



# BAMC BUSINESS STRATEGY 2016-2022

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BUSINESS STRATEGY WAS PREPARED IN SEPTEMBER 2016 AND AMENDED IN DECEMBER 2016.

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## EXECUTIVE SUMMARY

### PREAMBLE

Bank Assets Management Company (hereinafter: BAMC) submitted its Strategy and Business Plan for the period 2015-2022 on a stand-alone basis in September 2015, which was then approved by the Government of the Republic of Slovenia (hereinafter: the Government) as its General Assembly on 6 October 2015. The strategy presented below is an amendment of that strategy, taking into account two fundamental changes that affected BAMC's operations at the beginning of 2016:

- The amendment of the Act Defining the Measures of the Republic of Slovenia to Strengthen Bank (hereinafter: ZUKSB), effective from 27 January 2016.
- The merger of two 100% state-owned banks (Factor banka d.d., Ljubljana – hereinafter: Factor banka and Probanka d.d., Maribor – hereinafter: Probanka) in orderly wind-down, into BAMC, on 19 February 2016 after revocation of their banking licence, with cut-off date 1 January 2016.

BAMC's strategy encompasses the acquisition, management and restructuring and cashing of non-performing assets acquired from Nova Ljubljanska banka d.d., Ljubljana (hereinafter: NLB), Nova Kreditna banka Maribor d.d. (hereinafter: NKBM), Abanka Vipava d.d., Ljubljana (hereinafter: Abanka) and Banka Celje d.d., Celje (hereinafter: Banka Celje), assets merged from Factor banka and Probanka, and exposures taken according to ZUKSB to strengthen its position and enhance value in individual cases.

During 2014 and 2015, BAMC concluded asset intake and the build-up of its organisation. By merging Factor banka and Probanka in the beginning of 2016, the organization substantially expanded and changed. New functional and process organization was introduced which fully supports effective management of additional assets merged by BAMC and requirements which were brought by amendments of the ZUKSB taking effect in 2016. Further changes and upgrades will be implemented continuously but BAMC is now a robust institution capable of delivering the results set out in this strategic plan. BAMC has well defined governance, supervision, policies, decision protocols and working procedures.

All of BAMC's activities are geared towards adding value to the Republic of Slovenia and its taxpayers in a broad sense. Such value creation covers not only the achievement of financial targets laid in ZUKSB and the Guidelines on the operations of the Bank Assets Management Company (hereinafter: the Guidelines), but also the indirect positive impact of strengthening the fundamentals of the Slovenian economy through successful restructurings and corporate governance improvements, and building up a knowledge base of distressed asset management which can be used beyond the boundaries of BAMC and even Slovenia.

## STRATEGIC TARGETS

The mission and main strategic targets of BAMC remain the same as defined in the last approved strategy.

### STRATEGIC GOALS OF BAMC ARE:

- financially: (1) to redeem the state guaranteed bonds issued to pay for the transferred assets, and (2) in addition, to generate the required return of the initially invested equity by the Republic of Slovenia,
- to manage assets intensively and invest in them so as to optimise their income-producing potential and disposal value,
- consistent with the previous objective, to act in the way which will aim to restructure companies if economically justifiable and to contribute to a renewal of sustainable activity in the property and other asset markets in Slovenia.

In the Guidelines the Government has set<sup>1</sup> Key Performance Indicator (hereinafter: KPI) targets under which BAMC is considered to operate in an economical, efficient and successful manner. These are presented below while a list of KPIs for the whole BAMC's lifespan and their definitions can be found in the Business plan summary (page 53).

TABLE 1: GUIDELINES-SET KPIs

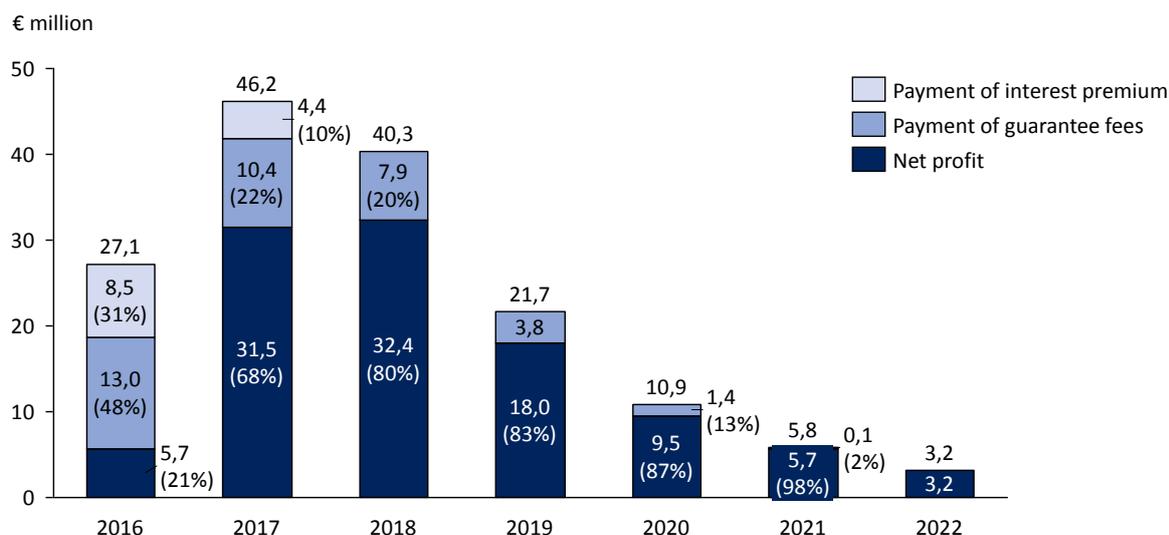
Key Performance Indicator	2017	2018	2019	2020	2021	2022
Minimum cumulative cash generated (in € million)	676	877	1.078	1.279	1.480	1.681
Cash generated %	10%	10%	10%	10%	10%	10%
EROE	8%	8%	8%	8%	8%	8%
Cost efficiency	1,9%	2,0%	2,0%*	2,0%*	2,0%*	2,0%*

NOTE: \*Cost efficiency KPI may change in years noted if BAMC's portfolio changes considerably.

As stipulated in the Guidelines, BAMC's goal is to generate an 8% ROE annually. However, in addition to that, it provided and provides, especially in the first four years of its existence, a guaranteed return to the Government and state-owned financial institutions in the form of guarantee fees and interest premium over government YTM rates (at the time of bond issues) paid on its debt. This is a cost for BAMC but revenue for the Slovenian public sector. Securing a high fixed return to the Republic of Slovenia through guarantee fees and interest premium will constitute a significant share of the total return in 2016 and 2017, while statutory ROE target component will gain weight with the gradual reduction of such financing costs in the later stages of the planning period (BAMC lifetime).

<sup>1</sup> New Guidelines on the operations of BAMC were accepted on 7 December 2016.

FIGURE 1: PLANNED STRUCTURE OF RETURNS PROVIDED BY BAMC



**NOTE:** BAMC pays an interest premium over the costs of financing for its primary issued bonds which are going to be fully repaid at the end of 2017.

In 2013, the Republic of Slovenia invested €203,6 million worth of share capital into BAMC. As shown in the table below, by mid-year 2016 BAMC realized a loss of €187,7 million through transactions where the transaction price was not negotiated but instructed by the decision of the owner – the Government – thus lowering BAMC equity to the level of €15,9 million (in other words, this was the real value of the de facto provided net capital). Because of this the Business plan includes a €50 million recapitalisation in the second half of 2016 which, together with an already performed €4,6 million recapitalisation of July 2016, increases the invested capital with corrections to €70,5 million, the level BAMC takes as a reference for its performance assessment.

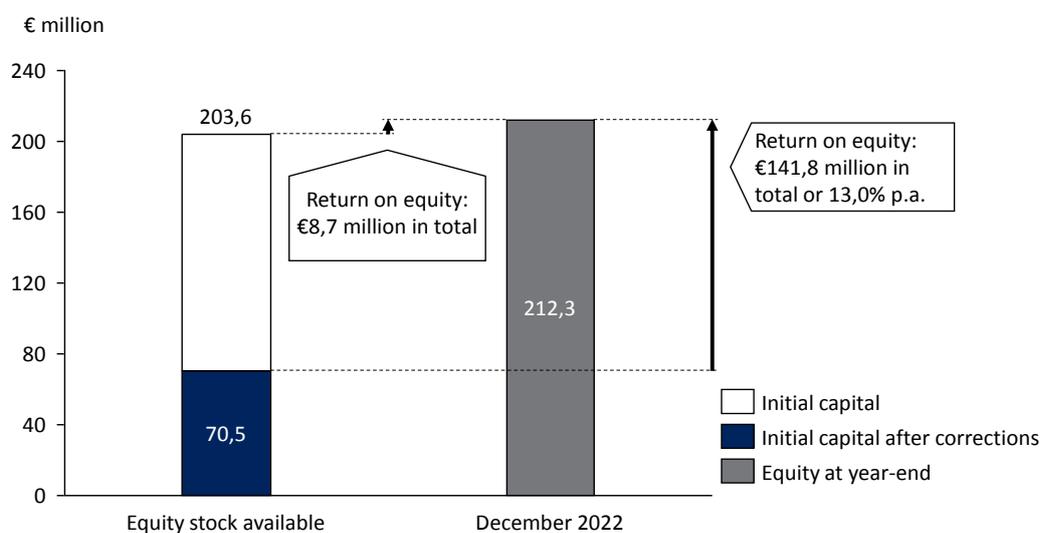
TABLE 2: CORRECTIONS TO INITIALLY INVESTED CAPITAL

in € million	BAMC equity effect
Capital invested by the Republic of Slovenia in 2013	203,6
<b>Cumulative capital returned to the owner in the 2013 – H1 2016 period</b>	<b>-187,7</b>
Transfers of non-performing assets from NLB, NKBM, Abanka and Banka Celje in 2013 and 2014	-110,1
Other transactions based on General Meeting decisions in 2014 and 2015	-5,4
Merger of Factor banka and Probanka into BAMC in 2016	-72,3
<b>De facto invested capital by H1 2016</b>	<b>15,9</b>
Recapitalisations in 2016	54,6
Realised recapitalisation in May 2016 (booked in July 2016)	4,6
Planned recapitalisation in H2 2016	50,0
<b>Initial capital with corrections (returns to the owner and recapitalisations)</b>	<b>70,5</b>

At the end of its lifespan, in 2022, BAMC projects to have equity in the amount of €212,3 million thus retaining the initial capital invested by the Republic of Slovenia in addition to the above mentioned guaranteed and incurred returns of capital to the owner during its operations. Taking all corrections into account BAMC projects to generate a 13,0% average yearly ROE (termed EROE) in its lifetime on the residual equity i.e., on the initial capital with corrections.

However, there are considerable risk elements associated with achieving this target. BAMC financial leverage is high and future results depend on a number of important restructurings. Furthermore, the expected return on equity is sensitive to the amount and timing of planned exits.

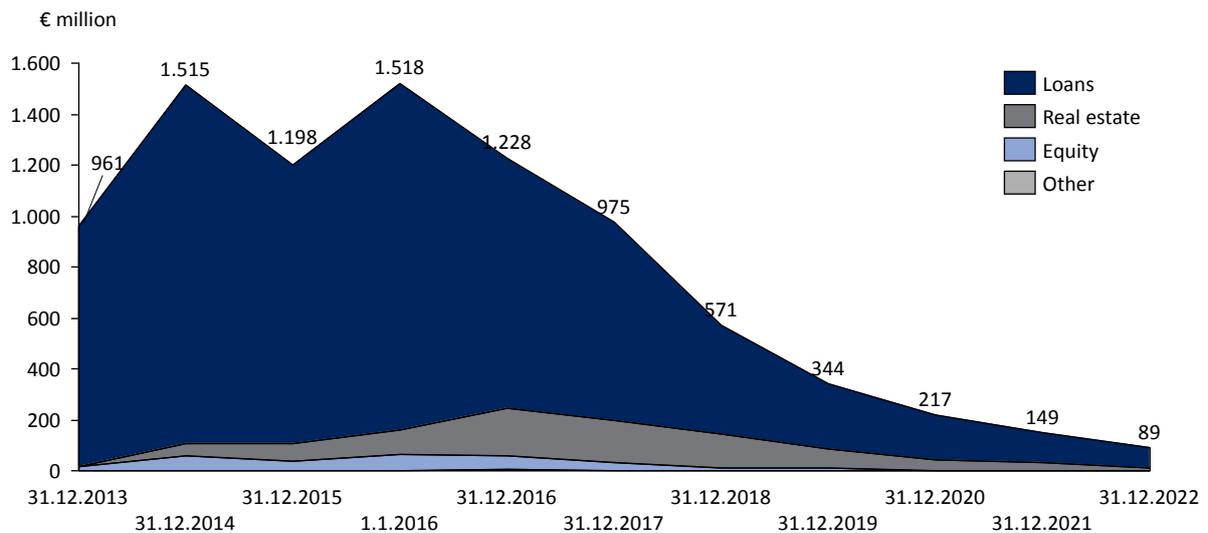
FIGURE 2: PLANNED FINANCIAL OUTCOME OF BAMC



**NOTE:** Corrections to initial capital include day-one losses and other revaluations related to acquisition of transferred assets, merger effects and recapitalisations. See Table 2 for details.

Loans will constitute the bulk of BAMC's assets throughout its life time. However, as repayments and refinancing of debt of successfully restructured companies will reduce the share of restructuring cases in the portfolio, the active management of own (repossessed) and collateralised real estate will gain importance over time.

FIGURE 3: ACTUAL AND PLANNED PORTFOLIO DEVELOPMENT



**NOTE:** BAMC will perform debt to equity swaps in cases where it is economically justifiable. The fair value of gained equity through debt conversion in most cases equals to zero since the enterprise value of the company after the conversion mostly still does not exceed the debt level of the company.

1. January 2016 displays the portfolio at the merger of Factor banka and Probanka into BAMC.

BAMC’s own financing will closely follow the cash flows from managing its assets and will minimise financing costs through tight liquidity management.

