

**CENTRAL BANK OF  
BOSNIA AND HERZEGOVINA**

INDEPENDENT AUDITOR'S REPORT AND FINANCIAL STATEMENTS  
FOR THE YEAR ENDED  
31 DECEMBER 2016

**Contents**

|   | <b>Page</b> |
|---|-------------|
| <b>Responsibility of the Management and Governing Board for the preparation and approval of the annual financial statements</b> | 1           |
| <b>Independent Auditor's Report</b>   | 2           |
| <b>Financial statements</b>   |             |
| Income statement  | 5           |
| Statement of comprehensive income   | 6           |
| Statement of financial position   | 7           |
| Statement of changes in equity  | 8           |
| Statement of cash flows   | 10          |
| Notes to the financial statements   | 11 - 51     |

## Responsibility of the Management and Governing Board for the preparation and approval of the annual financial statements

The Management is required to prepare financial statements for each financial year which give a true and fair view of the financial position of the Central Bank of Bosnia and Herzegovina (the "Bank") and of the results of its operations and cash flows, in accordance with International Financial Reporting Standards ("IFRS"), as published by the International Accounting Standards Board ("IASB"). The Management 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 Governing Board is responsible for selecting suitable accounting policies to conform to applicable legal requirements and the Management is responsible for their consistent application, making judgements and estimates that are reasonable and prudent and preparing the financial statements on a going concern basis.

The Management is responsible for the submission to the Governing Board of its annual financial statements, following which the Governing Board is required to approve the annual financial statements for submission to the Parliamentary Assembly of Bosnia and Herzegovina.

The accompanying financial statements set out on pages 5 to 51 were authorised by the Governing Board on 29 March 2017 and are signed below to signify this, on its behalf by:

  
Senad Softić, Ph.D.  
Governor





## Independent Auditor's Report

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### **To the Governing Board of the Central Bank of Bosnia and Herzegovina**

#### **Opinion**

We have audited the accompanying financial statements of the Central Bank of Bosnia and Herzegovina (hereinafter: the "Bank"), which comprise the Statement of financial position as at 31 December 2016, and the Income statement, Statement of comprehensive income, Statement of changes in equity and Statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2016, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

#### **Basis for Opinion**

We conducted our audit in accordance with International Standards on Auditing (hereinafter: "ISAs") effective for audits of financial statements for period ending on or 15 December 2016. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements of the Bank in the 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.

#### **Responsibilities of the Management and the Governing Board of the Bank for the Financial Statements**

The Management of the Bank is responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards, and for such internal control as the 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, the Management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern.

The Governing Board of the Bank is responsible for overseeing the Bank's financial reporting process.

#### **Auditor's Responsibilities for the Audit of the Financial Statements**

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but it 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, our responsibility as auditors is to exercise professional judgment and maintain professional scepticism 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 a 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 the Management.

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

We communicate with the Governing Board of the Bank 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.

**Other matter**

The financial statements of the Central Bank of Bosnia and Herzegovina as of and for the year ended 31 December 2015 were audited by another auditor who expressed an unmodified opinion on those statements on 31 March 2016.

Aleksandar Džombić, PhD  
 Director  
 Grant Thornton d.o.o.

Banja Luka, 29 March 2017



Aleksandar Džombić, PhD  
 Certified Auditor  
 Grant Thornton d.o.o.

Banja Luka, 29 March 2017

Suzana Stavrikj, Partner

Grant Thornton d.o.o.

Skopje, 29 March 2017



Kledian Kodra, Partner

Grant Thornton sh.p.k.

Tirana, 29 March 2017

## INCOME STATEMENT

| In thousands of KM  | Note | <i>For the year ended 31 December</i> |                 |
|---|------|---------------------------------------|-----------------|
|   |      | 2016                                  | 2015            |
| Interest income   | 18   | 28,740                                | 28,475          |
| Effects of negative interest rates from interest-bearing financial assets         | 18   | (8,565)                               | (1,098)         |
| Effects of negative deposit interest rate on deposits from local commercial banks | 18   | 2,169                                 | -               |
| <b>NET INTEREST INCOME</b>  |      | <b>22,344</b>                         | <b>27,377</b>   |
| Fee and commission income   | 19   | 10,072                                | 9,188           |
| Fee and commission expenses   | 19   | (533)                                 | (619)           |
| <b>NET FEE AND COMMISSION INCOME</b>  |      | <b>9,539</b>                          | <b>8,569</b>    |
| Net realized gains from sale of financial assets available-for-sale               | 6    | 8,383                                 | 24,266          |
| Net foreign exchange gains  | 20   | 60                                    | 858             |
| Other income  | 21   | 1,571                                 | 815             |
| <b>OPERATING INCOME</b>   |      | <b>41,897</b>                         | <b>61,885</b>   |
| Personnel expenses  | 22   | (18,929)                              | (20,433)        |
| Administrative and other operating expenses                                       | 23   | (6,793)                               | (7,824)         |
| Depreciation and amortisation   | 10   | (2,113)                               | (2,250)         |
| <b>OPERATING EXPENSES</b>   |      | <b>(27,835)</b>                       | <b>(30,507)</b> |
| <b>NET PROFIT FOR THE YEAR</b>  |      | <b>14,062</b>                         | <b>31,378</b>   |

The accompanying notes on pages 11 to 51 are an integral part of these financial statements.

## STATEMENT OF COMPREHENSIVE INCOME

| In thousands of KM  | Note | <i>For the year ended 31 December</i> |                |
|---|------|---------------------------------------|----------------|
|   |      | 2016                                  | 2015           |
| <b>NET PROFIT FOR THE YEAR</b>  |      | <b>14,062</b>                         | <b>31,378</b>  |
| <b>Other comprehensive income</b>   |      |                                       |                |
| <i>Items that may be reclassified subsequently to the income statement:</i>                             |      |                                       |                |
| Monetary gold   |      |                                       |                |
| Net changes in fair value of monetary gold  | 7    | 22,788                                | (435)          |
|   |      | <u>22,788</u>                         | <u>(435)</u>   |
| Financial assets available-for-sale   |      |                                       |                |
| Net changes in fair value of financial assets available-for-sale  | 6    | 53,673                                | 20,837         |
| Realized fair value gains from financial assets available-for-sale reclassified to the income statement | 6    | (8,383)                               | (24,266)       |
|   |      | <u>45,290</u>                         | <u>(3,429)</u> |
| <b>Total other comprehensive income / (loss)</b>  |      | <b>68,078</b>                         | <b>(3,864)</b> |
| <b>TOTAL COMPREHENSIVE INCOME FOR THE YEAR</b>  |      | <b>82,140</b>                         | <b>27,514</b>  |

The accompanying notes on pages 11 to 51 are an integral part of these financial statements.

## STATEMENT OF FINANCIAL POSITION

| In thousands of KM  | Note | 31 December<br>2016 | 31 December<br>2015 |
|---|------|---------------------|---------------------|
| <b>ASSETS</b>   |      |                     |                     |
| Foreign currency in cash                                    | 4    | 194,846             | 128,520             |
| Deposits with foreign banks                                 | 5    | 2,970,397           | 1,003,635           |
| Special Drawing Rights with the International Monetary Fund | 29   | 2,642               | 3,778               |
| Financial assets available-for-sale                         | 6    | 5,025,829           | 6,145,872           |
| Monetary gold   | 7    | 205,102             | 182,315             |
| Held-to-maturity investments                                | 8    | 1,132,328           | 1,142,191           |
| Other assets  | 9    | 4,626               | 3,955               |
| Property, equipment and intangible assets                   | 10   | 45,475              | 44,828              |
| Other investments   | 11   | 27,813              | 27,813              |
| <b>TOTAL ASSETS</b>   |      | <b>9,609,058</b>    | <b>8,682,907</b>    |
| <b>LIABILITIES, EQUITY AND RESERVES</b>                     |      |                     |                     |
| Currency in circulation                                     | 12   | 4,066,804           | 3,499,468           |
| Deposits from banks   | 13   | 4,269,143           | 4,063,537           |
| Deposits from the Government and other depositors           | 14   | 590,392             | 501,594             |
| Provisions for liabilities and charges                      | 15   | 1,611               | 1,452               |
| Other liabilities   | 16   | 13,676              | 23,127              |
| <b>Total liabilities</b>                                    |      | <b>8,941,626</b>    | <b>8,089,178</b>    |
| Initial capital   |      | 25,000              | 25,000              |
| General reserves (Retained earnings)                        |      | 537,892             | 532,267             |
| Other reserves  |      | 31,300              | 31,300              |
| Fair value reserves – monetary gold                         |      | (38,357)            | (61,145)            |
| Fair value reserves – financial assets available-for-sale   |      | 111,597             | 66,307              |
| <b>Total equity and reserves</b>                            | 17   | <b>667,432</b>      | <b>593,729</b>      |
| <b>TOTAL LIABILITIES, EQUITY AND RESERVES</b>               |      | <b>9,609,058</b>    | <b>8,682,907</b>    |

The accompanying notes on pages 11 to 51 are an integral part of these financial statements.

**STATEMENT OF CHANGES IN EQUITY**

| In thousands of KM                                   | Initial capital | General reserves<br>(Retained earnings) | Other reserves | Fair value reserves –<br>monetary gold | Fair value reserves –<br>financial assets<br>available-for-sale | Total          |
|--|-----------------|---|----------------|--|---|----------------|
| <b>Balance as of 1 January 2016</b>                  | <b>25,000</b>   | <b>532,267</b>                          | <b>31,300</b>  | <b>(61,145)</b>                        | <b>66,307</b>   | <b>593,729</b> |
| <b>Total comprehensive income for the year</b>       |                 |   |                |  |   |                |
| Profit for the year                                  | -               | 14,062                                  | -              | -                                      | -   | 14,062         |
| Other comprehensive income                           | -               | -                                       | -              | 22,788                                 | 45,290  | 68,078         |
|  | -               | <b>14,062</b>                           | -              | <b>22,788</b>                          | <b>45,290</b>   | <b>82,140</b>  |
| <b>Distribution of profit</b>                        |                 |   |                |  |   |                |
| Distribution of profit to the state budget (Note 24) | -               | (8,437)                                 | -              | -                                      | -   | (8,437)        |
| <b>Balance as of 31 December 2016</b>                | <b>25,000</b>   | <b>537,892</b>                          | <b>31,300</b>  | <b>(38,357)</b>                        | <b>111,597</b>  | <b>667,432</b> |

The accompanying notes on pages 11 to 51 are an integral part of these financial statements.

**STATEMENT OF CHANGES IN EQUITY (CONTINUED)**

| In thousands of KM                                   | Initial capital | General reserves (Retained earnings) | Other reserves | Fair value reserves – monetary gold | Fair value reserves – financial assets available-for-sale | Total          |
|--|-----------------|--------------------------------------|----------------|-------------------------------------|---|----------------|
| <b>Balance as of 1 January 2015</b>                  | <b>25,000</b>   | <b>519,716</b>                       | <b>31,300</b>  | <b>(60,710)</b>                     | <b>69,736</b>   | <b>585,042</b> |
| <b>Total comprehensive income for the year</b>       |                 |                                      |                |                                     |   |                |
| Profit for the year                                  | -               | 31,378                               | -              | -                                   | -   | 31,378         |
| Other comprehensive income                           | -               | -                                    | -              | (435)                               | (3,429)   | (3,864)        |
|  | -               | <b>31,378</b>                        | -              | <b>(435)</b>                        | <b>(3,429)</b>  | <b>27,514</b>  |
| <b>Distribution of profit</b>                        |                 |                                      |                |                                     |   |                |
| Distribution of profit to the state budget (Note 24) | -               | (18,827)                             | -              | -                                   | -   | (18,827)       |
| <b>Balance as of 31 December 2015</b>                | <b>25,000</b>   | <b>532,267</b>                       | <b>31,300</b>  | <b>(61,145)</b>                     | <b>66,307</b>   | <b>593,729</b> |

The accompanying notes on pages 11 to 51 are an integral part of these financial statements.

## STATEMENT OF CASH FLOWS

|  | Note | <i>For the year ended 31 December</i> |                    |
|--|------|---------------------------------------|--------------------|
|  |      | 2016                                  | 2015               |
| <b>In thousands of KM</b>  |      |                                       |                    |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>  |      |                                       |                    |
| <b>Profit for the year</b>   |      | <b>14,062</b>                         | <b>31,378</b>      |
| Adjustments for:   |      |                                       |                    |
| Depreciation and amortisation  |      | 2,113                                 | 2,250              |
| Net realized gains from sale of financial assets available-for-sale  |      | (8,383)                               | (24,266)           |
| Income from grants   |      | (218)                                 | (122)              |
| Provisions for liabilities and charges   |      | 219                                   | 341                |
| Loss on disposal of property and equipment   |      | 4                                     | 2                  |
| Dividend income recognized in the income statement   |      | (562)                                 | (586)              |
| Interest income from held-to-maturity investments and financial assets available-for-sale recognized in the income statement |      | (28,726)                              | (28,344)           |
| <b>Net cash flows from operating activities before changes in operating assets and liabilities</b>                           |      | <b>(21,491)</b>                       | <b>(19,347)</b>    |
| <b>Changes in operating assets and liabilities</b>   |      |                                       |                    |
| (Increase) in deposits with foreign banks  |      | (195,444)                             | -                  |
| (Increase) / decrease in other assets  |      | (283)                                 | 1,632              |
| Increase of currency in circulation  |      | 567,336                               | 288,960            |
| Increase in deposits   |      | 294,404                               | 482,546            |
| Increase / (decrease) in other liabilities   |      | 1,157                                 | (15)               |
| Pay-out of severance payments  |      | (60)                                  | (183)              |
| <b>Net cash from operating activities</b>  |      | <b>645,619</b>                        | <b>753,593</b>     |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>  |      |                                       |                    |
| Purchases of property, equipment and intangible assets   |      | (2,764)                               | (890)              |
| Collected principal and interest from available-for-sale financial assets  |      | 5,203,667                             | 4,975,016          |
| Purchases of available-for-sale financial assets   |      | (4,342,772)                           | (7,418,276)        |
| Sales of available-for-sale financial assets   |      | 330,016                               | 1,294,539          |
| Collected principal and interest from held-to-maturity investments   |      | 21,395                                | 14,444             |
| Purchases of held-to-maturity investments  |      | -                                     | (720,508)          |
| Dividends received   |      | 562                                   | 586                |
| <b>Net cash used in investing activities</b>   |      | <b>1,210,104</b>                      | <b>(1,855,089)</b> |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>  |      |                                       |                    |
| Distribution of profit to the state budget   |      | (18,827)                              | (21,247)           |
| <b>Net cash used in financing activities</b>   |      | <b>(18,827)</b>                       | <b>(21,247)</b>    |
| <b>Net increase / (decrease) in cash and cash equivalents</b>  |      | <b>1,836,896</b>                      | <b>(1,122,743)</b> |
| <b>Cash and cash equivalents at 1 January</b>  |      | <b>1,136,185</b>                      | <b>2,258,928</b>   |
| <b>Cash and cash equivalents at 31 December</b>  | 25   | <b>2,973,081</b>                      | <b>1,136,185</b>   |

The accompanying notes on pages 11 to 51 are an integral part of these financial statements.

