CROATIA BANKA d.d.

ANNUAL REPORT FOR 2013

CROATIA BANKA d.d.

C O N T E N T

INTRODUCTION

The Annual report includes the Report on the Bank's position, financial overview and overview of operations, audited financial statements with the Independent auditor's report and additional financial statements for the Croatian National Bank.

Legal form

The Annual report was prepared in line with the Accounting Act and the Companies Act which require reporting to the shareholders at the annual meeting of shareholders by the company Management. According to the Companies Act, the main financial statements include the statement of financial position, the income statement, the statement of changes in equity, the cash flow statement and notes to the financial statements, and the Companies Act, in Article 250a, stipulates an obligation to submit an annual report on the Bank's position.

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

Abbreviations

In the 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" and the State Agency for Deposit Insurance and Bank Rehabilitation as the "DAB".

Foreign exchange rate

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

31 December 2013	EUR 1 = HRK 7.637643	USD 1 = HRK 5.549000
31 December 2012	EUR 1 = HRK 7.545624	USD 1 = HRK 5.726794

Operations summary and main financial indicators
(amounts in millions of HRK)

Indicator/Year	2013	2012	2011	2010	2009
Main indicators					
Net loss	(25)	(104)	(14)	(42)	(53)
Total assets	2,629	1,984	1,886	1,892	1,770
Loans and advances to customers	1,630	1,042	980	1,010	1,062
Total deposits received	2,066	1,486	1,348	1,308	1,192
Capital and reserves	195	220	117	126	97

Other indicators					
Ratio of operating expenses in operating income	-111.9%	-129.0%	-100.8%	-121.3%	-108.3%
Regulatory capital	193	218	187	192	167
Capital adequacy	14.0%	17.4%	15.4%	14.5%	10.8%

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 with the social ownership capital paid the amount of the founding fund (the founding principal) of 22,340,435,000 former Yugoslav dinars or DEM 319,149 (which was then the condition for establishing a bank) and the founding fund was then divided into 4,565 founding shares. The Bank obtained the Decision on full authorization on 25 January 1990 by the Yugoslav National Bank, and registered it at the court as of 18 July 1990. As of 4 May 1990, the Bank changed its name from Banka male privrede d.d. Zagreb into Croatia banka male privrede d.d. Zagreb, (short name Croatia banka d.d. Zagreb), and as of 21 June 1995 it changed its name into Croatia banka d.d. Zagreb.

Due to difficulties the Bank had, in 1999, a procedure to rehabilitate the Bank was commenced, and, in line with Article 15 Paragraph 1, Article 16 Paragraph 1, and Article 17 Paragraph 1 of the Bank Rehabilitation and Restructuring Act (Official Gazette No. 44/94), and Point VII of the Decision of the Government of the Republic of Croatia on 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. on 13 September 2000 made a Decision on issuing new substitute shares in the amount of HRK 204.6 million, and the 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 substitute shares, so the Bank continued in operation as a joint-stock company fully owned by the state.

Information on economic trends[1] and forecasts[2]

According to the data of the Croatian Bureau of Statistics, during the fourth quarter of 2013, real GDP dropped by 0.4% compared to the previous quarter, while GDP in the fourth quarter of 2013 fell 1.2% compared to the same quarter of 2012. Unfavourable trends at the end of 2013 were marked by the decrease in real retail turnover, whereby consumer ability of the domestic population was limited by the decrease in the number of employed persons and unfavourable trends in consumer optimism. Also, a decrease in foreign demand for domestic products was recorded, the stagnation of construction activities, a decrease in energy production were recorded, while, on the other hand, the physical volume of industrial production increased due to the growth of nondurable consumer goods and capital goods.

At the end of 2013, conditions in the labour market deteriorated (the number of employed persons was decreasing, and the number of the unemployed was increasing). The number of employed persons fell by 2.4% in the last quarter of 2013, which is the sharpest quarterly fall in the number of employed persons since the beginning of recession. On the other hand, the number of unemployed persons continued to mildly rise during the first nine months of 2013, with the sharp increase in the last quarter, and was, on average, higher by 2.1% compared to the previous quarter. As a result, the unemployment rate also increased, so in the fourth quarter it was on average 20.9% (in the third quarter it was 19.8%).

The annual inflation rate in December 2013 was 0.3%, and was 0.1 percentage point lower compared to the previous month. This very low inflation rate was mainly impacted by decreases in the prices of raw material for the food industry in the global market and the increased competition, especially after the Croatian accession to the European Union which abolished the remaining protective custom duties.

High liquidity of domestic financial system characterised the majority of 2013.

During eleven months of 2013, the central government income was lower by 2.1% compared to the same period of the previous year, while expenses increased by 5.5%. The decrease in income was mainly impacted by the decrease in income from income tax, VAT and social contributions, while the expenses increased due to the increase in expenses for social benefits, expenses for pensions and healthcare and interest expense and contributions related to the EU membership.

In 2014, a mild increase in economic activities, ranging from 0.5% to 1.0% is expected, impacted primarily by more dynamic export and increase in investments. It is expected that the government spending will decrease following the initiation of the excessive deficit procedure due to the violation of the Stability and Growth Pact rules, whereby Croatia will have to decrease the structural balance to the level of 3% in the following years.

Considering the expected low economic growth rate, only mild improvements of conditions in the labour market can be expected, but the level of the survey unemployment rate will remain high.
Further decline in the prices of raw material for food industry will largely impact further decrease in the inflation rate, which is estimated at the rate of 1.3% in 2014.

In 1014, it is expected that the current and capital account balances will improve, primarily due to relatively favourable trends in the international trade of goods and services, stimulated by the recovery of foreign demand. Also, the increase in net transfers from the EU budget is expected. It is estimated that the export of goods and services will intensify in the following period under the influence of the gradual recovery of demand by the main foreign trading partners and favourable impacts of the EU accession.

In the conditions of slow economic growth in the eurozone, compared to the USA, the US dollar will gradually strengthen against the Euro.

[1] *Information on economic trends, Croatian National bank, February 2014*
[2] *Information on economic trends and forecasts, Croatian national Bank, December 2013*

During 2014, a moderate improvement in the conditions of financing domestic sectors is expected, but they will remain under the influence of the movement in risk premium paid on foreign debt. As a result, a moderate recovery of credit institutions placements is expected, so it could grow at a rate of 1-2%.
The profit of credit institutions in 2014 will be negatively impacted by the amendments to the Consumer Credit Act and regulatory requirements under which credit institutions have to more actively test the value of collaterals for granted loans or increase the provisions for bad debt if the value of collaterals is not tested.

After the period of the decreasing foreign direct investments, in the following period a gradual recovery of foreign direct investment inflow is expected. This could be mainly impacted by the intensification of privatisation projects, the positive impact of the full membership in the EU on the perception of Croatia among foreign investors and an improvement of the investment climate in the country.

The CNB's monetary policy in 2014 will continue to support the stability of the domestic currency exchange rate against EUR and the continued policy of high primary liquidity. A significant growth in monetary and credit aggregates may be expected only in conditions of a significant recovery of the total economic activity.

Description of operations

The Bank's activities include all types of deposit and credit activities 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.

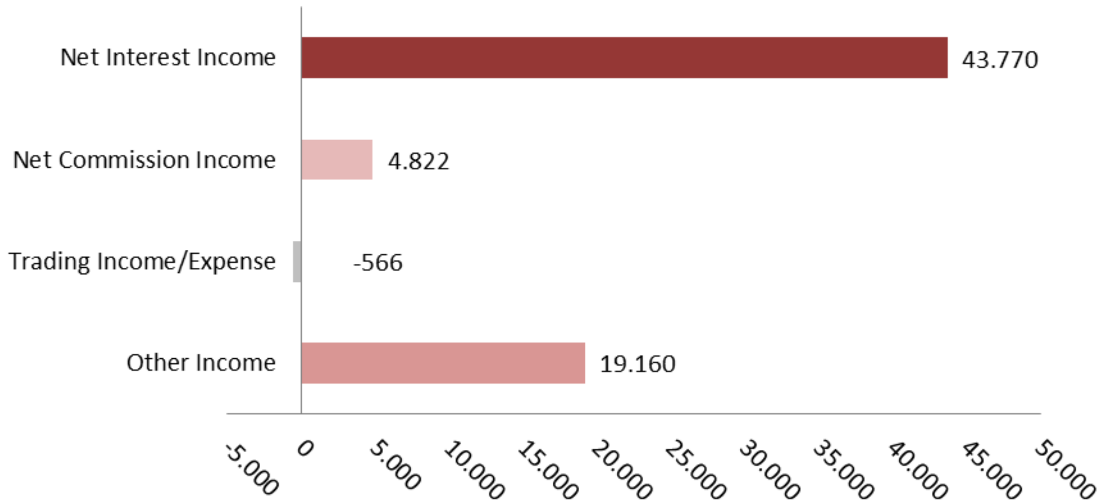
The Bank is 100% owned by the state, and according to the amount of assets (HRK 2.6 billion) it takes 14th position of the total of 30 banks. As at 31 December 2013, the Bank has 17 branches and 3 bureaus.

As at 31 December 2013, the regulatory capital amounts to HRK 192.9 million, and the regulatory capital adequacy rate is 14.0%

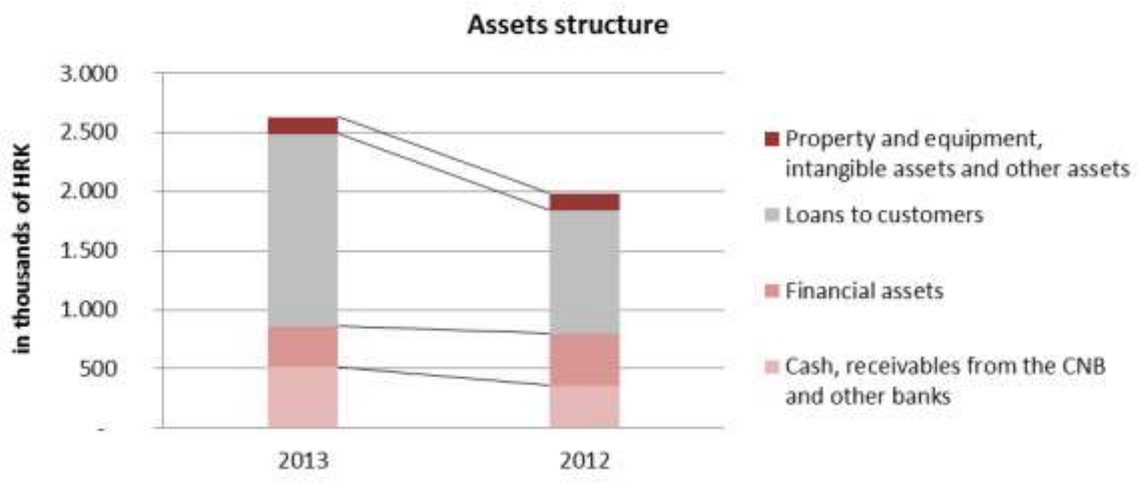
In 2013, the Bank realised loss before and after tax in the amount of HRK 24.6 million. Operating loss amounts to HRK 8 million, and impairment costs and provisions to HRK 16.6 million.

Total operating income increased by 22.8 percent compared to 2012. The most significant portion of operating income is net interest income which makes 65.1 percent (HRK 43.8 million) of the total income.

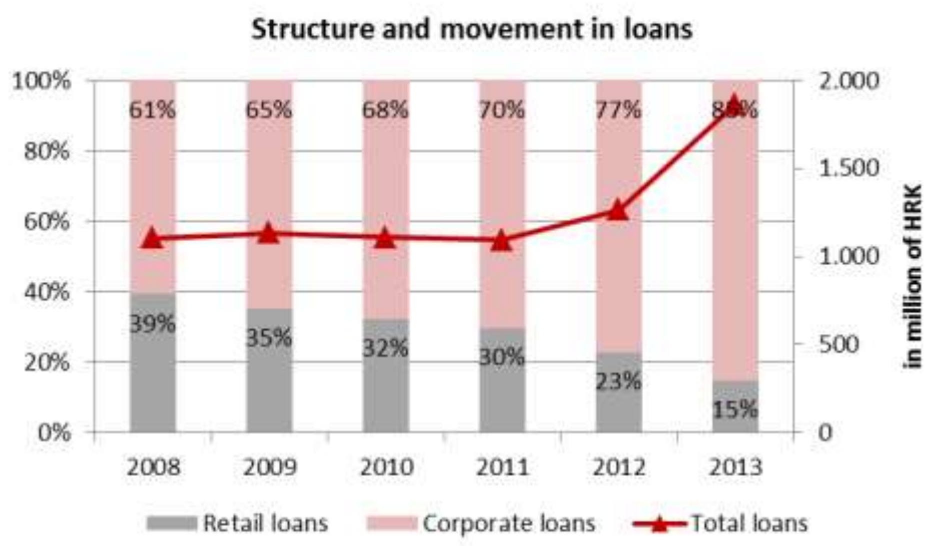
Structure of operating income for the period from 1 January 2013 to 31 December 2013



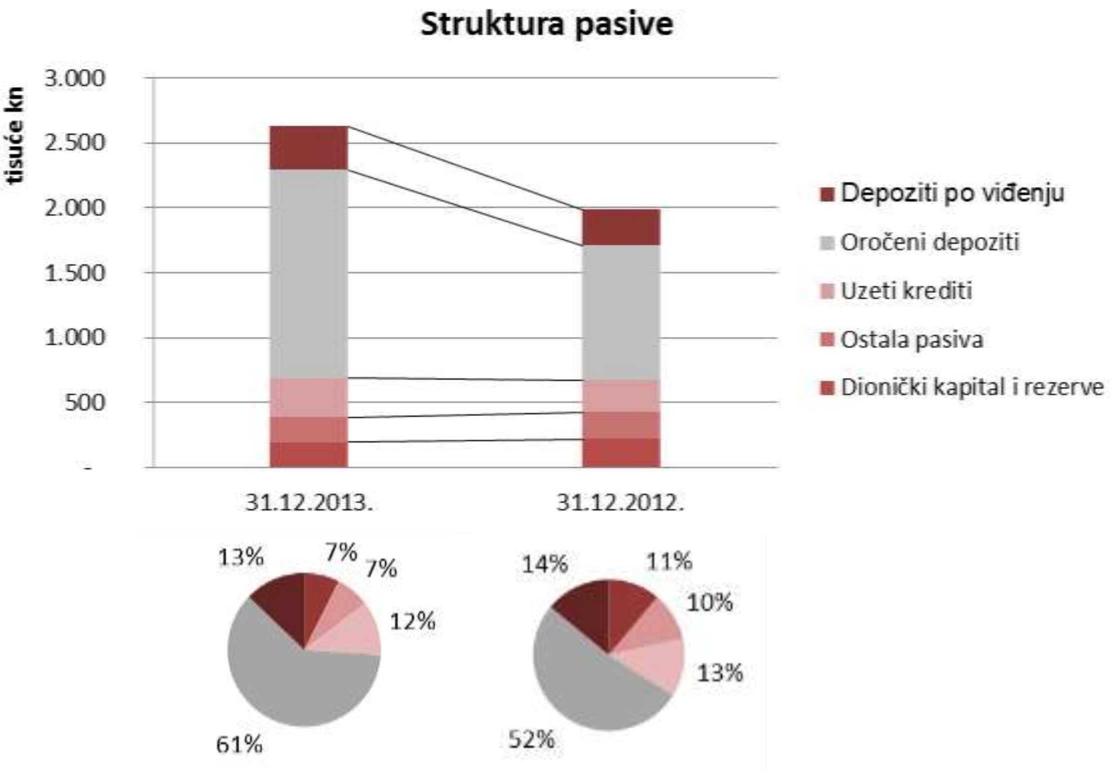
At the end of 2013, the Bank's assets amounted to HRK 2,628.6 million and increased by HRK 644.4 million or 32.5 percent compared to 2012. In the assets structure, the greatest share make loans and receivables from customers (62.0 percent), followed by cash funds, receivables from the Croatian National Bank and other banks (20.0%) and financial assets (13.0 percent).



As at 31 December 2013, the total gross loans to customers amounted to HRK 1,861.6 million and increased by 47.4 percent compared to 2012. In the structure of loans to customers, 85 percent make loans to legal persons, and 15 percent loans to individuals (including loans to craftsmen).

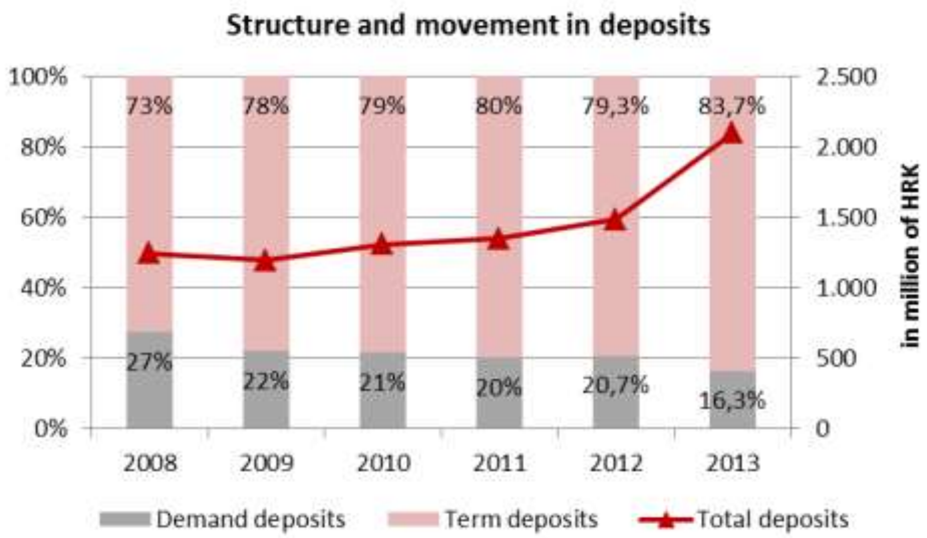


In the liability structure, the most significant share of 61 percent make term deposits. They are followed by deposits held at call with 13 percent.



Customer deposits recorded an increase compared to the end of 2012 by 48.1 percent, and the growth in total deposits (including deposits of banks) was 39.0 percent and at the end of 2013, they amounted to HRK 2.1 billion.

In the total deposit structure, the greatest share have term deposits (83.7 percent) compared to deposits held at call (16.3 percent). Term deposits increased by 51.9 percent, and their share in the total deposit structure increased by 4.4 percentage points. In 2013, deposits held at call increased by 10.9 percent.



Operations with individuals

In the field of operations with individuals, in 2013 the Bank focused its activities on the improvement and development of the existing loan models, as well as on the development of new credit products, improvement of Internet banking services and all other activities related to this operating segment. The number of open current accounts and the amount of placements was increased several times compared to the previous year.

However, unfavourable economic trends, over-indebtedness of citizens and fear of further debt impacted the slower growth of credit activities compared to the plan, while deposit activities were exceptional, which enabled the record growth of deposits by individuals.

In the total deposit structure, deposits of individuals make 57.0 percent and increased compared to the previous year by 48.5%, and amount to HRK 1,178.0 million. Of this, deposits held at call amount to HRK 101.7 million, and term deposits to HRK 1,076.3 million.

The total gross credit portfolio of individuals (including craftsmen) at the end of 2013 amounted to HRK 275.3 million, and in the total credit portfolio, it makes 14.8 percent.

In the structure of total loans to individuals, the greatest share have cash loans, then used revolving loans on current accounts and housing loans that mainly relate to loans to employees.

Operations with legal persons

Deposits of legal persons (excluding deposits of banks) make 35.5 percent of the Bank's total deposits. Compared to the end of 2012, deposits of legal persons record an increase of 47.4 percent and amount to HRK 733.6 million. Of this, deposits held at call amount to HRK 236.5 million, and term deposits to HRK 497.1 million and they increased by 55.2 percent.

At the end of 2013, the total gross credit portfolio of legal persons amounted to HRK 1,586.3 million, which is an increase by HRK 611.6 million, or 62.8 percent compared to end of 2012.

In 2013, market activity in operations with legal persons increased significantly. Implemented acquisition campaigns resulted in an increase in the number of clients, especially companies owned by the state and local government units. These mainly contributed to the strengthening of the deposit base and to the growth in credit portfolio with first-class collaterals. The quality of business processes was improved, especially of the credit process, which resulted in an improved efficiency and increased level of the service quality.

Treasury operations
The Bank maintains liquidity with available instruments of HRK and foreign currency liquidity (funds in Bank's accounts, securities, inter-bank loans and repurchase and collateral loans), and it does not use more advanced instruments, such as different types of derivatives.

In managing operating liquidity, internal methodology has been developed for reporting on daily liquidity needs. In addition, internal methodology has been established for managing position foreign exchange differences for the purpose of decreasing and/or eliminating the impact of foreign exchange losses.

In its efforts to increase the activities of sale of products with risk, and establish a better communication and contact with clients, the Bank introduced and elaborated the internal methodology of foreign currency trading with the Bank's clients (Customer Desk). This way, direct contact with a portion of clients was established, with the aim to present the possibilities of transactions of purchasing and selling foreign currency, and the invitation for cooperation was sent with the presentation of advantages the Bank offers at its Customer Desk. As support to sales activities, the possibilities and direct contacts of the Treasury have been published on the Bank's official website.

In the previous year, the Treasury increased the volumes and number of transactions for all products and thereby actively accepted the role of the bank's profit centre.

Investment banking operations
The Bank has obtained all permits from the Croatian National Bank and the Croatian Financial Services Supervisory Agency for providing investment services and activities, and has ensured all preconditions for providing investment services. In the field of investment banking, the Bank offers to its clients the activities of mediation in purchase and sale of financial instruments, and activities of custody over client's financial assets, margin loans for the purchase of financial instruments, and cash S-loans with collaterals of financial instruments in the bank's custody.

