

**CENTRAL BANK OF BOSNIA AND HERZEGOVINA**

**CONDENSED INTERIM FINANCIAL STATEMENTS  
FOR THE PERIOD ENDED 31 MARCH 2018**

**(unaudited)**

**In accordance with the requirements of IAS 34**

**Sarajevo, 24 April 2018**

**CENTRAL BANK OF BOSNIA AND HERZEGOVINA**  
*Condensed interim financial statements for the period ended 31 March 2018*

**Contents**

	<b>Page</b>
<b>Financial statements</b>	
Statement of profit or loss	1
Statement of comprehensive income	2
Statement of financial position	3
Statement of changes in equity	4
Statement of cash flows	5
Notes to the condensed interim financial statements	6 - 26

**CENTRAL BANK OF BOSNIA AND HERZEGOVINA**  
Condensed interim financial statements for the period ended 31 March 2018

**STATEMENT OF PROFIT OR LOSS**

*For the period*

(unaudited) (in thousands of KM)	Note	01/01- 31/03/2018 <sup>(1)</sup>	01/01 – 31/03/2017
Interest income		7,145	7,422
Effects of negative interest rates from interest-bearing financial assets		(2,596)	(2,947)
Effects of negative deposit interest rates on deposits from local commercial banks		1,398	1,041
<b>NET INTEREST INCOME</b>	<b>5</b>	<b>5,947</b>	<b>5,516</b>
Fee and commission income		4,053	3,025
Fee and commission expense		(162)	(128)
<b>NET FEE AND COMMISSION INCOME</b>	<b>6</b>	<b>3,891</b>	<b>2,897</b>
Net realised gains from sale of financial assets measured at fair value through other comprehensive income (FVOCI)		233	-
Net (losses) from expected credit losses (ECL) on financial assets	7	(670)	-
Net foreign exchange (losses)	8	(216)	(48)
Other income		462	136
<b>OPERATING INCOME</b>		<b>9,647</b>	<b>8,501</b>
Personnel expenses		(4,210)	(4,091)
Administrative and other operating expenses	9	(2,059)	(1,499)
Depreciation and amortisation		(523)	(484)
<b>OPERATING EXPENSES</b>		<b>(6,792)</b>	<b>(6,074)</b>
<b>NET PROFIT FOR THE PERIOD</b>		<b>2,855</b>	<b>2,427</b>

The accompanying notes on pages 6 to 26 are the integral parts of these condensed interim financial statements.

*(1) Statement of profit or loss for the period ended on 31 March 2018 reflects adoption of IFRS 9 from 1 January 2018. For additional information on IFRS 9 adoption see Notes 2 and 4 of these unaudited condensed interim financial statements. Comparative financial information has not been restated.*

## STATEMENT OF COMPREHENSIVE INCOME

*For the period*

(unaudited) (in thousands of KM)

	01/01/- 31/03/2018 <sup>(1)</sup>	01/01/- 31/03/2017
<b>NET PROFIT FOR THE PERIOD</b>	<b>2,855</b>	<b>2,427</b>
<b>Other comprehensive income</b>		
<i>Items that may be reclassified subsequently to the statement of profit or loss:</i>		
Financial assets available-for-sale		
Net changes in fair value during the period	-	(28,071)
Reclassification to the statement of profit or loss	-	-
	-	(28,071)
Debt instruments at fair value through OCI		
Net changes in fair value during the period	(5,167)	-
Net Changes in allowances for expected credit losses	80	-
Reclassification to the statement of profit or loss	(233)	-
	(5,320)	-
Monetary gold		
Net changes in fair value	(1,765)	13,248
	(1,765)	13,248
<b>Total other comprehensive (loss)</b>	<b>(7,085)</b>	<b>(14,823)</b>
<b>TOTAL COMPREHENSIVE (LOSS) FOR THE PERIOD</b>	<b>(4,230)</b>	<b>(12,396)</b>

The accompanying notes on pages 6 to 26 are an integral part of these condensed interim financial statements.

(1) Statement of comprehensive income for the period ended on 31 March 2018 reflects adoption of IFRS 9 from 1 January 2018. For additional information on IFRS 9 adoption see Notes 2 and 4 of these unaudited condensed interim financial statements. Comparative financial information has not been restated.

## STATEMENT OF FINANCIAL POSITION

As of

(unaudited) (in thousands of KM)	Note	31 March 2018 <sup>(1)</sup>	1 January 2018 <sup>(1)</sup>	31 December 2017
<b>ASSETS</b>				
Foreign currency in cash		245,504	236,402	236,402
Deposits with foreign banks	10	2,513,142	2,697,015	2,698,650
Financial assets available-for-sale		-	-	6,202,071
Debt instruments at fair value through OCI	11	7,922,217	7,473,857	-
Monetary gold		202,093	203,858	203,908
Held-to-maturity investments		-	-	1,214,062
Special Drawing Rights with the IMF		1,746	1,531	1,531
Other assets		11,687	11,626	11,656
Property and equipment		45,617	45,465	45,465
Intangible assets		1,124	1,072	1,072
Equity securities at fair value through OCI		27,813	27,813	27,813
<b>TOTAL ASSETS</b>		<b>10,970,943</b>	<b>10,698,639</b>	<b>10,642,630</b>
<b>LIABILITIES, EQUITY AND RESERVES</b>				
Currency in circulation		4,342,748	4,319,360	4,319,360
Deposits from banks		5,205,291	5,033,065	5,033,065
Deposits from the Government and other depositors		704,365	624,708	624,708
Provisions for liabilities and charges		1,459	1,650	1,650
Other liabilities	12	12,666	11,212	11,212
<b>Total liabilities</b>		<b>10,266,529</b>	<b>9,989,995</b>	<b>9,989,995</b>
Initial capital		25,000	25,000	25,000
General reserves (Retained earnings)		506,289	506,289	542,766
Special reserves		31,300	31,300	31,300
Fair value reserves		138,970	146,055	53,569
Fair value reserves – financial assets available-for-sale		-	-	93,120
Fair value reserves – debt instruments at fair value through OCI		140,733	146,053	-
Fair value reserves – equity securities at fair value through OCI		2	2	-
Revaluation reserves– monetary gold		(1,765)	-	(39,551)
Profit for the period		2,855	-	-
<b>Total equity and reserves</b>		<b>704,414</b>	<b>708,644</b>	<b>652,635</b>
<b>TOTAL LIABILITIES, EQUITY AND RESERVES</b>		<b>10,970,943</b>	<b>10,698,639</b>	<b>10,642,630</b>

The accompanying notes on pages 6 to 26 are an integral part of these condensed interim financial statements.

(1) Statement of financial position as of 31 March 2018 reflects adoption of IFRS 9 from 1 January 2018. For additional information on IFRS 9 adoption see Notes 2 and 4 of these unaudited condensed interim financial statements. Comparative financial information has not been restated.

