

REPORT

**on Disclosure of Data and Information of
Komercijalna banka A.D. Beograd Group for the year 2013**

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1. INTRODUCTION

- Komercijalna banka AD Beograd Banking Group (hereinafter: Group) in accordance with the Law on Banks and the Decision on Disclosure of Data and Information by Banks, further below publishes the Report for the year 2013.
- This Report contains qualitative and quantitative information as prescribed by the above mentioned Decision.
- The Report shall be publicized on the Bank's Internet domain (www.kombank.com).

THE EXECUTIVE BOARD OF THE BANK

Andrijana Milanović

Member of the Executive Board

Ivica Smolić

President of the Executive Board

2. GENERAL INFORMATION ABOUT THE BANKING GROUP

- Komercijalna banka AD Beograd Group is composed of Komercijalna banka AD Beograd, as a parent bank and three subsidiary legal entities:
- Komercijalna banka AD Budva (100% in the Bank ownership) was incorporated in November 2002 and entered in the Central Register of the Economic Court of Podgorica on 6 March 2003,
- Komercijalna banka AD Banja Luka (99.99% in the Bank ownership) was incorporated in September 2006 and entered on September 15th of the same year in the Court Register based on the Ruling of the First Instance Court of Banja Luka.
- Investment Fund Management Company - Kombank Invest AD Beograd (100% owned by the Bank) was established in December 2007 and registered on 5 February 2008.
- The Group's largest shareholder is the Republic of Serbia (42,6%), which has the strategic agreement with the second largest shareholder EBRD (25%). Among the shareholders of Komercijalna Banka there are also a number of internationally renowned professional investors (IFC, Swed Fund, DEG...), as well as different powerful domestic public and private companies.

3. RISK MANAGEMENT

3.1. Risk Management Strategy

- The Banking Group has established the comprehensive and reliable risk management system, which allows for management of all risks that the Group is or may be exposed to on the basis of all business operations and which is proportionate to the nature, scope and complexity of Group's business activities. The established system of risk management ensures that the risk profile is in line with the determined propensity towards risks, and/or the risk profile of the Group.
- Risk management system at the Banking Group level is defined by the following internal legal documents:
 - Risk Management Strategy, Capital Management Strategy and Capital Management Plan;
 - Risk Management Policies;
 - Risk Management Procedures;
 - Methodologies for Risk Management;
 - Other internal documents.
- Risk Management Strategy regulates the uniform and consistent managing of risks to which the Group is or may be exposed in its operations and the same is aligned with the Business Policy and Strategy.
- The implementation of the Risk Management Strategy shall be the responsibility of the competent authorities of the parent Bank and those organizational units which implement and participate in risk management system, as well as bodies and organizational units of Group members:

General Meeting of Shareholders of the parent Bank:

- adopts the parent Bank's business policy and its strategies;
- renders decisions to increase the capital, and/or decides on equity investments in another bank or other legal entities, and also on level of investments in fixed assets of the parent Bank.

Board of Directors of the parent Bank:

- responsible for establishing a uniform system of risk management of the Group and also for supervising such system;
- adopts risk management strategy and policies, along with Capital Management Strategy and Plan at Group level ;
- establishes the internal controls system at Group level;
- supervises the work of the Executive Board of the parent Bank;
- adopts the program and plan of the internal audit;
- reviews the reports of external and internal audit at Group level;
- ensures the implementation of the internal capital adequacy assessment process and its compliance with the strategic objectives of business operations.

Executive Board of the parent Bank

- implements the risk management strategy and policies, and capital management strategy and plan;
- adopts and analyzes the efficiency of implementation of procedures for risk management, which define more closely the process of identifying, measuring and assessment of risk and risk management and reports to the Board of Directors in connection with those activities and semiannual and annual statements at Group level;

- adopts procedures and methodologies for risk management and internal capital adequacy assessment at Group level;
- implements the procedures for supervising Group activities, regularly assesses their quality and, if necessary, enhances them in accordance with the Business Policy

Audit Committee of the parent Bank

- analyzes and adopts the Group's draft strategies and policies pertaining to risk management and internal controls system which are submitted to the Board of Directors for review and adoption;
- analyzes and supervises the application and adequate implementation of adopted strategies and policies for risk management along with the implementation of internal controls system;
- analyzes the consolidated statements of the Group which are submitted to the Board of Directors for consideration and adoption;
- reviews the Statements/Reports of external and internal audit at Group level.

Asset/Liability Management Committee (ALCO)

- Each Group member has the Asset/Liability Management Committee.

Credit Committee

- Each Group member has the Credit Committee which makes decisions within its competences and limits.
- Competences of other Committees of the Group which participate in the risk management system are determined by regulatory provisions and documents that are applied at Group level, whereas the competences of the Committees of the Group members are defined by local legislation and their internal documents.

Risk Management Function of the parent Bank

- independent business function responsible for risk management at Group level, which performs the following:
 - defines and proposes for adoption the strategy and policies of risk management;
 - defines and proposes for adoption the procedures and methodologies of risk management;
 - develops models and methodologies for risk identification, measuring, mitigation, monitoring and control,
 - identifies, measures, assesses, monitors and manages the risks which the Group is exposed to in its operations;
 - reports to the competent authorities of the Group on risk management on consolidated basis (Bank's Board of Directors, Audit Committee, Executive Board, Asset/Liability Management Committee...).

Treasury Management Division of the parent Bank:

- it is included in process of asset and liquidity management, as well as with asset/liability management at Group level. Likewise, it participates in liquidity risk, interest rate risk and foreign exchange risk management.

Compliance Division of the parent Bank

- responsible for:
 - identification and monitoring of Group operations compliance risk and for managing such risk, which particularly includes and refers to risk of sanctions by regulatory authority and risk of financial losses, as well as reputational risk.

Internal Audit Function of the parent Bank

- competent and responsible for:
 - continuous supervision of implementation of risk management policies and procedures at Group level and examines the adequacy of procedures and compliance of the Group with them. Internal Audit reports on its findings and recommendations to the Audit Committee and Board of Directors.
- Banking Group members have the organizational units for risk management, prevention of money laundering, asset management and internal audit.
- By its Risk Management Strategy the Group included the following:
 - overview and definition of all the risks which the Group is, or may be exposed to;
 - long-term objectives, established by the Group's Business Policy and Strategy, and also propensity to risks as determined in accordance with those objectives;
 - basic principles of assuming and managing the risks;
 - basic principles of internal capital adequacy assessment process of the Group.
- The Group has identified and defined the risks to which it is exposed, or to which it may be exposed in its operations, as follows:
- **Credit risk** is the risk of possible negative effects on financial result and capital of the Group that might occur due to debtors' failure to discharge their liabilities to the Group. Credit risk includes:
 - **Residual risk** - risk that the credit risk mitigation techniques may be less efficient than expected, or that their implementation/use has an insufficient impact on reduction of all the risks to which the Group is exposed.
 - **Dilution Risk** - is the risk of possibility of occurrence of adverse effects on Group's financial result and capital due to reduced value of purchased receivables as a result of cash or non-cash liabilities of the former creditor to the

debtor.

- **Settlement/Delivery Risk** – is the possibility of adverse effects on the Group's financial result and capital arising from unsettled transactions or counterparty's failure to deliver in free delivery transactions on the due settlement/delivery date.
- **Counterparty Risk** – is the possibility of occurrence of adverse effects on the Group's financial result and capital arising from counterparty's failure to fulfill his part of the deal in a transaction before final settlement of cash flows of the transaction
- **Credit – Foreign Exchange Risk** – is the possibility that the Group shall suffer the loss due to debtor's failure to discharge his liabilities within the agreed time limits and which arises due to adverse effect of changes in RSD exchange rate on debtor's financial position.
- **Environmental Risk** (risk of environmental and social protection) – risk of occurrence of adverse effects on Group's financial result, capital and reputation due to event which has or is likely to have a material adverse effect on the environment, health or safety, or the community as a whole.
- **Concentration Risk** is the risk which directly or indirectly arises from exposure of the Group to the same or similar risk factor or type of risk, such as exposure to one party or a group of related parties, industries, geographic areas, types of products and activities, credit protection instruments, financial instruments, commodities...
- **Investment Risk** is the risk which arises from Group's investment in other legal entities and fixed assets.
- **Country Risk** is the risk relating to the country of origin of the entity to which the Group is exposed, or the risk of possible negative effects on the financial result and capital of the Group due to Group's inability to collect claims from such entity/debtor for reasons arising from political, economic or social conditions in such entity's/debtor's country of origin. Country risk includes the following risks:
 - **political and economic risk**, which means the probability of loss due to the inability of the Group to collect the receivables due to the limitations imposed by state laws and bylaws and other authorities of the country of origin of the debtor, as well as general and systemic conditions in that country;
 - **transfer risk**, which means the probability of loss due to inability to collect the receivables denominated in a currency other than the currency of the country of origin of the debtor and due to limitations in payments of liabilities to the creditors from other countries in a particular currency as determined by legislation of the state and other authorities of the country of the debtor.
- **Operational Risk** is the risk of possible occurrence of adverse effects on Group's financial result and capital due to unintentional and intentional omissions in the work of employees, inadequate internal procedures and processes, inadequate management of information and other systems in the Group, as well as due to occurrence of unforeseen external events. Operational risk includes legal risk.
 - **Legal risk** is the risk of occurrence of adverse effects on Group's financial result and capital on the basis of court or out-of-court proceedings in connection with Group's operations (labor relations, contracts and torts...)
- **Liquidity Risk** is the risk of possible negative effects on the financial result and capital of the Group caused by the Group's inability to meet all its due obligations, on account of:
 - **Withdrawal of the existing funding sources**, or inability to obtain new sources of funding (funding liquidity risk), or
 - **Difficulty of converting assets into liquid assets due to market disruption (market liquidity risk).**
- **Interest Rate Risk** is the risk of possible negative effects on the financial result and capital of the Group arising from positions in the banking book due to adverse changes in interest rates.
- **Market Risks** are the risks of possible occurrence of adverse effects on Group's financial result and capital on the basis of losses in the balance sheet and off-balance sheet positions due to market price movements, and the same include the following:
 - **Foreign Exchange Risk** is the risk of occurrence of negative effects on the financial result and capital of the Group caused by changes in exchange rates for the items that are kept in the banking book and the trading book.
 - **Price Risk** based on debt and equity securities is the risk of possible occurrence of negative effects on Group's financial result and capital due to losses caused by market price fluctuations of debt and equity securities in the trading book.
 - **Commodity Risk** is the risk of occurrence of adverse effects on the financial result and capital of the Group due to losses caused by the movement of prices of commodities in the market.
 - **Options Risk** is the risk of possible occurrence of negative effects on Group's financial result and capital due to losses caused by movement of prices of options in the market.

