CROATIAN BANK FOR RECONSTRUCTION AND DEVELOPMENT

Annual financial statements for 2016

Zagreb, March 2017

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Hrvatska banka za obnovu i razvitak

ANNUAL REPORT

OF THE CROATIAN BANK FOR RECONSTRUCTION AND DEVELOPMENT GROUP

FOR 2016

March 2017

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HBOR

Hrvatska banka za obnovu i razvitak

STATEMENT OF PERSONS RESPONSIBLE FOR THE PREPARATION OF THE ANNUAL REPORT

To the best of our knowledge the 2016 Annual Report contains a truthful development of events and business results as well as the position of the Croatian Bank for Reconstruction and Development and the Group and the description of the most significant risks and contingencies the Croatian Bank for Reconstruction and Development and the Group are exposed to.

President of the Management Board

Tamara Perko, MSc

Member of the Management Board

Martina Jus

Zagreb, 17 March 2017

MANAGEMENT REPORT FOR 2016

The Annual Report includes the summary of financial information, description of operations and audited Annual Financial Statements with the Independent auditor's report for the year ended 31 December 2016. Revised Financial Statements are shown for the Croatian Bank for Reconstruction and Development Group and the Croatian Bank for Reconstruction and Development.

Legal status

The Annual Report includes the annual financial statements prepared in accordance with the International Financial Reporting Standards and the Accounting Act and audited in accordance with the International Standards on Auditing. The compliance of the Annual Report with the Annual Financial Statements has been confirmed by auditors, pursuant to Article 17 of the Accounting Act.

Exchange rate

For the purpose of converting amounts in foreign currencies into HRK, the following middle exchange rates of the Croatian National Bank have been applied:

31 December 2016	EUR 1 = HRK 7.557787	USD 1 = HRK 7.168536
31 December 2015	EUR 1 = HRK 7.635047	USD 1 = HRK 6.991801

GENERAL INFORMATION

Establishment

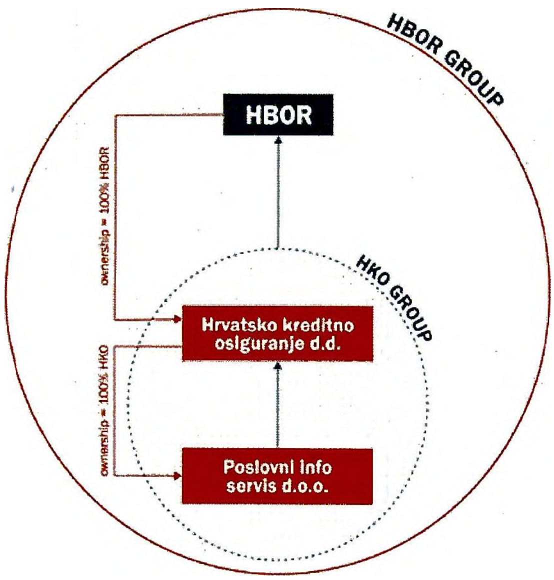
HBOR was established on 12 June 1992 by the Act on Hrvatska kreditna banka za obnovu (HKBO). The Bank was renamed Hrvatska banka za obnovu i razvitak (Croatian Bank for Reconstruction and Development) by changes and amendments to the above Act in December 1995. In December 2006, the Croatian Parliament passed a new Act on HBOR, which came into force on 28 December 2006. On 15 February 2013, the Croatian Parliament passed the Act on Amendments to the Act on the Croatian Bank for Reconstruction and Development, whereby the Supervisory Board of HBOR was amended and increased by one member – the Minister of Regional Development and EU Funds, and now consists of ten members.

Hrvatska banka za obnovu i razvitak Group

HBOR is the parent company of the HBOR group that was formed in 2010. The Group consists of the parent company, Hrvatsko kreditno osiguranje d.d. (HKO d.d.) and Poslovni info servis d.o.o. (PIS d.o.o.).

Name	Role within the Group	% of participation	Headquarters	Business activities
Hrvatsko kreditno osiguranje d.d.	Subsidiary company, direct equity participation	100% HBOR	Republic of Croatia	Insurance for company's foreign and domestic short-term receivables, regarding shipments of goods and services
Poslovni info servis d.o.o.	Subsidiary company, indirect equity participation	100% Hrvatsko kreditno osiguranje d.d.	Republic of Croatia	Providing analysis, credit risk assessment and information on creditworthiness

Illustration of the Group structure



Strategic goals of the Bank

In its operations, and within the framework of its powers and authorisations, HBOR promotes systematic, sustainable and balanced economic and social development pursuant to the overall strategic goals of the Republic of Croatia.

Priority activity areas

- Promoting start-ups and the development of SMEs
- Promoting exports
- Developing tourism
- Financing innovation and development of new technologies
- Financing the development of agriculture
- Promoting the EU Funds utilisation
- Financing projects for environmental protection, energy efficiency and renewable energy resources

Breakdown of the most significant financial information for HBOR

- In HRK million -

	2012	2013	2014	2015	2016
Total assets	25,763.23	26,162.59	25,777.05	25,540.78	27,374.92
Gross loans	24,106.96	24,941.60	24,721.41	24,722.82	26,343.12
Total equity	8,111.41	8,888.79	9,430.13	9,662.45	10,037.98
Total income	979.39	983.08	918.13	917.11	924.00
Total expense	(844.97)	(793.92)	(749.79)	(711.88)	(610.47)
Profit	134.42	189.16	168.34	205.23	313.53
Interest income	965.85	955.25	903.57	872.61	870.34
Interest expense	(555.79)	(520.91)	(490.16)	(474.53)	(452.67)
Net interest income	410.06	434.34	413.41	398.08	417.67

Credit rating as at 31 December 2016

- Ba1 by Moody's
- BB by Standard & Poor's

Regional offices

- Regional office for Slavonia and Baranja
- Regional office for Dalmatia
- Regional office for Istria
- Regional office for Lika
- Regional office for Primorje and Gorski Kotar

Number of employees

On 31 December 2016, there were 349 employees in HBOR.

On 31 December 2016, there were 364 employees in HBOR Group.

STATEMENT ON THE CODE OF CORPORATE GOVERNANCE APPLICATION

The Croatian Bank for Reconstruction and Development applies HBOR's Code of Corporate Governance dated February 2013.

HBOR's Code of Corporate Governance contains the basic principles determined by the Decision on Passing the Code of Corporate Governance in Companies with Shares or Participations owned by the Republic of Croatia (Official Gazette of the Republic of Croatia No. 112/2010, hereinafter: the Decision) and the principles determined in the European Banking Authority Guidelines on Internal Governance GL 44, September/2011, hereinafter: the Guidelines).

In accordance with the text of the Decision, the basic principles of corporate governance are applied to HBOR that it incorporated in its Code of Corporate Governance, whereas the principles stated in the Guidelines are implemented to a degree to which they are applicable due to the fact that the Guidelines relate to credit institutions and are not fully applicable to HBOR as a special financial institution.

HBOR applies fully the Code of Corporate Governance of HBOR that was adopted by the Management Board and the Supervisory Board and published on the web pages of HBOR: https://www.hbor.hr/.

In addition to HBOR's Code of Corporate Governance passed in 2013, as a measure of good corporate governance in terms of strengthening the transparency and determining the criteria for the selection of members of the Management Board of HBOR, the valid Decree on the Criteria for the Implementation of Procedures for Selection and Appointment of Presidents and Members of Management Board of Companies and Other Legal Entities of Strategic and Special Interest for the Republic of Croatia is at any time applied to HBOR. By the Decree, the requirements by which the policy of diversity in terms of age, gender, education, and profession would be applied, are not prescribed.

Compliance with laws and regulations and adherence to internal rules are the basis of responsible corporate governance and a necessary condition for sustainable business success. HBOR continuously monitors legislation and best practices in the field of corporate governance and integrates corporate governance principles in its operations pursuant to sound banking practices.

In accordance with the principles of public business, in the reporting period the financial statements of the Bank and the Group were published on the web sites of HBOR and the Luxembourg Stock Exchange. HBOR's annual financial statements on an unconsolidated and consolidated basis are confirmed by the Supervisory Board and submitted to the Croatian Parliament for approval. HBOR's rating is assessed annually by two international independent rating agencies (Standard & Poor's, Moody's). Pursuant to the Freedom of Information Act, HBOR submits a report on the implementation of this act to the Public Relations Commissioner.

In the reporting period, the duties, responsibilities and powers of the members of the Management Board and the Supervisory Board were regulated by the Act on HBOR (Official Gazette of the Republic of Croatia, No. 138/06) and by the Act on Amendments to the Act on HBOR (Official Gazette of the Republic of Croatia, No. 25/13) and further elaborated in the By-laws of HBOR. The Management Board and the Supervisory Board successfully co-operate through open discussions; the timely submission of thorough written reports to the Supervisory Board represents the basis for this co-operation. The Act on HBOR, the By-laws of HBOR and decisions made by the Supervisory Board determine the activities that HBOR may perform only with the prior consent of the Supervisory Board.

The **Supervisory Board** determines the principles of operating policy and strategy, supervises the business activities of the Bank, adopts HBOR's lending policies, adopts the Annual Financial Statements, and examines the Internal Audit reports and reports drafted by external independent auditors and by the State Audit Office. The Supervisory Board also monitors and controls the legality of the business activities of the Management Board, and appoints and dismisses the President and the members of the Management Board. In the reporting period, the Supervisory Board consisted of ten members: six ministers in the Government of the Republic of Croatia, three Members of Parliament, and the President of the Croatian Chamber of Economy.

Since the members of the Supervisory Board from among the Members of Parliament were not appointed, the Supervisory Board members until 10 November 2016 were as follows:

Zdravko Marić, DSc, Minister of Finance, President of the Supervisory Board

Tomislav Panenić, Minister of Economy, Vice President of the Supervisory Board

Tomislav Tolušić, Minister of Regional Development and EU Funds, Member

Darko Horvat, Minister of Entrepreneurship and Crafts, Member

Anton Kliman, Minister of Tourism, Member

Davor Romić, Prof.DSc, Minister of Agriculture, Member

Luka Burilović, President of the Croatian Chamber of Economy, Member

By the dismissal of members of the Supervisory Board from their duties and the appointment of new ones by the Decision of the Government of the Republic of Croatia of 10 November 2016 (appointment of members of the Supervisory Board from among the ministers) and of 9 December 2016 (appointment of members from among the members of Parliament), the Supervisory Board members are:

Zdravko Marić, DSc, Minister of Finance, President of the Supervisory Board

Martina Dalić, DSc, Deputy Prime Minister and Minister of Economy, Entrepreneurship and Crafts, Vice President of the Supervisory Board

Gabrijela Žalac, Minister of Regional Development and EU Funds, Member

Gari Cappelli, Minister of Tourism, Member

Tomislav Tolušić, Minister of Agriculture, Member

Slaven Dobrović, DSc, Minister of Environment and Energy, Member

Luka Burilović, President of the Croatian Chamber of Economy, Member

Boris Lalovac, Member of the Croatian Parliament, Member

Ivana Ninčević-Lesandrić, Member of the Croatian Parliament, Member

Grozdana Perić, Member of the Croatian Parliament, Member

The Management Board represents HBOR, conducts HBOR's business and administers its assets, and is obliged and authorised to undertake all actions and pass all resolutions it considers necessary for the legal and successful conduct of business. The powers of the Management Board also include adopting normative acts that determine the manner of operations and the internal organisation of HBOR, adopting loan programmes, making individual loan approval decisions and decisions on other financial transactions, making decisions on the appointment and dismissal of employees with special powers, making decisions on the rights and obligations of employees and reporting to the Supervisory Board. The Management Board of HBOR consists of 3 members, one of whom is the President of the Management Board.

Members of the Management Board of HBOR in 2016:

Dušan Tomašević, President of the Management Board

Goran Filipić, Member of the Management Board

Martina Jus, Member of the Management Board

In order to ensure as effective and as high quality risk management as possible and reduce the risks to the lowest level possible, the following committees operate under the Management Board: the Assets and Liabilities Management Committee, the Credit Risk Evaluation and Measurement Committee, the Information System Management Committee and the Business Change Management Committee.

On the basis of HBOR's Code of Corporate Governance and the Audit Act, the Audit Committee of HBOR has been established pursuant to the decision of the Supervisory Board. The Audit Committee is comprised of three members, one of whom is appointed from among the members of the Supervisory Board of HBOR and the other two, at least one of whom must be an independent member, are appointed by the Supervisory Board. The President is appointed by the Supervisory Board from among the independent members of the Audit Committee. Since in 2016 the Audit Committee was not appointed, the function of the Audit Committee was performed by the Supervisory Board.

The internal control system of the Croatian Bank for Reconstruction and Development is organised through independent organisational units as follows:

- independent organisational unit for risk management conducts the identification, assessment, measurement, supervision and control of all risks that HBOR is exposed or may be exposed to within the framework of its operations
- HBOR's Internal Audit, as an independent organisation unit, is in charge of verifying the adequacy of the risk management procedures and the internal control system, including risk control function and compliance function, as well as implementing the internal policies and procedures, and activities related to the prevention of money laundering
- independent compliance function organizes, coordinates and directs the activities concerning compliance at the level of HBOR, advises on matters of compliance, controls measures taken to minimize compliance risk, incorporates information on compliance monitoring, identifies and assesses the risks of compliance and provides regular reports. The main tasks of the compliance function are to limit the non-compliance risk and its possible negative effects, ensure compliance of all internal documents and business processes with the relevant regulations and promote the principles of ethical business.

  The internal control system of Hrvatsko kreditno osiguranje d.d. is organised through the following independent functions:

- compliance function
- risk management function
- internal audit function
- actuarial function

  Hrvatsko kreditno osiguranje d.d. has established an adequate internal control system on the basis of the internal regulation, the Ordinance on the Internal Control System, thus increasing the probability of timely detecting fraud and contributing to the reduction of unjustified costs, the reduction of abuse and error, the prevention of inappropriate acts and the reduction of risks related to compliance with the legislative framework. In proportion to its size, to the type, scope and complexity of operations and in accordance with its risk profile, the Company establishes permanent and effective controls that are independent from the business processes and activities in which risks arise and which they monitor and supervise.

Legal status, organisation and management of Hrvatsko kreditno osiguranje d.d. as well as other issues important for the operations of the Company are determined by the Statutes of the Company pursuant to the provisions of the Companies Act and the Insurance Act.

Company management bodies are the Management Board, the Supervisory Board and the Shareholders' Meeting. Hrvatsko kreditno osiguranje d.d. is managed by the two-member Management Board that makes its decision in accordance with the Rules of Procedure for the Management Board.

All decisions are made by following the "double check principle" ("four eyes principle") supported by the suitable system of authorisation.

Hrvatsko kreditno osiguranje d.d. has not adopted the Code of Corporate Governance, however, to the extent adequate to the size and development status of the Company, it voluntarily applies the principles of corporate governance code on its operations that have been prepared by the Croatian Financial Services Supervisory Agency (HANFA) and Zagrebačka burza d.d. (Zagreb Stock Exchange).

The Code of Conduct of HBOR prescribes specific values and rules for the prevention of corruption and assurance of professional conduct, and provides for the possibility of filing a report on the grounds of violation of the Code. The report form, the e-mail address for filing reports and the description of the filing are available on HBOR's websites. The person in charge of compliance monitoring reports annually on reports filed and proceedings initiated in respect of reports filed on the grounds of violation of the Code of Conduct. The Code of Corporate Governance establishes the standards of corporate governance and the transparency and upgrading of HBOR's operations for effective and responsible management of public capital, as well as the activities of special social significance for the development of the Croatian economy. In order to achieve the standard of corporate governance, HBOR's Code describes the relationships with governing bodies and stakeholders, as well as the adopted business principles aimed at mitigating the risks of operating in adverse market conditions.

This Statement is considered to be part of the Annual Report of the Croatian Bank for Reconstruction and Development Group for the period from 1 January to 31 December 2016.

DESCRIPTION OF OPERATIONS OF HBOR GROUP IN 2016

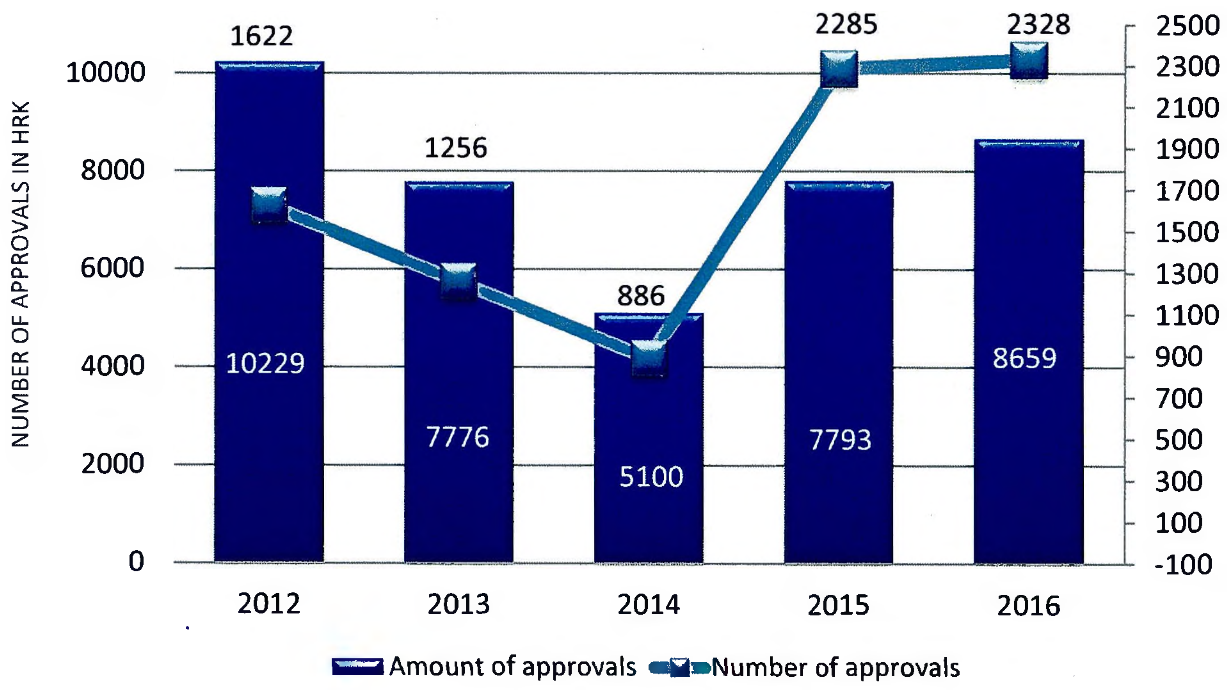
CROATIAN BANK FOR RECONSTRUCTION AND DEVELOPMENT

In 2016, HBOR conducted its operations with the aim of promoting entrepreneurs' new investments, using the proceeds of the EU funds and entering the international market. Due to the continuous enhancement of its operations and introduction of new measures and manners of lending to make favourable funds accessible to Croatian entrepreneurs more easily, in 2016, HBOR supported 2,602 projects of Croatian business entities through lending, insurance of export receivables and issuing of guarantees in the total amount of HRK 11.47 billion. The number of supported projects is the largest one in HBOR's operations so far.

In 2016, lending activity increased by 11 percent in comparison with the previous year, i.e. 2,328 loans were approved in the total amount of HRK 8.66 billion.

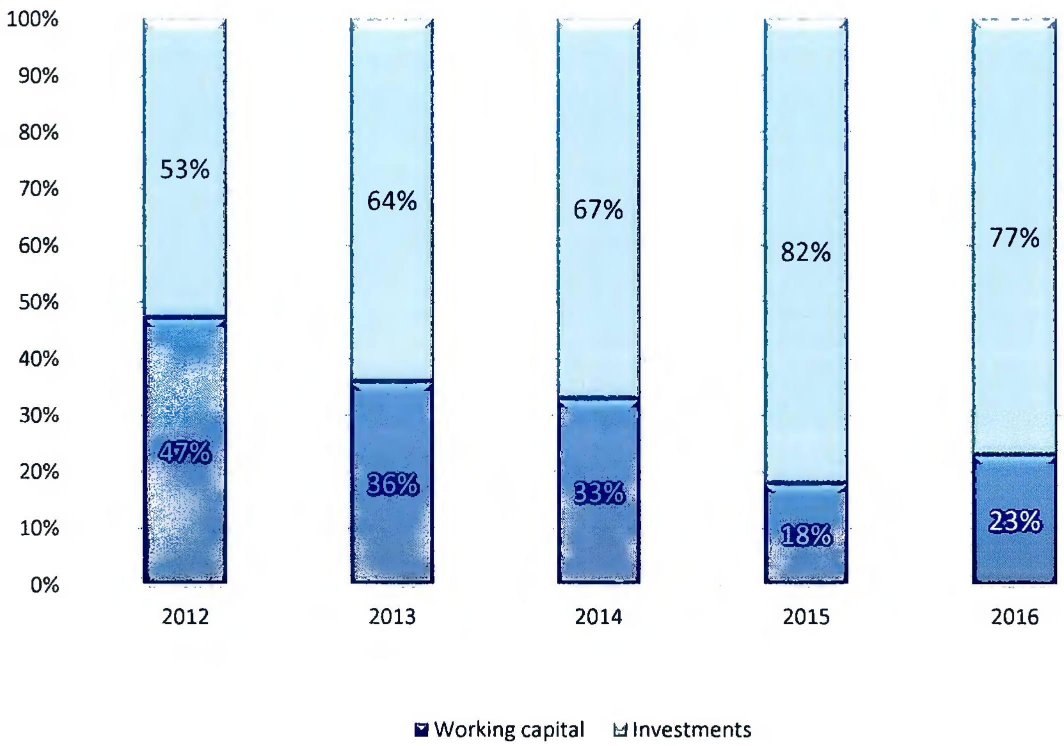
This result is particularly important, because it indicates the continuation of a positive trend that started in 2015, when the fall in lending activity was stopped. Consequently, the reporting year ended with more than 2,000 loans approved.

Amount and number of approvals, 2012 to 2016



During 2016, out of the total loans approved, 77 percent were approved for capital investments, whereas for working capital 23 percent.

Structure of approved funds by purpose from 2012 to 2016



During 2016, a significant rise in approvals for underdeveloped counties was noticed: for projects in Sisak-Moslavina county three times more funds were approved than in 2015, the financing of projects in Bjelovar-Bilogora county recorded a growth of 143 percent, in Karlovac county 73 percent, in Lika-Senj county 48 percent, and in Požega-Slavonia county and Šibenik-Knin county 31 percent in comparison with the previous year. This increase is the result of investments in manufacturing, tourism and environmental protection, but also in the projects co-financed by the proceeds of the EU funds, the funding plan of which was completed by HBOR.

SMALL AND MEDIUM-SIZED ENTERPRISES – 85 PERCENT HIGHER AMOUNT OF LOANS APPROVED

Under all loan programmes, 2,213 loans were extended to small and medium-sized enterprises totalling HRK 5.89 billion, i.e. 95 percent of all approved loans. In comparison with 2015, 85 percent higher loan volume was approved to small and medium-sized enterprises.

In 2016, loans were extended to small and medium-sized enterprises under 32 HBOR loan programmes that are implemented either directly or via commercial banks and leasing companies. In 2016, the largest number of projects was supported via leasing companies and via framework loans with more than 1.5 thousand projects supported in the amount of HRK 2.90 billion. Micro-entrepreneurs were approved 178 loans in the total amount of HRK 25.48 million through the programme Micro-loans with EU support.

By using HBOR proceeds, small and medium-sized enterprises invested almost HRK 860 million into 81 project in the tourism sector. Under the loan programme for the establishment and development of female entrepreneurship, 80 loans were approved in the amount exceeding HRK 37 million, an increase of 27 percent in comparison with 2015. For investment projects in environmental protection, infrastructure improvement and energy renovation of buildings, small and medium-sized enterprises were approved more than HRK 670 million, which is more than three times higher amount than that approved for these purposes in 2015.

MORE THAN HRK 500 MILLION APPROVED FOR INVESTMENTS IN AGRICULTURE

During 2016, HBOR also directed a part of its activities into the promotion of investments in agriculture as one of the basic branches of the Croatian economy. Via HBOR loan programmes, it is possible to finance investments in fixed assets: equipment, livestock, land, construction facilities or perennial plants, but also in the preparation of agricultural production. Agricultural producers also have at their disposal loan funds for the completion of the financial plan of the projects co-financed out of the proceeds of the EU funds.

In 2016, HRK 239 million were invested in primary agriculture and 209 projects were supported via various HBOR loan programmes. If financing of the EU rural development, fisheries and wine envelope projects are added to this figure, the amount exceeding half a billion HRK is reached.

TOURISM – INCREASE IN NUMBER OF APPROVALS BY 17 PERCENT

By favourable funds, investments in tourism are financed with the final aim of extending the tourist season. These are for the major part investments in the enhancement and extension of accommodation capacities, as well as the introduction of new services and facilities. Tourist companies recognise increasingly the advantages of utilisation of grants of the EU funds for co-financing the projects, the funding plan of which can also be completed by favourable HBOR loan programmes.

In 2016, HBOR supported 274 projects in the tourism industry with the total amount of HRK 1.81 billion, an increase of 17 percent in comparison with 2015.

More than 90 percent of loan funds were approved for investments in the Adriatic region, and the rest for continental tourism. In the so-called „sea counties", the majority of funds were approved in Split-Dalmatia county (60 projects, HRK 474.13 million) and Istria county (29 projects, HRK 456.49 million). During 2016, 76 continental tourism projects were supported in the total amount of HRK 127.36 million, of which the majority in the City of Zagreb for investments in hostels, then in Lika-Senj county, Karlovac county and Varaždin county, where investments were made mostly in the development of rural tourism.

FINANCING OF PROJECTS CO-FINANCED OUT OF THE EU FUNDS

Promoting the use of available proceeds of the EU funds is one of HBOR's priorities. For this purpose, three separate loan programmes were introduced that enabled quality and favourable completion of the funding plan for EU projects, both of private and public sectors, rural development, fisheries and wine envelope. Under HBOR loan programmes, financing of eligible, but also ineligible project costs is made possible, i.e. the completion of the funding plan of the entire investment. Financing is implemented either via commercial banks or through a direct placement on equal terms and conditions for the final borrower.

Under the programmes for the financing of projects co-financed out of the ESI funds, in 2016 HBOR approved almost 30 percent more funds in comparison with the previous year, i.e. HRK 632.10 million for co-financing of 56 projects. The majority of projects co-financed out of the EU funds for which HBOR loans were extended relates to small and medium-sized enterprises.

Beside the loan programmes, HBOR offers the possibility of using an advance payment guarantee for its direct borrowers that plan to use an advance payment in their projects with the objective to plan the sufficient liquidity level for the entire project lifetime.

Financial instruments of the EU funds

In December 2016, the Funding Agreement between HBOR and the Ministry of Regional Development and EU Funds RRFEU was signed for the purpose of initiating a new financial instrument „ESIF Growth and Expansion Loans“. Within the framework of the instrument „ESIF Growth and Expansion Loans“, long-term investment loans in the total amount of EUR 220 million with a repayment period of up to 12 years will be made available to Croatian entrepreneurs at a favourable interest rate. Through co-operation with financial intermediaries, i.e. through the network of their branch offices, this financial instrument will be made available to small and medium-sized companies operating in all regions of the Republic of Croatia. The implementation of the instrument is planned for 2017.

NEW MEASURES AND ENHANCEMENT OF OPERATIONS IN 2016

The successful operations of HBOR in 2016 is the result of measures that started to be implemented before or during 2016. The most important measures relate to the improvement of co-operation with financial intermediaries and to the reduction in interest rates. Beside the extension of individual measures to 2017, at the end of the reporting period, a decision was made on the reduction in fees for loan application processing until the end of 2017.

ENHANCEMENT OF CO-OPERATION WITH FINANCIAL INTERMEDIARIES (COMMERCIAL BANKS AND LEASING COMPANIES)

HBOR approves loan funds either directly or via commercial banks as financial intermediaries, where loan terms and conditions for the final borrower are equal, regardless of the manner of approval.

Since 2015, HBOR has been co-operating with leasing companies as financial intermediaries through which small and medium-sized companies can finance the purchase of machinery, equipment, commercial vehicles and vessels. The goal of co-operation with financial intermediaries is to make available favourable HBOR funds to entrepreneurs in all regions of the Republic of Croatia.

The share of approvals via financial intermediaries in the total approvals during 2016 increased by 64 percent in comparison with 2015, when it amounted to 43 percent. In 2016, 1,144 loans were approved via commercial banks in the total amount of HRK 4.48 billion.

This increase is the result of introduction of new ways of lending and the enhancement of co-operation with financial intermediaries:

Framework loans with commercial banks model

For the purpose of accelerating the loan approval procedure and improving the availability of favourable loans, in 2015 HBOR started to approve loans through framework loan arrangements with commercial banks. The model of financing via Framework loan arrangements was extended to a larger number of commercial banks and in 2016, the co-operation under this model was concluded with 10 largest commercial banks. Framework loans are intended for small and medium-sized companies, for the financing of investments, but also necessary working capital. Through this model, during 2016, the amount exceeding HRK 1.87 billion was made available to small and medium-sized companies. The goal of this measure is, beside the increase in lending activity via commercial banks, better regional presence of HBOR loan funds and more efficient approval of small loan amounts to a large number of borrowers.

Continued implementation of the Risk sharing model with commercial banks

With the aim of encouraging commercial banks to increase lending to business sector, in 2016 HBOR continued the implementation of the Risk Sharing Model. The Risk Sharing Model implies the manner of HBOR loan programme implementation in co-operation with commercial banks, where HBOR and the commercial bank share the risk of repayment of loan proceeds.

Leasing companies

Co-operation with leasing companies that started in 2015, opened a completely new distribution channel that enabled financing of small and medium-sized companies via financial leasing. After initial co-operation with 4 leasing companies, in 2016, the co-operation was extended to 5 new companies. In this way, HBOR enabled simpler and more favourable procurement of necessary equipment, machinery, commercial vehicles and vessels.

Entrepreneurs recognised the advantages of this co-operation very fast: the share of approvals via leasing companies increased from 4 percent in the total business activity in 2015 to 12 percent in 2016. In 2016, 991 projects were supported via leasing companies in the total amount exceeding HRK 1 billion.

REDUCED INTEREST RATES AS INCENTIVE TO INVESTMENTS

For the purpose of encouraging new investments and initiating an investment cycle, HBOR additionally reduced its interest rates for certain purposes and under certain loan programmes, and in co-operation with the European Investment Bank and the European Investment Fund, additional reduction in interest rates was made possible for innovative entrepreneurs and those employing young persons.

Extended application of interim measure of lowering interest rates by one percentage point for new investments

Lowering of interest rates applied to financing new investments in agriculture and fisheries, tourism, processing industry, energy efficiency and environmental protection projects. Pursuant to this measure, interest rate under this measure can be 2 or 3 percent p.a., depending on the size and former success of entrepreneur, and on the area of investment. Loan repayment periods for such investments are up to 17 years, with a possible grace period of 2 to 5 years. At the end of the reporting period, this measure was prolonged until 30 June 2017.

Reduced interest rates for units of local and regional government and legal entities majority-owned by them

Interest rate was reduced from 4 to 3 percent p.a. for projects of units of local and regional government and legal entities majority-owned by them, the possibility of financing in HRK was introduced and the commitment fee cancelled. At the end of 2016, interest rate for financing infrastructure investments of general importance was additionally reduced to 2.5 percent until the end of 2017.

REDUCED INTEREST RATES UNDER INDIVIDUAL LOAN PROGRAMMES

Tourism

During 2016, interest rate of 6 percent was cancelled for large enterprises for investments in tourism and it is now 2 or 4 percent, depending on the area of investment and former success of enterprises. This programme is intended for the implementation of investment projects that create conditions for encouraging employment in the tourism industry, prolongation of the tourist season and the increase in income in tourism aiming at improving the competitiveness of tourist destinations. Loans are approved with the loan repayment period of up to 17 years, including a grace period of up to 4 years.

New production and Economy

Interest rates for loan programmes Economy and New production were reduced by 1 percentage point and until the end of 2017, they will be 2 or 3 percent annually, depending on the type of the project and the area of investment. The possibility of direct lending for the programme Economy is introduced as a novelty. These programmes are intended for investments in the modernisation of production, introduction of new technologies and products, as well as investments in research and development of new products, new technologies, research of market and marketing. Repayment periods are from 12 to 14 years, including a grace period of up to 3 years, or 5 years in case of investments in planting or restructuring of perennial plants.

Pre-export finance

Under the programme Pre-export finance, basic interest rate was reduced from 4 to 3 percent. Interest rate for final borrowers is determined on the basis of the basic interest rate and margin that is determined depending on the credit rating of the client and offered collaterals.

Under the programme Pre-export finance that was implemented via commercial banks exclusively, the possibility of direct lending was introduced for small and medium-sized enterprises with assets over HRK 50 million, the income of which generated from the sale of products and services abroad amounts at least 30 percent of their operating income, and that require funds for pre-export finance in the amount exceeding HRK 10 million.

For start-up exporters that are defined as economic operators entering foreign markets for the first time ever, or entering for the first time a foreign market they have not tapped into so far, or introducing a new product and/or service on a foreign market where they are already present, the basic interest rate is 2 percent.

REDUCTION IN INTEREST RATES FOR YOUTH EMPLOYMENT AND INNOVATIVE COMPANIES

Youth employment

HBOR joined the Jobs for Youth Initiative of the European Investment Bank through which investments of small and medium-sized enterprises into education and skills as well as employment of young people are financed. The main feature of this Initiative is saving on interest rate achieved by entities employing or training young persons. Small and medium-sized companies that meet one of the prescribed criteria can make use of the reduced interest rate of 0.5 percentage points under 14 HBOR loan programmes, regardless of whether a loan is approved directly or via commercial bank. The reduced interest rate is applied to the entire loan repayment period.

Lending to innovative companies under the InnovFin SME Guarantee Facility

Thanks to HBOR's inclusion in lending under the InnovFin SME Guarantee Facility, interest rate for innovative small and medium-sized companies investing in production, development and/or implementation of new or significantly improved products, procedures or services is reduced by 0.422 or 0.572 percentage points, depending on the size of the final beneficiary. The reduced interest rates can be applied to companies which meet the prescribed criteria of innovation, and such reduction can be applied for direct approvals within the framework of the existing HBOR loan programmes. This measure is a part of the Investment Plan for Europe.

INVESTMENT PLAN FOR EUROPE

Pursuant to the Decision of the Government of the Republic of Croatia, HBOR, as the national development bank, was entrusted the key activities related to the implementation of the Investment Plan for Europe (The Juncker plan).

In the implementation of the Juncker plan, HBOR co-operates with relevant state administration bodies, agencies and other legal entities with public authorities that appointed national coordinators for the support in the implementation of the Juncker plan.

HBOR has initiated a number of activities with the objective to familiarise domestic investors and key partners with the possibilities and terms and conditions of financing under the Juncker plan. During 2016, first agreements were signed that facilitate the operations of Croatian business entities:

„InnovFin SME Guarantee Facility"

In June 2016, HBOR and the European Investment Fund (EIF) signed the Guarantee Agreement for *InnovFin SME guarantee facility* in the amount of EUR 20 million This is the first Croatian project within the framework of the Investment Plan for Europe. As previously mentioned, the Guarantee enables reduction in interest rates for enterprises which meet the prescribed criteria of innovation.

It is a guarantee product of the European Investment Fund (EIF) that covers 50 percent of principal and regular interest for loans approved by HBOR for investments of small and medium-sized companies (up to 250 employees) and small Mid-caps (250 to 499 employees) in the production, development or implementation of new or significantly improved products, procedures or services, as well as other financing of companies meeting the innovation criteria.

Guarantee Agreement for the Risk Sharing Model

In November 2016, a Guarantee Agreement for the Risk Sharing Model was signed between EIB and HBOR in the amount of EUR 50 million, i.e. the second Croatian project under the Juncker plan. Within the framework of the Risk Sharing Model, EIB provides a guarantee to HBOR in the amount of up to EUR 50 million for the partial coverage of risks under the existing portfolio of loans approved to Mid-caps. The loan portfolio may not exceed EUR 100 million and should meet certain criteria.

Since this is an indirect Risk Sharing Model, the EIB guarantee covers the existing portfolio of loans at an appropriate guarantee rate. The guarantee rate rises between 0 percent to 50 percent in proportion to the increase in newly approved loans for Mid-caps and other priorities. EIB does not take the risk of new, but exclusively of the existing, directly approved loans. In this way, it is made possible for HBOR to take additional risks and to increase its lending activity in the amount of up to EUR 100 million towards Mid-caps and other priorities.

Access to the European Investment Advisory Hub provided

For the purpose of supporting the implementation of measures for the increase of employment, growth and investments within the Juncker plan, HBOR signed the Memorandum of Understanding with EIB. The objective of the Memorandum is providing access to a wide range of advisory services of the European Investment Advisory Hub (EIAH) which provides its services both at the EU level and local level through promotional banks. The main purpose of EIAH is to provide advice to investors – private and public project promoters with the objective of preparing and monitoring of projects.

ECONOMIC CO-OPERATION FUNDS

In the second half of 2010, by the Decision of the Government of the Republic of Croatia, HBOR was appointed a qualified investor for participation in the establishment of the Economic Co-operation Funds (ECFs), investing for itself and on behalf of the Government of the Republic of Croatia in each of the ECFs an amount equal to the amount invested in the ECF in question by private investors. The field of investment of ECFs are companies which have their headquarters in the Republic of Croatia and are active exclusively or predominantly in the Republic of Croatia. The envisaged duration of investment is 10 years with the possibility of a maximum extension of up to 2 years. The maximum investment obligation of the Government of the Republic of Croatia towards one ECF amounts to HRK 300 million.

ECFs were established and operated in accordance with the Investment Funds Act (Official Gazette of the Republic of Croatia, No. 150/05), as open-end investment funds of private venture capital. At the beginning of 2011, 5 ECFs were established which met all the prescribed requirements and obtained HANFA's (Croatian Financial Services Supervisory Agency) approval for operation. In July 2013, a new Act on Alternative Investment Funds (Official Gazette of the Republic of Croatia, No. 16/13) came into force, by which the operations of ECFs are prescribed.

Pursuant to the above, in 2014 the ECF management companies carried out the adjustment of former statutory documents, the Prospectus and the By-Laws of the Fund with the Act on Alternative Investment Funds and accompanying Ordinances prescribed by the HANFA regulatory agency.

In 2016, decisions on investment into three projects were implemented in the total amount of HRK 144 million, of which 50 percent relates to the share of the Republic of Croatia. Funds were invested into companies active in the tourism and construction sectors, and in the wood industry. The companies that received investments in 2016 have 2,339 employees altogether.

EIF-NPI Equity Platform

In 2016, HBOR joined the EIF-NPI Equity Platform and became a member of the consultancy forum. The Platform represents a basis for the development of venture capital market in the Republic of Croatia and the development of concrete risk capital products that are planned to facilitate the access to funds for small and medium-sized companies employing up to 250 employees and for Mid-caps (250 – 3000 employees).

<u>HBOR AS EXPORT BANK AND EXPORT CREDIT AGENCY OF THE REPUBLIC OF CROATIA</u>

By implementing its export finance programmes, HBOR contributes to the increase in competitiveness and value of Croatian exports and improvement of the recognisability and quality of Croatian products and services in the foreign markets.

Within the framework of its export promotion task, HBOR, through its loan programmes, issuing of bank guarantees at the request of an exporter and insurance of export receivables, provides support to exporters in all stages of an export transaction, starting from negotiations until the final payment for an export transaction. HBOR, as the Croatian export bank and export credit agency, developed a system of providing exporters with financial support as other export banks and export-credit agencies in order to provide Croatian exporters with equal competitive conditions in international markets.

