



ProCredit Bank

Serbia

Annual Report 2003





CONTENTS

4	Key Figures
5	Mission Statement
6	Letter from the Board of Directors
8	Letter from the Management
10	ProCredit - An International Network
12	Partner Banks in the Region
14	The Bank and its Shareholders
16	Business Review
26	Branch Network
28	Organisation, Staff and Staff Development
30	Environmental and Ethical Standards
32	Our Clients
38	Audited Financial Statements



Key Figures

EURO '000	2003	2002	Change
Balance Sheet Data			
Total Assets	103,991	68,567	51%
Gross Loan Portfolio	74,323	38,965	91%
Business Loan Portfolio	65,370	32,124	103%
Micro Loans (< EUR 10,000)	24,875	9,507	162%
Small Loans (> EUR 10,000; < EUR 50,000)	28,661	17,215	66%
Medium Loans (> EUR 50,000)	11,833	5,403	119%
Housing Loan Portfolio	-	-	-
Other Loan Portfolio	7,022	5,154	74%
Loan Loss Provisions	1,931	1,253	55%
Accrued Interest	792	434	90%
Net Loan Portfolio	72,392	37,290	92%
Total Customer Funds	55,172	38,473	42%
Total Borrowing from Financial Institutions	37,074	19,190	93%
Shareholders' Equity	10,779	10,438	2%
Income Statement			
Operating Income	11,743	4,054	193%
Operating Expenses	10,363	5,762	84%
Operating Profit Before Tax	1,243	-1,708	N/A
Net Profit	1,380	-1,335	N/A
Key Ratios			
Cost/Income Ratio %	84%	114%	
ROE %	11%	-25,5%	
Capital Ratio	12%	24,8%	
Operational Statistics			
Number of Loans Outstanding	25,437	5,872	333%
Number of Business Loans Outstanding	11,722	4,485	161%
Number of Deposit Accounts	89,773	54,895	64%
Number of Staff	536	266	91%
Number of Branches and Outlets	21	18	17%

MISSION STATEMENT

ProCredit Bank Serbia is a development-oriented full-service bank. We offer excellent customer service and a wide range of banking products. In our credit operations, we focus on lending to micro, small and medium-sized enterprises, as we are convinced that these businesses create the largest number of jobs and make a vital contribution to the economies in which they operate. Our bank explicitly avoids all speculative lines of business and issues large loans only in exceptional cases, thus minimising the risk associated with such activities.

Our shareholders – most of whom are major, well-established international institutions – expect a sustainable return on investment, but are not primarily interested in short-term profit maximisation. We invest extensively in the training of our staff in order to create an enjoyable and efficient working atmosphere, and to ensure that our customers receive the friendliest and most competent service possible.



LETTER FROM THE BOARD OF DIRECTORS



The beginning of 2003 saw the assassination of Serbia's prime minister, Zoran Djindjic. The year ended with early parliamentary elections, as the democratic and reform-oriented government had lost the confidence of the public. Certainly, the year just ended was a tragic and challenging one for Serbia in terms of its efforts to transform itself into a democratic society with a free market economy. Now more than ever, the shareholders are united in their determination that ProCredit Bank shall continue to support this process and play a vital role in the establishment of a private sector in Serbia. We will pursue our mission with renewed commitment in 2004.

In 2003, ProCredit Bank developed into one of the main providers of financial intermediation for the private sector. The bank is among the top 10 banks in Serbia, both in deposit mobilisation and in lending to SMEs and private customers. ProCredit Bank is by far the leading provider of loans to very small enterprises in Serbia, and we strongly believe that, as such, it is making a valuable contribution to the economy. The bank is also one of the fastest-growing institutions in the entire banking sector.

After the dynamic start made in 2001 and 2002, the year 2003 was one of consolidation and institutional strengthening. The bank's procedures and risk management systems, as well as its audit and internal control functions, were subjected to a thorough review and were revised to meet both present and future challenges. As a result, the bank reached operational break-even, and posted a profit for the year as a whole. In addition, the improved structures enabled us to resume the expansion of the bank's branch network in the last quarter of 2003. Today, ProCredit Bank is serving people throughout Serbia through a network of 21 fully-fledged branches and lending offices.

The bank's staff almost doubled during the year as a result of the opening of new branches, the upgrading of existing lending offices and the strengthening of the head office. The performance of both experienced staff and the many new employees was outstanding. And we greatly appreciate the commitment, dedication and enthusiasm which our employees have invariably shown.

Despite the many challenges that lie ahead for Serbia, we are confident about the future of our bank. We have established a business model for our operations that enables us to achieve dynamic growth on a sustainable basis. In 2004 we will make significant investments in the bank's branch network, in staff recruitment and training, and in technology; moreover, we will become even more strongly integrated into the ProCredit Bank network, enabling us to reap even greater benefits from our membership of this group of financial institutions.



Dr. Klaus Glaubitt
Chairman

**Members of the Board of Directors
as at December 31, 2003:**

*Dr. Klaus Glaubitt
Dr. Helmut Töllner
Dr. Claus-Peter Zeitingner
Karlo de Waal
Elizabeth Wallace*

**Members of the Audit Committee
as at December 31, 2003:**

*Rüdiger Rurainsky (Chairman)
Eckard von Leesen
Carlen Dam
Martin Godemann*

LETTER FROM THE MANAGEMENT

In 2003 ProCredit Bank continued to work toward the goals it has defined for itself. Roughly 12,000 loans were disbursed to individual entrepreneurs and businesses at a combined value of more than YUM 5 billion (EUR 78 million), which translated into a loan portfolio growth of almost 100%. More than 35,000 new business and retail customers were served through a network of 16 branches and five credit offices, increasing the customer base to more than 60,000.

This growth was facilitated by a 42% increase in customer deposits and by funding support from the bank's shareholders. The EBRD, IFC and KfW provided long-term credit facilities equivalent to 100% of the bank's capital. As long as the political and economic situation in Serbia remains unstable, further support from international financial institutions and banks will be required if the ProCredit Bank's growth is to continue. We believe that we have made good use of the funds entrusted to us, in terms of both financial and developmental criteria.

Today, the bank has a sound and rapidly growing income base, which puts it in a position to invest further in growth and in the expansion of its market presence. Costs and risks are well under control. The management therefore assesses the outlook for the year 2004 and beyond as favourable. Indeed, if the macroeco-

omic environment improves and certain constraints (e.g. the requirement that 50% of retail clients' foreign currency savings be deposited with the NBS) are eliminated, then even greater growth potential will be generated. The capital and money markets in Serbia have gradually been developing as they undergo reform, and the bank will make use of the opportunities created by these reforms.

After the first two years of operation, in which it focused on building and expanding its branch network, the bank's priority in early 2003 was to strengthen its head office departments and improve procedures, risk management and cost control. We are grateful for the commitment of the bilateral and international technical assistance providers who supported this process.

We would also like to express our gratitude to the bank's hard-working and dedicated staff. Over 250 new staff members were recruited, trained and integrated into our team, bringing the total number of employees to more than 500. While the competition among banks for young, motivated and well-trained staff is increasingly strong in Serbia, we believe that in comparison to our competitors, we offer a better working climate, better guidance, more opportunities for advancement and a greater appreciation for the individual. This has been and remains the key to our bank's success.



Christoph Freytag
General Director

Dörte Weidig
Deputy General Director

Gian Marco Felice
Deputy General Director

PROCREDIT – AN INTERNATIONAL NETWORK



ProCredit Bank

ProCredit Bank Serbia is part of a large network of financial institutions which currently has 18 members worldwide. In this introduction to our annual report, we would like to briefly acquaint you with this network.

Small and medium-sized enterprises (SMEs) are seen by many economists and development experts as the main engine of growth and job creation. Moreover, in political terms, the middle class which emerges when SMEs grow and develop usually plays a stabilising role in society. One important factor for the development of SMEs is their access to financial services. Most commercial banks, however, are reluctant to extend credit to this client group, citing various reasons, some more justified than others: the inability of SMEs to provide sufficient collateral, a lack of formal accounts and transparency, excessive costs for the administration and monitoring of such loans, insufficient demand for other banking services among these clients, excessive credit risk, etc. Consequently, most banks focus only on the upper end of this market segment, and, if they offer small loans at all, then usually in the form of consumer lending, which is less demanding in terms of credit technology and risk management.

