KOMERCIJALNA BANKA AD BEOGRAD

# ANNUAL REPORT OF A PUBLIC COMPANY FOR 2014

Belgrade, April 2015

# CONTENTS

# 1. PUBLIC COMPANY'S FINANCIAL STATEMENT

## 1.1. Balance -sheet as at december 31, 2014

| To be filled out by the bank | | | | | |
|---|---|---|---|---|---|
| Registration number: | 07737068 | Activity code: | 6419 | Tax identification number: | 100001931 |
| Name of the bank: | КОМЕРЦИЈАЛНА БАНКА АД БЕОГРАД | | | | |
| Bank's registered office: | БЕОГРАД, СВЕТОГ САВЕ 14 | | | | |

BALANCE SHEET
as of 31.12.2014.

(In RSD thousand)

| Group of accounts, account | POSITION | ADP code | Remark number | Current year | Previous year 2013 | Previous year 2012 |
|---|---|---|---|---|---|---|
| 1 | 2 | 3 | 4 | 5 | 6 | 7 |
| 00 without 002, 010, 025, 05 (exept 050, 052 and part of 059), 060, 07, 085, 196, 296 and parts of 009, 019, 029, 069, 089, 199 and 299 | **ASSETS**<br>Cash and balances with central banks | 0001 | 3к; 19 | 68.547.389 | 70.934.839 | 65.480.687 |
| | Pledged funds | 0002 | | - | - | - |
| 120, 220, 125 и 225 | Financial assets at fair value through profit or loss held for trading | 0003 | 3 л; 20 | 121.634 | 115.319 | 212.690 |
| 121, 221 | Financial assets initially recognized at fair value through profit or loss | 0004 | | - | - | - |
| 122, 222, parts of 129, 229 | Financial assets available for sale | 0005 | 3н; 21 | 95.481.249 | 56.885.285 | 41.085.776 |
| 124, 224, parts of 129, 229 | Financial assets held to maturity | 0006 | 3н; 22 | 51.442 | 149.900 | 349.807 |
| 002, 01 (except 010 and part of 019), part of 020, 028, 050, 052, 06 (except 060 and part of 069), 080, 088, 10, 11, 16, 20, 21, 26, 190, 191, 290, 291, part of 493 and 593 as deductible items (SSKR - SS code 1 (except code 17), code 70 and parts of codes 71 and 74) and parts of 009, 029, 059, 089, 199 and 299 | Loans and advances to banks and other financial institutions | 0007 | 3м; 23 | 34.737.605 | 35.247.935 | 22.566.291 |
| 01 (except 010 and part of 019), part of 020, 028, 06 (except 060 and part of 069), 080, 088, 10, 11, 16, 20, 21, 26, 190, 191, 290, 291, part of 493 and 593 as deductible items (SSKR - SS code 17 and all other codes except the code 70 and parts of codes 71 and 74) and parts of 029, 069, 089, 199 and 299 | Loans and advancest to clients | 0008 | 3м; 24 | 185.377.035 | 177.560.058 | 176.904.911 |
| 123, 223 | Changes in fair value of items that are the subject of hedging | 0009 | | - | - | - |
| 126, 226 | Receivables from financial derivatives held for hedging | 0010 | | - | - | - |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| 130, 131, 230, 231, part of 139 and 239 | Investments in associates and joint ventures | 0 | 0 | 1 | 1 | | - | - | - |
| 132, 232, part of 139 and 239 | Investments in subsidiaries | 0 | 0 | 1 | 2 | 3н; 25 | 5.480.888 | 5.480.888 | 5.480.888 |
| 33 | Intangible assets | 0 | 0 | 1 | 3 | 3л; 26 | 405.774 | 537.445 | 600.438 |
| 34 | Property, plant and equipment | 0 | 0 | 1 | 4 | 3o; 27 | 6.329.077 | 6.577.670 | 5.690.613 |
| 35 | Investment property | 0 | 0 | 1 | 5 | 3љ; 28 | 2.581.144 | 1.808.554 | 1.726.233 |
| 034 and part of 039 | Current tax assets | 0 | 0 | 1 | 6 | 29 | 73.835 | 712.700 | 12.784 |
| 37 | Deferred tax assets | 0 | 0 | 1 | 7 | | - | - | 4.896 |
| 36 | Non-current assets held for sale and assets of discontinued operations | 0 | 0 | 1 | 8 | 31 | 84.227 | 71.630 | 78.763 |
| 021, 022, 024, 027, 03 (except 034 and part of 039), 081, 082, 084, 087, 09, 134,192, 194, 195, 234, 292, 294, 295, 30, 38 and parts of 029, 089, 139, 199, 239 and 299 | Other assets | 0 | 0 | 1 | 9 | 3н; 32 | 6.990.225 | 6.704.096 | 3.190.132 |
| **TOTAL ASSETS** (from 0001 to 0019) | | 0 | 0 | 2 | 0 | | **406.261.524** | **362.786.319** | **323.384.909** |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | **LIABILITIES** | | | | | | | | |
| 411, 416, 511, 516 | Financial liabilities at fair value through profit or loss held for trading | 0 | 4 | 0 | 1 | | - | - | - |
| 415, 515 | Financial liabilities initially recognized at fair value through profit or loss | 0 | 4 | 0 | 2 | | - | - | - |
| 417, 517 | Liabilities from financial derivatives held for hedging | 0 | 4 | 0 | 3 | | - | - | - |
| parts of 40, 420, 421, 490, 50, 520, 521, 590, and parts of 193 and 293 as deductible items (SSKR - SS code 1 (without code 17) and code 70 and parts of codes 71 and 74) | Deposits and other liabilities to banks, other financial institutions and the central bank | 0 | 4 | 0 | 4 | 3т; 33 | 23.743.018 | 21.058.542 | 13.343.870 |
| parts of 40, 420, 421, 490, 50, 520, 521, 590, and parts of 193 and 293 as deductible items (SSKR - SS code 17 and all other codes, except code 70 and parts of codes 71 and 74) | Deposits and other liabilities to other clients | 0 | 4 | 0 | 5 | 3т; 34 | 301.954.911 | 266.020.289 | 240.055.122 |
| 418, 518 | Changes in fair value of items that are the subject of hedging | 0 | 4 | 0 | 6 | | - | - | - |
| 410, 412, 423, 496, 510, 512, 523, 596 and 127 as deductible items | Issued own securities and other borrowed funds | 0 | 4 | 0 | 7 | | - | - | - |
| 424, 425, 482, 497, 524, 525, 582, 597 and parts of 193 and 293 as deductible items | Subordinated liabilities | 0 | 4 | 0 | 8 | 3т; 35 | 6.036.680 | 5.711.409 | 5.654.932 |
| 450, 451, 452, 453 , 454 | Provisions | 0 | 4 | 0 | 9 | 3у; 36 | 1.640.595 | 765.132 | 2.331.760 |
| 46 | Liabilities from non-current assets held for sale and assets of discontinued operations | 0 | 4 | 1 | 0 | | - | - | - |
| 455 | Current tax liabilities | 0 | 4 | 1 | 1 | | - | - | - |
| 47 | Deferred tax liabilities | 0 | 4 | 1 | 2 | 18.3; 30.2. | 150.407 | 10.156 | - |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| 426, 427, 43, 44, 456, 457, 491, 492, 494, 495, 526, 527, 53, 591, 592, 594, 595 | Other liabilities | 0 | 4 | 1 | 3 | 37 | 3.189.109 | 4.258.573 | 2.132.665 |
| | **TOTAL LIABILITIES** (from 0401 to 0413) | 0 | 4 | 1 | 4 | | **336.714.720** | **297.824.101** | **263.518.349** |
| 80 | EQUITY<br>Equity | 0 | 4 | 1 | 5 | 3x; 38.1. | 40.034.550 | 40.034.550 | 40.034.550 |
| 128 | Own shares | 0 | 4 | 1 | 6 | | - | - | - |
| 83 | Profit | 0 | 4 | 1 | 7 | | 6.755.855 | 6.687.971 | 4.185.812 |
| 84 | Loss | 0 | 4 | 1 | 8 | | - | - | - |
| 81, 82 - credit balance | Reserves | 0 | 4 | 1 | 9 | 3x; 38.1. | 22.756.399 | 18.239.697 | 15.646.198 |
| 81, 82 - debit balance | Unrealized losses | 0 | 4 | 2 | 0 | | - | - | - |
| | Shares without control | 0 | 4 | 2 | 1 | | | - | - |
| | TOTAL EQUITY (0415 - 0416 + 0417 - 0418 + 0419 - 0420 + 0421) ≥ 0 | 0 | 4 | 2 | 2 | | 69.546.804 | 64.962.218 | 59.866.560 |
| | TOTAL DEFICIENCY OF CAPITAL (0415 - 0416 + 0417 - 0418 + 0419 - 0420 + 0421) < 0 | 0 | 4 | 2 | 3 | | - | - | - |
| | **TOTAL LIABILITIES** (0414 + 0422 - 0423) | 0 | 4 | 2 | 4 | | **406.261.524** | **362.786.319** | **323.384.909** |

In Belgrade, Legal representative of the bank

on 27.02.2015. ______________________

## *1.2. Income Statement for the period 01.01. to 31.12.2014*

| To be filled out by the bank | | | | | |
|---|---|---|---|---|---|
| Registration number: | 07737068 | Activity code: | 6419 | Tax identification number: | 100001931 |
| Name of the bank: | КОМЕРЦИЈАЛНА БАНКА АД БЕОГРАД | | | | |
| Bank's registered office: | БЕОГРАД, СВЕТОГ САВЕ 14 | | | | |

INCOME STATEMENT
in period from January 1st to December 31st, 2014.

(In RSD thousend)

| Group of accounts, account | POSITION | ADP code | Remark number | Current year | Previous year |
|---|---|---|---|---|---|
| 1 | 2 | 3 | 4 | 5 | 6 |
| 70 | Interest income | 1001 | 3ц; 8 | 21.224.379 | 22.023.774 |
| 60 | Interest expenses | 1002 | 3ц; 8 | 7.925.793 | 9.094.536 |
| **Net interest profit (1001-1002)** | | 1003 | | **13.298.586** | **12.929.238** |
| **Net interest loss (1002-1001)** | | 1004 | | - | - |
| 71 | Fee and commission income | 1005 | 3д; 9 | 5.677.040 | 5.493.211 |
| 61 | Fee and commission expenses | 1006 | 3д; 9 | 959.283 | 928.063 |
| **Net fee and commission income (1005 - 1006)** | | 1007 | | **4.717.757** | **4.565.148** |
| **Net fee and commission expenses (1006 - 1005)** | | 1008 | | - | - |
| 720 - 620 + 771 - 671 + 774 - 674 | Net gains on financial assets held for trading | 1009 | 3е; 10 | 6.076 | 22.342 |
| 620 - 720 + 671 - 771 + 674 - 774 | Net loss on financial assets held for trading | 1010 | | - | - |
| 775-675+770-670 | Net gains from risk protection | 1011 | | - | - |
| 675-775+670-770 | Net loss from risk protection | 1012 | | - | - |
| 725 - 625 + 776 - 676 | Net gains on financial assets that are initially recognized at fair value through profit or loss | 1013 | | - | - |
| 625 - 725 + 676 - 776 | Net losses on financial assets that are initially recognized at fair value through profit or loss | 1014 | | - | - |
| 721 - 621 | Net profit from sale of securities | 1015 | 11 | 51.282 | 1.738 |
| 621 - 721 | Net loss from sale of securities | 1016 | | - | - |
| 78 - 68 | Net income from foreign exchange differences and effects of contracted foreign currency clause | 1017 | | - | - |
| 68 - 78 | Net foreign exchange losses and the effects of contracted foreign currency clause | 1018 | 3б; 12 | 205.943 | 48.733 |
| 723 - 623 | Net gains on investments in associates and joint ventures | 1019 | | - | - |
| 623 - 723 | Net loss on investments in associates and joint ventures | 1020 | | - | - |
| 724, 74, 752, 753, 76 (except 760, 769), 772, 773 | Other operating income | 1021 | 3г; 3у; 13 | 569.191 | 1.123.546 |
| 750 - 650 + 751 - 651 + 760 - 660 | Net income from reversal of impairment of financial assets and off-balance sheet credit risk items | 1022 | | - | - |
| 650 - 750 + 651 - 751 + 660 - 760 | Net impairment losses of financial assets and off-balance sheet credit risk items | 1023 | 5; 14 | 2.725.389 | 3.220.075 |
| **NET OPERATING PROFIT (1003 - 1004 + 1007 - 1008 + 1009 - 1010 + 1011 - 1012 + 1013 - 1014 + 1015 - 1016 + 1017 - 1018 + 1019 - 1020 + 1021 + 1022 - 1023) ≥ 0** | | 1024 | | **15.711.560** | **15.373.204** |
| **NET OPERATING LOSS (1003 - 1004 + 1007 - 1008 + 1009 - 1010 + 1011 - 1012 + 1013 - 1014 + 1015 - 1016 + 1017 - 1018 + 1019 - 1020 + 1021 + 1022 - 1023) < 0** | | 1025 | | - | - |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| 63, 655, 755 | Saleries, wages, and other personnel indemnities | 1 | 0 | 2 | 6 | 15 | 4.211.489 | 4.262.123 |
| 642 | Depreciation costs | 1 | 0 | 2 | 7 | 3o; 16 | 844.632 | 792.648 |
| 64 (except 642), 624, 652, 653, 66 (except 660, 669), 672, 673 | Other expenses | 1 | 0 | 2 | 8 | 3x; 17 | 5.897.850 | 5.730.058 |
| **PROFIT FROM CONTINUING OPERATIONS BEFORE TAX (1024 - 1025 - 1026 - 1027 - 1028) ≥ 0** | | 1 | 0 | 2 | 9 | | **4.757.589** | **4.588.375** |
| **LOSS FROM CONTINUING OPERATIONS BEFORE TAX (1024 - 1025 - 1026 - 1027 - 1028) < 0** | | 1 | 0 | 3 | 0 | | **-** | **-** |
| 850 | Tax on profit | 1 | 0 | 3 | 1 | | - | - |
| 861 | Deffered tax income for the period | 1 | 0 | 3 | 2 | 3и; 18.1. | 47.547 | 87.950 |
| 860 | Deffered tax expense for the period | 1 | 0 | 3 | 3 | 3и; 18.1. | 19.559 | - |
| **PROFIT FROM CONTINUING OPERATIONS AFTER TAX (1029 - 1030 - 1031 + 1032 - 1033) ≥ 0** | | 1 | 0 | 3 | 4 | | **4.785.577** | **4.676.325** |
| **LOSS FROM CONTINUING OPERATIONS AFTER TAX(1029 - 1030 - 1031 + 1032 - 1033) < 0** | | 1 | 0 | 3 | 5 | | - | - |
| 769 - 669 | NET PROFIT OF DISCONTINUED OPERATIONS | 1 | 0 | 3 | 6 | | - | - |
| 669 - 769 | NET LOSS OF DISCONTINUED OPERATIONS | 1 | 0 | 3 | 7 | | - | - |
| | **NET PROFIT (1034 - 1035 + 1036 - 1037) ≥ 0** | 1 | 0 | 3 | 8 | | **4.785.577** | **4.676.325** |
| | **NET LOSS (1034 - 1035 + 1036 - 1037) < 0** | 1 | 0 | 3 | 9 | | **-** | **-** |
| | Net profit which belongs to owners of parent legal entity | 1 | 0 | 4 | 0 | | - | - |
| | Net profit which belongs to minority investors | 1 | 0 | 4 | 1 | | - | - |
| | Net loss which belongs to owners of parent legal entity | 1 | 0 | 4 | 2 | | - | - |
| | Net loss which belongs to minority investors | 1 | 0 | 4 | 3 | | - | - |
| | Earnings per share | | | | | | - | - |
| | Basic earnings per share (in RSD, rounded) | 1 | 0 | 4 | 4 | 3ж; 38 | 253 | 468 |
| | Diluted earnings per share (in RSD, rounded) | 1 | 0 | 4 | 5 | 3ж; 38 | 253 | 242 |

In Belgrade,

on 27.02.2015.

Legal representative of the bank

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## *1.3. Report on other results in the period 01.01. to 31.12.2014*

| To be filled out by the bank | | | |
|---|---|---|---|
| Registration number: 07737068 | Activity code: 6419 | Tax identification number: 100001931 | |
| Name of the bank: КОМЕРЦИЈАЛНА БАНКА АД БЕОГРАД | | | |
| Bank's registered office: БЕОГРАД, СВЕТОГ САВЕ 14 | | | |

OTHER FINANCIAL RESULT
January 1 to December 31, 2014

(In RSD thousand)

| Accounting year | ITEM | ADP flag | | | | Remark No. | Current year | Last year |
|---|---|---|---|---|---|---|---|---|
| 1 | 2 | 3 | | | | 4 | 5 | 6 |
| | PROFIT FOR PERIOD | 2 | 0 | 0 | 1 | | 4.785.577 | 4.676.325 |
| | LOSS FOR PERIOD | 2 | 0 | 0 | 2 | | - | - |
| 820 | Other result for the period<br>Components of other results that cannot be reclassified to profit or loss:<br>The increase in revaluation reserves based on intangible assets and fixed assets | 2 | 0 | 0 | 3 | | - | 711.119 |
| 820 | Decrease in revaluation reserves based on intangible assets and fixed assets | 2 | 0 | 0 | 4 | 38.2. | 3.472 | 24.439 |
| 822 | Actuarial gains | 2 | 0 | 0 | 5 | | - | - |
| 822 | Actuarial gains | 2 | 0 | 0 | 6 | 36; 38.2. | 27.779 | - |
| 825 | The positive effects of the changes in values arising from other components of other results that cannot be reclassified to profit or loss | 2 | 0 | 0 | 7 | | - | - |
| 825 | The negative effects of changes in the values based on other components of other results that cannot be reclassified to profit or loss | 2 | 0 | 0 | 8 | | - | - |
| 821 | The components of other results that may be reclassified to profit or loss:<br>The positive effects of fair value adjustments on financial assets available for sale | 2 | 0 | 0 | 9 | 38.2. | 695.067 | 349.854 |
| 823 | Unrealized losses on securities available for sale | 2 | 0 | 1 | 0 | 38.2. | 83.726 | 179.995 |
| 824 | Gains on hedging instruments in cash flow (cash flow hedges) | 2 | 0 | 1 | 1 | | - | - |
| 824 | Losses on hedging instruments in cash flow (cash flow hedges) | 2 | 0 | 1 | 2 | | - | - |
| 826 | Positive cumulative differences arising from exchange rate revaluation of foreign transactions | 2 | 0 | 1 | 3 | | - | - |
| 826 | Negative cumulative differences arising from exchange rate revaluation of foreign transaction | 2 | 0 | 1 | 4 | | | |
| 826 | The positive effects of changes in the values based on other components of other results that may be reclassified to profit or loss | 2 | 0 | 1 | 5 | | - | - |
| 826 | The negative effects of changes in the values based on other components of other results that may be reclassified to profit or loss | 2 | 0 | 1 | 6 | | - | - |
| 82 | Net tax income relating to other result of the period | 2 | 0 | 1 | 7 | 38.2. | 45.412 | - |
| 82 | Net tax losses relating to other result of period | 2 | 0 | 1 | 8 | 30.1.; 38.2. | 213.650 | 103.002 |
| | Total other positive result for the period (2003 - 2004 + 2005 - 2006 + 2007 - 2008 + 2009 - 2010 + 2011 - 2012 + 2013 - 2014 + 2015 - 2016 + 2017 - 2018) ≥ 0 | 2 | 0 | 1 | 9 | | 411.852 | 753.537 |
| | Total negative result for the period (2003 - 2004 + 2005 - 2006 + 2007 - 2008 + 2009 - 2010 + 2011 - 2012 + 2013 - 2014 + 2015 - 2016 + 2017 - 2018) < 0 | 2 | 0 | 2 | 0 | | - | - |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | TOTAL POSITIVE RESULT FOR THE PERIOD (2001 - 2002 + 2019 - 2020) ≥ 0 | 2 | 0 | 2 | 1 | | 5.197.429 | 5.429.862 |
| | TOTAL NEGATIVE RESULT FOR THE PERIOD (2001 - 2002 + 2019 - 2020) < 0 | 2 | 0 | 2 | 2 | | - | - |
| | Total positive result for the period belonging to the parent entity | 2 | 0 | 2 | 3 | | - | - |
| | The total positive result for the period attributable to non-controlling owners | 2 | 0 | 2 | 4 | | - | - |
| | The total negative result for the period belonging to the parent entity | 2 | 0 | 2 | 5 | | - | - |
| | The total negative result for the period attributable to non-controlling owners | 2 | 0 | 2 | 6 | | - | - |

In Belgrade, Legal representative of the bank

on 27.02.2015. ______________________

### *1.4. Cash flow Statement for the period 01.01. to 31.12.2014*

| To be filled out by the bank | | |
|---|---|---|
| Registration number: 07737068 | Activity code: 6419 | Tax identification number: 100001931 |
| Name of the bank: КОМЕРЦИЈАЛНА БАНКА АД БЕОГРАД | | |
| Bank's registered seat: БЕОГРАД, СВЕТОГ САВЕ 14 | | |

CASH FLOW STATEMENT
in period from 1.01. to 31.12.2014.

(In RSD thousand)

| | POSITION | ADP code | | | | Current year | Previous year |
|---|---|---|---|---|---|---|---|
| | 1 | 2 | | | | 3 | 4 |
| A.<br>I. | **CASH FLOWS FROM OPERATING ACTIVITIES**<br>**Cash inflows from operating activities (from 3002 to 3005)** | 3 | 0 | 0 | 1 | **26.173.313** | **26.515.177** |
| 1. | Inflows from Interest | 3 | 0 | 0 | 2 | 20.196.420 | 20.455.890 |
| 2. | Inflows from allowances | 3 | 0 | 0 | 3 | 5.661.699 | 5.493.457 |
| 3. | Inflows from other operating income | 3 | 0 | 0 | 4 | 204.599 | 209.753 |
| 4. | Inflows from dividends and participation in profit | 3 | 0 | 0 | 5 | 110.595 | 356.077 |
| II. | **Cash outflows from operating activities (from 3007 to 3011)** | 3 | 0 | 0 | 6 | **19.051.974** | **19.690.614** |
| 5. | Outflows from interest | 3 | 0 | 0 | 7 | 8.072.315 | 8.948.540 |
| 6. | Outflows from allowances | 3 | 0 | 0 | 8 | 960.358 | 929.932 |
| 7. | Outflows from gross salleries, wages and other personnel indemnities | 3 | 0 | 0 | 9 | 4.003.672 | 4.318.918 |
| 8. | Outflows from taxes, contributions and other obligations from income | 3 | 0 | 1 | 0 | 798.934 | 927.771 |
| 9 | Outflows from other operating expenses | 3 | 0 | 1 | 1 | 5.216.695 | 4.565.453 |
| III. | **Net cash inflow from operating activities prior to increase or decrease in advances and deposits (3001 - 3006)** | 3 | 0 | 1 | 2 | **7.121.339** | **6.824.563** |
| IV. | **Net cash outflow from operating activities prior to increase or decrease in advances and deposits (3006 - 3001)** | 3 | 0 | 1 | 3 | - | - |
| V. | **Decrease in loans and increase in deposits and other liabilities (from 3015 to 3020)** | 3 | 0 | 1 | 4 | **32.605.699** | **23.508.143** |
| 10. | Decrease in loans and advances to banks, other financial institutions, central bank and other clients | 3 | 0 | 1 | 5 | 5.760.091 | - |
| 11. | Decrease of financial assets that are initially recognized at fair value through profit or loss, financial assets held for trading and other securities that are not intended for investment | 3 | 0 | 1 | 6 | - | 1.850.488 |
| 12. | Decrease in receivables from financial derivatives held for hedging and fair value adjustments of items that are the subject of hedging | 3 | 0 | 1 | 7 | - | - |
| 13. | Increase in deposits and other liabilities to banks, other financial institutions, central banks and other clients | 3 | 0 | 1 | 8 | 26.845.608 | 21.657.655 |
| 14. | Increase in financial liabilities initially recognized at fair value through profit or loss and financial liabilities held for trading | 3 | 0 | 1 | 9 | - | - |
| 15. | Increase in liabilities from financial derivatives held for hedging and fair value adjustments of items that are the subject of hedging | 3 | 0 | 2 | 0 | - | - |
| VI. | **Increase in loans and decrease in deposits and other liabilities (from 3022 to 3027)** | 3 | 0 | 2 | 1 | **4.633.940** | **24.137.331** |
| 16. | Increase in loans and advances to banks, other financial institutions, central bank and other clients | 3 | 0 | 2 | 2 | - | 24.137.331 |
| 17. | Increase in financial assets that are initially recognized at fair value through profit or loss, financial assets held for trading and other securities that are not intended for investment | 3 | 0 | 2 | 3 | 4.633.940 | - |
| 18. | Increase in receivables from financial derivatives held for hedging and fair value adjustments of items that are the subject of hedging | 3 | 0 | 2 | 4 | - | - |
| 19. | Decrease in deposits and other liabilities to banks, other financial institutions, central bank and other clients | 3 | 0 | 2 | 5 | - | - |
| 20. | Decrease of financial liabilities initially recognized at fair value | 3 | 0 | 2 | 6 | - | - |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| | through profit or loss and financial liabilities held for trading | | | | | | |
| 21. | Decrease of liabilities from financial derivatives held for hedging and fair value adjustments of items that are the subject of hedging | 3 | 0 | 2 | 7 | - | - |
| **VII.** | **Net cash inflow from operating activities before tax (3012 - 3013 + 3014 - 3021)** | 3 | 0 | 2 | 8 | **35.093.098** | **6.195.375** |
| **VIII.** | **Net cash outflow from operating activities before tax (3013 - 3012 + 3021 - 3014)** | 3 | 0 | 2 | 9 | - | - |
| 22. | Profit tax paid | 3 | 0 | 3 | 0 | - | 699.916 |
| 23. | Dividends paid | 3 | 0 | 3 | 1 | 485.151 | 269.195 |
| **IX.** | **Net cash inflow from operating activities (3028 - 3029 - 3030 - 3031)** | 3 | 0 | 3 | 2 | **34.607.947** | **5.226.264** |
| **X.** | **Net cash outflow from operating activities (3029 - 3028 + 3030 + 3031)** | 3 | 0 | 3 | 3 | - | - |
| | | | | | | | |
| **Б. I.** | **CASH FLOWS FROM INVESTING ACTIVITIES Cash inflows from investing activities (од 3035 до 3039)** | 3 | 0 | 3 | 4 | **18.126.491** | **14.283.199** |
| 1. | Inflows from long-term investment in securities | 3 | 0 | 3 | 5 | 18.117.937 | 14.271.063 |
| 2. | Inflows from sale of investments in subsidiaries and associates and joint ventures | 3 | 0 | 3 | 6 | - | - |
| 3. | Inflows from sale of intangible assets, property, plant and equipment | 3 | 0 | 3 | 7 | 8.554 | 12.136 |
| 4. | Inflow of sale of investment property | 3 | 0 | 3 | 8 | - | - |
| 5. | Other inflows from investing activities | 3 | 0 | 3 | 9 | - | - |
| **II.** | **Cash outflows from investing activities (from 3041 to 3045)** | 3 | 0 | 4 | 0 | **49.181.554** | **32.336.193** |
| 6. | Outflows from investment in long-term securities | 3 | 0 | 4 | 1 | 48.706.989 | 31.584.013 |
| 7. | Outflows from purchase of investments in subsidiaries and associates and joint ventures | 3 | 0 | 4 | 2 | - | 976 |
| 8. | Outflows from purchase of sale of intangible assets, property, plant and equipment | 3 | 0 | 4 | 3 | 474.565 | 751.204 |
| 9. | Outflows from purchase of investment property | 3 | 0 | 4 | 4 | - | - |
| 10. | Other outflows from investing activities | 3 | 0 | 4 | 5 | - | - |
| **III.** | **Net cash inflow from investing activities (3034 - 3040)** | 3 | 0 | 4 | 6 | - | - |
| **IV.** | **Net cash outflow from investing activities (3040 - 3034)** | 3 | 0 | 4 | 7 | **31.055.063** | **18.052.994** |
| **B. I.** | **CASH FLOWS FROM FINANCING ACTIVITIES Cash inflows from financing activities (from 3049 to 3054)** | 3 | 0 | 4 | 8 | **208.836.248** | **219.234.820** |
| 1. | Inflows from capital increase | 3 | 0 | 4 | 9 | - | - |
| 2. | Cash inflows from subordinated obligations | 3 | 0 | 5 | 0 | - | - |
| 3. | Cash inflows from loans received | 3 | 0 | 5 | 1 | 208.836.248 | 219.234.820 |
| 4. | Inflows from securities | 3 | 0 | 5 | 2 | - | - |
| 5. | Inflows from sale of own shares | 3 | 0 | 5 | 3 | - | - |
| 6. | Other inflows from financing activities | 3 | 0 | 5 | 4 | - | - |
| **II.** | **Cash outflows from financing activities (from 3056 to 3060)** | 3 | 0 | 5 | 5 | **208.645.771** | **206.115.732** |
| 7. | Outflows from purchase of own shares | 3 | 0 | 5 | 6 | - | - |
| 8. | Cash outflows from subordinated obligations | 3 | 0 | 5 | 7 | - | - |
| 9. | Cash outflows from loans received | 3 | 0 | 5 | 8 | 208.645.771 | 206.115.732 |
| 10. | Cash outflows from securities | 3 | 0 | 5 | 9 | - | - |
| 11. | Other outflows from financing activities | 3 | 0 | 6 | 0 | - | - |
| **III.** | **Net cash inflow from financing activities (3048 - 3055)** | 3 | 0 | 6 | 1 | **190.477** | **13.119.088** |
| **IV.** | **Net cash outflow from financing activities (3055 - 3048)** | 3 | 0 | 6 | 2 | - | - |
| **Г.** | **TOTAL NET CASH INFLOWS (3001 + 3014 + 3034 + 3048)** | 3 | 0 | 6 | 3 | 285.741.751 | 283.541.339 |
| **Д.** | **TOTAL NET CASH OUTFLOWS (3006 + 3021 + 3030 + 3031 + 3040 + 3055)** | 3 | 0 | 6 | 4 | 281.998.390 | 283.248.981 |
| **Ђ.** | **NET INCREASE IN CASH (3063 - 3064)** | 3 | 0 | 6 | 5 | **3.743.361** | **292.358** |
| **E.** | **NET DECREASE IN CASH (3064 - 3063)** | 3 | 0 | 6 | 6 | - | - |
| **Ж.** | **CASH AT THE BEGINNING OF THE YEAR** | 3 | 0 | 6 | 7 | **40.297.749** | **39.900.993** |
| **З.** | **PROFIT ON EXCHANGE** | 3 | 0 | 6 | 8 | 1.201.216 | 936.537 |
| **И.** | **LOSS ON EXCHANGE** | 3 | 0 | 6 | 9 | 82.149 | 832.139 |
| **J.** | **CASH AT END OF PERIOD (3065 - 3066 + 3067+ 3068 - 3069)** | 3 | 0 | 7 | 0 | **45.160.177** | **40.297.749** |

In Belgrade,

on 27.02.2015.

Legal representative of the bank

## 1.5. Statement of changes in equity for the period 01.01. to 31.12.2014

| No | ITEM | ADP code | Share and other capital (accounts 800,801,803) | ADP code | Own shares (account 128) | ADP code | Issue premium (account 802) | ADP code | Reserves from profit and other reserves (account group 81) | ADP code | Revaluation reserves (account group 82 credit balance) | ADP code | Revaluation reserves (account group 82 debit balance) | ADP code | Profit (account group 83) | ADP code | Loss (accounts 840,841,842) | ADP code | Total (column 2-3+4+5+6-7+8-9)≥0 | ADP code | Total (column 2-3+4+5+6-7+8-9)<0 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1 | | 2 | | 3 | | 4 | | 5 | | 6 | | 7 | | 8 | | 9 | | 10 | | 11 |
| 1. | **Opening balance as of January 1st of preceding year** | 4001 | 17.191.466 | 4029 | | 4057 | 22.843.084 | 4085 | 14.785.440 | 4113 | 867.774 | 4127 | 7.016 | 4141 | 4.185.812 | 4175 | | 4209 | 59.866.560 | 4215 | - |
| 2. | Correction of material misstatement and changes to accounting policies in preceding year – increase | 4002 | | 4030 | | 4058 | | 4086 | | 4114 | | 4128 | | 4142 | | 4176 | | x | x | x | x |
| 3. | Correction of material misstatement and changes to accounting policies in preceding year – decrease | 4003 | | 4031 | | 4059 | | 4087 | | 4115 | | 4129 | | 4143 | | 4177 | | x | x | x | x |
| 4. | **Adjusted opening balance as of January 1st of preceding year (number 1+2-3)** | 4004 | 17.191.466 | 4032 | 0 | 4060 | 22.843.084 | 4088 | 14.785.440 | 4116 | 867.774 | 4130 | 7.016 | 4144 | 4.185.812 | 4178 | - | 4210 | 59.866.560 | 4216 | - |
| 5. | Total positive other result for the period | x | x | x | x | x | x | x | x | 4117 | 923.494 | 4131 | | x | x | x | x | x | x | x | x |
| 6. | Total negative other result for the period | x | x | x | x | x | x | x | x | 4118 | | 4132 | 179.995 | x | x | x | x | x | x | x | x |
| 7. | Profit for the year | x | x | x | x | x | x | x | x | x | x | x | x | 4145 | 4.676.325 | x | x | x | x | x | x |
| 8. | Loss for the year | x | x | x | x | x | x | x | x | x | x | x | x | x | x | 4179 | | x | x | x | x |
| 9. | Transfer from reserves to result due to release of reserves – increase | x | x | x | x | x | x | x | x | x | x | x | x | 4146 | | 4180 | | x | x | x | x |
| 10. | Transfer from reserves to result due to release of reserves - decrease | x | x | x | x | x | x | x | x | x | x | x | x | 4147 | | 4181 | | x | x | x | x |
| 11. | Transactions with owners, recorded directly in equity – increase | 4005 | | 4033 | | 4061 | | 4089 | | x | x | x | x | 4148 | | 4182 | | x | x | x | x |
| 12. | Transactions with owners, recorded directly in equity – decrease | 4006 | | 4034 | | 4062 | | 4090 | | x | x | x | x | 4149 | | 4183 | | x | x | x | x |
| 13. | Profit distribution – increase | 4007 | | 4035 | | 4063 | | 4091 | 1.850.000 | x | x | x | x | 4150 | | 4184 | | x | x | x | x |
| 14. | Profit distribution, and/or loss coverage – decrease | 4008 | | 4036 | | 4064 | | 4092 | | x | x | x | x | 4151 | 1.850.000 | 4185 | | x | x | x | x |
| 15. | Dividend payments | 4009 | | 4037 | | 4065 | | 4093 | | x | x | x | x | 4152 | 37.351 | 4186 | | x | x | x | x |
| 16. | Other – increase | 4010 | | 4038 | | 4066 | | 4094 | | x | x | x | x | 4153 | 10.038 | 4187 | | x | x | x | x |
| 17. | Other – decrease | 4011 | | 4039 | | 4067 | | 4095 | | x | x | x | x | 4154 | 296.853 | 4188 | | x | x | x | x |
| 18. | **Total transactions with owners (number 11-12+13-14-15+16-17) ≥ 0** | 4012 | 0 | 4040 | 0 | 4068 | 0 | 4096 | 1.850.000 | x | x | x | x | 4155 | - | 4189 | - | x | x | x | x |
| 19. | **Total transactions with owners (number 11-12+13-14-15+16-17) < 0** | 4013 | 0 | 4041 | 0 | 4069 | 0 | 4097 | - | x | x | x | x | 4156 | 2.174.166 | 4190 | - | x | x | x | x |
| 20. | **Balance as of December 31st of preceding year (number 4+5-6+7+8+9-10+18-19 for columns from 2,3,4,5,6,8,9), for column 7 (number 4+6-5)** | 4014 | 17.191.466 | 4042 | 0 | 4070 | 22.843.084 | 4098 | 16.635.440 | 4119 | 1.791.268 | 4133 | 187.011 | 4157 | 6.687.971 | 4191 | - | 4211 | 64.962.218 | 4217 | - |

| No | ITEM | ADP code | Share and other capital (accounts 800,801,803) | ADP code | Own shares (account 128) | ADP code | Issue premium (account 802) | ADP code | Reserves from profit and other reserves (account group 81) | ADP code | Revaluation reserves (account group 82 credit balance) | ADP code | Revaluation reserves (account group 82 debit balance) | ADP code | Profit (account group 83) | ADP code | Loss (accounts 840,841, 842) | ADP code | Total (column 2-3+4+5+6-7+8-9)≥0 | ADP code | Total (column 2-3+4+5+6-7+8-9)<0 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1 | | 2 | | 3 | | 4 | | 5 | | 6 | | 7 | | 8 | | 9 | | 10 | | 11 |
| 21. | **Opening balance as of January 1st of the current year** | 4015 | 17.191.466 | 4043 | | 4071 | 22.843.084 | 4099 | 16.635.440 | 4120 | 1.791.268 | 4134 | 187.011 | 4158 | 6.687.971 | 4192 | | 4212 | 64.962.218 | 4218 | - |
| 22. | Correction of material misstatement and changes to accounting policies in preceding year – increase | 4016 | | 4044 | | 4072 | | 4100 | | 4121 | | 4135 | | 4159 | | 4193 | | x | x | x | x |
| 23. | Correction of material misstatement and changes to accounting policies in preceding year – decrease | 4017 | | 4045 | | 4073 | | 4101 | | 4122 | | 4136 | | 4160 | | 4194 | | x | x | x | x |
| 24. | **Adjusted opening balance as of January 1st of the current year (number 21+22-23)** | 4018 | 17.191.466 | 4046 | 0 | 4074 | 22.843.084 | 4102 | 16.635.440 | 4123 | 1.791.268 | 4137 | 187.011 | 4161 | 6.687.971 | 4195 | 0 | 4213 | 64.962.218 | 4219 | - |
| 25. | Total positive other result for the period | x | x | x | x | x | x | x | x | 4124 | 559.817 | 4138 | | x | x | x | x | x | x | x | x |
| 26. | Total negative other result for the period | x | x | x | x | x | x | x | x | 4125 | | 4139 | 43.115 | x | x | x | x | x | x | x | x |
| 27. | Profit for the year | x | x | x | x | x | x | x | x | x | x | x | x | 4162 | 4.785.577 | x | x | x | x | x | x |
| 28. | Loss for the year | x | x | x | x | x | x | x | x | x | x | x | x | x | x | 4196 | | x | x | x | x |
| 29. | Transfer from reserves to result due to release of reserves – increase | x | x | x | x | x | x | x | x | x | x | x | x | 4163 | | 4197 | | x | x | x | x |
| 30. | Transfer from reserves to result due to release of reserves – decrease | x | x | x | x | x | x | x | x | x | x | x | x | 4164 | | 4198 | | x | x | x | x |
| 31. | Transactions with owners, recorded directly in equity – increase | 4019 | | 4047 | | 4075 | | 4103 | | x | x | x | x | 4165 | | 4199 | | x | x | x | x |
| 32. | Transactions with owners, recorded directly in equity – decrease | 4020 | | 4048 | | 4076 | | 4104 | | x | x | x | x | 4166 | | 4200 | | x | x | x | x |
| 33. | Profit distribution – increase | 4021 | | 4049 | | 4077 | | 4105 | 4.000.000 | x | x | x | x | 4167 | | 4201 | | x | x | x | x |
| 34. | Profit distribution, and/or loss coverage – decrease | 4022 | | 4050 | | 4078 | | 4106 | | x | x | x | x | 4168 | 4.000.000 | 4202 | | x | x | x | x |
| 35. | Dividend payments | 4023 | | 4051 | | 4079 | | 4107 | | x | x | x | x | 4169 | 604.620 | 4203 | | x | x | x | x |
| 36. | Other – increase | 4024 | | 4052 | | 4080 | | 4108 | | x | x | x | x | 4170 | 27.283 | 4204 | | x | x | x | x |
| 37. | Other – decrease | 4025 | | 4053 | | 4081 | | 4109 | | x | x | x | x | 4171 | 140.356 | 4205 | | x | x | x | x |
| 38. | **Total transactions with owners (number 31-32+33-34-35+36- 37) ≥ 0** | 4026 | 0 | 4054 | 0 | 4082 | 0 | 4110 | 4.000.000 | x | x | x | x | 4172 | - | 4206 | 0 | x | x | x | x |
| 39. | **Total transactions with owners (number 31-32+33-34-35+36- 37) < 0** | 4027 | 0 | 4055 | 0 | 4083 | 0 | 4111 | - | x | x | x | x | 4173 | 4.717.693 | 4207 | 0 | x | x | x | x |
| 40. | **Balance as of December 31st of the current year (number 24+25-26+27+28+29-30+38-39 for columns from 2,3,4,5,6,8,9), for the column 7 (number 24+26-25)** | 4028 | 17.191.466 | 4056 | 0 | 4084 | 22.843.084 | 4112 | 20.635.440 | 4126 | 2.351.085 | 4140 | 230.126 | 4174 | 6.755.855 | 4208 | 0 | 4214 | 69.546.804 | 4220 | - |

In Belgrade,

on 27.02.2015.

Bank's legal representative

*1.6. Notes to the financial statements*

# NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR 2014

**Belgrade, February 2015**

## 1. BANK'S ESTABLISHMENT AND ACTIVITY

Komercijalna banka a.d., Beograd (hereinafter the "Bank"), was established as at December 1, 1970 and transformed into a shareholding company as of May 6, 1992. The Bank was registered with the Commercial Court in Belgrade on July 10, 1991 and later registered with the Serbian Business Registers Agency on April, 14 2006. The Bank was issued its operating license by the National Bank of Yugoslavia on July 3, 1991.

The principal holders of voting shares in the Bank are as follows:

| | |
|---|---|
| Republic of Serbia | 41.74% |
| EBRD, London | 24.43% |

The Bank is registered for performing crediting, depositary and guarantee operations, as well as for payment transfer operations in the country and abroad.

As of December 31, 2014, the Bank was comprised of the Head Office in Belgrade at the address of no. 14, Svetog Save St., 24 branches and 220 sub-branches in the territory of the Republic of Serbia (December 31, 2013: 24 branches and 233 sub-branches in the territory of the Republic of Serbia).

As of December 31, 2014, the Bank had 2,906 employees (December 31, 2013: 2,966 employees). The Bank's tax identification number is 100001931.

## 2. BASIS OF PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS

### 2.1. Basis of Preparation and Presentation of Financial Statements

Legal entities and entrepreneurs incorporated in Serbia are required to maintain their books of account, to recognize and value assets and liabilities, income and expenses, and to present, submit and disclose financial statements in conformity the Law on Accounting (hereinafter referred as: the "Law", Official Gazette of the Republic of Serbia no. 63/2013). As a large legal entity, the Bank is required to apply International Financial Reporting Standards ("IFRS"), which as per the aforementioned law comprise the following: the Framework for the Preparation and Presentation of Financial Statements (the "Framework"), International Accounting Standards ("IAS"), International Financial Reporting Standards ("IFRS"), as well as the related interpretations issued by the International Financial Reporting Interpretations Committee ("IFRIC") and additional related interpretations issued by International Accounting Standards Board ("IASB"), the translations of which to the Serbian language were approved and issued by the competent Ministry of Finance and which were in effect as at December 31, 2013.

The amendments to IAS, as well as the newly issued IFRS and the related interpretations issued by the IASB and the IFRIC, in the period between December 31, 2002 and January 1, 2009, were officially adopted pursuant to a Decision enacted by the Ministry of Finance of the Republic of Serbia (the "Ministry") on October 5, 2010 and published the Official Gazette of the Republic of Serbia no. 77/2010. The Ministry's Decision dated March 13, 2014 adopted the translation of the Conceptual Framework for Financial Reporting and (the "Conceptual Framework," adopted by the IASB in September 2010, which supplants the Framework for Preparation and Presentation of the Financial Statements) and basic texts of IAS and IFRS ("Decision on Adoption of the Translations of the Conceptual Framework for Financial Reporting and Basic Texts of International Accounting Standards and International Financial Reporting Standards," published the Official Gazette of the Republic of Serbia no. 35 on March 27, 2014 ("Decision on Adoption of the Translations"), encompassing amendments to IAS and new IFRS and related interpretations issued by IASB and IFRIC/effective as of December 31, 2013. Based on this Decision on Adoption of the Translations, the Conceptual Framework, IAS, IFRS, IFRIC and related interpretations that have been translated shall be applied to the financial statements prepared as of December 31, 2014.

Standards and interpretations issued that came into effect in the current period pursuant to the Decision on Adoption of the Translations are disclosed in Note 2.2, while standards and interpretations in issue but not yet in effect are disclosed in Note 2.3.

## 2. BASIS OF PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS (Continued)

### 2.1. Basis of Preparation and Presentation of Financial Statements (Continued)

The accompanying financial statements are presented in the format prescribed under the Decision on the Forms and Contents of the Items in the Forms of the Financial Statements of Banks (Official Gazette of RS nos. 71/2014 and 135/2014).

These financial statements were prepared at historical cost principle unless otherwise stipulated in the accounting policies presented hereunder.

In the preparation of the accompanying financial statements, the Bank adhered to the accounting policies described in Note 3.

The Bank's financial statements are stated in thousands of dinars (RSD). Dinar is the official reporting currency in the Republic of Serbia.

### 2.2. Standards and Interpretations Issued that Came into Effect in the Current Period Pursuant to the Decision on Adoption of the Translations of the Ministry

- Amendments to IFRS 7 "Financial Instruments: Disclosures" – Amendments improving fair value and liquidity risk disclosures (revised in March 2009, effective for annual periods beginning on or after January 1, 2009);

- Amendments to IFRS 1 "First-Time Adoption of IFRS" – Additional Exemptions for First-Time Adopters. The amendments relate to assets in oil and gas industry and determining whether an arrangement contains a lease (revised in July 2009, effective for annual periods beginning on or after January 1, 2010);

- Amendments to various standards and interpretations resulting from the Annual Quality Improvement Project of IFRS published on April 16, 2009 (IFRS 5, IFRS 8, IAS 1, IAS 7, IAS 17, IAS 36, IAS 39, IFRIC 16) primarily with a view to removing inconsistencies and clarifying wording, (amendments are to be applied for annual periods beginning on or after 1 January 2010, while the amendment to IFRIC is to become effective as of July 1, 2009);

- Amendments to IAS 38 "Intangible Assets" (revised in July 2009, effective for annual periods beginning on or after July 1, 2009);

- Amendments to IFRS 2 "Share-Based Payment": Amendments resulting from the Annual Quality Improvement Project of IFRS (revised in April 2009, effective for annual periods beginning on or after July 1, 2009) and amendments relating to group cash-settled share-based payment transactions (revised in June 2009, effective for annual periods beginning on or after January 1, 2010);

- Amendments IFRIC 9 "Reassessment of Embedded Derivatives" effective for annual periods beginning on or after July 1, 2009 and IAS 39 "Financial Instruments: Recognition and Measurement" – Embedded Derivatives (effective for annual periods beginning on or after June 30, 2009);

- IFRIC 18 "Transfers of Assets from Customers" (effective for annual periods beginning on or after July 1, 2009);

- "Conceptual Framework for Financial Reporting 2010" being amendments to "Framework for the Preparation and Presentation of Financial Statements" (effective for transfer of assets from customers received on or after September 2010);

- Amendments to IFRS 1 "First-time Adoption of International Financial Reporting Standards" – Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters (effective for annual periods beginning on or after July 1, 2010);

## 2. BASIS OF PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS (Continued)

### 2.2. Standards and Interpretations Issued that Came into Effect in the Current Period Pursuant to the Decision on Adoption of the Translations of the Ministry (Continued)

- Amendments to IAS 24 “Related Party Disclosures” – Simplifying the disclosure requirements for government-related entities and clarifying the definition of a related party (effective for annual periods beginning on or after January 1, 2011);
- Amendments to IAS 32 “Financial Instruments: Presentation” – Accounting for Rights Issues (effective for annual periods beginning on or after February 1, 2010);
- Amendments to various standards and interpretations “Improvements to IFRSs (2010)” resulting from the Annual quality improvement project of IFRS published on May 6, 2010 (IFRS 1, IFRS 3, IFRS 7, IAS 1, IAS 27, IAS 34, IFRIC 13) primarily with a view to removing inconsistencies and clarifying wording, (most amendments are to be applied for annual periods beginning on or after January 1, 2011);
- Amendments to IFRIC 14 “IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and Their Interaction” – Prepayments of a Minimum Funding Requirement (effective for annual periods beginning on or after January 1, 2011);
- IFRIC 19 “Extinguishing Financial Liabilities with Equity Instruments” (effective for annual periods beginning on or after July 1, 2010).
- Amendments to IFRS 1 “First-Time Adoption of IFRS” – Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters (effective for annual periods beginning on or after July 1, 2011);
- Amendments to IFRS 7 “Financial Instruments: Disclosures” – Transfers of Financial Assets (effective for annual periods beginning on or after January 1, 2011);
- Amendments to IAS 12 “Income Taxes” – Deferred Tax: Recovery of Underlying Assets (effective for annual periods beginning on or after January 1, 2012);
- IFRS 10 “Consolidated Financial Statements” (effective for annual periods beginning on or after January 1, 2013);
- IFRS 11 “Joint Arrangements” (effective for annual periods beginning on or after January 1, 2013);
- IFRS 12 “Disclosures of Involvement with Other Entities” (effective for annual periods beginning on or after January 1, 2013);
- Amendments to IFRS 10, IFRS 11 and IFRS 12 “Consolidated Financial Statements, Joint Arrangements and Disclosures of Involvement with Other Entities: Transition Guidance” (effective for annual periods beginning on or after January 1, 2013);
- IAS 27 (revised in 2011) “Separate Financial Statements” (effective for annual periods beginning on or after January 1, 2013);
- IAS 28 (revised in 2011) “Investments in Associates and Joint Ventures” (effective for annual periods beginning on or after January 1, 2013);
- IFRS 13 “Fair Value Measurement” (effective for annual periods beginning on or after January 1, 2013);
- Amendments to IFRS 1 “First-time Adoption of International Financial Reporting Standards” – Government Loans with a Below-Market Rate of Interest (effective for annual periods beginning on or after January 1, 2013);

## 2. BASIS OF PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS (Continued)

### 2.2. Standards and Interpretations Issued that Came into Effect in the Current Period Pursuant to the Decision on Adoption of the Translations of the Ministry (Continued)

- Amendments to IFRS 7 "Financial Instruments: Disclosures" – Offsetting Financial Assets and Financial Liabilities (effective for annual periods beginning on or after January 1, 2013);
- Amendments to IAS 1 "Presentation of Financial Statements" – Presentation of Items of Other Comprehensive Income (effective for annual periods beginning on or after July 1, 2012);
- Amendments to IAS 19 "Employee Benefits" – Improvements to the Accounting for Post-Employment Benefits (effective for annual periods beginning on or after January 1, 2013);
- Amendments to various standards "Improvements to IFRSs (2009-2011 Cycle)" issued in May 2012, resulting from the annual improvement project of IFRS (IFRS 1, IAS 1, IAS 16, IAS 32, IAS 34) primarily with a view to removing inconsistencies and clarifying wording (amendments are to be applied for annual periods beginning on or after January 1, 2013);
- IFRIC 20 "Stripping Costs in the Production Phase of a Surface Mine" (effective for annual periods beginning on or after January 1, 2013); and
- Amendments to IAS 32 "Financial Instruments: Presentation" – Offsetting Financial Assets and Financial Liabilities (effective for annual periods beginning on or after January 1, 2014).

### 2.3. Standards and Interpretations in Issue not yet in Effect

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

- IFRS 9 "Financial Instruments" and subsequent amendments, supplanting the requirements of IAS 39 "Financial Instruments: Recognition and Measurement," with regard to classification and measurement of financial assets. This standard eliminates the categories existing under IAS 39 – assets held to maturity, assets available for sale and loans and receivables. IFRS 9 shall be effective for annual periods beginning on or after January 1, 2018, with early adoption permitted.

In accordance with IFRS 9, financial assets shall be classified in one of the following two categories upon initial recognition: financial assets at amortized cost or financial assets at fair value. A financial asset shall be measured at amortized cost if the following two criteria are met: financial assets relate to the business model whose objective is to collect the contractual cash flows and the contractual terms provide the basis for collection at certain future dates of cash flows that are solely payments of principal and interest on the principal outstanding. All other financial assets shall be measured at fair value. Gains and losses on the fair value measurement of financial assets shall be recognized in the profit and loss statement, except for investments in equity instruments which are not traded, where IFRS 9 allows at initial recognition a subsequently irreversible choice to recognize changes in fair value within other gains and losses in the statement of comprehensive income. An amount recognized in such a manner within the statement of comprehensive income cannot subsequently be recognized in profit and loss.

Given the nature of the Bank's operations, the adoption of the standard is expected to have a significant impact on the Bank's financial statements.

- Amendments to IFRS 11 "Joint Arrangements" – Accounting for Acquisition of an Interest in a Joint Operation (effective for annual periods beginning on or after January 1, 2016);
- IFRS 14 "Regulatory Deferral Accounts" (effective for annual periods beginning on or after January 1, 2016);

## 2. BASIS OF PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS (Continued)

### 2.3. Standards and Interpretations in Issue not yet in Effect (Continued)

- IFRS 15 "Revenue from Contracts with Customers," defining the framework for revenue recognition. IFRS 15 supplants IAS 18 "Revenue," IAS 11 "Construction Contracts," IFRIC 13 "Customer Loyalty Programs," IFRIC 15 "Agreements for the Construction of Real Estate" and IFRIC 18 "Transfers of Assets from Customers." IFRS 15 shall be effective for annual periods beginning on or after January 1, 2017, with early adoption permitted.

- Amendments to IAS 16 "Property, Plant and Equipment" and IAS 38 "Intangible Assets" – Clarification of Acceptable Methods of Depreciation and Amortization (effective for annual periods beginning on or after January 1, 2016 );

- Amendments to IAS 16 "Property, Plant and Equipment" and IAS 41 "Agriculture" – Agriculture: Bearer Plants (effective for annual periods beginning on or after January 1, 2016);

- IAS 27 "Separate Financial Statements" – Equity Method in Separate Financial Statements (effective for annual periods beginning on or after January 1, 2016);

- 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 for annual periods beginning on or after January 1, 2016 );

- Amendments to IAS 19 "Employee Benefits" – Defined Benefit Plans: Employee Contributions (effective for annual periods beginning on or after July 1, 2014);

- Amendments resulting from Annual Improvements 2010-2012 Cycle issued in December 2013 (IFRS 2, IFRS 3, IFRS 8, IFRS 13, IAS 16, IAS 24 and IAS 38) with a view to removing inconsistencies and clarifying wording (effective for annual periods beginning on or after July 1, 2014); and

- Amendments resulting from Annual Improvements 2011-2013 Cycle issued in December 2013 (IFRS 1, IFRS 3, IFRS 13 and IAS 40) with a view to removing inconsistencies and clarifying wording (effective for annual periods beginning on or after July 1, 2014).

### 2.4. Going Concern

The financial statements were prepared on a going concern assumption entailing the Bank's continuation of operations for an indefinite period in the foreseeable future.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in these financial statements.

### *(a) Consolidation*

The Bank has control over the following legal entities, which are not consolidated into these financial statements:

| Legal Entity | Equity Interest |
|---|---|
| Komercijalna banka a.d. Budva, Montenegro | 100% |
| Komercijalna banka a.d. Banja Luka, Bosnia and Herzegovina | 99.99% |
| Investment Fund Management Company KomBank Invest a.d. Beograd, Serbia | 100% |

The Bank's consolidated financial statements are prepared and disclosed separately.

### *(b) Foreign Exchange Translation*

Transactions in foreign currencies are translated into Dinars at the spot middle exchange rates at the date of the transactions.

Monetary assets and liabilities denominated in foreign currencies which are stated at cost, are translated at the rate ruling at the reporting date. Foreign exchange differences arising on translation are recognized in the income statement . Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of transaction.

Exchange rates for major currencies used in the translation of the statement of financial position items denominated in foreign currencies, as determined by the National Bank of Serbia, were as follows:

| | | In RSD |
|---|---|---|
| | 2014 | 2013 |
| USD | 99.4641 | 83.1282 |
| EUR | 120.9583 | 114.6421 |
| CHF | 100.5472 | 93.5472 |
| JPY | 0.830986 | 0.791399 |

### *(c) Interest*

Interest income and expense are recognized in profit or loss 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 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 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 expense presented in the statement of comprehensive income include:

- interest on financial assets and financial liabilities measured at amortized cost calculated on an effective interest basis;
- interest on investment securities available for sale.

Interest income and expenses on all trading assets and liabilities are considered to be incidental to the Bank's trading operations and are presented together with all other changes in the fair value of trading assets and liabilities in net trading income.

**3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***(d) Fees and Commissions***

Fee and commission income and expenses that are integral 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 is recognized as the related services are performed. Fee and commission income includes transfer payments in foreign currency, domestic payments transactions, loan administration, guarantee, letter of credit business and other banking services. When a loan commitment is not expected to result in the draw-down of a loan, the related loan commitment fees are recognized on a straight-line basis over the commitment period.

Other fee and commission expenses relate mainly to transaction and service fees, which are expensed as the services are received.

***(e) Net Trading Income***

Net trading income comprises gains less losses, related to trading assets and liabilities, and includes all realized and unrealized fair value changes and foreign exchange differences.

***(f) Net income from Other Financial Instruments at Fair Value through Profit or Loss***

Net income from other financial instruments at fair value through profit or loss, relates to financial assets and liabilities designated at fair value through profit or loss and includes all realized and unrealized fair value changes.

***g) Dividends***

Income from dividends is recognized at the moment of economic benefits inflow arising from dividends. . Dividends are reported under other income.

***(h) Operating and Finance Lease Payments***

Payments made during the year under operating leases are charged to the income statement on a straight-line basis over the period of the lease. Lease incentives received are recognized as an integral part of the total lease expense, over the term of the lease.

Minimum lease payments made under finance leases are apportioned between the finance expense and the reduction of the outstanding liability. The finance expense is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

***(i) Tax Expenses***

Tax expense comprises current taxes and deferred taxes. Current taxes and deferred taxes are recognized in profit or loss except to the extent that it relates to items recognized directly in equity or in other comprehensive income.

*(i) Current Income Tax*

Current tax is expected tax payable or receivable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

*(ii) Deferred Income Tax*

Deferred income tax is recognized in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted by the reporting date.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

*(i) Tax Expenses(Continued)*
*(ii) Deferred Income Tax (Continued)*

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities against current tax assets, and they relate to taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously in future periods.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences to the extent that it is probable that the future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized. Deferred tax liabilities are recognized on all taxable temporary differences.

*(iii) Other Taxes and Contributions*

According to the relevant legislation in the Republic of Serbia, the Bank pays various taxes and contributions, such as VAT, capital gains tax and payroll contributions. These are included under “other operating expenses”.

### *(j) Financial Assets and Liabilities*

*(i) Recognition*

The Bank initially recognizes loans and receivables, deposits, borrowings and subordinated liabilities on the date at which they are originated. All other financial assets and liabilities are initially recognized on the balancing date at which the Bank becomes a party to the contractual provisions of the instrument.

A financial asset or liability is measured initially at fair value plus transaction costs that are directly attributable to its acquisition or issue, for items that are not carried at fair value through profit or loss.

*(ii) Classification*

The Bank classified its financial assets into the following categories: financial assets held for trading, loans and receivables and investment securities – please refer to accounting policies 3(l), 3(m) and 3(n).

The Bank classifies its financial liabilities as measured at amortized cost or held for trading – please refer to accounting policies.

*(iii) Derecognition*

The Bank derecognizes a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all the risk and rewards of ownership and it does not retain control of the financial asset. Any interest in transferred financial assets that qualifies for derecognition that is created or retained by the Bank is recognized as a separate asset or liability in the statement of financial position. On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset transferred), and the sum of the consideration received (including any new asset obtained less any new liability assumed) and any cumulative gain or loss that had been recognized in other comprehensive income is recognized in profit or loss.

***(j) Financial Assets and Liabilities (continued)***

The Bank enters in transactions whereby it transfers assets recognized on its statement of financial position, but retains either all or substantially all of the risks and rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognized. Transfers of assets with retention of all or substantially all risks and rewards include, for example, repurchase transactions.

In transactions in which the Bank neither retains nor transfers substantially all the risk and rewards of ownership of a financial asset and it retains control over the asset, the Bank continues to recognize the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of transferred asset.

*(iv) Offsetting*

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

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

*(v) Amortized Cost Measurement*

The amortized cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortization using the effective interest method of any difference between the initial amount recognized and the maturity amount, less any impairment.

*(vi) Fair Value Measurement*

The fair values stated for financial instruments are the amounts for which the asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

When available, the Bank measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, the Bank establishes fair value using a valuation technique. Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analyses and other optional models. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to the Bank, incorporates all factors that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument. The Bank calibrates valuation techniques and tests them for validity using prices from observable current market transactions in the same instrument of based on other available observable market data.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price, i.e. the fair value of the consideration given or received, unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e., without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When transaction price provides the best evidence of fair value at initial recognition, the financial instrument is initially measured at the transaction price and any difference between this price and the value initially obtained from a valuation model is subsequently recognized in profit or loss depending on the individual facts and circumstances of the transaction but not later than when the valuation is supported wholly by observable market data or the transaction is closed out.

### *(j) Financial Assets and Liabilities (continued)*

*(vi) Fair Value Measurement (continued)*

Any difference between the fair value at initial recognition and the amount that would be determined at that date using a valuation technique in a situation in which the valuation is dependent on unobservable parameters is not recognized in profit or loss immediately but is recognized over the life of the instrument on an appropriate basis or when the instrument is redeemed, transferred or sold, or the fair value becomes observable. Assets and long positions are measured at a bid price and liabilities and short positions are measured at an asking price. Fair values reflect the credit risk of the instrument and include adjustments to take account of the credit risk of the Bank and counterparty where appropriate. Fair value estimates obtained from models are adjusted for any other factors, such as liquidity risk or model uncertainties to the extent that the Bank believes a third-party market participant would take them into account in pricing a transaction.

*(vii) Identification and Measurement of Impairment*

At reporting date the Bank assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. A financial asset or a group of financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the assets, and that the loss event has an impact on the future cash flows of the assets that can be estimated reliably.

Objective evidence that financial assets (including equity securities) are impaired can include significant financial difficulty of the borrower or issuer, default or delinquency by a borrower, restructuring of a loan or advance by the Bank on terms that the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

The Bank considers evidence of impairment for loans and receivables and held-to-maturity investment securities at both a specific asset and collective level. All individually significant loans and receivables and held-to-maturity investment securities are assessed for specific impairment. All individually significant loans and receivables and held-to-maturity investment securities found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and receivables and held-to-maturity investment securities that are not individually significant are collectively assessed for impairment by grouping together loans and receivables and held-to-maturity investment securities with similar risk characteristics.

In assessing collective impairment the Bank uses statistical modeling of historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgment as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical modeling. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

Impairment losses on assets carried at amortized cost are measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognized in profit or loss and reflected in an allowance account against loans and receivables. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss. Impairment losses on available-for-sale investment securities are recognized by transferring the cumulative loss that has been recognized in other comprehensive income to profit or loss as a reclassification adjustment. The cumulative loss that is reclassified from other comprehensive income to profit or loss is the difference between the acquisition costs, net of any principal repayment and amortization, and the current fair value, less any impairment loss previously recognized in profit or loss. Changes in impairment provisions attributable to time value are reflected as a component of interest income. Movements on provisions for impairment losses attributable to the time value are included as a component of the interest rate.

***(j) Financial Assets and Liabilities (continued)***

*(vi) Fair Value Measurement (continued)*

If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in profit or loss, the impairment loss is reversed, with the amount of the reversal recognized in profit or loss. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognized in other comprehensive income.

The Bank writes off certain loans and receivables and investment securities when they are determined to be uncollectible (see note 4(b)).

***(k) Cash and Cash Equivalents***

Cash and cash equivalents include notes and coins on hand, unrestricted balances held with central banks and highly liquid financial assets with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value, and are used by the Group in the management of its short-term commitments.

Cash and cash equivalents are carried at amortized cost in the balance sheet.

***(l) Trading Assets and Liabilities***

Trading assets and liabilities are those assets and liabilities that the Bank acquires or incurs principally for the purpose of selling or repurchasing in the near term, or holds as part of a portfolio that is managed together for short-term profit or position taking.

Trading assets and liabilities are initially recognized and subsequently measured at fair value in the statement of financial position, with transaction costs directly recognized in profit or loss. All changes in fair value are recognized as part of net trading income in profit or loss. Trading assets were not reclassified subsequent to their initial recognition, except that non-derivative trading assets, other than those designated at fair value through profit or loss upon initial recognition, may have been reclassified out of the fair value through profit or loss, i.e. trading category, if they were no longer held for the purpose of being sold or repurchased in the near term and either of the conditions below were met.

- If the financial asset would have met the definition of loans and receivables (if the financial asset had not been required to be classified as held for trading at initial recognition), then it may be reclassified if the legal entity has the intention and ability to hold the financial asset for the foreseeable future or until maturity.
- If the financial asset would not have met the definition of loans and receivables, then it may be reclassified out of the trading category only in rare circumstances.

*Derivatives*

Financial derivatives comprise forward and swap transactions. Financial derivatives are initially recognized at cost and are subsequently measured at market value. Market values are ascertained based on quoted prices on an active market, as well as by using different valuation techniques, including discounted cash flows. Financial derivatives are accounted for under assets if their market value is positive, and under liabilities if their market value is negative. Fluctuations in market value of financial assets are reported in the statement of comprehensive income, under net trading income.

***(m) Loans and Receivables***

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Bank does not intend to sell immediately or in the near term. They arise when the Bank provides money or services directly to a debtor with no intention of trading the receivable. Loans and receivables comprise loans and receivables to banks and customers. Loans and receivables are initially measured at fair value plus incremental direct transaction costs, and subsequently measured at their amortized cost using the effective interest method.

***(m) Loans and Receivables (continued)***

Approved dinar loans which are hedged using a contractual currency clause linked to the dinar EUR exchange rate, to another foreign currency or consumer price index are converted into dinars at balance sheet date in accordance with the terms of the particular loan agreement. The effects of the currency conversion are reported under trading income and expenses. Loans and receivables are presented net of specific and collective allowances for impairment. Specific and collective allowance, are made against the carrying amount of loans and receivables that are identified as being impaired in order to reduce their value to recoverable amount. 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 (such as an improvement in the debtor's credit rating), the previously recognized impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognized in the statement of comprehensive income in impairment charge for credit losses.

***(n) Investment Securities***

Investment securities are initially measured at fair value plus, in case of investment securities not at fair value through profit or loss, incremental direct transaction costs, and subsequently accounted for depending on their classification as either held-to-maturity, fair value through profit or loss, or available-for-sale.

*(i) Held-to-Maturity Financial Assets*

Held to maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Bank has the positive intention and the ability to hold them to maturity, and which are not designated as at fair value through profit or loss or as available-for-sale.

Held-to-maturity investments are carried at amortized cost using the effective interest method. Any sale or reclassification of a more than insignificant amount of held-to-maturity investments would result in the reclassification of all held-to-maturity investments as available-for-sale, and prevent the Bank from classifying investment securities as held-to-maturity for the current and the following two financial years. However, sales and reclassifications in any of the following circumstances would not trigger a reclassification:

- sales or reclassifications that are so close to maturity that changes in the market rate of interest would not have a significant effect on the financial asset's fair value,
- sales or reclassifications after the Bank has collected substantially all of the asset's original principal, and
- sales or reclassifications attributable to non-recurring isolated events beyond the Bank's control that could not have been reasonably anticipated.

*(ii) Financial Assets at Fair Value through Profit or Loss*

Financial assets at fair value through profit or loss are financial assets that are classified as held for trading or upon initial recognition are designated by the Bank as at fair value through profit or loss. Financial assets at fair value through profit or loss are those that the Bank acquired or incurred principally for the purpose of selling or repurchasing it in the near term, part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking or derivatives.

*(iii) Available- for- Sale Financial Assets and Equity Investments*

Available for sale financial assets are those non-derivative financial assets that are designated as available for sale or are not classified as another category of financial asset. Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

***(n) Investment Securities (continued)***

*(iii) Available- for- Sale Financial Assets and Equity Investments (continued)*

Unquoted equity securities whose fair value cannot be reliably measured are carried at cost. All other available-for-sale investments are carried at fair value.

Interest income is recognized in profit or loss using the effective interest method. Dividend income is recognized in profit or loss when the Bank becomes entitled to the dividend. Foreign exchange gains or losses on available-for-sale debt security investments are recognized in profit or loss.

Other fair value changes are recognized in other comprehensive income until the investment is sold or impaired, whereupon the cumulative gains and losses previously recognized in other comprehensive income are reclassified to profit or loss as a reclassification adjustment.

When a decline in the fair value of an available-for-sale financial asset has been recognized in other comprehensive income and there is objective evidence that the asset is impaired (long and continuing decline in the fair value in the period longer than twelve months, as well as decline above 30% of cost), as well as the cumulative loss that had been recognized in other comprehensive income shall be reclassified from equity to profit or loss as a reclassification adjustment even though the financial asset has not been derecognized (IAS 39.59, IAS 39.67 and IAS 39.68)

A non-derivative financial asset may be reclassified from the available-for-sale category to the loans and receivables category if it otherwise would have met the definition of loans and receivables and if the Bank has the intention and ability to hold that financial assets for the foreseeable future or until maturity.

***(o) Property and Equipment***

*(i) Recognition and Measurement*

Items of property and equipment are measured at cost.

Cost includes expenditures that are directly attributable to the acquisition of the asset. Purchased software that is integral to the functionality of the related equipment is capitalized as part of that equipment.

Following initial recognition items of equipment are measured at cost less accumulated depreciation and accumulated impairment losses.

Following initial recognition, property is measured at valuation amount which represents its fair value at valuation date less subsequent accumulated depreciation and subsequent accumulated impairment losses. Valuation is performed regularly in order to ensure that net book value does not differ significantly from reported amounts that would result from using the fair value approach at the end of reporting period.

When parts of an item of property or equipment have different useful lives, they are accounted for as separate items (major components) of property and equipment.

The gain or loss on disposal of an item of property and equipment is determined by comparing the proceeds from disposal with the carrying amount of the item or property and equipment, and are recognized net within other income in profit or loss.

*(ii) Subsequent Costs*

The cost of replacing part of an item of property or equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Bank and its cost can be measured reliably. The carrying amount of the replaced part is derecognized. The costs of the day-to-day servicing of property and equipment are recognized in profit or loss as incurred.

**3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***(o) Property and Equipment (Continued)***

*(iii) Depreciation*

Depreciation is recognized in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property and equipment since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Leased assets are depreciated over the shorter of the lease term and their useful lives.

The estimated depreciation rates for the current and comparative periods were as follows:

| Asset | Estimated useful life (in years) | Rate % |
|---|---|---|
| Buildings | 40 | 2.50% |
| Computer equipment | 4 | 25% |
| Furniture and other equipment | 5 – 15 | 10%-15.5% |
| Leasehold improvements | 1 – 11 | 4.25%-86.2% |

Depreciation methods, useful lives and residual values are reassessed at each financial year-end and adjusted if appropriate.

Maintenance costs for assets are recognized in the profit or loss in the period when occurred.

**(p) Intangible Assets**

Intangible assets acquired by the Bank are stated at cost less accumulated amortization and accumulated impairment losses.

Subsequent expenditure on intangible assets is capitalized only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Amortization is recognized in profit or loss on a straight-line basis over the estimated useful life of the intangible asset, from the date that it is available for use since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. The estimated useful life of intangible assets is 3 to 5 years and amortization rates used range between 14.29% and 33.34%.

Amortization methods, useful lives and residual values are reassessed at each financial year-end and adjusted if appropriate.

***(q) Investment Property***

Investment property is property held either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business, use in the production or supply of goods or services or for administrative purposes.

Investment property is initially measured at cost. Cost of acquired investment property comprises the purchase price and all expenses that can be directly attributed to the acquisition of the asset.

For subsequent measurement of investment property the Bank uses the cost model, such that investment property is measured at cost less accumulated depreciation and impairment losses.

Estimated useful life of investment property amounts to 40 years, while the depreciation rate used amounts to 2.5%. Depreciation is provided for in profit or loss on a straight line basis over the useful life of a given item of property, given that it reflects best the expected exploitation of the useful economic value embodied in the asset.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *(r) Leases*

The Bank is a lessee based on leasing agreements. The Bank classifies leases as financial leasing when the lease agreement stipulates that the basic risks and benefits of ownership over the leased assets are transferred to the lessee. All other leasing agreements are classified as operating leases.

Lease agreements that relate to lease of office space in which the Bank's branches are located primarily relate to operating leases. All payments made during the year based on operating leases are reported as an expense in the statement of comprehensive income on a straight line basis over the duration of the lease period.

Assets that are held based on a finance lease agreement are recognized as the Bank's assets at the lower of their fair value or the present value of minimum lease payments specified at the start of the lease agreement. The corresponding liability toward the lessor is reported in the statement of financial position as a finance lease liability. Lease payments are apportioned between the finance expense and the reduction of the outstanding finance lease liability, such that a constant interest rate is achieved on the outstanding portion of the liability. The financial expense is reported directly as a period expense.

### *(s) Impairment of Non-Financial Assets*

The carrying amounts of the Bank's non-financial assets, other than investment property and deferred tax assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated. An impairment loss is recognized if the carrying amount of an asset exceeds its estimated recoverable amount.

The recoverable amount of an asset is the greater of its value in use and its fair value less costs 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.

An impairment loss is recognized when the carrying amount of an asset exceeds its recoverable amount. Impairment losses are recognized in profit or loss.

Impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. 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 amortization, if no impairment loss had been recognized.

### *(t) Deposits, Borrowings and Subordinated Liabilities*

Deposits, debt securities, borrowings and subordinated liabilities are the Bank's main sources of financing.

The Bank classifies capital instruments as financial liabilities or equity instruments in accordance with the substance of the contractual terms of the instruments.

Deposits, debt securities, borrowings and subordinated liabilities are initially measured at fair value increased for all directly attributable transaction costs, while they are subsequently measured at amortized cost using the effective interest rate method.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *(u) Provisions*

A provision is recognized if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

### *(v) Employment Benefits*

In accordance with regulatory requirements, the Bank is obligated to pay contributions to tax authorities and to various state social security funds, which guarantee social security insurance benefits to employees. These obligations involve the payment of taxes and contributions on behalf of the employee, by the employer, in an amount computed by applying the specific, legally-prescribed rates. The Bank is also legally obligated to withhold contributions from gross salaries to employees, and on behalf of its employees, to transfer the withheld portions directly to government funds. These taxes and contributions payable on behalf of the employee and employer are charged to personnel expenses in the period in which they arise.

In accordance with the Labor Law, the Bank is under obligation to pay its vesting employees retirement benefits. Long-term liabilities for retirement benefit provisions upon fulfillment of retirement criteria reported as of December 31, 2014 represent the present value of the expected future payments to employees as determined by actuarial assessment using assumptions disclosed in Note 36(b).

### *(w) Financial Guarantees*

Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

Financial guarantee liabilities are initially recognized at their fair value, and the initial fair value is amortized over the life of the financial guarantee. The guarantee liability is subsequently carried at the higher of this amortized amount and the present value of any expected payment (when a payment under the guarantee has become probable). Financial guarantees are reported under off-balance sheet items.

### *(x) Capital and Reserves*

The Bank's equity consists of founders' capital, shares of subsequent issues, share premium, profit reserves, revaluation reserves and unrealized losses on available for sale securities, retained earnings and current period result.

The Bank's equity is comprised of funds invested by the Bank's founders in pecuniary form. A founder cannot withdraw funds invested in the Bank's equity.

### *(y) Earnings per Share*

The Bank presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the period.

Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *(z) Segment Reporting*

An operating segment is a component of the Bank that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Bank's other components, whose operating results are reviewed regularly by Bank management (being the chief operating decision maker) to make decisions about resources allocated to each segment and assess its performance, and for which discrete financial information is available.

## 4. RISK MANAGEMENT

The Bank has recognized risk management process as the key element of business management given that risk exposure is an inseparable part of banking and is managed through a process of continued identification, measurement, monitoring, minimizing and setting of risk limits and through other types of control, including reporting in accordance with adopted strategies and policies.

The Bank has established a comprehensive and reliable risk management system that includes: risk management strategies, policies and procedures, appropriate organizational structure, effective and efficient process of managing all risk it is exposed to, adequate system of internal controls adequate information system and process of internal capital adequacy assessment.

Risk management process involves clear determining and documenting risk profile and adjusting risk profile to the Bank's aptitude to assume risk in accordance with the adopted strategies and policies.

