

**CROATIA BANKA d.d.**  
**ANNUAL REPORT FOR 2016**

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## **INTRODUCTION**

The Annual Report includes the Management Board Report on the Bank's position, an overview of financial and operational performance, audited financial statements, together with the Independent Auditor's Report, and other regulatory reports for the Croatian National Bank.

### **Legal form**

The Annual Report has been prepared pursuant to the Accounting Act and the Companies Act which require reporting to the shareholders at the annual meeting of shareholders by the company management. Pursuant to the Companies Act, the full statutory set of financial statements consists of the statement of financial position, the statement of comprehensive income, the statement of changes in equity, the cash flow statement and notes to the financial statements, and the Companies Act stipulates in Article 250a an obligation to submit an annual report on the Bank's state of affairs.

The annual financial statements have been prepared in line with the legal requirements for bank accounting in Croatia and audited in accordance with International Standards on Auditing.

### **Abbreviations**

In this Annual Report, Croatia banka d.d. is referred to as the "Bank", the Croatian National Bank as the "CNB", the Croatian Bank for Reconstruction and Development as the "CBRD", the State Agency for Deposit Insurance and Bank Rehabilitation as the "DAB" and the Financial Agency as "FINA", European Union as the "EU" and gross domestic product as the "GDP".

### **Exchange rates**

For the purpose of translating the amounts in foreign currencies into HRK amounts, the following mid exchange rates of the CNB were used:

At 31 December 2016      EUR 1 = HRK 7.557787; USD 1 = HRK 7.168536

At 31 December 2015      EUR 1 = HRK 7.635047; USD 1 = HRK 6.991801

**Operational summary and key financial indicators**  
(amounts in millions of HRK)

Indicator / Year	2016	2015	2014	2013	2012
<b>Key indicators</b>					
Profit/(loss) before tax	3	2	5	(25)	(126)
Net profit/(loss)	2	(15)	4	(25)	(104)
Total assets	3,110	3,109	3,038	2,629	1,984
Loans and advances to customers	1,591	1,893	1,906	1,630	1,042
Total deposits received	2,609	2,616	2,593	2,066	1,486
Capital and reserves	190	182	200	195	220
<b>Other indicators</b>					
Ratio of operating expenses in operating income	71.5%	73.00%	79.70%	113.70%	129.00%
Return on equity	0.9%	(8.3%)	2.0%	(12.6%)	(47.1%)
Assets return	0.1%	(0.5%)	0.1%	(0.9%)	(5.2%)
Own funds	174	175	171	193	218
Total capital ratio	16.81%	15.91%	13.29%	14.00%	17.36%

**Historical development of the Bank**

Croatia banka d.d., Zagreb was founded on 22 December 1989, under the name Banka male privrede, d.d., Zagreb. On that day, 50 shareholders paid in socially owned capital contributions to form the initial (share) capital of 22,340,435,000 former Yugoslav dinars, equivalent to DEM 319,149 (which was then the condition for establishing a bank), which was subsequently divided into 4,565 founders' shares. On 25 January 1990 the Bank received from the Yugoslav National Bank the Decision granting full banking licence and had it registered at the court on 18 July 1990. On 4 May 1990 the Bank changed its name from Banka male privrede d.d. Zagreb into Croatia banka male privrede d.d. Zagreb, (abbreviated: "Croatia banka d.d. Zagreb"), and on 21 June 1995 it changed its name into Croatia banka d.d. Zagreb.

As a result of difficulties faced by the Bank, a procedure to rehabilitate the Bank was initiated in 1999 and, pursuant to Article 15(1), Article 16(1) and Article 17(1) of the Bank Rehabilitation and Restructuring Act (Croatian Official Gazette no 44/94) and Point VII of the Decision of the Government of the Republic of Croatia on the rehabilitation and restructuring of Croatia banka d.d. Zagreb of 27 September 1999 and the Decision of the Government of the Republic of Croatia on amendments to the Decision on rehabilitation and restructuring of Croatia banka d.d. Zagreb of 24 May 2000, the General Assembly of Croatia banka d.d. adopted on 13 September 2000 a Decision on issuing new replacement shares in the amount of HRK 204.6 million and a Decision on amendments to the Statute of Croatia banka d.d., which formally ended the process of the Bank's rehabilitation. The DAB contributed capital to the Bank in the amount of the replacement shares, and the Bank continued to operate as a Croatian public limited company (Croatian: 'dioničko društvo') fully owned by the State.

### Information on economic trends and forecasts<sup>1</sup>

The 2016 positive economic trends supported by solid tourist and consumer business performance continued in the second half of the year.

Despite the continuing positive developments on the labour market, the gradual workforce decline is partly due to emigration, which may impair the growth potential in the long run.

In September and October, the decline in the annual consumer price index (CPI) somewhat decelerated compared with August, resulting from the movements in the energy prices.

Favourable fiscal movements continued, leading to a considerable lower general government deficit in 2016 compared with prior year, with the debt remaining at the level reported at the end of 2015.

The Croatian National Bank has continued to uphold a stable exchange rate of the Croatian kuna against the euro as a prerequisite for preserving the financial stability. With four structured reverse repo auctions in 2016, the central bank issued almost a total of one billion kunas for a term of four years, whereby the interest rate decreased from 1.8 percent to 1.4 percent. The interest rate on regular weekly reverse repo agreement operations also decreased, from 0.5 percent to 0.3 percent. A high-level liquidity on the financial market made both passive and active interest rates offered by commercial banks in Croatia decline further, which, coupled with the positive economic trends, resulted in a higher loan demand as well as a higher level of lending.

The start of the fourth quarter of the year saw a continuation of favorable manufacturing industry and retail sales trends, with the GDP for the entire 2016 estimated to reach around 2.8 percent, and even slightly increase in 2017. Foreign demand could further contribute to the growing domestic activity in the light of the expected growing share of capital expenditure as a result of intensified utilization of EU funds and continuing investments in tourism. Favourable effects of the tax reform will give rise to continuing personal consumption and enhance it as a steady contributing factor to the overall GDP growth.

The CPI inflation rate for 2016 is estimated to be around -1.2 percent, with energy being the greatest negative contributing factor. The average CPI inflation rate for 2017 could increase to 1.6 percent, mainly as a result of the import-related inflation pressure, that is the expected increase in crude oil and other raw material prices, an accelerated inflation in the euro area, the strengthening of the US dollar against the euro as well as indirect tax system reforms.

The budget deficit for 2016 could fall below 2.7 percent of the GDP, and the projected general government deficit indicates that, in 2017, Croatia could find itself outside the scope of corrective measures imposed by the Stability and Growth Pact.

In 2017 the monetary policy will preserve its expansive character, while preserving the Croatian kuna to the euro exchange rate steady. Structural and regular repo auctions of the CNB will help maintain domestic interest rates low, which could reflect itself on the dynamics of lending and turn out beneficial for the economic trends.

<sup>1</sup>Macroeconomic trends and forecast, CNB, December 2016

### Description of operations

The Bank's activities include all types of deposit and loan operations for legal and natural persons, domestic and foreign payments, issuing guarantees, avals and other forms of guarantees, purchase and sale of securities and other banking activities.

The Bank is fully (100%) owned by the state and ranked by assets (HRK 3.1 billion) as the 12<sup>th</sup> of a total of 27 banks. As at 31 December 2016, the Bank has 15 branches and 3 outlets.

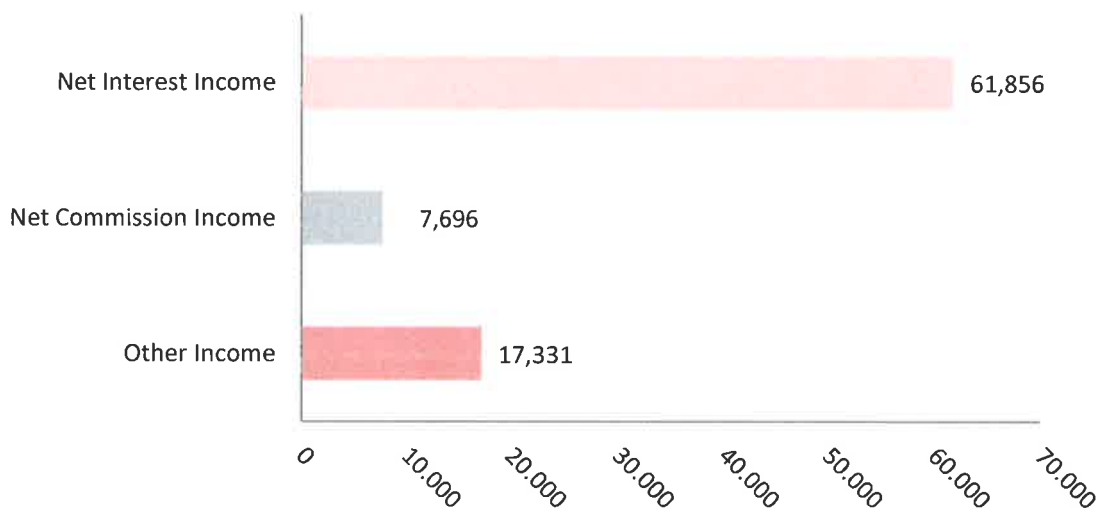
The Bank's own (regulatory) capital as at 31 December 2016 amounts to HRK 173,654 thousand, and the regulatory capital adequacy rate is 16.81%.

In 2016 the Bank generated a pre-tax profit in the amount of HRK 2,664 thousand, and the loss after tax amounts to HRK 1,638 thousand.

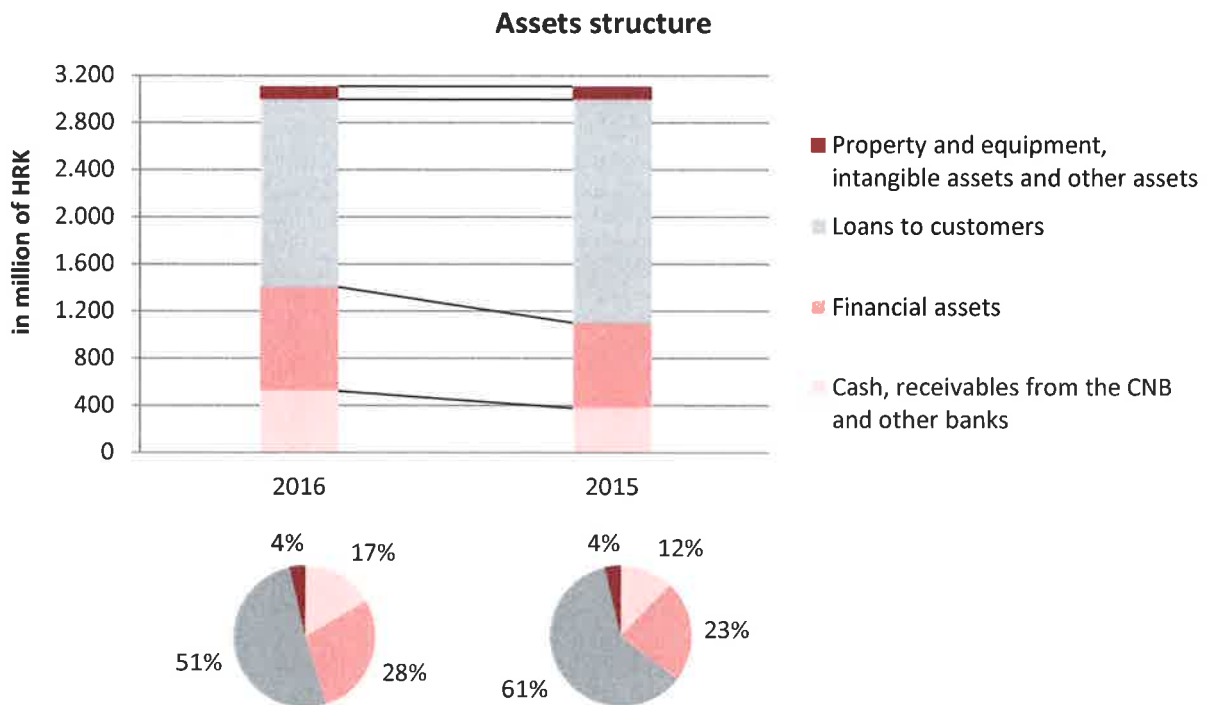
The operating profit for the year amounts to HRK 24,771 thousand, the impairment and provisioning expense amounts to HRK 22,107 thousand.

Total net operating income decreased by 2.2%, while operating expenses decreased by 4.3% compared to 2015 which contributed to a rise in operating profit in 2016. Interest income represents the most significant share of the total income and amounts to 71.2 percent (HRK 61,856 thousand).

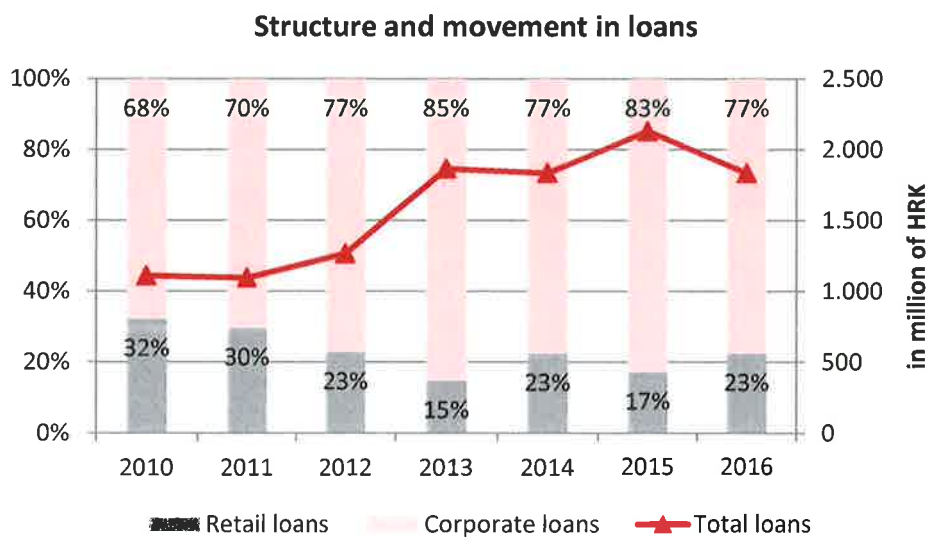
### Structure of operating income for the period from 1 January 2016 to 31 December 2016 (in thousands of HRK)



At the end of 2016 the Bank's assets amount to HRK 3,110,015 thousand, HRK 1,448 thousand more than at the end of 2015. Loans and receivables from customers represent the largest share (51percent), followed by financial assets (28percent), with cash, receivables from the Croatian National Bank and other banks constituting in aggregate 17percent.

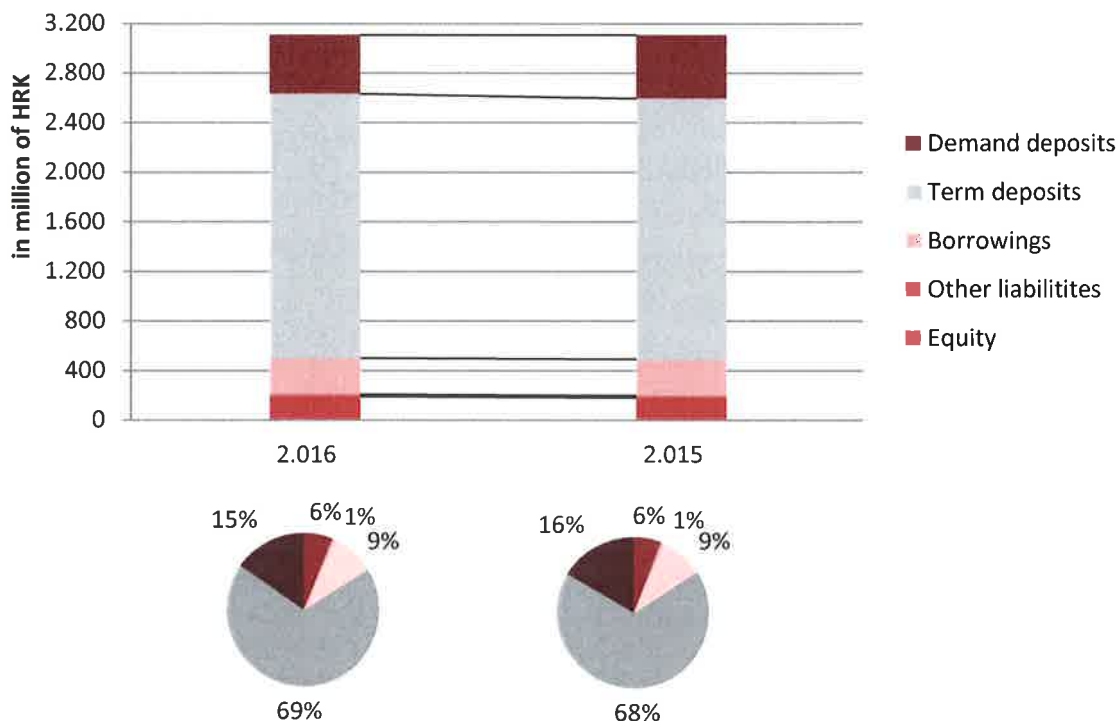


At 31 December 2016, the balance of total gross loans to customers was HRK 1,832,389 thousand, which is 13.9 percent less than in 2015 mainly due to reduced public sector loans. Loans to legal persons represent 77 percent of the total loans to customers, and loans to individuals (including sole traders) account for 23 percent.



Term deposits represent the largest portion of liabilities and account for 69 percent, followed by demand deposits which represent 15 percent.

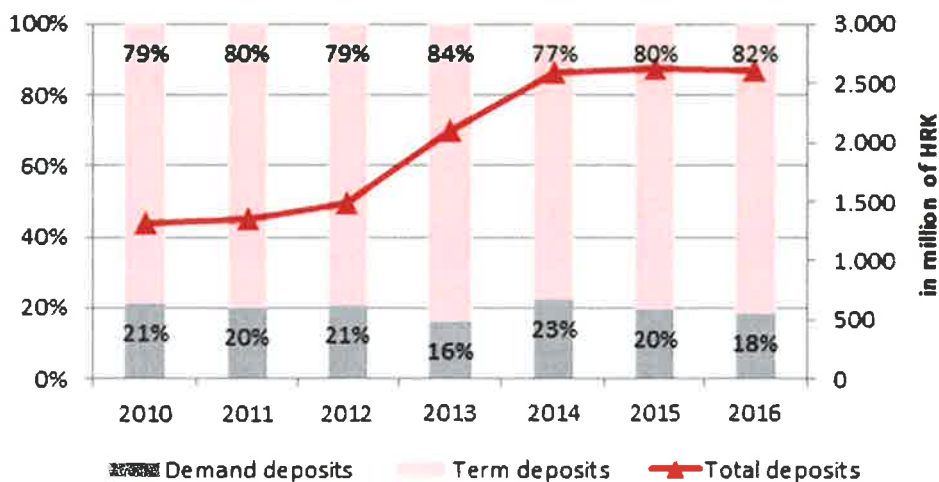
### Liabilities structure



Total deposits at the end of 2016 amounted to 2.6 billion, which presents a decrease compared to the end of 2015 by 0.3 percent, wherein retail deposits increased by 3.9 percent, and corporate deposits decreased by 9.4 percent, which had a positive effect on the concentration of deposits.

As regards the structure of total deposits, term deposits (82 percent) prevail by far over demand deposits (18 percent) and increased 1.4 percent, with their share in the total deposits having increased by 2 percentage points. In 2016 demand deposits fell by 7.1 percent.

### Structure and movement in deposits





### **Retail customer operations**

Operations involving individuals continued to perform well in 2016, as in previous years, and all key targets were achieved related to net interest and noninterest income.

General-purpose loans remained the largest share in total structure of given loans, with the share of housing loans increasing compared with the prior year.

Deposit interest rates were reduced several times during the year, resulting in 8.7 percent lower interest expense. On the other hand, total retail deposits increased by HRK 65,440 thousand, representing an annual growth of 3.9 percent.

The positive developments in the number of current accounts as a result of an increasing number of customers continued significantly improved the level of non-interest income from fees. In the middle of May 2016 the Bank introduced m-banking as part of its efforts to enhance its offer. Good trends in sales from services involving third-party products, such as bank assurance, also continued and additionally increased the non-interest income, so that business targets in the area of fee income were also achieved.

### **Operations with legal persons**

Deposits from legal persons (excluding deposits from other banks) account for 28 percent of the Bank's total deposits. They fell by 10 percent from the end of 2015 and amount to HRK 716,147 thousand. Of that balance, demand deposits amount to HRK 306,513 thousand, and term deposits amount to HRK 409,634 thousand. The decrease was mostly due to several larger deposits being strategically released for high interest expense. On the other hand, term deposits of individuals were growing, as a planned substitute for the released deposits.

At the end of 2016, the total portfolio of loans to legal persons amounted to HRK 1,419,999 thousand, which is HRK 341,849 thousand less than at the end of 2015. The same applies to public sector lending. The loans issued to public sector entities were duly repaid in 2016 and were not reprogrammed. Given a lower number of public tenders, the general decline of the public-sector loan demand and the very low interest rates offered to the sector by competitors, and given the prices at which the Bank obtains its funds, the Bank is not able to offer loans at such low interest rates.

As part of its 2016 plan for corporate customers, the Bank intended to preserve its existing good customers as well as continuously improve the quality of its business processes in cooperation with other organizational units of the Bank, with an emphasis on the lending process, which the Bank succeeded in the most part. The plan is to continue the efforts in 2017. The total number of customers remained more or less the same, albeit with a somewhat lower non-interest income than in 2015. Fee income decreased, mainly on issued guarantees and letters of credit. The decrease is a result of an early return of a significant guarantee, but also a lower volume of business of one of the Bank's major customer.

### **Treasury operations**

The Bank maintains its liquidity using available liquid instruments denominated in HRK and foreign currencies (balances on accounts with the Bank, securities, inter-bank loans, repo loans). A more sophisticated instrument used by the Bank to manage its liquidity position is an FX swap. Throughout the year 2016 the Bank maintained a high liquidity as well as a balanced foreign exchange position on all currencies.

In 2016 the securities portfolio (bonds and treasury bills) increased by 18.2 percent (of which bonds by 81.8 percent, but the T-bill portfolio decreased by 4.2 percent). As a result and despite the unfavourable movements on the market and the decrease in active interest rates, the actual interest income and trading results were on budget.

Regarding the quality of the business processes, a key change was introduced in the area of collecting data relevant for liquidity and foreign exchange position management. The Treasury managed to improve and simplify further its internally used software applications it developed to communicate with the Retail and Corporate Divisions.

### **Investment banking**

The Bank has obtained all permits from the Croatian National Bank and the Croatian Financial Services Supervisory Agency for providing investment services and activities and has achieved all prerequisites for providing investment services. In the field of investment banking, the Bank offers to its clients brokerage services, custody services for customers' financial assets, margin loan for purchases of financial instruments, as well as general-purpose S-loans against financial instruments placed into the Bank's custody.

Despite the unfavourable situation on the Croatian financial market, which features low transaction volumes and meagre investments, the Bank achieved a significant growth in the investment banking segment. Over the past one-year period, its customer base has grown considerably, and the portfolio of its investment banking customers has multiplied. As a result, the Bank reported a considerable increase in interest income, which supports the sustainability and profitability of this segment in the long run.

### **Internal control system and internal audit**

The internal control system at the Bank's level has been set up by means of internal acts that vertically and horizontally divide responsibilities among the Bank's organizational units.

The internal control system at the Bank has been implemented as a set of established processes and procedures established for the purpose of adequate risk control, monitoring the efficiency and effectiveness of the Bank's operations, reliability of its financial and other information, and regulatory compliance, including compliance with internal acts, standards and codes, to ensure the stability of the Bank's operations.

### **Internal audit**

The internal audit function has been set up as a separate organizational unit that is functionally and organizationally independent of activities it audits as well as of other organizational units of the Bank.

The Annual Audit Plan is based on documented risk assessments and contains all the relevant elements from the Decision on the internal control system and internal acts. The annual work plan of the internal audit is approved by the Bank's Management Board based on a prior consent of the Audit Committee and/or the Supervisory Board.

Internal audit reports are delivered to all members of the Management Board, persons responsible for the Bank's organizational part audited and the Audit Committee.

The Internal Audit also prepares its activity reports and submits them to the Management Board and the Audit Committee on a quarterly basis, to the Supervisory Board semi-annually, as well as the annual report for the CNB.

### **Implementation of the Corporate Governance Code**

Pursuant to the provisions of Article 272 of the Companies Act, the Management Board of Croatia bank d.d. Zagreb hereby declares that the Bank implements the Corporate Governance Positions of the Croatian National Bank for Banks on a voluntary basis.

In 2016, the Bank continuously followed and applied the recommendations determined in the CNB's Positions, disclosing all information the disclosure of which is provided by positive regulations as well as making disclosures that are in the interest of the Bank's owners and clients.

Pursuant to the corporate governance requirements and in line with the provisions of the Companies Act, the Supervisory Board performs the internal oversight by regular controls of submitted reports. Members of the Supervisory Board regularly obtain detailed information on the Bank's management and operations. At the Supervisory Board meetings, all issues from the Board's area of responsibilities are discussed and decided on.

The Bank keeps business and other records and business documentation, prepares accounting documents, realistically assesses assets and liabilities, prepares financial statements and other reports in accordance with accounting regulations and standards and the applicable legislation.

Corporate governance at the Bank is implemented not only by meeting regulatory requirements, but it also derives from the culture of corporate and personal integrity of the management and employees. Main features of the implemented internal oversight and risk management relevant for financial reporting are described further below.

Nominees for the president and members of the Bank's Management Board must meet all requirements prescribed by legislation governing banking operations and other relevant regulations. Once the Croatian National Bank approves the nominees, the Supervisory Board appoints the president and members of the Management Board with a mandate of up to four years. The powers of the Bank's Management Board are defined by law and the Statute. The division of the respective responsibilities of the Management Board and its president are determined in a separate decision adopted with the consent of the Supervisory Board.

Decisions on amendments to the Statute are adopted at the Bank's General Assembly, in line with the Act and the Statute.

For the purpose of protecting the interests of the owners, clients, employees and all other stakeholders, Croatia banka d.d. Zagreb aims to maintain its operations in line with highest corporate governance standards.

### **Governance structure of the Bank**

In accordance with the Companies Act, the Credit Institutions Act and the Bank's Statute, the Bank's governance structure comprises the Supervisory Board and the Management Board, whose duties and responsibilities are also regulated by those acts.

### **Other information**

The Bank did not carry out any research and development activities in 2016.

The Bank did not purchase any treasury shares during in 2016.

The Bank does not own other legal entities.

Purchase and sale of financial instruments constitute an integral part of the Bank's operations and are described in detail in these financial statements.

Details about the Bank's financial risk management goals and policies, its exposure to price risk, credit risk, liquidity risk and other risks are provided in the accompanying financial statements.

Pursuant to the Croatian Accounting Law, the Management Board is responsible for ensuring that financial statements are prepared for each financial year in accordance with applicable accounting standards, which give a true and fair view of the state of affairs and results of Croatia banka d.d. ("Bank") for that period.