Despite unfavourable situation in the Croatian financial market, marked by low turnovers, and low activity of investors, the Bank achieved positive results in the field of investment banking. In the last year, the client base was significantly extended, and the turnover on the Zagreb Stock Exchange increased several times. In the following period, the Bank will offer to its clients the Internet trading service and the service of a depository bank for institutional clients, which should ultimately result in an additional improvement in the result in this field.

Development plan

In 2014, the Bank will continue the activities of consolidation of operations, moderate growth, improvement in the internal controls system and cost rationalisation with the ultimate goal of positive operations.

Taking into account the need to continue in operation and uncertainty related to the application of new regulatory regulations related to the capital adequacy, the Bank is considering possibilities to increase the total capital, which were presented to the Bank's Supervisory Board.

The increase in credit activities will be determined by the increase in deposits, as the primary source of Bank's funds. In addition to deposits, the Bank will increase its source structure by the continuous cooperation with the CBRD.

Although significantly less than in the previous year, the greatest portion of credit activities will continue to be focused on crediting large companies and public government bodies, and with respect to SMEs, programmes of crediting agriculture will be specially supported. On the other hand, the development of operations with individuals should record higher growth rates aimed at increasing the base of individually small placements.

The Bank will systematically improve the risk management system, the system of collecting uncollected receivables, it will continually work on the improvement in the image, corporate culture and safety, introduce new and redesign the existing products with the aim to increase sales and the number of clients, it will carry out activities of the rational management of the network of branches and bureaus and extend distribution sale channels (introducing mobile banking, telephone banking, POS devices, improving Internet banking etc.).

At the level of the total assets, care will continually be taken of ensuring funds for maintaining the Bank's liquidity in line with legal provisions, CNB's decisions and internal acts.

During the next financial year, it is planned to sell a portion of assets foreclosed in exchange for uncollected receivables.

By the planned significant increase in operating income on one hand, and the decrease in expenses on the other, the Bank would end 2014 with operating profit and profit from operations. Simultaneously, additional provision costs for the existing loan portfolio are planned, as well as impairment costs on a collective basis due to the increase in gross loan portfolio.

Internal controls system and internal audit

The internal controls system is established at the Bank's level by internal acts that vertically and horizontally divide responsibilities among the Bank's organisational units.

The internal controls system in the Bank is established as a set of processes and procedures established for an adequate risk control, monitoring the efficiency and effectiveness of the Bank's operations, reliability of its financial and other information, and compliance with regulations, internal acts, standards and codes for the purpose of ensuring stability of the Bank's operations.

Internal audit

The internal audit function is organised as a separate organisational part, functionally and organisationally independent of activities it audits and other organisational parts of the Bank.

The annual audit plan is based on the documented risk assessment, and it contains all the elements prescribed by the Credit Institutions Act and internal acts. The annual work plan of the internal audit is approved by the Bank's Management Board with previous opinion of the Audit Committee and consent of the Supervisory Board.

Report on the results of the performed audit is delivered to responsible persons of the Bank's organisational part responsible for the audited business areas, the member of the Management Board responsible for the audited business area and the Audit Committee.

Internal audit prepares and submits to the Management Boards and the Audit Committee quarterly, to the Supervisory Board semi-annual, and to the CNB annual reports on its work.

Statement on the corporate management code application
In accordance with the provisions of Paragraph 272.p of the Companies Act, the Management Board of Croatia banka d.d. Zagreb states that the Bank in its operations voluntarily applies the Positions of the Croatian National Bank on corporate management in banks.

In 2013, the Bank mainly followed and applied the recommendations determined by the CNB's Positions, disclosing all information the disclosure of which is foreseen by the effective regulations and information that is in the interest of the Bank's owners and clients.

In accordance with the corporate management requirements, and in line with the provisions of the Companies Act, the Supervisory Board carries out the internal supervision 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 competence of this Body 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 effective laws and regulations.
Corporate management is conducted in the Bank not only by meeting regulatory requirements, but it also arises from the culture of corporate and personal integrity of management and employees. The description of main characteristics in carrying out internal supervision and risk management in relation to financial reporting are contained in this Annual report.
Candidates for the president and members of the Bank's Management Board must meet all conditions prescribed by law that regulates the operations of banks and other relevant regulations. After obtaining preliminary approval of the central bank, the Supervisory Board appoints the president and members of the Board for a period of maximum four years. The competences of the Bank's Board are defined by law and the Statute. A special decision, adopted with the consent of the Supervisory Board, determines the division of responsibilities of the president and other members of the Management Board.

Decisions on amendments to the Statute are adopted at the Bank's General Assembly, in line with the Law 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 fully adjust its operations with the highest standards of corporate management.

Bank's management structure
In accordance with the Companies Act, the Credit Institutions Act and the Bank's Statute, the Bank's management structure comprise the Supervisory and Management Boards, and these acts also regulate the duties and responsibilities of the Supervisory and Management Boards.

Significant events after the end of the business year
In accordance with the CNB's decision of 6 August 2013, the Bank appointed another authorised auditor who re-audited the Bank's financial statements for 2012 and performed the audit for the CNB's purposes for 2012. Consequently, as of 30 January 2014, the previously issued financial statements for 2012 were withdrawn, and the new financial statements for 2012 were issued.
As at 30 December 2013, the new Credit Institutions Act was issued, effective as of 1 January 2014, based on the Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013, effective in all European Union countries.

Other information
The Bank did not carry out any research and development activities during 2013.
The Bank did not purchase any treasury shares during 2013.
The Bank does not own other legal entities.
Purchase and sale of financial instruments is an integral part of the Bank's operations, described in detail in these financial statements.
The Bank's goals and policies related to financial risk management, and the company's exposure to price risk, credit risk, liquidity risk and cash flow risk are described in detail in the financial statements.

RESPONSIBILITY FOR THE FINANCIAL STATEMENTS FOR 2013

The Management Board of the Bank is required to prepare financial statements for each financial year, which give a true and fair view of the financial position of the Bank, results of operations and cash flow, in accordance with applicable accounting standards and is responsible for maintaining proper accounting records to enable the preparation of such financial statements at any time. It has a general responsibility for taking such steps as are reasonably available to it to safeguard the assets of the Bank and to prevent and detect fraud and other irregularities.

The Management Board is responsible for selecting suitable accounting policies to conform with applicable accounting standards and then apply them consistently; making judgements and estimates that are reasonable and prudent; and preparing the financial statements on a going concern basis unless it is inappropriate to presume that the Bank will continue in business.

The Management Board is responsible for the submission of the annual report, including the annual financial statements to the Supervisory Board for their review. If the Supervisory Board agrees with the annual financial statements they are considered as confirmed by the Management Board and Supervisory Board.

The financial statements for 2013 set out on pages 19 to 96 as well as the schedules prepared in accordance with the Decision of the Croatian National Bank on the Structure and Content of the Annual Financial Statements of Banks, dated 30 May 2008 (Official Gazette 62/08) were authorised by the Management Board on 11 April 2014 for issue to the Supervisory Board.

As an acknowledgment, financial statements are signed by the authorized persons as follows

For and on behalf of Croatia banka d.d.

Suzana Brenko
President of the Management Board

CROATIA BANKA
d.d. Zagreb
UPRAVA

Stjepan Mandic
Member of the Management Board

Independent Auditor's Report

To the Shareholders and Management of Croatia banka d.d.

We have audited the accompanying financial statements of Croatia banka d.d., Zagreb (the "Bank"), which comprise the statement of financial position as at 31 December 2013 and the statements of comprehensive income, changes in equity and cash flows for the year then ended and notes comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with statutory accounting requirements for banks in the Republic of Croatia as set out in Note 3 – 'Basis for presentation of financial statements', and for such internal control as Management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

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T: +385 (1) 6328 888, F:+385 (1) 6111 556, www.pwc.hr

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2013, and its financial performance and its cash flows for the year then ended in accordance with statutory accounting requirements for banks in the Republic of Croatia as set out in Note 3 – 'Basis for presentation of financial statements'.

Other Legal and Regulatory Requirements

Pursuant to the Decision of the Croatian National Bank on the Structure and Content of the Annual Financial Statements of Banks (Official Gazette 62/08, hereinafter: the "Decision"), the Management Board of the Bank has prepared the schedules set out on pages 97 to 109, which comprise the balance sheet of the Bank as at 31 December 2013, the income statement, the statement of changes in equity and the cash flow statement of the Bank for the year then ended together with information on the reconciliation with the Bank's financial statements. The Management Board of the Bank is responsible for the preparation of these schedules and the reconciliation, which do not form an integral part of these financial statements but contain information prescribed by the Decision. The financial information in the schedules is derived from the Bank's financial statements that have been prepared in accordance with the statutory accounting requirements for banks in the Republic of Croatia as set out in Note 3 – 'Basis for presentation of financial statements' set out on pages 19 to 96 and adjusted in accordance with the Decision.

In addition, we have read the accompanying Annual Report of the Bank for the year ended 31 December 2013 set out on pages 3 to 15. We have verified that the information included in the Annual Report which describes matters that are also presented in the financial statements is consistent, in all material respects, with the financial statements referred to above.

PricewaterhouseCoopers d.o.o.

PricewaterhouseCoopers d.o.o.
Zagreb, 29 April 2014

in thousands of HRK

	Note	**2013**	**2012**
Interest income	*5*	112,894	91,519
Interest expense	*6*	(69,124)	(52,523)
Net interest income		**43,770**	**38,996**
Fee and commission income	*7*	9,803	10,146
Fee and commission expense	*8*	(4,981)	(4,652)
Net fee and commission income		**4,822**	**5,494**
Net expense from financial operations	*9*	(566)	(1,291)
Net income from foreign exchange differences	*10*	4,333	4,272
Other income from operating activities	*11*	14,827	7,220
Total other income		**18,594**	**10,201**
Other operating expenses	*12*	(75,187)	(70,570)
Impairment losses and provisions	*13*	(16,643)	(110,483)
Total other expenses		**(91,830)**	**(181,053)**
Loss before tax		**(24,644)**	**(126,362)**
Income tax	*14*	**-**	**22,761**
Loss for the year		**(24,644)**	**(103,601)**
Unrealised (losses)/gains from the valuation of financial assets available for sale		(183)	6,855
TOTAL COMPREHENSIVE LOSS		**(24,827)**	**(96,746)**
Earnings per share	*33*	**(5)**	**(22)**

Significant accounting policies and other notes on pages 23 to 96 form an integral part of these financial statements.

in thousands of HRK

	Notes	**31 December 2013**	**31 December 2012**
ASSETS			
Cash	*15*	266,877	90,710
Receivables from the Croatian National Bank	*16*	192,094	129,232
Placements with banks	*17*	57,497	138,807
Financial assets held for trading	*18*	5,081	-
Financial assets available for sale	*19*	333,495	436,949
Financial assets held to maturity	*20*	2,149	2,542
Loans and advances to customers	*21*	1,629,818	1,041,835
Investment property	*22*	36,095	36,095
Property and equipment	*23*	20,921	21,389
Intangible assets	*23*	2,715	3,174
Foreclosed assets	*24*	25,810	24,151
Deferred tax assets	*14*	22,761	22,761
Other assets	*25*	33,240	36,492
Total assets		**2,628,553**	**1,984,137**
LIABILITIES			
Liabilities to banks	*26*	154,412	174,430
Demand deposits	*27*	338,204	277,591
Term deposits	*28*	1,604,622	1,034,171
Borrowings	*29*	301,647	246,400
Other liabilities	*30*	21,734	19,886
Provisions	*31*	12,709	11,607
Total liabilities		**2,433,328**	**1,764,085**
EQUITY			
Share capital	*32*	474,600	474,600
Accumulated losses		(256,315)	(152,714)
Reserves		1,584	1,767
Loss for the year		(24,644)	(103,601)
Total equity		**195,225**	**220,052**
Total liabilities and equity		**2,628,553**	**1,984,137**

Significant accounting policies and other notes on pages 23 to 96 form an integral part of these financial statements.

CROATIA BANKA d.d.
STATEMENT OF CHANGES IN EQUITY
for 2013

in thousands of HRK

	Share capital	Accumulated losses	Reserves	Loss for the year	Total
Balance at 1 January 2012	**274,600**	**(138,785)**	**(4,818)**	**(13,929)**	**117,068**
Changes in equity in 2012					
Transfer of accumulated losses	-	(13,929)	-	13,929	-
Unrealised change in fair value of available-for-sale financial assets	-	-	6,585	-	6,585
Net income recognised directly in equity	-	-	*6,585*	-	*6,585*
Loss for the year	-	-	-	(103,601)	(103,601)
Increase in share capital	200,000	-	-	-	200,000
Balance at 31 December 2012	**474,600**	**(152,714)**	**1,767**	**(103,601)**	**220,052**
Balance at 1 January 2013	**474,600**	**(152,714)**	**1,767**	**(103,601)**	**220,052**
Changes in equity in 2013					
Transfer of accumulated losses	-	(103,601)		103,601	-
Unrealised change in fair value of available-for-sale financial assets	-	-	(183)	-	(183)
Net loss recognised directly in equity	-	-	*(183)*	-	*(183)*
Loss for the year	-			(24,644)	(24,644)
Balance at 31 December 2013	**474,600**	**(256,315)**	**1,584**	**(24,644)**	**195,225**

Significant accounting policies and other notes on pages 23 to 96 form an integral part of these financial statements.

	2013	2012
		in thousands of HRK
NET CASH FLOW FROM OPERATING ACTIVITIES		
Loss before tax	**(24,644)**	**(126,362)**
Adjustment to net cash from operating activities		
Impairment allowance on loans and other assets (net)	15,154	110,483
Provisions for potential liabilities (net)	543	2,209
Provision for litigation (net)	(678)	360
Other provisions (net)	1,237	-
Loss on realisation of available-for-sale financial assets (Note 9)	566	1,291
Amortization and depreciation (Note 23)	4,484	5,562
Foreign exchange differences on translation	163	309
Gains on sale of tangible assets	(5,594)	(1,134)
Write-offs of tangible assets	82	17
Changes in assets and liabilities from operating activities		
Decrease/(increase) in receivables from the Croatian National Bank	(63,497)	8,158
Increase in loans and advances to customers	(597,473)	(174,254)
Decrease/(increase) in other assets	2,522	(7,258)
Increase/(decrease) in liabilities to banks	(20,018)	114,702
Increase in demand deposits	60,613	23,891
Increase/(decrease) in term deposits	563,317	(1,045)
Increase/(decrease) in other liabilities	1,848	(47,067)
Net cash flow from operating activities	**(61,375)**	**(90,138)**
CASH FLOW FROM INVESTING ACTIVITIES		
Sale of available-for-sale financial assets	102,705	-
Purchase of available-for-sale financial assets	-	(155,085)
Purchase of financial assets held for trading	(5,081)	-
Collection of held-to-maturity financial assets	397	7,265
Purchase of property, equipment and intangible assets	(3,692)	(2,698)
Sale of tangible assets	7,602	7,577
Net cash flow from investing activities	**101,931**	**(142,941)**
CASH FLOW FROM FINANCING ACTIVITIES		
Borrowings received	55,247	-
Borrowings settled	-	(29,352)
Increase in share capital	-	130,000
Net cash flow from financing activities	**55,247**	**100,648**
Net change in cash and cash equivalents	**95,803**	**(132,431)**
Cash and cash equivalents at beginning of the year (Note 36)	**231,577**	**364,008**
Cash and cash equivalents at end of the year (Note 36)	**327,380**	**231,577**

Significant accounting policies and other notes on pages 23 to 96 form an integral part of these financial statements.

1. GENERAL INFORMATION ABOUT THE BANK

Legal framework and activities

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

The Bank is engaged in all types of deposit and credit related services to legal entities and individuals, domestic and international payments, guarantees, avals and other forms of guarantees, securities trading and other banking activities.

The Bank has 17 branches – Branch Zagreb, Branch Bjelovar, Branch Čakovec, Branch Đakovo, Branch Metković, Branch Osijek, Branch Petrinja, Branch Poreč, Branch Požega, Branch Rijeka, Branch Slavonski Brod, Branch Split, Branch Vinkovci, Branch Virovitica, Branch Vukovar, Branch Zadar, Branch Županja, and 3 bureaus; Bureau Šubićeva, Bureau Ploče and Bureau Drenovci.

Bank's Bodies

Supervisory Board

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 Management'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, policy of salaries and other benefits, organisational structure of the Bank, and it also decides on other issues as determined by law or Bank's internal acts.

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

The Supervisory Board generally holds meetings once a month or in shorter time intervals, as required.

During 2013, the members of the Supervisory Board were:

Marija Hrebac – President

Branka Grabovac – Deputy President

Ivan Tomljenović – Member

Mladen Duliba – Member (from 10 April 2013)

Stanko Kršlović – Member (until 09 April 2013)

Alen Kišić – Member (until 13 June 2013)

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.

The Management Board's main responsibility is conducting the Bank's operations and representing the Bank toward third parties. In addition, the Management Board is responsible for ensuring that the Bank operates in accordance with the rules on risk management pursuant to the Credit Institutions Act and other regulations that govern banking operations and the provision of other financial services and regulations adopted on the basis of law and Bank's general acts; 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 in accordance with the Credit Institutions Act, and acts adopted in line with the Act; ensuring functioning of the internal controls system for all areas of the Bank's operations; ensuring unobstructed internal audit; ensuring that the Bank keeps business and other records and business documentation, prepares accounting documents, realistically estimates assets and liabilities, prepares financial and other reports in accordance with accounting regulations and standards and the Credit Institutions Act and other regulations adopted on the basis of law; ensuring that the Bank reports and informs the Croatian National Bank in line with the Credit Institutions Act and other regulations adopted on the basis of law; and ensuring the implementation of measures ordered by the Croatian National Bank.

The Bank's Management Board had not less than two and not more than three members, of which one is appointed as the President of the Management Board. The President of the Management Board represents the Bank jointly and severally, and a member of the Management Board together with another member of the Management Board.

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

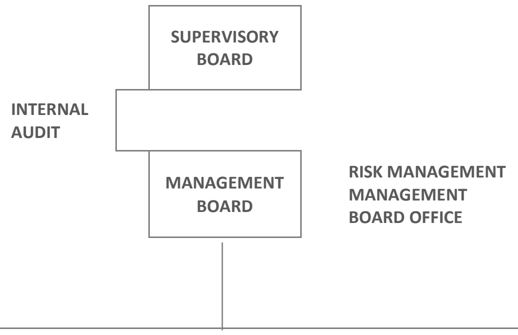
Members of the Board who have performed their functions during the year were:

Suzana Brenko – President

Stjepan Mandić – Member

Jasminka Gregurić Matić – Member

Organisational structure



OPERATIONS WITH LEGAL PERSONS	OPERATIONS WITH INDIVIDUALS	FINANCIAL MARKETS	FINANCES	CREDIT ADMINISTRATION, LEGAL AFFAIRS AND COMPLIANCE	BANK'S CORPORATE FUNCTIONS	OPERATIONS AND INFORMATION TECHNOLOGIES
Sale management	Sale management	Treasury	Controlling and reporting	Administration of loans and deposits	Corporate communication	Payment transactions
Product development	Product development	Investment banking	Accounting	Legal affairs	Human resources management	Information technologies
Management of placements with risk					General affairs	

BUSINESS NETWORK

2. GOING CONCERN

Effect of capital contribution and new business strategy:

The Bank has not managed to achieve profits from operating activities for a several years, therefore the owner increased the share capital of the Bank on several occasions, the latest being in October 2012 in the amount of HRK 200 million, consisting of conversion of issued bonds into equity that fully represented a hybrid instrument i.e. additional capital in the amount of HRK 70 million, and payment in the amount of HRK 130 million.

In 2013, the Bank mainly focused its credit activity on crediting the state and legal entities owned by the state with guarantees of the Republic of Croatia for which, in line with effective regulations, capital requirements do not need to be made, and they yield a satisfactory interest income. As for the funds sources, the Bank realised a significant increase in total deposits (especially deposits by individuals) which ensure funds sources for credit activities. Management believes that in this way, in addition to decreasing operating expenses, they will achieve positive result already in 2014.

The effect of the financial crisis:

Conditions in global financial markets and the impact on Republic of Croatia

Global financial markets, particularly in Europe, continued to be marked with a lack of confidence in public finances in some Eurozone countries during 2013 The global uncertainty in the financial markets expanded to the entire European "emerging markets", including Croatia. During 2013, credit rating of Croatia was decreased from BB+ to BB.

We believe that the economy competitiveness continues to be low, among other things, due to the rigidity of the labour market and complex business environment" Standard & Poor's states in its explanation.

Unemployment is still rising, inflation mildly grows, GDP is still in the negative indicator, and uncertainty continues to be one of the main characteristics of the business environment, as well as reduced activity in the domestic securities market.

In the banking sector, a further decline in quality of loans is present, with new regulatory rules on classification which at the end of 2013 led to a significant growth in impairment costs. The fact that banks continue with the rationalisation of operations and lower interest expenses support their operating performance, but the main problem remains to be a decrease in interest income in the period when impairment costs rise. Savings on operating expenses continue, but their effects are limited by decreasing yields and they do not provide sufficient space for a stronger effect on earnings.[2]

Effect on liquidity

Despite the crisis, the Bank has sufficient liquidity throughout 2013, and in particular after increase of share capital.