The Group is not exposed to options risk or commodity risk.
- **Compliance Risk** is the risk of possible occurrence of negative effects on the financial result and capital of the Group due to Group's failure to comply its operations with the law, bylaws, its internal documents, procedures for prevention of money laundering and financing of terrorism, as well as with the rules of profession, sound business practices and

business ethics and in particular encompasses the risk of sanctions by the regulatory authority, risk of financial losses and reputational risk.

- **Reputational Risk** is the risk of possible occurrence of adverse effects on Group's financial result and capital due to the loss of public confidence and unfavorable public attitude about the Group's business operations, irrespective of whether there exist the grounds for it or not.
- **Strategic Risk** is the risk of probable negative effects on Group's financial result or capital due to lack of appropriate business policy and strategy, their inadequate implementation and also due to changes in environment in which the Group operates, or Group's failure to properly react to such changes.

Long-term Objectives

- Long-term objectives for Group's risk management are as follows:
 - development of activities in line with the Business Strategy and opportunities and market development in order to create a competitive advantage;
 - avoiding or minimizing the risk in order to maintain the business operations within the acceptable level of risk;
 - minimizing negative effects on Group's capital;
 - maintaining the required level of capital adequacy;
 - diversification of risks to which the Group is exposed.
- The objectives of risk management are aligned with the Business Plan and can be modified during the year.
- The Group defines the risk profile and tendency for assuming risk on the basis of capacity to cover risk
- The Risk Management Process includes clear defining and documenting the risk profile and compliance of risk profile with Group's propensity to risk assuming.
- Propensity to risks shall imply the Group's intention to assume risks in order to accomplish its strategies and policies and to establish this assumption to be at acceptable risk level.

Basic principles of risk assumption and management

- The basic principles of risk assumption:
 - establishing explicit and clear rules for managing the individual types of risks, with associated policies and procedures for management of individual risk types with corresponding objectives of operations at Group level;
 - gathering of complete, timely and truthful information important for risk management and provision of adequate capacities for safekeeping and processing of data;
 - conservative risk taking – implies that the relation towards the risks undertaken by the Group is such that the expected yields significantly outweigh losses which may incur by risk taking;
 - making business decisions determined by the qualitative and quantitative analysis on the basis of applicable risk parameters;
 - utilization of a number of methods for risk identification and measurement – when managing the risks the Group, in addition to regulatory prescribed frameworks and approaches for risk management, also applies the internal methods taking into account their applicability and justifiability in terms of investment in their development and justification of their implementation in terms of complexity and volume of business activities.
 - development of quantitative modeling mechanism which allows measurement analysis of the effects of changes in the business and market environment on Group's risk exposure profile and further impact on profitability, liquidity and net worth of the Group.

3.2. Risk Management Policies

- Risk Management Policy determines the following:
 - implementation of the risk management strategy by all risk types: credit, market, interest rate, liquidity and operational risk;
 - manner of organizing the risk management process of the Group and clear division of the employees' responsibilities at all stages of that process;
 - manner of assessing the risk profile of the Group members and methodologies for risk identification, measurement or assessment;
 - methods of risk monitoring and control and establishment of the system of limits or the types of limits used by the Group, and their structure;
 - measures for risk mitigation and rules for applying such measures;
 - manner and methodology for implementing the internal capital adequacy assessment process of the Group;
 - principles for the functioning of the internal controls system;
 - framework and frequency of stress tests, as well as actions taken in cases of unfavorable stress test results.
- External reporting of the Group is conducted pursuant to the statutory regulations and by-laws of the National Bank of

Serbia.

- Group members on monthly basis report to the Risk Management Division of the parent Bank, which monitors all types of risks at Group level.

3.3. Organizational Structure of the Risk Management Function

- All Group members have established the independent Risk Management Function.
- The Risk Management Function of the parent Bank conducts its activities through the following organizational units: Risk Management Division, Credit Risk Analysis Division and Workout Department.
- Risk Management Division of the parent Bank is responsible for risk management at Group level and preparation of six-month consolidated reports on risk management and it consists of Credit Risk Management Department, Portfolio Monitoring Department, Market Risks Management Department and Operational Risk Management Department.
- Credit Risk Analysis Division of the parent Bank is composed of Department of Credit Risk Analysis for Corporate Clients and Department of Credit Risk Analysis for Retail Clients, Micro Clients and Farmers, which perform activities at parent Bank level from scope of its competences, as well as analysis and providing opinions pertaining to credit proposals exceeding defined limits for subsidiaries.
- Komercijalna banka AD Budva and Komercijalna banka AD Banja Luka carry out the risk management-related activities through established risk management divisions which on monthly basis report to the Risk Management Division of the parent Bank on conducted risk management activities at the level of Group members.

3.3.1. Credit Risk

- Credit risk management policy represents the document which more specifically defines the **credit risk management system**, including the residual risk, the dilution risk, concentration risk, settlement/delivery risk, and the counterparty risk to which the Group is or may be exposed in its operations, as a part of the risk management system.
- The most important processes of the risk management system are:
 - The loan approval process;
 - The process of managing the credit protection instruments;
 - The process of monitoring the loans for early detection of warning signs;
 - The process of credit risk measurement in accordance with the regulations of the Central Banks of the Group members;
 - The process of non-performing loan management;
 - The process of calculation of the minimum capital requirement for credit risk and internal capital adequacy assessment;
- The risk profile of the Group is determined by an acceptable risk level for the Group and in accordance with the Risk Management Strategy and depends on the Group's portfolio structure. The purpose of credit risk management is to minimize the negative effects of the credit risk on the financial result and capital of the Group, on the basis of balance sheet and off-balance sheet items, as well as on the basis of operations with the counterparty for the positions kept in the banking book.
- Credit risk identification starts by filing an application for loan approval.
- The loan approval process consists of gathering and verification of all the necessary documentation, information and data on the basis of which a credit analysis of individual loans is performed, as well as of the credit risk factors.
- Individual loan analysis includes the analysis of qualitative and quantitative indicators of the client's operations, identification of the risk level (establishment of classification pursuant to regulations of the Central Banks of Group members and the client's internal rating according to Group methodology), and the control of the extent to which the limit has been used up at Group level;
- The process of credit risk measurement is based on two approaches:
 - regulatory approach – the loan impairment process and estimation of the provisions for losses under off-balance sheet items according to the International Accounting Standard 39 and the International Accounting Standard 37;
 - internal approach – measurement of the risk level of an individual loan on the basis of the internal rating system of the Group.
- Within the loan approval process, exposure relative to regulatory and internally defined limits is reviewed.
- Loan approval limits are defined by decision-making system of each Group member, depending on the types of clients and the level of exposure.
- For each subsidiary of the Group an individual decision making limit is defined, pertaining to the maximum amount up to

which the subsidiaries can independently place funds, i.e. without obtaining the opinion from the Credit Risk Analysis Division of the parent Bank.