## 1. GENERAL INFORMATION

The Central Bank of Bosnia and Herzegovina (the "Bank") was established in accordance with the Law on the Central Bank of Bosnia and Herzegovina, which was adopted by the Parliamentary Assembly of Bosnia and Herzegovina ("BiH") on 20 June 1997, according to the General Framework Peace Agreement in Bosnia and Herzegovina.

The Central Bank of Bosnia and Herzegovina started its operations on 11 August 1997.

The main objectives and tasks of the Central Bank of Bosnia and Herzegovina are:

- to define, adopt and control the implementation of monetary policy of BiH through the issuance of local currency (Convertible Mark or "KM") with full coverage in free, convertible foreign exchange assets;
- to keep and manage the official foreign exchange reserves of the Bank in a safe and profitable manner;
- to implement monetary policy in accordance with the Law on the Central Bank of Bosnia and Herzegovina;
- to establish and maintain adequate payment and settlement systems;
- to coordinate the activities of the banking agencies, who are in charge of issuing banking licences and supervising banks;
- to accept deposits from the state and public institutions of BiH and deposits from commercial banks;
- to issue provisions and guidelines for the performance of the Bank's operations, in accordance with the Law on the Central Bank of BiH;
- to take part in the operations of international organisations working on strengthening the financial and economic stability of the country;
- to represent BiH in international organisations regarding monetary policy issues.

The highest body of the Bank is the Governing Board, which is in charge of defining monetary policy and the control of its implementation, and the organisation and the strategy of the Bank in accordance with the Law on the Central Bank of Bosnia and Herzegovina.

The Management of the Bank consists of the Governor and Vice-Governors, appointed by the Governor with the approval of the Governing Board. The Management operationally manages the Bank's activities.

According to the Law on the Central Bank of Bosnia and Herzegovina, the Governor, with the approval of the Governing Board, appoints the Chief Audit Executive and three Deputies.

The Bank operates through its Head Office, three main units located in Sarajevo, Mostar, and Banja Luka, and two branches, one in Brčko District and other in Pale, the latter of which operates under the authorisation of the Main Bank of Republika Srpska of the Central Bank of Bosnia and Herzegovina in Banja Luka.

During the course of 2015 and 2016 and up to the date of this report, the Governing Board, Management, Office of the Chief Audit Executive and Audit Committee members were:

### **Governing Board**

|                         |                                 |
|-------------------------|---------------------------------|
| Senad Softić Ph.D.      | Chairman (from 11 August 2015)  |
| Ankica Kolobarić M.Sc.  | Member (from 11 August 2015)    |
| Kemal Kozarić Ph.D.     | Member (from 11 August 2015)    |
| Trivo Marinković M.Sc.  | Member (from 11 August 2015)    |
| Ljubiša Vladušić Ph.D.  | Member (from 11 August 2015)    |
| Kemal Kozarić Ph.D.     | Chairman (until 10 August 2015) |
| Fikret Čaušević Ph.D.   | Member (until 10 August 2015)   |
| Milenko Krajišnik Ph.D. | Member (until 10 August 2015)   |
| Željko Šain Ph.D.       | Member (until 10 August 2015)   |
| Vasilij Žarković Ph.D.  | Member (until 10 August 2015)   |

### **Management**

|                         |  |
|-------------------------|--|
| Senad Softić Ph.D.      | Governor (from 11 August 2015)         |
| Kemal Kozarić Ph.D.     | Governor (until 10 August 2015)        |
| Ernadina Bajrović M.Sc. | Vice-Governor                          |
| Radomir Božić Ph.D.     | Vice-Governor (until 16 February 2016) |
| Ankica Kolobarić M.Sc.  | Vice-Governor                          |
| Milica Lakić Ph.D.      | Vice-Governor (from 1 June 2016)       |

## 1. GENERAL INFORMATION (CONTINUED)

### **Office of the Chief Audit Executive**

|                      |                                 |
|----------------------|---------------------------------|
| Edis Kovačević M.Sc. | Chief Audit Executive           |
| Angela Medić         | Deputy to Chief Audit Executive |
| Jasmina Novalija     | Deputy to Chief Audit Executive |
| Krstinja Tošović     | Deputy to Chief Audit Executive |

### **Audit Committee**

|                   |                                |
|-------------------|--------------------------------|
| Mila Gadžić Ph.D. | Member                         |
| Sead Kreso Ph.D.  | Member                         |
| Radomir Repija    | Member (from 1 September 2015) |
| Gordana Ković     | Member (until 31 August 2015)  |

## 2. BASIS FOR PREPARATION

### 2.1. Statement of compliance

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

### 2.2. Basis of measurement

The financial statements have been prepared on the historical cost basis, except for the revaluation of certain financial instruments and monetary gold, which are stated at fair value.

Historical cost is generally based on the fair value of the consideration given in exchange for assets.

Fair value is the price that would be received to sell or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the Bank takes into account the characteristics of the asset or liability which market participants would take into account when pricing the asset or liability at the measurement date.

In addition, for financial reporting purposes, fair value measurements are categorised into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

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

### 2.3. Use of estimates and judgements

The preparation of financial statements in conformity with IFRS requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and their reported amounts of revenues and expenses during the reporting period. Actual results could differ from those 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 revision and future periods if the revision affects both current and future periods.

Information on amounts where significant uncertainty exists in their estimate and critical judgments in applying accounting policies that have the most impact on the amounts disclosed in these financial statements are disclosed in Note 3.17.

## **2. BASIS FOR PREPARATION (CONTINUED)**

### **2.4. Functional and presentation currency**

The Bank's financial statements are stated in the official national currency of Bosnia and Herzegovina which is the Convertible Mark (KM). All financial information has been rounded to the nearest thousand (unless otherwise indicated).

The official exchange rate of KM to the Euro (EUR) has been defined by the Law on the Central Bank of Bosnia and Herzegovina as KM 1.95583 = EUR 1. As required by the Law, the Bank is obliged to purchase and sell KM for EUR on demand, without any restrictions, within the territory of Bosnia and Herzegovina, at the defined exchange rate.

The Law on the Central Bank of Bosnia and Herzegovina defines the operational rules for a "currency board" to be used for issuing KM, according to which KM is issued only with the purchase of convertible foreign exchange currency with full coverage in net foreign assets.

### **2.5. Standards, interpretations and amendments to published standards that are effective in the current period**

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

- IFRS 14: "Regulatory Deferral Accounts" (effective for annual periods beginning on or after 1 January 2016),
- Amendments to IFRS 10: "Consolidated Financial Statements", IFRS 12: "Disclosure of Interests in Other Entities" and IAS 28: "Investments in Associates and Joint Ventures" - Investment Entities: Applying the Consolidation Exception (effective for annual periods beginning on or after 1 January 2016),
- Amendments to IFRS 11: "Joint Arrangements" – Accounting for Acquisitions of Interests in Joint Operations (effective for annual periods beginning on or after 1 January 2016),
- Amendments to IAS 1: "Presentation of Financial Statements" - Disclosure Initiative (effective for annual periods beginning on or after 1 January 2016),
- Amendments to IAS 16: "Property, Plant and Equipment" and IAS 38: "Intangible Assets" - Clarification of Acceptable Methods of Depreciation and Amortisation (effective for annual periods beginning on or after 1 January 2016),
- Amendments to IAS 16: "Property, Plant and Equipment" and IAS 41: "Agriculture" - Agriculture: Bearer Plants (effective for annual periods beginning on or after 1 January 2016),
- Amendments to IAS 27: "Separate Financial Statements" - Equity Method in Separate Financial Statements (effective for annual periods beginning on or after 1 January 2017),
- Amendments to various standards "Improvements to IFRSs (cycle 2012-2014)" resulting from the annual improvement project of IFRS (IFRS 5, IFRS 7, IAS 19 and IAS 34) primarily with a view to removing inconsistencies and clarifying wording (amendments are to be applied for annual periods beginning on or after 1 January 2016).

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

### **2.6. Standards and Interpretations in issue not yet adopted**

At the date of authorization 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 2018),
- IFRS 15: "Revenue from Contracts with Customers" (effective for annual periods beginning on or after 1 January 2018),
- IFRS 16: "Leases" (effective for annual periods beginning on or after 1 January 2019),
- Amendments to IFRS 2: „ Share – based Payment" - Classification and Measurement of Share-based Payment Transactions (effective for annual periods beginning on or after 1 January 2018),
- Amendments to IFRS 10: "Consolidated Financial Statements" and IAS 28: "Investments in Associates and Joint Ventures" – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (effective date postponed indefinitely),

## **2. BASIS FOR PREPARATION (CONTINUED)**

### **2.6. Standards and Interpretations in issue not yet adopted (continued)**

- Amendments to IAS 7: "Statement of Cash Flows" – Disclosure initiative (effective for annual periods beginning on or after 1 January 2017),
- Amendments to IAS 12: "Income Taxes" – Recognition of deferred tax assets from non-performed losses (effective for annual periods beginning on or after 1 January 2017),
- Amendments to IFRS 4: "Insurance Contracts" - Applying IFRS 9: "Financial Instruments" with IFRS 4 "Insurance Contracts" (effective for annual periods beginning on or after 1 January 2018 or when IFRS 9: "Financial Instruments" is first applied),
- IFRIC 22 "Foreign Currency Transactions and Advance Consideration" (effective for annual periods beginning on or after 1 January 2018),
- Amendments to IAS 40: "Investment Property"- Transfers of Investment Property (effective for annual periods beginning on or after 1 January 2018),
- Amendments to various standards "Improvements to IFRSs (cycle 2012-2014)" resulting from the annual improvement project of IFRS (IFRS 1, IFRS 12 and IAS 28) primarily with a view to removing inconsistencies and clarifying wording (amendments to IFRS 12 are to be applied for annual periods beginning on or after 1 January 2017 and amendments for IFRS 1 and IAS 28 are to be applied for annual periods beginning on or after 1 January 2018).

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, except for IFRS 9. Management is currently analysing the impact of IFRS 9 on the Bank's financial statements.

## **3. SIGNIFICANT ACCOUNTING POLICIES**

The accounting policies set out below have been applied in the preparation and presentation of these annual financial statements.

### **3.1. Interest income and expenses**

Interest income and expenses are recognized in the income statement using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the net carrying amount of the financial asset or liability. When calculating the effective interest rate, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not future credit losses.

The calculation of the effective interest rate includes all transaction costs and fees and points paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or liability.

Interest income and expenses presented in the income statement include interest on financial assets and financial liabilities measured at amortized cost calculated on an effective interest basis.

### **3.2. Fee and commission income and expenses**

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

Other fee and commission income and expenses mainly comprise fees earned and spent on domestic and foreign payment transactions for financial instruments issued and received by the Bank, respectively and are recognized in the income statement upon performance of the relevant service.

### 3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

#### 3.3. Foreign currency transactions

Transactions in foreign currencies are translated into the functional currency at the exchange rate prevailing on the settlement date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate applicable at that date. Non-monetary assets and liabilities that are measured based on historical cost in a foreign currency are translated using the exchange rate at the date of the transaction and are not retranslated at the reporting date.

Foreign exchange differences arising on retranslation of transactions and the assets and liabilities denominated in foreign currencies are recognized in the income statement.

| Middle exchange rate: | 31 December 2016 | 31 December 2015 |
|-----------------------|------------------|------------------|
|                       | KM               | KM               |
| USD                   | 1.85545          | 1.79007          |
| SDR                   | 2.494348         | 2.489439         |

#### 3.4. Dividend income

Dividend income from equity securities is recognized in the income statement when the Bank's right to receive income is established.

#### 3.5. Financial instruments

Financial assets and financial liabilities are recognized when the Bank becomes a party to the contractual provisions of the financial instruments.

Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognized directly in profit or loss.

##### Method of effective interest rate

The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability (or group of financial assets or financial liabilities) and of allocating interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or 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 instruments, or, where appropriate, a shorter period to the net carrying amount of the financial asset or financial liability.

##### 3.5.1 Financial assets

Financial assets are recognized and derecognized on the settlement date on which the purchase or sale of an instrument is delivered to or by the Bank, and are initially measured at fair value, plus 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: "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. As at 31 December 2016 and 2015, the Bank has no financial assets at FVTPL.

### 3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

#### 3.5. Financial instruments (continued)

##### 3.5.1 Financial assets (continued)

###### Loans and receivables

Receivables (including deposits with foreign banks) that have fixed or determinable payments that are not quoted in an active market are classified as loans and receivables.

Loans and receivables are initially recognized at fair value plus transaction costs.

After initial recognition, loans and receivables are measured at amortised cost using the effective interest rate method, less any impairment. Interest income is recognized by applying the effective interest rate.

###### Held-to-maturity investments

Government debt securities with fixed or determinable payments and fixed maturity dates that the Bank has the positive intent and ability to hold to maturity are classified as held-to-maturity investments. Held-to-maturity investments are recorded at amortized cost using the effective interest method less any impairment, with revenue recognized on an effective yield basis.

###### Financial assets available-for-sale ("AFS")

Debt and equity securities held by the Bank are classified as being AFS and are stated at fair value. Fair value is determined in the manner described in the Note 28. Gains and losses arising from changes in fair value of debt and equity securities are recognized in other comprehensive income in the fair value reserve account with the exception of impairment losses, interest calculated using the effective interest rate method and foreign exchange gains and losses on financial assets, which are recognized directly in profit or loss. Where the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously recognized in the fair value reserve account in other comprehensive income is included in profit or loss for the period.

Dividends on AFS equity instruments are recognized in profit or loss when the Bank's right to receive payments is established.

The fair value of AFS financial assets denominated in a foreign currency is determined in that foreign currency and translated at the middle exchange rate at the reporting period date. The change in fair value attributable to translation differences that result from a change in amortized cost of the asset is recognized in profit or loss and other changes are recognized in equity.

###### Impairment of financial assets

Financial assets are assessed for indicators of impairment at each reporting 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.

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 reorganisation.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively. Those individually significant assets which are not identified as impaired are subsequently included in the basis for collective impairment assessment. For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics.

For financial assets carried at amortized 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.

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

#### **3.5. Financial instruments (continued)**

##### **3.5.1 Financial assets (continued)**

###### Impairment of financial assets (continued)

The carrying amount of the financial asset is reduced through the use of an allowance account. When a 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 is reversed does not exceed what the amortized 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 in other comprehensive income.