The Management Board has a reasonable expectation that the Bank has adequate resources to continue in operational existence for the foreseeable future. For this reason, the Management Board continues to adopt the going concern basis in preparing the financial statements.

In preparing those financial statements, the responsibilities of the Management Board include ensuring that:

- suitable accounting policies are selected and then applied consistently;
- judgements and estimates are reasonable and prudent;
- applicable accounting standards are followed, subject to any material departures disclosed and explained in the financial statements; and
- the financial statements are prepared on the going concern basis unless it is inappropriate to presume that the Bank will continue in business.

The Management Board is responsible for keeping proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Bank and must also ensure that the financial statements comply with the Croatian Accounting Law (Official Gazette no. 78/15, 134/15 and 120/16). The Management Board is also responsible for safeguarding the assets of the Bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Management Board is responsible for preparation and content of the annual report in accordance with the article 19 of the Accounting Act (Official Gazette 78/15, 134/15 and 120/16), and also for other regulatory supplementary reports.

For and on behalf of Croatia banka d.d.

20 March 2017

  
Mladen Duliba  
President of the Management Board

  
Ivan Sverko  
Member of the Management Board



## INDEPENDENT AUDITOR'S REPORT

To the owners of Croatia bank d.d. Zagreb

### Report on the Audit of the Financial Statements

#### Opinion

We have audited the financial statements of Croatia bank d.d. , which comprise the statement of financial position as at December 31, 2016, and statement of comprehensive income, the statement of changes in equity and reserves and the statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at December 31, 2016, and its financial performance and its cash flows for the year then ended in accordance with statutory accounting requirements for banks in Croatia.

#### Basis for Opinion

We conducted our audit in accordance with the Audit Act and International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and we have fulfilled our ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

The company was registered at Zagreb Commercial Court: MBS 030022053; paid-in initial capital: Kn 44,900.00; Board Members: Branislav Vrtačnik, Eric Daniel Olcott, Marina Tonžetić, Juraj Moravek, Dražen Nimčević and John Jozef H. Ploem; Bank: Zagrebačka banka d.d., Trg bana Josipa Jelačića 10, 10 000 Zagreb, bank account no. 2360000-1101896313; SWIFT Code: ZABHR2X IBAN: HR2723600001101896313; Privredna banka Zagreb d.d., Radnička cesta 50, 10 000 Zagreb, bank account no. 2340009-1110098294; SWIFT Code: PBZGHR2X IBAN: HR3823400091110098294; Raiffeisenbank Austria d.d., Petrinjska 59, 10 000 Zagreb, bank account no. 2484008-1100240905; SWIFT Code: RZBHR2X IBAN: HR1024840081100240905.

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## **INDEPENDENT AUDITOR'S REPORT (CONTINUED)**

### **Other Information**

Management is responsible for the other information. The other information comprises the information included in the Annual Management Report, but does not include the financial statements and our auditor's report.

Our opinion on the financial statements does not cover the other information.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. With respect to the Annual Management Report which is included in the Annual Report, we have also performed the procedures prescribed by the Accounting Act. These procedures include examination of whether the Annual Management Report includes required disclosures as set out in the Article 21 of the Accounting Act.

Based on the procedures performed during our audit, to the extent we are able to assess it, we report that:

- 1) Information included in the other information is, in all material respects, consistent with the attached financial statements for the year,
- 2) Annual Management Report for the year 2016 has been prepared, in all material respects, in accordance with Article 21 of the Accounting Act,

Based on the knowledge and understanding of the Bank and its environment, which we gained during our audit of the financial statements, we have not identified material misstatements in the other information. We have nothing to report in this respect.

## **INDEPENDENT AUDITOR'S REPORT (CONTINUED)**

### **Responsibilities of Management for the Financial Statements**

Management is responsible for the preparation and fair presentation of the financial statements in accordance with statutory accounting requirements for banks in Croatia and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

### **Auditor's Responsibilities for the Audit of the Financial Statements**

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

## INDEPENDENT AUDITOR'S REPORT (CONTINUED)

### Auditor's Responsibilities for the Audit of the Financial Statements (continued)

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.



## INDEPENDENT AUDITOR'S REPORT (CONTINUED)

### Report on Other Legal and Regulatory Requirements

Pursuant to the Decision of the Croatian National Bank on the Form and Content of the Bank Annual Financial Statements (Official Gazette No 62/08, hereinafter: "the Decision") the Bank's management has prepared the forms, as presented in the Appendix to these financial statements on pages 93 to 106, which comprise the balance sheet as at 31 December 2016, the income statement, the statement of changes in equity and the statement of cash flow for the year then ended, together with reconciliation to the financial statements. These forms and the accompanying reconciliation to the financial information are the responsibility of the Bank's management and, do not represent components of the financial statements prepared in accordance with statutory accounting requirements for banks in Croatia, which are set out on pages 18 to 92, but rather a requirement specified by the Decision. The financial information provided in those forms has been derived from the financial statements.



**Branislav Vrtačnik**

President of the Management Board

Zagreb, 20 March 2017

**Deloitte d.o.o.**

Radnička cesta 80, Zagreb

CROATIA BANKA d.d.  
STATEMENT OF COMPREHENSIVE INCOME  
At 31 December 2016

		<i>in thousands of HRK</i>	
	Notes	2016	2015
Interest income	5	131,425	149,034
Interest expense	6	(69,569)	(82,966)
<b>Net interest income</b>		<b>61,856</b>	<b>66,068</b>
Fee and commission income	7	12,056	13,357
Fee and commission expense	8	(4,360)	(4,894)
<b>Net fee and commission income</b>		<b>7,696</b>	<b>8,463</b>
Net financial gains	9	7,751	4,385
Net income from exchange differences	10	3,219	3,628
Other operating income	11	6,361	6,290
<b>Total other income</b>		<b>17,331</b>	<b>14,303</b>
Other operating expenses	12	(62,112)	(64,908)
Impairment losses and provisions	13	(22,107)	(21,663)
<b>Total other expenses</b>		<b>(84,219)</b>	<b>(86,571)</b>
<b>Profit before taxation</b>		<b>2,664</b>	<b>2,263</b>
Income tax	14	(1,026)	(17,397)
<b>Profit/(loss) for the year</b>		<b>1,638</b>	<b>(15,134)</b>
<b>Other comprehensive income</b>			
<b>Beginning balance</b>		<b>(395)</b>	<b>2,609</b>
<b>Items potentially included subsequently in profit or loss:</b>		<b>5,966</b>	<b>(3,004)</b>
Unrealised gains/(losses) from the valuation of financial assets available for sale		7,013	(1,144)
Cumulative loss/(gain) on the sale of available-for-sale financial assets transferred to profit or loss		275	(1,959)
Deferred tax on financial assets available for sale		(1,322)	99
<b>Closing balance</b>		<b>5,571</b>	<b>(395)</b>
<b>TOTAL COMPREHENSIVE INCOME/LOSS</b>		<b>7,604</b>	<b>(18,138)</b>
<b>Earnings/(loss) per share</b>	<b>32</b>	<b>0.35</b>	<b>(3.19)</b>

The significant accounting policies and other notes on pages 22 to 92 form an integral part of these financial statements.

CROATIA BANKA d.d.  
STATEMENT OF FINANCIAL POSITION  
At 31 December 2016

		31 December 2016	<i>in thousands of HRK</i> 31 December 2015
	<i>Notes</i>		
<b>ASSETS</b>			
Cash	15	276,808	103,596
Receivables from the Croatian National Bank	16	191,709	226,137
Placements with banks	17	53,334	47,985
Financial assets available for sale	18	833,773	677,732
Financial assets held to maturity	19	50,647	48,579
Loans and advances to customers	20	1,590,643	1,892,503
Investment property	21	33,702	35,696
Property and equipment	22	13,427	15,595
Intangible assets	22	4,926	4,289
Foreclosed assets	23	23,389	24,539
Deferred tax assets	14	1,898	4,246
Other assets	24	35,759	27,670
<b>Total assets</b>		<b>3,110,015</b>	<b>3,108,567</b>
<b>EQUITY AND LIABILITIES</b>			
Liabilities to banks	25	92,095	109,903
Demand deposits	26	471,935	473,276
Term deposits	27	2,044,562	2,032,676
Borrowings	28	292,003	292,726
Other liabilities	29	9,109	9,769
Provisions	30	10,676	8,186
<b>Total liabilities</b>		<b>2,920,380</b>	<b>2,926,536</b>
<b>EQUITY</b>			
Share capital	31	474,600	474,600
Accumulated losses		(290,536)	(292,174)
Reserves		5,571	(395)
<b>Total equity</b>		<b>189,635</b>	<b>182,031</b>
<b>Total liabilities and equity</b>		<b>3,110,015</b>	<b>3,108,567</b>

The significant accounting policies and other notes on pages 22 to 92 form an integral part of these financial statements.

CROATIA BANKA d.d.  
STATEMENT OF CHANGES IN EQUITY  
For the year 2016

	Share capital	Accumulated losses	Reserves	<i>in thousands of HRK</i> Total
<b>Balance at 1 January 2015</b>	<b>474,600</b>	<b>(277,040)</b>	<b>2,609</b>	<b>200,169</b>
<i>Changes in equity in 2015</i>				
Unrealised change in fair value of available-for-sale financial assets	-	-	(1,144)	(1,144)
Cumulative gains on the sale of available-for-sale financial assets transferred to profit or loss	-	-	(1,959)	(1,959)
Deferred tax on available-for-sale financial assets	-	-	99	99
<i>Net loss recognised directly in equity</i>	-	-	(3,004)	(3,004)
Loss for the year	-	(15,134)	-	(15,134)
<b>Balance at 31 December 2015</b>	<b>474,600</b>	<b>(292,174)</b>	<b>(395)</b>	<b>182,031</b>
<b>Balance at 1 January 2016</b>	<b>474,600</b>	<b>(292,174)</b>	<b>(395)</b>	<b>182,031</b>
<i>Changes in equity in 2016</i>				
Unrealized change in fair value of available-for-sale financial assets	-	-	7,013	7,013
Cumulative gains on the sale of available-for-sale financial assets transferred to profit or loss	-	-	275	275
Deferred tax on available-for-sale financial assets	-	-	(1,322)	(1,322)
Net income recognised directly in equity	-	-	5,966	5,966
Profit for the year	-	1,638	-	1,638
<b>Balance at 31 December 2016</b>	<b>474,600</b>	<b>(290,536)</b>	<b>5,571</b>	<b>189,635</b>

The significant accounting policies and other notes on pages 22 to 92 form an integral part of these financial statements.

CROATIA BANKA d.d.  
STATEMENT OF CASH FLOWS  
For the year 2016

in thousands of HRK

	2016	2015
<b>NET CASH FLOW FROM OPERATING ACTIVITIES</b>		
Profit before taxation	2,664	2,263
<i>Adjustment to net cash from operating activities</i>		
Impairment allowance on loans and other assets (net) (Note 13)	17,139	22,835
Provisions for contingent liabilities (net) (Note 13)	(102)	(973)
Litigation provision (net) (Note 13)	5,282	1,683
Other provisions (net) (Note 30)	42	(663)
Gains from realization of available-for-sale and held to maturity financial assets (Note 9)	(7,705)	(4,115)
Gains on trading financial assets at fair value through profit or loss (Note 9)	(46)	(270)
Amortization and depreciation (Note 22)	3,470	3,343
Foreign exchange differences on translation	145	429
Gains on the sale of foreclosed assets (Note 11)	(1,593)	(1,070)
Write-offs of tangible assets	2,128	2,602
<i>Changes in assets and liabilities from operating activities</i>		
Decrease/(increase) in receivables from the Croatian National Bank	34,776	(17,867)
Decrease/(increase) in loans and advances to customers	284,781	(5,451)
Increase/(decrease) in other assets	(7,820)	5,782
Decrease in liabilities to banks	(17,808)	(16,462)
Decrease in a vista deposits	(1,341)	(94,456)
Increase in term deposits	16,543	132,043
Decrease in other liabilities	(3,392)	(22,627)
<b>Net cash flow from operating activities</b>	<b>327,163</b>	<b>7,026</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Sale of financial assets available for sale	778,896	825,489
Purchase of financial assets available for sale	(921,220)	(908,309)
Purchase/(maturity) of financial assets held to maturity	(2,087)	12,719
Purchases of property, equipment and intangible assets	(4,067)	(3,853)
Proceeds from the sale of <i>property</i>	2,462	3,919
<b>Net cash from investing activities</b>	<b>(146,016)</b>	<b>(70,035)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds/Repayments of borrowings, net	(723)	89,312
<b>Net cash flow from financing activities</b>	<b>(723)</b>	<b>89,312</b>
<b>Net change in cash and cash equivalents</b>	<b>180,424</b>	<b>26,303</b>
<b>Cash and cash equivalents at beginning of the year (Note 35)</b>	<b>152,834</b>	<b>126,531</b>
<b>Cash and cash equivalents at end of the year (Note 35)</b>	<b>333,258</b>	<b>152,834</b>

The significant accounting policies and other notes on pages 22 to 92 form an integral part of these financial statements.

## **1 GENERAL INFORMATION ABOUT THE BANK**

### **Legal framework and activity**

Croatia banka d.d. Zagreb ("the Bank") was registered in the court register as a joint stock company in 1989 under the registration number 080007370. The headquarters of the Bank are at Roberta Frangeša Mihanovića 9, Zagreb, Croatia.

The Bank's activities include all types of deposit and loan operations for legal and natural persons, domestic and foreign payments, issuing guarantees, avals and other forms of guarantees, purchase and sale of securities and other banking activities.

The Bank has 15 branches – Branch Zagreb, Branch Bjelovar, Branch Čakovec, Branch Metković, Branch Osijek, Branch Pula, Branch Požega, Branch Rijeka, Branch Slavonski Brod, Branch Split, Branch Vinkovci, Branch Virovitica, Branch Vukovar, Branch Zadar, Branch Županja, and 3 outlets: Outlet Šubićeva, Outlet Sky Office, and Outlet Drenovci.

### **Governance and management**

#### **Supervisory Board**

The Supervisory Board operates in accordance with the Companies Act, the Credit Institutions Act and the Bank's Statute, whereby its main responsibility is the supervision of Bank's operations and appointment and dismissal of the president and members of the Management Board. In addition, the Supervisory Board approves the Management Board's business policies, financial plans, strategies and policies of risk taking and management, strategies and procedures for assessing the adequacy of internal capital, acts that establish and ensure adequate functioning of the internal control system, plans of control functions operations, salary and other benefits policy, organizational structure of the Bank, and it also decides on other issues as determined by law or the Bank's internal acts.

The Supervisory Board has four members that are elected and appointed for a period of four years.

Supervisory Board members in 2016:

#### **From 1 January to 7 May 2016**

Maruška Vizek, President  
Josip Lozančić, Deputy President  
Branka Grabovac, Member

#### **From 8 May to 30 May 2016**

Josip Lozančić, Deputy President

#### **From 31 May to 6 June 2016**

Josip Lozančić, Deputy President  
Maruška Vizek, Member  
Branka Grabovac, Member

#### **From 7 June to 30 November 2016**

Maruška Vizek, President  
Josip Lozančić, Deputy President  
Branka Grabovac, Member

#### **From 1 December to 19 December 2016**

Josip Lozančić, Deputy President

**1 GENERAL INFORMATION ABOUT THE BANK (continued)**

**From 20 December to 27 December 2016**

Josip Lozančić, Deputy President  
Maruška Vizek, Member  
Branka Grabovac, Member

**From 28 December to 31 December 2016**

Maruška Vizek, President  
Josip Lozančić, Deputy President  
Branka Grabovac, Member

Supervisory Board members in 2015:

**From 1 January to 31 March 2015**

Marija Hrebac, President  
Branka Grabovac, Deputy President  
Mladen Duliba, Member  
Ivan Tomljenović, Member (exceptionally until 9 February 2015)

**From 1 to 9 April 2015**

Branka Grabovac, Deputy President  
Mladen Duliba, Member  
Maruška Vizek, Member  
Ratko Bajakić, Member  
Josip Lozančić, Member

**From 9 April to 10 July 2015**

Ratko Bajakić, President  
Mladen Duliba, Deputy President  
Branka Grabovac, Member  
Maruška Vizek, Member  
Josip Lozančić, Member

**From 10 July to 16 July 2015.**

Mladen Duliba, Deputy President  
Josip Lozančić, Member  
Branka Grabovac, Member  
Maruška Vizek, Member

**From 16 July to 30 September 2015.**

Mladen Duliba, President  
Josip Lozančić, Deputy President  
Branka Grabovac, Member  
Maruška Vizek, Member

**From 1 October to 31 December 2015**

Mladen Duliba, President  
Maruška Vizek, Deputy President  
Branka Grabovac, Member

## **1 GENERAL INFORMATION ABOUT THE BANK (continued)**

### **Management Board**

Competences, duties and responsibilities of the Bank's Management Board in managing the operations and representing the Bank are determined by the Companies Act, the Credit Institutions Act, the Statute and the Rules of Procedure of the Bank's Management Board.

Management Board manages its business and manages its assets, and it has the responsibility and power to take any action and make any decision necessary for the successful management of the Bank. In the managing of business operations Management Board in particular is responsible for ensuring that the Bank operates in accordance with the rules on risk management in accordance with the Credit Institutions Act and other legislation and internally set regulations and laws; approving and regularly reviewing risk management strategies and policies, including managing risks that arise from the macroeconomic environment in which the Bank operates, and the state of the business cycle of the Bank; ensuring systematic monitoring, assessment and the strategy for maintaining or reaching the adequate amount of capital in relation to risks to which the Bank is exposed in its operations; ensuring functioning of the internal controls system for all areas of the Bank's operations; ensuring unobstructed internal audit; ensuring that the Bank keeps business and other records and business documentation, prepares accounting documents, realistically estimates assets and liabilities, prepares financial and other reports in accordance with accounting regulations and standards and the Credit Institutions Act and other regulations adopted on the basis of law; ensuring that the Bank reports and informs the Croatian National Bank in line with the Credit Institutions Act and other regulations adopted on the basis of law; and ensuring the implementation of measures ordered by the Croatian National Bank.

The Bank's Management Board consists of at least two to maximum three members, one of which is appointed as the President of the Management Board. The President of the Management Board represents the Bank solely and independently, and a member of the Management Board represents the Bank jointly with another member of the Management Board.

The Bank's Management Board is appointed by the Supervisory Board for a period of not more than four years, with the option of reappointment.

The Members of the Board during the 2016 were as follows:

Mladen Duliba – President

Ivan Šverko – Member

The Members of the Board during the 2015 were as follows:

Ivan Šverko – Member

Josip Lozančić – President (from 1 October 2015 to 31 December 2015)

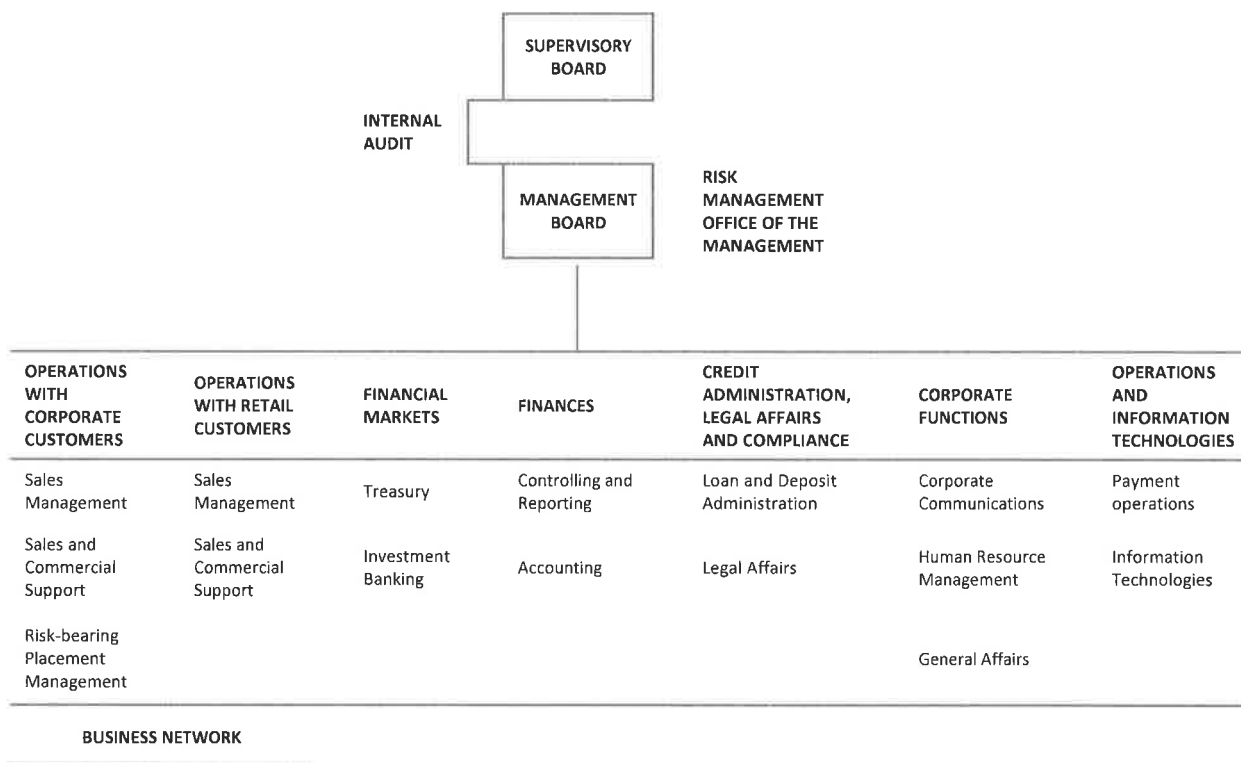
Suzana Brenko – President (till 30 September 2015)

Stjepan Mandić – Member (till 30 September 2015)



**1 GENERAL INFORMATION ABOUT THE BANK (continued)**

**Organisation chart**



## 2 GOING CONCERN

### Capital management

For several years the Bank had not managed to reach operating profit, which is why the Bank's share capital was increased on several occasions, the most recent in the amount of HRK 200 million taking place in October 2012 by converting into equity bonds representing in aggregate a hybrid instrument, i.e. supplementary capital in the amount of HRK 70 million, and contributing HRK 130 million in cash.

Similar to the previous year, in 2016 the Bank's lending activities continued to be focused on extending loans to the government and state-owned companies guaranteed by the Republic of Croatia that, under the applicable regulations, are not subject to capital requirements and still bring a satisfactory level of interest income. Regarding the sources of funds, total deposits (especially deposits from individuals) increased and ensure sources to lending activities. In 2016 operating expenses were reduced additionally, which, coupled with the continuing increase in operating income, resulted in a higher positive financial performance.

Total capital ratio at 31 December 2016 is 16.81 percent (2015: 15.91 percent).

## 3 BASIS FOR THE PRESENTATION OF FINANCIAL STATEMENTS

### Statement of compliance

These financial statements are prepared in accordance with the legal requirements applicable to accounting for banks in the Republic of Croatia. The Bank's operations are subject to the Credit Institutions Act under which the Bank's financial reporting is regulated by the Croatian National Bank ("the CNB") as the central institution overseeing the banking system in Croatia. These financial statements are prepared in accordance with the above-mentioned banking regulations.

The accounting regulations of the CNB are based on International Financial Reporting Standards ("IFRS"), but differ from them, both in terms of presentation and in terms of recognition and measurement.

The principal differences between the accounting regulations of the CNB and the recognition and measurement requirements of International Financial Reporting Standards are as follows:

- The CNB requires from banks to recognise in their income statements losses on impairment of assets not identified as impaired (including those bearing the Central Government Risk) at prescribed rates (with the exception of financial assets at fair value through profit or loss and assets available for sale). The portfolio-based provisions are presented on the Bank's balance sheet in accordance with the CNB requirements which include the requirement to recognise the related expense within impairment losses for the year.
- The Bank recognises impairment losses on loans and advances to customer by discounting the future expected cash flows using the original effective interest rate of the instrument, in accordance with International Financial Reporting Standards. The CNB requires the amortisation of the discount to be presented in the statement of comprehensive income as a change in impairment losses on loans and advances to customer instead of including them in interest income as required under IFRSs.
- Additionally, the CNB prescribes minimum levels of impairment losses against certain specifically identified impaired exposures, which may differ from the impairment loss required to be recognised in accordance with IFRSs.
- The CNB prescribes minimum provisions for legal actions initiated against the Bank to be set at 1 percent of the total claim for individual claims exceeding 0.1 percent of the Bank's assets based on the audited prior-year financial statements.

### **3 BASIS FOR THE PRESENTATION OF FINANCIAL STATEMENTS (continued)**

#### **Basis of measurement**

The financial statements are prepared on the fair value basis for financial assets available for sale and financial assets at fair value through profit or loss, except those for which a reliable measure of fair value is not available. Other financial assets and liabilities, and non-financial assets and liabilities are carried at amortised or historical cost.

#### **Use of estimates and judgements**

In preparing the financial statements, management is required to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities and disclosure of commitments and contingencies at the financial statements date, as well as amounts of income and expense for the period. The estimates and underlying assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about the carrying amounts of assets and liabilities that are not readily apparent from other sources. Actual results may differ from those estimates. The estimates and underlying assumptions are reviewed on a regular basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of revision and future periods if the revision affects both current and future periods.

The Bank monitors the creditworthiness of its customers on an ongoing basis. On-balance sheet and off-balance sheet credit risk exposures are reviewed for impairment on a quarterly basis. Impairment losses are generally charged to the carrying amount of loans and receivables issued to legal persons and individuals and as provisions for risk and charges arising from off-balance sheet exposures to customers, which mostly take on the form of approved, but not utilised loans, guarantees and letters of credit. In addition to individually identified impairment losses, the Bank monitors and recognises, on an ongoing-basis, impairment losses that are known to exist at the financial statements date, but have not been separately identified. In assessing unidentified impairment losses on a portfolio basis, the Bank seeks to collect sufficient reliable information about appropriate loss rates, based on its historical experience, adjusted to reflect the current circumstances and the period in which the loss is identified. The Bank has recognised a general provision of 1 percent which, pursuant to the CNB regulations, applies to all credit risk exposures other than those measured at fair value, including off-balance sheet credit risk exposures and the central government risk.

#### **Functional and presentation currency**

The financial statements are presented in Croatian kunas (HRK), which is the primary currency of the economic environment in which the Bank operates (its functional currency). At 31 December 2016, the official exchange rate of the Croatian kuna against 1 euro was HRK 7.557787 (2015: HRK 7.635047) and for 1 US dollar it was HRK 7.168536 (2015: HRK 6.991801).