In the post-merger reorganisation process BAMC ensured to remain a lean and mean entity, favourably comparable in efficiency terms to its peers. The strategic target is to maintain such internationally competitive efficiency level, characteristic for every stage of its lifespan.

## IMPLEMENTATION

BAMC will implement its strategy in the following framework where all BAMC's activities are ultimately performed to add value for the Republic of Slovenia.

FIGURE 4: STRATEGIC FRAMEWORK



Striking the fine balance between profitability and faster cash generation (especially sales) is the key in simultaneous achievement of often conflicting targets. In BAMC's field of operations, there are several major directions where profit and cash flow generation may even strengthen each other, and therefore should enjoy special attention in strategy implementation in addition to the traditional focus of activities:

- Due to valuation specifics, accelerating real estate sales if the market can absorb them at reasonable prices.
- Making successfully restructured debtors bankable, ready for refinancing by banks.
- Sale of claims when reaching flattening curve of expected future results from restructuring.
- Applying new technics in a broader circle to accelerate repayments from improving operating cash flows of restructured debtors.
- Introduce new ways of financing/debt instruments to tightly adjust liquidity to incoming cash flows in order to minimise interest and state guarantee costs.

In order to secure the achievement of ambitious cash flow generation targets, BAMC will:

- Implement active external sales support activities: interactive websites, electronic media campaigns, build investor database for targeted offers, regular roadshows.
- Build an internal database and sales support platform for deal flow management, break down CF targets and backtesting to units/teams and individuals, develop a balanced scorecard including numerical targets for performance assessment and link the bonus system to target achievement.
- Preserve and enhance operational soundness by developing into a self-improving organisation.
- Establish internal forum for regular best practice sharing exercises.
- Execute a HR development plan based on knowledge matrix gap analysis, regular educational forums, prepare staff for gradual internal transformation or external job search.
- As part of its knowledge preservation and management program create “bad practice/good practice handbook” to share internally/with the broader financial community to avoid future problems.
- Complete financial crime detection program, manage defence lines actively and achieve at least the second Ethic Intelligence grade in prevention of corruption, implementing zero tolerance program against all sorts of malpractices and damages caused.

BAMC’s know-how in distressed asset management, processes, and IT solutions is ahead of ex-Yugoslav and most Eastern European countries, therefore value realisation opportunities through commercialisation of this know-how should be examined, in the Slovenian market and beyond.

The financial and non-financial targets and the implementation principles are detailed in the supporting strategies in the chapters of this strategy document.

## PRESENTATION OF BAMC

TABLE 3: BASIC COMPANY DATA

Full company name	Družba za upravljanje terjatev bank, d.d. Bank Assets Management Company	
Short company name	DUTB, d.d. BAMC	
Registered office	Davčna ulica 1, 1000 Ljubljana	
Telephone	+386 8 2054 235	
Fax	+386 1 4293 859	
E-mail	info@dutb.eu	
Website	www.dutb.eu	
Core business	Activities of collection agencies and credit bureaus	
Registration entry	2013/11708, District Court of Ljubljana	
Company ID number	6339620000	
Tax number	41251482	
VAT number	SI41251482	
Initial share capital	€208.235.000,00	
Number of shares	104.117.500 ordinary no-par value shares	
Board of Directors		Term ending on
Non-executive directors as at 15 December 2016	Marko Simoneti, Chairman of the Board	28 January 2017*
	Janez Širovnik, Deputy Chairman of the Board	31 December 2017
	Juan Barba Silvela	24 March 2021
Executive directors as at 15 December 2016	Imre Balogh, CEO	1 October 2021
	Janez Škrubej	31 December 2017
	Aleš Koršič	31 December 2017

**NOTE:** \*Due to resignation from his function the term of Marko Simoneti ends on 28 January 2017.

## CORPORATE GOVERNANCE AND ORGANISATIONAL STRUCTURE

BAMC has a one-tier system of corporate governance, where the highest decision-making body is the Board of Directors. Following the provisions of ZUKSB and the Articles of Association, the Board of Directors comprises four non-executive directors<sup>2</sup> and three executive directors. The Board of Directors has four committees: the Audit Committee, the Accreditation Committee, the Remuneration Committee and the Board Credit and Investment Committee. For the Audit, Remuneration and

<sup>2</sup> From 8 October 2015 onwards, Board of Directors comprised only two non-executive directors since Lars Nyberg was called-off from his position of member of Board of Directors and non-executive member Imre Balogh temporarily stepped into the position of CEO due to discharge of Torbjörn Månsson from the position.

On 24 March 2016 the Government in the capacity of the General Meeting of BAMC appointed Juan Barba Silvela as non-executive director for the period of five years from the date of appointment.

On 7 September 2016 the non-executive directors appointed Imre Balogh as the CEO of BAMC with his five-year mandate beginning on 1 October 2016.

Accreditation committees, the committee members comprise of non-executive directors and one external member with the relevant professional experience in Slovenia. The Board Credit and Investment Committee comprises of all Board members. The Board of Directors and its committees function in accordance with the relevant rules of procedure.

The ZUKSB amendments stipulated that the non-executive directors are appointed and recalled by the Government of the Republic of Slovenia and have powers of the supervisory board while executive directors are appointed and recalled by the non-executive directors. Executive directors are responsible for BAMC's day-to-day operations and non-executive directors are not involved therein.

In March 2016 the new Articles of Association, new Operational guidelines of DUTB and new Decree on the implementation of measures to strengthen the stability of banks entered into force. An overhaul of the applicable internal bylaws (e.g., Rules of procedure of the Board of Directors of BAMC, Rules of procedure on the work of Executive Directors, BAMC enlarged scope of new financing/asset purchase tools) took place in BAMC to bring them in line with the amended legislation, subsidiary regulations, and changed business circumstances following the merger of Probanka and Factor banka into BAMC.

The Board of Directors established the Executive Credit and Investment Committee and the Operative Credit and Investment Committee to decide on claims owned or managed by BAMC. The Board of Directors also established the Board Credit and Investment Committee in respect to just give consent to the decisions/proposals of Executive Credit and Investment Committee if necessary. With new decision-making committee structures in 2016 overlaps were eliminated and responsibilities are clear with more responsibility delegated to operative level while even strengthening the depth of decision-making and control on high volume/high impact cases.

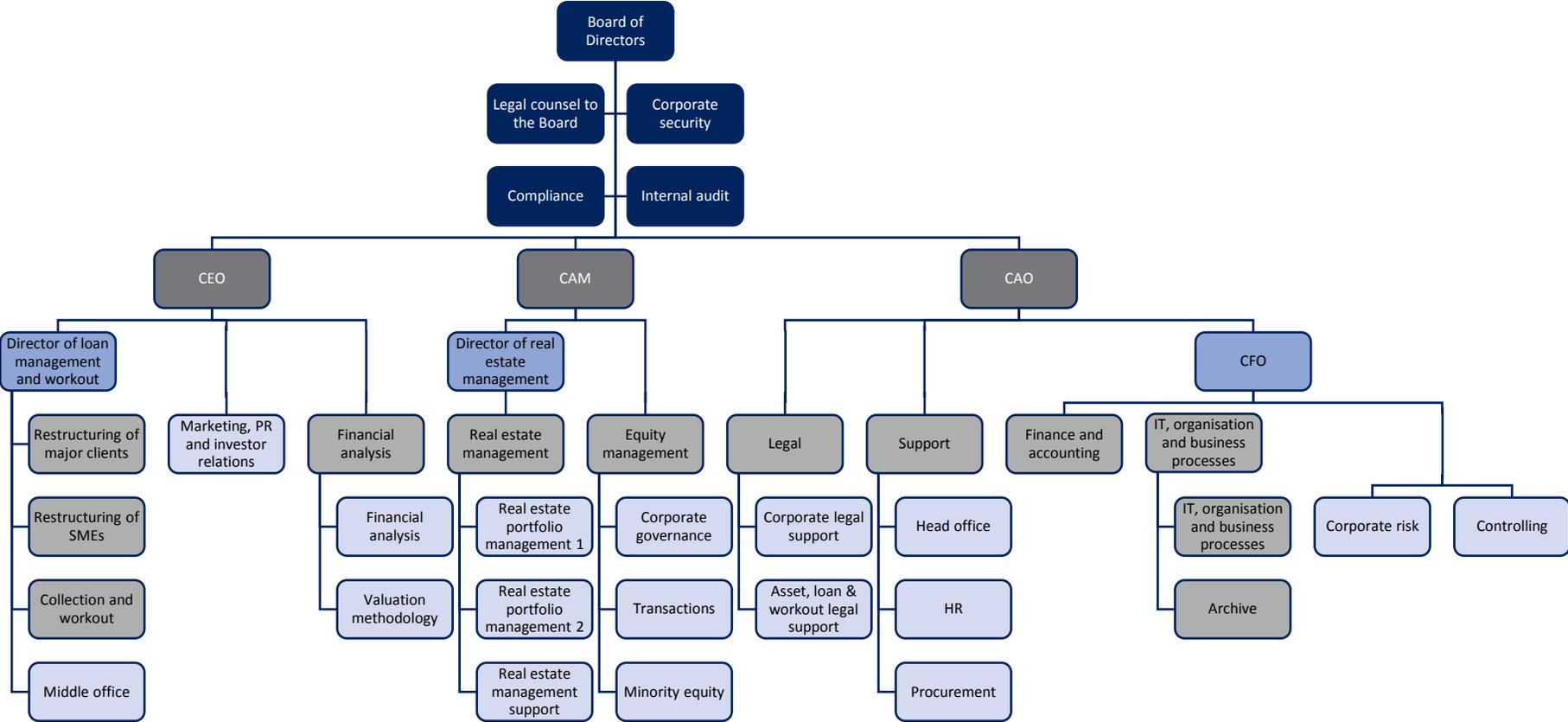
BAMC has an internal audit function that reports directly to the Audit Committee. In addition, Risk and Compliance Management Committee is supporting the work of the executive directors and this committee's reports are a standing item in each of BAMC's Board meetings.

#### FUNCTIONAL ORGANISATIONAL STRUCTURE

BAMC is organised to be effective in its mission, and in the achievement of the strategic objectives defined by the ZUKSB, the Government representing its owner and the Board of Directors. The functional organisational structure as illustrated in the picture below, is valid from July 2016. Reorganization made in July 2016 enables cost efficient operations of BAMC and continuous process optimization with clear goal to additionally increase the efficiency of BAMC's operations.

BAMC's core processes are performed in the loan management and workout division and the asset management division. The former consists of units specialised in exposure, complexity and profile of the debtors and the latter consists of a real estate management and an equity management unit. Credit and asset managers receive support from financial analysts and valuation review, the legal unit and middle office. Units are separated and independent which is ensuring suitable process controls.

FIGURE 5: ORGANISATIONAL STRUCTURE



## DECISION-MAKING SYSTEM

BAMC's decision-making system covers several levels and is adapted to ensure rapid, factual and effective decision-making with the aim of maximising the value of the company's assets.

Decisions relating to corporate governance are made by the Board of Directors, taking into account the opinions and recommendations issued by the Board committees. The Board of Directors also makes strategic decisions that relate to the transfer of assets and the funding of BAMC.

Strategic decisions that relate to the management of the loans, equity and real estate portfolios are also made by the Board. The Board adopted the Process and decision-making powers of the committees document where the structure of the credit and investment committees is defined as well as rules and procedures governing the work of these committees. BAMC has three credit and investment committees, one of each at the Board level, the executive directors level and at the operational level. The Process and decision-making powers of the committees document also defines authorisations and the hierarchy in the decision-making process, as well as the principles of corporate governance, which include a four-eye principle. Decision-making authorities, responsibilities and membership of committees are strictly segregated, without overlap between them. No decision can be made by a single individual.

Credit and investment decisions with lower importance are discussed and accepted at the operational level by Operational credit and investment committee consisting of one of the operational heads included in the asset management process. All other decisions are adopted by the Executive credit and investment committee. The most important credit and investment decisions adopted by the Executive credit and investment committee are subject of additional consent by the Board credit and investment committee. All decisions are documented. Executive directors and subordinated organisational units are fully responsible for the implementation of adopted Board decisions.

The appointment of directors at limited liability companies (which have no supervisory board) being restructured by BAMC is the responsibility of executive directors. Members of supervisory boards at companies being restructured by BAMC are appointed by the Board at the recommendation of the Accreditation Committee.

BAMC introduced changes in the decision-making system in the beginning of April 2016 as a response to changes in ZUKSB, merger process and changed structure of portfolio of assets under management. Completely renewed structure of credit and investment committees has eliminated the overlapping of responsibilities on Executive and Board levels. Now the Board Credit and Investment Committee is a consent-giving body to the most important decisions adopted by the Executive Credit and Investment Committee.

Limits between different types of credit and investment committees are clearly established, and participants at the specific levels of committees are clearly defined. Operational Credit and Investment

Committee now takes more operational decisions for cases with higher exposures and most of the decisions for cases with smaller exposures, while executive level committee still controls majority of larger exposures (80+% of total portfolio value altogether).

## AMENDMENTS OF ZUKSB

In attaining its strategic goals, BAMC was confronted with limitations and inconsistencies set also by other legislation, particularly in the field of insolvency legislation and legislation limiting the remuneration in state-owned companies. The Ministry of Finance started preparing amendments to the ZUKSB in 2014. BAMC played an active role in preparing a number of proposed amendments to the ZUKSB in 2015, addressing the most pressing obstacles in the implementation of BAMC's mission and strategic goals.

On 18 December 2015, the National Assembly passed the amendments of and supplementations to the ZUKSB, which took effect on 27 January 2016.