In response, the initiators of the ProCredit network have established 18 target group-oriented financial institutions over the last five years, in Eastern Europe, Latin America and Africa. These institutions focus on providing business loans to enterprises ranging from the very small to the medium-sized, thereby helping to close a major

gap in the market. Over the years, we have developed a profound understanding of both the problems faced by these small businesses and the opportunities available to them, and we have tailored our credit technology to reflect the realities of their operating environment.

As the figures demonstrate, our approach has been a resounding success: As of December 31, 2003 the network had grown to over 200 branches and 4,600 employees, and the combined total assets of the network institutions exceeded EUR 1.0 billion. The loan portfolio amounted to some EUR 600 million and was distributed among roughly 300,000 customers, which translates into an average loan size of around EUR 2,000. And only 1% of the overall credit volume outstanding at the end of 2003 was more than 30 days overdue. This proves that it is precisely the small borrowers we serve who are the most reliable customers.

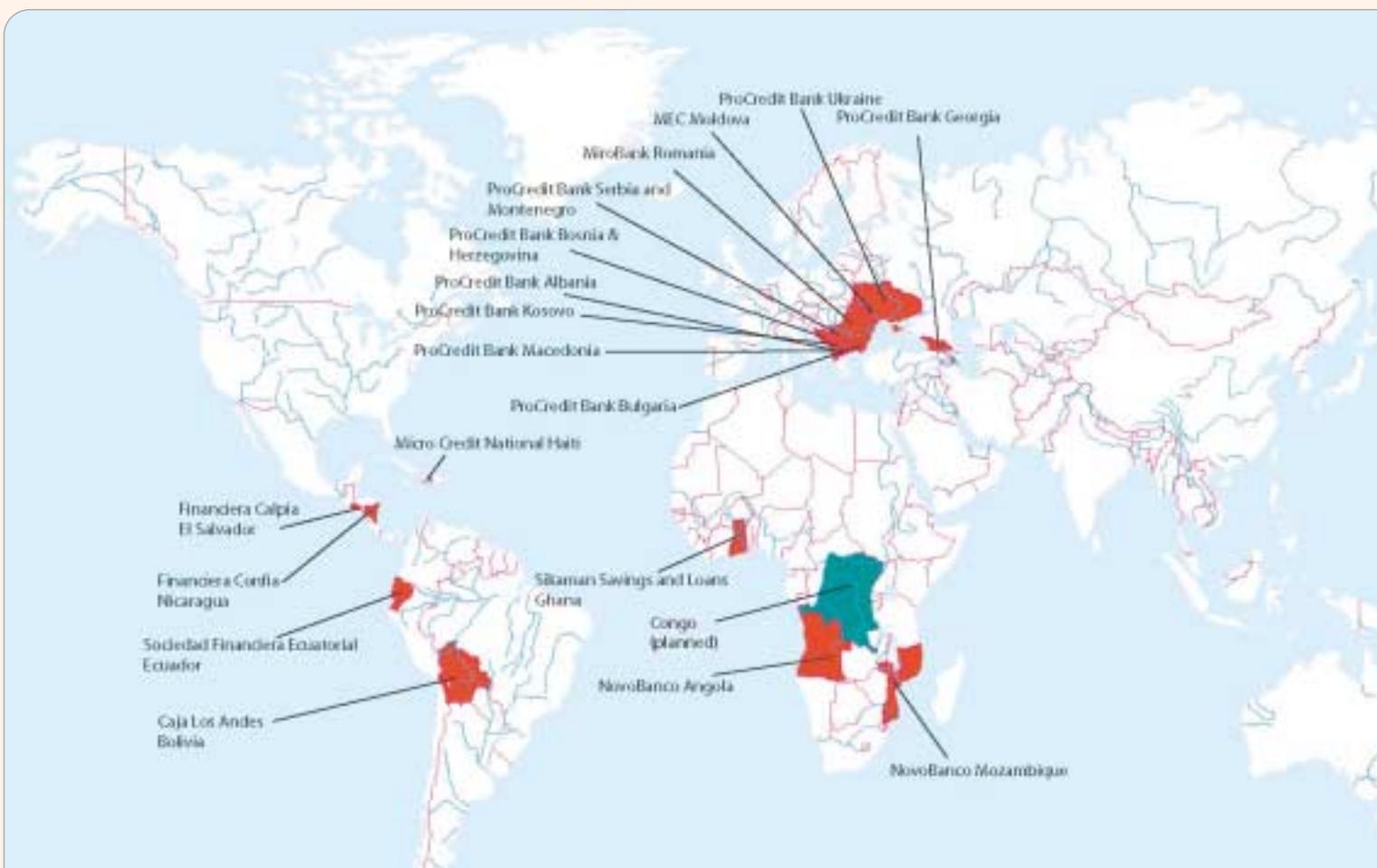
In their initial phase of operations, the ProCredit institutions focus on lending. Over time, as they extend their range of products to include deposit-taking and other banking services demanded by their customers, the institutions gradually develop into full-service banks – without, however, losing their special character and their focus on the SME client group. Based on our initial success and the phasing of operational focus at country level, our planning envisages significant network expansion. By the end of 2008, we expect the network to have a presence in 25 countries, with 450 branches, 10,000 employees and a loan portfolio of EUR 2.5 billion. Growth on such a scale can only be financed if, in addition to maintaining successful lending operations, we also succeed in deepening the trust of our depositors. As of the end of 2003 the network reported a total deposit volume of around EUR 550 million, and we are confident of being able to raise this figure to around EUR 2.0 billion within the next five years.

The network institutions are profit-oriented, but at the same time the major shareholders retain their commitment to developmental goals. They do not see profit maximisation as the sole objective of the banks' activities. In 2003, the ROE for all of the institutions in the network in hard currency, after deduction of profit taxes, was 10%.

The major shareholders in the individual network institutions are Internationale Micro Investitionen (IMI), the KfW Banking Group, the IFC, the EBRD, FMO and the DOEN Foundation. IMI, which is owned to a large extent by the same institutions that hold shares in the individual network institutions, can be considered the strategic investor of this group. Through share swaps and sales, IMI's direct stakes in the individual institutions are increasing every year.

The network members' activities are guided and supervised by IMI and by IPC, the management consulting firm which provides management services to the banks. Both IMI and IPC are located in Frankfurt am Main, Germany. This centralised management and supervision makes it possible to achieve synergies which have a positive impact in many areas – for example, in regard to training, corporate culture and identity (including establishment of the common “ProCredit Bank” logo and corporate brand), risk management, auditing, business policies, funding for lending activities, as well as ethical and other professional standards.

The international network of ProCredit institutions; see also www.imi-ag.com



PARTNER BANKS IN THE REGION

ProCredit Bank Serbia benefits from steadily increasing cooperation with a number of partner banks in the region – banks that share our philosophy and mostly have a shareholder structure similar to that of ProCredit Bank Serbia.

The shareholders of ProCredit Bank Serbia, who have already proven their commitment to Serbia, also share a regional vision and

support banks that are successfully carrying out the same mission in neighbouring countries.

As a member of a regional network uniting banks with common experiences and objectives, ProCredit Bank Serbia is in a unique position to satisfy the needs of Serbian customers for competent and reliable services throughout the region.



