

**BANKA KOVANICA d.d.**

**Annual report for the year 2019**

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## **Our opinion**

## Responsibility for the financial statements

Pursuant to the Croatian Accounting Act (Official Gazette 78/15, 134/15, 120/16 and 116/18), 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 the 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 78/15, 134/15, 120/16 and 116/18). The Management Board is also responsible for safeguarding the assets of the Bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Management Board is also responsible for the preparation and content of the Management Report, as required by the Croatian Accounting Act. The Management Report was approved by the Management Board on 30 March 2019 and signed accordingly.

Signed on behalf of the Management Board:

Nicola Ceccaroli

President of the Management Board

Ivan Mužić

Member of the Management Board

Banka Kovanica d.d.,  
P. Preradovića 29  
Varaždin

30 March 2020

**BANKA KOVANICA d.d.  
VARAŽDIN**

**MANAGEMENT REPORT  
for 2019**

**Management Board Remarks**

In 2019, Croatia experienced its fifth consecutive year of economic growth, closing the year with real GDP up +2.9% and forecasts for 2020 (+2.6%) and 2021 (+2.3%) showing a slightly declining trend. Positive economic growth was once again largely driven by private consumption and tourism, supported by a sustained increase in wages and employment boosting disposable income and household confidence. Positive growth rates were also recorded in investments and public consumption, while exports ended the year recording a negative net balance. Considering the slowing growth trends recorded by its key trade partners, Croatia's economic growth is expected to shrink over the next couple of years in the context of moderate inflation (core inflation estimates: +1.4% in 2020 and +1.5 in 2021). Significant activity is expected in public and private investments, spurred by an increase in financial resources available through EU funds. The fiscal consolidation process continued to be implemented in 2019, although at somewhat lower levels due to an increase in public consumption and a decrease in taxes. The monetary policy remained accommodative, marked by large interbank reserves and low rates in money and commercial markets. The growth in bank loans, driven primarily by the retail sector, which boasts a two-digit growth in general-purpose consumer loans, exceeded the inflation rate, while loans to non-financial companies remained almost at the same level. In 2019, Croatia's investment grade rating was confirmed by two leading rating agencies ("BBB-"). Such stable or positive outlook reflects the potential of the reforms to ensure faster convergence, taking into consideration the performance metrics recorded by Croatia's trade partners and the risks arising from international insecurities. It is also expected that the public finances will continue to be affected by the negative demographic trend. And finally, after a multi-year Stability and Growth Pact compliance verification process, in 2019 Croatia applied for Eurozone membership with the European Exchange Rate Mechanism (ERM-II).

In 2019, the Croatian banking system recorded normalised earnings before taxes in the amount of HRK 6.6 billion (according to preliminary CNB data), which is an annual increase of 18%. In a relatively concentrated banking system (where the eight leading banks, whose individual shares exceed 5% of total assets, make up a cumulative market share of more than 94%), Banka Kovanica d.d. ranks 18<sup>th</sup> by total assets (market share: 0.3%) and 17<sup>th</sup> by own funds. In a sample of 12 small banks, each accounting for less than 1% of total assets (2.1 billion, on average), the Bank holds a market share of 5.2%. In 2019, the relevant sample of small banks recorded total normalised earnings before taxes at the level of HRK 201.8 million. One of the banks operated at a loss, while the Bank accounted for 7.8% of the total amount. In addition, the Bank also recorded a two-digit own funds profitability rate and ranked high among the small banks included in the sample. Profit before tax recorded by the Bank, which amounted to HRK 17.5 million, even exceeded the plan (+3.0%) despite the corrections, value adjustments and the extraordinary cost of provisions that resulted from the implementation of precautionary measures to accommodate the supervisory recommendations of the Croatian National Bank. Furthermore, the Bank recorded total assets in the amount of HRK 1,344.7 million (+8.8%), which is in line with the Business Plan 2017 – 2020, while its capital and reserves amounted to HRK 133.1 million (or HRK 143.4 million if the provisions for the initial application of IFRS 9 are included), mainly as a result of a decrease in net non-performing loans to 3.1%, which is in line with the domestic banking system and the best-in-class in the sample of small banks.

**Most Significant Financial and Business Results:**

- increasing business results with a return on equity (ROE) on the rise to 13.4%, which confirms the high earning capacity of the Bank ranking high in the sample of small banks,
- total capital adequacy ratio on the rise to 16.5% (18.0% if the 2019 results are included), resulting from capital base adjustments made to reflect the envisaged growth targets in the volume of investments, focusing primarily on consumer loans and secondly on working capital loans intended for SMEs,
- further significant decline in net receivables more than 90 days past due, whose weight in relation to equity and other capital instruments fell below 20% (Texas ratio proxy), thus confirming the Bank's prudent investment policy and effective uncollected debt recovery policy,
- further automation of company processes (with the aim of creating a paper-free office) for the purpose of optimising the back- and middle-office functions, and identifying measurable economies of scale in accordance with the niche bank model.

At the General Meeting, the Management Board will propose that the 2019 net profit, which amounts to HRK 14,691,990.63, as determined on the basis of the audited Financial Statements as at 31 December 2019, be allocated to reserves in order to boost the capital base with the aim of ensuring convergence to the average values recorded by the domestic banking system, in line with the Business Plan 2017 – 2020.

The Management Board would like to use this opportunity to thank all the Bank's business partners, clients and shareholders for their confidence, and the members of the Supervisory Board for their cooperation and commitment. We would also like to thank all our employees for their effort and contribution, and kindly request that additional efforts be made in order to ensure achievement of the ambitious goals set under the Business Plan.

**General Information about the Bank and its Organizational Structure**

The Bank has been operating since 1997, when it was entered in the register of the Commercial Court of Varaždin under the name of Štedionica Kovanica. In April 2002, Štedionica was converted into a bank, and in 2005 it obtained the Approval to Operate from the Croatian National Bank ("CNB").

The Company's registered office is in Varaždin, Petra Preradovića 29.

The Bank's share capital amounts to HRK 106,961,910. It is divided in 3,565,397 shares (nominal value per share: HRK 30.00) and has been paid in full. The Bank's majority shareholder (*Cassa di Risparmio della Repubblica di San Marino S.p.a.*) holds 99.496% of the total share capital. Private domestic shareholders collectively account for 0.3018%, while own shares represent 0.0042% of the total share capital.

The Bank's registered activities are as follows:

- accepting cash deposits,
- extending loans and making other investments in its own name and for its own account,
- issuing means of payment in the form of electronic money,
- issuing guarantees and other warranties,

- factoring,
- finance leasing,
- credit operations, including consumer loans, mortgage loans and trade finance (including forfeiting),
- trading in its own name and for its own account, or in its own name and for a client's account in money market instruments and other transferable securities, currency (FX) exchange activities,
- trading in futures and forwards, including both instruments and options, and currency and interest rate instruments,
- performing national and international payments,
- collecting data, preparing analyses and providing creditworthiness information in respect of both legal and natural persons,
- providing insurance sales agency services in accordance with the act regulating insurance business, intermediation and representation in insurance,
- issuing and managing payment instruments, financial intermediation.

The Bank has joined the SWIFT service and the Croatian Registry of Credit Obligations (HROK).

The Bank's shares are not listed on any stock exchange.

On 31 December 2019, the Bank had the following management bodies in place:

#### ***General Meeting***

appointed at the meeting

Chairman

#### ***Supervisory Board***

Francesco Carobbi

President

Filippo Francini

Vice President (resigned on January 10, 2020)

Stefano Marsigli Rossi Lombardi

Member (resigned on March 13, 2020)

Mladen Vedriš

Member (new Vice President)

Franjo Gregurić

Member (from January 23, 2019)

#### ***Management Board***

Nicola Ceccaroli

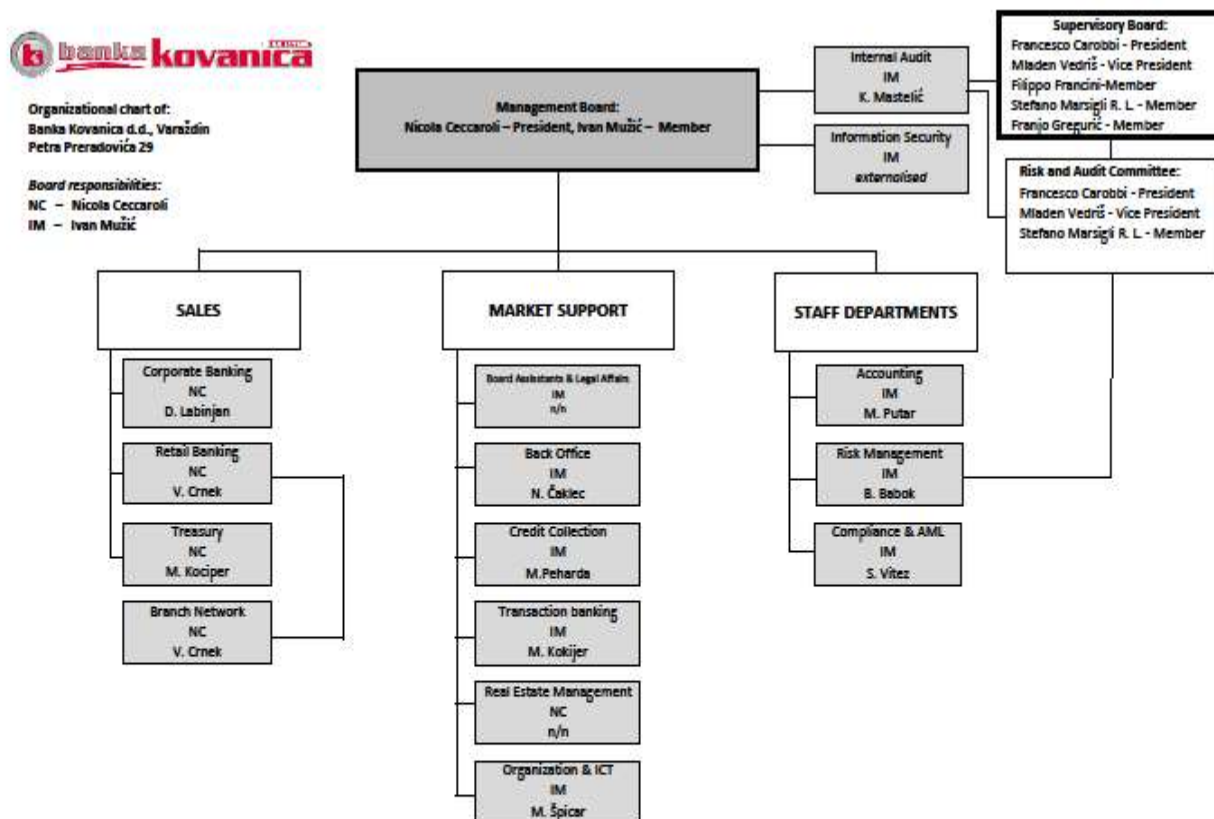
President (term renewed on March 13, 2020)

Ivan Mužić

Member (term renewed on March 13, 2020)



The Bank operates through a network of 12 branches and 7 ATMs on the territory of Croatia, offering services to both natural and legal persons. It is functionally organized in accordance with the requirements prescribed under the Basel II Standard, the Credit Institutions Act, recommendations and guidelines issued by the CNB, and the concrete needs of a modern bank. The Bank's Management Board remains responsible for ensuring further rationalization of the branch network in the age of digital banking, excluding the assumptions regarding the future consolidation of small and medium-sized banks.



Valid as of: 31.12.2019.

The Bank's operations are managed by the Management Board, which is composed of two members who are assigned direct management responsibilities based on the separation of back- and front-office activities. In accordance with the structure adopted in 2014, the Bank is organized in 6 divisions and 7 management support departments.

Consolidation of management centres into a single centre at the level of the Bank led to certain organizational changes, aimed particularly at improving the effectiveness of operational processes and reducing operational risks:

- merging of the Human Resources Department with the Management Board and Legal Department,

- merging of the Payments, Treasury and Trade Finance Departments into a new Transaction Banking Department, and
- transfer of the FINA (filing order) and back-office operations (payments) from the Loan Recovery Department to the Bank Transactions Department.

The Bank belongs to a group of small banks operating in a highly concentrated banking market. It has been granted general approval to provide all services associated with lending, collection and payment in foreign currencies and accepting deposits, as well as payment and other financial services.

In July 2007, the Bank was acquired by Cassa di Risparmio della Repubblica di San Marino S.p.a., the oldest bank in the Republic of San Marino. During its existence, the Bank has been recapitalized by its majority owner several times. The latest HRK 3.0 million capital injection (accompanied by simultaneous dividend and reserve disbursements in the same amount), based on the General Meeting's decision from April 28, 2017, was recorded in the register of the Commercial Court of Varaždin, increasing the Bank's share capital to a total of HRK 106,961,910.

### ***Human Resources***

The Human Resources Department was established in 2009. In 2014, it was merged with the Management Board and Legal Affairs Office. Among other, the Office is responsible for hiring as well as employee training and professional development. In the course of 2019, the Bank hired 21 new employees, while 14 employees were laid off. On 31 December 2019, the Bank had 104 employees, including 5 workers employed under the annual public training program implemented with the aim of introducing new graduates into the world of labour (2018: 97 employees). The employee structure included primarily workers employed full time on the basis of an open-ended contract, while 5 workers were employed on the basis of a fixed term contract, mainly as substitutes for employees on maternity leave or as additional staff required due to a temporary increase in the volume of business in certain offices of the Bank. Without the said substitutes and trainees, the number of employees (FTE) as at 31 December 2019 would be almost the same as last year (94). The total assets per employee ratio (FTE) was HRK 14.3 million, up +7.7% y-o-y. The Management Board will continue to make efforts to further improve this efficiency index to ensure convergence towards the target values of the peer group through back- and middle-office staff optimisation and process automation. On the reporting date, the total structure of employees included 74% women, the average age of employees was 41, and 45% of employees were under 40. 70% of employees completed higher university education programs (MA and higher), 27% completed the bachelor program, while 43% had a college degree. The Bank spent HRK 31 thousand on employee education/training in 2019, including participation in seminars and professional advancement programs, acquisition of new knowledge, work quality improvement and adjustment to changes in legislation. The Bank also organised periodic internal training conducted by responsible persons from the relevant divisions.

### ***Movements in Assets, Financial Results and Condition***

The Bank's financial statements were audited by PricewaterhouseCoopers d.o.o., an independent auditor. The financial statements comprise the Balance Sheet, the Income Statement, the Final Share Capital Account for the accounting period that ended on 31 December 2019, and the Notes to the Financial Statements. After

performing the audit of the Bank's financial statements, the independent auditor confirmed the accuracy and authenticity of the balance sheet, the financial reports and the financial results of the Bank in accordance with the valid accounting regulations applicable to Croatian banks. Thus, the Bank received an unqualified opinion for the fifth consecutive year. On 31 December 2019, total assets amounted to HRK 1,345.6 million, up 9% year over year, primarily as a result of an increase in loans approved to clients. Net loans approved to clients amounted to HRK 996.1 million, up 11% compared to 2018. Retail loans increased by 7%, reaching HRK 838.5 million, whereas corporate loans increased by 42%, reaching HRK 157.6 million. The Bank recorded a year-over-year decrease of 49% in cash and cash equivalents, which fell to HRK 74.6 million as a result of the treasury optimisation process in the segment of high-quality liquid assets. Statutory reserves amounted to HRK 78.5 million, up 8% compared to the year before. The Bank further recorded an increase in securities available for sale as a result of investments in short- and medium-term Eurozone government bonds, while financial assets held to maturity increased as a result of bill discounting. Client deposits amounted to HRK 1,143.8 million (contributed almost entirely by retail deposits), indicating an annual increase of 8% as a result of the continued decrease in the average interest rate on term deposits. On 31 December 2019, regulatory capital amounted to HRK 153.6 million. The total capital to risk weighted assets ratio was at the level of 16.5% (excluding the operating profit), exceeding the budget target and the required minimum of 12%. Income from interest and other similar income amounted to HRK 82.3 million, up 10% year over year. Interest expenses and other similar expenses amounted to HRK 15.2 million, dropping by 4% compared to the year before. Net income from interest amounted to HRK 67.0 million, up 13.2% year over year. Income from fees amounted to HRK 8.6 million, rising by 11% compared to the year before, while the cost of fees amounted to HRK 2.5 million, which is also an 11% increase compared to 2018. Net income from fees remained almost the same as in 2018. Other net income amounted to HRK -3.0 million, compared to HRK -1.8 million in 2018. General administrative costs and amortisation amounted to HRK 39.7 million, up 15% compared to the year before. Such increase is primarily attributed to the impairment of foreclosed/repossessed fixed assets, strictly for prudential supervision purposes, and secondarily to an increase in wages. Loan loss provisions amounted to HRK 14.7 million, down 13% year over year, despite the fact that they were booked strictly for prudential supervision purposes. Net profit before tax amounted to HRK 17.5 million, while net profit after tax amounted to HRK 14.7 million. This is an annual increase of 70.7%. The Bank's net profit was reduced, among other, also due to a write-off of deferred tax assets in the amount of HRK 2.0 million (booked in 2012), performed pursuant to the applicable tax regulations, while taking into account the new deferred tax assets in the amount of HRK 0.8 million.

**Main Products and Services Offered by the Bank****1. Credit Operations**

In the retail credit operations segment, the Bank offers several types of general-purpose loans, including:

- short-term general-purpose cash loans with a currency clause in EUR intended for the clients of the Bank; repayment period: up to 12 months,
- general-purpose cash loans with a currency clause in EUR; repayment period: up to 144 months,
- general-purpose cash loans in HRK; repayment period: up to 144 months,
- general-purpose cash loans with a currency clause in EUR; security required: real estate,
- general-purpose loans; security required (term deposit),
- general-purpose cash loans in HRK for refinancing; repayment period: up to 144 months,
- general-purpose cash loans with a currency clause in EUR for refinancing; repayment period: up to 144 months.

The Bank adjusts the loan terms depending on the needs of the market, and the terms offered by competition.

The Bank also offers special-purpose loans, including housing loans with a repayment period of up to 30 years.

**2. Deposit Operations**

In the segment of deposit operations, the Bank offers a wide range of savings products with a fixed or variable interest rate, as well as demand and term deposits, applying an individual approach in negotiating the terms.

The Bank offers:

- term deposits allowing additional payments in HRK with a currency clause or in a foreign currency; terms: from 3 to 60 months,
- profit-generating term deposits in HRK, in HRK with a currency clause, or in a foreign currency; terms: from 3 to 60 months,
- annuity-based term deposits in HRK, in HRK with a currency clause, or in a foreign currency; terms: from 3 to 60 months, and
- Klinko children's savings in HRK and EUR.

In October 2015, the Bank started offering term deposits to individuals in the Federal Republic of Germany under the EU Passport regime and in cooperation with SAVEDO GmbH (Deposit Solutions Group). The online platform operator manages, together with its banking partner, the entire customer life cycle in German (online/offline client acquisition, request form, customer service). By collecting cross-border savings, the Bank aims to achieve the following key goals: reduction in the cost of financing, customer base diversification, and consolidation of maturities. The cross-border savings program is supervised by the Croatian National Bank based on the screening performed by the German Federal Financial Supervisory Authority (BaFin).

### **3. Accounts – Financial Transactions**

The Bank offers solutions that allow effective, quick and safe transactions in the management of financial instruments.

#### **3.1. Current Accounts**

A current account allows the client to arrange a wide selection of products and services adjusted to his/her individual needs, including:

- *Konto ko-net* current account – a current account package available in three different models depending on the selection of additional services,
- approved account overdraft,
- checks,
- standing order,
- Maestro debit card,
- *ko-net* internet banking,
- mKovanica mobile banking,
- POS payments and withdrawals using ATMs, in instalments,
- payment by instalment,
- SMS services.

In 2019, the Bank implemented the European Payment Services Directive ("PSD 2") and developed certain new applications to ensure compliance with the regulations on anti-money laundering and counter-terrorism financing ("AML/CFT") and data protection ("GDPR"). The Bank also developed several business process automation projects trying to achieve the following three goals: to reduce the cost of procedure (by creating a paper-free office), to shorten the time of production, and to prevent operational risks; including primarily the establishment of an electronic board decision archive and an electronic consumer lending SOP. In 2020, the Bank plans to complete the electronic corporate lending procedure (CORPAS), activate business relationship management tools (CRM) and, in cooperation with its IT partner, digitalize the debt collection procedure (e-Collection), the electronic invoice issuance procedure (e-Invoice), and the document management procedure (DDM).

