ProCredit Bank

# Annual report 2021

**Contents:** **Page**

**Management report for the year ended 31 December 2021**



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 2021 | December 31 2020 | Change |
|---|---|---|---|
| **BALANCE SHEET** | | | |
| Cash, Central bank and other financial institutions balances | 185,165 | 135,500 | 36.7% |
| Loans and advances to customers | 504,322 | 449,400 | 12.2% |
| Other assets | 19,989 | 22,640 | -11.7% |
| Liabilities to customers | 457,656 | 330,544 | 38.5% |
| Liabilities to banks and financial institutions (inc. Subdebt) | 180,898 | 229,508 | -21.2% |
| Other liabilities | 3,898 | 3,684 | 5.8% |
| Equity | 67,024 | 43,804 | 53.0% |
| **Total balance sheet – financial position** | **709,476** | **607,540** | **16.8%** |
| **STATEMENT OF PROFIT AND LOSS** | | | |
| Net Interest Income | 16,463 | 13,080 | 25.9% |
| Loss allowances | (2,882) | (1,751) | 64.6% |
| Net fee and commission income | 4,283 | 3,622 | 18.2% |
| Operating income | 23,552 | 18,598 | 26.6% |
| Operating expenses | (17,619) | (16,289) | 8.2% |
| Profit/(loss) for the period | **2,677** | **507** | **428%** |
| **KEY INDICATORS** | | | |
| Return of average equity (RoAE) | 4.8% | 1.1% | |
| Cost Income Ratio | 82% | 90.2% | 8 pp |
| Deposit to loan ratio | 91% | 73.6% | 14 pp |
| **CAPITAL RATIOS** | | | |
| RWA – Risk Weighted Assets | 373,820 | 352,907 | 5.9% |
| CAR - Capital Adequacy Ratio | 17.1% | 14.5% | 2.6 pp |
| **OPERATIONS** | | | |
| No. employees | 139 | 148 | -6% |
| Business units | **6** | **6** | |

# OUR MISSION

*Be the leading bank for SME*


## Financial year in brief

### STRENGHTENED MARKET POSITION

- "Housebank" concept as catalyst to support SMEs in a challenging market environment
- Strong portfolio growth of 12%
- Share of "green loans" in total loan portfolio 18%
- Deposit growth of 38%
- NPL of 2.9%
- Improved internal environmental footprint

### GUIDANCE FOR 2022

- 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 regulatory 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 Bank is based on a long-term relationship with our clients and employees as well as a conservative appetite for risks. The 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 EUR 50,000 to 3 million. 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.

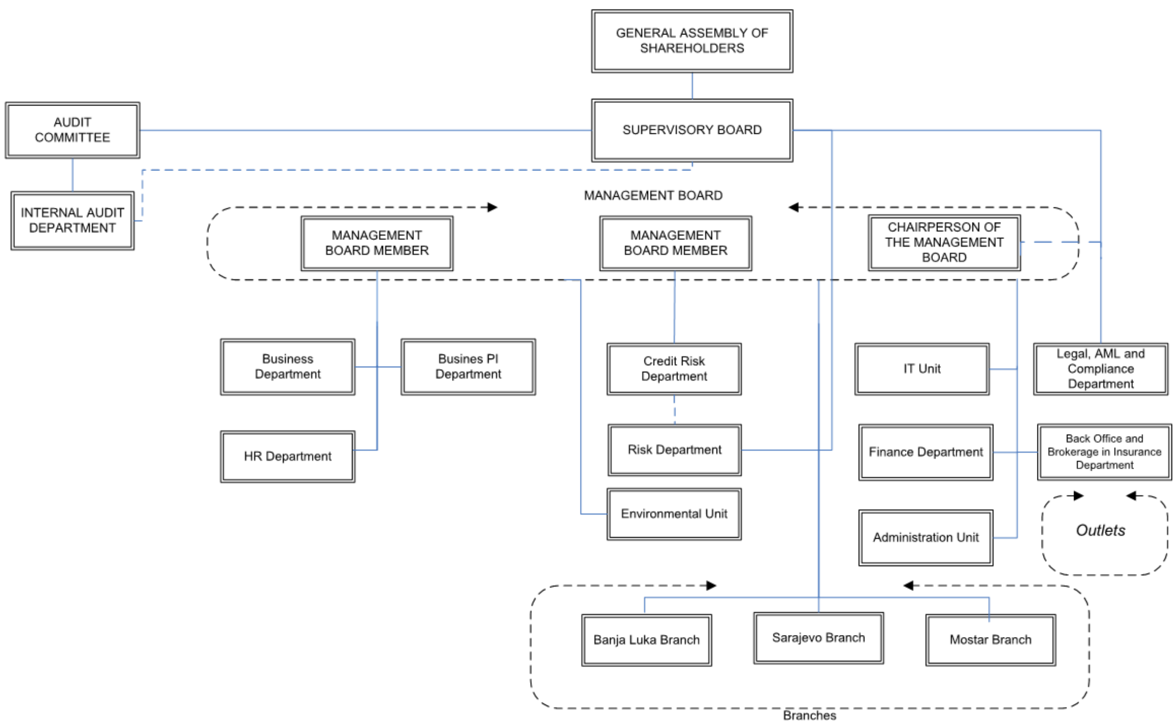
The Bank's risk strategy reflects a clearly defined business model, a high degree of diversification and careful selection and continuous training of employees. The quality and motivation of employees is one of the key factors in achieving business goals. The selection of employees is done with special 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 the remaining part is on a free quotation.

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 and the rules od corporate governance




Part of ProCredit Group's overall mission is to set standards in the financial sector in which it operates in order to make a visible impact, not only in the quality of financial services it provides, but also in business ethics and environmental issues that are fully integrated into the business model. Corporate values play a key role in this regard.

Five basic principles have been established on which the Bank's and the Group's operations are based:

a) Transparency,
b) Open communication,
c) Social responsibility and tolerance,
d) High professional standards, and
e) Personal integrity and commitment.

These principles are the basis of corporate culture and are actively applied in everyday business.

***Legal and regulatory framework of corporate governance***

Implementing the corporate governance system, the Bank moves within the regulatory framework established by the Law on Banks of the Federation of Bosnia and Herzegovina (hereinafter: the Law), the Law on Companies, decisions of the Banking Agency of the Federation of BiH and Republika Srpska (hereinafter: the Agency), as well as the applicable regulations governing the securities market.

At the same time, good corporate governance practice is based and upgraded through the implementation of experiences from the corporate governance practice of the group to which the Bank belongs. ProCredit Holding AG & Co. KGaA, as the holder of the Group, applies corporate governance in accordance with the international best banking practice and regulatory standards of Germany, taking into account the local legislation of the countries where the members of the ProCredit Group operate.

The Bank has also adopted the Corporate Governance Policy, the current version of which is from December 31, 2021.

*Shareholders and the Assembly*

The Bank has one shareholder, ProCredit Holding AG & Co.KGaA, Germany, and the powers of the Assembly are exercised by the shareholder.

During 2021 the Assembly held four sessions, three of which were held for the purpose of adopting acts necessary for the procedure of increasing capital, and amendments to the Statute in accordance with the amendments to applicable regulations.

*Supervisory Board*

The Supervisory Board consists of five members appointed and dismissed by the Bank's Assembly, of which at least two are independent in accordance with the definition of the Law on Banks and the Decision on the Internal Management System in the FBiH Banking Agency. Four members of the Bank's Supervisory Board actively know one of the languages in official use in BiH, and one of the members resides in the territory of BiH.

Members of the Supervisory Board are appointed simultaneously for a period of four years with the possibility of re-election. The current mandate of the members expires on May 31, 2023.

The Supervisory Board appoints the Audit Committee and directly performs the tasks of the Remuneration Committee, the Nomination Committee and the Risk Committee.

The Audit Committee has three members and provides professional assistance to the Supervisory Board in supervising the bank's operations and the work of the Bank's Management Board, and is directly responsible for its work to the Supervisory Board, and the members are appointed by the Supervisory Board for a period of four years, with the possibility of appointment for two consecutive terms.

*Management*

The Bank's Management Board consists of the President and two members of the Management Board, who organize, conduct business and represent the Bank. Members of the Bank's Management Board represent the Bank in legal transactions in such a way that all legally binding documents are signed by at least two members of the Bank's Management Board, so no member of the Management Board can be authorized to represent the Bank individually in the entire scope of its activities.

The Supervisory Board appoints and dismisses the Bank's Management Board and supervises its work. The mandate of the management expires on November 8, 2023. During 2021, the Management Board held a total of 41 sessions at which it discussed topics from its area of responsibility.

*Control functions*

The Bank has control functions established by the Supervisory Board in a way that is independent, ie functionally separate from business processes and activities in which risk arises, ie from business processes and activities which are monitored, controlled and evaluated by these control functions: risk management function, monitoring function compliance and internal audit function.

*Banking secret*

Persons who have access to data considered banking secrecy in the performance of their duties are obliged to keep such data and may not use it for their personal benefit or communicate it to third parties.

These persons are obliged to keep banking secrecy even after the termination of employment with the Bank, termination of their engagement with the Bank, or termination of the status on the basis of which they gained access to such data.

*Publishing data*

Once a year, the Bank publishes quantitative and qualitative data, which are important for informing the public about the financial situation and operations, and they are published and available on the Bank's website.

*Financial report*

The Bank prepares annual financial statements, which truthfully and objectively reflect its financial result and financial position in accordance with the statutory accounting requirements applicable to banks in the Federation of Bosnia and Herzegovina.

The Bank publishes the audit company's report in abbreviated form, within 15 days of its receipt, on its website and in one or more daily newspapers available throughout BiH, as well as audited annual financial statements together with its annual report within six months from the end of the business year to which they relate.

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

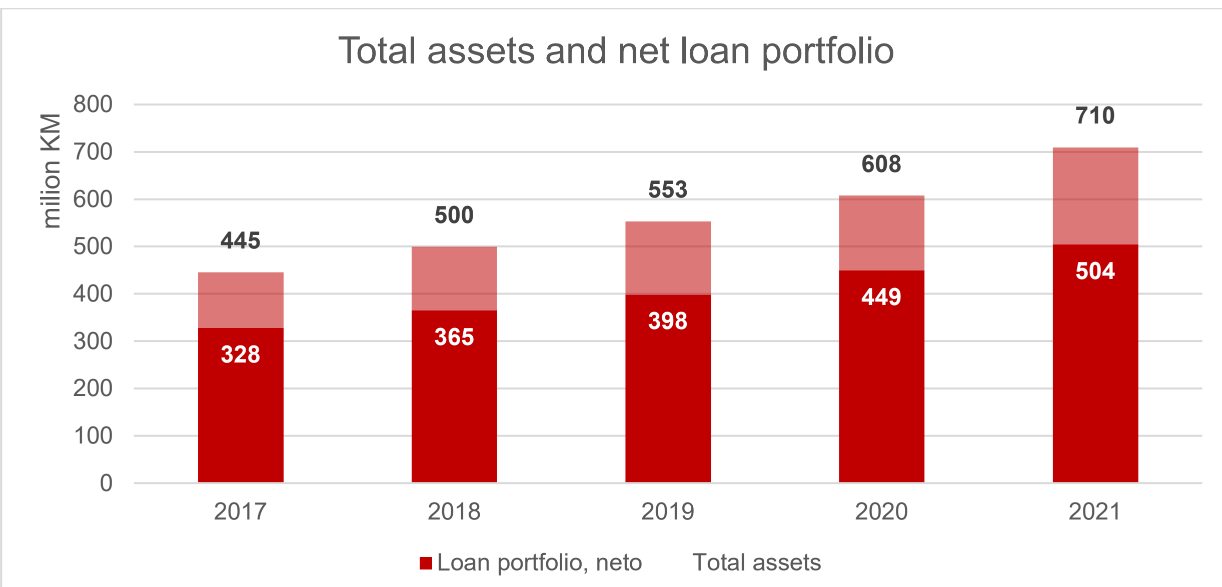
### Course of business operations

The overall business result last year was positive despite the effects on national economy of still present challenges by the COVID-19 pandemic. The total gross loan portfolio grew by 12% compared to 2020, which is one of 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 38% or about BAM 126 million. The Bank achieved a positive financial result of BAM 2,7 million, while a year earlier it achieved a result in the amount of BAM 507 thousand.

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.