Name	Highlights	Contact
ProCredit Bank Albania	Founded in March 1999 13 branches 9,003 borrowers / EUR 47 million in loans 36,261 depositors / EUR 80 million 271 employees	Rruga Sami Frasheri, Tirana Tel./Fax +355-4-271 272 / -276 info@procreditbank.com.al www.procreditbank.com.al
ProCredit Bank Bosnia and Herzegovina	Founded in October 1997 8 branches 10,761 borrowers / EUR 44 million in loans 17,958 depositors / EUR 10.6 million 216 employees	Sime Milutinovica Sarajlije 4, 71000 Sarajevo Tel./Fax +387-33-250 950 / 441 428 info@procreditbank.ba www.procreditbank.ba
ProCredit Bank Bulgaria	Founded in June 2001 28 branches 16,000 borrowers / EUR 76 million in loans 12,500 depositors / EUR 38 million 456 employees	131, Hristo Botev Blvd., 1233 Sofia Tel./Fax +359-2-92171-05 / -09 contact@procreditbank.bg www.procreditbank.bg
ProCredit Bank Georgia	Founded in May 1999 17 branches 10,653 borrowers / EUR 37.9 million in loans 20,641 depositors / EUR 14.0 million 404 employees	Tamar Mephe Ave. 18, 0112 Tbilisi Tel./Fax +995-32-202 222 / 250 580 info@procreditbank.ge www.procreditbank.ge
ProCredit Bank Kosovo	Founded in January 2000 11 branches 15,950 borrowers / EUR 67 million in loans 145,375 depositors / EUR 256 million 287 employees	Rr. Skenderbeu, 38000 Prishtina Tel./Fax +381-38-240 248 / 248 778 info@procreditbank-kos.com www.procreditbank-kos.com
ProCredit Bank Macedonia	Founded in June 2003 4 branches 1,480 borrowers / EUR 7 million in loans 2,704 depositors / EUR 2 million 82 employees	Marks i Engels 3, 1000 Skopje Tel./Fax +389-2-3219 -900 / -901 info@procreditbank.com.mk www.procreditbank.com.mk
Micro Enterprise Credit (MEC) Moldova	Founded in December 1999 10 branches 2,887 borrowers / EUR 6.6 million in loans 89 employees	Str. Ismail 31, 2001 Chisinau Tel./Fax +373-22-270 707 / 273 488 office@mec-moldova.com www.mec-moldova.com
MIRO Bank Romania	Founded in May 2002 8 branches 5,010 borrowers / EUR 26.6 million in loans 9,535 depositors / EUR 5 million 163 employees	Str. Fagaras 6, 7000 Bucharest, Sector 1 Tel./Fax +40-21-402 8380 / -8383 headoffice@mirobank.ro www.mirobank.ro
ProCredit Bank Ukraine	Founded in December 2000 23 branches 12,580 borrowers / EUR 59 million in loans 1,061 depositors / EUR 11 million 446 employees	Vul. Bozhenka 86, 03150 Kiev Tel./Fax +380-44-490 6040 / -6081 procredit@procreditbank.com.ua www.procreditbank.com.ua

THE BANK AND ITS SHAREHOLDERS

ProCredit Bank Serbia was established in April 2001 by international investors under the name Micro Finance Bank. As reflected in its shareholder structure, the bank is a genuine private-public partnership. By providing financial services to small businesses, the shareholders intend to achieve developmental aims; at the same time, it is their shared conviction that the development goals can only be achieved in a

sustainable way through a regulated banking institution, operating in the private sector. In the three years since its founding ProCredit Bank Serbia has developed into a full-scale commercial bank providing a broad range of banking services. Although the bank is already funding a considerable share of its lending activities with deposits, it still needs the financial support of public, international financial institutions.

Shareholder	Sector	Headquarters	Share	Paid-in Capital in EUR
KfW	Banking	Germany	16.6%	1,890,041
IFC	Banking	USA	16.6%	1,890,041
EBRD	Banking	UK	16.6%	1,890,041
FMO	Banking	Netherlands	16.6%	1,890,041
IMI	Investment	Germany	16.6%	1,890,041
Commerzbank	Banking	Germany	16.6%	1,890,041
Total			100%	11,340,248



KfW Banking Group (Kreditanstalt für Wiederaufbau), founded in 1948,

provides financial packages designed to stimulate economic, social and ecological development in Germany, Europe and the world over. The group focuses on the promotion of SMEs, the financing of housing construction and modernisation, protection of the environment and the climate, export and project finance and support for developing countries and transition economies.



The **International Finance Corporation (IFC)**, a multilateral institution, promotes the development of the private sector in its developing member countries. A member of the World Bank Group, but legally and financially independent, IFC provides long-term loans and equity finance at market terms and conditions in support of private sector activities, helps mobilise additional financing from other sources and provides advisory services to both government and businesses. Since its founding in 1956, IFC has invested almost USD 30 billion of its own funds in more than 2,400 companies in 136 developing countries.

The **Nederlandse Financierings-Maatschappij voor Ontwikkelings-**



landen (FMO) is owned by the Dutch government and leading Dutch banks. It supports private sector development in 71 countries. FMO provides finance for projects that meet its three investment criteria: additionality, catalysis, and good governance. As such FMO provides finance for professionally managed ventures where “ordinary” banks would not, and where it can mobilise significant additional private sector investment. FMO focuses on providing support to the financial sector and companies in “low-income” and “low-middle-income” countries.



The **European Bank for Reconstruction and Development (EBRD)** was established in 1991. It aims to foster the transition towards open, market-oriented economies and to promote private and entrepreneurial initiative in the countries of Central and Eastern Europe and the Commonwealth of Independent States (CIS) committed to democracy, pluralism and market economics. The EBRD seeks to help its 27 countries of operations to implement structural and sectoral economic reforms, promoting competition, privatisation and entrepreneurship. In fulfilling its role as a catalyst of change, the bank encourages cofinancing and foreign direct investment from the private and public sectors, helps to mobilise domestic capital, and provides technical cooperation in relevant areas.

Internationale Micro Investitionen AG (IMI), founded in 1998, is a commercial development-oriented investment company.



It has so far taken equity stakes totalling EUR 40 million in 18 banks and financial institutions based in developing countries and transition economies. IMI can be seen as the strategic investor in the ProCredit network, and as its administrative headquarters. The company’s shareholders represent a 50:50 mix of private and public investors.

Commerzbank AG was established in 1870 and today is one of the top five



banks in Germany. With a strong international network comprising offices and shareholdings in 43 countries, Commerzbank is a universal bank providing retail, wholesale and investment banking services. It also offers other financial services via a number of subsidiaries, such as leasing fund management, real estate and equity investment.

BUSINESS REVIEW



2003 will be remembered in Serbia mainly for two events: the assassination of Prime Minister Zoran Djindjic in March, and the victory of the nationalistic Radical Party in the parliamentary elections held in December after the government lost the support of the Serbian public. Although these events were clearly setbacks, we believe that they will not derail Serbia's efforts to achieve a peaceful and democratic future through reform, growth and development.

Despite the difficult political situation in 2003, which brought the reform process almost to a halt, the economy showed positive signs. Inflation declined still further, to 7.8% (down from 14% in 2002). The dinar depreciated against the euro at a moderate rate of 13%, and the GDP grew by an estimated 5% (up from 4.1% in 2002).

On the downside, domestic demand lost momentum in 2003, while unemployment remained at an unacceptably high level. Privatization proceeds in 2003 were impressive, but resulted by and large from the sale of a few quasi-monopolistic companies (e.g. in the tobacco industry), and were mostly used to finance the budget deficit and to compensate for the growing trade deficit. The restructuring of large companies which account for a significant number of jobs still lies ahead, and the social problems which can be expected as a result represent a serious challenge for the government. As a consequence, promoting SMEs has become part of the politicians' agenda and is now given a higher priority.

2003 was a turbulent year in the financial sector, as in the economy as a whole. While little progress was made towards the restructuring of the state-owned or partly state-owned banks which control over 60% of the sector's assets, a number of foreign banks entered the market. The sector's total assets stand at EUR 5 billion. Financial intermediation in Serbia is still at a low level and hindered by a number of constraints. First and foremost among them is the requirement that 50% of the foreign currency savings of private customers be maintained with the National Bank of Serbia (NBS), which, given that over 90% of all savings in Serbia are denominated in foreign currency, limits banks' lending activities and increases the cost of funding. Another constraint is the 20% sales tax on interest income, which is indicative of the high level of nominal interest rates in Serbia.

On the other hand, the former state payment agency ZOP was abolished in 2003, and companies now maintain accounts and facilitate payments through a modern and efficient RTGS clearing system. Towards the end of the year a new domestic debit card, the DINA Card, was introduced and is rapidly finding its place in Serbia's payment industry.

In response to these changes, the banks noticeably expanded their lending and retail activities, but still did not seek to serve the target group of small businesses or a broader public. ProCredit Bank is one of the few banks, most of them foreign, which finance the private sector in Serbia to a noticeable degree, and it is the market leader in terms of lending to micro, small and medium-sized businesses.