- In order to maintain the risk at acceptable level, the Group members apply the credit risk mitigation techniques at the level of individual loan by observing the exposure limits, diversification of investments, and by acquiring acceptable collaterals for the purpose of secondary collection.
- Upon approval of a loan, the loan itself and the client's operations are monitored through regular and extraordinary monitoring in order to timely identify the warning signs.
- By monitoring and controlling the portfolio as a whole and by individual segments, the Group members make comparisons to the previous time periods, identify the trends and the causes of changes in the level of credit risk. Likewise, they monitor the asset quality indicators (NPL trends, NPL coverage by allowance for impairment...), as well as the exposure to regulatory and internally defined limits.
- Reporting on credit risk at the Group's level includes the system of external and internal reporting on credit risk management. External reporting on consolidated basis is carried out in accordance with the requirements of the National Bank of Serbia and the International Financial Reporting Standard 7 for credit risk, and the internal reporting in accordance with the Group's internal documents.
- The report on credit risk management includes: total exposure to credit risk on consolidated basis, exposure to credit risk according to internal rating system, due receivables, risky placements and loans, collaterals, allowance for impairment, exposure risks...

3.3.2 Liquidity Risk

- The basic objective of the liquidity risk management is to maintain the level of liquid assets in order to properly and timely settle the due liabilities on balance sheet and off-balance sheet operations at Group level and of each member separately, or to minimize the negative effects on the financial result and capital at Group level and each member separately.
- The Group has established an adequate organizational structure, business activities, the lines of decision-making and responsibilities by a clear delineation of the liquidity risk management process (implemented by the independent function responsible for risk management of the parent Bank and also the independent functions of individual members) and the process of support to managing this risk from the process of liquidity risk taking.
- Basic principles of liquidity risk management:
 - the readiness to respond to matured obligations, through maintenance of minimum level of liquid assets for Group members;
 - maintenance of the match between inflow and outflow of assets by limiting the currency and maturity mismatch of receivables and liabilities;
 - establishment of planned activities in the case of occurrence of unforeseen events (liquidity crisis).
- In 2013 the Bank implemented an application for managing assets and liabilities, thereby significantly improving the existing methodologies, and introduced new liquidity risk management models, with the aim of measuring this risk more accurately.
- Measurement of exposure to liquidity risk includes the assessment of the current and the future exposure to liquidity risk and the same is conducted by applying the regulatory and internally defined methods and models:
 - Regulatory approach – application of liquidity ratio and more specific liquidity ratio at Group level;
 - Internal approach – application of static and dynamic GAP and ratio analysis, stress testing (sensitivity analysis and analyses scenario) and simulations.
- The parent Bank has defined the internal standards for liquidity risk management, which refer to defined internal limit of liquidity ratio, limits of liquidity gaps by maturity, identification and quantification of early elements of liquidity crisis.
- In order to manage the liquidity risk the system has been established of external (prescribed by local regulatory authorities of the Group members' countries) and internal limits (adopted by competent committees of the Group). Regulatory defined liquidity limits are observed by all Group members and they maintain the liquidity level above defined minimum values, aligning their operations with the limits defined at Group level. For the purpose of liquidity risk management the system of monitoring of limits has been established. The limits which the Group and Group members observe refer to maintaining minimum liquidity ratios in period of 1 day, 3 days and average for a month. When defining the limit of exposure to liquidity risk, multiple aspects of liquidity risk are reviewed, taking into account the limiting negative effect on financial result and capital, thus limiting the maturity mismatch.
- The Group has established the monitoring and control of liquidity risk process, which includes the monitoring of business activity compliance with the defined limit system, in order to maintain the liquidity risk at the level accepted by the defined risk profile of the Group, as well as to follow up and monitor the implementation of measures. The liquidity risk monitoring and control have been established and integrated in all business activities of the Group and at all levels

of liquidity risk management, as has also been established an independent control of the assessment of adequacy, reliability and efficiency of the liquidity risk management system.

- In order to maintain the liquidity risk at the level accepted by the defined risk profile, the Group applies the techniques and measures of liquidity risk mitigation in the conditions when the exposure to liquidity risk tends to the upper limit of the defined risk profile. The applied techniques relate to maintenance of sufficient level of liquidity reserves, or marketable liquid assets in major currencies, diversification of funding sources by maturity and currency, reducing the concentration of funding sources by sector structure, for the purpose of establishing a stable base of sources of funds.
- The Group has in place the established system for liquidity risk reporting which includes assessment and analysis of the exposure to the liquidity risk, compliance with the limits, results of the stress test analysis and proposal of measures.

3.3.3. Interest Rate Risk in the Banking Book

- The objective of interest rate risk management is to preserve the economic value of the Group's capital, with simultaneous minimization of negative effects of changes in interest rates on the financial result, for the positions that are kept in the Banking Book.
- The Group has established an appropriate organizational structure, business activities, decision-making and responsibilities lines, by clear delineation of risk assumption process from risk management process.
- Asset/Liability Management Committee has a significant and primary role in interest rate risk management process, within its competence. Likewise, in interest rate risk management process other parent Bank's Committees have their roles and their decisions may have an impact on exposure to the above stated risk.
- Basic principles of Group's interest rate risk management are:
 - maintenance of interest rate risk level which allows for minimizing the negative effect of changes in interest rates on the market and also the maintenance of minimum required interest rate margin;
 - limitation as to maturity and currency mismatch for the purpose of preserving the economic value of capital, or minimizing the negative impact of interest rate changes on exposure to interest rate risk;
 - optimization of the cost of funds with adaptation and caution during the formation of competitive interest rates on products Group members.
- During 2013 the Group implemented an application for managing assets and liabilities and thereby significantly improved the existing methodologies and introduced new interest risk management models with the aim of measuring this risk more accurately.
- Identification of the interest rate risk implies the analysis of all the indicators and factors which lead to occurrence and increase of exposure to interest rate risk, along with the type of interest rate risk to which the Group and its members are exposed.
- Measurement of interest risk constitutes a quantitative and qualitative assessment of exposure to interest risk and is conducted using the internal models of static and dynamic GAP and ratio analysis, economic value of capital, net present value and stress testing.
- Measurement of interest rate risk of the Group represents the quantitative and qualitative assessment of the exposure to interest rate risk by applying gap and ratio analysis, duration, economic value of capital and stress testing. Mitigation of interest rate risk is conducted continuously by maintaining the risk at acceptable level for risk profile and by establishing and implementing the adequate measures and techniques. In interest rate risk management process the Group applies the external limits system (defined by local regulatory authorities of the Group members' countries) and internal limits (adopted by the competent committees of the Group) defined separately for members, as well as limit at Group level. When defining the exposure limit to interest rate risk the Group takes into account multiple aspects of interest rate risk, thus limiting the negative effect on the financial result and the economic value of the capital. At Group level the limits are defined of interest-bearing positions, and limit of changes of the economic value of capital, by which the negative impact on capital is limited.
- Group has established the process of monitoring and control of interest rate risk, which includes the monitoring of compliance of operations with defined system of limits, for the purpose of maintaining the interest rate risk at the level accepted by the defined risk profile of the Group, as well as the follow-up and monitoring of implementation of the measures. The system of internal interest rate risk control is integrated in all business operations of the Group, as is also the independent control of the assessment of adequacy, reliability and efficiency of the interest rate risk management system.
- The Group has established the process for monitoring and reporting on the effects of implementation of applied risk mitigation measures and techniques, that are aimed at maintaining the match of interest rate-sensitive positions, diversifying the funding sources by type of interest rate, maturity, or repricing and currency and at optimizing the cost of funds.

- The system of reporting on exposure to interest rate risk includes the assessment and analysis of the exposure to interest rate risk, compliance with the limits, results of stress test analysis and proposals of measures.

3.3.4. Market Risk

- In its everyday operations the Group is exposed to foreign exchange risk and price risk.

Foreign Exchange Risk Management

- The objective of foreign exchange risk management is to ensure safe operation of the Group, through minimization of the negative effects of changes in the exchange rate on the financial result and capital of the Group, for the positions that are kept in the banking book and the trading book.
- The Group has established an appropriate organizational structure, business activities, decision-making and responsibilities lines, by clear delineation of foreign exchange risk assumption process from the process of its management and the support process at Group level and individual members.
- Identification of the foreign exchange risk refers primarily to consideration of transaction and balance sheet exposure, and also to exposure arising from introduction of new products and activities and to analysis of internal and external factors. Identification of exposure to foreign exchange risk is conducted at the level of exposure to a single currency and also at the level of entire foreign exchange portfolio for all the currencies.
- Measurement of foreign exchange risk represents quantitative and qualitative assessment of the exposure to foreign exchange risk and includes the assessment of the current and the future exposure to foreign exchange risk and is performed by applying the regulatory and internally defined methods and models:
 - Regulatory approach – application of foreign exchange risk ratios at Group level;
 - Internal approach – stress testing (sensitivity and scenario analysis) and simulations, value at risk and back testing.
- The Group conducts a continuous mitigation of foreign exchange risk by maintaining the risk at acceptable level for risk profile, and also by establishing and applying the appropriate measures and techniques, and by follow up and monitoring of implementation of the measures. The Group implements the system of external (prescribed by regulators) and internal limits (adopted by competent committees of the Group), established on the basis of foreign exchange risk ratio at Group level and each individual member. When defining the exposure limit to foreign exchange risk multiple aspects of foreign exchange risk are taken into account, thus limiting the negative effect on the financial result and capital of the Group.
- The Group uses derivatives and other instruments and measures in the segment of assets and funding sources in order to minimize and mitigate the exposure to the mentioned risk.
- At the level of Group and its members the system has been established of follow up and control of limits and implementation of measures for minimizing the foreign exchange risk.