#### **3.2. Gyro Accounts – Individual Clients**

Individual clients – gyro account holders can use the *ko-net* internet banking service, which allows them to manage the funds in their accounts in the most convenient manner.

#### **4. Card Operations**

The Bank offers the following cards:

- *Maestro* debit card – the technology applied in the development of this chip card guarantees banking service improvement, and provision of additional services associated with the *Maestro* debit card,
- MasterCard charge,
- MasterCard revolving,
- Business Master card.

In 2019, the Bank launched contactless debit and credit cards with a refreshed graphic design, implemented the MasterCard transaction authorization process (Chip & PIN), and updated the security protocol for the multi-factor authenticity check procedure (2FA). In the course of 2020, the Bank plans to implement biometric authentication on mobile devices to additionally improve customer experience and security of payments.

#### **5. ATMs**

The *Maestro* debit card enables the holder to withdraw cash at ATMs and execute POS payments in the Republic of Croatia, as well as to withdraw cash at ATMs (Cirrus) and POS payments (*Maestro*) abroad. At the Bank's ATMs and the ATMs from the MBNET network, cash can be withdrawn free of charge (the number of free transactions per month is predefined). The Bank offers the possibility of paying in instalments via POS devices and withdrawing cash at ATMs through periodic debits from the designated current account.

#### **Main Risks and Insecurities to which the Bank is Exposed**

In its operations, the Bank is exposed to various types of risk, which must be managed systematically. Risk management includes risk identification, analysis, assessment, management and monitoring, as prescribed in the policies and procedures that, among other, also define the acceptable levels of risks for the Bank. The most significant types of risks to which the Bank is exposed include: credit risk, liquidity risk, market risk (including interest, currency and price risks) and operational risk. A more detailed analytical report on financial risks is provided in Notes 30), 31) and 32) of the audited Annual Financial Report as at 31 December 2019, which is enclosed herewith.

#### **Operational Risk**

Operational risk is the risk of loss resulting from inadequate internal processes, human factor or external events, including compliance risk. Operational risk is inherent to all banking activities, processes and products. The capital requirement for operational risk is calculated applying the basic indicator approach (BIA). The Bank has adopted the Operational Risk Management Policy and Guidelines for the Classification of Operational Risk Applying the Risk Mapping Method, and it has also defined the 'significant risk' threshold. In case this threshold is exceeded, a detailed cause and effect analysis is performed with the aim of improving the control procedures, avoiding the occurrence of similar events in the future or mitigating the consequences.

***Current Significant Events and Future Activities***

In 2014, the new management initiated the restructuring and relaunch process. As a result, the Bank achieved operating profit in 2014 and net profit in 2015. All loan quality indicators started significantly improving and converging towards the average values recorded by the domestic banking system, despite the unfavourable loan portfolio the new management inherited at the beginning of the term, confirming its prudent credit policy. In 2019, the Bank recorded a cost/income ratio at the level of 55.4% and a two-digit own funds profitability rate, thus becoming one of the leading banks in the relevant sample of small domestic banks.

In spite of the successful restructuring and relaunch process undertaken by the new management appointed in 2014, the Business Plan 2020 – 2023 envisages a reduction of execution risk and reflects a context marked by extremely low interest rates, and significant and increasing regulatory and competitive pressures, primarily affecting less significant institutions, through the implementation of the supervisory measures imposed by the Croatian National Bank. More precisely, pursuant to the guidelines issued by the holding company, the new plan envisages a review of the reduced profitability, i.e. 10%+ in ROE before tax, being still in the first quartile in terms of profitability of banks within the EU. Furthermore, the new plan also envisages a relative increase in exposure to non-financial companies (mainly through short-term working capital financing) up to 25%+ of total net loans, with the aim of limiting the growth rate of general-purpose consumer loans and promoting increased diversification by asset classes. Finally, the new plan also envisages a dividend distribution policy up to 50% of the periodic profit, starting from 2022.

The annual Supervisory Review and Evaluation Process ("SREP 2019") confirmed a 3.3% additional adverse scenario-based capital requirement in accordance with Article 92.1.c) of Regulation (EU) No. 575/2013, to ensure the so-called total capital ratio of 15.3%. As a result of the regular onsite paper inspection, the Bank recognised areas for improvement in the segment of general-purpose consumer loans and implemented the relevant supervisory measures to further strengthen the risk management function in accordance with the expectations of the supervisor and the best banking practices applicable to small and non-complex banks. The Bank is making efforts to strengthen its position in the retail sector with the aim of becoming a bank of choice in the household and SME segments. It builds its competitive advantage on "listening", as a true distinguishing factor. The Bank therefore places high priority on capacity building in terms of achieving income and internal generation of capital based on a reinforced budget. The multi-year replacement of the banking information system plays a key role in the implementation of the digital banking offer. As already mentioned, the Bank's Business Plan is primarily a plan based on margins and secondarily on volumes. More precisely, the goals associated with the expected growth inevitably depend on compliance with the prescribed capital requirements, while the investment dynamics must be such to ensure capital buffer protection ("CRR/CRD IV") and add-ons to own funds ("SREP"). The Bank's Business Plan still lays down ambitious goals, but also envisages a more moderate downward correction of the main KPIs with the aim of limiting the execution risk, even in the implementation of supervisory recommendations, and strives to achieve a more diversified loan product portfolio intended for SMEs in order to limit the retail loan growth rate, without however affecting the Bank's focus on general-purpose consumer loans in the process.

The main risks to which the Bank is exposed are:



- ❖ increasing competition dynamics in the context of the banking sector consolidation, technological innovations and changing client preferences, aggravated by the continued trend of extremely low interest rates,
- ❖ constant issuance of new national and international rules and regulatory measures, bringing high compliance costs and high strategic, operational and reputational risks, particularly affecting less significant institutions,
- ❖ high counterparty default rates, particularly in the corporate segment, along with the ineffectiveness and delays in the performance of civil procedures associated with debt collection.

The crisis caused by the coronavirus (COVID-19) pandemic and the extraordinary national and supranational measures implemented in reaction to this global health threat, which materialized at the beginning of 2020, could result in serious social and economic disruption of systemic proportions, even in the best-case scenario - a rapid regression of the contagion curve. On the date of this Annual Report, the medium- and long-term impacts of the coronavirus crisis on state, corporate and household budgets could not be assessed with sufficient accuracy since this crisis is unlike any other crisis the world has ever seen before, unprecedented in history, and there are no predetermined models to follow. The Bank has immediately activated its Business Continuity Plan in order to guarantee the safety of its employees and key business processes, in accordance with the instructions issued by the competent authorities. In the process of drafting the Interim Management Report, the Bank will prepare a preliminary analysis of budget execution, capital adequacy and liquidity in the never-anticipated stress scenarios, taking into account the recent extraordinary support measures adopted by the government, the community, and the central banks.

#### ***Statement by the Management Board***

Responsible governance lies at the core of the Bank's identity. It is also considered the most important condition for creating long-term value for all shareholders, clients and employees. The Bank, however, does not have internal corporate governance rules in place. Instead, it applies the rules of the Croatian Banking Association. The Bank's Management Board believes that the Bank's organizational structure is suitable for performing operations in compliance with the valid regulations of the Republic of Croatia, and that it is also in line with the modern banking needs. The Management Board undertakes to continue making efforts to further strengthen the corporate governance principles and corporate culture in order to promote a merit- and results-based organizational environment. The Management Board and the Supervisory Board cooperate through transparent communication and regular meetings at which the Management Board presents all the required reports concerning the Bank's condition and business flow to the Supervisory Board, while the Supervisory Board provides the required support to the Management Board.

#### ***Corporate Governance***

The Bank's shareholders exercise their rights at the General Meeting. Participation is, however, restricted to the shareholders registered with the Central Depository Agency. Each share entitles the holder to one vote at the General Meeting, as well as to dividend payment and other rights envisaged under the law and the Bylaws of the Bank.



***General Meeting***

The General Meeting is convened at least once a year. The Notice to Convene is sent to individual shareholders via certified mail, or published in the Official Gazette. The General Meeting is usually convened in the first eight months of the business year, as prescribed under the Bylaws, but it can also be convened, either by the Management Board or the Supervisory Board, whenever the convening of the General Meeting is deemed in the interest of the Bank. The regular General Meeting is usually held in the first six months of the business year, and it is convened by the Management Board once the Supervisory Board adopts the Bank's annual financial statements and condition report. The regular General Meeting is responsible for duly noting both the annual financial statements and the annual Management Board report.

Based on the analysis of the submitted reports, the General Meeting passes decisions concerning the approval of activities of the Supervisory Board and the Management Board. The General Meeting passes decisions concerning the matters specifically envisaged under the law and the Bylaws of the Bank, particularly with regard to the appointment and dismissal of the members of the Supervisory Board, appointment of the auditor, increase or reduction in share capital, and other status changes. The General Meeting passes decisions on the basis of a simple majority of votes, unless prescribed otherwise under the law or the Bylaws of the Bank for specific decisions.

***Supervisory Board***

In order to ensure the well-being, successful operation and development of the Bank, regular and effective cooperation between the Bank's Management Board and Supervisory Board is ensured and maintained. The Management Board thus passes strategic decisions subject to approval of the Supervisory Board. As a result, pursuant to the provisions of the law, the Bylaws of the Bank and the Rules of Procedure of the Supervisory Board, certain decisions, which may only be passed if approved by the Supervisory Board, were passed in connection with, for example, changes in organizational structure, approval of large exposures, appointment of the auditor, acquisition and disposal of real estate, opening and closing of branches, membership in interest companies, and drafting of annual plans and budgets. An essential element of effective cooperation between these two governing bodies is regular communication based on comprehensive and detailed reports, and unofficial interactions. On 31 December 2019, the Supervisory Board comprised five members, including the President and the Vice President. Supervisory Board members are appointed by the General Meeting. Pursuant to applicable regulations, the Supervisory Board must have one independent member. Two members of the Supervisory Board resigned in 2020 for personal reasons. The smallest required number of Supervisory Board members prescribed by the Bylaws, which is three, was not brought into question. The Supervisory Board supervises the operations of the Bank, appoints and dismisses the members of the Management Board, ensures guidance in the drafting of the Bank's business policy and actively contributes to its implementation. Supervisory Board members receive a fee for their work, which is determined on the basis of the decision passed by the Bank's General Meeting.

***Prevention of Conflicts of Interest in the Work of the Supervisory Board***

In performing their activities, all members of the Supervisory Board are required to act in the best interest of the Bank, i.e. in a manner that ensures protection of the Bank's interests. In order to prevent conflicts of interest, the Supervisory Board applies the same rules as the Management Board.

***Committee Established within the Bank's Supervisory Board***

In order to ensure comprehensive supervision of the Bank's activities, the Supervisory Board has internally established a Risk and Audit Committee. The Risk and Audit Committee, whose duties and responsibilities are prescribed under the Audit Act and the Credit Institutions Act, discusses various matters in accordance with the relevant applicable regulations, particularly those associated with financial statements, the processes and the effectiveness of the internal audit function and the internal control system, risk management, as well as oversight of the financial statement audit procedure and activities of independent auditors.

***Management Board***

The Bank's Management Board is composed of two members, including the President, who is responsible for managing the activities of the Management Board, as well as for coordination of business functions and delivery of reports to the Supervisory Board and the General Meeting in the name of the Management Board. The Management Board manages the Bank's affairs on its own responsibility. More precisely, the President represents the Bank individually and independently, while the other member of the Management Board represents the Bank jointly with the President. When representing the Bank, the members of the Management Board are required to act in compliance with the restrictions prescribed under the Bank's Bylaws, decisions of the Supervisory Board and the General Meeting, and the Rules of Procedure of the Management Board. In performing management activities, the Management Board ensures that the Bank acts in compliance with all the applicable laws and industry standards, particularly with regard to the monitoring of all risks to which it is exposed and its compliance with and ability to ensure an adequate level of capital in line with the prescribed capital requirements. The Bank's Management Board is also responsible for ensuring proper and accurate preparation of financial statements in accordance with the accounting regulations and standards, the laws of the Republic of Croatia, and the rules issued by the Croatian National Bank.

***Prevention of Conflicts of Interest in the Work of the Management Board***

By acting in compliance with the relevant regulations and internal rules, the Management Board ensures that conflicts of interest are managed in a transparent and effective manner. To this end, the members of the Management Board comply with the applicable regulations and internal acts regulating their relationship with the Bank at all levels. In managing the Bank's affairs, the members of the Management Board may not pass or enforce decisions which are contrary to or in conflict with the interests of the Bank, including the use of the confidential data for the purpose of achieving personal gains. And finally, in managing the Bank's affairs, the Management Board is supported by the Assets and Liabilities Board, the Credit Board, and the Asset Quality Control Board.

***Internal Control System***

With the aim of protecting the Bank's assets and overall operations, an internal control system has been put in place. The established internal control system is in line with the applicable regulations but should be further improved in order to ensure maximum operational effectiveness, reliability of financial reports and ongoing compliance with the statutory and subordinate regulations and good business practices, primarily for the purpose of ensuring adequate credit and operational risk management in a market marked by high NPL levels and reduced judicial system efficiency, and consequently reducing the number and length of the related court procedures. Besides the members of the Supervisory Board and the members of the Management Board, all organizational parts of the Bank participate, either directly or indirectly, in the implementation of the relevant controls.

***Timely and Transparent Reporting***

The Bank makes special efforts to ensure timely and complete communication with the Croatian National Bank, which is performed through periodic reports and delivery of all other relevant documents and data.

**Banka Kovanica d.d.**  
**Statement of comprehensive income**

for the year ended 31 December 2019

	<b>Note</b>	<b>2019</b> <b>HRK'000</b>	<b>2018</b> <b>HRK'000</b>
Interest income		82,296	75,055
Interest expense		(15,632)	(15,907)
<b>Net interest income</b>	<b>4</b>	<b>66,664</b>	<b>59,148</b>
Fee and commission income		8,633	8,469
Fee and commission expense		(2,476)	(2,225)
<b>Net fee and commission income</b>	<b>5</b>	<b>6,157</b>	<b>6,244</b>
Foreign exchange differences – net	6	1,320	1,201
Realised (losses)/gains from financial assets at fair value through other comprehensive income	17	30	(10)
Realised (losses)/gains from available-for-sale financial assets	17	97	-
Other operating income	7	2,852	2,937
Impairment charge for credit losses – net	8	(14,686)	(16,906)
Administrative expenses	9	(41,039)	(34,657)
Other operating expenses	10	(3,891)	(5,900)
<b>Profit before tax</b>		<b>17,504</b>	<b>12,057</b>
Income tax	11	(2,812)	(3,451)
<b>Profit after tax</b>		<b>14,692</b>	<b>8,606</b>
Unrealised gains from financial assets at fair value through other comprehensive income		1,892	497
<b>Other comprehensive income</b>		<b>1,892</b>	<b>497</b>
<b>Total comprehensive income</b>		<b>16,584</b>	<b>9,103</b>
Earnings per share	12	4.1	2.4

*The accompanying accounting policies and notes form an integral part of these financial statements.*

**Banka Kovanica d.d.**  
**Statement of financial position**

as at 31 December 2019

	<b>Note</b>	<b>31 December 2019 HRK'000</b>	<b>31 December 2018 HRK'000</b>
<b>ASSETS</b>			
Cash	13	74,731	147,957
Obligatory reserve with the Croatian National Bank	14	78,311	72,810
Placements with banks	15	998	1,005
Loans and advances to customers	16	996,124	893,680
Financial assets at fair value through other comprehensive income	17	138,912	62,632
Property and equipment	18	16,355	10,964
Intangible assets	18	1,484	2,006
Reposessed collateral	19	23,024	32,008
Other assets	20	15,613	12,356
<b>Total assets</b>		<b>1,345,552</b>	<b>1,235,418</b>
<b>LIABILITIES</b>			
Deposits from customers	21	1,143,805	1,058,262
Due to banks	22	5,946	5,889
Hybrid instruments	23	39,725	39,510
Lease liabilities	26	5,656	-
Other liabilities	25	18,138	16,059
		<b>1,213,270</b>	<b>1,119,720</b>
<b>SHAREHOLDERS' EQUITY</b>			
Share capital	27	106,962	106,962
Treasury shares		(38)	(38)
Reserves		21,023	10,525
Retained earnings/(Accumulated loss)		4,335	(1,751)
		<b>132,282</b>	<b>115,698</b>
<b>Total liabilities and shareholders' equity</b>		<b>1,345,552</b>	<b>1,235,418</b>

*The accompanying accounting policies and notes form an integral part of these financial statements.*

**Banka Kovanica d.d.**  
**Statement of changes in equity**

for the year ended 31 December 2019

	Share capital	Treasury shares	Capital reserves	Other reserves	Fair value reserves	Retained earnings/(a ccumulated loss)	Total
	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000
<b>Balance at 1 January 2018</b>	<b>106.962</b>	<b>(38)</b>	<b>-</b>	<b>5,007</b>	<b>(287)</b>	<b>5,307</b>	<b>116,951</b>
Reconciliation of retained earnings due to IFRS 9 adoption (Note 2.3.)	-	-	-	-	1	(10,357)	(10,356)
<b>Balance at 1 January 2018 after reconciliation</b>	<b>106.962</b>	<b>(38)</b>	<b>-</b>	<b>5,007</b>	<b>(286)</b>	<b>(5,050)</b>	<b>106,595</b>
Coverage of accumulated losses	-	-	-	-	-	-	-
Transfer to reserves	-	-	-	5,307	-	(5,307)	-
Contributions in equity	-	-	-	-	-	-	-
Profit for the year	-	-	-	-	-	8,606	8,606
Unrealised gains from financial assets at fair value through other comprehensive income	-	-	-	-	497	-	497
<b>Total comprehensive income</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>497</b>	<b>8,606</b>	<b>9,103</b>
<b>Balance at 31 December 2018</b>	<b>106,962</b>	<b>(38)</b>	<b>-</b>	<b>10,314</b>	<b>211</b>	<b>(1,751)</b>	<b>115,698</b>
<b>Balance at 1 January 2019</b>	<b>106,962</b>	<b>(38)</b>	<b>-</b>	<b>10,314</b>	<b>211</b>	<b>(1,751)</b>	<b>115,698</b>
Coverage of accumulated losses	-	-	-	-	-	-	-
Transfer to reserves	-	-	-	8,606	-	(8,606)	-
Contributions in equity	-	-	-	-	-	-	-
Profit for the year	-	-	-	-	-	14,692	14,692
Unrealised gains from financial assets at fair value through other comprehensive income	-	-	-	-	1,892	-	1,892
<b>Total comprehensive income</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>1,892</b>	<b>14,692</b>	<b>16,584</b>
<b>Balance at 31 December 2019</b>	<b>106,962</b>	<b>(38)</b>	<b>-</b>	<b>18,920</b>	<b>2,103</b>	<b>4,335</b>	<b>132,282</b>

The accompanying accounting policies and notes form an integral part of these financial statements.

**Banka Kovanica d.d.**  
**Statement of cash flows**

for the year ended 31 December 2019

	<b>Note</b>	<b>2019</b> <b>HRK'000</b>	<b>2018</b> <b>HRK'000</b>
<b>Cash flow from operating activities</b>			
Profit for the year		14,692	8,606
Depreciation and amortisation	9, 18	2,691	1,574
Gain on sale of property and equipment and intangible assets		(9)	(471)
Impairment charge for credit losses – net	8	14,686	16,906
Result of financial assets at fair value through other comprehensive income		355	(1,193)
Other non-cash items		987	(672)
<b>Operating result before changes in operating assets</b>		<b>32,402</b>	<b>24,750</b>
(Increase)/decrease in assets with the Croatian National Bank		(5,501)	(8,489)
(Increase) in loans and advances to customers		(117,084)	(111,448)
Decrease/(increase) in repossessed collateral and other assets		(9,510)	7,347
Increase/(decrease) in deposits from customers		85,543	109,898
(Decrease)/increase in hybrid instruments		215	(371)
(Decrease)/increase in other liabilities		1,938	(15,998)
<b>Net cash used in operating activities</b>		<b>(10,997)</b>	<b>5,689</b>
<b>Cash flow from investing activities</b>			
Purchase of property and equipment and intangible assets	18	(1,697)	(1,034)
Proceeds from sale of property and equipment and intangible assets		18	4,217
Proceeds from sale of repossessed collateral		15,256	4,139
Purchase of financial assets at fair value through other comprehensive income	18	(119,481)	(17,325)
Disposals of financial assets at fair value through other comprehensive income	18	44,570	-
<b>Net cash used in investing activities</b>		<b>(61,334)</b>	<b>(10,003)</b>
<b>Cash flow from financing activities</b>			
Increase/(decrease) in deposits from banks		-	14
Increase/(decrease) in bank borrowings		(488)	(2,786)
Increase in lease liabilities		(586)	
<b>Net cash inflow from financing activities</b>		<b>(1,074)</b>	<b>(2,772)</b>
Changes in expected credit losses on cash and cash equivalents		179	1,012
<b>Net decrease in cash and cash equivalents</b>		<b>(73,226)</b>	<b>(7,086)</b>
Cash and cash equivalents at beginning of year		147,957	154,031
<b>Cash and cash equivalents at end of year</b>	13	<b>74,731</b>	<b>147,957</b>

The accompanying accounting policies and notes form an integral part of these financial statements.