Loan Portfolio Development

The year 2003 was one of internal consolidation for ProCredit Bank Serbia, after the first two years of rapid branch expansion and before a new phase of regional expansion in the years to come. However, despite its focus on establishing new structures and strengthening existing ones, the bank was able to accelerate its growth in 2003:

Offering loans and all other relevant financial services to SMEs is the bank's core business. In line with this mission, the number of loan officers was increased from 70 to 115 in order to enable the branches to increase their disbursement capacity.

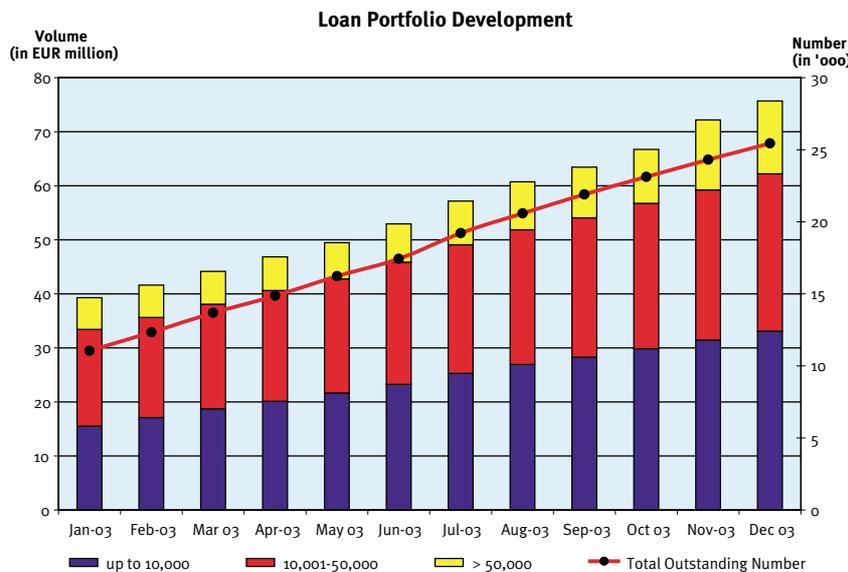
As a result, the business loan portfolio increased 103% in terms of volume, to EUR 65 million as of December 2003, and 160% in terms

of numbers, to 11,700 loans outstanding. When the consumer loan portfolio is added, ProCredit Bank's total portfolio amounts to EUR 73 million.

The difference in the rates of growth in terms of volume and in terms of numbers reflects the bank's focus in 2003 on lending to very small enter-

prises demanding loan amounts up to EUR 10,000. This segment of the market has without doubt long been ignored by the banking sector; traditional banks and even banks active in SME lending consider such enterprises to be credit-worthy in principle, but too risky as borrowers.

As of December 2003 the bank had 60,000 clients, 25,000 outstanding loans, a healthy loan portfolio, a much larger deposit base and an expanded range of retail products. And thanks to successful cost control measures and its increased business income, the bank broke even in 2003.

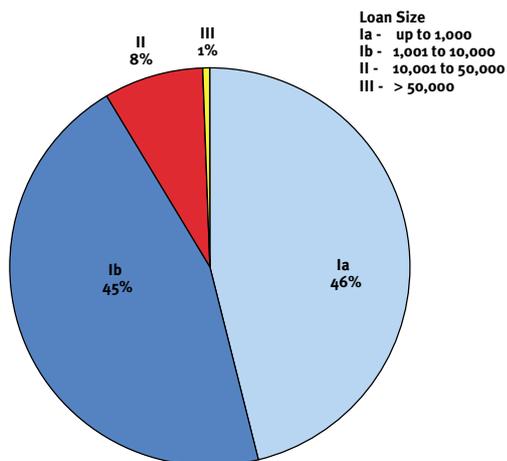


ProCredit Bank definitely does not adhere to this view. More than 90% of all loans disbursed went to this group of clients. The average outstanding loan amount for the business portfolio of EUR 5,600 is a reflection of this focus. In order to ensure that the very small loans are even more in line with the clients' needs, the bank introduced a simplified and accelerated procedure for loans below EUR 2,000.

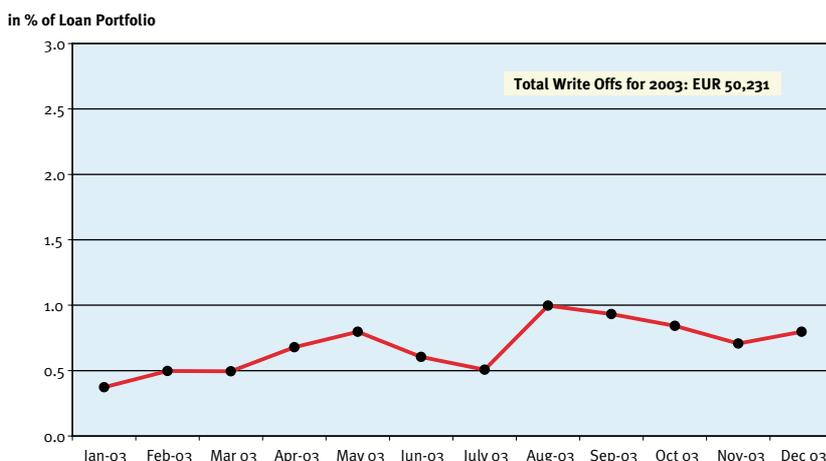
ket opportunities for our bank. Loan officers were given specialised training to allow them to better serve this group of customers. As a result of our efforts in this area, the medium portfolio increased from EUR 5 million to EUR 12 million during 2003.

The agricultural lending programme, begun in 2002, continued to expand in 2003. The credit technology, initially developed and

Number of Outstanding Loans by Loan Size (13-Dec-2003)



Loan Portfolio Quality (arrears > 30 days)

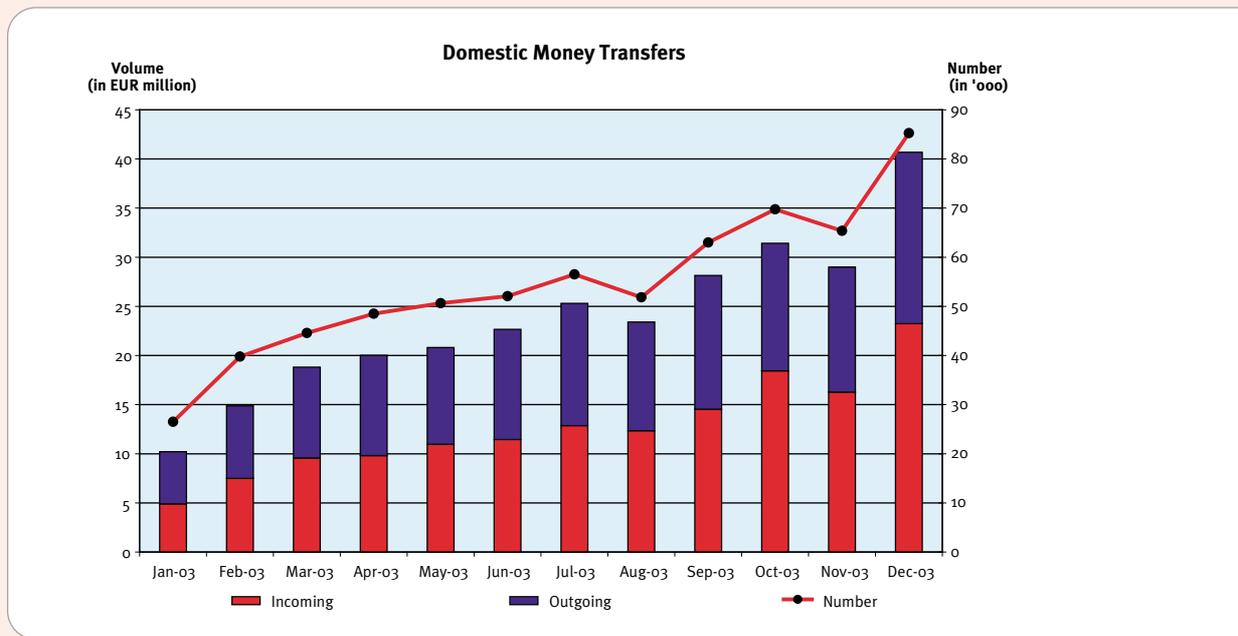


In addition to providing very small enterprises with loans, ProCredit Bank also established a specialised unit for medium-sized loans, i.e. loans above EUR 50,000. Such loans are being disbursed by other banks too; however, not to a sufficient extent and not in a very flexible manner, which leaves considerable mar-

tested in Novi Sad, was implemented in all branches. More than 3,000 farmers have taken out loans; the average outstanding loan amount is only EUR 3,100. In most cases these individuals had never had any contact with a formal financial institution at all and were being integrated into the formal financial system for the

first time. 2003 was a difficult year for farmers, with a drought which affected the whole of Europe, and in Serbia, the harvest of many agricultural products was much smaller than in previous years; in spite of this, the agricultural loan programme did not experience any arrears or losses. As of the end of December 2003, the bank's portfolio in agriculture and food processing amounted to EUR 10 million.