Price Risk Management

- The Group has established an appropriate organizational structure, business activities, decision-making and responsibilities lines, by clear delineation of risk assumption process at the level of members and Group from the process of its management and support, and guided by the principles of the risk management system organization of the trading book.
- Basic principles for Group's price risk management are:
 - maintenance of the risk level in compliance with the externally and internally defined limits;
 - monitoring the changes on the market that may lead to increased exposure to the trading book risks;
 - determination of the measures for mitigating the exposure to risks in the circumstances when the Group tends to the upper limit of the accepted risk profile of the risk exposure.
- Identification of the risk of trading book operations includes the analysis of all the indicators and factors which lead to occurrence and increase of the risk profile.
- Measurement and assessment of the risk of trading book operations includes the following implementation:
 - standardized (regulatory prescribed) approach
 - internal model by using Value at Risk methodology.
- The Group has in place the established system of internal limits adopted by the competent Committees and Boards of the Group, both at Group level and at the level of individual members. At the Group level defined are: the exposure limits for all trading book positions and limits of trading book share in overall operations of the Group.
- The system of price risk internal control is integrated in all business activities of the Group, as is also the independent control of the assessment of adequacy, reliability and efficiency of the price risk management system.
- Mitigation of price risk the Group carries out continuously by maintaining the risk at acceptable level for risk profile and

by establishing and implementing the adequate measures and techniques. Defining and applying the appropriate safeguards and preventive measures, defining the exposure limit and defining and implementing the measures for price risk mitigation characterize the phase of mitigating the price risk.

- The system of price risk internal control is integrated in all business activities of the Group, as is also the independent control of the assessment of adequacy, reliability and efficiency of the price risk management system. Control of price risk includes also the regular control of each transaction.
- Pursuant to the established system of reporting on Group's price risk, the reporting is performed on exposure to price risks.

3.3.1. Operational Risks

- In order to minimize occurrence of an operational risk event, the Group establishes an appropriate framework which includes: the process of identifying the operational risk event, the process of classifying the operational risk events according to risk level, the analysis of the operational risk event, the process of monitoring the operational risk event, the process of monitoring the measures for operational risk mitigation, and the system of early detection of operational risk event.
- When assuming the operational risk the Group is guided by the following principles:
 - business operations in accordance with the good operational risk management practices;
 - provision of adequate controls for operational risk management;
 - timely identification and continuous monitoring of the operational risk event, minimization of operational risk event occurrence by implementation of the measures;
 - analysis of key risk indicators that lead to occurrence of operational risk event,
 - measurement of the current exposure to operational risk and the assessment of the exposure based on the introduction of new products and activities on the implementation of measures to minimize the operational risk events.
- The Group continuously mitigates the operational risk, which involves maintenance of the risk at the acceptable level for risk profile, through determination of measures to minimize the operational risk mitigation measures, which include the following:
 - definition of the exposure limit;
 - definition and application of the operational risk mitigation measures;
 - system of physical controls;
 - Business Continuity Plan and
 - Disaster Recovery Plan.
- Operational risk monitoring and control involve the monitoring of the compliance of business operations with the defined system of limits for the purpose of maintaining the operational risk at the level accepted by the defined risk profile of the Group, as well as the follow-up and monitoring of implementation of the measures. Operational risk monitoring and control have been established and integrated in all business activities of the Group and at all levels of operational risk management, as has also been established the independent control for assessing the adequacy, reliability and efficiency of the operational risk management system.
- The Group has established the process of monitoring and reporting on the effects of implementation of the applied measures and techniques of operational risk mitigation through regular reporting to the competent committees and bodies, and a clear division of responsibilities, definition of the rules with regard to frequency of reporting on implementation of the measures adopted to minimize the operational risk.
- The system of reporting on operational risk includes timely reporting on the operational risk events by event type and business lines, the causes and sources of the event occurrence, significance of the event, exposure trend, measures intended to be taken or already taken for the purpose of mitigating and limiting the consequences of the events, and activities entrusted by the Group to third parties.

3.3.2. Country Risk

- The objective of country risk management is to ensure minimum exposure through adequate country risk measurement by applying the adopted methodology and defined limits of exposure to countries or a group of countries on the basis of the country rating.
- Identification of country risk includes the analysis of all the indicators that give rise to and increase the country risk, carried out at the level of the individual placement and the overall portfolio.
- Prerequisite for achieving the defined objectives of the country risk management is the existence of adequate and updated database containing the recorded information provided by the business sectors on client's domicile country and his place of residence.

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- Measurement of country risk is based on external credit ratings of client's domicile country, on the basis of which the loans are classified/grouped to certain level of risk.
- The Group defines the procedure for country risk monitoring and control as monitoring of the limit on consolidated level, and of the measures adopted for mitigating the country risk, as well as the control process.
- The Group has in place the established system for country risk reporting on consolidated level by which the management, competent committees and organizational units are timely informed.

3.3.3. Investment Risk

- The Group has the established investment risk system, thus ensuring that the investment outside the financial sector does not exceed 10% of the Group's capital, and that the Group's investments in financial sector and in fixed assets do not exceed 60% of the capital of the Group.

4. BANKING GROUP CAPITAL

- The Group's Capital Strategy and Plan concretely stipulate and specify the implementation of the strategic objectives and guidelines for capital planning, and set the time period for their accomplishment in view of the impact of macro-economic indicators and changes in economic cycle trends on the strategic plans, the manner in which the Group will respond to capital requirements in the future, and relevant limitations on the capital, as well as the general plan for acting in unforeseen circumstances.
- Pursuant to the defined targeted values, the Group members undertake measures for their realization and maintenance.

Capital structure	RSD 000	
Name	31.12.2013.	31.12.2012.
CORE CAPITAL	46.429.841	52.667.051
Nominal value of paid up shares, except for cumulative preferred shares,	17.191.466	17.191.466
Paid up ordinary shares	8.709.310	8.709.310
Paid up non-cumulative preferred shares	373.510	373.510
Paid up convertible preferred bank shares	8.108.646	8.108.646
Issue premium	22.843.084	22.843.084
Reserves from the profit	17.063.823	15.149.319
Profit of current year	-	-
Profit from previous years	-	434.631
Deductible items from core capital	12.109.578	4.339.873
Intangible investments	588.924	644.258
Amount of bank shares taken in pledge, except for cumulative preferred shares	290.274	151.903
Non-realized losses arising from securities available/held for sale	187.011	7.016
Required reserves from profit for estimated losses under balance sheet assets and off-balance sheet items of the bank	11.043.369	3.536.696
Minority stakes in subsidiaries	63	62
Other positive consolidated reserves	1.440.983	1.388.362
SUPPLEMENTARY CAPITAL	4.988.153	5.329.728
Part of revaluation reserves of the bank	1.548.890	780.996
Subordinated liabilities	3.439.263	4.548.732
DEDUCTIONS FROM CAPITAL	11.233.079	10.799.045
Direct and indirect investment in banks and other entities in the financial sector in amount higher than 10% of the capital of such banks or other entities	189.710	188.957
Required reserve from profit for estimated losses under balance sheet assets and off-balance sheet items of the bank	11.043.369	10.610.088
TOTAL CORE CAPITAL	40.184.914	47.197.734
TOTAL SUPPLEMENTARY CAPITAL	-	-
TOTAL REGULATORY CAPITAL	40.184.914	47.197.734

- The Group calculates the capital adequacy ratio and capital requirements in accordance with the regulations of the National Bank of Serbia by using the standardized approach for credit risks, market risks and operational risks.
- Regulatory prescribed minimum capital adequacy ratio is 12%.

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Overview of total capital requirements according to standardized approach

RSD 000

Capital Requirements	31.12.2013.	31.12.2012.
Credit risk, counterparty risk and settlement/ delivery risk based on free deliveries	21.919.590	23.234.452
Exposures to states and central banks	531.532	738.681
Exposures to territorial autonomies and local government units	280.303	279.583
Exposures to international development banks	2.168	1.362
Exposures to banks	851.943	695.577
Exposures to companies	11.650.157	13.509.333
Exposures to private individuals	3.234.832	3.106.720
Exposures secured by mortgages on real property	2.804.860	2.570.499
Due outstanding receivables	826.943	763.395
Other exposures	1.736.853	1.569.302
Market Risks	152.259	44.180
Capital requirement for price risk based on debt securities	-	-
Capital requirement for price risk based on equity securities	-	-
Capital requirement for foreign exchange risk	152.259	44.180
Capital requirement for commodity risk	-	-
Operational Risks	2.209.153	2.005.952
Exposure to operational risk	2.209.153	2.005.952
Total capital requirements	24.281.002	25.284.584
Capital adequacy ratio (minimum 12%)	19,86%	22,40%

- The Group includes the trading book positions in calculation of capital requirements for credit risk, taking into consideration that value and share of trading book in total operations do not obligate the Banking Group to allocate special capital requirements for market risks.
- Capital requirement for foreign exchange risk is calculated for Group subsidiaries with the FX risk ratio more than 2%
-