[2] *Financial stability, No. 12/year 7/ II 2014, Croatian National Bank*

Impact on customers

Impairment losses are monitored for each customer, based on the type of the receivables. Exposures to related party groups are also monitored. The Bank assess the adequacy of all collaterals on an individual or group basis, however the market value of properties taken as collateral is difficult to assess with reasonable certainty, considering the current difficulties and comparatively inactive markets. Although the final impact of the financial crisis cannot be predicted, including its duration and inability to protect from it, the Bank has invested additional efforts and increased its activities in monitoring of quality of the existing portfolio of customers during 2013

Taking into consideration all of the above, Management believes that the Bank will be able to meet its obligations in the future, and it is therefore appropriate to prepare the financial statements on the going concern basis.

3. BASIS FOR PREPARATION OF FINANCIAL STATEMENTS

Statement of compliance:

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

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

Attention is drawn to the following differences between the accounting regulations of the CNB and recognition and measurement requirements of IFRS:

- The CNB requires banks to recognise impairment losses in the income statement on assets not identified as impaired on individual basis (including assets with sovereign risk) at prescribed rates (excluding financial assets carried at fair value through profit and loss and available for sale). As at 31 December 2013, the provisions on a collective basis amounting to HRK 19,027 thousand (2012: HRK 12,293 thousand) are presented in the Bank's balance sheet in line with the CNB requirements, and on the basis of the CNB regulation, the expense for the Bank was recognised on the basis of these provisions within impairment losses for the year.
- Additional difference between IFRS and the accounting regulations of the CNB relates to the calculation of impairment losses by discounting the expected cash flows of the impaired asset at the instrument's original effective interest rate. Bank calculates impairment losses for individually significant items by estimating the future cash flows, and discounting them with original effective interest rate. Amortization of such discounts is recognised as a decrease in provision. However, in some cases, collections are recognized as interest income only at the moment of reversal of impairment, in the full amount.
- Additionally, the CNB prescribes minimum level of provisions for impairment losses for certain specific exposures, which may be different from the impairment loss required to be recognised in accordance with IFRS.

Basis of measurement:

The financial statements are prepared on the fair value basis for financial assets available for sale, 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 recognised at amortised or historical cost.

Use of estimates and judgments:

The preparation of financial statements requires management to make judgments, estimates and assumptions that affect the application of policies and the reported amounts of assets and liabilities and disclosure of contingent liabilities at balance sheet date, as well as the reported amounts of revenues and expenses for the period. The estimates and associated assumptions are based on historical experience and various other factors which are believed to be reasonable under the circumstances, and information available at the date of preparation of financial statements, result of which makes the basis for the judgments about carrying values of assets and liabilities which is not directly apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed regularly. Changes in accounting estimates are recognized in the period in which they arise if they affect only that period, or the period in which they are incurred and future periods, if they affect both current and future periods.

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 at 31 December, 2013 was HRK 7.637643 per EUR 1 (2012: HRK 7.545624) and HRK 5.549000 per USD 1 (2012: HRK 5.726794).

Standards, interpretations and amendments to published standards not yet effective

Certain regulations have been issued by the HNB at the time these statements were authorized for issue, but are not yet effective at the balance sheet date, but it will be mandatory for accounting periods that begin as at 1 January 2013 or later. The Bank considers that the following regulations could have a significant impact on the financial statements or a significant financial impact on its operations:

Adoption of new and revised International Financial Reporting Standards

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

The Bank has adopted the following new and amended IFRS and IFRIC interpretations during the year which were endorsed by the EU. When the adoption of the standard or interpretation is deemed to have an impact on the financial statements or performance of the Bank, its impact is described below.

Amendment to IAS 1 Financial Statement Presentation Regarding Other Comprehensive Income (effective for annual periods beginning on or after 1 July 2012)

The main change resulting from these amendments is a requirement for entities to group items presented in other comprehensive income (“OCI”) on the basis of whether they are potentially reclassifiable to comprehensive income subsequently (reclassification adjustments). The amendments do not address which items are presented in OCI. The amendment affects presentation only and therefore did not have an impact on the Bank’s financial position or performance.

AS 19 Employee Benefits (revised 2011) and Amendment to IAS 19 (effective for annual periods beginning on or after 1 January 2013)

These amendments eliminate the corridor approach and calculate finance costs on a net funding basis. IAS 19 Employee benefits was revised in June 2011. The revised employee benefit standard introduces changes to the recognition, measurement, presentation and disclosure of post-employment benefits. This amendment did not have an impact on these financial statements.

Amendment to IFRS 1 First Time Adoption on Government Loans (effective for annual periods beginning on or after 1 January 2013)

This amendment addresses how a first-time adopter would account for a government loan with a below-market rate of interest when transitioning to IFRS. This amendment is not relevant, because the Bank is not a first-time adopter or user of government loans.

Amendment to IFRS 7 Financial Instruments: Disclosures on Asset and Liability Offsetting (effective for annual periods beginning on or after 1 January 2013)

This amendment includes new disclosures to facilitate comparison between those entities that prepare IFRS financial statements to those that prepare financial statements in accordance with US GAAP.

IFRS 13 Fair Value Measurement (effective for annual periods beginning on or after 1 January 2013)

IFRS 13 aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across IFRSs. The requirements, which are largely aligned between IFRS and US GAAP, do not extend the use of fair value accounting but provide guidance on how it should be applied where its use is already required or permitted by other standards within IFRSs or US GAAP. The impact of IFRS 13 on the financial statements of the Bank is described in Note 1.2 (d).

IFRIC 20 Stripping Costs in the Production Phase of a Surface Mine (effective for annual periods beginning on or after 1 January 2013)

This interpretation sets out the accounting for overburden waste removal (stripping) costs in the production phase of a mine. This interpretation is not relevant to the Bank's operations.

Annual improvements 2011 (effective for annual periods beginning on or after 1 January 2013)

These annual improvements, address six issues in the 2009-2011 reporting cycle. It includes changes to:

IFRS 1,	First time adoption
IAS 1,	Financial statement presentation
IAS 16,	Property plant and equipment
IAS 32,	Financial instruments; Presentation
IAS 34,	Interim financial reporting

These improvements did not have impact an impact on the Bank's financial statements.

Standards and interpretations issued but not yet effective:

IFRS 10 Consolidated Financial Statements (effective for annual periods beginning on or after 1 January 2014)

The objective of IFRS 10 is to establish principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entity (an entity that controls one or more other entities) to present consolidated financial statements. It defines the principle of control, and establishes controls as the basis for consolidation. It sets out how to apply the principle of control to identify whether an investor controls an investee and therefore must consolidate the investee. It also sets out the accounting requirements for the preparation of consolidated financial statements. The Bank is currently assessing the impact that IFRS 10 will have on the financial statements but does not expect any impact on them. The amendment will not have any impact on these financial statements.

IFRS 11 Joint Arrangements (effective for annual periods beginning on or after 1 January 2014)

IFRS 11 is a more realistic reflection of joint arrangements by focusing on the rights and obligations of the arrangement rather than its legal form. The amendment will not have any impact on these financial statements.

IFRS 12 Disclosures of Interests in Other Entities (effective for annual periods beginning on or after 1 January 2014)

IFRS 12 includes the disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles. The Bank is currently assessing the impact that IFRS 12 will have on the financial statements. The Bank plans to adopt this new standard on its effective date.

IAS 27 (revised 2011) Separate Financial Statements (effective for annual periods beginning on or after 1 January 2014)

IAS 27 (revised 2011) includes the provisions on separate financial statements that are left after the control provisions of IAS 27 have been included in the new IFRS 10. The Bank does not expect any impact.

IAS 28 (revised 2011) Associates and Joint Ventures (effective for annual periods beginning on or after 1 January 2014)

IAS 28 (revised 2011) includes the requirements for joint ventures, as well as associates, to be equity accounted following the issue of IFRS 11. The amendment will not have any impact on these financial statements.

Amendment to IFRSs 10, 11 and 12 on Transition Guidance (effective for annual periods beginning on or after 1 January 2014)

These amendments provide additional transition relief to IFRSs 10, 11 and 12, limiting the requirement to provide adjusted comparative information to only the preceding comparative period. For disclosures related to unconsolidated structured entities, the amendments will remove the requirement to present comparative information for periods before IFRS 12 is first applied. The Bank is currently assessing the impact of the amendment on its financial statements, but does not expect any impact on them. The Bank plans to adopt this amendment on its effective date.

Amendments to IFRS 10, IFRS 12 and IAS 27 – on Consolidation for Investment Entities (issued on 31 October 2012 and effective for annual periods beginning 1 January 2014)

These amendments mean that many funds and similar entities will be exempt from consolidating most of their subsidiaries. Instead, they will measure them at fair value through comprehensive income. The amendment will not have any impact on these financial statements.

Amendments to IAS 32 Financial Instruments: Presentation on Asset and Liability Offsetting (issued in December 2012 and effective for annual periods beginning on or after 1 January 2014)

These amendments are to the application guidance in IAS 32 Financial instruments: Presentation, and clarify some of the requirements for offsetting financial assets and financial liabilities on the statement of financial position. The Bank is currently assessing the impact of amendments that might have impact on the presentation in the financial statements of the Bank. The Bank plans to adopt this new amendment on its effective date.

Amendment to IAS 36 Impairment of Assets on Recoverable Amount Disclosures (issued on 29 May 2013 and effective for annual periods beginning 1 January 2014)

This amendment addresses the disclosure of information about the recoverable amount of impaired assets if that amount is based on fair value less costs of disposal. The amendment could have an impact on disclosure only, but not on measurement and recognition of the assets in the Bank's financial position or performance. The Bank plans to adopt this amendment on its effective date.

Amendment to IAS 39 Financial Instruments: Recognition and Measurement 'Novation of Derivatives' (issued on 27 June 2013 and effective for annual periods beginning 1 January 2014)

This amendment provides relief from discontinuing hedge accounting when novation of a hedging instrument to a central counter party meets specified criteria. The amendment will not have any impact on these financial statements.

IFRS 9 Financial Instruments (effective for annual periods beginning on or after 1 January 2015)

IFRS 9 is the first standard issued as part of a wider project to replace IAS 39 Financial Instruments: Recognition and Measurement. IFRS 9 retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets: amortised cost and fair value. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. The guidance in IAS 39 on impairment of financial assets and hedge accounting continues to apply. The Bank is assessing the impacts of this standard on the financial statements. The Bank plans to adopt this new standard on the effective date as of and when endorsed by the EU.

IFRIC 21 Levies (issued on 20 May 2013 and effective for annual periods beginning on or after 1 January 2014)

This is an interpretation of IAS 37 Provisions, contingent liabilities and contingent assets. IAS 37 sets out criteria for the recognition of a liability, one of which is the requirement for the entity to have a present obligation as a result of a past event (known as an obligating event). The interpretation clarifies that the obligating event that gives rise to a liability to pay a levy is the activity described in the relevant legislation that triggers the payment of the levy. The Bank does not expect IFRIC 21 to have an impact on the financial statements. The Bank plans to adopt this new interpretation on the effective date as of and when endorsed by the EU.

The Bank's Management decided not to apply the stated standards, amendments and interpretations before their effective dates.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

Where the accounting policies are aligned with accounting principles of International Financial Reporting Standards (hereinafter IFRS or Standards), in describing the Bank's accounting policies there can be a reference to certain standards. Unless otherwise stated, these are standards that have been applied on 31 December 2013

4.1. Financial Instruments

Classification

The Bank classifies its financial instruments 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 amortized cost.

The classification depends on the purpose for which the financial instruments were acquired. Management determines the classification of financial instruments at initial recognition.

Loans and receivables

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

Financial assets available for sale

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 equity 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 includes financial assets that returns fixed or determinable payments with a fixed maturity, and the Bank intends to hold it to maturity.

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 sales 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 amortized cost are recognized when funds are given or received.

Bank derecognized financial instruments (in whole or in part) when their 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 realized, expired or are surrendered. Bank derecognized financial liabilities only when the financial liability ceases to exist; it is discharged, cancelled or expired. If the terms of a financial liability change, the Bank will cease recognizing that liability and will recognize a new financial liability, with new conditions.

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

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.

Financial assets carried at fair value through profit or loss are initially recognised at fair value and transaction costs are expensed in the income statement.

After initial recognition, the Bank evaluates the financial assets available for sale at its fair value, 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 statement are measured at amortized cost.

Profits and losses

Profits or losses from changes in fair value of monetary assets available for sale are recognized directly in the fair value reserve in equity, and are disclosed in the statement of changes in equity. Impairment losses, profits and losses from foreign exchange gains, interest income, and amortization of premium or discount monetary assets available for sale are recognized in the income statement. Upon sale or other derecognition of available-for-sale assets, any cumulative profits or losses on the instrument are transferred to the income statement.

Unrealised gains and losses arising from changes in fair value of financial assets at fair value through profit or loss, as well as all related realised gains and losses arising on the sale or other derecognition of these assets and liabilities are recognised in the income statement. Interest on the basis of holding these instruments is recognised as interest income, whereas dividends are recognised as dividend income in the income statement.

Profits 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 recognized in the income statement when the financial instrument is derecognized or when its value is impaired.

Determining the fair value of financial instruments

The fair values of financial instruments that are quoted in active markets are based on closing prices obtained from the regulated market (Level 1 according to IFRS fair value hierarchy). These instruments include liquid securities traded on liquid stock-exchanges.

The fair value of financial instruments whose value is determined by reference to similar instruments traded in active markets is based on valuation techniques that use observable market data (Level 2 according to IFRS fair value hierarchy). These instruments include less liquid debt and equity securities.

If there is no active market for a financial instrument or if, for other reasons, the fair value cannot be reliably measured by the market price, the Bank adequately assess the value by maximum use of market information that was not available in the market (Level 3 according to IFRS fair value hierarchy). These instruments include non-liquid debt and equity securities.

Impairment of financial assets

Impairment of assets identified as impaired

At each balance sheet date, all financial assets are reviewed to determine whether there is objective evidence of impairment. If any such indication exists, the recoverable amount of the asset is assessed.

The Bank evaluates and conducts impairment of all financial assets.

The recoverable amount of financial assets carried at amortized cost is calculated as the present value of expected future cash flows, discounted at the original interest rate of the instrument. Short-term balances are not discounted.

Impairment of assets not identified as impaired

In addition to the impairment of assets identified as impaired, the Bank recognizes impairment in the income statement on the balance sheet exposures that is not identified as impaired at rates of 1.00%, according to the accounting regulations of the CNB.

Cash and cash equivalents

Cash and cash equivalents includes 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 and uncollectible amounts, and items in process of collection.

Debt securities

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

Placements with banks

Placements with banks are classified as loans and receivables and are measured at amortized cost net of impairment losses.

4.2. Income tax

The income tax charge is based on taxable profit 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, in which case it is recognised in equity. Current tax is the expected tax payable on the taxable income for the year, using the tax rates enacted or substantially enacted at the balance sheet date, and any adjustments to tax payable in respect of previous years.

Deferred taxes are calculated by using the balance sheet liability method. Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax 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.

The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Bank expects, at the reporting date, to collect or settle the carrying amount of assets and liabilities.

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 recognized only to the extent that it is likely to be used as tax relief. At each balance sheet date, the Bank reassesses unrecognized potential deferred tax assets and the carrying amount of recognized deferred tax assets.

4.3. Property and equipment

Items of property and equipment are recognised at historical cost or estimated cost reduced by accumulated depreciation and impairment losses.

Amortization is calculated on a linear 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.

	2013	**2012**
Buildings	2.50%	2.50%
Computers	25%	25%
Furniture and equipment	10% - 20%	10% - 20%
Vehicles	25%	25%
Other not mentioned tangible assets	5%-10%	5%-10%

4.4. Intangible assets

Intangible assets are recognised at acquisition cost net of accumulated amortization and impairment losses. Expenditure on development activities is recognized as an intangible asset if it satisfies all the requirements in accordance with IAS 38 "Intangible Assets”. Amortization is calculated on a linear basis over the estimated useful lives of intangible assets.

Intangible assets are amortized on a linear basis over their estimated useful lives as follows:

	2013	2012
Intangible assets (other)	10%-20%	10%-20%
Intangible assets Software	10%-25%	10%-25%

4.5. Foreclosed assets

The Bank initially recognises tangible assets taken in exchange for uncollected receivables at the lower of the cost or fair value. The foreclosed assets are subsequently measured at the lower of the net carrying amount and fair value net of transaction costs.

Tangible assets taken in exchange for uncollected receivables are recorded in the statement of financial position in the foreclosed assets position in accordance with International Accounting Standard 2 Inventories or assets held for sale if the conditions from International Accounting Standard 5 Non-current Assets Held for Sale are met. These conditions are met if the sale is highly probable, if the assets are available for sale in present state under normal conditions, if there is an active plan to sell at a reasonable price and if it is expected that the sale will be completed within a year of classification.

4.6. Investment property

Investment property includes Bank’s investments held for rental yields or appreciation of property.

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

4.7. Impairment of non-financial assets

Impairment of assets, that have an indefinite useful life and are not amortized, is tested annually. Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. An impairment loss is recognized as the difference between the asset's carrying amount and its recoverable amount. The recoverable amount is fair value of assets reduced by costs to sell or value in use, whichever is higher. For the purposes of assessing impairment, assets are grouped at the lowest levels in order to separately identify the cash flows (cash generating units). Non-financial assets for which is expressed impairment loss are reviewed at each reporting date for possible reversal of the impairment.

Property, plant and equipment and intangible assets are reviewed for impairment in the circumstances that 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, or is treated as a revaluation reserve decreased for assets carried at revalued amount if the impairment loss does not exceed the amount held in the revaluation. Depending on which is higher, the recoverable amount is the net selling price of assets or its value in use.

4.8. Provisions for liabilities and charges

Provisions for liabilities and charges are maintained at a level that management believe are 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.

4.9. Employee benefits

Defined pension contributions

Bank pays contributions to planned insurance on a mandatory, contractual basis. Bank has no further payment obligations once the contributions are paid. The contributions are recognized as an expense recognized as an employee benefit when incurred.

The Bank recognizes a provision for bonuses where contractually obliged or when there is a past practice based on which are created derivative obligation. Furthermore, the Bank recognizes a liability for accumulated fees for absences from work based on unused vacation days 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 preformed, using discount rates that, in the opinion of management, best represent the time value of money.

4.10. Share capital and reserves

Share capital is stated in HRK at nominal value.

4.11. Accumulated losses

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

4.12. Interest income and expenses

Interest income and expense is recognized in the income statement as it occurs, for all interest-bearing financial instruments, including those that are measured at amortized cost and available for sale, using the linear method, with the exception of income on treasury bills and bonds, which are recognized using the effective interest rate. Such income and expense is presented as interest income and similar income or interest expense and similar expense in the income statement. Interest income and expense also includes the amortization of premium or discount, and other differences between the initial carrying amount of an interest bearing instrument and its value at maturity, recognized by linear method.

In the case when loans repayment becomes doubtful, the principal is reduced to its estimated recoverable amount, and interest income is thereafter recognized at the rate used to discount future cash flows.

4.13. Fee and commission income and expense

Fee and commission income comprises mainly of fees received from customers for loans, guarantees, letters of credit and other services provided by the Bank. Fees are recorded to income due to maturity 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.

4.14. 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 balance sheet date are translated at the exchange rate defined at the balance sheet date. Exchange differences arising from conversion are recognized in the income statement. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are converted at the exchange rate at the date when the fair value was determined. Non-monetary assets and items that are measured in terms of historical cost in a foreign currency are converted at the exchange rate of the transaction and are not converted at the balance sheet date.

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.

5. Interest income

in thousands of HRK

	2013	2012
Companies	71,394	46,564
Individuals	20,972	24,721
State units	17,143	15,964
Banks and other financial institutions	2,846	4,209
Other organisations	539	61
Total	**112,894**	**91,519**

Interest income includes income from partially recoverable placements in the amount of HRK 17.7 million (2012: HRK 16.8 million), of which HRK 14.6 million (2012: HRK 12.3 million) relates to transactions with legal persons, and the remaining HRK 3.1 million (2012: HRK 4.5 million) relates to transactions with individuals.

6. Interest expense

in thousands of HRK

	2013	2012
Companies	8,929	1,910
Individuals	35,674	29,994
State units	613	3,999
Banks and other financial institutions	20,277	16,050
Other organisations	3,631	570
Total	**69,124**	**52,523**

7. Fee and commission income

in thousands of HRK

	2013	2012
Companies	5,498	5,236
Individuals	1,668	1,739
Other	2,637	3,171
Total	**9,803**	**10,146**

8. Fee and commission expense

in thousands of HRK

	2013	2012
Provision for FINA services	(2,658)	(3,085)
Foreign banks	(175)	(147)
Domestic clients	(2,148)	(1,420)
Total	**(4,981)**	**(4,652)**

9. Net expense from financial operations

in thousands of HRK

	2013	2012
Expense from the sale of financial assets available for sale	(566)	(1,291)
Total	**(566)**	**(1,291)**

10. Net income from foreign exchange differences

in thousands of HRK

	2013	2012
Foreign exchange differences arising from change of exchange rate	(7,134)	(1,078)
Foreign exchange differences arising from foreign currency clause	7,733	892
Foreign exchange differences on foreign currency trading	4,496	4,581
Foreign exchange differences incurred on translation of provision for possible losses on loans	(762)	(123)
Total	**4,333**	**4,272**

11. Other operating income

in thousands of HRK

	2013	2012
Net revenues from sale of property, plant and equipment and foreclosed assets	5,594	1,134
Rental income	4,430	4,400
Income from release of provisions for litigation against the bank	770	779
Income from settlements with insurance company	2,000	-
Income from reversal of provisions for jubilee awards, termination benefits, etc.	1,469	-
Other income	564	907
Total	**14,827**	**7,220**

12. Other operating expenses

As at 31 December 2013 the Bank had 268 employees (31 December 2012: 277 employees).