In 2016, beside the mentioned reduction in interest rates for funds intended for pre-export finance for all exporters, HBOR improved the terms and conditions of insurance of export receivables for exporters that agree upon the deferral of payment of up to one year with foreign buyers: the percentage of cover was increased from 85 to 90 percent, and the period of waiting for indemnity payment shortened from 5 to 3 months. In this way, more efficient liquidity management is made possible for exporters. Also, the decision was made on the continued implementation of issuing insurance policies for export credit insurance for small volume exporters and start-up exporters. Also, by retaining the additionally reduced interest rates for start-up exporters, HBOR adjusted its services to the smallest exporters or entrepreneurs considering exports for the first time ever in order to encourage the internationalisation of their operations.

Along with the programmes intended for export transactions exclusively, HBOR supports exporters through short-term and long-term credit lines at favourable interest rates. Investment loans are also available to exporters intended for expansion and modernisation of the production, construction of new plants, but also various loans for working capital that are not necessarily tied to export transaction exclusively. The utilisation of such funds is intended to increase the competitiveness of entrepreneurs, which is a precondition for the realisation of successful entry into foreign markets.

In 2016, Croatian exporters were backed by HBOR with the total amount of HRK 6.31 billion: under all loan programmes, exporters were approved 500 loans totalling HRK 3.64 billion, and through export credit insurance policies, export turnover insured amounted to HRK 1.44 billion and 20 bank guarantees at the request of exporters issued totalling HRK 1.23 billion. By issuing bank guarantees, HBOR provides support to Croatian exporters when contracting and performing export transactions, especially in cases when commercial banks are not in a position to support export transactions due to the fact that the exporter has reached its limit with them.

EXPORT CREDIT INSURANCE IN 2016

Since 1998, the Croatian Bank for Reconstruction and Development as the Croatian export credit agency for and on behalf of the Republic of Croatia performs export credit insurance against non-market political and commercial risks with the objective to promote the Croatian exports, internationalisation and increase in competitiveness of the Croatian exporters in the foreign markets.

Export credit insurance activities include a number of insurance programmes through which HBOR can insure exporter's receivables for delivered goods and services to foreign buyers, financial loans for pre-shipment or financing buyers abroad, as well as bank guarantees issued for export transactions.

In 2016, HBOR through its export credit insurance activities supported exports of capital projects in the shipbuilding, energetics, telecommunications, electronic engineering and other sectors of importance for the national economy, and exports of small and medium-sized companies that contributes to additional employment, growth of the Croatian economy, the promotion of Croatian economic interests and internationalisation of Croatian exporters.

HBOR insures the collection of short-term receivables from buyers abroad to exporters, and provides the service of reinsurance of short-term export receivables to private credit insurers for risks that may not be insured in the private insurance market. Through this service, HBOR gives additional impetus to Croatian exports and supplements the lack of supply in the credit insurance market, simultaneously respecting the rules of market competition.

With the objective to provide a complete export credit insurance service, HBOR cooperates with foreign export credit agencies through its participation in the projects in which the Croatian exporters participate with their foreign partners in third markets.

In 2016, HBOR provided insurance for the Croatian export turnover in the amount of HRK 1.44 billion.

In 2016, HBOR approved coverage to Croatian exporters and banks that support exporters in the total amount of HRK 759.52 million for newly contracted export transactions, of which the most important export transactions were realised in the markets of Algeria, the Netherlands and Armenia.

The most important transactions of Croatian exporters supported by HBOR in 2016 through export credit insurance programmes:

- Construction of the largest sailing vessel in the world for the buyer from Monaco, with an insured sum of HRK 155.16 million under the Pre-Export Financing Insurance Programme,
- Construction of a vessel for transportation of bulk cargo, with an insured sum of HRK 135.13 million under the Pre-Export Financing Insurance Programme,
- Delivery of pharmaceutical products to buyers in the Russian Federation in the amount of HRK 113.04 million under the Programme for the Insurance of Short-Term Export Receivables,
- Construction of bucket dredger with excavator for the buyer in the Netherlands, with an insured sum of HRK 88.43 million under the Programme for the Insurance of Bank Guarantees Issued for the Purpose of Winning or Performing Export Contracts,
- Delivery of telecommunication equipment and services to the buyer in Armenia, with an insured sum of HRK 86.23 million under the Supplier Credit Insurance Programme,
- Designing, construction and equipping of a military hospital for the buyer from Algeria, with an insured sum of HRK 35.87 million under the Programme for the Insurance of Bank Guarantees Issued for the Purpose of Winning or Performing Export Contracts,
- Construction of a self-elevating work platform for the buyer from Luxembourg, with an insured sum of HRK 31.70 million under the Pre-Export Financing Insurance Programme.

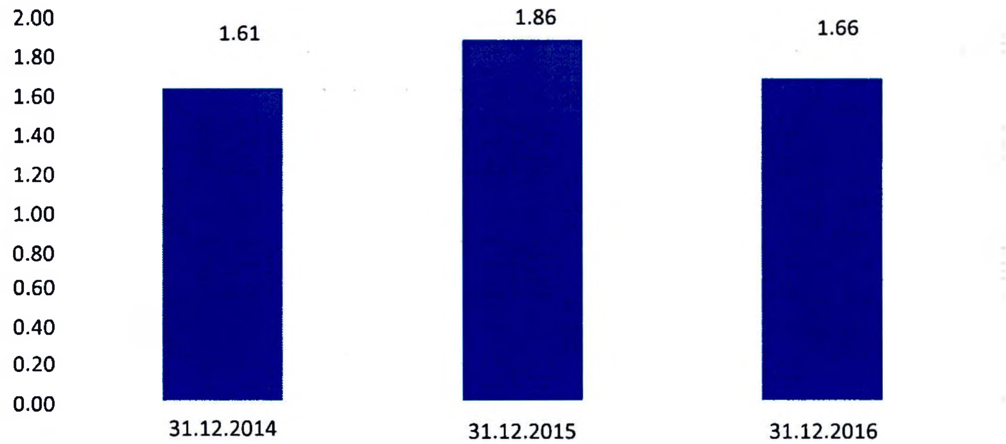
Summary of results by export credit insurance transactions, comparison 2015/2016

Description	2015	2016
Total insured export transaction	HRK 1.54 billion	HRK 1.44 billion
Insurance premium paid	HRK 22.49 million	HRK 16.30 million
Total approved new insurance	HRK 815.03 million	HRK 759.52 million
Paid indemnities to insured parties	HRK 0.87 million	HRK 8.81 million
Recourse collections from debtors	HRK 0.07 million	HRK 1.50 million
Balance of the Guarantee fund as at 31 December[1]	HRK 310.80 million	HRK 332.36 million
Gross exposure as at 31 December	HRK 1.86 billion	HRK 1.66 billion

As at 31 December 2016, gross exposure of HBOR under export credit insurance transactions amounted to HRK 1.66 billion. The expiry of the insurance policy for the guarantee upon the successfully delivered vessel in the amount of HRK 393 million for the buyer in Luxembourg had the major influence on the fall in total exposure.

The fall in exposure in relation to the previous year is for the major part the result of decrease in exposures under the Programme for the Insurance of Bank Guarantees Issued for the Purpose of Winning or Performing Export Contracts and the Programme for the Insurance of Short-Term Export Receivables.

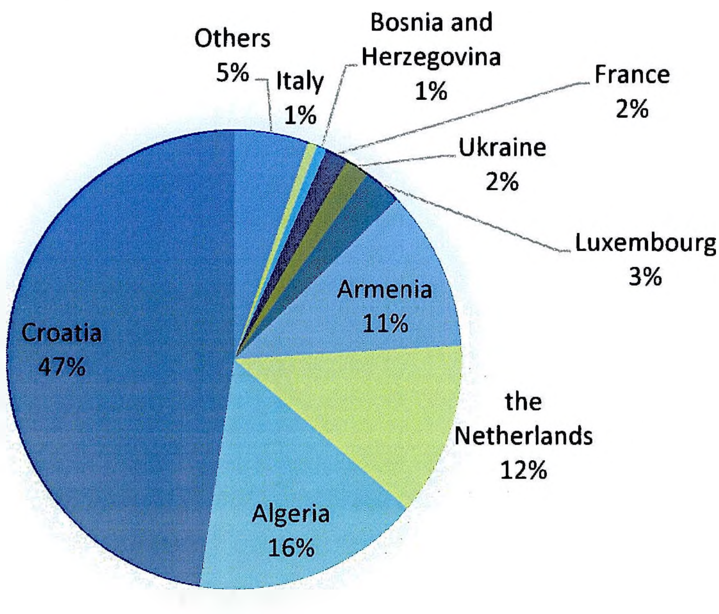
Exposure by year, in HRK billion



[1] *The Guarantee fund proceeds serve for the performance of export credit insurance transactions, payment of indemnities, coverage of expenses to prevent the occurrence of loss and for the coverage of other expenses of the insurer in the implementation of export credit insurance programmes. The proceeds of the Guarantee fund consist of payments of the Republic of Croatia from the state budget, collected insurance premiums and recourse collected funds under indemnities paid.*

In 2016, HBOR through its export credit insurance programmes supported exports of Croatian goods and services to 35 countries worldwide.

Approved insurance in 2016, by countries

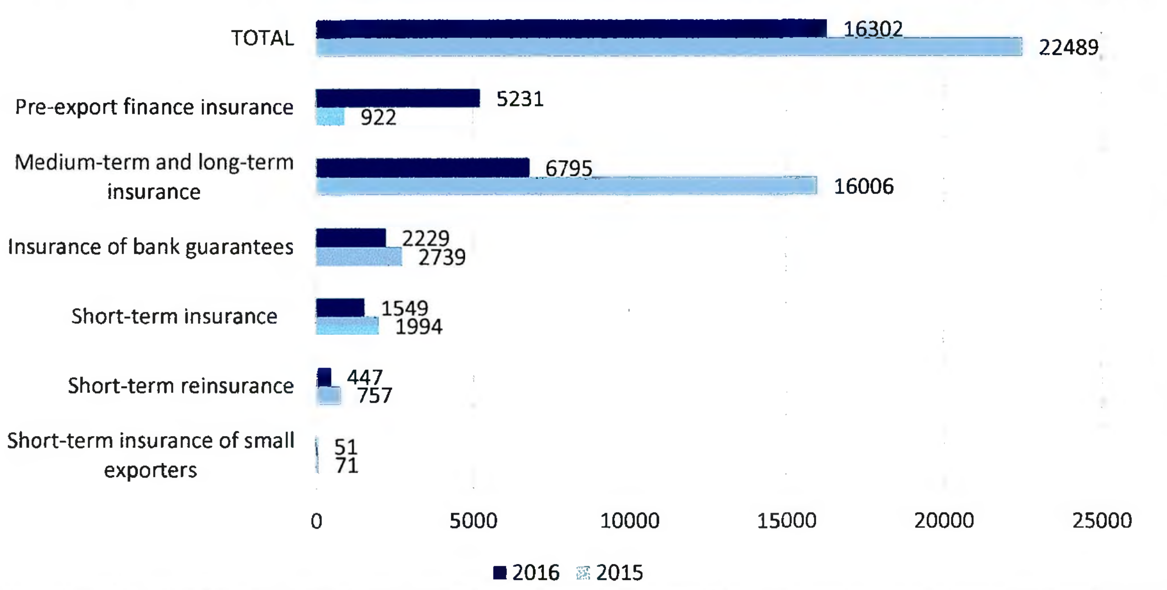


In the reporting period, the majority of risk coverage was approved for the banks which finance Croatian exporters and for exports towards the buyers in Algeria, the Netherlands, and Armenia.

INSURANCE PREMIUMS AND INDEMNITIES

In 2016, the total charged insurance premium under export credit insurance transactions amounted to HRK 16.30 million.

Premiums charged by type of insurance in 2015 and 2016, in HRK million



In 2016, 6 indemnities were paid totalling HRK 8.81 million.

The major part of indemnities paid in 2016 (97 percent or HRK 8.55 million) relates to the indemnity paid to a local bank due to the occurrence of commercial risk of loan non-repayment by the exporter, pursuant to HBOR's insurance policy for pre-export finance loan.

Other indemnities paid in 2016 are the result of the occurrence of commercial risk of prolonged non-payment by buyers from Azerbaijan, Italy, Montenegro and Kosovo. The mentioned payments of indemnities relate to the programme of insurance and reinsurance of short-term receivables collection.

In 2016, total recoveries amounted to HRK 1.50 million and two indemnities paid in previous years were completely recovered. The first of the two indemnities was paid due to the impossibility of repayment of the loan approved to an Iranian bank as a result of imposed sanctions (political risk), whereas the other one was paid due to the non-payment by an Italian buyer (commercial risk).

INSURANCE AND REINSURANCE OF SHORT-TERM EXPORT RECEIVABLES

In 2016, HBOR provided insurance of exports of consumer goods in the amount of HRK 746.69 million through its programmes of insurance and reinsurance of short-term export receivables, mostly for exporters engaged in the production of pharmaceutical products, glass package, aluminium products, wood products, and in wholesale trade. The largest export turnover with insurance coverage was realised for buyers in Serbia, the Russian Federation and Bosnia and Herzegovina.

In 2016, for the purpose of ensuring alignment with the market requirements, the Programme for the Insurance of Short-Term Export Receivables was amended for the benefit of exporters by increasing the cover percentage from 85 percent to 90 percent and by shortening the waiting period for the submission of a claim from 5 months to 3 months.

The Programme for the Insurance of Export Receivables for Exporters with Annual Export Turnover of up to EUR 2 million (insurance programme for small exporters), which was adopted at the end of 2014, was actively implemented during 2016. The Programme is intended for micro entrepreneurs, family businesses and start-ups that begin to sell their products and services in the foreign market as there are no insurance products for such businesses in the private insurance market. In 2016, the total approved insurance amount under this Programme was HRK 4.56 million. Under the Programme, the export of the processing industry was supported for the major part (sanitary facilities, PVC package, other paper and cardboard products, wood products, printing industry, etc.).

At the end of 2016, HBOR extended the implementation period of the Programme for the Insurance of Short-Term Export Receivables for Exporters with Annual Export Turnover of up to EUR 2 million until the end of 2018 for the exporters of consumer goods.

MEDIUM- AND LONG-TERM INSURANCE

For exports of capital goods and services in 2016, the insurance coverage amount of HRK 108.91 million was approved.

In 2016, the issuance of two insurance policies covering the collection of receivables in the amount of HRK 22.67 million enabled construction industry exporters to successfully continue the implementation of the fishing port construction project in the Skikda region, Algeria. In addition, the issuance of two insurance policies totalling HRK 86.32 million covered the collection of payment upon the delivery of equipment and software for the construction of LTE network in Armenia. This project is the first export transaction insured by HBOR in the Armenian market.

INSURANCE OF PRE-EXPORT FINANCING LOANS

HBOR gave additional stimulus to exports by amending the Pre-Export Financing Insurance Programme intended for exporters through the alignment of the insurance policy with the requirements of the banks in order to make insurance policies acceptable collateral from the risk management standpoint, which led to the widening of cooperation under this programme with individual commercial banks in the Republic of Croatia.

In 2016, through the Pre-Export Financing Insurance Programme, coverage for loans in the amount of HRK 361.17 million was approved for the purpose of pre-export finance of goods and services. On the basis of the approved insurance, HBOR supported exporters in the shipping, textile and metal industries. By the approval of insurance, banks were enabled to finance exporters in the stage of manufacturing goods for exports.

INSURANCE OF BANK GUARANTEES

For the purpose of increasing effectiveness, shortening application processing periods and meeting the needs of exporters, HBOR simplified the process of extending the coverage period of guarantees under the programme for the insurance of performance-related bank guarantees caused by the extensions of deadlines for the execution of export contracts. This relates to the guarantees issued at the order of exporters (performance guarantees and advance payment guarantees).

In 2016, HBOR approved coverage for issued bank guarantees in the total amount of HRK 225.63 million, where the highest amount guarantees related to the construction of a self-propelled, self-elevating platform for a buyer in Luxembourg. Besides, prolongation of the guarantee insurance was approved for export transactions in Algeria: construction and equipping of a military hospital, construction of a viaduct and construction of a fishing port, and in the Netherlands: construction of a self-propelled dredger with a digger.

In addition, by issuing insurance policies for tender guarantees for the participation in the bidding procedure related to the reconstruction of transformer stations, HBOR enabled Croatian exporters in the energy sector to enter into the market of Ukraine, thus joining the efforts aimed at supporting this market as well.

FUND RAISING: FAVOURABLE SOURCES OF FINANCE PROVIDED

In 2016, HBOR and the European Investment Bank (EIB) signed two Finance Contracts under the framework contract signed at the beginning of 2014 in the amount of EUR 800 million for the financing of SMEs and Mid-Cap companies in the Republic of Croatia.

The first Finance Contract for the financing of projects implemented by Mid-Cap companies was signed on 17 February 2016 in the amount of EUR 150 million. Mid-Cap companies are defined as those companies that have more than 250 and fewer than 3 thousand employees. The funds are earmarked for the financing of projects implemented by Mid-Cap companies primarily in the industry, services and tourism sectors as well as public and private companies investing in knowledge-based, infrastructure and environmental projects.

On 11 July 2016, HBOR and the EIB signed the second Finance Contract in the amount of EUR 250 million for the financing of projects implemented by small and medium-sized enterprises. By signing this contract, HBOR joined the implementation of the programme of the European Commission and the EIB called "Jobs for Youth Initiative".

RISK MANAGEMENT

Pursuant to the Act on HBOR, the Bank is obliged to reduce risks in its operations to the lowest level possible by applying the principles of banking operations. In the risk management process, the Bank continuously identifies, assesses, measures, monitors, contains and controls risks it is or may be exposed to in its operations. The manner, procedures and frequency of measurements and assessments in risk management are prescribed by the Bank's general documents. In the Bank's day-to-day operations, credit risk, liquidity risk, interest rate risk in the banking book, currency risk, operational risk and outsourcing risk are managed through policies, procedures, methodologies, ordinances, limits and controls.

The Bank has a functionally and organisationally separate and independent organisational unit for controlling business risks that is directly responsible to the Management Board. This organisational unit is responsible for the identification, assessment, measurement, supervision and control of risks the Bank is or may be exposed to in its operations. The Risk Management Unit performs its function also by analysing and giving suggestions and recommendations for adequate management of exposure to credit and non-credit risks, by developing risk-related policies, ordinances, procedures and methodologies, by recommending exposure limits and monitoring the adherence to the adopted exposure limits as well as by risk-related reporting to the Management Board and the risk management committees.

When assessing and measuring risks, the Bank takes into account historical data, business plans, current and expected market conditions and specific features of the Bank as a special financial institution. The results of measurements/assessments and analyses conducted in the field of risks are reported to the risk management committees, the Management Board and the Supervisory Board. A system of limits has been established for the purpose of managing, monitoring and controlling credit risk, liquidity risk, interest rate risk in the banking book and currency risk. The

Bank performs sensitivity analyses and scenario analyses by assuming changes in one or more risk factors in regular and stressful circumstances of operations and it reports on the results of such analyses to HBOR's bodies in charge. Systems of proactive risk management are continuously developed for the purpose of mitigating potential future risks.

The Management Board of HBOR is responsible for the implementation of the risk management strategy and for the establishment and implementation of an effective and reliable system for the management of all risks. For the purpose of accomplishing its function, the Management Board has delegated its powers to four risk management committees:

- Asset and Liability Management Committee – manages liquidity risk, interest rate risk in the banking book and currency risk through the prescribed policies and procedures that regulate this area
- Credit Risk Assessment and Measurement Committee – manages credit risk through the prescribed policies, procedures and other internal documents that are related to credit risk
- HBOR Information System Management Committee – manages the resources of the information system and adequately manages the risks that arise from the use of information technology
- Business Change Management Committee – manages business changes (co-ordination of the procedures for the suggestion, approval, monitoring and implementation of business changes) in order to reduce the risks associated with the implementation of business changes.

The risk management strategy aims to achieve and maintain a good and efficient system of risk management in line with the local and international banking practices and the recommendations of the Croatian National Bank (HNB), the European regulations and the Basel Committee recommendations applicable to HBOR as a special financial institution.

Credit risk

The Bank controls credit risk through credit policies, ordinances and prescribed procedures that determine the internal control systems with an objective to act preventively.

HBOR's Management Board conducts a conservative credit risk management policy. The credit risk management system represents the most important part of HBOR's business policy and an important factor of its business strategy. Therefore, this area is regulated by a separate document called the Credit Risk Management Procedures that applies to all phases of the credit process (from the development of new banking products, to loan applications, client monitoring and final loan repayments). The Credit Risk Management Procedures represent a comprehensive document comprised of separate methodologies aiming to evaluate various client target groups.

In order to mitigate credit risk and reduce operating costs, the Bank, in accordance with the HBOR Act, on-lends part of its placements via commercial banks that assume the risk of collecting repayments from final borrowers. For the purpose of facilitating access to HBOR's funds, the Bank on-lends part of its placements through risk sharing models. Generally, all direct placements and placements through the risk sharing models are secured by mortgages on immovable property, and, if possible, the Bank requires guarantees issued by HAMAG BICRO and also other types of guarantees and warranties. The Bank has determined the required ratio between placement value and collateral value according to the type of collateral, the loan programme, the general terms and conditions of security and the decision of the body in charge.

The Bank's development loan programmes cover the entire territory of the Republic of Croatia with a focus on the areas of special state concern. Credit risk is diversified by geographical regions, activities, sectors and loan programmes. The Bank aims to prevent the excessive concentration of credit risk and, by providing more favourable terms and conditions and creating new loan programmes (products), to promote the development of less developed regions of the Republic of Croatia in accordance with the state development strategy for individual activities.

Liquidity risk, currency risk and interest rate risk in the banking book

The Bank ensures quality management of liquidity, currency and interest rate risks in the banking book through the Asset and Liability Management Committee. The management of these risks implies a reduction of interest rate risk, currency risk and liquidity risk to the lowest possible level. The majority of the Bank's organisational units are included, directly and indirectly, in the operations of the Asset and Liability Management Committee in order to ensure a high-quality, integrated and comprehensive system for the management of these risks.

Liquidity risk

The basic concepts and principles for managing HBOR's liquidity risk are defined in internal documents as well as in the decisions and conclusions made by the Supervisory Board, the Management Board and the Asset and Liability Management Committee.

For the purposes of managing liquidity risk, the Bank has established a system of limits. The Bank monitors and verifies that the limits are obeyed. It maintains the necessary level of liquidity reserves, continuously monitors current and planned liquidity and provides sufficient kuna and foreign currency funds necessary for the timely settlement of obligations and disbursements under committed loans and planned commitments. The Bank monitors and strives to achieve compatibility of the existing and planned placements and sources in terms of maturity. The Bank does not take deposits from citizens and is therefore not exposed to wide daily fluctuations in liquidity. The Bank monitors liquidity risk also through scenario analyses and sensitivity analyses both under regular business conditions and under stress. Early warning signals and procedures for liquidity crisis indication or occurrence are determined in the Liquidity Risk Management Ordinance.

Interest rate risk in the banking book

The basic concepts and principles for managing the Bank's interest rate risk are defined in separate internal documents and in the decisions and conclusions made by the Management Board and the Asset and Liability Management Committee. For the purpose of measuring and monitoring interest rate risk, the Bank analyses the interest rate gap. The interest rate gap is analysed with respect to specific periods in terms of possible changes in interest rates and it illustrates the sensitivity of the Bank to such changes in interest rates. Interest rates are elaborated in detail per currency, type and level of interest rates, and projections of developments in average weighted interest rates on the Bank's sources and placements are prepared. In addition to adjustment of interest rates applied on sources and placements, current market conditions and development projections for basic market indicators are also monitored.

Currency risk

The basic concepts and principles for HBOR's currency risk management are defined in internal documents as well as in the decisions and conclusions made by the Management Board and the Asset and Liability Management Committee. The methods for the measurement/assessment, monitoring and management of currency risk have been established, the limits and procedures in the case of crisis indication or occurrence have been determined, and the reports necessary for overall currency risk containment have been defined.

For the measurement of exposure to currency risk, the Bank monitors the open foreign currency position. In addition to the daily monitoring of the open foreign currency position and the preparing of its development projections, the Bank uses the VAR model as an auxiliary model for the purpose of assessing and measuring currency risk. The Bank regularly reports on the maximum possible losses under major currencies to the bodies in charge. Scenario analyses and sensitivity analyses are conducted both under regular business conditions and under stress.

Operational risk

The basic principles for operational risk management are determined in the umbrella document, the Operational Risk Management Policies. The system structure of management and responsibility has been set up, the approach to the calculation of capital requirements for operational risk has been defined and the reporting system has been established.

HBOR's Information System Management Committee has been formed with the task of monitoring and supervising IT system performance. Its purpose is to manage the IT resources and to set up the appropriate level of efficiency and security of IT in order to provide, among other things, appropriate management of risks arising from IT technology utilisation. The supervision of the IT system security is covered by the IT system security control function. Within this function, a system for the management of business continuity has been set up.

Outsourcing risk

The Bank manages the outsourcing risk on the basis of internal documents that are in compliance with the regulations prescribed by the Croatian National Bank applicable to the Bank as a special financial institution. The internal documents that determine the management of this risk determine also the procedures for the outsourcing of activities, the rules for the management of relations with the service providers and the obligation to reduce the risk to the lowest level possible.

The Central records of outsourced activities have been established. Reports on materially significant outsourced activities are submitted to the Management Board and the Supervisory Board of the Bank on an annual basis.

Assets Quality Review of HBOR

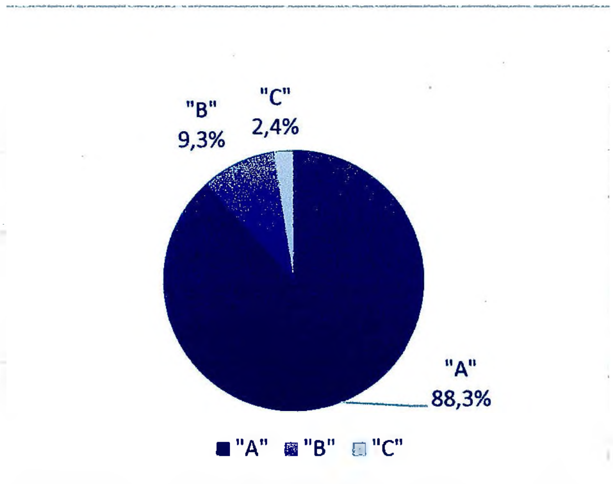
In the National Reform Programme 2016, the Republic of Croatia committed to the implementation of the Asset Quality Review (AQR) of HBOR. For the need of implementation of asset quality review in HBOR, the Croatian National Bank adjusted the methodology of the European Central Bank and prepared the Asset Quality Review Manual. The review will, among others, include the overview of processes, policies, accounting, lending documentation on the selected sample of debtors, evaluation of collateral and real estate value. It will be implemented by the Croatian National Bank in the period from April to August 2017.

At the end of 2016, in co-operation with a consulting company, the preparation process for the mentioned review started for the purpose of its efficient implementation in the planned period.

As at 31 December 2016, HBOR's total portfolio amounted to approximately HRK 36,481.7 million, and HBOR maintained the balanced quality of portfolio in the reporting years.
Of the total portfolio, 88.3 percent was classified into the risk category "A", 9.3 percent was classified into the risk category "B" and 2.4 percent was classified into the risk category "C". Approximately 11.7 percent of the total portfolio was classified into the risk categories "B" and "C" (the so-called "bad" portfolio), a decrease of 1.7 percentage points compared to 2015.

Total portfolio by risk categories

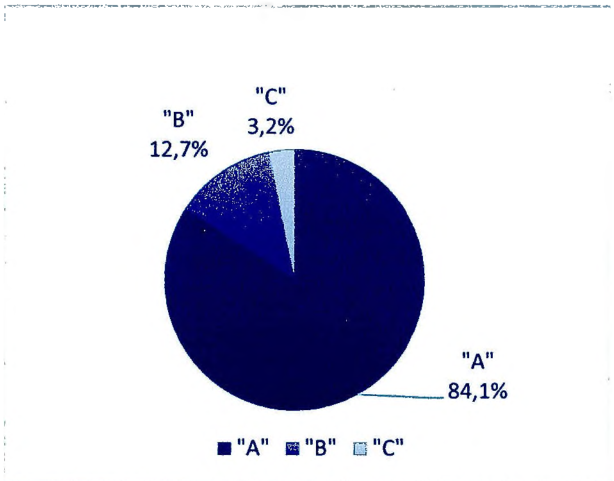
As at 31 December 2016



Having in mind the fact that the loans comprised 72 percent of the total portfolio, there was no significant difference in the quality of total portfolio and total loans. The loans classified into the risk categories "B" and "C" (the so-called bad or non-performing loans) represent 15.9 percent of total loans (a decrease of 1.6 percentage points compared to 2015).

Total gross loans by risk categories

As at 31 December 2016



CONTROL AND AUDIT

The Control and Audit unit is part of HBOR's supervision system. It is in charge of monitoring the overall operations on the basis of the principles of legality and HBOR's internal regulations by applying the internal audit standards. The organisational unit of Control and Audit carries out its tasks independently and determines the manner of operating and reporting as well as preparing its findings, opinions and recommendations on its own. It is administratively responsible to the Management Board and functionally to the Audit Committee and the Supervisory Board of HBOR, to which reports are submitted quarterly/semi-annually. Based on the audit report and according to the recommendations of the Control and Audit unit, the Management Board makes the necessary decisions to take corrective measures and activities.

COMPLIANCE MONITORING FUNCTION

The function of monitoring compliance has been established as an independent and permanent function. Compliance monitoring activities include the identification and assessment of compliance risks to which HBOR is or might be exposed as well as the provision of advice to the Management Board and other responsible persons on the manner of applying relevant legislation, standards and rules, including the information on the latest news regarding these issues.

The compliance monitoring function evaluates the impacts that the amendments to the relevant regulations will have on the operations of HBOR, it assesses the compliance of new products or new procedures with the relevant laws and regulations and with the amendments to the regulations, provides advice during the preparation of compliance-related training programmes and participates in the management of procedures pertaining to complaints and reported irregularities. The compliance monitoring function submits periodical reports to the Management Board, the Audit Committee and the Supervisory Board of HBOR.

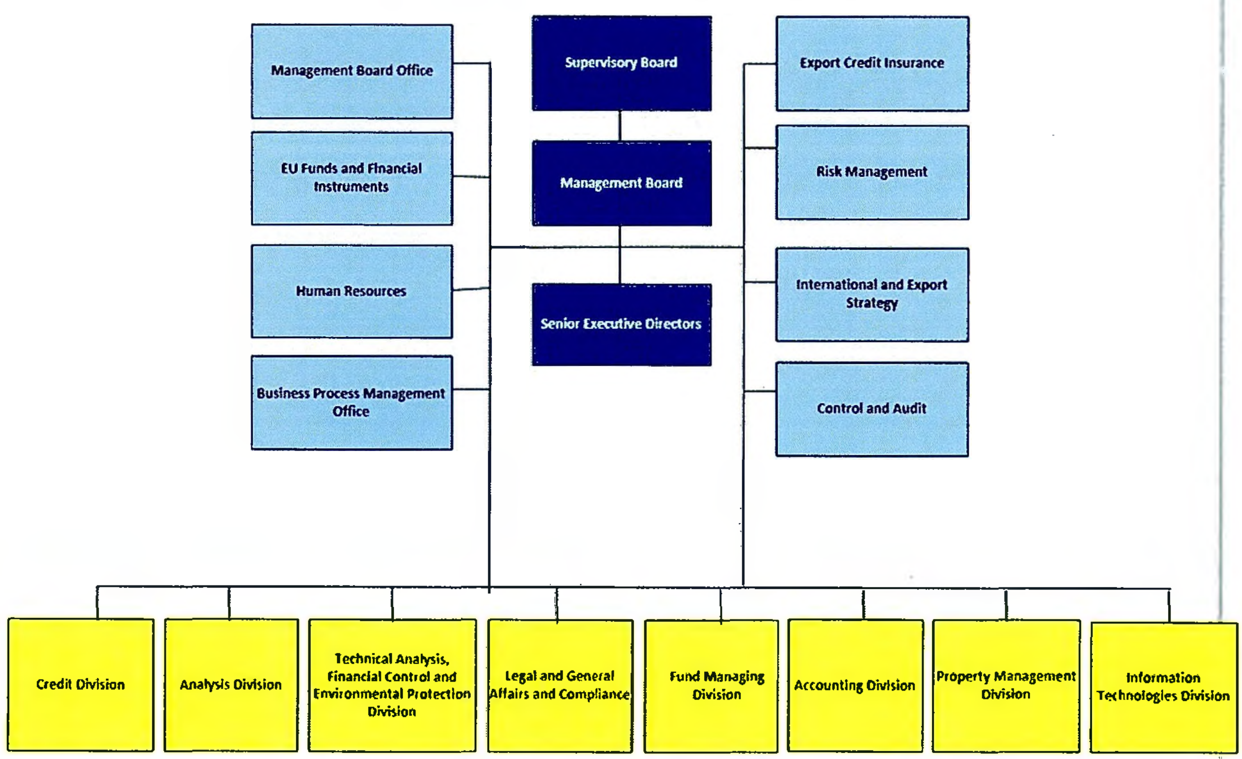
HUMAN RESOURCES

In 2016, HBOR renewed the Employer Partner Certificate that is awarded by Selectio d.o.o. for excellence in human resource management. Continuous certification during eleven years shows that HBOR is on the right path to achieve its goals and that business processes have been created and are being implemented whilst maintaining the highest standards of the profession. Results of 2015/2016 recertification demonstrate a better overall score compared with the previous year: 86 percent against 81 percent scored in the previous year.

The goal of the human resource management process is to select quality employees and ensure permanent development of their potential and continuous upgrading of their competences as the only way to achieve excellence in work. Regular processes and activities related to the management of human resources cover the entire career of an employee in the organisation and provide support to the management in key issues associated with human resources: selection and employment of candidates, management of employees' goals and competences, remuneration as well as development of employees' skills. After employment, that is carried out on the basis of clear selection criteria, new employees are introduced to business through in-house training programmes. Success at work of all employees is monitored and documented on a quarterly basis, whereas individual interviews take place on an annual basis. Training and development of competences considered crucial in the activities that are performed by employees are organised through in-house workshops and through participation in individual programmes and trainings organised outside of the Bank.

As at 31 December 2016, there were altogether 349 employees, of which 306, i.e. 88 percent, holding a university degree. The average age of employees was 41. The share of women in the total number of employees was 67 percent and the share of men 33 percent.

Organisational structure of HBOR



OTHER ACTIVITIES

In 2016, HBOR launched the public invitation called "NOVI POGLEDI" seeking applications for the award of grants for innovation and excellence in education, culture and arts. The grants were awarded to 17 projects totalling almost HRK 600 thousand. Names of all grant recipients were published on HBOR's websites.

In June 2016, HBOR published its Social Responsibility Report for 2015, i.e. its seventh report on the manner of and progress in the implementation of the UN Global Compact principles in the areas of human rights, labour standards, environment and anti-corruption.

International co-operation

HBOR pays special attention to the establishment and maintenance of successful relations with international financial institutions, development banks, export-credit agencies, associations and clubs such as the European Association of Public Banks (EAPB), the Network of European Financial Institutions for SMEs (NEFI), the Banking Association for Central and Eastern Europe (BACEE), the Berne Union, the United Nations Environment Programme Finance Initiative (UNEP FI), the UN Global Compact, the International Development Finance Club (IDFC), numerous bilateral chambers of commerce and, as an establishing member, the European Long Term Investors association (ELTI). Memberships of the above associations are a means for developing business and upgrading knowledge as well as for effectively exchanging best practices and specific expertise among members on various business issues.

In September, HBOR hosted the gathering of the Network of European Financial Institutions for SMEs (NEFI) where the participants discussed the implementation of financial instruments and other EU initiatives for the development of small and medium-sized entrepreneurship.

In November, HBOR's 15th International Conference on Export Promotion took place under the auspices of the Government of the Republic of Croatia. The Conference gathered 350 representatives of Croatian exporters, domestic and foreign institutions and banks. At the Conference, three workshops were held to discuss the possibilities for providing security against non-payment in the domestic and foreign markets, to highlight the advantages of HBOR's insurance policy when applying for loans and guarantees, and to introduce the European Investment Advisory Hub and the experiences of entrepreneurs with regard to the utilisation of EU funds.

REGIONAL OFFICES

During 2016, numerous activities aimed primarily at small enterprises and start-up enterprises were performed through HBOR's regional offices.

In 2016, the regional offices were contacted by almost three thousand entrepreneurs or potential entrepreneurs seeking information on lending possibilities. More than one third (39 percent) of individual loan approvals were to entrepreneurs who used the services of HBOR's regional offices.

In the reporting year, the regional offices organised more than 150 workshops and education events, among which numerous workshops called "In 7 Steps to a Loan" intended to strengthen the financial literacy of potential entrepreneurs. This form of training is particularly focused on young entrepreneurs and start-up entrepreneurs interested in special programmes intended for these target groups of borrowers.

A significant focus of the regional offices' activities is on individual advisory services provided to clients interested to cooperate with HBOR, i.e. on the preparation of visits to and on the visiting of clients in the phase of their loan application processing. HBOR's Info Days, which are organised in co-operation with partner institutions, offer individual advice to entrepreneurs on the possibilities for utilising HBOR's funds as a source of funding. In 2016, almost one thousand entrepreneurs participated in the Info Days.

Public disclosure of activities

HBOR considers public disclosure of activities to be an important precondition for the credibility of its operations. Special focus is put on providing complete and understandable information to the public about its goals and about the measures for their attainment as well as about the results of its activities by simultaneously following the principle of bank secrecy. Therefore, through various forms of providing information, HBOR regularly informed the public about all its important activities in 2016. In the reporting period, HBOR published 21 press releases informing the public about the operations, attained results, new loan programmes and amendments to the existing ones. All business information can be accessed on HBOR's websites, except for the information subject to the bank secrecy provisions of the Credit Institutions Act.

During the reporting year, 29 public procurement procedures were published in the Electronic Public Procurement Classifieds, whereas, since August 2010, all bidding announcements have been published on HBOR's websites.

In 2016, five requests for access to information pursuant to the Act on the Right of Access to Information were received.

HRVATSKO KREDITNO OSIGURANJE GROUP

HRVATSKO KREDITNO OSIGURANJE D.D. and POSLOVNI INFO SERVIS D.O.O.

Hrvatsko kreditno osiguranje d.d. (hereinafter: HKO or the Company) is a joint-stock insurance company specialised in the insurance of short-term receivables (payment terms of up to 2 years) arisen from the sale of goods or services among business entities. The insurance covers political and commercial risks.

In 2016, HKO offered the following insurance products: insurance of export receivables, insurance of domestic receivables and insurance of export and domestic factoring.

On 26 October 2010, HKO established Poslovni info servis d.o.o. By establishing this company, HKO started to operate as the Hrvatsko kreditno osiguranje Group (hereinafter: the HKO Group) and to prepare its consolidated financials. Within the Group, Poslovni info servis d.o.o. (hereinafter: PIS) is in charge of analysing and assessing credit risks relating to the insurance transactions.

As at 31 December 2016, there were 15 employees in the HKO Group, of which Hrvatsko kreditno osiguranje d.d. employed 13 and PIS 2. Fourteen employees of the HKO Group have a university degree and one employee has secondary school education.

Ownership structure

HKO is 100% owned by the Croatian Bank for Reconstruction and Development.

Management

Legal status, organisation and management of the Company, all other issues important for the operations of the Company as well as all harmonisation issues provided for in the Companies Act and the Insurance Act are determined by the Statutes of the Company.

