ProCredit Bank

Annual report 2020

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This version of the annual report is a translation from the original, which was prepared in Bosnian 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 the report and the original language version of the annual report take precedence over this translation.

Key financial figures

ProCredit Bank d.d. Sarajevo (.000 BAM)	December 31 2020	December 31 2019	Change
BALANCE SHEET			
Cash, Central bank and other financial institutions balances	135,499	135,293	0.2%
Loans and advances to customers	449,400	398,254	12.8%
Other assets	22,641	19,436	16.5%
Liabilities to customers	330,544	282,167	17.1%
Liabilities to banks and financial institutions (inc. Subdebt)	229,508	217,826	5.4%
Other liabilities	3,684	3,885	(5.1%)
Equity	43,804	49,105	(10.8%)
Total assets (Liabilities and equity)	**607,540**	**552,983**	**9.9%**
STATEMENT OF PROFIT AND LOSS			
Net Interest Income	12,520	9,679	29.3%
Loss allowances	(1,751)	(692)	183.5%
Net fee and commission income	4,182	4,330	(4.5%)
Operating income	25,437	22,897	12.0%
Operating expenses	(23,128)	(23,690)	(2.3%)
Profit/loss for the period	507	(1,559)	
KEY INDICATORS			
Return of average equity (RoAE)	1.1%	(3.1%)	
Cost Income Ratio	90.2%	103%	13.3 pp
Deposit to loan ratio	73.6%	71%	2.7 pp
CAPITAL RATIOS			
RWA – Risk Weighted Assets	352,907	331,493	6.5%
CAR - Capital Adequacy Ratio	14.5%	15.0%	0.5 pp
OPERATIONS			
No. employees	148	140	6%
Business units	**6**	**6**	

OUR MISSION

Be the leading bank for SME

Financial year in brief

STRENGHTENED MARKET POSITION AND FOCUS ON SUSTAINABILITY

- "Housebank" concept as catalyst to support SMEs in a challenging market environment
- Strong portfolio growth of 13.5%
- Share of "green loans" in total loan portfolio 18.5%
- Deposit growth of 17%
- NPL of 2.6%
- Improved internal environmental footprint

GUIDANCE FOR 2021

- Planned growth of new to bank clients
- Above market average customer deposit and loan portfolio growth
- Further increase of share of "green loans" in total loan portfolio
- Improved cost/income ratio
- Operation income growth
- Capital adequacy ratio, above limits

BASIC INFORMATION ABOUT PROCREDIT BANK

Strategy

ProCredit Bank is focused on providing banking services to small and medium enterprises as well as direct banking services to individuals. The Bank operates within the ProCredit Group, which operates in Southeast Europe, Eastern Europe, South America and Germany. The owner of the bank is ProCredit Holding based in Frankfurt am Main, Germany.

Through business activities, we strive to achieve a stable return on invested capital of shareholders while contributing to economic, social and environmental development in the areas of business. The business strategy of the group / bank is based on a long-term relationship with our clients and employees as well as a conservative appetite for risks. The Group / Bank does not perform speculative business activities.

Self-sustainability is one of the key components of the bank's business strategy with the desire that business activities have a positive and self-sustainable contribution to the environment and society. Each bank within the group coordinates its own activities using a comprehensive environmental management system. The impact on the environment, both our own activities and the activities of our clients, is being analyzed. Within this process, we encourage clean or green investment projects, especially in energy efficiency and renewable energy projects.

The bank aims to fulfill the role of "Housebank" of our clients. As such, the goal is to be their first contact for banking lending, deposit and payment services. Our clients, small and medium enterprises, generally require financing ranging from 50,000 to 3 million EUR. Specializing in financing small and medium enterprises, the bank recognizes special customer requirements for banking services, offering a range of financing services, deposit and transaction operations. Our client group consists of innovative companies that show dynamic growth and development as well as a stable and formalized structure. Through our activities we want to contribute to the creation of new jobs, increase of innovative capacities and investment in environmentally friendly projects. Special attention is paid to "green" financing and local production, especially in agriculture. Our approach is based on the careful selection of clients, who operate stably, transparently and socially responsibly. We believe that our clients contribute significantly to the formal sector, social and economic development. At the same time, the bank has clear requirements for clients in terms of ethics of business practices as well as environmental responsibilities.

In addition to serving small and medium enterprises, the bank strives to promote direct banking for individuals. The comprehensiveness of "online" services enables the development of long-term cooperation with clients. In general, the bank does not offer counter and cash transactions, and the bank's clients can use the services through our digital channels, that is extremely useful for all parties in the pandemic.

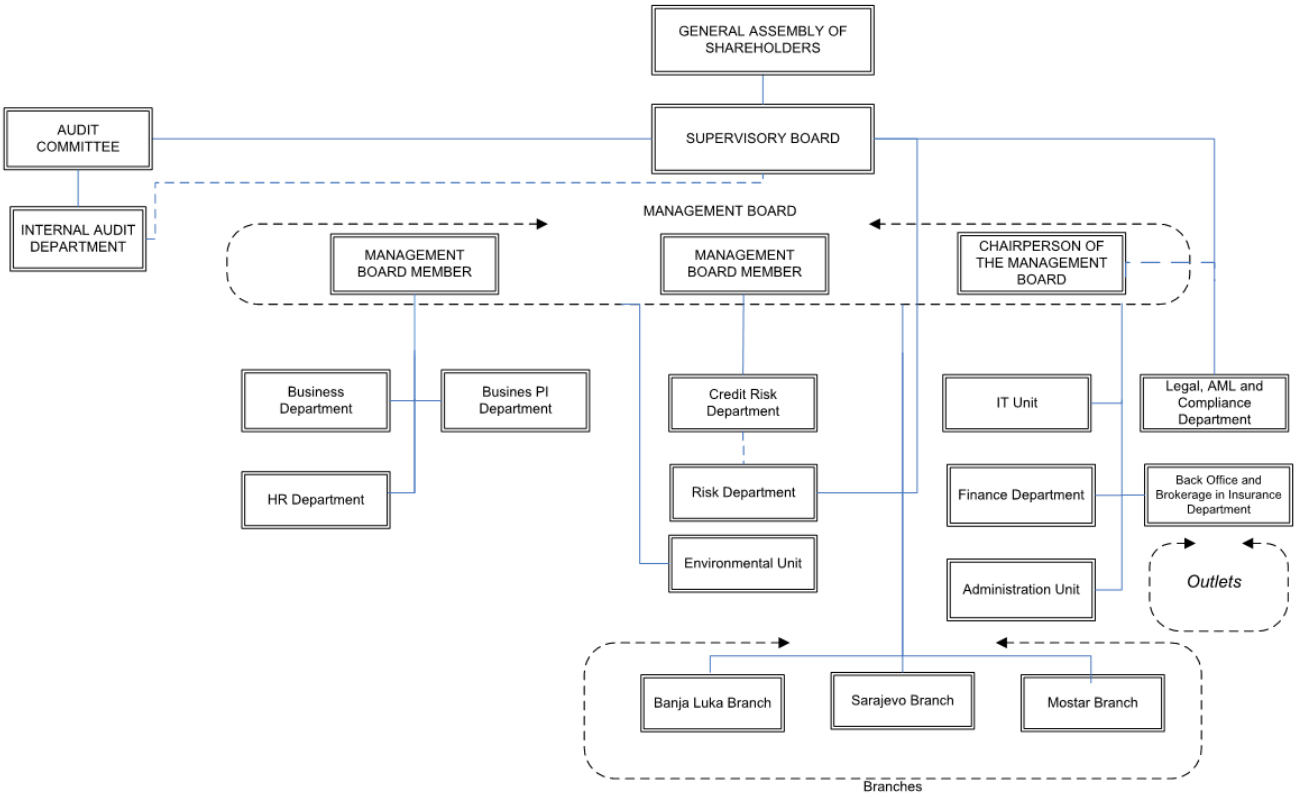
The bank's risk strategy reflects a clearly defined business model, a high degree of diversification and careful selection and continuous training of employees. The quality and motivation of employees is one of the key factors in achieving business goals. The selection of employees is done with special care, offering the possibility of a long-term career. In order to ensure the continuity of education, the group has developed a program of various trainings that are held within its own training centers. In addition, a Code of Conduct was implemented and it defines corporate values, adherence to common values of mutual respect and responsible behavior in everyday activities.

Bank owner

ProCredit Bank is 100% owned by ProCredit Holding, which is registered as a limited partnership. The most significant shareholders of the Holding are: Zeitinger Invest GmbH 17.0%, KfW 13.2%, DOEN Participaties B.V. 12.5%, International Finance Corporation IFC 10.0%, TIAA 8.6% and ProCredit Staff Invest.

The largest single shareholder is Zeitinger Invest GmbH, Frankfurt am Main, who is also the key initiator of the formation of the ProCredit Group. KfW is one of the most important development banks with the aim of promoting economic, social and environmental life around the planet on behalf of the Federal Republic of Germany. Other shareholders are development-oriented institutions that have activities around the world. The development institutions are crucial in forming the business model of the ProCredit Group and the bank.

Organizational chart of the bank



Detailed information about bank's corporate structure can be found in Note 1 of the financial statements.

REPORT ON THE ECONOMIC POSITION OF THE BANK

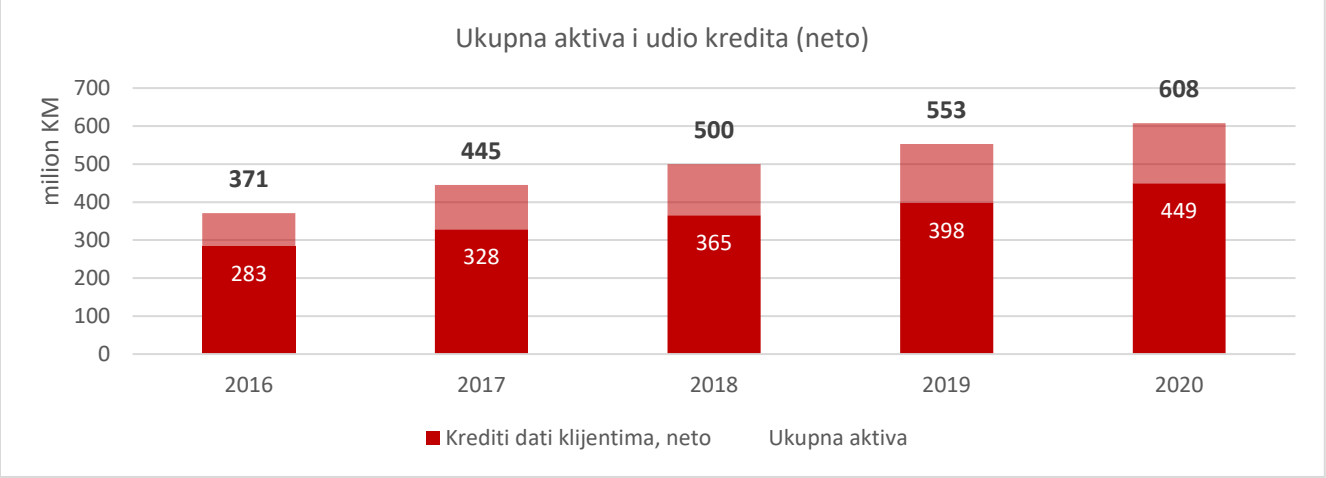
Course of business operations

The overall business result last year was positive despite the challenges caused by the COVID-19 pandemic. The total gross loan portfolio grew by 13.4% compared to 2019, which is the largest single growth in the banking market. A significant share of the loan portfolio are "green" or "green" loans approved for environmentally friendly projects. Client deposits also recorded a positive development, growing by more than 17% or about BAM 48 million. The Bank achieved a positive financial result of BAM 507 thousand, while a year earlier it achieved a negative result in the amount of BAM 1,559 thousand. In 2020, the Bank achieved an operational and financial result in accordance with the business plan created in the period before the COVID-19 pandemic.

In accordance with the mission and strategy, the Bank focuses on the provision of services to small and medium enterprises, which is reflected in the structure of assets, especially the loan portfolio. The largest part of the loan portfolio is loans granted to legal entities, which is the reason why the bank does not report loan and deposit development as separate business segments according to the type of client. The operational data presented will include loans and deposits from legal entities and individuals.

Assets

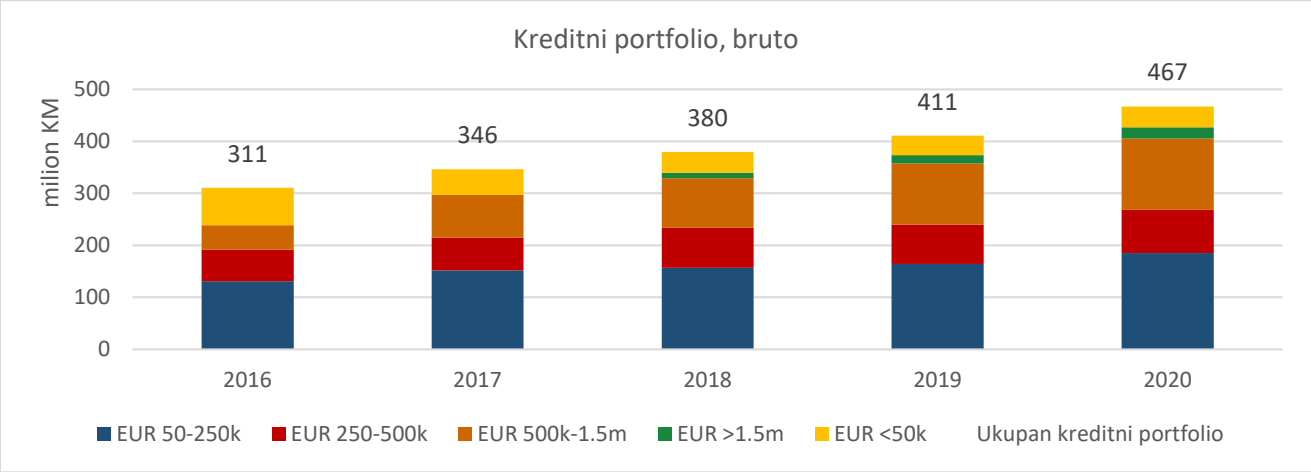
The total assets of the bank increased by BAM 54.5 million or 10%, of which the growth of loans to customers is significant. The Bank also retained stable funds held with the Central Bank of BiH and other financial institutions, satisfying all liquidity requirements. In order to optimize assets and liquidity needs and position, as well as more efficient cost management, in 2020 the bank purchased treasury bills issued by the FBiH Government for BAM 5 million, with a maturity of 12 months or half of 2021. The Bank has its own real estate from other asset items and there were no significant new investments. The Bank owns a number of properties acquired in the collection process, 2020: BAM 1.5 million (2019: BAM 2.3 million) over which regular fair value testing is performed and if necessary a reduction in accordance with the requirements of the regulator.



Total bank asset and net loan portfolio

The portfolio of loans granted to clients grew by BAM 51 million or 12.8%, which is one of the highest growth rates on the market. The overall growth is in line with the plan defined by the bank in the period before the COVID-19 pandemic. The bank's activities were in line with the regulator's recommendations that in the conditions of growing need for liquidity on the market, the process of credit financing should not be stopped.

Noting that the bank has conservative risk appetites and approved loans have undergone a process of detailed credit analysis and assessment.

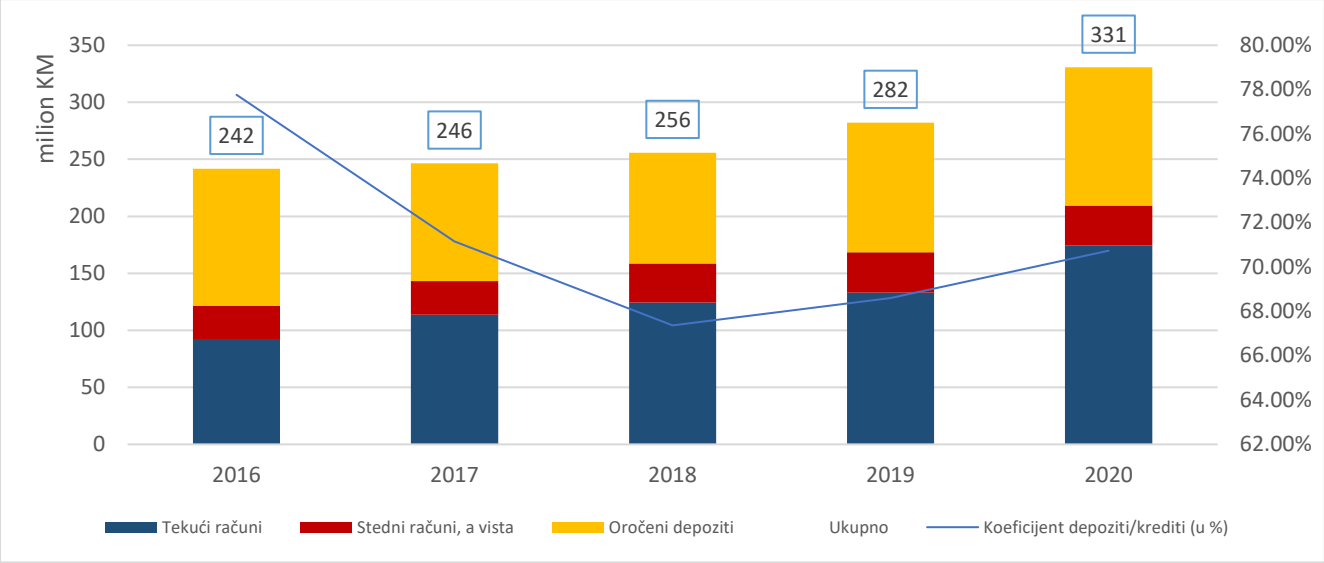


Loan portfolio, by the amount of approved loan

The basic parameter for classifying credit clients is the credit exposure in the bank. This parameter is also used when displaying the bank's total loan portfolio. The most significant part of the loan portfolio are loans granted to legal entities with a share higher than 95%.

Liabilities and equity

The bank's liabilities or liabilities mainly consist of customer deposits and liabilities for loans received from financial institutions. Client deposits are the most important position of funding sources and by the end of 2020 they accounted for 59% (2019: 56%). The growth of deposits compared to last year was BAM 48 million or over 17%. At the same time, the share of deposits compared to other sources has improved. The growth of deposits was realized on current and term accounts. The deposit-to-credit ratio improved in 2020 to 70.7% (2019: 68.6%).



Customer deposits

Other sources of financing, loans taken from financial institutions also increased compared to 2019 by 5.4% and the total share of these liabilities in sources decreased compared to the previous year. The Bank uses loans from related parties from ProCredit Holding, and short-term sources from ProCredit Bank Germany. Other creditors of the bank are relevant international financial institutions.

The bank's equity, despite the positive result, was reduced compared to 2019, due to the application of the new Decision on credit risk management and determination of expected credit losses. The first application of the Decision was on 01.01.2020. and the total effect on equity was BAM (5,829) thousand.

Operational result

Profit for 2020 amounts to BAM 507 thousand (2019: BAM 1,559 thousand), which results in a slight return on capital. Net interest income increased by BAM 2.8 million or 29.4% compared to the previous year. The growth of the loan portfolio is the primary generator of income growth, while the stabilization of the interest margin to a lesser extent had a positive impact on income trends. The net interest margin in 2020 increased by 0.3 percentage points compared to the year before.

Increased provisions for potential credit losses mitigated the positive development of interest income. In a pandemic situation, banks have identified certain industries where increased credit risks are possible. In accordance with that, it increased its reserves, which does not have to be realized in the following period. Compared to the previous year, the costs of reserves increased by BAM 1 million or 153%.

The development of net fee and commission income decreased by 3.4% due to a smaller number of transactions during the pandemic period and restrictions on movement, with a recovery in the second half of the year. As the bank 100% transaction banking works through digital platforms, the recovery period was relatively fast and without further negative trends. This negative effect was annulled in volume by positive trends from revenues from transactions and foreign currency conversions. Revenue from FX transactions increased by 28% or BAM 241 thousand. The bank expects positive development in the coming period as well, and is the result of an increased volume of transactions and new clients who use the competitive advantages of foreign payments offered by the bank.

Administrative and staff costs declined slightly, mostly due to lower business travel and overhead costs. Employee costs also declined slightly due to certain severance payments in 2019.

The financial position of the bank as well as the result in 2020 show the stability of business activities. The Bank complied with all obligations and requirements throughout the period.

REPORT ON EXPECTED DEVELOPMENTS

Macroeconomic environment and competitive situation

In 2020, there was a collapse in the global economy due to COVID-19 pandemic. Global supply and demand were significantly constrained. IMF forecasted B&H GDP rate at decrease for 5.5% for 2021 initial forecast was at 5%, which was lately corrected to 3.5%. For following year it is projected annual rate in average of 3%. Although, IMF projected recovery in 2021 the pandemic challenges will still play important role mainly due to uncertainty with vaccination which is important for further stabilization.

Operations of banking sector showed signs of lending slowdown or completely constrains from loan approval. Customer deposits stock continued to grow during 2020 with under average rate. Most of the banks on market recognized increase in credit risk which was reflected in profitability. For 2021 the bank expects increase in credit activity which could be in line with recovery expectation. 2010 will be more competitive with more banks involved in lending activities. The Bank forecasts these developments. And with business adjustments from previous year together with close client relationship and their business partners we believe that the bank can achieve positive and profitable medium term growth.

Expected development of the bank

In 2020 the bank slightly increased its total assets and loan market share. Significant growth, above market average, of loans to customers is achieved. For 2021 and in medium term, we plan market position improvements and to see good potential for long-term, profitable and sustainable growth.

In addition to expanding our market position, our focus remains on strengthening the business relationships with our clients. It gives us hope that existing customers have so far been able to weather the economic consequences of the pandemic. Nevertheless, the 2021 financial year will also present many challenges.

For 2021 and in the medium term, the bank plan to achieve customer loan portfolio growth in line with historical development. We plan to increase share of “green” portfolio up to 20% with further increase of promotion and environmental activities. Expectation in green part is based on growing need potential in energy efficiency and renewable energy.

We are planning solid growth in customer deposits in 2021and in medium term. This growth is achievable by acquiring new loan and non-loan clients, legal and physical entities. Direct (digital) banking concept, as well as simple services are useful tools to attract new clients. These clients have recognized positive sides of cashless concept during the pandemic.

Liabilities to banks and other financial institutions are other important source of funding for the bank. In 2021 plan is to increase borrowed funds similarly as in 2020 and in following years in smaller range. Total liabilities are planned to grow from 7.7% in 2021 and from 9 to 11% in next years.

The Capital Plan forecasts capital increase in 2021 in amount of BAM 11.7 million together with subordinated debt conversion to equity in amount of BAM 8.8 million. The bank in 2019 has started procedure for capital increase in amount of BAM 3.9 million for which all necessary approval are given. To complete whole process only final resolution from local Securities Commission is needed.

For 2021, we expect a largely positive interest and net interest income development. In line with growth forecast of interest bearing assets. An annual growth for the net interest income in 2021 is planned, mainly from loan portfolio growth and effects from sub debt conversion. Subordinated debt conversion can lead to BAM 500 thousand interest expenses savings. For the following years growth rate will be in average from 9 to 11%, which is under the growth rate for loan portfolio due to conservative planning in interest rates.

Fee and commission income and other incomes are planned in 2021 in a range similar to year before, while related expenses goes in line with expected inflation and service volume. Planned growth rate for administrative expenses in 2021 is mainly driven by the implementation of new digital services and platforms. Personnel expenses reflects projections for slightly staff number increase and salary revisions. In addition, the bank has planned education expenses from internal training centers and specific out of the group courses.

All above projections as a result have positive development in cost to income ratio.

The bank expects that cost of risk to remain elevated in 2021, albeit below the 2020 level for 8%. This reflects expectations for increase of credit risk for certain industries, above all HORECA.

In total the bank forecasted profit for 2021 in amount which is better than in 2020, and improved return on equity in following five years.

With these projections and with planned capital increase, capital adequacy ratios will be well above regulator's limits for the next five years.

Assessment of business opportunities and risks

In principle, the COVID-19 pandemics disturbed foreign trade and labor market. Also, it affected and caused uncertainty in our planning till full normalization is reached. Prolongation of the effects can affect lower loan portfolio growth rate thus resulting in lower profitability.

We are of the opinion that the business model of the bank is not jeopardized in these scenarios. Moreover, it is strengthened with already started capital increase processes. Planned capital increase reflects strong support from of the bank, and this is recognized by FITCH credit rating agency. In April, 2021 FITHC confirmed credit ratinf for ProCrredit Holding of BBB, and for the bank B+, Stable.

