

CZECH NATIONAL BANK

**FINANCIAL STATEMENTS PREPARED
IN ACCORDANCE WITH INTERNATIONAL
ACCOUNTING STANDARDS**

31 DECEMBER 1998

REPORT OF INDEPENDENT AUDITORS

TO THE BANKING BOARD OF THE CZECH NATIONAL BANK

We have audited the accompanying balance sheet of the Czech National Bank (“ČNB”) as at 31 December 1998, and the related statements of income, changes in equity and cash flows for the year then ended. These financial statements are the responsibility of the management of ČNB. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion the accompanying financial statements present fairly, in all material respects, the financial position of ČNB as at 31 December 1998, and the results of its operations, its changes in equity and its cash flows for the year then ended in accordance with International Accounting Standards.

Without qualifying our opinion, we draw attention to the matters described in following paragraphs.

As set down in Note 11 of the Notes to the Financial Statements, ČNB’s assets include CZK 26,122 million of receivables from Národní banka Slovenska resulting from the separation of the assets and liabilities of the former Státní banka československá and from the losses resulting from the split of the federal currency. The ultimate collection of this receivable depends on the result of on-going negotiations between both parties. At present, it is not possible to evaluate the outcome.

30 April 1999

REPORT OF INDEPENDENT AUDITORS (continued)

As set down in Note 37 of the Notes to the Financial Statements, the Government has issued a guarantee to ČNB to cover potential losses on ultimate realisation of assets amounting to CZK 22,500 million which were acquired from certain commercial banks to provide stability to the banking sector. This guarantee was signed on 19 March 1997 and lasts for ten years from that date. ČNB is required to make provisions for these potential losses during the life of this guarantee in order to limit any final settlement arising from the guarantee. The necessary provisions, which depend on the factors affecting the realisability of the assets, will be created only when sufficient income to cover the provisions is earned. It is therefore not possible to estimate with reasonable accuracy the amount of provisions ČNB will create and the current fair value of these assets to ČNB.

30 April 1999

PricewaterhouseCoopers

PricewaterhouseCoopers Audit, s.r.o.

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

Income statement

(all amounts expressed in millions of CZK)

| | Note | Year ended 31 December 1998 | Year ended 31 December 1997 |
|---|------|--------------------------------|--------------------------------|
| Interest and discount income | | 57,450 | 40,909 |
| Interest expense | | <u>(55,881)</u> | <u>(34,065)</u> |
| Net interest income | 3 | 1,569 | 6,844 |
| Fee and commission income | | 513 | 552 |
| Fee and commission expense | | <u>(52)</u> | <u>(101)</u> |
| Net fee and commission income | | 461 | 451 |
| Foreign exchange (losses) / gains | 4 | (38,014) | 44,745 |
| Net loss from trading | 5 | (3,288) | (5,134) |
| Dividend income | | - | 37 |
| Other operating income | | <u>59</u> | <u>73</u> |
| Operating income | | (41,243) | 39,721 |
| Operating expenses | 6 | (2,563) | (6,563) |
| Provision for loan losses and other estimated losses and receivables written off | 8 | <u>(9,012)</u> | <u>(29,708)</u> |
| (Loss)/Profit | | <u>(50,788)</u> | <u>10,745</u> |

The following notes form an integral part of these financial statements.

(1)

CZECH NATIONAL BANK**FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS****31 DECEMBER 1998****Balance sheet**

(all amounts expressed in millions of CZK)

| | Note | Year ended <u>31 December 1998</u> | Year ended <u>31 December 1997</u> |
|--|------|---------------------------------------|---------------------------------------|
| ASSETS | | | |
| Cash and current accounts in other banks | 9 | 5,519 | 3,695 |
| Gold and other precious metals | 10 | 578 | 3,960 |
| Due from other banks | 11 | 91,398 | 209,325 |
| Treasury bills and other eligible bills | 12 | 167,431 | 141,870 |
| Dealing securities | 13 | 175,990 | 75,576 |
| Loans and advances to customers | 14 | 29,113 | 18,978 |
| Investment securities | 15 | 50 | 50 |
| Investments in unconsolidated subsidiary and associated undertakings | 16 | 17,178 | 3,845 |
| Membership quota at the IMF | 17 | 26,320 | 24,963 |
| Property and equipment | 18 | 6,860 | 5,644 |
| Other assets | 19 | <u>4,903</u> | <u>3,095</u> |
| Total assets | | <u>525,340</u> | <u>491,001</u> |
| LIABILITIES | | | |
| Due to other banks | 20 | 261,570 | 205,532 |
| Due to state | 21 | 28,370 | 26,825 |
| Due to customers | 22 | 36,657 | 44,744 |
| Debt securities in issue | 23 | 9,069 | 9,360 |
| Other borrowed funds | 24 | 16,671 | 14,339 |
| Due to the IMF | 17 | 26,320 | 24,963 |
| Currency in circulation | 25 | 146,060 | 139,145 |
| Other liabilities | 26 | <u>41,729</u> | <u>16,416</u> |
| Total liabilities | | <u>566,446</u> | <u>481,324</u> |
| SHAREHOLDERS' EQUITY | | | |
| Share capital fund | | 1,400 | 1,400 |
| Reserves | | 8,282 | 6,186 |
| (Accumulated losses) / Retained profits | | <u>(50,788)</u> | <u>2,091</u> |
| Total shareholders' equity | 29 | <u>(41,106)</u> | <u>9,677</u> |
| Total equity and liabilities | | <u>525,340</u> | <u>491,001</u> |

The following notes form an integral part of these financial statements.

(2)

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

Statement of changes in equity

(all amounts expressed in millions of CZK)

| | <u>Share capital fund</u> | <u>Reserves</u> | <u>Retained profits / (Losses)</u> | <u>Total / (Deficiency in) equity</u> |
|------------------------------------|-------------------------------|-----------------|--|---|
| Balance at 1 January 1997 | 1,400 | 6,222 | (8,654) | (1,032) |
| Transfer to statutory reserve | - | (36) | - | (36) |
| Profit for the year | - | - | <u>10,745</u> | <u>10,745</u> |
| Balance at 31 December 1997 | <u>1,400</u> | <u>6,186</u> | <u>2,091</u> | <u>9,677</u> |
| Balance at 1 January 1998 | 1,400 | 6,186 | 2,091 | 9,677 |
| Transfer to statutory reserve | - | 2,096 | (2,091) | 5 |
| Loss for the year | - | - | <u>(50,788)</u> | <u>(50,788)</u> |
| Balance at 31 December 1998 | <u>1,400</u> | <u>8,282</u> | <u>(50,788)</u> | <u>(41,106)</u> |

The following notes form an integral part of these financial statements.

(3)

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

Cash flow statement

(all amounts expressed in millions of CZK)

| | Year ended <u>31 December 1998</u> | Year ended <u>31 December 1997</u> |
|---|---------------------------------------|---------------------------------------|
| Cash flows from operating activities | | |
| Interest and commission receipts | 57,146 | 40,330 |
| Interest payments | (54,820) | (32,968) |
| Fee and commission receipts | 513 | 552 |
| Fee and commission payments | (52) | (101) |
| Other income received | 59 | 73 |
| Cash payments to employees and suppliers | (2,137) | (1,994) |
| Income taxes paid | <u>(1)</u> | <u>(3)</u> |
| Cash flows from operating profits before changes in operating assets and liabilities | <u>708</u> | <u>5,889</u> |
| Changes in operating assets and liabilities: | | |
| Net decrease in T-bills and other discounted securities | 34,369 | 27,981 |
| Net (increase)/decrease in dealing securities | (87,200) | 50,437 |
| Net decrease in loans and advances to banks | 18,005 | 19,999 |
| Net (increase) in loans and advances to customers | (10,136) | (15,064) |
| Net (increase) in membership quota at the IMF | (1,357) | (1,288) |
| Net (increase) in other assets | (13,229) | (35,216) |
| Net increase in deposits from other banks | 50,917 | 68,188 |
| Net increase/(decrease) in liabilities to state | 1,545 | (12,510) |
| Net (decrease) in amounts due to customers | (8,087) | (14,841) |
| Net increase in issue of money | 6,915 | 1,291 |
| Net (increase) in deposits from IMF | (1,357) | (1,288) |
| Net (decrease) in other liabilities | <u>(3,024)</u> | <u>(41,092)</u> |
| | <u>(12,639)</u> | <u>46,597</u> |
| Net cash from operating activities | <u>(11,931)</u> | <u>52,486</u> |

The following notes form an integral part of these financial statements.