Company management bodies:

Management Board

Supervisory Board

Shareholders' Meeting

People authorised to represent

Management Board

Edvard Ribarić, Chairman of the Management Board until 31 March 2016

Marija Jerkić, Deputy Member of the Management Board in accordance with the decision made by the Supervisory Board on 1 April 2016, whereas her term of office as the Member of the Supervisory Board is suspended

Ksenija Sanjković, Member of the Management Board

Authorised Representative

Ružica Adamović

Supervisory Board of HKO

Until 18 October 2016, the membership of the Supervisory Board of HKO was as follows:

Marko Topić, Chairman of the Supervisory Board

Ante Artuković, Deputy Chairman of the Supervisory Board

Marija Jerkić, Member of the Supervisory Board; Deputy Member of the Management Board in accordance with the decision made by the Supervisory Board on 1 April 2016, whereas her term of office as the Member of the Supervisory Board is suspended

Andreja Mergeduš, Member of the Supervisory Board

From 18 October 2016, the membership of the Supervisory Board of HKO was as follows:

Goran Filipić, Chairman of the Supervisory Board

Marko Topić, Deputy Chairman of the Supervisory Board

Ante Artuković, Member of the Supervisory Board

Marija Jerkić, Member of the Supervisory Board; Deputy Member of the Management Board in accordance with the decision made by the Supervisory Board on 1 April 2016, whereas her term of office as the Member of the Supervisory Board is suspended

Poslovni info servis d.o.o.

In 2016, Ružica Adamović performed the function of the Manager of PIS, and Ivana Paić was the authorised representative.

HKO Audit Committee

Until 18 October 2016, the membership of the Audit Committee of HKO was as follows:

Marija Jerkić, Chairman

Andreja Sekušak, Deputy Chairman

Ante Artuković, Member

From 18 October 2016, the membership of the Audit Committee of HKO was as follows:

Ante Artuković, Chairman

Goran Filipić, Deputy Chairman

Andreja Sekušak, Member

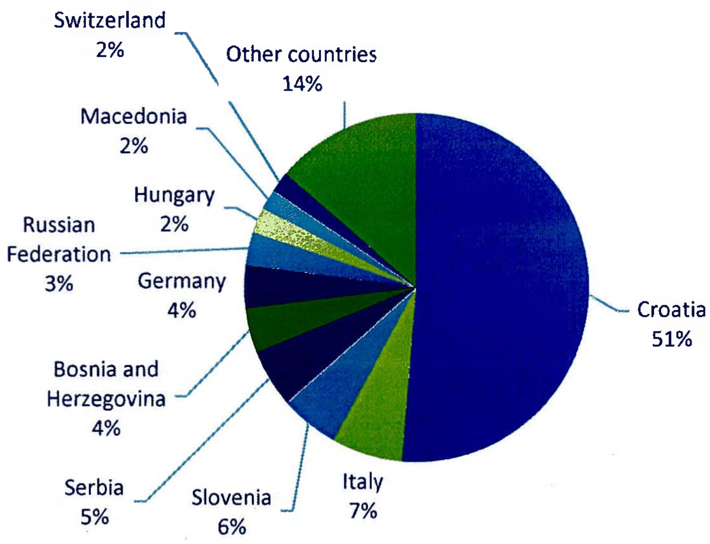
Reporting to the supervisory bodies

In 2016, the Company provided regular reports to the supervisory bodies on all relevant facts and changes in the Company pursuant to the Insurance Act, the ordinances of the Croatian Financial Services Supervisory Agency and other regulations in force. The Company regularly met all requirements of the supervisory bodies in terms of control of operations and submission of the Company's data.

OPERATIONS IN 2016

In 2016, Hrvatsko kreditno osiguranje d.d. concluded 106 insurance contracts, of which 17 were related to the insurance of both domestic and export receivables. A total of 3,026 credit limits were covered by the insurance, i.e. an increase of 24.62 percent on the previous year. Within the total structure of limits, 1,868 credit limits were related to domestic receivables, and 1,158 credit limits were related to export receivables towards 59 countries of the world.

EXPOSURE BY COUNTRIES (ACCORDING TO LIMIT AMOUNTS) as at 31 December 2016



The total volume of insured transactions in 2016 amounted to HRK 3.80 billion, whereas it amounted to HRK 3.68 billion, an increase of 3.10 percent.

In 2016, the total charged premium amounted to HRK 11.81 million, a decrease of 2.9 percent on 2015 when it stood at HRK 12.17 million.

In the reporting period, the Company paid 5 indemnities. In 2016, the total amount of paid indemnities amounted to HRK 1.72 million, whereas the amount of paid indemnities in the previous year equalled HRK 2.21 million. The paid indemnities were related to buyers in Montenegro, Kosovo, Italy, Germany and Croatia.

INSURANCE BUSINESS INDICATORS

	2014	2015	2016
Volume of insured receivables (in HRK thousands)	3,129,107.94	3,684,431.54	3,798,540.23
Exposure as at 31 December (in HRK thousands)	1,260,637.41	1,579,198.16	1,709,409.46
Gross premium charged (in HRK thousands)	10,835.71	12,167.19	11,814.18
Amount of paid indemnities (in HRK thousands)	2,505.01	2,207.67	1,717.33
Number of active limits as at 31 December	2,156	2,428	3,026

Acquisition costs, marketing costs, administration costs and other operating expenses of the HKO Group in 2016 amounted to HRK 6.05 million, whereas, at the Company level, they amounted to HRK 5.27 million.

The business year 2016 is the sixth full year of operations. Prior to consolidation with the parent's financial statements, the HKO Group recorded profit before taxes for the year in the amount of HRK 1.12 million, whereas 2015 ended with a profit of HRK 0.74 million.

As at 31 December 2016, the total assets of the HKO Group amounted to HRK 57.97 million, an increase of 3.41 percent on the previous year. As at 31 December 2016, the total capital amounted to HRK 39.06 million and technical reserves to HRK 9.60 million net.

PRINCIPLES OF FINANCIAL REPORTING

The HBOR Group prepares:

1. Separate financial statements of the parent company – Croatian Bank for Reconstruction and Development (HBOR), and
2. Consolidated financial statements that include HBOR and the companies under its control – subsidiary companies.

When preparing and presenting its annual financial statements, the HBOR Group applies the International Financial Reporting Standards (IFRS). Consequently, all data and financial statements for consolidation are prepared by the members of the Group in accordance with the IFRSs.

Financial statements are prepared and presented in order to provide information on the financial position, success in operations and changes in the financial position of HBOR and the HBOR Group in order to enable their users to make appropriate economic decisions.

Financial statements are prepared and presented for the purpose of making information available to their users on a regular basis regarding the financial position, success in operations and changes in the financial position of HBOR and the HBOR Group as well as for giving financial information about how the strategy of HBOR's Group is carried out.

For the purpose of financial reporting and disclosures, the HBOR Group applies the following principles:

- **Transparency in disclosure** in order to enhance its users' understanding of the presented information,
- **Consistency in presentation** within each reporting period and between reporting periods,
- **Simplicity in disclosure** in order to allow the users to gain an easier understanding of the financial position, business performance and changes in financial position, as well as to ease decision-making,
- **Focusing on legal requirements** in order to ensure compliance,
- **Application of the best presentation practices** appropriate to the Group's activities with respect to up-to-date international trends in financial reporting as well as market requirements.

OVERVIEW OF FINANCIAL PERFORMANCE IN 2016

The HBOR Group was formed in 2010. It consists of the Croatian Bank for Reconstruction and Development, as the parent company, and the subsidiary companies: Hrvatsko kreditno osiguranje d.d. and Poslovni info servis d.o.o., which constitute the Hrvatsko kreditno osiguranje Group.

The first consolidated financial statements prepared and presented by HBOR were those prepared for the year 2010.

The financial statements include both HBOR and the Group. The financial statements of the Group consist of the consolidated financial statements of HBOR and its subsidiaries. However, the separate, non-consolidated, financial statements of the parent company are also presented.

The separate and consolidated Annual Financial Statements of HBOR for 2016, which can be found enclosed, have been audited by the audit company Ernst & Young d.o.o. that expressed an unqualified opinion in the Independent Auditor's Report.

In the text to follow, an overview of the financial performance and operations is given separately for the Group and for HBOR as the parent company and the entity subject to this report.

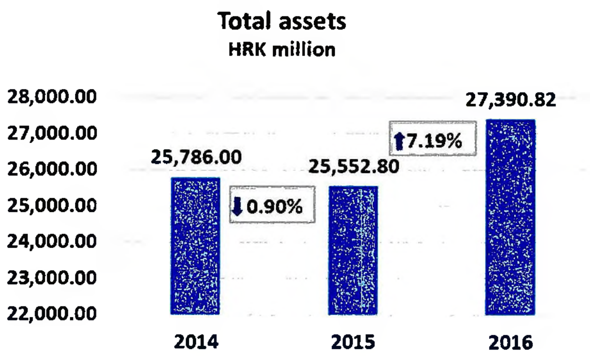
OVERVIEW OF FINANCIAL OPERATIONS OF THE GROUP

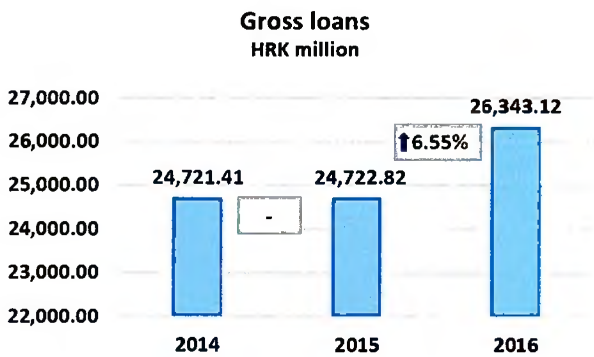
Having in mind the size of the subsidiary companies and the volume of their operations compared with the operations of the parent company, their financial data in the first years of the Group are not significant so as to be particularly highlighted within the framework of the consolidated financial statements. Consequently, they do not have a material effect on the consolidated financial statements in comparison with the separate statements of HBOR as the parent company. The Hrvatsko kreditno osiguranje Group represents 0.20 percent of the parent company's assets.

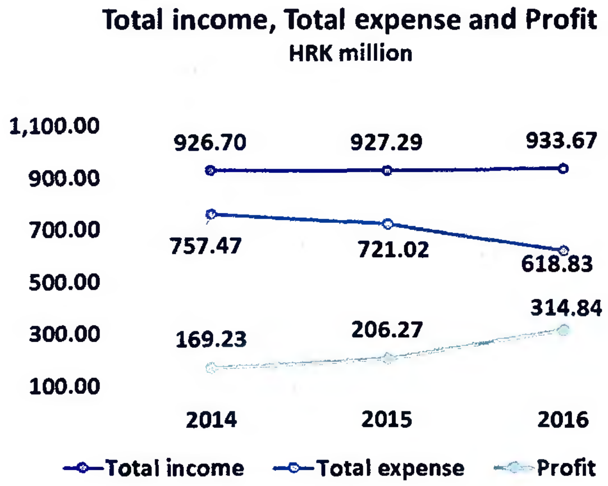
BREAKDOWN OF THE MOST SIGNIFICANT FINANCIAL INFORMATION OF THE GROUP:

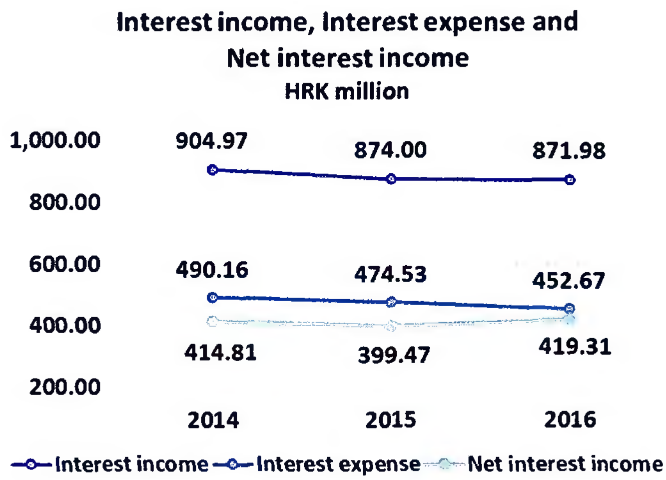
HRK million

	2014	2015	2016
Total assets	25,786.00	25,552.80	27,390.82
Gross loans	24,721.41	24,722.82	26,343.12
Total equity	9,431.02	9,664.54	10,042.70
Total income	926.70	927.29	933.67
Total expense	(757.47)	(721.02)	(618.83)
Profit	169.23	206.27	314.84
Interest income	904.97	874.00	871.98
Interest expense	(490.16)	(474.53)	(452.67)
Net interest income	414.81	399.47	419.31









Results of the Group

In 2016, the HBOR Group generated profit after tax in the amount of HRK 314.84 million. The recorded profit is by 52.63 percent higher as compared to the previous year, and the reasons are stated in the description of HBOR's financial performance.

Pursuant to the provisions of the Act on HBOR, the parent company is exempt from income tax and income tax liabilities arise exclusively from the activities of the other members of the Group.

In 2016, total income on consolidated basis amounted to HRK 933.67 million, whereas total expenses amounted to HRK 618.83 million.

In the structure of income of the Group, the largest portion, i.e. 93.39 percent, relates to interest income as a result of operation of the parent company.

The major part of total expenses, i.e. 73.15 percent, relates to interest expenses arising from the operations of the parent company.

The consolidated operating expenses in 2016 amounted to HRK 160.30 million and consisted of general and administrative expenses and other operating expenses.

There were 364 employees in the Group on 31 December 2016, whereas there had been 357 employees at the end of 2015.

Assets and liabilities of the Group

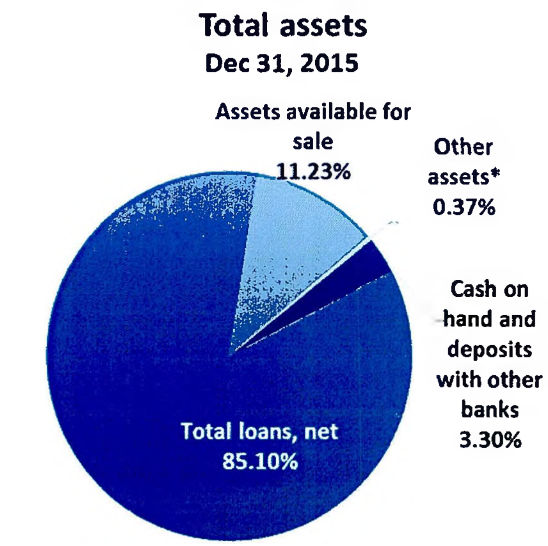
Total assets of the Group on consolidated basis amount to HRK 27,390.8 million, an increase of 7.19 percent compared with the beginning of the year. The reasons for such tendency are stated in the description of HBOR's financial performance.

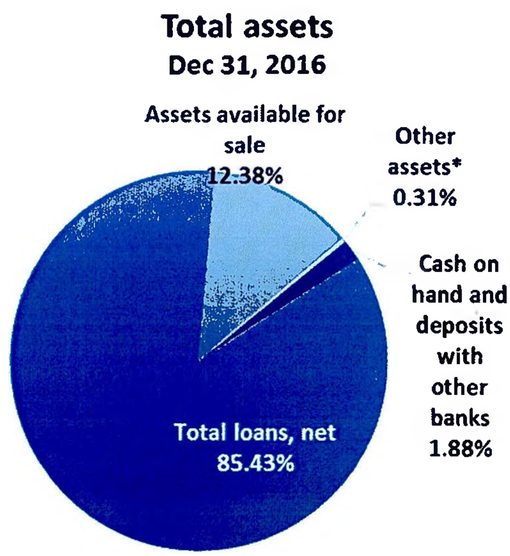
In the structure of assets, the major portion relates to the lending activities of the parent company, i.e. net loans account for 85.43 percent of total assets.

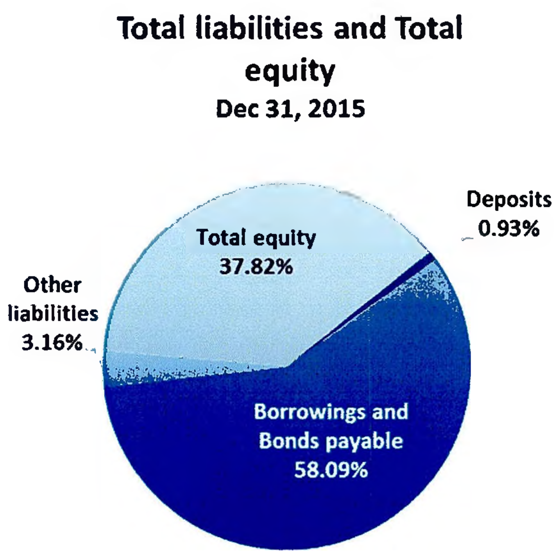
Total liabilities and total equity as of 31 December 2016 amount to HRK 27,390.82 million and, out of this amount, total liabilities amount to HRK 17,348.12 million, i.e. 63.34 percent.

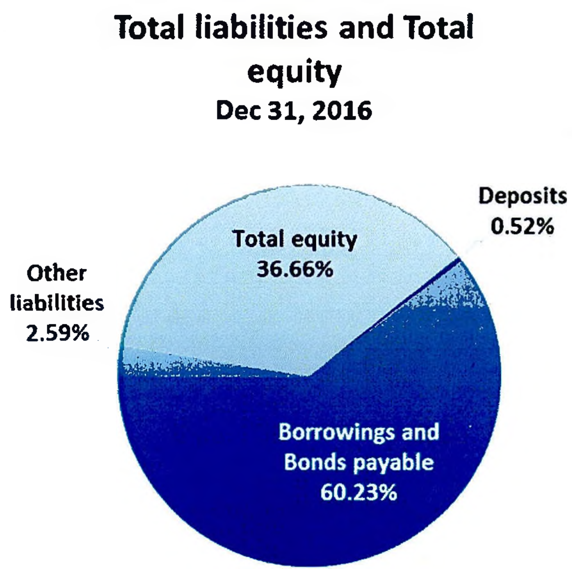
In total liabilities and total equity of the Group, the major portion, i.e. 60.23 percent, consists of borrowings and bonds payable of the parent company.

At the end of the reporting period, total equity on consolidated basis amounted to HRK 10,042.70 million and accounted for 36.66 percent of total liabilities and total equity of the Group.









*Financial assets at fair value through profit or loss, Assets held to maturity, Property, plant and equipment and intangible assets, Non-current assets held for sale and Other assets

OVERVIEW OF FINANCIAL OPERATIONS OF HBOR

The following text gives an overview and explanation of the significant changes in financial position and operating performance in the reporting year.

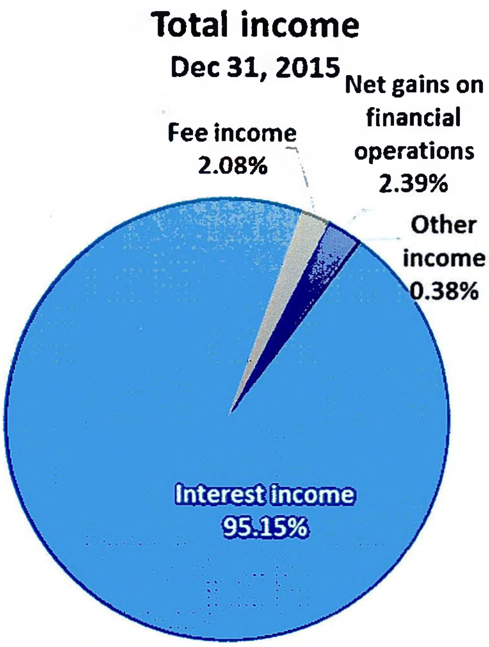
Financial performance

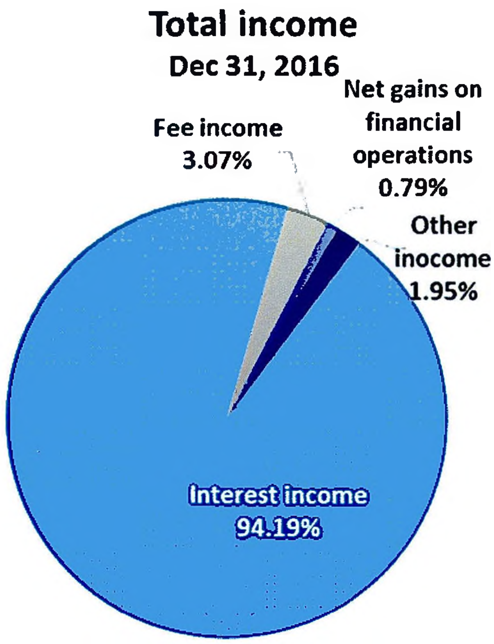
In 2016, HBOR generated total income of HRK 924.0 million, expenses of HRK 610.47 million and profit in the amount of HRK 313.53 million. HBOR's profit generated in 2016 rose by HRK 108.30 million compared with the profit generated in 2015, i.e. 52.77 percent.

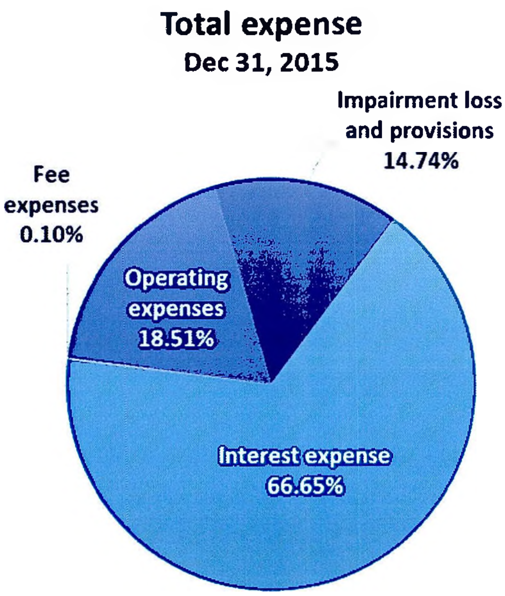
Higher profit in 2016 was mostly a result of a decrease in expenses of HRK 101.41 million. The circumstances that affected the financial result achieved in 2016 compared to the results generated in 2015 are:

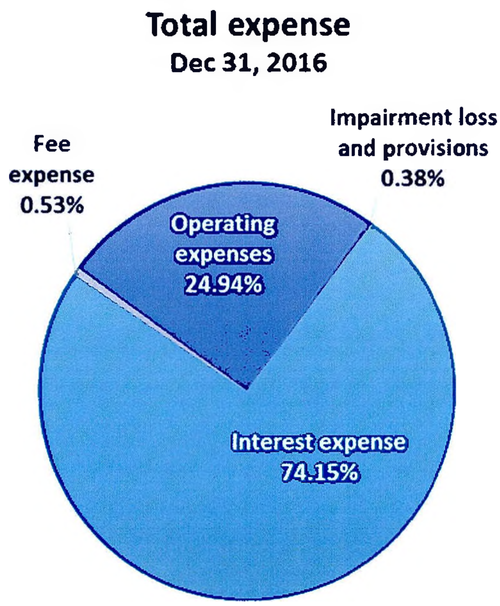
- decrease in interest expenses of HRK 21.86 million compared to 2015,
- decrease in impairment loss and provisions of HRK 102.54 million compared to 2015,
- increase in operating expenses of HRK 20.39 million compared to 2015.

A detailed description of trends is given for each category separately in the following text.









Net interest income

Net interest income amounted to HRK 417.67 million, an increase of 4.92 percent on the previous reporting year.

Interest income amounted to HRK 870.34 million and remained at the level of interest income generated in 2015. This trend is in line with the projections and is mostly a result of the following circumstances:

- interest rate reduction measure implemented by HBOR since the beginning of 2012,
- extended loan repayment periods,
- recalculation of interest due to the restructuring of loans and pre-bankruptcy settlements,
- early repayments of loans in 2015 and during the reporting 2016,
- low interest rates on liquidity reserve funds.

Particular attention should be drawn to the fact that HBOR, through the measure of reducing interest rates for certain categories of final borrowers and investments in the last five business years, gave up a portion of its profits in order to provide support to Croatian business entities in crisis conditions.

Interest expenses amounted to HRK 452.67 million, a decrease of 4.61 percent compared with the previous reporting year mostly as a result of:

- stronger early repayments of individual borrowings in 2013, 2014 and 2015 totalling HRK 5,326.39 million, and
- utilisation of credit lines from special financial institutions at more favourable interest rates.

Having in mind the described trends in interest income and interest expenses, net interest margin remained unchanged compared to the previous year and stood at 1.58 percent.

Net fee income

Net fee income amounted to HRK 25.07 million, an increase of 35.88 percent compared to the previous year as a result of increased fee income from guarantee activities caused by a higher volume of guarantees issued.

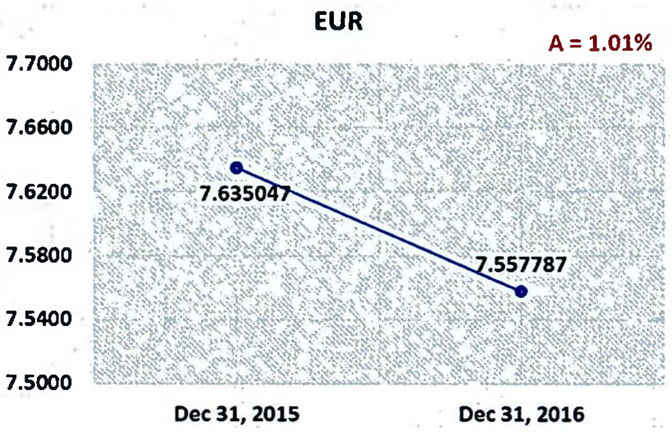
In 2016, HBOR approved the volume of HRK 1,286.60 million in guarantees, whereas the volume of guarantees approved in 2015 stood at HRK 2,926.95 million.

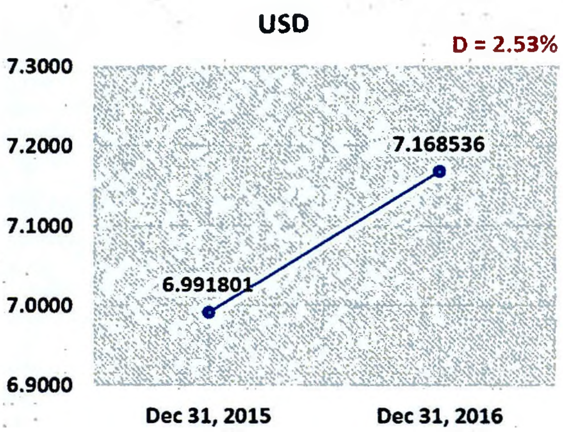
Net gains/(losses) from financial activities

Net gains/(losses) from financial activities are comprised of net foreign exchange gains/(losses) on the principal amount of receivables and liabilities, net revenues or expenditures arising out of the loan contracts with embedded „call option", gains/(losses) arising out of value adjustment of assets stated at fair value through profit or loss and realised gains/(losses) arising out of assets available for sale.

In the reporting period, net gains from financial activities amounted to HRK 7.31 million, whereas, in the previous year, net gains amounted to HRK 21.87 million.

A breakdown of changes in the exchange rate of HRK against the EUR and the USD:





Note:

A = HRK appreciation 2016/2015

D = HRK depreciation 2016/2015

Foreign currency and foreign currency indexed assets and sources of funds are converted by HBOR into HRK equivalent value by applying the exchange rate of the Croatian National Bank valid at the reporting date.

Foreign currency revenues and expenditures are converted in accordance with the exchange rate at the transaction date. The resulting foreign exchange gains or losses are recorded in the Statement of Profit or Loss and Other Comprehensive Income in net figures.

Other income

Other income amounted to HRK 18.02 million, a considerable increase compared to the previous year. This trend is a result of a one-off effect of income recorded as a consequence of the taking of a loan in the amount of HRK 10.35 million into direct relationship from Jadranska banka d.d., Šibenik that is undergoing the process of rehabilitation.

Operating expenses

Operating expenses that include general and administrative expenses and other operating expenses stood at HRK 152.23 million, an increase of 15.47 percent compared with the previous year.

This development is mostly affected by other expenses increasing by HRK 12.67 million compared with the previous year. This increase is a result of a recalculation arising from partial assumption of the placement by another debtor resulting in the expense in the amount of HRK 5.88 million as well as of the recalculation upon restructured loans and pre-bankruptcy settlements. Excluding the above mentioned one-off expenses, the operating expenses would increase by 5.53 percent compared with the same reporting period previous year.

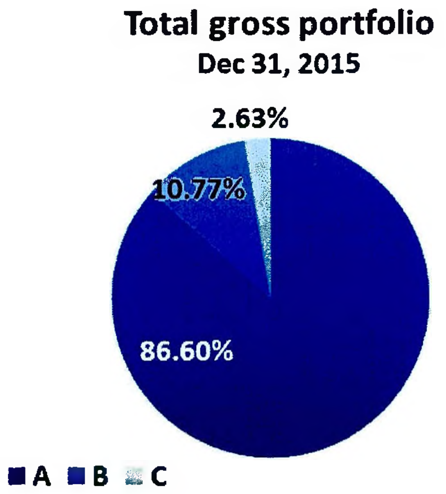
There were 349 employees at the end of 2016, whereas there were 342 employees at the end of 2015.

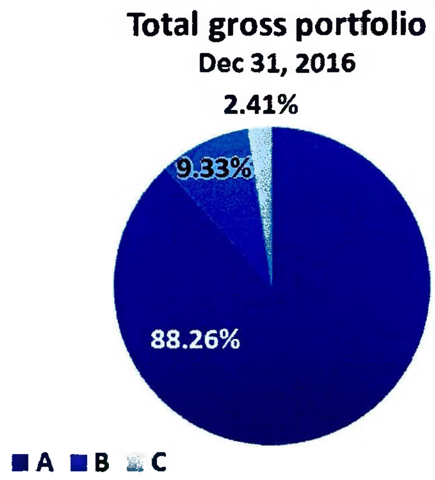
Impairment loss and provisions

In accordance with the regulations and internal acts, HBOR determines the amount of impairment loss and provisions and maintains it at the level it considers adequate for the coverage of possible future risks.

In the reporting period, net impairment loss stood at HRK 2.31 million and is considerably lower compared with the previous year due to a higher number of debtors undergoing bankruptcy proceedings in 2015, which lead to higher provisions, as well as due to a higher number of pre-bankruptcy settlement proceedings. In addition, provisioning for court proceedings in the amount of HRK 23.45 million was cancelled in 2016 as a result of a court settlement. The impairment losses resulted from the assessment of risk inherent to the placements, mostly the placements to clients undergoing bankruptcy or pre-bankruptcy settlement proceedings, the placements with recorded delays in the settlement of obligations and the restructured placements.

The following text contains a breakdown of the quality of portfolio:





	2015		2016	
	HRK million	Structure (%)	HRK million	Structure (%)
Total gross portfolio	**33,114.18**	**100.00**	**36,481.66**	**100.00**
out of which:				
- financial institutions	16,006.68	48.34	15,888.50	43.55
- direct	17,107.50	51.66	20,593.16	56.45
Total provisions	**3,075.26**	**100.00**	**3,042.51**	**100.00**
out of which:				
- financial institutions	500.09	16.26	395.46	13.00
- direct	2,575.17	83.74	2,647.05	87.00
Provisions/gross portfolio	**9.29 percent**	-	**8.34 percent**	-

Significant changes in the financial position

Total assets of HBOR as of 31 December 2016 amounted to HRK 27,374.92 million, an increase of 7.18 percent compared with the beginning of the year. The increase in assets is mostly due to the increase in lending activities and the net loan balance was 7.61 percent higher compared with the beginning of the year.

Cash on hand and deposits with other banks

As at 31 December 2016, cash on hand and deposits with other banks amounted to HRK 514.57 million representing 1.88 percent of total assets. This item decreased by 38.67 percent compared with the previous year as a result of reallocation of liquidity reserve funds.

Loans to financial institutions and other customers

Total net loans increased by 7.61 percent compared with the previous year and stood at HRK 23,400.30 million at the end of 2016 representing 85.48 percent of total assets.

Total gross loans amounted to HRK 26,343.12 million and increased by 6.55 percent compared with the beginning of the year. Gross loans to other customers increased by 20.14 percent compared with the beginning of the year, which is mostly due to disbursements under the loan programmes for tourism, export finance and infrastructure finance. Gross loans to financial institutions decreased by 5.71 percent compared with the previous year as a result of reallocation of liquid funds into other financial instruments and premature repayment of loans.

At the end of 2016, the ratio between gross loans approved through financial institutions and direct placements was 46.51 percent : 53.49 percent.

Assets available for sale

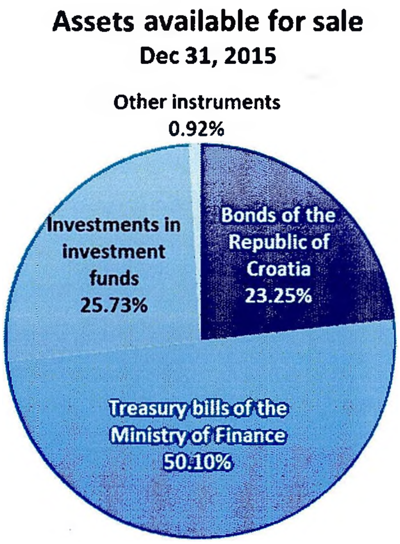
Assets available for sale were comprised primarily of liquidity reserve funds, further to which assets available for sale were comprised primarily of debt instruments and, to a minor extent, of investments into investment funds and equity instruments.

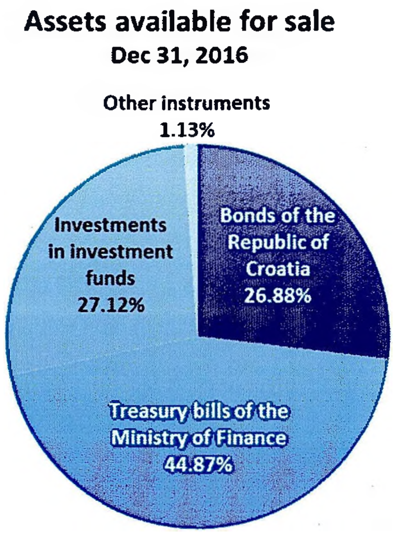
This item amounted to HRK 3,343.58 million, an increase of 18.05 percent compared with the beginning of the year due to the investments of available funds in treasury bills of the Ministry of Finance, investment funds in the Republic of Croatia and bonds of the Republic of Croatia as liquidity reserve instruments.

In 2016, investment in the following instruments of assets available for sale was made:

HRK million

Treasury bills of the Ministry of Finance	1,487.16
Bonds of the Republic of Croatia	382.15
Investment in investment funds in the Republic of Croatia	289.59
Total	**2,158.90**





Total liabilities

At the end of 2016, total liabilities amounted to HRK 17,336.94 million, which represents 63.33 percent of total liabilities and total equity. The major part of total liabilities consists of HBOR borrowings and bonds payable in the total amount of HRK 16,497.32 million.

In 2016, HBOR continued to raise earmarked funds from special financial institutions for the purpose of financing its increased lending activity; thus, the following finance contracts were concluded:

- With the European Investment Bank on 17 February 2016 in the amount of EUR 150 million. Funds are intended for the financing of mid-cap companies in the industry, services, tourism and other sectors, as well as public and private companies investing in knowledge-based, infrastructure and environmental projects.

- With the European Investment Bank on 11 July 2016 in the amount of EUR 250 million to support the projects of local small and medium-sized enterprises (SMEs). The loan will contribute to the implementation of projects in the areas of industry services, tourism and other priority sectors. The loan also provides support to the EIB "Jobs for Youth Initiative", whereby EIB and HBOR additionally support final beneficiaries if they can document that their investment projects financed under the facility also contribute to the creation of youth employment.

Both contracts are a part of the framework in the amount of EUR 800 million for the financing of small and medium-sized enterprises and mid-cap companies signed between HBOR and EIB on 24 March 2014.

Borrowings and bonds payable increased by 11.3 percent compared with the beginning of the year due to the drawdown of borrowed funds.

Total drawdown of borrowed funds in 2016 amounted to HRK 3,730.87 million. The amount of HRK 1,955.34 million relates to loan repayments, of which repayment of borrowed funds in the amount of HRK 1,730.85 million and repayments under securities issued in the amount of HRK 224.49 million.

Of the above mentioned amount, on 11 July 2016, the Bank made the final payment under the long-term bonds issued with amortised repayment in the amount of HRK 224.49 million, together with interest of HRK 10.79 million.

On 11 July 2006, based on the agreement between HBOR and Deutsche Bank AG London (lead manager), HBOR launched a EUR 150 million bond issue maturing in 10 years at fixed interest rate of 4.807 percent and with amortising repayment from 2012 to 2016.

On 30 December 2016, syndicated loan of local banks under the Programme for the Development of the Economy in the amount of HRK 746.97million, together with interest of HRK 10.66 million, was repaid in full.

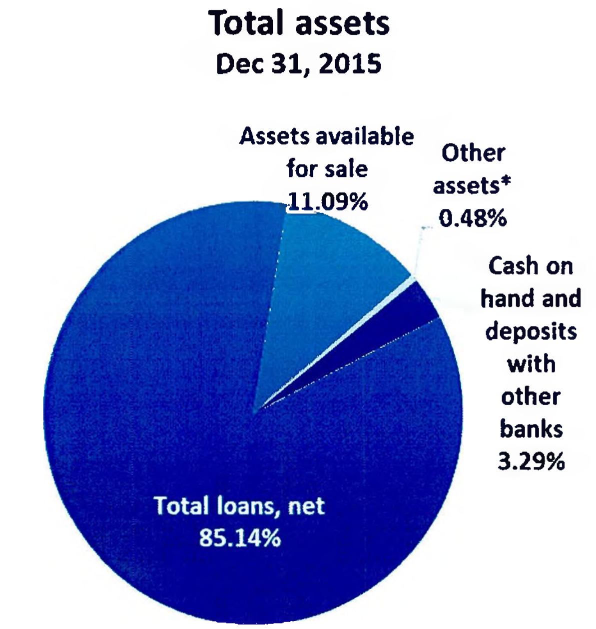
Total equity

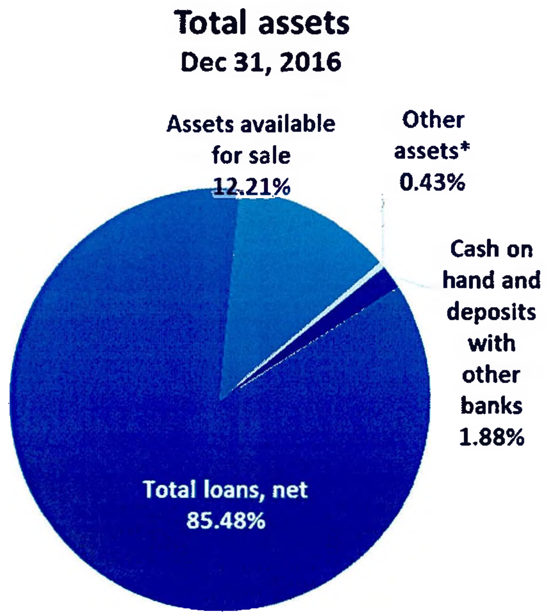
Total equity amounted to HRK 10,037.98 million, representing 36.67 percent of total liabilities and total equity.

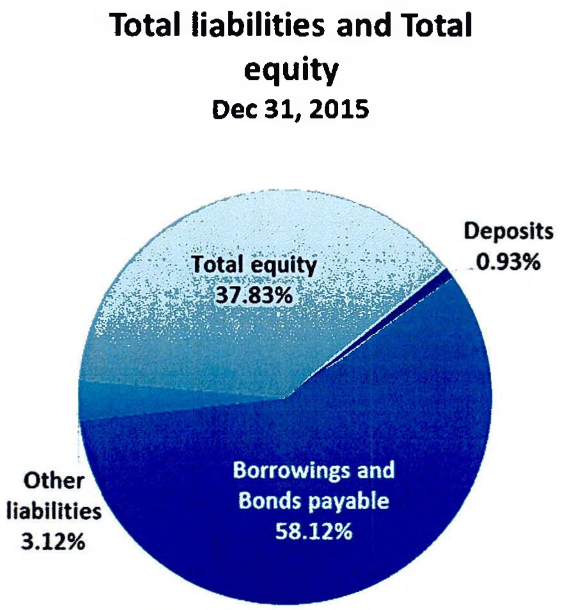
Total equity of HBOR is comprised of the capital and the guarantee fund. HBOR's capital is comprised of founder's capital contributed from the budget of the Republic of Croatia, retained earnings from the profits generated in the previous years, other reserves and profits for the current year.