### 3 BASIS FOR THE PRESENTATION OF FINANCIAL STATEMENTS (continued)

#### Initial application of new amendments to the existing Standards and Interpretation effective for current financial period

The following amendments to the existing standards and new interpretation issued by the International Accounting Standards Board (IASB) and adopted by the EU are effective for current financial period:

- **Amendments to IFRS 10 “Consolidated Financial Statements”, IFRS 12 “Disclosure of Interests in Other Entities” and IAS 28 “Investments in Associates and Joint Ventures”** - Investment Entities: Applying the Consolidation Exception - adopted by the EU on 22 September 2016 (effective for annual periods beginning on or after 1 January 2016),
- **Amendments to IFRS 11 “Joint Arrangements”** – Accounting for Acquisitions of Interests in Joint Operations - adopted by the EU on 24 November 2015 (effective for annual periods beginning on or after 1 January 2016),
- **Amendments to IAS 1 “Presentation of Financial Statements”** - Disclosure Initiative - adopted by the EU on 18 December 2015 (effective for annual periods beginning on or after 1 January 2016),
- **Amendments to IAS 16 “Property, Plant and Equipment” and IAS 38 “Intangible Assets”** - Clarification of Acceptable Methods of Depreciation and Amortization - adopted by the EU on 2 December 2015 (effective for annual periods beginning on or after 1 January 2016),
- **Amendments to IAS 16 “Property, Plant and Equipment” and IAS 41 “Agriculture”** - Bearer Plants - adopted by the EU on 23 November 2015 (effective for annual periods beginning on or after 1 January 2016),
- **Amendments to IAS 19 “Employee Benefits”** - Defined Benefit Plans: Employee Contributions - adopted by the EU on 17 December 2014 (effective for annual periods beginning on or after 1 February 2015),
- **Amendments to IAS 27 “Separate Financial Statements”** - Equity Method in Separate Financial Statements - adopted by the EU on 18 December 2015 (effective for annual periods beginning on or after 1 January 2016),
- **Amendments to various standards “Improvements to IFRSs (cycle 2010-2012)”** resulting from the annual improvement project of IFRS (IFRS 2, IFRS 3, IFRS 8, IFRS 13, IAS 16, IAS 24 and IAS 38) primarily with a view to removing inconsistencies and clarifying wording - adopted by the EU on 17 December 2014 (amendments are to be applied for annual periods beginning on or after 1 February 2015),
- **Amendments to various standards “Improvements to IFRSs (cycle 2012-2014)”** resulting from the annual improvement project of IFRS (IFRS 5, IFRS 7, IAS 19 and IAS 34) primarily with a view to removing inconsistencies and clarifying wording - adopted by the EU on 15 December 2015 (amendments are to be applied for annual periods beginning on or after 1 January 2016).

### **3 BASIS FOR THE PRESENTATION OF FINANCIAL STATEMENTS (continued)**

#### **Initial application of new amendments to the existing Standards and Interpretation effective for current financial period (continued)**

The adoption of these amendments to the existing standards and interpretations has not led to any changes in the Group's and Bank's accounting policies.

#### **Standards and amendments to the existing Standards issued by IASB and adopted by the EU but not yet effective**

At the date of authorization of these financial statements the following new standards and amendments to the existing standards issued by IASB and adopted by the EU are not yet effective:

- **IFRS 9 "Financial Instruments" adopted by the EU on 22 November 2016 (effective for annual periods beginning on or after 1 January 2018)**
- **IFRS 15 "Revenue from Contracts with Customers" and amendments to IFRS 15 "Effective date of IFRS 15" - adopted by the EU on 22 September 2016 (effective for annual periods beginning on or after 1 January 2018).**

#### **New Standards and amendments to the existing Standards issued by IASB but not yet adopted by the EU**

At present, IFRS as adopted by the EU do not significantly differ from regulations adopted by the IASB except from the following new standards, amendments to the existing standards and new interpretation, which were not endorsed for use in EU as at the date of publishing these financial statements:

- **IFRS 14 "Regulatory Deferral Accounts"** (effective for annual periods beginning on or after 1 January 2016) - the European Commission has decided not to launch the endorsement process of this interim standard and to wait for the final standard,
- **IFRS 16 "Leases"** (effective for annual periods beginning on or after 1 January 2019),
- **Amendments to IFRS 2 "Share-based Payment"** - Classification and Measurement of Share-based Payment Transactions (effective for annual periods beginning on or after 1 January 2018),
- **Amendments to IFRS 4 "Insurance Contracts"** - Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (effective for annual periods beginning on or after 1 January 2018 or when IFRS 9 "Financial Instruments" is applied first time),
- **Amendments to IFRS 10 "Consolidated Financial Statements" and IAS 28 "Investments in Associates and Joint Ventures"** - Sale or Contribution of Assets between an Investor and its Associate or Joint Venture and further amendments (effective date deferred indefinitely until the research project on the equity method has been concluded),

### 3 BASIS FOR THE PRESENTATION OF FINANCIAL STATEMENTS (continued)

#### New Standards and amendments to the existing Standards issued by IASB but not yet adopted by the EU (continued)

- **Amendments to IFRS 15 “Revenue from Contracts with Customers”** - Clarifications to IFRS 15 Revenue from Contracts with Customers (effective for annual periods beginning on or after 1 January 2018),
- **Amendments to IAS 7 “Statement of Cash Flows”** - Disclosure Initiative (effective for annual periods beginning on or after 1 January 2017),
- **Amendments to IAS 12 “Income Taxes”** - Recognition of Deferred Tax Assets for Unrealized Losses (effective for annual periods beginning on or after 1 January 2017),
- **Amendments to IAS 40 “Investment Property”** - Transfers of Investment Property (effective for annual periods beginning on or after 1 January 2018),
- **Amendments to various standards “Improvements to IFRSs (cycle 2014-2016)”** resulting from the annual improvement project of IFRS (IFRS 1, IFRS 12 and IAS 28) primarily with a view to removing inconsistencies and clarifying wording (amendments to IFRS 12 are to be applied for annual periods beginning on or after 1 January 2017 and amendments to IFRS 1 and IAS 28 are to be applied for annual periods beginning on or after 1 January 2018),
- **IFRIC 22 “Foreign Currency Transactions and Advance Consideration”** (effective for annual periods beginning on or after 1 January 2018).

#### The new and revised International Financial Reporting Standards issued by the IASB that have been adopted in the EU and take effect after the reporting period

- **IFRS 9 Financial Instruments was published in July 2014** (effective for annual periods beginning on or after 1 January 2018 with earlier application permitted) is a replacement for IAS 39 "Financial Instruments: Recognition and Measurement" contains requirements relating to the recognition and measurement, impairment, derecognition and hedge accounting in general.
- **Classification and measurement** - IFRS 9 introduces a new approach to the classification of financial assets based on the characteristics of the cash flow and business model under which an item of financial assets is held. The new model also introduces a unique model of impairment which applies to all financial instruments.
- **Impairment** - IFRS 9 introduces a new model of impairment to expected losses, which will require more timely recording of expected credit losses.
- **Hedge accounting** - IFRS 9 introduces significantly altered model of hedge accounting, with expanded information that should be disclosed about the activities of risk management.

### 3 BASIS FOR THE PRESENTATION OF FINANCIAL STATEMENTS (continued)

#### The new and revised International Financial Reporting Standards issued by the IASB that have been adopted in the EU and take effect after the reporting period (continued)

During 2016, the Bank started the IFRS 9 Implementation Project. Based on this project, up to now Bank worked independently on an analysis of clauses of the contracts to determine the gaps between the current situation and the application of IFRS 9, on analysis of the change of the chart of accounts, also has carried out continuous training of employees and an analysis of changes in accounting policies. Also, selection for external partners to assist the Bank in the implementation of IFRS 9 is in process. Within the project following phases are planned:

- Series of educations for acquainting employees with the IFRS 9 and its requirements
- Gap analysis between the current status and IFRS 9 requirements in the classification and measurement stream:
  - Determine business models
  - Determine characteristics of contracted cash flows
- Gap analysis between the current status and IFRS 9 requirements in the impairment stream
- Quantitative impact study of the IFRS 9 effects
- Development of functional specifications for the IT application solution – software implementation
- Development of the impairment methodology according to the business models of the Bank – development of the model for calculating risk parameters required for expected credit loss calculation as required per IFRS 9.

For the classification and measurement stream, the Bank is considering definitions of the business models and other requirements of the IFRS 9 based on determined gaps and identified activities for bridging the gaps.

For the impairment stream, the Bank will develop the methodologies for calculating expected credit loss and modelling the risk parameters with incorporation of necessary parameters for forward looking expectations.

Quantitative impacts will be identified during 2017. The impact for the impairment stream depends on defined methodology of calculating expected credit losses and risk parameters arising from them.

#### **4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

A summary of significant accounting policies adopted in the preparation of financial statements is set out below. The accounting policies have been consistently applied to all the years presented in these financial statements unless stated otherwise.

Where the accounting policies are aligned with accounting principles of International Financial Reporting Standards (hereinafter IFRS or Standards), the description of the Bank's accounting policies may contain a reference to certain standards. Unless otherwise stated, these are the standards applicable at 31 December 2016.

##### **4.1 Financial instruments**

###### ***Classification***

The Bank classifies its financial assets into the following categories: loans and receivables, financial assets available for sale, financial assets at fair value through profit or loss and financial assets held to maturity. The classification depends on the nature and purpose of the instrument acquired. The management determines the classification of financial instruments upon initial recognition.

Financial liabilities are classified as either financial liabilities at fair value through profit or loss or other financial liabilities.

###### ***Loans and receivables***

This category comprises all non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

###### ***Financial assets available for sale***

This category comprises non-derivative financial assets not classified as loans and receivables, held-to-maturity investments, or financial assets at fair value through profit or loss. Financial assets available for sale are intended to be held for an indefinite period of time, but may be sold in response to liquidity needs or changes in interest rates, foreign exchange rates, or equity prices.

###### ***Financial assets at fair value through profit or loss***

This category comprises two subcategories: financial instruments held for trading and those designated by management as at fair value through profit or loss at inception. A financial instrument is classified in this category if it is acquired or incurred principally for the purpose of selling or repurchasing it in the near term, for short-term profit taking, or if designated as at fair value through profit or loss by management.

Financial instruments held for trading include shares (units) in investment funds.

###### ***Financial assets held to maturity***

This category comprises non-derivative financial assets with fixed or determinable payments and fixed maturity not classified as loans and receivables that the Bank intends and is able to hold to maturity. Included in this category are certain debt securities.



#### **4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

##### **4.1 Financial instruments (continued)**

###### ***Other financial liabilities***

Other financial liabilities include all financial liabilities not designated as at fair value through profit or loss.

###### ***Recognition and derecognition***

Purchases and sales of financial assets available for sale are recognised on the trade date, i.e. the date on which the financial instrument is delivered or transferred by the Bank. Loans and receivables, financial assets held to maturity and financial liabilities at amortized cost are recognised at the settlement date when received or issued.

The Bank derecognises financial instruments (in full or part) when the rights to receive cash flows from a financial instrument have expired or when it loses control over the contractual rights to the instrument. This occurs when the Bank has transferred substantially all the risks and rewards of ownership to another entity or when the rights are realized, expired or are surrendered. The Bank derecognises a financial liability only when the liability ceases to exist, i.e. it is discharged, cancelled or expired. If the terms of a financial liability change, the Bank will derecognise the liability and simultaneously recognise a new financial liability with new terms and conditions.

Realized gains and losses from the sale of financial instruments are determined using the weighted average cost method.

###### ***Initial and subsequent measurement***

Available-for-sale financial assets, loans and receivables, held-to-maturity financial assets and liabilities are recognised initially at fair value plus transaction costs directly attributable to the acquisition or issuance of financial assets or financial liabilities.

Financial assets or liabilities at fair value through profit or loss are recognised initially at fair value, with the transaction costs recognised immediately in profit or loss.

The Bank recognises financial assets available for sale and financial assets or liabilities at fair value through profit or loss subsequently at fair value, without any deduction for transaction costs.

Loans and receivables and held-to-maturity investments as well as financial liabilities not designated at fair value through profit or loss are measured at amortised cost using effective interest rate.

###### ***Gains and losses***

Gains or losses arising from a change in the fair value of available-for-sale financial assets are recognised directly in the fair value reserve within equity and are disclosed in the statement of changes in equity. Impairment losses, foreign exchange differences, interest income and amortisation of premium or discount on available-for-sale monetary assets are recognised in profit or loss. When an asset available for sale is sold or otherwise disposed of, any cumulative gains or losses on the instrument are transferred to profit or loss.

Unrealised gains and losses arising from changes in fair value of financial assets at fair value through profit or loss, as well as gains and losses realised on such assets and liabilities when they are sold or otherwise disposed of are included in profit or loss. Interest earned while holding those instrument is included in interest income, and dividends are recognised as dividend income and presented in profit or loss.

#### **4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

##### **4.1 Financial instruments (continued)**

Gains or losses arising from financial assets and financial liabilities carried at amortized cost are included in the income statement over the period of amortization. Gains or losses can also be recognised in profit and loss when the financial instrument is derecognised or impaired.

##### ***Fair value measurement of financial instruments***

Financial instruments carried at fair value are classified into three-level fair value measurements according to the IFRS fair value hierarchy. Level 1 (based on closing prices on regulated markets), Level 2 (based on valuation techniques using inputs observable on the market), and Level 3 (fair value determined using other available data).

##### **Fair value hierarchy for financial assets**

The most reliable fair value measurement is the price quoted in an active market. If the price is observable, it is used as an input for the fair value measurement (Level 1 of the fair value hierarchy).

In absence of a liquid market, the fair value is determined based on observable market indicators, with the instruments measured on the basis of such inputs being classified into Level 2 of the fair value hierarchy.

The fair value of financial instruments traded rarely and whose prices are not readily observable is a less objective measure. Therefore, in calculating the fair value for such a financial asset or liability, all significant risks affecting it should be identified and considered.

In calculating fair value, the Bank considers the rules of the fair value hierarchy that reflect the significance of the measurement inputs. Each instrument is subject to an individual detailed analysis.

Where quoted market prices for a financial instrument are not observable, the fair value of the instrument is determined using valuation models relying on observable market data. If all significant inputs into the model are available, the instrument is classified into Level 2 of the fair value hierarchy.

The fair value hierarchy levels are determined by reference to the lowest level of inputs that are significant for measuring the fair value of the instrument. The fair value measurement levels described further below relate to financial assets reported in the balance sheet at fair value.

##### ***Impairment of financial assets***

##### ***Impairment of assets identified as impaired***

Financial assets are reviewed at each financial statements date to determine whether there is objective evidence of impairment. If any such indication exists, the recoverable amount of an item is estimated.

Individually significant financial assets are tested for impairment on an individual basis. Remaining financial assets are reviewed on a collective basis, in accordance with the relevant CNB regulations. Financial assets not identified as impaired are included in the impairment test for the purpose of a collective assessment.

The Bank first assesses whether objective evidence of impairment exists individually for assets that are individually significant (mainly corporate exposures) and collectively for assets that are not individually significant (mainly retail exposures). However, assets assessed individually as unimpaired are then included in groups of assets with similar credit risk characteristics.

#### **4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

##### **4.1 Financial instruments (continued)**

The Bank estimates impairment losses in cases where it judges that the observable data indicate the likelihood of a measurable decrease in the estimated future cash flows of the asset or portfolio of assets. Such evidence includes delinquency in payments or other indications of financial difficulty of borrowers and adverse changes in the economic conditions in which borrowers operate, or in the value or enforceability of security, where these changes can be correlated with defaults.

The recoverable amount of financial assets measured at amortised cost is calculated as the present value of the expected future cash flows, discounted at the instrument's original interest rate. Short-term balances are not discounted. The carrying amounts of assets are impaired through an allowance account, and the impairment losses are recognised in the income statement.

##### *Impairment of assets not identified as impaired*

In addition to impairment of assets identified as impaired, the Bank recognises impairment in profit or loss in respect of exposures that are not identified as impaired at total amount of 1 % of total exposures, in accordance with the accounting regulations of the CNB.

##### **Cash and cash equivalents**

Cash and cash equivalents include cash and current accounts with the Croatian National Bank with an original maturity of up to 90 days as well as balances with other banks, net of any provision for impairment and uncollectible amounts and items in process of collection.

##### **Debt securities**

Debt securities that the Bank holds for the purpose of short-term profit-taking are classified as assets available for sale and carried at fair value.

##### **Placements with banks**

Placements with banks are classified as loans and receivables and measured at amortised cost less provision for impairment.

#### **4.2 Income tax**

Income tax expense represents the sum of the tax currently payable and deferred tax. Income tax is recognised in profit or loss except to the extent that it relates to items recognised directly in equity or other comprehensive income, in which case it is also recognised in equity or other comprehensive income. Current tax is the expected tax payable on the taxable income for the year, using the tax rates enacted or substantially enacted at the financial statements date, and any adjustments to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation

#### 4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

##### 4.2 Income tax (continued)

purposes. Deferred tax assets and liabilities are measured at tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on tax rates in effect at the balance sheet date.

Deferred taxes are not discounted and are classified in the balance sheet as non-current assets and/or non-current liabilities. Deferred tax assets are recognised only to the extent that it is probable that the related tax benefit will be realised. At each financial statements date, the Bank reviews the unrecognised contingent tax assets and the carrying amount of the recognised tax assets.

##### 4.3 Property and equipment

Items of property and equipment are recognised at historical cost or revalued amount less accumulated depreciation and accumulated impairment losses.

Depreciation is provided on a straight-line basis so as to write down the cost over the estimated useful life of an asset. Land and assets under construction are not depreciated.

The residual values and useful lives of assets are reviewed, and adjusted if appropriate, at each financial statements date. Where the net carrying amount of an asset exceeds its recoverable amount, it is written down immediately to its recoverable amount. Gains and losses on disposal are determined as the difference between the proceeds and the net carrying amount and included in the income statement.

Depreciation is provided on a straight-line basis over the estimated useful life of an asset as follows:

	2016	2015
Buildings	2.50%	2.50%
Computers	25%	25%
Furniture and equipment	10% - 20%	10% - 20%
Motor vehicles	25%	25%
Other tangible assets not mentioned above	5% – 10%	5% – 10%

##### 4.4 Intangible assets

Intangible assets are recognised at cost less accumulated amortization and impairment losses. Development costs are capitalized if all the requirements specified in IAS 38 'Intangible Assets' are met. Amortisation is provided on a straight-line basis over the estimated useful life of an intangible asset.

Amortisation is provided on a straight-line basis over the estimated useful life of an asset as follows:

	2016	2015
Intangible assets (other)	10%–20%	10%–20%
Intangible assets - software	20%–25%	10%–25%

#### **4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

##### **4.5 Foreclosed assets**

For assets acquired in lieu of uncollected receivables the Bank assesses the marketability and only marketable assets, the value of which can be measured reliably, are recognised as assets in the statement of financial position. Such assets are stated at the lower of the cost of related outstanding receivables and the current fair value of that asset. Bank's intention is mainly to sell such assets (such assets are not amortised) or held it to earn rentals (such assets are disclosed within Note 21 Investment property).

##### **4.6 Investment property**

Investment properties are properties which are held by the Bank either to earn rentals or for capital appreciation.

Investment property is measured initially at cost. At subsequent measurement of investment property, the Bank applies the fair value model.

##### **4.7 Impairment of non-financial assets**

Intangible assets that have an indefinite useful life not subject to amortisation and are tested annually for impairment. Depreciable assets are reviewed for impairment whenever events or changes in the circumstances indicate that the carrying amount of an asset may not be recoverable. An impairment loss is determined as the difference between the carrying amount of an asset and its recoverable amount. Recoverable amount is the higher of fair value less costs to sell and value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment loss are reviewed for possible reversal of the impairment at each reporting date.

Property, plant and equipment as well as intangible assets are reviewed for impairment whenever circumstances indicate that the carrying amount of an asset may not be recovered.

When the carrying amount of an asset exceeds its recoverable amount, an impairment loss is recognised in the income statement for items of property, plant and equipment and intangible assets carried at acquisition cost.

##### **4.8 Provisions for liabilities and charges**

The Bank recognises provisions when it has a present legal or constructive obligation as a result of past events and if it is probable that it will have an outflow to settle these obligations whose amount can be reliably estimated.

Provisions for liabilities and charges are maintained at a level which Management believes is adequate to absorb probable future losses. Management determines the adequacy of the provision based upon reviews of individual items, current economic conditions, the risk characteristics of the various categories of transactions and other relevant factors.

When the outflow of economic benefits to settle the obligations is no longer probable or less than the estimated provision is reversed. Provisions are released only for those costs which are originally recognised.

#### **4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

##### **4.9 Employee benefits**

The Bank pays contributions to pension insurance funds on a mandatory, contractual basis, in accordance with the law. The Bank has no further payment obligations once the contributions have been paid. The contributions are recognised as employee benefit expense when they arise.

The Bank recognises a provision for bonuses when there is a constructive obligation resulting from a contract or past practice. Furthermore, the Management recognises accrued benefits on the basis of annual vacation days outstanding at the date of the financial statements.

In calculating provisions for severance payments and jubilee rewards, discounted expected future cash flows arising from the liabilities is performed, using discount rates that, in the opinion of management, best represent the time value of money.

##### **4.10 Share capital and reserves**

Share capital is denominated in the Croatian kunas and stated at nominal value.

##### **4.11 Accumulated losses**

If the Bank recognises a loss for the financial year, it is transferred to accumulated losses.

##### **4.12 Interest income and expense**

Interest income and expense for all interest bearing financial instruments are recognised in the income statement as they accrue, including those measured at amortized cost and those available for sale, using the effective interest rate method. The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability and of allocating interest income or expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of a financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. The calculation inputs include all fees and percentage points paid or received between the parties to the contract that are included in the effective interest rate, as well as transaction costs and all other premiums or discounts. The resulting income and expenses are included in profit or loss within interest income and income expense respectively.

They also include fees and commissions on loans and advances to customers as well as on borrowings from other banks.

##### **4.13 Fee and commission income and expense**

Fee and commission income comprises mainly fees received from customers for loans, guarantees, letters of credit and other services provided by the Bank. Fees are recognised as income upon the maturity date of services.

Fee and commission expense consist of fees paid to licensed banks for payment services provided in the foreign exchange operations, as well as to the Financial Agency services (FINA) for domestic payments.

##### **4.14 Foreign currencies**

Transactions in foreign currencies are translated into Croatian kunas at the rates of exchange applicable at the dates of the transactions. Monetary assets and liabilities that are denominated in foreign currencies are retranslated at the exchange rate in effect at the financial statements date. Foreign exchange differences arising on translation are recognised in the income statement. Non-monetary assets and liabilities denominated in foreign currency that are stated at fair value are translated in HRK at the foreign exchange rates applicable at the dates when the fair values were determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated at the transaction date but are not retranslated at the balance sheet date.

#### **4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

##### **4.14 Foreign currencies (continued)**

Changes in the fair value of monetary securities denominated in foreign currencies and classified as available for sale are analysed as the difference between the exchange differences arisen from changes in the security's amortised cost and other changes in the net carrying amount of the security. Exchange differences are recognised in profit or loss as part of exchange gains and losses on revaluation of monetary assets and liabilities.

##### **4.15 Contingent liabilities and commitments**

In the ordinary course of business, the Bank enters into commitments which are maintained on off-balance-sheet accounts and primarily include guarantees, letters of credit and undrawn loan commitments. Such financial commitments are recognised in the statement of financial position if and when they become payable.

##### **4.16 Rents**

The Bank rents office space to perform operations that are treated as operating leases. The underlying asset is not recognised in the statement of financial position, and payments under operating leases are recognised in the income statement or loss on a straight-line basis over the lease term.

Rental income under operating leases Bank recognises in the profit or loss on a straight-line basis over the lease term.

##### **4.17 Borrowings**

Borrowings are recognised initially at fair value net less costs. Subsequent valuation is carried at amortized cost and the difference between proceeds less transaction costs, and the amount payable at maturity is recognised in the statement of profit or loss during the period of the borrowings as interest expense. The amount was subsequently reduced by the deferred part of the fees paid during the loan approval.

##### **4.18 Activities in the name and on behalf of third parties**

The Bank manages assets on behalf of legal persons. These amounts do not represent the Bank's assets and are excluded from the statement of financial position. For the services provided the Bank charges a fee which is recognised in the statement of profit or loss.

##### **4.19 Reporting by business segments**

A business segment is an integral part of the Bank that engages in business activities from which it may earn revenues or expenses, including transactions with other parts of the Bank. The bank in 2016 did not apply the internal transfer pricing when determining business performance of individual segments.

## 5 Interest income

### 5.1 Interest income analysed by type of customer

	<i>in thousands of HRK</i>	
	2016	2015
Companies	79,703	93,489
Individuals	25,763	28,707
Government units	23,364	24,163
Banks and other financial institutions	1,941	1,417
Other organisations	654	1,258
<b>Total</b>	<b>131,425</b>	<b>149,034</b>

Included in interest income is income from partly recoverable placements in the amount of HRK 5.9 million (2015: HRK 11.1 million), of which HRK 4.4 million (2015: HRK 4.9 million) relate to legal persons, and the remaining HRK 1.5 million (2015: HRK 6.2 million) to individuals.

### 5.2 Interest income analysed by portfolio

	<i>in thousands of HRK</i>	
	2016	2015
Loans and receivables	111,011	127,572
Financial assets available for sale	13,545	19,540
Financial assets held to maturity	6,869	1,922
<b>Total</b>	<b>131,425</b>	<b>149,034</b>

## 6 Interest expense

### 6.1 Interest expense analysed by source

	<i>in thousands of HRK</i>	
	2016	2015
Individuals	40,925	44,848
Banks and other financial institutions	9,621	15,380
Companies	6,581	10,265
Savings deposit insurance costs	5,853	5,440
Non-residents	3,393	3,902
Croatian National Bank	1,673	206
Government units	1,200	2,584
Other organisations	323	341
<b>Total</b>	<b>69,569</b>	<b>82,966</b>



**6 Interest expense (continued)**

**6.2 Interest expense analysed by portfolio**

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Financial liabilities at amortised cost	63,716	77,526
Savings deposit insurance costs	5,853	5,440
<b>Total</b>	<b>69,569</b>	<b>82,966</b>

**7 Fee and commission income**

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Companies	6,628	8,172
Individuals	4,067	3,962
Financial institutions	800	657
Non-profit organisations	265	278
Government units	218	208
Non-residents	78	80
<b>Total</b>	<b>12,056</b>	<b>13,357</b>

**8 Fee and commission expense**

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Service fees and commissions to FINA	2,048	2,386
Domestic partners	2,092	2,275
Foreign banks	179	198
Republic of Croatia	41	35
<b>Total</b>	<b>4,360</b>	<b>4,894</b>

## 9 Net financial gains

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Net gain on financial assets available for sale	6,679	4,115
Net gain on financial assets held to maturity	1,026	-
Net gain on financial assets at fair value through profit or loss	46	270
<b>Total</b>	<b>7,751</b>	<b>4,385</b>

The net gain on assets held to maturity represents the result on early redemption of bonds by the bond issuer, which the Bank classified initially as held to maturity. This event represents an event beyond the Bank's control.