###### Derecognition of financial assets

The 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

##### **3.5.2 Financial liabilities**

Financial liabilities are classified as either financial liabilities "at FVTPL" or "other financial liabilities". As at 31 December 2016 and 2015, the Bank has no financial liabilities at FVTPL.

###### Other financial liabilities

Other financial liabilities, including currency in circulation, deposits from the local banks and deposits from the Government and other depositors, are initially measured at fair value, net of transaction costs.

Other financial liabilities are subsequently measured at amortized cost using the effective interest method, with interest expense recognized on an effective yield basis.

###### Derecognition of financial liabilities

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

##### **3.6. Monetary gold**

Gold is initially recognized at cost, being the fair value of the consideration given including acquisition charges associated with the investment. After initial recognition, the gold is re-measured at fair value. Gains and losses arising from changes in fair value, referring to price changes and foreign exchange differences from conversion from USD to Convertible Mark are recognized in the fair value reserve within other comprehensive income, until the gold is sold, when they are recognized as realized gains or losses in the income statement.

The fair value of monetary gold is expressed in American dollars (USD), converted at the middle exchange rate as published by the Bank at the reporting date, and is measured at the last bid price for one ounce of gold (Oz) at the reporting date quoted on Reuters.

Foreign exchange gains and losses from conversion of prices of gold from USD to Convertible Mark are recognized as a part of fair value adjustments in the fair value reserve in other comprehensive income.

### 3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

#### 3.7. Cash and cash equivalents

For the purpose of reporting cash flows, cash and cash equivalents comprise the following categories: giro accounts, foreign currency in cash, foreign currency demand deposits, and deposits with maturity up to three months or less from the date of acquisition and Special Drawing Rights in the International Monetary Fund.

#### 3.8. Property, equipment and intangible assets

Properties, equipment and intangible assets consist of assets obtained from the Bank's own funds and cash and non-cash grants.

Properties, equipment and intangible assets are stated at cost, less accumulated depreciation/amortization and any recognized accumulated impairment losses. The purchase cost includes the purchase price and all costs directly related to bringing the asset into operating 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.

Property, equipment and intangible assets are periodically reviewed for impairment. Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount.

Assets in course of construction are reported at their cost of construction including costs charged by third parties. Upon completion, all accumulated costs of the asset are transferred to the relevant property and equipment category and subsequently subject to the applicable depreciation rates.

Depreciation and amortization is provided on all assets except land and assets in the course of construction on a straight-line basis at prescribed rate designed to write off the cost of the assets over their estimated useful lives. The estimated depreciation and amortization rates during 2015 and 2016 were as follows:

|                         |                |
|-------------------------|----------------|
| Software                | 20.0%          |
| Other intangible assets | 20.0%          |
| Buildings               | 1.3% to 4.0%   |
| Equipment               | 11.0% to 20.0% |
| Furniture               | 10.0% to 12.5% |
| Vehicles                | 15.5%          |

Gains and losses on disposal of property and equipment are recognized in the income statement.

The useful life of the property, equipment and intangible assets is reviewed and adjusted on an annual basis at minimum, if necessary, and it is applied prospectively.

#### 3.9. Impairment of non-financial assets

The carrying amounts of the Bank's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognized whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognized in the income statement.

The recoverable amount of other assets is the greater of their value in use and fair value less cost to sell. 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. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, as if no impairment loss had been recognized.

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

#### **3.10. Provisions for liabilities and charges**

Provisions are recognized 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 are determined by discounting the expected future cash flows at a rate that reflects current market assessments of the time value of money and the risks specific to the liability.

Provisions for liabilities and charges are maintained at the level that the Bank's management considers sufficient for absorption of incurred losses. The 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 recognized at inception. If the outflow of economic benefits to settle the obligations is no longer probable, the provision is reversed.

#### **3.11. Grants**

Grants related to assets, including non-cash grants, are initially recognized as deferred income at fair value and are then recognized as income from grants on a systematic basis over the useful life of the assets. Grants that compensate the Bank for expenses incurred are recognized in income statement as income from grants on a systematic basis in the same periods in which the expenses are recognized.

#### **3.12. Taxes**

According to Article 69 of the Law on the Central Bank of Bosnia and Herzegovina, the Bank, its assets, property and income, and its operations and transactions are exempt from all taxes and duties.

#### **3.13. Currency in circulation**

The Bank administers the issue and withdrawal of domestic bank notes and coins. The corresponding liability from the issued currency in circulation is recorded in the statement of financial position.

When currency is withdrawn from circulation, it is recognized as a liability as part of currency in circulation, until the formal date of withdrawal. Any outstanding amount not withdrawn, after the formal due date, is recognized as income.

Costs related to the production and design of banknotes and coins are initially recognized as a deferred cost and subsequently amortized through other operating expenses over a period of three years.

#### **3.14. Managed funds for and on behalf of third parties**

The Bank maintains certain accounts in foreign currencies related to agreements concluded between the governments of Bosnia and Herzegovina and its constituent entities and foreign governments and financial organisations, as well as foreign currency accounts of state institutions and agencies, and of commercial banks, for which the Bank acts as an agent.

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

#### **3.15. Employee benefits**

##### *Short-term employee benefits*

In accordance with local regulations, on behalf of its employees, the Bank 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 Bank pays those tax and contributions in the favour of the institutions of the Federation of Bosnia and Herzegovina (on federal and cantonal levels), Republika Srpska and Brčko District.

In addition, meal allowances, transport allowances and vacation bonuses are paid in accordance with the domestic legislation requirements. These expenses are recognized in the income statement in the period in which the expense is incurred.

##### *Long-term employee benefits*

According to local legal requirements, employees of the Bank are entitled to receive a one-time benefit on retirement, provided legal conditions are met, such as the age or years of service, which in accordance with the Bank's internal Acts is based on six regular monthly salaries paid to the respective employee in the last six months.

Such payments are treated as long-term employee benefits which are calculated annually by independent actuaries using the projected unit credit method. The discount rate used in the calculation of the liability is based on interest rates of domestic corporate bonds and government bonds which exist on the market.

#### **3.16. Financial arrangements of Bosnia and Herzegovina with the International Monetary Fund**

According to the financial arrangements made at the end of 2002 between Bosnia and Herzegovina and the International Monetary Fund ("IMF"), the statement of financial position of the Bank includes the following items related to Bosnia and Herzegovina's membership of the IMF: holdings of Special Drawing Rights ("SDRs"), accrued interest on such SDR holdings and the IMF No. 1 account and IMF No. 2 account.

Other assets and liabilities related to the IMF, belonging to or being the responsibility of Bosnia and Herzegovina, are recorded in a special Trust Fund within off-balance-sheet records (see also Note 29).

#### **3.17. Critical accounting judgements and key source 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 on-going 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 assumptions and estimates relating to material statement of financial position items are presented below.

##### Fair value of assets

The Bank's policy is to disclose fair value information on those financial assets and financial liabilities for which public market information is readily available or such value may be calculated by applying some alternative valuation techniques, and whose fair value is materially different from their recorded amounts. According to the Bank's management, amounts presented in the financial statements reflect the most reliable and useful estimate of fair value for financial reporting purposes, in accordance with IFRS.

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

**3.17. Critical accounting judgements and key source of estimation uncertainty (continued)**

Depreciation and amortisation charge and rates applied

The calculation of depreciation and amortisation, as well as depreciation and amortisation rates are based on the assessed economic useful life of property, equipment and intangible assets. Once a year, the Bank assesses economic useful life based on current assumptions.

**4. FOREIGN CURRENCY IN CASH**

Foreign currency in cash relates to:

| In thousands of KM           | 31 December<br>2016 | 31 December<br>2015 |
|------------------------------|---------------------|---------------------|
| Cash in vaults per currency: |                     |                     |
| - EUR                        | 194,768             | 128,440             |
| - CHF                        | 40                  | 39                  |
| - USD                        | 21                  | 21                  |
| - GBP                        | 17                  | 20                  |
| <b>TOTAL</b>                 | <b>194,846</b>      | <b>128,520</b>      |

**5. DEPOSITS WITH FOREIGN BANKS**

Term and demand deposits with foreign banks, analysed by type of currency, are as follows:

| In thousands of KM | 31 December<br>2016 | 31 December<br>2015 |
|--------------------|---------------------|---------------------|
| Term deposits:     |                     |                     |
| - EUR              | 2,265,332           | -                   |
|                    | <b>2,265,332</b>    | -                   |
| Demand deposits:   |                     |                     |
| - EUR              | 699,285             | 1,001,986           |
| - USD              | 4,286               | 1,606               |
| - Other currencies | 1,494               | 43                  |
|                    | <b>705,065</b>      | <b>1,003,635</b>    |
| <b>TOTAL</b>       | <b>2,970,397</b>    | <b>1,003,635</b>    |

Term deposits with foreign banks, analysed by remaining maturity, are as follows:

| In thousands of KM  | 31 December<br>2016 | 31 December<br>2015 |
|---------------------|---------------------|---------------------|
| Up to 1 month       | 742,008             | -                   |
| From 1 to 2 months  | 644,529             | -                   |
| From 2 to 3 months  | 683,351             | -                   |
| From 4 to 12 months | 195,444             | -                   |
| <b>TOTAL</b>        | <b>2,265,332</b>    | -                   |

## 5. DEPOSITS WITH FOREIGN BANKS (CONTINUED)

During 2016 the interest rates on demand deposits ranged from (0.68%) p.a. to (0.20%) p.a. (2015: from (0.50%) p.a. to (0.21% p.a.) and on term deposits from (0.54%) p.a. to (0.34%) p.a. (2015: from 0.01% p.a. to 0.03% p.a.).

Deposits with foreign banks include negative accrued interest in the amount KM (1.679) thousand as at 31 December 2016 (2015: included negative accrued interest in the amount KM (110) thousand).

The average effective yield rate on deposits amounted to (0.39%) (2015: (0.08%)).

Deposits with foreign banks analysed by the type of the bank invested in, are as follows:

| In thousands of KM | 31 December<br>2016 | 31 December<br>2015 |
|--------------------|---------------------|---------------------|
| Central banks      | 1,855,646           | 783,544             |
| Commercial banks   | 1,114,751           | 220,091             |
| <b>TOTAL</b>       | <b>2,970,397</b>    | <b>1,003,635</b>    |

Deposits with foreign banks can be analysed on a geographical basis as follows:

| In thousands of KM           | 31 December<br>2016 | 31 December<br>2015 |
|------------------------------|---------------------|---------------------|
| <b>Germany</b>               |                     |                     |
| Term deposits                | 664,357             | -                   |
| Demand deposits              | 329,620             | 630,582             |
|                              | <b>993,977</b>      | <b>630,582</b>      |
| <b>Luxembourg</b>            |                     |                     |
| Term deposits                | 624,880             | -                   |
| Demand deposits              | 293,192             | 293,307             |
|                              | <b>918,072</b>      | <b>293,307</b>      |
| <b>Switzerland</b>           |                     |                     |
| Term deposits                | 586,048             | -                   |
| Demand deposits              | 4,180               | 1,531               |
|                              | <b>590,228</b>      | <b>1,531</b>        |
| <b>Netherlands</b>           |                     |                     |
| Term deposits                | 390,047             | -                   |
| Demand deposits              | -                   | -                   |
|                              | <b>390,047</b>      | -                   |
| <b>France</b>                |                     |                     |
| Term deposits                | -                   | -                   |
| Demand deposits              | 78,073              | 78,215              |
|                              | <b>78,073</b>       | <b>78,215</b>       |
| <b>Total term deposits</b>   | <b>2,265,332</b>    | -                   |
| <b>Total demand deposits</b> | <b>705,065</b>      | <b>1,003,635</b>    |
| <b>TOTAL</b>                 | <b>2,970,397</b>    | <b>1,003,635</b>    |

## 6. FINANCIAL ASSETS AVAILABLE-FOR-SALE

Financial assets available-for-sale are quality instruments with a high degree of marketability and liquidity, with a credit rating from AAA to BBB (Fitch). The portfolio includes short-term and long-term debt securities with a fixed interest rate, which are issued by the governments of other foreign countries. Financial assets available-for-sale are denominated in EUR.

The structure of the financial assets available-for-sale is as follows:

| In thousands of KM | 31 December<br>2016 | 31 December<br>2015 |
|--------------------|---------------------|---------------------|
| Debt securities    | 4,986,018           | 6,096,823           |
| Accrued interest   | 39,811              | 49,049              |
| <b>TOTAL</b>       | <b>5,025,829</b>    | <b>6,145,872</b>    |

The average effective yield rate on financial assets available-for-sale amounted to 0.48% (2015: 0.76%).

Financial assets available-for-sale can be analysed on a geographical basis as follows:

|                    | 31 December 2016   |               | 31 December 2015   |               |
|--------------------|--------------------|---------------|--------------------|---------------|
|                    | In thousands of KM | %             | In thousands of KM | %             |
| <i>France</i>      | 1,136,535          | 22.61         | 953,567            | 15.52         |
| <i>Belgium</i>     | 1,011,011          | 20.12         | 589,354            | 9.59          |
| <i>Spain</i>       | 900,412            | 17.92         | 1,701,072          | 27.68         |
| <i>Italy</i>       | 585,423            | 11.64         | 1,363,912          | 22.18         |
| <i>Germany</i>     | 541,175            | 10.77         | 531,970            | 8.66          |
| <i>Austria</i>     | 438,424            | 8.72          | 341,098            | 5.55          |
| <i>Finland</i>     | 229,082            | 4.56          | 232,366            | 3.78          |
| <i>Netherlands</i> | 177,704            | 3.54          | 426,402            | 6.94          |
| <i>Slovakia</i>    | 6,063              | 0.12          | 6,131              | 0.10          |
| <b>TOTAL</b>       | <b>5,025,829</b>   | <b>100.00</b> | <b>6,145,872</b>   | <b>100.00</b> |

Movements in fair value of financial assets available-for-sale can be analysed as follows:

| In thousands of KM                                   | 2016             | 2015             |
|--|------------------|------------------|
| <b>Opening balance as of 1 January</b>               | <b>6,145,872</b> | <b>4,955,537</b> |
| Purchases during the year                            | 4,342,772        | 7,418,276        |
| Sales during the year                                | (330,016)        | (1,294,539)      |
| Interest income recognized during the year (Note 18) | 17,194           | 20,777           |
| Collected principal and interest                     | (5,203,667)      | (4,975,016)      |
| Fair value adjustment                                | 53,674           | 20,837           |
| <b>Closing balance as of 31 December</b>             | <b>5,025,829</b> | <b>6,145,872</b> |

Net realized gains from the sale of financial assets available-for-sale in 2016 amounted to KM 8,383 thousand (2015: KM 24,266 thousand).

## 7. MONETARY GOLD

The Bank holds monetary gold in a bank in Switzerland which is physically held in a vault at the Bank of England. The value of the monetary gold as of 31 December 2016 amounts to KM 205,102 thousand, representing 96,000.000 ounces of gold at KM 2,136 per ounce (2015: KM 182,315 thousand representing 96,000.000 ounces of gold at KM 1,899 per ounce).

