DEVELOPMENT BANK OF THE FEDERATION OF BOSNIA AND HERZEGOVINA

Financial statements for the year ended
31 December 2011 prepared in accordance with
International Financial Reporting Standards with
Independent Auditors' Report

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Responsibility for the financial statements

The Management Board is responsible for ensuring that financial statements are prepared for each financial period in accordance with International Financial Reporting Standards (IFRS), as published by the International Accounting Standards Board which give a true and fair view of the state of affairs and results of Development Bank of the Federation of Bosnia and Herzegovina ("the Bank") for that period.

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

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

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

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

Signed on behalf of the Management Board

Ramiz Džaferović
President of the Management Board

Development Bank of the Federation of Bosnia and Herzegovina
Igmanska 1
71000 Sarajevo
Bosnia and Herzegovina

8 May 2012

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Independent Auditors' Report

To the Owner of Development Bank of the Federation of Bosnia and Herzegovina

We have audited the accompanying financial statements of Development Bank of the Federation of Bosnia and Herzegovina ('the Bank'), set out on pages 4 to 38 which comprise of the balance sheet as at 31 December 2011, and the income statement, statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and 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.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of Development Bank of Federation of Bosnia and Herzegovina as of 31 December 2011, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Emphasis of matter

In accordance with Article 3 of the Law on Development Bank of the Federation of Bosnia and Herzegovina, the Government of the Federation of Bosnia and Herzegovina should have increased the capital of the Bank by by 400 million KM from the budget in equal instalments starting from 2008 to 2011. As of the date of this report the increase in capital was not done in accordance with the dynamics and amounts as stated by the Law on Development Bank of the Federation of Bosnia and Herzegovina.

Our opinion is not qualified in respect of these matters

Other Matters

The financial statements of Development Bank of Federation of Bosnia and Herzegovina for the year ended 31 December 2010 were audited by another auditor who expressed unqualified opinion on those statements on 9 March 2011.

Sead Bahtanović, director and licensed auditor

Sabina Softić, licensed auditor

Sarajevo, Bosnia and Herzegovina

8 May 2012

Income statement
for the year ended 31 December 2011
(all amounts are expressed in thousands of KM, unless otherwise stated)

	Notes	2011	2010
Interest and similar income	5	10,761	8,733
Interest expense and similar charges	6	(76)	(87)
Net interest income		**10,685**	**8,646**
Fee and commission income	7	1,455	1,529
Net fee and commission income		**1,455**	**1,529**
Other operating expenses	8	(42)	(259)
Other operating income	9	105	114
Income from operating activities		**12,203**	**10,030**
Personnel expenses	10	(5,102)	(4,916)
Depreciation expenses	17	(388)	(401)
Other administrative expenses	11	(1,550)	(1,692)
Operating expenses		**(7,040)**	**(7,009)**
LOSS BEFORE IMPAIRMENT LOSSES, PROVISIONS AND TAXATION		**5,163**	**3,021**
Impairment losses and provisions	12	303	(797)
Recoveries		320	264
NET PROFIT FOR THE YEAR		**5,786**	**2,488**

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

Statement of comprehensive income
for the year ended 31 December 2011
(all amounts are expressed in thousands of KM, unless otherwise stated)

	Notes	2011	2010
Net profit for the year		5,786	2,488
Other comprehensive income		-	-
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		**5,786**	**2,488**

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

Balance sheet
as of 31 December 2011
(all amounts are expressed in thousands of KM, unless otherwise stated)

	Notes	31 December 2011	31 December 2010
ASSETS			
Cash and balances with banks	13	61,380	70,399
Obligatory reserve with Central bank of Bosnia and Herzegovina	14	3,629	4,181
Loans to banks, net	15	1,888	3,332
Loans to customers, net	16	204,306	166,664
Other assets, net		211	73
Tangible and intangible assets	17	5,625	5,173
TOTAL ASSETS		**277,039**	**249,822**
LIABILITIES			
Due to customers	18	61,032	78,323
Borrowings	19	4,820	5,156
Provisions	20	804	1,151
Other liabilities	21	44,596	51,712
Total liabilities		**111,252**	**136,342**
EQUITY			
Owner's capital	22	153,000	106,489
Retained earnings		7,906	6,991
Regulatory reserves		4,881	-
Total equity		**165,787**	**113,480**
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		**277,039**	**249,822**
OFF BALANCE SHEET ITEMS	20	**19,100**	**19,045**

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

Signed on behalf of Development Bank of the Federation of Bosnia and Herzegovina on 8 May 2012:

Ramiz Džaferović
President of the Management Board

Belma Čemirlija
Executive Director for business support and funds management

Cash flow statement
for the year ended 31 December 2011
(all amounts are expressed in thousands of KM, unless otherwise stated)

	2011	2010
Net Profit	**5,786**	**2,488**
Adjustments to reconcile net result to net cash provided by operating activities:		
Depreciation	388	401
Impairment losses and provisions	(303)	797
Loss on disposal of property and equipment	2	30
Changes in assets and liabilities:		
Decrease / (increase) in obligatory reserve with CBBH	552	(576)
Decrease in loans to banks, before allowance, net	2,835	4,360
Increase in loans to customers, before allowance, net	(34,161)	(10,450)
Increase / (decrease) in other assets, before allowance net	(133)	41
Increase in liabilities to customers, net	9,349	5,457
(Decrease) / increase in other liabilities, net	(7,156)	11,321
NET CASH (USED IN) / FROM OPERATING ACTIVITIES	**(22,841)**	**13,869**
Investing activities		
Purchases of property and equipment	(842)	(409)
NET CASH USED IN INVESTING ACTIVITIES	**(842)**	**(409)**
Financing activities		
Repayment of borrowings, net	(336)	(107)
Increase of share capital	15,000	-
NET CASH FROM / (USED IN) FINANCING ACTIVITIES	**14,664**	**(107)**
NET (DECREASE) / INCREASE IN CASH AND CASH EQUIVALENTS	**(9,019)**	**13,353**
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF YEAR	**70,399**	**57,046**
CASH AND CASH EQUIVALENTS AT THE END OF YEAR	**61,380**	**70,399**

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

Statement of changes in equity
for the year ended 31 December 2011
(all amounts are expressed in thousands of KM, unless otherwise stated)