(4)

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

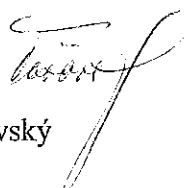
Cash flow statement (continued)

(all amounts expressed in millions of CZK)

| | Note | Year ended 31 December 1998 | Year ended 31 December 1997 |
|---|------|--------------------------------|--------------------------------|
| Cash flows from investing activities | | | |
| Purchase of property and equipment | | (1,805) | (695) |
| Proceeds from sale of property and equipment | | 12 | 15 |
| Purchase of investment securities | 10 | (13,333) | - |
| Proceeds from sales of gold | | <u>19,722</u> | <u>-</u> |
| Net cash used in investing activities | | <u>4,596</u> | <u>(680)</u> |
| Cash flows from financing activities | | | |
| Proceeds from borrowed funds and debt securities | | 19,717 | - |
| Repayments of borrowed funds and debt securities | | <u>(5,151)</u> | <u>(337)</u> |
| Net cash from financing activities | | <u>14,566</u> | <u>(337)</u> |
| Effect of exchange rate changes on cash and cash equivalents | | <u>(27,065)</u> | <u>28,173</u> |
| Net (decrease) / increase in cash and cash equivalents | | (19,834) | 79,642 |
| Cash and cash equivalents at beginning of year | | <u>277,384</u> | <u>197,742</u> |
| Cash and cash equivalents at end of year | 30 | <u>257,550</u> | <u>277,384</u> |

On behalf of ČNB:

Doc. Ing. Josef Tošovský
Governor



30 April 1999

The following notes form an integral part of these financial statements.

(5)

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

1 ACCOUNTING POLICIES

The Czech National Bank ("the Bank") is the Central bank of the Czech Republic. The Bank was established on 1 January 1993 following the dissolution of the Czech and Slovak Federal Republic as the successor, in the Czech Republic, to the State Bank of Czechoslovakia, the Central bank of the former federal republic.

Established as an independent institution under Act No. 6/1993 Col., "The Czech National Bank Act", the principal functions of the Bank are to ensure the stability of the Czech currency. The Bank is responsible for determining monetary policy, issuing bank notes and coins, controlling the money supply, settlement and supervision of the banking sector. The Bank provides banking services to the State, including the maintenance of the accounts of the state budget, state funds and state financial assets and liabilities. ČNB provides also loans to domestic commercial banks and selected companies within a limited range.

The Bank operates from its headquarters in Prague and seven branches located throughout the Czech Republic

The principal accounting policies adopted in the preparation of these financial statements are set out below:

(a) **Basis of presentation**

The financial statements are prepared in accordance with and comply with International Accounting Standards ("IAS"). The financial statements are prepared under the historical cost convention as modified by the revaluation of certain trading assets and liabilities to fair value.

The financial statements are reported in Czech Crowns (CZK) and all amounts are stated in millions.

(b) **Investment in unconsolidated subsidiary and associated undertakings**

Subsidiary undertakings are those companies in which the Bank, directly or indirectly, has an interest of more than one half of the voting rights or otherwise has power to exercise control over the operations. Investment in associated undertakings are those companies over which the Bank, directly or indirectly, has between 20% and 50% of the voting rights, and over which the Bank exercises significant influence, but which it does not control.

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

1 ACCOUNTING POLICIES (continued)

(b) Investment in unconsolidated subsidiary and associate undertakings (continued)

The only subsidiary undertaking is Česká finanční, s. r. o. ("CF"). Although CF is fully owned by the Bank, due to the fact that the Bank is, pursuant to the guarantee agreement described in Note 36, providing for the losses of CF covered by this agreement, the effect of consolidation of CF is, in the opinion of the Banking Board of the Bank, not material for the fair presentation of the financial position and results of the Bank and therefore CF has not been consolidated.

The associated undertaking Ceskoslovenska obchodni banka, a.s. was not accounted for under the equity method, as it is held exclusively for resale.

The associated undertaking Bankovní institut, a.s. has not been consolidated for reasons of materiality.

(c) Foreign currencies

Foreign currency transactions are accounted for at the exchange rates prevailing at the date of the transactions, gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies, are recognized in the income statement. Such balances are translated at year-end exchange rates.

(d) Derivative financial instruments

Foreign currency and interest rate swap agreements are entered into solely in connection with the management of the Bank's foreign currency position and interest rate risks arising from borrowings denominated in foreign currencies. Income or expense from interest rate and foreign currency swap agreements is recorded as interest income or expense over the lives of the agreements in the profit and loss account. A similar procedure applies for swap operations with gold. The Bank also enters into options and forward operations.

(e) Interest and discount income and expense

Interest income and expense are recognised in the income statement on an accruals basis.

(f) Gold and other precious metals

Gold and other precious metals are held for investment purposes and are stated at historical cost.

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

1 ACCOUNTING POLICIES (continued)

(g) Dealing securities

Dealing securities are stated at lower of cost and market value on a portfolio basis. All gains and losses realised and provisions for unrealised losses from trading in dealing securities are reported in net trading income. Interest earned whilst holding dealing securities is reported as interest income. Dividends received are included separately in dividend income. Dealing securities include securities sold under sale and repurchase agreements.

Debt securities issued by the Bank are described in Note 23.

(h) Sale and repurchase agreements

Securities sold under sale and repurchase agreements ('repos') are retained in the financial statements and the counterparty liability is included in deposits from banks or customers as appropriate. Securities purchased under agreements to resell ('reverse repos') are recorded as loans and advances to other banks or customers as appropriate. The difference between sale and repurchase price is treated as interest and accrued evenly over the life of repo and reverse repo agreements.

(i) Investment securities

Investment securities include debt which management of the Bank intends to hold until maturity and equity securities which management of the Bank intends to hold in perpetuity are stated at cost as adjusted for the amortisation of premiums or discounts on purchases over the period to maturity. Interest earned on investment securities is reported as interest income. Dividends received are included in the gains less losses from investment securities. A reduction in market value is not taken into account unless it is considered to be permanent.

(j) Membership quota at the IMF

The membership quota of the International Monetary Fund (IMF) is denominated in Special Drawing Rights and is translated to CZK at the last rate advised by the IMF.

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

1 ACCOUNTING POLICIES (continued)

(k) Receivables and provisions for impairment

A specific credit risk provision for loan impairment is established to provide for the Bank management's estimate of credit losses as soon as the recovery of an exposure is identified as doubtful.

In the case of receivables from borrowers in countries where there is an increased risk of difficulties in servicing external debt, an assessment of the political and economic situation is made, and additional country risk provisions are established as necessary.

When a loan is deemed uncollectable, it is written off against the related provision for impairments. Subsequent recoveries are credited to the income statement if previously written off.

(l) Fixed assets

All property, equipment, intangible assets and other assets are stated at historical cost less depreciation. Land is not depreciated.

Depreciation is calculated on the straight line method to write off the cost of each asset to their residual values over their estimated useful life as follows:

| | |
|---|----------|
| Office equipment and personal computers | 3 years |
| Software | 4 years |
| Motor vehicles | 8 years |
| Equipment | 8 years |
| Buildings | 45 years |

Fixed assets at purchase price from CZK 1,000 to CZK 40,000 are fully written off to expenses after commencement of use; they are recorded in tangible and intangible fixed assets including the related depreciation / amortisation. Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Gains and losses on disposal of property and equipment are determined by reference to their carrying amount and are taken into account in determining operating profit. Repairs and renewals are charged to the income statement when the expenditure is incurred.

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

1 ACCOUNTING POLICIES (continued)

(m) Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than 90 days maturity from the date of acquisition including: cash and balances with central banks, treasury bills and other eligible bills, amounts due from other banks and dealing securities.

(n) Bills issued

Bills issued by the Bank are recorded at their nominal value. Any related discount or premium is recorded net in other assets or other liabilities respectively and charged to interest expense or interest income over the life of the bills issued. The nominal amount of bills issued is reduced by bills from repos closed, bills and the nominal value is adjusted for amortised discount or premium.

(o) Pension obligations

The Bank does not operate any defined benefit and defined contribution plans.

(p) Provisions

Provisions are recognised when the Bank has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

(q) Taxation

The Bank is exempt from the payment of income tax under the provisions of article 17 section 2 of the ČNR Act No. 586/92 Coll., as amended.