## 7. MONETARY GOLD (CONTINUED)

Movements in fair value of monetary gold can be analysed as follows:

In thousands of KM

|   | 2016           | 2015           |
|---|----------------|----------------|
| <b>Opening balance as of 1 January</b>            | <b>182,315</b> | <b>182,750</b> |
| Purchases during the year                         | -              | -              |
| - Changes in prices of gold                       | 14,307         | (22,418)       |
| - Foreign exchange gains from conversion USD / KM | 8,480          | 21,983         |
| <b>Closing balance as of 31 December</b>          | <b>205,102</b> | <b>182,315</b> |

## 8. HELD-TO-MATURITY INVESTMENTS

All held-to-maturity investments are with credit rating from AAA to BBB (Fitch) and are denominated in EUR.

The structure of the held-to-maturity investments is presented as follows:

In thousands of KM

|                  | 31 December<br>2016 | 31 December<br>2015 |
|------------------|---------------------|---------------------|
| Debt securities  | 1,124,596           | 1,134,453           |
| Accrued interest | 7,732               | 7,738               |
| <b>TOTAL</b>     | <b>1,132,328</b>    | <b>1,142,191</b>    |

The average effective yield rate on held-to-maturity investments amounted to 1.01% (2015: 0.96%).

Held-to-maturity investments can be analysed on a geographical basis as follows:

|                    | 31 December 2016   |               | 31 December 2015   |               |
|--------------------|--------------------|---------------|--------------------|---------------|
|                    | In thousands of KM | %             | In thousands of KM | %             |
| <i>France</i>      | 321,083            | 28.36         | 322,089            | 28.20         |
| <i>Italy</i>       | 221,688            | 19.57         | 226,894            | 19.86         |
| <i>Belgium</i>     | 204,721            | 18.08         | 205,831            | 18.02         |
| <i>Finland</i>     | 181,263            | 16.01         | 181,877            | 15.92         |
| <i>Austria</i>     | 162,106            | 14.32         | 162,938            | 14.27         |
| <i>Netherlands</i> | 41,467             | 3.66          | 42,562             | 3.73          |
| <b>TOTAL</b>       | <b>1,132,328</b>   | <b>100.00</b> | <b>1,142,191</b>   | <b>100.00</b> |

Movements in held-to-maturity investments can be analysed as follows:

In thousands of KM

|  | 2016             | 2015             |
|--|------------------|------------------|
| <b>Opening balance as of 1 January</b>               | <b>1,142,191</b> | <b>428,560</b>   |
| Purchases during the year                            | -                | 720,508          |
| Interest income recognized during the year (Note 18) | 11,532           | 7,567            |
| Collected principal and interest                     | (21,395)         | (14,444)         |
| <b>Closing balance as of 31 December</b>             | <b>1,132,328</b> | <b>1,142,191</b> |

## 9. OTHER ASSETS

| In thousands of KM   | 31 December<br>2016 | 31 December<br>2015 |
|--|---------------------|---------------------|
| Prepaid expenses   | 1,306               | 1,080               |
| Receivables from domestic banks                              | 1,036               | 943                 |
| Numismatic collections                                       | 885                 | 772                 |
| Giro accounts  | 640                 | 252                 |
| Loans to employees   | 378                 | 518                 |
| Other miscellaneous assets                                   | 376                 | 387                 |
| Advances   | 5                   | 3                   |
| Receivables from employee based on domestic currency deficit | 600                 | 600                 |
| Less: Impairment of other receivables                        | (600)               | (600)               |
| <b>TOTAL</b>   | <b>4,626</b>        | <b>3,955</b>        |

As of 31 December 2016, prepaid expenses include expenditure of KM 141 thousand incurred on the production of coins (31 December 2015: KM 740 thousand incurred on the production of banknotes and coins). As explained in Note 3.13 such costs are initially deferred and subsequently amortized over a period of three years.

Other assets include receivable from employee in the amount of KM 600 thousand related to domestic currency deficit as at reporting dates. This receivable was fully impaired. This receivable is associated with the fraud executed by the employee in the vault of the Central Bank of Bosnia and Herzegovina, Sarajevo – Main Unit. The fraud was revealed on 8 December 2014.

## 10. PROPERTY, EQUIPMENT AND INTANGIBLE ASSETS

| In thousands of KM                                   | Software<br>and other<br>intangible<br>assets | Land<br>and<br>buildings | Equipment<br>and<br>furniture | Vehicles     | Other      | Assets under<br>construction | TOTAL         |
|--|---|--------------------------|-------------------------------|--------------|------------|------------------------------|---------------|
| <b>Cost</b>  |   |                          |                               |              |            |                              |               |
| <b>As at 1 January 2015</b>                          | 13,700  | 42,987                   | 24,089                        | 1,826        | 930        | 323                          | 83,855        |
| Additions  | 451   | 5                        | 311                           | 1            | 16         | 106                          | 890           |
| Write offs   | -   | -                        | (830)                         | -            | (2)        | -                            | (832)         |
| Transfers  | 68  | -                        | 246                           | -            | 1          | (315)                        | -             |
| <b>As at 31 December 2015</b>                        | <b>14,219</b>                                 | <b>42,992</b>            | <b>23,816</b>                 | <b>1,827</b> | <b>945</b> | <b>114</b>                   | <b>83,914</b> |
| Additions  | 147   | -                        | 800                           | -            | 9          | 1,808                        | 2,764         |
| Write offs   | (103)   | -                        | (2,040)                       | -            | (34)       | -                            | (2,177)       |
| Transfers  | -   | -                        | 48                            | -            | -          | (48)                         | -             |
| <b>As at 31 December 2016</b>                        | <b>14,263</b>                                 | <b>42,992</b>            | <b>22,624</b>                 | <b>1,827</b> | <b>920</b> | <b>1,874</b>                 | <b>84,500</b> |
| <b>Accumulated depreciation<br/>and amortization</b> |   |                          |                               |              |            |                              |               |
| <b>As at 1 January 2015</b>                          | 13,045  | 3,110                    | 19,327                        | 1,591        | 592        | -                            | 37,665        |
| Charge for the year                                  | 265   | 506                      | 1,331                         | 90           | 58         | -                            | 2,250         |
| Write offs   | -   | -                        | (828)                         | -            | (2)        | -                            | (830)         |
| <b>As at 31 December 2015</b>                        | <b>13,310</b>                                 | <b>3,616</b>             | <b>19,830</b>                 | <b>1,681</b> | <b>648</b> | <b>-</b>                     | <b>39,085</b> |
| Charge for the year                                  | 307   | 506                      | 1,189                         | 57           | 54         | -                            | 2,113         |
| Write offs   | (103)   | -                        | (2,037)                       | -            | (33)       | -                            | (2,173)       |
| <b>As at 31 December 2016</b>                        | <b>13,514</b>                                 | <b>4,122</b>             | <b>18,982</b>                 | <b>1,738</b> | <b>669</b> | <b>-</b>                     | <b>39,025</b> |
| <b>Net book value</b>                                |   |                          |                               |              |            |                              |               |
| <b>As at 1 January 2016</b>                          | 909   | 39,376                   | 3,986                         | 146          | 297        | 114                          | 44,828        |
| <b>As at 31 December 2016</b>                        | <b>749</b>                                    | <b>38,870</b>            | <b>3,642</b>                  | <b>89</b>    | <b>251</b> | <b>1,874</b>                 | <b>45,475</b> |

As at 31 of December 2016 and 2015, the Bank has no encumbrances over its property, equipment and intangible assets.

## 11. OTHER INVESTMENTS

The structure of other investments is as follows:

| In thousands of KM  | 31 December<br>2016 | 31 December<br>2015 |
|---|---------------------|---------------------|
| <i>Equity securities:</i>   |                     |                     |
| Shares in Bank for International Settlements (BIS), Basel (Note 17) | 27,803              | 27,803              |
| Shares in SWIFT   | 10                  | 10                  |
| <b>TOTAL</b>  | <b>27,813</b>       | <b>27,813</b>       |

Equity securities are composed of ordinary Bank for International Settlements (hereinafter: BIS) shares with a nominal value of 5,000 SDR per share (paid up at 25% of their nominal value). BIS and SWIFT shares represent unquoted equity instruments whose fair value cannot be reliably determined and therefore are carried at cost.

SWIFT shares are composed of two ordinary shares and their total value is KM 10 thousand.

During the year the Bank received dividend income from BIS in the amount of KM 562 thousand (2015: KM 586 thousand) (Note 21).

## 12. CURRENCY IN CIRCULATION

Currency in circulation can be analysed as follows:

| In thousands of KM  | 2016             | 2015             |
|---|------------------|------------------|
| <b>Currency placed into circulation - opening balance as of 1 January</b> | <b>3,499,468</b> | <b>3,210,508</b> |
| Increase in currency in circulation during the year                       | 567,336          | 288,960          |
| <b>Currency placed into circulation - balance as of 31 December</b>       | <b>4,066,804</b> | <b>3,499,468</b> |

Of the total currency placed into circulation of KM 4,066,804 thousand as at 31 December 2016, KM 605 thousand was placed into circulation outside of Bosnia and Herzegovina (2015: KM 605 thousand out of KM 3,499,468 thousand).

|              | Nominal value | 31 December 2016   |                          | 31 December 2015   |                          |
|--------------|---------------|--------------------|--------------------------|--------------------|--------------------------|
|              |               | Pieces             | Value in thousands of KM | Pieces             | Value in thousands of KM |
| Coins        | 0.05          | 58,005,994         | 2,900                    | 52,262,527         | 2,613                    |
| Coins        | 0.10          | 90,219,478         | 9,022                    | 83,943,760         | 8,394                    |
| Coins        | 0.20          | 65,465,345         | 13,093                   | 60,740,117         | 12,148                   |
| Coins        | 0.50          | 31,728,243         | 15,864                   | 29,558,189         | 14,779                   |
| Coins        | 1             | 44,751,826         | 44,752                   | 41,870,560         | 41,871                   |
| Coins        | 2             | 12,654,299         | 25,309                   | 11,578,832         | 23,158                   |
| Coins        | 5             | 9,212,158          | 46,061                   | 8,509,335          | 42,547                   |
| Banknotes    | 10            | 10,635,610         | 106,356                  | 9,894,614          | 98,946                   |
| Banknotes    | 20            | 8,483,902          | 169,678                  | 7,947,931          | 158,959                  |
| Banknotes    | 50            | 18,230,190         | 911,510                  | 16,590,165         | 829,508                  |
| Banknotes    | 100           | 19,475,164         | 1,947,515                | 17,141,506         | 1,714,150                |
| Banknotes    | 200           | 3,873,719          | 774,744                  | 2,761,975          | 552,395                  |
| <b>TOTAL</b> |               | <b>372,735,928</b> | <b>4,066,804</b>         | <b>342,799,511</b> | <b>3,499,468</b>         |

### 13. DEPOSITS FROM BANKS

The structure of deposits from banks is provided in the following table:

| In thousands of KM  | 31 December<br>2016 | 31 December<br>2015 |
|---|---------------------|---------------------|
| Deposits of local commercial banks                        | 4,268,467           | 4,063,249           |
| Reserve accounts of organizational units of the Bank      | 640                 | 252                 |
| Special deposit of local commercial banks – blocked funds | 36                  | 36                  |
| <b>TOTAL</b>  | <b>4,269,143</b>    | <b>4,063,537</b>    |

Deposits of local domestic commercial banks are placed in accordance with obligatory reserve requirements for those banks to meet obligations for settling debts and for the transactions between commercial banks and the Central Bank of Bosnia and Herzegovina. On 31 December 2016 the total amount of KM 4,268,467 thousand (2015: KM 4,063,249 thousand represented deposits of 24 banks (2015: 27 banks).

Interest on deposits from local commercial banks is calculated according to the Law on the Central Bank of Bosnia and Herzegovina which was not calculated in the period 01/01/2015-30/06/2016 and in the period 01/07/2016-31/12/2016 was calculated on the amount exceeding the required reserve. Calculation policy changes on interest rates on deposits placed by local commercial banks during the reporting periods are provided in Note 18.

Deposits from banks include negative accrued interest in the amount KM (376) thousand as at 31 December 2016 (31 December 2015: did not include accrued interest).

### 14. DEPOSITS FROM THE GOVERNMENT AND OTHER DEPOSITORS

The structure of deposits from the Government and other depositors is provided in the following table:

| In thousands of KM   | 31 December<br>2016 | 31 December<br>2015 |
|--|---------------------|---------------------|
| Deposits for the budget of BiH Institutions                    | 460,478             | 344,709             |
| Deposits of other governments and government institutions      | 77,940              | 105,137             |
| Deposits of public institutions                                | 51,968              | 51,743              |
| Deposit account under International Monetary Fund transactions | 6                   | 5                   |
| <b>TOTAL</b>   | <b>590,392</b>      | <b>501,594</b>      |

### 15. PROVISIONS FOR LIABILITIES AND CHARGES

Provisions for liabilities and charges relate to provisions for employees' severance payments and provisions for potential liabilities on litigations.

#### *Litigations*

The Bank is a defendant in several legal proceedings arising from its operations. The Bank contests these claims and based on legal advice considers that no other material liabilities will be incurred, except for the amount of KM 150 thousands already provided for (Note 23).

Movement in provisions for liabilities and charges is presented below:

| In thousands of KM                           | 2016         | 2015         |
|--|--------------|--------------|
| <b>Opening balance as of 1 January</b>       | <b>1,452</b> | <b>1,294</b> |
| Compensations paid                           | (60)         | (183)        |
| Net charge to the income statement (Note 22) | 69           | 341          |
| Provisions for employees' payments           | 1,461        | 1,452        |
| Provisions for litigations (Note 23)         | 150          | -            |
| <b>Closing balance as of 31 December</b>     | <b>1,611</b> | <b>1,452</b> |

## 16. OTHER LIABILITIES

The structure of other liabilities is presented in the following table:

| In thousands of KM  | 31 December<br>2016 | 31 December<br>2015 |
|---|---------------------|---------------------|
| Liabilities based on allocation of profit to the state budget (Note 24) | 8,437               | 18,827              |
| IMF Accounts No. 1 and 2 (Note 29)                                      | 1,711               | 1,095               |
| Suppliers   | 1,493               | 752                 |
| Liabilities to employees  | 943                 | 1,346               |
| Deferred income   | 416                 | 617                 |
| World Bank deposits   | 447                 | 232                 |
| Accrued expenses and other liabilities                                  | 229                 | 258                 |
| <b>TOTAL</b>  | <b>13,676</b>       | <b>23,127</b>       |

## 17. EQUITY AND RESERVES

The structure of equity is presented in the following table:

| In thousands of KM  | 31 December<br>2016 | 31 December<br>2015 |
|---|---------------------|---------------------|
| Initial capital   | 25,000              | 25,000              |
| General reserves (Retained earnings)                      | 537,892             | 532,267             |
| Other reserves  | 31,300              | 31,300              |
| Fair value reserves – financial assets available-for-sale | 111,597             | 66,307              |
| Fair value reserves – monetary gold                       | (38,357)            | (61,145)            |
| <b>TOTAL</b>  | <b>667,432</b>      | <b>593,729</b>      |

### Initial capital

Initial capital represents nominal capital paid in on 12 June 1998 in accordance with the Law on Central Bank of Bosnia and Herzegovina.

