,568 | - | - | - | 58,568 |
| Change in the gross exposure | (7,289) | - | - | - | (7,289) |
| of which, increase | 37,345 | - | - | - | 37,345 |
| of which, decrease | (44,634) | - | - | - | (44,634) |
| of which, transfers among Stages | - | - | - | - | - |
| Write-offs | - | - | - | - | - |
| Originated or purchased assets | - | - | - | - | - |
| Derecognized assets | (7,345) | - | - | - | (7,345) |
| Foreign exchange effects | (304) | - | - | - | (304) |
| Other movements | - | - | - | - | - |
| **Gross exposure at December 31, 2019** | **43,630** | **-** | **-** | **-** | **43,630** |

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Gross exposure at January 1, 2018** | 19,401 | - | 24 | - | 19,425 |
| Change in the gross exposure | 37,488 | - | - | - | 37,488 |
| of which, increase | 38,298 | - | - | - | 38,298 |
| of which, decrease | (810) | - | - | - | (810) |
| of which, transfers among Stages | - | - | - | - | - |
| Write-offs | - | - | (25) | - | (25) |
| Originated or purchased assets | 8,463 | - | - | - | 8,463 |
| Derecognized assets | (7,337) | - | - | - | (7,337) |
| Foreign exchange effects | 553 | - | 1 | - | 554 |
| Other movements | - | - | - | - | - |
| **Gross exposure at December 31, 2018** | **58,568** | **-** | **-** | **-** | **58,568** |

## 17. BALANCES HELD WITH OTHER BANKS (Continued)

Movements on the impairment allowance/provisions in 2019 and 2018 were as follows:

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Provisions at January 1, 2018** | (121) | - | - | - | (121) |
| Change in the provisions | (10) | - | - | - | (10) |
| of which, transfers among Stages | - | - | - | - | - |
| of which, increase | (53) | - | - | - | (53) |
| of which, decrease | 43 | - | - | - | 43 |
| of which, effects on the interest income | - | - | - | - | - |
| Write-offs | - | - | - | - | - |
| Modification effect not resulting in derecognition of assets | - | - | - | - | - |
| Originated or purchased assets | - | - | - | - | - |
| Derecognized assets | 21 | - | - | - | 21 |
| Model/parameter changes | - | - | - | - | - |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Provisions at December 31, 2018** | **(110)** | **-** | **-** | **-** | **(110)** |

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Provisions at January 1, 2018** | (31) | - | (12) | - | (43) |
| Change in the provisions | (114) | - | 12 | - | (102) |
| of which, transfers among Stages | - | - | - | - | - |
| of which, increase | (118) | - | - | - | (118) |
| of which, decrease | 4 | - | 12 | - | 16 |
| of which, effects on the interest income | - | - | - | - | - |
| Write-offs | - | - | - | - | - |
| Modification effect not resulting in derecognition of assets | - | - | - | - | - |
| Originated or purchased assets | - | - | - | - | - |
| Derecognized assets | - | - | - | - | - |
| Model/parameter changes | - | - | - | - | - |
| Foreign exchange effects | 24 | - | - | - | 24 |
| Other movements | - | - | - | - | - |
| **Provisions at December 31, 2018** | **(121)** | **-** | **-** | **-** | **(121)** |

## 18. LOANS AND RECEIVABLES DUE FROM CUSTOMERS

Loans and receivables at amortized cost comprise the following:

| | 2019 | 2018 |
|---|---|---|
| Loans and receivables due form customers | 564,206 | 506,896 |
| Other financial assets | 3,226 | 2,782 |
| **Total loans and receivables** | **567,432** | **509,678** |

### 18.1. Loans and Receivables Due from Customers

| | 2019 | 2018 |
|---|---|---|
| Retail customers | 382,403 | 362,419 |
| Private companies | 199,998 | 154,166 |
| Public sector (Government) | 20,908 | 31,055 |
| Public companies | 23,013 | 20,975 |
| Entrepreneurs | 10,327 | 11,605 |
| Non-residents | 1,061 | 1,309 |
| Non-banking financial institutions | 14,446 | 15,893 |
| Other organizations | 117 | 144 |
| **Total, gross** | **652,273** | **597,566** |
| *Less:* Impairment allowance of loans and receivables | (86,216) | (89,106) |
| **Total loans, net** | **566,057** | **508,460** |
| Accrued fee income charged | (1,851) | (1,564) |
| **Total net loans and receivables due from customers** | **564,206** | **506,896** |

Loans and receivables due from customers per product type are presented below:

| | 2019 | 2018 |
|---|---|---|
| Investment loans | 180,090 | 146,727 |
| Consumer loans | 280,973 | 244,664 |
| Housing loans | 51,240 | 62,948 |
| Loans for working capital | 39,919 | 60,753 |
| Mortgage loans | 20,539 | 24,120 |
| Account overdrafts | 57,564 | 36,162 |
| Car loans | 1 | 165 |
| Paid guarantees | 136 | 159 |
| Other | 21,811 | 21,868 |
| **Total** | **652,273** | **597,566** |
| *Less:* Impairment allowance of loans and receivables | (86,216) | (89,106) |
| **Total loans, net** | **566,057** | **508,460** |
| Accrued fee income charged | (1,851) | (1,564) |
| **Total net loans and receivables due from customers** | **564,206** | **506,896** |

## 18. LOANS AND RECEIVABLES DUE FROM CUSTOMERS (Continued)

### 18.1. Loans and Receivables Due from Customers (Continued)

During 2019 the Bank acquired real estate properties and movables in lieu of debt collection (property and assets used as collateral securitizing loans) in the total amount of BAM 189 thousand (2018: BAM 882 thousand).

During the year, the Bank sold assets acquired in lieu of debt collection with the carrying value of BAM 254 thousand (2018: BAM 399 thousand).

Movements on the Bank's gross exposure in 2019 and 2018 were as follows:

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Gross exposure at January 1, 2019** | 467,479 | 41,383 | 88,704 | - | 597,566 |
| Change in the gross exposure | **(68,637)** | **(1,748)** | **1,093** | **-** | **(69,292)** |
| of which, increase | 34,044 | 5,357 | 2,841 | - | 42,242 |
| of which, decrease | (90,790) | (12,403) | (8,341) | - | (111,534) |
| of which, transfers among Stages | (11,891) | 5,298 | 6,593 | - | - |
| Write-offs | (7) | (6) | (5,463) | - | (5,476) |
| Originated or purchased assets | 236,648 | 4,407 | 341 | - | 241,396 |
| Derecognized assets | (104,962) | (5,875) | (692) | - | (111,529) |
| Foreign exchange effects | 224 | (9) | (607) | - | (392) |
| Other movements | - | - | - | - | - |
| **Gross exposure at December 31, 2019** | **530,745** | **38,152** | **83,376** | **-** | **652,273** |

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Gross exposure at January 1, 2018** | 483,060 | 28,606 | 121,786 | - | 633,452 |
| Change in the gross exposure | (70,132) | 18,348 | (11,411) | - | (63,195) |
| of which, increase | 356,479 | 30,536 | 72,217 | - | 459,232 |
| of which, decrease | (397,524) | (35,114) | (89,789) | - | (522,427) |
| of which, transfers among Stages | (29,087) | 22,926 | 6,161 | - | - |
| Write-offs | (10) | (54) | (27,651) | | (27,715) |
| Originated or purchased assets | 176,360 | 4,237 | 7,228 | - | 187,825 |
| Derecognized assets | (121,846) | (9,763) | (1,975) | - | (133,584) |
| Foreign exchange effects | 105 | 9 | 738 | - | 852 |
| Other movements | (58) | - | (11) | | (69) |
| **Gross exposure at December 31, 2018** | 467,479 | 41,383 | 88,704 | - | 597,566 |

## 18. LOANS AND RECEIVABLES DUE FROM CUSTOMERS (Continued)

### 18.1. Loans and Receivables Due from Customers (Continued)

Movements on the impairment allowance/provisions in 2019 and 2018 were as follows:

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Provisions at January 1, 2019** | (4,512) | (9,702) | (74,892) | - | (89,106) |
| Change in the provisions | **2,165** | **448** | **(2,534)** | **-** | **79** |
| of which, transfers among Stages | (6,650) | 8,118 | (1,468) | - | - |
| of which, increase | (2,833) | (12,913) | (8,835) | - | (24,581) |
| of which, decrease | 11,648 | 5,243 | 8,767 | - | 25,658 |
| of which, effects on the interest income | - | - | (998) | - | (998) |
| Write-offs | 7 | 5 | 5,366 | - | 5,378 |
| Modification effect not resulting in derecognition of assets | - | - | - | - | - |
| Originated or purchased assets | (2,678) | (1,324) | (276) | - | (4,278) |
| Derecognized assets | 553 | 840 | 524 | - | 1,917 |
| Model/parameter changes | - | - | - | - | - |
| Foreign exchange effects | - | (2) | (204) | - | (206) |
| Other movements | - | - | - | - | - |
| **Provisions at December 31, 2019** | **(4,465)** | **(9,735)** | **(72,016)** | **-** | **(86,216)** |