The bank managed to generate strong loan portfolio growth rate, mostly due to good and close customer relationship and conservative risk appetite. In principle, uncertain macroeconomic environment has some challenges yet there is some signs of opportunities for the bank to remain reliable partner for SMEs. In the medium term, we believe in some positive trends and opportunities for profitable growth.

Energy Trade d.o.o. – Solar Power Plant. ProCredit Bank client

DISCLOSURES REQUIRED BY THE LAW ON ACCOUNTING AND AUDITING SECTION C

The bank did not have any significant post balance sheet events that might have the effect on financial statements as of 31 December 2020. All transactions performed are regular and in line with business model of the bank and do not differ from usual transactions.

In previous chapters the banks has provided details on business operations and forecasts. In line with mentioned, the bank except development of customer made services in line with the business model does not conduct specific development and research. In addition, the bank does not plan to purchase its shares. Capital development is described in previous paragraphs.

This report should be read together with the financial reports and notes with financial reports where risk report and risk management of the banks is described in more details.

ProCredit Bank

Financial statements 2020

Responsibilities of the Management and Supervisory Board for the preparation and approval of the financial statements

The Management Board is required to prepare financial statements, which give a true and fair view of the financial position of the Bank and of the results of its operations and cash flows, in accordance with applicable accounting standards, and is responsible for maintaining proper accounting records to enable the preparation of such financial statements at any time. Management has a general responsibility for taking such steps as are reasonably available to it to safeguard the assets of the Bank and to prevent and detect fraud and other irregularities.

The Management Board is responsible for selecting suitable accounting policies to conform with applicable accounting standards and then applying them consistently; making judgments and estimates that are reasonable and prudent; and preparing the financial statements on a going concern basis unless it is inappropriate to presume that the Bank will continue in business.

The Management Board is responsible for the submission to the Supervisory Board of its annual financial statements, following which the Supervisory Board approves the financial statements for submission to the General Assembly for adoption.

The financial statements set out on pages 21 to 110 were authorised by the Management Board on 31 May 2021 for issue to the Supervisory Board, and are signed bellow to signify this, on behalf of the Bank, by:

For and on the behalf of Management Board

President of the Management Board
Amir Salkanović

ProCredit Bank d.d. Sarajevo

Member of Management Board
Amina Durmo Trlin

ProCredit Bank d.d. Sarajevo
Franca Lehara bb
71000 Sarajevo
Bosna i Hercegovina
31 May 2021

KPMG

Independent Auditors' report

To the shareholders of ProCredit Bank d.d. Sarajevo

Opinion

We have audited the financial statements of ProCredit Bank d.d. Sarajevo ("the Bank"), which comprise the statement of financial position as at 31 December 2020, the statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank as at 31 December 2020 and of its financial performance and its cash flows for the year then ended in accordance with the statutory accounting requirements applicable to banks in the Federation of Bosnia and Herzegovina.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditors' 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' International Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code), together with the ethical requirements that are relevant to our audit of the financial statements in Federation of Bosnia and Herzegovina, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

KPMG

Independent Auditors' report
To the shareholders of ProCredit Bank d.d. Sarajevo (continued)

Key Audit Matters

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

Impairment of loans and receivables from customers

As at 31 December 2020, gross loans and receivables: BAM 467 million, related impairment allowance: BAM 18 million and impairment loss recognised in the income statement for the year then ended: BAM 1.7 million (31 December 2019: gross loans and receivables: BAM 411 million, impairment allowance: BAM 13 million and impairment loss recognised in the income statement for the year then ended: BAM 0.6 million).

Refer to Note 2.6 Changes in accounting policies due to the application of the *Decision on credit risk management and determination of expected credit losses* and Note 5 Transition to calculation of expected credit losses in accordance with the new regulatory requirements.

Refer to Note 3 Significant accounting policies, Note 4 Critical accounting judgements and key sources of estimation uncertainty, Note 21 Loans and receivables to customers, and Note 6.1 Credit risk.

Key audit matter	How our audit addressed the matter
Impairment allowances represent Management Board's best estimate of the expected credit losses ("ECLs") within loans and receivables from customers (collectively, "loans", "exposures") at the reporting date. We focused on this area as the measurement of impairment allowances requires the Management Board to make complex and subjective judgements over the amounts of such impairment. Since 1 January 2020, in accordance with the requirements of the Federal Banking Agency of the Federation of Bosnia and Herzegovina ("FBA"), the Bank has applied a new impairment model which combines the requirements of IFRS 9 "Financial Instruments" applied by the Bank in earlier periods with the prescribed minimum requirements for provisioning.	Our audit procedures in this area, performed, where applicable, with the assistance of our own valuation, financial risk management and information technology (IT) specialists included, among others: • Inspecting the Bank's ECL methods and models, and assessing their compliance with the relevant requirements of the regulatory and financial reporting framework. As part of the above, we challenged the Management Board on whether the level of the methodology's sophistication is appropriate based on an assessment of the entity-level factors; • Making relevant inquiries of the Bank's risk management and information technology (IT) personnel in order to obtain an understanding of the provisioning process, IT applications used therein, key data sources and assumptions used in the ECL model. Also, assisted by our own IT specialists, assessing and testing of the Bank's IT control environment for data security and access; • Testing the design, implementation and operating effectiveness of selected controls over the approval, recording and monitoring of loans, including, but not limited to, the controls relating to the identification of significant increase in credit risk, loss events and default, appropriateness of the classification of exposures into performing and non-performing and their segmentation into homogenous groups, calculation of days past due, collateral valuations and calculation of the impairment allowances.

Key Audit Matters (continued)

Key audit matter	How our audit addressed the matter *(continued)*
The impairment allowances for the performing exposures (Stage 1 and Stage 2 in the framework's hierarchy) and Stage 3 below EUR 50 thousand individually are determined by modelling techniques relying on key parameters such as the probability of default (PD), exposure at default (EAD) and loss given default (LGD), taking into account historical experience, identification of exposures with a significant deterioration in credit quality and forward-looking information, as well as specific rules of the FBA regarding various minimum provisioning requirements (together "collective impairment allowance"). Expected credit losses for individually significant Stage 3 (non-performing) exposures (above EUR 50 thousand) are determined on an individual basis by means of a discounted cash flows analysis. The process involves subjectivity and reliance on a number of significant assumptions, including those in respect of the probable sale proceeds from the related collateral and the minimum period for collateral disposal, as well as the FBA's specific minimum provisioning requirements.	• Evaluating whether in its loan staging and ECL measurement the Bank appropriately considered the effects of the market disruption resulting from the COVID-19 pandemic; • With respect to the adoption of the FBA's new requirements: — Obtaining understanding of the overall transition process activities and testing whether the prescribed minimum requirements were applied at the transition date, as well as evaluating completeness and accuracy of the related disclosures; • For loss allowances calculated on a collective basis: — Obtaining the relevant forward-looking information and macroeconomic projections used in the Bank's ECL assessment. Independently assessing the information by means of corroborating inquiries of the Management Board and inspecting publicly available information; — Challenging the collective PD, EAD and LGD parameters used by the Bank, by performing back-testing of historical defaults and by reference to historical realized losses on those defaults, and also considering any required adjustments to reflect expected changes in circumstances; • For impairment allowances calculated individually, for a risk-based sample of loans: — critically assessing the existence of any triggers for classification to Stage 2 or Stage 3 as at 31 December 2020, with focus on debtors from the economic sectors most affected by the effects of the COVID-19 pandemic, by reference to the underlying documentation (loan files) and through inquiries of the loan officers and credit risk management personnel; — for individually significant exposures classified in Stage 3, challenging key assumptions applied in the Management Board's estimates of future cash flows used in the impairment calculation, such as discount rates, collateral values and realization period by reference to loan files and market rates;

Key Audit Matters (continued)

Key audit matter	How our audit addressed the matter *(continued)*
In the wake of the above factors, coupled with the significantly higher estimation uncertainty stemming from the impact of the COVID-19 global pandemic on multiple sectors of the economy, we considered impairment of loans and receivables to be associated with a significant risk of material misstatement in the financial statements. Accordingly, we considered this area to be our key audit matter.	• For loan exposures in totality: — Assessing the adequacy of expected credit losses against the various minimum provisioning requirements prescribed by the FBA; — Assessing the overall reasonableness of the impairment allowances, including the loans provision coverage development, and benchmarking them against publicly available data. — Examining whether the Bank's loan impairment and credit risk-related disclosures in the financial statements appropriately include and describe the relevant quantitative and qualitative information required by the applicable financial reporting framework.

Key Audit Matters (continued)

Going concern considerations related to COVID-19

Refer to note 2.5 Going concern and note 36 which specifically addressed the uncertainties related to the COVID 19 outbreak.

Key audit matter	How our audit addressed the matter *(continued)*
The Bank's financial statements are prepared on a going concern basis. As discussed in Note 2.5, for the year ended 31 December 2020, the Bank reported a net profit of BAM 507 thousand. In addition, as at 31 December 2020, it had accumulated losses of BAM 27,864 thousand, which represented a significant increase over the prior annual reporting date, due to effects of the adoption of the expected credit loss requirements in respect of the Bank's loan portfolio, as discussed in Note 2.6. During 2020, in the wake of the said losses, the Bank received several capital injections from the shareholder in order to maintain its capital adequacy ratio at least at the minimum level required by the FBA. As disclosed in Note 6.4, the Bank's total capital adequacy ratio as at 31 December 2020 amounted to 14.5%. Although the ratio is above the FBA's minimum prescribed level, potential future losses without adequate capital support may erode the capital base. In addition, as disclosed in Note 36, the outbreak of the COVID-19 and the measures taken by the Government of BiH to mitigate the pandemic's spread, have sharply curtailed economic activity, resulting in declines in GDP and has raised further uncertainty with regards to the timing and extent of recovery. This in turn adversely affected the Bank's loan quality in certain industries, mostly affected by COVID-19 pandemic (e.g. tourism).	Our audit procedures in this area included, among others: • Inspecting the Management Board's assessment of the going concern basis of accounting, including their evaluation of the business/operating and liquidity risks, and plans for further actions in response to the risks identified. As part of the procedure we also made corroborating inquiries of the Management Board. As part of the procedure, we focused specifically on the Bank's analysis of COVID-19-related sources of risk, including potential negative effects of the outbreak on the loan portfolio; • Comparing the Bank's profit and loss and cash flows forecasts for the prior year to the current year's outcomes to assess the quality of the Management Board's forecasting process; • Independently evaluating the reasonableness and feasibility of the plans for future actions, by challenging the assumed forecasted business growth plans, based on the results of the preceding procedure, our understanding of the Bank's activities and by reference to our knowledge of the market. As part of this procedure, we also, among other things: — challenged the Bank's financial performance and cash flow forecasts in support of the management's use of the going concern basis of accounting, by assessing the planned measures to be implemented by the Bank; specifically challenging the key assumptions and judgements applied, including, among others, those in respect of interest and similar income, growth in loan portfolio and expected loan impairment losses; — assessed the availability of equity and other financing facilities, by inspecting approved capital commitments from the parent entity and assessing the parent's intent and ability to provide such financial support by reference to its financial information and through corroborating inquiries of the Bank's Management Board, as well as the parent's representatives. In addition, we inspected signed financing facilities and stand by arrangements available in 2021 from parent entity and other financial institutions.

Key Audit Matters (continued)

Key audit matter	How our audit addressed the matter *(continued)*
The Bank's going concern assessment was based on analysis of profit and loss forecasts, liquidity projections and capital adequacy. The preparation thereof incorporated a number of complex assumptions and required significant judgment. As part of the assessment, the Bank also considered a number of actions aimed at alleviating the potential disruption to its business and liquidity position, such as FBA and BiH Government measures. The Management Board concluded that the range of possible outcomes considered at arriving at this judgment does not give rise to material uncertainties related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. Note 36 to the financial statements further explains how the judgment was formed by the Management Board. The Bank's use of the going concern basis of accounting is a key audit matter due to the associated extent of uncertainty, and consequently, high level of judgment required in evaluating the Management Board's plans for future actions and their financial impact.	— in the context of the above forecasts, analyzed the Bank's expected development of the capital adequacy position in the foreseeable future. • Performing an analysis of the going concern conclusion's sensitivity to changes in the aforementioned key assumptions adopted in the going concern assessment, and considering whether there were any indicators of management bias in the assessment; • Considering whether any additional relevant facts or information have become available since the date on which the Bank made its assessment; • Evaluating the appropriateness of Bank's disclosures in respect of the going concern assessment, subsequent events and any related uncertainties in the financial statements.

Other Information

Management is responsible for the other information. The other information comprises the Key financial figures, Basic information about ProCredit Bank, Report on the economic position of the Bank, Report on expected developments, Disclosures required by law on accounting and auditing section C, that are all parts of the Annual Report, but does not include the financial statements and our auditors' report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation of the financial statements that give a true and fair view in accordance with the statutory accounting requirements applicable to banks in the Federation of Bosnia and Herzegovina, 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.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an 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 ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

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

Independent Auditors' report

To the shareholders of ProCredit Bank d.d. Sarajevo (continued)

Auditors' Responsibilities for the Audit of the Financial Statements (continued)

- 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 auditors' 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 auditors' 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 charged with 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 charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, actions taken to eliminate threats or safeguards applied.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Vedran Vukotić.

KPMG B-H d.o.o. za reviziju *31 May 2021*

Registered Auditors
Zmaja od Bosne 7-7a
71000 Sarajevo
Bosna i Hercegovina

D.O.O. ZA REVIZIJU KPMG B-H SARAJEVO

This version of the Auditors' report is a translation from the original, which was prepared in Bosnian 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 report takes precedence over translation.

Statement of profit or loss for the year ended 31 December 2020
(all amounts are expressed in thousands of BAM, unless otherwise stated)

	Notes	**2020**	**2019**
Interest income calculated using the effective interest method	*8*	17,476	15,213
Other interest income		162	87
Interest expense	*9*	(5,118)	(5,621)
Net interest income		**12,520**	**9,679**
Fee and commission income	*10*	5,903	6,047
Fee and commission expense	*11*	(1,721)	(1,717)
Net fee and commission income		**4,182**	**4,330**
Net income from foreign currency trading	*12*	1,094	853
Other operating income	*13*	802	697
Net operating income		**18,598**	**15,559**
Administrative expenses	*14*	(7,812)	(8,056)
Personnel expenses	*15*	(4,855)	(5,146)
Depreciation and amortisation	*23,24,25*	(1,550)	(1,562)
Other operating expenses	*16*	(2,072)	(1,588)
Operating expenses		**(16,289)**	**(16,352)**
Profit/(Loss) before impairment losses and income tax		**2,309**	**(793)**
Impairment losses, net	*17*	(1,751)	(692)
PROFIT /(LOSS) BEFORE TAX		**558**	**(1,485)**
Income tax expense	*18*	(51)	(74)
NET PROFIT/(LOSS) FOR THE PERIOD		**507**	**(1,559)**
Earnings/(Loss) per share (BAM)	*33*	0.07	(0.22)

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

Statement of other comprehensive income for the year ended 31 December 2020
(all amounts are expressed in thousands of BAM, unless otherwise stated)

	2020	2019
Net profit/loss for the period	**507**	**(1,559)**
Items that will not be reclassified to profit or loss		
Net gains and losses from changes in fair value of equity securities at fair value through other comprehensive income	***21***	**-**
Other comprehensive income for the year	***21***	**-**
TOTAL COMPREHENSIVE INCOME/LOSS FOR THE YEAR	**528**	**(1,559)**

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

Statement of financial position as at 31 December 2020
(all amounts are expressed in thousands of BAM, unless otherwise stated)

	Notes	31 December 2020	31 December 2019
ASSETS			
Cash in hand	*19*	6,744	6,712
Funds held at the Central Bank of BiH	*19*	104,143	108,676
Loans and receivables to banks	*19*	24,612	19,905
Loans and receivables to customers	*21*	449,400	398,254
Investment securities			
at fair value through other comprehensive income		64	43
at amortized cost	*20*	5,001	-
Current tax assets		259	236
Investment property	*22*	2,174	1,681
Property and equipment	*23*	11,686	12,967
Intangible assets	*24*	731	985
Deferred tax assets	*18*	29	80
Other assets and receivables	*25*	2,697	3,444
TOTAL ASSETS		**607,540**	**552,983**
LIABILITIES			
Liabilities to banks	*26*	40,957	39,180
Liabilities to other financial institutions	*27*	179,747	169,842
Liabilities to customers	*28*	330,544	282,167
Subordinated debt	*29*	8,804	8,804
Provisions for liabilities and charges	*30*	1,587	818
Other liabilities	*31*	2,097	3,067
TOTAL LIABILITIES		**563,736**	**503,878**
EQUITY AND RESERVES			
Share capital	*30*	71,126	71,126
Share premium		293	293
Statutory reserves		228	228
Accumulated losses		(27,864)	(22,542)
Fair value reserves		21	-
TOTAL EQUITY AND RESERVES		**43,804**	**49,105**
TOTAL LIABILITIES, EQUITY AND RESERVES		**607,540**	**552,983**

The accompanying notes form an integral part of these financial stateme

	Issued share capital	Share premium	Fair value reserves	Accumulated losses	Fair value reserve	Total
Balance as at 1 January 2019	**71,126**	**293**	**228**	**(20,983)**	**-**	**50,664**
Net loss for the period	**-**	**-**	**-**	**(1,559)**		**(1,559)**
Other comprehensive income						
Other comprehensive income	**-**	**-**	**-**	**-**	**-**	**-**
Total comprehensive income/(loss)	-	-	-	(1.559)	-	(1.559)
Balance as at 31 December 2019	**71,126**	**293**	**228**	**(22,542)**	**-**	**49,105**
Balance as at 1 January 2020	**71,126**	**293**	**228**	**(22,542)**	**-**	**49,105**
First time adoption FBA Decision (Note 5)	-	-	-	(5,829)	-	(5,829)
Balance as of January 1, 2020 (change in valuation)	**71,126**	**293**	**228**	**(28,371)**	**-**	**43,276**
Net profit for the year	-	-	-	507	-	507
Other comprehensive income						
Net gains and losses from change in fair value of equity securities at fair value through OSD					*21*	***21***
Total comprehensive income				**507**	**21**	528
Balance as at 31 December 2020	**71,126**	**293**	**228**	**(27,864)**	**21**	**43,804**

Statement of cash flows for the year ended 31 December 2020
(all amounts are expressed in thousands of BAM, unless otherwise stated)

	Notes	31 December 2020	31 December 2019
CASH FLOW FROM OPERATING ACTIVITIES			
Net profit/(loss) before taxr		558	(1,485)
Adjustments for:			
Depreciation and amortisation		1,550	1,562
Impairment losses, net		1,751	692
Net gain from sale of property and equipments		-	(5)
Net loss from writte off of property and equipment		10	1
Net change in provisions for liabilities and charges		614	259
Net (gain)/loss from sale of repossessed assets		(61)	(380)
Impairement allowance for repossessed assets		774	578
Net interest income		(12,520)	(9,679)
		(7,324)	**(8,457)**
Changes in operating assets and liabilities:			
Net change in obligatory reserves with CBBH		(6,250)	(6,846)
Net change in loans and receivables to customers, before impairment		(58,263)	(34,160)
Net change in other assests and receivables, before impairment		126	2,740
Net change in liabilities to banks		1,760	(1,878)
Net change in liabilities to customers		48,655	26,387
Payments of provisions for liabilities and charges		(152)	-
Net change in other liabilities		(631)	488
Paid income tax		(23)	(86)
Received interest		17,395	15,141
Paid interest		(5,593)	(5,006)
NET CASH FLOW USED IN OPERATING ACTIVITIES		**(10,300)**	**(11,677)**
CASH FLOW FROM INVESTING ACTIVITIES			
Purchase of securities at amortized cost		(5,006)	
Purchase of property and equipment		(437)	(161)
Proceeds from property and equipment sold		-	11
Purchase of intangible assets		(58)	
NET CASH FLOW USED IN FINANCING ACTIVITIES		**(5,501)**	**(150)**
FINANCING ACTIVITIES			
Proceeds from liabilities to banks and other financial institutions		29,338	42,996
Repayments of liabilities to banks and other financial institutions		(19,219)	(15,259)
Lease liabilities paid		(362)	(414)
Increase in share capital		-	-
NET CASH FLOW USED IN FINANCING ACTIVITIES		**9,757**	**27,323**
NET (DECREASE) / INCREASE IN CASH AND CASH EQUIVALENTS		**(6,044)**	**15,496**
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD	*19*	**88,246**	**72,750**
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD	*19*	**82,202**	**88,246**

The accompanying notes form an integral part of these financial statement.

1. REPORTING ENTITY

ProCredit Bank d.d. Sarajevo (the "Bank") is incorporated as a joint stock company domiciled in Bosnia and Herzegovina.

The Bank is part of a global network of financial institutions, managed and fully owned by ProCredit Holding AG & Co. KGaA.

The Bank is incorporated to perform all banking activities in accordance with the Law on banks in the Federation of Bosnia and Herzegovina and the main activities include commercial lending, receiving of deposits, foreign exchange deals, and payment operation services in the country and abroad and retail banking services. The Bank is a development-oriented commercial bank which offers customer services to small and medium enterprises and to private individuals.
The Bank's registered address is in Sarajevo, Franca Lehara bb, Bosnia and Herzegovina. As at 31 December 2020 the Bank had 148 employees (31 December 2019: 139 employees).

The Bank operated with branches, Contact Centre and 24/7 (self-service) Zones, in order to provide customers with comprehensive and more accessible services.

Branch offices	***Service Points***
Sarajevo, Franca Lehara bb	Sarajevo, Ilidža, Ibrahima Ljubovića 20
Mostar, Biskupa Čule bb	Bijeljina, Majevička 102
Banja Luka, Prvog krajiškog korpusa 54	Tuzla, Aleje Alije Izetbegovića 2

The Supervisory Board, Management Board and Audit Committee

During 2020 and on the date of this report, the members of the Supervisory Board were:

Supervisory Board

Gian Marco Felice	Chairman
Igor Anić	Deputy Chairman
Wolfgang Bertelsmeier	Member
Aida Soko	Member
Natia Tkhilaishvili	Member

During 2020 and on the date of this report, the members of the Audit Committee were:

Audit Committee

Emanuela Caushi	Chairman from 17 november 2020.
Emilija Spirovska	Member from 17 november 2020.
Heiko Buzin	Member from 17 november 2020.
Violeta Ivanković	Chairman till 17 november 2020
Vesna Paunovska Petroska	Member till 17 november 2020
Rumyana Velichkova Todorova	Member till 17 november 2020

During 2020 and on the date of this report, the members of Management Boand were:

Management Board

Amir Salkanović	Chairman
Amina Durmo - Trlin	Member
Vladimir Rajić	Member

2. BASIS OF PREPARATION

2.1. Statement of compliance

The financial statements have been prepared in accordance with the legal accounting regulations applicable to banks in the Federation of Bosnia and Herzegovina ("FBiH"), which are based on the FBiH Law on Accounting and Auditing, the FBiH Banking Law and bylaws of the Banking Agency of the Federation of Bosnia and Herzegovina ("Agency" or "FBA") adopted on the basis of the mentioned laws.

- The FBiH Law on Accounting and Auditing prescribes the preparation of financial statements in accordance with International Financial Reporting Standards ("IFRS").
- The Law on Banks of the FBiH prescribes the preparation of annual financial statements in accordance with the aforementioned Law on Accounting and Auditing of the FBiH, this law, and bylaws adopted on the basis of both laws.
- The Agency adopted the Decision on Credit Risk Management and Determination of Expected Credit Losses (the "Decision"), applicable from 1 January 2020 and which resulted in certain differences resulting from the calculation of impairment for credit losses due to the application of minimum rates prescribed by the Decision, which are not required by IFRS 9: "Financial Instruments" ("IFRS 9"). The Decision also has an impact on the valuation of non-financial assets arising from credit operations (acquired tangible assets whose valuation is within the scope of other relevant IFRS).