	Owner's equity	Regulatory reserves	Retained earnings	Total
Balance as of 1 January 2010	**87,486**	**-**	**23,506**	**110,992**
Transfer of retained earnings of the legal successor of the Bank	19,003	-	(19,003)	-
Profit for the year	-	-	2,488	2,488
Other comprehensive income	-	-	-	-
Total comprehensive income	-	-	*2,488*	*2,488*
Balance as of 31 December 2010	**106,489**	**-**	**6,991**	**113,480**
Increase in equity (Note 22)	41,640	-	-	41,640
Transfer (Note 22)	4,871	-	(4,871)	-
Effects of change of accounting policy (Note 3)	-	-	4,881	4,881
Regulatory reserves (Note 3)	-	4,881	(4,881)	-
Profit for the year	-	-	5,786	5,786
Other comprehensive income	-	-	-	-
Total comprehensive income	-	-	*5,786*	*5,786*
Balance as of 31 December 2011	**153,000**	**4,881**	**7,906**	**165,787**

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

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

1. GENERAL

Development Bank of the Federation of Bosnia and Herzegovina ("the Bank") was established by the Law on the Development Bank of the Federation of Bosnia and Herzegovina ("Official Gazette No. 37/08). The Bank's headquartered in Igmanska 1, Sarajevo. The Bank is 100%-owned by the Federation of Bosnia and Herzegovina.

In compliance with the Law and the Statute of the Bank, bodies of the Bank are: the Assembly (consisting of the Government of the FBiH), the Supervisory Board, the Management Board and the Audit Committee.

As of 31 December 2011 the Bank has organizational components – branch offices in Mostar, Bihać, Zenica, Orašje and Livno.

The goals of the Bank are encouragement of economic development and overall social development and the encouragement of sustainable growth to the territory of the Federation of Bosnia and Herzegovina, relating to the financial and general social goals defined by the Law.

Corporate loan and guarantee approval are the key activities of the Bank either directly or through other banks, in order to support the local economy, regional development and employment. The Bank performs loan operations in the name and on behalf of the Bank (from capital, collected deposits and borrowings), as well as in the name and on behalf of the Federation BiH, on which behalf it manages its domestic and foreign funds aimed for development projects, as well as receives cash deposits and takes loans, as a function of financing development projects.

Supervisory Board (from 1 December 2011)

Petar Jurčić	Chairman
Senad Softić	Member
Samir Ćatović	Member
Ružica Ćurković	Member
Ivica Musić	Member
Dženan Đonlagić	Member
Aid Berbić	Member

Supervisory Board (from 25 May until 25 July 2011)

Ivan Šakota	Chairman
Senad Softić	Member
Mirna Čomić	Member
Aid Berbić	Member
Marijana Bandić-Glavaš	Member
Mirsad Novalić	Member
Katica Vranjković	Member

Supervisory Board (until 30 April 2011)

Ante Vidačak	Chairman
Senad Softić	Member
Branko Ivković	Member
Duljko Hasić	Member
Lutvo Mehonić	Member
Fikret Hadžić	Member
Zoran Pandža	Member

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

1. GENERAL (CONTINUED)

Management Board

Ramiz Džaferović	Director and President
Borislav Trlin	Vice president (from 29 February 2012)
Gojko Ivanković	Vice president (until 29 February 2012)
Dubravka Bošnjak	Executive Director
Belma Izmirlija	Executive Director

Audit Committee

Dragan Prusina	President
Advija Alihodžić	Vice president
Fatima Drinčić	Member
Dragan Kolobarić	Member
Meliha Bašić	Member from 28 April 2011

2. ADOPTION OF NEW AND REVISED STANDARDS

2.1 Standards and Interpretations effective in current period

The following amendments to the existing standards issued by the International Accounting Standards Board and interpretations issued by the International Financial Reporting Interpretations Committee are effective for the current period:

- Amendments to IFRS 1 "First-time Adoption of IFRS"- Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters (effective for annual periods beginning on or after 1 July 2010),
- Amendments to IAS 24 "Related Party Disclosures" - Simplifying the disclosure requirements for government-related entities and clarifying the definition of a related party (effective for annual periods beginning on or after 1 January 2011),
- Amendments to IAS 32 "Financial Instruments: Presentation" – Accounting for rights issues (effective for annual periods beginning on or after 1 February 2010),
- Amendments to various standards and interpretations "Improvements to IFRSs (2010)" resulting from the annual improvement project of IFRS published on 6 May 2010 (IFRS 1, IFRS 3, IFRS 7, IAS 1, IAS 27, IAS 34, IFRIC 13) primarily with a view to removing inconsistencies and clarifying wording (amendments are to be applied for annual periods beginning on or after 1 July 2010 or 1 January 2011 depending on standard/interpretation),
- Amendments to IFRIC 14 "IAS 19 - The Limit on a defined benefit Asset, Minimum Funding Requirements and their Interaction" - Prepayments of a Minimum Funding Requirement (effective for annual periods beginning on or after 1 January 2011),
- IFRIC 19 "Extinguishing Financial Liabilities with Equity Instruments" (effective for annual periods beginning on or after 1 July 2010).

The adoption of these amendments to the existing standards and interpretations has not led to any changes in the Bank's accounting policies.

2. ADOPTION OF NEW AND REVISED STANDARDS (CONTINUED)

2.2 Standards and Interpretations in issue not yet adopted

At the date of authorisation of these financial statements the following standards, revisions and interpretations were in issue but not yet effective:

- IFRS 9 "Financial Instruments" (effective for annual periods beginning on or after 1 January 2015),
- IFRS 10 "Consolidated Financial Statements" (effective for annual periods beginning on or after 1 January 2013),
- IFRS 11 "Joint Arrangements" (effective for annual periods beginning on or after 1 January 2013),
- IFRS 12 "Disclosures of Involvement with Other Entities" (effective for annual periods beginning on or after 1 January 2013),
- IFRS 13 "Fair Value Measurement" (effective for annual periods beginning on or after 1 January 2013),
- IAS 27 (revised in 2011) "Separate Financial Statements" (effective for annual periods beginning on or after 1 January 2013),
- IAS 28 (revised in 2011) "Investments in Associates and Joint Ventures" (effective for annual periods beginning on or after 1 January 2013),
- Amendments to IFRS 1 "First-time Adoption of IFRS"- Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters (effective for annual periods beginning on or after 1 July 2011),
- Amendments to IFRS 1 "First-time Adoption of IFRS" - Government Loans (effective for annual periods beginning on or after 1 January 2013),
- Amendments to IFRS 7 "Financial Instruments: Disclosures"- Transfers of Financial Assets (effective for annual periods beginning on or after 1 July 2011),
- Amendments to IFRS 7 "Financial Instruments: Disclosures" - Offsetting Financial Assets and Financial Liabilities (effective for annual periods beginning on or after 1 January 2013),
- Amendments to IFRS 9 "Financial Instruments" and IFRS 7 "Financial Instruments: Disclosures" – Mandatory Effective Date and Transition Disclosures,
- Amendments to IAS 1 "Presentation of financial statements" - Presentation of Items of Other Comprehensive Income (effective for annual periods beginning on or after 1 July 2012),
- Amendments to IAS 12 "Income Taxes" - Deferred Tax: Recovery of Underlying Assets (effective for annual periods beginning on or after 1 January 2012),
- Amendments to IAS 19 "Employee Benefits" - Improvements to the Accounting for Post-employment Benefits (effective for annual periods beginning on or after 1 January 2013),
- Amendments to IAS 32 "Financial instruments: presentation" - Offsetting Financial Assets and Financial Liabilities (effective for annual periods beginning on or after 1 January 2014),
- IFRIC 20 "Stripping Costs in the Production Phase of a Surface Mine" (effective for annual periods beginning on or after 1 January 2013).

The Bank has elected not to adopt these standards, revisions and interpretations in advance of their effective dates. The Bank anticipates that the adoption of these standards, revisions and interpretations will have no material impact on the financial statements of the Bank in the period of initial application.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Statement of compliance

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

The financial statements have been prepared on the historical cost basis except for the revaluation of certain non-current assets and financial instruments.

The financial statements are prepared on an accrual basis of accounting, under the going concern assumption.

The financial statements are presented in thousands of Convertible mark (KM'000) which is the functional currency of the Bank.

Change of accounting policy

Up to 31 December 2010, as it was required by local legislation and decisions of Banking Agency of the Federation of Bosnia and Herzegovina ("FBA"), the Bank was preparing the financial statements in accordance with IFRS as modified by the regulatory requirements prescribed by FBA with respect to the calculation of provision for impairment of financial instruments. These rules required banks to calculate the allowance for impairment of financial assets and provision for commitments and contingencies using the matrix system based on number of overdue days. The matrix system applied on outstanding loan receivables, as well as on commitments and contingencies, was as follows:

- 0 - 30 overdue days - 2%,
- 31 - 50 overdue days - 5%,
- 51 - 70 overdue days - 10%,
- 71 - 90 overdue days - 15%,
- 91 - 120 overdue days - 16%,
- 121 - 140 overdue days - 20%,
- 141 - 160 overdue days - 30%,
- 161 - 180 overdue days - 40%,
- 181 - 210 overdue days - 41%,
- 211 - 230 overdue days - 45%,
- 231 - 250 overdue days - 50%,
- 251 - 270 overdue days - 60%,
- Above 271 overdue days - 100%.

This was not in accordance with International Accounting Standard ("IAS") 39: 'Financial Instruments: Recognition and Measurement', which requires assessment at each reporting period date as to whether there is any objective evidence that a financial asset or group of financial assets is impaired. If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost has been incurred, the amount of the loss should be measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate.

Additionally, the banks had to recognize the general provision of 2% for some other items of assets.

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

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Change of accounting policy (continued)

Based on the Guidelines on the changes to the means for creating, recording and reporting forms for the loan loss reserves, issued by FBA in January 2011, the banks are obliged to introduce a new methodology for assessment of impairment losses on the financial assets (loans and receivables), in line with the requirements of IAS 39, and provisions for commitments and contingencies, in line with the requirements of IAS 37: "Provisions, Contingent Liabilities and Contingent Assets", effective from 1 January 2011. These guidelines also eliminated the requirement for general provisions of 2 % for other items of assets. Also, the banks are required to recognize the difference between the allowance for impairment losses on financial assets and provisions according to new accounting policy and the level of allowance for impairment losses on financial assets and provisions that would have been determined if the matrix system was still applied, under Regulatory reserves within the equity. The difference should be determined at the end of every year and upon decision of the Bank's Assembly on allocation of net result for the year kept at required level.

Due to the fact that new accounting policy for impairment losses on financial assets and provisions by its nature is based on the approximations and the accounting estimates made by the Management, the Bank was not able to determine the effects of the change in the accounting balances to the individual balances on the income statements, statement of comprehensive income, statement of cash flows and changes in equity for the years ended 31 December 2009 and 2010.

Consequently, according to IAS 8: "Accounting Policies, Changes in Accounting Estimates and Errors", the new accounting policy was applied prospectively by making an adjustment to the opening balances of the equity in 2011. The adjustment may be presented as follows:

	Effect on Regulatory reserves (within the equity)
Release of allowance for impairment losses on loans to other banks (Note 15)	1,392
Release of allowance for impairment losses on loans and advances to customers (Note 16)	3,102
Adjustment on provision for commitments and contingencies (Note 20)	387
	4,881

With regard to the change of accounting policy, FBA required the banks to create regulatory reserve as difference between the allowance for impairment losses on financial assets and provisions according to the new accounting policy and the level of allowance for impairment losses on financial assets and provisions that would have been determined if the matrix system had been applied at the date of new accounting policy application.

Interest income and expense

Interest income and expense for all interest-bearing financial instruments, except for those classified as held for trading or designated at fair value through profit and loss, are recognized within 'interest and similar income' and 'interest expense and similar charge' in the income statement using the effective interest rate method.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fee and commission income and expense

Fees and commissions consist mainly of fees earned on domestic and foreign payment transactions, and fees for loans and other credit instruments issued by the Bank. Fees for payment transactions are recognized in the period when services are rendered.

Loan origination fees, after approval and drawdown of loans, are deferred (together with related direct costs) and recognized as an adjustment to the effective yield of the loan over its life.