## 10 Net income from exchange differences

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Net foreign exchange gains/(loss) arising from foreign currency clause	4,657	(1,371)
Income from foreign currency trading	3,364	4,057
Net foreign exchange gains on translation of provision for potential credit losses	377	290
Net foreign exchange losses/(gains) arising from foreign currency clause	(5,179)	652
<b>Total</b>	<b>3,219</b>	<b>3,628</b>

## 11 Other operating income

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Rental income	4,451	4,520
Net gains from the sale of property, plant and equipment, and foreclosed assets	1,593	1,070
Suspended interest	62	224
Other income	255	476
<b>Total</b>	<b>6,361</b>	<b>6,290</b>

**12 Other operating expenses**

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Net salaries	19,130	19,587
Contributions, taxes and surtaxes	14,054	14,653
Other staff-related costs	1,899	3,054
Net provision for long-term employee benefits (jubilee awards and termination benefits) (Note 30)	28	(676)
<b>Total staff-related costs</b>	<b>35,111</b>	<b>36,618</b>
Amortization and depreciation (Note 22)	3,470	3,343
<b>Total amortization and depreciation</b>	<b>3,470</b>	<b>3,343</b>
Materials and services	21,018	22,082
Marketing expenses	435	720
Judicial and administrative fees	497	758
Other	1,581	1,387
<b>Total other operating expenses</b>	<b>23,531</b>	<b>24,947</b>
<b>Total</b>	<b>62,112</b>	<b>64,908</b>

At 31 December 2016, the Bank employed 213 persons (31 December 2015: 219 employees).

Personnel expenses include HRK 5,636 thousand (2015: HRK 5,730 thousand) of mandatory pension contributions paid into mandatory pension funds. The contributions are determined at a certain percentage of the employees' gross salaries.

**12.1 Rental costs**

Rental costs mostly relates to rental costs of office space in which the Bank carries out its activities.

**31 December 2016**

	<i>In thousands of HRK</i>		
	<b>Up to 1 year</b>	<b>1 to 3 years</b>	<b>3 to 5 years</b>
Rental cost	6,529	6,529	6,529

**31 December 2015**

	<i>In thousands of HRK</i>		
	<b>Up to 1 year</b>	<b>1 to 3 years</b>	<b>3 to 5 years</b>
Rental cost	5,043	5,270	3,362

**13 Impairment losses and provisions**

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Impairment losses on loans and advances to customers (Note 20.2)	(15,066)	(18,879)
Net change in the provisions for legal actions against the Bank (Note 30)	(5,282)	(1,683)
Impairment of investment property	(1,994)	-
Impairment losses on other assets (including provisions for unidentified losses on a collective basis)	(899)	(937)
Impairment losses on foreclosed assets (Note 23)	(494)	(2,469)
Impairment losses on interest receivable (Note 20.2)	(20)	270
Other provisions	(14)	(15)
Provisions for identified losses for contingent liabilities (Note 30)	36	22
Provisions for unidentified losses on a collective basis for contingent liabilities (Note 30)	66	951
Subsequently recovered placements written-off as uncollectible in prior years	212	1,881
Provisions and impairment allowances on loans and other receivables on a collective basis (Notes 15,16,17,19, 20.2. and 24)	1,348	(804)
<b>Total</b>	<b>(22,107)</b>	<b>(21,663)</b>

**14 Income tax**

*Movements in deferred tax assets*

*in thousands of HRK*

	Deferred fee income /(expenses) included in effective interest rate on given loans/(borrowings)	Deferred income per impairment of foreclosed assets	Deferred income from unrealised change in the fair value of available-for- sale financial assets	Tax losses	Total
<b>At 1 January 2015</b>	2,609	-	-	18,935	21,544
Recognised in profit or loss	(456)	910	-	(17,851)	(17,397)
Recognised in equity and other comprehensive income	-	-	99	-	99
<b>At 31 December 2015</b>	<b>2,153</b>	<b>910</b>	<b>99</b>	<b>1,084</b>	<b>4,246</b>
Recognised in profit or loss	(582)	355	-	(799)	(1,026)
Recognised in equity and other comprehensive income	-	-	(1,322)	-	(1,322)
<b>At 31 December 2016</b>	<b>1,571</b>	<b>1,265</b>	<b>(1,223)</b>	<b>285</b>	<b>1,898</b>

**14 Income tax (continued)**

**Deferred tax assets recognised on tax losses available for carry forward**

Reconciliation between the accounting and tax results is shown as follows:

	2016	2015
<b>Accounting profit before taxation</b>	<b>2,664</b>	<b>2,263</b>
Effect of income tax at the rate of 18% (2015: 20%)	799	453
Effect of tax non-deductible expenses	1,080	1,698
Effect of non-taxable income	(761)	(1,152)
Utilisation of tax losses brought forward	(1,118)	(999)
Effect of change in estimated utilisation of tax losses available for carry forward	92	(16,398)
<b>Income tax</b>	<b>(1,026)</b>	<b>(17,397)</b>

The table below shows the tax effect of deferred tax assets in respect of tax losses carried forward and expected to be utilised in the next 5 years from the end of the reporting period in which they were generated.

The tax losses are expected to be utilised as follows:

*in thousands of HRK*

	2016	2016
	<b>Total tax loss</b>	<b>Tax loss effect</b>
31 December 2017.	1,583	285

Unrecognised deductible temporary differences, unused tax losses and tax approval:

*in thousands of HRK*

Available for transfer up to	Tax loss	The amount of unrecognised deferred tax assets
2017	126,265	22,728
2018	11,010	1,982
<b>Total</b>	<b>137,275</b>	<b>24,710</b>

The possibility of using unrecognised tax approvals expires in 2018.

The amount of unused tax losses are not recognised as deferred tax assets in the statement of comprehensive income because it is not likely that there will be sufficient taxable income to use these deferred tax assets.

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**15 Cash**

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Current account balance	58,866	21,965
Cash in hand:		
- in HRK	14,948	17,891
- in foreign currencies	6,756	9,682
Cash on foreign currency accounts with foreign banks	3,872	21,501
Cash on foreign currency accounts with domestic banks	194,938	33,324
Checks and other assets in course of collection	5	1
<i>Provisions for impairment for unidentified losses on a collective basis</i>	(2,577)	(768)
<b>Total</b>	<b>276,808</b>	<b>103,596</b>

**16 Receivables from the Croatian National Bank**

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Obligatory reserve		
- in HRK	192,439	195,919
- in foreign currencies	-	32,502
Other obligatory deposits	1,206	-
<i>Provisions for impairment for unidentified losses on a collective basis</i>	(1,936)	(2,284)
<b>Total</b>	<b>191,709</b>	<b>226,137</b>

The CNB imposes a requirement to banks to calculate an obligatory reserve, which is required to be deposited with the CNB and held in the form of other liquid receivables.

The obligatory reserve requirement as at 31 December 2016 was 12 % (2015: 12 %) of deposits, borrowings and issued debt securities denominated in kunas and foreign currencies.

As at 31 December 2016, the required rate for the part of the obligatory reserve calculated based on kuna liabilities to be deposited with the CNB amounted to 70%, 0 percent of the foreign-currency denominated balance (2015: 60%), whereas the remaining 30 percent (2015: 30%) could be held in the form of other liquid receivables. This includes the part of foreign currency obligatory reserve required to be held in HRK. The foreign-currency portion of the obligatory reserve is maintained through daily balances of foreign-currency receivables on the Target 2 foreign-currency account with the Croatian National Bank as well as on accounts with foreign banks with appropriate ratings. The minimum share of the foreign-currency reserve funds on the CNB Target2 reserve account is 2 percent, whereas 75 percent of the foreign-currency reserve funds are included in the allocated kuna-denominated obligatory reserve funds and maintained in kunas.

**17 Placements with banks**

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Deposits with foreign banks	52,016	46,484
Deposits with domestic banks	1,837	1,985
Accrued interest	20	1
<i>Provisions for impairment for unidentified losses on a collective basis</i>	<i>(539)</i>	<i>(485)</i>
<b>Total</b>	<b>53,334</b>	<b>47,985</b>

**18 Financial assets available for sale**

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Treasury bills /i/	498,257	520,302
HRK-denominated bonds /ii/	202,756	77,145
Foreign-currency denominated bonds /iii/	125,265	76,552
Corporate bills	774	774
Shares /iv/	439	439
<i>Provisions for impairment for unidentified losses on a collective basis</i>	<i>(774)</i>	<i>(774)</i>
Accrued interest	7,056	3,294
<b>Total</b>	<b>833,773</b>	<b>677,732</b>

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**18 Financial assets available for sale (continued)**

	<i>In thousands of HRK</i>				
	Treasury bills	Bonds	Shares	Accrued interest	TOTAL
<b>At 01 January 2016</b>	<b>520,302</b>	<b>153,697</b>	<b>439</b>	<b>3,294</b>	<b>677,732</b>
Increase	582,634	341,254	-	3,762	927,650
Changes in fair value	-	7,287	-	-	7,287
Decrease	(604,679)	(174,217)	-	-	(778,896)
<b>At 31 December 2016</b>	<b>498,257</b>	<b>328,021</b>	<b>439</b>	<b>7,056</b>	<b>833,773</b>
<b>At 01 January 2015</b>	<b>481,380</b>	<b>109,608</b>	<b>439</b>	<b>2,203</b>	<b>593,630</b>
Increase	778,315	129,895	-	1,091	909,301
Changes in fair value	-	(3,103)	-	-	(3,103)
Decrease	(739,393)	(82,703)	-	-	(822,096)
<b>At 31 December 2015</b>	<b>520,302</b>	<b>153,697</b>	<b>439</b>	<b>3,294</b>	<b>677,732</b>

As of 31 December 2016 Bank has pledged, based on received repo loans of the Croatian National Bank in the amount of HRK 160,000 thousand (2015:HRK 130 thousand), treasury bills and government bonds worth HRK 172,603 thousand (2015.: HRK 162,391 thousand of treasury bills), whereas it accepted from domestic companies shares in the total amount of HRK 5,308 thousand for repo loans issued in the amount of HRK 3,500 thousand (the Bank did not issue any repo loans in 2015).

/i/ The treasury bills relate to:

- HRK 130,000 thousand (nominal) of HRK treasury bills (2015: HRK 220,000 thousand) issued by the Croatian Ministry of Finance with a yield of 0,951% - 1,457% (2015: 1,496% - 1,504%)
- HRK 287.196 thousand (nominal) of foreign currency treasury bills (2015: HRK 285,065 thousand) issued by the Croatian Ministry of Finance with a yield of 0,70% (2015: 1,95%).
- HRK 83.136 thousand (nominal) of treasury bills (2015: HRK 45.810 thousand) issued by the Croatian Ministry of Finance and tied under a currency protection clause, with a yield of 0,171% - 0,249% (2015: 0,201% - 0,250%).

/ii/ HRK-denominated bonds comprise the following:

- HRK 12,000 thousand (nominal) in respect of a bond issued by the Croatian Ministry of Finance that matures on 10 July 2018, with a nominal interest rate of 5.250% (the same as in the same as in 2015)
- HRK 15,000 thousand (nominal) in respect of a bond issued by the Croatian Ministry of Finance that matures on 8 February 2017, with a nominal interest rate of 4.750% (the same as in 2015)
- HRK 4,780 thousand (nominal) in respect of a bond issued by Hrvatska pošta that matures on 10 November 2019, with a nominal interest rate of 5.125% (the same as in 2015)
- HRK 4,500 thousand (nominal) in respect of a bond issued by the Croatian Ministry of Finance that matures on 9 July 2025, with a nominal interest rate of 4.500% (the same as in 2015)
- HRK 12,800 thousand (nominal) in respect of a bond issued by the Croatian Ministry of Finance that matures on 14 December 2026, with a nominal interest rate of 4.250% (the same as in 2015)
- HRK 20,000 thousand (nominal) in respect of a bond issued by the Croatian Ministry of Finance that matures on 8 July 2021, with a nominal interest rate of 2.750% (the same as in 2015)



**18 Financial assets available for sale (continued)**

/iii/ The foreign-currency denominated bonds comprise the following:

- HRK 22,673 thousand (nominal) in respect of a bond issued by the Croatian Ministry of Finance (2015: HRK 22,905 thousand ) that matures on 30 May 2022, with a nominal interest rate of 3,875% (2015: 3,875%)
- HRK 75,578 thousand (nominal) in respect of a bond issued by the Croatian Ministry of Finance that matures on 11 March 2025, with a nominal interest rate of 3.000%
- HRK 22,673 thousand (nominal) in respect of a bond issued by the Croatian Ministry of Finance (2015: HRK 22,905 thousand ) that matures on 9 July 2018, with a nominal interest rate of 5.875% (2015: 5,875%)

/iii/ The bonds with a currency protection clause comprise the following:

- HRK 133,367 thousand (nominal) in respect of a bond issued by the Croatian Ministry of Finance that matures on 10 July 2024, with a nominal interest rate of 5.750%
- HRK 756 thousand (nominal) in respect of a bond issued by the Croatian Ministry of Finance(2015: HRK 763 thousand ) that matures on 22 July 2022, with a nominal interest rate of 6.500% (2015: 6,500%)

/iv/ The shares relate to the Bank's equity interest in companies and financial institutions below 20%.

The shares are not quoted and comprise the following:

- 1,044 units of the Croatian Register of Debtors
- 85 shares of Tržište novca Zagreb (TNZ-R-A).

	2016			in thousands of HRK 2015		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Foreign-currency bonds	125,265	-	-	76,552	-	-
HRK bonds	202,756	-	-	77,145	-	-
Treasury bills	-	498,257	-	-	520,302	-
Shares	-	-	439	-	-	439
<b>Total</b>	<b>328,021</b>	<b>498,257</b>	<b>439</b>	<b>153,697</b>	<b>520,302</b>	<b>439</b>

Financial instruments carried at fair value are categorised into three levels of the IFRS fair value hierarchy, as follows:

- Level 1 - instruments that are valued using quoted prices in active markets, liquid markets. These instruments include: liquid debt securities that are traded on liquid stock markets and shares in investment funds.
- Level 2 – Instruments measured using valuation techniques using observable market data. The fair value of those instruments is determined by reference to similar instruments traded on active markets, or where all inputs used in a particular valuation technique are available on the market. These instruments include less liquid debt securities that are valued based on a model that uses Level 1 input.
- Level 3 – instruments measured using valuation techniques that are based on market data not readily available in the market. These are instruments whose fair value cannot be determined directly by reference to available market information and for whose value calculation different valuation techniques are used. These instruments include illiquid debt securities and illiquid equity securities.

**19 Assets held to maturity**

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Domestic currency bills of exchange	46,358	19,065
HRK bonds	4,766	4,763
Foreign-currency bonds	-	24,550
<i>Accrued interest</i>	34	693
<i>Provisions for impairment for unidentified losses on a collective basis</i>	(511)	(492)
<b>Total</b>	<b>50,647</b>	<b>48,579</b>

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**20 Loans and advances to customers**

**20.1 Analysis by type of client**

Analysis by type of client (including accrued interest and provision for interest)

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
<b>Individuals</b>		
Cash loans	168,905	134,772
Housing loans	57,895	52,520
Loans for agriculture	48,821	50,204
Margin loans	25,935	16,798
Lombard loan	15,510	11,729
Overdrafts on transaction accounts	14,983	13,424
Loans for tourism	14,869	15,447
Mortgage loans	7,882	9,175
Other loans	57,590	62,883
<b>Total loans to individuals</b>	<b>412,390</b>	<b>366,952</b>
<i>Provisions for impairment for identified losses</i>	<i>(32,802)</i>	<i>(28,467)</i>
<i>Provisions for impairment for unidentified losses on a collective basis</i>	<i>(3,575)</i>	<i>(3,100)</i>
<i>Interest impairment provision - individuals</i>	<i>(437)</i>	<i>(481)</i>
<i>Total provisions for impairment - individuals</i>	<i>(36,814)</i>	<i>(32,048)</i>
Accrued interest	2,585	2,541
<b>Total loans to individuals, net</b>	<b>378,161</b>	<b>337,445</b>
<b>Legal persons (Corporate customers)</b>		
Syndicated loans	704,802	816,578
Investment loans	293,641	516,840
Working-capital loans	175,470	148,465
Overdrafts on transaction accounts	35,833	37,626
Lombard loans	28,964	24,078
Loans for agriculture	13,766	14,668
Loans for construction	9,856	10,234
Loans for payments under guarantees	7,071	8,427
Other loans	150,596	184,932
<b>Total loans to legal persons</b>	<b>1,419,999</b>	<b>1,761,848</b>
<i>Provisions for impairment for identified losses</i>	<i>(203,784)</i>	<i>(201,986)</i>
<i>Provisions for impairment for unidentified losses on a collective basis</i>	<i>(10,755)</i>	<i>(14,252)</i>
<i>Interest impairment provision - legal persons</i>	<i>(1,893)</i>	<i>(1,662)</i>
<b>Total provisions for impairment</b>	<b>(216,432)</b>	<b>(217,900)</b>
Accrued interest	8,915	11,110
<b>Total loans to legal persons, net</b>	<b>1,212,482</b>	<b>1,555,058</b>
<b>Total loans</b>	<b>1,843,889</b>	<b>2,142,451</b>
<i>Total loan provision</i>	<i>(253,246)</i>	<i>(249,948)</i>
<b>Total net sales</b>	<b>1,590,643</b>	<b>1,892,503</b>

## 20 Loans and advances to customers (continued)

As at 31 December 2016, the total gross exposure arising from partly recoverable and non-recoverable loans was HRK 411,942 thousand (2015: HRK 413,794 thousand), and the associated impairment losses amounted to HRK 236,586 thousand (2015: HRK 230,453 thousand).

### 20.2 Changes in impairment losses and provision for contingent losses

Changes in impairment losses and provision for contingent losses are as follows:

	2016			2015		
	Impairment	Specific provisions for unidentified losses on a collective basis	Total	Impairment	Specific provisions for unidentified losses on a collective basis	Total
<b>Balance at 1 January</b>	<b>232,596</b>	<b>17,352</b>	<b>249,948</b>	<b>235,585</b>	<b>16,716</b>	<b>252,301</b>
Net impairment losses i.e. provisions (Note 13)	15,066	(3,022)	12,044	18,879	636	19,515
Net impairment losses on interest receivable (Note 13)	20	-	20	(270)	-	(270)
Exchange differences	(383)	-	(383)	292	-	292
Write-offs	(8,383)	-	(8,383)	(21,890)	-	(21,890)
<b>Balance at 31 December</b>	<b>238,916</b>	<b>14,330</b>	<b>253,246</b>	<b>232,596</b>	<b>17,352</b>	<b>249,948</b>

Under the applicable legislation, the Bank has to form reserves for unidentified losses on a loan portfolio basis based on prior experience. Taking into account the legal provisions, the amount of the reserves by the Bank's policies cannot be less than 1% of non-risk assets and 1% of non-risk commitments and contingencies as at 31 December 2016 (2015: 1% of non-risk assets and 1% of non-risk commitments and contingencies).

## 21 Investment property

	in thousands of HRK	
	2016	2015
Investment property	33,702	35,696
<b>Total</b>	<b>33,702</b>	<b>35,696</b>

Investment properties are properties which are held by the Bank either to earn rentals or for capital appreciation. Bank made in 2016 an impairment of the asset values in accordance with the new assessment of its market value. Investment property is measured initially at cost. Fair value reflects income from operating leases and other assumptions otherwise considered by other market participant in determining the fair value of investment property under the current market conditions. The reported fair value reflects the market conditions prevailing for an asset at the same location and in the same condition under a similar lease agreement.

**21 Investment property (continued)**

Investment property contains one property on the basis of which the Bank earns income from the lease. The contract with the tenant was concluded for an indefinite period and because very good business relationship of many years and the attractiveness of the location, the Bank does not expect contract termination in the coming period of 5 years.

Under the contract, the Bank has no obligation to invest in the premises, and incurred no costs in this respect.

**21.1 Lease income and expense**

**31 December 2016**

	<i>in thousands of HRK</i>		
	Up to 1 year	1 to 3 years	3 to 5 years
Received lease payments - income	3,780	4,200	4,200

**31 December 2015**

	<i>in thousands of HRK</i>		
	Up to 1 year	1 to 3 years	3 to 5 years
Received lease payments - income	4,212	8,424	8,424

**21.2 Fair value hierarchy**

	<i>in thousands of HRK</i>			
	Level 1	Level 2	Level 3	Total
<b>Balance at 31 December 2016</b>				
Investment property	-	-	33,702	33,702
<b>Total assets</b>	-	-	<b>33,702</b>	<b>33,702</b>
<b>Balance at 31 December 2015</b>				
Investment property	-	-	35,696	35,696
<b>Total assets</b>	-	-	<b>35,696</b>	<b>35,696</b>

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**22 Property and equipment, and intangible assets**

*in ths. of HRK*

	Land and buildings	Furniture and vehicles	Equipment and other tangible assets	Tangible assets under construction	Total tangible assets	Intangible assets	Intangible assets under development	Total intangible assets	Grand total
<b>Cost</b>									
<b>Balance at 31 December 2014</b>	33,329	8,852	23,877	14	66,072	27,654	-	27,654	93,726
Additions	-	18	600	30	648	2,935	270	3,205	3,853
Disposals and retirements	(5,182)	(467)	(1,696)	-	(7,345)	(2,984)	-	(2,984)	(10,329)
<b>Balance at 31 December 2015</b>	28,147	8,403	22,781	44	59,375	27,605	270	27,875	87,250
Transferred from/to	-	-	-	(30)	(30)	-	(30)	(30)	(60)
Additions	434	86	1,197	-	1,717	2,410	-	2,410	4,127
Disposals and retirements	(3,873)	(757)	(2,373)	-	(7,003)	(152)	-	(152)	(7,155)
<b>Balance at 31 December 2016</b>	24,708	7,732	21,605	14	54,059	29,863	240	30,103	84,162
<b>Accumulated depreciation/amortisation</b>									
<b>Balance at 31 December 2014</b>	17,716	7,594	21,316	-	46,626	25,124	-	25,124	71,750
Charge for the year 2014	714	368	815	-	1,897	1,446	-	1,446	3,343
Disposals and retirements	(2,615)	(462)	(1,666)	-	(4,743)	(2,984)	-	(2,984)	(7,727)
<b>Balance at 31 December 2015</b>	15,815	7,500	20,465	-	43,780	23,586	-	23,586	67,366
Charge for the year 2015	579	348	800	-	1,727	1,743	-	1,743	3,470
Disposals and retirements	(1,843)	(755)	(2,277)	-	(4,875)	(152)	-	(152)	(5,027)
<b>Balance at 31 December 2016</b>	14,551	7,093	18,988	-	40,632	25,177	-	25,177	65,809
<b>Net book value at 31 December 2014</b>	15,613	1,258	2,561	14	19,446	2,530	-	2,530	21,976
<b>Net book value at 31 December 2015</b>	12,332	903	2,316	44	15,595	4,019	270	4,289	19,884
<b>Net book value at 31 December 2016</b>	10,157	639	2,617	14	13,427	4,686	240	4,926	18,353

During the year, the Bank retired certain items of property and equipment with a total cost of HRK 3,047 thousand (2015: HRK 4,978 thousand) and sold a portion in the amount of HRK 1,980 thousand (2015: HRK 5,351 thousand).

At 31 December 2016 no freehold assets of the Bank were pledged as collateral, nor in 2015.

At 31 December 2016 the balance of assets still in used although fully written off amounts to HRK 28,262 thousand (2015: HRK 30,464 thousand).

### 23 Foreclosed assets

Changes in foreclosed assets for uncollected receivables are as follows:

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
<b>Balance at 1 January</b>	<b>24,539</b>	<b>28,842</b>
Increase based on foreclosing assets	391	1,016
New provisions/impairment made (Note 13)	(494)	(2,470)
Other adjustments (transfer of assets upon final settlement)	(178)	-
Foreclosed assets sold	(869)	(2,849)
<b>Balance</b>	<b>23,389</b>	<b>24,539</b>

In 2016 the Bank foreclosed assets in the amount of HRK 869 thousand (2015: HRK 2,849 thousand) and realised a gain in the amount of HRK 1,593 thousand (2015: HRK 1,070 thousand).

### 24 Other assets

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Receivables from the state	17,759	17,759
Receivables based on payments deposited with court by third purchasers	10,593	-
Trade receivables	8,422	9,745
Other receivables from employees	4,539	4,516
Fees and commissions receivable	4,013	4,109
Other receivables	3,955	4,047
Receivables from domestic legal persons based on paid court costs	2,656	2,696
Items in course of collection	2,293	2,220
Provisions for unidentified losses on a collective basis	(182)	(42)
Provisions for individually identified losses	(18,289)	(17,380)
<b>Total other assets</b>	<b>35,759</b>	<b>27,670</b>

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**25 Liabilities to banks**

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Demand deposits		
- in HRK	3,114	22,572
- in foreign currencies	667	16,400
<b>Total demand deposits</b>	<b>3,781</b>	<b>38,972</b>
Term deposits		
- in HRK	86,900	69,330
- in foreign currencies	1,233	1,231
<b>Total term deposits</b>	<b>88,133</b>	<b>70,561</b>
Accrued interest	181	370
<b>Total</b>	<b>92,095</b>	<b>109,903</b>

**26 Demand deposits**

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Demand deposits - individuals		
- in HRK	86,856	80,427
- in foreign currencies	78,566	86,937
<b>Total demand deposits from individuals</b>	<b>165,422</b>	<b>167,364</b>
Demand deposits - corporate		
- in HRK	190,245	166,958
- in foreign currencies	9,175	10,210
<b>Total corporate deposits</b>	<b>199,420</b>	<b>177,168</b>
Demand deposits - financial institutions		
- in HRK	1,861	1,046
- in foreign currencies	2	2
<b>Total deposits from financial institutions</b>	<b>1,863</b>	<b>1,048</b>
Demand deposits - government and other institutions		
- in HRK	62,648	86,958
- in foreign currencies	12,722	9,289
<b>Total demand deposits from government and other institutions</b>	<b>75,370</b>	<b>96,247</b>
Restricted deposits		
- in HRK	2,630	3,405
- in foreign currencies	16,253	16,487
<b>Total restricted deposits</b>	<b>18,883</b>	<b>19,892</b>
Deposits from foreign entities		
- in HRK	2,031	2,280
- in foreign currencies	8,946	9,277
<b>Total deposits from foreign entities</b>	<b>10,977</b>	<b>11,557</b>
<b>Total</b>	<b>471,935</b>	<b>473,276</b>



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**27 Term deposits**

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Deposits from individuals		
- in HRK	161,764	168,912
- in foreign currencies	1,425,625	1,351,095
<b>Total term deposits from individuals</b>	<b>1,587,389</b>	<b>1,520,007</b>
Deposits - corporate		
- in HRK	97,051	141,531
- in foreign currencies	35,585	40,194
<b>Total corporate term deposits</b>	<b>132,636</b>	<b>181,725</b>
Deposits - financial institutions		
- in HRK	110,820	131,833
- in foreign currencies	680	-
<b>Total term deposits from financial institutions</b>	<b>111,500</b>	<b>131,833</b>
Deposits - government and other institutions		
- in HRK	23,740	32,339
<b>Total term deposits from government and other institutions</b>	<b>23,740</b>	<b>32,339</b>
Deposits from foreign entities		
- in HRK	3,997	3,251
- in foreign currencies	137,761	135,517
<b>Total deposits from foreign entities</b>	<b>141,758</b>	<b>138,768</b>
<b>Deposits from non-profit organisations - foreign-currency denominated</b>	<b>-</b>	<b>76</b>
Accrued interest	47,539	27,928
<b>Total</b>	<b>2,044,562</b>	<b>2,032,676</b>

**28 Borrowings**

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Croatian National Bank	160,000	130,000
Domestic banks	129,922	162,435
Accrued interest	2,081	291
<b>Total</b>	<b>292,003</b>	<b>292,726</b>

### 29 Other liabilities

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Amounts due to employees	2,771	2,970
Liabilities for savings deposit insurance	1,518	1,434
Deferred income and accrued expenses	1,440	1,430
Other liabilities	1,357	1,020
Liabilities to suppliers	1,281	1,431
Amounts owed for insured deposits of bankrupt banks /i/	412	1,190
Fees and commissions payable	330	294
<b>Total</b>	<b>9,109</b>	<b>9,769</b>

/i/ The State Agency for Bank Rehabilitation is making payments of insured deposits of bankrupt banks (Credo banka and Centar banka) through the Bank. The amount payable by the Bank in 2016 under claims of insured deposit holders is HRK 412 thousand (2015: HRK 1,190 thousand).