In accordance with the provisions of the Decision as at 31 December 2020 the Bank calculated an impairment for credit losses that is higher by BAM 5,671 thousand than the amount obtained by calculating the result of the Bank's internal model for calculating expected credit losses, compliant with the requirements of IFRS 9, with details as follows:

- Application of Article 23 of the Decision prescribing the application of minimum impairment rates for all exposures allocated to credit risk level 1 - calculated difference in the amount of BAM 1,132 thousand,
- Application of Article 24 of the Decision prescribing the application of minimum impairment rates for all credit exposures in credit risk level 2 - calculated difference in the amount of BAM 1,864 thousand,
- Application of minimum impairment rates prescribed in Article 25 of the Decision for exposures at credit risk level 3 (non-performing assets) - calculated difference in the amount of BAM 2,669 thousand, of which the amount of BAM 1,152 thousand relates to exposures not secured by acceptable collateral, and the amount of BAM 1,517 thousand to exposures secured by acceptable collateral,
- application of the minimum impairment rates prescribed in Article 26 of the Decision for trade receivables, receivables based on factoring and financial leasing and other receivables - the difference in the amount of BAM 6 thousand.

2. BASIS OF PREPARATION (continued)

2.1. Statement of compliance (continued)

The table below presents the effects of the previously described difference between the legal accounting regulations applicable to banks in the FBiH and the requirements for recognition and measurement under International Financial Reporting Standards:

	January 1, 2020	**December 31, 2020**
Assets	(5,615)	(5,380)
Liabilities	214	291
Equity	(5,829)	(5,671)

Note: positive amounts represent increases and negative ones represent decreases.

This is the first set of financial statements in which the Bank has applied the Decision on credit risk management and determination of expected credit losses. Changes in significant accounting policies are described in Note 2.6 *Changes in accounting policies* and Note 5 *Transition to the calculation of expected credit losses in accordance with the new regulatory requirements*.

These financial statements were authorizes by the Management Board as at 31 May 2021 for submission to the Supervisory Board.

2.2. Basis for measurement

These financial statements have been prepared on the historical or amortised cost basis, except for financial assets at fair value through profit or loss and financial assets at fair value.

2.3. Functional and presentation currency

These financial statements are presented are presented in Bosnian Marks ("BAM"), which is the Bank's functional and presentation currency, rounded to the nearest thousand . Bosnian Mark is pegged to Euro (1 EUR = 1.95583 BAM).

2.4. Use of estimates and judgements

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, revenues and expenses. Although these judgements and estimates are based on management's best knowledge of current events and conditions, actual results may differ from those estimates.

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

Information on areas with significant uncertainty in the estimates and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in these financial statements are disclosed in Note 4.

2. BASIS OF PREPARATION (continued)

2.5 Going concern

As presented in the financial statements, the Bank reported net profit for the year ended 31 December 2020 in the amount of BAM 507 thousand (31 December 2019: net loss BAM 1.559 thousand). Management has prepared the 5 -year business plan, adopted by the Supervisory Board, anticipating the reasonable growth of loan portfolio, interest income and deposit basis over the period 2021-2025, as well as increase in share capital in the amount of BAM 11.700 thousand through share capital cash in direct payment and BAM 8.804 thousand through conversion of subordinated debt into capital, both planned in 2021. Due to significant losses in the past, the Bank had several recapitalisations by the majority owner in prior years, in order to maintain capital adequacy prescribed by the Agency.

The Management expects to continue operating with the profit in the following periods, however this may change due to the potential further negative effects of COVID 19 on the Bank's clients. Nevertheless, we expect the Bank to continue to be compliant with the regulatory requirements, especially considering planned increase in share capital which will additionally improve and strengthen the Bank's capital position. The Bank analysed a number of future scenarios, including those adverse but plausible, for example significant deterioration in loan portfolio quality, slowdown in growth and decrease in funding from deposits. Based on those scenarios, no material uncertainties related to going concern were identified.

As disclosed in Note 6.4, the Bank's capital adequacy amounts to 14,5% as at 31 December 2020 which is within capital buffer as approved by the regulator (minimum capital adequacy of 12% and capital buffer of 2.5%). Increase in share capital, in the amount of BAM 3,900 thousand and conversion of subordinated debt into equity have already been initiated in December 2019, however, due to some administrative issues in the country (outside of the Bank's control) where State Security Commission does not operate for more than a year, the Bank is not in a position to receive and register increase in share capital. Federal Banking Agency is aware of this issue. In the period after year end, but before issuance of these financial statements, the Bank continues with stable profitable operations, in line with approved budget, and is in compliance with regulatory prescribed capital adequacy and liquidity limits.

Based on the above, these financial statements have been prepared under a going concern assumption, which means that the Bank will be able to realize its receivables and settle liabilities in the ordinary course of business. The Management concluded that the range of possible outcomes considered at arriving at this judgment does not give rise to material uncertainties related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern.

2.6. Changes in accounting policies

As previously stated in Note 2.1 *Statement of compliance* as of January 1, 2020, the Bank applied the *Decision on Credit Risk Management and Determination of Expected Credit Losses* issued by the Banking Agency of the Federation of Bosnia and Herzegovina, which resulted in changes in accounting policies and adjustments to amounts previously recognized in financial statements.

As prescribed by the Decision, the Bank did not revise the comparative data for 2019. The effects of the first application of the Decision are recognized against the opening balance of retained earnings and reserves on January 1, 2020. Other significant accounting policies applied in the preparation of the financial statements are the same as in the preparation of the annual financial statements as at 31 December 2019.

The implementation of the new Decision has resulted in changes in accounting policies related to the measurement of financial assets. A detailed description of the changes is disclosed in Note 3 *Significant accounting policies* and Note 5 *Transition to the calculation of expected credit losses in accordance with the new regulatory requirements of these financial statements*.

3. SIGNIFICANT ACCOUNTING POLICIES

Except for the previously described changes in Note 2.6 *Changes in accounting policies*, the Bank has consistently applied the accounting policies further described below to all periods disclosed in these financial statements.

3.1 Foreign currency transactions

Transactions in currencies other than Bosnian Marks ("BAM") are initially recorded at the exchange rates prevailing on the dates of transactions. Monetary assets and liabilities are translated at rates prevailing on the reporting date. Non-monetary items carried at fair value denominated in foreign currencies are translated at prevailing rates on the date when fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated. Profits and losses arising on translation are included in the income statement for the period.

The Bank values its assets and liabilities at the middle rate of the Central Bank of Bosnia and Herzegovina valid at the reporting date. The principal rates of exchange set forth by the Central Bank and used in the preparation of the Bank's statement of financial position at the reporting dates were as follows:

	31 December 2019	**31 December 2020**
USD	1.74799	1.59257
EUR	1.95583	1.95583

3.2. Interest income and expense

Effective interest rate

Interest income and expense are recognised in profit or loss using the effective interest rate method. The "effective interest rate" is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to:

- gross carrying amount of the financial asset; or
- the amortized costs of the financial liability.

When calculating the effective interest rate for financial instruments other than purchased or originated credit-impaired assets, the Bank estimates future cash flows considering all contractual terms of the financial instruments, but not expected credit loss ("ECL"). For purchased or originated credit impaired financial assets, a credit-adjusted effective interest rate is calculated using estimated future cash flows including ECL.

The calculation of the effective interest rate includes all paid or received transaction costs, fees and points, which are an integral part of the effective interest rate. Transaction costs include all incremental costs incurred directly in connection with the issuance or acquisition of financial assets or financial liabilities.

Amortised cost and gross carrying value

The amortised cost of a financial asset or a financial liability is the amount at which the financial assets or financial liability is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any loss allowance (or impairment).

"Gross carrying amount of financial assets" is the amortised cost of a financial asset before adjusting for any expected credit loss allowance.

3. SIGNIFICANT ACCOUNTING POLICIES

3.2. Interest income and expense *(continued)*

Calculation of interest income and expense

Effective interest rate on a financial asset or financial liability is calculated on initial recognition of a financial asset or liability. In calculating interest income and expense, the effective interest rate is applied to the gross carrying amount of the asset (when the asset is not credit-impaired) or to the amortised cost of the liability. The effective interest rate is revised as a result of periodic re-estimation of cash flows of floating rate instruments to reflect the movements in market rates of interest.

However, for financial assets that have been credit-impaired subsequently to initial recognition, interest income is calculated by applying the effective interest rate to the amortised cost of financial assets. If the asset is no longer credit-impaired, the calculation of interest income returns to the gross basis.

For financial assets that were credit-impaired on initial recognition, interest income is calculated by applying the credit-adjusted effective interest rate on the amortised cost of the asset. The calculation of interest income does not revert to a gross basis, even if the credit risk of the asset improves.

3.3. Fee and commission income and expenses

Fee and commission income and expenses that are integral part of the effective interest rate on a financial asset or liability are included in the effective interest rate, and are recognised in interest income and expense.

Fee and commission income and expenses, reported as such, comprise mainly fees related to credit card transactions, the issuance of guarantees and letters of credit, domestic and foreign payment transactions and other services and are recognised in the profit and loss statement upon performance of the relevant service.

Fee and commission income from contracts with customers is measured based on the consideration specified in a contract with a customer. The Bank recognizes revenue when it transfers controls over a service to a customer.

The table below shows the nature and timing of the satisfaction of performance obligation, including significant payment terms and related revenue recognition policies.

Type of service	**Nature and timing of satisfaction of performance obligations, including significant payment terms**	**Revenue recognition under IFRS 15**
Private and business clients banking service	The Bank provides banking services to private and business customers, including account management, provision of overdraft facilities, foreign currency transactions, credit card and servicing fees. Fees for ongoing account management are charged to the customer's account on a monthly basis. The Bank sets the rates separately for private and business banking customers on an annual basis. Transaction-based fees for interchange, foreign currency transactions and overdrafts are charged to the customer's account when the transaction takes place. Servicing fees are charged on a monthly basis and are based on fixed rates reviewed annually by the Bank.	Revenue from account service and servicing fees is recognised over time as the services are provided. Revenue related to transactions is recognised at the point in time when the transaction takes place.

A contract with a customer that results in a recognised financial instrument in the Bank's financial statements may be partially in the scope of IFRS 9 and partially in the scope of IFRS 15. If this is the case, then the Bank first applies IFRS 9 to separate and measure the part of the contract that is in the scope of IFRS 9 and then applies IFRS 15 to the residual.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

3.4. Net income from foreign currency trading

Gains less losses from foreign exchange trading include unrealized and realized gains and losses from foreign exchange spot transactions.

3.5. Leases

At inception of a contract, the Bank assesses whether a contact is, or contains, a lease. A contract is, or contains a lease, if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. To assess whether a contract conveys the right to control the use of an identified asset, the Bank uses the definiton of a lease in accordance with IFRS 16 „*Leases*".

This policy is applied to the contracts entered into (or modified) on or after 1 January 2019.

i) As a lessee

The Bank recognizes right-of-use asset and a lease liabiliy from the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date plus any initial direct costs incurred and an estimate of costs to dismantle and remove any improvements made to business premises. The lessee incurs a liability for these costs at commencement date of the lease or as a result of the use of the relevant property over a specified period.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term, or over the period for which the lease is expected to be active. In addition, right-of-use asset is periodicaly reduced by impairment losses, if any and adjusted for any remeasruement of lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Bank's incremental borrowing rate. Generally, the Bank uses its incremental borrowing rate of 3.95% and 1.13% for renting other equipment and 3.65% for business premises as the discount rate. The Bank determines the incremental borrowing rate as an interest rate paid to borrow funds of similar value as the right of use, in a similar economic environment, under similar terms and conditions.

Lease payments included in the measurement of the lease liability comprise the following:

- fixed payments, including in-substance fixed payments;
- variable payments that depend on a particular index or rate and that are initially measured against that index or rate on the first day of the lease;
- amounts expected to be payable under a residual value guarantee; and
- the exercise price under a purchase option that the Bank is reasonably certain to exercise, lease payments in an optional renewal period if the Bank is reasonably certain to exercise an extension option, and penalties for early termination of a lease unless the Bank is reasonably certain not to terminate early

The lease liability is measured at amortised cost using the effective interest rate method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Bank's estimate of the amount expected to be payable under a residual value guarantee, if the Bank changes its assessment of whether it will exercise purchase, extension or termination option or if there is a revised in-substance fixed lease payment.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

3.5. Leases *(continued)*

When the lease liability is remeasured in this way, the carrying amount of the asset is properly adjusted for use or the difference is recorded in the income statement if the carrying amount of the asset is reduced to zero.

The Bank presents right-of-use assets in '*Property and equipment*' and lease liabilities in '*Other liabilities*' in the statement of financial position.

Short-term leases and leases of law value

The Bank has elected not to recognise right-of-use assets and lease liabilities to leases of low-value assets and short-term leases. The Bank recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

ii) As a lessor

The Bank recognises lease payments received under operating leases as income on a straightline basis over the lease term.

3.6. Income tax

Tax expense, on income tax base, is the sum of current tax and deferred taxes.

Current income tax

Net income differs from taxable income of the period reported in income statement and statement of comprehensive income, as it includes items of income and expense that are taxable or non-taxable in other years, as well as items that are never taxable or are deductible. The Bank's current tax liabilities are calculated by applying tax rates that are in effect or in the process of being adopted at the reporting date.

Deferred income tax

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

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the asset to be recovered.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

3.7. Financial assets and liabilities

Recognition and initial measurement

The Bank initially recognises loans and advances, deposits, debt securities and subordinated liabilities on the date on which they are originated. All other financial instruments (including regular-way purchases and sales of financial assets) are recognised on the trade date, which is the date on which the Bank becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value plus any transaction costs that are directly attributable to its acquisition or issue, except for financial assets and liabilities at fair value through profit and loss.

3.7.1 Financial assets

(i) Classification and subsequent measurement

The Bank classifies its financial assets based on their underlying business model (ie. the purpose of managing financial assets) and the contractual cash flows characteristic ("Solely Payments of Principle and Interest", further "SPPI test" or "SPPI") in the following measurement categories:

- Financial assets measured at amortised cost
- Financial assets measured at fair value through other comprehensive income (FVOCI)
- Financial assets at fair value through profit and loss (FVPL)

The classification requirements for debt and equity instruments are described below.

Business model assessment

Differentiation is made between the following business models:

- "hold to collect": The financial assets are held with the aim of collecting the contractual cash flows .
- "hold to collect and sell": The financial assets are held with the aim of both collecting the contractual cash flows and selling the financial assets, and
- "other": This business model is used for financial assets that are neither allocated to the 'hold to collect' business model nor to the 'hold to collect and sell' business model.

The Bank makes an assessment of the objective of a business model in which the asset is held at the portfolio level (ie. on the basis of a group of financial assets) because this best reflects the way the business is managed and information is provided to the management. The following criteria, among others are taken into account:

- The business and risk strategy of the Bank.
- The way in which the development of the business model is evaluated and reported to the Management and Supervisory Board of the Bank, and
- If there were sales in previous period, the frequency, volume, timing and reasons for those sales as well as expectations regarding future sales activities.

As a result, the balance sheet items allocated to the 'hold to collect' business model are: "Central bank balance", "Current accounts with other banks", "Loans and advances to customers" and "Other assets". "Investment securities" are allocated to the "hold to collect" or to the "hold to collect and sell" business model.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

3.7. Financial assets and liabilities *(continued)*

3.7.1 Financial assets *(continued)*

(i) Classification and subsequent measurement (continued)

Assessment of whether contractual cash flows are solely payments of principal and interest (SPPI)

Test of features of contractual cash flows from the point of view of solely payment of principal and interest is one of the criteria for the classification of financial assets in an individual category of measurement. SPPI test is implemented for the purpose of establishing whether the interest rate on unsettled principle reflects the fee for time value of money, credit risk and other basic risks of borrowing, lending costs and profit margin.

SPPI test is performed:

- for each financial asset, allocated to a business model whose purpose is to hold financial assets for the payment of contractual cash flows and a business model for the purpose of collecting contractual cash flows and selling financial asset on the date of its initial recognition,
- for each financial asset in cases where the original asset has been significantly modified and therefore re-recognised as new assets,
- when introducing new models and/or loan programs to determine in advance the eligibility of the considered loan term and conditions in relation to the need to subsequently monitor the value of any financial assets that would arise from them.

Equity instruments have contractual cash flows that do not meet the SPPI criterion. The Bank designates its equity instuments at fair value through other comprehensive income.

- **Financial assets at amortised cost**

Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest ("SPPI"), and that are not designated at fair value through profit and loss, are measured at amortized cost.

After initial recognition, the carrying amount of these assets is adjusted by any expected credit loss (ECL) allowance recognised and measured as described in Note 6.1.1.

Interest income is calculated using the effective interest rate and it is included in the line „Interest income calculated using the effective interest rate method".

Financial assets at amortised cost at the balance sheet date include: cash and cash equivalents, obligatory reserves at the Central Bank of BiH, loans and receivables to customers, investments in debt securities and other assets.

- **Financial assets through other comprehensive income**

Financial assets that are held for collection of contractual cash flows and for selling the assets, where the assets' cash flows represent solely payments of principal and interest, and that are not designated at fair value through profit and loss, are measured at fair value through other comprehensive income.

Measurements in fair value of a financial asset measured through other comprehensive income are recognised through other comprehensive income except for recognition of gains or losses on impairment, interest income and foreign exchange differences that are recognised in profit or loss, except in case of equity investments where unrealised gains/losses are never reclassified to profit or loss.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

3.7. Financial assets and liabilities *(continued)*

3.7.1. Financial assets *(continued)*

When the financial asset through other comprehensive income is derecognised, the cumulative gain or loss previously recognised through other comprehensive income is reclassified from equity to income statement, except for equity investments for which gains and losses are not recycled to profit or loss statement but directly transferred to retained earnings Interest income is calculated using the effective interest rate method.

At the balance sheet date, the Bank did not hold any debt instrumetns classified as financial assets at fair value through other comprehensive income. Investment securities include equity investments that are classified as financial assets through other comprehensive income at the balance sheet date.

- **Financial assets at fair value through profit and loss**

Financial assets are subsequently measured at fair value through profit or loss unless subsequently measured at amortised cost or at fair value through other comprehensive income. Gains and losses arising from changes in the fair value of a financial asset at fair value through profit or loss are recognised in the income statement.

In addition, the Bank has the option to designate, on initial recognition, financial assets that otherwise meet the requirements to be measured at amortised cost or at FVOCI at fair value through profit and loss, if doing so significantly reduces the accounting mismatch that would otherwise arise.

At the balance sheet date, the Bank did not hold any financial assets at fair value through profit and loss.

(ii) Derecognition of financial assets

The Bank derecognizes financial assets (in whole or in part) when the contractual rights to receive the cash flows from the financial instrument expire or when it loses control over contractual rights over that financial asset. This occurs when the Bank transfers substantially all the risks and rewards of ownership to another business entity or when rights have been realized, transferred or expired.

When the financial assets is derecognised, the difference between the carrying amount (or the carrying amount allocated to the portion of the assets that is derecognised) and the amount received (including any new assets less any new liabilities) and any cumulative gain or loss previously recognized through comprehensive income is recognised in the income statement.

Any cumulative gain or loss recognised through other comprehensive income in respect of equity investment securities designated as at fair value through other comprehensive income is not recognised in profit or loss on derecognition of such securities, but are directly recognised in retained earnings.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

3.7. Financial assets and liabilities *(continued)*

3.7.1. Financial assets *(continued)*

(iii) Modification of financial assets

Modification of financial assets is a process where the terms of the original contract are modified as a result of:

1) caused by current borrowers' needs (for example a reduction in the effective interest rate, prolongation of contract period, collateral substitution) and not caused by financial difficulties of the borrower,

2) caused by the current financial difficulties of the borrower or the difficulties that will arise soon, or by deteriorating the borrowers creditworthiness.

Modification of financial assets occurs when changes to some or all of the contract's provisions have been made.

In the case of a financial asset that represents a debt instrument (securities and loans and receivables), the Bank determines whether the modification is significant or whether the difference between the present value of the remaining modified cash flows discounted using the original effective interest rate and the current value of the modified cash flows discounted using the original effective interest rate is more than 10%.

If the modification is significant, the Bank ceases to recognize the original financial asset and begins to recognize new financial assets at fair value plus transaction costs and recalculates the new effective interest rate for the asset. The modification date is consequently considered to be the date of initial recognition for the purpose of calculating the impairment, including the purpose of determining whether a significant increase in credit risk has occurred.

However, the Bank also assesses whether the new financial asset recognised is deemed to be credit-impaired at initial recognition, especially in circumstances where the modification was driven by the debtor being unable to meet the originally agreed payments. The differences in the carrying amount are also recognized in profit or loss as a gain or loss on derecognition.

If the modification of the financial asset is not significant and the modification did not result in derecognition of the financial asset, then the Bank recalculates the gross carrying amount of the asset based on the revised cash flows of the financial asset and recognizes the modification gain or loss in profit or loss. The new gross carrying amount is recalculated by discounting modified cash flows at the original effective interest rate (or using an effective interest rate adjusted for credit risk in the case of POCI assets). If the modification is not significant, any resulting modification gain or loss is recorded together with the impairment losses.

(iv) Impairment

IFRS 9 outlines a "three-stage" model for impairment of financial assets based on changes in credit quality since initial recognition of financial assets.

Impairment of financial assets is recognized on the basis of, starting from 01 January 2020 based on, the expected credit loss model (ECL) for assets subsequently measured at amortized cost and assets subsequently measured at fair value through other comprehensive income (other than equity instruments). As disclosed in Note 2.6 and further below, as of January 1, 2020, the Bank applies a new Decision on Credit Risk Management and Determination of Expected Credit Losses according to which the Bank recognizes expected credit losses either at the minimum rates, as required by the Decision, or amounts calculated according to the internal ECLmodel of the Banks depending on what is higher.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

3.7. Financial assets and liabilities *(continued)*

3.7.1. Financial liabilities (continued)

(iv) Impairment (continued)

Calculation and measurement of ECLs, based on the Bank's internal model, is an area of significant judgement, and implies methodology, models and data inputs. The following components of ECL calculation have the major impact on credit loss allowance for ECLs: default definition, significant increase in credit risk, PD, LGD and EAD. The Bank regularly reviews and validates models and inputs to the models to reduce any differences between expected credit loss estimates and actual credit loss experience.

See Note 6.1.1. which explains more details regarding internal impairment model.

Policy applicable from 1 January 2020 – Decision on credit risk management and determination of expected credit losses.

As disclosed in Notes 2.1, 2.6 and 5, as of January 1, 2020, the Bank measures expected credit losses in accordance with the requirements of the Decision on Credit Risk Management and Determination of Expected Credit Losses. The requirements of the new Decision regarding impairment are based on the model of expected credit losses of IFRS 9, with certain specifics (for example, the prescribed minimum rates of expected credit losses for credit risk levels). Following the new requirements of the regulator, the Bank updated the impairment methodology in accordance with the requirements of the new Decision, and defined minimum criteria for measuring expected losses in accordance with the distribution of exposure to credit risk levels, as described below.

1 Credit risk level 1:

The Bank shall determine and recognize expected credit losses for exposures allocated to the credit risk level 1 at least in the following amounts:

a) for low risk exposures - 0.1% of exposure,
b) for exposures to central governments and central banks outside Bosnia and Herzegovina for which there is a credit assessment by a recognized external credit rating institution which is assigned to credit quality level 3 and 4 in accordance with Article 69 of the Decision on calculation of bank's capital - 0.1 % of exposure,
c) for exposures to banks and other entities of the financial sector for which there is a credit assessment by a recognized external credit rating institution which is assigned to credit quality level 1, 2 or 3 in accordance with Article 69 of the Decision on calculation of bank's capital - 0.1 % of exposure,
d) for other exposures - 0.5% of exposures.

If the Bank, in accordance with its internal methodology, determines the amount of expected credit losses higher than those arising from the above provisions of the Decision, the Bank shall apply the higher amount.

2 Credit risk level 2:

For exposures allocated to credit risk level 2, the Bank determines and recognizes the expected credit losses in the amount higher of the following:

a) 5% of exposure,
b) the amount determined in accordance with the Bank's internal methodology.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

3.7. Financial assets and liabilities *(continued)*

3.7.1. Financial liabilities (continued)

(iv) Impairment (continued)

Policy applicable from 1 January 2020 – Decision on credit risk management and determination of expected credit losses (continued)

3 Credit risk level 3:

The minimum rates of expected credit losses allocated to Level 3 depend on whether the exposure is secured by eligible collateral or not, and accordingly, the minimum rates are as follows:

a) exposures secured by eligible collateral:

Days past due	Minimum expected credit loss
Up to 180 days	15%
from 181 to 270 days	25%
from 271 to 365 days	40%
from 366 to 730 days	60%
from 731 to 1460 days	80%
over 1460 days	100%

a) exposures secured by eligible collateral:

Days past due	Minimum expected credit loss
Up to 180 days	15%
from 181 to 270 days	45%
from 271 to 365 days	75%
from 366 to 456 days	85%
over 456 days	100%

Exceptionally, if the Bank has taken appropriate legal action and can document the certainty of collection from eligible collateral in the next three years, the increase in the level of expected credit losses is not required to exceed 80% of the exposure. In doing so, the estimate of future cash flows from eligible collateral reduced to present value must be greater than 20% of that receivable. In the event that the Bank does not collect receivables in the specified period of three years, it is obliged to record the expected credit losses in the amount of 100% of the exposure.

