CROATIA BANKA d.d.

ANNUAL REPORT FOR 2018

C O N T E N T

INTRODUCTION

The Annual Report includes the Management Board Report on the Bank’s position, an overview of financial and operational performance, audited financial statements, together with the Independent Auditor’s Report, and other regulatory reports for the Croatian National Bank. Unless otherwise noted, all amounts in the Annual Report are presented in thousands of Kuna (HRK).

Legal form

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

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

Abbreviations

In this Annual Report, Croatia banka d.d. is referred to as the “Bank”, the Croatian National Bank as the “CNB”, the Croatian Bank for Reconstruction and Development as the “CBRD”, the State Agency for Deposit Insurance and Bank Rehabilitation as the “DAB”, the Financial Agency as "FINA", European Union as the “EU”, International Financial Reporting Standards as “IFRS”, Other comprehensive income as “OCI”, Available for sale as “AFS”, Profit and loss account as P&L and gross domestic product as the “GDP”.

Exchange rates

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

At 31 December 2018 EUR 1 = HRK 7.417575; USD 1 = HRK 6.469192

At 31 December 2018 EUR 1 = HRK 7.513648; USD 1 = HRK 6.269733

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

Indicator / Year	2018	2017	2016	2015	2014
Key indicators					
Profit/(loss) before tax	(22)	(31)	3	2	5
Net profit/(loss)	(25)	(31)	2	(15)	4
Total assets	2,306	2,491	3,110	3,109	3,038
Loans and advances to customers	1,081	1,153	1,591	1,893	1,906
Total deposits received	2,037	2,156	2,609	2,616	2,593
Capital and reserves	130	152	190	182	200

Other indicators					
Ratio of operating expenses in operating income	99.9%	72.7%	71.5%	73.00%	79.70%
Return on equity	(17.7%)	(17.9%)	0.9%	(8.3%)	2.0%
Assets return	(0.9%)	(1.1%)	0.1%	(0.5%)	0.1%
Own funds	126	146	174	175	171
Total capital ratio	14.98%	15.85%	16.81%	15.91%	13.29%

Historical development of the Bank

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

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

Information on economic trends and forecasts[1]

During the third quarter of 2018, economic activity growth slowed down on a quarterly basis due to slight decrease in exports of goods and services, strong growth of total imports and a slowdown in personal consumption growth. According to the provisional estimate of the Central Bureau of Statistics, in 2018 real GDP growth was up by 2.6%, down from 2017, when it grew by 2.9%.
In 2019, economic growth is expected to remain at about the same level as in 2018. Growth of gross investments in fixed capital is expected, assuming that the general government investment will be strengthened due to stronger utilisation of EU funds. Continued personal consumption growth is expected to be driven by continued growth in employment and wages and relieving the tax burden.

Labour market

During the third quarter of 2018, favourable labour market trends continued, although somewhat slower than in the first half of last year. The employment rate grew by 0.3% during the third quarter, with the strongest contribution to employment growth recorded in construction and other service activities. In October, the employment rate increased by 0.5% compared to the previous quarter's average. Relatively favourable labour market trends will further reduce the unemployment rate, but with somewhat milder intensity, which could drop to 7.2% in 2019. Growth of nominal gross and net wages is expected to increase due to tax changes in income taxation, which came into effect as of 1 January 2019.

Prices

Average annual inflation in consumer prices was 1.5% in 2018 (2017: 1.1%), and was mainly due to an increase in the average annual growth rate of energy prices. It has been estimated that the average annual inflation rate in 2019 will slow down to 0.9%, as a result of the fall in the value added tax rate on certain products and the expected decline in crude oil prices in the world market.

Current and capital account of balance of payments

Current and capital account balances in 2018 are expected to be somewhat more favourable than in the previous year, primarily due to continued growth in tourism revenues and stronger utilisation of EU funds. Movements in foreign commodity exchange in the first nine months of 2018 recorded a noticeable slowdown in export growth, but there was a significant improvement in international trade. In contrast, in 2019, the surplus in the current and capital account is expected mainly due to an increase in foreign trade shortages, primarily due to the forecast slowdown in the growth of tourism revenues.
With respect to foreign capital flows, a net outflow is expected largely on the basis of a decline in net debt obligations of domestic sectors, which will gradually slow down. These trends should be reflected in further improvement of relative indicators of external imbalances.

[1]Macroeconomic trends and forecast, CNB, December 2018

Information on economic trends and forecasts (continued)

Monetary policy

In 2018, the CNB continued to implement expansive monetary policy by supporting the high liquidity of the monetary system and maintaining the stable exchange rate of the kuna against the euro. The increase in liquidity was largely due to the redemption of foreign currency by commercial banks, which had mitigated appreciation pressures on domestic currency and increased gross international reserves. Due to high liquidity, there was no interest of commercial banks for short-term HRK funds offered in the form of regular weekly reverse repo auctions. In such circumstances, the trend of improving domestic financing conditions which lasted for a several years continued, and coupled with the relaxing of the lending standards and the growth in credit demand, continued growth in domestic sector placements is observable.

Fiscal policy

Amendments to the 2018 budget and the 2019 budget proposal anticipate that after the 2017 budget surplus, 2018 and 2019 could record a general government deficit of about -0.5% of GDP . The European Commission's projections from November this year suggest that the balance of the general government could be more favourable than anticipated by the Ministry of Finance. The structural budget balance in the projection period should not exceed the medium-term budget target, and general government debt is likely to continue to decline in line with the prescribed fiscal rules.

Private sector financing

The trend of improving domestic sector financing conditions over the last several years continued throughout the second half of 2018. The interest rate on short-term government borrowings remained extremely low in 2018 (0.09% for HRK and 0.00% for foreign currency), while the long-term borrowing recorded the most favourable funding conditions so far (in July, a five-year bond with a yield of 1.22% and an eleven-year bond with a yield of 2.58% were issued).
Enterprise financing costs continued to decrease (at the end of 2018, the average interest rate on long-term loans to corporations with a currency clause was under 3% for the first time). The same trend continued with retail loans.
The EURIBOR is still in the negative zone, while the national reference rate (NRS) continues to decline.

Description of operations

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

The Bank is fully (100%) owned by the state and ranked by assets (HRK 2.3 billion) as the 13th of a total of 21 banks. As at 31 December 2018, the Bank has 11 branches and 3 outlets.

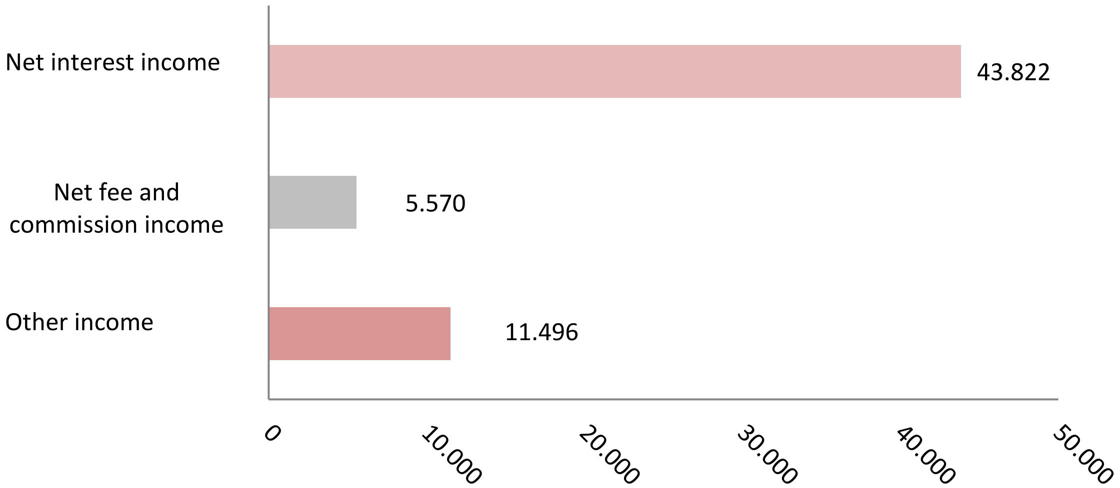
The Bank's own (regulatory) capital as at 31 December 2018 amounts to HRK 125,837 thousand, and the regulatory capital adequacy rate is 14.98%.

In 2018 the Bank generated a pre-tax loss in the amount of HRK 22,086 thousand, and the loss after tax amounts to HRK 24,989 thousand.

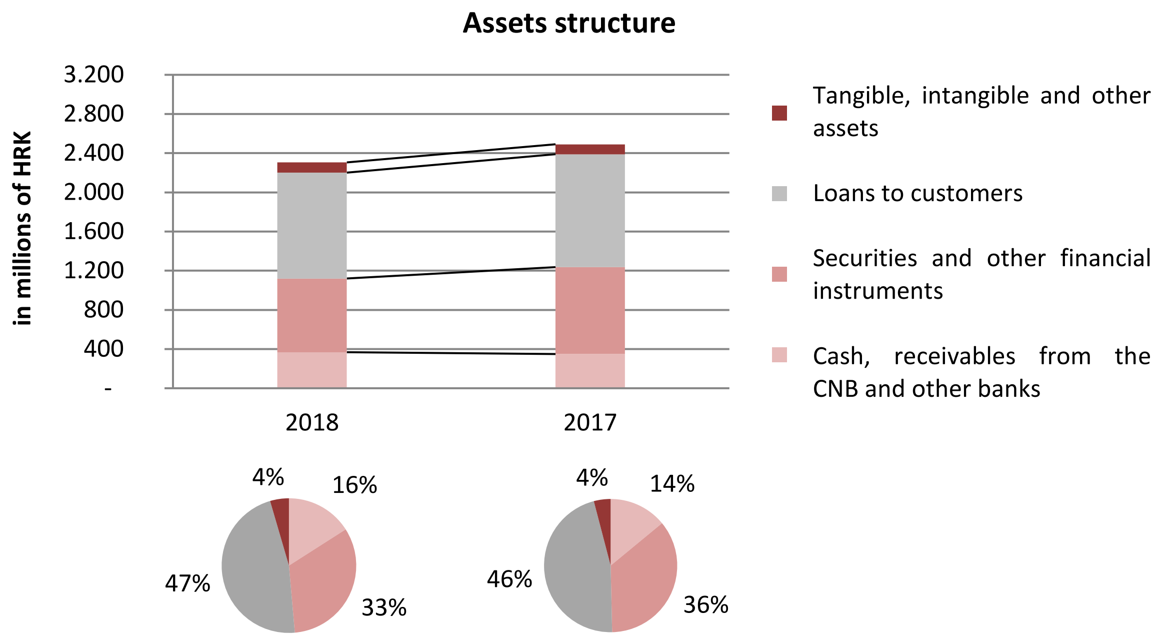
The operating profit for the year amounts to HRK 46,000, the impairment and provisioning expense amounts to HRK 22,132 thousand.

Total net operating income decreased by 28.7%, while operating expenses decreased by 2% compared to 2017 which contributed to a drop in operating profit in 2018. Interest income represents the most significant share of the total income and amounts to 72 percent (HRK 43,822 thousand).

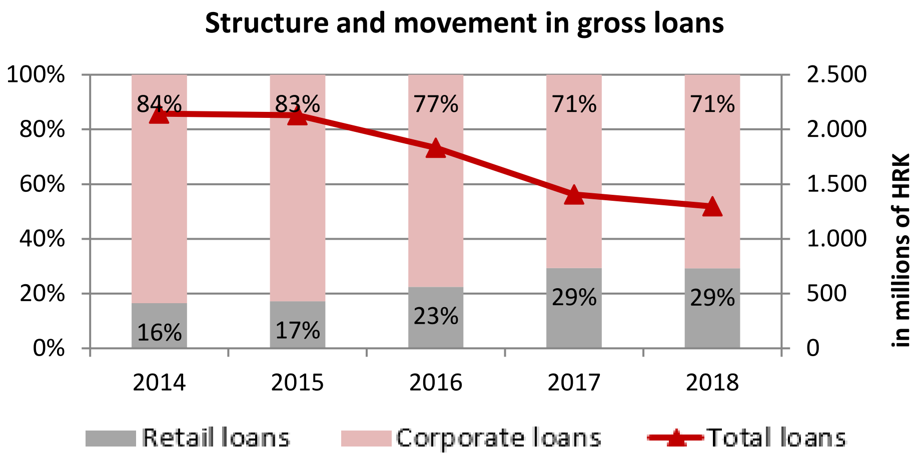
Structure of operating income for the period from 1 Jan. to 31 Dec. 2018 (in thousands of HRK)



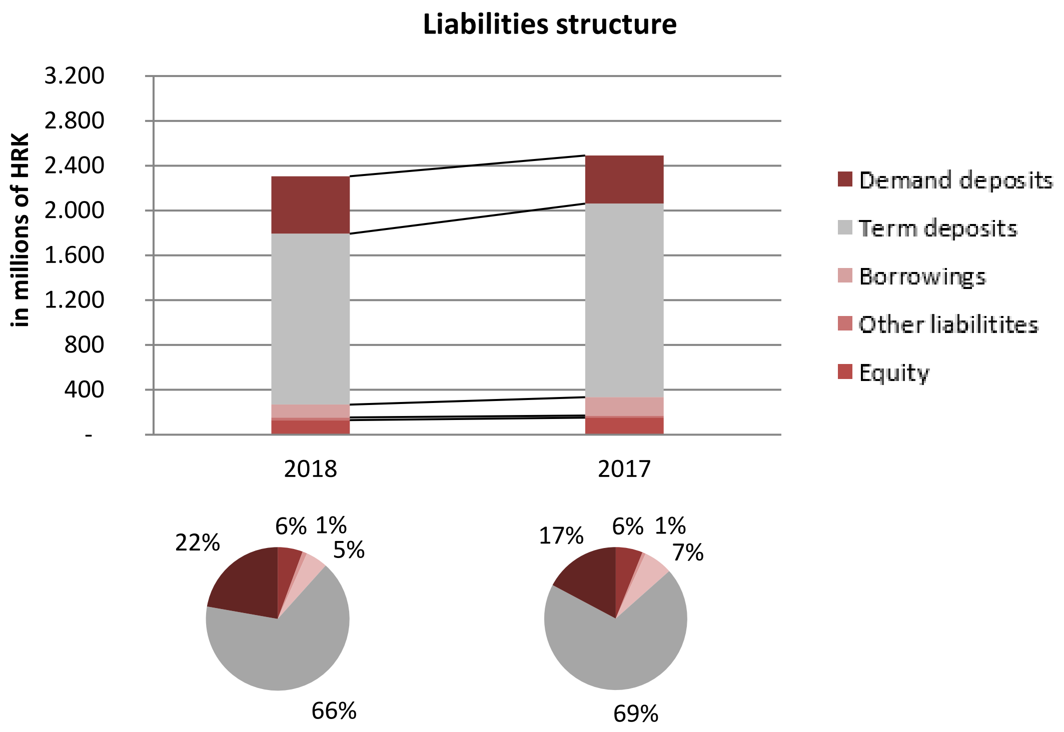
At the end of 2018 the Bank's assets amount to HRK 2,305,660 thousand, HRK 185,156 thousand less than at the end of 2017. Loans and receivables from customers represent the largest share (47 percent), followed by securities and other instruments (33 percent), cash and receivables from the Croatian National Bank and other banks constituting (16 percent).



At 31 December 2018, the balance of total gross loans to customers was HRK 1,296,252 thousand, which is 7.8 percent less than in 2017 mainly due to a decrease in public sector lending. Loans to legal persons represent 71 percent of the total loans to customers, and loans to individuals (including sole traders) account for 29 percent.

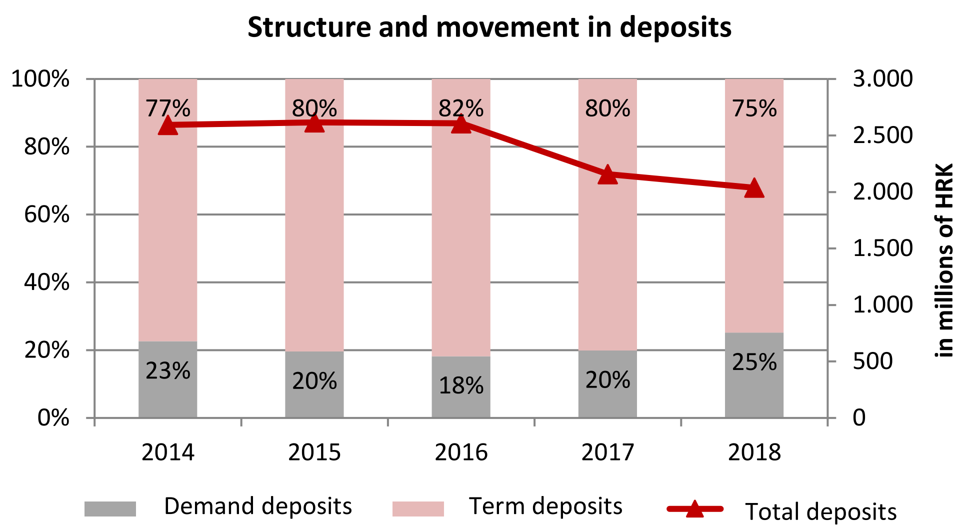


Term deposits represent the largest portion of liabilities and account for 66 percent, followed by demand deposits which represent 22 percent.



Total deposits at the end of 2018 amounted to 2.0 billion, which represents a decrease compared to the end of 2017 by 15.5 percent, wherein retail deposits decreased by 11.4 percent, and corporate deposits increased by 11.3 percent.

As regards the structure of total deposits, term deposits (74.8 percent) prevail over demand deposits (25.2 percent). Customer term deposits decreased by 11.7 percent, and their share in total deposits decreased by 5.3 pp. In 2018, demand deposits recorded an increase of 19.5 percent.



Retail customer operations

The past 2018 was the year in which more attention was paid to deposit activity, due to the overall consolidation of the liquidity structure at the level of the entire Bank. The biggest impact was the closure of the two branches (Metković and Bjelovar), which led to a significant level of decrease in the deposits of individuals over a period of several months. It has contributed to the Bank reducing excessive and unnecessary liquidity reserves, which resulted in significant reduction of interest costs.
Lending with reduced intensity due to capital constraints, as well as due to the closure of two large branches, continued in 2018, which further influenced the reduction of placements.
Despite the decline in the business network, there has been no reduction in the number of current accounts although the closure effects on this issue might be observed in 2019.

Operations with legal persons

Deposits from legal persons (excluding deposits from other banks) account for 20 percent of the Bank's total deposits. They increased by 11.3 percent from the end of 2017 and amount to HRK 373,638 thousand. Of that balance, demand deposits amount to HRK 285,596 thousand, and term deposits amount to HRK 88,042 thousand.

At the end of 2018, the total gross portfolio of loans to legal persons amounted to HRK 917,325 thousand, which is HRK 76,025 thousand less than at the end of 2017. The same applies to public sector lending.

As part of its 2018 plan for corporate customers, the Bank intended to preserve its existing good customers as well as continuously improve the quality of its business processes in cooperation with other organizational units of the Bank, with an emphasis on the lending process, which the Bank succeeded in the most part. The plan is to continue the efforts in 2019. Fee income decreased, mainly due to a decrease in fees in payment transactions and the increase in the share of payments over other channels.

Treasury operations

The Bank maintains its liquidity using available liquid instruments denominated in HRK and foreign currencies (balances on accounts with the Bank, securities, inter-bank loans, repo loans). Among other instruments, the Bank uses foreign currency exchange and FX swap to maintain its liquidity position. Throughout the year 2018 the Bank maintained a high liquidity as well as a balanced foreign exchange position on all currencies.

In 2018, the securities portfolio (bonds and treasury bills) decreased by 14.3 percent, which is about 2.5% less than the planned decrease. Regardless of the downward trend in interest rates and price volatility on the capital market, planned interest income and trading income were realised. During 2018, with a view to adapting the Bank to changes in regulatory requirements, the securities portfolio was largely restructured. The amount of foreign currency bonds of the Republic of Croatia in the portfolio decreased by 70.8% (HRK 161.4m) and the amount of foreign currency T-bills of the Republic of Croatia by 40.7% (HRK 106.9m), while the amount of foreign currency bonds increased by 15.8% (HRK 26.8m) and the treasury bills of the Republic of Croatia with the currency clause by 17.3% (HRK 20.7m). Furthermore, as at 31 December 2018, the Bank also had HRK 94.5 million worth of bonds of the European Monetary Union in its bond portfolio, with the highest credit rating, unlike 2017, when there were no investments of this kind.

Investment banking

The Bank has secured all of the prerequisites and obtained permits from the Croatian National Bank and the Croatian Financial Services Supervisory Agency for the provision of investment services and activities and ancillary services referred to in Article 5 of the Capital Market Act (OG 65/18), paragraph 1, items 1 to 3 , 6 to 7, paragraph 2, items 1 to 2 and 4. In the field of investment banking, the Bank offers brokerage services to its clients, loans, storage and administration of financial instruments for a client's account, including custody and custody-related services. When providing loans, the Bank offers its clients margin short-term HRK specific-purpose loans for the purchase of financial instruments and general-purpose short-term HRK loans secured by financial instruments placed into the Bank's custody.

Despite the challenging situation on the Croatian financial market, which features low transaction volumes and meagre investments, the Bank achieved a good results in the investment banking segment. Over the past one-year period, its customer base has continued to expand, and the portfolio of its investment banking customers has increased considerably. The effects of the increase in interest income will be visible in the coming year.

Internal control system and internal audit

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

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

The internal audit in the course of the audit implementation evaluates the internal control system of specific business segments.

Internal audit

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

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

Following the audit, the Internal Audit Service submits an operational report on each audit performed to each member of the Management Board and to the responsible persons of the organizational segment of the Bank competent for the business segment that was subject to audit, and to the Audit and Risk Committee.

The Internal Audit submits quarterly reports on internal audit activities to the Bank's Management Board, the Audit and Risk Committee, the semi-annual and annual report on operations also to the Bank's Supervisory Board, and the annual report also to the Croatian National Bank.

Implementation of the Corporate Governance Code

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

In 2018, the Bank continuously followed and applied the recommendations determined in the CNB's Positions, disclosing all information the disclosure of which is provided by positive regulations as well as making disclosures that are in the interest of the Bank's owners and clients.

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

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

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

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

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

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

Governance structure of the Bank

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

Other information

The Bank did not carry out any research and development activities in 2018.

The Bank did not purchase any treasury shares in 2018.

The Bank does not own other legal entities.

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

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

Independent auditor's report to the Shareholder of Croatia banka d.d.

Report on the audit of the financial statements

Our opinion

In our opinion, the financial statements give a true and fair view of the financial position of Croatia banka d.d. (the "Bank") as at 31 December 2018, and of its financial performance and its cash flows for the year then ended in accordance with statutory accounting regulations for banks in the Republic of Croatia.

Our opinion is consistent with our additional report to the Audit Committee.

What we have audited

The financial statements of the Bank, which comprise:

- statement of comprehensive income for the year ended 31 December 2018;
- statement of financial position as at 31 December 2018;
- statement of changes in equity for the year then ended;
- statement of cash flows for the year then ended; and
- the notes to the financial statements, which include significant accounting policies and other explanatory information.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the financial statements* section of our report.

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

Independence

We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code). We have fulfilled our other ethical responsibilities in accordance with the IESBA Code.

To the best of our knowledge and belief, we declare that we have not provided non-audit services that are prohibited under Article 5(1) of Regulation (EU) No 537/2014, and furthermore, we have not provided any non-audit services to the Bank in the period from 1 January 2018 to 31 December 2018.

Our audit approach

Overview

Materiality	• HRK 2.7 million, which represents 10% of average loss before tax from for the past 2 years.
Key audit matters	• Impairment of loans and advances to customers

As part of designing our audit we determined materiality and assessed the risks of material misstatement in the financial statements. In particular, we considered where management made subjective judgements; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits, we also addressed the risk of management override of internal controls, including among other matters consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the financial statements as a whole, taking into account the structure of the Bank, the accounting processes and controls, and the industry in which the Bank operates.

Materiality

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance whether the financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall materiality for the financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, if any, both individually and in aggregate on the financial statements as a whole.

Overall materiality	HRK 2.7 million
How we determined it	10 % of average loss before tax for the past 2 years.
Rationale for the materiality benchmark applied	We have used average loss before tax as the benchmark due to certain fluctuations of net result (loss before tax) in previous years. We have used loss before tax because, based on our judgment, it represents benchmark which is commonly used to indicate the performance of the Bank's operations.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter	How our audit addressed the Key audit matter
Impairment of loans and advances to customers	
See Note 19 to the financial statements under heading 'Loans and advances to customers', Note 4.20.1. under subheading 'Losses on impairment of loans and receivables'. As at 31 December 2018, the Bank had impairment provisions for loans and advances to customers in the amount of HRK 221 million. Impairment provisions are the management's best estimate of expected credit losses on loans and advances portfolio at the reporting date. The amount of the provisions is determined in accordance with accounting regulations applicable to banks in Croatia as explained in Note 3 to the financial statements. The Bank applies a three-stage model for impairment, based on changes in credit quality since initial recognition. For loans in Stage 1 and Stage 2, the Bank applied IFRS 9 methodology, however the loan loss provision has been determined as minimum of 0.8% of exposure to which it applies as prescribed by the Croatian National Bank. For loans in Stage 3, it is determined as the difference between the book value and the recoverable amount, which represents the present value of expected cash flows, including amounts recoverable from guarantees and collateral, discounted at the loans' original effective interest rate.	We tested controls for approving and monitoring of loans and advances to customers, including appropriateness of classification of loans, calculation of days past due and calculation of impairment provisions. We have selected a sample of loans and advances to customers with the focus on exposures with potentially highest impact on the financial statements due to their size and/or risk profile. We have also focused on other exposures that we assessed as highly risky, such as restructured exposures and non-performing loans. We have reviewed supporting documentation for selected stage 3 exposures and discussed any issues with responsible persons in the Bank. For impaired exposures, we have re-examined key assumptions used in future cash flows estimates, such as value of collateral to ensure the exposures have been classified and measured in accordance with accounting regulations applicable to banks in Croatia. We have reviewed expected credit loss calculation methodology and policies for impairment losses recognized for Stage 1 and Stage 2 portfolio. Furthermore, we evaluated whether key components of expected credit loss calculation are correctly incorporated in the models and tested on a sample basis the correctness of stage allocation according to the relevant policies in order to conclude on appropriateness of impairment provision as per Croatia National Bank's requirements and any significant deviation to IFRS. Our procedures did not result in any material adjustments to the financial statements.