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Provisions at January 1, 2018** | (5,153) | (4,199) | (100,978) | - | (110,330) |
| Change in the provisions | (1,565) | 1,045 | (1,920) | - | (2,440) |
| of which, transfers among Stages | 1,771 | 118 | (1,88) | - | - |
| of which, increase | (6,317) | (1,658) | (11,401) | - | (19,376) |
| of which, decrease | 2,981 | 2,585 | 12,559 | - | 18,125 |
| of which, effects on the interest income | - | - | (1,189) | - | (1,189) |
| Write-offs | - | 2 | 27,468 | - | 27,470 |
| Modification effect not resulting in derecognition of assets | - | - | - | - | - |
| Originated or purchased assets | (1,644) | (359) | (335) | - | (2,338) |
| Derecognized assets | 503 | 503 | 1,462 | - | 2,468 |
| Model/parameter changes | 3,347 | (6,691) | - | - | (3,344) |
| Foreign exchange effects | (1) | (2) | (589) | - | (592) |
| Other movements | - | - | - | - | - |
| **Provisions at December 31, 2018** | **(4,513)** | **(9,701)** | **(74,892)** | **-** | **(89,106)** |

## 18. LOANS AND RECEIVABLES DUE FROM CUSTOMERS (Continued)

### 18.2. Other Financial Assets

| | 2019 | 2018 |
|---|---|---|
| Other financial assets | | |
| In BAM: | | |
| - receivables due from customers per court rulings | 801 | 455 |
| - receivables from collateral foreclosures | 45 | 46 |
| - receivables per credit cards | 1,517 | 1,209 |
| - advances paid to suppliers | 310 | 313 |
| - rental income receivables | 49 | 68 |
| - receivables for consultancy services rendered | 1 | 6 |
| - third party receivables (managed funds) | 297 | 424 |
| - receivables for assets sold | - | - |
| - other receivables | 307 | 536 |
| In foreign currencies: | | |
| - receivables per credit cards | 1,300 | 728 |
| - prepaid interest | - | 1 |
| - other receivables | 259 | 266 |
| **Total** | **4,886** | **4,052** |
| *Less:* Impairment allowance of other financial assets | (1,660) | (1,270) |
| | **3,226** | **2,782** |

Movements on the Bank's gross exposure in 2019 and 2018 were as follows:

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Gross exposure at January 1, 2019** | 2,793 | 13 | 1,246 | - | 4,052 |
| Change in the gross exposure | 302 | 65 | 506 | - | 873 |
| of which, increase | 936 | 66 | 588 | - | 1,590 |
| of which, decrease | (634) | (1) | (82) | - | (717) |
| of which, transfers among Stages | - | - | - | - | - |
| Write-offs | - | (1) | (38) | - | (39) |
| Originated or purchased assets | - | - | - | - | - |
| Derecognized assets | - | - | - | - | - |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Gross exposure at December 31, 2019** | **3,095** | **77** | **1,714** | **-** | **4,886** |

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Gross exposure at January 1, 2018** | 2,225 | - | 2,375 | - | 4,600 |
| Change in the gross exposure | 353 | 12 | 52 | - | 417 |
| of which, increase | 657 | - | 63 | - | 720 |
| of which, decrease | (292) | - | (11) | - | (303) |
| of which, transfers among Stages | (12) | 12 | - | - | - |
| Write-offs | - | - | (1,449) | - | (1,449) |
| Originated or purchased assets | 215 | 1 | 276 | - | 492 |
| Derecognized assets | - | - | (8) | - | (8) |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Gross exposure at December 31, 2018** | **2,793** | **13** | **1,246** | **-** | **4,052** |

## 18. LOANS AND RECEIVABLES DUE FROM CUSTOMERS (Continued)

### 18.2. Other Financial Assets (Continued)

Movements on the impairment allowance/provisions in 2019 and 2018 were as follows:

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Provisions at January 1, 2019** | (52) | (4) | (1,215) | - | (1,271) |
| Change in the provisions | 45 | (23) | (450) | - | (428) |
| of which, transfers among Stages | - | - | - | - | - |
| of which, increase | (1) | (27) | (471) | - | (499) |
| of which, decrease | 46 | 4 | 21 | - | 71 |
| of which, effects on the interest income | - | - | - | - | - |
| Write-offs | - | 1 | 38 | - | 39 |
| Modification effect not resulting in derecognition of assets | - | - | - | - | - |
| Originated or purchased assets | - | - | - | - | - |
| Derecognized assets | - | - | - | - | - |
| Model/parameter changes | - | - | - | - | - |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Provisions at December 31, 2019** | **(7)** | **(26)** | **(1,627)** | **-** | **(1,660)** |

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Provisions at January 1, 2018** | (32) | - | (2,372) | - | (2,404) |
| Change in the provisions | (19) | (4) | (298) | - | (321) |
| of which, transfers among Stages | - | | - | - | - |
| of which, increase | (28) | (4) | (314) | - | (346) |
| of which, decrease | 9 | - | 16 | - | 25 |
| of which, effects on the interest income | - | - | - | - | - |
| Write-offs | - | - | 1,455 | - | 1,455 |
| Modification effect not resulting in derecognition of assets | - | - | - | - | - |
| Originated or purchased assets | - | - | - | - | - |
| Derecognized assets | - | - | - | - | - |
| Model/parameter changes | - | - | - | - | - |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Provisions at December 31, 2018** | **(51)** | **(4)** | **(1,215)** | **-** | **(1,270)** |

## 19. INVESTMENTS IN SECURITIES

### 19.1. Debt and Equity Securities

| | 2019 | 2018 |
|---|---|---|
| ***Financial assets at FVtOCI*** | | |
| **Debt securities** | | |
| Bonds of BNP Paribas BA | 10,121 | 9,758 |
| Bonds of Commerce Bank Frankfurt | 7,850 | 7,515 |
| Bonds of Intesa Sanpaolo SPA | 5,831 | 5,927 |
| Bonds of UBS AG | - | 9,818 |
| Bonds of UniCredit SPA | 6,261 | 6,020 |
| Bonds of the Polish Government | - | 13,834 |
| Bonds of the Italian Government | 7,887 | - |
| Bonds of the Bulgarian Government | 14,740 | - |
| Bonds of the Spanish Government | 9,252 | - |
| RS Ministry of Finance bonds | 5 | 2,027 |
| **Equity securities** | | |
| Banja Luka Stock Exchange | 175 | 175 |
| Central Register of Securities, Banja Luka | 30 | 30 |
| S.W.I.F.T | 24 | 24 |
| | **62,176** | **55,128** |

The Bank's investments in debt securities totaling BAM 61,947 thousand as of December 31, 2018 refer to the long-term debt securities issued by the Ministry of Finance of the Republic of Srpska, EU member states and EU banks. Investments in debt securities are made for the purpose of the available Bank's liquidity management and for achievement of profit from investments.

Movements on the Bank's gross exposure in 2019 and 2018 were as follows:

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | Stage 1 (12-month ECL) |
|---|---|---|---|---|---|
| **Gross exposure at January 1, 2019** | 54,899 | - | - | - | 54,899 |
| Change in the gross exposure | 7,048 | - | - | - | 7,048 |
| of which, increase | 32,966 | - | - | - | 32,966 |
| of which, decrease | (25,918) | - | - | - | (25,918) |
| of which, transfers among Stages | - | - | - | - | - |
| Write-offs | - | - | - | - | - |
| Originated or purchased assets | - | - | - | - | - |
| Derecognized assets | - | - | - | - | - |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Gross exposure at December 31, 2019** | **61,947** | **-** | **-** | **-** | **61,947** |

## 19. INVESTMENTS IN SECURITIES (Continued)

### 19.1. Debt and Equity Securities (Continued)

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Gross exposure at January 1, 2018** | 2,029 | - | - | - | 2,029 |
| Change in the gross exposure | 52,870 | - | - | - | 52,870 |
| of which, increase | 53,316 | - | - | - | 53,316 |
| of which, decrease | (446) | - | - | - | (446) |
| of which, transfers among Stages | - | - | - | - | - |
| Write-offs | - | - | - | - | - |
| Originated or purchased assets | - | - | - | - | - |
| Derecognized assets | - | - | - | - | - |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Gross exposure at December 31, 2018** | **54,899** | **-** | **-** | **-** | **54,899** |

Movements on the impairment allowance/provisions in 2019 and 2018 were as follows:

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Provisions at January 1, 2019** | (118) | - | - | - | (118) |
| Change in the provisions | 86 | - | - | - | 86 |
| of which, transfers among Stages | - | - | - | - | - |
| of which, increase | (1) | - | - | - | (1) |
| of which, decrease | 87 | - | - | - | 87 |
| of which, effects on the interest income | - | - | - | - | - |
| Write-offs | - | - | - | - | - |
| Modification effect not resulting in derecognition of assets | - | - | - | - | - |
| Originated or purchased assets | - | - | - | - | - |
| Derecognized assets | - | - | - | - | - |
| Model/parameter changes | - | - | - | - | - |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Provisions at December 31, 2019** | **(32)** | **-** | **-** | **-** | **(32)** |