Employee benefits

On behalf of its employees, the Company pays personal income tax, and contributions for pension, disability, health and unemployment insurance, on and from salaries, which are calculated as per the set legal rates during the course of the year on the gross salary. The Company pays those tax and contributions in the favour of the institutions on federal and cantonal level, as follows:

	Federation	Canton
Personal income tax	-	100%
Contributions for pension and disability insurance	100%	-
Contributions for health insurance	9%	91%
Contributions for unemployment insurance	30%	70%

Retirement severance payments

According to the local legislation he Bank makes provision for retirement severance payments of minimum six salaries of the employee in question paid in the preceding month or six average salaries of the Federation of Bosnia and Herzegovina for the preceding month, depending on what is more favourable to the employee.

The obligation and costs of these benefits are determined by using a projected unit credit method. The projected unit credit method considers each period of service as giving rise to an additional unit of benefit entitlement and measures each unit separately to build up the final obligation. The obligation is measured at the present value of estimated future cash flows using a discount rate that is similar to the estimated interest rate on government bonds.

Taxation

According to Article 32 of the Law on Development Bank of the Federation of Bosnia and Herzegovina ("Official Gazette number 37/08), the Bank's, the Bank is not subject to corporate profit tax.

Bank's liability is to pay various indirect taxes which are included in administrative expenses.

Cash and cash equivalents

For the purpose of reporting cash flows, cash and cash equivalents are defined as cash, balances with the Central bank of Bosnia and Herzegovina ("CBBH"), current accounts with other banks and cash at hand.

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

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Financial assets

Financial assets are recognized and derecognized on a trade date where the purchase or sale of an investment is under a contract whose terms require delivery of the instrument within the timeframe established by the market concerned, and are initially measured at fair value, net of transaction costs, except for those financial assets classified as at fair value through profit or loss, which are initially measured at fair value.

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

Method of effective interest rate

The effective interest method is a method of calculating the amortized cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period.

Income is recognized on an effective interest basis for financial instruments: 'held-to-maturity investments', 'available-for-sale' and 'loans and receivables'.

Financial assets at FVTPL

Financial assets are classified as at FVTPL where the financial asset is either held for trading or it is designated as at FVTPL.

A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling in the near future; or
- it is a part of an identified portfolio of financial instruments that the Bank manages together and has a recent actual pattern of short-term profit-taking.

Financial assets at FVTPL are stated at fair value, with any resultant gain or loss recognized in profit or loss. The net gain or loss recognized in profit or loss incorporates any dividend or interest earned on the financial asset. Fair value is determined in the manner described in Note 25, point j).

Loans and receivables

Loans and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as loans and receivables. Loans and receivables are measured at amortized cost using the effective interest method, less any impairment. Interest income is recognized by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Impairment of financial assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at each reporting period date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.

For all other financial assets objective evidence of impairment could include:

- significant financial difficulty of the counterparty; or
- default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organisation.

For financial assets carried at amortised cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, where the carrying amount is reduced through the use of an allowance account. When a trade receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognized in profit or loss.

With the exception of AFS equity instruments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment does not exceed what the amortised cost would have been had the impairment not been recognized.

In respect of AFS equity securities, any increase in fair value subsequent to an impairment loss is recognized directly in equity.

Derecognition of financial assets

Bank derecognizes a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Bank neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Bank continues to recognize the financial asset.

Financial liabilities

Financial guarantee contract liabilities

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

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

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Financial liabilities (continued)

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

Other financial liabilities

Other financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs.

Other financial liabilities are subsequently measured at amortised cost using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

Derecognition of financial liabilities

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

Tangible and intangible assets

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

Properties in the course of construction for supply or administrative purposes are carried at cost, less any recognised impairment loss. Cost includes professional fees and, for qualifying assets, borrowing costs capitalised in accordance with the Bank's accounting policy. Such properties are classified to the appropriate categories of property and equipment when completed and ready for intended use.

Depreciation commences when the assets are ready for their intended use. Depreciation is calculated on a straight-line basis over the estimated useful life of the applicable assets. Estimated depreciation rates were as follows:

	%
Buildings	3.00
Furniture and other office equipment	20.00
Vehicles	20.00
Computers	33.33

Impairment

At each reporting period date, the Bank reviews the carrying amounts of its tangible and intangible assets 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).

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Tangible and intangible assets (continued)

Impairment (continued)

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 recognized as an expense immediately, unless the relevant asset is land or buildings other than investment property carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

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 recognized for the asset in prior years. A reversal of an impairment loss is recognized 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.

Foreign currency translation

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

The Bank values its assets and liabilities by middle rate of CBBH valid at the date of balance sheet, which approximate market rates. The principal rates of exchange set forth by CBBH and used in the preparation of the Bank's balance sheet at the reporting dates were as follows:

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

Funds managed for and on behalf of third parties

The Bank manages significant funds for and on behalf of the Government of the FBiH (Ministry of Finance, Ministry of Development, Entrepreneurship and Craft and Ministry of Agriculture, Water Management and Forestry and Ministry of environment and tourism) and the Federal Employment Agency. These amounts do not represent the Bank's assets and are excluded from the Bank's balance sheet. Income and expenses from such operations are charged to the principal and the Bank does not bear any liabilities and risks. For these services, the Bank charges fees. For details refer to Note 24.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Provisions

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

Owner's capital

Owner's capital consists of one share of the Federation of BiH and represents the capital of the legal predecessor of the Bank, the Investment bank of the FBiH, taken over by the Bank on its inception.

In accordance with the provisions of the Law on Development Bank of the Federation of Bosnia and Herzegovina, Article 3, the capital of the Bank should be increased by 400 million KM from the budget of Government of the FBiH in equal installments in the next four years, starting from 2008 to 2011.

Up to 31 December 2011 the Government did not make the capital injection in the above stated contracted dynamics and amounts.

4. CRITICAL ACCOUNTING JUDGMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the Bank's accounting policies, which are described in Note 3, the Management is required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

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

Key sources of estimation uncertainty

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

Useful lives of property and equipment

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

Impairment losses on loans

As described in Note 3 above, at each reporting period date, the Bank assessed indicators for impairment of loans and other financial assets.

Provisions for employee benefits

As described at Note 3 above, in paragraph with heading employee benefits, provisions for the employee benefits are calculated using the projected credit unit method.