Reporting on other information including Management Report

Management is responsible for the other information. The other information comprises the Annual Report of the Bank, which includes the Management Report, but does not include the financial statements and our independent auditor's report thereon.

Our opinion on the financial statements does not cover the other information, including the Management Report.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

With respect to the Management Report, we also performed procedures required by the Accounting Act in Croatia. Those procedures include considering whether the Management Report includes the disclosures required by Article 21 of the Accounting Act.

Based on the work undertaken in the course of our audit, in our opinion:

- the information given in the Management Report for the financial year for which the financial statements are prepared is consistent, in all material respects, with the financial statements; and
- the Management Report has been prepared in accordance with the requirements of Article 21 of the Accounting Act.

In addition, in light of the knowledge and understanding of the Bank and their environment obtained in the course of the audit, we are also required to report if we have identified material misstatements in the Management Report. We have nothing to report in this respect.

Responsibilities of management and those charged with governance for the financial statements

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

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

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditor's responsibilities for the audit of the financial statements

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

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our independent auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our independent auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our independent auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on other legal and regulatory requirements

Appointment

We were first appointed as auditors of the Bank on 27 September 2018. The audit of financial statements for the year ended 31 December 2018 represents our first year of audit.

Other legal and regulatory requirements

Based on the Decision on the structure and content of annual financial statements of credit institutions (Official Gazette 42/18), (the "Decision"), the Management Board of the Bank prepared the forms presented on pages 108 to 122 (the "Forms"), which are entitled the Statement of financial position of the Bank as at 31 December 2018, the Income statement of the Bank, the Statement of changes in shareholders' equity of the Bank and the Cash flows statement of the Bank for the year then ended together with information to reconcile the Forms to the Bank's financial statements. The Bank's management is responsible for the preparation of the Forms and information on reconciliation. They do not represent an integral part of the financial statements, but contain information required by the Decision. The financial information in the Forms is based on the Bank's financial statements prepared in accordance with statutory accounting regulations for banks in the Republic of Croatia as presented on pages 20 to 107 and adjusted for the purposes of the Decision.

The engagement partner on the audit resulting in this independent auditor's report is Siniša Dušić.

PricewaterhouseCoopers d.o.o.
Heinzelova 70, Zagreb
29 March 2019

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

Pursuant to the Croatian Accounting Act in force, the Management Board is responsible for ensuring that the financial statements are prepared for each financial year in accordance with legal accounting regulations applicable to banks in the Republic of Croatia, in order to give a true and fair view of the financial position and operating results of Croatia banka d.d. (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 the 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; 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 in force (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 taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Management Board is responsible for the preparation and the content of the annual report in accordance with Article 19 of the Accounting Act (Official Gazette 78/15, 134/15, 120/16 and 116/18), and also for the supplementary regulatory reports.

Signed on behalf of the Management Board:

29 March 2019

Danijel Luković
President of the Management Board

CROATIA BANKA
d.d. Zagreb

Tadija Vrdoljak
Member of the Management Board

CROATIA BANKA d.d.
STATEMENT OF COMPREHENSIVE INCOME
for the year ended 31 December 2018

in thousands of HRK	*Note*	**2018**	**2017**
Interest income	*5*	67,424	98,156
Interest expense	*6*	(23,602)	(39,503)
Net interest income		**43,822**	**58,653**
Fee and commission income	*7*	9,116	10,453
Fee and commission expense	*8*	(3,546)	(4,753)
Net fee and commission income		**5,570**	**5,700**
Net financial gains	*9*	3,021	18,345
Net foreign exchange losses	*10*	(47)	(418)
Other operating income	*11*	8,522	8,694
Total other income		**11,496**	**26,621**
Other operating expenses	*12*	(60,842)	(67,646)
Impairment losses and provisions	*13*	(22,132)	(54,615)
Total other expenses		**(82,974)**	**(122,261)**
Loss before tax		**(22,086)**	**(31,287)**
Income tax	*14*	**(2,903)**	**656**
Loss for the year		**(24,989)**	**(30,631)**
Other comprehensive loss			
Items subsequently transferred to profit or loss		**304**	**(6,996)**
Unrealised gains on valuation of available-for-sale financial assets		x	(1,814)
Unrealised gains on valuation of financial assets at fair value through other comprehensive income		(219)	x
Cumulative gains on sale of available-for-sale financial assets transferred to profit or loss		x	(6,717)
Cumulative loss on sale of financial assets at fair value through other comprehensive income transferred to profit or loss		591	x
Deferred tax		(68)	1,535
TOTAL COMPREHENSIVE LOSS		**(24,685)**	**(37,627)**
Loss per share	*32*	**(5.27)**	**(6.45)**

in thousands of HRK	*Note*	**31 December 2018**	**31 December 2017**
ASSETS			
Cash	*15*	206,351	176,668
Receivables from the Croatian National Bank	*16*	142,387	149,557
Placements with banks	*17*	19,249	23,092
Financial assets at fair value through OCI	*18*	752,681	x
Financial assets at fair value through profit or loss		492	x
Financial assets at amortised cost		496	x
Available-for-sale financial assets	*18*	x	887,053
Loans and advances to customers	*19*	1,081,330	1,153,021
Investment property	*20*	34,446	33,630
Property and equipment	*21*	5,646	6,280
Intangible assets	*21*	3,506	4,187
Foreclosed assets	*22*	28,518	15,397
Assets held for sale	*23*	5,280	5,280
Deferred tax assets	*14*	1,119	4,089
Other assets	*24*	24,159	32,562
Total assets		**2,305,660**	**2,490,816**
EQUITY AND LIABILITIES			
Liabilities to banks	*25*	110,543	62,173
Demand deposits	*26*	508,601	411,882
Term deposits	*27*	1,418,110	1,682,228
Borrowings	*28*	114,311	163,492
Other liabilities	*29*	10,054	10,663
Provisions	*30*	13,944	8,370
Total liabilities		**2,175,563**	**2,338,808**
EQUITY			
Share capital	*31*	474,600	474,600
Accumulated loss	*31*	(343,382)	(321,167)
Reserves	*31*	(1,121)	(1,425)
Total equity		**130,097**	**152,008**
Total liabilities and equity		**2,305,660**	**2,490,816**

CROATIA BANKA d.d.
STATEMENT OF CHANGES IN EQUITY
for the year ended 31 December 2018

in thousands of HRK	Share capital	Accumulated loss	Reserves	Total
Balance at 1 January 2017	**474,600**	**(290,536)**	**5,571**	**189,635**
Changes in equity in 2017				
Unrealised change in fair value of available-for-sale financial assets	-	-	(1,814)	(1,814)
Cumulative loss on sale of available-for-sale financial assets transferred to profit and loss	-	-	(6,717)	(6,717)
Deferred tax on available-for-sale financial assets	-	-	1,535	1,535
Net expense recognised directly in other comprehensive income	-	-	*(6,996)*	*(6,996)*
Loss for the year	-	(30,631)	-	(30,631)
Total comprehensive income	474,600	(321.167)	(1,425)	152,008
Balance at 31 December 2017	**474,600**	**(321,167)**	**(1,425)**	**152,008**
Balance at 1 January 2018	**474,600**	**(321,167)**	**(1,425)**	**152,008**
Changes in equity in 2018				
Effect of IFRS 9 application:	-	2,774	-	2,774
Balance at 1 January - restated	**474,600**	**(318,393)**	**(1,425)**	**154,782**
Unrealised change in fair value of financial assets at fair value through other comprehensive income	-	-	(219)	(219)
Accumulated gains on sale of financial assets at fair value through other comprehensive income transferred to profit and loss	-	-	591	591
Deferred tax on financial assets	-	-	(68)	(68)
Net income recognised directly in other comprehensive income	-	-	*303*	*303*
Loss for the year	-	(24,989)	-	(24,989)
Total comprehensive income	*474,600*	*343,382*	*1,121*	*130,097*
Balance at 31 December 2018	**474,600**	**(343,382)**	**(1,121)**	**130,097**

CROATIA BANKA d.d.
STATEMENT OF CASH FLOWS
for the year ended 31 December 2018

in thousands of HRK	2018	2017
NET CASH FLOW FROM OPERATING ACTIVITIES		
Loss before tax	**(22,086)**	**(31,287)**
Adjustment to net cash from operating activities		
Impairment of loans and other assets (net) (Note 13)	15,962	54,196
Reversal of provisions for contingent liabilities (net) (Note 13)	149	(423)
Provisions for legal disputes (net) (Note 13)	6,325	1,307
Other provisions (net) (Note 13, Note 30)	177	56
Gains on realisation of financial assets at fair value through OCI (Note 9)	(639)	x
Gains on realisation of available-for-sale and held-to-maturity financial assets (Note 9)	-	(15,184)
Fair valuation gains on Investment property (Note 11)	(816)	-
Gains on foreign currency trading (Note 9)	(2,382)	(3,161)
Amortisation and depreciation (Note 22)	2,964	3,425
Foreign exchange losses on translation to the CNB mid exchange rate (Note 10)	47	418
Gains on sale of foreclosed assets (Note 11)	(1,883)	(4,073)
Write-offs of tangible assets	4	15
Changes in assets and liabilities from operating activities		
Decrease in receivables from the Croatian National Bank	7,203	42,577
(Increase)/decrease in loans and advances to customers	(12,269)	320,647
Decrease in other assets	10,353	3,174
Interest received	64,248	100,577
Interest paid	(3,091)	(6,039)
Increase/(decrease) in liabilities to banks	48,370	(29,922)
Increase/(decrease) in demand deposits	96,719	(60,053)
Decrease in term deposits	(253,101)	(354,636)
Decrease in other liabilities	(1,398)	(1,692)
Net cash flow from operating activities	**(45,144)**	**19,922**
CASH FLOW FROM INVESTING ACTIVITIES		
Purchase of financial assets at fair value through OCI	(513,513)	x
Sale of financial assets at fair value through OCI	631,450	x
Purchase of available-for-sale financial assets	x	(956,141)
Sale of available-for-sale financial assets	x	912,146
Increase in financial assets at amortised cost	(499)	x
Sale/(purchase) of held-to-maturity financial assets	x	15,520
Purchase of property, equipment and intangible assets	(1,653)	(1,491)
Proceeds from the sale of property	4,793	6,717
Net cash flow from investing activities	**120,578**	**(23,249)**
CASH FLOW FROM FINANCING ACTIVITIES		
Repayments of borrowings	(139,181)	(168,511)
New borrowings	90,000	40,000
Net cash flow from financing activities	**(49,181)**	**(128,511)**
Net change in cash and cash equivalents	**26,253**	**(131,838)**
Cash and cash equivalents at beginning of year (Note 35)	**201,420**	**333,258**
Effects of exchange rate changes on cash equivalents	**-**	**-**
Cash and cash equivalents at end of year (Note 35)	**227,673**	**201,420**

The Bank presented the information on cash flows from financing activities for 2017 on a net basis, which is presented in this report on a gross basis. In addition, the Interest received and Interest paid for 2017 and the item Gains on foreign currency trading is presented separately within non-cash items.

1. GENERAL INFORMATION ABOUT THE BANK

Legal framework and activities

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

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

The Bank has 11 branches - Branch Zagreb, Branch Čakovec, Branch Osijek, Branch Pula, Branch Požega, Branch Slavonski Brod, Branch Split, Branch Vinkovci, Branch Virovitica, Branch Vukovar, Branch Županja, and 3 outlets: Outlet Šubićeva, Outlet Sky Office, and Outlet Drenovci.

Bank bodies

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

Members of the Supervisory Board are elected i.e. appointed for a period of four years.

In 2018, the members of the Supervisory Board were:
From 1 January to 29 August 2018
Maruška Vizek, President
Josip Lozančić, Deputy President
Zdenka Pogarčić, Member
Ana Michieli Pavuna, Member

From 30 August to 31 December 2018
Maruška Vizek, President
Josip Lozančić, Deputy President
Zdenka Pogarčić, Member
Ana Michieli Pavuna, Member
Branka Grabovac, Member

In 2017, the members of the Supervisory Board were:

From 1 January to 24 January 2017
Maruška Vizek, President
Josip Lozančić, Deputy President
Branka Grabovac, Member

From 25 January to 31 December 2017
Maruška Vizek, President
Josip Lozančić, Deputy President
Branka Grabovac, Member
Zdenka Pogarčić, Member
Ana Michieli Pavuna, Member

1. GENERAL INFORMATION ABOUT THE BANK (continued)

Management Board

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

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

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

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

In 2018, the Management Board Members were as follows:

From 1 January 2018
Ivan Šverko - Member of the Management Board

From 2 January to 31 January 2018
Branka Grabovac, Deputy Member of the Management Board
Ivan Šverko - Member of the Management Board

From 31 January to 2 April 2018
Branka Grabovac, Deputy Member of the Management Board
Zoran Sabolić, Member of the Management Board

From 3 January to 30 June 2018
Branka Grabovac, Member of the Management Board
Zoran Sabolić, Member of the Management Board

From 1 July to 22 July 2018
Danijel Luković, President of the Management Board
Zoran Sabolić, Member of the Management Board

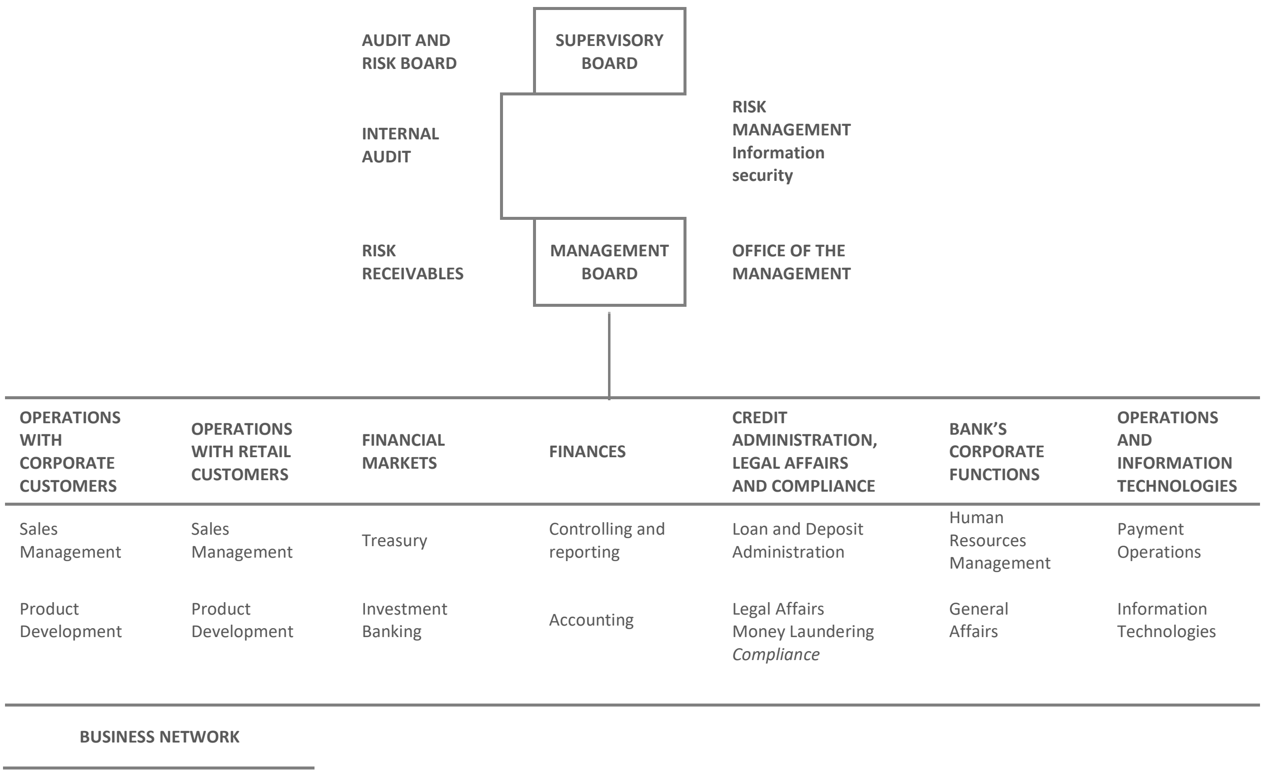
From 23 July to 31 December 2018
Danijel Luković, President of the Management Board
Tadija Vrdoljak, Member of the Management Board

Members of the Management Board in 2017 were as follows:

Mladen Duliba – President (until 31 December 2017)
Ivan Šverko – Member (until 31 December 2017)

1. GENERAL INFORMATION ABOUT THE BANK (continued)

Organisational structure



GOING CONCERN

Capital management

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

Similar to the previous year, in 2018 the Bank's lending activities continued to be focused on extending loans to the government and state-owned companies guaranteed by the Republic of Croatia that, under the applicable regulations, are not subject to capital requirements and still bring a satisfactory level of interest income. Regarding the sources of funds, the Bank achieved a fall in total deposits (in particular deposits of individuals) primarily as a result of the closure of two subsidiaries. Therefore, the Bank reduced excessive and unnecessary liquidity reserves, which resulted in significant reduction of interest costs. The Bank's business plan by 2020 is based on the currently available capital, planning to achieve profitable business operations in accordance with all legal regulations. If necessary for any reason, the Bank will also consider options for capital increase.

2. BASIS OF PREPARATION

Statement of compliance

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

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

The accounting regulations on the basis of which these financial statements have been prepared differ from IFRS.

The main differences between the accounting regulations of the CNB and the recognition and measurement requirements under IFRS in 2018 are provided below:

- The CNB requires banks to recognise impairment losses in the income statement at the prescribed minimum rate of 0.8% for exposures measured at amortised cost and performing off-balance sheet exposures (including central government risk). In accordance with these requirements, in the statement of financial position as at 31 December 2018, the Bank recorded provisions for impairment of performing placements in the amount of HRK 11,031 million. In accordance with the CNB regulations, the Bank continues to recognise these provisions as a replacement for expected losses accounted for in accordance with IFRS requirements.

- For certain non-performing exposures, the CNB prescribes minimum amounts of impairment provisions. These amounts may differ from impairment amounts calculated in accordance with IFRS.

- The CNB prescribes minimum impairment ratios and minimum collection periods for certain non-performing exposures for which future cash flows are estimated by collection from collateral. Therefore, impairment losses under IFRS may be lower for certain non-performing exposures.

- The CNB sets minimum provisions for legal disputes filed against the Bank in the amount of 1% of the total amount of the legal dispute in the event that the total amount of the legal dispute exceeds 0.1% of the Bank's assets according to the audited financial statements of the previous year.

The main differences between the accounting regulations of the CNB and the recognition and measurement requirements under IFRS in 2017 are provided below:

- The CNB requires banks to recognise impairment losse sin their income statements for exposures not identified as impaired on an individual basis (including those bearing the Central Government Risk) at the prescribed rates (with the exception of financial assets at fair value through profit or loss and assets available for sale). The portfolio-based provisions are presented on the Bank's balance sheet as at 31 December 2017 in accordance with the CNB requirements in the amount of HRK 12,940 and based on the CNB regulations, the Bank recognised the expense from these provisions within impairment losses for the year.
- The Bank accounts for impairment losses on loans and advances to customer by discounting the future expected cash flows using the original effective interest rate of the instrument, in accordance with International Financial Reporting Standards. The CNB requires the amortisation of the discount to be presented in the statement of comprehensive income as a change in impairment losses on loans and advances to customer instead of including them in interest income as required under IFRSs.
- The CNB prescribes minimum levels of provisions for impairment losses on certain specifically identified exposures, which may differ from the impairment losses calculated in accordance with IFRS.
- The CNB sets minimum provisions for legal disputes filed against the Bank in the amount of 1% of the total amount of the legal dispute in the event that the total amount of the legal dispute exceeds 0.1% of the Bank's assets according to the audited financial statements of the previous year.

Basis of measurement

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

Functional and presentation currency:

The financial statements have been prepared in HRK, which is the primary currency of the economic environment in which the Bank operates ("the functional currency"), and amounts are rounded to nearest thousand. The official exchange rate as at 31 December 2018 was HRK 7.417575 for EUR 1 (2017: HRK 7.513648) and HRK 6.469192 for USD 1 (2017: HRK 6.269733).

3. BASIS OF PREPARATION (continued)

3.1. New and amended standards adopted by the Bank

The bank applied the following standards and amendments for the annual reporting period beginning on 1 January 2018 for the first time:

- IFRS 9 Financial Instruments
- IFRS 15 Revenue from Contracts with Customers
- Annual Improvements for the Reporting Cycle from 2014 to 2016
- Transfer to investment property - Amendments to IAS 40
- IFRIC 22 Foreign Currency Transactions and Advance Consideration

Following the adoption of IFRS 9 the Bank needed to change its accounting policies and implement certain retrospective adjustments. This is set out in Note 15. Most of the above amendments did not have any effect on the amounts recognised in previous periods and they are not expected to affect significantly the current or future periods.

3.2. Standards and interpretations not yet adopted

Certain new accounting standards and interpretations have been published that are not mandatory for 31 December 2018 reporting periods and have not been early adopted by the Bank. The Bank's assessment of the impact of these new standards and interpretations is set out below:

- IFRS 16 Leases (effective for annual periods beginning on or after 1 January 2019, early adoption is permitted only if IFRS 15 is adopted at the same time)

  IFRS 16 was issued in January 2016. Under this standard the lessees are required to recognise virtually all leases in the balance sheet, as the difference between operating and finance leases has been eliminated and assets (right-of-use-assets for property leases) and financial lease liability are recognised. The only exception are short-term and low value leases.

  The Bank has set up a project team which has reviewed all leasing arrangements over the last year in light of the new lease accounting rules in IFRS 16. The standard will affect primarily the accounting for the Bank's operating leases. The Bank expects to recognise right-of-use assets of approximately HRK 4,137 thousand on 1 January 2019, lease liabilities of HRK 4,309 thousand (after adjustments for prepayments and accrued lease payments recognised as at 31 December 2018). The Bank expects that net profit after tax will decrease by approximately HRK 150,000 for 2019 as a result of adopting the new standard.

  The Bank will apply the standard from its mandatory adoption date of 1 January 2019. The Bank will apply the simplified transition approach and will not restate comparative amounts for the year prior to first adoption.

  There are no other standards not yet effective and which are expected to have a significant impact on the current period or any future reporting periods and future transactions.

3. SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies provided below have been consistently applied to all the years presented, unless otherwise stated.

Where the accounting policies are consistent with the accounting principles of International Financial Reporting Standards (hereinafter: "IFRS" or "Standards"), the Bank may refer to specific Standards in the description of the its accounting policies. Unless otherwise stated, these are Standards that have been applied on 31 December 2018

4.1. Financial assets and liabilities

Policy applicable as of 1 January 2018

Measurement techniques

Amortised cost is the amount at which the financial asset or financial liability is measured at initial recognition, net of prepayments, increased or decreased by the cumulative amortisation using the effective interest rate method of any difference between the initial amount and the amount of maturity and, in the case of financial assets, less the amount of the provision.

An effective interest rate is the rate used to discount the expected future proceeds or payments over the expected life of a financial asset or financial liability of the gross carrying amount of financial assets or the amount of the amortised cost of the financial liability. The calculation does not take into account the expected credit loss and includes transaction costs, premiums or discounts, fees and other payments and proceeds that are considered an integral part of the effective interest rate. An audit of expected future cash flows is carried out using the original effective interest rate.

Interest income and expense

Interest income is accounted for using the effective interest rate method applied to the gross carrying amount of financial assets, except for:

- Purchased or generated financial assets reduced by the credit risk. For such assets, an effective interest rate adjusted for credit risk is applied,
- Financial assets that are not purchased or generated financial assets net of credit losses but that subsequently became financial assets net of credit losses. For such assets, the effective interest rate is applied to the amortised cost of such assets in subsequent reporting periods.

The Bank recognises interest income only upon collection of financial assets allocated to Stage 3 of expected credit losses.

Initial recognition and measurement

The Bank recognises a financial asset or liability in the statement of financial position only if it becomes a party to the contractual provisions of the instrument.

The Bank initially recognises financial assets (other than trade receivables) or financial liabilities at their fair value, which, in the case of financial assets or financial liabilities not designated at fair value through profit or loss, increases or decreases by transaction costs that may be directly attributed to the acquisition or issue of a financial asset or financial liability.

FINANCIAL ASSETS

The Bank classifies financial assets into three basic categories:

- assets subsequently measured at amortised cost,
- assets subsequently measured at fair value through other comprehensive income, and
- assets subsequently measured at fair value through profit or loss.

4. SIGNIFICANT ACCOUNTING POLICIES (continued)

4.1. Financial assets and liabilities (continued)

Financial assets measured at amortised cost are assets whose purpose is to collect cash flows that are solely payments of principal and interest. The carrying amount is adjusted for the expected credit losses. Interest income is accounted for by applying the effective interest rate.

Financial assets measured at fair value through other comprehensive income are assets whose purpose is to collect contractual cash flows and to sell financial assets where cash flows of an asset are solely principal and interest payments. Changes in the carrying amounts are recognised in other comprehensive income, except for gains or losses on impairment, interest income and exchange rate differences that are recognised in the income statement. Upon derecognition of these financial assets the accumulated gains and losses previously recognised in other comprehensive income are reclassified from equity to profit and loss.