Personnel expenses include HRK 6.8 million (2012: HRK 6.3 million) of contributions for mandatory pension insurance which are paid into mandatory pension funds. Contributions are calculated as a percentage of employees' gross salaries.

in thousands of HRK

	2013	2012
Net salary	(22,324)	(21,355)
Contributions, taxes and surtaxes	(16,691)	(15,274)
Other personnel expenses	(2,778)	(2,003)
Total staff costs	(41,793)	(38,632)
Amortization and depreciation	(4,484)	(5,562)
Total amortization and depreciation	(4,484)	(5,562)
Material costs and services	(24,398)	(22,521)
Marketing expenses	(1,636)	(592)
Judicial and administrative fees	(313)	(348)
Other	(2,563)	(2,915)
Total other operating expenses	(28,910)	(26,376)
Total	**(75,187)**	**(70,570)**

13. Impairment losses and provisions

in thousands of HRK

	2013	2012
Impairment of loans and advances to customers (Note 21.2)	(6,177)	(106,298)
Impairment of financial assets available for sale (Note 19)	-	6
Impairment of interest receivable	39	(1,718)
Impairment of receivables for interest income	316	
Impairment of other assets (including provisions for unidentified losses on a collective basis) (Note 25)	(747)	(2,464)
Impairment of tangible and intangible assets (Note 24)	(222)	-
Incomes from collection of written-off loans in previous years	1,852	2,360
Provisions and impairment on a collective basis for loans and other receivables	(7, 336)	973
Provision for litigation against the Bank (Note 31)	(1,118)	(1,140)
Provisions for pensions and other obligations to employees	(496)	(1,915)
Provisions for identified losses for contingent liabilities	130	(106)
Provisions for unidentified losses on a collective basis for contingent liabilities	(673)	(187)
Total provisions for contingencies (Note 31)	***(543)***	***(293)***
Other provisions	(2,211)	-
Total expenses of impairment losses and provisions	**(16,643)**	**(110,489)**

14. Income tax

Income tax expense recognized in the income statement

	2013	2012
Current income tax expense	-	-
Deferred tax income	-	22,761
	-	-

Reconciliation of accounting and tax results is shown as follows:

	2013	2012
Accounting loss before tax	**(24,644)**	**(126,362)**
Effect of income tax at the rate of 20% (2012: 20%)	(4,929)	(25,272)
Effect of non-deductible tax expenses	111	63
Effect of non-taxable income	(47)	(45)
Tax losses for the year potentially available for carry forward	(4,865)	(25,254)
Recognised deferred tax assets	-	22,761
	-	**22,761**

Movements in deferred tax assets

	Deferred income by fees included in effective interest rate on loans given	Tax losses	Total
At 1 January 2012	-	-	-
Credited in the in income statement	-	22,761	22,761
At 31 December 2012	**-**	**22,761**	**22,761**
Credited in the in income statement	2,512	(2,512)	-
At 31 December 2013	**2,512**	**20,249**	**22,761**

Recognised deferred tax assets on tax losses transferable to future periods

The table below shows the tax effect of recognized deferred tax assets on tax losses transferable to future periods, expected to be used in the next 5 years from the reporting period in which they are generated.

The amount of tax losses that is planned to be used until:	2013	2013
	Total tax loss	**Effect of tax losses**
31 December 2015	14,295	2,859
31 December 2016	27,614	5,523
31 December 2017	36,554	7,311
31 December 2018	22,781	4,556
	101,244	**20,249**

15. Cash

	in thousands of HRK	
	2013	**2012**
Giro account	88,198	37,477
Petty cash:		
- HRK	15,678	14,693
- foreign currency	11,100	10,870
Cash in foreign currency accounts in foreign banks	136,022	20,635
Cash in foreign currency accounts in domestic banks	18,296	7,640
Checks and other assets in the course of collection	8	53
Provisions for impairment for unidentified losses on a collective basis	(2,425)	(658)
Total cash	**266,877**	**90,710**

16. Receivables from the Croatian National Bank

	in thousands of HRK	
	2013	**2012**
Obligatory reserve		
- HRK	156,118	112,472
- foreign currency	26,701	18,062
Other mandatory deposits	11,215	-
accrued interest	-	3
Provisions for impairment for unidentified losses on a collective basis	*(1,940)*	*(1,305)*
Total	**192,094**	**129,232**

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 obligatory reserve requirement as at 31 December 2013 amounted to 12.00% (2012: 13.5%) of kuna and foreign currency deposits, borrowings and issued debt securities.

As at 31 December 2013, the required rate for the part of the obligatory reserve calculated based on kuna liabilities to be deposited with the CNB amounted to 70% (2013: 70%), while the remaining 30% (2012: 30%) had to be held in the form of other liquid receivables. This includes the part of foreign currency obligatory reserve required to be held in HRK. At least 60% (2012: 60%) of the part of the obligatory reserve based on foreign currency liabilities must be deposited with the CNB, while the remaining 40% (2012: 40%) (or less to the extent that the amount deposited with the CNB exceeds 60%) must be held in the form of other liquid receivables, after adjusting for the obligatory reserve requirement arising from foreign currency funds from non-residents and related parties (which is required to be held in full with the CNB). 75% of the part of the obligatory reserve calculated based on foreign currency liabilities is required to be held in HRK and is added to the kuna part of the obligatory reserve.

17. Placements with banks

in thousands of HRK

	2013	2012
Deposits with foreign banks	56,541	77,281
Deposits with domestic banks	1,525	52,907
Loans to domestic banks	-	10,000
accrued interest	12	21
Provisions for impairment for unidentified losses on a collective basis	*(581)*	*(1,402)*
Total	**57,497**	**138,807**

18. Financial assets held for trading

in thousands of HRK

	2013	2012
Shares in investment funds	5,081	-
TOTAL	**5,081**	**-**

19. Financial assets available for sale

in thousands of HRK

	2013	2012
Foreign currency bonds	38,595	23,978
Domestic currency bonds	37,257	24,081
Treasury bills	184,779	241,068
Bills of exchange of companies	71,469	46,069
Shares	439	705
Investment funds	41	100,727
Impairment allowance – available-for-sale portfolio	*(774)*	*(774)*
Accrued interest	1,689	1,095
Total	**333,495**	**436,949**

Foreign currency bonds refer to bonds issued by the Croatian Ministry of Finance which mature in 2014, 2015 and 2018, with the nominal interest rate from 4.25% to 5.875% (2012: 5% to 5.875%) per annum.

Foreign currency bonds also include bonds issued by the Grand Duchy of Luxembourg which mature in 2028, with the nominal interest rate of 2.25% per annum.

Domestic currency bonds refer to bonds issued by the Croatian Ministry of Finance which mature in 2018, with the nominal interest rate of 5.25% (2012: 4.25% to 5.875%) per annum.

Domestic currency bonds refer to the bond issued by ERSTE UND STEIERMAERKISCHE BANK D.D. RIJEKA which matures in 2017, with the nominal interest rate of 5.875% per annum.

Treasury bills are issued by the Croatian Ministry of Finance with an interest rate from 2.15% to 2.55% (2012: 2% to 5.25%) per annum with maturity in one year.

Bills of exchange of companies were bought off at the discount rate from 6.95% to 13.89% (2012: 12.55% - 13.89%) per annum.

Shares relating to the Bank shares in companies and financial institutions with less than 20% of the property are presented below.

in thousands of HRK

	2013	2012
Shares listed on the Stock Exchange	-	266
Shares not listed on the Stock Exchange	439	439
	439	**705**

Shares in investment funds are related entirely to investments in money market funds, as follows:

in thousands of HRK

	2013	2012
Domestic currency funds	5,122	18,753
Shares with a currency clause	-	81,974
	5,122	**100,727**

Movements in the provision for impairment are as follows:

in thousands of HRK

	2013	2012
Balance as at 1 January	**774**	**780**
Impairment	-	(6)
Balance as at 31 December	**774**	**774**

The fair value hierarchy of financial assets

The determination of fair value for financial assets and liabilities for which there is no observable market price requires the use of valuation techniques. For financial instruments that trade infrequently and have little price transparency, fair value is less objective, and therefore the calculation of the fair value of each financial asset or liability requires identifying and considering all risks affecting the specific instrument.

When calculating fair value, the Bank takes into account the rules of IFRS fair value hierarchy that reflect the significance of inputs used in the valuation process. Each instrument is individually assessed in detail.

The levels of the fair value hierarchy are determined based on the lowest level of input data significant for determining the fair value of the instrument.

	2013			**2012**		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Foreign currency bonds	38,595	-	-	23,978	-	-
Domestic currency bonds	37,257	-	-	24,081	-	-
Treasury bills	-	184,779	-	-	241,068	-
Bills of exchange of companies	-	-	71,469	-	-	46,069
Shares	-	-	439	266	-	439
Investment funds	5,122	-	-	100,727	-	-
	80,974	**184,779**	**71,908**	**149,052**	**241,068**	**46,508**

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 are valued using valuation techniques that are based on market data not readily available in the market. These are instruments whose fair value cannot be determined directly by reference to available market information and for whose value calculation different valuation techniques are used. These instruments include illiquid debt securities and illiquid equity securities.

20. Assets held to maturity

in thousands of HRK

	2013	**2012**
Repurchased receivables	**2,171**	**2,568**
Provisions for impairment for unidentified losses on a collective basis	(22)	(26)
Total	**2,149**	**2,542**

21. Loans and advances to customers

21.1. Analysis by type of client

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

in thousands of HRK

	2013	2012
Individuals		
Overdrafts on transaction accounts	11,607	9,303
Mortgage loans	2,872	1,063
Housing loans	24,691	14,837
Cash loans	61,982	53,050
Loans for agriculture	24,631	33,769
Other loans	149,509	176,442
Total loans to individuals	**275,292**	**288,464**
Provision for impairment for identified losses	*(42,955)*	*(44,303)*
Provision for impairment for unidentified losses on a collective basis	*(1,881)*	*(1,850)*
Provision for interest impairment – individuals	*(512)*	*(720)*
Total provisions for impairment – individuals	*(45,348)*	*(46,873)*
Accrued interest	1,779	2,161
Total loans to individuals, net	**231,723**	**243,752**
Legal entities		
Overdrafts on transaction accounts	29,432	11,376
Loans for payments under guarantees	16,103	8,385
Syndicated loans	438,846	116,141
Loans for working capital	257,563	234,914
Loans for investments	632,801	374,707
Other loans	211,559	229,154
Total loans to legal entities	**1,586,304**	**974,677**
Provision for impairment for identified losses	*(181,669)*	*(173,442)*
Provision for impairment for unidentified losses on a collective basis	*(11,976)*	*(6,249)*
Provision for interest impairment – legal entities	*(3,145)*	*(2,948)*
Total provisions for impairment	***(196,790)***	***(182,639)***
Accrued interest	8,581	6,045
Total loans to legal entities, net	**1,398,095**	**798,083**
Total loans	***1,871,956***	***1,271,347***
Total provisions for loans	*(242,138)*	*(229,512)*
Total loans and advances to customers, net	**1,629,818**	**1,041,835**

As at 31 December 2013, gross exposure arising from partly recoverable and non-recoverable placements was HRK 483,768 thousand (2012: HRK 470,637 thousand), and the associated impairment losses amounted to HRK 228,281 thousand (2012: HRK 221,413 thousand).

21.2. Changes in impairment losses and provision for potential losses

The changes in the impairment losses and provision for potential losses are as follows:

in thousands of HRK

	2013			2012		
	Impairment	Special reserves for ident. losses on a collective basis	Total	Impairment	Special reserves for ident. losses on a collective basis	Total
Balance as at 1 January	**221,413**	**8,099**	**229,512**	**112,911**	**7,691**	**120,602**
Net impairment losses i.e. provisions (Note 13)	6,177	5,758	**11,935**	106,298	326	**106,624**
Net impairment of interest receivable (Note 13)	(39)		**(39)**	1,718	82	**1,800**
Exchange differences	791	-	**791**	128	-	**128**
Write offs	(61)	-	**(61)**	(50)	-	**(50)**
Corrections	-		**-**	408	-	**408**
Balance as at 31 December	**228,281**	**13,857**	**242,138**	**221,413**	**8,099**	**229,512**

In accordance with current legislation, the Bank has to create reserves for identified losses on a collective basis, determined in the credit portfolio based on previous experience. Taking into account the legal provisions, the amount of these reserves by the Bank's policies cannot be less than 1% of non-risk assets and 1% of non-risk commitments and contingencies as at 31 December 2013 (2012: 1% of non-risk assets and 1% of non-risk commitments and contingencies).

22. Investment property

in thousands of HRK

	2013	2012
Investment property	36,095	36,095
Total	**36,095**	**36,095**

The Bank mainly realises rental income on these properties.

23. Property, plant, equipment and intangible assets

in thousands of HRK

	Land and buildings	Furniture and vehicles	Equipment and other tangible assets	Tangible assets acquired, but not brought into use	Total tangible assets	Intangible assets	Intangible assets acquired, but not brought into use	Total intangible assets	Total
Cost									
Balance as at 31 December 2011	**35,677**	**11,976**	**28,543**	**-**	**76,196**	**29,574**	**-**	**29,574**	**105,770**
New purchases	25	76	1,259	53	**1,413**	1,285		**1,285**	**2,698**
Disposal and sale		(575)	(2,015)		**(2,590)**	(177)		**(177)**	**(2,767)**
Balance as at 31 December 2012	**35,702**	**11,477**	**27,787**	**53**	**75,019**	**30,682**	**-**	**30,682**	**105,701**
Transfer from / to accounts					-			-	-
New purchases		1,535	916	(53)	**2,398**	1,241		**1,241**	**3,639**
Disposal and sale	(2,441)	(3,262)	(2,680)		**(8,383)**	(3,219)		**(3,219)**	**(11,602)**
Balance as at 31 December 2013	**33,261**	**9,750**	**26,023**	**-**	**69,034**	**28,704**	**-**	**28,704**	**97,738**
Accumulated depreciation									
Balance as at 31 December 2011	**17,744**	**11,381**	**24,014**	**-**	**53,139**	**25,187**	**-**	**25,187**	**78,326**
Depreciation in 2012	815	281	1,967		**3,063**	2,499		**2,499**	**5,562**
Disposal and sale		(558)	(2,014)		**(2,572)**	(178)		**(178)**	**(2,750)**
Balance as at 31 December 2012	**18,559**	**11,104**	**23,967**	**-**	**53,630**	**27,508**	**-**	**27,508**	**81,138**
Depreciation in 2013	800	274	1,710		**2,784**	1,700		**1,700**	**4,484**
Disposal and sale	(2,441)	(3,210)	(2,650)		**(8,301)**	(3,219)		**(3,219)**	**(11,520)**
Balance as at 31 December 2013	**16,918**	**8,168**	**23,027**	**-**	**48,113**	**25,989**	**-**	**25,989**	**74,102**
Net book amount as at 31 December 2011	**17,933**	**595**	**4,529**	**-**	**23,057**	**4,387**	**-**	**4,387**	**27,444**
Net book amount as at 31 December 2012	**17,143**	**373**	**3,820**	**53**	**21,389**	**3,174**	**-**	**3,174**	**24,563**
Net book amount as at 31 December 2013	**16,343**	**1,582**	**2,996**	**-**	**20,921**	**2,715**	**-**	**2,715**	**23,636**

The Bank wrote off certain assets from property and equipment with the cost in the amount of HRK 9,162 thousand and sold a portion in the amount of HRK 2,440 thousand.

24. Foreclosed assets

Changes in foreclosed assets for uncollected receivables are as follows:

in thousands of HRK

	2013	2012
Balance as at 1 January	**24,151**	**26,384**
Increase based on foreclosing the assets	3,835	4,210
Decrease due to impairment (Note 13)	(221)	-
Decrease due to sales	(1,955)	(6,443)
Balance as at 31 December 2013	**25,810**	**24,151**

In 2013, the Bank sold foreclosed assets in the amount of HRK 1,955 thousand (2012: HRK 6,443 thousand) and thus realised the profit from sale in the amount of HRK 792 thousand (2012: HRK 1,134 thousand).

25. Other assets

in thousands of HRK

	2013	2012
Receivables for fees and commissions	3,990	3,860
Trade receivables	15,092	17,262
Other receivables	26,840	27,335
Provisions for unidentified losses on an individual basis	(12,480)	(11,885)
Provisions for unidentified losses on a collective basis	(202)	(80)
Total other assets	**33,240**	**36,492**

26. Liabilities towards banks

in thousands of HRK

	2013	2012
Demand deposits		
- in kuna	2,668	24,366
- in currency	742	6,089
Total demand deposits	**3,410**	**30,455**
Term deposits		
- in kuna	122,990	122,547
- in currency	26,739	20,224
Total term deposits	**149,729**	**142,771**
accrued interest	1,273	1,204
Total	**154,412**	**174,430**

27. Demand deposits

in thousands of HRK

	2013	2012
Demand deposits - retail		
- in kuna	53,026	53,607
- in currency	48,702	46,848
Total individuals	**101,728**	**100,455**
Demand deposits - corporate		
- in kuna	131,454	102,306
- in currency	9,267	4,068
Total companies	**140,721**	**106,374**
Demand deposits – financial institutions		
- In kuna	549	1,261
Total financial institutions	**549**	**1,261**
Demand deposits – government and other institutions		
- in kuna	57,619	36,441
- in currency	10,285	8,520
Total government and other institutions	**67,904**	**44,961**
Limited deposits		
- in kuna	2,414	3,207
- in currency	16,000	15,195
Total limited deposits	**18,414**	**18,402**
Deposits from foreign entities		
- in kuna	1,213	964
- in currency	7,675	5,174
Total foreign entities	**8,888**	**6,138**
Total	**338,204**	**277,591**

28. Term deposits

in thousands of HRK

	2013	2012
Deposits - retail		
- in kuna	138,109	90,795
- in currency	938,173	602,036
Total retail	**1,076,282**	**692,831**
Deposits - corporate		
- in kuna	121,639	55,683
- in currency	78,182	857
Total corporate	**199,821**	**56,540**
Deposits – financial institutions		
- in kuna	152,326	133,338
- in currency	535	-
Total financial institutions	**152,861**	**133,338**
Deposits – government and other institutions		
- in kuna	28,552	37,624
Total government and other institutions	**28,552**	**37,624**
Deposits of foreign entities		
- in kuna	3,035	1,596
- in currency	112,872	91,312
Total foreign entities	**115,907**	**92,908**
Accrued interest	**31,199**	**20,930**
Total term deposits	**1,604,622**	**1,034,171**

29. Borrowings

in thousands of HRK

	2013	2012
Domestic banks	278,076	223,309
Foreign banks	22,913	22,637
Accrued interest	658	454
Total borrowings	**301,647**	**246,400**

30. Other liabilities

in thousands of HRK

	2013	2012
Liabilities for fees and commissions	1,348	992
Liabilities for derivatives	41	106
Trade payables	1,925	1,881
Liabilities to employees	3,610	3,735
Deferred tax liabilities	-	442
Accrued income	8,113	8,631
Other liabilities	6,697	4,099
Total other liabilities	**21,734**	**19,886**

31. Provisions

in thousands of HRK

	2013	2012
Provisions for judicial proceedings	8,091	8,769
Provisions for contingencies and commitments	1,466	923
Provisions for unused vacation days	459	1,424
Provisions for jubilee awards	482	491
Other provisions	2,211	-
TOTAL	**12,709**	**11,607**

Changes in provisions are shown as follows:

in thousands of HRK

	2013	2012
At 1 January	**11,607**	**9,038**
Income from reversal of provisions for legal claims against the bank (Note 12)	(770)	(779)
Additional provision for judicial proceedings (Note 14)	1,118	1,140
Changes in provisions for commitments and contingencies	543	293
Income from reversal of provision for unused vacation days	(1,424)	-
Income from reversal of provision for jubilee awards	(45)	-
Increase in provision for vacation days	459	1,424
Increase in provision for jubilee awards	36	491
Increase in other provisions	2,210	-
Costs paid for legal claims	(1,025)	-
At 31 December	**12,709**	**11,607**

During 2013, the provision in the amount of HRK 1,025 thousand was paid (2012: there were no payments or write-offs of existing provisions).

Provisions for off-balance-sheet exposure to credit risk and legal claims are recognized as other losses from impairment and provisions in the profit and loss account.

32. Share capital

The only shareholder of the Bank as at 31 December 2013 and 31 December 2012 is the State Agency for Deposit Insurance and Bank Rehabilitation.

in thousands of HRK

	2013	**2012**
Share capital	474,600	474,600
Accumulated loss	(256,315)	(152,714)
Reserves	1,584	1,767
Loss for the period	(24,644)	(103,601)
Total capital	**195,225**	**220,052**

Share capital in the amount of HRK 474,600 thousand (31 December 2012: HRK 474,600 thousand) consists of 4,746,000 shares with nominal value HRK 100 (31 December: 4,746,000 shares with nominal value HRK 100).

During 2010 the Bank issued bonds in the amount of HRK 70,000,000.00, which formed a hybrid instrument included in the calculation of additional capital. The issue was not secured by any own warranties, mortgages or other instruments, and it carried an interest rate of 5,5% p.a. The total bond issue was subscribed and paid by the State Agency for Deposit Insurance and Bank Rehabilitation.

In the meeting held on 29 October 2012 the General Assembly of the Bank decided to increase share capital of the Bank from HRK 274,600 thousand by the amount of HRK 200,000 thousand to the amount of HRK 474,600 thousand, by converting issued bonds and by payment of HRK 130 million.