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

5. INTEREST AND SIMILAR INCOME

	2011	2010
Interest on loans to customers	10,298	8,444
Interest on loans to banks	302	113
Interest on placements with CBBH	102	49
Interest on placements with other banks	59	127
	10,761	**8,733**

6. INTEREST EXPENSE AND SIMILAR CHARGES

	2011	2010
Interest on borrowings	76	87
	76	**87**

7. FEE AND COMMISSION INCOME

	2011	2010
Fee income from Agency Activities	1,034	1,067
Fees income from guarantees and letter of credits	231	224
Fees from other transactions	190	238
	1,455	**1,529**

8. OTHER OPERATING EXPENSES

	2011	2010
Donations	27	50
FOREX loss	8	197
Loss on disposal of equipment	1	10
Other	6	2
	42	**259**

9. OTHER OPERATING INCOME

	2011	2010
Grants	73	60
Other	32	54
	105	**114**

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

10. PERSONNEL EXPENSES

	2011	2010
Net salaries	2,279	2,241
Taxes and contributions	1,651	1,587
Other	1,250	1,135
	5,180	**4,963**

The average number of employees of the Bank during the year ended 31 December 2011 and 31 December 2010 was 133 and 121, respectively.

11. OTHER ADMINISTRATIVE EXPENSES

	2011	2010
Advertising, entertaining and sponsorship	256	202
Fees and taxes	205	172
Telecommunication costs	201	210
Energy costs	135	146
Supervisory board and Audit committee fees	133	189
Services	123	136
Maintenance	96	202
Material costs	89	92
Rent	83	145
Insurance	44	43
Bank fees	15	17
Other costs	92	91
	1,472	**1,645**

12. IMPAIRMENT LOSSES AND PROVISIONS

	2011	2010
Loans to banks (Note 15)	1	(130)
Loans and receivables to customers (Note 16)	(379)	991
Other assets	(5)	-
Provision for commitments and contingencies (Note 20)	2	(111)
Other provisions (Note 20)	78	47
	(303)	**797**

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

13. CASH AND BALANCES WITH BANKS

	31 December 2011	31 December 2010
Current accounts with other banks in foreign currencies	36,994	57,375
Current account with CBBH	24,347	12,984
Cash at hand	39	40
	61,380	**70,399**

Cash and current accounts with banks include funds for and on behalf of third parties (Note 24).

14. OBLIGATORY RESERVE WITH THE CENTRAL BANK OF BOSNIA AND HERZEGOVINA

	31 December 2011	31 December 2010
Obligatory reserve with CBBH	3,629	4,181
	3,629	**4,181**

Minimum obligatory reserve is calculated as 10% as at 31 December 2011 (2010: 14%) on the average amount of deposits and borrowed funds in all currencies for each working day during 10 calendar days.

Interest rates on funds kept up to minimum obligatory reserve as of 31 December 2011 and 2010 were 0.11% to 1.22% and 0.5% to 0.2% respectively.

15. LOANS TO BANKS, NET

	31 December 2011	31 December 2010
Loans to banks	**3,498**	**3,436**
Provisions for potential losses	(1,610)	(104)
Total loans to banks after allowance for impairment	**1,888**	**3,332**

The movements in the allowance for impairment losses are summarized as follows:

	2011	2010
Balance at beginning of the year	**104**	**234**
Effects of change of accounting policy – re-recognition of receivables previously written-off in full amount according to superseded FBA's decision (E category)	2,897	-
Effects of change of accounting policy – release of allowance (Note 3)	(1,392)	-
Net changes in allowances (Note 12)	1	(130)
Balance at end of the year	**1,610**	**104**

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

16. LOANS TO CUSTOMERS, NET

	31 December 2011	31 December 2010
Short-term loans (including current portion of long-term loans):		-
Corporate	18,204	1,871
Retail	96	36
Current portion of long-term loans	14,704	1,047
	33,004	*2,954*
Long-term loans (excluding current portion):		
Corporate	187,029	170,205
Retail	3,296	3,298
	190,325	*173,503*
Total loans before allowance for impairment	***223,329***	***176,457***
Provisions for potential losses	(19,023)	(9,793)
	204,306	**166,664**

The movements in the allowance for impairment losses are summarized as follows:

	2011	2010
Balance at beginning of the year	**9,793**	**9,280**
Effects of change of accounting policy – re-recognition of receivables previously written-off in full amount according to superseded FBA's decision (E category)	12,711	-
Effects of change of accounting policy – release of allowance (Note 3)	(3,102)	-
Net changes in allowances (Note 12)	(379)	991
Write off	-	(478)
Balance at end of the year	**19,023**	**9,793**

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

16. LOANS TO CUSTOMERS, NET (CONTINUED)

Analysis of loans before allowance for impairment losses by industry:

	31 December 2011	31 December 2010
Loans to corporate		
Manufacturing	109,585	89,783
Agricultural	22,849	18,216
Construction	16,084	7,029
Trade	11,657	8,418
Restaurants	3,900	3,156
Transportation, storage and telecommunication	9,592	5,510
Financial services	664	1,292
Real estates	181	-
Public administration and defense	24,955	15,987
Other	19,804	23,732
	219,271	*173,123*
Loans to retail		
General consumption	238	390
Housing loans	620	740
Crafts	3,200	2,204
	4,058	*3,334*
	223,329	**176,457**

Figures presented in above table includes principal, increased for interest receivables and decreased for deferred income from origination fee as of 31 December 2011 and 31 December 2010.

Weighted average interest rates for granted loans as at 31 December 2011 and 2010 were as follows:

	31 December 2011	31 December 2010
Corporate	4.70%	4.63%
Retail	4.17%	4.10%

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

17. TANGIBLE AND INTANGIBLE ASSETS

	Buildings	Vehicles	Furniture & equipment	Software	Assets in progress	Total
COST						
At 31 December 2009	**6,160**	**620**	**1,808**	**525**	**-**	**9,113**
Additions	5	50	30	11	313	409
Disposals	-	(114)	(15)	-	-	(129)
At 31 December 2010	**6,165**	**556**	**1,823**	**536**	**313**	**9,393**
Additions	-	-	133	27	682	842
Disposals	-	-	(24)	-	-	(24)
At 31 December 2011	**6,165**	**556**	**1,932**	**563**	**995**	**10,211**
ACCUMULATED DEPRECIATION						
At 31 December 2009	**1,475**	**474**	**1,492**	**477**	**-**	**3,918**
Depreciation charge	185	72	133	11	-	401
Disposals	-	(84)	(15)	-	-	(99)
At 31 December 2010	**1,660**	**462**	**1,610**	**488**	**-**	**4,220**
Depreciation charge	185	57	124	22	-	388
Disposals	-	-	(22)	-	-	(22)
At 31 December 2011	**1,845**	**519**	**1,712**	**510**	**-**	**4,586**
NET BOOK VALUE						
31 December 2011	**4,320**	**37**	**220**	**53**	**995**	**5,625**
31 December 2010	**4,505**	**94**	**213**	**48**	**313**	**5,173**