Financial assets measured at fair value through profit or loss are assets that are not measured at amortised cost or at fair value through other comprehensive income.

Business model

The Bank decides on a business model at a level that reflects the method of joint management of financial asset groups (portfolios) to achieve a specific business objective. In assessing the business model for managing financial assets the Bank relies on judgments based on the following information:

- Whether the strategic focus of management is to achieve interest income, in particular maintaining the interest rate profile, adjusting the maturity of financial assets to the maturity of the liabilities that are the source of the asset or the realisation of cash flows by selling assets,
- How to determine and report on portfolio performance,
- Risks affecting the business model's performance and how these risks are managed,
- How the managers are rewarded,
- Frequency, volume and time of sales in previous periods.

With the hold-to-collect business model for the purpose of collecting contracted cash flows or collecting cash flows and selling, the Bank estimates whether the cash flows of a financial instrument represent solely payments of principal and interest (SPPI test).

Impairment

The Bank recognises impairment allowances for the expected credit losses for the financial assets measured at amortised cost or measured at fair value through other comprehensive income and for the exposure arising from contingencies. At the reporting date, the Bank reviews whether there has been a change in the credit risk of the financial instrument after initial recognition and recognises the impairment gains or losses in profit and loss in the amount of expected losses or gains.

The measurement of expected credit losses reflects:

- an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes
- time value of money, and
- reasonable and supportable information on the reporting date that is available without undue cost or effort about past events, current conditions and forecasts of future economic conditions.

Debt modifications

The Bank sometimes modifies the contracted cash flows of client loans. When this happens, the Bank reviews whether the new conditions differ significantly from the terms of the contract initially agreed upon. The Bank then takes into account different circumstances:

- If a debtor has financial difficulties, does the modification only reduce the contracted cash flows to the amounts that the debtor expects to be able to pay,
- Has a new significant term been contracted affecting the repayment of the loan, which has a significant impact on the risk profile of the loan,
- A more significant extension of the loan repayment period when the borrower has no financial difficulties,
- Significant changes in the interest rate,
- Changes in the original currency of the loan,
- Adding collaterals, other security instruments or credit enhancement instruments that have a significant impact on credit risk.

4. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

4.1. Financial assets and liabilities (continued)

If the terms of the loan have changed considerably, the Bank derecognises the original loan and recognises a new loan at fair value and calculates the new effective interest rate on the loan. The date of the new contract is considered to be the date of initial recognition for the purposes of the calculation of the impairment, including any need for a significant increase in credit risk. Any difference in the carrying amount of the loan will be recognised in the income statement as a gain or loss on derecognition.

Derecognition other than on modification

Financial assets or a portion thereof, are derecognised when the Bank loses the rights to the cash flows from a financial asset or when it transfers the financial asset in a transaction by which substantially all the risks and rewards of ownership have been transferred to another entity.

The Bank enters into transactions where it retains contractual rights to cash flows from assets, but assumes a contractual obligation to pay those cash flows and transfers all of the significant risks and rewards. These transactions are accounted for as "pass through" transfers that result in derecognition if the Bank:.

- has no obligation to make payments unless it collects equivalent amounts from the assets,
- is prohibited from selling or pledging the assets, and
- has an obligation to remit any cash it collects from the assets without material delay.

FINANCIAL LIABILITIES

Classification and subsequent measurement

The Bank classifies the financial liabilities and subsequently measures them at amortised cost, except for

- Financial liabilities (including derivatives) designated at fair value through profit or loss.
- Financial liabilities arising from the transfer of financial assets which do not qualify for derecognition or if an approach to further participation is applied.
- Financial guarantee contracts.

Derecognition of financial liabilities

The Bank derecognises financial liabilities only when they are extinguished, i.e. when the obligation specified in the contract is discharged, cancelled or expires.
The difference between the carrying amount of a financial liability (or a portion of a financial liability) that has been met or transferred to another party and the consideration paid, including any non-cash transferred assets or liabilities assumed, is recognised in the income statement.

Contingent liabilities and commitments

Financial guarantees are contracts that require the Bank to make specific payments to reimburse the holder of the guarantee for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument. In the ordinary course of business, the Bank enters into arrangements by which it assumes contingent liabilities maintained on off-balance-sheet accounts and that primarily include guarantees, letters of credit and undrawn loan commitments and limits on lines of credit. Such financial commitments are recognised in the Bank’s statement of financial position if and when they become payable.

4. SIGNIFICANT ACCOUNTING POLICIES (continued)

4.1. *Financial assets and liabilities (continued)*

Classification of financial assets and liabilities at the IFRS 9 adoption date

Original measurement categories in accordance with IAS 39 and new measurement categories in accordance with IFRS 9 for financial assets and liabilities of the Bank as at 1 January 2018 are presented in the table below:

in thousands of HRK

	Classification under IAS 39	Carrying amount	Classification under IFRS 9	Carrying amount
Financial assets		**2,412,992**		**2,415,465**
Cash and receivables from the Croatian National Bank	Amortised cost (Loans and receivables)	326,225	Amortised cost	326,225
Placements with banks	Amortised cost (Loans and receivables)	23,092	Amortised cost	23,131
Investment securities	FVTOCI (Available for sale)	887,053	FVTOCI	887,053
Loans and advances to customers	Amortised cost (Loans and receivables)	1,152,529	Amortised cost	1,154,742
	Amortised cost (Loans and receivables)	492	FVTPL (mandatory)	492
Other financial receivables	Amortised cost (Loans and receivables)	23,601	Amortised cost	23,822
Financial liabilities		**2,328,477**		**2,328,778**
Liabilities to banks	Amortised cost	62,173	Amortised cost	62,173
Liabilities for deposits received	Amortised cost	2,094,110	Amortised cost	2,094,110
Liabilities for borrowings	Amortised cost	163,492	Amortised cost	163,492
Other financial liabilities	Amortised cost	7,591	Amortised cost	7,591
Off-balance sheet contingent liabilities for loans and financial guarantees	Amortised cost (Loans and receivables)	1,111	Amortised cost	1,412

4. SIGNIFICANT ACCOUNTING POLICIES (continued)

4.1. Financial assets and liabilities (continued)

in thousands of HRK

	IAS 39 carrying amount at 31 December 2017	Reclassification	Remeasurement	IFRS 9 carrying amount at 1 January 2018
Financial assets	**2,412,992**		**2,473**	**2,415,465**
Cash and receivables from the Croatian National Bank	326,225	-	-	326,225
Placements with banks	23,092	-	39	23,131
Investment securities	887,053			887,053
Loans and advances to customers (amortised cost)	1,153,021	(492)	2,213	1,154,742
Loans and advances to customers (FVPL)	-	492	-	492
Other financial receivables (amortised cost)	23,601	-	221	23,822
Financial liabilities	**2,328,477**		**301**	**2,328,778**
Liabilities to banks	62,173	-	-	62,173
Liabilities for deposits received	2,094,110			2,094,110
Liabilities for borrowings	163,492			163,492
Other financial liabilities	7,591	-	-	7,591
Off-balance sheet contingent liabilities for loans and financial guarantees	1,111	-	301	1,412

4. SIGNIFICANT ACCOUNTING POLICIES (continued)

4.1. Financial assets and liabilities (continued)

Classification of financial assets and liabilities and remeasurement at the IFRS 9 adoption date

The following table presents:

- closing balance of provisions for impairment of financial assets in accordance with IAS 39 and provisions for loan liabilities and financial guarantee contracts in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets as at 31 December 2017
- opening balances of ECL determined in accordance with IFRS 9 as at 1 January 2018

in thousands of HRK

	31 December 2017 (IAS 39(IAS 37)	Reclassification	Remeasurement	1 January 2018 (IFRS 9)
Loans and receivables (IAS 39)/Financial assets at amortised cost (IFRS 9)				
Cash and receivables from the Croatian National Bank	3,424	-	-	3,424
Placements with banks	233	-	(39)	194
Available for sale (IAS 39)/FVOCI (IFRS 9)				
Investment securities	29,467	-	-	29,467
Loans and receivables (IAS 39)/Financial assets at amortised cost (IFRS 9)				
Loans and advances to customers				
Loans and receivables (IAS 39)/FVTPL (IFRS 9)				
Loans and advances to customers	-	1,147	-	1,147
Loans and receivables (IAS 39)/Financial assets at amortised cost (IFRS 9)				
Other financial receivables	19,714	-	(221)	19,493
Off-balance sheet contingent liabilities for loans and financial guarantees (amortised cost)	1,111		(301)	810

The reconciliation between the financial assets exposure not subject to impairment is provided in the table below:

in thousands of HRK

	Maximum amount of exposure
Financial assets at fair value through profit or loss	
Loans and advances to customers	492

4. SIGNIFICANT ACCOUNTING POLICIES (continued)

4.1. Financial assets and liabilities (continued)

The policy applied until 31 December 2017.

Classification

The Bank classifies its financial assets into the following categories: loans and receivables, financial assets available for sale, financial assets at fair value through profit or loss, financial assets held to maturity and financial liabilities at amortised cost. The classification depends on the purpose for which the financial instruments were acquired. Management determines the classification of financial instruments at initial recognition.

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

Loans and receivables

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

Available-for-sale financial assets

This category includes non-derivative financial assets that are not defined as loans and receivables or investments held-to-maturity, or are not defined as financial assets at fair value through profit or loss. Financial assets defined as available for sale are intended to be held indefinitely, but may be sold in response to needs for liquidity or changes in interest rates, changes in exchange rates or debt security prices.

Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading and those classified at initial recognition by management as financial assets at fair value through profit or loss. A financial asset is classified in this category if it is acquired or incurred principally for the purpose of selling or repurchasing in the near term, for short-term profit or if so designated by management.

Financial instruments held for trading include shares in investment funds.

Financial assets held to maturity

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

Other financial liabilities

Other financial liabilities include all financial liabilities that are not allocated at fair value through profit or loss.

Recognition and derecognition

Acquisitions and sale of financial assets available for sale are recognized on the trade date, i.e. the date on which the financial instrument is delivered or transferred by the Bank. Loans and receivables, financial assets held to maturity and financial liabilities at amortised cost are recognised when funds are given or received.

The Bank derecognizes financial instruments (in whole or in part) when its rights to receive cash flows from the financial asset expire, or when it loses control of the contractual rights of the instrument. It occurs when the Bank transfers substantially all the risks and rewards of ownership to another entity or when the rights are realised, expired or are surrendered. The Bank derecognises financial liabilities only when the financial liability ceases to

4. SIGNIFICANT ACCOUNTING POLICIES (continued)

4.1. Financial assets and liabilities (continued)

exist; it is discharged, cancelled or expires. If the terms of a financial liability significantly change, the Bank will derecognise that liability and will recognise a new financial liability, with new terms.

Realised gains and losses from the sale of financial instruments are calculated using the average acquisition cost method.

Initial and subsequent measurement

Financial assets available for sale, loans, receivables, financial assets held to maturity and liabilities are recognized initially at fair value plus transaction costs that are directly attributable to the acquisition or issue of financial assets or financial liabilities.

The Bank initially recognises financial assets or liabilities carried at fair value and transaction costs are expensed in the income statement.

After initial recognition, the Bank evaluates the financial assets available for sale and financial assets and liabilities at fair value through profit or loss, without any deduction for transaction costs.

Loans and receivables, financial assets held to maturity and financial liabilities which are not carried at fair value through profit or loss are measured at amortised cost, applying the effective interest rate.

Gains and losses

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

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

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

Impairment of financial assets

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

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

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

4. SIGNIFICANT ACCOUNTING POLICIES (continued)

4.1. Financial assets and liabilities (continued)

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

Impairment of assets not identified as impaired

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

Accounting policies applied in the previous and current period

4.1.1. Determination of fair value

Fair value is the price that would be received by selling an item of asset or paid for the transfer of a liability in an arm's length transaction between market participants at the measurement date.
When measuring the fair value, the following asset or liability characteristics should be considered:

- asset condition and location and
- any restrictions on the sale or use of the asset.

The impact of a particular characteristic on the measurement will vary depending on how the market participants would consider it.
Assets or liabilities measured at fair value may be, either:

- an independent asset or liability item, or
- a group of items of assets or liabilities or a group of items of assets and liabilities.

The fair value measure assumes that the asset sale transaction, i.e. the transfer of the liability, takes place either

- on the primary market of the respective asset or liability, or
- if the primary market does not exist, on the most favourable market for the asset i.e. the liability concerned.

Where possible, fair value reflects the quoted price on the primary market the Bank has access to.
A financial instrument is considered as quoted on an active market if quoted prices are easily and regularly available and those prices represent actual and regularly occurring market transactions on an arm's-length basis.
If there is no quoted price on the active market for financial instruments as a whole, but there is an active market for their components, the fair value is determined on the basis of the relevant market values of the components.
If the market for a financial instrument is not active and if for any reason it is not possible to reliably measure fair value then fair value is determined by applying valuation techniques that use the relevant and available parameters to the fullest extent, which include all the factors that the market participants used to evaluate the transaction.
Fair value measurements of non-financial assets take into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

4. SIGNIFICANT ACCOUNTING POLICIES (continued)

4.1. Financial assets and liabilities (continued)

4.1.2 Fair value hierarchy

For a higher consistency and comparability of fair value measures and related information, a fair value hierarchy has been established, consisting of three levels. The highest importance is given to prices quoted on active markets for identical assets, i.e. liabilities (Level 1 inputs), and the lowest on unobservable inputs (Level 3 inputs). The input categories according to their degree of availability and significance in relation to the total fair value measure are:

- Level 1 inputs (unadjusted) are quoted prices in active markets for identical assets or liabilities that the entity can access at the measurement date
- Level 2 inputs are inputs other than quoted market prices included within Level 1 that are observable for the asset or liability, either directly or indirectly
- Level 3 inputs are unobservable inputs for the asset or liability.

4.2. Income tax

Income tax is based on taxable income for the year and comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity or other comprehensive income, in which case the tax is recognised in equity or other comprehensive income. Current tax is the expected tax payable on the taxable income for the year, using the tax rates enacted at the reporting 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 measurement of deferred tax assets and liabilities reflects the tax consequences that would follow from the manner in which the enterprise expects, at the balance sheet date, to recover or settle the carrying amount of its assets and liabilities, based on tax rates enacted or substantially enacted at the balance sheet date.

Deferred tax assets and liabilities are not discounted and are classified as long-term assets and/or liabilities in the balance sheet. Deferred tax assets are recognised only to the extent that it is probable that they could be utilised as a tax benefit. At each reporting date, the Bank reassesses unrecognized potential deferred tax assets and the carrying amount of recognized deferred tax assets.

4.3. Cash and cash equivalents

Cash and cash equivalents include cash and current accounts with the Croatian National Bank with an original maturity of up to 90 days and with other banks, deducted for provision for impairment on collective basis and uncollectible amounts, and items in process of collection.

4. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

4.4. Property and equipment

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

Depreciation is calculated on a straight-line basis to allocate the cost of assets to their residual values over their estimated useful lives. Land and assets under construction are not depreciated.

Assets' residual values, depreciation method and estimated useful life are reviewed at each balance sheet date and adjusted if appropriate. The carrying value of an asset is written down immediately to its recoverable amount if the asset's carrying amount exceeds its recoverable amount. Profits and losses on disposals are determined by comparing the amount collected and the carrying amount, and are included in the profit and loss account.

Tangible assets are depreciated on a straight-line basis over their estimated useful lives as follows:

	2018	**2017**
Buildings	2.50%	2.50%
Computers	25%	25%
Furniture and equipment	10% - 20%	10% - 20%
Vehicles	25%	25%
Other not listed tangible assets	5% - 10%	5% - 10%

4.5. Intangible assets

Intangible assets are recorded at cost less accumulated amortisation and impairment. Expenditure on development activities is recognised as an intangible asset if it meets all the requirements in accordance with IAS 38 "Intangible Assets”. Amortisation is calculated on a straight-line basis over the estimated useful lives of intangible assets.

Intangible assets are amortised on a straight-line basis over their estimated useful lives as follows:

	2018	**2017**
Intangible assets (other)	10% - 20%	10% - 20%
Intangible assets – *software*	20% - 25%	20% - 25%

4. SIGNIFICANT ACCOUNTING POLICIES (continued)

4.6. Foreclosed assets

For assets acquired in lieu of uncollected receivables the Bank assesses the marketability and only marketable assets, the value of which can be measured reliably, are recognised. Such assets are stated at the lower of the cost of related outstanding receivables and the current fair value of that asset. The Bank’s intention is to sell such assets as soon as possible (such assets are not amortised). After initial recognition the foreclosed assets are subsequently measured in accordance with IAS 2 Inventories.

4.7. Assets held for sale

Tangible assets taken over in exchange for uncollected receivables are stated in the statement of financial position on the assets held for sale if the following conditions are met:

- there is a sales plan and activities are carried out to find a buyer,
- the assets are ready for sale in the present state,
- sales are highly probable,
- assets offered for sale at a reasonable price, or when the price of an asset is acceptable in relation to its market value, and it is unlikely that there will be significant deviations from the sale or resignation plan,
- sales should be completed within one year from the date of classification, unless the delay is caused by events or circumstances beyond the control of the Bank and there is sufficient evidence that it will remain in compliance with the asset sales plan.

In cases where due to the aggravating circumstances of sales caused by events or circumstances beyond the control of the Bank and there is sufficient evidence that the Bank has remained consistent with its sales plan, tangible assets taken over in exchange for uncollected receivables will continue to be recognized, measured and disclosed as an asset held for sale.

This asset category is initially recognized at fair value, net of estimated expected selling costs.

These assets are subsequently measured at the lower of the net carrying amount and fair value net of selling costs. If the above conditions are not met, the Bank's material assets taken over in exchange for uncollected receivables are initially recognised as held assets in accordance with International Accounting Standard 2 Inventories.

4.8. Investment property

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

Investment property is carried at cost. At subsequent measurement of investment property, the Bank applies the fair value model. The Bank conducts measurement of fair value on an income basis annually by an independent valuer.

The purchase cost is the amount of money or cash equivalents paid or the fair value of other consideration paid for the purpose of acquiring such property. Transaction costs are included in the initial measurement.

4. SIGNIFICANT ACCOUNTING POLICIES (continued)

4.9. Impairment of non-financial assets

Assets that are subject to amortisation and depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

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

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

4.10. Provisions for liabilities and charges

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

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

When an outflow of economic benefits to settle the obligations is no longer probable, the provision is reversed. Provisions are released only for those costs in respect of which provisions are recognised at inception.

4.11. Employee benefits

The Bank makes payments to the mandatory pension funds on behalf of its employees as required by law. The Bank has no further payment obligations once the contributions have been paid. The contributions are recognised as employee benefit expense when they arise.

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

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

4.12. Share capital and reserves

Share capital is denominated in HRK at nominal value.

4. SIGNIFICANT ACCOUNTING POLICIES (continued)

4.13. Accumulated losses

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

4.14. Fee and commission income and expense

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

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

4.15. Foreign currencies

Transactions in foreign currencies are translated into HRK applying the middle exchange rate of CNB at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the financial statements date are translated at the exchange rate defined at the financial statements date. Foreign exchange differences arising on translation are recognized in the income statement. Non-monetary assets and liabilities denominated in foreign currencies and measured at fair value are translated into HRK at the foreign exchange rate prevailing at the date on which their fair value was determined. Non-monetary assets and items that are measured in terms of historical cost in a foreign currency are translated at the exchange rate at the transaction date and are not retranslated at the date of the statement of financial position.

Changes in the fair value of monetary securities denominated in foreign currency classified as available for sale are analysed between translation differences resulting from changes in amortized cost of the security and other changes in the carrying amount of the securities. Exchange differences are recognized in the income statement as part of the foreign exchange gains or losses on conversion of monetary assets and liabilities.

4.16. Leases

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

4.17. Borrowings

Borrowings are recognised initially at fair value, net of associated costs. Subsequent valuation is carried at amortised cost and the difference between proceeds less transaction costs, and the amount payable at maturity is recognised in the income statement during the period of the borrowings as interest expense.

4.18. Activities for and on behalf of third parties

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

4.19. Segment reporting

A business segment is an integral part of the Bank that engages in business activities from which it may earn revenues or expenses, including transactions with other parts of the Bank. In 2017, the Bank did not apply the internal transfer pricing when determining business performance of individual segments.

4. SIGNIFICANT ACCOUNTING POLICIES (continued)

4.20. Accounting estimates and judgments in application of accounting policies

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

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

The sensitivity analysis with regard to changes in property prices (increase or decrease in market price by 1%) is disclosed in Note 20 Investment property, 22 Foreclosed assets and 23 Assets held for sale.

4.20.1. Losses on impairment of loans and advances

The Bank monitors the creditworthiness of its customers on an ongoing basis. On-balance sheet and off-balance sheet credit risk exposures are reviewed for impairment on a quarterly basis. Impairment losses are generally charged to the carrying amount of loans and receivables issued to retail and corporate customer and as provisions for risk and charges arising from off-balance sheet exposures to customers, which mostly take on the form of approved, but not utilised loans, guarantees and letters of credit. In addition to individually identified impairment losses, the Bank monitors and recognises, on an ongoing-basis, impairment losses that are known to exist at the financial statements date, but have not been separately identified. In assessing unidentified impairment losses on a portfolio basis, the Bank seeks to collect sufficient reliable information about appropriate loss rates, based on its historical experience, adjusted to reflect the current circumstances and the period in which the loss is identified. For more details please refer to Note 37.1. Credit risk.

4.20.2. Legal disputes

The Bank conducts individual assessments of all court proceedings against the Bank. The assessment is conducted by the Bank’s Legal department. As set out in Note 31, the Bank has provided for HRK 12,614 thousand in principal and interest on liabilities for legal disputes (2017: HRK 7,065 thousand). These amounts represent the Bank’s best estimate of losses on legal disputes.

4.20.3. Investment property

Investment property is initially carried at fair value. At subsequent measurement of investment property, the Bank applies the fair value model. The Bank performs measurement of fair value on a yearly basis by an independent valuer.

5. INTEREST INCOME

5.1. Interest income by type of customer

in thousands of HRK

	2018	2017
Corporate	36,708	60,945
Retail	23,545	26,602
Government units	6,684	9,325
Banks and other financial institutions	444	1,211
Other organisations	43	73
Total	**67,424**	**98,156**

Interest income comprises income from partially recoverable placements in the amount of HRK 8.1 million (2017: HRK 5.4 million) of which HRK 7.7 million (2017: HRK 4.2 million) relates to corporate transactions, and the remaining HRK 0.4 million (2017: HRK 1.2 million) relates to retail transactions.

5.2. Interest income analysed by portfolio

in thousands of HRK

	2018	2017
Financial assets at amortised cost	62,022	x
Loans and receivables	x	89,286
Financial assets at fair value through other comprehensive income	5,391	x
Financial assets available for sale	x	5,847
Financial assets held to maturity	x	3,023
Financial assets not held for trading and mandatorily measured at fair value through profit or loss	11	x
Total	**67,424**	**98,156**

6. INTEREST EXPENSE

6.1. Interest expense analysed by type of customer

in thousands of HRK

	2018	2017
Retail	17,932	28,558
Croatian National Bank	1,893	2,150
Non-residents	1,383	2,602
Banks and other financial institutions	1,074	3,921
Corporate	999	1,592
Government units	179	527
Other organisations	142	153
Total	**23,602**	**39,503**

6. INTEREST EXPENSE (CONTINUED)

6.2. Interest expense by portfolio

in thousands of HRK

	2018	2017
Financial liabilities at amortised cost	23,602	39,503
Total	**23,602**	**39,503**

7. FEE AND COMMISSION INCOME

7.1. Income from fees by type of customer

in thousands of HRK

	2018	2017
Corporate	4,571	5,088
Retail	3,341	4,071
Financial institutions	631	730
Non-profit organisations	240	262
Government units	222	219
Non-residents	111	83
Total	**9,116**	**10,453**

7.2. Income from fees by type

in thousands of HRK

	2018	2017
Payment transaction fees	3,398	4,035
Fees from guarantees and letters of credit	1,607	1,430
Account maintenance fees	1,168	1,510
Online banking fees	903	924
Card transaction fees	532	553
Income from fees - sales of third-party products	151	187
Brokerage and custodial fees	275	524
Other commissions	1,082	1,290
Total	**9,116**	**10,453**

8. FEE AND COMMISSION EXPENSE

8.1. Fee and commission expense by type of customer

in thousands of HRK

	2018	2017
Domestic clients	(1,819)	(2,948)
Service fees and commissions to FINA	(1,438)	(1,602)
Foreign banks	(240)	(167)
Republic of Croatia	(49)	(36)
Total	**(3,546)**	**(4,753)**

8.2. Fee and commission expense by types

in thousands of HRK

	2018	2017
FINA's non-cash and cash payment services (clients)	(1,418)	(1,602)
Credit card commission	(1,371)	(1,642)
Financial institutions service costs	(545)	(1,217)
Authorised exchange office services	(61)	(81)
Other commissions	(151)	(211)
Total	**(3,546)**	**(4,753)**

9. NET FINANCIAL GAINS

in thousands of HRK

	2018	2017
Net gains on assets at fair value through other comprehensive income	639	x
Net gains on sale of financial assets available for sale	x	9,773
Net gains on realisation of held-to-maturity financial assets	x	5,411
Income from foreign currency trading	2,382	3,161
Total	**3,021**	**18,345**

The realised net gains on held-to-maturity assets relate to the sale of bonds classified by the Bank as held-to-maturity portfolio at initial recognition.