## 19. INVESTMENTS IN SECURITIES (Continued)

### 19.1. Debt and Equity Securities (Continued)

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Provisions at January 1, 2018** | (93) | - | - | - | (93) |
| Change in the provisions | (25) | - | - | - | (25) |
| of which, transfers among Stages | - | - | - | - | - |
| of which, increase | (96) | - | - | - | (96) |
| of which, decrease | 71 | - | - | - | 71 |
| of which, effects on the interest income | - | - | - | - | - |
| Write-offs | - | - | - | - | - |
| Modification effect not resulting in derecognition of assets | - | - | - | - | - |
| Originated or purchased assets | - | - | - | - | - |
| Derecognized assets | - | - | - | - | - |
| Model/parameter changes | - | - | - | - | - |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Provisions at December 31, 2018** | **(118)** | **-** | **-** | **-** | **(118)** |

### 19.2. Derivative Financial Assets and Liabilities

*Derivatives held for trading*

| | *2019* | *2018* |
|---|---|---|
| **Assets** | | |
| *Fair value:* | | |
| Currency forwards and currency swaps | 1 | - |
| *Notional amount:* | | |
| Currency forwards and currency swaps | 136,908 | 115,394 |
| **Liabilities** | | |
| *Fair value:* | | |
| Currency forwards and currency swaps | 3 | - |
| *Notional amount:* | | |
| Currency forwards and currency swaps | 136,908 | 115,394 |

The Bank uses foreign currency forward contracts and currency swaps to manage foreign exchange risk. Derivatives are classified as financial instruments held for trading, as the Bank has not implemented hedge accounting.

The notional amounts of certain types of financial assets provide a basis for comparison with the assets in the statement of financial position, but do not necessarily indicate the amount of future cash flows or current fair value of the assets and therefore do not indicate the exposure to credit risk, or the risk of price changes.

## 20. PROPERTY AND EQUIPMENT

### 20.1. Land, Buildings and Equipment

| | Land and buildings | Equipment, and other assets | Investments in progress | ROU assets | Total |
|---|---|---|---|---|---|
| **Cost** | | | | | |
| *Balance, January 1, 2018* | *37,312* | *9,208* | *2* | *-* | *46,522* |
| Additions | - | 87 | 84 | - | 171 |
| Transfers | - | 1 | (1) | - | - |
| Retirement and disposal | - | (30) | - | - | (30) |
| Appraisal effects | - | - | - | - | - |
| Write-off | - | - | - | - | - |
| Sales | - | (2) | - | - | (2) |
| Reclassifications | - | - | - | - | - |
| **Balance, December 31, 2018** | **37,312** | **9,264** | **85** | **-** | **46,661** |
| *Balance, January 1, 2019* | *37,312* | *9,264* | *85* | *1,240* | *47,901* |
| Additions | 4 | 204 | 509 | 226 | 943 |
| Transfers | 199 | 257 | (456) | - | - |
| Retirement and disposal | - | (416) | - | - | (416) |
| Appraisal effects | 77 | - | - | - | 77 |
| Write-off | - | - | - | - | - |
| Sales | (558) | (48) | - | - | (606) |
| Reclassifications | - | - | - | - | - |
| **Balance, December 31, 2019** | **37,034** | **9,261** | **138** | **1,466** | **47,899** |
| **Accumulated depreciation** | | | | | |
| *Balance, January 1, 2018* | *11,779* | *7,134* | - | - | *18,913* |
| Charge for the year | 546 | 553 | - | - | 1,099 |
| Retirement and disposal | - | (28) | - | - | (28) |
| Appraisal effects | - | - | - | - | - |
| Write-off | - | - | - | - | - |
| Sales | - | - | - | - | - |
| Reclassifications | - | (2) | - | - | (2) |
| **Balance, December 31, 2018** | **12,325** | **7,657** | **-** | **-** | **19,982** |
| *Balance, January 1, 2019* | *12,325* | *7,657* | - | - | *19,982* |
| Charge for the year | 534 | 524 | - | 525 | 1,583 |
| Retirement and disposal | - | (398) | - | - | (398) |
| Appraisal effects | 1,345 | - | - | - | 1,345 |
| Write-off | - | - | - | - | - |
| Sales | (239) | (47) | - | - | (286) |
| Reclassifications | - | - | - | - | - |
| **Balance, December 31, 2019** | **13,965** | **7,736** | **-** | **525** | **22,226** |
| **Net book value:** | | | | | |
| **at December 31, 2019** | **23,069** | **1,525** | **138** | **941** | **25,673** |
| **at December 31, 2018** | **24,987** | **1,607** | **85** | **-** | **26,679** |

## 20. PROPERTY AND EQUIPMENT (Continued)

### 20.1. Land, Buildings and Equipment (Continued)

As of December 31, 2019, the Bank's property included land and buildings with the carrying value of BAM 306 thousand for which the Bank did not possess appropriate title deeds (2018: BAM 707 thousand).

As of December 31, 2019, the Bank had no mortgage or pledge liens assigned over its property and equipment.

Based on the appraisal performed by a certified appraiser as of December 31, 2019, the Bank recorded impairment of its property and equipment in the amount of BAM 1,268 thousand, of which BAM 1,245 thousand was recorded as a decrease of previously recognized revaluation reserve while BAM 23 thousand was recognized within expenses, as impairment loss, in the profit and loss statement.

If the value of property and equipment were presented at historical cost, the Bank would have recognized the following amounts:

| | *2019* | *2018* |
|---|---|---|
| Cost | **51,025** | **49,757** |
| Accumulated depreciation | (26,512) | (25,781) |
| **Net book value** | **24,513** | **23,976** |

### 20.2. Investment Property

| Cost | |
|---|---|
| **Balance at December 31, 2017** | **2,388** |
| *Balance at January 1, 2018* | *2,388* |
| Additions | 13 |
| Appraisal effects | - |
| **Balance at December 31, 2018** | **2,401** |
| *Balance at January 1, 2019* | *2,401* |
| Additions | - |
| Appraisal effects | 100 |
| **Balance at December 31, 2019** | **2,501** |

Based on the appraisal performed by a certified appraiser as of December 31, 2019, the Bank recorded positive investment property valuation (appraisal) effects of BAM 100 thousand within income in the profit or loss statement.

## 21. INTANGIBLE ASSETS

| | Licenses, software |
|---|---|
| **Cost** | |
| *Balance at January 1, 2018* | *20,252* |
| Additions | 2,875 |
| Disposal and retirement | (16) |
| **Balance at December 31, 2018** | **23,111** |
| *Balance at January 1, 2019* | *23,111* |
| Additions | 2,717 |
| Disposal and retirement | (549) |
| **Balance at December 31, 2019** | **25,279** |
| **Accumulated amortization** | |
| *Balance at January 1, 2018* | *15,814* |
| Charge for the year | 1,423 |
| **Balance at December 31, 2018** | **17,237** |
| *Balance at January 1, 2019* | *17,237* |
| Charge for the year | 2,030 |
| Disposal and retirement | (549) |
| **Balance at December 31, 2019** | **18,718** |
| **Net book value:** | |
| **at December 31, 2019** | **6,561** |
| **at December 31, 2018** | **5,874** |

If the value of intangible assets were presented at historical cost, the Bank would have recognized the following amounts:

| | *2019* | *2018* |
|---|---|---|
| **Cost** | **25,127** | **22,806** |
| Accumulated amortization | (18,384) | (16,932) |
| **Net book value** | **6,743** | **5,874** |

## 22. ASSETS HELD FOR SALE

In accordance with IFRS 5, the Bank classified assets not used for its own purposes and intended for sale as the assets held for sale. Breakdown of the Bank’s assets held for sale is provided in the table below:

| Cost | |
|---|---|
| *Balance at January 1, 2018* | 545 |
| **Balance at December 31, 2018** | **545** |
| *Balance at January 1, 2019* | 545 |
| Additions | 49 |
| Appraisal effects – changes in the fair value | 40 |
| Sales | (42) |
| **Balance at December 31, 2019** | **592** |

Based on the appraisal performed by a certified appraiser as of December 31, 2019, the Bank recorded positive valuation (appraisal) effects in respect of assets held for sale of BAM 40 thousand within income in the profit or loss statement.