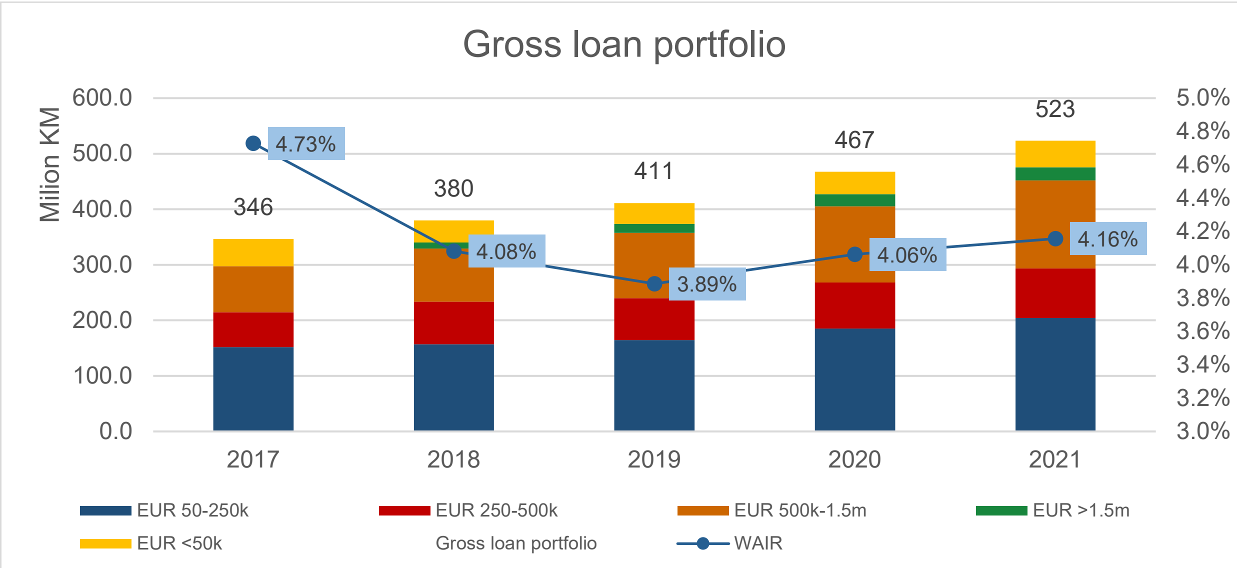
*Assets*

The total assets of the bank increased by 17%, 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, the bank holds treasury bills issued by the FBiH Government of BAM 5 million, with a maturity of 12 months. 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, at the end of 2021 most of the repossessed properties were sold and the rest was fully impaired and moved to off balance accounts. Value before impairment was BAM 120 thousand (2020: BAM 1.5 million ).




Total bank asset and net loan portfolio

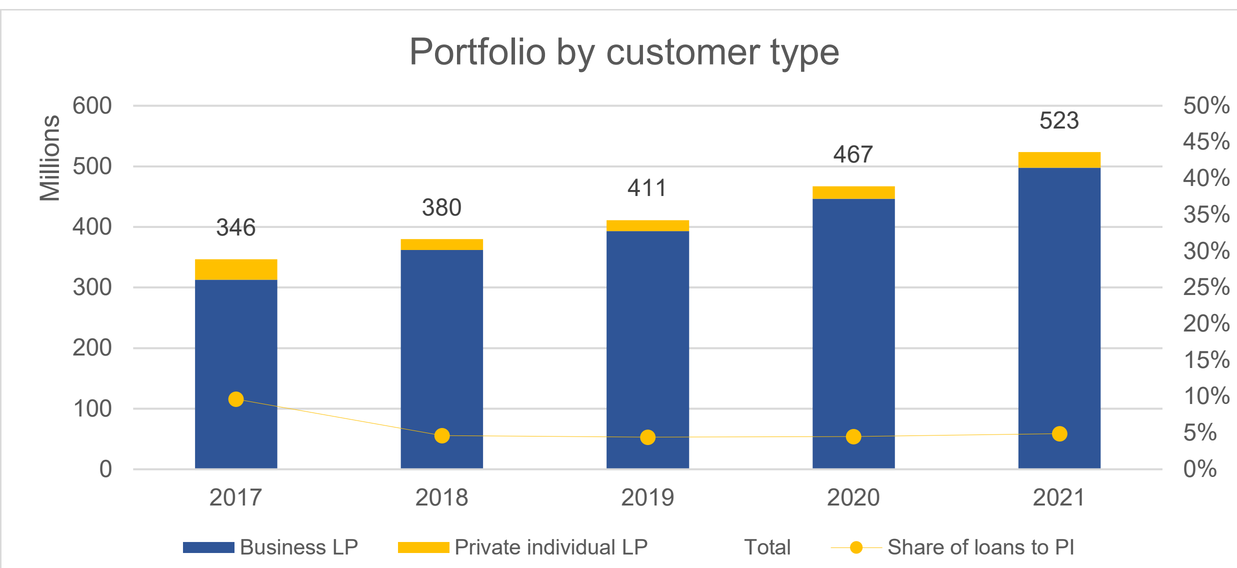
The portfolio of loans granted to clients grew by BAM 56 million or 12%, which is one of the highest growth rates on the market. The overall growth is in line with the plan defined by the bank. During a previous period that was significantly marked by the COVID-19 environment, the Bank's activities were in line with the regulator's recommendations issued at the end of 2020 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.

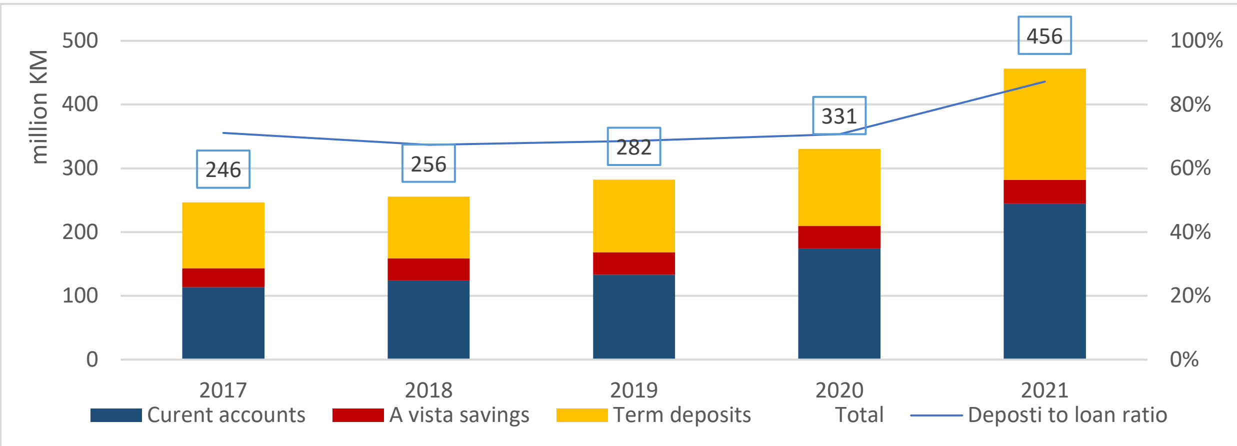
The overview below gives a breakdown of the loan portfolio by customer type. The main motive of credit activity is business with legal entities or business clients (Business).The most significant part of the loan portfolio are loans granted to legal entities with a share higher than 95%.



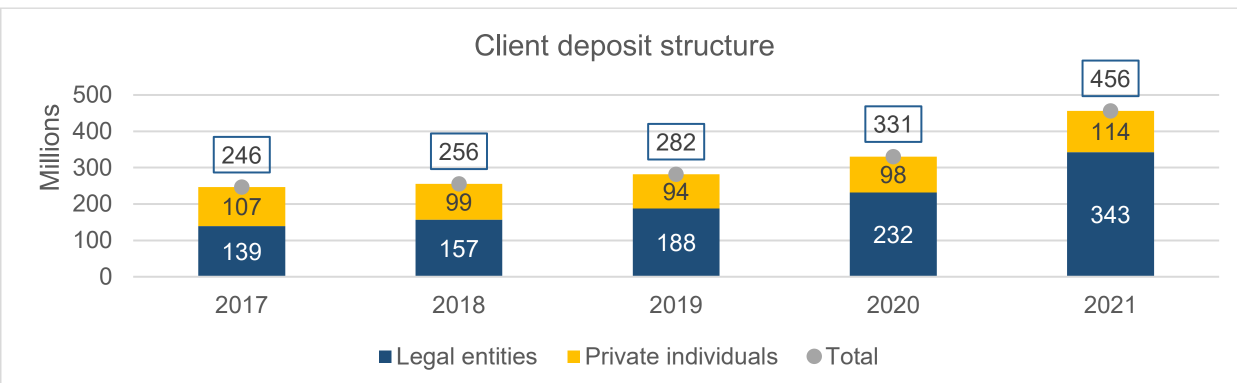

Loan portfolio, by customer type

*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 2021 they accounted for 72% (2020: 60%). The growth of deposits compared to last year was BAM 126 million or over 38%. 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 2021 to 87.2% (2020: 70.7%).




Customer deposits




Customer deposits by segments

Other sources of financing, loans taken from financial institutions have decreased compared to 2020 by 18% 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. During 2021 the bank had loans from primary financial institutions from EU (EBRD and CEB).

The Bank's equity, after a period of delay in work of the Securities Commission is managed to be increased by the Bank, based on previous arrangements. Owner of the bank payed in additional capital in the amount of BAM 12.7 million (EUR 6.5m), and in parallel subordinated debt is translated to equity in amount of BAM 8.8 milion (EUR 4.5m) .Objective of the capital increase is to strengthen market position and to support asset growth. Moreover, capital increase with further improve capital adequacy ratio.

*Operational result*

Profit for 2021 amounts to BAM 2.7 million (2020: BAM 507 thousand), which results in a slighty improved return on capital. Net interest income increased by BAM 3 million or 25% 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 2021 increased by 0.14 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, moast of which is driven by the two clients with increased credit risk, where the Bank has increased its provisions from increased risk (Level 2) to Level 3. Compared to the previous year, the costs of reserves increased by BAM 1.1 million or 56%.

The development of net fee and commission income decreased by 32% mostly by increase in client number and number of transactions. As the bank 100% transaction banking works through digital platforms, it helped durign the pandemic and was competetive advantage for client acquisition. 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 grew during 2021. Employee costs also grew slightly due to regular salary increase. Main driver for administrative costs increase are related to IT supprot projects and marceting actitivties for the better visual position of the bank. In addition, the bank promoted different ECO friendly projects and green funding to increase awareness of selfsustainable business.

The financial position of the Bank as well as the result in 2021 show the stability of business activities. Together with the capital increase gives a sound basis for stable growth and sustainable business model. The Bank complied with all obligations and regulatory 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. Impacts and effects on economy were present during 2021. Global economy was constraint by the limitation in movements of good and people. Additionally, strong inflation had significant impact especialy in second part of the year. Price increase had reflection in Bosnian market, reports from the Agency for Statistics showed increase in prices for 6.4%. Growing trends can be restrained by the recovery in supply chain and with already introduces monetary measures. Positive outlook for recovery are projected for second half of 2022[1]. However, as the 2020 was under strong COVID-19 environment, economic recovery was recorded during 2021 in most of the industries. Records on GDP growth of 8.4% are published in Q3 2021 (Agency for Statistics B&H). Recovery started in Q3 2020, with GDP growth of 3.9% compering to Q2 2020. IMF projects GDP growth for 2021 of 2.8% and 3.2% for 2022. In parallel BiH Directorate for Economic Planning projected GDP growth of 3.1% for 2022 and 3.4% in 2023.

The economic activity recovery was also reflected in foreign trade increase. Total exports at the end of 2021 increased by 36% compared to the same period last year, and imports increased by 28%. The coverage of imports by exports is at the level of over 60%. Investment activities also increased for the observed period, in December 2021, compared to December 2020, there was an increase of 7.2%, and for the whole year, investment activity increased by 10.7%. Retail activity increased by 18%.

Operations of banking sector showed signs of recovery. Customer deposits stock continued to grow during 2021 with similar rates as in pre COVID-19 (11%). Total sector loan portfolio grew 4%, which is slightly bellow what was the development in pre COVID-19. Moreover, with increase of negative rates on funds with Central bank of B&H it is to expect furher increase in credit actitivties from other banks. Profitability of the sector is on the pre COVID-19 level with expectation of sability for the whole sector.

## Expected development of the Bank

In 2021 the Bank significantly increased its total assets compering to previous year and to the market share. Significant growth, above market average, of loans to customers is achieved. For 2022 and in medium term, we plan market position improvements and to see good potential for long-term, profitable and sustainable growth. With the owner's support in capital increase the bank continue to do business and long term presence.

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.

For 2022 and in the medium term, the bank plan to achieve customer loan portfolio growth in line with historical development or around 10%. 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 2022 for 17% and 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.

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[1] [1] https://www2.deloitte.com/us/en/insights/economy/global-economic-outlook/weekly-update.html

Liabilities to banks and other financial institutions are other important source of funding for the bank. In 2022 plan is to increase borrowed funds which will follow development in customer deposits. If asset growth continue with hisotrical rate the Management considers liability increase with T2 or subordinated debt.

The Bank managed to finish capital increase in 2021 in amount of BAM 12.7 million together with subordinated debt conversion to equity in amount of BAM 8.8 million. Capital increase had positive impact on Capital Adequacy Ratio with 17.1% at the end of year (2020: 14.5%). Above mentioned possibility to take new subordinated debt in the amount of BAM 7.9 million can be used to maintain adequate capital postion. Especially, with the new SREP rquirements. The Bank receives SREP report with possible 1.25% of additional capital requirements.

For 2022, the bank expects 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 2022 is planned with the rate of 17%, 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. As previously mentioned, with the increase in negative interest rate from Central Bank expectations are that some of the banks will decrease interest rates on loans.