The net profit after budgeted usage and distribution to the statutory reserve fund and to other funds from profit represents a contribution to the state budget. Distribution of profit is made according to the decision of the Banking Board.

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

1 ACCOUNTING POLICIES (continued)

(r) Comparatives

Where necessary, comparative figures have been adjusted to conform with changes in presentation in the current year. In particular, the comparatives have been adjusted to take into account the requirements of the following revised or new International Accounting Standards which the Bank implemented in 1998, in advance of their effective dates:

IAS 1 – Presentation of financial statements

IAS 14 – Segment reporting

IAS 36 – Impairment of Assets

IAS 37 – Provisions, Contingent Liabilities and Contingent Assets

IAS 38 – Intangible Assets

There are no changes in accounting policy that affect operating profit resulting from the adoption of the above standards in these financial statements, as the Bank was already following the recognition and measurement principles in those standards.

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

(In the notes all amounts are shown in millions of CZK unless otherwise stated)

2 SEGMENTAL REPORTING

Year ended 31 December 1998

| | <u>Central bank activities</u> | <u>Stabilisation of the banking sector</u> | <u>Total</u> |
|---|--------------------------------|--|--------------|
| Operating result | (21,526) | (19,717) | (41,243) |
| Segment result | (24,693) | (26,095) | (50,788) |
| Segment assets | 462,005 | 63,335 | 525,340 |
| Segment liabilities | 514,065 | 52,381 | 566,446 |
| Capital expenditure | 1,805 | - | 1,805 |
| Depreciation | 454 | - | 454 |
| Creation of provision for loan losses and other estimated losses | 2,648 | 6,364 | 9,012 |

Year ended 31 December 1997

| | <u>Central bank activities</u> | <u>Stabilisation of the banking sector</u> | <u>Total</u> |
|---|--------------------------------|--|--------------|
| Operating result | 39,703 | 18 | 39,721 |
| Segment result | 41,250 | (30,505) | 10,745 |
| Segment assets | 457,194 | 33,807 | 491,001 |
| Segment liabilities | 467,967 | 13,357 | 481,324 |
| Capital expenditure | 695 | - | 695 |
| Depreciation | 516 | - | 516 |
| Creation of provision for loan losses and other estimated losses | 2,960 | 26,748 | 29,708 |

The Bank's activities can be split between following segments:

- Central bank activities – administration of Czech currency in respect of foreign exchange rate and currency of circularisation, administration of foreign currency reserves and banking sector supervision.
- Stabilisation of the banking sector – see detail in Notes 36 and 37.

All assets and liabilities comprise operating assets and liabilities, which arose from operations in the Czech Republic.

CZECH NATIONAL BANK

**FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING
STANDARDS**

31 DECEMBER 1998

3 INTEREST INCOME

| | <u>1998</u> | <u>1997</u> |
|-------------------------------------|---------------|---------------|
| Interest and discount income | | |
| Due from banks | 13,950 | 17,467 |
| Debt securities and gold deposits | 37,884 | 21,309 |
| Loan to CF | 2,605 | 613 |
| Other | <u>3,011</u> | <u>1,520</u> |
| | <u>57,450</u> | <u>40,909</u> |
| Interest expense | | |
| Due to banks | 22,150 | 10,697 |
| Due to state | 4,867 | 6,160 |
| Due to customers | 161 | 535 |
| Issued T-bills | 26,895 | 15,026 |
| Other | <u>1,808</u> | <u>1,647</u> |
| | <u>55,881</u> | <u>34,065</u> |
| Net interest income | <u>1,569</u> | <u>6,844</u> |

4 FOREIGN EXCHANGE GAINS AND LOSSES

| | <u>1998</u> | <u>1997</u> |
|-------------------------|-----------------|----------------|
| Foreign exchange gains | 941 | 46,704 |
| Foreign exchange losses | <u>(38,955)</u> | <u>(1,959)</u> |
| Net result | <u>(38,014)</u> | <u>44,745</u> |

5 NET LOSS FROM TRADING

| | <u>1998</u> | <u>1997</u> |
|---|-----------------|----------------|
| Income from sale of gold | 16,433 | - |
| Realised gains less losses from the trading portfolio | 121 | (5,197) |
| Net creation of provisions for trading securities | <u>(19,842)</u> | <u>63</u> |
| | <u>(3,288)</u> | <u>(5,134)</u> |

CZECH NATIONAL BANK

**FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING
STANDARDS**

31 DECEMBER 1998

6 OPERATING EXPENSES

| | <u>1998</u> | <u>1997</u> |
|--|--------------|--------------|
| Staff costs (Note 7) | 614 | 608 |
| Cost of issue of notes and coins | 297 | 366 |
| Professional services | 481 | 461 |
| Depreciation | 454 | 516 |
| Loss on sale of property and equipment | 5 | - |
| Rentals | 394 | 369 |
| Other | <u>318</u> | <u>4,243</u> |
| | <u>2,563</u> | <u>6,563</u> |

Other expenses in 1997 included CZK 3,838 million representing losses from receivables sold to CF.

7 STAFF COSTS

| | <u>1998</u> | <u>1997</u> |
|-----------------------|-------------|-------------|
| Wages and salaries | 442 | 444 |
| Social security costs | 131 | 124 |
| Other social costs | <u>41</u> | <u>40</u> |
| | <u>614</u> | <u>608</u> |

The average number of persons employed by the Bank during the year was 1,511 (1997: 1,704).

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

8 PROVISIONS FOR LOAN LOSSES AND OTHER ESTIMATED LOSSES

| | Due from banks (Note 11) | Due from clients (Note 14) | Other reserves (Note 26) | Total |
|------------------------------------|--------------------------------|----------------------------------|--------------------------------|----------------------|
| Balance at 31 December 1997 | 34,846 | 667 | 13,419 | 48,932 |
| Additions | 32,020 | 3,252 | 5,517 | 40,789 |
| Release | (31,236) | (359) | (183) | (31,778) |
| Reclassification * | <u>(18,900)</u> | <u>-</u> | <u>18,900</u> | <u>-</u> |
| Balance at 31 December 1998 | <u>16,730</u> | <u>3,560</u> | <u>37,653</u> | <u>57,943</u> |

* The provision of CZK 18,900 million was created in 1997 as a specific provision for loans and in 1998 it was transferred to provision for the unrealised losses arising from decline in value of CF assets due to transfer of certain loans from the Bank to CF (Note 36).

The provisions for securities are analysed in Notes 12 and 13.

9 CASH AND CURRENT ACCOUNTS IN OTHER BANKS

| | <u>1998</u> | <u>1997</u> |
|---------------------------------|---------------------|---------------------|
| Cash in hand | 904 | 2,072 |
| Current accounts of other banks | 3,865 | 752 |
| Short term deposits | <u>750</u> | <u>871</u> |
| | <u>5,519</u> | <u>3,695</u> |

Geographic sector risk concentrations within the current accounts in other banks were as follows:

| | <u>1998</u> | <u>1998</u> % | <u>1997</u> | <u>1997</u> % |
|--------------------------|---------------------|-------------------|---------------------|-------------------|
| Czech Republic | 4,739 | 85 | 2,758 | 75 |
| Other European countries | 25 | 1 | 52 | 1 |
| Canada and USA | 751 | 14 | 880 | 24 |
| Japan | 4 | - | 3 | - |
| Other countries | <u>-</u> | <u>-</u> | <u>2</u> | <u>-</u> |
| | <u>5,519</u> | <u>100</u> | <u>3,695</u> | <u>100</u> |

CZECH NATIONAL BANK

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31 DECEMBER 1998

10 GOLD AND OTHER PRECIOUS METALS

| | <u>1998</u> | <u>1997</u> |
|-----------------------|-------------|--------------|
| Gold | 541 | 3,922 |
| Other precious metals | <u>37</u> | <u>38</u> |
| | <u>578</u> | <u>3,960</u> |

The market value of gold was CZK 2,488 million as at 31 December 1998 and CZK 20,838 million as at 31 December 1997. During 1998 58 tons of gold were sold and a gain of CZK 16,433 million was realised (Note 5).