## 23. OTHER ASSETS

Breakdown of the Bank's non-financial assets:

| | 2019 | 2018 |
|---|---|---|
| Other non-financial assets | | |
| *In local currency:* | | |
| - Tangible assets received in lieu of debt collection | 2,191 | 2,256 |
| - Consumables, tools and fixtures | 103 | 119 |
| - Prepaid expenses | 117 | 73 |
| - Receivables for deposited funds | 352 | 407 |
| - Receivables from investment funds | 87 | - |
| - Receivables for assets in acquisition | 378 | 315 |
| - Other receivables | 2,668 | 2,137 |
| *In foreign currencies*: | | |
| - Prepaid expenses | 361 | 263 |
| - Other receivables | 32 | - |
| **Total:** | **6,289** | **5,570** |
| *Less:* Impairment allowance | - | - |
| | **6,289** | **5,570** |

## 24. FINANCIAL LIABILITIES MEASURED AT AMORTIZED COST (AC)

### 24.1. Deposits Due to Banks and Other Financial Institutions

Deposits due to banks and financial institutions, grouped per agreed placement/maturity period, are presented below:

| | 2019 | 2018 |
|---|---|---|
| Demand deposits | 4,852 | 10,049 |
| Short-term deposits | 28,661 | 1,000 |
| Long-term deposits | 14,479 | 20,301 |
| | **47,992** | **31,350** |

Out of the total short-term deposits in foreign currencies, the amount of BAM 24,625 thousand pertains to deposits placed by Addiko Bank Group members for periods of up to 6 months, at a fixed interest rate of 1%.

Deposits due to banks and financial institutions classified per currency are presented below:

| | 2019 | 2018 |
|---|---|---|
| Local currency | 15,644 | 9,731 |
| Foreign currency | 32,348 | 21,619 |
| | **47,992** | **31,350** |

Deposits denominated in BAM with contracted currency clause are presented within appropriate foreign currency items.

### 24.2. Deposits Due to Customers

Deposits due to customers, grouped per agreed placement/maturity period, are presented below:

| | 2019 | 2018 |
|---|---|---|
| Demand deposits | 331,740 | 307,908 |
| Short-term deposits | 6,401 | 8,168 |
| Long-term deposits | 219,420 | 224,169 |
| | **557,561** | **540,245** |

## 24. FINANCIAL LIABILITIES MEASURED AT AMORTIZED COST (AC) (Continued)

### 24.2. Deposits Due to Customers (Continued)

Deposits due to customers classified per customer type are presented below:

| | 2019 | 2018 |
|---|---|---|
| Retail customers | 394,784 | 380,925 |
| Private companies | 83,908 | 81,252 |
| Public sector | 24,440 | 32,086 |
| Non-residents | 18,653 | 19,705 |
| Public companies | 9,328 | 11,872 |
| Entrepreneurs | 8,337 | 7,469 |
| Other organizations | 18,111 | 6,936 |
| | **557,561** | **540,245** |

Deposits due to customers classified per currency are presented below:

| | 2019 | 2018 |
|---|---|---|
| Local currency | 277,093 | 257,836 |
| Foreign currency | 280,468 | 282,409 |
| | **557,561** | **540,245** |

Deposits denominated in BAM with contracted currency clause are presented within appropriate foreign currency items.

### 24.3. Borrowings

| | 2019 | 2018 |
|---|---|---|
| *Long-term foreign currency borrowings:* | | |
| EBRD (European Bank for Reconstruction and Development) | 15,767 | 9,877 |
| EFSE (European Fund for Southeast Europe) | 12,184 | 15,659 |
| | **27,951** | **25,536** |
| *Long-term local currency borrowings:* | | |
| - RS Development and Employment Fund | 9,265 | 4,151 |
| - Fund for Development of Eastern Region of the Republic of Srpska | 2,554 | 2,991 |
| - RS Housing Fund | 16,426 | 19,834 |
| | **28,245** | **26,976** |
| | **56,196** | **52,512** |

Long-term borrowings in local currency were contracted with a foreign currency clause.

The Bank's foreign currency borrowings are subject to contractually defined covenants. As of December 31, 2019, the Bank was fully compliant with all the covenants stipulated by the relevant loan agreements.

## 24. FINANCIAL LIABILITIES MEASURED AT AMORTIZED COST (AC) (Continued)

### 24.3. Borrowings (Continued)

EBRD (European Bank for Reconstruction and Development) approved a long-term loan to the Bank for general long-term financing of micro-sized, small and medium entities in EUR. The interest rate was defined as 6-month EURIBOR adjusted for percentage points as the determined minimum interest rate in accordance with the relevant Financing Agreement. The companies that are extended loans from these funds are required to comply with the prescribed environmental and social provisions of the legislation of Bosnia and Herzegovina and the Republic of Srpska.

EFSE (European Fund for Southeast Europe) approved a long-term loan to the Bank for general long-term financing of micro-sized, small and medium entities in EUR. The interest rate was defined as 6-month EURIBOR adjusted for percentage points as the determined minimum interest rate in accordance with the relevant Financing Agreement. The companies that are extended loans from these funds are required to comply with the prescribed environmental and social provisions of the legislation of Bosnia and Herzegovina and the Republic of Srpska.

RS Development and Employment Fund, Banja Luka approved a loan to the Bank for financing development projects. The repayment was agreed in accordance with the repayment schedules to the end users of the loans. Interest is charged at the rate of 6-month EURIBOR as adjusted for percentage points in accordance with the criteria for adjustment of interest rates pursuant to the Framework Agreement applied to the Investment Development Bank of the Republic of Srpska Banja Luka credit facilities.

Housing Fund of the Republic of Srpska, Banja Luka has provided a loan to the Bank for financing the purchase, reconstruction, and extension of homes. The repayment was agreed in accordance with the repayment schedules to the end users of the loans. Interest is charged at the rate of 6-month EURIBOR as adjusted for percentage points in accordance with the criteria for adjustment of interest rates pursuant to the Framework Agreement applied to the Investment Development Bank of the Republic of Srpska Banja Luka credit facilities.

### 24.4. Other Financial Liabilities

| | 2019 | 2018 |
|---|---|---|
| **Local currency liabilities:** | | |
| - Accounts payable | 690 | 437 |
| - Liabilities arising from credit card operations | 1,546 | 545 |
| - Lease liabilities | 888 | - |
| - Liabilities per advances received | 367 | 103 |
| - Early loan repayments | 633 | 593 |
| - Suspended customer accounts | 43 | 99 |
| - Unrealized payments for foundation of entities | 105 | 109 |
| - PTA liabilities | 3 | - |
| - Dividend payment liabilities | 70 | 70 |
| - Other liabilities | 80 | 130 |
| **Foreign currency liabilities:** | | |
| - Early loan repayments | 4,493 | 5,145 |
| - Accounts payable | 1,466 | 1,117 |
| - Liabilities arising from credit card operations | 117 | 67 |
| - Other liabilities | 394 | 265 |
| | **10,895** | **8,680** |

## 25. OTHER LIABILITIES

Breakdown of the Bank's non-financial liabilities is provided below:

| | 2019 | 2018 |
|---|---|---|
| **Local currency liabilities:** | | |
| - Liabilities to employees | 1,591 | 1,722 |
| - Liabilities for taxes and contributions | 586 | 860 |
| - Liabilities to employees for unused annual leaves | 274 | 293 |
| - Deferred interest income | 100 | 100 |
| - Other deferred fees | 81 | 86 |
| - Accrued expenses | 809 | 790 |
| - Other liabilities | 599 | 64 |
| **Foreign currency liabilities** | | |
| - Other liabilities | 8 | 69 |
| | **4,048** | **3,984** |

Movements on provisions for unused annual leaves are presented below:

| | 2019 | 2018 |
|---|---|---|
| **Balance at January 1** | **293** | **314** |
| Charge for the year | - | - |
| Release of provisions | - | - |
| Reversal of provisions | (19) | (21) |
| ***(Reversal) for the year, net*** | ***(19)*** | ***(21)*** |
| **Balance at December 31** | **274** | **293** |

## 26. EQUITY

***Share Capital***

The Bank's share capital includes initial shareholder investments and subsequent share issues. The Bank's shareholders are entitled to participation in the management of the Bank, as well as in the distribution of profit.

During 2019 the Bank did not increase/decrease its share capital. The Bank's share capital comprises 153,094,205 common stock (ordinary) shares with a par value of BAM 1 per share, which was registered with the District Commercial Court of Banja Luka on January 25, 2017 under Decision no. 057-0-Reg-17-001851.

As of December 31, 2019, the Bank's majority shareholder was Addiko Bank AG with a 99.87% equity interest (December 31, 2018: equity interest of the majority shareholder was 99.86%). The change in the shareholding was due to the request of four minority shareholders to be enabled sale of their shares to the majority shareholder Addiko Bank AG.

***Reserves***

The Bank's reserves as of December 31, 2019 and 2018 are provided in the following table:

| | 2019 | 2018 |
|---|---|---|
| Legal reserves | - | - |
| Other reserves from profit | 61,351 | 56,819 |
| Special reserves for regulatory losses according to BARS regulations | - | 4,532 |
| **Balance at December 31** | **61,351** | **61,351** |

On December 19, 2018, BARS issued the Decision on the Conditions for Inclusion of the Formed Reserves for Credit Losses into the Regular Core Capital of Banks (Official Gazette of RS no. 117/2018), whereby conditions are prescribed that banks need to fulfill in order to recognize the reserves for credit losses as the regular core capital item in accordance with the Decision on Bank Capital Calculation.