In the case of restructured exposures, the Bank will maintain the expected credit losses at the level of coverage formed on the date of approval of the restructuring, which cannot be lower than 15% of the exposure, for all 12 months of the recovery period. For the third and each subsequent restructuring of a previously restructured exposure that was allocated to credit risk level 3 or POCI assets at the time of restructuring, the Bank determines and recognizes the expected credit losses in the amount of 100% of the exposure.

For exposures related to cases when the debtor has not fulfilled its obligation to the bank no later than 60 days from the day when the protest was performed on the basis of a previously issued guarantee, the Bank determines and recognizes the expected credit loss in the amount of 100% of the exposure.

If the Bank, in accordance with its internal methodology, determines the amount of expected credit losses higher than the amounts arising from the provisions of the Decision, the Bank determines and recognizes these amounts in the books.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

3.7. Financial assets and liabilities *(continued)*

3.7.1. Financial assets (continued)

(iv) Impairment (continued)

Policy applicable from 1 January 2020 – Decision on credit risk management and determination of expected credit losses (continued)

The minimum rates of expected credit losses for trade receivables, factoring and financial leasing receivables and other receivables are applied according to the table bellow:

Days past due	Minimum expected credit loss
there is no material past due amount	0,5%
up to 30 days	2%
from 31 to 60 days	5%
from 61 to 90 days	10%
from 91 to 120 days	15%
from 121 to 180 days	50%
from 181 to 365 days	75%
over 365 days	100%

3.7.2. Financial liabilities

(i) Classification

The Bank classifies financial liabilities at fair value through profit or loss and financial liabilities at amortised cost. The classification depends on the intention for which the financial instruments have been acquired. The Management determines the classification of financial instruments at initial recognition and reviews that classification at each reporting date.

Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss have two sub-categories: financial instruments held for trading (including derivatives) and those designated by management as at fair value through profit or loss at inception. A financial instrument is classified in this category only if it is acquired or incurred principally for the purpose of selling or repurchasing it in the near term for the purpose of short-term profit taking or designated as such by management at initial recognition. The Bank has no financial liabilities classified at fair value through profit or loss.

Other financial liabilities

Other financial liabilities comprise all financial liabilities which are not at fair value through profit and loss and include liabilities to customers, liabilities to banks and other financial institutions and subordinated debt.

(ii) Initial and subsequent measurement

Financial liabilities at fair value through profit or loss are initially recognised at fair value, while transaction costs are immediately expensed. Subsequent measurement is also at fair value.

Gains and losses arising from a change in the fair value of financial liabilities at fair value through profit or loss are recognised in the income statement.

Other financial liabilities are initially measured at fair value including transaction costs. Subsequent to initial recognition the Bank measures other financial liabilities at amortised cost using the effective interest rate.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

3.7. Financial assets and liabilities *(continued)*

3.7.2. Financial liabilities (continued)

(iii) Derecognition of financial liabilities

The Bank derecognises financial liabilities when, and only when, the Bank's obligations are discharged, cancelled or they expire.

(iv) Modification of financial liabilities

The Bank derecognises a financial liability when its terms are modified and the cash flows of the modified liability are substantially different. In this case, a new financial liability based on the modified terms is recognised at fair value. The difference between the carrying amount of the financial liability derecognised and consideration paid is recognised in profit or loss. Consideration paid includes non-financial assets transferred, if any, and the assumption of liabilities, including the new modified financial liability.

If the modification of a financial liability is not accounted for as derecognition, then the amortised cost of the liability is recalculated by discounting the modified cash flows at the original effective interest rate and the resulting gain or loss is recognised in profit or loss. For floating-rate financial liabilities, the original effective interest rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of the modification. Any costs and fees incurred are recognised as an adjustment to the carrying amount of the liability and amortised over the remaining term of the modified financial liability by re-computing the effective interest rate on the instrument.

3.7.3 Offsetting of financial assets and liabilities

Financial assets and financial liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Bank currently has a legally enforceable right to set off the amounts and it intends either to settle them on a net basis or to realise the asset and settle the liability simultaneously.

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

3.7.4. Specific financial instruments

Cash and cash equivalents

Cash and cash equivalents include cash in hand, unrestricted balances held with the Central Bank, current accounts with other banks and higly liquid financial assets with original maturities of three months or less from the date of acquisition.

Cash and cash equivalents are carried at amortised cost in the statement of financial position.

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

Loans and receivables

Loans to customers are presented at amortised cost net of impairment allowances to reflect the estimated revocable amounts.

"Loans and receivables" captions in the statement of financial position include:

- loans and receivables measured at amortised cost (see Note 3.7.1), thet are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method;

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

3.7. Financial assets and liabilities *(continued)*

3.7.4. Specific financial instruments (continued)

Investment securities

The investment securities caption in the statement of financial position includes equity investment securities designated as at fair value through other comprehensive income and debt securities measured at amortised costs. .

Financial guarantees and loan commitments

'Financial guarantees' are contracts that require the Bank to make specified payments to reimburse the holder for a loss that it incurs because a specified debtor fails to make payment when it is due in accordance with the terms of a debt instrument. 'Loan commitments' are firm commitments to provide credit under pre-specified terms and conditions.

Borrowings and subordinated debt

Interest-bearing borrowings and subordinated debt are classified as other financial liabilities and are recognised initially at fair value, less attributable transaction costs. Subsequent to initial recognition, these are stated at amortized cost with any difference between proceeds (net of transaction costs) and redemption value being recognised in the profit or loss statement over the period of the borrowings using the effective interest rate method.

Current accounts and deposits from banks and customers

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

3.8 Property and equipment

Property and equipment are stated at historical cost less accumulated depreciation and impairment losses. The cost includes expenditures that are directly attributable to the acquisition of the asset. Subsequent cost is included in net book value or is accounted for as separate assets only if it is probable that the future economic benefits embodied within the part will flow to the Bank and its cost can be measured reliably. The costs of day-to-day repairs and maintenance are recognised in the income statement as incurred. Land is not depreciated.

Depreciation is charged from the moment the fixed asset is ready for its intended use. It is calculated in the basis of the estimated useful life of the asset, using the straight-line method.

Useful lives of tangible assets are as follows:

	Useful life 2019	**Useful life 2018**
Buildings	40 years	40 years
Computers	3 – 7 years	3 – 7 years
Furniture and equipment	5 – 10 years	5 – 10 years
ATMs	5 – 8 years	5 – 8 years
Motor vehicles	3 – 5 years	3 – 5 years
Other assets	2 – 7 years	2 – 7 years

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in the statement of profit or loss in the period they occur.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

3.9. Intangible assets

Intangible assets are stated at cost less accumulated amortization and impairment losses. The cost includes all expenditure that is directly attributable to the acquisition of the items.

Useful life of intangible assets is as follows:

	Useful life 2019	**Useful life 2018**
Intangible assets	5 years	5 years

3.10. Investment property

Investment property, which is property held to earn rental income and/or for capital appreciation, is measured initially at its cost, including transaction costs. Subsequent to initial recognition, investment property is stated at cost, less accumulated depreciation and any recognized accumulated impairment losses. Depreciation commences when the assets are ready for their intended use and is calculated in the basis of the estimated useful life of the asset, using the straight-line method as follows:

	Useful life 2020	**Useful life 2019**
Buildings	40 years	40 years

The Bank did not have investment property in 2018. Rental income from investment property are classified within 'Other operating income' in the Statement of profit and loss.

3.11 Assets repossessed from disbursement of loans

The Bank may recover assets that were originally received as collateral for the loan after exercising contractual rights or undertaking specific legal actions. When both of the following conditions are satisfied, the relevant assets shall be included in the Bank's balance sheet:

- The recovery activity has been completed
- The Bank has become owner of the asset

The Bank classifies repossessed assets under IFRS 5 and subsequenty measures tham at lower of between book value and fair value less costs to sell.

According to the requirements of the new Decision (Note 2.6. Change in accounting policy) from January 1, 2020, if the Bank does not sell assets repossessed from disbursement of loans, it is obliged to reduce the value of the same to 1 KM within three years from the date of initial recognition, while for assets recognised before January 1, 2019, its value must be reduced to 1 KM within two years from the date of initial application of the new Decision.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

3.12 Impairment of non-financial assets

At each reporting period date, the Bank reviews the carrying amounts of its property and equipment to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any).

Recoverable amount is the greater of net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. Impairment losses are recognised as an expense in profit or loss.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

3.13 Provisions for liabilities and charges

Provisions are recognised when the Bank has a present legal or constructive obligation as a result of past events for which it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of the obligation can be made.

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

Provisions are released only for such expenditure in respect of which provisions are recognised at inception. If the outflow of economic benefits to settle the obligations is no longer probable, the provision is reversed.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

3.14. Employee benefits

i. Liabilities for a contribution plan

The Bank, in the normal course of business, makes payments on behalf of its employees for pensions, health care, employment and personnel tax that are calculated on the basis of gross salaries and wages, food allowances, holyday allowances and travel expenses according to the legislation. The Bank makes these contributions to the Government's health and retirement funds, at the statutory rates in force during the year, based on gross salary payments.

The Bank pays contributions to public pension insurance funds on a mandatory basis. Once the contributions have been paid, the Bank has no further payment obligations. The regular contributions constitute costs for the year in which they are due and as such are included in staff costs. The cost of these payments is charged to profit or loss in the same period as the related salary cost.

ii. Short-term employee benefits

Short-term employee benefit obligations are measured on undiscounted basis and are expensed as the related service is provided.

A provision is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Bank has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

iii. Long-term employee benefits

According to local legal requirements, employees of the Bank are entitled to receive one-time benefit on retirement, dependent on factors such as age, years of service and the salary they had with the Bank.

Such payments are treated as post-employment benefits and the liability recognised in the statement of financial position is the present value of the defined benefit obligation at the reporting date less the fair value of plan assets (if any), together with adjustments for unrecognised actuarial gains or losses and past service costs.

This obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by applying a discount rate which is similar to the rate of return on corporate bonds in the Federation of Bosnia and Herzegovina and the average interest rate of time deposit accounts held with commercial banks in the Federation of Bosnia and Herzegovina.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are recognised immediately in profit and loss as well as all past service costs.

3.15. Equity and reserves

i. Share capital

Shere capital represents the nominal value of paid-in ordinary shares classified as equity and is denominated in BAM. Dividens are recognized as liability in the period in which they are declared.

ii. Share premium

Share premium represents the excess of contribution received over the nominal value of shares issued.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

3.15. Equity and reserves *(continued)*

Statutory reserves

Statutory reserve is created in accordance with the Company Law of the Federation of Bosnia and Herzegovina, which requires 10% of the profit for the year to be appropriated to this reserve until reaching 25% of issued share capital. If the statutory reserve does not reach 25% of issued share capital within five business years, a joint stock company is required to increase its appropriations to this reserve to 20% of its profit for the year at the end of the fifth and any following business years until reaching 25% of the issued share capital. This reserve can be used for covering current and prior year losses.

Retained earnings/accumulated loss

Profit or loss for the period after appropriations to owners is transferred to retained earnings/accumulated losses.

3.16. Earnings per share

The Bank publishes basic and diluted earnings per share (EPS) data.

Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the period. The Bank does not have preference shares.

3.17 New standards and interpretations

Several new standards and accompanying additions are in place for the accounting period starting on 1 January 2020. The Bank believes that the new standards and amendments to the standards will not have a significant impact on the financial statements in the period of first application.

4. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

The Bank makes estimates and assumptions about uncertain events, including estimates and assumptions about the future. Such accounting assumptions and estimates are regularly evaluated 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.

Impairment losses on loans and receivables

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

Information about judgements made in applying accounting policies that have the most significant effects on the amounts recognised in the financial statements is included in the following notes:

- Note 3.7.1: classification of financial assets: assessment of the business model within which the assets are held and assessment of whether the contractual terms of the financial asset are SPPI on the principal amount outstanding.
- Note 6.1.1: establishing the criteria for determining whether credit risk on the financial asset has increased significantly since initial recognition, determining methodology for incorporating forward-looking information into measurement of ECL and selection and approval of models used to measure ECL.

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment in the year ended 31 December 2020 and 31 December 2019 is included in the following notes.

- Note 6.1.1.: impairment of financial instruments: determining inputs into the ECL measurement model, including incorporation of forward-looking information.
- Note 6.1.1.: impairment of financial instruments: key assumptions used in estimating recoverable cash flows.

COVID-19

As disclosed in Note 6, outbreak of COVID-19 represent signifficant new event that has afected credit risk management and the determination of loan impairment. Significant judgments relating to impairment for expected credit losses are particularly complex in the current uncertain environment. The COVID 19 pandemic continues to develop and the economic environment in which the Bank operates is subject to volatility, which could have a further impact on financial results as the duration of the COVID 19 pandemic and the effectiveness of measures taken by governments and the banking regulator are uncertain.

Due to these economic changes, the Bank has adjusted its approach to measuring expected credit losses as explained in detail in Note 6.1. Additionaly, in this regard the Bank continues to monitor and implement regulatory requirement as prescribed by the Decision on temporary measures of banks to mitigate negative economic consequences caused by "COVID-19".

The Bank continues to monitor and evaluate the impact of the COVID 19 pandemic on key accounting judgments, estimates and assumptions.

Taxation

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

Regulatory requirements

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

4. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY (*continued)*

Litigation and claims

The total amount of legal proceedings is BAM 1,399 thousand (2019: BAM 1.152 thousand). The Bank performs an individual assessment of all court cases and creates provisions in accordance with the assessment. The assessment of risks and proposal for provisions for legal cases is performed by the Legal Affairs Department and Finance Division, and a decision on the creation of provisions is made by the Bank's management.

As stated in Note 30, the Bank provided BAM 683 thousand (2019: BAM 425 thousand), which management estimates as sufficient.

5. TRANSITION TO CALCULATION OF EXPECTED CREDIT LOSSES IN ACCORDANCE WITH NEW REGULATORY REQUIREMENTS

Estimated impact of the adoption of the Decision on credit risk management and calculation of expected credit losses - First adoption ("FTA")

On June 20, 2019, the Banking Agency of the Federation of Bosnia and Herzegovina issued a new Decision on Credit Risk Management and Determination of Expected Credit Losses (Official Gazette of the FBiH No. 44/19 of June 26, 2019), the application of which is binding on all banks. starting on January 1, 2020.

The requirements of the new Decision in the area of impairment are based on the model of expected credit losses of IFRS 9, with certain specifics prescribed, which mostly refer to the prescribed minimum rates of expected credit losses for credit risk levels (for details see Note 3.7.1. (iv)). In accordance with the above, the banks were obliged to calculate the effects of the first time adoption of this Decision as of December 31, 2019, ie the opening balance as of January 1. 2020, and recognize them in the equity accounts on that day without correction of the comparative information for 2019.

The effects of the first time adoption are the difference between the expected credit losses determined in accordance with the provisions of this Decision and those identified and accounted for by the Bank in accordance with its internal methodology in accordance with IFRS 9, when the expected credit losses determined this way are smaller. In line with the requirements of the Decision, the effects are calculated for each individual exposure.

The impact of the transition to the calculation of expected credit losses in accordance with the new Decision on January 1, 2020 on the Bank's financial statements was a decrease in net assets in the amount of BAM 5,829 thousand, arising from:

- Decrease in the amount of BAM 5,615 thousand from additional impairment of financial assets,
- Increase in provisions for financial guarantees and loan commitments in the amount of BAM 214 thousand.

The Bank has an adequate capital adequacy ratio following the adoption of the Decision. Capital adequacy ratios as at 31 December 2020 are presented in Note 6.4.

The impact of the adoption of the Decision on credit risk management and the calculation of expected credit losses is presented in the table below:

5. TRANSITION TO CALCULATION OF EXPECTED CREDIT LOSSES IN ACCORDANCE WITH NEW REGULATORY REQUIREMENTS

Estimated impact of the adoption of the Decision on credit risk management and calculation of expected credit losses - First adoption ("FTA") *(continued)*

The effects of the first application are shown in the table below:

	December 31, 2019 IFRS 9	Re-measurement	January 1, 2020. FBA decision
ASSETS			
Funds held at the Central Bank of BiH	108,676	(61)	**108,615**
Loans and receivables from banks	19,905	(41)	**19,864**
Loans and receivables to customers*	398,254	(5,499)	**392,755**
Other assets and receivables	3,444	(14)	**3,430**
LIABILITIES			
Provisions for off-balance sheet items	3,067	214	**3,281**
EQUITY AND RESERVES			
Retained losses	(22,542)	(5,829)	**(28,371)**

* In accordance with the requirements of the new Decision, the Bank writes off the balance sheet exposures two years after the Bank has recorded the expected credit losses in the amount of 100% of the gross book value of that exposure and declared it fully matured. In this regard, on the day of the first adoption, ie on January 1, 2020, the Bank made an accounting write-off of loans and receivables given to customers that were 100% reserved in the total gross amount of BAM 1,632 thousand.

6. FINANCIAL RISK MANAGEMENT

The Bank is exposed to risks in the course of its business activities. An informed approach to risk management is a central component of our business model. This is also reflected in our risk culture and our risk appetite. By following a consistent approach to managing risks, the aim is to ensure that the liquidity and capital adequacy of the Bank continues to be appropriate at all times, as well as to achieve steady results. The overall risk profile of the Bank is appropriate and stable. This is based on an overall assessment of the individual risks, as presented in this risk report.

While the business strategy lists the objectives of the Bank for all material business activities and regions of operation and presents the measures to be taken to achieve them, the bank risk strategy addresses the material risks arising from the implementation of the business strategy and defines the objectives and measures of risk management. The risk strategy is broken down into strategies for all material risks in the Bank. The strategies are updated annually and are approved by the Management of the Bank following discussions with the Supervisory Board.

The principles of our business activity, as listed below, provide the foundation for our risk management. The consistent application of these principles reduces the risks to which the Bank is exposed.

The implemented risk management principles and strategies did not change significantly compared to the previous year. During the COVID-19 pandemic, a more conservative approach to risk management proved to be extremely adequate. The Bank recognized the risks as well as the extent of COVID-19's impact on the market and economy of Bosnia and Herzegovina and adjusted its business activities to the situation. At the very beginning of the pandemic, working groups were formed for the tasks of organizing and managing human and technical resources, operational risks, credit risk, liquidity risk and financing. The potential impacts of the pandemic were monitored and appropriate decisions were made. Organizational activities were undertaken in order to protect employees and clients, contacts and the number of employees in one place were limited, and work from home was provided for the largest number of employees. Continuity is ensured for all key functions of the Bank. In order to adequately manage credit risks, the most exposed industries were assessed and the largest number of clients were contacted in order to identify the need for mitigation measures.

For the needs of liquidity management, stress tests were performed and regular communication was maintained with the parent company in case of liquidity support. Regular monitoring of indicators has been established for early recognition and response to possible effects. In the past period, the regulator has made certain changes to the limits in order to more efficiently manage liquidity during the pandemic. The Bank did not have a liquidity problem nor was there a need to use additional sources of liquidity.

In the following period, in which the effects of the COVID-19 pandemic are present, the Bank will regularly monitor the impact on changes in credit, operational and liquidity risk.

Focus on core business

The Bank focus on the provision of financial services to small and medium businesses as well as to private clients. Accordingly, income is generated primarily in the form of interest income on customer loans and fee income from account operations and payments. All of the Banks' other operations are performed mainly in support of the core business. The Bank assume mainly credit risk, interest rate risk and liquidity risk in the course of their day-to-day operations. At the same time, the Bank avoids or very strictly limits all other risks involved in banking operations.

High degree of transparency, simplicity and diversification

The Bank's focus on small and medium-sized businesses entails a very high degree of diversification in both customer loans and customer deposits. In terms of client groups, this diversification spans economic sectors, client groups (SMEs and private clients) and income groups. The diversification of the loan portfolio is a central pillar of the credit risk management policy. A further characteristic of our approach is that we seek to provide our clients with simple, easily understandable services. This leads to a high degree of transparency not only for the respective client, but also from a risk management point of view. Both the high degree of diversification and our simple, transparent services and processes result in a significant reduction of the Bank's risk profile.

6. FINANCIAL RISK MANAGEMENT

Key elements of risk management

Risk management comprises identifying, quantifying, managing, monitoring, controlling and reporting risks. In managing risks, the Bank takes account of the "Minimum Requirements for Risk Management" (MaRisk), of relevant publications by national and international regulatory authorities and of Bank's knowledge of the markets acquired over many years. The mechanisms designed to hedge and mitigate risks are monitored regularly to ensure their effectiveness, and the procedures and methods used to manage risks are subject to ongoing further development.

The key elements of risk management in the Bank are presented below.

- The Bank applies a single common risk management framework, which defines minimum standards. The risk management policies and standards are approved by the Management of the Bank and are updated at least annually. These specify the responsibilities at Bank level, and establish minimum requirements for managing, monitoring and reporting.
- All risks assumed are managed by ensuring at all times an adequate level of regulatory and internal capital of the Bank,
- The annually conducted risk inventory ensures that all material and non-material risks are identified and, if necessary, considered in the strategies and risk management processes,
- Monitoring and control of risks and possible risk concentrations is carried out using comprehensive analysis tools for all material risks,
- Early warning indicators (reporting triggers) and limits are set and monitored for all material risks,
- Regular stress tests are performed for all material risks and for each individual risk category,
- Regular and ad-hoc reporting is carried out on the risk profile
- The effectiveness of the chosen measures, limits and methods is continuously monitored and controlled.
- Processes and procedures for an effective internal control system are in place. These ae based on principles of segregation of duties, dual control and, for all risk-relevant operations, the separation of front and back office up to the management level,
- New or significantly changed products undergo a thorough analysis before being used for the first time in order to ensure detailed new risk assessment.

Organisation of risk management position and risk reporting

The Management of the Bank bears responsibility for risk management within the Bank. The Bank has risk management department, a risk management committee and an ALCO, as well as specialised committees that address individual risks. These committees monitor and manage the risk profile of the Bank.

At the Bank level, risk positions are analysed regularly, discussed intensively and documented in standardised reports. The risk department of the Bank reports regularly to the different risk functions within the Bank and the Supervisory Board is informed on at least a quarterly basis about all risk-relevant developments.

The management of key risks in the Bank is described in greater detail in the following section. This includes: credit risk, foreign currency risk, interest rate risk and liquidity and funding risk..

6. FINANCIAL RISK MANAGEMENT *(continued)*

Management of individual risks

6.1 Credit risk

The Bank defines credit risk as the risk that losses will be incurred if the party to a transaction cannot fulfil its contractual obligations at all, not in full or not on time. Within overall credit risk we distinguish between customer credit risk, counterparty risk (including issuer risk) and country risk. Credit risk is the most significant risk facing the Bank, and customer credit exposures account for the largest share of that risk.

Maximum exposure to credit risk:

	31 December 2020	31 December 2019
Central bank balances	104,143	108,677
Loans and receivables to banks	24,612	19,905
Investment securities	5,065	43
Loans and receivables to customers	449,400	398,254
Other assets	316	436
Contingent liabilities and commitments	82,066	77,910
Total	**665,602**	**605,225**

5.1.1. Customer credit risk

The key objectives of credit risk management are to achieve high loan portfolio quality, low risk concentrations within the loan portfolio and appropriate coverage of credit risks with loan loss provisions.

The Bank serves a broad spectrum of clients, ranging from relatively small business clients with increasingly formalised structures to larger SMEs. For our lending operations, we apply the following principles, among others:

- Analysis of the debt and payment capacity of borrowers, including an analysis of future capital flows,
- Documenting credit risk analyses and processes conducted during lending operations, ensuring that the analyses performed can be understood by knowledgeable third parties,
- Strictly avoiding over indebtedness among credit clients,
- Building a long-term relationship with the client, maintaining regular contact and documenting the development of the exposure within the regular monitoring reports,
- Strictly monitoring the repayment of credit exposures,
- Applying closely customer-oriented, intensified loan management in the event of arrears,
- Collecting collateral in the event of insolvency.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

The Bank's framework for managing customer credit risk is presented in the relevant policies and standards. The policies specify, among other things, the responsibilities for managing credit risk in the Bank, the principles for the organisation of the lending business, the principles involved in lending operations, and the framework for the valuation of collateral for credit exposures. The standards contain detailed explanations of the Bank's lending operations with business clients and private clients and of the range of credit offered. They also set forth the rules governing restructuring, risk provisioning and write-offs. Thus, the policies and standards define risk-mitigating measures for the pre-disbursement phase (credit risk assessment) and the post-disbursement phase (e.g. regular monitoring of the financial situation, review of early warning indicators, and both intensified and problem loan management).