10. NET FOREIGN EXCHANGE LOSSES

in thousands of HRK

	2018	2017
Net gain on exchange differences, from revaluation of monetary balance sheet items to CNB's mid foreign exchange rate		
Net gain on exchange differences, from revaluation of impairment of provisions for potential losses on loans to CNB's mid foreign exchange rate	7,926	1,659
Net loss on exchange differences, from revaluation of balance sheet items with a currency clause to CNB's mid exchange rate	682	148
	(8,655)	(2,225)
Total		
	(47)	**(418)**

11. OTHER OPERATING INCOME

in thousands of HRK

	2018	2017
Rental income	4,560	4,196
Net gain on sale of property, plant and equipment and foreclosed assets	1,883	4,073
Collection under suspended interest income	50	5
Gain on revaluation of Investment property to fair value	816	-
Other income	1,213	420
Total	**8,522**	**8,694**

12. OTHER OPERATING EXPENSES

	2018	2017
Net salaries	16.64	18,355
Pension contributions	4,814	5,251
Contributions, taxes and surtaxes	6,764	7,305
Other staff costs	2,266	2,329
Provisions for employee benefits (Note 30)	171	46
Total staff costs	**30,662**	**33,286**
Depreciation and amortisation (Note 22)	2,964	3,425
Total depreciation and amortisation	**2,964**	**3,425**
Material and services	14,514	14,736
Rental expenses	4,838	5,308
Marketing	236	460
Judicial and administrative fees	895	1,415
Deposits insurance premiums	5,266	5,576
Other	1,467	3,440
Total other operating expenses	**27,216**	**30,935**
Total	**60,842**	**67,646**

As at 31 December 2018, the Bank had 175 employees (31 December 2017: 191 employees).

Staff costs include HRK 4,814 thousand (2017: HRK 5,251 thousand) of prescribed pension contributions paid into mandatory pension funds. Contributions are determined at a certain percentage of employees' gross salaries.

12. OTHER OPERATING EXPENSES (continued)

12.1. Rental costs

Rental costs mainly relate to rental costs of office space in which the Bank carries out its activities. In 2018, the rental costs amounted to HRK 4,838 thousand (2017: HRK 5,308 thousand).
Minimum payments under operating lease are presented below:

31 December 2018

in thousands of HRK

	Up to 1 year	1 to 2 years	2 to 5 years
Rental cost / payment	4,838	4,433	4,433

31 December 2017

in thousands of HRK

	Up to 1 year	1-2 years	2 to 5 years
Rental cost / payment	5,308	5,308	5,308

13. IMPAIRMENT LOSSES AND PROVISIONS

in thousands of HRK

	2018	2017
Impairment of loans and advances to customers (Note 19.2)	(2,695)	19,115
Impairment of securities (Note 18)	(12,054)	(28,693)
Impairment of interest receivable (Note 19.2)	59	(70)
Impairment of other assets	(669)	(1,698)
Impairment of tangible and foreclosed assets (Note 22, 23)	(184)	(6,988)
Income from collection of loans written-off in previous years	311	475
Impairment of deposits with banks	(419)	-
Reversal of provisions and impairment losses on a collective basis for other receivables (Note 16, 17, 18 and 25)	x	2,440
Provision for legal disputes against the Bank (Note 30)	(6,325)	(1,307)
Provisions for contingencies (Note 30)	(149)	423
Impairment losses on non-financial assets	-	(72)
Other provisions	(7)	(10)
Total expenses of impairment losses and provisions	**(22,132)**	**(54,615)**

Note: The impairment of securities mainly relates to bills of exchange which were reclassified from the available-for-sale portfolio to the portfolio at amortised cost in 2018.

14. INCOME TAX

	2018	2017
	in thousands of HRK	
Accounting loss before tax	**(22,086)**	**(31,286)**
Effect of items increasing tax base	9,353	9,205
Effect of items decreasing tax base	(5,262)	(5,303)
Tax base	**(17,995)**	**(27,384)**

Movements in tax losses carried forward

	2018	2017
	in thousands of HRK	
Tax losses carried forward from the previous period	**(149,379)**	**(122,268)**
Increase in tax losses from the previous period	**(17,995)**	**(27,111)**
Utilisation of tax losses	-	-
Expiration of tax losses carried forward	111,258	-
Tax loss available for carry forward in future periods	**(56,116)**	**(149,379)**
Deferred tax assets at 18% (2017: 18%)	(10,101)	(26,888)
Recognised deferred tax assets	-	-
Unrecognised deferred tax assets	(10,101)	(26,888)

Tax losses expire as follows:

in thousands of HRK

Tax loss expiry	Tax loss
2018	11,010
2022	27,111
2023	17,995
Total	**56,116**

Deferred tax assets from tax losses carried forward were not recognised as its utilisation in future periods is uncertain.

14. INCOME TAX (CONTINUED)

Movements in deferred tax assets

in thousands of HRK

	Deferred fee income included in effective interest rate on given loans	Impairment of foreclosed assets	Unrealised fair value of financial assets AFS/OCI	Amortisation above tax rate	Tax losses	Total
At 1 January 2017	**1,571**	**1,265**	**(1,223)**	**-**	**285**	**1,898**
Recognised in profit or loss	(363)	913	-	106	-	656
Recognised in other comprehensive income	-	-	1,536	-	-	1,536
At 31 December 2017	**1,208**	**2,178**	**313**	**106**	**285**	**4,090**
Recognised in profit or loss	(430)	(2,178)	-	(10)	(285)	(2,903)
Recognised in other comprehensive income	-	-	(68)	-	-	(68)
At 31 December 2018	**778**	**-**	**245**	**96**	**-**	**1.119**

15. CASH

in thousands of HRK

	31 December 2018	31 December 2017
Giro account	178,191	67,339
Cash on hand:		
- HRK	11,782	13,596
- foreign currency	6,772	21,769
Cash in foreign currency accounts in domestic banks	9,142	71,340
Cash in foreign currency accounts in foreign banks	2,409	4,046
Checks and other assets in the course of collection	1	5
Expected credit losses (IFRS 9)	(1,946)	**x**
Provisions for impairment for unidentified losses on a collective basis (IAS 39)	x	(1,427)
Total	**206,351**	**176,668**

16. RECEIVABLES FROM THE CROATIAN NATIONAL BANK

in thousands of HRK

	31 December 2018	31 December 2017
Obligatory reserve		
- HRK	143,865	151,068
Expected credit losses (IFRS 9)	*(1,478)*	*x*
Provisions for impairment for unidentified losses on a collective basis	*(1,478)*	*(1,511)*
Total	**142,387**	**149,557**

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

The reserve requirement rate as at 31 December 2018 was 12% (2017: 12%) of HRK and foreign currency deposits, borrowings and issued debt securities.

At 31 December 2018, the required rate for the part of the HRK obligatory reserve with the CNB amounted to 70% (2017: 70%) and the foreign-currency denominated portion 0% (2017: 0%), while the remaining 30% (2017: 30%) is held in the form of other liquid receivables. This includes the part of foreign currency obligatory reserve required to be held in HRK. The foreign-currency portion of the obligatory reserve is maintained through daily balances of foreign-currency receivables on the Target 2 foreign-currency account with the Croatian National Bank as well as on accounts with foreign banks with appropriate ratings. The minimum share of the foreign-currency reserve funds on the CNB Target2 reserve account is 2%, whereas 75% of the foreign-currency reserve funds are included in the allocated HRK-denominated obligatory reserve funds and maintained in HRK.

17. PLACEMENTS WITH BANKS

in thousands of HRK

	31 December 2018	31 December 2017
Deposits with foreign banks	18,952	22,892
Deposits with domestic banks	418	424
Accrued interest	6	9
Expected credit losses (IFRS 9)	*(127)*	*x*
Provisions for impairment for unidentified losses on a collective basis	*x*	*(233)*
Total	**19,249**	**23,092**

18. FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME AT 31 DECEMBER 2018/AVAILABLE FOR SALE AT 31 DECEMBER 2017

in thousands of HRK

	31 December 2018	**31 December 2017**
Bonds of the Republic of Croatia with a currency clause	196,622	
Treasury bills of the Republic of Croatia denominated in foreign currency	155,754	-
Treasury bills of the Republic of Croatia with a currency clause	140,934	-
Foreign currency bonds of foreign countries	94,483	-
HRK-denominated treasury bills of the Republic of Croati	79,981	462,839
Foreign currency bonds of the Republic of Croatia	66,668	228,099
HRK-denominated bonds of the Republic of Croatia	12,181	179,886
Corporate bills of exchange	774	13,130
Shares	439	439
Impairment	*(774)*	*(774)*
Accrued interest	5,619	3,434
Total	**752,681**	**887,053**

18.1. FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME AT 31 DECEMBER 2018/AVAILABLE FOR SALE AT 31 DECEMBER 2017 (CONTINUED)

in thousands of HRK

	Treasury bills	Bonds	Shares	Bills of exchange	Accrued interest	TOTAL
At 31 December 2017	**462,839**	**407,985**	**439**	**12,356**	**3,434**	**887,053**
Reclassification	-	-	-	(12,356)	-	(12,356)
At 1 January 2018	**462,839**	**407,985**	**439**		**3,434**	**916,520**
Purchase	220,184	293,329	-	-	2.185	515,698
Change in fair value	-	371	-	-	-	371
Sale	(303,339)	(333,502)	-	-	-	(636,841)
Other (write-off, exchange differences)	(3,015)	1,771	-	-	-	(1,244)
At 31 December 2018	**376,669**	**369,954**	**439**	**-**	**5,619**	**752,681**

	Treasury bills	Bonds	Shares	Bills of exchange	Accrued interest	TOTAL
At 1 January 2017	**498,257**	**328,021**	**439**	**-**	**7,056**	**833,773**
Purchase	502,015	454,126	-	-	-	956,141
Change in fair value (without the impact of deferred tax assets)	-	(8,531)	-	-	-	(8,531)
Sale	(537,433)	(365,631)	-	-	(3,622)	(906,686)
Reclassification	-	-	-	12,356	(29,467)	12,356
At 31 December 2017	**462,839**	**407,985**	**439**	**12,356**	**3,434**	**887,053**

As at 31 December 2018, the Bank has pledged, based on received HRK 110,000 thousand of structured loans with financial insurance by the Croatian National Bank (2017: HRK 110,000 thousand of received structured loans from the Croatian National Bank and received HRK 40,000 thousand of repo loans from Erste&Steiermärkische Bank) the treasury bills in the total amount of HRK 116,167 thousand (2017: HRK 162,697 thousand of treasury bills and government bonds).
There were no securities received as pledge as at 31 December 2018, since there were no placements in repo loans (2017: HRK 6,100 thousand of loans, HRK 8,924 thousand of pledges).

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

- Level 1 - instruments that are valued using quoted prices in active markets, liquid markets. These instruments include: liquid debt securities that are traded on liquid stock markets and shares in investment funds.
- Level 2 - instruments that are valued using valuation techniques that use available market data. These are instruments whose fair value is determined in the amount of similar instruments traded in active markets, or where all the inputs used for valuation techniques are available on the market.
- These instruments include less liquid debt securities that are valued based on a model that uses level 1 input.
- Level 3 – instruments measured using valuation techniques that are based on market data not readily available in the market. These are instruments whose fair value cannot be determined directly by

18.1. FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME AT 31 DECEMBER 2018/AVAILABLE FOR SALE AT 31 DECEMBER 2017 (CONTINUED)

reference to available market information and for whose value calculation different valuation techniques are used. These instruments include illiquid debt securities and illiquid equity securities.

The following note shows net financial assets categorised according to the stated IFRS fair value hierarchy (shown without interest receivable):

in thousands of HRK

	31 December 2018				31 December 2017			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Foreign currency bonds	161,151	-	-	161,151	228,099	-	-	228,099
HRK-denominated bonds	208,803			208,803	179,886			179,886
Treasury bills	-	376,669	-	376,669	-	462,839	-	462,839
Bills of exchange	-	-	-		-	-	12,356	12,356
Shares	-	-	439	439	-	-	439	439
Total	**369.954**	**376.669**	**439**	**747.062**	**407.985**	**462.839**	**12.795**	**883.619**

Bills of exchange sensitivity analysis for 2017, assuming a 5% increase or decrease in impairment of the bill of exchange, represents a net change in profit or loss of HRK 2,050 thousand. At the end of 2018, the Bank had no bills of exchange in the asset portfolio measured at fair value through other comprehensive income.

19. LOANS AND ADVANCES TO CUSTOMERS

19.1. Analysis by type of client

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

in thousands of HRK

	31 December 2018				31 December 2017
	Level 1	Level 2	Level 3	TOTAL	
Retail					
Cash loans	143,872	9,772	10,805	164,449	170,883
Housing loans	49,405	1,883	2,420	53,708	56,910
Loans for agriculture	29,388	2,534	13,405	45,327	34,720
Other loans	13,950	2,999	24,445	41,394	128,262
Margin loans	25,319	490	-	25,809	-
Overdrafts on transaction accounts	13,725	88	1,752	15,565	15,732
Loans for tourism	1,026	4,877	6,471	12,374	-
Lombard loans	11,236	734	19	11,989	-
Mortgage loans	6,638	379	1,295	8,312	6,641
Total retail loans	**294,559**	**23,756**	**60,612**	**378,927**	**413,148**
Expected credit losses	*(2,616)*	*(201)*	*(37,471)*	*(40,288)*	*x*
Provisions for impairment for identified losses					*(38,546)*
Provisions for imp. for unidentified losses on a collective basis	-	-	-	-	*(3,557)*
Interest impairment provision – individuals	-	-	*(282)*	*(282)*	*(442)*
Total provisions for impairment – individuals	*(2,616)*	*(201)*	*(37,753)*	*(40,570)*	*(42,545)*
Accrued interest	1,625	160	282	2,067	2,588
Total retail loans, net	**293,568**	**23,715**	**23,141**	**340,424**	**373,191**
Corporate					
Syndicated loan	373,419	-	-	373,419	378,891
Investment loans	45,718	35,680	152,670	234,068	250,205
Working-capital loans	61,099	10,629	63,065	134,793	160,893
Other loans	23,446	31	81,516	104,993	163,582
Lombard loans	1,723	45,210	-	46,933	-
Overdrafts on transaction accounts	6,551	3,003	2,417	11,971	37,321
Loans for agriculture	3,439	87	5,493	9,019	-
Loans for payments under guarantees	-	-	2,129	2,129	2,458
Total corporate loans	**515,395**	**94,640**	**307,290**	**917,325**	**993,350**
Expected credit losses	*(3,593)*	*(651)*	*(175,196)*	*(179,440)*	-
Provisions for impairment for identified losses	-	-	-	-	*(210,113)*
Provisions for imp. for unidentified losses on a collective basis	-	-	-	-	*(6,079)*
Interest impairment provision – corporate	-	-	*(928)*	*(928)*	*(1,794)*
Total provisions for impairment	*(3,593)*	*(651)*	*(176,124)*	*(180,368)*	*(217,986)*
Accrued interest	2,205	816	928	3,949	4,466
Total corporate loans, net	**514,007**	**94,805**	**132,094**	**740,906**	**779,830**
Total loans (gross)	***813,784***	***119,372***	***369,112***	***1,302,268***	***1,413,552***
Total provisions for loans	*(6,209)*	*(852)*	*(213,877)*	*(220,938)*	*(260,531)*
Total loans and advances to customers, net	**807,575**	**118,520**	**155,235**	**1,081,330**	**1,153,021**

19. LOANS AND ADVANCES TO CUSTOMERS (CONTINUED)

19.1. Analysis by type of client (continued)

As at 31 December 2018, the gross exposure arising from partly recoverable and non-recoverable loans was HRK 369,112 thousand (2017: HRK 451,196 thousand), and the associated impairment losses amounted to HRK 213,877 thousand (2017: HRK 248,659 thousand).

19.2. Changes in impairment losses and provision for contingent losses

Changes in impairment losses and provisions for potential losses are as follows:

in thousands of HRK

	2018				2017		
	Stage 1	**Stage 2**	**Stage 3**	**Total**	**Impairment**	**Specific provisions for unidentified losses on a collective basis**	**Total**
At 1 January	**6,740**	**504**	**253,287**	**260,531**	**238,916**	**14,330**	**253,246**
Impact on profit or loss							
Net impairment losses i.e. provisions (Note 13)	(499)	343	2,851	**2,695**	23,809	(4,694)	19,115
Net impairment losses on interest receivable (Note 13)	6	(12)	(52)	**(59)**	70	-	70
Exchange differences	(37)	16	(674)	**(694)**	(157)	-	(157)
Without impact on P&L							
Write-off	-	-	(41,535)	**(41,535)**	(11,743)	-	**(11,743)**
At 31 December	**6,210**	**851**	**213,877**	**220,938**	**250,895**	**9,636**	**260,531**

Under the applicable legislation, the Bank has to form reserves for credit risk Stage 1 and 2 (2017: provisions for unidentified losses on collective basis). Taking into account the legal provisions, the amount of the reserves by the Bank's policies cannot be less than 0.8% of assets and contingencies and commitments as at 31 December 2018 (2017: 1% of non-risk assets and 1% of non-risk contingencies and commitments).

19. LOANS AND ADVANCES TO CUSTOMERS (CONTINUED)

19.2. Changes in impairment losses and provision for contingent losses (continued)

In respect of the changes in impairment losses (without the impact of write-offs) affecting the Income Statement, a breakdown of changes in impairment losses by different types of loans within the categories Retail and Corporate is given below:

		2018		in thousands of HRK
	Stage 1	**Stage 2**	**Stage 3**	**Total**
At 1 January	**6,740**	**504**	**253,287**	**260,531**
Retail				
At 1 January	**2,874**	**275**	**34,576**	**37,725**
Cash loans	(100)	(54)	1.564	1.410
Mortgage loans	13	-	41	54
Loans for agriculture	(52)	(5)	38	(19)
Loans for tourism	(1)	(4)	371	366
Lombard loans	(10)	(5)	-	(15)
Margin loans	(38)	1	-	(37)
Other loans	(33)	(9)	859	817
Overdrafts on transaction accounts	(16)	-	305	289
Housing loans	(20)	2	(2)	(20)
At 31 December	**2.617**	**201**	**37.753**	**40.570**
Corporate				
At 1 January	**3,866**	**229**	**218,711**	**222,806**
Investment loans	(54)	36	5,435	5,417
Loans for payments under guarantees	-	-	100	100
Working-capital loans	(120)	62	(7,688)	(7,746)
Loans for agriculture	(20)	(1)	227	206
Loans for tourism	(3)	-	126	123
Lombard loans	6	302	-	308
Other loans	(61)	9	1.024	972
Overdrafts on transaction accounts	6	13	(275)	(256)
Syndicated loan	(27)	-	-	(27)
At 31 December	**3,593**	**650**	**217,660**	**221,903**
Total Retail and Corporate	**6,210**	**851**	**255,413**	**262,473**
Write-off	-	-	**(41.535)**	**(41.535)**
At 31 December	**6,210**	**851**	**213,877**	**220,938**

19. LOANS AND ADVANCES TO CUSTOMERS (CONTINUED)

19.3. Changes in gross loans and impairment losses by credit risk stages

19.3.1. Changes in gross loans by credit risk stages

in thousands of HRK

	Stage 1	Stage 2	Stage 3	Total
At 1 January 2018	**889,823**	**64,752**	**451,922**	**1,406,497**
From Stage 1 to Stage 2	(8,490)	8,490	-	-
From Stage 1 to Stage 3	(8,177)	-	8,177	-
From Stage 2 to Stage 1	3.612	(3,612)	-	-
From Stage 2 to Stage 3	-	(9,813)	9,813	-
From Stage 3 to Stage 2	-	398	(398)	-
New assets	425,053	22,666	2,567	450,286
Derecognition of assets	(491,868)	35,517	(104,180)	(560,531)
At 31 December 2018	**809,953**	**118,398**	**367,901**	**1,296,252**

Note: The above amounts do not include interest receivable.

19.3.2. Changes in impairment losses by credit risk stages

in thousands of HRK

	Stage 1	Stage 2	Stage 3	TOTAL
Retail				
From Stage 1 to Stage 2	-	(6)	-	(6)
From Stage 1 to Stage 3	-	-	445	445
From Stage 2 to Stage 1	(18)	-	0	(18)
New assets	668	18	16	702
Derecognition	(496)	(28)	(703)	(1,227)
Change in provisions	(404)	(64)	3,411	2,943
Foreign exchange differences	(9)	(1)	(16)	(26)
Corporate				
From Stage 1 to Stage 2	-	-	-	-
From Stage 1 to Stage 3	-	-	142	142
From Stage 2 to Stage 1	(1)	-	-	-1
Issues and acquisitions	2,307	493	6,247	9,047
Derecognition	(2,202)	(77)	(12,917)	(15,196)
Change in provisions	(349)	(4)	6,159	5,806
Foreign exchange differences	(28)	17	(658)	(669)
Total (impact on P&L)	**(532)**	**348**	**2,126**	**1,942**

20. INVESTMENT PROPERTY

in thousands of HRK

	31 December 2018	31 December 2017
Investment property	34,446	33,630
Total	**34,446**	**33,630**

Investment properties are properties which are held by the Bank either to earn rentals or for capital appreciation. In 2018, the Bank increased the said asset values in accordance with the new assessment of their market value.

Investment property is initially measured at cost and the fair value is subsequently adjusted under the income method by an independent valuer. Revenue is determined on the basis of income earned on the market and is determined from the sum of the capitalised pure income and the determined value of land that is discounted on the day of valuation. The Bank conducts fair value measurement on an annual basis.
Investment property contains one property on the basis of which the Bank earns income from the lease. The contract with the lessee was concluded for an indefinite period and due to a very good business relationship of many years and the attractive location, the Bank does not expect to terminate the contract in the subsequent period of 5 years. Under the contract, the Bank has no obligation to invest in the premises, and incurred no costs in this respect.

Sensitivity to fluctuations in property prices by 1 percent is presented in the table below:

in thousands of HRK	31 December 2018		31 December 2017	
	Decrease	Increase	Decrease	Increase
Investment property	-344	344	-336	336

20.1. Rental income

The Bank has one real estate classified as an investment property and realised rental income from this real in the amount of HRK 4,031 thousand (2017: HRK 3,794 thousand).
Future expected operating lease income is given below:

31 December 2018

in thousands of HRK	Up to 1 year	1 to 2 years	2 to 5 years
Rental income/collection	4,560	4,560	4,560

31 December 2017

in thousands of HRK	Up to 1 year	1 to 2 years	2 and 5 years
Rental income/collection	4,196	4,196	4,196

20. INVESTMENT PROPERTY

20.2. Fair value hierarchy

in thousands of HRK

	Level 1	Level 2	Level 3	Total
At 31 December 2018				
Investment property	-	-	34,446	34,446
Total assets	**-**	**-**	**34,446**	**34,446**

	Level 1	Level 2	Level 3	Total
At 31 December 2017				
Investment property	-	-	33,630	33,630
Total assets	**-**	**-**	**33,630**	**33,630**

21. PROPERTY, EQUIPMENT AND INTANGIBLE ASSETS

in thousands of HRK

	Land and buildings	Furniture and vehicles	Equipment and other tangible assets	Tangible assets under construction	Total tangible assets	Intangible assets	Intangible assets in progress	Total intangible assets	Total
Cost									
At 1 January 2017	**24,708**	**7,732**	**21,605**	**14**	**54,059**	**29,863**	**240**	**30,103**	**84,162**
Additions	-	38	299	-	337	1,214	180	1,394	1,731
Transfer from account during the year	-	-	27	-	27	(27)	(240)	(267)	(240)
Reclassification under IFRS 5	5,280	-	-	-	(5,280)	-	-	-	(5,280)
Disposals and retirements	(7,025)	(2,918)	(3,010)	-	(12,953)	(296)	-	(296)	(13,249)
At 31 December 2017	**12,403**	**4,852**	**18,921**	**14**	**36,190**	30,754	**180**	30,934	67,124
Additions		37	168	177	382	1,271	-	1,271	1,653
Transfer from account during the year		-	-	-	-	180	(180)	-	-
Disposals and retirements		(743)	(659)	-	(1,402)	(93)	-	(93)	(1,495)
At 31 December 2018	12,403	4,146	18,430	**191**	35,170	32,112	-	32,112	67,282
Accumulated depreciation/amortisation									
At 1 January 2017	**14,551**	**7,093**	**18,988**	**-**	**40,632**	**25,177**	**-**	**25,177**	**65,809**
Charge for the year 2017	515	343	701	-	1,559	1,866	-	1,866	3,425
Disposals and retirements	(6,384)	(2,905)	(2,992)	-	(12,281)	(296)	-	(296)	(12,577)
At 31 December 2017	**8,682**	**4,531**	**16,697**	**-**	**29,910**	**26,747**	**-**	**26,747**	**56,657**
Charge for the year 2018	187	245	580	-	1,012	1,952	-	1,952	2,964
Disposals and retirements	-	(741)	(657)	-	(1,398)	(93)	-	(93)	(1,491)
At 31 December 2018	8,869	4,035	16,620	-	29,524	28,606	-	28,606	58,130
Net book amount at 31 December 2017	**3,721**	**321**	**2,224**	**14**	**6,280**	**4,007**	**180**	**4,187**	**10,467**
Net book amount at 31 December 2018	**3,534**	**111**	**1,810**	**191**	**5,646**	**3,506**	**-**	**3,506**	**9,152**

During the year, the Bank retired certain items of property and equipment with a total cost of HRK 1,439 (2017: HRK 6,183 thousand) and sold a portion in the amount of HRK 55 thousand (2017: HRK 40 thousand).

At 31 December 2018 and 31 December 2017, no assets of the Bank were pledged as collateral.

At 31 December 2018, the balance of assets still in use although fully written off amounts to HRK 24,894 thousand (2017: HRK 23,351 thousand).

