NATIONAL BANK OF THE REPUBLIC OF MACEDONIA

Pursuant to Article 64 paragraph 1 item 22 of the Law on the National Bank of the Republic of Macedonia ("Official Gazette of the Republic of Macedonia" no. 3/02, 51/03, 85/03, 40/04, 61/05 and 129/06) and Article 68 paragraph 1 and Article 69 paragraph 2 of the Banking Law ("Official Gazette of the Republic of Macedonia" no. 67/2007), the National Bank of the Republic of Macedonia Council adopted the following

DECISION
on credit risk management
("Official Gazette of the Republic of Macedonia" no. 17/2008)

I. GENERAL PROVISIONS

1. This Decision sets forth the credit risk management methodology, including criteria on classification of on-balance sheet and off-balance sheet assets items of a bank according to the risk degree, the method of determining and the amount of impairment and special reserve, and the scope and the contents of credit risk management system.

2. The bank shall establish a credit risk identification, measurement, monitoring and control system.

Credit risk, in light of this Decision, shall denote a risk of loss for the bank due to the incapability of its client to settle its liabilities within the agreed amount and/or periods.

3. Client, for the purposes of this Decision, shall be a person/entity and persons/entities connected thereto, which is:

- user of credit or other type of credit risk exposure approved by the bank,
- issuer of financial instrument underlying the credit risk exposure of the bank.

II. CREDIT RISK EXPOSURE CLASSIFICATION

4. The bank shall classify each on-balance sheet and off-balance sheet asset item according to the credit risk degree it has been exposed to as a result of such item (hereinafter referred to as: credit risk exposure), in a manner and according to criteria specified by this Decision.

5. Credit risk exposure, subject to classification by the bank, shall include:

a) on-balance sheet asset claims based on due and undue credits, non-performing credits, deposits with banks and other financial institutions, claims on the Republic of Macedonia and the National Bank of the Republic of Macedonia (hereinafter referred to as: National Bank), purchased claims (factoring and forfeiting), financial lease, claims on guarantee-backed payments, L/Cs, backing guarantees and other on-balance sheet claims arising from the bank's off-balance sheet exposure, interest receivables, non-performing interest, fee and comission receivables, investments in securities and other financial instruments held to maturity, investments in securities and other financial instruments available for sale, other due claims, other non-performing claims and other claims that expose the bank to credit risk,

b) off-balance sheet asset items based on: unused irrevocable lines of credits, unused irrevocable credits based on overdrafts on current accounts, credit cards and other potential credit risk exposure, unsettled assumed irrevocable liabilities on financial lease, unsettled assumed irrevocable liabilities for claim purchase (factoring and forfeiting), issued non-backed guarantees, opened non-backed L/Cs, backing guarantees, bank acceptances, non-backed performance guarantees and other types of off-balance sheet items, which are contingent liability for the bank.

6. For the purposes of this Decision, the on-balance sheet asset items below shall not be subject to classification by the degree of credit risk:

- cash, bank's accounts with the National Bank, intangible assets, real estate and equipment, natural heritage, working assets and stocks,
- items that expose the bank to market and/or other risk, different from the credit risk - investments in securities and other financial instruments held for trading, investments in securities and other financial instruments measured at fair value through profit and loss, investments in subsidiaries, affiliates and joint ventures, and credits and claims measured at fair value through profit and loss.

7. When classifying the credit risk exposure, the bank shall take into account:

- the client's creditworthiness,
- the regularity of liabilities settlement by the client, and
- the collateral quality.

The creditworthiness of a client shall be evaluated at least according to the following:

- the client's character, i.e. its status and economic distinctions, quality and professionalism of the management and executive bodies of the client, the quality of program/project for which the client requested financial assistance from the bank,

- the client's capital and property power, including its capability to generate future cash inflows for liabilities settlement,

- client's liquidity and profitability,

- the perspective of the client and its business,

- the total credit risk exposure of the banking system of the Republic of Macedonia to the client (source of data: Credit Registry of the National Bank), and

- client's exposure to currency and other risks.