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

18. DUE TO CUSTOMERS

	31 December 2011	31 December 2010
Demand deposits		
Private entities	5,638	14,782
Governments	10,698	430
Public entities	3,455	167
Individuals and crafts	120	158
Total demand deposits	***19,911***	***15,537***
Purpose deposits		
Individuals and crafts	2	30
Private entities	1	5
Total purpose deposits	***3***	***35***
Term deposits:		
Domestic currency		
Federal Employment Agency	34,463	32,917
Federal Ministry of Agriculture, Water Management and Forestry	-	683
Federal Ministry of Development, Entrepreneurship and Craft	*550*	2,746
Federal Ministry of Environment and Tourism	494	500
Federal Ministry of Displaced Persons and Refugees	3,000	-
Government of Federation of BiH (Saudi Fund)	2,372	2,575
Public entities	8	8
	40,887	*39,429*
Foreign currency		
Government of Federation of BiH - EUR	231	21,181
Government of Federation of BiH - USD	-	2,141
	231	*23,322*
Total term deposits	*41,118*	*62,751*
	61,032	**78,323**

No interest was charged on demand, purpose and term deposits.

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

19. BORROWINGS

	31 December 2011	31 December 2010
Government of the FBiH – Saudi Fund loan for development, interest rate 2% p.a. with maturity date 31 August 2021.	3,779	4,050
Government of the FBiH – Belgian merchandise loan, without interest rate, with maturity date 31 December 2027.	1,041	1,106
	4,820	**5,156**

By Government decision, the Bank has assumed obligation to pay the loan which Government contracted with creditors.

20. PROVISIONS

	Contingent liabilities	Employee benefits	Total
Balance as of 1 January 2010	**878**	**359**	**1,237**
Additional provisions recognized (Note 11)	-	47	47
Release of provisions (Note 12)	(111)	-	(111)
Reductions resulting from payments	-	(22)	(22)
Balance as of 31 December 2010	**767**	**384**	**1,151**
Effects of change of accounting policy – release of allowance (Note 3)	(387)	-	(387)
Additional provisions recognized (Note 12)	2	78	80
Reductions resulting from payments	-	(40)	(40)
Balance as of 31 December 2011	**382**	**422**	**804**

Contingent liabilities (Off-Balance sheet) as of 31 December 2011 were as follows:

	31 December 2011	31 December 2010
Performance guarantees	14,861	13,846
Undrawn lending commitments	3,199	4,436
Advance and payment guarantees	1,040	763
Tender guarantees	-	-
	19,100	**19,045**

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

21. OTHER LIABILITIES

	31 December 2011	31 December 2010
Manage funds liabilities (Note 24)	44,029	51,140
Deferred income	307	257
Liabilities toward suppliers	61	206
Accrued expenses	49	50
Other	150	59
	44,596	**51,712**

22. OWNER'S CAPITAL

	%	31 December 2011	%	31 December 2010
Government of the Federation of Bosnia and Herzegovina	100	153,000	100	106,489
		153,000		**106,489**

The owner's capital of the Bank has been increased through capitalization of Government's deposits as follows:

- Assembly's decision as of 6 July 2011 in amount of KM 3,640 thousand,
- Assembly's decision as of 30 September 2011 in amount of KM 23 millions.

Also, the owner's capital of the Bank has been increased through direct payments as follows:

- Assembly's decision as of 25 August 2011 in amount of KM 15 millions.

The Assembly of the Bank has, on its meeting held on 10 June 2011, adopted the Decision by which the amount of KM 4,871 thousand was transferred from retained earnings to the owner's capital of the Bank.

23. RELATED PARTY TRANSACTIONS

Transactions with related parties as at 31 December 2011 are summarized as follows:

Party	**Type of relation**	**31 December 2011**		**31 December 2010**	
		Receivables	**Payables**	**Receivables**	**Payables**
Government of the Federation of Bosnia and Herzegovina	Owner	-	55,495	-	86,122
Public institutions	Common owner	-	34,463	-	32,917
Companies in majority ownership of the Government of FBiH	Common owner	22,960	4	19,186	8
		22,960	**89,962**	**19,186**	**119,047**

Party	**Type of relation**	**2011**		**2010**	
		Income	**Expenses**	**Income**	**Expenses**
Government of the Federation of Bosnia and Herzegovina	Owner	986	76	1,016	87
Public institutions	Common owner	48	-	111	-
Companies in majority ownership of the Government of FBiH	Common owner	601	1,969	1,022	572
		1,635	**2,045**	**2,149**	**659**

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

23. RELATED PARTY TRANSACTIONS (CONTINUED)

Director's and executives' remuneration

The remuneration of directors and other members of key management during the year ended 31 December 2011 were as follows:

	2011	**2010**
Gross salaries	565	554
Other benefits	21	12
Fees to the members of Supervisory Board	78	123
	664	**689**

24. MANAGED FUNDS

Funds managed by the Bank on behalf of Government of FBIH and Federal Employment Agency are not assets of the Bank and, therefore, are not included in its balance sheet.

The table below provides analysis of the funds managed on behalf of customers:

	31 December 2011	**31 December 2010**
LOANS		
Funds placed by projects:		
Water and gas supply	59,231	62,721
Road construction and transport	15,414	16,206
Healthcare and education	24,325	16,700
Manufacturing	10,264	9,950
Agriculture	36,336	36,557
Forestry	444	668
Employment incentives	3,757	4,166
Micro finance	20,424	24,137
Other	2,349	2,401
Total placed by projects	*172,544*	*173,506*
Accrued interest and fees	11,326	10,857
Total	**183,870**	**184,363**
SOURCE OF FINANCING		
Government of FBIH	212,736	220,369
Federal Employment Agency	3,757	4,166
Other	80	111
Total sources:	*216,573*	*224,646*
Liabilities for accrued interest and fees	11,326	10,857
Total	**227,899**	**235,503**
Current liabilities from managed funds activities (see Note 21)	**44,029**	**51,140**

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

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

25. FINANCIAL INSTRUMENTS

a) Capital risk management

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

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

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

	31 December 2011	31 December 2010
Debt	65,852	83,479
Equity	165,787	113,480
Net debt to capital ratio	**39.72**	**73.56**

Debt is defined as liabilities to banks and clients presented in detail in Notes 18 and 19, also including finance lease liabilities. Capital includes total share equity, statutory reserves and accumulated losses.

