

**BANKA KOVANICA d.d.**

**Financial statements as at  
31 December 2015 together with the  
Independent Auditor's Report**

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## Responsibility for the financial statements

Pursuant to the Croatian Accounting Act (Official Gazette 109/07, 54/13 and 121/14), the Management Board is responsible for ensuring that the financial statements are prepared for each financial year in accordance with statutory accounting regulations applicable to banks in Croatia, in order to give a true and fair view of the financial position and results of the 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 financial statements.

In preparing 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 Act (Official Gazette 190/07, 54/13 and 121/14). 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.

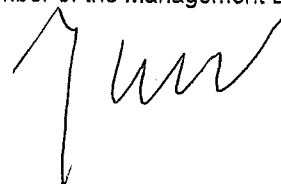
Signed on behalf of the Management Board:

Nicola Ceccaroli

Darko Kosovec

President of the Management Board

Member of the Management Board



Banka Kovanica d.d.  
Preradovićeve 29  
Varaždin

30 March 2016



## ***Independent Auditor's Report***

### **To the Shareholders and Management of Banka Kovanica d.d.**

We have audited the accompanying financial statements of Banka Kovanica d.d. (the "Bank"), which comprise the balance sheet as at 31 December 2015 and the statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes comprising a summary of significant accounting policies and other explanatory information.

### **Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting regulations applicable to banks in Croatia as set out in Note 2.1 - 'Accounting framework' to the financial statements 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.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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*PricewaterhouseCoopers d.o.o., Ulica kneza Ljudevita Posavskog 31, 10000 Zagreb, Croatia*  
*T: +385 (1) 6328 888, F: +385 (1) 6111 556, [www.pwc.hr](http://www.pwc.hr)*

Commercial Court in Zagreb, Tt-99/7257-2, Reg. No.: 080238978; Company ID No.: 81744835353; Founding capital: HRK 1,810,000.00, paid in full; Management Board: Hrvoje Zgombić, President; J. M. Gasparac, Member; S. Dušić, Member; T. Mačašović, Member; Giro-Account: Raiffeisenbank Austria d.d., Petrinjska 59, Zagreb, IBAN: HR8124840081105514875.



## **Opinion**

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2015, its financial performance and cash flows for the year then ended in accordance with accounting regulations applicable to banks in Croatia as set out in Note 2.1 - 'Accounting framework' to the financial statements.

## **Emphasis of Matter**

Without qualifying our opinion, we draw attention to Note 29 which states that the Bank is involved in a legal dispute relating to the issuance of the Bank's guarantee in the amount of EUR 710 thousand, which is contested by the Bank. In the first-instance verdict the claim was entirely rejected, i.e. the court ruled in favour of the Bank and the Bank's Management believes that the final ruling will be positive for the Bank.

PricewaterhouseCoopers d.o.o.  
Zagreb, 30 March 2016

This version of our report is a translation from the original, which was prepared in Croatian language. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.

# Statement of comprehensive Income

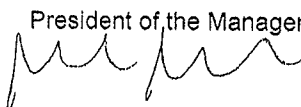
for the period from 1 January to 31 December 2015

	Note	2015 HRK'000	2014 HRK'000
Interest income		81,145	78,470
Interest expense		(29,515)	(36,361)
<b>Net interest income</b>	4	<b>51,630</b>	<b>42,109</b>
Fee and commission income		6,648	5,923
Fee and commission expense		(1,465)	(1,279)
<b>Net fee and commission income</b>	5	<b>5,183</b>	<b>4,644</b>
Foreign exchange differences – net	6	1,683	1,695
Result of assets available for sale - net	17	261	2,178
Other operating income	7	1,547	3,193
Impairment charge for credit losses - net	8	(5,769)	(17,818)
Administrative expenses	9	(37,200)	(44,874)
Other operating expenses	10	(6,587)	(4,611)
<b>Profit/(loss) before Income tax</b>		<b>10,747</b>	<b>(13,484)</b>
Income tax	11	-	-
<b>Profit/loss after tax</b>		<b>10,747</b>	<b>(13,484)</b>
Unrealised (loss)/gains from available-for-sale financial assets		(161)	1,802
<b>Other comprehensive (loss)/profit</b>		<b>(161)</b>	<b>1,802</b>
<b>Total comprehensive Income/loss</b>		<b>10,586</b>	<b>(11,682)</b>
Earnings/(loss) per share.	12	3.20	(4.15)

The financial statements set out on pages 4 to 56 were approved by the Management Board of the Bank on 30 March 2016.

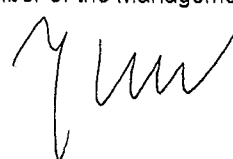
Nicola Ceccaroli

President of the Management Board



Darko Kosovec

Member of the Management Board

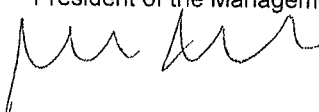
The notes to the financial statements are an integral part of the Statement of comprehensive income.

**Statement of financial position**  
as at 31 December 2015

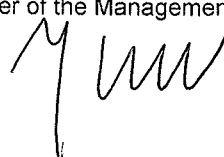
	Note	31 December 2015	31 December 2014
		HRK'000	HRK'000
<b>ASSETS</b>			
Cash on hand and balances with banks	13	175,498	128,770
Obligatory reserve with the Croatian National Bank	14	82,754	91,548
Placements with banks	15	39,225	39,313
Loans and advances to customers	16	740,912	750,021
Available-for-sale financial assets	17	65,362	72,624
Held-to-maturity financial assets	18	910	1,008
Property and equipment	19	15,867	18,390
Intangible assets	19	1,867	1,103
Reposessed collateral	20	37,867	37,519
Other assets	21	27,623	13,092
<b>Total assets</b>		<b>1,187,887</b>	<b>1,153,388</b>
<b>LIABILITIES</b>			
Deposits from customers	22	1,000,566	973,870
Due to banks	23	22,076	54,536
Hybrid instruments	24	34,594	14,925
Other liabilities	26	19,710	9,702
		<b>1,076,946</b>	<b>1,053,033</b>
<b>SHAREHOLDERS' EQUITY</b>			
Share capital	27	333,834	333,834
Treasury shares		(15)	(15)
Share premium		76,430	76,430
Reserves		920	1,081
Accumulated loss		(310,975)	(297,491)
Loss for the year		10,747	(13,484)
		<b>110,941</b>	<b>100,355</b>
<b>Total liabilities and shareholders' equity</b>		<b>1,187,887</b>	<b>1,153,388</b>

The financial statements set out on pages 4 to 56 were approved by the Management Board of the Bank on 30 March 2016.

Nicola Ceccaroli  
President of the Management Board



Darko Kosovec  
Member of the Management Board



## Statement of changes in equity

for the year from 1 January to 31 December 2015

	Share capital HRK'000	Treasury shares HRK'000	Share premium HRK'000	Reserves HRK'000	Accumulated loss HRK'000	Total HRK'000
<b>Balance at 31 December 2014</b>	<b>333,834</b>	<b>(15)</b>	<b>76,430</b>	<b>1,082</b>	<b>(310,976)</b>	<b>100,355</b>
Loss for the year	-	-	-	-	10,747	10,747
Unrealised gains on available-for-sale financial assets	-	-	-	(161)	-	(161)
<b>Total comprehensive income/(loss)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(161)</b>	<b>10,747</b>	<b>10,586</b>
<b>Balance at 31 December 2015</b>	<b>333,834</b>	<b>(15)</b>	<b>76,430</b>	<b>921</b>	<b>(300,229)</b>	<b>110,941</b>

	Share capital HRK'000	Treasury shares HRK'000	Share premium HRK'000	Reserves HRK'000	Accumulated loss HRK'000	Total HRK'000
<b>Balance at 31 December 2013</b>	<b>291,084</b>	<b>(15)</b>	<b>76,430</b>	<b>(721)</b>	<b>(297,491)</b>	<b>69,288</b>
Loss for the year	-	-	-	-	(13,484)	(13,484)
Unrealised gains on available-for-sale financial assets	-	-	-	1,802	-	1,802
<b>Total comprehensive income/(loss)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>1,802</b>	<b>(13,484)</b>	<b>(11,682)</b>
Contributions in equity	42,750	-	-	-	-	42,750
<b>Balance at 31 December 2014</b>	<b>333,834</b>	<b>(15)</b>	<b>76,430</b>	<b>1,081</b>	<b>(310,975)</b>	<b>100,355</b>

The notes to the financial statements are an integral part of the Statement of changes in equity.



## Statement of cash flows

for the year from 1 January to 31 December 2015

	Note	2015 HRK'000	2014 HRK'000
<b>Cash flow from operating activities</b>			
Profit/(loss) for the year		10,747	(13,484)
Depreciation and amortisation	9, 19	3,311	3,904
Write-off and disposals of property and equipment	19	(7)	(8,423)
Impairment charge for credit losses - net	8	5,769	17,818
Result of assets available for sale - net		(7,001)	11,887
Other non-cash items		(31,113)	48,110
<b>Operating result before changes in operating assets</b>		<b>(18,294)</b>	<b>59,812</b>
(Increase)/decrease in assets with the Croatian National Bank		8,794	6,313
(Increase)/decrease in loans and advances to customers		1,895	(37,210)
(Increase)/decrease in bills of exchange		796	1,660
(Increase)/decrease in repossessed and other assets		(14,163)	(2,159)
Increase/(decrease) in deposits from customers		26,696	(56,287)
Increase/(decrease) in hybrid instruments		19,669	(43,357)
Increase/(decrease) in other liabilities		10,008	(2,019)
<b>Net cash outflow from operating activities</b>		<b>35,401</b>	<b>(73,247)</b>
<b>Cash flow from investing activities</b>			
Purchase of property and equipment and intangible assets	19	(1,559)	(3,319)
Purchase of available-for-sale financial assets	17	(165,747)	(113,433)
Disposal of available-for-sale financial assets	17	167,034	105,725
<b>Net cash outflow from investing activities</b>		<b>(272)</b>	<b>(11,027)</b>
<b>Cash flow from financing activities</b>			
Contributions in equity	27	-	42,750
Increase/(decrease) of deposits from banks		21,986	(21,152)
Increase/(decrease) in bank borrowings		(10,476)	(7,030)
<b>Net cash inflow from financing activities</b>		<b>11,510</b>	<b>14,568</b>
<b>Net (decrease)/increase in cash and cash equivalents</b>		<b>46,639</b>	<b>(69,706)</b>
Cash and cash equivalents at the beginning of the financial year		168,083	237,789
<b>Cash and cash equivalents at end of year</b>	28	<b>214,722</b>	<b>168,083</b>

*The notes to the financial statements are an integral part of the Statement of cash flows.*

## Notes to the financial statements

for the year from 1 January to 31 December 2015

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### 1. General information

#### Activities

BANKA KOVANICA d.d. Varaždin (the Bank) was incorporated in 1997 and registered at the Commercial Court in Varaždin. The address of the Bank's registered office is in Varaždin, Preradovićeve 29.

The Bank's registered activities are as follows:

- accepting cash deposits
- granting loans and other placements in its own name and for its own account
- issuing electronic money
- issuing guarantees and other warranties
- factoring
- finance lease
- credit operations, including consumer credit, mortgage loans and financing of commercial operations (including forfeiting)
- trading in its own name and for its own account or in its own name and for a customer's account: in money market instruments and other transferable securities, foreign currencies including foreign exchange activities
- trading in financial forward contracts and options, currency and interest instruments
- performing local and international payments
- collection of data, conducting analyses and providing information on the creditworthiness of legal and natural persons who conduct business activities on their own
- representation in the sale of insurance policies, in accordance with the law regulating insurance, intermediation and representation in insurance activities
- issuing and managing instruments of payment, intermediation in concluding financial deals.