The portfolio growth could not be considered successful if we could not at the same time report excellent portfolio quality over the whole range of loan products. Although the political events and the unstable economic situation had a negative impact on the very small, small and medium enterprise sector, and despite a shortage of liquidity and a decline in domestic purchasing power in the second half of the year, the bank was able to keep the share of the portfolio



at risk under 1%. Only 15 loans had to be restructured, and the loss rate (write-offs against average loan portfolio) was less than 0.1%.

In January the National Bank of Serbia abolished the centralised payment system ZOP, allowing all commercial banks to process domestic and international payments. Consequently, since the beginning of 2003, ProCredit Bank has actively participated in the national payment system. Our payment services are fast and reliable, and are becoming increasingly popular with our business loan clients.

In order to make it easier for business clients to access the bank's services, especially those clients who are based outside the cities where ProCredit Bank has a branch, e-banking was introduced. Small and medium-sized clients have the option of processing all their banking business and all their payments through the Internet.

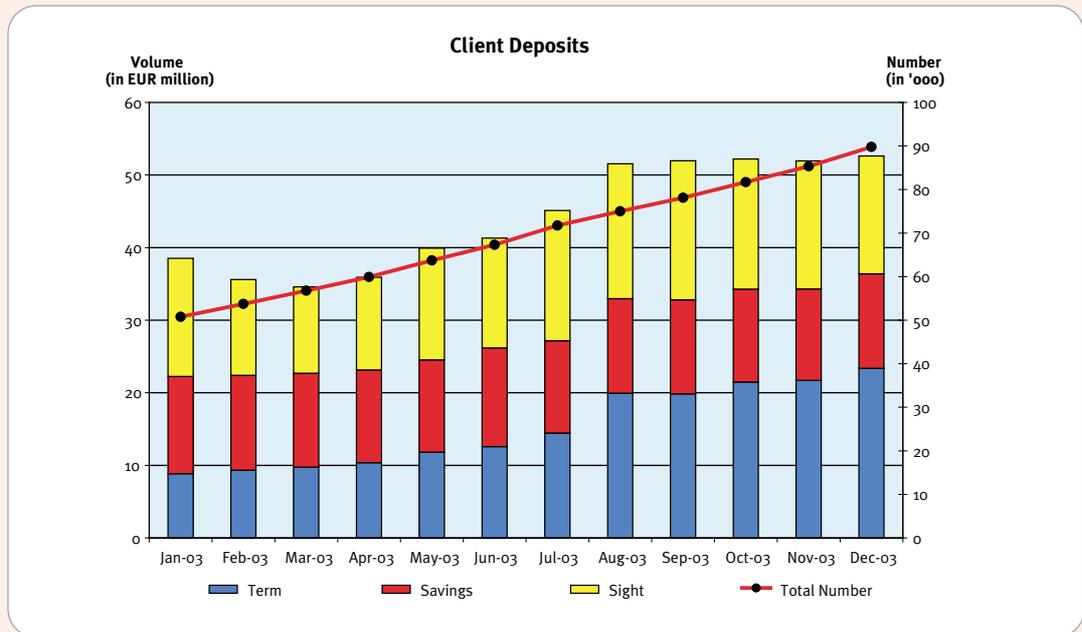


A positive trend was also observed with regard to international payments. Enterprises with business connections abroad made increasing use of the bank's funds transfer services. The bank also intensified its marketing of letters of guarantee and letters of credit, and by the end of 2003 the volume of transactions in this area of international business had increased to EUR 3 million.

Diversification of the Client Base

In order to achieve its objectives of realising strong portfolio growth, achieving a substantial degree of financial intermediation and positioning the bank as a full-service bank, ProCredit Bank must offer a wide range of retail products to the general public and must increase its attractiveness for depositors.

A further positive sign of the public’s confidence in the bank was the very positive reaction to the name change from “Micro Finance Bank” to “ProCredit Bank” in September 2003. With this change in name, ProCredit Bank aimed both to emphasise its membership in a network of ProCredit Banks and to strengthen its image as a full-service bank. The new name, logo and corporate style were welcomed not only by our clients, but by our staff as well.



Through attractive conditions for both savings and term deposits and through active marketing of the bank as a full-service bank, the bank was able to increase its total deposit base by 42%, to EUR 54 million, by the end of 2003.

A further step in expanding the range of products for private customers was the introduction of the new debit card "DINA Card" in November 2003. By the end of the year, ProCredit Bank had issued 1,800 DINA Cards and received another 4,900 applications. Based on these results, we are confident that the bank will play an important role in this market in 2004.

ProCredit Bank also took the introduction of the card as an opportunity to support the installation of the equipment needed to use it, i.e. ATMs and POS terminals. By the end of 2003 the bank was in the process of equipping all its branches with ATMs and had set up a special unit promoting POS facilities to merchants of all kinds, but in particular to the retail shops among the bank's loan clients.

Since its inception ProCredit Bank has counted many NGOs, international organisations and embassies among its clients. A tailored service package is available for this group of clients, and a specialised client advisor is on staff to attend to their needs. During 2003 the bank continued to offer this target group high-quality customer service in the processing of their international payments and attractive rates on their deposits.

Financial Performance

During 2002, the strong branch expansion, and the fact that the credit portfolio was still young, led to a net loss for the year, as expected. In 2003 the bank reached the break-even point, and its annual financial statements, which were prepared in accordance with IAS, showed a net profit of EUR 1.1 million.

The growth of the portfolio provided the bank with steadily increasing interest and fee income, whereby interest margins remained broadly stable. Together with a low rate of arrears, this ensured stable and growing income during the year.

The payment business made an important contribution to the positive financial result for the year. The income from international payments was stable despite the market pressure on commission fees, while income from domestic payments increased substantially during the year. Income from foreign exchange business, i.e. net income from buying and selling currencies to and from clients and banks, increased as well. In addition, careful liquidity management allowed the bank to reduce the cost of obtaining onlending funds, while investments of short-term excess liquidity, within set limits, in treasury bills issued by the National Bank of Serbia led to increased income

Feature: Risk Management

ProCredit Bank consolidated its operations and strengthened its internal control during 2003. The establishment of the Risk Management Committee (RMC), which was created to monitor, control and manage the various risks faced by the bank, played a vital role in the process.



With regard to the **credit risk**, the portfolio of ProCredit Bank has always performed strongly. The portfolio at risk has never exceeded 1%, and on average has remained below 0.5%. Nonetheless, given that lending to very small, small and medium enterprises is ProCredit Bank's core business and most important source of income, the management of credit risk is a priority.

In order to better quantify and control credit risk exposure, two approaches to portfolio analysis are applied. In the case of small

loans (between EUR 10,000 and EUR 50,000) and very small loans (below EUR 10,000), we monitor the distribution of the overall portfolio in terms of maturity, activity and region in order to identify any undesirable concentration of credit risk. In contrast, medium loans (above EUR 50,000) and the associated credit risk are analysed on an individual basis in the framework of regular financial monitoring and risk assessment by the RMC.

The bank's loan loss provisioning policy reflects this approach: Both general loan loss provisions, and specific loan loss provisions based on the number of days in arrears, are set aside for loans smaller than EUR 50,000; while individual loan loss provisions are established for medium-sized loans, based on the RMC's financial assessment.

Apart from credit risk, the main risks to which the bank is exposed in the course of its normal business operations are: liquidity risk, currency risk, interest rate risk and compliance risk.