The basic objectives that the Bank set for the risk management system within its risk management and capital management strategies are the following: minimizing the negative effects on financial result and equity within acceptable risk levels, maintaining the required level of capital adequacy, developing the Bank's activities in accordance with business opportunities and market development with a view to gain competitive advantage.

The Bank implements Basel II standards and permanently monitors all the announcement and amendments to the effective regulations, analyses the risk levels and undertakes measures for timely reconciliation of its operations with newly enacted regulations in accordance with the risk level acceptable to the Bank. Through the clearly defined process of introducing new products, the bank analyses the influence of all new services and products on the future risk exposures in order to optimize its revenues and losses based on the estimated risk as well as to minimize all potential adverse effects on the Bank's financial result.

**Risk Management System**

The risk management system is governed by the following internal enactments:

- Risk Management Strategy and Capital Management Strategy;
- Risk Management Policies;
- Risk Management Procedures;
- Methodologies for Managing Individual Risks; and
- Other enactments.

Risk Management Strategy sets out:

- Long-term objectives, defined by the Bank's business policy and strategy and its attitude to assume risk determined in accordance with those objectives;
- Basic principles of risk assumption and management;
- Basic principles of the process of internal assessment of the Bank's capital adequacy; and
- Overview and definitions of all types of risk the Bank is exposed to or may be exposed to.

**4. RISK MANAGEMENT (Continued)**

**Risk Management System (Continued)**

The Bank specified the basic principles of risk management for meeting its long-term objectives:

- Organizing operation of a separate organizational unit for risk management;
- Functional and organizational separation of risk management activities from the regular operating activities of the Bank;
- Comprehensive risk management;
- Effective risk management;
- Cyclic risk management;
- Developing risk management as a strategic orientation; and
- Risk management as a part of corporate culture.

Policies for managing certain risk types define the following:

- Manner of organizing risk management processes within the Bank and clear division of personnel responsibilities in all stages of the process;
- Manner of assessing the Bank's risk profile and methodology for identifying, measuring and assessing risks;
- Manners of risk monitoring and control and establishing the system of limits, i.e. types of limits the Bank uses as well as their structure;
- Measures for risk mitigation and rules for implementation thereof;
- Manner and methodology for implementing the process of internal assessment of the Bank's capital adequacy;
- Principles of the system of internal controls; functioning; and
- Framework and frequency for stress testing and procedure in instances of unfavorable test results.

Procedures for managing certain risk types define, in greater detail, the process of managing risks and competencies and responsibilities of all organizational units of the Bank in the risk management system.

Individual methodologies further and in more detail prescribe methods and approaches used in the risk management system.

**Competencies**

*The Board of Directors* is authorized and responsible for establishing a uniform risk management system and for monitoring such system, adopting policies and procedures for risk management and capital management strategy, establishment of internal control system, supervision of the work of the Executive Board and execution of the process of internal capital adequacy assessment.

*The Executive Board* is authorized and responsible for implementation of risk management strategy and policies, capital management strategy adoption and efficiency analysis of risk management procedure implementation, which define processes of identifying, measuring, minimizing, monitoring, controlling reporting risk the Bank is exposed to. Executive Board reports to the Board of Directors on implementation efficiency of defined management risk procedures.

*The Audit Committee* is authorized and responsible for continued monitoring of application of risk management policies and procedures, and for implementing the internal control system. The Audit Committee at least monthly reports to The Board of Directors on its activities, irregularities, and propose how they will be removed.

*The Asset and Liability Committee* (ALCO) is authorized and responsible for monitoring the Bank's risk exposure resulting from the structure of its receivables, payables and off-balance sheet items, and proposes measures for managing interest and liquidity risks.

*The Credit Committee* decides on loan requests in accordance with the Bank's internal acts, it analyzes the Bank's exposure to credit, interest and currency risk, it analyzes the credit portfolio and implements results of internal audit under the Committee's jurisdiction, and also suggests adequate measures to the Executive Board.

## 4. RISK MANAGEMENT (Continued)

### Competencies (Continued)

*The Collections Committee* is authorized and responsible for managing risk weighted placements; it makes decisions on the write-off of risk-weighted loans up to set limits of authorization and recommends write-off of loans to the Executive Board and Board of Directors through its limits of authorization.

*The Risk Management Organizational Unit* defines and proposes for adoption, the risk management strategy, policies, procedures and methodologies identifies, measures, mitigates, monitors, controls and reports on the risks the Bank is exposed to. It is also in charge of developing models and methodologies of risk management and reporting to the competent Bank's bodies.

*The Treasury* is responsible for managing assets and liquidity, the Bank's assets and liabilities, their overall financial structure, and is primarily responsible for the Bank's liquidity risk, interest rate risk and foreign currency risk.

*The Internal Audit Division* is responsible for continued monitoring of implementation of risk management policies and procedures, and tests the adequacy of procedures and the Bank's compliance thereto. Internal Audit reports its findings and recommendations to the Audit Committee and the Board of Directors.

*The Compliance Control Division* is obligated to identify and assess compliance risks at least annually and propose risk management plans, whereof it prepares a report and submits it to the Executive Board and Board for Monitoring of the Bank's operation.

### Risk Management Process

The Bank regularly measures and evaluates risks identified in its operations. Measurement entails applying qualitative and quantitative measurement methods and models that enable detection of changes in risk profile and assessment of new risks.

For all risks identified the Bank determines their significance based on as comprehensive assessment of risks in the Bank's particular operations, products, activities and processes.

Risk alleviation or mitigation involves risk diversification, transfer, minimization and or avoidance; the Bank performs risk mitigation in accordance with risk profile and risk appetite.

Risk monitoring and control is based on limits that are set by the Bank. They in turn depend on business strategy and the business environment, as well as on the level of risk that the Bank is ready to accept.

Risk management reports are regularly submitted to: the Bank's Board of Directors, Executive Board, Audit Committee, ALCO and Credit Committee, and they contain all the information required for risk assessment and reaching of conclusions about the Bank's risks.

### Risk Types

In its regular course of business, the Bank is particularly exposed to the following risks: credit risk and risks associated with the credit risk, liquidity risk, market risk, operational risks, investment risk, exposure risk and country risk as well as to all other risks that may arise from the Bank's regular operations.

## 4.1. Credit Risk

Credit risk represents the risk of negative effects on the Bank's financial result and capital arising from debtors' inability to settle the matured liabilities to the Bank.

The Bank has defined criteria for loan approval and rescheduling and restructuring of receivables prescribed by its loan approval procedures and methodology. Loans are approved depending on the target market, borrower characteristics and loan purpose.

**4. RISK MANAGEMENT (Continued)**
**4.1. Credit Risk (Continued)**

Prior to loan approval, the Bank assesses the creditworthiness of the borrower based on internally defined criteria as a primary and offered collateral as a secondary source of collection/loan repayment. Based on the identified and measured credit risk level (assessed financial situation and credit worthiness of the borrower, value and legal security of the credit hedge and other relevant factors), and independent risk assessment, the Bank's competent bodies enact a loan approval decision in accordance with the defined decision making system.

Decisions on credit risk exposure are defined through the decision making system that depends on the type of customer and exposure level: for loans within defined limits decisions are made by the branch credit committees, although in certain cases approval of the risk management organizational unit is required. Central Credit Committee decides on the loans in excess of the defined limits (depending on the type of client) with prior opinion of the risk management organizational unit. The Executive Board and Board of Directors make decisions depending on the exposure levels.

In decision making the principle of double control, the so-called "four eyes principle," is observed which ensures that there is always a party that proposes and a party that approves a particular loan/investment.

For loans contracted in foreign currencies or RSD loans indexed to a currency clause, the Bank estimates the effects of the changes in foreign exchange rates on the financial situation and creditworthiness of debtors and particularly analyzes adequacy of the debtor's cash flows in relation to the changed level of liabilities per loans assuming that there will be certain fluctuation in RSD exchange rates on an annual basis.

***Credit Risk Management***

According to the volume, type and complexity of its operations, the Bank has organized the credit risk management process and clearly delineated employee responsibilities in all stages of the process.

The organizational model of credit risk management system enables adequate communication, information exchange and collaboration at all organizational levels within the Bank as well as clear operational and organizational separation of functions for independent risk management and supporting activities on one hand and the activities of risk assumption on the other, i.e. segregation of duties, competencies and responsibilities. The Bank has also established an adequate information system for full coverage of persons involved in credit risk management system and appropriate management reporting.

The level of credit risk exposure acceptable to the Bank is in line with the defined risk management strategy and depends on the Bank's portfolio structure based on which is limited negative effects on the Bank's financial result and capital adequacy. On the other hand, the Bank does not make high-risk investments such as investments in highly profitable projects with significant risk levels.

The basic principles of credit risk management are as follows:

- Managing credit risk at the individual loan level as well as the Bank's entire portfolio level;
- Maintaining credit risk level that minimizes the negative effects on the Bank's financial result and capital;
- Loan rating according to risk;
- Operating in accordance with best banking practices of loan approval;
- Ensuring adequate credit risk management controls.

In its effort to manage credit risk the Bank seeks to do business with customers that have good credit rating and to acquire appropriate collaterals to secure repayments. The Bank assesses creditworthiness of each customer upon the submission of a loan application and regularly monitors its debtors, loans and collaterals, in order to be able to undertake appropriate activities for the purpose of collecting its receivables.

**4. RISK MANAGEMENT (Continued)**
**4.1. Credit Risk (Continued)**
***Credit Risk Management (Continued)***

The Bank performs quantitative and/or qualitative measurement, i.e. assessment of the identified credit risk. The credit risk measurement process is based on measuring risk level of individual loans and investments based on the internally adopted rating system.

The rating system is not merely an instrument for encasement individual decisions and assessing risk levels of individual investments; it is also a basis for portfolio analysis, support in loan approval and loan impairment procedure as well as in estimating provisions against losses per off-balance sheet items for the purpose of loan and investment ranking by risk level and stating realistic value of receivables. Internal rating system is subject to regular review and improvements.

In addition to the internal rating system, in credit risk analysis the Bank also uses principles prescribed by the National Bank of Serbia, which require classification of loans based on the prescribed criteria as well as calculation of the reserve for estimated credit risk losses. Application of these principles allows the Bank to cover unexpected losses due to the customer's inability to settle liabilities as they fall due, in accordance with contractually defined terms. For these purposes, the Bank classifies receivables and assesses the level of necessary reserve using the regular analysis of portfolio. The analysis includes the measurement of adequacy of reserves formed against individual borrowers, risk categories, portion of portfolio and at overall portfolio level.

Alleviating credit risk entails maintaining the risk at the level acceptable to the Bank's risk profile, i.e. maintaining acceptable quality level of the Bank's loan portfolio.

Basic credit risk alleviating techniques are:

- Exposure limits – concentration risk;
- Investment diversification; and
- Collaterals.

The Bank's exposure limits per individual debtor are based on the assessment of the debtor's credit-worthiness, whereas the exposure limits at the portfolio level are focused on restricting exposure concentration within the portfolio. The Bank continuously controls credit risk movements within a defined risk profile.

Concentration risk includes: large exposure (exposure to a single entity or a group of related entities and the Bank's related parties), group exposures with the same or similar risk factors such as industry sectors, types of products, geographical areas and the like, county risk and credit risk hedges.

Monitoring investment quality at the individual debtor level is primarily based on obtaining updated information on the financial situation and creditworthiness of the debtor as well as on the market value of collateral, whereas credit risk monitoring at the portfolio level is performed through identification of changes at the level of client groups with certain preset levels of risk, investment, collateral and required reserves for estimated and unexpected losses for the purpose of establishing management of the asset balances and quality.

Credit risk control entails a process of continuous reconciling business operations with the defined system of limits, both on a daily and monthly bases, as well as under conditions of large credit exposure approaching the upper risk profile limit, i.e. upon introduction of new products and business activities.

As a hedge against counterparty default risk, the Bank undertakes the following steps in respect to collection of due receivables: rescheduling or restructuring; out-of-court settlement; seizure of goods or properties in order to collect receivables; sale and/or assignment of receivables; executing agreements with interested third parties; and instigating court proceedings and other measures.

**4. RISK MANAGEMENT (Continued)**
**4.1. Credit Risk (Continued)**
***Credit Risk Management (Continued)***

If the undertaken measures for regulating collection, i.e. enforced collection and court proceedings fail to provide expected results, i.e. when receivables cannot be collected in full, the Bank initiates write-off of the remaining receivables.

Apart from credit risk exposure, the Bank also has off-balance sheet exposures (various types of payment and performance guarantees, acceptances and letters of credit) based on which the Bank has contingent liabilities to make payments on behalf of third parties. For off-balance sheet exposures the Bank uses the same control processes and procedures that are used for credit risk.

Credit risk reporting includes internal and external reporting systems executed on a monthly basis according to a preset schedule and in conformity with the defined reporting system.

**Downgrade Risk**

The quality of the Bank's assets is measured by the level of exposure to individual risk categories according to internal rating system criteria. The internal rating system focuses on quantitative and qualitative parameters for assigning customer ratings. The rating scale consists of 5 risk categories that are subdivided into 17 subcategories. Different exposures to the same borrower are grouped in the same credit rating category irrespective of the specificities of different loan types.

The Bank uses varying credit rating models depending on the borrower type. Credit rating is calculated on monthly basis based on the qualitative and quantitative parameters and timely and regular liability settlement.

A low level of risk implies doing business with customers with a high credit rating (risk rating categories 1 and 2), increased level of risk implies doing business with customers with operating difficulties that could have a negative impact on the settlement of liabilities (risk rating category 3), and a high level of risk characterizes customers with negative operating results and poor credit rating history (risk rating categories 4 and 5).

The Bank protects itself against downgrade risk through continuous monitoring of customers' business operations and by identifying changes that could arise through: deterioration of a borrower's financial standing, delays in repayment and changes in the business environment, as well as by securing appropriate collaterals.

*Risk of Change in Value of Assets*

Allowance for impairment of loans is intended to ensure reasonable, cautious and timely registering of losses on loan impairment, as well as to intervene in respect of contingent liabilities with a view to protect the Bank in the period when the loss occurs and is definitely confirmed (realized), due to inability to collect contracted amounts or through outflow of assets to settle contingent liabilities.

Allowance for impairment of loans and provisions are made when there is justification and objective evidence of impairment arising as the result of events that occurred after initial recognition of a loan, that have a negative effect on future cash flows associated with a loan.

Key elements in assessing impairment of loans are as follows: overdue payments on principal or interest, cash flow difficulties on the part of the borrower, the borrower's credit rating deterioration or changes in the initial terms of contract etc.

Allowance for impairment is based on estimated future cash flows from the borrower's business or collateral foreclosure if it is assessed that a loan can be realistically settled from such assets.

The Bank assesses allowance for impairment of receivables on an individual and on a group basis.

## 4. RISK MANAGEMENT (Continued)
### 4.1. Credit Risk (Continued)
*Credit Risk Management (Continued)*

*Individual Assessment*

The Bank assesses impairment of each individually significant loan and considers the financial position of the loan beneficiary, sustainability of its business plan, its ability to improve performance in the event of financial difficulties, income projections, availability of other financial support and collateral value which can be realized, as well as scheduling of expected cash flows. In the event of new information coming to light that significantly alters the customer's creditworthiness, value of collateral and likelihood that liabilities toward the Bank will be settled, ad hoc assessment of loan impairment is performed.

*Group Assessment*

Impairment is assessed on a group basis for loans that are not individually significant and for individually significant loans and advances, when there is no objective evidence of individual impairment. Group assessment is performed monthly within groups that are determined based on internal methodology and internal rating system. Group impairment percentages are calculated based on migration of risk rating categories in default status per type of borrower or product.

Impairment of loans decreases the value of loans and is recognized as an expense in the income statement.

*Assessment of Provisions for Losses on Off-Balance Sheet Items*

Assessment of provisions for losses on off-balance sheet items (contingent liabilities) is performed when it is estimated that it is fairly certain that an outflow of assets will be required to settle contingent liabilities.

In assessing provisions for contingent losses on off-balance sheet items, funds obtained by

activating collaterals are recognized if it is completely certain that cash outflows for contingent liabilities

will be settled from collaterals.

### 4.1.1. Maximum Credit Risk Exposure

Maximum credit risk exposure as of December 31, 2014 and 2013 is presented in the table below without taking into account any collateral or any other sort of credit risk hedge. The stated values are presented in gross and net carrying amounts (after impairment effects).

*Maximum Credit Risk Exposure before Collateral or any Other Improvements*

| | December 31, 2014 | | December 31, 2013 | |
|---|---|---|---|---|
| | Gross | Net | Gross | Net |
| **I. Assets** | **411,491,955** | **387,248,783** | **365,278,655** | **344,901,797** |
| Cash and cash funds held with the central bank | 68,547,389 | 68,547,389 | 70,934,839 | 70,934,839 |
| Loans and receivables due from banks and other financial institutions | 35,106,194 | 34,737,605 | 35,573,308 | 35,247,935 |
| Loans and receivables due from customers | 208,462,012 | 185,377,035 | 196,390,640 | 177,560,058 |
| Financial assets | 95,774,547 | 95,654,325 | 57,195,947 | 57,150,504 |
| Other assets | 3,601,813 | 2,932,429 | 5,183,921 | 4,008,461 |
| **II. Off-balance sheet items** | **30,165,789** | **29,597,365** | **30,882,511** | **30,408,862** |
| Payment guarantees (Note 39.1) | 4,767,131 | 4,626,118 | 7,357,476 | 7,291,000 |
| Performance bonds (Note 39.1) | 7,883,510 | 7,734,385 | 5,787,610 | 5,661,141 |
| Irrevocable commitments | 16,715,960 | 16,715,960 | 16,830,341 | 16,830,341 |
| Other items | 799,188 | 520,902 | 907,084 | 626,380 |
| **Total (I+II)** | **441,657,744** | **416,846,148** | **396,161,166** | **375,310,659** |

The largest credit risk is associated with the executed loan arrangements; however, the Bank is exposed to credit risk based on off-balance sheet items resulting from commitments and contingent liabilities.

**4. RISK MANAGEMENT (Continued)**
**4.1. Credit Risk (Continued)**

**4.1.1. Maximum Credit Risk Exposure (Continued)**

**Loans and receivables due from customers, banks and other financial institutions**

| | | | | | | | | | December 31, 2014 |
|---|---|---|---|---|---|---|---|---|---|
| | Housing Loans | Cash Loans | Agricultural Loans | Other Loans | Micro Business | Total Retail | Corporate Customers | Total | Due from Banks |
| Loans not matured and not provided for | - | - | - | - | - | - | 2,313,323 | 2,313,323 | 27,533,227 |
| Loans matured and not provided for | - | - | - | - | - | - | 1,557,306 | 1,557,306 | 7,204,378 |
| Group-level impaired | 37,033,132 | 15,133,016 | 5,307,696 | 7,264,505 | 6,248,660 | 70,987,009 | 95,147,574 | 166,134,583 | 368,589 |
| Individually impaired | 760,253 | - | 94,069 | - | 995,964 | 1,850,286 | 36,606,514 | 38,456,800 | - |
| **Total** | **37,793,385** | **15,133,016** | **5,401,765** | **7,264,505** | **7,244,624** | **72,837,295** | **135,624,717** | **208,462,012** | **35,106,194** |
| **Impairment allowance** | **543,326** | **903,607** | **436,472** | **720,048** | **1,070,353** | **3,673,807** | **19,411,170** | **23,084,977** | **368,589** |
| Group-level impairment allowance | 440,780 | 903,607 | 413,477 | 720,048 | 883,455 | 3,361,367 | 8,733,842 | 12,095,209 | 368,589 |
| Individual impairment allowance | 102,546 | - | 22,995 | - | 186,899 | 312,440 | 10,677,328 | 10,989,768 | - |
| **Net carrying value** | **37,250,059** | **14,229,409** | **4,965,292** | **6,544,457** | **6,174,271** | **69,163,489** | **116,213,547** | **185,377,035** | **34,737,605** |

| | Housing Loans | Cash Loans | Agricultural Loans | Other Loans | Micro Business | Total Retail | Corporate Customers | Total | Due from Banks |
|---|---|---|---|---|---|---|---|---|---|
| Loans not matured and not provided for | - | - | - | - | - | - | 9,308,456 | 9,308,456 | 34,239,484 |
| Loans matured and not provided for | - | - | - | - | - | - | 10,872,773 | 10,872,773 | 1,008,450 |
| Group-level impaired | 33,194,871 | 12,698,570 | 4,200,215 | 7,934,218 | 5,489,608 | 63,517,482 | 77,823,250 | 141,340,732 | 325,374 |
| Individually impaired | 503,566 | - | 37,487 | - | 962,271 | 1,503,324 | 33,365,355 | 34,868,679 | - |
| **Total** | **33,698,436** | **12,698,570** | **4,237,702** | **7,934,218** | **6,451,880** | **65,020,806** | **131,369,833** | **196,390,640** | **35,573,308** |
| **Impairment allowance** | **467,808** | **712,610** | **319,152** | **636,461** | **990,703** | **3,126,734** | **15,703,847** | **18,830,581** | **325,374** |
| Group-level impairment allowance | 329,772 | 712,610 | 306,438 | 636,461 | 855,235 | 2,840,516 | 9,583,119 | 12,423,635 | 325,374 |
| Individual impairment allowance | 138,036 | - | 12,714 | - | 135,468 | 286,218 | 6,120,728 | 6,406,946 | - |
| **Net carrying value** | **33,230,629** | **11,985,960** | **3,918,550** | **7,297,757** | **5,461,176** | **61,894,072** | **115,665,986** | **177,560,058** | **35,247,935** |

**4. RISK MANAGEMENT (Continued)**
**4.1. Credit Risk (Continued)**

### 4.1.1. Maximum Credit Risk Exposure (Continued)

*Impaired Loans and Receivables*

Impaired loans and receivables are those for which the Bank has determined the existence of objective evidence of impairment and does not expect them to be collected in full amounts of principal and interest matured pursuant to the relevant loan agreements. Loans and receivables are impaired on both an individual and a group basis.

*Receivables Matured but not Impaired*

Loans and receivables matured but not impaired represent those loans and receivables where there is default in settling liabilities for contractually agreed interest or principal outstanding (the report shows the entire receivable amount as matured for any matured portion of principal or interest). The Bank believes that it is not appropriate to make impairment allowance for such receivables given that there is certainty of collection by the Bank.

*Receivables not Matured and not Impaired*

Loans and receivables not matured and not impaired are those determined as ineligible for impairment allowance given the probability of default status and certainty of collection by the Bank (loans and receivables due from the Republic of Serbia).

## 4. RISK MANAGEMENT (Continued)
## 4.1. Credit Risk (Continued)

### 4.1.1. Maximum Credit Risk Exposure (Continued)

**Loans and receivables due from customers, banks and other financial institutions, not matured and not impaired**

December 31, 2014

| | Housing Loans | Cash Loans | Agricultural Loans | Other Loans | Micro Business | Total Retail | Corporate Customers | Total | Due from Banks |
|---|---|---|---|---|---|---|---|---|---|
| Low (IR 1, 2) | - | - | - | - | - | - | 2,313,323 | 2,313,323 | 27,510,292 |
| Medium (IR 3) | - | - | - | - | - | - | - | - | 22,935 |
| **Total** | **-** | **-** | **-** | **-** | **-** | **-** | **2,313,323** | **2,313,323** | **27,533,227** |

December 31, 2013

| | Housing Loans | Cash Loans | Agricultural Loans | Other Loans | Micro Business | Total Retail | Corporate Customers | Total | Due from Banks |
|---|---|---|---|---|---|---|---|---|---|
| Low (IR 1, 2) | - | - | - | - | - | - | 5,229,621 | 5,229,621 | 34,204,200 |
| Medium (IR 3) | - | - | - | - | - | - | 4,078,835 | 4,078,835 | 35,284 |
| **Total** | **-** | **-** | **-** | **-** | **-** | **-** | **9,308,456** | **9,308,456** | **34,239,484** |

**Loans and receivables due from customers, banks and other financial institutions**

December 31, 2014

| | Housing Loans | Cash Loans | Agricultural Loans | Other Loans | Micro Business | Total Retail | Corporate Customers | Total | Due from Banks |
|---|---|---|---|---|---|---|---|---|---|
| Up to 30 days past due | - | - | - | - | - | - | 1,375,310 | 1,375,310 | 7,204,378 |
| 31 - 90 days past due | - | - | - | - | - | - | - | - | - |
| Over 90 days past due | - | - | - | - | - | - | 181,996 | 181,996 | - |
| **Total** | **-** | **-** | **-** | **-** | **-** | **-** | **1,557,306** | **1,557,306** | **7,204,378** |

December 31, 2013

| | Housing Loans | Cash Loans | Agricultural Loans | Other Loans | Micro Business | Total Retail | Corporate Customers | Total | Due from Banks |
|---|---|---|---|---|---|---|---|---|---|
| Up to 30 days past due | - | - | - | - | - | - | 10,194,103 | 10,194,103 | 1,008,450 |
| 31 - 90 days past due | - | - | - | - | - | - | 73,340 | 73,340 | - |
| Over 90 days past due | - | - | - | - | - | - | 605,330 | 605,330 | - |
| **Total** | **-** | **-** | **-** | **-** | **-** | **-** | **10,872,773** | **10,872,773** | **1,008,450** |

**4. RISK MANAGEMENT (Continued)**
**4.1. Credit Risk (Continued)**

*4.1.2. Loans with Altered Initially Agreed Terms*

Loans with altered initially agreed terms are loans rescheduled and/or restructured due to the borrowers' difficulties in servicing liabilities as these fall due. Considering such difficulties, the Bank decides on altering the terms and deadlines stipulated by loan agreements giving the borrowers the opportunity to discharge liabilities more easily.

Rescheduling of receivables is performed for debtors with currently mismatching cash inflows and outflows, yet whose financial indicators have not deteriorates suggesting that the debtor will be able to settle the rescheduled liabilities according to the subsequently agreed repayment terms. Receivables are rescheduled if due from debtors up to 90 days in default, most commonly per individual loan subaccount, i.e. not including all the receivables due from the same debtor (not all loan subaccounts).

Restructuring is performed for loans due from debtors with significant problems in business where financial indicators are substantially deteriorating. Upon restructuring:

- All balance sheet receivables due from the debtor or a greater portion thereof are replaced;
- Terms whereunder the relevant receivable was approved are essentially altered (which particularly entails extension of the period for repayment of principal or interest, decrease in interest rate applied or the amount receivable and other modifications of terms which are to facilitate the position of a debtor);
- Adoption of an adequate financial consolidation program is mandatory.

**4. RISK MANAGEMENT (Continued)**
**4.1. Credit Risk (Continued)**

*4.1.2. Loans with Altered Initially Agreed Terms (Continued)*

The following table presents total amount of loans with altered initially agreed terms as of December 31,2014 and 2013. The stated values are presented in gross and net carrying amounts (after impairment effects).

*Loans with altered initially agreed terms, gross*

| | Rescheduled | | | | Restructured | | | |
|---|---|---|---|---|---|---|---|---|
| | December 31, 2014 | | December 31, 2013 | | December 31, 2014 | | December 31, 2013 | |
| | Gross | Net | Gross | Net | Gross | Net | Gross | Net |
| Housing loans | 596,943 | 556,173 | 568,206 | 532,674 | 145,546 | 137,391 | 84,024 | 71,652 |
| Cash loans | 224,193 | 210,710 | 198,795 | 188,299 | 40,721 | 28,648 | 43,887 | 32,549 |
| Agricultural loans | 64,211 | 55,919 | 137,523 | 123,176 | 32,673 | 29,229 | 41,370 | 36,647 |
| Other loans | 12,407 | 11,953 | 19,894 | 19,112 | 506 | 375 | 121 | - |
| Micro businesses | 200,575 | 188,381 | 256,623 | 215,083 | 401,880 | 341,390 | 428,898 | 389,271 |
| **Total retail** | **1,098,329** | **1,023,136** | **1,181,041** | **1,078,344** | **621,326** | **537,033** | **598,300** | **530,119** |
| Corporate customers | 23,582,662 | 23,058,599 | 26,507,514 | 26,076,310 | 16,995,750 | 12,581,987 | 12,004,182 | 7,412,417 |
| **Total** | **24,680,991** | **24,081,735** | **27,688,555** | **27,154,654** | **17,617,076** | **13,119,020** | **12,602,482** | **7,942,536** |

**Credit quality of loans and receivables (gross)**

| | December 31, 2014 | | | December 31, 2013 | | |
|---|---|---|---|---|---|---|
| | Loans and receivables | Rescheduled and restructured receivables | % | Loans and receivables | Rescheduled and restructured receivables | % |
| Not matured and not impaired | 2,313,323 | - | - | 9,308,456 | - | - |
| Matured but not impaired | 1,557,306 | - | - | 10,872,773 | - | - |
| Group-level impaired | 166,134,583 | 23,282,417 | 14.01% | 141,340,732 | 22,687,573 | 16.05% |
| Individually impaired | 38,456,800 | 19,015,650 | 49.45% | 34,868,679 | 17,603,464 | 50.49% |
| **Total** | **208,462,012** | **42,298,067** | **20.29%** | **196,390,640** | **40,291,037** | **20.52%** |
| **Impairment allowance** | **23,084,977** | **5,097,313** | **22.08%** | **18,830,581** | **5,193,847** | **27.58%** |
| Group-level impairment allowance | 12,095,209 | 401,437 | 3.32% | 12,423,635 | 2,349,655 | 18.91% |
| Individual impairment allowance | 10,989,768 | 4,695,876 | 42.73% | 6,406,946 | 2,844,192 | 44.39% |
| **Securitized with collaterals** | **180,511,165** | **35,538,202** | **19.69%** | **157,006,188** | **30,628,887** | **19.51%** |

## 4. RISK MANAGEMENT (Continued)
## 4.1. Credit Risk (Continued)

### 4.1.3. Concentration Risk

The Bank manages concentration risk by establishing a system of limits to the exposures with the same or similar risk factors (industry sectors/activities, product types, geographic regions, single entities or groups of related entities, collaterals…). Establishment of appropriate exposure limits is the basis for concentration risk control with the aim of loan portfolio diversification.

*Breakdown of loans and receivables due from customers, banks and other financial institutions and commitments per industry is provided below:*

| | Loans and receivables | | | | Off-balance sheet items | | | |
|---|---|---|---|---|---|---|---|---|
| | December 31, 2014 | | December 31, 2013 | | December 31, 2014 | | December 31, 2013 | |
| | Gross | Net | Gross | Net | Gross | Net | Gross | Net |
| **Finance and insurance sector** | **10,643,439** | **10,537,316** | **10,034,522** | **9,891,305** | **292,092** | **292,091** | **897,031** | **897,031** |
| **Corporate and public company sector** | **119,316,219** | **108,947,880** | **118,423,903** | **105,938,463** | **19,936,661** | **19,373,087** | **20,120,473** | **19,649,427** |
| Agriculture | 6,573,945 | 6,306,710 | 6,212,209 | 5,877,157 | 558,384 | 291,839 | 774,549 | 513,051 |
| Processing industry | 52,531,430 | 46,191,776 | 46,072,282 | 38,981,248 | 4,025,921 | 3,978,542 | 4,577,951 | 4,504,435 |
| Power industry | 6,329,773 | 6,329,319 | 8,783,688 | 8,783,265 | 921,693 | 921,592 | 781,666 | 781,586 |
| Construction industry | 4,738,069 | 4,348,898 | 4,849,182 | 4,307,481 | 7,488,399 | 7,376,936 | 4,325,512 | 4,274,384 |
| Wholesale and retail | 35,253,379 | 32,288,190 | 37,083,838 | 33,631,082 | 5,238,480 | 5,118,562 | 8,075,830 | 8,008,356 |
| Services industries | 11,572,132 | 11,290,458 | 12,858,509 | 11,921,957 | 962,197 | 950,536 | 823,166 | 813,958 |
| Real estate business | 2,317,491 | 2,192,529 | 2,564,195 | 2,436,275 | 741,587 | 735,080 | 761,799 | 753,657 |
| **Entrepreneurs** | **2,768,358** | **2,492,689** | **2,263,844** | **2,008,313** | **429,318** | **425,429** | **406,760** | **404,418** |
| **Public sector** | **10,943,750** | **10,912,080** | **13,555,594** | **13,525,198** | **339,888** | **338,928** | **72,843** | **72,833** |
| **Retail sector** | **65,592,670** | **62,989,218** | **58,568,927** | **56,432,896** | **8,652,116** | **8,652,116** | **8,567,239** | **8,567,239** |
| **Non-residents** | **17,215,508** | **16,870,780** | **21,183,663** | **20,882,595** | **105,098** | **105,098** | **635,722** | **635,722** |
| **Other customers** | **17,088,262** | **7,364,677** | **7,933,495** | **4,129,223** | **410,616** | **410,616** | **182,443** | **182,192** |
| **Total** | **243,568,206** | **220,114,640** | **231,963,948** | **212,807,993** | **30,165,789** | **29,597,365** | **30,882,511** | **30,408,862** |

Depending on general economic trends and individual industry sector trends, the Bank diversifies investments into the industry sectors that are resistant to the impact of adverse economic trends.

**4. RISK MANAGEMENT (Continued)**
**4.1. Credit Risk (Continued)**

**4.1.3. Concentration Risk (Continued)**

**Breakdown of loans and receivables due from customers, banks and other financial institutions and commitments per geographic area is provided below:**

| | Loans and receivables | | | | Off-balance sheet items | | | |
|---|---|---|---|---|---|---|---|---|
| | December 31, 2014 | | December 31, 2013 | | December 31, 2014 | | December 31, 2013 | |
| | Gross | Net | Gross | Net | Gross | Net | Gross | Net |
| Serbia | 219,294,893 | 196,202,331 | 198,460,191 | 179,624,778 | 30,046,297 | 29,477,873 | 30,230,779 | 29,757,132 |
| Montenegro | 156,391 | 154,536 | 570,466 | 564,898 | 1,708 | 1,708 | 1,798 | 1,798 |
| Bosnia and Herzegovina | 756,552 | 756,216 | 523,055 | 522,747 | - | - | 344,290 | 344,290 |
| European Union | 14,803,936 | 14,801,605 | 15,550,455 | 15,547,960 | 64,244 | 64,244 | 191,827 | 191,827 |
| USA and Canada | 398,411 | 135,285 | 620,163 | 400,250 | 45,916 | 45,916 | 108,023 | 108,023 |
| Other countries | 8,158,023 | 8,064,667 | 16,239,618 | 16,147,361 | 7,624 | 7,624 | 5,794 | 5,792 |
| **Total** | **243,568,206** | **220,114,640** | **231,963,948** | **212,807,993** | **30,165,789** | **29,597,365** | **30,882,511** | **30,408,862** |

**4. RISK MANAGEMENT (Continued)**
**4.1. Credit Risk (Continued)**

**4.1.4. Financial Assets**

| | December 31, 2014 | | December 31, 2013 | |
|---|---|---|---|---|
| | Gross | Net | Gross | Net |
| **Financial assets:** | **95,774,547** | **95,654,325** | **57,195,947** | **57,150,504** |
| - at fair value through profit and loss, held for trading | 121,634 | 121,634 | 115,577 | 115,319 |
| - available for sale | 95,481,744 | 95,481,249 | 56,887,797 | 56,885,285 |
| - held to maturity | 171,169 | 51,442 | 192,573 | 149,900 |
| **Changes in fair value of risk-hedged items** | - | - | - | - |
| **Receivables per derivatives designated as risk hedging instruments** | - | - | - | - |
| **Total** | **95,774,547** | **95,654,325** | **57,195,947** | **57,150,504** |

Financial assets at fair value through profit and loss relate to the Republic of Serbia's old foreign currency savings bonds, corporate and bank shares and investment units. These assets are measured using the methodology of adjusting to the market prices (mark to market) or internally developed valuation models (mark to model), depending on the availability of daily changing prices or whether they are subject of continuous trading.

Available-for-sale financial assets represent financial instruments which are intended to be held over an indefinite time period and which may be sold for liquidity purposes, due to the movements in interest rates, exchange rates or prices of capital. They mostly comprise Treasury bills and bonds issued by the Republic of Serbia, United Kingdom, local municipalities and bonds of other banks. Available-for-sale assets are initially measured at cost, and on a quarterly basis fair value thereof is determined based on the market prices for securities traded in active stock exchange (mark to market). Internally developed valuation models (mark to model) are used in instances that for certain financial instruments independent sources of market information are not available, and are based on the maturity of the security and the risk-free interest rate level.

Financial assets held to maturity entirely relate to discounted bills of exchange

**4.1.5. Credit Risk Hedges (Collaterals)**

For the purpose of protection against credit risk, in addition to regular monitoring of the customer business operations, the Bank also acquires security instruments (collaterals) to secure the collection of receivables and minimize credit risk. The collateral quantity and type depend on the assessed credit risk.

As a standard type of loan security instrument, the Bank demands and receives from clients contractual authorizations for account withdrawals and bills of exchange, whereas, depending on the credit risk assessment and loan type, additional collaterals agreed upon include the following:

- for commercial loans – pledge liens instituted over movable assets and immovable property (mortgages), deposits, banking, corporate and state-issued guarantees, sureties, pledge liens instituted over securities, equity interests, receivables and livestock;
- for retail loans – mortgages, deposits, co-sureties and insurance of the National Corporation for Housing Loans.

## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

#### 4.1.5. Credit Risk Hedges (Collaterals) (Continued)

For valuation of property or pledges assigned over movable assets, the bank hires certified appraisers in order to minimize potential risk of unrealistic valuation. Property, goods, equipment and other movables pledged must be insured by an insurance company acceptable to the Bank and insurance policies must be duly endorsed in favor of the Bank.

For protection against changes in the market value of collaterals (mortgages, pledge liens, securities, etc.) the appraised collateral value is adjusted for the predefined haircut percentage dependent on the type and location of collateral, which is reviewed at least annually, o more frequently, as appropriate. This is how the bank protects itself from potential losses arising from inability to collect its receivables from collateral foreclosure.

The Bank monitors and updates the values and trends in collaterals in order to minimize the risk of unrealistic valuation, if necessary, the bank may demand additional collateral in accordance with the executed loan agreements. Collaterals represent a secondary source of collection of receivables.

The following breakdowns present the value of collaterals as their fair values, only up to the loan gross amounts (in instances of collateral values exceeding the respective loan values). When collateral values are below the respective loan gross amounts, the values of collaterals are presented.

The values of collaterals and guarantees received to reduce credit risk exposures arising from the loans extended to customers are presented in the following table:

## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

#### 4.1.5. Credit Risk Hedges (Collaterals) (Continued)

**Loans and receivables due from customers secured with collaterals**

| | December 31, 2014 | | | | | December 31, 2013 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Properties | Deposits | Guarantees | Other collaterals | Total | Properties | Deposits | Guarantees | Other collaterals | Total |
| Housing loans | 30,748,217 | - | - | 4,867,522 | 35,615,739 | 28,503,974 | - | - | 2,523,140 | 31,027,114 |
| Cash loans | 97,639 | 274,274 | - | 3,242,179 | 3,614,093 | 110,319 | 265,752 | - | 1,463,046 | 1,839,117 |
| Agricultural loans | 2,849,789 | 16,463 | 73,816 | 1,321,095 | 4,261,163 | 2,328,436 | 44,270 | 72,414 | 728,305 | 3,173,425 |
| Other loans | 19,295 | 50,511 | - | 347,213 | 417,019 | 22,505 | 45,837 | - | 596,037 | 664,379 |
| Micro business | 2,494,280 | 464,556 | - | 4,846,869 | 7,805,705 | 2,875,782 | 475,741 | - | 2,528,028 | 5,879,551 |
| **Total retail loans** | **36,209,220** | **805,804** | **73,816** | **14,624,878** | **51,713,718** | **33,841,016** | **831,600** | **72,414** | **7,838,556** | **42,583,586** |
| Corporate loans | 58,205,326 | 1,100,476 | 8,680,492 | 60,811,153 | 128,797,447 | 70,472,795 | 1,113,839 | 9,426,051 | 33,409,917 | 114,422,602 |
| **Total** | **94,414,546** | **1,906,280** | **8,754,308** | **75,436,031** | **180,511,165** | **104,313,811** | **1,945,439** | **9,498,465** | **41,248,473** | **157,006,188** |

Note: A portion of housing loans secured with mortgages assigned over real estate properties is insured with the National Corporation for Housing Loans Insurance (2014: RSD 27.4 billion; 2013: RSD 25.5 billion).

## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

#### 4.1.5. Credit Risk Hedges (Collaterals) (Continued)

The ratio of the loan amount to the appraised value of the property held as collateral is monitored as loan to value ratio (LTV ratio).

**Breakdown of housing loans per LTV ratio spread**

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Below 50% | 5,301,359 | 4,851,190 |
| From 50% to 70% | 7,787,807 | 6,595,698 |
| From 71% to 100% | 14,119,316 | 13,661,280 |
| From 101% to 150% | 5,510,500 | 4,211,155 |
| Above 150% | 2,368,052 | 1,203,805 |
| Other | 2,706,351 | 3,175,308 |
| **Total exposure** | **37,793,385** | **33,698,436** |
| **Average LTV ratio** | **70.07%** | **69.85%** |

#### 4.1.6. Tangible Assets Acquired in Lieu of Debt Collection

Collaterals foreclosed by the Bank in the process of loan and receivable collection are provided below:

**Collaterals foreclosed**

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Residential premises | 204,802 | 279,216 |
| Business premises | 2,758,640 | 1,516,067 |
| Equipment | 106,469 | 101,805 |
| Land and forests | 155,737 | 71,722 |
| **Total** | **3,225,648** | **1,968,810** |
| Accumulated depreciation | (188,336) | (141,357) |
| **Net book value** | **3,037,312** | **1,827,453** |

In 2014, in the process of debt collection the bank foreclosed collaterals totaling RSD 2,313,063 thousand (2013: RSD 1,060,829 thousand).

### 4.2. Liquidity Risk

Liquidity risk represents the risk of negative effects on the Bank’s financial result and equity resulting from the Bank’s difficulty or inability to settle its matured liabilities in instances of insufficient liquidity reserves and inability to cover for unexpected outflows and other liabilities.

The Bank operates in accordance with the basic principles of liquidity, maintaining a sufficient level of funds to cover liabilities incurred in the short term, i.e. it observes the principle of solvency by establishing the optimal financial leverage and sufficient liquidity reserves which do not compromise realization of the projected return on equity.

**4. RISK MANAGEMENT (Continued)**

**4.2. Liquidity Risk (Continued)**

Liquidity risk is manifest as the mismatch of the inflow of assets on one end and the maturities of liabilities on the other, including the possibility of delays in expected inflows as well as that of unexpected outflows. Liquidity risk may be manifest as the risk related to sources of funds and market liquidity risk. The problem of liquidity in respect of the sources of funds relates to the structure of liabilities and is expressed through potential significant share of unstable and short-term sources of funds or their concentration. On the other hand, liquidity risk is reflected in reserves deficiency and difficulty or inability to obtain liquid assets at reasonable market prices.

The Bank has established appropriate organizational structure, which allows for clear differentiation between the process of assuming and the process of managing liquidity risk. The Asset and Liability Management Committee and Liquidity Committee have the most significant role therein as well as other competent boards/committees, whose decisions can impact the Bank's exposure to this risk.

In order to minimize liquidity risk, the Bank:

- Diversifies sources of assets in respect to their currencies and maturities;
- Forms sufficient liquidity reserves;
- Manages monetary funds;
- Monitors future cash flows and liquidity levels on a daily basis;
- Limits principal sources of credit risk with most significant impact on liquidity; and
- Defines and periodically tests Plans for Liquidity Management in Crisis Situations.

The liquidity management process comprises identification, measurement, minimizing, monitoring, control and liquidity risk reporting.

In identifying liquidity risk, the Bank identifies in a comprehensive and timely manner the causes that lead to the occurrence of liquidity risk determines current liquidity risk exposure as well as liquidity risk exposure arising from new business products and activities.

Measurement and assessment of liquidity risk in the Bank is performed through quantitative and/or qualitative assessment of identified liquidity risk by using the following techniques:

- GAP analysis;
- Ratio analysis; and
- Stress test.

Minimizing liquidity risk consists of maintaining this risk at a level that is acceptable to the Bank’s risk profile through definition of the system of exposure limits including both internal and statutory limits and timely implementation of measures to mitigate the risk and operation within the set internal and external limits.

Control and monitoring of liquidity risk includes the process of monitoring compliance with internally defined limits, and monitoring of defined measures for reducing the bank's exposure to liquidity risk. Liquidity risk control involves the control at all liquidity risk management levels as well as the independent control system implemented by the bank's organizational units responsible for internal audit and compliance monitoring.

Liquidity risk reporting consists of internal and external reporting systems and is performed on a daily basis and a set schedule according to the defined system. .

The Bank’s operations are reconciled daily with legally prescribed liquidity ratio as follows: minimum 0.8 for one working day; minimum 0.9 for no longer than three consecutive working days and minimum 1 as the average liquidity ratio for all working days in a month. The Bank also monitors compliance with the regulatory prescribed rigid/cash liquidity ratio as follows: minimum 0.5 for one working day; minimum 0.6 for no longer than three consecutive working days and minimum 0.7 as the average liquidity ratio for all working days in a month.

**4. RISK MANAGEMENT (Continued)**

**4.2. Liquidity Risk (Continued)**

**Compliance with liquidity ratio limits externally prescribed:**

| | Liquidity Ratio | | Rigid/Cash Liquidity Ratio | |
|---|---|---|---|---|
| | 2014 | 2013 | 2014 | 2013 |
| As at December 31 | 2.84 | 3.45 | 2.52 | 3.08 |
| Average for the period | 3.29 | 2.73 | 2.88 | 2.43 |
| Maximum for the period | 4.40 | 3.89 | 4.09 | 3.39 |
| Minimum for the period | 1.70 | 1.69 | 1.51 | 1.50 |

During 2014 the Bank's liquidity ratio and cash liquidity ratio were both well above the prescribed limits.

The Bank sets internal limits, based on the internal reporting on liquidity GAP for all balance sheet components.

**Compliance with last day liquidity ratio limits internally defined:**

| | Limits | 2014 | 2013 |
|---|---|---|---|
| GAP up to 1 month / Total assets | Max (10%) | 10.93% | 10.42% |
| Cumulative GAP up to 3 months / Total assets | Max (20%) | 12.08% | 6.75% |

In addition, the Bank limits and coordinates its operations with the limits defined for maturity per major foreign currencies.

**Maturity structure of monetary assets and monetary liabilities as of December 31, 2014**

| | Up to 1 month | From 1 - 3 months | From 3 -12 months | From 1 - 5 years | Over 5 years | Total |
|---|---|---|---|---|---|---|
| Cash and cash funds held with the central bank | 68,547,389 | - | - | - | - | 68,547,389 |
| Loans and receivables due from banks and other financial institutions | 34,501,291 | - | - | 236,314 | - | 34,737,605 |
| Loans and receivables due from customers | 35,403,685 | 11,911,181 | 48,217,308 | 55,461,224 | 34,383,637 | 185,377,035 |
| Financial assets (securities) | 10,804,439 | 9,710,565 | 24,456,167 | 42,389,721 | 8,293,433 | 95,654,325 |
| Other assets | 2,356,289 | - | 573,664 | 2,476 | - | 2,932,429 |
| **Total** | **151,613,093** | **21,621,746** | **73,247,139** | **98,089,735** | **42,677,070** | **387,248,783** |
| Deposits and other liabilities due to banks, other financial institutions and the central bank | 6,716,656 | 476,967 | 3,324,780 | 11,133,250 | 2,091,365 | 23,743,018 |
| Deposits and other liabilities due to customers | 145,966,665 | 27,209,991 | 87,116,252 | 39,314,095 | 2,347,908 | 301,954,911 |
| Subordinated liabilities | (11,235) | - | - | 6,047,915 | - | 6,036,680 |
| Other liabilities | 2,710,826 | - | 256,460 | - | - | 2,967,286 |
| **Total** | **155,382,912** | **27,686,958** | **90,697,492** | **56,495,260** | **4,439,273** | **334,701,895** |
| **Net liquidity gap** | | | | | | |
| **As of December 31, 2014** | **(3,769,819)** | **(6,065,212)** | **(17,450,353)** | **41,594,475** | **38,237,797** | **52,546,888** |
| **As of December 31, 2013** | **17,587,646** | **(15,002,185)** | **(29,496,029)** | **42,691,974** | **32,561,801** | **48,343,207** |

The report on the maturity structure of monetary assets and liabilities includes monetary balance sheet items distributed according to maturities outstanding, i.e. the conservative assumption was used that all transaction and demand deposits will be withdrawn within one month.

## 4. RISK MANAGEMENT (Continued)

### 4.2. Liquidity Risk (Continued)

The Bank collects deposits of corporate and retail customers which commonly have shorter maturity periods and can be withdrawn at the client request. Short-term nature of such deposits increases the bank's liquidity risk and requires active liquidity risk management and constant monitoring of market trends.

In near term, the Bank manages liquidity risk by monitoring and controlling items in all major currencies in order to identify the needs for additional funding in a timely manner in case of maturities of certain items, i.e. in the long term, the Bank plans the structure of its funding sources and investments in order to provide sufficient stable funding sources and liquidity reserves.

The Bank's management believes that adequate diversification of the deposit portfolio per number and type of depositors as well as historical experience provide a solid basis for existence of a stable and long-term deposit base, i.e. no significant outflow of funds is expected thereof.

The Bank regularly tests the Plans for Liquidity Management in Crisis Situations which are intended for testing potential crisis, checks the survival period and solvency, availability of funding for liabilities that could arise and assesses the support under the assumed crisis conditions.

**Undiscounted cash flows from monetary assets and monetary liabilities as of December 31, 2014**

| | Up to 1 month | From 1 - 3 months | From 3 -12 months | From 1 - 5 years | Over 5 years | Total |
|---|---|---|---|---|---|---|
| Cash and cash funds held with the central bank | 68,547,389 | - | - | - | - | 68,547,389 |
| Loans and receivables due from banks and other financial institutions | 40,816,045 | - | - | 268,225 | - | 41,084,270 |
| Loans and receivables due from customers | 36,421,274 | 13,938,739 | 55,306,004 | 71,228,553 | 48,350,757 | 225,245,327 |
| Financial assets (securities) | 11,232,816 | 10,436,803 | 26,171,255 | 46,008,849 | 8,631,016 | 102,480,739 |
| Other assets | 2,356,289 | - | 573,664 | 2,476 | - | 2,932,429 |
| **Total** | **159,373,813** | **24,375,542** | **82,050,923** | **117,508,103** | **56,981,773** | **440,290,154** |
| Deposits and other liabilities due to banks, other financial institutions and the central bank | 6,717,593 | 583,864 | 3,749,007 | 12,111,956 | 2,337,061 | 25,499,481 |
| Deposits and other liabilities due to customers | 146,312,504 | 27,628,455 | 89,937,195 | 43,111,370 | 2,562,758 | 309,552,282 |
| Subordinated liabilities | (11,235) | - | - | 6,660,934 | - | 6,649,699 |
| Other liabilities | 2,710,826 | - | 256,460 | - | - | 2,967,286 |
| **Total** | **155,729,688** | **28,212,319** | **93,942,662** | **61,884,260** | **4,899,819** | **344,668,748** |
| **Net liquidity gap** | | | | | | |
| **As of December 31, 2014** | **3,644,125** | **(3,836,777)** | **(11,891,739)** | **55,623,843** | **52,081,954** | **95,621,406** |
| **As of December 31, 2013** | **17,807,042** | **(14,524,891)** | **(28,776,753)** | **43,779,085** | **32,943,301** | **51,227,784** |

Undiscounted cash flows arising from the items of monetary assets and monetary liabilities include future cash flows per balance sheet items and future interest. In the case of transaction deposits and demand deposits, which, observing the conservative approach, are categorized into deposits with maturities of up to a month, the undiscounted cash flows include only the cash flows from the debt principal outstanding.

## 4. RISK MANAGEMENT (Continued)

### 4.3. Market Risk

Market risk represents the possibility of occurrence of negative effects on the Bank's financial result and equity due to changes in market variables and comprises interest rate risk, currency risk for all business operations and price risk for all items in the trading book.

The Bank is exposed to price risk, interest rate risk, currency risk, counterparty risk and risk of settlement related to trading book items. The trading book contains balance sheet and off-balance sheet assets and liabilities related to financial instruments that the Bank holds for trading or to hedge other financial instruments that are maintained in the trading book.

The Bank has established appropriate organizational structure, which allows for clear differentiation between the process of assuming market risks and the process of managing those risks. The Asset and Liability Management Committee (ALCO) and Investment Committee have the most significant role therein as well as other competent boards/committees, whose decisions can impact the Bank's exposure to this risk.

#### *4.3.1. Interest Risk*

Interest rate risk represents the probability of negative effects on the Bank's financial result and equity through items of the banking general ledger due to adverse interest rate fluctuations. The exposure to this risk depends on the relation between the interest rate sensitive assets and liabilities.

The Bank manages the following types of interest rate risk:

- Repricing risk of temporal mismatch between maturity and repricing;
- Yield curve risk – to which the Bank is exposed due to changes in yield curve shape;
- Basis risk – to which the Bank is exposed due to different reference interest rates for interest rate sensitive items with similar maturity or repricing characteristics; and
- Optionality risk – to which the Bank is exposed due to contractually agreed optional terms – loans with an option of early repayment, deposits with an option of early withdrawal, etc.

The basic objective of interest rate risk management is maintaining the acceptable level of interest rate risk exposure from the aspect of the effect on the financial result, by conducting adequate policy of matching periods of interest rate repricing, matching adequate sources to investments per interest rate type and maturity, as well as projecting movements in the yield curve in both foreign and domestic markets. Primarily, the Bank manages the internal yield margin through the prices of loans and deposits, focusing on the interest rate margin.

The Bank particularly considers the effects of interest rate changes and changes in the structure of interest-bearing assets and liabilities from the perspective of maturity, interest rate repricing and currency structure and manages the effect thereof on the economic value of equity.

The process of interest rate risk management consists of identification, measurement, minimizing, monitoring, control and interest rate risk reporting.

Identification of interest rate risk consists of comprehensive and timely identification of the causes and factors that lead to the occurrence of interest rate risk, which includes determining current interest rate risk exposure, as well as interest rate risk exposure arising from new business products and activities.

Measurement and assessment of interest rate risk at the Bank is performed through quantitative and/or qualitative assessment of identified interest rate risk by using the following techniques:

- GAP analysis;
- Ratio analysis;
- Duration;
- Economic value of equity; and
- Stress test.

## 4. RISK MANAGEMENT (Continued)

### 4.3. Market Risk (Continued)

*4.3.1. Interest Risk (Continued)*

Minimizing interest rate risk means maintaining this risk at a level that is acceptable for the Bank's risk profile. Alleviating interest rate risk refers to the process of defining the systems of limited exposure of the Bank to the interest rate risk and implementing measures for interest rate risk mitigation.

Control and monitoring of interest rate risk entails the process of monitoring compliance with the established system of limits as well as monitoring defined measures for reducing the Bank's exposure to the interest rate risk. Control of interest rate risk refers to control on all management levels as well as an independent control system implemented by the organizational units responsible for internal audit and compliance monitoring.

Interest rate risk reporting consists of an internal system of reporting to competent boards/committees and the Bank's interest rate risk management bodies.

Internal limits are determined based on the internal report on the interest rate GAP, which includes all the balance sheet items.

**Compliance with internally defined interest rate risk limits at the last day was as follows:**

| | Limits | 2014 | 2013 |
|---|---|---|---|
| Relative GAP | Max 15% | 0.69% | (3.66%) |
| Mismatch ratio | 0.75 – 1.25 | 1.01 | 0.95 |

During 2014 the Bank's interest rate risk ratios were within internally prescribed limits.

The Bank has defined internal limits for interest rate risk exposure per major currency as well as the limit of the maximum economic value of equity.

**Compliance with internally defined limits of economic value of equity:**

| | 2014 | 2013 |
|---|---|---|
| As at December 31 | 8.50% | 5.20% |
| Average for the year | 8.06% | 5.98% |
| Maximum for the year | 10.86% | 7.45% |
| Minimum for the year | 4.82% | 4.78% |
| Limit | 20% | 20% |

**4. RISK MANAGEMENT (Continued)**

**4.3. Market Risk (Continued)**

*4.3.1. Interest Risk (Continued)*

The exposure to interest rate risk can be reviewed through the Report on Interest Rate GAP in monetary assets and liabilities as follows:

**The Report on Interest Rate GAP in monetary assets and liabilities as of December 31, 2014:**

| | Up to 1 Month | From 1 - 3 Months | From 3 -12 Months | From 1 - 5 Years | Over 5 Years | Interest-Bearing | Non-Interest Bearing | Total |
|---|---|---|---|---|---|---|---|---|
| Cash and cash funds held with the central bank | 26,851,647 | - | - | - | - | 26,851,647 | 41,695,742 | 68,547,389 |
| Loans and receivables due from banks and other financial institutions | 33,780,001 | - | - | - | - | 33,780,001 | 957,604 | 34,737,605 |
| Loans and receivables due from customers | 90,548,334 | 15,341,940 | 42,720,426 | 16,077,662 | 16,509,149 | 181,197,511 | 4,179,524 | 185,377,035 |
| Financial assets (securities) | 11,934,760 | 19,667,235 | 17,413,798 | 36,993,447 | 8,187,593 | 94,196,833 | 1,457,492 | 95,654,325 |
| Other assets | - | - | - | - | - | - | 2,932,429 | 2,932,429 |
| **Total** | **163,114,742** | **35,009,175** | **60,134,224** | **53,071,109** | **24,696,742** | **336,025,991** | **51,222,791** | **387,248,783** |
| Deposits and other liabilities due to banks, other financial institutions and the central bank | 6,692,000 | 6,161,241 | 10,850,418 | 35,859 | 3,500 | 23,743,018 | - | 23,743,018 |
| Deposits and other liabilities due to customers | 155,202,029 | 24,083,955 | 82,952,118 | 36,617,677 | - | 298,855,779 | 3,099,132 | 301,954,911 |
| Subordinated liabilities | - | - | 6,036,680 | - | - | 6,036,680 | - | 6,036,680 |
| Other liabilities | - | - | - | - | - | - | 2,967,286 | 2,967,286 |
| **Total** | **161,894,029** | **30,245,196** | **99,839,216** | **36,653,536** | **3,500** | **328,635,477** | **6,066,418** | **334,701,895** |
| **Interest rate GAP:** | | | | | | | | |
| **- at December 31, 2014** | **1,220,713** | **4,763,979** | **(39,704,993)** | **16,417,573** | **24,693,242** | **7,390,515** | **45,156,373** | **52,546,888** |
| **- at December 31, 2013** | **4,146,816** | **(4,416,038)** | **(42,932,674)** | **8,448,556** | **21,414,967** | **(13,338,373)** | **61,681,580** | **48,343,207** |

**4. RISK MANAGEMENT (Continued)**

**4.3. Market Risk (Continued)**

*4.3.1. Interest Risk (Continued)*

Interest rate risk GAP report of monetary sub-balance includes monetary balance items distributed according to the shorter of period of interest rate repricing and maturity outstanding. In accordance with the aforesaid, the conservative assumption is used that all transactions and demand deposits will be withdrawn within one month.

The Bank's management believes that appropriate matching of items per interest rate type and interest rate repricing period constitutes a solid prerequisite for existence with required financial results achieved and maintenance of economic value of equity.

In addition to the GAP analyses, interest rate risk management also entails monitoring the sensitivity of the Bank's assets and liabilities to different scenarios of changes in interest rates. The Bank performs regular interest rate risk stress testing to assess the estimated impact of the changes in the key factors on the Bank's interest rate risk.

In scenario modelling, in addition to the changes in interest rates, particular consideration is given to the impact of early deposit withdrawal and early loan repayment, which the Bank estimates based on historical trends and expert estimates. The Bank estimated trends with regard to transaction deposits, demand deposits and savings deposits of retail customers using time series statistical modeling.

The standard scenario entails parallel changes (increases and decreases) in the interest rate by 100 basis points (b.p.). The Bank's sensitivity analysis, i.e. impact on the Bank's financial performance of the increase/decrease in the interest rates assuming symmetrical movement in yield curves and constant financial position is presented in the table below:

| | Parallel increases by 100 b.p. | Parallel decreases by 100 b.p. |
|---|---|---|
| **2014** | | |
| As at December 31 | 413,081 | (413,081) |
| Average for the year | 295,375 | (295,375) |
| Maximum for the year | 413,081 | (413,081) |
| Minimum for the year | 177,670 | (177,670) |
| **2013.** | | |
| As at December 31 | 376,389 | (376,389) |
| Average for the year | 341,589 | (341,589) |
| Maximum for the year | 376,389 | (376,389) |
| Minimum for the year | 306,788 | (306,788) |

*4.3.2. Currency Risk*

Currency risk represents the possibility of negative effects on the Bank's financial result and equity due to fluctuations in exchange rates between currencies, fluctuations in the domestic currency with respect to foreign currencies or changes in the value of gold and other precious metals. All items in the banking book and the trading book that are denominated in a foreign currency and gold, including dinar items indexed to foreign currency clause are exposed to currency risk.

In order to minimize the currency risk exposure, the Bank diversifies the currency structure of its portfolio and currency structure of liabilities, reconciling open positions in certain currencies pursuant to the principles of maturity transformation.

## 4. RISK MANAGEMENT (Continued)

### 4.3. Market Risk (Continued)

#### *4.3.2. Currency Risk (Continued)*

The Bank has established appropriate organizational structure, which allows for clear differentiation between the process of assuming currency risk and the process of managing currency risk. The Asset and Liability Management Committee has the most significant role therein as well as other competent boards/committees, whose decisions can impact the Bank's exposure to this risk.

The process of currency risk management entails identifying, measuring, minimizing, monitoring, control and currency risk reporting.

In identifying currency risks, the Bank identifies in a comprehensive and timely manner the causes that lead to emergence of currency risk and includes the determination of current currency risk exposure, as well as currency risk exposure resulting from new business products and activities.

Measurement and assessment of currency risk in the Bank is performed through quantitative and/or qualitative assessment of identified currency risk by using the following techniques:

- GAP analysis and currency risk ratio;
- VaR analysis;
- Stress test;
- Back testing.

Relieving foreign currency risk entails maintenance of risk at an acceptable level for the Bank’s risk profile through the establishment of a transparent system of limits and defining measures used to mitigate foreign currency risk.

Control and monitoring of the currency risk consists of observation and supervision of compliance with internally and externally defined limits as well as monitoring of defined and implemented measures. Continuous monitoring and control of foreign currency risk during the day ensures timely undertaking measures for the purpose of maintaining the currency risk within defined limits. Foreign currency risk control means control at all management levels as well as independent control system implemented by the organizational units responsible for internal audit and compliance monitoring.

Reporting on currency risk includes internal and external reporting systems. It is performed on a daily basis.

The Bank reconciles its business operations with the prescribed foreign currency risk ratio, which represents the ratio between the total net foreign currency balance and the position of gold relative to the Bank’s regulatory capital.

**Breakdown of the total currency risk balance and legally defined currency risk ratio at December 31:**

| | 2014 | 2013 |
|---|---|---|
| Total currency risk balance | 938,820 | 720,703 |
| Currency risk ratio | 2.90% | 2.12% |
| Legally-defined limit | 20% | 20% |

## 4. RISK MANAGEMENT (Continued)

### 4.3. Market Risk (Continued)

*4.3.2. Currency Risk (Continued)*

**Breakdown of Monetary Assets and Monetary Liabilities per Currencies as of December 31, 2014**

| | EUR | USD | CHF | Other Currencies | FX Total | Currency Clause EUR | Currency Clause USD | Currency Clause u CHF | RSD Items | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| Cash and cash funds held with the central bank | 40,085,327 | 128,877 | 394,499 | 281,353 | **40,890,056** | - | - | - | 27,657,333 | **68,547,389** |
| Loans and receivables due from banks and other financial institutions | 20,953,667 | 1,582,913 | 878,900 | 975,426 | **24,390,906** | - | - | - | 10,346,699 | **34,737,605** |
| Loans and receivables due from customers | 12,521,795 | 72,317 | - | - | **12,594,112** | 112,635,073 | - | 5,717,903 | 54,429,947 | **185,377,035** |
| Financial assets (securities) | 52,112,935 | 6,534,761 | 1,397,811 | 326,704 | **60,372,211** | 512,557 | - | - | 34,769,557 | **95,654,325** |
| Other assets | 1,256,445 | 407,356 | 183 | 37 | **1,664,021** | | - | - | 1,268,408 | **2,932,429** |
| **Total** | **126,930,169** | **8,726,224** | **2,671,393** | **1,583,520** | **139,911,306** | **113,147,630** | **-** | **5,717,903** | **128,471,944** | **387,248,783** |
| Deposits and other liabilities due to banks, other financial institutions and the central bank | 18,603,718 | 210,878 | 25,283 | 27,901 | **18,867,780** | 119,572 | - | - | 4,755,666 | **23,743,018** |
| Deposits and other liabilities due to customers | 210,386,406 | 7,442,589 | 8,256,064 | 1,419,632 | **227,504,691** | 3,656,178 | 690,265 | 2,475 | 70,101,302 | **301,954,911** |
| Subordinated liabilities | 6,036,680 | - | - | - | **6,036,680** | - | - | - | - | **6,036,680** |
| Other liabilities | 532,668 | 326,794 | 33,526 | 46,951 | **939,939** | - | - | - | 2,027,347 | **2,967,286** |
| **Total** | **235,559,472** | **7,980,261** | **8,314,873** | **1,494,484** | **253,349,090** | **3,775,750** | **690,265** | **2,475** | **76,884,315** | **334,701,895** |
| **Net currency position** | | | | | | | | | | |
| **- December 31, 2014** | **(108,629,303)** | **745,963** | **(5,643,480)** | **89,036** | **(113,437,784)** | **109,371,880** | **(690,265)** | **5,715,428** | **51,587,630** | **52,546,888** |
| **- December 31, 2013** | **(115,195,557)** | **64,250** | **(5,686,296)** | **57,151** | **(120,760,452)** | **114,477,937** | **(56,633)** | **5,703,061** | **48,979,294** | **48,343,207** |

## 4. RISK MANAGEMENT (Continued)

### 4.3. Market Risk (Continued)

#### *4.3.2. Currency Risk (Continued)*

**Ten-Day VaR**

The Bank also conducts currency risk stress testing to estimate the potential effects of specific events and/or changes in more than one financial variable on the Bank's financial result, capital and the currency risk ratio.

The VaR represents the highest possible loss in the Bank's portfolio during a specified period with a predefined confidence interval. The Bank calculates a one day and a ten day VaR, with a 99% confidence interval for foreign currency positions (currency VaR). In order to estimate the regulatory capital adequacy requirements regarding currency risk, the Bank calculates the VaR by using the generalized autoregressive-conditional heteroskedastic (GARCH) model for which it did not request approval from the National Bank of Serbia.

Currency VaR is calculated for foreign currency items as well as currency clause-indexed RSD items in both the banking book and trading book.

The breakdown of ten-day VaR with confidence interval of 99% for 2014 and 2013 is presented in the table below:

| | As of December 31 | Average | Maximum | Minimum |
|---|---|---|---|---|
| 2014 | | | | |
| Currency risk | 45,478 | 8,712 | 59,862 | 610 |
| 2013 | | | | |
| Currency risk | 5,551 | 24,391 | 117,205 | 538 |

### 4.4. Operational Risk

Operational risk represents the possibility of negative effects on the Bank's financial result and equity due to employee errors (intentional or accidental), inadequate procedures and processes in the Bank, inadequate management of information and other systems in the Bank, as well as occurrence of unforeseen external events. Operational risk includes legal risk.

Operational risk is defined as an event that occurred as the result of inappropriate or unsuccessful internal processes, employee and system actions or system and other external events, internal and external abuses, hiring and security practices at the workplace, customer receivables, product distribution, fines and penalties for infractions, damage incurred to property, disruptions in operations and system errors and process management.

The Bank monitors operational risk events according to the following business lines: corporate financing, trade and sales, retail brokerage services, corporate banking, retail banking, payment transfers, agency services and asset management.

The process of operational risk management represents an integral part of the Bank's activities conducted on all levels and ensures identification, measuring, relieving, monitoring and reporting continually on operational risks ahead of their realization, as in accordance with the legal requirements and deadlines. The existing process relies on known methods of measuring operational risk exposures, database on operating losses, an updated control and reporting system.

## 4. RISK MANAGEMENT (Continued)

### 4.4. Operational Risk (Continued)

The Bank monitors operational risk events daily and manages operating risks. For the purpose of efficient operational risk monitoring, the Bank appoints employees who are in charge of operational risk with the objective of monitoring operational risk in its every organizational part, where such employees are responsible for accuracy and timeliness of information about all operational risk events that occur in their organizational unit, as well as for keeping records about all such events in the operational risk database. The organizational part of the Bank which is responsible for risk management monitors and reports operational risks to the Bank's Board of Directors, the Bank's Executive Board and the Audit Committee.

Measurement and assessment of operational risk at the Bank is done through quantitative and/or qualitative assessment of identified operational risk. The Bank measures operational risk exposure through event records, self-assessment and stress testing. Self-assessment consists of assessment of risk exposure by organizational units based on the roadmap for identifying operating risks, through measurement of potential ranges and frequencies of events that can result in losses, identification of levels of control that business areas must maintain over these risks and measures of improvement. Stress test represents an operational risk management technique which is used to assess potential effects of specific events and/or changes in several financial variables on the Bank's exposure to operational risk.

The Bank cannot eliminate all operational risks, but by introducing a rigorous framework of control, monitoring and response to potential risks it is capable of managing these risks. The Bank takes measures in order to relieve operational risks and ensure proactive response to events potentially creating operational risks through continued monitoring of all activities, application of adequate and reliable information system and by applying project approach orientation, the implementation of which helps improve the business practice and optimize the Bank's business processes.

Through reliable reporting on the implementation of measures undertaken to mitigate operational risks, the Bank has established a system for monitoring the activities undertaken by the Bank's organizational parts in order to reduce arising operational risks. The Bank assess the risk of entrusting third parties with activities related to the Bank's operations and based on the service contracts executed with such third parties which clearly define terms, rights, obligations and responsibilities of the contracting parties.

With the objective of smooth and continued operation of all significant systems and processes in the Bank, and to limit losses that could be incurred in extraordinary circumstances, the Bank adopted the Business Continuity Plan, in order to ensure the restoration and recovery of the information technology systems in the event of interruption or stoppage of operations, the Bank adopted the Disaster Recovery Plan.

### 4.5. The Bank's Investment Risks

The Bank's investment risk relates to the risk of investing in other entities and capital expenditures. The Bank's investments in a non-financial sector entity cannot exceed 10% of the Bank's equity, whereby such investments entail investments through which the Bank acquires equity interest or shares in a non-financial sector entity. The total Bank's investment in non-financial sector entities and Bank's own fixed assets cannot exceed 60% of the Bank's equity, but this restriction does not apply to the acquisition of shares for further trading and sales thereof within six months from the acquisition date.

## 4. RISK MANAGEMENT (Continued)

### 4.6. Exposure Risk

Large exposures of the Bank to a single entity or a group of related entities, including Bank's related parties, are exposures amounting to over 10% of the Bank's capital.

In its operations, the Bank takes care of the compliance with statutory exposure limits:

- The Bank's exposure to a single entity or a group of related entities cannot exceed 25% of the Bank's equity;
- The Bank's exposure to a party that is related to the Bank cannot exceed 5% of the Bank's equity, while total exposure to the Bank's related parties cannot exceed 20% of the Bank's equity;
- The aggregate amount (sum) of the Bank's large exposures cannot exceed 400% of the Bank's equity.

The Bank's exposure to a single party or a group of related parties, as well as exposure to the Bank's own related parties, were within the prescribed limits.

### 4.7. Country Risk

Country risk relates to the risk of the country of origin of the entity the Bank is exposed to, i.e. the possibility of negative effects on the Bank's financial result and equity due to inability to collect receivables from abroad and is caused by political, economic and social conditions in the borrower's country of origin. Country risk includes the following risks:

- Political and economic risk relates to the likelihood of losses due to the inability to collect the Bank's receivables because of deterioration in macroeconomic stability, due to limitations prescribed by government regulations or due to other structural changes in the economy of the given country;

- Transfer risk relates to the probability of losses due to the inability to collect receivables in a currency which is not the official currency in the borrower's country of origin, due to limitations to liability settlement toward creditors from other countries in specific currency that is predetermined by the official state regulations and bylaws of state and other bodies of the borrower's country of origin.

Management of country risk is made per individual loans and receivables and at the Bank's portfolio level. Measurement of exposure of an individual receivable to country risk is based on the country rating of the Bank's borrower's country of origin as defined by internationally recognized agencies, while measurement of portfolio exposure to country risk is based on setting limits to exposure in terms of a percentage of the Bank's equity, depending on the internal country rating category. The Bank measures and controls portfolio exposure to country risk by grouping receivables by default level of risk of the borrower countries of origin.

For the purpose of adequate country risk control, the Bank defines exposure limits individually per borrower country of origin.

The Bank's loans approved to the borrowers domiciled outside of the Republic of Serbia for financing businesses in the Republic of Serbia, whose financial liabilities to the Bank are expected to be settled from the operating results achieved in the Republic of Serbia, represent the Bank's receivables without exposure to the risk of the borrower country of origin.

## 4. RISK MANAGEMENT (Continued)

### 4.8. Fair Value of Financial Assets and Liabilities

#### 4.8.1. Breakdown of carrying values and fair values of financial assets and liabilities other than measured at fair value

| | December 31, 2014 | | | | | December 31, 2013 | |
|---|---|---|---|---|---|---|---|
| | Carrying value | Fair value | Level 1 | Level 2 | Level 3 | Carrying value | Fair value |
| **Financial assets** | | | | | | | |
| Loans and receivables due from customers | 185,377,035 | 184,544,586 | | | 184,544,586 | 177,560,058 | 176,513,004 |
| Investment securities held to maturity | 51,442 | 51,442 | | | 51,442 | 149,900 | 149,900 |
| **Financial liabilities** | | | | | | | |
| Deposits and other liabilities due to customers | 301,954,911 | 301,788,878 | | | 301,788,878 | 266,020,289 | 265,858,821 |

Fair values of loans and receivables due from customers are estimated using the discounted cash flows model in instances of loans and receivables at fixed interest rates. Discounts rates are based on the current market interest rates applied to instruments offered under similar terms to borrowers with similar credit ratings. In addition, liabilities due to customers with defined maturities and contracted at fixed interest rates are discounted taking into account the prevailing terms according to the deposit types, terms and maturities.

Loans that are no longer approved and cannot be approved (loans indexed to CHF) are discounted at the same interest rates. In addition, loans approved at fixed interest rates subsidized by the Government were discounted at the same rate since the Bank would not have approved loans at low interest rates had the Government not subsidized portion of the interest rate. All loans and receivables approved at variable interest rates were approved in accordance with the prevailing market terms and the Bank's Business Policy.

Fair values of investment securities held to maturity are estimated using market prices or the discounted cash flows model based on current market interest rates applied to similar product instruments offered. Investment securities held to maturity have all matured resulting in the carrying values being equal to their fair values.

**4. RISK MANAGEMENT (Continued)**

**4.8. Fair Value of Financial Assets and Liabilities (Continued)**

**4.8.2. Financial instruments measured at fair value**

| | Level 1 | Level 2 | Level 3 | December 31, 2014 Total assets / liabilities at fair value |
|---|---|---|---|---|
| **Assets** | | | | |
| Financial assets at fair value through profit and loss | 121,634 | - | - | 121,634 |
| Securities available for sale (RSD) | - | 35,179,215 | - | 35,179,215 |
| Securities available for sale (FX) | - | 60,302,034 | - | 60,302,034 |
| **Total** | **121,634** | **95,481,249** | **-** | **95,602,883** |

| | Level 1 | Level 2 | Level 3 | December 31, 2013 Total assets / liabilities at fair value |
|---|---|---|---|---|
| **Assets** | | | | |
| Financial assets at fair value through profit and loss | 115,319 | | - | 115,319 |
| Securities available for sale (RSD) | - | 25,189,121 | - | 25,189,121 |
| Securities available for sale (FX) | - | 31,696,164 | - | 31,696,164 |
| **Total** | **115,319** | **56,885,285** | **-** | **57,000,604** |

Level 1 includes financial instruments traded in the stock exchange, while Level 2 includes securities whose fair values are estimated using the internally developed models based on the information from the auctions held in the secondary securities market (auctions).

Fair values of assets determined using the prices from the banking market are classified into Level 3.

**4.9. Capital Management**

The Bank has established a risk management system in accordance with the volume and structure of its business activities and the capital management is aimed at unhindered achievement of the Bank's business policy goals.

The calculation of the amount of capital and capital adequacy ratio is reconciled with the Basel II Standards.