4.1. Internal Capital Adequacy Assessment Process – ICAAP

- The Group has set up an internal capital adequacy assessment process (hereinafter ICAAP) in accordance with its risk profile. The aim of ICAAP is to strengthen the relationship between risk management and the Group's capital i.e. to ensure that the Group has sufficient capital at its disposal to support current and future activities and to cover all materially significant risks the Bank is exposed to in its operation.
- ICAAP is included in the risk management system and forms an integral part of the decision-making process in the Group. Also, it is regularly revised and adjusted, especially when the Bank is exposed to new risks or significant changes.
- The Group has established the Capital Management Strategy and the Capital Management Plan. Capital Management Plan includes:
 - Strategic goals and time periods for their implementation, taking into account the impact of macroeconomic environment and economic cycle phases;
 - Manner of organization of available internal capital management process;
 - Procedures for planning the adequate level of available internal capital;
 - Manner of accomplishment and maintenance of adequate internal capital level;
 - Business plan in the case of unforeseen events which can influence the amount of available internal capital.
- ICAAP is a stable risk management process which adequately identifies, measures, aggregates and monitors risks by including all key elements of capital requirements assessment and capital management and planning.
- ICAAP is a documented process which is carried out on a continued basis and in accordance with the Risk Management Strategy and individual Risk Management Policies, and Capital Management Strategy. Basic conditions met by ICAAP implemented in the Group:
 - It is based on the process of risk identification and measurement, or risk assessment;
 - It provides a comprehensive risk assessment, as well as monitoring of the significant risks the Group is or may be exposed to in its operations;
 - Ensures adequate internal capital in accordance with the Group's risk profile;
 - It is incorporated in the Group's management system and in decision-making process in the Group;
 - It is subject to regular analysis, monitoring and verification.
- ICAAP objective is a clear establishment of the capital level that is sufficient to cover all risks the Group is exposed to.
- By determining the potential for risk coverage, the Group indirectly sets the maximum level of the risk it is ready to accept. Apart from assessment of internal capital requirements, internal capital is also assessed through ICAAP.

Planning of internal capital also ensures maintaining the level of capital that can support the growth of loans, future funding sources, dividend policy...

- The framework of internal capital adequacy assessment process reflects the Risk Management Strategy, Capital Management Strategy and Capital Management Plan, and the limits set where ICAAP serves as a comprehensive managing model.
- The Group continuously assesses the risk profile and regularly revises the procedure for internal capital adequacy assessment developing at the same time the methodologies for assessment of other risk types in order for the comprehensive risk management at the Group level to be as efficient as possible.
- The basic principles of the internal capital adequacy assessment process of the Group are:
 - establishment of the internal capital adequacy assessment process of the Group in accordance with the risk management objectives and principles for risk taking and management;
 - identification, measurement (assessment), mitigation and monitoring of all risks as a basis for capital adequacy assessment;
 - establishment of the internal capital adequacy assessment process of the Group in accordance with the volume, type and complexity of the Group's operations;
 - provision of the internal capital in accordance with the risk profile of the Group.

ICAAP Phases:

- Establishment of materially significant risks – Quantitative and qualitative criteria are established based on the methodology, serving to determine the materially significant risks that will be included in the internal capital adequacy assessment process in accordance with the type, volume and complexity of the Group's business operations, as well as the specificities of the markets on which it operates. In assessing the risk materiality, the Group considers all risks to which it is exposed or which it assumes. All assumed risks can be divided into significant, which require allocation of a part of the capital, and those which do not require such allocation since they have been assessed as non-material or the Group manages them through the established risk management system.
- Calculation of the amount of the internal capital requirements for individual risks – the Group uses the methods prescribed for calculation of minimum capital requirements, as well as the internal approaches to measurement. The Group performs the stress testing for all materially significant risks and internal capital, which include the risk factors specific for the environment in which the Group operates. The stress test results are taken into account at assessing and maintaining the internal capital at a certain level.
- For the purpose of inclusion of materially significant risks in ICAAP, the Group applies the following methodologies for the following:
 - **Credit risk** – standardized approach with stress testing by applying econometric models with a time horizon of one year;
 - **Operational risk** – Monte Carlo VaR model with a confidence interval of 99,9%, with application of stress testing.
 - **Market risk (Foreign exchange risk)** – VaR methodology with application of stress testing as well.
 - **Interest rate risk** – methodology of standardized interest rate shock, which also incorporates the changes of factors and stress testing of interest rate risk.
 - **Liquidity risk** – for ICAAP needs, the application of testing of "hypothetical" level of liquidity crisis and the calculation of the amount of missing funds are taken into consideration;
 - **Residual risk** – stress testing of deteriorating efficiency of applied mitigation techniques;
 - **Credit FX risk** – stress testing the effects on increase of exposure to credit risk due to increase in exchange rate;
 - **Strategic risk** – stress testing the negative departures from the planned values of net interest income;
 - **Materially insignificant risks** are included in ICAAP through the system of policies and procedures, system of limits, decision-making system...
- Calculation of total internal capital includes results of stress testing. Also, for regulatory and internal capital planning the time horizon is three years.
- Comparison of the capital amount calculated in accordance with regulatory requirements and the amount of the available internal capital, as well as the minimum capital requirements and the internal capital requirements.

5. EXPOSURE TO RISKS

5.1. Credit Risk and Dilution Risk

In the credit risk analysis and assessment the Group uses two parallel approaches: internal and regulatory.

- Internal rating system is not only the instrument for shaping the individual decisions and the assessment of risk level of an individual loan, but instead it represents the basis for portfolio analysis, support in loan approval process and in

process of loan impairment and also in assessment of provisions for losses under off-balance sheet positions in order to rank the risk exposure level of a loan and to express the real value of claims. Internal rating system is subject to regular audit and improvement.

- In credit risk analysis, in addition to Internal rating system, the Group members also use the principles prescribed by the local regulations of the Central Banks of their countries, which require the classification of each loan based on stipulated criteria and calculation of reserves for credit risk assessment. Application of these criteria allows the Group members to cover the unexpected losses that may be incurred due to inability of the client to settle his liabilities at maturity in line with contractually defined terms. Therefore, the Group members classify the receivables and calculate the required level of provisions, which is a form of protection from possible negative consequences if invested funds are not repaid when due and in full amount.

The matured unsettled receivables the Group defines as all receivables not recovered at maturity (principal, interest and fees, as well as the interventions under guarantees, guarantees of a bill and other forms of sureties, illicit overdraft in clients' accounts, and other due obligations of the clients).

Exposures with performed allowances for impairment are exposures where assessment of their collectability is made, or where reduction is made for the amount of the expected loss.

- The Group has the clearly defined criteria for credit and receivable assessment and recognition, and the criteria for assessing and recognizing the provisions for contingent liabilities, also by observing the requirements of the International Accounting Standards (IAS) 39 and 37.
- Loans are impaired and provisions are made only in the case when there are justifiable grounds, or when there is objective evidence of the impairment as a consequence of the events occurring after the initial recognition of the receivable, and which have an adverse impact on regular settlement of debtor's liabilities to the Group.
- The main elements in assessing the impairment of a loan are: overdue payment of principal or interest, difficulties in cash flows of loan beneficiaries, fall in the credit rating or changes of the original contractual terms and conditions, etc.
- Loan is impaired based on the assessment of expected future cash flows from clients' operation, and by realization of the collateral if assessed that there is a realistic possibility for the loan to be recovered from such funds.

Calculation of Allowances for impairment for Balance Sheet Assets

- The Group members assess the impairment of receivables as individual and group assessment. All clients are grouped pursuant to the internally prescribed methodology based on the Group's internal rating system.
- The procedure for impairment assessment is done on individual level when there is objective proof of loan impairment, for each materially significant loan, and at group level for materially less significant loans. The impairment amount is assessed individually as a difference between the carrying value and the present value of expected future cash flows, determined by discounting the expected inflows from the loan through application of the last agreed effective interest rate of the specific loan. In case of interventions under guarantees and other forms of sureties, the present value is determined by discounting the expected inflows through application of the average annual default interest rate.
- Impairment for materially less significant loans is assessed on a group basis, for each group separately, in view of their similar characteristics in terms of credit risk, as a percentage of migrations of the relevant group to the worst group, adjusted by the percentage of the loan recovery.
- If during individual assessment of materially significant loans it is assessed that there is no objective proof of the loan impairment, such loan will be impaired by the percentage of impairment of the solvency group to which it belongs.
- Loan impairment that reduces the value of a loan is recorded in the provision account in the balance sheet, and is recognized as an expense in the income statement.

Calculation of Provisions for Losses under Off-Balance Sheet Items

- Provisions of the Group members are calculated on individual and group basis. Contingent liabilities with a high degree of probability to entail an outflow of assets are assessed individually, while the rest of contingent liabilities are assessed on group level.
- Assessment of the provisions on the group level is performed based on the migrations of the risk categories by taking into consideration all elements of the internal rating system, in the manner identical to the one applied in the procedure pertaining to balance sheet positions.
- Provisions are recorded within liabilities in the balance sheet and are recognized as an expense in the income statement of the period in which the probability originated.