Fee and commission income and other incomes are planned in 2022 in a range similar to year before. Planned growth rates are between 2 to 5%. Fee expenses are planned with increase more than fee income, main driver is guarantee fee which is paid by the bank for Guarantee schemes. This schemes are used as 100% cash collateral. Other expenses are adjusted for inflatory expectations in a range of 5%. Personal expensesa re planned with the increase in a range of 5%. Increase comes from regular salary increases and with new employees. It is expected to have increase in personal costs of 5% in 2022 and with 3% in following years. 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 in similar range but bellow expenses recorded in 2021. This reflects expectations for increase of credit risk for certain industries, above all HORECA. Although, the bank for these industries already increased credit risk expectations which were reflected in financial statements in 2021.

In total the bank forecasted profit for 2022 in amount which is better than in year before. At the same time improved return on equity in following five years is planned.

With these projections and with planned capital/Tier 2 increase, capital adequacy ratios will be well above regulator's limits for the next five years.

## DISCLOSURES REQUIRED BY THE LAW ON ACCOUNTING AND AUDITING SECTION C

The previous chapters provide an overview of the development of operations in the previous year as well as planned expectations of the bank in the next period of operations. As stated, the bank operates mostly with legal entities, small and medium enterprises, which is the main business segment of the bank. In addition to providing classic financial services, the bank is actively working on the promotion and provision of direct and digital banking services. Most of the services provided to the client are done via direct and digital access where possible. The approach of developing specific products for its clients, which are in line with the business model and the digital banking model, is also active. In addition to services used through digital platforms and applications, the bank does not do special research and development.

Also, in accordance with the need to respond to the requirements of Article 42 of the Law on Accounting and Auditing, the bank did not and does not plan to repurchase its own shares. The movement and plan of capital is explained in the previous paragraphs.

In its operations, the Bank has significant exposure to credit risk, as well as liquidity risks, counterparty risk, operational, market and other risks. The bank's risk apetite and risks management is presented in detail in Note 5 "Financial risks" of the financial report on pages 49 to 81.

The Bank did not have any significant events after the balance date that could have an impact on the financial statements as of December 31, 2021. As presented in the Note 35, Management states that the conflict in Ukraine will not have any direct impact on the Bank operations, however, indirect effects cannot be ruled out such as financial market volatility, negative effects on some of the clients and simiral. The Bank has regular business transactions that are in line with the Bank's business model and do not deviate from the regular business operations.

This report should be read together with the financial report and notes to the financial statements, in order to understand the risk profile of the Bank as well as the appetites for taking and managing risks.

Amir Salkanović, President of the Management Board

ProCredit Bank d.d. Sarajevo 3

Amina Durmo Trlin, Member of the Management Board


ProCredit Bank

Financial statements 2021

## 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 04 May 2022 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

ProCredit Bank d.d. Sarajevo

**President of the Management Board**
Amir Salkanović

**Member of Management Board**
Amina Durmo Trlin

ProCredit Bank d.d. Sarajevo
Franca Lehara bb
71000 Sarajevo
Bosna i Hercegovina
04 May 2022

# 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 2021, 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 2021 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 the 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.

# 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 2021, gross loans and receivables: BAM 524 million, related impairment allowance: BAM 19 million and, for the year then ended, impairment loss recognised in the income statement: BAM 2.8 million (31 December 2020: gross loans and receivables: BAM 467 million, related impairment allowance: BAM 18 million and, for the year then ended, impairment loss recognised in the income statement: BAM 1.7 million).

Refer to Note 3 Significant accounting policies, Note 4 Critical accounting judgements and key sources of estimation uncertainty, Note 20 Loans and receivables to customers, and Note 5.1 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 and assumptions.<br><br>The Bank calculates allowances for credit losses in accordance with the requirements of the Federal Banking Agency of the Federation of Bosnia and Herzegovina (“FBA”), which combine the requirements of IFRS 9 “Financial Instruments” with the prescribed minimum requirements for provisioning.<br><br>The impairment allowances for performing exposures (Stage 1 and Stage 2 in the framework’s hierarchy) and non-performing (Stage 3) exposures not exceeding BAM 100 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”). | Our audit procedures in this area, performed, where applicable, with the assistance of our own financial risk management and information technology (IT) specialists included, among others:<br><br>• 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 identified the relevant models, assumptions and sources of data, and assessed whether such models, assumptions, data and their application are appropriate in the context of the said requirements. We also challenged the Management Board on whether the level of the methodology’s sophistication is appropriate based on an assessment of the entity-level factors;<br>• Making relevant inquiries of the Bank’s risk management and 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, assessing and testing of the Bank’s IT control environment for data security and access;<br>• Testing the design and implementation of selected controls over the loan approval, recording and monitoring, including those 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. We also tested operating effectiveness of selected controls over the loan approval and recording. |

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..

### *Key Audit Matters (continued)*

| Key audit matter | How our audit addressed the matter *(continued)* |
|---|---|
| Expected credit losses for individually significant Stage 3 (non-performing) exposures (above BAM 100 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.<br><br>In the wake of the above factors, coupled with the significantly higher estimation uncertainty stemming from the continued 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, which required our increased attention in the audit. Accordingly, we considered this area to be our key audit matter. | • For loss allowances calculated on a collective basis:<br>— Evaluating the overall ECL modelling approach, including challenging the key risk parameters (PD, EAD and LGD) used by the Bank, by reference to historical realized losses on defaults, and also considering any required adjustments to reflect expected changes in circumstances;<br>— 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, also assessing whether the information properly considers the impact of the COVID 19 global pandemic;<br>• For impairment allowances calculated individually, for a risk-based sample of loans:<br>— Taking into account debtor's business, market conditions and payment history, critically assessing, by reference to the underlying documentation (loan files) and through discussion with the loan officers and credit risk management personnel, the existence of any triggers for classification to Stage 2 or Stage 3;<br>— 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; |

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

### *Key Audit Matters (continued)*

| Key audit matter | How our audit addressed the matter *(continued)* |
|---|---|
| | • For loan exposures in totality:<br>— Assessing the adequacy of expected credit losses against the various minimum provisioning requirements prescribed by the FBA;<br>— Critically assessing the overall reasonableness of the impairment allowances, including the loans provision coverage development, and share of the gross performing and non-performing exposures in total gross exposure and the performing and non-performing loans provision coverage.<br>— 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. |

### *Other Information*

Management is responsible for the other information. The other information comprises the Management Report included in the Annual Report of the Bank, 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, except to the extent otherwise explicitly stated in our report, 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.

With respect to the Management Report, we also performed procedures required by the Law on Accounting and Auditing in Federation of Bosnia and Herzegovina ("Law on Accounting and Auditing"). Those procedures include considering whether the Management Report has been consistent with financial statements for the same financial year.

Based solely on the work required to be undertaken in the course of the audit of the financial statements and procedures above, in our opinion the information given in the Management Report for the financial year for which the financial statements are prepared, is consistent, in all material respects, with the financial statements.

In addition, in light of the knowledge and understanding of the entity and its environment obtained in the course of the audit, we are also required to report if we have identified material misstatements in the Management Report. We have nothing to report in this respect

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

### *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** *04 May 2022*

*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.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

| | *Notes* | **2021** | **2020** |
|---|---|---|---|
| Interest income calculated using the effective interest method | *7* | 20,725 | 17,476 |
| Other interest income | | 135 | 162 |
| Interest expense | *8* | (4,397) | (4,558) |
| **Net interest income** | | **16,463** | **13,080** |
| Fee and commission income | *9* | 7,068 | 5,903 |
| Fee and commission expense | *10* | (2,785) | (2,281) |
| **Net fee and commission income** | | **4,283** | **3,622** |
| Net income from foreign currency trading | *11* | 1,769 | 1,094 |
| Other operating income | *12* | 1,037 | 802 |
| **Net operating income** | | **23,552** | **18,598** |
| Administrative expenses | *13* | (9,180) | (7,870) |
| Personnel expenses | *14* | (5,181) | (4,855) |
| Depreciation and amortisation | *21, 22, 23* | (1,531) | (1,550) |
| Other operating expenses | *15* | (1,727) | (2,072) |
| **Operating expenses** | | **(17,619)** | **(16,289)** |
| **Profit before impairment losses and income tax** | | **5,933** | **2,309** |
| Impairment losses, net | *16* | (2,882) | (1,751) |
| **PROFIT BEFORE TAX** | | **3,051** | **558** |
| Income tax expense | *17* | (374) | (51) |
| **NET PROFIT FOR THE PERIOD** | | **2,677** | **507** |
| Earnings per share (BAM) | *32* | 0.36 | 0.07 |

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

| In '000 BAM | 2021 | 2020 |
|---|---|---|
| **Net profit** | **2,677** | **507** |
| **Other comprehensive income** | | |
| **Items that are or might be reclassified to profit or loss** | | |
| *Net gains and losses from changes in fair value of debt securities at fair value through other comprehensive income* | | |
| Change in fair value, net | - | - |
| Net amount transferred to the statement of profit or loss | - | - |
| **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* | | |
| Change in fair value, net | **6** | 21 |
| Total other comprehensive income fo the year | **6** | **21** |
| **Total comprehensive income for the year** | **2,683** | **528** |

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

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

| | Notes | 31 December 2021 | 31 December 2020 |
|---|---|---|---|
| **ASSETS** | | | |
| Cash in hand | 18 | 8,357 | 6,744 |
| Funds held at the Central Bank of BiH | 18 | 155,908 | 104,143 |
| Loans and receivables to banks | 18 | 20,900 | 24,612 |
| Loans and receivables to customers, net | 20 | 504,322 | 449,400 |
| Investment securities | | | |
| at fair value through other comprehensive income | 19 | 5,082 | 64 |
| at amortized cost | 19 | - | 5,001 |
| Current tax assets | | 375 | 259 |
| Investment property | 21 | 2,110 | 2,174 |
| Property and equipment | 22 | 10,787 | 11,686 |
| Intangible assets | 23 | 445 | 731 |
| Deferred tax assets | 17 | - | 29 |
| Other assets and receivables | 24 | 1,190 | 2,697 |
| **TOTAL ASSETS** | | **709,476** | **607,540** |
| **LIABILITIES** | | | |
| Liabilities to banks | 25 | 29,217 | 40,957 |
| Liabilities to financial institutions | 26 | 151,681 | 179,747 |
| Liabilities to customers | 27 | 457,656 | 330,544 |
| Subordinated debt | 28 | - | 8,804 |
| Provisions | 29 | 1,512 | 1,587 |
| Current tax liability | | 148 | - |
| Other liabilities | 30 | 2,238 | 2,097 |
| **TOTAL LIABILITIES** | | **642,454** | **563,736** |
| **EQUITY AND RESERVES** | | | |
| Share capital | 31 | 91,663 | 71,126 |
| Share premium | | 293 | 293 |
| Statutory reserves | | 228 | 228 |
| Accumulated losses | | (25,187) | (27,864) |
| Fair value reserves | | 27 | 21 |
| **TOTAL EQUITY AND RESERVES** | | **67,024** | **43,804** |
| **TOTAL LIABILITIES, EQUITY AND RESERVES** | | **709,476** | **607,540** |

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

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

| | Issued share capital | Share premium | Fair value reserves | Accumulated losses | Fair value reserve | Total |
|---|---|---|---|---|---|---|
| **Balance as at 31 December 2019** | **71,126** | **293** | **228** | **(22,542)** | **-** | **49,105** |
| First time adoption FBA Decision | - | - | - | (5,829) | | (5,829) |
| **Balance as of January 1, 2020** | **71,126** | **293** | **228** | **(28,371)** | | **43,276** |
| Net loss for the period | - | - | - | 507 | - | 507 |
| **Other comprehensive income** | | | | | | |
| *Net gains and losses from changes in fair value of equity securities at fair value through OCI* | - | - | - | - | 21 | 21 |
| **Total comprehensive income for the year** | **-** | **-** | **-** | **507** | **21** | **528** |
| **Balance as at 31 December 2020** | **71,126** | **293** | **228** | **(27,864)** | **21** | **43,804** |
| **Balance as at 1 January 2020** | **71,126** | **293** | **228** | **(27,864)** | **21** | **43,804** |
| Net profit for the year | - | - | - | 2,677 | - | 2,677 |
| **Other comprehensive income** | | | | | | |
| *Net gains and losses from change in fair value of equity securities at fair value through OCI* | - | - | - | - | *6* | ***6*** |
| **Total comprehensive income for the year** | **-** | **-** | **-** | **2,677** | **6** | **2,683** |
| **Transactions with the Bank 's shareholders** | | | | | | |
| Capital increase (Note 31) | 20,537 | - | - | - | - | 20,537 |
| **Balance as at 31 December 2021** | **91,663** | **293** | **228** | **(25,187)** | **27** | **67,024** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