The following shall be taken into account when determining the regularity of liability settlement by the client:

- the client's credit history, by checking the capability to service its liabilities to the bank or other banks (provided that the client previously used credits or other types of credit risk exposure in the bank or other banks),

- evaluation of the likelihood whether the usage of the funds according to the agreed purpose of the credit or other type of credit risk exposure would cause cash inflow for the client in volume and dynamics suitable to the agreed method of liability repayment.

The following shall be taken into account when determining the collateral quality:

- possibility to sell the collateral,

- whether the collateral is supported by documents and the possibility to be monitored by the bank;

- possibility for forced collection of the collateral.

8. General indicators used in the determining of loss from damage based on credit risk:

- information on the financial problems of the client,

- information on breach of the contract, including default on due liabilities,

- the bank approves considerable relieves to the client for its financial problems, the bank would otherwise not offer to other clients,

- certainty that the client would go into bankruptcy or other type of financial reorganization,

- vanish of active market for specific claim or financial instrument, due to the financial problems of the client, or

- data indicating a decrease in the estimated future cash flows for a group of credit risk exposures, compared to their initial recognition, although the decrease cannot be related to individual credit risk exposure, including:

    a. negative changes in the client's repayment capabilities (e.g. more late payments or more clients - credit card users who reached their maximum permitted limit - overdraft, and who pay minimum monthly amount), or

    b. deterioration of the national or economic conditions that affect the liabilities repayment by the clients (e.g. higher unemployment rate in the geographic area of the client, lower prices of property that serves as collateral, lower prices of manufactured products i.e. service provided by the clients, etc.).

9. The bank shall classify the credit risk exposure:

- on individual basis, for any exposure that according to item 10 of this Decision is considered as individually important item, by applying the provisions of section III of this Decision,

- on group basis, for retail credit portfolio, according to section IV of this Decision, or

- on group basis, for a group of similar financial instruments, as specified by section IV of this Decision.

10. As an individually important item shall be considered the total exposure to a client:

a) exceeding Denar 300,000, or
b) exceeding 0.007% of the total credit risk exposure of the bank.

11. As an exception to items 9 and 10 of this Decision, the bank shall classify the credit risk exposure to banks and equity investments which are credit risk exposure only on individual basis, in consistence with section III of this Decision.

III. EXPOSURE CLASSIFICATION AND DETERMINATION OF THE IMPAIRMENT AND THE SPECIAL RESERVE ON INDIVIDUAL BASIS

III. 1. Classification of the credit risk exposure on individual basis

12. The bank shall classify the credit risk exposure in the following risk categories:

a) Risk category A shall include:

- claims on the National Bank, the Republic of Macedonia, the European Central Bank and governments and central banks of EU member-states, Switzerland, Canada, Japan, Australia, Norway and the USA,

- credit risk exposure to clients whose current financial standing and the estimated future cash inflows do not put at stake its further business and the possibility to settle the current and future liabilities to the bank,

- credit risk exposure to a client which settles its liabilities within the maturity period or with a delay of not more than 30 days and for which the bank did not make any claim restructuring over the last two years,

- credit risk exposure fully collateralized by first-class collateral instruments specified under item 19 of this Decision.

b) Risk category B shall include:

- credit risk exposure to a client whose cash inflows are considered by the bank, on the basis of creditworthiness assessment, to be sufficient for full settlement of the due liabilities, irrespective of the current financial weaknesses, and that there are no signs for further deterioration of the client's condition,

- credit risk exposure to a client which most often settles its liabilities with a delay of 31 to 60 days, or with an exception from 61 to 90 days, if the delay is only occasional within the interval form 61 to 90 days, and for which the bank did not make any claim restructuring within the last six months.

c) Risk category C shall include:

- credit risk exposure to a client whose cash flows are considered inadequate for regular settlement of the due liabilities,

- credit risk exposure to an inadequately capitalized client,

- credit risk exposure to a client with inadequate maturity structure of the assets and the liabilities,

- credit risk exposure to a client for whom the bank does not have an access to all required and updated information necessary to assess the creditworthiness of the client,