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Overview of Exposures to Credit Risk per Assets Class

RSD 000

Exposure to Credit Risk	31.12.2013		31.12.2012	
	Exposure	Average value	Exposure	Average value
States and central banks	118.806.101	98.752.706	90.379.310	88.726.008
Territorial autonomies and local government units	3.473.946	2.713.668	3.017.171	2.333.530
International development banks	96.763	78.983	75.876	70.093
Banks	27.644.140	21.556.549	21.160.503	18.512.754
Companies	112.547.210	111.989.704	124.265.564	111.710.952
Private individuals	37.030.308	34.942.425	35.503.989	33.898.484
Exposures secured by mortgages on real property	37.570.881	31.827.117	32.580.198	28.955.235
Due outstanding receivables	19.769.009	12.686.325	13.639.305	9.144.983
Other exposures	44.582.892	37.269.928	41.015.992	33.613.447
Total	401.521.251	351.817.406	361.637.909	326.965.483

**Note: gross exposure reduced by allowances and provisions for estimated losses and adjusted for conversion factors for off-balance sheet items.*

Sector Exposure Distribution per Classes of Assets

RSD 000

Exposure to Credit Risk	31.12.2013	31.12.2012
	Value of exposure	Value of exposure
States and central banks	126.820.745	96.527.717
Finance and insurance sector	57.174.064	45.979.643
Public sector	69.642.060	50.548.000
Foreign entities sector	4.622	74
Territorial autonomies and local government units	3.433.977	2.997.479
Public sector	2.953.751	2.562.268
Foreign entities sector	480.225	435.211
International development banks	96.763	75.876
Finance and insurance sector	96.763	75.876
Banks	27.614.445	21.395.939
Finance and insurance sector	6.289.595	1.688.993
Foreign entities sector	21.324.849	19.706.912
Banks-other	1	34
Companies	97.084.641	112.582.149
Finance and insurance sector	6.283.277	4.668.677
Public companies sector	3.569.948	3.496.221
Company sector	84.857.755	101.756.440
Entrepreneurs sector	607.544	664.321
Public sector	841.171	923.915
Foreign entities sector	234.105	681.512
Other clients' sector	120.863	77.328
Household corporate firms with employees and farms	569.978	234.097
Other	-	79.638
Private individuals	35.915.700	34.429.140
Finance and insurance sector	666	522
Public companies sector	22.435	9
Company sector	5.819.652	5.568.841
Entrepreneurs sector	1.349.342	1.285.595
Public sector	10.262	8.767
Retail sector	25.003.195	24.722.371
Foreign entities sector	35.511	124
Household corporate firms with employees and farms	3.583.751	2.780.947
Other clients' sector	90.865	60.477
Other	20	1.487
Exposures secured by mortgages on real property	37.068.714	32.134.839
Finance and insurance sector	-	-
Company sector	4.146.089	4.027.961
Entrepreneurs sector	241.031	250.357
Retail sector	32.299.344	27.477.127
Foreign entities sector	5.165	3.079
Household corporate firms with employees and farms	339.816	344.966
Other clients' sector	37.267	31.349

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Due outstanding receivables	6.626.240	4.966.747
Finance and insurance sector	508	–
Public companies sector	116.596	217
Company sector	5.966.850	4.359.397
Entrepreneurs sector	17.593	8.373
Public sector	57.368	54.095
Retail sector	383.029	384.082
Foreign entities sector	28	66.018
Household corporate firms with employees and farms	48.358	63.383
Other clients' sector	35.910	31.182
Other exposures	43.217.370	40.030.199
Finance and insurance sector	2.387.737	2.665.926
Public companies sector	157.604	2.004
Company sector	337.321	656.045
Entrepreneurs sector	2.673	4.091
Public sector	4.189	41.463
Foreign entities sector	259.135	337.962
Other clients' sector	54.078	61.829
Other	40.014.634	36.260.879
Total	377.878.593	345.140.085

**Note: gross exposure reduced by allowances, provisions for estimated losses and required reserves and adjusted for conversion factors for off-balance sheet items upon application of mitigation techniques*

Gross exposure where allowances and provisioning under off-balance sheet items was made

RSD 000

Exposure to credit risk	31.12.2013		31.12.2012	
	Gross exposure where allowance or provisioning was made	Allowance and provisions	Gross exposure where allowance or provisioning was made	Allowance and provisions
States and Central Banks	–	–	1.545.684	16.463
Finance and Insurance sector	–	–	1.545.684	16.463
Territorial autonomies and local government units	1.223.235	1.745	1.935.940	2.722
Finance and Insurance sector	1.223.235	1.745	1.935.940	2.722
Banks	223.386	223.223	259.124	230.687
Finance and insurance sector	807	644	21.038	2.713
Foreign entities sector	222.579	222.578	238.086	227.974
Companies	88.395.911	3.329.984	95.112.781	2.820.863
Finance and insurance sector	3.886.852	2.805	5.076.231	7.859
Public companies sector	573.201	712	3.695.648	1.054
Company sector	81.335.362	3.108.018	83.657.112	2.795.823
Entrepreneurs sector	628.110	3.386	666.954	2.550
Public sector	764.722	2.386	931.087	1.098
Foreign entities sector	444.234	210.129	384.311	9.755
Other clients' sector	187.836	2.160	385.566	2.151
Household corporate firms with employees and farms	575.593	387	234.611	11
Other	–	–	81.262	563
Private individuals	33.429.458	533.137	31.309.920	812.764
Finance and insurance sector	253	9	199	135
Public companies sector	5.865	11	256.456	109.023
Company sector	5.874.803	217.664	5.355.330	212.312
Entrepreneurs sector	1.327.345	29.515	1.262.168	26.834
Public sector r	9.856	426	7.842	159
Retail sector	22.514.483	241.201	21.558.248	412.011
Foreign entities sector	7.491	313	23	–
Household corporate firms with employees and farms	3.585.675	38.778	2.799.654	41.588
Other clients' sector	103.688	5.221	70.001	10.702
Exposures secured by mortgages on real property	38.242.707	81.080	33.384.905	36.924
Finance and insurance sector	–	–	–	–
Company sector	5.030.437	32.289	5.284.848	17.353
Entrepreneurs sector	232.250	1.375	250.606	2.665
Retail sector	32.590.319	45.262	27.460.525	16.458
Foreign entities sector	5.165	–	3.079	–
Household corporate firms with employees and farms	346.886	1.922	354.231	276
Other clients' sector	37.650	232	31.616	172

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Due outstanding receivables	37.411.823	18.205.538	27.752.757	14.540.144
Finance and insurance sector	142.972	142.972	142.959	142.959
Public companies sector	166.580	2.073	1.897	1.760
Company sector	29.054.527	11.836.694	17.835.285	8.546.951
Entrepreneurs sector	318.032	247.266	292.372	239.449
Public sector	491.564	319.749	87.395	31.590
Retail sector	2.568.497	1.860.987	2.470.645	1.775.807
Foreign entities sector	262.216	161.985	2.482.308	167.384
Household corporate firms with employees and farms	409.811	293.162	360.747	244.797
Other clients' sector	3.997.624	3.340.651	4.079.149	3.389.447
Other exposures	16.179.071	4.948.736	16.982.832	4.329.750
Finance and insurance sector	6.977	67	2.646.141	261
Public companies sector	3	1	3	1
Company sector	453.124	7.983	558.688	11.423
Entrepreneurs sector	1.648	41	3.887	56
Public sector	1.263	1	2.175	-
Foreign entities sector	-	-	328.566	33
Other clients' sector	61.871	1.847	60.654	3.663
Other	15.654.186	4.938.796	13.382.718	4.314.313
Total	215.105.590	27.323.442	208.283.943	22.790.317

*Note: presented is the gross exposure of items where allowance and provisions for off-balance sheet items was made

Geographic exposure according to materially significant areas, per classes of assets

RSD 000

Exposure to credit risk	31.12.2013	31.12.2012
	Exposure value	Exposure value
States and central banks	126.820.745	96.527.717
Republic of Serbia	122.391.312	92.233.004
Bosnia and Herzegovina	3.744.542	3.722.066
Other	684.891	572.647
Territorial autonomies and local government units	3.433.977	2.997.479
Republic of Serbia	1.716.016	1.616.456
Other	1.717.961	1.381.023
International development banks	96.763	75.876
Other	96.763	75.876
Exposures to Banks	21.395.940	16.567.823
Republic of Serbia	2.148.427	1.965.195
Germany	11.250.168	10.967.933
Switzerland	3.813.877	1.493.147
United States of America	1.266.501	786.203
Great Britain	2.152.347	619.211
Other	764.620	736.134
Companies	97.084.641	112.582.149
Republic of Serbia	87.714.493	100.710.857
Bosnia and Herzegovina	5.251.635	6.835.071
Montenegro	4.103.812	4.678.811
Other	14.701	357.411
Private individuals	35.915.700	34.429.140
Republic of Serbia	33.759.786	31.466.270
Bosnia and Herzegovina	1.288.017	1.200.327
Montenegro	856.802	1.745.418
Other	11.095	17.125
Exposures secured by mortgages on real property	37.068.714	32.134.838
Republic of Serbia	33.822.829	30.684.415
Bosnia and Herzegovina	2.062.121	1.145.831
Montenegro	1.180.887	-
Other	2.876	304.593
Due outstanding receivables	6.626.240	4.966.747
Republic of Serbia	5.366.907	3.959.805
Other	1.259.333	1.006.942
Other exposures	43.217.370	40.030.198
Republic of Serbia	40.903.691	38.448.600
Other	2.313.679	1.581.598
Total	377.878.593	345.140.085