### 30 Provisions

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
Provisions for judicial proceedings	9,004	6,453
Provisions for contingent liabilities and commitments	1,534	1,637
Vacation accruals	100	72
Other provisions	38	24
<b>Total</b>	<b>10,676</b>	<b>8,186</b>

Changes in provisions are shown as follows:

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
<b>Balance at 1 January</b>	<b>8,186</b>	<b>9,301</b>
Income from reversal of provisions for legal claims against the bank (Note 13)	(848)	(2,056)
New provisions made for judicial proceedings (Note 13)	6,130	3,739
Changes in provisions for commitments and contingencies (Note 13)	(102)	(973)
Income from reversal of provisions for jubilee awards, termination and similar benefits	28	(676)
Changes in other provisions	14	12
Changes in payments made under legal actions	(2,732)	(1,161)
<b>Balance at 31 December</b>	<b>10,676</b>	<b>8,186</b>

In 2016 the Bank paid HRK 2,732 thousand from the provisions for judicial proceedings (2015: HRK 1,161 thousand).

Provisions for off-balance-sheet exposure to credit risk and legal claims are recognised in profit or loss as other losses from impairment and provisions (Note 13).

### 31 Share capital

The only shareholder of the Bank as at 31 December 2016 and 31 December 2015 is the State Agency for Deposit Insurance and Bank Rehabilitation.

	<i>in thousands of HRK</i>	
	2016	2015
Share capital	474,600	474,600
Accumulated losses	(292,174)	(277,040)
Reserves	5,571	(395)
Profit/(loss) for the year	1,638	(15,134)
<b>Total equity</b>	<b>189,635</b>	<b>182,031</b>

The share capital in the amount of HRK 474,600 thousand (31 December 2015: HRK 474,600 thousand) consists of 4,746,000 shares with a nominal value of HRK 100 per share (31 December 2015: 4,746,000 shares with a nominal value of HRK 100 per share).

### 32 Earnings per share

	<i>in thousands of HRK</i>	
	2016	2015
Profit/(loss) for the year	1,638	(15,134)
Number of shares (in thousands)	4,746	4,746
<b>Earnings/(loss) per share</b>	<b>0.35</b>	<b>(3.19)</b>

### 33 Contingent liabilities and commitments

*in thousands of HRK*

	2016	2015
Other common risk-bearing off-balance sheet items	60,444	50,861
Guarantees	46,373	74,797
Revolving loans	45,278	35,502
Unbacked letters of credit	1,143	2,356
<b>Total</b>	<b>153,238</b>	<b>163,516</b>

### 34 Legal actions

More than 200 legal claims from ex-shareholders of the Bank, and around thirty legal actions on other grounds have been initiated against the Bank.

The Bank assesses the potential outflow of cash under proceedings carrying a risk of loss and forms appropriate provisions in accordance with its internal act and applicable regulations.

As at 31 December 2016, the provisions for losses from legal claims filed against the Bank amounted to HRK 9,004 thousand (2015: HRK 6,453 thousand).

Due to mentioned above, ex-shareholders of the Bank, suing the Bank for the return of shares and compensation for share cancellation, have filed more than 200 legal claims against the Bank. Until 31 December 2016 several dozens of final court decisions were issued in favour of the Bank.

Until the date of this report almost all proceedings were completed, with the majority being ruled in favour of the Bank, and only several proceedings ruled in favour of the shareholders. However, as these proceedings pertain to the ownership of shares, they do not produce a significant impact on the financial operations of the Bank. Constitutional appeals were filed in cases where the judgements were in favour of the shareholders, and the Constitutional Court made the decision to acknowledge the Bank's constitutional appeals and returned the cases to the commercial court for retrial.

### 35 Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise the following:

*in thousands of HRK*

	2016	2015
Cash in hand and on current accounts with banks (Note 15)	279,385	104,364
Balances with other banks with maturities of up to 3 months (Note 17)	53,873	48,470
<b>Total</b>	<b>333,258</b>	<b>152,834</b>

### 36 Transactions with related parties

The Bank is fully (100%) owned by the State Agency for Deposit Insurance and Bank Rehabilitation (DAB). The Bank considers to be directly related to its shareholder, Supervisory Board and Management Board members and other executive management (jointly referred to as "the key management personnel"), close members of their families, companies jointly controlled or significantly influenced by the Managing Board members and close members of their families, in accordance with the definition of the related party provided in International Accounting Standard 24 "Related Party Disclosures" (IAS 24). Key management includes members of the Management Board, Department directors, directors of branches and directors of control function departments. At 31 December 2016, the key management personnel of the Bank consisted of 29 persons (2015: 30 employees).

The balances of assets and liabilities as well as income and expenses as at 31 December 2016 and 31 December 2015 and for the years then ended resulting from key transactions with related parties are as follows:

*in thousands of HRK*

<b>2016</b>	Receivables	Liabilities	Income	Expenses
DAB (sole shareholder)	61	19,703	11	5,896
<b>Key management personnel</b>				
Short-term (a vista deposits, bonuses, salaries and fees)	4	614	24	9,182
Long-term (loans, deposits and other benefits)	8,832	1,899	324	46
State in narrow and broad definitions	1,659,453	317,276	59,139	10,143
<b>Total</b>	<b>1,668,350</b>	<b>339,492</b>	<b>59,498</b>	<b>25,267</b>

*in thousands of HRK*

<b>2015</b>	Receivables	Liabilities	Income	Expenses
DAB (sole shareholder)	11	40,939	7	5,474
<b>Key management personnel</b>				
Short-term (a vista deposits, bonuses, salaries and fees)	25	597	14	11,124
Long-term (loans, deposits and other benefits)	8,372	2,181	301	60
State in narrow and broad definitions	1,691,561	352,370	70,794	11,832
<b>Total</b>	<b>1,699,969</b>	<b>396,087</b>	<b>71,116</b>	<b>28,490</b>

### 36 Transactions with related parties (continued)

Key management personnel do not hold any of the Bank's shares. Loans and receivables from customers include HRK 8,402 thousand (2015: HRK 7,867 thousand) of loans to key management personnel. During the year, the Bank collected interest in the amount of HRK 319 thousand (2015: HRK 265 thousand) from loans and receivables in respect of key management personnel, which were approved at annual interest rates ranging from 3,00% - 5,23% (2015: 3.80% to 7.33%). The balance of current accounts and deposits of customers includes term deposits of key management personnel in the amount of HRK 1,899 thousand (2015: HRK 1,641 thousand). The interest paid on those deposits in 2015 amounts to HRK 50 thousand (2015: HRK 62 thousand), and the interest rates ranged from 0.10% to 3.33% (2015: 0.10% to 3.85%).

Expenses in respect of the Supervisory Board for 2016 amount to HRK 312 thousand (2015: HRK 411 thousand).

Transactions with the state in narrow and broad definitions comprise transactions with:

- the Central Government,
- local governments,
- public non-financial companies,
- public insurance companies and pension funds,
- public auxiliary financial institutions,
- other monetary financial institutions of the state,
- other public financial intermediaries.

As at 31 December 2016, the exposure to the state in narrow and broad definitions comprises the exposure to state-owned company Hrvatske autoceste d.o.o. in the amount of HRK 424,026 thousand (2015: HRK 480,028 thousand) in respect of a syndicated loan.

The Bank also has an exposure under a syndicated loan to state-owned company Hrvatske ceste in the amount of HRK 174,988 thousand (2015: HRK 218,288 thousand), whereas the loan in the amount of HRK 165,720 thousand provided to Restructuring and Sale Center (CERP) became due and was fully repaid in late 2016. The Bank's exposure to HŽ Cargo amounts to HRK 94,593 thousand (2015: HRK 99,926 thousand). The Bank is exposed to amounts owed by Borovo d.d. of HRK 17,760 thousand (2015: HRK 18,726 thousand). Receivables from Đuro Đaković Holding amount to HRK 33,673 thousand (2015: HRK 30,650 thousand).

The Bank's exposures to the Ministry of Finance comprise those on the Ministry's quoted bonds in the amount of HRK 620,570 thousand (2015: HRK 136,992 thousand) and the treasury bills in the amount of HRK 212,765 thousand (2015: HRK 520,302 thousand) issued by the Ministry of Finance.

The restricted deposit of the Ministry of Finance amounts to HRK 15,116 thousand (2015: HRK 15,270 thousand).

As at 31 December 2016, the Restructuring and Sale Centre holds on the transaction account at the Bank HRK 36,903 thousand (2015: HRK 31,965 thousand).

As at 31 December 2016, the Bank's shareholder, the State Agency for Deposit Insurance and Bank Rehabilitation, holds on the transaction account HRK 18,185 thousand (2015: HRK 40,939 thousand).

At 31 December 2016 the amount owed by the Bank for loans received from the Croatian Bank for Reconstruction and Development (joint customer funding with CBRD) HRK 130,754 thousand (31 December 2015: HRK 164,750 thousand).

All the above-mentioned significant transactions with the state and state-owned companies were entered into on a market-based principle.

**36 Transactions with related parties (continued)**

Income recognised in the profit and loss for 2016 treated as key transactions is as follows:

- income from loans to Hrvatske autoceste for the year 2016 in the amount of HRK 22,188 thousand (2015: HRK 23,315 thousand).
- income from loans to Hrvatske ceste for the year 2016 in the amount of HRK 10,382 thousand (2015: HRK 13,119 thousand).
- income from bonds issued by the Ministry of Finance in the amount of HRK 17,523 thousand (2015 : HRK 5,444 thousand).
- income from treasury bills issued by the Ministry of Finance amounts to HRK 1,911 thousand (2015 : HRK 10,916 thousand).

Expenses recognised in the profit and loss treated as key transactions is as follows:

- term deposit from Hrvatske autoceste d.o.o. in the amount of HRK 1,118 thousand (2015: HRK 223 thousand).
- costs of loans received from CBRD in 2016 in the amount of HRK 4,524 thousand (2015: HRK 5,553 thousand).
- expenses in respect of DAB relate to costs for the savings deposit insurance and rental expenses in the amount of HRK 5,853 thousand and to transaction account costs in the amount of HRK 44 thousand (2015: HRK 5,440 thousand : HRK 28 thousand).

Exposures under receivables from key management personnel and the state in broad and narrow definitions include off-balance sheet receivables of the Bank in the following amounts:

<i>in thousands of HRK</i>	Key management personnel	State in narrow and broad definitions
<b>2016</b>		
Guarantees	-	6,873
Credit lines	430	9,173

*in thousands of HRK*

<b>2015</b>		
Guarantees	-	194
Credit lines	471	2,057

The Bank's maximum off-balance sheet exposure to the state in narrow and broader definitions relates to Narodne novine d.d. and amounts to HRK 10,383 thousand (2015: to Hrvatske autoceste in the amount of HRK 816 thousand). All the exposures presented in this note are presented on a net basis, i.e. less identified and unidentified impairment losses.

### **37 Risk management policies**

Details on the Bank's exposure to risks and methods the Management Board used to manage those risks are described below. The key financial risks to which the Bank is exposed comprise credit risk, liquidity risk and market risk. Market risk includes currency risk, interest rate risk and price risk.

#### **37.1 Credit risk**

The Bank is continually exposed to credit risk arising from its lending and investing activities and in cases where it acts as an intermediary on behalf of customers or other third parties.

The Bank's primary exposure to credit risk arises from loans and receivables from customers and banks and investments in securities. In addition, the Bank is exposed to credit risk on its off-balance sheet items, reflecting its commitments under undrawn facilities and guarantees issued.

Credit risk is the greatest individual risk arising from the Bank's operations; therefore, all organisational units and functions of the Bank monitor the risk closely. Credit risk management and controls are centralised within the Risk Management Office that provides regular risk reports to the Management Board, other bodies of the Bank, its Supervisory Board and senior management.

For the purpose of credit risk management, the Bank has spread its principal credit risk management activities over the following processes:

- loan approval
- loan monitoring
- loan portfolio analysis
- non-performing loans
- early warning of increased credit risk
- loan classification according to the magnitude of risk.

Establishing appropriate relations between the individual processes is a particularly important process, as it helps prevent any process overlaps and misalignment and establishes the necessary level of segregation of duties and responsibilities for the processes.

Organisational responsibilities for credit risk management are divided among the responsibility structures of sales and back-office/organisational units/functionalities, among control and management functions, and operation support, and are additionally positioned for all credit risk management segments, including:

- risk identification and monitoring
- risk analysis and supervision
- risk measurement/assessment
- risk controls
- risk reporting



### **37 Risk management policies (continued)**

#### **37.1 Credit risk (continued)**

Loan analysis is organisationally placed within the Risk Management Function whose scope of responsibilities directly affect the credit risk management, primarily in developing analyses and opinions regarding the Bank's credit risk appetite, which includes the following sub-processes:

- Providing opinion on new credit placements
- Providing opinion on proposals for changes to the conditions for the already existing placements
- Analysing the viability of proposed renewal and restructuring of the existing placements
- Periodic reviews of all existing placements.

In analysing placements that belong to the credit risk management area, the Risk Management Service also estimates the acceptability of credit risk by individual placements, in accordance with the standards and criteria of best banking practice, i.e. application of the effective (external and internal) normative regulations. It communicates its views/principles of assessing the credit risk acceptability to decision-making individuals and bodies responsible for loans.

Further responsibilities of staff engaged in loan analysis include monitoring credit risk exposure, including the early warning of increased credit risk. The duties and responsibilities of the Risk Management Service include the credit portfolio control activity, which ensures, in cooperation with other organisational units at the Bank, timely identification of clients with potential risk. Such an approach involves a complex management of business relations with customers with the aim to reduce the cost of credit risk as well as improve the quality of the Bank's credit portfolio.

Credit risk control is based on an individual approach to the credit risk assessment specifically tailored to individual clients, including identification of clients with a potential risk, analysis and classification of clients with potential risk, determining the form and manner of managing business relations with clients, and following-up.

Special attention is paid to managing exposures to related parties by reference to the effective organisational normative and operational rules, as well as other aspects of credit risk exposure defined by the Credit Institutions Act and the related by-laws and internal acts governing its implementation.

##### **37.1.1. Credit risk assessment**

#### ***Loans and receivables (including contingent liabilities)***

The Bank assesses the probability of default by individual clients using internal assessment tools created for all groups of customers in line with the internal acts and applicable laws.

Loans and contingent liabilities are classified into the following three key risk groups:

- 1.1. fully recoverable loans (risk group A) – loans assessed as fully recoverable (both principal and interest) and contingent liabilities expected not to result in an outflow of the Bank's resources, or if such an outflow is required, that they will be recovered in full.
- 1.2. partly recoverable loans (risk group B) – loans assessed as not recoverable at contractual amounts (principal and interest) or contingent liabilities expected to result in an outflow of the Bank's resources in excess of the estimated recoverable amount.
- 1.3. irrecoverable loans (risk group C) – loans estimated as fully irrecoverable or insignificantly recoverable and contingent liabilities expected to result in an outflow of the Bank's resources that will never be recovered.

## **37 Risk management policies (continued)**

### **37.1 Credit risk (continued)**

#### **37.1.1. Credit risk assessment (continued)**

##### **Loans and receivables (including contingent liabilities) (continued)**

Managing credit risk of a portfolio of workout or non-performing (bad) loans is the responsibility of a separate unit within the Bank which is in charge of working out such debt (Workout and Non-performing Loan Department), both owed from legal persons and individuals. These activities are primarily aimed at realising positive effects of the implementation of various forms of financial consolidation of clients' business, including various forms of prolongation, renewal or restructuring of loans with the aim of their recovery and maximising the recoverability of loans and receivables as well as improving the loan and guarantee portfolio of the Bank, or fully or partially stabilising as well as cases of full or partial stabilisation of the clients' business by taking consolidation measures, enabling the inclusion of such loans in "performing" ones.

The Risk Management Service estimates future cash flows from non-performing loans on the basis of which provisions for impairment are determined. Such assessment is prepared for all loans managed.

The Bank makes provisions for identified losses on loans and their impairment as follows:

- a) on an individual basis
  - for loans that are not included in the "small loans portfolio"
- b) on a collective basis
  - for loans classified in risk group "A";
  - for loans classified in the "small loans portfolio";
  - for all loans to a single debtor in bankruptcy procedure, if the Bank does not have the status of a creditor with a separate satisfaction right and assesses these loans on an individual basis.

The small loans portfolio comprises the total Bank's exposure to one person or a group of related persons that is not individually significant, i.e. at the date of assessment does not exceed HRK 250,000. Thereby the total exposure amount includes all active balance sheet and off-balance sheet items that are subject to classification in risk groups.

The large loans portfolio, individually significant exposure, comprises the total exposure to one person or a group of related persons whose total exposure at the estimation date exceeds HRK 250,000.

The credit risk assessment on an individual basis is a separate estimation of future cash flows and determining the existence or non-existence of loss for each individual loan and each individual off-balance sheet liability that the Bank is obliged to apply in assessing loans and off-balance sheet liabilities that make an integral part of individually significant exposure.

Credit risk assessment on a collective basis is a collective estimation of future cash flows and determining the existence or non-existence of loss for groups with similar characteristics of credit risk and off-balance sheet liabilities, and is performed in the following cases:

- in assessing the quality of loans and off-balance sheet liabilities for which evidence of the existence of visible losses was not identified, but which might bear latent losses, estimated on the basis of experience on a collective basis (this assessment includes all loans and off-balance sheet liabilities of the risk group A)
- in assessing identified losses for loans included in the small loans portfolio.

Finally, it should be noted that the Bank is currently in the process of upgrading and modifying the internal rating model, which will be introduced in the Bank's operations in the first half of year 2017. This rating model will improve credit risk assessment and estimation, for the purpose of accurate and timely credit risk management in the Bank.

## **37 Risk management policies (continued)**

### **37.1 Credit risk (continued)**

#### **37.1.2. Risk limit control and policies for risk mitigation**

The Bank manages, limits and controls credit risk concentrations wherever such risk is identified – especially with respect to individual clients and groups, industry sectors and countries. Concentrations are determined at the level of exposure to individual debtor (or a group of related parties) against the regulatory capital (over 10 % of the capital) as well as by reference to exposure of a particular activity relative to the overall exposure of the Bank.

The Bank manages credit risk levels by limiting credit risk with respect to a single customer, or a group of customers, and geographic and economic activity segments. Limits set by reference to products, industry sectors and countries are approved by the Bank's management.

The exposure to any debtor is further limited by sub-limitations that cover balance sheet and off-balance sheet exposures, as well as daily limits (the liability settlement risk) compared to items that are not traded. The actual exposure in relation to limitations is monitored on a daily basis. The credit risk exposure is also managed by a regular analysis of the ability of the existing clients and potential clients to settle their liabilities of repaying interest and principal and by changing credit limitations where necessary.

Further specific measures for credit risk control and mitigation are stated below.

#### **(a) Security instruments**

The Bank uses policies of security instruments for receivables that prescribe the main rules aimed at minimising the risk from credit operations.

Security instruments for receivables represent the secondary collection source, while the clients' operations and their ability to generate sufficient cash funds for settling financial liabilities are the primary source of collecting the Bank's receivables. The rules that prescribe the obligation to take security instruments for which the normative acts prescribe the conditions for acceptability, individually for each of the specific security instruments categories are standardised. Also, specific modalities of credit protection aimed at decreasing or mitigating credit risks are determined.

The most significant types of security instruments for loans and receivables are as follows:

- a) Mortgage over property,
- b) Pledge over operating/tangible assets,
- c) Pledge over financial instruments such as debt or equity securities
- d) Insurance policies for loan receivables, life insurance policies with redemption values and other instruments whose quality based on evidence may be equalised with the quality of other above-mentioned instruments.

Non-current financial assets, loans to companies and natural persons are generally secured by appropriate security instruments.

In addition, in order to reduce credit loss, the Bank requires additional collaterals from the contractual parties as soon as indicators of impairment for individual relevant loans and advances are determined. The collateral held as security for all financial assets other than loans and advances is determined on the basis of the nature of the instrument. Debt securities, treasury and other bills are generally not secured, with the exception of securities with coverage in assets and similar instruments secured by financial instruments portfolios.

#### **(b) Commitments to extend credit**

Loan commitments are unused granted loan amounts in the form of loans, guarantees or letters of credit. With respect to credit risk from loan commitments, the Bank is potentially exposed to loss in the amount equal to the total unused commitments.

### **37 Risk management policies (continued)**

#### **37.1 Credit risk (continued)**

##### **37.1.2. Risk limit control and policies for risk mitigation (continued)**

However, the potential loss amount is lower than the total amount of unused commitments, since the majority of commitments depends on maintaining specific credit standards by the clients. The Bank monitors the remaining period to loan maturities as non-current liabilities generally have a higher degree of credit risk compared to current liabilities.

##### **37.1.3. Impairment and provisioning policies**

The amount of provisions for impairment in the portfolio of clients monitored on an individual basis is determined using the dynamic approach, on the basis of the calculation of the loan's recoverable value, calculated as the net present value of estimated future cash flows discounted at the effective interest rate of the loan at the moment when it was assessed as "non-performing" (for loans granted at fixed rates it is the original effective rate calculated at the moment of granting). The regulations of the Croatian National Bank on minimum rates of special provisions in special cases are also taken into account.

Instruments of credit protection for which the nominal value is discounted are as follows:

- pledge over housing property
- pledge over other property and movables for which the market exists and which may be sold in acceptable time periods.

Discounting future cash flows to the present value is calculated individually for all long-term loans from the large loans portfolio for which the impairment loss was identified and it is estimated that their future cash flow from operating activities and cash flow from security instruments will not be sufficient.

Based on the repayment on time criteria, loans in the large loans portfolio are classified into the following risk groups:

1) risk group "A" includes loans that meet the following criteria:

- the debtor's current financial situation and estimated future cash flows do not rise any doubts with respect to the debtor's further operations and settlement of their current and future liabilities to the Bank and other creditors,
- the debtor settles their liabilities to the Bank in contracted terms, and only exceptionally and occasionally after their maturity,
- the loans are secured by adequate security instruments for receivables.

2) Risk group B1 (loans for which the determined loss does not exceed 30% of the nominal carrying amount of individual loans).

3) Risk group B2 (loans for which the determined loss is from 30% to 70% of the nominal carrying amount of individual loans).

4) Risk group B3 (loans for which the determined loss is over 70% and less than 100% of the nominal carrying amount of individual loans).

5) Risk group C (fully unrecoverable loans are considered to be Bank's receivables arisen on a disputable legal basis and other receivables for which, due to an exceptionally poor asset and financial position of the debtor, and due to the lack of adequate security instruments, no cash flows may be expected for settling the debtor's liabilities to the Bank). The Bank is obliged to classify such loans in the risk group C. Loans classified in the risk group C, 100% impaired, are recorded by the Bank in the balance sheet until all legal procedures are finalised related to the termination of the debtor's liability, in line with the policies and procedures of the credit institution and the law that regulates civil obligations.

Specific provisions for impairment for the remaining portfolio of non-performing small loans (exposures below HRK 250 thousand) are calculated by reference to the regularity of payment.

**37 Risk management policies (continued)**

**37.1 Credit risk (continued)**

**37.1.3. Impairment and provisioning policies (continued)**

Based on the timeliness of repayment, loans in the small loans portfolio are classified into the following risk groups:

- 1) Risk group "A" includes fully recoverable loans. For a loan to remain classified in the risk group "A", the following conditions must be met:
  - the debtor's past due liabilities to the Bank are not older than 90 days
  - the full loan amount is covered by a guarantee deposit.
- 2) Risk group "B" or "C" loans must be provided for on the basis of the number of days of late payment according to specially determined tables
- 3) Risk group "C" includes loans that do not meet the conditions for classification in risk groups "A" and "B", and 100% unrecoverable loans, as follows:
  - unsecured loans (default in payments > 90 days);
  - loans classified in the 100% provision position according to specially determined tables.

**37.1.4. Debt securities**

For the purpose of realising future yield, the Bank usually invests surplus liquid funds in high-quality government debt securities and foreign bonds.

**37.1.5. Past due loans and receivables**

**Past due loans and receivables by type at 31.12.2016**

*in thousands of  
HRK*

Past due	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Up to 30 days	90	4,052	5,097	7,504	10	2,043	18,796
31-60 days	122	11,072	184	-	1	993	12,372
61-90 days	30	317	-	-	1	5	353
Over 90 days	3,416	212,528	18,554	2,630	1,203	89,267	327,598
<b>Total</b>	<b>3,658</b>	<b>227,969</b>	<b>23,835</b>	<b>10,134</b>	<b>1,215</b>	<b>92,308</b>	<b>359,119</b>

**37 Risk management policies (continued)**

**37.1 Credit risk (continued)**

**37.1.5. Past due loans and receivables (continued)**

**Past due loans and receivables by type at 31.12.2015**

*in thousands of HRK*

Past due	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Up to 30 days	219	4,797	4,538	3,013	11	3,204	15,782
31-60 days	50	2,417	317	19	21	697	3,521
61-90 days	39	-	-	58	-	27	124
Over 90 days	1,821	229,534	18,226	3,207	840	92,361	345,989
<b>Total</b>	<b>2,129</b>	<b>236,748</b>	<b>23,081</b>	<b>6,297</b>	<b>872</b>	<b>96,289</b>	<b>365,416</b>

**Unimpaired loans at 31.12.2016**

*in thousands of HRK*

	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Not yet due	161,923	251,970	50,845	40,645	56,022	829,749	1,391,154
Due	93	14,160	5,192	7,001	9	2,839	29,294
<b>Total</b>	<b>162,016</b>	<b>266,130</b>	<b>56,037</b>	<b>47,646</b>	<b>56,031</b>	<b>832,588</b>	<b>1,420,448</b>

**Unimpaired loans at 31.12.2015**

*in thousands of HRK*

	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Not yet due	131,121	465,311	51,955	44,734	51,648	951,532	1,696,301
Due	234	8,963	4,620	2,550	32	2,306	18,705
<b>Total</b>	<b>131,355</b>	<b>474,274</b>	<b>56,575</b>	<b>47,284</b>	<b>51,680</b>	<b>953,838</b>	<b>1,715,006</b>

Unimpaired loans and receivables refer to placements classified in risk groups AA and A9. The placements in the risk group AA are loans and receivables regularly repaid by clients and not impaired by the Bank. The placements in the risk group A9 are loans and receivables with defaults in payments of more than 90 days, but not impaired by the Bank due to quality security instruments, as it is estimated that these receivables will be fully collected, but with delay.