## **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, P. Preradovića 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 (leasing)
- 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.

### ***Management Board***

Nicola Ceccaroli	President
Ivan Mužić	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.

## **2. Basis of preparation**

### **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 the Republic of 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 (the 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 International Financial Reporting Standards as adopted by the European Union (IFRS) and the CNB refers to the recognition of provisions for impairment of financial assets. In accordance with CNB regulations, banks domiciled in the Republic of Croatia should recognise provisions on the portfolio basis at the minimally prescribed rates on balance sheet and off-balance sheet exposure to credit risk of counterparties for whom impairment on individual basis is not determined, while IFRS requires that provisions on the portfolio basis should be determined for expected credit 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 impairment amounts in line with CNB requirements may differ from those in line with IFRS requirements.

The Bank calculates impairment losses on individually identified loans to legal entities as the present value of expected future cash flows, discounted at the instrument's original effective interest rate, in accordance with IFRS, with the application of prescribed minimum amounts of provisions for impairment losses for specifically identified impaired exposures, as prescribed by the CNB, which may differ from the impairment losses calculated in accordance with IFRS.

The CNB requires the amortisation of the calculated discount, provided that it meets the definition, 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 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 financial assets at fair value through other comprehensive income. 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.



## **2.3 Adoption of new accounting standards**

### **(a) Adoption of new or revised standards and interpretations**

*IFRS 16 Leases* (issued on 13 January 2016 and effective for annual periods beginning on or after 1 January 2019)

For all leases, except for short-term leases and leases of low-value assets other than those which are subleased, previously classified as operating leases, the following applies:

- as at 1 January 2019 the Bank has recognised a lease liability measured at the present value of the remaining lease payments, discounted using the Bank's incremental borrowing rate as of 1 January 2019;
- for all leases, the Bank has elected to recognise a right-of-use asset at an amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to those leases recognised in the statement of financial position immediately before the date of initial application.

Low-value assets which are sub-leased are accounted for as right-of-use assets with the corresponding lease liability.

The Bank elected the following practical expedients:

- applying a single discount rate to a portfolio of leases with reasonably similar characteristics;
- relying on its previous assessment on whether leases are onerous applying IAS 37 immediately before 1 January 2019 as an alternative to performing an impairment analysis. The analysis of the onerous contracts as at 31 December 2018 has not resulted in a need to recognise an impairment allowance. The right-of-use assets as at 1 January 2019 were not adjusted for any impairment;
- it will not apply the new lessee accounting model to leases for which the lease term ends within 12 months after the date of initial application.

Instead, it has accounted for those leases as short-term leases.

The explanation of the difference between operating lease commitments disclosed as at 31 December 2018 when applying IAS 17 to the lease liabilities recognised as at 1 January 2019 is presented in the table below:

(in thousands of HRK)	1 January 2019
Operating lease commitments as at 31 December 2018 under IAS 17	<b>7,618</b>
Excluded short-term leases	(18)
The effect of discounting using the incremental borrowing rate at 1 January 2019	(1,728)
Lease liability as at 1 January 2019	5,872
Short-term portion	1,607
Long-term portion	4,265

## **2.3 Adoption of new accounting standards (continued)**

### *(b) New standards and interpretations not yet adopted*

The following amended standards became effective from 1 January 2019, but did not have any material impact on the Bank:

- *IFRIC 23 – Uncertainty over Income Tax Treatments* (issued on 7 June 2017 and effective for annual periods beginning on or after 1 January 2019)
- *Annual Improvements to IFRSs 2015-2017 cycle – amendments to IFRS 3, IFRS 11, IAS 12 and IAS 23* (issued on 12 December 2017 and effective for annual periods beginning on or after 1 January 2019).

Certain new standards and interpretations have been published that are not mandatory for 31 December 2019 reporting periods and have not been early adopted by the Bank.

*Amendments to the Conceptual Framework for Financial Reporting (effective for annual periods beginning on or after 1 January 2020).* The revised Conceptual Framework includes a new chapter on measurement; guidance on reporting financial performance; improved definitions and guidance – in particular the definition of a liability; and clarifications in important areas, such as the roles of stewardship, prudence and measurement uncertainty in financial reporting.

*Definition of materiality – Amendments to IAS 1 and IAS 8 (effective for annual periods beginning on or after 1 January 2020).* The amendments clarify the definition of material and how it should be applied by including in the definition guidance that until now has featured elsewhere in IFRS. In addition, the explanations accompanying the definition have been improved. Finally, the amendments ensure that the definition of material is consistent across all IFRS Standards. Information is material if omitting, misstating or obscuring it could reasonably be expected to influence the decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity. The Bank is currently assessing the impact of the amendments on the financial statements.

Unless otherwise described above, the new standards and interpretations are not expected to affect significantly the Bank's financial statements.

## **2.4 Critical accounting estimates and judgements**

In applying 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.

According to the requirements of IFRS 9, all receivables carried at amortised cost must be classified into one of the three stages based on risk criteria. As explained in the previous paragraphs, receivables in default are classified in stage 3, receivables with a significant increase in credit risk are classified in stage 2, while all other receivables are included in stage 1. The stated criteria will be clearly defined below.

### **a) Default**

Default occurs in one or both of the following events:

- The client's material liability is 90 days past due,
- It is probable that the client will not fully meet contractual obligations.

The Bank has established a systemic process ensuring recognition of default status at the client level.

The client level implies that in the case of the client's default on any risk exposure, all the client's balance sheet and off-balance exposures shall be considered defaulted. In the event of the client's default, the Bank systematically assesses whether the default of the client (as the principal debtor) has resulted in a deteriorated financial position of the guarantors. In case there is an obvious uncertainty as to the payments of the overall loan exposure by the client's guarantors, such guarantors shall also be considered defaulted. In that case the default status is also determined at the client level.

The same principle applies to a group of related parties, where the default of one client may cause deterioration in the financial position of other clients, regardless of whether they are guarantors or not. Therefore, for each client in that group, it is individually estimated whether the default of one or more members of a group of related parties significantly deteriorates the financial position of that client, and therefore obligations are not expected to be fully settled without realising the collateral. In that case the client is considered defaulted.

## **2.4. Critical accounting estimates and judgements (continued)**

### **b) Significant increase in credit risk ("SICR")**

Bearing in mind that IFRS 9 does not clearly define the "significant increase in credit risk" and taking into account that the Bank must use all available information according to the same requirements, in this item a significant increase in credit risk will be defined, considering the availability of information, the development of the Bank's risk management system, as well as the Bank's portfolio size and structure.

The Bank considers receivables with a significant increase in credit risk to be those receivables that meet at least one of the following conditions:

- delay in payment over 30 days,
- restructured placement,
- blocked account,
- client deceased.

## **3. Significant accounting policies**

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

### **3. Significant accounting policies (continued)**

#### **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.

### **3. Significant accounting policies (continued)**

#### **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 2019	EUR 1 = HRK 7.442580	USD 1 = HRK 6.669861
31 December 2018	EUR 1 = HRK 7.417575	USD 1 = HRK 6.469192

### **3. Significant accounting policies (continued)**

#### **3.6. Cash and cash equivalents**

For the purposes of the statement of cash flows, 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 the 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.

#### **3.7. Financial assets**

All types of financial assets are classified entirely using two criteria:

- business model for managing the financial assets
- the contractual cash flow characteristics of the financial assets

Types of business models for managing financial assets:

- business model whose objective is to hold assets solely to collect the contractual cash flows (hold-to-collect) under which financial assets are managed to realise cash flows by collecting contractual payments over the life of the instrument and not for sale in order to realise profit. The objective of an entity's business model might be to hold financial assets in order to collect contractual cash flows, even if the financial assets are sold or expected to be sold in future periods, provided that they are infrequent (even if they are significant in value) or insignificant in value, both individually or in aggregate (even if they are frequent).
- business model whose objective is both to collect contractual cash flows and sell financial assets (hold-to-collect and sell) to manage everyday liquidity needs, maintain a particular interest yield profile or match the duration of financial assets and liabilities
- Other business models include assets that are not held in the hold-to-collect business model or the hold-to-collect and sell business model. In this model, financial assets are measured at fair value through profit or loss, and financial assets are managed in order to realise cash flows through the sale of assets.

Depending on the business model of financial asset management and the contractual characteristics of cash flows, financial assets are classified as:

- Financial assets subsequently measured at fair value through profit or loss
- Financial assets subsequently measured at amortised cost
- Financial assets subsequently measured at fair value through comprehensive income (FVOCI):
  - FVOCI – debt securities
  - FVOCI – equity securities

### **3. Significant accounting policies (continued)**

#### **3.7. Financial assets**

Financial assets at amortised cost - are subsequently measured at amortised cost if both of these conditions are met:

- the financial assets are held in the business model whose purpose is to hold a financial asset for the purpose of collecting contractual cash flows (hold to collect) and
- based on the contractual terms of financial assets, on specific dates cash flows are generated that are solely payments of principal and interest (SPPI).

Financial assets at fair value through OCI - they are subsequently measured at fair value through other comprehensive income if both of these conditions are met:

- the financial assets are held in the business model for the purpose of collecting contractual cash flows and selling financial assets (hold to collect and sell); and
- based on the contractual terms of financial assets, on specific dates cash flows are generated that are solely payments of principal and interest (SPPI), if debt securities are involved.

Financial assets are measured at fair value through profit or loss unless they are measured at:

- amortised cost or
- at fair value through other comprehensive income

#### **Recognition of financial assets**

All financial assets including derivative instruments are recognised in the balance sheet when the Bank becomes party to a binding agreement on financial assets.

Purchase and sales transactions of financial instruments (foreign exchange, securities and similar financial instruments), which are spot transactions or transactions where the period from the trading date to the settlement date is not longer than the one established by generally accepted convention, are recorded in the Bank's balance sheet at the settlement date. Considering the above, acquired financial assets are recognised or recorded on appropriate balance sheet accounts at the date the transaction value is settled with the counterparty, and from the trading date to the settlement date, they are recorded on off-balance sheet accounts.

For the purpose of determining the foreign exchange position, all spot transactions denominated in foreign currencies and with foreign currency clause are recorded on the trading day on off-balance sheet accounts (account groups 96 and 99).

Financial assets are initially measured at their fair value, which, in the case of financial assets not designated at fair value through profit or loss, increases or decreases by transaction costs directly attributable to the acquisition or issue of a financial asset.

#### **Subsequent measurement**

Upon initial recognition, all financial assets classified as at fair value through profit or loss and assets at fair value through OCI are stated at fair value other than those financial assets whose price is not quoted in an active market and whose fair value cannot be reliably determined. The value of such financial assets is carried at cost, including transaction costs, less any amortisation and impairment losses. Loans and receivables and held-to-maturity assets are measured at amortised cost less impairment losses. Amortised cost is calculated using the effective interest rate method. Premiums and discounts, including initial transaction costs, are included in the relevant instrument's carrying amount and are amortised based on the instrument's effective interest.

The fair value of financial assets is based on the market price on the balance sheet date, without deducting transaction costs. If the market price is not available, the fair value of the asset is measured at cost.



### **3. Significant accounting policies (continued)**

#### **3.7. Financial assets (continued)**

Where the discounted cash flow method is used, estimated future cash inflows are based on management's best estimates and the discount rate is the market rate effective at the balance sheet date and used for financial instruments with similar features and conditions.

The fair value of derivative instruments that are not traded in an active market is estimated based on the value of proceeds or expenditures that the Bank would have if it would terminate the contract at the balance sheet date, taking into account current market assessments and the counterparty's credit risk.

Gains or losses from financial assets at fair value through profit or loss are recognised in profit or loss.

Gains or losses from financial assets at fair value through other comprehensive income are recognised directly in equity except for impairment losses and foreign exchange differences until the derecognition of instruments, when cumulative gains and losses previously recognised in equity, are recognised in profit or loss.

#### **Loss on impairment of financial assets**

With a view to timely recognising losses, the impairment model reflects expected credit losses (ECL), i.e. for impairment it is no longer necessary for a credit event to have occurred. The amount of expected losses is updated by the Bank at each reporting date to reflect changes in credit risk since initial recognition.

As to the regularity in settlement of outstanding liabilities, the Bank's placements can be categorised into three basic groups:

- STAGE 1 – performing placements with no significant increase in the credit risk of the debtor's exposure upon initial recognition. For Stage 1 placements interest is recognised in the full amount in profit or loss, while impairment and provisions for exposures are made in an amount equalling 12-month expected credit losses.
- STAGE 2 – underperforming placements with a significant increase in the credit risk of the debtor's exposure upon initial recognition. For Stage 2 placements interest is recognised in the full amount in profit or loss, while impairment and provisions for exposures are made in an amount equalling lifetime expected credit losses.
- STAGE 3 – credit impaired placements with a significant increase in credit risk upon initial recognition. For Stage 3 placements impairment and provisions for exposures are made in the amount equalling lifetime expected credit losses, which are computed as the positive difference between the gross carrying amount of each exposure and the present value of the estimated debtor's future cash flows discounted using the effective interest rate.

Expected losses are measured on any of the following grounds:

- 12-month expected credit losses - part of lifetime expected credit losses which represents expected credit losses resulting from default in relation to a financial instrument and which may arise within a period of 12 months after the reporting date.
- Lifetime expected credit losses - losses arising from any default events over the expected lifetime of the financial instrument

### **3. Significant accounting policies (continued)**

#### **3.7. Financial assets (continued)**

The recoverable amount of loans and receivables and held-to-maturity investments is calculated as the present value of expected future cash flows, discounted at the original effective interest rate of the instrument. If future cash flows are expected within one year from the balance sheet date, cash flows do not have to be discounted.

The recoverable amount of the Bank's held-to-maturity investment securities and receivables is calculated as the present value of expected future cash inflows and outflows, discounted at the original effective interest rate, as explained in the policies of impairment of financial instruments.

The recognised impairment loss on securities or receivables held to maturity is charged if the subsequent increase in the recoverable amount can be objectively associated with an event that occurs after the recognition of the impairment loss. Income cannot exceed the original loss amount.

#### **Derecognition of financial assets**

When assets at fair value through OCI and at fair value through profit or loss are sold, they are derecognised, i.e. they are eliminated from the respective balance sheet accounts at the date the transaction is settled with the counterparty.

Held-to-maturity assets and loans and receivables are derecognised on the date when contractual rights to cash flows from financial assets expire, when financial assets are transferred or when the Bank loses control over them. Financial assets are transferred if and only if contractual rights to receive cash flows from financial assets are transferred or if the contractual right to receive cash flows from financial assets is retained, but the contractual obligation is assumed to pay cash flows to one or more recipients.

#### **3.8. Special financial instruments**

##### ***Investments in debt securities***

Debt securities include bills of exchange, papers and bonds with floating or fixed interest rates and other debt-backed debt instruments regardless of who the issuer is. Debt securities are quoted on behalf of the bearer and are issued in series (there are several securities of the same characteristics).

Debt securities may be classified at acquisition in any of the existing categories of financial assets, depending on the specifics of the debt security and in accordance with the above-mentioned classification criteria.

Debt securities classified as financial assets at fair value through profit or loss or at fair value through other comprehensive income are, as a minimum, reconciled with the estimated or fair value at the end of the month. For debt securities whose price is quoted in an active market, fair value is determined on the basis of the price valid on the revaluation date (as a minimum on a monthly basis, on the last day of the month).

Debt securities acquired with an intention to hold to maturity are carried at amortised cost less impairment losses. Amortised cost is calculated using the effective interest rate method. Discounts and premiums, including initial transaction costs, are included in the carrying amount of the instrument, they are amortised on the basis of the effective interest rate and are recognised as interest income or expense. In the business records, the principal, discount or premium are recorded separately, and the corresponding interest is recorded per each security.

### **3. Significant accounting policies (continued)**

### **3.8. Special financial instruments (continued)**

The Bank will reclassify financial assets if it changes its business model in order to manage these financial assets. These changes are expected to be very infrequent. Such changes are determined by senior management based on external and internal changes. They must be significant to the Bank's operations and demonstrable to external parties. The objective of an entity's business model must be changed before the reclassification date.

#### ***Investments in equity securities***

Equity securities comprise shares or interests in companies. Equity securities entitle the Bank to participate in the company's profits and assets after the rights of creditors and other financial providers are met.

Equity securities are classified as financial assets at fair value through profit or loss (assets held for trading and assets initially recognised at fair value through profit or loss) or as financial assets at fair value through other comprehensive income

Equity securities classified as financial assets at fair value through profit or loss (assets held for trading and assets initially recognised at fair value through profit or loss) and at fair value through other comprehensive income are adjusted to fair value, as a minimum at the end of the month. For equity securities quoted in an active market, the fair value is determined on the basis of the closing price on that market. If an equity security is not quoted in an active market, it can be recorded at fair value if the fair value can be measured reliably. It is considered that fair value can be measured reliably if:

- the change in value within a reasonable number of fair value estimates of the same instrument is not significant, or
- the probability of different estimates within a number of estimates can reasonably be estimated and used when estimating fair value.

If the number of reasonable estimates of the equity instrument's fair value is significant and the probability of different estimates cannot reasonably be estimated, such instrument is not measured at fair value but at cost.

#### ***Loans to credit institutions and customers***

Loans comprise current and non-current receivables based on:

- approved loans and advances
- acceptance credits
- payments made on guarantees and other warranties
- utilised credit lines
- repo loans

If there is a permanent deterioration in the value of the loans, due to existing objective evidence that the receivable will not be fully settled, a value adjustment (provision) of the placement is performed where potential losses are identified on an individual basis. In addition to these provisions, a provision is made for losses or impairment on a collective basis for placements classified in risk category A.

Provisions or impairment of the placements referred to in the previous paragraph are charged to provision costs.

### **3. Significant accounting policies (continued)**

#### **3.8. Special financial instruments (continued)**

When a loan is known to be uncollectable, all the necessary legal procedures have been completed and the final loss has been determined, the loan is written off. If impairment losses decrease in the following period due to collection, the collected amount is recognised in the income statement.

#### ***Contracts with the right to repurchase***

The Bank contracts purchases (sales) of investments by negotiating the resale (repurchase) of substantially the same investments at a certain date in the future at a fixed price. Investments purchased with a future resale obligation are not recognised in the balance sheet, but expenditures under these contracts are recognised as loans granted to banks or customers. It is also recorded that the purchased receivables are secured by appropriate security instruments from the repurchase agreement. Investments sold on the basis of a repurchase agreement continue to be recognised in the balance sheet in accordance with the accounting policy for assets at fair value through other comprehensive income or held-to-maturity assets, whichever is the most appropriate. Proceeds from the sale of investments are reported as liabilities to either credit institutions or customers.

The difference between the amount of sales and re-purchase is recognised on the basis of the calculation over the transaction period and is recorded as income in the income statement.

### **3.9. Income tax**

The tax expense comprises current tax and deferred tax. Current tax is the tax payable on the taxable income for the year, using tax rates at the balance sheet date, and any adjustments to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates in effect at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the unutilised tax loss can be utilised. The recorded tax loss can be utilised within 5 years after the year of its occurrence. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

### 3. Significant accounting policies (continued)

#### 3.10 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:

	2019	2018
	%	%
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.

#### ***Leases - applied until 1 January 2019***

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.

### **3.11 Leases**

#### ***Leases - applied from 1 January 2019***

The new standard IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases. All leases result in the lessee recognising the right to use an asset at the commencement date of the lease, and if lease payments are made over time, also recognising 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.

The Bank recognises: (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 statement of comprehensive income.

The Bank decided to apply the standard from its mandatory adoption date of 1 January 2019. The Bank has applied the simplified transition approach and will not restate comparative information for the year prior to first-time adoption. Right-of-use assets for property leases are measured on transition as if the new rules had always applied. All other right-of-use assets are measured at the amount of the lease liability on adoption (adjusted for any prepaid or accrued expenses).