The Bank divides its credit exposures into three categories: small and medium-sized business credit exposures and credit exposures to private clients. Depending on the client category to which the respective credit exposure is assigned, different credit risk assessment processes are applied. These processes differ from one another in terms of the following attributes: the degree of segregation of duties, type of information that provides the basis for the credit analysis, criteria for credit decisions, and collateral requirements. A strict separation of front and back office functions up to the management level is applied for risk-relevant operations.

The experience of the Bank has shown that a thorough creditworthiness assessment constitutes the most effective form of credit risk management. The credit decisions of the Bank are therefore based predominantly on an analysis of the client's financial situation and creditworthiness. Regular on-site visits are performed for all clients to ensure an adequate consideration of their specific features and needs.

All credit decisions in the Bank are taken by a credit committee. Its members have approval limits that reflect their expertise and experience. All decisions on medium credit exposures are taken by credit committees at the Bank. If the exposures are particularly significant for the Bank based on its size, the decision is taken by the Supervisory Board of the Bank.

The most important factor for credit committee decisions is a funding and collateral structure that is based on the client's needs and conditional on the respective risk profile. In this context, the following general principles apply: the lower the loan amount, the more detailed the documentation provided by the client, the shorter the loan period, the longer the client's history with the Bank, and the higher the client's account turnover with the Bank, then the lower the collateral requirements will be.

The Bank'a and the group credit risk management policies limit the possibility for unsecured credit operations. Depending on the risk profile and the term of the exposure, loans may also be issued without being fully collateralised. As a general rule, credit exposures with a higher risk profile are covered with solid collateral, mostly through mortgages.

The valuation of immovable collateral is based on assessments conducted by external, independent experts, included in the list of the Bank's certified assessors. In order to ensure that a reduction in the value of the collateral is detected at an early stage and appropriate measures can be taken, plausibility checks of collateral value are a fixed component of the monitoring process for exposures. The assessments are updated at regular intervals, with plausibility checks being carried out by specialised Bank's staff.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

Based on our collateralisation requirements, securing loans with mortgages is among the most important instruments for limiting credit risk.

Type of collateral	% of total	31 December 2020	% of total	31 December 2019
Property	78.4%	342,942	70.4%	224,749
Movable property	8.8%	38,278	11.5%	36,828
Financial guarantees	11.8%	51,545	16.4%	52,297
Cash deposits	1.0%	4,408	1.7%	5,425
Total		**437,173**		**319,299**

The value of collateral is based on the most recent appriaisals taking into account internally defined haircuts depending on the type of collateral. For each loan, the value of disclosed collateral in the table above is capped at the carring amount of the loan that it is held against. The early detection of increases in credit risk at the borrower level is incorporated into all lending-related processes, resulting in prompt identification and timely assessment of the financial difficulties faced by clients.

Moreover, the Bank has developed indicators for the early identification of risks based on quantitative and qualitative risk features. These include, but are not limited to, declining account turnover or volume, high usage of granted credit lines and overdrafts over a longer period of time, and arrears. Regular recording and analysis of these early warning indicators helps to manage the performing portfolio, identify potential default risks at an early stage and take the required measures to avoid a significant increase in credit risk. Reports on the affected portfolio are regularly given to the branch managers, the Bank's head office and in aggregated form to ProCredit Holding.

Exceptional events which could have an impact on a significant part of the loan portfolio (common risk factors) are also analysed and discussed. This can lead to the imposition of limits on risk exposures towards certain groups of clients, e.g. in specific sectors of the economy or geographical regions.

In addition, asset quality indicators were implemented, on the basis of which the loan portfolio is divided into the categories: performing, underperforming and defaulted. Exposures are assigned to these categories based on a risk classification and other risk characteristics of the borrower. Of particular importance here are the risk classification, overdue contractual payments (especially those over 90 days overdue), initiation of bankruptcy proceedings or similar court procedures, restructurings or collateral liquidations by other banks, as well as other factors indicating a significant deterioration of the economic situation of the client. The indicators allow for a clear overview of the quality of the Bank's portfolio and that of an individual bank, and represent one of the most important tools for the credit risk management process.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

- The *performing* loan portfolio shows no signs of a potential risk increase. Although some exposures show early warning signals, these may not necessarily result in a risk increase being determined.
- The *underperforming* loan portfolio comprises exposures showing increased credit risk. This can be caused by temporary payment difficulties (30-90 days), restructuring or other factors. Nevertheless, the Bank still assesses full repayment of the exposure to be possible, e.g. after restructuring.
- The *defaulted* loan portfolio comprises all exposures in default, most of which have shown lasting payment difficulties (over 90 days) or other negative factors, e.g. initiation of bankruptcy proceedings. Further details are provided below.

Once a higher risk of default is detected for a credit exposure, it is placed under intensified management. This centres on close communication with the client, identification of the source of higher credit default risk and close monitoring of their business activities. Decisions on measures to reduce the credit default risk are taken by the authorised decision-making bodies. In addition, specialised recovery officers may be called in to support the intensified management of the credit exposure. One of the first steps in managing such loans is to determine the economic and financial situation of the client, as this is the most important basis for decisions on whether or not the exposure can be restructured. The aim is to take such decisions at an early stage, while the chances of stabilisation are high and before the exposure enters an advanced phase of payment delay. When a credit exposure is classified as defaulted, it is passed on to officers responsible for customer service. These officers are supported by specialists in settlement and liquidation (legal department). Collateral is sold through liquidation to a third party at the highest possible price, typically via public auction. The majority of the collateral sold consists of tangible assets such as land or buildings.

Assets obtained by taking possession of collateral (repossessed property)

Details of non-financial assets obtained by the Bank during the year by taking possession of collateral held as security against loans and advances and held at the year-end are shown below.

	31 December 2020	31 December 2019
Real estate	1,417	2,258
Land	79	79
Repossessed property	**1,496**	**2,337**

The Bank's policy is to pursue timely realisation of the collateral in an orderly manner. The Bank does not generally use the non-cash collateral for its own operations.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

Loss allowances

Loss allowances are established in line with the defined Bank standards, which are based on IFRS 9 impairment model. The forward-looking expected credit loss (ECL) model is the central element of the approach to quantifying credit loss allowances for on- and off-balance sheet financial instruments. The model calculates loss allowances considering the credit losses expected over various default scenarios in the future. The calculated loss allowances represent the sum of probability-weighted outcomes; ECL estimates are unbiased and include supportable information about past events, current conditions, and forecasts of future economic conditions.

Three-stage approach

At each reporting date, all credit exposures to customers are allocated among the three stages listed below, based on the development of credit risk since initial recognition. A specific methodology is applied for each stage in order to determine impairement. During the lifetime of an exposure, movement is possible between the stages.

- *Stage 1* comprises exposures for which credit risk has not significantly increased since initial recognition as well as those showing low credit risk as of the reporting date and for which thus there is no indication of a trigger for allocation to Stage 2 or Stage 3. Generally, all exposures are allocated to Stage 1 upon initial recognition, with the exception of those categorised as purchased or originated credit impaired (POCI) assets. For Stage 1 exposures, the expected credit losses arising from possible default events within the period of up to 12 months following the reporting date are recognised in expenses. For exposures with a remaining maturity of less than 12 months, the shorter contractual maturity is applied.

- *Stage 2* comprises exposures for which credit risk has significantly increased since initial recognition, but for which there are no objective indications of impairment. Loss allowances are established in an amount equivalent to the expected credit losses over the entire remaining maturity.

- *Stage 3* includes all defaulted exposures, i.e. as of the reporting date, there is both a significant increase in credit risk and objective indications of impairment. The respective calculation of loss allowances is performed based on the expected credit losses over the entire remaining maturity considering 100% probability of default.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

Calculation of expected credit loss (ECL)

The following parameters are used in the calculation of expected credit loss:

- Exposure at default (EAD):

EAD is the expected exposure amount at the time of a loan default. It is derived from the currently outstanding receivable from the customer and possible future changes under the applicable contractual condition. Thus, the EAD consist of the gross carrying amount at the time of default. For exposures with regular repayment plans, the modelled EAD is adjusted for the expected possibility of early repayment base on historical observations and on scenarios for the development of the economic environment and associated forecasts. Based on historical data, estimates are made of the potential exposures that may arise in the future from the utilisation of existing credit commitments such as credit lines and overdraft facilities. For financial guarantees, the EAD corresponds to the guaranteed amount, based on professional discretion, the conversion factor has generally been set at 100%.

- Probability of default (PD):

The probability of a loan default within a certain period of time is derived from historical default events. These data include the time, type and amount of default, as well as information about the risk characteristics of clients as used in the internal risk classification system. The parameters take into account country specifics and also differentiate the risk levels of exposures according the the customer segments defined at the Bank level. The Bank uses statistical models to analyse collected data and make forecasts for the expected PD based on scenarios for the development of the economic environment. In addition, PDs over the remaining lifetime of an exposure are estimated.

- Loss given default (LGD):

The expected LGD is based on historical data about recoveries obtained from defaulted clients. LGDs are calculated on a discounted cash flows, taking into account the cost of recovery, and the size of the credit exposure. Estimated LGDs are modelled as forward-looking forecasts that account for the assumed scenarios about the development of the economic environment.

Input data for the assessment of credit risk parameters are based on multi-year data histories for all borrowers in the Bank. Regression analysis is used to estimate the impact of client risk characteristics as well as macroeconomic factors for the considered parameters. Selection of relevant macroeconomic factors (GDP growth, inflation rate, unemployment rate) is based on their statistical significance and economic plausibility. For PDs and LGDs, a probability-weighted average value is calculated based on the various scenarios for the macroeconomic factors in the forecast year. In accordance with IFRS 9, the Bank uses three macroeconomic scenarios: baseline, optimistic and pessimistic each with a weight of 25%, 50% and 25%. Macroeconomic forecasts are based on IMF macroeconomic predictions.

Changes in these assumptions can lead to changes in the calculated loss allowances over time. The Bank acknowledges that discretionary decisions of the Management and estimations uncertainties can have a significant impact on the establishment of loss allowances for collectively and individually assessed exposures. Such discretion is based on the applied definition of default, the approach to determining a significant increase in credit risk (SICR), and the selected macroeconomic factors.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

Expected credit loss for all performing exposures (Stage 1 and 2) and individually insignifficant non performing exposures classified as Stage 3 (below EUR 50.000) are determined using the collective assessment of credit risk. Expected credit loss for individually significant Stage 3 exposures are determined on an individual basis (described in details below under *Definition of default*).

Significant increase in credit risk (SICR)

Quantitative and qualitative information is used to determine whether there is a significant increase in credit risk.

The quantitative test (introduced as at 31 December 2019) for SICR consist of a comparison between the expected PD over the remaining lifetime as of the reporting date and the expected PD over the corresponding time period at initial recognition. A SICR is deemed to occur if the difference between PDs exceeds a set limit of 250%. In this case the respective financial instrument is transferred from Stage 1 to Stage 2. Conversely, a transfer from Stage 2 to Stage 1 is possible when the associated credit risk has decreased significantly.

Additionally, qualitative criteria are used for SICR decisions. A transfer from Stage 1 to Stage 2 occurs if one of the following criteria applies:

- Contractual payments are past due by more than 30 days but not more than 90 days.
- Classification of the customer as "restructured" pursuant to internal policies (adjustment of contractually agreed conditions).
- The customer is assigned to a risk class defined as insufficient in the risk classification system.

Impaired credit exposures

A credit exposure is considered as credit impaired and transferred to Stage 3 if one of the following criteria is applies at the reporting date:

- Contractual payments are more than 90 days past due,
- Indications of significant financial difficulty of the debtor,
- Loan repayment is not possible without the realisation of collateral,
- Initiation of bankruptcy proceedings for the customer,
- Legal proceedings against the client that endanger the existence of the business or repayment capacity and
- Allegations of fraud against the customer.

Definition of default

The Bank has adjusted the definition of impairement according to IFRS 9 to the regulatory definition of default. This is also the definition used for internal risk management and is applied to all exposures which are part of the Bank's customer loan portfolio. The Bank considers an exposure to be impaired, and transferred to Stage 3, if at least one of the above criteria is met and the expected cash flows have been negatively impacted to such an extent that full repayment of the receivable can no longer be assumed.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

When determining provisions in Stage 3, a distinction is drawn between individually significant and individually insignificant credit exposures; the threshold is EUR 50,000. For significant exposures with indications of impairment, an individual assessment is performed to determine provisioning, taking account for the expected inflows, including collateral liquidation. For individually insignificant exposures, loss allowances are determined using parameters for the collective assessment of credit risk. Returning an exposure from Stage 3 to lower stage is possible if the customer is able to settle outstanding debts in full without recourse to collateral realisation. No migration between stages is possible for POCI exposures.

Purchased or Originated Credit Impaired (POCI) exposures

The Bank has separate rules for POCI (Purchased or Originated Credit Impaired) exposures. Within our business model, the acquisition of impaired exposures is not permitted. POCI exposures can only arise in a course of a new negotiation through significant modification of the contractually agreed cash. For POCI exposures, no allowances for impairment are made at the time of initial recognition. In subsequent periods, any changes to the estimated lifetime ECL are recognised as an expense in the profit and loss and reported accordingly as loss allowances for these exposures.

Changes to contractual terms (modifications)

Changes to the originally agreed contractual conditions of an exposures are possible, in particular with the aim of improving the prospect of repayment and, if possible, avoiding default, foreclosure or the realization of collateral. The Bank uses quantitative and qualitative factors to determine the existence of a substantial modification of contractual conditions. As a quantitative factor, the net present value of cash flows is determined in order to assess the changed condition of an exposure (The Net Present Value Test). In the event of a substantial modification, the original loan is derecognised and a new loan is recognised at its fair value at the modification date. In the case of non-substantial change, the gain or loss from modification is recognized in profit or loss.

Write off

When a loan is uncollectable, it is written off against the corresponding loss allowance which has been set aside, provided there is no justified expectation of repayment.

For exposures of any size, the Bank carry out an individual assessment of justified feasibility of repayments. For exposures bellow EUR 10 thousands, this assessment is to be carried out at the latest once payment is 180 days overdue; for largest exposures, at the latest after 360 days, particularly if there is no realisable collateral. Based on the assessment the Bank may decide to write off the exposure or continue to actively manage the exposure in order to allow for further repayment of the loan.

Policy applicable from 1 January 2020 - Decision on credit risk management and determination of expected credit losses

In accordance with the Decision on Credit Risk Management and Determination of Expected Credit Losses, effective from January 1, 2020, the Bank writes off the balance sheet exposure two years after the Bank has recognized expected credit losses in the amount of 100% of the gross book value of that exposure. and declared it fully due.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

COVID-19

The COVID-19 pandemic had a negative impact on the operations of a certain part of legal entities, and on a part of private individuals with the possible consequence of the emergence of liquidity difficulties in settling their financial obligations. In order to reduce long-term negative impacts on the economy, the Bank has taken a number of measures within the framework set by the Banking Agency of the Federation of Bosnia and Herzegovina, EBA guidelines received thru the Group, and similar measures have been applied by other credit institutions in the market. In accordance with the above, since the beginning of the pandemic in 2020, the Bank has approved measures to clients affected by the negative effects of the pandemic. During the state of "Natural or other disasters in the territory of Bosnia and Herzegovina", the Bank granted clients a temporary moratorium measure. During the moratorium, the Bank did not calculate penalty interest on the amount of overdue receivables. On the other hand, the regular calculation of interest was further performed and it was attributed to the final repayment plan after the final modality was agreed.

Upon expiration of temporary measures (measures during the state of natural disaster), special measures approved by the Bank to clients, private and legal persons, were:

a) moratorium, ie delay in repayment of credit obligations for a maximum of 6 months (not counting the temporary moratorium),
b) introduction of a "grace" period for repayment of the principal of credit obligations in the case of loans that are repaid in annuity for a period not exceeding 6 months,
c) extension of the maturity for repayment of annuity loans,
d) extension of the maturity of single-maturity loans, including revolving loans and overdrafts on transaction accounts, whereby clients could use during that period the part of the exposure that was unused on the day of modification,
e) granting an additional amount of exposure for the purpose of overcoming current liquidity difficulties,
f) adjusting the repayment plan in proportion to the reduction of income or some other relevant parameter determined by the bank,
g) other measures taken by the bank in order to facilitate the servicing of the client's credit obligations and the establishment of sustainable business flow of the client.

In accordance with the regulatory framework, the measures were approved as of December 31, 2020. Approval of the moratorium measure or other special measures did not in itself cause reclassification of exposures into restructured exposures or reclassification of clients to a higher level of risk or default status, and instead, regular credit risk analysis was conducted for all exposures and in line with available data and information collected from clients the Bank assessed the likelihood of clients being unable to timely fulfill their obligations.

In the initial months under the COVID-19 pandemic, the Bank approved some of the measures to a significant number of clients and loans. In relation to the balance of the loan portfolio as of December 31, 2020, the Bank approved some of the measures for 40% of the total volume of approved loans. As of December 31, 2020, 8% of total loans were still under active measure.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

COVID-19 (continued)

The table below presents the total exposure of loans for which one of the possible measures was approved as of December 31, 2020.

	2020							
	Stage 1		Stage 2		Stage 3		**Total**	
	Number of accounts	Exposure BAM '000	Number of accounts	Exposure BAM '000	Number of accounts	Exposure BAM '000	**Number of accounts**	**Exposure BAM '000**
Business								
Moratoria	4	4,592	-	-	-	-	**4**	**4,592**
Grace period	1	356	-	-	-	-	**1**	**356**
Additional resources	119	28,265	6	566	-	-	**125**	**28,831**
Extension of short-term placements	4	741	9	631	-	-	**13**	**1,372**
Private								
Moratoria	1	42	1	13	-	-	**2**	**55**
Additional resources	3	200	-	-	-	-	**3**	**200**
Total:	**132**	**34,196**	**16**	**1,210**	**-**	**-**	**148**	**35,406**
% of the total portfolio	**3.6%**	**7.7%**	**0.4%**	**0.3%**	**-**	**-**	**4.1%**	**8.0%**

Given the sudden and significant economic downturn due to the shock caused by COVID 19, the Bank categorized the loan portfolio based on which the Bank prioritized credit exposure monitoring in line with the potential impact of COVID-19.

When classifying the loan portfolio, two main criteria were taken into account:

1. The main financial indicators of the client obtained on the basis of the last risk classification, and
2. Expected impact of the sector (estimated risk for the sectors is based on current events and the impact of government interventions, and projected long-term economic consequences).

Based on the expected impact of the pandemic, the loan portfolio is grouped into the following categories:

- ***low impact of COVID 19*** - the client is not affected by the consequences of the COVID-19 pandemic, or is affected only to a lesser extent; the company can overcome the situation by applying general measures (moratorium, grace period, and other support). No delays in obligations are expected. Demand for working capital funds can be expected to meet new orders.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

COVID-19 (continued)

- ***medium impact of COVID 19*** - the client is under the influence of COVID 19 despite the approved moratorium; the client could overcome this situation with its own resources (liquidity), but it could need funds for working capital, possibly for operating costs, and possible delays can be expected; restructuring is not required.
- ***high influence of COVID 19*** - the client is under the influence of COVID 19 despite the approved moratorium, usually longer than 6 months; the client could overcome this situation with funds from banks, and / or the sale of fixed assets; the client may need funds for working capital, funds for operating costs for more than 3 months, and possible delays can be expected; a restructuring option is possible.
- ***very high impact of COVID 19*** - restructuring is more likely to be required

All modified credit exposures of the company will be categorized into two groups:

(1) regular monitoring - the next monitoring may be performed according to the regular schedule;

(2) priority monitoring - if the client has some of the defined characteristics that indicate a greater sensitivity of the client to the negative consequences of a pandemic.

Priority monitoring means that the next monitoring needs to be carried out earlier than planned.

At the end of the year, the Bank, through deteriorating risk classifications, recognized increased credit risk with the group of clients affected by the negative impact of the COVID-19 pandemic, and operating in industries significantly affected by the negative impact, and for these exposures life time credit losses are recognised.

In addition to approving measures for clients affected by the COVID 19 pandemic and monitoring the client in order to identify increased risk due to the COVID-19 pandemic, activities in risk management were focused on activities related to updating macroeconomic scenarios in calculating expected losses and generating adequate amounts of expected losses for customers whose business has been affected or is expected to be significantly affected by the impact of the COVID-19 pandemic.

The GDP growth forecast for 2020 was derived by weighing the actual IMF forecasts for 2020, 2021 and 2022 (published in April 2020). The weights for the forecasts for each of these years are determined on the basis of the maturity structure of the portfolio (for deriving the weights, the shares in the volume of exposure maturing in 2020, 2021 and 2022 and later are used).

6. UPRAVLJANJE FINANSIJSKIM RIZIKOM *(nastavak)*

6.1 Kreditni rizik *(nastavak)*

6.1.1. Kreditni rizik klijenta *(nastavak)*

Credit quality analysis and credit risk concentration

The following table provides an overview of the respective gross and net customer loan portfolio, as well as respective loss allowances:

	Stage 1 Stage 12-month ECL	Stage 2 Life time ECL	Stage 3 Life time ECL	POCI	Total
31 December 2020					
Business loans					
Gross outstanding amount	373,166	61,460	11,425	270	**446,321**
Loss allowances	(2,326)	(3,267)	(10,763)	(270)	**(16,626)**
Carrying amount	**370,840**	**58,193**	**662**	**-**	**429,695**
Private loans					
Gross outstanding amount	18,181	1,975	822	-	**20,978**
Loss allowances	(436)	(140)	(697)	-	**(1,273)**
Carrying amount	**17,745**	**1,835**	**125**	**-**	**19,705**

	Stage 1 Stage 12-month ECL	Stage 2 Life time ECL	Stage 3 Life time ECL	POCI	Total
31 December 2019					
Business loans					
Gross outstanding amount	340,516	37,637	14,671	270	**393,094**
Loss allowances	(987)	(337)	(10,395)	(263)	**(11,982)**
Carrying amount	**339,529**	**37,300**	**4,276**	**7**	**381,112**
Private loans					
Gross outstanding amount	15,642	1,689	858	-	**18,189**
Loss allowances	(286)	(82)	(679)	-	**(1,047)**
Carrying amount	**15,356**	**1,607**	**179**	**-**	**17,142**

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

The following table shows the information on credit quality of loans and receivables. For loan commitments and financial guarantee contracts, the amounts in the table represent the amounts committed or guaranted.