- credit risk exposure to a client whose liabilities have been restructured,

- credit risk exposure to a client who most often settles its liabilities with a delay of 61 to 120 days, or with an exception from 121 to 180 days, if the delay is only occasionally within the interval of 121 to 180 days.

d) Risk category D shall include:

- credit risk exposure to an illiquid client,

- credit risk exposure to a client whose creditors written off their claims thereon,

- credit risk exposure to a client under bankruptcy, from which the bank expects to collect its claims partially,

- credit risk exposure to a client under liquidation procedure,

- credit risk exposure, the collection of which depend on the foreclosure of the collateral instruments,

- credit risk exposure where there are expectations that the bank would collect only a portion of its claims on the client,

- credit risk exposure to a client who most often settles its liabilities with a delay of 121 to 270 days, or with an exception with occasional delay of over 270 days.

e) Risk category E shall include:

- credit risk exposure to a client who settles its liabilities with a delay of over 270 days or is in default,
- credit risk exposure to a client under bankruptcy, not collateralized by a high quality collateral instrument,
- credit risk exposure subject to lawsuit,
- credit risk exposure where there are firm expectations that the bank will not be able to collect fully its claims on the client or that it will collect only an insignificant portion.

13. The claim classified in D and E risk category or claim, which on any basis (principal, interest, other non-interest bearing income) has not been collected for more than 90 days after the maturity date, the bank shall record (reenter) on a special account for non-performing claims - credits, interest, other claims (in the bank's Chart of Accounts: suspicious and contested claims).

Once the accrued interest becomes non-performing, the bank shall make full impairment of the accrued interest.

The claim may be excluded from the category of non-performing claims only if the portion of the claim that fell due has been collected and if the requirements for its upgrading have been met.

III. 2. Determination of impairment and of special reserve on an individual basis

14. Once the credit risk exposure is classified on individual basis, the bank shall assess the need and shall accordingly make impairment of the on-balance sheet asset claims, i.e. shall allocate special reserves for the off-balance sheet asset claims by evaluating the present value of the future cash flows that would occur on the basis of such claims.

15. The amount of impairment of the on-balance sheet asset claims on individual basis shall be the difference between the carrying value of the on-balance sheet claims and their present value (estimated compensable amount). The present value of on-balance sheet asset claims shall be derived by discounting the expected future cash flows based on such claims by applying effective interest rate specified by the contract.

The effective interest rate shall be an interest rate the application of which would make the present value of all future cash inflows equal to the present value of all future cash outflows. When calculating the effective interest rate, the bank shall:

a) take into account all future cash flows (inflows and outflows) expected to occur under the contractual terms,

b) take into account all paid and/or unpaid fees and commisions which are an integral part of the effective interest rate on the claim,

c) not take into account the fees and commisions for depositing cash as claim collateral;

d) not take into account the future losses arising from the credit risk of the claim.

The effective annual interest rate shall be used for discounting the future cash flows.

If, due to financial problems of the client, the bank approves a modification of the lending terms, with regard to the interest and the repayment periods, the expected future cash flows shall be discounted at the effective interest rate applicable prior to the modification of the lending terms.

The bank shall apply the effective interest rate for discounting the expected future cash flows from claims with floating interest rates, as specified by the contract, applicable on the date of determining the present value of the expected cash flows. In such cases, the effective interest rate shall be calculated over the validity period of the agreement (not only the remaining period to maturity), by applying the interest rate applicable on the date of determining the present value of the expected cash flows.

As an exception to paragraph 5 of this item, if the interest rate on the date of determining the present value changes by less than 10% relative to the last interest rate used for discounting the future cash flows, the bank may apply the previous effective interest rate used in the determining of the present value of the expected future cash flows.

16. The amount of special reserve for the off-balance sheet asset items on individual basis shall be equal to the present value of the expected future cash flows from bank's payments on the assumed contingent liabilities and from collections from the client, discounted by the current market price of risk-free securities issued in the same currency and same maturity date as the currency and the maturity date of the expected payment or collection.