The line item 'Other' comprises the participation in syndicated loans in the amount of HRK 704,802 thousand (2015: HRK 816,578 thousand), as well as lombard loans in the amount of HRK 43,813 thousand (2015: HRK 35,807), margin loans in the amount of HRK 25,935 thousand (2015: HRK 16,578 thousand) and mortgage loans in the amount of HRK 7,255 thousand (2015: HRK 8,488 thousand). The remaining balance consist of individual smaller loans intended for diverse purposes.

**37 Risk management policies (continued)**

**37.1 Credit risk (continued)**

**37.1.6. Impaired loans**

**Impaired loans at 31.12.2016**

*in thousands of HRK*

	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Not yet due	3,325	29,702	6,015	26	658	42,964	82,690
Due	3,564	213,810	18,643	3,133	1,205	88,896	329,251
<b>Total</b>	<b>6,889</b>	<b>243,512</b>	<b>24,658</b>	<b>3,159</b>	<b>1,863</b>	<b>131,860</b>	<b>411,941</b>
<b>Impairment</b>	<b>3,688</b>	<b>146,340</b>	<b>11,688</b>	<b>3,012</b>	<b>809</b>	<b>71,049</b>	<b>236,586</b>

**Impaired loans at 31.12.2015**

*in thousands of HRK*

	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Not yet due	1,522	5,480	10,079	-	-	50,003	67,084
Due	1,895	227,785	18,461	3,747	840	93,982	346,710
<b>Total</b>	<b>3,417</b>	<b>233,265</b>	<b>28,540</b>	<b>3,747</b>	<b>840</b>	<b>143,985</b>	<b>413,794</b>
<b>Impairment</b>	<b>2,348</b>	<b>144,927</b>	<b>9,785</b>	<b>3,020</b>	<b>239</b>	<b>70,134</b>	<b>230,453</b>

Within the line item 'Other', long-term loans for the restructuring of various placements in the amount of HRK 39,001 thousand are the largest individual item, followed by long-term financial restructuring loans in cooperation with the CBRD in the amount of HRK 23,813 thousand (2015: HRK 7,437 thousand), construction loans in the amount of HRK 11,637 thousand (2015: HRK 12,113 thousand) and loans for making payments under guarantees and other sureties in the amount of HRK 7,789 thousand (2015: HRK 9,145 thousand).

**37 Risk management policies (continued)**

**37.1 Credit risk (continued)**

**37.1.7. Placement structure by type of activity**

Placement structure by type of activity at 31.12.2016

*in thousands of HRK*

Activity sector	Total placements and off-balance sheet liabilities	Placements of unimpaired value	Placements of impaired value	Impairment and provisions	% of impairment
Agriculture, hunting, forestry and fishing	151,611	118,021	33,590	20,533	<b>13.54</b>
Manufacturing	238,938	110,068	128,871	61,201	<b>25.61</b>
Construction	715,061	628,381	86,680	66,737	<b>9.33</b>
Wholesale and retail trade, repair of motor vehicles and household items	218,176	124,946	93,231	71,160	<b>32.62</b>
Service activities	312,893	256,153	56,741	28,344	<b>9.06</b>
Financial intermediation	53,268	52,269	999	1,461	<b>2.74</b>
Foreign financial institutions	55,908	55,908	0	559	<b>1.00</b>
CNB	428,930	428,930	0	4,289	<b>1.00</b>
<b>Other activities</b>	<b>93,769</b>	<b>65,408</b>	<b>28,361</b>	<b>5,264</b>	<b>5.61</b>
<b>Activity sectors outside the Croatian National Classification</b>	<b>341,821</b>	<b>318,722</b>	<b>23,099</b>	<b>19,250</b>	<b>5.63</b>
<b>TOTAL</b>	<b>2,610,375</b>	<b>2,158,806</b>	<b>451,572</b>	<b>278,798</b>	<b>10.68</b>

Placement structure by type of activity at 31.12.2015

*in thousands of HRK*

Activity sector	Total placements and off-balance sheet liabilities	Placements of unimpaired value	Placements of impaired value	Impairment and provisions	% of impairment
Agriculture, hunting, forestry and fishing	175,904	138,387	37,517	18,240	<b>10.37</b>
Manufacturing	258,882	136,237	122,645	62,464	<b>24.13</b>
Construction	813,804	722,413	91,391	65,675	<b>8.07</b>
Wholesale and retail trade, repair of motor vehicles and household items	212,349	98,650	113,699	71,873	<b>33.85</b>
Service activities	312,238	265,336	46,901	26,876	<b>8.61</b>
Financial intermediation	252,879	252,864	15	2,543	<b>1.01</b>
Foreign financial institutions	67,986	67,986	-	680	<b>1.00</b>
CNB	250,464	250,464	-	2,505	<b>1.00</b>
<b>Other activities</b>	<b>139,147</b>	<b>115,264</b>	<b>23,844</b>	<b>4,731</b>	<b>3.40</b>
<b>Activity sectors outside the Croatian National Classification</b>	<b>270,159</b>	<b>249,897</b>	<b>20,262</b>	<b>17,441</b>	<b>6.45</b>
<b>TOTAL</b>	<b>2,753,812</b>	<b>2,297,498</b>	<b>456,314</b>	<b>273,028</b>	<b>9.91</b>



### 37 Risk management policies (continued)

#### 37.1 Credit risk (continued)

##### 37.1.8. Past due loans and advances to customers in risk groups B and C for which provisions have been made

*in thousands of HRK*

	Individuals	Corporate customers	Total
<b>31 December 2016</b>			
Total exposure	59,411	352,530	<b>411,941</b>
Provisions	32,230	204,356	<b>236,586</b>
Total net exposure	27,181	148,174	<b>175,355</b>
Fair value of collateral	40,475	200,560	<b>241,035</b>
% of collateral coverage	148.91%	135.35%	<b>137.45%</b>

*in thousands of HRK*

	Individuals	Corporate customers	Total
<b>31 December 2015</b>			
Total exposure	60,751	353,043	<b>413,794</b>
Provisions	27,895	202,558	<b>230,453</b>
Total net exposure	32,856	150,485	<b>183,341</b>
Fair value of collateral	49,029	212,330	<b>261,359</b>
% of collateral coverage	149.22 %	141.10%	<b>142.55%</b>

#### 37.2. Liquidity risk

Liquidity risk is the risk of loss arising from the existing or expected Bank's inability to settle its cash liabilities at maturities. This risk arises due to a mismatch of maturities of assets and liabilities, and is manifested as the risk that it will not be possible to convert some receivable into cash in suitable term and at suitable price, i.e. that it will not be possible to convert any non-cash form of assets into cash in a suitable timetable without loss.

The Financial Markets Sector, the Risk Management Service and the ALCO Committee are responsible for liquidity risk management, while the Bank's Management Board makes decisions, whereby precise roles in the liquidity management process are allocated to the following organisational parts or Bank's functionalities:

Cost rates are calculated by the Financial Markets Sector and the Treasury Department. The report does not include funds received from the Croatian Bank for Reconstruction and Development.

Internal prices of products are approved by the Asset-Liability Committee (hereinafter: the ALCO). Internal prices are calculated on a monthly basis, directly prior to the ALCO Committee meeting. Internal prices are confirmed by the ALCO Committee and they are effective until their following meeting. The Risk Management Service is responsible for controlling the limit, and if some of the limits are exceeded, it must immediately inform the Management Board, the Liquidity Committee and the Asset-Liability Committee.

On the relevant meeting of the Asset-Liability Committee it is decided whether the limit excess is acceptable until a certain date or the Treasury Department has to bring indicators within the prescribed limits in accordance with the strategy determined at the Asset-Liability Committee meeting.

The allowed excess of liquidity indicators and the strategy defining the reasons for allowing the excess are documented by the minutes of the Asset-Liability Committee meeting.

### **37 Risk management policies (continued)**

#### **37.2. Liquidity risk (continued)**

If the limits are not exceeded, but the early warning indicators related to the limits have been reached, the Treasury Department prepares a written explanation for the Management Board and the Liquidity Committee within not more than 3 working days about the reasons why the indicator of early warning has been reached and with the proposal of possible solutions. The Management Board and the Liquidity Committee make the decision on further action.

The Risk Management Service controls limits within the monthly report, and reports the exceeding of limits on the ALCO meetings.

Sources of Bank financing are deposits and equity capital. The Bank continually reassesses liquidity risk by identifying and following changes in financing that are necessary for accomplishing business aims set according to Bank strategy. Moreover, the Bank manages a portfolio of liquid assets as a part of its liquidity risk management strategy.

The Bank adjusts its operations concerning liquidity risk according to legal provisions and internal policies. The Bank manages assets and sources of funds from a viewpoint of financial flows, cash flows and concentration, all with the aim of adjusting cash inflows with Bank outflows.

Managing in that way assumes identification of known, expected and potential cash outflows and the production of different asset and liabilities management strategies in order to secure the Bank needs for cash inflows. According to the stated, the liquidity risk management system comprises the following: evaluation and measurement of liquidity risk exposure, setting limits of liquidity risk exposure and reporting and supervision of limit utilization.

Liquidity risk management is realized by operative management of short-term liquidity and by management of long-term liquidity. Management of short-term liquidity is realized with maintenance of a regular liquidity reserve in HRK and by planning and forecasting daily and weekly cash flows. The Bank produces daily, weekly, monthly and annual liquidity plans and evaluates current and future outflows and inflows based on them.

Indicators related to a possible crisis in the Bank's liquidity and general crisis of the banking system liquidity are monitored by the Risk Management Service and the Treasury Department, they are determined by the Risk Management Service and reported to the Management Board, Liquidity Committee and/or the Asset-Liability Committee.

**37 Risk management policies (continued)**

**37.2 Liquidity risk (continued)**

Future outflows under financial liabilities at 31 December 2016 represent undiscounted cash flows, including future interest payments in the amount of HRK 50,542 thousand on received deposits and borrowings, classified by maturities. Asset items are classified by maturities of the carrying amounts.

	<i>in thousands of HRK</i>					
2016	Up to 1 month	1 to 3 months	3 to 12 months	1 to 3 years	Over 3 years	Total
<b>ASSETS</b>						
Cash	276,808	-	-	-	-	276,808
Receivables from the Croatian National Bank	191,709	-	-	-	-	191,709
Placements with banks	52,903	-	431	-	-	53,334
Financial assets available for sale	54,192	37,141	429,479	37,314	275,647	833,773
Financial assets held to maturity	43,809	1,606	515	4,717	-	50,647
Loans and advances to customers	212,947	55,936	392,713	415,789	513,258	1,590,643
Investment property	33,702	-	-	-	-	33,702
Property and equipment	13,427	-	-	-	-	13,427
Intangible assets	4,926	-	-	-	-	4,926
Foreclosed assets	23,389	-	-	-	-	23,389
Deferred tax assets	1,898	-	-	-	-	1,898
Other assets	35,759	-	-	-	-	35,759
<b>Total assets</b>	<b>945,469</b>	<b>94,683</b>	<b>823,138</b>	<b>457,820</b>	<b>788,905</b>	<b>3,110,015</b>
<b>EQUITY AND LIABILITIES</b>						
Liabilities to banks	15,223	7,182	70,080	-	-	92,485
Demand deposits	471,935	-	-	-	-	471,935
Term deposits	166,185	231,338	1,194,414	477,750	12,687	2,082,374
Borrowings	80,008	4,539	25,281	47,626	146,889	304,343
Other liabilities	9,109	-	-	-	-	9,109
Provisions	10,676	-	-	-	-	10,676
<b>Total liabilities</b>	<b>753,136</b>	<b>243,059</b>	<b>1,289,775</b>	<b>525,376</b>	<b>159,576</b>	<b>2,970,922</b>
<b>EQUITY</b>						
Share capital	-	-	-	-	474,600	474,600
Accumulated losses	-	-	-	-	(290,536)	(290,536)
Revaluation reserve	-	-	-	-	5,571	5,571
<b>Total equity</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>189,635</b>	<b>189,635</b>
<b>Total liabilities and equity</b>	<b>753,136</b>	<b>243,059</b>	<b>1,289,775</b>	<b>525,376</b>	<b>349,211</b>	<b>3,160,557</b>
Net assets/liabilities and equity	192,333	(148,376)	(466,637)	(67,556)	439,694	(50,542)

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**37 Risk management policies (continued)**

**37.2 Liquidity risk (continued)**

Future outflows under financial liabilities at 31 December 2015 reflect undiscounted cash flows, including future interest payments in the amount of HRK 89,597 thousand on received deposits and borrowings classified by maturities. Assets positions are classified by maturities of carrying amounts.

	<i>in thousands of HRK</i>					
2015	Up to 1 month	1 to 3 months	3 to 12 months	1 to 3 years	Over 3 years	Total
<b>ASSETS</b>						
Cash	103,596	-	-	-	-	<b>103,596</b>
Receivables from the Croatian National Bank	226,137	-	-	-	-	<b>226,137</b>
Placements with banks	47,985	-	-	-	-	<b>47,985</b>
Financial assets available for sale	131,392	68,705	323,937	64,846	88,852	<b>677,732</b>
Financial assets held to maturity	9,862	9,012	693	24,298	4,714	<b>48,579</b>
Loans and advances to customers	222,656	52,623	537,849	478,275	601,100	<b>1,892,503</b>
Investment property	-	-	-	-	35,696	<b>35,696</b>
Property and equipment	-	-	-	-	15,595	<b>15,595</b>
Intangible assets	-	-	-	-	4,289	<b>4,289</b>
Foreclosed assets	-	-	-	-	24,539	<b>24,539</b>
Deferred tax assets	-	-	-	-	4,246	<b>4,246</b>
Other assets	27,670	-	-	-	-	<b>27,670</b>
<b>Total assets</b>	<b>769,298</b>	<b>130,340</b>	<b>862,479</b>	<b>567,419</b>	<b>779,031</b>	<b>3,108,567</b>
<b>EQUITY AND LIABILITIES</b>						
Liabilities to banks	50,352	267	59,877	-	-	<b>110,496</b>
Demand deposits	473,276	-	-	-	-	<b>473,276</b>
Term deposits	123,821	160,823	709,863	1,095,727	13,605	<b>2,103,839</b>
Borrowings	134,583	4,838	30,370	63,393	77,357	<b>310,541</b>
Other liabilities	9,769	-	-	-	-	<b>9,769</b>
Provisions	8,186	-	-	-	-	<b>8,186</b>
<b>Total liabilities</b>	<b>799,987</b>	<b>165,928</b>	<b>800,110</b>	<b>1,159,120</b>	<b>90,962</b>	<b>3,016,107</b>
<b>EQUITY</b>						
Share capital	-	-	-	-	474,600	<b>474,600</b>
Accumulated losses	-	-	-	-	(292,174)	<b>(292,174)</b>
Revaluation reserve	-	-	-	-	(395)	<b>(395)</b>
<b>Total equity</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>182,031</b>	<b>182,031</b>
<b>Total liabilities and equity</b>	<b>803,594</b>	<b>165,928</b>	<b>800,110</b>	<b>1,159,120</b>	<b>272,993</b>	<b>3,198,138</b>
Net assets/liabilities and equity	(30,689)	(35,588)	62,369	(591,701)	506,038	(89,571)

## **37 Risk management policies (continued)**

### **37.3. Market risks**

Market risks represent potential effects that external conditions may have on the value of assets, liabilities and off-balance sheet positions of the Bank, and are caused by changes in prices and movements in financial markets.

All instruments for trading are subject to market risk, the risk that future changes in market conditions can make an instrument unfavourable or lead to value reduction.

The Bank manages financial instruments available for sale according to changes in market conditions. Exposure to market risk is formally managed by buying or selling instruments according to limits set by Management.

Market risk is the risk of loss on balance sheet and off-balance sheet positions arising from unfavourable movements in prices on some of the 4 fundamental markets: debt securities, foreign currencies, commodity and equity securities markets.

Market risks are as follows:

- Interest rate risk
- Currency risk
- Price risk – risk of a change in prices of equity and debt securities.

Interest rate risk is defined by the impact of changes in market interest rates on the Bank's financial results. The Bank's daily activities depend on the interest rate risk impacted by the terms of collection of assets and liabilities in relation to interest income and expenses or the terms in which interest rates change. These terms are controlled by the ALCO by defining the interest rate limits and coordinating activities that the bank has to take.

Interest rate risk is described in more detail in chapter 37.5. of the Report.

The Bank's activities are exposed to the risk of changes in the value of main currencies, which impacts the Bank's financial result and cash flow. The Bank controls foreign currency assets and foreign currency liabilities with the aim to avoid an inadequate currency risk.

The Management Board defined internal limits of open foreign currency position that are below the legally prescribed limits determined in line with the CNB Regulation.

Currency risk is described in more detail in the following chapter of the Report (item 37.4).

Market risk managements is performed in the Financial Markets Sector, Risk Management Service and the ALCO, and the Bank's Management Board is informed and makes decisions.

### **37 Risk management policies (continued)**

#### **37.3.1. Currency risk**

Currency risk is the risk of loss that results from currency changes.

Exposure to currency risk materializes from holding assets and liabilities and/or off-balance sheet items denominated and/or indexed in foreign currency, or when they are structurally unadjusted in cases of unfavourable movement of HRK towards international currencies as well as unfavourable mutual movements of currencies.

Currency risk management process includes: identifying the Bank's exposure to currency risk, measuring currency risk exposure, defining boundaries and limits of currency risk exposure, instruments and processes for risk optimisation, currency risk management process supervision, reporting on the currency risk exposure.

At the end of each working day, the Bank adjusts its total open FX position so that the total open FX position (increased by the position in gold) does not exceed the amount of regulatory capital determined in line with the regulations of the Croatian National Bank.

The Bank uses the Value at Risk methodology (VaR) to evaluate exposure to market risk and expected maximum loss for the position in trading and other activities. VaR represents a statistically based evaluation of potential losses on the existing portfolio due to unfavourable market movements.

The Value at Risk method measures the maximum expected loss for the Bank in case of most unfavourable foreign currency movements in an observed time interval with normal market conditions and a given level of significance based on historical data. The Bank directs its business activities primarily trying to minimize the mismatch between assets' and liabilities' items denominated in foreign currency or carrying an FX clause. The Bank seeks to manage its assets and liabilities by matching the currencies of the individual asset and liability items to optimise the relationship between risk and profitability in unfavourable inter-currency movements.

The potential maximum daily loss of open foreign currency position (VaR: reliability 95%) as of 31.12.2016. was HRK 39 thousand (2015 : HRK 44 thousand).

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**37 Risk management policies (continued)**

**37.3.1 Currency risk (continued)**

FX assets and liabilities of the Bank as at 31 December 2016 are shown as follows:

2016							<i>in thousands of HRK</i>	
	EUR	USD	Other	HRK, currency clause	Total FX equivalents	HRK	Total	
<b>ASSETS</b>								
Cash	184,262	2,264	19,044	-	205,570	71,238	<b>276,808</b>	
Receivables from the Croatian National Bank	-	-	-	-	-	191,709	<b>191,709</b>	
Placements with banks	422	43,306	9,606	-	53,334	-	<b>53,334</b>	
Financial assets available for sale	413,747	-	-	221,560	635,307	198,466	<b>833,773</b>	
Financial assets held to maturity	-	-	-	-	-	50,647	<b>50,647</b>	
Loans and advances to customers	611,719	-	732	379,178	991,629	599,014	<b>1,590,643</b>	
Investment property	-	-	-	-	-	33,702	<b>33,702</b>	
Property and equipment	-	-	-	-	-	13,427	<b>13,427</b>	
Intangible assets	-	-	-	-	-	4,926	<b>4,926</b>	
Foreclosed assets	-	-	-	-	-	23,389	<b>23,389</b>	
Deferred tax assets	-	-	-	-	-	1,898	<b>1,898</b>	
Other assets	390	-	12	-	403	35,356	<b>35,759</b>	
<b>Total assets</b>	<b>1,210,540</b>	<b>45,570</b>	<b>29,394</b>	<b>600,738</b>	<b>1,886,243</b>	<b>1,223,772</b>	<b>3,110,015</b>	
<b>EQUITY AND LIABILITIES</b>								
Liabilities to banks	1,806	98	-	-	1,904	90,191	<b>92,095</b>	
Demand deposits	109,774	7,620	8,505	-	125,899	346,036	<b>471,935</b>	
Term deposits	1,577,029	40,367	20,825	18,065	1,656,286	388,276	<b>2,044,562</b>	
Borrowings	-	-	-	114,926	114,926	177,077	<b>292,003</b>	
Other liabilities	149	-	908	-	1,057	8,052	<b>9,109</b>	
Provisions	-	-	-	-	-	10,676	<b>10,676</b>	
<b>Total liabilities</b>	<b>1,688,758</b>	<b>48,085</b>	<b>30,238</b>	<b>132,991</b>	<b>1,900,072</b>	<b>1,020,308</b>	<b>2,920,380</b>	
<b>EQUITY</b>								
Share capital	-	-	-	-	-	474,600	<b>474,600</b>	
Accumulated losses	-	-	-	-	-	(290,536)	<b>(290,536)</b>	
Revaluation reserve	-	-	-	-	-	5,571	<b>5,571</b>	
<b>Total equity</b>	-	-	-	-	-	189,635	<b>189,635</b>	
<b>Total liabilities and equity</b>	<b>1,688,758</b>	<b>48,085</b>	<b>30,238</b>	<b>132,991</b>	<b>1,900,072</b>	<b>1,209,943</b>	<b>3,110,015</b>	
Net assets/liabilities and equity	(478,218)	(2,515)	(844)	467,747	(13,829)	13,829	-	

**37 Risk management policies (continued)**

**37.3.1 Currency risk (continued)**

FX assets and liabilities of the Bank as at 31 December 2015 are shown as follows:

2015							<i>in thousands of HRK</i>	
	EUR	USD	Other	HRK, currency clause	Total FX equivalents	HRK	Total	
<b>ASSETS</b>								
Cash	34,777	6,079	23,210	-	64,066	39,530	<b>103,596</b>	
Receivables from the Croatian National Bank	32,177	-	-	-	32,177	193,960	<b>226,137</b>	
Placements with banks	426	39,455	8,104	-	47,985	-	<b>47,985</b>	
Financial assets available for sale	333,550	-	-	73,164	406,714	271,018	<b>677,732</b>	
Financial assets held to maturity	24,957	-	-	-	24,957	23,622	<b>48,579</b>	
Loans and advances to customers	713,092	-	970	549,516	1,263,578	628,925	<b>1,892,503</b>	
Investment property	-	-	-	-	-	35,696	<b>35,696</b>	
Property and equipment	-	-	-	-	-	15,595	<b>15,595</b>	
Intangible assets	-	-	-	-	-	4,289	<b>4,289</b>	
Foreclosed assets	-	-	-	-	-	24,539	<b>24,539</b>	
Deferred tax assets	-	-	-	-	-	4,246	<b>4,246</b>	
Other assets	871	-	1	-	872	26,798	<b>27,670</b>	
<b>Total assets</b>	<b>1,139,850</b>	<b>45,534</b>	<b>32,285</b>	<b>622,680</b>	<b>1,840,349</b>	<b>1,268,218</b>	<b>3,108,567</b>	
<b>EQUITY AND LIABILITIES</b>								
Liabilities to banks	17,541	97	8	-	17,646	92,257	<b>109,903</b>	
Demand deposits	118,049	5,794	8,574	-	132,417	340,859	<b>473,276</b>	
Term deposits	1,476,435	49,002	23,076	19,401	1,567,914	464,762	<b>2,032,676</b>	
Borrowings	-	-	-	144,068	144,068	148,658	<b>292,726</b>	
Other liabilities	134	-	1	-	135	9,634	<b>9,769</b>	
Provisions	-	-	-	-	-	8,186	<b>8,186</b>	
<b>Total liabilities</b>	<b>1,612,159</b>	<b>54,893</b>	<b>31,659</b>	<b>163,469</b>	<b>1,862,180</b>	<b>1,064,356</b>	<b>2,926,536</b>	
<b>EQUITY</b>								
Share capital	-	-	-	-	-	474,600	<b>474,600</b>	
Accumulated losses	-	-	-	-	-	(292,174)	<b>(292,174)</b>	
Revaluation reserve	-	-	-	-	-	(395)	<b>(395)</b>	
<b>Total equity</b>	-	-	-	-	-	182,031	<b>182,031</b>	
<b>Total liabilities and equity</b>	<b>1,612,159</b>	<b>54,893</b>	<b>31,659</b>	<b>163,469</b>	<b>1,862,180</b>	<b>1,246,387</b>	<b>3,108,567</b>	
Net assets/liabilities and equity	(472,309)	(9,359)	626	459,211	(21,831)	21,831	-	



### **37 Risk management policies (continued)**

#### **37.3.2. Interest rate risk**

Interest rate risk in the Bank's trading book is the risk of loss arising from possible changes in interest rates, which impact the items in the Bank's book. This risk arises due to a mismatch of assets and liabilities with respect to their type, base and amount of interest rates.

Repricing risk is the risk of a decrease in net interest income due to changes in interest rates and a decrease in economic value of capital due to changes in interest rates.

Interest rate risk is a result of: temporary mismatch in revaluation of assets, liabilities and off-balance sheet items; early repayment of loans, deposit withdrawal (term and without term) or the difference in the movements of active and passive interest rates (basic (primary) risk).

The Bank's operations are exposed to the risk of changes in interest rates to the extent that interest-bearing assets and liabilities mature or their interest rates change in different periods or in different amounts. Risk management activities are directed to optimizing net interest income according to the Bank's business strategy, at the given market rates.

Activities of managing "asset-liability" risks are performed in the context of the Bank's sensitivity to interest rate changes. Exposure to risk of interest rate changes is a consequence of assets' and liabilities' items mismatch considering the possibility of interest rate changes, and it is supervised by applying an analysis of assets' and liabilities' mismatch. The aim of interest rate risk management is to secure an optimal and stable net interest margin, and thus net profit. Interest rate risk is minimized by accepting deposits and approving loans as well as with investments carrying fixed interest rates.

The main elements of the interest rate risk management are as follows:

- interest rate sensitivity analysis
- establishing internal limits and thresholds (limit of a decrease in economic value or maturity periods)
- control of performing/fulfilling/meeting the set limits;
- testing the resistance to stress for interest rate risk and the analysis of the results obtained;
- introducing hedging operations if required.