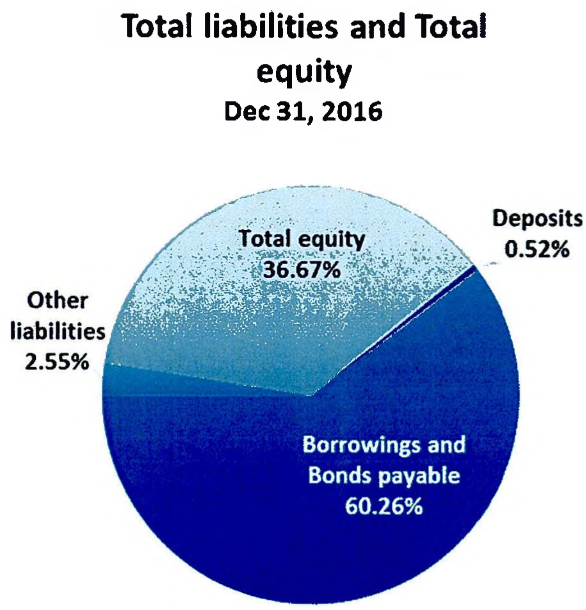
In the reporting period, the amount of HRK 33.00 million was contributed from the budget of the Republic of Croatia into the founder's capital, and the total amount of capital contributed from the budget of the Republic of Croatia amounted to HRK 6,533.00 million at the end of 2016. The remaining amount to be contributed to the founder's capital up to the total amount of HRK 7,000.00 million set by the HBOR Act is HRK 467.00 million.

Pursuant to the provisions of the Act on HBOR, the entire profit of the reporting period of the Bank is allocated to reserves.









*Investments in subsidiaries, Property, plant and equipment and intangible assets, Non-current assets held for sale and Other assets.

Responsibility for the Financial Statements

Pursuant to the Croatian Accounting Law, the Management Board is responsible for ensuring that financial statements are prepared for each financial year in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union, which give a true and fair view of the state of affairs and results of Croatian Bank for Reconstruction and Development, Zagreb ("the Bank") and the Group for that period.

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

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

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

In the financial statements, materially significant items and information are stated. The estimation of materiality is applied to the entire financial statements, including notes.

When making a decision what data will be published in the financial statements and accompanying notes, professional judgements are applied.

Certain stated items can be analysed in more details, but are stated consistently from period to period on an aggregated basis. Notes that include significant accounting policies and other explanations are presented by order of items stated in the Statement of Profit and Loss and the Statement of Financial Position by structure for financial institutions.

The Management Board is responsible for keeping proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Bank and the Group and must also ensure that the financial statements comply with the Croatian Accounting Law. The Management Board is also responsible for safeguarding the assets of the Bank and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Valerija Marić
Assistant Accounting Division Executive Director

M. Sc. Tamara Perko
President of the Management Board

Martina Jus
Member of the Management Board

Zagreb, 17 March 2017

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Independent auditor's report

To the Owner of Hrvatska banka za obnovu i razvitak

Opinion

We have audited the separate and consolidated financial statements of Hrvatska banka za obnovu i razvitak ("the Bank") and its subsidiaries ("the Group"), which comprise the separate and consolidated statement of financial position as at 31 December 2016, separate and consolidated income statement and the separate and consolidated statement of other comprehensive income, separate and consolidated statement of changes in equity and separate and consolidated statement of cash flows for the year then ended, and notes to the separate and consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying separate and consolidated financial statements give a true and fair view of the financial position of the Bank and the Group as at 31 December 2016 and of their financial performance and their cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by EU ("IFRS as adopted by EU").

Basis for opinion

We conducted our audit in accordance with the International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the separate and consolidated financial statements* section of our report. We are independent of the Bank and the Group in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

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

Key audit matters

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

We have fulfilled the responsibilities described in the Auditor's responsibilities for the audit of the separate and consolidated financial statements section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the separate and consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying separate and consolidated financial statements.

Loan Loss Provisions

Credit impairment is a highly subjective area due to the level of judgement applied by management in determining loan loss provisions.

The identification of impairment and the determination of the recoverable amount are an inherently uncertain process involving various assumptions and factors, including the financial condition of the counterparty, expected future

Our work covered impairment of both Bank's and Group's Receivables from corporate counterparties and Receivables from financial institutions (other banks and leasing companies).

We assessed the design of the controls over individual impairment calculations and tested the operating effectiveness of the controls over individual impairment calculations of the Bank's and

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cash flows, and expected net selling prices of collaterals. The use of different modelling techniques and assumptions could produce significantly different estimates of loan loss provisions.

The portfolios which give rise to the greatest uncertainty are typically those where impairments are derived from estimates of future cash flows and realizable value of collateral, which are unsecured or are subject to potential collateral shortfalls. These are usually part of the Bank's loan placements to corporate debtors. Judgement is applied to determine appropriate Parameters and assumptions used to calculate impairment.

High level of uncertainty is also related to models used for impairment calculation for exposures toward financial institutions. Judgement is required to determine whether a loss has been incurred and a slight change in parameters used in the calculation could significantly affect the level of impairment recognized.
Due to the significance of loans and advances (representing 85% of Total assets of the Bank and 85% of Total assets at the Group level) and the related estimation uncertainty, this is considered a key audit matter.

the Group's Corporate portfolio including the quality of underlying data and systems.

We focused on the measurement of impairment of individually significant credit exposures, including the assessment of whether historic experience is appropriate when assessing the amount of incurred losses in the portfolios. In addition, we also focused on individually significant exposures that are not individually impaired, however, either continued to be, have become, or were at risk of being individually impaired.

We also assessed whether the separate and consolidated financial statement disclosures appropriately reflect the Bank's and the Group's exposure to credit risk and are compliant with the IFRS as adopted by EU requirements. Refer to Note 31.2 Credit risk for further details.

In addition we have performed the following substantive procedures for discrete parts of credit portfolio of the Bank and the Group:

<u>Financial Institutions portfolio</u>
We understood management's basis for determining whether the exposure toward certain financial institution is impaired and assessed the reasonableness using our understanding of the Bank's and Group's products, lending portfolios and our broader industry knowledge. Considering that due days and due debt do not timely reflect occurrence of default event of financial institutions, the Bank and the Group use internally developed rating model which takes into consideration financial and macro-prudential data of each financial institution. We understood and assessed the model used. Where changes had been made during the year in model parameters and assumptions, we understood the reasons why changes had taken place and used our industry knowledge and experience to evaluate the appropriateness of such changes. We also re-performed the provision calculation for entire portfolio applying our judgement. We understood and corroborated any material differences identified.

<u>Corporate portfolio</u>
We assessed the criteria for determining whether an impairment event had occurred and tested a sample of performing loans with characteristics that might imply an impairment event had occurred (including customers experiencing financial difficulties or clients with overdue debts for higher number of days

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for which impairment loss was not recognized) to assess whether all impairment events had been properly and timely identified by management. For a sample of individually impaired credit exposures within the Corporate portfolio we tested the assumptions underlying the impairment identification and quantification including forecasts of future cash flows, valuation of underlying collateral and estimates of recovery on default. This included taking into consideration the impact of forbearance as well as the latest developments at the borrower.

Other information included in The Bank's and the Group's 2016 separate and consolidated Annual Report

Management is responsible for the other information. Other information consists of the information included in the separate and consolidated Annual Report which includes the Management report and Corporate Governance Statement, other than the separate and consolidated financial statements and our auditor's report thereon. Our opinion on the separate and consolidated financial statements does not cover the Other information including the Management report and Corporate Governance Statement.

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

With respect to the Management Report and Corporate Governance Statement, we also performed procedures required by the Accounting Act (NN 78/15, 34/15, 120/16) in Croatia. Those procedures include considering whether the Management Report includes the disclosures required by Article 21 of the Accounting Act, and whether the Corporate Governance Statement includes the information specified in Article 22 of the Accounting Act.

Based on the procedures undertaken, to the extent we are able to assess it, we report that:

1. the information given in the enclosed Management report for the 2016 financial year are consistent, in all material respects, with the enclosed separate and consolidated financial statements;

2. the enclosed Management report for 2016 financial year is prepared in accordance with requirements of Article 21 of the Accounting Act;

3. Corporate Governance Statement, included in the Bank's and Group's separate and consolidated Annual report, includes the information referred to in Article 22., paragraph 1., items 2, 5, 6 and 7 of the Accounting Act; and

4. elements of Corporate Governance Statement containing the information referred to in Article 22, paragraph 1, items 3 and 4 of the Accounting Act, included in the Bank's and Group's separate and consolidated Annual report are prepared in accordance with requirements of the Accounting Act and are consistent, in all material respects, with the enclosed separate and consolidated financial statements;

In addition, in the light of the knowledge and understanding of the entity and its environment obtained in the course of the audit, we are also required to report if we have identified material misstatements in the Management Report, Corporate Governance Statement and separate and consolidated Annual report. We have nothing to report in this respect.

Responsibilities of management and Supervisory Board for the separate and consolidated financial statements

Management is responsible for the preparation and fair presentation of the separate and consolidated financial statements in accordance with IFRSs as adopted by EU, and for such internal control as management determines is necessary to enable the preparation of separate and consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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

Supervisory Board is responsible for overseeing the Bank's and Group's financial reporting process.

Auditor's responsibilities for the audit of the separate and consolidated financial statements

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

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

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

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

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

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

The partner in charge of the audit resulting in this independent auditor's report is Zvonimir Madunić.

Zvonimir Madunić
Member of the Board and certified auditor

Ernst & Young d.o.o.
Radnička cesta 50 (Green Gold), Zagreb
17 March 2017

Financial statements of the Group
Consolidated Statement of Profit or Loss
for the year ended 31 December 2016
(All amounts are expressed in HRK thousand)

	Notes	2016 HRK '000	2015 HRK '000
Interest income	3	871,985	873,997
Interest expense	4	(452,673)	(474,530)
Net interest income		**419,312**	**399,467**
Fee income	5	30,434	21,505
Fee expense	5	(3,265)	(659)
Net fee income		**27,169**	**20,846**
Net gains on financial operations	6	7,496	22,281
Other income		23,758	9,506
		477,735	**452,100**
Operating expenses	7	(160,288)	(140,875)
Impairment loss and provisions	8	(2,373)	(104,799)
Profit before income tax		**315,074**	**206,426**
Income tax	9	(233)	(161)
Profit for the year		**314,841**	**206,265**
Attributable to:			
Equity holder of the parent		**314,841**	**206,265**

The accompanying accounting policies and notes are an integral part of this Statement of Profit or Loss.

Consolidated Statement of Profit or Loss and Other Comprehensive Income for the year ended 31 December 2016

(All amounts are expressed in HRK thousand)

	2016 HRK '000	2015 HRK '000
Profit for the year	**314,841**	**206,265**
Other comprehensive income		
Items that are not transferred subsequently to profit or loss:		
Unrealized actuarial (losses)/gain	(3,255)	135
Total items that are not transferred subsequently to profit or loss	**(3,255)**	**135**
Items that may be reclassified subsequently to profit or loss:		
Increase in fair value of assets available for sale	86,526	39,381
Decrease in fair value of assets available for sale	(50,227)	(38,841)
Net foreign exchange on available for sale equity instruments	(234)	(73)
Transfer of realized gains on assets available for sale to statement of profit or loss	(2,114)	(6,226)
Transfer of realized losses on assets available for sale to statement of profit or loss	16	72
Deferred tax – other comprehensive income	(262)	(42)
Total items that may be reclassified subsequently to profit or loss	**33,705**	**(5,729)**
Other comprehensive income after income tax	**30,450**	**(5,594)**
Total comprehensive income after income tax	**345,291**	**200,671**
Attributable to:		
Equity holder of the parent	**345,291**	**200,671**

The accompanying accounting policies and notes are an integral part of this Statement of Profit or Loss and Other Comprehensive Income.

Consolidated Statement of Financial Position
for the year ended 31 December 2016
(All amounts are expressed in HRK thousand)

	Notes	2016 HRK '000	2015 HRK '000
Assets			
Cash on hand and due from banks	10	491,246	482,950
Deposits with other banks	11	23,872	359,397
Loans to financial institutions	12	11,889,111	12,522,652
Loans to other customers	13	11,511,194	9,223,069
Financial assets at fair value through profit or loss	14	286	3,707
Assets available for sale	15	3,390,034	2,870,315
Assets held to maturity	16	1,422	1,451
Investments in associates	18	-	-
Property, plant and equipment and intangible assets	19	57,305	62,238
Non-current assets held for sale	20	17,230	21,715
Other assets	21	9,122	5,278
Total assets		**27,390,822**	**25,552,772**
Liabilities			
Deposits	22	142,844	236,636
Borrowings	23	13,391,749	11,478,087
Bonds payable	24	3,105,569	3,366,566
Other liabilities	25	707,952	806,939
Total liabilities		**17,348,114**	**15,888,228**
Equity			
Founder's capital	26	6,959,632	6,926,632
Retained earnings and reserves		2,682,127	2,475,862
Other reserves		73,733	43,283
Profit for the year		314,841	206,265
Total equity attributable to equity holder of the parent		**10,030,333**	**9,652,042**
Guarantee fund	27	12,375	12,502
Total equity		**10,042,708**	**9,664,544**
Total liabilities and total equity		**27,390,822**	**25,552,772**

The accompanying accounting policies and notes are an integral part of this Statement of Financial Position.

Consolidated Statement of Cash Flows
for the year ended 31 December 2016
(All amounts are expressed in HRK thousand)

	Notes	2016 HRK '000	2015 HRK '000
Operating activities			
Profit before income tax		315,074	206,426
Adjustments to reconcile to net cash from and used in operating activities:			
Depreciation		7,428	7,654
Income tax		495	203
Impairment loss and provisions		2,373	104,799
Accrued interest		(47,016)	(21,226)
Deferred fees		10,149	6,773
Operating profit before working capital changes		*288,503*	*304,629*
Changes in operating assets and liabilities:			
Net decrease in deposits with other banks, before provision for impairment		338,749	879,939
Net decrease in loans to financial institutions, before provision for impairment		696,187	1,053,188
Net (increase) in loans to other customers, before provision for impairment		(2,311,708)	(1,074,727)
Net (gain) on financial assets at fair value through profit or loss		(121)	(83)
Net realized (gain) on assets available for sale		(2,098)	(6,154)
(Increase) of discount in assets available for sale, assets held to maturity and bonds payable		(1,935)	(16,584)
Net decrease in non-current assets held for sale		2,438	-
Net (increase) in other assets, before provision for impairment		(4,837)	(504)
Net (decrease)/increase in deposits from banks and companies		(93,792)	53,740
Net (decrease) in other liabilities, before provisions		(125,214)	(168,600)
Net cash (used in)/provided by operating activities		**(1,213,828)**	**1,024,844**
Investment activities			
(Purchase) of financial assets at fair value through profit or loss		(8,990)	(24,417)
Sale of financial assets at fair value through profit or loss		12,488	22,928
Net (purchase) of assets available for sale		(2,168,568)	(2,430,713)
Sale of assets available for sale		1,681,725	2,094,325
Net (purchase) of property, plant and equipment and intangible assets		(2,495)	(3,075)
Net cash (used in) investment activities		**(485,840)**	**(340,952)**
Financing activities			
Increase in founder's capital		33,000	32,893
Increase in borrowings – withdrawn funds		3,730,867	769,062
(Decrease) in borrowings – repayments of principal		(1,730,849)	(848,277)
(Decrease) in bonds payable – repayment		(224,487)	(226,915)
Net cash provided by/(used in) financing activities		**1,808,531**	**(273,237)**
Effect of foreign currency to cash and cash equivalents			
Net foreign exchange		(101,281)	(53,374)
Net effect		**(101,281)**	**(53,374)**
Net increase in cash and cash equivalents		7,582	357,281
Balance as of 1 January, before provisions		486,743	129,462
Net increase in cash		7,582	357,281
Balance as of 31 December, before provisions	10	**494,325**	**486,743**
Additional note - Operational cash flows			
Interest paid		462,758	481,715
Interest received		702,452	685,868

The accompanying accounting policies and notes are an integral part of this Statement of Cash Flows.

Consolidated Statement of Changes in Equity
for the year ended 31 December 2016

(All amounts are expressed in HRK thousand)

	Founder`s capital HRK '000	Retained earnings and reserves HRK '000	Other reserves HRK '000	Net profit for the year HRK '000	Total equity HRK '000
Balance as of 1 January 2015	**6,893,739**	**2,306,634**	**48,877**	**169,228**	**9,418,478**
Profit for the year	-	-	-	206,265	**206,265**
Other comprehensive income	-	-	(5,594)	-	**(5,594)**
Total comprehensive income	-	-	(5,594)	206,265	**200,671**
Capital paid-in from the State Budget (Note 26)	32,893	-	-	-	**32,893**
Transfer of profit 2014 to retained earnings	-	169,228	-	(169,228)	-
Balance as of 31 December 2015	**6,926,632**	**2,475,862**	**43,283**	**206,265**	**9,652,042**
Profit for the year	-	-	-	314,841	**314,841**
Other comprehensive income	-	-	30,450	-	**30,450**
Total comprehensive income	-	-	30,450	314,841	**345,291**
Capital paid-in from the State Budget (Note 26)	33,000	-	-	-	**33,000**
Transfer of profit 2015 to retained earnings	-	206,265	-	(206,265)	-
Balance as of 31 December 2016	**6,959,632**	**2,682,127**	**73,733**	**314,841**	**10,030,333**

The accompanying accounting policies and notes are an integral part of this Statement of Changes in Equity.

Financial statements of the Bank

Unconsolidated Statement of Profit or Loss

for the year ended 31 December 2016

(All amounts are expressed in HRK thousand)

	Notes	2016 HRK '000	2015 HRK '000
Interest income	3	870,344	872,609
Interest expense	4	(452,673)	(474,530)
Net interest income		**417,671**	**398,079**
Fee income	5	28,332	19,112
Fee expense	5	(3,265)	(659)
Net fee income		**25,067**	**18,453**
Net gains on financial operations	6	7,312	21,868
Other income		18,016	3,520
		468,066	**441,920**
Operating expenses	7	(152,227)	(131,840)
Impairment loss and provisions	8	(2,314)	(104,852)
Profit before income tax		**313,525**	**205,228**
Income tax	2	-	-
Profit for the year		**313,525**	**205,228**
Attributable to:			
Equity holder of the parent		**313,525**	**205,228**

The accompanying accounting policies and notes are an integral part of this Statement of Profit or Loss.

Unconsolidated Statement of Profit or Loss and Other Comprehensive Income for the year ended 31 December 2016

(All amounts are expressed in HRK thousand)

	2016 HRK '000	2015 HRK '000
Profit for the year	**313,525**	**205,228**
Other comprehensive income		
Items that are not transferred subsequently to profit or loss:		
Unrealized actuarial (losses)/gain	(3,255)	135
Total items that are not transferred subsequently to profit or loss	**(3,255)**	**135**
Items that may be reclassified subsequently to profit or loss:		
Increase in fair value of assets available for sale	84,151	37,754
Decrease in fair value of assets available for sale	(49,665)	(37,830)
Net foreign exchange on available for sale equity instruments	(234)	(73)
Transfer of realized gains on assets available for sale to statement of profit or loss	(1,878)	(5,819)
Transfer of realized losses on assets available for sale to statement of profit or loss	16	72
Total items that may be reclassified subsequently to profit or loss	**32,390**	**(5,896)**
Other comprehensive income after income tax	**29,135**	**(5,761)**
Total comprehensive income after income tax	**342,660**	**199,467**
Attributable to:		
Equity holder of the parent	**342,660**	**199,467**

The accompanying accounting policies and notes are an integral part of this Statement of Profit or Loss and Other Comprehensive Income.

Unconsolidated Statement of Financial Position
as of 31 December 2016

(All amounts are expressed in HRK thousand)

	Notes	2016 HRK '000	2015 HRK '000
Assets			
Cash on hand and due from banks	10	490,695	482,708
Deposits with other banks	11	23,872	356,351
Loans to financial institutions	12	11,889,111	12,522,652
Loans to other customers	13	11,511,194	9,223,069
Assets available for sale	15	3,343,574	2,832,323
Investments in subsidiaries	17	36,124	36,124
Investments in associates	18	-	-
Property, plant and equipment and intangible assets	19	57,216	62,083
Non-current assets held for sale	20	17,230	21,715
Other assets	21	5,900	3,751
Total assets		**27,374,916**	**25,540,776**
Liabilities			
Deposits	22	142,844	236,636
Borrowings	23	13,391,749	11,478,087
Bonds payable	24	3,105,569	3,366,566
Other liabilities	25	696,774	797,040
Total liabilities		**17,336,936**	**15,878,329**
Equity			
Founder's capital	26	6,959,632	6,926,632
Retained earnings and reserves		2,682,131	2,476,903
Other reserves		70,317	41,182
Profit for the year		313,525	205,228
Capital		**10,025,605**	**9,649,945**
Guarantee fund	27	12,375	12,502
Total equity		**10,037,980**	**9,662,447**
Total liabilities and total equity		**27,374,916**	**25,540,776**

The accompanying accounting policies and notes are an integral part of this Statement of Financial Position.

Unconsolidated Statement of Cash Flows
for the year ended 31 December 2016

(All amounts are expressed in HRK thousand)

	Notes	2016 HRK '000	2015 HRK '000
Operating activities			
Profit before income tax		313,525	205,228
Adjustments to reconcile to net cash from and used in operating activities:			
Depreciation		7,359	7,475
Impairment loss and provisions		2,314	104,852
Accrued interest		(47,037)	(21,089)
Deferred fees		10,149	6,773
Operating profit before working capital changes		*286,310*	*303,239*
Changes in operating assets and liabilities:			
Net decrease in deposits with other banks, before provision for impairment		335,749	865,968
Net decrease in loans to financial institutions, before provision for impairment		696,187	1,053,188
Net (increase) in loans to other customers, before provision for impairment		(2,311,708)	(1,074,727)
Net realized (gain) on assets available for sale		(1,862)	(5,747)
(Increase) of discount in assets available for sale and bonds payable		(2,341)	(16,835)
Net decrease in non-current assets held for sale		2,438	-
Net (increase) in other assets, before provision for impairment		(2,680)	(1,224)
Net (decrease)/increase in deposits from banks and companies		(93,792)	53,740
Net (decrease) in other liabilities, before provisions		(125,907)	(170,393)
Net cash (used in)/provided by operating activities		**(1,217,606)**	**1,007,209**
Investment activities			
Net (purchase) of assets available for sale		(2,158,899)	(2,406,810)
Sale of assets available for sale		1,679,193	2,086,420
Net (purchase) of property, plant and equipment and intangible assets		(2,492)	(3,025)
Net cash (used in) investment activities		**(482,198)**	**(323,415)**
Financing activities			
Increase in founder's capital		33,000	32,893
Increase in borrowings – withdrawn funds		3,730,867	769,062
(Decrease) in borrowings – repayments of principal		(1,730,849)	(848,277)
(Decrease) in bonds payable – repayment		(224,487)	(226,915)
Net cash provided by/(used in) financing activities		**1,808,531**	**(273,237)**
Effect of foreign currency to cash and cash equivalents			
Net foreign exchange		(101,454)	(53,385)
Net effect		**(101,454)**	**(53,385)**
Net increase in cash and cash equivalents		7,273	357,172
Balance as of 1 January, before provisions		486,501	129,329
Net increase in cash		7,273	357,172
Balance as of 31 December, before provisions	10	**493,774**	**486,501**
Additional note - Operational cash flows			
Interest paid		462,758	481,715
Interest received		700,366	684,330

The accompanying accounting policies and notes are an integral part of this Statement of Cash Flows.

Unconsolidated Statement of Changes in Equity
for the year ended 31 December 2016

(All amounts are expressed in HRK thousand)

	Founder`s capital HRK '000	Retained earnings and reserves HRK '000	Other reserves HRK '000	Net profit for the year HRK '000	Total equity HRK '000
Balance as of 1 January 2015	**6,893,739**	**2,308,560**	**46,943**	**168,343**	**9,417,585**
Profit for the year	-	-	-	205,228	**205,228**
Other comprehensive income	-	-	(5,761)	-	**(5,761)**
Total comprehensive income	-	-	(5,761)	205,228	**199,467**
Capital paid-in from the State Budget (Note 26)	32,893	-	-	-	**32,893**
Transfer of profit 2014 to retained earnings	-	168,343	-	(168,343)	-
Balance as of 31 December 2015	**6,926,632**	**2,476,903**	**41,182**	**205,228**	**9,649,945**
Profit for the year	-	-	-	313,525	**313,525**
Other comprehensive income	-	-	29,135	-	**29,135**
Total comprehensive income	-	-	29,135	313,525	**342,660**
Capital paid-in from the State Budget (Note 26)	33,000	-	-	-	**33,000**
Transfer of profit 2015 to retained earnings	-	205,228	-	(205,228)	-
Balance as of 31 December 2016	**6,959,632**	**2,682,131**	**70,317**	**313,525**	**10,025,605**

The accompanying accounting policies and notes are an integral part of this Statement of Changes in Equity.

1. General information

1.1. Group:

The Croatian Bank for Reconstruction and Development ("HBOR" or "the Bank") is the parent company of the Croatian Bank for Reconstruction and Development Group ("Group") that operates in the Republic of Croatia. The Group primarily performs banking activities and, to the lesser extent, insurance activities and credit risk assessment activities. These Financial Statements include unconsolidated and consolidated financial statements of the Bank and the Group.

The legal address of the Bank is Strossmayerov trg 9, Zagreb, Croatia.

The Group was formed in 2010, the Bank's subsidiary companies are Hrvatsko kreditno osiguranje d.d. and Poslovni info servis d.o.o. that constitute the Hrvatsko kreditno osiguranje Group ("HKO Group").

Croatian Bank for Reconstruction and Development is the 100% owner of HKO.

The legal address of the HKO Group is Zagreb, Bednjanska 12.

As of 31 December 2016, the Group had 364 employees (31 December 2015: 357 employees).

1.2. Bank:

The Croatian Bank for Reconstruction and Development ("HBOR" or "the Bank") was established on 12 June 1992 under the Act on the Croatian Credit Bank for Reconstruction ("HKBO"). In December 1995, the Bank changed its name to Croatian Bank for Reconstruction and Development. The founder and 100% owner of HBOR is the Republic of Croatia.

The Republic of Croatia guarantees HBOR's liabilities unconditionally, irrevocably and on first call, without issuing any particular guarantee. The responsibility of the Republic of Croatia as guarantor for HBOR´s liabilities is joint and unlimited.

With the Act on the Croatian Bank for Reconstruction and Development passed in December 2006, HBOR's founding capital was HRK 7 billion, the payment schedule of which is determined by the State budget.

As of 31 December 2016, there were 349 employees at the Bank (31 December 2015: 342 employees).

1. General information (continued)

1.2. Bank (continued):

1.2.1. Activities of the Bank:

The principal activities of the Bank comprise the following:
- financing of reconstruction and development of the Croatian economy,
- financing of infrastructure,
- promoting exports,
- providing support to the development of SMEs,
- promoting environmental protection, and
- providing domestic goods and services export insurance against non-market risks for and on behalf of the Republic of Croatia.

HBOR may perform other financial activities according to the decisions of the Government of the Republic of Croatia if, in their opinion, it is in the best interest of the Republic of Croatia.

1.3. Bodies of the Bank and the Group:

Supervisory Board
During 2016, the Supervisory Board members were as follows:

- Zdravko Marić, DSc, Minister of Finance - ex officio President of the Supervisory Board (since 4 March 2016),
- Boris Lalovac, MSc, Minister of Finance - ex officio President of the Supervisory Board (until 4 March 2016),
- Martina Dalić, DSc, Deputy Prime Minister and Minister of the Economy, Entrepreneurship and Trade – ex officio Vice President of the Supervisory Board (since 10 November 2016),
- Tomislav Panenić, Minister of Economy – ex officio Vice President of the Supervisory Board (from 4 March 2016 to 10 November 2016),
- Ivan Vrdoljak, Minister of Economy – ex officio Vice President of the Supervisory Board (until 4 March 2016),
- Gabrijela Žalac, Ministry of Regional Development and EU Funds – ex officio Member of the Supervisory Board (since 10 November 2016),
- Tomislav Tolušić, Minister of Regional Development and EU Funds – ex officio Member of the Supervisory Board (from 4 March 2016 to 10 November 2016),
- Luka Burilović, President of the Croatian Chamber of Economy – ex officio Member of the Supervisory Board,

  Members of the Supervisory Board:
- Gari Cappelli, Minister of Tourism (since 10 November 2016),
- Tomislav Tolušić, Minister of Agriculture (since 10 November 2016),
- Slaven Dobrović, DSc, Minister of Environmental Protection and Energetics (since 10 November 2016),
- Grozdana Perić, Chairman of the Finance and Central Budget Committee of the Croatian Parliament (since 9 November 2016),

1. General information (continued)

1.3. Bodies of the Bank and the Group (continued):

Supervisory Board (continued)

During 2016, the Supervisory Board members were as follows (continued):

- Boris Lalovac, MSc, Member of the Croatian Parliament (since 9 November 2016),
- Ivana Ninčević-Lesandrić, Member of the Croatian Parliament (since 9 November 2016),
- Anton Kliman (from 4 March 2016 to 10 November 2016),
- Davor Romić, Prof. DSc, (from 4 March 2016 to 10 November 2016),
- Darko Horvat (from 4 March 2016 to 10 November 2016),
- Branko Grčić, Prof. DSc (until 4 March 2016),
- Gordan Maras (until 4 March 2016),
- Darko Lorencin (until 4 March 2016),
- Tihomir Jakovina (until 4 March 2016).

Pursuant to the Act on Croatian Bank for Reconstruction and Development, the Supervisory Board consists of six ministers of the Government of the Republic of Croatia. The minister in charge of finances, the minister in charge of the economy and the minister in charge of regional development and EU funds are obligatory members of the Supervisory Board, whereas other three ministers are appointed to the Supervisory Board by the Government of the Republic of Croatia among the ministers in charge of tourism, agriculture, environmental protection and construction or entrepreneurship and craft. The Croatian Parliament appoints three members of the Supervisory Board and their permanent deputies among the members of the Croatian Parliament. The President of the Croatian Chamber of Economy is ex officio member of the Supervisory Board.

Management Board

In 2016, members of the Management Board were as follows:

- Dušan Tomašević, President of the Management Board,
- Martina Jus, Member of the Management Board,
- Goran Filipić, Member of the Management Board.

By the Decision of the Supervisory Board of HBOR of 25 January 2017, President and Members of the Supervisory Board of HBOR were dismissed from their duties as of 31 January 2017 as follows: Dušan Tomašević from the duty of the President of the Management Board and Martina Jus and Goran Filipić from their duties of members of the Management Board of HBOR.

By the Decision of the Supervisory Board of HBOR as of 25 January 2017, Tamara Perko, MSc is appointed the President of the Management Board of HBOR, and Martina Jus the Member of the Management Board of HBOR as of 1 February 2017 until the implementation of procedure for the selection and appointment of members of the Management Board of HBOR pursuant to the Decree on the Criteria for the Implementation of Procedures for Selection and Appointment of Presidents and Members of Management Board of Companies and Other Legal Entities of Strategic and Special Interest for the Republic of Croatia (Official Gazette Nos. 33/16, 46/16 and 109/16), but for the maximum period of six months.

Audit Committee

The term of office of the members of the Audit Committee lasts as long as the term of office of members of the Supervisory Board that has appointed it. After the termination of the term of office of members of the Supervisory Board, on 4 March 2016 until the day of compiling of these statements, new members of the Audit Committee has not been appointed and the Supervisory Board currently performs its role.

1. General information (continued)

1.4. Current economic situation and its impact on the Bank

So far, the economic situation in the Republic of Croatia has not had a significant impact on the financial position and performance of the Bank. The Bank monitors closely the credit, liquidity, interest rate and foreign exchange risk on a regular basis. The highest exposure of credit portfolio until the end of 2015 is the one towards financial institutions, which minimizes the level of credit risk due to strictly regulated banking sector by the central bank. However, in 2016, there is a tendency of increased direct exposures to other customers, and the proportion of gross placements via financial institutions and direct placements is 47% : 53% (in 2015: 53% : 47%).
In 2015, six-year negative trend of the economic activity in domestic economy was halted and GDP grew by 1.6%. According to the forecasts of the European Commission, in 2016, Croatia's economy is expected to have grown by 2.8%*, and in 2017, by 3.1%*. The growth of 1.7% in the third quarter of 2016 as compared to the previous quarter was higher than expected, and all components of domestic demand contributed to this strong performance. Due to the strong tourist season, exports of services jumped by 3.5%* q-o-q.
The strong growth momentum gathered in 2016 is projected to carry over to 2017 under the influence of tax reform on personal consumption and investments. Export of goods and services could in this respect provide the largest contribution to the overall GDP growth, while the domestic consumption is expected to strengthen significantly.

However, the Croatian economy is further confronted with macroeconomic imbalances, among others primarily the public debt and deficit level and it is certain that the consequences of the economic situation will further impact certain industries (construction, processing industries, real estate sector) and the ability of some customers to meet their loan obligations.

For that reason, the Management Board maintains its expectations for an increase in loan restructuring applications as it was the case in the last six business years. Additionally, there are uncertainties with regard to the possibility of collection under the collateral in view of the illiquid real estate market that is still not influenced by the economic growth as well as the decline in their value.

In 2017, HBOR will continue to encourage target segments and groups of customers that it encouraged in the previous years with emphasis on better utilisation of the EU proceeds in their financing.

The Bank has sufficient funds and high level of liquidity for financing planned loan activities, meeting obligations and liabilities and maintaining required level of liquidity.

** Source: European Commission web pages: Winter 2017 Economic Forecast for the Republic of Croatia dated 13 February 2017. Such forecasts are prepared by the Directorate General for Economic and Financial Affairs (ECFIN).*

2. Summary of significant accounting policies

2.1. Accounting policies

Principal accounting policies applied when preparing these financial statements are summarized below.

Accounting policies were consistently applied to all periods presented in these financial statements.

Basis of accounting

The Bank and the Group maintain their accounting records in HRK in accordance with Croatian law and the accounting principles and practices observed by financial institutions in the Republic of Croatia.

Statement of compliance

These consolidated and unconsolidated financial statements are prepared in accordance with International Financial Reporting Standards (IFRS), as issued by International Accounting Standards Board ("IASB") and endorsed by the EU.

Basis of financial statements presentation

The financial statements are prepared under the historical cost convention, with an exception of certain financial assets and financial liabilities that are measured and stated at fair value, as it can be seen in the following text:

Items	Measurement basis
Financial assets at fair value through profit or loss	Fair value
Assets available for sale	Fair value

The financial statements are prepared on an accrual and a going concern basis.

Reporting currency

The financial statements of the Bank and the Group are prepared in Croatian Kuna (HRK) as the functional and reporting currency of the Bank and the Group.

Amounts presented are rounded to a nearest thousand, unless otherwise stated.

The effective exchange rate of HRK as of 31 December 2016 was HRK 7.557787 per 1 Euro and HRK 7.168536 per 1 United States dollar (31 December 2015: HRK 7.635047 per 1 Euro and HRK 6.991801 per 1 United States dollar), unless otherwise contracted.

2. Summary of significant accounting policies

2.1. Accounting policies (continued)

Basis of consolidation

The financial statements include the Bank and the Group. The financial statements of the Group include the consolidated financial statements of the Bank and its subsidiary companies. Unconsolidated financial statements of the parent company are also stated.

Subsidiary companies

Subsidiary companies are all those companies that are controlled by the Bank.

Subsidiary companies are included into consolidated financial statements in accordance with the full consolidation method from the moment when the actual control is transferred to the Bank. The consolidation ceases from the moment they are sold or liquidated, i.e. from the moment when the control is lost.

With the beginning of application of new definition of control according to IFRS 10 Consolidated Financial Statements, the Group made a re-assessment of control and relations within the Group. The scope and substance of control are unchanged in the context of new requirements and definitions.

Investments in subsidiary companies are stated at investment cost, i.e. in accordance with the cost method.

When preparing data and consolidated financial statements, the amount of the parent's investment in each subsidiary and the parent's portion of equity of each subsidiary are eliminated, and intragroup balances and transactions, revenues and expenditures as well as unrealised gains and losses are eliminated in full.

The accounting policies of subsidiary companies are in line with those of the parent company in order to ensure comparability at the level of the Group.

The acquisition of subsidiaries is accounted by using the purchase method. The cost of the business combination is measured as the aggregate of the fair values (at the date of exchange) of assets given, liabilities incurred or assumed and equity instruments issued in exchange for control over the acquiree. Acquisition costs incurred are expensed and included in operating costs.

Non-controlling interests in the net assets of consolidated subsidiaries are identified separately from the parent's ownership interests in them. Non-controlling interests in the net assets consist of the amount of those non-controlling interests at the date of the initial recognition of investment in the subsidiary company and the non-controlling interests' share of changes in equity since the date of acquisition of the interest. Losses incurred by a subsidiary company will be allocated between controlling and non-controlling interests even if losses exceed the non-controlling equity investment in the subsidiary.

Subsequent acquisition of a non-controlling interest is not a business combination and is accounted for as an equity transaction.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Basis of consolidation (continued)

Subsidiary companies (continued)

For measurement of changes in relative interests of the parent and non-controlling interest in the subsidiary on the date of acquisition, the Group used the approach of taking into account the proportionate share of the acquiree's identifiable net assets. The amount of positive movements in the parent equity is recognised in other reserves.

In cases when investments into subsidiary companies that are stated by investment cost are classified as investments intended for sale or distribution, they are stated pursuant to IFRS 5 Non-Current Assets Held for Sale and Discontinued Operations. In such circumstances, measurement of investments calculated pursuant to IAS 39/IFRS 9 is not changed.

Associated companies

Associates are all those companies, in which the Group has directly or indirectly (e.g. through subsidiaries) a significant influence, i.e. is entitled to participate in decisions on the financial and operating policies of the investee, but does not have control of those policies. The Group has significant influence if holds, directly or indirectly 20% or more of the voting power of the investee. In 2016 the Group aligned its accounting policies with the amended and newly adopted standard 27 Separate Financial Statements.

Investments in associated companies are recognised using the equity method in the consolidated and separate financial statements. By applying the equity method, such investment is stated at investment cost at initial recognition, and its carrying amount of assets is increased or decreased on the basis of HBOR equity recognition in the profit or loss of the investee after the acquisition date. HBOR's equity in the profit or loss of the investee is included in the profit and loss of HBOR.

The amounts that the investee paid to HBOR reduce the carrying amount of the investment.

The changes in HBOR's proportional part occurred as a result of changes in other comprehensive income of the associated company (changes arising from revaluation of real estate, plants and equipment and foreign exchange gains/losses) are stated within other comprehensive income.

In case there is an intention to sell the entire or a portion of equity in associated companies, IFRS 5 Non-Current Assets Held for Sale and Discontinued Operations is applied, namely to the portion held for sale.

The remaining equity in associated companies intended to be hold, over which there is still a significant influence, will continue to be stated by applying the equity method.

Should over the remaining portion that is intended to be kept such significant influence cease, it will be stated as financial instrument pursuant to the provisions of IAS 39/IFRS 9 only after the sale of the equity.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Fair value measurement

Fair value represents the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction at the measurement date in the principal or the most advantageous market under current market conditions.

Basic price is an exit price, regardless of whether that price is directly observable or estimated using another valuation technique.

At initial recognition, when an asset is acquired or a liability is assumed in an exchange transaction for that asset or liability, the transaction price is the price paid to acquire the asset or received to assume the liability (an entry price).

The fair value of the asset or liability is the price that would be received to sell the asset or paid to transfer the liability (an exit price).

If another IFRS requires or permits an entity to measure an asset or a liability initially at fair value and the transaction price differs from fair value, the Group shall recognize the resulting gain or loss in profit or loss unless that IFRS specifies otherwise.