If there is no present market value of risk-free securities with same maturity date as the maturity date of the expected payment, the present value of the expected payment on the assumed contingent liability of the bank shall be determined at the current market value of the risk-free security with the maturity date which is closest to the maturity date of the expected payment.

17. The bank shall not discount the expected future cash flows of credit risk exposure with residual maturity date shorter than one year from the date of determining the amount of credt risk loss. In this case, the amount of loss is equal to the difference between the accounting value of the credit risk exposure and the amount of expected future payments and collections based on such exposure.

18. When determining the present value of the expected future cash flows, the bank shall also take into account the value of collateral on such claim, provided that:

a) the collateral is a first-class collateral instrument, under item 19 of this Decision,

b) the collateral is unconditional irrevocable guarantee from non-banking financial and non-financial institution with at least A- rating (according to the Standard & Poor's rating), A3 (according to the Moody's rating) or respective rating given by other recognized international credit rating agency,

c) the asset serving as collateral is adequate asset for claim collection. An asset serving as collateral shall be considered adequate for collection if:

   - there is a functional market for such asset or similar assets,

   - there is an information of purchase and sale transaction of same or similar assets over the last three months,

   - the information on the negotiated purchase and sale prices of same or similar assets are publicly available,

   - the collection of the potential sale of the asset used as collateral (in the case of foreclosure of the asset for collection of overdue claims) is expected to be made within a period not longer than 12 months after the foreclosure,

   In the case of real estate used as collateral for the claim, besides the requirements referred to in paragraph 1 of this sub-item, the bank shall keep regular documentation for the pledged real estate, including:

   - notary act with enclosures regarding the established mortgage on real estate, including execution clause,

   - assessment of the market value of the real estate, less the expected sale costs payable by the bank, at the moment of establishing the mortgage,

   - property certificate or other evidence issued by a competent institution for establishing mortgage on the real estate,

   - insurance real estate policy restrictively endorsed for the benefit of the bank,

   - to have a first priority to the foreclosure of the pledged real estate before the other pledgees,

   - to have the right of regular control and physical examination of the pledged property,

   - evaluation of the market value of the real estate, less the expected sale costs payable by the bank, which the bank is required to conduct at least once a year. The bank shall evaluate the market value of the real estate in a shorter period, in the case of considerable drop in the market prices of a similar property or if the collateral value exceeds 5% of the bank's own funds,

- the market value of the real estate referred to in indents 2 and 7 of this paragraph has been appraised by a certified appraiser.

In the case of pledging a movable, securities, claims and other rights (hereinafter: movable collateral) as claim collateral, the bank, beyond the requirements referred to in paragraph 1 of this sub-item, shall have:

- a regular documentation on movable collateral, in consistence with the Law on Contractual Collateral,

- evaluation of the market value of the movable, less the expected sale costs made at the moment of establishing the collateral,

- an evidence on registration in collateral registry,

- a first priority in the foreclosure of the movable collateral before the other pledgees,

- an insurance policy on the pledged movable, restrictively endorsed for the benefit of the bank,

- a right of regular control and physical examination of the movable collateral,

- reevaluation of the movable market value, less the expected sale costs payable by the bank, made at least once every twelve months. Evaluation of the movable market value shall be required for a shorter period, in the case of considerable drop in the market prices of such or similar property or if the collateral value exceeds 5% of the bank's own funds,

- the market value of the movable referred to in indents 2 and 7 of this paragraph appraised by a certified appraiser.

19. First class collateral instruments, for the purpose of this Decision shall include:

a) cash deposit or cash in the depot, with the following requirements being fulfilled:

- the maturity date of the cash deposit is equal or longer than the maturity date indicated in the credit risk exposure agreement, i.e. the cash in the depot may be withdrawn only if the credit risk exposure of the bank is fully settled,

- there is a written document confirming the purpose of the deposit, i.e. the cash in the depot, as collateral for credit risk exposure,

- in the case of collateral foreclosure, the bank shall be the only beneficiary of the deposit, i.e. the cash in the depot,