**Notes to the financial statements (continued)**for the year from 1 January to 31 December 2015

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***Supervisory Board***

Fabiomassimo Mango	President
Ivan Majdak	Vice president
Emanuele Restelli Prandoni Della Fratta	Member
Albani Marino	Member
Mladen Vedriš	Member

***Management Board***

Nicola Ceccaroli	President
Ivan Majdak	Deputy member from 1 June 2015 to 11 June 2015
Darko Kosovec	Member

The Bank is subject to the regulatory requirements of the Croatian National Bank. These regulations include limits and other restrictions pertaining to minimum capital adequacy requirements, classification of loans and off-balance sheet commitments and provisioning to cover credit risk, liquidity, interest rate and foreign currency positions.

## **Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

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### **2. Basis of presentation of financial statements**

The principal accounting policies applied in the preparation of these financial statements are summarised below. Where specific accounting policies are aligned with the accounting principles set out in International Financial Reporting Standards (IFRS), reference may be made to certain Standards in describing the accounting policies of the Bank; unless otherwise stated, these references are to Standards applicable in the European Union as at 31 December 2015.

#### **2.1. Compliance with Croatian bank accounting requirements and IFRS**

The financial statements have been prepared in accordance with statutory accounting requirements for banks in Croatia. The Bank's operations in Croatia are subject to the Credit Institutions Act, in accordance with which the Bank's financial reporting is regulated by the Croatian National Bank (CNB) which is the central monitoring institution of the banking system in Croatia. These financial statements have been prepared in accordance with these banking regulations.

The main difference between the requirements of the International Financial Reporting Standards (IFRS) and of CNB relates to the recognition of impairment losses of financial assets calculated on a portfolio basis. In accordance with CNB regulations, banks domiciled in Croatia should recognise impairment on the portfolio basis by the prescribed rates on balance sheet and off-balance sheet exposure to credit risk of counterparties for which impairment on individual basis is not determined, while IFRS requires that the provisions on the portfolio basis should be determined for existing but unidentified losses on the basis of valuation models taking into account individual characteristics of the Bank and the counterparty in the portfolio (e.g. collateral, customers' scoring, etc.).

The Bank calculates impairment losses on corporate lending as the present value of expected future cash flows, discounted at the instrument's original effective interest rate, in accordance with IFRS. CNB requires the amortisation of the calculated discount to be presented in the income statement within the movement in impairment losses on loans and advances to customers and other assets, rather than as interest income, as required by International Financial Reporting Standards.

Additionally, CNB prescribes the minimum levels of impairment losses against certain specifically identified impaired exposures, which may be different from the impairment loss required to be recognised in accordance with IFRS.

#### **2.2. Basis of preparation**

The financial statements are presented in thousands of Croatian kuna (HRK), unless otherwise stated.

The financial statements have been prepared on the accrual basis of accounting, under the going concern assumption.

The financial statements are prepared on the historical or amortised cost basis, except for available-for-sale financial assets, which are recorded at fair value. Other financial assets and liabilities, and non-monetary assets and liabilities, are stated at amortised or historical cost, less impairment, where appropriate.

The accounting policies adopted are consistent with those of the previous financial year unless otherwise stated and disclosed.

## Notes to the financial statements (continued)

for the year from 1 January to 31 December 2015

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### **Standards and interpretations issued and effective:**

The Bank has adopted the following new and amended standards for their annual reporting period commencing 1 January 2015 which were endorsed by the European Union and which are relevant for the Bank's financial statements:

- *Annual Improvements to IFRSs – 2010 – 2012 Cycle comprising changes to seven standards (IFRS 1, IFRS 3, IFRS 8, IFRS 13, IAS 16, IAS 28 and IAS 24).*
- *Annual Improvements to IFRSs – 2011 – 2013 Cycle comprising changes to four standards (IFRS 2, IFRS 3, IFRS 13 and IAS 40).*
- *Defined Benefit Plans: Employee Contributions - Amendments to IAS 19*

The adoption of the improvements did not have any impact on the current period or any prior period and is not likely to affect future periods.

### **Standards and interpretations issued but not yet effective:**

Certain new standards and interpretations have been published that are not mandatory for 31 December 2015 reporting periods and have not been early adopted by the group. None of these is expected to have significant effect on the Bank's financial statements, except for the following standards:

- *IFRS 9 Financial instruments and associated amendments to various other standards (effective for annual periods beginning on or after 1 January 2018)*

The complete version of IFRS 9 replaces most of the guidance in IAS 39. IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortised cost, fair value through OCI and fair value through P&L. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. Investments in equity instruments are required to be measured at fair value through profit or loss with the irrevocable option at inception to present changes in fair value in OCI. There is now a new expected credit losses model that replaces the incurred loss impairment model used in IAS 39. For financial liabilities there were no changes to classification and measurement except for the recognition of changes in own credit risk in other comprehensive income, for liabilities designated at fair value, through profit or loss. IFRS 9 relaxes the requirements for hedge effectiveness by replacing the bright line hedge effectiveness tests. It requires an economic relationship between the hedged item and hedging instrument and for the 'hedged ratio' to be the same as the one that the Management Board actually uses for risk management purposes. Adequate documentation is still required but is different to that currently prepared under IAS 39. The Bank plans to adopt this new standard on the effective date as of and when adopted by EU. The Bank is still assessing the impact of this standard.

- *IFRS 15 Revenue from contracts with customer and associated amendments to various other standards (effective for annual periods beginning on or after 1 January 2018)*

The IASB has issued a new standard for the recognition of revenue. This will replace IAS 18 which covers contracts for goods and services and IAS 11 which covers construction contracts.

## Notes to the financial statements (continued)

for the year from 1 January to 31 December 2015

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The new standard is based on the principle that revenue is recognised when control of a good or service transfers to a customer – so the notion of control replaces the existing notion of risks and rewards.

Key changes to current practice are:

- Any bundled goods or services that are distinct must be separately recognised, and any discounts or rebates on the contract price must generally be allocated to the separate elements
- Revenue may be recognised earlier than under current standards if the consideration varies for any reasons (such as for incentives, rebates, performance fees, royalties, success of an outcome etc) – minimum amounts must be recognised if they are not at significant risk of reversal)
- The point at which revenue is able to be recognised may shift: some revenue which is currently recognised at a point in time at the end of a contract may have to be recognised over the contract term and vice versa
- There are new specific rules on licenses, warranties, non- refundable upfront fees and, consignment arrangements, to name a few; and
- As with any new standard, there are also increased disclosures.

Entities will have a choice of full retrospective application, or prospective application with additional disclosures. The Bank is currently assessing the impact of the amendments on their financial statements, but do not expect any impact. The Bank plans to adopt this amendment on its effective date.

- *IFRS 16 “Leases” (issued in January 2016 and effective for annual periods beginning on or after 1 January 2019)*

The new standard sets out the principles for the recognition, measurement, presentation and disclosure of leases. All leases result in the lessee obtaining the right to use an asset at the start of the lease and, if lease payments are made over time, also obtaining financing. Accordingly, IFRS 16 eliminates the classification of leases as either operating leases or finance leases as is required by IAS 17 and, instead, introduces a single lessee accounting model. Lessees will be required to recognize: a) assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value, and b) depreciation of lease assets separately from interest on lease liabilities in the income statement. IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. The Bank is currently assessing the impact of the amendments on its financial statements.

## **Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

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### **2.3. Critical accounting judgements and key sources of estimation uncertainty**

In the application of the Bank's accounting policies, the Management Board is required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing 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 the revision and future periods if the revision affects both current and future periods.

The key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below.

While it is possible that in particular periods the Bank may sustain losses, which are substantially relative to the allowance for impairment losses, it is the judgement of the Management Board that the allowance for impairment losses is adequate to absorb losses incurred on the risk assets.

There are several legal actions against the Bank, which have arisen from the regular course of its operations. The Bank's Management Board believes that the probable outcome will have no significant negative effects on the Banks' financial position or its future operating results.

### **3. Summary of significant accounting policies**

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

#### **3.1. *Interest income and expense***

Interest income is accrued on a time-basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

Interest income includes coupons earned on fixed income investments and securities and accrued discount and premium on treasury bills and other discounted instruments.

When loans become impaired, they are written down to their recoverable amounts and interest income thereafter is recognized based on the rate of interest that was used to discount the future cash flows for the purpose of measuring the recoverable amount.

## **Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

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### **3.2. Fee and commission income and expense**

Fees and commissions consist mainly of fees on domestic and foreign payments, fees for issuing guarantees and letters of credit, fees and commissions on card operations and other credit instruments issued by the Bank. Fees and commissions are generally recognized as income when service is provided. Loan origination fees for loans which are probable of being drawn down are deferred (together with the related direct issue costs) and recognized as an adjustment to the effective yield of the loan, and thus adjust the interest income.

### **3.3. Taxation**

The tax expense represents the sum of the tax currently payable and deferred tax.

The current tax liability is based on taxable profit for the year. Taxable profit differs from profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Bank's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered. Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised. Deferred tax is recognised as an expense or income in profit or loss, except when it relates to items credited or debited directly to equity, in which case the deferred tax is also recognised directly in equity. Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the Bank has the ability and intention to settle its current tax asset and liability on a net basis.

### **3.4. Segment reporting**

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns different from those of segments operating in other economic environments.



## Notes to the financial statements (continued)

for the year from 1 January to 31 December 2015

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### 3.5. Foreign currency translation

#### *(a) Functional and presentation currency*

Items included in the financial statements of the Bank are measured using the currency of the primary economic environment in which the Bank operates (the functional currency). The Bank's financial statements are presented in Croatian kuna (HRK), which is the Bank's functional currency and presentation currency.

#### *(b) Transactions and balances*

Transactions denominated in foreign currencies are translated into HRK at the prevailing exchange rates on the date of the transaction.

Monetary items denominated in foreign currencies are retranslated into HRK at the appropriate spot rates of exchange prevailing at the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on their retranslation, are included in 'Foreign exchange differences - net' for the period. Exchange differences arising on the retranslation of non-monetary assets carried at fair value are included in profit or loss for the period except for exchange differences arising on the retranslation of non-monetary assets available-for-sale in respect of which gains and losses are recognized directly in equity. For such non-monetary items, any exchange component of that gain or loss is also recognized directly in equity.

The Bank has assets and liabilities originated in HRK, which are linked to a foreign currency clause. Due to this clause the Bank has to revalue both the asset and related liability by higher of: foreign exchange rate valid as at the date of maturity, or foreign exchange rate valid as at the date of origination of the financial instrument. In case of liability linked to this clause, the counterparty has the same option. As such, the Bank values its assets and liabilities related to this clause by the middle exchange rate of CNB valid at the balance sheet date or by the exchange rate agreed by the option (rate valid at origination), whichever is higher.

The principal rates of exchange set forth by CNB and used in the preparation of the Bank's balance sheet at the reporting dates were as follows:

31 December 2015	EUR 1 = HRK 7.635047	USD 1 = HRK 6.991801
31 December 2014	EUR 1 = HRK 7.661471	USD 1 = HRK 6.302107

### 3.6. Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise cash on hand, balances with CNB, balances with banks on giro accounts and term deposits with other banks with remaining maturities of three months or less.

Cash and cash equivalents exclude the obligatory reserves with CNB as these funds are not available for the Bank's day to day operations. The obligatory reserve with CNB is a required reserve to be held by all commercial banks licensed in Croatia.