The bank aims to minimise the short-term **liquidity risks** associated with both cash and non-cash liquidity. Cash management for the branch network is centralised in the head office in order to ensure that the level of cash in the vaults is optimised with respect to opportunity and cost. Serbia is still suffering from the effects of many years of instability in the financial sector, and we are aware that clients are very sensitive to the availability of cash on demand, judging a bank's reliability by it. On the other hand, by optimising cash management

and by introducing analytical tools to manage cash positions in the branches, the bank was able, over the course of 2003, to reduce the average amount of cash kept in the vaults by two-thirds. As regards non-cash liquidity, we optimised the overall liquidity position of the bank by introducing advanced liquidity planning tools. ProCredit Bank is also an active participant in the developing Serbian interbank market.

In 2003 ProCredit Bank restructured its capital base from dollars to euro. Given that the Serbian economy is euro-dominated, this restructuring had the effect of shielding the bank from the undesirable effects of volatility between the dollar and the euro. In general, the RMC manages the **currency risk** by analysing the open currency position of the bank on a daily basis, and clearly defined limits for open currency positions are in place.

Interest rate risk arises when there is an imbalance between fixed-rate and floating-rate assets and liabilities. Most of the bank's credit portfolio is fixed-rate, while most of the external financing provided to the bank is floating-rate. The RMC monitors the current situation and makes projections as to how the parameters will change in the future. Since the margins are comfortable and the structure of the loan portfolio is predominantly short-term, the level of interest rate risk taken on by the bank is considered acceptable for the time being.

Finally, **compliance risk** arises with regard to the bank's obligation to respect certain prudential limits set by the National Bank of Serbia and by its shareholders. The RMC monitors and enforces compliance with these limits.

Outlook

Despite the uncertainty as to how the economy will develop, the business prospects for ProCredit Bank in 2004 are favourable. The bank is continuing its regional expansion: it is in the process of upgrading credit outlets, opening additional branch offices in cities where the bank already has a presence, and new branches



in cities which are not yet served by the bank. Based on this expansion, another very dynamic year of lending activities can be expected. The portfolio growth will be supported by ongoing training measures for both experienced and new lending staff and by stronger segmentation of the bank's range of loan products. And with new products for private individuals and a strong emphasis on attracting deposits, growth can be expected in this area as well.

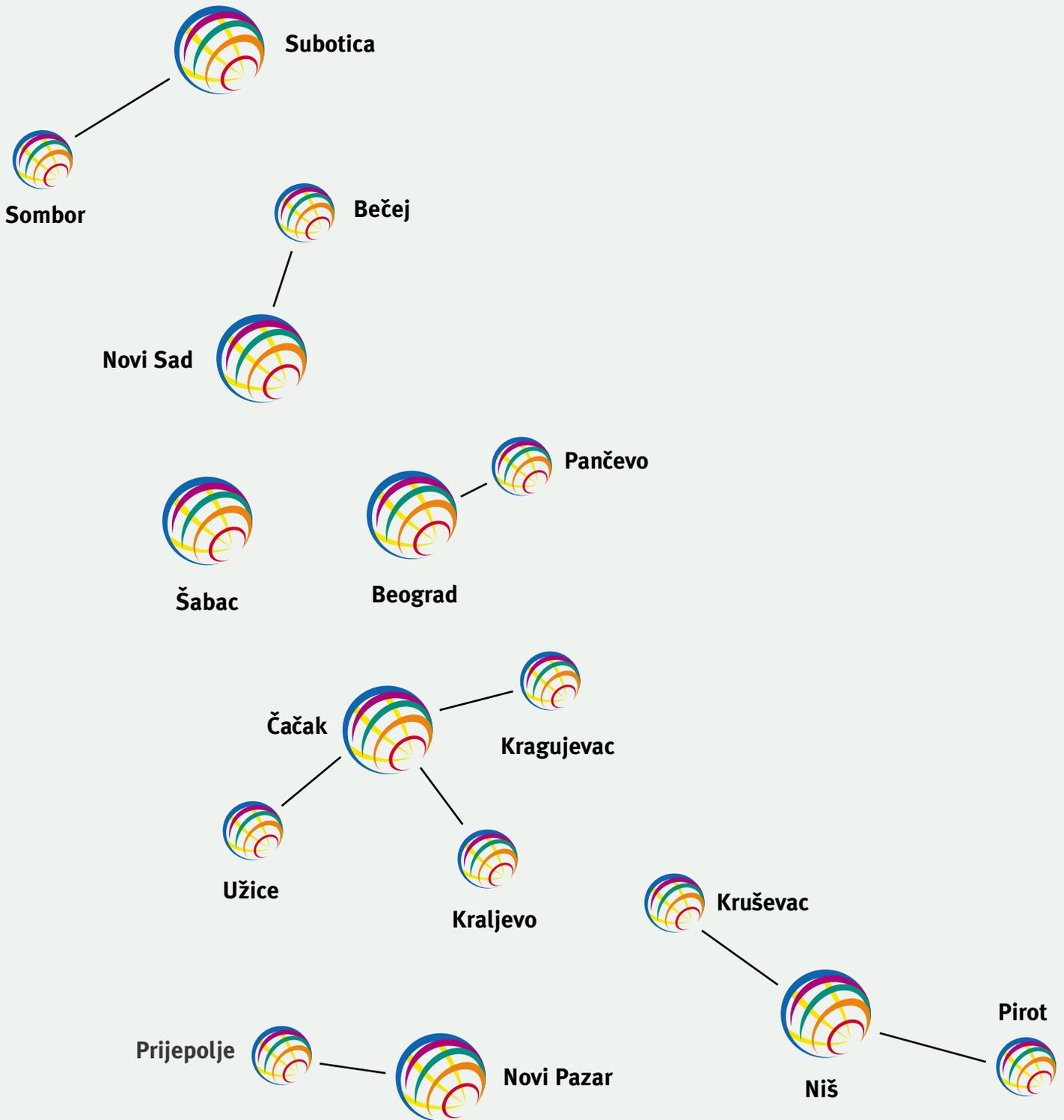
BRANCH NETWORK



ProCredit Bank's branch network is rapidly expanding. The bank already has a presence in all of the main regions of Serbia. The full range of services is available in the following cities: Belgrade, Novi Sad, Nis, Subotica, Novi Pazar, Cacak, Uzice, Sabac, Kragujevac, Kraljevo, Kursevac. In addition to these full-fledged branches, the bank has also created a network of credit offices, mainly offering loans

for small and medium-sized businesses. Credit offices of this type operate in Pancevo, Pirot, Becej, Sombor and Prijepolje.

The dynamic expansion of the branch network is an ongoing process. ProCredit Bank will soon have an outlet in more than 20 towns and cities in Serbia.