22. FORECLOSED ASSETS

Movements in foreclosed assets for uncollected receivables are as follows:

in thousands of HRK

	31 December 2018	31 December 2017
At 1 January	**15,397**	**23,389**
Increase based on foreclosing assets	16,215	983
Decrease due to impairment (Note 13)	(184)	(6,347)
Decrease due to sale of foreclosed assets	(2,910)	(2,628)
Balance	**28,518**	**15,397**

In 2018, the Bank sold foreclosed assets in the amount of HRK 2,910 thousand (2017: HRK 2,628 thousand) and realised a gain in the amount of HRK 1,883 thousand (2017: HRK 4,073 thousand).

Sensitivity to fluctuations in property prices by 1 percent is presented in the table below:

in thousands of HRK

	31 December 2018		31 December 2017	
	Decrease	Increase	Decrease	Increase
Foreclosed assets	(285)	285	(154)	154

23. ASSETS HELD FOR SALE

in thousands of HRK

	31 December 2018	31 December 2017
Assets held for sale	5,280	5,280
Total	**5,280**	**5,280**

The Bank has reclassified tangible assets no longer used for business activities (business premises in Zadar and Poreč) to assets held for sale at their net book value, since the assets' fair value exceeds their net book value.

Sensitivity to fluctuations in property prices by 1 percent is presented in the table below:

in thousands of HRK

	31 December 2018		31 December 2017	
	Decrease	Increase	Decrease	Increase
Assets held for sale	(53)	53	(53)	53

24. OTHER ASSETS

	in thousands of HRK	
	31 December 2018	**31 December 2017**
Receivables from the state	17,759	17,759
Trade receivables	8,004	10,669
Other receivables	5,333	4,945
Other receivables from employees	4,551	4,537
Fees and commissions receivable	4,161	3,985
Receivables from domestic legal entities based on paid court costs	2,641	2,662
Cash in transit	1,899	1,908
Receivables for third-party deposits made at court	13	5,811
Provisions for expected credit losses (IFRS 9)	(20,202)	x
Provisions for unidentified losses on a collective basis (IAS 39)	x	(134)
Provisions for individually identified losses (IAS 39)	x	(19,580)
Total other assets	**24,159**	**32,562**

25. LIABILITIES TO BANKS

		in thousands of HRK
	31 December 2018	**31 December 2017**
Demand deposits		
- in HRK	3,286	16,545
- in foreign currencies	647	651
Total demand deposits	**3,933**	**17,196**
Term deposits		
- in HRK	105,238	43,694
- in foreign currencies	1,230	1,237
Total term deposits	**106,468**	**44,931**
Accrued interest	142	46
Total	**110,543**	**62,173**

26. DEMAND DEPOSITS

		in thousands of HRK
	31 December 2018	**31 December 2017**
Demand deposits - retail		
- in HRK	103,341	93,099
- in foreign currencies	101,857	83,318
Total retail	**205,198**	**176,417**
Demand deposits - corporate		
- in HRK	173,204	118,750
- in foreign currencies	14,458	11,280
Total corporate	**187,662**	**130,030**
Demand deposits - financial institutions		
- in HRK	563	1,187
- in foreign currencies	2	2
Total financial institutions	**565**	**1,189**
Demand deposits - government and other institutions		
- in HRK	60,863	59,006
- in foreign currencies	17,334	13,057
Total government and other institutions	**78,197**	**72,063**
Restricted deposits		
- in HRK	4,268	5,392
- in foreign currencies	14,904	15,103
Total restricted deposits	**19,172**	**20,495**
Deposits of foreign entities		
- in HRK	2,456	1,835
- in foreign currencies	15,351	9,853
Total foreign entities	**17,807**	**11,688**
Total	**508,601**	**411,882**

27. TERM DEPOSITS

in thousands of HRK

	31 December 2018	31 December 2017
Deposits - retail		
- in HRK	154,694	146,294
- in foreign currencies	1,065,740	1,274,023
Total retail	**1,220,434**	**1,420,317**
Deposits - corporate		
- in HRK	56,740	73,526
- in foreign currencies	482	2,080
Total corporate	**57,222**	**75,606**
Deposits - financial institutions		
- in HRK	17,000	16,000
- in foreign currencies	0	676
Total financial institutions	**17,000**	**16,676**
Deposits of government and other institutions - in HRK	**13,609**	**19,363**
Deposits of foreign entities		
- in HRK	1,647	2,540
- in foreign currencies	92,418	124,066
Total foreign entities	**94,065**	**126,606**
Deposits of non-profit organisations - in foreign currencies	**211**	**188**
Accrued interest	**15,569**	**23,472**
Total	**1,418,110**	**1,682,228**

28. BORROWINGS

in thousands of HRK

	31 December 2018	31 December 2017
Croatian National Bank	110,000	110,000
Domestic banks	3,974	50,596
Accrued interest	337	2,896
Total	**114,311**	**163,492**

29. OTHER LIABILITIES

in thousands of HRK

	31 December 2018	31 December 2017
Deferred income and accrued expenses	2,634	3,072
Amounts due to employees	2,859	2,511
Other liabilities	1,641	2,080
Liabilities for savings deposit insurance	1,110	1,350
Trade payables	1,361	1,146
Fees and commissions payable	204	259
Liabilities for payment of insured deposits of bankrupt banks /i/	245	245
Total	**10,054**	**10,663**

/i/ The State Agency for Bank Rehabilitation makes payments of insured deposits of bankrupt banks (Credo banka and Centar banka) through the Bank. In 2018, the stated amount totalled HRK 245 thousand (2017: HRK 245 thousand).

30. PROVISIONS

in thousands of HRK

	31 December 2018	31 December 2017
Provisions for legal disputes	12,614	7,065
Provisions for contingent liabilities and commitments	959	1,111
Provisions for unused vacation days	193	146
Provisions for termination benefits	123	
Other provisions	55	48
Total	**13,944**	**8,370**

Movements in provisions are presented in the table below:

in thousands of HRK

	2018	2017
At 1 January	**8,370**	**10,676**
Income from reversal of provisions for legal disputes against the bank (Note 13)	(1,003)	(318)
New provisions for legal disputes (Note 13)	7,328	1,625
Changes in provisions for commitments and contingencies (Note 13)	(152)	(423)
Cost of provisions for termination benefits, vacation days etc. (Note 13)	170	46
Changes in other provisions (Note 13)	7	10
Changes in payments made under legal disputes	(776)	(3,246)
At 31 December	**13,944**	**8,370**

In 2018, the Bank paid HRK 776 thousand from the provisions for legal disputes (2017: HRK 3,246 thousand). Provisions for off-balance-sheet exposure to credit risk and legal disputes are recognised as other losses from impairment and provisions in profit or loss (Note 13).

31. SHARE CAPITAL

The only shareholder of the Bank as at 31 December 2017 and 2016 is the State Agency for Deposit Insurance and Bank Rehabilitation.

		in thousands of HRK
	31 December 2018	**31 December 2017**
Share capital	474,600	474,600
Accumulated loss	(318,393)	(290,536)
Reserves	(1,121)	(1,425)
Loss for the year	(24,989)	(30,631)
Total equity	**130,097**	**152,008**

Share capital in the amount of HRK 474,600 thousand (2017: HRK 474,600 thousand) consists of 4,746,000 shares with a nominal value of HRK 100 per share (2017: 4,746,000 shares with a nominal value of HRK 100 per share). Each share carries one vote.

32. LOSS PER SHARE

		in thousands of HRK
	2018	**2017**
Loss for the year	(24,989)	(30,631)
Number of shares	4,746	4,746
Loss per share	**(5.27)**	**(6.45)**

33. CONTINGENT LIABILITIES AND COMMITMENTS

	31 December 2018	31 December 2017
Guarantees	63,519	43,067
Other common risk-bearing off-balance sheet items	20,642	30,213
Revolving loans	29,391	29,978
Unbacked letters of credit	3,780	7,821
Total	**117,332**	**111,079**

34. LEGAL DISPUTES

More than 200 legal disputes have been initiated against the Bank by former shareholders of the Bank, as well as forty legal disputes on other grounds.

In accordance with internal bylaws and legal regulations, the Bank assesses the potential outflow of cash regarding disputes carrying a risk of loss and forms appropriate provisions.

As at 31 December 2018, the provisions for losses from legal disputes filed against the Bank amounted to HRK 12,614 thousand (2017: HRK 7,065 thousand).

As to the disputes filed by former shareholders, up to 31 December 2018, 220 disputes have been finalised, and only three disputes are formally active although they have been interrupted for several years (from 2008 to 2012) and are not expected to continue.

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

35. CASH AND CASH EQUIVALENTS

Cash and cash equivalents for the purposes of preparing a cash flow statement are presented in the table below:

in thousands of HRK

	31 December 2018	31 December 2017
Cash on hand and on current accounts with banks (Note 15)	208,297	178,095
Balances with other banks with maturities up to 3 months (Note 17)	19,376	23,325
Total	**227,673**	**201,420**

36. RELATED PARTY TRANSACTIONS

The Bank is fully (100%) owned by the State Agency for Deposit Insurance and Bank Rehabilitation (DAB). The Bank considers to be directly related to its shareholder, Supervisory Board and Management Board members and other executives (jointly referred to as "the key management personnel"), their close family members, companies under common control or under significant influence of Management Board members and their close family members, in accordance with the definition of related parties provided in International Accounting Standard 24 "Related Party Disclosures" (IAS 24). Key management includes members of the Management Board, Department directors, directors of branches and directors of control functions. As at 31 December 2018, the key management personnel of the Bank consisted of 23 employees (2017: 24 employees).

The balances of assets and liabilities as well as income and expenses as at 31 December 2018 and 31 December 2017 and for the years then ended resulting from key transactions with related parties are as follows:

in thousands of HRK

2018	Receivables	Liabilities	Income	Expenses
DAB (sole shareholder)	156	22,042	5	5,417
Key management personnel				
Short-term (a vista deposits, bonuses, salaries, benefits)	4	637	6	6,146
Pension insurance contributions	-	-	-	1,129
Long-term (loans, term deposits and other)	4,379	2,412	134	10
State in narrow and broad definition	1,139,691	124,051	12,046	2,975
Total	**1,144,230**	**149,142**	**12,191**	**15,677**

in thousands of HRK

2017	Receivables	Liabilities	Income	Expenses
DAB (sole shareholder)	2,216	18,565	14	5,581
Key management personnel				
Short-term (a vista deposits, bonuses, salaries, benefits)	4	486	28	6,978
Pension insurance contributions	-	-	-	1,524
Long-term (loans, term deposits and other)	7,003	2,591	290	51
State in narrow and broad definition	1,357,850	110,504	56,214	6,981
Total	**1,376,073**	**132,146**	**56,546**	**21,115**

36. RELATED PARTY TRANSACTIONS (CONTINUED)

Key management personnel

Key management personnel does not hold any of the Bank's shares. Loans and receivables from customers include HRK 4,379 thousand (2017: HRK 7,003 thousand) of loans to key management personnel. During the year, the Bank collected interest in the amount of HRK 134 thousand (2017: 290 HRK thousand) from loans and receivables from key management personnel granted at annual interest rates ranging from 3.00% to 5.00% (2017: from 3.57% to 5.00%). The balance of current accounts and customer deposits includes term deposits of key management personnel in the amount of HRK 2,387 thousand (2017: HRK 2,545 thousand). The interest that the Bank paid on those deposits in 2018 amounted to HRK 10 thousand (2017: 51 HRK thousand) at an annual interest rate ranging from 0.20% - 2.75% (2017: 0.10% - 2.75%).

In 2018, costs in respect of the Supervisory Board amounted to HRK 554 thousand (2017: HRK 350 thousand).

In 2018, costs of the Management Board of the Bank amounted to HRK 1,237 thousand (2017: HRK 1,822 thousand).

State in narrow and broad definition

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

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

Most significant receivables from the state in narrow and broad definition are as follows:

As at 31 December 2018, the exposure to the state in narrow and broad definitions comprises the exposure to the state-owned company Hrvatske autoceste d.o.o. in the amount of HRK 297,362 thousand (2017: HRK 291,359 thousand) in respect of a syndicated loan.

The Bank's exposure to HŽ Cargo amounted to HRK 75,121 thousand (2017: HRK 84,723 thousand), the receivable from Borovo d.d. amounted to HRK 45,988 thousand (2017: HRK 16,999 thousand), and the receivables from Đuro Đaković Holding amounted to HRK 21,131 thousand (2017: HRK 32,510 thousand).

The Bank's exposures to the Ministry of Finance comprise those on the Ministry's quoted bonds in the amount of HRK 436,316 thousand (2017: HRK 669,074 thousand), and treasury bills issued by the Ministry of Finance in the amount of HRK 220,915 thousand (2017: HRK 200,137 thousand).

Most significant liabilities to the state in narrow and broad definition are as follows:

The restricted deposit of the Ministry of Finance amounted HRK 14,906 thousand (2017: HRK 15,027 thousand).

As at 31 December 2018, the Restructuring and Sale Centre holds HRK 22,191 thousand on the transaction account at the Bank (2017: HRK 22,157 thousand).

As at 31 December 2018, the Bank’s shareholder, the State Agency for Deposit Insurance and Bank Rehabilitation, holds HRK 22,042 thousand on the transaction account (2017: HRK 17,215 thousand).

As at 31 December 2018, the amount owed by the Bank for loans received from the Croatian Bank for Reconstruction and Development (joint customer funding with CBRD) was HRK 3,976 thousand (31 December 2017: HRK 10,647 HRK thousand).

All the above-mentioned significant transactions with the state and state-owned companies were entered into at arm’s length.

36. RELATED PARTY TRANSACTIONS (CONTINUED)

Most significant income and expenses from the state in narrow and broad definition are as follows:

Income recognised in the profit or loss for 2018 treated as key transactions is as follows:

- income from loans to Hrvatske autoceste in the amount of HRK 13,238 thousand (2017: HRK 18,675 thousand).
- income from loans to HŽ Cargo in the amount of HRK 3,604 thousand (2017: HRK 4,044 thousand).
- income from bonds issued by the Ministry of Finance in the amount of HRK 5,553 thousand (2017: HRK 22,108 thousand).
- income from treasury bills issued by the Ministry of Finance in the amount of HRK 130 thousand (2017: HRK 840 thousand).

Expenses recognised in the profit or loss for 2018 treated as key transactions are as follows:

- costs of loans received from CBRD in the amount of HRK 200 thousand (2017: HRK 2,502 thousand).
- expenses in respect of DAB relating to expenses for the savings deposit insurance in the amount of HRK 5,266 thousand and transaction account costs in the amount of HRK 150 thousand (2017: HRK 5,576 thousand; HRK 5 thousand).

Off-balance sheet contingent liabilities to key management personnel and the state in narrow and broad definition:

in thousands of HRK

31 December 2018	Key management personnel	State in narrow and broad definition
Guarantees	-	-
Credit lines and other off-balance-sheet items	339	2,821

31 December 2017		
Guarantees	-	5,417
Credit lines and other off-balance-sheet items	375	1,692

The Bank's maximum off-balance sheet exposure to the state in narrow and broader definitions relates to Narodne novine d.d. in the amount of HRK 993 HRK thousand (2017: Đuro Đaković in the amount of HRK 5,925 thousand). All exposures presented in this note are on a net basis (i.e. less identified and unidentified impairment losses).

37. RISK MANAGEMENT POLICIES

Details on the Bank's exposure to risks and methods Management applies for risk control are described below. The most significant types of financial risks the Bank is exposed to are credit risk, liquidity risk and market risk. Market risk includes currency risk, interest rate risk and price risk.

37.1. Credit risk

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

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

Credit risk is the greatest individual risk arising from the Bank's operations; therefore, all organisational units and functions of the Bank monitor the risk closely. Credit risk management and control are centralised in the Risk Management Service which regularly reports to the Management Board, other bodies of the Bank, the Supervisory Board and senior management.

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

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

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

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

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

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.1. Credit risk (continued)

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

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

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

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

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

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

37.1.1. Credit risk management

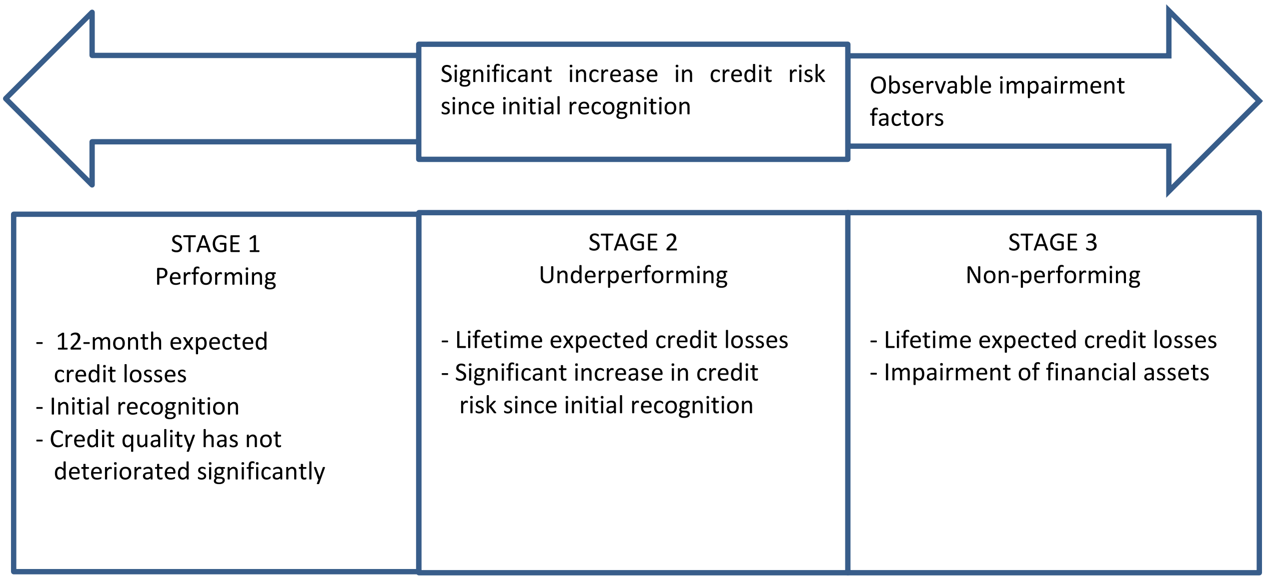
The expected credit losses are calculated as a sum of PD (Probability of Default), Loss Given Default (LGD) and Exposure at Default (EAD) over the remaining expected life of the financial asset and are discounted at the reporting date at the effective interest rate for exposures with a significant increase in credit risk (Stage 2 Contracts). On the other hand, for exposures classified as Stage 1, the expected credit loss is calculated over a one-year period, i.e. the expected credit loss of 1 year is estimated.

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.1. Credit risk (continued)

37.1. Credit risk management (continued)

Increase in credit risk since initial recognition



When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, the Bank considers quantitative and qualitative information and expert credit assessments based on historical experience. For the purpose of proper allocation of income-based exposures, criteria for determining a significant increase in credit risk (transition from Stage 1 to Stage 2) were defined:

- If the debtor defaults on payment of due exposures for more than 30 days, but does not exceed a period of 90 days. This provision does not apply to exposures to the central government and other exposures for which the Bank can prove that a 30-day default is not a relevant indicator;
- The debtor has watch-list or exit status/monitoring and days of delay do not exceed 90 days;
- The debtor meets the blockage criterion (in line with internal segmentation, for natural persons if continuous blockage exceeds 10 days, and for others if continuous blockage exceeds 15 days) and the number of days of default does not exceed 90 days.

In addition to assessing the risk of default, the Bank also defines the default status. It is considered that the status of default of a particular debtor (Stage 3) has occurred when one of the following conditions or both of the following conditions have been met:

a) The Bank considers it likely that the debtor will not fully meet its obligations, not taking into account the possibility of recovery from the collateral;

b) if the debtor is more than 90 days past due.

Exceptionally, for the exposures from the retail exposures category the Bank assesses the default status based on an individual product and if it has a balance sheet exposure towards a debtor with the default status and the gross carrying amount of exposure with the default status accounts for more than 20% of gross carrying amount of all balance sheet exposures to that debtor, all on-balance sheet and off-balance sheet exposures by all products of that debtor are considered to be in default.
When defining the default status, the Bank uses objective evidence of partial or complete irrecoverability of placements.
The following is considered as objective evidence of partial recoverability of placements:

- observable significant financial difficulties of the debtor;

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.1. Credit risk (continued)

37.1. Credit risk management (continued)

- if the debtor is in default for more than 90 days or in the event of a frequent delinquency in interest and/or principal payments or failure to perform other contractual provisions;
- if the Bank makes a payment on the given guarantees and the debtor does not settle the obligation within 90 days;
- if cash flows from operations and secondary sources (insurance instruments) are not sufficient to settle the contractual obligations, taking into account the timeliness of settlement (days of default);
- if the debtor requires exposure restructuring, write-offs of liabilities and other actions that result in the decrease of the client's original liabilities.

The following is considered to be objective evidence of total irrecoverability/loss:
- bankruptcy, liquidation or termination of business for other reasons, while at the same time the Bank has no recognised and separate satisfaction and/or exclusion rights over the assets of the debtor or other collaterals and it is estimated that the Bank cannot expect to collect a portion of its receivables due to the debtor's insufficient funds and/or the recovery priority order in bankruptcy proceedings;
- if the debtor is in continuous default for more than 365 days, and the Bank does not have adequate collaterals;
- if the placement is the subject of a legal dispute for which it is presumed that the Bank could lose it in its entirety.

In order to determine the increased credit risk in addition to the quantitative indicators, the Bank conducts a placements monitoring process and a system of early increased credit risk detection for the purpose of timely identification of clients with increased risk exposure and for the purpose of establishing adequate placement / client monitoring at an already established increased degree of risk, all in order to avoid and/or reduce potential losses on placements.
The following monitoring statuses (risk zones) were established for the placement/client portfolio:
- STANDARD - standard exposure - monitored every 12 months, with the exception of the Financial Markets Sector for which exposure is monitored every 3 months
- WATCH - potentially problematic exposure - monitored within a year, every 3 to 9 months,
- EXIT - problematic exposure where the Bank exits from a business relationship with a client - exposure is monitored every 3 months,
- NO MONITORING NECESSARY

Expected credit loss measurement

The key inputs for measuring the expected credit loss are the following variables:
- PD - probability of default
- LGD - loss given default
- EAD - exposure at default

Expected credit losses for the exposures (ECL) in Stage 1 are calculated by multiplying the 12-month PD with LGD and EAD.
Lifetime expected credit losses are calculated by multiplying the lifetime PD with LGD and EAD and discounting it at the reporting date.

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.1. Credit risk (continued)

37.1.1. Credit risk management (continued)

Probability of default (PD) i.e. the probability of a transition from a performing to the non-performing status.

The basis for estimating lifetime PD is the empirical default rate. The empirical default rates and consequently the estimated lifetime PDs are calculated at the segment level:

- Corporate
- SME
- Retail
- Public
- Financials
- Retail Overdraft

Loss given default (LGD), loss expressed in percentage given default). The Bank decided to apply the 45% LGD on all exposures until it develops an internal collection model.

Exposure at default (EAD) is the value a bank is exposed to when a loan defaults. The Bank calculates the exposure at default:

- For products with cash flows (mortgages, long-term loans, investment loans, bonds...) EAD is calculated based on cash flows received from repayment plans.

For other products with no cash flow the CFF factor 1 applies.

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.2. Credit risk measurement

Loans and receivables (including contingent liabilities)

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

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

1.1. fully recoverable loans (risk group A) – loans assessed as fully recoverable (both principal and interest) and contingent liabilities expected not to result in an outflow of the Bank's resources, or if such an outflow is required, that they will be recovered in full. The Bank must allocate the exposures in risk group A to the following risk subgroups:

- A-1 if after initial recognition the credit risk of a certain exposure of the debtor has not increased significantly,
- A-2 if after initial recognition the credit risk of a certain exposure of the debtor has increased significantly.

1.2. partly recoverable loans (risk group B) – loans assessed as not recoverable at contractual amounts (principal and interest) or contingent liabilities expected to result in an outflow of the Bank's resources in excess of the estimated recoverable amount.

1.3. irrecoverable loans (risk group C) – loans estimated as fully irrecoverable or insignificantly recoverable and contingent liabilities expected to result in an outflow of the Bank's resources that will never be recovered.

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.2. Credit risk measurement (continued)

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

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

In accordance with the provisions of IFRS 9 for performing loans the Bank appropriately impairs and provides for exposures equalling the following:

- 12-month expected credit losses for risk subgroup A-1,
- lifetime expected credit losses for risk subgroup A-2.

The CNB requires the banks to recognise impairment losses in profit or loss at the prescribed minimum rate of 0.8%, for performing exposures.

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

a) on an individual basis

- for loans classified in the "large loans portfolio"

b) on a collective basis

- for loans classified in the "small loans portfolio" and current accounts

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

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

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

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

- in assessing expected credit losses for loans included in the small loans portfolio and current accounts.

Finally, it should be noted that in the first half of 2017 the Bank Introduced a new internal rating model. During 2018, the model continued to improve and it is expected to enhance credit risk assessment and estimation, for the purpose of accurate and timely credit risk management in the Bank.

The credit risk exposure is also managed by a regular analysis of the ability of the existing clients and potential clients to settle their liabilities of repaying interest and principal and by changing credit limitations where necessary. Further specific measures for credit risk control and mitigation are stated below.

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.3. Risk limit control and mitigation policies

(a) Security instruments

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

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

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

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

In addition, in order to reduce credit loss, the Bank requires additional collaterals from the contractual parties as soon as indicators of impairment for individual relevant loans and advances are determined. The collateral held as security for all financial assets other than loans and advances is determined on the basis of the nature of the instrument. Debt securities, treasury and other eligible bills are generally unsecured, with the exception of asset-backed securities and similar instruments, which are secured by portfolios of financial instruments.