11 DUE FROM OTHER BANKS

| | <u>1998</u> | <u>1997</u> |
|--|-----------------|-----------------|
| Placements with other banks | 15,643 | 59,169 |
| Sale and repurchase agreements | 16,356 | 60,148 |
| Loans to banks | 34,419 | 57,152 |
| Loss loans | 14 | 22,644 |
| Other receivables from banks | <u>41,696</u> | <u>45,058</u> |
| Due from other banks in total | 108,128 | 244,171 |
| Less specific provision for impairment | <u>(16,730)</u> | <u>(34,846)</u> |
| | <u>91,398</u> | <u>209,325</u> |

Other receivables from banks include CZK 26,122 million of receivables from Národná banka Slovenska resulting from the separation of the assets and liabilities of the former Státní banka československá into the central banks of Czech Republic and Slovak Republic and from the losses resulting from the split of the federal currency. The ultimate collection of this receivable depends on the result of on-going negotiations between both parties. At present, it is not possible to evaluate the outcome.

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11 DUE FROM OTHER BANKS (continued)

Geographic sector risk concentrations within the receivables from other banks were as follows:

| | <u>1998</u> | <u>1998</u> % | <u>1997</u> | <u>1997</u> % |
|--------------------------|----------------|------------------|----------------|------------------|
| Czech Republic | 50,002 | 46 | 98,445 | 40 |
| Slovak Republic | 26,122 | 24 | 26,122 | 11 |
| Other European countries | 25,203 | 23 | 106,294 | 44 |
| Canada and USA | <u>6,801</u> | <u>7</u> | <u>13,310</u> | <u>5</u> |
| | <u>108,128</u> | <u>100</u> | <u>244,171</u> | <u>100</u> |

12 TREASURY BILLS AND OTHER ELIGIBLE BILLS

| | <u>1998</u> | <u>1997</u> |
|--|----------------|----------------|
| Treasury bills | 91,607 | 40,293 |
| Other eligible bills | <u>75,826</u> | <u>101,582</u> |
| Treasury bills and other eligible bills in total | 167,433 | 141,875 |
| Provisions | <u>(2)</u> | <u>(5)</u> |
| | <u>167,431</u> | <u>141,870</u> |

Geographic sector risk concentrations within the treasury bills and other eligible bills were as follows:

| | <u>1998</u> | <u>1998</u> % | <u>1997</u> | <u>1997</u> % |
|--------------------------|----------------|------------------|----------------|------------------|
| Italy | 30,339 | 18 | - | - |
| Switzerland | 71,194 | 43 | 102,553 | 72 |
| Other European countries | 11,917 | 7 | 12,312 | 9 |
| Japan | <u>53,983</u> | <u>32</u> | <u>27,010</u> | <u>19</u> |
| | <u>167,433</u> | <u>100</u> | <u>141,875</u> | <u>100</u> |

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13 DEALING SECURITIES

| | <u>1998</u> | <u>1997</u> |
|--|-----------------|---------------|
| Government bonds | 174,390 | 84,594 |
| Other debt securities | 4,230 | 7,338 |
| Other debt securities in REPO transactions | (6,799) | (18,254) |
| Coupons | 4,430 | 1,021 |
| Shares | 19,717 | - |
| Bonds transferred for received loans assurance | <u>-</u> | <u>1,027</u> |
| Debt securities in total | 195,968 | 75,726 |
| Provisions | <u>(19,978)</u> | <u>(150)</u> |
| | <u>175,990</u> | <u>75,576</u> |

Shares in GE Capital Bank, a.s. of purchase price CZK 20 million has been provided against in the amount of CZK 20 million. The net book value of the shares represents their nominal value.

Bonds transferred for received loans assurance were pledged under repurchase agreements with other banks whose market value at 31 December 1997 was CZK 1,030 million. This type of securities were not pledged as at 31 December 1998.

Geographic sector risk concentrations within the dealing securities were as follows:

| | <u>1998</u> | <u>1998</u> | <u>1997</u> | <u>1997</u> |
|--------------------------|----------------|-------------|---------------|-------------|
| | | % | | % |
| Czech Republic | 19,717 | 10 | - | - |
| Germany | 42,504 | 22 | 24,556 | 32 |
| France | 31,519 | 16 | - | - |
| Italy | 27,708 | 14 | - | - |
| USA | 44,465 | 23 | 14,984 | 20 |
| Other European countries | <u>30,055</u> | <u>15</u> | <u>36,186</u> | <u>48</u> |
| | <u>195,968</u> | <u>100</u> | <u>75,726</u> | <u>100</u> |

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14 LOANS AND ADVANCES TO CUSTOMERS

| | <u>1998</u> | <u>1997</u> |
|---|----------------|---------------|
| Loans in respect of the stabilisation of the banking sector | 13,008 | 8,774 |
| Loans to CF | 18,567 | 9,638 |
| Other | <u>1,098</u> | <u>1,233</u> |
| Gross loans and advances | 32,673 | 19,645 |
| Less specific provisions for impairment | <u>(3,560)</u> | <u>(667)</u> |
| | <u>29,113</u> | <u>18,978</u> |

Movements in provisions for impairment are as follows:

| | <u>Specific provisions</u> | <u>General provision</u> |
|------------------------------------|----------------------------|--------------------------|
| Balance at 1 January 1997 | 1,186 | 52 |
| Charge for provisions | 104 | 10 |
| Release of provisions | <u>(623)</u> | <u>-</u> |
| Balance at 31 December 1997 | <u>667</u> | <u>62</u> |
| Charge for provisions | 2,929 | 10 |
| Release of provisions | <u>(36)</u> | <u>(11)</u> |
| Balance at 31 December 1998 | <u>3,560</u> | <u>61</u> |

All loans within the loan portfolio were granted to entities in the Czech Republic.

Loans and advances are further analysed as a part of the balance sheet in the following notes: Currency risk (Note 32), Interest rate risk (Note 33), Liquidity risk (Note 34) and Related party transactions (Note 35).

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15 INVESTMENT SECURITIES

The Bank has in its portfolio 5,330 shares of the Bank for International Settlements in Basle, which represents 1.1% of issued shares. These equity securities are unlisted.

16 INVESTMENT IN UNCONSOLIDATED SUBSIDIARY AND ASSOCIATE UNDERTAKINGS

| | <u>1998</u> | | <u>1997</u> | |
|--------------------------------------|---------------|--------------|--------------|--------------|
| | | % | | % |
| Bankovní institut, a.s. | 11 | 29.9 | 11 | 29.9 |
| Československá obchodní banka, a. s. | 1,353 | 26.5 | 1,353 | 26.5 |
| CF (Note 36) | <u>15,814</u> | <u>100.0</u> | <u>2,481</u> | <u>100.0</u> |
| | <u>17,178</u> | | <u>3,845</u> | |
| | | % | | |
| Investment in CF | | | | |
| Opening balance at 1 January 1998 | 2,481 | 100 | | |
| Capital increase during the year | <u>13,333</u> | _____ | | |
| Closing balance at 31 December 1998 | <u>15,814</u> | <u>100</u> | | |

The Bank increased CF's capital in order to enable CF to fund acquisitions of investments.

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17 MEMBERSHIP QUOTA AND PAYABLES AT THE IMF

| | <u>1998</u> | <u>1997</u> |
|-------------------------------|---------------|---------------|
| Membership quota at the IMF | <u>26,320</u> | <u>24,963</u> |
| Total receivable from the IMF | <u>26,320</u> | <u>24,963</u> |
| Payable to the IMF | 26,254 | 24,900 |
| IMF current account | <u>66</u> | <u>63</u> |
| Total payable to the IMF | <u>26,320</u> | <u>24,963</u> |

The Bank administers a membership in the IMF, denominated in special drawing rights, which was funded through the issuance of bills of exchange, payable upon demand. Pursuant to this membership the amounts of CZK 26,320 million and CZK 24,963 million as at 31 December 1998 and 1997, respectively are maintained at the IMF. IMF holds deposits of the same amount with the Bank.

18 PROPERTY AND EQUIPMENT

| | <u>Buildings</u> | <u>Other</u> | <u>Software</u> | <u>Total</u> |
|-------------------------------------|------------------|--------------|-----------------|--------------|
| At 31 December 1997 | | | | |
| Cost | 2,695 | 4,324 | 418 | 7,437 |
| Accumulated depreciation | <u>240</u> | <u>1,373</u> | <u>180</u> | <u>1,793</u> |
| Net book amount | <u>2,455</u> | <u>2,951</u> | <u>238</u> | <u>5,644</u> |
| Year ended 31 December 1998 | | | | |
| Opening net book amount | 2,455 | 2,951 | 238 | 5,644 |
| Additions | 940 | 2,368 | 427 | 3,735 |
| Disposals | 730 | 1,004 | 331 | 2,065 |
| Depreciation charge | <u>56</u> | <u>300</u> | <u>98</u> | <u>454</u> |
| Closing net book amount | <u>2,609</u> | <u>4,015</u> | <u>236</u> | <u>6,860</u> |
| At 31 December 1998 | | | | |
| Cost | 2,905 | 5,688 | 514 | 9,107 |
| Accumulated depreciation | <u>296</u> | <u>1,673</u> | <u>278</u> | <u>2,247</u> |
| Net book amount at 31 December 1998 | <u>2,609</u> | <u>4,015</u> | <u>236</u> | <u>6,860</u> |

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18 PROPERTY AND EQUIPMENT (continued)

Advances paid for reconstruction of buildings of CZK 2,763 million at 31 December 1998 (31 December 1997: CZK 1,340 million) are included in Other property and equipment.