The key changes and new additions brought by the new ZUKSB are as follows:

- the law grants more powers to the Republic of Slovenia as the owner with regard to managing and supervising the operations of BAMC,
- the law introduces a new way of appointment and dismissal of non-executive and executive directors,
- the law restricts the role of non-executive directors with regard to managing the affairs of BAMC to the supervisory role, as held by the members of supervisory boards,
- the law expands BAMC's role in restructuring of debtors,
- the law grants BAMC new tools in restructuring of debtors,
- the law introduces restrictions for BAMC's managing equity of companies which the Government has classified as strategic investments,
- the law introduces additional restrictions and control mechanisms with regard to the management of BAMC assets (e.g., limitations to sale of assets to debtor-related parties),
- consolidation of companies in which BAMC has acquired a majority equity stake in the context of restructuring is not required,
- the law eliminates certain unnecessary and redundant provisions in the previously valid act, e.g. forming a Bank Stability Fund,
- the law grants the possibility of merging banks undergoing winding-down procedures,
- the law limits the mandate of Board members, appointed to their position before ZUKSB amendments came into effect, to 31 December 2017, and
- the law extends BAMC's lifespan by the end of 2022.

In accordance with the new ZUKSB the Government aligned and amended the Decree, Guidelines and Articles of Association with the new ZUKSB in March 2016.

## ORIGIN AND STRUCTURE OF ASSETS

In late 2013 the Government completed the recapitalisation of the two largest Slovenian banks, NLB and NKBM. The aforementioned banks transferred €3,3 billion in non-performing assets, primarily loans, to BAMC at a transfer value of €1.008,4 million in exchange for bonds issued by BAMC. BAMC's first step was to determine the initial fair value of acquired assets. The valuation process was completed in June 2014 and resulted in an initial loss recognition of €39,9 million.

In H1 2014, real estate with a transfer value of €11,6 million was received from NKBM and in H2 2014 BAMC received additional non-performing assets from Abanka and Banka Celje in exchange for additional issued bonds. Thus, €1.142,4 million of non-performing assets were transferred to BAMC from Abanka in October 2014 at a transfer value of €423,8 million and additional €392,2 million from Banka Celje in December 2014 at a transfer value of €125,7 million. After 2014 asset transfers from NKBM, Abanka and Banka Celje in BAMC estimated their initial fair values, following the valuation methodology used for first transfers as well. Fair value of assets taken over was €68,0 million or 12,1% lower than the transfer prices which resulted in initial loss recognition by BAMC.

### BAMC PAID €623 MILLION MORE FOR THE ASSETS THAN THE ESTIMATED MARKET VALUE

The EU estimated also the market value of the assets transferred under legislative directions, i.e. the price at which the banks could have sold the assets to a buyer other than BAMC. The difference between these market values and the transfer values is documented in EU state aid decisions regarding the four banks. The market values were estimated to be €623 million less than the transfer price.

In order to complement its exposures to certain debtors, in 2014 BAMC purchased claims (loans) totalling €172,9 million from Factor banka and Probanka in the amount of €38,6 million in arm's length transactions at negotiated prices.

### MERGER OF FACTOR BANKA AND PROBANKA INTO BAMC

On 19 February 2016, BAMC merged Factor banka and Probanka through the simplified merger process, based on Government decision.

The merger of Factor banka and Probanka into BAMC had some negative impact on BAMC's equity owing to the negative cumulative equity of the banks in the amount of €8,6 million. Due to this and possible need for additional revaluation of merged assets to initial fair value, BAMC has initiated that the owner, the Republic of Slovenia, will ensure additional capital thus enhancing BAMC's capital structure when and in the amount needed.

With the merger, the profile and composition of assets shifted towards a more granular and diversified portfolio, especially in the loan/claims section.

TABLE 4: CLAIM PORTFOLIO STRUCTURE FROM THE MERGER PERSPECTIVE

values in € thousand	BAMC 31 December 2015		Factor banka 1 January 2016		Probanka 1 January 2016		BAMC 30 June 2016	
Classification of borrowers	Number	Value	Number	Value	Number	Value	Number	Value
Gross exposure above €300 thousand	546	1.090.410	143	134.939	183	109.974	758	1.194.767
Gross exposure below €300 thousand	16	596	106	4.054	1.709	14.190	1.881	19.063
<b>Total</b>	<b>562</b>	<b>1.091.006</b>	<b>249</b>	<b>138.993</b>	<b>1.892</b>	<b>124.164</b>	<b>2.639</b>	<b>1.213.830</b>

NOTE: Gross exposure was assessed on a group level. Estimated claims include leasings.

With acquisition of the two banks, BAMC took over not only assets of acquired companies, but also over €369,0 million of obligations towards the Ministry of Finance from Factor banka and Probanka which originally matured in August and September 2016. In April 2016, BAMC made an early repayment of €150,0 million of aforementioned obligations and extended the maturity of remaining obligations by December 2016 when DUT02 bond matures as well. In August 2016, BAMC made another early repayment of €120,0 million to the Ministry of Finance, further reducing its debt.

## FUNDING STRUCTURE OF BAMC

The Republic of Slovenia paid in €208.235.000 of share capital in three tranches in 2013 and one in 2016. Majority of the equity was paid in government bonds (RS68 and RS38) while recapitalization in 2016 was paid in claims towards Cimos d.d. in the amount of €4,61 million. Merger of Factor banka and Probanka into BAMC in February 2016 did not change share capital.

BAMC financed its non-performing assets acquisition from four banks by issuing four bond issues in the total nominal amount of €1.563,2 million. After repaying the first bond issue in December 2015, and after merging additional obligations from Factor banka and Probanka, BAMC's financial obligations are as presented below.

TABLE 5: FINANCING CHARACTERISTICS AS AT 30 JUNE 2016

<b>Financing liability</b>	<b>Nominal value</b> (in € million)	<b>Coupon/ interest rate</b>	<b>Issued</b>	<b>Principal maturity</b>	<b>Interest payment</b>
DUT02 bond	505,8	4,50%	Dec 2013	Dec 2016	annually
DUT03 bond	424,6	1,50%	Oct 2014	Dec 2017	half-yearly
DUT04 bond	127,0	1,37%	Dec 2014	Dec 2017	half-yearly
NLB loan	200,0		Dec 2015	Dec 2017	quarterly
MF loan	198,4	1,20%	merged 2016	Dec 2016	monthly
SID banka loan	3,3		merged 2016	May 2018	half-yearly
PBS loan	0,2		merged 2016	Mar 2017	quarterly

**NOTE:** As some of the bonds were not "sold" (exchanged) at par value, their effective interest rate is somewhat higher. More precisely, DUT03 effective rate was 1,57% and DUT04 effective rate was 1,38%. Interest rates on commercial loans are not individually disclosed.

MF = Ministry of Finance, PBS = Poštna banka Slovenije.

BAMC is liable for the repayment of the liabilities with all its assets. In addition, all bonds are irrevocably and unconditionally guaranteed by the government. BAMC pays an annual guarantee fee to the government equal to 1,25% of the issue value. All bonds are acceptable as Eurosystem collateral, so banks that hold the bonds may use them to secure liquidity on favourable terms. NLB loan is also under subsidiary guarantee of the Government.

## BAMC'S MISSION AND STRATEGIC GOALS

### MISSION OF BAMC AS DEFINED IN THE GUIDELINES

BAMC's mission is defined in the Guidelines and in line with the mission the Board of BAMC has adopted BAMC's key objectives and strategic goals.

- Implement the measures to strengthen the stability of banks, adopted by the Government of the Republic of Slovenia.
- Promote trust in the financial system and operate by the rules of the business-financial profession and the highest ethical management standards, avoiding any conflict of interest.
- Implement a proactive, cooperative and holistic approach to the restructuring of companies.
- Being an active asset owner.
- Manage the assets in a way that would allow exiting at the best possible price.

### KEY OBJECTIVES AND STRATEGIC GOALS OF BAMC

BAMC's financial goal is to maximize the return to state and ultimately to the taxpayer and in this respect:

- (1) redeem the state guaranteed bonds issued to pay for the transferred assets, and (2) in addition, generate the required return on the initially invested equity by the Republic of Slovenia.
- Consistent with the previous objective, act in the way which will aim to restructure companies when economically justifiable and to contribute to a renewal of sustainable activities in the property and other asset markets in Slovenia.
- Manage assets intensively and invest in them so as to optimise their income-producing potential and disposal value.

For effective monitoring and reporting, the Government and BAMC have defined a set of Key Performance Indicators, i.e. KPIs. These KPIs provide a starting point for BAMC's strategic and financial planning and are presented in the Business plan summary (page 53).

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**STRATEGIES TO ADD VALUE TO MANAGED ASSETS**


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<b>Overall imperatives</b>	BAMC continues its operations as a non-performing asset manager of international standing
	Acceleration of restructuring and transformation from being predominantly a claim manager to becoming a predominantly real estate manager
	Value maximising, unbiased, fact-based case strategies and action planning and transparent, professional decision-making
	Asset management with the recognition of BAMC as only a temporary owner – ensuring BAMC’s assets are marketable at all the time
	Active use of additional means provided by ZUKSB
	Competitive, professional and transparent exiting processes
	Efficiency in operations
	Excellence in designing and executing BAMC’s internal processes
	Zero tolerance towards corruptive and unlawful practices
<b>Management of restructuring and majority equity stakes</b>	BAMC is maximizing enterprise value (meaning debt and equity together) of restructuring cases where this strategy is economically justified
	Maximisation of sales results
	BAMC aims to keep control over the debtor’s cash flow in cases where BAMC is the economic owner
	BAMC will maximize the value of its exposures in financial holdings by ensuring viable operations of their subsidiaries
	BAMC will provide liquidity to restructuring cases where it is commercially justifiable and the debtor is not yet bankable
	BAMC will charge interest rates above market level thus incentivising owners of the debtors to refinance at least part of expensive debt with less expensive financing on the banking market
	BAMC initiates, assists and monitors operating restructuring of debtors
BAMC will complement individual case strategies by bundling assets into portfolios	
<b>Management of recovery situations</b>	In cases where BAMC determines that the debtor as a going concern is no longer viable, and where no commercially (and legally) acceptable offer for BAMC’s exposure is available, BAMC will initiate bankruptcy proceedings against the debtor
	BAMC will decide for the disposal of operating companies’ assets where taking control over the company is not prudent or even possible
	Pursuing recovery strategy for viable companies when restructuring is effectively not possible due to non-cooperation of the debtor
<b>Management of performing loans toward individuals and micro companies</b>	BAMC will create packages of loans and sell them to commercial banks or other interested investors
<b>Management of leasing contracts</b>	BAMC will create packages of leasing contracts and sell them to leasing companies or other interested investors
<b>Management of minority non-strategic equity stakes</b>	BAMC will execute a transparent and optimal exit for each directly owned minority shareholding

**Management of real estate**

BAMC will take over collateralised real estate where economically justifiable

BAMC will ensure value protection and value enhancement through facility management

BAMC will add value to its real estate through a wide range of marketing activities

BAMC will use rental options to optimise the combined yield and exit value from real estate

BAMC will not be a real estate developer but may invest in completion of almost finished projects

If deemed advantageous, BAMC will create real estate portfolios with distinct risk and return profiles

Selecting optimal selling technique and process in bankruptcy procedures

Competitive and transparent exiting process

Termination exit strategy

## OVERALL IMPERATIVES

### *BAMC CONTINUES ITS OPERATIONS AS A NON-PERFORMING ASSET MANAGER OF INTERNATIONAL STANDING*

In the three years since its establishment, BAMC has put in place an effective management mechanism not just for non-performing loans but also for other types of non-performing assets that were a burden on the banks' balance sheets. BAMC has:

- qualified expert managers of non-performing loans, equity and real estate,
- established processes for effective management of non-performing assets, and
- the necessary restructuring competences (financial and operational) to take on and successfully resolve complex case situations.

The processes are easily scalable and supported effectively, partly by in-house and partly by outsourced solutions.

However, BAMC has the ambition to become an organisation with operations that have a value exceeding the value of its assets. This should provide the owner, the Government of the Republic of Slovenia, with the flexibility to utilise BAMC for further non-performing loan resolution.

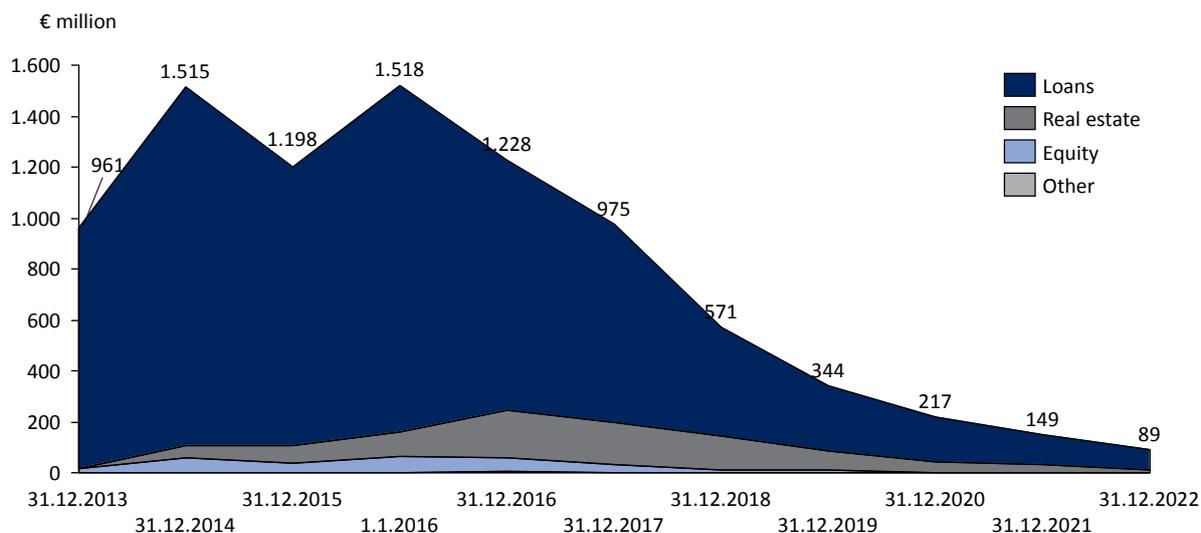
With a fully functioning organisation, robust management and decision processes, full understanding of its assets, clearly defined value creation strategies and a track record of solid results BAMC intends to be the best choice of manager (integrator) for the remaining synergistic, non-performing assets left in the balance sheets of the banks in the Republic of Slovenia and their subsidiaries in the Republic of Slovenia and abroad. Transferring additional non-performing assets to BAMC could in many cases create positive synergies. Furthermore, economies of scale could potentially improve the cost efficiency of the asset management process.