33. Earnings per share

in thousands of HRK

	2013	**2012**
Loss for the current year	(24,644)	(103,601)
Number of shares (in thousands)	4,746	4,746
Earnings per share	**(5)**	**(22)**

34. Contingencies and commitments

in thousands of HRK

	2013	2012
Guarantees	(50,725)	(49,075)
Uncovered letters of credit	(7,391)	(2,010)
Revolving loans	(73,974)	(26,331)
Other classic off-balance sheet items with risk	(11,021)	(30)
Total contingencies and commitments	**(143,111)**	**(77,446)**

35. Legal claims

Several legal claims have been filed against the Bank. The Bank has, according to the internal act – Rulebook and the decision of the Croatian National Bank, formed adequate provisions for the proceedings carrying a risk of loss, and respectively evaluated a potential outflow of funds.

As at 31 December 2013 the provisions for losses from legal claims filed against the Bank amounted to HRK 8,091 thousand (2012: HRK 8,769 thousand).

As stated in Note 2 to financial statements, ex-shareholders of the Bank, suing the Bank for the return of shares and compensation for share cancellation, have filed more than 200 legal claims against the Bank. Until 31 December 2013 the stated proceedings resulted in several dozens of legally valid court decisions in Bank's favour.

Until the date of this report almost all proceedings are completed, with the most ruled in the favour of the Bank, while only several proceedings are ruled in the favour of shareholders, but considering these proceedings are related to share ownership they do not present a significant influence on the financial operations of the Bank. In cases where the judgements were in favour of the shareholders, Constitutional appeals were filed and in these legal proceedings the Constitutional Court made the decision to adopt the Bank's constitutional appeals and returned the case to the commercial court for a retrial.

36. Cash and cash equivalents

Cash and cash equivalents for the cash flow statement are shown as follows:

in thousands of HRK

	2013	2012
Petty cash and current accounts with banks (Note 15)	269,302	91,368
Deposits with other banks up to 3 months (Note 17)	58,078	140,209
	327,380	**231,577**

37. Transactions with related parties

The Bank is 100% owned by the State Agency for Deposit Insurance and Bank Rehabilitation (DAB). The Bank considers itself immediately related to its shareholder, the members of the Supervisory Board and the Management Board and other executives („key personnel“), to immediate family members of key personnel, to jointly controlled companies or companies under significant influence of Management Board members and members of their immediate families, according to the definition stated in International Accounting Standard 24 "Related Party Disclosures" ("IAS 24"). Key management includes members of the Management Board, Department directors, directors of branches and directors of control function departments. In 2013, key management comprised 40 employees (2012: 32 employees).

Assets and liabilities as well as revenues and expenses as at and for the year ended 31 December 2013 and 31 December 2012 result from key transactions with related parties as follows:

(in thousands of HRK)

2013	receivables	liabilities	revenue	expense
DAB (sole shareholder)	355	30,148	16	4,538
Key personnel				
Short-term benefits (bonuses, salaries, benefits)	-	-	-	12,898
Long-term benefits (loans and deposits)	6,549	2,421	275	226
State in narrow and broad definition	1,036,298	457,491	36,346	15,906
Total	**1,043,202**	**490,060**	**36,637**	**33,568**

(in thousands of HRK)

2012	receivables	liabilities	revenue	expense
DAB (sole shareholder)	-	19,118	-	7,553
Key personnel				
Short-term benefits (bonuses, salaries, benefits)	-	-	-	9,903
Long-term benefits (loans and deposits)	2,061	1,358	172	122
State in narrow and broad definition	571,244	359,111	24,390	14,341
Total	**573,305**	**379,587**	**24,562**	**31,919**

Key management does not own Bank's shares. Loans and receivables from customers include HRK 6.5 million (2012: HRK 2.1 million) related to loans and receivables granted to key management. During the year, the Bank collected interest in the amount of HRK 0.3 million (2012: HRK 0.2 million) on loans and receivables from key management granted with annual interest rates from 3.50% to 6.50% (2012: from 5% to 9.7%). The amount of current accounts and customer deposits includes HRK 2.4 million of key management deposits (2012: HRK 1.4 million). During 2013, the Bank paid interest on this basis in the amount of HRK 0.2 million (2012: HRK 0.1 million), with annual interest rates from 2.10% to 4.60% (2012: 1.5% to 4.6%).

Supervisory Board expenses in 2013 amounted to HRK 282 thousand, while in 2012 they amounted to HRK 232 thousand.

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

- Central government
- Local administration
- Public non-financial companies
- Public insurance companies and pension funds
- Public financial auxiliary institutions
- Public other monetary financial institutions
- Public other financial mediators

As at 31 December 2013, the exposure to the state in narrow and broad definition comprises the exposure to the state company Hrvatske autoceste d.o.o. in the amount of HRK 248.2 million, of which HRK 247.2 million relates to receivables under a syndicated loan (HRK 75.5 million as at 31 December 2012) and the exposure to the Croatian Bank for Reconstruction and Development in the amount of HRK 29.6 million, of which HRK 29.5 million relates to loans receivables (as at 31 December 2012 in the amount of HRK 40.7 million).

The Bank also has an exposure under a syndicated loan to the company Hrvatske ceste in the amount of HRK 113.3 million and the exposure under a loan for investments to the Restructuring and Sale Centre in the amount of HRK 224.5 million.

The Bank has exposure to the Ministry of Finance under loans in the amount of HRK 18.9 million (HRK 94.5 million as at 31 December 2012), under listed Ministry of Finance bonds in the amount of HRK 57.7 million (as at 31 December 2012 in the amount of HRK 44.1 million), and it also has exposure under issued MoF treasury bills in the amount of HRK 184.8 million (HRK 241.1 million in 2012).

As at 31 December 2013, Croatia osiguranje d.d. has a term deposit in the Bank in the amount of HRK 40.1 million (HRK 60.1 million as at 31 December 2012), and the Ministry of Finance limited deposit amounts to HRK 15.3 million (deposit balance as at 31 December 2012: HRK 15.1 million).

As at 31 December 2013, the Restructuring and Sale Centre holds in the transaction account in the Bank HRK 4.4 million.

As at 31 December 2013, a Bank’s shareholder, the State Agency for Deposit Insurance and Bank Rehabilitation holds in the transaction account HRK 29.1 million.

As at 31 December 2013, the Bank has a liability to the Croatian Bank for Reconstruction and Development on the basis of the borrowing in the amount of HRK 208.8 million (as at 31 December 2012: HRK 196.9 million).

All the above mentioned significant transactions related to the state were concluded at market principles.

Income recognised in the income statement in 2013 treated as key transactions is as follows:

- income from loans to Hrvatske autoceste in 2013 amounts to HRK 9.6 million (2012: HRK 138 thousand)
- income from loans to Hrvatske ceste in 2013 amounts to HRK 1.0 million
- income from syndicated loan to CBRD amounts to HRK 0.4 million
- income from loans given to the Ministry of Finance amounts to HRK 4.9 million (HRK 2.2 million in 2012)
- income from MoF bonds amount to HRK 3.9 million (2012: HRK 3.7 million)
- income from MoF treasury bills amount to HRK 5.7 million (2012: HRK 8.2 million)

Expenses recognised in the income statement treated as key transactions are as follows:

- costs of the term deposit of Croatia osiguranje in 2013 in the amount of HRK 2.4 million (2012: HRK 1.7 million)
- costs of the term deposit of the company Hrvatske autoceste d.o.o. in the amount of HRK 2.5 million
- costs of the borrowing from CBRD in 2013 in the amount of HRK 5.6 million (2012: HRK 5.9 million)
- costs to DAB relate to costs for the savings deposit insurance and rental expenses

Exposures under receivables to DAB, key management, the state in broad and narrow definition, contain off-balance sheet receivables of the Bank in the following amounts:

(in thousands of HRK)	key management	state in narrow and broad definition
2013		
guarantees	-	471
letters of credit	-	-
revolving loans	557	36,344

(in thousands of HRK)		
2012		
guarantees	-	622
letters of credit	-	193
revolving loans	433	344

The Bank has the highest off-balance sheet exposure in the group State in narrow and broad definition to clients Đuro Đaković in the amount of HRK 9.9 million and Plinara istočne Slavonije d.o.o. for the gas supply in the amount of HRK 9.4 million.

38. 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 the foreign exchange risk and the risk of interest rate changes.

38.1. Credit risk

The Bank is continually exposed to credit risk in its operations through crediting and investing activities and in cases where it acts as a mediator on behalf of customers or third parties.

The Bank's primary exposure to credit risk arises from loans and receivables from customers and banks and investments available for sale. The amount of credit exposure on this basis and on the basis of debt securities available for sale is the carrying amount of assets in the balance sheet.

Also, the Bank is exposed to credit risk on off-balance sheet items, through liabilities for unused granted loans and issued guarantees.

Credit risk is the greatest individual risk in bank's operations, so all organisational units and bank's functionalities pay their maximum attention to it. Credit risk management and control are centralised in the Risk Management Service which regularly reports to the Management Board, Bank bodies, the Supervisory Board and higher management.

For the purposes of credit risk management, the Bank divided its basic activities into the following parts of the credit risk management process

- process of granting loans
- process of monitoring loans
- credit portfolio analysis
- procedure with bad loans
- system of early detection of increased credit risk
- process of loan classification according to risk degrees.

A specially important process is related to establishing appropriate relations between individual types of the stated processes, in order to avoid their disharmony and overlapping, for the purpose of establishing the required divisions of competences and responsibilities for them.

Organisational responsibilities for credit risk management are divided among the responsibility structures of sale and background jobs/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 control
- risk reporting

The work of credit analysis, organisationally located in the Risk Management Service, by its scope of activities directly influences credit risk management, primarily during the analysis and giving opinions on acceptability of credit risk for banks, including the following sub-processes:

- Giving opinion on new credit placements
- Giving opinion on proposals for changes in conditions of the existing placements
- Analysis of acceptability of the proposal for the renewal and restructuring of the existing placements
- Periodical review of all existing placements

In performing the analysis of 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 informs about its attitudes/principles of credit risk acceptability assessment individuals and bodies competent for making decision on loan approvals.

Further competences of employees engaged in placement analysis relate to the process of monitoring the credit risk exposure, including also monitoring the indicators for early detection of increased credit risk. The scope of work and responsibility of the Risk Management Service includes the credit portfolio control activity, which ensures, in cooperation with other bank's organisational units, timely identification of clients with potential risk. The aims of such approach are a complex management of business relations with clients, directed at decreasing credit risk costs, and at improving the quality of the Bank's credit portfolio.

Credit risk control is based on individual approach to the credit risk assessment in relation to individual clients, including identification of clients with potential risk, analysis and classification of clients with potential risk, determining the form and manner of managing business relations with clients, and the supervision of the activity implementation (*follow up*).

Special attention is paid to management of exposures to related parties, on the basis of the effective organisational normative and operative regulations, as well as other aspects of credit risk exposure, defined by the Credit Institutions Act and by-laws and internal acts for its implementation.

38.1.1. Credit risk measurement

Loans and receivables (including contingencies)

The Bank estimates the probability of defaults in settling liabilities of individual clients using internal assessment tools created for all groups of clients, in line with the internal acts and effective legal regulations.

Loans and contingencies are divided in three main risk groups:

1.1. fully recoverable loans (risk group A) – loans for which it is estimated they will be fully collected (principal and interest) and contingencies on the basis of which it is expected that no Bank's resources outflow will occur or if the outflow occurs, that they will be fully recovered.

1.2. partially recoverable loans (risk group B) – loans for which it is estimated they will not be collected in the contracted amount (principal and interest), and contingencies on the basis of which it is expected that Bank's resources outflow will occur exceeding the estimated recoverable amount.

1.3. unrecoverable loans (risk group C) – loans for which it is estimated they are fully uncollectible, or collectible in insignificant amounts, and contingencies on the basis of which it is expected that Bank's resources outflow will occur assessed as fully unrecoverable.

Credit risk management on the basis of the credit risk deterioration (*workout* or “non-performing” or “bad” loans) is performed by a separate organisational unit responsible for collecting these receivables (Department for managing loans with risk) for 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.

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

- on an individual basis

  - for loans that are not included in the “small loans portfolio”

- on a collective basis

  - for loans classified in risk group “A”;

  - for loans classified in the “small loans portfolio”;

  - for all loans to one debtor in bankruptcy procedure, if the Bank does not have the status of a creditor with special treatment and assesses these loans on an individual basis.

The small loans portfolio makes 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 estimation date exceeds HRK 250,000.

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

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

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

- in assessing identified losses for loans included in the small loans portfolio.

38.1.2. Risk limit control and policies for risk mitigation

The Bank manages, limits and controls credit risk concentrations wherever such risk is identified – especially with respect to individual clients and groups, industry sectors and countries.

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 economic segments. Limitations on the credit risk level to products, industry sectors and countries are approved by the Bank's management.

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

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

(a) Security instruments

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

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

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

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

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

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

(b) Commitments related to loans

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.

By issuing guarantees, the Bank is also exposed to credit risk. With the aim to reduce the credit risk cost, guarantees are generally secured by appropriate security instruments.

38.1.3. Policies for impairment and provisions

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

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

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

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

Exceptionally, the Bank does not determine the present value of expected future cash flows on partially recoverable loans by discounting them, if the time period in which the future cash flows are expected from these loans is less than one year of the balance sheet date. In this case, it is considered that the loss on a partially recoverable loan equals the difference between the loan carrying amount and expected future cash flows from the loan.

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

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

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

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

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

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

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

For the remainder of non-performing loans classified in the small loans portfolio (exposure below HRK 250 thousand) special provisions for impairment are calculated based on the repayment on time criteria.

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

1) Risk group "A" includes fully recoverable loans. For a loan to remain classified in the risk group "A", the following conditions must be met:

- the debtor's past due liabilities to the Bank are not older than 90 days
- the full loan amount is covered by a guarantee deposit.

2) Risk group "B" or "C" loans must be provided for on the basis of the number of days of late payment according to specially determined tables

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

- unsecured loans (default in payments > 90 days);
- loans classified in the 100% provision position according to specially determined tables.

38.1.4. Debt securities

For the purpose of realising future yield, the Bank places excess liquidity in government debt securities and foreign bonds of the highest rating or rating acceptable according to the CNB methodology.

38.1.5. Loans due

Loans due (II method DNP) by types of loans as at 31 December 2013

in thousands of HRK

Due	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Up to 30 days	144	7,910	4,177	3,537	31	4,233	20,033
31-60 days	215	8,522	1,130	-	9	1,126	11,001
61-90 days	39	9,473	34	-	4	188	9,738
over 90 days	6,185	167,977	21,767	2,930	491	85,446	284,795
Total	**6,583**	**193,881**	**27,108**	**6,467**	**535**	**90,993**	**325,567**

Loans due (II method DNP) by types of loans as at 31 December 2012

in thousands of HRK

Due	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Up to 30 days	255	4,479	10,284	3,477	30	1,200	19,725
31-60 days	181	4,604	1,704	32	10	1,967	8,498
61-90 days	259	1,010	118	41	5	231	1,664
over 90 days	5,872	147,598	19,753	2,839	301	74,248	250,611
Total	**6,567**	**157,691**	**31,859**	**6,389**	**346**	**77,646**	**280,498**

Using method II delay is shown in time classes as the debt was created, excluding the undue part.

38.1.6. Loans of unimpaired value

Loans of unimpaired value as at 31 December 2013

in thousands of HRK

	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Undue	54,263	620,347	69,803	34,533	23,985	563,785	1,366,716
Due	108	7,243	4,258	784	31	4,310	16,733
Total	**54,371**	**627,590**	**74,061**	**35,316**	**24,016**	**568,095**	**1,383,450**

Loans of unimpaired value as at 31 December 2012

in thousands of HRK

	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Undue	44,099	359,037	98,886	14,227	14,029	259,181	789,459
Due	139	4,852	9,177	504	28	605	15,305
Total	**44,238**	**363,889**	**108,063**	**14,731**	**14,057**	**259,786**	**804,764**

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

38.1.7. Loans of impaired value

Loans of impaired value as at 31 December 2013

in thousands of HRK

	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Undue	1,136	124,529	13,312	21	171	43,825	182,994
Due	6,474	186,639	22,850	5,684	504	74,965	297,117
Total	**7,611**	**311,168**	**36,162**	**5,705**	**675**	**118,790**	**480,111**
Impairment	**6,749**	**139,620**	**13,570**	**5,067**	**357**	**59,260**	**224,623**

Loans of impaired value as at 31 December 2012

in thousands of HRK

	Cash	Investments and working capital	Agriculture and tourism	Credit cards and overdrafts	Housing	Other	Total
Undue	2,385	156,740	20,182	64	461	25,612	205,444
Due	6,427	152,839	22,682	5,884	318	77,043	265,193
Total	**8,812**	**309,579**	**42,864**	**5,948**	**779**	**102,655**	**470,637**
Impairment	**6,518**	**133,190**	**14,717**	**5,010**	**487**	**57,822**	**217,744**

38.1.8. Placement structure by sector

Placement structure by sector as at 31 December 2013 *in thousands of HRK*

Sector	Total placements and off-balance sheet liabilities	Placements of unimpaired value	Placements of impaired value	Impairment and provisions	% of impairment
Agriculture, hunting, forestry and fishing	251,072	196,631	54,441	20,923	8.33
Manufacturing	264,476	113,946	150,529	59,907	22.65
Construction	492,053	397,615	94,437	69,652	14.16
Wholesale and retail trade, repair of motor vehicles and household items	317,551	205,067	112,484	46,013	14.49
Service activities	**186,916**	**149,071**	**37,845**	**19,502**	10.43
Financial intermediation	282,396	282,382	14	2,838	1.00
Foreign financial institutions	192,575	192,575	-	1,926	1.00
CNB	282,632	282,632	-	112	0.04
Other activities	**89,362**	**70,414**	**18,949**	**7,264**	8.13
Sectors outside of NKD	199,094	**152,029**	**47,065**	**33,117**	16.63
TOTAL	**2,558,127**	**2,042,362**	**515,765**	**261,254**	-

Placement structure by sector as at 31 December 2012 *in thousands of HRK*

Sector	Total placements and off-balance sheet liabilities	Placements and off-balance sheet liabilities by groups		Impairment and provisions	% of impairment
		Placements of unimpaired value	Placements of impaired value		
Agriculture, hunting, forestry and fishing	207,993	151,265	56,728	18,017	8.66
Manufacturing	219,855	95,171	124,684	56,056	25.50
Construction	201,756	105,997	95,759	59,980	29.73
Wholesale and retail trade, repair of motor vehicles and household items	229,660	103,928	125,732	44,106	16.04
Service activities	**197,523**	**163,373**	**34,150**	**18,615**	**9.42**
Financial intermediation	117,159	117,146	13	13	0.01
Foreign financial institutions	97,926	97,926	-	-	-
CNB	168,020	168,020	-	-	-
Other activities	**140,238**	**119,960**	**20,278**	**4,075**	**0.96**
Sectors outside of NKD	155,882	**107,565**	**48,317**	**29,800**	**19.12**
TOTAL	**1,736,012**	**1,230,351**	**505,661**	**230,663**	**-**

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

in thousands of HRK

	Individuals	Legal entities	Total
31 December 2013			
Total amount of exposure	46,858	468,907	515,765
Provisions	32,758	225,261	258,019
Market value of security instruments	46,553	1,000,417	1,046,970

in thousands of HRK

	Individuals	Legal entities	Total
31 December 2012			
Total amount of exposure	27,816	709,564	737,380
Provisions	17,990	198,398	216,388
Market value of security instruments	45,304	937,667	982,971

38.1.10. Restructured loans

38.1.1. Restructured loans

in thousands of HRK

	2013	2012
Restructured loans and receivables to customers		
- with value decreased after restructuring	232	1,324
Restructured loans and receivables to customers		
- that would be transferred to B1 risk group if not restructured	69	393
- that would remain in risk group A even if not restructured	7,663	43,665
Total	**7,964**	**45,382**

38.2. Liquidity risk

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

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

Cost rates are calculated by the Financial Markets Sector, Treasury Department, on the basis of the data from the WEB report "SPP report on the average interest rate as at..." The report does not include funds received from the Croatian Bank for Reconstruction and Development.

Internal prices of products are approved by the Asset-Liability Committee (hereinafter: the ALCO Committee).

Internal prices are calculated on a monthly basis, directly prior to the ALCO Committee meeting. Internal prices are confirmed by the ALCO Committee and they are effective until their following meeting. The Risk Management Service is responsible for controlling the limit, and if some of the limits are exceeded, it must immediately inform the Management Board, the Liquidity Committee and the Asset-Liability Committee. On the relevant meeting of the Asset-Liability Committee it is decided whether the limit excess is acceptable until a certain date or the Treasury Department has to bring indicators within the prescribed limits in accordance with the strategy determined at the Asset-Liability Committee meeting.

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

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

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

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

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

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

Liquidity risk management is realized by operative management of short-term liquidity and by management of long-term liquidity. Management of short-term liquidity is realized with maintenance of a regular liquidity reserve in kuna 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.