For measuring fair value the Group is maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

The Group selects inputs that are consistent with the characteristics of the asset or liability that market participants would take into account in a transaction for the asset or liability.

If an asset or a liability measured at fair value has a bid price and an ask price (e.g. an input from a dealer market), the Group uses the price within the bid-ask spread as the most representative of fair value.

Pursuant to aforesaid, the carrying amounts of cash and balances with the Croatian National Bank approximately present their fair values.

The estimated fair value of deposits approximates their carrying amounts since all deposits mature up to 90 days.

Loans and advances to banks and other customers are presented net of provisions for impairment. The estimated fair value of loans and advances represents the discounted amount of estimated future cash flows expected to be received. The interests subsidies that are recognized as deferred income in discounted amounts are presented within other liabilities are taken into account in estimating fair value. The fair value of HRK loans with one-way currency clause is assessed as described under the "Foreign currency transactions and foreign currency clause" paragraph.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Fair value measurement (continued)

The Bank's long-term borrowings have no quoted market price, and their fair value is estimated as the present value of future cash flows, discounted at interest rates in effect at the Statement of Financial Position date for new borrowings of a similar nature and with a similar remaining maturity. As the Bank's long term borrowings mostly bear variable interest, the Bank estimates that its carrying amount is reasonable approximation of fair value.

The fair value of bonds issued by HBOR on 31 December 2016 is stated in Note 24 and is presented by using level 2 inputs that are observable at Bloomberg service on the basis of mid-rate of Bloomberg Generic (BGN) prices.

BGN or Bloomberg Generic price is the simple average price that includes indicative prices and executable prices. The mid-rate is the average between the quoted "ask" price and the "bid" price.

The Group takes care of the fair value hierarchy presentation that comprises of three levels of inputs to valuation techniques used to measure fair value as follows:

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

The Group discloses transfers between levels of the fair value hierarchy at the end of the reporting period during which the transfer occurred.

Interest income and expense

Interest income and expense are recognized in the statement of profit or loss and other comprehensive income when earned or incurred. Interest income and expense are recognized in the statement of profit or loss and other comprehensive income for all interest-bearing instruments on an accrual basis using the effective interest rate, which is the rate that discounts estimated future cash payments or receipts through the expected life of the financial instrument or on a shorter period, where appropriate. Interest income includes coupons earned on fixed income investments.

Loan origination fees, together with estimated related costs, are deferred and proportionally recognized as an adjustment to the effective yield on the loan over the term of loan.

(All amounts are expressed in HRK thousand)

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Interest income and expense (continued)

Notional interest is recognized on impaired loans and other financial assets based on the rate used to discount future cash flows to their net present value and are recognized in the statement of profit or loss.

Fee and commission income

Fee and commission income is comprised mainly of fees receivable from companies for guarantees granted and other services rendered by the Group, together with commissions for managing funds for and on behalf of legal entities and fees for foreign and domestic payment transactions. Fees and commissions are generally recognized in the period when the related service is rendered.
Fees on issued financial/payment guarantees are deferred and are proportionally recognized and reported in the statement of profit or loss and other comprehensive income over the term of guarantee.
Fee and commission income of non-interest income character (loan management fees for and on behalf of other parties, payment transaction fees, other fees of non-interest type) are recognized in the statement of profit or loss as they incur.

Employee benefits

Pursuant to local legislation, the Group is obliged to pay contributions to the State Pension and Health Insurance Funds. This obligation relates to full-time employees and provides for paying contributions as certain percentages determined on the basis of the gross salary as follows:

	2016	2015
Contributions for state health insurance fund	15.00%	15.00%
Contributions for employment fund	1.70%	1.60%
Special contribution for employment of disabled persons	-	0.20%
Contribution for health protection at work	0.50%	0.50%

The Group is also obliged to withhold and pay contributions from gross pay on behalf of the employees to the State Pension Fund and Mandatory Pension Fund.

The Group does not have pension arrangements separate from the state pension system of the Republic of Croatia. This system requires that current contributions by the employer be calculated as a percentage of current gross salary payments; these expenses are charged to the statement of profit or loss and other comprehensive income in the period the related compensation is earned by the employee.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Employee benefits (continued)

The contributions on behalf of employees and on behalf of the employer are charged to expense in the period to which they relate. The Group calculates and pays required personal income tax and surtax on personal income tax from gross salary for each employee.

The Group recognizes provisions for other liabilities towards employees when there is a contractual obligation or practice in the past based on which the obligation has arisen. Further, the Group recognizes the liabilities for accumulated vacation allowances based on unutilised vacation days as of the date of the financial statements.

Foreign currency transactions and foreign currency clause

Assets and liabilities expressed in foreign currencies are converted into HRK at the exchange rates quoted by the Croatian National Bank at the Statement of Financial Position date or at the contract exchange rates. Income and expense arising in foreign currencies are converted at the rate of exchange on the transaction date. The resulting foreign exchange gains and losses are recorded in the Statement of Profit or Loss and Other Comprehensive Income.

The Bank has assets originated in HRK and linked to a foreign currency with a one-way currency clause. Due to this clause, the Bank has the option to revalue the asset using a foreign exchange rate, if beneficial for the Bank valid as of the date of maturity, compared to the foreign exchange rate valid as of the date of origination of asset.

Changes arising from one-way currency clause contracts, based on which the value of receivables and liabilities denominated in a functional currency is changed with regard to the respective contract foreign currency (embedded derivatives – weighted exchange rate) imply changes in the fair value of embedded derivatives. The Bank has assets originated in HRK that are linked to a foreign currency with two-way currency clause. These assets are translated to HRK as if they were originated in foreign currency.

The principal rates of exchange set forth by the Croatian National Bank and used in the preparation of the financial statements at the reporting dates were as follows:

31 December 2016	1 EUR = HRK 7.557787	1 USD = HRK 7.168536
31 December 2015	1 EUR = HRK 7.635047	1 USD = HRK 6.991801

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Taxation

Based on Article 9 of the Act on the HBOR, the parent company is exempt from income tax.

Income tax liabilities arise exclusively from the activities of the other members of the Group.

Income tax is charged on taxable profits in accordance with tax regulations and at the statutory tax rate.

Income tax expense is comprised of current and deferred tax. The amount of the income tax is reported in the statement of profit or loss and other comprehensive income except for the income tax that relates to the items that are recognised directly in equity and reserves when income tax is recognised in equity and reserves.

Current tax is the expected tax payable charged on the taxable amount of profits for the year by applying the tax rates in effect at the reporting date and all tax liability adjustments for previous periods.

The amount of deferred tax is calculated by applying the balance sheet liability method, providing for all temporary differences between the carrying amounts of assets and liabilities recorded for reporting purposes and the amounts used for tax calculation purposes. Deferred tax is calculated at the tax rates that are expected to apply on temporary differences when remunerated or settled in accordance with the valid regulations.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. Deferred tax liabilities are reviewed at each reporting date and reduced to the extent that it is no longer probable that the related tax benefits will be realisable.

Deferred tax assets and liabilities are not discounted; they are recognised as long-term assets and/or long-term liabilities.

Cash and cash equivalents

For the purposes of the cash flows reporting, cash and cash equivalents comprise cash and current accounts with the Croatian National Bank and other banks less provisions for impairment and un-collectable amounts.

Financial instruments

Financial assets and financial liabilities presented in the Statement of Financial Position include cash and cash equivalents, debt instruments, trade and other accounts receivable and payable, long-term loans and leases, deposits and investments.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Financial instruments (continued)

The Group classifies its own financial instruments into following categories:
- financial assets at fair value through profit or loss,
- available-for-sale financial assets,
- held-to-maturity financial assets,
- loans and receivables.

Financial instruments are classified into the above categories pursuant to the intention at acquisition. Classification of financial instruments at initial recognition and accounting principles of their measurement are prescribed by accounting policies brought by the Management Board.

The principal difference among the categories relates to the measurement approach of financial assets and the recognition of their fair values in the financial statements that is described in the text below.

All securities held by the Group are recognized using settlement date accounting and are initially measured at cost and directly attributable transaction costs when investments are not recognised at fair value through the statement of profit or loss.

The Bank does not make acquisitions of financial instruments and investments to attain gain from short term trading activities.

a) Financial assets at fair value through profit or loss

The above category is divided into two sub-categories: financial instruments held for trading purposes and those initially classified by the management into this category that are not traded actively.

Upon initial recognition, financial assets carried at fair value through profit or loss are accounted for and presented at fair value which corresponds to the quoted prices or amounts obtained by the application of acceptable valuation models. When measuring the fair value of shares in cash investment funds, the price that is applied is the price of the share in the fund as of a given date acquired from the investment fund management company. The Group includes unrealized gains and losses in 'Net gains/(losses) on financial operations'.

b) Available-for-sale financial assets

Assets available for sale are financial assets designated as available for sale or not classified as either held to maturity or carried at fair value through profit or loss or loans and receivables.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Financial instruments (continued)

b) Available-for-sale financial assets (continued)

Financial assets classified as assets available for sale are provided for the purposes of maintaining liquidity reserves or for the purpose of placement of available funds until their further placement in long-term loans. In the available-for-sale assets portfolio, investments in long-term securities and in other financial instruments are recorded, as well as equity instruments with the intention to hold over 90 days that are held for an unlimited period and shares in investment funds that the Bank intends to held for a period of over 30 days.

Subsequent to initial recognition, available-for-sale financial assets are re-measured at fair value based on quoted prices or amounts derived from cash flow models. In circumstances where the quoted market prices are not readily available, the fair value of debt instruments is estimated using various valuation techniques including the use of present value of future cash flows and mathematical models, while the fair value of unquoted equity instruments is estimated using applicable price/earnings or price/cash flow ratios refined to reflect the specific circumstances of the issuer.

For available for sale assets, unrealized gains and losses arising from changes in fair value are recognized directly in other comprehensive income, until their disposal or impairment, at which time the realized gain or loss is included in the statement of profit or loss.

Impairment losses on assets available for sale are presented in the statement of profit or loss. If the fair value of an equity instrument subsequently increases, the increase will be recognized in other comprehensive income, and will not be subsequently reversed in the statement of profit or loss. Impairment losses recognized in statement of profit or loss for debt instruments are subsequently reversed if an increase in the fair value of the instrument can be objectively related to an event occurring after the recognition.

When a decline in the fair value of available-for-sale financial assets has been recognized in other comprehensive income and there is an objective evidence that the asset is impaired according to IAS 39 provisions, the cumulative loss that has been recognized in other comprehensive income shall be reclassified from other comprehensive income to statement of profit or loss as a reclassification adjustment, even though the financial asset has not been derecognized.

The objective evidence on impairment loss on certain investment in an equity instrument includes information on significant adverse changes with impact on the technological, market, economic or legal conditions of operation of the issuer and indicates that the cost of investment in debt instruments cannot be recovered.

Significant or prolonged decline in the fair value of investments into debt instruments below their cost is also an objective evidence of impairment.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Financial instruments (continued)

b) Available-for-sale financial assets (continued)

Interest earned whilst holding available for sale instruments is accrued on a daily basis and is reported as 'Interest income' in the statement of profit or loss.

Foreign exchange gains/(losses) related to available for sale equity instruments held in foreign currency are recognized together with fair value gains and losses in other comprehensive income until the financial asset is sold. Foreign exchange gains/(losses) related to available-for-sale debt instruments in foreign currency are reported in the statement of profit or loss.

c) Held-to-maturity financial assets

Investments held-to-maturity are financial assets with fixed or identifiable payments and fixed maturities for which the Group has the intent and ability to hold to maturity. This portfolio generally comprises instruments issued for a period exceeding one year, such as bonds, bills of exchange etc.

Financial assets held to maturity are initially recognised at fair value, increased by transaction costs. After initial recognition, assets held to maturity are measured and stated at amortized investment cost, i.e. acquisition cost (nominal value of purchased securities increased/decreased by a discount/premium and transaction costs) adjusted by amortized discount/premium.

Interest earned is recognized as interest receivable on the date of settlement and is not HBOR's income.

The Group assesses on a regular basis whether there is any objective evidence that an investment held-to- maturity may be impaired. A financial asset is impaired if its carrying amount is greater than its estimated recoverable amount, which is equal to the present value of the expected future cash flows discounted at the financial instrument's original effective interest rate. The amount of the impairment loss for assets carried at amortized cost is calculated as the difference between the asset's carrying amount and the present value of the expected future cash flows discounted at the financial instrument's original effective interest rate. When an impairment of assets is identified, the Group recognizes provisions through the statement of profit or loss under 'Impairment loss and provisions'.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Financial instruments (continued)

d) Loans to financial institutions and other customers

Amounts paid-out by HBOR in providing funds directly to the borrower at drawdown are categorized as loans to customers and are carried at amortized cost derived from using the effective interest method and adjusted for possible impairment.

The amount of the subsidized interest provided for the final user under the Programme of Preferential Financing through HBOR's Loan Programmes is presented as deferred interest income in other liabilities and released over the term of the loan and is shown in the statement of profit or loss on a time basis during the repayment of the loan applying effective interest rate method.

All loans and advances are recognized when cash is paid-out to borrowers.

Provision for impairment is performed if there is objective evidence that HBOR will not be able to collect all amounts due. The Management Board of HBOR determines the adequacy of the provision based upon analysis of various factors, the structure of the loan portfolio and past experience (see Note 31.2. Risk management – Credit risk).

The amount of the provision is the difference between the carrying and recoverable amounts of the balance outstanding, being the present value of expected cash flows, including amounts recoverable from guarantees and collateral, discounted based on the effective interest rate.

The loan loss provision is also assessed on portfolio basis covering losses where there is objective evidence that possible losses are present, specifically identified in components of the loan portfolio at the Statement of Financial Position date. These have been estimated based upon historical patterns of losses (in each component, the credit ratings allocated to the borrowers and reflecting the current economic climate in which the borrowers operate).

If there is no objective evidence that an impairment loss has been incurred, whether it is significant or not, the financial asset is classified into the group of assets with similar credit risk characteristics and all assets from this group are subject to joint estimation for the purpose of a collective evaluation of impairment. Contracted cash flows and historical loss experience for assets with similar credit risk characteristics are subject to collective evaluation of expected cash flows.

When a loan is deemed uncollectible, it is written off against the related provision for impairment. Subsequent recoveries of these loans are recognized in the statement of profit or loss.

Securities purchased under agreements to purchase and resell ('reverse repos') are not recognized in the Statement of Financial Position of the Bank and expenses based on such contracts are recognized in the statement on financial position as loans to financial institutions collateralized by securities that are the subject matter of contracts. Interest earned in the period from the purchase until the resale of the security is accrued on a daily basis and reported as 'Interest income' in the statement of profit or loss.

(All amounts are expressed in HRK thousand)

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

At the end of 2016, the Group's REPO deals amounted to HRK 232,489 thousand (31 December 2015: HRK 606,930 thousand) collateralized by securities in the amount of HRK 247,026 thousand (31 December 2015: HRK 645,673 thousand).

Property, plant and equipment and intangible assets

Property, plant and equipment and intangible assets are initially recognized and subsequently measured at acquisition cost. Depreciation is charged using the linear method, by applying the annual rates ranging from 3.03% to 33.3% to the cost of assets over their estimated useful lives.

Estimated useful lives are as follows:

	2016	2015
	years	years
Buildings	33	33
Computers	3	3
Furniture and Equipment	5 - 8	5 - 8
Vehicles	3	3
Other assets and investments not mentioned	5	5
Intangible Assets	3 - 5	3 - 5

Depreciation is not charged on property, plant and equipment and intangible assets in the course of construction, until they are available for use. Repairs and maintenance are expensed in the statement of profit or loss and other comprehensive income as incurred. Expenditure that increases the future economic benefits of existing tangible and intangible assets (improvements) is capitalized.

Impairment of assets

An assessment of financial assets is made at the reporting date to determine whether there is objective evidence that a specific financial asset may be impaired. If such evidence exists, the estimated recoverable amount of that asset and any impairment loss, based on the net present value of future anticipated cash flows including anticipated recoveries from guarantees and collateral instruments, discounted by the original effective interest rate, is recognized in the statement of profit or loss.

Property, plant and equipment and intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Whenever the carrying amount of an asset exceeds its recoverable amount, an impairment loss is recognized in the statement of profit or loss and other comprehensive income for items of property, plant and equipment and intangible assets carried at cost. The recoverable amount is the higher of an asset's net selling price and its value in use.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Investments in property

Investments in property include investments of the Group in the real estate for the purpose of generating income from rent, but not investments held for sale within the framework of regular operations or for administration purposes.
Investments in property are initially recognized at purchase cost including the transaction costs. After initial recognition, investments in real estate are carried at purchase cost reduced by accumulated depreciation and impairment losses.

Investments in property are amortized by linear method through a period of 33 years.

Investments in property cease to be recognized at sale or at final withdrawal of investments in property from use or when no future economic benefits are expected from sale.
Gains or losses from withdrawal or sale of investments in property are recognized in the statement of profit or loss in the period of withdrawal or sale.
These assets are stated in note 21 Other assets due to immaterial amount.

Non-current assets held for sale

Non-current assets held for sale consist of property, plant and equipment that the Group acquired in settlement of uncollected receivables. The Group expects that the carrying amount of these assets will be recovered principally through a sale transaction rather than through continuing use.

This category of assets is initially stated at fair value less estimated expected costs to sell.

The Group measures these assets at the lower of its carrying amount and fair value (determined by an independent assessor) less estimated expected costs to sell.

Depreciation on these assets is not charged.

The Bank recognises an impairment provision for any initial or subsequent partial write-off of these assets up to the fair value less costs to sell. It recognises a gain for any subsequent increase in fair value of assets less costs to sell up to the amount of cumulative impairment provision that has been recognised.

Impairment provisions are recognized in the statement of profit or loss and other comprehensive income, as well as gains/losses upon subsequent measurement and on sale of the non-current assets.

The cases in which due to more difficult circumstances of sale because of objective circumstances and events beyond the Bank's control, the sale will not be completed in the planned period, or the period necessary for the conclusion of sale should be prolonged even after the period of one year, and a decision of an authorised body on giving up the sale or the plan of sale has not been made, and the activities are further undertaken to find a buyer and there is enough evidence that the Bank has remained consistent

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Non-current assets held for sale (continued)

with the plan of sale of such type of assets, do not exclude that the assets are still classified as non-current assets held-for-sale.

Bank's borrowings and bonds payable

Financial liabilities of the Bank and the Group arise from received loans and securities issued.

Financial liabilities are initially recognized at fair value, adjusted by transaction costs. After initial recognition, financial liabilities are measured at amortized cost determined using the effective interest rate method.

Financial liabilities are stated in the contracted currency translated to Kuna at the middle exchange rate of the Croatian National Bank, contract exchange rate or determined rate arising from business and financial transactions based on documentation.

The Group recognises interest expense related to borrowings and bonds payable in the statement of profit or loss.
Investments sold on the basis of repurchase agreement (repo agreements) continue to be recognized in the statement on financial position and are valued in compliance with the accounting policy for the respective financial asset. Receipts from sale of securities are stated as collateralized loans taken from financial institutions. Interest earned in the period from the sale of securities until the repurchase is calculated daily and stated in the statement on profit and loss under interest expenses.
At the end of 2016, for repo transactions in the amount of HRK 315,416 thousand (31 December 2015: HRK 0 thousand) the Group sold securities in the amount of HRK 345,049 thousand (31 December 2015: HRK 0 thousand).

Government grants

Interest for the borrowers qualifying for subsidized interest under the Programme of Preferential Financing through HBOR's Loan Programmes, the Financing Model for the Reconstruction and Modernisation of the Fishing Fleet, investments into entrepreneurial zones, the loans approved to young and/or start-up entrepreneurs is subsidized by the Republic of Croatia – the Ministry of Finance, Ministry of the Economy, Entrepreneurship and Trade and the Ministry of Agriculture during the entire loan repayment period.

The discounted amount of the interest subsidies provided for the final user is presented as deferred interest income in other liabilities and is recognized in the statement of profit or loss and other comprehensive income on a time basis during the repayment of the loan. Consequently, loans are measured at amortized cost by using interest rate without taking into account the effects of subsidies contributed by the State.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Guarantees and other loan related commitments

In the ordinary course of business, the Bank issues financial guarantees, including letters of credit that are recorded off-balance sheet. Financial guarantee contracts are initially measured at their fair values. Subsequent to initial recognition, guarantees are measured at fair value at the higher of the amount of the obligation under the contract and the amount initially recognized less, where appropriate, cumulative amortization recognized in accordance with the revenue recognition policies.

Contingent liabilities under guarantees are, to the extent of 82%, collateralized by the guarantees and deposits or the liability was taken over by the Republic of Croatia. Letters of credit are entirely covered by deposits.

Provisions for commitments upon undrawn loans and issued guarantees are maintained at a level considered as adequate by the Management Board in order to absorb potential losses.

Provisions are recognized when the Bank has a present legal or contractual obligation as a result of past events, when it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and when a reliable estimate of the amount of the obligation can be made.

Segment reporting

The Segment is a unique component of the Group and its operations are the supply of products or services (business segment) or the supply of products or services within a certain business environment (geographical segment) subject to unique risks and benefits, different from the ones in other segments.

The general format of business segments is based on the decision of the Management Board and the stated segments are in line with financial statements which are prepared in accordance with the International Financial Reporting Standards.

The Group has identified three main segments: banking activities, insurance activities and other activities.

Since the Group predominantly operates in the Republic of Croatia, there are no secondary (geographical) segments.

Managed funds for and on behalf of third parties

The Bank manages significant assets for and on behalf of the Ministry of Finance, Ministry of the Economy, Entrepreneurship and Trade, Ministry of the Sea, Transport and Infrastructure, Ministry of Agriculture, Ministry of Regional Development and EU Funds, Ministry of Environmental Protection and Energetics, Vodovod i kanalizacija d.o.o., Split and the Croatian Agency for SMEs, Innovation and Investments ("HAMAG-BICRO"), that are used for the financing of reconstruction and development programmes.

These amounts do not represent assets of HBOR and are excluded from the Bank's Statement of financial position but are recorded separately from the Bank's operations.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Managed funds for and on behalf of third parties (continued)

Revenues and expense relating to this business activity are charged to third parties, and the Bank does not have other liabilities nor bears any risks. For services provided within the framework of some of the programmes, the Bank charges a fee, whereas other programmes are performed by the Bank free of charge (see Note 29).

2.2. Significant accounting judgments and estimates

For the preparation of financial statements in accordance with IFRS's, the Management Board is required to give estimations and make assumptions that influence the reported balances of assets and liabilities and to disclose contingent amounts of assets and liabilities at the date of financial statements, and present income and expense for the reporting period. As a result of uncertainties which inherent in business activities, some items in the financial statements cannot be measured with precision but can only be estimated.

The procedure of estimation includes the judgements based on latest reliable information available at the reporting date, so that actual amounts may differ from those estimated.

The changes in accounting estimates are adjustments of the carrying amount of some assets or liabilities or the pattern of consumption during useful life arising through the estimation of the current situation and expected future benefits and obligations associated with these assets and liabilities.

The use of reasonable estimations is essential part of the preparation of financial statements and does not undermine their reliability.

The changes in accounting estimates occur if there are changes in circumstances based on which the estimation was based as a result of new information or more experience. The changes in estimates do not relate to prior periods and is not the correction of an error.

In the process of applying the Bank's accounting policies, the management has made judgments and estimates in determining the amounts recognized in the financial statements. The most significant use of judgments and estimates are as follows:

a) Fair value of financial instruments

If there is no active market for a certain financial instrument, or if for any other reason the fair value of financial assets and financial liabilities presented in the Statement of Financial Position cannot be reliably measured by the market price, the Group determines the fair value by using various valuation techniques including the use of mathematical models. The input data for these models are taken from other recognizable markets where possible, but if it is not possible, there is a certain degree of judgment required in determining fair values.

2. Summary of significant accounting policies (continued)

2.2. Significant accounting judgments and estimates (continued)

b) Valuation of financial instruments

The Bank's accounting policy on fair value measurements is discussed in Note 2.1. Fair value measurement and 32 Fair value of financial assets and financial liabilities .

c) Loan impairment provisions

The Bank regularly monitors its loans and receivables to assess impairment. The Bank uses its experience of judgments to estimate the amount of any impairment loss in cases where a borrower is in financial difficulties and there are several available sources of historical data relating to similar borrowers.

Similarly, the Bank estimates changes in future cash flows using the data indicating an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group.

The management uses estimates based on the historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the group of loans and receivables. The Bank uses its experience and judgment to adjust available data for a group of loans or receivables according to current market conditions.

d) Provisions for legal cases

The Group performs a risk classification of legal cases taking into consideration the legal basis of the claim, prior legal practice, opinions of relevant in-house lawyers, opinions of the outsourced attorneys and the Bank's own experience.

The Group makes provisions for legal cases in proportion with the total amount and estimated likelihood of not winning the case. In estimating provisions, the Bank takes into account the due legal process in the Republic of Croatia, which allows a multiple appeal procedure in certain cases.

Provisions for costs arising from initiated legal proceedings are reversed in the period in which legally valid sentence, arbitration award or settlement in the conciliation proceedings was made, pursuant to the procedures of monitoring legal cases against HBOR.

e) Provisions for retirement and jubilee benefits

In calculating provisions for retirement and jubilee benefits, the Group discounts expected future cash flows in respect of the liabilities, using discount rates that, in the opinion of the Bank's management, best represent the time value of the money.

Provisions for regular retirement and jubilee benefits are calculated and determined by a licensed actuary. Unrealised actuarial gains/(losses) arising from the calculation of provisions are stated within the framework of other comprehensive income so that net assets or liability may reflect the entire value of deficit or surplus planned.

2. Summary of significant accounting policies (continued)

2.3. Adoption of new and amended International financial reporting standards

The following new and amended IFRSs have been applied in the current year and have affected presentation and disclosures in these financial statements.

a) *New and amended International Financial Reporting Standards effective in the reporting period and adopted in the European Union with the assessment of impact on the financial statements:*

- Amendments to IAS 16 Property, Plant and Equipment and IAS 41 Agriculture (effective for periods beginning on or after 1 January 2016, adopted in the European Union on 23 November 2015) – Agriculture: Bearer Plants, amending the existing standard pertaining to the bearer biological assets. These amendments do not affect the Group after the initial application.

- Amendments to IFRS 11 Joint Arrangements (effective for periods beginning on or after 1 January 2016, adopted in the European Union on 24 November 2015) amending the provisions of the existing Standard and clarifying accounting for acquisitions of interests in joint operations. These amendments do not affect the Group after the initial application.

- Amendments to IAS 16 Property, Plant and Equipment and IAS 38 Intangible Assets (effective for periods beginning on or after 1 January 2016, adopted in the European Union on 2 December 2015) amending the existing Standard and clarifying acceptable methods of depreciation and amortization of long-term tangible and intangible assets. The Amendments aim to clarify that the use of revenue-based methods to calculate the depreciation of an asset is not appropriate because revenue generated by an activity that includes the use of an asset generally reflects factors other than the consumption of the economic benefits embodied in the asset. The Amendments also clarify that revenue is generally presumed to be an inappropriate basis for measuring the consumption of the economic benefits embodied in an intangible asset.
These amendments do not affect the Group after the initial application.

- Annual Improvements 2012-2014 (effective for periods beginning on or after 1 January 2016, adopted in the European Union on 15 December 2015) – primary with a view to removing inconsistencies and clarifying wording pertaining to:

    - IFRS 5 Non-current Assets Held for Sale and Discontinued Operations – changes in methods of disposal,

    - IFRS 7 Financial Instruments: Disclosures
        - Servicing contracts – additional guidance pertaining to the application of paragraph 42C of IFRS 7 relating to servicing contracts,
        - Applicability of the amendments to IFRS 7 to condensed interim financial statements – no disclosures are required in condensed interim financial statements pertaining to the offsetting of financial assets and financial liabilities until required by IAS 34 Interim Financial Reporting.

2. Summary of significant accounting policies (continued)

1.3. Adoption of new and amended International financial reporting standards (continued)

a) New and amended International Financial Reporting Standards effective in the reporting period and adopted in the European Union with the assessment of impact on the financial statements (continued):

- Annual Improvements 2012-2014 (continued)

  - IAS 19 Employee Benefits – Discount rate: regional market issue – high quality corporate bonds used in estimating the discount rate for post-employment benefits should be denominated in the same currency as the benefits to be paid,

  - IAS 34 Interim Financial Reporting – Disclosure of information "elsewhere in the interim financial report" – clarifies the meaning of the term and its application.

  These amendments do not affect the Group after the initial application.

- Amendments to IAS 1 Presentation of Financial Statements (effective for periods beginning on or after 1 January 2016, adopted in the European Union on 18 December 2015) – under the Disclosure Initiative. The amendments are design to serve as further incentive to companies by encouraging them to apply professional judgement in determining information to disclose in their financial statements and to clarify that companies should use professional judgement in determining where and in what order information is presented in the financial disclosures.
  These amendments have been applied to the financial statements of the Group.

- Amendments to IAS 27 Separate Financial Statements (effective for periods beginning on or after 1 January 2016, adopted in the European Union on 18 December 2015) allow the use of the equity method in separate financial statements to account for investments in subsidiaries, joint ventures and associates.

  The parent has aligned its accounting policies with the stated changes and amendments to IAS 27 that have been applied from 1 January 2016 onwards. Taking into account the Group's existing organisation and business model, these amendment does not affect the financial statements of the Group.

- Amendments to IFRS 10 Consolidated Financial Statements, IFRS 12 Disclosure of Interests in Other Entities and IAS 28 Investments in Associates and Joint Ventures (effective for periods beginning on or after 1 January 2016, adopted in the European Union on 22 September 2016) - Investment Entities – provide an exemption from the consolidation with an objective of clarifying the requirements when accounting for investment entities and provide relief in particular circumstances.

  The above amendments do not affect the Group after the initial application.

2. Summary of significant accounting policies (continued)

2.3. Adoption of new and amended International financial reporting standards (continued)

b) New and amended International Financial Reporting Standards that become effective in the reporting period, and that have not been adopted in the European Union yet:

- New IFRS 14 Regulatory Deferral Accounts – transitional standard (effective for periods beginning on or after 1 January 2016, but has not been adopted in the European Union yet) that refers to first-time adopters of IFRS currently recognising the deferral accounts in accordance with its previous generally accepted accounting principles, to enable them to continue so when they adopt IFRS. The disclosures are also prescribed identifying the nature of, and risk associated with, the rate regulation.

  The new IFRS does not affect the Group after the initial application.

c) New and amended International Financial Reporting Standards not effective in the reporting period and adopted in the European Union with the assessment of impact on the financial statements:

- New IFRS 15 Revenue from Contracts with Customers (effective for periods beginning on or after 1 January 2018, adopted in the European Union on 22 September 2016) establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. After its effective date, it will supersede the following standards and interpretations: IAS 18 Revenues; IAS 11 Construction Contracts; IFRIC 13 Customer Loyalty Programmes; IFRIC 15 Agreements for the Construction of Real Estate; IFRIC 18 Transfer of Assets from Customers and SIC 31 Revenue – Barter Transactions Involving Advertising Services.
  The core principle of IFRS 15 is for companies to recognise revenues to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.
  The standard establishes a five-step model framework that will be applied to revenues generated from contracts with customers irrespective of the type of transaction or activity as follows: identify the contract(s) with a customer, identify the performance obligations in the contract, determine the transaction price, allocate the transaction price to the performance obligations in the contract and recognise revenues when (or as) the entity satisfies a performance obligation. However, the standard does not apply to financial instruments and other contractual rights or obligations within the scope of IAS 39 Financial Instruments: Recognition and Measurement, i.e. IFRS 9 Financial Instruments, IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements, IAS 27 Separate Financial Statements and IAS 28 Investments in Associates and Joint Ventures, insurance contracts within the scope of IFRS 4 Insurance Contracts, and consequently it will not affect the Group after the initial application.

- IFRS 9 Financial instruments - in July 2014, the final wording of the new IFRS 9 Financial Instruments (effective for periods beginning on or after 1 January 2018, adopted in the European Union on 22 November 2016), that shall from the date of its effectiveness completely replace IAS 39 Financial Instruments: Recognition and Measurement, and contains requirements relating to the recognition and measurement, impairment, de-recognition and hedge accounting in general.

2. Summary of significant accounting policies (continued)

2.3. Adoption of new and amended International financial reporting standards (continued)

c) *New and amended International Financial Reporting Standards not effective in the reporting period and adopted in the European Union with the assessment of impact on the financial statements (continued):*

- IFRS 9 Financial instruments (continued)

  Classification and measurement of financial assets and financial liabilities – all recognised financial assets that is currently within the scope of IAS 39, shall from the date of application of IFRS 9 be measured either at amortised cost or at fair value.

  Impairment – IFRS 9 introduces a new expected loss impairment model according to which the occurrence of a credit loss is no longer necessary to recognise impairment. The entities recognise the annual expected credit loss or the expected credit loss throughout the lifetime of a financial instrument, depending on whether the credit risk has increased significantly since initial recognition. Any measurement of expected credit losses shall reflect the probability of outcome, incorporate the time value of money and be based on reasonable and supportable information.

  Hedge accounting – IRFS 9 introduces a substantially-reformed model for hedge accounting with enhanced disclosures about risk management activity. The new model represents a substantial overhaul of hedge accounting that aligns the accounting treatment with risk management activities.

  The Group shall not apply IFRS 9 in the period before its obligatory application.

  During 2016, the Bank started the IFRS 9 Implementation Project, engaging external consultants.

  Based on this project, the following phases are conducted:

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

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

2. Summary of significant accounting policies (continued)

2.3. Adoption of new and amended International financial reporting standards (continued)

c) *New and amended International Financial Reporting Standards not effective in the reporting period and adopted in the European Union with the assessment of impact on the financial statements (continued):*

- IFRS 9 Financial instruments (continued)

  For the impairment stream, the Bank is developing the methodology for calculating expected credit loss and modelling the risk parameters with incorporation of necessary parameters for forward looking expectations.

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

  Simultaneously, adjustments to HBOR's accounting policies and financial reporting processes are being made.

  Temporary exemption has been granted to the subsidiary company – the HKO Group – owing to immateriality and will be applied from 1 January 2018 to 1 January 2021, i.e. the start of the implementation of the new insurance contracts Standard, unless otherwise determined by the Croatian Financial Services Supervisory Agency (HANFA).

d) *New and amended International Financial Reporting Standards that become effective after the reporting period and that have not been adopted in the European Union:*

- Amended IFRS 10 Consolidated Financial Statements and IAS 28 Investments in Associates and Joint Ventures (application deferred for an indefinite period) dealing with the sale or contribution of assets between an investor and its associate or joint venture in the way that, in a transaction involving an associate or a joint venture, the extend of gain or loss recognition depends on whether the assets sold or contributed constitute a business.

  The Group shall apply the above amendments if such a transaction arises in the period after the start of the standard application.

- New IFRS 16 Leases (effective for periods beginning on or after 1 January 2019 but have not been adopted in the European Union yet) – sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer ("lessee") and the supplier "lessor"). The new standard requires lessees to recognize most leases on their financial statements. Lessees will have a single accounting model for all leases, with certain exemptions.
  The above new IFRS will not affect the significantly Group after the initial application.

2. Summary of significant accounting policies (continued)

2.3. Adoption of new and amended International financial reporting standards (continued)

d) New and amended International Financial Reporting Standards that become effective after the reporting period and that have not been adopted in the European Union (continued):

- Amended IAS 12 Income Taxes (effective for periods beginning on or after 1 January 2017, but has not been adopted in the European Union yet) – Recognition of Deferred Tax Assets for Unrealised Losses. IASB has concluded that the diversity in practice around the recognition of a deferred tax asset that is related to a debt instrument measured at fair value is mainly attributable to uncertainty about the application of some of the principles in IAS 12. Therefore the amendments consist of some clarifications and an illustrating example.
  This amendment will not affect the Group after the initial application.

- Amended IAS 7 Statement of Cash Flows (effective for periods beginning on or after 1 January 2017, but has not been adopted in the European Union yet) – Disclosure Initiative. The amendments come with the objective that entities shall provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including changes arising from cash flows and non-cash changes.
  This amendment will not affect the Group after the initial application.

- Changes and amendments to IFRS 15 Revenue from Contracts with Customers (effective for periods beginning on or after 1 January 2018, but have not been adopted in the European Union yet) – Clarifications to IFRS 15 issued.
  The amendments do not change the underlying principles of the standard, just clarify and offer some additional transition relief.

  The standard 15 does not apply to financial instruments and other contractual rights or obligations within the scope of IAS 39 Financial Instruments: Recognition and Measurement, i.e. IFRS 9 Financial Instruments, IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements, IAS 27 Separate Financial Statements and IAS 28 Investments in Associates and Joint Ventures, insurance contracts within the scope of IFRS 4 Insurance Contracts, and consequently it will not affect the Group after the initial application.

- Changes and amendments to IFRS 2 Share-Based Payment (effective for periods beginning on or after 1 January 2018, but have not been adopted in the European Union yet) – issued clarifications of IFRS 2 regarding the classification and measurement of share-based payment transactions.
  This amendment will not affect the Group after the initial application.

- Amendments to IFRS 4 Insurance Contracts - Applying IFRS 9 Financial Instruments with IFRS 4 (effective for periods beginning on or after 1 January 2018, but have not been adopted in the European Union yet) – the Amendments to existing requirements—IFRS 4 *Insurance Contracts*:
  - the „temporary exemption" - permit entities whose predominant activities are connected with insurance to defer the application of IFRS 9 until 2021; and

2. Summary of significant accounting policies (continued)

2.3. Adoption of new and amended International financial reporting standards (continued)

d) New and amended International Financial Reporting Standards that become effective after the reporting period and that have not been adopted in the European Union (continued):

- Amendments to IFRS 4 Insurance Contracts (continued):
  - the „overlay approach" - permit all issuers of insurance contracts to recognize in other comprehensive income, rather than profit or loss, the volatility that could arise when IFRS 9 is applied before the new insurance contracts Standard is issued.
  - Temporary exemption has been granted to the subsidiary company – the HKO Group – owing to immateriality and will be applied from 1 January 2018 to 1 January 2021, i.e. the start of the implementation of the new insurance contracts Standard, unless otherwise determined by the Croatian Financial Services Supervisory Agency (HANFA).

- Annual improvements 2014-2016 - The primary objective of the process is to enhance the quality of standards, by amending existing IFRSs to clarify guidance and wording, or to correct for relatively minor unintended consequences, conflicts or oversights.
  The issues included in this cycle are:

  - IFRS 12 Disclosure of Interests in Other Entities (effective for periods beginning on or after 1 January 2017, but have not been adopted in the European Union yet): Clarified the scope of the standard by specifying that the disclosure requirements in the standard, except for those in paragraphs B10–B16, apply to an entity's interests listed in paragraph 5 that are classified as held for sale, as held for distribution or as discontinued operations in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations.*

  - IFRS 1 First-time Adoption of International Financial Reporting Standards (effective for periods beginning on or after 1 January 2018, but have not been adopted in the European Union yet): Deleted the short-term exemptions in paragraphs E3–E7 of IFRS 1, because they have now served their intended purpose.

  - IAS 28 Investments in Associates and Joint Ventures (effective for periods beginning on or after 1 January 2018, but have not been adopted in the European Union yet): Clarified that the election to measure at fair value through profit or loss an investment in an associate or a joint venture that is held by an entity that is a venture capital organization, or other qualifying entity, is available for each investment in an associate or joint venture on an investment-by-investment basis, upon initial recognition.

2. Summary of significant accounting policies (continued)

2.3. Adoption of new and amended International financial reporting standards (continued)

d) New and amended International Financial Reporting Standards that become effective after the reporting period and that have not been adopted in the European Union (continued):

- New interpretation - IFRIC 22 Foreign Currency Transactions and Advance Consideration (effective for periods beginning on or after 1 January 2018, but have not been adopted in the European Union yet) – clarifies the accounting for transactions that include the receipt or payment of advance consideration in a foreign currency.