### *ACCELERATION OF RESTRUCTURING AND TRANSFORMATION FROM BEING PREDOMINANTLY A CLAIM MANAGER TO BECOMING A PREDOMINANTLY REAL ESTATE MANAGER*

Current focus of BAMC is to ensure accelerated restructuring of its exposures in the corporations that are going-concerns and are deemed to be commercially viable if successfully restructured. By the end of 2017, BAMC will have to successfully restructure the majority of its portfolio. A continued reorganisation of BAMC's cases, such as case manager specialisation and creation of portfolios of similar assets, is planned and will be executed on. This will ensure that necessary resources and focus are allocated to each restructuring case.

Loans will constitute the bulk of BAMC's assets throughout its life time. However, as repayments and refinancing of debt of successfully restructured companies will reduce the share of restructuring cases in the portfolio, the active management of own (repossessed) and collateral real estate will gain importance over time.

FIGURE 6: ACTUAL AND PLANNED PORTFOLIO DEVELOPMENT



**NOTE:** BAMC will perform debt to equity swaps in cases where it is economically justifiable. The fair value of gained equity through debt conversion in most cases equals to zero since the enterprise value of the company after the conversion mostly still does not exceed the debt level of the company.

The value of loan portfolio is heavily based on successful real estate collateral management.

1. January 2016 displays the portfolio at the merger of Factor banka and Probanka into BAMC.

Depending on the changes in the share of specific types of assets in its portfolio, BAMC will further adapt its organizational structure and processes. The details of how the staff structure and IT architecture is expected to change over time are presented in the Organisational strategies chapter.

#### *VALUE MAXIMISING, UNBIASED, FACT-BASED CASE STRATEGIES AND ACTION PLANNING AND TRANSPARENT, PROFESSIONAL DECISION-MAKING*

Following the acquisition of an asset, typically a loan, BAMC performed a detailed analysis, initially for the exposure to a specific company and then for the exposure to an entire business group, if the exposure belongs to such a group. The analysis includes:

- an assessment of the debtor's ability to repay liabilities over the medium-and long term from cash flows or divestment opportunities,
- the legal framework that would facilitate the maximum repayment of a claim,
- the debtor's willingness to search for a mutually acceptable solution, and
- other circumstances that may affect the repayment of BAMC's claim.

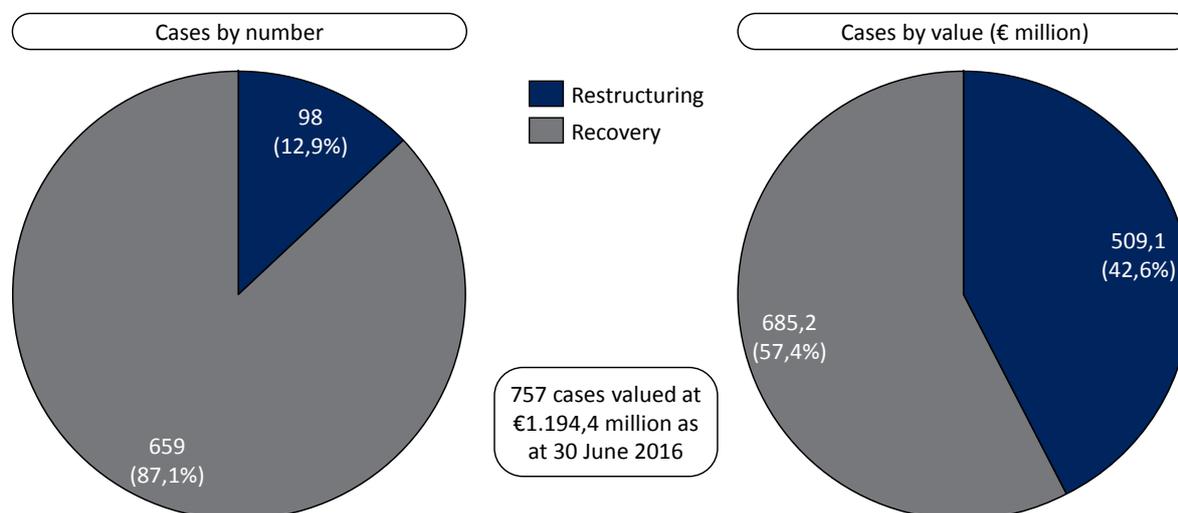
Based on the analysis, an internal asset valuation is preformed, which provides the basis for the selection of a relevant asset management strategy for the acquired assets. BAMC selects either a restructuring strategy or a recovery strategy.

BAMC opts for a restructuring strategy whenever it assesses that financial and operational restructuring measures will improve a debtor's operations to such an extent that it will achieve a higher rate of repayment than if it recovered debt from the debtor through the liquidation of pledged collateral. BAMC's objective in the restructuring of a company is to ensure the long-term efficiency and

viability of the debtor's operations and its competitiveness, and to maximise the repayment of debt with cash flows from operations. Therefore, financial restructuring is also linked to business or operational restructuring, which may involve the sale of the company's obsolete assets and/or lines of business.

In case of loss-making companies against which BAMC holds claims, when it is clear that it would be impossible to create greater value through financial and operational restructuring than through recovery of collateral, BAMC's actions as a prudent and diligent manager dictate that it opts for the recovery strategy. A recovery strategy is also used in the case of companies against which bankruptcy proceedings had already been initiated before their transfer to BAMC. It has to be noted that this was the case in a substantial number of companies transferred (more than half of recovery classified cases).

FIGURE 7: LOAN PORTFOLIO BY STRATEGY



**NOTE:** The figure does not include gross exposures under €300 thousand on a group level.

BAMC will continue to invest in its decision-making processes to further ensure their robustness, transparency and effectiveness by selective introduction of IT-solution support. This is further described in the Organisational strategies chapter.

*ASSET MANAGEMENT WITH THE RECOGNITION OF BAMC AS ONLY A TEMPORARY OWNER – ENSURING BAMC'S ASSETS ARE MARKETABLE AT ALL THE TIME*

Based on its mission outlined in the ZUKSB, BAMC is a project company whose purpose is to ultimately sell all the assets that were transferred to it. According to the ZUKSB, BAMC is required to provide cash generation of at least 10% of transferred assets' appraised value every year.

BAMC is prepared to sell any asset as soon as it has received a substantiated bid from an eligible acquirer that is exceeding the estimated value of the asset that BAMC believes it can generate from continued ownership. Any sale will be executed in a competitive and transparent sale procedure. To support the decision-making, BAMC will perform regular valuations of all its assets using an internal valuation method, attested to and approved by external experts and auditors.

#### VALUATION OF ASSETS

BAMC assesses the fair value of assets using an internal asset valuation methodology that was verified by external auditor.

Most of the value in BAMC's portfolio is driven by the value of the underlying assets, that is mainly pledged real estate and equity. The valuation of these assets is done based on the valuation methods which are also widely used by external valuers, i.e. mainly income and market approach. The discount rates used in this context reflect the estimated cost of capital for an average market investor.

The valuation of loans with a restructuring strategy is based on the binominal real option pricing model. In addition to the main restructuring scenario collateral values are also considered as an exit option. These are a safety net representing the outcome in case of restructuring failure. The riskiness of the loan is taken into account through the probabilities of the two scenarios instead of the discount rate. As the risk is accounted for separately, the discount rate in this context represents only the time value of money for BAMC.

The assessed fair values of assets represent one of the key quantitative information inputs that BAMC takes into account when adopting decisions.

#### *ACTIVE USE OF ADDITIONAL MEANS PROVIDED BY ZUKSB*

ZUKSB changes that came into effect in January 2016 have, together with clarifying and increasing BAMC governing mechanisms exercised by the Government, vested additional formal powers to BAMC in order to better pursue and fulfil its mission. The most notable of these are:

- granting new loans towards existing debtors,
- purchase of additional claims towards existing debtors, and
- refinancing of restructured debtors by cooperating banks.

Although BAMC had legal grounds to act and perform the above mentioned actions already based on the existing other legislation and has in the interest of maximization of the value used them before, BAMC will continue to use these instruments where economically justifiable with the aim of increasing its expected return from the specific debtor.

#### *COMPETITIVE, PROFESSIONAL AND TRANSPARENT EXIT PROCESSES*

BAMC has developed clear policies on how to ensure that its exit processes are competitive, professional and transparent. The guiding key principles are to ensure that the optimal price is being achieved from an eligible acquirer. BAMC will also strive to enhance Slovenia's position as being an investor friendly environment by managing its exit processes professionally.

Credit management performs control of the exit process in order to comply with the restriction to avoid selling exposures back to the original debtors. BAMC's consideration of proposed exit terms will be on strict commercial grounds to avoid any potential illegal state aid provisions. BAMC is state-owned and as such any non-commercial consideration without prior consent of the relevant competition authority would likely be considered as illegal state aid.

#### *EFFICIENCY IN OPERATIONS*

BAMC strives to ever improve the efficiency of its operations. Therefore it regularly follows the achievement of its strategy goals and thresholds set by the owner. Moreover, BAMC benchmarks itself to the most known European bad banks based on their published annual data.

Internally, the balanced scorecard framework is being set up with the aim of quantifying and following the effectiveness of BAMC's specific processes and functions.

TABLE 6: BALANCED SCORECARD FRAMEWORK

<b>Organisational unit</b>	<b>Broad criteria description</b>
BAMC as a whole	KPIs as defined by the owner and the Board
All functions	On-time and in-budget completion of projects Factual vs. planned cash flows and sales activities
Credit and equity management	Attaining required return Compliance with credit decisions
Real estate management	Attaining goals in sales/renting and costs Supporting collateralised credit management results
Legal	Success in legal disputes Supporting and sharing credit and asset management results
Middle office	On-time and correct submission of booking requests On-time closing of inflows Supporting and sharing credit and asset management results
Valuations (credit, real estate and equity)	On-time completion of valuations Minimising subsequent amendments following review/audit
Finance	Adequate financing/refinancing procedures Accurate and secure payment functions Management of liquidity reserves
Accounting	On-time reporting of accounts for internal and external users Prompt booking of business events
Controlling	On-time internal and external reporting
IT	Uninterrupted operations of systems On-time internal applications development
Compliance	Ensuring compliant operations of the company
Internal audit	Yearly plan realisation

*EXCELLENCE IN DESIGNING AND EXECUTING BAMC'S INTERNAL PROCESSES*

BAMC is constantly improving its internal processes, particularly in the fields of:

- legal procedures in managing cases,
- sales procedures,
- procurement procedures (in line with Law on public procurement), and
- other internal processes with special focus on prevention of operational risks.

*ZERO TOLERANCE TOWARDS CORRUPTIVE AND UNLAWFUL PRACTICES*

BAMC employees are strictly monitoring and reporting all criminal suspicious or illegal activities of debtors or lenders which resulted in non-performing loans or a reduction of BAMC's exposure value. A separate internal investigation function has been established with the aim of strengthening this field ever further.

Zero tolerance will also be exercised in case of internal fraud, corruption, damages caused by intentional wrong-doing, gross negligence, unauthorized usage or disclosure of confidential information, or any other malpractices.

## MANAGEMENT OF RESTRUCTURING CASES AND MAJORITY EQUITY STAKES

*BAMC IS MAXIMIZING ENTERPRISE VALUE (MEANING DEBT AND EQUITY TOGETHER) OF RESTRUCTURING CASES WHERE THIS STRATEGY IS ECONOMICALLY JUSTIFIED*

In the context of financial restructuring, BAMC ensures capital adequacy and solvency through debt-to-equity swaps, disposal of non-strategic real estate and other non-core assets, or write-offs. In cases where other creditors are present BAMC usually closely cooperates with these creditors in line with the general principles adopted by the Bank Association of Slovenia. In cases where it is the largest creditor, BAMC is taking a leadership role in creditor consortiums.

### *MAXIMISATION OF SALES RESULTS*

BAMC is maximising sales proceeds via joint sales of equity and debt positions. In order to maximise the enterprise value, BAMC might also form joint ventures with interested investors in competitive processes or maintain minority equity stakes or other earn-out options for future upsides.

*BAMC AIMS TO KEEP CONTROL OVER THE DEBTOR'S CASH FLOW IN CASES WHERE BAMC IS THE ECONOMIC OWNER*

The free cash flow generated by the debtor is a key resource for debt servicing, repayment and generating residual debtor value. When BAMC decides to restructure the debtor, it is therefore essential that the debtor's management will:

- be able to maximize the debtor's free cash flows,
- act in the company's interest, i.e. in the interest of the debtor's economic owner (BAMC) and that it will not steer the free cash flows to fit the interests of other interest groups (e.g. the formal owners and the related parties).

BAMC wants to have its own trusted agent in companies subject to restructuring efforts, reducing the so-called agency costs. BAMC will therefore seek to lower agency costs in companies where it acts as the economic owner by appointing trustworthy professionals in the debtors' supervisory and management boards, or it will appoint a procurator in such companies.

BAMC will enter into the direct ownership of restructured companies via debt-to-equity swaps when:

- this will provide capital adequacy and sustainable debt to the debtor,
- this is the most efficient or the only way to lower agency costs,
- entering into the ownership structure will improve BAMC's options for maximizing the value of its investment in the debtor,
- the risks involved in entering into the ownership structure do not exceed the expected benefits.

*BAMC WILL MAXIMIZE THE VALUE OF ITS EXPOSURES IN FINANCIAL HOLDINGS BY ENSURING VIABLE OPERATIONS OF THEIR SUBSIDIARIES*

The value of the financial holdings lays in the value of their investments which are in many cases operative companies. Although BAMC has in general received the exposure only towards the financial holdings (suboptimal from the value maximization point of view and contrary to BAMC's preference)

rather than the whole group, including the daughter companies which are generating cash flows, it is in BAMC's interest that the operative companies are performing well and thus the possibility of repayment on the holding level is increased, which can be achieved through various legal means.