## Notes to the financial statements (continued)

for the year from 1 January to 31 December 2015

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### 3.7. Financial assets

Financial assets held by the Bank are categorized into portfolios in accordance with the Bank's intent on acquisition and pursuant to the Bank's investment strategy. Financial assets and liabilities are classified as 'at fair value through profit or loss', 'held to maturity', 'available for sale' or as 'loans and receivables'. The principal difference among the portfolios relates to the measurement of financial assets and the recognition of their fair values in the financial statements.

All financial assets and liabilities are recognized and derecognized on a settlement date basis, where the purchase or sale of a financial asset or liability is under a contract whose terms require delivery of the financial asset within the timeframe established by the market concerned.

When a financial asset or financial liability is recognized initially, the Bank measures it at its fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

#### (a) Financial assets at fair value through profit or loss

Financial assets are classified at fair value through profit or loss where the financial assets are held for trading.

A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling in the near future; or
- it is a part of an identified portfolio of financial instruments that the Bank manages and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

#### Measurement:

Financial assets at fair value through profit or loss are initially accounted at fair value and related transaction costs are recorded as an expense. Subsequent to the initial recognition, financial assets at fair value through profit or loss are accounted for and stated at fair value which approximates the price quoted on recognised stock exchanges or acceptable valuation models. The Bank includes unrealised gains and losses in 'Result of trading assets - net'. Interest earned on assets at fair value through profit or loss representing coupons on debt securities is accrued on a daily basis and reported as 'Interest income' in the income statement.

Dividends on trading securities are recorded when declared and included as a receivable in the balance sheet line 'Other assets' and in 'Other operating income' in the income statement.

All purchases and sales of securities held for trading that require delivery within the time frame established by regulation or market convention ('regular way' purchases and sales) are recognized as spot transactions. Transactions that do not meet the 'regular way' settlement criterion are treated as financial derivatives.

## Notes to the financial statements (continued)

for the year from 1 January to 31 December 2015

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### **(b) Assets available for sale**

Available-for-sale financial assets are those non-derivative financial assets that are designated as available for sale or are not classified as: (a) loans and receivables, (b) held-to-maturity investments or (c) financial assets at fair value through profit or loss.

This portfolio comprises equity and debt securities. Subsequent to initial recognition, available-for-sale financial assets are re-measured at fair value based on quoted prices or amounts derived from cash flow models.

In circumstances where the quoted market prices are not readily available, the fair value of debt securities is estimated using the present value of future cash flows and the fair value of unquoted equity instruments is estimated using applicable price/earnings or price/cash flow ratios refined to reflect specific circumstances of the issuer.

For available-for-sale assets, gains and losses arising from changes in fair value are recognised directly in equity under the caption 'Reserves', until the security is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognized in equity is included in the profit or loss for the period.

The Bank assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity investments classified as available for sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the income statement.

Impairment losses recognized in profit or loss for equity investments classified as available-for-sale are not subsequently reversed through profit or loss. Impairment losses recognised in profit or loss for debt instruments classified as available-for-sale are subsequently reversed if an increase in the fair value of the instrument can be objectively related to an event occurring after the recognition of the impairment loss.

Interest earned whilst holding available-for-sale securities is accrued on a daily basis using the effective interest rate method and reported as "Interest income" in the income statement.

Foreign exchange differences related to available-for-sale equity instruments held in foreign currency are reported together with fair value gains and losses in equity until the financial asset is sold. Foreign exchange differences related to available-for-sale debt instruments held in foreign currency are reported in the income statement.

Dividends on securities available for sale are recorded as declared and included as a receivable in the balance sheet line 'Other assets' and in 'Other operating income' in the income statement. Upon payment of the dividend, the receivable is offset against the collected cash.

## **Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

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### **(c) Held-to-maturity investments**

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Bank's Management Board has the positive intention and ability to hold to maturity. Held-to-maturity investments are carried at amortised cost using the effective interest method, less any allowance for impairment.

The Bank assess on a regular basis whether there is an objective evidence that an investment held to maturity may be impaired. A financial assets is impaired if its carrying amount is greater than its recoverable amount which is equal to the present value of the expected future cash flows

discounted at the financial instrument's original effective interest rate. The amount of impairment loss for assets carried at amortised cost is calculated as the difference between the asset's carrying amount and the present value of the expected future cash flows discounted at the financial instrument's original effective interest method. When an impairment of assets is identified, the Bank recognises allowances through the income statement.

Impairment losses are reversed in subsequent periods when an increase in the recoverable amount can be related objectively to an event occurring after the impairment was recognised, with the restriction that the carrying amount of the investment at the date the impairment is reversed shall not exceed the amount of the amortised cost that would have been recorded, had the impairment not been recognised.

### **(d) Loans and receivables**

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than: (a) those that the Bank intends to sell immediately or in the near term, which shall be classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss; (b) those that the Bank upon initial recognition designates as available for sale; or (c) those for which the Bank may not recover substantially all of its initial investment, other than because of credit deterioration, which shall be classified as available for sale.

This portfolio comprises loans provided to customers.

Loans and receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. Third party expenses, such as legal fees, incurred in securing a loan are treated as part of the cost of the transaction as well as fees received from customers. Loan origination fees for loans which are probable of being drawn down, are deferred (together with related direct costs) and recognized as an adjustment to the effective yield of the loan and as such adjust the interest income.

The Bank assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a loss event) and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

## Notes to the financial statements (continued)

for the year from 1 January to 31 December 2015

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The criteria that the Bank uses to determine that there is objective evidence of an impairment loss include:

- Delinquency in contractual payments of principal or interest;
- Cash flow difficulties experienced by the borrower (for example, equity ratio, net income percentage of sales);
- Breach of loan covenants or conditions;
- Initiation of bankruptcy proceedings;
- Deterioration of the borrower's competitive position;
- Deterioration in the value of collateral; and
- Downgrading below investment grade level.

### (e) Financial liabilities

Financial liabilities of the Bank such as 'Due to banks', 'Deposits from customers', are recognised initially at fair value net of transaction cost incurred. Financial liabilities are subsequently measured at amortized cost using the effective interest method. Interest expense arising on the issue of certificated debts is included in the income statement line 'Interest expense'.

### 3.8. Financial guarantee contracts

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument. Such financial guarantees are given to banks, financial institutions and other bodies on behalf of customers to secure loans, overdrafts and other banking products.

Financial guarantees are initially recognised in the financial statements at fair value on the date the guarantee was given. Subsequent to initial recognition, the bank's liabilities under such guarantees are measured at the higher of the initial measurement, less amortisation calculated to recognise in the income statement the fee income earned on a straight-line basis over the life of the guarantee and the best estimate of the expenditure required to settle any financial obligation arising at the balance sheet date. These estimates are determined based on experience of similar transactions and history of past losses, supplemented by the judgement of the Management Board.

Any increase in the liability relating to guarantees is recognised in the income statement under other operating expenses.

### 3.9. Derivative financial instruments

Derivative financial instruments include foreign exchange rate forward contracts and are initially recognised in the balance sheet at fair value and subsequently re-measured at their fair value. Fair values are obtained from quoted market prices or pricing models as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

Derivative financial instruments include contracts with one-way currency clause. The contracted value is initially recognised in the off-balance-sheet records and as a loan given with a one-way currency clause in the balance sheet. They are subsequently measured at amortised cost as for all other placements that carry credit risk in the balance sheet. Increase in exchange rates (fair value of the embedded derivative) above the contracted, is recorded in the balance sheet as an embedded derivative and recognised within profit or loss from embedded derivatives in the income statement.

## Notes to the financial statements (continued)

for the year from 1 January to 31 December 2015

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The Bank's derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in the income statement under net trading income. However, the gains and losses arising from changes in the fair value of derivatives that are managed in conjunction with designated financial assets or financial liabilities are included in 'net income from financial instruments designated at fair value'.

### 3.10. Sale and repurchase agreements

If a financial asset is sold under an agreement to repurchase it at a fixed price or at the sale price plus a lender's return or if it is loaned under an agreement to return it to the transferor, it is not derecognized as the Bank retains substantially all the risks and rewards of ownership.

### 3.11. Offsetting of financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

### 3.12. Non-current tangible and intangible assets

Non-current tangible and intangible assets are recorded at cost less accumulated depreciation/amortisation. Depreciation/amortisation is calculated on a straight-line basis to write down the cost of such assets to their residual values over their estimated useful lives. Assets under construction are not depreciated.

Depreciation of other assets is calculated using the straight-line method to allocate their cost over their estimated useful lives, as follows:

	2015	2014
	%	%
Property	2.5	2.5
Leasehold improvements	20	20
Electronic equipment	20	20
Other assets	20-25	20-25
Software	20	20
Leasehold improvements	20	20

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. In addition, the carrying amounts of non-current tangible and intangible assets are reviewed at each balance sheet date to assess whether they are recorded in excess of their recoverable amounts. Where the carrying amount of an asset exceeds its estimated recoverable amount, it is written down immediately to its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. An impairment is recognized in the respective period and is included in operating expenses. After the recognition of an impairment loss the depreciation charge for fixed assets is adjusted in future periods to allocate the assets' revised carrying value, less its residual value (if any), on a systematic basis over its remaining useful life.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the income statement.

## **Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

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### **3.13. Leases**

The leases entered into by the Bank are operating leases. The total payments made under operating leases are charged to other operating expenses in the income statement on a straight-line basis over the period of the lease. When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which the termination takes place.

### **3.14. Non-current assets held for sale**

Non-current assets are classified as assets held for sale and stated at the lower of carrying amount and fair value less costs to sell if their carrying amount is recovered principally through a sale transaction rather than through continuing use.

### **3.15. Provisions**

Provisions are recognised when: the Bank has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. The Management Board determines the adequacy of the provision based upon reviews of individual items, recent loss experience, current economic conditions, the risk characteristics of the various categories of transactions and other pertinent factors at the balance sheet date. If the effect is material, provisions are discounted to the present value.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

### **3.16 Employee benefits**

The Bank has no post-retirement benefit plans for its employees or management. The Bank makes contributions on behalf of its employees to mandatory state pension plans, which are charged as expense in the period to which they relate. Any future payments to employees are the responsibility of the Republic of Croatia.

### **3.17. Borrowings**

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities, unless the Bank has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

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**3.18. Fiduciary activities**

Assets and income arising thereon, together with related undertakings to return such assets to customers, are excluded from these financial statements when the Bank acts in a fiduciary capacity such as nominee, trustee or agent.

**3.19. Share capital and treasury shares**

External costs directly attributable to the issuance of new shares, except for those resulting from business combinations, are deducted from the equity, net of any related taxes.

When the Bank or its associates purchase or become entitled to purchase its share capital, the consideration paid, including all transaction costs less any taxes, is presented as a deduction from the total equity. Gains and losses on the sale of treasury shares are credited and charged, respectively, to treasury shares within equity. The acquisition of treasury shares is recognised within capital at the trade date.