The Bank manages capital on an ongoing basis in order to:

- Maintain the minimum regulatory capital requirement (EUR 10 million);
- Comply with the prescribed capital adequacy ratio (minimum 12%);
- Maintain customer trust in the safety and stability of the Bank's operations;
- Realize business and financial plans;
- Support the expected growth of loans and receivables due from customers;
- Ensure optimum future sources of funds and deployment thereof;
- Realize of the dividend policy.

The Bank's regulatory capital represents the sum of the core capital and supplementary capital, reduced for deductible items. The capital adequacy ratio represents the Bank's capital relative to the sum of credit risk-weighted assets, foreign currency gap and operational risk exposure. Credit risk-weighted assets are determined according to risk weights prescribed for all types of assets. Exposure to operational risk is determined by multiplying the reciprocal value of the prescribed capital adequacy ratio by the capital requirement for operational risk, which represent a three-year average of the product of exposure indicators for all lines of business by the prescribed capital requirement rates for each individual business line.

## 4. RISK MANAGEMENT (Continued)

### 4.9. Capital Management (Continued)

**Capital adequacy ratio**

| | 2014 | 2013 |
|---|---|---|
| Core capital | 33,286,532 | 45,134,001 |
| Supplementary capital | 4,593,961 | 4,961,842 |
| Deductible items | (5,555,355) | (16,076,615) |
| **Capital** | **32,325,138** | **34,019,228** |
| Credit risk-weighted assets | 162,919,928 | 161,509,806 |
| Operational risk exposure | 19,093,050 | 16,668,642 |
| Foreign currency risk exposure | 938,917 | 720,804 |
| **Capital adequacy ratio (minimum 12%)** | **17.67%** | **19.02%** |

In the course of 2014 the Bank's capital adequacy ratio was in excess of the prescribed regulatory limit of 12%.

Through its Capital Management Strategy and Capital Management Plan, the Bank ensures maintenance of the level and structure of the internal capital, which adequately supports increase in loans and receivables, future sources of funding and their utilizations, dividend policy and changes in regulatory requirements.

As part of the system of capital management, the Capital Management Plan, includes the following:

- Strategic goals and schedule for realization thereof;
- Manner of organizing the process of available internal capital management;
- Procedures for planning adequate levels of available internal capital;
- Manner of attaining and maintaining adequate levels of available internal capital; and
- The Business Continuity Plan in case of unforeseen events.

The Bank continuously implements processes of internal assessment of capital adequacy in accordance with the nature, volume and complexity of its business operations and in compliance with the adopted risk management strategy, individual risk management policies and capital management strategy.

As a documented and continuous process, internal assessment of capital adequacy meets the following criteria:

- it is based on risk identification and measurement;
- it provides comprehensive assessment and monitoring of risks the Bank is or may be exposed to;
- it provides adequate level of internally available capital according to the Bank's risk profile,
- it is included in the Bank's management system and decision making process; and
- it is subject to regular analysis, supervision and review.

Stages of the internal capital adequacy assessment include the following:

- determination of materially significant risks as per qualitative and quantitative criteria;
- calculation of the amounts of internal capital requirements;
- determination of the aggregate internal capital requirement;
- comparison of the following elements:
  - capital to available internal capital;
  - minimum prescribed capital requirements to internal capital requirements for individual risks; and
  - sum of the minimum capital requirements to the aggregate internal capital requirement.

## 5. USE OF ESTIMATES

Management makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and underlying assumptions are continually reviewed and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

### Key Sources of Estimation Uncertainty

*Provisions for Credit Losses*

Assets accounted for at amortized cost are assessed for impairment on a basis described in accounting policy 3(j) (vii).

The specific counterparty component of the total allowances for impairment applies to financial assets evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgments about counterparty's financial situation and the net realizable value of any underlying collateral. Each impaired asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are independently approved by the Credit Risk function.

Collectively assessed impairment allowances cover credit losses inherent in portfolios of loans and receivables and held-to-maturity investment securities with similar credit risk characteristics when there is objective evidence to suggest that they contain impaired items cannot yet be identified. In assessing the need for collective loss allowances, management considers factors such as credit quality, portfolio size, concentrations and economic factors. In order to estimate the required allowances, assumptions are made to define the way inherent losses are modelled and to determine the required input parameters, based on historical experience and current economic conditions. The accuracy of the allowances depends on the estimates of future cash flows for specific counterparty allowances and the model assumptions and parameters used in determining collective allowances.

*Determining Fair Values*

The determination of fair value for financial assets and liabilities for which there is no observable market price requires the use of valuation techniques as described in accounting policy 3(j) (vi). For financial instruments that trade infrequently and have little price transparency, fair value is less objective, and requires varying degrees of judgment depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument.

### Critical Accounting Judgments in Applying the Bank's Accounting Policies

Critical accounting judgments made in applying the Bank's accounting policies include:

*Impairment of Investments in Equity Shares*

Investments in equity shares are estimated for impairment in accordance with the method described under accounting policies 3(j) (vii) and 3(n).

## 5. USE OF ESTIMATES (continued)

### Critical Accounting Judgments in Applying the Bank's Accounting Policies (continued)

*Valuation of Financial Instruments*

The Bank accounting policy on fair value measurement is disclosed in accounting policy 3(j) (vi).

The Bank measures fair values using the following fair value hierarchy that reflects the significance of the inputs used valuation:

- Level 1: Quoted market price (unadjusted) in an active market for an identical instrument.
- Level 2: Valuation techniques based on observable inputs other than quoted prices, either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.
- Level 3: Valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

Fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments the Bank determines fair values using valuation techniques.

Valuation techniques include net present value and discounted cash flow models, comparison to similar instruments for which market observable price exist and other valuation models. Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates, credit spreads and other premiums used in estimating discount rates, bond and equity prices, foreign exchange rates, equity and equity index prices and expected price volatilities and correlations. The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date, which would have been determined by market participants acting at arm's length.

The Bank uses widely recognized valuation models for determining the fair value of common and more simple financial instruments, like interest rate and currency swaps that use only observable market data and require little management judgment and estimation. Observable prices and model inputs are usually available in the market for listed debt and equity securities, exchange traded derivatives and simple over the counter derivatives like interest rate swaps.

Availability of observable market prices and model inputs reduces the need for management judgment and estimation and also reduces the uncertainty associated with determination of fair values. Availability of observable market prices and inputs varies depending on the products and markets and is prone to changes based on specific events and general conditions in the future markets.

## 6. SEGMENT REPORTING

As described in the following passages, the Bank has three operating segments, which are the Bank's strategic divisions. The strategic divisions offer different products and services, and are managed separately based on the Bank's management and internal reporting structure. For each of the strategic divisions, the Bank's management reviews internal management reports on at least a monthly basis. The following summary describes the operations in each of the Bank's reporting segments:

| | |
|---|---|
| Corporate Banking | Includes loans, deposits and other transactions and balances with corporate customers |
| Retail Banking | Includes loans, deposits and other transactions and balances with retail customers |
| Investment banking and interbank operations | Include securities and other financial instruments, as well as transactions with banks |

Information regarding the results of each reporting segment is included below. Performance is measured based on segment profit before taxes, as included in the internal management reports that are reviewed by the Bank's Executive and Supervisory Boards. Segment profit is used to measure performance as management believes that such information is the most relevant in evaluating the results of certain segments relative to other entities that operate within these industries. Inter-segment pricing is determined on an arm's length basis.

## 6. SEGMENT REPORTING (Continued)

Operating segments report for 2014 is provided below:

| | Retail banking* | Corporate banking | Investment and Interbank operations | Other | Total |
|---|---|---|---|---|---|
| External revenues and expenses | | | | | |
| Interest, fee and commission income | 10,540,415 | 9,194,539 | 7,166,465 | - | 26,901,419 |
| Interest, fee and commission expenses | (5,002,794) | (1,594,687) | (2,287,595) | - | (8,885,076) |
| Net gains/losses from impairment allowance | (382,120) | (2,341,030) | (2,239) | - | (2,725,389) |
| Net foreign exchange gains/losses | - | - | (205,943) | - | (205,943) |
| Net other income and expenses | 60,140 | 298,208 | 60,140 | - | 418,488 |
| Profit before operating expenses | **5,215,642** | **5,557,029** | **4,730,828** | **-** | **15,503,499** |
| Direct operating expenses | (5,478,080) | (1,588,907) | (331,978) | - | (7,398,965) |
| Net income/expenses from related party transactions | 2,303,754 | (3,428,395) | 1,124,641 | - | - |
| Profit after operating expenses and related party transactions | **2,041,315** | **539,728** | **5,523,491** | **-** | **8,104,534** |
| Indirect operating expenses** | (1,868,265) | (1,144,048) | (334,632) | - | (3,346,945) |
| **Profit before taxes*** | **173,050** | **(604,320)** | **5,188,859** | - | **4,757,589** |
| **Assets per segment** | | | | | |
| Cash and cash funds held with the central bank | - | - | 68,547,389 | - | 68,547,389 |
| Loans and receivables due from banks and other financial institutions | - | - | 34,737,605 | - | 34,737,605 |
| Loans and receivables due from customers | 69,071,647 | 116,305,388 | - | - | 185,377,035 |
| Investment securities | - | - | 95,654,325 | - | 95,654,325 |
| Other | **-** | **-** | 5,480,888 | 16,464,283 | 21,945,171 |
| | **69,071,647** | **116,305,388** | **204,420,207** | **16,464,283** | **406,261,524** |
| **Liabilities per segment** | | | | | |
| Deposits and other liabilities due to banks, other financial institutions and the central bank | - | - | 23,743,018 | - | 23,743,018 |
| Deposits and other liabilities due to customers | 210,246,716 | 57,748,604 | 33,959,592 | - | 301,954,911 |
| Subordinated liabilities | - | - | 6,036,680 | - | 6,036,680 |
| Other | | - | - | 4,980,111 | 4,980,111 |
| | **210,246,716** | **57,748,604** | **63,739,290** | **4,980,111** | **336,714,720** |

* Loans to micro clients are presented within Retail banking segment
** Indirect operating expenses refer to expenses that are not controlled by the business segments

## 6. SEGMENT REPORTING (Continued)

Operating segments report for 2013 is provided below:

| | Retail banking* | Corporate banking | Investment and Interbank operations | Other | Total |
|---|---|---|---|---|---|
| External revenues and expenses | | | | | |
| Interest, fee and commission income | 10,034,643 | 11,325,958 | 6,156,383 | - | 27,516,985 |
| Interest, fee and commission expenses | (5,687,926) | (1,933,536) | (2,401,137) | - | (10,022,599) |
| Net gains/losses from impairment allowance | (241,744) | (3,024,372) | 46,041 | - | (3,220,075) |
| Net foreign exchange gains/losses | | | (48,733) | - | (48,733) |
| Net other income and expenses | 105,163 | 314,266 | 105,162 | - | 524,591 |
| **Profit before operating expenses** | **4,210,137** | **6,682,316** | **3,857,717** | **-** | **14,750,169** |
| Direct operating expenses | (5,092,812) | (1,413,775) | (281,088) | - | (6,787,675) |
| Net income/expenses from related party transactions | 2,312,653 | (4,124,184) | 1,811,531 | - | - |
| Profit after operating expenses and related party transactions | 1,429,978 | 1,144,356 | 5,388,160 | - | 7,962,493 |
| Indirect operating expenses** | (1,878,056) | (1,155,370) | (340,693) | - | (3,374,119) |
| **Profit before taxes*** | **(448,079)** | **(11,014)** | **5,047,467** | **-** | **4,588,375** |
| **Assets per segment** | | | | | |
| Cash and cash funds held with the central bank | - | - | 70,934,839 | - | 70,934,839 |
| Loans and receivables due from banks and other financial institutions | - | - | 35,247,935 | - | 35,247,935 |
| Loans and receivables due from customers | 61,832,082 | 115,727,976 | - | - | 177,560,058 |
| Investment securities | - | - | 57,150,504 | - | 57,150,504 |
| Other | - | - | 5,480,888 | 16,412,095 | 21,892,983 |
| | **61,832,082** | **115,727,976** | **168,814,166** | **16,412,095** | **362,786,319** |
| **Liabilities per segment** | | | | | |
| Deposits and other liabilities due to banks, other financial institutions and the central bank | | | 21,058,542 | - | 21,058,542 |
| Deposits and other liabilities due to customers | 189,120,025 | 45,178,850 | 31,721,413 | - | 266,020,289 |
| Subordinated liabilities | - | - | 5,711,409 | - | 5,711,409 |
| Other | - | - | - | 5,033,861 | 5,033,861 |
| | **189,120,025** | **45,178,850** | **58,491,364** | **5,033,861** | **297,824,101** |

** Loans to micro clients are presented within Retail banking segment
** Indirect operating expenses refer to expenses that are not controlled by the business segment

## 7. FINANCIAL ASSETS AND LIABILITIES - ACCOUNTING CLASSIFICATION AND FAIR VALUES

The following describes the methodologies and assumptions used to determine fair values for those financial instruments which are not already recorded at fair value in the financial statements:

*(i) Assets for which fair value approximates carrying value*

For financial assets and financial liabilities that are highly liquid or having a short term original maturity (less than one year) it is assumed that the carrying amount approximate to their fair value. This assumption is also applied to demand deposits, saving accounts without a specific maturity and variable interest rate financial instruments.

*(ii) Fixed rate financial instruments*

The fair value of fixed interest rate financial assets and liabilities carried at amortized cost are estimated by comparing market interest rates when they were first recognized with current market rates offered for similar financial instruments. The assessed fair values of assets and liabilities with fixed interest rates mostly correspond to the carrying values thereof given that the interest rates applied do not depart from market interest rates. There are no materially significant departures in this respect.

## 8. NET INTEREST INCOME

Net interest income includes:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Loans and receivables due from banks | 591,752 | 1,270,256 |
| Loans and receivables due from customers | 14,686,703 | 16,539,021 |
| Central bank | 587,127 | 710,674 |
| Investment securities | 5,358,797 | 3,503,823 |
| **Total interest income** | 21,224,379 | 22,023,774 |
| Deposits from and liabilities due to banks | 688,661 | 972,264 |
| Deposits from and liabilities due to customers | 6,133,656 | 7,233,835 |
| Borrowings received | 1,103,476 | 888,437 |
| **Total interest expenses** | 7,925,793 | 9,094,536 |
| **Net interest income** | 13,298,586 | 12,929,238 |

Total interest income and expenses calculated using the effective interest rate method presented in the table above relate to financial assets and liabilities other than those at fair value through profit or loss.

## 9. NET FEE AND COMMISSION INCOME/EXPENSES

Net fee and commission income/expenses includes:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| ***Fees and commission* income *in RSD*** | | |
| Payment transfer operations | 2,835,577 | 2,744,327 |
| Fees on issued loans and guarantees - retail customers | 20,011 | 21,602 |
| Fees on issued loans and guarantees - corporate customers | 259,847 | 249,650 |
| Fees on purchase and sale of foreign currencies | 443,916 | 542,380 |
| Brokerage and custody fees | 60,375 | 43,534 |
| Fees arising from card operations | 1,160,379 | 1,015,231 |
| Credit Bureau processing fees | 84,265 | 81,642 |
| Other banking services | 645,203 | 649,453 |
| | 5,509,573 | 5,347,819 |
| ***Fee and commission income in foreign currencies*** | | |
| Payment transfer operations | 86,079 | 78,584 |
| Fees on issued loans and guarantees - corporate customers | 2,383 | 4,799 |
| Brokerage and custody fees | 2,195 | 3,098 |
| Fees arising from card operations | 72,258 | 58,295 |
| Other banking services | 4,552 | 616 |
| | 167,467 | 145,392 |
| | 5,677,040 | 5,493,211 |
| ***Fee and commission expenses in RSD*** | | |
| Payment transfer operations | 206,287 | 213,196 |
| Fees arising on purchase and sale of foreign currencies | 19,437 | 51,282 |
| Fees arising from card operations | 273,557 | 235,321 |
| Credit Bureau processing fees | 64,802 | 65,184 |
| Other banking services | 128,585 | 114,501 |
| | 692,668 | 679,484 |
| ***Fee and commission expenses in foreign currencies*** | | |
| Payment transfer operations | 39,533 | 31,630 |
| Fees arising from card operations | 183,028 | 160,273 |
| Other banking services | 44,054 | 56,676 |
| | 266,615 | 248,579 |
| | 959,283 | 928,063 |
| **Net fee and commission income** | 4,717,757 | 4,565,148 |

## 10. NET GAINS ON FINANCIAL ASSETS HELD FOR TRADING

Net gains on the financial assets held for trading include:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Gains on the fair value adjustment of securities – bonds | 3,669 | 6,092 |
| Gains on the fair value adjustment of securities – investment units | 1,040 | 504 |
| Gains on the fair value adjustment of securities – shares | 426 | 958 |
| Gains on the sales of securities at fair value through profit and loss | 2,469 | 16,340 |
| | 7,604 | 23,894 |
| Losses on the fair value adjustment of securities – shares | (508) | (290) |
| Losses on the fair value adjustment of securities – bonds | (532) | (1,262) |
| Losses on the fair value adjustment of securities – investment units | (49) | - |
| Losses on the sales of securities and other financial assets held for trading | (439) | - |
| | (1,528) | (1,552) |
| Net gains on the financial assets held for trading | 6,076 | 22,342 |

## 11. NET GAINS ON FINANCIAL ASSETS AVAILABLE FOR SALE

Net gains on the financial assets available for sale include:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Gains on the sale of securities available for sale | 52,028 | 1,738 |
| Losses on the sale of securities available for sale | (746) | - |
| **Net gains on the financial assets available for sale** | 51,282 | 1,738 |

Gains on the sale of securities available for sale of RSD 52,028 thousand relate to the gains from the sale of old foreign currency savings bonds (2014 series) in the amount of RSD 8,248 thousand and the Republic of Serbia Treasury bills in the amount of RSD 43,780 thousand.

## 12. NET FOREIGN EXCHANGE LOSSES AND NEGATIVE CURRENCY CLAUSE EFFECTS

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Positive currency clause effects | 4,993,387 | 4,551,137 |
| Positive currency clause effects – value adjustment of securities | 14,022 | 7,737 |
| Foreign exchange gains – value adjustment of securities | 27,065 | 421,001 |
| Positive currency clause effects – retail customers | 2,607,787 | 1,946,214 |
| Foreign exchange gains | 6,504,190 | 1,440,279 |
| | 14,146,451 | 8,366,368 |
| Negative currency clause effects | (980,887) | (3,833,060) |
| Negative currency clause effects – value adjustment of securities | (3,392) | (7,452) |
| Negative currency clause effects – value adjustment of liabilities | (207,365) | (460,227) |
| Negative currency clause effects – retail customers | (343,072) | (1,716,465) |
| Foreign exchange losses | (12,817,678) | (2,397,897) |
| | (14,352,394) | (8,415,101) |
| **Net foreign exchange losses and negative currency clause effects** | (205,943) | (48,733) |

## 13. OTHER OPERATING INCOME

Other operating income relates to:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Gains on the valuation of property and equipment | - | 12,260 |
| Reversal of unreleased provisions for litigations | - | 381,670 |
| Other income from operations | 179,395 | 186,815 |
| Other income | 389,796 | 542,801 |
| **Total** | 569,191 | 1,123,546 |

Within the line item of other income the largest portion relates to the prior years' interest income from corporate customers and prior years' interest income from retail customers in the amount of RSD 177,926 thousand and RSD 41,570 thousand, respectively.

In 2014 the Bank received dividend from its subsidiary bank from Budva in the amount of RSD 120,689 thousand (EUR 1,000 thousand). The Bank withheld and paid withholding tax at the rate of 9% in Montenegro in the amount of RSD 10,862 thousand (EUR 90 thousand). The net amount of dividend paid was RSD 109,827 thousand, i.e., EUR 910 thousand.

Within the line item of other income from operations in 2014, the amount of RSD 101,130 thousand relates to rental income (out of which RSD 93,770 thousand relates to income from properties leased out for business purposes.

## 14. NET LOSSES FROM IMPAIRMENT OF FINANCIAL ASSETS AND CREDIT RISK-WEIGHTED OFF-BALANCE SHEET ASSETS

Net losses from impairment of financial assets relate to:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Impairment allowance of loans and receivables | 10,107,502 | 8,778,348 |
| Provisions for off-balance sheet items | 540,305 | 602,322 |
| Reversal of impairment allowance of loans and receivables | (7,476,813) | (5,583,660) |
| Reversal of provisions for off-balance sheet items | (445,528) | (576,908) |
| Income from collection of receivables previously written-off | (77) | (27) |
| **Total** | 2,725,389 | 3,220,075 |

Until the end of January 2015 the Bank did not have material collections of loans and receivables previously written off that would affect the reversal of impairment allowance in accordance with IAS 10.

**MOVEMENTS ON IMPAIRMENT ALLOWANCE ACCOUNTS AND PROVISION FOR OFF-BALANCE SHEET ITEMS**

| | Loans and receivables due from banks (Note 23.2) | Loans and receivables due from customers (Note 24.2) | Investment securities (Notes 21 and 22) | Other assets (Note 32) | Off-balance sheet liabilities (Note 36) | Total |
|---|---|---|---|---|---|---|
| **Balance as at January 1, 2014** | **325,374** | **18,830,581** | **45,185** | **1,764,028** | **473,647** | **21,438,815** |
| Charge for the year | 2,468 | 9,835,443 | 9,428 | 260,163 | 540,305 | 10,647,807 |
| Charge for the year | (2,452) | (6,714,653) | (12,715) | (746,993) | (445,528) | (7,922,341) |
| Decrease in impairment allowance | | 394,977 | - | - | - | 394,977 |
| Foreign exchange effects | 43,199 | 452,908 | 94 | 9,486 | - | 505,687 |
| Write-off | - | (268,885) | - | (1,530) | - | (270,415) |
| Other movements | - | 554,606 | 78,229 | 21,147 | - | 653,982 |
| **Balance as at December 31, 2014** | **368,589** | **23,084,977** | **120,221** | **1,306,301** | **568,424** | **25,448,512** |

## 15. STAFF COSTS

Staff costs include:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Net salaries | 2,519,942 | 2,583,349 |
| Net benefits | 429,025 | 408,709 |
| Payroll taxes | 373,034 | 413,507 |
| Payroll contributions | 783,688 | 757,473 |
| Considerations paid to seasonal and temporary staff | 40,725 | 54,145 |
| Provisions for retirement benefits - net | (2,748) | 4,014 |
| Other staff costs | 67,823 | 40,926 |
| **Total** | 4,211,489 | 4,262,123 |

## 16. DEPRECIATION/AMORTIZATION CHARGE

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Amortization charge – intangible assets (Note 26.2) | 283,451 | 258,440 |
| Depreciation charge – property and equipment (Note 27.2) | 524,597 | 501,092 |
| Depreciation charge – investment property (Note 28.1) | 36,584 | 33,116 |
| **Total** | 844,632 | 792,648 |

## 17. OTHER EXPENSES

Other expenses include:

| | Year Ended December 31, 2014. | 2013. |
|---|---|---|
| Cost of materials | 398,717 | 460,929 |
| Cost of production services | 2,176,374 | 2,036,059 |
| Non-material costs (without taxes and contributions) | 2,224,978 | 1,615,612 |
| Taxes payable | 139,132 | 142,444 |
| Contributions payable | 713,802 | 816,697 |
| Other costs | 34,037 | 39,297 |
| Other expenses | 210,113 | 408,592 |
| Losses on the valuation of property and equipment, investment property and intangible assets | 697 | 197,328 |
| Provisions for litigations | - | 13,100 |
| **Total** | 5,897,850 | 5,730,058 |

## 18. INCOME TAXES

18.1 Components of income taxes as of December 31 were as follows:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Deferred income tax benefits | 47,547 | 87,950 |
| Deferred income tax expenses | (19,559) | - |
| **Total** | 27,988 | 87,950 |

In 2014 and 2013 the Bank did not report current income tax expenses pursuant to the effective tax regulations.

## 18. INCOME TAXES (continued)

18.2 Reconciliation of the effective tax rate is presented in the table below:

| | 2014 | 2014 | 2013 | 2013 |
|---|---|---|---|---|
| Profit for the year before taxes | | **4,757,589** | | **4,588,375** |
| Tax calculated using the local income tax rate | 15% | 713,638 | 15% | 688,256 |
| Expenses not recognized for tax purposes | 1.18% | 56,261 | 1.63% | 74,673 |
| Tax effects of the net capital losses /gains | -0.01% | (412) | -0.01% | (73) |
| Tax effects of income reconciliation | -0.30% | (14,441) | -1.01% | (46,245) |
| Tax credit received and used in the current year | 0% | - | -1.06% | (48,356) |
| Tax effects of the interest income from debt securities issued by the Republic of Serbia, AP Vojvodina or NBS | -17.72% | (843,246) | -14.57% | (668,255) |
| Tax effect adjustments (used and new ones) | -0.59% | (27,988) | -1.92% | (87,950) |
| ***Tax effects stated within the income statement*** | - | **(27,988)** | - | **(87,950)** |

18.3 Movements in deferred taxes as at December 31 are presented as follows

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Balance as at January 1 | (10,156) | 4,896 |
| Occurrence and reversal of temporary differences | (140,251) | (15,052) |
| Balance as at December 31 | (150,407) | (10,156) |

## 19. CASH AND CASH FUNDS HELD WITH THE CENTRAL BANK

Cash and cash funds held with the central bank include:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| ***In RSD*** | | |
| Cash on hand | 2,466,110 | 2,524,909 |
| Gyro account | 25,191,123 | 22,926,420 |
| Interest on obligatory RSD reserves | - | 20,550 |
| Other RSD cash funds | 100 | 100 |
| | 27,657,333 | 25,471,979 |
| ***In foreign currencies*** | | |
| Cash on hand | 2,492,030 | 1,921,714 |
| Foreign currency obligatory reserves | 36,737,503 | 41,148,420 |
| Other cash funds | 1,660,523 | 2,392,726 |
| | 40,890,056 | 45,462,860 |
| **Total** | 68,547,389 | 70,934,839 |

*Adjustments to cash and cash equivalents for the purpose of preparing the statement of cash flows*

| | | |
|---|---|---|
| Foreign currency accounts held with foreign banks (Note 23.1) | 13,350,291 | 10,531,880 |
| Foreign currency obligatory reserves | (36,737,503) | (41,148,420) |
| Interest on obligatory RSD reserves | - | (20,550) |
| | (23,387,212) | (30,637,090) |
| Cash and cash equivalents reported in the statement of cash flows | 45,160,177 | 40,297,749 |

In the statement of cash flows the Bank reports on the cash funds held on the gyro account held with NBS, cash on accounts held with foreign banks, cash funds held on the account with the Central Securities Registry, Depository and Clearing House and cash on hand.

The gyro account balance includes the RSD obligatory reserves, which represent the minimum amount of RSD reserves allocated in accordance with the Decision on Obligatory Reserves Held with the NBS. In accordance with the said Decision, the obligatory dinar reserves are calculated based on the average daily carrying amount of RSD deposits, loans and other RSD liabilities during a single calendar month, using a rate in the range between 0% to 5%, depending on the maturity of liabilities and their sources, whereby dinar reserve is comprised of: obligatory RSD reserves, 36% of RSD equivalent of obligatory reserves in EUR to deposits up to 730 days, and 28% of RSD equivalent of obligatory reserves in EUR to deposits over 730 days (Official gazette of RS, no. 135/2014). The National Bank of Serbia pays interest on these dinar reserves in the amount of 2.5% per annum (2013: 2.5% p.a.).

The Bank calculates the obligatory reserves in foreign currency on the 17th day of the month based on the average balance of foreign currency deposits registered in the preceding calendar month. The required reserve in foreign currency is allocated onto a special account held with the National Bank of Serbia and these funds may be drawn as necessary. The Bank is under obligation to maintain the average monthly balance of the allocated foreign currency reserve in the amount of the calculated foreign currency obligatory reserve, where, for the purposes of realizing average daily balance of allocated required reserve, the daily balance on the account of required reserve may be below or above the calculated foreign currency obligatory reserve.

Foreign currency obligatory reserve does not accrue interest. During 2014, in accordance with the Decision on Required Reserves of Banks with the National Bank of Serbia, the Bank allocated a certain portion of its foreign currency reserve in dinars to its gyro account.

Other foreign currency cash funds of RSD 1,660,523 thousand (2013: RSD 2,392,726 thousand) entirely relate to the clearing account held with the s Central Securities Registry, Depository and Clearing House for trade in securities.

## 20. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT AND LOSS, HELD FOR TRADING

Financial assets held for trading comprise:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Securities held for trading (in RSD) | 51,458 | 21,569 |
| Securities held for trading (in foreign currencies) | 70,176 | 93,750 |
| | 121,634 | 115,319 |

Breakdown of financial assets held for trading is provided below:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| | Total assets held for trading | Total assets held for trading |
| Republic of Serbia bonds | 70,176 | 93,751 |
| Corporate shares | 3,787 | 3,574 |
| Bank shares | 180 | 490 |
| Investment units of OIF monetary fund | 47,491 | 17,504 |
| Balance as at December 31 | 121,634 | 115,319 |

## 21. FINANCIAL ASSETS AVAILABLE FOR SALE

Financial assets available for sale comprise*:*

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Securities available for sale (in RSD) | 35,179,709 | 25,191,634 |
| Securities available for sale (in foreign currencies) | 60,302,034 | 31,696,164 |
| | 95,481,743 | 56,887,798 |
| Impairment allowance of securities available for sale | (494) | (2,513) |
| | 95,481,249 | 56,885,285 |

***Financial assets available for sale***

*In RSD:*
Republic of Serbia Treasury bills in the amount of RSD 10,590,077 thousand; Republic of Serbia bonds in the amount of RSD 22,992,331 thousand; bonds from the City of Pančevo and Municipalities Stara Pazova and Šabac budgets in the amount of RSD 443,283 thousand; bonds of the company Tigar a.d., Pirot in the amount of RSD 69,769 thousand; and bonds of the following banks: Societe generale banka a.d., Beograd in the amount of RSD 1,084,159 thousand and AIK banka a.d., Niš in the amount of RSD 90 thousand.

Out of the total amount of impairment allowance, RSD 490 thousand relates to the bonds of the company Tigar a.d., Pirot.

## 21. FINANCIAL ASSETS AVAILABLE FOR SALE (continued)

*In foreign currencies:*
Republic of Serbia Treasury bills in the amount of RSD 10,257,953 thousand; long-term Government of the Republic of Serbia bonds in the amount of RSD 46,972, thousand; Republic of Serbia old savings bonds in the amount of RSD 1,346,991 thousand; foreign bank bonds - Raiffeisen Bank International in the amount of RSD 1,397,811 thousand; and bonds of the UK Government in the amount of RSD 326,704 thousand.

Movements on the account of impairment allowance of securities available for sale were as follows:

**Impairment allowance of securities available for sale**

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| **Individual impairment allowance** | | |
| Balance at January 1 | 2,512 | 2,546 |
| Current year impairment allowance: | | |
| Charge for the year | 1,962 | 16,607 |
| Effects of the changes in foreign exchange rates | 94 | 442 |
| Reversal | (4,074) | (17,083) |
| **Total individual impairment allowance** | 494 | 2,512 |

## 22. FINANCIAL ASSETS HELD TO MATURITY

Financial assets held to maturity comprise*:*

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Securities held to maturity (discounted bills of exchange) | 171,169 | 192,573 |
| Impairment allowance of securities held to maturity | (119,727) | (42,673) |
| | 51,442 | 149,900 |

***Financial assets held to maturity***

**Impairment allowance of securities held to maturity**

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| **Individual impairment allowance** | | |
| Balance at January 1 | 42,673 | 51,253 |
| Current year impairment allowance: | | |
| Charge for the year | 7,466 | 128,566 |
| Reclassified from individual to group impairment allowance | (24,411) | - |
| Reversal | (7,547) | (137,146) |
| Other | 32 | - |
| **Total individual impairment allowance** | 18,213 | 42,673 |
| **Group impairment allowance** | | |
| Balance at January 1 | - | - |
| Charge for the year | | |
| Reclassified from individual to group impairment allowance | 24,411 | - |
| Reversal | (1,094) | - |
| Other | 78,197 | - |
| **Total group impairment allowance** | 101,514 | - |
| **Total group and individual impairment allowance** | 119,727 | 42,673 |

## 23. LOANS AND RECEIVABLES DUE FROM BANKS AND OTHER FINANCIAL INSTITUTIONS

23.1 Loans and receivables due from banks include:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| ***RSD loans and receivables*** | | |
| Per repo transactions | 7,000,000 | 12,246,700 |
| Loans for working capital | 1,200,000 | 100,000 |
| Overnight loans | 2,200,000 | - |
| Other receivables | 27,567 | 28,986 |
| Prepayments | 24,595 | 2,602 |
| Impairment allowance | (105,463) | (105,463) |
| | 10,346,699 | 12,272,825 |
| ***FX loans and receivables*** | | |
| Foreign currency accounts held with foreign banks (Note 19) | 13,350,291 | 10,531,880 |
| Overnight loans | 8,094,628 | 9,238,017 |
| Other loans and receivables due from foreign banks | 575,355 | 480,225 |
| Foreign currency deposits placed with other banks | 1,117,200 | 1,046,461 |
| Prepayments | 3,513 | 6,920 |
| Other receivables | 15,924 | 17,165 |
| Loans to foreign banks (subsidiaries) | 604,792 | 653,460 |
| Secured foreign currency sureties | 892,329 | 1,220,893 |
| Impairment allowance | (263,126) | (219,911) |
| | 24,390,906 | 22,975,110 |
| | 34,737,605 | 35,247,935 |

As of December 31, 2013 securities acquired through repo transactions with the National Bank of Serbia amounting to RSD 7,000,000 thousand relate to the Treasury bills purchased from the National Bank of Serbia with maturities of up to 8 days at the annual interest rate of 6.2%.

Short-term RSD deposits of other banks were placed with the Bank for a period of a year at interest rates ranging from 6.0 % to 10.5% per annum.

Short-term foreign currency deposits of other banks were placed with the Bank for a period of a year at interest rates ranging from 0.01% to 0.8% annually for EUR deposits and from 0.02% to 0.4% and 0.05% for USD and CHF deposits, respectively.

Interest rates applied to the loans extended to subsidiary banks ranged between 3.75% plus EURIBOR and 3.83% plus EURIBOR.

23.2 Movements on the account of impairment allowance of loans and receivables due from banks are provided in the table below:

| | | |
|---|---|---|
| **Group impairment allowance** | | |
| Balance at January 1 | 325,374 | 333,437 |
| Current year impairment allowance: | | |
| Charge for the year | 2,468 | 990 |
| Effects of the changes in foreign exchange rates | 43,199 | 47,762 |
| Reversal | (2,452) | (56,815) |
| **Total group impairment allowance** | **368,589** | **325,374** |

## 24. LOANS AND RECEIVABLES DUE FROM CUSTOMERS

24.1 Loans and receivables due from customers:

| | 2014 | | | 2013 | | |
|---|---|---|---|---|---|---|
| | Gross Amount | Impairment Allowance | Carrying Amount | Gross Amount | Impairment Allowance | Carrying Amount |
| **Corporate customers** | | | | | | |
| Transaction account overdrafts | 655,510 | (188,902) | 466,608 | 870,024 | (145,294) | 724,730 |
| Working capital loans | 51,932,892 | (6,089,887) | 45,843,005 | 47,629,473 | (4,027,004) | 43,602,469 |
| Export loans | 2,181,694 | (887,774) | 1,293,920 | 2,905,328 | (927,611) | 1,977,717 |
| Investment loans | 35,389,792 | (2,081,382) | 33,308,410 | 36,897,924 | (1,337,528) | 35,560,396 |
| Purchased loans and receivables - factoring | 101,171 | (80,424) | 20,747 | 159,499 | (29,458) | 130,041 |
| Loans for payment of imported goods and services | 5,270,391 | (1,804,796) | 3,465,595 | 4,805,144 | (2,086,475) | 2,718,669 |
| Loans for discounted bills of exchange ,acceptances and payments made for guarantees called on | 1,865,582 | (1,058,213) | 807,369 | 1,888,584 | (1,013,810) | 874,774 |
| Other loans and receivables | 50,663,189 | (8,730,494) | 41,932,695 | 46,888,173 | (7,450,449) | 39,437,724 |
| Prepayments | 445,249 | (905) | 444,344 | 341,767 | - | 341,767 |
| Accruals | (283,166) | - | (283,166) | (359,271) | - | (359,271) |
| **Retail customers** | | | | | | |
| Transaction account overdrafts | 4,450,820 | (638,367) | 3,812,453 | 4,609,541 | (569,436) | 4,040,105 |
| Housing loans | 37,842,597 | (517,453) | 37,325,144 | 33,800,924 | (460,696) | 33,340,228 |
| Cash loans | 15,060,740 | (854,475) | 14,206,265 | 12,632,696 | (681,094) | 11,951,602 |
| Consumer loans | 597,545 | (49,927) | 547,618 | 1,165,521 | (55,983) | 1,109,538 |
| Other loans and receivables | 2,447,906 | (97,021) | 2,350,885 | 2,324,113 | (45,743) | 2,278,370 |
| Prepayments | 220,458 | (4,957) | 215,501 | 183,756 | - | 183,756 |
| Accruals | (380,358) | - | (380,358) | (352,557) | - | (352,557) |
| **Balance as at December 31** | **208,462,012** | **(23,084,977)** | **185,377,035** | **196,390,639** | **(18,830,581)** | **177,560,058** |

## 24. LOANS AND RECEIVABLES DUE FROM CUSTOMERS (Continued)

24.2 Movements on the account of impairment allowance of loans and receivables due from customers are presented in the table below:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| **Individual impairment allowance** | | |
| Balance as at January 1 | 6,406,946 | 3,410,334 |
| Current year impairment allowance: | | |
| Charge for the year | 5,715,603 | 4,825,093 |
| Reclassified from group to individual impairment allowance | 3,021,278 | 58,681 |
| Effects of the changes in foreign exchange rates | 517,703 | 37,365 |
| Reversal | (5,555,663) | (1,916,049) |
| Transfer from off-balance sheet items | 394,977 | - |
| Prior years' interest income | (171,669) | - |
| Other | 660,593 | (8,478) |
| **Total individual impairment allowance** | **10,989,768** | **6,406,946** |
| **Group impairment allowance** | | |
| Balance as at January 1 | 12,423,635 | 12,085,663 |
| Current year impairment allowance: | | |
| Charge for the year | 4,119,840 | 3,579,923 |
| Reclassified from group to individual impairment allowance | (3,021,278) | (58,681) |
| Effects of the changes in foreign exchange rates | 106,874 | (26,047) |
| Reversal | (1,158,990) | (3,136,099) |
| Write-off | (268,885) | (13,728) |
| Other | (105,987) | (7,396) |
| **Total group impairment allowance** | **12,095,209** | **12,423,635** |
| **Balance as at December 31** | **23,084,977** | **18,830,581** |

24.3 Short-term RSD and foreign currency loans were approved for periods from 30 days to one year, at interest rates ranging between 0.53% and 1.8% per month.

Long-term RSD and foreign currency loans were approved for periods from 1 to the maximum of 30 years, at interest rates ranging between 3.35% (increased by the interest rate agreed upon for the related monetary collateral) and 22.5% per annum.

**Risks and Uncertainties**

The Bank's management recorded provisions for potential credit losses based on all known or anticipated credit risks as of the issue date of the financial statements. The Bank's loan portfolio receivables were classified based on the most recent financial information available as well as based on the expected effects of the restructuring processes. If these effects fail to provide possibilities to settle the liabilities due to the Bank, the Bank's receivables are mostly collateralized by mortgages assigned over property held by debtors, as well as pledges on movables. In the case that the debt recovery actions undertaken by the Bank's management are unsuccessful, additional amounts of allowances for impairment and provisions for losses based on the assessed irrecoverability would be required in the forthcoming reporting periods.

## 25. INVESTMENTS IN SUBSIDIARIES

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| KomBank INVEST a.d., Beograd | 140,000 | 140,000 |
| Komercijalna banka a.d., Banja Luka | 2,974,615 | 2,974,615 |
| Komercijalna banka a.d., Budva | 2,366,273 | 2,366,273 |
| | 5,480,888 | 5,480,888 |

## 26. INTANGIBLE ASSETS

26.1 Intangible assets comprise:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Intangible assets | 388,775 | 527,025 |
| Intangible assets in progress | 16,999 | 10,420 |
| | 405,774 | 537,445 |

26.2 Movements on the account of intangible assets in 2014 and 2013 are presented below:

| | Licenses and Software | Intangible Assets in Progress | Total |
|---|---|---|---|
| **Cost** | | | |
| Balance at January 1, 2013 | 1,166,177 | 46,537 | 1,212,714 |
| Additions | - | 195,447 | 195,447 |
| Transfers | 231,564 | (231,564) | - |
| Balance at December 31, 2013 | 1,397,741 | 10,420 | 1,408,161 |
| Balance at January 1, 2014 | 1,397,741 | 10,420 | 1,408,161 |
| Additions | - | 151,781 | 151,781 |
| Transfers | 145,202 | (145,202) | - |
| Balance at December 31, 2014 | 1,542,943 | 16,999 | 1,559,942 |
| **Accumulated Amortization** | | | |
| Balance at January 1, 2013 | 612,276 | - | 612,276 |
| Charge for the year (Note 16) | 258,440 | - | 258,440 |
| Balance at December 31, 2013 | 870,716 | - | 870,716 |
| Balance at January 1, 2014 | 870,716 | - | 870,716 |
| Charge for the year (Note 16) | 283,451 | - | 283,451 |
| Balance at December 31, 2014 | 1,154,167 | - | 1,154,167 |
| **Net Book Value** | | | |
| - Balance at January 1, 2013 | 553,901 | 46,537 | 600,438 |
| - Balance at December 31, 2013 | 527,025 | 10,420 | 537,445 |
| - Balance at December 31, 2014 | **388,775** | **16,999** | **405,774** |

## 27. PROPERTY, PLANT AND EQUIPMENT

27.1 Property, plant and equipment comprise:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Property | 5,466,855 | 5,560,302 |
| Equipment | 838,138 | 926,305 |
| Investments in progress | 24,084 | 91,063 |
| | 6,329,077 | 6,577,670 |

27.2 Movements on the account of property and equipment in 2014 and 2013 are presented below:

| | Property | Equipment | Investment in Progress | Total |
|---|---|---|---|---|
| **Cost** | | | | |
| Balance at January 1, 2013 | 5,765,101 | 2,795,998 | 50,434 | 8,611,533 |
| Additions | - | - | 1,006,523 | 1,006,523 |
| Transfers from investment in progress (Note 28.1) | 287,195 | 379,504 | (965,894) | (299,195) |
| Transfers from investment property(Note 28.1) | 154,350 | - | - | 154,350 |
| Disposal and retirement | (3,743) | (112,618) | - | (116,361) |
| Appraisal (revaluation) increase | 972,450 | - | - | 972,450 |
| Appraisal (revaluation) decrease | (191,808) | - | - | (191,808) |
| Impairment due to force majeure | (27,806) | - | - | (27,806) |
| Balance at December 31, 2013 | 6,955,739 | 3,062,884 | 91,063 | 10,109,686 |
| Balance at January 1, 2014 | 6,955,739 | 3,062,884 | 91,063 | 10,109,686 |
| Additions | - | - | 1,128,920 | 1,128,920 |
| Transfers from investment in progress (Note 28.1) | 107,598 | 280,815 | (1,195,899) | (807,486) |
| Transfers to investment property(Note 28.1) | (7,001) | - | - | (7,001) |
| Disposal and retirement | (34,087) | (100,179) | - | (134,266) |
| Sales | (10,180) | (47,770) | - | (57,950) |
| Balance at December 31, 2014 | 7,012,069 | 3,195,750 | 24,084 | 10,231,903 |
| **Accumulated Depreciation** | | | | |
| Balance at January 1, 2013 | 1,031,410 | 1,889,510 | - | 2,920,920 |
| Charge for the year (Note 16) | 147,369 | 353,723 | - | 501,092 |
| Transfers from investment property(Note 28.1) | 20,755 | - | - | 20,755 |
| Impairment due to force majeure | (3,649) | - | - | (3,649) |
| Disposal and retirement | (2,923) | (107,323) | - | (110,246) |
| Appraisal (revaluation) increase | 226,092 | - | - | 226,092 |
| Appraisal (revaluation) decrease | (23,617) | - | - | (23,617) |
| Other | - | 669 | - | 669 |
| Balance at December 31, 2013 | 1,395,437 | 2,136,579 | - | 3,532,016 |
| Balance at January 1, 2014 | 1,395,437 | 2,136,579 | - | 3,532,016 |
| Charge for the year (Note 16) | 164,446 | 360,151 | - | 524,597 |
| Transfers to investment property(Note 28.1) | (1,394) | - | - | (1,394) |
| Disposal and retirement | (11,072) | (93,791) | - | (104,863) |
| Sales | (2,203) | (45,327) | - | (47,530) |
| Balance at December 31, 2014 | 1,545,214 | 2,357,612 | - | 3,902,826 |
| **Net Book Value** | | | | |
| - Balance at January 1, 2013 | 4,733,691 | 906,488 | 50,434 | 5,690,613 |
| - Balance at December 31, 2013 | 5,560,302 | 926,305 | 91,063 | 6,577,670 |
| - Balance at December 31, 2014 | 5,466,855 | 838,138 | 24,084 | 6,329,077 |

## 27. PROPERTY, PLANT AND EQUIPMENT (Continued)

The Bank had no buildings assigned under mortgage as collateral for the repayment of borrowings.

As a result of incomplete land registers, as at December 31, 2014, the Bank did not have title deeds as proof of ownership for 38 buildings and land lots stated at the net book value of RSD 1,726,221 thousand. The Bank's management has taken all actions necessary to obtain the appropriate property titles for these buildings.

Based on the annual count of assets, permanently unusable items of property, plant and equipment with the net book value of RSD 4,842 thousand were retired and derecognized from the Bank's records.

## 28. INVESTMENT PROPERTY

28.1 Movements on the account of investment property in 2014 and 2013 are presented below:

| | Total |
|---|---|
| **Cost** | |
| Balance at January 1, 2013 | 1,907,716 |
| Transfer from investments in progress (Note 27.2) | 299,195 |
| Transfer to property (Note 27.2) | (154,350) |
| Appraisal (revaluation) – decrease | (52,000) |
| Balance at December 31, 2013 | 2,000,561 |
| Balance at January 1, 2014 | 2,000,561, |
| Transfer from investments in progress (Note 27.2) | 807,486 |
| Transfer from property (Note 27.2) | 7,001 |
| Appraisal (revaluation) – decrease | (4,216) |
| Balance at December 31, 2014 | 2,810,832 |
| **Accumulated Depreciation** | |
| Balance at January 1, 2013 | 181,483 |
| Charge for the year (Note 16) | 33,116 |
| Transfer to property (Note 27.2) | (20,755) |
| Appraisal effect | (1,837) |
| Balance at December 31, 2013 | 192,007 |
| Balance at January 1, 2014 | 192,007 |
| Charge for the year (Note 16) | 36,584 |
| Transfer from property (Note 27.2) | 1,394 |
| Appraisal effect | (297) |
| Balance at December 31, 2014 | 229,688 |
| **Net Book Value** | |
| - Balance at January 1, 2013 | 1,726,233 |
| - Balance at December 31, 2013 | 1,808,554 |
| - Balance at December 31, 2014 | 2,581,144 |

As of December 31, 2014 the Bank stated investment property as totaling RSD 2,581,144 thousand comprised of leased out buildings/premises.

Pursuant to executed long-term lease agreements in 2014 the Bank transferred to investment property tangible assets acquired in lieu of debt collection (Beograd: Radnička 22 and Beogradska 39; Niš: Bulevar 12. februar bb and Gradina) totaling RSD 807,486 thousand.

## 28. INVESTMENT PROPERTY (Continued)

28.2 As of December 31, 2014 the net profit realized form investment property amounted to RSD 35,896 thousand:

| Property | Area in $m^2$ | Total Expenses | Total Rental Income | Net Profit |
|---|---|---|---|---|
| Beograd, Makedonska 29 | 5,553 | (21,239) | 34,162 | 12,923 |
| Niš, Vrtište new D building | 1,816 | (556) | 3,939 | 3,383 |
| Niš, TPC Kalča | 85 | (800) | 3,370 | 2,570 |
| Beograd, Omladinskih brigada 19 | 15,218 | (14,172) | 15,952 | 1,780 |
| Šabac, Majur, Obilazni put bb | 1,263 | (870) | 1,543 | 673 |
| Lovćenac, Maršala Tita bb, | 46,890 | (3,772) | 8,414 | 4,642 |
| Negotin, Save Dragovića 20-22 | 658 | (1,032) | 701 | (331) |
| Gradina, border crossing | 60 | (62) | 847 | 785 |
| Niš, Bulevar 12. februar bb | 816 | (745) | 2,198 | 1,453 |
| Beograd, Radnička 22 | 7,190 | (1,570) | 5,383 | 3,813 |
| Beograd, Beogradska 39 | 460 | (533) | 4,738 | 4,205 |
| | | (45,351) | 81,247 | 35,896 |

## 29. CURRENT TAX ASSETS

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Current tax assets (paid monthly advance income tax payments for 2014 as prescribed by the Corporate Income Tax Law) | 73,835 | 712,700 |

During 2014 the Bank had a refund of the prepaid income tax from the Tax Administration in the amount of RSD 1,000,000 thousand. The income tax was prepaid as a result of the obligatory monthly advance income tax payments for the years 2013 and 2014 pursuant to the Corporate Income Tax Law and of the fact that in 2013 the Bank had no tax liabilities in this respect due to tax exemption of the interest income from debt securities of the Republic of Serbia and the National Bank of Serbia.

The prerequisite for the prepaid income tax refund was a field inspection conducted by the Tax Administration, which identified no irregularities in the Bank's calculation and payment of the corporate income taxes.

## 30. DEFERRED TAX ASSETS AND LIABILITIES

30.1 Deferred tax assets and liabilities relate to:

| | 2014 Assets | 2014 Liabilities | 2014 Net | 2013 Assets | 2013 Liabilities | 2013 Net |
|---|---|---|---|---|---|---|
| Difference in net carrying amount of tangible assets for tax and financial reporting purposes | - | (64,287) | (64,287) | - | (105,617) | (105,617) |
| Effect of increase in deferred tax liabilities for securities available for sale and equity investments | 40,611 | (213,650) | (173,039) | - | - | - |
| Long-term provisions for retirement benefits | 26,750 | - | 26,750 | 42,088 | - | 42,088 |
| Impairment of assets | 60,142 | - | 60,142 | 53,291 | - | 53,291 |
| Assets based on calculation of public duties | 27 | - | 27 | 82 | - | 82 |
| **Total** | 127,530 | (277,937) | (150,407) | 95,461 | (105,617) | (10,156) |

30.2 Movements on temporary differences during 2014 and 2013 are presented as follows

| | Balance at January 1 | Recognized in Profit or Loss | Recognized in Equity | Balance at December 31 |
|---|---|---|---|---|
| Property and equipment | (105,617) | 40,696 | 634 | (64,287) |
| Securities | - | - | (173,039) | (173,039) |
| Long-term provisions for retirement benefits | 42,088 | (19,505) | 4,167 | 26,750 |
| Impairment of assets | 53,291 | 6,851 | - | 60,142 |
| Assets based on calculating public duties | 82 | (55) | - | 27 |
| **Total** | (10,156) | 27,987 | (168,238) | (150,407) |

| | Balance at January 1 | Recognized in Profit or Loss | Recognized in Equity | Balance at December 31 |
|---|---|---|---|---|
| Property and equipment | (57,760) | 55,145 | (103,002) | (105,617) |
| Long-term provisions for retirement benefits | 41,486 | 602 | - | 42,088 |
| Impairment of assets | 21,159 | 32,132 | - | 53,291 |
| Assets based on calculating public duties | 11 | 71 | - | 82 |
| **Total** | 4,896 | 87,950 | (103,002) | (10,156) |

## 31. NON-CURRENT ASSETS HELD FOR SALE AND ASSETS FROM DISCONTINUED OPERATIONS

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Non-current assets held for sale and assets from discontinued operations | 84,227 | 71,630 |
| | 84,227 | 71,630 |

Non-current assets held for sale:

| Property | Area in $m^2$ | Carrying Value |
|---|---|---|
| Jasika, business premises | 75.87 | 611 |
| Požarevac, M.Pijade 2, business premises | 790.82 | 31,839 |
| Požarevac, M.Pijade 2, business premises | 880.86 | 26,345 |
| Belgrade, Toše Jovanovića 7, business premises | 24.05 | 2,213 |
| Vrbas, M. Tita 49, business premises | 145.56 | 3,992 |
| Kruševac, Dositejeva bb, business premises | 431.51 | 19,227 |
| | | 84,227 |

The Bank's management still intends to realize the sale of all assets that were not sold during the past year.

## 32. OTHER ASSETS

Other assets comprise:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| ***In RSD*** | | |
| Fee receivables per other assets | 126,644 | 119,908 |
| Inventories | 144,119 | 157,876 |
| Assets acquired in lieu of debt collection | 3,225,648 | 1,968,810 |
| Prepaid expenses | 140,804 | 171,129 |
| Equity investments | 1,195,544 | 1,020,176 |
| Other RSD receivables | 1,729,226 | 4,469,560 |
| | 6,561,985 | 7,907,459 |
| *Impairment allowance of:* | | |
| Fee receivables per other assets | (61,494) | (56,482) |
| Assets acquired in lieu of debt collection | (188,336) | (141,357) |
| Equity investments | (448,581) | (446,954) |
| Other RSD receivables | (537,374) | (1,085,090) |
| | (1,235,785) | (1,729,883) |
| ***In foreign currencies*** | | |
| Other receivables from operations | 1,024,993 | 336,697 |
| Receivables in settlement | 809,686 | 323,250 |
| Other foreign currency receivables | 3,219 | 2,306 |
| | 1,837,898 | 662,253 |
| *Impairment allowance of* | | |
| Other receivables from operations | (94,922) | (60,913) |
| Receivables in settlement | (78,951) | (74,820) |
| | (173,873) | (135,733) |
| | 6,990,225 | 6,704,096 |

## 32. OTHER ASSETS (Continued)

Implementation of the effective regulations as of December 31, 2014 and the modified contents of the line item of other assets required reclassification of equity investments from equity investments to other assets as shown in the following table:

| *Equity investments* | 2014 | 2013 |
|---|---|---|
| Equity investments in banks and other financial organizations | 143,383 | 135,667 |
| Equity investments in companies and other legal entities | 460,913 | 457,178 |
| Equity investments in non-resident entities abroad | 591,248 | 427,331 |
| | 1,195,544 | 1,020,176 |
| *Impairment allowance of:* | | |
| Equity investments in banks and other financial organizations | (26,683) | (25,266) |
| Equity investments in companies and other legal entities | (421,898) | (421,688) |
| | (448,581) | (446,954) |

Equity investments in banks and other financial organizations relate to: Euroaxis banka a.d., Moskva in the amount of RSD 78,386 thousand, AIK banka a.d., Niš in the amount of RSD 61,061 thousand, Jubmes banka a.d., Beograd in the amount of RSD 2,053 thousand, Union banka d.d., Sarajevo in the amount of RSD 1,874 thousand and Universal banka in bankruptcy in the amount of RSD 9 thousand.

Equity investments in companies mostly pertain to: 14. oktobar a.d., Kruševac in the amount of RSD 324,874 thousand, RTV Politika d.o.o., Beograd in the amount of RSD 37,634 thousand, Kompanija Dunav osiguranje a.d., Beograd in the amount of RSD 50,737 thousand and Politika a.d., Beograd in the amount of RSD 39,187 thousand.

Equity investments in non-resident entities abroad relate to VISA Company in the amount of RSD 487,895 thousand and MASTER Card in the amount of RSD 103,353 thousand.

Impairment allowance of equity investments totaling RSD 448,581 thousand refers to the impairment of cost of those equity investments that have no market value, out of which the major portion refers to: 14. oktobar a.d., Kruševac - RSD 324,874 thousand, RTV Politika d.o.o., Beograd - RSD 37,634 thousand, Politika a.d., Beograd - RSD 28,484 thousand, Kompanija Dunav osiguranje a.d., Beograd - RSD 28,828 thousand and AIK banka a.d., Niš - RSD 19,287 thousand.

Other RSD receivables mostly refer to other receivables from operations totaling RSD 253,028 thousand, advances paid for working capital assets of RSD 81,704 thousand, rental receivables of RSD 369,862 thousand and interest receivables per other assets of RSD 268,543 thousand.

Other receivables from operations in foreign currencies for the most part pertain to receivables for purchase and sale of foreign currencies due from banks in the amount of RSD 725,750 thousand.

Movements on the allowance for impairment account related to other assets and prepayments during the year are presented in the table below:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Balance as at January 1 | 1,764,028 | 1,321,432 |
| Current year impairment allowance: | | |
| Charge for the year | 260,163 | 227,169 |
| Effects of the changes in foreign exchange rates | 9,486 | 736 |
| Reversal | (746,993) | (320,468) |
| Write-off | (1,530) | (10,056) |
| Other | 21,147 | 545,215 |
| **Balance as at December 31** | 1,306,301 | 1,764,028 |

Assets acquired in lieu of debt collection totaling RSD 3,225,648 thousand gross, less recorded impairment allowance of RSD 188,336 thousand, with the net book value of RSD 3,037,312 thousand relate to:

## 32. OTHER ASSETS (Continued)

*Properties acquired in lieu of debt collection after December 30, 2013 – amounts included in the calculation of reserves from profit in accordance with the relevant NBS decision*

| Property | Area in $m^2$ | Value | Acquisition Date |
|---|---|---|---|
| | 434.58 | 4,959 | 17/04/2013 |
| CM Vukovac, CM Milatovac, arable land | 132,450.00 | 586 | 16/05/2014 |
| Bor, Nikole Pašića 21, buildings, warehouse, plant | 3,823.00 | 90,913 | 08/05/2014 |
| Aleksinac, arable land (fields, vineyards, pastures) | 36,787.00 | 243 | 09/07/2014 |
| Subotica, Magnetna 17, production plant, warehouse | 2,492.00 | 50,865 | 18/07/2014 |
| Reževići, Montenegro, karst, category 5 forest | 1,363.20 | 24,483 | 22/07/2014 |
| Reževići, Montenegro, category 5 forest | 5,638.54 | 86,600 | 22/07/2014 |
| Bajina Bašta, Vojvode Mišića 72/1, family house | 110.25 | 2,800 | 01/08/2014 |
| Mokra Gora, house, meadows pastures, fields | 58,400.00 | 11,901 | 31/01/2014 |
| Kopaonik, house and yard | 337.00 | 10,955 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 30a, business premises 6/3 | 29.00 | 4,421 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 30a, business premises 7/3 | 44.00 | 6,683 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 30a, business premises 8/3 | 35.00 | 5,347 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 30a, business premises 9/3 | 34.00 | 5,141 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 30a, business premises 10/3 | 39.00 | 5,963 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 88, business premises no. 1 | 266.00 | 122,923 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 88, business premises no. 2 | 57.00 | 26,393 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 88, business premises no. 11 | 44.00 | 6,858 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 88, business premises no. 22 | 226.00 | 60,474 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 88, business premises no. 23 | 253.00 | 81,983 | 31/01/2014 |
| Novi Sad, Vardarska 1/b, business premises no. 1 | 291.00 | 48,629 | 31/01/2014 |
| Novi Sad, Tihomira Ostojića 4, business premises no. 7 | 134.00 | 17,664 | 31/01/2014 |
| Novi Sad, Polgar Andraša 40/a, business premises no. 8 | 81.00 | 10,702 | 31/01/2014 |
| Novi Sad, Polgar Andraša 40/a, business premises no. 9 | 79.00 | 10,495 | 31/01/2014 |
| Novi Sad, Polgar Andraša 40/a, business premises no. | 408.00 | 71,488 | 31/01/2014 |
| Zrenjanin, Bagljaš, Novosadski put 4, building, construction land, transformer substation, gas station, building in construction | 9,144.00 | 38,310 | 14/08/2014 |
| Beograd, Jurija Gagarina 153a, business premises | 30.00 | 6,538 | 27/08/2014 |
| Amerić, Mladenovac, category 3 and category 4 fields | 7,768.00 | 260 | 03/10/2014 |
| CO Kajtasovo, Bela Crkva, forest | 4,187.00 | 85 | 03/10/2014 |
| Mladenovac, Šepšin, fields, orchards | 25,136.00 | 551 | 03/10/2014 |
| Total I | | 815,213 | |

## 32. OTHER ASSETS (Continued)

*Properties acquired in lieu of debt collection in prior periods (12 months before) – amounts included in the calculation of reserves from profit in accordance with the relevant NBS decision*

| Property | Area in m$^2$ | Value | Acquisition Date |
|---|---|---|---|
| Mur, Novi Pazar, house and category 3 orchard | 1,190.00 | 5,535 | 06/04/2012 |
| I.C.P Kruševac, commercial building | 12,836.00 | 49,982 | 08/06/2012 |
| Soko Banja, arable land (orchard, fields) | - | 3,230 | 31/07/2013 |
| Novi Pazar, Ejupa Kurtagića 13, house | 139.90 | 4,010 | 24/07/2012 |
| Majur, Tabanovačka, category 4 arable field | 1,445 ha | 1,671 | 10/08/2012 |
| Mladenovac, category 3 arable field | 16,633 | 274 | 22/11/2012 |
| Prokuplje, Maloplanska 7, two buildings and land | 490,00 | 314 | 11/06/2012 |
| Obrenovac, Mislođin, arable field | 10,017 | 1,078 | 11/07/2012 |
| Gnjilica, category 7 arable field | 2,638.00 | 115 | 11/06/2008 |
| Hotel President, Čačak, at Bulevar oslobođenja bb | 2,278.92 | 113,882 | 12/02/2009 |
| Residential building, Čačak, at Ratka Mitrovića 6 | 195 | 3,706 | 12/05/2009 |
| Novi Pazar, Kej skopskih žrtava 44, store | 82.95 | 3,435 | 27/09/2006 |
| Novi Pazar, yard and category 4 meadow | 1 ha 24 a | 181 | 26/08/2010 |
| Tivat, Mrčevac – residential building, ancillary facilities in construction and garage | 277 | 5,512 | 23/12/2010 |
| Tutin, Buče category 4 forest | 8,292 | 338 | 26/11/2010 |
| NBGD, Milentija Popovića 5b, apartment MZ S2 no.3 | 173 | 41,779 | 24/12/2010 |
| NBGD, Milentija Popovića 5b, apartment I S2 no.5 | 171 | 41,283 | 24/12/2010 |
| NBGD, Milentija Popovića 5b, apartment II S2 no.9 | 175 | 42,273 | 24/12/2010 |
| Tutin, Ostrovica, forest, field and pasture | 110,782 | 601 | 30/07/2012 |
| Mali Požarevac, Veliko polje, category 3 and 4 fields | 21,915 | 328 | 27/09/2012 |
| Mur, Novi Pazar, forest, field and orchard | 3,496 | 4,379 | 12/07/2011 |
| Budva, category 4 forest | 974 | 4,113 | 27/05/2011 |
| Prijevor, category 4 forest | 1,995 | 4,838 | 27/05/2011 |
| Residential building Galathea | 925 | 319,214 | 21/11/2011 |
| Vranje, field, category 2 vineyard | 2,339 | 1,858 | 29/11/2013 |
| Prijepolje, Karoševina, saw mill | 450 | 1,126 | 08/11/2013 |
| Ćuprija, Alekse Šantića 2/24, apartment | 72.40 | 924 | 15/01/2013 |
| Leskovac, Kralja Petra I, commercial building | 335 | 5,863 | 04/02/2013 |
| Niš, Ivana Milutinovića 30, business premises | 438.39 | 5,614 | 23/04/2013 |
| Niš, Triglavska 3/1, apartment | 79.80 | 3,609 | 04/06/2013 |
| Vranić, Milijane Matić 2, commercial building, ancillary facilities and land | 10,584.24 | 27,571 | 09/07/2013 |
| Mladenovac, field, category 3 forest | 1,142 | 506 | 18/07/2013 |
| Niš, Bulevar 12. februara, warehouse, ancillary facility | 2,062 | 45,931 | 31/07/2013 |
| Kula, Železnička bb, business premises, warehouse, transformer substation | 7,959 | 25,071 | 22/11/2013 |
| Total II | | 770,144 | |

*Properties acquired in lieu of debt collection after December 30, 2013 – amounts excluded from the calculation of reserves from profit in accordance with the relevant NBS decision*

| Property | Area in m$^2$ | Value | Acquisition Date |
|---|---|---|---|
| Beograd, Resavska 29, building | 1,944 | 404,637 | 03/06/2014 |
| Beograd, Resavska 31, building | 3,411 | 697,131 | 03/06/2014 |
| Zemun, Cara Dušana 130, factory complex | 6,876 | 243,235 | 16/06/2014 |
| Valjevo, Rađevo selo, warehouse | 394 | 483 | 11/06/2014 |
| Total III | | 1,345,486 | |

## 32. OTHER ASSETS (Continued)

*Equipment acquired in lieu of debt collection in prior periods (12 months before)*

| Description | Value | Acquisition Date |
|---|---|---|
| Kruševac, movables (machinery, furniture, equipment) | 45,243 | 11/06/2012 |
| Niš and Soko Banja, movables (coffee processing line, transporters and cleaning equipment) | 34,701 | 31/07/2012 |
| Paraćin, coffee roasting line | 11,018 | 31/12/2012 |
| Vranić, equipment, production line | 10,843 | 09/07/2013 |
| Total IV | 101,805 | |

*Equipment acquired Equipment acquired in lieu of debt collection after December 30, 2013 – amounts excluded from the calculation of reserves from profit in accordance with the relevant NBS decision*

| Description | Value | Acquisition Date |
|---|---|---|
| Movables (installation materials, metal shelving) | 1,939 | 13/05/2014 |
| Equipment, inventories of waste materials | 2,660 | 18/07/2014 |
| Total V | **4,599** | |

*Equipment acquired Equipment acquired in lieu of debt collection after December 30, 2013 – amounts included in the calculation of reserves from profit in accordance with the relevant NBS decision*

| Description | Value | Acquisition Date |
|---|---|---|
| Peugeot 406, HDI | 60 | - |
| Thermal accumulation heater | 3 | - |
| Samsung TV set | 2 | -. |
| Total VI | **65** | |
| TOTAL (net book value) I + II+ III+ IV+V+VI | **3,037,312** | |

During 2014 the Bank sold seven properties thus decreasing the value of the assets acquired in lieu of debt collection by the total of RSD 74,482 thousand (two apartments in Novi Beograd, two apartments in Niš, a commercial building in Niš, a house in Sombor and a commercial and residential building in Grabovica). The total sales price of the aforesaid properties amounted to RSD 83,072 thousand. The Bank does not hold ownership titles for 22 properties. The Bank's management is undertaking all the necessary actions to sell such properties.

## 33. DEPOSITS AND OTHER LIABILITIES DUE TO BANKS, OTHER FINANCIAL INSTITUTIONS AND THE CENTRAL BANK

Deposits and other liabilities due to banks, other financial institutions and the central bank comprise:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Demand deposits | 6,230,123 | 1,587,917 |
| Term deposits | 1,139,880 | 6,079,898 |
| Borrowings | 16,467,781 | 13,380,370 |
| Expenses deferred at the effective interest rate (deductible item) | (142,034) | (122,469) |
| Other | 47,268 | 132,826 |
| **Balance as at December 31** | **23,743,018** | **21,058,542** |

Short-term RSD deposits placed by banks were deposited for periods of up to one year at interest rates ranging from 5.7 % to 9.1% per annum. In 2014 the Bank had no liabilities per long-term deposits placed by banks.

The largest portion of demand deposits relates to the transaction RSD deposit of Kompanija Dunav osiguranje a.d., Beograd amounting to RSD 4,822,226 thousand.

Newly enacted regulations define what extraterritorial organization and non-resident are regarded as banks and what as customers for the purposes of balance sheet preparation. This resulted in splitting and presenting the total liabilities per foreign loan facilities obtained in separate line items of the balance sheet, depending on the creditor.

Breakdown of long-term borrowings included within the line item of deposits and other liabilities due to banks is presented below:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| FEES | 5,926,957 | 5,011,497 |
| GAFF | 1,987,345 | 2,636,768 |
| FM | 2,419,166 | 2,292,842 |
| IF | 1,814,374 | - |
| EBRD | 4,319,939 | 3,439,263 |
| **Balance at December 31** | 16,467,781 | 13,380,370 |

The loan facility agreements executed with the creditors stipulate certain financial covenants. The methodology for calculating the financial ratios defined by loan facility agreements differs from the method for calculating those same ratios in accordance with the regulations of the National Bank of Serbia in part relating to the calculation of capital and includes items eligible for determining open credit exposure.

Pursuant to the loan agreements executed with the creditors listed in the table above, the Bank is obligated to comply with certain financial covenants until the final repayment of loans obtained. As of December 31, 2014, the Bank was in full compliance with all the contractually defined financial ratios toward the aforelisted foreign creditors.

## 34. DEPOSITS AND OTHER LIABILITIES DUE TO CUSTOMERS

Deposits and other liabilities due to customers comprise:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| **Corporate customers** | | |
| Demand deposits | 50,212,715 | 40,407,356 |
| Other deposits | 24,092,376 | 20,082,972 |
| Borrowings | 12,694,050 | 13,326,230 |
| Earmarked deposits | 8,115,734 | 4,050,221 |
| Deposits for loans approved | 674,136 | 543,924 |
| Interest payable, accrued interest liabilities and other financial liabilities | 737,675 | 1,814,390 |
| **Retail customers** | | |
| Demand deposits | 14,399,711 | 11,222,105 |
| Savings deposits | 183,902,102 | 168,941,206 |
| Earmarked deposits | 2,148,492 | 1,169,896 |
| Deposits for loans approved | 1, 509,090 | 1,476,736 |
| Interest payable, accrued interest liabilities and other financial liabilities | 3,420,497 | 2,943,262 |
| Other deposits | 48,333 | 41,991 |
| **Balance at December 31** | 301,954,911 | 266,020,289 |

*Corporate Customer Deposits*

RSD demand deposits of corporate customers mostly comprise balances of transaction deposits of companies and other legal entities. In accordance with the Decision on Interest Rates for 2014, these deposits became interest-bearing. Depending on the average monthly balances on these transaction accounts of the customers, the interest rate applied thereto ranged from 0.25% and 1.5% per annum.

Foreign currency demand deposits of non-resident customers are non-interest bearing, except for specific business arrangements.

In 2014 short-term RSD deposits of corporate customers were placed at annual interest rates ranging between the key policy rate less 4 percentage points for deposits placed up to 7 days to key policy rate less 2.05 percentage points for deposits placed up to a year per annum.

Short-term foreign currency deposits of corporate customers were placed at an interest rate ranging between 0.25% and 2.15% annually for EUR deposits and 1.2% annually for deposits in other currencies.

Long-term RSD deposits of corporate customers were placed at an interest rate determined by the amount of the National Bank of Serbia key policy annual rate decreased by 1.7 percentage points, whereas those denominated in foreign currency accrued interest at the annual rate of 1.09% for other currencies and 2.75% for EUR.

In 2014 short-term deposits of corporate customers indexed to EUR exchange rate were placed at interest rates ranging from 0.5% to 1.3% annually.

Long-term deposits of corporate customers indexed to EUR exchange rate were placed at interest rates ranging from 1.6% to 1.9% annually.

*Retail Customer Deposits*

Demand RSD savings deposits of retail customers were placed at the annual interest rate of 0.15%, while foreign currency demand deposits accrued interest at the respective rates of 0.15% and 0.05% for EUR and other currencies per annum.

## 34. DEPOSITS AND OTHER LIABILITIES DUE TO CUSTOMERS (Continued)

*Retail Customer Deposits (Continued)*

In 2014 short-term dinar RSD deposits of retail customers were placed at interest rates ranging from 4.25% to 8.5 % annually and those in foreign currencies at rates from 0.05% to 2.55% annually.

Long-term RSD deposits of retail customers were placed at interest rates ranging from 7.75% to 10.25 annually and those in foreign currencies at rates from 1% to 3.1% annually.

Newly enacted regulations define what extraterritorial organization and non-resident are regarded as banks and what as customers for the purposes of balance sheet preparation. This resulted in splitting and presenting the total liabilities per foreign loan facilities obtained in separate line items of the balance sheet, depending on the creditor.

Breakdown of long-term borrowings included within the line item of deposits and other liabilities due to customers is presented below:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| LEDIB 1 and 2 (Kingdom of Denmark) | 19,602 | 18,406 |
| Republic of Italy Government | 798,788 | 1,062,640 |
| European Investment Bank (EIB) | 5,629,831 | 5,781,447 |
| European Agency for Reconstruction (EAR) | 197,913 | 158,421 |
| KfW | 6,047,916 | 6,305,316 |
| **Balance at December 31** | 12,694,050 | 13,326,230 |

The above presented long-term borrowings mature in the period from 2014 to 2022.

The loan facility agreements executed with the creditors stipulate certain financial covenants. The methodology for calculating the financial ratios defined by loan facility agreements differs from the method for calculating those same ratios in accordance with the regulations of the National Bank of Serbia in part relating to the calculation of capital and includes items eligible for determining open credit exposure.

Pursuant to the loan agreements executed Kreditanstalt fur Wiederaufbau (German Development Bank, abbreviated: KfW), the Bank is obligated to comply with certain financial covenants until the final repayment of loans obtained. As of December 31, 2014, the Bank was in full compliance with all the contractually defined financial ratios toward the aforesaid foreign creditor.

## 35. SUBORDINATED LIABILITIES

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Foreign currency subordinated liabilities | 6,047,915 | 5,732,105 |
| Other liabilities (accrued interest liabilities) | 14,077 | 13,054 |
| Expenses deferred at the effective interest rate (deductible item) | (25,312) | (33,750) |
| **Balance at December 31** | 6,036,680 | 5,711,409 |

In accordance with the regulations of the National bank of Serbia related to the capital adequacy requirements and implementation of the Basel II Standard, in 2011 the Bank enhanced its core capital by obtaining a subordinated loan from the International Finance Corporation (IFC). The subordinated loan received totaled RSD 6,047,915 thousand, i.e., EUR 50,000 thousand as of December 31, 2014.

## 36. PROVISIONS

Provisions relate to:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Provisions for off-balance sheet items (Note 14) | 568,424 | 473,647 |
| Provisions for litigations (Note 39.3) | 766,556 | 10,900 |
| Provisions for employee benefits in accordance with IAS 19 | 305,615 | 280,585 |
| **Balance at December 31** | 1,640,595 | 765,132 |

Movements on the accounts of provisions are provided below:

| | 2014 | | | | 2013 | | | |
|---|---|---|---|---|---|---|---|---|
| | **Provisions for Off- Balance Sheet Items (Note 14)** | **Provisions for Litigations (Note 39.3)** | **Provisions for Employee Benefits (IAS 19)** | **Total** | **Provisions for Off- Balance Sheet Items (Note 14)** | **Provisions for Litigations (Note 39.3)** | **Provisions for Employee Benefits (IAS 19)** | **Total** |
| Balance, January 1 | 473,647 | 10,900 | 280,585 | 765,132 | 497,632 | 1,557,557 | 276,571 | 2,331,760 |
| Charge for the year | 540,305 | 755,656 | 28,172 | 1,324,133 | 602,322 | 13,100 | 7,637 | 623,059 |
| Provisions against actuarial gains within equity | - | - | 27,779 | 27,779 | - | - | - | - |
| Release of provisions | - | | | | (49,399) | (1,178,087) | - | (1,227,486) |
| Reversal of provisions | (445,528) | - | (30,921) | (476,449) | (576,908) | (381,670) | (3,623) | (962,201) |
| **Balance at December 31** | 568,424 | 766,556 | 305,615 | 1,640,595 | 473,647 | 10,900 | 280,585 | 765,132 |

a) Comment on movements on provisions for litigations:

Based on the Belgrade Supreme Appellate Court ruling, in 2014 the Bank had a refund of the amount of RSD 755,656 thousand, which was transferred from the Bank's account for enforced collection in the previous year, in respect of the lawsuit involving the Bank and Ineks Intereksport a.d., Beograd (in bankruptcy). This ruling annulled the previous adjudication of the Commercial Court of Belgrade from 2013 and the case was referred to the first instance court for redeliberation. The Court ruled in favor of the Bank, i.e. the amount claimed shall belong to the Bank until the revised litigation is finalized. The Bank provided for this amount in full.

The Court accepted the Bank's request that the case be split into two separate cases given that the Republic of Serbia filed a lawsuit against the Bank on the same grounds. The total RSD amount of provisions of RSD 755,656 thousand relates to the following lawsuits:

- Lawsuit filed by the Republic of Serbia with the claim amount of USD 4,773 thousand and
- Lawsuit filed by Intereksport a.d., Beograd (in bankruptcy) with the claim amount of USD 1,948 thousand.

b) The main actuarial assumptions used in calculation of retirement benefits were as follows:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Discount rate | 8.75% | 11.25% |
| Salary growth rate within the Bank | 2.5% | 4% |
| Employee turnover | 5% | 5% |

The discount rate equaled the previous years' key policy rate of the National Bank of Serbia as of December 31, 2014.