Future outflows under financial liabilities that as at 31 December 2013 contain undiscounted cash flows including future interest payments in the amount of HRK 20.3 million on received deposits and borrowings classified by maturities. Assets positions are classified by maturities of carrying amounts.

in thousands of HRK

2013	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 3 years	Over 3 years	Total
ASSETS						
Cash	266,877	-	-	-	-	**266,877**
Receivables from the Croatian National Bank	192,094		-	-	-	**192,094**
Placements with banks	57,119	-	378	-	-	**57,497**
Financial assets held for trading	5,081	-	-	-	-	**5,081**
Financial assets available for sale	589	48,809	210,394	19,524	54,179	**333,495**
Financial assets held to maturity	272	1,267	610	-	-	**2,149**
Loans and advances to customers	231,505	101,220	237,804	501,720	557,569	**1,629,818**
Investments in subsidiaries	-	-	-	-	36,095	**36,095**
Property, plant and equipment	-	-	-	-	20,921	**20,921**
Intangible assets	-	-	-	-	2,715	**2,715**
Foreclosed assets	-	-	-	-	25,810	**25,810**
Deferred tax assets	-	-	-	-	22,761	**22,761**
Other assets	33,240	-	-	-	-	**33,240**
Total assets	**786,777**	**151,296**	**449,186**	**521,244**	**720,050**	**2,628,553**
LIABILITIES						
Liabilities to banks	22,041	57,819	76,479	-	-	**156,339**
Demand deposits	338,204	-	-	-	-	**338,204**
Time deposits	190,416	295,566	818,872	292,985	13,370	**1,611,209**
Borrowings	37,877	27,676	29,708	89,734	128,419	**313,414**
Other liabilities	21,734	-	-	-	-	**21,734**
Provisions	12,709	-	-	-	-	**12,709**
Issued hybrid instruments	0	-	-	-	-	**-**
Total liabilities	**622,981**	**381,061**	**925,059**	**382,719**	**141,789**	**2,453,609**
EQUITY						
Share capital	-	-	-	-	474,600	**474,600**
Accumulated loss	-	-	-	-	(256,315)	**(256,315)**
Revaluation reserves	-	-	-	-	1,584	**1,584**
Loss for the year	-	-	-	-	(24,644)	**(24,644)**
Total equity	**-**	**-**	**-**	**-**	**195,225**	**195,225**
Total liabilities and equity	**622,981**	**381,061**	**925,059**	**382,719**	**337,014**	**2,648,834**
Net assets/liabilities and equity	163,796	(229,765)	(475,873)	138,525	383,036	-

Future outflows under financial liabilities that as at 31 December 2012 contain undiscounted cash flows including future interest payments in the amount of HRK 43 million on received deposits and borrowings classified by maturities. Assets positions are classified by maturities of carrying amounts.

in thousands of HRK

	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 3 years	Over 3 years	Total
ASSETS						
Cash	90,710	-	-	-	-	**90,710**
Receivables from the Croatian National Bank	38,909	18,256	46,337	17,381	8,349	**129,232**
Placements with banks	116,170	22,637	-	-	-	**138,807**
Financial assets available for sale	212,141	54,471	122,328	26,825	21,184	**436,949**
Financial assets held to maturity			2,542			**2,542**
Loans and advances to customers	144,293	47,197	180,962	199,810	469,573	**1,041,835**
Investment property	-	-	-	-	36,095	**36,095**
Property, plant and equipment	-	-	-	-	21,389	**21,389**
Intangible assets	-	-	-	-	3,174	**3,174**
Foreclosed assets		5,176	11,471	7,504	-	**24,151**
Deferred tax assets	-	-	-	-	22,761	**22,761**
Other assets	22,526	-	814	7,057	6,095	**36,492**
Total assets	**624,751**	**147,737**	**364,454**	**258,577**	**588,620**	**1,984,137**
LIABILITIES						
Liabilities to banks	32,078	619	139,644	8	4,004	**176,353**
Demand deposits	277,591	-	-	-	-	**277,591**
Time deposits	100,699	56,870	567,843	322,252	16,979	**1,064,643**
Borrowings	28,095	653	33,654	6,887	192,801	**262,090**
Other liabilities	7,153		12,733	-	-	**19,886**
Provisions	10,994	-	21	85	507	**11,607**
Issued hybrid instruments	-	-	-	-	-	**-**
Total liabilities	**456,610**	**58,142**	**753,895**	**329,232**	**214,291**	**1,812,170**
EQUITY						
Share capital	-	-	-	-	474,600	**474,600**
Accumulated loss	-	-	-	-	(193,218)	**(193,218)**
Revaluation reserves	-	-	-	-	1,767	**1,767**
Loss for the year	-	-	-	-	(67,211)	**(67,211)**
Total equity	**-**	**-**	**-**	**-**	**215,937**	**215,937**
Total liabilities and equity	**456,610**	**58,142**	**753,895**	**329,232**	**430,228**	**2,028,107**
Net assets/liabilities and equity	168,141	89,595	(389,441)	(70,655)	158,392	-

38.3. 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 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
- Commodity risk (not represented in the Bank)

Interest rate risk is defined by the impact of changes in market interest rates on the bank's financial results. 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 Committee 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.

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

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

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

38.3.1. Currency risk

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

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

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

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

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

The Value at Risk method measures the maximum expected loss for the Bank in case of most unfavourable foreign currency movements in an observed time interval with normal market conditions and a given level of significance based on historical data. The Bank directs its business activities primarily trying to minimize the mismatch between assets' and liabilities' items denominated in foreign currency or carrying a FX clause. The Bank is trying to manage its assets and liabilities in a way that maintains currency compatibility of individual assets' and liabilities' items in the goal of optimizing the relationship between risk and profitability in unfavourable intercurrency movements.

FX assets and liabilities of the Bank as at 31 December 2013 are shown as follows:

in thousands of HRK

2013	EUR	USD	Other	HRK with FX clause	Total FX equivalents	HRK	Total
ASSETS							
Cash	99,106	42,784	23,536	-	165,426	101,451	**266,877**
Receivables from the Croatian National Bank	26,434	-	-	-	26,434	165,660	**192,094**
Placements with banks	49,532	-	7,965	-	57,497	-	**57,497**
Financial assets held for trading		-	-	-	-	5,081	**5,081**
Financial assets available for sale	39,568	-	-	19,899	59,467	274,028	**333,495**
Financial assets held to maturity	-	-	-	-	-	2,149	**2,149**
Loans and advances to customers	407,770	4,742	490	771,325	1,184,327	445,491	**1,629,818**
Investment property	-	-	-	-	-	36,095	**36,095**
Property, plant and equipment	-	-	-	-	-	20,921	**20,921**
Intangible assets	-	-	-	-	-	2,715	**2,715**
Foreclosed assets	-	-	-	-	-	25,810	**25,810**
Deferred tax assets	-	-	-	-	-	22,761	**22,761**
Other assets	2,225	-	1	-	2,226	31,014	**33,240**
Total assets	**624,635**	**47,526**	**31,992**	**791,224**	**1,495,377**	**1,133,176**	**2,628,553**
LIABILITIES							
Liabilities to banks	27,588	79	280	-	27,947	126,465	**154,412**
Demand deposits	81,347	3,664	6,918	-	91,929	246,275	**338,204**
Time deposits	1,080,770	45,992	27,305	34,622	1,188,689	415,933	**1,604,622**
Borrowings	22,913	-	-	187,985	210,898	90,749	**301,647**
Other liabilities	-	-	-	47	47	21,687	**21,734**
Provisions	-	-	-	-	-	12,709	**12,709**
Issued hybrid instruments	-	-	-	-	-	-	**-**
Total liabilities	**1,212,618**	**49,735**	**34,503**	**222,654**	**1,519,510**	**913,818**	**2,433,328**
EQUITY							
Share capital	-	-	-	-	-	474,600	**474,600**
Accumulated loss	-	-	-	-	-	(256,315)	**(256,315)**
Revaluation reserves	-	-	-	-	-	1,584	**1,584**
Loss for the year	-	-	-	-	-	(24,644)	**(24,644)**
Total equity	**-**	**-**	**-**	**-**	**-**	**195,225**	**195,225**
Total liabilities and equity	**1,212,618**	**49,735**	**34,503**	**222,654**	**1,519,510**	**1,109,043**	**2,628,553**
Net assets/liabilities and equity	(587,983)	(2,209)	(2,511)	568,570	(24,133)	24,133	-

FX assets and liabilities of the Bank as at 31 December 2012 are shown as follows:

in thousands of HRK

2012	EUR	USD	Other	HRK with FX clause	Total FX equivalents	HRK	Total
ASSETS							
Cash	18,408	9,307	11,482	-	39,197	51,513	**90,710**
Receivables from the Croatian National Bank	-	18,061	-	-	18,061	111,171	**129,232**
Placements with banks	81,622	8,590	38,595	-	128,807	10,000	**138,807**
Financial assets available for sale	61,133			82,420	143,553	293,396	**436,949**
Financial assets held to maturity	-	-	-	-	-	2,542	**2,542**
Loans and advances to customers	75,456	17,180	544	608,281	701,461	340,374	**1,041,835**
Investment property	-	-	-	-	-	36,095	**36,095**
Property, plant and equipment	-	-	-	-	-	21,389	**21,389**
Intangible assets	-	-	-	-	-	3,174	**3,174**
Foreclosed assets	-	-	-	-	-	24,151	**24,151**
Deferred tax assets	-	-	-	-	-	22,761	**22,761**
Other assets	-	-	-	-	-	36,492	**36,492**
Total assets	**236,619**	**53,138**	**50,621**	**690,701**	**1,031,079**	**930,297**	**1,984,137**
LIABILITIES							
Liabilities to banks	26,274	32	118,902	-	145,208	29,222	**174,430**
Demand deposits	68,803	4,049	6,953	-	79,805	197,786	**277,591**
Time deposits	608,808	50,660	34,736	34,173	728,377	305,794	**1,034,171**
Borrowings	22,637	-	-	177,219	199,856	46,544	**246,400**
Other liabilities	14,521	53	-	2,430	17,004	2,882	**19,886**
Provisions	-	-	-	-	-	11,607	**11,607**
Issued hybrid instruments	-	-	-	-	-	-	-
Total liabilities	**741,043**	**54,794**	**160,591**	**213,822**	**1,170,250**	**593,835**	**1,764,085**
EQUITY							
Share capital	-	-	-	-	-	474,600	**474,600**
Accumulated loss	-	-	-	-	-	(152,714)	**(152,714)**
Revaluation reserves	-	-	-	-	-	1,767	**1,767**
Loss for the year	-	-	-	-	-	(103,601)	**(103,601)**
Total equity	-	-	-	-	-	**220,052**	**220,052**
Total liabilities and equity	**741,043**	**54,794**	**160,591**	**213,822**	**1,170,250**	**813,887**	**1,984,137**
Net assets/liabilities and equity	(504,424)	(1,656)	(109,970)	476,879	(139,171)	116,410	-

38.3.2. Interest rate risk

Interest rate risk in the bank’s records is the risk of loss arising from possible changes in interest rates, which impact the items in the bank’s records. 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 economic value of capital due to changes in interest rates.

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

The Bank's operations are subject to 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, taking market interest rates as given.

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

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

- sensitivity analysis for interest rate risk
- 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 protection techniques/procedures (hedging operations) if required.

The table below shows assets and liabilities of the Bank at carrying value, classified into categories based on contractual price change or maturity, depending on which date is first as at 31 December 2013;

in thousands of HRK

2013	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 3 years	Over 3 years	Non-interest-bearing	Total
ASSETS							
Cash	254,131	-	-	-	-	12,746	**266,877**
Receivables from the Croatian National Bank	35,976	-	156,118	-	-	-	**192,094**
Placements with banks	57,497	-	-	-	-	-	**57,497**
Financial assets held for trading	-	-	-	-	-	5,081	**5,081**
Financial assets available for sale	5,000	49,302	210,323	19,803	48,885	182	**333,495**
Financial assets held to maturity	-		2,149	-	-	-	**2,149**
Loans and advances to customers	568,519	91,175	753,153	84,872	35,221	96,878	**1,629,818**
Investment property	-	-	-	-	-	36,095	**36,095**
Property, plant and equipment	-	-	-	-	-	20,921	**20,921**
Intangible assets	-	-	-	-	-	2,715	**2,715**
Foreclosed assets	-	-	-	-	-	25,810	**25,810**
Deferred tax assets	-	-	-	-	-	22,761	**22,761**
Other assets	-	-	-	-	-	33,240	**33,240**
Total assets	**921,123**	**140,477**	**1,121,743**	**104,675**	**84,106**	**251,348**	**2,628,553**
LIABILITIES							
Liabilities to banks	22,425	56,523	75,464	-	-	-	**154,412**
Demand deposits	359	-	337,845	-	-	-	**338,204**
Time deposits	250,005	437,689	782,190	130,346	4,392	-	**1,604,622**
Borrowings	48,291	26,688	52,975	63,894	109,799	-	**301,647**
Other liabilities	-	-	-	-	-	21,734	**21,734**
Provisions	-	-	-	-	-	12,709	**12,709**
Total liabilities	**321,080**	**520,900**	**1,248,474**	**194,240**	**114,191**	**34,443**	**2,433,328**
EQUITY							
Share capital	-	-	-	-	-	474,600	**474,600**
Accumulated loss	-	-	-	-	-	(256,315)	**(256,315)**
Revaluation reserves	-	-	-	-	-	1,584	**1,584**
Loss for the year	-	-	-	-	-	(24,644)	**(24,644)**
Total equity	**-**	**-**	**-**	**-**	**-**	**195,225**	**195,225**
Total liabilities and equity	**321,080**	**520,900**	**1,248,474**	**194,240**	**114,191**	**229,668**	**2,628,553**
Net assets/liabilities and equity	**600,043**	**(380,423)**	**(126,731)**	**(89,565)**	**(30,085)**	**26,761**	**-**

The table below shows assets and liabilities of the Bank at carrying value, classified into categories based on contractual price change or maturity, depending on which date is first at 31 December 2012;

in thousands of HRK

2012	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 3 years	Over 3 years	Non-interest-bearing	Total
ASSETS							
Cash	65,804	-	-	-	-	24,906	**90,710,0**
Receivables from the Croatian National Bank	38,909	18,256	46,337	17,381	8,349	-	**129,232,0**
Placements with banks	116,170	22,637	-	-	-	-	**138,807,0**
Financial assets available for sale	212,141	54,471	122,328	26,825	21,184	-	**436,949,0**
Financial assets held to maturity	-	-	2,542	-	-	-	**2,542,0**
Loans and advances to customers	144,293	47,198	180,963	199,811	469,570	-	**1,041,835,0**
Investment property	-	-	-	-	-	36095	**36,095,0**
Property, plant and equipment	-	-	-	-	-	21,389	**21,389,0**
Intangible assets	-	-	-	-	-	3,174	**3,174,0**
Foreclosed assets	-	-	-	-	-	24,151	**24,151,0**
Deferred tax assets						22,761	**22,761,0**
Other assets	-	-	-	-	-	36,492	**36,492,0**
Total assets	**577,317**	**142,562**	**352,170**	**244,017**	**499,103**	**168,968**	**1,984,137**
LIABILITIES							
Liabilities to banks	31,659		138,771	-	4000	-	**174,430**
Demand deposits	277,591	-	-	-	-	-	**277,591**
Time deposits	97,769	52,523	556,027	316,365	11,487	-	**1,034,171**
Borrowings	27,454	-	30,637	1,000	187,309	-	**246,400**
Other liabilities	-	-	-	-	-	19,886	**19,886**
Provisions	-	-	-	-	-	11,607	**11,607**
Issued hybrid instruments	-	-	-	-	-	-	**-**
Total liabilities	**434,473**	**52,523**	**725,435**	**317,365**	**202,796**	**31,493**	**1,764,085**
EQUITY							
Share capital	-	-	-	-	-	474,600	**474,600**
Accumulated loss	-	-	-	-	-	(152,714)	**(152,714)**
Revaluation reserves	-	-	-	-	-	1,767	**1,767**
Loss for the year	-	-	-	-	-	(103,601)	**(103,601)**
Total equity	**-**	**-**	**-**	**-**	**-**	**220,052**	**220,052**
Total liabilities and equity	**434,473**	**52,523**	**725,435**	**317,365**	**202,796**	**251,545**	**1,984,137**
Net assets/liabilities and equity	**142,844**	**90,039**	**(373,265)**	**(73,348)**	**296,307**	**(82,577)**	**-**

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

	2013	2012
	in %	*in %*
Assets		
Cash	0.00 - 0.15	0.00 - 0.15
Receivables from the Croatian National Bank	0.00 - 0.00	0.00 - 0.25
Placements with banks	0.00 - 4.00	0.00 - 6.50
Financial assets available for sale	0.10 - 5.88	2.00 - 5.87
Loans and advances to customers	2.75 - 11.50	3.00 - 11.50
Liabilities		
Liabilities to banks	0.10 - 3.50	0.40 - 5.00
Demand deposits	0.05 - 2.50	0.10 - 0.40
Time deposits	0.15 - 5.30	0.10 - 5.50
Borrowings	0.00 - 5.00	0.00 - 5.00

38.3.3. Price risk

Price risk is the risk that the value of a financial instrument will fluctuate as a result of changes in market prices, whether this is caused by factors specific for an individual instrument or issuer or all factors that affect all instruments traded on the market.

38.3.4 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.

Boundaries and limits to currency risk exposure
The Bank is obliged to adjust its operations so that at any time the following structural principles are followed:

- the total open FX position, calculated using the methodology of the Croatian National Bank may not exceed the legally prescribed rate of 30% of the Bank's regulatory capital at any moment,
- the Bank internally determines that the Bank's total open FX position does not exceed 28% of the Bank's regulatory capital,
- the maximum allowed open FX position in EUR amounts to 28% of the regulatory capital,
- the maximum allowed open FX position in USD amounts to 20% of the regulatory capital,
- the maximum allowed open FX position by individual currencies, other than EUR and USD, amounts to 12% of the regulatory capital.

	Internal limit	Internal system of early warning
Bank’s total open FX position	28.00%	26.00%
Maximum open FX position in EUR	28.00%	26.00%
Maximum open FX position in USD	20.00%	18.00%
Maximum open FX position in other currencies	12.00%	10.00%

	Internal limit	Internal system of early warning	as at 31 December 2013
Bank’s total open FX position	28.00%	26.00%	1.66%
Maximum open FX position in EUR	28.00%	26.00%	1.66%
Maximum open FX position in USD	20.00%	18.00%	0.16%
Maximum open FX position in other currencies	12.00%	10.00%	0.09% for CHF

** - other currencies – the maximum allowed open FX position by individual currencies, other than EUR and USD, amounts to 12% of the regulatory capital*

Daily VAR calculation

In accordance with the provisions of Basel II agreement on market risk measurement, in the calculation of FX position exposure to changes in foreign currency exchange rates (the impact of unfavourable movements in rates on the amount of open FX position), the Bank opted for the VaR method of calculation.
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 makes the Bank's FX position in accordance with the Value-at-Risk methodology on a daily basis, and reports to the ALCO Committee at their meetings.

Date	Parameter method				Historical method	
	1 day		10 days		1 day	
	reliability 95%	reliability 99%	reliability 95%	reliability 99%	reliability 95%	reliability 99%
31 Dec 2013	-5,844	-8,252	-18,479	-26,095	-5,821	-8,144

Open FX position	% of regulatory capital	Risk value of currency risk (VaR 99% 10d)	Capital requirement (standard approach)	% of regulatory capital	Capital requirement (own model)	% of regulatory capital
-3.321.000	-1.66%	-26,095	398,520	0.13%	104,378	0.05%

Stress tests

Stress-resistance test is a risk management technique used for assessing potential impacts of specific events and/or changes in several risk factors on the Bank's financial position.
The purpose of the stress-resistance test 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) that impact the Bank's capital, risk profile and profit. The stress-resistance test may be divided into the scenario analysis and sensitivity analysis.
The scenario analysis is a type of stress-resistance test which estimates the impact of a 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-resistance test which estimates the impact of a certain risk factor on the Bank's financial position whereby the stress cause is not identified. The resistance to stress test is performed semi-annually.

The stress-resistance test for liquidity risk;

Liquidity stress test I

For testing stress-resistance of liquidity risk, the Bank presumes the liquidity shock on the market – withdrawal of deposits and inability to market the instruments3 owned by the Bank.

For this purpose, firstly the VaR analysis of deposits of individuals and legal entities in the Bank is performed (reviewing the VaR calculation at least on a quarterly basis and accordingly data for 100% percentile are adjusted), so that the amounts of deposit withdrawal are identified at percentiles of 95%, 99% and 100% reliability for various time horizons (a week, a month and three months) – the shock for Bank deposits.

Based on the (latest available) information on the shock for Bank deposits and information on the deposit withdrawal, the following scenarios are performed:

- Weekly shock on the data from the MKL form – it is presumed that the debt matures in a week (1W) and the deposits are withdrawn by 4.60% companies and individuals (VaR on weekly data of 100% percentiles = -4.60%) with anticipated expected outflows (OO form)
- Monthly shock on the data from the MKL form – it is presumed that the debt matures in a month and the deposits are withdrawn by 7.30% companies and individuals (VaR on monthly/quarterly (depending on which are higher) data of 100% percentiles = -7.30%) with anticipated expected outflows (OO form)

The Bank will apply the following scenarios for the liquidity stress-resistance test:

1. Standard stress scenario – stagnation of GDP while maintaining the standard exchange rate which results in a decrease in collection under loans of 10% and deposit withdrawal by 7.30% of companies and individuals (VaR on monthly data of 100% percentiles). For treasury bills and available-for-sale securities, the corrective factor of 10% is applied.

2. Shock scenario – real drop in GDP, causing the decrease in employment of 5% with simultaneous increase in the annual amount of loan repayment due to depreciation of HRK exchange rate against EUR, resulting in a 22%4 decrease in the collection of loans to individuals, a decrease in the collection of loans to companies by 17%5 and withdrawal of deposits by companies and individuals of 20%6. For treasury bills and available-for-sale securities, the corrective factor of 20% is applied.