## STATEMENT OF CHANGES IN EQUITY

*For the period*

(unaudited) (in thousands of KM)	Initial capital	General reserves (Retained earnings)	Special reserves	Fair value reserves – financial assets available-for-sale	Fair value reserves – debt instruments at fair value through OCI	Fair value reserves – equity securities at fair value through OCI	Revaluation reserves/ Fair value reserves-monetary gold	Profit for the period	Total
<b>Balance as of 31 December 2017</b>	<b>25,000</b>	<b>542,766</b>	<b>31,300</b>	<b>93,120</b>	<b>-</b>	<b>-</b>	<b>(39,551)</b>	<b>-</b>	<b>652,635</b>
Adjustment on initial adoption of IFRS 9 (Note 4)	-	(36,477)	-	(93,120)	146,053	2	39,551	-	<b>56,009</b>
<b>Opening balance as of 1 January 2018</b>	<b>25,000</b>	<b>506,289</b>	<b>31,300</b>	<b>-</b>	<b>146,053</b>	<b>2</b>	<b>-</b>	<b>-</b>	<b>708,644</b>
<b>Total comprehensive income for the period</b>									
Profit for the period	-	-	-	-	-	-	-	2,855	2,855
Other comprehensive income	-	-	-	-	(5,320)	-	(1,765)	-	(7,085)
	-	-	-	-	(5,320)	-	(1,765)	2,855	(4,230)
<b>Balance as of 31 March 2018 <sup>(1)</sup></b>	<b>25,000</b>	<b>506,289</b>	<b>31,300</b>	<b>-</b>	<b>140,733</b>	<b>2</b>	<b>(1,765)</b>	<b>2,855</b>	<b>704,414</b>
<b>Balance as of 1 January 2017</b>	<b>25,000</b>	<b>537,892</b>	<b>31,300</b>	<b>111,597</b>	<b>-</b>	<b>-</b>	<b>(38,357)</b>	<b>-</b>	<b>667,432</b>
<b>Total comprehensive income for the period</b>									
Profit for the period	-	-	-	-	-	-	-	2,427	2,427
Other comprehensive income	-	-	-	(28,071)	-	-	13,248	-	(14,823)
	-	-	-	(28,071)	-	-	13,248	2,427	(12,396)
<b>Balance as of 31 March 2017</b>	<b>25,000</b>	<b>537,892</b>	<b>31,300</b>	<b>83,526</b>	<b>-</b>	<b>-</b>	<b>(25,109)</b>	<b>2,427</b>	<b>655,036</b>

The accompanying notes on pages 6 to 15 are an integral part of these condensed interim financial statements.

(1) Statement of changes in equity for the period ended on 31 March 2018 reflects adoption of IFRS 9 from 1 January 2018. For additional information on IFRS 9 adoption see Notes 2 and 4 of these unaudited condensed interim financial statements. Comparative financial information has not been restated.

## STATEMENT OF CASH FLOWS

		For the period	
(unaudited) (in thousands of KM)	Note	01/01 – 31/03/2018 <sup>(1)</sup>	01/01 – 31/03/2017
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
<b>Profit for the period</b>		<b>2,855</b>	<b>2,427</b>
Adjustments for:			
Depreciation and amortisation		523	484
Net losses from ECL on debt instruments at fair value through OCI		80	-
Net realised (gains) from sale of debt instruments at fair value through OCI		(233)	-
Income from grants		(33)	(33)
Provisions for liabilities and charges		(154)	-
Interest income from debt instruments at fair value through OCI		(7,132)	-
Interest income from financial assets available-for-sale and held-to-maturity investments recognized in the statement of profit or loss		-	(7,416)
<b>Net cash flows from operating activities before changes in operating assets and liabilities</b>		<b>(4,094)</b>	<b>(4,538)</b>
<b>Changes in operating assets and liabilities</b>			
(Increase) in deposits with foreign banks		(193,034)	(526,589)
(Increase) / decrease in other assets		585	(4,136)
Increase of currency in circulation		23,388	7,581
Increase / (decrease) in deposits		251,883	(282,523)
Increase in other liabilities		1,487	1,742
Pay-out of severance payments		(37)	(54)
<b>Net cash from operating activities</b>		<b>80,178</b>	<b>(808,517)</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Purchases of property, equipment and intangible assets		(727)	(1,018)
Collected principal and interest from debt instruments at fair value through OCI		686,747	-
Purchases of debt instruments at fair value through OCI		(1,309,725)	-
Sales of debt instruments at fair value through OCI		176,583	-
Collected principal and interest from available-for sale financial assets		-	1,108,333
Purchases of available-for sale financial assets		-	(1,100,024)
Sales of available-for sale financial assets		-	-
Collected principal and interest from held-to-maturity investments		-	2,445
Purchases of held-to-maturity investments		-	(90,720)
<b>Net cash used in investing activities</b>		<b>(447,122)</b>	<b>(80,984)</b>
<b>Net (decrease) in cash and cash equivalents</b>		<b>(366,944)</b>	<b>(889,501)</b>
<b>Cash and cash equivalents at the beginning of the year</b>		<b>2,060,001</b>	<b>2,973,081</b>
<b>Cash and cash equivalents at the end of the period</b>	13	<b>1,693,057</b>	<b>2,083,580</b>

The accompanying notes on pages 6 to 26 are an integral part of these condensed interim financial statements.

(1) Statement of cash flows for the period ended on 31 March 2018 reflects adoption of IFRS 9 from 1 January 2018. For additional information on IFRS 9 adoption see Notes 2 and 4 of these unaudited condensed interim financial statements. Comparative financial information has not been restated.

## **NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS FOR THE PERIOD ENDED 31 MARCH 2018**

Note 1	Basis for preparation	6	Note 11	Debt instruments at fair value through OCI	18
Note 2	Accounting policy changes	8	Note 12	Other liabilities	18
Note 3	Future accounting policy changes	12	Note 13	Cash and cash equivalents	19
Note 4	Impact of accounting policy changes	12	Note 14	Currency board arrangement	19
Note 5	Net interest income	16	Note 15	Financial risk management	20
Note 6	Net fee and commission income	17	Note 16	Fair value measurement	22
Note 7	Net (losses) from ECL on financial assets	17	Note 17	Off-balance sheet items	24
Note 8	Net (losses) from foreign exchange differences	18	Note 18	Post-reporting date events	26
Note 9	Administrative and other operating expenses	19	Note 19	Approval of the condensed interim financial statements	26
Note 10	Deposits with foreign banks	18			

### **1. BASIS FOR PREPARATION**

#### **1.1. Reporting entity**

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 ("BH") on 20 June 1997, according to the General Framework Peace Agreement in Bosnia and Herzegovina. The main objective of the Bank is maintaining the monetary stability of Bosnia and Herzegovina.

Head Office of the Bank is located in Sarajevo, Maršala Tita Street, No 25.

According to the article 64, paragraph 2 of the Law on the Central Bank of Bosnia and Herzegovina, the Bank is obliged to submit unaudited financial statements for each quarter to the BH Presidency.