*BAMC WILL PROVIDE LIQUIDITY TO RESTRUCTURING CASES WHERE IT IS COMMERCIALY JUSTIFIABLE AND THE DEBTOR IS NOT YET BANKABLE*

By definition, mainly non-performing assets were transferred to BAMC. At the time of the transfer, the debtors were over-indebted, usually insolvent and burdened with capital inadequacy. This is also the case for companies where BAMC pursues a restructuring strategy. In cases where BAMC opts for financial restructuring of the debtor, BAMC will aim at restructuring the debtor's financial liabilities so that the debtor will have sufficient capital adequacy and ability to meet its financial obligations. As a rule, this means that after the restructuring of cash flows has been arranged by signing a contract, the debtor will once again be able to acquire additional liquidity on the market to finance its operating capital and make urgent investments required to stay in business or restart its operations.

In some cases where BAMC pursues a restructuring strategy, the debtors may be unable to access bank financing to fund their immediate working capital needs or urgent capital expenditures. This is not unusual in cases where financial restructuring has not yet been agreed or the restructuring process has not yet commenced. Even in other cases banks may be insisting on BAMC participation. Inability to access credit may put the indebted company's survival at risk, and therefore also the execution of the restructuring strategy.

In such cases, BAMC can provide the debtor with the necessary liquidity in the form of a loan or additional capital, depending on which option proves to be more viable. Before doing that, BAMC must have:

- ascertained whether providing the necessary liquidity is indeed urgent and
- ensured control over the debtor's cash flows.

*BAMC WILL CHARGE INTEREST RATES ABOVE MARKET LEVEL THUS INCENTIVISING OWNERS OF THE DEBTORS TO REFINANCE AT LEAST PART OF EXPENSIVE DEBT WITH LESS EXPENSIVE FINANCING ON THE BANKING MARKET*

BAMC will manifest this pricing policy in cases where BAMC is not the prevailing owner of the debtor's equity when:

- restructuring existing debt (MRAs),
- providing new lending.

*BAMC INITIATES, ASSISTS AND MONITORS OPERATING RESTRUCTURING OF DEBTORS*

In addition to financial restructuring, most of the debtors undergoing a restructuring process also need operational restructuring. It is not enough to deleverage the debtor and adjust the financial outflows in the debt servicing options; it is also necessary to initiate changes to increase the cash flows from operations.

BAMC has a limited capacity of in-house industry specialists, who could assist the debtors' managements in the operational restructuring efforts. BAMC will provide assistance and advice in seeking out the best experts (domestic or international), who might assist the debtor's management staff in the execution of operational restructuring.

BAMC will always directly supervise the progress of operational restructuring and its effects. It will do so either by appointing procurators in the debtor companies, by appointing members in supervisory boards, or by directly tracking progress through the involvement of BAMC's case managers.

In all cases where BAMC is a major economic owner (through equity or debt) BAMC will exert decisive influence on the corporate governance of the debtor.

*BAMC WILL COMPLEMENT INDIVIDUAL CASE STRATEGIES BY BUNDLING ASSETS INTO PORTFOLIOS*

There is a high degree of uniqueness and complexity in most of the cases BAMC manages. To optimise the value for BAMC, strategies and exit options have to be developed, assessed and decided on in each case.

Portfolios may enable more effective value creation and will likely attract more interest from investors with targeted investment strategies or - which is common for international investors - with minimum sums to invest.

Creating portfolios that have a specific risk return profile may enhance value. Examples include portfolios in the fields of retail, parking, hospitality/hotels, residential real estate and commercial real estate.

Such portfolios can be formed inside BAMC or within a special legal entity ("SPV"). SPVs will be managed by the same principles and rules as BAMC and BAMC's credit and investment committees will be authorized to handle the SPVs' asset management decisions.

## MANAGEMENT OF RECOVERY CASES

*IN CASES WHERE BAMC DETERMINES THAT THE DEBTOR AS A GOING CONCERN IS NO LONGER VIABLE, AND WHERE NO COMMERCIALY (AND LEGALLY) ACCEPTABLE OFFER FOR BAMC'S EXPOSURE IS AVAILABLE, BAMC WILL INITIATE BANKRUPTCY PROCEEDINGS AGAINST THE DEBTOR*

In bankruptcy proceedings, the bankruptcy trustee, who will monitor and supervise the selling process, is playing the most important role. BAMC will involve itself in, or lead, the creditors' committee, where it will keep close watch over the administration of bankruptcy proceedings and disposal of the bankrupt creditor's assets.

Where appropriate, BAMC will seek to actively support the activities set forward by the bankruptcy trustee, especially concerning assets collateralised to BAMC. When it is estimated that BAMC can add value to collateralised assets, and where BAMC has a legal and commercially justifiable ground to do so, BAMC will seek to take over the assets and sell them on its own.

*BAMC WILL DECIDE FOR THE DISPOSAL OF OPERATING COMPANIES' ASSETS WHERE TAKING CONTROL OVER THE COMPANY IS NOT PRUDENT OR EVEN POSSIBLE*

BAMC will opt for the disposal of pledged collateral and other assets in operating companies where cash flows from ongoing operations will not suffice for repayment, or in cases where the company management and/or shareholders are not willing to cooperate constructively in finding a solution for debt repayment. The manner of the sale and the procedure involved depend on the type of asset and the legal characteristics of the collateral. In disposing of collateral, BAMC will engage in necessary judicial recovery and other judicial proceedings, as well as out-of-court procedures. In some cases, BAMC may decide to purchase or acquire assets and thereby settle its claims, either partially or in full.

BAMC may find it advantageous to sell a claim along with the collateral to a third party, who will then continue the on-going recovery proceedings. In particular, BAMC will seek to sell promptly when it deems that immediate payment would be a preferable solution to the lengthy recovery process involving the disposal of assets through court and other proceedings.

*PURSUIING RECOVERY STRATEGY FOR VIABLE COMPANIES WHEN RESTRUCTURING IS EFFECTIVELY NOT POSSIBLE DUE TO NON-COOPERATION OF THE DEBTOR*

There are situations where BAMC is the economic owner of the debtor, but the existing owner is preventing the execution of activities which would maximize the value of BAMC's repayment and court-related procedures also do not enable pursuit of maximal repayment. In such cases, BAMC may opt for immediate sales or initiating insolvency procedures/enforcement thereby maximizing the value of its claim and in many cases also the claims of other creditors.

#### MANAGEMENT OF PERFORMING LOANS TOWARD INDIVIDUALS AND MICRO COMPANIES

##### *BAMC WILL CREATE PACKAGES OF LOANS AND SELL THEM TO COMMERCIAL BANKS OR OTHER INTERESTED INVESTORS*

In the process of merging Factor banka and Probanka, BAMC has received a portfolio of retail loans towards micro companies and natural persons. As these are numerous and small exposures not in line with BAMC's purpose of operations, BAMC will bundle loans into offers interesting to banks or other investing entities.

#### MANAGEMENT OF LEASING CONTRACTS

##### *BAMC WILL CREATE PACKAGES OF LEASING CONTRACTS AND SELL THEM TO LEASING COMPANIES OR OTHER INTERESTED INVESTORS*

In the process of merging Factor banka and Probanka, BAMC has also received a performing leasing portfolio. As this is not BAMC's core business, BAMC will offer bundles of such contracts to leasing companies or other investing entities.

#### MANAGEMENT OF MINORITY NON-STRATEGIC EQUITY STAKES

##### *BAMC WILL EXECUTE A TRANSPARENT AND OPTIMAL EXIT FOR EACH DIRECTLY OWNED MINORITY SHAREHOLDING*

Minority ownership stakes were also transferred to BAMC with no credit exposure. In many of these cases the previous owners (banks) had been unsuccessful in finding acceptable exits.

Taking into account existing regulation (ZGD-1, Zpre-1) regarding corporate governance rights of minority shareholders, there are no fast and easy ways to exit minority ownership positions<sup>3</sup>.

Different approaches will be considered, including:

- Proposing to the majority owners to acquire BAMC ownership share,
- Proposing to the majority owner and management of the company to form a treasury shares fund by the company itself,
- Searching for interested investors in cooperation with other owners
- Improving the attractiveness by cooperating with other owners

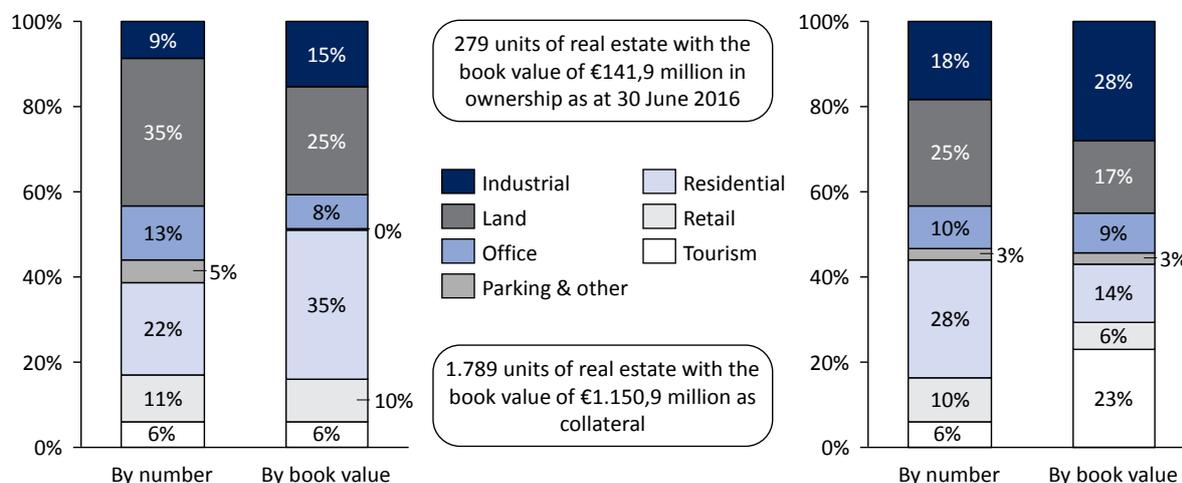
In equity investments which are important or strategic to the owner of BAMC, BAMC will offer these stakes in competitive sales processes to Slovenian Sovereign Holding (hereinafter: SDH) or the workers in accordance with ZUKSB.

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<sup>3</sup> Except cases where majority shareholder owns more than 90% of the company.

## MANAGEMENT OF REAL ESTATE

FIGURE 8: REAL ESTATE PORTFOLIO BY REAL ESTATE TYPE



**NOTE:** Values of the real estate collateral portfolio do not take into account ranking and mortgage sizes related to loans, but only present the value of real estate pledged as any collateral.

### *BAMC WILL TAKE OVER COLLATERALISED REAL ESTATE WHERE ECONOMICALLY JUSTIFIABLE*

Internal valuations of pledged collateral serve as BAMC's basic price, based on which it can decide whether or not to accept a price proposed by a bankruptcy trustee. If BAMC finds that a proposed selling price is too low, it will actively intervene and acquire or take possession of the asset effectively settling its claim either partially or in full.

BAMC will acquire real estate from distressed/bankrupt companies in the following cases:

- real estate which the bankruptcy trustee is not able to sell (forced take over). In this case the real estate will be taken over only if the internally estimated value exceeds the charged bankruptcy cost,
- deteriorating real estate in bankruptcy procedures for which a further deterioration cannot be prevented due to a lack of funding (the same goes for unfinished projects),
- selected real estate, for which BAMC believes that fire sales should be avoided because the assets can be sold under better conditions in the future,
- specific types of real estate in order to bundle and sell them.

BAMC will study the feasibility of a proactive takeover of larger real estate from bankruptcy procedures under the assumption of more successful management and liquidation of these real estate.

For each piece of real estate, an individual business plan will be prepared, containing the important elements for successful marketing. These business/action plans will be discussed and approved by the relevant Investment committee. Before the real estate is taken over it has to be visited by the respective BAMC real estate expert and, if needed, additional examinations are done in order to make sure there are no environmental or other issues with the property.

*BAMC WILL ENSURE VALUE PROTECTION AND VALUE ENHANCEMENT THROUGH FACILITY MANAGEMENT*

A large number of properties, for which BAMC will obtain ownership, will not be possible to be sold immediately. BAMC will therefore put in place a comprehensive and efficient facility management system. A limited number of external service providers/facility managers will be needed to accomplish this.

*BAMC WILL ADD VALUE TO ITS REAL ESTATE THROUGH A WIDE RANGE OF MARKETING ACTIVITIES*

An individual strategy for each real estate will be developed and approved by the relevant investment committee. When devising such a strategy, consideration will be given to whether the real estate might fit into a larger portfolio, which could be offered to international real estate investors. If so, BAMC will still try to market the real estate individually and in case an appropriate price is received, execute the transaction. At the same time such real estate will be “earmarked” for inclusion in a possible larger portfolio. BAMC will regularly investigate the interest.

*BAMC WILL USE RENTAL OPTIONS TO OPTIMISE THE COMBINED YIELD AND EXIT VALUE FROM REAL ESTATE*

In cases where real estate will not be possible to sell immediately, BAMC will try to find temporary tenants. Generally, rented real estate is also easier to sell. For flats in residential complexes, BAMC may also use a “rent to buy” option. Interested buyers will be encouraged to rent the flats first before finally buying it. Part of the rent is normally recognized as purchase price.

*BAMC WILL NOT BE A REAL ESTATE DEVELOPER BUT MAY INVEST IN COMPLETION OF ALMOST FINISHED PROJECTS*

BAMC should not develop any project by itself. However, partnerships with sound local and international developers/investors are possible. Only companies with high credit rating and proven track record should be considered potential partners of BAMC.

BAMC may however develop real estate projects to a certain stage in order to facilitate the selling process. For example BAMC might develop a land plot by financing a new building plan, building infrastructure like roads and subdivide the plot.