**Notes to the financial statements (continued)**  
for the year from 1 January to 31 December 2015

**4. Net interest income**

**Interest income**

	<b>2015</b>	<b>2014</b>
	<b>HRK'000</b>	<b>HRK'000</b>
Loans and advances:		
- to customers	76,409	74,545
- to banks	3,393	2,791
Securities	1,343	1,134
	<b>81,145</b>	<b>78,470</b>

**Interest expense**

	<b>2015</b>	<b>2014</b>
	<b>HRK'000</b>	<b>HRK'000</b>
Customers deposits	27,323	34,481
Hybrid instruments	1,224	649
Other borrowed funds	968	1,231
	<b>29,515</b>	<b>36,361</b>

**5. Net fee and commission income**

**Fee and commission income**

	<b>2015</b>	<b>2014</b>
	<b>HRK'000</b>	<b>HRK'000</b>
Payment transactions	3,340	3,209
Guarantees and letter of credits given	42	3
Other	3,266	2,711
	<b>6,648</b>	<b>5,923</b>

**Fee and commission expense**

	<b>2015</b>	<b>2014</b>
	<b>HRK'000</b>	<b>HRK'000</b>
Payment transactions	372	430
Other	1,093	849
	<b>1,465</b>	<b>1,279</b>

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

**6. Foreign exchange differences – net**

	<b>2015</b> <b>HRK'000</b>	<b>2014</b> <b>HRK'000</b>
Net foreign exchange gains on foreign exchange dealing	2,651	2,924
Foreign exchange gains/(losses) on translation of balance sheet items to middle exchange rate	(968)	(1,229)
	<b>1,683</b>	<b>1,695</b>

**7. Other operating income**

	<b>2015</b> <b>HRK'000</b>	<b>2014</b> <b>HRK'000</b>
Gain from transfer of receivables	-	9
Court costs refund	161	117
Other	1,386	3,067
	<b>1,547</b>	<b>3,193</b>

**8. Impairment charge for credit losses - net**

	<b>2015</b> <b>HRK'000</b>	<b>2014</b> <b>HRK'000</b>
Loans and advances to customers (Note 16)	7,214	17,584
Collected receivables written off in previous years	(379)	(541)
Held-to-maturity financial assets (Note 18)	(698)	(2)
Other assets (Note 21)	(368)	828
Provision for contingent liabilities and commitments (Note 26)	-	(51)
	<b>5,769</b>	<b>17,818</b>

**9. Administrative expenses**

	<b>2015</b> <b>HRK'000</b>	<b>2014</b> <b>HRK'000</b>
<b>Staff costs</b>		
Net salaries	10,806	12,353
Pension insurance contributions	2,946	3,516
Health insurance contributions	2,931	3,211
Other contributions and taxes on salaries	2,615	3,380
Other staff costs	1,048	924
	<b>20,346</b>	<b>23,384</b>
Other administrative expenses	13,543	17,586
Depreciation and amortisation (Note 19)	3,311	3,904
	<b>37,200</b>	<b>44,874</b>

As at 31 December 2015, the Bank had 111 employees (2014: 117 employees).

**10. Other operating expenses**

	<b>2015</b> <b>HRK'000</b>	<b>2014</b> <b>HRK'000</b>
Rental costs	2,225	1,973
Deposits insurance charge	2,976	3,041
Provisions for legal disputes	(170)	(198)
Accrued unused vacation	77	(246)
Other	1,479	41
	<b>6,587</b>	<b>4,611</b>

**11. Income tax**

	<b>2015</b> <b>HRK'000</b>	<b>2014</b> <b>HRK'000</b>
<b>Accounting loss before tax</b>	<b>10,747</b>	<b>(13,484)</b>
Effect of items increasing tax base	5,703	9,360
Effect of items decreasing tax base	(5,628)	(7,053)
<b>Tax gain/(loss)</b>	<b>10,822</b>	<b>(11,177)</b>
Income tax at 20%	2,149	-
Effect of tax losses carried forward	(2,149)	-
<b>Income tax</b>	<b>-</b>	<b>-</b>
<b>Effective tax rate</b>	<b>-</b>	<b>-</b>

Movement of tax losses carried forward was as follows:

	<b>2015</b> <b>HRK'000</b>	<b>2014</b> <b>HRK'000</b>
<b>Tax losses carried forward from the previous period</b>	<b>(213,754)</b>	<b>(242,353)</b>
Utilisation of tax losses	10,822	-
Expiration of tax losses carried forward	65,957	39,776
<b>Tax loss available for carry forward in future periods</b>	<b>(136,975)</b>	<b>(213,754)</b>
Deferred tax assets at 20%	27,395	42,751
Recognized deferred tax assets (Note 21)	5,463	5,463
Unrecognised deferred tax assets	21,932	37,288

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

Movements in deferred tax assets were as follows:

	<b>2015</b> <b>HRK'000</b>	<b>2014</b> <b>HRK'000</b>
<b>At 1 January</b>	<b>5,463</b>	<b>5,463</b>
Reversal of unrecognised deferred tax assets	(2,164)	-
Recognition of deferred tax assets	2,164	-
<b>At 31 December</b>	<b>5,463</b>	<b>5,463</b>

In 2015, the Bank utilised a portion of its deferred tax assets, i.e. The portion of tax losses carried forward used to settle the current income tax charge. The Bank also recognised deferred tax assets in the same amount on the basis of the conservative estimate of future period planned profits expected to be realised. The Bank has not recognised deferred tax assets in the further amount of HRK 21,932 thousand in the progress of adopting the new 5-year plan.

The Bank may utilise the recorded tax loss in the amount of HRK 136,975 thousand not later than in a period of 5 years:

- tax loss for 2011 in the amount of HRK 19,276 thousand not later than (including) 2017
- tax loss for 2012 in the amount of HRK 63,235 thousand not later than (including) 2018
- tax loss for 2013 in the amount of HRK 43,287 thousand not later than (including) 2019
- tax loss for 2014 in the amount of HRK 11,177 thousand not later than (including) 2020

In accordance with local regulations, the Tax Administration may at any time inspect the Bank's books and records within 3 years following the year in which the tax liability is reported and may impose additional tax liabilities and penalties. The Bank's Management Board is not aware of any circumstances, which may give rise to a potential material liability in this respect.

**12. Earnings/(loss) per share****Basic**

Basic earnings per share are calculated by dividing the net loss for the year by the weighted average number of existing shares (ordinary) for the period, excluding treasury shares.

	<b>2015</b>	<b>2014</b>
Profit/(loss) for the year (in HRK'000)	10,747	(13,484)
Weighted average number of shares in issue excluding treasury	3,338,344	3,249,339
Basic earnings/(loss) per share – ordinary (in HRK)	<b>3.22</b>	<b>(4.15)</b>

**Diluted**

Diluted earnings/loss per share for 2015 and 2014 is equal to basic loss per share, since the Bank did not have any convertible instruments or options outstanding during either period.

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

**Cash on hand and balances with banks**

	<b>31 December 2015 HRK'000</b>	<b>31 December 2014 HRK'000</b>
Cash on hand	16,295	15,677
Cash on the clearing account	65,916	41,452
Foreign currency account	93,287	71,641
	<b>175,498</b>	<b>128,770</b>

**13. Obligatory reserve with the Croatian National Bank**

	<b>31 December 2015 HRK'000</b>	<b>31 December 2014 HRK'000</b>
Earmarked obligatory reserve		
- in HRK	68,904	67,228
- in foreign currency	13,850	13,461
CNB treasury notes	-	10,859
	<b>82,754</b>	<b>91,548</b>

The obligatory reserve rate as at 31 December 2015 was 12% of HRK and foreign currency deposits, loans taken and debt securities issued (31 December 2014: 12%). On 30 September 2015, pursuant to the Decision on revoking Decision on purchasing compulsory CNB bills, the banks' obligation to purchase and keep with CNB compulsory CNB bills has been repealed. The Decision entered into force on 7 October 2015; thus, CNB paid for the entire purchased amount of compulsory bills.

**14. Placements with banks**

	<b>31 December 2015 HRK'000</b>	<b>31 December 2014 HRK'000</b>
Loans	5,138	5,138
Deposits	39,225	39,313
	<b>44,363</b>	<b>44,451</b>
Provision for identified losses	(5,138)	(5,138)
	<b>39,225</b>	<b>39,313</b>

Movement in the provision for identified losses:

	<b>31 December 2015 HRK'000</b>	<b>31 December 2014 HRK'000</b>
<b>At 1 January</b>	<b>5,138</b>	<b>5,138</b>
Additional provisions (Note 8)	-	-
Collected amounts (Note 8)	-	-
<b>At 31 December</b>	<b>5,138</b>	<b>5,138</b>

**Notes to the financial statements (continued)**  
for the year from 1 January to 31 December 2015

**15. Loans and advances to customers**

	<b>31 December 2015</b>	<b>31 December 2014</b>
	<b>HRK'000</b>	<b>HRK'000</b>
Retail customers	643,936	597,363
Corporate customers	310,215	360,748
<b>Gross loans and advances</b>	<b>954,151</b>	<b>958,111</b>
Less: Provisions for impairment	(213,239)	(208,090)
<b>Net loans and advances</b>	<b>740,912</b>	<b>750,021</b>
Current portion	105,100	136,060
Non-current portion	635,812	613,961

The movements in the provisions for impairment on loans and advances to customers is as follows:

<b>2015</b>	<b>Retail HRK'000</b>	<b>Corporate HRK'000</b>	<b>Total HRK'000</b>
<b>At 1 January</b>	<b>35,781</b>	<b>172,309</b>	<b>208,090</b>
Additional provisions (Note 8)	17,528	36,746	54,274
Collected amounts (Note 8)	(13,482)	(33,578)	(47,060)
Write-off	(135)	(1,711)	(1,846)
Foreign exchange differences	6	(226)	(220)
<b>At 31 December</b>	<b>39,698</b>	<b>173,540</b>	<b>213,238</b>
<b>2014</b>	<b>Retail HRK'000</b>	<b>Corporate HRK'000</b>	<b>Total HRK'000</b>
<b>At 1 January</b>	<b>31,967</b>	<b>166,355</b>	<b>198,322</b>
Additional provisions (Note 8)	25,936	45,895	71,831
Collected amounts (Note 8)	(22,068)	(32,179)	(54,247)
Write-off	(166)	(8,013)	(8,179)
Foreign exchange differences	112	251	363
<b>At 31 December</b>	<b>35,781</b>	<b>172,309</b>	<b>208,090</b>

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

**16. Available-for-sale financial assets**

	<b>31 December 2015</b>	<b>31 December 2014</b>
	<b>HRK'000</b>	<b>HRK'000</b>
Bonds and treasury bills	62,477	69,755
Corporate bonds	2,152	2,179
Equity securities – listed	592	549
Equity securities – unlisted	141	141
	<b>65,362</b>	<b>72,624</b>

Movements in available-for-sale financial assets may be summarised as follows:

	<b>31 December 2015</b>	<b>31 December 2014</b>
	<b>HRK'000</b>	<b>HRK'000</b>
<b>At 1 January</b>	<b>72,624</b>	<b>62,915</b>
Additions	165,747	113,433
Disposals	(167,034)	(105,725)
Unrealised (loss)/gain	(161)	1,802
Result of assets available for sale - net	261	2,178
Interest payment	4,426	2,292
Foreign exchange differences	(10,501)	(4,271)
<b>At 31 December</b>	<b>65,362</b>	<b>72,624</b>

**Bonds and treasury bills as at 31 December 2015:**

<b>Name</b>	<b>Maturity</b>	<b>Nominal amount (in thousands)</b>	<b>Currency</b>	<b>Carrying amount</b>	<b>Unrealised gains/(losses)</b>
				<b>HRK'000</b>	<b>HRK'000</b>
XS0757376610	21 March 2022	500	EUR	4,367	(42)
US857524AC63	22 January 2024	500	USD	3,735	(118)
XS0982708926	18 February 2019	200	USD	1,493	14
HRRHMFT632X5	11 August 2016	7,000	EUR	52,882	-
				<b>62,477</b>	<b>(146)</b>

As at 31 December 2015, there were no bonds pledged as collateral in repurchase agreements.