  The Interpretation covers foreign currency transactions when an entity recognizes a non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration before the entity recognizes the related asset, expense or income. It does not apply when an entity measures the related asset, expense or income on initial recognition at fair value or at the fair value of the consideration received or payed at a date other than the date of initial recognition of the non-monetary asset or non-monetary liability. Also, the Interpretation need not be applied to income taxes, insurance contracts or reinsurance contracts.

  The Interpretations Committee came to the following conclusion:

  - The date of the transaction, for the purpose of determining the exchange rate, is the date of initial recognition of the non-monetary prepayment asset or deferred income liability.
  - If there are multiple payments or receipts in advance, a date of transaction is established for each payment or receipt.

- Amendments to IAS 40 Investment Property—Transfers of investment property (effective for periods beginning on or after 1 January 2018, but have not been adopted in the European Union yet).

  The amendments in Transfers of Investment Property are:

  - Paragraph 57 has been amended to state that an entity shall transfer a property to, or from, investment property when, and only when, there is evidence of a change in use. A change of use occurs if property meets, or ceases to meet, the definition of investment property. A change in management's intentions for the use of a property by itself does not constitute evidence of a change in use.
  - The list of evidence in paragraph 57(a) – (d) was designated as non-exhaustive list of examples instead of the previous exhaustive list.

3. Interest income

Interest income by borrowers:

	Group 2016 HRK '000	Group 2015 HRK '000	Bank 2016 HRK '000	Bank 2015 HRK '000
Public sector	118,604	72,478	117,020	71,392
State-owned companies	42,607	43,503	42,607	43,503
Foreign companies	13,111	5,100	13,111	5,100
Domestic companies	340,611	356,283	340,611	356,259
Domestic financial institutions	284,149	313,120	284,092	312,842
Foreign financial institutions	136	940	136	940
Penalty interest	14,164	23,616	14,164	23,616
Other	58,603	58,957	58,603	58,957
	871,985	**873,997**	**870,344**	**872,609**

Interest income by type of facility:

	Group 2016 HRK '000	Group 2015 HRK '000	Bank 2016 HRK '000	Bank 2015 HRK '000
Interest on loans				
- financial institutions	284,291	313,479	284,291	313,479
- other customers	538,468	510,699	538,468	510,699
	822,759	824,178	822,759	824,178
Investments in securities	48,987	48,582	47,403	47,444
Deposits	239	1,236	182	987
Interest income on cash	-	1	-	-
	871,985	**873,997**	**870,344**	**872,609**

The difference between interest income and interest received or collected (see Statement of Cash Flows) mostly relates to the income in respect to interest subsidies inflows that are recorded upon payment. The discounted amount of the interest subsidies provided for the final user is presented as deferred interest income (see Note 25 Other liabilities) and is recognized in the statement of profit or loss and other comprehensive income on a time basis during the repayment of the loan. Interest income earned on this basis in 2016 amounts to HRK 128,312 thousand (31 December 2015: HRK 162,451 thousand).

Further, the difference between interest income and interest collected relates to the amount of loan fees and accrued interest. Loan fees are collected after origination of the loan, but their recognition in the statement of profit or loss and other comprehensive income is performed using effective interest rate method. Accrued interest is recognized in the statement of profit or loss and other comprehensive income on a time basis.

4. Interest expense

Interest expense by type of payee:

	Group		Bank	
	2016 HRK '000	2015 HRK '000	2016 HRK '000	2015 HRK '000
Domestic financial institutions	11,627	10,655	11,627	10,655
Foreign financial institutions	441,046	463,875	441,046	463,875
	452,673	**474,530**	**452,673**	**474,530**

Interest expense by type of facility:

	Group		Bank	
	2016 HRK '000	2015 HRK '000	2016 HRK '000	2015 HRK '000
Borrowings	280,115	289,793	280,115	289,793
Debt securities	172,518	184,737	172,518	184,737
Deposits	40	-	40	-
	452,673	**474,530**	**452,673**	**474,530**

The difference between interest expense and interest paid (see the Statement of Cash Flows) mostly relates to the changes in the amount of the interest accrued in relation to the prior year and the amortization of discount for issued debt securities.

5. Net fee income

	Group		Bank	
	2016 HRK '000	2015 HRK '000	2016 HRK '000	2015 HRK '000
Fee income:				
From issued guarantees	20,945	11,991	20,945	11,991
From managed funds for and on behalf of third parties	6,733	6,666	6,733	6,666
From payment operations	585	350	585	350
Reinsurance commission income	2,102	2,393	-	-
Other	69	105	69	105
	30,434	**21,505**	**28,332**	**19,112**
Fee expense	(3,265)	(659)	(3,265)	(659)
Net fee income	**27,169**	**20,846**	**25,067**	**18,453**

6. Net gains on financial operations

	Group		Bank	
	2016 HRK '000	2015 HRK '000	2016 HRK '000	2015 HRK '000
Net foreign exchange gains/(losses) on foreign currency assets:				
Cash on hand, accounts at banks and due from banks	(2,107)	(7,104)	(2,107)	(7,052)
Loans given to financial institutions and other customers	(98,092)	(31,227)	(98,092)	(31,227)
Financial assets at fair value through profit or loss	(44)	1	-	-
Assets held to maturity	(15)	(5)	-	-
Assets available for sale	(10,047)	(634)	(9,931)	(624)
Other	1,811	297	1,811	297
	(108,494)	(38,672)	(108,319)	(38,606)
Net foreign exchange gains/(losses) on foreign currency liabilities:				
Deposits	1,355	(1,842)	1,355	(1,842)
Borrowings and issued long-term securities	112,780	55,942	112,780	55,942
Other	(364)	616	(366)	627
	113,771	54,716	113,769	54,727
Net foreign exchange gains on foreign currency assets and liabilities	**5,277**	**16,044**	**5,450**	**16,121**
Gains on assets at fair value through profit or loss and realized gains on assets available for sale	2,219	6,237	1,862	5,747
Net gains on financial operations	**7,496**	**22,281**	**7,312**	**21,868**

7. Operating expenses

Operating expenses can be shown as follows:

	Group		Bank	
	2016 HRK '000	2015 HRK '000	2016 HRK '000	2015 HRK '000
General and administrative expenses:				
Employee expenses	87,801	82,641	84,830	79,472
Depreciation	7,428	7,654	7,359	7,475
Administration expenses	15,163	12,750	14,851	12,519
Material and services	29,862	29,780	28,220	28,078
	140,254	132,825	135,260	127,544
Other expenses:				
Taxes and contributions	704	663	700	658
Other expenses	19,330	7,387	16,267	3,638
	20,034	8,050	16,967	4,296
	160,288	**140,875**	**152,227**	**131,840**

Other expenses of the Group presented contain changes in technical reserves:

	Group		Bank	
	2016 HRK '000	2015 HRK '000	2016 HRK '000	2015 HRK '000
Change in the claims provision	(2,251)	3,373	-	-
Change in the claims provision, reinsurer's share	2,217	(1,892)	-	-
Expenses of insurance operations	**(34)**	**1,481**	-	-

The most significant part of provisions for losses relates to the IBNR provision, the method of calculation of which was changed as compared to the previous year. The Bornhuetter-Ferguson method was used for the gross amount of provisions that enable the supervision of development of the subsidiary company's loss by the year of delivery. The reinsurance share is determined in accordance with the valid terms and conditions of reinsurance contracts for the respective year of delivery. Further to this, this provision decreased both in the gross amount and in the reinsurance share in comparison with the previous year.

8. Impairment loss and provisions

The provision for impairment losses on placements may be summarized as follows:

		Group		Bank
	2016	2015	2016	2015
	HRK '000	HRK '000	HRK '000	HRK '000
Impairment losses on cash on hand and due from financial institutions	(714)	3,120	(714)	3,120
Impairment losses on deposits with other banks	(3,462)	(8,702)	(3,462)	(8,702)
Impairment losses on loans to financial institutions	(39,164)	(81,637)	(39,164)	(81,637)
Impairment losses on loans to other customers and interest	20,690	162,645	20,690	162,645
Impairment losses on non-current assets held for sale	2,047	12,512	2,047	12,512
Impairment losses on assets available for sale	-	(807)	-	(807)
Impairment losses on other assets	528	248	531	270
Total increase in provision for impairment losses on assets	(20,075)	87,379	(20,072)	87,401
Provision for guarantees and commitments	11,922	20,809	11,922	20,809
Other provisions	10,526	(3,389)	10,464	(3,358)
Total increase in provision for guarantees and commitments and other provisions	22,448	17,420	22,386	17,451
Total increase of provisions	**2,373**	**104,799**	**2,314**	**104,852**

9. Income tax

Based on Article 9 of the Act on the HBOR, the parent company is exempt from income tax. Income tax liabilities arise exclusively from the activities of the other members of the Group.

		Group
	2016	**2015**
	HRK '000	**HRK '000**
Recognised in the Statement of Profit or Loss		
Deferred tax expenditure	(233)	(161)
Income tax	**(233)**	**(161)**
Income tax reconciliation		
Profit before tax	**1,548**	**1,197**
Income tax at 20% rate	(224)	(149)
Non-deductible expense	(40)	(34)
Tax-exempt income	31	22
Income tax recognised in the Statement of Profit or Loss	**(233)**	**(161)**
Recognised in the Statement of Profit or Loss and Other Comprehensive Income		
Deferred tax expenditure	(262)	(42)
Income tax recognised in the Statement of Profit or Loss and Other Comprehensive Income	**(262)**	**(42)**
Deferred tax liabilities throughout the year	**(495)**	**(203)**

10. Cash on hand and due from banks

		Group		Bank
	2016 HRK 000	2015 HRK 000	2016 HRK 000	2015 HRK 000
Account with the Croatian National Bank	186,167	107,353	186,167	107,353
Due from domestic banks in foreign currency	1,626	900	1,626	900
Due from foreign banks in foreign currency	305,981	378,248	305,981	378,248
Due from domestic banks in HRK	551	242	-	-
	494,325	486,743	493,774	486,501
Provisions for impairment losses	(3,079)	(3,793)	(3,079)	(3,793)
	491,246	**482,950**	**490,695**	**482,708**

Due from foreign banks in foreign currency includes the amount drawn from a loan tranche approved by the International Bank for Reconstruction and Development (IBRD) under the credit line „Croatia Export Finance Intermediation Loan Project" and amounts to EUR 0 thousand (31 December 2015: EUR 8,759 thousand).

The movements in the provision for impairment losses on amounts due from banks may be summarized as follows:

		Group		Bank
	2016 HRK 000	2015 HRK 000	2016 HRK 000	2015 HRK 000
Balance as at 1 January	3,793	673	3,793	673
Increase of provision for impairment losses on amounts due from banks	-	3,120	-	3,120
Release of provision for impairment losses on amounts due from banks	(714)	-	(714)	-
Balance as at 31 December	**3,079**	**3,793**	**3,079**	**3,793**

11. Deposits with other banks

	2016	Group 2015	2016	Bank 2015
	HRK '000	HRK '000	HRK '000	HRK '000
Deposits with foreign banks	20,789	305,402	20,789	305,402
Deposits with domestic banks	3,330	57,466	3,330	54,466
Accrued interest	1	239	1	193
	24,120	363,107	24,120	360,061
Provisions for impairment losses	(248)	(3,710)	(248)	(3,710)
	23,872	**359,397**	**23,872**	**356,351**

The movements in the provision for impairment losses on deposits with other banks may be summarized as follows:

	2016	Group 2015	2016	Bank 2015
	HRK '000	HRK '000	HRK '000	HRK '000
Balance as of 1 January	3,710	12,412	3,710	12,412
Release of provision for impairment losses on deposits with other banks	(3,462)	(8,702)	(3,462)	(8,702)
Balance as of 31 December	**248**	**3,710**	**248**	**3,710**

12. Loans to financial institutions

Loans to financial institutions, net of provision for impairment losses, may be summarized as follows:

		Group		Bank
	2016	2015	2016	2015
	HRK '000	HRK '000	HRK '000	HRK '000
Long-term loans under loan programmes	11,918,947	12,075,158	11,918,947	12,075,158
Short-term loans and reverse repo transactions	362,489	971,930	362,489	971,930
Accrued interest	37,363	14,043	37,363	14,043
Deferred recognition of loan origination fees	(66,371)	(66,533)	(66,371)	(66,533)
	12,252,428	12,994,598	12,252,428	12,994,598
Provisions for impairment losses	(363,317)	(471,946)	(363,317)	(471,946)
	11,889,111	**12,522,652**	**11,889,111**	**12,522,652**

The movements in the provision for impairment losses on loans to financial institutions may be summarized as follows:

		Group		Bank
	2016	2015	2016	2015
	HRK '000	HRK '000	HRK '000	HRK '000
Balance as of 1 January	471,946	564,191	471,946	564,191
Increase of provision for impairment losses on loans to financial institutions	45,864	94,621	45,864	94,621
Release of provision for impairment losses on loans to financial institutions	(85,028)	(176,258)	(85,028)	(176,258)
Net foreign exchange losses on provision for impairment losses	(1,927)	(1,055)	(1,927)	(1,055)
Provisions transferred from loans to other customers	203	-	203	-
Provisions transferred to loans to other customers	(67,741)	(9,553)	(67,741)	(9,553)
Balance as of 31 December	**363,317**	**471,946**	**363,317**	**471,946**

Transfer of provisions to loans to other customers relates to the transfer of provisions of Jadranska banka d,d., Šibenik in rehabilitation proceedings (in 2015, Nava banka d.d. Zagreb in bankruptcy proceedings) to final borrowers for placements taken over by HBOR into a direct creditor-debtor relationship.

12. Loans to financial institutions (continued)

Loans to financial institutions, net of provision for impairment losses, by purpose of the loan programme may be summarized as follows:

	Group		Bank	
	2016 HRK '000	2015 HRK '000	2016 HRK '000	2015 HRK '000
Loan programme for reconstruction and development of the economy	2,775,682	3,244,064	2,775,682	3,244,064
Export financing	3,466,148	3,612,334	3,466,148	3,612,334
Loan programme for reconstruction and development of infrastructure in the Republic of Croatia	1,602,331	1,681,125	1,602,331	1,681,125
Loan programme for small and medium-sized enterprises	4,064,711	3,526,036	4,064,711	3,526,036
Loan programme for war-torn and demolished housing and business facilities	10,075	11,599	10,075	11,599
Other	362,489	971,930	362,489	971,930
Accrued interest	37,363	14,043	37,363	14,043
Deferred recognition of loan fees	(66,371)	(66,533)	(66,371)	(66,533)
	12,252,428	12,994,598	12,252,428	12,994,598
Provisions for impairment losses	(363,317)	(471,946)	(363,317)	(471,946)
	11,889,111	**12,522,652**	**11,889,111**	**12,522,652**

Average interest rates for total loans to financial institutions are stated at 1.07% (31 December 2015: 1.22%) and for loans under HBOR loan programmes excluding the liquidity reserve at 1.07% (31 December 2015: 1.21%).

Average interest rates reflect the ratio of interest income generated from the mentioned placements and average assets.

Item "Other" refers to reverse REPO agreements in the total amount of HRK 232,489 thousand (31 December 2015: HRK 606,930 thousand). The above placements are collateralized by securities in the amount of HRK 247,026 thousand (31 December 2015: HRK 645,673 thousand).

13. Loans to other customers

Loans to other customers, net of provision for impairment losses, may be summarized as follows:

	Group		Bank	
	2016	2015	2016	2015
	HRK '000	HRK '000	HRK '000	HRK '000
Domestic companies	10,463,392	8,721,759	10,463,392	8,721,759
State-owned companies	1,183,103	1,353,314	1,183,103	1,353,314
Public sector	1,528,564	678,730	1,528,564	678,730
Foreign companies	237,429	232,742	237,429	232,742
Non-profit institutions	1,712	5,972	1,712	5,972
Other	712,400	768,720	712,400	768,720
Accrued interest	83,423	69,086	83,423	69,086
Deferred recognition of loan origination fees	(119,328)	(102,098)	(119,328)	(102,098)
	14,090,695	11,728,225	14,090,695	11,728,225
Provisions for impairment losses	(2,579,501)	(2,505,156)	(2,579,501)	(2,505,156)
	11,511,194	**9,223,069**	**11,511,194**	**9,223,069**

The movements in the provision for impairment losses on loans to other customers may be summarized as follows:

	Group		Bank	
	2016	2015	2016	2015
	HRK '000	HRK '000	HRK '000	HRK '000
Balance as of 1 January	2,505,156	2,346,608	2,505,156	2,346,608
Increase of provision for impairment losses on loans to other customers and interest	256,313	333,586	256,313	333,586
Release of provision for impairment losses on loans to other customers and interest	(234,827)	(170,885)	(234,827)	(170,885)
Net foreign exchange losses on provision for impairment losses	(9,333)	(3,244)	(9,333)	(3,244)
Collection of off-balance sheet receivables	(796)	(56)	(796)	(56)
Provisions transferred from off-balance sheet	796	56	796	56
Acquisition of immovable property	(1,078)	-	(1,078)	-
Write-offs	(4,268)	(10,462)	(4,268)	(10,462)
Provisions transferred to loans to financial institutions	(203)	-	(203)	-
Provisions transferred from loans to financial institutions	67,741	9,553	67,741	9,553
Balance as of 31 December	**2,579,501**	**2,505,156**	**2,579,501**	**2,505,156**

Provisions transferred from loans to financial institutions in the amount of HRK 67,741 thousand (31 December 2015: HRK 9,553 thousand) relates to the transfer of provisions of Jadranska banka d.d., Šibenik in rehabilitation proceedings (in 2015 Nava banka d.d., Zagreb in bankruptcy proceedings), to final borrowers for placements taken over by HBOR into a direct creditor-debtor relationship.

13. Loans to other customers (continued)

The movements in the provision for impairment losses on loans to other customers may be summarized as follows (continued):

Value adjustment of loans to other customers was reduced by the amount of HRK 1,078 thousand relating to takeover of the real estate in the execution procedure. The amount of HRK 759 thousand relates to interest written off due to the repurchase of receivables, impossibility of collection, settlement under the cancelled contract, removal of debtors from the court register as a result of pre-bankruptcy settlement procedure and death of debtors, whereas the amount of HRK 3,509 thousand relates to the principal written off as a result of death of debtors, settlement under the cancelled contract, repurchase of HBOR's receivable and the impossibility of collection.

Loans to other customers, net of provision for impairment losses, may be summarized by loan programme as follows:

		Group		Bank
	2016	**2015**	**2016**	**2015**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**
Loan programme for reconstruction and development of the economy	4,123,892	3,807,190	4,123,892	3,807,190
Export financing	4,687,115	3,254,161	4,687,115	3,254,161
Loan programme for reconstruction and development of infrastructure in the Republic of Croatia	3,075,022	2,513,074	3,075,022	2,513,074
Loan programme for small and medium-sized enterprises	2,158,612	2,115,820	2,158,612	2,115,820
Other	81,959	70,992	81,959	70,992
Accrued interest	83,423	69,086	83,423	69,086
Deferred recognition of loan origination fees	(119,328)	(102,098)	(119,328)	(102,098)
	14,090,695	11,728,225	14,090,695	11,728,225
Provisions for impairment losses	(2,579,501)	(2,505,156)	(2,579,501)	(2,505,156)
	11,511,194	**9,223,069**	**11,511,194**	**9,223,069**

Average interest rates on loans to other customers are stated at 2.04% (31 December 2015: 1.99%).
Average interest rates reflect the ratio of interest income from generated the mentioned placements and average assets.

14. Financial assets at fair value through profit or loss

		Group		Bank
	2016	**2015**	**2016**	**2015**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**
Shares in investment funds recognised at fair value through profit or loss	286	3,707	-	-
Balance as at 31 December	**286**	**3,707**	**-**	**-**

15. Assets available for sale

	Group		Bank	
	2016 HRK '000	2015 HRK '000	2016 HRK '000	2015 HRK '000
Debt instruments:				
Listed debt instruments:				
Bonds of the Ministry of Finance of the Republic of Croatia	925,887	679,617	884,914	644,532
Financial institution bonds	910	930	-	-
Corporate bonds	1,161	396	-	-
Treasury bills of the Ministry of Finance of the Republic of Croatia	1,500,420	1,418,963	1,500,420	1,418,963
Accrued interest	14,495	14,441	13,890	13,862
	2,442,873	**2,114,347**	**2,399,224**	**2,077,357**
Unlisted debt instruments:				
Corporate bonds	502	2,320	502	1,551
Accrued interest	99	31	99	30
	601	**2,351**	**601**	**1,581**
Equity instruments:				
Listed equity instruments:				
Investments in company's shares	10,938	-	10,938	-
	10,938	**-**	**10,938**	**-**
Unlisted equity instruments:				
Investments in shares of foreign legal entities	32	26	32	26
Investments in financial institutions shares	161	161	161	161
Shares of foreign financial institutions – EIF (Note 28)	25,815	24,420	25,815	24,420
Investments in company's shares	16,725	23,834	16,725	23,834
Provision for impairment losses	(16,725)	(23,834)	(16,725)	(23,834)
	26,008	**24,607**	**26,008**	**24,607**
Investments in investment funds:				
Shares classified as assets available for sale	909,614	729,010	906,803	728,778
	909,614	**729,010**	**906,803**	**728,778**
Balance as at 31 December	**3,390,034**	**2,870,315**	**3,343,574**	**2,832,323**

The movements in the provision for impairment losses on assets available for sale may be summarized as follows:

	Group		Bank	
	2016 HRK '000	2015 HRK '000	2016 HRK '000	2015 HRK '000
Balance as at 1 January	23,834	24,641	23,834	24,641
Increase of provisions for impairment losses on assets available for sale	2,721	4,594	2,721	4,594
Reversal of provisions for impairment losses on assets available for sale	(2,721)	(5,401)	(2,721)	(5,401)
Carrying at fair value	(7,109)	-	(7,109)	-
Balance as at 31 December	**16,725**	**23,834**	**16,725**	**23,834**

15. Assets available for sale (continued)

The following text contains investment breakdown:

	Date of issue	Date of maturity	Interest rate (%)	Group 2016 HRK '000	Group 2015 HRK '000	Bank 2016 HRK '000	Bank 2015 HRK '000
Debt instruments:							
Listed debt instruments:							
Bonds of the Republic of Croatia indexed to foreign currency:							
RHMF-O-19BA	29.11.2004	29.11.2019.	5.375	48,602	51,273	47,588	47,883
RHMF-O -227E	22.7.2011.	22.7.2022.	6.5	172,432	169,365	172,432	169,365
RHMF-O-247E	10.7.2013.	10.7.2024.	5.75	17,802	17,238	12,558	12,188
RHMF-O-203E	5.3.2010.	5.3.2020.	6.5	875	884	-	-
Bonds of the Republic of Croatia in foreign currency:							
XS0645940288	8.7.2011.	9.7.2018.	5.875	57,370	58,159	57,370	58,159
XS0776179656	27.4.2012.	27.4.2017.	6.25	14,529	14,476	14,529	14,476
XS1117298916	11.3.2015.	11.3.2025.	3.0	53,248	48,455	53,248	48,455
Bonds of the Republic of Croatia in HRK:							
RHMF-O-167A	22.7.2011.	22.7.2016.	5.75	-	139,066	-	139,066
RHMF-O-172A	8.2.2007.	8.2.2017.	4.75	100,995	103,396	100,410	102,800
RHMF-O-187A	10.7.2013.	10.7.2018.	5.25	42,406	42,712	37,094	37,415
RHMF-O-17BA	25.11.2010.	25.11.2017.	6.25	161,910	4,839	157,185	-
RHMF-O-203A	5.3.2010.	5.3.2020.	6.75	3,003	2,974	-	-
RHMF-O-257A	9.7.2015.	9.7.2025.	4.5	9,335	8,755	-	-
RHMF-O-26CA	14.12.2015.	14.12.2026.	4.25	41,909	18,025	33,089	14,725
RHMF-O-217A	8.7.2016.	8.7.2021.	2.75	201,471	-	199,411	-
Financial institution bonds in HRK:							
RIBA-O-17BA	23.11.2012.	23.11.2017.	5.88	522	525	-	-
Financial institution bonds indexed to foreign currency:							
RIBA-O-177A	18.7.2011.	18.7.2017.	6.5	388	405	-	-
Corporate bonds in HRK:							
JDGL-O-20CA	21.12.2015.	21.12.2020.	5.81	770	-	-	-
Corporate bonds indexed to foreign currency:							
JRLN-O-17AA	24.10.2012.	24.10.2017.	6.5	391	396	-	-
Treasury bills in HRK up to 364			0.438 - 0.977	1,087,406	963,968	1,087,406	963,968
Treasury bills indexed to foreign currency up to 364			-	-	190,612	-	190,612
Treasury bills in foreign currency up to 455 days			0.752	413,014	264,383	413,014	264,383
Accrued interest				14,495	14,441	13,890	13,862
				2,442,873	**2,114,347**	**2,399,224**	**2,077,357**
Unlisted debt instruments:							
Corporate bonds indexed to foreign currency:							
LNGU-O-31AE	24.7.2015.	15.10.2031.	4.5	502	1,551	502	1,551
Corporate bonds in HRK:							
JDGL-O-20CA	21.12.2015.	21.12.2020.	5.81	-	769	-	-
Accrued interest				99	31	99	30
				601	**2,351**	**601**	**1,581**

15. Assets available for sale (continued)

The following text contains investment breakdown (continued):

	Group		Bank	
	2016	2015	2016	2015
	HRK '000	HRK '000	HRK '000	HRK '000
Equity instruments:				
Listed equity instruments:				
Investments in company's shares	10,938	-	10,938	-
	10,938	**-**	**10,938**	**-**
Unlisted equity instruments:				
Investments in shares of foreign legal entities in foreign currency	32	26	32	26
Investments in financial institutions' shares	161	161	161	161
Investments in shares of foreign financial institutions in foreign currency - EIF	25,815	24,420	25,815	24,420
Investments in companie's shares	16,725	23,834		23,834
Provisions for impairment losses	(16,725)	(23,834)	(16,725)	(23,834)
	26,008	**24,607**	**26,008**	**24,607**
Investments in investments funds in the Republic of Croatia	**909,614**	**729,010**	**906,803**	**728,778**
Total	**3,390,034**	**2,870,315**	**3,343,574**	**2,832,323**

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-19BA) issued with foreign currency clause on 29 November 2004 are repayable over 15 years with an interest rate of 5.375%. As of 31 December 2016, the value of these outstanding bonds for the Group amounted to HRK 48,602 thousand (31 December 2015: HRK 51,273 thousand) and for the Bank HRK 47,588 thousand (31 December 2015: HRK 47,883 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-227E) issued with foreign currency clause on 22 July 2011 are repayable over 11 years with an interest rate of 6.5%. As of 31 December 2016, the value of these outstanding bonds amounted to HRK 172,432 thousand (31 December 2015: HRK 169,365 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-247E) issued with foreign currency clause on 10 July 2013 are repayable over 11 years with an interest rate of 5.75%. As of 31 December 2016, the value of these outstanding bonds for the Group amounted to HRK 17,802 thousand (31 December 2015: HRK 17,238 thousand) and for the Bank HRK 12,558 thousand (31 December 2015: HRK 12,188 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-203E) issued with foreign currency clause on 5 March 2010 are repayable over 10 years with an interest rate of 6.5%. As of 31 December 2016, the value of these outstanding bonds amounted to HRK 875 thousand (31 December 2015: HRK 884 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (XS0645940288) issued in foreign currency on 8 July 2011 are repayable over 7 years with an interest rate of 5.875%. As of 31 December 2016, the value of these outstanding bonds amounted to HRK 57,370 thousand (31 December 2015: HRK 58,159 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (XS0776179656) issued in foreign currency on 27 April 2012 are repayable over 5 years with an interest rate of 6.25%. As of 31 December 2016, the value of these outstanding bonds amounted to HRK 14,529 thousand (31 December 2015: HRK 14,476 thousand).

15. Assets available for sale (continued)

Bonds of the Ministry of Finance of the Republic of Croatia (XS1117298916) issued in foreign currency on 11 March 2015 are repayable over 10 years with an interest rate of 3.0%. As of 31 December 2016, the value of these outstanding bonds amounted to HRK 53,248 thousand (31 December 2015: HRK 48,455 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-167A) issued in kuna on 22 July 2011 are repayable over 5 years with an interest rate of 5.75%. The bonds were deemed upon maturity on 22 July 2016 (31 December 2015: HRK 139,066 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-172A) issued in kuna on 8 February 2007 are repayable over 10 years with an interest rate of 4.75%. As of 31 December 2016, the value of these outstanding bonds for the Group amounted to HRK 100,995 thousand (31 December 2015: HRK 103,396 thousand) and for the Bank HRK 100,410 thousand (31 December 2015: HRK 102,800 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-187A) issued in kuna on 10 July 2013 are repayable over 5 years with an interest rate of 5.25%. As of 31 December 2016, the value of these outstanding bonds for the Group amounted to HRK 42,406 thousand (31 December 2015: HRK 42,712 thousand) and for the Bank HRK 37,094 thousand (31 December 2015: HRK 37,415 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-17BA) issued in kuna on 25 November 2010 are repayable over 7 years with an interest rate of 6.25%. As of 31 December 2016, the value of these outstanding bonds for the Group amounted to HRK 161,910 thousand (31 December 2015: HRK 4,839 thousand) and for the Bank HRK 157,185 thousand (31 December 2015: HRK 0 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-203A) issued in kuna on 5 March 2010 are repayable over 10 years with an interest rate of 6.75%. As of 31 December 2016, the value of these outstanding bonds amounted to HRK 3,003 thousand (31 December 2015: HRK 2,974 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-257A) issued in kuna on 9 July 2015 are repayable over 10 years with an interest rate of 4.5%. As of 31 December 2016, the value of these outstanding bonds amounted to HRK 9,335 thousand (31 December 2015: HRK 8,755 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-26CA) issued in kuna on 14 December 2015 are repayable over 11 years with an interest rate of 4.25%. As of 31 December 2016, the value of these outstanding bonds for the Group amounted to HRK 41,909 thousand (31 December 2015: HRK 18,025 thousand) and for the Bank HRK 33,089 thousand (31 December 2015: HRK 14,725 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-217A) issued in kuna on 8 July 2016 are repayable over 5 years with an interest rate of 2.75%. As of 31 December 2016, the value of these outstanding bonds for the Group amounted to HRK 201,471 thousand and for the Bank HRK 199,411 thousand (31 December 2015: HRK 0 thousand).

Financial institution bonds (RIBA-O-17BA) issued in kuna on 23 November 2012 and are repayable over 5 years with an interest rate of 5.88%. As of 31 December 2016, the value of these outstanding bods amounted to HRK 522 thousand (31 December 2015: HRK 525 thousand).

15. Assets available for sale (continued)

Financial institution bonds (RIBA-O-177A) issued with foreign currency clause on 18 July 2011 and are repayable over 6 years with an interest rate of 6.5%. As of 31 December 2016, the value of these outstanding bonds amounted to HRK 388 thousand (31 December 2015: HRK 405 thousand).

Corporate bonds (JDGL-O-20CA) issued in kuna on 21 December 2015 and are repayable over 5 years with an interest rate of 5.81%. As of 31 December 2016, the value of these outstanding bonds amounted to HRK 770 thousand (31 December 2015: HRK 769 thousand). The bond of the company Jadran – Galenski laboratorij d.d. was listed on the official market of the Zagreb Stock Exchange in March 2016.

Corporate bonds (JRLN-O-17AA) issued with foreign currency clause on 24 October 2012 and are repayable over 5 years with an interest rate of 6.5%. As of 31 December 2016, the value of these outstanding bods amounted to HRK 391 thousand (31 December 2015: HRK 396 thousand).

Corporate bonds (LNGU-O-31AE) issued with foreign currency clause on 24 July 2015 and are repayable over 16 years with an interest rate of 4.5%. As of 31 December 2016, the value of these outstanding bods amounted to HRK 502 thousand (31 December 2015: HRK 1,551 thousand). By the Agreement on Transfer of Bonds of the company Lanište d.o.o. concluded on 10 September 2015 between HBOR and Ingra d.d., 203,078 bonds issued by the company Lanište d.o.o. were transferred for the settlement of HBOR's claims (fees for issued counter-guarantees and other receivables), and pursuant to the pre-bankruptcy settlement concluded between Ingra and the creditor in the pre-bankruptcy settlement procedure. In the settlement procedure, it was established that HBOR's claim would be settled by transfer of bonds. The bonds of the company Lanište d.o.o. are not listed.

In 2007, HBOR made acquisitions of five shares of the European Investment Fund (EIF), and on 15 July 2014 it made acquisitions of three more shares of EIF that were as of 31 December 2016 stated under Assets available for sale in the total amount of HRK 25,815 thousand (31 December 2015: HRK 24,420 thousand). The payment made represents 20% of the nominal amount of purchased shares and the other 80% makes a contingent liability towards EIF. On 31 December 2016 this contingent liability was EUR 6.4 million (31 December 2015: EUR 6.4 million) (Note 28).
The General Meeting, acting on a proposal from the Board of Directors, may require payment of the subscribed but not paid capital to the extent required for the Fund to meet its liabilities towards its creditors. Such payment shall be effected within 90 days from the decision of the General Meeting.

Corporate shares comprise shares in capital of the company for the production of agricultural products, Vinka d.d., and of the shipyard company Brodogralište Viktor Lenac d.d., Rijeka. The shares were acquired within restructuring measures for those companies in exchange for a portion of receivables. In March 2010, when all preconditions were met, HBOR's receivables were partly turned into an equity share in the company Vinka d.d., Vinkovci amounting to HRK 16,725 thousand, representing a 5.1823% of the equity share belonging to HBOR in the company's equity.
HBOR effected a 100% impairment of value for the complete amount of the equity share since it was estimated uncollectable.

In 2011, however, owing to an increase in capitalisation, the percentage of HBOR's share in the company's equity was changed to 0.9365%. The shares of the company Vinka d.d., Vinkovci (LPVC-R-B) are not listed.

Upon the commencement of bankruptcy proceedings of the company Brodogradilište Viktor Lenac d.d. in December 2003, HBOR effected a 100% impairment of value for the complete amount of receivables from the company, since they were estimated uncollectable, and the receivables were classified as bad and doubtful receivables.

15. Assets available for sale (continued)

On the conclusion of the bankruptcy proceedings in April 2008, the equity of the shipyard company was divided into 12,407,813 common shares in the nominal value of HRK 10.00 per share, issued in the procedure of conclusion of the bankruptcy proceedings by registration of rights – receivables in cash. HBOR registered a part of recognized receivables in the amount of HRK 13,673 thousand from the bankruptcy proceedings into the equity of the debtor, by which the Bank acquired 11.0194% of the equity of the company. The conversion of a portion of receivables into the equity in the above mentioned amount has been recorded and stated with a 100% value adjustment, transferred from off-balance sheet.

In 2011, owing to an increase in capitalisation, the percentage of HBOR's share in the company's equity was changed to 8.1321%. The shares of the company (VLEN-R-B) were listed in 2008 at the Zagreb Stock Exchange, and trade started in May 2009. Quoted price per share as of 31 December 2016 amounted to HRK 8.00 (31 December 2015: HRK 5.20 per share).

Pursuant to the decision of the subsidiary's management dated 30 September 2015, 18 December 2015, 31 March 2016, 5 September 2016, 28 October 2016 and 8 December 2016, shares in investment funds were classified as assets available for sale.

16. Assets held to maturity

	2016	Group 2015	2016	Bank 2015
	HRK '000	HRK '000	HRK '000	HRK '000
Debt instruments:				
Listed debt instruments:				
Bonds of the Ministry of finance of the Republic of Croatia	1,408	1,437	-	-
Accrued interest	14	14	-	-
Balance as at 31 December	**1,422**	**1,451**	**-**	**-**

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-203E) issued with foreign currency clause on 5 March 2010 are repayable over 10 years with an interest rate of 6.5%. As of 31 December 2016, the value of these outstanding bonds amounted to HRK 476 thousand (31 December 2015: HRK 488 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-19BA) issued with foreign currency clause on 29 November 2004 are repayable over 15 years with an interest rate of 5.375%. As of 31 December 2016, the value of these outstanding bonds amounted to HRK 932 thousand (31 December 2015: HRK 949 thousand).

17. Investments in subsidiaries

As at 31 December 2016, the Bank's subsidiaries are as follows:

Consolidated company	Activity	Ownership 2016	Ownership 2015	Investment 2016	Investment 2015
Direct share					
Hrvatsko kreditno osiguranje d.d. Zagreb, Republic of Croatia	Providing insurance for company's foreign and domestic short-term receivables regarding shipments of goods and services	100%	100%	36,124	36,124
Total				**36,124**	**36,124**

Result of the subsidiary has been disclosed in Appendix – Financial performance of the HKO Group.

18. Investments in associates

	Group 2016 HRK '000	Group 2015 HRK '000	Bank 2016 HRK '000	Bank 2015 HRK '000
Investments in associates	23,687	23,687	23,687	23,687
Value adjustments	(23,687)	(23,687)	(23,687)	(23,687)
	-	-	-	-

Investments in associates were carried out within a Program of investments in the equity of companies – small and medium sized entrepreneurs or pursuant to single decisions of authorized bodies of HBOR. The investments were made for a period ranging from 4 to 6 years with the right of HBOR to sell the shares after the contracted term of holding an equity stake.

	Line of business	% ownership in 2016	% ownership in 2015
Bila boja d.o.o., Grohote, in bankruptcy	Production of plastic products	17.96%	17.96%
THC d.o.o., Obrovac	Production of metal products	38.45%	38.45%
Tri D Drvo d.o.o., Vrhovine, in bankruptcy	Wood processing, production of wood products	26.00%	26.00%
Pounje d.d., Hrvatska Kostajnica	Textile industry – clothes production	13.55%	13.55%
Metal-Sint Oklaj d.d., Oklaj	Metal industry sintered products and composed material production	40.84%	40.84%

The value of investment was 100% adjusted in prior years due to assessed non-recoverability of the investment.