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**37 Risk management policies (continued)**

**37.3.2. Interest rate risk (continued)**

The table below shows the carrying amounts of the Bank's assets and liabilities at 31 December 2016, classified into categories by the earlier of contractual repricing and maturity.

2016	Up to 1 month	1 to 3 months	3 to 12 months	1 to 3 years	Over 3 years	Non-interest bearing	<i>in thousands of HRK</i>
							Total
<b>ASSETS</b>							
Cash	-	-	-	-	-	276,808	<b>276,808</b>
Receivables from the Croatian National Bank	-	-	-	-	-	191,709	<b>191,709</b>
Placements with banks	53,314	-	-	-	-	20	<b>53,334</b>
Financial assets available for sale	50,000	35,060	428,531	37,314	278,526	4,342	<b>833,773</b>
Financial assets held to maturity	43,000	1,650	500	4,775	0	722	<b>50,647</b>
Loans and advances to customers	169,710	142,568	766,586	316,869	75,178	119,732	<b>1,590,643</b>
Investment property	-	-	-	-	-	33,702	<b>33,702</b>
Property and equipment	-	-	-	-	-	13,427	<b>13,427</b>
Intangible assets	-	-	-	-	-	4,926	<b>4,926</b>
Foreclosed assets	-	-	-	-	-	23,389	<b>23,389</b>
Deferred tax assets	-	-	-	-	-	1,898	<b>1,898</b>
Other assets	-	-	-	-	-	35,759	<b>35,759</b>
<b>Total assets</b>	<b>316,024</b>	<b>179,278</b>	<b>1,195,617</b>	<b>358,958</b>	<b>353,704</b>	<b>706,434</b>	<b>3,110,015</b>
<b>EQUITY AND LIABILITIES</b>							
Liabilities to banks	11,275	7,000	73,402	-	-	418	<b>92,095</b>
Demand deposits	238	-	456,236	-	-	15,461	<b>471,935</b>
Term deposits	159,061	220,053	1,148,531	454,527	11,309	51,081	<b>2,044,562</b>
Borrowings	73,901	4,062	24,664	42,707	141,075	5,594	<b>292,003</b>
Other liabilities	-	-	-	-	-	9,109	<b>9,109</b>
Provisions	-	-	-	-	-	10,676	<b>10,676</b>
<b>Total liabilities</b>	<b>244,475</b>	<b>231,115</b>	<b>1,702,833</b>	<b>497,234</b>	<b>152,384</b>	<b>92,339</b>	<b>2,920,380</b>
<b>EQUITY</b>							
Share capital	-	-	-	-	-	474,600	<b>474,600</b>
Accumulated losses	-	-	-	-	-	(290,536)	<b>(290,536)</b>
Revaluation reserve	-	-	-	-	-	5,571	<b>5,571</b>
<b>Total equity</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>189,635</b>	<b>189,635</b>
<b>Total liabilities and equity</b>	<b>244,475</b>	<b>231,115</b>	<b>1,702,833</b>	<b>497,234</b>	<b>152,384</b>	<b>281,974</b>	<b>3,110,015</b>
<b>Net assets/liabilities and equity</b>	<b>71,549</b>	<b>(51,837)</b>	<b>(507,216)</b>	<b>(138,276)</b>	<b>201,320</b>	<b>424,460</b>	<b>-</b>

**37 Risk management policies (continued)**

**37.3.2 Interest rate risk (continued)**

The table below shows the carrying amounts of the Bank's assets and liabilities at 31 December 2015, classified into categories by the earlier of contractual repricing and maturity.

2015	Up to 1 month	1 to 3 months	3 to 12 months	1 to 3 years	Over 3 years	Non-interest bearing	in thousands of HRK
							Total
<b>ASSETS</b>							
Cash	-	-	-	-	-	103,596	<b>103,596</b>
Receivables from the Croatian National Bank	-	-	-	-	-	226,137	<b>226,137</b>
Placements with banks	47,985	-	-	-	-	-	<b>47,985</b>
Financial assets available for sale	130,000	68,164	322,705	64,846	90,355	1,662	<b>677,732</b>
Financial assets held to maturity	10,000	9,200	-	24,403	4,775	201	<b>48,579</b>
Loans and advances to customers	146,790	158,797	1,115,722	271,454	63,597	136,143	<b>1,892,503</b>
Investment property	-	-	-	-	-	35,696	<b>35,696</b>
Property and equipment	-	-	-	-	-	15,595	<b>15,595</b>
Intangible assets	-	-	-	-	-	4,289	<b>4,289</b>
Foreclosed assets	-	-	-	-	-	24,539	<b>24,539</b>
Deferred tax assets	-	-	-	-	-	4,246	<b>4,246</b>
Other assets	-	-	-	-	-	27,670	<b>27,670</b>
<b>Total assets</b>	<b>334,775</b>	<b>236,161</b>	<b>1,438,427</b>	<b>360,703</b>	<b>158,727</b>	<b>579,774</b>	<b>3,108,567</b>
<b>EQUITY AND LIABILITIES</b>							
Liabilities to banks	38,972	-	70,561	-	-	370	<b>109,903</b>
Demand deposits	293	-	472,983	-	-	-	<b>473,276</b>
Term deposits	127,120	200,733	626,741	1,040,520	9,634	27,928	<b>2,032,676</b>
Borrowings	133,584	4,133	28,909	56,832	68,977	291	<b>292,726</b>
Other liabilities	-	-	-	-	-	9,769	<b>9,769</b>
Provisions	-	-	-	-	-	8,186	<b>8,186</b>
<b>Total liabilities</b>	<b>299,969</b>	<b>204,866</b>	<b>1,199,194</b>	<b>1,097,352</b>	<b>78,611</b>	<b>46,544</b>	<b>2,926,536</b>
<b>EQUITY</b>							
Share capital	-	-	-	-	-	474,600	<b>474,600</b>
Accumulated losses	-	-	-	-	-	(292,174)	<b>(292,174)</b>
Revaluation reserve	-	-	-	-	-	(395)	<b>(395)</b>
<b>Total equity</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>182,031</b>	<b>182,031</b>
<b>Total liabilities and equity</b>	<b>299,969</b>	<b>204,866</b>	<b>1,199,194</b>	<b>1,097,352</b>	<b>78,611</b>	<b>228,575</b>	<b>3,108,567</b>
<b>Net assets/liabilities and equity</b>	<b>34,806</b>	<b>31,295</b>	<b>239,233</b>	<b>(736,649)</b>	<b>80,116</b>	<b>351,199</b>	<b>-</b>

### 37 Risk management policies (continued)

#### 37.3.2. Interest rate risk (continued)

The table below shows effective interest rates for interest-bearing assets and liabilities.

	2016 (in %)	2015 (in %)
<b>Assets</b>		
Cash	0.00-0.00	0.00-0.15
Placements with banks	0.00-4.50	0.01-3.00
Financial assets available for sale	0.17-6.50	0.20-5.88
Loans and advances to customers	3.00-10.50	3.69-10.90
<b>Equity and liabilities</b>		
Liabilities to banks	0.90-1.90	0.00-1.20
Demand deposits	0.01-2.50	0.01-2.50
Term deposits	0.07-3.15	0.00-3.80
Borrowings	0.30-5.00	0.25-3.60

#### 37.4. Price risk

Price risk is the risk that the value of the financial instrument will fluctuate as a result of changes in market prices, whether caused by factors specific to an individual investment, its issuer or all factors affecting all instruments traded in the market. The risk is managed by setting maximum volumes, limits and other restrictions. The Bank manages the risk by setting Trading Book limits (generally not applied, and the Bank had no positions in the Trading Book at 31 December 2016 and 2015), with the available-for-sale and held-to-maturity portfolio durations being measured, monitored and reported regularly.

#### 37.5. Market risk measurement techniques

Measurement techniques used for measuring and controlling market risks are the Value at Risk (VaR) method and stress tests.

##### **VaR method**

The VaR method measures the Bank's maximum loss (the maximum expected loss) in case of unfavourable movements in FX exchange rates in a set time interval under normal market conditions and the set level of reliability on the basis of historical data.

##### **Currency exposure limits**

The Bank is obliged to adjust its operations so that at any time the following structural principles are followed:

- the Bank internally determines that the Bank's total open FX position does not exceed 25% of the Bank's regulatory capital,
- the maximum allowed open FX position in EUR amounts to 20% of the regulatory capital,
- the maximum allowed open FX position in USD amounts to 10% of the regulatory capital,
- the maximum allowed open FX position by individual currencies other than EUR and USD amounts to 5% of the regulatory capital.

### 37 Risk management policies (continued)

#### 37.5 Market risk measurement techniques (continued)

	Internal limit	At 31.12.2016
Bank's total open FX position	25.00%	1.30%
Maximum open FX position in EUR	20.00%	0.63%
Maximum open FX position in USD	10.00%	0.04%
Maximum open FX position in other currencies	5.00%	0.20% for CHF

#### Daily VAR calculation

In accordance with the provisions of Basel II agreement on market risk measurement, the Bank has opted for the VaR method for calculating its FX position exposure to changes in foreign currency exchange rates (the impact of unfavourable movements in rates on the amount of open FX position).

For calculating VAR, the Bank develops the application of the Variance-Covariance Model, which implies the assessment of the present open risk on the basis of movements in exchange rates.

The Risk Management Service reports on the Bank's FX position under Value-at-Risk methodology on a daily basis, and to the ALCO at their meetings.

#### Stress tests

Stress test is a risk management technique used for assessing potential impacts of specific events and/or changes in several risk factors on the Bank's financial position.

The purpose of the stress test is to determine whether the Bank has an appropriate level of capital in case of the specific events and/or changes in several risk factors. These are unfavourable events that are difficult to foresee (extreme, but possible) and that impact the Bank's capital, risk profile and profit. The stress test may be divided into the scenario analysis and sensitivity analysis.

The scenario analysis is a stress test that analyses the impact of simultaneous changes of several risk factors on the Bank's financial position in clearly defined stress scenarios. The sensitivity analysis is a type of stress test that analyses the impact of a particular risk factor on the Bank's financial position without the stress cause being identified. The stress test is performed semi-annually.

In performing liquidity stress tests, the Bank assumes a liquidity shock on the market, such as deposit withdrawal or inability to place on the market the instruments the Bank possesses without incurring significant loss. In doing so, potential outflows are estimated under scenario and sensitivity analyses. In defining a scenario, the Bank considers the circumstances that may arise upon the expiry of a significant volume of deposits or losing a part of its unsecured sources of funding, including deposits from major customers etc. The baseline scenario used for the purpose of the analysis, with individual factors having two levels of disturbance intensity, are defined as follows:

- 1) Internal crisis of the Bank,
- 2) Market crisis
- 3) A combination of both.

VaR is not used in performing liquidity stress tests, as in extreme circumstances the losses exceed the expected losses in a much larger number of instances than envisaged using VaR.

### 37 Risk management policies (continued)

#### 37.5 Market risk measurement techniques (continued)

##### Interest rate risk in the banking book

Interest rate risk in the banking book is the risk of loss arising from possible changes in interest rates that affect items in the Bank's banking book. For the purposes of the stress tests, the Bank uses simplified calculation of the changes in the economic value of the banking book, as defined in the Decision on the interest rate risk in the banking book. A change of 200 and 300 basis points is assumed, exceptionally 500 basis points.

In order to determine the weights over time horizons for a 300-bp change, the following weights are applied:

Time horizon	Time zones centers	Estimated modified duration	Weight (200bp)	Weight (300bp)	Weight (500bp)
Up to 1 month	0.50	0.04	0.08%	0.12%	0.20%
1 to 3 months	2.00	0.16	0.32%	0.48%	0.80%
3 to 6 months	4.50	0.36	0.72%	1.08%	1.80%
6 to 12 months	9.00	0.71	1.43%	2.13%	3.55%
1 to 2 years	1.50	1.38	2.77%	4.14%	6.90%
2 to 3 years	2.50	2.25	4.49%	6.75%	11.25%
3 to 4 years	3.50	3.07	6.14%	9.21%	15.35%
4 to 5 years	4.50	3.85	7.71%	11.55%	19.25%
5 to 7 years	6.00	5.08	10.15%	15.24%	25.40%
7 to 10 years	8.50	6.63	13.26%	19.89%	33.15%
10 to 15 years	12.50	8.92	17.84%	26.76%	44.60%
15 to 20 years	17.50	11.21	22.43%	33.63%	56.05%
Over 20 years	22.50	13.01	26.03%	39.03%	65.05%

The Bank performs the shock-test to determine the impact of a one-off increase or decrease of interest rates by 100 and 20 basis points over a one-year horizon.

The Bank has to align its operations so that the following structural principles are complied with at any time:

The economic value to regulatory capital, pursuant to the methodology of the CNB (200 bp) may never exceed the legally set rate of 20 percent of the Bank's regulatory capital.

*in thousands of HRK*

	Internal limit	Internal early warning system	At 31 December 2016
Economic value change / own funds	15%	13%	11.61%

#### 37.6. Operational risk

The Bank is exposed to operational risk in all its business activities. The aim of operational risk management is identification of all observable forms of operational risk, its control and minimization of exposure.

The Bank is trying to accomplish optimal management of operational risk according to the principles defined by the regulator and Bank policies, and with the purpose of diminishing and mitigating operational risk. In relation to this the Bank collects data on operational risk events, follows key risk indicators, conducts scenario analysis,

### 37 Risk management policies (continued)

#### 37.6. Operational risk (continued)

evaluates operational risk in its operations, reports to Management on operational risk exposure and proposes measures for diminishing, mitigating and transferring operational risk. Operational risk does not have material effect on Bank's operations.

### 38 Fair value of financial assets and liabilities

The fair value of a financial instruments is the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, the so-called exit price. Financial assets available for sale are measured at fair value, except for treasury bills, which are carried at the balance sheet date at discounted values.

Table below summarises the year-end fair value estimates made by the Management Board.

	Carrying amount		Fair value	
	2016	2015	2016	2015
<b>Financial assets</b>				
Loans to and receivables from banks	53,334	47,985	53,334	47,985
Loans and receivables from customers	1,590,643	1,892,503	1,564,350	1,870,084
<b>Financial liabilities</b>				
Deposits from banks	92,095	109,903	92,095	109,903
Deposits from customers	2,516,497	2,505,952	2,485,858	2,437,062
Borrowings	292,003	292,726	292,003	292,726

Loans and receivables from customers and deposits from customers represent aggregate balances received from/owed to corporate and retail customers that bear interest at different average variable rates, and their effects are presented separately in the following tables.

#### Corporate customers

	Carrying amount		Fair value	
	2016	2015	2016	2015
<b>Financial assets</b>				
Loans and receivables from customers	1,212,482	1,555,058	1,205,413	1,547,112
<b>Financial liabilities</b>				
Deposits from customers	569,506	668,256	568,034	661,334

#### Individuals

	Carrying amount		Fair value	
	2016	2015	2016	2015
<b>Financial assets</b>				
Loans and receivables from customers	378,161	337,445	358,937	322,972
<b>Financial liabilities</b>				
Deposits from customers	1,946,991	1,837,696	1,917,824	1,775,728

### **38 Fair value of financial assets and liabilities (continued)**

Set out below is an overview of key methods and assumptions used in estimating the fair values of financial instruments.

#### ***Loans to and receivables from banks***

Loans and receivables are reported net of provision for impairment. The estimated fair value of loans and receivables represents future cash flows, discounted using the current market rates to arrive at the fair value of those assets.

#### ***Loans and receivables from customers***

Loans and receivables are reported net of provision for impairment. The estimated fair value of loans and receivables represents discounted expected future cash flows. Future cash flows are discounted using current market rates to arrive at their fair value. Future expected losses are not considered, and no adjustment is performed to reflect any amounts doubtful of collection (including timing uncertainty) for exposures under due and reprogrammed amounts as well as under exposures not yet due but required to be monitored more closely.

#### ***Deposits from banks***

Fair value estimates of fixed-maturity deposits are based on expected cash flows discounted using current market rates on deposits with similar remaining maturities, but they may not be lower than the nominal amount of deposits that may be called by customers at any time.

Considering their short maturity, Management considers that their carrying amounts do not differ from their fair values.

#### ***Deposits from customers***

The fair value estimate of fixed-maturity deposits is based on cash flows discounted at currently valid market rates on deposits with similar remaining maturities, however, the fair value cannot be lower than the nominal amount for those deposits that may be called by customers at any time. The value of client relationships is not taken into account in assessing the fair value.



### 39 Capital management

The main goal in managing the Bank's capital is to ensure the compliance with all regulatory capital requirements and maintain the credit rating and total capital adequacy to improve the operations.

The Bank manages its capital structure and adjusts it in accordance with changes in economic conditions and characteristics of its business risks.

In managing capital, the Bank also follows the principles of:

- Compliance with all legally prescribed capital requirements
- Maintaining the Bank's ability to continue operations and achieve the Bank's goals
- Maintaining the strong capital base that will enable a continued and sustainable development with the aim to achieve positive results in the income statement.

The Bank's regulatory capital and the total capital rate, calculated in accordance with the requirements of the Regulation (EU) no 575/2013 only for the Bank, were as follows:

	2016	2015
	<i>in thousands of HRK</i>	
<b>Own funds</b>		
<b><i>Tier 1 capital</i></b>		
Issued share capital	474,600	474,600
Share premium	-	-
Accumulated losses (excluding the profit for the current year)	(292,174)	(277,040)
Loss for the year, net of dividends proposed	-	(15,134)
Legal, statutory and other reserves	-	-
Deductions pursuant to Regulation (EU) no. 575/2013 /i/	(8,772)	(7,459)
Total Tier 1 capital	173,654	174,967
<b><i>Additional capital</i></b>	-	-
Total additional capital	-	-
Deductions in respect of investments in banks and financial institutions	-	-
<b>Total own funds</b>	<b>173,654</b>	<b>174,967</b>

/i/ The amount includes deferred tax assets, intangible assets, unrealised losses on financial assets available for sale (not offset with gains) and 0.1% on the entire portfolio of financial assets available for sale.

As at 31 December 2016, the Bank's regulatory capital (own funds) amounts to HRK 173,654 thousand (2015: HRK 174,967 thousand).

**39 Capital management (continued)**

	<i>in thousands of HRK</i>	
	2016	2015
<b>Capital adequacy according to the Regulation EU No. 575/2013</b>		
<i>Capital requirements</i>		
Credit risk exposure	69,243	75,324
<i>Balance sheet items</i>	68,085	73,537
<i>Off-balance sheet items</i>	1,158	1,787
Currency risk exposure	-	-
Operating risk exposure	13,408	12,639
<b>Total capital requirement</b>	<b>82,651</b>	<b>87,963</b>
<i>Additional capital requirements</i>		
Additional capital adequacy rate requirement	29,548	31,447
Capital conservation buffer	25,828	27,489
Systemic risk buffer	15,497	16,493
<b>Total capital requirement</b>	<b>153,524</b>	<b>163,392</b>
<b>Common Equity Tier 1 capital ratio</b>	<b>16.81%</b>	<b>15.91%</b>
<b>Tier 1 capital ratio</b>	<b>16.81%</b>	<b>15.91%</b>
<b>Total capital ratio</b>	<b>16.81%</b>	<b>15.91%</b>

The comparative information presents the capital adequacy in accordance with the requirements of the Regulation (EU) no. 575/2013. As at 31 December 2016, the total capital ratio is 16.81% (2015.: 15.91%).

At 31 December 2016 the Bank complied with all capital requirements, as well as at 31 December 2015.

*Legal reserve*

The Companies Act requires that 5% of profit for the year is added to this reserve until 5% of issued share capital is reached. The legal reserve, amounting to 5% of the issued share capital, may be used to cover the current and prior year losses.

*Fair value reserve*

The fair value reserve includes unrealized gains and losses from changes in fair value of financial assets available for sale as well as foreign exchange differences resulting from non-monetary financial assets available for sale.

*Accumulated losses*

Accumulated losses include losses accumulated from previous years.

#### **40 Accounting estimates and judgements in the application of the accounting policies**

The Bank produces estimates and assumptions on uncertain events, including estimates and assumptions on the future. Such accounting assumptions and estimates are regularly reviewed, and they are based on historical experience and other factors, like the expected flow of future events that may be reasonably assumed in existing circumstances but, despite of this, inevitably represent the sources of estimate uncertainty. Evaluation of losses from impairment of a portfolio exposed to credit risk and evaluation of fair value of collateral in the form of real estate as an integral part of the evaluation, represents the most significant source of estimation uncertainty. This and other key sources of estimation uncertainty, that carry considerable risk of possible significant adjustments of assets' and liabilities' carrying value in the next business year, are described below.

##### a) Losses from impairment of loans and receivables

Chapter 3 'Basis of preparation of the financial statements' details the estimates and judgments made regarding loans and receivables.

Chapter 4 'Accounting policies' provides detailed explanations of the estimates and judgements applied to financial assets at amortised cost.

##### b) Deferred tax

The Bank recognises deferred tax asset in line with management estimate. The management estimate is based on the Long-term business plan aimed at future profitable operations.

##### c) Regulatory requirements

The CNB and the Croatian Financial Services Supervisory Agency are authorized to exercise regulatory supervision over the Bank's operations and may impose the requirement to revise the assets' and liabilities' carrying amounts, in accordance with relevant regulations.

CROATIA BANKA d.d.  
 NOTES TO THE FINANCIAL STATEMENTS  
 For the year 2016 (continued)

**41 Concentrations of assets, liabilities and off-balance sheet items**

Concentrations of assets, liabilities and off-balance sheet items are shown as follows:

*in thousands of HRK*

	31 December 2016			31 December 2015		
	Assets	Liabilities	Off-balance sheet items	Assets	Liabilities	Off-balance sheet items
<b>Geographic region</b>						
Republic of Croatia	3,054,220	2,952,674	153,236	3,033,157	2,958,141	163,515
Europe	16,847	68,251		64,804	78,686	1
Other	38,948	89,090	2	10,606	71,740	-
<b>Total by geographical region</b>	<b>3,110,015</b>	<b>3,110,015</b>	<b>153,238</b>	<b>3,108,567</b>	<b>3,108,567</b>	<b>163,516</b>
<b>Sector</b>						
Republic of Croatia (state)	879,076	250,144	1,515	738,394	198,815	15,926
Croatian National Bank	235,209	161,295	-	250,474	130,555	-
Trade and commerce	171,375	29,094	5,552	212,317	26,884	12,523
Finance	104,035	112,808	5,515	325,938	167,889	16,510
Tourist trade	35,680	4,358	14	41,271	2,764	2
Agriculture	147,855	10,925	3,755	175,903	9,526	3,444
Manufacturing	904,331	44,252	48,470	1,088,758	22,662	55,866
Individuals	542,447	1,901,558	22,026	270,043	1,836,543	14,014
Other	90,007	595,581	66,391	5,469	712,929	45,231
<b>Total by sector</b>	<b>3,110,015</b>	<b>3,110,015</b>	<b>153,238</b>	<b>3,108,567</b>	<b>3,108,567</b>	<b>163,516</b>
<b>Allocated value of collateral</b>	1,379,036		56,963	1,736,871	-	68,524

**42 Subsequent events**

There was a change in the Bank, at the beginning of 2017, in the composition of the Management Board members as follows:

Zdenka Pogarčić - Member of Supervisory Board (since 02.02.2017.)

Ana Michieli Pavuna - Member of Supervisory Board (since 02.02.2017.)

CROATIA BANKA d.d.  
APPENDIX A – OTHER REGULATORY REQUIREMENTS

Supplementary report for the Croatian National Bank

The statutory financial statements presented below were prepared under the reporting requirements and the financial reporting schedules determined by the CNB Decision on the structure and content of annual financial statements of banks (the 'Decision').