Governing Board of the Bank, consisting of five members, approves these condensed interim financial statements, while the Management of the Bank, consisting of four members, is responsible for the preparation of condensed interim financial statements. Members of the Governing Board and Management are:

#### **Governing Board**

Senad Softić, Ph.D.	Chairman
Ankica Kolobarić, M.Sc.	Member
Šerif Isović, M.Sc.	Member
Trivo Marinković, M.Sc.	Member
Ljubiša Vladušić, Ph.D.	Member

#### **Management**

Senad Softić, Ph.D.	Governor
Ernadina Bajrović, M.A.	ViceGovernor
Milica Lakić, Ph.D.	ViceGovernor
Želimira Raspudić	ViceGovernor



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

### **1.2. Basis of accounting**

The condensed interim financial statements are prepared in accordance with the Law on the Central Bank of Bosnia and Herzegovina and in accordance with the International Financial Reporting Standards (IFRS) as published by the International Accounting Standards Board (IASB).

These condensed interim financial statements are prepared in accordance with International Accounting Standard 34: "Interim financial reporting", and should be read in conjunction with the latest audited annual financial statements of the Bank for the year ended on 31 December 2017 („annual statements“).

The accompanying notes of these condensed interim financial statements clarify events and transactions that are important for understanding the changes in the Bank's financial position and performance compared to the latest audited annual statements.

The condensed interim financial statements have been prepared in accordance with the same accounting policies applied in the preparation of the annual statements, except for policy changes described in Note 2 of these condensed interim financial statements. Accounting policy changes, applicable from 1 January 2018, are result of the implementation of IFRS 9: "Financial instruments" and change of accounting policy for monetary gold in accordance with IAS 8: "Accounting Policies, Changes in Accounting Estimates and Errors".

As stated in Note 2, the Bank applied the accounting policies changes without restating comparative financial information for the year 2017. Note 4 of these condensed interim financial statements gives summary of accounting policy changes impact on statement of financial position of the Bank as of 1 January 2018.

As of 1 January 2018 the Bank has changed the certain positions in financial statements and made reclassifications of certain amounts.

In the reporting period there were neither cyclic nor periodical operational activities in the operations of the Bank, all activities were done according to the subject and time of realization on a going concern basis.

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  $KM\ 1.95583 = 1\ EUR$ . 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 Bank's financial statements are stated in the official national currency of Bosnia and Herzegovina which is the convertible mark (KM). All financial information have been rounded to the nearest thousand (unless otherwise indicated).

The significant judgements made by Management in applying the Bank's accounting policies and the key sources of estimation uncertainty were the same as those described in the annual statements, except for new significant judgements and estimates related to the application of IFRS 9, which are described in Note 2.

### **1.3. Fair value measurement**

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 available 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 available for the asset or liability, either directly or indirectly; and
- Level 3 inputs are unavailable inputs for the asset or liability.

A fair value measurement of financial assets and liabilities of the Bank is presented in Note 16.

## 2. ACCOUNTING POLICY CHANGES

The below-described accounting policies have been applied from 1 January 2018 following the implementation of IFRS 9 "Financial instruments" and change of accounting policy for monetary gold in accordance with IAS 8: "Accounting Policies, Changes in Accounting Estimates and Errors". As permitted by these standards, the Bank has not restated comparative financial information in financial statements. Note 4 gives an overview of the impact of accounting policy changes on amounts in statement of financial position as of 1 January 2018.

### 2.1. Summary of accounting policy changes for financial assets according to IFRS 9

#### *Business model*

The business model reflects how the Bank manages its financial assets in order to generate contractual cash flows. By selecting the business model the Bank determines to generate cash flows by collecting the contractual cash flows, by selling financial assets, or by both.

A financial asset that generates contractual cash flows during its lifetime is classified within a "hold to collect contractual cash flows" model.

A financial asset that generates contractual cash flows during its lifetime or by selling is classified within a "hold to collect contractual cash flows and sell" model.

A financial asset that is kept for generating cash flows by selling that asset is classified within other business models.

#### *Contractual cash flow characteristics*

For the purpose of classifying a financial asset, the Bank must determine whether the contractual cash flows associated with the financial asset are solely payments of principal and interest on the principal amount outstanding. The principal is generally the fair value of the financial asset at initial recognition. The interest consists of consideration for the time value of money, for the credit risk associated with the principal amount outstanding during a particular period of time, and for other basic lending risks and costs related to the holding the financial asset.

#### *Recognition, classification and measurement of financial assets*

All financial assets are initially measured at fair value. Transaction costs that are directly attributable to the acquisition of financial assets are added to the fair value of the financial assets, as appropriate, on initial recognition.

After initial recognition, financial asset is classified as financial asset subsequently measured at amortised cost or as financial asset subsequently measured at fair value through other comprehensive income (FVOCI). Classification of financial assets depends on the business model determined by the Bank to manage certain categories of financial assets and on the contractual cash flows characteristics of the asset.

The Bank has made an irrevocable election for subsequent measurement of fair value for equity securities in other comprehensive income and they are initially recognized at cost for which the Bank considers to be their fair value.

#### *Method of effective interest rate*

The effective interest rate is the rate that exactly discounts future cash payments or receipts through the expected life of the financial assets or financial liabilities to the gross carrying amount of the financial asset or to the amortised cost of financial liability.

When calculating effective interest rate, the Bank estimates expected cash flows, considering all contractual conditions of financial asset, but excluding expected credit losses. The calculation includes all fees and all amounts paid or received between the Bank and counterparties that form an integral part of the effective interest rate, transaction costs and other premiums or discounts.

The effective interest method is a method used by Bank in calculation of the amortised cost of a financial asset or a financial liability and in allocation and recognition of the interest income or interest expense in profit or loss over the relevant period.

## **2. ACCOUNTING POLICY CHANGES (CONTINUED)**

### **2.1. Summary of accounting policy changes for financial assets according to IFRS 9 (continued)**

#### *Financial asset at amortised cost*

Financial asset is subsequently measured at amortised cost using the effective interest rate method to the gross carrying amount of financial assets during the holding of the financial asset until maturity.

Effects of subsequent measurement are recognized as interest income or interest expense in profit or loss in the period in which they occur.

#### *Financial assets at fair value through other comprehensive income (FVOCI)*

Financial asset is subsequently measured at fair value through other comprehensive income-using the effective interest rate method for interest income and expense to the gross carrying amount and is adjusted with the fair value of financial asset on reporting dates during the holding of the financial asset.

Effects of subsequent measurements are recognized as interest income or interest expense in profit or loss in the period when they occur.

Effects of fair value adjustment of financial asset subsequently measured at fair value through other comprehensive income are recognized within other comprehensive income in the period when they occur.

Fair value is measured by quoted prices in active markets taken from official services.

#### *Equity securities*

Equity securities held by the Bank are not subject of trade on active markets due to its specific characteristics. Calculation of impairment for expected credit losses is not made for equity securities. Equity securities are initially recognized at acquisition cost. Dividend income is recognized in profit or loss in the period when occur.

#### *Impairment of financial assets*

##### *Scope*

The Bank applies a three stage model for impairment based of credit losses using the expected credit losses approach, as required by IFRS 9. It is applied for the following categories of financial instruments not measured at profit or loss:

- financial asset at amortized cost and
- debt securities through other comprehensive income.

Financial asset is being moved within three phases based on change of credit risk from the initial recognition date.