31 December 2020

	Stage 1	Stage 2	Stage 3	POCI	Total
Loans and advances to customers					
Grade 1-5	366,418	49,353	-	-	**415,771**
Grade 6-7	45	7,289	-	-	**7,334**
Grade 8	-	-	9,851	-	**9,851**
Not graded	24,884	6,793	2,396	270	**34,343**
Total	**391,347**	**63,435**	**12,247**	**270**	**467,299**
Less: imapirment	2,762	3,407	11,460	270	**17,899**
Total	**388,585**	**60,028**	**787**	**-**	**449,400**

31 December 2020

	Stage 1	Stage 2	Stage 3	POCI	Total
Guarantees					
Grade 1-5	36,633	1,700	-	-	**38,333**
Grade 6-7	-	215	-	-	**215**
Grade 8	-	-	-	-	**-**
Not graded	1,191	421	-	-	**1,612**
Total	**37,824**	**2,336**	**-**	**-**	**40,160**
Less: imapirment	98	79	-	-	**177**
Total	**37,726**	**2,257**	**-**	**-**	**39,983**

31 December 2020

	Stage 1	Stage 2	Stage 3	POCI	Total
Loan commitments					
Grade 1-5	36,677	1,523	-	-	**38,200**
Grade 6-7	-	29	-	-	**29**
Grade 8	-	-	-	-	**-**
Not graded	3,384	210	-	-	**3,594**
Total	**40,061**	**1,762**	**-**	**-**	**41,823**
Less: imapirment	177	57	-	-	**234**
Total	**39,884**	**1,705**	**-**	**-**	**41,589**

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

31 December 2019

	Stage 1	Stage 2	Stage 3	POCI	Total
Loans and advances to customers					
Grade 1-5	337,136	36,097	-	-	**373,233**
Grade 6-7	-	1,146	-	-	**1,146**
Grade 8	-	-	13,342	-	**13,342**
Not graded	19,022	2,083	2,187	270	**23,562**
Total	**356,158**	**39,326**	**15,529**	**270**	**411,283**
Less: imapirment	*1,273*	*419*	*11,074*	*263*	***1,.029***
Total	**354,885**	**38,907**	**4,455**	**7**	**398,254**

31 December 2019

	Stage 1	Stage 2	Stage 3	POCI	Total
Guarantees					
Grade 1-5	40,547	1,557	-	-	42,104
Grade 6-7	39	39	-	-	78
Grade 8	-	-	-	-	-
Not graded	280	-	-	-	280
Total	**40,866**	**1,596**	**-**	**-**	**42,462**
Less: imapirment	**42**	**6**	**-**	**-**	**48**
Total	**40,824**	**1,590**	**-**	**-**	**42,414**

31 December 2019

	Stage 1	Stage 2	Stage 3	POCI	Total
Loan commitments					
Grade 1-5	31,817	1,651	-	-	33,468
Grade 6-7	-	-	-	-	-
Grade 8	-	-	-	-	-
Not graded	1,529	6	-	-	1,535
Total	**33,346**	**1,657**	**-**	**-**	**35,003**
Less: imapirment	**54**	**2**	**-**	**-**	**56**
Total	**33,292**	**1,655**	**-**	**-**	**34,947**

The credit risk of loans and receivables and credit lines and guarantees is presented through the internal credit risk classification. Not graded category relates to all private clients and business clients with exposure below EUR 50,000.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

The following table sets out information about the overdue status of loans and advances to customers in Stages 1, 2 and 3.

31 December 2020

	Stage 1	Stage 2	Stage 3	**Total**
Loans and advances to customers – gross carrying amount				
Current	382,283	57,458	208	**439,949**
Overdue < 30 days	9,064	5,239	-	**14,303**
Overdue > 30 days < 90 days	-	738	67	**805**
Overdue > 90 days	-	-	11,972	**11,972**
Total:	**391,347**	**63,435**	**12,247**	**467,029**

31 December 2019

	Stage 1	Stage 2	Stage 3	**Total**
Loans and advances to customers – gross carrying amount				
Current	347,958	36,288	207	**384,453**
Overdue < 30 days	8,200	2,991	845	**12,036**
Overdue > 30 days < 90 days	-	47	218	**265**
Overdue > 90 days	-	-	14,259	**14,259**
Total:	**356,158**	**39,326**	**15,529**	**411,013**

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

The following table presents gross and net exposures, broken down according to economic sector and by stage.

31. decembar 2020.			**Business loans**				**Private loans**		
u KM '000	Wholesale and retail trade	Agriculture, forestry and fishing	Production	Transporation and storage	Other economic activities	Housing	Investment loans and OVDs	Others	**Total**
Stage 1									
Gross outstanding amount	135,025	113,258	34,401	16,580	73,902	11,469	6,712	-	**391,347**
Loss allowances for loans to customers	(789)	(727)	(222)	(105)	(482)	(256)	(181)	-	**(2,762)**
Net outstanding amount	134,236	112,531	34,179	16,475	73,420	11,213	6,531	-	**388,585**
Stage 2									
Gross outstanding amount	17,298	20,381	3.465	736	19,580	1,886	65	24	**63,435**
Loss allowances for loans to customers	(1,027)	(1,021)	(205)	(37)	(977)	(134)	(4)	(2)	**(3,407)**
Net outstanding amount	16,271	19,360	3.260	699	18.603	1.752	61	22	**60,028**
Stage 3									
Gross outstanding amount	1,688	6,770	179	911	1.878	323	415	83	**12,247**
Loss allowances for loans to customers	(1,586)	(6,483)	(159)	(776)	(1.760)	(263)	(350)	(83)	**(11,460)**
Net outstanding amount	102	287	20	135	118	60	65	-	**787**
POCI									
Gross outstanding amount	270	-	-	-	-	-	-	-	**270**
Loss allowances for loans to customers	(270)	-	-	-	-	-	-	-	**(270)**
Net outstanding amount	-	-	-	-	-	-	-	-	**-**

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

31 December 2019	**Business loans**					**Private loans**			
in BAM '000	Wholesale and retail trade	Agriculture, forestry and fishing	Production	Transporation and storage	Other economic activities	Housing	Investment loans and OVDs	Others	**Total**
Stage 1									
Gross outstanding amount	110,962	3	130,170	32,909	66,471	10,969	4,364	310	**356,158**
Loss allowances for loans to customers	(334)	-	(348)	(90)	(214)	(198)	(82)	(7)	**(1,273)**
Net outstanding amount	110,628	3	129,822	32,819	66,257	10,771	4,282	303	**354,885**
Stage 2									
Gross outstanding amount	11,710	-	15,818	4,548	5,560	1,608	69	13	**39,326**
Loss allowances for loans to customers	(99)	-	(145)	(35)	(57)	(79)	(3)	(1)	**(419)**
Net outstanding amount	11,611	-	15,673	4,513	5,503	1,529	66	12	**38,907**
Stage 3									
Gross outstanding amount	8,217	458	3,151	387	2,458	446	342	70	**15,529**
Loss allowances for loans to customers	(5,476)	(458)	(2,255)	(309)	(1,897)	(352)	(262)	(65)	**(11,074)**
Net out standing amount	2,741	-	896	78	561	94	80	5	**4,455**
POCI									
Gross outstanding amount	-	-	270	-	-	-	-	-	**270**
Loss allowances for loans to customers	-	-	(263)	-	-	-	-	-	**(263)**
Net outstanding amount	-	-	7	-	-	-	-	-	**7**

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

Credit risk at the portfolio level is assessed on a monthly basis and, if necessary, more frequently. This includes an analysis of portfolio structure and quality, restructured exposures, write offs, the coverage level and concentration risk.

Concentration risk in the customer loan portfolio is effectively limited by a high degree of diversification. This diversification is a consequence of lending to small and medium-sized businesses in various economic sectors and to private clients, and the distribution of the loan portfolio.

The following table presents gross loans broken down according to business area, economic sector and loan size.

31 December 2020	up to EUR 50,000	EUR 50,000 – 250,000)	over 250,000 EUR	**Total**
Business loans				
Production	7,270	52,169	94,843	**154,282**
Trade	11,667	58,257	70,484	**140,408**
Transport and warehousing	3,675	18,002	16,368	**38,045**
Agriculture, forestry	813	8,163	9,251	**18,227**
Other business activities	7,517	38,362	49,480	**95,359**
Total business loans	**30,942**	**174,953**	**240,426**	**446,321**
Private loans				
Housing loans	4,794	7,488	1,396	**13,678**
Investment loans and OVDs	4,450	2,365	389	**7,204**
Other	96	-	-	**96**
Total private loans	**9,340**	**9,853**	**1,785**	**20,978**
Total customer loan portfolio (gross)	**40,282**	**184,806**	**242,211**	**467,299**

31 December 2019	up to EUR 50,000	EUR 50,000 – 250,000	over 250,000 EUR	**Total**
Business loans				
Production	7,270	55,100	87,039	**149,409**
Trade	11,150	52,675	67,064	**130,889**
Transport, telecommunications and communications	3,950	19,304	14,591	**37,845**
Agriculture, forestry	461	-	-	**461**
Other	5,696	29,346	39,448	**74,490**
Total business loans	**28,527**	**156,425**	**208,142**	**393,094**
Private loans				
Housing loans	5,554	6,896	573	**13,023**
Investment loans and OVDs	2,822	1,368	584	**4,774**
Other	392	-	-	**392**
Total private loans	**8,768**	**8,264**	**1,157**	**18,189**
Total customer loan portfolio (gross)	**37,295**	**164,689**	**209,299**	**411,283**

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

In addition, the Bank limit the concentration risk of their portfolios by means of the following requirements: Large credit exposures (those exceeding 10% of the regulatory capital of the Bank) require the approval of the Group Risk Management Committee and of the Supervisory Board of the Bank. No large credit exposure may exceed 25% of regulatory capital of a Bank, and the sum of all large credit exposures of a Bank may not exceed 150% of its regulatory capital.

The quality of the loan portfolio in all client categories is monitored by credit control units at the Bank. They assess the quality of the credit analysis as well as compliance with internal procedures and identify signs of fraudulent activity. These teams comprise experienced staff who not only conduct on-site visits to customers in order to monitor the lending process but also systematically screen the portfolio for irregularities.

Continuous training of the staff ensures that credit risk is properly evaluated whenever a loan is issued, and that credit exposures are closely observed throughout their lifetime and, if necessary, that appropriate measures are taken in a timely manner.

6.1.2 Counterparty risk, including issuer risk

The Bank defines counterparty risk, including the risk of the issuer, as the risk that a counterparty/issuer cannot fulfil its contractual obligations at all, not in full or not on time. Counterparty risk in the bank mainly arises from keeping highly liquid assets for the purpose of managing liquidity. There are also structural exposures towards Central Bank of Bosnia and Herzegovina in the form of mandatory minimum reserves.

In order to minimize the counterparty's risk, the Bank conducts business with banks with high credit ratings, short-term placements and the Bank uses a very limited number of financial instruments.

The Bank is prohibited from engaging in speculative trading and, where necessary, the Bank purchases highly liquid securities with a maximum maturity of up to three months. During 2020 and 2019, the Bank did not invest or deposit funds with other institutions.

	31 December 2020	**in %**	**31 December 2019**	**in %**
Central bank balances	104,342	77.9%	108,792	84.6%
Loss allowances for central bank balances	*(199)*		*(115)*	
Of which obligatory reserve	53,297		*47,047*	
Of which other balances	51,045		*61,745*	
Current accounts with other banks (mainly ProCredit group)	24,657	18.4%	*19,905*	15.5%
Loss allowances for current accounts with other banks institutions	*(45)*		*(-)*	
Investment in securities	5,066	3.8%	43	0.0%
Impairment	*(5)*		-	
Total	**134,015**	**100.0**	**128,740**	**100.0**

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.1 Credit risk *(continued)*

6.1.1. Customer credit risk *(continued)*

The exposures to counterparties and issuers are managed on the basis of the limit system, as is the case with clients' credit risk. The Bank concludes transactions only with other counterparties for which an analysis has been made and for which a limit has been approved. An approval is also required prior to investing in securities other than those centrally issued or central bank securities in local currency with a remaining maturity of up to three months. During 2020 and 2019, the Bank did not invest or deposit funds with other institutions.

6.1.2 Country risk

The Bank defines country risk as the risk that the Bank is not able to enforce rights over certain assets in a country or that a counterparty in that country is unable to perform an obligation due to convertibility or transfer restrictions or expropriation of its cross-border obligations. Country risk thus arises solely from cross-border transactions.

The Bank is only exposed to country risk to a very limited extent through nostro accounts maintained with other banks (mainly ProCredit Bank member banks).

6.2. Market risks

Market risks are defined as risks of possible losses due to changes in market prices, such as exchange rates or other parameters which influence prices. Relevant market risks for the Bank are foreign currency risk and interest rate risk in the banking book. The Bank manages market risks in such a way that their impact is as limited as possible from an overall risk perspective. In line with the ProCredit Group strategy, currency risk and interest rate risk cannot be used for speculative purposes. The Bank is non-trading book institution.

6.2.1. Foreign currency risk

Foreign currency risk is the risk that the Bank incurs losses due to exchange rate fluctuations or that the Bank's equity is reduced through currency translation effects. Foreign currency risk can have adverse effects on income and can lead to a decline in regulatory capital ratios.

Results are impacted negatively when the volume of its assets and liabilities denominated in foreign currencies do not match and the exchange rates move unfavourably. The key risk indicator that captures the balance sheet discrepancy for each currency is the open currency position (OCP). Limits for OCP are set at the Bank level and also take into account limits prescribed by the regulator.

The following table shows the open credit positions of the Bank in EUR and in USD. The position "other currencies" mainly includes CHF and other currencies with relatively small transaction volume. The banks keeps their significant amount of assets and liabilities in EUR and due to the fixed EUR/BAM rate the Bank assumes that this risk is very limited.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.2. Market risks (continued)

6.2.1. Foreign currency risk (continued)

31 December 2020	BAM	EUR*	USD	Other currencies	Total
Financial assets					
Cash and cash equivalents	5,582	1,135	20	7	6,744
Obligatory reserves at the Central bank of BiH	104,091	52	-	-	104,143
Loans and advances to banks	5,130	13,569	5,729	184	24,612
Loans to customers	96,220	353,180	-	-	449,400
*of which indexed to EUR**	-	*353,180*	-	-	*353,180*
Investment in securities	5,001	64	-	-	5,065
Other assets	202	113	1	-	316
	216,226	**368,113**	**5,750**	**191**	**590,280**
Financial liabilities					
Liabilities to banks	-	40,957	-	-	40,957
Liabilities to financial institutions	-	179,747	-	-	179,747
Liabilities to customers	197,114	127,321	5,986	123	330,544
*of which indexed to EUR**	-	*12,550*	-	-	*12,550*
Subordinated debt	-	8,804	-	-	8,804
Provisions for guarantees and loan commitments	313	96	2	-	411
Other liabilities	1,568	267	2	-	1,837
	198,995	**357,192**	**5,990**	**123**	**562,300**
Net position	***17,231***	***10,922***	***(240)***	***68***	***27,981***

* The Bank has a number of agreements governed by a foreign currency clause. Due to the fixed relationship between EUR and BAM, the Bank is not exposed to significant currency risk from positions denominated in EUR.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.2. Market risks (continued)

6.2.1. Foreign currency risk (continued)

31 December 2019	BAM	EUR*	USD	Other currencies	Total
Financial assets					
Cash and cash equivalents	5,310	1,384	11	7	6,712
Obligatory reserves at the Central bank of BiH	99,781	8,895	-	-	108,676
Loans and advances from banks	5,081	12,620	1,841	363	19,905
Loans to customers	80,891	317,363	-	-	398,254
*of which indexed to EUR**	-	317,363	-	-	317,363
Investment in securities	-	43	-	-	43
Advance payment of current tax on	236	-	-	-	236
Other assets	272	161	3	-	436
	191,571	**340,466**	**1,855**	**370**	**534,262**
Financial liabilities					
Liabilities to banks	-	39,180	-	-	39,180
Liabilities to other financial institutions	1,799	168,043	-	-	169,842
Liabilities to customers	160,104	120,094	1,809	160	282,167
*of which indexed to EUR**		16,773			16,773
Subordinated debt	-	8,804	-	-	8,804
Provisions for guarantees and loan commitments	77	26	1	-	104
Other liabilities	1,830	246	-	-	2,076
	163,810	**336,393**	**1,810**	**160**	**502,173**
Net position	*27,761*	*4,073*	*45*	*210*	*32,089*

* The Bank has a number of agreements governed by a foreign currency clause. Due to the fixed relationship between EUR and BAM, the Bank is not exposed to significant currency risk from positions denominated in EUR.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.2. Market risks (continued)

6.2.2. Interest rate risk in the banking book

Interest rate risk is the risk of incurring losses due to changes in market interest rates and primarily arises from differences between the repricing maturities of assets and liabilities. The aim of interest rate risk management is to keep these differences as small as possible in all currencies. This is particularly relevant against the background of the limited opportunities to manage this risk using interest rate derivatives in local currency.

The measuring, monitoring and limiting of interest rate risk is based on economic value impact and P&L-oriented indicators. The risk is measured on a regular basis, at least quarterly. The assets and liabilities are distributed across time buckets according to the terms of the underlying contracts. Interest-bearing sight deposits and savings accounts are included in the gap analyses.

At the Bank level, we assume a parallel shift of the interest rate curve. For EUR and USD the interest rate shock is ± 200 basis points, whereas for domestic currencies the magnitude of the shock is derived on the basis of a historical analysis. Limits are set in relation to regulatory capital (non-netted in each case) for the economic value impact and for the P&L effect.

Total net weighted position of banking book is stated in absolute amount and represents economic value impact which is a result from application of standard interest rate shock.

	Economic Value Impact	
Currency	**31 December 2020**	**31 December 2019**
BAM	(867)	(587)
EUR	(3,497)	(1,504)
USD	-	-
Other currencies	(81)	(27)
Total (in BAM '000)	**(4,445)**	**(2,118)**

The Bank started with economic value impact calculations in line with the new regulation framework in 2018.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.3. Liquidity and funding risk

Liquidity and funding risk addresses the Bank's short- and long-term ability to meet its financial obligations in a complete and timely manner, even in stress situations.

The Bank assesses short-term liquidity risk in the Bank on the basis of a liquidity gap analysis, among other instruments, and the Bank monitors this risk using numerous indicators. These include a 30-day liquidity indicator (sufficient liquidity indicator - "*SLI"*), a survival period and the minimum liquidity ratio stipulated by Capital Requirements Regulations - CRR (Liquidity Coverage Ratio, '*LCR*') as well as a local regulator. The SLI measures whether institutions have sufficient liquidity in relation to the expected inflows and outflows of funds in the next 30 days. The survival period is the timeframe during which the banks are able to fulfil all payment obligations, despite reduced liquidity inflows and elevated outflows. The calculation applies outflows derived from historical analyses of deposit movements in the Bank. LCR indicates whether the Bank have sufficient liquidity to cover the net outflows expected in the next 30 days, even in the event of a specified severe economic shock scenario.

In addition, early warning indicators are defined and monitored, and the key indicator in this respect is the highly liquid assets *(HLA)* indicator, which ensures that the Bank holds sufficient highly liquid assets at all times to be able to pay out a certain percentage of all customer deposits.

Market-wide, institution-specific, combined and longer-term stress tests are conducted monthly and ad hoc to make sure that the Bank keeps sufficient liquid funds to meet its obligations, even in difficult times. Moreover, the Bank has a contingency plan. If unexpected circumstances arise and the Bank proves not to have sufficient liquid funds, the ProCredit group has also developed a liquidity contingency plan and ProCredit Holding would step in as a "lender of last resort". ProCredit Holding keeps an adequate liquidity reserve available for this purpose. The amount of the liquidity reserve is determined on the basis of group stress tests and monitored on a regular basis.

The liquidity of the Bank is managed on a daily basis by the respective treasury departments, based on the Group ALCO-approved cash flow projections, and is monitored by risk management and ALCO. The Bank had enough liquidity available at all times in 2019 to meet all financial obligations in a timely manner.

The Bank held extraordinary ALCO committees to monitor the effects of the COVID-19 pandemic on liquidity risk and maturity compliance. During March, the bank performed a stress test in order to identify potential effects on the maturity structure and compliance, and activities were undertaken to provide adequate sources to meet liquidity requirements. The Bank did not have significant outflows of customer deposits during the COVID-19 pandemic, nor were liquidity positions threatened.

The following tables show the undiscounted cash flows of the financial assets and financial liabilities of the Bank according to their remaining contractual maturities. The remaining contractual maturity is defined as the period between the balance sheet date and the contractually agreed due date of the asset or liability, or the due date of a partial payment under the contract for an asset or liability.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.3 Liquidity risk management *(continued)*

31 December 2020	Carrying amount	Gross nominal inflow/out flow	up to 1 month	1 - 3 months	4 - 12 months	1 – 5 years	over 5 years
Financial assets							
Cash in hand	**6,744**	**6,744**	6,744	-	-	-	-
Funds held at the Central Bank of BiH	**104,143**	**104,338**	104,338	-	-	-	-
Loans and receivables to banks	**24,612**	**24,658**	24,658	-	-	-	-
Loans and receivables to customers	**449,400**	**495,666**	24,882	42,437	120,329	227,271	80,747
Investment securities	**5,065**	**5,065**	-	-	5,001	-	64
Other assets	**316**	**316**	306	-	10	-	-
Total assets	**590,280**	**636,787**	**160,928**	**42,437**	**125,340**	**227,271**	**80,811**
Financial liabilities							
Liabilities to banks	**40,957**	**41,012**	-	17,745	23,267	-	-
Liabilities to other financial institutions	**179,747**	**182,920**	666	618	42,692	123,225	15,719
Liabilities to customers	**330,544**	**332,832**	218,548	8,186	44,754	59,510	1,834
Subordinated debt	**8,804**	**11,909**	46	86	388	2,070	9,319
Other liabilities	**1,837**	**1,961**	541	68	304	932	116
Ukupno obaveze	**561,889**	**570,634**	**219,801**	**26,703**	**111,405**	**185,737**	**26,988**
Contingent liabilities							
Financial guarantees	**228**	**40,160**	40,160	-	-	-	-
Credit commitments (irrevocable loan commitments)	**183**	**28,055**	28,055	-	-	-	-
Contractual liquidity surplus	**27,980**	**2,062**	**(127,088)**	**15,734**	**13,935**	**41,534**	**53,823**

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.3 Liquidity risk management *(continued)*

	Carrying amount	Gross nominal inflow/out flow	up to 1 month	1 - 3 months	4 - 12 months	1 – 5 years	over 5 years
31 December 2019							
Imovina							
Cash in hand	**6,712**	**6,712**	6,712	-	-	-	-
Funds held at the Central Bank of BiH	**108,676**	**108,676**	108,676	-	-	-	-
Loans and receivables from banks	**19,905**	**19,905**	19,905	-	-	-	-
Loans and receivables to customers	**398,254**	**436,199**	23,509	45,006	101,185	197,805	68,694
Investment securities	**43**	**43**	-	-	-	-	43
Other assets	**436**	**436**	436	-	-	-	-
Total assets	**534,026**	**571,971**	**159,238**	**45,006**	**101,185**	**197,805**	**68,737**
Liabilities							
Liabilities to banks	**39,180**	**39,269**	-	23,635	15,634	-	-
Liabilities to other financial institutions	**169,842**	**179,623**	676	925	53,502	109,368	15,152
Liabilities to customers	**282,167**	**283,806**	171,455	16,044	72,477	20,726	3,104
Subordinated debt	**8,804**	**12,986**	-	-	527	2,100	10,359
Other liabilities	**2,076**	**2,363**	38	100	454	1,205	566
Total liabilities	**502,069**	**518,047**	**172,169**	**40,704**	**142,594**	**133,399**	**29,181**
Contingent liabilities							
Guarantees	**48**	**42,462**	42,462	-	-	-	-
Credit commitments (irrevocable loan commitments)	**56**	**24,785**	24,785	-	-	-	-
Contractual liquidity surplus	**31,853**	**(13,323)**	**(80,178)**	**4,302**	**(41,409)**	**64,406**	**39,556**

Short-term liquidity risk is measured primarily by means of LCR. As of 31 December 2020, the LCR was 241% (201: 187%), and thus comfortably above the local regulatory requirement of minimum 100%. Funding risk is the danger that additional funding cannot be obtained, or can only be obtained at higher costs. It therefore covers parts of the non-systemic effect of interest rate changes. This risk is mitigated by the fact that the Bank finances its lending operations primarily through customer deposits which are supplemented by long-term credit lines from international financial institutions (IFIs). As of 31 December 2020 the largest funding source was customer deposits, with BAM 331 million (2019: BAM 282 million). International Financial Institutions within the group and the Other International financial institutions (IFIs) are the second largest source of funding.

The Bank manages, measures and limits funding risk through business planning, maturity gap analysis and several indicators, including stress scenario on a vista funding withdrawals. The funding needs of the Bank, identified in the business planning process, are monitored and regularly reviewed at the Bank and at the group level. ProCredit Holding also offers bridge financing in the event of assessed need, and currently the Bank has stand by line approved by ProCredit Holding in the amount of EUR 5 million. A key indicator for limiting funding risk is the deposit concentration indicator. Two more indicators additionally restrict the level of funding from the interbank market.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.4 Capital management

Capital management in the Bank is guided by the principle that the Bank may at any time incur greater risks than they are able to bear. This principle is monitored using different indicators for which early warning indicators and limits have been established.

The indicators for the Bank include, in addition to regulatory standards, a capital adequacy calculation in accordance with CRR requirements, a Tier 1 leverage ratio in accordance with CRR and an internal capital adequacy assessment.

The objective of capital management is to maintain sufficient and adequate capital level which can in any moment meet all of qualitative and quantitative requirements. Thus providing normal activity of the Bank.