At the commencement date, lease liabilities are measured at an amount equal to the present value of the following lease payments for the underlying right-of-use assets during the lease term:

- fixed payments (including in-substance fixed payments), less any lease incentives receivable;
- variable lease payments that are based on an index or a rate;
- amounts expected to be payable by the Bank under residual value guarantees;
- the exercise price of a purchase option if the Bank is reasonably certain to exercise that option;
- payments of penalties for terminating the lease, if the lease term reflects the Bank exercising that option.

The lease payments are discounted using the interest rate implicit in the lease, if that rate can be readily determined, or using the incremental borrowing rate of the Bank.

Each lease payment is allocated between the liability and finance cost. Lease liabilities are subsequently measured using the effective interest method. The carrying amount of the liability is remeasured to reflect any reassessment, lease modification or revised in-substance fixed payments.

The lease term is a non-cancellable period of a lease; periods covered by options to extend and terminate the lease are only included in the lease term if it is reasonably certain that the lease will be extended or not terminated.

### **3. Significant accounting policies (continued)**

#### ***Leases - applied from 1 January 2019***

Right-of-use assets are measured initially at cost comprising the following:

- the amount of the initial measurement of the lease liability;
- any lease payments made at or before the commencement date less any lease incentives received;
- any initial direct costs;
- restoration costs.

Subsequently, the right-of-use assets are measured at cost less accumulated depreciation and any accumulated impairment losses, and adjusted for remeasurement of the lease liability due to reassessment or lease modifications.

The right-of-use assets are depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis. Depreciation periods for right-of-use assets are as follows:

- right-of-use property up to 5 years
- right-of-use equipment up to 3 years

Payments associated with all short-term leases and certain leases of all low-value assets are recognised on a straight-line basis as an expense in profit or loss. The Bank applies the exemption for low-value assets on a lease-by-lease basis i.e. for the leases where the asset is sub-leased, a right-of-use asset is recognised with corresponding lease liability; for all other leases of low-value assets, the lease payments associated with those leases will be recognised as an expense on a straight-line basis over the lease term.

Short-term leases are leases with a lease term of 12 months or less.

#### **3.12 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. Significant accounting policies (continued)**

#### **3.13 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. Provisions are increased in each period to reflect the passage of time. This increase is recognised as interest expense.

#### **3.14 Employee benefits**

##### **Pension obligations and post-employment benefits**

In the normal course of business through salary deductions, the Bank makes payments to mandatory pension funds on behalf of its employees as required by law. All contributions made to the mandatory pension funds are recorded as salary expense when incurred. The Bank does not have any other pension scheme and consequently, have no other obligations in respect of employee pensions. The Bank is not obliged to provide any other post-employment benefits.

##### **Bonuses**

The Bank approves the amounts of variable remuneration in accordance with the performance assessment and the decision of the Supervisory Board on the maximum allowed amount of variable remuneration on a yearly basis. Liabilities for bonuses are therefore not assessed but are recognised as an expense for the period to which they relate.

##### **Old-age retirement benefits and jubilee awards**

The Bank has no post-retirement benefit plans for its employees or management for payment of termination benefits or jubilee awards. 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.

#### **3.15 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.

### **3. Significant accounting policies (continued)**



### **3.16 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.

### **3.17 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.

**4. Net interest income**

	<b>2019</b>	<b>2018</b>
	<b>HRK'000</b>	<b>HRK'000</b>
<b>Interest income</b>		
Loans and advances:		
- to customers	77,101	72,990
- to banks	158	1
Securities	5,037	2,064
	<b>82,296</b>	<b>75,055</b>
<b>Interest expense</b>		
Deposits from customers	(11,818)	(12,401)
Hybrid instruments	(2,900)	(2,774)
Leases	(370)	-
Other borrowed funds	(544)	(732)
	<b>(15,632)</b>	<b>(15,907)</b>
<b>Net interest income</b>	<b>66,664</b>	<b>59,148</b>

**5. Net fee and commission income**

	<b>2019</b>	<b>2018</b>
	<b>HRK'000</b>	<b>HRK'000</b>
<b>Fee and commission income</b>		
Payment transactions	3,657	3,492
Guarantees and letters of credit given	66	54
Other	4,910	4,923
	<b>8,633</b>	<b>8,469</b>
<b>Fee and commission expense</b>		
Payment transactions	(409)	(372)
Other	(2,067)	(1,853)
	<b>(2,476)</b>	<b>(2,225)</b>
<b>Net fee and commission income</b>	<b>6,157</b>	<b>6,244</b>

**6. Foreign exchange differences – net**

	<b>2019</b>	<b>2018</b>
	<b>HRK'000</b>	<b>HRK'000</b>
Net foreign exchange gains on foreign exchange transactions	1,019	895
Foreign exchange gains on translation of balance sheet items to middle exchange rate	301	306
	<b>1,320</b>	<b>1,201</b>

**7. Other operating income**

	<b>2019</b>	<b>2018</b>
	<b>HRK'000</b>	<b>HRK'000</b>
Court costs refund	104	141
Income from sale of tangible assets	970	1,651
Court settlements and reimbursement of costs	836	413
Lease income	118	96
Other	824	636
	<b>2,852</b>	<b>2,937</b>

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

	<b>2019</b>	<b>2018</b>
	<b>HRK'000</b>	<b>HRK'000</b>
Loans and advances to customers (Note 16)	15,119	16,327
Collected receivables written off in previous years	(472)	(490)
Cash	(179)	(20)
Fair value through other comprehensive income	191	49
Other assets (Note 20)	7	1,131
Provision for contingent liabilities and commitments (Note 25)	20	(92)
	<b>14,686</b>	<b>16,906</b>

**9. Administrative expenses**

	<b>2019</b>	<b>2018</b>
	<b>HRK'000</b>	<b>HRK'000</b>
<b>Staff costs</b>		
Net salaries	11,866	11,655
Pension insurance contributions	3,204	3,176
Health insurance contributions	2,888	3,010
Other contributions and taxes on salaries	2,435	2,642
Other staff costs	1,496	1,106
	<b>21,889</b>	<b>21,589</b>
Other administrative expenses	11,878	11,168
Impairment of repossessed collateral (Note 19)	4,581	326
Depreciation and amortisation (Note 18)	2,691	1,574
	<b>41,039</b>	<b>34,657</b>

As at 31 December 2019, the Bank had 104 employees (2018: 97 employees).

**10. Other operating expenses**

	<b>2019</b>	<b>2018</b>
	<b>HRK'000</b>	<b>HRK'000</b>
Rental costs	203	1,914
Deposits insurance charge	3,499	3,288
Provisions for legal disputes (Note 25)	37	624
Accrued unused vacation	85	(23)
Other	67	97
	<b>3,891</b>	<b>5,900</b>

**11. Income tax**

	<b>2019</b>	<b>2018</b>
	<b>HRK'000</b>	<b>HRK'000</b>
Current tax	1,628	-
Deferred tax	1,184	1,281
<b>Income tax</b>	<b>2,812</b>	<b>1,281</b>

11. Income tax (continued)

	2019 HRK'000	2018 HRK'000
<b>Accounting profit before tax</b>	<b>17,504</b>	<b>12,057</b>
Effect of items increasing tax base	12,729	5,748
Effect of items decreasing tax base	(10,013)	(6,843)
<b>Tax base</b>	<b>20,220</b>	<b>10,962</b>
Income tax at 18%	3,151	2,170
Effect of recognition of deferred tax assets	(828)	-
Effect of release of unutilised deferred tax assets	489	1,281
<b>Income tax</b>	<b>2,812</b>	<b>3,451</b>
<b>Effective tax rate</b>	<b>16.06%</b>	<b>28.62%</b>

Movements in tax losses carried forward were as follows:

	2019 HRK'000	2018 HRK'000
<b>Tax losses carried forward from the previous period</b>	<b>(11,178)</b>	<b>(54,467)</b>
Utilisation of tax losses	11,178	7,511
Expiration of tax losses carried forward	-	35,778
<b>Tax loss available for carry forward in future periods</b>	<b>-</b>	<b>(11,178)</b>
Deferred tax assets at 18% (2018: 18%)	828	2,012
Recognised deferred tax assets (Note 20)	828	2,012

Movements in deferred tax assets were as follows:

	2019 HRK'000	2018 HRK'000
<b>At 1 January</b>	<b>2,012</b>	<b>5,463</b>
Release of unrecognised deferred tax assets	(2,012)	(3,451)
Recognition of deferred tax assets	828	-
<b>At 31 December</b>	<b>828</b>	<b>2,012</b>

The Bank utilised deferred tax assets on the basis of tax loss in the amount of HRK 2,012 thousand, and in accordance with tax regulations recognised new deferred tax assets based on temporary differences in the amount of HRK 828 thousand.

## 12. Earnings per share

### Basic

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

	<u>2019</u>	<u>2018</u>
Profit for the year (in HRK'000)	14,692	8,606
Weighted average number of shares in issue excluding treasury shares	<u>3,565,244</u>	<u>3,565,244</u>
Basic earnings per share – ordinary (in HRK)	<b>4.12</b>	<b>2.41</b>

### Diluted

Diluted earnings per share for 2019 and 2018 are equal to basic earnings per share, since the Bank did not have any convertible instruments or share options outstanding during either period.

## 13. Cash

	<u>31 December 2019</u>	<u>31 December 2018</u>
	<u>HRK'000</u>	<u>HRK'000</u>
Cash on hand	14,379	15,425
Cash on the clearing account	34,856	38,452
Foreign currency account	25,719	94,506
Expected credit losses	<u>(223)</u>	<u>(426)</u>
	<b>74,731</b>	<b>147,957</b>

## 14. Obligatory reserve with the Croatian National Bank

	<u>31 December 2019</u>	<u>31 December 2018</u>
	<u>HRK'000</u>	<u>HRK'000</u>
Earmarked obligatory reserve:		
- in HRK	78,507	72,992
Expected credit losses	<u>(196)</u>	<u>(182)</u>
	<b>78,311</b>	<b>72,810</b>

The obligatory reserve rate as at 31 December 2019 was 12% of HRK and foreign currency deposits, loans taken and debt securities issued (31 December 2018: 12%).

15. Placements with banks

	31 December 2019 HRK'000	31 December 2018 HRK'000
Loans	5,138	5,138
Deposits	1,018	1,015
	<b>6,156</b>	<b>6,153</b>
Expected credit losses	(5,158)	(5,148)
	<b>998</b>	<b>1,005</b>

Movement in the provision for identified losses:

	31 December 2019 HRK'000	31 December 2018 HRK'000
At 1 January	5,148	5,148
Additional provisions	10	-
At 31 December	<b>5,158</b>	<b>5,148</b>

16. Loans and advances to customers

	Stage 1	Stage 2	Stage 3	31 December 2019 HRK'000 Total	31 December 2018 HRK'000 Total
<b>Retail customers</b>	<b>820,842</b>	<b>7,674</b>	<b>73,364</b>	<b>901,880</b>	<b>861,381</b>
Housing loans	18,651	879	1,243	20,773	24,405
Cash general-purpose loans	759,764	6,571	48,154	814,489	770,731
Other loans	42,427	224	23,967	66,618	66,245
<b>Corporate customers</b>	<b>143,824</b>	<b>4,236</b>	<b>169,315</b>	<b>317,375</b>	<b>281,151</b>
Working capital loans	21,934	3,434	89,461	114,829	128,715
Factoring	72,790	629	3,029	76,448	42,882
Other loans	49,100	173	76,825	126,098	109,554
<b>Gross loans and advances</b>	<b>964,666</b>	<b>11,910</b>	<b>242,679</b>	<b>1,219,255</b>	<b>1,142,532</b>
<b>Retail customers</b>	<b>(7,572)</b>	<b>(648)</b>	<b>(54,818)</b>	<b>(63,038)</b>	<b>(78,397)</b>
Housing loans	(169)	(160)	(389)	(718)	(520)
Cash general-purpose loans	(6,914)	(476)	(35,074)	(42,464)	(53,343)
Other loans	(489)	(12)	(19,355)	(19,856)	(24,534)
<b>Corporate customers</b>	<b>(2,761)</b>	<b>(602)</b>	<b>(156,730)</b>	<b>(160,093)</b>	<b>(170,455)</b>
Working capital loans	(439)	(499)	(82,175)	(83,113)	(97,657)
Factoring	(1,340)	(90)	(2,714)	(4,144)	(2,166)
Other loans	(982)	(13)	(71,841)	(72,836)	(70,632)
<b>Provisions for impairment</b>	<b>(10,333)</b>	<b>(1,250)</b>	<b>(211,548)</b>	<b>(223,131)</b>	<b>(248,852)</b>
<b>Net loans and advances</b>	<b>954,333</b>	<b>10,660</b>	<b>31,131</b>	<b>996,124</b>	<b>893,680</b>

**16. Loans and advances to customers (continued)**

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

<b>2019</b>	<b>Retail customers HRK'000</b>	<b>Corporate entities HRK'000</b>	<b>Total HRK'000</b>
<b>At 1 January</b>	<b>78,398</b>	<b>170,454</b>	<b>248,852</b>
<b>IFRS 9 (Note 2.3.)</b>	<b>-</b>	<b>-</b>	<b>-</b>
Additional provisions (Note 8)	21,390	11,559	32,949
Stage 1	2,152	2,248	4,400
Stage 2	525	600	1,125
Stage 3	18,713	8,711	27,424
Collected amounts (Note 8)	(9,616)	(8,215)	(17,831)
Stage 1	(2,522)	(806)	(3,328)
Stage 2	(183)	(48)	(231)
Stage 3	(6,911)	(7,361)	(14,272)
Write-offs	(27,040)	(13,898)	(40,938)
Stage 3	(27,040)	(13,898)	(40,938)
Foreign exchange differences	(94)	193	99
<b>At 31 December</b>	<b>63,038</b>	<b>160,093</b>	<b>223,131</b>
<b>2018</b>	<b>Retail customers HRK'000</b>	<b>Corporate entities HRK'000</b>	<b>Total HRK'000</b>
<b>At 1 January</b>	<b>60,246</b>	<b>176,466</b>	<b>236,712</b>
<b>IFRS 9 (Note 2.3.)</b>	<b>9,372</b>	<b>1,504</b>	<b>10,876</b>
Additional provisions (Note 8)	19,681	9,988	29,669
Stage 1	2,598	965	3,563
Stage 2	742	-	742
Stage 3	16,341	9,023	25,364
Collected amounts (Note 8)	(10,201)	(3,141)	(13,342)
Stage 1	(4,703)	(424)	(5,127)
Stage 2	(346)	(154)	(500)
Stage 3	(5,152)	(2,563)	(7,715)
Write-offs	(65)	(13,538)	(13,603)
Stage 3	(65)	(13,538)	(13,603)
Foreign exchange differences	(636)	(824)	(1,460)
<b>At 31 December</b>	<b>78,397</b>	<b>170,455</b>	<b>248,852</b>

**17. Financial assets at fair value through other comprehensive income**

	<b>31 December 2019 HRK'000</b>	<b>31 December 2018 HRK'000</b>
Bonds and treasury bills	138,471	61,811
Equity securities – listed	303	681
Equity securities – unlisted	141	141
Expected credit losses	(3)	(1)
	<b>138,912</b>	<b>62,632</b>



# 17. Financial assets at fair value through other comprehensive income (continued)

Movements in financial assets at fair value through other comprehensive income are as follows:

	31 December 2019 HRK'000	31 December 2018 HRK'000
<b>At 1 January</b>	<b>62,632</b>	<b>43,616</b>
IFRS 9 (Note 2.3.)	-	539
Additions	119,290	17,325
Disposals	(44,570)	-
Unrealised gains/(losses)	1,703	(89)
Result of assets at fair value through other comprehensive income	127	(10)
Interest payment	557	239
Foreign exchange differences	(827)	1,012
<b>At 31 December</b>	<b>138,912</b>	<b>62,632</b>

## Bonds and treasury bills as at 31 December 2019:

Name	Maturity	Nominal amount (in thousands)	Currency	Carrying amount HRK'000	Unrealised gains/(losses) HRK'000
XS0757376610	21 March 2022	500	EUR	4,020	52
US857524AC63	22 January 2024	500	USD	3,635	24
IT0004536949	1 March 2020	2,500	EUR	19,002	105
ES0000012C46	31 October 2021	2,500	EUR	18,753	81
FR0011619436	25 May 2024	1,500	EUR	12,640	120
IT0005359846	15 February 2025	3,000	EUR	23,491	1,169
ES00000124W3	30 April 2024	2,500	EUR	22,209	271
PTOTEKOE0011	15 October 2025	4,000	EUR	34,721	(63)
				<b>138,471</b>	<b>1,759</b>

As at 31 December 2019, there were no bonds pledged as collateral in repurchase agreements.

18. Property and equipment and intangible assets

	Land and buildings	Electronic equipment	Right- of-use assets	Other assets	Total property and equipment	Software	Assets under construction	Leasehold improvements	Total intangible assets
Cost	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000
<b>At 31 December 2017</b>	<b>17,234</b>	<b>6,423</b>	-	<b>12,602</b>	<b>36,259</b>	<b>8,635</b>	<b>338</b>	<b>15,102</b>	<b>24,075</b>
Additions	-	176	-	290	466	111	201	775	1,087
Transfers	-	-	-	-	-	-	(519)	-	(519)
Disposals	(4,673)	(694)	-	(3,172)	(8,539)	-	-	(155)	(155)
<b>At 31 December 2018</b>	<b>12,561</b>	<b>5,905</b>	-	<b>9,720</b>	<b>28,186</b>	<b>8,746</b>	<b>20</b>	<b>15,722</b>	<b>24,488</b>
IFRS 16 first adoption	-	-	5,872	-	5,872	-	-	-	-
Additions	-	116	1,112	267	1,495	107	40	115	262
Transfers	-	-	-	-	-	-	(60)	-	(60)
Disposals	-	(263)	-	(264)	(527)	-	-	-	-
<b>At 31 December 2019</b>	<b>12,561</b>	<b>5,758</b>	<b>6,984</b>	<b>9,723</b>	<b>35,026</b>	<b>8,853</b>	<b>0</b>	<b>15,837</b>	<b>24,690</b>
<b>Accumulated depreciation</b>									
<b>At 31 December 2017</b>	<b>3,497</b>	<b>6,059</b>	-	<b>11,794</b>	<b>21,350</b>	<b>8,452</b>	-	<b>13,276</b>	<b>21,728</b>
Depreciation/amortisation charge for the period	284	136	-	245	665	260	-	649	909
Disposals	(992)	(694)	-	(3,107)	(4,793)	-	-	(155)	(155)
<b>At 31 December 2018</b>	<b>2,789</b>	<b>5,501</b>	-	<b>8,932</b>	<b>17,222</b>	<b>8,712</b>	-	<b>13,770</b>	<b>22,482</b>
Depreciation/amortisation charge for the period	237	133	1,328	269	1,967	30	-	694	724
Disposals	-	(259)	-	(259)	(518)	-	-	-	-
<b>At 31 December 2019</b>	<b>3,026</b>	<b>5,375</b>	<b>1,328</b>	<b>8,942</b>	<b>18,671</b>	<b>8,742</b>	-	<b>14,464</b>	<b>23,206</b>
<b>Net carrying amount</b>									
<b>As at 31 December 2018</b>	<b>9,772</b>	<b>404</b>	-	<b>788</b>	<b>10,964</b>	<b>34</b>	<b>20</b>	<b>1,952</b>	<b>2,006</b>
<b>As at 31 December 2019</b>	<b>9,535</b>	<b>383</b>	<b>5,656</b>	<b>781</b>	<b>16,355</b>	<b>111</b>	<b>0</b>	<b>1,373</b>	<b>1,484</b>

## 19. Repossessed collateral

Movements in repossessed collateral during the year:

	31 December 2019 HRK'000	31 December 2018 HRK'000
<b>As at 1 January</b>	<b>32,008</b>	<b>32,933</b>
Additions	6,246	2,404
Disposals	(10,649)	(3,003)
Impairment (Note 9)	(4,581)	(326)
<b>As at 31 December</b>	<b>23,024</b>	<b>32,008</b>

The Bank's repossessed collateral as at 31 December 2019 included property in the total amount of HRK 3,536 thousand (2018: HRK 4,492 thousand) which was not in the Bank's possession. The Bank repossessed this property in exchange for outstanding receivables and is currently involved in the process of obtaining physical possession.