##### *Impairment model based on expected credit losses*

1. Stage 1 – At initial recognition, all financial assets, that are assessed to be impaired according to IFRS 9, are allocated in Stage 1 and requires the calculation of expected losses. For financial assets in Stage 1, 12-month expected credit losses are calculated using the probability of loss for the next 12 months.
2. Stage 2 – If a significant increase in credit risk since initial recognition is identified, financial assets is moved to Stage 2. For financial assets in Stage 2, lifetime expected credit losses are calculated based on the probability of loss for the remaining estimated lifetime of the financial assets.
3. Stage 3 – The criteria for movement into the Stage 3 is assignment of the default status to financial assets. Expected credit loss calculation is done similarly to the Stage 2

## **2. ACCOUNTING POLICY CHANGES (CONTINUED)**

### **2.1. Summary of accounting policy changes for financial assets according to IFRS 9 (continued)**

#### **Expected credit losses measurement**

Probability of default, Exposure at Default and Loss Given Default are the inputs used for estimation of expected credit losses and are modeled based on macroeconomic variables closely related to credit losses in portfolio.

Expected credit losses are the discounted product of the Probability of Default (PD), Loss Given Default (LGD) and Exposure at Default (EAD), defined as follows:

- Probability of Default (PD) is an estimate of the probability that an issuer will not be able to meet its debt liabilities over the certain period.
- Exposure at Default (EAD) represents the book value of the financial instrument, i.e. the carrying amount at the date of the initial recognition or on the reporting date.
- Loss Given Default (LGD) is an estimation of the percentage of exposure to the issuer who, in case of default, will not be charged. For this parameter the Bank uses the constant value according to the article 161 of the Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 (CRR).

#### **Forward-looking information**

Expected credit losses measurement for each stage and estimation of significant increase in credit risk is including both past and future information, as well as reasonable forecasts of future events and economic conditions.

For expected credit loss calculation, the Bank uses the long-term composite credit rating. Composite credit rating is the average of ratings assigned to a certain issuer by at least two of the three rating agencies (Standard and Poor's, Fitch Ratings and Moody's). In order to include macroeconomic forecast in expected credit losses model, the Bank relies on predicting changes in rating for individual instruments in its portfolio, in a way which incorporates the prediction of rating movement direction: positive, stable, negative.

#### **Assessment of significant increase in credit risk**

At each reporting date, the Bank assesses whether there has been a significant increase in credit risk from the initial recognition. The assessment is made by comparing the risk of default between the reporting date and initial recognition date for the remaining expected lifetime. Credit risk of the financial instrument is considered to be low if Probability of Default of issuer has significant capacity to orderly pays its contractual cash liabilities, in the short and long term. The Bank considers that all exposures with the composite credit rating AA minus (AA-) or higher have the low credit risk

Financial instrument is allocated out of Stage 1 if it is considered that significant increase in credit risk has occurred, and if payment is delayed for 30 days it is allocated to the Stage 2, respectively to the Stage 3 if payment is delayed for 90 days. Except for the mentioned delay criteria, the Bank assesses if there was significant increase in credit risk comparing to initially assessed risks, while deciding on allocation of individual financial instruments to the Stage 2. In case there was decrease in composite credit rating for more than two notches in relation to initial recognition date and/or decrease in composite credit rating below investment level of composite credit rating, i.e. below the BBB minus (BBB-) rating, the exposure will be transferred to the Stage 2. The exposure can be reverted from Stage 2 to Stage 1 if the causes that led to the transfer to Stage 2 have been removed and at least 90 days after removal of the cause.

#### **Presentation of ECL allowances in the statement of financial position**

- for financial assets at amortised cost as deduction of gross carrying amount of the financial assets;
- for debt securities at other comprehensive income, the allowances are recognized in other comprehensive income within the capital and reserves, not in statement of financial position.

Gain or loss from impairment is recognized in the profit or loss, irrespectively to subsequent measurements of financial assets.

## **2. ACCOUNTING POLICY CHANGES (CONTINUED)**

### **2.1. Summary of accounting policy changes for financial assets according to IFRS 9 (continued)**

#### *Definition of default*

The Bank considers that a financial instrument is in the default status when one or more impairment events occurred after the date of initial recognition have a negative impact on the estimated future cash flows of the instrument. Default criteria are objective evidences of impairment and especially:

- Significant financial difficulties of securities' issuers,
- Breach of contractual obligations in terms of delinquency on principal and interest,
- Any restructuring or modification of existing terms of servicing obligations arising from the financial instrument debt for reasons related to financial difficulties of the issuer,
- Probability of bankruptcy and/or liquidation or other form of financial reorganization,
- Lack of an active trading market.

In addition to the criteria mentioned above, if payment is delayed for 90 days, the financial instrument will be transferred to default stage.

#### *Reclassification*

In case of reclassification, the Bank reclassifies its financial assets prospectively from the date of reclassification.

If financial asset is reclassified out of the category measured at fair value through other comprehensive income into the category at amortised cost, accumulated gain or loss in other comprehensive income is used for adjustment of fair value of financial asset, becoming the amortised cost as of reclassification date.

If financial asset is reclassified out of the category at amortised cost into the category measured at fair value through other comprehensive income, difference between the fair value of the asset and its gross carrying amount is recognized in other comprehensive income as of the reclassification date.

#### *De-recognition*

When derecognizing the financial assets subsequently measured at amortised cost, remaining balance for impairment at de-recognition date is transferred to profit or loss for the period.

When derecognizing the financial assets, subsequently measured at fair value through other comprehensive income, accumulated gain or loss previously recognized in other comprehensive income is transferred from the equity to profit or loss for the period.

### **2.2. Summary of changes in accounting policy for monetary gold**

Monetary gold is part of foreign exchange reserves of the Bank and it is classified as a financial asset. The Bank has revised the current accounting policy for monetary gold and changed the accounting treatment of monetary gold, effective from 1 January 2018, as follows:

Monetary gold is initially recognized at fair value, including transaction cost directly attributable to the acquisition of the gold. After initial recognition, the gold is re-measured at fair value.

Unrealized gains and losses arising from changes in fair value, referring to the price changes of monetary gold, are recognized in the revaluation reserve account within other comprehensive income.

In the event that unrealised losses exceed the balance in the revaluation reserve for monetary gold at the end of the financial year, the Bank shall charge the excess against the period's profit available for distribution.

## **2. ACCOUNTING POLICY CHANGES (CONTINUED)**

### **2.2. Summary of changes in accounting policy for monetary gold (continued)**

On the sale of gold, the Bank shall recycle existing unrealized gains and losses through profit and loss.

The fair value of monetary gold is expressed in EUR, converted at the fixed rate of KM at the reporting date, and it is measured at the last bid price for one ounce of gold (Oz) at the reporting date quoted on Reuters.

## **3. FUTURE ACCOUNTING POLICY CHANGES**

The Bank closely monitors both new accounting standards and amendments to existing accounting standards issued by the IASB. The Bank is currently assessing how adoption of new and amended accounting standards will impact the financial statements of the Bank. Aside from the adoption of IFRS 9 on 1 January 2018 and changed accounting policy for monetary gold, there have been no significant updates to the accounting policies used in preparation of annual financial statements.