3. Banking system crisis – difficulties in settling liabilities for all financial sector clients as well as delays in settling liabilities of all clients whose cash inflows depend on the state; the corrective factor of 40% is applied and in the financial sector the corrective factor of 10% is applied and withdrawal of deposits by companies and individuals of 50%[7].

[3] *It is presumed that they cannot be converted into cash immediately or in the short term so the corrective factor is applied.*
[4] *See Financial stability No.4, February 2010, p. 33.*
[5] *See Financial stability No.6, January 2011, p. 52 in the section outlining scenarios for the basic and shock scenario and fig. 90 and text on p. 53*
[6] *The percentage withdrawal of deposits of 20% includes expected outflows (OO form).*
[7] *The percentage is determined/estimated after analysing the annual financial statements of Riječka banka for 2002 (balance of deposits of individuals and companies as at 31 December 2001). The percentage withdrawal of 50% includes expected outflows (OO form).*

Liquidity stress test II

For the purposes of assessing the sufficiency of minimum required funds of liquidity reserves, the following is monitored on a monthly basis:

- the balance and changes of the total Bank deposits as follows:
  - HRK deposits
    - current and giro accounts
    - savings deposits
    - term deposits
  - foreign currency deposits
    - current and giro accounts
    - savings deposits
    - term deposits

Liquidity stress test II implies measuring the sufficiency of reserves and in the sense of this Methodology, it is defined as follows: the difference between the minimum and maximum deposit balance is determined, it is put in relation to the median, which is the basis for the liquidity stress test calculation as follows:

- HRK deposits without term (giro and current accounts and savings deposits) up to the maximum of 80% of the greatest difference (min – max balance) determined for the minimum period of two years preceding the measurement date;
- HRK term deposits up to the maximum of 30% of the greatest difference (min – max balance) determined for the minimum period of two years preceding the measurement date;
- foreign currency giro and current accounts fully the greatest difference (min – max balance) determined for the minimum period of two years preceding the measurement date;
- foreign currency savings deposits up to the maximum of 40% of the greatest difference (min – max balance) determined for the minimum period of two years preceding the measurement date;
- foreign currency term deposits up to the maximum of 20% of the greatest difference (min – max balance) determined for the minimum period of two years preceding the measurement date.

Liquidity stress test III

In addition to the above stated shock calculation for Bank deposits, the sensitivity analysis is performed in a way that percentages for the deposit decrease in the shock calculation are determined randomly. In this case, the shock is not calculated using the VaR. The reason for this are deficiencies of the VaR:

- Unlike physical values, financial values are not often normally distributed,
- Extreme (rare) losses (shocks) do not need to depend on past losses
- It is not robust when calculating the function “tail”, i.e. the amount with which the maximum expected loss with certain probability (percentile 95%, 99% etc.) is matched and significantly depends on the data used in the calculation
- Often in extreme conditions losses exceed the expected losses in a significantly larger number of cases than anticipated by the VaR.

For these reasons, in performing the sensitivity analysis for liquidity risk factors, random percentages are defined (review of the percentages is performed once a year) of deposit withdrawals from the Bank, as follows:

1. 8%
2. 12%
3. 30%

in order to determine their impact on the Bank's operations without regard to the values obtained by the VaR calculation.

The sensitivity analysis includes the following steps, i.e. the decrease in liquid liabilities of 8% results in the following steps:

1. Classifying balance sheet assets and liabilities as liquid or illiquid
2. Calculation of liquid assets (TUI) and liquid liabilities
3. Liquidity shock (decrease in liquid liabilities of 8%) results in:

    a. Decrease in liquid liabilities = liquid liabilities * 8%
    b. Revised liquid assets = liquid assets – decrease in liquid liabilities
    c. Revised liquid liabilities = liquid liabilities – decrease in liquid liabilities
    d. Revised percentage = (Revised liquid assets / revised liquid liabilities) * 100

The same methodology is applied to the decrease in liquid liabilities of 12% and 30%.

Stress test results are presented below:

	WEEKLY SHOCK – 4.60%									
	31 December 2013				30 June 2013					
	HRK		foreign currency		HRK		foreign currency		total	
	1W	1M	1W	1M	1W	1M	1W	1M	1W	1M
stress test	**1.62**	**1.26**	**1.96**	**2.05**	**2.10**	**1.44**	**2.58**	**2.03**	**2.38**	**1.73**
without stress test	**1.99**	**1.47**	**4.48**	**4.04**	**3.46**	**1.80**	**4.72**	**3.03**	**4.16**	**2.36**

	MONTHLY SHOCK – 7.30%									
	31 December 2013				30 June 2013					
	HRK		foreign currency		HRK		foreign currency		total	
	1W	1M	1W	1M	1W	1M	1W	1M	1W	1M
stress test	**1.99**	**1.17**	**4.48**	**1.59**	**3.46**	**1.29**	**4.72**	**1.70**	**4.16**	**1.50**
without stress test	**1.99**	**1.47**	**4.48**	**4.04**	**3.46**	**1.80**	**4.72**	**3.03**	**4.16**	**2.36**

	STANDARD STRESS SCENARIO				
	31 December 2013		30 June 2013		
	HRK	foreign currency	HRK	foreign currency	total
stress test	**0.81**	**1.63**	**0.77**	**1.73**	**1.25**
without stress test	**1.47**	**4.04**	**1.80**	**3.03**	**2.36**

	SHOCK SCENARIO				
	31 December 2013		30 June 2013		
	HRK	foreign currency	HRK	foreign currency	total
stress test	**0.37**	**0.73**	**0.22**	**0.92**	**0.61**
without stress test	**1.47**	**4.04**	**1.80**	**3.03**	**2.36**

	BANKING SYSTEM CRISIS				
	31 December 2013		30 June 2013		
	HRK	foreign currency	HRK	foreign currency	total
stress test	**0.42**	**0.34**	**0.36**	**0.47**	**0.43**
without stress test	**1.47**	**4.04**	**1.80**	**3.03**	**2.36**

Percentage of decrease in liquid liabilities	**8%**
Decrease in liquid liabilities	130,391,736
Revised liquid liabilities	1,499,504,965
Revised liquid assets	728,377,608
Revised percentage	48.57%

Percentage of decrease in liquid liabilities	**12%**
Decrease in liquid liabilities	195,587,604
Revised liquid liabilities	1,434,309,097
Revised liquid assets	663,181,740
Revised percentage	46.24%

Percentage of decrease in liquid liabilities	**30%**
Decrease in liquid liabilities	488,969,010
Revised liquid liabilities	1,140,927,691
Revised liquid assets	369,800,334
Revised percentage	32.41%

Resistance to stress test for interest rate risk in the bank's records

Interest rate risk in the bank's records is the risk of loss arising from possible changes in interest rates, impacting the items in the bank's records. In calculating the stress tests, the Bank uses the method of a simplified calculation of evaluation of the economic value application of the Bank's records as prescribed by the Decision on interest rate risk in the bank's records. For changing the economic value in the stress test, 200 and 300 bp are applied. Exceptionally, the movement of 500bp may be applied.

For the purposes of determining weights by time periods for 300 bp, the following weights are applied:

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

The stress test results are as follows:

in thousands of HRK

as at 31 December 2013		200 bp	300bp	500bp
NET WEIGHTED POSITION IN CURRENCY - EVKI (FKS +PKS+AKS) - currency 1	EUR	-9,906	-14,962	-24,688
NET WEIGHTED POSITION IN CURRENCY - EVKI (FKS +PKS+AKS) - currency 2	HRK	1,438	2,009	3,624
NET WEIGHTED POSITION IN CURRENCY - EVKI (FKS +PKS+AKS) - currency 3	OTHER	-458	-684	-1,140
CHANGE IN ECONOMIC VALUE		8,926	13,637	22,205
REGULATORY CAPITAL		192,865	192,865	192,865
(CHANGE IN ECONOMIC VALUE / REGULATORY CAPITAL)*100		4.63%	7.07%	11.51%

The Bank calculates the shock test of the impact of one-off increase or decrease in interest rates by 100 and 20 basis points for a period of one year.
The Bank is obliged to adjust its operations so that at any moment, the following structural principles are followed:

- a change in the economic value in relation to the regulatory capital, calculated using the Croatian National Bank methodology (200bp), may not exceed the legally prescribed rate of 20% of the Bank's regulatory capital at any time,
- a change in interest rates of 100 bp for one-year period does not exceed HRK – 6,000 thousand
- a change in interest rates of 200 bp for one-year period does not exceed HRK –10,000 thousand

	Internal limit	Internal system of early warning
Change in economic value / RC	20%	14%
Change in interest rates of 100 bp for one-year period	HRK -6,000 thousand	HRK -5,000 thousand
Change in interest rates of 200 bp for one-year period	HRK -10,000 thousand	HRK -8,000 thousand

in thousands of HRK

	Internal limit	Internal system of early warning	as at 31 December 2013
Change in economic value / RC	20%	14%	4.63%
Change in interest rates of 100 bp for one-year period	-6,000	-5,000	1,917
Change in interest rates of 200 bp for one-year period	-10,000	-8,000	3,867

38.4. Operational risk

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

The Bank is trying to accomplish optimal management of operational risk according to the principles defined by the regulator and Bank policies, and with the purpose of diminishing and mitigating operational risk. In relation to this the Bank collects data on operational risk events, follows key risk indicators, conducts scenario analysis, evaluates operational risk in its operations, reports to Management on operational risk exposure and proposes measures for diminishing, mitigating and transferring operational risk.

39. Fair value of financial assets and liabilities

Fair value represents the amount for which assets may be exchanged or liabilities settled in the best interest of the parties involved.

The table below summarizes management evaluation of fair values at year end.

Total	Carrying value		Fair value	
	2013	2012	2013	2012
Financial assets				
Loans and receivables from banks	57,497	138,807	57,497	138,807
Loans and receivables from clients	1,629,818	1,041,835	1,610,280	1,015,302
Financial liabilities				
Deposits from banks	154,412	174,430	154,412	174,430
Deposits from clients	1,942,826	1,311,762	1,915,468	1,303,164
Received loans	301,647	246,400	301,647	246,400

Loans and receivables from customers and deposits from customers are the sum of balances of legal persons and individuals that have different average variable interest rates and their effects are recorded separately in the following tables;

Legal persons	Carrying amount		Fair value	
	2013	2012	2013	2012
Financial assets				
Loans and receivables from customers	1,398,095	707,377	1,382,978	691,219
Financial liabilities				
Deposits from customers	618,046	513,321	609,634	509,142

Individuals	Carrying amount		Fair value	
	2013	2012	2013	2012
Financial assets				
Loans and receivables from customers	231,723	334,458	227,301	324,083
Financial liabilities				
Deposits from customers	1,324,780	798,441	1,305,834	794,022

A summary of principal methods and assumptions used in evaluation of fair value of financial instruments is set out below;

Loans and receivables from banks

Loans and receivables are decreased for provisions for impairment. Estimated fair value of loans and receivables represents the discounted amount of future cash flows. Future cash flows are discounted by currently valid market rates with the goal of establishing their fair value.

Considering their short maturity, Management considers carrying value does not differ from fair value.

Loans and receivables from customers

Loans and receivables are decreased for provisions for impairment. Estimated fair value of loans and receivables represents the discounted amount of estimated future cash flows. Future cash flows are discounted by currently valid market rates with the goal of establishing 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

Estimated fair value of fixed-maturity deposits is based on expected cash flows discounted by currently valid market rates on deposits with similar remaining maturities, but it cannot be lower than the nominal amount for those deposits that may at any time be claimed by clients.

Considering their short maturity, Management considers carrying value does not differ from fair value.

Deposits from clients

Estimated fair value of fixed-maturity deposits is based on expected cash flows discounted by 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 at any time be claimed by clients. The value of client relationships is not taken into account in fair value evaluation.

40. Fair value of financial instruments

Fair value represents the amount for which assets may be exchanged or liabilities settled in ordinary market conditions. Financial assets available for sale are shown at fair value, except Investments in Treasury bills that are shown at discounted value at the balance sheet date.

41. 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 adequacy rates of the Bank's capital in order to improve operations.

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

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

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

The regulatory capital of the Bank and its capital adequacy are calculated according to the CNB requirements for the Bank only, was as follows:

		in thousands of HRK
	2013	**2012**
Regulatory capital		
Base capital		
Issued equity capital	474,600	474,600
Premium on issued shares	-	-
Retained earnings (excluding profit for the year)	(256,315)	(152,714)
Profit for the year, net of proposed dividend	(24,644)	(103,601)
Legal, statutory and other reserves	-	-
Deductions according to the CNB regulations	(776)	(226)
Total base capital	192,865	218,059
Additional capital	-	-
Total additional capital	-	-
Deductions from investments in banks and other financial institutions	-	-
Total regulatory capital	**192,865**	**218,059**

As at 31 December 2013, the Bank's regulatory capital amounts to HRK 192,865 thousand (HRK 218,059 thousand in 2012).

in thousands of HRK

	2013	2012
Capital adequacy according to the CNB requirements		
Capital requirements		
Balance sheet items	142,668	129,795
Off-balance sheet items	7,448	4,459
Currency risk exposure	612	2,553
Position risk exposure	-	-
Contractual party risk exposure	-	-
Operating risk exposure	14,602	13,923
Total risk weighted assets	**165,330**	**150,730**
Capital adequacy rate	**14.00%**	**17.36%**

The comparative information presents the capital adequacy in accordance with the requirements of the Croatian National Bank. As at 31 December 2013, the capital adequacy rate is 14.00% (31 December 2012: 17.36%). The decrease in the capital adequacy rate is a consequence of a decrease in the regulatory capital of the company in 2013 by HRK 25,194 thousand with the simultaneous increase in total capital requirements by HRK 14,600 thousand.

Legal reserve

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

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 nonmonetary financial assets available for sale, net of the adequate income tax.

Accumulated loss

Accumulated loss includes accumulated losses from previous years.

42. Accounting estimates and judgments in application of accounting policies

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

a) Losses from impairment of loans and receivables

The Bank continually follows the creditworthiness of its clients. The need for impairment of balance sheet and off-balance sheet exposures to credit risk is estimated quarterly. Impairment losses are mainly recognized so that they are matched to the carrying value of loans and receivables from legal and physical entities and as provisions for liabilities and expenses resulting from risky off-balance sheet exposures to clients, most frequently in the form of approved but unused loans, guarantees and letters of credit. With losses from impairment that are individually identified the Bank also constantly observes and recognizes losses from impairment that are known to exist at the balance sheet date, but are not yet individually identified. In estimating unidentified impairment losses that exist in portfolios that are assessed as a group, the Bank is trying to collect reliable data on appropriate loss rates, that are based on historical experience adjusted for current conditions and the corresponding period of impairment losses recognition. The Bank has also shown a general provision, by the rate of 1%, determined by the CNB and applied to all exposures to credit risk, except for those valued at fair value, including off-balance sheet exposure to credit risk and the risk of central government.

The amount of general provisions as at 31 December 2013 was HRK 19,027 thousand (2012: HRK 12,293 thousand), for balance sheet and off-balance sheet exposures, according to applicable regulatory requirements.

Financial assets valued at amortized cost

The Bank foremost estimates whether there exists objective evidence of impairment, individually for assets that are individually significant (mostly exposures to legal entities) and as a group for assets that are not individually significant (mostly exposures to physical entities). However, assets not individually recognized for impairment are included in groups of assets with similar credit risk characteristics, and then evaluated as a group for impairment.

The Bank estimates impairment losses in cases when it considers available data point to probability of a measurable decrease of estimated future cash flows from assets or a portfolio of assets. As evidence the Bank considers irregularity of repayment or other indications of financial difficulty of the borrower and unfavourable changes in economic conditions affecting the borrower's operations or the value/probability of realizing collateral, when these changes can be related to the impossibility of repayment.

b) Taxes

The Bank recognizes a tax liability according to tax regulations of the Republic of Croatia. Tax applications are approved by tax administrations with authority to exercise subsequent control of taxpayers.

c) Regulatory requirements

The CNB and the Croatian Financial Services Supervisory Agency are authorized to exercise regulatory supervision over Bank's operations and may demand amendments of the assets' and liabilities' carrying value, according to appropriate regulations.

43. Concentration of assets, liabilities and off-balance sheet items

Concentration of assets, liabilities and off-balance sheet items is shown as follows:

in thousands of HRK.

	31 December 2013			31 December 2012		
	Assets	Liabilities	OBS items	Assets	Liabilities	OBS items
Geographical region						
Republic of Croatia	2,423,142	2,477,774	143,108	1,947,745	1,882,998	77,444
Europe	164,023	124,761	4	23,864	84,770	-
Other	41,388	26,018	-	12,528	16,369	-
Total geographical region	**2,628,553**	**2,628,553**	**143,112**	**1,984,137**	**1,984,137**	**77,444**
Sector						
Republic of Croatia	325,908	243,487	8,513	456,303	83,150	-
Croatian National Bank	279,806	-	-	130,538	-	-
Trade	315,613	19,171	11,840	209,945	11,680	11,593
Finance	480,811	566,238	554	54,792	520,106	908
Tourism	37,637	3,370	390	144,632	1,907	571
Agriculture	231,344	7,501	5,786	204,454	5,113	1,552
Industry	628,789	49,139	52,289	192,150	51,123	23,080
Physical entities	148,222	1,303,368	24,675	287,171	892,340	13,394
Other	180,423	436,279	39,065	304,152	418,718	26,346
Total sector analysis	**2,628,553**	**2,628,553**	**143,112**	**1,984,137**	**1,984,137**	**77,444**

Supplementary report for the Croatian National Bank

Annual financial statements are prepared according to the reporting frame and annual financial statements determined by the CNB Decision on the structure and content of annual financial statements of banks (the 'Decision').

Balance sheet

ASSETS	2013	2012
Cash	26,378	25,557
Financial assets held for trading	**5,081**	**-**
Derivatives held for trading	-	-
Equity instruments	-	-
Debt instruments	5,081	-
Loans	-	-
Financial assets at fair value through profit or loss	**-**	**-**
Equity instruments	-	-
Debt instruments	-	-
Loans	-	-
Financial assets available for sale	**333,495**	**436,950**
Equity instruments	439	705
Debt instruments	333,056	436,245
Loans	-	-
Loans and receivables (including finance lease)	**2,155,228**	**1,425,268**
Deposits with the CNB	279,806	168,020
Deposits given (except for deposits with the CNB)	210,272	158,483
Debt instruments	2,149	2,568
Loans and receivables	1,663,002	1,096,196
Investments held to maturity	**-**	**-**
Debt instruments	-	-
Loans	-	-
Derivatives used as hedging instruments	-	-
Micro hedges	-	-
Macro hedges from interest rate risk	-	-
Changes in fair value of hedged items in the hedge of portfolio from interest rate risk	-	-
Tangible assets	**82,827**	**81,635**
Property, plant and equipment	46,732	45,540
Investment property	36,095	36,095
Intangible assets	**2,714**	**3,385**
Goodwill (only in consolidation)	-	-
Other intangible assets	2,714	3,385
Investments in associates, subsidiaries and joint ventures	-	-
Tax assets	**22,761**	**22,786**
Current tax assets	-	24
Deferred tax assets	22,761	22,761
Non-current assets and groups for disposal classified as held for trading	-	-
Other assets	68	126
Less: Impairment for losses on a collective basis	-	11,570
TOTAL ASSETS	**2,628,553**	**1,984,137**

LIABILITIES		
Financial liabilities held for trading	**-**	**-**
Derivatives held for trading	-	-
Financial liabilities traded - short selling	-	-
Other financial liabilities held for trading	-	-
Financial liabilities at fair value through profit or loss	**-**	**-**
Financial liabilities valued at amortised cost	**2,398,688**	**1,732,787**
Electronic money	-	-
Transaction accounts	252,981	225,783
Savings deposits	70,422	63,861
Term deposits	1,755,624	1,178,146
Other deposits received	17,653	18,185
Borrowings	301,687	246,506
Issued debt securities	-	-
Hybrid and subordinated instruments	-	-
Other financial liabilities valued at amortised cost	320	305
Derivatives used as hedging instruments	-	-
Micro hedge	-	-
Macro hedges from interest rate risk	-	-
Changes in fair value of hedged items in the hedge of portfolio from interest rate risk	-	-
Provisions	**12,710**	**11,115**
Provisions for restructuring costs	-	-
Provisions for legal claims	8,091	8,769
Provisions for liabilities to employees	941	1,424
Provisions for pensions and other liabilities to former employees	-	-
Provisions for losses on acquired off-balance sheet liabilities	1,466	923
Provisions for onerous contracts	-	-
Other provisions	2,211	-
Tax liability	1,274	1,041
Current tax liability	1,274	599
Deferred tax liability	-	442
Liabilities included in groups for disposal classified as held for trading	-	-
Other liabilities	20,657	19,142
TOTAL LIABILITIES	**2,433,328**	**1,764,084**
CAPITAL		
Share capital	474,600	474,600
Subscribed capital	474,600	474,600
Capital gains on share issue (capital reserves)	-	-
Equity portion of complex financial instruments	-	-
Revaluation reserves	1,584	1,767
Unrealised gain (loss) on impairment of financial assets available for sale	1,584	1,767

Reserves on net foreign exchange differences	-	-
Reserves arisen from revaluation of tangible assets	-	-
Reserves arisen from revaluation of intangible assets	-	-
Reserves incurred from hedging transactions – effective portion of hedge of net investment in foreign operations	- -	- -
Reserves incurred from hedging transactions – effective portion of cash flow hedge	-	-
Reserves on the basis of tangible assets or groups for assets for disposal classified as "assets held for trading"	- -	- -
Other revaluation reserves	-	-
Reserves	-	-
Legal reserves	-	-
Statutory and other capital reserves	-	-
Capital gain (loss) on purchase and sale of treasury shares	-	-
Less: treasury shares	-	-
Retained earnings (loss)	(256,315)	(152,714)
Profit / loss for the previous year	-	-
Profit / loss for the current year	(24,644)	(103,601)
Capital attributable to majority owners (only in consolidation)	-	-
Capital attributable to minority interests (only in consolidation)	-	-
TOTAL EQUITY	**195,224**	**220,052**
TOTAL LIABILITIES AND EQUITY	**2,628,553**	**1,984,137**