## 20. Other assets

	31 December 2019 HRK'000	31 December 2018 HRK'000
Deferred tax assets	828	2,012
Receivables for court costs refunds	6,470	7,354
Trade receivables	2,929	4,735
Other prepayments	419	237
Prepaid expenses	2,064	1,969
Court receivables for sold property	8,940	4,647
Other	2,571	1,035
	<b>24,221</b>	<b>21,989</b>
Expected credit losses	(8,608)	(9,633)
	<b>15,613</b>	<b>12,356</b>

Movement in expected credit losses during the year:

	31 December 2019 HRK'000	31 December 2018 HRK'000
<b>As at 1 January</b>	<b>9,633</b>	<b>8,798</b>
IFRS 9 (Note 2.3.)	-	293
Additional provisions (Note 8)	2,374	3,042
Collected amounts previously provided for (Note 8)	(2,367)	(1,881)
Write-off	(1,032)	(619)
<b>As at 31 December</b>	<b>8,608</b>	<b>9,633</b>

## 21. Deposits from customers

Deposits comprise demand deposits and term deposits:

	31 December 2019 HRK'000	31 December 2018 HRK'000
<b>Demand deposits</b>		
Corporate customers	23,702	18,544
Retail customers	200,237	168,908
	<b>223,939</b>	<b>187,452</b>
<b>Time deposits</b>		
Corporate customers	14,018	7,550
Retail customers	905,848	863,260
	<b>919,866</b>	<b>870,810</b>
<b>Deposits from customers</b>	<b>1,143,805</b>	<b>1,058,262</b>
Current portion	509,512	537,430
Non-current portion	634,293	520,832

## 22. Due to banks

	31 December 2019 HRK'000	31 December 2018 HRK'000
Borrowings:		
- Croatian Bank for Reconstruction and Development	3,453	5,443
Deposits	2,493	446
	<b>5,946</b>	<b>5,889</b>
Current portion	2,497	446
Non-current portion	3,449	5,443

As at 31 December 2019 and 31 December 2018, all deposits from banks are current.

## 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 2019 HRK'000	31 December 2018 HRK'000
Foreign entities	30,078	29,895
Domestic entities	9,647	9,615

39,725

39,510

## 24. Repurchase agreements

As at 31 December 2019 and 31 December 2018, the Bank did not have any repurchase agreements.

## 25. Other liabilities

	31 December 2019 HRK'000	31 December 2018 HRK'000
Provision for legal disputes	398	361
Provision for contingent liabilities and commitments	222	202
Payables in the course of settlement	12,003	11,522
Trade payables	795	640
Employee payables – salaries and contributions	1,635	1,643
Liabilities for deposits insurance charge	885	739
Accrued unused vacation	367	282
Other liabilities	1,833	670
	<b>18,138</b>	<b>16,059</b>

Movement in provisions for legal disputes:

	31 December 2019 HRK'000	31 December 2018 HRK'000
<b>As at 1 January</b>	<b>361</b>	<b>12,340</b>
Additional provisions (Note 10)	37	637
Release of provisions (Note 10)	-	(13)
Payments made per court rulings	-	(12,603)
<b>As at 31 December</b>	<b>398</b>	<b>361</b>

Movement in provisions for contingent liabilities and commitments:

	31 December 2019 HRK'000	31 December 2018 HRK'000
<b>As at 1 January</b>	<b>202</b>	<b>148</b>
<b>IFRS 9 (Note 2.3.)</b>	<b>-</b>	<b>146</b>
Additional provisions (Note 8)	2,136	1,387
Release of provisions (Note 8)	(2,116)	(1,479)
<b>As at 31 December</b>	<b>222</b>	<b>202</b>

**26. Lease liabilities**

	31 December 2019 HRK'000	31 December 2018 HRK'000
Lease liabilities	5,656	-
	<b>5,656</b>	-
Current portion	1,261	-
Non-current portion	4,395	-

Liabilities under financial instruments relate to liabilities to banks, hybrid instruments and deposits from customers.

	Liabilities under financial instruments (996,906)	Lease liabilities -	Total debt (996,906)	Cash and cash equivalents 154,031	Net debt (842,875)
<b>At 1 January 2018</b>					
Cash flows	(106,755)	-	(106,755)	(6,074)	112,829
Balance at 31 December 2018	(1,103,661)	-	(1,103,661)	147,957	(955,704)
Reconciliation under IFRS 16	-	(5,872)	(5,872)	-	(5,872)
<b>At 1 January 2019</b>	<b>(1,103,661)</b>	<b>(5,872)</b>	<b>(1,109,533)</b>	<b>147,957</b>	<b>(961,576)</b>
Cash flows	(70,552)	585	(69,967)	(73,226)	(143,193)
Accrued interest	(15,263)	(369)	(15,632)	-	(15,632)
<b>At 31 December 2019</b>	<b>(1,189,476)</b>	<b>(5,656)</b>	<b>(1,195,132)</b>	<b>74,731</b>	<b>(1,120,401)</b>

**27. Shareholders' equity**

**Share capital**

As at 31 December 2019, the Bank's share capital amounted to HRK 106,962 thousand (31 December 2018: HRK 106,962 thousand), and it is divided among 3,565,397 ordinary shares (31 December 2018: 3,565,397) (VSK-R-A) with a nominal value of HRK 30 per share.

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

	31 December 2019		31 December 2018	
Shareholder	Number of shares	% in share capital	Number of shares	% in share capital
Cassa di Risparmio della Repubblica di San Marino	3,554,514	99.69	3,554,514	99.69
Treasury shares	153	0.00	153	0.00
Other	10,730	0.31	10,730	0.31
<b>Total</b>	<b>3,565,397</b>	<b>100.00</b>	<b>3,565,397</b>	<b>100.00</b>

## 28. Contingent liabilities and commitments

### Legal disputes

The Bank is currently subject to 8 legal proceedings. As at 31 December 2019, provisions for legal disputes for which the Bank anticipates outflow of economic benefits amount to HRK 398 thousand (2018: HRK 362 thousand).

### Capital commitments

As at 31 December 2019 and 31 December 2018, 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 2019 HRK'000</b>	<b>31 December 2018 HRK'000</b>
Guarantees	1,998	1,236
Loan and other commitments	12,993	13,761
<b>Total</b>	<b>14,991</b>	<b>14,997</b>

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.

## 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 2019 and 2018, transactions with related parties were as follows:

	<b>Supervisory Board, Management Board and their related parties</b>	
	<b>2019</b>	<b>2018</b>
	<b>HRK'000</b>	<b>HRK'000</b>
<b>Income and expenses</b>		
Interest income	1	2
Other operating income	104	94
Interest expense	27	34
Other operating expenses	4,756	5,001
<b>Loans</b>		
At 1 January	120	120
Increase	1	-
<b>As at 31 December</b>	<b>121</b>	<b>120</b>
<b>Deposits received</b>		
At 1 January	3,189	2,751
Increase	3,353	2,951
Decrease	(2,950)	(2,513)
<b>As at 31 December</b>	<b>3,592</b>	<b>3,189</b>

In 2019, gross salaries and other short-term benefits of the Management Board and the Supervisory Board amounted to HRK 4,756 thousand (2018: HRK 5,001 thousand). The total amount of retirement benefits in 2019 is HRK 794 thousand (2018: HRK 789 thousand).



**29. Related party transactions (continued)**

	<b>Cassa di Risparmio della Repubblica di San Marino</b>	
	<b>2019</b>	<b>2018</b>
	<b>HRK'000</b>	<b>HRK'000</b>
<b>Income and expenses</b>		
Interest income	-	-
Other operating income	-	10
Other operating expenses	(462)	(462)
Interest expense	(1,400)	(1,265)
<b>Given deposits and cash</b>		
As at 1 January	1,211	1,224
Increase	-	3
Decrease	(528)	(16)
<b>As at 31 December</b>	<b>683</b>	<b>1,211</b>
<b>Deposits received</b>		
As at 1 January	541	549
Increase	2,104	-
Decrease	-	(8)
<b>As at 31 December</b>	<b>2,645</b>	<b>541</b>
<b>Hybrid instruments</b>		
As at 1 January	17,600	17,697
Increase	142	-
Decrease	-	(97)
<b>As at 31 December</b>	<b>17,742</b>	<b>17,600</b>

As at 31 December 2019, the exposure towards the majority shareholder amounted to HRK 683 thousand, which represents 0.44% of the Bank's regulatory capital (2018: 0.82%, 2017: 0.88%, 2016: 0.00%, 2015: 15.36%). 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.

Interbank transactions between the Bank and the parent bank CRSM relate to short-term active and passive deposits.

In 2019, the Bank did not have short-term active and passive deposits with its parent bank CRSM, and therefore neither the Bank nor the parent bank CRSM generated profit through transfer pricing to avoid paying tax liabilities. The Bank has contractual hybrid instruments with its related parties Nekretnine plus and CRSM that have capital and liability characteristics in accordance with Article 63 of the Regulation (EU) No. 575/2013 of the European Parliament and of the Council with value dates, maturity dates and agreed interest.

**29. Related party transactions (continued)**

	<b>Nekretnine plus d.o.o.</b>	
	<b>2019</b>	<b>2018</b>
	<b>HRK'000</b>	<b>HRK'000</b>
<b>Income and expenses</b>		
Interest income	307	312
Other operating income	396	195
Other operating expenses	(526)	(526)
Interest expense	(680)	(678)
<b>Loans given</b>		
As at 1 January	6,001	6,202
Increase	49	-
Decrease	(112)	(201)
<b>As at 31 December</b>	<b>5,938</b>	<b>6,001</b>
<b>Deposits received</b>		
At 1 January	2,346	821
Increase	536	1,525
Decrease	(1,184)	-
<b>As at 31 December</b>	<b>1,698</b>	<b>2,346</b>
<b>Hybrid instruments</b>		
As at 1 January	9,615	9,730
Increase	32	-
Decrease	-	(115)
<b>As at 31 December</b>	<b>9,647</b>	<b>9,615</b>

### **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). 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.

#### **30.1. 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.

### **30.1. Credit risk (continued)**

The Bank calculates impairment provisions in accordance with the IFRS 9 Expected Credit Loss model (ECL model).

ECL (Expected Credit Loss) is the expected credit loss for the financial asset under review. According to the pattern, ECL is defined as lifetime expected credit loss of a financial instrument (Stage 2), but by limiting the T parameter for one year it can be easily redefined as 12-month expected credit loss (Stage 1). ECL for Stage 3 does not assume the use of such pattern and the parameters defined, therefore it is not subject to this part of the methodology.

EAD (Exposure At Default) represents the exposure as per financial instrument at the moment of default. From the presented pattern it is clear that EAD will not be constant over time, it will change with the passage of time, due to repayments (repayments per amortisation schedule as well as due to early repayments) and due to new withdrawals (e.g. lines of credit). Per IFRS 9 requirements, it is necessary to project the EAD over the life of a financial instrument, since keeping the EAD constant would result in a higher than realistic ECL, while for cases where the exposure is increasing, the usage of a constant EAD parameter would result in a lower than actual ECL.

MPD (Marginal Probability of Default) represents the marginal probability of default for a financial instrument in a given time period (t). The MPD estimate represents the most challenging area of provision calculation in accordance with IFRS 9. MPD over the life of a financial instrument should reflect all relevant factors that influence this probability, i.e. in addition to considering historical data based on the PD and DR (default rate) statistics, it is also necessary to include macroeconomic assumptions for the future period, all with a view to project ECL as realistically as possible. There are several possible approaches to MPD parameter modelling and this methodology provides two alternative approaches: the basic approach and the advanced approach. The basic approach is based on Markov chain matrices, it assumes generation of three base cases (the base, expansion, recession), after which macroeconomic assumptions are implemented by use of the z-shift model, while the time dimension is brought by multiplying the adequate matrices based on the projections for future periods. This model is simplified and it is recommended if historical data is not sufficiently representative for applying advanced approaches.

LDG (Loss Given Default) is a loss in case of a default status of a financial instrument. LGD also requires consideration of projections for future periods, if it is determined that projections of relevant factors influencing LGD indicate significant changes in this parameter, which would further reflect also on the level of calculated lifetime ECL. If it is determined that no significant changes are expected which would influence this parameter or if it is not possible to link the movement of relevant factors with the LGD, the appropriate solution may be maintaining this factor on the same level for future periods. In accordance with IFRS 9, a collateral can no longer be used as an item decreasing the base for provision calculation, which implies that LGD should include all possible settlement alternatives for a certain receivable, i.e. it is necessary to approximate the comprehensive LGD which incorporates both collection (LGD unsecured) and realisation of collaterals (LGD secured). Furthermore, it is necessary to consider possible recoveries from NPL to PL status.

DF (Discount Factor) is the factor used for discounting throughout a certain period, based on the effective interest rate.

Other than the discount factor which is calculated in a familiar manner and which is based on the effective interest rate whose definition has not been changed, all other factors require certain modelling and should be considered individually.

Adequate modelling of parameters is necessary for a good calculation of the value adjustment and the approximation of each of the above parameters respecting the requirements imposed by IFRS 9 is set out below.

### **30.1. Credit risk (continued)**

Alternatively, the Bank can apply the Single Parameter Approach (SP).

#### **EAD model**

EAD represents the estimated gross carrying amount at the moment of default, considering cash flows of the financial instrument, as well as future withdrawals from the credit line until the date of default, i.e. over the life of the financial instrument. Although IFRS 9 does not explicitly require banks to model EAD, the expectation that the exposure to credit risk will evolve over time is key for an unbiased assessment of expected credit loss. The major challenge with EAD is to assess this parameter for financial instruments for which lifetime expected credit loss is calculated (Stage 2). By ignoring the expected decrease in the exposure, the expected credit loss can be overstated (e.g. for loans repaid successively), i.e. ignoring the expected increase in the exposure can lead to an understated expected credit loss (e.g. for credit line withdrawals).

In order to determine the lifetime expected credit loss, it is necessary to determine EAD for each year over the life of the financial instrument (and not only for one upcoming year as prescribed by Basel II).

In order to determine EAD, financial instruments can be divided in accordance with the following criteria:  
are there contractual cash flows?  
does a financial instrument have a defined maturity?

In order to calculate lifetime EAD, financial instruments can be divided into 4 categories:

Financial instruments with contractually defined cash flows and with defined maturity: cash loans, housing loans, consumer loans, investment loans, working capital loans, general-purpose loans as well as other loan types which the Bank has in its offering. For these financial instruments lifetime EAD is estimated based on existing contractual repayment schedules.

Financial instruments which do not have contractually defined cash flows and with defined maturity: frame credit lines with defined maturity. For these financial instruments, the Bank will use CCF factors as prescribed by relevant regulations.

Financial instruments which do not have contractually defined cash flows and without defined maturity: preference shares. These financial instruments are not specific to market conditions and this methodology does not provide a solution for EAD assessment of such assets.

### **30.1. Credit risk (continued)**

#### **PD model**

PD or Probability of Default is a probability that the client will enter the default status. The term lifetime PD represents an equal probability for the entire remaining life of a financial instrument. Marginal PD or MPD (t) represents a probability (unconditional) of entering into default within the time period t, while cumulative PD or CPD (t) represents the sum of all marginal PDs starting from initial recognition up to a given time moment t.

Considering the size and structure of the portfolio, as well as the availability of data, for PD calculation the Bank has selected an approach based on Markov chain transition matrices, using the homogeneous matrices in discrete time. The approach of this technique is to multiply migration matrices from one time period to another, while assuming that the migration schedule in the upcoming period depends solely on the current period schedule. While constructing the homogeneous matrices, transitions between days past due time buckets are observed.

Homogeneous matrices assume an identical migration structure from one time period to another, e.g. transitions between buckets are not dependant on the time period in which they are observed. Therefore, it is assumed that there is approximately the same migration schedule in a year t compared to a period t+1 or t-2. Discrete matrices follow the migration at period-end, comparing it to the end of the previous period (migrations during the year are not considered). For example, migrations on 31 December 2016 compared to 31 December 2015 are observed, or migrations on 31 July 2016 compared to 31 July 2015.

In order to introduce forward-looking information, the Bank converts PD calculated based on previously described matrices from TTC PD (Through-the-Cycle PD) to PIT PD (Point-in-Time PD). This is achieved by introducing macroeconomic variables.

Considering that comparing the Bank's data with the development of macroeconomic variables did not lead to a conclusion that there is a correlation between portfolio quality development and macroeconomic variables, the Bank makes its best estimate of expectations for portfolio quality development (in terms of PD development) as described in the upcoming paragraphs.

The Bank's management estimates the development of 3 macroeconomic parameters: % of change in GDP, % of change in unemployment rate and % of change in inflation rate. The values (scores) have been defined for each macroeconomic parameter, as well as the scale for transformation of scores to values for applying the z-shift. Management presents 3 scenarios of the development of parameters (basic, optimistic and pessimistic) as well as probability weights assigned to each defined scenario, therefore enabling the application of the probability weighted approach. This estimate is performed once annually.

Before preparing the matrices, the portfolio is segmented based on characteristics, considering that there should be sufficient data for constructing steady matrices. Based on current data, considering the portfolio size, structure and number of exposures with default status, it is estimated that the only possible segmentation is a split between legal entities (including companies and sole proprietors) and natural persons. In the upcoming revisions of this methodology, the Bank will assess whether the conditions will be met for an additional or more detailed portfolio segmentation.

The basic matrix is based on historical data and it is compiled using at least 3 annual matrices. It represents the weighted average of historical annual matrices in which the Bank defines weights considering the portfolio development per years, changes in the risk management system as well as other factors which may cause deviations in terms of portfolio development.

By applying the z-shift, the effects of macroeconomic variables development are added to the basic matrix in accordance with the scores set. From the basic matrix, a matrix of cumulative probabilities is created. The last column and row are cancelled (they do not affect the result) and for the values from the remaining matrix inverse values are found to which the macro variable score is added. The newly generated matrix is returned to the matrix of cumulative values, from which the final one-year matrix of marginal probabilities is derived – from which further, by multiplying with itself, PD parameter values are generated for the upcoming years until the final maturity of each financial instrument.

### **30.1. Credit risk (continued)**

#### **LGD model**

Considering the complexity of IFRS 9 requirements for the LGD model development, as well as the Bank's size, a relatively simple portfolio structure and small data sample size, for the purposes of the provision calculation the Bank will use LGD parameter values as defined by the Basel framework. According to assessment of regulatory LGD parameter values, the Bank will add a conservative factor of 5bps. LGD parameter values in use by the Bank:

retail secured – 40%  
retail unsecured – 80%  
corporate – 50%

#### **Unique parameter approach**

The Bank may apply the unique parameter SP which is estimated based on historical data on costs of risk for a certain portfolio. The SP parameter is assessed as the average cost of risk for a certain portfolio during at least 3 previous years. Such calculated parameter is applied for calculation using the following formula

for Stage 1:  $ECL = EAD \times SP$   
for Stage 2:  $ECL = EAD \times SP \times M$   
where M is the number of years to maturity.

#### **Calculation of impairment allowance**

After calculating the parameters, a provision for the impairment allowance is calculated. By using the data from the existing portfolio, after segmentation in accordance with calculated parameters (segments based on which PD and LGD parameters have been estimated), at first the criteria for classification into Stages are applied. After that, provisions for Stage 1 and Stage 2 exposures are calculated, while for Stage 3 exposures the impairment allowance is determined as the positive difference between the gross book value and present value of estimated future cash flows, discounted using the effective interest rate.

The Bank calculates an impairment provision on each reporting date (quarterly), while the PD and LGD parameters are estimated at least once a year and they are effective for a period of one year.

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. For all exposure groups, the financial analyst must provide an opinion on the financial position of the client based on the collected data and indicators, 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.

### **30.1. Credit risk (continued)**

#### **Calculation of impairment allowance (continued)**

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

For debt securities and other bills, external rating such as Standard & Poor's, Moody's, Fitch, BCA 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.

##### **30.1.2. 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 (stage1, stage 2, stage 3) 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.



### 30.1.3. Impairment and provisioning policies

In accordance with the CNB rules, 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

	2019		2018	
	Loans and advances	Provisions for impairment	Loans and advances	Provisions for impairment
	HRK'000	HRK'000	HRK'000	HRK'000
1. Fully recoverable placements	976,575	11,583	853,315	9,595
2. Partially recoverable placements	102,208	71,076	133,513	83,553
3. Unrecoverable placements	140,472	140,472	155,703	155,703
	<b>1,219,255</b>	<b>223,131</b>	<b>1,142,531</b>	<b>248,851</b>

#### Bank's rating

	2019		2018	
	Loans and advances (%)	Provision for impairment (%)	Loans and advances (%)	Provision for impairment (%)
	HRK'000	HRK'000	HRK'000	HRK'000
1. Fully recoverable placements	80.10	5.19	76.68	3.85
2. Partially recoverable placements	8.38	31.85	11.69	33.58
3. Unrecoverable placements	11.52	62.95	13.63	62.57
	<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.