## 37. OTHER LIABILITIES

Other liabilities include:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Accounts payable | 198,960 | 253,193 |
| Liabilities to employees (salaries, payroll taxes and contributions and other liabilities to employees) | 272,955 | 54,339 |
| Advances received | 32,414 | 35,964 |
| Accrued interest, fees and commissions | 202,557 | 217,929 |
| Accrued liabilities and other accruals | 239,443 | 662,493 |
| Liabilities in settlement | 1,756,755 | 2,755,271 |
| Dividend payment liabilities | 277,367 | 150,124 |
| Taxes and contributions payable | 61,783 | 21,616 |
| Other liabilities | 146,875 | 107,644 |
| **Balance as at December 31** | 3,189,109 | 4,258,573 |

Liabilities in settlement totaling RSD 1,756,755 thousand mostly, in the amount of RSD 727,100 thousand and RSD 699,100 thousand, refer to the liabilities for sale and purchase of foreign currencies in the foreign exchange market and foreign currency liabilities for spot transactions, respectively.

Dividend payment liabilities refer to the liabilities to pay out preferred and convertible share dividend in the amount of RSD 123,900 thousand and liabilities for taxes relating to employees in the amount of RSD 153,468 thousand.

## 38. EQUITY

38.1 Equity is comprised of:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Issued capital | 17,191,466 | 17,191,466 |
| Share premium | 22,843,084 | 22,843,084 |
| Reserves from profit and other reserves | 20,635,440 | 16,635,440 |
| Revaluation reserves | 2,120,959 | 1,604,257 |
| Retained earnings | 6,755,855 | 6,687,971 |
| Balance as at December 31 | 69,546,804 | 64,962,218 |

The Bank's issued (share) capital was established through initial shareholder contributions and the ensuing issues of new shares. Shareholders have the right to manage the Bank as well as to shares in profit distribution. As of December 31, 2014 the Bank's share capital totaled RSD 17,191,466 thousand and comprised 17,191,466 shares with the individual par value of RSD 1 thousand.

Breakdown of the Bank's shares is provided in the table below:

| | Share Count | |
|---|---|---|
| **Share Type** | **December 31, 2014** | **December 31, 2013** |
| Ordinary shares | 16,817,956 | 8,709,310 |
| Preferred convertible shares | - | 8,108,646 |
| Preferred shares | 373,510 | 373,510 |
| Balance as at December 31 | 17,191,466 | 17,191,466 |

Pursuant to the Decision of the Bank' Shareholder Assembly on the 27th Issue of Ordinary Shares through Public Offering without Publishing Prospectus for conversion of preferred shares into ordinary shares, on November 24, 2014, the Bank converted 8,108,646 convertible preferred shares into voting shares. The aforesaid conversion affected the ordinary shares ownership percentages.

## 38. EQUITY (Continued)

The largest portions of the Bank's voting shares are held by the Republic of Serbia (41.74% of ordinary shares) and EBRD, London (24.43% of ordinary shares).

The structure of the Bank's shareholders with ordinary (common stock) shares at December 31, 2014 was as follows:

| Shareholder | Share Count | % Interest |
|---|---|---|
| Republic of Serbia | 7,020,346 | 41.74 |
| EBRD, London | 4,109,440 | 24.43 |
| IFC Capitalization Fund LP | 1,706,810 | 10.15 |
| DEG Deutche Investitions | 772,850 | 4.60 |
| Swedfund International Aktiebo | 386,420 | 2.30 |
| Jugobanka a.d., Beograd in bankruptcy | 321,600 | 1.91 |
| Invej d.o.o., Beograd | 230,000 | 1.37 |
| East Capital (lux)-Balkan Fund | 208,106 | 1.24 |
| Evropa osiguranje a.d., Beograd in bankruptcy | 197,420 | 1.17 |
| Kompanija Dunav osiguranje a.d., Beograd | 171,380 | 1.02 |
| UniCredit bank, a.d., Srbija | 150,187 | 0.89 |
| East Capital(LUX) Eastern Europe | 125,408 | 0.75 |
| UniCredit bank, a.d., Srbija (*custody* account) | 125,205 | 0.74 |
| Stankom co. d.o.o., Beograd | 117,535 | 0.70 |
| Erste bank a.d., Novi Sad | 85,700 | 0.51 |
| Others (1,084 shareholders) | 1,089,549 | 6.48 |
| | 16,817,956 | 100.00 |

The structure of the Bank's shareholders with preferred shares at December 31, 2014 was as follows:

| Shareholder | Share Count | % Interest |
|---|---|---|
| Jugobanka a.d., Beograd in bankruptcy | 18,090 | 4.84 |
| Others (629 shareholders) | 355,420 | 95.16 |
| | 373,510 | 100.00 |

Revaluation reserves totaling RSD 2,120,959 thousand (2013: RSD 1,604,257 thousand) relate to the effects of increase in the value of property based on the independent appraisal amounting to RSD 1,032,462 thousand, net gains on the value adjustment of securities available for sale amounting to RSD 979,977 thousand and actuarial gains of RSD 108,520 thousand.

In 2014 prior years' dividends on preferred shares were paid in the amount of RSD 485,172 thousand (2013: RSD 40,342 thousand).

Within the line items of retained earnings and revaluation reserves adjustments were made to the actuarial gain amount based on the changes to the actuarial assumptions used in the previous period and applied in the current year amounting to RSD 132,132 thousand.

The basic earnings per share totaled RSD 253 or 25.25 % of a common share par value in 2014, whereas in 2013 the basic earnings per share amounted to RSD 468 or 46.75 % of a common share par value. Decrease in the earnings per share percentage in 2014 as compared to 2013 was due to the increase in the number of commons stock (ordinary) shares through conversion of preferred into ordinary shares.

| | 2014 | 2013 |
|---|---|---|
| Profit for the year less preferred share dividend | 4,246,824 | 4,071,705 |
| Weighted average number of shares outstanding | 16,817,956 | 8,709,310 |
| Basic earnings per share (in RSD) | 253 | 468 |

## 38. EQUITY (Continued)

Diluted earnings per share totaled RSD 253 or 25.25% of a common share par value in 2014, whereas in 2013 the diluted earnings per share amounted to RSD 242 or 24.21% of a common share par value.

| | 2014 | 2013 |
|---|---|---|
| Profit for the year less preferred share dividend | 4,246,824 | 4,071,705 |
| Weighted average number of shares outstanding | 16,817,956 | 16,817,956 |
| Diluted earnings per share (in RSD) | 253 | 242 |

38.2 Tax effects related to the other comprehensive income for the year:

| | 2014 | | | 2013 | | |
|---|---|---|---|---|---|---|
| | Gross | Tax | Net | Gross | Tax | Net |
| Increase due to fair value adjustments of equity investments and securities available for sale | 695,067 | (213,650) | 481,417 | 169,859 | - | 169,859 |
| Net decease due to actuarial losses | (27,779) | 4,167 | (23,612) | - | - | - |
| Valuation of property | (3,472) | 634 | (2,838) | 686,680 | (103,002) | 583,678 |
| Decrease due to fair value adjustments of equity investments and securities available for sale | (83,726) | 40,611 | (43,115) | - | - | - |
| Total | 580,090 | (168,238) | 411,852 | 856,539 | (103,002) | 753,537 |

## 39. CONTINGENT LIABILITIES AND OTHER OFF-BALANCE SHEET ITEMS

39.1 The Bank issues guarantees and letters of credit to vouch to third parties for the liability settlement by its clients. Such contracts have defined validity terms, which most commonly last up to a year. The contractual values of contingent liabilities are presented in the table below:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Payment guarantees (Note 4.1.1.) | 4,767,131 | 7,357,476 |
| Performance guarantees (Note 4.1.1.) | 7,883,510 | 5,787,610 |
| Letters of credit | 27,709 | 45,808 |
| Acceptances of bills of exchange | 27,185 | 37,737 |
| **Balance as at December 31** | 12,705,535 | 13,228,631 |

The above listed amounts represent the maximum amount of loss that the Bank would incur as at reporting date in the event that none of the Bank's clients were able to settle their contractual obligations (Note 4).

**39. CONTINGENT LIABILITIES AND OTHER OFF-BALANCE SHEET ITEMS (Continued)**

39.2 The breakdown of commitments is provided below:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Unused portion of approved payment and credit card loan facilities and overdrafts | 9,235,730 | 9,200,577 |
| Irrevocable commitments for undrawn loans | 7,311,860 | 7,640,316 |
| Other irrevocable commitments | 270,207 | 78,380 |
| Other commitments per contracted value of securities | 3,243,647 | 681,463 |
| **Balance as at December 31** | 20,061,444 | 17,600,736 |

39.3 Litigation

Based on the expert estimate made by the Bank's Legal Department and attorneys at law representing the Bank, the Bank made provisions for potential litigation losses for all the legal suits filed against the bank in 2014 in the total amount of RSD 766,556 thousand (Note 36).

As of December 31, 2014 contingent liabilities based on legal suits filed against the Bank amounted to RSD 2,894,016 thousand (for 244 cases). The Bank's management anticipates no materially significant losses thereof in the forthcoming period.

In addition, the Bank is involved in legal suits against third parties where the most significant portion of the total claims amounted to RSD 27,323,175 thousand (for 552 cases with the largest individual claim amounts). The Bank's management anticipates favorable outcome of the most lawsuits.

39.4 Commitments for operating lease liabilities are provided below:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Commitments due within one year | 450,325 | 455,767 |
| Commitments due in the period from 1 to 5 years | 1,190,071 | 1,300,046 |
| Commitments due in the period longer than 5 years | 230,741 | 100,511 |
| Total | 1,871,137 | 1,856,324 |

39.5 Other off-balance sheet items comprise managed funds and other off-balance sheet assets.

Funds managed on behalf and for the account of third parties are mostly comprised of assets for consignment loans of the Republic of Serbia, the largest portion of which, in the amount of RSD 3,716,372 thousand, relates to the long-term housing loans extended to retail customers. Other managed funds mostly refer to loans approved for agriculture and assets received from foreign grantors for micro loans.

Within other off-balance sheet assets, the Bank, among other things, records custody operations performed for the account of its clients, repo investments in Treasury bills and old FX savings bonds. As per its operating license to perform custody operations, the Bank maintains the financial instruments of its clients on the security accounts, recorded off balance. The Bank takes no credit risk in respect of managed funds.

Moreover, in accordance with the newly enacted regulations, other off-balance sheet assets include the value of the tangible assets received as collaterals securitizing loan repayment: residential and commercial real estate properties and other collaterals – pledge liens.

## 40. RELATED PARTY DISCLOSURES

40.1 The largest portions of the Bank's voting shares are held by the Republic of Serbia (41.74% of ordinary shares) and EBRD, London (24.43% of ordinary shares). The Bank has 3 subsidiaries: Komercijalna banka a.d., Budva, Komercijalna banka a.d., Banja Luka and KomBank Invest a.d., Beograd.

In the normal course of business, a number of banking transactions are performed with subsidiaries. these include loans, deposits, investments in equity securities and derivative instruments.

Related party transactions with subsidiaries were performed at arm's length.

### A . Balance as at December 31, 2014

**RECEIVABLES**

| Subsidiaries | Loans and Receivables | Interest and Fees | Other Assets | Net Balance Exposure | Off-Balance Sheet Items | Total |
|---|---|---|---|---|---|---|
| Komercijalna banka a.d., Budva | 6,442 | 862 | - | 7,304 | - | 7,304 |
| Komercijalna banka a.d., Banja Luka | 604,792 | - | 3,443 | 608,235 | - | 608,235 |
| KomBank INVEST a.d., Beograd | - | 1 | 3 | 4 | 197 | 201 |
| **Total:** | 611,234 | 863 | 3,446 | 615,543 | 197 | 615,740 |

**LIABILITIES**

| Subsidiaries | Deposits and Loans | Interest and Fees | Other Liabilities | Total |
|---|---|---|---|---|
| Komercijalna banka a.d., Budva | 117,835 | - | 1,689 | 119,524 |
| Komercijalna banka a.d., Banja Luka | 10,831 | - | - | 10,831 |
| KomBank INVEST a.d., Beograd | 9,757 | 3 | - | 9,760 |
| **Total:** | 138,423 | 3 | 1,689 | 140,115 |

**INCOME AND EXPENSES**

| Subsidiaries | Interest Income | Fee and Commission Income | Dividend Income | Interest Expenses | Fee and Commission Expense | Net Income/ Expenses |
|---|---|---|---|---|---|---|
| Komercijalna banka a.d., Budva | 12,674 | 2,122 | 120,689 | - | (1,317) | 134,168 |
| Komercijalna banka a.d., Banja Luka | 10,058 | 1,289 | - | - | (1,252) | 10,095 |
| KomBank INVEST a.d., Beograd | - | 56 | - | (25) | - | 31 |
| **Total:** | 22,732 | 3,467 | 120,689 | (25) | (2,569) | 144,294 |

Komercijalna banka a.d., Beograd realized net foreign exchange gains in the amount of RSD 202 thousand (2013: net foreign exchange losses of RSD 1,189 thousand) from related party transactions.

## 40. RELATED PARTY DISCLOSURES (Continued)

### B . Balance as at December 31, 2013

RECEIVABLES

| Subsidiaries | Loans and Receivables | Interest and Fees | Other Assets | Net Balance Exposure | Off-Balance Sheet Items | Total |
|---|---|---|---|---|---|---|
| Komercijalna banka a.d., Budva | 430,157 | 825 | 4,253 | 435,235 | - | 435,235 |
| Komercijalna banka a.d., Banja Luka | 232,271 | - | 2,646 | 234,917 | 343,926 | 578,843 |
| KomBank INVEST a.d., Beograd | - | 1 | - | 1 | 200 | 201 |
| **Total:** | 662,428 | 826 | 6,899 | 670,153 | 344,126 | 1,014,279 |

LIABILITIES

| Subsidiaries | Deposits and Loans | Interest and Fees | Other Liabilities | Total |
|---|---|---|---|---|
| Komercijalna banka a.d., Budva | 147,914 | - | 1,601 | 149,515 |
| Komercijalna banka a.d., Banja Luka | 9,228 | - | - | 9,228 |
| KomBank INVEST a.d., Beograd | 12,940 | 13 | - | 12,953 |
| **Total:** | 170,082 | 13 | 1,601 | 171,696 |

INCOME AND EXPENSES

| Subsidiaries | Interest Income | Fee and Commission Income | Dividend Income | Interest Expenses | Fee and Commission Expense | Net Income/ Expenses |
|---|---|---|---|---|---|---|
| Komercijalna banka a.d., Budva | 4,414 | 1,548 | 387,597 | - | (831) | 392,728 |
| Komercijalna banka a.d., Banja Luka | 2,639 | 628 | - | (390) | (293) | 2,584 |
| KomBank INVEST a.d., Beograd | - | 47 | - | (948) | - | (901) |
| **Total:** | 7,053 | 2,223 | 387,597 | (1,338) | (1,124) | 394,411 |

Komercijalna banka a.d., Beograd incurred net foreign exchange losses in the amount of RSD 1,189 thousand in 2013 (2012: RSD 4,662 thousand) from related party transactions.

40.2 Gross and net remunerations paid to the members of the Bank's Executive Board, Board of Directors and Audit Committee were as follows:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| **Gross remunerations** | | |
| Executive Board | 78,485 | 83,788 |
| **Net remunerations** | | |
| Executive Board | 67,031 | 71,179 |
| **Gross remunerations** | | |
| Board of Directors and Audit Committee | 30,540 | 26,845 |
| **Net remunerations** | | |
| Board of Directors and Audit Committee | 19,344 | 17,276 |

The Bank approved loans to the members of the Bank's Executive Board, Board of Directors and Audit Committee in the total amount of RSD 112,637 thousand (2013: RSD 119,725 thousand).

## 41. EVENTS AFTER THE REPORTING PERIOD

At its session held on January 26, 2015 the Bank's Shareholder Assembly enacted Decision on Adopting the Strategy and Business Plan for 2015 – 2017 Period.

In accordance with the Decision on Measures for Preservation of Financial System Stability in relation to loans indexed to foreign currency (the "Decision") issued by the National Bank of Serbia on February 24, 2015, the Bank assessed and calculated potential effects in respect of loans indexed to CHF. According to the aforesaid calculation, the Bank assessed that potential adverse effects, i.e., losses, in this respect will total up to RSD 110 million.

### Unreconciled Outstanding Item Statements

Based on the analysis of the regular annual asset/liability count performed as of December 31, 2014, the Bank had unreconciled outstanding item statements totaling RSD 11,007 thousand. Statements unreconciled with 40 customers mostly relate to the clients contesting the amount or the manner of calculation of interest and fees, those with accounts blocked or those contesting the amounts outstanding as per their respective reorganization plans.

### Unrealized Dividends

Unrealized dividends payable in 2015 amount to:

- RSD 538,753 thousand for 2014 (6.29 % of the nominal value of preferred shares).
- RSD 123,900 thousand for 2013 (9.91% of the nominal value of preferred shares).

## 42. EXCHANGE RATES

The official exchange rates for major currencies as determined in the interbank foreign exchange market and used in the translation of balance sheet components denominated in foreign currencies into dinars (RSD) as of December 31, 2014 and 2013 were as follows:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| USD | 99.4641 | 83.1282 |
| EUR | 120.9583 | 114.6421 |
| CHF | 100.5472 | 93.5472 |

## *2. AUDIT REPORT (as a whole)*

**KOMERCIJALNA BANKA A.D., BEOGRAD**

**Financial Statements**
**Year Ended December 31, 2014**
**and Independent Auditors' Report**

***Translation of the Auditors' Report issued in the Serbian language***

**CONTENTS**

# Deloitte.

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***Translation of the Auditors' Report issued in the Serbian language***

**INDEPENDENT AUDITORS' REPORT**

**To the Board of Directors and Owners of Komercijalna banka A.D., Beograd**

We have audited the accompanying financial statements of Komercijalna banka A.D., Beograd (hereinafter: the "Bank"), enclosed on pages 2 to 93, which comprise the balance sheet as of December 31, 2014 and the related income statement, statement of other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

*Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the International Financial Reporting Standards as per the Law on Accounting of the Republic of Serbia and regulations of the National Bank of Serbia governing financial reporting of banks, as well as for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

*Auditors' Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing and the Law on Audit of the Republic of Serbia. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Bank's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

*Opinion*

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Bank as at December 31, 2014, and its financial performance and cash flows for the year then ended in accordance with the International Financial Reporting Standards as per the Law on Accounting of the Republic of Serbia and regulations of the National Bank of Serbia governing financial reporting of banks.

Belgrade, February 27, 2015

Deloitte d.o.o. BEOGRAD IV

Miroslav Tončić
Certified Auditor

**BALANCE SHEET**
**As of December 31, 2014**
**(Thousands of RSD)**

| | Note | 2014 | 2013 | 2012 |
|---|---|---|---|---|
| **ASSETS** | | | | |
| Cash and cash funds held with the central bank | 19 | 68,547,389 | 70,934,839 | 65,480,687 |
| Financial assets at fair value through profit and loss, held for trading | 20 | 121,634 | 115,319 | 212,690 |
| Financial assets available for sale | 21 | 95,481,249 | 56,885,285 | 41,085,776 |
| Financial assets held to maturity | 22 | 51,442 | 149,900 | 349,807 |
| Loans and receivables due from banks and other financial institutions | 23 | 34,737,605 | 35,247,935 | 22,566,291 |
| Loans and receivables due from customers | 24 | 185,377,035 | 177,560,058 | 176,904,911 |
| Investments in subsidiaries | 25 | 5,480,888 | 5,480,888 | 5,480,888 |
| Intangible assets | 26 | 405,774 | 537,445 | 600,438 |
| Property, plant and equipment | 27 | 6,329,077 | 6,577,670 | 5,690,613 |
| Investment property | 28 | 2,581,144 | 1,808,554 | 1,726,233 |
| Current tax assets | 29 | 73,835 | 712,700 | 12,784 |
| Deferred tax assets | 30 | - | - | 4,896 |
| Non-current assets held for sale and assets from discontinued operations | 31 | 84,227 | 71,630 | 78,763 |
| Other assets | 32 | 6,990,225 | 6,704,096 | 3,190,132 |
| **Total assets** | | 406,261,524 | 362,786,319 | 323,384,909 |
| **LIABILITIES AND EQUITY** | | | | |
| Deposits and other liabilities due to banks, other financial institutions and the central bank | 33 | 23,743,018 | 21,058,542 | 13,343,870 |
| Deposits and other liabilities due to customers | 34 | 301,954,911 | 266,020,289 | 240,055,122 |
| Subordinated liabilities | 35 | 6,036,680 | 5,711,409 | 5,654,932 |
| Provisions | 36 | 1,640,595 | 765,132 | 2,331,760 |
| Deferred tax liabilities | 18.3; 30.2 | 150,407 | 10,156 | - |
| Other liabilities | 37 | 3,189,109 | 4,258,573 | 2,132,665 |
| **Total liabilities** | | 336,714,720 | 297,824,101 | 263,518,349 |
| Equity | 38 | | | |
| Issued capital and share premium | | 40,034,550 | 40,034,550 | 40,034,550 |
| Retained earnings | | 6,755,855 | 6,687,971 | 4,185,812 |
| Reserves | | 22,756,399 | 18,239,697 | 15,646,198 |
| **Total equity attributable to the owners of the Bank** | | 69,546,804 | 64,962,218 | 59,866,560 |
| **Total liabilities and equity** | | 406,261,524 | 362,786,319 | 323,384,909 |

Notes on the following pages
form an integral part of these financial statements.

These financial statements were approved by the Executive Board of Komercijalna banka a.d., Beograd on February 27, 2015.

Signed on behalf of Komercijalna banka a.d., Beograd by:

Snežana Pejčić
Head of Accounting

Ivica Smolić
Executive Board Chairman

**INCOME STATEMENT**
**Year Ended December 31, 2014**
**(Thousands of RSD)**

| | Note | 2014 | 2013 |
|---|---|---|---|
| Interest income | 8 | 21,224,379 | 22,023,774 |
| Interest expenses | 8 | (7,925,793) | (9,094,536) |
| **Net interest income** | | 13,298,586 | 12,929,238 |
| Fee and commission income | 9 | 5,677,040 | 5,493,211 |
| Fee and commission expenses | 9 | (959,283) | (928,063) |
| **Net fee and commission income** | | 4,717,757 | 4,565,148 |
| Net gains on the financial assets held for trading | 10 | 6,076 | 22,342 |
| Net gains on the financial assets available for sale | 11 | 51,282 | 1,738 |
| Net foreign exchange losses and negative currency clause effects | 12 | (205,943) | (48,733) |
| Other operating income | 13 | 569,191 | 1,123,546 |
| Net losses from impairment of financial assets and credit risk-weighted off-balance sheet assets | 14 | (2,725,389) | (3,220,075) |
| **Total operating income** | | 15,711,560 | 15,373,204 |
| Staff costs | 15 | (4,211,489) | (4,262,123) |
| Depreciation and amortization charge | 16 | (844,632) | (792,648) |
| Other expenses | 17 | (5,897,850) | (5,730,058) |
| **Profit before taxes** | | 4,757,589 | 4,588,375 |
| Gains on created deferred tax assets and decrease in deferred tax liabilities | 18.1 | 47,547 | 87,950 |
| Losses decrease in deferred tax assets and created deferred tax liabilities | 18.1 | (19,559) | - |
| **Profit for the year** | | 4,785,577 | 4,676,325 |
| Earnings per share | | | |
| Basic earnings per share | | 0.253 | 0.468 |
| Diluted earnings per share | | 0.253 | 0.242 |

Notes on the following pages
form an integral part of these financial statements.

Signed on behalf of Komercijalna banka a.d., Beograd by:

Snežana Pejčić
Head of Accounting

Ivica Smolić
Executive Board Chairman

**STATEMENT OF OTHER COMPREHENSIVE INCOME**
**Year Ended December 31, 2014**
**(Thousands of RSD)**

| | Note | 2014 | 2013 |
|---|---|---|---|
| **Profit for the year** | | 4,785,577 | 4,676,325 |
| *Other comprehensive income* | | | |
| Increase/(decrease) in revaluation reserves in respect of intangible assets, property, plant and equipment | 38.2 | (3,472) | 686,680 |
| Actuarial losses | 36; 38.2 | (27,779) | - |
| Net increase from the fair value adjustment of equity investments and securities available for sale | 38.2 | 611,341 | 169,859 |
| Losses from taxes related to the other comprehensive income | 38.2 | (168,238) | (103,002) |
| Other comprehensive income for the year, net of taxes | | 411,852 | 753,537 |
| Total comprehensive income for the year | | 5,197,429 | 5,429,862 |

Notes on the following pages
form an integral part of these financial statements.

Signed on behalf of Komercijalna banka a.d., Beograd by:

Snežana Pejčić
Head of Accounting

Ivica Smolić
Executive Board Chairman

**STATEMENT OF CHANGES IN EQUITY**
**Year Ended December 31, 2014**
**(Thousands of RSD)**

| | Issued Capital | Share Premium | Revaluation Reserves | Reserves from Profit and Other Reserves | Retained Earnings/ Accumulated Losses | Total |
|---|---|---|---|---|---|---|
| Balance at January 1, 2013 | 17,191,466 | 22,843,084 | 860,758 | 14,785,440 | 4,185,812 | 59,866,560 |
| **Total comprehensive income for the year** | | | | | | |
| Profit for the year | - | - | - | - | 4,676,325 | 4,676,325 |
| Transfer of 2012 retained earnings portion to legal reserves | - | - | - | 1,850,000 | (1,850,000) | - |
| | - | - | - | 1,850,000 | 2,826,325 | 4,676,325 |
| **Other comprehensive income for the year, net of income tax** | | | | | | |
| Change in the value of properties as per revaluation performed by an independent appraiser | - | - | 686,680 | - | - | 686,680 |
| Gains on realized reserves (depreciation effects) | - | - | (10,038) | - | 10,038 | - |
| Net increase based on the change in the fair value of equity investments and securities available-for-sale | - | - | 169,859 | - | - | 169,859 |
| Effect of increase in deferred tax liabilities in respect of securities available for sale and equity investments | - | - | (103,002) | - | - | (103,002) |
| Effect of deferred tax liabilities in respect of increase in property and equipment due to revaluation | - | - | 743,499 | - | 10,038 | 753,537 |
| Other comprehensive income for the year, net of tax | - | - | 743,499 | 1,850,000 | 2,836,363 | 5,429,862 |
| **Transactions with equity holders, recognized directly in equity** | | | | | | |
| **Payments from and to equity holders** | | | | | | |
| Payment of dividends for preferred shares | - | - | - | - | (37,351) | (37,351) |
| Employee share in profit | - | - | - | - | (296,853) | (296,853) |
| **Balance at December 31, 2013** | 17,191,466 | 22,843,084 | 1,604,257 | 16,635,440 | 6,687,971 | 64,962,218 |

Notes on the following pages
form an integral part of these financial statements.

**STATEMENT OF CHANGES IN EQUITY (Continued)**
**Year Ended December 31, 2014**
**(Thousands of RSD)**

| | Issued Capital | Share Premium | Revaluation Reserves | Reserves from Profit and Other Reserves | Retained Earnings/ Accumulated Losses | Total |
|---|---|---|---|---|---|---|
| Balance at January 1, 2014 | 17,191,466 | 22,843,084 | 1,604,257 | 16,635,440 | 6,687,971 | 64,962,218 |
| **Total comprehensive income for the year** | | | | | | |
| Profit for the year | - | - | - | - | 4,785,577 | 4,785,577 |
| Transfer of 2013 retained earnings portion to legal reserves | - | - | - | 4,000,000 | (4,000,000) | - |
| | - | - | - | 4,000,000 | 785,577 | 4,785,577 |
| **Other comprehensive income for the year, net of income tax** | | | | | | |
| Decrease in revaluation reserves from property, plant and equipment | - | - | (3,472) | - | - | (3,472) |
| Gains from the realized reserves (depreciation/amortization effect) | - | - | (27,283) | - | 27,283 | - |
| Net increase based on the change in the fair value of equity investments and securities available-for-sale | - | - | 611,341 | - | - | 611,341 |
| Actuarial losses (Note 36) | - | - | (27,779) | - | - | (27,779) |
| Tax effects of other comprehensive income | - | - | (168,238) | - | - | (168,238) |
| Other comprehensive income for the year, net of tax | - | - | 384,569 | - | 27,283 | 411,852 |
| Total comprehensive income for the year | - | - | 384,569 | 4,000,000 | 812,860 | 5,197,429 |
| **Transactions with equity holders, recognized directly in equity** | | | | | | |
| **Payments from and to equity holders** | | | | | | |
| Payment of dividends for preferred shares | - | - | - | - | (604,620) | (604,620) |
| Employee share in profit | - | - | - | - | (7,775) | (7,775) |
| | - | - | - | - | (612,395) | (612,395) |
| **Other** | | | | | | |
| Actuarial gains from prior years (Note 38) | - | - | 132,132 | - | (132,132) | - |
| Other | - | - | 1 | - | (449) | (448) |
| | | | 132,133 | - | (132,581) | (448) |
| **Balance at December 31, 2014** | 17,191,466 | 22,843,084 | 2,120,959 | 20,635,440 | 6,755,855 | 69,546,804 |

Notes on the following pages
form an integral part of these financial statements.

Signed on behalf of Komercijalna banka a.d., Beograd by:

Snežana Pejčić
Head of Accounting

Ivica Smolić
Executive Board Chairman

## STATEMENT OF CASH FLOWS
**Year Ended December 31, 2014**
**(Thousands of RSD)**

| | 2014 | 2013 |
|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | |
| **Cash generated by operating activities** | **26,173,313** | **26,515,177** |
| Interest receipts | 20,196,420 | 20,455,890 |
| Fee and commission receipts | 5,661,699 | 5,493,457 |
| Receipts of other operating income | 204,599 | 209,753 |
| Dividend receipts and profit sharing | 110,595 | 356,077 |
| **Cash used in operating activities** | **(19,051,974)** | **(19,690,614)** |
| Interest payments | (8,072,315) | (8,948,540) |
| Fee and commission payments | (960,358) | (929,932) |
| Payments to, and on behalf of employees | (4,003,672) | (4,318,918) |
| Taxes, contributions and other duties paid | (798,934) | (927,771) |
| Payments for other operating expenses | (5,216,695) | (4,565,453) |
| **Net cash inflows from operating activities prior to changes in loans and deposits** | **7,121,339** | **6,824,563** |
| **Decrease in loans and increase in deposits received and other liabilities** | **32,605,699** | **23,508,143** |
| Decrease in loans and receivables due from banks, other financial institutions, the central bank and customers | 5,760,091 | - |
| Decrease in financial assets initially recognized at fair value through profit and loss, held for trading | - | 1,850,488 |
| Increase in deposits and other liabilities due to banks, other financial institutions, the central bank and customers | 26,845,608 | 21,657,655 |
| **Increase in loans and decrease in deposits received and other liabilities** | **(4,633,940)** | **(24,137,331)** |
| Increase in loans and receivables due from banks, other financial institutions, the central bank and customers | - | (24,137,331) |
| Increase in financial assets initially recognized at fair value through profit and loss, financial assets held for trading and other securities not held for investments | (4,633,940) | - |
| **Net cash generated by operating activities before income taxes** | **35,093,098** | **6,195,375** |
| Income taxes paid | - | (699,916) |
| Dividends paid | (485,151) | (269,195) |
| **Net cash generated by operating activities** | **34,607,947** | **5,226,264** |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | |
| **Cash generated by investing activities** | **18,126,491** | **14,283,199** |
| Proceeds from investment securities | 18,117,937 | 14,271,063 |
| Proceeds from the sales of intangible assets, property, plant and equipment | 8,554 | 12,136 |
| **Cash used in investing activities** | **(49,181,554)** | **(32,336,193)** |
| Cash used for investment securities | (48,706,989) | (31,584,013) |
| Cash used for investments in subsidiaries and associates and joint ventures | - | (976) |
| Cash used for the purchases of intangible assets, property, plant and equipment | (474,565) | (751,204) |
| **Net cash used in investing activities** | **(31,055,063)** | **(18,052,994)** |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | |
| **Cash generated by financing activities** | **208,836,248** | **219,234,820** |
| Inflows from the borrowings | 208,836,248 | 219,234,820 |
| **Cash used in financing activities** | **(208,645,771)** | **(206,115,732)** |
| Cash used in the repayment of borrowings | (208,645,771) | (206,115,732) |
| **Net cash generated by financing activities** | **190,477** | **13,119,088** |
| **TOTAL CASH INFLOWS** | 285,741,751 | 283,541,339 |
| **TOTAL CASH OUTFLOWS** | (281,998,390) | (283,248,981) |
| **NET CASH INCREASE** | **3,743,361** | **292,358** |
| **CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR** | **40,297,749** | **39,900,993** |
| **FOREIGN EXCHANGE GAINS** | 1,201,216 | 936,537 |
| **FOREIGN EXCHANGE LOSSES** | (82,149) | (832,139) |
| **CASH AND CASH EQUIVALENTS, END OF YEAR** | **45,160,177** | **40,297,749** |

Notes on the following pages
form an integral part of these financial statements.

Signed on behalf of Komercijalna banka a.d., Beograd by:

Snežana Pejčić
Head of Accounting

Ivica Smolić
Executive Board Chairman

**NOTES TO THE FINANCIAL STATEMENTS**
**December 31, 2014**
*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 1. BANK'S ESTABLISHMENT AND ACTIVITY

Komercijalna banka a.d., Beograd (hereinafter the "Bank"), was established as at December 1, 1970 and transformed into a shareholding company as of May 6, 1992. The Bank was registered with the Commercial Court in Belgrade on July 10, 1991 and later registered with the Serbian Business Registers Agency on April, 14 2006. The Bank was issued its operating license by the National Bank of Yugoslavia on July 3, 1991.

The principal holders of voting shares in the Bank are as follows:

| | |
|---|---|
| Republic of Serbia | 41.74% |
| EBRD, London | 24.43% |

The Bank is registered for performing crediting, depositary and guarantee operations, as well as for payment transfer operations in the country and abroad.

As of December 31, 2014, the Bank was comprised of the Head Office in Belgrade at the address of no. 14, Svetog Save St., 24 branches and 220 sub-branches in the territory of the Republic of Serbia (December 31, 2013: 24 branches and 233 sub-branches in the territory of the Republic of Serbia).

As of December 31, 2014, the Bank had 2,906 employees (December 31, 2013: 2,966 employees). The Bank's tax identification number is 100001931.

## 2. BASIS OF PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS

### 2.1. Basis of Preparation and Presentation of Financial Statements

Legal entities and entrepreneurs incorporated in Serbia are required to maintain their books of account, to recognize and value assets and liabilities, income and expenses, and to present, submit and disclose financial statements in conformity the Law on Accounting (hereinafter referred as: the "Law", Official Gazette of the Republic of Serbia no. 63/2013). As a large legal entity, the Bank is required to apply International Financial Reporting Standards ("IFRS"), which as per the aforementioned law comprise the following: the Framework for the Preparation and Presentation of Financial Statements (the "Framework"), International Accounting Standards ("IAS"), International Financial Reporting Standards ("IFRS"), as well as the related interpretations issued by the International Financial Reporting Interpretations Committee ("IFRIC") and additional related interpretations issued by International Accounting Standards Board ("IASB"), the translations of which to the Serbian language were approved and issued by the competent Ministry of Finance and which were in effect as at December 31, 2013.

The amendments to IAS, as well as the newly issued IFRS and the related interpretations issued by the IASB and the IFRIC, in the period between December 31, 2002 and January 1, 2009, were officially adopted pursuant to a Decision enacted by the Ministry of Finance of the Republic of Serbia (the "Ministry") on October 5, 2010 and published the Official Gazette of the Republic of Serbia no. 77/2010. The Ministry's Decision dated March 13, 2014 adopted the translation of the Conceptual Framework for Financial Reporting and (the "Conceptual Framework," adopted by the IASB in September 2010, which supplants the Framework for Preparation and Presentation of the Financial Statements) and basic texts of IAS and IFRS ("Decision on Adoption of the Translations of the Conceptual Framework for Financial Reporting and Basic Texts of International Accounting Standards and International Financial Reporting Standards," published the Official Gazette of the Republic of Serbia no. 35 on March 27, 2014 ("Decision on Adoption of the Translations"), encompassing amendments to IAS and new IFRS and related interpretations issued by IASB and IFRIC/effective as of December 31, 2013. Based on this Decision on Adoption of the Translations, the Conceptual Framework, IAS, IFRS, IFRIC and related interpretations that have been translated shall be applied to the financial statements prepared as of December 31, 2014.

Standards and interpretations issued that came into effect in the current period pursuant to the Decision on Adoption of the Translations are disclosed in Note 2.2, while standards and interpretations in issue but not yet in effect are disclosed in Note 2.3.

## 2. BASIS OF PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS (Continued)

### 2.1. Basis of Preparation and Presentation of Financial Statements (Continued)

The accompanying financial statements are presented in the format prescribed under the Decision on the Forms and Contents of the Items in the Forms of the Financial Statements of Banks (Official Gazette of RS nos. 71/2014 and 135/2014).

These financial statements were prepared at historical cost principle unless otherwise stipulated in the accounting policies presented hereunder.

In the preparation of the accompanying financial statements, the Bank adhered to the accounting policies described in Note 3.

The Bank's financial statements are stated in thousands of dinars (RSD). Dinar is the official reporting currency in the Republic of Serbia.

### 2.2. Standards and Interpretations Issued that Came into Effect in the Current Period Pursuant to the Decision on Adoption of the Translations of the Ministry

- Amendments to IFRS 7 "Financial Instruments: Disclosures" – Amendments improving fair value and liquidity risk disclosures (revised in March 2009, effective for annual periods beginning on or after January 1, 2009);

- Amendments to IFRS 1 "First-Time Adoption of IFRS" – Additional Exemptions for First-Time Adopters. The amendments relate to assets in oil and gas industry and determining whether an arrangement contains a lease (revised in July 2009, effective for annual periods beginning on or after January 1, 2010);

- Amendments to various standards and interpretations resulting from the Annual Quality Improvement Project of IFRS published on April 16, 2009 (IFRS 5, IFRS 8, IAS 1, IAS 7, IAS 17, IAS 36, IAS 39, IFRIC 16) primarily with a view to removing inconsistencies and clarifying wording, (amendments are to be applied for annual periods beginning on or after 1 January 2010, while the amendment to IFRIC is to become effective as of July 1, 2009);

- Amendments to IAS 38 "Intangible Assets" (revised in July 2009, effective for annual periods beginning on or after July 1, 2009);

- Amendments to IFRS 2 "Share-Based Payment": Amendments resulting from the Annual Quality Improvement Project of IFRS (revised in April 2009, effective for annual periods beginning on or after July 1, 2009) and amendments relating to group cash-settled share-based payment transactions (revised in June 2009, effective for annual periods beginning on or after January 1, 2010);

- Amendments IFRIC 9 "Reassessment of Embedded Derivatives" effective for annual periods beginning on or after July 1, 2009 and IAS 39 "Financial Instruments: Recognition and Measurement" – Embedded Derivatives (effective for annual periods beginning on or after June 30, 2009);

- IFRIC 18 "Transfers of Assets from Customers" (effective for annual periods beginning on or after July 1, 2009);

- "Conceptual Framework for Financial Reporting 2010" being amendments to "Framework for the Preparation and Presentation of Financial Statements" (effective for transfer of assets from customers received on or after September 2010);

- Amendments to IFRS 1 "First-time Adoption of International Financial Reporting Standards" – Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters (effective for annual periods beginning on or after July 1, 2010);

## 2. BASIS OF PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS (Continued)

### 2.2. Standards and Interpretations Issued that Came into Effect in the Current Period Pursuant to the Decision on Adoption of the Translations of the Ministry (Continued)

- Amendments to IAS 24 "Related Party Disclosures" – Simplifying the disclosure requirements for government-related entities and clarifying the definition of a related party (effective for annual periods beginning on or after January 1, 2011);

- Amendments to IAS 32 "Financial Instruments: Presentation" – Accounting for Rights Issues (effective for annual periods beginning on or after February 1, 2010);

- Amendments to various standards and interpretations "Improvements to IFRSs (2010)" resulting from the Annual quality improvement project of IFRS published on May 6, 2010 (IFRS 1, IFRS 3, IFRS 7, IAS 1, IAS 27, IAS 34, IFRIC 13) primarily with a view to removing inconsistencies and clarifying wording, (most amendments are to be applied for annual periods beginning on or after January 1, 2011);

- Amendments to IFRIC 14 "IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and Their Interaction" – Prepayments of a Minimum Funding Requirement (effective for annual periods beginning on or after January 1, 2011);

- IFRIC 19 "Extinguishing Financial Liabilities with Equity Instruments" (effective for annual periods beginning on or after July 1, 2010).

- Amendments to IFRS 1 "First-Time Adoption of IFRS" – Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters (effective for annual periods beginning on or after July 1, 2011);

- Amendments to IFRS 7 "Financial Instruments: Disclosures" – Transfers of Financial Assets (effective for annual periods beginning on or after January 1, 2011);

- Amendments to IAS 12 "Income Taxes" – Deferred Tax: Recovery of Underlying Assets (effective for annual periods beginning on or after January 1, 2012);

- IFRS 10 "Consolidated Financial Statements" (effective for annual periods beginning on or after January 1, 2013);

- IFRS 11 "Joint Arrangements" (effective for annual periods beginning on or after January 1, 2013);

- IFRS 12 "Disclosures of Involvement with Other Entities" (effective for annual periods beginning on or after January 1, 2013);

- Amendments to IFRS 10, IFRS 11 and IFRS 12 "Consolidated Financial Statements, Joint Arrangements and Disclosures of Involvement with Other Entities: Transition Guidance" (effective for annual periods beginning on or after January 1, 2013);

- IAS 27 (revised in 2011) "Separate Financial Statements" (effective for annual periods beginning on or after January 1, 2013);

- IAS 28 (revised in 2011) "Investments in Associates and Joint Ventures" (effective for annual periods beginning on or after January 1, 2013);

- IFRS 13 "Fair Value Measurement" (effective for annual periods beginning on or after January 1, 2013);

- Amendments to IFRS 1 "First-time Adoption of International Financial Reporting Standards" – Government Loans with a Below-Market Rate of Interest (effective for annual periods beginning on or after January 1, 2013);

## 2. BASIS OF PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS (Continued)

### 2.2. Standards and Interpretations Issued that Came into Effect in the Current Period Pursuant to the Decision on Adoption of the Translations of the Ministry (Continued)

- Amendments to IFRS 7 "Financial Instruments: Disclosures" – Offsetting Financial Assets and Financial Liabilities (effective for annual periods beginning on or after January 1, 2013);
- Amendments to IAS 1 "Presentation of Financial Statements" – Presentation of Items of Other Comprehensive Income (effective for annual periods beginning on or after July 1, 2012);
- Amendments to IAS 19 "Employee Benefits" – Improvements to the Accounting for Post-Employment Benefits (effective for annual periods beginning on or after January 1, 2013);
- Amendments to various standards "Improvements to IFRSs (2009-2011 Cycle)" issued in May 2012, resulting from the annual improvement project of IFRS (IFRS 1, IAS 1, IAS 16, IAS 32, IAS 34) primarily with a view to removing inconsistencies and clarifying wording (amendments are to be applied for annual periods beginning on or after January 1, 2013);
- IFRIC 20 "Stripping Costs in the Production Phase of a Surface Mine" (effective for annual periods beginning on or after January 1, 2013); and
- Amendments to IAS 32 "Financial Instruments: Presentation" – Offsetting Financial Assets and Financial Liabilities (effective for annual periods beginning on or after January 1, 2014).

### 2.3. Standards and Interpretations in Issue not yet in Effect

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

- IFRS 9 "Financial Instruments" and subsequent amendments, supplanting the requirements of IAS 39 "Financial Instruments: Recognition and Measurement," with regard to classification and measurement of financial assets. This standard eliminates the categories existing under IAS 39 – assets held to maturity, assets available for sale and loans and receivables. IFRS 9 shall be effective for annual periods beginning on or after January 1, 2018, with early adoption permitted.

In accordance with IFRS 9, financial assets shall be classified in one of the following two categories upon initial recognition: financial assets at amortized cost or financial assets at fair value. A financial asset shall be measured at amortized cost if the following two criteria are met: financial assets relate to the business model whose objective is to collect the contractual cash flows and the contractual terms provide the basis for collection at certain future dates of cash flows that are solely payments of principal and interest on the principal outstanding. All other financial assets shall be measured at fair value. Gains and losses on the fair value measurement of financial assets shall be recognized in the profit and loss statement, except for investments in equity instruments which are not traded, where IFRS 9 allows at initial recognition a subsequently irreversible choice to recognize changes in fair value within other gains and losses in the statement of comprehensive income. An amount recognized in such a manner within the statement of comprehensive income cannot subsequently be recognized in profit and loss.

Given the nature of the Bank's operations, the adoption of the standard is expected to have a significant impact on the Bank's financial statements.

- Amendments to IFRS 11 "Joint Arrangements" – Accounting for Acquisition of an Interest in a Joint Operation (effective for annual periods beginning on or after January 1, 2016);
- IFRS 14 "Regulatory Deferral Accounts" (effective for annual periods beginning on or after January 1, 2016);

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 2. BASIS OF PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS (Continued)

### 2.3. Standards and Interpretations in Issue not yet in Effect (Continued)

- IFRS 15 "Revenue from Contracts with Customers," defining the framework for revenue recognition. IFRS 15 supplants IAS 18 "Revenue," IAS 11 "Construction Contracts," IFRIC 13 "Customer Loyalty Programs," IFRIC 15 "Agreements for the Construction of Real Estate" and IFRIC 18 "Transfers of Assets from Customers." IFRS 15 shall be effective for annual periods beginning on or after January 1, 2017, with early adoption permitted.
- Amendments to IAS 16 "Property, Plant and Equipment" and IAS 38 "Intangible Assets" – Clarification of Acceptable Methods of Depreciation and Amortization (effective for annual periods beginning on or after January 1, 2016 );
- Amendments to IAS 16 "Property, Plant and Equipment" and IAS 41 "Agriculture" – Agriculture: Bearer Plants (effective for annual periods beginning on or after January 1, 2016);
- IAS 27 "Separate Financial Statements" – Equity Method in Separate Financial Statements (effective for annual periods beginning on or after January 1, 2016);
- 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 for annual periods beginning on or after January 1, 2016 );
- Amendments to IAS 19 "Employee Benefits" – Defined Benefit Plans: Employee Contributions (effective for annual periods beginning on or after July 1, 2014);
- Amendments resulting from Annual Improvements 2010-2012 Cycle issued in December 2013 (IFRS 2, IFRS 3, IFRS 8, IFRS 13, IAS 16, IAS 24 and IAS 38) with a view to removing inconsistencies and clarifying wording (effective for annual periods beginning on or after July 1, 2014); and
- Amendments resulting from Annual Improvements 2011-2013 Cycle issued in December 2013 (IFRS 1, IFRS 3, IFRS 13 and IAS 40) with a view to removing inconsistencies and clarifying wording (effective for annual periods beginning on or after July 1, 2014).

### 2.4. Going Concern

The financial statements were prepared on a going concern assumption entailing the Bank's continuation of operations for an indefinite period in the foreseeable future.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in these financial statements.

***(a) Consolidation***

The Bank has control over the following legal entities, which are not consolidated into these financial statements:

| Legal Entity | Equity Interest |
|---|---|
| Komercijalna banka a.d. Budva, Montenegro | 100% |
| Komercijalna banka a.d. Banja Luka, Bosnia and Herzegovina | 99.99% |
| Investment Fund Management Company KomBank Invest a.d. Beograd, Serbia | 100% |

The Bank's consolidated financial statements are prepared and disclosed separately.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *(b) Foreign Exchange Translation*

Transactions in foreign currencies are translated into Dinars at the spot middle exchange rates at the date of the transactions.

Monetary assets and liabilities denominated in foreign currencies which are stated at cost, are translated at the rate ruling at the reporting date. Foreign exchange differences arising on translation are recognized in the income statement . Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of transaction.

Exchange rates for major currencies used in the translation of the statement of financial position items denominated in foreign currencies, as determined by the National Bank of Serbia, were as follows:

| | | In RSD |
|---|---|---|
| | 2014 | 2013 |
| USD | 99.4641 | 83.1282 |
| EUR | 120.9583 | 114.6421 |
| CHF | 100.5472 | 93.5472 |
| JPY | 0.830986 | 0.791399 |

### *(c) Interest*

Interest income and expense are recognized in profit or loss 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 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 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 expense presented in the statement of comprehensive income include:

- interest on financial assets and financial liabilities measured at amortized cost calculated on an effective interest basis;
- interest on investment securities available for sale.

Interest income and expenses on all trading assets and liabilities are considered to be incidental to the Bank's trading operations and are presented together with all other changes in the fair value of trading assets and liabilities in net trading income.

### *(d) Fees and Commissions*

Fee and commission income and expenses that are integral 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 is recognized as the related services are performed. Fee and commission income includes transfer payments in foreign currency, domestic payments transactions, loan administration, guarantee, letter of credit business and other banking services. When a loan commitment is not expected to result in the draw-down of a loan, the related loan commitment fees are recognized on a straight-line basis over the commitment period.

Other fee and commission expenses relate mainly to transaction and service fees, which are expensed as the services are received.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *(e) Net Trading Income*

Net trading income comprises gains less losses, related to trading assets and liabilities, and includes all realized and unrealized fair value changes and foreign exchange differences.

### *(f) Net income from Other Financial Instruments at Fair Value through Profit or Loss*

Net income from other financial instruments at fair value through profit or loss, relates to financial assets and liabilities designated at fair value through profit or loss and includes all realized and unrealized fair value changes.

### *g) Dividends*

Income from dividends is recognizedat the moment of economic benefits inflow arising from dividends. . Dividends are reported under other income.

### *(h) Operating and Finance Lease Payments*

Payments made during the year under operating leases are charged to the income statement on a straight-line basis over the period of the lease. Lease incentives received are recognized as an integral part of the total lease expense, over the term of the lease.

Minimum lease payments made under finance leases are apportioned between the finance expense and the reduction of the outstanding liability. The finance expense is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

### *(i) Tax Expenses*

Tax expense comprises current taxes and deferred taxes. Current taxes and deferred taxes are recognized in profit or loss except to the extent that it relates to items recognized directly in equity or in other comprehensive income.

*(i) Current Income Tax*

Current tax is expected tax payable or receivable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

*(ii) Deferred Income Tax*

Deferred income tax is recognized in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted by the reporting date.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities against current tax assets, and they relate to taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously in future periods.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences to the extent that it is probable that the future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized. Deferred tax liabilities are recognized on all taxable temporary differences.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *(i) Tax Expenses (Continued)*

*(iii) Other Taxes and Contributions*

According to the relevant legislation in the Republic of Serbia, the Bank pays various taxes and contributions, such as VAT, capital gains tax and payroll contributions. These are included under "other operating expenses".

### *(j) Financial Assets and Liabilities*

*(i) Recognition*

The Bank initially recognizes loans and receivables, deposits, borrowings and subordinated liabilities on the date at which they are originated. All other financial assets and liabilities are initially recognized on the balancing date at which the Bank becomes a party to the contractual provisions of the instrument.

A financial asset or liability is measured initially at fair value plus transaction costs that are directly attributable to its acquisition or issue, for items that are not carried at fair value through profit or loss.

*(ii) Classification*

The Bank classified its financial assets into the following categories: financial assets held for trading, loans and receivables and investment securities – please refer to accounting policies 3(l), 3(m) and 3(n).

The Bank classifies its financial liabilities as measured at amortized cost or held for trading – please refer to accounting policies.

*(iii) Derecognition*

The Bank derecognizes a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all the risk and rewards of ownership and it does not retain control of the financial asset. Any interest in transferred financial assets that qualifies for derecognition that is created or retained by the Bank is recognized as a separate asset or liability in the statement of financial position. On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset transferred), and the sum of the consideration received (including any new asset obtained less any new liability assumed) and any cumulative gain or loss that had been recognized in other comprehensive income is recognized in profit or loss.

The Bank enters in transactions whereby it transfers assets recognized on its statement of financial position, but retains either all or substantially all of the risks and rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognized. Transfers of assets with retention of all or substantially all risks and rewards include, for example, repurchase transactions.

In transactions in which the Bank neither retains nor transfers substantially all the risk and rewards of ownership of a financial asset and it retains control over the asset, the Bank continues to recognize the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of transferred asset.

*(iv) Offsetting*

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

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *(j) Financial Assets and Liabilities (Continued)*

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

*(v) Amortized Cost Measurement*

The amortized cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortization using the effective interest method of any difference between the initial amount recognized and the maturity amount, less any impairment.

*(vi) Fair Value Measurement*

The fair values stated for financial instruments are the amounts for which the asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

When available, the Bank measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, the Bank establishes fair value using a valuation technique. Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analyses and other optional models. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to the Bank, incorporates all factors that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument. The Bank calibrates valuation techniques and tests them for validity using prices from observable current market transactions in the same instrument of based on other available observable market data.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price, i.e. the fair value of the consideration given or received, unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e., without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When transaction price provides the best evidence of fair value at initial recognition, the financial instrument is initially measured at the transaction price and any difference between this price and the value initially obtained from a valuation model is subsequently recognized in profit or loss depending on the individual facts and circumstances of the transaction but not later than when the valuation is supported wholly by observable market data or the transaction is closed out.

Any difference between the fair value at initial recognition and the amount that would be determined at that date using a valuation technique in a situation in which the valuation is dependent on unobservable parameters is not recognized in profit or loss immediately but is recognized over the life of the instrument on an appropriate basis or when the instrument is redeemed, transferred or sold, or the fair value becomes observable. Assets and long positions are measured at a bid price and liabilities and short positions are measured at an asking price. Fair values reflect the credit risk of the instrument and include adjustments to take account of the credit risk of the Bank and counterparty where appropriate. Fair value estimates obtained from models are adjusted for any other factors, such as liquidity risk or model uncertainties to the extent that the Bank believes a third-party market participant would take them into account in pricing a transaction.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *(j) Financial Assets and Liabilities (Continued)*

*(vii) Identification and Measurement of Impairment*

At reporting date the Bank assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. A financial asset or a group of financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the assets, and that the loss event has an impact on the future cash flows of the assets that can be estimated reliably.

Objective evidence that financial assets (including equity securities) are impaired can include significant financial difficulty of the borrower or issuer, default or delinquency by a borrower, restructuring of a loan or advance by the Bank on terms that the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

The Bank considers evidence of impairment for loans and receivables and held-to-maturity investment securities at both a specific asset and collective level. All individually significant loans and receivables and held-to-maturity investment securities are assessed for specific impairment. All individually significant loans and receivables and held-to-maturity investment securities found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and receivables and held-to-maturity investment securities that are not individually significant are collectively assessed for impairment by grouping together loans and receivables and held-to-maturity investment securities with similar risk characteristics.

In assessing collective impairment the Bank uses statistical modeling of historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgment as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical modeling. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

Impairment losses on assets carried at amortized cost are measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognized in profit or loss and reflected in an allowance account against loans and receivables. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss. Impairment losses on available-for-sale investment securities are recognized by transferring the cumulative loss that has been recognized in other comprehensive income to profit or loss as a reclassification adjustment. The cumulative loss that is reclassified from other comprehensive income to profit or loss is the difference between the acquisition costs, net of any principal repayment and amortization, and the current fair value, less any impairment loss previously recognized in profit or loss. Changes in impairment provisions attributable to time value are reflected as a component of interest income. Movements on provisions for impairment losses attributable to the time value are included as a component of the interest rate.

If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in profit or loss, the impairment loss is reversed, with the amount of the reversal recognized in profit or loss. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognized in other comprehensive income.

The Bank writes off certain loans and receivables and investment securities when they are determined to be uncollectible (see note 4(b)).

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *(k) Cash and Cash Equivalents*

Cash and cash equivalents include notes and coins on hand, unrestricted balances held with central banks and highly liquid financial assets with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value, and are used by the Group in the management of its short-term commitments.

Cash and cash equivalents are carried at amortized cost in the balance sheet.

### *(l) Trading Assets and Liabilities*

Trading assets and liabilities are those assets and liabilities that the Bank acquires or incurs principally for the purpose of selling or repurchasing in the near term, or holds as part of a portfolio that is managed together for short-term profit or position taking.

Trading assets and liabilities are initially recognized and subsequently measured at fair value in the statement of financial position, with transaction costs directly recognized in profit or loss. All changes in fair value are recognized as part of net trading income in profit or loss. Trading assets were not reclassified subsequent to their initial recognition, except that non-derivative trading assets, other than those designated at fair value through profit or loss upon initial recognition, may have been reclassified out of the fair value through profit or loss, i.e. trading category, if they were no longer held for the purpose of being sold or repurchased in the near term and either of the conditions below were met.

- If the financial asset would have met the definition of loans and receivables (if the financial asset had not been required to be classified as held for trading at initial recognition), then it may be reclassified if the legal entity has the intention and ability to hold the financial asset for the foreseeable future or until maturity.
- If the financial asset would not have met the definition of loans and receivables, then it may be reclassified out of the trading category only in rare circumstances.

*Derivatives*

Financial derivatives comprise forward and swap transactions. Financial derivatives are initially recognized at cost and are subsequently measured at market value. Market values are ascertained based on quoted prices on an active market, as well as by using different valuation techniques, including discounted cash flows. Financial derivatives are accounted for under assets if their market value is positive, and under liabilities if their market value is negative. Fluctuations in market value of financial assets are reported in the statement of comprehensive income, under net trading income.

### *(m) Loans and Receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Bank does not intend to sell immediately or in the near term. They arise when the Bank provides money or services directly to a debtor with no intention of trading the receivable. Loans and receivables comprise loans and receivables to banks and customers. Loans and receivables are initially measured at fair value plus incremental direct transaction costs, and subsequently measured at their amortized cost using the effective interest method.

Approved dinar loans which are hedged using a contractual currency clause linked to the dinar EUR exchange rate, to another foreign currency or consumer price index are converted into dinars at balance sheet date in accordance with the terms of the particular loan agreement. The effects of the currency conversion are reported under trading income and expenses. Loans and receivables are presented net of specific and collective allowances for impairment. Specific and collective allowance, are made against the carrying amount of loans and receivables that are identified as being impaired in order to reduce their value to recoverable amount. 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 (such as an improvement in the debtor's credit rating), the previously recognized impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognized in the statement of comprehensive income in impairment charge for credit losses.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *(n) Investment Securities*

Investment securities are initially measured at fair value plus, in case of investment securities not at fair value through profit or loss, incremental direct transaction costs, and subsequently accounted for depending on their classification as either held-to-maturity, fair value through profit or loss, or available-for-sale.

*(i) Held-to-Maturity Financial Assets*

Held to maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Bank has the positive intention and the ability to hold them to maturity, and which are not designated as at fair value through profit or loss or as available-for-sale.

Held-to-maturity investments are carried at amortized cost using the effective interest method. Any sale or reclassification of a more than insignificant amount of held-to-maturity investments would result in the reclassification of all held-to-maturity investments as available-for-sale, and prevent the Bank from classifying investment securities as held-to-maturity for the current and the following two financial years. However, sales and reclassifications in any of the following circumstances would not trigger a reclassification:

- sales or reclassifications that are so close to maturity that changes in the market rate of interest would not have a significant effect on the financial asset's fair value,
- sales or reclassifications after the Bank has collected substantially all of the asset's original principal, and
- sales or reclassifications attributable to non-recurring isolated events beyond the Bank's control that could not have been reasonably anticipated.

*(ii) Financial Assets at Fair Value through Profit or Loss*

Financial assets at fair value through profit or loss are financial assets that are classified as held for trading or upon initial recognition are designated by the Bank as at fair value through profit or loss. Financial assets at fair value through profit or loss are those that the Bank acquired or incurred principally for the purpose of selling or repurchasing it in the near term, part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking or derivatives.

*(iii) Available- for- Sale Financial Assets and Equity Investments*

Available for sale financial assets are those non-derivative financial assets that are designated as available for sale or are not classified as another category of financial asset. Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

Unquoted equity securities whose fair value cannot be reliably measured are carried at cost. All other available-for-sale investments are carried at fair value.

Interest income is recognized in profit or loss using the effective interest method. Dividend income is recognized in profit or loss when the Bank becomes entitled to the dividend. Foreign exchange gains or losses on available-for-sale debt security investments are recognized in profit or loss.

Other fair value changes are recognized in other comprehensive income until the investment is sold or impaired, whereupon the cumulative gains and losses previously recognized in other comprehensive income are reclassified to profit or loss as a reclassification adjustment.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *(n) Investment Securities (Continued)*

*(iii) Available- for- Sale Financial Assets and Equity Investments (Continued)*

When a decline in the fair value of an available-for-sale financial asset has been recognized in other comprehensive income and there is objective evidence that the asset is impaired (long and continuing decline in the fair value in the period longer than twelve months, as well as decline above 30% of cost), as well as the cumulative loss that had been recognized in other comprehensive income shall be reclassified from equity to profit or loss as a reclassification adjustment even though the financial asset has not been derecognized (IAS 39.59, IAS 39.67 and IAS 39.68)

A non-derivative financial asset may be reclassified from the available-for-sale category to the loans and receivables category if it otherwise would have met the definition of loans and receivables and if the Bank has the intention and ability to hold that financial assets for the foreseeable future or until maturity.

### *(o) Property and Equipment*

*(i) Recognition and Measurement*

Items of property and equipment are measured at cost.

Cost includes expenditures that are directly attributable to the acquisition of the asset. Purchased software that is integral to the functionality of the related equipment is capitalized as part of that equipment.

Following initial recognition items of equipment are measured at cost less accumulated depreciation and accumulated impairment losses.

Following initial recognition, property is measured at valuation amount which represents its fair value at valuation date less subsequent accumulated depreciation and subsequent accumulated impairment losses. Valuation is performed regularly in order to ensure that net book value does not differ significantly from reported amounts that would result from using the fair value approach at the end of reporting period.

When parts of an item of property or equipment have different useful lives, they are accounted for as separate items (major components) of property and equipment.

The gain or loss on disposal of an item of property and equipment is determined by comparing the proceeds from disposal with the carrying amount of the item or property and equipment, and are recognized net within other income in profit or loss.

*(ii) Subsequent Costs*

The cost of replacing part of an item of property or equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Bank and its cost can be measured reliably. The carrying amount of the replaced part is derecognized. The costs of the day-to-day servicing of property and equipment are recognized in profit or loss as incurred.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *(o) Property and Equipment (Continued)*

*(iii) Depreciation*

Depreciation is recognized in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property and equipment since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Leased assets are depreciated over the shorter of the lease term and their useful lives.

The estimated depreciation rates for the current and comparative periods were as follows:

| Asset | Estimated useful life (in years) | Rate % |
|---|---|---|
| Buildings | 40 | 2.50% |
| Computer equipment | 4 | 25% |
| Furniture and other equipment | 5 – 15 | 10%-15.5% |
| Leasehold improvements | 1 – 11 | 4.25%-86.2% |

Depreciation methods, useful lives and residual values are reassessed at each financial year-end and adjusted if appropriate.

Maintenance costs for assets are recognized in the profit or loss in the period when occurred.

### (p) Intangible Assets

Intangible assets acquired by the Bank are stated at cost less accumulated amortization and accumulated impairment losses.

Subsequent expenditure on intangible assets is capitalized only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Amortization is recognized in profit or loss on a straight-line basis over the estimated useful life of the intangible asset, from the date that it is available for use since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. The estimated useful life of intangible assets is 3 to 5 years and amortization rates used range between 14.29% and 33.34%.

Amortization methods, useful lives and residual values are reassessed at each financial year-end and adjusted if appropriate.

### *(q) Investment Property*

Investment property is property held either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business, use in the production or supply of goods or services or for administrative purposes.

Investment property is initially measured at cost. Cost of acquired investment property comprises the purchase price and all expenses that can be directly attributed to the acquisition of the asset.

For subsequent measurement of investment property the Bank uses the cost model, such that investment property is measured at cost less accumulated depreciation and impairment losses.

Estimated useful life of investment property amounts to 40 years, while the depreciation rate used amounts to 2.5%. Depreciation is provided for in profit or loss on a straight line basis over the useful life of a given item of property, given that it reflects best the expected exploitation of the useful economic value embodied in the asset.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *(r) Leases*

The Bank is a lessee based on leasing agreements. The Bank classifies leases as financial leasing when the lease agreement stipulates that the basic risks and benefits of ownership over the leased assets are transferred to the lessee. All other leasing agreements are classified as operating leases.

Lease agreements that relate to lease of office space in which the Bank's branches are located primarily relate to operating leases. All payments made during the year based on operating leases are reported as an expense in the statement of comprehensive income on a straight line basis over the duration of the lease period.

Assets that are held based on a finance lease agreement are recognized as the Bank's assets at the lower of their fair value or the present value of minimum lease payments specified at the start of the lease agreement. The corresponding liability toward the lessor is reported in the statement of financial position as a finance lease liability. Lease payments are apportioned between the finance expense and the reduction of the outstanding finance lease liability, such that a constant interest rate is achieved on the outstanding portion of the liability. The financial expense is reported directly as a period expense.

### *(s) Impairment of Non-Financial Assets*

The carrying amounts of the Bank's non-financial assets, other than investment property and deferred tax assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated. An impairment loss is recognized if the carrying amount of an asset exceeds its estimated recoverable amount.

The recoverable amount of an asset is the greater of its value in use and its fair value less costs 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.

An impairment loss is recognized when the carrying amount of an asset exceeds its recoverable amount. Impairment losses are recognized in profit or loss.

Impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. 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 amortization, if no impairment loss had been recognized.

### *(t) Deposits, Borrowings and Subordinated Liabilities*

Deposits, debt securities, borrowings and subordinated liabilities are the Bank's main sources of financing.

The Bank classifies capital instruments as financial liabilities or equity instruments in accordance with the substance of the contractual terms of the instruments.

Deposits, debt securities, borrowings and subordinated liabilities are initially measured at fair value increased for all directly attributable transaction costs, while they are subsequently measured at amortized cost using the effective interest rate method.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *(u) Provisions*

A provision is recognized if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

### *(v) Employment Benefits*

In accordance with regulatory requirements, the Bank is obligated to pay contributions to tax authorities and to various state social security funds, which guarantee social security insurance benefits to employees. These obligations involve the payment of taxes and contributions on behalf of the employee, by the employer, in an amount computed by applying the specific, legally-prescribed rates. The Bank is also legally obligated to withhold contributions from gross salaries to employees, and on behalf of its employees, to transfer the withheld portions directly to government funds. These taxes and contributions payable on behalf of the employee and employer are charged to personnel expenses in the period in which they arise.

In accordance with the Labor Law, the Bank is under obligation to pay its vesting employees retirement benefits. Long-term liabilities for retirement benefit provisions upon fulfillment of retirement criteria reported as of December 31, 2014 represent the present value of the expected future payments to employees as determined by actuarial assessment using assumptions disclosed in Note 36(b).

### *(w) Financial Guarantees*

Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

Financial guarantee liabilities are initially recognized at their fair value, and the initial fair value is amortized over the life of the financial guarantee. The guarantee liability is subsequently carried at the higher of this amortized amount and the present value of any expected payment (when a payment under the guarantee has become probable). Financial guarantees are reported under off-balance sheet items.

### *(x) Capital and Reserves*

The Bank's equity consists of founders' capital, shares of subsequent issues, share premium, profit reserves, revaluation reserves and unrealized losses on available for sale securities, retained earnings and current period result.

The Bank's equity is comprised of funds invested by the Bank's founders in pecuniary form. A founder cannot withdraw funds invested in the Bank's equity.

### *(y) Earnings per Share*

The Bank presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the period.

Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### *(z) Segment Reporting*

An operating segment is a component of the Bank that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Bank's other components, whose operating results are reviewed regularly by Bank management (being the chief operating decision maker) to make decisions about resources allocated to each segment and assess its performance, and for which discrete financial information is available.

## 4. RISK MANAGEMENT

The Bank has recognized risk management process as the key element of business management given that risk exposure is an inseparable part of banking and is managed through a process of continued identification, measurement, monitoring, minimizing and setting of risk limits and through other types of control, including reporting in accordance with adopted strategies and policies.

The Bank has established a comprehensive and reliable risk management system that includes: risk management strategies, policies and procedures, appropriate organizational structure, effective and efficient process of managing all risk it is exposed to, adequate system of internal controls adequate information system and process of internal capital adequacy assessment.

Risk management process involves clear determining and documenting risk profile and adjusting risk profile to the Bank's aptitude to assume risk in accordance with the adopted strategies and policies.

The basic objectives that the Bank set for the risk management system within its risk management and capital management strategies are the following: minimizing the negative effects on financial result and equity within acceptable risk levels, maintaining the required level of capital adequacy, developing the Bank's activities in accordance with business opportunities and market development with a view to gain competitive advantage.

The Bank implements Basel II standards and permanently monitors all the announcement and amendments to the effective regulations, analyses the risk levels and undertakes measures for timely reconciliation of its operations with newly enacted regulations in accordance with the risk level acceptable to the Bank. Through the clearly defined process of introducing new products, the bank analyses the influence of all new services and products on the future risk exposures in order to optimize its revenues and losses based on the estimated risk as well as to minimize all potential adverse effects on the Bank's financial result.

### Risk Management System

The risk management system is governed by the following internal enactments:

- Risk Management Strategy and Capital Management Strategy;
- Risk Management Policies;
- Risk Management Procedures;
- Methodologies for Managing Individual Risks; and
- Other enactments.

Risk Management Strategy sets out:

- Long-term objectives, defined by the Bank's business policy and strategy and its attitude to assume risk determined in accordance with those objectives;
- Basic principles of risk assumption and management;
- Basic principles of the process of internal assessment of the Bank's capital adequacy; and
- Overview and definitions of all types of risk the Bank is exposed to or may be exposed to.

## 4. RISK MANAGEMENT (Continued)

### Risk Management System (Continued)

The Bank specified the basic principles of risk management for meeting its long-term objectives:

- Organizing operation of a separate organizational unit for risk management;
- Functional and organizational separation of risk management activities from the regular operating activities of the Bank;
- Comprehensive risk management;
- Effective risk management;
- Cyclic risk management;
- Developing risk management as a strategic orientation; and
- Risk management as a part of corporate culture.

Policies for managing certain risk types define the following:

- Manner of organizing risk management processes within the Bank and clear division of personnel responsibilities in all stages of the process;
- Manner of assessing the Bank's risk profile and methodology for identifying, measuring and assessing risks;
- Manners of risk monitoring and control and establishing the system of limits, i.e. types of limits the Bank uses as well as their structure;
- Measures for risk mitigation and rules for implementation thereof;
- Manner and methodology for implementing the process of internal assessment of the Bank's capital adequacy;
- Principles of the system of internal controls; functioning; and
- Framework and frequency for stress testing and procedure in instances of unfavorable test results.

Procedures for managing certain risk types define, in greater detail, the process of managing risks and competencies and responsibilities of all organizational units of the Bank in the risk management system.

Individual methodologies further and in more detail prescribe methods and approaches used in the risk management system.

### Competencies

*The Board of Directors* is authorized and responsible for establishing a uniform risk management system and for monitoring such system, adopting policies and procedures for risk management and capital management strategy, establishment of internal control system, supervision of the work of the Executive Board and execution of the process of internal capital adequacy assessment.

*The Executive Board* is authorized and responsible for implementation of risk management strategy and policies, capital management strategy adoption and efficiency analysis of risk management procedure implementation, which define processes of identifying, measuring, minimizing, monitoring, controlling reporting risk the Bank is exposed to. Executive Board reports to the Board of Directors on implementation efficiency of defined management risk procedures.

*The Audit Committee* is authorized and responsible for continued monitoring of application of risk management policies and procedures, and for implementing the internal control system. The Audit Committee at least monthly reports to The Board of Directors on its activities, irregularities, and propose how they will be removed.

*The Asset and Liability Committee* (ALCO) is authorized and responsible for monitoring the Bank's risk exposure resulting from the structure of its receivables, payables and off-balance sheet items, and proposes measures for managing interest and liquidity risks.

*The Credit Committee* decides on loan requests in accordance with the Bank's internal acts, it analyzes the Bank's exposure to credit, interest and currency risk, it analyzes the credit portfolio and implements results of internal audit under the Committee's jurisdiction, and also suggests adequate measures to the Executive Board.

## 4. RISK MANAGEMENT (Continued)

**Competencies (Continued)**

*The Collections Committee* is authorized and responsible for managing risk weighted placements; it makes decisions on the write-off of risk-weighted loans up to set limits of authorization and recommends write-off of loans to the Executive Board and Board of Directors through its limits of authorization.

*The Risk Management Organizational Unit* defines and proposes for adoption, the risk management strategy, policies, procedures and methodologies identifies, measures, mitigates, monitors, controls and reports on the risks the Bank is exposed to. It is also in charge of developing models and methodologies of risk management and reporting to the competent Bank's bodies.

*The Treasury* is responsible for managing assets and liquidity, the Bank's assets and liabilities, their overall financial structure, and is primarily responsible for the Bank's liquidity risk, interest rate risk and foreign currency risk.

*The Internal Audit Division* is responsible for continued monitoring of implementation of risk management policies and procedures, and tests the adequacy of procedures and the Bank's compliance thereto. Internal Audit reports its findings and recommendations to the Audit Committee and the Board of Directors.

*The Compliance Control Division* is obligated to identify and assess compliance risks at least annually and propose risk management plans, whereof it prepares a report and submits it to the Executive Board and Board for Monitoring of the Bank's operation.

**Risk Management Process**

The Bank regularly measures and evaluates risks identified in its operations. Measurement entails applying qualitative and quantitative measurement methods and models that enable detection of changes in risk profile and assessment of new risks.

For all risks identified the Bank determines their significance based on as comprehensive assessment of risks in the Bank's particular operations, products, activities and processes.

Risk alleviation or mitigation involves risk diversification, transfer, minimization and or avoidance; the Bank performs risk mitigation in accordance with risk profile and risk appetite.

Risk monitoring and control is based on limits that are set by the Bank. They in turn depend on business strategy and the business environment, as well as on the level of risk that the Bank is ready to accept.

Risk management reports are regularly submitted to: the Bank's Board of Directors, Executive Board, Audit Committee, ALCO and Credit Committee, and they contain all the information required for risk assessment and reaching of conclusions about the Bank's risks.

**Risk Types**

In its regular course of business, the Bank is particularly exposed to the following risks: credit risk and risks associated with the credit risk, liquidity risk, market risk, operational risks, investment risk, exposure risk and country risk as well as to all other risks that may arise from the Bank's regular operations.

### 4.1. Credit Risk

Credit risk represents the risk of negative effects on the Bank's financial result and capital arising from debtors' inability to settle the matured liabilities to the Bank.

The Bank has defined criteria for loan approval and rescheduling and restructuring of receivables prescribed by its loan approval procedures and methodology. Loans are approved depending on the target market, borrower characteristics and loan purpose.

## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

Prior to loan approval, the Bank assesses the creditworthiness of the borrower based on internally defined criteria as a primary and offered collateral as a secondary source of collection/loan repayment. Based on the identified and measured credit risk level (assessed financial situation and credit worthiness of the borrower, value and legal security of the credit hedge and other relevant factors), and independent risk assessment, the Bank's competent bodies enact a loan approval decision in accordance with the defined decision making system.

Decisions on credit risk exposure are defined through the decision making system that depends on the type of customer and exposure level: for loans within defined limits decisions are made by the branch credit committees, although in certain cases approval of the risk management organizational unit is required. Central Credit Committee decides on the loans in excess of the defined limits (depending on the type of client) with prior opinion of the risk management organizational unit. The Executive Board and Board of Directors make decisions depending on the exposure levels.

In decision making the principle of double control, the so-called "four eyes principle," is observed which ensures that there is always a party that proposes and a party that approves a particular loan/investment.

For loans contracted in foreign currencies or RSD loans indexed to a currency clause, the Bank estimates the effects of the changes in foreign exchange rates on the financial situation and creditworthiness of debtors and particularly analyzes adequacy of the debtor's cash flows in relation to the changed level of liabilities per loans assuming that there will be certain fluctuation in RSD exchange rates on an annual basis.

***Credit Risk Management***

According to the volume, type and complexity of its operations, the Bank has organized the credit risk management process and clearly delineated employee responsibilities in all stages of the process.

The organizational model of credit risk management system enables adequate communication, information exchange and collaboration at all organizational levels within the Bank as well as clear operational and organizational separation of functions for independent risk management and supporting activities on one hand and the activities of risk assumption on the other, i.e. segregation of duties, competencies and responsibilities. The Bank has also established an adequate information system for full coverage of persons involved in credit risk management system and appropriate management reporting.