19. Property, plant and equipment and intangible assets

Group 2016	Buildings	Computers	Furniture, equipment and vehicles	Property, plant and equipment and intangible assets not ready for use	Total property, plant and equipment	Intangible assets	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Cost							
At 31 December 2015	**77,102**	**11,690**	**15,133**	**896**	**104,821**	**27,611**	**132,432**
Additions	-	-	-	2,539	2,539	-	2,539
Transfer from assets not yet ready for use	-	294	321	(2,399)	(1,784)	1,784	-
Adjustment of intangible assets	-	-	-	-	-	17	17
Disposals and write-offs	-	(766)	(218)	-	(984)	(3,830)	(4,814)
At 31 December 2015	**77,102**	**11,218**	**15,236**	**1,036**	**104,592**	**25,582**	**130,174**
Accumulated depreciation							
At 31 December 2015	**25,809**	**8,891**	**12,358**	**-**	**47,058**	**23,136**	**70,194**
Depreciation for 2016	2,336	1,546	1,000	-	4,882	2,546	7,428
Adjustment of intangible assets - Amortisation	-	-	-	-	-	17	17
Disposals and write-offs	-	(755)	(185)	-	(940)	(3,830)	(4,770)
At 31 December 2016	**28,145**	**9,682**	**13,173**	-	**51,000**	**21,869**	**72,869**
Net book value at 31 December 2016	**48,957**	**1,536**	**2,063**	**1,036**	**53,592**	**3,713**	**57,305**
Net book value at 31 December 2015	**51,293**	**2,799**	**2,775**	**896**	**57,763**	**4,475**	**62,238**

19. Property, plant and equipment and intangible assets (continued)

Group 2015	Buildings	Computers	Furniture, equipment and vehicles	Property, plant and equipment and intangible assets not ready for use	Total property, plant and equipment	Intangible assets	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Cost							
At 31 December 2014	**77,102**	**12,008**	**15,518**	**1,440**	**106,068**	**24,840**	**130,908**
Additions	-	-	-	3,090	3,090	-	3,090
Transfer from assets not yet ready for use	-	102	76	(3,634)	(3,456)	3,456	-
Disposals and write-offs	-	(487)	(505)	-	(992)	(685)	(1,677)
Returned to service	-	67	44	-	111	-	111
At 31 December 2015	**77,102**	**11,690**	**15,133**	**896**	**104,821**	**27,611**	**132,432**
Accumulated depreciation							
At 31 December 2014	**23,473**	**7,357**	**11,759**	**-**	**42,589**	**21,502**	**64,091**
Transfer from/to	-	4	(4)	-	-	-	-
Depreciation for 2015	2,336	1,944	1,054	-	5,334	2,320	7,654
Disposals and write-offs	-	(481)	(495)	-	(976)	(686)	(1,662)
Returned to service	-	67	44	-	111	-	111
At 31 December 2015	**25,809**	**8,891**	**12,358**	**-**	**47,058**	**23,136**	**70,194**
Net book value at 31 December 2015	**51,293**	**2,799**	**2,775**	**896**	**57,763**	**4,475**	**62,238**
Net book value at 31 December 2014	**53,629**	**4,651**	**3,759**	**1,440**	**63,479**	**3,338**	**66,817**

19. Property, plant and equipment and intangible assets (continued)

Bank 2016	Buildings	Computers	Furniture, equipment and vehicles	Property, plant and equipment and intangible assets not ready for use	Total property, plant and equipment	Intangible assets	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Cost							
At 31 December 2015	**77,102**	**11,311**	**14,895**	**896**	**104,204**	**26,990**	**131,194**
Additions	-	-	-	2,511	2,511	-	2,511
Transfer from assets not ready for use	-	285	312	(2,371)	(1,774)	1,774	-
Adjustment of intangible assets	-	-	-	-	-	17	17
Returned to service	-	(766)	(173)	-	(939)	(3,830)	(4,769)
At 31 December 2016	**77,102**	**10,830**	**15,034**	**1,036**	**104,002**	**24,951**	**128,953**
Accumulated depreciation							
At 31 December 2015	**25,809**	**8,575**	**12,201**	**-**	**46,585**	**22,526**	**69,111**
Depreciation for 2016	2,336	1,509	980	-	4,825	2,534	7,359
Adjustment of intangible assets - Amortisation	-	-	-	-	-	17	17
Returned to service	-	(755)	(165)	-	(920)	(3,830)	(4,750)
At 31 December 2016	**28,145**	**9,329**	**13,016**	**-**	**50,490**	**21,247**	**71,737**
Net book value at 31 December 2016	**48,957**	**1,501**	**2,018**	**1,036**	**53,512**	**3,704**	**57,216**
Net book value at 31 December 2015	**51,293**	**2,736**	**2,694**	**896**	**57,619**	**4,464**	**62,083**

19. Property, plant and equipment and intangible assets (continued)

Bank 2015	Buildings	Computers	Furniture, equipment and vehicles	Property, plant and equipment and intangible assets not ready for use	Total property, plant and equipment	Intangible assets	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Cost							
At 31 December 2014	**77,102**	**11,660**	**15,294**	**1,440**	**105,496**	**24,224**	**129,720**
Additions	-	-	-	3,040	3,040	-	3,040
Transfer from assets not ready for use	-	71	62	(3,584)	(3,451)	3,451	-
Disposals and write-offs	-	(487)	(505)	-	(992)	(685)	(1,677)
Returned to service	-	67	44	-	111	-	111
At 31 December 2015	**77,102**	**11,311**	**14,895**	**896**	**104,204**	**26,990**	**131,194**
Accumulated depreciation							
At 31 December 2014	**23,473**	**7,098**	**11,634**	**-**	**42,205**	**20,982**	**63,187**
Transfer from/to	-	4	(4)	-	-	-	-
Depreciation for 2015	2,336	1,887	1,022	-	5,245	2,230	7,475
Disposals and write-offs	-	(481)	(495)	-	(976)	(686)	(1,662)
Returned to service	-	67	44	-	111	-	111
At 31 December 2015	**25,809**	**8,575**	**12,201**	**-**	**46,585**	**22,526**	**69,111**
Net book value at 31 December 2015	**51,293**	**2,736**	**2,694**	**896**	**57,619**	**4,464**	**62,083**
Net book value at 31 December 2014	**53,629**	**4,562**	**3,660**	**1,440**	**63,291**	**3,242**	**66,533**

20. Non-current assets held for sale

		Group		Bank
	2016	2015	2016	2015
	HRK '000	HRK '000	HRK '000	HRK '000
Non-current assets held for sale	47,639	49,469	47,639	49,469
Provisions for impairment losses	(30,409)	(27,754)	(30,409)	(27,754)
	17,230	**21,715**	**17,230**	**21,715**

In 2016 acquisitions of property took place in the total amount of HRK 0 thousand, with acquisition value and provisions of HRK 1,692 thousand, and relates to the acquisition value and provisions for buildings of debtor in the bankruptcy proceedings (in 2015 there were no acquisitions of non-current assets held for sale).
The amount of HRK 0 thousand relates to acquired moveable property, with acquisition value of and provisions of HRK 23 thousand. Fair value of acquired property at the end of the year amounted to HRK 1,635 thousand.

In 2016, a sale of non-current assets held for sale took place in the total amount of HRK 923 thousand, which relates to buildings (in 2015, sale of non-current assets held for sale took place in the amount of HRK 152 thousand, of which the land plot in the amount of HRK 4 thousand and buildings in the amount of HRK 148 thousand).

In 2016, this property was transferred to lease on the item Investments in property in the amount of HRK 1,872 thousand, which is presented under Other assets due to immaterial significance.

The fair value of non-current assets held for sale at the beginning of the reporting period stood at HRK 29,080 thousand and the end of the reporting period at HRK 25,741 thousand.

The movements in the provision for impairment losses on non-current assets held for sale may be summarized as follows:

		Group		Bank
	2016	2015	2016	2015
	HRK '000	HRK '000	HRK '000	HRK '000
Balance as of 1 January	27,754	15,809	27,754	15,809
Increase of provisions for impairment losses on non-current assets held for sale	2,275	12,571	2,275	12,571
Decrease of provisions for impairment losses on non-current assets held for sale	(228)	(59)	(228)	(59)
Written off impairment for non-current assets held for sale	(668)	(567)	(668)	(567)
Write-offs	(4)	-	(4)	-
Return on provisions at taking over	1,715	-	1,715	-
Reclassification of assets	(435)	-	(435)	
Balance as of 31 December	**30,409**	**27,754**	**30,409**	**27,754**

21. Other assets

	2016 HRK '000	Group 2015 HRK '000	2016 HRK '000	Bank 2015 HRK '000
Receivables from customers	2,687	2,078	2,687	2,078
Fees receivable	886	1,224	886	1,224
Prepaid expenses	1,023	1,022	1,023	1,022
Premium receivables	592	673	-	-
Receivables for reinsurance commissions	393	461	-	-
Receivables for risk assessment fees	247	115	-	-
Deferred tax assets	54	230	-	-
Other assets	7,781	3,516	5,841	3,456
	13,663	9,319	10,437	7,780
Provisions for impairment losses	(4,541)	(4,041)	(4,537)	(4,029)
	9,122	**5,278**	**5,900**	**3,751**

The movements in the provision for impairment losses on other assets may be summarized as follows:

	2016 HRK 000	Group 2015 HRK 000	2016 HRK 000	Bank 2015 HRK 000
Balance as at 1 January	4,041	3,793	4,029	3,779
Increase of provision for impairment losses on other assets	1,221	993	1,191	986
Release of provision for impairment losses on other assets	(675)	(709)	(659)	(700)
Collection of off-balance sheet receivable items	(18)	(36)	(1)	(16)
Provisions transferred from off-balance sheet	1	36	1	16
Acquisition of immovable property	(13)	-	(13)	-
Write-offs	(16)	(36)	(11)	(36)
Balance as of 31 December	**4,541**	**4,041**	**4,537**	**4,029**

22. Deposits

		Group		Bank
	2016	2015	2016	2015
	HRK '000	HRK '000	HRK '000	HRK '000
Bank deposits	1,324	26,921	1,324	26,921
Foreign currency regular accounts of companies	6	6	6	6
Foreign currency account of the Ministry of Finance of the Republic of Croatia	34,124	32,195	34,124	32,195
Foreign currency special purpose accounts of the companies	59,163	111,512	59,163	111,512
Deposits by state institutions	40,058	53,870	40,058	53,870
Other deposits	8,169	12,132	8,169	12,132
	142,844	**236,636**	**142,844**	**236,636**

The foreign currency account of the Ministry of Finance of the Republic of Croatia relates to the Export Insurance Guarantee Fund comprising of reinsurance premiums paid for export insurance operations of HRK 19,829 thousand (31 December 2015: HRK 18.252 thousand), grant funds provided by the Global Environment Facility (GEF) aimed at the Renewable Energy Resources Project of HRK 7,843 thousand (31 December 2015: HRK 7,650 thousand), the grant funds provided by the GEF aimed at the Programme of issuing bank guarantees for energy efficiency projects within the Energy Efficiency Project of HRK 6,452 thousand (31 December 2015: HRK 6,293 thousand), all managed by HBOR for and on behalf of the Republic of Croatia.

Demand deposits by State institutions relate to the Bank's operations carried out for and on behalf of the Ministry of Finance, the Ministry of the Economy, Entrepreneurship and Crafts, the Ministry of the Sea, Transport and Infrastructure, the Ministry of Agriculture, the Ministry of Regional Development and EU Funds, the company Vodovod i kanalizacija d.o.o., Split.

Foreign currency special purpose accounts of the companies relate to the inflow of funds and disposition of the advance payment funds paid to the company's account in relation to the issued guarantees of HBOR for the repayment of advance for export transactions. The funds of the advance are used exclusively for the specified purpose of implementation of an export contract, with the consent of HBOR.

HBOR does not pay interest on the above deposits.

23. Borrowings

	Group		Bank	
	2016	**2015**	**2016**	**2015**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**
Balance as of 1 January	11,453,796	11,572,516	11,453,796	11,572,516
New borrowings	3,730,867	769,062	3,730,867	769,062
Repayments	(1,730,849)	(848,277)	(1,730,849)	(848,277)
Net foreign exchange gains/(losses)	(75,757)	(39,505)	(75,757)	(39,505)
	13,378,057	11,453,796	13,378,057	11,453,796
Accrued interest	64,018	67,573	64,018	67,573
Deferred recognition of borrowing origination fees	(50,326)	(43,282)	(50,326)	(43,282)
Balance as of 31 December	**13,391,749**	**11,478,087**	**13,391,749**	**11,478,087**

Interest rates on borrowings ranged from 0.60% fixed per annum to variable interest rates on the International money market (EURIBOR) increased by 0.06 percentage points annually.

The Bank is subject to different financial covenants arising from contracts. During 2016 and as at 31 December 2016, the Bank was in compliance with all the required contractual financial covenants.

Average interest rates on borrowings are 1.06% (31 December 2015: 1.13%).

Average interest rates represent ratio of interest expenses on borrowings and average liabilities and equity.

24. Bonds payable

The book value of bonds includes interest.

Group and Bank	Effective interest rate %	Fair value 2016 HRK '000	Net book value 2016 HRK '000	Fair value 2015 HRK '000	Net book value 2015 HRK '000
Bonds EUR 150 million	4.836	-	-	235,410	229,023
Bonds EUR 250 million	5.076	1,915,899	1,888,837	1,959,077	1,906,811
Bonds EUR 150 million	6.37	1,270,695	1,121,261	1,263,814	1,129,466
Accrued interest		-	95,932	-	101,852
Deferred recognition of bond payable origination fees		-	(461)	-	(586)
		3,186,594	**3,105,569**	**3,458,301**	**3,366,566**

The fair value of bonds issued by HBOR is presented by using level 2 inputs corroborated by the market and observable at Bloomberg service on the basis of the mid-rate of Bloomberg Generic prices (BGN).

Average interest rates on bonds payable are 0.65% (31 December 2015: 0.72%).

Average interest rates represent ratio of interest expenses on bonds payable and average liabilities and equity.

According to the Agreement between HBOR and Deutsche Bank AG London (as lead manager), HBOR issued bonds on 11 July 2006 of EUR 150,000 thousand with a maturity period of 10 years and a fixed interest rate of 4.807% and amortized repayment in the period from 2012 to 2016. On 11 July 2016, the Bank made the final repayment under long-term securities issued with amortized repayment in the amount of HRK 235,274 thousand together with interest.

According to the Agreement between HBOR and UBS Investment Bank and Deutsche Bank AG London (as joint lead managers), HBOR issued bonds on 14 June 2007 of EUR 250,000 thousand (HRK 1,915,899 thousand as at 31 December 2016 and HRK 1,906,811 thousand as at 31 December 2015) with maturity period of 10 years and fixed interest rate of 5.0%. Interest is paid annually, in arrears. Bonds are listed in Luxembourg Stock Exchange quotation.

According to the Agreement between HBOR and Deutsche Bank AG London Branch and J.P. Morgan Securities PLC (as joint lead managers), HBOR issued bonds on 13 August 2013 of EUR 150,000 thousand (HRK 1,270,695 thousand as at 31 December 2016 and HRK 1,129,466 thousand as at 31 December 2015) with maturity period of 6 years and 9 months and fixed interest rate of 6.0%. Interest is paid annually, in arrears. Bonds were listed in Luxembourg Stock Exchange quotation on 25 August 2015 and were delisted from the Vienna Stock Exchange quotation on 29 September 2015.

25. Other liabilities

	Group		Bank	
	2016	2015	2016	2015
	HRK '000	HRK '000	HRK '000	HRK '000
Deferred recognition of interest income	425,347	528,866	425,347	528,866
Liabilities in respect of subsidized interest	95,422	118,576	95,422	118,576
Provisions for guarantees and commitments	75,103	62,785	75,103	62,785
Provisions for other liabilities	85,507	71,726	85,230	71,511
Accrued salaries	6,845	6,664	6,699	6,515
Liabilities to suppliers	3,015	1,040	2,938	925
Liabilities for prepaid receivables	1,920	3,995	1,920	3,995
Deferrable premium	3,358	2,189	-	-
Provisions for claims	3,960	4,028	-	-
Provisions for return premiums	452	407	-	-
Liabilities to re-insurers	1,172	1,602	-	-
Deferred tax liabilities	480	218	-	-
Other liabilities	5,371	4,843	4,115	3,867
	707,952	**806,939**	**696,774**	**797,040**

Liabilities in respect of subsidized interest represent advances taken in respect of interest subsidies on loans, which are provided for final customers at a lower interest rate in accordance with the following programmes implemented by HBOR for and on behalf of the Republic of Croatia (see Note 29). These liabilities include:

- HRK 95,327 thousand in respect of the Programme of Preferential Financing through HBOR's Loan Programmes (31 December 2015: HRK 117,229 thousand),

- HRK 0 thousand in respect of the Financing Model for the Reconstruction and Modernisation of the Fishing Fleet (31 December 2015: HRK 40 thousand),

- HRK 95 thousand (31 December 2015: HRK 1,307 thousand) in respect of the Loan Programme for the Financing of Youth Entrepreneurship.

25. Other liabilities (continued)

Deferred recognition of interest income of HRK 425,347 thousand (31 December 2015: HRK 528,866 thousand) consists of state subsidies for interest in respect of loans which are provided and drawn down by final borrowers at lower interest rates (see Note 2) but are not yet in repayment stage, amounting to HRK 26,463 thousand (31 December 2015: HRK 25,717 thousand), and in respect of those already in repayment stage amounting to HRK 398,884 thousand (31 December 2015: HRK 503,149 thousand) (see Note 2).

Provisions for guarantees and commitments represent the best estimation of the outflow for settlement of the outstanding liabilities at the Statement of Financial Position date and are determined in accordance with IAS 37 – Provisions, contingent liabilities and contingent assets.

Out of the total provisions for guarantees and commitments, HRK 28,811 thousand relates to financial institutions (31 December 2015: HRK 20,636 thousand), HRK 38,900 thousand relates to domestic companies (31 December 2015: HRK 29,387 thousand), HRK 170 thousand relates to state-owned companies (31 December 2015: HRK 1,737 thousand), HRK 7,164 thousand relates to the public sector (31 December 2015: HRK 10,430 thousand), HRK 58 thousand relates to others liabilities (31 December 2015: HRK 232 thousand) and HRK 0 thousand to foreign legal entities (31 December 2015: HRK 363 thousand).

Movements in the provision for guarantees, commitments and other liabilities may be summarized as follows:

		Group		Bank
	2016	2015	2016	2015
	HRK '000	HRK '000	HRK '000	HRK '000
Balance as at 1 January	62,785	42,551	62,785	42,551
Increase in provision for guarantees and commitments	51,006	58,665	51,006	58,665
Release in provision for guarantees and commitments	(39,084)	(37,856)	(39,084)	(37,856)
Net foreign exchange gains/(losses) on provision for impairment losses	396	(575)	396	(575)
Provision for guarantees and commitments	**75,103**	**62,785**	**75,103**	**62,785**
Balance as at 1 January	71,726	75,250	71,511	75,004
Increase in provision for other liabilities	53,102	14,835	52,756	14,619
Release in provision for other liabilities	(42,576)	(18,224)	(42,292)	(17,977)
Unrealized actuarial gain/(losses)	3,255	(135)	3,255	(135)
Provisions for other liabilities	**85,507**	**71,726**	**85,230**	**71,511**
Balance as at 31 December	**160,610**	**134,511**	**160,333**	**134,296**

25. Other liabilities (continued)

In 2016, provisions for other liabilities for the Group totalled HRK 85,507 thousand (31 December 2015: HRK 71,726 thousand) and for the Bank stood at HRK 85,230 thousand (31 December 2015: HRK 71,511 thousand). The total amount of provisions for other liabilities was comprised of HRK 35,820 thousand for court proceedings initiated against the Bank (31 December 2015: HRK 27,625 thousand), HRK 26,007 thousand for liabilities for the Group and for the Bank based on benefits defined in accordance with IAS 19 Employee Benefits (31 December 2015: HRK 21,858 thousand), and in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets HRK 23,680 thousand for provisions for other liabilities for the Group (31 December 2015: HRK 22,243 thousand) and HRK 23,403 thousand for the Bank (31 December 2015: HRK 22,028 thousand).

The latest actuarial assessment of present value of liabilities based on defined benefits as at 31 December 2016 was performed by a certified actuary. The model took into account mortality and discount rate, and the calculations for every employee considered age, gender, years of service, expected mortality and discount rate, i.e. the long-run sustainable yield rate on bonds.

The applied discount rate that represents the yield rate on bonds sustainable in the long run is 4.25% (In 2015: 5.5%).

Unrealised actuarial gains/(losses) arising from the calculation of provisions are stated within the framework of other comprehensive income so that net assets or liability may reflect the entire value of deficit or surplus planned.

26. Founder's capital and reserves

Under the HBOR Act, the prescribed founder's capital should amount to HRK 7,000,000 thousand, paid from the State Budget and from other sources as specified by separate laws.

The schedule of annual amounts of payment and the time schedule of payments out of the State Budget into the capital is not set in advance, but is determined by the Croatian Parliament as part of the process of adoption of the State Budget of the Republic of Croatia.

Within its Accounting policies, the Group has set out its objectives of capital management, category of capital managed by the Bank as well as measuring and assessing the policies for capital management. Capital management is described and presented in Note 34.

Founder's capital of the subsidiary Hrvatsko kreditno osiguranje d.d. amounts to HRK 37,500 thousand and is 100% owned by the Bank, and the founder's capital of the company Poslovni info servis d.o.o. amounts to HRK 300 thousand and is 100% owned by Hrvatsko kreditno osiguranje d.d.. The capital of both companies is subscribed and paid in full.

27. Guarantee fund

Group and Bank	**HRK '000**
Balance as of 1 January 2015	**12,545**
Net foreign exchange	(43)
Balance as of 31 December 2015	**12,502**
Net foreign exchange	(127)
Balance as of 31 December 2016	**12,375**

The Guarantee fund, of HRK 12,375 thousand and HRK 12,502 thousand as of 31 December 2016 and 2015 respectively, relates to funds of the guarantee fund from Deutsche Investitions- und Entwicklungsgesellschaft (DEG) in respect of a financial contribution (granted funds) for the account of the German Government, which are used for covering contingent losses on guarantees issued for loans granted under the Programme for financing business start-ups in Croatia. The funds of the Guarantee fund are unconditionally contributed and have no maturity. The funds of the Guarantee fund give the Government of the Federal Republic of Germany neither controlling rights nor a right to a share of the operating results of the Group.

28. Guarantees and commitments

In its regular activities, the Group contracts various commitments and contingent liabilities. The purpose of these instruments is to ensure that the funds are available to a customer when required.

These obligations contain credit risk and are therefore part of the overall risk of the Group although they are not recognised in the Statement of financial position.

Group and Bank

	2016	**2015**
	HRK '000	**HRK '000**
Guarantees issued in HRK	32,409	4,352
Guarantees issued in foreign currency	2,007,578	1,062,639
Undrawn loans	3,978,340	3,397,517
EIF – subscribed, not called up capital (Note 15)	48,370	48,864
Other irrevocable contingent liabilities	339	339
	6,067,036	4,513,711
Provisions for guarantees and commitments	(75,103)	(62,785)
	5,991,933	**4,450,926**

28. Guarantees and commitments (continued)

Guarantees

Issued guarantees and open letters of credit represent the liability to the Bank to make payments on behalf of customers if the customer is unable to honour its commitments towards third parties or in the event of a specific act, generally related to the export or import of goods and other purposes specified in the contracts with the customers. Guarantees and letters of credit bear the same credit risk as loans.

Bank guarantees are, to the extent of 82%, collateralized by the guarantees, deposits and bank guarantees or the liability was taken over by the Republic of Croatia.

Commitments upon undrawn loans

The Bank has an obligation to disburse funds for loans and revolving loans upon committed undrawn loans. The expiry date of disbursement or other termination clause is determined by the contract. Disbursements are exercised in several withdrawals, depending on the purpose of the loan, phase of the project or documentation needed for disbursement. Since commitments may expire without being drawn upon, the total contractual amounts do not necessarily represent future cash outflows.
Committed undrawn loans include less potential credit risk than loans, since most commitments depend upon meeting specific terms and conditions by the customers in order to use the funds. The Bank monitors the terms to maturity of loan commitments.

Other irrevocable contingent liabilities

Other irrevocable contingent liabilities relate to HBOR's obligation based on the Agreement concluded on 24 January 2014 with HBOR – Export Credit Insurance performing transactions for and on behalf of the Republic of Croatia. Pursuant to this Agreement, HBOR shall, in case of disposal of the real estate taken over and the recovery from debtors in a pre-bankruptcy settlement, provided that certain conditions have been fulfilled, pay the recovered funds to the Guarantee fund of the Export Credit Insurance.

29. Managed funds for and on behalf of third parties

The Group manages funds on behalf of and for the account of the Ministry of Finance, the Ministry of the Economy, Entrepreneurship and Crafts, the Ministry of the Sea, Transport and Infrastructure, the Ministry of Agriculture, the Ministry of Regional Development and EU Funds, the Ministry of Environment and Energy, the company Vodovod i kanalizacija d.o.o., Split and the Croatian Agency for SMEs, Innovation and Investment ("HAMAG-BICRO"), that are mainly used for various reconstruction and development programmes. These assets are separated from the Group's assets. The income and expense relating to these transactions are charged to the principal, and the Group does not have any other liabilities. The Group charges a fee for part of the services and part of the services are performed free of charge depending on the contract with the customer and taking into account that the stated amounts are insignificant for the Group.

Agency business funds per individual programmes amount to:

Group and Bank

Programme	2016 HRK '000	2015 HRK '000
Development and Reconstruction of Rural Housing	29,895	34,878
Employment of Former Soldiers	332,614	326,783
Emergency Reconstruction Project (loan IBRD 3760 - HR)	-	40
Municipal Environmental Infrastructure Investment Program – MEIP	853,298	843,298
Collection of receivables under HAMAG-BICRO guarantees	221	226
Insurance of export transactions	339,524	312,883
Programme of Preferential Financing through HBOR's Loan Programmes	95,327	117,229
Programme for Regional Development of the Republic of Croatia - loans	11,196	13,375
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of Agriculture - interest subsidy	-	40
Renewable Energy Resources Project	25,522	25,240
VIK – EKO account A – dedicated water charge	596,857	541,867
VIK – EKO account B – VAT	153,819	148,475
Programme of Issuing Bank Guarantees for Energy Efficiency Projects – IBRD	6,452	6,293
Financing the Establishment of Fishing Infrastructure – Ministry of Maritime Affairs, Transport and Infrastructure	46,665	46,665
Model of financing investment in the adjustment of fishing fleet and investment in fishing boats – Ministry of Agriculture	12,904	13,090
Micro-Loans with EU Support – commercial banks	30	-
Loan Programme for the Financing of Youth Entrepreneurship – Ministry of Entrepreneurship and Crafts - interest subsidy	95	1,307
Transactions related to investments in the Economic Co-operation Funds*	506,113	436,409
	3,010,522	**2,868,098**

*The fair value of net assets value of the Economic Co-operation Funds in 2016 is recognised on the basis of the latest available data and does not represent the final fair value, whereas, in 2015, the amount was recognised in accordance with the audited financial statements.

30. Related-party transactions

Related parties are companies that directly or indirectly, through one or more intermediaries, control, or are controlled by, the reporting company.

The majority of related-party transactions relate to the transactions with the Republic of Croatia, the 100% owner of the Bank and state-owned companies over which the Republic of Croatia has the controlling influence. All transactions stated were carried out under usual/regular conditions of the Bank.

As of 31 December 2016 and 31 December 2015, balances arising from transactions with related parties, including the Bank's key management personnel, include the following:

a) Related-party transactions

Group	Exposure	Liabilities	Income	Expense	Exposure	Liabilities	Income	Expense
	2016	2016	2016	2016	2015	2015	2015	2015
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Owner	3,193,565	153,374	91,685	6,643	2,388,181	183,488	56,669	428
Government funds, executive authorities and agencies	1,087,460	14,214	21,905	1,199	1,086,167	22,737	13,686	8,299
State-owned companies	1,193,668	2	55,269	7,511	1,513,557	7	45,104	2,242
Associates	6	-	858	-	9	-	706	90
Other intra-group transactions	-	-	-	71	-	-	-	71
Key management personnel	4,289	-	147	-	5,749	-	174	11
Total	**5,478,988**	**167,590**	**169,864**	**15,424**	**4,993,663**	**206,232**	**116,339**	**11,141**

Bank	Exposure	Liabilities	Income	Expense	Exposure	Liabilities	Income	Expense
	2016	2016	2016	2016	2015	2015	2015	2015
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Owner	3,193,565	153,374	91,685	6,643	2,388,181	183,488	56,669	428
Government funds, executive authorities and agencies	1,044,382	14,079	20,135	658	1,048,914	22,528	11,512	7,520
State-owned companies	1,193,271	-	55,251	7,443	1,513,155	4	45,085	2,174
Subsidiary companies	36,124	-	-	-	36,124	-	-	-
Associates	6	-	858	-	9	-	706	90
Key management personnel	4,000	-	137	-	5,476	-	165	11
Total	**5,471,348**	**167,453**	**168,066**	**14,744**	**4,991,859**	**206,020**	**114,137**	**10,223**

Exposures include loans to other customers, available-for-sale assets, assets held to maturity, other assets and off-balance sheet exposure relating to guarantees, letters of credit and commitments.

Liabilities include deposits and other liabilities.

30. Related-party transactions (continued)

a) Related-party transactions (continued)

Income includes interest income, fee income, other income and reversal of impairment losses and provisions.

Expense includes impairment losses and provisions and other expense.

b) Collateral received

		Group		Bank
	2016	**2015**	**2016**	**2015**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**
The Republic of Croatia	3,092,258	2,842,985	3,007,698	2,751,832
State agencies	603,215	646,430	603,215	646,430
Total	**3,695,473**	**3,489,415**	**3,610,913**	**3,398,262**

Collateral received relates to first-class collateral instruments received as security for HBOR's placements comprising the Republic of Croatia guarantees, HAMAG-BICRO guarantees, insurance policies of export transactions against political and/or commercial risks and statutory guarantees in cases when the Republic of Croatia or other state executive body guarantees the liabilities of certain borrowers pursuant to provisions of certain laws. HBOR issues reinsurance policies for and on behalf of the Republic of Croatia, i.e. covers a proportional part (quota reinsurance) of political and commercial risks of export loans and receivables arising from export of goods and services. The reinsurer covers all non-marketable (non-market) risks underwritten by the Insurer or Hrvatsko kreditno osiguranje d.d. in the percentage ranging from 30% to 90% of an insured amount.

c) Salaries of key management personnel

Salaries include compensation paid for regular work, annual vacation, national holidays, paid leave, sick leave, jubilee awards and payments under contractual agreements. In 2016, salaries for the Group amounted to HRK 7,746 thousand (31 December 2015: HRK 9,992 thousand), and for the Bank HRK 6,719 thousand (31 December 2015: HRK 8,600 thousand).

Remuneration for the work of the members of the Supervisory Board in 2016 amounted to HRK 320 thousand for the Group (31 December 2015: HRK 190 thousand) and for the Bank HRK 193 thousand (31 December 2015: HRK 136 thousand) and it relates to the HBOR Supervisory Board member eligible for remuneration and members of supervisory boards at associates and subsidiaries who were appointed by HBOR.

31. Risk management

31.1. Introduction

Based on the Act on the Croatian Bank for Reconstruction and Development, the Bank is obliged to mitigate business risks directed by the principles of banking operations.

In the process of risk management, the Bank identifies, estimates, measures, monitors, contains and controls the risks to which it is or might be exposed in the course of business and reports about them to the bodies in charge. By the mentioned procedures, appropriate internal documents and adequate organisational structure, a comprehensive and complete risk management system is provided.

The most significant risks the Bank is exposed to: credit risk, liquidity risk, interest rate risk and foreign exchange risk, operational risk and outsourcing risk. These risks are managed daily in accordance with the policies, procedures, methodologies and limit systems as well as decisions/conclusions of the Supervisory Board, the Management Board and the risk management committees.

The Bank implements the sensitivity analyses and scenario analyses, provided that one or several risk factors are changed in regular or stressful circumstances, and the systems of pro-active risk management are continuously developed for the purpose of reducing possible future risks.

Risk management structure

The Supervisory Board is responsible for monitoring the appropriateness and effectiveness of the risk management process in the Bank. The Supervisory Board adopts HBOR's Risk Management Strategy that lays out the main principles and standards of risk management and defines the tendency towards risk-taking.

The Management Board of the Bank is responsible for implementing the risk management strategy and establishing an effective and reliable risk management system. In order to accomplish its task, the Management Board delegated their risk management authority to four committees.

Risk management committees

- **Assets and Liabilities Management Committee (ALCO) –** manages liquidity risk, interest rate risk and currency risk within the framework of the Liquidity Risk Management Ordinance, the Currency Risk Management Procedures and the Interest Rate Risk Management Procedures, the Assets and Liabilities Management Procedures as well as other documents of the Bank that regulate this area.
- **Credit Risk Evaluation and Measurement Committee –** manages credit risk within the framework set through accepted Loan Policies, Credit Risk Management Procedures, methodologies, ordinances and other internal acts that cover issues related to credit risk.
- **HBOR Information System Management Committee –** manages the resources of the information system and adequately manages the risks that result from the use of information technology.
- **Business Change Management Committee –** manages business changes (co-ordination of procedures for the suggestion, approval, monitoring and implementation of business changes) in order to reduce risks associated with the implementation of business changes.

31. Risk management (continued)

31.1. Introduction (continued)

Risk Management Unit
The Risk Management unit is organised as a functionally and organizationally separate and independent organizational unit for the control of business risks, which is directly responsible to the Management Board. This organisational unit is responsible for defining, evaluating or measuring, monitoring and controlling the risks to which the Bank is exposed in the course of its business.

The Risk Management unit carries out its role by performing risk analyses and evaluations or measurements, developing risk management procedures and methodologies, supervising and monitoring of their application, recommending and controlling the accepted exposure limits, giving suggestions and recommendations for adequate risk management as well as reporting to the bodies in charge.

The risk management strategy is directed towards achieving and maintaining the system that would provide quality and efficiency in risk management complied with domestic and international banking practices and Croatian National Bank, European regulations and Basel Committee recommendations applicable to the Bank as a special financial institution.

Organizational Unit for Control and Audit
Control and audit is organized as a separate organizational unit, functionally and organizationally independent from the activities subject to its audit and other organizational units of HBOR. The Control and Audit unit is responsible to the Management Board, Supervisory Board and Audit committee. The Control and Audit unit verifies the application and efficiency of the procedures and methodologies for risk management. Their role is achieved through testing of the risk management system according to the principles of operational stability, including managing IT resources and other associated technologies.

Organisational unit State Aid and Compliance Department
The State Aid and Compliance Department is in charge of the activities covered by the function responsible for monitoring compliance and harmonisation of HBOR's operations with the state aid rules.

The compliance monitoring function has been established in the Legal and General Affairs and Compliance Division as an independent and permanent function.

The compliance monitoring function is in charge of monitoring and controlling the following risks: legal and regulatory risks (the risk of disobedience of the laws, legislation and professional practice in effect), sanction risk (the risk of court, administrative or disciplinary sanctions and/or measures resulting from breaches of law, legislation, rules, standards and/or contractual obligations) and reputational risk.

Risk measurement and reporting systems
When assessing or measuring risk, the Bank takes into account historical data, business plans, current and expected market conditions and the specific characteristics of the Bank as a special financial institution. The results of risk assessments or measurements, analyses carried out and stress test are presented at the meetings of the Risk Management Committee, the Management Board and the Supervisory Board. For the purpose of risk monitoring and control, systems of limits are introduced for the management of credit risk, liquidity risk, interest rate risk and currency risk.

31. Risk management (continued)

31.1. Introduction (continued)

Risk measurement and reporting systems (continued)
Bodies in charge are systematically reported on the quality of the loan portfolio, high exposure and the highest permissible exposure, regulatory capital adequacy, collection of receivables and risk placements, changes in internal ratings of commercial banks and measures taken in case of rating deterioration, a number of liquidity status indicators and projections of open foreign currency positions, possible losses by significant currencies, interest rate gap, projections of average weighted rates for sources and placements of financial institutions, etc. The reporting dynamics and the risk measurement and assessment methodologies are prescribed by the Bank's internal documents.

31.2. Credit risk

The Bank controls credit risk by way of credit policies, ordinances and prescribed procedures for the management of this risk that determine internal control systems aiming to act preventively.

The credit risk management system is a crucial part of the Bank's business policy and it is an important strategic factor of business conduct, and therefore this area is regulated by a separate act - Credit risk management procedures, that are applied in all phases of the credit process (from the development of new bank products or from the credit application, monitoring of the client's business operations until the final loan repayment).

Credit risk management procedures are included in a comprehensive document comprised of methodologies aimed at the evaluation of business operations of different targeted groups of clients:

- Credit risk evaluation methodologies which encompass:
    - Credit rating evaluation methodology,
    - Methodology for the analysis of clients who keep their business records in accordance with the Income Tax Act,
    - Methodology for the analysis of business monitoring of clients who keep their business records in accordance with the Income Tax Act,
    - Methodology for the evaluation of the risk inherent to the branch of activity,
    - Methodology for the quarterly monitoring of clients' business,
    - Methodology for the evaluation and selection of leasing companies,
    - Collateral evaluation methodology,
- Credit scoring methodologies,
- Methodologies for evaluation and selection of banks,
- Methodologies for evaluation and selection of foreign banks.

In the case of direct clients, the Bank uses the Credit risk evaluation methodology (for loans over HRK 1,500 thousand) or the Credit scoring methodology (for loans below HRK 1,500 thousand) to determine creditworthiness. The Credit scoring methodology is used to determine creditworthiness of clients that belong to the "small portfolio" and contains five scoring models: placements up to HRK 300 thousand to companies, crafts businesses and farmers, placements to start-ups up to HRK 300 thousand placements from HRK 300 thousand to HRK 1,500 thousand to companies, placements to start-ups from HRK 300 thousand to HRK 1,500 thousand and placements from HRK 300 thousand to HRK 1,500 thousand for all other entrepreneurs.

31. Risk management (continued)

31.2. Credit risk

Pursuant to the HBOR Act, the Bank on-lends part of its placements via commercial banks or leasing companies. The assessment of commercial banks is based on the Methodology for the Evaluation and Selection of Banks and the Methodology for the Evaluation and Selection of Foreign Banks, whereas the assessment of leasing companies is based on the Methodologies for the Evaluation and Selection of Leasing Companies.

The Bank controls related party risk on the occasion of direct credit approval and for the duration of a business relationship when it is requested from the clients to state their related parties. The information thereby gathered is verified and the type and nature of intra-relationship is determined as well as the existence of a group of related parties and the occurrence of the influence of the improvement or worsening of economic and financial conditions of one related party to the economic or financial position of the related party.

The Bank, as a developmental financial institution, supports growth and development of the Croatian economy through investment. For this reason, the clients mainly approach the Bank with applications for credit financing of investment projects. In order to minimize risk and objectively estimate economic sustainability of the project as well as a return on investment, the Bank is constantly improving existing organizational and technical solutions, reports and internal acts and proposes new organization regulations and implementation instructions.

By continuous monitoring and evaluation of the clients' businesses, the Bank makes an effort to identify difficulties in their operation on a timely basis. For clients with difficulties, the Bank tries to find appropriate ways to collect receivables by considering the possibilities of alternative repayment terms with a view to continue the production process and employment increase. Special emphasis is placed on identifying and monitoring reasons for bad debts, and procedures for prevention are built in operational procedures with a view to decreasing the share of high risk placements of the Bank.

Also, large exposure limits as well as highest amount of credit risk exposure toward single client and his related parties were determined.

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and maximum credit risk exposure

The table below shows the highest gross credit risk exposures existing in the Statement of Financial Position and in Guarantees and commitments as of the reporting date, before the effect of mitigation through collateral received:

	Group		Bank	
	Gross highest exposure 2016	Gross highest exposure 2015	Gross highest exposure 2016	Gross highest exposure 2015
	HRK '000	HRK '000	HRK '000	HRK '000
Assets				
Cash on hand and due from banks	491,243	482,939	490,692	482,697
Deposits with other banks	23,872	359,397	23,872	356,351
Loans to financial institutions	11,889,111	12,522,652	11,889,111	12,522,652
Loans to other customers	11,511,194	9,223,069	11,511,194	9,223,069
Financial assets at fair value through profit or loss	286	3,707	-	-
Assets available for sale	3,353,086	2,870,315	3,306,628	2,832,323
Assets held to maturity	1,422	1,451	-	-
Other assets	6,249	3,575	3,079	2,278
Total	**27,276,463**	**25,467,105**	**27,224,576**	**25,419,370**
Guarantees and commitments				
Guarantees issued in HRK	32,082	4,303	32,082	4,303
Issued guarantees in foreign currency	1,982,969	1,042,484	1,982,969	1,042,484
Undrawn loans	3,928,177	3,354,940	3,928,177	3,354,940
EIF – subscribed, not called up capital	-	48,864	-	48,864
Other irrevocable contingent liabilities	335	335	335	335
Total	**5,943,563**	**4,450,926**	**5,943,563**	**4,450,926**
Total credit risk exposure	**33,220,026**	**29,918,031**	**33,168,139**	**29,870,296**

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and maximum credit risk exposure (continued)

The Bank, with its developmental loan programmes, covers the entire Republic of Croatia with a special emphasis on special concern areas, hill or mountain areas and the islands. Through development of new loan programmes (products), the Bank takes into account concentration of credit risk with a view to evenly develop all areas of the Republic of Croatia.

Through financing of different sectors by stimulating production and development with the purpose of developing the Croatian economy, the Bank is creating a better base for repayment of loans and minimization of risk.

As of 31 December 2016, the highest credit exposure of the Group to one debtor equalled HRK 3,147,235 thousand (31 December 2015: HRK 2,764,572 thousand), and of the Bank HRK 3,147,235 thousand (31 December 2015: HRK 2,763,386 thousand) without considering the effect of mitigation through collateral received. The collateral policy is disclosed further in Note 31.2.