*Note: gross exposure reduced by allowance, provisions for estimated losses and required reserves and adjusted for conversion factors for off-balance sheet items upon application of mitigation techniques

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Maturity distribution of all exposures per classes of assets

RSD 000

Exposure to credit risk	31.12.2013.	31.12.2012.
	Exposure value	Exposure value
States and central banks	126.820.745	96.527.717
Up to three months	63.988.005	66.617.185
From three months to 6 months	13.111.554	5.669.181
From 6 months to 1 year	6.752.318	2.971.600
Over 1 year	42.968.868	21.269.751
Territorial autonomies and local government units	3.433.977	2.997.479
Up to three months	480.226	493.830
From three months to 6 months	11.526	33.380
From 6 months to 1 year	192.559	9.571
Over 1 year	2.749.666	2.460.698
International development banks	96.763	75.876
Up to three months	61.158	75.876
From three months to 6 months	-	-
From 6 months to 1 year	-	-
Over 1 year	35.605	-
Banks	27.614.445	21.395.940
Up to three months	23.323.149	17.319.987
From three months to 6 months	154.135	1.059.280
From 6 months to 1 year	1.513.087	227.196
Over 1 year	2.624.073	2.789.477
Companies	97.084.641	112.582.149
Up to three months	9.669.202	13.145.181
From three months to 6 months	10.852.780	8.700.451
From 6 months to 1 year	12.602.658	18.154.110
Over 1 year	63.960.000	72.582.406
Private individuals	35.915.700	34.429.141
Up to three months	5.659.557	5.493.912
From three months to 6 months	2.283.771	2.191.871
From 6 months to 1 year	4.806.364	3.711.862
Over 1 year	23.166.008	23.031.496
Exposures secured by mortgages on real property	37.068.714	32.134.838
Up to three months	183.195	150.577
From three months to 6 months	269.115	147.076
From 6 months to 1 year	839.240	227.371
Over 1 year	35.777.164	31.609.815
Due outstanding receivables	6.626.240	4.966.747
Up to three months	887.043	624.920
From three months to 6 months	49.992	174.724
From 6 months to 1 year	438.961	137.068
Over 1 year	5.250.243	4.030.035
Other exposures	43.217.370	40.030.197
Up to three months	40.051.192	28.448.205
From three months to 6 months	70.209	120.888
From 6 months to 1 year	218.949	169.840
Over 1 year	2.877.019	11.291.263
Total	377.878.593	345.140.085

*Note: gross exposure reduced by allowances, provisions for estimated losses and required reserves and adjusted for conversion factors for off-balance sheet items upon application of mitigation techniques

Changes in allowances and provisions

RSD 000

	Loans and deposits	Interest and fee receivables	Securities	Stake in capital	Other investments	Other assets	Off-balance sheet exposure	Total
Balance as of 01.01.2013	12.941.732	1.707.170	4.671	446.954	3.200.471	313.707	521.239	19.135.944
Increase	8.781.547	872.962	38.144	-	508.977	200.946	659.140	11.061.716
Decrease	(5.700.159)	(360.688)	(38.648)	-	(567.512)	(391.369)	(644.042)	(7.702.418)
Exchange differentials	57.281	6.228	444	-	7.512	2.297	51	73.812
Write-offs	(10.689)	(10.304)	-	-	(736)	(2.055)	-	(23.784)
Other changes	2.803	(15.748)	-	-	(2.818)	545.105	(49.399)	479.943
Balance 31.12.2013	16.072.515	2.199.620	4.611	446.954	3.145.894	668.631	486.989	23.025.214

Note: Allowances for fixed assets, intangible investments and inventories are not included in the allowance and provisions changes

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Exposure according to risk categories and client type as of 31.12.2013

RSD 000

Risk Category	Corporate clients	Banks	Retail clients	Total
1	25.488.311	22.188.437	62.558.284	110.235.032
2	62.960.823	4.249.177	11.257.899	78.467.899
3	38.860.331	34.076	1.853.532	40.747.939
4	8.230.229	1.208	1.173.534	9.404.971
5	32.082.883	1.626.224	6.184.174	39.893.281
Total	167.622.577	28.099.122	83.027.423	278.749.122

*Note: total exposure to credit risk by risk category and client type is shown in gross amount before mitigation effect based on the amount of impairment.

Use of credit ratings

- During 2013 for the class of exposure to countries and central banks, the Bank used credit ratings of the external credit rating agency Moody's.
- For exposures in the form of financial instruments from the banking book, the Bank does not use the credit ratings of the issuers nor their specific issues due to their non-existence. For financial instruments issued by the Republic of Serbia, the Bank applies the preferential risk weight, or 0%.

Credit rating assignment to credit risk levels

Moody's CREDIT RATING	Aaa – Aa3	A1- A3	Baa1 – Baa3	Ba1 – Ba3	B1 – B3	Caa1 – D
The level of credit quality	1	2	3	4	5	6
Credit risk weight	0%	20%	50%	100%	100%	150%

Overview of classes of exposure to states and central banks per credit quality level and risk weight RSD 000

Categories of lowest export insurance premiums	Credit risk weight	Exposure amount before application of credit protection instruments		Exposure amount after application of credit protection instruments	
		31.12.2013.	31.12.2012.	31.12.2013.	31.12.2012.
States and central banks		118.767.976	90.350.238	126.820.745	96.527.717
1	0%	114.338.543	86.055.599	122.391.312	92.233.078
5	100%	4.429.433	572.573	4.429.433	572.573
6	150%	-	3.722.066	-	3.722.066

Credit Risk Mitigation Techniques

Valuation of credit protection instruments and their managing

- The Group has regulated by its internal documents the valuation of credit protection instruments and their managing.
- The types of security for the receivables and instruments on that basis are in each concrete case determined by the special provision of the Agreement between the Group member and the applicant, and their procuring after the conclusion of the agreement and prior to realization of the loan.
- The Group members regularly assess/value the collaterals, prior to the conclusion of the loan agreement and during the agreement validity.
- The acceptable loan amount and collateral value ratio is determined based on the assessed collateral value, which is adjusted by application of defined percentage depending on type of collateral, thereby establishing the liquidation value of the collateral that the Group member can collect.

Description of basic types of credit protection instruments

- The Group uses the following credit protection instruments:
 - material credit protection;
 - non-material credit protection;
- Among the instruments of material credit protection, the Group uses the financial instruments by applying the complex method in accordance with the regulations of the National Bank of Serbia. As to financial instruments, the Group uses as eligible instruments of protection:
 - cash and cash equivalents deposited with the Group members, such as the deposits placed as collateral;
 - Securities, which include debt securities issued by the states and central banks, and shares.

- As a form of non-material credit protection, the Group uses guarantees, other forms of sureties, counter-guarantees, etc.

Basic types of credit protection providers

- In the case of using the guarantees as the credit protection instruments, the Group uses the guarantees issued by:
 - states,
 - banks,
 - territorial autonomies,
 - other
- Guarantees as credit protection instruments are taken only if the guarantor's risk weight is more favorable than the counterparty's risk weight.

Data about market or credit risk concentration within the applicable mitigation techniques

- The Group follows up and manages the credit and market risk concentration in the segment of large exposures by also considering the issuers of eligible security instruments. Also, the Group reports to the management semiannually about large exposures on consolidated basis.
- In order to manage the concentration risk in the framework of used credit risk mitigation techniques:
 - Analysis is made of indirect exposure to the credit protection provider, within the credit process and
 - of the established exposure limit system.
- The major part of eligible non-material credit protection instruments accounts for the guarantees of the Government of the Republic of Serbia

Exposures secured by credit protection instruments per classes of assets

RSD 000

Exposure to credit risk	Amount of exposures secured by material credit protection instruments		Amount of exposures secured by non-material credit protection instruments	
	31.12.2013	31.12.2012	31.12.2013	31.12.2012
States and central banks	-	-	-	-
Territorial autonomies and local government units	-	-	-	-
International development banks	-	-	-	-
Banks	-	-	-	-
Companies	896.369	1.518.859	8.066.889	6.430.734
Private individuals	749.858	840.556	-	-
Exposures secured by mortgages on real property	24.707	62.590	-	-
Due outstanding receivables	-	164.963	-	-
Other exposures	24.907	58.464	-	-
Total	1.695.842	2.645.432	8.066.889	6.431.673

*Note: exposure presented after application of the conversion factor and volatility factor

5.2. Counterparty Risk

Counterparty Risk

- The Group performs transactions in the trading book and banking book which fall under the counterparty risk, and in part of operations with:
 - Financial derivatives;
 - Repo and reverse repo transactions.
- The Banking Group members do not perform transactions that are subject to counterparty risk.
- For the needs of calculating the exposure of the positions that are subject to calculation of the capital requirements for the counterparty risk, the Group uses:
 - the current exposure method for financial derivatives;
 - the complex method for calculation of adjusted transaction and collateral value in the case of repo and reverse repo transactions, and for the lending and borrowing transactions. A characteristic of „repo“ transactions performed by the Group with the National Bank of Serbia is that the collateral cannot be used as an eligible credit protection instrument since the collateral issuer and the counterparty is one and the same.