### General reserves (Retained earnings)

General reserves (Retained earnings) comprise accumulated undistributed profits of the Bank since the beginning of its operations on 11 August 1997.

### Other reserves

Other reserves relate to following:

- reserves from grants in the amount of KM 3,497 thousand, which relate to grants received in cash from the Council of Ministers of Bosnia and Herzegovina on 12 June 1998. The status of these reserves is regulated by the Decision of the Governing Board of the Central Bank of Bosnia and Herzegovina with the approval of the Presidency of Bosnia and Herzegovina. The right to utilise the reserves from grants fall within the competence of the Governing Board of the Central Bank of Bosnia and Herzegovina.
- amounts received in accordance with the Succession Agreement of the former Yugoslavia in the amount of KM 27,803 thousand and relates to shares in Bank for International Settlements Brussels (BIS), Basel (see also Note 11).

### Fair value reserves

Fair value reserves represent unrealized gains or losses incurred as a result of measurement of the financial assets available-for-sale and monetary gold.

**18. INTEREST INCOME AND EXPENSES**

| In thousands of KM   | For the year ended<br>31 December |                |
|--|-----------------------------------|----------------|
|  | 2016                              | 2015           |
| Interest income arising from:  |                                   |                |
| - financial assets available-for-sale (Note 6)                                     | 17,194                            | 20,777         |
| - held-to-maturity investments (Note 8)  | 11,532                            | 7,567          |
| - deposit with foreign banks   | 11                                | 128            |
| - other  | 3                                 | 3              |
|  | <b>28,740</b>                     | <b>28,475</b>  |
| Effects of negative interest rates from interest bearing financial assets from:    |                                   |                |
| - term deposits held with foreign banks  | (6,138)                           | -              |
| - demand deposits held with foreign banks  | (2,427)                           | (1,098)        |
|  | <b>(8,565)</b>                    | <b>(1,098)</b> |
| Effects of negative deposit interest rates on deposits from local commercial banks | <b>2,169</b>                      | -              |
| <br>   |                                   |                |
| <b>Net interest income</b>   | <b>22,344</b>                     | <b>27,377</b>  |

The base for calculation of interest on commercial banks' deposits includes the total deposits of commercial banks on reserve accounts during the settlement period, which consists of required reserve amounts and excess above the required reserves.

In the period 01/01/2015-30/06/2016 the base for calculation of the required reserve of commercial banks consisted of deposits and borrowings, except the borrowings received from non-residents and all funds placed by governments of entities into development projects.

Rates of deposits and borrowed funds which constituted the base for required reserve calculation in the period 01/01/2015-30/06/2016 were as follows:

|                                    | (in %) |
|------------------------------------|--------|
| Short-term deposits and borrowings | 10.00  |
| Long-term deposits and borrowings  | 7.00   |

Until 30 April 2015 the interest rate calculated on the required reserves is 70% of the rate based on weighted average of interest rates achieved by the Bank in the same period on deposits invested up to one month while the interest rate calculated on the amount exceeding the required reserves is 90% of the rate based on weighted average of interest rates achieved by the Bank in the same period on deposits invested up to one month. In the period 01/01/2015-30/06/2016 the policy of calculating fees on the required reserves and on the amount exceeding the required reserves to commercial banks has been amended in a way that the Bank will not calculate interest on those items if the Bank did not invest in deposits up to one month due to lack of opportunities to achieve positive interest rate on the market, or if, for any reason, the Bank achieved an average negative interest rate on deposits invested up to one month.

From 1 May 2015 the fee on required reserves was calculated as the average of EONIA recorded on the market less 10 basis points for the same period, or minimum zero, if the average of EONIA reduced by 10 basis points has a negative value, while the zero rate fee was calculated on the amount exceeding the required reserve.

From 1 July 2016 the base for the required reserve calculation for commercial banks consists of deposits and borrowings regardless of fund currency expressed. Also, the unique required reserve rate of 10% is established to be applied by the Bank on the base for the required reserve calculation.

**18. INTEREST INCOME AND EXPENSES (CONTINUED)**

The Bank does not calculate the fee on the required reserve amount while the fee on the amount exceeding the required reserve is calculated at the rate equal to 50% of the European Central Bank rate applied on commercial bank deposits.

Effects of negative interest rates from interest-bearing financial assets are the result of negative interest rates calculated on term deposits and current accounts that could not be avoided according to current market circumstances.

Effects of negative deposit interest rates on deposits from local commercial banks are the result of the negative interest rate on the amount exceeding the required reserve which amounted to (0.20%) in the period 01/07-31/12/2016.

**19. FEE AND COMMISSION INCOME AND EXPENSES**

| In thousands of KM   | For the year ended<br>31 December |              |
|--|-----------------------------------|--------------|
|  | 2016                              | 2015         |
| Fee and commission income:                                       |                                   |              |
| - from local commercial banks                                    | 9,592                             | 8,692        |
| - from services for the Government and other non-banking clients | 480                               | 496          |
|  | <b>10,072</b>                     | <b>9,188</b> |
| Fee and commission expenses:                                     |                                   |              |
| - transactions with foreign banks                                | (533)                             | (619)        |
|  | <b>(533)</b>                      | <b>(619)</b> |
| <b>Net fee and commission income</b>                             | <b>9,539</b>                      | <b>8,569</b> |

**20. NET FOREIGN EXCHANGE GAINS**

| In thousands of KM                         | For the year ended<br>31 December |            |
|--|-----------------------------------|------------|
|  | 2016                              | 2015       |
| Income from foreign exchange differences   | 1,078                             | 1,906      |
| Expenses from foreign exchange differences | (1,018)                           | (1,048)    |
| <b>Net gains</b>                           | <b>60</b>                         | <b>858</b> |

**21. OTHER INCOME**

| In thousands of KM        | For the year ended<br>31 December |            |
|---------------------------|-----------------------------------|------------|
|                           | 2016                              | 2015       |
| Dividend income (Note 11) | 562                               | 586        |
| Income from grants        | 218                               | 122        |
| Other income              | 791                               | 107        |
| <b>TOTAL</b>              | <b>1,571</b>                      | <b>815</b> |

**22. PERSONNEL EXPENSES**

| In thousands of KM                          | For the year ended<br>31 December |               |
|---|-----------------------------------|---------------|
|   | 2016                              | 2015          |
| Salaries                                    | 10,543                            | 11,375        |
| Taxes and contributions                     | 6,013                             | 6,516         |
| Other employee benefits                     | 2,304                             | 2,201         |
| Provisions for severance payments (Note 15) | 69                                | 341           |
| <b>TOTAL</b>                                | <b>18,929</b>                     | <b>20,433</b> |

Personnel costs include KM 3,541 thousand (2015: KM 3,775 thousand) of defined pension contributions paid into the public pension funds in Bosnia and Herzegovina. Contributions are calculated as percentage of the gross salary. As at 31 December 2016 the Bank had 361 employees (2015: 354 employees).

**23. ADMINISTRATIVE AND OTHER OPERATING EXPENSES**

| In thousands of KM  | For the year ended<br>31 December |              |
|---|-----------------------------------|--------------|
|   | 2016                              | 2015         |
| Maintenance costs   | 2,587                             | 2,340        |
| Expenses for production and design of banknotes and coins | 599                               | 1,563        |
| Other administrative and operating expenses               | 3,607                             | 3,921        |
| <b>TOTAL</b>  | <b>6,793</b>                      | <b>7,824</b> |

Other administrative and operating expenses include expenses related to provisions on litigations in the amount 150 thousand (2015: the Bank did not have expenses of provisions on litigations).

**24. PROFIT ALLOCATION**

The allocation of the net profit is carried out in accordance with the Law on the Central Bank of Bosnia and Herzegovina.

The provisions of the above mentioned Law define the criteria of the net profit allocation, according to which the Bank allocates 60% of the current profit to the account of the institution responsible for the Budget of Bosnia and Herzegovina, provided that the amount of the initial capital and general reserves (retained earnings) is equal or higher than 5.00% of the total monetary liabilities.

This ratio, before the profit allocation in 2016 amounted to 6.24% (2015: 6.75%). According to the Decision of the Governing Board 60% of the net profit for the financial year of 2016 in the amount of KM 8,437 thousand (2015: KM 18,827 thousand) was allocated to the state budget, and 40%, i.e. the amount of KM 5,625 thousand was allocated to the general reserves (retained earnings) of the Bank (2015: KM 12,551 thousand).

**2016**

**Before profit allocation**

|  |  |
|--|--|
| <b>Monetary liabilities (Currency in circulation and domestic deposits)</b>                    | (in thousands of KM)<br><b>8,926,339</b> |
| Initial capital and general reserves (retained earnings)                                       | 557,267                                  |
| <b>Ratio - initial capital and general reserves (retained earnings) / monetary liabilities</b> | <b>6.24%</b>                             |

**24. PROFIT ALLOCATION (CONTINUED)**

**Profit allocation**

|  |                      |
|--|----------------------|
|  | (in thousands of KM) |
| <b>Net profit before allocation</b>                          | <b>14,062</b>        |
| Allocation of profit to the state budget                     | 8,437                |
| Allocation of profit to general reserves (retained earnings) | 5,625                |

**After profit allocation**

|  |                      |
|--|----------------------|
|  | (in thousands of KM) |
| Initial capital and general reserves (retained earnings)                                       | 562,892              |
| <b>Ratio - Initial capital and general reserves (retained earnings) / monetary liabilities</b> | <b>6.31%</b>         |

**2015**

**Before profit allocation**

|  |                      |
|--|----------------------|
|  | (in thousands of KM) |
| <b>Monetary liabilities (Currency in circulation and domestic deposits)</b>                    | <b>8,064,599</b>     |
| Initial capital and general reserves (retained earnings)                                       | 544,716              |
| <b>Ratio - initial capital and general reserves (retained earnings) / monetary liabilities</b> | <b>6.75%</b>         |

**Profit allocation**

|  |                      |
|--|----------------------|
|  | (in thousands of KM) |
| <b>Net profit before allocation</b>                          | <b>31,378</b>        |
| Allocation of profit to the state budget                     | 18,827               |
| Allocation of profit to general reserves (retained earnings) | 12,551               |

**After profit allocation**

|  |                      |
|--|----------------------|
|  | (in thousands of KM) |
| Initial capital and general reserves (retained earnings)                                       | 557,267              |
| <b>Ratio - Initial capital and general reserves (retained earnings) / monetary liabilities</b> | <b>6.91%</b>         |

**25. CASH AND CASH EQUIVALENTS**

For the purposes of the cash flow statement, cash and cash equivalents comprise of:

| In thousands of KM  | 31 December<br>2016 | 31 December<br>2015 |
|---|---------------------|---------------------|
| Foreign currency deposits with maturity up to three months or less from the date of acquisition | 2,069,888           | -                   |
| Foreign currency demand deposits  | 705,065             | 1,003,635           |
| Foreign currency in cash  | 194,846             | 128,520             |
| Special Drawing Rights in the International Monetary Fund                                       | 2,642               | 3,778               |
| Giro accounts   | 640                 | 252                 |
| <b>TOTAL</b>  | <b>2,973,081</b>    | <b>1,136,185</b>    |

## 26. RELATED PARTY TRANSACTIONS

In the normal course of its operations, the Bank enters into transactions with related parties. Having in mind that the Bank has been established by a Legal Act passed by Parliamentary Assembly of Bosnia and Herzegovina and that the initial capital has been paid up by the Council of Ministers of Bosnia and Herzegovina, transactions performed as part of regular operations of the Bank with the state and state institutions represent related party transactions. In addition, the Bank considers that it has an immediate related party relationship with its key management personnel, close family members of key management personnel, and entities controlled, jointly controlled or significantly influenced by key management personnel and their close family members.

Transactions with the state and state institutions are disclosed in the following table:

### In thousands of KM

| 2016  | Exposure | Liabilities    | Income | Expenses |
|---|----------|----------------|--------|----------|
| State   | -        | 502,124        | -      | -        |
| <i>State institutions</i>                             |          |                |        |          |
| Indirect taxation authority of Bosnia and Herzegovina | -        | 22,839         | -      | -        |
| Deposit Insurance Agency                              | -        | 23,288         | -      | -        |
| <b>TOTAL</b>  | -        | <b>548,251</b> | -      | -        |

### In thousands of KM

| 2015  | Exposure | Liabilities    | Income | Expenses |
|---|----------|----------------|--------|----------|
| State   | -        | 412,719        | -      | -        |
| <i>State institutions</i>                             |          |                |        |          |
| Indirect taxation authority of Bosnia and Herzegovina | -        | 8,508          | -      | -        |
| Deposit Insurance Agency                              | -        | 18,972         | -      | -        |
| <b>TOTAL</b>  | -        | <b>440,199</b> | -      | -        |

### Remuneration of key management members

The total remuneration of the members of the key personnel (members of Management and Governing Board) in 2016 amounted to KM 898 thousand, out of which KM 562 thousand was related to salaries and other remuneration and KM 336 thousand to taxes and contributions (in 2015 out of total amount of KM 988 thousand the amount of KM 620 thousand was related to salaries and other remuneration and KM 368 thousand was related to taxes and contributions).

## **27. RISK MANAGEMENT**

The major financial risks to which the Bank is exposed are as follows:

- Liquidity risk
- Market risk
- Credit risk.

This note presents information about the Bank's exposure to each of the above risks, the Bank's objective, policies and procedures for measuring and managing risks.

Given that the primary purpose of the Bank is to preserve monetary stability in Bosnia and Herzegovina, its financial risk framework is different from the framework of commercial banks. The majority of financial risks in the Bank occur based on the management of foreign currency reserves and based on financial market operations.

The Bank seeks to ensure that strong and effective risk management and control system are in place for identifying, assessing, monitoring and managing risk exposures. Risk management and estimation of the level of acceptable risk is a continuous process and the integral element of the Bank's business strategy. By instruments of business policy and control mechanisms through the level of the Governing Board of the Bank, the Management, the Audit Committee and the Investment Committee of the Bank, completeness in risk management is provided. Holding foreign exchange reserves in convertible currency at fixed exchange rate arrangement, investing in short term deposits with fixed interest rate in foreign banks with high credit ratings and in quality securities are the basic principles of managing liquidity risk, foreign exchange risk, interest rate risk and credit risk.