| | *Notes* | **31 December 2021** | **31 December 2020** |
|---|---|---|---|
| **CASH FLOW FROM OPERATING ACTIVITIES** | | | |
| Net profit/(loss) before taxr | | 3,051 | 558 |
| *Adjustments for:* | | | |
| Depreciation and amortisation | | 1,531 | 1,550 |
| Impairment losses, net | | 2,882 | 1,751 |
| Net loss from writte off of property and equipment | | 83 | 10 |
| Net change in provisions for liabilities and charges | | 305 | 614 |
| Net (gain)/loss from sale of repossessed assets | | (341) | (61) |
| Impairement allowance for repossessed assets | | 591 | 774 |
| Net interest income | | (16,463) | (13,080) |
| | | **(8,361)** | **(7,884)** |
| *Changes in operating assets and liabilities:* | | | |
| Net change in obligatory reserves with CBBH | | (6,710) | (6,250) |
| Net change in loans and receivables to customers, before impairment | | (55,875) | (58,263) |
| Net change in other assests and receivables, before impairment | | 1,253 | 126 |
| Net change in liabilities to banks | | (11,538) | 1,760 |
| Net change in liabilities to customers | | 127,144 | 48,655 |
| Payments of provisions for liabilities and charges | | (315) | (152) |
| Net change in other liabilities | | 384 | (631) |
| Paid income tax | | (313) | (23) |
| Received interest | | 18,866 | 17,395 |
| Paid interest | | (4,736) | (5,033) |
| **NET CASH FLOW USED IN OPERATING ACTIVITIES** | | **59,799** | **(10,300)** |
| **CASH FLOW FROM INVESTING ACTIVITIES** | | | |
| Purchase of securities at amortized cost | | - | (5,006) |
| Maturity of securities at amortized cost | | 5,001 | - |
| Purchase of securities at fair value through other comprehensive income | | (5,013) | - |
| Purchase of property and equipment | | (237) | (437) |
| Purchase of intangible assets | | - | (58) |
| **NET CASH FLOW USED IN FINANCING ACTIVITIES** | | **(249)** | **(5,501)** |
| **FINANCING ACTIVITIES** | | | |
| Proceeds from liabilities to banks and other financial institutions | | 24,448 | 29,338 |
| Repayments of liabilities to banks and other financial institutions | | (61,212) | (19,219) |
| Lease liabilities paid | | (367) | (362) |
| Increase in share capital | | 20,537 | - |
| **NET CASH FLOW USED IN FINANCING ACTIVITIES** | | **(16,594)** | **9,757** |
| **NET (DECREASE) / INCREASE IN CASH AND CASH EQUIVALENTS** | | **42,956** | **(6,044)** |
| **CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD** | *18* | **82,202** | **88,246** |
| **CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD** | *18* | **125,158** | **82,202** |

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

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 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, who is also a 100% owner.

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 2021 the Bank had 139 employees (31 December 2020: 148 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 2021 and on the date of this report, the members of the Supervisory Board were:

**Supervisory Board**

| | |
|---|---|
| Gian Marco Felice | Chairman |
| Igor Anić | Deputy Chairman till 1 October 2021 |
| Vladimir Rajić | Deputy Chairman from 1 October 2021 |
| Wolfgang Bertelsmeier | Member |
| Aida Soko | Member |
| Emilija Spirovska | Member from 1 June 2021 |
| Natia Tkhilaishvili | Member till 1 June 2021 |

During 2021 and on the date of this report, the members of the Audit Committee were:

**Audit Committee**

| | |
|---|---|
| Emanuela Caushi | Chairman |
| Stevče Kuzmanovski | Member from 23 February 2021 |
| Maja Mihajlova | Member from 16 November 2021 |
| Emilija Spirovska | Member till 23 February 2021 |
| Heiko Buzin | Member from 16 November 2021 |

During 2021 and on the date of this report, the members of Management Boand were:

**Management Board**

| | |
|---|---|
| Amir Salkanović | Chairman |
| Amina Durmo - Trlin | Member |
| Srđan Ožegović | Member from 1 October 2021 |
| Vladimir Rajić | Member till 1 October 2021 |

## 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 2021 the Bank calculated an impairment for credit losses that is higher by BAM 4,668 thousand (2020. 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 1,219 thousand (2020. 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 591 thousand (2020. 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 2,846 thousand (2020. BAM 2,669 thousand), of which the amount of BAM 1,087 thousand (2020, BAM 1,152 thousand) relates to exposures not secured by acceptable collateral, and the amount of BAM 1,759 thousand (2020, 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 12 thousand (2020. BAM 6 thousand).

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

**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:

| | December 31, 2020 | December 31, 2021 |
|---|---|---|
| Assets | (5,380) | (4,449) |
| Liabilities | 291 | 219 |
| Equity | (5,671) | (4,668) |

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

These financial statements were authorizes by the Management Board as at 04 May 2022 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.

**2.5 Going concern**

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.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 2. BASIS OF PREPARATION (continued)

### 2.6. Changes in presentation of financial statements

In 2021, the Bank reviewed the statement of comprehensive income, which led to a change in the classification of fees for the use of guarantee lines from the position of interest expenses to the position of expenses on fees and commissions (Note 10). The reclassification was performed in order to more adequately reflect the nature of expenditures. This is the payment of a fee for the use of guarantee lines that the Bank uses as collateral.

In line with the above, in the profit or loss report for the year ended 31 December 2020, the Bank reclassified BAM 560 thousand from the position of interest expenses to the position fee and commission expenses, for the sake of comparability with the presentation of the current year. These changes do not affect the net profit for the period or other comprehensive income.

## 3. SIGNIFICANT 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 2020 | 31 December 2021 |
|---|---|---|
| USD | 1.59257 | 1.72563 |
| 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.

## 3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

### 3.2. Interest income and expense *(continued)*

***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.

***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.

***Presentation***

Interest income calculated using the effective interest method in the statement of profit or loss includes:

- interest on financial assets and liabilities measured at amortized cost

- interest on debt securities measured at fair value through other comprehensive income.

Other income includes default and penalty interest.

Interest expense presented in the statement of profit or loss includes interest expense on financial liabilities measured at amortized cost, and negative interest on financial assets measured at amortized cost.

**3. SIGNIFICANT ACCOUNTING POLICIES *(continued)***

### 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.<br>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.<br>Transaction-based fees for interchange, foreign currency transactions and overdrafts are charged to the customer's account when the transaction takes place.<br>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.<br>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.

### 3.4. 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. SIGNIFICANT ACCOUNTING POLICIES *(continued)***

**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 5.1.1.

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, 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.

Investment securities include debt and 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 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 5.1.1. 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, 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.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

**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.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

**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 and debt investment securities designated as at fair value through other comprehensive income.

***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 2021** | **Useful life 2020** |
|---|---|---|
| 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.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 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 2021 | Useful life 2020 |
|---|---|---|
| Intangible assets | 5-10 years | 5-10 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 2021 | Useful life 2020 |
|---|---|---|
| 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 2021. 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 5.1.1: 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 2021 and 31 December 2020 is included in the following notes.

- Note 5.1.1.: impairment of financial instruments: determining inputs into the ECL measurement model, including incorporation of forward-looking information.
- Note 5.1.1.: impairment of financial instruments: key assumptions used in estimating recoverable cash flows.

***COVID-19***

The outbreak of the COVID-19 pandemic and its impact on the global economy continued to affect the Bank's operations, namely credit risk management and the determination of loan impairment. The speed with which countries in the region can return to the level of economic activity that characterized them before COVID 19 will vary depending on the effectiveness of measures taken by governments and banking regulators, the continuing spread of infection and the ability of governments to introduce vaccines in each country. COVID-19 consequently leads to increased uncertainty, especially in relation to the measurement of expected credit losses, and continues to require increased monitoring of the model's output to take into account all pandemic impacts.

For more detailed information on the adjustment to the measurement of expected credit losses carried out by the Bank due to the aforementioned economic changes, details are explained in Note 5.1.1.

The Bank continues to monitor and assess 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 1,580 thousand (2020: BAM 1,399 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 29, the Bank provided BAM 642 thousand (2020: BAM 683 thousand), which management estimates as sufficient.

## 5. 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 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, and the main focus was on managing and maintaining the quality of the loan portfolio. 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. The Bank did not have a liquidity problem nor was there a need to use additional sources of liquidity.

The health and economic crisis continues, despite clear signs of economic recovery during 2021. Rising energy prices, bottlenecks in supply chains and rising inflation, especially in late 2021, have created additional uncertainty. The development of this situation will shape the focus of the Bank's risk management activities in 2022. The Bank will continue to monitor the situation in the country in the coming period in order to assess the potential impact on changes in credit, operational and liquidity risk and to take adequate measures.

The principles of our business strategy, explained below, represent the basis on which the risk management system is built. Consistent application of these principles reduces the risks to which the Bank is exposed.

**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.

**5. FINANCIAL RISK MANAGEMENT (*continued)***

**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..

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

**Management of individual risks**

### 5.1 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 2021 | 31 December 2020 |
|---|---|---|
| Central bank balances | 155,908 | 104,143 |
| Loans and receivables to banks | 20,900 | 24,612 |
| Investment securities | 5,082 | 5,065 |
| Loans and receivables to customers | 504,322 | 449,400 |
| Other assets | 281 | 316 |
| Contingent liabilities and commitments | 84,027 | 82,068 |
| **Total** | **770,520** | **665,604** |

#### 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.

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

#### 5.1.1. 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 made by the credit committee. Its members have approval restrictions that reflect their expertise and experience. All decisions on medium credit exposures are made by credit committees at the Bank's headquarters. If the exposures are particularly significant for the Bank due to their size, the decision is made by the Bank's Supervisory Board.

The most important basis for decision-making within the credit committee is the proposal for financing and the structure of collateral that is tailored to the needs of the client and depends on his risk profile.

The Bank’s 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.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

### 5.1.1. 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 2021 | % of total | 31 December 2020 |
|---|---|---|---|---|
| Property | 73.6% | 346,076 | 78.4% | 342,942 |
| Movable property | 0.3% | 1,483 | 8.8% | 38,278 |
| Financial guarantees | 21% | 98,854 | 11.8% | 51,545 |
| Cash deposits | 5.1% | 24,115 | 1.0% | 4,408 |
| **Total** | | **470,528** | | **437,173** |

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. Assessing the impact of the COVID-19 pandemic is currently a particular priority in this context. At the beginning of the pandemic, the Bank's focus was on providing direct support measures to affected clients and immediately assessing the potential increase in risk for certain segments of the loan portfolio. In 2021, the assessment of COVID-19-related impacts was integrated into the regular monitoring of loans. Stricter requirements have been applied in assessment, particularly for borrowers where we continue to see increased risks of pandemic-related effects on the businesses or where use was made of moratoria. In this process, consideration was given to the impact of the pandemic on the economic sector as well as the liquidity and earnings situation of the company. The greater we consider the risk to be, the more intensive the monitoring. This is reflected primarily in the frequency and the requirements of the monitoring. There is also an intensified monitoring process for new loan disbursements and their subsequent performance. As a result of intensified monitoring, risk classification downgrades were made where needed.

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

#### 5.1.1. Customer credit risk *(continued)*

The Bank offered its clients a moratorium and other special measures, the issuance of which was allowed according to the rules of the Agency until March 2022. This mainly referred to temporary measures to address short-term liquidity problems. The share of the loan portfolio with temporary measures was 8% at the end of 2020, and by the end of 2021 the Bank no longer had exposures with active measures (as shown below). In accordance with the regulatory framework, the approval of the moratorium measure or other special measures did not in itself cause reclassification of exposures to restructured exposures or reclassification of clients to a higher level of risk or default, but for all exposures the Bank regularly conducted credit risk analysis. available data on exposures and information provided by clients, assessed the probability that the client will not be able to properly meet its obligations and acclordingly performed an adequate classification into the level of risk with the corresponding impairment.

- Based on asset quality indicators, the Bank divides the loan portfolio into three levels of credit risk. categories: performing, underperforming and default. Exposures are attributed to these categories of credit risk levels based on risk classification and other risk characteristics of the obligor. Of particular importance is the classification of risks, overdue contractual payments (especially those overdue for more than 90 days), initiating bankruptcy proceedings or similar lawsuits, restructuring or liquidation of collateral by other banks, and other factors that significantly worsen the client's economic condition. Indicators provide a clear overview of the quality of the Bank's portfolio and are one of the most important tools for the credit risk management process. The level of credit risk I shows no signs of potential increase in risk. Although some exposures show signs of early warning, they do not necessarily result in increased risk.
- The level of credit risk includes exposures that show increased credit risk. This can be caused by temporary payment difficulties (30-90 days), restructuring or other factors. However, the Bank still estimates that full repayment of the exposure is possible, eg after restructuring.
  Credit risk level III includes all delayed exposures, most of which have shown long-term payment difficulties (over 90 days) or other negative factors, such as litigation. More details are described 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.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

**5. FINANCIAL RISK MANAGEMENT *(continued)***

**5.1 Credit risk *(continued)***

**5.1.1. Customer credit risk *(continued)***

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 2021 | 31 December 2020 |
|---|---|---|
| Real estate | - | 1,417 |
| Land | - | 79 |
| **Repossessed property** | **-** | **1,496** |

The Bank sold most of repossessed property, remaining stock was fully impaired and moved to off-balance records.

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.

*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.

### 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

### 5.1.1. Customer credit risk *(continued)*

- *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.

- *POCI (Purchased or Originated Credit Impaired) exposures refer to defaulted exposures; however, they are recorded separately and are differentiated from other exposures in Stage 3 in the recognition of loss allowances.*

<u>*Calculation of expected credit loss (ECL)*</u>

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.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

### 5.1.1. Customer credit risk *(continued)*

- 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.