Capital adequacy and the use of regulatory capital are monitored daily by the Bank's management, employing techniques based on the guidelines developed by FBA for supervisory purposes. The required information is filed with the FBA on a quarterly basis.

FBA requires each bank to: (a) hold the minimum level of the share capital and the lowest level of net capital (regulatory capital) of KM 15 million, and (b) maintain a ratio of total regulatory capital to the risk-weighted asset at or above the minimum of 12%. As of 31 December 2011 the Bank maintains a ratio of 69.5% (2010: 53.1%).

b) Significant accounting policies

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

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

25. FINANCIAL INSTRUMENTS (CONTINUED)

c) Categories of financial instruments

	31 December 2011	31 December 2010
Financial assets		
Cash and cash equivalents (including Obligatory reserves with CBBH)	65,009	74,580
Loans and receivables	206,194	169,996
Other assets	119	6
	271,322	**244,582**
Financial liabilities		
At amortized cost	110,142	134,934
	110,142	**134,934**

d) Financial risk management objectives

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

e) Market risk

The Bank's activities expose it primarily to the financial risks of changes in foreign currency exchange rates and interest rates (see below points f and g).

Market risk exposures are supplemented by sensitivity analysis. There has been no change to the Bank's exposure to market risks or the manner in which it manages and measures the risk.

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

25. FINANCIAL INSTRUMENTS (CONTINUED)

f) Foreign currency risk management

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

	KM	EUR	USD	Other currencies	Total
As of 31 December 2011					
ASSETS					
Cash and balances with banks	24,382	33,220	3,778	-	61,380
Obligatory reserve with CBBH	3,629	-	-	-	3,629
Loans and advances to banks, net	1,888	-	-	-	1,888
Loans and advances to customers, net	204,269	-	37	-	204,306
Other assets	118	1	-	-	119
Total	**234,286**	**33,221**	**3,815**	**-**	**271,322**
LIABILITIES					
Borrowings	-	1,041	3,779	-	4,820
Due to customers	60,796	236	-	-	61,032
Other liabilities	38,798	5,491	1	-	44,290
Total	**99,594**	**6,768**	**3,780**	**-**	**110,142**
As of 31 December 2010					
Total Monetary assets	**185.125**	**53.512**	**5.945**	**-**	**244.582**
Total Monetary liabilities	**102.650**	**26.092**	**6.192**	**-**	**134.934**

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

25. FINANCIAL INSTRUMENTS (CONTINUED)

f) Foreign currency risk management (Continued)

Foreign currency sensitivity analysis

The Bank is mainly exposed to EUR and USD. Since Convertible Mark (KM) is pegged to EUR, the Bank is not exposed to risk of change of EUR exchange rate.

The following table details the Bank's sensitivity to a 10% increase and decrease in KM against USD. 10% is the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the reasonably possible change in foreign exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the period end for a 10% change in USD. The sensitivity analysis includes external loans where the denomination of the loan is in a currency other than the currency of the lender or the borrower. A positive number below indicates an increase in profit where KM strengthens 10% against USD. For a 10% weakening of KM against USD, there would be an equal and opposite impact on the profit, and the balances below would be negative.

	USD Impact	
	31 December 2011	**31 December 2010**
Profit / (loss)	4	247

g) Interest rate risk management

The Bank is not exposed to interest rate due to borrowings with fixed interest rates.

The Bank's exposures to interest rates on financial assets and financial liabilities are detailed in the liquidity risk management section of this note (see point i).

h) Credit risk management

Credit risk refers to the risk that counterparty will default on its contractual obligations resulting in financial loss to the Bank. The Bank has adopted a policy of only dealing with creditworthy counterparties and obtaining sufficient collateral, where appropriate, as a means of mitigating the risk of financial loss from defaults.
The Bank's exposure and the credit ratings of its counterparties are continuously monitored and the aggregate value of transactions concluded is spread amongst approved counterparties. Credit exposure is controlled by counterparty limits that are reviewed and approved by the risk management committee annually.

The Bank does not have any significant credit risk exposure to any single counterparty or any company of counterparties having similar characteristics. The Bank defines counterparties as having similar characteristics if they are related entities.

For the particular loan exposures that are either past due or impaired, the Bank could renegotiate the contracted terms. The carrying amount of such financial assets as of 31 December 2011 amounted to KM 20,267 thousand (2010: KM 11,101 thousand).

The carrying amount of financial asset presented in financial statements, decreased for losses based on impairments, represents the Bank's maximum exposure to credit risk without taking account of the value of any collateral obtained.

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

25. FINANCIAL INSTRUMENTS (CONTINUED)

h) Credit risk management (continued)

Financial assets

	Total gross carrying amount	Unimpaired assets	Individually impaired assets	Individual impairment allowance	Collective impairment allowance	Total net carrying amount
31 December 2011						
Cash and balances with banks	61,380	61,371	9	-	-	61,380
Obligatory reserve with CBBH	3,629	3,629	-	-	-	3,629
Loans banks	3,498	1,354	2,144	1,610	-	1,888
Loans to customers, net	223,329	166,200	57,129	15,998	3,025	204,306
TOTAL	**291,836**	**232,554**	**59,282**	**17,608**	**3,025**	**271,203**
31 December 2010						
Cash and balances with banks	70,399	70,395	4	-	-	70,399
Obligatory reserve with CBBH	4,181	4,181	-	-	-	4,181
Loans banks	3,436	3,436	-	-	104	3,332
Loans to customers, net	176,457	166,106	10,351	3,382	6,411	166,664
TOTAL	**254,473**	**244,118**	**10,355**	**3,382**	**6,515**	**244,576**