- the collateral to be foreclosed when the client is in default on the obligations arising from the credit risk exposure agreement.

b) Securities of the Republic of Macedonia and the National Bank, the European Central Bank and governments and central banks of EU member-states, Switzerland, Canada, Japan, Australia, Norway and the USA,

c) Irrevocable guarantees or super-guarantees issued by domestic or first-class foreign banks, including the words: "on first call" or "protest-free",

d) Unconditional guarantees payable on first written call, issued by the Republic of Macedonia, governments and central banks of the EU member-states, Switzerland, Canada, Japan, Australia, Norway and the USA, and entities established by these institutions, the operations and liabilities of which are fully covered by explicit guarantee issued by these institutions.

The credit risk exposure which is fully collateralized by the instruments referred to in paragraph 1 of this item shall be classified in A risk category up until the foreclosure of the instrument, but not later than 30 days after the maturity date of the claim.

20. First-class bank, for the purposes of this Decision, shall be any bank with at least A- rating (according to the Standard & Poor's rating), A3 rating (according to the Moody's rating) or respective rating of other recognized international credit rating institution.

21. In the calculation of the present value of the expected future cash flows arising from the claim, the value of the collateralized property that meets the requirements referred to in item 18 sub-item c), shall be discounted by the time period of the expected sale of the pledged property for the purpose of claim collection, if the property is expected to be sold for a period longer than one year.

22. In the calculation of the present value of the future cash flows, the collateral shall be included up to the amount of total credit risk exposure, covered by the collateral.

23. Based on the present value of the on-balance sheet and off-balance sheet asset claims defined by this section, the bank shall make impairment, i.e. allocate special reserve within the following limits:

- from 0% to 10% of the credit risk exposure classified in A risk category,
- over 10% to 25% of the credit risk exposure classified in B risk category,
- over 25% to 50% of the credit risk exposure classified in C risk category,
- over 50% to 75% of the credit risk exposure classified in D risk category,
- over 75% to 100% of the credit risk exposure classified in E risk category.

The amount of impairment, i.e. the amount of allocated special reserve may not be below the lower limit specified under paragraph 1 of this item for each risk category.

If in the determining of the present value of each credit risk exposure classified on individual basis, the bank calculates higher amount of impairment, i.e. special reserve than the amount specified under paragraph 1 of this item for the risk category which house the respective credit risk exposure, it shall reclassify the credit risk exposure into the risk category that corresponds to the determined amount of impairment, i.e. special reserve.

24. As an exception to item 14 of this Decision, if the bank does not determine the present value of the on-balance sheet and off-balance sheet asset claims, the amount of impairment, i.e. special reserve for each credit risk exposure classified on individual basis shall be calculated by applying the upper limit specified by item 23 of this Decision, depending on the risk category which house the credit risk exposure.

The bank shall not apply the exception to paragraph 1 of this item to credit risk exposure that was subject to calculation of impairment, i.e. special reserve by determining the present value of the future cash flows.

25. The bank shall record the calculated amount of additional or released impairment for a specific claim, in the income statement on the respective account for impairment (losses due to impairment) of credits and placements and on the respective account for impairment (asset impairment) within the on-balance sheet asset claims accounts.

The bank shall record the calculated amount of additional or released special reserve, in the income statement on the special reserve account for off-balance sheet credit exposure on individual basis and on the account on the liability side for special reserve for the off-balance sheet credit exposure on individual basis.

26. The bank shall assess the likelihood of loss due to credit risk on a group basis, as defined by the provisions of section IV of this Decision, for the credit risk exposures classified on individual basis, for which, by determining their present value, it has been found that there is no loss due to credit risk and which have not been subject to impairment, i.e. no special reserve has been allocated.

As an exception to paragraph 1 of this item, the bank shall not assess the likelihood of loss from credit risk on a group basis, for the credit risk exposures for which there have been found that there is no loss due to credit risk and which are:

- claims on the Republic of Macedonia and the National Bank, the European Central Bank and governments and central banks of the EU member-states, Switzerland, Canada, Japan, Australia, Norway and the USA,

- claims collateralized by first-class instruments,

- credit risk exposure to foreign banks and domestic banks and savings houses established and operating by a license issued by the Governor of the National Bank,

- equity investments,
- off-balance sheet asset items.