(b) Commitments to extend credit

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

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

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.4. Impairment and provisioning policies

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

Security instruments for which the nominal value is discounted are as follows:

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

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

Based on the timely repayment criteria, loans in the large loans portfolio are classified into the following risk groups:
1) risk group "A" includes loans that meet the following criteria:

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

The Bank must allocate the exposures in risk group A to the following risk subgroups:

- A-1 if after initial recognition the credit risk of a certain exposure of the debtor has not increased significantly,
- A-2 if after initial recognition the credit risk of a certain exposure of the debtor has increased significantly.

The Bank has prescribed the following indicators for determining increased credit risk of the debtor and classifying it in risk subgroup A-2:

- If the debtor defaults on payment of due exposures for more than 30 days, but does not exceed a period of 90 days. This provision does not apply to exposures to the central government and other exposures for which the Bank can prove that a 30-day default is not a relevant indicator;
- The debtor has watch-list or exit status/monitoring and days of delay do not exceed 90 days;
- The debtor meets the blockage criterion (in line with internal segmentation, for natural persons if continuous blockage exceeds 10 days, and for others if continuous blockage exceeds 15 days) and the number of days of delay does not exceed 90 days.

2) risk group B1 - loans for which expected credit losses do not exceed 30% of the nominal carrying amount of individual loans.
3) risk group B2 - loans for which expected credit losses are over 30% and less than 70% of the nominal carrying amount of individual loans.
4) risk group B3 - loans for which expected credit losses are over 70% and less than 100% of the nominal carrying amount of individual loans.

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

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.4. Impairment and provisioning policies (continued)

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

Based on the timely repayment criteria, loans in the small loans portfolio and current accounts are classified into the following risk groups:

1) Risk group "A" includes fully recoverable loans. For a loan to remain classified in the risk group "A" (whereby the criteria for risk groups A1 and A2 are the same as for large loans), the following conditions must be met:

   - the debtor's past due liabilities to the Bank are not older than 90 days

   - the full loan amount is covered by a guarantee deposit.

2) Risk group "B" or "C" loans must be provided for on the basis of the number of days in default.

3) Risk group "C" includes loans that do not meet the conditions for classification in risk groups "A" and "B", i.e. 100% irrecoverable loans, as follows:

   - loans with default in payments more than 365 days;

   - loans classified in the 100% provision position according to specially determined tables.

37.5. Debt securities

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

37.6. Past due loans and not past due loans and receivables

Past due and not past due loans and receivables by type at 31 December 2018

in thousands of HRK

Past due	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Up to 30 days	111	2,899	2,106	4,177	8	643	9,944
31-60 days	56	2,364	268	20	2	1,286	3,996
61-90 days	222	-	-	-	-	49	271
Over 90 days	5,337	162,327	17,197	2,713	1,818	64,109	253,501
Not past due	158,723	232,046	48,618	20,627	51,881	522,661	1,034,556
Total	**164,449**	**399,636**	**68,189**	**27,537**	**53,709**	**588,748**	**1,302,268**

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.6. Past due loans and receivables (continued)

Past due loans and receivables by type at 31 December 2017

in thousands of HRK

Past due	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Up to 30 days	82	6,266	2,013	8,259	9	675	17,304
31-60 days	45	1,059	189	77	2	698	2,070
61-90 days	317	4	-	-	1	6	328
Over 90 days	4,429	217,977	17,732	2,720	1,326	83,006	327,190
Not past due	167,139	227,302	57,677	42,122	55,832	516,588	1,066,660
Total	**172,012**	**452,608**	**77,611**	**53,178**	**57,170**	**600,973**	**1,413,552**

37.7 Unimpaired loans at 31 December 2018

in thousands of HRK

	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Not past due	153,546	168,762	39,485	20,441	51,282	490,462	923,978
Past due	98	3,124	2,075	2,926	7	948	9,178
Total	**153,644**	**171,886**	**41,560**	**23,367**	**51,289**	**491,410**	**933,156**

Unimpaired loans at 31 December 2017

in thousands of HRK

	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Not past due	163,396	196,751	49,970	18,806	55,049	467,304	951,276
Past due	66	5,179	2,049	3,631	8	147	11,080
Total	**163,462**	**201,930**	**52,019**	**22,437**	**55,057**	**467,451**	**962,356**

Unimpaired loans and receivables refer to placements classified in risk groups A1 and A2. The placements in risk groups A1 and A2 are loans and receivables regularly repaid by clients and not impaired by the Bank.

The line item 'Other' comprises the participation in syndicated loans which in 2018 amounted to HRK 373,419 thousand (2017: HRK 378,891 thousand), as well as lombard loans in the amount of HRK 58,903 thousand (2017: HRK 15,516 thousand), margin loans in the amount of HRK 25,809 thousand (2017: HRK 20,979 thousand) and mortgage loans in the amount of HRK 7,014 thousand (2017: HRK 5,165 thousand). The remaining balance consist of individual smaller loans intended for diverse purposes.

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.7. Impaired loans (continued)

Impaired loans at 31 December 2018

in thousands of HRK

	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Not past due	5,177	63,284	9,133	186	599	32,199	110,578
Past due	5,628	164,466	17,496	3,984	1,821	65,139	258,534
Total	**10,805**	**227,750**	**26,629**	**4,170**	**2,420**	**97,338**	**369,112**
Impairment	**6,710**	**129,469**	**13,170**	**3,576**	**1,093**	**59,859**	**213,877**

Impaired loans at 31 December 2017

in thousands of HRK

	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Not past due	3,743	30,551	7,707	23,316	783	49,284	115,384
Past due	4,807	220,127	17,885	7,425	1,330	84,238	335,812
Total	**8,550**	**250,678**	**25,592**	**30,741**	**2,113**	**133,522**	**451,196**
Impairment	**5,384**	**154,890**	**12,713**	**3,551**	**1,093**	**73,264**	**250,895**

The item 'Other' mainly comprises loans to customers undergoing pre-bankruptcy in the amount of HRK 26,345 thousand (2017: HRK 42,399 thousand) and financial restructuring in the amount of HRK 49,671 thousand (2017: HRK 44,223 thousand), as well as construction loans in the amount of HRK 118 thousand (2017: HRK 11,110 thousand) and loans for payments under guarantees and other sureties in the amount of HRK 2,847 thousand (2017: HRK 3,176 thousand). The remaining balance consist of individual smaller loans intended for diverse purposes.

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.8. Structure of loans and off-balance contingent liabilities by type of activity

Structure of loans and off-balance sheet contingent liabilities by type of activity at 31 December 2018 in thousands of HRK

Activity sector	Total loans and off-balance sheet liabilities	Unimpaired loans and off-balance sheet liabilities	Impaired loans and off-balance sheet liabilities	Impairment and provisions	% of impairment and provisions
Agriculture, hunting, forestry and fishing	103,029	75,615	27,414	19,524	**18.95**
Manufacturing	231,260	146,809	84,450	43,478	**18.80**
Construction	398,570	311,267	87,303	67,333	**16.89**
Wholesale and retail trade, repair of motor vehicles and household items	113,354	44,868	68,486	45,006	**39.70**
Service activities	205,890	144,416	61,474	24,389	**11.85**
Financial intermediation	13,174	13,174	0	137	**1.04**
Foreign financial institutions	-	-	-	-	-
CNB	-	-	-	-	-
Other activities	51,044	28,822	22,222	4,896	9.59
Activity sectors outside the Croatian National Classification	303,279	282,228	21,052	17,134	5.65
TOTAL	**1,419,600**	**1,047,199**	**372,401**	**221,897**	**15.63**

Structure of loans and off-balance sheet contingent liabilities by type of activity at 31 December 2017 in thousands of HRK

Activity sector	Total loans and off-balance sheet liabilities	Unimpaired loans and off-balance sheet liabilities	Impaired loans and off-balance sheet liabilities	Impairment and provisions	% of impairment and provisions
Agriculture, hunting, forestry and fishing	120,824	89,650	31,173	20,196	**16.72**
Manufacturing	246,059	106,199	139,859	66,088	**26.86**
Construction	413,718	311,254	102,464	78,430	**18.96**
Wholesale and retail trade, repair of motor vehicles and household items	134,740	60,454	74,286	50,501	**37.48**
Service activities	218,814	145,025	73,790	26,515	**12.12**
Financial intermediation	17,234	17,234	0	174	**1.01**
Foreign financial institutions	0	0	0	0	**0.00**
CNB	0	0	0	0	**0.00**
Other activities	54,321	37,027	17,294	2,413	**4.44**
Activity sectors outside the Croatian National Classification	318,921	297,867	18,055	17,325	**5,43**
TOTAL	**1,524,631**	**1,067,710**	**456,921**	**261,642**	**17.16**

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.9. Loans and advances to B and C risk group customers for which provisions have been made

in thousands of HRK

	Retail customers	Corporate customers	Total
31 December 2018			
Total exposure	60,894	308,218	**369,112**
Provisions	37,753	176,124	**213,877**
Total net exposure	23,141	132,094	**155,235**
Market value of collateral	36,733	150,988	**187,721**
% of collateral coverage	158.74%	114.30%	**120.93%**

	Retail customers	Corporate customers	Total
31 December 2017			
Total exposure	62,395	388,801	**451,196**
Provisions	37,974	210,685	**248,659**
Total net exposure	24,421	178,116	**202,537**
Market value of collateral	40,121	204,208	**244,329**
% of collateral coverage	164.29%	114.65%	**120.63%**

37.10. Credit risk sensitivity analysis

As part of the macroeconomic factors sensitivity analysis regarding credit risk provisions, the Bank analyzes the effects of macroeconomic indicators and parameters on future operations by increasing the B and C placements, the "bad" migration of NPLs etc.
The Bank uses the stress test scenario of the Croatian National Bank as published in Financial Stability from July 2015 as the basis for creating a stress test scenario. In this document, the CNB develops two stress scenarios (baseline and adverse), and the Bank uses a combination of both.

On this basis, the Bank uses the following parameters and indicators in stress testing:
- Increase in B and C placements in total placements by 20%,
- Arranging new defaults in a way that in B1 risk group comprises 60% of placements, and the remaining 40% of newly-defaulted placements is included in B2,
- Transfer from risk group B1 to B2, from B2 to B3 and from B3 to C at 10% exposure,
- VICR stress tests are subtracted from the projected new value adjustments.

The result of the applied test according to the latest testing would be a decline in regulatory capital of the Bank by 22%.

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.11. Credit quality of financial assets

The credit quality of financial assets as rated by external agencies is given below:

in thousands of HRK

	Rating agency	31 December 2018	31 December 2017
Cash		**206,351**	**176,668**
Ba2	Moody's	199,879	155,384
A1	Moody's	1,268	-
A2	Moody's	-	1,117
A3	Moody's	97	49
Baa1	Moody's	320	171
Aa3	Moody's	724	2,709
BBB-	Fitch	448	2,683
No rating	-	3,615	14,555
Receivables from the Croatian National Bank		**142,387**	**149,557**
Ba2	Moody's	142,387	149,557
Placements to banks		**19,249**	**23,092**
Aaa	Moody's	18,831	22,668
No rating	-	418	424
Financial assets carried at fair value through OCI		**752,681**	**x**
Ba2	Moody's	657,760	x
Aaa	Moody's	53,835	x
Aa2	Moody's	40,648	x
No rating	-	438	x
Financial assets carried at fair value through profit loss		**492**	**x**
No rating	-	492	x
Financial assets at amortised cost		**496**	**x**
No rating	-	496	x
Financial assets available for sale		**x**	**887,053**
Ba2	Moody's	x	886,615
No rating	-	x	438
Loans and advances to customers		**1,081,330**	**1,153,021**
No rating	-	1,081,330	1,153,021
Other financial assets	-	**15,444**	**23,601**
No rating		15,444	23,601

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.12. Concentration risk

The Bank manages, limits and controls concentrations of credit risk in accordance with the Credit Policy wherever such risk is identified – in particular, with respect to individual clients and groups, industries and countries. Concentration is determined at the level of exposure of a particular debtor (at the level of a group of related persons) in relation to regulatory capital (over 10% of the recognised capital) and also by exposure of a particular activity to the total exposure of the Bank.

The Bank establishes credit risk levels it undertakes by placing limitations on the amount of risk accepted in relation to one client, or a group of clients, and to geographical and industry segments. Limitations on the credit risk level to products, industry sectors and countries are approved by the Bank's Management.

The exposure to any borrower is further limited by sub-limits covering both balance sheet and off-balance sheet exposures, as well as daily limits (the liability settlement risk) in relation to the items traded. The actual exposure in relation to limitations is monitored on a daily basis.

37.13. Liquidity risk

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

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

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.13. Liquidity risk (continued)

The allowed excess of liquidity indicators and the strategy defining the reasons for allowing the excess are documented by the minutes of the ALCO meeting.

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

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

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

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

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

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

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

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.13. Liquidity risk (continued)

Future outflows under financial liabilities that as at 31 December 2018 include undiscounted cash flows including future interest payments in the amount of HRK 10,787 thousand on received deposits and borrowings, classified by remaining maturities. Asset items are classified by maturities of the carrying amounts.

in thousands of HRK

2018	Up to 1 month	1 to 3 months	3 to 12 months	1 to 3 years	Over 3 years	Total
ASSETS						
Cash	206,351	-	-	-	-	**206,351**
Receivables from the Croatian National Bank	142,387	-	-	-	-	**142,387**
Placements with banks	18,834	-	415	-	-	**19,249**
Financial assets at fair value through other comprehensive income	4,982	206,327	225,638	29,613	286,121	**752,681**
Financial assets at fair value through profit or loss	-	-	-	-	492	**492**
Financial assets at amortised cost	496	-	-	-	-	**496**
Loans and advances to customers	104,983	38,602	152,060	240,115	545,570	**1,081,330**
Other financial assets	14,868	-	295	246	35	**15,444**
Total assets	**492,901**	**244,929**	**378,408**	**269,974**	**832,218**	**2,227,430**
EQUITY AND LIABILITIES						
Liabilities to banks	98,671	11,893	-	-	-	**110,564**
Demand deposits	508,600	-	-	-	-	**508,600**
Term deposits	82,520	105,883	967,043	258,564	14,552	**1,428,562.00**
Borrowings	374	276	691	1,678	111,607	**114,626**
Other financial liabilities	7,420	-	-	-	-	**10,054**
Total equity and liabilities	**697,585**	**118,052**	**967,734**	**260,242**	**126,159**	**2,172,406**

Off-balance sheet items	Up to 1 month	1 to 3 months	3 to 12 months	1 to 3 years	Over 3 years	Total
Guarantees	3,292	12,887	25,663	15,376	5,843	63,061
Unbacked letters of credit	3,754	-	-	-	-	3,754
Revolving loans and credit lines	28,673	-	26	1	484	29,184
Other common risk-bearing off-balance sheet items	-	751	12,926	4,121	2,576	20,374
TOTAL OFF-BALANCE SHEET ITEMS	**35,719**	**13,638**	**38,615**	**19,498**	**8,903**	**116,373**
Net assets/liabilities and equity	**(240,403)**	**113,239**	**(627,941)**	**(9,776)**	**697,156**	**(67,715)**

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.13. Liquidity risk (continued)

Future outflows under financial liabilities that as at 31 December 2017 reflect undiscounted cash flows including future interest payments in the amount of HRK 25,137 thousand on received deposits and borrowings, classified by remaining maturities. Asset items are classified by maturities of the carrying amounts.

in thousands of HRK

2017	Up to 1 month	1 to 3 months	3 to 12 months	1 to 3 years	Over 3 years	Total
ASSETS						
Cash	176,668	-	-	-	-	**176,668**
Receivables from the Croatian National Bank	149,557	-	-	-	-	**149,557**
Placements with banks	22,672	-	420	-	-	**23,092**
Available-for-sale financial assets	65,381	589	150,397	347,876	322,810	**887,053**
Held-to-maturity financial assets	-	-	-	-	-	**-**
Loans and advances to customers	182,395	33,131	218,358	331,101	388,036	**1,153,021**
Other financial assets	23,601	-	-	-	-	**23,601**
Total assets	**620,274**	**33,720**	**369,175**	**678,977**	**710,846**	**2,412.992**
EQUITY AND LIABILITIES						
Liabilities to banks	17,241	10,116	35,040	-	-	**62,397**
Demand deposits	411,882	-	-	-	-	**411,882**
Term deposits	98,573	147,325	705,806	738,176	16,478	**1,706,358.00**
Borrowings	43,674	764	2,182	93,982	23,673	**164,275**
Other financial liabilities	7,591	-	-	-	-	**7,591**
Total equity and liabilities	**578,961**	**158,205**	**743,028**	**832,158**	**40,151**	**2,352,503**

Off-balance sheet items	Up to 1 month	1 to 3 months	3 to 12 months	1 to 3 years	Over 3 years	Total
Guarantees	1,986	6,607	19,050	14,301	693	**42,637**
Unbacked letters of credit	2,103	3,973	1,666	-	-	**7,742**
Revolving loans and credit lines	29,488	-	-	1	188	**29,677**
Other common risk-bearing off-balance sheet items	542	-	4,812	22,945	1,613	**29,912**
Total OFF-BALANCE SHEET ITEMS	**34,119**	**10,580**	**25,528**	**37,247**	**2,494**	**109,968**

Net assets/liabilities and equity	**7,194**	**(135,065)**	**(399,381)**	**(190,428)**	**668,201**	**(49,479)**

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.14. Market risk

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

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

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

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

Market risks are as follows:

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

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

Interest rate risk is described in more detail in chapter 38.3.2. of the Report.

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

Currency risk is described in more detail in the following chapter of the Report (item 38.3.1.).

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

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.14. Market risks (continued)

37.14.1. Currency risk

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

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

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

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

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

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

The potential maximum daily loss of the open foreign currency position (VaR: 95% reliability) as of 31 December 2018 amounted to HRK 7.9 thousand (2017: HRK 22 thousand).

The sensitivity of currency risk measurement is carried out using monthly stress tests. Stress test is based on the simulation of the exchange rate fluctuation with respect to the openness of the position of the most significant currencies

(EUR, USD, CHF, AUD). Data used are based on the historical movements of the Kuna exchange rate according to the 4 most significant currencies mentioned above in the last 2 years.

When performing the testing, 3 levels of intensity are carried out: the geometric mean of the exchange rate fluctuations that exclude extreme fluctuations; 95 percentile or maximum possible exchange rate fluctuation with 95% probability of fluctuation; 99 percentile or maximum possible exchange rate fluctuation with 99% probability of fluctuation.

in thousands of HRK

CURRENCY	LONG/SHORT POSITIONS 31 Dec. 2018	% OF RECOGNISED CAPITAL	Scenario 1	Scenario 2	Scenario 3
EUR – OPEN POSITION	452,000	0.36%	191.35	787.41	1,130.40
USD – OPEN POSITION	-187,000	-0.15%	-446.59	-1,730.33	-2,532.49
CHF – OPEN POSITION	229,000	0.18%	355.88	1,508.09	2,325.84
AUD – OPEN POSITION	177,000	0.14%	411.84	1,595.39	2,435.77
TOTAL			**512.48**	**2,160.56**	**3,359.51**

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.14. Market risks (continued)

37.14.1. Currency risk (continued)

FX assets and liabilities of the Bank as at 31 December 2018 are presented as follows:

in thousands of HRK

2018	**EUR**	**USD**	**Other**	**HRK, currency clause**	**Total FX equivalents**	**HRK**	**Total**
ASSETS							
Cash	12,363	1,737	4,103	-	18,203	188,148	**206,351**
Receivables from the Croatian National Bank	-	-	-	-	-	142,387	**142,387**
Placements with banks	7,261	415	11,573	-	19,249	-	**19,249**
Financial assets at fair value through other comprehensive income	319,140	-	-	340,920	660,060	92,621	**752,681**
Financial assets at fair value through profit or loss	-	-	-	-	-	492	**492**
Financial assets at amortised cost	-	-	-	-	-	496	**496**
Loans and advances to customers	1,432	3,816	416	627,105	632,769	448,561	**1,081,330**
Investment property	-	-	-	-	-	34,446	**34,446**
Property and equipment	-	-	-	-	-	5,646	**5,646**
Intangible assets	-	-	-	-	-	3,506	**3,506**
Foreclosed assets	-	-	-	-	-	28,518	**28,518**
Assets held for sale	-	-	-	-	-	5,280	**5,280**
Deferred tax assets	-	-	-	-	-	1,119	**1,119**
Other assets	-	-	4	2	6	24,153	**24,159**
Total assets	**340,196**	**5,968**	**16,096**	**968,027**	**1,330,287**	**975,373**	**2,305,660**
EQUITY AND LIABILITIES							
Liabilities to banks	1,789	88	187	0	2,064	108,479	**110,543**
Demand deposits	149,393	3,370	11,142	0	163,905	344,696	**508,601**
Term deposits	1,144,486	14,890	12,848	11,518	1,183,742	234,368	**1,418,110**
Borrowings	-	-	-	-	-	114,311	**114,311**
Other liabilities	131	2	2	-	135	9,919	**10,054**
Provisions	-	-	-	-	-	13,944	**13,944**
Total liabilities	**1,295,799**	**18,350**	**24,179**	**11,518**	**1,349,846**	**825,717**	**2,175,563**
EQUITY							
Share capital	-	-	-	-	-	474,600	**474,600**
Accumulated loss	-	-	-	-	-	(343,382)	**(343,382)**
Revaluation reserves	-	-	-	-	-	(1,121)	**(1,121)**
Total equity	-	-	-	-	-	130,097	**130,097**
Total liabilities and equity	**1,295,799**	**18,350**	**24,179**	**11,518**	**1,349,846**	**955,814**	**2,305,660**
Net assets/liabilities and equity	(955,603)	(12,382)	(8,083)	956,509	(19,559)	19,559	-

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.14. Market risks (continued)

37.14.1 Currency risk (continued)

FX assets and liabilities of the Bank as at 31 December 2017 are shown as follows:

in thousands of HRK

2017	EUR	USD	Other	HRK, currency clause	Total FX equivalents	HRK	Total
ASSETS							
Cash	76,000	3,398	17,006	-	96,404	80,264	**176,668**
Receivables from the Croatian National Bank	-	-	-	-	-	149,557	**149,557**
Placements with banks	420	14,902	7,770	-	23,092	-	**23,092**
Available-for-sale financial assets	491,378	-	-	292,809	784,187	102,866	**887,053**
Held-to-maturity financial assets	-	-	-	-	-	-	**-**
Loans and advances to customers	297,817	4,167	613	351,614	654,211	498,810	**1,153,021**
Investment property	-	-	-	-	-	33,630	**33,630**
Property and equipment	-	-	-	-	-	6,280	**6,280**
Intangible assets	-	-	-	-	-	4,187	**4,187**
Foreclosed assets	-	-	-	-	-	15,397	**15,397**
Assets held for sale	-	-	-	-	-	5,280	**5,280**
Deferred tax assets	-	-	-	-	-	4,089	**4,089**
Other assets	744	-	3	-	747	31,815	**32,562**
Total assets	**866,359**	**22,467**	**25,392**	**644,423**	**1,560,482**	**932,175**	**2,490,816**
EQUITY AND LIABILITIES							
Liabilities to banks	1,804	85	238	-	2,127	60,046	**62,173**
Demand deposits	121,822	5,543	5,488	-	132,853	279,029	**411,882**
Term deposits	1,384,255	18,909	19,131	12,274	1,434,569	247,659	**1,682,228**
Borrowings	-	-	-	414	414	163,078	**163,492**
Other liabilities	154	2	-	-	156	10,507	**10,663**
Provisions	-	-	-	-	-	8,370	**8,370**
Total liabilities	**1,508,035**	**24,539**	**24,857**	**12,688**	**1,570,119**	**768,689**	**2,338,808**
EQUITY							
Share capital	-	-	-	-	-	474,600	**474,600**
Accumulated loss	-	-	-	-	-	(321,167)	**(321,167)**
Revaluation reserves	-	-	-	-	-	(1,425)	**(1,425)**
Total equity	-	-	-	-	-	152,008	**152,008**
Total liabilities and equity	**1,508,035**	**24,539**	**24,857**	**12,688**	**1,570,119**	**920,697**	**2,490,816**
Net assets/liabilities and equity	(641,676)	(2,072)	535	631,735	(11,478)	11,478	-

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.14. Market risks (continued)

37.14.2 Currency risk (continued)

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

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

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

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

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

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

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

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.14. Market risks (continued)

37.14.2 Currency risk (continued)

The table below shows the carrying amounts of the Bank's assets and liabilities as at 31 December 2018, classified into categories by the earlier of contractual repricing and maturity.

in thousands of HRK

2018	Up to 1 month	1 to 3 months	3 to 12 months	1 to 3 years	Over 3 years	Non-interest-bearing	Total
ASSETS							
Cash	-	-	-	-	-	206,351	**206,351**
Receivables from the Croatian National Bank	-	-	-	-	-	142,387	**142,387**
Placements with banks	19,243	-	-	-	-	6	**19,249**
Financial assets at fair value through other comprehensive income	-	205,754	225,154	29,613	286,121	6,039	**752,681**
Financial assets at fair value through profit or loss	492	-	-	-	-	-	**492**
Financial assets at amortised cost	496	-	-	-	-	-	**496**
Loans and advances to customers	133,624	337,245	146,347	335,017	69,029	60,068	**1,081,330**
Investment property	-	-	-	-	-	34,446	**34,446**
Property and equipment	-	-	-	-	-	5,646	**5,646**
Intangible assets	-	-	-	-	-	3,506	**3,506**
Foreclosed assets	-	-	-	-	-	28,518	**28,518**
Assets held for sale	-	-	-	-	-	5,280	**5,280**
Deferred tax assets	-	-	-	-	-	1,119	**1,119**
Other assets	-	-	-	-	-	24,159	**24,159**
Total assets	**153,855**	**542,999**	**371,501**	**364,630**	**355,150**	**517,525**	**2,305,660**
EQUITY AND LIABILITIES							
Liabilities to banks	95,055	11,600	3,746	-	-	142	**110,543**
Demand deposits	15,938	0	492,663	-	-	-	**508,601**
Term deposits	87,540	102,604	944,139	254,712	13,547	15,568	**1,418,110**
Borrowings	39	260	619	1,539	111,530	324	**114,311**
Other liabilities	-	-	-	-	-	10,054	**10,054**
Provisions	-	-	-	-	-	13,944	**13,944**
Total liabilities	**198,572**	**114,464**	**1,441,167**	**256,251**	**125,077**	**40,032**	**2,175,563**
EQUITY							
Share capital	-	-	-	-	-	474,600	**474,600**
Accumulated loss	-	-	-	-	-	(343,382)	**(343,382)**
Revaluation reserves	-	-	-	-	-	(1,121)	**(1,121)**
Total equity	-	-	-	-	-	**130,097**	**130,097**
Total liabilities and equity	**198,572**	**114,464**	**1,441,167**	**256,251**	**125,077**	**170,129**	**2,305,660**
Net assets/liabilities and equity	**(44,717)**	**428,535**	**(1,069,666)**	**108,379**	**230,073**	**347,396**	-