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

					31 December 2019 HRK'000	31 December 2018 HRK'000
	No impact	Stage 1	Stage 2	Stage 3		
<b>Credit risk exposure relating to balance sheet assets</b>						
Cash on hand and balances with banks	14,379	60,352	-	-	74,731	147,957
Obligatory reserve with the Croatian National Bank	-	78,311	-	-	78,311	72,810
Placements with banks	-	998	-	-	998	1,005
Loans and advances to customers	-	954,333	10,660	31,131	996,124	893,680
Financial assets at fair value through other comprehensive income	444	138,468	-	-	138,912	62,632
Other assets	2,960	12,627	26	-	15,613	12,356
	<b>17,783</b>	<b>1,245,089</b>	<b>10,686</b>	<b>31,131</b>	<b>1,304,689</b>	<b>1,190,440</b>
<b>Credit risk exposure relating to off-balance sheet assets</b>						
Financial guarantees	-	1,964	34	-	1,998	1,236
Letters of credit	-	-	-	-	-	-
Loan commitments and other credit related liabilities	-	12,978	15	-	12,993	13,761
	-	<b>14,942</b>	<b>49</b>	-	<b>14,991</b>	<b>14,997</b>

The above table represents Bank's maximum exposure to credit risk as at 31 December 2019 and 2018, 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, 76.35% of the total maximum exposure is derived from loans and advances to banks and customers (2018: 75.07%).

### 30.1.5. Loans and advances

Loans and advances are summarised as follows:

	31 December 2019		31 December 2018	
	Loans and advances to customers	Loans and advances to banks	Loans and advances to customers	Loans and advances to banks
	HRK'000	HRK'000	HRK'000	HRK'000
Neither past due nor impaired	969,519	1,018	845,558	1,015
Past due but not impaired	7,056	-	7,756	-
Individually impaired	242,680	5,138	289,217	5,138
<b>Gross</b>	<b>1,219,255</b>	<b>6,156</b>	<b>1,142,531</b>	<b>6,153</b>
Less: provision for impairment	(223,131)	(5,158)	(248,851)	(5,148)
<b>Net</b>	<b>996,124</b>	<b>998</b>	<b>893,680</b>	<b>1,005</b>

The total impairment provision for loans and advances is HRK 223,132 thousand (2018: HRK 248,851 thousand) of which HRK 211,548 thousand (2018: HRK 239,256 thousand) represents individually impaired loans and the remaining amount of HRK 11,584 thousand (2018: HRK 9,595 thousand) represents the provision for the portfolio of fully recoverable placements. Further information of the impairment provision for loans and advances to banks and to customers is provided in Notes 15 and 16

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

	Retail customers	Corporate customers	Total loans and advances to customers	Loans and advances to banks
	HRK'000	HRK'000	HRK'000	HRK'000
<b>31 December 2019</b>				
<i>Neither past due nor impaired</i>	824,674	144,845	<b>969,519</b>	1,018
Fully recoverable placements	3,841	3,215	<b>7,056</b>	-
<i>Past due but not impaired</i>				-
Past due up to 30 days	2,174	2,555	<b>4,729</b>	-
Past due from 30 to 90 days	1,667	660	<b>2,327</b>	-
<i>Individually impaired</i>				
Individually impaired loans	73,365	169,315	<b>242,680</b>	5,138
<b>Total</b>	<b>901,880</b>	<b>317,375</b>	<b>1,219,255</b>	<b>6,156</b>
<b>31 December 2018</b>				
<i>Neither past due nor impaired</i>				
Fully recoverable placements	764,003	81,555	<b>845,558</b>	1,015
<i>Past due but not impaired</i>				
Past due up to 30 days	1,954	3,342	<b>5,296</b>	-
Past due from 30 to 90 days	2,255	205	<b>2,460</b>	-
<i>Individually impaired</i>				
Individually impaired loans	93,169	196,049	<b>289,218</b>	5,138
<b>Total</b>	<b>861,381</b>	<b>281,151</b>	<b>1,142,532</b>	<b>6,153</b>

### 30.1.5 Loans and advances (continued)

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 December 2019 HRK'000
	Gross exposure	Accumulated depreciation/ amortisation	Carrying amount	Exposure amount secured by collateral
<b>Retail customers</b>	<b>901,880</b>	<b>63,038</b>	<b>838,842</b>	<b>56,768</b>
Housing loans	20,773	718	20,055	20,800
Cash general-purpose loans	814,489	42,464	772,025	18,955
Other loans	66,618	19,856	46,762	17,013
<b>Corporate customers</b>	<b>317,375</b>	<b>160,093</b>	<b>157,282</b>	<b>132,565</b>
Working capital loans	114,829	83,113	31,716	51,284
Factoring	76,448	4,144	72,304	7,134
Other loans	126,098	72,836	53,262	74,147

**Total impairment of credit  
assets**

				31 December 2018 HRK'000
	Gross exposure	Accumulated depreciation/ amortisation	Carrying amount	Exposure amount secured by collateral
<b>Retail customers</b>	<b>861,381</b>	<b>78,397</b>	<b>782,984</b>	<b>61,502</b>
Housing loans	24,405	520	23,885	23,361
Cash general-purpose loans	770,731	53,343	717,388	19,609
Other loans	66,245	24,534	41,711	18,532
<b>Corporate customers</b>	<b>281,151</b>	<b>170,455</b>	<b>110,696</b>	<b>98,427</b>
Working capital loans	128,715	97,657	31,058	46,214
Factoring	42,882	2,166	40,716	4,707
Other loans	109,554	70,632	38,922	47,506
<b>Total impairment of credit assets</b>	<b>1,142,532</b>	<b>248,852</b>	<b>893,680</b>	<b>159,929</b>

30.1.5. Loans and advances (continued)

				HRK'000
	Stage 1	Stage 2	Stage 3	Total
<b>Housing loans</b>				
<b>Gross carrying amount as at 31 December 2018</b>	<b>22,494</b>	<b>505</b>	<b>1,406</b>	<b>24,405</b>
Movements:				
Stage 1 to Stage 2	(879)	879	-	0
Stage 1 to Stage 3	(60)	-	60	0
Stage 2 to Stage 3	-	(440)	440	0
Stage 2 to Stage 1	-	-	-	-
Stage 3 to Stage 1	-	-	-	-
No change	(2,904)	(65)	(663)	(3,632)
Write-offs	-	-	-	-
<b>Total gross carrying amount as at 31 December 2019</b>	<b>18,651</b>	<b>879</b>	<b>1,243</b>	<b>20,773</b>

				HRK'000
	Stage 1	Stage 2	Stage 3	Total
<b>Housing loans</b>				
<b>Expected credit losses as at 31 December 2018</b>	<b>205</b>	<b>32</b>	<b>283</b>	<b>520</b>
Movements:				
Stage 1 to Stage 2	(160)	160	-	0
Stage 1 to Stage 3	(43)	-	43	0
Stage 2 to Stage 1	-	-	-	-
Stage 3 to Stage 1	-	-	-	-
PD/LGD/EAD changes (Note 8)	168	(23)	-	145
Changes in assumptions and methodology (Note 8)	-	-	54	54
Foreign exchange differences and other movements	-	-	-	-
Total net impact on profit for the year	(36)	137	97	198
Other movements without impact on profit for the year				
Movements:				
Stage 2 to Stage 3	-	(9)	9	0
Stage 3 to Stage 2	-	-	-	-
Write-off	-	-	-	-
<b>Total expected credit losses as at 31 December 2019</b>	<b>169</b>	<b>160</b>	<b>389</b>	<b>718</b>

30.1.5. Loans and advances (continued)

				HRK'000
	Stage 1	Stage 2	Stage 3	Total
<b>Cash general-purpose loans</b>				
<b>Gross carrying amount</b>				
<b>as at 31 December 2018</b>	<b>695,548</b>	<b>13,524</b>	<b>61,659</b>	<b>770,731</b>
Movements:				
Stage 1 to Stage 2	(4,986)	4,986	-	0
Stage 1 to Stage 3	(10,169)	-	10,169	0
Stage 2 to Stage 3	-	(5,956)	5,956	0
Stage 2 to Stage 1	4,390	(4,390)	-	0
Stage 3 to Stage 1	2,185	-	(2,185)	0
Stage 3 to Stage 2	-	343	(343)	0
No change	72,796	(1,936)	(5,266)	65,594
Write-offs	-	-	(21,836)	(21,836)
<b>Total gross carrying amount as at 31 December 2019</b>	<b>759,764</b>	<b>6,571</b>	<b>48,154</b>	<b>814,489</b>

				HRK'000
	Stage 1	Stage 2	Stage 3	Total
<b>Cash general-purpose loans</b>				
<b>Expected credit losses as at 31 December 2018</b>	<b>6,395</b>	<b>1,003</b>	<b>45,945</b>	<b>53,343</b>
Movements:				
Stage 1 to Stage 2	(370)	370	-	0
Stage 1 to Stage 3	(2,535)	-	2,535	0
Stage 2 to Stage 1	40	(40)	-	0
Stage 3 to Stage 1	20	-	(20)	0
PD/LGD/EAD changes (Note 8)	3,364	2,024	-	5,388
Changes in assumptions and methodology (Note 8)	-	-	5,569	5,569
Foreign exchange differences and other movements	-	-	-	-
<b>Total net impact on profit for the year</b>	<b>519</b>	<b>2,354</b>	<b>8,084</b>	<b>10,957</b>
<b>Other movements without impact on profit for the year</b>				
Movements:				
Stage 2 to Stage 3	-	(2,908)	2,908	0
Stage 3 to Stage 2	-	27	(27)	0
Write-offs	-	-	(21,836)	(21,836)
<b>Total expected credit losses as at 31 December 2019</b>	<b>6,914</b>	<b>476</b>	<b>56,910</b>	<b>.42,464</b>

30.1.5 Loans and advances (continued)

				HRK'000
	Stage 1	Stage 2	Stage 3	Total
<b>Other loans to retail customers</b>				
<b>Gross carrying amount</b>				
<b>as at 31 December 2018</b>	<b>35,753</b>	<b>389</b>	<b>30,103</b>	<b>66,245</b>
Movements:				
Stage 1 to Stage 2	(135)	135	-	0
Stage 1 to Stage 3	(2,002)	-	2,002	0
Stage 2 to Stage 3	-	(111)	111	0
Stage 2 to Stage 1	52	(52)	-	0
Stage 3 to Stage 1	152	-	(152)	0
Stage 3 to Stage 2	-	-	-	-
No change	8,240	(137)	(2,895)	5,208
Write-offs	-	-	(5,204)	(5,204)
<b>Total gross carrying amount as at 31 December 2019</b>	<b>42,060</b>	<b>224</b>	<b>23,965</b>	<b>66,249</b>

				HRK'000
	Stage 1	Stage 2	Stage 3	Total
<b>Other loans to retail customers</b>				
<b>Expected credit losses as at 31 December 2018</b>	<b>420</b>	<b>14</b>	<b>24,101</b>	<b>24,534</b>
Movements:				
Stage 1 to Stage 2	(11)	11	-	0
Stage 1 to Stage 3	(1,763)	-	1,763	0
Stage 2 to Stage 1	1	(1)	-	0
Stage 3 to Stage 1	3	-	(3)	0
PD/LGD/EAD changes (Note 8)	1,809	6	-	1,815
Changes in assumptions and methodology (Note 8)	-	-	(1,321)	(1,321)
Foreign exchange differences and other movements	-	-	-	-
<b>Total net impact on profit for the year</b>	<b>39</b>	<b>16</b>	<b>439</b>	<b>494</b>
<b>Other movements without impact on profit for the year</b>				
Movements:				
Stage 2 to Stage 3	-	(18)	18	0
Stage 3 to Stage 2	-	-	-	-
Write-offs	-	-	(5,204)	(5,204)
<b>Total expected credit losses as at 31 December 2019</b>	<b>459</b>	<b>12</b>	<b>19,354</b>	<b>19,824</b>

30.1.5. Loans and advances (continued)

				HRK'000
Working capital loans	Stage 1	Stage 2	Stage 3	Total
Gross carrying amount as at 31 December 2018	16,285	641	111,789	128,715
Movements:				
Stage 1 to Stage 2	(61)	61	-	-
Stage 1 to Stage 3	(14)	-	14	-
Stage 2 to Stage 3	-	-	-	-
Stage 2 to Stage 1	97	(97)	-	-
Stage 3 to Stage 1	-	-	-	-
Stage 3 to Stage 2	-	-	-	-
No change	5,627	2,829	(8,466)	(10)
Write-offs	-	-	(13,876)	(13,876)
<b>Total gross carrying amount as at 31 December 2019</b>	<b>21,934</b>	<b>3,434</b>	<b>89,461</b>	<b>114,829</b>

				HRK'000
Working capital loans	Stage 1	Stage 2	Stage 3	Total
Expected credit losses as at 31 December 2018	328	58	97,272	97,657
Movements:				
Stage 1 to Stage 2	(3)	3	-	-
Stage 1 to Stage 3	-	-	-	-
Stage 2 to Stage 1	2	(2)	-	-
Stage 3 to Stage 1	-	-	-	-
PD/LGD/EAD changes (Note 8)	112	441	-	553
Changes in assumptions and methodology (Note 8)	-	-	(1,222)	(1,222)
Foreign exchange differences and other movements	-	-	-	-
<b>Total net impact on profit for the year</b>	<b>111</b>	<b>442</b>	<b>(1,222)</b>	<b>(669)</b>
<b>Other movements without impact on profit for the year</b>				
Movements:				
Stage 2 to Stage 3	-	-	-	-
Stage 3 to Stage 2	-	-	-	-
Write-offs	-	-	(13,876)	(13,876)
<b>Total expected credit losses as at 31 December 2019</b>	<b>439</b>	<b>500</b>	<b>82,174</b>	<b>83,112</b>



30.1.5 Loans and advances (continued)

				HRK'000
	Stage 1	Stage 2	Stage 3	Total
<b>Factoring</b>				
<b>Gross carrying amount as at 31 December 2018</b>	<b>41,150</b>	<b>-</b>	<b>1,732</b>	<b>42,882</b>
Movements:				
Stage 1 to Stage 2	-	-	-	-
Stage 1 to Stage 3	-	-	-	-
Stage 2 to Stage 3	-	-	-	-
Stage 3 to Stage 1	-	-	-	-
Stage 2 to Stage 1	-	-	-	-
Stage 3 to Stage 2	-	-	-	-
No change	31,640	629	1,297	33,566
Write-offs	-	-	-	-
<b>Total gross carrying amount as at 31 December 2019</b>	<b>72,790</b>	<b>629</b>	<b>3,029</b>	<b>76,448</b>

				HRK'000
	Stage 1	Stage 2	Stage 3	Total
<b>Factoring</b>				
<b>Expected credit losses as at 31 December 2018</b>	<b>472</b>	<b>-</b>	<b>1,164</b>	<b>2,165</b>
Movements:				
Stage 1 to Stage 2	-	-	-	-
Stage 1 to Stage 3	-	-	-	-
Stage 2 to Stage 1	-	-	-	-
Stage 3 to Stage 1	-	-	-	-
PD/LGD/EAD changes (Note 8)	867	89	-	956
Changes in assumptions and methodology (Note 8)	-	-	1,020	1,020
Foreign exchange differences and other movements	-	-	-	-
<b>Total net impact on profit for the year</b>	<b>867</b>	<b>89</b>	<b>1,020</b>	<b>1,976</b>
<b>Other movements without impact on profit for the year</b>				
Movements:				
Stage 2 to Stage 3	-	-	-	-
Stage 3 to Stage 2	-	-	-	-
Write-offs	-	-	-	-
<b>Total expected credit losses as at 31 December 2019</b>	<b>1,339</b>	<b>89</b>	<b>2,714</b>	<b>4,141</b>

30.1.5. Loans and advances (continued)

				HRK'000
	Stage 1	Stage 2	Stage 3	Total
<b>Other loans to corporate customers</b>				
<b>Gross carrying amount as at 31 December 2018</b>	<b>26,085</b>	<b>741</b>	<b>82,527</b>	<b>109,553</b>
Movements:				
Stage 1 to Stage 2	-	-	-	-
Stage 1 to Stage 3	-	-	-	-
Stage 2 to Stage 3	-	(640)	-	-
Stage 2 to Stage 1	-	-	-	-
Stage 3 to Stage 1	-	-	-	-
Stage 3 to Stage 2	-	-	-	-
No change	23,385	(129)	(6,320)	16,936
Write-offs	-	-	(22)	(22)
<b>Total gross carrying amount as at 31 December 2019</b>	<b>49,470</b>	<b>172</b>	<b>76,825</b>	<b>126,467</b>

				HRK'000
	Stage 1	Stage 2	Stage 3	Total
<b>Other loans to corporate customers</b>				
<b>Expected credit losses as at 31 December 2018</b>	<b>526</b>	<b>143</b>	<b>69,961</b>	<b>70,629</b>
Movements:				
Stage 1 to Stage 2	-	-	-	-
Stage 1 to Stage 3	-	-	-	-
Stage 2 to Stage 1	-	-	-	-
Stage 3 to Stage 1	-	-	-	-
PD/LGD/EAD changes (Note 8)	491	(75)	-	416
Changes in assumptions and methodology (Note 8)	-	-	1,848	1,848
Foreign exchange differences and other movements	-	-	-	-
<b>Total net impact on profit for the year</b>	<b>491</b>	<b>(75)</b>	<b>1,848</b>	<b>2,264</b>
<b>Other movements without impact on profit for the year</b>				
Movements:				
Stage 2 to Stage 3	-	(55)	55	0
Stage 3 to Stage 2	-	-	-	-
Write-offs	-	-	(22)	(22)
<b>Total expected credit losses as at 31 December 2019</b>	<b>1,017</b>	<b>13</b>	<b>71,842</b>	<b>72,871</b>

### 30.1.6. Repossessed collateral

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

### 30.1.7. 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 2019. For this table, the Bank has allocated exposures to regions based on the country of domicile of its counterparties.

	<b>Croatia</b> <b>HRK'000</b>	<b>European Union</b> <b>HRK'000</b>	<b>Other countries</b> <b>HRK'000</b>	<b>Total</b> <b>HRK'000</b>
Cash on hand and balances with banks	62,835	11,210	686	74,731
Obligatory reserve with the Croatian National Bank	78,311	-	-	78,311
Placements with banks	998	-	-	998
Loans and advances to customers	983,941	12,183	-	996,124
Financial assets at fair value through other comprehensive income	444	138,468	-	138,912
Other assets	15,304	309	-	15,613
<b>At 31 December 2019</b>	<b>1,141,833</b>	<b>162,170</b>	<b>686</b>	<b>1,304,689</b>
<b>At 31 December 2018</b>	<b>1,144,071</b>	<b>45,158</b>	<b>1,211</b>	<b>1,190,440</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.