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

**Corporate bonds of other companies as at 31 December 2015:**

Name	Maturity	Nominal amount (in thousands)	Currency	Carrying amount	Unrealised gains/(losses)
				HRK'000	HRK'000
ATGR-O-169A	20 September 2016	2,000	HRK	2,152	116
				<b>2,152</b>	<b>116</b>

**17. Held-to-maturity financial assets**

	31 December 2015	31 December 2014
	HRK'000	HRK'000
Bills of exchange	1,977	2,773
	<b>1,977</b>	<b>2,773</b>
Provision for identified losses	(1,067)	(1,765)
	<b>910</b>	<b>1,008</b>

Movement in the provision for identified losses:

	31 December 2015	31 December 2014
	HRK'000	HRK'000
<b>At 1 January</b>	<b>1,765</b>	<b>1,767</b>
Additional provisions (Note 8)	-	-
Collected amounts (Note 8)	(698)	(2)
Write-off	-	-
<b>At 31 December</b>	<b>1,067</b>	<b>1,765</b>



**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

**18. Property and equipment and intangible assets**

	Land and buildings	Leasehold improvements	Electronic equipment	Other assets	Total property and equipment	Software	Assets under construction	Total intangible assets
<b>Cost</b>	<b>HRK'000</b>	<b>HRK'000</b>	<b>HRK'000</b>	<b>HRK'000</b>	<b>HRK'000</b>	<b>HRK'000</b>	<b>HRK'000</b>	<b>HRK'000</b>
<b>At 1 January 2014</b>	<b>25,138</b>	<b>12,962</b>	<b>9,280</b>	<b>12,264</b>	<b>59,644</b>	<b>8,547</b>	<b>-</b>	<b>8,547</b>
Additions	2,570	18	116	328	3,032	287	-	287
Disposals	(10,474)	-	(62)	(222)	(10,758)	-	-	-
<b>At 31 December 2014</b>	<b>17,234</b>	<b>12,980</b>	<b>9,334</b>	<b>12,370</b>	<b>51,918</b>	<b>8,834</b>	<b>-</b>	<b>8,834</b>
Additions	187	8	67	4	266	563	1,150	1,713
Disposals	-	(419)	(2,762)	(349)	(3,530)	(1,060)	-	(1,060)
<b>At 31 December 2015</b>	<b>17,421</b>	<b>12,569</b>	<b>6,639</b>	<b>12,025</b>	<b>48,654</b>	<b>8,337</b>	<b>1,150</b>	<b>9,487</b>
<b>Accumulated amortisation and</b>								
<b>At 1 January 2014</b>	<b>4,213</b>	<b>8,461</b>	<b>8,799</b>	<b>11,085</b>	<b>32,558</b>	<b>7,132</b>	<b>-</b>	<b>7,132</b>
Amortisation charge for the period	437	2,009	272	587	3,305	599	-	599
Disposals	(2,050)	-	(62)	(223)	(2,335)	-	-	-
<b>At 31 December 2014</b>	<b>2,600</b>	<b>10,470</b>	<b>9,009</b>	<b>11,449</b>	<b>33,528</b>	<b>7,731</b>	<b>-</b>	<b>7,731</b>
Amortisation charge for the period	300	1,766	152	424	2,642	669	-	669
Disposals	-	(279)	(2,755)	(349)	(3,383)	(780)	-	(780)
<b>At 31 December 2015</b>	<b>2,900</b>	<b>11,957</b>	<b>6,406</b>	<b>11,524</b>	<b>32,787</b>	<b>7,620</b>	<b>-</b>	<b>7,620</b>
<b>Net book amount</b>								
<b>At 31 December 2014</b>	<b>14,634</b>	<b>2,510</b>	<b>325</b>	<b>921</b>	<b>18,390</b>	<b>1,103</b>	<b>-</b>	<b>1,103</b>
<b>At 31 December 2015</b>	<b>14,521</b>	<b>612</b>	<b>233</b>	<b>501</b>	<b>15,867</b>	<b>717</b>	<b>1,150</b>	<b>1,867</b>

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

**19. Repossessed collateral**

Movements in repossessed collateral during the year:

	<b>31 December 2015 HRK'000</b>	<b>31 December 2014 HRK'000</b>
<b>At 1 January</b>	<b>37,519</b>	<b>37,975</b>
Additions	983	4,064
Disposals	(634)	(4,520)
<b>At 31 December</b>	<b>37,868</b>	<b>37,519</b>

The Bank's repossessed collateral as at 31 December 2015 included property in the total amount of HRK 5,452 thousand (2014: HRK 6,390 thousand) which was not in the Bank's possession. The Bank took over formal ownership over the property in exchange for outstanding receivables in the process of obtaining physical possession.

**20. Other assets**

	<b>31 December 2015 HRK'000</b>	<b>31 December 2014 HRK'000</b>
Deferred tax assets	5,463	5,463
Receivables for court costs refunds	4,137	4,094
Trade receivables	24,991	9,303
Other prepayments	246	307
Prepaid expenses	185	954
Derivative financial assets	-	325
Other	787	1,228
	<b>35,809</b>	<b>21,674</b>
Provision for identified losses	(8,186)	(8,582)
	<b>27,623</b>	<b>13,092</b>

Movement in the provision for identified losses during the year:

	<b>31 December 2015 HRK'000</b>	<b>31 December 2014 HRK'000</b>
<b>At 1 January</b>	<b>8,582</b>	<b>7,763</b>
Additional provisions (Note 8)	1,577	2,483
Collected amounts (Note 8)	(1,945)	(1,655)
Write-off	(28)	(9)
<b>At 31 December</b>	<b>8,186</b>	<b>8,582</b>

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

**21. Deposits from customers**

Deposits comprise demand deposits and term deposits:

	<b>31 December 2015 HRK'000</b>	<b>31 December 2014 HRK'000</b>
<b>Demand deposits</b>		
Corporate customers	19,114	9,990
Retail customers	99,936	88,749
	<b>119,050</b>	<b>98,739</b>
<b>Term deposits</b>		
Corporate customers	5,843	6,315
Retail customers	875,673	868,816
	<b>881,516</b>	<b>875,131</b>
<b>Deposits from customers</b>	<b>1,000,566</b>	<b>973,870</b>
Current portion	886,716	844,655
Non-current portion	113,850	129,215

**22. Due to banks**

	<b>31 December 2015 HRK'000</b>	<b>31 December 2014 HRK'000</b>
Borrowings:		
- Croatian Bank for Reconstruction and Development	20,877	31,352
Deposits	1,198	23,184
	<b>22,075</b>	<b>54,536</b>
Current portion	1,198	23,184
Non-current portion	20,877	31,352

As at 31 December 2015 and 31 December 2014, all deposits from banks are current.

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

**23. Hybrid instruments**

Hybrid financial instruments represent special term deposits from citizens and legal entities with no option of cancellation prior to maturity, except for the purpose of purchasing shares of the Bank, and which are under certain conditions, prescribed by the Croatian National Bank, calculated within the Bank's regulatory capital.

	31 December 2015 HRK'000	31 December 2014 HRK'000
Legal entities	24,707	14,802
Corporate customers	9,887	-
Retail customers	-	123
	<b>34,594</b>	<b>14,925</b>

**24. Repurchase agreements**

As at 31 December 2015 and 31 December 2014, the Bank did not have any repurchase agreements.

**25. Other liabilities**

	31 December 2015 HRK'000	31 December 2014 HRK'000
Provisions for legal disputes	629	799
Provision for contingent liabilities and commitments	367	368
Payables in the course of settlement	11,729	2,483
Trade payables	2,240	1,697
Employee payables – salaries and contributions	1,633	1,861
Liabilities for deposits insurance charge	743	747
Accrued unused vacation (Note 10)	269	192
Other liabilities + provisions for conversion	2,100	1,555
	<b>19,710</b>	<b>9,702</b>

Movement in provisions for legal disputes:

	31 December 2015 HRK'000	31 December 2014 HRK'000
<b>At 1 January</b>	<b>799</b>	<b>1,019</b>
Additional provisions	36	282
Release of provisions	(206)	(492)
Payments made per court verdicts	-	(10)
<b>At 31 December</b>	<b>629</b>	<b>799</b>

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

Movement in provisions for contingent liabilities and commitments:

	<b>31 December 2015 HRK'000</b>	<b>31 December 2014 HRK'000</b>
<b>At 1 January</b>	<b>368</b>	<b>419</b>
Additional provisions	1,202	2,350
Release of provisions	(1,202)	(2,401)
<b>At 31 December</b>	<b>368</b>	<b>368</b>

**26. Shareholders' equity****Share capital**

As at 31 December 2015, the Bank's share capital amounted to HRK 333,834 thousand (31 December 2014: HRK 333,834 thousand), and it is divided among 3,338,344 ordinary shares ( 31 December 2014: 3,338,344) (VSK-R-A) with a nominal value of HRK 100 per share.

The Bank's main shareholders as at 31 December were as follows:

<b>Shareholder</b>	<b>31 December 2015</b>		<b>31 December 2014</b>	
	<b>Number of shares</b>	<b>% in share capital</b>	<b>Number of shares</b>	<b>% in share capital</b>
Cassa di Risparmio della Repubblica di San Marino	3,327,461	99.67	3,327,461	99.67
Treasury shares	153	0.01	153	0.01
Other	10,730	0.32	10,730	0.32
<b>Total</b>	<b>3,338,344</b>	<b>100.00</b>	<b>3,338,344</b>	<b>100.00</b>

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

**27. Cash and cash equivalents**

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

	<b>Note</b>	<b>31 December 2015 HRK`000</b>	<b>31 December 2014 HRK`000</b>
Cash on hand and balances with banks	13	175,498	128,770
Placements with banks	15	39,225	39,313
		<b>214,723</b>	<b>168,083</b>

**28. Contingencies and commitments****Legal disputes**

The Bank is currently subject to 10 legal proceedings. As at 31 December 2015, provisions for legal disputes for which the Bank anticipates outflow of economic benefits amount to HRK 628 thousand (2014: HRK 799 thousand). Total contingent liabilities arising from the dispute with the company Prvi Faktor d.o.o. per the instituted enforcement proceedings against the Bank in the amount of EUR 710 thousand as at 31 December 2015 amounted to HRK 10,120 thousand, and the total provisions for contingent liabilities arising from the dispute amounted to HRK 101 thousand. It is a guarantee issued by the Bank in favour of the company Prvi Faktor d.o.o. for the loan payment to the company Glas Istre d.o.o. The first-instance court ruling was issued in the Bank's favour, rejecting the plaintiff's claim.

**Capital commitments**

As at 31 December 2015 and 31 December 2014, the Bank had no capital commitments in respect of purchases of buildings and equipment.

**Loan commitments, guarantees and other financial instruments**

The following table indicates the contractual amounts of the Bank's off-balance sheet financial instruments:

	<b>31 December 2015 HRK`000</b>	<b>31 December 2014 HRK`000</b>
Guarantees	6,686	7,678
Letters of credit	8,277	5,079
Loan commitments and other	21,773	24,004
Less: Provision for contingent liabilities and commitments (Note 26)	-	-
<b>Total</b>	<b>36,736</b>	<b>36,761</b>

**Notes to the financial statements (continued)**for the year from 1 January to 31 December 2015

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The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit, which represent irrevocable assurance that the Bank will make payments in the event that customer cannot meet its obligations to third parties, carry the same credit risks as loans given.

Commitments to lend represent unused portions of authorisations to lend in the form of loans or guarantees. With respect to credit risk on commitments to lend, the Bank is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to lend are contingent upon customers maintaining specific credit standards.