19 OTHER ASSETS

| | <u>1998</u> | <u>1997</u> |
|-----------------------|--------------|--------------|
| Advances paid | 4,086 | 1,402 |
| Prepaid expenses | 271 | 422 |
| Accrued income | 304 | 652 |
| Other | <u>246</u> | <u>622</u> |
| Other assets in total | 4,907 | 3,098 |
| Provisions | <u>(4)</u> | <u>(3)</u> |
| | <u>4,903</u> | <u>3,095</u> |

20 DUE TO OTHER BANKS

| | <u>1998</u> | <u>1997</u> |
|--|----------------|----------------|
| Statutory minimum reserves of domestic banks | 86,606 | 89,830 |
| Deposits on demand from other banks | 10,464 | 14,158 |
| Term deposits from other banks | 44 | 44 |
| Loans in respect of sale and repurchase agreements | <u>164,456</u> | <u>101,500</u> |
| | <u>261,570</u> | <u>205,532</u> |

21 DUE TO STATE

| | <u>1998</u> | <u>1997</u> |
|--------------|---------------|---------------|
| State assets | 22,942 | 26,038 |
| State funds | <u>5,428</u> | <u>787</u> |
| | <u>28,370</u> | <u>26,825</u> |

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22 DUE TO CUSTOMERS

| | <u>1998</u> | <u>1997</u> |
|-------------------------------|---------------|---------------|
| Current accounts | 15,486 | 18,115 |
| Term deposits | 16,330 | 22,732 |
| Accounts of local authorities | <u>4,841</u> | <u>3,897</u> |
| | <u>36,657</u> | <u>44,744</u> |

23 DEBT SECURITIES IN ISSUE

| | <u>Average interest rate</u> % | <u>1998</u> | <u>1997</u> |
|--|-----------------------------------|------------------|------------------|
| Medium term issue in JPY | 6.6 | 9,069 | 9,360 |
| CNB bills | | 350,000 | 150,000 |
| Accrued interest expense | | <u>(9,808)</u> | <u>(3,702)</u> |
| | | 349,261 | 155,658 |
| Less: | | | |
| CNB bills repurchased: | | | |
| – held in the T-bills portfolio | | (176,646) | (43,674) |
| – under sale and repurchase agreements | | <u>(163,546)</u> | <u>(102,624)</u> |
| | | <u>9,069</u> | <u>9,360</u> |

The Bank has entered into swap transactions to hedge foreign currency exchange and interest rate risk related to bonds issued in JPY. Based on the swap agreement the Bank pays interest in DEM (8.6% for the amount of DEM 239 million and 6m LIBOR + 2.13% for the amount of DEM 318 million) and receives fixed interest in JPY corresponding with the interest payments on the bonds denominated in JPY (6.6% for the amount of JPY 35,000 million). These swap transactions mature on 8 August 2000, concurrent with the maturity of the bonds. At the maturity of these swap transactions, the Bank receives JPY 35,070 million and pays DEM 534 million.

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24 OTHER BORROWED FUNDS

| | <u>Interest rate</u> % | <u>1998</u> | <u>1997</u> |
|--|---------------------------|---------------|---------------|
| Loan in respect of gold swap | - | - | 11,072 |
| Loan in respect of stabilisation of the Czech banking sector | 14.04 | 14,788 | - |
| Loan from Export-Import Bank of Japan | 4.60 | 1,670 | 1,946 |
| Other loans received | - | <u>213</u> | <u>1,321</u> |
| | | <u>16,671</u> | <u>14,339</u> |

Export-Import Bank of Japan (EXIM Bank)

Long-term debt represents advances under the loan facility between the Czech and Slovak Federal Republic and the EXIM Bank entered into on 9 December 1991. This loan facility is advanced under a USD 450 million loan agreement with the World Bank, available in various currencies for the purpose of providing funding export activity by commercial banks in the Czech Republic. This loan agreement appoints the Bank as the loan administrator. The loan facility provides for advances under three tranches.

| Tranche <u>amount</u> JPY | Advance <u>date</u> | Advance <u>amount</u> JPY | Balance at <u>31 December 1998</u> CZK | Interest <u>rate</u> % | Balance at <u>31 December 1997</u> CZK |
|---------------------------------|------------------------|---------------------------------|--|------------------------------|--|
| 1,500 | 9 March 1993 | 4,366,000 | 1,002 | 4.7 | 1,168 |
| 7,500 | 1 February 1995 | 1,455,000 | 334 | 4.7 | 389 |
| 7,500 | 17 July 1995 | 1,455,000 | <u>334</u> | 2.5 | <u>389</u> |
| | | | <u>1,670</u> | | <u>1,946</u> |

The interest rate on advances under this facility is the Japanese long-term prime lending rate prevailing on the disbursement date minus 0.2%. Required semi-annual repayments of JPY 1,289 billion commenced on 15 March 1997 and were based on the total amount advanced. Prepayments in multiples of JPY 1 million may be made upon 30 days notice with payment of a penalty of 0.5% of the amount prepaid. The Bank pays a commitment fee on the unused portion of the loan facility of 0.5% p. a.

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24 OTHER BORROWED FUNDS (continued)

European Investment Bank (EIB)

The remaining balance of long-term borrowings of CZK 213 million as at 31 December 1998 and CZK 242 million as at 31 December 1997 consists of an advance from the EIB denominated in ECU under a loan agreement allowing for advances of up to ECU 57 million. This agreement provided for funding of specific projects approved by the Bank and expired in February 1996. Repayment is due semi-annually commencing on 15 August 1998 at a rate of 5% of the total balance advanced, with the final payment due on 15 February 2008. The interest rate of this loan was 7.05% as at 31 December 1998.

Loans advanced by the Bank to commercial banks under the EXIM Bank and EIB loan facilities totalled CZK 1,963 million and CZK 2,347 million as at 31 December 1998 and 1997, respectively.

Geographic sector risk concentrations within dealing securities were as follows:

| | <u>1998</u> | <u>1998</u> | <u>1997</u> | <u>1997</u> |
|--------------------|---------------|-------------|---------------|-------------|
| | | % | | % |
| Great Britain | - | - | 1,613 | 11 |
| Switzerland | - | - | 5,306 | 37 |
| European countries | 213 | 1 | 2,470 | 17 |
| USA | 14,788 | 89 | 3,004 | 21 |
| Japan | <u>1,670</u> | <u>10</u> | <u>1,946</u> | <u>14</u> |
| | <u>16,671</u> | <u>100</u> | <u>14,339</u> | <u>100</u> |

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25 CURRENCY IN CIRCULATION

One of the Bank's central bank activities is administration of Czech currency in respect of foreign exchange rate and currency of circulation.

The following table summarises movements in the balance of currency in circulation:

| | <u>1998</u> | <u>1997</u> |
|--------------------------------|-----------------|-----------------|
| Balance at 1 January 1998 | 139,146 | 137,854 |
| Currency produced during 1998 | 52,761 | 59,947 |
| Currency removed during 1998 | <u>(45,847)</u> | <u>(58,656)</u> |
| Balance as at 31 December 1998 | <u>146,060</u> | <u>139,145</u> |

26 OTHER LIABILITIES

| | <u>1998</u> | <u>1997</u> |
|-------------------------------|---------------|---------------|
| Creditors | 347 | 507 |
| Accruals | 1,073 | 1,097 |
| Other reserves and provisions | 37,653 | 13,419 |
| Other | <u>2,656</u> | <u>1,393</u> |
| | <u>41,729</u> | <u>16,416</u> |

27 CONTINGENT LIABILITIES AND COMMITMENTS

Legal Proceedings

As at 31 December 1998 there was a legal proceeding outstanding against the Bank. The Directors of the Bank decided to create a 100% provision to cover the potential loss amounting to CZK 822 million.