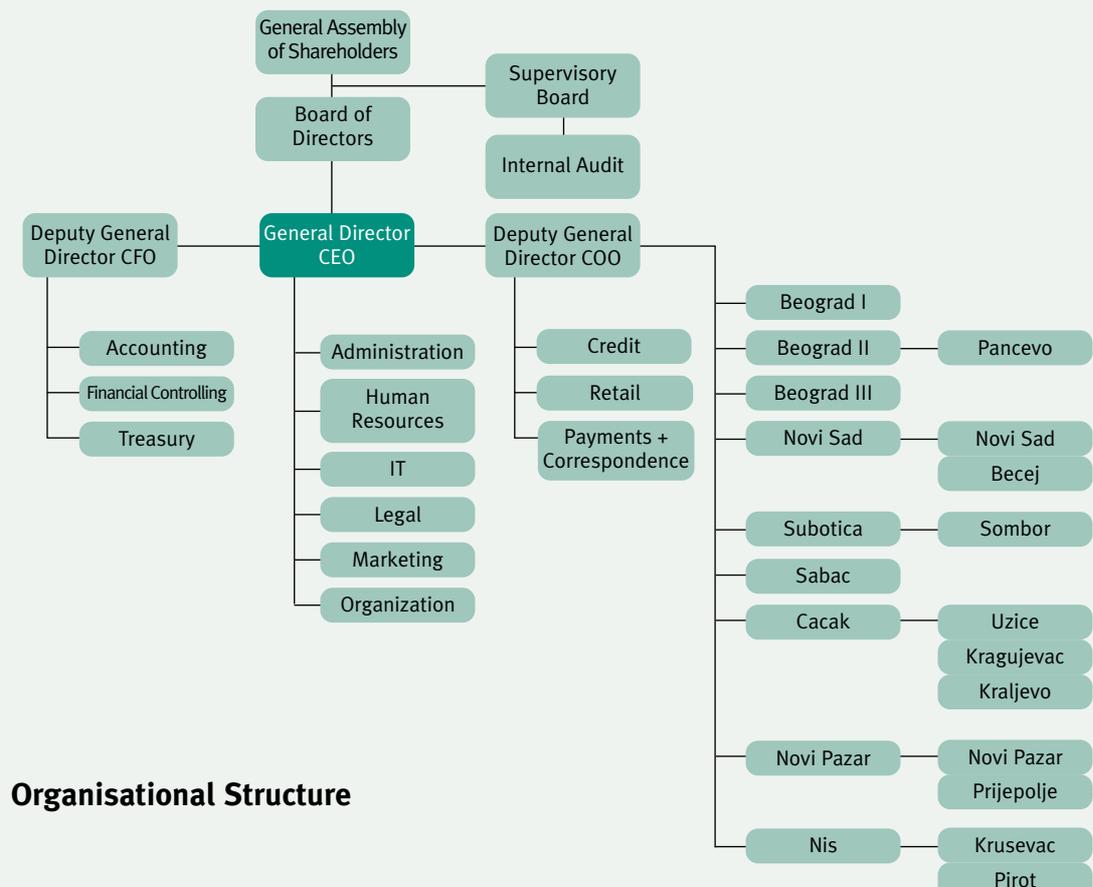
ORGANISATION, STAFF AND STAFF DEVELOPMENT

Personal contact has always been important in banking. Despite the increasing importance of modern technologies, this fact has not changed; if anything, interaction with customers has gained in importance, and more attention is given to customer relationship management than ever before. Although loan agreements, credit and debit cards, payments etc. are all backed by documentation, the banking transactions themselves remain abstract and virtual; banking products are not tangible, and selling them to customers consequently requires personal communication – i.e. the provision of explanation, advice and support.

The success of a bank therefore depends on the qualifications and the commitment of its

employees. Every bank is only as good as its employees' ability to provide good customer service; the bank's customers must find its staff competent, trustworthy and friendly. A bank will only succeed in its business operations if it first succeeds in developing a team of individuals who are competent in their areas of expertise, identify with the bank's business goals, and are quick and creative in finding solutions to even the most complex financial problems presented by the bank's customers.

This is also true for ProCredit Bank, a young and fast-growing institution. Its employees, both the specialists in the head office and the more generalised staff in the bank's branches, must be technically proficient in a variety of fields. And in light of the bank's increasingly customer-oriented focus, the employees require not



only expertise as bankers, but also a methodical approach to their work and sound social skills. In other words, they need to be able to solve problems systematically and be good communicators, with the empathy and flexibility both to respond to the needs of the businesses and individuals served by the bank, and to cooperate well with fellow employees in teams.

The bank's accelerated growth, the rapid introduction of new products and the preparations for the faster pace of branch expansion planned for the coming years posed considerable challenges for the staff in 2003, and thus for human resources management at the bank. ProCredit Bank was able to master these challenges because personnel development has always been an integral part of its business strategy:

Firstly, the bank's hiring policy has always been to recruit mostly young people, but also to employ more experienced staff where necessary, thus ensuring that the institution has the optimum combination of enthusiasm and know-how required to provide high quality services. The hiring of university graduates and young professionals was and is considered to be a very important aspect of the bank's commitment to the development of Serbia, since it is important to give young graduates a chance to pursue a career in their home country.

Secondly, the bank seeks to enhance employees' skills and abilities on an ongoing basis in order to consistently maintain high standards in the performance of their duties. Training measures are planned in consultation with the employees themselves in order to ensure that their own expectations are taken into account. The bank provides initial intensive training in the form of seminars for new recruits, as well as ongoing training measures for more



experienced employees. Most of the seminars are internally organised, but the bank has increasingly made use of external training seminars. The teaching of foreign language skills, in particular English, is a complementary training

measure designed to integrate key staff members into the international network of ProCredit Banks. Some of the staff members have also received training abroad at other institutions within our network. All of these training activities have resulted in the emergence of a core group of staff members distinguished by their ability to learn and to disseminate the culture of the institution through their initiative and sense of responsibility.

The dynamic and transparent corporate culture of our bank creates an environment in which people enjoy working, and our employees also have the satisfaction of working for an institution with a good public image. We will strive to ensure that this does not change in the future. At the end of 2003, the bank employed 508 staff members, whose average age was 27. The bank hired, trained and integrated more than 250 new staff members during the year. Thus, ProCredit Bank has one of the fastest-growing and youngest teams in the local banking industry.

ENVIRONMENTAL AND ETHICAL STANDARDS

In today's world, where public awareness of environmental and social issues is growing, a bank with an explicit developmental orientation must pay special attention to these issues. Therefore, ProCredit Bank has established an environmental management system (EMS) which sets forth its objectives in this area, namely:

- to provide financing only to environmentally and socially sound projects;
- to ensure borrowers' compliance with the national environmental, health and safety requirements; and
- to refrain from lending to borrowers engaged in activities which are socially questionable or ecologically harmful.

Complying with the EMS means that all loans are classified according to the environmental risk posed by the borrower's main economic activity. All loans considered to be of increased environmental risk are subject to an environmental assessment, which, depending on the findings, might lead to the rejection of the loan application. All employees who are responsible for compliance with environmental standards, in particular the designated environmental coordinator, receive regular instruction in environmental issues.

Three years after the start of its economic transition, Serbia has come substantially closer to Western ways of thinking and economic standards. Apart from the tangible changes, such as privatisation and deregulation, another sign of this is the increasing prominence of environmental issues in the public debate; consumers are starting to think about the quality of the surroundings in which they live. In this situation, the bank's environmental standards are an important contribution to greater environmental awareness, and encouraging entrepreneurs to think about these issues is an important aspect of the bank's developmental mission.

Finally, ProCredit Bank also regards the environmental standards as one of its risk management measures, because they avoid reputational risks for the bank and its shareholders on the one hand, and financial risks to its investments on the other.

As illustrated elsewhere in this report, ProCredit Bank does its utmost to work for the satisfaction of its customers and to support them in their economic activities by meeting their financial needs. Obviously, the quality of service we provide should be high enough to meet the expectations of demanding customers. However, ProCredit Bank closely monitors that this is achieved without departing from the formal and ethical framework which applies to sound banking operations and which ensures transparency in financial transactions. One of the most important rules is that the bank must not participate in transactions involving funds which may be suspected to have originated from criminal activities. The legal requirements for the prevention of money laundering are given special emphasis. The anti-money laundering compliance officer reports on a regular basis to the local authorities, and ProCredit Bank's operational modules are designed to detect and track suspicious transactions.

We pay very close attention to ensuring that our employees do not take improper advantage of their position in the bank. By the same token, employees are not permitted to handle transactions in which they themselves, or their relatives or friends, have a material interest. Employees who are in doubt concerning ethical questions are encouraged to contact their immediate supervisors. Our high ethical standards are reflected in the bank's Code of Conduct.



OUR CLIENTS

Publishing and Advertising



In 1994, Miroslav Gligorevic founded a small company named “Abak”. In the beginning, it was just his wife and himself, engaged in desktop publishing. As demand grew, he hired seven employees and added new services to his range, including the production of billboards and other advertising materials, the creation of websites, and the sale and maintenance of PCs and other office equipment. He was one of ProCredit Bank’s first loan clients in Nis. Up to now he has had three loans from the bank and is actively using a number of the bank’s services, both for his company and as a private individual. Here is what he has to say about his business and his relationship with our bank:

“It is very important, both for me personally and for my business, to be able to count on the bank’s financial support – especially these days, when it is hard to get paid and collect outstanding debts from my clients.”