The level of credit risk exposure acceptable to the Bank is in line with the defined risk management strategy and depends on the Bank's portfolio structure based on which is limited negative effects on the Bank's financial result and capital adequacy. On the other hand, the Bank does not make high-risk investments such as investments in highly profitable projects with significant risk levels.

The basic principles of credit risk management are as follows:

- Managing credit risk at the individual loan level as well as the Bank's entire portfolio level;
- Maintaining credit risk level that minimizes the negative effects on the Bank's financial result and capital;
- Loan rating according to risk;
- Operating in accordance with best banking practices of loan approval;
- Ensuring adequate credit risk management controls.

In its effort to manage credit risk the Bank seeks to do business with customers that have good credit rating and to acquire appropriate collaterals to secure repayments. The Bank assesses creditworthiness of each customer upon the submission of a loan application and regularly monitors its debtors, loans and collaterals, in order to be able to undertake appropriate activities for the purpose of collecting its receivables.

## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

***Credit Risk Management (Continued)***

The Bank performs quantitative and/or qualitative measurement, i.e. assessment of the identified credit risk. The credit risk measurement process is based on measuring risk level of individual loans and investments based on the internally adopted rating system.

The rating system is not merely an instrument for encasement individual decisions and assessing risk levels of individual investments; it is also a basis for portfolio analysis, support in loan approval and loan impairment procedure as well as in estimating provisions against losses per off-balance sheet items for the purpose of loan and investment ranking by risk level and stating realistic value of receivables. Internal rating system is subject to regular review and improvements.

In addition to the internal rating system, in credit risk analysis the Bank also uses principles prescribed by the National Bank of Serbia, which require classification of loans based on the prescribed criteria as well as calculation of the reserve for estimated credit risk losses. Application of these principles allows the Bank to cover unexpected losses due to the customer's inability to settle liabilities as they fall due, in accordance with contractually defined terms. For these purposes, the Bank classifies receivables and assesses the level of necessary reserve using the regular analysis of portfolio. The analysis includes the measurement of adequacy of reserves formed against individual borrowers, risk categories, portion of portfolio and at overall portfolio level.

Alleviating credit risk entails maintaining the risk at the level acceptable to the Bank's risk profile, i.e. maintaining acceptable quality level of the Bank's loan portfolio.

Basic credit risk alleviating techniques are:

- Exposure limits – concentration risk;
- Investment diversification; and
- Collaterals.

The Bank's exposure limits per individual debtor are based on the assessment of the debtor's credit-worthiness, whereas the exposure limits at the portfolio level are focused on restricting exposure concentration within the portfolio. The Bank continuously controls credit risk movements within a defined risk profile.

Concentration risk includes: large exposure (exposure to a single entity or a group of related entities and the Bank's related parties), group exposures with the same or similar risk factors such as industry sectors, types of products, geographical areas and the like, county risk and credit risk hedges.

Monitoring investment quality at the individual debtor level is primarily based on obtaining updated information on the financial situation and creditworthiness of the debtor as well as on the market value of collateral, whereas credit risk monitoring at the portfolio level is performed through identification of changes at the level of client groups with certain preset levels of risk, investment, collateral and required reserves for estimated and unexpected losses for the purpose of establishing management of the asset balances and quality.

Credit risk control entails a process of continuous reconciling business operations with the defined system of limits, both on a daily and monthly bases, as well as under conditions of large credit exposure approaching the upper risk profile limit, i.e. upon introduction of new products and business activities.

As a hedge against counterparty default risk, the Bank undertakes the following steps in respect to collection of due receivables: rescheduling or restructuring; out-of-court settlement; seizure of goods or properties in order to collect receivables; sale and/or assignment of receivables; executing agreements with interested third parties; and instigating court proceedings and other measures.

## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

***Credit Risk Management (Continued)***

If the undertaken measures for regulating collection, i.e. enforced collection and court proceedings fail to provide expected results, i.e. when receivables cannot be collected in full, the Bank initiates write-off of the remaining receivables.

Apart from credit risk exposure, the Bank also has off-balance sheet exposures (various types of payment and performance guarantees, acceptances and letters of credit) based on which the Bank has contingent liabilities to make payments on behalf of third parties. For off-balance sheet exposures the Bank uses the same control processes and procedures that are used for credit risk.

Credit risk reporting includes internal and external reporting systems executed on a monthly basis according to a preset schedule and in conformity with the defined reporting system.

*Downgrade Risk*

The quality of the Bank's assets is measured by the level of exposure to individual risk categories according to internal rating system criteria. The internal rating system focuses on quantitative and qualitative parameters for assigning customer ratings. The rating scale consists of 5 risk categories that are subdivided into 17 subcategories. Different exposures to the same borrower are grouped in the same credit rating category irrespective of the specificities of different loan types.

The Bank uses varying credit rating models depending on the borrower type. Credit rating is calculated on monthly basis based on the qualitative and quantitative parameters and timely and regular liability settlement.

A low level of risk implies doing business with customers with a high credit rating (risk rating categories 1 and 2), increased level of risk implies doing business with customers with operating difficulties that could have a negative impact on the settlement of liabilities (risk rating category 3), and a high level of risk characterizes customers with negative operating results and poor credit rating history (risk rating categories 4 and 5).

The Bank protects itself against downgrade risk through continuous monitoring of customers' business operations and by identifying changes that could arise through: deterioration of a borrower's financial standing, delays in repayment and changes in the business environment, as well as by securing appropriate collaterals.

*Risk of Change in Value of Assets*

Allowance for impairment of loans is intended to ensure reasonable, cautious and timely registering of losses on loan impairment, as well as to intervene in respect of contingent liabilities with a view to protect the Bank in the period when the loss occurs and is definitely confirmed (realized), due to inability to collect contracted amounts or through outflow of assets to settle contingent liabilities.

Allowance for impairment of loans and provisions are made when there is justification and objective evidence of impairment arising as the result of events that occurred after initial recognition of a loan, that have a negative effect on future cash flows associated with a loan.

Key elements in assessing impairment of loans are as follows: overdue payments on principal or interest, cash flow difficulties on the part of the borrower, the borrower's credit rating deterioration or changes in the initial terms of contract etc.

Allowance for impairment is based on estimated future cash flows from the borrower's business or collateral foreclosure if it is assessed that a loan can be realistically settled from such assets.

The Bank assesses allowance for impairment of receivables on an individual and on a group basis.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

***Credit Risk Management (Continued)***

*Individual Assessment*

The Bank assesses impairment of each individually significant loan and considers the financial position of the loan beneficiary, sustainability of its business plan, its ability to improve performance in the event of financial difficulties, income projections, availability of other financial support and collateral value which can be realized, as well as scheduling of expected cash flows. In the event of new information coming to light that significantly alters the customer's creditworthiness, value of collateral and likelihood that liabilities toward the Bank will be settled, ad hoc assessment of loan impairment is performed.

*Group Assessment*

Impairment is assessed on a group basis for loans that are not individually significant and for individually significant loans and advances, when there is no objective evidence of individual impairment. Group assessment is performed monthly within groups that are determined based on internal methodology and internal rating system. Group impairment percentages are calculated based on migration of risk rating categories in default status per type of borrower or product.

Impairment of loans decreases the value of loans and is recognized as an expense in the income statement.

*Assessment of Provisions for Losses on Off-Balance Sheet Items*

Assessment of provisions for losses on off-balance sheet items (contingent liabilities) is performed when it is estimated that it is fairly certain that an outflow of assets will be required to settle contingent liabilities.

In assessing provisions for contingent losses on off-balance sheet items, funds obtained by activating collaterals are recognized if it is completely certain that cash outflows for contingent liabilities will be settled from collaterals.

#### *4.1.1. Maximum Credit Risk Exposure*

Maximum credit risk exposure as of December 31, 2014 and 2013 is presented in the table below without taking into account any collateral or any other sort of credit risk hedge. The stated values are presented in gross and net carrying amounts (after impairment effects).

*Maximum Credit Risk Exposure before Collateral or any Other Improvements*

| | December 31, 2014 | | December 31, 2013 | |
|---|---|---|---|---|
| | **Gross** | **Net** | **Gross** | **Net** |
| **I. Assets** | **411,491,955** | **387,248,783** | **365,278,655** | **344,901,797** |
| Cash and cash funds held with the central bank | 68,547,389 | 68,547,389 | 70,934,839 | 70,934,839 |
| Loans and receivables due from banks and other financial institutions | 35,106,194 | 34,737,605 | 35,573,308 | 35,247,935 |
| Loans and receivables due from customers | 208,462,012 | 185,377,035 | 196,390,640 | 177,560,058 |
| Financial assets | 95,774,547 | 95,654,325 | 57,195,947 | 57,150,504 |
| Other assets | 3,601,813 | 2,932,429 | 5,183,921 | 4,008,461 |
| **II. Off-balance sheet items** | **30,165,789** | **29,597,365** | **30,882,511** | **30,408,862** |
| Payment guarantees (Note 39.1) | 4,767,131 | 4,626,118 | 7,357,476 | 7,291,000 |
| Performance bonds (Note 39.1) | 7,883,510 | 7,734,385 | 5,787,610 | 5,661,141 |
| Irrevocable commitments | 16,715,960 | 16,715,960 | 16,830,341 | 16,830,341 |
| Other items | 799,188 | 520,902 | 907,084 | 626,380 |
| **Total (I+II)** | **441,657,744** | **416,846,148** | **396,161,166** | **375,310,659** |

The largest credit risk is associated with the executed loan arrangements; however, the Bank is exposed to credit risk based on off-balance sheet items resulting from commitments and contingent liabilities.

**NOTES TO THE FINANCIAL STATEMENTS**
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## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

#### 4.1.1. *Maximum Credit Risk Exposure (Continued)*

*Loans and receivables due from customers, banks and other financial institutions*

| | Housing Loans | Cash Loans | Agricultural Loans | Other Loans | Micro Business | Total Retail | Corporate Customers | December 31, 2014 Total | December 31, 2014 Due from Banks |
|---|---|---|---|---|---|---|---|---|---|
| Loans not matured and not provided for | - | - | - | - | - | - | 2,313,323 | 2,313,323 | 27,533,227 |
| Loans matured and not provided for | - | - | - | - | - | - | 1,557,306 | 1,557,306 | 7,204,378 |
| Group-level impaired | 37,033,132 | 15,133,016 | 5,307,696 | 7,264,505 | 6,248,660 | 70,987,009 | 95,147,574 | 166,134,583 | 368,589 |
| Individually impaired | 760,253 | - | 94,069 | - | 995,964 | 1,850,286 | 36,606,514 | 38,456,800 | - |
| **Total** | **37,793,385** | **15,133,016** | **5,401,765** | **7,264,505** | **7,244,624** | **72,837,295** | **135,624,717** | **208,462,012** | **35,106,194** |
| **Impairment allowance** | **543,326** | **903,607** | **436,472** | **720,048** | **1,070,353** | **3,673,807** | **19,411,170** | **23,084,977** | **368,589** |
| Group-level impairment allowance | 440,780 | 903,607 | 413,477 | 720,048 | 883,455 | 3,361,367 | 8,733,842 | 12,095,209 | 368,589 |
| Individual impairment allowance | 102,546 | - | 22,995 | - | 186,899 | 312,440 | 10,677,328 | 10,989,768 | - |
| **Net carrying value** | **37,250,059** | **14,229,409** | **4,965,292** | **6,544,457** | **6,174,271** | **69,163,489** | **116,213,547** | **185,377,035** | **34,737,605** |

| | Housing Loans | Cash Loans | Agricultural Loans | Other Loans | Micro Business | Total Retail | Corporate Customers | Total | Due from Banks |
|---|---|---|---|---|---|---|---|---|---|
| Loans not matured and not provided for | - | - | - | - | - | - | 9,308,456 | 9,308,456 | 34,239,484 |
| Loans matured and not provided for | - | - | - | - | - | - | 10,872,773 | 10,872,773 | 1,008,450 |
| Group-level impaired | 33,194,871 | 12,698,570 | 4,200,215 | 7,934,218 | 5,489,608 | 63,517,482 | 77,823,250 | 141,340,732 | 325,374 |
| Individually impaired | 503,566 | - | 37,487 | - | 962,271 | 1,503,324 | 33,365,355 | 34,868,679 | - |
| **Total** | **33,698,436** | **12,698,570** | **4,237,702** | **7,934,218** | **6,451,880** | **65,020,806** | **131,369,833** | **196,390,640** | **35,573,308** |
| **Impairment allowance** | **467,808** | **712,610** | **319,152** | **636,461** | **990,703** | **3,126,734** | **15,703,847** | **18,830,581** | **325,374** |
| Group-level impairment allowance | 329,772 | 712,610 | 306,438 | 636,461 | 855,235 | 2,840,516 | 9,583,119 | 12,423,635 | 325,374 |
| Individual impairment allowance | 138,036 | - | 12,714 | - | 135,468 | 286,218 | 6,120,728 | 6,406,946 | - |
| **Net carrying value** | **33,230,629** | **11,985,960** | **3,918,550** | **7,297,757** | **5,461,176** | **61,894,072** | **115,665,986** | **177,560,058** | **35,247,935** |

## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

#### *4.1.1. Maximum Credit Risk Exposure (Continued)*

*Impaired Loans and Receivables*

Impaired loans and receivables are those for which the Bank has determined the existence of objective evidence of impairment and does not expect them to be collected in full amounts of principal and interest matured pursuant to the relevant loan agreements. Loans and receivables are impaired on both an individual and a group basis.

*Receivables Matured but not Impaired*

Loans and receivables matured but not impaired represent those loans and receivables where there is default in settling liabilities for contractually agreed interest or principal outstanding (the report shows the entire receivable amount as matured for any matured portion of principal or interest). The Bank believes that it is not appropriate to make impairment allowance for such receivables given that there is certainty of collection by the Bank.

*Receivables not Matured and not Impaired*

Loans and receivables not matured and not impaired are those determined as ineligible for impairment allowance given the probability of default status and certainty of collection by the Bank (loans and receivables due from the Republic of Serbia).

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

#### *4.1.1. Maximum Credit Risk Exposure (Continued)*

*Loans and receivables due from customers, banks and other financial institutions, not matured and not impaired*

December 31, 2014

| | Housing Loans | Cash Loans | Agricultural Loans | Other Loans | Micro Business | Total Retail | Corporate Customers | Total | Due from Banks |
|---|---|---|---|---|---|---|---|---|---|
| Low (IR 1, 2) | - | - | - | - | - | - | 2,313,323 | 2,313,323 | 27,510,292 |
| Medium (IR 3) | - | - | - | - | - | - | - | - | 22,935 |
| **Total** | **-** | **-** | **-** | **-** | **-** | **-** | **2,313,323** | **2,313,323** | **27,533,227** |

December 31, 2013

| | Housing Loans | Cash Loans | Agricultural Loans | Other Loans | Micro Business | Total Retail | Corporate Customers | Total | Due from Banks |
|---|---|---|---|---|---|---|---|---|---|
| Low (IR 1, 2) | - | - | - | - | - | - | 5,229,621 | 5,229,621 | 34,204,200 |
| Medium (IR 3) | - | - | - | - | - | - | 4,078,835 | 4,078,835 | 35,284 |
| **Total** | **-** | **-** | **-** | **-** | **-** | **-** | **9,308,456** | **9,308,456** | **34,239,484** |

*Loans and receivables due from customers, banks and other financial institutions*

December 31, 2014

| | Housing Loans | Cash Loans | Agricultural Loans | Other Loans | Micro Business | Total Retail | Corporate Customers | Total | Due from Banks |
|---|---|---|---|---|---|---|---|---|---|
| Up to 30 days past due | - | - | - | - | - | - | 1,375,310 | 1,375,310 | 7,204,378 |
| 31 - 90 days past due | - | - | - | - | - | - | - | - | - |
| Over 90 days past due | - | - | - | - | - | - | 181,996 | 181,996 | - |
| **Total** | **-** | **-** | **-** | **-** | **-** | **-** | **1,557,306** | **1,557,306** | **7,204,378** |

December 31, 2013

| | Housing Loans | Cash Loans | Agricultural Loans | Other Loans | Micro Business | Total Retail | Corporate Customers | Total | Due from Banks |
|---|---|---|---|---|---|---|---|---|---|
| Up to 30 days past due | - | - | - | - | - | - | 10,194,103 | 10,194,103 | 1,008,450 |
| 31 - 90 days past due | - | - | - | - | - | - | 73,340 | 73,340 | - |
| Over 90 days past due | - | - | - | - | - | - | 605,330 | 605,330 | - |
| **Total** | **-** | **-** | **-** | **-** | **-** | **-** | **10,872,773** | **10,872,773** | **1,008,450** |

## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

#### *4.1.2. Loans with Altered Initially Agreed Terms*

Loans with altered initially agreed terms are loans rescheduled and/or restructured due to the borrowers' difficulties in servicing liabilities as these fall due. Considering such difficulties, the Bank decides on altering the terms and deadlines stipulated by loan agreements giving the borrowers the opportunity to discharge liabilities more easily.

Rescheduling of receivables is performed for debtors with currently mismatching cash inflows and outflows, yet whose financial indicators have not deteriorates suggesting that the debtor will be able to settle the rescheduled liabilities according to the subsequently agreed repayment terms. Receivables are rescheduled if due from debtors up to 90 days in default, most commonly per individual loan subaccount, i.e. not including all the receivables due from the same debtor (not all loan subaccounts).

Restructuring is performed for loans due from debtors with significant problems in business where financial indicators are substantially deteriorating. Upon restructuring:

- All balance sheet receivables due from the debtor or a greater portion thereof are replaced;
- Terms whereunder the relevant receivable was approved are essentially altered (which particularly entails extension of the period for repayment of principal or interest, decrease in interest rate applied or the amount receivable and other modifications of terms which are to facilitate the position of a debtor);
- Adoption of an adequate financial consolidation program is mandatory.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

*4.1.2. Loans with Altered Initially Agreed Terms (Continued)*

The following table presents total amount of loans with altered initially agreed terms as of December 31,2014 and 2013. The stated values are presented in gross and net carrying amounts (after impairment effects).

*Loans with altered initially agreed terms, gross*

| | Rescheduled | | | | Restructured | | | |
|---|---|---|---|---|---|---|---|---|
| | December 31, 2014 | | December 31, 2013 | | December 31, 2014 | | December 31, 2013 | |
| | Gross | Net | Gross | Net | Gross | Net | Gross | Net |
| Housing loans | 596,943 | 556,173 | 568,206 | 532,674 | 145,546 | 137,391 | 84,024 | 71,652 |
| Cash loans | 224,193 | 210,710 | 198,795 | 188,299 | 40,721 | 28,648 | 43,887 | 32,549 |
| Agricultural loans | 64,211 | 55,919 | 137,523 | 123,176 | 32,673 | 29,229 | 41,370 | 36,647 |
| Other loans | 12,407 | 11,953 | 19,894 | 19,112 | 506 | 375 | 121 | - |
| Micro businesses | 200,575 | 188,381 | 256,623 | 215,083 | 401,880 | 341,390 | 428,898 | 389,271 |
| **Total retail** | **1,098,329** | **1,023,136** | **1,181,041** | **1,078,344** | **621,326** | **537,033** | **598,300** | **530,119** |
| Corporate customers | 23,582,662 | 23,058,599 | 26,507,514 | 26,076,310 | 16,995,750 | 12,581,987 | 12,004,182 | 7,412,417 |
| **Total** | **24,680,991** | **24,081,735** | **27,688,555** | **27,154,654** | **17,617,076** | **13,119,020** | **12,602,482** | **7,942,536** |

*Credit quality of loans and receivables (gross)*

| | December 31, 2014 | | | December 31, 2013 | | |
|---|---|---|---|---|---|---|
| | Loans and receivables | Rescheduled and restructured receivables | % | Loans and receivables | Rescheduled and restructured receivables | % |
| Not matured and not impaired | 2,313,323 | - | - | 9,308,456 | - | - |
| Matured but not impaired | 1,557,306 | - | - | 10,872,773 | - | - |
| Group-level impaired | 166,134,583 | 23,282,417 | 14.01% | 141,340,732 | 22,687,573 | 16.05% |
| Individually impaired | 38,456,800 | 19,015,650 | 49.45% | 34,868,679 | 17,603,464 | 50.49% |
| **Total** | **208,462,012** | **42,298,067** | **20.29%** | **196,390,640** | **40,291,037** | **20.52%** |
| **Impairment allowance** | **23,084,977** | **5,097,313** | **22.08%** | **18,830,581** | **5,193,847** | **27.58%** |
| Group-level impairment allowance | 12,095,209 | 401,437 | 3.32% | 12,423,635 | 2,349,655 | 18.91% |
| Individual impairment allowance | 10,989,768 | 4,695,876 | 42.73% | 6,406,946 | 2,844,192 | 44.39% |
| **Securitized with collaterals** | **180,511,165** | **35,538,202** | **19.69%** | **157,006,188** | **30,628,887** | **19.51%** |

**NOTES TO THE FINANCIAL STATEMENTS**
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## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

#### *4.1.3. Concentration Risk*

The Bank manages concentration risk by establishing a system of limits to the exposures with the same or similar risk factors (industry sectors/activities, product types, geographic regions, single entities or groups of related entities, collaterals...). Establishment of appropriate exposure limits is the basis for concentration risk control with the aim of loan portfolio diversification.

*Breakdown of loans and receivables due from customers, banks and other financial institutions and commitments per industry is provided below:*

| | Loans and receivables | | | | Off-balance sheet items | | | |
|---|---|---|---|---|---|---|---|---|
| | December 31, 2014 | | December 31, 2013 | | December 31, 2014 | | December 31, 2013 | |
| | Gross | Net | Gross | Net | Gross | Net | Gross | Net |
| **Finance and insurance sector** | 10,643,439 | 10,537,316 | 10,034,522 | 9,891,305 | 292,092 | 292,091 | 897,031 | 897,031 |
| **Corporate and public company sector** | 119,316,219 | 108,947,880 | 118,423,903 | 105,938,463 | 19,936,661 | 19,373,087 | 20,120,473 | 19,649,427 |
| Agriculture | 6,573,945 | 6,306,710 | 6,212,209 | 5,877,157 | 558,384 | 291,839 | 774,549 | 513,051 |
| Processing industry | 52,531,430 | 46,191,776 | 46,072,282 | 38,981,248 | 4,025,921 | 3,978,542 | 4,577,951 | 4,504,435 |
| Power industry | 6,329,773 | 6,329,319 | 8,783,688 | 8,783,265 | 921,693 | 921,592 | 781,666 | 781,586 |
| Construction industry | 4,738,069 | 4,348,898 | 4,849,182 | 4,307,481 | 7,488,399 | 7,376,936 | 4,325,512 | 4,274,384 |
| Wholesale and retail | 35,253,379 | 32,288,190 | 37,083,838 | 33,631,082 | 5,238,480 | 5,118,562 | 8,075,830 | 8,008,356 |
| Services industries | 11,572,132 | 11,290,458 | 12,858,509 | 11,921,957 | 962,197 | 950,536 | 823,166 | 813,958 |
| Real estate business | 2,317,491 | 2,192,529 | 2,564,195 | 2,436,275 | 741,587 | 735,080 | 761,799 | 753,657 |
| **Entrepreneurs** | 2,768,358 | 2,492,689 | 2,263,844 | 2,008,313 | 429,318 | 425,429 | 406,760 | 404,418 |
| **Public sector** | 10,943,750 | 10,912,080 | 13,555,594 | 13,525,198 | 339,888 | 338,928 | 72,843 | 72,833 |
| **Retail sector** | 65,592,670 | 62,989,218 | 58,568,927 | 56,432,896 | 8,652,116 | 8,652,116 | 8,567,239 | 8,567,239 |
| **Non-residents** | 17,215,508 | 16,870,780 | 21,183,663 | 20,882,595 | 105,098 | 105,098 | 635,722 | 635,722 |
| **Other customers** | 17,088,262 | 7,364,677 | 7,933,495 | 4,129,223 | 410,616 | 410,616 | 182,443 | 182,192 |
| **Total** | 243,568,206 | 220,114,640 | 231,963,948 | 212,807,993 | 30,165,789 | 29,597,365 | 30,882,511 | 30,408,862 |

Depending on general economic trends and individual industry sector trends, the Bank diversifies investments into the industry sectors that are resistant to the impact of adverse economic trends.

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## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

*4.1.3. Concentration Risk (Continued)*

*Breakdown of loans and receivables due from customers, banks and other financial institutions and commitments per geographic area is provided below:*

| | Loans and receivables | | | | Off-balance sheet items | | | |
|---|---|---|---|---|---|---|---|---|
| | December 31, 2014 | | December 31, 2013 | | December 31, 2014 | | December 31, 2013 | |
| | Gross | Net | Gross | Net | Gross | Net | Gross | Net |
| Serbia | 219,294,893 | 196,202,331 | 198,460,191 | 179,624,778 | 30,046,297 | 29,477,873 | 30,230,779 | 29,757,132 |
| Montenegro | 156,391 | 154,536 | 570,466 | 564,898 | 1,708 | 1,708 | 1,798 | 1,798 |
| Bosnia and Herzegovina | 756,552 | 756,216 | 523,055 | 522,747 | - | - | 344,290 | 344,290 |
| European Union | 14,803,936 | 14,801,605 | 15,550,455 | 15,547,960 | 64,244 | 64,244 | 191,827 | 191,827 |
| USA and Canada | 398,411 | 135,285 | 620,163 | 400,250 | 45,916 | 45,916 | 108,023 | 108,023 |
| Other countries | 8,158,023 | 8,064,667 | 16,239,618 | 16,147,361 | 7,624 | 7,624 | 5,794 | 5,792 |
| **Total** | **243,568,206** | **220,114,640** | **231,963,948** | **212,807,993** | **30,165,789** | **29,597,365** | **30,882,511** | **30,408,862** |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

#### *4.1.4. Financial Assets*

| | December 31, 2014 | | December 31, 2013 | |
|---|---|---|---|---|
| | Gross | Net | Gross | Net |
| **Financial assets:** | **95,774,547** | **95,654,325** | **57,195,947** | **57,150,504** |
| - at fair value through profit and loss, held for trading | 121,634 | 121,634 | 115,577 | 115,319 |
| - available for sale | 95,481,744 | 95,481,249 | 56,887,797 | 56,885,285 |
| - held to maturity | 171,169 | 51,442 | 192,573 | 149,900 |
| **Changes in fair value of risk-hedged items** | - | - | - | - |
| **Receivables per derivatives designated as risk hedging instruments** | - | - | - | - |
| **Total** | **95,774,547** | **95,654,325** | **57,195,947** | **57,150,504** |

Financial assets at fair value through profit and loss relate to the Republic of Serbia's old foreign currency savings bonds, corporate and bank shares and investment units. These assets are measured using the methodology of adjusting to the market prices (mark to market) or internally developed valuation models (mark to model), depending on the availability of daily changing prices or whether they are subject of continuous trading.

Available-for-sale financial assets represent financial instruments which are intended to be held over an indefinite time period and which may be sold for liquidity purposes, due to the movements in interest rates, exchange rates or prices of capital. They mostly comprise Treasury bills and bonds issued by the Republic of Serbia, United Kingdom, local municipalities and bonds of other banks. Available-for-sale assets are initially measured at cost, and on a quarterly basis fair value thereof is determined based on the market prices for securities traded in active stock exchange (mark to market). Internally developed valuation models (mark to model) are used in instances that for certain financial instruments independent sources of market information are not available, and are based on the maturity of the security and the risk-free interest rate level.

Financial assets held to maturity entirely relate to discounted bills of exchange

#### *4.1.5. Credit Risk Hedges (Collaterals)*

For the purpose of protection against credit risk, in addition to regular monitoring of the customer business operations, the Bank also acquires security instruments (collaterals) to secure the collection of receivables and minimize credit risk. The collateral quantity and type depend on the assessed credit risk.

As a standard type of loan security instrument, the Bank demands and receives from clients contractual authorizations for account withdrawals and bills of exchange, whereas, depending on the credit risk assessment and loan type, additional collaterals agreed upon include the following:

- for commercial loans – pledge liens instituted over movable assets and immovable property (mortgages), deposits, banking, corporate and state-issued guarantees, sureties, pledge liens instituted over securities, equity interests, receivables and livestock;
- for retail loans – mortgages, deposits, co-sureties and insurance of the National Corporation for Housing Loans.

## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

#### *4.1.5. Credit Risk Hedges (Collaterals) (Continued)*

For valuation of property or pledges assigned over movable assets, the bank hires certified appraisers in order to minimize potential risk of unrealistic valuation. Property, goods, equipment and other movables pledged must be insured by an insurance company acceptable to the Bank and insurance policies must be duly endorsed in favor of the Bank.

For protection against changes in the market value of collaterals (mortgages, pledge liens, securities, etc.) the appraised collateral value is adjusted for the predefined haircut percentage dependent on the type and location of collateral, which is reviewed at least annually, o more frequently, as appropriate. This is how the bank protects itself from potential losses arising from inability to collect its receivables from collateral foreclosure.

The Bank monitors and updates the values and trends in collaterals in order to minimize the risk of unrealistic valuation, if necessary, the bank may demand additional collateral in accordance with the executed loan agreements. Collaterals represent a secondary source of collection of receivables.

The following breakdowns present the value of collaterals as their fair values, only up to the loan gross amounts (in instances of collateral values exceeding the respective loan values). When collateral values are below the respective loan gross amounts, the values of collaterals are presented.

The values of collaterals and guarantees received to reduce credit risk exposures arising from the loans extended to customers are presented in the following table:

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

#### *4.1.5. Credit Risk Hedges (Collaterals) (Continued)*

**Loans and receivables due from customers secured with collaterals**

| | December 31, 2014 | | | | | December 31, 2013 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Properties | Deposits | Guarantees | Other collaterals | Total | Properties | Deposits | Guarantees | Other collaterals | Total |
| Housing loans | 30,748,217 | - | - | 4,867,522 | 35,615,739 | 28,503,974 | - | - | 2,523,140 | 31,027,114 |
| Cash loans | 97,639 | 274,274 | - | 3,242,179 | 3,614,093 | 110,319 | 265,752 | - | 1,463,046 | 1,839,117 |
| Agricultural loans | 2,849,789 | 16,463 | 73,816 | 1,321,095 | 4,261,163 | 2,328,436 | 44,270 | 72,414 | 728,305 | 3,173,425 |
| Other loans | 19,295 | 50,511 | - | 347,213 | 417,019 | 22,505 | 45,837 | - | 596,037 | 664,379 |
| Micro business | 2,494,280 | 464,556 | - | 4,846,869 | 7,805,705 | 2,875,782 | 475,741 | - | 2,528,028 | 5,879,551 |
| **Total retail loans** | **36,209,220** | **805,804** | **73,816** | **14,624,878** | **51,713,718** | **33,841,016** | **831,600** | **72,414** | **7,838,556** | **42,583,586** |
| Corporate loans | 58,205,326 | 1,100,476 | 8,680,492 | 60,811,153 | 128,797,447 | 70,472,795 | 1,113,839 | 9,426,051 | 33,409,917 | 114,422,602 |
| **Total** | **94,414,546** | **1,906,280** | **8,754,308** | **75,436,031** | **180,511,165** | **104,313,811** | **1,945,439** | **9,498,465** | **41,248,473** | **157,006,188** |

Note: A portion of housing loans secured with mortgages assigned over real estate properties is insured with the National Corporation for Housing Loans Insurance (2014: RSD 27.4 billion; 2013: RSD 25.5 billion).

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 4. RISK MANAGEMENT (Continued)

### 4.1. Credit Risk (Continued)

#### *4.1.5. Credit Risk Hedges (Collaterals) (Continued)*

The ratio of the loan amount to the appraised value of the property held as collateral is monitored as loan to value ratio (LTV ratio).

**Breakdown of housing loans per LTV ratio spread**

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Below 50% | 5,301,359 | 4,851,190 |
| From 50% to 70% | 7,787,807 | 6,595,698 |
| From 71% to 100% | 14,119,316 | 13,661,280 |
| From 101% to 150% | 5,510,500 | 4,211,155 |
| Above 150% | 2,368,052 | 1,203,805 |
| Other | 2,706,351 | 3,175,308 |
| **Total exposure** | **37,793,385** | **33,698,436** |
| **Average LTV ratio** | **70.07%** | **69.85%** |

#### *4.1.6. Tangible Assets Acquired in Lieu of Debt Collection*

Collaterals foreclosed by the Bank in the process of loan and receivable collection are provided below:

**Collaterals foreclosed**

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Residential premises | 204,802 | 279,216 |
| Business premises | 2,758,640 | 1,516,067 |
| Equipment | 106,469 | 101,805 |
| Land and forests | 155,737 | 71,722 |
| **Total** | **3,225,648** | **1,968,810** |
| Accumulated depreciation | (188,336) | (141,357) |
| **Net book value** | **3,037,312** | **1,827,453** |

In 2014, in the process of debt collection the bank foreclosed collaterals totaling RSD 2,313,063 thousand (2013: RSD 1,060,829 thousand).

### 4.2. Liquidity Risk

Liquidity risk represents the risk of negative effects on the Bank's financial result and equity resulting from the Bank's difficulty or inability to settle its matured liabilities in instances of insufficient liquidity reserves and inability to cover for unexpected outflows and other liabilities.

The Bank operates in accordance with the basic principles of liquidity, maintaining a sufficient level of funds to cover liabilities incurred in the short term, i.e. it observes the principle of solvency by establishing the optimal financial leverage and sufficient liquidity reserves which do not compromise realization of the projected return on equity.

## 4. RISK MANAGEMENT (Continued)

### 4.2. Liquidity Risk (Continued)

Liquidity risk is manifest as the mismatch of the inflow of assets on one end and the maturities of liabilities on the other, including the possibility of delays in expected inflows as well as that of unexpected outflows. Liquidity risk may be manifest as the risk related to sources of funds and market liquidity risk. The problem of liquidity in respect of the sources of funds relates to the structure of liabilities and is expressed through potential significant share of unstable and short-term sources of funds or their concentration. On the other hand, liquidity risk is reflected in reserves deficiency and difficulty or inability to obtain liquid assets at reasonable market prices.

The Bank has established appropriate organizational structure, which allows for clear differentiation between the process of assuming and the process of managing liquidity risk. The Asset and Liability Management Committee and Liquidity Committee have the most significant role therein as well as other competent boards/committees, whose decisions can impact the Bank's exposure to this risk.

In order to minimize liquidity risk, the Bank:

- Diversifies sources of assets in respect to their currencies and maturities;
- Forms sufficient liquidity reserves;
- Manages monetary funds;
- Monitors future cash flows and liquidity levels on a daily basis;
- Limits principal sources of credit risk with most significant impact on liquidity; and
- Defines and periodically tests Plans for Liquidity Management in Crisis Situations.

The liquidity management process comprises identification, measurement, minimizing, monitoring, control and liquidity risk reporting.

In identifying liquidity risk, the Bank identifies in a comprehensive and timely manner the causes that lead to the occurrence of liquidity risk determines current liquidity risk exposure as well as liquidity risk exposure arising from new business products and activities.

Measurement and assessment of liquidity risk in the Bank is performed through quantitative and/or qualitative assessment of identified liquidity risk by using the following techniques:

- GAP analysis;
- Ratio analysis; and
- Stress test.

Minimizing liquidity risk consists of maintaining this risk at a level that is acceptable to the Bank's risk profile through definition of the system of exposure limits including both internal and statutory limits and timely implementation of measures to mitigate the risk and operation within the set internal and external limits.

Control and monitoring of liquidity risk includes the process of monitoring compliance with internally defined limits, and monitoring of defined measures for reducing the bank's exposure to liquidity risk. Liquidity risk control involves the control at all liquidity risk management levels as well as the independent control system implemented by the bank's organizational units responsible for internal audit and compliance monitoring.

Liquidity risk reporting consists of internal and external reporting systems and is performed on a daily basis and a set schedule according to the defined system. .

The Bank's operations are reconciled daily with legally prescribed liquidity ratio as follows: minimum 0.8 for one working day; minimum 0.9 for no longer than three consecutive working days and minimum 1 as the average liquidity ratio for all working days in a month. The Bank also monitors compliance with the regulatory prescribed rigid/cash liquidity ratio as follows: minimum 0.5 for one working day; minimum 0.6 for no longer than three consecutive working days and minimum 0.7 as the average liquidity ratio for all working days in a month.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 4. RISK MANAGEMENT (Continued)

### 4.2. Liquidity Risk (Continued)

**Compliance with liquidity ratio limits externally prescribed:**

| | Liquidity Ratio 2014 | Liquidity Ratio 2013 | Rigid/Cash Liquidity Ratio 2014 | Rigid/Cash Liquidity Ratio 2013 |
|---|---|---|---|---|
| As at December 31 | 2.84 | 3.45 | 2.52 | 3.08 |
| Average for the period | 3.29 | 2.73 | 2.88 | 2.43 |
| Maximum for the period | 4.40 | 3.89 | 4.09 | 3.39 |
| Minimum for the period | 1.70 | 1.69 | 1.51 | 1.50 |

During 2014 the Bank's liquidity ratio and cash liquidity ratio were both well above the prescribed limits.

The Bank sets internal limits, based on the internal reporting on liquidity GAP for all balance sheet components.

**Compliance with last day liquidity ratio limits internally defined:**

| | Limits | 2014 | 2013 |
|---|---|---|---|
| GAP up to 1 month / Total assets | Max (10%) | 10.93% | 10.42% |
| Cumulative GAP up to 3 months / Total assets | Max (20%) | 12.08% | 6.75% |

In addition, the Bank limits and coordinates its operations with the limits defined for maturity per major foreign currencies.

**Maturity structure of monetary assets and monetary liabilities as of December 31, 2014**

| | Up to 1 month | From 1 - 3 months | From 3 -12 months | From 1 - 5 years | Over 5 years | Total |
|---|---|---|---|---|---|---|
| Cash and cash funds held with the central bank | 68,547,389 | - | - | - | - | 68,547,389 |
| Loans and receivables due from banks and other financial institutions | 34,501,291 | - | - | 236,314 | - | 34,737,605 |
| Loans and receivables due from customers | 35,403,685 | 11,911,181 | 48,217,308 | 55,461,224 | 34,383,637 | 185,377,035 |
| Financial assets (securities) | 10,804,439 | 9,710,565 | 24,456,167 | 42,389,721 | 8,293,433 | 95,654,325 |
| Other assets | 2,356,289 | - | 573,664 | 2,476 | - | 2,932,429 |
| **Total** | **151,613,093** | **21,621,746** | **73,247,139** | **98,089,735** | **42,677,070** | **387,248,783** |
| Deposits and other liabilities due to banks, other financial institutions and the central bank | 6,716,656 | 476,967 | 3,324,780 | 11,133,250 | 2,091,365 | 23,743,018 |
| Deposits and other liabilities due to customers | 145,966,665 | 27,209,991 | 87,116,252 | 39,314,095 | 2,347,908 | 301,954,911 |
| Subordinated liabilities | (11,235) | - | - | 6,047,915 | - | 6,036,680 |
| Other liabilities | 2,710,826 | - | 256,460 | - | - | 2,967,286 |
| **Total** | **155,382,912** | **27,686,958** | **90,697,492** | **56,495,260** | **4,439,273** | **334,701,895** |
| **Net liquidity gap** | | | | | | |
| **As of December 31, 2014** | **(3,769,819)** | **(6,065,212)** | **(17,450,353)** | **41,594,475** | **38,237,797** | **52,546,888** |
| **As of December 31, 2013** | **17,587,646** | **(15,002,185)** | **(29,496,029)** | **42,691,974** | **32,561,801** | **48,343,207** |

The report on the maturity structure of monetary assets and liabilities includes monetary balance sheet items distributed according to maturities outstanding, i.e. the conservative assumption was used that all transaction and demand deposits will be withdrawn within one month.

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## 4. RISK MANAGEMENT (Continued)

### 4.2. Liquidity Risk (Continued)

The Bank collects deposits of corporate and retail customers which commonly have shorter maturity periods and can be withdrawn at the client request. Short-term nature of such deposits increases the bank's liquidity risk and requires active liquidity risk management and constant monitoring of market trends.

In near term, the Bank manages liquidity risk by monitoring and controlling items in all major currencies in order to identify the needs for additional funding in a timely manner in case of maturities of certain items, i.e. in the long term, the Bank plans the structure of its funding sources and investments in order to provide sufficient stable funding sources and liquidity reserves.

The Bank's management believes that adequate diversification of the deposit portfolio per number and type of depositors as well as historical experience provide a solid basis for existence of a stable and long-term deposit base, i.e. no significant outflow of funds is expected thereof.

The Bank regularly tests the Plans for Liquidity Management in Crisis Situations which are intended for testing potential crisis, checks the survival period and solvency, availability of funding for liabilities that could arise and assesses the support under the assumed crisis conditions.

**Undiscounted cash flows from monetary assets and monetary liabilities as of December 31, 2014**

| | Up to 1 month | From 1 - 3 months | From 3 -12 months | From 1 - 5 years | Over 5 years | Total |
|---|---|---|---|---|---|---|
| Cash and cash funds held with the central bank | 68,547,389 | - | - | - | - | 68,547,389 |
| Loans and receivables due from banks and other financial institutions | 40,816,045 | - | - | 268,225 | - | 41,084,270 |
| Loans and receivables due from customers | 36,421,274 | 13,938,739 | 55,306,004 | 71,228,553 | 48,350,757 | 225,245,327 |
| Financial assets (securities) | 11,232,816 | 10,436,803 | 26,171,255 | 46,008,849 | 8,631,016 | 102,480,739 |
| Other assets | 2,356,289 | - | 573,664 | 2,476 | - | 2,932,429 |
| **Total** | **159,373,813** | **24,375,542** | **82,050,923** | **117,508,103** | **56,981,773** | **440,290,154** |
| Deposits and other liabilities due to banks, other financial institutions and the central bank | 6,717,593 | 583,864 | 3,749,007 | 12,111,956 | 2,337,061 | 25,499,481 |
| Deposits and other liabilities due to customers | 146,312,504 | 27,628,455 | 89,937,195 | 43,111,370 | 2,562,758 | 309,552,282 |
| Subordinated liabilities | (11,235) | - | - | 6,660,934 | - | 6,649,699 |
| Other liabilities | 2,710,826 | - | 256,460 | - | - | 2,967,286 |
| **Total** | **155,729,688** | **28,212,319** | **93,942,662** | **61,884,260** | **4,899,819** | **344,668,748** |
| **Net liquidity gap** | | | | | | |
| **As of December 31, 2014** | **3,644,125** | **(3,836,777)** | **(11,891,739)** | **55,623,843** | **52,081,954** | **95,621,406** |
| **As of December 31, 2013** | **17,807,042** | **(14,524,891)** | **(28,776,753)** | **43,779,085** | **32,943,301** | **51,227,784** |

Undiscounted cash flows arising from the items of monetary assets and monetary liabilities include future cash flows per balance sheet items and future interest. In the case of transaction deposits and demand deposits, which, observing the conservative approach, are categorized into deposits with maturities of up to a month, the undiscounted cash flows include only the cash flows from the debt principal outstanding.

## 4. RISK MANAGEMENT (Continued)

### 4.3. Market Risk

Market risk represents the possibility of occurrence of negative effects on the Bank's financial result and equity due to changes in market variables and comprises interest rate risk, currency risk for all business operations and price risk for all items in the trading book.

The Bank is exposed to price risk, interest rate risk, currency risk, counterparty risk and risk of settlement related to trading book items. The trading book contains balance sheet and off-balance sheet assets and liabilities related to financial instruments that the Bank holds for trading or to hedge other financial instruments that are maintained in the trading book.

The Bank has established appropriate organizational structure, which allows for clear differentiation between the process of assuming market risks and the process of managing those risks. The Asset and Liability Management Committee (ALCO) and Investment Committee have the most significant role therein as well as other competent boards/committees, whose decisions can impact the Bank's exposure to this risk.

#### *4.3.1. Interest Risk*

Interest rate risk represents the probability of negative effects on the Bank's financial result and equity through items of the banking general ledger due to adverse interest rate fluctuations. The exposure to this risk depends on the relation between the interest rate sensitive assets and liabilities.

The Bank manages the following types of interest rate risk:

- Repricing risk of temporal mismatch between maturity and repricing;
- Yield curve risk – to which the Bank is exposed due to changes in yield curve shape;
- Basis risk – to which the Bank is exposed due to different reference interest rates for interest rate sensitive items with similar maturity or repricing characteristics; and
- Optionality risk – to which the Bank is exposed due to contractually agreed optional terms – loans with an option of early repayment, deposits with an option of early withdrawal, etc.

The basic objective of interest rate risk management is maintaining the acceptable level of interest rate risk exposure from the aspect of the effect on the financial result, by conducting adequate policy of matching periods of interest rate repricing, matching adequate sources to investments per interest rate type and maturity, as well as projecting movements in the yield curve in both foreign and domestic markets. Primarily, the Bank manages the internal yield margin through the prices of loans and deposits, focusing on the interest rate margin.

The Bank particularly considers the effects of interest rate changes and changes in the structure of interest-bearing assets and liabilities from the perspective of maturity, interest rate repricing and currency structure and manages the effect thereof on the economic value of equity.

The process of interest rate risk management consists of identification, measurement, minimizing, monitoring, control and interest rate risk reporting.

Identification of interest rate risk consists of comprehensive and timely identification of the causes and factors that lead to the occurrence of interest rate risk, which includes determining current interest rate risk exposure, as well as interest rate risk exposure arising from new business products and activities.

Measurement and assessment of interest rate risk at the Bank is performed through quantitative and/or qualitative assessment of identified interest rate risk by using the following techniques:

- GAP analysis;
- Ratio analysis;
- Duration;
- Economic value of equity; and
- Stress test.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 4. RISK MANAGEMENT (Continued)

### 4.3. Market Risk (Continued)

#### *4.3.1. Interest Risk (Continued)*

Minimizing interest rate risk means maintaining this risk at a level that is acceptable for the Bank's risk profile. Alleviating interest rate risk refers to the process of defining the systems of limited exposure of the Bank to the interest rate risk and implementing measures for interest rate risk mitigation.

Control and monitoring of interest rate risk entails the process of monitoring compliance with the established system of limits as well as monitoring defined measures for reducing the Bank's exposure to the interest rate risk. Control of interest rate risk refers to control on all management levels as well as an independent control system implemented by the organizational units responsible for internal audit and compliance monitoring.

Interest rate risk reporting consists of an internal system of reporting to competent boards/committees and the Bank's interest rate risk management bodies.

Internal limits are determined based on the internal report on the interest rate GAP, which includes all the balance sheet items.

**Compliance with internally defined interest rate risk limits at the last day was as follows:**

| | Limits | 2014 | 2013 |
|---|---|---|---|
| Relative GAP | Max 15% | 0.69% | (3.66%) |
| Mismatch ratio | 0.75 – 1.25 | 1.01 | 0.95 |

During 2014 the Bank's interest rate risk ratios were within internally prescribed limits.

The Bank has defined internal limits for interest rate risk exposure per major currency as well as the limit of the maximum economic value of equity.

**Compliance with internally defined limits of economic value of equity:**

| | 2014 | 2013 |
|---|---|---|
| As at December 31 | 8.50% | 5.20% |
| Average for the year | 8.06% | 5.98% |
| Maximum for the year | 10.86% | 7.45% |
| Minimum for the year | 4.82% | 4.78% |
| Limit | 20% | 20% |

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## 4. RISK MANAGEMENT (Continued)

### 4.3. Market Risk (Continued)

*4.3.1. Interest Risk (Continued)*

The exposure to interest rate risk can be reviewed through the Report on Interest Rate GAP in monetary assets and liabilities as follows:

**The Report on Interest Rate GAP in monetary assets and liabilities as of December 31, 2014:**

| | Up to 1 Month | From 1 - 3 Months | From 3 -12 Months | From 1 - 5 Years | Over 5 Years | Interest-Bearing | Non-Interest Bearing | Total |
|---|---|---|---|---|---|---|---|---|
| Cash and cash funds held with the central bank | 26,851,647 | - | - | - | - | 26,851,647 | 41,695,742 | 68,547,389 |
| Loans and receivables due from banks and other financial institutions | 33,780,001 | - | - | - | - | 33,780,001 | 957,604 | 34,737,605 |
| Loans and receivables due from customers | 90,548,334 | 15,341,940 | 42,720,426 | 16,077,662 | 16,509,149 | 181,197,511 | 4,179,524 | 185,377,035 |
| Financial assets (securities) | 11,934,760 | 19,667,235 | 17,413,798 | 36,993,447 | 8,187,593 | 94,196,833 | 1,457,492 | 95,654,325 |
| Other assets | - | - | - | - | - | - | 2,932,429 | 2,932,429 |
| **Total** | **163,114,742** | **35,009,175** | **60,134,224** | **53,071,109** | **24,696,742** | **336,025,991** | **51,222,791** | **387,248,783** |
| Deposits and other liabilities due to banks, other financial institutions and the central bank | 6,692,000 | 6,161,241 | 10,850,418 | 35,859 | 3,500 | 23,743,018 | - | 23,743,018 |
| Deposits and other liabilities due to customers | 155,202,029 | 24,083,955 | 82,952,118 | 36,617,677 | - | 298,855,779 | 3,099,132 | 301,954,911 |
| Subordinated liabilities | - | - | 6,036,680 | - | - | 6,036,680 | - | 6,036,680 |
| Other liabilities | - | - | - | - | - | - | 2,967,286 | 2,967,286 |
| **Total** | **161,894,029** | **30,245,196** | **99,839,216** | **36,653,536** | **3,500** | **328,635,477** | **6,066,418** | **334,701,895** |
| **Interest rate GAP:** | | | | | | | | |
| **- at December 31, 2014** | **1,220,713** | **4,763,979** | **(39,704,993)** | **16,417,573** | **24,693,242** | **7,390,515** | **45,156,373** | **52,546,888** |
| **- at December 31, 2013** | **4,146,816** | **(4,416,038)** | **(42,932,674)** | **8,448,556** | **21,414,967** | **(13,338,373)** | **61,681,580** | **48,343,207** |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 4. RISK MANAGEMENT (Continued)

### 4.3. Market Risk (Continued)

#### *4.3.1. Interest Risk (Continued)*

Interest rate risk GAP report of monetary sub-balance includes monetary balance items distributed according to the shorter of period of interest rate repricing and maturity outstanding. In accordance with the aforesaid, the conservative assumption is used that all transactions and demand deposits will be withdrawn within one month.

The Bank's management believes that appropriate matching of items per interest rate type and interest rate repricing period constitutes a solid prerequisite for existence with required financial results achieved and maintenance of economic value of equity.

*Risk of interest rate changes*

In addition to the GAP analyses, interest rate risk management also entails monitoring the sensitivity of the Bank's assets and liabilities to different scenarios of changes in interest rates. The Bank performs regular interest rate risk stress testing to assess the estimated impact of the changes in the key factors on the Bank's interest rate risk.

In scenario modelling, in addition to the changes in interest rates, particular consideration is given to the impact of early deposit withdrawal and early loan repayment, which the Bank estimates based on historical trends and expert estimates. The Bank estimated trends with regard to transaction deposits, demand deposits and savings deposits of retail customers using time series statistical modeling.

The standard scenario entails parallel changes (increases and decreases) in the interest rate by 100 basis points (b.p.). The Bank's sensitivity analysis, i.e. impact on the Bank's financial performance of the increase/decrease in the interest rates assuming symmetrical movement in yield curves and constant financial position is presented in the table below:

| | **Parallel increases by 100 b.p.** | **Parallel decreases by 100 b.p.** |
|---|---|---|
| **2014** | | |
| As at December 31 | 413,081 | (413,081) |
| Average for the year | 295,375 | (295,375) |
| Maximum for the year | 413,081 | (413,081) |
| Minimum for the year | 177,670 | (177,670) |
| **2013.** | | |
| As at December 31 | 376,389 | (376,389) |
| Average for the year | 341,589 | (341,589) |
| Maximum for the year | 376,389 | (376,389) |
| Minimum for the year | 306,788 | (306,788) |

#### *4.3.2. Currency Risk*

Currency risk represents the possibility of negative effects on the Bank's financial result and equity due to fluctuations in exchange rates between currencies, fluctuations in the domestic currency with respect to foreign currencies or changes in the value of gold and other precious metals. All items in the banking book and the trading book that are denominated in a foreign currency and gold, including dinar items indexed to foreign currency clause are exposed to currency risk.

In order to minimize the currency risk exposure, the Bank diversifies the currency structure of its portfolio and currency structure of liabilities, reconciling open positions in certain currencies pursuant to the principles of maturity transformation.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 4. RISK MANAGEMENT (Continued)

### 4.3. Market Risk (Continued)

#### 4.3.2. *Currency Risk (Continued)*

The Bank has established appropriate organizational structure, which allows for clear differentiation between the process of assuming currency risk and the process of managing currency risk. The Asset and Liability Management Committee has the most significant role therein as well as other competent boards/committees, whose decisions can impact the Bank's exposure to this risk.

The process of currency risk management entails identifying, measuring, minimizing, monitoring, control and currency risk reporting.

In identifying currency risks, the Bank identifies in a comprehensive and timely manner the causes that lead to emergence of currency risk and includes the determination of current currency risk exposure, as well as currency risk exposure resulting from new business products and activities.

Measurement and assessment of currency risk in the Bank is performed through quantitative and/or qualitative assessment of identified currency risk by using the following techniques:

- GAP analysis and currency risk ratio;
- VaR analysis;
- Stress test;
- Back testing.

Relieving foreign currency risk entails maintenance of risk at an acceptable level for the Bank's risk profile through the establishment of a transparent system of limits and defining measures used to mitigate foreign currency risk.

Control and monitoring of the currency risk consists of observation and supervision of compliance with internally and externally defined limits as well as monitoring of defined and implemented measures. Continuous monitoring and control of foreign currency risk during the day ensures timely undertaking measures for the purpose of maintaining the currency risk within defined limits. Foreign currency risk control means control at all management levels as well as independent control system implemented by the organizational units responsible for internal audit and compliance monitoring.

Reporting on currency risk includes internal and external reporting systems. It is performed on a daily basis.

The Bank reconciles its business operations with the prescribed foreign currency risk ratio, which represents the ratio between the total net foreign currency balance and the position of gold relative to the Bank's regulatory capital.

**Breakdown of the total currency risk balance and legally defined currency risk ratio at December 31:**

| | 2014 | 2013 |
|---|---|---|
| Total currency risk balance | 938,820 | 720,703 |
| Currency risk ratio | 2.90% | 2.12% |
| Legally-defined limit | 20% | 20% |

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*All amounts expressed in thousands of RSD, unless otherwise stated.*

**4. RISK MANAGEMENT (Continued)**

**4.3. Market Risk (Continued)**

*4.3.2. Currency Risk (Continued)*

**Breakdown of Monetary Assets and Monetary Liabilities per Currencies as of December 31, 2014**

| | EUR | USD | CHF | Other Currencies | FX Total | Currency Clause EUR | Currency Clause USD | Currency Clause u CHF | RSD Items | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| Cash and cash funds held with the central bank | 40,085,327 | 128,877 | 394,499 | 281,353 | **40,890,056** | - | - | - | 27,657,333 | **68,547,389** |
| Loans and receivables due from banks and other financial institutions | 20,953,667 | 1,582,913 | 878,900 | 975,426 | **24,390,906** | - | - | - | 10,346,699 | **34,737,605** |
| Loans and receivables due from customers | 12,521,795 | 72,317 | - | - | **12,594,112** | 112,635,073 | - | 5,717,903 | 54,429,947 | **185,377,035** |
| Financial assets (securities) | 52,112,935 | 6,534,761 | 1,397,811 | 326,704 | **60,372,211** | 512,557 | - | - | 34,769,557 | **95,654,325** |
| Other assets | 1,256,445 | 407,356 | 183 | 37 | **1,664,021** | | - | - | 1,268,408 | **2,932,429** |
| **Total** | **126,930,169** | **8,726,224** | **2,671,393** | **1,583,520** | **139,911,306** | **113,147,630** | **-** | **5,717,903** | **128,471,944** | **387,248,783** |
| Deposits and other liabilities due to banks, other financial institutions and the central bank | 18,603,718 | 210,878 | 25,283 | 27,901 | **18,867,780** | 119,572 | - | - | 4,755,666 | **23,743,018** |
| Deposits and other liabilities due to customers | 210,386,406 | 7,442,589 | 8,256,064 | 1,419,632 | **227,504,691** | 3,656,178 | 690,265 | 2,475 | 70,101,302 | **301,954,911** |
| Subordinated liabilities | 6,036,680 | - | - | - | **6,036,680** | - | - | - | - | **6,036,680** |
| Other liabilities | 532,668 | 326,794 | 33,526 | 46,951 | **939,939** | - | - | - | 2,027,347 | **2,967,286** |
| **Total** | **235,559,472** | **7,980,261** | **8,314,873** | **1,494,484** | **253,349,090** | **3,775,750** | **690,265** | **2,475** | **76,884,315** | **334,701,895** |
| **Net currency position** | | | | | | | | | | |
| **- December 31, 2014** | **(108,629,303)** | **745,963** | **(5,643,480)** | **89,036** | **(113,437,784)** | **109,371,880** | **(690,265)** | **5,715,428** | **51,587,630** | **52,546,888** |
| **- December 31, 2013** | **(115,195,557)** | **64,250** | **(5,686,296)** | **57,151** | **(120,760,452)** | **114,477,937** | **(56,633)** | **5,703,061** | **48,979,294** | **48,343,207** |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 4. RISK MANAGEMENT (Continued)

### 4.3. Market Risk (Continued)

*4.3.2. Currency Risk (Continued)*

**Ten-Day VaR**

The Bank also conducts currency risk stress testing to estimate the potential effects of specific events and/or changes in more than one financial variable on the Bank's financial result, capital and the currency risk ratio.

The VaR represents the highest possible loss in the Bank's portfolio during a specified period with a predefined confidence interval. The Bank calculates a one day and a ten day VaR, with a 99% confidence interval for foreign currency positions (currency VaR). In order to estimate the regulatory capital adequacy requirements regarding currency risk, the Bank calculates the VaR by using the generalized autoregressive-conditional heteroskedastic (GARCH) model for which it did not request approval from the National Bank of Serbia.

Currency VaR is calculated for foreign currency items as well as currency clause-indexed RSD items in both the banking book and trading book.

The breakdown of ten-day VaR with confidence interval of 99% for 2014 and 2013 is presented in the table below:

| | As of December 31 | Average | Maximum | Minimum |
|---|---|---|---|---|
| 2014 | | | | |
| Currency risk | 45,478 | 8,712 | 59,862 | 610 |
| 2013 | | | | |
| Currency risk | 5,551 | 24,391 | 117,205 | 538 |

### 4.4. Operational Risk

Operational risk represents the possibility of negative effects on the Bank's financial result and equity due to employee errors (intentional or accidental), inadequate procedures and processes in the Bank, inadequate management of information and other systems in the Bank, as well as occurrence of unforeseen external events. Operational risk includes legal risk.

Operational risk is defined as an event that occurred as the result of inappropriate or unsuccessful internal processes, employee and system actions or system and other external events, internal and external abuses, hiring and security practices at the workplace, customer receivables, product distribution, fines and penalties for infractions, damage incurred to property, disruptions in operations and system errors and process management.

The Bank monitors operational risk events according to the following business lines: corporate financing, trade and sales, retail brokerage services, corporate banking, retail banking, payment transfers, agency services and asset management.

The process of operational risk management represents an integral part of the Bank's activities conducted on all levels and ensures identification, measuring, relieving, monitoring and reporting continually on operational risks ahead of their realization, as in accordance with the legal requirements and deadlines. The existing process relies on known methods of measuring operational risk exposures, database on operating losses, an updated control and reporting system.

## 4. RISK MANAGEMENT (Continued)

### 4.4. Operational Risk (Continued)

The Bank monitors operational risk events daily and manages operating risks. For the purpose of efficient operational risk monitoring, the Bank appoints employees who are in charge of operational risk with the objective of monitoring operational risk in its every organizational part, where such employees are responsible for accuracy and timeliness of information about all operational risk events that occur in their organizational unit, as well as for keeping records about all such events in the operational risk database. The organizational part of the Bank which is responsible for risk management monitors and reports operational risks to the Bank's Board of Directors, the Bank's Executive Board and the Audit Committee.

Measurement and assessment of operational risk at the Bank is done through quantitative and/or qualitative assessment of identified operational risk. The Bank measures operational risk exposure through event records, self-assessment and stress testing. Self-assessment consists of assessment of risk exposure by organizational units based on the roadmap for identifying operating risks, through measurement of potential ranges and frequencies of events that can result in losses, identification of levels of control that business areas must maintain over these risks and measures of improvement. Stress test represents an operational risk management technique which is used to assess potential effects of specific events and/or changes in several financial variables on the Bank's exposure to operational risk.

The Bank cannot eliminate all operational risks, but by introducing a rigorous framework of control, monitoring and response to potential risks it is capable of managing these risks. The Bank takes measures in order to relieve operational risks and ensure proactive response to events potentially creating operational risks through continued monitoring of all activities, application of adequate and reliable information system and by applying project approach orientation, the implementation of which helps improve the business practice and optimize the Bank's business processes.

Through reliable reporting on the implementation of measures undertaken to mitigate operational risks, the Bank has established a system for monitoring the activities undertaken by the Bank's organizational parts in order to reduce arising operational risks. The Bank assess the risk of entrusting third parties with activities related to the Bank's operations and based on the service contracts executed with such third parties which clearly define terms, rights, obligations and responsibilities of the contracting parties.

With the objective of smooth and continued operation of all significant systems and processes in the Bank, and to limit losses that could be incurred in extraordinary circumstances, the Bank adopted the Business Continuity Plan, in order to ensure the restoration and recovery of the information technology systems in the event of interruption or stoppage of operations, the Bank adopted the Disaster Recovery Plan.

### 4.5. The Bank's Investment Risks

The Bank's investment risk relates to the risk of investing in other entities and capital expenditures. The Bank's investments in a non-financial sector entity cannot exceed 10% of the Bank's equity, whereby such investments entail investments through which the Bank acquires equity interest or shares in a non-financial sector entity. The total Bank's investment in non-financial sector entities and Bank's own fixed assets cannot exceed 60% of the Bank's equity, but this restriction does not apply to the acquisition of shares for further trading and sales thereof within six months from the acquisition date.

## 4. RISK MANAGEMENT (Continued)

### 4.6. Exposure Risk

Large exposures of the Bank to a single entity or a group of related entities, including Bank's related parties, are exposures amounting to over 10% of the Bank's capital.

In its operations, the Bank takes care of the compliance with statutory exposure limits:

- The Bank's exposure to a single entity or a group of related entities cannot exceed 25% of the Bank's equity;
- The Bank's exposure to a party that is related to the Bank cannot exceed 5% of the Bank's equity, while total exposure to the Bank's related parties cannot exceed 20% of the Bank's equity;
- The aggregate amount (sum) of the Bank's large exposures cannot exceed 400% of the Bank's equity.

The Bank's exposure to a single party or a group of related parties, as well as exposure to the Bank's own related parties, were within the prescribed limits.

### 4.7. Country Risk

Country risk relates to the risk of the country of origin of the entity the Bank is exposed to, i.e. the possibility of negative effects on the Bank's financial result and equity due to inability to collect receivables from abroad and is caused by political, economic and social conditions in the borrower's country of origin. Country risk includes the following risks:

- Political and economic risk relates to the likelihood of losses due to the inability to collect the Bank's receivables because of deterioration in macroeconomic stability, due to limitations prescribed by government regulations or due to other structural changes in the economy of the given country;

- Transfer risk relates to the probability of losses due to the inability to collect receivables in a currency which is not the official currency in the borrower's country of origin, due to limitations to liability settlement toward creditors from other countries in specific currency that is predetermined by the official state regulations and bylaws of state and other bodies of the borrower's country of origin.

Management of country risk is made per individual loans and receivables and at the Bank's portfolio level. Measurement of exposure of an individual receivable to country risk is based on the country rating of the Bank's borrower's country of origin as defined by internationally recognized agencies, while measurement of portfolio exposure to country risk is based on setting limits to exposure in terms of a percentage of the Bank's equity, depending on the internal country rating category. The Bank measures and controls portfolio exposure to country risk by grouping receivables by default level of risk of the borrower countries of origin.

For the purpose of adequate country risk control, the Bank defines exposure limits individually per borrower country of origin.

The Bank's loans approved to the borrowers domiciled outside of the Republic of Serbia for financing businesses in the Republic of Serbia, whose financial liabilities to the Bank are expected to be settled from the operating results achieved in the Republic of Serbia, represent the Bank's receivables without exposure to the risk of the borrower country of origin.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 4. RISK MANAGEMENT (Continued)

### 4.8. Fair Value of Financial Assets and Liabilities

*4.8.1. Breakdown of carrying values and fair values of financial assets and liabilities other than measured at fair value*

| | December 31, 2014 | | | | | December 31, 2013 | |
|---|---|---|---|---|---|---|---|
| | Carrying value | Fair value | Level 1 | Level 2 | Level 3 | Carrying value | Fair value |
| **Financial assets** | | | | | | | |
| Loans and receivables due from customers | 185,377,035 | 184,544,586 | | | 184,544,586 | 177,560,058 | 176,513,004 |
| Investment securities held to maturity | 51,442 | 51,442 | | | 51,442 | 149,900 | 149,900 |
| **Financial liabilities** | | | | | | | |
| Deposits and other liabilities due to customers | 301,954,911 | 301,788,878 | | | 301,788,878 | 266,020,289 | 265,858,821 |

Fair values of loans and receivables due from customers are estimated using the discounted cash flows model in instances of loans and receivables at fixed interest rates. Discounts rates are based on the current market interest rates applied to instruments offered under similar terms to borrowers with similar credit ratings. In addition, liabilities due to customers with defined maturities and contracted at fixed interest rates are discounted taking into account the prevailing terms according to the deposit types, terms and maturities.

Loans that are no longer approved and cannot be approved (loans indexed to CHF) are discounted at the same interest rates. In addition, loans approved at fixed interest rates subsidized by the Government were discounted at the same rate since the Bank would not have approved loans at low interest rates had the Government not subsidized portion of the interest rate. All loans and receivables approved at variable interest rates were approved in accordance with the prevailing market terms and the Bank's Business Policy.

Fair values of investment securities held to maturity are estimated using market prices or the discounted cash flows model based on current market interest rates applied to similar product instruments offered. Investment securities held to maturity have all matured resulting in the carrying values being equal to their fair values.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 4. RISK MANAGEMENT (Continued)

### 4.8. Fair Value of Financial Assets and Liabilities (Continued)

*4.8.2. Financial instruments measured at fair value*

| | Level 1 | Level 2 | Level 3 | December 31, 2014 Total assets / liabilities at fair value |
|---|---|---|---|---|
| **Assets** | | | | |
| Financial assets at fair value through profit and loss | 121,634 | - | - | 121,634 |
| Securities available for sale (RSD) | - | 35,179,215 | - | 35,179,215 |
| Securities available for sale (FX) | - | 60,302,034 | - | 60,302,034 |
| **Total** | **121,634** | **95,481,249** | **-** | **95,602,883** |

| | Level 1 | Level 2 | Level 3 | December 31, 2013 Total assets / liabilities at fair value |
|---|---|---|---|---|
| **Assets** | | | | |
| Financial assets at fair value through profit and loss | 115,319 | | - | 115,319 |
| Securities available for sale (RSD) | - | 25,189,121 | - | 25,189,121 |
| Securities available for sale (FX) | - | 31,696,164 | - | 31,696,164 |
| **Total** | **115,319** | **56,885,285** | **-** | **57,000,604** |

Level 1 includes financial instruments traded in the stock exchange, while Level 2 includes securities whose fair values are estimated using the internally developed models based on the information from the auctions held in the secondary securities market (auctions).

Fair values of assets determined using the prices from the banking market are classified into Level 3.

### 4.9. Capital Management

The Bank has established a risk management system in accordance with the volume and structure of its business activities and the capital management is aimed at unhindered achievement of the Bank's business policy goals.

The calculation of the amount of capital and capital adequacy ratio is reconciled with the Basel II Standards.

The Bank manages capital on an ongoing basis in order to:
- Maintain the minimum regulatory capital requirement (EUR 10 million);
- Comply with the prescribed capital adequacy ratio (minimum 12%);
- Maintain customer trust in the safety and stability of the Bank's operations;
- Realize business and financial plans;
- Support the expected growth of loans and receivables due from customers;
- Ensure optimum future sources of funds and deployment thereof;
- Realize of the dividend policy.

The Bank's regulatory capital represents the sum of the core capital and supplementary capital, reduced for deductible items. The capital adequacy ratio represents the Bank's capital relative to the sum of credit risk-weighted assets, foreign currency gap and operational risk exposure. Credit risk-weighted assets are determined according to risk weights prescribed for all types of assets. Exposure to operational risk is determined by multiplying the reciprocal value of the prescribed capital adequacy ratio by the capital requirement for operational risk, which represent a three-year average of the product of exposure indicators for all lines of business by the prescribed capital requirement rates for each individual business line.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 4. RISK MANAGEMENT (Continued)

### 4.9. Capital Management (Continued)

**Capital adequacy ratio**

| | 2014 | 2013 |
|---|---|---|
| Core capital | 33,286,532 | 45,134,001 |
| Supplementary capital | 4,593,961 | 4,961,842 |
| Deductible items | (5,555,355) | (16,076,615) |
| **Capital** | **32,325,138** | **34,019,228** |
| Credit risk-weighted assets | 162,919,928 | 161,509,806 |
| Operational risk exposure | 19,093,050 | 16,668,642 |
| Foreign currency risk exposure | 938,917 | 720,804 |
| **Capital adequacy ratio (minimum 12%)** | **17.67%** | **19.02%** |

In the course of 2014 the Bank's capital adequacy ratio was in excess of the prescribed regulatory limit of 12%.

Through its Capital Management Strategy and Capital Management Plan, the Bank ensures maintenance of the level and structure of the internal capital, which adequately supports increase in loans and receivables, future sources of funding and their utilizations, dividend policy and changes in regulatory requirements.

As part of the system of capital management, the Capital Management Plan, includes the following:

- Strategic goals and schedule for realization thereof;
- Manner of organizing the process of available internal capital management;
- Procedures for planning adequate levels of available internal capital;
- Manner of attaining and maintaining adequate levels of available internal capital; and
- The Business Continuity Plan in case of unforeseen events.

The Bank continuously implements processes of internal assessment of capital adequacy in accordance with the nature, volume and complexity of its business operations and in compliance with the adopted risk management strategy, individual risk management policies and capital management strategy.

As a documented and continuous process, internal assessment of capital adequacy meets the following criteria:

- it is based on risk identification and measurement;
- it provides comprehensive assessment and monitoring of risks the Bank is or may be exposed to;
- it provides adequate level of internally available capital according to the Bank's risk profile,
- it is included in the Bank's management system and decision making process; and
- it is subject to regular analysis, supervision and review.

Stages of the internal capital adequacy assessment include the following:

- determination of materially significant risks as per qualitative and quantitative criteria;
- calculation of the amounts of internal capital requirements;
- determination of the aggregate internal capital requirement;
- comparison of the following elements:
  - capital to available internal capital;
  - minimum prescribed capital requirements to internal capital requirements for individual risks; and
  - sum of the minimum capital requirements to the aggregate internal capital requirement.

## 5. USE OF ESTIMATES

Management makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and underlying assumptions are continually reviewed and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

**Key Sources of Estimation Uncertainty**

*Provisions for Credit Losses*

Assets accounted for at amortized cost are assessed for impairment on a basis described in accounting policy 3(j) (vii).

The specific counterparty component of the total allowances for impairment applies to financial assets evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgments about counterparty's financial situation and the net realizable value of any underlying collateral. Each impaired asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are independently approved by the Credit Risk function.

Collectively assessed impairment allowances cover credit losses inherent in portfolios of loans and receivables and held-to-maturity investment securities with similar credit risk characteristics when there is objective evidence to suggest that they contain impaired items cannot yet be identified. In assessing the need for collective loss allowances, management considers factors such as credit quality, portfolio size, concentrations and economic factors. In order to estimate the required allowances, assumptions are made to define the way inherent losses are modelled and to determine the required input parameters, based on historical experience and current economic conditions. The accuracy of the allowances depends on the estimates of future cash flows for specific counterparty allowances and the model assumptions and parameters used in determining collective allowances.

*Determining Fair Values*

The determination of fair value for financial assets and liabilities for which there is no observable market price requires the use of valuation techniques as described in accounting policy 3(j) (vi). For financial instruments that trade infrequently and have little price transparency, fair value is less objective, and requires varying degrees of judgment depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument.

**Critical Accounting Judgments in Applying the Bank's Accounting Policies**

Critical accounting judgments made in applying the Bank's accounting policies include:

*Impairment of Investments in Equity Shares*

Investments in equity shares are estimated for impairment in accordance with the method described under accounting policies 3(j) (vii) and 3(n).

*Valuation of Financial Instruments*

The Bank accounting policy on fair value measurement is disclosed in accounting policy 3(j) (vi).

## 5. USE OF ESTIMATES (Continued)

### Critical Accounting Judgments in Applying the Bank's Accounting Policies

The Bank measures fair values using the following fair value hierarchy that reflects the significance of the inputs used valuation:

- Level 1: Quoted market price (unadjusted) in an active market for an identical instrument.
- Level 2: Valuation techniques based on observable inputs other than quoted prices, either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.
- Level 3: Valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

Fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments the Bank determines fair values using valuation techniques.

Valuation techniques include net present value and discounted cash flow models, comparison to similar instruments for which market observable price exist and other valuation models. Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates, credit spreads and other premiums used in estimating discount rates, bond and equity prices, foreign exchange rates, equity and equity index prices and expected price volatilities and correlations. The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date, which would have been determined by market participants acting at arm's length.

The Bank uses widely recognized valuation models for determining the fair value of common and more simple financial instruments, like interest rate and currency swaps that use only observable market data and require little management judgment and estimation. Observable prices and model inputs are usually available in the market for listed debt and equity securities, exchange traded derivatives and simple over the counter derivatives like interest rate swaps.

Availability of observable market prices and model inputs reduces the need for management judgment and estimation and also reduces the uncertainty associated with determination of fair values. Availability of observable market prices and inputs varies depending on the products and markets and is prone to changes based on specific events and general conditions in the future markets.

## 6. SEGMENT REPORTING

As described in the following passages, the Bank has three operating segments, which are the Bank's strategic divisions. The strategic divisions offer different products and services, and are managed separately based on the Bank's management and internal reporting structure. For each of the strategic divisions, the Bank's management reviews internal management reports on at least a monthly basis. The following summary describes the operations in each of the Bank's reporting segments:

| | |
|---|---|
| Corporate Banking | Includes loans, deposits and other transactions and balances with corporate customers |
| Retail Banking | Includes loans, deposits and other transactions and balances with retail customers |
| Investment banking and interbank operations | Include securities and other financial instruments, as well as transactions with banks |

Information regarding the results of each reporting segment is included below. Performance is measured based on segment profit before taxes, as included in the internal management reports that are reviewed by the Bank's Executive and Supervisory Boards. Segment profit is used to measure performance as management believes that such information is the most relevant in evaluating the results of certain segments relative to other entities that operate within these industries. Inter-segment pricing is determined on an arm's length basis.