The capital management framework of the Bank has the following objectives:

- Compliance with regulatory capital requirements (normative perspective)
- Ensuring adequate capitalisation in the economic perspective
- Compliance with the internally defined capital requirements and creation of a sufficient capital buffer

The capital management of the Bank is governed by internal policies and monitored on a monthly basis by the ACLO committee.

Internal capital adequacy

ProCredit Bank faces various risks resulting from its business activities. The Bank manages the risks appropriately and in accordance with their significance to the Bank. The risk catalogue is an instrument which should identify materiality of risks to which the Bank is exposed, to present the overall risk profile of the Bank. The risk catalogue is a basis for the Bank's risk management. The risk catalogue consists of the introductory document and a special risk catalogue table. The introductory document provides for an overview of the general risk catalogue framework, responsibilities and steps to be taken to assess individual risk categories. The risk catalogues provides for an overview of all potential risks and assessment of their significance to the Bank.

The risk catalogue is regularly updated, at least once a year, or more often if required, starting the risk identification process and assessing their materiality. In determination of materially significant risks to which the Bank is exposed, and which will be included into internal capital adequacy assessment process, the type, scope and complexity of business operations are taken into account as well as specifics of market where the bank operates. Also, previous experience in risk management of the Bank and ProCredit Group are taken into account, including historical data on negative effects on financial performance and capital of the Bank.

Identification and risk management is performed by Risk Management Department in cooperation with other relevant Departments/Units in accordance with the criteria for material significance for specific risk stated in risk catalogue. Similar risks are managed together with the main risk (e.g. credit risk). The risk catalogue is subject to discussion among all relevant Department/Units including the bank’s Management and Supervisory board.

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.4 Capital management *(continued)*

Within the internal capital adequacy assessment process the Bank has defined all requirements in accordance with the principles proscribed by Federal Banking Agency on risk management. Methodology of internal process of the Bank's capital adequacy assessement and asessment of the adequacy of the liquidy position, including assumptions used in the internal methodology, are approved by the Bank's Supervisory board. This act define methodology of stress testing for ICAAP. The stress test has to be performed once per year as minimum. Information on stress testing are as follows:

Risk	Description	Assumptions
Credit risk	Internal model with ECL rates	Reliability level 99.8%
Counterparty risk	Internal model – reiting related to probabily of raiting migration and PDs	Ratings for the banks are decreased by 2 notches
Currency risk	VaR	Reliability level 99.8%
Operating risk	Analysis of the probability of the number of events and the probability of loss per event	Reliability level 99.8%
Interest rate risk	Simplified calculations with simulation of stronger interest rate shock	Interst rate shock of 400 bp
Liquidity risk	Internal and external factors	Prolonged market stress simulation

Regulatory capital adequacy

Methods for the calculation of capital adequacy are based on the local regulation which is in line with Basel II requirement. Compliance with regulatory requirements are monitored on a regularal basis. During the reporting period, all regulatory capital requirements were met at all times. During 2020, the Bank received formal aproval from the regulator to use capital buffer.

The capital adequacy ratio of the Bank is above the prescribed limit of 12%. Following table presents the structure of equity and capital requirements of the Bank on 31 December 2020 and 31 December 2019:

In BAM '000	**31 December 2020**	**31 December 2019**
Common equity Tier 1 capital	42,253	47,697
Additional Tier 1 capital	-	-
Tier 2 capital	8,801	1,888
Total capital	**51,054**	**49,585**
Risk weighted assets (unaudited)	**352,907**	**331,493**

	31 December 2020	**31 December 2019**
Common equity Tier 1 capital	12.0%	14.4%
Tier 1 capital ratio	12.0%	14.4%
Total capital ratio	**14.5%**	**15.0%**

6. FINANCIAL RISK MANAGEMENT *(continued)*

6.4 Capital management *(continued)*

The capital ratios decreased slightly in the 2020 financial year. During the course of 2020, the CET1 ratio and T1 ratio declined to 12% due to the growth of the balance sheet. The total capital ratio fell to 14.5% as a result of growth as well as the early repayment of supplementary capital instruments. The Bank already initiated capital increase at the end of 2019 which will be effective in first half of 2021.

Within the internal capital adequacy assessment process the Bank will calculate the regulatory capital requirement for credit risk in accordance with the FBA Decision on calculation of a bank's capital (standardised approach). In addition, based on the internal model it shall calculate internal capital requirement for credit risk and compare it to the regulatory capital requirement to avoid possible credit risk underestimations due to use of the standardised approach. The Bank will also perform the credit risk stress test to avoid possible credit risk underestimations due to use the standardised approach in the crisis circumstances.

In additon, the Bank is obliged to ensure and maintan an additional leverage ratio which is not risk-based (financal leverage ratio). This is defined as the ratio of the Tier 1 capital to total weighted on- and off-balance sheet risk exposures. The minimum requirement for the leverage ratio has set at 6%. As of year-end the Bank reported leverage ratio of 6.5%.

Leverage ratio

	31 December 2020	**31 December 2019**
Tier 1 capital	42,253	47,697
Assets	649,516	574,623
Leverage ratio	**6.5%**	**8.3%**

7. FAIR VALUE OF FINANCIAL INSTRUMENTS

The following table sets out the fair values of financial instruments not measured at fair value and analyses them by the level in the fair value hierarchy into which each fair value measurement is categorised.

31 December 2020	Category	Level 1	Level 2	Level 3	Fair value	Carrying amount
Financial assets						
Cash in hand	AC	6,744	-	-	**6,744**	**6,744**
Funds held at the Central Bank of BiH	AC	-	104,143	-	**104,143**	**104,143**
Loans and receivables to banks	AC	-	24,612	-	**24,612**	**24,612**
Loans and receivables to customers	AC	-	-	458,498	**458,498**	**449,400**
Investments securities at amortized cost	AC	4,998	-	-	**4,998**	**5,001**
Other assets	AC	-	316	-	**316**	**316**
Total		**11,742**	**129,071**	**458,498**	**599,311**	**590,216**
Financial liabilities						
Liabilities to banks	AC	-	-	40,861	**40,861**	**40,957**
Liabilities to other financial institutions	AC	-	-	178,260	**178,260**	**179,747**
Liabilities to customers	AC	-	209,401	122,250	**331,651**	**330,544**
Subordinated debt	AC	-	-	10,437	**10,437**	**8,804**
Other liabilities	AC	-	-	1,837	**1,837**	**1,837**
Total		**-**	**209,401**	**353,645**	**563,046**	**561,889**

31 December 2019	Category	Level 1	Level 2	Level 3	Fair value	Carrying amount
Financial assets						
Cash in hand	AC	6,712		-	**6,712**	**6,715**
Funds held at the Central Bank of BiH	AC	-	108,676	-	**108,676**	**108,676**
Loans and receivables to banks	AC	-	19,905		**19,905**	**19,905**
Loans and receivables to customers	AC	-	-	400,650	**400,650**	**398,254**
Other assets	AC	-	-	436	**436**	**436**
Total		**6,712**	**128,581**	**401,086**	**536,379**	**533,983**
Financial liabilities						
Liabilities to banks	AC	-	-	38,602	**38,602**	**39,180**
Liabilities to other financial institutions	AC	-	-	170,224	**170,224**	**169,842**
Liabilities to customers	AC	-	168,489	114,057	**282,546**	**282,167**
Subordinated debt	AC	-	-	10,646	**10,646**	**8,804**
Other liabilities	AC	-	-	2,076	**2,076**	**2,076**
Total		**-**	**168,489**	**335,605**	**504,094**	**502,069**

7. FAIR VALUE OF FINANCIAL INSTRUMENTS (*continued*)

The following table sets out the fair values of financial instruments not measured at fair value and analyses them by the level in the fair value hierarchy into which each fair value measurement is categorised.

31 December 2020	**Level 1**	**Level 2**	**Level 3**	**Total**
Financial assets at fair value through other comprehensive income				
Equity securities issued by non-resident legal entities	64	-	-	**64**
Total	*64*			**64**

31 December 2019	**Level 1**	**Level 2**	**Level 3**	**Total**
Financial assets at fair value through other comprehensive income				
Equity securities issued by non-resident legal entities	43	-	-	**43**
Ukupno	**43**	**-**	**43**	**43**

The Bank's fair value determination gives the highest priority to (unadjusted) quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. For short-term financial instruments carried at amortised costs, the carrying value represents a reasonable estimate of fair value.

Upon acquisition, financial instruments are measured at fair value. In principle, this is the transaction price at the time they are acquired. Depending on their respective category, financial instruments are subsequently recognised either at fair value or at (amortised) cost.

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal (or most advantageous) market between market participants at the measurement date.

The Bank applies the IFRS hierarchy to measure fair value. The hierarchy categorises the inputs used in the valuation techniques to measure fair value into three levels:

(a) Level 1 Inputs

Quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date. A market is regarded as active if market transactions with the asset or liability occur there sufficiently frequently and in sufficient volumes to ensure the ongoing availability of pricing information.

7. FAIR VALUE OF FINANCIAL INSTRUMENTS (*continued*)

(b) Level 2 Inputs

Other than quoted market prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, the valuation techniques applied are approximations of the current fair value of similar instruments and discounted cash flow analysis using observable market parameters. The Bank applies individual observable interest and exchange rates, made available predominantly by the Central bank of Bosnia and Herzegovina.

(c) Level 3 Inputs

Unobservable inputs for the asset or liability. If observable market interest rates are not available, internal rates are used as an input for a discounted cash flow model. These internal rates reflect the cost of funds, taking into account foreign currency effects and maturities as well as a risk margin, e.g. Bank's Funding interest rates. Internal rates are regularly compared to those applied for third-party transactions and are consistent with the parameters of an orderly transaction between market participants under market conditions at the measurement date.

Loans and advances to customers

The fair value of loans and advances is calculated based on discounted expected future principal and interest cash flows. Loan repayments are assumed to occur at contractual repayment dates, where applicable. The estimated fair values of loans reflect changes in credit status since the loans were made and changes in interest rates in the case of fixed rate loans. The carrying value of loans with variable interest rate approximates their fair value.

Deposits from banks, other financial institutions, customers and subordinated debt

The estimated fair value of deposits with no stated maturity, which includes non-interest-bearing deposits, is the amount repayable on demand.

The estimated fair value of fixed interest-bearing deposits and other borrowings not quoted in an active market is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

Fair value of term deposits with variable interest rate is approximately same as their carrying value at the reporting date.

Market is considered active if quoted prices are easily and regularly available from trade, dealers, brokers, industry group, cost of services from regulatory agencies, and that those prices represent actual and regular transactions on the market based on the arm's length principles.

8. INTEREST INCOME

	2020	2019
Interest revenue calculated using the effective interest rate method		
Loans and receivables		
business clients	16,043	14,009
private clients	1,427	1,188
Banks	6	16
Other interest income	162	87
	17,638	**15,300**

9. INTEREST EXPENSE

	2020	2019
Financial institutions	2,230	2,508
Private and business clients	1,410	1,634
Banks	591	619
Subordinated debt	526	525
Interest expense from lease liabilities (Note 31)	54	66
Other interest expense	307	269
	5,118	**5,621**

10. FEE AND COMMISION INCOME

	2020	2019
Major service lines		
Payment transactions	2,665	2,713
Account maintenance fee	1,756	1,796
Credit card business	237	391
Other	342	340
	5,000	5,240
Letters of credit, guarantees and unused loans	903	807
	5,903	**6,047**

11. FEE AND COMMISION EXPENSE

	2020	2019
Fee and commission expense		
Payment transactions	844	873
Credit card business	819	785
Account maintenance fee	5	13
Other	53	46
	1,721	**1,717**

12. NET INCOME FROM FOREIGN CURRENCY TRADING

	2020	2019
Income from foreign currency transactions	1.204	881
Net gains and losses from FX revaluation	(110)	(28)
	1.094	**853**

13. OTHER OPERATING INCOME

	2020	2019
Gain from release of accrued expenses	372	-
Rent income from investment properties	143	85
Gain from sale of repossessed assets	61	380
Income from litigation settlements	23	75
Income from sale of property and equipment	3	5
Other income	200	152
	802	**697**

14. ADMINISTRATIVE EXPENSES

	2020	2019
IT expenses	2,758	3,385
Advisory services	1,162	1,081
Other taxes and contributions	560*	88
Recruitment and education	404	544
Security services	323	342
Legal and court fees	257	211
Utility and electricity expenses	245	239
Maintenance of fixed assets and equipment	241	189
Post and telecommunications	200	188
Promotion and marketing	190	232
Audit fees	136	108
Lease expenses	123	142
Transportation expenses	121	267
Insurance	115	102
Membership fees	76	82
Office supplies	55	43
Other administrative expenses	846	813
	7,812	**8,056**

* Other taxes and contributions were increased due to the paid additional obligation according to the Decision of the FBiH Tax Authorities, and it refers to the determined obligations for the tax after deduction of foreign services. The bank filed an appeal against the Decision of the Tax Authorities, which is being considered by the second instance body.

15. PERSONNEL EXPENSES

	2020	2019
Net salaries and income taxes	2,657	2,720
Social security expenses	1,550	1,652
Change in provisions for employee benefits (Note 30)	47	7
Social security refund	(42)	(21)
Other employee expenses	643	631
Post-employment benefits	-	157
	4,855	**5,146**

16. OTHER OPERATING EXPENSES

	2020	2019
Impairment of repossessed assets	774	578
Deposit and loan insurance expenses	575	538
Provisions for court cases (Note 30)	348	167
Expenses from litigation settlements	114	157
Expenses for the previous period	44	71
Loss from disposal of property, plant and equipment	-	1
Other expenses	217	76
	2,072	**1,588**

17. IMPAIRMENT LOSSES, NET

The charge to income statement in respect of impairment losses is analysed as follows:

	2020	2019
Impairment of loans and receivables to customers, net (*Note 21)*	1,733	662
(Release) of impairement of other assets and receivables, net (*Note 25)*	(106)	(8)
Impairment of funds held at the Central bank of BiH, net	22	115
Impairment / (Release) from current accounts with other banks, net	4	(17)
Impairment of investment securities	5	-
Increas / (Release) of provisions from off-balance exposures, net (Note 30)	93	(60)
	1,751	**692**

18. INCOME TAX

Total income tax recognized in the income statement can be shown as follows:

	2020	2019
Current tax	-	45
Deferred tax	51	29
	51	**74**

18. INCOME TAX *(continued)*

Reconciliation of effective tax rate may be presented as follows:

	2020	2019
Profit before income tax	**558**	**(1,559)**
	-	
Income tax at a rate of 10%	56	(156)
Effects of unrecognized revenues	-	-
- effects of unrecognized expenditures – permanent difference	466	112
- use of transferred tax loss	51	29
- tax charge in Republic of Srpska*	-	45
- utilised/(Unutilised) tax losses carried forward	102	(44)
Income tax	**51**	**74**

*Income tax charged in RS is calculated separately based on specific cost allocation for expenses and income incurred in RS.

The change in deferred tax assets may be presented as follows:

	31 December 2020	31 December 2019
Balance at the beginning of period	80	109
Release of deferred tax assets	(51)	(29)
Balance at the end of the period	**29**	**80**

Deferred tax assets are recognised where it is probable that future taxable profit will be available against which the temporary differences can be utilised. The Bank does not establish deferred tax assets for losses carried forward.

Tax effect of BAM 4,555 thousand relating to tax loss of BAM 455 thousand as at 31 Decmeber 2020 can be carried forward in accordance with the filed tax report are as follows:

	31 December 2020	31 December 2019
Expire in 2020	-	11
Expire in 2021	293	671
Expire in 2022	3,818	4,452
Expire in 2023	-	-
Expire in 2024	444	444
Expire in 2025	-	-
Total	**4,555**	**5,578**

19. CASH AND CASH EQUIVALENTS AND OBLIGATORY RESERVES AT THE CENTRAL BANK OF BOSNIA AND HERZEGOVINA

	31 December 2020	31 December 2019
Cash in hand	6.744	6.712
Funds held at the Central Bank of BiH	104.342	108.791
Loss allowances for cash and central bank balances	*(199)*	*(115)*
Cash and central bank balances	**110.887**	**115.388**
Loans and receivables to banks at amortized cost	24.657	19.905
Loss allowances for current account with other banks	*(45)*	-
Obligatory reserve which does not qualify as cash and cash equivalenst	(53.297)	(47.047)
Cash and cash equivalents for the statement of cash flows	**82.202**	**88.246**

The minimum reserve requirement is calculated as a percentage of the average amount of total deposits and borrowed funds for each business day during 10 calendar days after the mandatory reserve maintenance period.

From 1 July 2016, a single rate of 10% of total short-term and long-term deposits and borrowed funds is applied. Cash held as a compulsory reserve in the CBBH account is not available for use without the special approval of CBBH and FBA.

19. CASH AND CASH EQUIVALENTS AND OBLIGATORY RESERVES AT THE CENTRAL BANK OF BOSNIA AND HERZEGOVINA (*continued*)

The changes in loss allowances for central bank balances are presented in the following table. All central bank balances are classified as Stage 1.

	2020	2019
Balance as at 31 December 2019	**(115)**	**-**
Effect of the implementation of the new FBA Decision (Note 5)	(61)	-
Impairment allowances as of 1 January 2020	**(177)**	-
Newly recognized financial assets (*Note 17*)	(33)	(115)
Derecognition *(Note 17)*	11	-
Impairment allowances as of 31 December 2020	**(199)**	**(115)**

The changes in loss allowances for current accounts with other banks are presented in the following table. All balances with other banks are classified as Stage 1.

	2020	2019
Balance as at 31 December 2019	**-**	**-**
Effect of the implementation of the new FBA Decision (Note 5)	(41)	-
Impairment allowances as of 1 January 2020	**(41)**	**(17)**
Newly recognized financial assets (*Note 17*)	(4)	-
Derecognition (*Note 17*)	-	17
Impairement allowances as of 31 December 2020	**(45)**	**-**

19. CASH AND CASH EQUIVALENTS AND OBLIGATORY RESERVES AT THE CENTRAL BANK OF BOSNIA AND HERZEGOVINA (*continued*)

Credit reitings of banks where the Bank has current accounts are as follows:

	31 December 2020	**Credit risk rating**
ProCredit Bank AG. Frankfurt am Main, Njemačka	11,122	BBB
DZ BANK AG Deutsche Zentral-Genossenschaftsbank, Frankfurt am Main, Njemačka	8,309	AA-
Raiffeisen Bank International d.d. Sarajevo, Bosna i Hercegovina	5,017	B*
UniCredit Bank d.d. Mostar, Bosna i Hercegovina	140	B*
Raiffeisen Bank International AG. Beč, Austrija	25	A-
ProCredit Bank Sh.a. Kosovo	14	BB
Zagrebačka Banka d.d. Zagreb, Hrvatska	30	BB+
Gross value	**24,657**	
Less: impairment for credit lossess	*(45)*	
Net value	**24,612**	

** Country credit rating*

	31 December 2019	**Credit risk rating**
DZ BANK AG Deutsche Zentral-Genossenschaftsbank, Frankfurt am Main, Germany	3,313	AA-
ProCredit Bank AG, Frankfurt am Main, Germany	9,449	BBB
ProCredit Bank a.d. Belgrade, Serbia	240	BBB-
ProCredit Bank (Bugarska) EAD	90	BBB-
ProCredit Bank Sh.a, Kosovo	38	BB
Raiffeisen Bank International AG, Vienna, Austria	1,634	BBB+
Zagrebačka Banka d.d. Zagreb, Croatia	60	BBB-
Raiffeisen Bank International d.d. Sarajevo, Bosnia and Herzegovina	5,004	B
UniCredit Bank d.d. Mostar, Bosnia and Herzegovina	77	B
Gross value	**19,905**	
Less: impairment	**-**	
Net value	**19,905**	

During 2020 there were no changes in credit ratings of listed banks.

20. INVESTMENT SECURITIES

During 2020, the Bank has carried out the investment in treasury bills in order to hold to maturity.

	31 December 2020	31 December 2019
Treasury bills issued by the Government of FBiH	5,006	-
Less: impairment for credit losses	(5)	
Net book value	**5,001**	**-**

	31 December 2020	31 December 2019
Balance as at 31 December 2019	-	-
Newly recognized financial assets	5,006	-
Derecognition	-	-
Gross value as at 31 December 2020	**5,006**	**-**

	31 December 2020	31 December 2019
Impairment as at 31 December 2019	**-**	**-**
Newly recognized financial assets *(Note 17)*	(5)	-
Release due to derecognition	-	-
Increase / Decrease of credit risk	-	-
Impairment as at 31 December 2020	**(5)**	**-**

21. LOANS AND RECEIVABLES TO CUSTOMERS

The analysis of loans and receivables according to the original maturity is as follows:

	31 December 2020	31 December 2019
Short-term loans:		
Short-term loans in domestic currency	86,640	70,294
Short-term loans in foreign currency (*including indexed to EUR)*	1,516	1,531
	88,156	*71,825*
Long term loans:		
Long-term loans in domestic currency	12,461	15,596
Long-term loans in foreign currency (*including indexed to EUR)*	366,682	323,862
	379,143	*339,458*
Total loans before impairment	***467,299***	***411,283***
Less: impairment	(17,899)	(13,029)
	449,400	**398,254**

Interest rates on loans and receivables to customers as at 31 December 2020 and 31 December 2019 are as follows:

	31 December 2020		31 December 2019	
	‘000 BAM	Annual interest rate	‘000 BAM	Annual interest rate
Domestic currency				
Business	98.322	2.50% - 12.50%	84,780	2.00% – 12.50%
Private	779	4.50% - 15.00%	1,110	3.50% – 15.00%
Foreign currency				
Business	347.999	2.00% - 13.00%	308,314	3.00% – 12.00%
Private	20.199	2.50% - 14.00%	17,079	1.90% – 14.00%
	467,299		***411,283***	

21. LOANS AND RECEIVABLES TO CUSTOMERS *(continued)*

All loans and receivables to customers are measured at amortized cost. The following tables show reconciliationsfrom the opening to the closing balance of the loans and advances to customers and respective loss allowances.

	Stage 1	Stage 2	Stage 3	POCI	Total
Gross amount as of 31 December 2019	356,158	39,326	15,529	270	**411,283**
Effect of the implementation of the new FBA Decision *(Note 5)*	-	-	(1,632)	-	**(1,632)**
Transition from Stage 2 to Stage 3	-	(58)	58	-	**-**
Gross amount as of 1 January 2020	**356,158**	**39,268**	**13,955**	**270**	**409,651**
New loans and receivables originated	219,120	1,085	49	-	**220,254**
Modification of cash flows	(76)	207	-	-	**131**
Derecognitions (including write-offs)	(85,426)	(6,846)	(1,614)	-	**(93,886)**
Changes in interest accrual and principal	(58,086)	(9,956)	(809)	-	**(68,851)**
Transfer from Stage 1 to Stage 2	(52,917)	52,917	-	-	**-**
Transfer from Stage 1 to Stage 3	(74)	-	74	-	**-**
Transfer from Stage 2 to Stage 1	12,642	(12,642)	-	-	**-**
Transfer from Stage 2 to Stage 3	-	(680)	680	-	**-**
Transfer from Stage 3 to Stage 2	-	82	(82)	-	**-**
Transfer from Stage 3 to Stage 1	6	-	(6)	-	**-**
Other movements	-	-	-	-	-
Gross amount as of 31 December 2020	**391,347**	**63,435**	**12,247**	**270**	

	Stage 1	Stage 2	Stage 3	POCI	Total
Impairement allowances as of 31 December 2019	(1,273)	(419)	(11,074)	(263)	**(13,029)**
Effect of the implementation of the new FBA Decision *(Note 5)*	(913)	(1,616)	(2,970)	-	**(5,499)**
Effect of the implementation of the new FBA Decision *(Note 5)*	-	-	1,632	-	**1,632**
Impairement allowances as of 1 January 2020	**(2,186)**	**(2,035)**	**(12,412)**	**(263)**	**(16,896)**
New loans and receivables originated	(1,613)	-	-	-	**(1,613)**
Release due to derecognition	458	343	359	-	**1,160**
Transfers to Stage 1	(672)	667	5	-	**-**
Transfers to Stage 2	424	(455)	31	-	**-**
Transfers to Stage 3	3	68	(71)	-	**-**
Change in credit risk	824	(1,995)	(300)	(7)	**(1,478)**
Usage of allowance	-	-	928	-	**928**
Other movements	-	-	-	-	**-**
Impairement allowances as of 31 December 2020	**(2,762)**	**(3,407)**	**(11,460)**	**(270)**	**(17,899)**

21. LOANS AND RECEIVABLES TO CUSTOMERS *(continued)*

	Stage 1	Stage 2	Stage 3	POCI	Total
Gross amount as of 1 January 2019	**355,660**	**2,791**	**21,267**	**-**	**379,718**
New loans and receivables originated	223,544	54	44	296	223,938
Modification of contractual cash flows of financial assets	-	-	40	-	40
Derecognitions (including write-offs)	(97,530)	(550)	(5,866)	(26)	(103,972)
Changes in interest accrual, principal and disbursement fee	(85,909)	(1,108)	(1,424)	-	(88,441)
Transfer from Stage 1 to Stage 2	(42,734)	42,734	-	-	-
Transfer from Stage 1 to Stage 3	-	-	-	-	-
Transfer from Stage 2 to Stage 1	3,232	(3,232)	-	-	-
Transfer from Stage 2 to Stage 3	-	(1,411)	1,411	-	-
Transfer from Stage 3 to Stage 2	-	132	(132)	-	-
Transfer from Stage 3 to Stage 1	2		(2)	-	-
Other movements	(107)	(84)	191	-	-
Gross amount as of 31 December 2019	**356,158**	**39,326**	**15,529**	**270**	**411,283**

	Stage 1	Stage 2	Stage 3	POCI	Total
Impairement allowances as of 1 January 2019	**(1,674)**	**(268)**	**(12,910)**	**-**	**(14,852)**
New loans and receivables originated	(1,264)	(5)	(17)	(263)	(1,549)
Release due to derecognition	551	73	1,629	-	2,253
Transfers to Stage 1	(250)	250	-	-	-
Transfers to Stage 2	250	(265)	15	-	-
Transfers to Stage 3	-	6	(6)	-	-
Change in credit risk	1,114	(210)	(2,646)	-	(1,742)
Usage of allowance	-	-	2,443	-	2,443
Other movements	-	-	418	-	418
Impairement allowances as of 31 December 2019	**(1,273)**	**(419)**	**(11,074)**	**(263)**	**(13,029)**

21. LOANS AND RECEIVABLES TO CUSTOMERS *(continued)*

The table below provides a reconciliation between amounts showen in the tables above reconciling opening and closing balances of impairement allowances and impairement losses line item in the statement of profit and loss.