Balance sheet

	<i>in thousands of HRK</i>	
	2016	2015
1 CASH AND BALANCES WITH THE CNB (1.1+1.2)	449,721	277,961
1.1 Cash	20,866	27,498
1.2 Balances with the CNB	428,855	250,463
2 DEPOSITS WITH BANKING INSTITUTIONS	77,162	103,293
3 TREASURY BILLS OF THE MINISTRY OF FINANCE AND OF THE CNB	498,257	520,302
4 SECURITIES AND OTHER FINANCIAL INSTRUMENTS HELD FOR TRADING	-	-
5 SECURITIES AND OTHER FINANCIAL INSTRUMENTS AVAILABLE FOR SALE	328,460	154,135
6 SECURITIES AND OTHER FINANCIAL INSTRUMENTS HELD TO MATURITY	51,124	48,378
7 SECURITIES AND OTHER FINANCIAL INSTRUMENTS AT FVTPL THAT ARE NOT ACTIVELY TRADED	-	-
8 DERIVATIVE FINANCIAL ASSETS	-	-
9 LOANS TO FINANCIAL INSTITUTIONS	25,564	25,366
10 LOANS AND ADVANCES TO OTHER CUSTOMERS	1,582,720	1,887,605
11 INVESTMENTS IN SUBSIDIARIES, ASSOCIATES AND JOINT VENTURES	-	-
12 FORECLOSED ASSETS	57,092	60,234
13 TANGIBLE ASSETS (NET OF DEPRECIATION)	13,504	15,706
14 INTEREST, FEES AND OTHER ASSETS	40,585	19,293
<b>TOTAL ASSETS</b>	<b>3,124,189</b>	<b>3,112,273</b>
<b>LIABILITIES</b>		
1 LOANS FROM FINANCIAL INSTITUTIONS (1.1+1.2)	290,320	292,435
1.1 Short-term borrowings	163,911	130,000
1.2 Long-term borrowings	126,409	162,435
2 DEPOSITS (2.1+2.2+2.3)	2,541,631	2,567,743
2.1 Balances on giro and current accounts	338,669	364,667
2.2 Savings deposits	117,806	127,767
2.3 Term deposits	2,085,156	2,075,308
3 OTHER BORROWED FUNDS (3.1+3.2)	-	-
3.1 Short-term borrowings	-	-
3.2 Long-term borrowings	-	-
4 DERIVATIVE FINANCIAL AND OTHER LIABILITIES HELD FOR TRADING	-	3
5 ISSUED DEBT SECURITIES (5.1+5.2)	-	-
5.1 Short-term debt securities issued	-	-
5.2 Long-term debt securities issued	-	-
6 SUBORDINATED INSTRUMENTS ISSUED	-	-
7 HYBRID INSTRUMENTS ISSUED	-	-
8 INTEREST, FEES AND OTHER LIABILITIES	102,603	69,566
<b>TOTAL LIABILITIES</b>	<b>2,934,554</b>	<b>2,930,242</b>

## Supplementary report for the Croatian National Bank (continued)

**EQUITY**

1 SHARE CAPITAL	474,600	474,600
2 PROFIT/(LOSS) FOR THE YEAR	1,638	(15,134)
3 RETAINED PROFIT/(ACCUMULATED LOSSES)	(292,174)	(277,040)
4 LEGAL RESERVES	-	-
5 STATUTORY AND OTHER CAPITAL RESERVES	-	-
6 UNREALISED GAINS/(LOSSES) ON REVALUATION OF FINANCIAL ASSETS AVAILABLE FOR SALE	5,571	(395)
7 HEDGING RESERVE	-	-
<b>TOTAL EQUITY</b>	<b>189,635</b>	<b>182,031</b>
<b>TOTAL EQUITY AND LIABILITIES</b>	<b>3,124,189</b>	<b>3,112,273</b>

## Supplementary report for the Croatian National Bank (continued)

## Income statement

	<i>in thousands of HRK</i>	
	<b>2016</b>	<b>2015</b>
1 Interest income	131,241	148,904
2 Interest expense	(69,290)	(82,909)
<b>3 Net interest income</b>	<b>61,951</b>	<b>65,995</b>
4 Fee and commission income	12,056	13,357
5 Fee and commission expenses	(4,360)	(4,894)
<b>6 Net fee and commission income</b>	<b>7,696</b>	<b>8,463</b>
7 Gains/(losses) on investments in subsidiaries, associates and joint ventures	-	-
8 Trading gains/(losses)	3,405	4,105
9 Gains/(losses) on embedded derivatives	3	(3)
10 Gains / (losses) on assets at FVTPL not actively traded	-	-
11 Gains / (losses) on available-for-sale assets	6,679	4,115
12 Gains / (losses) on held-to-maturity (HTM) assets	1,026	-
13 Hedging gains/(losses)	-	-
14 Gains on investments in subsidiaries, associates and joint ventures	-	-
15 Gains on other equity investments	-	-
16 Foreign exchange gains/(losses)	(490)	(449)
17 Other income	7,147	8,798
18 Other expenses	(3,221)	(5,794)
19 General administrative expenses and depreciation	(62,468)	(66,013)
<b>20 Net profit from operations before impairment and provisions for losses</b>	<b>21,728</b>	<b>19,217</b>
21 Impairment losses and provisions	(19,064)	(16,954)
<b>22 PROFIT BEFORE TAXATION</b>	<b>2,664</b>	<b>2,263</b>
<b>23 INCOME TAX</b>	<b>(1,026)</b>	<b>(17,397)</b>
<b>24 (LOSS)/PROFIT FOR THE YEAR</b>	<b>1,638</b>	<b>(15,134)</b>
25 Earnings/loss per share	0.38	(3.19)

CROATIA BANKA d.d.  
APPENDIX A – OTHER REGULATORY REQUIREMENTS (continued)

Supplementary report for the Croatian National Bank (continued)

Statement of cash flows

I T E M	<i>in thousands of HRK</i>	
	2016	2015
<b>Operating activities</b>		
Profit/(loss) before taxation	2,664	2,263
Impairment allowance and provisions for losses	17,139	22,835
Depreciation and amortisation	3,470	3,343
Net unrealised (gains)/losses on financial assets and liabilities at FVTPL	(46)	-
(Gains)/losses on sale of tangible assets	(1,593)	(1,070)
Other (gains) / losses	(210)	(1,307)
<b>Operating cash flows before changes in operating assets</b>	<b>21,424</b>	<b>26,064</b>
Balances with the CNB	34,776	(17,867)
Treasury bills of the Ministry of Finance and of the CNB	22,044	(38,921)
Deposits with banking institutions and loans to financial institutions	-	-
Loans and advances to other customers	287,821	(5,451)
Securities and other financial instruments available for sale	(174,325)	(45,181)
Securities and other financial instruments held for trading	-	-
Securities and other financial instruments at FVTPL that are not actively traded	-	-
Other operating assets	(12,923)	7,044
<b>Net (increase) / decrease in operating assets</b>	<b>157,393</b>	<b>(100,376)</b>
Demand deposits	(25,999)	(71,334)
Savings and term deposits	4,544	93,973
Other liabilities	28,137	(19,368)
<b>Net increase / (decrease) in operating liabilities</b>	<b>6,682</b>	<b>3,271</b>
Net cash flow from operations before income tax	185,499	(71,041)
Income taxes paid	-	-
<b>Net cash inflow / (outflow) from operating activities</b>	<b>185,499</b>	<b>(71,041)</b>
<b>Investing activities</b>		
Proceeds from sale/(Payments for purchases) of tangible and intangible assets	2,461	3,919
Proceeds from sale of/Payments for investments in subsidiaries, associates and joint ventures	-	-
Proceeds from/(Payments to acquire) securities and other financial instruments held to maturity	(2,746)	12,592
Dividends received	-	-
Other receipts/(payments) from financing activities	(4,067)	(8,479)
<b>Net cash from investing activities</b>	<b>(4,352)</b>	<b>8,032</b>
<b>Financing activities</b>		
Net increase/(decrease) in borrowings	(723)	89,312
Net increase/decrease of issued debt securities	-	-
Net increase/(decrease) in subordinated and hybrid instruments	-	-
Other receipts/(payments) from financing activities	-	-
Increase in share capital	-	-
<b>Net cash from financing activities</b>	<b>(723)</b>	<b>89,312</b>
<b>Net increase / (decrease) in cash and cash equivalents</b>	<b>180,424</b>	<b>26,303</b>
<b>Cash and cash equivalents, beginning of the year</b>	<b>152,834</b>	<b>126,531</b>
<b>Cash and cash equivalents at the end of the year</b>	<b>333,258</b>	<b>152,834</b>



Supplementary report for the Croatian National Bank (continued)

Statement of changes in equity

*in thousands of HRK*

Type of change in equity	Share capital	Retained earnings / (Accumulated losses)	Profit/(Loss) for the year	Unrealised gains/losses on revaluation of financial assets available for sale	Total equity
<b>At 1 January of the current year</b>	<b>474,600</b>	<b>(277,040)</b>	<b>(15,134)</b>	<b>(395)</b>	<b>182,031</b>
Change in the fair value of financial assets available for sale	-	-	-	5,966	5,966
Net gains/losses recognised directly in equity	-	-	-	-	-
Profit/(Loss) for the year	-	-	1,638	-	1,638
Total recognised income and expenses for the year	-	-	-	-	-
Increase/Decrease in share capital	-	-	-	-	-
Other changes	-	(15,134)	15,134	-	-
<b>Balance at 31 December of the current year</b>	<b>474,600</b>	<b>(292,174)</b>	<b>1,638</b>	<b>5,571</b>	<b>189,635</b>

CROATIA BANKA d.d.  
APPENDIX A – OTHER REGULATORY REQUIREMENTS (continued)

Supplementary report for the Croatian National Bank (continued)

Balance sheet reconciliation at 31.12.2016

I T E M	<i>in thousands of HRK</i>		
	Under CNB Decision	Under Annual Report	Difference
<b>Assets</b>			
1 CASH AND BALANCES WITH THE CNB (1.1+1.2)	<b>449,721</b>	-	<b>449,721</b>
1.1 Cash	20,866	-	20,866
1.2 Balances with the CNB	428,855	-	428,855
2 DEPOSITS WITH BANKING INSTITUTIONS	77,162	-	77,162
<i>Cash</i>	-	276,808	(276,808)
<i>Balances with the CNB</i>	-	191,709	(191,709)
<i>Placements with banks</i>	-	53,334	(53,334)
3 CNB TREASURY BILLS	498,257	-	498,257
4 SECURITIES AND OTHER FINANCIAL INSTRUMENTS HELD FOR TRADING	-	-	-
5 SECURITIES AND OTHER FINANCIAL INSTRUMENTS AVAILABLE FOR SALE	328,460	833,773	(505,313)
6 SECURITIES AND OTHER FINANCIAL INSTRUMENTS HELD TO MATURITY	51,124	50,647	477
7 SECURITIES AND OTHER FINANCIAL INSTRUMENTS AT FVTPL THAT ARE NOT ACTIVELY TRADED	-	-	-
8 DERIVATIVE FINANCIAL ASSETS	-	-	-
9 LOANS TO FINANCIAL INSTITUTIONS	25,564	-	25,564
10 LOANS AND ADVANCES TO OTHER CUSTOMERS	1,582,720	1,590,643	(7,923)
11 INVESTMENTS IN SUBSIDIARIES, ASSOCIATES AND JOINT VENTURES	-	-	-
12 FORECLOSED ASSETS	57,092	23,389	33,703
13 TANGIBLE ASSETS (NET OF DEPRECIATION)	13,504	13,427	77
<i>Investment property</i>	-	33,702	(33,702)
<i>Intangible assets</i>	-	4,926	(4,926)
<i>Deferred tax assets</i>	-	1,898	(1,898)
14 INTEREST, FEES AND OTHER ASSETS	40,585	35,759	4,826
<b>TOTAL ASSETS</b>	<b>3,124,189</b>	<b>3,110,015</b>	<b>14,174</b>

CROATIA BANKA d.d.  
APPENDIX A – OTHER REGULATORY REQUIREMENTS (continued)

Supplementary report for the Croatian National Bank  
(continued)  
Balance sheet reconciliation at 31.12.2016 (continued)

I T E M	Under CNB Decision	Under Annual Report	Difference
<b>Liabilities and equity</b>			
1 LOANS FROM FINANCIAL INSTITUTIONS (1.1+1.2)	290,320	292,003	(1,683)
1.1 Short-term borrowings	163,911	-	163,911
1.2 Long-term borrowings	126,409	-	126,409
<i>Borrowings</i>	-	292,003	(292,003)
2 DEPOSITS (2.1+2.2+2.3)	2,541,631	2,608,592	(66,961)
2.1 Balances on giro and current accounts	338,669	-	338,669
2.2 Savings deposits	117,806	-	117,806
2.3 Term deposits	2,085,156	2,044,562	40,594
<i>Demand deposits</i>	-	471,935	(471,935)
<i>Liabilities to banks</i>	-	92,095	(92,095)
3 OTHER BORROWED FUNDS (3.1+3.2)	-	-	-
3.1 Short-term borrowings	-	-	-
3.2 Long-term borrowings	-	-	-
4 DERIVATIVE FINANCIAL AND OTHER LIABILITIES HELD FOR TRADING	-	-	-
5 ISSUED DEBT SECURITIES (5.1+5.2)	-	-	-
5.1 Short-term debt securities issued	-	-	-
5.2 Long-term debt securities issued	-	-	-
6 SUBORDINATED INSTRUMENTS ISSUED	-	-	-
7 HYBRID INSTRUMENTS ISSUED	-	-	-
8 INTEREST, FEES AND OTHER LIABILITIES	102,603	9,109	93,494
<i>Provisions</i>	-	10,676	(10,676)
<b>TOTAL LIABILITIES (1+2+3+4+5+6+7+8)</b>	<b>2,934,554</b>	<b>2,920,380</b>	<b>14,174</b>
<b>Equity</b>			
1 SHARE CAPITAL	474,600	474,600	-
2 PROFIT/(LOSS) FOR THE YEAR	1,638	1,638	-
3 RETAINED PROFIT/(ACCUMULATED LOSSES)	(292,174)	(292,174)	-
4 LEGAL RESERVES	-	-	-
5 STATUTORY AND OTHER CAPITAL RESERVES	-	-	-
6 UNREALISED GAINS/(LOSSES) ON REVALUATION OF FINANCIAL ASSETS AVAILABLE FOR SALE	5,571	5,571	-
7 HEDGING RESERVE	-	-	-
<b>TOTAL EQUITY</b>	<b>189,635</b>	<b>189,635</b>	<b>-</b>
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>3,124,189</b>	<b>3,110,015</b>	<b>14,174</b>

**Supplementary report for the Croatian National Bank (continued)****Balance sheet reconciliation at 31.12.2016 (continued)**

The departures on the items included in the Annual Report versus the standard under the CNB Decision comprise the following:

**ASSETS**

Cash and deposits with the CNB, Deposits with banking institutions and Loans to financial institutions are items separately shown under the CNB standard, while in the Annual report those items are shown within the items Cash, Receivables from the CNB and Placements with banks. The CNB reporting line items Specific reserves for identified losses on a collective basis is included in Interest, fees and other assets, whereas in the Annual Report they are presented along with the items to which they relate.

Treasury bills of the Ministry of Finance and Securities and other financial instruments available for sale, disclosed separately under the CNB standard, are aggregated in the Annual Report under Financial assets available for sale.

The line item 'Loans and advances to customers' reported in the Annual report includes loan principal and the related accrued interest reduced by portfolio-based i.e. collective and individual provisions less overpaid loans and collected interest income relating to future periods. The CNB report line items 'Loans to other customers' and 'Loans to financial institutions' include principal amounts reduced by individual provisions, whereas collective provisions and accrued interest are presented under the line item 'Interest, fees and other assets', and overpaid loans and collected interest income relating to future periods under the line item 'Interest, fees and other liabilities'.

In addition, Tangible assets disclosed under the CNB decision include inventories which are presented in the Annual Report under Other assets.

Intangible assets are presented in the Annual Report separately, while in the CNB report they are included in Interest, fees and other assets. In addition, Interest, fees and other assets disclosed under the CNB requirements relate to the related receivables, whereas in the Annual Report interest receivable is presented along with the items it relates to.

**LIABILITIES AND EQUITY**

Loans from financial institutions (both short-term and long-term) and other loans are items that are presented separately under the CNB standard, and in the Annual Report they are included in Borrowings.

Giro account and current account balances, Savings deposits and Term deposits represent items under the CNB standard, while in the Annual Report they are included under line items Demand deposits, Term deposits and Liabilities to banks.

Restricted deposits are also included in the Interest, fees and other liabilities under the CNB disclosure requirements, and in the Annual Report they are presented under Demand deposits.

Interest, fees and other liabilities is a separate line item under the CNB presentation requirements, and in the Annual Report the individual components are included in Borrowings, Term deposits, Liabilities to banks, Provisions and Other liabilities, as appropriate.

Supplementary report for the Croatian National Bank (continued)

Reconciliation of profit and loss items at 31.12.2016

I T E M	<i>in thousands of HRK</i>		
	Under CNB Decision	Under Annual Report	Difference
1 Interest income	131,241	131,425	(184)
2 Interest expense	(69,290)	(69,569)	279
<b>3 Net interest income</b>	<b>61,951</b>	<b>61,856</b>	<b>95</b>
4 Fee and commission income	12,056	12,056	-
5 Fee and commission expenses	(4,360)	(4,360)	-
<b>6 Net fee and commission income</b>	<b>7,696</b>	<b>7,696</b>	-
7 Gains/(losses) on investments in subsidiaries, associates and joint ventures	-	-	-
8 Trading gains/(losses)	3,405	-	3,405
9 Gains/(losses) on embedded derivatives	3	-	3
10 Gains/(losses) on assets at FVTPL not actively traded	-	-	-
<i>Net financial (losses) gains</i>	-	7,751	(7,751)
<i>Net gains from exchange differences</i>	-	3,219	(3,219)
11 Gains/(losses) on available-for-sale assets	6,679	-	6,679
12 Gains/(losses) on held-to-maturity (HTM) assets	1,026	-	1,026
13 Hedging gains/(losses)	-	-	-
14 Gains on investments in subsidiaries, associates and joint ventures	-	-	-
15 Gains on other equity investments	-	-	-
16 Foreign exchange gains/(losses)	(490)	-	(490)
17 Other income	7,147	6,361	786
18 Other expenses	(3,221)	-	(3,221)
19 General administrative expenses and depreciation	(62,468)	-	(62,468)
<i>Other operating expenses</i>	-	(62,112)	62,112
<b>20 Net profit from operations before impairment and provisions for losses</b>	<b>21,728</b>	<b>24,771</b>	<b>(3,043)</b>
21 Impairment losses and provisions	(19,064)	(22,107)	3,043
<b>22 PROFIT BEFORE TAXATION</b>	<b>2,664</b>	<b>2,664</b>	-
<b>23 INCOME TAX</b>	<b>(1,026)</b>	<b>(1,026)</b>	-
<b>24 LOSS FOR THE YEAR</b>	<b>1,638</b>	<b>1,638</b>	-
25 Loss per share	0.35	0.35	-

**Supplementary report for the Croatian National Bank (continued)**

**Reconciliation of profit and loss items at 31.12.2016 (continued)**

The line items Interest income/Interest expense under the CNB standard include Net foreign exchange gains which are reported in the Annual Report under Net foreign exchange gains.

Under the CNB standard, Trading gains/(losses), Gains/(losses) on embedded derivatives, Gains/(losses) on exchange differences and the already mentioned net exchange differences on interest income/expense are presented in the Annual Report, except for exchange differences on provisions which are included in the CNB report in Impairment and provisions for losses.

Furthermore, under the CNB standards, Gains/(losses) on available for sale assets and Gains on other equity investments are combined under Net financial (loss)/gains in the Annual Report.

Items Other expenses, General administrative expenses and depreciation under the CNB standard comprise the line item Other operating expenses in the Annual Report, and the difference relates to provisions for legal actions initiated against the Bank and to provisions for liabilities to employees which were included in the Annual Report in Impairment allowance and provisions for losses.

## Supplementary report for the Croatian National Bank (continued)

## Reconciliation of the Statements of cash flows for 2016

I T E M	Under CNB Decision	Under Annual Report	Difference
<b>Operating activities</b>			
Profit/(loss) before taxation	2,664	2,664	-
Impairment allowance and provisions for losses	17,139	-	17,139
<i>Impairment allowance on loans and other assets (net)</i>	-	17,139	(17,139)
<i>Provisions for contingent liabilities (net)</i>	-	(102)	102
<i>Litigation provision (net)</i>	-	5,282	(5,282)
<i>Other provisions (net)</i>	-	42	(42)
Depreciation and amortisation	3,470	3,470	-
Net unrealised (gains)/losses on financial assets and liabilities at FVTPL	(46)	-	(46)
(Gains)/losses on sale of tangible assets	(1,593)	(1,593)	-
<i>Foreign exchange differences on translation</i>	-	145	(145)
<i>Write-offs of tangible assets</i>	-	2,128	(2,128)
<i>(Gains)/losses on realisation of available-for-sale assets</i>	-	(7,705)	7,705
<i>Gains on trading financial assets at fair value</i>	-	(46)	46
Other (gains) / losses	(210)	-	(210)
<b>Operating cash flows before changes in operating assets</b>	<b>21,424</b>	<b>21,424</b>	<b>-</b>
Balances with the CNB	34,776	-	34,776
<i>Decrease / Increase in receivables from the Croatian National Bank</i>	-	34,776	(34,776)
Treasury bills of the Ministry of Finance and of the CNB	22,044	-	22,044
Deposits with banking institutions and loans to financial institutions	-	-	-
Loans and advances to other customers	287,821	-	287,821
<i>(Increase) in loans and advances to customers</i>	-	284,781	(284,781)
Securities and other financial instruments available for sale	(174,325)	-	(174,325)
Securities and other financial instruments held for trading	-	-	-
Securities and other financial instruments at FVTPL that are not actively traded	-	-	-
Other operating assets	(12,923)	(7,820)	(5,103)
<b>Net (increase) / decrease in operating assets</b>	<b>157,393</b>	<b>311,737</b>	<b>(154,344)</b>
Demand deposits	(25,999)	(17,808)	(8,191)
Savings and term deposits	4,544	(1,341)	5,885
<i>Increase/(decrease) in liabilities to other banks</i>	-	16,543	(16,543)
Other liabilities	28,137	(3,392)	31,529
<b>Net increase / (decrease) in operating liabilities</b>	<b>6,682</b>	<b>(5,998)</b>	<b>12,680</b>
Net cash flow from operations before income tax	185,499	327,163	(141,664)
Income taxes paid	-	-	-
<b>Net cash inflow / (outflow) from operating activities</b>	<b>185,499</b>	<b>327,163</b>	<b>(141,664)</b>
<b>Investing activities</b>			
Proceeds from sale/(Payments for purchases) of tangible and intangible assets	2,461	-	2,461
Proceeds from sale of/Payments for investments in subsidiaries, associates and joint ventures	-	-	-
Proceeds from/(Payments to acquire) securities and other financial instruments held to maturity	(2,746)	-	(2,746)

**Supplementary report for the Croatian National Bank  
(continued)**
**Reconciliation of the Statements of cash flows for 2016  
(continued)**

<i>Sale of financial assets available for sale</i>	-	(921,220)	921,220
<i>Purchase of financial assets available for sale</i>	-	778,896	(778,896)
<i>Decrease in financial assets held to maturity</i>	-	(2,087)	2,087
<i>Purchases of property, equipment and intangible assets</i>	-	(4,067)	(4,067)
<i>Decrease/(increase) in foreclosed assets</i>	-	2,462	(2,462)
Dividends received			
Other receipts/(payments) from financing activities	(4,067)	-	4,067
<b>Net cash from investing activities</b>	<b>(4,352)</b>	<b>(146,016)</b>	<b>141,664</b>
<b>Financing activities</b>	<b>(723)</b>	<b>(723)</b>	<b>-</b>
Net increase/(decrease) in borrowings	-	-	-
<i>Proceeds from borrowings, net</i>	-	-	-
Net increase/decrease of issued debt securities	-	-	-
Net increase/(decrease) in subordinated and hybrid instruments	-	-	-
Other receipts/(payments) from financing activities			-
Increase in share capital			-
<b>Net cash from financing activities</b>	<b>(723)</b>	<b>(723)</b>	<b>-</b>
<b>Net increase / (decrease) in cash and cash equivalents</b>	<b>180,424</b>	<b>180,424</b>	<b>-</b>
<b>Cash and cash equivalents, beginning of the year</b>	<b>152,834</b>	<b>152,834</b>	<b>-</b>
			-
<b>Cash and cash equivalents at the end of the year</b>	<b>333,258</b>	<b>333,258</b>	<b>-</b>

The departures on the items included in the Annual Report versus the standard under the CNB Decision comprise the following:

According to the CNB standard, Impairment allowance and provisions for losses as a single amount, while in the Annual Report they are shown within the items Impairment of loans and other assets, Provisions for contingent liabilities, Provisions for judicial proceedings and Other provisions.

MoF treasury bills under the CNB standard, together with items Securities and other financial instruments available for sale and Securities and other financial instruments held for trading are presented in the Annual Report within Investing activities, while under the CNB standard they are presented within Operating activities.



**Supplementary report for the Croatian National Bank (continued)**

In accordance with Article 164 of the Credit Institutions Act, the Bank is required to disclose the following information relating to the previous financial year:

1. Banking and financial services provided, the nature of its activities and the geographic location of services provision;
2. Amount of total income;
3. Number of employees on a full-time equivalent basis;
4. Amount of income tax; and
5. The amount of state subsidies received

## Ad.1.

In accordance with the Credit Institutions Act 164, the Bank engages in the following banking and financial services in the country and abroad:

- Receiving cash deposits,
- Granting of loans and other placements on its own behalf and for its own account,
- Issuing means of payment in the form of electronic money,
- Issuing guarantees and other commitments,
- Factoring,
- Finance leasing,
- Lending, including customer loans, mortgage loans and financing commercial transactions (including forfeiting),
- Trading on its own behalf and for its own account or on its own behalf and for the account of the client: money market instruments and other transferable securities, foreign currencies, including currency exchange, financial futures and options, currency and interest rate instruments,
- Payment transactions in the country and abroad in accordance with special laws,
- Collection, analysis and provision of information on the creditworthiness of legal entities and natural persons who perform activities independently,
- Issuing and management of payment instruments,
- Rental of safe deposit boxes,
- Representation in insurance,
- Receipt and transfer of orders in relation to one or more financial instruments,
- Execution of orders on behalf of clients,
- Trading for own account,
- Underwriting services, i.e. the sale of financial instruments with a purchase obligation,
- Underwriting Services, i.e. the sale of financial instruments without a purchase obligation,
- Safekeeping and administration of financial instruments for the account of clients, including custodianship and related services such as cash management and security instruments,

**Supplementary report for the Croatian National Bank (continued)**

- Providing loans to investors to allow carrying out transactions with one or more financial instruments, if the transactions involve a company that grants loans,
- Foreign exchange services, if related to the provision of investment services,
- Services related to underwriting or selling financial instruments with a purchase obligation.

In accordance with the National Classification of Activities, the activities of Croatia banka are defined as: 64.19 Other monetary intermediation.

In 2016 Croatia banka performed its activities in the Republic of Croatia.

Ad.2.

In 2016, Croatia banka realised a total net income of HRK 86,883 thousand.

Ad.3.

As at 31 December 2016, Croatia banka had 208 employees based on the number of hours of work, but at the end of 2016 the actual number of employees was 213.

Ad.4.

Income tax expense represents the sum of the tax currently payable and deferred tax. The Bank realised a taxable profit for 2016, but has no obligation to pay income tax because it utilises the benefit of tax losses brought forward from 2012 and 2013.

The amount reported under income tax relates to reversal of deferred tax assets in respect of tax losses upon the revision of the Long-term financial plan and to net deferred tax assets on prepaid/paid benefits.

Ad.5.

In 2016 Croatia banka did not receive any state subsidies.

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IBAN:                         HR0324850031000009027

**BUSINESS NETWORK**

<b>The City</b>	<b>Address</b>	<b>Phone</b>	<b>Fax</b>
Bjelovar Branch	Ulica Petra Zrinskog 14 43000 Bjelovar	043 241 610 043 241 611	043 241 612
Čakovec Branch	Ulica Ivana Mažuranića 2 40000 Čakovec	040 310 160 040 311 672	040 310 643
Drenovci Branch	Veliki šor 2 32257 Drenovci	032 862 842 032 862 843	032 862 844
Metković Branch	Ulica S.Radića 8 20350 Metković	020 681 013 020 681 082	020 681 089
Osijek Branch	Šamačka ulica 1 31000 Osijek	031 203 001 031 203 005	031 203 002
Pula Branch	Istarska ulica 14 52100 Pula	052 451 202 052 451 304	052 451 505
Požega Branch	Cehovska ulica 3 34000 Požega	034 274 460	034 274 440
Rijeka Branch	Riva Boduli 1 51000 Rijeka	051 214 927 051 214 957	051 214 947
Slavonski Brod Branch	Trg Ivane Brlić Mažuranić 15 35000 Slavonski Brod	035 442 112	035 442 110
Split Branch	Ulica Matice Hrvatske 1 21000 Split	021 539 795	021 539 794
Vinkovci Branch	Duga ulica b.b. 32100 Vinkovci	032 331 377 032 331 453	032 331 213

CROATIA BANKA d.d.  
BUSINESS NETWORK AND CONTACTS (continued)

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The City	Address	Phone	Fax
Virovitica Branch	Trg kralja Zvonimira 10 33000 Virovitica	033 725 441	033 725 602
Vukovar Branch	Josipa Jurja Strossmayera 5 32000 Vukovar	032 450 520	032 450 490
Zadar Branch	Ulica Franje Tuđmana 46 23000 Zadar	023 305 294 023 305 055	023 305 130
Šubićeva Outlet, Zagreb	Šubićeva 67 10000 Zagreb	01 4623 024	01 4623 027
Zagreb Branch / Sky Office Outlet	R.F. Mihanovića 9 10110 Zagreb	01 2391 667 01 2391 282	01 2391 240
Županja Branch	Strossmayerova 5 32270 Županja	032 831 051	032 833 424