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.14. Market risks (continued)

37.14.2. Interest rate risk (continued)

The table below shows the carrying amounts of the Bank's assets and liabilities as at 31 December 2017, classified into categories by the earlier of contractual repricing and maturity.

in thousands of HRK

2017	Up to 1 month	1 to 3 months	3 to 12 months	1 to 3 years	Over 3 years	Non-interest-bearing	Total
ASSETS							
Cash	-	-	-	-	-	176,668	**176,668**
Receivables from the Croatian National Bank	-	-	-	-	-	149,557	**149,557**
Placements with banks	23,083	-	-	-	-	9	**23,092**
Available-for-sale financial assets	50,000	-	150,195	347,876	322,824	16,158	**887,053**
Held-to-maturity financial assets	-	-	-	-	-	-	**-**
Loans and advances to customers	143,024	36,676	454,204	343,929	73,871	101,317	**1,153,021**
Investment property	-	-	-	-	-	33,630	**33,630**
Property and equipment	-	-	-	-	-	6,280	**6,280**
Intangible assets	-	-	-	-	-	4,187	**4,187**
Foreclosed assets	-	-	-	-	-	15,397	**15,397**
Assets held for sale	-	-	-	-	-	5,280	**5,280**
Deferred tax assets	-	-	-	-	-	4,089	**4,089**
Other assets	-	-	-	-	-	32,562	**32,562**
Total assets	**216,107**	**36,676**	**604,399**	**691,805**	**396,695**	**545,134**	**2,490,816**
EQUITY AND LIABILITIES							
Liabilities to banks	-	10,000	51,890	-	-	283	**62,173**
Demand deposits	238	-	407,835	-	-	3,809	**411,882**
Term deposits	94,372	144,045	670,050	728,329	15,001	30,431	**1,682,228**
Borrowings	40,170	715	1,986	93,694	23,454	3,473	**163,492**
Other liabilities	-	-	-	-	-	10,663	**10,663**
Provisions	-	-	-	-	-	8,370	**8,370**
Total liabilities	**134,780**	**154,760**	**1,131,761**	**822,023**	**38,455**	**57,029**	**2,338,808**
EQUITY							
Share capital	-	-	-	-	-	474,600	**474,600**
Accumulated loss	-	-	-	-	-	(321,167)	**(321,167)**
Revaluation reserves	-	-	-	-	-	(1,425)	**(1,425)**
Total equity	-	-	-	-	-	**152,008**	**152,008**
Total liabilities and equity	**134,780**	**154,760**	**1,131,761**	**822,023**	**38,455**	**209,037**	**2,490,816**
Net assets/liabilities and equity	**81,327**	**(118,084)**	**(527,362)**	**(130,218)**	**358,240**	**336,097**	**-**

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.14. Market risks (continued)

37.14.2. Interest rate risk (continued)

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

in thousands of HRK

	2018	2017
	in %	*in %*
Assets		
Cash	(0.65)-0.00	(0.65)-0.00
Placements with banks	0.00-3.50	0.00-4.50
Available-for-sale financial assets	0.00-4.98	0.05-7.26
Loans and advances to customers	1.95-8.50	2.10-10.50
Equity and liabilities		
Liabilities to banks	0.01-1.20	0.15-1.40
Demand deposits	0.00-0.06	0.00-0.06
Term deposits	0.03-2.10	0.01-2.10
Borrowings	0.00-1.80	0.20-1.80

37.14.3. Price risk

Price risk is the risk that the value of the financial instrument will fluctuate as a result of changes in market prices, whether caused by factors specific to an individual investment, its issuer or all factors affecting all instruments traded in the market. The risk is managed by setting maximum volumes, limits and other restrictions. The Bank manages the risk by setting Trading Book limits (generally not applied, and the Bank had no positions in the Trading Book at 31 December 2018), with the available-for-sale and held-to-maturity portfolio durations being measured, monitored and reported regularly.

Stress testing interest rate risk in the banking book

Interest rate risk in the banking book is the risk of loss arising from possible changes in interest rates, impacting the items in the banking book. For the purposes of the stress tests, the Bank uses a simplified calculation of the changes in the economic value of the banking book, as defined in the Decision on interest rate risk in the banking book.

The Bank performs the shock-test to determine the impact of a one-off increase or decrease of interest rates by 100 basis points over a one-year period. As at 31 December 2018 it amounted to HRK 1,510 thousand or 2.44% (2017, HRK 1,660 thousand or 2.40%). The impact relates to the impact of the interest gap on the expected annual interest margin at 100 basis points. Potential risk is due to premature repayment of asset items due to the potential downward interest rates movement of the competition together with the equity and liabilities contracted for a longer term at a fixed interest rate.

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.15. Market risk measurement techniques

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

VaR method

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

Currency exposure limits

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

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

Daily VAR calculation

	Internal limit	At 31 December 2018
Bank's total open FX position	25.00%	0.97%
Maximum open FX position in EUR	20.00%	0.36%
Maximum open FX position in USD	10.00%	-0.15%
Maximum open FX position in other currencies	5.00%	0.18% for CHF

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

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

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

Stress tests

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

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

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.15. Market risk measurement techniques (continued)

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

In performing liquidity stress tests, the Bank assumes a liquidity shock on the market, such as deposit withdrawal or inability to place on the market the instruments the Bank possesses without incurring significant loss. In doing so, potential outflows are estimated under scenario and sensitivity analyses. In defining a scenario, the Bank considers the circumstances that may arise upon the expiry of a significant volume of deposits or losing a part of its unsecured sources of funding, including deposits from major customers etc. The baseline scenarios used for the purpose of the analysis, with individual factors having two levels of disturbance intensity, are defined as follows:
1) Internal crisis of the Bank,
2) Market crisis
3) A combination of both.
VaR is not used in performing liquidity stress tests, as in extreme circumstances the losses exceed the expected losses in a much larger number of instances than envisaged using VaR.

Stress testing interest rate risk in the banking book

Interest rate risk in the banking book is the risk of loss arising from possible changes in interest rates, impacting the items in the banking book. For the purposes of the stress tests, the Bank uses a simplified calculation of the changes in the economic value of the banking book, as defined in the Decision on interest rate risk in the banking book.
The Bank performs the shock-test to determine the impact of a one-off increase or decrease of interest rates by 100 basis points over a one-year period.

TIME ZONES *	ESTIMATED MODIFIED DURATION *	WEIGHTED (200bb) *
UP TO 1 MONTH	0,04	0,08%
FROM 1 TO 3 MONTHS	0,16	0,32%
FROM 3 TO 6 MONTHS	0,36	0,72%
FROM 6 TO 12 MONTHS	0,71	1,43%
FROM 1 TO 2 YEARS	1,38	2,77%
FROM 2 TO 3 YEARS	2,25	4,49%
FROM 3 TO 4 YEARS	3,07	6,14%
FROM 4 TO 5 YEARS	3,85	7,71%
FROM 5 TO 7 YEARS	5,08	10,15%
FROM 7 TO 10 YEARS	6,63	13,26%
FROM 10 TO 15 YEARS	8,92	17,84%
FROM 15 TO 20 YEARS	11,21	22,43%
OVER 20 YEARS	13,01	26,03%

The economic value to regulatory capital, pursuant to the methodology of the CNB (200 bp), calculated on 31 December 2018, is as follows:

	Internal limit	**Internal early warning system**	**At 31 December 2018**
Change in economic value/regulatory capital	15%	13%	18.09%

37. RISK MANAGEMENT POLICIES (CONTINUED)

37.16. Operational risk

The Bank is exposed to operational risk in all its business activities. The objective of operational risk management is to identify all occurrences of operational risk, to control and minimise operational risk exposure.

The Bank seeks to achieve optimum operational risk management in accordance with the principles defined by the Bank's regulator and policies, with a view to mitigating and avoiding operational risks. In this regard, the Bank collects data on operational risk events, monitors key risk indicators, conducts scenario analysis, assesses operational risk in its operations, reports to Management on operational risk exposure and proposes measures to reduce, avoid and transfer operational risk. Operational risk does not have a material effect on the Bank’s operations.

38. Fair value of financial assets and liabilities

Fair value is defined as the price that would be received from selling an asset or paid for transferring a liability in an orderly transaction between market participants at the measurement date, the so-called exit price. Financial assets measured at fair value through other comprehensive income are stated at fair value.

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

in thousands of HRK

	Carrying amount		Fair value	
	2018	**2017**	**2018**	**2017**
Financial assets				
Cash				
Receivables from the Croatian National Bank	206,351	176,668	206,351	176,668
Placements with banks	142,387	149,557	142387	149,557
Loans and receivables from banks	19,249	23,092	19,249	23,092
Loans and receivables from customers	19,249	23,092	19,249	23,092
Financial assets at FV through OCI	1,081,330	1,154,862	1,055,336	1,126,079
Financial assets at FV through P&L	752,681	-	752,681	-
	492	-	492	-
Financial liabilities				
Deposits from banks	110,543	62,173	110,543	62,173
Deposits from customers	1,926,711	2,094,110	1,898,022	2,059,842
Borrowings	114,311	163,492	114,311	163,492

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

Corporate customers	Carrying amount		Fair value	
	2018	**2017**	**2018**	**2017**
Financial assets				
Loans and receivables from customers	740,906	781,671	732,491	771,990
Held-to-maturity financial assets	-	-	-	-
Financial liabilities				
Deposits from customers	389,207	317,637	389,065	316,943

38. FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES (CONTINUED)

Retail customers	**Carrying amount**		**Fair value**	
	2018	**2017**	**2018**	**2017**
Financial assets				
Loans and receivables from customers	340,424	373,191	322,845	354,089
Financial liabilities				
Deposits from customers	1,537,504	1,776,473	1,508,957	1,742,899

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

Loans and receivables from banks

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

Loans and receivables from customers

Loans and receivables are reported net of provision for impairment. The estimated fair value of loans and receivables represents the discounted amount of estimated future cash flows. Future cash flows are discounted using current market rates to arrive at their fair value. Expected future losses are not taken into account and adjustments for uncertainty of collection are not made (including terms) for due and restructured exposures, as well as undue exposures that require increased attention.

Deposits from banks

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

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

Deposits from customers

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

39. CAPITAL MANAGEMENT

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

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

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

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

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

in thousands of HRK

	31 December 2018	31 December 2017
Regulatory capital		
Tier 1 capital		
Issued share capital	474,600	474,600
Share premium	-	-
Accumulated loss (excluding profit for the year)	(343,382)	(321,167)
Legal, statutory and other reserves	-	-
Deductions according to the Regulation (EU) No. 575/2013 /i/	(5,381)	(7,252)
Total Tier 1 capital	125,837	146,181
Additional capital	-	-
Total additional capital	-	-
Deductions from investments in banks and other financial institutions	-	-
Total regulatory capital	**125,837**	**146,181**

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

At 31 December 2018, the Bank's regulatory capital amounted to HRK 125,837 thousand (2017: HRK 146,181 thousand).

39. CAPITAL MANAGEMENT (CONTINUED)

in thousands of HRK

	31 December 2018	31 December 2017
Total capital ratio according to Regulation EU No. 575/2013		
Capital requirements		
Credit risk exposure	55,976	61,105
Balance sheet items	*54,376*	*59,652*
Off-balance-sheet items	*1,600*	*1,453*
Currency risk exposure	232	-
Operational risk exposure	11,009	12,681
Capital requirements for total capital ratio	**67,217**	**73,786**
Additional capital requirements		
Capital requirements for prescribed additional capital rate	26,803	34,218
Capital conservation buffer	21,005	23,058
Systemic risk buffer	12,603	13,835
Total capital requirements	**127,628**	**144,897**
Common Equity Tier 1 capital ratio	**14.98%**	**15.85%**
Tier 1 capital ratio	**14.98%**	**15.85%**
Total capital ratio	**14.98%**	**15.85%**

The comparative information presents the total capital ratio in accordance with the requirements of Regulation (EU) No. 575/2013. As at 31 December 2018, the total capital ratio is 14.98% (2017: 15.85%).

At 31 December 2018, the Bank did not comply with all capital requirements, whereas as at 31 December 2017 all capital requirements were met. At the beginning of 2018, the Bank activated the Capital Conservation Plan in accordance with subordinate legislation defining procedures in cases of non-compliance with capital requirements approved by the CNB. In addition, no additional measures were taken by the CNB.

Meanwhile, as at 20 February 2019 thee Bank met all capital requirements and the total capital ratio was 15.37%, whereof the Bank informed the Croatian National Bank. Thereby the requirements that had resulted in the preparation and implementation of the Capital Conservation Plan ceased to exist, but the Bank still has to carry out the planned activities in order to maintain the minimum capital ratio.

Legal reserve

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

Fair value reserve

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

Accumulated loss

Accumulated loss includes losses accumulated from previous years.

40. CONCENTRATION OF ASSETS, LIABILITIES AND OFF-BALANCE SHEET ITEMS

The concentration of assets, liabilities and off-balance sheet items is presented below:

in thousands of HRK

	31 December 2018			31 December 2017		
	Assets	Liabilities	Off-balance sheet items	Assets	Liabilities	Off-balance sheet items
Geographical region						
Republic of Croatia	2,189,210	2,192,066	117,373	2,463,640	2,349,920	111,073
Europe	115,607	46,017	10	24,544	127,400	5
Other	843	67,577	21	2,632	13,496	-
Total by geographical region	**2,305,660**	**2,305,660**	**117,404**	**2,490,816**	**2,490,816**	**111,078**
Sector						
Republic of Croatia (state)	697,616	31,680	1,550	902,991	292,250	591
Croatian National Bank	327,015	125,444	0	121,860	107,826	-
Trade and commerce	104,697	24,235	14,027	119,534	23,956	10,447
Finance	39,657	160,524	1,184	55,349	80,828	400
Tourism	33,715	2,179	9	29,769	3,250	225
Agriculture	103,376	8,730	1,447	120,530	6,732	2,076
Industry	597,705	35,920	53,460	614,469	41,070	51,909
Individuals	291,380	1,534,733	18,718	504,567	1,732,430	15,868
Other	110,499	382,215	27,010	21,747	202,474	29,562
Total by sector	**2,305,660**	**2,305,660**	**117,404**	**2,490,816**	**2,490,816**	**111,078**
Allocated value of collateral	883,221		31,461	971,673		37,488

41. EVENTS AFTER THE BALANCE SHEET DATE

As at 31 December 2018, the Bank did not meet all capital requirements (the prescribed minimum ratio of total capital was 15.19%), while as at 31 December 2017 the Bank met all the requirements. At the beginning of 2018, the Bank activated the Capital Conservation Plan in accordance with subordinate legislation defining procedures in cases of non-compliance with capital requirements approved by the CNB. In addition, no additional measures were taken by the CNB.

Meanwhile, as at 20 February 2019, the Bank met all capital requirements and the total capital ratio was 15.37%, whereof the Bank informed the Croatian National Bank. Thereby the requirements that had resulted in the preparation and implementation of the Capital Conservation Plan ceased to exist, but the Bank still has to carry out the planned activities in order to maintain the minimum capital ratio.

Danijel Luković		Tadija Vrdoljak
President of the Management Board	CROATIA BANKA d.d. Zagreb UPRAVA	Member of the Management Board

SUPPLEMENTARY REPORT FOR THE CROATIAN NATIONAL BANK

The basic financial statements proovided below were prepared within the reporting framework and the basic financial statements stipulated by the CNB's Decision on the structure and content of annual financial statements of banks (hereinafter referred to as the 'Decision').

Statement of financial position (Balance sheet)
as at 31 December 2018

BAN-BIL form

Entity: CROATIA BANKA d.d.				
Description	AOP mark	Note no.	Previous year (net)	Current year (net)
1	2	3	4	5
Assets				
1. Cash receivables from central banks and other demand deposits (AOP 002 to 004)	001		349,307,684	206,349,913
1.1. Cash on hand	002		34,946,809	17,683,366
1.2. Cash receivables from central banks	003		270,198,986	182,262,035
1.3. Other demand deposits	004		44,161,889	6,404,512
2. Financial assets held for trading (AOP 006009)	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 that must be carried at fair value through profit or loss (AOP 011 to 013)	010		0	491,574
3.1. Equity instruments	011		0	0
3.2. Debt securities	012		0	0
3.3. Loans and advances	013		0	491,574
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		887,050,877	752,680,191
5.1. Equity instruments	018		438,500	438,500
5.1. Debt securities	019		886,612,377	752,241,691
5.2. Loans and advances	020		0	0
6. Financial assets at amortised cost (AOP 022+023)	021		1,188,498,397	1,270,699,912
6.1. Debt securities	022		0	495,940
6.2. Loans and advances	023		1,188,498,397	1,270,203,972
7. Derivatives - hedge accounting.	024		0	0
8. Changes in fair value of hedged items in hedging the portfolio against credit risk	025		0	0
9. Investments in subsidiaries, joint ventures and associates	026		0	0
10. Tangible assets	027		55,307,718	40,091,701
11. Intangible assets	028		4,187,188	3,506,467
12. Tax assets	029		4,098,948	1,126,724
13. Other assets	030		597,163	29,387,044
14. Non-current assets and disposal groups classified as held-for-sale	031		5,280,062	5,280,062
15. TOTAL ASSETS(AOP 001 + 005 + 010 + 014 + 017 + 021 + 024 do 031)	032		2,494,328,037	2,309,613,588
Description	AOP mark	Note no.	Previous year (net)	Current year (net)

1	2	3	4	5
Liabilities				
16. Financial liabilities held for trading (AOP 034 to 038)	**033**		0	0
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
17. Financial liabilities at fair value through or loss (AOP 040 to 042)	**039**		0	0
17.1. Deposits	**040**		0	0
17.2. Issued debt securities	**041**		0	0
17.3. Other financial liabilities	**042**		0	0
18. Financial liabilities carried at amortised cost (AOP 044 to 046)	**043**		2,317,134,711	2,149,934,510
18.1. Deposits	**044**		2,316,881,012	2,149,730,449
18.2. Debt securities issued	**045**		0	0
18.3. Other financial liabilities	**046**		253,699	204,061
19. Derivatives - hedge accounting	**047**		0	0
20. Changes in fair value of hedged items in hedging the portfolio against credit risk	**048**		0	0
21. Provisions	**049**		8,368,588	13,627,903
22. Tax payable	**050**		340,085	216,214
23. Share capital repayable on demand	**051**		0	0
24. Other liabilities	**052**		16,476,227	15,738,417
25. Liabilities of disposal group classified as held-for-sale	**053**		0	0
26. TOTAL LIABILITIES(AOP 033039043047+134053)	**054**		2,342,319,611	2,179,517,044
Equity				
27. Share capital	**055**		474,600,000	474,600,000
28. Share premium	**056**		0	0
29. Issued equity instruments except for equity	**057**		0	0
30. Other equity instruments	**058**		0	0
31. Accumulated other comprehensive income	**059**		-1,424,629	-1,121,432
32. Retained earnings	**060**		-290,536,057	-318,392,941
33. Revaluation reserves	**061**		0	0
34. Other reserves	**062**		0	0
35. Treasury shares	**063**		0	0
36. Profit or loss attributable to owners of the parent company	**064**		-30,630,888	-24,989,083
37. Dividends for the year	**065**		0	0
38. Minority (non-controlling) interests	**066**			0
39. TOTAL EQUITY (AOP 055 to 066)	**067**		152,008,426	130,096,544
40. TOTAL LIABILITIES AND EQUITY (AOP 054+067)	**068**		2,494,328,037	2,309,613,588

SUPPLEMENTARY REPORT FOR THE CROATIAN NATIONAL BANK (CONTINUED)

Income statement for the period from 1 January 2018 to 31 December 2018 - BAN-RDG form

Entity: CROATIA BANKA d.d.

Description	AOP mark	Note no.	Previous year	Current year
1	2	3	4	5
1. Interest income	069		98,090,152	67,426,958
2. Interest expense	070		39,502,644	23,603,538
3. Expenses from share capital repayable on demand	071		0	0
4. Dividend income	072		0	0
5. Fee and commission income	073		10,304,888	9,115,691
6. Fee and commission expense	074		4,753,491	3,545,644
7. Gains or losses on derecognition of financial assets and liabilities not carried at fair value through profit or loss, net	075		15,183,547	638,848
8. Gains or losses on financial assets and liabilities held for trading, net	076		2,595,774	2,408,865
9. Gains or losses on financial assets not traded and carried at fair value through profit or loss, net	077		0	0
10. Gains or losses on financial assets and liabilities at fair value through profit or loss, net	078		0	0
11. Hedging gains/losses	079		0	0
12. Foreign exchange gains or losses, net	080		0	-73,988
13. Gains or losses on derecognition of non-financial assets, net	081		4,073,145	0
14. Other operating income	082		4,604,608	8,471,423
15. Other operating expenses:	083		5,989,470	418,088
16. TOTAL OPERATING INCOME, NET (AOP 069 - 070 - 071 + 072 + 073 - 074 + 075 to 082 - 083)	084		84,606,509	60,420,527
17. Administrative expenses	085		58,152,044	57,405,215
18. Depreciation and amortisation	086		3,425,125	2,963,885
19. Gains or losses on changes, net	087		0	0
20. Provisions or reversal of provisions	088		927,178	6,481,311
21. Impairment or reversal of impairment of financial assets not carried at fair value through profit or loss	089		46,295,805	15,418,184
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		7,060,150	183,798
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		0	0
27. PROFIT OR LOSS BEFORE TAX FROM CONTINUING OPERATIONS (AOP 084 - 085 - 086 + 087 - 088 do 091+ 092 to 094)	095		-31,253,793	-22,031,866
28. Tax expense or income relating to profit or loss from continuing operations	096		**-655,604**	2,903,068

Description	AOP mark	Note no.	Previous year	Current year
1	2	3	4	5
29. PROFIT OR LOSS AFTER TAX FROM CONTINUING OPERATIONS (AOP 095 - 096)	**097**		-30,598,189	-24,934,934
30. Profit or loss after tax from discontinued operations (AOP 099 - 100)	**098**		-32,699	-54,149
30.1. Profit or loss before tax from discontinued operations	**099**		**-32,699**	**-54,149**
30.2. Tax expense or income relating to discontinued operations	**100**			
31. PROFIT OR LOSS FOR THE YEAR (AOP 097 + 098; 102 + 103)	**101**		-30,630,888	-24,989,083
32. Attributable to minority (non-controlling) interest	**102**			
33. Attributable to owners of the parent company	**103**			
STATEMENT OF OTHER COMPREHENSIVE INCOME				
1. Comprehensive income or loss of current year (AOP 101+024)	**104**		-30,630,888	-24,989,083
2. Other comprehensive income (AOP 106 + 118)	**105**		-6,995,687	303,197
2.1. Items that will not be reclassified to profit or loss (AOP 107 to 113 + 116 + 117	**106**		0	0
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 Changes in fair value of equity instruments carried at fair value through other comprehensive income (hedged item)	**114**		0	0
2.1.9 Changes in fair value of equity instruments carried at fair value through other comprehensive income (hedging instrument)	**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
2.2. Items that may be reclassified to profit or loss (AOP 119 to 126)	**118**		-6,995,687	303,197
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**		-8,531,326	369,752
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**		1,535,639	-66,555
3. Total comprehensive income for the year (AOP 104 + 105 and AOP 128 + 129)	**127**		-37,626,575	-24,685,886
4. Attributable to minority (non-controlling) interest	**128**			
5. Attributable to owners of the parent company	**129**			

SUPPLEMENTARY REPORT FOR THE CROATIAN NATIONAL BANK (CONTINUED)