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## 6. SEGMENT REPORTING (Continued)

Operating segments report for 2014 is provided below:

| | Retail banking* | Corporate banking | Investment and Interbank operations | Other | Total |
|---|---|---|---|---|---|
| External revenues and expenses | | | | | |
| Interest, fee and commission income | 10,540,415 | 9,194,539 | 7,166,465 | - | 26,901,419 |
| Interest, fee and commission expenses | (5,002,794) | (1,594,687) | (2,287,595) | - | (8,885,076) |
| Net gains/losses from impairment allowance | (382,120) | (2,341,030) | (2,239) | - | (2,725,389) |
| Net foreign exchange gains/losses | - | - | (205,943) | - | (205,943) |
| Net other income and expenses | 60,140 | 298,208 | 60,140 | - | 418,488 |
| Profit before operating expenses | **5,215,642** | **5,557,029** | **4,730,828** | **-** | **15,503,499** |
| Direct operating expenses | (5,478,080) | (1,588,907) | (331,978) | - | (7,398,965) |
| Net income/expenses from related party transactions | 2,303,754 | (3,428,395) | 1,124,641 | - | - |
| Profit after operating expenses and related party transactions | **2,041,315** | **539,728** | **5,523,491** | **-** | **8,104,534** |
| Indirect operating expenses** | (1,868,265) | (1,144,048) | (334,632) | - | (3,346,945) |
| **Profit before taxes*** | **173,050** | **(604,320)** | **5,188,859** | **-** | **4,757,589** |
| **Assets per segment** | | | | | |
| Cash and cash funds held with the central bank | - | - | 68,547,389 | - | 68,547,389 |
| Loans and receivables due from banks and other financial institutions | - | - | 34,737,605 | - | 34,737,605 |
| Loans and receivables due from customers | 69,071,647 | 116,305,388 | - | - | 185,377,035 |
| Investment securities | - | - | 95,654,325 | - | 95,654,325 |
| Other | - | - | 5,480,888 | 16,464,283 | 21,945,171 |
| | **69,071,647** | **116,305,388** | **204,420,207** | **16,464,283** | **406,261,524** |
| **Liabilities per segment** | | | | | |
| Deposits and other liabilities due to banks, other financial institutions and the central bank | - | - | 23,743,018 | - | 23,743,018 |
| Deposits and other liabilities due to customers | 210,246,716 | 57,748,604 | 33,959,592 | - | 301,954,911 |
| Subordinated liabilities | - | - | 6,036,680 | - | 6,036,680 |
| Other | - | - | - | 4,980,111 | 4,980,111 |
| | **210,246,716** | **57,748,604** | **63,739,290** | **4,980,111** | **336,714,720** |

* Loans to micro clients are presented within Retail banking segment
** Indirect operating expenses refer to expenses that are not controlled by the business segments

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## 6. SEGMENT REPORTING (Continued)

Operating segments report for 2013 is provided below:

| | Retail banking* | Corporate banking | Investment and Interbank operations | Other | Total |
|---|---|---|---|---|---|
| External revenues and expenses | | | | | |
| Interest, fee and commission income | 10,034,643 | 11,325,958 | 6,156,383 | - | 27,516,985 |
| Interest, fee and commission expenses | (5,687,926) | (1,933,536) | (2,401,137) | - | (10,022,599) |
| Net gains/losses from impairment allowance | (241,744) | (3,024,372) | 46,041 | - | (3,220,075) |
| Net foreign exchange gains/losses | | | (48,733) | - | (48,733) |
| Net other income and expenses | 105,163 | 314,266 | 105,162 | - | 524,591 |
| **Profit before operating expenses** | **4,210,137** | **6,682,316** | **3,857,717** | **-** | **14,750,169** |
| Direct operating expenses | (5,092,812) | (1,413,775) | (281,088) | - | (6,787,675) |
| Net income/expenses from related party transactions | 2,312,653 | (4,124,184) | 1,811,531 | - | - |
| Profit after operating expenses and related party transactions | 1,429,978 | 1,144,356 | 5,388,160 | - | 7,962,493 |
| Indirect operating expenses** | (1,878,056) | (1,155,370) | (340,693) | - | (3,374,119) |
| **Profit before taxes*** | **(448,079)** | **(11,014)** | **5,047,467** | **-** | **4,588,375** |
| **Assets per segment** | | | | | |
| Cash and cash funds held with the central bank | - | - | 70,934,839 | - | 70,934,839 |
| Loans and receivables due from banks and other financial institutions | - | - | 35,247,935 | - | 35,247,935 |
| Loans and receivables due from customers | 61,832,082 | 115,727,976 | - | - | 177,560,058 |
| Investment securities | - | - | 57,150,504 | - | 57,150,504 |
| Other | - | - | 5,480,888 | 16,412,095 | 21,892,983 |
| | **61,832,082** | **115,727,976** | **168,814,166** | **16,412,095** | **362,786,319** |
| **Liabilities per segment** | | | | | |
| Deposits and other liabilities due to banks, other financial institutions and the central bank | | | 21,058,542 | - | 21,058,542 |
| Deposits and other liabilities due to customers | 189,120,025 | 45,178,850 | 31,721,413 | - | 266,020,289 |
| Subordinated liabilities | - | - | 5,711,409 | - | 5,711,409 |
| Other | - | - | - | 5,033,861 | 5,033,861 |
| | **189,120,025** | **45,178,850** | **58,491,364** | **5,033,861** | **297,824,101** |

* Loans to micro clients are presented within Retail banking segment
** Indirect operating expenses refer to expenses that are not controlled by the business segment

## 7. FINANCIAL ASSETS AND LIABILITIES - ACCOUNTING CLASSIFICATION AND FAIR VALUES

The following describes the methodologies and assumptions used to determine fair values for those financial instruments which are not already recorded at fair value in the financial statements:

*(i) Assets for which fair value approximates carrying value*

For financial assets and financial liabilities that are highly liquid or having a short term original maturity (less than one year) it is assumed that the carrying amount approximate to their fair value. This assumption is also applied to demand deposits, saving accounts without a specific maturity and variable interest rate financial instruments.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 7. FINANCIAL ASSETS AND LIABILITIES - ACCOUNTING CLASSIFICATION AND FAIR VALUES (Continued)

*(ii) Fixed rate financial instruments*

The fair value of fixed interest rate financial assets and liabilities carried at amortized cost are estimated by comparing market interest rates when they were first recognized with current market rates offered for similar financial instruments. The assessed fair values of assets and liabilities with fixed interest rates mostly correspond to the carrying values thereof given that the interest rates applied do not depart from market interest rates. There are no materially significant departures in this respect.

## 8. NET INTEREST INCOME

Net interest income includes:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Loans and receivables due from banks | 591,752 | 1,270,256 |
| Loans and receivables due from customers | 14,686,703 | 16,539,021 |
| Central bank | 587,127 | 710,674 |
| Investment securities | 5,358,797 | 3,503,823 |
| **Total interest income** | 21,224,379 | 22,023,774 |
| Deposits from and liabilities due to banks | 688,661 | 972,264 |
| Deposits from and liabilities due to customers | 6,133,656 | 7,233,835 |
| Borrowings received | 1,103,476 | 888,437 |
| **Total interest expenses** | 7,925,793 | 9,094,536 |
| **Net interest income** | 13,298,586 | 12,929,238 |

Total interest income and expenses calculated using the effective interest rate method presented in the table above relate to financial assets and liabilities other than those at fair value through profit or loss.

**NOTES TO THE FINANCIAL STATEMENTS**
**December 31, 2014**
*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 9. NET FEE AND COMMISSION INCOME

Net fee and commission income includes:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| ***Fees and commission* income** | | |
| Payment transfer operations | 2,835,577 | 2,744,327 |
| Fees on issued loans and guarantees - retail customers | 20,011 | 21,602 |
| Fees on issued loans and guarantees - corporate customers | 259,847 | 249,650 |
| Fees on purchase and sale of foreign currencies | 443,916 | 542,380 |
| Brokerage and custody fees | 60,375 | 43,534 |
| Fees arising from card operations | 1,160,379 | 1,015,231 |
| Credit Bureau processing fees | 84,265 | 81,642 |
| Other banking services | 645,203 | 649,453 |
| | 5,509,573 | 5,347,819 |
| ***Fee and commission expenses*** | | |
| Payment transfer operations | 86,079 | 78,584 |
| Fees on issued loans and guarantees - corporate customers | 2,383 | 4,799 |
| Brokerage and custody fees | 2,195 | 3,098 |
| Fees arising from card operations | 72,258 | 58,295 |
| Other banking services | 4,552 | 616 |
| | 167,467 | 145,392 |
| | 5,677,040 | 5,493,211 |
| ***Fee and commission expenses in RSD*** | | |
| Payment transfer operations | 206,287 | 213,196 |
| Fees arising on purchase and sale of foreign currencies | 19,437 | 51,282 |
| Fees arising from card operations | 273,557 | 235,321 |
| Credit Bureau processing fees | 64,802 | 65,184 |
| Other banking services | 128,585 | 114,501 |
| | 692,668 | 679,484 |
| ***Fee and commission expenses in foreign currencies*** | | |
| Payment transfer operations | 39,533 | 31,630 |
| Fees arising from card operations | 183,028 | 160,273 |
| Other banking services | 44,054 | 56,676 |
| | 266,615 | 248,579 |
| | 959,283 | 928,063 |
| **Net fee and commission income** | 4,717,757 | 4,565,148 |

## 10. NET GAINS ON FINANCIAL ASSETS HELD FOR TRADING

Net gains on the financial assets held for trading include:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Gains on the fair value adjustment of securities – bonds | 3,669 | 6,092 |
| Gains on the fair value adjustment of securities – investment units | 1,040 | 504 |
| Gains on the fair value adjustment of securities – shares | 426 | 958 |
| Gains on the sales of securities at fair value through profit and loss | 2,469 | 16,340 |
| | 7,604 | 23,894 |
| Losses on the fair value adjustment of securities – shares | (508) | (290) |
| Losses on the fair value adjustment of securities – bonds | (532) | (1,262) |
| Losses on the fair value adjustment of securities – investment units | (49) | - |
| Losses on the sales of securities and other financial assets held for trading | (439) | - |
| | (1,528) | (1,552) |
| Net gains on the financial assets held for trading | 6,076 | 22,342 |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 11. NET GAINS ON FINANCIAL ASSETS AVAILABLE FOR SALE

Net gains on the financial assets available for sale include:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Gains on the sale of securities available for sale | 52,028 | 1,738 |
| Losses on the sale of securities available for sale | (746) | - |
| **Net gains on the financial assets available for sale** | 51,282 | 1,738 |

Gains on the sale of securities available for sale of RSD 52,028 thousand relate to the gains from the sale of old foreign currency savings bonds (2014 series) in the amount of RSD 8,248 thousand and the Republic of Serbia Treasury bills in the amount of RSD 43,780 thousand.

## 12. NET FOREIGN EXCHANGE LOSSES AND NEGATIVE CURRENCY CLAUSE EFFECTS

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Positive currency clause effects | 4,993,387 | 4,551,137 |
| Positive currency clause effects – value adjustment of securities | 14,022 | 7,737 |
| Foreign exchange gains – value adjustment of securities | 27,065 | 421,001 |
| Positive currency clause effects – retail customers | 2,607,787 | 1,946,214 |
| Foreign exchange gains | 6,504,190 | 1,440,279 |
| | 14,146,451 | 8,366,368 |
| Negative currency clause effects | (980,887) | (3,833,060) |
| Negative currency clause effects – value adjustment of securities | (3,392) | (7,452) |
| Negative currency clause effects – value adjustment of liabilities | (207,365) | (460,227) |
| Negative currency clause effects – retail customers | (343,072) | (1,716,465) |
| Foreign exchange losses | (12,817,678) | (2,397,897) |
| | (14,352,394) | (8,415,101) |
| **Net foreign exchange losses and negative currency clause effects** | (205,943) | (48,733) |

## 13. OTHER OPERATING INCOME

Other operating income relates to:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Gains on the valuation of property and equipment | - | 12,260 |
| Reversal of unreleased provisions for litigations | - | 381,670 |
| Other income from operations | 179,395 | 186,815 |
| Other income | 389,796 | 542,801 |
| **Total** | 569,191 | 1,123,546 |

Within the line item of other income the largest portion relates to the prior years' interest income from corporate customers and prior years' interest income from retail customers in the amount of RSD 177,926 thousand and RSD 41,570 thousand, respectively.

In 2014 the Bank received dividend from its subsidiary bank from Budva in the amount of RSD 120,689 thousand (EUR 1,000 thousand). The Bank withheld and paid withholding tax at the rate of 9% in Montenegro in the amount of RSD 10,862 thousand (EUR 90 thousand). The net amount of dividend paid was RSD 109,827 thousand, i.e., EUR 910 thousand.

Within the line item of other income from operations in 2014, the amount of RSD 101,130 thousand relates to rental income (out of which RSD 93,770 thousand relates to income from properties leased out for business purposes.

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*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 14. NET LOSSES FROM IMPAIRMENT OF FINANCIAL ASSETS AND CREDIT RISK-WEIGHTED OFF-BALANCE SHEET ASSETS

Net losses from impairment of financial assets relate to:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Impairment allowance of loans and receivables | 10,107,502 | 8,778,348 |
| Provisions for off-balance sheet items | 540,305 | 602,322 |
| Reversal of impairment allowance of loans and receivables | (7,476,813) | (5,583,660) |
| Reversal of provisions for off-balance sheet items | (445,528) | (576,908) |
| Income from collection of receivables previously written-off | (77) | (27) |
| **Total** | 2,725,389 | 3,220,075 |

Until the end of January 2015 the Bank did not have material collections of loans and receivables previously written off that would affect the reversal of impairment allowance in accordance with IAS 10.

**MOVEMENTS ON IMPAIRMENT ALLOWANCE ACCOUNTS AND PROVISION FOR OFF-BALANCE SHEET ITEMS**

| | Loans and receivables due from banks (Note 23.2) | Loans and receivables due from customers (Note 24.2) | Investment securities (Notes 21 and 22) | Other assets (Note 32) | Off-balance sheet liabilities (Note 36) | Total |
|---|---|---|---|---|---|---|
| **Balance as at January 1, 2014** | **325,374** | **18,830,581** | **45,185** | **1,764,028** | **473,647** | **21,438,815** |
| Charge for the year | 2,468 | 9,835,443 | 9,428 | 260,163 | 540,305 | 10,647,807 |
| Charge for the year | (2,452) | (6,714,653) | (12,715) | (746,993) | (445,528) | (7,922,341) |
| Decrease in impairment allowance | | 394,977 | - | - | - | 394,977 |
| Foreign exchange effects | 43,199 | 452,908 | 94 | 9,486 | - | 505,687 |
| Write-off | - | (268,885) | - | (1,530) | - | (270,415) |
| Other movements | - | 554,606 | 78,229 | 21,147 | - | 653,982 |
| **Balance as at December 31, 2014** | **368,589** | **23,084,977** | **120,221** | **1,306,301** | **568,424** | **25,448,512** |

## 15. STAFF COSTS

Staff costs include:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Net salaries | 2,519,942 | 2,583,349 |
| Net benefits | 429,025 | 408,709 |
| Payroll taxes | 373,034 | 413,507 |
| Payroll contributions | 783,688 | 757,473 |
| Considerations paid to seasonal and temporary staff | 40,725 | 54,145 |
| Provisions for retirement benefits - net | (2,748) | 4,014 |
| Other staff costs | 67,823 | 40,926 |
| **Total** | 4,211,489 | 4,262,123 |

## 16. DEPRECIATION/AMORTIZATION CHARGE

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Amortization charge – intangible assets (Note 26.2) | 283,451 | 258,440 |
| Depreciation charge – property and equipment (Note 27.2) | 524,597 | 501,092 |
| Depreciation charge – investment property (Note 28.1) | 36,584 | 33,116 |
| **Total** | 844,632 | 792,648 |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 17. OTHER EXPENSES

Other expenses include:

| | Year Ended December 31, 2014. | 2013. |
|---|---|---|
| Cost of materials | 398,717 | 460,929 |
| Cost of production services | 2,176,374 | 2,036,059 |
| Non-material costs (without taxes and contributions) | 2,224,978 | 1,615,612 |
| Taxes payable | 139,132 | 142,444 |
| Contributions payable | 713,802 | 816,697 |
| Other costs | 34,037 | 39,297 |
| Other expenses | 210,113 | 408,592 |
| Losses on the valuation of property and equipment, investment property and intangible assets | 697 | 197,328 |
| Provisions for litigations | - | 13,100 |
| **Total** | 5,897,850 | 5,730,058 |

## 18. INCOME TAXES

18.1 Components of income taxes as of December 31 were as follows:

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Deferred income tax benefits | 47,547 | 87,950 |
| Deferred income tax expenses | (19,559) | - |
| **Total** | 27,988 | 87,950 |

In 2014 and 2013 the Bank did not report current income tax expenses pursuant to the effective tax regulations.

18.2 Reconciliation of the effective tax rate is presented in the table below:

| | 2014 | 2014 | 2013 | 2013 |
|---|---|---|---|---|
| Profit for the year before taxes | | **4,757,589** | | **4,588,375** |
| Tax calculated using the local income tax rate | 15% | 713,638 | 15% | 688,256 |
| Expenses not recognized for tax purposes | 1.18% | 56,261 | 1.63% | 74,673 |
| Tax effects of the net capital losses /gains | -0.01% | (412) | -0.01% | (73) |
| Tax effects of income reconciliation | -0.30% | (14,441) | -1.01% | (46,245) |
| Tax credit received and used in the current year | 0% | - | -1.06% | (48,356) |
| Tax effects of the interest income from debt securities issued by the Republic of Serbia, AP Vojvodina or NBS | -17.72% | (843,246) | -14.57% | (668,255) |
| Tax effect adjustments (used and new ones) | -0.59% | (27,988) | -1.92% | (87,950) |
| ***Tax effects stated within the income statement*** | - | **(27,988)** | - | **(87,950)** |

18.3 Movements in deferred taxes as at December 31 are presented as follows

| | Year Ended December 31, 2014 | 2013 |
|---|---|---|
| Balance as at January 1 | (10,156) | 4,896 |
| Occurrence and reversal of temporary differences | (140,251) | (15,052) |
| Balance as at December 31 | (150,407) | (10,156) |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 19. CASH AND CASH FUNDS HELD WITH THE CENTRAL BANK

Cash and cash funds held with the central bank include:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| ***In RSD*** | | |
| Cash on hand | 2,466,110 | 2,524,909 |
| Gyro account | 25,191,123 | 22,926,420 |
| Interest on obligatory RSD reserves | - | 20,550 |
| Other RSD cash funds | 100 | 100 |
| | 27,657,333 | 25,471,979 |
| ***In foreign currencies*** | | |
| Cash on hand | 2,492,030 | 1,921,714 |
| Foreign currency obligatory reserves | 36,737,503 | 41,148,420 |
| Other cash funds | 1,660,523 | 2,392,726 |
| | 40,890,056 | 45,462,860 |
| **Total** | 68,547,389 | 70,934,839 |

*Adjustments to cash and cash equivalents for the purpose of preparing the statement of cash flows*

| | | |
|---|---|---|
| Foreign currency accounts held with foreign banks (Note 23.1) | 13,350,291 | 10,531,880 |
| Foreign currency obligatory reserves | (36,737,503) | (41,148,420) |
| Interest on obligatory RSD reserves | - | (20,550) |
| | (23,387,212) | (30,637,090) |
| Cash and cash equivalents reported in the statement of cash flows | 45,160,177 | 40,297,749 |

In the statement of cash flows the Bank reports on the cash funds held on the gyro account held with NBS, cash on accounts held with foreign banks, cash funds held on the account with the Central Securities Registry, Depository and Clearing House and cash on hand.

The gyro account balance includes the RSD obligatory reserves, which represent the minimum amount of RSD reserves allocated in accordance with the Decision on Obligatory Reserves Held with the NBS. In accordance with the said Decision, the obligatory dinar reserves are calculated based on the average daily carrying amount of RSD deposits, loans and other RSD liabilities during a single calendar month, using a rate in the range between 0% to 5%, depending on the maturity of liabilities and their sources, whereby dinar reserve is comprised of: obligatory RSD reserves, 36% of RSD equivalent of obligatory reserves in EUR to deposits up to 730 days, and 28% of RSD equivalent of obligatory reserves in EUR to deposits over 730 days (Official gazette of RS, no. 135/2014). The National Bank of Serbia pays interest on these dinar reserves in the amount of 2.5% per annum (2013: 2.5% p.a.).

The Bank calculates the obligatory reserves in foreign currency on the 17th day of the month based on the average balance of foreign currency deposits registered in the preceding calendar month. The required reserve in foreign currency is allocated onto a special account held with the National Bank of Serbia and these funds may be drawn as necessary. The Bank is under obligation to maintain the average monthly balance of the allocated foreign currency reserve in the amount of the calculated foreign currency obligatory reserve, where, for the purposes of realizing average daily balance of allocated required reserve, the daily balance on the account of required reserve may be below or above the calculated foreign currency obligatory reserve.

Foreign currency obligatory reserve does not accrue interest. During 2014, in accordance with the Decision on Required Reserves of Banks with the National Bank of Serbia, the Bank allocated a certain portion of its foreign currency reserve in dinars to its gyro account.

Other foreign currency cash funds of RSD 1,660,523 thousand (2013: RSD 2,392,726 thousand) entirely relate to the clearing account held with the s Central Securities Registry, Depository and Clearing House for trade in securities.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 20. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT AND LOSS, HELD FOR TRADING

Financial assets held for trading comprise:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Securities held for trading (in RSD) | 51,458 | 21,569 |
| Securities held for trading (in foreign currencies) | 70,176 | 93,750 |
| | 121,634 | 115,319 |

Breakdown of financial assets held for trading is provided below:

| | December 31, 2014 Total assets held for trading | December 31, 2013 Total assets held for trading |
|---|---|---|
| Republic of Serbia bonds | 70,176 | 93,751 |
| Corporate shares | 3,787 | 3,574 |
| Bank shares | 180 | 490 |
| Investment units of OIF monetary fund | 47,491 | 17,504 |
| Balance as at December 31 | 121,634 | 115,319 |

## 21. FINANCIAL ASSETS AVAILABLE FOR SALE

Financial assets available for sale comprise:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Securities available for sale (in RSD) | 35,179,709 | 25,191,634 |
| Securities available for sale (in foreign currencies) | 60,302,034 | 31,696,164 |
| | 95,481,743 | 56,887,798 |
| Impairment allowance of securities available for sale | (494) | (2,513) |
| | 95,481,249 | 56,885,285 |

***Financial assets available for sale***

*In RSD:*
Republic of Serbia Treasury bills in the amount of RSD 10,590,077 thousand; Republic of Serbia bonds in the amount of RSD 22,992,331 thousand; bonds from the City of Pančevo and Municipalities Stara Pazova and Šabac budgets in the amount of RSD 443,283 thousand; bonds of the company Tigar a.d., Pirot in the amount of RSD 69,769 thousand; and bonds of the following banks: Societe generale banka a.d., Beograd in the amount of RSD 1,084,159 thousand and AIK banka a.d., Niš in the amount of RSD 90 thousand.

Out of the total amount of impairment allowance, RSD 490 thousand relates to the bonds of the company Tigar a.d., Pirot.

*In foreign currencies:*
Republic of Serbia Treasury bills in the amount of RSD 10,257,953 thousand; long-term Government of the Republic of Serbia bonds in the amount of RSD 46,972, thousand; Republic of Serbia old savings bonds in the amount of RSD 1,346,991 thousand; foreign bank bonds - Raiffeisen Bank International in the amount of RSD 1,397,811 thousand; and bonds of the UK Government in the amount of RSD 326,704 thousand.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 21. FINANCIAL ASSETS AVAILABLE FOR SALE (Continued)

Movements on the account of impairment allowance of securities available for sale were as follows:

**Impairment allowance of securities available for sale**

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| **Individual impairment allowance** | | |
| Balance at January 1 | 2,512 | 2,546 |
| Current year impairment allowance: | | |
| Charge for the year | 1,962 | 16,607 |
| Effects of the changes in foreign exchange rates | 94 | 442 |
| Reversal | (4,074) | (17,083) |
| **Total individual impairment allowance** | 494 | 2,512 |

## 22. FINANCIAL ASSETS HELD TO MATURITY

Financial assets held to maturity comprise:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Securities held to maturity (discounted bills of exchange) | 171,169 | 192,573 |
| Impairment allowance of securities held to maturity | (119,727) | (42,673) |
| | 51,442 | 149,900 |

***Financial assets held to maturity***

**Impairment allowance of securities held to maturity**

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| **Individual impairment allowance** | | |
| Balance at January 1 | 42,673 | 51,253 |
| Current year impairment allowance: | | |
| Charge for the year | 7,466 | 128,566 |
| Reclassified from individual to group impairment allowance | (24,411) | - |
| Reversal | (7,547) | (137,146) |
| Other | 32 | - |
| **Total individual impairment allowance** | 18,213 | 42,673 |
| **Group impairment allowance** | | |
| Balance at January 1 | - | - |
| Charge for the year | | |
| Reclassified from individual to group impairment allowance | 24,411 | - |
| Reversal | (1,094) | - |
| Other | 78,197 | - |
| **Total group impairment allowance** | 101,514 | - |
| **Total group and individual impairment allowance** | 119,727 | 42,673 |

**NOTES TO THE FINANCIAL STATEMENTS**
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## 23. LOANS AND RECEIVABLES DUE FROM BANKS AND OTHER FINANCIAL INSTITUTIONS

23.1 Loans and receivables due from banks include:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| ***RSD loans and receivables*** | | |
| Per repo transactions | 7,000,000 | 12,246,700 |
| Loans for working capital | 1,200,000 | 100,000 |
| Overnight loans | 2,200,000 | - |
| Other receivables | 27,567 | 28,986 |
| Prepayments | 24,595 | 2,602 |
| Impairment allowance | (105,463) | (105,463) |
| | 10,346,699 | 12,272,825 |
| ***FX loans and receivables*** | | |
| Foreign currency accounts held with foreign banks (Note 19) | 13,350,291 | 10,531,880 |
| Overnight loans | 8,094,628 | 9,238,017 |
| Other loans and receivables due from foreign banks | 575,355 | 480,225 |
| Foreign currency deposits placed with other banks | 1,117,200 | 1,046,461 |
| Prepayments | 3,513 | 6,920 |
| Other receivables | 15,924 | 17,165 |
| Loans to foreign banks (subsidiaries) | 604,792 | 653,460 |
| Secured foreign currency sureties | 892,329 | 1,220,893 |
| Impairment allowance | (263,126) | (219,911) |
| | 24,390,906 | 22,975,110 |
| | 34,737,605 | 35,247,935 |

As of December 31, 2013 securities acquired through repo transactions with the National Bank of Serbia amounting to RSD 7,000,000 thousand relate to the Treasury bills purchased from the National Bank of Serbia with maturities of up to 8 days at the annual interest rate of 6.2%.

Short-term RSD deposits of other banks were placed with the Bank for a period of a year at interest rates ranging from 6.0 % to 10.5% per annum.

Short-term foreign currency deposits of other banks were placed with the Bank for a period of a year at interest rates ranging from 0.01% to 0.8% annually for EUR deposits and from 0.02% to 0.4% and 0.05% for USD and CHF deposits, respectively.

Interest rates applied to the loans extended to subsidiary banks ranged between 3.75% plus EURIBOR and 3.83% plus EURIBOR.

23.2 Movements on the account of impairment allowance of loans and receivables due from banks are provided in the table below:

| | | |
|---|---|---|
| **Group impairment allowance** | | |
| Balance at January 1 | 325,374 | 333,437 |
| Current year impairment allowance: | | |
| Charge for the year | 2,468 | 990 |
| Effects of the changes in foreign exchange rates | 43,199 | 47,762 |
| Reversal | (2,452) | (56,815) |
| **Total group impairment allowance** | **368,589** | **325,374** |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 24. LOANS AND RECEIVABLES DUE FROM CUSTOMERS

24.1 Loans and receivables due from customers:

| | 2014 Gross Amount | 2014 Impairment Allowance | 2014 Carrying Amount | 2013 Gross Amount | 2013 Impairment Allowance | 2013 Carrying Amount |
|---|---|---|---|---|---|---|
| **Corporate customers** | | | | | | |
| Transaction account overdrafts | 655,510 | (188,902) | 466,608 | 870,024 | (145,294) | 724,730 |
| Working capital loans | 51,932,892 | (6,089,887) | 45,843,005 | 47,629,473 | (4,027,004) | 43,602,469 |
| Export loans | 2,181,694 | (887,774) | 1,293,920 | 2,905,328 | (927,611) | 1,977,717 |
| Investment loans | 35,389,792 | (2,081,382) | 33,308,410 | 36,897,924 | (1,337,528) | 35,560,396 |
| Purchased loans and receivables - factoring | 101,171 | (80,424) | 20,747 | 159,499 | (29,458) | 130,041 |
| Loans for payment of imported goods and services | 5,270,391 | (1,804,796) | 3,465,595 | 4,805,144 | (2,086,475) | 2,718,669 |
| Loans for discounted bills of exchange ,acceptances and payments made for guarantees called on | 1,865,582 | (1,058,213) | 807,369 | 1,888,584 | (1,013,810) | 874,774 |
| Other loans and receivables | 50,663,189 | (8,730,494) | 41,932,695 | 46,888,173 | (7,450,449) | 39,437,724 |
| Prepayments | 445,249 | (905) | 444,344 | 341,767 | - | 341,767 |
| Accruals | (283,166) | - | (283,166) | (359,271) | - | (359,271) |
| **Retail customers** | | | | | | |
| Transaction account overdrafts | 4,450,820 | (638,367) | 3,812,453 | 4,609,541 | (569,436) | 4,040,105 |
| Housing loans | 37,842,597 | (517,453) | 37,325,144 | 33,800,924 | (460,696) | 33,340,228 |
| Cash loans | 15,060,740 | (854,475) | 14,206,265 | 12,632,696 | (681,094) | 11,951,602 |
| Consumer loans | 597,545 | (49,927) | 547,618 | 1,165,521 | (55,983) | 1,109,538 |
| Other loans and receivables | 2,447,906 | (97,021) | 2,350,885 | 2,324,113 | (45,743) | 2,278,370 |
| Prepayments | 220,458 | (4,957) | 215,501 | 183,756 | - | 183,756 |
| Accruals | (380,358) | - | (380,358) | (352,557) | - | (352,557) |
| **Balance as at December 31** | **208,462,012** | **(23,084,977)** | **185,377,035** | **196,390,639** | **(18,830,581)** | **177,560,058** |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 24. LOANS AND RECEIVABLES DUE FROM CUSTOMERS (Continued)

24.2 Movements on the account of impairment allowance of loans and receivables due from customers are presented in the table below:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| **Individual impairment allowance** | | |
| Balance as at January 1 | 6,406,946 | 3,410,334 |
| Current year impairment allowance: | | |
| Charge for the year | 5,715,603 | 4,825,093 |
| Reclassified from group to individual impairment allowance | 3,021,278 | 58,681 |
| Effects of the changes in foreign exchange rates | 517,703 | 37,365 |
| Reversal | (5,555,663) | (1,916,049) |
| Transfer from off-balance sheet items | 394,977 | - |
| Prior years' interest income | (171,669) | - |
| Other | 660,593 | (8,478) |
| **Total individual impairment allowance** | **10,989,768** | **6,406,946** |
| **Group impairment allowance** | | |
| Balance as at January 1 | 12,423,635 | 12,085,663 |
| Current year impairment allowance: | | |
| Charge for the year | 4,119,840 | 3,579,923 |
| Reclassified from group to individual impairment allowance | (3,021,278) | (58,681) |
| Effects of the changes in foreign exchange rates | 106,874 | (26,047) |
| Reversal | (1,158,990) | (3,136,099) |
| Write-off | (268,885) | (13,728) |
| Other | (105,987) | (7,396) |
| **Total group impairment allowance** | **12,095,209** | **12,423,635** |
| **Balance as at December 31** | **23,084,977** | **18,830,581** |

24.3 Short-term RSD and foreign currency loans were approved for periods from 30 days to one year, at interest rates ranging between 0.53% and 1.8% per month.

Long-term RSD and foreign currency loans were approved for periods from 1 to the maximum of 30 years, at interest rates ranging between 3.35% (increased by the interest rate agreed upon for the related monetary collateral) and 22.5% per annum.

**Risks and Uncertainties**

The Bank's management recorded provisions for potential credit losses based on all known or anticipated credit risks as of the issue date of the financial statements. The Bank's loan portfolio receivables were classified based on the most recent financial information available as well as based on the expected effects of the restructuring processes. If these effects fail to provide possibilities to settle the liabilities due to the Bank, the Bank's receivables are mostly collateralized by mortgages assigned over property held by debtors, as well as pledges on movables. In the case that the debt recovery actions undertaken by the Bank's management are unsuccessful, additional amounts of allowances for impairment and provisions for losses based on the assessed irrecoverability would be required in the forthcoming reporting periods.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 25. INVESTMENTS IN SUBSIDIARIES

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| KomBank INVEST a.d., Beograd | 140,000 | 140,000 |
| Komercijalna banka a.d., Banja Luka | 2,974,615 | 2,974,615 |
| Komercijalna banka a.d., Budva | 2,366,273 | 2,366,273 |
| | 5,480,888 | 5,480,888 |

## 26. INTANGIBLE ASSETS

26.1 Intangible assets comprise:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Intangible assets | 388,775 | 527,025 |
| Intangible assets in progress | 16,999 | 10,420 |
| | 405,774 | 537,445 |

26.2 Movements on the account of intangible assets in 2014 and 2013 are presented below:

| | Licenses and Software | Intangible Assets in Progress | Total |
|---|---|---|---|
| **Cost** | | | |
| Balance at January 1, 2013 | 1,166,177 | 46,537 | 1,212,714 |
| Additions | - | 195,447 | 195,447 |
| Transfers | 231,564 | (231,564) | - |
| Balance at December 31, 2013 | 1,397,741 | 10,420 | 1,408,161 |
| Balance at January 1, 2014 | 1,397,741 | 10,420 | 1,408,161 |
| Additions | - | 151,781 | 151,781 |
| Transfers | 145,202 | (145,202) | - |
| Balance at December 31, 2014 | 1,542,943 | 16,999 | 1,559,942 |
| **Accumulated Amortization** | | | |
| Balance at January 1, 2013 | 612,276 | - | 612,276 |
| Charge for the year (Note 16) | 258,440 | - | 258,440 |
| Balance at December 31, 2013 | 870,716 | - | 870,716 |
| Balance at January 1, 2014 | 870,716 | - | 870,716 |
| Charge for the year (Note 16) | 283,451 | - | 283,451 |
| Balance at December 31, 2014 | 1,154,167 | - | 1,154,167 |
| **Net Book Value** | | | |
| - Balance at January 1, 2013 | 553,901 | 46,537 | 600,438 |
| - Balance at December 31, 2013 | 527,025 | 10,420 | 537,445 |
| - Balance at December 31, 2014 | **388,775** | **16,999** | **405,774** |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 27. PROPERTY, PLANT AND EQUIPMENT

27.1 Property, plant and equipment comprise:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Property | 5,466,855 | 5,560,302 |
| Equipment | 838,138 | 926,305 |
| Investments in progress | 24,084 | 91,063 |
| | 6,329,077 | 6,577,670 |

27.2 Movements on the account of property and equipment in 2014 and 2013 are presented below:

| | Property | Equipment | Investment in Progress | Total |
|---|---|---|---|---|
| **Cost** | | | | |
| Balance at January 1, 2013 | 5,765,101 | 2,795,998 | 50,434 | 8,611,533 |
| Additions | - | - | 1,006,523 | 1,006,523 |
| Transfers from investment in progress (Note 28.1) | 287,195 | 379,504 | (965,894) | (299,195) |
| Transfers from investment property(Note 28.1) | 154,350 | - | - | 154,350 |
| Disposal and retirement | (3,743) | (112,618) | - | (116,361) |
| Appraisal (revaluation) increase | 972,450 | - | - | 972,450 |
| Appraisal (revaluation) decrease | (191,808) | - | - | (191,808) |
| Impairment due to force majeure | (27,806) | - | - | (27,806) |
| Balance at December 31, 2013 | 6,955,739 | 3,062,884 | 91,063 | 10,109,686 |
| Balance at January 1, 2014 | 6,955,739 | 3,062,884 | 91,063 | 10,109,686 |
| Additions | - | - | 1,128,920 | 1,128,920 |
| Transfers from investment in progress (Note 28.1) | 107,598 | 280,815 | (1,195,899) | (807,486) |
| Transfers to investment property(Note 28.1) | (7,001) | - | - | (7,001) |
| Disposal and retirement | (34,087) | (100,179) | - | (134,266) |
| Sales | (10,180) | (47,770) | - | (57,950) |
| Balance at December 31, 2014 | 7,012,069 | 3,195,750 | 24,084 | 10,231,903 |
| **Accumulated Depreciation** | | | | |
| Balance at January 1, 2013 | 1,031,410 | 1,889,510 | - | 2,920,920 |
| Charge for the year (Note 16) | 147,369 | 353,723 | - | 501,092 |
| Transfers from investment property(Note 28.1) | 20,755 | - | - | 20,755 |
| Impairment due to force majeure | (3,649) | - | - | (3,649) |
| Disposal and retirement | (2,923) | (107,323) | - | (110,246) |
| Appraisal (revaluation) increase | 226,092 | - | - | 226,092 |
| Appraisal (revaluation) decrease | (23,617) | - | - | (23,617) |
| Other | - | 669 | - | 669 |
| Balance at December 31, 2013 | 1,395,437 | 2,136,579 | - | 3,532,016 |
| Balance at January 1, 2014 | 1,395,437 | 2,136,579 | - | 3,532,016 |
| Charge for the year (Note 16) | 164,446 | 360,151 | - | 524,597 |
| Transfers to investment property(Note 28.1) | (1,394) | - | - | (1,394) |
| Disposal and retirement | (11,072) | (93,791) | - | (104,863) |
| Sales | (2,203) | (45,327) | - | (47,530) |
| Balance at December 31, 2014 | 1,545,214 | 2,357,612 | - | 3,902,826 |
| **Net Book Value** | | | | |
| - Balance at January 1, 2013 | 4,733,691 | 906,488 | 50,434 | 5,690,613 |
| - Balance at December 31, 2013 | 5,560,302 | 926,305 | 91,063 | 6,577,670 |
| - Balance at December 31, 2014 | 5,466,855 | 838,138 | 24,084 | 6,329,077 |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 27. PROPERTY, PLANT AND EQUIPMENT (Continued)

The Bank had no buildings assigned under mortgage as collateral for the repayment of borrowings.

As a result of incomplete land registers, as at December 31, 2014, the Bank did not have title deeds as proof of ownership for 38 buildings and land lots stated at the net book value of RSD 1,726,221 thousand. The Bank's management has taken all actions necessary to obtain the appropriate property titles for these buildings.

Based on the annual count of assets, permanently unusable items of property, plant and equipment with the net book value of RSD 4,842 thousand were retired and derecognized from the Bank's records.

## 28. INVESTMENT PROPERTY

28.1 Movements on the account of investment property in 2014 and 2013 are presented below:

| | Total |
|---|---|
| **Cost** | |
| Balance at January 1, 2013 | 1,907,716 |
| Transfer from investments in progress (Note 27.2) | 299,195 |
| Transfer to property (Note 27.2) | (154,350) |
| Appraisal (revaluation) – decrease | (52,000) |
| Balance at December 31, 2013 | 2,000,561 |
| Balance at January 1, 2014 | 2,000,561, |
| Transfer from investments in progress (Note 27.2) | 807,486 |
| Transfer from property (Note 27.2) | 7,001 |
| Appraisal (revaluation) – decrease | (4,216) |
| Balance at December 31, 2014 | 2,810,832 |
| **Accumulated Depreciation** | |
| Balance at January 1, 2013 | 181,483 |
| Charge for the year (Note 16) | 33,116 |
| Transfer to property (Note 27.2) | (20,755) |
| Appraisal effect | (1,837) |
| Balance at December 31, 2013 | 192,007 |
| Balance at January 1, 2014 | 192,007 |
| Charge for the year (Note 16) | 36,584 |
| Transfer from property (Note 27.2) | 1,394 |
| Appraisal effect | (297) |
| Balance at December 31, 2014 | 229,688 |
| **Net Book Value** | |
| - Balance at January 1, 2013 | 1,726,233 |
| - Balance at December 31, 2013 | 1,808,554 |
| - Balance at December 31, 2014 | 2,581,144 |

As of December 31, 2014 the Bank stated investment property as totaling RSD 2,581,144 thousand comprised of leased out buildings/premises.

Pursuant to executed long-term lease agreements in 2014 the Bank transferred to investment property tangible assets acquired in lieu of debt collection (Beograd: Radnička 22 and Beogradska 39; Niš: Bulevar 12. februar bb and Gradina) totaling RSD 807,486 thousand.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 28. INVESTMENT PROPERTY (Continued)

28.2 As of December 31, 2014 the net profit realized form investment property amounted to RSD 35,896 thousand:

| Property | Area in $m^2$ | Total Expenses | Total Rental Income | Net Profit |
|---|---|---|---|---|
| Beograd, Makedonska 29 | 5,553 | (21,239) | 34,162 | 12,923 |
| Niš, Vrtište new D building | 1,816 | (556) | 3,939 | 3,383 |
| Niš, TPC Kalča | 85 | (800) | 3,370 | 2,570 |
| Beograd, Omladinskih brigada 19 | 15,218 | (14,172) | 15,952 | 1,780 |
| Šabac, Majur, Obilazni put bb | 1,263 | (870) | 1,543 | 673 |
| Lovćenac, Maršala Tita bb, | 46,890 | (3,772) | 8,414 | 4,642 |
| Negotin, Save Dragovića 20-22 | 658 | (1,032) | 701 | (331) |
| Gradina, border crossing | 60 | (62) | 847 | 785 |
| Niš, Bulevar 12. februar bb | 816 | (745) | 2,198 | 1,453 |
| Beograd, Radnička 22 | 7,190 | (1,570) | 5,383 | 3,813 |
| Beograd, Beogradska 39 | 460 | (533) | 4,738 | 4,205 |
| | | (45,351) | 81,247 | 35,896 |

## 29. CURRENT TAX ASSETS

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Current tax assets (paid monthly advance income tax payments for 2014 as prescribed by the Corporate Income Tax Law) | 73,835 | 712,700 |

During 2014 the Bank had a refund of the prepaid income tax from the Tax Administration in the amount of RSD 1,000,000 thousand. The income tax was prepaid as a result of the obligatory monthly advance income tax payments for the years 2013 and 2014 pursuant to the Corporate Income Tax Law and of the fact that in 2013 the Bank had no tax liabilities in this respect due to tax exemption of the interest income from debt securities of the Republic of Serbia and the National Bank of Serbia.

The prerequisite for the prepaid income tax refund was a field inspection conducted by the Tax Administration, which identified no irregularities in the Bank's calculation and payment of the corporate income taxes.

**NOTES TO THE FINANCIAL STATEMENTS**
**December 31, 2014**
*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 30. DEFERRED TAX ASSETS AND LIABILITIES

30.1 Deferred tax assets and liabilities relate to:

| | 2014 | | | 2013 | | |
|---|---|---|---|---|---|---|
| | Assets | Liabilities | Net | Assets | Liabilities | Net |
| Difference in net carrying amount of tangible assets for tax and financial reporting purposes | - | (64,287) | (64,287) | - | (105,617) | (105,617) |
| Effect of increase in deferred tax liabilities for securities available for sale and equity investments | 40,611 | (213,650) | (173,039) | - | - | - |
| Long-term provisions for retirement benefits | 26,750 | - | 26,750 | 42,088 | - | 42,088 |
| Impairment of assets | 60,142 | - | 60,142 | 53,291 | - | 53,291 |
| Assets based on calculation of public duties | 27 | - | 27 | 82 | - | 82 |
| **Total** | 127,530 | (277,937) | (150,407) | 95,461 | (105,617) | (10,156) |

30.2 Movements on temporary differences during 2014 and 2013 are presented as follows

| | Balance at January 1 | Recognized in Profit or Loss | Recognized in Equity | Balance at December 31 |
|---|---|---|---|---|
| Property and equipment | (105,617) | 40,696 | 634 | (64,287) |
| Securities | - | - | (173,039) | (173,039) |
| Long-term provisions for retirement benefits | 42,088 | (19,505) | 4,167 | 26,750 |
| Impairment of assets | 53,291 | 6,851 | - | 60,142 |
| Assets based on calculating public duties | 82 | (55) | - | 27 |
| **Total** | (10,156) | 27,987 | (168,238) | (150,407) |

| | Balance at January 1 | Recognized in Profit or Loss | Recognized in Equity | Balance at December 31 |
|---|---|---|---|---|
| Property and equipment | (57,760) | 55,145 | (103,002) | (105,617) |
| Long-term provisions for retirement benefits | 41,486 | 602 | - | 42,088 |
| Impairment of assets | 21,159 | 32,132 | - | 53,291 |
| Assets based on calculating public duties | 11 | 71 | - | 82 |
| **Total** | 4,896 | 87,950 | (103,002) | (10,156) |

**NOTES TO THE FINANCIAL STATEMENTS**
**December 31, 2014**
*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 31. NON-CURRENT ASSETS HELD FOR SALE AND ASSETS FROM DISCONTINUED OPERATIONS

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Non-current assets held for sale and assets from discontinued operations | 84,227 | 71,630 |
| | 84,227 | 71,630 |

Non-current assets held for sale:

| Property | Area in $m^2$ | Carrying Value |
|---|---|---|
| Jasika, business premises | 75.87 | 611 |
| Požarevac, M.Pijade 2, business premises | 790.82 | 31,839 |
| Požarevac, M.Pijade 2, business premises | 880.86 | 26,345 |
| Belgrade, Toše Jovanovića 7, business premises | 24.05 | 2,213 |
| Vrbas, M. Tita 49, business premises | 145.56 | 3,992 |
| Kruševac, Dositejeva bb, business premises | 431.51 | 19,227 |
| | | 84,227 |

The Bank's management still intends to realize the sale of all assets that were not sold during the past year.

## 32. OTHER ASSETS

Other assets comprise:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| ***In RSD*** | | |
| Fee receivables per other assets | 126,644 | 119,908 |
| Inventories | 144,119 | 157,876 |
| Assets acquired in lieu of debt collection | 3,225,648 | 1,968,810 |
| Prepaid expenses | 140,804 | 171,129 |
| Equity investments | 1,195,544 | 1,020,176 |
| Other RSD receivables | 1,729,226 | 4,469,560 |
| | 6,561,985 | 7,907,459 |
| *Impairment allowance of:* | | |
| Fee receivables per other assets | (61,494) | (56,482) |
| Assets acquired in lieu of debt collection | (188,336) | (141,357) |
| Equity investments | (448,581) | (446,954) |
| Other RSD receivables | (537,374) | (1,085,090) |
| | (1,235,785) | (1,729,883) |
| ***In foreign currencies*** | | |
| Other receivables from operations | 1,024,993 | 336,697 |
| Receivables in settlement | 809,686 | 323,250 |
| Other foreign currency receivables | 3,219 | 2,306 |
| | 1,837,898 | 662,253 |
| *Impairment allowance of* | | |
| Other receivables from operations | (94,922) | (60,913) |
| Receivables in settlement | (78,951) | (74,820) |
| | (173,873) | (135,733) |
| | 6,990,225 | 6,704,096 |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 32. OTHER ASSETS (Continued)

Implementation of the effective regulations as of December 31, 2014 and the modified contents of the line item of other assets required reclassification of equity investments from equity investments to other assets as shown in the following table:

| *Equity investments* | 2014 | 2013 |
|---|---|---|
| Equity investments in banks and other financial organizations | 143,383 | 135,667 |
| Equity investments in companies and other legal entities | 460,913 | 457,178 |
| Equity investments in non-resident entities abroad | 591,248 | 427,331 |
| | 1,195,544 | 1,020,176 |
| *Impairment allowance of:* | | |
| Equity investments in banks and other financial organizations | (26,683) | (25,266) |
| Equity investments in companies and other legal entities | (421,898) | (421,688) |
| | (448,581) | (446,954) |

Equity investments in banks and other financial organizations relate to: Euroaxis banka a.d., Moskva in the amount of RSD 78,386 thousand, AIK banka a.d., Niš in the amount of RSD 61,061 thousand, Jubmes banka a.d., Beograd in the amount of RSD 2,053 thousand, Union banka d.d., Sarajevo in the amount of RSD 1,874 thousand and Universal banka in bankruptcy in the amount of RSD 9 thousand.

Equity investments in companies mostly pertain to: 14. oktobar a.d., Kruševac in the amount of RSD 324,874 thousand, RTV Politika d.o.o., Beograd in the amount of RSD 37,634 thousand, Kompanija Dunav osiguranje a.d., Beograd in the amount of RSD 50,737 thousand and Politika a.d., Beograd in the amount of RSD 39,187 thousand.

Equity investments in non-resident entities abroad relate to VISA Company in the amount of RSD 487,895 thousand and MASTER Card in the amount of RSD 103,353 thousand.

Impairment allowance of equity investments totaling RSD 448,581 thousand refers to the impairment of cost of those equity investments that have no market value, out of which the major portion refers to: 14. oktobar a.d., Kruševac - RSD 324,874 thousand, RTV Politika d.o.o., Beograd - RSD 37,634 thousand, Politika a.d., Beograd - RSD 28,484 thousand, Kompanija Dunav osiguranje a.d., Beograd - RSD 28,828 thousand and AIK banka a.d., Niš - RSD 19,287 thousand.

Other RSD receivables mostly refer to other receivables from operations totaling RSD 253,028 thousand, advances paid for working capital assets of RSD 81,704 thousand, rental receivables of RSD 369,862 thousand and interest receivables per other assets of RSD 268,543 thousand.

Other receivables from operations in foreign currencies for the most part pertain to receivables for purchase and sale of foreign currencies due from banks in the amount of RSD 725,750 thousand.

Movements on the allowance for impairment account related to other assets and prepayments during the year are presented in the table below:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Balance as at January 1 | 1,764,028 | 1,321,432 |
| Current year impairment allowance: | | |
| Charge for the year | 260,163 | 227,169 |
| Effects of the changes in foreign exchange rates | 9,486 | 736 |
| Reversal | (746,993) | (320,468) |
| Write-off | (1,530) | (10,056) |
| Other | 21,147 | 545,215 |
| **Balance as at December 31** | 1,306,301 | 1,764,028 |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 32. OTHER ASSETS (Continued)

Assets acquired in lieu of debt collection totaling RSD 3,225,648 thousand gross, less recorded impairment allowance of RSD 188,336 thousand, with the net book value of RSD 3,037,312 thousand relate to:

*Properties acquired in lieu of debt collection after December 30, 2013 – amounts included in the calculation of reserves from profit in accordance with the relevant NBS decision*

| Property | Area in $m^2$ | Value | Acquisition Date |
|---|---|---|---|
| | 434.58 | 4,959 | 17/04/2013 |
| CM Vukovac, CM Milatovac, arable land | 132,450.00 | 586 | 16/05/2014 |
| Bor, Nikole Pašića 21, buildings, warehouse, plant | 3,823.00 | 90,913 | 08/05/2014 |
| Aleksinac, arable land (fields, vineyards, pastures) | 36,787.00 | 243 | 09/07/2014 |
| Subotica, Magnetna 17, production plant, warehouse | 2,492.00 | 50,865 | 18/07/2014 |
| Reževići, Montenegro, karst, category 5 forest | 1,363.20 | 24,483 | 22/07/2014 |
| Reževići, Montenegro, category 5 forest | 5,638.54 | 86,600 | 22/07/2014 |
| Bajina Bašta, Vojvode Mišića 72/1, family house | 110.25 | 2,800 | 01/08/2014 |
| Mokra Gora, house, meadows pastures, fields | 58,400.00 | 11,901 | 31/01/2014 |
| Kopaonik, house and yard | 337.00 | 10,955 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 30a, business premises 6/3 | 29.00 | 4,421 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 30a, business premises 7/3 | 44.00 | 6,683 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 30a, business premises 8/3 | 35.00 | 5,347 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 30a, business premises 9/3 | 34.00 | 5,141 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 30a, business premises 10/3 | 39.00 | 5,963 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 88, business premises no. 1 | 266.00 | 122,923 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 88, business premises no. 2 | 57.00 | 26,393 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 88, business premises no. 11 | 44.00 | 6,858 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 88, business premises no. 22 | 226.00 | 60,474 | 31/01/2014 |
| Novi Sad, Bul.Oslobođenja 88, business premises no. 23 | 253.00 | 81,983 | 31/01/2014 |
| Novi Sad, Vardarska 1/b, business premises no. 1 | 291.00 | 48,629 | 31/01/2014 |
| Novi Sad, Tihomira Ostojića 4, business premises no. 7 | 134.00 | 17,664 | 31/01/2014 |
| Novi Sad, Polgar Andraša 40/a, business premises no. 8 | 81.00 | 10,702 | 31/01/2014 |
| Novi Sad, Polgar Andraša 40/a, business premises no. 9 | 79.00 | 10,495 | 31/01/2014 |
| Novi Sad, Polgar Andraša 40/a, business premises no. | 408.00 | 71,488 | 31/01/2014 |
| Zrenjanin, Bagljaš, Novosadski put 4, building, construction land, transformer substation, gas station, building in construction | 9,144.00 | 38,310 | 14/08/2014 |
| Beograd, Jurija Gagarina 153a, business premises | 30.00 | 6,538 | 27/08/2014 |
| Amerić, Mladenovac, category 3 and category 4 fields | 7,768.00 | 260 | 03/10/2014 |
| CO Kajtasovo, Bela Crkva, forest | 4,187.00 | 85 | 03/10/2014 |
| Mladenovac, Šepšin, fields, orchards | 25,136.00 | 551 | 03/10/2014 |
| Total I | | 815,213 | |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 32. OTHER ASSETS (Continued)

*Properties acquired in lieu of debt collection in prior periods (12 months before) – amounts included in the calculation of reserves from profit in accordance with the relevant NBS decision*

| Property | Area in m² | Value | Acquisition Date |
|---|---|---|---|
| Mur, Novi Pazar, house and category 3 orchard | 1,190.00 | 5,535 | 06/04/2012 |
| I.C.P Kruševac, commercial building | 12,836.00 | 49,982 | 08/06/2012 |
| Soko Banja, arable land (orchard, fields) | - | 3,230 | 31/07/2013 |
| Novi Pazar, Ejupa Kurtagića 13, house | 139.90 | 4,010 | 24/07/2012 |
| Majur, Tabanovačka, category 4 arable field | 1,445 ha | 1,671 | 10/08/2012 |
| Mladenovac, category 3 arable field | 16,633 | 274 | 22/11/2012 |
| Prokuplje, Maloplanska 7, two buildings and land | 490,00 | 314 | 11/06/2012 |
| Obrenovac, Mislođin, arable field | 10,017 | 1,078 | 11/07/2012 |
| Gnjilica, category 7 arable field | 2,638.00 | 115 | 11/06/2008 |
| Hotel President, Čačak, at Bulevar oslobođenja bb | 2,278.92 | 113,882 | 12/02/2009 |
| Residential building, Čačak, at Ratka Mitrovića 6 | 195 | 3,706 | 12/05/2009 |
| Novi Pazar, Kej skopskih žrtava 44, store | 82.95 | 3,435 | 27/09/2006 |
| Novi Pazar, yard and category 4 meadow | 1 ha 24 a | 181 | 26/08/2010 |
| Tivat, Mrčevac – residential building, ancillary facilities in construction and garage | 277 | 5,512 | 23/12/2010 |
| Tutin, Buče category 4 forest | 8,292 | 338 | 26/11/2010 |
| NBGD, Milentija Popovića 5b, apartment MZ S2 no.3 | 173 | 41,779 | 24/12/2010 |
| NBGD, Milentija Popovića 5b, apartment I S2 no.5 | 171 | 41,283 | 24/12/2010 |
| NBGD, Milentija Popovića 5b, apartment II S2 no.9 | 175 | 42,273 | 24/12/2010 |
| Tutin, Ostrovica, forest, field and pasture | 110,782 | 601 | 30/07/2012 |
| Mali Požarevac, Veliko polje, category 3 and 4 fields | 21,915 | 328 | 27/09/2012 |
| Mur, Novi Pazar, forest, field and orchard | 3,496 | 4,379 | 12/07/2011 |
| Budva, category 4 forest | 974 | 4,113 | 27/05/2011 |
| Prijevor, category 4 forest | 1,995 | 4,838 | 27/05/2011 |
| Residential building Galathea | 925 | 319,214 | 21/11/2011 |
| Vranje, field, category 2 vineyard | 2,339 | 1,858 | 29/11/2013 |
| Prijepolje, Karoševina, saw mill | 450 | 1,126 | 08/11/2013 |
| Ćuprija, Alekse Šantića 2/24, apartment | 72.40 | 924 | 15/01/2013 |
| Leskovac, Kralja Petra I, commercial building | 335 | 5,863 | 04/02/2013 |
| Niš, Ivana Milutinovića 30, business premises | 438.39 | 5,614 | 23/04/2013 |
| Niš, Triglavska 3/1, apartment | 79.80 | 3,609 | 04/06/2013 |
| Vranić, Milijane Matić 2, commercial building, ancillary facilities and land | 10,584.24 | 27,571 | 09/07/2013 |
| Mladenovac, field, category 3 forest | 1,142 | 506 | 18/07/2013 |
| Niš, Bulevar 12. februara, warehouse, ancillary facility | 2,062 | 45,931 | 31/07/2013 |
| Kula, Železnička bb, business premises, warehouse, transformer substation | 7,959 | 25,071 | 22/11/2013 |
| Total II | | 770,144 | |

*Properties acquired in lieu of debt collection after December 30, 2013 – amounts excluded from the calculation of reserves from profit in accordance with the relevant NBS decision*

| Property | Area in m² | Value | Acquisition Date |
|---|---|---|---|
| Beograd, Resavska 29, building | 1,944 | 404,637 | 03/06/2014 |
| Beograd, Resavska 31, building | 3,411 | 697,131 | 03/06/2014 |
| Zemun, Cara Dušana 130, factory complex | 6,876 | 243,235 | 16/06/2014 |
| Valjevo, Rađevo selo, warehouse | 394 | 483 | 11/06/2014 |
| Total III | | 1,345,486 | |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 32. OTHER ASSETS (Continued)

*Equipment acquired in lieu of debt collection in prior periods (12 months before)*

| Description | Value | Acquisition Date |
|---|---|---|
| Kruševac, movables (machinery, furniture, equipment) | 45,243 | 11/06/2012 |
| Niš and Soko Banja, movables (coffee processing line, transporters and cleaning equipment) | 34,701 | 31/07/2012 |
| Paraćin, coffee roasting line | 11,018 | 31/12/2012 |
| Vranić, equipment, production line | 10,843 | 09/07/2013 |
| Total IV | 101,805 | |

*Equipment acquired Equipment acquired in lieu of debt collection after December 30, 2013 – amounts excluded from the calculation of reserves from profit in accordance with the relevant NBS decision*

| Description | Value | Acquisition Date |
|---|---|---|
| Movables (installation materials, metal shelving) | 1,939 | 13/05/2014 |
| Equipment, inventories of waste materials | 2,660 | 18/07/2014 |
| Total V | **4,599** | |

*Equipment acquired Equipment acquired in lieu of debt collection after December 30, 2013 – amounts included in the calculation of reserves from profit in accordance with the relevant NBS decision*

| Description | Value | Acquisition Date |
|---|---|---|
| Peugeot 406, HDI | 60 | - |
| Thermal accumulation heater | 3 | - |
| Samsung TV set | 2 | - |
| Total VI | **65** | |
| TOTAL (net book value) I + II+ III+ IV+V+VI | **3,037,312** | |

During 2014 the Bank sold seven properties thus decreasing the value of the assets acquired in lieu of debt collection by the total of RSD 74,482 thousand (two apartments in Novi Beograd, two apartments in Niš, a commercial building in Niš, a house in Sombor and a commercial and residential building in Grabovica). The total sales price of the aforesaid properties amounted to RSD 83,072 thousand. The Bank does not hold ownership titles for 22 properties. The Bank's management is undertaking all the necessary actions to sell such properties.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 33. DEPOSITS AND OTHER LIABILITIES DUE TO BANKS, OTHER FINANCIAL INSTITUTIONS AND THE CENTRAL BANK

Deposits and other liabilities due to banks, other financial institutions and the central bank comprise:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Demand deposits | 6,230,123 | 1,587,917 |
| Term deposits | 1,139,880 | 6,079,898 |
| Borrowings | 16,467,781 | 13,380,370 |
| Expenses deferred at the effective interest rate (deductible item) | (142,034) | (122,469) |
| Other | 47,268 | 132,826 |
| **Balance as at December 31** | **23,743,018** | **21,058,542** |

Short-term RSD deposits placed by banks were deposited for periods of up to one year at interest rates ranging from 5.7 % to 9.1% per annum. In 2014 the Bank had no liabilities per long-term deposits placed by banks.

The largest portion of demand deposits relates to the transaction RSD deposit of Kompanija Dunav osiguranje a.d., Beograd amounting to RSD 4,822,226 thousand.

Newly enacted regulations define what extraterritorial organization and non-resident are regarded as banks and what as customers for the purposes of balance sheet preparation. This resulted in splitting and presenting the total liabilities per foreign loan facilities obtained in separate line items of the balance sheet, depending on the creditor.

Breakdown of long-term borrowings included within the line item of deposits and other liabilities due to banks is presented below:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| FEES | 5,926,957 | 5,011,497 |
| GAFF | 1,987,345 | 2,636,768 |
| FM | 2,419,166 | 2,292,842 |
| IF | 1,814,374 | - |
| EBRD | 4,319,939 | 3,439,263 |
| **Balance at December 31** | 16,467,781 | 13,380,370 |

The loan facility agreements executed with the creditors stipulate certain financial covenants. The methodology for calculating the financial ratios defined by loan facility agreements differs from the method for calculating those same ratios in accordance with the regulations of the National Bank of Serbia in part relating to the calculation of capital and includes items eligible for determining open credit exposure.

Pursuant to the loan agreements executed with the creditors listed in the table above, the Bank is obligated to comply with certain financial covenants until the final repayment of loans obtained. As of December 31, 2014, the Bank was in full compliance with all the contractually defined financial ratios toward the aforelisted foreign creditors.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 34. DEPOSITS AND OTHER LIABILITIES DUE TO CUSTOMERS

Deposits and other liabilities due to customers comprise:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| **Corporate customers** | | |
| Demand deposits | 50,212,715 | 40,407,356 |
| Other deposits | 24,092,376 | 20,082,972 |
| Borrowings | 12,694,050 | 13,326,230 |
| Earmarked deposits | 8,115,734 | 4,050,221 |
| Deposits for loans approved | 674,136 | 543,924 |
| Interest payable, accrued interest liabilities and other financial liabilities | 737,675 | 1,814,390 |
| **Retail customers** | | |
| Demand deposits | 14,399,711 | 11,222,105 |
| Savings deposits | 183,902,102 | 168,941,206 |
| Earmarked deposits | 2,148,492 | 1,169,896 |
| Deposits for loans approved | 1, 509,090 | 1,476,736 |
| Interest payable, accrued interest liabilities and other financial liabilities | 3,420,497 | 2,943,262 |
| Other deposits | 48,333 | 41,991 |
| **Balance at December 31** | 301,954,911 | 266,020,289 |

*Corporate Customer Deposits*

RSD demand deposits of corporate customers mostly comprise balances of transaction deposits of companies and other legal entities. In accordance with the Decision on Interest Rates for 2014, these deposits became interest-bearing. Depending on the average monthly balances on these transaction accounts of the customers, the interest rate applied thereto ranged from 0.25% and 1.5% per annum.

Foreign currency demand deposits of non-resident customers are non-interest bearing, except for specific business arrangements.

In 2014 short-term RSD deposits of corporate customers were placed at annual interest rates ranging between the key policy rate less 4 percentage points for deposits placed up to 7 days to key policy rate less 2.05 percentage points for deposits placed up to a year per annum.

Short-term foreign currency deposits of corporate customers were placed at an interest rate ranging between 0.25% and 2.15% annually for EUR deposits and 1.2% annually for deposits in other currencies.

Long-term RSD deposits of corporate customers were placed at an interest rate determined by the amount of the National Bank of Serbia key policy annual rate decreased by 1.7 percentage points, whereas those denominated in foreign currency accrued interest at the annual rate of 1.09% for other currencies and 2.75% for EUR.

In 2014 short-term deposits of corporate customers indexed to EUR exchange rate were placed at interest rates ranging from 0.5% to 1.3% annually.

Long-term deposits of corporate customers indexed to EUR exchange rate were placed at interest rates ranging from 1.6% to 1.9% annually.

*Retail Customer Deposits*

Demand RSD savings deposits of retail customers were placed at the annual interest rate of 0.15%, while foreign currency demand deposits accrued interest at the respective rates of 0.15% and 0.05% for EUR and other currencies per annum.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 34. DEPOSITS AND OTHER LIABILITIES DUE TO CUSTOMERS (Continued)

*Retail Customer Deposits (Continued)*

In 2014 short-term dinar RSD deposits of retail customers were placed at interest rates ranging from 4.25% to 8.5 % annually and those in foreign currencies at rates from 0.05% to 2.55% annually.

Long-term RSD deposits of retail customers were placed at interest rates ranging from 7.75% to 10.25 annually and those in foreign currencies at rates from 1% to 3.1% annually.

Newly enacted regulations define what extraterritorial organization and non-resident are regarded as banks and what as customers for the purposes of balance sheet preparation. This resulted in splitting and presenting the total liabilities per foreign loan facilities obtained in separate line items of the balance sheet, depending on the creditor.

Breakdown of long-term borrowings included within the line item of deposits and other liabilities due to customers is presented below:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| LEDIB 1 and 2 (Kingdom of Denmark) | 19,602 | 18,406 |
| Republic of Italy Government | 798,788 | 1,062,640 |
| European Investment Bank (EIB) | 5,629,831 | 5,781,447 |
| European Agency for Reconstruction (EAR) | 197,913 | 158,421 |
| KfW | 6,047,916 | 6,305,316 |
| **Balance at December 31** | 12,694,050 | 13,326,230 |

The above presented long-term borrowings mature in the period from 2014 to 2022.

The loan facility agreements executed with the creditors stipulate certain financial covenants. The methodology for calculating the financial ratios defined by loan facility agreements differs from the method for calculating those same ratios in accordance with the regulations of the National Bank of Serbia in part relating to the calculation of capital and includes items eligible for determining open credit exposure.

Pursuant to the loan agreements executed Kreditanstalt fur Wiederaufbau (German Development Bank, abbreviated: KfW), the Bank is obligated to comply with certain financial covenants until the final repayment of loans obtained. As of December 31, 2014, the Bank was in full compliance with all the contractually defined financial ratios toward the aforesaid foreign creditor.

## 35. SUBORDINATED LIABILITIES

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Foreign currency subordinated liabilities | 6,047,915 | 5,732,105 |
| Other liabilities (accrued interest liabilities) | 14,077 | 13,054 |
| Expenses deferred at the effective interest rate (deductible item) | (25,312) | (33,750) |
| **Balance at December 31** | 6,036,680 | 5,711,409 |

In accordance with the regulations of the National bank of Serbia related to the capital adequacy requirements and implementation of the Basel II Standard, in 2011 the Bank enhanced its core capital by obtaining a subordinated loan from the International Finance Corporation (IFC). The subordinated loan received totaled RSD 6,047,915 thousand, i.e., EUR 50,000 thousand as of December 31, 2014.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 36. PROVISIONS

Provisions relate to:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Provisions for off-balance sheet items (Note 14) | 568,424 | 473,647 |
| Provisions for litigations (Note 39.3) | 766,556 | 10,900 |
| Provisions for employee benefits in accordance with IAS 19 | 305,615 | 280,585 |
| **Balance at December 31** | 1,640,595 | 765,132 |

Movements on the accounts of provisions are provided below:

| | 2014 | | | | 2013 | | | |
|---|---|---|---|---|---|---|---|---|
| | Provisions for Off- Balance Sheet Items (Note 14) | Provisions for Litigations (Note 39.3) | Provisions for Employee Benefits (IAS 19) | Total | Provisions for Off- Balance Sheet Items (Note 14) | Provisions for Litigations (Note 39.3) | Provisions for Employee Benefits (IAS 19) | Total |
| Balance, January 1 | 473,647 | 10,900 | 280,585 | 765,132 | 497,632 | 1,557,557 | 276,571 | 2,331,760 |
| Charge for the year | 540,305 | 755,656 | 28,172 | 1,324,133 | 602,322 | 13,100 | 7,637 | 623,059 |
| Provisions against actuarial gains within equity | - | - | 27,779 | 27,779 | - | - | - | - |
| Release of provisions | - | | | | (49,399) | (1,178,087) | - | (1,227,486) |
| Reversal of provisions | (445,528) | - | (30,921) | (476,449) | (576,908) | (381,670) | (3,623) | (962,201) |
| **Balance at December 31** | 568,424 | 766,556 | 305,615 | 1,640,595 | 473,647 | 10,900 | 280,585 | 765,132 |

a) Comment on movements on provisions for litigations:

Based on the Belgrade Supreme Appellate Court ruling, in 2014 the Bank had a refund of the amount of RSD 755,656 thousand, which was transferred from the Bank's account for enforced collection in the previous year, in respect of the lawsuit involving the Bank and Ineks Intereksport a.d., Beograd (in bankruptcy). This ruling annulled the previous adjudication of the Commercial Court of Belgrade from 2013 and the case was referred to the first instance court for redeliberation. The Court ruled in favor of the Bank, i.e. the amount claimed shall belong to the Bank until the revised litigation is finalized. The Bank provided for this amount in full.

The Court accepted the Bank's request that the case be split into two separate cases given that the Republic of Serbia filed a lawsuit against the Bank on the same grounds. The total RSD amount of provisions of RSD 755,656 thousand relates to the following lawsuits:

- Lawsuit filed by the Republic of Serbia with the claim amount of USD 4,773 thousand and
- Lawsuit filed by Intereksport a.d., Beograd (in bankruptcy) with the claim amount of USD 1,948 thousand.

b) The main actuarial assumptions used in calculation of retirement benefits were as follows:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Discount rate | 8.75% | 11.25% |
| Salary growth rate within the Bank | 2.5% | 4% |
| Employee turnover | 5% | 5% |

The discount rate equaled the previous years' key policy rate of the National Bank of Serbia as of December 31, 2014.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 37. OTHER LIABILITIES

Other liabilities include:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Accounts payable | 198,960 | 253,193 |
| Liabilities to employees (salaries, payroll taxes and contributions and other liabilities to employees) | 272,955 | 54,339 |
| Advances received | 32,414 | 35,964 |
| Accrued interest, fees and commissions | 202,557 | 217,929 |
| Accrued liabilities and other accruals | 239,443 | 662,493 |
| Liabilities in settlement | 1,756,755 | 2,755,271 |
| Dividend payment liabilities | 277,367 | 150,124 |
| Taxes and contributions payable | 61,783 | 21,616 |
| Other liabilities | 146,875 | 107,644 |
| **Balance as at December 31** | 3,189,109 | 4,258,573 |

Liabilities in settlement totaling RSD 1,756,755 thousand mostly, in the amount of RSD 727,100 thousand and RSD 699,100 thousand, refer to the liabilities for sale and purchase of foreign currencies in the foreign exchange market and foreign currency liabilities for spot transactions, respectively.

Dividend payment liabilities refer to the liabilities to pay out preferred and convertible share dividend in the amount of RSD 123,900 thousand and liabilities for taxes relating to employees in the amount of RSD 153,468 thousand.

## 38. EQUITY

38.1 Equity is comprised of:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Issued capital | 17,191,466 | 17,191,466 |
| Share premium | 22,843,084 | 22,843,084 |
| Reserves from profit and other reserves | 20,635,440 | 16,635,440 |
| Revaluation reserves | 2,120,959 | 1,604,257 |
| Retained earnings | 6,755,855 | 6,687,971 |
| Balance as at December 31 | 69,546,804 | 64,962,218 |

The Bank's issued (share) capital was established through initial shareholder contributions and the ensuing issues of new shares. Shareholders have the right to manage the Bank as well as to shares in profit distribution. As of December 31, 2014 the Bank's share capital totaled RSD 17,191,466 thousand and comprised 17,191,466 shares with the individual par value of RSD 1 thousand.

Breakdown of the Bank's shares is provided in the table below:

| | Share Count | |
|---|---|---|
| **Share Type** | **December 31, 2014** | **December 31, 2013** |
| Ordinary shares | 16,817,956 | 8,709,310 |
| Preferred convertible shares | - | 8,108,646 |
| Preferred shares | 373,510 | 373,510 |
| Balance as at December 31 | 17,191,466 | 17,191,466 |

Pursuant to the Decision of the Bank' Shareholder Assembly on the 27th Issue of Ordinary Shares through Public Offering without Publishing Prospectus for conversion of preferred shares into ordinary shares, on November 24, 2014, the Bank converted 8,108,646 convertible preferred shares into voting shares. The aforesaid conversion affected the ordinary shares ownership percentages.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 38. EQUITY (Continued)

The largest portions of the Bank's voting shares are held by the Republic of Serbia (41.74% of ordinary shares) and EBRD, London (24.43% of ordinary shares).

The structure of the Bank's shareholders with ordinary (common stock) shares at December 31, 2014 was as follows:

| Shareholder | Share Count | % Interest |
|---|---|---|
| Republic of Serbia | 7,020,346 | 41.74 |
| EBRD, London | 4,109,440 | 24.43 |
| IFC Capitalization Fund LP | 1,706,810 | 10.15 |
| DEG Deutche Investitions | 772,850 | 4.60 |
| Swedfund International Aktiebo | 386,420 | 2.30 |
| Jugobanka a.d., Beograd in bankruptcy | 321,600 | 1.91 |
| Invej d.o.o., Beograd | 230,000 | 1.37 |
| East Capital (lux)-Balkan Fund | 208,106 | 1.24 |
| Evropa osiguranje a.d., Beograd in bankruptcy | 197,420 | 1.17 |
| Kompanija Dunav osiguranje a.d., Beograd | 171,380 | 1.02 |
| UniCredit bank, a.d., Srbija | 150,187 | 0.89 |
| East Capital(LUX) Eastern Europe | 125,408 | 0.75 |
| UniCredit bank, a.d., Srbija (*custody* account) | 125,205 | 0.74 |
| Stankom co. d.o.o., Beograd | 117,535 | 0.70 |
| Erste bank a.d., Novi Sad | 85,700 | 0.51 |
| Others (1,084 shareholders) | 1,089,549 | 6.48 |
| | 16,817,956 | 100.00 |

The structure of the Bank's shareholders with preferred shares at December 31, 2014 was as follows:

| Shareholder | Share Count | % Interest |
|---|---|---|
| Jugobanka a.d., Beograd in bankruptcy | 18,090 | 4.84 |
| Others (629 shareholders) | 355,420 | 95.16 |
| | 373,510 | 100.00 |

Revaluation reserves totaling RSD 2,120,959 thousand (2013: RSD 1,604,257 thousand) relate to the effects of increase in the value of property based on the independent appraisal amounting to RSD 1,032,462 thousand, net gains on the value adjustment of securities available for sale amounting to RSD 979,977 thousand and actuarial gains of RSD 108,520 thousand.

In 2014 prior years' dividends on preferred shares were paid in the amount of RSD 485,172 thousand (2013: RSD 40,342 thousand).

Within the line items of retained earnings and revaluation reserves adjustments were made to the actuarial gain amount based on the changes to the actuarial assumptions used in the previous period and applied in the current year amounting to RSD 132,132 thousand.

The basic earnings per share totaled RSD 253 or 25.25 % of a common share par value in 2014, whereas in 2013 the basic earnings per share amounted to RSD 468 or 46.75 % of a common share par value. Decrease in the earnings per share percentage in 2014 as compared to 2013 was due to the increase in the number of commons stock (ordinary) shares through conversion of preferred into ordinary shares.

| | 2014 | 2013 |
|---|---|---|
| Profit for the year less preferred share dividend | 4,246,824 | 4,071,705 |
| Weighted average number of shares outstanding | 16,817,956 | 8,709,310 |
| Basic earnings per share (in RSD) | 253 | 468 |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 38. EQUITY (Continued)

Diluted earnings per share totaled RSD 253 or 25.25% of a common share par value in 2014, whereas in 2013 the diluted earnings per share amounted to RSD 242 or 24.21% of a common share par value.

| | 2014 | 2013 |
|---|---|---|
| Profit for the year less preferred share dividend | 4,246,824 | 4,071,705 |
| Weighted average number of shares outstanding | 16,817,956 | 16,817,956 |
| Diluted earnings per share (in RSD) | 253 | 242 |

38.2 Tax effects related to the other comprehensive income for the year:

| | 2014 Gross | 2014 Tax | 2014 Net | 2013 Gross | 2013 Tax | 2013 Net |
|---|---|---|---|---|---|---|
| Increase due to fair value adjustments of equity investments and securities available for sale | 695,067 | (213,650) | 481,417 | 169,859 | - | 169,859 |
| Net decease due to actuarial losses | (27,779) | 4,167 | (23,612) | - | - | - |
| Valuation of property | (3,472) | 634 | (2,838) | 686,680 | (103,002) | 583,678 |
| Decrease due to fair value adjustments of equity investments and securities available for sale | (83,726) | 40,611 | (43,115) | - | - | - |
| Total | 580,090 | (168,238) | 411,852 | 856,539 | (103,002) | 753,537 |

## 39. CONTINGENT LIABILITIES AND OTHER OFF-BALANCE SHEET ITEMS

39.1 The Bank issues guarantees and letters of credit to vouch to third parties for the liability settlement by its clients. Such contracts have defined validity terms, which most commonly last up to a year. The contractual values of contingent liabilities are presented in the table below:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Payment guarantees (Note 4.1.1.) | 4,767,131 | 7,357,476 |
| Performance guarantees (Note 4.1.1.) | 7,883,510 | 5,787,610 |
| Letters of credit | 27,709 | 45,808 |
| Acceptances of bills of exchange | 27,185 | 37,737 |
| **Balance as at December 31** | 12,705,535 | 13,228,631 |

The above listed amounts represent the maximum amount of loss that the Bank would incur as at reporting date in the event that none of the Bank's clients were able to settle their contractual obligations (Note 4).