## **4. IMPACT OF ACCOUNTING POLICY CHANGES**

### **4.1. Classification and measurement of financial asset**

The IFRS 9 classification and measurement requirements, also the impairment requirements, as well as the change of accounting policy for monetary gold have been applied by the Bank, with no restatement of comparative periods. The impacts of IFRS 9 adoption were recognized at the position of general reserves (retained earnings) of the Bank.

The effects of adopting IFRS 9 on the carrying amounts of financial assets on 1 January 2018 relate mainly to the new impairment requirements, as described further below.

The following table and the below accompanying notes present the reconciliation of the original classification under IAS 39 and new classification under IFRS 9 for each group of financial assets of the Bank, as of 1 January 2018.

(in thousands of KM)

<b>Financial asset</b>	<b>Original classification under IAS 39</b>	<b>New classification under IFRS 9</b>	<b>Original carrying value under IAS 39</b>	<b>New carrying value under IFRS 9</b>	<b>Reference</b>
Foreign currency in cash	Loans and receivables	Amortised cost	236,402	236,402	(A)
Deposits with foreign banks	Loans and receivables	Amortised cost	2,698,650	2,697,015	(B)
Special drawing rights with the IMF	Loans and receivables	Amortised cost	1,531	1,531	(C)
Debt securities	Available-for-sale	Fair value through other comprehensive income	6,202,071	7,473,857	(D)
Debt securities	Held-to-maturity	Fair value through other comprehensive income	1,214,062	-	(E)
Equity securities	Available-for-sale	Fair value through other comprehensive income – irrevocable selection	27,813	27,813	(F)
Other financial asset	Loans and receivables	Amortised cost	2,746	2,716	(G)
<b>TOTAL</b>			<b>10,383,275</b>	<b>10,439,334</b>	

#### **4. IMPACT OF ACCOUNTING POLICY CHANGES (CONTINUED)**

##### **4.1. Classification and measurement of financial asset (continued)**

(A) Foreign currency in cash is measured both under IAS 39 and IFRS 9 at amortised cost and due to its characteristics have the same accounting treatment.

(B) Deposits with foreign banks originally classified as loans and receivables under IAS 39, are now classified as financial asset subsequently measured at amortised cost.

(C) Special drawing rights with the IMF that were originally classified as loans and receivables under IAS 39, are now classified as financial asset subsequently measured at amortised cost.

(D) Debt securities were originally classified as available for sale under IAS 39. The Bank has classified securities as financial asset subsequently measured at fair value through other comprehensive income.

(E) Debt securities were originally classified as held to maturity under IAS 39. The Bank has classified securities as financial asset subsequently measured at fair value through other comprehensive income.

(F) For equity securities that were classified as available-for-sale, the Bank irrevocably selected to present subsequent changes of fair value in other comprehensive income. Equity securities do not have active market.

(G) Other financial assets used to be classified as loans and receivables under IAS 39 are now classified as financial assets at amortised cost.

The following table presents the review of the accounting treatment and value of monetary gold until 31 December 2017 and from 1 January 2018.

(in thousands of KM)

##### **Change of accounting policy for monetary gold**

Initial classification	Subsequent measurement	Currency	Effects of subsequent measurement	Policy applied	Carrying value
Fair value	Fair value	USD	Through other comprehensive income	until 31 December 2017	203,908
Fair value	Fair value	EUR	Through other comprehensive income throughout the year, but in case of negative balance at the end of the year, negative amount is recognized in the profit or loss	from 1 January 2018	203,858

Carrying value of financial asset of the Bank as of 31 December 2017 and 1 January 2018 is given in the following table:

(in thousands of KM)

Category of financial asset	31 December 2017	1 January 2018
Financial asset under IAS 39/IFRS 9	10,383,275	10,439,334
Monetary gold	203,908	203,858
<b>TOTAL</b>	<b>10,587,183</b>	<b>10,643,192</b>

#### 4. THE IMPACT OF ACCOUNTING POLICY CHANGES (CONTINUED)

##### 4.1. The classification and measurement of financial asset (continued)

The following table presents a reconciliation of the financial asset carrying values established in accordance with IAS 39 and IFRS 9, as well as the impact of the IFRS 9 implementation, by classes of financial assets.

(In thousands of KM)

	IFRS 9 adjustments			Reconciliation of new carrying values under IFRS 9
	Classification	Measurement	Impairment	
<b>Deposits with foreign banks</b>				
Under IAS 39 as of 31 December 2017				2,698,650
Impairment for ECL	-	-	(1,635)	(1,635)
<b>Under IFRS 9 as of 1 January 2018</b>	-	-	<b>(1,635)</b>	<b>2,697,015</b>
<b>Available-for-sale financial assets</b>				
Under IAS 39 as of 31 December 2017				6,202,071
Reclassification into:				
FVOCI	(6,202,071)	-	-	(6,202,071)
<b>Under IFRS 9 as of 1 January 2018</b>	<b>(6,202,071)</b>	-	-	-
<b>Financial assets at fair value through other comprehensive income</b>				
Under IAS 39 as of 31 December 2017				-
Reclassification from:				
Available-for-sale	6,202,071	-	-	6,202,071
Held-to-maturity	1,214,062	57,724	-	1,271,786
<b>Under IFRS 9 as of 1 January 2018</b>	<b>7,416,133</b>	<b>57,724</b>	-	<b>7,473,857</b>
<b>Financial assets held-to-maturity</b>				
Under IAS 39 as of 31 December 2017				1,214,062
Reclassification into:				
FVOCI	(1,214,062)	-	-	(1,214,062)
<b>Under IFRS 9 as of 1 January 2018</b>	<b>(1,214,062)</b>	-	-	-
<b>Other financial assets</b>				
Under IAS 39 as of 31 December 2017				2,746
Reclassification into:				
Financial asset at amortised cost	(2,746)			(2,746)
<b>Under IFRS 9 as of 1 January 2018</b>	<b>(2,746)</b>			-
<b>Financial assets at amortised cost</b>				
Under IAS 39 as of 31 December 2017				-
Reclassification from:				
Loans and receivables	2,746		(30)	2,716
<b>Under IFRS 9 as of 1 January 2018</b>	<b>2,746</b>		<b>(30)</b>	<b>2,716</b>
<b>IFRS 9 impact on financial asset as of 1 January 2018</b>	-	<b>57,724</b>	<b>(1,665)</b>	<b>56,059</b>



#### **4. THE IMPACT OF ACCOUNTING POLICY CHANGES (CONTINUED)**

##### **4.1. The classification and measurement of financial asset (continued)**

The following table presents the implementation of new accounting policy for monetary gold as of 1 January 2018:

(in thousands of KM)

	Classification	Measurement	Impairment	New carrying value
<b>Monetary gold</b>				
As of 31 December 2017				203,908
New accounting policy implementation – foreign exchange differences	-	-	(50)	(50)
<b>As of 1 January 2018</b>	-	-	<b>(50)</b>	<b>203,858</b>

The impact of IFRS 9 and the new accounting policy for monetary gold on the financial asset of the Bank is given below:

(in thousands of KM)

The IFRS 9 impact as of 1 January 2018	56,059
The impact of new accounting policy for monetary gold	(50)
<b>TOTAL</b>	<b>56,009</b>

The following table gives the impact of transition to IFRS 9 and the change of accounting policy for monetary gold on the opening balance of the general reserves (retained earnings) and the fair value reserves:

(in thousands of KM)

Impact of the IFRS 9 implementation  
and the accounting policy change  
on the opening balances

##### **General reserves (retained earnings)**

Recognition of ECL under IFRS 9	(5,955)
New effective interest rate method application under IFRS 9	9,079
New accounting policy for monetary gold implementation -fair value	(39,551)
New accounting policy for monetary gold implementation –foreign exchange differences	(50)
<b>Impact as of 1 January 2018</b>	<b>(36,477)</b>

##### **Fair value reserves**

Reclassification of held-to-maturity financial asset into financial asset subsequently measured at FVOCI	57,724
New effective interest rate method application under IFRS 9	(9,079)
Allowances for ECL for financial asset at FVOCI	4,290
New accounting policy for monetary gold implementation	39,551
<b>Impact as of 1 January 2018</b>	<b>92,486</b>

The impact of IFRS 9 and the new accounting policy for monetary gold on the equity of the Bank is given below:

(in thousands of KM)

The IFRS 9 impact as of 1 January 2018	56,059
The impact of new accounting policy for monetary gold	(50)
<b>TOTAL</b>	<b>56,009</b>

Financial liabilities were classified as „other financial liabilities“ under IAS 39 and measured at amortised cost. The financial liabilities treatment under IFRS 9 has remained unchanged.

## 5. NET INTEREST INCOME

	For the period	
(in thousands of KM)	1 January – 31 March 2018	1 January – 31 March 2017
Interest income arising from:		
- financial assets at fair value through other comprehensive income	7,132	-
- financial assets available-for-sale	-	4,380
- held-to-maturity investments	-	3,036
- deposits with foreign banks	6	4
- other	7	2
	<b>7,145</b>	<b>7,422</b>
The effects of negative interest rates from interest bearing financial assets from:		
- term deposits held with foreign banks	(2,077)	(2,402)
- demand deposits held with foreign banks	(519)	(545)
	<b>(2,596)</b>	<b>(2,947)</b>
The effects of negative deposit interest rates on deposits from local commercial banks	<b>1,398</b>	<b>1,041</b>
<b>Net interest income</b>	<b>5,947</b>	<b>5,516</b>

The average negative effective interest rate on deposits invested in foreign banks amounted to 0.42% in the period 1 January - 31 March 2018 (in the period 1 January - 31 March 2017 amounted to negative 0.43%).

The average effective yield on invested debt securities at fair value through other comprehensive income amounted to 0.39% in the period 1 January - 31 March 2018.

The average effective yield on the invested available-for-sale securities amounted to 0.35% in the period 1 January - 31 March 2017.

The average effective yield on held-to-maturity investments amounted to 1.03% in the period 1 January - 31 March 2017.

From 1 July 2016 the base for the required reserve calculation for commercial banks has included deposits and borrowings regardless of currency which the funds are denominated in. Also, the single required reserve rate of 10% has been established applied by the Bank on the base for the required reserve calculation.

The Bank does not calculate a 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.

The effects of negative interest rates from interest-bearing financial assets result from negative interest rates on term deposits and funds in current accounts that could not be avoided given the current market circumstances.

The effects of negative deposit interest rates on deposits from local commercial banks result from negative interest rate on the amount exceeding the required reserve which amounted to 0.20% in the reporting periods.

## 6. NET FEE AND COMMISSION INCOME

	For the period	
(in thousands of KM)	1 January – 31 March 2018	1 January – 31 March 2017
Fee and commission income:		
- from local commercial banks	3,762	2,836
- from services for the Government and other non-banking clients	291	189
	<u>4,053</u>	<u>3,025</u>
Fee and commission expenses:		
- transactions with foreign banks	(162)	(128)
	<u>(162)</u>	<u>(128)</u>
<b>Net fee and commission income</b>	<u><b>3,891</b></u>	<u><b>2,897</b></u>

## 7. NET (LOSSES) FROM EXPECTED CREDIT LOSSES ON FINANCIAL ASSETS

	For the period
(in thousands of KM)	1 January – 31 March 2018
Gains from expected credit losses:	
- from deposits with foreign banks	1,554
- from financial assets subsequently measured at fair value through other comprehensive income	987
- from other financial assets	10
- from Special Drawing Rights with the IMF	-
	<u>2,551</u>
Losses from expected credit losses:	
- from deposits with foreign banks	(2,144)
- from financial assets subsequently measured at fair value through other comprehensive income	(1,067)
- from other financial assets	(10)
- from Special Drawing Rights with the IMF	-
	<u>(3,221)</u>
<b>Net (losses) from expected credit losses on financial assets</b>	<u><b>(670)</b></u>

The Bank did not have gains and losses arising from impairment of financial assets according to IAS 39 in the period 1 January - 31 March 2017.

## 8. NET FOREIGN EXCHANGE (LOSSES)

For the period

(In thousands of KM)	1 January – 31 March 2018	1 January – 31 March 2017
Income from foreign exchange differences	85	178
Expenses from foreign exchange differences	(301)	(226)
<b>Net foreign exchange (losses)</b>	<b>(216)</b>	<b>(48)</b>

## 9. ADMINISTRATIVE AND OTHER OPERATING EXPENSES

Administrative and other operating expenses in the period 1 January – 31 March 2018 include also the deferred costs of the production of banknotes and coins in the amount of KM 438 thousand (1 January – 31 March 2017 these expenses included the deferred costs of the production of banknotes and coins in the amount of KM 171 thousand).

## 10. DEPOSITS WITH FOREIGN BANKS

Deposits with foreign banks, analysed by the remaining maturity, are as follows:

(in thousands of KM)	31 March 2018	31 December 2017
<b>Demand deposits</b>	<b>602,625</b>	<b>671,583</b>
Up to 1 month	510,629	993,768
From 1 to 2 months	135,786	136,200
From 2 to 3 months	642,682	449,303
From 3 to 4 months	524,355	117,154
From 4 to 12 months	97,065	330,642
<b>Total term deposits</b>	<b>1,910,517</b>	<b>2,027,067</b>
<b>TOTAL</b>	<b>2,513,142</b>	<b>2,698,650</b>

As of 31 March 2018 deposits with foreign banks include also the allowances for expected credit losses in the amount of KM 2,224 thousand (See Note 15).

## 11. DEBT INSTRUMENTS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

Debt instruments at fair value through other comprehensive income are quality debt securities with a high degree of marketability and liquidity, with credit ratings from AAA to BBB. The portfolio includes short-term and long-term debt securities with a fixed interest rate, which are issued by the governments of foreign countries. As of 31 March 2018 all debt instruments at fair value through other comprehensive income are denominated in EUR.

As of 31 March 2018 allowances for expected credit losses for debt instruments at fair value through other comprehensive income amount to KM 4,208 thousand (See Note 15).

## 12. OTHER LIABILITIES

Other liabilities as of reporting dates include also the liabilities based on the allocation of a part of the 2017 profit in the amount of KM 7,311 thousand to the state budget (See Note 18).