The establishment of loss allowances for the 2021 financial year was also impacted by the COVID-19 pandemic. In anticipation of the continued increased uncertainty due to the COVID-19 pandemic, also in the longer term, appropriate adjustments have been made to the fundamental macroeconomic factors used to determine the ECL model parameters. These adjustments were based on the newest IMF World Economic Outlook Database macroeconomic forecasts, taking account for the longer-term outlook. The parameters are calculated by weighting the three scenarios (base/pessimistic/optimistic). The following table presents the macroeconomic factors used to calculate ECL parameters as of the reporting date for the banks in the group during the forecast period.

| | GDP growth in % | | |
|---|---|---|---|
| | **2021.** | **2022.** | **2023.** |
| Baseline scenario | 0.43 | 1.14 | 1.51 |
| Pessimistic scenario | -1.65 | -0.94 | -0.57 |
| Optimistic scenario | 1.89 | 2.59 | 2.97 |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

### 5.1.1. Customer credit risk *(continued)*

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.

Due to the granting of COVID-19-related moratoria on loan repayments for a certain portion of the loan portfolio, a supplementary adjustment of PD model parameters was made for 2021. The country-specific PDs are assigned to the scale for internal risk classification. This results in a breakdown of the loan portfolio into the presented PD intervals. The risk classifications are assigned according to an internal evaluation process for the current repayment capacity of the credit exposure, based on quantitative as well as qualitative factors.

| | **12-months PD range** | | **31. decembar 2021.** | | **31. decembar 2020.** |
|---|---|---|---|---|---|
| Grade 1-5: Performing | 0% - 1% | 45.28 % | 237,167 | 48.23% | 225,362 |
| | 1% - 3% | 35.84 % | 187,724 | 33.17% | 155,022 |
| | 3%- 5% | 5.80% | 30,388 | 0.00% | 128 |
| | 5% - 10% | 0.98% | 5,251 | 7.55% | 35,259 |
| Grade 6-7: Underperforming | 10% < 100% | 3.04% | 15,910 | 1.57% | 7,334 |
| Grade 8: Defaulted | 100% | 1.75% | 9,214 | 2.68% | 9,657 |
| Not graded* | - | 7.27% | 38,089 | 6.77% | 34,537 |
| **Total gross exposure** | | **100%** | **523,743** | **100%** | **467,299** |

** Unrated category includes all private individuals and legal entities with an exposure of less than BAM 100,000.*

Expected credit loss for all performing exposures (Stage 1 and 2) and individually insignifficant non performing exposures classified as Stage 3 (below BAM 100.000) are determined using the collective assessment of credit risk. Expected credit loss for individually significant Stage 3 exposures (above BAM 100.000) are determined on an individual basis (described in details below under *Definition of default*).

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

### 5.1.1. Customer credit risk *(continued)*

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 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 200% (2020.: 250%) its considered that there was a significant change in credit risk. This limit is set by the Management, based on an analysis of historical data on the risk characteristics of the loan portfolio. In 2021.SICR limit was reduced with the goal to maintain conservative approach to risk classification. 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);
- Client account is blocked over 30 days;
- Client is assessed as “watch list” due to indications of significant increase in credit risk.

A return from Stage 2 to Stage 1 occurs when no overdue payments are outstanding for more than 30 days and no other Stage 2 criteria are met. Restructuring (forbearance) is subject to an additional two-year probationary period during which no payments due may be outstanding for more than 30 days. The period begins with the restructuring of the contract.

*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,
- Loan repayment is not possible without the realisation of collateral,
- The client is assigned to risk classification 8,
- Cases of reprogramming with impaired value;
- Initiation of bankruptcy proceedings for the customer,
- Legal proceedings against the client that endanger the existence of the business or repayment capacity,
- Allegations of fraud against the customer,
- Client’s account has been blocked continuously for more than 60 days,
- Client did not settle his obligations under the guarantee for a period longer than 60 days in the case of protest of the guarantee
- POCI asset
- Other signs of impairment indicating that the client will not be able to repay in full.

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

### 5.1.1. Customer credit risk *(continued)*

*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.

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.

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.

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

#### 5.1.1. Customer credit risk *(continued)*

**Special measures under COVID-19**

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 the beginning of 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 volume of approved loans. As of December 31, 2020, 8% of loans in terms of amount were still under active measure, while as of December 31, 2021, the Bank had no credit exposures under active measure.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. UPRAVLJANJE FINANSIJSKIM RIZIKOM *(nastavak)*

### 5.1 Kreditni rizik *(nastavak)*

### 5.1.1. Kreditni rizik klijenta *(nastavak)*

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%** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

### 5.1.1. Customer credit risk *(continued)*

**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 2021** | | | | | |
| **Business loans** | | | | | |
| Gross outstanding amount | 458,096 | 25,240 | 14,687 | - | **498,023** |
| Loss allowances | (3,160) | (2,801) | (12,025) | - | **(17,986)** |
| **Carrying amount** | **454,936** | **22,439** | **2,662** | **-** | **480,037** |
| **Private loans** | | | | | |
| Gross outstanding amount | 22,680 | 2,206 | 834 | - | **25,720** |
| Loss allowances | (546) | (138) | (751) | - | **(1,435)** |
| **Carrying amount** | **22,134** | **2,068** | **83** | **-** | **24,285** |

| | 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** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

### 5.1.1. 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 2021**

| | Stage 1 | Stage 2 | Stage 3 | POCI | Total |
|---|---|---|---|---|---|
| **Loans and advances to customers** | | | | | |
| Grade 1-5 | 447,689 | 12,841 | - | - | **460,530** |
| Grade 6-7 | 4,171 | 11,739 | - | - | **15,910** |
| Grade 8 | - | - | 9,214 | - | **9,214** |
| Not graded | 29,916 | 2,866 | 6,307 | - | **38,089** |
| **Total** | **480,776** | **27,446** | **15,521** | **-** | **523,743** |
| Less: imapirment | (3,706) | (2,939) | (12,776) | - | **(19,421)** |
| **Total** | **477,070** | **24,507** | **2,745** | **-** | **504,322** |

**31 December 2021**

| | Stage 1 | Stage 2 | Stage 3 | POCI | Total |
|---|---|---|---|---|---|
| **Guarantees** | | | | | |
| Grade 1-5 | 37,404 | 1,338 | - | - | **38,742** |
| Grade 6-7 | - | 39 | - | - | **39** |
| Grade 8 | - | - | - | - | **-** |
| Not graded | 703 | 7 | - | - | **709** |
| **Total** | **38,107** | **1,384** | **-** | **-** | **39,491** |
| Less: imapirment | (82) | (29) | - | - | **(111)** |
| **Total** | **38,025** | **1,355** | **-** | **-** | **39,380** |

**31 December 2021**

| | Stage 1 | Stage 2 | Stage 3 | POCI | Total |
|---|---|---|---|---|---|
| **Loan commitments** | | | | | |
| Grade 1-5 | 40,224 | 1,210 | - | - | **41,434** |
| Grade 6-7 | - | 182 | - | - | **182** |
| Grade 8 | - | - | - | - | **-** |
| Not graded | 2,856 | 29 | - | - | **2,885** |
| **Total** | **43,080** | **1,421** | **-** | **-** | **44,501** |
| Less: imapirment | (189) | (46) | - | - | **(235)** |
| **Total** | **42,891** | **1,375** | **-** | **-** | **44,266** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

### 5.1.1. Customer credit risk *(continued)*

**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 | - | - | 9,657 | - | **9,657** |
| Not graded | 24,884 | 6,793 | 2,590 | 270 | **34,537** |
| **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** |

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 BAM 100,000.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

#### 5.1.1. 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 2021**

| | Stage 1 | Stage 2 | Stage 3 | **Total** |
|---|---|---|---|---|
| Loans and advances to customers – gross carrying amount | | | | |
| Current | 471,304 | 25,649 | 72 | **497,025** |
| Overdue < 30 days | 9,472 | 1,640 | 9 | **11,121** |
| Overdue > 30 days < 90 days | - | 157 | 840 | **997** |
| Overdue > 90 days | - | - | 14,600 | **14,600** |
| **Total:** | **480,776** | **27,446** | **15,521** | **523,743** |

**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** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

#### 5.1.1. Customer credit risk *(continued)*

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

| **31 December 2021** | | | 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 | 164.690 | 130.612 | 34.665 | 21.935 | 106.194 | 11.980 | 8.942 | 1.758 | **480.776** |
| Loss allowances for loans to customers | (1.057) | (855) | (228) | (132) | (888) | (266) | (260) | (20) | **(3.706)** |
| Net outstanding amount | 163.633 | 129.757 | 34.437 | 21.803 | 105.306 | 11.714 | 8.682 | 1.738 | **477.070** |
| **Stage 2** | | | | | | | | | |
| Gross outstanding amount | 4.403 | 6.324 | 2.149 | 300 | 12.064 | 1.641 | 565 | - | **27.446** |
| Loss allowances for loans to customers | (502) | (701) | (150) | (15) | (1.433) | (108) | (30) | - | **(2.939)** |
| Net outstanding amount | 3.901 | 5.623 | 1.999 | 285 | 10.631 | 1.533 | 535 | - | **24.507** |
| **Stage 3** | | | | | | | | | |
| Gross outstanding amount | 1.503 | 9.825 | 113 | 532 | 2.714 | 294 | 410 | 131 | **15.521** |
| Loss allowances for loans to customers | (927) | (7.884) | (111) | (496) | (2.607) | (279) | (341) | (131) | **(12.776)** |
| Net outstanding amount | 576 | 1.941 | 2 | 36 | 107 | 15 | 69 | - | **2.745** |
| **POCI** | | | | | | | | | |
| Gross outstanding amount | - | - | - | - | - | - | - | - | - |
| Loss allowances for loans to customers | - | - | - | - | - | - | - | - | - |
| Net outstanding amount | - | - | - | - | - | - | - | - | - |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

#### 5.1.1. Customer credit risk *(continued)*

| 31 December 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 | - | - | - | - | - | - | - | - | **-** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

#### 5.1.1. 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 2021** | up to EUR 50,000 | EUR 50,000 – 250,000) | over 250,000 EUR | **Total** |
|---|---|---|---|---|
| **Business loans** | | | | |
| Production | 9,199 | 59,684 | 101,713 | **170,596** |
| Trade | 11,055 | 60,470 | 75,236 | **146,761** |
| Transport and warehousing | 4,649 | 17,274 | 15,004 | **36,926** |
| Agriculture, forestry | 972 | 7,981 | 13,814 | **22,767** |
| Other business activities | 9,574 | 46,791 | 64,608 | **120,972** |
| **Total business loans** | **35,449** | **192,200** | **270,374** | **498,023** |
| **Private loans** | | | | |
| Housing loans | 4,943 | 8,155 | 817 | **13,915** |
| Investment loans and OVDs | 6,882 | 2,492 | 543 | **9,917** |
| Other | 422 | 1,466 | - | **1,888** |
| **Total private loans** | **12,247** | **12,113** | **1,360** | **25,720** |
| **Total customer loan portfolio (gross)** | **47,696** | **204,313** | **271,734** | **523,743** |

| **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** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

### 5.1.1. 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.

### 5.1.2 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.

The Bank's exposure to counterparty risk increased compared to the previous year as a result of higher liquidity reserves.

| | 31 December 2021 | in % | 31 December 2020 | in % |
|---|---|---|---|---|
| Central bank balances | 156,215 | 85.71% | 104,342 | 77.9% |
| *Loss allowances for central bank balances* | *(308)* | | *(199)* | |
| Of which obligatory reserve | 60,007 | | 53,297 | |
| Of which other balances | 96,209 | | 51,045 | |
| Current accounts with other banks (mainly ProCredit group) | 20,922 | 11.49% | 24,657 | 18.4% |
| *Loss allowances for current accounts with other banks institutions* | *(22)* | | *(45)* | |
| Investment in securities | 5,082 | 2.79% | 5,066 | 3.8% |
| *Impairment* | - | | *(5)* | |
| **Total** | **182,220** | **100.0** | **134,065** | **100.0** |

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.1 Credit risk *(continued)*

#### 5.1.1. 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 2021 and 2010, the Bank did not invest or deposit funds with other institutions.