## 26. EQUITY (Continued)

***Reserves (Continued)***

Considering all the aforesaid, on December 27, 2018, the Bank's Shareholder Assembly enacted Decision no. 01-1-22786/2018 on inclusion of the formed reserves for credit losses into the other reserves.

Due to the inclusion of the formed reserves for credit losses into the other reserves the Bank's regulatory capital increased by BAM 56,819 thousand as BAM 4,532 thousand remained as the balance of the reserves for credit losses as per regulatory requirements (Note 6.8).

On April 30, 2019, the Bank's Shareholder Assembly enacted Decision no. S-9/2019 on inclusion of the remaining reserves for credit losses amounting to BAM 4,532 thousand into the other reserves.

Due to the inclusion of the formed reserves for credit losses into the other reserves the Bank's regulatory capital increased by BAM 4,532 thousand as of December 31, 2019 (Note 6.8).

As of December 31, 2019 and 2018, the Bank's shortfall/surplus had no recorded shortfall reserves as per BARS regulations.

| | 2019 | 2018 |
|---|---|---|
| Total reserves per regulatory requirements for balance sheet assets and off-balance sheet items | 93,102 | 96,897 |
| Total impairment allowance as per IAS/IFRS(for balance sheet assets and off-balance sheet items | 88,865 | 92,405 |
| Special reserves for regulatory losses per BARS regulations | - | 4,532 |
| The shortfall/(excess) amount of credit loss reserves according to BARS regulations | 4,237 | (40) |

## 27. EARNINGS PER SHARE

| | 2019 | 2018 |
|---|---|---|
| | 6,720 | 3,285 |
| Weighted average number of shares outstanding | 153,094,205 | 153,094,205 |
| **Basic earnings per share (in BAM)** | **0.044** | **0.021** |

The Bank has no potentially dilutive ordinary shares such as convertible debt and share options. Therefore, the Bank does not calculate diluted earnings per share.

## 28. OTHER PROVISIONS

Other provisions as of December 31, 2019 and 2018 are presented below:

| | 2019 | 2018 |
|---|---|---|
| Litigation | 2,568 | 1,861 |
| Restructuring | 117 | 507 |
| Other provisions | 16 | 16 |
| Retirement benefits | 288 | 290 |
| | 2,989 | 2,674 |
| Provisions for contingent liabilities | 852 | 1,175 |
| | **3,841** | **3,849** |

## 28. OTHER PROVISIONS (Continued)

Movements on the Bank's provisions may be summarized as follows:

| | Restructuring | Retirement Benefits | Litigations | Other | Total |
|---|---|---|---|---|---|
| **January 1, 2019** | **507** | **290** | **1,861** | **16** | **2,676** |
| Charge for the year | - | - | 1,292 | - | 1,292 |
| Reversal or decrease | - | - | (525) | - | (525) |
| Release | (390) | (2) | (546) | - | (940) |
| Other | - | - | 486 | - | 486 |
| **December 31, 2019** | **117** | **288** | **2,568** | **16** | **2,989** |

| | Restructuring | Retirement Benefits | Litigations | Other | Total |
|---|---|---|---|---|---|
| **January 1, 2018** | **775** | **294** | **3,106** | **16** | **4,191** |
| Charge for the year | - | - | 766 | - | 766 |
| Reversal or decrease | - | - | (812) | - | (812) |
| Release | (268) | (4) | (1,199) | - | (1,469) |
| **December 31, 2018** | **507** | **290** | **1,861** | **16** | **2,676** |

Movements on the Bank's provisions for off-balance sheet exposures are shown below:

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Provisions at January 1, 2019** | (688) | (338) | (149) | - | (1,175) |
| Change in the provisions | 247 | 305 | (17) | - | 535 |
| of which, transfers among Stages | (582) | 601 | (19) | - | - |
| of which, increase | (585) | (629) | (120) | - | (1,334) |
| of which, decrease | 1,414 | 333 | 122 | - | 1,869 |
| of which, effects on the interest income | - | - | - | - | - |
| Write-offs | - | - | - | - | - |
| Modification effect not resulting in derecognition of assets | - | - | - | - | - |
| Originated or purchased assets | (463) | (5) | (3) | - | (471) |
| Derecognized assets | 163 | 9 | 87 | - | 259 |
| Model/parameter changes | - | - | - | - | - |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Provisions at December 31, 2019** | **(741)** | **(29)** | **(82)** | **-** | **(852)** |

28. OTHER PROVISIONS (Continued)

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Provisions at January 1, 2018** | (980) | (48) | (232) | - | (1,260) |
| Change in the provisions | 611 | (294) | 77 | - | 394 |
| of which, transfers among Stages | 50 | (35) | (15) | - | - |
| of which, increase | (226) | (333) | (63) | - | (622) |
| of which, decrease | 787 | 74 | 155 | - | 1,016 |
| of which, effects on the interest income | - | - | - | - | - |
| Write-offs | - | - | - | - | - |
| Modification effect not resulting in derecognition of assets | - | - | - | - | - |
| Originated or purchased assets | (440) | (3) | (32) | - | (475) |
| Derecognized assets | 121 | 7 | 38 | - | 166 |
| Model/parameter changes | - | - | - | - | - |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Provisions at December 31, 2018** | **(688)** | **(338)** | **(149)** | **-** | **(1,175)** |

### *Provisions for Restructuring*

The table below presents the expected maturities of restructuring provisions:

| | *2019* | *2018* |
|---|---|---|
| Within a year | 117 | 507 |
| From 1 to 5 years | - | - |
| | **117** | **507** |

### *Provisions for Retirement Benefits*

From the total decrease in the amount of provisions for retirement benefits in the amount of BAM 2 thousand in 2019, BAM 6 thousand refers to the actuarial losses per demographic assumptions and BAM 4 thousand to the actuarial gains per financial assumptions. More details on actuarial assumption used in the calculation of the provisions for retirement benefits are provided in Note 30 – *Retirement Benefits*.

### *Provisions for Litigations and Other Provisions*

In an attempt to collect receivables arising from loans, guarantees, letters of credit or other grounds, as at December 31, 2019 the Bank was involved in the total of 4,315 court cases with the aggregate value of BAM 79,182 thousand.

As of December 31, 2019, there were 117 pending lawsuits filed against the Bank, with the total nominal value claimed of BAM 39,218 thousand. U The aforesaid amount includes 4 cases with the total nominal amount of BAM 21.5 thousand, where the claims had been paid in prior periods, so that they do not pose any additional risk of contingent losses, but were still listed as pending lawsuits as there were procedures in progress as per extraordinary remedy, i.e., case revisions were underway as of December 31, 2019. The aforesaid amount also includes 23 lawsuits totaling BAM 20,084 thousand, which, in accordance with the agreements on assignment of receivables (Brush), were transferred under the remit of the assuming party and do not pose any risk to the Bank..

There were 44 lawsuits altogether with claims relating to the loans contracted with CHF currency clause and the alleged increased interest margin. The aggregate nominal value of such suits amounted to BAM 6,037 thousand.

## 28. OTHER PROVISIONS (Continued)

*Provisions for Litigations and Other Provisions (Continued)*

The Bank assesses the amount of provisions for litigation costs based on the estimated probability of cash outflows arising from the past or constructive obligations. As of December 31, 2019, the Bank made provisions for litigation losses/costs in the amount of BAM 2,568 thousand, which was estimated as sufficient by the management.

In 2019 the Bank intensified activities or resolving the ongoing lawsuits and managing legal risk inherent in the lawsuits. Strategies were reviewed per case as well as models of legal representation of the Bank and court defense coordination, out-of-court resolution or settlement processes were set up, as well as recording of and reporting on lawsuits involving the Bank. The foregoing resulted in a significant decrease in the total number of lawsuits involving the Bank and their aggregate value compared to those as at December 31, 2018.

## 29. COMMITMENTS AND CONTINGENT LIABILITIES

**Loans, Payment and Performance Guarantees and Letters of Credit**

| | 2019 | 2018 |
|---|---|---|
| Loan commitments | 72,471 | 71,584 |
| Payment guarantees | 25,824 | 28,817 |
| Performance guarantees | 21,178 | 12,609 |
| Letters of credit and other sureties | - | 1,419 |
| | **119,473** | **114,429** |

In the course of their business, the Bank assumes credit commitments which are maintained on the off-balance sheet accounts and primarily include guarantees, letters of credit and undrawn portions of loans approved. The Bank formed provisions for these exposures, as disclosed in Note 14.