	<b>Financial institutions</b> <b>HRK'000</b>	<b>Manu- facturing</b> <b>HRK'000</b>	<b>Properties</b> <b>HRK'000</b>	<b>Wholesale and retail trade</b> <b>HRK'000</b>	<b>Public sector</b> <b>HRK'000</b>	<b>Other industries</b> <b>HRK'000</b>	<b>Individuals</b> <b>HRK'000</b>	<b>Total</b> <b>HRK'000</b>
Placements with banks	998	-	-	-	-	-	-	998
Loans and advances to customers	7,286	34,396	24,320	43,595	14,299	33,386	838,842	996,124
Assets at fair value through OCI	138,771	-	141	-	-	-	-	138,912
Other assets	5,181	31	123	71	7,113	514	2,580	15,613
<b>At 31 December 2019</b>	<b>152,236</b>	<b>34,427</b>	<b>24,584</b>	<b>43,666</b>	<b>21,412</b>	<b>33,900</b>	<b>841,422</b>	<b>1,151,646</b>
<b>At 31 December 2018</b>	<b>35,219</b>	<b>30,590</b>	<b>19,749</b>	<b>35,733</b>	<b>43,696</b>	<b>20,148</b>	<b>784,538</b>	<b>969,673</b>

### **31. 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.

### 31.1. Currency 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 2019</b>					
<b>Assets</b>					
Cash on hand and balances with banks	44,314	19,186	2,482	8,749	74,731
Obligatory reserve with the CNB	78,311	-	-	-	78,311
Placements with banks	-	998	-	-	998
Loans and advances to customers	234,580	761,196	348	-	996,124
Financial assets at fair value through other comprehensive income	444	134,833	3,635	-	138,912
Other assets	14,125	1,488	-	-	15,613
<b>Total financial assets</b>	<b>371,774</b>	<b>917,701</b>	<b>6,465</b>	<b>8,749</b>	<b>1,304,689</b>
<b>Liabilities</b>					
Deposits from customers	242,030	886,637	6,423	8,715	1,143,805
Due to banks	34	5,912	-	-	5,946
Hybrid instruments	-	39,725	-	-	39,725
Lease liabilities	5,656	-	-	-	5,656
Other liabilities	17,769	369	-	-	18,138
<b>Total financial liabilities</b>	<b>265,489</b>	<b>932,643</b>	<b>6,423</b>	<b>8,715</b>	<b>1,213,270</b>
<b>Net on-balance sheet financial position</b>	<b>106,285</b>	<b>(14,942)</b>	<b>42</b>	<b>34</b>	<b>91,419</b>
Loan commitments	13,207	1,784	-	-	14,991

31.1. Foreign exchange risk (continued)

	HRK	EUR	USD	Other currencies	Total
	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000
<b>Balance at 31 December 2018</b>					
<b>Assets</b>					
Cash on hand and balances with banks	48,921	89,900	1,704	7,432	147,957
Obligatory reserve with the CNB	72,810	-	-	-	72,810
Placements with banks	-	1,005	-	-	1,005
Loans and advances to customers	185,579	708,013	88	-	893,680
Financial assets at fair value through other comprehensive income	822	57,125	4,685	-	62,632
Other assets	12,356	-	-	-	12,356
<b>Total financial assets</b>	<b>320,488</b>	<b>856,043</b>	<b>6,477</b>	<b>7,432</b>	<b>1,190,440</b>
<b>Liabilities</b>					
Deposits from customers	221,007	823,627	6,323	7,305	1,058,262
Due to banks	84	5,805	-	-	5,889
Hybrid instruments	-	39,510	-	-	39,510
Other liabilities	15,805	254	-	-	16,059
<b>Total financial liabilities</b>	<b>236,896</b>	<b>869,196</b>	<b>6,323</b>	<b>7,305</b>	<b>1,119,720</b>
<b>Net on-balance sheet financial position</b>	<b>83,592</b>	<b>(13,153)</b>	<b>154</b>	<b>127</b>	<b>70,720</b>
Loan commitments	9,789	3,972	-	-	13,761

At 31 December 2019, if the EURO had strengthened/weakened by 1% against the HRK by 1%, profit before tax would have been HRK 149 thousand lower/higher (31 December 2019: profit before tax would have been HRK 132 thousand lower/higher).

### 31.2. 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 2019</b>							
<b>Assets</b>							
Cash on hand and balances with banks	-	-	-	-	-	74,731	74,731
Obligatory reserve with the CNB	-	-	-	-	-	78,311	78,311
Placements with banks	-	-	-	-	-	998	998
Loans and advances to customers	76,805	39,987	94,951	172,965	611,416	-	996,124
Financial assets at fair value through profit or loss	1,348	-	18,739	22,706	95,675	444	138,912
Other assets	2,893	-	-	-	-	12,720	15,613
<b>Total financial assets</b>	<b>81,046</b>	<b>39,987</b>	<b>113,690</b>	<b>195,671</b>	<b>707,091</b>	<b>167,204</b>	<b>1,304,689</b>
<b>Liabilities</b>							
Deposits from customers	167,078	122,153	250,295	313,673	152,261	138,345	1,143,805
Due to banks	35	471	1,148	1,136	662	2,494	5,946
Hybrid instruments	-	-	9,638	5,396	24,691	-	39,725
Lease liabilities	-	-	-	-	5,656	-	5,656
Other liabilities	-	1,628	-	-	-	16,510	18,138
<b>Total financial liabilities</b>	<b>167,113</b>	<b>124,252</b>	<b>261,081</b>	<b>320,205</b>	<b>183,270</b>	<b>157,349</b>	<b>1,213,270</b>
<b>Net on-balance sheet financial position</b>	<b>(86,067)</b>	<b>(84,264)</b>	<b>(147,390)</b>	<b>(124,534)</b>	<b>523,821</b>	<b>9,853</b>	<b>91,419</b>

### 31.2. Interest rate risk (continued)

	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	Non-interest bearing HRK'000	Total HRK'000
<b>At 31 December 2018</b>							
<b>Assets</b>							
Cash on hand and balances with banks	-	-	-	-	-	147,957	147,957
Obligatory reserve with the CNB	-	-	-	-	-	72,810	72,810
Placements with banks	-	-	-	-	-	1,005	1,005
Loans and advances to customers	77,180	23,995	72,202	151,079	559,263	9,961	893,680
Financial assets at fair value through other comprehensive income	404	34,667	-	19,396	7,344	821	62,632
Other assets	-	-	-	-	-	12,356	12,356
<b>Total financial assets</b>	<b>77,584</b>	<b>58,662</b>	<b>72,202</b>	<b>170,475</b>	<b>566,607</b>	<b>244,910</b>	<b>1,190,440</b>
<b>Liabilities</b>							
Deposits from customers	117,079	85,666	343,954	256,935	132,733	121,895	1,058,262
Due to banks	35	472	1,504	2,212	1,226	440	5,889
Hybrid instruments	-	-	-	14,984	24,526	-	39,510
Other liabilities	-	-	-	-	-	16,059	16,059
<b>Total financial liabilities</b>	<b>117,114</b>	<b>86,138</b>	<b>345,458</b>	<b>274,131</b>	<b>158,485</b>	<b>138,394</b>	<b>1,119,720</b>
<b>Net on-balance sheet financial position</b>	<b>(39,530)</b>	<b>(27,476)</b>	<b>(273,256)</b>	<b>(103,656)</b>	<b>408,122</b>	<b>106,516</b>	<b>70,720</b>

### 31.3. 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.

#### 31.3.1. 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.



### 31.3.2. 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>31 December 2019</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	305,258	122,153	250,305	313,700	152,389	1,143,805
Due to banks	2,528	471	1,148	1,136	661	5,946
Hybrid instruments	-	-	9,638	5,396	24,691	39,725
Lease liabilities	-	-	-	-	5,656	5,656
Other liabilities	16,338	1,659	125	14	2	18,138
<b>Total liabilities</b> (contractual maturity dates)	<b>324,124</b>	<b>124,283</b>	<b>261,216</b>	<b>320,246</b>	<b>183,399</b>	<b>1,213,270</b>
<b>Total liabilities on unused loans</b> (expected maturity dates)	<b>2,928</b>	<b>2,165</b>	<b>7,113</b>	<b>687</b>	<b>100</b>	<b>12,993</b>

<b>31 December 2018</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	238,767	85,666	343,972	256,996	132,861	1,058,262
Due to banks	475	472	1,504	2,212	1,226	5,889
Hybrid instruments	-	-	-	14,984	24,526	39,510
Other liabilities	15,919	30	99	9	2	16,059
<b>Total liabilities</b> (contractual maturity dates)	<b>255,161</b>	<b>86,168</b>	<b>345,575</b>	<b>274,201</b>	<b>158,615</b>	<b>1,119,720</b>
<b>Total liabilities on unused loans</b> (expected maturity dates)	<b>4,925</b>	<b>1,906</b>	<b>6,055</b>	<b>775</b>	<b>100</b>	<b>13,761</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.

### 31.3.3. 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.

	<b>No later than 1 year HRK'000</b>	<b>1 to 3 years HRK'000</b>	<b>Over 3 years HRK'000</b>	<b>Total HRK'000</b>
<b>31 December 2019</b>				
Loan commitments	12,206	687	100	12,993
Guarantees, letters of credit and other	1,964	34	-	1,998
<b>Total</b>	<b>14,170</b>	<b>721</b>	<b>100</b>	<b>14,991</b>
<b>31 December 2018</b>				
Loan commitments	12,886	775	100	13,761
Guarantees, letters of credit and other	1,236	-	-	1,236
<b>Total</b>	<b>14,122</b>	<b>775</b>	<b>100</b>	<b>14,997</b>

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.

### **31.4. 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

	<b>31 December 2019</b>			<b>31 December 2018</b>		
	<b>Level 1</b>	<b>Level 2</b>	<b>Total</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Total</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>
Bonds	138,471	-	138,471	61,810	-	61,810
Shares	303	141	444	681	141	822
	<b>138,774</b>	<b>141</b>	<b>138,915</b>	<b>62,491</b>	<b>141</b>	<b>62,632</b>

**Banka Kovanica d.d.**  
Notes to the financial statements

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	
	2019 HRK'000	2018 HRK'000	2019 HRK'000	2018 HRK'000
<b>Financial assets</b>				
Placements with banks	998	1,005	998	1,005
Loans and advances to customers	996,124	893,680	996,124	893,680
Other assets	15,613	12,356	15,613	12,356
<b>Total financial assets</b>	<b>1,012,735</b>	<b>907,041</b>	<b>1,012,735</b>	<b>907,041</b>
<b>Financial liabilities</b>				
Deposits from customers	1,143,805	1,058,262	1,143,805	1,058,262
Due to banks	5,946	5,889	5,946	5,889
Hybrid instruments	39,725	39,510	39,725	39,510
Lease liabilities	5,656	-	5,656	-
Other liabilities	18,138	16,059	18,138	16,059
<b>Total financial liabilities</b>	<b>1,213,270</b>	<b>1,119,720</b>	<b>1,213,270</b>	<b>1,119,720</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.

*(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 applied to deposits of similar remaining maturities.

### **31.5. Capital 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%).

The table below summarises the composition of regulatory capital and the Bank's ratios at 31 December 2019 and 2018.

	<b>31 December 2019 HRK'000</b>	<b>31 December 2018 HRK'000</b>
<b>Regulatory capital</b>		
Share capital	106,924	106,924
Supplementary capital	28,842	34,103
Deductions from regulatory capital	17,847	5,948
<b>Regulatory capital</b>	<b>153,613</b>	<b>146,975</b>
<b>Structure of risk exposure</b>		
Exposure amount weighted by credit risk	807,358	762,255
Market risk exposure	269	363
Operating risk exposure	125,661	113,752
<b>Total risk exposure</b>	<b>933,288</b>	<b>876,370</b>
<b>Structure of capital requirements</b>		
Capital requirements for total capital ratio (8%)	74,663	70,110
Additional tier for capital protection (2.5%)	23,332	21,909
Additional tier for structural system risk (1.5%)	13,999	13,145
Capital requirements for total capital ratio (2019: 3.3%; 2018: 2.6%; 2017: 2.6%; 2016: 3.09%)	30,799	22,786
<b>Total capital requirements</b>	<b>142,793</b>	<b>127,950</b>
<b>Capital adequacy</b>	<b>16.46%</b>	<b>16.77%</b>

### **32. Events after the balance sheet date (subsequent events)**

The coronavirus pandemic crisis (COVID-19) and exceptional national and supranational measures in response to the global health emergency that materialised in early 2020 could cause severe socioeconomic disruption of systemic importance, even in the best-case scenario of rapid regression of the epidemic curve. The Bank considers this to be a non-adjusting post-balance sheet event. At the date of preparation of this annual report, it is not possible to estimate with sufficient approximation the medium and long-term impact on the budgets of governments, businesses and families due to this unprecedented crisis, with no historical precedents and lacking pre-determined models. The Bank immediately implemented a business continuity plan to ensure the safety of employees and key business processes, in accordance with the instructions of the competent authorities. When preparing its Interim Management Report, the Bank will conduct a preliminary analysis of budget execution and capital and liquidity adequacy in never-anticipated stress scenarios, taking into account recent exceptional government, community and central bank support measures. The Bank considers that the above situation will not affect the Bank's ability to continue as a going concern.

for the period from 1 January to 31 December 2019

## Supplementary information for the Croatian National Bank

Pursuant to the Decision on the structure and content of annual financial statements of credit institutions (Official Gazette no. 42/2018) forms required by the Croatian National Bank as at 31 December 2019 and for the year then ended are presented below.

Income statement				BAN-RDG form
For the period from 1 January 2019 to 31 December 2019				
Entity: BANKA KOVANICA D.D. VARAŽDIN				
Position	AOP mark	Note no.	Previous year	Current year
1	2	3	4	5
1. Interest income	069		75,055,443	82,333,747
2. Interest expense	070		15,906,511	15,670,118
3. Expenses from share capital repayable on demand	071		0	0
4. Dividend income	072		8,997	9,728
5. Fee and commission income	073		8,468,749	8,633,554
6. Fee and commission expense	074		2,225,259	2,476,570
7. Gains or losses on derecognition of financial assets and liabilities not carried at fair value through profit or loss, net	075		0	96,725
8. Gains or losses on financial assets and liabilities held for trading, net	076		894,614	1,019,241
9. Gains or losses on financial assets not traded and carried at fair value through profit or loss, net	077		-9,673	29,927
10. Gains or losses on financial assets and liabilities at fair value through profit or loss, net	078		0	0
11. Hedging gains/losses, net	079		0	0
12. Foreign exchange gains or losses, net	080		306,042	300,792
13. Gains or losses on derecognition of non-financial assets, net	081		885,378	-3,955,843
14. Other operating income	082		0	0
15. Other operating expenses	083		3,936,433	4,167,469
16. TOTAL OPERATING INCOME; NET (AOP 069 - 070 - 071 + 072 + 073 - 074 + 075 to 082 - 083)	084		63,541,347	66,153,714
17. Administrative expenses	085		33,395,745	32,664,201
18. Depreciation and amortisation	086		2,151,594	3,203,590
19. Gains or losses on changes, net	087		0	0
20. Provisions or reversal of provisions	088		426,049	56,099
21. Impairment or reversal of impairment of financial assets not carried at fair value through profit or loss	089		16,998,348	14,679,128
22. Impairment or reversal of impairment of investments in subsidiaries, joint ventures and associates	090		0	0
23. Impairment or reversal of impairment of non-financial assets	091		-251,458	0
24. Negative goodwill recognised in profit or loss	092		0	0
25. Share of profit or loss on investments in subsidiaries, joint ventures and associates accounted for using the equity method	093		0	0
26. Gains or losses on non-current assets and disposal group classified as held for sale not qualifying for classification as discontinued operations	094		723,788	211,821
27. PROFIT OR LOSS BEFORE TAX FROM CONTINUING OPERATIONS (AOP 084 - 085 - 086 + 087 - 088 do 091+ 092 to 094)	095		11,544,857	15,762,517
28. Tax expense or income relating to profit or loss from continuing operations	096		3,450,907	2,811,859
29. PROFIT OR LOSS AFTER TAX FROM CONTINUING OPERATIONS (AOP 095 - 096)	097		8,093,950	12,950,658
30. Profit or loss after tax from discontinued operations (AOP 099 - 100)	098		512,307	1,741,332
30.1. Profit or loss before tax from discontinued operations	099		512,307	1,741,332
30.2. Tax expense or income relating to discontinued operations	100		0	0
31. PROFIT OR LOSS FOR THE YEAR (AOP 097 + 098; 102 + 103)	101		8,606,257	14,691,990
32. Attributable to minority (non-controlling) interest	102		0	0
33. Attributable to owners of the parent company	103		0	0

**Statement of other comprehensive income**  
**For the period from 1 January to 31 December 2019**

<b>STATEMENT OF OTHER COMPREHENSIVE INCOME</b>				
<b>1. Profit or loss for the year (AOP 101)</b>	<b>104</b>		<b>8,606,257</b>	<b>14,691,990</b>
<b>2. Other comprehensive income (AOP 106 to 118)</b>	<b>105</b>		<b>497,401</b>	<b>1,891,855</b>
<b>2.1. Items that will not be reclassified to profit or loss (AOP 107 to 113 + 116 + 117)</b>	<b>106</b>		<b>0</b>	<b>0</b>
2.1.1. Tangible assets	107		0	0
2.1.2. Intangible assets	108		0	0
2.1.3. Actuarial gains/(losses) on defined benefit pension plans	109		0	0
2.1.4. Non-current assets and disposal groups held for sale	110		0	0
2.1.5. Share of other recognised income and expenses from entities accounted for using the equity method	111		0	0
2.1.6. Changes in fair value of equity instruments carried at fair value through other comprehensive income	112		0	0
2.1.7. Gains or losses on hedge accounting of equity instruments carried at fair value through other comprehensive income, net	113		0	0
2.1.8. Change in fair value of equity instruments carried at fair value through other comprehensive income	114		0	0
2.1.9. Changes in fair value of equity instruments carried at fair value through other comprehensive income	115		0	0
2.1.10. Changes in fair value of financial liabilities carried at fair value through profit or loss attributable to changes in credit risk	116		0	0
2.1.11 Income tax relating to items that will not be reclassified	117		0	0
<b>2.2. Items that may be reclassified to profit or loss (AOP 119 to 126 )</b>	<b>118</b>		<b>497,401</b>	<b>1,891,855</b>
2.2.1. Net investment in foreign operations hedge (effective share)	119		0	0
2.2.2. Foreign currency translation	120		0	0
2.2.3. Cash flow hedges (effective share)	121		0	0
2.2.4. Hedging instruments (not determined elements)	122		0	0
2.2.5. Debt instruments at fair value through other comprehensive income	123		497,401	1,891,855
2.2.6. Non-current assets and disposal groups held for sale	124		0	0
2.2.7. Share of other recognised income and expenses from investments in subsidiaries, joint ventures and associates	125		0	0
2.2.8. Income tax on items that may be reclassified to profit or loss	126		0	0
<b>3. Total comprehensive income for the year (AOP 104 + 105 and AOP 128 + 129)</b>	<b>127</b>		<b>9,103,658</b>	<b>16,583,845</b>
<b>4. Attributable to minority (non-controlling) interest</b>	<b>128</b>		<b>0</b>	<b>0</b>
<b>5. Attributable to owners of the parent company</b>	<b>129</b>		<b>0</b>	<b>0</b>



Statement of financial position (Balance sheet) As at 31 December 2019				BAN-BIL form
Entity: BANKA KOVANICA D.D. VARAŽDIN				
Position	AOP mark	Note no.	Previous year (net)	Current year (net)
1	2	3	4	5
<b>Assets</b>				
1. Cash, cash receivable from central banks and other demand deposits (AOP 002 to 004)	001		147,956,974	74,730,544
1.1. Cash on hand	002		15,424,907	14,378,931
1.2. Cash receivable from central banks	003		111,171,783	44,523,920
1.3. Other demand deposits	004		21,360,284	15,827,693
2. Financial assets held for trading (AOP 006 to 009)	005		0	0
2.1. Derivatives	006		0	0
2.2. Equity instruments	007		0	0
2.3. Debt securities	008		0	0
2.4. Loans and advances	009		0	0
3. Financial assets that are not traded and mandatorily carried at fair value through profit or loss (AOP 011 to 013)	010		680,693	302,623
3.1. Equity instruments	011		680,693	302,623
3.2. Debt securities	012		0	0
3.3. Loans and advances	013		0	0
4. Financial assets at fair value through profit or loss (AOP 015+016)	014		0	0
4.2. Debt securities	015		0	0
4.3. Loans and advances	016		0	0
5. Financial assets at fair value through other comprehensive income (AOP 018 to 020)	017		61,810,412	138,467,864
5.1. Equity instruments	018		0	0
5.1. Debt securities	019		61,810,412	138,315,074
5.2. Loans and advances	020		0	152,790
6. Financial assets at amortised cost (AOP 022+023)	021		975,819,977	1,088,086,061
6.1. Debt securities	022		1,762,519	1,811,562
6.2. Loans and advances	023		974,057,458	1,086,274,499
7. Derivatives - hedge accounting	024		0	0
8. Changes in fair value of hedged items in hedging the portfolio against interest rate risk	025		0	0
9. Investments in subsidiaries, joint ventures and associates	026		141,000	141,000
10. Tangible assets	027		33,740,763	32,126,362
11. Intangible assets	028		2,005,687	1,483,948
12. Tax assets	029		2,062,685	894,470
13. Other assets	030		1,968,804	2,065,643
14. Non-current assets and disposal groups held for sale	031		9,231,291	7,253,080
15. TOTAL ASSETS (AOP 001+005+010+014 +017+021+024 to 031)	032		1,235,418,286	1,345,551,595