Capital commitments

At 31 December 1998 the Bank had capital commitments from reconstruction of CZK 1,546 million (1997: CZK 2,087 million) in respect of buildings and equipment purchases.

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27 CONTINGENT LIABILITIES AND COMMITMENTS (continued)

Other

As at 31 December 1998 the amount of guarantees issued by the Bank was CZK 79,423 million (31 December 1997: CZK 75,170 million).

28 DERIVATIVE FINANCIAL INSTRUMENTS

| | <u>1998</u> | <u>1997</u> |
|--------------------------------------|-------------|-------------|
| Receivables under swaps | 9,069 | 9,360 |
| Payables under swaps | 9,962 | 10,777 |
| Receivables under forward operations | 60,287 | 32,810 |
| Payables under forward operations | 61,767 | 32,900 |
| Receivables under options | 4,451 | 22,539 |
| Payables under options | 4,451 | 22,408 |
| Receivables under spot operations | 1,200 | - |
| Payables under spot operations | - 1,199 | - |

The previous table provides a detailed breakdown of the contractual or notional amounts of the Bank's derivative financial instruments outstanding at year end as described below. These instruments, comprising foreign exchange and interest rate derivatives allow the Bank to transfer, modify or reduce foreign exchange and interest rate risks. These instruments are exclusively used by the Bank to hedge its foreign exchange and interest rate risk arising from its operations, hence, in the opinion of the Banking Board, it is not considered necessary to provide the fair values of the instruments.

More details on swap operations are included in Note 23.

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29 CAPITAL, RESERVES AND OTHER FUNDS

The Bank's capital is comprised of a statutory fund of CZK 1,400 million. In addition to the statutory fund the Bank maintains capital and reserve funds totalling CZK 8,282 million and a profit and loss reserve of CZK 50,788 million.

| | <u>1998</u> | <u>1997</u> |
|------------------------------|-----------------|----------------|
| Share capital fund | 1,400 | 1,400 |
| Statutory reserve | 7,773 | 5,759 |
| Other capital fund | 292 | 260 |
| Other reserve fund | 217 | 167 |
| (Loss) / profit for the year | (50,788) | 10,745 |
| Accumulated losses | <u>-</u> | <u>(8,654)</u> |
| | <u>(41,106)</u> | <u>9,677</u> |

30 CASH AND CASH EQUIVALENTS

For the purposes of the cash flow statement, cash and cash equivalents comprises the following balances with less than 90 days maturity:

| | <u>1998</u> | <u>1997</u> |
|--|----------------|----------------|
| Cash and current accounts in other banks (from Note 9) | 5,519 | 3,695 |
| Due from other banks (from Note 11) | 47,686 | 147,608 |
| Treasury bills and other eligible bills (from Note 12) | 149,104 | 84,054 |
| Dealing securities (from Note 13) | <u>55,241</u> | <u>42,027</u> |
| | <u>257,550</u> | <u>277,384</u> |

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31 CREDIT RISK

Geographical concentrations of assets, liabilities and off balance sheet items

| | <u>Total assets</u> | <u>Total liabilities</u> | <u>Off balance sheet items</u> |
|-------------------------------|---------------------|--------------------------|--------------------------------|
| As at 31 December 1998 | | | |
| Czech Republic | 139,382 | 508,669 | - |
| Germany | 42,402 | - | - |
| Switzerland | 71,194 | - | - |
| France | 31,519 | - | - |
| Italy | 58,047 | - | - |
| Slovak Republic | 9,754 | - | - |
| Other European countries | 67,132 | 213 | (20,655) |
| Canada and USA | 51,923 | 14,788 | (27,518) |
| Japan | <u>53,987</u> | <u>1,670</u> | <u>50,546</u> |
| | <u>525,340</u> | <u>525,340</u> | <u>2,373</u> |
| | | | |
| As at 31 December 1997 | | | |
| Czech Republic | 140,626 | 476,662 | 31,354 |
| Germany | 24,456 | - | - |
| Switzerland | 102,553 | 5,306 | - |
| Great Britain | - | 1,613 | - |
| Slovak Republic | 12,388 | - | - |
| Other European countries | 154,839 | 2,470 | (6,519) |
| Canada and USA | 29,124 | 3,004 | (24,295) |
| Japan | 27,013 | 1,946 | 836 |
| Other countries | <u>2</u> | <u>-</u> | <u>-</u> |
| | <u>491,001</u> | <u>491,001</u> | <u>1,376</u> |

As an active participant in the international banking markets, the Bank has a significant concentration of credit risk with other financial institutions. In total, credit risk exposure to financial institutions was estimated to have amounted to CZK 176,890 million at 31 December 1998 (31 December 1997: CZK 210,948 million).

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31 CREDIT RISK (continued)

The credit risk results mainly from the Consolidation programme (see details in Notes 36 and 37), which is closely connected with the supervision and assurance of stability of the Czech banking sector, and from sale and repurchase agreements. The credit risk from sale and repurchase agreements is limited because the loans are secured by pledged liquid securities (mostly by CNB T-bills).

32 CURRENCY RISK

Concentrations of assets, liabilities and off balance sheet items

The Bank had the following significant currency positions:

| | CZK | ECU | USD | DEM | JPY | Other | Total |
|--|-----------------------|----------------------|----------------------|-----------------------|----------------------|----------------------|-----------------------|
| As at 31 December 1998 | | | | | | | |
| Assets | | | | | | | |
| Cash and current accounts in other banks | 4,703 | 3 | 752 | 4 | 4 | 53 | 5,519 |
| Gold and other precious metals | 578 | - | - | - | - | - | 578 |
| Due from other banks | 31,309 | 26,890 | 7,850 | 17,764 | 7,585 | - | 91,398 |
| Treasury bills and other eligible bills | - | 700 | 24,915 | 57,688 | 53,980 | 30,148 | 167,431 |
| Dealing securities | - | 34,584 | 53,422 | 58,940 | - | 29,044 | 175,990 |
| Loans and advances to customers | 29,113 | - | - | - | - | - | 29,113 |
| Investment securities | - | - | - | - | - | 50 | 50 |
| Investments in unconsolidated subsidiary and associated undertakings | 17,178 | - | - | - | - | - | 17,178 |
| Membership quota at the IMF | 26,320 | - | - | - | - | - | 26,320 |
| Fixed assets | 6,860 | - | - | - | - | - | 6,860 |
| Other assets | <u>4,600</u> | <u>-</u> | <u>19</u> | <u>30</u> | <u>254</u> | <u>-</u> | <u>4,903</u> |
| Total assets | <u>120,661</u> | <u>62,177</u> | <u>86,958</u> | <u>134,426</u> | <u>61,823</u> | <u>59,295</u> | <u>525,340</u> |

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32 CURRENCY RISK (continued)

| | CZK | ECU | USD | DEM | JPY | Other | Total |
|---|------------------|---------------|-----------------|-----------------|----------------|---------------|-----------------|
| Liabilities | | | | | | | |
| Due to other banks | 261,570 | - | - | - | - | - | 261,570 |
| Due to state | 28,370 | - | - | - | - | - | 28,370 |
| Due to customers | 35,195 | 32 | - | 1,429 | - | 1 | 36,657 |
| Debt securities in issue | - | - | - | - | 9,069 | - | 9,069 |
| Other borrowed funds | 14,788 | - | - | 213 | 1,670 | - | 16,671 |
| Due to the IMF | 26,320 | - | - | - | - | - | 26,320 |
| Currency in circulation | 146,060 | - | - | - | - | - | 146,060 |
| Other liabilities | <u>40,290</u> | <u>-</u> | <u>-</u> | <u>10,245</u> | <u>(8,806)</u> | <u>-</u> | <u>41,729</u> |
| Total liabilities | <u>552,593</u> | <u>32</u> | <u>-</u> | <u>11,887</u> | <u>1,933</u> | <u>1</u> | <u>566,446</u> |
| Net balance sheet position | <u>(431,932)</u> | <u>62,145</u> | <u>86,958</u> | <u>122,539</u> | <u>59,890</u> | <u>59,294</u> | <u>(41,106)</u> |
| Off balance sheet net notional position | <u>-</u> | <u>-</u> | <u>(27,518)</u> | <u>(20,650)</u> | <u>50,546</u> | <u>(5)</u> | <u>2,373</u> |
| As at 31 December 1997 | | | | | | | |
| Total assets | 124,034 | 26,140 | 99,242 | 212,409 | 29,056 | 120 | 491,001 |
| Total liabilities | <u>455,340</u> | <u>56</u> | <u>11,077</u> | <u>3,229</u> | <u>11,583</u> | <u>39</u> | <u>481,324</u> |
| Net balance sheet position | <u>(331,306)</u> | <u>26,084</u> | <u>88,165</u> | <u>209,180</u> | <u>17,473</u> | <u>81</u> | <u>9,677</u> |
| Off balance sheet net notional position | <u>-</u> | <u>-</u> | <u>(24,295)</u> | <u>(6,519)</u> | <u>836</u> | <u>31,354</u> | <u>1,376</u> |