#### 5.1.2 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).

### 5.2. 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.

#### 5.2.1. 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.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### *5.2. Market risks (continued)*

*5.2.1. Foreign currency risk (continued)*

| **31 December 2021** | **BAM** | **EUR*** | **USD** | **Other currencies** | **Total** |
|---|---|---|---|---|---|
| **Financial assets** | | | | | |
| Cash and cash equivalents | 5,822 | 1,975 | 558 | 2 | 8,357 |
| Obligatory reserves at the Central bank of BiH | 155,848 | 60 | - | - | 155,908 |
| Loans and advances to banks | 182 | 11,269 | 9,234 | 215 | 20,900 |
| Loans to customers | 136,245 | | | | |
| *of which indexed to EUR** | - | 368,077 | - | - | 504,322 |
| | | *368,077* | | | *368,077* |
| Investment in securities | 5,013 | 69 | - | - | 5,082 |
| Other assets | 253 | 16 | 4 | - | 273 |
| | **303,363** | **381,466** | **9,796** | **217** | **694,842** |
| **Financial liabilities** | | | | | |
| Liabilities to banks | - | 29,217 | - | - | 29,217 |
| Liabilities to financial institutions | - | 151,681 | - | - | 151,681 |
| Liabilities to customers | 285,344 | 162,156 | 10,079 | 77 | 457,656 |
| *of which indexed to EUR** | - | *12,550* | - | - | *12,550* |
| Provisions for off balance | 293 | 52 | 1 | - | 346 |
| Other liabilities | 1,454 | 404 | 3 | - | 1,861 |
| | **287,091** | **343,510** | **10,083** | **77** | **640,761** |
| *Net position* | ***16,272*** | ***37,956*** | ***(287)*** | ***140*** | ***54,081*** |

* 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.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### *5.2. Market risks (continued)*

*5.2.1. 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*** | ***27,980*** |

* 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.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### *5.2. Market risks (continued)*

#### *5.2.2. 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.

For the purpose of reporting to the FBiH Banking Agency on interest rate risk exposure in the banking book, the bank uses a simple calculation to estimate changes in the economic value of the banking book, applying standard interest shock to banking book positions in all major currencies individually and for other currencies in total. The total net weighted position of the banking book is expressed in absolute amount and represents the change in the economic value of the bank's banking book that arose as a result of the application of the standard interest rate shock.

| | Economic Value Impact | |
|---|---|---|
| **Currency** | **31 December 2021** | **31 December 2020** |
| BAM | (2.236) | (867) |
| EUR | (4.474) | (3.497) |
| USD | - | - |
| Other currencies | (137) | (81) |
| **Total (in BAM '000)** | **(6.847)** | **(4.445)** |

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

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.3. 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 2021 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. On a monthly basis, the Bank prepares stress scenarios with potential outflows of 15%, 25%, 50% and 100% on liquidity positions in order to identify potential effects on maturity structure and compliance, and activities are undertaken to provide adequate sources to meet liquidity conditions. The Bank did not have significant outflows of customer deposits during the COVID-19 pandemic, nor were liquidity positions threatened which remained during 2021. The Bank achieved significant increase in deposits and new credi arrangements with other banks and financial institutions.

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.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.3 Liquidity risk management *(continued)*

| 31 December 2021 | 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 | **8,357** | **8,357** | 8,357 | - | - | - | - |
| Funds held at the Central Bank of BiH | **155,908** | **156,216** | 96,209 | | 60,007 | | |
| Loans and receivables to banks | **20,900** | **20,922** | 20,922 | | | | |
| Loans and receivables to customers | **504,322** | **556,434** | 21,498 | 45,586 | 146,566 | 261,014 | 81,770 |
| Investment securities | **5,082** | **5,079** | - | - | 5,010 | - | 69 |
| Other assets | **273** | **273** | 263 | - | 10 | - | - |
| **Total assets** | **694,842** | **747,281** | **147,249** | **45,586** | **211,593** | **261,014** | **81,839** |
| **Financial liabilities** | | | | | | | |
| Liabilities to banks | **29,217** | **29,298** | 5,930 | 13,741 | 9,627 | - | - |
| Liabilities to other financial institutions | **151,681** | **154,385** | 51 | 16,200 | 45,789 | 70,435 | 21,910 |
| Liabilities to customers | **457,656** | **460,271** | 287,607 | 7,753 | 112,792 | 49,284 | 2,835 |
| Subordinated debt | **-** | **-** | - | - | - | - | - |
| Other liabilities | **1,861** | **1,949** | 806 | 101 | 243 | 706 | 76 |
| **Ukupno obaveze** | **640,415** | **645,903** | **294,394** | **37,795** | **168,451** | **120,442** | **24,821** |
| **Contingent liabilities** | | | | | | | |
| Financial guarantees | **39,491** | **39,491** | 39,491 | | | | |
| Credit commitments (irrevocable loan commitments) | **26,403** | **26,403** | 26,403 | | | | |
| **Contractual liquidity surplus** | **120,321** | **167,272** | **(81,251)** | **7,791** | **43,142** | **140,572** | **57,018** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.3 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** |

Short-term liquidity risk is measured primarily by means of LCR. As of 31 December 2021, the LCR was 160% (2020: 241%), 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 2021 the largest funding source was customer deposits, with BAM 458 million (2020: BAM 331 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.

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.4 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.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.4 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 | Internal model - simple approach adapted to the specifics of the bank when calculating the modified duration and interest rate shock | Interest rate shocks based on historical changes in interest rates with a confidence level of 99.8% |
| 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, that was also used during 2021, until the finished recapitalization process started earlier. After the recapitalization in the total amount of KM 20.5 million (KM 11.7 million by direct cash payment and KM 8.8 million conversion of subordinated debt), capital adequacy was significantly strengthened.

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 2021 and 31 December 2020:

| In BAM '000 | 31 December 2021 | 31 December 2019 |
|---|---|---|
| Common equity Tier 1 capital | 63,889 | 42,253 |
| Additional Tier 1 capital | - | - |
| Tier 2 capital | - | 8,801 |
| **Total capital** | **63,889** | **51,054** |
| **Risk weighted assets (unaudited)** | **373,820** | **352,907** |

| | 31 December 2021 | 31 December 2020 |
|---|---|---|
| Common equity Tier 1 capital | 17.1% | 12.0% |
| Tier 1 capital ratio | 17.1% | 12.0% |
| **Total capital ratio** | **17.1%** | **14.5%** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 5. FINANCIAL RISK MANAGEMENT *(continued)*

### 5.4 Capital management *(continued)*

During the course of 2021, 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. At the end of year the bank managed to complete capital increase which resulted in a higher CAR and fully in line with adequacy reguirements.

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.

As part of its internal capital adequacy assessment process for counterparty risk (including issuer risk), the Bank calculates its internal capital requirement using an internal model (which includes a stress test). The Bank compares the internal capital requirement with the regulatory capital requirements in order to avoid possible underestimation of this risk due to the application of the internal model. The Bank allocates an internal capital requirement for counterparty risk at least in the amount of the regulatory capital requirement.

Within the stress scenario for operational risk, ie the calculation of the internal capital requirement required to cover operational risk, the Bank performs testing based on historical data on the number of events during one year and gross risk exposure for the last 10 years with a confidence level of 99.8%. Based on the above data, the expected amount of gross risk exposure for operational risks is estimated. The total amount of risk exposure increases by 100% under the influence of stress factors. The calculation also includes risk exposures based on contingent liabilities arising from litigation in accordance with the expert assessment of potential loss.

To calculate the stress scenario for interest rate risk, the Bank uses two approaches: the internal model of changes in the economic value of the banking book and the internal model of the impact of interest rate risk in the banking book on net interest income. A value with a greater negative effect on the bank is adopted as an internal capital requirement for interest rate risk.

For other material risks, for which the internal methodology for assessing the internal capital requirement has not been adopted, 5% of the Bank's total risk exposure multiplied by a rate of 12% is allocated as a capital requirement.

In the framework of the internal assessment of liquidity adequacy, the bank assesses liquidity risk as material. The internal effect on liquidity is calculated on the basis of internal models for short-term liquidity financing risk and long-term liquidity financing risk.

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 8.4%.

***Leverage ratio***

| | 31 December 2021 | 31 December 2020 |
|---|---|---|
| Tier 1 capital | 63,889 | 42,253 |
| Assets | 756,485 | 649,516 |
| Leverage ratio | **8.4%** | **6.5%** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 6. 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 2021 | Category | Level 1 | Level 2 | Level 3 | Fair value | Carrying amount |
|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | |
| Cash in hand | AC | - | 8,357 | - | **8,357** | **8,357** |
| Funds held at the Central Bank of BiH | AC | - | 155,908 | - | **155,908** | **155,908** |
| Loans and receivables to banks | AC | - | 20,900 | - | **20,900** | **20,900** |
| Loans and receivables to customers | AC | - | - | 504,008 | **504,008** | **504,322** |
| Other assets | AC | - | 273 | - | **273** | **273** |
| **Total** | | **-** | **185,438** | **504,008** | **689,446** | **689,760** |
| **Financial liabilities** | | | | | | |
| Liabilities to banks | AC | - | - | 29,298 | **29,298** | **29,217** |
| Liabilities to other financial institutions | AC | - | - | 154,386 | **154,386** | **151,681** |
| Liabilities to customers | AC | - | 282,694 | 175,620 | **458,313** | **457,656** |
| Subordinated debt | AC | - | - | - | **-** | **-** |
| Other liabilities | AC | - | - | 1,861 | **1,861** | **1,861** |
| **Total** | | **-** | **282,694** | **361,167** | **643,860** | **640,417** |

| 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** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 6. 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 2021 | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| **Financial assets at fair value through other comprehensive income** | | | | |
| Treasury bills issued by resident Ministry of Finance Federation of BiH | | 5,013 | - | **5,013** |
| Equity securities issued by non-resident legal entities | - | 69 | - | **69** |
| **Total** | - | **5,082** | | **5,082** |

| 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** |

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.

**6. 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.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 7. INTEREST INCOME

| | 2021 | 2020 |
|---|---|---|
| **Interest revenue calculated using the effective interest rate method** | | |
| ***Loans and receivables*** | | |
| business clients | 19,027 | 16,043 |
| private clients | 1,694 | 1,427 |
| Banks | 4 | 6 |
| **Other interest income** | 135 | 162 |
| | **20,860** | **17,638** |

## 8. INTEREST EXPENSE

| | 2021 | 2020 |
|---|---|---|
| Financial institutions | 1.613 | 1.977 |
| Private and business clients | 1.577 | 1.410 |
| Banks | 720 | 591 |
| Subordinated debt | 449 | 526 |
| Interest expense from lease liabilities (Note 30) | 38 | 54 |
| | **4.397** | **4.558** |

## 9. FEE AND COMMISION INCOME

| | 2021 | 2020 |
|---|---|---|
| **Major service lines** | | |
| Payment transactions | 3,422 | 2,665 |
| Account maintenance fee | 1,866 | 1,756 |
| Credit card business | 315 | 237 |
| Other | 566 | 342 |
| | 6,169 | 5,000 |
| Letters of credit, guarantees and unused loans | 899 | 903 |
| | **7,068** | **5,903** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 10. FEE AND COMMISION EXPENSE

| | 2021 | 2020 |
|---|---|---|
| Fee and commission expense | | |
| Payment transactions | 928 | 844 |
| Credit card business | 927 | 819 |
| Fees for received guarantees | 858 | 560 |
| Account maintenance fee | 5 | 5 |
| Other | 67 | 53 |
| | **2,785** | **2,281** |

## 11. NET INCOME FROM FOREIGN CURRENCY TRADING

| | 2021 | 2020 |
|---|---|---|
| Income from foreign currency transactions | 1,871 | 1,204 |
| Net gains and losses from FX revaluation | (102) | (110) |
| | **1,769** | **1,094** |

## 12. OTHER OPERATING INCOME

| | 2021 | 2020 |
|---|---|---|
| Gain from release of accrued expenses | 320 | 372 |
| Rent income from investment properties | 171 | 143 |
| Gain from sale of repossessed assets | 341 | 61 |
| Income from litigation settlements | 9 | 23 |
| Income from sale of property and equipment | 17 | 3 |
| Other income | 179 | 200 |
| | **1.037** | **802** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 13. ADMINISTRATIVE EXPENSES

| | 2021 | 2020 |
|---|---|---|
| IT expenses | 3,423 | 2,758 |
| Advisory services | 1,159 | 1,162 |
| Recruitment and education | 552 | 404 |
| Promotion and marketing | 485 | 190 |
| Legal and court fees | 339 | 257 |
| Security services | 324 | 323 |
| VAT, Other taxes and contributions | 307 | 58 |
| Maintenance of fixed assets and equipment | 296 | 241 |
| Utility and electricity expenses | 265 | 245 |
| Audit fees | 233 | 136 |
| Post and telecommunications | 230 | 200 |
| Withholding tax and other contributions | 220 | 560 |
| Insurance | 218 | 115 |
| Transportation expenses | 148 | 121 |
| Lease expenses | 136 | 123 |
| Membership fees | 106 | 76 |
| Office supplies | 42 | 55 |
| Other administrative expenses | 697 | 788 |
| | **9,180** | **7,812** |

## 14. PERSONNEL EXPENSES

| | 2021 | 2020 |
|---|---|---|
| Net salaries and income taxes | 2,798 | 2,657 |
| Social security expenses | 1,644 | 1,550 |
| Change in provisions for employee benefits (Note 29) | 94 | 47 |
| Redundancy payment | 31 | - |
| Social security refund | (23) | (42) |
| Other employee expenses | 637 | 643 |
| | **5,181** | **4,855** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 15. OTHER OPERATING EXPENSES

| | 2021 | 2020 |
|---|---|---|
| Deposit and loan insurance expenses | 746 | 575 |
| Impairment of repossessed assets | 591 | 774 |
| Provisions for court cases (Note 29) | 274 | 348 |
| Loss from disposal of property, plant and equipment | 76 | - |
| Expenses from litigation settlements | - | 114 |
| Expenses for the previous period | 7 | 44 |
| Other expenses | 33 | 217 |
| | **1,727** | **2,072** |