Credit exposure and collateral

	Credit risk exposure		
	Net exposure	Loan commitments / Guarantees	Fair value of collateral
31 December 2011			
Cash and balances with banks	61,380	-	-
Obligatory reserve with CBBH	3,629	-	-
Loans banks	1,888	-	-
Loans to customers	204,306	19,100	735,817
Total	**271,203**	**19,100**	**735,817**
31 December 2010			
Cash and balances with banks	70,399	-	-
Obligatory reserve with CBBH	4,181	-	-
Loans banks	3,332	-	-
Loans to customers	166,664	19,045	720,075
Total	**244,576**	**19,045**	**720,075**

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

25. FINANCIAL INSTRUMENTS (CONTINUED)

Fair value of the collaterals

	31 December 2011	31 December 2010
Real estate	645,499	623,906
Movable property	81,949	91,980
Guarantees and insurance policy	8,369	4,189
Total	**735,817**	**720,075**

Arrears

	Total gross loan portfolio (principal)	Not due	Up to 30 days	31 – 90 days	91 – 180 days	181 – 270 days	over 270 days
Corporate loans	178,169	176,972	652	434	87	24	
Retail loans	3,348	3,298	23	19	7	1	-
Total	**181,517**	**180,270**	**675**	**453**	**94**	**25**	**-**

i) Liquidity risk management

Ultimate responsibility for liquidity risk management rests with the Management Board, which has built an appropriate liquidity risk management framework for the management of the Bank's short, medium and long-term funding and liquidity management requirements. The Bank manages liquidity risk by maintaining adequate reserves, banking facilities and reserve borrowing facilities, by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities.

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

25. FINANCIAL INSTRUMENTS (CONTINUED)

Liquidity and interest risk tables

The following tables detail the Bank's remaining contractual maturity for its financial assets. The tables have been drawn up based on the undiscounted contractual maturities of the financial assets including interest that will be earned.

Maturity for financial assets

	Weighted average effective interest rate (%)	Less than 1 month	2 to 6 months	7 months to 1 year	2 to 5 years	Over 5 years	Total
31 December 2011							
Non-interest bearing		65,133	-	-	-	-	65,133
Variable interest rate instruments	5.32	202	330	367	599	271	1,769
Fixed interest rate instruments	5.10	9,643	47,509	30,732	118,686	19,513	226,083
		74,978	**47,839**	**31,099**	**119,285**	**19,784**	**292,985**
31 December 2010							
Non-interest bearing		74,596	-	-	-	-	74,596
Variable interest rate instruments	4.91	304	750	1,393	1,359	340	4,146
Fixed interest rate instruments	5.03	5,297	23,997	29,189	108,365	19,083	185,931
		80,197	**24,747**	**30,582**	**109,724**	**19,423**	**264,673**

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

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

25. FINANCIAL INSTRUMENTS (CONTINUED)

Liquidity and interest risk tables (Continued)

Maturity for financial liabilities

	Weighted average effective interest rate (%)	Less than 1 month	2 to 6 months	7 months to 1 year	2 to 5 years	Over 5 years	Total
31 December 2011							
Non-interest bearing		64,435	122	127	1,191	41,132	107,007
Fixed interest rate instruments	2.00	-	227	225	1,731	1,993	4,176
		64,435	**349**	**352**	**2,922**	**43,125**	**111,183**
31 December 2010							
Non-interest bearing		67,333	296	201	1,103	62,820	13,753
Fixed interest rate instruments	2.00	184	40	223	1,716	2,353	4,516
		67,517	**336**	**424**	**2,819**	**65,173**	**136,269**

The Bank expects to meet its other obligations from operating cash flows and proceeds of maturing financial assets.

j) Fair value of financial instruments

The fair value of a financial instrument is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's-length transaction. Where available, fair value is based on quoted market prices. However, no readily available market prices exist for a significant portion of the Bank's financial instruments. In circumstances where the quoted market prices are not readily available, the fair value is estimated using discounted cash flow models or other pricing techniques as appropriate. Changes in underlying assumptions, including discount rates and estimated future cash flows, significantly affect the estimates. Therefore, the calculated fair market estimates may not be realisable in a current sale of the financial instrument, in particular considering lack of liquid market in Bosnia and Herzegovina.

Cash and cash equivalents

The carrying values of cash and balances with banks are generally deemed to approximate their fair value.

Loans to customers

Considering the specificity of the Bank, a large part of its portfolio of loans carries fixed interest rates and longer-term maturity whereby interest rates are below market rates

Customer deposits

For demand deposits and deposits with no defined maturities, fair value is taken to be the amount payable on demand at the balance sheet date. The estimated fair value of fixed-maturity deposits is based on discounted cash flows using rates currently offered for deposits of similar remaining maturities.

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

25. FINANCIAL INSTRUMENTS (CONTINUED)

j) Fair value of financial instruments *(Continued)*

Borrowings

Borrowings are either non-interest bearing or with fixed interest rate. The fair value of borrowings at fixed interest rates is estimated using discounted cash flow analyses, based upon interest rates currently offered for loans with similar terms to borrowers of similar credit quality..

26. CONTINGENT LIABILITIES

As of 31 December 2011, the Bank had contingent liabilities from pending litigations in the amount of KM 757 thousands (2010 – KM 213 thousands). Based on legal advices, the Management believes that cases can be successfully defended without leading to losses for the Bank. In accordance with the previously mentioned, there is no need to recognise any provisions.

27. EVENTS AFTER THE BALANCE SHEET DATE

Changes within the Board of Directors

As of 29 February 2012, Mr. Borislav Trlin was appointed as a new Vice-president, replacing Mr. Gojko Ivanković.

Regulatory requirements

With regard to the change of accounting policy as described in Note 3, on 29 March 2012, FBA issued an instruction requesting the banks that if the difference, between the allowance for impairment losses on financial assets and provisions according to the new accounting policy described in Note 3 of this report, at the level of individual contracts is less than the level of allowance for impairment losses on financial assets and provisions that would have been determined if the matrix system had been applied, then such difference should be recognized as Regulatory reserves within retained earnings. Furthermore, FBA requires that the effect of Regulatory reserves according to this instruction should be determined and booked as of 31 March 2012 that was subsequently, on 29 April 2012 changed to 30 June 2012.

28. APPROVAL OF THE FINANCIAL STATEMENTS

These financial statements were adopted and approved by the Management Board on 8 May 2012:

Ramiz Džaferović	Borislav Trlin	Dubravka Bošnjak	Belma Izmirlija
President of the Management Board	Vice President of the Management Board	Executive director	Executive director