On the other hand BAMC can and will invest in real estate projects which are almost finished and only some finishing and/or renovation works are needed. With such investments the value and saleability of the real estate can be increased substantially. Many times BAMC also has to remedy legal errors like obtaining missing documentation and permits or ensuring access to the property.

*IF DEEMED ADVANTAGEOUS, BAMC WILL CREATE REAL ESTATE PORTFOLIOS WITH DISTINCT RISK AND RETURN PROFILES*

BAMC will consider forming real estate special purpose vehicles (“RSPV”) as subsidiary companies and sell the whole or part of it to the interested investors. The RSPV could be formed by the type of asset (residential, land, etc.) or by other criteria, which could be of interest to the investors. Listing such a RSPV on the stock exchange might be considered as an exit option.

*SELECTING OPTIMAL SELLING TECHNIQUE AND PROCESS IN BANKRUPTCY PROCEDURES*

In cases where BAMC finds that the sale process suggested by the bankruptcy trustee to be suboptimal, it will not give its consent to the sale and propose another approach, which it believes will provide the best way of settling of its claims.

BAMC will take an active role and support the bankruptcy trustee in the selling process, e.g. by using BAMC's network to find potential investors, assigning real estate agents, etc. BAMC will further publish all actual real estate bankruptcy auctions on its own web site.

*COMPETITIVE AND TRANSPARENT EXIT PROCESS*

All real estate for sale or rent will be published on BAMC web site. Each advertisement will be published for a certain minimum time period (longer for larger real estate). In case of several interested buyers an auction/tender will be organized. BAMC may use external real estate agents. For more complex residential real estate (e.g., Celovški dvori and Nokturno) special interactive web sites will be developed.

*TERMINATION EXIT STRATEGY*

Some real estate objects may be difficult to exit even in the long run. After BAMC ceases to exist, the remaining real estate can be transferred either to another public company or sold to a private real estate fund or other interested party.

The conceptual marketing strategies that may be applied to various types of real estate are summarised in the table below.

TABLE 7: CONCEPTUAL MARKETING STRATEGIES BY REAL ESTATE TYPE

	<b>Residential complexes</b>	<b>Residential single units</b>	<b>Industrial</b>	<b>Undeveloped land</b>	<b>Office</b>	<b>Retail</b>
<b>Takeover priority</b>	High, especially if unfinished and good location	Low	Low	Low	Low	Low
<b>Fit-for-sale measures</b>	Yes	Yes	Yes	Yes	Yes	Yes
<b>Finish projects and remedy defects</b>	Yes	No	No		Yes, if large real estate	No
<b>Project development</b>				Generally no, limited in specific cases		
<b>Appointing facility manger</b>	Yes	Yes	Yes	Yes	Yes	Yes
<b>Sale or rent?</b>	Sale + rent to buy (alternative)	Sale	Sale If reasonable temporary rent	Sale	Sale If reasonable temporary rent	Sale If reasonable temporary rent
<b>Marketing strategy</b>	Real estate agent, special approach (interactive web-site)	Real estate agent	Real estate agent + own marketing activities for large/specific real estate + support of community	Real estate agent + own marketing activities for large/specific real estate + support of community	Real estate agent + own marketing activities for large/specific real estate	Real estate agent + own marketing activities for large/specific real estate
<b>Target markets</b>	Funds, individuals	Individuals, funds	Local, regional and international entrepreneurs (for larger real estate)	Local, regional and international entrepreneurs (for larger real estate)	Local, regional and international entrepreneurs (for larger real estate)	Local, regional and international entrepreneurs (for larger real estate)
<b>Market liquidity</b>	Medium	High	Low, especially for larger real estate	Low, especially for larger plots	Medium	Medium

## FINANCING STRATEGY

- BAMC will continue to manage its cash reserves prudently and efficiently.
- BAMC will be repaying state-guaranteed liabilities.
- With extended lifetime, BAMC will seek redeemable financial liabilities.
- Being 100% state-owned, BAMC recognizes that it is returning funds to the Republic of Slovenia also through the paid taxes and will therefore not pursue specific tax optimization

BAMC's financial liabilities amounted to €1.253,5 million at the end of 2015 and were increased by €411,7 million with merging of Factor banka and Probanka on 1 January 2016. Before the registration of the merger of Factor banka and Probanka into BAMC, both banks had repaid all except one loan towards SID banka and part of financial liabilities towards the Ministry of Finance.

In April 2016, BAMC agreed with the Ministry of Finance to repay €150 million of liabilities, extend the maturity of the remaining liabilities by December 2016 and decrease the interest rate from 1,67% to 1,20%. In August 2016, BAMC made another early repayment of €120,0 million to the Ministry of Finance, further reducing its debt.

BAMC's ability to service its future financial liabilities is determined by current debt and BAMC's ability to effectively manage and exit the assets. Efficiency of asset management is shown through:

- Cash generated from asset management,
- Cash invested in upgrading asset quality and value maximization, including providing liquidity for working capital and necessary capital expenditure to restructuring cases, and
- Efficient management of BAMC's operating costs.

BAMC will partially refinance financial liabilities which mature in December of 2016 and 2017, respectively (issued bonds and liabilities towards the Ministry of Finance). The refinancing will be done in a transparent and competitive process, taking into consideration the regulation on state owned companies' borrowing. A guarantee from the Republic of Slovenia will be required for refinancing BAMC's financial liabilities.

### *BAMC WILL CONTINUE TO MANAGE ITS CASH RESERVES PRUDENTLY AND EFFICIENTLY*

BAMC will manage its available cash so that it is able at all times to meet the expected, and unexpected, payment obligations.

BAMC expects to have relatively predictable liquidity outflows. The outflows by the end of 2017 are mainly related to the repayment of principal and interest of matured bonds and the merged obligation towards the Ministry of Finance. On the other hand, inflows are expected to come in relatively evenly throughout the year in the coming years. As a consequence, BAMC will have temporary cash surpluses

in this period and will manage its liquidity in accordance with the adopted Investment policy for the management of liquidity reserves.

In handling its liquidity, BAMC will pursue the principles of prudence, liquidity and profitability, in the order stated. BAMC applies the prudence principle by investing available cash strictly in the following types of investment:

- Overnight bank deposits, deposits with up to 365-day maturity, on-call deposits with a credit institution based in the Republic of Slovenia, an EU Member State or an OECD member country,
- Debt securities issued by the Republic of Slovenia or another EU Member State, the European Central Bank, Bank of Slovenia or a central bank of another EU Member State,
- Debt securities other than subordinate securities issued by a bank based in the Republic of Slovenia or a credit institution based in another EU Member State.

BAMC will limit its maximum exposure to any individual credit institution according to the Investment policy for the management of liquidity reserves.

#### *BAMC WILL SEEK REDEEMABLE FINANCIAL LIABILITIES*

BAMC is generating relatively constant cash inflows from actively managed assets. On top of that, some larger transactions like sales of specific portfolios or individual large cases, will generate large inflows which cannot be accurately predicted timewise.

According to legislation, BAMC is allowed to invest only in fixed income low-risk instruments which provide almost no return at time being. Therefore, BAMC will seek redeemable financial liabilities in order to ensure flexibility and maximization of returns in cash management.

#### *BEING HIGHLY LEVERAGED, BAMC WILL SEEK A FINANCING STRUCTURE WHERE FINANCIAL LIABILITIES ARE GUARANTEED BY THE REPUBLIC OF SLOVENIA*

Like other bad banks, BAMC's gearing is extremely high. Debt-to-equity ratio was 31,9 as per 30 June 2016 but will decrease through BAMC lifespan, also through planned recapitalisation in H2 2016. Such capital structure demands a guarantee of the Republic of Slovenia for all future refinancings of BAMC.

In order to strengthen its capital structure BAMC is also planning to:

- be recapitalized from the Republic of Slovenia for €50 million in H2 2016,
- denominate shares from €2 per share to €1 per share thus creating capital reserves for covering potential losses in the amount of €104,1 million.

#### *BAMC IS RETURNING FUNDS TO THE REPUBLIC OF SLOVENIA ALSO THROUGH TAXES*

BAMC is 100% owned by the state and is returning funds to its owner also through paid taxes. BAMC will not involve in any tax optimization procedures that may appear as attempts of tax evasion.

## ORGANISATIONAL STRATEGIES

- BAMC's organization and its organizational strategies are designed and chosen to effectively enable and support the execution of BAMC's core value-adding processes and achievement of BAMC's core strategic objectives.
- BAMC's structure and key decision processes will be continuously re-evaluated and adjusted to meet BAMC's changing priorities over its intended life-span.
- Structure and processes are only effective with the right people having the right tools and systems to be successful. BAMC's HR and IT strategies are further elaborated upon below.
- BAMC's strategy vis-a-vis its people, its Human Resources strategy is geared to ensure that BAMC attracts, recruits, retains and develops its people so that: (i) BAMC needs are met, (ii) BAMC's people develop and require skills and experience that are valuable for the Slovenian economy post BAMC's end of existence
- BAMC's strategy vis-a-vis core systems and tools, its Information Technology strategy, will ensure that BAMC's information system provides accurate and on-time information to support BAMC's decision-making processes in a secure and confidential way.
- IT and technology solutions will be cost effective solutions taking special consideration of BAMC's limited lifespan and its changing strategic priorities over its life-span and should provide the tools for efficient management of the transferred assets on a consolidated basis.

### HR STRATEGY

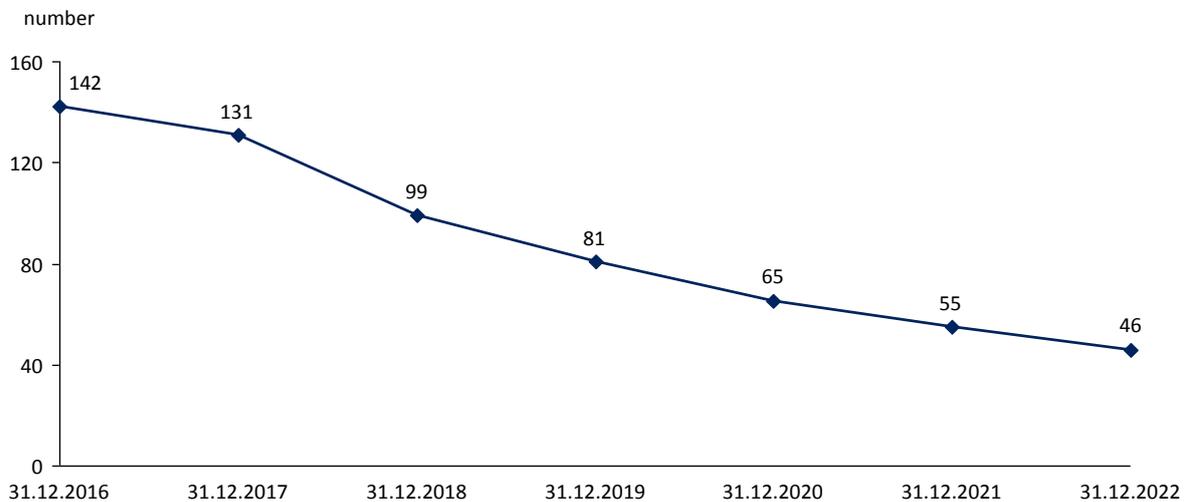
At the end of June 2016 BAMC had 187 employees. In the reorganisation process, the target staffing model was defined and the target number of permanent employees, including insourced services for cost savings, was set at 142. In this way, BAMC ensured that the pre-merger productivity levels were restored/increased, and overall productivity of the merged entity is 15% higher than the three separate entities combined. To further develop the organisation, train the staff, and implement the enablers to execute the strategies successfully, the HR department and management prepared a HR strategy and set of activities that supports its effective implementation.

BAMC works to create an organisation that that makes BAMC more valuable than the value of the assets BAMC manages. This additional value will stem from the organisation and the people BAMC employs. Organisational development is therefore a key priority for BAMC.

Due to limited lifespan, BAMC will periodically adjust its organisation to align to the different needs in its overall strategic phases, both its Act of systemisation and headcount dimensioning will be reviewed and adjusted during the planning horizon.

Headcount will gradually reduce, following reduction of assets under management and best practice norms.

FIGURE 9: PERMANENT HEADCOUNT PLAN



In case the proactive takeover of larger real estate from bankruptcy procedures under the assumption of more successful management and liquidation of these real estate proves justified, BAMC will adjust the number of employees in the real estate management unit correspondingly.

#### *USE OF INTERNAL VS. EXTERNAL RESOURCES*

BAMC will seek to operate with internal resources to ensure efficiency and optimal learning and capability development. To the extent that this is not possible, e.g., due to lack of available expertise that can be attracted on the terms BAMC can offer as an employer, due to overall cost effectiveness, due to time constraints or the temporary nature of tasks at hand, external resources (vendors, consultants, advisors, sub-contractors, and similar) can and will be used. These external resources will be engaged in line with external regulations, internal policies and good practices.

#### *INTERNAL HUMAN RESOURCES STRATEGY*

BAMC people work in an organisational structure and corporate culture in which collaboration, professionalism, good solutions, self-improvement and results matter more than the formal job title.

Besides experience, expert knowledge and integrity, it is essential for the company's successful operations that BAMC's employees have the motivation and capacity for:

- solving problems,
- quick learning,
- building and continuously improving the organisation, team and procedures, and
- working diligently and supporting fast decision-making in an environment operating with a significant number of unknowns.

The corporate culture is also fostering 10 key values:

- having integrity,
- showing accountability,
- taking responsibility,
- being ethical,
- being professional,
- acting solution-oriented,
- ensuring fact-based decision making,
- being and acting socially responsible,
- appreciating and promoting diversity,
- considering all views internally but speaking externally with “one voice”.