## 16. IMPAIRMENT LOSSES, NET

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

| | 2021 | 2020 |
|---|---|---|
| Impairment of loans and receivables to customers, net (*Note 20)* | 2,862 | 1,733 |
| (Release) of impairement of other assets and receivables, net (*Note 24)* | 4 | (106) |
| Impairment of funds held at the Central bank of BiH, net | 109 | 22 |
| Impairment / (Release) from current accounts with other banks, net | (23) | 4 |
| Impairment of investment securities | (5) | 5 |
| Increas / (Release) of provisions from off-balance exposures, net (Note 29) | (65) | 93 |
| | **2,882** | **1,751** |

## 17. INCOME TAX

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

| | 2021 | 2020 |
|---|---|---|
| Current tax* | 345 | - |
| Deferred tax | 29 | 51 |
| | **374** | **51** |

*For the result of 2021 the Bank had no obligation to pay income tax due to tax losses carried forward. However, the Bank calculated income tax in the amount of BAM 345 thousand for the operations in Entity of Republic of Srpska out of which BAM 197 thousand relates to underestimated amount of taxes in Republika Srpska from previous years.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

**17. INCOME TAX *(continued)***

Reconciliation of effective tax rate may be presented as follows:

| | 2021 | 2020 |
|---|---|---|
| **Profit before income tax** | **3,051** | **558** |
| Income tax at a rate of 10% | 305 | 56 |
| Effects of unrecognized revenues | - | - |
| - tax deductible expenses | 200 | 399 |
| - non-taxable income | (144) | (352) |
| Use of transferred deferred tax | 29 | 51 |
| Tax charge in the Republic of Srpska* | 148 | - |
| Underestimated amount of tax in the Republika Srpska from previous years * | 197 | - |
| Utilized tax losses carried forward | 361 | 102 |
| **Income tax** | **374** | **51** |

*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 2021 | 31 December 2020 |
|---|---|---|
| **Balance at the beginning of period** | 29 | 80 |
| Release of deferred tax assets | (29) | (51) |
| **Balance at the end of the period** | **-** | **29** |

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 940 thousand relating to tax loss of BAM 94 thousand - at 31 Decmeber 2021 can be carried forward in accordance with the filed tax report are as follows:

| | 31 December 2021 | 31 December 2020 |
|---|---|---|
| Expire in 2021 | - | 293 |
| Expire in 2022 | 496 | 3,818 |
| Expire in 2023 | - | - |
| Expire in 2024 | 444 | 444 |
| Expire in 2025 | - | - |
| **Total** | **940** | **4,555** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

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

| | 31 December 2021 | 31 December 2020 |
|---|---|---|
| Cash in hand | 8,357 | 6,744 |
| Funds held at the Central Bank of BiH | 156,216 | 104,342 |
| *Loss allowances for cash and central bank balances* | *(308)* | *(199)* |
| **Cash and central bank balances** | **164,265** | **110,887** |
| Loans and receivables to banks at amortized cost | 20,922 | 24,657 |
| *Loss allowances for current account with other banks* | *(22)* | *(45)* |
| Obligatory reserve which does not qualify as cash and cash equivalenst | (60,007) | (53,297) |
| **Cash and cash equivalents for the statement of cash flows** | **125,158** | **82,202** |

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.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

**18. 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.

| | 2021 | 2020 |
|---|---|---|
| **Balance as at 31 December** | **(199)** | **(177)** |
| Newly recognized financial assets (*Note 16*) | (109) | (33) |
| Derecognition *(Note 16)* | - | 11 |
| **Impairment allowances as of 31 December** | **(308)** | **(199)** |

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.

| | 2021 | 2019 |
|---|---|---|
| **Balance as at 31 December** | **(45)** | **(41)** |
| Newly recognized financial assets (*Note 16*) | (8) | (4) |
| Derecognition | 31 | - |
| **Impairement allowances as of 31 December** | **(22)** | **(45)** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 18. 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 2021 | Credit risk rating |
|---|---|---|
| ProCredit Bank AG. Frankfurt am Main, Njemačka | 12,862 | BBB |
| Bank im Bistum, Essen, NJemačka | 5,709 | AA- |
| DZ BANK AG Deutsche Zentral-Genossenschaftsbank, Frankfurt am Main, Njemačka | 1,962 | AA- |
| UniCredit Bank d.d. Mostar, Bosna i Hercegovina | 183 | B* |
| Zagrebačka Banka d.d. Zagreb, Hrvatska | 174 | BBB |
| Raiffeisen Bank International AG. Beč, Austrija | 23 | A- |
| ProCredit Bank Sh.a. Kosovo | 9 | BB |
| Raiffeisen Bank International d.d. Sarajevo, Bosna i Hercegovina | - | B* |
| **Gross value** | **20,922** | |
| *Less: impairment for credit lossess* | *(22)* | |
| **Net value** | **20,900** | |

* *Country credit rating*

During 2021 Zagrebačka bank had increase in credit risk rating for two notches.

| | 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*

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 19. INVESTMENT SECURITIES AT AMORTISED COST

During 2020, the Bank has carried out the investment in treasury bills in order to hold to maturity, which were collected at the maturity date in 2021.

| | 31 December 2021 | 31 December 2020 |
|---|---|---|
| Treasury bills – Government FBiH | 5,006 | 5,006 |
| Derecognition - regular maturity | (5,006) | - |
| | | |
| **Gross value as at 31 December** | **-** | **5,006** |

| | 31 December 2021 | 31 December 2020 |
|---|---|---|
| **Impairment as at 31 December** | **(5)** | **-** |
| Newly recognized financial assets | - | (5) |
| Release due to derecognition (Note 17) | 5 | - |
| Increase / Decrease of credit risk | - | - |
| **Impairment as at 31 December** | **-** | **(5)** |

## 19. INVESTMENT SECURITIES AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

During 2021, the Bank made new investments in securities, which it classified at fair value through other comprehensive income. The holding of these securities is motivated solely by maintaining adequate liquidity positions.

| | 31. decembar 2021. | 31. decembar 2020. |
|---|---|---|
| Treasury bills – Government FBiH | 5,013 | - |
| | | |
| **Neto knjigovodstvena vrijednost na 31. decembar** | **5,013** | **-** |

Securities at fair value through other comprehensive income are classified in Phase 1 on 31 December 2021.

As at 31 December 2021, the Bank also held equity securities in the amount of BAM 69 thousand (BAM 64 thousand in 2020) in its securities portfolio.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 20. LOANS AND RECEIVABLES TO CUSTOMERS

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

| | 31 December 2021 | 31 December 2020 |
|---|---|---|
| Short-term loans: | | |
| Short-term loans in domestic currency | 103,802 | 86,640 |
| Short-term loans in foreign currency (*including indexed to EUR)* | 991 | 1,516 |
| | *104,793* | *88,156* |
| Long term loans: | | |
| Long-term loans in domestic currency | 36,883 | 12,461 |
| Long-term loans in foreign currency (*including indexed to EUR)* | 382,067 | 366,682 |
| | *418,950* | *379,143* |
| ***Total loans before impairment*** | ***523,743*** | ***467,299*** |
| Less: impairment | (19,421) | (17,899) |
| | **504,322** | **449,400** |

Interest rates on loans and receivables to customers as at 31 December 2021 and 31 December 2020 are as follows:

| | 31 December 2020 | | 31 December 2020 | |
|---|---|---|---|---|
| | '000 BAM | Annual interest rate | '000 BAM | Annual interest rate |
| *Domestic currency* | | | | |
| Business | 139,486 | 2.50% - 13.00% | 98.322 | 2.50% - 12.50% |
| Private | 1,198 | 4.50% - 10.00% | 779 | 4.50% - 15.00% |
| *Foreign currency* | | | | |
| Business | 358,536 | 2.20% - 12.00% | 347.999 | 2.00% - 13.00% |
| Private | 24,522 | 2.50% - 9.00% | 20.199 | 2.50% - 14.00% |
| | *523,743* | | *467,299* | |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 20. 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 1 January 2021** | **391,347** | **63,435** | **12,247** | **270** | **467,299** |
| New loans and receivables originated | 263,419 | 726 | - | - | **264,145** |
| Modification of cash flows | 116 | (79) | 18 | - | **55** |
| Derecognitions (including write-offs) | (103,113) | (11,210) | (1,666) | (270) | **(116,259)** |
| Changes in interest accrual and principal | (76,466) | (13,856) | (1,175) | - | **(91,497)** |
| Transfer from Stage 1 to Stage 2 | (36,137) | 36,137 | - | - | **-** |
| Transfer from Stage 1 to Stage 3 | (20) | - | 20 | - | **-** |
| Transfer from Stage 2 to Stage 1 | 41,572 | (41,572) | - | - | **-** |
| Transfer from Stage 2 to Stage 3 | - | (6,284) | 6,284 | - | **-** |
| Transfer from Stage 3 to Stage 2 | - | 149 | (149) | - | **-** |
| Transfer from Stage 3 to Stage 1 | 58 | - | (58) | - | **-** |
| **Gross amount as of 31 December 2021** | **480,776** | **27,446** | **15,521** | **-** | **523,743** |

| | Stage 1 | Stage 2 | Stage 3 | POCI | Total |
|---|---|---|---|---|---|
| **Impairement allowances as of 31 December 2021** | **(2,762)** | **(3,407)** | **(11,460)** | **(270)** | **(17,899)** |
| New loans and receivables originated | (2,124) | (59) | - | - | **(2,183)** |
| Release due to derecognition | 598 | 565 | 52 | - | **1,215** |
| Transfers to Stage 1 | (2,424) | 2,403 | 21 | - | **-** |
| Transfers to Stage 2 | 296 | (351) | 55 | - | **-** |
| Transfers to Stage 3 | 1 | 551 | (552) | - | **-** |
| Change in credit risk | 2,709 | (2,641) | (2,495) | - | **(2,427)** |
| Usage of allowance | - | - | 842 | 270 | **1,112** |
| Other movements | - | - | 761 | - | **761** |
| **Impairement allowances as of 31 December 2020** | **(3,706)** | **(2,939)** | **(12,776)** | **-** | **(19,421)** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 20. LOANS AND RECEIVABLES TO CUSTOMERS *(continued)*

| | 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 | - | - | (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** | **467,299** |

| | 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 | (913) | (1,616) | (2,970) | - | **(5,499)** |
| Effect of the implementation of the new FBA Decision | - | - | 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)** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 20. 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.

| | 2021 | 2020 |
|---|---|---|
| Effects of the net cost of provision recognized through movement of impairment allowance | 3,395 | 1,931 |
| Modification effects, net | (34) | (113) |
| Collected written-off receivables | (509) | (209) |
| Direct write-offs | 10 | 124 |
| **Impairment losses, net** | **2,862** | **1,733** |

**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 2021 | 31 Decembar 2020 |
|---|---|---|
| **Financial assets modified during the reporting period** | | |
| **Stage 1** | | |
| Amortized cost before modification | 788 | 113,547 |
| Modification effect, net cost | 2 | (96) |
| **Stage 2** | | |
| Amortized cost before modification | 2,157 | 40,551 |
| Modification effect, net income | (34) | 209 |
| **Stage 2** | | |
| Amortized cost before modification | 100 | - |
| Modification effect, net income | (2) | - |
| **Financial assets modified from the date of initial recognition** | | |
| Gross amount of financial assets previously modified for which the amount of impairment was changed from life expectancy to 12-month ECL | - | - |

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 5.1.1. in the "COVID-19" section. According to the adopted accounting policies, the effect of non signifficant modifications are recognized within net impairment losses.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 21. INVESTMENT PROPERTY

| Nabavna vrijednost | 31 December 2021 | 31 December 2020 |
|---|---:|---:|
| **Balance at 1 January** | **2,652** | **1,987** |
| Additions | - | - |
| Transfers | - | 665 |
| **Balance at 31 December** | **2,652** | **2,652** |
| | | |
| **Accumulated depreciation** | | |
| **Balance at 1 January** | **478** | **306** |
| Charge for the year | 64 | 53 |
| Transfers | - | 119 |
| **Balance at 31 December** | **542** | **478** |
| | | |
| **Balance at 31 December** | **2,110** | **2,174** |

The Bank leased part of it headquorter building to third party which is then recognized as investment property. Carryin value of investment property reflects its current recoverable amount. The last assessment of the fair value of investment properties was performed in April 2022 by the internal appraiser (cerfified court apprairesers) – Bank’s employee who has appropriate qualifications and recent experience in estimating assets at fair value at relevant locations – who assessted the value of the bulidng in the amount of BAM 3 million. 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 (income 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 3 million.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 22. 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 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)** |
| | | | | | |
| **Cost** | | | | | |
| **At 1 January 2021** | **11,563** | **7,023** | **1,350** | **478** | **20,414** |
| Additions | 35 | 202 | - | 128 | 365 |
| Disposals and write-off | (353) | (116) | - | - | (469) |
| Transfer | - | - | - | - | - |
| **Balance at 31 December 2021** | **11,245** | **7,109** | **1,350** | **606** | **20,310** |
| | | | | | |
| **Accumulated depreciation at 1 January 2021** | **(2,316)** | **(5,864)** | **(399)** | **(149)** | **(8,728)** |
| Charge for the year | (297) | (524) | (205) | (155) | (1,181) |
| Disposals and write-off | 278 | 108 | - | - | 386 |
| Transfer | - | - | - | - | - |
| **Accumulated depreciation at 31 December 2021** | **(2,335)** | **(6,280)** | **(604)** | **(304)** | **(9,523)** |
| **Net book value at 31 December 2020** | **9,247** | **1,159** | **951** | **329** | **11,686** |
| **Net book value at 31 December 2021** | **8,910** | **829** | **746** | **302** | **10,787** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 23. INTANGIBLE ASSETS

| | Software | | Licences | |
|---|---|---|---|---|
| **Softver i licence** | **2021** | **2020** | **2021** | **2020** |
| Balance at 1 January | 1,856 | 1,856 | 5,134 | 5,076 |
| Additions | - | - | - | 58 |
| Disposals and write-off | (452) | - | (4.144) | - |
| **Balance at 31 December** | **1,404** | **1,856** | **990** | **5,134** |
| | | | - | - |
| Accumulated depreciation at 1 January | (1,441) | (1,298) | (4,818) | (4,649) |
| Charge for the period | (141) | (143) | (145) | (169) |
| Disposals and write-off | 452 | - | 4.144 | - |
| **Accumulated depreciation at 31 December** | **(1,130)** | **(1,441)** | **(819)** | **(4,818)** |
| **Net book value** | **274** | **415** | **171** | **316** |

## 24. OTHER ASSETS AND RECEIVABLES

| | **31 Decembar 2021** | **31 Decembar 2020** |
|---|---|---|
| Repossessed assets | - | 1,496 |
| Short-term financial assets | 347 | 386 |
| Advances given | 60 | 65 |
| Inventory | 6 | 5 |
| Other assets - accruals | 851 | 815 |
| | **1,264** | **2,767** |
| *Less. impairment* | *(75)* | *(70)* |
| **Other assets** | **1,190** | **2,697** |

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.