Movements on the Bank's gross off-balance sheet exposure in 2019 and 2018 were as follows:

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Gross exposure at January 1, 2019** | 111,178 | 3,030 | 221 | - | 114,429 |
| Change in the gross exposure | 9,316 | (2,656) | (53) | - | 6,607 |
| of which, increase | 4,155 | 2,607 | - | - | 6,762 |
| of which, decrease | - | - | (155) | - | (155) |
| of which, transfers among Stages | 5,161 | (5,263) | 102 | - | - |
| Write-offs | - | - | - | - | - |
| Originated or purchased assets | 48,058 | 46 | 75 | - | 48,179 |
| Derecognized assets | (49,490) | (132) | (120) | - | (49,742) |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Gross exposure at December 31, 2019** | 119,062 | 288 | 123 | - | 119,473 |

## 29. COMMITMENTS AND CONTINGENT LIABILITIES (Continued)

| | Stage 1 (12-month ECL) | Stage 2 (lifetime ECL-unimpaired assets) | Stage 3 (lifetime ECL-impaired assets) | POCI assets | TOTAL |
|---|---|---|---|---|---|
| **Gross exposure at January 1, 2018** | 124,631 | 1,122 | 344 | - | 126,097 |
| Change in the gross exposure | 6,580 | 2,012 | (82) | - | 8,510 |
| of which, increase | 41,811 | 3,251 | 273 | - | 45,335 |
| of which, decrease | (32,640) | (3,795) | (390) | - | (36,825) |
| of which, transfers among Stages | (2,591) | 2,556 | 35 | - | - |
| Write-offs | - | - | - | - | - |
| Originated or purchased assets | 30,341 | 5 | 32 | - | 30,378 |
| Derecognized assets | (50,374) | (109) | (73) | - | (50,556) |
| Foreign exchange effects | - | - | - | - | - |
| Other movements | - | - | - | - | - |
| **Gross exposure at December 31, 2018** | **111,178** | **3,030** | **221** | **-** | **114,429** |

## 30. RETIREMENT BENEFITS

The following significant actuarial assumptions were used in calculation of the present value of the employee retirement benefits: discount rate, expected salary growth rate and mortality rate.

Sensitivity analysis of retirement benefits to the change in the discount rate may be presented as follows:

| | | | BAM '000 |
|---|---|---|---|
| Discount rate | 5% | 4.50% | 5.50% |
| Present value of the liabilities | 288 | 303 | 274 |
| % of variance | - | 5.19% | (4.79%) |

If the interest rate used for discounting were 0.5% lower, the present value of the liabilities would increase by 5.19%. On the other hand, if the discount rate were by 0.5% higher, the present value of the liabilities would decrease by 4.79%.

Sensitivity analysis of retirement benefits to the change in the average salary may be presented as follows:

| | | | BAM '000 |
|---|---|---|---|
| Average retirement benefit amount | *current* | *0.5% lower* | *0.5% higher* |
| Present value of the liabilities | 288 | 287 | 289 |
| % of variance | - | (0.50%) | 0.50% |

The impact of changes in salary amounts is directly proportional to the changes in retirement benefit amounts.

Sensitivity analysis of retirement benefits to the change in the mortality rate may be presented as follows:

| | | | BAM '000 |
|---|---|---|---|
| Average age | *current* | *1 year younger* | *1 year older* |
| Present value of the liabilities | 288 | 278 | 296 |
| % of variance | - | (3.38%) | 2.90% |

If the employees were a year older on average, the present value of retirement benefits would increase by 2.9%, and if they were a year younger on average, the average retirement benefit would decrease by 3.38%.

## 30. RETIREMENT BENEFITS (Continued)

The expected maturity periods of provisions for retirement benefits are provided below:

| | 2019 | 2018 |
|---|---|---|
| Within the ensuing 12 months | 29 | 28 |
| From 1 to 5 years | 57 | 64 |
| From 5 to10 years | 61 | 56 |
| After 10 years | 141 | 142 |
| **Total** | 288 | **290** |

## 31. RELATED PARTY TRANSACTIONS

In accordance with IAS 24, a related party is a person or an entity that is related to the entity that is preparing its financial statements

- A person or a close family member related to the entity if it:
  - has control or joint control over the reporting entity;
  - has significant influence over the reporting entity; or
  - is a member of the key management personnel of the reporting entity or of a parent of the reporting entity.

- An entity is related to a reporting entity if any of the following conditions applies:
  - The entity and the reporting entity are members of the same group;
  - One entity is an associate or joint venture of the other entity;
  - Both entities are joint ventures of the same third party;
  - One entity is a joint venture of a third entity and the other entity is an associate of the third entity;
  - The entity is a post-employment defined benefit plan for the benefit of employees of either the reporting entity or an entity related to the reporting entity. If the reporting entity is itself such a plan, the sponsoring employers are also related to the reporting entity;
  - The entity is controlled or jointly controlled by a person identified in point one;
  - A person identified above has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

- In accordance with IAS 24, the Bank's related parties are:
  - the major shareholder and its related parties (entities included in the consolidation of Addiko Group);
  - Supervisory Board and Management members (i.e., key management personnel);
  - key management personnel family members; and
  - legal entities where the Bank holds significant equity interests (above 10%).

## 31. RELATED PARTY TRANSACTIONS (Continued)

The following table presents the assets and liabilities arising from the Bank's transactions with related parties:

| | 2019 | 2018 |
|---|---|---|
| **ASSETS** | | |
| **Foreign currency accounts:** | | |
| ADDIKO BANK d.d., Ljubljana, Republic of Slovenia | 1,311 | 570 |
| ADDIKO BANK d.d., Zagreb, Republic of Croatia | 3,300 | 1,089 |
| ADDIKO BANK d.d., Sarajevo | 524 | 525 |
| ADDIKO BANK a.d., Beograd, Serbia | 68 | 71 |
| ADDIKO BANK AG, Vienna, Austria | 11,563 | 3,680 |
| **Other assets, net:** | | |
| ADDIKO BANK d.d., Zagreb, Republic of Croatia | - | - |
| ADDIKO BANK d.d., Sarajevo | 19 | 3 |
| ADDIKO BANK a.d., Podgorica, Montenegro | 4 | - |
| ADDIKO BANK a.d., Beograd, Serbia | 2 | - |
| ADDIKO BANK AG, Vienna, Austria | 364 | - |
| ADDIKO BANK d.d., Ljubljana, Republic of Slovenia | 1 | 45 |
| EBRD | - | 80 |
| | **17,156** | **6,063** |
| **LIABILITIES** | | |
| **Demand deposits:** | | |
| ADDIKO BANK a.d., Beograd, Serbia | 62 | 25 |
| ADDIKO BANK a.d., Podgorica, Montenegro | 40 | 122 |
| ADDIKO BANK d.d., Zagreb, Republic of Croatia | - | - |
| ADDIKO BANK AG, Vienna, Austria | 98 | - |
| **Short-term deposits:** | | |
| ADDIKO BANK d.d. Sarajevo | 11,944 | - |
| ADDIKO BANK AG, Vienna, Austria | 12,716 | - |
| **borrowings:** | | |
| EBRD | - | 9,878 |
| **Other liabilities:** | | |
| ADDIKO BANK a.d., Beograd, Serbia | 276 | 328 |
| ADDIKO BANK d.d., Sarajevo | 277 | 153 |
| ADDIKO BANK d.d., Zagreb, Republic of Croatia | 113 | 67 |
| ADDIKO BANK a.d., Podgorica, Montenegro | 6 | 3 |
| ADDIKO BANK AG, Vienna, Austria | 811 | 463 |
| | **26,343** | **11,039** |

| **OFF-BALANCE SHEET ITEMS** | ***2019*** | ***2018*** |
|---|---|---|
| **Unused loan limit** | | |
| ADDIKO BANK d.d., Ljubljana, Republic of Slovenia | - | 19,558 |

## 31. RELATED PARTY TRANSACTIONS (Continued)

The following table presents the income and expenses arising from the Bank's transactions with related parties:

| | 2019 | 2018 |
|---|---|---|
| **Interest income:** | | |
| ADDIKO BANK d.d., Sarajevo | 4 | - |
| | | |
| **Fee and commission income:** | | |
| ADDIKO BANK d.d., Sarajevo | 15 | 17 |
| ADDIKO BANK d.d., Zagreb, Republic of Croatia | 1 | - |
| | | |
| **Other operating expenses:** | | |
| ADDIKO BANK d.d., Sarajevo | 17 | 20 |
| ADDIKO BANK AG, Vienna, Austria | 500 | 242 |
| | **537** | **279** |
| **Interest expenses**: | | |
| ADDIKO BANK AG, Vienna, Austria | (11) | (3) |
| ADDIKO BANK d.d., Sarajevo | (32) | (59) |
| ADDIKO BANK a.d. Beograd , Serbia | - | (105) |
| ADDIKO BANK d.d. Zagreb, Republic of Croatia | (6) | (3) |
| EBRD | (151) | (222) |
| **Fee and commission expenses:** | | |
| ADDIKO BANK d.d., Sarajevo | - | (722) |
| ADDIKO BANK d.d., Zagreb, Republic of Croatia | (30) | (8) |
| ADDIKO BANK d.d. Ljubljana, Republic of Slovenia | (44) | (44) |
| ADDIKO BANK a.d. Beograd , Serbia | (4) | (4) |
| EBRD | - | (37) |
| **Other operating expenses**: | | |
| ADDIKO BANK AG, Vienna, Austria | (841) | (535) |
| ADDIKO BANK d.d., Zagreb, Republic of Croatia | (477) | (461) |
| ADDIKO BANK d.d., Sarajevo | (4) | (6) |
| ADDIKO BANK d.d. Ljubljana, Republic of Slovenia | (3) | - |
| ADDIKO BANK a.d. Beograd , Serbia | (198) | (201) |
| | **(1,801)** | **(2,410)** |
| | **(1,264)** | **(2,131)** |

On July 12, 2019, the Bank's owner, Addiko Bank AG, became a listed entity in the Vienna Stock Exchange and the share of Al Lake (Luxembourg) S.à r.l, a parent, in indirect ownership of Advent International and the European Bank for Reconstruction and Development (EBRD), decreased to 44.99%.