#### *RECRUITING*

Despite the fact that headcount will constantly reduce, efficiently following norms relating to assets movement, BAMC will still recruit employees due to fluctuation. BAMC’s recruiting approach is ensuring a fair, fact-based, competence-focused and thorough recruitment and screening process to attract and successfully recruit its personnel, fully in line with the Slovenian legislation and good practices. In cases where specific, or international, competences are required and sought after, the support of an HR agency may be used. BAMC is proactively managing its recruitment process to avoid recruiting biases, e.g., in terms of gender, age, origin or nationality, associations or connections. Recruiting decisions are made following the “grandfather” principle, i.e., a manager never takes the final decision to recruit his or her own directly subordinated employee. The decision is taken or approved by the line manager’s direct supervisor or similar level decision authority.

#### *EMPLOYEE DEVELOPMENT*

People development is critical to the success of BAMC. A significant part of the competence development comes from on-the-job training and internal experience sharing. External training on an individually assessed and agreed basis complements common internal training. As part of BAMC’s performance evaluation system, each employee at BAMC will meet with his or her direct line manager and agree on an individual development plan every 12 months.

#### *REMUNERATION, INCENTIVES AND RETENTION MANAGEMENT*

The Government has defined the overall remuneration policy of BAMC’s Board, i.e. the non-executive and executive directors of BAMC. Remuneration of other BAMC employees is defined by BAMC. Oversight of BAMC’s remuneration policies is supported by the Remuneration Committee that recommends policy decisions to the Board. The Board is the ultimate decision maker in matters of remuneration policy.

In order to attract and retain highly skilled employees to a company with a time-limited life span, BAMC has to offer market-based, competitive salaries. These are defined based on the potential employee’s

other opportunities and not only upon a comparison with Slovenian public sector institutions or organisations.

In 2016, BAMC will have completed its process of introducing the Management-by-objectives & numbers and Performance management system. The remuneration system for employees that are not Board members will then comprise variable components of salary based on work and measurable quantified targets, derived from the scorecard for business/support/operational performance, reinforcing BAMC's goal-oriented corporate culture.

#### *EMPLOYEE EXIT PREPARATIONS*

Each employee's individual development plan will eventually include steps for exit preparations. BAMC will actively look for ways to support its employees to find positions outside BAMC where the acquired skills and experience from BAMC can be used to further add value to Slovenian businesses and organisations.

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### INFORMATION SYSTEM STRATEGY

The main role of BAMC's information system is to provide accurate and on-time information in the decision-making process of BAMC as well as provide an audit trail of BAMC's decisions and activities. BAMC information technology strategy establishes the general outline for developing the IT systems over BAMC's lifespan, which is scheduled to end in 2022 and significantly influences the BAMC's IT strategy. The primary emphasis is on the development of a cost-effective and fully-functional IT system with short implementation time, which will cover the majority of BAMC's processes and provide the relevant information to those involved in the processes. Finding the optimal balance between business requirements, costs and quality of the IT service is an ongoing task.

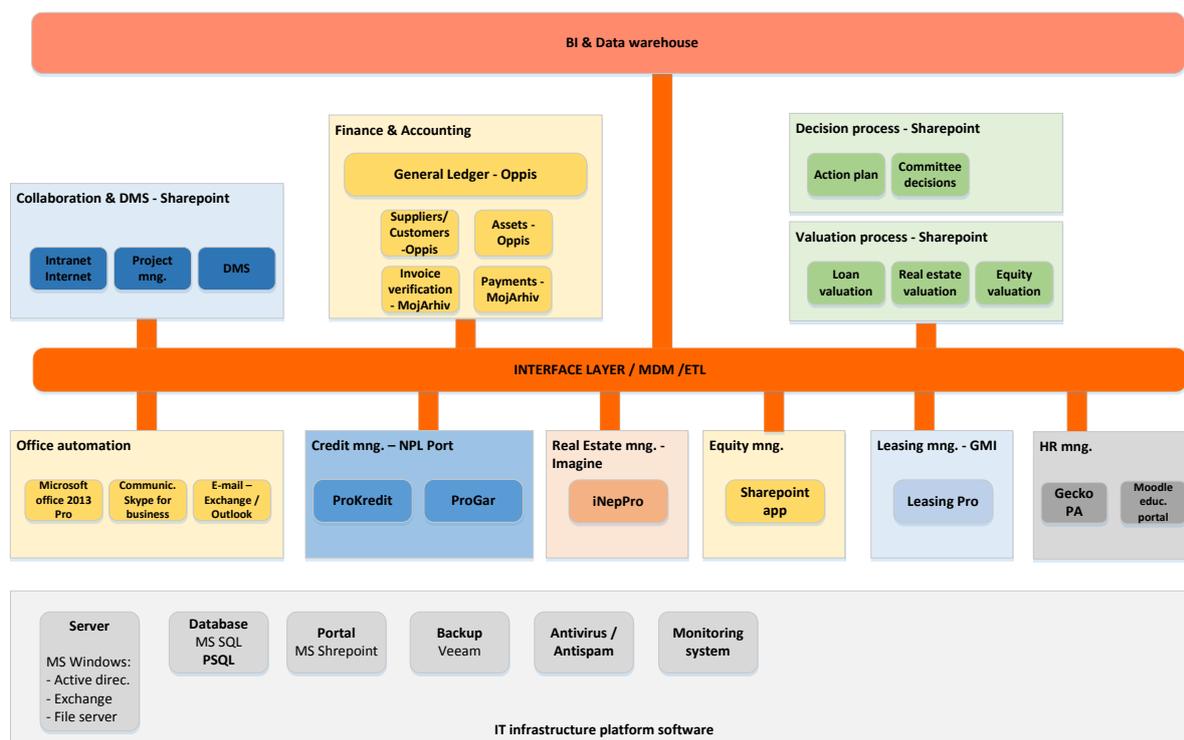
Since BAMC is managing different classes of assets which were transferred from different banks, the development of an integrated IT system while covering specific BAMC's processes was an issue. The current IT system architecture is the result of past portfolio migrations and merged companies. During the migration and merger process, optimal IT solutions were selected and implemented. Thus the target IT architecture is already in place and the strategy focuses more on the optimization, integration and improvement of this architecture and on the implementation of IT solutions for processes which are still manual. This will serve to reduce the likelihood of human mistakes and decrease the general risk to the company. Special emphasis should be also be put on master data management and data quality.

The strategy covers different IT areas: an application strategy, infrastructure strategy and IT management strategy.

### *APPLICATION STRATEGY*

From the application point of view, the strategy should answer the question which type of software to use – either a standard software solution or a custom-made one. As a generic guidance, the first choice is to use standard software solutions parameterised to accommodate BAMC's processes. The use of a custom-made solution can be a choice in cases where the standard solutions do not fully cover the process or if there are no standard solutions available. The IT architecture of BAMC's applications is shown in the figure below.

FIGURE 10: APPLICATION SOLUTION MAP



Basically, BAMC's applications architecture consists of: core process solutions for credit, real estate and equity management, the collaboration and document management system, the accounting and human resource system and at the end the office automation system. The core process of credit management is supported with the IT solution provided by BAMC's subsidiary NPL Port. This solution incorporates the banking process know-how and as a result reduces the operational risk of BAMC.

To integrate different applications together and to assure quality data to the business intelligence system (BI), a reliable interface layer with strong master data management (MDM) should be built in the future.

Assuring long term data availability is becoming an important strategic issue for BAMC. This is particularly important after the merger of the two banks into BAMC, when many of IT systems have become archive systems. Active management of archive systems should be considered in a similar way as for systems in active use.

#### *INFRASTRUCTURE STRATEGY*

The main goal of the infrastructure strategy is to have a secure and reliable infrastructure. On the infrastructure side, the strategy for productive systems is to use solutions from a single provider so that the integration of different services will be simplified. The core infrastructure solution is based on Microsoft solutions (MS Windows Server, Hyper-V virtualisation, MS SQL database, MS Active directory and MS Exchange) and consists of the core infrastructure: servers, storage, network, backup, operating

system, and the database. The best practices for a secure and reliable infrastructure should be followed.

Due to the sensitivity of BAMC's data the usage of cloud services will be very restricted and conservative. To assure similar services to the users, a private cloud strategy will be developed. A similar approach will also be implemented for mobile devices.

#### *IT MANAGEMENT STRATEGY*

The main goal of the IT management strategy is to build a lean IT organisation that is capable of managing development and maintenance tasks in combination with outsourced resources. With this strategy BAMC wants to keep a high level of IT knowledge, which will allow the management of outsourced services and projects to be more controlled. It is important to have highly trained staff with a broad knowledge of different IT areas.

Going forward, more attention will be placed on BAMC's business processes and applications to support them, as well as building the required IT team. Due to the specific nature of BAMC's processes, which are a mix of different industries, the accumulated know-how in terms of processes and IT solutions which supports these processes, could be very valuable, and could potentially be sold on the market after the end of BAMC's lifespan.

Assuring security and compliance is important to BAMC. Risk assessment should be performed on an ongoing basis, with clear and strong backup and security policies in place. A disaster recovery plan (DRP) should be prepared and periodically rehearsed.

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## STAKEHOLDER STRATEGIES

### COMPLIANCE AND LEGAL STRATEGY

BAMC shall be fully compliant with all relevant legislation and regulation and will also continue to cooperate with all government bodies and report to them in accordance with the established reporting system. BAMC will increase its role as a proactive proposer of better, improved, more rational and efficient operations.

In areas where the legal and regulatory frameworks are ambiguous, BAMC will seek clarification from the appropriate authorities or through testing cases in the court system in order to reduce uncertainty that reduces effectiveness.

In March 2015 BAMC received the Audit Report of the Court of Audit of the Republic of Slovenia (abbreviated: CoA) "Establishment of the conditions for the functioning and operations of DUTB, d.d. in 2013". Within the deadline provided by the CoA, BAMC submitted its response report, which demonstrated the corrective measures taken by BAMC. BAMC eliminated all irregularities and inconsistencies in the segment of the audit, which pertains to BAMC's operations in 2013. The implementation of corrective measures was applied with maximum care to comply with the opinions and recommendations of the CoA. Currently, audit is ongoing at BAMC, which goal is to express an opinion on regularity, efficiency and effectiveness of BAMC's operations in 2014 and 2015.

In August 2015, Ethic intelligence, an independent certification body, awarded BAMC with anti-corruption compliance program certificate. In 2017, BAMC will repeat the certification process in order to review the current situation and to obtain the upgraded certificate.

BAMC will proactively work with, propose and implement effective processes to comply with the investigative needs of institutions such as CoA, Commission for the Prevention of Corruption (abbreviated: CPC) and the Information Commissioner, and incorporate their recommendations already in the investigation phase to the extent possible.

BAMC has a clear Integrity plan, aligned with the Commission for the Prevention of Corruption (hereinafter: CPC), plan and Measures for identification and prevention of corruption risks and the risk of other wrongdoing or unethical conduct. Integrity plan is a tool for establishing and verifying the integrity of BAMC. It is devoted to:

- identifying relevant corruption risks in different working fields of an individual organization,
- assessment, what danger corruption risks may pose to individual organization, and
- determining measures to reduce or eliminate corruption risks.

In the sense of implementation, the integrity plan is basically a systematic and documented process in which all employees are actively involved. They identify risks, analyse and evaluate them and propose appropriate measures, meanwhile they constantly debate and communicate with each other.

BAMC is implementing a protection program for whistle-blowers reporting wrongful or unethical conduct. The Compliance officer reports regularly on the meetings of the Board of Directors and Audit Committee.

BAMC is planning to perform additional trainings related to compliance issues for its employees.

Coordination between compliance, risk management and internal audit is established through regular meetings of the Committee for Compliance and risk management. This committee reports from this Committee are a standing item on the Board of BAMC's meeting agenda.

One of the key objectives of ZUKSB is to facilitate the identification of irregularities, which led to loans and investments, which were transferred to BAMC as risky items. In order to meet the objective, BAMC has set up a special investigation task force in 2016, i.e., a permanent investigation team to ensure that the process of investigation of criminal activities is brought to a successful conclusion and that all cases in the BAMC portfolio are systematically monitored regarding any suspicious activity.

Any identified suspicions based on internal investigations carried out by the special task force will be reported to the National Bureau of Investigation or BAMC will directly press charges. BAMC will investigate if it is appropriate to complement BAMC's organisation with some forensics capability to be able to more effectively assist the authorities in these cases.

BAMC will continue to follow the protocol for regular reporting of such suspicions to the appropriate authorities and to assist the relevant authorities in their further pursuit of such cases.

#### CORPORATE COMMUNICATION STRATEGY

##### *IMPROVE COMMUNICATIONS CAPABILITY, STRENGTHEN PR AND ADDING THE FUNCTIONALITY OF INVESTOR RELATIONS AND MARKETING*

During 2016, the goal is to ensure that the work of BAMC is more effectively and objectively reported to the general public as well as to the key stakeholders, including investors. One of the activities in 2016 was to upgrade BAMC's website with, among others, a powerful search engine for interested potential investors and a new anonymous box for external whistle-blowers, all to further enhance the transparency of BAMC's operations.

The current communication strategy focuses on:

- supporting BAMC's strategic goals by promoting the understanding of the role of BAMC and the benefits BAMC brings to the Republic of Slovenia and the taxpayers in key audiences,
- obtaining the support of key audiences in implementation of measures,
- managing media relations, that will, as far as possible, support the achievement of BAMC's objectives,
- ensuring the "one company one voice" communication effect, and
- changing BAMC's communication from being reactive to being proactive.

To improve communication effectiveness, BAMC is continuously reassessing key messages for each stakeholder group, the best channel and means of communication. Current key stakeholders, in addition to the general public and media, include:

- Slovenian decision-makers, e.g., the Ministry of Finance, the Bank of Slovenia, the Ministry of Economic Development and Technology, the Interministerial Committee, the Committee for Finance and Monetary Policy, and individual Members of Parliament,
- Slovenian public authorities, e.g., CPC, the Information Commissioner, the Competition Protection Office of the Republic of Slovenia, the Court of Audit of the Republic of Slovenia,
- EU and International decision makers – the European Commission, ECB, and IMF,
- Slovenian financial institutions,
- The corporate sector – BAMC’s clients, owners and management team of clients, several business-related Slovenian associations,
- Investors – property buyers, funds and investment companies with investor mandates encompassing BAMC’s assets, including international institutions such as EBRD and IFC,
- Opinion-leaders,
  - Slovenian – Association of Slovenian Banks, leading experts, academics, commentators, management in different institutions, media editors,
  - European – European Banking Agency (EBA), IMF, ESM.