### **27.1. Liquidity risk**

Liquidity risk refers to the possible difficulties in liquidating a portion of assets quickly, possibly in a situation where market conditions are unfavorable and also with adverse price movement.

Liquid assets are defined as those assets whose conversion into cash causes minimal transaction costs and whose value is the closest to market value.

Considering the need of guaranteeing the KM convertibility, the daily liquidity should be provided by the maturity adjustment of the Bank foreign exchange reserves.

The liquidity framework should match the forecasted potential liquidity needs with identified liquid instruments. The liquidity of each financial instrument eligible for investment must be duly considered before the investment in the instrument is made.

#### *Maturity analysis*

Tables below present the financial liabilities of the Bank as at 31 December 2016 and 2015 classified into relevant maturity groupings based on the remaining period from the reporting date to the contractual maturity date.

Currency in circulation has been classified in the maturity period within three months.

**27. RISK MANAGEMENT (CONTINUED)**

**27.1. Liquidity risk (continued)**

| 31 December 2016                                     |                   |                           |                      |                 |                                  |                  |
|--|-------------------|---------------------------|----------------------|-----------------|----------------------------------|------------------|
| In thousands of KM                                   | Up to 3<br>months | From 3 to<br>12<br>months | From 1 to<br>3 years | Over 3<br>years | Without<br>specified<br>maturity | Total            |
| Currency in circulation                              | 4,066,804         | -                         | -                    | -               | -                                | 4,066,804        |
| Deposits from banks                                  | 4,269,143         | -                         | -                    | -               | -                                | 4,269,143        |
| Deposits from the Government and other<br>depositors | 590,392           | -                         | -                    | -               | -                                | 590,392          |
| Other financial liabilities                          | 4,606             | 8,437                     | -                    | -               | -                                | 13,043           |
| <b>TOTAL FINANCIAL LIABILITIES</b>                   | <b>8,930,945</b>  | <b>8,437</b>              | <b>-</b>             | <b>-</b>        | <b>-</b>                         | <b>8,939,382</b> |

| 31 December 2015                                     |                   |                           |                      |                 |                                  |                  |
|--|-------------------|---------------------------|----------------------|-----------------|----------------------------------|------------------|
| In thousands of KM                                   | Up to 3<br>months | From 3 to<br>12<br>months | From 1 to<br>3 years | Over 3<br>years | Without<br>specified<br>maturity | Total            |
| Currency in circulation                              | 3,499,468         | -                         | -                    | -               | -                                | 3,499,468        |
| Deposits from banks                                  | 4,063,537         | 70                        | -                    | -               | -                                | 4,063,607        |
| Deposits from the Government and other<br>depositors | 501,594           | -                         | -                    | -               | -                                | 501,594          |
| Other financial liabilities                          | 3,431             | 18,827                    | -                    | -               | -                                | 22,258           |
| <b>TOTAL FINANCIAL LIABILITIES</b>                   | <b>8,068,030</b>  | <b>18,897</b>             | <b>-</b>             | <b>-</b>        | <b>-</b>                         | <b>8,086,927</b> |

## 27. RISK MANAGEMENT (CONTINUED)

### 27.2. Market risk

Market risk is the risk that changes in market prices, such as interest rates, equity prices and foreign exchange rates will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures with acceptable parameters, while optimising the return on risk.

#### 27.2.1. Foreign exchange risk

The Bank is exposed to currency risk through transactions in foreign currencies. This is the risk that the value of a financial instrument will fluctuate because of changes in foreign exchange rates. Foreign currency exposure arises from deposit and investment activities.

The control and management of the foreign exchange risk is based on the strict adherence to the provisions of the Law on the Central Bank of Bosnia and Herzegovina and the Guidelines of the Central Bank on investment of the foreign exchange reserves.

The above framework defines the limits for holding assets and liabilities in each foreign currency. The biggest part of monetary assets is held in EUR, and the maximum amount that can be held in other convertible currencies, subject to the changes in the market rate, must not exceed 50% of the total amount of the capital and the reserves of the Bank.

The Bank had the following foreign currency position as at 31 December 2016 and 31 December 2015.

#### 31 December 2016

| In thousands of KM   | EUR              | USD            | Other<br>foreign<br>currencies | KM                 | Total            |
|--|------------------|----------------|--------------------------------|--------------------|------------------|
| Foreign currency in cash                                       | 194,768          | 21             | 57                             | -                  | 194,846          |
| Deposits with foreign banks                                    | 2,964,617        | 4,286          | 1,494                          | -                  | 2,970,397        |
| Special Drawing Rights with the<br>International Monetary Fund | -                | -              | 2,642                          | -                  | 2,642            |
| Financial assets available-for-sale                            | 5,025,829        | -              | -                              | -                  | 5,025,829        |
| Monetary gold  | -                | 205,102        | -                              | -                  | 205,102          |
| Held-to-maturity investments                                   | 1,132,328        | -              | -                              | -                  | 1,132,328        |
| Other investments  | 10               | -              | -                              | 27,803             | 27,813           |
| Other financial assets   | -                | -              | -                              | 2,217              | 2,217            |
| <b>Total financial assets</b>                                  | <b>9,317,552</b> | <b>209,409</b> | <b>4,193</b>                   | <b>30,020</b>      | <b>9,561,174</b> |
| Currency in circulation  | -                | -              | -                              | 4,066,804          | 4,066,804        |
| Deposits from banks  | -                | -              | -                              | 4,269,143          | 4,269,143        |
| Deposits from the Government and other<br>depositors           | -                | -              | -                              | 590,392            | 590,392          |
| Other financial liabilities                                    | 483              | 3              | 39                             | 12,518             | 13,043           |
| <b>Total financial liabilities</b>                             | <b>483</b>       | <b>3</b>       | <b>39</b>                      | <b>8,938,857</b>   | <b>8,939,382</b> |
| <b>NET FOREIGN EXCHANGE POSITION</b>                           | <b>9,317,069</b> | <b>209,406</b> | <b>4,154</b>                   | <b>(8,908,837)</b> | <b>621,792</b>   |

**27. RISK MANAGEMENT (CONTINUED)**

**27.2. Market risk (continued)**

**27.2.1. Foreign exchange risk (continued)**

31 December 2015

| In thousands of KM   | EUR              | USD            | Other<br>foreign<br>currencies | KM                 | Total            |
|--|------------------|----------------|--------------------------------|--------------------|------------------|
| Foreign currency in cash                                       | 128,440          | 21             | 59                             |                    | 128,520          |
| Deposits with foreign banks                                    | 1,001,986        | 1,606          | 43                             | -                  | 1,003,635        |
| Special Drawing Rights with the<br>International Monetary Fund | -                | -              | 3,778                          | -                  | 3,778            |
| Financial assets available-for-sale                            | 6,145,872        | -              | -                              | -                  | 6,145,872        |
| Monetary gold  | -                | 182,315        | -                              | -                  | 182,315          |
| Held-to-maturity investments                                   | 1,142,191        | -              | -                              | -                  | 1,142,191        |
| Other investments  | 10               | -              | -                              | 27,803             | 27,813           |
| Other financial assets   | -                | -              | -                              | 1,876              | 1,876            |
| <b>Total financial assets</b>                                  | <b>8,418,499</b> | <b>183,942</b> | <b>3,880</b>                   | <b>29,679</b>      | <b>8,636,000</b> |
| Currency in circulation  | -                | -              | -                              | 3,499,468          | 3,499,468        |
| Deposits from banks  | -                | -              | -                              | 4,063,537          | 4,063,537        |
| Deposits from the Government and other<br>depositors           | -                | -              | -                              | 501,594            | 501,594          |
| Other financial liabilities                                    | 506              | 3              | 1                              | 21,748             | 22,258           |
| <b>Total financial liabilities</b>                             | <b>506</b>       | <b>3</b>       | <b>1</b>                       | <b>8,086,347</b>   | <b>8,086,857</b> |
| <b>NET FOREIGN EXCHANGE POSITION</b>                           | <b>8,417,993</b> | <b>183,939</b> | <b>3,879</b>                   | <b>(8,056,668)</b> | <b>549,143</b>   |

**27. RISK MANAGEMENT (CONTINUED)**

**27.2. Market risk (continued)**

**27.2.1.1. Foreign exchange risk - Sensitivity analysis**

The Bank is not exposed to EUR foreign currency risk due to currency board arrangement aligning KM to EUR at fixed exchange rate of EUR 1: KM 1.95583.

The sensitivity analysis includes outstanding foreign currency denominated monetary items at the statement of financial position date and indicates the effects of the assumed changes in foreign currency rates on the reported profit and equity. The table below provides an analysis of the Bank's main currency exposures. A positive number indicates an increase in income statement and increase in equity where the KM weakens i.e. strengthens against the relevant currency.

| <b>2016</b>                                    | <b>USD</b>    | <b>SDR</b> | <b>Other</b> |
|--|---------------|------------|--------------|
| In thousands of KM                             | +/- 3%        | +/- 2%     | +/- 2%       |
| <b>Foreign exchange rate risk (on P&amp;L)</b> | 129/(129)     | 53/(53)    | 30/(30)      |
|  |               |            |              |
| <b>2015</b>                                    | <b>USD</b>    | <b>SDR</b> | <b>Other</b> |
| In thousands of KM                             | +/- 3%        | +/- 2%     | +/- 2%       |
| <b>Foreign exchange rate risk (on P&amp;L)</b> | 49/(49)       | 76/(76)    | 2/(2)        |
|  |               |            |              |
| <b>2016</b>                                    | <b>USD</b>    | <b>SDR</b> | <b>Other</b> |
| In thousands of KM                             | +/- 3%        | +/- 2%     | +/- 2%       |
| <b>Foreign exchange rate risk (on Equity)</b>  | 6,153/(6,153) | 0/(0)      | 0/(0)        |
|  |               |            |              |
| <b>2015</b>                                    | <b>USD</b>    | <b>SDR</b> | <b>Other</b> |
| In thousands of KM                             | +/- 3%        | +/- 2%     | +/- 2%       |
| <b>Foreign exchange rate risk (on Equity)</b>  | 5,469/(5,469) | 0/(0)      | 0/(0)        |

**27. RISK MANAGEMENT (CONTINUED)**

**27.2. Market risk (continued)**

**27.2.2. Interest rate risk**

The Bank's exposure to market risk for changes in interest rates is concentrated in its investment portfolio. The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest earning assets and interest bearing liabilities mature or reprice at different time or in different amounts.

The Bank is exposed to interest rate risk through investment of foreign currency reserves. The Bank manages its investment portfolio with the aim to minimize interest rate risk. The investments bear different interest rates, depending on the time period of the investment, with the maximum term of investment being one year for deposits and ten years for securities.

The tables below summarize the Bank's exposure to interest rate risk at year-end.

| 31 December 2016   |                   |                           |                      |                 |                             |                  |
|--|-------------------|---------------------------|----------------------|-----------------|-----------------------------|------------------|
| In thousands of KM   | Up to 3<br>months | From 3<br>to 12<br>months | From 1 to<br>3 years | Over 3<br>Years | Non-<br>interest<br>bearing | Total            |
| Foreign currency in cash                                       | -                 | -                         | -                    | -               | 194,846                     | 194,846          |
| Deposits with foreign banks                                    | 2,776,632         | 195,444                   | -                    | -               | (1,679)                     | 2,970,397        |
| Special Drawing Rights with the<br>International Monetary Fund | 2,642             | -                         | -                    | -               | -                           | 2,642            |
| Available for sale financial assets                            | 2,097,594         | 2,888,424                 | -                    | -               | 39,811                      | 5,025,829        |
| Monetary gold  | -                 | -                         | -                    | -               | 205,102                     | 205,102          |
| Held-to-maturity investments                                   | 116,689           | 1,007,907                 | -                    | -               | 7,732                       | 1,132,328        |
| Other investments  | -                 | -                         | -                    | -               | 27,813                      | 27,813           |
| Other financial assets   | 37                | 111                       | 195                  | 61              | 1,813                       | 2,217            |
| <b>Total financial assets</b>                                  | <b>4,993,594</b>  | <b>4,091,886</b>          | <b>195</b>           | <b>61</b>       | <b>475,438</b>              | <b>9,561,174</b> |
| Currency in circulation  | -                 | -                         | -                    | -               | 4,066,804                   | 4,066,804        |
| Deposits from banks  | 2,039,880         | -                         | -                    | -               | 2,229,263                   | 4,269,143        |
| Deposits from the Government and other<br>depositors           | -                 | -                         | -                    | -               | 590,392                     | 590,392          |
| Other liabilities  | -                 | -                         | -                    | -               | 13,043                      | 13,043           |
| <b>Total financial liabilities</b>                             | <b>2,039,880</b>  | <b>-</b>                  | <b>-</b>             | <b>-</b>        | <b>6,899,502</b>            | <b>8,939,382</b> |
| <b>INTEREST RATE GAP</b>                                       | <b>2,953,714</b>  | <b>4,091,886</b>          | <b>195</b>           | <b>61</b>       | <b>(6,424,064)</b>          | <b>621,792</b>   |

**27. RISK MANAGEMENT (CONTINUED)**

**27.2. Market risk (continued)**

**27.2.2. Interest rate risk (continued)**

31 December 2015

| In thousands of KM   | Up to 3<br>months | From 3 to<br>12 months | From 1 to<br>3 years | Over 3<br>years | Non-<br>interest<br>bearing | Total            |
|--|-------------------|------------------------|----------------------|-----------------|-----------------------------|------------------|
| Foreign currency in cash                                       | -                 | -                      | -                    | -               | 128,520                     | 128,520          |
| Deposits with foreign banks                                    | 1,003,745         | -                      | -                    | -               | (110)                       | 1,003,635        |
| Special Drawing Rights with the<br>International Monetary Fund | 3,778             | -                      | -                    | -               | -                           | 3,778            |
| Financial assets available-for-sale                            | 2,748,514         | 3,348,309              | -                    | -               | 49,049                      | 6,145,872        |
| Monetary gold  | -                 | -                      | -                    | -               | 182,315                     | 182,315          |
| Held-to-maturity investments                                   | 120,759           | 1,013,693              | -                    | -               | 7,739                       | 1,142,191        |
| Other investments  | -                 | -                      | -                    | -               | 27,813                      | 27,813           |
| Other financial assets   | 38                | 114                    | 277                  | 133             | 1,314                       | 1,876            |
| <b>Total financial assets</b>                                  | <b>3,876,834</b>  | <b>4,362,116</b>       | <b>277</b>           | <b>133</b>      | <b>396,640</b>              | <b>8,636,000</b> |
| Currency in circulation  | -                 | -                      | -                    | -               | 3,499,468                   | 3,499,468        |
| Deposits from banks  | 1,508,789         | -                      | -                    | -               | 2,554,748                   | 4,063,537        |
| Deposits from the Government and other<br>depositors           | 5                 | -                      | -                    | -               | 501,589                     | 501,594          |
| Other financial liabilities                                    | -                 | -                      | -                    | -               | 22,258                      | 22,258           |
| <b>Total financial liabilities</b>                             | <b>1,508,794</b>  | <b>-</b>               | <b>-</b>             | <b>-</b>        | <b>6,578,063</b>            | <b>8,086,857</b> |
| <b>INTEREST RATE GAP</b>                                       | <b>2,368,040</b>  | <b>4,362,116</b>       | <b>277</b>           | <b>133</b>      | <b>(6,181,423)</b>          | <b>549,143</b>   |

**27. RISK MANAGEMENT (CONTINUED)**

**27.2. Market risk (continued)**

**27.2.2.1 Interest rate risk - Sensitivity analysis**

The sensitivity analyses below have been determined based on the exposure to interest rates for financial assets and financial liabilities at the statement of financial position date and the assumed change of interest rate taking place at the beginning of the financial year and held constant throughout the reporting period.