Thus the indirect shareholding of EBRD fell below 10%, so that the table above includes only receivables and payables from/to EBRD for the previous year, while the income and expenses are presented up to July 12, 2019.

Salaries and payroll taxes and contributions paid to and on behalf of the Bank's Supervisory/Management Board members are provided below:

| | 2019 | 2018 |
|---|---|---|
| Net salaries | 451 | 441 |
| Payroll taxes and contributions | 295 | 288 |
| Severance pays and retirement benefits | - | - |
| Taxes and contributions payable on severance pays and retirement benefits | - | - |
| | **746** | **729** |

## 31. RELATED PARTY TRANSACTIONS (Continued)

The following table provides details on loans and deposits of the Bank's key management personnel and their family members:

| | 2019 | 2018 |
|---|---|---|
| *Supervisory Board, management and key managerial personnel* | | |
| **ASSETS** | | |
| ***Management Board*** | | |
| Loans | 6 | 10 |
| Impairment allowances | | |
| | | |
| ***Key management personnel*** | | |
| Loans | 441 | 423 |
| Impairment allowances | (23) | (25) |
| | | |
| ***Family members of the Bank's key management personnel*** | | |
| Loans | - | 5 |
| Impairment allowances | - | - |
| **Total assets** | **424** | **413** |
| | | |
| **LIABILITIES** | | |
| ***Management Board*** | | |
| Deposits | 30 | 17 |
| Provisions for contingent liabilities | - | - |
| | | |
| ***Key management personnel*** | | |
| Deposits | 288 | 515 |
| Provisions for contingent liabilities | - | - |
| | | |
| ***Family members of the Bank's key management personnel*** | | |
| Deposits | 99 | 104 |
| Provisions for contingent liabilities | - | - |
| | | |
| ***Members of the governing bodies and management of the Banking Group*** | | |
| Deposits | - | 26 |
| Provisions for contingent liabilities | - | - |
| **Total liabilities** | **417** | **662** |
| | | |
| ***Irrevocable crediting commitments*** | | |
| Supervisory Board | 14 | 14 |
| Management Board | 23 | 22 |
| Key management personnel | 34 | 65 |
| Family members of the Bank's key management personnel | 9 | 9 |
| **Total irrevocable crediting commitments** | **80** | **110** |

## 31. RELATED PARTY TRANSACTIONS (Continued)

The following table provides details on interest and fee and commission income and expenses relating to the Bank's key management personnel and their family members:

| | 2019 | 2018 |
|---|---|---|
| ***Supervisory Board*** | | |
| ***Management Board*** | | |
| Interest income | 1 | 1 |
| Fee and commission income | 2 | 2 |
| Other expenses | - | (4) |
| ***Key management personnel*** | | |
| Interest income | 20 | 23 |
| Interest expenses | (6) | (5) |
| Fee and commission income | 7 | 7 |
| Other expenses | - | (4) |
| ***Family members of the Bank's key management personnel*** | | |
| Interest income | - | - |
| Interest expenses | (2) | (1) |
| Fee and commission income | 1 | 1 |
| **Total** | **23** | **20** |

## 32. OPERATING LEASE ARRANGEMENTS

Operating lease is mostly related to office space leases for branches and the lease of space for ATM installation.

In 2019, the Bank recorded lease expenses under the items of interest expenses, depreciation and rental costs, as presented in the table below

| | 2019 |
|---|---|
| Interest expenses (Note 7.2) | 25 |
| Depreciation of assets leased (ROU assets, Note 20) | 525 |
| Rental costs (Note 13) | 385 |
| | **935** |

Total future minimum lease payments to be settled pursuant to the operating lease contracts involving the Bank as the lessee are provided below:

| December 31, 2019 | Within a year | From 1 to 5 years | After 5 years | Total |
|---|---|---|---|---|
| Interest expenses | 16 | 6 | - | 22 |
| Depreciation charge per ROU assets | 500 | 440 | - | 940 |
| Rental costs | 127 | 93 | - | 220 |
| **Total** | **643** | **539** | **-** | **1,182** |

| December 31, 2018 | Within a year | From 1 to 5 years | After 5 years | Total |
|---|---|---|---|---|
| Rental costs | 653 | 1,016 | - | 1,669 |

## 32. OPERATING LEASE ARRANGEMENTS (Continued)

Total future minimum lease payments to be collected pursuant to the long-term lease contracts were as follows:

| | 2019 | 2018 |
|---|---|---|
| Up to 1 year | 322 | 364 |
| From 1 to 5 years | 750 | - |
| After 5 years | - | - |
| | 1,072 | 364 |

The Bank's operating lease income in the financial year 2019 amounted to BAM 385 thousand (2018: BAM 405 thousand).

## 33. EVENTS AFTER THE REPORTING PERIOD

The rapid development of the Covid-19 virus and its social and economic impact in Republic of Srpska and globally may result in assumptions and estimates requiring revisions which may lead to material adjustments to the carrying value of assets and liabilities within the next financial year. At this stage management is not able to reliably estimate the impact as events are unfolding day-by-day.

In addition, on March 20, 2020, the Banking Agency of the Republic of Srpska enacted the Decision on Provisional Measures to be Taken by Banks for Mitigation of Adverse Economic Consequences Caused by Viral Disease, COVID-19 (the "Decision to prescribe special measures that banks may approve to clients such as: debt moratorium or postponed repayment of loan principal and payment of interest on loans, which may last as a minimum until cessation of the state of emergency, introduction of grace period for principal repayment of no more than 6 months, approval of additional exposure amount for overcoming a client's current liquidity difficulties and maintenance of a client's business, and other measures in in order to facilitate liability settlement on the part of clients and support maintenance and preservation of their business. The Bank's management is currently, within a single working day after enactment of the Decision, which, at the time of preparation of this Note, has not yet become effective, unable to estimate the effects of the Decision on the Bank's financial statements.

The longer term impact may also affect lending and trading volumes, cash flows and profitability. Nevertheless at the date of these financial statements the Bank continues to meet its obligations as they fall due and therefore continues to apply the going concern basis of preparation."

Except for the foregoing, there have been no significant events after the reporting date that that would require adjustment to or disclosure in the notes to the Bank's financial statements for 2019.

## 34. TAXATION RISKS

The Republic of Srpska and Bosnia and Herzegovina currently have several tax laws in effect, as imposed by various governmental agencies. The applicable taxes include: a turnover tax, corporate tax, and payroll (social insurance) taxes, among others. Hence, few precedents with regard to tax issues have been established in the Republic of Srpska. Often, contrary opinions pertaining to legal interpretations exist both among, and within, governmental ministries and organizations, thus creating uncertainties and areas of legal contention. Tax returns, along with other legal compliance matters (e.g., customs and currency control matters) are subject to the review and investigation by a number of authorities that are legally enabled to impose extremely severe fines, penalties and interest charges.

The interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Bank and the Group may not coincide with that of the management. As a result, transactions may be challenged by tax authorities and the Bank may be assessed additional taxes, penalties and interest, which can be significant. In accordance with the Law on Tax Administration of the Republic of Srpska, expiration period of the tax liability is five years. This virtually means that tax authorities could determine payment of outstanding liabilities in the period of five years from the origination of the liability. The aforedescribed situation creates tax risks in the Republic of Srpska that are substantially more significant than those typically existing in countries with more developed tax systems.