Communication is planned, directed and managed by BAMC’s Marketing, corporate communication and investor relation unit, which is directly reporting to the CEO. This unit is BAMC’s communication hub where external and internal information is reviewed, harmonised, revised, adjusted and created in compliance with strategic, business and communication objectives of BAMC.

## TERMINATION STRATEGY

- BAMC's termination strategy will seek to prevent any fire-sale situations at the end of BAMC's mandate.
- With a prolonged life span to 2022, BAMC will be able to exit most of its assets and terminate all its activities and operations orderly.
- Detailed termination strategy and action planning will be determined in 2020.

According to the original ZUKSB, BAMC's lifespan was limited to the end of 2017 but the law amendments include an extended lifespan until 2022.

The main benefits of BAMC's prolonged existence are:

- avoiding the risk of an exit with a potential discount when selling/transferring the remaining portfolio at premature life-end. Thus, a prolonged life-span should improve the probability of good economic returns to the Republic of Slovenia,
- increasing the success rate of restructuring processes as these processes can be completed by managers with an in-depth knowledge of specific cases,
- a more orderly and cost effective adjustment and ramp-down of the organisation and headcount.

The assets remaining in BAMC's management at the end of 2022 are going to be, in accordance with Article 36 of ZUKSB, transferred to SDH or other institution as decided by the owner. BAMC projects to have €79,4 million of claims and €8,9 million of real estate at the end of its lifetime.

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## RISK MANAGEMENT

### RISK MANAGEMENT MODEL

Risk management model is established with the Risk management policy, where good practices are set as general guidelines.

### PARTICIPANTS IN RISK MANAGEMENT

All BAMC employees are part of the risk management system in their daily operations. However, risk management department develops methodology and ensures systematic approach in addressing key risks. In addition, compliance provides an overview on compliance rules and standards and informs employees regarding changes in the relevant legislation and internal acts. Compliance is a key body in preparing an integrity plan and measures for identification and prevention of corruption risks and the risk of other wrongdoing or unethical conduct. Internal audit encompasses the evaluation of adequacy and effectiveness of risk management and internal controls as well as the quality of performance carrying out assigned responsibilities to achieve the organization's stated goals and objectives and provides an overall view on risk management on all levels of BAMC.

### RISK IDENTIFICATION

All business units are actively involved in identifying key risks for their business units and BAMC as a whole. This allows the risk management system to be adjusted to business processes and be consistent with BAMC's operational goals. Process of risk management is based on business processes, where risk owners and owners of business processes are actively involved in monitoring and estimation of risk (bottom-up approach). Role of the risk management department is to prepare a model and methodology and to associate all activities for risk mitigation with business owners. In addition, the management of BAMC adopts a "risk appetite" and shows guidelines with adoption of strategic and business decisions both for risk management department and process owners (top-down approach).

### RISK ESTIMATION

The risk management model is based on estimation of risk as a product of probability for such risk to realize and value or impact which would be caused for BAMC. Probability of occurrence is estimated based on historic data or frequency of such event to realize. Value of such risk is estimated according to the impact on BAMC operations, financial impact or any distress in business processes or to BAMC's reputation. Both, probability and value of risk, are estimated on a five-point scale which allows for clear and objective intensity of risks. In that way, risks are mitigated and monitored as a result of an objective analysis and not as a subjective opinion.

### RISK CATALOGUE

Risk catalogue is regularly reviewed and amended with main identified risks together with their estimation, mitigation and monitoring of impact of risks over time. Risk catalogue represents identified

risks based on estimation of heads of departments, identified loss events, performed surveys among employees and is reviewed on a monthly basis. Each identified risk has a determined risk mitigation, total estimation of risk is regularly monitored.

#### LOSS EVENTS

Important role in risk management is monitoring of occurred loss events. BAMC categorises a loss event as each event which has (potential) negative financial consequence for BAMC. Loss events show direct sign of necessary attention needed in such processes in order to lower the loss, caused by such event, and/or to prevent re-occurrence of such events. All employees are part of reporting of identified risks and loss events and have an important role in risk management system with their proposals to mitigate risks and loss events.

#### RISK AND COMPLIANCE MANAGEMENT COMMITTEE

Risk and compliance management committee is established with systematic approach to risk management. The committee on an executive level is held on a monthly basis and provides a prompt reaction to most important risk and compliance issues. Participants of the committee are risk owners of key business processes, which leads to maximal operability of the committee.

#### INTERNAL CONTROL SYSTEM

Special attention of risk management is devoted to increased and empowered internal control system. The risk management department is involved in regular reporting system and has provided additional four-eye principle in key business processes, such as valuation of assets, and several risk reviews in decision-making process. Impact of internal controls is expected to be increased.

#### CHANGES OF INTERNAL ORGANIZATION AND DECISION-MAKING SYSTEM

Changes in the legal framework, corporate governance and supervisory function together with merger of Factor banka and Probanka into BAMC have resulted in the need to adjust the internal organization. BAMC responded quickly and efficient to challenges that emerged in the first half of 2016.

BAMC's portfolio structure has significantly changed with the merger of Factor banka and Probanka into BAMC. Changes in internal organization were therefore crucial in order to manage assets in the most efficient and effective way, including horizontal controls built in the processes by a clear segregation of duties between case/equity/real estate management, financial analysis and valuation verification, mid-office and legal support . In addition, internal organization, implemented at the beginning of July 2016, fully corresponds to the amendments of ZUKSB regarding restricted role of non-executive directors, distinction of functions, and new powers of BAMC.

The decision-making system has been renewed with a four-eye principle which allowed operational heads to fully cover the operational decisions for minor exposures. While executive directors adopt

decisions with greater impact for BAMC, strategic guidelines for managing assets are still set by the Board entirely. Decisions regarding granting additional loans (provided with ZUKSB) is also one of the objectives of detailed review of departments, separated from credit management.

BAMC introduced changes in the decision-making system in the beginning of April 2016 as a response to changes in ZUKSB, merger process and changed structure of portfolio of assets under management. Completely renewed structure of credit and investment committees has eliminated the overlapping of responsibilities on Executive and Board levels. Now the Board Credit and Investment Committee is a consent-giving body to the decisions adopted by the Executive Credit and Investment Committee.

Limits between different types of credit and investment committees are clearly established, and participants at the specific levels of committees are clearly defined. Operational Credit and Investment Committee now takes more operational decisions for cases with higher exposures and most of the decisions for cases with smaller exposures, while executive level committee still controls all high impact decisions related to larger exposures.

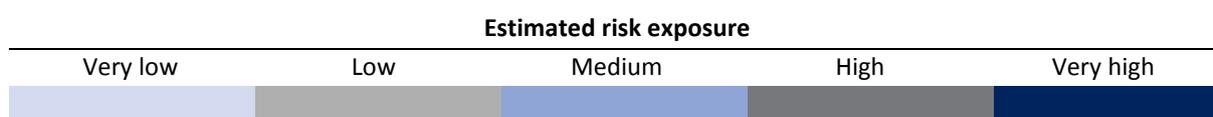
Action plan template was changed in a way to unify management of loan and equity exposure on the one hand and to simplify the decision-making process for smaller exposures with less significant impact of the proposed decisions on the other.

## KEY RISKS AND THEIR MITIGATION

Most important identified risks categorised as strategy, operational, reputational and financial risks are presented below.

### STRATEGY RISKS

#### *RISK OF UNSUCCESSFUL IMPLEMENTATION OF THE OPTIMAL RESTRUCTURING STRATEGY*



BAMC is pursuing the restructuring strategy in some 100 indebted companies. BAMC will opt for the restructuring strategy in cases where financial and operational restructuring would yield a higher value compared to the disposal value of the collateral. There is a risk, however, that the restructuring will not be successful and that the recovery strategy will have to be used instead, or that the planned cash flows will not materialise in the amount and/or timing planned which would result in decreased revenue for BAMC. This risk can materialise either due to developments in the macroeconomic environment or due to failed financial, and in most cases strategic and operational restructuring of the debtors.

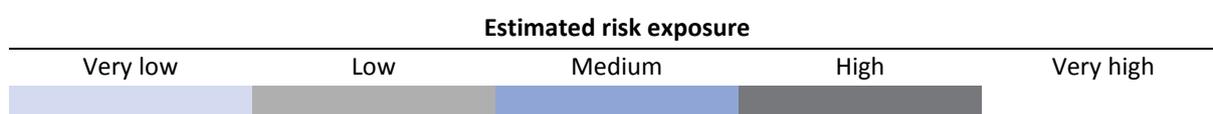
## OPERATIONAL RISKS

### *RISK OF ERROR IN LEGAL PROCEEDINGS*



Particularly in debtor companies where BAMC is implementing the recovery strategy there is a risk that BAMC might miss the deadlines in judicial procedures involving foreclosure. BAMC may thus lose its rights to repayment through disposal of collateral.

## REPUTATIONAL RISK

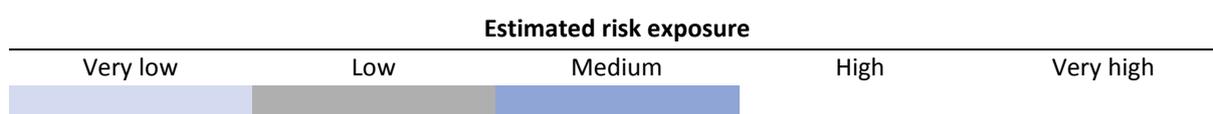


Reputational risk is a risk of loss resulting from damages to a firm's reputation. In case of BAMC it can be shown as negative public, political or industry opinion that can impact its core business activities and undermine BAMC's ability to achieve its objectives. BAMC's reputation could be damaged as a result of an actual or perceived manner in which BAMC conducts its operations. Negative opinion could be created due to increased operational costs, loss of significant legal cases, leak of information and in case of fraudulent actions. Adverse media publications, often incentivised by interested stakeholder groups, could also result in significantly negative perception of BAMC's efforts to meet its objectives.

Reputation and credibility of BAMC when dealing with debtors, stakeholders involved in other cases or potential buyers can also be severely damaged by unexpected Government decisions, instructions on its operations or other institutions.

## FINANCIAL RISKS

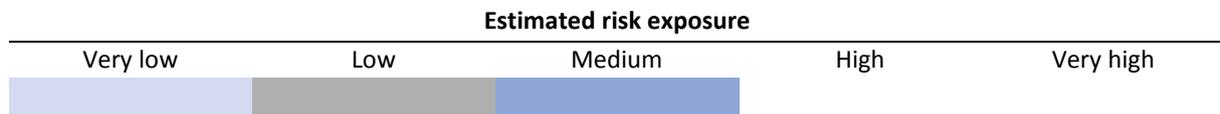
### *LIQUIDITY RISK*



Liquidity risk is the risk that BAMC will not be able to meet its financial obligations as they fall due. BAMC ensures maximum possible liquidity by always having sufficient liquid assets to meet its liabilities when due, under both normal and demanding conditions, without incurring unacceptable losses or risking damage to its reputation. The key liquidity risk for BAMC is the repayment of issued debt. In December 2016, debt matures in the amount of over €580 million and BAMC is planning to repay part

of its obligations with liquidity reserves and part with refinancing with Republic of Slovenia's guarantee.

#### *CAPITAL ADEQUACY RISK*



Due to negative equity of the merged Factor banka and Probanka and negative difference between fair values of merged assets at the initial recognition and bank's book values, the equity of BAMC deteriorated to the level where the management had to assess capital inadequacy and concluded that BAMC will be able to meet all of its obligations when they fall due. BAMC's General Assembly has been informed on the potential risk already in the February 2016 Merger report. The current business plan envisages recapitalization of BAMC in the amount of €50 million in the second half of 2016 in order to strengthen its capital structure.

## BUSINESS PLAN 2016-2022 SUMMARY

- Planned BAMC equity of €212,3 million in 2022 is larger than the initial investment by the Government in 2013.
- Taking returns of capital to the owner (as well as recapitalisations) into account this stands for an average yearly EROE of 13,0%.
- Operating costs in the 2016-2022 period are planned to amount to €98,1 million.
- Net profit in the 2016-2022 period is planned to total €105,9 million.
- Cash flows of €1.223,6 million from loan portfolio, €296,1 million from real estate portfolio and €81,9 million from equity portfolio to support these results.

## KEY PERFORMANCE INDICATORS

Key performance indicator	Definition	2014	2015	2016	2017	2018	2019	2020	2021	2022
		Actual		Planned						
Cumulative cash generated	Absolute amount (in € million)	137	494	869	1.200	1.666	1.930	2.078	2.159	2.229
Cash generated in %	Cash generated / NPAs transfer value	11,5%	22,0%	18,7%	16,5%	23,2%	13,1%	7,4%	4,0%	3,5%
Cost efficiency	Operating costs without direct transactional costs / average total assets	0,97%	1,01%	1,75%	1,89%	1,99%	2,60%	3,12%	3,35%	2,87%
<b>Profitability</b>										
ROE	Net income (loss) / average equity	21,9%	-5,7%	5,0%	24,6%	20,3%	9,7%	4,8%	2,8%	1,5%
EROE (cumulative, yearly average)	Equity / initial capital with corrections - 1	82,8%	24,1%	16,7%	19,5%	20,1%	18,4%	16,3%	14,6%	13,0%

**NOTE:** It has to be noted that towards the end of BAMC's lifetime yearly cash generation of 10% will not be possible anymore, mainly because realisation in the preceding years will substantially surpass this threshold. Nevertheless, BAMC will exceed the cumulative cash generated performance indicator in all years of its operations.

Direct transactional costs are costs directly related to sales of equity, real estate or claims and are recorded separately by BAMC.

Initial capital with corrections (denominator of EROE performance indicator), used by BAMC to assess its successfulness, represents the value of equity following decisions of the owner as presented in Table 2.