Guarantees and undrawn loan commitments are subject to similar credit risk monitoring and credit policies as utilised in the approval of loans. The Management Board of the Bank believes that the market risk associated with guarantees and undrawn loan commitments is minimal.

**Operating lease commitments where the Bank is the lessee**

The future minimum lease payments receivable from operating leases are as follows:

	<b>31 December 2015 HRK'000</b>	<b>31 December 2014 HRK'000</b>
Up to 1 year	2,060	2,457
From 2 to 5 years	6,368	7,051
Over 5 years	4,113	5,219
<b>Total</b>	<b>12,541</b>	<b>14,727</b>

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

**29. Related party transactions**

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. Related-party transactions are part of the normal course of business.

The Bank considers itself to be an immediately related person to its major shareholders, their subsidiaries, Supervisory and Management Board members and their close family members.

In 2015 and 2014, transactions with related parties were as follows:

	<b>Supervisory Board, Management Board and their related parties</b>	
	<b>2015</b>	<b>2014</b>
	<b>HRK'000</b>	<b>HRK'000</b>
Interest income	52	61
Interest expense	15	6
<b>Loans</b>		
At 1 January	1,432	1,531
Increase	-	-
Decrease	(192)	(99)
<b>At 31 December</b>	<b>1,240</b>	<b>1,432</b>
<b>Deposits received</b>		
At 1 January	1,005	2,343
Increase	448	855
Decrease	(47)	(2,193)
<b>At 31 December</b>	<b>1,406</b>	<b>1,005</b>



**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

	<b>Cassa di Risparmio della Repubblica di San Marino</b>	
	<b>2015</b>	<b>2014</b>
	<b>HRK'000</b>	<b>HRK'000</b>
Interest income	237	142
Other operating income	1	126
Interest expense	(642)	(667)
<b>Given deposits and cash</b>		
At 1 January	19,199	29,053
Increase	19,089	19,173
Decrease	(19,173)	(29,027)
<b>At 31 December</b>	<b>19,115</b>	<b>19,199</b>
<b>Deposits received</b>		
At 1 January	23,154	1,936
Increase	-	21,220
Decrease	(22,073)	(2)
<b>At 31 December</b>	<b>1,081</b>	<b>23,154</b>
<b>Hybrid instruments</b>		
At 1 January	14,802	58,160
Increase	16	14,802
Decrease	-	(58,160)
<b>At 31 December</b>	<b>14,818</b>	<b>14,802</b>

As at 31 December 2015, the exposure towards the majority shareholder amounts to HRK 19,115 thousand, which represents 15.36% of the Bank's regulatory capital (2014: 18.66%, 2013: 23.58%). The regulatory limit exposure to one person or Group of related persons is a maximum of 25% of the regulatory capital of a credit institution.

**Key management and Supervisory Board compensation**

	<b>31 December 2015</b>	<b>31 December 2014</b>
	<b>HRK'000</b>	<b>HRK'000</b>
Gross salaries and other short-term benefits	3,640	3,569

### **30. Financial risk management**

The Bank's activities are exposed to a variety of financial and operational risks, the management of which includes the analysis, evaluation, acceptance and management to some degree of risk or combination of risks. Risk management and risk acceptance represents the basic merit of financial operations. The Bank's aim is therefore to achieve an appropriate balance between risk and return and minimise potential adverse effects on the Bank's financial performance.

The Bank's risk management policies are designed to identify and analyse these risks, to set appropriate risk limits and controls, and to monitor the risks and adherence to limits by means of reliable and up-to-date information systems. The Bank regularly reviews its risk management policies and systems to reflect changes in market, products and emerging best practise.

Risk management is the responsibility of the Management Board and the Assets and Liabilities Committee (ALCO) and the Committee for credit risk management (RICO). Management identifies, evaluates and hedges financial risks in close co-operation with the Bank's operating units. The Management Board provides written principles for overall risk management, as well as written policies covering specific areas, such as currency risk, interest rate risk, credit risk, liquidity risk, price risk, operational risk and use of derivative and non-derivative financial instruments. In addition, the Internal Audit Department is responsible for the independent review of risk management and the control environment.

The most important types of risk are credit risk, liquidity risk, market risk and operational risk. Market risk includes currency risk, interest rate and other types of price risk.

#### **31.1. Credit risk**

The Bank is exposed to credit risk, which is the risk that a counterparty will be unable to settle its obligations in full when due. Significant changes in the economy, or in the particular industry segment that represents a concentration in the Bank's portfolio, could result in losses that are different from those provided for at the balance sheet date. The Management Board therefore carefully manages its exposure to credit risk. Credit exposures arise principally in loans and advances, debt and other securities. There is also credit risk in off-balance-sheet financial arrangements such as loan commitments and other issued guarantees. The credit risk management and control are centralised within the Risk Management Sector.

## Notes to the financial statements (continued)

for the year from 1 January to 31 December 2015

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### 31.1.1. Credit risk measurement

#### *(a) Loans and advances*

When granting loans and advances to customers and loans to banks according to the contract, the Bank estimates and measures credit risk based on:

1. assessment of counterparty's credit worthiness,
2. assessment of counterparty's regularity in obligations settlement and
3. quality of collateral.

The Bank assesses the counterparty's credit worthiness using the external rating tools. The tools combine statistical analysis with financial advisor judgement and are validated, where appropriate, by comparison with externally available data. Financial analyst exposures for all groups over EUR 150 thousand based on the collected data and indicators must make an opinion on the financial position of the client, and give their opinion regarding the approval. The Bank's placements to customers are segmented into three rating classes; fully recoverable placements, partially recoverable and unrecoverable placements.

Settlement of obligations means the payment of all liabilities within contractual maturity terms, without establishing new receivables in that respect.

The quality of collateral is established based on market effectiveness, the existence of documentation and the possibility of forced collection.

#### *(b) Debt securities and other bills*

For debt securities and other bills, external rating such as Standard & Poor's, Moody's, Fitch/BCA rating or their equivalents are used by the Treasury Sector, if available. The investments in those securities and bills are viewed as a way to gain a better credit quality mapping and maintain a readily available source to meet the funding requirement at the same time.

## Notes to the financial statements (continued)

for the year from 1 January to 31 December 2015

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### 31.1.2. Risk limit control and mitigation policies

The Bank manages, limits and controls concentrations of credit risk wherever they are identified – in particular, with respect to individual counterparties and groups, and to industries and countries.

The Bank structures the level of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, his related parties and industry segments. Limits on the level of credit risk by industry sector are subject to an annual or more frequent review, when considered necessary.

Exposure to credit risk is also managed through regular analysis of the ability of borrowers and potential borrowers to meet all obligations towards the Bank, and by changing these lending limits where appropriate.

Some other specific control and mitigation measures are outlined below:

#### *(a) Collateral*

The Bank employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security for certain types of placements. The Bank has internal regulations in place on the acceptability of specific classes of collateral or credit risk mitigation. The principal collateral types are:

- Mortgages over residential properties;
- Mortgages over business assets such as premises, inventory and receivables, equipment;
- Mortgages over financial instruments such as debt and equity securities.

Debt securities, treasury and other eligible bills are generally unsecured.

#### *(b) Commitments related to loans*

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees carry the same credit risk as loans. Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans or guarantees. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Bank monitors the term to the maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

## Notes to the financial statements (continued)

for the year from 1 January to 31 December 2015

### 31.1.3. Impairment and provisioning policies

Impairment provisions are recognised for financial reporting purposes only for losses that have been incurred at the balance sheet date based on objective evidence of impairment.

The impairment provision shown in the balance sheet at year-end is derived from each of the three internal rating grades. However, the majority of the impairment provision comes from the bottom two grades. The table below shows the percentage of balance items of the Bank's on-balance sheet items relating to loans and advances to customers, and the associated impairment provision for each of the Bank's internal rating categories:

#### Bank's rating

	2015		2014	
	Loans and advances	Provisions for impairment	Loans and advances	Provisions for impairment
	HRK'000	HRK'000	HRK'000	HRK'000
1. Fully recoverable placements	662,298	9,664	656,300	9,076
2 Partially recoverable placements	164,768	76,495	182,820	80,024
3 Unrecoverable placements	127,085	127,080	118,991	118,991
	<b>954,151</b>	<b>213,239</b>	<b>958,111</b>	<b>208,091</b>

#### Bank's rating

	2015		2014	
	Loans and advances (%)	Provision for impairment (%)	Loans and advances (%)	Provision for impairment (%)
	HRK'000	HRK'000	HRK'000	HRK'000
1 Fully recoverable placements	69.41	4.53	68.50	4.36
2 Partially recoverable placements	17.27	35.87	19.08	38.46
3 Unrecoverable placements	13.32	59.60	12.42	57.18
	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>

The internal rating tool assists the Management Board to determine whether objective evidence of impairment exists, based on the following criteria set out by the Bank:

- Delinquency in contractual payments of principal, interest or fee;
- Cash flow difficulties experienced by the borrower (e.g. equity ratio, net income percentage of sales);
- Breach of loan covenants or conditions approved loans;
- Initiation of bankruptcy proceedings;
- Deterioration in the value of collateral.

The Bank's policy requires the review of individual financial assets that are above materiality thresholds at least annually or more regularly when individual circumstances require. Impairment allowances on individually assessed accounts are determined by an evaluation of the incurred loss at balance sheet date on a case-by-case basis, and are applied to all individually significant accounts. The assessment normally encompasses collateral held (including re-confirmation of its enforceability) and the anticipated receipts for that individual account.

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

**31.1.4 Maximum exposure to credit risk before collateral held or other credit enhancements**

	31 December 2015 HRK'000	31 December 2014 HRK'000
<b>Credit risk exposure relating to balance sheet assets is as follows:</b>		
Cash on hand and balances with banks	175,498	128,770
Obligatory reserve with the Croatian National Bank	82,754	91,548
Placements with banks	39,225	39,313
Loans and advances to customers	740,912	750,021
Available-for-sale financial assets	65,362	72,624
Held-to-maturity financial assets	910	1,008
Other assets	27,623	13,092
	<b>1,132,284</b>	<b>1,096,376</b>
<b>Exposure to credit risk relating to off-balance-sheet assets is as follows:</b>		
Financial guarantees	6,686	7,678
Letters of credit	8,277	5,079
Loan commitments and other credit related liabilities	21,773	24,004
	<b>1,169,020</b>	<b>1,133,137</b>

The above table represents Bank's maximum exposure to credit risk as at 31 December 2015 and 2014, without taking into account any collateral held or other credit enhancements attached. For balance sheet items, exposures set out above are based on net carrying amounts as reported in the balance sheet. As indicated above, 68.90% of the total maximum exposure is derived from loans and advances to banks and customers (2014: 71.99%).