<b>Liabilities</b>				
<b>16. Financial liabilities held for trading (AOP 034 to 038)</b>	<b>033</b>		<b>0</b>	<b>0</b>
16.1. Derivatives	034		0	0
16.2. Short-term items	035		0	0
16.3. Deposits	036		0	0
16.4. Debt securities issued	037		0	0
16.5. Other financial liabilities	038		0	0
<b>17. Financial liabilities at fair value through profit or loss (AOP 040 to 042)</b>	<b>039</b>		<b>0</b>	<b>0</b>
17.1. Deposits	040		0	0
17.2. Debt securities issued	041		0	0
17.3. Other financial liabilities	042		0	0
<b>18. Financial liabilities at amortised cost (AOP 044 to 046)</b>	<b>043</b>	<b>1,103,667,065</b>	<b>1,195,135,018</b>	
18.1. Deposits	044	1,103,665,462	1,189,477,502	
18.2. Debt securities issued	045	0	0	
18.3. Other financial liabilities	046	1,603	5,657,516	
<b>19. Derivatives - hedge accounting</b>	<b>047</b>	<b>0</b>	<b>0</b>	
<b>20. Changes in fair value of hedged items in hedging the portfolio against interest rate risk</b>	<b>048</b>	<b>0</b>	<b>0</b>	
<b>21. Provisions</b>	<b>049</b>	<b>846,280</b>	<b>987,548</b>	
<b>22. Tax payable</b>	<b>050</b>	<b>138,953</b>	<b>1,807,322</b>	
<b>23. Share capital repayable on demand</b>	<b>051</b>	<b>0</b>	<b>0</b>	
<b>24. Other liabilities</b>	<b>052</b>	<b>15,067,645</b>	<b>15,339,518</b>	
<b>25. Liabilities of disposal groups classified as held for sale</b>	<b>053</b>	<b>0</b>	<b>0</b>	
<b>26. TOTAL LIABILITIES (AOP 033 + 039 + 043 + 047 to 053)</b>	<b>054</b>	<b>1,119,719,943</b>	<b>1,213,269,406</b>	
<b>Equity</b>				
<b>27. Share capital</b>	<b>055</b>	<b>106,961,910</b>	<b>106,961,910</b>	
<b>28. Share premium</b>	<b>056</b>	<b>0</b>	<b>0</b>	
<b>29. Issued equity instruments except for equity</b>	<b>057</b>	<b>0</b>	<b>0</b>	
<b>30. Other equity instruments</b>	<b>058</b>	<b>0</b>	<b>0</b>	
<b>31. Accumulated other comprehensive income</b>	<b>059</b>	<b>209,779</b>	<b>2,101,635</b>	
<b>32. Retained earnings</b>	<b>060</b>	<b>-10,356,723</b>	<b>-10,356,723</b>	
<b>33. Revaluation reserves</b>	<b>061</b>	<b>0</b>	<b>0</b>	
<b>34. Other reserves</b>	<b>062</b>	<b>10,315,424</b>	<b>18,921,681</b>	
<b>35. Treasury shares</b>	<b>063</b>	<b>-38,304</b>	<b>-38,304</b>	
<b>36. Profit or loss attributable to owners of the parent company</b>	<b>064</b>	<b>8,606,257</b>	<b>14,691,990</b>	
<b>37. Dividends for the year</b>	<b>065</b>	<b>0</b>	<b>0</b>	
<b>38. Minority (non-controlling) interests</b>	<b>066</b>	<b>0</b>	<b>0</b>	
<b>39. TOTAL EQUITY (AOP 055 to 066)</b>	<b>067</b>	<b>115,698,343</b>	<b>132,282,189</b>	
<b>40. TOTAL CAPITAL AND RESERVES (AOP 054+067)</b>	<b>068</b>	<b>1,235,416,286</b>	<b>1,345,551,595</b>	

STATEMENT OF CASH FLOWS – Indirect method For the period from 1 January 2019 to 31 December 2019				BAN-NTI form
Entity: BANKA KOVANICA D.D. VARAŽDIN				
Position	AOP mark	Note no.	Previous year	Current year
1	2	3	4	5
<b>Operating activities and adjustments</b>				
1. Profit/loss before tax	001		8,606,257	14,691,990
2. Impairment losses and provisions	002		16,998,348	14,679,128
3. Depreciation and amortisation	003		2,151,594	3,203,590
4. Net unrealised gains/losses on financial assets and liabilities at fair value through profit or loss	004		9,673	-29,927
5. Gains/losses on sale of tangible assets	005		1,609,166	325,097
6. Other non-cash items	006		0	0
<b>Movements in assets and liabilities from operating activities</b>				
7. Deposits with CNB	007		17,549,186	66,647,863
8. Deposits with financial institutions and loans to financial institutions	008		-9,016,783	5,532,591
9. Loans and advances to other customers	009		-104,009,211	-126,945,212
10. Securities and other financial instruments at fair value through other comprehensive income	010		-1,700,613	-1,559,336
11. Securities and other financial instruments held for trading	011		0	0
12. Securities and other financial instruments not actively traded but carried at fair value through profit or loss	012		0	0
13. Securities and other financial instruments mandatorily carried at fair value through profit or loss	013		0	0
14. Securities and other financial instruments carried at amortised cost	014		0	0
15. Other assets from operating activities	015		3,395,822	1,071,376
<b>Increase/decrease in operating liabilities</b>				
16. Deposits from financial institutions	016		14,017	1,160,129
17. Transaction accounts of other customers	017		17,302,861	19,943,258
18. Savings deposits of other customers	018		12,951,243	17,991,739
19. Term deposits of other customers	019		79,655,551	54,154,678
20. Derivative financial liabilities and other trading liabilities	020		0	0
21. Other liabilities	021		-14,434,623	2,081,510
22. Outstanding interest from operating activities	022		0	0
23. Dividend received from operating activities	023		0	0
24. Interest paid from operating activities	024		0	0
25. Income tax paid	025		0	0
<b>A) Net cash flows from operating activities (AOP 001 to 025)</b>	<b>026</b>		<b>31,082,488</b>	<b>72,948,474</b>
<b>Investing activities</b>				
1. Proceeds from sale/payments for purchase/of tangible and intangible assets	027		1,450,071	585,664
2. Proceeds from sale/payments for purchases/of investments in subsidiaries, joint ventures and associates	028		0	0
3. Proceeds from collection/payments for purchases/of securities and other financial instruments from investing activities	029		-17,324,653	-74,690,119
4. Dividends received from investing activities	030		0	0
5. Other proceeds/payments from investment activities	031		0	0
<b>A) Net cash flows from investing activities (AOP 027 to 031)</b>	<b>032</b>		<b>-15,874,582</b>	<b>-74,104,455</b>
<b>Financing activities</b>				
1. Net increase/decrease in borrowings from financing activities	033		-3,537,504	-1,996,346
2. Net increase/decrease in issued debt securities	034		0	0
3. Net increase/decrease in instruments of supplementary capital	035		-370,978	214,495
4. Share capital increase	036		0	0
5. Dividend paid	037		0	0
6. Other proceeds/payments from financing activities	038		-9,859,322	1,891,856
<b>C) Net cash flows from financing activities (AOP 033 to 038)</b>	<b>039</b>		<b>-13,767,804</b>	<b>110,005</b>
<b>NET INCREASE/DECREASE IN CASH AND CASH EQUIVALENTS (+032+039)</b>	<b>040</b>		<b>1,440,102</b>	<b>-1,045,976</b>
<b>Cash and cash equivalents at beginning of year</b>	<b>041</b>		<b>13,984,805</b>	<b>15,424,907</b>
<b>Effects of foreign currency exchange rate fluctuations on cash and cash equivalents</b>	<b>042</b>			
<b>Cash and cash equivalents at end of year (AOP 040+041+042)</b>	<b>043</b>		<b>15,424,907</b>	<b>14,378,931</b>

**Supplementary statements for the Croatian National Bank**
**Appendix 1**

for the period from 1 January to 31 December 2019

**CHANGES IN EQUITY**

For the period from 1 January 2019 to 31 December 2019

Entity: BANKA KOVANICA D.D. VARAŽDIN

**BAN-PK  
form**

Position	AOP mark	Note no.	Attributable to equity holders of the parent											Minority interest		Total
			Equity	Share premium	Issued equity instru- ments except for equity	Other equity shares	Accum. OCI	Retained earnings	Re- valuation reserves	Other reserves	Treasury shares	Profit / loss attributable to owners of the parent company	Divi- dends for the year	Accum. OCI	Other Items	
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17 (4 to 16)
<b>1. Opening balance (before restatement)</b>	<b>01</b>		106,961,910	0	0	0	209,779	-10,356,723	0	10,315,424	-38,304	8,606,257	0	0	0	<b>115,698,343</b>
2. Effects of corrections of errors	02		0	0	0	0	0	0	0	0	0	0	0	0	0	0
3. Effects of changes in accounting policies	03		0	0	0	0	0	0	0	0	0	0	0	0	0	0
<b>4. Opening balance (current period) (AOP 01 to 03)</b>	<b>04</b>		<b>106,961,910</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>209,779</b>	<b>-10,356,723</b>	<b>0</b>	<b>10,315,424</b>	<b>-38,304</b>	<b>8,606,257</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>115,698,343</b>
5. Issue of ordinary shares	05		0	0				0	0	0					0	0
6. Issue of preference shares	06		0	0	0			0	0	0					0	0
7. Issue of other equity instruments	07				0			0	0	0					0	0
8. Execution or expiry of other issued equity instruments	08				0			0	0	0					0	0
9. Debt to equity swaps	09		0	0	0	0		0	0	0					0	0
10. Capital reduction	10		0	0				0	0	0	0	0			0	0
11. Dividends	11		0	0	0	0		0	0	0	0		0		0	0
12. Purchase of treasury shares	12							0	0	0	0			0	0	0
13. Sale or extinguishment of treasury shares	13							0	0	0	0			0	0	0
14. Reclassification of financial instruments from equity instruments to liabilities	14		0	0	0	0									0	0
15. Reclassification of financial instruments from liabilities to equity instruments	15		0	0	0	0									0	0
16. Transfers between equity instr. components	16				0	0	0	0	0	0		0	0	0	0	0
17. Increase or decrease in equity instruments resulting from business combinations	17		0	0	0	0	0	0	0	0	0				0	0
18. Share-based payments	18		0	0		0					0				0	0
19. Other increase or decrease in equity instruments	19				0	0	0	0	0	8,606,257	0	-8,606,257	0	0	0	0
20. Total comprehensive income for the year	20						1,891,855	0	0	0		14,691,990		0	0	<b>16,583,845</b>
<b>21. Closing balance (current period) (AOP 04 to 20)</b>	<b>21</b>		<b>106,961,910</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>2,101,634</b>	<b>-10,356,723</b>	<b>0</b>	<b>18,921,681</b>	<b>-38,304</b>	<b>14,691,990</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>132,282,188</b>

**Disclosures in accordance with Article 164 of the Credit Institutions Act**

- 1) In addition to banking services such as accepting deposits and approving loans for its own account, the Bank also provides the following financial service on the entire territory of the Republic of Croatia:
  - approval of loans and credits, including consumer credits and loans and mortgage credits, financing commercial activities, including export financing based on discount repurchase and without reimbursement of long-term unmatured claims ensured by financial instruments (forfeiting);
  - purchase of receivables with or without recourse (factoring); factoring,
  - issuing guarantees and other warrants;
  - trading for its own account in money market instruments and other transferable securities, foreign currencies including foreign exchange activities, financial futures and option;
  - issuing electronic money;
  - performing local and international payments;
  - representation in the sale of insurance policies, in accordance with the law regulating insurance, intermediation and representation in insurance activities;
  - collection of data, conducting analyses and providing information on creditworthiness of legal and natural persons who conduct business activities on their own;
  - issuing and managing instruments of payment, intermediation in concluding financial deals.
- 2) The Bank's total income in 2019 amounted to HRK 94,377 thousand.
- 3) The Bank employs 104 full-time employees, of which 94 are employed for an indefinite period time, 5 for a definite period of time and 5 based on the On-the-job training for work without employment measure;
- 4) Profit for 2019 amounted to HRK 14,692 thousand.
- 5) Income tax for 2019 amounted to HRK 2,812 thousand.
- 6) In 2019, the Bank did not receive any state subsidies.

for the period from 1 January to 31 December 2019

	GFI-BAN	Annual Report	Differences
	HRK'000	HRK'000	HRK'000
Interest income	82,333	82,296	37
Interest expense	(15,669)	(15,632)	(37)
<b>Net interest income</b>	<b>66,664</b>	<b>66,664</b>	<b>0</b>
Commission and fee income	8,633	8,633	0
Commission and fee expense	(2,476)	(2,476)	0
<b>Net commission and fee income</b>	<b>6,157</b>	<b>6,157</b>	<b>0</b>
Dividend income	10	0	10
Gains/(losses) on trading activities	1,019	0	1,019
Gains or losses on non-trading assets mandatorily at fair value through profit or loss	30	30	0
Gains or losses on derecognition of financial assets and financial liabilities	97	97	0
Foreign exchange gains/losses	301	1,320	(1,019)
Losses/gains on derecognition of non-financial assets	(3,956)	0	(3,956)
Other operating income	0	2,852	(2,852)
Other operating expenses	(4,167)	(3,891)	(276)
General administrative expenses and depreciation/amortisation	(32,664)	(41,039)	8,375
Depreciation charge	(3,204)	0	(3,204)
Provisions/Reversal of provisions	(56)	0	(56)
Impairment losses and loss provisions	(14,679)	(14,686)	7
Impairment of non-financial assets	0	0	0
Gains/losses on impairment of assets held for sale	211	0	211
Other non-continuing income/expenses	1,741	0	1,741
<b>Profit/loss before tax</b>	<b>17,504</b>	<b>17,504</b>	<b>0</b>
Income tax	(2,812)	(2,812)	0
<b>Profit/loss for the year</b>	<b>14,692</b>	<b>14,692</b>	<b>0</b>

for the period from 1 January to 31 December 2019

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**Income statement reconciliation**

The differences between the items disclosed in the Income statement in the Annual Report and those prescribed by the CNB Decision relate to the following categories:

- the difference of HRK 10 thousand arises from the different treatment of dividend income, which is presented within Other income in the Annual Report and as a separate item in the Income statement pursuant to the CNB Decision;
- the difference of HRK 1,019 thousand arises from the different treatment of foreign exchange differences based on the purchase and sale of foreign currencies, which are presented within Net foreign exchange differences in the Annual Report, and as a separate item - Net gains/losses on financial assets and financial liabilities held for trading - pursuant to the CNB Decision;
- the difference of HRK 3,956 thousand arises from the different treatment of impairment of collateral repossessed in exchange for uncollected receivables and gains on the sale of these assets, presented within Other operating income in the Annual Report, and as a separate item - Gains/losses on derecognition of non-financial assets - pursuant to the CNB Decision. The difference of HRK 211 thousand arises from the different treatment of gains on the sale of the collateral repossessed in exchange for uncollected receivables, presented within Other operating income in the Annual Report, while pursuant to the CNB's Decision they are presented as a separate item - Gains/losses on assets held for sale. The amount of HRK 1,872 thousand is presented within Other operating income in the Annual Report and pursuant to the CNB Decision it is presented as non-continuing income/expenses. The amount of HRK 131 thousand relating to administrative expenses in the Annual Report is presented within Non-continuing income/expenses pursuant to the CNB Decision;
- Depreciation and amortisation is, pursuant to the CNB Decision, a separate item, while in the Annual Report it is presented within Administrative expenses (HRK 3,204 thousand);
- Pursuant to the CNB Decision, provisions for annual leave are presented within Administrative expenses, while they are presented within Other operating expenses in the Annual Report (HRK 85 thousand). In the Annual Report, Other operating expenses include rental costs, while they are included in administrative expenses (HRK 203 thousand) pursuant to the CNB Decision. In the Annual Report, provisions for litigation are presented within Other operating expenses, while, pursuant to the CNB Decision, they are a separate item within Provisions (HRK 36 thousand). Pursuant to the CNB Decision, taxes, membership fees and other income taxes are presented within Other operating expenses, while they are included in administrative expenses in the Annual Report (HRK 508 thousand);
- the difference of HRK 20 thousand relates to the impairment of commitments that are presented within provisions pursuant to the CNB Decision, while in the Annual Report they are presented within the costs of impairment losses and loss provisions.

for the period from 1 January to 31 December 2019

	GFI-BAN HRK'000	Annual Report HRK'000	Differences HRK'000
<b>ASSETS</b>			
Cash, cash receivable and other demand deposits	74,731	74,731	-
Receivables from CNB	-	78,311	(78,311)
Placements with banks	-	998	(998)
Financial assets at amortised cost	1,088,085	996,124	91,961
Financial assets at fair value through OCI	138,468	138,912	(444)
Non-trading financial assets mandatorily measured at fair value through profit or loss	303	-	303
Investments in subsidiaries, associates and joint ventures	141	-	141
Tangible assets	32,126	16,355	15,771
Intangible assets	1,484	1,484	-
Non-current assets held for sale	7,253	23,024	(15,771)
Other assets	2,066	15,613	(13,547)
Tax assets	895	-	895
<b>TOTAL ASSETS</b>	<b>1,345,552</b>	<b>1,345,552</b>	<b>-</b>
<b>LIABILITIES AND EQUITY</b>			
Financial liabilities at amortised cost	1,195,135	1,143,805	51,330
Due to banks	-	5,946	(5,946)
Hybrid instruments	-	39,725	39,725
Lease liabilities	-	5,656	(5,656)
Other liabilities	15,340	18,138	(2,798)
Provisions	988	-	988
Tax payable	1,807	-	1,807
<b>TOTAL LIABILITIES</b>	<b>1,213,270</b>	<b>1,213,270</b>	<b>-</b>
<b>EQUITY</b>			
Share capital	106,962	106,962	-
Treasury shares	(38)	(38)	-
Capital gain	-	-	-
Profit/(loss) for the year	14,692	14,692	-
Retained earnings/(accumulated losses)	(10,357)	(10,357)	-
Accumulated OCI	2,102	-	2,102
Statutory and other equity reserves	18,921	21,023	(2,102)
<b>TOTAL EQUITY</b>	<b>132,282</b>	<b>132,282</b>	<b>-</b>
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>1,345,552</b>	<b>1,345,552</b>	<b>-</b>



### **Balance sheet reconciliation**

The differences between the items disclosed in the Balance sheet in the Annual Report and those prescribed by the CNB Decision relate to the following categories:

- in the Annual Report, placements with banks include loans to banks in the amount of HRK 5,138 thousand, which are presented within Financial assets at amortised cost under the CNB standard;
- in the Annual Report, placements with banks include term deposits with banks in the amount of HRK 998 thousand, which are presented within Financial assets at amortised cost under the CNB standard;
- in the Annual Report, Receivables from the CNB (Obligatory reserve) is a separate item in the balance sheet, while the obligatory reserve is presented within Financial assets at amortised cost under the CNB standard;
- in the Annual Report, investments in subsidiaries, associates and joint ventures are presented within Financial assets at fair value through profit or loss in the amount of HRK 141 thousand, and this is a separate line item pursuant to the CNB Decision. In the Annual Report, financial assets at fair value through profit or loss include non-trading financial assets measured at fair value through profit or loss in the amount of HRK 444 thousand;
- the difference of HRK 15,771 thousand in property, plant and equipment relates to the collateral repossessed in exchange for uncollected receivables, which is presented within Non-current assets available for sale in the Annual Report;
- tax assets in the amount of HRK 895 thousand in the Annual Report are presented within Other assets and, according to the CNB standard, they are a separate asset item;
- the difference of HRK 13,547 thousand between Other assets according to the Annual Report and the CNB standard relates to receivables for reimbursement of court costs and fees receivable, which are included in Financial assets at amortised cost under the CNB standard;
- liabilities to banks in the Annual Report include term and savings deposits of banks, leases and loans received from banks, while the same items are presented within financial liabilities measured at amortised cost under the CNB standard;
- hybrid instruments are a separate liability item in the Annual Report, while hybrid instruments are stated within financial liabilities measured at amortised cost under the CNB standard;
- in the Annual Report, restricted deposits in the amount of HRK 2 thousand are presented within Other liabilities, and under the CNB standard they are included in Financial liabilities measured at amortised cost;
- tax liabilities in the amount of HRK 1,807 and provisions in the amount of HRK 988 thousand in the Annual Report are included within Other liabilities, and they are a separate liability item under the CNB standard;
- in the presentation of equity, the difference relates to accumulated other comprehensive income in the amount of HRK 2,102 thousand, which is presented within Reserves in the Annual Report, and is a separate item under the CNB standard;

### **Statement of cash flows reconciliation**

for the period from 1 January to 31 December 2019

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The differences between the items in the statement of cash flows included in the Annual Report and those defined by the structure and contents prescribed by the CNB are not material and arise from the different treatment and presentation of certain items of the balance sheet and the income statement. Balance sheet differences have been described within the comparison of the balance sheet according to the two types of reporting.

**Statement of changes in equity reconciliation**

There are no differences regarding the statement of changes in equity included in the Annual Report with respect to the CNB standard.