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

33 INTEREST RATE RISK

As at 31 December 1998

| | Up to <u>1 month</u> | 1-3 <u>months</u> | 3-12 <u>months</u> | 1-5 <u>years</u> | Over 5 <u>years</u> | Non- interest <u>bearing</u> | <u>Total</u> |
|-----------------------------------|-------------------------|----------------------|-----------------------|---------------------|------------------------|------------------------------------|-----------------|
| Assets | | | | | | | |
| Cash and current accounts in | | | | | | | |
| other banks | 5,519 | - | - | - | - | - | 5,519 |
| Due from other banks | 75,600 | 6,044 | - | - | - | 9,754 | 91,398 |
| Treasury and other eligible bills | 47,386 | 101,718 | 18,327 | - | - | - | 167,431 |
| Dealing securities | 25,847 | 44,092 | 16,241 | 75,720 | 14,090 | - | 175,990 |
| Loans and advances to | | | | | | | |
| customers | 10,410 | 18 | 18,617 | 26 | 42 | - | 29,113 |
| Other | <u>578</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>55,311</u> | <u>55,889</u> |
| Total assets | <u>165,340</u> | <u>151,872</u> | <u>53,185</u> | <u>75,746</u> | <u>14,132</u> | <u>65,065</u> | <u>525,340</u> |
| Liabilities | | | | | | | |
| Due to other banks | 251,126 | 10,200 | 200 | - | 44 | - | 261,570 |
| Due to state | 12,129 | 11,030 | 5,062 | 149 | - | - | 28,370 |
| Due to customers | 35,228 | 1,429 | - | - | - | - | 36,657 |
| Debt securities in issue | - | - | - | 9,069 | - | - | 9,069 |
| Other borrowed funds | 14,788 | 119 | 119 | 949 | 696 | - | 16,671 |
| Other | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>214,109</u> | <u>214,109</u> |
| Total liabilities | <u>313,271</u> | <u>22,778</u> | <u>5,381</u> | <u>10,167</u> | <u>740</u> | <u>214,109</u> | <u>566,446</u> |
| On balance sheet | | | | | | | |
| Interest sensitivity gap | <u>(147,931)</u> | <u>129,094</u> | <u>47,804</u> | <u>65,579</u> | <u>13,392</u> | <u>(149,044)</u> | <u>(41,106)</u> |
| Off balance sheet | | | | | | | |
| Interest sensitivity gap | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> |

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

33 INTEREST RATE RISK (continued)

Interest sensitivity of assets, liabilities and off balance sheet items

The Bank is exposed to various risks associated with the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. The table above summarises the Bank's exposure to interest rate risks. Included in the above table are the Bank's assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates. The carrying amounts of derivative financial instruments are included in 'Other assets' and 'Other Liabilities' under the heading 'Non-interest bearing'. The off-balance sheet gap represents the net notional amounts of all interest sensitive derivative financial instruments.

The table below summarises the effective interest rate by major currencies for monetary financial instruments:

As at 31 December 1998

| | % | <u>CZK</u> | <u>ECU</u> | <u>USD</u> | <u>DEM</u> | <u>JPY</u> |
|--|------|------------|------------|------------|------------|------------|
| Assets | | | | | | |
| Cash and current accounts in other banks | | - | 0.5 | 4.0 | - | - |
| Due from other banks | 11.8 | - | - | 6.1 | 3.6 | 0.3 |
| Treasury and other eligible bills | N/A | 3.2 | 3.2 | 6.1 | 3.6 | - |
| Dealing securities | N/A | 3.2 | 3.2 | 6.1 | 3.6 | - |
| Loans and advances to customers | 9.1 | N/A | N/A | N/A | N/A | N/A |
| Liabilities | | | | | | |
| Due to other banks | | 8.8 | N/A | N/A | N/A | N/A |
| Due to state | 10.1 | N/A | N/A | N/A | N/A | N/A |
| Due to customers | 5.9 | 1.9 | 1.9 | N/A | 3.4 | N/A |
| Debt securities in issue | N/A | N/A | N/A | N/A | - | 6.6 |
| Other borrowed funds | 14.0 | N/A | N/A | N/A | - | 4.6 |

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

33 INTEREST RATE RISK (continued)

| As at 31 December 1997 | Up to <u>1 month</u> | 1-3 <u>months</u> | 3-12 <u>months</u> | 1-5 <u>years</u> | Over 5 <u>years</u> | Non- interest bearing | <u>Total</u> |
|--|-------------------------|----------------------|-----------------------|---------------------|------------------------|-----------------------------|----------------|
| Assets | | | | | | | |
| Cash and current accounts in other banks | 2,825 | - | 870 | - | - | - | 3,695 |
| Due from other banks | 194,590 | - | - | - | 2,347 | 12,388 | 209,325 |
| Treasury and other eligible Bills and Dealing securities | 29,472 | 119,150 | 29,879 | 32,637 | 6,308 | - | 217,446 |
| Loans and advances to customers | 9,098 | 9,643 | 133 | 72 | 32 | - | 18,978 |
| Other | <u>4,180</u> | <u>-</u> | <u>2,623</u> | <u>-</u> | <u>-</u> | <u>34,754</u> | <u>41,557</u> |
| Total assets | <u>240,165</u> | <u>128,793</u> | <u>33,505</u> | <u>32,709</u> | <u>8,687</u> | <u>47,142</u> | <u>491,001</u> |
| Liabilities | | | | | | | |
| Due to other banks | 205,488 | - | - | - | 44 | - | 205,532 |
| Due to state | 26,038 | - | - | - | - | 787 | 26,825 |
| Due to customers | 43,189 | 1,555 | - | - | - | - | 44,744 |
| Debt securities in issue | - | - | - | 9,360 | - | - | 9,360 |
| Other borrowed funds | <u>14,114</u> | <u>1,097</u> | <u>6</u> | <u>35</u> | <u>2,147</u> | <u>177,464</u> | <u>194,863</u> |
| Total liabilities | <u>288,829</u> | <u>2,652</u> | <u>6</u> | <u>9,395</u> | <u>2,191</u> | <u>178,251</u> | <u>481,324</u> |
| On balance sheet | | | | | | | |
| Interest sensitivity gap | <u>(48,664)</u> | <u>126,141</u> | <u>33,499</u> | <u>23,314</u> | <u>6,496</u> | <u>(131,109)</u> | <u>9,677</u> |
| Off balance sheet | | | | | | | |
| Interest sensitivity gap | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> |

The Banking Board decided not to disclose comparative information in respect of effective interest rates and basing dates as at 31 December 1997 due to the excessive investment in terms of both cost and time necessary to derive relevant data from the accounting records.