Supplementary report for the Croatian National Bank (continued)

Income statement

in thousands of HRK

CONTINUED OPERATIONS	2013	2012
Interest income	113,295	89,758
Interest expenses	(65,941)	(49,736)
Net interest income	**47,354**	**40,022**
Fee and commission income	9,527	10,075
Fee and commission expense	(4,981)	(4,652)
Net fee and commission income	**4,546**	**5,423**
Income from other equity investments	-	91
Gains (losses)	4,623	3,272
Other operating income	12,586	7,221
Other operating expenses	3,442	5,356
Other non-interest income - net	**13,767**	**5,228**
Total operating income	**65,667**	**50,673**
General administrative expenses and depreciation	75,291	67,989
Net operating income before loss provisions	**(9,624)**	**(17,315)**
Provision costs and income from reversal of provisions	1,586	3,053
Impairment costs for placements and provisions for identified losses on off-balance sheet liabilities	5,304	106,650
Impairment costs and provisions for identified losses on a collective basis	8,131	(879)
Impairment costs for assets available for sale	-	223
Impairment costs for non-financial assets	-	-
Total impairment costs and provisions	**15,021**	**109,047**
Negative goodwill	-	-
Shares in profit (loss) on investments in subsidiaries, associates and joint ventures (only in consolidated statements)	-	-
Gains (losses) on non-current assets and groups for disposal held for trading not classified as discontinued operations	-	-
Total other gains (losses)	**-**	**-**
Profit (loss) from continued operations, before tax	**(24,644)**	**(126,362)**
Income tax on continued operations	-	(22,761)
Profit (loss) from continued operations, after tax	(24,644)	(103,601)
DISCONTINUED OPERATIONS	-	-
Profit (loss) from discontinued operations, after tax	-	-
Profit (loss) for the year	**(24,644)**	**(103,601)**
Profit (loss) attributable to majority owners (only in consolidation)	(24,644)	(103,601)
Profit (loss) attributable to minority interests (only in consolidation)	-	-

Cash flow statement

in thousands of HRK

POSITION	2013	2012
Operating activities		
Gains/(losses) before tax	(24,644)	(126,362)
Impairment and provisions for losses	15,019	-
Impairment of loans and other assets (net)	-	(72,535)
Provisions for contingencies (net)	-	5,562
Provisions for legal claims (net)	-	6,835
Other provisions (net)	-	
Other (gains) / losses	(4,357)	(67,544)
Cash flow from operating activities before changes in operating assets	***(13,982)***	***(181,509)***
Deposits with the CNB	(63,497)	(42,167)
MoF treasury bills and CNB bills	56,289	13,092
Deposits with banking institutions and loans to financial institutions	(41,789)	(59,037)
Loans to other customers	(597,473)	57,983
Securities and other financial instruments available for sale	47,166	147,260
Securities and other financial instruments held for trading	(5,081)	-
Securities and other financial instruments not traded actively, carried at fair value through profit or loss	-	-
Other operating assets	2,820	2,001
Net (increase)/decrease in operating assets	***(601,565)***	***119,132***
Demand deposits	27,198	39,866
Savings and term deposits	584,039	104,216
Other liabilities	36,694	(152,361)
Net increase (decrease) in operating liabilities	***647,931***	***(8,279)***
Net cash flow from operating activities before profit tax	32,384	(70,656)
Profit tax paid	-	-
Net inflow (outflow) of cash from operating activities	**32,384**	**(70,656)**
Investing activities		
Cash receipts from sales of / (payments to acquire) tangible and intangible assets	7,549	-
Proceeds for sale /(payments to acquire) investments in subsidiaries, associates and joint ventures	-	-
Cash receipts from sales of / (cash payments to acquire) securities and other financial instruments held to maturity	397	-
Dividend received	-	91
Other receipts from /(payments for) investments	(3,692)	(163,115)
Net cash flow from investing activities	**4,254**	**(163,024)**
Financing activities		
Net increase/(decrease) in received loans	55,181	(28,715)
Net increase /(decrease) in issued debt securities	-	-
Net increase /(decrease) in subordinated and hybrid instruments	-	-
Other proceeds /(payments) from financing activities		
Increase of share capital	-	130,000
Net cash flow from financing activities	**55,181**	**101,285**
Net increase / (decrease) in cash and cash equivalents	**91,819**	**(132,395)**
Cash and cash equivalents at beginning of the year	**231,577**	**363,972**
Cash and cash equivalents at end of the year	**323,396**	**231,577**

Statement of changes in equity

in thousands of HRK

Type of change	Share capital	Retained earnings /(loss)	Current year profit/(loss)	Unrealised gains/losses on value adjustments of financial assets available for sale	Total equity and reserves
Balance as at 1 January of the current year	**474,600**	**(152,714)**	**(103,601)**	**1,767**	**220,052**
Changes in fair value of the portfolio of available-for-sale financial assets	-	-	-	(183)	(183)
Net gains/losses recognised directly in equity and reserves	-	-	-	(183)	(183)
Current year profit/(loss)		-	(24,644)		(24,644)
Total current year income and expenses	-	-	(24,644)	-	(24,644)
Increase/decrease in share capital	-	-	-	-	-
Other changes	-	(103,601)	103,601	-	-
Closing balance as at 31 December of the current year	**474,600**	**(256,315)**	**(24,644)**	**1,584**	**195,225**

Adjustment of the balance sheet as at 31 December 2013

in thousands of HRK

	CNB Decision	Annual report	Difference
ASSETS			
Cash	26,378	266,877	(240,499)
Financial assets held for trading	**5,081**	**5,081**	**-**
Derivatives held for trading	-	-	-
Equity instruments	-	-	-
Debt instruments	5,081	5,081	-
Loans	-	-	-
Financial assets at fair value through profit or loss	**-**	**-**	**-**
Equity instruments	-	-	-
Debt instruments	-	-	-
Loans	-	-	-
Financial assets available for sale	**333,495**	**333,495**	**-**
Equity instruments	439	439	-
Debt instruments	333,056	333,056	-
Loans	-	-	-
Loans and receivables (including finance lease)	**2,155,228**	**1,629,818**	**525,410**
Deposits with the CNB	279,806	192,094	87,712
Deposits given (except for deposits with the CNB)	210,272	57,497	152,775
Debt instruments	2,149	2,149	-
Loans and receivables	1,663,002	1,629,818	33,184
Investments held to maturity	**-**	**-**	**-**
Debt instruments	-	-	-
Loans	-	-	-
Derivatives used as hedging instruments	-	-	-
Micro hedges	-	-	-
Macro hedges from interest rate risk	-	-	-
Changes in fair value of hedged items in the hedge of portfolio from interest rate risk	-	-	-
Tangible assets	**82,827**	**82,826**	**1**
Property, plant and equipment	46,732	46,731	1
Investment property	36,095	36,095	-
Intangible assets	**2,714**	**2,715**	**1**
Goodwill (only in consolidation)	-	-	-
Other intangible assets	2,714	2,715	1
Investments in associates, subsidiaries and joint ventures	-	-	-
Tax assets	**22,761**	**22,761**	**-**
Current tax assets	-	-	-
Deferred tax assets	22,761	22,761	-
Non-current assets and groups for disposal classified as held for trading	-	-	-
Other assets	68	33,240	(33,172)
Less: Impairment for losses on a collective basis	-	-	-
TOTAL ASSETS	**2,628,553**	**2,628,553**	**-**

LIABILITIES			
Financial liabilities held for trading	**-**	**-**	**-**
Derivatives held for trading	-	-	-
Financial liabilities traded - short selling	-	-	-
Other financial liabilities held for trading	-	-	-
Financial liabilities at fair value through profit or loss	**-**	**-**	**-**
Financial liabilities valued at amortised cost	**2,398,688**	**2,398,885**	**(197)**
Electronic money	-	-	-
Transaction accounts	252,981	338,204	(85,223)
Savings deposits	70,422	-	70,422
Term deposits	1,755,624	1,759,034	(3,410)
Other deposits received	17,653	-	17,653
Borrowings	301,687	301,647	40
Issued debt securities	-	-	-
Hybrid and subordinated instruments	-	-	-
Other financial liabilities valued at amortised cost	320	-	320
Derivatives used as hedging instruments	-	-	-
Micro hedge	-	-	-
Macro hedges from interest rate risk	-	-	-
Changes in fair value of hedged items in the hedge of portfolio from interest rate risk	-	-	-
Provisions	**12,710**	**12,710**	**-**
Provisions for restructuring costs	-	-	-
Provisions for legal claims	8,091	8,091	-
Provisions for liabilities to employees	941	941	-
Provisions for pensions and other liabilities to former employees	-	-	-
Provisions for losses on acquired off-balance sheet liabilities	1,466	1,466	-
Provisions for onerous contracts	-	-	-
Other provisions	2,211	2,211	-
Tax liability	1,274	-	1,274
Current tax liability	1,274	-	1,274
Deferred tax liability	-		
Liabilities included in groups for disposal classified as held for trading	-		
Other liabilities	20,657	21,734	(1,077)
TOTAL LIABILITIES	**2,433,328**	**2,433,329**	
CAPITAL			
Share capital	474,600	474,600	-
Subscribed capital	474,600	474,600	-
Capital gains on share issue (capital reserves)	-	-	-
Equity portion of complex financial instruments	-	-	-
Revaluation reserves	1,584	1,767	-
Unrealised gain (loss) on impairment of financial assets available for sale	1,584	1,767	-
Reserves on net foreign exchange differences	-	-	-
Reserves arisen from revaluation of tangible assets	-	-	-
Reserves arisen from revaluation of intangible assets	-	-	-
Reserves incurred from hedging transactions – effective portion of hedge of net investment in foreign operations	- -	- -	- -
Reserves incurred from hedging transactions – effective portion of cash flow hedge	- -	- -	- -
Reserves on the basis of tangible assets or groups for assets for disposal classified as “assets held for trading”	- -	- -	- -
Other revaluation reserves	-	-	-
Reserves	-	-	-
Legal reserves	-	-	-
Statutory and other capital reserves	-	-	-
Capital gain (loss) on purchase and sale of treasury shares	-	-	-

Less: treasury shares	-	-	-
Retained earnings (loss)	(256,315)	(256,315)	-
Profit / loss for the previous year			
Profit / loss for the current year	(24,644)	(24,644)	-
Capital attributable to majority owners (only in consolidation)			
Capital attributable to minority interests (only in consolidation)			
TOTAL EQUITY	**195,224**	**195,224**	**-**
TOTAL LIABILITIES AND EQUITY	**2,628,553**	**2,628,553**	**-**

Deviations of balance sheet items in the Annual report from the standard determined by the CNB Decision refer to the following categories:

ASSETS

Cash and deposits with the CNB, Deposits with banking institutions and Loans to financial institutions are items separately shown in the CNB standard, while in the Annual report those values are shown within the items Cash, Receivables from the CNB and Placements with banks.

Item Loans and receivables in the CNB standard includes receivables, while in the Annual report they are included in Other assets.

LIABILITIES AND EQUITY

Giro account and current account deposits, Savings deposits and Term deposits are items of the CNB standard, while in the Annual report these items have been included in the items Demand deposits, Term deposits and Liabilities to banks.

Derivative financial liabilities are shown separately in the CNB report; while in the Annual report they are shown within the item Other liabilities.

Tax liabilities in the CNB report are shown separately, while in the Annual report they are shown within the item Other liabilities.

Supplementary report for the Croatian National Bank (continued)

in thousands of HRK

CONTINUED OPERATIONS	CNB Decision	Annual report	Difference
Interest income	113,295	112,894	401
Interest expenses	(65,941)	(69,124)	3,183
Net interest income	**47,354**	**43,770**	**3,584**
Fee and commission income	9,527	9,803	(276)
Fee and commission expense	(4,981)	(4,981)	-
Net fee and commission income	**4,546**	**4,822**	**(276)**
Income from equity investments	-	-	-
Gains (losses)	4,623	3,767	856
Other operating income	12,586	14,827	(2,241)
Other operating expenses	3,442	-	(3,442)
Other non-interest income - net	**13,767**	**18,594**	**(4,827)**
Total operating income	**65,667**	**67,186**	**(1,519)**
General administrative expenses and depreciation	(75,291)	(75,187)	(104)
Net operating income before loss provisions	**(9,624)**	**-**	**-**
Provision costs and income from reversal of provisions	1,586	-	-
Impairment costs for placements and provisions for identified losses on off-balance sheet liabilities	5,304	-	-
Impairment costs and provisions for identified losses on a collective basis	8,131	-	-
Impairment costs for assets available for sale	-	-	-
Impairment costs for non-financial assets	-	-	-
Total impairment costs and provisions	**(15,021)**	**(16,643)**	**1,622**
Negative goodwill	-	-	-
Shares in profit (loss) on investments in subsidiaries, associates and joint ventures (only in consolidated statements)	-	-	-
Gains (losses) on non-current assets and groups for disposal held for trading not classified as discontinued operations	-	-	-
Total other gains (losses)	**-**	**-**	**-**
Profit (loss) from continued operations, before tax	**(24,644)**	**(24,644)**	**-**
Income tax on continued operations	-	-	-
Profit (loss) from continued operations, after tax	(24,644)	-	-
DISCONTINUED OPERATIONS	-	-	-
Profit (loss) from discontinued operations, after tax	-	-	-
Profit (loss) for the year	**(24,644)**	**-**	**-**
Profit (loss) attributable to majority owners (only in consolidation)	(24,644)	-	-
Profit (loss) attributable to minority interests (only in consolidation)	-	-	-

The item Interest income / Interest expenses in the CNB standard includes Income from net exchange differences.

Impairment costs on income from interest and fees and net foreign exchange differences on these impairments are presented in the supervisory report RN in items Interest income/ Interest expense and also in positions Commission and fee income / Commission and fee expense, and these positions differ accordingly. Also, premium expense for savings deposits insurance is recorded in the Annual Report in item Interest expense, and according to the CNB standard, they are recorded in Other operating expenses.

Items Other expenses, General administrative expenses and depreciation in the CNB standard comprise the item Other operating expenses in the Annual report, and the difference refers to income from reversal of provisions for legal claims filed against the Bank and provisions for liabilities to employees that are included in the item Other operating expenses in the Annual report, and in the item Provision costs and Income from reversal of provisions in the CNB standard.

Adjustment of the cash flow statement for 2012

POSITION	CNB Decision	Annual report	Difference
Operating activities			
Profit/(loss) before tax	(24,644)	(24,644)	-
Impairment and provisions for losses	16,256	-	16,256
Impairment of loans and other assets (net)	-	15,154	(15,154)
Provisions for contingencies (net)	-	543	(543)
Provisions for legal claims (net)	-	(678)	678
Other provisions (net)	-	1,237	(1,237)
Depreciation	4,484	4,484	-
Net unrealized (gains)/losses from financial assets and liabilities at fair value through profit or loss	(566)	(566)	-
(Gains)/losses from sale of tangible assets	(5,594)	(5,594)	-
Other (gains)/losses	-	-	-
Cash flow from operating activities before changes in operating assets	***(10,064)***	***(10,064)***	**-**
Deposits with the CNB	(63,497)	(63,497)	-
MoF treasury bills and CNB bills	56,289	-	56,289
Deposits with banking institutions and loans to financial institutions	(41,789)	-	(41,789)
Loans to other clients	(597,473)	-	(597,473)
(Increase) in loans and advances to customers	-	(597,473)	597,473
Securities and other financial instruments available for sale	47,166	-	47,166
Securities and other financial instruments held for trading	(5,081)	-	(5,081)
Securities and other financial instruments not traded actively, carried at fair value through profit or loss	-	-	-
Other operating assets	2,820	2,820	-
Net (increase)/decrease in operating assets	***(601,565)***	***(658,150)***	***56,585***
Demand deposits	27,198	60,613	(33,415)
Savings and time deposits	584,039	563,317	20,722
Increase/(decrease) in liabilities to banks		(20,018)	
Other liabilities	36,694	1,848	34,846
Net increase/(decrease) in operating liabilities	***647,931***	***605,760***	***42,171***
Net cash flow from operating activities before profit tax	36,302	(62,454)	98,756
Profit tax paid	-	-	-
Net inflow /(outflow) of cash from operating activities	**36,302**	**(62,454)**	**98,756**
Investing activities			
Cash receipts from sale/(payments to acquire) tangible and intangible assets	7,549	7,549	-
Cash receipts from sale/(payments to acquire) investment in subsidiaries, associates and joint ventures	-	-	-
Cash receipts from collection/(payments to acquire) securities and other financial instruments held to maturity	397	397	-
Decrease in financial assets available for sale		103,837	(103,837)
Decrease in financial assets held for trading		(5,081)	5,081
			-
Dividend received	-	-	-
Decrease/(increase) in property, plant and equipment and intangible assets		(3,692)	3,692
Other receipts from/(payments for) investments	(3,692)	-	(3,692)
Net cash flow from investing activities	**4,254**	**103,010**	**(98,756)**

Financing activities			
Net increase/(decrease) in received loans	55,247	55,247	-
Net increase/(decrease) in issued debt securities	-	-	-
Net increase/(decrease) in subordinated and hybrid instruments	-	-	-
Other proceeds/(payments) from financing activities	-	-	-
Increase of share capital	-	-	-
Net cash flow from financing activities	**55,247**	**55,247**	**-**
Net increase/(decrease) in cash and cash equivalents	**95,803**	**95,803**	**-**
Cash and cash equivalents at beginning of the year	**231,577**	**231,577**	**-**
Cash and cash equivalents at end of the year	**327,380**	**327,380**	**-**

Differences of cash flow statement items in the Annual report from the standard determined by the CNB Decision refer to the following categories:

According to the CNB standard, Impairment and provisions for losses are shown in one amount, while in the Annual report they are shown within the items Impairment of loans and other assets, Provisions for potential liabilities and Provisions for legal claims and Other provisions.

MoF treasury bills in the CNB standard together with items Securities and other financial instruments available for sale and Securities and other financial instruments held for trading comprise in the Annual report the item Decrease in financial assets available for sale and Decrease in financial assets held for trading.

Supplementary report for the Croatian National Bank (continued)

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

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

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

During 2013, Croatia banka performed its activities in the Republic of Croatia. In 2013, Croatia banka performed its services in the Republic of Croatia.

Ad.2.

In 2013, Croatia banka realised a total net income of HRK 67,186 thousand.

Ad.3.

As at 31 December 2013, Croatia banka had 263 employees based on the number of hours of work, but at the end of 2013 the actual number of employees was 278.

BUSINESS NETWORK AND CONTACTS

HEADQUARTERS

Address	Roberta Frangeša Mihanovića 9
	10110 Zagreb
Website	www.croatiabanka.hr
Telephone	0800 57 57
Fax	01 2391 244
E-mail	info@croatiabanka.hr
IBAN:	HR0324850031000009027

BUSINESS NETWORK

Town	Address	Telephone	Fax
Branch Bjelovar	Ulica Petra Zrinskog 14 43000 Bjelovar	043 241 610 043 241 611	043 241 612
Branch Čakovec	Ulica Ivana Mažuranića 2 40000 Čakovec	040 310 160 040 311 672	040 310 643
Bureau Drenovci	Veliki šor 2 32257 Drenovci	032 862 842 032 862 843	032 862 844
Branch Đakovo	Ulica A. Cesarca 7 31400 Đakovo	031 812 307 031 814 034	031 811 941
Branch Metković	Ulica S.Radića 8 20350 Metković	020 681 013 020 681 082	020 681 089
Branch Osijek	Šamačka ulica 1 31000 Osijek	031 203 001 031 203 005	031 203 002
Branch Petrinja	Šenoina bb 44250 Petrinja	044 815 641	044 815 661
Bureau Ploče	Vukovarska 17 20340 Ploče	020 670 933 020 670 934	020 676 043
Branch Poreč	Zagrebačka 2 52440 Poreč	052 451 202 052 451 304	052 451 505
Branch Požega	Cehovska ulica 3 34000 Požega	034 274 460	034 274 440
Branch Rijeka	Riva Boduli 1 51000 Rijeka	051 214 927 051 214 957	051 214 947

Town	Address	Telephone	Fax
Branch Slavonski Brod	Petra Krešimira IV 3 35000 Slavosnki Brod	035 442 112	035 442 110
Branch Split	Ulica Matice Hrvatske 1 21000 Split	021 539 795	021 539 794
Branch Vinkovci	Duga ulica b.b. 32100 Vinkovci	032 331 377 032 331 453	032 331 213
Branch Virovitica	Trg kralja Zvonimira 10 33000 Virovitica	033 725 441	033 725 602
Branch Vukovar	Dr. Franje Tuđmana 1 32000 Vukovar	032 450 520	032 450 490
Branch Zadar	Ulica Franje Tuđmana 46 23000 Zadar	023 305 294 023 305 055	023 305 130
Bureau Šubićeva, Zagreb	Šubićeva 67 10000 Zagreb	01 2391 667	01 2391 240
Branch Zagreb/ Bureau Sky Office	R.F. Mihanovića 9 10110 Zagreb	01 4623 024	01 4623 027
Branch Županja	Strossmayerova 5 32270 Županja	032 831 051	032 833 424