**31.1.5 Loans and advances**

Loans and advances are summarised as follows:

	31 December 2015 Loans and advances to customers HRK'000	31 December 2015 Loans and advances to banks HRK'000	31 December 2014 Loans and advances to customers HRK'000	31 December 2014 Loans and advances to banks HRK'000
Neither past due nor impaired	644,072	39,225	639,156	39,313
Past due but not impaired	18,226	-	17,144	-
Individually impaired	291,853	5,138	301,811	5,138
<b>Gross</b>	<b>954,151</b>	<b>44,363</b>	<b>958,111</b>	<b>44,451</b>
Less: provision for impairment	(213,239)	(5,138)	(208,090)	(5,138)
<b>Net</b>	<b>740,912</b>	<b>39,225</b>	<b>750,021</b>	<b>39,313</b>

The total impairment provision for loans and advances is HRK 213,239 thousand (2014: HRK 208,090 thousand) of which HRK 203,575 thousand (2014: HRK 199,014 thousand) represents the individually impaired loans and the remaining amount of HRK 9,664 thousand (2014: HRK 9,076 thousand) represents the portfolio provision. Further information of the impairment provision for loans and advances to banks and to customers is provided in Notes 15 and 16

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

The breakdown of the gross amount of loans and advances by class held by the Bank are as follows:

	<b>Retail customers</b>	<b>Corporate customers</b>	<b>Total loans and advances to customers</b>	<b>Loans and advances to banks</b>
	<b>HRK'000</b>	<b>HRK'000</b>	<b>HRK'000</b>	<b>HRK'000</b>
<b>31 December 2015</b>				
<i>Neither past due nor impaired</i>				
Fully recoverable placements	579,739	64,333	<b>644,072</b>	39,225
<i>Past due but not impaired</i>				
Past due up to 30 days	2,020	303	<b>2,323</b>	-
Past due from 30 to 90 days	4,109	11,794	<b>15,903</b>	-
<i>Individually impaired</i>				
Individually impaired loans	58,068	233,785	<b>291,853</b>	5,138
<b>Total</b>	<b>643,936</b>	<b>310,215</b>	<b>954,151</b>	<b>44,363</b>

	<b>Retail customers</b>	<b>Corporate customers</b>	<b>Total loans and advances to customers</b>	<b>Loans and advances to banks</b>
	<b>HRK'000</b>	<b>HRK'000</b>	<b>HRK'000</b>	<b>HRK'000</b>
<b>31 December 2014</b>				
<i>Neither past due nor impaired</i>				
Fully recoverable placements	538,762	100,394	<b>639,156</b>	39,313
<i>Past due but not impaired</i>				
Past due up to 30 days	2,010	645	<b>2,655</b>	-
Past due from 30 to 90 days	4,686	9,803	<b>14,489</b>	-
<i>Individually impaired</i>				
Individually impaired loans	51,905	249,906	<b>301,811</b>	5,138
<b>Total</b>	<b>597,363</b>	<b>360,748</b>	<b>958,111</b>	<b>44,451</b>

Loans and advances less than 90 days past due are not considered impaired, unless other information is available to indicate the contrary. Upon initial recognition of loans and advances, the fair value of collateral is based on valuation techniques commonly used for the corresponding assets. In subsequent periods, the fair value is updated on the basis of market prices or indexes of similar assets.

**31.1.6 Repossessed collateral**

Reposessed collateral is sold as soon as practicable with the proceeds used to reduce the outstanding indebtedness.

## Notes to the financial statements (continued)

for the year from 1 January to 31 December 2015

### 31.1.7 Concentration of risks of financial assets with credit risk exposure

#### (a) Geographical sectors

The following table breaks down the Bank's main credit exposure at their carrying amounts, as categorised by geographical region as at 31 December 2015. For this table, the Bank has allocated exposures to regions based on the country of domicile of its counterparties.

	Croatia HRK'000	European Union HRK'000	Other countries HRK'000	Total HRK'000
Cash on hand and balances with banks	104,934	51,325	19,239	175,498
Obligatory reserve with the Croatian National Bank	82,754	-	-	82,754
Placements with banks	1,044	-	38,181	39,225
Loans and advances to customers	740,648	264	-	740,912
Available-for-sale assets	55,767	9,595	-	65,362
Held-to-maturity financial assets	910	-	-	910
Other assets	27,623	-	-	27,623
<b>At 31 December 2015</b>	<b>1,013,680</b>	<b>61,184</b>	<b>57,420</b>	<b>1,132,284</b>
<b>At 31 December 2014</b>	<b>957,414</b>	<b>90,726</b>	<b>48,236</b>	<b>1,096,376</b>

#### (b) Industry sectors

The following table breaks down the Bank's main credit exposure at their carrying amounts, as categorised by the industry sectors of our counterparties.

	Financial institutions HRK'000	Manufact uring HRK'000	Properties HRK'000	Wholesale and retail trade HRK'000	Public sector HRK'000	Other industries HRK'000	Individuals HRK'000	Total HRK'000
Placements with banks	39,225	-	-	-	-	-	-	39,225
Loans and advances to customers		31,849	35,660	37,011	621	36,351	599,420	740,912
Available-for-sale assets	9,863	7	202	2,239	52,882	169	-	65,362
Held-to-maturity financial assets	-	-	-	-	-	507	403	910
Other assets	27,255	45	14	63	61	65	120	27,623
<b>At 31 December 2015</b>	<b>76,343</b>	<b>31,901</b>	<b>35,876</b>	<b>39,313</b>	<b>53,564</b>	<b>37,092</b>	<b>599,943</b>	<b>874,032</b>
<b>At 31 December 2014</b>	<b>101,846</b>	<b>62,166</b>	<b>38,447</b>	<b>43,624</b>	<b>23,663</b>	<b>48,790</b>	<b>557,522</b>	<b>876,058</b>



## Notes to the financial statements (continued)

for the year from 1 January to 31 December 2015

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### 32 Market risk

The Bank is exposed to market risks, which is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risks arise from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rate or prices such as interest rates, credit spreads, foreign exchange rate and equity prices. The Bank separates exposures to market risk into either trading or non-trading portfolios.

The market risks arising from trading and non-trading activities are concentrated in the Treasury Division. Regular reports are submitted to the Management Board and heads of each business unit.

Trading portfolios include those positions arising from market-making transactions where the Bank acts as principal with clients or with the market.

Non-trading portfolios primarily arise from the interest rate management of the entity's retail and commercial banking assets and liabilities. Non-trading portfolios also consist of foreign exchange and equity risks arising from the Bank's available-for-sale investments held to maturity.

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the Management Board of the Bank. It is unusual for banks ever to be completely matched since business transacted is often of uncertain term and of different types. An unmatched position potentially enhances profitability, but can also increase the risk of losses.

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature, are important factors in assessing the liquidity of the Bank and its exposure to changes in interest rates and exchange rates.

Liquidity requirements to support guarantee payments and standby letters of credit are considerably less than the amount of the commitment because the Bank does not generally expect the third party to draw funds under the agreement. The total outstanding contractual amount of commitments to extend credit at the balance sheet date does not necessarily represent future cash flows, since many of these commitments will expire or be terminated without being funded.

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

**32.1. Foreign exchange risk**

The Bank is exposed to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Bank manages its currency risk by setting principles and limits for foreign currency exposures and by monitoring exposure with respect to limits. The Bank directs its business activities trying to minimise the gap between assets and liabilities denominated in or linked to foreign currency, and maintaining the daily business activities within daily potential loss limits. The parameters are regularly reviewed in accordance with fluctuations in foreign currency rates and correlations between currencies.

The table below summarises the Bank's exposure to currency risk as at 31 December. Included in the table are the Bank's financial instruments at carrying amounts, categorised by currency.

**Concentrations of currency risk – on- and off-balance sheet financial instruments**

	HRK	EUR	USD	Other currencies	Total
	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000
<b>At 31 December 2015</b>					
<b>Assets</b>					
Cash on hand and balances with banks	76,115	86,905	6,834	5,644	175,498
Obligatory reserve with the CNB	68,904	13,850	-	-	82,754
Placements with banks	-	39,225	-	-	39,225
Loans and advances to customers	141,386	595,595	-	3,931	740,912
Available-for-sale financial assets	2,885	57,250	5,227	-	65,362
Held-to-maturity financial assets	910	-	-	-	910
Other assets	27,623	-	-	-	27,623
<b>Total financial assets</b>	<b>317,823</b>	<b>792,825</b>	<b>12,061</b>	<b>9,575</b>	<b>1,132,284</b>
<b>Liabilities</b>					
Deposits from customers	232,015	747,071	12,169	9,311	1,000,566
Due to banks	9,191	12,884	-	-	22,075
Hybrid instruments	-	34,594	-	-	34,594
Other liabilities	10,515	9,113	79	3	19,710
<b>Total financial liabilities</b>	<b>251,721</b>	<b>803,662</b>	<b>12,248</b>	<b>9,314</b>	<b>1,076,945</b>
<b>Net on-balance sheet financial position</b>	<b>66,102</b>	<b>(10,837)</b>	<b>(187)</b>	<b>261</b>	<b>55,339</b>
Loan commitments	8,496	10,657	2,620	-	21,773
<b>At 31 December 2014</b>					
Total financial assets	297,967	786,365	7,483	4,561	1,096,376
Total financial liabilities	245,082	795,952	7,545	4,454	1,053,033
<b>Net on-balance sheet financial position</b>	<b>52,885</b>	<b>(9,587)</b>	<b>(62)</b>	<b>107</b>	<b>43,343</b>
Loan commitments	9,005	11,325	3,674	-	24,004

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

**32.2 Interest rate risk**

Cash flow interest rate risk is the risk that the future cash flows of financial instruments will fluctuate because of changes in market interest rates. Fair value interest rate risk is the risk that the value of the financial instrument will fluctuate because of changes in market interest rates. The Bank is exposed to the effects of fluctuations in the prevailing levels of market interest rates on both its fair value and cash flow risks. Interest spreads may increase as a result of such changes, but may also reduce losses in the event that unexpected movements arise. The Management Board sets limits on the level of mismatch of interest rates repricing that may be undertaken, which is monitored daily by the Bank's Treasury.

The table below summarises the Bank's exposure to interest rate risks. Included in the table are the Bank's assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

	Up to 1 month	1 - 3 months	3 - 12 months	1 - 3 years	Over 3 years	Non- interest bearing	Total
	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000
<b>At 31 December 2015</b>							
<b>Assets</b>							
Cash on hand and balances with banks	-	-	-	-	-	175,498	175,498
Obligatory reserve with the CNB	-	-	-	-	-	82,754	82,754
Placements with banks	39,225	-	-	-	-	-	39,225
Loans and advances to customers	109,604	26,592	54,405	135,826	413,717	768	740,912
Available-for-sale financial assets	187	-	52,883	-	11,559	733	65,362
Held-to-maturity financial assets	245	447	218	-	-	-	910
Other assets	-	-	-	-	-	27,623	27,623
Total financial assets	149,261	27,039	107,506	135,826	425,276	287,376	1,132,284
<b>Liabilities</b>							
Deposits from customers	212,447	137,883	555,488	67,976	23,778	2,994	1,000,566
Due to banks	415	778	3,579	9,315	6,790	1,198	22,075
Hybrid instruments	1,191	-	-	-	33,403	-	34,594
Other liabilities	-	-	-	-	-	19,710	19,710
Total financial liabilities	214,053	138,661	559,067	77,291	63,971	23,902	1,076,945
<b>Net on-balance sheet financial position</b>	<b>(64,792)</b>	<b>(111,622)</b>	<b>(451,561)</b>	<b>58,535</b>	<b>361,305</b>	<b>263,474</b>	<b>55,339</b>
<b>At 31 December 2014</b>							
Total financial assets	164,637	28,468	118,653	138,311	409,701	236,606	1,096,376
Total financial liabilities	216,877	125,973	590,693	51,058	53,882	14,550	1,053,033
<b>Net on-balance sheet financial position</b>	<b>(52,240)</b>	<b>(97,505)</b>	<b>(472,040)</b>	<b>87,253</b>	<b>355,819</b>	<b>222,056</b>	<b>43,343</b>

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

**32.3 Liquidity risk**

Liquidity risk is the risk that the Bank will be unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay depositors and fulfil commitments to lend.

The Bank is exposed to daily calls on its available cash resources from overnight deposits, current accounts, maturing deposits, loan draw downs and other calls on cash. The Bank does not maintain cash resources to meet all of these needs as experience shows that the minimum level of reinvestment of maturing funds can be predicted with a high level of certainty. The Bank manages liquidity reserves daily, ensuring also meeting all customer needs.