Statement of cash flows, indirect method– POD-NTI form

Entity; CROATIA BANKA d.d.				
Description	AOP mark	Note no.	Previous year	Current year
1	2	3	4	5
Operating activities and adjustments				
1. Profit/loss before tax	001		-31,286,492	-22,086,015
2. Impairment losses and provisions	002		55,135,133	22,614,059
3. Depreciation and amortisation	003		3,425,125	2,963,885
4. Net unrealised gains/losses from financial assets and liabilities at fair value through profit or loss	004		-3,161,143	-3,020,791
5. Gain/losses on sale of tangible assets	005		-4,073,145	-1,883,096
6. Other non-cash items	006		-17,912,405	-765,495
Movements in assets and liabilities from operating activities				
7. Deposits with CNB	007		42,577,141	7,203,482
8. Deposits with financial institutions and loans to financial institutions	008		0	0
9. Loans and advances to other customers	009		318,568,689	-14,357,428
10. Securities and other financial instruments at fair value through other comprehensive income	010		-43,009,401	117,936,817
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 be carried at fair value through profit or loss	013		0	0
14. Securities and other financial instruments carried at amortised cost	014		0	-499,232
15. Other assets from operating activities	015		9,403,448	11,906,084
Increase/decrease in operating liabilities				
16. Deposits from financial institutions	016		-29,921,118	48,367,837
17. Transaction accounts of other customers	017		-50,868,759	-673,938
18. Savings deposits of other customers	018		-514,594	97,391,843
19. Term deposits of other customers	019		-367,216,505	-253,099,806
20. Derivative financial liabilities and other trading liabilities	020			0
21. Other liabilities	021		242,333	-861,681
22. Outstanding interest from operating activities	022		100,576,655	64,248,203
23. Dividend received from operating activities	023		0	0
24. Interest paid from operating activities	024		-6,039,260	-3,091,256
25. Income tax paid	025		0	0
A) Net cash flows from operating activities (AOP 001 to 025)	026		-24,074,298	72,293,472
Investing activities				
1. Proceeds from sale/payments for purchases/of tangible and intangible assets	027		6,717,025	3,140,250
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		15,520,450	0
4. Dividends received from investing activities	030		0	0
5. Other proceeds/payments from investing activities	031		-1,490,494	0
B) Net cash flow from investing activities (AOP 027 to 031)	032		20,746,981	3,140,250
Financing activities				
1. Net increase/decrease in borrowings from financing activities	033		-128,510,972	-49,180,510
2. Net increase/decrease in issued debt securities	034		0	0
3. Net increase/decrease in T2 capital instruments	035		0	0
4. Share capital increase	036		0	0
5. Dividend paid	037		0	0
6. Other proceeds/payments from financing activities	038		0	0
C) Net cash flows from financing activities (AOP 033 to 038)	039		-128,510,972	-49,180,510
D) Net increase / decrease in cash and cash equivalents (AOP 026+032+039)	040		-131,838,289	26,253,212
Cash and cash equivalents at beginning of year	041		333,257,921	201,419,632
Effects of foreign currency exchange rate fluctuations on cash and cash equivalents	042		0	0
Cash and cash equivalents at end of year (AOP 040+041+042)	043		201,419,632	227,672,844

SUPPLEMENTARY REPORT FOR THE CROATIAN NATIONAL BANK (CONTINUED)

CHANGES IN CAPITAL for the period from 1 January 2018 to 31 December 2018 - BANK-PK form

Position description	AOP mark	Note no.	Attributable to equity holders of the parent											Minority interest		Total
			Equity	Share premium	Issued equity instruments except for equity	Other equity instruments	Accumulated other comprehensive income	Retained earnings	Revaluation reserves	Other reserves	Treasury shares	Profit / loss attributable to owners of the parent company	Dividends during the year	Accumulated other comprehensive income	Other items	
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17 (4 to 16)
1. Opening balance (before restatement)	**01**		**474,600,000**				**-1,424,629**	**-318,392,941**								**154,782,430**
2. Effect of corrections of errors	**02**															0
3. Effects of changes in accounting policies	**03**															0
4. Opening balance (current period)(AOP 01 to 03)	**04**		**474,600,000**	**0**	**0**	**0**	**-1,424,629**	**-318,392,941**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**154,782,430**
5. Issue of ordinary shares	**05**															0
6. Issue of preference shares	**06**															0
7. Issue of other equity instruments	**07**															0
8. Execution or expiry of other issued equity instr.	**08**															0
9. Debt to equity swaps	**09**															0
10. Capital reduction	**10**															0
11. Dividends	**11**															0
12. Purchase of treasury shares	**12**															0
13. Sale or extinguishment of treasury shares	**13**															0
14. Reclassification of financial instruments from equity instruments to liabilities	**14**															0
15. Reclassification of financial instruments from liabilities to equity instruments	**15**															0
16. Transfers between equity instr.components	**16**															0
17. Increase or decrease in equity instruments resulting from business combinations	**17**															0
18. Share-based payments	**18**															0
19. Other increase or decrease in equity instr.	**19**															0
20. Total comprehensive income for the year	**20**						303,197					-24,989,083				-24,685,886
21. Closing (current period) (AOP 04 to 20)	**21**		**474,600,000**	**0**	**0**	**0**	**-1,121,432**	**-318,392,941**	**0**	**0**	**0**	**-24,989,083**	**0**	**0**	**0**	**130,096,544**

SUPPLEMENTARY REPORT FOR THE CROATIAN NATIONAL BANK (CONTINUED)

Balance sheet reconciliation as at 31 December 2018

Mismatches of items in the balance sheet disclosed in the Annual Report in relation to the standard prescribed in CNB's Decision relate to the following categories:

in thousands of HRK

Item		CNB Decision	Annual Report	Difference
1. Cash, cash receivable from central banks and other demand deposits	**001**	**206,351**	**367,987**	**(161,636)**
1.1. Cash on hand	002	17,683	-	17,683
1.2. Cash receivable from central banks	003	182,262	-	182,262
1.3. Other demand deposits	004	6,406	-	6,406
Cash		-	*206,351*	*(206,351)*
Receivables from the Croatian National Bank		-	*142,387*	*(142,387)*
Placements with banks		-	*19,249*	*(19,249)*
2. Financial assets held for trading (AOP 006 to 009)	**005**	**-**	**-**	**-**
2.1. Derivatives	006	-	-	-
2.2. Equity instruments	007	-	-	-
2.3. Debt securities	008	-	-	-
2.4. Loans and advances	009	-	-	-
3. Financial assets not traded and mandatorily carried at fair value through profit or loss (AOP 011 to 013)	**010**	**491,574**	**491,574**	**-**
3.1. Equity instruments	011	-	-	-
3.2. Debt securities	012	-	-	-
3.3. Loans and advances	013	491,574		491,574
Financial assets carried at fair value through profit or loss			*491,574*	*(491,574)*
4. Financial assets at fair value through profit or loss(AOP 015+016)	**014**	**-**	**-**	**-**
4.2. Debt securities	015	-	-	-
4.3. Loans and advances	016	-	-	-
5. Financial assets at fair value through other comprehensive income (AOP 018 to 020)	**017**	**752,681**	**752,681**	**-**
5.1. Equity instruments	018	439	-	439
5.1. Debt securities	019	752,242	-	752,242
5.2. Loans and advances	020	-	-	-
Financial assets carried at fair value through profit or loss			*752,681*	*(752,681)*
6. Financial assets at amortised cost (AOP 022+023)	**021**	**1,270,204**	**1,081,826**	**188,378**
6.1. Debt securities	022	496	-	496
Financial liabilities at amortised costs			*496*	*(496)*
6.2. Loans and advances	023	1,270,204		1,270,204
Loans and advances to customers		-	*1,081,330*	*(1,081,330)*
7. Derivatives - hedge accounting	**024**	**-**	**-**	**-**
8. Changes in fair value of hedged items in hedging the portfolio against credit risk	**025**	**-**	**-**	**-**
9. Investments in subsidiaries, joint ventures and associates	**026**	**-**	**-**	**-**
10. Tangible assets	**027**	**40,092**	**-**	**40,092**
Investment property		-	*34,446*	*(34,446)*
Property, plant and equipment		-	*5,646*	*(5,646)*
Foreclosed assets		-	*28,518*	*(28,518)*
11. Intangible assets	**028**	**3,506**	**3,506**	**-**
12. Tax assets	**029**	**1,127**	**-**	**1,127**
Deferred tax assets		-	*1,120*	*(1,120)*
13. Other assets	**030**	**29,387**	**-**	**29,387**
Other assets		-	*24,158*	*(24,158)*
14. Non-current assets and disposal groups classified as held-for-sale	**031**	**5,280**	**5,280**	**-**
15. TOTAL ASSETS (AOP 001+005+010+014+017+021+024 to 031)	**032**	**2,309,614**	**2,305,660**	**3,954**

SUPPLEMENTARY REPORT FOR THE CROATIAN NATIONAL BANK (CONTINUED)

Balance sheet reconciliation as at 31 December 2018 (continued)

in thousands of HRK

Item		CNB Decision	Annual Report	Difference
Liabilities				
16. Financial liabilities held for trading (AOP 034 to 038)	**033**	**-**	**-**	**-**
16.1. Derivatives	034	-	-	-
16.2. Short-term items	035	-	-	-
16.3. Deposits	036	-	-	-
16.4. Debt securities issued	037	-	-	-
16.5. Other financial liabilities	038	-	-	-
17. Financial assets at fair value through profit or loss (AOP 040 to 024)	**039**	**-**	**-**	**-**
17.1. Deposits	040	-	-	-
17.2. Debt securities issued	041	-	-	-
17.3. Other financial liabilities	042	-	-	-
18. Financial liabilities carried at amortised cost (AOP 044 to 046)	**043**	**2,149,936**	**2,151,565**	**(1,629)**
18.1. Deposits	044	2,149,730	-	2,149,730
18.2. Debt securities issued	045	-	-	-
18.3. Other financial liabilities	046	204	-	204
Bank borrowings		-	*110,543*	*(110,543)*
Demand deposits		-	*508,601*	*(508,601)*
Term deposits		-	*1,418,110*	*(1,418,110)*
Borrowings		-	*114,311*	*(114,311)*
19. Derivatives - hedge accounting	**047**	**-**	**-**	**-**
20. Changes in fair value of hedged items in hedging the portfolio against credit risk	**048**	**-**	**-**	**-**
21. Provisions	**049**	**13,628**	**13,944**	**(316)**
22. Tax payable	**050**	**216**	**-**	**216**
23. Share capital repayable on demand	**051**	**-**	**-**	**-**
24. Other liabilities	**052**	**15,738**		**15,738**
Other liabilities		-	*10,054*	*(10,054)*
25. Liabilities of disposal group classified as held-for-sale	**053**	**-**	**-**	**-**
26. TOTAL LIABILITIES (AOP 033 + 039 + 043 + 047 to 053)	**054**	**2,179,517**	**2,175,563**	**3,954**
Equity				
27. Share capital	**055**	**474,600**	**474,600**	**-**
28. Share premium	**056**	**-**	**-**	**-**
29. Issued equity instruments except for equity	**057**	**-**	**-**	**-**
30. Other equity instruments	**058**	**-**	**-**	**-**
31. Accumulated other comprehensive income	**059**	**(1,121)**	**(1,121)**	**-**
32. Retained earnings	**060**	**(318,393)**	**(318,393)**	**-**
33. Revaluation reserves	**061**	**-**	**-**	**-**
34. Other reserves	**062**	**-**	**-**	**-**
35. Treasury shares	**063**	**-**	**-**	**-**
36. Profit or loss attributable to owners of the parent company	**064**	**(24,989)**	**(24,989)**	**-**
37. Dividends for the year	**065**	**-**	**-**	**-**
38. Minority (non-controlling) interests	**066**	**-**	**-**	**-**
39. TOTAL EQUITY (AOP 055 to 066)	**067**	**130,097**	**130,097**	**-**
40. Total capital and reserves (AOP 054 to +067)	**068**	**2,309,614**	**2,305,660**	**3,954**

SUPPLEMENTARY REPORT FOR THE CROATIAN NATIONAL BANK (CONTINUED)

Balance sheet reconciliation as at 31 December 2018 (continued)

ASSETS

Cash on hand, Cash receivable from central banks and Other demand deposits are items separately dislosed under the CNB standard, while in the Annual Report those items are disclosed within Cash, Receivables from the CNB and Placements with banks. The exception is the mandatory reserve with the CNB, which is disclosed within Receivables from the Croatian National Bank in the Annual Report, while it is disclosed within "Loans and advances (at amortised cost)" in the CNB report.

In the Annual Report, Loans and advances to customers include amounts of principal and accrued interest, less any loan prepayments and collected interest income relating to future periods. In the CNB report, the principal and interest amounts net of the accrued interest income of the future period are disclosed under Loans and advances (at amortised cost) and the amounts of the loan prepayments are disclosed under Other liabilities (not netted off). This item also includes the separate mandatory reserve with the CNB, which is disclosed within Receivables from the Croatian National Bank in the Annual Report. Other receivables are disclosed within Loans and advances in the CNB Report, while in the Annual Report they are disclosed within Other assets.

Also, the item Tangible assets consists of the inventory amount in the CNB report, while inventories in the Annual Report are disclosed within Other assets. Foreclosed assets are disclosed separately in the Annual Report, while they are disclosed within Other assets in the CNB report.

Finally, the balance sheet disclosed in the Annual Report and the CNB Report differ due to the reduction in the prepayment of Loans and advances in the Annual Report.

LIABILITIES AND EQUITY

Financial liabilities carried at amortised cost disclosed in the CNB report in the Annual Report are disclosed within Liabilities to Banks, Demand Deposits, Term Deposits and Borrowings. The difference in amounts refers to Deposits for Custody and Brokerage Services that are reported in the CNB Statement under Other Liabilities and Fees and Commissions payable that are disclosed within Other Liabilities in the Annual Report.

SUPPLEMENTARY REPORT FOR THE CROATIAN NATIONAL BANK (CONTINUED)

Income statement reconciliation as at 31 December 2018

in thousands of HRK

Item		CNB Decision	Annual Report	Difference
1. Interest income	069	67,427	67,424	3
2. Interest expense	070	23,604	23,602	2
3. Expense on share capital repayable on demand	071	-	-	-
4. Dividend income	072	-	-	-
5. Fee and commission income	073	9,116	9,116	-
6. Fee and commission expense	074	3,546	3,546	-
7. Gains or losses on derecognition of financial assets and liabilities not carried at fair value through profit or loss, net	075	639	-	639
8. Gains or losses on financial assets and liabilities held for trading, net	076	2,409	-	2,409
Net (expense)/income from financial operations	-	-	*3,021*	*(3,021)*
9. Gains or losses on financial assets not held for trading and carried at fair value through profit or loss, net	077	-	-	-
10. Gains or losses on financial assets and financial liabilities at fair value through profit or loss, net	078	-	-	-
11. Hedging gains or losses, net	079	-	-	-
12. Foreign exchange gains or losses, net	080	(74)		(74)
Net foreign exchange losses			*(47)*	*47*
13. Gains or losses on derecognition of non-financial assets, net	081	-	-	-
14. Other operating income	082	8,472	8,522	(50)
15. Other operating expenses	083	418	-	418
16. TOTAL OPERATING INCOME, NETO (AOP 069 - 070 - 071 + 072 + 073 - 074 + 075 to 082 - 083)	084	60,421	60,888	(467)
17. Administrative expenses	085	57,405	-	57,405
18. Depreciation and amortisation	086	2,964	-	2,964
Other operating expenses		-	*60,842*	*(60,842)*
19. Gains or losses on changes, net	087	-	-	-
20. Provisions or reversal of provisions	088	6,481	-	6,481
21. Impairment or reversal of impairment of financial assets not carried at fair value through profit or loss	089	15,418	-	15,418
22. Impairment or reversal of impairment of investments in subsidiaries, joint ventures and associates	090	-	-	-
23. Impairment or reversal of impairment of non-financial assets	091	184		184
Impairment losses and provisions			*(22,132)*	*22,132*
24. Negative goodwill recognised in profit or loss	092	-	-	-
25. Share of profit or loss on investment in subsidiaries, joint ventures and associates accounted for using the equity method	093	-	-	-
26. Gains or losses on non-current assets and disposal group classified as held for sale not qualifying for classification as discontinued operations	094	-	-	-
27. PROFIT OR LOSS BEFORE TAX FROM CONTINUING OPERATIONS (AOP 084 - 085 - 086 + 087 - 088 do 091+ 092 to 094)	**095**	**(22,032)**	**(22,086)**	**54**
28. Tax expenses or income relating to gains or losses on continuing operations	096	(2,903)	(2,903)	-
29. PROFIT OR LOSS AFTER TAX FROM CONTINUING OPERATIONS (AOP 095 - 096)	**097**	**(24,935)**	**(24,989)**	**54**
30. Profit or loss after tax from discontinued operations (AOP 099 - 100)	098	(54)	-	(54)
30.1. Profit or loss before tax from discontinued operations	099	(24,989)	(24,989)	-
30.2. Tax expense or income relating to discontinued operations	100	-	-	-
31. PROFIT OR LOSS FOR THE YEAR (AOP 097 + 098; 102 + 103)	**101**	**(24,989)**	**(24,989)**	**-**
32. Attributable to minority (non-controlling) interest	102	-	-	-
33. Attributable to owners of the parent company	103	-	-	-

SUPPLEMENTARY REPORT FOR THE CROATIAN NATIONAL BANK (CONTINUED)

Income statement reconciliation as at 31 December 2018

The item Net income from financial operations in the Annual Report consists of gains from trading in securities and foreign exchange gains that are disclosed separately in the CNB statement within Gains or losses on derecognition of financial assets and financial liabilities not carried at fair value through profit or loss and Gains or losses on financial assets and liabilities held for trading. The difference results from the gains on swap transactions disclosed in the CNB form within Gains or losses on financial assets and liabilities held for trading", while in the Annual Report it is disclosed within Net Foreign Exchange Losses.

Other operating expenses in the Annual Report in the CNB are disclosed separately within Administrative Expenses, Depreciation and Amortisation and Other Operating Expenses.

Impairment losses and provisions in the Annual Report in the CNB report are presented separately within Provisions or reversal of provisions, Impairment or reversal of impairment of financial assets not carried at fair value through profit or loss and Impairment or reversal of impairment of non-financial assets.

SUPPLEMENTARY REPORT FOR THE CROATIAN NATIONAL BANK (CONTINUED)

Statement of cash flows reconciliation for 2018

in thousands of HRK

Item		CNB Decision	Annual Report	Difference
Operating activities and adjustments				
1. Profit/loss before tax	001	(22,086)	(22,086)	-
2. Impairment losses and provisions	002	22,614	-	-
Impairment allowance for loans and other assets (net)		-	15,962	(15,962)
Provisions for contingent liabilities (net)		-	149	(149)
Provisions for legal disputes (net)		-	6,325	(6,325)
Other provisions (net)		-	177	(177)
3. Depreciation and amortisation	003	2,964	2,964	-
4. Net unrealised gains/losses on financial assets and liabilities at fair value through profit or loss	004	(3,021)	-	(3,021)
(Gains)/losses on realisation of available-for-sale financial assets		-	(639)	639
Gains on currency trading		-	(2,382)	2,382
5. Gains/losses on sale of tangible assets	005	(1,883)	(1,883)	-
6. Other non-cash items	006	(765)	-	(765)
Investment property fair valuation		-	(816)	816
Foreign exchange translation differences		-	47	(47)
Write-off of tangible assets		-	4	(4)
Movements in assets liabilities from financing activities				-
7. Balances with CNB	007	7,203	7,203	-
8. Deposits with financial institutions and loans to financial institutions	008	-	-	-
9. Loans and advances to other customers	009	(14,357)	-	(14,357)
(Increase)/decrease in loans and advances to customers		-	(12,269)	12,269
10. Securities and other financial instruments at fair value through other comprehensive income	010	117,937		117,937
11. Securities and other financial instruments held for trading	011	-	-	-
12. Securities and other financial instruments not actively traded but carried at fair value through profit or loss	012	-	-	-
13. Securities and other financial instruments mandatorily carried at fair value through profit or loss	013	-	-	-
14. Securities and other financial instruments carried at amortised cost	014	(499)	-	(499)
15. Other assets from operating activities	015	11,906	-	11,906
Decrease/increase in other assets		-	10,353	(10,353)
Increase in other liabilities		-	(1,398)	1,398
Increase/decrease in operating liabilities				
16. Deposits from financial institutions	016	48,368		48,368
Increase/(decrease) in bank borrowings		-	48,370	(48,370)
17. Transaction accounts of other customers	017	(674)	-	(674)
18. Savings deposits of other customers	018	97,392	-	97,392
Increase/decrease in demand deposits		-	96,719	(96,719)
19. Term deposits of other customers	019	(253,100)	-	(253,100)
Increase in term deposits		-	(253,101)	253,101
20. Derivative financial liabilities and other trading liabilities	020	-	-	-
21. Other liabilities	021	(862)	-	(862)
22. Interest collected from operating activities	022	64,248	-	64,248
Interest received		-	64,248	(64,248)
23. Dividends received from operating activities	023	-	-	-
24. Interest paid from operating activities	024	(3,091)	-	(3,091)
Interest expense		-	(3,091)	3,091
25. Income tax paid	025	-	-	0
A) Net cash flows from operating activities (AOP 001 to 025)	**026**	**72,294**	**(45,144)**	**117,438**

SUPPLEMENTARY REPORT FOR THE CROATIAN NATIONAL BANK (CONTINUED)

Reconciliation of statement of cash flows for 2018

in thousands of HRK

Item		CNB Decision	Annual Report	Difference
Investing activities				
1. Proceeds from sale/payments for purchases of tangible and intangible assets	027	3,140	-	3,140
Decrease/(increase) in property, plant and equipment and intangible assets		-	(1,653)	1,653
Decrease/(increase) in foreclosed assets		-	4,793	(4,793)
2. Proceeds from sale/payments for purchases/investments in subsidiaries, associates and joint ventures	028	-	-	-
3. Proceeds from collection/payments for purchases of/securities and other financial instruments from investing activities	029	-	-	-
4. Dividends received from investing activities	030	-	-	-
. Other proceeds/payments from investing activities	031	-	-	-
Increase/decrease in financial assets at amortised cost		0	(499)	499
Purchase of financial assets at fair value through other comprehensive income		-	(513,513)	513,513
Sale of financial assets at fair value through other comprehensive income		-	631,450	(631,450)
B) Net cash flow from investing activities (AOP 027 to 031)	**032**	**3,140**	**120,578**	**(117,438)**
Financing activities				
1. Net increase/decrease in borrowings from financing activities	033	(49,181)		(49,181)
Repayment of borrowings		-	(139,181)	139,181
New borrowings		-	90,000	(90,000)
2. Net increase/decrease in issued debt securities	034	-	-	-
3. Net increase/decrease in T2 capital instruments	035	-	-	-
4. Share capital increase	036	-	-	-
5. Dividend paid	037	-	-	-
6. Other proceeds/payments from financing activities	038	-	-	-
C) Net cash flows from financing activities (AOP 033 to 038)	**039**	**(49,181)**	**(49,181)**	-
D) Net increase/decrease in cash and cash equivalents (AOP 026+032+039)	**040**	**26,253**	**26,253**	-
Cash and cash equivalents at beginning of year	**041**	**201,420**	**201,420**	-
Effects of foreign currency exchange rate fluctuations on cash and cash equivalents	**042**	-	-	-
Cash and cash equivalents at end of year (AOP 040+041+042)	**043**	**227,673**	**227,673**	-

Mismatches of items in the income statement disclosed in the Annual Report in relation to the structure and contents prescribed in CNB’s decision relate to the following categories:

According to the CNB, impairment losses and provisions are disclosed in one amount within Impairment losses and provisions, while in the Annual Report they are disclosed within Impairment of loans and other assets, Provisions for contingent liabilities, Provisions for legal disputes and Other provisions.

Items Transaction accounts of other customers and Savings deposits of other customers are disclosed separately in the CNB report, while in the Annual Report they are disclosed together within the Increase/(Decrease in demand deposits.

Purchase of financial assets at fair value through OCI and Sale of financial assets at fair value through OCI are disclosed in the Annual Report within Investing activities, while they are disclosed within Securities and other financial instruments at fair value through the OCI within the operating activities in the CNB report.

Reconciliation of the statement of comprehensive income and statement of changes in equity

The Statement of comprehensive income and the Statement of changes in equity prepared under the CNB standard do not differ from the Annual Report.

SUPPLEMENTARY REPORT FOR THE CROATIAN NATIONAL BANK (CONTINUED)

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

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

Ad.1.

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

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

SUPPLEMENTARY REPORT FOR THE CROATIAN NATIONAL BANK (CONTINUED)

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

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

In 2018, Croatia banka performed its activities in the Republic of Croatia.

Ad.2.

In 2018, Croatia banka realised a total net income of HRK 60,888 thousand.

Ad.3.

As at 31 December 2018, Croatia banka had 164 employees based on the number of hours of work, and at the end of 2018 the number of employees was 175.

Ad. 4.

Income tax is based on taxable income for the year and comprises current and deferred tax. The Bank realised a taxable loss for 2018 in total amount HRK 17.995 thousand, and intends to use the tax benefit resulting from this loss in the subsequent years.

The amount reported under income tax relates to net deferred tax assets on prepaid/paid benefits.

Ad.5.

In 2018, Croatia banka did not receive any state subsidies.

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IBAN:	HR0324850031000009027

BUSINESS NETWORK

City	Address	Telephone	Fax
Čakovec Branch	Ulica Ivana Mažuranića 2 40000 Čakovec	040 310 160 040 311 672	040 310 643
Drenovci Branch	Veliki šor 2 32257 Drenovci	032 862 842 032 862 843	032 862 844
Osijek Branch	Ulica Josipa Jurja Strossmayera 4 31000 Osijek	031 203 001 031 203 005	031 203 002
Pula Branch	Istarska ulica 14 52100 Pula	052 451 202 052 451 304	052 451 505
Požega Branch	Cehovska ulica 3 34000 Požega	034 274 460	034 274 440
Slavonski Brod Branch	Trg Ivane Brlić Mažuranić 15 35000 Slavonski Brod	035 442 112	035 442 110
Split Branch	Ulica Domovinskog rata 49A 21000 Split	021 539 795	021 539 794
Vinkovci Branch	Duga ulica b.b. 32100 Vinkovci	032 331 377 032 331 453	032 331 213

City	Address	Telephone	Fax
Virovitica Branch	Trg kralja Zvonimira 10 33000 Virovitica	033 725 441	033 725 602
Vukovar Branch	Josipa Jurja Strossmayera 5 32000 Vukovar	032 450 520	032 450 490
Zagreb Branch	R.F. Mihanovića 9 10110 Zagreb	0800 57 57	01 2391 288
Šubićeva Outlet, Zagreb	Šubićeva 67, 10000 Zagreb	01 4623 024	01 4623 027
Sky Office Outlet	R.F. Mihanovića 9 10110 Zagreb	01 2391 294 01 2391 282	01 2391 240
Županja Branch	Strossmayerova 5 32270 Županja	032 831 051	032 833 424