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

31 DECEMBER 1998

34 LIQUIDITY RISK

Maturities of assets and liabilities

| As at 31 December 1998 | Up to <u>1 month</u> | 1-3 <u>months</u> | 3-12 <u>months</u> | 1-5 <u>years</u> | Over 5 <u>years</u> | Un- <u>specified</u> | <u>Total</u> |
|--|-------------------------|----------------------|-----------------------|---------------------|------------------------|-------------------------|-----------------|
| Assets | | | | | | | |
| Cash and current accounts in other banks | 5,519 | - | - | - | - | - | 5,519 |
| Gold and other precious metals | 578 | - | - | - | - | - | 578 |
| Due from other banks | 43,288 | 4,398 | 17,553 | 824 | 15,581 | 9,754 | 91,398 |
| Treasury bills and other eligible bills | 47,386 | 101,718 | 18,327 | - | - | - | 167,431 |
| Dealing securities | 19,240 | 36,001 | 16,481 | 102,523 | 1,745 | - | 175,990 |
| Loans and advances to customers | 10,349 | 18 | 18,678 | 26 | 42 | - | 29,113 |
| Investment securities | - | - | - | - | - | 50 | 50 |
| Investments in unconsolidated subsidiary and associated undertakings | - | - | 1,353 | 15,814 | - | 11 | 17,178 |
| Membership quota at the IMF | - | - | - | - | - | 26,320 | 26,320 |
| Other | <u>219</u> | <u>-</u> | <u>599</u> | <u>-</u> | <u>-</u> | <u>10,945</u> | <u>11,763</u> |
| Total assets | <u>126,579</u> | <u>142,135</u> | <u>72,991</u> | <u>119,187</u> | <u>17,368</u> | <u>47,080</u> | <u>525,340</u> |
| Liabilities | | | | | | | |
| Due to other banks | 250,715 | 10,200 | 611 | - | 44 | - | 261,570 |
| Due to state | 12,129 | 11,030 | 5,062 | 149 | - | - | 28,370 |
| Due to customers | 33,902 | - | 2,402 | 353 | - | - | 36,657 |
| Debt securities in issue | - | - | - | 9,069 | - | - | 9,069 |
| Other borrowed funds | - | 119 | 119 | 15,736 | 697 | - | 16,671 |
| Due to the IMF | - | - | - | - | - | 26,320 | 26,320 |
| Other | <u>1,899</u> | <u>-</u> | <u>1,345</u> | <u>893</u> | <u>-</u> | <u>183,652</u> | <u>187,789</u> |
| Total liabilities | <u>298,645</u> | <u>21,349</u> | <u>9,539</u> | <u>26,200</u> | <u>741</u> | <u>209,972</u> | <u>566,446</u> |
| Net liquidity gap | <u>(172,066)</u> | <u>120,786</u> | <u>63,452</u> | <u>92,987</u> | <u>-16,627</u> | <u>(162,892)</u> | <u>(41,106)</u> |
| As at 31 December 1997 | | | | | | | |
| Total assets | 187,529 | 106,252 | 36,201 | 84,565 | 14,939 | 61,515 | 491,001 |
| Total liabilities | <u>245,271</u> | <u>1,097</u> | <u>29,165</u> | <u>23,794</u> | <u>3,746</u> | <u>178,251</u> | <u>481,324</u> |
| Net liquidity gap | <u>(57,742)</u> | <u>105,155</u> | <u>7,036</u> | <u>60,771</u> | <u>11,193</u> | <u>(116,736)</u> | <u>9,677</u> |

CZECH NATIONAL BANK

FINANCIAL STATEMENTS PREPARED UNDER INTERNATIONAL ACCOUNTING STANDARDS

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34 LIQUIDITY RISK (continued)

The table above analyses assets and liabilities of the Bank into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest bearing liabilities as they mature, are important factors in assessing the liquidity of the Bank and its exposure to changes in interest rates and exchange rates.

35 RELATED PARTY TRANSACTIONS

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. The Bank exercised such influence over its 100% owned subsidiary undertaking CF. The purpose and principal activities of CF are described in Note 36 below.

Transactions were entered into with CF performing the Bank's role in stabilisation of the banking sector. Loans were extended at arm's length interest rate terms. These include principally loans and advances and can be summarised as follows.

| | <u>1998</u> | <u>1997</u> |
|---------------------------------------|-----------------|----------------|
| Loans outstanding at 1 January 1998 | 9,638 | - |
| Loans issued during the year | 19,436 | 11,538 |
| Loans repaid during the year | <u>(10,507)</u> | <u>(1,900)</u> |
| Loans outstanding at 31 December 1998 | <u>18,567</u> | <u>9,638</u> |
| Interest income earned | <u>2,605</u> | <u>613</u> |

36 ČESKÁ FINANČNÍ, S. R. O.

CF was acquired by the Bank in 1997 as a special purpose vehicle to administer the Banking industry stabilisation and consolidation programmes which focused on small and middle sized banks. The stabilisation program was approved by the Government of the Czech republic in 1996.

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36 ČESKÁ FINANČNÍ, S. R. O. (continued)

The Stabilisation programme involved transfers of certain doubtful assets of banks taking part in this programme to CF in exchange for a cash advance from CF. The banks involved are obliged to repay this advance in seven year's time from the date of the transfer of assets to CF. This programme is financed by Konsolidacni banka, s.p.u. and the National Property Fund has issued a guarantee in favour of CF covering any potential losses borne by CF as a result of repayment delinquency of any of the banks involved. The net book value of the stabilisation programme assets administered by CF was CZK 9,949 million as at 31 December 1998 (1997: CZK 9,081 million).

The Consolidation programme involved transfers of certain doubtful assets of banks taking part in this programme to CF in exchange for an irrecoverable cash advance from CF. The aim of this programme was to assist certain small banks to regain financial stability. The consolidation programme is financed by the Bank. The program was started in 1997. In this respect the Bank provided CF with a loan of CZK 18,567 million (1997: CZK 9,638 million). During 1998 the Bank increased the share capital of CF by CZK 13,333 million. The net book amount of the Consolidation programme assets net of provisions created administered by CF was CZK 32,677 million as at 31 December 1998 (1997: CZK 10,731 million).

On 3 February 1998 CF and the Bank entered into a guarantee agreement whereby the Bank agreed to cover all losses borne by CF in respect of the Consolidation programme as well as all other costs of operation of CF. Pursuant to this agreement the Bank has created a provision of CZK 28,030 million as at 31 December 1998 (1997: CZK 4,709 million). When arriving at this provision the Banking Board of the Bank took into consideration the expected recoverability of assets at risk covered by the guarantee as well as the expected level of operational costs of CF.

The calculation of the provision as at 31 December 1998 is as follows:

| Assets | <u>Nominal value</u> | <u>Expected recovery</u> | <u>Provision</u> |
|--|----------------------|--------------------------|------------------|
| Receivables in the Consolidation programme | 29,731 | 8,318 | 21,413 |
| Securities in Consolidation programme | 2,946 | 363 | 2,583 |
| Operational losses | — | — | <u>4,034</u> |
| | <u>32,677</u> | <u>8,681</u> | <u>28,030</u> |

CZECH NATIONAL BANK

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37 GUARANTEE RECEIVED FROM THE STATE

Pursuant to its role in supporting and maintaining the stability of the banking sector the Bank took over certain assets and liabilities or guaranteed certain liabilities of various banks. The Government of the Czech republic issued a guarantee in favour of the Bank of CZK 22,500 million to limit the exposure of the Bank arising as a consequence of these activities. The guarantee was issued on 19 March 1997 and lasts ten years from that date. The Bank is required to establish an unspecified amount of provisions for potential losses in years when it achieves positive net income before such provisions. As at 31 December 1998 the assets covered by the state guarantee were CZK 17,958 million (1997: CZK 17,665 million).

The assets taken over or guarantees issued within this programme as at 31 December 1998 can be summarised as follows.

| | Amount at <u>31 December 1998</u> | Covered by <u>the Guarantee</u> | <u>Provision</u> | <u>Net amount</u> |
|----------------------------------|--------------------------------------|------------------------------------|------------------|-------------------|
| Loans to banks | 13,007 | 10,077 | 2,930 | - |
| Receivables purchased from banks | 271 | 271 | 0 | - |
| Guarantees and promises | <u>16,350</u> | <u>7,610</u> | <u>8,740</u> | - |
| | <u>29,628</u> | <u>17,958</u> | <u>11,670</u> | - |

38 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES

The following table summarises the carrying amounts and fair values of those financial assets not presented on the Bank's balance sheet at their fair value.

| | Carrying value | | Fair value | |
|---|----------------|-------------|-------------|-------------|
| | <u>1998</u> | <u>1997</u> | <u>1998</u> | <u>1997</u> |
| Financial assets | | | | |
| Gold and other precious metals | 578 | 3,960 | 2,488 | 20,838 |
| Loans and advances to customers | 29,113 | 18,978 | * | * |
| Treasury bills and other eligible bills and dealing securities | 343,421 | 217,446 | 343,993 | 217,657 |
| Investment securities | 50 | 50 | 1,065 | 1,246 |

* The fair value of Loans and advances to customers should be lower than the carrying value as a result of certain assets within this caption being supported by the State guarantee (see Note 37). However given the circumstances of the State guarantee it is not possible to determine the fair value of these assets with a reasonable degree of accuracy.

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39 POST BALANCE SHEET EVENTS

In January 1999 the Bank redenominated receivables due from and to banks and clients, securities and other balances expressed in the legacy European Monetary Union currencies recorded on balance sheet or off balance sheet into euros. This redenomination has not affected the results of the Bank.