39.2 The breakdown of commitments is provided below:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Unused portion of approved payment and credit card loan facilities and overdrafts | 9,235,730 | 9,200,577 |
| Irrevocable commitments for undrawn loans | 7,311,860 | 7,640,316 |
| Other irrevocable commitments | 270,207 | 78,380 |
| Other commitments per contracted value of securities | 3,243,647 | 681,463 |
| **Balance as at December 31** | 20,061,444 | 17,600,736 |

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 39. CONTINGENT LIABILITIES AND OTHER OFF-BALANCE SHEET ITEMS

39.3 Litigation

Based on the expert estimate made by the Bank's Legal Department and attorneys at law representing the Bank, the Bank made provisions for potential litigation losses for all the legal suits filed against the bank in 2014 in the total amount of RSD 766,556 thousand (Note 36).

As of December 31, 2014 contingent liabilities based on legal suits filed against the Bank amounted to RSD 2,894,016 thousand (for 244 cases). The Bank's management anticipates no materially significant losses thereof in the forthcoming period.

In addition, the Bank is involved in legal suits against third parties where the most significant portion of the total claims amounted to RSD 27,323,175 thousand (for 552 cases with the largest individual claim amounts). The Bank's management anticipates favorable outcome of the most lawsuits.

39.4 Commitments for operating lease liabilities are provided below:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| Commitments due within one year | 450,325 | 455,767 |
| Commitments due in the period from 1 to 5 years | 1,190,071 | 1,300,046 |
| Commitments due in the period longer than 5 years | 230,741 | 100,511 |
| Total | 1,871,137 | 1,856,324 |

39.5 Other off-balance sheet items comprise managed funds and other off-balance sheet assets.

Funds managed on behalf and for the account of third parties are mostly comprised of assets for consignment loans of the Republic of Serbia, the largest portion of which, in the amount of RSD 3,716,372 thousand, relates to the long-term housing loans extended to retail customers. Other managed funds mostly refer to loans approved for agriculture and assets received from foreign grantors for micro loans.

Within other off-balance sheet assets, the Bank, among other things, records custody operations performed for the account of its clients, repo investments in Treasury bills and old FX savings bonds. As per its operating license to perform custody operations, the Bank maintains the financial instruments of its clients on the security accounts, recorded off balance. The Bank takes no credit risk in respect of managed funds.

Moreover, in accordance with the newly enacted regulations, other off-balance sheet assets include the value of the tangible assets received as collaterals securitizing loan repayment: residential and commercial real estate properties and other collaterals – pledge liens.

**NOTES TO THE FINANCIAL STATEMENTS**
**December 31, 2014**
*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 40. RELATED PARTY DISCLOSURES

40.1 The largest portions of the Bank's voting shares are held by the Republic of Serbia (41.74% of ordinary shares) and EBRD, London (24.43% of ordinary shares). The Bank has 3 subsidiaries: Komercijalna banka a.d., Budva, Komercijalna banka a.d., Banja Luka and KomBank Invest a.d., Beograd.

In the normal course of business, a number of banking transactions are performed with subsidiaries. these include loans, deposits, investments in equity securities and derivative instruments.

Related party transactions with subsidiaries were performed at arm's length.

### A. Balance as at December 31, 2014

**RECEIVABLES**

| Subsidiaries | Loans and Receivables | Interest and Fees | Other Assets | Net Balance Exposure | Off-Balance Sheet Items | Total |
|---|---|---|---|---|---|---|
| Komercijalna banka a.d., Budva | 6,442 | 862 | - | 7,304 | - | 7,304 |
| Komercijalna banka a.d., Banja Luka | 604,792 | - | 3,443 | 608,235 | - | 608,235 |
| KomBank INVEST a.d., Beograd | - | 1 | 3 | 4 | 197 | 201 |
| **Total:** | 611,234 | 863 | 3,446 | 615,543 | 197 | 615,740 |

**LIABILITIES**

| Subsidiaries | Deposits and Loans | Interest and Fees | Other Liabilities | Total |
|---|---|---|---|---|
| Komercijalna banka a.d., Budva | 117,835 | - | 1,689 | 119,524 |
| Komercijalna banka a.d., Banja Luka | 10,831 | - | - | 10,831 |
| KomBank INVEST a.d., Beograd | 9,757 | 3 | - | 9,760 |
| **Total:** | 138,423 | 3 | 1,689 | 140,115 |

**INCOME AND EXPENSES**

| Subsidiaries | Interest Income | Fee and Commission Income | Dividend Income | Interest Expenses | Fee and Commission Expense | Net Income/ Expenses |
|---|---|---|---|---|---|---|
| Komercijalna banka a.d., Budva | 12,674 | 2,122 | 120,689 | - | (1,317) | 134,168 |
| Komercijalna banka a.d., Banja Luka | 10,058 | 1,289 | - | - | (1,252) | 10,095 |
| KomBank INVEST a.d., Beograd | - | 56 | - | (25) | - | 31 |
| **Total:** | 22,732 | 3,467 | 120,689 | (25) | (2,569) | 144,294 |

Komercijalna banka a.d., Beograd realized net foreign exchange gains in the amount of RSD 202 thousand (2013: net foreign exchange losses of RSD 1,189 thousand) from related party transactions.

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 40. RELATED PARTY DISCLOSURES (Continued)

### B. Balance as at December 31, 2013

RECEIVABLES

| Subsidiaries | Loans and Receivables | Interest and Fees | Other Assets | Net Balance Exposure | Off-Balance Sheet Items | Total |
|---|---|---|---|---|---|---|
| Komercijalna banka a.d., Budva | 430,157 | 825 | 4,253 | 435,235 | - | 435,235 |
| Komercijalna banka a.d., Banja Luka | 232,271 | - | 2,646 | 234,917 | 343,926 | 578,843 |
| KomBank INVEST a.d., Beograd | - | 1 | - | 1 | 200 | 201 |
| **Total:** | 662,428 | 826 | 6,899 | 670,153 | 344,126 | 1,014,279 |

LIABILITIES

| Subsidiaries | Deposits and Loans | Interest and Fees | Other Liabilities | Total |
|---|---|---|---|---|
| Komercijalna banka a.d., Budva | 147,914 | - | 1,601 | 149,515 |
| Komercijalna banka a.d., Banja Luka | 9,228 | - | - | 9,228 |
| KomBank INVEST a.d., Beograd | 12,940 | 13 | - | 12,953 |
| **Total:** | 170,082 | 13 | 1,601 | 171,696 |

INCOME AND EXPENSES

| Subsidiaries | Interest Income | Fee and Commission Income | Dividend Income | Interest Expenses | Fee and Commission Expense | Net Income/ Expenses |
|---|---|---|---|---|---|---|
| Komercijalna banka a.d., Budva | 4,414 | 1,548 | 387,597 | - | (831) | 392,728 |
| Komercijalna banka a.d., Banja Luka | 2,639 | 628 | - | (390) | (293) | 2,584 |
| KomBank INVEST a.d., Beograd | - | 47 | - | (948) | - | (901) |
| **Total:** | 7,053 | 2,223 | 387,597 | (1,338) | (1,124) | 394,411 |

Komercijalna banka a.d., Beograd incurred net foreign exchange losses in the amount of RSD 1,189 thousand in 2013 (2012: RSD 4,662 thousand) from related party transactions.

40.2 Gross and net remunerations paid to the members of the Bank's Executive Board, Board of Directors and Audit Committee were as follows:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| **Gross remunerations** | | |
| Executive Board | 78,485 | 83,788 |
| **Net remunerations** | | |
| Executive Board | 67,031 | 71,179 |
| **Gross remunerations** | | |
| Board of Directors and Audit Committee | 30,540 | 26,845 |
| **Net remunerations** | | |
| Board of Directors and Audit Committee | 19,344 | 17,276 |

The Bank approved loans to the members of the Bank's Executive Board, Board of Directors and Audit Committee in the total amount of RSD 112,637 thousand (2013: RSD 119,725 thousand).

*All amounts expressed in thousands of RSD, unless otherwise stated.*

## 41. EVENTS AFTER THE REPORTING PERIOD

At its session held on January 26, 2015 the Bank's Shareholder Assembly enacted Decision on Adopting the Strategy and Business Plan for 2015 – 2017 Period.

In accordance with the Decision on Measures for Preservation of Financial System Stability in relation to loans indexed to foreign currency (the "Decision") issued by the National Bank of Serbia on February 24, 2015, the Bank assessed and calculated potential effects in respect of loans indexed to CHF. According to the aforesaid calculation, the Bank assessed that potential adverse effects, i.e., losses, in this respect will total up to RSD 110 million.

### Unreconciled Outstanding Item Statements

Based on the analysis of the regular annual asset/liability count performed as of December 31, 2014, the Bank had unreconciled outstanding item statements totaling RSD 11,007 thousand. Statements unreconciled with 40 customers mostly relate to the clients contesting the amount or the manner of calculation of interest and fees, those with accounts blocked or those contesting the amounts outstanding as per their respective reorganization plans.

### Unrealized Dividends

Unrealized dividends payable in 2015 amount to:

- RSD 538,753 thousand for 2014 (6.29 % of the nominal value of preferred shares).
- RSD 123,900 thousand for 2013 (9.91% of the nominal value of preferred shares).

## 42. EXCHANGE RATES

The official exchange rates for major currencies as determined in the interbank foreign exchange market and used in the translation of balance sheet components denominated in foreign currencies into dinars (RSD) as of December 31, 2014 and 2013 were as follows:

| | December 31, 2014 | December 31, 2013 |
|---|---|---|
| USD | 99.4641 | 83.1282 |
| EUR | 120.9583 | 114.6421 |
| CHF | 100.5472 | 93.5472 |

*3. ANNUAL REPORT ON BANK'S OPERATION*

KOMERCIJALNA BANKA AD BEOGRAD

# ANNUAL REPORT FOR THE YEAR 2014

February 27th, 2015

# CONTENTS

## *KEY PERFORMANCE INDICATORS*

| ITEM | 2014 | 2013 | Index 14/13 | 2012 | 2011 | 2010 |
|---|---|---|---|---|---|---|
| **INCOME STATEMENT** (RSD 000) | | | | | | |
| Profit before tax | 4.757.589 | 4.588.375 | 103,7 | 4.572.662 | 3.952.066 | 2.791.964 |
| Net interest income | 13.298.586 | 12.929.237 | 102,9 | 10.910.317 | 9.853.368 | 7.437.483 |
| Net fee income | 4.717.757 | 4.565.148 | 103,3 | 4.554.466 | 4.423.399 | 3.892.459 |
| **PROFITABILITY INDICATORS** | | | | | | |
| ROA | 1,2% | 1,3% | | 1,5% | 1,5% | 1,2% |
| ROE – on share capital | 11,9% | 11,5% | | 15,1% | 13,9% | 12,3% |
| ROE – on total capital | 7,1% | 7,3% | | 9,4% | 9,2% | 7,0% |
| Net interest margin on total assets[1] | 3,5% | 3,7% | | 3,6% | 3,8% | 3,1% |
| Cost / income ratio[1] | 59,6% | 58,0% | | 63,5% | 63,0% | 74,7% |
| Operating expenses (000 RSD)[2] | 10.745.910 | 10.161.794 | 105,7 | 9.812.888 | 8.995.578 | 8.462.471 |
| Net expenses from indirect loan write-off and provisions (000 RSD) | 2.725.389 | 3.220.075 | 84,6 | 1.444.299 | 1.335.461 | 1.416.354 |

| ITEM | 2014. | 2013. | Index 14/13 | 2012. | 2011. | 2010. |
|---|---|---|---|---|---|---|
| **BALANCE SHEET** (RSD 000) | | | | | | |
| Balance sheet assets | 406.261.524 | 362.786.319 | 112,0 | 323.384.909 | 275.488.718 | 255.868.309 |
| Off-balance sheet operations | 373.803.974 | 224.949.027 | 166,2 | 204.642.280 | 183.524.897 | 145.180.526 |
| **RETAIL**[3] | | | | | | |
| Loans | 69.039.387 | 61.848.487 | 111,6 | 55.917.000 | 48.555.491 | 45.372.699 |
| Deposits | 207.430.548 | 186.766.804 | 111,1 | 164.532.866 | 143.061.647 | 130.964.790 |
| **CORPORATE** | | | | | | |
| Loans | 112.768.251 | 112.261.312 | 100,5 | 118.860.421 | 98.486.288 | 90.244.925 |
| Deposits | 57.437.462 | 42.131.535 | 136,3 | 40.526.379 | 31.728.178 | 36.543.673 |

| ITEM | 2014. | 2013. | 2012. | 2011. | 2010. |
|---|---|---|---|---|---|
| **LOANS TO DEPOSITS RATIO** | | | | | |
| Gross loans /deposits | 72,4% | 77,8% | 80,2% | 80,7% | 80,9% |
| Net loans/deposits | 66,3% | 72,0% | 75,2% | 75,5% | 75,6% |
| **CAPITAL** (RSD 000) | 69.546.804 | 64.962.218 | 59.866.560 | 44.275.566 | 41.054.428 |
| Capital adequacy ratio | 17,7% | 19,0% | 21,9% | 17,3% | 17,1% |
| Number of employees | 2.906 | 2.966 | 2.989 | 3.022 | 3.101 |
| Assets per employee ( EUR 000) | 1.156 | 1.067 | 951 | 871 | 782 |

1 Due to application of new „unwiding“ concept at the end of 2014, interest income decreased by RSD 442,6 million
2 Within the operating costs are shown wages, material and non operating expenses

3Item „retail“ in part of loans includes retail clients, farms, entrepreneurs and micro clients

## *MACROECONOMIC OPERATING CONDITIONS*

2014 is the year of geopolitical tensions and uneven and slower than expected growth of global economy, despite numerous pro-cyclical measures and the significant „easing“ in the financial markets which, however, did not spread to consumption and investments, except in the Unites States, whose recovery is evident but the sustainability is still uncertain. The year was marked by political crisis in Ukraine, the introduction of sanctions against Russia, riots in the Middle East, a number of natural disasters a significant drop in oil prices as well as gold. Global repositioning is strong – China's GDP is for the first time higher than in the United States, the conclusion of the gas agreement between Russia and China, economic association of BRIKS countries...IMF lowered its growth forecast for the global economy this and next year, with the necessity for implementation of numerous and diverse structural reforms and a more powerful launch of infrastructure projects.

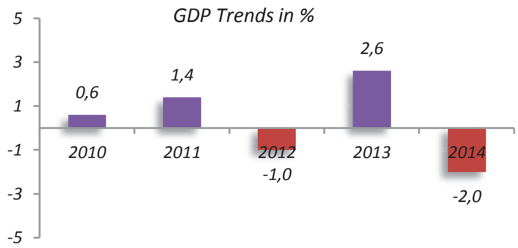
Slow and uneven growth, strong deflationary pressures and still high unemployment rate, with uncertain magnitude of the negative effect of the Ukrainian crisis characterize the European Union. There is a growing concern regarding the growth of the German economy, especially after the introduction of sanctions against Russia, while France and Italy are already on the verge of recession. Further effects are expected of relaxation of monetary policy of the ECB.

In Serbia 2014 was marked by formal start of EU accession negotiations, early parliamentary elections and the announcement of a number of structural reforms, in major part deferred due to catastrophic floods in May, which further slowed the growth and contributed to further deterioration of the economic environment. In November 2014 the negotiations with the IMF were finalized on a three-year stand-by precautionary arrangement (EUR 1,0 billion), which is expected to be concluded in February 2015.

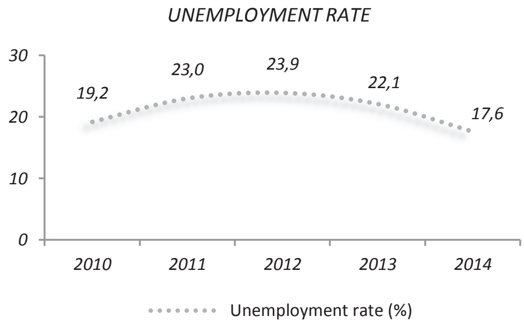
The risk premium for Serbia, measured by the EMBI index has increased and equals 309 b.p.

**GDP Trends**

According to first estimates, GDP dropped by 2% in 2014, compared to 2013 according to preliminary estimates of the Statistical Office of the Republic of Serbia. Broken down by sector, growth in GDP is recorded in agriculture, forestry and fishing, in sector of information and communication and in transport and storage. The fall in GDP was recorded in electricity supply sector, mining, construction, sector of financial activity and insurance. Industrial production in 2014 recorded a decline in the physical volume of production of 6,8 %[4] mainly due to the decline in sector of electricity production (as a result of flooding).




One of the key issues and indicators of economic activity, *unemployment*, has recorded a surprisingly large decline according to the October Labour Force Survey (from 20.3% in April 2014 to 17.6% in October 2014) and it is primarily the result of seasonal factors but also of the growth in the number of employees in the informal ("grey") economy. According to the Statistical Office the total number of formally employed in 2014 was 1,697,686 which represents a decrease of 1.0% compared to 2013. The largest decline in employment in case of legal entities was recorded in the financial activities and insurance (5.8%) and in construction (5.5%).




Source: Ministry of Finance of the Republic of Serbia

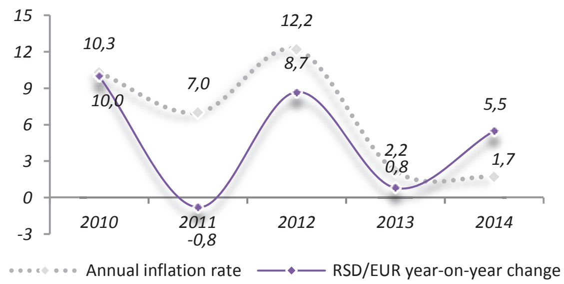
[4] Statistical Office of the Republic of Serbia

An important feature of 2014 is still present *insolvency* of a large part of the economy. The number of corporate clients, especially large ones, which from the liquidity problems fall into insolvency, is constantly growing with the growing trend of solving the problems through PPRP (pre-packaged reorganization plans). As of December 31st, 2014 the number of registered companies, according to data from the Serbian Business Registers Agency, was 115,692, this being an increase of 4.3% compared to 2013. 7740 companies were registered as being in the process of liquidation and in the process of bankruptcy 2062 companies[5]. In order to revive the economy, by the end of June 2014, a new Program of subsidized lending was launched from which, by the end of 2014, RSD 136 billion were disbursed (2014: EUR 1.124,9 million, in 2013 around EUR 320 million, 2012 around EUR 950 million ).

**Inflation**

After extremely high rates in previous years, the year-on-year inflation in the first two months of 2014 entered the limits of tolerance of 4±1,5%, and at the end of the year it ended below the lower limit of the target (1,7%).

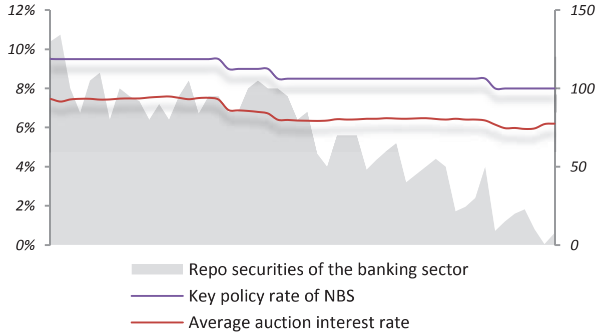
*RSD/EUR AND INFLATION 2010-2014*




It is a result of significant decline in aggregate demand, low prices of primary agricultural products, sudden and drastic decline in oil prices that occurred at the end of the financial year and the lack of the planned growth in regulated prices. The y-o-y core inflation (excluding energy, food, alcohol and cigarettes) at the end of December 2014 stood at 2,3%.

During 2014 the National Bank of Serbia, despite the significant weakening of inflationary pressures, maintained a high degree of monetary policy restrictiveness. The key policy rate at the beginning of the year stood at level of 9,5% only to lower to 9,0% in the month of May. Another reduction of the key policy rate was in mid-June (8,5%) and by the end of the year it decreased to the level of 8,0%. Additionally, the rates and currency structure of allocation of required reserves were changed (total rate of allocation is reduced by 1pp while allocation in RSD has been increased by 2pp). Further easing of the monetary policy of the National Bank of Serbia in the coming period will depend on monetary policies of the leading world economies in the following year (quantitative benefits and overcoming the problem of the borrowing limit by FED), announced new measures of the ECB, and internal factors, primarily the implementation of measures of fiscal consolidation.

*REPO TRANSACTIONS IN 2014.*

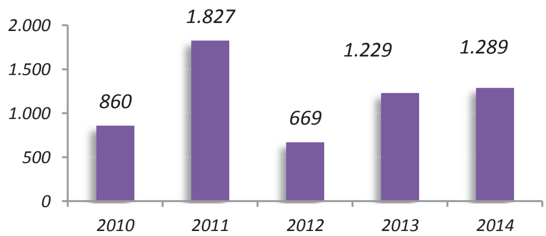



After abolishment of reverse and introduction of direct repo transactions in mid-2012, the banks were again enabled to invest liquid funds in T-bills, but by application of auction and multiple interest rates, which resulted in dividing the auction (lower) and key policy (higher) interest rate. Unlike the trend from 2013, in the course of 2014 the volume of repo transactions decreased during the year form the initial RSD 130 billion to a level of RSD 7,5 billion at the year end.

**Foreign Direct Investments**

Foreign direct investments reached at the end of 2014 the amount of EUR 1,3 billion[6] which is by EUR 112,9 million higher relative to the same period in 2013, or 40,7% greater than the amount in 2010 (note: since 2014 the reinvestment of profit is also included).

*FOREIGN DIRECT INVESTMENTS ( EUR mn)*



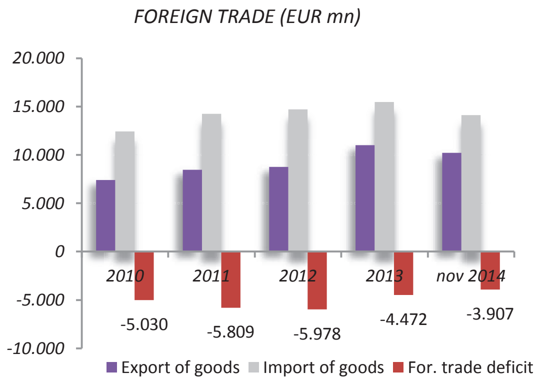

5 Serbian Business Registers Agency

6 Ministry of Finance of the Republic of Serbia

During 2014 a set of laws has been amended (Labour Law, Law on Privatization, Law on Bankruptcy...) in order to enhance the investment climate and to attract investors.
Investment portfolio net inflow amounted to EUR 424,7 million[7].

**Foreign Trade**

The total foreign trade of the Republic of Serbia, by the end of November 2014, reached the amount of EUR 24.3 billion[8], thus representing an increase of 22.6% compared to 2010 level. However, speaking year-on-year, exports in the third quarter of 2014 recorded a decline of 10.6% for the first time since the beginning of 2012.

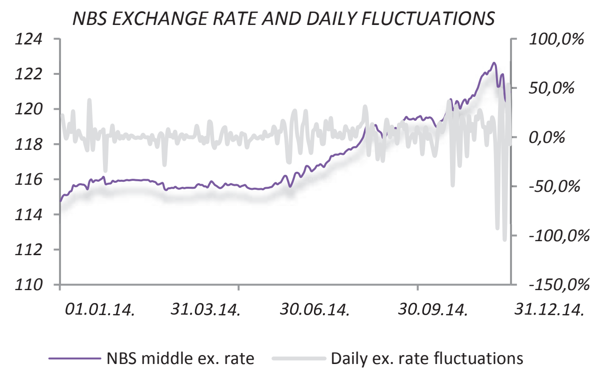



The company Fiat Automobiles Serbia doo Kragujevac (FAS), continues to be a leading exporter with exports volume of EUR 1.364 million (by the end of December 2014); it is followed by NIS ad Novi Sad, Tigar Tyres d.o.o. Pirot and Železara Smederevo d.o.o. Smederevo. Observed year-on-year, FAS however, in the fourth quarter alone recorded a decline in exports of EUR 98.8 million. Broken down by regions and countries, the EU countries accounted for 64.9% of total export, while the import from these countries accounts for 63.3% of total import. The main foreign trade partners from the EU are Italy and Germany which account for 29.7% of total export, while the import from the same countries accounts for 23.2% of total import.

**EUR/RSD Exchange Rate**

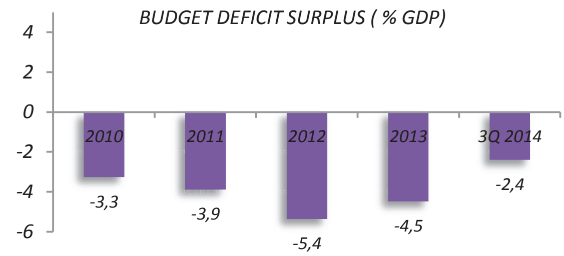
Global geopolitical crisis, reduced capital inflow, floods that in May afflicted Serbia and the region, unfavourable news about the sustainability of local public finances, increased energy import and weaker export, have influenced the EUR/RSD nominal exchange rate to fluctuate more in 2014 than in 2013. Greater exchange rate fluctuations have started since the end of July. In first nine months the exchange rate depreciated by 3,6%, or 5,4% for the whole year. In order to prevent drastic daily exchange rate fluctuations in 2014 the National Bank of Serbia intervened in FX market in both directions, by selling EUR 1.910 million and by purchasing EUR 260 million. Still important factor in establishing EUR/RSD exchange rate are foreign direct investments and portfolio investors.

At the end of December 2014 FX reserves of the National Bank of Serbia amounted to EUR 9,9 billion, which is sufficient for coverage of six month import of goods and services.




**Budget Deficit**

The consolidated budget deficit in 2014 amounted to RSD 187,5 billion, or 6,6% of GDP under the new methodology.




Source: National Bank of Serbia

Fiscal consolidation measures adopted in late 2013 proved to be inadequate – the budget deficit in 2014 is primarily the result of lower than planned income and high interest costs (3% of GDP). Budget revision adopted in October 2014 envisages reduction of wages in public sector and pensions, while other measures (some of the announced are the restructuring of public enterprises and abolishment of subsidies,

[7] Ministry of Finance of the Republic of Serbia
[8] Same

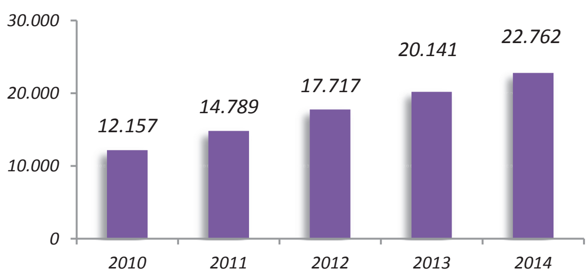
reducing the number of employees in public sector, the completion of privatization and enterprise restructuring) are defined by budget for 2015 and are agreed with the IMF in November 2014.

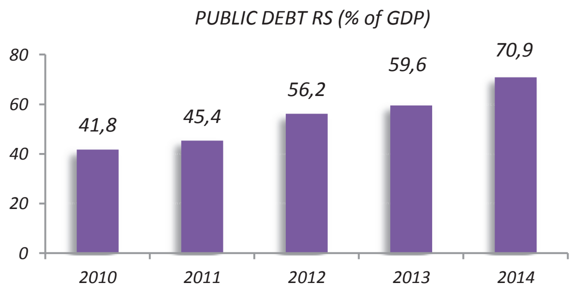
**Public Debt**

At the end of 2014, the public debt reached the level of 70,9%, despite the statutory limitation of 45% of GDP (Law on budget system)[9], primarily due to growing needs for financing of budget deficit. In 2014 the Government of the Republic of Serbia organized several auctions of securities of which the significant are the issues of five-year bonds in the month of January (EUR 50,0 million, yield 5,10%) and in the month of August (EUR 75,0 million, yield 5,00%), seven-year bonds in the month of March (RSD 10,0 billion, yield 13,00%), in the month of June (RSD 15,0 billion, yield 11,80%), and in the month of September (RSD 15,0 billion, yield 11,79%), and ten-year bonds (RSD 10,0 billion, yield 12,99 %). In addition, the government received the loan from UAE in the amount of USD 1,0 billion. After all, the public debt amounts to EUR 22,8 billion (+EUR 2,6 billion), and/or approximately 70,9% of GDP.

**External Debt**

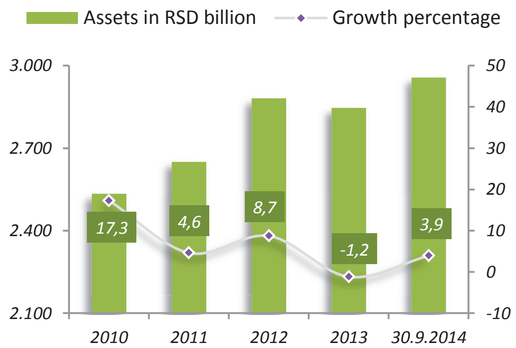
Due to reduced demand for loans the banks continued deleveraging abroad (EUR 814,5 million, December 2014) while the companies increased the indebtedness (EUR 77,2 million, December 2014), and thus the external debt increased by EUR 284,1 million compared to the end of 2013. Total external debt at the end of December 2014 amounted to EUR 26,0 billion[10]. The external debt of private sector decreased by EUR 736,2 million and amounted to EUR 11,8 billion, and the external debt of public sector increased by EUR 1,0 billion and amounted to EUR 14,2 billion.




BANKING SECTOR OF THE REPUBLIC OF SERBIA

At the end of 2014 the banking sector of Serbia comprised 29 banks with the assets of approximately EUR 24,8 billion, total capital of EUR 5,2 billion and 25.453 employees. During the year, among significant events those standing out are revocation of operating licence to Univerzal banka a.d. Beograd (January 2014), beginning of work of Telenor bank and issuance of operating licence to Mirabank from the United Arab Emirates.




Decline in lending activity in the first half of the year, has been halted by the Program of subsidized lending through which RSD 136,1 billion were disbursed. At the end of November 2014, according to the data of the National Bank of Serbia, gross loans have increased throughout 2014 by RSD 40,6 billion (and/or nominally 2,3% with exchange rate depreciation of 5,2%), retail loans recorded a growth (RSD 51,3 billion, or 7,6%, while corporate loans recorded a decline of RSD 10,8 billion, or 1,0%). As of November 30th, 2014, a significant part of funds have been invested in securities (RSD 448,3 billion), which is an increase of 33,1% relative to the end of 2013 (RSD 336,8 billion).

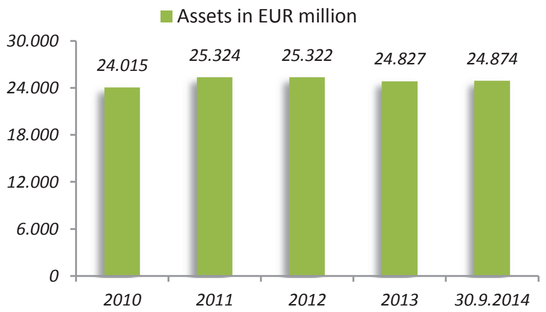
Share of *NPLs* (loans defaulting over 90 days), at the end of November 2014 reached the level of

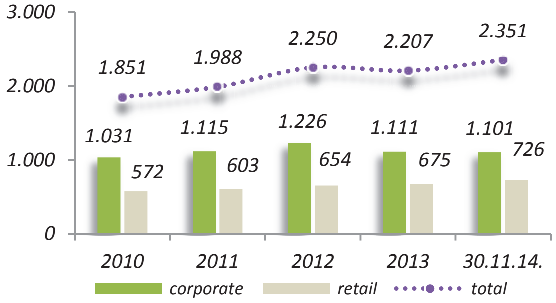
[9] Ministry of Finance of the Republic of Serbia
[10] National Bank of Serbia

22,5% (at the end of December 2013 it equalled 21,4%). Despite adopting the law that limited the deadlines for payments between commercial entities for up to 60 days, and payments by the state up to 45 days, increase in NPLs is a result of unfavourable overall business climate. In case of large corporate clients that have long resisted the influence of many years of economic crisis, in 2014 a problem showed up of regulating loan commitments (NPL of corporate clients 27,2%, and of retail clients 10,3%[11]). Impairment provision of total loans covers 56,7% of gross NPLs while coverage by statutory provisions equals 115,9% at the end of November[12]. Number of corporate clients, particularly large ones, which from the liquidity problems fall into insolvency, continually grows with the growing trend of solving the problems through PPRP (pre-packaged reorganization plans).

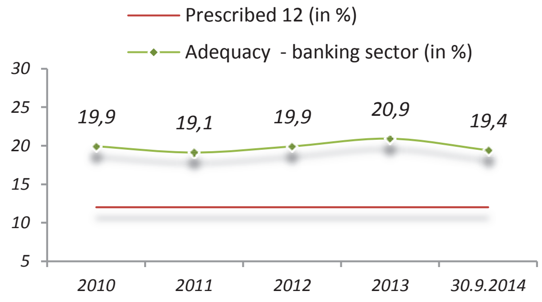
In order to solve accumulated NPLs the banks in first three quarters of 2014, through assignment of matured receivables to persons outside financial sector, released the amount RSD 7,2 billion [13].

*Retail foreign currency savings*, in 2014 continues to grow and by the end of the year (November) it reaches the amount of EUR 8,2 billion[14] with still high level of insured deposits (EUR 50.000).



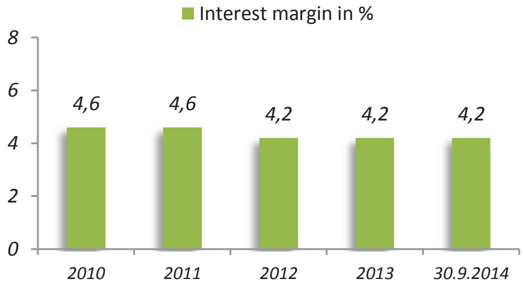




*Capital adequacy*, as of September 30th, 2014 equals 19,4, which is still significantly above the prescribed minimum of 12%. As of September 2014 the total capital of the banking sector amounts to EUR 5,2 billion e[15].



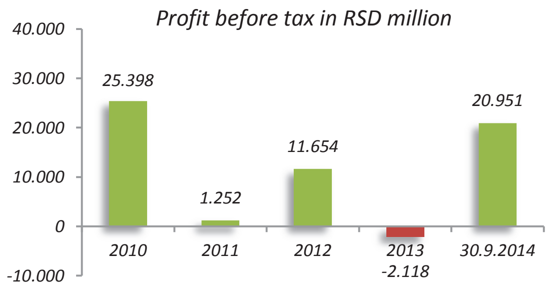

In 2014 as well, the outflow continues, or deleveraging of banks to foreign countries, which is a trend in operations of subsidiaries of the European banks in the region since mid-2011. By the end of November 2014 the outflow has been recorded in the amount of EUR 649 million.

*Profitability of banks* in 2014 has been growing but partially as a result of lack of large individual losses of the banks that have been recorded in the previous three years, and which have been closed in the meantime. Compared to the same period in 2013, the profit of the banking sector has been increased by 19,6%, but this growth resulted also from the loss which in the first three quarters of 2013 recorded KBC banka a.d. Beograd. After first three quarters of 2014, nine banks has been operating at a loss, twenty with profit of which only seven banks have ROE above 5%.

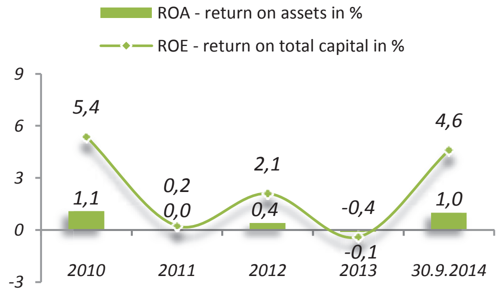



[11] Internet site of the National Bank of Serbia
[12] Same
[13] Same
[14] Same

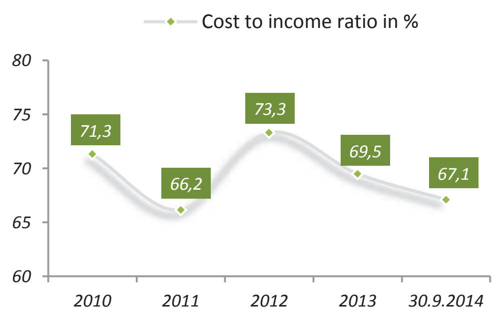
[15] Same




*Note: result before tax in 2011 includes the loss of Agrobanka of EUR 284 million, result at the end of 2012 includes the loss of Razvojna banka Vojvodina of EUR 128 million, and the result at the end of 2013 includes the loss of Univerzal banka of EUR 13 million.*




Factor that have a prevailing impact on profitability of banks in Serbia are high costs of credit risk, level of required reserve, focus on local funding sources, lack of demand of retail clients, limited number of quality corporate clients.




Cost-to-Income ratio continues the downward trend, after an increase in 2012, and reaches the value from the end of 2011.

The new Law on Accounting defined a new chart of accounts which is in effect as from December 31st, 2014, as well as the full implementation of IFRS, where significant changes are presented through application of unwinding concept, and/or recognition of interest income on impaired financial assets which are measured at amortized cost.

## 1. BUSINESS OPERATIONS AND ORGANIZATIONAL STRUCTURE

Within its registered activities the Bank performs the following operations:

1. Deposit operations (accepting and placing deposits),
2. Lending operations (lending and borrowing),
3. Foreign exchange, foreign exchange-currency and exchange operations;
4. Payment system operations;
5. Issuance of payment cards;
6. Securities operations (issue of securities, custody bank operations and other);
7. Broker-dealer operations;
8. Issuance of guarantees, sureties and other forms of guarantees (guarantee operations);
9. Purchase, sale and collection of receivables (factoring, forfeiting and other);
10. Insurance agency activities, upon prior consent of the National Bank of Serbia;
11. Operations for which it is authorized by the law;
12. Other operations which are essentially similar or related to the operations referred to in Items 1) to 11) of this paragraph, in line with the Agreement and the Bank's Articles of Association.

The Bank has been authorized for performing international payment transactions since 2003.

The Bank has been authorized for conducting the operations of a broker-dealer company since 2005.

Banka has been authorized to perform the activities of the custody bank since 2006.

### 1.1. Bank's Board of Directors

The Bank's Board of Directors has been established in accordance with the Law on Banks and the Agreement between the shareholders – Republic of Serbia and the group of international financial institutions (EBRD, IFC, DEG, SwedFund) and is composed of nine members, inclusive of the Chairman, of whom three members are persons independent of the Bank. The members of the

Bank's Board of Directors are appointed by the General Meeting of Bank's Shareholders for a period of four years.

The competences of the Bank's Board of Directors are defined by the Article 73 of the Law on Banks and Article 27 of the Bank's Articles of Association. The members of the Bank's Board of Directors as of December 31st, 2014 are as follows:

| NAME AND SURNAME | SHAREHOLDER/ MEMBER INDEPENDENT OF THE BANK | FUNCTION |
|---|---|---|
| *Professor Milovan Stanišić, PhD* | *Republic of Serbia* | *Chairman* |
| *Radomir Kostadinović* | *Republic of Serbia* | *Member* |
| *Miroljub Ćosić* | *Republic of Serbia* | *Member* |
| *Andreas Klingen* | *EBRD* | *Member* |
| *Philippe Delpal* | *EBRD* | *Member* |
| *Khosrow Zamani* | *IFC* | *Member* |
| *Ismail Musabegović, PhD* | *Member independent of the Bank* | *Member* |
| *Milan Šojić, PhD* | *Member independent of the Bank* | *Member* |
| *Mats Kjaer* | *Member independent of the Bank* | *Member* |

### 1.2. Bank's Executive Board

The Executive Board is composed of the President of the Executive Board, Deputy President of the Executive Board and of at least three members. The President of the Executive Board manages the work of the Executive Board and is responsible for implementing decisions within the competence of the Executive Board.

The term of office of the members of the Bank's Executive Board, including the President and the Deputy President is four years from the day of appointment.

The competences of the Executive Board are defined by the Article 76 of the Law on Banks and Article 31 of the Bank's Articles of Association.

The members of the Bank's Executive Board as of December 31st, 2014 are as follows:

| NAME AND SURNAME | FUNCTION |
|---|---|
| *Ivica Smolić* | *President* |
| *Dragan Santovac* | *Deputy President* |
| *Slavica Đorđević* | *Member* |
| *Andrijana Milanović* | *Member* |
| *Lidija Sklopić* | *Member* |

### 1.3. Audit Committee

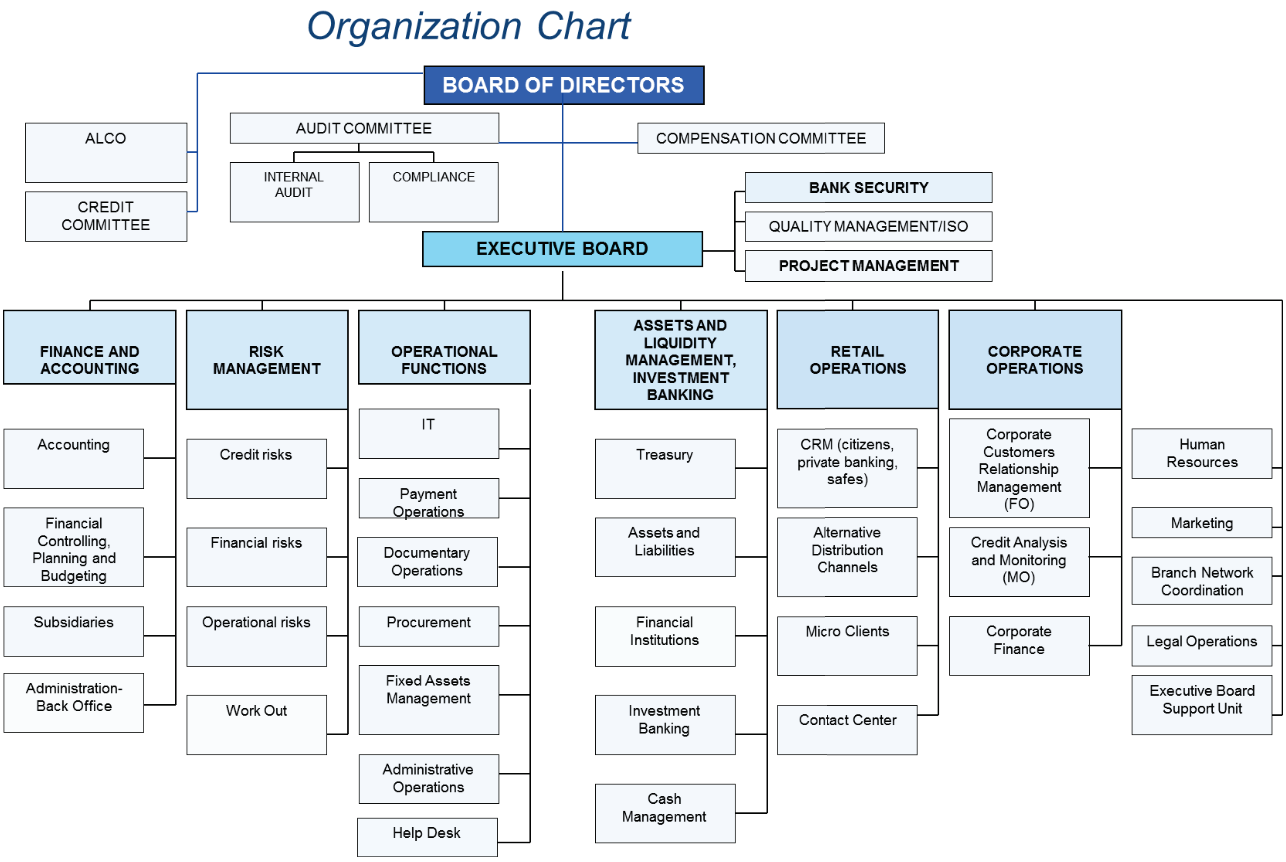
The Bank's Audit Committee is composed of three members, of whom two are the members of the Bank's Board of Directors with relevant experience in finance. One member of the Audit Committee is a person independent of the Bank. Members of the Audit Committee are appointed for a period of four years.

Duties of the Audit Committee are defined by the Article 80 of the Law on Banks and Article 34 of the Bank's Articles of Association.

The following are the members of the Audit Committee as of December 31st, 2014:

| NAME AND SURNAME | FUNCTION |
|---|---|
| *Mats Kjaer* | *Chairman* |
| *Andreas Klingen* | *Member* |
| *Radomir Kostadinović* | *Member* |

## 1.4. Organizational Structure



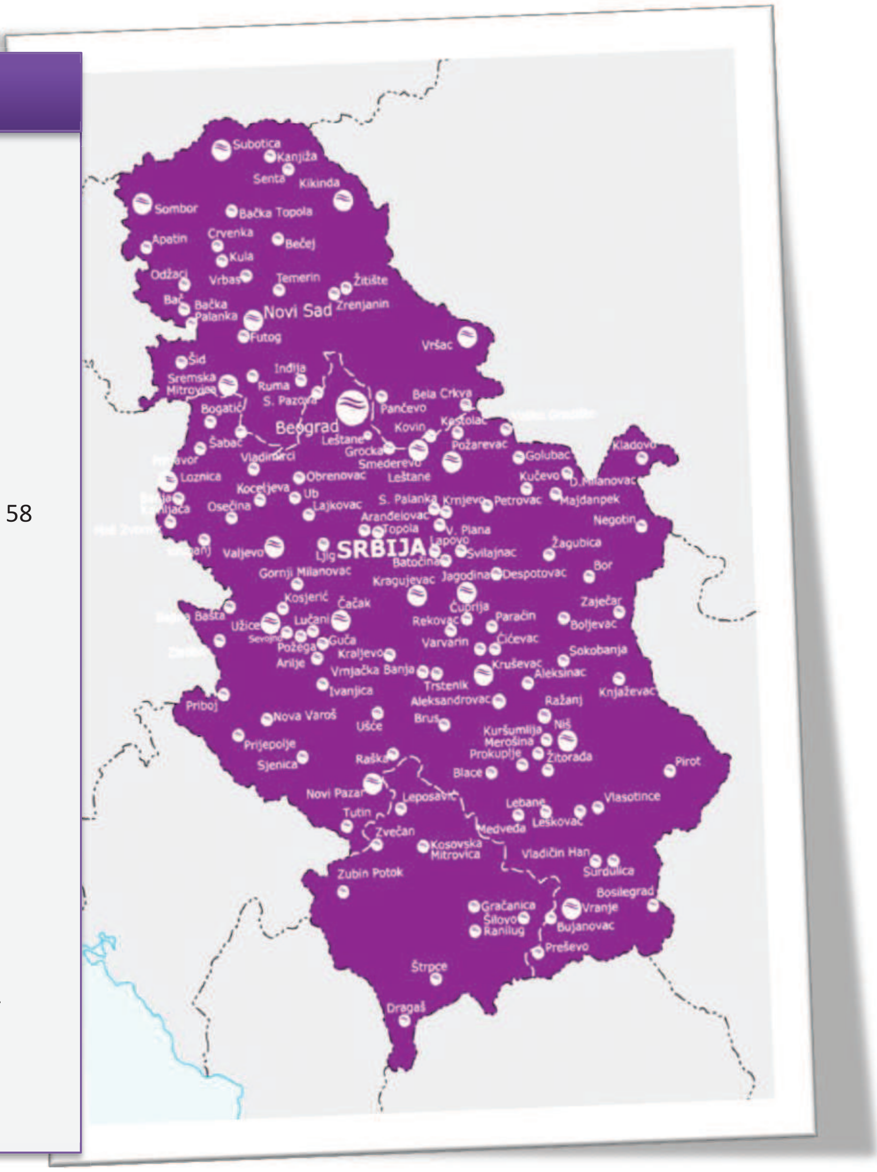

## 1.5. Locations of Bank's Head Office

| ADDRESS | Svetog Save 14 | Svetogorska 42-44 | Makedonska 29 |
|---|---|---|---|
| TELEPHONE | +381-11- 30-80-100 | +381-11-32-40-911 | +381-11-33-39-001 |
| TELEX | 12133 COMBANK YU | 12133 COMBANK YU | 12133 COMBANK YU |
| FAX | 3442-347 | 32-36-160 | 33-39-196 |
| S.W.I.F.T. code | KOBBRSBG | KOBBRSBG | KOBBRSBG |
| REUTERS code | KOMB | KOMB | KOMB |
| INTERNET | http:www.kombank.com | http:www.kombank.com | http:www.kombank.com |
| E-mail | posta@kombank.com | posta@kombank.com | posta@kombank.com |

*1.6. Regional Distribution of Bank's Branches in the Republic of Serbia*

## BRANCHES

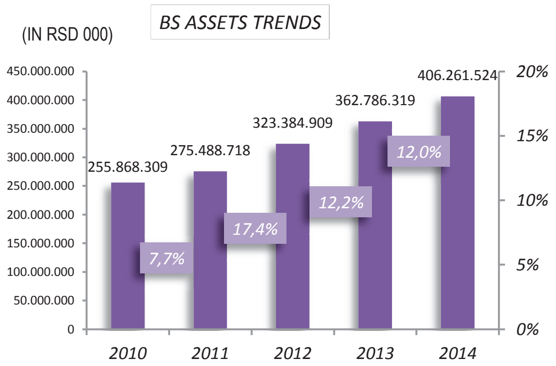
Niš -Episkopska 32
Kruševac-Trg Fontana 1
Kraljevo -Trg S. Ratnika bb
Novi Pazar -Njegoševa 1
Novi Sad -Novosadskog sajma 2
Užice -Petra Ćelovića 4
Zrenjanin -Trg Slobode 5
Čačak- Gradsko šetalište 10-14
Vranje -K. Stefana Prvovenčanog 58
Valjevo -Gradski Trg bb
Subotica -Korzo 10
Šabac -Gospodar Jevremova 2
Kragujevac-Save Kovačevića 1
Smederevo-Karađorđeva 37
Požarevac- Moše Pijade 2
Jagodina- Knjeginje Milice 10
Loznica- Gimnazijska 1
S. Mitrovica- Kralja Petra I 5-7
Zaječar-Nikole Pašića 25
Kikinda -Braće Tatić 7
Sombor-Staparski put 14
Vršac-Trg Sv. Teodora vršačkog 2
Beograd -Svetogorska 42-44
K. Mitrovica -Kneza Miloša 27

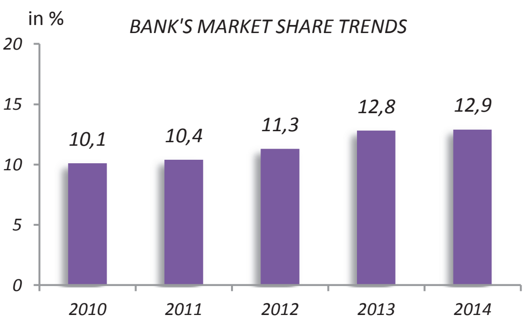


## 2. DEVELOPMENT OF THE BANK, FINANCIAL POSITION AND BUSINESS RESULTS

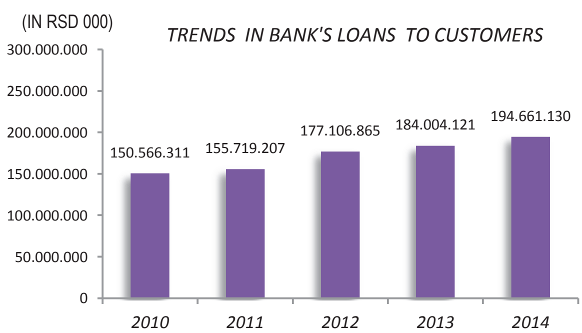
INTRODUCTION

In the previous five-year period the Bank accomplished a steady growth in relation to the banking sector and its main competitors. Looking at the results of the banking sector (balance as of September 30th, 2014) the Bank, with the balance sheet assets in the amount of RSD 380.099 million held 12,9% of the market, while at the end of 2010 it held 10,1%.

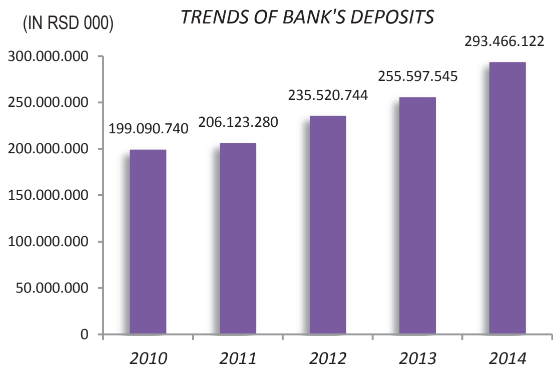


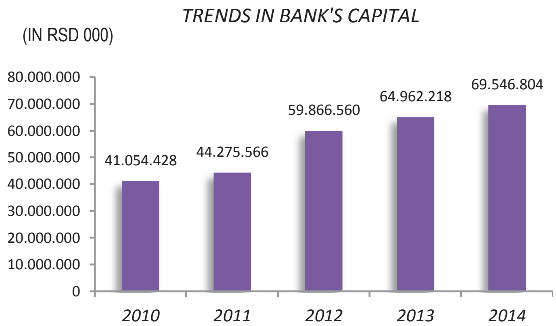

Item loans and deposits to customers [16], records a stable growth over the period 2010-2014, with an increase in Bank's market share from 9,2% to 11,5% (September 30th, 2014).



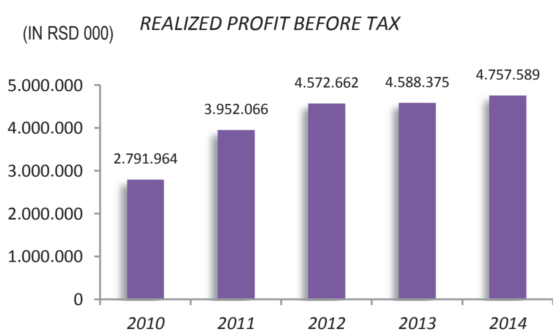

The collected deposits [17] also recorded a stable five-year growth from RSD 199.091 million and 13,2% of market share to over RSD 267.874 million and 14,8% of share (September 30th, 2014).




Broken down by share in sectors, the Bank has further strengthened the capital base from RSD 41.054 million to over RSD 68.341 million, respectively from 8,2% to 11,1% of the market (September 30th, 2014).




Profit before tax over the period 2010-2014 also records a slight growth from 11,0% to 13,4% of market share (September 30th, 2014), or from RSD 2,8 billion to over RSD 4,8 billion at the end of 2014.




[16] Item loans and deposits to customers does not include other placements

[17] Item deposits does not include other liabiilities and assets received through credit lines

## *2.1. Business Operations of Komercijalna banka in 2014*

All activities and operations of KB continue in 2014 to be focused to short-term sustainability and stability.

*Balance Sheet Total*

Growth of balance sheet total from RSD 43,5 billion or 12,0% to over RSD 406,2 billion (EUR 3,4 billion), is primarily a result of growth in collected deposits of customers (RSD 35.934,6 million or 13,5%). Focus is still on sustainable business operations, through a balance between profitability and portfolio quality, further optimization of the structure of assets, finding new sources of income and faster employment of funds.

*Sources*

In 2014 the growth of FX savings continued (EUR 55 million), but also the growth of deposits and other obligations towards the clients and the banks and other financial organizations (OFO) in the amount of RSD 38.619,1 million (under the new balance sheet format).

During 2014, credit lines were drawn in the amount of EUR 40 million: EBRD credit line for energy efficiency and the use of renewable energy source, in the amount of EUR 10 million, EFSE credit line for retail lending for improvement of housing conditions, renovations and extensions, (re)construction of real estate for people who live in them, in the amount of EUR 15 million and IFC credit line for financing the program pertaining to housing loans, also of EUR 15 million.

Subordinated liabilities at the end of the reporting year amount to RSD 6.036,7 million.

*Loans*

Despite the complex business conditions in the preceding business year, the Bank achieved the growth in corporate and retail loans and recorded a slight decline in loans to banks and OFO. The launching of the program of subsidized loans (since May 2014) resulted in growth of loans to customers, despite the present problem of quality demand for loans. Significant part of liquid funds was invested in RSD and FX securities. At the end of the year, RSD 95.481,2 million were invested in securities available for sale, which makes for an increase of RSD 38.596,0 million compared to the same period in 2013 (increase of 67,8%).

*Loan Portfolio Quality*

The operations of Komercijalna banka, as well as the rest of the sector, in 2014 were mainly marked by the problem of illiquidity, or insolvency of large corporate clients. The above problem placed even stronger focus on maintaining the portfolio quality. The growth of NPLs in the market is for the most part a consequence of excessive length of the crisis, failure to solve the problem of illiquid companies, but also the stagnation of sector's lending activity. The trend of corporate NPLs was mainly affected by the companies from the processing industry, trade, construction and by the companies in bankruptcy. The level of retail NPLs continued in 2014 to be significantly lower in comparison to companies (10,3%, November 2014 at the sector level[18]).

*Profitability*

Interest margin on total assets for 2014 equals 3,5%, which is a significant result in view of the pressures to reduce lending and debit interest rates. Strong pressures of loans on the interest margin have continued; the lack of quality demand and huge competitive pressure on limited number of quality clients affect the cost-to-risk ratio, which along with high level of required reserve make for main factors that exert adverse impact on the interest margin. Optimization of interest margin in 2014 is a result of further optimization and diversification of sources of funds, whereas the key factor for overall profitability is still the quality of assets, but also the additional unplanned deposit insurance premium, which increased the operating costs by RSD 440 million.

*Capital Adequacy*

Capital adequacy at the end of the reporting period equalled 17,7% which represents a satisfactory level in view of the environment, regulatory requirements and the requirements of the Bank to cover all business risks, primarily the credit risk. The capital base is stable and at the required level.

*Description of changes in business policies of the company*

During 2014 the Bank did not make changes in the document Business Policy. The Bank's Business

[18] National Bank of Serbia

Policy was adopted at the General Meeting of Bank's Shareholders held on January 26th, 2012.

The Business Policy determines the basic principles of operations and defines the activities performed by the Bank in order to achieve the business results and the priorities defined by the applicable Strategy and Business Plan of the Bank, which is based on the following:

- Bank's position in the financial market and the gained trust of the customers in the Bank.
- Projections of the basic parameters of macroeconomic policy.
- Development goals of the Bank.

The Bank's Business Policy is also compliant with the Risk Management Strategy and the Capital Management Strategy, as well as with the Individual Risk Management Policies.

The Bank operates independently, according to market principles, by applying the principles of liquidity, profitability and safety, while observing the laws, other regulations and general principles of banking operations in achieving its goals in a socially responsible manner, in accordance with the fundamental values and business ethics.

## *2.2. Corporate Banking Operations*

Market – key tendencies

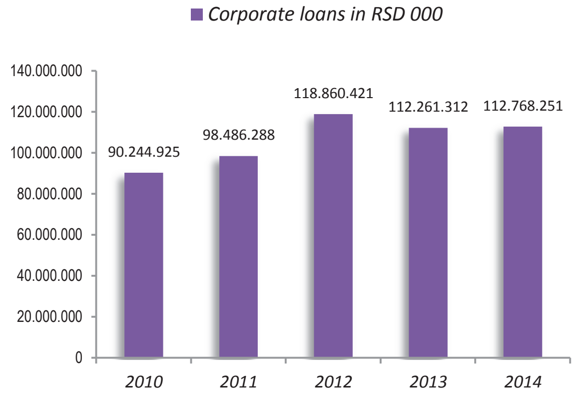
An absence of investment activities as well as the reluctance of clients to borrow more marked 2014 as well. Until the Program of subsidized lending to corporate entities was launched (end of May) there had been constant decline in the banking sector exposure to the economy. According to NBS data (Statistical Bulletin for the month of November) decrease in banks' engagement with corporate entities in 2014 amounts to RSD 10,8 billion.

*Loans[19] - operations of KB*

| CORPORATE | 31.12.2014. | | 31.12.2013. | | Growth in %, 14/13 |
|---|---|---|---|---|---|
| | amount in RSD 000 | share (%) | amount in RSD 000 | share (%) | |
| RSD LOANS | 112.768.251 | 100,0% | 112.261.312 | 100,0% | 0,5% |
| Short-term | 17.322.551 | 15,4% | 16.768.501 | 14,9% | 3,3% |
| Long-term | 83.312.970 | 73,9% | 83.336.753 | 74,2% | 0,0% |
| FX LOANS | 12.132.730 | 10,8% | 12.156.058 | 10,8% | -0,2% |
| Short-term | 784.774 | 0,7% | 962.905 | 0,9% | -18,5% |
| Long-term | 11.347.956 | 10,1% | 11.193.153 | 10,0% | 1,4% |

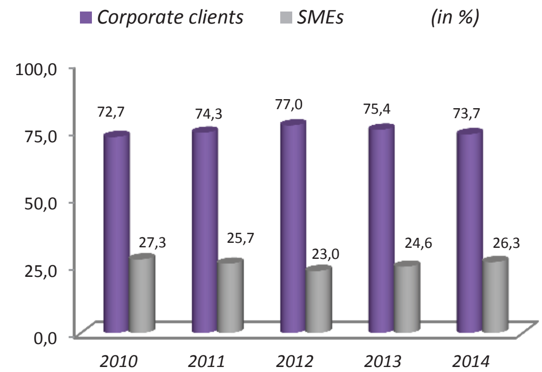
[19] Item loans and deposits to customers does not include other loans and advances

In order to alleviate the effects of the poor market environment and to stimulate the demand, before the Program of subsidized lending the Bank launched KOM PROGRESSIVE program (the mix of credit and non-credit products) intended to SMEs. The Bank has taken significant participation in the Program of subsidized lending (RSD 12,1 billion disbursed), through which 70% of total number of clients in segment of small, medium and macro enterprises borrowed. In segment of small enterprises the Bank ranked first in the market in terms of amount of disbursed loans (RSD 7,6 billion disbursed).




The fact that the subsidized loans were available exclusively in RSD led to significant share growth of RSD loans in loan portfolio (December 31st, 2014); share of RSD loans 22,8%, growth by 5,4 p.p. in comparison to the end of 2013).

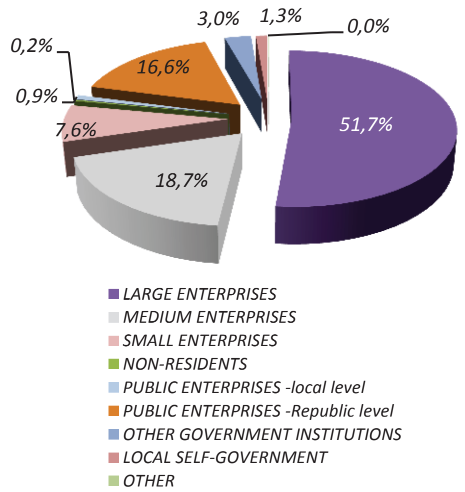
In 2014 there was a slight growth of share of short-term loans.

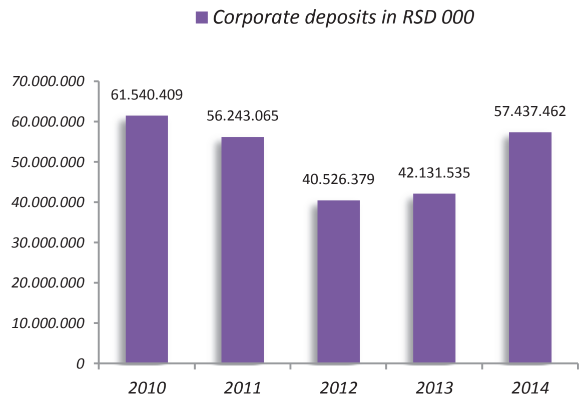



The huge competitive pressure to reduce interest rates, the portfolio decline due to early repayment of loans in the first half of the year as well as the effect of unwinding (in the amount of RSD 315,8 million) resulted in significant reduction in interest income in 2014. As regards the competition

Sberbank Srbija a.d. Beograd, Erste bank a.d. Novi Sad and ProCredit Bank a.d. Beograd have noticeably stepped up their activities while Banca Intesa a.d. Beograd, Raiffeisen banka a.d. Beograd and UniCredit bank Srbija a.d. Beograd keep their activities at its usual high level.

*Structure of clients as of 31.12.2014*



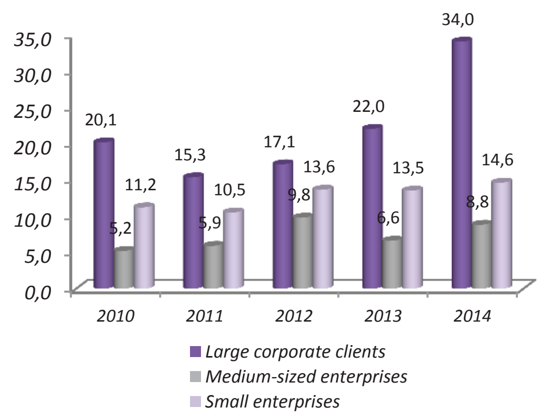




Following a decline in corporate deposits in 2012 and 2013, in 2014 the Bank achieved the growth of deposits

## Deposits [20]

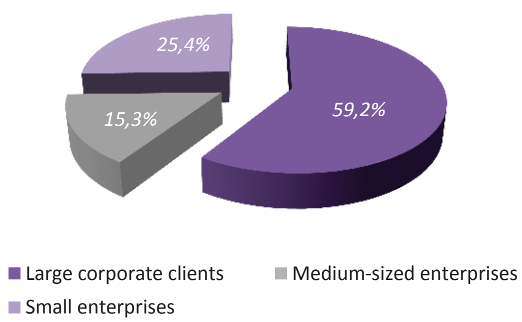
| CORPORATE | 31.12.2014 | | 31.12.2013 | | Growth in %, 14/13 |
|---|---|---|---|---|---|
| | amount in RSD 000 | share (%) | amount in RSD 000 | share (%) | |
| DEPOSITS | 57.437.462 | 100,0% | 42.131.535 | 100,0% | 36,3% |
| RSD DEPOSITS | 37.761.817 | 65,7% | 29.007.305 | 68,8% | 30,2% |
| Transaction | 24.005.453 | 41,8% | 20.539.213 | 48,8% | 16,9% |
| Other | 13.756.364 | 24,0% | 8.468.092 | 20,1% | 62,4% |
| FX DEPOSITS | 19.675.645 | 34,3% | 13.124.230 | 31,2% | 49,9% |
| Transaction | 10.352.299 | 18,0% | 6.277.674 | 14,9% | 64,9% |
| Other | 9.323.346 | 16,2% | 6.846.556 | 16,3% | 36,2% |

*Structure of corporate deposits in RSD billion*




Despite the reduction in debit interest rates and significantly deteriorated market conditions, and/or reduced liquidity of the economy, the growth has been recorded of corporate deposits of 36,3% as a result of the fall of the price sensitivity of customers, along with increase in sensitivity to reputation, or image of the banks, taking into account the circumstances and developments in the banking sector in 2014.

*Structure of depositors as at 31.12.2014*




[20] Item deposits does not include other liabilities and funds received through credit lines

## *2.3. Retail Banking Operations*

Market - key tendencies

General facts that have an impact on lending activity and characterize 2014 are as follows:

- High average unemployment rate of over 20% during 2014 (17,6% in the last quarter);

- The average debt is still relatively low compared to the other countries in the region and amounts to EUR 861 or 2,3 average salaries, of which EUR 780 in loans, EUR 32 in current account overdraft, EUR 43 in credit cards and EUR 6 in lease instalments[21];

- Since January 01st, 2014, the salaries of the employees in the public sector are reduced by the introduction of "solidarity tax" (20% personal income tax on salaries over RSD 60.000 or 25% personal income tax on salaries over RSD 100.000) which subsequently leads to decrease in demand by the highest quality segment of clients, in terms of taking loans;

- Instead of solidarity tax, in order to reduce the budget deficit, in October 2014, the Serbian Government adopted the *Decision on reduction of wages in public sector* (linear 10%) and on reduction of pensions in excess of RSD 25.000 as of November 2014;

- The difficulties in the operations of companies in private sector, which is reflected in the shift of a number of employees to a minimum guaranteed salary, as well as delays in payment of salaries, further affect the servicing of existing obligations towards the banks and the possibility of new borrowings.

Generally speaking, in spite of all the above and due to even more prominent limiting factors in corporate segment, the banks have still focused its operations on retail clients. Thus, according to the Association of Serbian Banks (ASB), the number of loan beneficiaries - retail clients in relation to the year 2013 increased by 42.687 which is actually the number of clients at the level in 2012.
On the other hand, activities in debt collection are slower and there is a stagnation of the defaulting loan users. Namely, the number of loan users - retail clients who are in default for over 90 days continuously, is practically the same as in 2013 (approximately 118.000). According to the data of the National Bank of Serbia, at the level of the banking sector there is an increase in share of NPLs in the total loans (as of 30 June 2014), and the same according to the latest data equals 10,3% (November 2014, while as at 31st December, 2013 it stood at 9,6%).

90% of the above mentioned increase in the number of clients using loans, according to ASB, refers to cash loans which proves that presently these loans are in highest demand in the market and particularly so in local currency. The competitors have taken quite an aggressive approach supported through constant different marketing campaigns aimed to lower interest rates, longer repayment periods and lower fees.

In the housing loan segment, since 2011, there has been a tendency of reduced demand, intensified in 2014, especially bearing in mind the abolishment of subsidies by the Republic of Serbia for the first time since 2006.

According to the National Mortgage Insurance Corporation (NMIC), in 2014 the total amount of disbursed housing loans was by 18.3% lower compared to 2013, while subsidized loans had a decrease of 61,5% and unsubsidized loans a slight growth of 4,9%. For subsidized loans, "belated" disbursement of loans under the program of the Government of the Republic of Serbia from the previous year existed until May, after which the subsidized loans intended for the army are only disbursed by AIK Banka ad Niš and Societe Generale Bank Serbia ad Belgrade.

**Housing loans insured by the NMIC without subsidies in EUR 000**

| Year | Banking sector | | KB | | Share of KB in the amount of |
|---|---|---|---|---|---|
| | Number | Amount | Number | Amount | |
| **2014** | **4.630** | **152.306** | **1.035** | **32.025** | **21,03%** |

**Subsidized housing loans in EUR 000**

| Year | Banking sector | | KB | | Share of KB in the amount of |
|---|---|---|---|---|---|
| | Number | Amount | Number | Amount | |
| **2014** | **790** | **29.970** | **96** | **3.377** | **11,27%** |

**Total disbursed housing loans in EUR 000**

| Year | Banking sector | | KB | | Share of KB in the amount of |
|---|---|---|---|---|---|
| | Number | Amount | Number | Amount | |
| **2014** | **5.420** | **182.276** | **1.131** | **35.402** | **19,42%** |

In order to stimulate demand in segment of corporate clients and entrepreneurs, at the end of the second quarter the Government introduced a program of subsidized liquidity loans, which led to growth of loans in the micro client segment.

21 Association of Serbian Banks

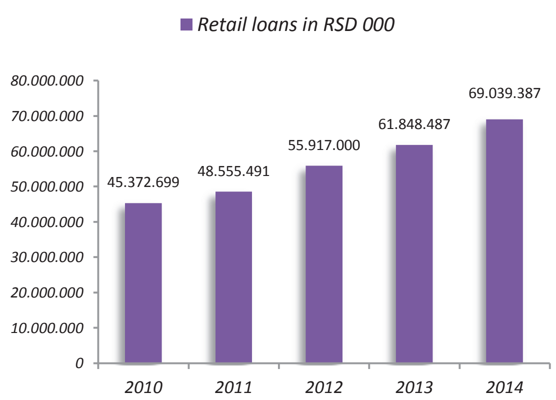
After a one year break in 2013, the Government continued with subsidized loans for agriculture in 2014.

Loans [22]- KB Operations

In 2014 loans were disbursed in the amount of RSD 24,2 billion, which is an increase by 14,4% in comparison to 2013. Disbursement has been increased in all segments except in segment of housing loans where due to lack of subsidies and reduced demand there is a decline of 19,1%. On the other hand, the biggest increase when compared to 2013 pertains to loans to micro clients (35,1%) and cash loans (27,1%). The Bank also managed to achieve a significant increase in agricultural loans, primarily by coordinating the subsidized and the loans from Bank's own lending potential, and also the loans from KFW credit line and by cooperating with dealers of agricultural machinery.

Cash loans accounted for the highest share of total loans approved in 2014 (42,6%), followed by loans to micro clients (25,7%) and housing loans (19%). This growth of retail loans has been achieved due to redesigning of the existing offer in terms of adjusting to market demands and maintaining the competitiveness by introducing new products in Bank's regular offer (in particular loans for pensioners with life insurance), launching discounted products and by increased engagement of Bank's business network. Additionally, the government subsidies make for significant contribution as do competitive credit lines for micro client and agriculture segment.

Of the total number of loans disbursed, 64% were denominated in dinars, while dinar-denominated loans account for 35,2% in total balance of retail loans.




22 Item loans and deposits to customers does not include other loans and advances

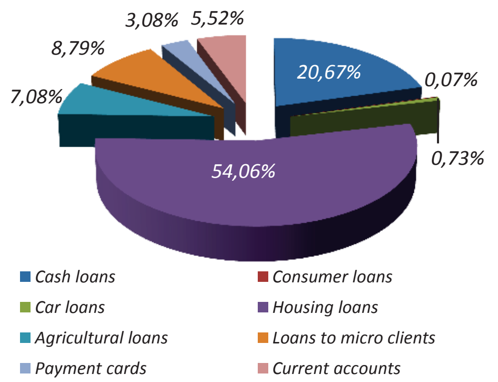
| Products | 31.12.2014 | | 31.12.2013 | |
|---|---|---|---|---|
| Types of loans | 000 RSD | % | 000 RSD | % |
| Cash loans | 14.269.953 | 20,67% | 12.021.153 | 19,44% |
| Consumer loans | 45.133 | 0,07% | 218.060 | 0,35% |
| Car loans | 502.485 | 0,73% | 891.478 | 1,44% |
| Housing loans | 37.325.144 | 54,06% | 33.340.228 | 53,91% |
| Agricultural loans | 4.885.651 | 7,08% | 3.848.933 | 6,22% |
| Loans to micro clients | 6.070.222 | 8,79% | 5.390.211 | 8,72% |
| Payment cards | 2.128.345 | 3,08% | 2.098.319 | 3,39% |
| Current accounts | 3.812.453 | 5,52% | 4.040.105 | 6,53% |
| Total | 69.039.387 | 100,00% | 61.848.487 | 100,00% |

In line with reduced demand and absence of government subsidies, car and consumer loans have been gradually decreasing.

Likewise, in segment of gross retail loans, according to the latest available data as at November 30th, 2014, the year-on-year Bank's growth equals 12,6%, and the growth of the banking sector 7,6%.

Interest income amounts to RSD 7,05 billion and records a growth compared to 2013 of 4,6%, whereas the fee income amounts to RSD 3,52 billion, which is an increase of 5,7%. Total net income amounts to RSD 5,57 billion, which is a significant increase of 27,1% in comparison to the preceding year.

STRUCTURE OF NET LOANS AND ADVANCES AS AT 31.12.2014



Payment Cards Operations

In the segment of payment cards operations the Bank focuses on the quality of its offer by introducing new products and services, improving the security of payments and maintaining a high quality of service. Below are some of the activities undertaken during the year 2014:

- Incentives for using PayPass cards at Bank's terminals and technological improvements;
- The promotional campaign "Use the card and win the gift" in cooperation with MasterCard and major acceptants
- New service: MasterCard Secure Code and Verified by Visa protection for online credit card payment.

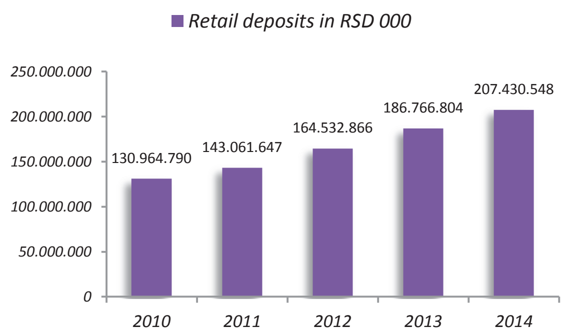
Compared to 2013, the following has been achieved:

- POS transactions increased by 12,4%, ATM transactions increased by 17,9%
- The number of issued cards increased by 16,5%;
- Interest-free sale in instalments: around 400 merchants and more than 1.200 locations.

All this, according to NBS data, contributed to Bank having a significantly faster growth in value of transactions (17,1%) compared to Serbian average (9,5%), which in turn increased its market share to 14,14%.

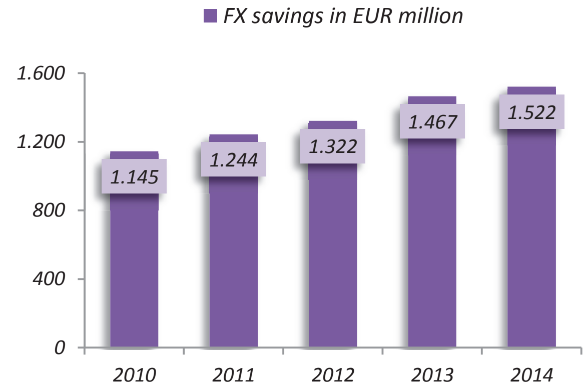
Deposits[23] - KB's Operations

At the level of the banking sector in 2014 (as of November 30th, 2014), a growth of FX deposits was EUR 66 million, while the Bank with its growth of EUR 59 million in 2014, despite the reduction in interest rates on several occasions, maintained its leading position in the market and increased its share to 19%.