### 13. CASH AND CASH EQUIVALENTS

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

(in thousands of KM)	31 March 2018	31 March 2017
Foreign exchange deposits with maturities up to three months or less, from the date of acquisition	842,100	1,365,894
Foreign exchange demand deposits	602,625	502,210
Foreign currency in cash	245,504	212,633
Special Drawing Rights with the IMF	1,746	2,570
Giro accounts	1,082	273
<b>TOTAL</b>	<b>1,693,057</b>	<b>2,083,580</b>

As of 1 January 2018 cash and cash equivalents in the amount of KM 2,060,001 thousand include the corresponding amount of allowances for expected credit losses for demand deposits and term deposits with maturity up to three months or less from the date of acquisition in the amount of KM 1,283 thousand.

### 14. 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 March 2018	31 December 2017
<b>Foreign assets</b>	<b>10,884,702</b>	<b>10,556,624</b>
Liabilities to non-residents	3,228	1,649
<b>Net foreign exchange reserves (foreign assets minus liabilities to non-residents)</b>	<b>10,881,474</b>	<b>10,554,975</b>
<b>Monetary liabilities</b>	<b>10,252,404</b>	<b>9,977,133</b>
<b>Net foreign assets (net foreign exchange reserves minus monetary liabilities)</b>	<b>629,070</b>	<b>577,842</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.

## 15. FINANCIAL RISK MANAGEMENT

The Bank's financial assets is largely comprised of financial instruments which expose the Bank to a number of financial risks, including credit risk, market risks and liquidity risk.

### 15.1. Credit risk

Credit risk is the risk of a 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 debt securities (foreign exchange reserves). The management of this risk is performed through the selection of counterparties with high level credit ratings assigned by internationally recognized rating agencies, by limiting the maturities, and by controlling the volume and the dynamics of investment. The credit ratings are monitored on a daily basis.

From 1 January 2018 the Bank has implemented a new concept of „expected credit losses“ in accordance with the IFRS 9 requirements in credit risk management. As explained in Note 2, the Bank is obliged to measure expected credit losses for financial assets measured at amortised cost and measured at fair value through other comprehensive income

The following table presents the movements in allowances for expected credit losses in the period 1 January - 31 March 2018:

(in thousands of KM)

Classes of financial instruments	31 March 2018	Decrease of allowances during the period	Additional allowances during the period	1 January 2018	31 December 2017
Deposits with foreign banks	2,224	(1,554)	2,143	1,635	-
<i>Demand deposits</i>	1,060	(1,362)	1,860	562	-
<i>Term deposits</i>	1,164	(192)	283	1,073	-
Financial assets at fair value through other comprehensive income	4,208	(1,148)	1,066	4,290	-
<i>Debt securities</i>	4,208	(1,148)	1,066	4,290	-
Special Drawing Rights with the IMF	-	-	-	-	-
Other financial assets	30	(10)	10	30	-
<b>TOTAL</b>	<b>6,462</b>	<b>(2,712)</b>	<b>3,219</b>	<b>5,955</b>	<b>-</b>

As of 31 March 2018 the expected credit losses are estimated in the amount of KM 6,462 thousand (As of 1 January 2018 KM 5,955 thousand). The increase in the expected credit losses (KM 507 thousand) is a result of the increase in expected credit losses from deposits with foreign banks because of an increased probability of default in most foreign banks where the Banks holds foreign exchange deposits and increase in the expected credit losses due to increased probability of default of the lowest risk Eurozone countries.

The following tables show the allocation of expected credit losses for the most important items of the Bank's financial assets in stages as of 1 January 2018 and as of 31 March 2018 as it follows:

(in thousands of KM)

	1 January 2018		
	Stage 1	Stage 2	Stage 3
Deposits with foreign banks	1,635	-	-
Debt securities at fair value through other comprehensive income	4,290	-	-

(in thousands of KM)

	31 March 2018		
	Stage 1	Stage 2	Stage 3
Deposits with foreign banks	2,224	-	-
Debt securities at fair value through other comprehensive income	4,208	-	-

## **15. FINANCIAL RISK MANAGEMENT (CONTINUED)**

### **15.2. Market risk**

The Bank monitors and manages both currency and interest rate risks as the basic market risks. Currency risk is a risk arising from decline of the value of the financial instrument denominated in a foreign currency due to changes in exchange rates. The interest rate risk denotes a risk from decrease of the market value of the financial instruments due to unfavourable movements of interest rates. The market risk management is performed by setting quantitative limits for the currency risk exposure as acceptable for the Bank and they are monitored on a daily basis. The objective of market risk management is to manage and control risks within the acceptable parameters, while optimising the return.

#### **15.2.1. Foreign exchange risk**

The Bank is exposed to foreign exchange 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 exchange risk exposure arises from deposits and investment related 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 Investment Guidelines of the Bank.

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.

#### **15.2.2. 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 interest varies in different periods or in different amounts.

The Bank is exposed to interest rate risk through investment of foreign exchange 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.

### **15.3. Liquidity risk**

Liquidity risk refers to the possible difficulties in liquidating a portion of assets quickly, possibly in a situation when 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's foreign exchange reserves.

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

**16. FAIR VALUE MEASUREMENT**

The following tables show the carrying amount and the fair value amount of financial assets and financial liabilities including fair value hierarchy:

(in thousands of KM)

As of 31 March 2018

	Carrying amount				Fair value			
	Financial assets at fair value through other comprehensive income	Financial assets at amortised cost	Other financial liabilities	Total	Level 1	Level 2	Level 3	Total
<b>Financial assets measured at fair value</b>								
Debt securities	7,922,217	-	-	7,922,217	-	7,922,217	-	7,922,217
Equity securities	27,813	-	-	27,813	-	-	27,813	27,813
<b>Financial assets not measured at fair value</b>								
Foreign currency in cash	-	245,504	-	245,504	-	245,504	-	245,504
Deposits with foreign banks	-	2,513,142	-	2,513,142	-	2,507,530	-	2,507,530
Special Drawing Rights with the IMF	-	1,746	-	1,746	-	1,746	-	1,746
Other financial assets	-	2,087	-	2,087	-	2,087	-	2,087
<b>FINANCIAL ASSETS</b>	<b>7,950,030</b>	<b>2,762,479</b>	<b>-</b>	<b>10,712,509</b>	<b>-</b>	<b>10,679,084</b>	<b>27,813</b>	<b>10,706,897</b>
<b>Financial liabilities not measured at fair value</b>								
Currency in circulation	-	-	4,342,748	4,342,748	-	4,342,748	-	4,342,748
Deposits from banks	-	-	5,205,291	5,205,291	-	5,196,444	-	5,196,444
Deposits from the Government and other depositors	-	-	704,365	704,365	-	703,168	-	703,168
Other financial liabilities	-	-	11,444	11,444	-	11,444	-	11,444
<b>FINANCIAL LIABILITIES</b>	<b>-</b>	<b>-</b>	<b>10,263,848</b>	<b>10,263,848</b>	<b>-</b>	<b>10,253,804</b>	<b>-</b>	<b>10,253,804</b>

As stated in Note 2.1., the Bank irrevocably elected to present subsequent changes in fair value in other comprehensive income for equity securities as they are not quoted in an active market. Therefore, they are classified into Level 3 of fair value hierarchy. The Bank calculates fair value of equity securities on annual basis.