**32.3.1 Funding approach**

Sources of liquidity are regularly reviewed by the Bank's Treasury to maintain a wide diversification by currency, geography, provider, product and term.

**32.3.2. Non-derivative cash flows**

The table below presents the cash flows payable by the Bank under non-derivative financial liabilities by remaining contractual maturities at the balance sheet date.

<b>At 31 December 2015</b>	<b>Up to 1 month HRK'000</b>	<b>1 - 3 months HRK'000</b>	<b>3 - 12 months HRK'000</b>	<b>1 - 3 years HRK'000</b>	<b>Over 3 years HRK'000</b>	<b>Total HRK'000</b>
Deposits from customers	214,763	137,888	555,681	68,060	24,174	1,000,566
Due to banks	1,613	778	3,579	9,315	6,790	22,075
Hybrid instruments	1,191	-	-	-	33,403	34,594
Other liabilities	16,041	1,548	2,117	4	-	19,710
<b>Total liabilities</b> (contractual maturity dates)	<b>233,608</b>	<b>140,214</b>	<b>561,377</b>	<b>77,379</b>	<b>64,367</b>	<b>1,076,945</b>
<b>Total liabilities on unused loans</b> (expected maturity dates)	<b>5,437</b>	<b>48</b>	<b>15,923</b>	<b>365</b>	<b>-</b>	<b>21,773</b>

## Notes to the financial statements (continued)

for the year from 1 January to 31 December 2015

At 31 December 2014	Up to 1 month HRK'000	1 - 3 months HRK'000	3 - 12 months HRK'000	1 - 3 years HRK'000	Over 3 years HRK'000	Total HRK'000
Deposits from customers	196,767	124,366	584,819	40,596	27,322	973,870
Due to banks	23,636	1,613	5,909	10,811	12,567	54,536
Hybrid instruments	560	-	-	-	14,365	14,925
Repurchase agreements	-	-	-	-	-	-
Other liabilities	7,643	776	1,280	2	-	9,702
<b>Total liabilities</b> (contractual maturity dates)	<b>228,606</b>	<b>126,755</b>	<b>592,008</b>	<b>51,409</b>	<b>54,254</b>	<b>1,053,033</b>
<b>Total liabilities on unused loans</b> (expected maturity dates)	<b>5,460</b>	<b>77</b>	<b>18,229</b>	<b>238</b>	<b>-</b>	<b>24,004</b>

Assets available to meet all of the liabilities and to cover outstanding loan commitments include cash, central bank balances, items in the course of collection and treasury and other eligible bills; loans and advances to banks; and loans and advances to customers. In the normal course of business, a proportion of customer loans contractually repayable within one year will be extended. The Bank would also be able to meet unexpected net cash outflows by selling securities and approaching other funding sources.

### 32.3.2. Off-balance-sheet items

#### (a) Loan commitments

The dates of the contractual amounts of the Bank's off-balance-sheet financial instruments that commit it to extend credit to customers and other financial instruments (Note 29) are summarised in the table below.

#### (b) Other financial instruments

Other financial instruments (Note 29) are also included below based on the earliest contractual maturity date.

	No later than 1 year HRK'000	1 to 3 years HRK'000	Over 3 years HRK'000	Total HRK'000
<b>At 31 December 2015</b>				
Loan commitments	21,408	365	-	21,773
Guarantees, letters of credit and other	14,963	-	-	14,963
<b>Total</b>	<b>36,371</b>	<b>365</b>		<b>36,736</b>
<b>At 31 December 2014</b>				
Loan commitments	23,766	238	-	24,004
Guarantees, letters of credit and other	12,757	-	-	12,757
<b>Total</b>	<b>36,523</b>	<b>238</b>	<b>-</b>	<b>36,761</b>

## Notes to the financial statements (continued)

for the year from 1 January to 31 December 2015

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the Management Board of the Bank. It is unusual for banks ever to be completely matched since business transacted is often of uncertain term and of different types. An unmatched position potentially enhances profitability, but can also increase the risk of losses.

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature, are important factors in assessing the liquidity of the Bank and its exposure to changes in interest rates and exchange rates.

Liquidity requirements to support guarantee payments and standby letters of credit are considerably less than the amount of the commitment because the Bank does not generally expect the third party to draw funds under the agreement. The total outstanding contractual amount of commitments to extend credit at the balance sheet date does not necessarily represent future cash flows, since many of these commitments will expire or be terminated without being funded.

### 32.4 Fair value of financial assets and liabilities

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Fair value is based on quoted market prices, where available. However, no readily available market prices exist for a significant portion of the Bank's financial instruments. In circumstances where the quoted market prices are not readily available, the fair value is estimated using discounted cash flow models or other pricing techniques as appropriate. Changes in assumptions on which the estimates are based, including discount rates and estimated future cash flows, significantly affect the estimates. Therefore, the calculated fair market estimates may not be realisable in a current sale of the financial instrument.

The Bank uses the following hierarchy for determining the fair value of financial instruments by using valuation techniques:

- level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities
- level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly
- level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data

	31 December 2015			31 December 2014		
	Level 1 HRK'000	Level 2 HRK'000	Total HRK'000	Level 1 HRK'000	Level 2 HRK'000	Total HRK'000
Bonds	64,629	-	64,629	71,934	-	71,934
Shares	592	141	733	549	141	690
	<b>65,221</b>	<b>141</b>	<b>65,362</b>	<b>72,483</b>	<b>141</b>	<b>72,624</b>

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

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

	Carrying amount		Fair value	
	2015	2014	2015	2014
	HRK'000	HRK'000	HRK'000	HRK'000
<b>Financial assets</b>				
Placements with banks	39,225	39,313	39,225	39,313
Loans and advances to customers	740,912	750,021	740,912	750,021
Held-to-maturity financial assets	910	1,008	910	1,008
Other assets	27,623	13,092	27,623	13,092
<b>Total financial assets</b>	<b>808,670</b>	<b>803,434</b>	<b>808,670</b>	<b>803,434</b>
<b>Financial liabilities</b>				
Deposits from customers	1,000,566	973,870	1,000,566	973,870
Due to banks	22,075	54,536	22,075	54,536
Hybrid instruments	34,594	14,925	34,594	14,925
Other liabilities	19,710	9,702	19,710	9,702
<b>Total financial liabilities</b>	<b>1,076,945</b>	<b>1,053,033</b>	<b>1,076,945</b>	<b>1,053,033</b>

For the purpose of the fair value assessment of the Bank's financial instruments the following methods and assumptions have been used:

*(a) Cash and funds with Central bank*

The carrying amount of cash and amounts due from banks, obligatory reserve with the Croatian National Bank, and placements with banks, deposits from banks and deposits from companies and similar entities are deemed to reflect their fair value due to the short-term maturity of these financial instruments.

*(b) Held-to-maturity financial assets*

The fair value of securities held-to-maturity is calculated based on quoted market prices.

*(c) Due from other banks*

The estimated fair values of amounts due from other banks, which mature within a maximum of 180 days approximate their carrying amounts. The fair values of other amounts due from banks is estimated based on discounted cash flow analyses using prevailing interest rates for investments under similar terms (market rates adjusted by credit risk). The fair value of non-performing amounts due from banks is estimated using a discounted cash flow analysis. Allowances are not taken into consideration when calculating fair values.

## Notes to the financial statements (continued)

for the year from 1 January to 31 December 2015

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### *(d) Loans to and receivables from customers*

The fair value of variable yield loans that regularly reprice, with no significant change in credit risk, generally approximates their carrying value. The fair value of loans at fixed interest rates is estimated using discounted cash flow analyses, based upon interest rates currently offered for loans with similar terms to borrowers of similar credit quality. The fair value of non-performing loans to customers is estimated using a discounted cash flow analysis or the appraised value of the underlying collateral, where available. Loans at fixed interest rates represent only a fraction of the total carrying value and hence the fair value of total loans to and receivables from customers approximates the carrying values as at the balance sheet date. Allowances are not taken into consideration when calculating fair values.

### *(e) Due to other banks and customers*

The fair value of term deposits payable on demand represents the carrying value of amounts payable on demand as at the balance sheet date. The fair value of term deposits at variable interest rates approximates their carrying values as at the balance sheet date. The fair value of deposits at fixed interest rates is estimated by discounting their future cash flows using rates currently offered for deposits of similar remaining maturities.

## **32.5 Capital risk management**

The Bank's objectives when managing capital, which is a broader concept than 'equity' on the face of balance sheets, are:

- to comply with the capital requirements set by the central bank;
- to safeguard the Bank's ability to continue as a going concern so that it can continue to provide returns for shareholders and benefits for other stakeholders; and
- to maintain a strong capital base to support the development of its business.

In accordance with the regulations governing this area of monitoring of the Bank's operations, the Bank is obliged to submit to the Croatian National Bank reports on capital adequacy and coverage of capital requirements on a quarterly basis.

Based on the capital requirements from Regulation (EU) 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No. 648/2012, the minimum rate of regulatory capital that the Bank must maintain is 8%, while maintaining a level of capital sufficient to cover the capital requirements of additional tier for capital protection (2.5%) and the additional tier for structural systemic risk (1.5%).



**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

The table below summarises the composition of regulatory capital and the ratios of the Bank for the year ended 31 December 2015.

	<b>31 December 2015 HRK'000</b>	<b>31 December 2014 HRK'000</b>
<b>Regulatory capital</b>		
Share capital	409,478	409,478
Supplementary capital	32,432	11,826
Deductions from regulatory capital	(317,427)	(318,437)
<b>Regulatory capital</b>	<b>124,483</b>	<b>102,867</b>
<b>Structure of risk exposure</b>		
Exposure amount weighted by credit risk	729,318	729,889
Market risk exposure	713	529
Operating risk exposure	95,158	89,392
<b>Total risk exposure</b>	<b>825,209</b>	<b>819,810</b>
<b>Structure of capital requirements</b>		
Capital requirements for total capital ratio (8%)	66,017	65,585
Additional tier for capital protection (2.5%)	20,630	20,495
Additional tier for structural system risk (1.5%)	12,378	12,297
<b>Total capital requirements</b>	<b>99,025</b>	<b>98,377</b>
<b>Capital adequacy</b>	<b>15.09%</b>	<b>12.55%</b>

**Notes to the financial statements (continued)**

for the year from 1 January to 31 December 2015

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**33. Events after the balance sheet date**

In February 2016, the Bank received a decision of the regulator based on which it is required to maintain regulatory capital by at least 3.09 percentage points higher than as prescribed in Article 92 paragraph 1 item c) of Regulation (EU) no. 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms and Chapter VII of the Credit Institutions Act, i.e. to maintain a rate of 15.09%. As at 31 December 2015, the Bank meets all additional capital requirements of the regulator.

On 29 February 2016, a regular meeting of the Bank's General Assembly was held at which it was proposed that a decision be made to declare dividends from the total operating profit in 2016 in the amount of HRK 3,805,712.16 to the shareholders, as well as that a decision be made to increase the regular share capital of the Bank by a total of HRK 10,734,345.04.

**Approval of the financial statements**  
for the year from 1 January to 31 December 2015

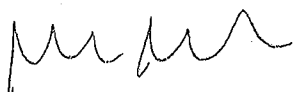
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**34. Approval of the financial statements**

The financial statements set out on pages 4 to 56 were approved by the Management Board of the Bank on 30 March 2016.

Nicola Ceccaroli

President of the Management Board



Darko Kosovec

Member of the Management Board