IV. CLASSIFICATION OF EXPOSURE AND DETERMINING OF IMPAIRMENT ON GROUP BASIS

IV.1. Classification of exposure on a group basis

27. The bank may classify the on-balance sheet and off-balance sheet asset claims which, as specified by item 10 of this Decision, are not considered individually important items, on a group basis in the retail credit portfolio.

As an exception to paragraph 1 of this item, the non-performing claims referred to in item 13 of this Decision shall not be classified into retail credit portfolio on a group basis.

28. To classify the credit risk exposure in the retail credit portfolio, the bank shall:

- segment the retail credit portfolio into several homogeneous sub-portfolios according to a credit risk similarity of the individual credit risk exposures (e.g. same collateral, same repayment source, geographic location, etc.);
- determine default rates for each retail credit sub-portfolio.

29. The total amount of retail credit portfolio shall not exceed 33% of the bank's total credit risk exposure.

The bank shall classify a portion of retail credit portfolio that exceeds the limit referred to in paragraph 1 of this item, as defined by section III of this Decision, i.e. shall classify the credit risk exposure on individual basis.

30. The bank shall classify on a group basis a group of similar financial instruments, the exposures for which no individual impairment has been made, according to item 26 of this Decision.

The bank shall classify the exposures referred to in paragraph 1 of this item into homogenous sub-portfolios according to the credit risk similarity (e.g. type of exposure, prevalent activities and functions, geographic location, etc.).

As an exception to paragraph 1 of this item, the bank shall not classify on a group basis the exposures referred to in paragraph 1 of this item, if they cannot be classified into homogeneous sub-portfolios.

IV.2. Determining of impairment and special reserve on a group basis

31. The bank shall determine the amount of impairment and special reserve for the exposures referred to in item 27 of this Decision, by applying statistical models for determining default rates for each sub-portfolio.

When establishing sub-portfolios and applying statistical modeling:

a) the bank shall use historical data on the default rate for each sub-portfolio. The bank shall have historical data on the past period, which is equal to the average agreed maturity period of the sub-portfolio, but not shorter than three years,

b) the statistical model shall at least take into account the time value of money, the expected future cash flows from the respective sub-portfolio and the maturity structure of the exposures in the portfolio.

The bank shall, at least once a year, test the reality of the model referred to in paragraph 2 of this item, by comparing the default rates by separate sub-portfolios, registered in one-year period prior to the testing. The testing shall include a sample of at least 30% of each retail credit sub-portfolio. The methodology and the statistical models of the bank for retail credit portfolio classification shall be considered adequate if 95% of the tested cases do not show difference between the defined and achieved default rates. Otherwise, the bank shall forthwith revise the methodology and statistical models for classification and calculation of the amount of impairment and special reserve of the retail credit portfolio.

The bank's Supervisory Board and the National Bank shall be notified on the testing and the results thereof.

32. The bank shall record the calculated amount of additional or released impairment, i.e. special reserve for the retail credit portfolio exposures, in the income statement on the account for group impairment for the retail credit portfolio, i.e. on the special reserve account for off-balance sheet credit exposure on group basis and on the account on the liability side for group impairment for the retail credit portfolio i.e. on the account on the liability side for special reserve for the off-balance sheet credit exposure on group basis.

33. The bank shall determine the amount of impairment for the exposures referred to in item 30 of this Decision in consistence with item 31 paragraph 2 of this Decision.

34. The bank shall record the calculated amount of additional or released impairment referred to in item 33 of this Decision, in the income statement on the account for group impairment for individually important exposures which have not been impaired on individual basis and on the account on the liability side for group impairment for individually important exposures which have not been impaired on individual basis.

V. CREDIT RISK MANAGEMENT SYSTEM

35. The bank shall establish a credit risk management system suitable to the nature, the volume and the complexity of its financial activities.