Fair value of monetary gold amounts to KM 202,093 thousand as of 31 March 2018 and belongs to Level 1 for which the quoted price in active market is used as valuation technique and key input.



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

(in thousands of KM)

As of 31 December 2017

	Carrying amount					Fair value			
	Loans and receivables	Available-for-sale	Held-to-maturity	Other financial liabilities	Total	Level 1	Level 2	Level 3	Total
<b>Financial assets measured at fair value</b>									
Debt securities	-	6,202,071	-	-	6,202,071	-	6,202,071	-	6,202,071
Other investments	-	27,813	-	-	27,813	-	27,813	-	27,813
<b>Financial assets not measured at fair value</b>									
Foreign currency in cash	236,402	-	-	-	236,402	-	236,402	-	236,402
Deposits with foreign banks	2,698,650	-	-	-	2,698,650	-	2,690,797	-	2,690,797
Special Drawing Rights with the IMF	1,531	-	-	-	1,531	-	1,531	-	1,531
Held-to-maturity investments	-	-	1,214,062	-	1,214,062	-	1,264,030	-	1,264,030
Other financial assets	2,746	-	-	-	2,746	-	2,746	-	2,746
<b>FINANCIAL ASSETS</b>	<b>2,939,329</b>	<b>6,229,884</b>	<b>1,214,062</b>	<b>-</b>	<b>10,383,275</b>	<b>-</b>	<b>10,425,390</b>	<b>-</b>	<b>10,425,390</b>
<b>Financial liabilities not measured at fair value</b>									
Currency in circulation	-	-	-	4,319,360	4,319,360	-	4,319,360	-	4,319,360
Deposits from banks	-	-	-	5,033,065	5,033,065	-	5,021,274	-	5,021,274
Deposits from the Government and other depositors	-	-	-	624,708	624,708	-	623,244	-	623,244
Other financial liabilities	-	-	-	10,510	10,510	-	10,510	-	10,510
<b>FINANCIAL LIABILITIES</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>9,987,643</b>	<b>9,987,643</b>	<b>-</b>	<b>9,974,388</b>	<b>-</b>	<b>9,974,388</b>

Fair value of monetary gold amounted to KM 203,908 thousand as of 31 December 2017 and belongs to Level 1 for which the quoted price in active market is used as valuation technique and key input

## **17. 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 Bank, they have not been included within the Bank's statement of financial position.

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

Off-balance sheet items consist of:

<b>(in thousands of KM)</b>	<b>31 March 2018</b>	<b>31 December 2017</b>
<b>Third party securities and funds held with foreign banks</b>	<b>47,726</b>	<b>43,566</b>
Deposits of USAID	2,897	2,825
<b>Deposits of non-residents</b>	<b>2,897</b>	<b>2,825</b>
Deposits of the Council of Ministers of BH	34,972	28,785
<i>Deposits of the Council of Ministers of BH on the basis of succession</i>	40	41
<i>Deposits of the Council of Ministers of BH regarding the servicing of foreign debt</i>	11,694	12,977
<i>Deposits of the Council of Ministers of BH regarding the Budget of BH institutions</i>	1,162	758
<i>Other deposits of the Council of Ministers of BH</i>	22,076	15,009
Deposits of other residents	9,675	9,922
<i>Deposits - Retirement allowances from Germany</i>	61	247
<i>Deposit accounts of banks</i>	9,614	9,675
<b>Deposits of residents</b>	<b>44,647</b>	<b>38,707</b>
Investments related to securities – Deposit Insurance Agency of BH	182	2,034
<b>Investments of residents related to securities</b>	<b>182</b>	<b>2,034</b>
<b>Liability for third party securities and funds</b>	<b>47,726</b>	<b>43,566</b>

## **BOSNIA AND HERZEGOVINA MEMBERSHIP IN THE IMF**

As depositary for BH membership in the IMF, the Bank maintains the IMF No. 1 and 2 accounts and provides a custodian service for the BH Promissory Notes issued to support the 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 BH in the relations with the IMF but does not have any responsibility for assets and liabilities related to the membership.

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

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

**Consolidated position of BH membership in the IMF as of 31 March 2018**

(in thousands of KM)

<b>Assets</b>		
Quota	611,961	
SDR holdings	1,740	
Accrued interest on SDR holdings	6	
<b>Total assets</b>	<b>613,707</b>	
<b>Liabilities</b>		
IMF No. 1 account		1,530
IMF No. 2 account		53
Securities		1,251,634
Accounts of payable charges		1,975
SDR allocation		371,253
Accrued interest on SDR allocation		494
<b>Total liabilities</b>		<b>1,626,939</b>
<b>Net member position with the IMF</b>		
BH liabilities to the IMF arising principally from repurchase and currency valuation adjustments	1,013,232	
<b>Net member position</b>	<b>1,013,232</b>	
	<b>1,626,939</b>	<b>1,626,939</b>
<b>The total consolidated position - assets and liabilities</b>		
IMF No. 1 account	(1,530)	(1,530)
IMF No. 2 account	(53)	(53)
<b>The total gross position of BH with the IMF - assets and liabilities</b>	<b>1,625,356</b>	<b>1,625,356</b>

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

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

## 17. OFF-BALANCE SHEET ITEMS (CONTINUED)

### Consolidated position of BH membership in the IMF as at 31 December 2017

(in thousands of KM)

<b>Assets</b>		
Quota	615,924	
SDR holdings	1,529	
Accrued interest on SDR holdings	2	
<b>Total assets</b>	<b>617,455</b>	
<b>Liabilities</b>		
IMF No. 1 account		1,540
IMF No. 2 account		53
Securities		1,205,738
Accounts of payable charges		1,898
SDR allocation		373,656
Accrued interest on SDR allocation		447
<b>Total liabilities</b>		<b>1,583,332</b>
<b>Net member position with the IMF</b>		
BH obligations to the IMF arising principally from repurchase and currency valuation adjustments	965,877	
<b>Net member position</b>	<b>965,877</b>	
	<b>1,583,332</b>	<b>1,583,332</b>
<b>Total consolidated position - assets and liabilities</b>		
	<b>1,583,332</b>	<b>1,583,332</b>
IMF No. 1 account	(1,540)	(1,540)
IMF No. 2 account	(53)	(53)
<b>Total gross position of BH with the IMF - assets and liabilities</b>	<b>1,581,739</b>	<b>1,581,739</b>

## 18. POST-REPORTING DATE EVENTS

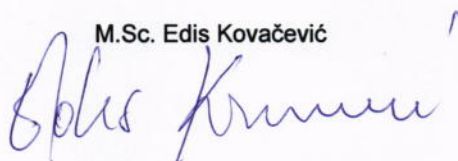
According to the relevant legal solutions, the Bank has transferred part of its profit for 2017 in the amount of KM 7,311 thousand to the account of the institution in charge for the budget of Bosnia and Herzegovina on 5 April 2018.

## 19. APPROVAL OF THE CONDENSED FINANCIAL STATEMENTS

These condensed financial statements have been approved by the Governing Board of the Bank on 24 April 2018.

Head of Accounting and Finance Department

M.Sc. Edis Kovačević



Chairman of the Governing Board

Ph.D. Senad Softić