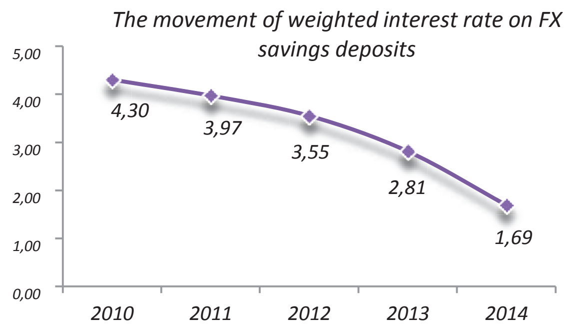



23 Item deposits does not include other liabilities and assets received through credit lines

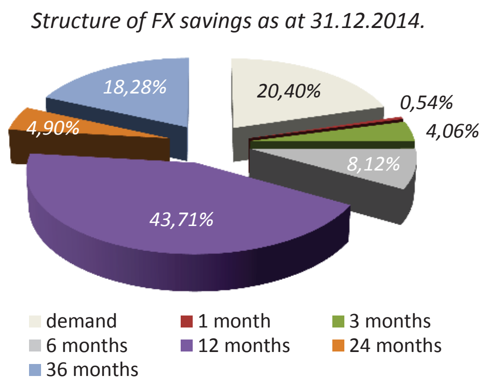
Under the existing market conditions, a proper balance has been struck between the cost, the Bank's image and brand and the desired stable growth of deposits.




* Presented FX savings do not include earmarked FX accounts (pensioners) and entrepreneurs.




It is evident that the weighted interest rate has a downward tendency.




In FX savings there is a stable share of deposits placed for a fixed term of up to and over 12 months, which stands at 60,7%, and there is also a prevailing share of deposits of up to EUR 50.000 (in terms of number over 99%, in terms of amount 80,5%).

The Bank will continue the active policy with respect to interest rates in order to maintain the balance between the cost and the desired growth of deposits with full utilization of Bank's brand.

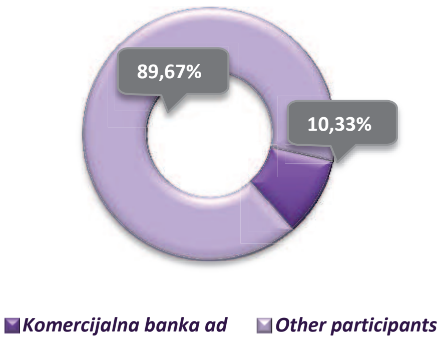
## *2.4. Treasury Operations*

Pursuant to the Bank's strategic orientation, the key objectives and business activities of the Treasury business function in 2014 focused on adequate liquidity management coupled with investment of free assets in the money and capital markets; support to operations with clients (retail and corporate) and ensuring the appropriate funding sources while reducing concentration and improving the maturity and currency match, thus successfully overcoming the limitations arising from the fact that there is no foreign parent bank, and/or global Treasury, and therefore inability to use favourable financial instruments and to exercise more flexibility in liquidity management.

In the last quarter of 2014 the National Bank of Serbia on two occasions reduced the foreign currency required reserve rate with concurrent changes in structure of allocation of FX required reserve (increase in allocation in dinars). In this way, the foreign currency liquidity was released to commercial banks in Serbia while sterilizing dinar liquidity which, in addition to the expected stabilizing effect on the foreign exchange market and the dinar exchange rate also had a significant impact on yields on government securities. Likewise, in 2014 there was a substantial spill over of short-term local currency placements (REPO with the National Bank of Serbia) in long-term investments in government securities and subsidized loans.

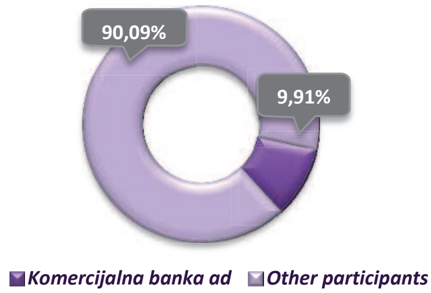
Through its policy of cautious investment in first-class financial instruments, in 2014 Komercijalna banka reaffirmed itself as one of the most active participants in the local financial market.

*Bank's share in investment in securities of the Republic of Serbia as of 31.12.2014*



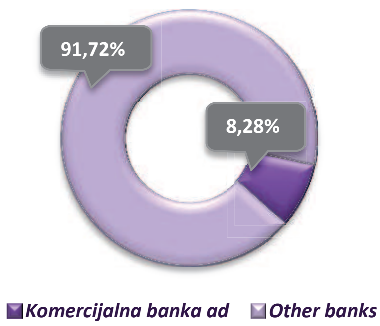

Extremely active participation of Komercijalna banka in the securities market was accompanied by the participation in the operations of the National Bank of Serbia on the open market – reverse REPO operations. In the course of 2014 the share of Komercijalna banka in total volume of reverse REPO operations in average stood at 9,91%. Compared to the preceding year this is a decrease by 40%.

*Bank's share in repo operations with NBS during 2014*




With total sales amounting to EUR 763 million and with total purchases amounting to EUR 810 million, Komercijalna banka is one of the most active participants in the foreign exchange market.

*Bank's share in FX sale and purchase between banks and residents in 2014*




By drawing down new credit lines in 2014, Komercijalna banka continued to rearrange its sources working towards achieving the mid-term objective of their full optimization. The effects achieved include both lower average cost of funds and greater flexibility in managing deposits.

Due to participation of the International Financial Institutions (IFIs) in its ownership structure and the earned international reputation of the first-class, safe bank, Komercijalna banka has facilitated access to international favourable funding sources. In 2014 Komercijalna banka used that fact to its advantage by attracting new credit lines from the international organisations, and agreeing credit lines which are expected to be disbursed in the course of 2015.

In 2014 the Bank drew a total of EUR 40 million in credit lines from IFIs to finance the needs of a wide range of clients, with different repayment terms depending on loan purpose. This enabled the Bank both to retain the existing clients and to attract the new ones with its offer of competitive products. In addition, the Bank provided for a better maturity match of funding sources /loans and advances, given the maturities of disbursed credit lines.

| | |
|---|---|
| *Overview of credit lines for 2014* | |
| EFSE European Fund for Southeast Europe | ***EUR 15.000.000, September 2014 (financing of end users (retail clients) for improvement of housing conditions, renovations, extensions, (re)construction and purchase of houses or housing units)*** |
| IFC International Finance Corporation World Bank Group | ***EUR 15.000.000, October 2014 (financing and extension of program of housing loans, to finance the purchase, renovation or reconstruction of real estate for people who live in them)*** |
| European Bank for Reconstruction and Development | ***EUR 10.000.000, December 2014 (financing of projects of energy efficiency and the use of renewable energy sources for private sector (small and medium-sized enterprises) and local self-government)*** |

## *2.5. Bank's Equity*

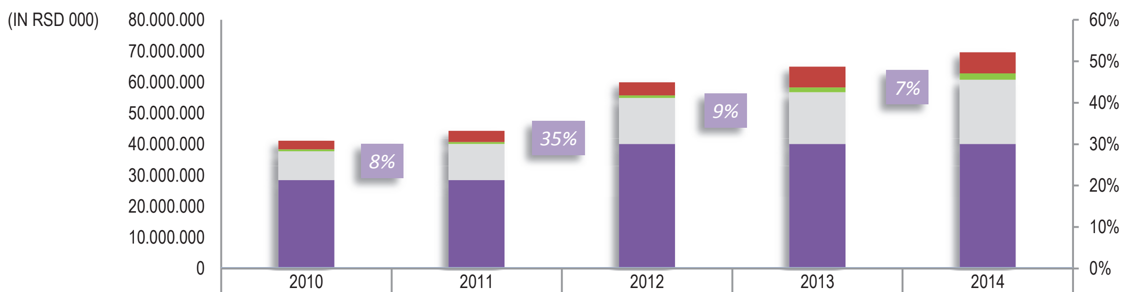
Changes in equity from 2010 to 2014:

| ITEM | 2014 | 2013 | 2012 | 2011 | 2010 |
|---|---|---|---|---|---|
| **BANK'S EQUITY** (IN RSD 000) | | | | | |
| Share capital | 40.034.550 | 40.034.550 | 40.034.550 | 28.462.553 | 28.462.553 |
| Reserves from profit | 20.635.440 | 16.635.440 | 14.785.440 | 11.635.440 | 9.235.440 |
| Revaluation reserves | 2.120.959 | 1.604.257 | 860.758 | 625.680 | 647.126 |
| Retained earnings | 6.755.855 | 6.687.971 | 4.185.812 | 3.551.893 | 2.709.309 |
| TOTAL EQUITY | 69.546.804 | 64.962.218 | 59.866.560 | 44.275.566 | 41.054.428 |

The following are the Bank's shareholders as at December 31st, 2014, following the conversion of convertible preferred shares into ordinary shares:

| SHAREHOLDERS | Ordinary shares | % of STAKE | Preferred shares | % of STAKE | TOTAL SHARES | % of STAKE |
|---|---|---|---|---|---|---|
| Republic of Serbia | 7.020.346 | 41,74 | 0 | 0,00 | 7.020.346 | 40,84 |
| EBRD | 4.109.440 | 24,43 | 0 | 0,00 | 4.109.440 | 23,90 |
| IFC | 1.706.810 | 10,15 | 0 | 0,00 | 1.706.810 | 9,93 |
| DEG | 772.850 | 4,60 | 0 | 0,00 | 772.850 | 4,50 |
| SWEDFUND | 386.420 | 2,30 | 0 | 0,00 | 386.420 | 2,25 |
| OTHERS | 2.822.090 | 16,78 | 373.510 | 100,00 | 3.195.600 | 18,59 |
| TOTAL | 16.817.956 | 100,00 | 373.510 | 100,00 | 17.191.466 | 100,00 |

*BANK'S TOTAL EQUITY*



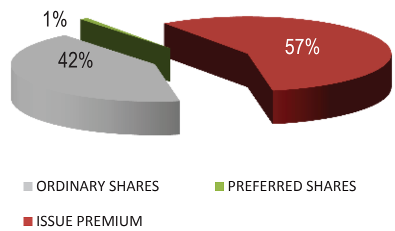

| | 2010 | 2011 | 2012 | 2013 | 2014 |
|---|---|---|---|---|---|
| PROFIT | 2.709.309 | 3.551.893 | 4.185.812 | 6.687.971 | 6.755.855 |
| REVALUATION RESERVES | 647.126 | 625.680 | 860.758 | 1.604.257 | 2.120.959 |
| RESERVES FROM PROFIT | 9.235.440 | 11.635.440 | 14.785.440 | 16.635.440 | 20.635.440 |
| SHARE CAPITAL | 28.462.553 | 28.462.553 | 40.034.550 | 40.034.550 | 40.034.550 |
| GROWTH RATES | 51% | 8% | 35% | 9% | 7% |
| TOTAL EQUITY | 41.054.428 | 44.275.566 | 59.866.560 | 64.962.218 | 69.546.804 |

Bank's total capital at the end of 2014 amounted to RSD 69,546.8 million and increased by over 69% since 2010. Share capital, in the same period has increased on the basis of two issues of convertible preference shares (in 2010 to the amount of RSD 11,400.0 million and RSD 11,572.0 million in 2012).

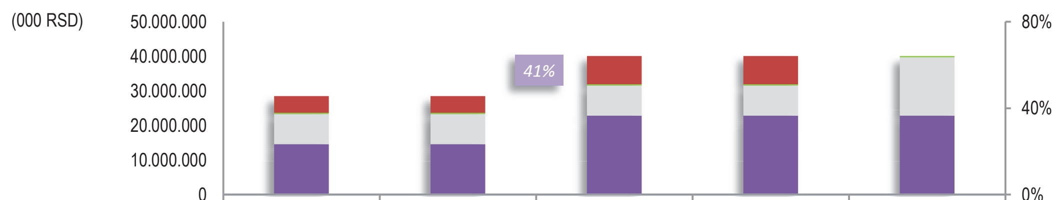
In the last five years, the Bank has formed additional reserves to the amount of RSD 12,874 million from the achieved profit and revaluation reserves, whereof RSD 4,516.7 million in 2014. The significant increase in reserves from the realized profit for each year was a rational decision of the shareholders and management in order to protect the operations of the Bank from risks, on the one hand, and to ensure safe operations of the Bank in the adverse macroeconomic conditions, on the other.
The Bank decided to strengthen its capital base by increasing reserves from profit, bearing in mind that no new increase in capital through the issue of shares is planned for the next three years and that the suboridinated debt (supplementary capital) is decreasing by 20% each year.

The formation of additional reserves was the guarantee of preserving stability of operations in the conditions of reduced loan demand and rising credit risk.

*STRUCTURE OF SHARE CAPITAL ON 31.12.2014*




*SHARE CAPITAL OF THE BANK*




| | 2010 | 2011 | 2012 | 2013 | 2014 |
|---|---|---|---|---|---|
| PREFERRED CONVERTIBLE SHARES | 4.798.190 | 4.798.190 | 8.108.646 | 8.108.646 | 0 |
| PREFERRED SHARES | 373.510 | 373.510 | 373.510 | 373.510 | 373.510 |
| ORDINARY SHARES | 8.709.310 | 8.709.310 | 8.709.310 | 8.709.310 | 16.817.956 |
| ISSUE PREMIUM | 14.581.543 | 14.581.543 | 22.843.084 | 22.843.084 | 22.843.084 |
| GROWTH RATE | 67% | 0% | 41% | 0% | 0% |
| TOTAL SHARE CAPITAL | 28.462.553 | 28.462.553 | 40.034.550 | 40.034.550 | 40.034.550 |

The Bank's ordinary shares have been traded on the Standard Market of the Belgrade Stock Exchange since 2010.

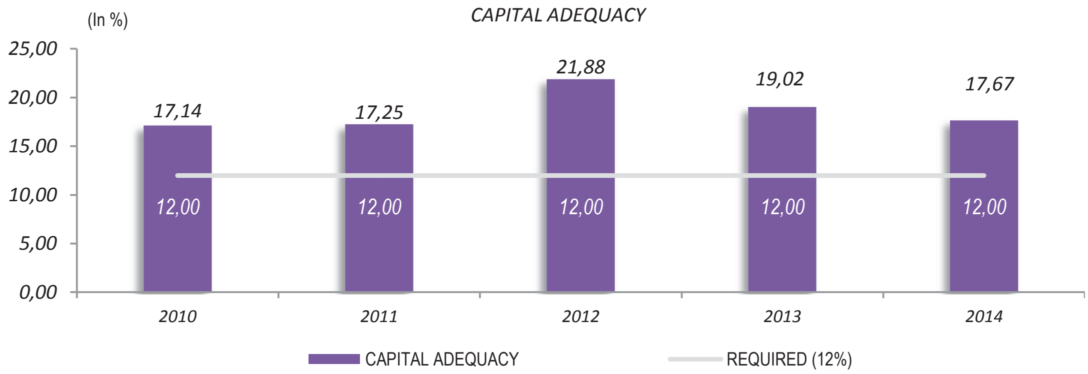
The conversion of preferred convertible shares into ordinary shares was carried out in 2014. The bank issued an additional 8,108,646 ordinary shares with a nominal value of RSD 1,000 per share. After the conversion, the Bank has 16,817,956 ordinary shares as of December the 31st 2014.
At the end of 2014, 1,099 shareholders hold ordinary shares of the Bank and 630 shareholders hold preferred shares.

The Dividend Policy of Komercijalna Banka ad Beograd was adopted at the session of the General Meeting of Shareholders held on 19 November 2014. Dividend policy aims to provide a regular and satisfactory flow of dividends (the desired ratio of dividend pay-out on ordinary shares is 30-50% of the unconsolidatated audited net profit from that financial year) and at the same time enable the Bank to maintain its financial stability and the potential for future growth and development.

## *2.6. Performance Indicators*

| No. | DESCRIPTION | REQUIRED | 31.12.2014 | 31.12.2013 | 31.12.2012 | 31.12.2011 | 31.12.2010 |
|---|---|---|---|---|---|---|---|
| 1. | CAPITAL ADEQUACY RATIO (NET CAPITAL/CREDIT RISK+OPERATIONAL RISKS+OPEN FX POSITION) | MIN. 12% | 17.67% | 19.02% | 21.88% | 17.25% | 17.14% |
| 2. | INDICATOR OF INVESTMENTS IN NON-FINANCIAL SECTOR ENTITIES AND FIXED ASSETS | MAX 60% | 27.60% | 24.67% | 18.38% | 27.98% | 21.70% |
| 3. | BANK'S LARGE EXPOSURE RATIO | MAX 400% | 160.59% | 97.78% | 107.37% | 109.51% | 82.51% |
| 4. | FX RISK RATIO | MAX 20% | 2.90% | 2.12% | 0.82% | 1.68% | 7.19% |
| 5. | LIQUIDITY RATIO | MIN. 0,8 | 2.84 | 3.45 | 2.18 | 2.91 | 2.45 |

In the observed period, the Bank has met all the required performance parameters, which is a reliable indicator of stable and secure business.

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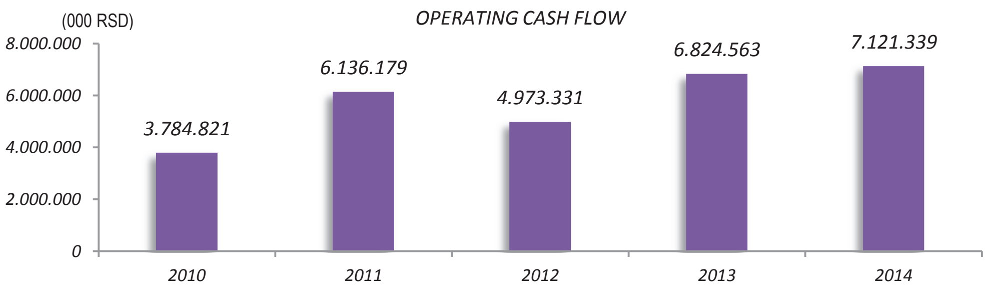
In accordance with regulatory requirements, the Bank has implemented a process of internal capital adequacy assessment process, whereby identifying all the risks to which it has been exposed or may become exposed in its operations and calculated internal capital requirements for materially significant risks, as well as the available internal capital. The process of internal capital adequacy assessment is a continuous process, which is involved in the daily decision-making and is an integral part of the risk management system.

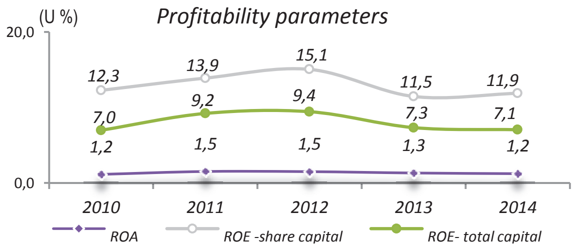
Percentage of interest and fees collection in 2014 came to 94.7%.

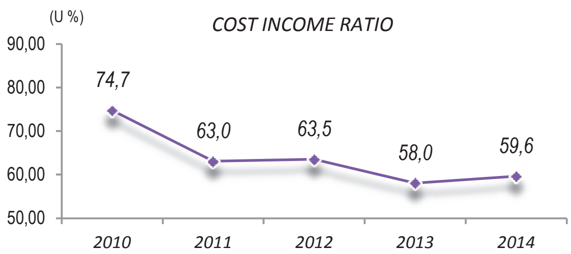



Operating cash flow at the end of 2014 was slightly higher than at the end of 2013. There was a growth in the fees inflow (3.1%), while the interest inflow was on the lower level (1.3%). The decrease in interest income of the corporate business line was partly compensated by higher interest inflow from the investments in government securities and the securities issued by National Bank of Serbia. On the other hand, interest outflows were on the lower level (9.8%) primarily due to the fall of the average interest rate on term deposits.

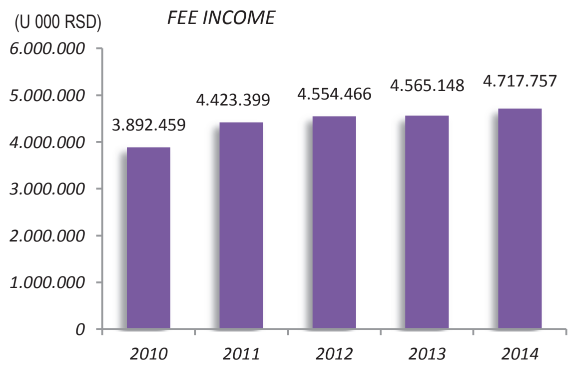
### *2.7. Bank's Profitability*

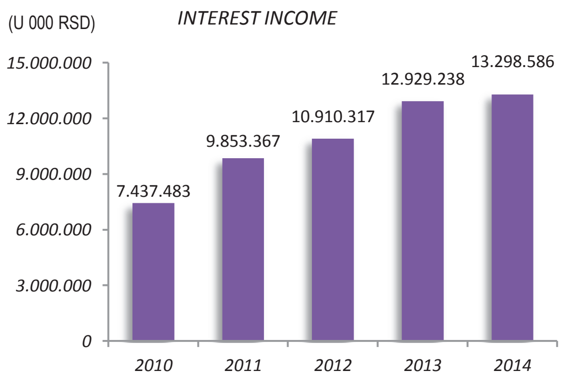

In the last three years the Bank achieved profit in excess of RSD 4.5 billion.

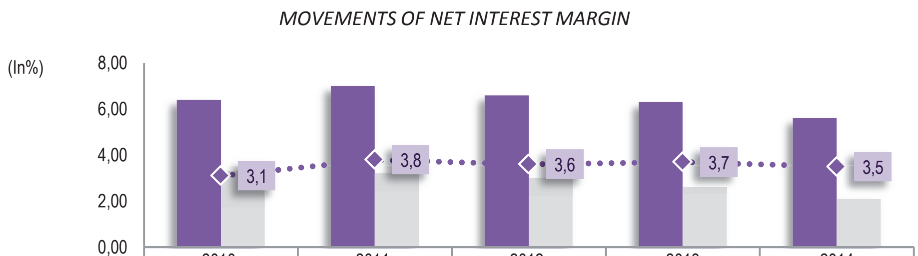



In 2014, interest income recorded 2.9% growth.
In 2014, fee income recorded 3.3% growth.



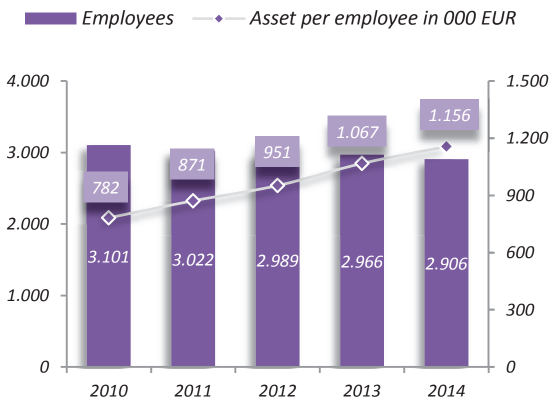




| | 2010. | 2011. | 2012. | 2013 | 2014 |
|---|---|---|---|---|---|
| Average lending rate | 6,4 | 7,0 | 6,6 | 6,3 | 5,6 |
| Average debit rate | 3,3 | 3,2 | 3,0 | 2,6 | 2,1 |
| Average interest margin | 3,1 | 3,8 | 3,6 | 3,7 | 3,5 |

The interest margin was under strong pressure due to a significant reduction in the price of funding sources, as a result of the limited possibilities of investing with a reasonable return to risk ratio, the focus of all active banks and IFIs on a small number of high quality customers and local funding, with constantly present, and necessary maintaining of a higher liquidity level compared to the competition (subsidiaries of European banks). The Bank continues to work towards further optimization of funding sources in terms of prices, currency structure, maturity, and the balanced investing.

## 2.8. Bank's Human Resources

A significant increase in the volume of business with the continuous optimization of the number and structure of employees resulted in an increase in the efficiency of the Bank, as measured by asset per employee in RSD and in EUR.




The Bank continually invests in training and development of employees. Development activities in 2014 indicate a continuation of qualitative and proactive approach to the implementation of training, based primarily on the identification of training needs, adapting the training content, design, and delivering internal training, organization of internal and external trainings, measuring and improving the quality of trainings and the training process.

| | 2010 | 2011 | 2012 | 2013 | 2014 |
|---|---|---|---|---|---|
| Asset per employee in 000 RSD | 82.512 | 91.161 | 108.192 | 122.315 | 139.801 |

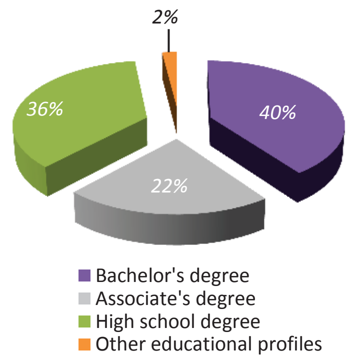
| Classification of educational degrees | Total | Up to 30 | 31-40 | 41-50 | 51-60 | Over 60 |
|---|---|---|---|---|---|---|
| I | 19 | | 5 | 5 | 9 | |
| II | 3 | | | 1 | 2 | |
| III | 29 | | 8 | 9 | 11 | 1 |
| IV | 1.050 | 41 | 270 | 306 | 417 | 16 |
| V | 3 | | 1 | 2 | | |
| VI | 645 | 56 | 283 | 141 | 150 | 15 |
| VII1 | 1.128 | 86 | 550 | 248 | 225 | 19 |
| VII2 | 27 | 1 | 14 | 9 | 3 | |
| VIII | 2 | | | 2 | | |
| TOTAL | 2.906 | 184 | 1.131 | 723 | 817 | 51 |

Observed by the subject of training, the most common were occupational trainings, aimed at the acquisition of new and improvement of the existing knowledge. The most important areas of training in 2014 according to the criteria of the topic importance and the number of participants are: product knowledge; retail business; compliance; e- banking; payment operations; credit analysis etc. In addition, the Bank also invests in trainings aimed at developing the capacity of staff in order to efficiently perform work (sales skills, presentation, leadership, communication), as well as technical skills.

Since 2008, the Bank has conducted appraisals based on set annual targets, monitoring the achievement of these targets, but also the abilities employees demonstrated in achieving them.
The annual performance appraisal is the basis for rewarding (reward system was developed in cooperation with German consultant ADG), staff career planning and planning of the budget and training programs.

The principles of rewarding the employees are clearly defined by the Remuneration Policy adopted by the Board of Directors at the proposal of Compensation Committee, which is one of the bodies established by Board of Directors. The objective of this Policy is not only to adequately reward the staff, but also to motivate them to achieve better work results. The amount of remuneration depends on the tasks that the employee performs and annual performance appraisal of the respective employee.

*Classification of employees' educational degrees in 2014*



## 2.9. Marketing and CSR Activities

Marketing activities of the Bank contributed to the further improvement of the strong market position and corporate branding, developing distribution channels and sales promotions of products and services of the Bank. Marketing communication was directed towards existing and potential target groups of customers, as well as the general public. In this continuous process, an adequate support to the work of other business sectors of the Bank has been provided.

A total of 7 ATL campaigns were realized, with the primary objective to promote the products and services of the Bank (New Year's Eve / gift cards, cash loans, housing loans, teen cards, Kombank agriculture, electronic banking, savings) and an extremely extensive CSR / ATL campaign - Together for Babies.

In addition to standard communication channels, we continued with a planned, intensive, targeted and comprehensive communication on social networks (Facebook, Twitter, YouTube, Google+, 4square, LinkedIn), which boosted the effects of promotional campaigns.

Almost all marketing activities were also promoted on the Bank's own web site, and after extensive preparations and testing, we have created and set up a new, updated, functionally improved and redesigned web site of Komercijalna Banka, with the same web address www.kombank.com. The new site was created in line with “responsive" design, which means that the site adjusts itself to the device used to open it. Regardless of whether the site is being opened by desktop or laptop computers, tablet or mobile phone, responsive site retains its structure, design and visual solution. Technological improvements make the content easier to share on social networks. The effectiveness of promotional campaigns has been continuously enhanced by the sophisticated and appropriate PR support.

In order to rejuvenate the customer base, marketing activities aimed at a younger target population have been intensified, especially in the card segment.

CSR activities gave a special contribution to maintaining and increasing the value of corporate image; the Bank took an active part in these activities that were carefully chosen and supported.

Mostly in the first half of the year, the Bank donated significant funds to help the community in the elimination of the consequences of floods.

However, the greatest media attention was given to the action "Together for Babies". The Bank started with realization of this campaign together with B92 Fund in 2014, and continued in 2015. The medical equipment for four maternity wards was provided in this action in 2014.

We got notable media space and public acceptance through 17 highly appreciated exhibitions in our gallery KOMBANK ART HOL.

We continued with the high-quality exploitation of the title sponsorship of Kombank Arena, as the most prestigious sports and concert facility in the country. We held 17 concerts and 12 sporting events (basketball Euro league), which also had significant media coverage through announcements and reports on all of these events in all the media.

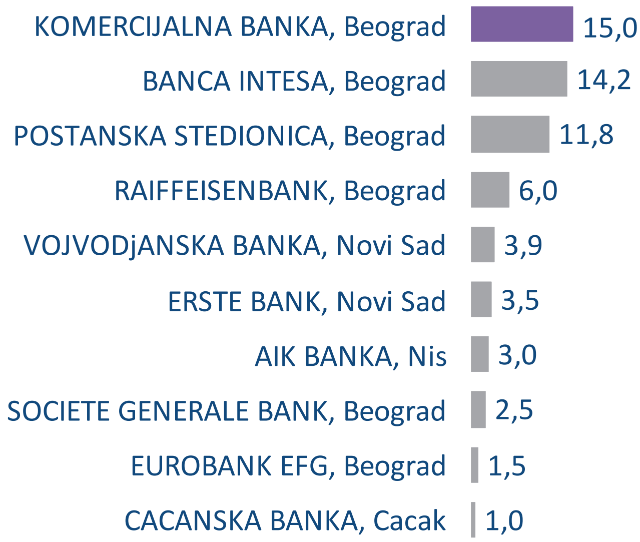
The Bank has helped the growing number of humanitarian, cultural, artistic and sports projects and actions.

In addition to maximized feedback effects of investment in donations, sponsorships and CSR activities, we got an additional pleasure from the support to our athletes who won medals at European and international level - the basketball team, Taekwondo Club Galeb - Milica Mandić, Athletic Association of Serbia - Ivana Španović and Mihailo Dudaš....

All marketing activities are coordinated with the Bank’s subsidiaries in Montenegro and the Republic of Srpska.

For consideration of the Bank's market position as a brand, its products and services, a good part of the marketing efforts were directed to the constant monitoring and analysis of quantitative and qualitative researches, aimed at improving the marketing activities. Studies show that the Bank has maintained a leading position in the public eye, as measured by the criteria of familiarity and quality. The practice of uploading the results of available researches to the Bank's internal portal continued, which provided additional information to the employees and management, as work and decision-making assistance.

*Best Bank in Serbia – 10 best banks*




*Source: IPSOS Strategic Marketing, Banking omnibus, November 2014*

## 2.10. Project and Project Portfolio Management

Altogether 11 projects with a total budget of EUR 523 thousand were implemented in 2014, while 22 projects remained in the Bank-s project portfolio as of 31 December 2014.

*Project finished in 2014*

| Category | Number of projects |
|---|---|
| Regulatory | 1 |
| Optimization and improvement | 4 |
| IT projects | 5 |
| Other | 1 |
| Total | 11 |

*The most important finished projects in 2014 were:*

- *Classification of KB Beograd Information* - The implementation of solutions which organize the process of classification and labelling of documents, records and security conditions for the protection of classified information (cryptography, storage, control, distribution).
- *Optimization of printing on laser printers in KB's network* **-** Optimization of printing process that contributes to a significant reduction in operating costs by replacing and updating obsolete printing equipment as well as "outsourcing" of the printing services to external company.
- *Management of business processes* – *I*mprovement of the Bank's business processes by applying „Lean/Six Sigma“ methodology. Successful implementation of the "pilot" project, wherewith the Bank received an adequate know-how which will in future be used in other business processes.
- *Consolidated reporting - Compliance of the banking group with the legal requirements of the parent bank and with the regulatory requirements of the National Bank of Serbia.*

*Active projects as of 31 December 2014*

| Category | Number of projects |
|---|---|
| Strategic | 2 |
| Regulatory | 1 |
| Optimisation and improvement | 9 |
| IT projects | 2 |
| Other | 1 |
| Total | 15 |

*The most important active project as of 31 December 2014:*

- Program of Basel II implementation internal approach - The program includes five projects. The aim of the implementation of the Bank's internal approach is to improve risk management through the development of customized internal models to correspond to the provided risk profile of the Bank. The increase in the Bank's ability to accurately measure and assess the risks to which it is exposed would lead to a reduction in adverse effects on the financial result and capital, and thus to increase the capital adequacy ratio.
- The centralization of Middle Office - Coordination of the overall risk management process with the requirements of the National Bank of Serbia, so that there is a clearly defined division of tasks and responsibilities of employees, which prevents a conflict of interest in risk analysis operations.
- Improvement of the system of project and project portfolio management - More efficient selection and allocation of resources of the Bank to projects and programs that will contribute to achieving the strategic goals of the Bank; Improving cost management system; Improving reporting systems; Improving the PMO document management system; Increased efficiency in PMO operations and better use of human resources.
- The introduction of ISO27001 certificates - project is of great importance to information security, risk reduction and improving information security management system (ISMS). The project objective and success criterion is to ensure all the necessary controls for the application of the principle of confidentiality, uniformity and availability of information, protection of information and data as well as acquiring ISO27001: 2013 certificate.
- Migrating SQL Server - Successful migration was performed with minimal downtime of the Core banking applications that depend on the Core system, with the same or better application performance and the same or better functionality brought by the new version of ther SQL Server 2008 R2.

## *2.11. Bank's Balance Sheet as of 31 December 2014*[24]

(000 RSD)

| No. | POSITION | 31.12.2014 | 31.12.2013 | INDICES | % OF SHARE AS OF 31.12.2014 |
|---|---|---|---|---|---|
| 1 | 2 | 3 | 4 | 5=(3:4)*100 | 6 |
| | **ASSETS** | | | | |
| 1. | Cash and funds held with the Central Bank | 68,547,389 | 70,934,839 | 96.6 | 16.9 |
| 2. | Pledged funds | - | - | - | |
| 3. | Financial assets by fair value though balance sheet intended for sale | 121,634 | 115,319 | 105.5 | 0.0 |
| 4. | Financial assets initially recognized at fair value through profit or loss | - | - | - | |
| 5. | Financial assets available for sale | 95,481,249 | 56,885,285 | 167.8 | 23.5 |
| 6. | Financial assets held to maturity | 51,442 | 149,900 | 34.3 | 0.0 |
| 7. | Loans and receivables due from banks and other financial institutions | 34,737,605 | 35,247,935 | 98.6 | 8.6 |
| 8. | Loans and receivables due from customers | 185,377,035 | 177,560,058 | 104.4 | 45.6 |
| 9. | Changes in fair value of items that are the subject of hedging | - | - | - | |
| 10. | Receivables from financial derivatives held for hedging | - | - | - | |
| 11. | Investments in associated companies and joint ventures | - | - | - | |
| 12. | Investments in subsidiaries | 5,480,888 | 5,480,888 | 100.0 | 1.3 |
| 13. | Intangible investments | 405,774 | 537,445 | 75.5 | 0.1 |
| 14. | Real-estate, buildings and equipment | 6,329,077 | 6,577,670 | 96.2 | 1.6 |
| 15. | Investment property | 2,581,144 | 1,808,554 | 142.7 | 0.6 |
| 16. | Current tax assets | 73,835 | 712,700 | 10.4 | 0.0 |
| 17. | Deferred tax assets | - | - | - | |
| 18. | Fixed assets intended for sale and funds from discontinued operations | 84,227 | 71,630 | 117.6 | 0.0 |
| 19. | Other assets | 6,990,225 | 6,704,096 | 104.3 | 1.7 |
| | **TOTAL ASSETS (1 to 19 )** | **406,261,524** | **362,786,319** | 112.0 | 100.0 |

[24]: The new Chart of Accounts for banks is in effect as of 31 December 2014, which is why the form of financial statements for 2014 was changed. For reasons of comparability of the financial data, the "translation" of balance sheet formats for 2013 was done on the new chart of accounts.

| No. | POSITION | 31.12.2014 | 31.12.2013 | INDICES | % OF SHARE AS OF 31.12.2014 |
|---|---|---|---|---|---|
| 1 | 2 | 3 | 4 | 5=(3:4)*100 | 6 |
| | **LIABILITIES** | | | | |
| 1. | Financial liabilities at fair value through profit or loss held for trading | - | - | - | |
| 2. | Financial liabilities initially recognized at fair value through profit or loss | - | - | - | |
| 3. | Liabilities arising from financial derivatives held for hedging | - | - | - | |
| 4. | Deposits and other liabilities to banks, other financial institutions and the central bank | 23,743,018 | 21,058,542 | 112.7 | 5.8 |
| 5. | Deposits and other liabilities to other customers | 301,954,911 | 266,020,289 | 113.5 | 74.3 |
| 6. | Changes in fair value of items that are the subject of hedging | - | - | - | |
| 7. | Issued own securities and other borrowed funds | - | - | - | |
| 8. | Subordinated liabilities | 6,036,680 | 5,711,409 | 105.7 | 1.5 |
| 9. | Provisions | 1,640,595 | 765,132 | 214.4 | 0.4 |
| 10. | Liabilities arising from funds intended for sale and funds from discontinued operations | - | - | - | |
| 11. | Current tax liabilities | - | - | - | |
| 12. | Deferred tax liabilities | 150,407 | 10,156 | 1.481.0 | 0.0 |
| 13. | Other liabilities | 3,189,109 | 4,258,573 | 74.9 | 0.8 |
| **14.** | **TOTAL LIABILITIES ( 1 to 13)** | **336,714,720** | **297,824,101** | 113.1 | 82.9 |
| | **CAPITAL** | | | | |
| 15. | Share capital | 40,034,550 | 40,034,550 | 100.0 | 9.9 |
| 16. | Own shares | | | | |
| 17. | Profit | 6,755,855 | 6,687,971 | 101.0 | 1.7 |
| 18. | Loss | | | | |
| 19. | Reserves | 22,756,399 | 18,239,697 | 124.8 | 5.6 |
| 20. | Unrealized gains | - | - | - | |
| 21. | Non-controlling interest | - | - | - | |
| **22.** | **TOTAL CAPITAL (15 to 21)** | **69,546,804** | **64,962,218** | 107.1 | 17.1 |
| **23.** | **TOTAL LIABILITIES (14+22)** | **406,261,524** | **362,786,319** | 112.0 | 100.0 |

## 2.12. Bank's 2014 Protif&Loss Statement

(000 RSD)

| No. | POSITION | 31.12.2014 | 31.12.2013 | INDICES (3:4)*100 |
|---|---|---|---|---|
| 1 | 2 | 3 | 4 | 5 |
| | **INCOME AND EXPENSES** | | | |
| 1.1. | Interest income[25] | 21,224,379 | 22,023,774 | 96.4 |
| 1.2. | Interest expenses | 7,925,793 | 9,094,536 | 87.1 |
| **1.** | **Net interest income** | **13,298,586** | **12,929,238** | 102.9 |
| 2.1. | Fee and commision income | 5,677,040 | 5,493,211 | 103.3 |
| 2.2. | Fee and commision expenses | 959,283 | 928,063 | 103.4 |
| **2.** | **Net fee and commission income** | **4,717,757** | **4,565,148** | 103.3 |
| **3.** | Net gain / loss on financial assets held for trading | 6,076 | 22,342 | 27.2 |
| **4.** | Net gain / loss on risk hedging | - | - | |
| **5.** | Net gain / loss on financial assets initially recognized at fair value through profit or loss | - | - | |
| **6.** | Net gain / loss on financial assets available for sale | 51,282 | 1,738 | 2.950.6 |
| **7.** | Net gains / losses on foreign exchange transactions and effects of foreign currency clause | -205,943 | -48,733 | 422.6 |
| **8.** | Net gain / loss on investments in associated companies and joint ventures | - | - | |
| **9.** | Other operating income | 569,191 | 1,123,546 | 50.7 |
| **10.** | Net gains / losses on impairment of financial assets and off-balance sheet credit risk items | -2,725,389 | -3,220,075 | 84.6 |
| **11.** | **TOTAL NET OPERATING INCOME / EXPENSES** | **15,711,560** | **15,373,204** | 102.2 |
| **12.** | Wages, salaries and other personal expenses | 4,211,489 | 4,262,123 | 98.8 |
| **13.** | Depreciation costs | 844,632 | 792,648 | 106.6 |
| **14.** | Other expenses | 5,897,850 | 5,730,058 | 102.9 |
| **15.** | **PROFIT BEFORE TAX (1 TO 14)** | **4,757,589** | **4,588,375** | 103.7 |
| **16.** | Profit tax | - | - | |
| **17.** | Profit from deferred tax | 47,547 | 87,950 | 54.1 |
| **18.** | Loss from deferred tax | 19,559 | - | |
| **19.** | **PROFIT AFTER TAX (15 to 18)** | **4,785,577** | **4,676,325** | 102.3 |
| **20.** | Net profit from discontinued operations | - | - | |
| **21.** | Net loss from discontinued operations | - | - | |
| **22.** | **RESULT FOR THE PERIOD – PROFIT ( 19 to 21)** | **4,785,577** | **4,676,325** | 102.3 |

25 Due to the implementation of the new concept of "unwinding" at the end of 2014, interest income is lower by the amount of RSD 442.6 million

## 3. INVESTMENTS IN ENVIRONMENTAL PROTECTION

The Bank abides by the highest international standards and values in the creation of financial products and services, developing activities in the field of environmental protection and the protection of human and labour rights. By adopting the policies and procedures on natural and social environment, the Bank has defined standards for identifying and managing the risks for natural and social environment in the process of approving and monitoring loans. The Bank has defined the procedure for addressing and responding to complaints against direct or indirect impact of the Bank's business activities to environment and society.

By negotiating credit lines to finance investments aimed at increasing energy efficiency and development of renewable energy, the Bank approved loans that contribute to reduction of energy consumption and carbon dioxide emissions.

Also, the Bank continuously monitors the emergency events occurring in business of its customers, which may have adverse effect on the environment, health, safety or the entire community, and regularly informs management bodies and the shareholders of the Bank thereof.

In order to protect the environment and minimize the possibilities for the occurrence of events that may have a material adverse impact on the environment, health or safety or the community as a whole, the Bank does not finance or provides minimal funding to the customers whose main activity is associated with the production of or trade in arms and ammunition, alcoholic beverages, radioactive materials and other technologies that can have a negative impact on the environment.

## 4. SIGNIFICANT EVENTS AFTER THE END OF THE FINANCIAL YEAR

One General Meeting of Bank's Shareholders was held from 31 December 2012 until 28 February 2015.

- Regular General Meeting of Bank's Shareholders was held on 26 January 2015.

  The following decisions were passed: On adoption of the Strategy and Business Plan of the Bank 2015 - 2017.

After the end of the financial year there were no events that have had a materially significant impact on the Bank's financial statements for the period ending on December 31, 2014.

## 5. PLAN FOR FUTURE DEVELOPMENT OF THE BANK

The Bank's strategy in the coming period is defined in the planning process starting with a workshop with members of the Board of Directors in September 2014 and finally through the adoption by the General Assembly of Shareholders of the Bank at its meeting held on 26 January 2015, thus continuing the practice of the three-year planning of the Bank's development, while retaining "roll-over" principle, or the detailed planning, following indicative projections for the next two years and keeping the main focus and orientation, all in line with uncertain and changing environment. When setting up basic strategic goals for the next period, the in focus has been set to a stable and sustainable business primarily through the following:

- Defence of interest margin
- Increasing efficiency and
- Maintaining the portfolio quality rather than focusing on the growth.

The Bank is also facing the beginning of privatization process.

The mission and long-term commitment of the Bank in the coming period remain – KB is and will continue to be:

- Leading Serbian bank with regional presence.
- Universal bank with an equal focus on corporate and retail sector.

Additionally, in these times, there is a significant KB's role in mitigating the crisis effects on its customers, and support, within the limits of its potential and not at the expense of its shareholders, to all measures aiming at the recovery of Serbian economy.

We can define the strategic goals as:

- Stable and sustainable business development.
- Management of all risks inherent to the Bank's operations.

- Sustainable profitability that enables creation of the conditions for its growth in the post-crisis period.

The principles which govern the Bank when setting its goals are as follows:

- Stability and long-term business sustainability and shareholder value.
- Prudence.
- Conservative approach.

The strategic goals of the Bank and the expected macro situation and environment, define business targets and priorities of KB for the upcoming period:

1. To maintain the quality of the existing portfolio through intensive monitoring and collection.
2. Further diversification and extenstion of the funding term structure, as well as stabilization of funding prices at the level lower than present.
3. The diversified growth of investments, primarily by use of withdrawn credit lines (agriculture, micro customers, small businesses, housing loans) with an emphasis on quality.
4. Active securities portfolio management in order to optimize the liquidity level.
5. Expanding the customer base and increase the efficiency of the network in order to create possibilities for rapid exploitation in the post-crisis period.
6. Active management of the asset portfolio (sale / leases).
7. Optimization of all available resources.

| *Plan* | *2015* | *2016* | *2017* |
|---|---|---|---|
| *Real growth of ban.sector* | *0,0%* | *3,0%* | *5,0%* |
| *Targeted market share* | *≥12%* | *≥12%* | *≥12%* |
| *KB growth (ex.rate effect incl.)* | *3,6%* | *5,2%* | *5,5%* |
| *ROE on KB share capital* | *11,9%* | *13,7%* | *15,4%* |
| *ROE on KB total capital* | *6,8%* | *7,5%* | *8,1%* |
| *ROA KB* | *1,2%* | *1,3%* | *1,4%* |

## *6. RESEARCH AND DEVELOPMENT*

Komercijalna Banka has been monitoring the results of the banking and financial market researches for years, seeking to examine the needs of customers, as well as the satisfaction of those who use its services.

For the purpose of conducting market and customer satisfaction research, the Bank engages specialized agencies for public opinion research. Thus it seeks to provide adequate information that will be helpful both as compared to the competition, and in the process of making business decisions, particularly important in respect to the development of new and improvement and modification of existing products and services.

According to the results of independent research, the Bank has occupied the leading position by brand recognition and quality of services offered for a considerable period of time. The Bank occupies a strongly perceived position owing to the palette and quality of its products and services, and their constant improvement.

In the process of continuous monitoring of market signals and needs of users and potential customers, business sectors of the Bank have, in the previous period, offered to the customers new and / or improved certain types of retail and micro customer loans, and developed a whole range of services in the field of electronic banking, debit and credit cards.

The results of research and development have been implemented in the Strategy and Business Plan Bank.

## *7. ACQUISITION OF OWN SHARES AND STAKES*

The Bank did not hold own shares as of December 31, 2014, or during 2014.

The Bank also does not intend to acquire its own shares in the coming period.

## 8. *BRANCHES OF THE BANK*

The Bank has organized its business through a network of branches and outlets. Business is taking place in the head office in Belgrade, 24 branches and 218 outlets, as shown in item 1.6.

The Bank has three subsidiaries, which together form Komercijalna Banka ad Beograd banking group:

1. Komercijalna Banka a.d. Budva in the Republic of Montenegro (100% ownership)
2. Komercijalna Banka a.d. Banja Luka in Bosnia and Herzegovina (99.99% ownership) and
3. KomBank INVEST a.d. Beograd, Investment Fund Management Company (IFMC) (100% ownership).

### *ALL IMPORTANT TRANSACTIONS WITH RELATED PERSONS*

Persons related to the Bank on 31.12.2014 are the following:

1. Komercijalna Banka a.d. Budva, Montenegro,
2. Komercijalna Banka a.d. Banja Luka, Bosnia and Herzegovina
3. IFMC KomBank Invest a.d. Beograd,
4. Six legal persons and an attorney (Lasta doo, Viš trade doo, Desk doo, Menta doo, Meplast doo Kruševac, Futura – Faculty of Applied Ecology Belgrade and Ristić Saša, attorney at law) as well as many natural persons, pursuant to the provisions of the Article 2 of the Law on Banks, in the part that specifies the term „persons related to the bank“.

Total exposure to persons related to the Bank on 31.12.2014 amounted to 702.528 thousand Dinars, which, in relation to the capital amounting to 32.325.138 thousand Dinars, came to 2.17% (according to the Law on Banks, the maximal value of total loans and advances to persons related to the Bank may come to no more than 20% of the capital).

The largest portion of exposure to the persons related to the Bank was 640.071 thousand RSD or 1.98% of the Bank's capital on 31.12.2014, and refers to the loans and advances to the natural persons related to the Bank.

Pursuant to the Article 37 of the Law on Bank, the Bank did not grant more favourable conditions to the persons related to the bank than the conditions granted to other persons not related to or employed by the bank. More detailed review of the Bank's relations with the related persons is provided in the Item 40 of the Notes to Financial Statements.

| | KOMERCIJALNA BANKA AD BUDVA | KOMERCIJALNA BANKA AD BANJA LUKA | DZUIF KomBank INVEST AD BEOGRAD |
|---|---|---|---|
| ADDRESS | Podkošljun bb | Veselina Masleše 6 | Kralja Petra 19 |
| PHONE | 00382-33-426-300 | 00387-51-244-700 | 011-330-8310 |


**KB BANJA LUKA**

Komercijalna Banka AD Banja Luka has:
- 144 employees,
- 26 organisational units
(8 branches and 18 agencies).

**KB BUDVA**

Komercijalna Banka AD Budva has:
- 124 employees,
-17 organisational units
(6 branches and 11 outlets).

## 9. FINANCIAL INSTRUMENTS OF IMPORTANCE FOR ASSESSMENT OF FINANCIAL POSITION

At the end of the fiscal 2014, the following financial instruments were of crucial importance for the assessment of the financial position of the Bank:

- On the right hand side of the balance sheet:
  - Loans and receivables due from customers;
  - Loans and receivables due from banks and financial organisations
  - Financial assets available for sale and
  - Cash and funds held with the central bank
- On the left hand side of the balance sheet:
  - Deposits and other liabilities to customers;
  - Deposits and other liabilities to banks, financial institutions and the central bank;
  - Subordinated obligations and
  - Capital.

Loans and advances to customers, banks and other financial institutions at the end of the year amounted to RSD 220,114.6 million and make up 54.2% of total assets, while at the end of 2013, loans amounted to RSD 212,808.0 million and were accounted for 58.7% in total assets.

During 2014, loans and advances increased by RSD 7306.6 million or 3.43%. Bearing in mind that loans and advances have made up more than 50% of the total assets for a considerable period of time, Bank has developed a risk management system in the previous period, with particular emphasis on credit risk. As a result of these efforts, the Bank now has a quality loan portfolio, which is provided with the appropriate amount of the allowance and profit-formed reserves.

Financial assets available for sale at the end of 2014 amounted to RSD 95,481.2 million RSD (23.5% of total assets), and compared to the situation as of the end of 2013 (RSD 56,885.3 million, 15.7% of total assets) increased by RSD 38,596.0 million or 67.8%. These assets are mainly related to investments in short-term and long-term securities of the Republic of Serbia.

Cash and funds held with the central bank, credit risk-free assets as of 31 December 2014 amounted to RSD 68,547.4 million RSD, and comparing to the beginning of the year decreased by 3.4% or RSD 2387.5 million. The amount of the funds held in the drawing account and funds allocated to be held with the National Bank of Serbia as the required reserve are dominant in the structure of this position.

Bearing in mind the structure of assets, it can be concluded that the assets sensitive to credit risk are maintained at an optimum level, abiding by the reasonable risk taking policy.

Deposits and other liabilities due to customers (including the assets taken in the form of credit lines) as or 31 December 2014 amounted to RSD 301,954.9 million and account for 74.3% in total liabilities. If compared to the beginning of the year, deposits and other liabilities due to customers increased by RSD 35,934.6 million or 13.5%.

Deposit potential of the Bank predominantly consists of retail foreign currency deposits, whereby there is a great diversification of deposits and a large number of small deposits.

Deposits and other liabilities due to banks financial institutions and the Central Bank amounted to RSD 23,743.0 million as of December 31, 2014, accounting for 5.8% of total liabilities.

In order to create a basis for better lending conditions for the customers, as well as for strengthening the capital base, the Bank has provided a portion of funds in the form of subordinated debt by the IFC. At December 31, 2014, subordinated liabilities amounted to RSD 6036.7 million and constitute 1.49% of liabilities.

As of December 31, 2014, the total capital of the Bank amounted to RSD 69,546.8 million RSD and makes 17.1% of total liabilities. Total capital increased by RSD 4584.6 million or 7.1% in the fiscal year.

Based on the above, we can conclude that the Bank has provided a variety of funding sources and that there is no high concentration of deposits.

## 10. OBJECTIVES AND POLICIES OF FINANCIAL RISK MANAGEMENT

The Bank has recognized the risk management process as a key element of business management, given that the exposure to risks arising from all the operations, as an inseparable part of the banking business, is managed through the identification, measurement, mitigation, monitoring, control and reporting, i.e. specifying the risk limits, and reporting in accordance with the strategies and policies.

The Bank has established a comprehensive and reliable risk management system which includes strategies, risk management policies and procedures, the appropriate organizational structure, effective and efficient management system for all the risks, adequate system of internal controls, appropriate information system and an adequate process of internal capital adequacy assessment process.

In the Risk Management Strategy and Capital Management Strategy, the Bank has set the following objectives within the system of risk management: minimizing adverse effects on the financial result and equity with respect to the defined framework of acceptable risk levels, maintaining the required level of capital adequacy, the development activities of the Bank in accordance with business opportunities and market development in order to achieve competitive edge.

There is a more detailed overview of the objectives and risk management policies of the Bank presented in Section 4 Notes to the Financial Statements.

### *Policy of Protection from Exposure to Credit Risk*

In order to protect against exposure to credit risk, when approving loans, the Bank especially takes into account two sources of debt collection: cash flow, as a primary source of repayment and security instruments (collaterals) as the secondary source of loan repayment. Types of collateral depend on the assessment of the debtor's credit risk and are determined in each case individually. Collaterals are provided after signing the contract and before the loan disbursement.

The Bank regulated the evaluation of credit risk protection instruments, as well as management of these instruments, by internal regulations.

When assessing the value of collateral, the Bank engages licensed appraisers, whose task is to reduce the potential risk of unrealistic assessments to a minimum, and the subject of pledge must be insured with an insurance company acceptable to the Bank with an insurance policy set up in favour of the Bank.

In order to protect against changes in the market value of the collateral, estimated value is adjusted for a defined percentage depending on the type of collateral and the location, which are reviewed and revised at least annually.

The Bank pays special attention to the monitoring of collateral and undertakes activities on securing new evaluations, as well as an additional collateral, primarily with respect to the customers who face some problems in business, but also with respect to the customers whose collateral coverage reduced due to declining collateral values.

## 11. *RISK EXPOSURE (PRICE, CREDIT, LIQUIDITY AND CASH FLOW) WITH THE STRATEGY FOR RISK MANAGEMENT AND ASSESSMENT OF THEIR EFFECTIVENESS*

The Bank is particularly exposed to the following risks in its operation:

1. Credit and related risks
2. Liquidity risk
3. Market risk
4. Operational risk
5. Investment risk
6. Exposure risk and
7. Country risk and all other risks that may occur in the ordinary course of business of the Bank.

Credit risk is the possibility of adverse effects on the financial result and equity of the Bank due to defaulting debtors. Credit risk is conditioned by the creditworthiness of the debtor, regularity of servicing his liabilities to the Bank, as well as the quality of collateral. Acceptable level of credit risk exposure of the Bank is in accordance with defined risk management strategy and depends on the structure of the Bank's portfolio, which serves as the basis for ensuring the limitation of the negative effects on the financial result and minimizing capital requirements for credit risk, settlement risk and delivery and counterparty risk, in order to maintain a capital adequacy ratio at an acceptable level. The Bank grants loans to customers (legal and natural persons) that are estimated as creditworthy. On the other hand, the Bank does not invest in high-risk investments such as investments in potentially profitable projects involving high risk or investment funds with the high-risk portfolios, etc.

Liquidity risk represents the possibility of occurrence of adverse events that may adversely affect the financial results and equity. Liquidity risk arises from the difficulty of the Bank to settle due liabilities in the event of a liquidity reserves shortfall and the inability to cover unexpected outflows and other liabilities. In its operation, the Bank abides by the basic liquidity principles, providing sufficient level of funds to cover liabilities incurred in the short term, or in other words it respects the principle of solvency by forming the optimal structure of its own and borrowed funds and the establishment of a sufficient level of liquidity reserves that do not compromise the achievement of the planned return on equity. Liquidity risk arises from the Bank's inability to meet its payment obligations. Liquidity risk may appear in the form of funding risk and market liquidity risk. The problem of liquidity in terms of funding sources relates to the structure of liabilities, or obligations, and is expressed through a potentially significant share of unstable sources, short term sources or their concentrations. On the other hand, liquidity risk also arises from the deficit of the liquidity reserves and difficulty or impossibility of obtaining liquid assets at reasonable market prices.

Market risk represents the possibility of negative effects on the financial result and equity due to changes in market variables and comprises interest rate risk in the banking book, foreign exchange risk for all business activities performed and the price risk of the trading book positions.

Interest rate risk is the risk of negative effects on the financial result and equity arising from banking book positions due to adverse changes in interest rates. Exposure to this type of risk depends on the ratio of interest-sensitive assets and liabilities. Interest rate risk management aims to maintain an acceptable level of exposure to interest rate risk in terms of the impact on the financial result and economic value of equity, by conducting an adequate policy of maturity match between the period of interest rates repricing and compliance with lending sources by type of interest rate and maturity.

The Bank is exposed to FX risk, which is manifested through the possibility of adverse effects on the financial result and equity due to changes in inter-currency ratios, changes in the value of the domestic currency against foreign currencies and changes in the value of gold and other precious metals. In order to minimize exposure to foreign exchange risk, the Bank diversifies the currency structure of the portfolio and currency structure of liabilities, harmonizes the open positions by individual currencies, while respecting the principles of maturity transformation of funds.

Operational risk is the possibility of adverse effects on the financial result and equity due to failures in the work of employees, inappropriate internal procedures and processes, inadequate management information and other systems in the bank, as well as due to the occurrence of unforeseen external events.

Investment risk of the Bank is the risk of investments in other legal entities and fixed assets.

Large exposures to a single person or a group of related persons, including persons related to the Bank, is the exposure that exceeds 10% of its capital.

Country risk is the risk that relates to the country of origin of the entity to which the Bank is exposed, or the risk of negative effects on the financial result and equity due to the inability of the Bank to collect receivables from debtors for reasons that are the result of political, economic or social conditions in the debtor's country of origin.

The detailed review and explanation of risks to which the Bank is exposed in its operations is presented in Section 4 Notes to the Financial Statements.

## *12. RULES OF CORPORATE GOVERNANCE*

The rules of corporate governance implemented in the Bank are based on the relevant legislation (primarily the Law on Banks and the Law on Companies).

Competences and powers of the Bank's bodies (General Meeting of Shareholders,Board of Directors, Executive Board, Audit Committee, the Asset and Liabilities Management Committee (ALCO Committee), Compensation Committee, credit committees and other committees), are based on the relevant legislation and defined in internal regulations (Memorandum on Association, the Bank's Statute, Rules of Procedure of the Bank's bodies and other internal regulations).

In its operation the Bank implements the Code of Corporate Governance of the Serbian Chamber of Commerce, which was adopted by the Assembly of the Serbian Chamber of Commerce.

The rules of corporate governance are implemented through internal regulations of the Bank and there are no discrepancies in their implementation.

Code of corporate governance has established the principles of corporate practice abided by the holders of the Bank's corporate governance who behave in accordance with these principles. The objective of the Code is the introduction of good business practices in corporate governance, equal influence of all stakeholders, existing and potential shareholders, employees, customers, the Bank's bodies, State and others. The final objective is to provide long-term and sustainable development of the Bank.

The text of the Code of Corporate Governance was published on the website of the Serbian Chamber of Commerce (www.pks.rs-ventricular services, corporate governance) as well as the Bank's web site (www.kombank.com/korporativno-upravljanje).

In 2014, IFC (International Finance Corporation) consultant carried out a detailed analysis of corporate governance; he estimated that the corporate governance practices of the Bank were among the best observed in the region and provided guidance for further "fine tuning", which will be implemented in the coming period.

## *13. IMPLEMENTATION OF THE BANK'S 2014 BUSINESS PLAN*

Despite the difficult operating conditions, as a consequence of the adverse global developments followed by the recession in Serbia (floods and the beginning of structural reforms and fiscal consolidation measures) and the deterioration of macroeconomic indicators in line with the above, the Bank is focusing on security, stability and sustainability of continued implementation of its strategy and its objectives.

| Macroeconomic indicaotors | Achieved 2014. | Plan 2014 |
|---|---|---|
| GDP growth | -2,0% | 1,0% |
| Money market rate | 8,0% | 9,0% |
| Inflation rate (CPI) | 1,7% | 5,5% |
| EUR/RSD (year-end) | 120,9 | 115,0 |

Operation of the banking sector in 2014 was characterized by significantly reduced loan demand and fall of the credit activities of the corporate customers, with an increased demand for retal liquidity. However, in 2014, the operations of all banks including KB's, were mostly marked by continuing economic collapse and structural adjustment resulting in resistant NPL level, which placed even greater focus on stabilizing and maintaining the portfolio quality.

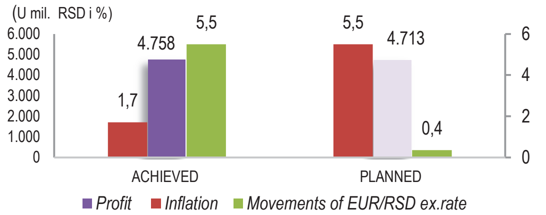
Besides the distinctive high credit risk in the market and the fall of credit activity, a key profitability factor in 2014 was the introduction of the excess deposit insurance premium, which burdened the result, i.e. operating costs with an additional RSD 440 million. However, the planned profit was achieved.

| Objectives | Achieved 2014 | Plan 2014 | Achieved without the unplanned expenses resulting from excess deposit insurance premim |
|---|---|---|---|
| Growth of assets | 11.98% | 0.20% | 11.98% |
| Profit (RSD million) | 4.757 | 4.713 | 5.198 |
| Net interest margin | 3.49% | 3.64% | 3.49% |
| ROA | 1.25% | 1.33% | 1.36% |
| ROE – share capital | 11.88% | 11.77% | 12.98% |
| ROE – total capital | 7.05% | 7.25% | 7.71% |
| CIR | 59.65% | 59.57% | 57.20% |

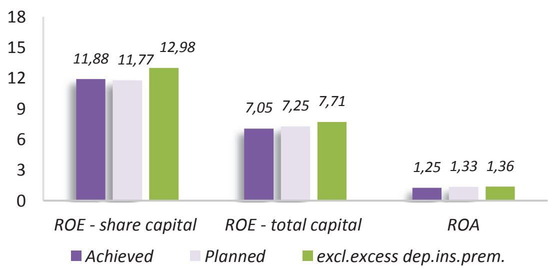
In 2014, Komercijalna Banka implemented the adopted Strategy and Business Plan for 2014 - 2016, and achieved all the objectives: profitability, busines growth, loan portfolio quality, liquidity, safety, cost management.

*Profitability*. Despite the decrease in corporate loan demand and remaining high credit risk level in the market, as well as introducing the excess deposit insurance premium, operating profit of the Bank amounted to RSD 4,757,6 million in 2014, or RSD 44.6 million higher than planned.

*PROFIT BEFORE TAX, INFLATION AND ANNUAL RSD EX.RATE CHANGE IN 2014*




*PROFITABILITY PARAMETERS IN 2014*

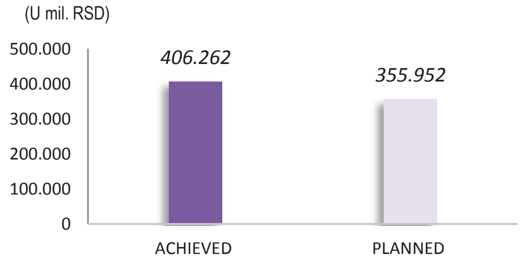



Profitability plan was achieved with 100.9% and the profitability parameters (ROA and ROE) were in line with the plan, with a slight deviation of ROE on total capital, due to the achieved level of total capital above the planned value in 2014 (an increase in revaluation reserves and tax effects).

The effect of "unwinding" on the interest margin was RSD 442 million or 3.6%. In the unfavorable operating conditions (recession, high unemployment, reduced loan demand, NPL growth), the Bank still achieved BS assets growth. At the end of 2014, the Bank's balance sheet assets amounted to RSD 406,262 million, or an increase of 12.0% as compared to the previous year. The growth of the Bank's operations in 2014 was achieved primarily due to growth in deposits. Total deposits amounted to RSD 293,466 million, which compared to the previous year represented an increase of 14.8%, while in the conditions of reduced loan demand, the Bank's total loan growth was 5.8%. Due to the reduced loan demand, the Bank's liquid assets were invested in securities in order to increase the interest-earning assets and achieve the planned profitability.

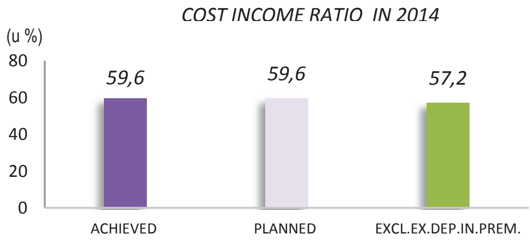
Market share was maintained above 12% (30 September 2014).

*BALANCE SHEET SUM IN 2014*




*Security*. Bank's capital adequacy ratio was 17.7% at the end of 2014, and was consistent with the set objective (no less than 15%).

*Cost management*. In 2014, the cost management aimed at rationalizing and reducing operating costs. Set objective, for the Cost income ratio to amount 59.6%, was achieved despite a significant increase in unplanned expenses arising from the introduced excess deposit insurance premium (RSD 441 million) on the one hand, and unplanned reduction in interest income resulting from the required application of the unwinding concept (RSD 442, 6 million) on the other.




*13.1. Realizatioon of the balance sheet projection for 2014.*

(In RSD million)

| No. | ASSET POSITION | ACHIEVED IN 2014 | PLAN FOR 2014 | INDICES (3:4)*100 |
|---|---|---|---|---|
| 1 | 2 | 3 | 4 | 5 |
| | **ASSETS** | | | |
| **1.** | Cash and cash equivalents | 45,160 | 34,365 | 131,4 |
| **2.** | Callable deposits and loans | 43,738 | 47,250 | 92,6 |
| **3.** | Interest, fees receivables | 2,811 | 2,528 | 111,2 |
| **4.** | **Loans and deposits to customers**[26] | **194,661** | **193,656** | 100,5 |
| 4.1. | Corporate | 112,768 | 115,000 | 98,1 |
| 4.2. | Retail | 69,039 | 65,986 | 104,6 |
| 4.3. | Banks | 12,854 | 12,670 | 101,5 |
| **5.** | Securities | 95,654 | 55,385 | 172,7 |
| **6.** | Shares (stakes) | 6,228 | 5,998 | 103,8 |
| **7.** | Other lending | 2,318 | 3,274 | 70,8 |
| **8.** | Fixed assets and investment property | 8,910 | 7,907 | 112,7 |
| **9.** | Other assets | 6,782 | 5,589 | 121,3 |
| **10.** | **TOTAL ASSETS (1 To 9)** | **406,262** | **355,952** | 114,1 |

- Position Cash and cash equivalents recorded growth in relation to the plan due to the growth of funds on the Bank's drawing account held with the National Bank of Serbia and funds on foreign currency transaction accounts.

- Reduced investments in repo securities and lower foreign currency reserve led to deviations between realized and planned value of the position callable deposits and loans.

- Achievement of corporate loans disbursed was lower due to the insufficient and poor demand which is compensated by disbursing

- Other assets were higher since there was no planned sale of acquired assets.

- Revaluation of the end of 2013 in the amount of RSD 543 million with an increase in investment property in the amount of RSD 773 million resulted in larger than planned amount of the fixed assets position.

[26] Position of loans and deposits to customers does not include other lending

| No. | LIABILITIES POSITIONE | ACHIEVED IN 2014 | PLAN FOR 2014 | INDICES (3:4)*100 |
|---|---|---|---|---|
| 1 | 2 | 3 | 4 | 5 |
| | **LIABILITIES** | | | |
| **1.** | **Deposits** [27] | **293,466** | **241,401** | 121,6 |
| 1.1. | Corporate | 57,437 | 39,714 | 144,6 |
| 1.1. | Retail | 207,431 | 182,756 | 113,5 |
| 1.2. | Banks | 28,598 | 18,931 | 151,1 |
| **2.** | Credit lines | 29,020 | 33,140 | 87,6 |
| **3.** | Provisions | 1,641 | 965 | 170,1 |
| **4.** | Other liabilities | 12,588 | 13,753 | 91,5 |
| **5.** | **TOTAL LIABILITIES (1 to 4)** | **336,715** | **289,259** | 116,4 |
| **6.** | Share capital | 40,035 | 40,035 | 100,0 |
| **7.** | Reserves from profit and non-allocated profit | 29,512 | 26,658 | 110,7 |
| **8.** | **TOTAL CAPITAL (6+7)** | **69,547** | **66,693** | 104,3 |
| **9.** | **TOTAL LIABILITIES(5+8)** | **406,262** | **355,952** | 114,1 |

- The rapid growth of corporate deposits at year-end was the result of growth in transaction and short-term deposits, bank deposit growth was the result of the absence of withdrawal of deposits from other financial institutions, and growth in retail deposits, despite the lowering of interest rates, resulted in an increase exceeding the plan.

- In line with the reduced loan demand, part of the credit lines that was planned to be withdrawn during 2014 was postponed for the comng period.

- Provisions recorded significant deviation from the planned values due to a dispute with Inex-Interexport, which was returned to the first instance court, but in the second quarter of 2014 the entire amount of RSD 755.6 million was paid back to the Bank, and that amount was allocated to the provision for litigations in full.

- Other liabilities were below the plan, primarily due to a net reduction in the amount of foreign currency buying and selling on the cut-off date.

- Total capital is higher than planned due to an increase in revaluation reserves above the plan and higher unallocated profit, or lack of income tax from 2013.

[27] Position *deposits* does not include other liabilities and funds raised through credit lines

*13.2. Achievement of the 2014 P&L Plan*

(In RSD million)

| No. | POSITION | ACHIEVED IN 2014 | 2014 PLAN | INDICES (3:4)*100 |
|---|---|---|---|---|
| 1 | 2 | 3 | 4 | 5 |
| 1.1. | Interest income | 21.224 | 22.005 | 96,5 |
| 1.2. | Interest expenses | 7.925 | 9.044 | 87,6 |
| **1.** | **Net interest income (1.1.-1.2)** | **13.299** | **12.961** | 102,6 |
| 2.1. | Fee and commission income | 5.677 | 5.769 | 98,4 |
| 2.2. | Fee and commission expenses | 959 | 966 | 99,3 |
| **2.** | **Net fee and commission income (2.1. -2.2.)** | **4.718** | **4.803** | 98,2 |
| **3.** | Net exchange differences and changes in value (currency clause) | -206 | - | |
| **4.** | Other operating income | 660 | 250 | 264,0 |
| **5.** | Net losses on impairment and provisions | 2.725 | 2.650 | 102,8 |
| **6.** | Operating and other expenses | 10.988 | 10.651 | 103,2 |
| **7.** | **OPERATING PROFIT** | **4.758** | **4.713** | 100,9 |

- Net interest income is higher than planned, despite the effects of the application of "unwinding" concept (reduction in interest income by RSD 442.6 million), owing to the active structure and funding sources price management and investing in securities, which partially eliminated the effect of the decrease in lending rates and low corporate credit demand.

- Achieved other operating income was significantly higher than planned on the basis of interest income from previous years due to the application of the "unwinding" concept (RSD 442.6 million) and dividends received from Komercijalna Banka a.d. Budva (RSD 120.7 million).

- In order to protect against credit risk, in 2014 the Bank continued to pursue a policy of providing the required level of impairment in accordance with the plan and in line with persistently increasing credit risk.

- Operating and other expenses are above the planned amount (3.2%) due to rising cost of deposit insurance premiums.

- The profit achieved in 2014 is by RSD 44.6 million, or 0.9% above the plan.

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KOMERCIJALNA BANKA AD BEOGRAD
Svetog Save 14
11000 Beograd
No. 8335/15
21.04.2015.

Pursuant to Article 368 of the Company Law (RS Official Gazette No 36/2011 and 99/2011), Komercijalna banka AD Beograd issues the following

## STATEMENT

In its operation Komercijalna banka AD Beograd, Svetog Save 14 (hereinafter: the Bank), applies the Corporate Governance Code of the Serbian Chamber of Commerce, adopted by the Assembly of the Serbian Chamber of Commerce and published in RS Official Gazette No. 99/2012. Text of the Corporate Governance Code is publicly available on the website of the Serbian Chamber of Commerce www.pks.rs – chamber services, corporate governance.

Corporate Governance Code has established the principles of corporate practice that are adhered to by the persons responsible for the Bank's corporate governance. The aim of the Code is to introduce good business practice of corporate governance and equal influence of all stakeholders (current and potential shareholders, employees, clients, the Bank's bodies, the Government, etc.). The final aim is to ensure the Bank's sustainable and long-term development.

Corporate governance rules are implemented through the Bank's internal documents and there are no deviations in their implementation.

KOMERCIJALNA BANKA AD BEOGRAD

| Deputy President of the Executive Board | President of the Executive Board |
|---|---|
| Dragan Santovac | Ivica Smolić |

KOMERCIJALNA BANKA
AD Beograd

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KOMERCIJALNA BANKA AD BEOGRAD
Svetog Save 14
No 9008
28/04/2014
11000 Beograd

*Pursuant to Article 50 of the Law on Capital Market (RS Official Gazette No. 31/2011) Komercijalna banka AD Beograd issues the following*

*S T A T E M E N T*

*I hereby state that, according to my best knowledge and based on the opinion of an external auditor, the annual financial statements have been prepared using the appropriate international financial reporting standards and provide truthful and objective information about the assets, liabilities, financial position and operations, profits and losses, cash flows and changes in equity of the public company.*

KOMERCIJALNA BANKA AD BEOGRAD

| Director of the Accounting Division | Executive Director for Finance and Accounting |
|---|---|
| Snežana Pejčić | Savo Petrović |

КОМЕРЦИЈАЛНА БАНКА АД БЕОГРАД
БЕОГРАД
4

*Executive Board*
*No. 8996*
*29.04.2015*

NOTE

*The financial statements for 2014 have been adopted by the Board of Directors on 04/29/2015 and in accordance with Article 73 of the Banking Act are forwarded to the Shareholders' Meeting for final approval. An independent auditor verified financial statements of the Bank and the Annual Report for 2014 and issued a positive opinion.*

*The decision to adopt the Annual Report of the Bank for 2014, Decision on Adoption of the Annual Financial Statements of the Bank for 2014 with the opinion of the external auditor and the Decision on Distribution of Profit from 2014 have not been passed, as the regular General Meeting of the Bank's Shareholders, where such decisions are made, was not held until the disclosure date of the Annual Report.*

*Decisions will be made public in accordance with the provisions of the Capital Market Law, following the adoption by the General Meeting of the Bank's of Shareholders at a regular session.*

KOMERCIJALNA BANKA AD BEOGRAD

| | |
|---|---|
| Deputy President of the Executive Board | President of the Executive Board |
| Dragan Santovac | Ivica Smolić |

Beograd, April 2015.

KOMERCIJALNA BANKA AD BEOGRAD

| Deputy President of the Executive Board | President of the Executive Board |
| --- | --- |
| Dragan Santovac | Ivica Smolić |
| Dragan Santovac 289063-2509960850014 | Ivica Smolić 289064-0308969810055 |
| Digitally signed by Dragan Santovac 289063-2509960850014<br>DN: c=RS, o=KOMERCIJALNA BANKA AD, cn=Dragan Santovac 289063-2509960850014, sn=Santovac, givenName=Dragan, email=dragan.santovac@kombank.com<br>Date: 2015.04.30 12:02:35 +02'00' | Digitally signed by Ivica Smolić 289064-0308969810055<br>DN: c=RS, o=KOMERCIJALNA BANKA AD, cn=Ivica Smolić 289064-0308969810055, sn=Smolić, givenName=Ivica, email=ivica.smolic@kombank.com<br>Date: 2015.04.30 11:59:02 +02'00' |