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Exposure to counterparty risk

RSD 000

Type of risk	Exposure value
Exposures to counterparty risk	12.246.700

5.3. Liquidity Risk

- The Group may be exposed to the risk of inability to settle matured obligations (default risk), as well as to possible occurrence of a liquidity crisis on the basis of external and internal factors. Internal factors relate to the structure of the Group's liabilities in terms of the structure and concentration of deposit potential and share of adequate sources of funding in the liabilities (funding sources risk), while external factors relate to exposure to non-marketability of assets in case of need to acquire the sources of funding.
- The Group manages the liquidity risk on daily basis by monitoring/following up and controlling its assets and due liabilities, by controlling the positions in all major currencies in order to timely perceive the needs for additional sources of financing, and/or in long-term the Group members plan the structure of their sources and loans so as to provide the enough stable sources and sufficient liquidity reserves.
- The parent Bank measures the exposure to the liquidity risk of the Group by analyzing the Group's exposure relative to the defined limits.
- The Group members test the individual Liquidity Management Plans in crisis situations which enables to identify a possible crisis, they test the survival period and solvency of the members in presumed crisis conditions, and also analyze the accessibility of the sources for covering potential obligations and/or assess the accompanying organizational support (public relations and the Plan for the case of occurrence of unforeseen events).
- The Group has developed an internal approach for the needs of determining the capital required for covering the liquidity risk.

5.4. Managing Interest Rate Risk in the Banking Book

- The Group is exposed to:
 - The risk of change in prices (repricing risk), which arises from the mismatch of assets and liabilities items relative to the remaining maturity (for positions with fixed interest rate) and re-pricing (for positions with variable interest rate);
 - Yield curve risk
 - Basis risk due to changes of different reference interest rates in case of interest rate sensitive positions with similar characteristics in terms of maturity or re-pricing,
 - Options risk, to which it may be exposed due to contractual provisions in connection with interest rate sensitive positions, as well as built-in minimum and maximum interest rates options.
- The Group measures semiannually, as a minimum, the exposure to interest rate risk by GAP and ratio analysis, interest rate shock and duration, stress tests and simulations, while GAP, ratio analysis, duration and interest rate shock are performed monthly at the level of Group members.
- For the needs of preparation of interest rate GAP, the mentioned positions are categorized in the following manner:
 - positions with contracted fixed interest rate are categorized according to maturity period,
 - positions with agreed market variable interest rate are categorized according to the repricing period provided such period is shorter than the maturity period,
 - positions with agreed variable interest rate in accordance with the business policy are categorized according to maturity period, assets and liabilities not having a defined maturity or having the maturities other than the agreed ones are categorized in relevant time frames based on the analysis of such positions in the previous period (assessment and prior experience).
- The Group regularly performs the stress testing of the interest rate risk by which it assesses the impact of the change in the key factors on the Group's interest rate risk. In modeling the scenarios, apart from the changes in interest rates, the impact of early withdrawal of deposits and prepayments of loans are particularly taken into consideration, which are assessed by the bank on the basis of historical trends and expert assessment. The parent Bank performed the assessment of the movement of transaction deposits and demand deposits by applying the relevant statistical models in the field of time series analysis, which is applied at the Group level.
- The Group has limited to 20% the impact on the economic value of capital and has internally developed a model for calculation of capital requirements for the interest rate risk.

5.5. Market Risks

- The Group is exposed to the risk of changes in the exchange rate of inter-currency pairs on the positions of the banking book and trading book (foreign exchange risk) as well as to the change in the price of equity and debt securities that are recorded in the trading book (price risk).
- Internal factors of exposure to foreign exchange risk originate from currency structure of loans and deposits: loans are primarily agreed in RSD with currency clause (EUR and CHF), and/or in BAM with currency clause. In 2013 the exposure to foreign exchange risk remained within the internally and externally defined limits
- The Group is insignificantly exposed to the price risk, which is also demonstrated by the share of the trading book in total operations of the Group, which is below 1%, and which is exclusively the exposure of the parent Bank. In the structure of price risk exposure the dominant is the share of bonds available for trading, while insignificant is the share of equity instruments. The Group members do not take up positions in the trading book. The Group has developed the customized internal approach for the purpose of establishing the required internal capital for risk coverage, for whose application it has not requested the permission of the National Bank of Serbia. The Group calculates the minimum capital requirements for these risks by using the standardized approach.

5.6. Exposures Arising from Equity Investments in the Banking Book

- Equity investments in the companies founded by the parent Bank in order to expand the offer of financial products and services have taken place for economic reasons or local regulations that impose that the offer of certain financial products and services must be made through companies exclusively founded for that purpose. This is the reason why the Bank has founded Komercijalna banka AD Budva, Komercijalna banka AD Banja Luka, as well as the Investment Fund Management Company (Kombank INVEST AD Beograd).
- In addition to majority stakes in subsidiaries, the parent Bank and the member from Budva also hold minority equity investments in companies, which enable them to perform certain types of financial services.
- Equity stakes are initially assessed at purchase price and at the balance sheet date at market value, if the same is known. The changes in market value are stated within the capital, credited or charged to revaluation reserves until the disposal of such financial assets when the revaluation reserves are transferred to income or expenses.
- In case when equity stakes record a fall in fair value, with the objective evidence of impairment of assets (long and continuous decline in value over a period longer than twelve months, as well as decline in value above 30% of assets purchase price), accumulated loss is recognized as an impairment charge, although the recognition of a financial asset has not stopped, (IAS 39).
- As to the investments in capital, intention is to hold them for an indefinite time period. These investments may be sold depending on liquidity needs or in the case of change in market prices. Investments in capital for which there is no active market are valued at purchase price.

Exposure per investment purpose as of 31.12.2013

RSD 000

Equity investments in banking book	Carrying value	Allowances	Fair value	Realized gain/loss	Unrealized gain	Unrealized loss
Banks and financial organizations	135.667	25.266	110.401	-	-	(1.545)
Companies and other legal entities	457.178	421.688	35.490	-	6.511	-
Foreign entities abroad	427.397		427.397	-	427.331	-
Total	1.020.242	446.954	573.288	-	433.842	(1.545)

Exposure value as of 31.12.2013

RSD 000

Exposure type	Carrying value	Fair value
Holdings and investments in capital		
quoted on stock exchange	569.135	492.352
not quoted on stock exchange	451.107	80.936
Total	1.020.242	573.288

- In 2013, the Group did not achieve realized gain / loss arising from sale or from closing the positions based on equity investments.
- Total unrealized gain/loss originating from equity investments is presented in the table, while the amount of unrealized gains which is included in calculation of supplementary capital is reduced by 10%. Unrealized losses are not reduced when included in supplementary capital.

5.7. Consolidated Financial Statements and Group Operations

- Financial statements of all the members of the Banking Group are consolidated by full consolidation method in accordance with relevant IAS/IFRS.
- The Group does not have related entities to whose financial statements the method of proportional consolidation and equity method would be applied or which would be excluded from consolidation because of Group member's participation that represents a deductible item from the Group capital.

5.7.1. Overview of Differences between Consolidated Financial Statements

		Consolidation for supervision		Consolidation pursuant to IFRS	
Company type	Company name	Consolidation method		Consolidation method	
		Full	Equity method	Full	Equity method
Bank	Komercijalna banka AD Beograd	X		X	
	Komercijalna banka AD Budva	X		X	
	Komercijalna banka AD Banja Luka	X		X	
Investment Fund Management Company	KomBank INVEST AD Beograd		X	X	

Consolidation for supervision		Consolidation according IFRS		Difference
Description of balance sheet position	Amount in RSD 000	Amount in RSD 000	Amount in RSD 000	Amount in RSD 000
Assets	385.270.976	385.261.548		9.428
Liabilities	318.231.136	318.219.852		11.284
Capital	67.039.840	67.041.696		(1.856)
Off-balance sheet items	227.797.699	227.797.499		200
Profit before tax	4.399.218	4.400.642		(1.424)
Income tax	(60.863)	(61.296)		433
Profit after tax	4.460.081	4.461.938		(1.857)

5.7.2. Legal or Other Impediments for the Transfer of Capital

- There were no legal or other impediments in the previous period for a timely transfer of capital and settlement of obligations between the parent bank and subsidiary companies within the Banking Group business operations.
- In the forthcoming period, the parent bank does not expect any difficulties in the cash flows between the Banking Group members or any legal and other impediments in business operations.