During 2021, the Bank sold most of the acquired assets, and the remaining real estate was reduced to the value of 0 BAM and transferred to off-balance sheet records.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

**24. 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 2021** | **(1)** | **(1)** | **(68)** | **-** | **(70)** |
| New financial assets originated | (5) | - | - | **-** | **(5)** |
| Derecognition of assets | 5 | 9 | 26 | **-** | **40** |
| Change in credit risk | - | (10) | (29) | **-** | **(39)** |
| **Impairement allowances as of 31 December 2021.** | **(1)** | **(2)** | **(71)** | - | **(74)** |

| | 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 | *(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)** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 25. LIABILITIES TO BANKS

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

| | 31 December 2021 | 31 December 2020 |
|---|---|---|
| ***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 | 19,633 | 17,602 |
| Short-term bank deposits with a maturity of up to one year | 9,584 | 23,355 |
| | **29,217** | **40,957** |

## 26. LIABILITIES TO OTHER FINANCIAL INSTITUTIONS

**Remaining maturity**

| **31 December 2021** | up to 3 months | 3 - 12 months | 1 - 5 years | more than 5 years | non cash relevant | **Total** |
|---|---|---|---|---|---|---|
| Liabilities with fixed interest rates | 15.893 | 45,521 | 68,680 | 21,587 | **-** | **151,681** |
| Liabilities with variable interest rates | - | - | - | - | **-** | **-** |
| **Total** | **15,893** | **45,521** | **68,680** | **21,587** | **-** | **151,681** |

**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** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 27. LIABILITIES TO CUSTOMERS

| | 31 December 2021 | 31 December 2020 |
|---|---|---|
| ***Current accounts:*** | **245,697** | **174,376** |
| *- Private* | *44,211* | *34,762* |
| *- Business* | *201,487* | *139,614* |
| ***Demand deposits:*** | **36,996** | **35,025** |
| *- Private* | *32,025* | *27,431* |
| *- Business* | *4,971* | *7,594* |
| ***Term deposits:*** | **174,962** | **121,143** |
| *- Private* | *37,422* | *36,261* |
| *- Business* | *137,540* | *84,882* |
| **Customer deposits** | **457,656** | **330,544** |

## 28. SUBORDINATED DEBT

| | 31 December 2021 | 31 December 2020 |
|---|---|---|
| ProCredit Holding AG | - | 8,804 |
| | **-** | **8,804** |

At the end of 2021 The Bank has finished a process of transferring subordinated debt to equity.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 29. PROVISIONS FOR LIABILITIES AND CHARGES

| | 31 December 2021 | 31 December 2020 |
|---|---|---|
| Provisions for court cases | 642 | 683 |
| Provisions for employee benefits | 345 | 251 |
| Provisions for off-balance items | 346 | 411 |
| Other | 179 | 242 |
| | **1,512** | **1,587** |

**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 2021 | 31 December 2020 |
|---|---|---|
| ***Loan commitments*** | | |
| Loan commitments (revocable) | 18,098 | 13,768 |
| Loan commitments (irrevocable) | 26,403 | 28,055 |
| | ***44,501*** | ***41,823*** |
| ***Guarantees*** | | |
| Performance guarantees | 29,579 | 26,265 |
| Payment guarantees | 9,912 | 13,895 |
| Letters of credit | 36 | 85 |
| | ***39,526*** | ***40,245*** |
| **Total gurantees and loan commitments** | **84,027** | **82,068** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

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

Movements in provisions for liabilities and charges were as follows:

| Provisions for: | 1 January 2021 | Additions | Releases | Used | 31 Decembar 2021 |
|---|---|---|---|---|---|
| Long-term employee benefits (*Note 14*) | **251** | 94 | - | - | **345** |
| Provisions for court cases *(Note 15)* | **683** | 585 | (311) | (315) | **642** |
| Provisions for off-balance items (*Note 16*) | **411** | 246 | (311) | - | **346** |
| Other provisions* | **242** | - | (63) | - | **179** |
| **Total** | **1,587** | **925** | **(685)** | **(315)** | **1,512** |

| Provisions for: | 1 January 2020 | First application of the FBA Decision (Note 5) | Additions | Releases | Used | 31 Decembar 2020 |
|---|---|---|---|---|---|---|
| Long-term employee benefits (*Note 14*) | **204** | - | 47 | - | - | **251** |
| Provisions for court cases *(Note 15)* | **425** | - | 356 | (8) | (90) | **683** |
| Provisions for off-balance items (*Note 16*) | **104** | 214 | 319 | (226) | - | **411** |
| Other provisions* | **85** | - | 219 | - | (62) | **242** |
| **Total** | **818** | **214** | **941** | **(234)** | **(152)** | **1,587** |

*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.

The total amount of legal proceedings is BAM 1,580 tousand (2020: BAM 1,399 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 2021: 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 – 3.0%

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 30. OTHER LIABILITIES

| | 31 December 2021 | 31 December 2020 |
|---|---|---|
| Lease liabilities | 1,091 | 1,330 |
| Accruals | 377 | 305 |
| Deferred income | 257 | 203 |
| Liabilities to suppliers | 185 | 42 |
| Liabilities to legal entities | 160 | 194 |
| Liabilities to governments | 21 | 21 |
| Other tax liabilities | 3 | 2 |
| Other | 144 | - |
| | **2,238** | **2,097** |

### *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 31.12.2021 |
|---|---|---|---|---|
| Lease liability – business premises | BAM | 3.65% | 2020-2027 | 784 |
| Lease liability - equipment | BAM | 3.95% | 2020-2022 | 42 |
| Lease liability - equipment | BAM | 1.13% | 2024 | 144 |
| Lease liability – bank equipment | BAM | 1.13% | 2023 | 17 |
| Lease liability –equipment | BAM | 1.13% | 2021 – 2025 | 58 |
| Lease liability – bank equipment | BAM | 1.13% | 2021 - 2024 | 46 |
| | | | | **1,091** |

| | 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** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

**30. OTHER LIABILITIES (*continued)***

***i. Lease liabilities (continued)***

***Amounts recognised in profit and loss***

| | 2021 | 2020 |
|---|---|---|
| Interest on lease liabilities *(Note 8)* | 38 | 54 |
| Depreciation of righ-of-use assets *(Note 22)* | 360 | 375 |
| Expenses relating to low value assets and short-term leases *(Note 13)* | 136 | 123 |

***Amounts presented in the statement of cash flows***

| | 2021 | 2020 |
|---|---|---|
| Total lease outflows | 405 | 416 |

**31. SHARE CAPITAL**

Capital is made up of 9,166,270 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 | 9,166,270 | 10 | 100.00 |
| **Total** | **9,166,270** | **91,662,700** | **100.00** |

At the end of 2021, the Bank completed the previously started recapitalization, and at the end of 2021, the share capital was increased in the amount of 20,537 thousand KM, of which 11,733 thousand KM by cash payment, and 8,804 thousand KM by conversion of subordinated debt into capital.

| | 2021 | 2020 |
|---|---|---|
| Balance as of January 1 | 71,126 | 71,126 |
| Newly issued shares | 20,537 | - |
| ***Balance as of December 31*** | **91,663** | **71,126** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

**32. 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 2021** | **31 December 2020** |
|---|---|---|
| (Loss) / (Profit) attributable to ordinary shareholders (BAM ‘000) | 2,667 | 507 |
| Weighted average number of regular shares outstanding | 7,389,725 | 7,112,649 |
| | **0.36** | **0.07** |

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

**33. SEGMENT REPORTING**

The Bank is managed as one operating segment.

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

## 34. RELATED PARTY TRANSACTIONS

Balances with related parties can be summarized as follows:

| | 31 December 2021 | 31 December 2020 |
|---|---|---|
| **Assets** | | |
| ProCredit bank Germany | 12,862 | 11,122 |
| ProCredit Academy Germany | - | 100 |
| ProCredit bank Serbia | - | - |
| ProCredit bank Bulgaria | - | - |
| ProCredit bank Kosovo | 16 | 15 |
| ProCredit Holding Germany | - | - |
| | **12,878** | **11,237** |
| Management Board | 6 | 1 |
| Family members of key personnel | 43 | 24 |
| | **49** | **25** |
| **Total** | **12,927** | **11,262** |
| **Liabilities** | | |
| ProCredit Holding Germany | 82,818 | 133,735 |
| ProCredit bank Germany | 29,217 | 40,957 |
| ProCredit bank Kosovo | 70 | 40 |
| Quipe Germany | 67 | 19 |
| ProCredit bank Serbia | - | - |
| | **112,172** | **174,751** |
| Management Board | 63 | 44 |
| Family members of key personnel | 76 | 82 |
| | **139** | **126** |
| **Total** | **112,311** | **174,877** |

| | 31 December 2021 | 31 December 2020 |
|---|---|---|
| **Income** | | |
| ProCredit bank Germany | 1 | 2 |
| | **1** | **2** |
| Management Board | 1 | - |
| Family members of key personnel | 2 | 3 |
| | **3** | **3** |
| **Total** | **4** | **5** |

*(all amounts are expressed in thousands of BAM, unless otherwise stated)*

### 34. RELATED PARTY TRANSACTIONS *(continued)*

| | 31 December 2021 | 31 December 2020 |
|---|---|---|
| **Expenses** | | |
| ProCredit Holding Germany | (2,844) | (3,097) |
| Quipe Germany | (2,528) | (2,005) |
| ProCredit bank Germany | (825) | (878) |
| ProCredit Academy Germany | (425) | (303) |
| ProCredit bank Serbia | (9) | (44) |
| ProCredit bank Kosovo | - | - |
| Quipe Kosovo | (43) | (11) |
| | **(6,674)** | **(6,338)** |
| Management Board | (489) | (324) |
| Supervisory Board | (4) | (5) |
| Family members of key personnel | (373) | (802) |
| | **(866)** | **(1,131)** |
| **Total** | **(7,540)** | **(7,469)** |

**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 2021 | 31. December 2020 |
|---|---|---|
| Net salaries | 272 | 178 |
| Taxes and contributions on salaries | 206 | 137 |
| Other benefits | 10 | 9 |
| | **488** | **324** |

**35. EVENTS AFTER THE REPORTING DATE - THE IMPACT OF THE CONFLICT IN UKRAINE ON THE BANK'S OPERATIONS**

The Bank is a member of the ProCredit Group, which includes a member from Ukraine, ProCredit Bank Ukraine. Apart from the ownership relation, the Bank has no direct credit exposure or financial obligations to the Bank in Ukraine or other institutions. The impact of the conflict on the Bank's operations is strictly limited to membership in the same Group.

On the other hand, the Bank's direct exposure to the risks associated with the conflict is manifested through the Bank's clients who have business relationships with customers and suppliers located in the affected areas. The bank conducted an analysis of clients' exposures to Russia, Belarus and Ukraine. There are a total of 8 clients with relations with these countries, and the bank's exposures to these clients amounts to BAM 4 million or 0.8% of the total portfolio, most of which are clients with a small share of market dependence on these countries and with good risk indicators. The Bank will continue to monitor developments that may have an impact on the operations of its clients or the Bank itself.

The effects of the conflict cannot be clearly predicted until the moment the report is issued, and the Management Board believes that the conflict will not affect the Bank's operations in the forthcoming period.