36. The bank shall have proper organizational structure for credit risk management in place, implying clearly defined competencies and responsibilities of the supervisory and management bodies.

The bank's Supervisory Board shall:

- approve credit risk management policy and monitor its implementation,
- review the adequacy of the adopted policy at least annually,
- monitor the efficiency of the internal control, as an integral part of the credit risk management system,
- other activities stated by the Banking Law and the bank's internal acts.

The Risk Management Committee shall be responsible for:

- establishing and monitoring of the credit risk management policy and providing suggestions for its revision,
- assessment of the credit risk management systems,
- analysis of the bank's credit risk exposure reports and monitoring of the activities undertaken for credit risk management,
- setting and regular reviewing of credit risk exposure limits,
- defining potential exception to the defined limits and delegating responsibilities for making decisions on applying such exceptions,
- other activities specified by the Banking Law and the bank's internal acts.

The bank's Board of Directors shall, as specified by the Banking Law and the credit risk management policies, at least:

- establish and implement proper credit risk management procedures, in line with the policy adopted by the Supervisory Board,
- establish and maintain efficient credit risk measurement, monitoring, control and reporting system, by type of credit risk exposure,
- establish adequate system of reporting to the Supervisory Board and the Risk Management Committee on the violations, if any, of the credit risk exposure limits,
- establish procedure for assessing the effect of new products to the credit risk exposure, and monitor the contingent liabilities and exposure based on off-balance sheet activities of the bank, including counterparty risk exposure,
- other activities in line with the Banking Law and the bank's internal acts.

37. The bank shall establish and apply credit risk management policy and adequate procedures relating to at least:

a) the criteria and procedures for lending and other type of on-balance sheet or off-balance sheet (potential) exposure,

b) more detailed criteria for determining and monitoring the creditworthiness of the client the bank has been exposed to and the collateral quality and value.

   To assess the credit risk arising from the client's exposure to currency risk, the bank shall have a system in place for monitoring, analyzing and assessing:

   - the compliance of the client's foreign exchange position,

   - the adjustability of the client's cash flows to the potentially changed level of total liabilities and particularly the liabilities to the bank as a result of the potential change in the exchange rate of the Denar against foreign currencies.

   The client's foreign exchange position shall be considered complied if its expected foreign exchange inflows, foreign exchange claims and foreign exchange indexed claims in Denars cover at least 80% of its total expected foreign exchange outflows, foreign exchange liabilities and foreign exchange indexed liabilities in Denars. Clients with complied foreign exchange position shall also be considered those whose prevalent product price depends on the price of such product on the international stock exchanges.

   The bank shall establish records of clients with complied and non-complied currency position.

   As an exception, the bank shall not apply the provisions of paragraphs 2, 3 and 4 of this sub-item, to clients whose total credit risk exposure amounts to Denar 150,000 for natural persons, i.e. Denar 300,000 for legal entities.

   The bank shall, in the criteria on monitoring the creditworthiness of clients - foreign persons/entities, take into account the risk of the country of its head office, i.e. the origin of such clients.

c) contents of the credit file for each bank's client,

d) measurement and monitoring of exposures for the purposes of estimating the level of taken credit risk and their classification into corresponding risk categories, that implies assessment of the creditworthiness in line with sub-item b) of this item, monitoring of the settlement of contractual obligations, monitoring of the changes in the collateral value, etc.,

e) calculation of impairment and special reserve on individual and group basis,

f) approval and monitoring of exposures which are part of the retail credit portfolio,

g) procedures for defining, identifying and monitoring of exposures with higher credit risk (problem exposures) and for monitoring the non-performing claims,

h) definition of internal credit risk exposure limits by client, by client category, activity, currency structure, geographic location, collateral instruments, i.e. measurement and monitoring of the exposure to risk of concentration in the credit risk exposure,

i) delegation of authorization to persons and bodies involved in the lending process,

j) definition of acceptable collateral - type of real estate and movables, securities, claims and other rights which may serve as collateral for a specific type of credit products of the bank, the required level of credit risk exposure coverage according to the type of collateral,

k) collateral foreclosure procedure,

l) procedure and frequency of evaluating the collateral market value,

m) method of extending the maturity date or claim restructuring, procedure for writing off claims, system for ban on lending for the purpose of claim collection,

n) procedures for monitoring the bank's lawsuits,

o) functioning of the system of internal control of the credit function,

p) generation of data on reporting to the supervisory and management bodies and all other persons involved in the credit risk management process,

q) definition of competencies, responsibilities and lines of reporting of the bank's bodies and the scope of activities of the respective organizational units in the bank responsible for credit risk management.