Production of Plastic Bags



During the 1980s Mrs. Gorica Savic started a small business producing plastic bags, “Deni Commerce”. Today, her sons Dejan (33) and Nenad (28) are the owners of the company, which employs 45 people and has a 1,000 sqm factory for the production and printing of all kinds of plastic bags. The firm is an exclusive supplier of plastic bags for big companies such as Maxi Discont, Impex Promet, Tigar Pirot, Trajal, Soko Stark, Forma Bravo and Zitopek. Mrs. Savic says:

“I am very proud of this company. It means everything to my family and me.” Her son Dejan adds: “The rapid development of our company would not have been possible without your bank and the loans you have granted us.”

Florist



Slavica Tresac is an entrepreneur who started out with a good idea and plenty of enthusiasm: she began cultivating flowers in the garden of her house in the centre of Cacak. With a greenhouse of 64 sqm in the back yard, she began cultivating different kinds of flowers, some of them very rare. In order to expand her business, she decided to visit ProCredit Bank, having heard that this is the bank for small businesses. She quickly got a loan to finance the construction of an additional greenhouse.

Now she cultivates spring and summer flowers, selling them at the open market and also supplying many flower shops around the city. Since she now has a considerable number of clients, both wholesalers and retailers, she plans to open her own flower shop in the very near future with the financial support of ProCredit Bank.

Pig Farmer



Mr. Rajcanji Florian grew up in an agricultural family and has always worked to improve the farming methods employed on the family farm. Today, he specialises in breeding pigs.

ProCredit Bank supported Mr. Florian by granting four loans in the total amount of EUR 14,500. The first loan was used to repair his existing pig housing facilities. “

The second loan helped me to buy special pure bred pigs (Hampshire, German Pietrain, German York-shire), which will put me one step ahead of most of the other breeders”, says Mr. Florian. Other loans followed to help him to develop his production capacity by building new livestock breeding premises.

Agricultural Equipment



ZZ Visnja was founded in February 2002; at that time its main activity was maintaining a cherry orchard. Later that same year, in November, the company had an opportunity to start importing tractors from Belarus, and in a short period of time ZZ Visnja became one of the most important tractor dealers in the Serbian market.

ProCredit Bank signed a cooperation agreement with ZZ Visnja to provide financing to individual agricultural producers and agricultural firms wishing to purchase tractors from the company. So far ProCredit Bank has financed the purchase of 82 tractors. At the same time the bank supported the development of the company's tractor business directly by disbursing a EUR 100,000 loan to Visnja.

Stone Processing Workshop



Mr. Sente Nandor has been a private entrepreneur since 1973. After graduating from the Mechanical Engineering University he established "Mermer", a stone processing workshop for the making of monuments.

Ten years ago, he expanded his activities and has since become a major supplier of the stonework used in interior design. ProCredit Bank supported Mr. Sente's development with two loans in a total amount of EUR 78,000. The loans helped the client to renovate his business premises, which they divided into a production and a showroom area, to buy a new truck and to upgrade his machinery. A loan for working capital allowed him to purchase a large quantity of stone from Italy. Mr. Sente is now regarded as the leading stonemason in Subotica.

Production of Knitwear



“Ivkovič Knitwear” is a family company founded in 1986 in Sarajevo, Bosnia and Herzegovina, by Mrs. Danica Komnenič Ivkovič. It started as a design studio for the production of a small series of unique high-quality knitwear. In 1996 the Ivkovič family moved to Belgrade and consequently relocated their business to Belgrade as well. Nowadays the company has 20 employees, five retail shops and a huge production facility. The company has been a ProCredit Bank client since the beginning of 2003. So far they have taken out two loans and process all their payments through ProCredit Bank, and they have been using other banking services as well. Here is what the owners have to say about doing business with our bank:

“ProCredit Bank approved two loans for us at a time when we urgently needed the financial support, and the funds allowed us to finish construction work on our new production facility.”

Retail Customer



Dragana Tojagic is currently employed as a secretary. She uses most of the bank’s customer services for private individuals, such as direct deposit of salary, consumer loans, overdraft facilities and the YUBA Card. She has been a customer of ProCredit Bank for a year now, and is very pleased with the services provided:

“ProCredit Bank meets all my criteria in regard to customer service. The bank has responded promptly to all my requests. I am very grateful for the services the bank offers, and I am more than satisfied with what it has done for me so far.”

Retail of Household Appliances



Bato Komerc is a retail company selling TV sets, refrigerators, ovens, heaters and other electrical appliances. The founder, Mr. Bekir Dukadjinac, continued his father's line of business, and made it what it is today, a highly respected and solid company. In recent years, the company owned by the Dukadjinac family has undertaken major investments which have made the business profitable, allowing the family to accumulate a certain amount of private wealth.

“The main purpose of banks is not only to look after people's money, but also to support the business environment in which they operate. When ProCredit Bank opened its branch in Novi Pazar I realised that the bank has this mission. I was also pleased to see that ProCredit Bank extended loans to my compatriots. Therefore I entrusted my money to the bank,” says Mr. Dukadjinac.

Supermarket and Bakery



Mr. Ivan Jakovljevic started his own grocery business in 1991 after having served as a manager at a state-owned company for many years. The business did so well that he was eventually able to open two well-stocked self-service supermarkets. In 1999 he started a bakery production business, which initially produced only the baked goods needed for his supermarkets. Then he began opening bakery bistros, starting with two in favourable locations.

Now he owns two supermarkets, the bakery production business, four retail outlets which produce small quantities of pastry, and other business premises. All of the premises are very well equipped and stylishly decorated. The loan disbursed by ProCredit Bank was in the amount of EUR 125,000.

CONTACT ADDRESSES

Head Office Belgrade

29.novembra 68c
Tel. +381 11 20 77 906, fax +381 11 20 77 905
info@procreditbank.co.yu

Branch Belgrade I

Gospodar Jevremova 9
Tel. +381 11 3025 625, fax +381 11 3025 605
infobel@procreditbank.co.yu

Branch Belgrade II

Vojvode Milenka 38
Tel. +381 11 3617 533, fax +381 11 3613 399
infobel2@procreditbank.co.yu

Credit Office Pancevo

Djуре Djakovica 2
Tel. +381 13 520 051
infopan@procreditbank.co.yu

Branch Belgrade III

Bulevar Kralja Aleksandra 90, 2nd floor
Tel. +381 11 3370 802, Fax +381 11 3370 651
infobel3@procreditbank.co.yu

Branch Nis

Lole Ribara 19
Tel./Fax +381 18 547 845, +381 18 547 846
infonis@procreditbank.co.yu

Credit Office Pirot

Dobrice Milutinovica bb
Tel./Fax +381 10 311 959
infonis@procreditbank.co.yu

Branch Krusevac

Mirka Tomica 99
Tel. +381 37 418 490
infoks@procreditbank.co.yu

Branch Novi Sad I

Bulevar Osloбodjenja 58
Tel./Fax +381 21 444 160, +381 21 444 162

Branch Novi Sad II

Bulevar Cara Lazara 7b
Tel./Fax +381 21 458 942, +381 21 458 122
infonov@procreditbank.co.yu

Credit Office Becej

Mose Pijade 3
Tel./Fax +381 21 813 220, +381 21 814 480

Branch Subotica

Lenjinov park 8
Tel./Fax +381 24 554 548
infosu@procreditbank.co.yu

Credit Office Sombor

Vojvodjanska 22
Tel./Fax +381 25 26 480

Branch Cacak

Sindjeliceva 35
Tel. +381 32 226 556, Fax +381 32 228 336
infoca@procreditbank.co.yu

Branch Uzice

Dositejeva 4
Tel. +381 31 510 135, Fax +381 31 510 535
infoca@procreditbank.co.yu

Branch Kraljevo

Cara Lazara 44
Tel. +381 36 317 290
infokv@procreditbank.co.yu

Branch Kragujevac

Kralja Petra I 3
Tel. +381 34 302 175
infokg@procreditbank.co.yu

Branch Novi Pazar

Stefana Nemanje 54
Tel. +381 20 316 584, Fax +381 20 316 591
mfbnp@procreditbank.co.yu

Branch Novi Pazar

28 November 93
mfbnp@procreditbank.co.yu

Credit Office Prijepolje

Valterova bb
Tel./Fax +381 33 716 040

Branch Sabac

Cara Dusana 1
Tel. +381 15 360 050, Fax +381 15 360 022
infosab@procreditbank.co.yu