The table below provides a sensitivity analysis of the Bank's interest rate exposures in main currencies based on the sensitivity range of +10/-10bp (2015: +5/-5bp) depending on the currency (which reflects Bank's assessment of the possible change in interest rates). A positive number indicates an increase in income statement and increase in equity where the rates according to new scenario are higher, i.e. lower than as of reporting dates.

| <b>2016</b>                            | <b>KM</b>     | <b>EUR</b>      | <b>SDR</b> |
|--|---------------|-----------------|------------|
| In thousands of KM                     | +10/-10bp     | +10/-10bp       | +10/-10bp  |
| <b>Interest rate risk (on P&amp;L)</b> | (2,229)/2,229 | (14,322)/14,418 | 3/(3)      |

| <b>2015</b>                            | <b>KM</b> | <b>EUR</b>    | <b>SDR</b> |
|--|-----------|---------------|------------|
| In thousands of KM                     | +1/-1bp   | +5/-5bp       | +1/-1bp    |
| <b>Interest rate risk (on P&amp;L)</b> | (151)/151 | (8,211)/8,238 | 0/(0)      |

| <b>2016</b>                           | <b>KM</b> | <b>EUR</b> | <b>SDR</b> |
|---------------------------------------|-----------|------------|------------|
| In thousands of KM                    | +10/-10bp | +10/-10bp  | +10/-10bp  |
| <b>Interest rate risk (on equity)</b> | 0/0       | (658)/663  | 0/(0)      |

| <b>2015</b>                           | <b>KM</b> | <b>EUR</b> | <b>SDR</b> |
|---------------------------------------|-----------|------------|------------|
| In thousands of KM                    | +1/-1bp   | +5/-5bp    | +1/-1bp    |
| <b>Interest rate risk (on equity)</b> | 0/0       | (180)/181  | 0/(0)      |

## 27. RISK MANAGEMENT (CONTINUED)

### 27.3. Credit risk

Credit risk is the risk of financial loss to the Bank if counterparty to a financial instrument fails to meet its contractual obligation and rises principally from the Bank's deposits with other banks and investments into securities (foreign currency reserves). The management of this risk is performed through the selection of counterparties with sound credit ratings, by limiting the maturity, and by controlling the volume and the dynamics of investment. The credit ratings are continuously monitored on a daily basis.

For the funds recorded in off-balance sheet records, the Bank is not exposed to credit risk, as all the risk, which may result from the investments of these funds, is to be borne contractually by the owners of these funds (see also Note 29).

#### 27.3.1. Credit risk concentration

The Bank is exposed to credit risk through the financial statement items that meet the definition of its financial assets.

#### Maximum exposure to credit risk before collateral held or other credit enhancements

The following table shows the maximum exposure to credit risk by type of financial assets:

| In thousands of KM  | Maximum exposure    |                     |
|---|---------------------|---------------------|
|   | 31 December<br>2016 | 31 December<br>2015 |
| <b>Carrying amounts</b>                                     |                     |                     |
| Foreign currency in cash                                    | 194,846             | 128,520             |
| Deposits with foreign banks                                 | 2,970,397           | 1,003,635           |
| Special Drawing Rights with the International Monetary Fund | 2,642               | 3,778               |
| Financial assets available-for-sale                         | 5,025,829           | 6,145,872           |
| Monetary gold   | 205,102             | 182,315             |
| Held-to-maturity investments                                | 1,132,328           | 1,142,191           |
| Other investments   | 27,813              | 27,813              |
| Other financial assets                                      | 2,217               | 1,876               |
| <b>TOTAL</b>  | <b>9,561,174</b>    | <b>8,636,000</b>    |

The Bank does not hold any collateral or other credit enhancements to cover this credit risk as the Bank invests its assets with the counterparties that have the highest credit ratings.

As of 31 December 2016 the Bank does not have any assets that are either past due or impaired.

#### Concentration of credit risk

The deposits placed with foreign banks in total amounted to KM 2,970,397 thousand as at 31 December 2016 (2015: KM 1,003,635 thousand). The largest portion of these funds is invested in two foreign banks with individual exposures exceeding total equity and reserves of the Bank (2015: none of the foreign banks had individual exposures exceeding total equity and reserves of the Bank).

#### Individual credit risk concentration exceeding total capital and reserves of the Bank:

| Bank rating | 31 December 2016   |            | Bank rating | 31 December 2015   |            |
|-------------|--------------------|------------|-------------|--------------------|------------|
|             | In thousands of KM | % of total |             | In thousands of KM | % of total |
| AAA         | 918,072            | 30.91      | -           | -                  | -          |
| AAA         | 859,501            | 28.94      | -           | -                  | -          |

The largest individual risk exposure as at 31 December 2016 amounted to KM 918,072 thousand (2015: KM 412,022 thousand)

**27. RISK MANAGEMENT (CONTINUED)**

**27.3. Credit risk (continued)**

**27.3.1. Credit risk concentration (continued)**

**Concentration per credit rating**

The table below presents an analysis of the Bank's concentration per credit rating for its financial assets as at 31 December 2016 (in thousands of KM).

| Credit rating   | Foreign currency in cash | Deposits with foreign banks | Special Drawing Rights with the IMF | Financial assets available-for-sale | Monetary gold  | Held-to-maturity investments | Other investments | Other financial assets | TOTAL            |
|-----------------|--------------------------|-----------------------------|-------------------------------------|-------------------------------------|----------------|------------------------------|-------------------|------------------------|------------------|
| AAA             | -                        | 2,363,620                   | -                                   | 718,879                             | -              | 41,467                       | -                 | -                      | 3,123,966        |
| AA+             | -                        | -                           | -                                   | 667,506                             | -              | 343,369                      | -                 | -                      | 1,010,875        |
| AA              | -                        | 78,073                      | -                                   | 1,136,535                           | -              | 321,083                      | -                 | -                      | 1,535,691        |
| AA-             | -                        | 390,047                     | -                                   | 1,011,011                           | -              | 204,721                      | -                 | -                      | 1,605,779        |
| A+              | -                        | -                           | -                                   | 6,063                               | -              | -                            | -                 | -                      | 6,063            |
| A               | -                        | -                           | -                                   | -                                   | -              | -                            | -                 | -                      | -                |
| A-              | -                        | 134,477                     | -                                   | -                                   | -              | -                            | -                 | -                      | 134,477          |
| II <sup>1</sup> | -                        | 4,180                       | 2,642                               | -                                   | 205,102        | -                            | 27,813            | -                      | 239,737          |
| BBB+            | -                        | -                           | -                                   | 900,412                             | -              | -                            | -                 | -                      | 900,412          |
| BBB             | -                        | -                           | -                                   | 585,423                             | -              | 221,688                      | -                 | -                      | 807,111          |
| Unrated         | 194,846                  | -                           | -                                   | -                                   | -              | -                            | -                 | 2,217                  | 197,063          |
| <b>TOTAL</b>    | <b>194,846</b>           | <b>2,970,397</b>            | <b>2,642</b>                        | <b>5,025,829</b>                    | <b>205,102</b> | <b>1,132,328</b>             | <b>27,813</b>     | <b>2,217</b>           | <b>9,561,174</b> |

The table below presents an analysis of the Bank's concentration per credit rating for its financial assets as at 31 December 2015 (in thousands of KM).

| Credit rating   | Foreign currency in cash | Deposits with foreign banks | Special Drawing Rights with the IMF | Financial assets available-for-sale | Monetary gold  | Held-to-maturity investments | Other investments | Other financial assets | TOTAL            |
|-----------------|--------------------------|-----------------------------|-------------------------------------|-------------------------------------|----------------|------------------------------|-------------------|------------------------|------------------|
| AAA             | -                        | 783,544                     | -                                   | 1,190,738                           | -              | 224,439                      | -                 | -                      | 2,198,721        |
| AA+             | -                        | -                           | -                                   | 341,098                             | -              | 162,938                      | -                 | -                      | 504,036          |
| AA              | -                        | -                           | -                                   | 1,542,920                           | -              | 527,920                      | -                 | -                      | 2,070,840        |
| AA-             | -                        | -                           | -                                   | -                                   | -              | -                            | -                 | -                      | -                |
| A+              | -                        | -                           | -                                   | 6,131                               | -              | -                            | -                 | -                      | 6,131            |
| A               | -                        | -                           | -                                   | -                                   | -              | -                            | -                 | -                      | -                |
| A-              | -                        | 208,750                     | -                                   | -                                   | -              | -                            | -                 | -                      | 208,750          |
| II <sup>2</sup> | -                        | 1,531                       | 3,778                               | -                                   | 182,315        | -                            | 27,813            | -                      | 215,437          |
| BBB+            | -                        | 9,810                       | -                                   | 1,701,072                           | -              | -                            | -                 | -                      | 1,710,882        |
| BBB             | -                        | -                           | -                                   | 1,363,913                           | -              | 226,894                      | -                 | -                      | 1,590,807        |
| Unrated         | 128,520                  | -                           | -                                   | -                                   | -              | -                            | -                 | 1,876                  | 130,396          |
| <b>TOTAL</b>    | <b>128,520</b>           | <b>1,003,635</b>            | <b>3,778</b>                        | <b>6,145,872</b>                    | <b>182,315</b> | <b>1,142,191</b>             | <b>27,813</b>     | <b>1,876</b>           | <b>8,636,000</b> |

<sup>1</sup> International institutions

<sup>2</sup> International institutions

**27. RISK MANAGEMENT (CONTINUED)**

**27.3. Credit risk (continued)**

**27.3.1. Credit risk concentration (continued)**

**Geographical concentration**

The following table provides the information about geographical concentration of Bank's financial assets as at 31 December 2016.

| In thousands of KM                  | EU countries     | Non-EU member countries | Bosnia and Herzegovina | Total            |
|-------------------------------------|------------------|-------------------------|------------------------|------------------|
| Foreign currency in cash            | -                | -                       | 194,846                | 194,846          |
| Deposits with foreign banks         | 2,380,169        | 590,228                 | -                      | 2,970,397        |
| SDR with the IMF                    | -                | 2,642                   | -                      | 2,642            |
| Available-for-sale financial assets | 5,025,829        | -                       | -                      | 5,025,829        |
| Monetary gold                       | -                | 205,102                 | -                      | 205,102          |
| Held-to-maturity investments        | 1,132,328        | -                       | -                      | 1,132,328        |
| Other investments                   | 10               | 27,803                  | -                      | 27,813           |
| Other financial assets              | -                | -                       | 2,217                  | 2,217            |
| <b>31 December 2016</b>             | <b>8,538,336</b> | <b>825,775</b>          | <b>197,063</b>         | <b>9,561,174</b> |
| <b>31 December 2015</b>             | <b>8,290,177</b> | <b>215,427</b>          | <b>130,396</b>         | <b>8,636,000</b> |

**28. FAIR VALUE MEASUREMENT**

**28.1 Fair value of the Bank's financial assets and financial liabilities that are measured at fair value on a recurring basis**

Some of the Bank's financial assets and financial liabilities are measured at fair value at the end of each reporting period. The following table gives information about how the fair values of these financial assets and financial liabilities are determined (in particular, the valuation technique(s) and inputs used).

| Financial assets /<br>financial liabilities            | Fair value as at   |  | Fair value<br>hierarchy | Valuation technique(s)<br>and key input(s)   |
|--|--|--|-------------------------|--|
|  | 31 December 2016   | 31 December 2015   |                         |  |
| 1) Financial assets available for<br>sale (see Note 6) | Listed debt securities on stock<br>exchanges in other countries: <ul style="list-style-type: none"> <li>• France – KM 1,136,535 thousand</li> <li>• Belgium – KM 1,011,011 thousand</li> <li>• Spain – KM 900,412 thousand</li> <li>• Italy – KM 585,423 thousand</li> <li>• Germany – KM 541,175 thousand</li> <li>• Austria – KM 438,424 thousand</li> <li>• Finland – KM 229,082 thousand</li> <li>• Netherlands – KM 177,704 thousand</li> <li>• Slovakia – KM 6,063 thousand</li> </ul> | Listed debt securities on stock<br>exchanges in other countries: <ul style="list-style-type: none"> <li>• France – KM 953,567 thousand</li> <li>• Belgium – KM 589,354 thousand</li> <li>• Spain – KM 1,701,072 thousand</li> <li>• Italy – KM 1,363,912 thousand</li> <li>• Germany – KM 531,970 thousand</li> <li>• Austria – KM 341,098 thousand</li> <li>• Finland – KM 232,366 thousand</li> <li>• Netherlands – KM 426,402 thousand</li> <li>• Slovakia – KM 6,131 thousand</li> </ul> | Level 2                 | Consensus prices - the<br>(weighted) average of<br>quotes from multiple<br>subscribers who each<br>submit quotes to the<br>pricing service |
| 2) Monetary gold (see Note 7)                          | Listed precious metals on stock<br>exchanges in other countries: <ul style="list-style-type: none"> <li>• Switzerland – KM 205,102 thousand</li> </ul>   | Listed precious metals on stock<br>exchanges in other countries: <ul style="list-style-type: none"> <li>• Switzerland – KM 182,315 thousand</li> </ul>   | Level 1                 | Quoted bid prices in an<br>active market.  |