	2020	2019
Effects of the net cost of provision recognized through movement of impairment allowance	1,931	1,038
Modification effects, net	(113)	-
Collected written-off receivables	(209)	(398)
Direct write-offs	124	22
Impairment losses, net	**1,733**	**662**

Modification of financial assets

The table below shows information on financial assets for which the contracted cash flows have changed during the reporting period.

	31 Decembar 2020	31 Decembar 2019
Stage 1		
Amortized cost before modification	113,547	-
Modification effect, net cost	(96)	-
Stage 2		
Amortized cost before modification	40,551	-
Modification effect, net income	209	-

The effects of the modification of financial assets relate to loans whose contractual terms have been modified due to the emergence of COVID-19 and the application of relevant decisions of the Banking Agency as explained in more detail in Note 6.1.1. in the “COVID-19” section. According to the adopted accounting policies, the effect of non signifficant modifications are recognized within net impairment losses.

22. INVESTMENT PROPERTY

Cost	**31 December 2020**
Balance at 1 January 2019	**-**
Additions	**-**
Transfers	**1,987**
Balance at 31 December 2019	**1,987**
Additons	**-**
Transfers	**665**
Balance at 31 December 2020	**2,652**
Accumulated depreciation	
Balance at 1 January 2019	**-**
Charge for the year	12
Transfers	294
Balance at 31 December 2019	**306**
Charge for the year	53
Transfers	119
Balance at 31 December 2020	**478**
NET BOOK VALUE	
Balance at 31 December 2019	**1,681**
Balance at 31 December 2020	**2,174**

During 2019 and 2020 the Bank leased part of it headquorter building to third party which is then recognized as investment property. The fair value of investment properties at 31 December 2019 was performed by the external appraiser (from the listo of approved apprairesers) and futher confirmed by internal appraires employed by the Bank who have appropriate qualifications and recent experience in estimating assets at fair value at relevant locations. The Bank's management believes that the carrying amount of the investment property reflects the actual, recoverable amount and no adjustment is required.

The fair value of investment property was determined using the market value method which reflects current value on the market, taking into consideration object's construction value and other factors (location, usability, quality and other factors). The fair value of investment property amounts to BAM 2.4 million.

23. PROPERTY AND EQUIPMENT

	Building and land	Equipment	Right of use assets - properties	Right of use assets - equipment other	Total properties and equipment
Cost					
At 1 January 2019	**14,236**	**7,357**	**1,981**	**326**	**23,900**
Additions	3	158	-	-	161
Disposals and write-off	(65)	(350)	(324)	-	(739)
Transfer (Note 22)	(1,987)	-	-	-	(1,987)
Balance at 31 December 2019	**12,187**	**7,165**	**1,657**	**326**	**21,335**
Accumulated depreciation at 1 January 2019	**(2,158)**	**(5,760)**	**-**	**-**	**(7,918)**
Charge for the year	(340)	(461)	(269)	(117)	(1,187)
Disposals and write-off	65	342	36		443
Transfer (Note 22)	294	-			294
Accumulated depreciation at 31 December 2019	**(2,139)**	**(5,879)**	**(233)**	**(117)**	**(8,368)**
Cost					
At 1 January 2020	**12,187**	**7,165**	**1,657**	**326**	**21,335**
Additions	41	396	-	242	679
Disposals and write-off	-	(538)	(307)	(90)	(935)
Transfer (Note 22)	(665)	-	-	-	(665)
Balance at 31 December 2020	**11,563**	**7,023**	**1,350**	**478**	**20,414**
Accumulated depreciation at 1 January 2020	**(2,137)**	**(5,880)**	**(234)**	**(117)**	**(8,368)**
Charge for the year	(298)	(512)	(253)	(122)	(1,185)
Disposals and write-off	-	528	88	90	706
Transfer (Note 22)	119	-	-	-	119
Accumulated depreciation at 31 December 2020	**(2,316)**	**(5,864)**	**(399)**	**(149)**	**(8,728)**
Net book value at 31 December 2019	**10,048**	**1,286**	**1,424**	**209**	**12,967**
Net book value at 31 December 2020	**9,247**	**1,159**	**951**	**329**	**11,686**

24. INTANGIBLE ASSETS

	Software		Licences	
Softver i licence	**2020**	**2019**	**2020**	**2019**
Balance at 1 January	1,856	1,856	5,076	5,076
Additions	-	-	58	-
Disposals and write-off	-	-	-	-
Balance at 31 December	**1,856**	**1,856**	**5,134**	**5,076**
			-	-
Accumulated depreciation at 1 January	(1,298)	(1,154)	(4,649)	(4,430)
Charge for the period	(143)	(144)	(169)	(219)
Disposals and write-off	-	-	-	-
Accumulated depreciation at 31 December	**(1,441)**	**(1,298)**	**(4,818)**	**(4,649)**
Net book value	**415**	**558**	**316**	**427**

25. OTHER ASSETS AND RECEIVABLES

	31 Decembar 2020	**31 Decembar 2019**
Repossessed assets	1,496	2,337
Short-term financial assets	386	599
Advances given	65	58
Inventory	5	2
Other assets - accruals	815	610
	2,767	**3,606**
Less. impairment	*(70)*	*(162)*
Other assets	**2,697**	**3,444**

Repossessed assets are non-financial assets acquired in the process of collection of credit claims with the aim to sell these assets as soon as the conditions are met. Assets are recognized at the lower of fair value less cost to sell or net carryng value of receivables. Depreciation is not charged on the repossessed assets. Any subsequent impairment or increases up to the initial value is recorded under other operating income/expense.

25. OTHER ASSETS AND RECEIVABLES *(continued)*

The following tables show reconciliations from the opening to the closing balance of the loss allowance for financial assets:

	Stage 1	Stage 2	Stage 3	POCI	Total
Impairement allowances as of 1 January 2019	**(1)**	**(21)**	**(140)**	-	**(162)**
Effect of the implementation of the new FBA Decision (Note 5)	*(2)*	*(6)*	*(6)*	-	*(14)*
Impairement allowances as of 1 January 2020	**(3)**	**(27)**	**(146)**	-	**(176)**
New financial assets originated	(9)	-	-	-	**(9)**
Derecognition of assets	11	55	132	-	**198**
Change in credit risk	-	(29)	(54)	-	**(83)**
Impairement allowances as of 31 December 2020.	**(1)**	**(1)**	**(68)**	-	**(70)**

	Stage 1	Stage 2	Stage 3	POCI	Total
Impairement allowances as of 1 January 2019	(2)	(6)	(162)	-	**(170)**
New financial assets originated	-	(15)	-	-	**(15)**
Release due to derecognition	-	-	26	-	**26**
Change in credit risk	1	-	(4)	-	**(3)**
Impairement allowances as of 31 December 2019	**(1)**	**(21)**	**(140)**	-	**(162)**

26. LIABILITIES TO BANKS

The analysis of liabilities to banks according to the original maturity is as follows:

	31 December 2020	31 December 2019
Long-term borrowings:		
Long-term borrowings from foreign banks and financial institutions	-	-
Less: Current portion of long-term borrowings	-	-
	-	**-**
Short-term borrowings:		
Add: Current portion of long-term borrowings	**-**	**-**
Short-term deposits:		
Short-term bank deposits with a maturity of up to three months	17,602	23,470
Short-term bank deposits with a maturity of up to one year	23,355	15,710
	40,957	**39,180**

27. LIABILITIES TO OTHER FINANCIAL INSTITUTIONS

	Remaining maturity					
31 December 2020	up to 3 months	3 - 12 months	1 - 5 years	more than 5 years	non cash relevant	**Total**
Liabilities with fixed interest rates	1,422	51,749	118,028	8,548	**-**	**179,747**
Liabilities with variable interest rates	-	-	-	-	**-**	**-**
Total	**1,422**	**51,749**	**118,028**	**8,548**	**-**	**179,747**

	Remaining maturity					
31 December 2019	up to 3 months	3 - 12 months	1 - 5 years	more than 5 years	non cash relevant	**Total**
Liabilities with fixed interest rates	2,411	28,870	122,701	15,152	**-**	**169,134**
Liabilities with variable interest rates	107	243	358	-	**-**	**708**
Total	**2,518**	**29,113**	**123,059**	**15,152**	**-**	**169,842**

28. LIABILITIES TO CUSTOMERS

	31 December 2020	31 December 2019
Current accounts:	**174,376**	**133,111**
- Private	*34,762*	*25,948*
- Business	*139,614*	*107,163*
Demand deposits:	**35,025**	**35,378**
- Private	*27,431*	*24,461*
- Business	*7,594*	*10,917*
Term deposits:	**121,143**	**113,678**
- Private	*36,261*	*43,894*
- Business	*84,882*	*69,784*
Customer deposits	**330,544**	**282,167**

29. SUBORDINATED DEBT

	31 December 2020	31 December 2019
ProCredit Holding AG	8,804	8,804
	8,804	**8,804**

There is one active borrowing from related party ProCredit Holding AG, approved on 31 August 2005, in total amount of BAM 8,804 thousand and includes only principal liability. The amendment to the subordinated debt agreement was signed on 16 December 2017. The principal will be charged interest at the rate of 6M EURIBOR + 5.88% per annum. Maturity date for this borrowing is as of 30 December 2027. The Bank was not in delay of principal or interest of this credit line nor dit it breach other provisions of subordinated debt contract. The funds of the subordinated loan are available to cover losses only in case of bankruptcy or liquidation of the Bank, and are not available for loss coverage of regular business operations of the Bank. In case of liquidation or bankruptcy of the Bank, the liabilities under the subordinated loan are subordinated to the other liabilities of the Bank.

Subject to the approval of FBA, subordinated debt may be used as additional capital for regulatory purpose. As noted in Note 2.5, The Bank has initiated a process of transferring subordinated debt to equity which is expected to be finalised in 2020.

30. PROVISIONS FOR LIABILITIES AND CHARGES

	31 December 2020	31 December 2019
Provisions for court cases	683	425
Provisions for employee benefits	251	204
Provisions for off-balance items	411	104
Other	242	85
	1,587	**818**

Gurantees and loan commitments

In the ordinary course of business, the Bank enters into credit related commitments which are recorded in off-balance sheet accounts and primarily include guarantees, letters of credit and undrawn loan commitments.

	31 December 2020	31 December 2019
Loan commitments		
Loan commitments (revocable)	13,768	10,218
Loan commitments (irrevocable)	28,055	24,785
	41,823	***35,003***
Guarantees		
Performance guarantees	26,265	27,803
Payment guarantees	13,895	14,659
Letters of credit	85	445
	40,245	***42,907***
Total gurantees and loan commitments	**82,068**	**77,910**

30. PROVISIONS FOR LIABILITIES AND CHARGES *(continued)*

Movements in provisions for liabilities and charges were as follows:

Provisions for:	1 January 2020	First application of the FBA Decision (Note 5)	Additions	Releases	Used	31 Decembar 2020
Long-term employee benefits (*Note 15*)	**204**	-	47	-	-	**251**
Provisions for court cases *(Note 15)*	**425**	-	356	(8)	(90)	**683**
Provisions for off-balance items (*Note 17*)	**104**	214	319	(226)	-	**411**
Other provisions*	**85**	-	219	-	(62)	**242**
Total	**818**	**214**	**941**	**(234)**	**(152)**	**1.587**

*The increase in other provisions mostly refers to the provision for default interest according to the Decision of the Tax Administration, on which the Bank appealed to the second instance body for decision-making.

Provisions for:	1 January 2019	Additions	Releases	Used	31 December 2019
Long-term employee benefits (*Note 15*)	**197**	7	-	-	**204**
Provisions for court cases (Note 15)	**258**	239	(72)	-	**425**
Provisions for off-balance items (*Note 17*)	**164**	8	(68)	-	**104**
Other provisions	**-**	85	-	-	**85**
Total	**619**	**339**	**(140)**	**-**	**818**

The total amount of legal proceedings is BAM 1,399 tousand (2019: BAM 1.152 thousand) which mainly relates to court procedures initiated by ex employees. The Bank creates provisions in support with its internal and external legal advisors and adjust the level of provisions based on the cirsumstances that exists at each reporting date.

If there are a number of similar obligations, the probability of outflows required to settle the obligation is determined by assuming that the same obligations are involved.

The following actuarial assumptions for 2020: were used to calculate the effects of provisions in accordance with IAS 19:

a. Demographic assumptions:

i. Average mortality rate – 0.79%

ii. Average fluctuation rate – 2.95%

b. Financial assumptions:

iii. Discount rate– 2.0% and

iv. Expected salary growth – 2.0%

31. OTHER LIABILITIES

	31 December 2020	31 December 2019
Lease liabilities	1,330	1,669
Accruals	305	817
Liabilities to legal entities	194	100
Deferred income	203	160
Liabilities to suppliers	42	77
Liabilities to governments	21	26
Other tax liabilities	2	2
Other	-	14
	2,097	**3,067**

i. Lease liabilities

Lease agreements relate to business premises in which the Bank performs its activities and equipment.

	Currency	Nominal interest rate	Agreed/ expected maturity	Present value as at 31.12.2020
Lease liability – business premises	BAM	3.65%	2020-2027	983
Lease liability - equipment	BAM	3.95%	2020-2022	115
Lease liability - equipment	BAM	1.13%	2024	200
Lease liability – bank equipment	BAM	1.13%	2023	32
				1.330

	Currency	Nominal interest rate	Agreed/ expected maturity	Present value as at 31.12.2019
Lease liability – business premises	BAM	3.65%	2020-2027	1,456
Lease liability - equipment	BAM	3.95%	2020-2022	213
				1,669

Amounts recognised in profit and loss

	2020	2019
Interest on lease liabilities *(Note 9)*	54	66
Depreciation of righ-of-use assets *(Note 23)*	375	386
Expenses relating to low value assets and short-term leases *(Note 14)*	123	142

31. OTHER LIABILITIES

Amounts presented in the statement of cash flows

	2020	2019
Total lease outflows	416	480

32. SHARE CAPITAL

Capital is made up of 7,112,649 ordinary shares at nominal value of BAM 10. Equity instruments of the Bank are not traded in a public market, but are listed at Sarajevo Stock Exchange.

The shareholding structure is as follows:

Shareholders	No. of Shares	'000 BAM	%
ProCredit Holding AG&CO. KGaA, Frankfurt, Germany	7,112,649	10	100.00
Total	**7,112,649**	**71,126,490**	**100.00**

As stated in Note 2.5, in 2019 the Bank initiated an additional recapitalization in the amount of BAM 3,900 thousand, which was not carried out due to the temporary termination of the Securities Commission. The Bank expects that the recapitalization process will be completed in 2021.

	2020	2019
Balance as of January 1	71,126	71,126
Weighted average number of regular shares outstanding	-	-
Balance as of December 31	**71,126**	**71,126**

33. BASIC EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the net profit/loss attributable to ordinary shareholders by weighted average number of ordinary shares in issue during the year.

	31 December 2020	31 December 2019
(Loss) / (Profit) attributable to ordinary shareholders (BAM '000)	507	(1,559)
Weighted average number of regular shares outstanding	7,112,649	7,112,649
	0.07	**(0.22)**

Diluted earnings per share are not presented as the Bank has not issued dilutive equity instruments.

34. SEGMENT REPORTING

The Bank is managed as one operating segment.

35. RELATED PARTY TRANSACTIONS

Balances with related parties can be summarized as follows:

	31 December 2020	31 December 2019
Assets		
ProCredit bank Germany	11,122	9,449
ProCredit Academy Germany	100	
ProCredit bank Serbia	-	240
ProCredit bank Bulgaria	-	90
ProCredit bank Kosovo	15	57
ProCredit Holding Germany	-	-
	11,237	**9,836**
Management Board	1	2
Family members of key personnel	24	98
	25	**100**
Total	**11,262**	**9,936**
Liabilities		
ProCredit Holding Germany	133,735	137,830
ProCredit bank Germany	40,957	39,180
ProCredit bank Kosovo	40	63
Quipe Germany	19	51
ProCredit bank Serbia	-	-
	174,751	177,124
Management Board	44	23
Family members of key personnel	82	92
	126	115
Total	174,877	177,239

	31 December 2020	31 December 2019
Income		
ProCredit bank Germany	2	16
	2	**16**
Management Board	-	1
Family members of key personnel	3	8
	3	**9**
Total	**5**	**25**

35. RELATED PARTY TRANSACTIONS *(continued)*

	31 December 2020	31 December 2019
Expenses		
ProCredit Holding Germany	(3,097)	(3,167)
Quipe Germany	(2,005)	(2,285)
ProCredit bank Germany	(878)	(921)
ProCredit Academy Germany	(303)	(340)
ProCredit bank Serbia	(44)	(96)
ProCredit bank Kosovo	-	(24)
Quipe Kosovo	(11)	(13)
ProCredit Academy Macedony	-	(6)
ProCredit bank Bugarska	-	-
	(6,338)	**(6,852)**
Management Board	(324)	(647)
Supervisory Board	(5)	(4)
Family members of key personnel	(802)	(840)
	(1,131)	**(1,491)**
Total	**(7,469)**	**(8,343)**

Fees to the Management and other members of the management:

The following fees were paid to the Management Board members during the period:

	31. December 2020.	31. December 2019.
Net salaries	178	357
Taxes and contributions on salaries	137	276
Other benefits	9	13
	324	**646**

36. IMPACT OF THE COVID-19 PANDEMIC ON THE BANK'S BUSINESS

Despite the outbreak of the COVID-19 pandemic in 2020, the Bank managed to achieve growth in loan portfolio with relatively smaller share of loans with approved temporary measure as prescribed by the regulator in response to COVID-19 effects (amounted to 7,7% of the total portfolio as at 31 December 2020). In order to maintain its liquidity position, the Bank managed to attract more deposit funding sources and continuously maintained compliance with all prescribed liquidity limits.

At the early stage of the COVID-19 outbreak, the Management considered the potential epidemic development, the expected impact on the Bank and the economic environment in which the Bank operates, including measures taken by the Government of Federation of Bosnia and Herzegovina. Furthermore, based on the Decision on temporary measures of banks to mitigate negative economic consequences caused by COVID-19 issued by the Federal Banking Agency, the Management of the Bank considered temporary measures that could be offered to clients and the impact of these measures on portfolio quality.

In order to protect business continuity and liquidity position of the Bank, the Management has implemented a number of measures, with particular emphasis on:

- continuous communication with the Headquarter, monitoring of the situation and regular reporting on quality status of portfolio, liquidity and equity position,
- active approach to corporate clients that are negatively affected by the outbreak of the epidemic, and who may need or require refinancing of the exposure,
- retail clients affected by the outbreak are offered solutions to mitigate their payment obligations,
- establishment of work in shift rotations and remote working for significant number of administrative and background jobs,
- adherence to the very strict standards of precaution, including social distance in customer service jobs,
- active cooperation and communication with the Agency in order to implement the requirements of the Decision,
- regular monitoring of the current and planned liquidity positions and liquidity buffers and its compliance with strict regulatory requirement,
- regular monitoring and assessment of potential effects on the financial performance, risk-weighted assets and capital of the bank using different stress based scenarios.

In accordance with the Decision on temporary measures of banks to mitigate negative economic consequences caused by "COVID-19" issued by the Agency, the Bank prepared a Program containing set of special measures that the Bank could offer to its clients negatively affected by the pandemic outbreak. In order to select the most favourable and appropriate measures for the client and the Bank, the Bank was guided by a defined level of client risk, which is mainly reflected through the industry in which the client operates and, in the case of private individuals, job loss and income reduction. The Bank granted reliefs to its clients, mainly in the form of payment moratoriums, with the aim of overcoming the difficulties they face and facilitating clients to settle their obligations to the Bank in the following period.

Even thought the Bank used general assessment for the whole economy to simulate a general shock for the loan portfolio, the Management is of the view that certain sectors have felt more severe downturn, such as transport, tourism and manufacturing, as also evidenced by the number of requests submitted for approval of temporary measures in the Bank. Currently, there is no significant concentration in any of these industries in the total portfolio.

The number of approved requests for temporary measures, as at 31 December 2020, amounts to 0.2% of the total volume of the portfolio of private individuals, and 8% of business entities, which in total gives 7.7% of the portfolio.

36. IMPACT OF THE COVID-19 PANDEMIC ON THE BANK'S BUSINESS *(continued)*

Initially the Bank estimated that the spread of COVID 19 virus infection during 2020 would have a negative impact on operating income and increase impairment losses for the same year. However, during the year, on the revenue side, the Bank realised increase in interest income (based on increase in loan portfolio with higher interest rates). Fee income slightly reduced comparing to last year end, mainly relating to period of lock down in country, with signs of improvement in the second half of the year with relaxation of restrictions. Additionally, the Bank performed continues monitoring of its loan portfolio, focusing on client with approved temporary measures and clients operating in risky industries, resulting in increased level of impairment allowance.

As reported in the note 6.4, the Bank's capital adequacy amounts to 14,5% as at 31 December 2020 which is within capital buffer as approved by the regulator (minimum capital adequacy of 12% and capital buffer of 2.5%). In August 2020 the Agency provided formal approval to the Bank for usage of capital buffer, which was requested due to situation with the State Security Commission (as explained in note 2.5) due to which the Bank is not in a position to receive and register increase in share capital that was initiated in December 2019. The Bank continues monitoring its capital adequacy on a monthly basis and its compliance with regulatory requirements.

The Bank has a stable liquidity position with recorded increase in deposit base, mainly relating to retail clients, achieved in 2020, with no significant deposit outflows caused by COVID-19 pandemic. The Bank regularly monitors liquidity indicators compliance with regulators' requirements and it does not expect significant negative impact on liquidity. As per annual liquidity plan the Bank projected additional third party borrowing in the amount of EUR 15 to be withdrawn in May 2021, for which the contract has already been signed (relates to additional funds from EIB). In case of a liquidity disruptions, the Bank has available standby line from ProCredit Holding in the amount of EUR 5m.

In management's view, the above factors support the assertion that the Bank will have sufficient resources to continue for a period of at least 12 months from the reporting date. However, the Management Board cannot exclude the possibility that a prolonged negative period of reduced economic activity, escalating and strengthening measures or the consequent negative effects of such measures on the economic environment, could have adverse effects on the Bank and its capital adequacy, financial position and operating results in the mid-term and long term. Management is closely monitoring the situation and will respond, as appropriate, with measures to mitigate the adverse effects of any events or different circumstances.