The bank shall establish and develop IT system for ensuring timely and permanent measurement, monitoring, control and reporting for the purposes of credit risk management.

38. The bank shall keep credit files for each client.

39. The credit file shall contain all relevant data available to the bank for determining the client's identity, creditworthiness, regularity of settling its liabilities and collateral quality.

The bank may keep the credit file for each client in electronic form, if it meets the IT security standards established by the National Bank.

40. The bank shall have an updated database in place on each credit product and on each type of collateral for the credit risk exposure, providing information on at least:

- the amount of non-performing claims by credit product and collateral,
- the amount of due claims by credit product and collateral,
- changes in the impairment and in the special reserve, presented in percentages, by credit product and collateral, on quarterly and annual basis,
- geographic, sector and other type of exposure concentration by credit product and collateral.

41. By applying the measurements and criteria specified in this Decision, the bank shall classify the credit risk exposure at least quarterly, and at the moment of approval of the credit risk exposure.

42. The National Bank shall, through on-site supervision, verify the classification made by the bank and the methodology for retail credit portfolio classification and the classification of similar financial instruments on group basis.

Based on on-site and off-site supervision of the bank's operations, the National Bank may require from the bank to change the risk category, the amount of impairment and the amount of special reserve for a certain credit risk exposure and of the methodology for classifying the retail credit portfolio and similar financial instruments on group basis.

VI. REPORTING TO THE NATIONAL BANK OF THE REPUBLIC OF MACEDONIA

43. The banks shall compile reports on the implementation of this Decision as of March 31, June 30, September 30 and December 31 and shall submit it to the National Bank.

The submission date of the report as of December 31 shall be 5 business days after the submission date for non-audited annual financial statements.

The submission date of the report as of March 31, June 30 and September 30 shall be 15 business days after the period the report refers to.

44. On special request of the National Bank, the bank shall compile a report as of another date and within another deadline different from the date and the deadline stated under item 43 of this Decision.

VII. TRANSITIONAL AND CLOSING PROVISIONS

45. The bank shall prepare the first report referred to in item 43 of this Decision, as of December 31, 2009 and submit it to the National Bank within the deadline specified by item 43 of this Decision.

46. For the purposes of calculating the present value of the on-balance sheet and off-balance sheet claims for which there was no obligation for discounting the expected future cash flows at the moment of their occurrence, the bank shall discount the expected future cash flows by applying the agreed interest rate.

47. The Governor of the National Bank shall prescribe the instructions and the form of the report on implementation of this Decision.

48. The provisions of this Decision shall respectively apply to foreign bank branches and savings houses in the Republic of Macedonia.

As an exception to item 10 of this Decision, individually important item shall be the total exposure of a savings houses to a client:

a) exceeding Denar 150,000, or
b) exceeding 0.007% of the total credit risk exposure of the savings house.

49. This Decision shall enter into force on the eighth day after its publishing in the "Official Gazette of the Republic of Macedonia" and shall start being applied on January 1, 2009.

50. On the date this Decision starts being applied, the Decision on classification of on-balance sheet and off-balance sheet items of the banks and the savings houses according to their risk degree ("Official Gazette of the Republic of Macedonia" no. 21/02 - revised text and 80/06) and the Decision on the amount and the method of establishing loan loss provisions of the banks ("Official Gazette of the Republic of Macedonia" no. 50/2001) shall become void.

D. no. 02-15/I-3/2008
January 31, 2008
Skopje

Petar Goshev, MSc.
Governor

President
of the National Bank of the Republic of Macedonia Council