**28. FAIR VALUE MEASUREMENT (CONTINUED)**

**28.2 Fair value of the Bank's financial assets and financial liabilities that are not measured at fair value on a recurring basis (but fair value disclosures are required)**

| In thousands of KM  | 31 December 2016 |            | 31 December 2015 |            |
|---|------------------|------------|------------------|------------|
|   | Carrying amount  | Fair value | Carrying amount  | Fair value |
| <b>Financial assets</b>                                       |                  |            |                  |            |
| <i>Loans and receivables</i>                                  |                  |            |                  |            |
| - Foreign currency in cash                                    | 194,846          | 194,846    | 128,520          | 128,520    |
| - Deposits with foreign banks                                 | 2,970,397        | 2,963,885  | 1,003,635        | 1,001,637  |
| - Special Drawing Rights with the International Monetary Fund | 2,642            | 2,642      | 3,778            | 3,778      |
| <i>Held-to-maturity investments</i>                           |                  |            |                  |            |
| - Held-to-maturity investments                                | 1,132,328        | 1,185,052  | 1,142,191        | 1,157,370  |
| <i>Available-for-sale financial assets</i>                    |                  |            |                  |            |
| - Available-for-sale financial assets                         | 5,025,829        | 5,025,829  | 6,145,872        | 6,145,872  |
| - Monetary gold   | 205,102          | 205,102    | 182,315          | 182,315    |
| - Other investments   | 27,813           | 27,813     | 27,813           | 27,813     |
| - Other financial assets                                      | 2,217            | 2,217      | 1,876            | 1,876      |
| <b>Financial liabilities</b>                                  |                  |            |                  |            |
| <i>Financial liabilities held at amortized cost:</i>          |                  |            |                  |            |
| - Currency in circulation                                     | 4,066,804        | 4,066,804  | 3,499,468        | 3,499,468  |
| - Deposits from banks   | 4,269,143        | 4,261,731  | 4,063,537        | 4,056,286  |
| - Deposits from the Government and other depositors           | 590,392          | 589,367    | 501,594          | 500,699    |
| - Other financial liabilities                                 | 13,043           | 13,043     | 22,258           | 22,258     |

| In thousands of KM                                   | Fair value hierarchy as at 31 December 2016 |                  |         |                  |
|--|---|------------------|---------|------------------|
|  | Level 1                                     | Level 2          | Level 3 | Total            |
| <b>Financial assets</b>                              |   |                  |         |                  |
| <i>Loans and receivables:</i>                        |   |                  |         |                  |
| - Deposits with foreign banks                        | -   | 2,963,885        | -       | 2,963,885        |
| - Held-to-maturity investments                       | -   | 1,185,052        | -       | 1,185,052        |
|  | -   | <b>4,148,937</b> | -       | <b>4,148,937</b> |
| <b>Financial liabilities</b>                         |   |                  |         |                  |
| <i>Financial liabilities held at amortized cost:</i> |   |                  |         |                  |
| - Deposits from banks                                | -   | 4,261,731        | -       | 4,261,731        |
| - Deposits from the Government and other depositors  | -   | 589,367          | -       | 589,367          |
|  | -   | <b>4,851,098</b> | -       | <b>4,851,098</b> |

**28. FAIR VALUE MEASUREMENT (CONTINUED)**

**28.2 Fair value of the Bank's financial assets and financial liabilities that are not measured at fair value on a recurring basis (but fair value disclosures are required) (continued)**

In thousands of KM

|  | Fair value hierarchy as at 31 December 2015 |                  |         |                  |
|--|---|------------------|---------|------------------|
|  | Level 1                                     | Level 2          | Level 3 | Total            |
| <b>Financial assets</b>                              |   |                  |         |                  |
| <i>Loans and receivables:</i>                        |   |                  |         |                  |
| - Deposits with foreign banks                        | -   | 1,001,637        | -       | 1,001,637        |
| - Held-to-maturity investments                       | -   | 1,157,370        | -       | 1,157,370        |
|  | -   | <b>2,159,007</b> | -       | <b>2,159,007</b> |
| <b>Financial liabilities</b>                         |   |                  |         |                  |
| <i>Financial liabilities held at amortized cost:</i> |   |                  |         |                  |
| - Deposits from banks                                | -   | 4,056,286        | -       | 4,056,286        |
| - Deposits from the Government and other depositors  | -   | 500,699          | -       | 500,699          |
|  | -   | <b>4,556,985</b> | -       | <b>4,556,985</b> |

The Management consider that the carrying amounts of foreign currency in cash, Special Drawing Rights with the International Monetary Fund, other financial assets, currency in circulation and other financial liabilities recognized in the financial statements approximate their fair values.

As at 31 December 2016 and 2015, available-for-sale securities include Bank for International Settlement (BIS) shares with a value of KM 27,803 thousand and SWIFT shares with a value of KM 10 thousand for which fair value cannot be reliably determined and therefore they are carried at cost.

The fair values of the financial assets and financial liabilities included in Level 2 category above have been determined in accordance with generally accepted pricing models based on a discounted cash flow analysis, with the most significant inputs being the discount rate that reflects the credit risk of counterparties. As discount rate, the Bank has used weighted average interest rate on corporate deposits for whole banking market in BiH.

**29. OFF-BALANCE SHEET ITEMS**

The Bank maintains certain accounts in foreign currencies related to agreements concluded between the governments of Bosnia and Herzegovina and foreign governments and financial organizations. As these accounts do not represent either assets or liabilities of the Central Bank of Bosnia and Herzegovina, they have not been included within the Bank's statement of financial position.

Off-balance sheet items also include foreign currency accounts of the state institutions and agencies, as well as of commercial banks, for which the Bank acts as an agent.

**29. OFF-BALANCE SHEET ITEMS (CONTINUED)**

Off-balance sheet items consist of:

| In thousands of KM  | 31 December<br>2016 | 31 December<br>2015 |
|---|---------------------|---------------------|
| <b>Third party securities and funds held with foreign banks</b>                             | <b>356,294</b>      | <b>308,646</b>      |
| Deposits of USAID   | 2,539               | 2,256               |
| <b>Deposits of non-residents</b>  | <b>2,539</b>        | <b>2,256</b>        |
| Deposits of the Council of Ministers of BiH   | 20,941              | 18,661              |
| <i>Deposits of the Council of Ministers of BiH on the basis of succession</i>               | 39                  | 35                  |
| <i>Deposits of the Council of Ministers of BiH regarding the servicing of foreign debt</i>  | 7,943               | 6,414               |
| <i>Deposits of the Council of Ministers of BiH regarding the Budget of BiH institutions</i> | 874                 | 6,422               |
| <i>Other deposits of the Council of Ministers of BiH</i>                                    | 12,085              | 5,790               |
| Deposits of other residents   | 7,131               | 6,069               |
| <i>Deposits - Retirement allowance from Germany</i>   | 375                 | -                   |
| <i>Deposit accounts of banks</i>  | 6,756               | 6,069               |
| <b>Deposits of residents</b>  | <b>28,072</b>       | <b>24,730</b>       |
| Investments related to securities – Deposit Insurance Agency                                | 325,683             | 281,660             |
| <b>Investments of residents related to securities</b>                                       | <b>325,683</b>      | <b>281,660</b>      |
| <b>Liability for third party securities and funds</b>                                       | <b>356,294</b>      | <b>308,646</b>      |

**USAID Deposits**

On the basis of the Agreement regarding financial assistance between Bosnia and Herzegovina and the United States of America for the financing of the reconstruction, special interest bearing accounts have been opened with the Bank of America. The Bank does not charge and does not collect any interest or fees on these accounts.

**Residents' investments related to securities**

The Bank enabled the Deposit Insurance Agency of the Bosnia and Herzegovina to invest in securities by opening cash and custodian accounts in the name of the Bank and the Deposit Insurance Agency of the Bosnia and Herzegovina. All transactions on the accounts are performed between the Deposit Insurance Agency of the Bosnia and Herzegovina and the Asset Manager. The Bank does not charge any interest or fees on such accounts.

**Bosnia and Herzegovina membership in the IMF**

As depositary for BiH membership in the IMF, the Central Bank of Bosnia and Herzegovina maintains the IMF No. 1 and 2 accounts and provides a custodian service for the BiH Promissory Notes issued to support IMF membership and repurchase obligations. The Bank holds SDRs as part of its foreign exchange reserve management function. As fiscal agent, the Bank acts on behalf of the BiH in dealing with the IMF but does not have any responsibility for assets and liabilities related to the membership.

**29. OFF-BALANCE SHEET ITEMS (CONTINUED)**

The following consolidated position provides a summary of the BiH position with the IMF:

**Consolidated position of BiH membership in the IMF as at 31 December 2016**

(In thousands of KM)

|   |                  |                  |
|---|------------------|------------------|
| <b>Assets</b>   |                  |                  |
| Quota   | 661,501          |                  |
| SDR holdings  | 2,641            |                  |
| Accrued interest on SDR holdings  | 1                |                  |
| <b>Total assets</b>   | <b>664,143</b>   |                  |
| <b>Liabilities</b>  |                  |                  |
| IMF No. 1 account (Note 16)   |                  | 1,654            |
| IMF No. 2 account (Note 16)   |                  | 57               |
| Securities  |                  | 1,687,755        |
| Accounts of payable charges   |                  | 2,157            |
| SDR allocation  |                  | 401,306          |
| Accrued interest on SDR allocation  |                  | 144              |
| <b>Total liabilities</b>  |                  | <b>2,093,073</b> |
| <b>Net member position with the IMF</b>   |                  |                  |
| BiH obligations to the IMF arising principally from repurchase and currency valuation adjustments | 1,428,930        |                  |
| <b>Net member position</b>  | <b>1,428,930</b> |                  |
|   | <b>2,093,073</b> | <b>2,093,073</b> |
| <b>Total consolidated position - assets and liabilities</b>                                       | <b>2,093,073</b> | <b>2,093,073</b> |
| IMF No. 1 account   | (1,654)          | (1,654)          |
| IMF No. 2 account   | (57)             | (57)             |
| <b>Total gross position of BiH with the IMF - assets and liabilities</b>                          | <b>2,091,362</b> | <b>2,091,362</b> |

SDR holdings, accrued interest on SDR holdings, IMF No. 1 account and IMF No. 2 account reflect accounts held on the statement of financial position of the Bank.

For the consolidated position of Bosnia and Herzegovina with the IMF, the gross position of the BiH is increased by the IMF No. 1 and 2 accounts.

**29. OFF-BALANCE SHEET ITEMS (CONTINUED)**

**Consolidated position of BiH membership in the IMF as at 31 December 2015**

(In thousands of KM)

| <b>Assets</b>   |  |                  |                  |
|---|--|------------------|------------------|
| Quota   |  | 420,964          |                  |
| SDR holdings  |  | 3,778            |                  |
| Accrued interest on SDR holdings  |  | -                |                  |
| <b>Total assets</b>   |  | <b>424,742</b>   |                  |
| <b>Liabilities</b>  |  |                  |                  |
| IMF No. 1 account (Note 16)   |  |                  | 1,058            |
| IMF No. 2 account (Note 16)   |  |                  | 37               |
| Securities  |  |                  | 1,456,417        |
| Accounts of payable charges   |  |                  | 1,843            |
| SDR allocation  |  |                  | 400,516          |
| Accrued interest on SDR allocation  |  |                  | 34               |
| <b>Total liabilities</b>  |  |                  | <b>1,859,905</b> |
| <b>Net member position with the IMF</b>   |  |                  |                  |
| BiH obligations to the IMF arising principally from repurchase and currency valuation adjustments |  | 1,435,163        |                  |
| <b>Net member position</b>  |  | <b>1,435,163</b> |                  |
|   |  | <b>1,859,905</b> | <b>1,859,905</b> |
| <b>Total consolidated position - assets and liabilities</b>                                       |  |                  |                  |
| IMF No. 1 account   |  | (1,058)          | (1,058)          |
| IMF No. 2 account   |  | (37)             | (37)             |
| <b>Total gross position of BH with the IMF - assets and liabilities</b>                           |  | <b>1,858,810</b> | <b>1,858,810</b> |

**30. CURRENCY BOARD ARRANGEMENT**

The Law on the Central Bank of Bosnia and Herzegovina requires that the aggregate amount of its monetary liabilities shall at no time exceed its net foreign exchange reserves.

Details of compliance with the rule are as follows:

| In thousands of KM   | 31 December<br>2016 | 31 December<br>2015 |
|--|---------------------|---------------------|
| <b>Foreign assets</b>  | <b>9,531,144</b>    | <b>8,606,311</b>    |
| Liabilities to non-residents   | 2,158               | 1,327               |
| <b>Net foreign exchange reserves (foreign assets minus liabilities to non-residents)</b> | <b>9,528,986</b>    | <b>8,604,984</b>    |
| <b>Monetary liabilities</b>  | <b>8,926,339</b>    | <b>8,064,599</b>    |
| <b>Net foreign assets (net foreign exchange reserves minus monetary liabilities)</b>     | <b>602,647</b>      | <b>540,385</b>      |

The monetary liabilities of the Bank, according to the Law on the Central Bank of Bosnia and Herzegovina, consist of currency in circulation and the domestic deposits from banks and other residents.

### 31. DOMESTIC PAYMENT AND SETTLEMENT SYSTEM

Pursuant to the law on the Central Bank of Bosnia and Herzegovina the Bank is responsible for the establishment and maintenance of domestic payment and settlement systems. The Bank has established two settlement systems from January 2001 in order to facilitate efficient settlement of domestic interbank payment transactions: Real Time Gross Settlement System („RTGS“) and Giro Clearing System („GCS“).

#### **Credit risk**

RTGS enables participants, i.e. the Bank and licensed commercial banks, to effect individual and prompt settlement of one by one (gross) payment by crediting and debiting settlement accounts held with the Central Bank in domestic currency. Through GCS the Bank provides clearing services arising from transmitted payment orders in accordance with the principle of multilateral clearing.

Each participant in the payment systems is obliged to cover its settlement account held with the Bank prior to settlement of payment orders and must meet certain technical requirements.

Pursuant to the role of the Bank as defined by the Law on the Central Bank of Bosnia and Herzegovina, the Bank does not provide any credit to RTGS and GCS participants which would provide liquidity to the system in any form.

#### **Operational risk**

With the aim of minimising operational risk within the domestic payment and settlement system, operating rules for RTGS and GCS have been issued, which define minimum security standards for operation of the systems.

Relevant security objectives, policies and procedures aim to ensure security measures and features. The computer systems and the networks are operated according to established objectives and policies. The security objectives and policies are reviewed periodically. Each direct participant is also required to have appropriate security measures and controls for processing payments.

The Bank has defined the following Contingency Settlement Procedures:

- **Contingency plans and measures:** the Bank has defined contingency measures in order to ensure continuity of reliable, correct and lawful operation of the payment and settlement systems in the event of disruption to the regular payment and settlement system, or other contingency events;
- **Backup location:** To support the primary location for the payment systems (RTGS, GCS and SWIFT) with redundant systems (if case of system falling, switching to another one on the primary location is done), the Bank has also established functional DR (Disaster Recovery) system located in Main Bank of Republika Srpska of the Central Bank of Bosnia and Herzegovina in Banja Luka.

Management of the Bank believes that the system has sufficient capacity to maintain operational reliability, which has never been jeopardised since the implementation of the system.

### 32. POST-REPORTING DATE EVENTS

No adjusting or significant non-adjusting events have occurred between the 31 December 2016 and the date of authorization of these financial statements.