## 35. EXCHANGE RATES

The official exchange rates for major currencies as of December 31, 2019 and 2018 used in the translation of statement of financial position components denominated in foreign currencies into BAM were as follows:

| | | In BAM |
|---|---|---|
| | December 31, 2019 | December 31, 2018 |
| USD | 1.747994 | 1.707552 |
| CHF | 1.799126 | 1.742077 |
| EUR | 1.955830 | 1.955830 |

# Glossary

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|---|---|
| ABC | Addiko Bank d.d., Croatia |
| ABBL | Addiko Bank a.d., Bosnia & Herzegovina (Banja Luka) |
| ABH | Addiko Bank AG, Austria (Holding) |
| ABM | Addiko Bank a.d., Montenegro |
| ABS | Addiko Bank d.d., Slovenia |
| ABSA | Addiko Bank d.d., Bosnia & Herzegovina (Sarajevo) |
| AC | Amortised costs |
| Associated company | A company over which a material influence is exerted in terms of its business or financial policy and that is recognised in the consolidated accounts using the equity method |
| Banking book | All risk-bearing on- and off-balance-sheet positions of a bank that are not assigned to the trading book |
| Bank@Work | An alternative sales channel, focusing on delivering the convenience promise as a main advantage to the customer. Branch teams are regularly visiting large companies' headquarters with mobile equipment, presenting Addiko's product and service offer, opening products on the spot or helping potential customers applying for a loan |
| CDS | Credit default swap; a financial instrument that securitizes credit risks, for example those associated with loans or securities |
| Change CL/GPL | Change in CL / gross performing loans |
| CL | Credit loss |
| CMA & CML | Customer Margin Assets (CMA) and Liabilities (CML) is as Gross Margin respectively on the asset and liability side, including the booked regular and interest like income and calculatoric costs and benefits defined within the Fund Transfer Pricing methodology |
| Cost/income ratio (CIR) | Operating expenses / (Net interest income + Net fee and commission income) |
| Cost of risk ratio | Credit loss expenses on financial assets/Credit risk bearing exposures |
| CRB | Credit Risk Bearing |
| Credit institutions | Any institution undertaking the business of which is to take deposits or other repayable funds from the public and to grant credits for its own account according to the Law on Banks |
| CSF | "Central Steering Functions" and designated services that have the character of shareholder activities and are therefore provided and charged solely to Addiko. CSF are related to strategic direction, coordination, support, monitoring and steering, e.g. human resources, legal, marketing |
| Customer loans | Exposure of on balance loans including accrued interest, gross amount of provisions of performing and non performing loans |
| Derivatives | Financial instruments whose value depends on the value of an underlying asset (such as stocks or bonds). The most important derivatives are futures, options and swaps |
| Fair value | Price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants on the measurement date |
| FDI | Foreign Direct Investment |
| FVTOCI | Fair value through OCI |
| FVTPL | Fair value through Profit or Loss |
| FX & DCC | Foreign exchange and Dynamic currency conversions |
| General governments | Central governments, state or regional governments, and local governments, including administrative bodies and non-commercial undertakings, but excluding public companies and private companies held by these administrations that have a commercial activity (which shall be reported under “credit institutions”, “other financial corporations” or “non-financial corporations” depending on their activity); social security funds; and international organisations, such as |

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|---|---|
| | institutions of the European Union, the International Monetary Fund and the Bank for International Settlements |
| Gross disbursements | Disbursements include disbursements of term loans (Consumer- Mortgage and Housing loans and Corporate term loans, not including revolving loans) and internal refinancing which relates to intra – bank transactions |
| Gross exposure | Exposure of on and off balance loans including accrued interest, gross amount of provisions of performing loans and non performing loans |
| Gross performing loans | Exposure of on balance loans without accrued interest and no deduction of provisions of performing loans |
| GSS | Means "group shared services" and designates services that are aimed at providing economic or commercial value to Group members by means of enhancing or maintaining their business position, e.g. transaction banking, back office, digital banking. GSS do not relate to shareholder activities, i.e. activities performed solely because of a shareholding interest in one or more other Group members, and are provided and charged to the respective receiving Group member |
| Households | Individuals or groups of individuals as consumers and producers of goods and non-financial services exclusively for their own final consumption, and as producers of market goods and non-financial and financial services provided that their activities are not those of quasi-corporations. Non-profit institutions which serve households (“NPISH”) and which are principally engaged in the production of non- market goods and services intended for particular groups of households shall be included |
| Large Corporates | The Segment Large Corporates includes legal entities and entrepreneurs with annual gross revenues of more than EUR 40 million |
| LCR | Liquidity coverage ratio; the ratio of high quality liquid assets and net cash flows in the next 30 days |
| Leverage ratio | The ratio of Tier 1 capital to specific exposures on and off the statement of financial position calculated in accordance with the methodology set out in Decision on capital calculation in Banks |
| Loans and receivables | Gross carrying amount of loans and receivables less ECL allowance |
| Loan to deposit ratio | Indicates a bank's ability to refinance its loans by deposits rather than wholesale funding. It is based on net customer loans and calculated with loans to non-financial corporations and households in relation to deposits from non-financial corporations and households. Segment level: Loans and receivables divided by financial liabilities at amortised costs |
| Loss identification period (LIP) | The time span from the default of the client until the recognition of the default in the Bank |
| Net banking income | The sum of net interest income and net fee and commission income |
| Net interest income (segment level) | Net interest income on segment level includes total interest income related to effective interest rate from gross performing loans, interest income from NPE, interest like income, interest expenses from customer deposits, consideration of funds transfer pricing and allocated contribution from interest and liquidity gap |
| NIM | Net interest margin is used for external comparison with other banks as well as an internal profitability measurement of products and segments. It is calculated with net interest income set in relation to average interest-bearing assets (total assets less investments in subsidiaries, joint ventures and associates, intangible fixed assets, tangible fixed assets, tax assets and other assets) |
| Non-financial corporations | Corporations and quasi-corporations not engaged in financial intermediation but principally in the production of market goods and non-financial services |
| NPE | Defaulted, non-performing exposure (Gross Carrying Amount). A default and thus a non-performing exposure applies if it can be assumed that a customer is unlikely to fulfill all of its credit obligations to the bank, or if the debtor is overdue at least 90 days on any material credit obligation to the bank |

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| NPE ratio | Is an economic ratio to demonstrate the proportion of loans that have been classified as defaulted non-performing in relation to the entire customer loan portfolio. The definition of non-performing has been adopted from regulatory standards and guidelines and comprises in general those customers where repayment is doubtful, a realization of collaterals is expected, and which thus have been moved to a defaulted customer rating segment. The ratio reflects the quality of the loan portfolio of the bank and provides an indicator for the performance of the bank's credit risk management. Non performing exposure/credit risk bearing exposure (on and off balance) |
| NPE coverage ratio | Describes to which extent defaulted non-performing exposure have been covered by impairments (individual and portfolio-based loan loss provisions) thus expressing also the ability of a bank to absorb losses from its NPE. It is calculated with impairment losses set in relation to defaulted non-performing exposure |
| NPE collateral coverage | Collaterals allocated to non-performing exposure / non-performing exposure |
| Option | The right to buy (call) or sell (put) an underlying reference asset at an agreed price with-in a specific period of time or at a fixed point in time |
| OTC | Over the counter; trade with non-standardised financial instruments directly between the market participants instead of through an exchange |
| Other financial corporations | All financial corporations and quasi-corporations other than credit institutions such as investment firms, investment funds, insurance companies, pension funds, collective investment undertakings, and clearing houses as well as remaining financial intermediaries, financial auxiliaries and captive financial institutions and money lenders |
| PI | Private individuals |
| POCI | Purchased or originated credit impaired assets |
| Public Finance | The Segment Public Finance includes all state-owner entities |
| Regular interest income | Regular interest income is related to nominal interest rate from gross performing loans excluding income from origination fees, penalty interests and funds transfer pricing |
| Repossessed assets | Assets acquired during the forced collection process of NPE portfolio |
| Retail (PI/Micro) | The Segment Retail includes the following categories: (i) PI, private individuals that are not representing a group, company, or organisation and (ii) Micro, includes private entrepreneurs and profit-oriented entities with annual gross revenues of less than BAM 0.5 million |
| Risk-weighted assets (RWA) | On-balance and off balance positions calculated in accordance with Decision on capital calculation in Banks |
| Return on tangible equity | Calculated as adjusted result after tax divided by the simple average of equity attributable to the owners adjusted for intangible assets of the parent for the respective period |
| SME | Within this corporate segment small & medium corporate businesses are included with an annual gross revenue between EUR 8 million and EUR 40 million. |
| Stage 1 | Impairment stage which relates to financial instruments for which expected credit loss model applies and for which no significant increase in credit risk has been recorded since their initial recognition. The impairment is measured in the amount of the 12-month expected credit loss |
| Stage 2 | Impairment stage which relates to financial instruments for which expected credit loss model applies and for which are subject to significant increase in credit risk has been recorded since their initial recognition. The impairment is measured in the amount of the lifetime expected credit loss |
| Stage 3 | Impairment stage which relates to financial instruments for which expected credit loss model applies and which are credit-impaired. The impairment is measured in the amount of the lifetime expected credit loss |
| Total capital ratio (TCR) | all the eligible own fund, presented in % of the total risk according to Decision about capital management |

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|---|---|
| Tier 2 capital | Tier 2 capital – T 2 consist of the sum of Tier 2 capital after regulatory adjustment according to Decision on capital calculation in Banks |
| TLOF | Total liabilities and own funds |
| Viber | Viber is a free chat service for smartphones and desktop computers. The program enables IP telephony and instant messaging between Viber users via the Internet |
| Yield GPL (simply Ø) | Regular interest income / simply Ø gross performing loans |

# Imprint

**Publisher of the Financial Report**
**and responsible for the content:**
Addiko Bank a.d
Aleja Svetog Save 13
78 000 Banja Luka
Tel. +387 (0)51 951 000
Fax +387 (0)51 336 518
www.addiko-rs.ba

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