As a special financial institution, the Bank performs its development role by granting loans to final borrowers via commercial banks with which it has entered into co-operation agreements. Since the exposure towards some of the banks has reached the maximum permitted level, the Bank, in order to be able to continue performing its development role and make the loans accessible to as many final borrowers as possible, has an approval from the Supervisory Board for an increase in the exposure towards the banks and their associated entities that have, in accordance with HBOR's internal methodology, been assigned a high rating. The exposure level is maintained by using all instruments and techniques available for mitigating HBOR's exposure towards the banks.

This exposure increase approved by the Supervisory Board was used by the Bank for further operating activities carried out with two banks.

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and maximum credit risk exposure (continued)

Concentration of assets and guarantees and commitments, according to geographical segments, before the effect of mitigation through collateral received, is as follows:

Group 2016	Republic of Croatia	EU countries	Other countries	Total
	HRK '000	HRK '000	HRK '000	HRK '000
Assets				
Cash on hand and due from banks	188,322	301,354	1,567	491,243
Deposits with other banks	3,291	20,581	-	23,872
Loans to financial institutions	11,889,111	-	-	11,889,111
Loans to other customers	11,281,848	-	229,346	11,511,194
Financial assets at fair value through profit or loss	286	-	-	286
Assets available for sale	3,353,086	-	-	3,353,086
Assets held to maturity	1,422	-	-	1,422
Other assets	5,644	605	-	6,249
Total	**26,723,010**	**322,540**	**230,913**	**27,276,463**
Guarantees and commitments				
Guarantees issued in HRK	31,480	602	-	32,082
Issued guarantees in foreign currency	1,982,969	-	-	1,982,969
Undrawn loans	3,928,177	-	-	3,928,177
Other irrevocable contingent liabilities	335	-	-	335
Total	**5,942,961**	**602**	**-**	**5,943,563**
Total credit risk exposure	**32,665,971**	**323,142**	**230,913**	**33,220,026**

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and maximum credit risk exposure (continued)

Concentration of assets and guarantees and commitments, according to geographical segments, before the effect of mitigation through collateral received (continued):

Group 2015	Republic of Croatia	EU countries	Other countries	Total
	HRK '000	HRK '000	HRK '000	HRK '000
Assets				
Cash on hand and due from banks	108,473	301,999	72,467	482,939
Deposits with other banks	56,864	302,533	-	359,397
Loans to financial institutions	12,522,528	-	124	12,522,652
Loans to other customers	8,997,934	-	225,135	9,223,069
Financial assets at fair value through profit or loss	3,707	-	-	3,707
Assets available for sale	2,845,869	24,446	-	2,870,315
Assets held to maturity	1,451	-	-	1,451
Other assets	3,025	550	-	3,575
Total	**24,539,851**	**629,528**	**297,726**	**25,467,105**
Guarantees and commitments				
Guarantees issued in HRK	3,099	1,204	-	4,303
Issued guarantees in foreign currency	1,042,484	-	-	1,042,484
Undrawn loans	3,319,026	-	35,914	3,354,940
EIF – subscribed, not called up capital	-	48,864	-	48,864
Other irrevocable contingent liabilities	335	-	-	335
Total	**4,364,944**	**50,068**	**35,914**	**4,450,926**
Total credit risk exposure	**28,904,795**	**679,596**	**333,640**	**29,918,031**

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and maximum credit risk exposure (continued)

Concentration of assets and guarantees and commitments, according to geographical segments, before the effect of mitigation through collateral received (continued):

Bank 2016	Republic of Croatia	EU countries	Other countries	Total
	HRK '000	HRK '000	HRK '000	HRK '000
Assets				
Cash on hand and due from banks	187,771	301,354	1,567	490,692
Deposits with other banks	3,291	20,581	-	23,872
Loans to financial institutions	11,889,111	-	-	11,889,111
Loans to other customers	11,281,848	-	229,346	11,511,194
Assets available for sale	3,306,628	-	-	3,306,628
Other assets	2,844	235	-	3,079
Total	**26,671,493**	**322,170**	**230,913**	**27,224,576**
Guarantees and commitments				
Guarantees issued in HRK	31,480	602	-	32,082
Issued guarantees in foreign currency	1,982,969	-	-	1,982,969
Undrawn loans	3,928,177	-	-	3,928,177
Other irrevocable contingent liabilities	335	-	-	335
Total	**5,942,961**	**602**	**-**	**5,943,563**
Total credit risk exposure	**32,614,454**	**322,772**	**230,913**	**33,168,139**

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and maximum credit risk exposure (continued)

Concentration of assets and guarantees and commitments, according to geographical segments, before the effect of mitigation through collateral received (continued):

Bank 2015	Republic of Croatia	EU countries	Other countries	Total
	HRK '000	HRK '000	HRK '000	HRK '000
Assets				
Cash on hand and due from banks	108,231	301,999	72,467	482,697
Deposits with other banks	53,818	302,533	-	356,351
Loans to financial institutions	12,522,528	-	124	12,522,652
Loans to other customers	8,997,934	-	225,135	9,223,069
Assets available for sale	2,807,877	24,446	-	2,832,323
Other assets	2,221	57	-	2,278
Total	**24,492,609**	**629,035**	**297,726**	**25,419,370**
Guarantees and commitments				
Guarantees issued in HRK	3,099	1,204	-	4,303
Issued guarantees in foreign currency	1,042,484	-	-	1,042,484
Undrawn loans	3,319,026	-	35,914	3,354,940
EIF – subscribed, not called up capital	-	48,864	-	48,864
Other irrevocable contingent liabilities	335	-	-	335
Total	**4,364,944**	**50,068**	**35,914**	**4,450,926**
Total credit risk exposure	**28,857,553**	**679,103**	**333,640**	**29,870,296**

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and maximum credit risk exposure (continued)

Concentration of assets and guarantees and commitments, according to industry, before and after the effect of mitigation through collateral received, is as follows:

Group	Gross highest exposure 2016 HRK '000	Net highest exposure 2016 HRK '000	Gross highest exposure 2015 HRK '000	Net highest exposure 2015 HRK '000
Financial intermediation and insurance	15,359,154	-	15,448,725	-
Water and electric supply and other infrastructure	1,322,277	959,881	1,327,987	1,014,914
Tourism	3,630,150	363,739	2,615,100	188,306
Transport, warehousing and connections	1,714,718	836,069	1,589,312	202,870
Shipbuilding	2,257,050	572,383	1,213,286	349,937
Agriculture and fishery	515,711	68,982	602,769	120,446
Food industry	1,159,546	205,632	779,282	301,795
Construction industry	1,225,887	53,900	1,300,797	120,178
Other industry	527,352	138,850	462,418	128,268
Public administration	2,426,716	2,426,716	2,100,572	2,100,572
Education	47,020	40,956	29,101	22,928
Manufacture of basic metals and fabricated metal products, except machinery and equipment	407,254	62,818	241,181	49,443
Manufacture of chemicals and chemical products	255,576	16,761	47,936	20,360
Manufacture of other non-metallic mineral products	273,959	4,399	294,210	33,444
Pharmaceutical industry	572,470	809	602,278	1,904
Other	1,525,185	311,092	1,263,077	100,433
Total credit risk exposure	**33,220,026**	**6,062,987**	**29,918,031**	**4,755,798**

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and maximum credit risk exposure (continued)

Concentration of assets and guarantees and commitments, according to industry, before and after the effect of mitigation through collateral received, is as follows:

Bank	Gross highest exposure	Net highest exposure	Gross highest exposure	Net highest exposure
	2016 HRK '000	2016 HRK '000	2015 HRK '000	2015 HRK '000
Financial intermediation and insurance	15,352,325	-	15,440,062	-
Water and electric supply and other infrastructure	1,322,277	959,881	1,327,987	1,014,914
Tourism	3,630,150	363,739	2,615,100	188,306
Transport, warehousing and connections	1,714,322	835,673	1,588,911	202,469
Shipbuilding	2,257,050	572,383	1,213,286	349,937
Agriculture and fishery	515,702	68,974	602,769	120,446
Food industry	1,159,491	205,577	779,209	301,722
Construction industry	1,225,813	53,826	1,300,685	120,066
Other industry	527,143	138,641	462,180	128,030
Public administration	2,383,635	2,383,635	2,063,320	2,063,320
Education	47,020	40,956	29,101	22,928
Manufacture of basic metals and fabricated metal products, except machinery and equipment	407,200	62,764	241,164	49,426
Manufacture of chemicals and chemical products	255,537	16,721	47,908	20,332
Manufacture of other non-metallic mineral products	273,896	4,336	294,166	33,399
Pharmaceutical industry	571,663	-	601,449	1,075
Other	1,524,915	310,823	1,262,999	100,356
Total credit risk exposure	**33,168,139**	**6,017,929**	**29,870,296**	**4,716,726**

Concentration of assets and guarantees and commitments according to industry for both years has been compiled in accordance with the National Classification of Activities 2007 („NKD 2007").

In the preparation of the Note, a combined approach is applied, which takes into consideration business activities of a debtor, retains the names of activities different from those in the National Classification of Activities and unites similar business activities.

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and maximum credit risk exposure (continued)

The fair value of collateral for the Group in 2016 amounted to HRK 27,157,039 thousand (31 December 2015: HRK 25,162,233 thousand) and for the Bank HRK 27,150,210 thousand (31 December 2015: HRK 25,153,570 thousand).

In the total net highest exposure of the Bank in 2016, the credit risk of HRK 4,136,125 thousand (31 December 2015: HRK 3,394,974 thousand) is not covered with ordinary collateral, but it relates to receivables and received funds from the Republic of Croatia of HRK 867,410 thousand (31 December 2015: HRK 408,096 thousand), from local (regional) authorities of HRK 395,629 thousand (31 December 2015: HRK 348,089 thousand), state-owned companies for whose commitments the Republic of Croatia guarantees jointly and unconditionally of HRK 242,735 thousand (31 December 2015: HRK 248,878 thousand), government funds of HRK 1,250 thousand (31 December 2015: HRK 2,860 thousand), government bonds and Treasury bills of the Ministry of Finance of HRK 2,399,224 thousand (31 December 2015: HRK 2,077,357 thousand). In addition, an amount of HRK 229,877 thousand (31 December 2015: HRK 309,694 thousand) relates to receivables from a majority state-owned company (controlling influence).

Part of the placements with net exposure relates to placements provisionally and partially covered with collateral and the further increase in exposure has been stopped pending the submission of the full collateral necessary for compliance with the requested collateral coverage ratio.

Financial intermediation includes mainly commercial banks; the operation and collateral quality for placements with commercial banks is described further in Note 31.2 under Collateral for placements with commercial banks.

Credit risk exposure by internal credit rating:

Internal credit rating	Historical default rate (%) 2016	Historical default rate (%) 2015	Group 2016	Group 2015	Bank 2016	Bank 2015
			HRK '000	HRK '000	HRK '000	HRK '000
A	1.52%	1.66%	31,671,378	28,279,955	31,619,491	28,232,220
B	34.08%	34.91%	1,548,648	1,638,076	1,548,648	1,638,076
C	95.56%	94.05%	-	-	-	-
	Total		**33,220,026**	**29,918,031**	**33,168,139**	**29,870,296**

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and maximum credit risk exposure (continued)
Credit risk assessment internal methodology

For the analysis and evaluation of various target groups of clients, the Bank has prescribed internal methodologies. They represent the guidelines for decisions on approval of loans, guarantees and letters of credit and one of criteria for determination of the placement risk category.

Methodology for evaluation of credit ratings is applied when determining the creditworthiness of clients in the case of direct placements over HRK 1,500 thousand. It comprises three main evaluation areas: client evaluation and project/investment evaluation and evaluation of client and project/investment. All evaluation areas consist of three basic parts: financial, non-financial analysis and correction of evaluation based on currency-induced credit risk (VIKR) for placements in foreign currency or in kuna indexed to foreign currency.

Methodologies of credit scoring are used during credit risk evaluation for all direct placements below HRK 1,500 thousand where the Bank is exposed to credit risk. The quality and value of collateral for the placement are a part of the credit scoring procedure.

Methodologies for the analysis of clients who keep their business records in accordance with the Income Tax Act (commitments) are applied on the occasion of determining the creditworthiness of clients in the case of direct lending for placements above HRK 1,500 thousand together with the evaluation of the project based on the Methodology for the evaluation of credit ratings (project evaluation).

The Methodology for evaluation and selection of banks and the Methodology for evaluation and selection of foreign banks are used for evaluation of domestic and foreign banks. The Methodology for the evaluation and selection of leasing companies is used for evaluation of leasing companies. The methodologies include the estimation of the financial risk (quantitative evaluation), the estimation of business risks for banks/leasing companies analysed (qualitative evaluation) and the estimation of reputation risk.

The result of application of the above methodologies is the rating of the client.

Impairment loss and provisions

The Bank forms provisions for identified losses in accordance with International Financial Reporting Standards and internal rules. Forming provisions is under the competence of the Credit risk evaluation and measurement committee.

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and maximum credit risk exposure (continued)

Provisioning on an individual basis

Provisioning on an individual basis represents impairment of partly recoverable and irrecoverable investments (risk groups "B" and "C"). Allocation of placements on an individual basis into risk groups is performed by the following criteria:

- creditworthiness,
- debtors' regularity of repayment upon maturity, and
- quality of placement collateral.

Placements that represent the portfolio of small loans are classified by the criteria of regular repayment upon maturity. The Bank does not determine the present value of discounted cash flows for partially recoverable placements where the expected inflow is expected within one year of the financial statements date.

Provisioning on a collective basis

Provisions on a collective basis are formed for fully recoverable placements or placements and commitments allocated in risk group "A". Allocation of debtors within the risk group is performed according to industry risk factor, geographical affiliation, type and the debtor's foreign currency alignment.

Regardless of other classification criteria, investments which are at least 80% covered by first class collateral are allocated in risk group "A".

The Management Board of HBOR believes that the policies and procedures of forming provisions are adequate and that they ensure sufficient provisions for losses.

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial assets

Credit risk analysis, before and after the effect of mitigation through collateral received according to the type of financial assets on positions of assets and guarantees and commitments by internal credit rating, is as follows:

Group 2016	Gross exposure of portfolio of risk group A	Gross exposure of portfolio of risk group B	Gross exposure of portfolio of risk group C	Gross exposure of total portfolio	Net exposure of portfolio of risk group A	Net exposure of portfolio of risk group B	Net exposure of portfolio of risk group C	Net exposure of total portfolio
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Assets								
Cash on hand and due from banks	491,243	-	-	491,243	-	-	-	-
Deposits with other banks	23,872	-	-	23,872	-	-	-	-
Loans to financial institutions	11,472,130	416,981	-	11,889,111	-	-	-	-
Loans to other customers	10,415,684	1,095,510	-	11,511,194	2,484,106	34,930	-	2,519,036
Financial assets at fair value through profit or loss	286	-	-	286	-	-	-	-
Assets available for sale	3,353,086	-	-	3,353,086	2,442,549	-	-	2,442,549
Assets held to maturity	1,422	-	-	1,422	1,422	-	-	1,422
Other assets	5,853	396	-	6,249	3,270	396	-	3,666
Total	**25,763,576**	**1,512,887**	**-**	**27,276,463**	**4,931,347**	**35,326**	**-**	**4,966,673**
Guarantees and commitments								
Guarantees issued in HRK	32,082	-	-	32,082	-	-	-	-
Issued guarantees in foreign currency	1,964,149	18,820	-	1,982,969	437,160	-	-	437,160
Undrawn loans	3,911,236	16,941	-	3,928,177	658,819	-	-	658,819
Other irrevocable contingent liabilities	335	-	-	335	335	-	-	335
Total	**5,907,802**	**35,761**	**-**	**5,943,563**	**1,096,314**	**-**	**-**	**1,096,314**
Total credit risk exposure	**31,671,378**	**1,548,648**	**-**	**33,220,026**	**6,027,661**	**35,326**	**-**	**6,062,987**

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial assets (continued)

Credit risk analysis, before and after the effect of mitigation through collateral received according to the type of financial assets on positions of assets and guarantees and commitments by internal credit rating, is as follows (continued):

Group 2015	Gross exposure of portfolio of risk group A	Gross exposure of portfolio of risk group B	Gross exposure of portfolio of risk group C	Gross exposure of total portfolio	Net exposure of portfolio of risk group A	Net exposure of portfolio of risk group B	Net exposure of portfolio of risk group C	Net exposure of total portfolio
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Assets								
Cash on hand and due from banks	482,939	-	-	482,939	-	-	-	-
Deposits with other banks	359,397	-	-	359,397	-	-	-	-
Loans to financial institutions	12,020,367	502,285	-	12,522,652	-	-	-	-
Loans to other customers	8,128,497	1,094,572	-	9,223,069	1,835,366	21,359	-	1,856,725
Financial assets at fair value through profit or loss	3,707	-	-	3,707	-	-	-	-
Assets available for sale	2,870,315	-	-	2,870,315	2,115,754	-	-	2,115,754
Assets held to maturity	1,451	-	-	1,451	1,451	-	-	1,451
Other assets	3,528	47	-	3,575	2,957	47	-	3,004
Total	**23,870,201**	**1,596,904**	**-**	**25,467,105**	**3,955,528**	**21,406**	**-**	**3,976,934**
Guarantees and commitments								
Guarantees issued in HRK	4,303	-	-	4,303	1,797	-	-	1,797
Issued guarantees in foreign currency	1,002,815	39,669	-	1,042,484	366,105	-	-	366,105
Undrawn loans	3,353,437	1,503	-	3,354,940	410,627	-	-	410,627
EIF – subscribed, not called up capital	48,864	-	-	48,864	-	-	-	-
Other irrevocable contingent liabilities	335	-	-	335	335	-	-	335
Total	**4,409,754**	**41,172**	**-**	**4,450,926**	**778,864**	**-**	**-**	**778,864**
Total credit risk exposure	**28,279,955**	**1,638,076**	**-**	**29,918,031**	**4,734,392**	**21,406**	**-**	**4,755,798**

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial assets (continued)

Credit risk analysis, before and after the effect of mitigation through collateral received according to the type of financial assets on positions of assets and guarantees and commitments by internal credit rating, is as follows (continued):

Bank 2016	Gross exposure of portfolio of risk group A	Gross exposure of portfolio of risk group B	Gross exposure of portfolio of risk group C	Gross exposure of total portfolio	Net exposure of portfolio of risk group A	Net exposure of portfolio of risk group B	Net exposure of portfolio of risk group C	Net exposure of total portfolio
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Assets								
Cash on hand and due from banks	490,692	-	-	490,692	-	-	-	-
Deposits with other banks	23,872	-	-	23,872	-	-	-	-
Loans to financial institutions	11,472,130	416,981	-	11,889,111	-	-	-	-
Loans to other customers	10,415,684	1,095,510	-	11,511,194	2,484,106	34,930	-	2,519,036
Assets available for sale	3,306,628	-	-	3,306,628	2,399,825	-	-	2,399,825
Other assets	2,683	396	-	3,079	2,358	396	-	2,754
Total	**25,711,689**	**1,512,887**	**-**	**27,224,576**	**4,886,289**	**35,326**	**-**	**4,921,615**
Guarantees and commitments								
Guarantees issued in HRK	32,082	-	-	32,082	-	-	-	-
Issued guarantees in foreign currency	1,964,149	18,820	-	1,982,969	437,160	-	-	437,160
Undrawn loans	3,911,236	16,941	-	3,928,177	658,819	-	-	658,819
Other irrevocable contingent liabilities	335	-	-	335	335	-	-	335
Total	**5,907,802**	**35,761**	**-**	**5,943,563**	**1,096,314**	**-**	**-**	**1,096,314**
Total credit risk exposure	**31,619,491**	**1,548,648**	**-**	**33,168,139**	**5,982,603**	**35,326**	**-**	**6,017,929**

In the total net highest exposure of the Group and the Bank, the amount of loans to other customers of HRK 1,498,400 thousand is not covered by ordinary collateral, but it relates to receivables and received funds from the Republic of Croatia of HRK 628,961 thousand, local (regional) authorities of HRK 395,629 thousand, public companies for whose liabilities the Republic of Croatia guarantees jointly and unconditionally of HRK 242,735 thousand and the government funds of HRK 1,198 thousand. An additional amount of HRK 229,877 thousand relates to receivables from majority state-owned companies (controlling influence).

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial assets (continued)

The amount of assets available for sale and held to maturity is not covered by ordinary collateral but it relates to government bonds and treasury bills of the Ministry of Finance of HRK 2,399,224 thousand for the Group and HRK 2,442,203 thousand for the Bank.

Other assets of HRK 922 thousand are not covered by ordinary collateral, but relate to receivables from the Republic of Croatia and the government funds.

The amount of HRK 237,245 thousand relates to a guarantee issued in foreign currency, for which the liability was assumed by the Republic of Croatia. The guarantee was removed from business records of HBOR after the reporting period date, i.e. on 13 February 2017, due to the cessation of payment obligation resulting from arbitration decision.

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial asset (continued)

Credit risk analysis, before and after the effect of mitigation through collateral received according to the type of financial assets on positions of assets and guarantees and commitments by internal credit rating, is as follows (continued):

Bank 2015	Gross exposure of portfolio of risk group A	Gross exposure of portfolio of risk group B	Gross exposure of portfolio of risk group C	Gross exposure of total portfolio	Net exposure of portfolio of risk group A	Net exposure of portfolio of risk group B	Net exposure of portfolio of risk group C	Net exposure of total portfolio
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Assets								
Cash on hand and due from banks	482,697	-	-	482,697	-	-	-	-
Deposits with other banks	356,351	-	-	356,351	-	-	-	-
Loans to financial institutions	12,020,367	502,285	-	12,522,652	-	-	-	-
Loans to other customers	8,128,497	1,094,572	-	9,223,069	1,835,366	21,359	-	1,856,725
Assets available for sale	2,832,323	-	-	2,832,323	2,078,937	-	-	2,078,937
Other assets	2,231	47	-	2,278	2,153	47	-	2,200
Total	**23,822,466**	**1,596,904**	**-**	**25,419,370**	**3,916,456**	**21,406**	**-**	**3,937,862**
Guarantees and commitments								
Guarantees issued in HRK	4,303	-	-	4,303	1,797	-	-	1,797
Issued guarantees in foreign currency	1,002,815	39,669	-	1,042,484	366,105	-	-	366,105
Undrawn loans	3,353,437	1,503	-	3,354,940	410,627	-	-	410,627
EIF – subscribed, not called up capital	48,864	-	-	48,864	-	-	-	-
Other irrevocable contingent liabilities	335	-	-	335	335	-	-	335
Total	**4,409,754**	**41,172**	**-**	**4,450,926**	**778,864**	**-**	**-**	**778,864**
Total credit risk exposure	**28,232,220**	**1,638,076**	**-**	**29,870,296**	**4,695,320**	**21,406**	**-**	**4,716,726**

In the total net highest exposure of the Group and the Bank, the amount of loans to other customers of HRK 1,084,770 thousand is not covered by ordinary collateral, but it relates to receivables and received funds from the Republic of Croatia of HRK 175,285 thousand, local (regional) authorities of HRK 348,089 thousand, public companies for whose liabilities the Republic of Croatia guarantees jointly and unconditionally of HRK 248,878 thousand and the government funds of HRK 2,824 thousand. An additional amount of HRK 309,694 thousand relates to receivables from majority state-owned companies (controlling influence).

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial asset (continued)

The amount of assets available for sale and held to maturity is not covered by ordinary collateral but it relates to government bonds and treasury bills of the Ministry of Finance of HRK 2,114,454 thousand for the Group and HRK 2,077,357 thousand for the Bank.

Other assets of HRK 1,117 thousand are not covered by ordinary collateral, but relate to receivables from the Republic of Croatia and the government funds.

The amount of HRK 231,396 thousand relates to a guarantee issued in foreign currency, for which the liability was assumed by the Republic of Croatia.

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial asset (continued)

Credit risk quality according to the gross exposure of the type of financial assets on positions of assets and guarantees and commitments by risk category:

Group 2016	Gross exposure neither past due nor impaired	Gross exposure past due not impaired	Gross exposure individually impaired	Total
	HRK '000	HRK '000	HRK '000	HRK '000
Assets				
Cash on hand and due from banks	491,243	-	-	491,243
Deposits with other banks	23,872	-	-	23,872
Loans to financial institutions	11,259,676	212,454	416,981	11,889,111
Loans to other customers	10,249,918	165,766	1,095,510	11,511,194
Financial assets at fair value through profit or loss	286	-	-	286
Assets available for sale	3,353,086	-	-	3,353,086
Assets held to maturity	1,422	-	-	1,422
Other assets	4,528	1,325	396	6,249
Total	**25,384,031**	**379,545**	**1,512,887**	**27,276,463**
Guarantees and commitments				
Guarantees issued in HRK	32,082	-	-	32,082
Issued guarantees in foreign currency	1,964,149	-	18,820	1,982,969
Undrawn loans	3,911,236	-	16,941	3,928,177
Other irrevocable contingent liabilities	335	-	-	335
Total	**5,907,802**	**-**	**35,761**	**5,943,563**
Total credit risk exposure	**31,291,833**	**379,545**	**1,548,648**	**33,220,026**

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial asset (continued)

Credit risk quality according to the gross exposure of the type of financial assets on positions of assets and guarantees and commitments by risk category (continued):

Group 2015	Gross exposure neither past due nor impaired	Gross exposure past due not impaired	Gross exposure individually impaired	Total
	HRK '000	HRK '000	HRK '000	HRK '000
Assets				
Cash on hand and due from banks	482,939	-	-	482,939
Deposits with other banks	359,397	-	-	359,397
Loans to financial institutions	11,958,892	61,475	502,285	12,522,652
Loans to other customers	7,875,356	253,141	1,094,572	9,223,069
Financial assets at fair value through profit or loss	3,707	-	-	3,707
Assets available for sale	2,870,315	-	-	2,870,315
Assets held to maturity	1,451	-	-	1,451
Other assets	2,529	999	47	3,575
Total	**23,554,586**	**315,615**	**1,596,904**	**25,467,105**
Guarantees and commitments				
Guarantees issued in HRK	4,303	-	-	4,303
Issued guarantees in foreign currency	1,002,815	-	39,669	1,042,484
Undrawn loans	3,353,437	-	1,503	3,354,940
EIF – subscribed, not called up capital	48,864	-	-	48,864
Other irrevocable contingent liabilities	335	-	-	335
Total	**4,409,754**	**-**	**41,172**	**4,450,926**
Total credit risk exposure	**27,964,340**	**315,615**	**1,638,076**	**29,918,031**

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial asset (continued)

Credit risk quality according to the gross exposure of the type of financial assets on positions of assets and guarantees and commitments by risk category (continued):

Bank 2016	Gross exposure neither past due nor impaired	Gross exposure past due not impaired	Gross exposure individually impaired	Total
	HRK '000	HRK '000	HRK '000	HRK '000
Assets				
Cash on hand and due from banks	490,692	-	-	490,692
Deposits with other banks	23,872	-	-	23,872
Loans to financial institutions	11,259,676	212,454	416,981	11,889,111
Loans to other customers	10,249,918	165,766	1,095,510	11,511,194
Assets available for sale	3,306,628	-	-	3,306,628
Other assets	1,666	1,017	396	3,079
Total	**25,332,452**	**379,237**	**1,512,887**	**27,224,576**
Guarantees and commitments				
Guarantees issued in HRK	32,082	-	-	32,082
Issued guarantees in foreign currency	1,964,149	-	18,820	1,982,969
Undrawn loans	3,911,236	-	16,941	3,928,177
Other irrevocable contingent liabilities	335	-	-	335
Total	**5,907,802**	**-**	**35,761**	**5,943,563**
Total credit risk exposure	**31,240,254**	**379,237**	**1,548,648**	**33,168,139**

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial asset (continued)

Credit risk quality due to the gross exposure of the type of financial assets on positions of assets and guarantees and commitments by risk category (continued):

Bank 2015	Gross exposure neither past due nor impaired	Gross exposure past due not impaired	Gross exposure individually impaired	Total
	HRK '000	HRK '000	HRK '000	HRK '000
Assets				
Cash on hand and due from banks	482,697	-	-	482,697
Deposits with other banks	356,351	-	-	356,351
Loans to financial institutions	11,958,892	61,475	502,285	12,522,652
Loans to other customers	7,875,356	253,141	1,094,572	9,223,069
Assets available for sale	2,832,323	-	-	2,832,323
Other assets	1,633	598	47	2,278
Total	**23,507,252**	**315,214**	**1,596,904**	**25,419,370**
Guarantees and commitments				
Guarantees issued in HRK	4,303	-	-	4,303
Issued guarantees in foreign currency	1,002,815	-	39,669	1,042,484
Undrawn loans	3,353,437	-	1,503	3,354,940
EIF – subscribed, not called up capital	48,864	-	-	48,864
Other irrevocable contingent liabilities	335	-	-	335
Total	**4,409,754**	**-**	**41,172**	**4,450,926**
Total credit risk exposure	**27,917,006**	**315,214**	**1,638,076**	**29,870,296**

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial asset (continued)

Aging analysis of past due but not impaired loans per class of financial asset:

Group 2016	Up to 15 days	16 to 30 days	31 to 60 days	61 to 90 days	Over 90 days	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Assets						
Loans to financial institutions	200,364	552	4,000	17	7,521	212,454
Loans to other customers	109,035	36	8,072	803	47,820	165,766
Other assets	936	200	125	38	26	1,325
Total	**310,335**	**788**	**12,197**	**858**	**55,367**	**379,545**

Group 2015	Up to 15 days	16 to 30 days	31 to 60 days	61 to 90 days	Over 90 days	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Assets						
Loans to financial institutions	5,733	4,823	8,588	33,853	8,478	61,475
Loans to other customers	118,913	15,466	11,209	8,959	98,594	253,141
Other assets	272	169	168	377	13	999
Total	**124,918**	**20,458**	**19,965**	**43,189**	**107,085**	**315,615**

Bank 2016	Up to 15 days	16 to 30 days	31 to 60 days	61 to 90 days	Over 90 days	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Assets						
Loans to financial institutions	200,364	552	4,000	17	7,521	212,454
Loans to other customers	109,035	36	8,072	803	47,820	165,766
Other assets	862	73	38	18	26	1,017
Total	**310,261**	**661**	**12,110**	**838**	**55,367**	**379,237**

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial asset (continued)

Aging analysis of past due but not impaired loans per class of financial asset (continued):

Bank 2015	Up to 15 days	16 to 30 days	31 to 60 days	61 to 90 days	Over 90 days	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Assets						
Loans to financial institutions	5,733	4,823	8,588	33,853	8,478	61,475
Loans to other customers	118,913	15,466	11,209	8,959	98,594	253,141
Other assets	124	11	85	365	13	598
Total	**124,770**	**20,300**	**19,882**	**43,177**	**107,085**	**315,214**

Since the amount of past due but not impaired receivables of the subsidiary company is immaterial, the following text contains the breakdown of changes in past due but not impaired loans of the parent company.

From total due and not impaired loans to financial institutions in 2016, an amount of HRK 11,448 thousand or 5% relates to not executed extensions of short-term revolving loans.

Due to the maturity falling on 31 December 2016 being a non-working day, an amount of HRK 193,524 thousand, i.e. 91% of due but not impaired loans to financial institutions, was collected on 2 January 2017 being the first following working day.

From total due and not impaired loans to other customers in 2016, an amount of HRK 109,035 thousand or 66% relates to delays of up to 15 days, of which the amount of HRK 10,430 thousand, i.e. 10%, was guaranteed by the Republic of Croatia.

From total due and not impaired loans to financial institutions in 2015, an amount of HRK 56,829 i.e. 92%, relates to not executed extensions of short-term revolving loans.

If the total amount of due and not impaired loans to financial institutions is reduced by the debt of financial institutions under the short-term revolving loans, the remaining debt equals HRK 4,646 thousand.

From total due and not impaired loans to other customers in 2015, an amount of HRK 118,913 thousand or 47% relates to delays of up to 15 days, of which the amount of HRK 9,306 thousand, i.e. less than 8%, was guaranteed by the Republic of Croatia.

31. Risk management (continued)

31.2. Credit risk (continued)

Collateral and other instruments

Collateral for the Bank's placements are:

1. obligatory (bills of exchange and promissory notes),
2. ordinary (property, ships, airplanes, bank guarantees, guarantees from the Republic of Croatia, guarantees from the local (regional) authorities, guarantees from HAMAG-BICRO (Croatian Agency for SMSs, Innovation and Investment), insurance policy against political and/or commercial risks), and
3. other collateral (movable property, bills of exchange or guarantees from other companies with solid creditworthiness, fiduciary or pledge of companies' equity instruments, repossession of cash receivables or assignment for collectible receivables, deposit repossession, restriction of transferability on insurance policy of assets and/or person, pledge on a trademark, etc.).

All Bank placements have to be secured with obligatory collateral. Low-exposure placements must be secured with one obligatory instrument of collateral at least.

Acceptable standard and other collateral are classified according to quality in five groups. The evaluation of collateral is based on quality, estimated based on marketability, documentation and possibility of supervision by the Bank as well as the possibility of enforced collection. Only the acceptable collateral is evaluated while the sixth group of collateral is unacceptable.

When deciding on loan approval, weak creditworthiness cannot be replaced by quality collateral, except when the security instruments are first class instruments: guarantees from the Republic of Croatia, guarantees of local/regional authorities (JLPS), guarantees from HAMAG-BICRO, insurance policy against political and/or commercial risks and when the Republic of Croatia, JLPS or other government bodies guarantee for clients implicitly (through legal acts).

Collateral for placements with commercial banks

For the purpose of mitigation of credit risk and reduction of business costs, and in compliance with the Act on the Croatian Bank for Reconstruction and Development, the Bank approves part of its placements with commercial banks/leasing companies. As collateral for placements approved to final customers through financial institutions, the Bank uses mandatory collateral from commercial banks/leasing companies. The commercial bank or the leasing company is obliged to deliver them based on the Mutual business cooperation agreement, but not for each individual placement to the final customer based on that Agreement. In the individual contracts for placements to the final customers, the use of obligatory collateral delivered with the Agreement on mutual business cooperation is contracted. As the commercial bank or the leasing company takes on the risk of default by the final customer, they are given the option to contract sufficient collateral with the final customer.

Where the loan is approved through a commercial bank, depending on the financial institution's internal rating, the Bank contracts a sub-mortgage. In this case, either the commercial bank transfers the ownership over the collateral, while the Bank takes a mortgage over the same collateral, or the commercial bank forms a mortgage on the collateral, while the Bank takes a sub-mortgage on the same collateral.

31. Risk management (continued)

31.2. Credit risk (continued)

Collateral and other instruments (continued)

Collateral for placements with commercial banks (continued)

By signing the Agreement on mutual business cooperation, a transfer of any claims the commercial bank may have towards the final customer is made to HBOR. Pursuant to the Agreement, the commercial bank authorises HBOR to unilaterally inform the bank in written form that, in the case of the commercial bank's insolvency or threat of liquidation, untimely repayments or default on the commitments agreed in the individual contract on interbank loan or actual (insolvent or regular) liquidation, the Bank assumes the receivable towards the final customer from the commercial bank, with the effect of assignment of receivables instead of contract fulfilment.

Additionally, based on the Agreement on mutual business cooperation and based on the said unilateral statement, the commercial bank authorises HBOR that HBOR may, without having to obtain any further consent or approval from the commercial bank, enter itself into all public registers, books or records as the creditor instead of the commercial bank under any security arrangements for assigned receivables as well as under any other proceedings.

From the moment of the assignment, the final customer is obliged to make all payments related to the assigned receivable directly to HBOR. Should the commercial bank receive any payments in the name of collection of receivables per particular placement, the bank is obliged to immediately transfer the funds to HBOR.

Collateral for direct placements

All direct placements are mainly secured with a transfer of ownership or with a mortgage over real estate and, if that is possible, the Bank obtains as security against credit risk a guarantee from HAMAG-BICRO, a guarantee from the local (regional) authority, a guarantee from the Republic of Croatia, etc.

The Bank has the right to verify the appraisal of the collateral value and such a confirmed appraisal is considered as the final collateral value.

Depending on the type of collateral, the credit programme, the general terms of security or the decision of an authorised body, the Bank has determined the necessary ratio of placements and collateral.

For real estate, the necessary ratio between the amount of placement and the appraised value of the real estate is 1:1.3 except for investments on islands, in areas of special concern and hill or mountain areas, where the ratio is 1:1.2. For movable property, the necessary ratio between the amount of placement and the appraised value of the property is 1:2.

The Bank continuously monitors the value of the collateral by verification/statistical evaluation. Monitoring of the value of mortgaged real estate is performed once a year for business real estate, and every three years for residential buildings. The Bank has formed a special organizational unit for:

- evaluation and verification of already appraised and offered collateral (real estate and movables),
- technical and technological analysis of investment projects, and
- financial supervision over the withdrawal of loan funds for the purpose of the construction of the investment project.

31. Risk management (continued)

31.2. Credit risk (continued)

Collateral and other instruments (continued)

Collateral for direct placements (continued)

In the event that it is not possible for the Bank to collect from regular operations, the Bank starts collection from the collateral at its disposal. This encompasses initiating collection from the obligatory collateral, then from first-class, unconditional collateral payable on first demand and then from the mortgage or fiduciary ownership of the real estate or movable property, including their repossession with a view to decreasing or fully settling the Bank's receivables. The Bank does not use repossessed assets for business purposes.

Collateral for placements under the risk-sharing models

In the case of risk-sharing models, collateral is created by commercial banks depending on the type of the model:

- in accordance with their own internal documents and good banking practices, and, consequently, HBOR's documents and collateral ratios prescribed in them do not apply,
- or collateral is created by commercial banks and HBOR for their respective shares in the loan in accordance with their own documents, decisions and/or procedures.

31. Risk management (continued)

31.3. Liquidity risk

Liquidity risk management includes liquidity risk assessment, measurement control, containment and reporting, the establishing of limits and the monitoring of limit utilisation, the determining of procedures, responsibilities and accountabilities for all organisational units that participate in the management of liquidity risk.

In order to manage liquidity risk, the Bank maintains the adequate level of liquidity reserve, continuously monitors current and planned liquidity, ensures HRK and foreign currency funds necessary for timely settlement of liabilities and for disbursements of approved loans and planned loan approvals.
The Bank's liquidity reserve is set in the amount of at least 10% of net assets.

Managing short term liquidity encompasses the monitoring and managing of daily liquidity, particularly on the basis of the limits established for investing in instruments aimed at the maintenance of liquidity reserve, the monitoring and managing of cash flow mismatch for the next 5 weeks and for 1-year period for the purpose of timely determining the activities targeted at the accomplishment of business plans and simultaneously maintaining the established liquidity reserve level.

By long term liquidity risk management, the Bank manages the mismatch between contracted and planned placements and their sources of funding in the period over one year, within the framework of which guidelines/resolutions/decisions on further activities are made by bodies in charge on the basis of long-term inflow and outflow projections as well as based on the relationship between the funding requirements of the Bank and the availability of funding sources.

Within the framework of stress tests, the Bank considers internal and external risk factors, and the results of such tests are reported to the Asset and Liability Management Committee and the Management Board.

Liquidity risk management is ensured by the established system of limits and a regular review of their adequacy, reporting to the competent authorities on the projected size of available resources and liquidity reserves in the short and long term, which also represent the basis for making conclusions by the Asset and Liability Management Committee/decisions by the Management Board about activities ensuring business continuity within the prescribed limits.

The Bank does not hold deposits of citizens and is therefore not exposed to significant daily fluctuations in liquidity.

31. Risk management (continued)

31.3. Liquidity risk (continued)

The table below provides an analysis of total assets and total liabilities and equity as of 31 December 2016 and 31 December 2015 placed into relevant maturity groupings based on the remaining period as at the Statement of Financial Position date related to the contractual maturity date, as follows:

Group 2016	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Total HRK '000
Assets						
Cash on hand and due from banks	491,246	-	-	-	-	491,246
Deposits with other banks	-	23,872	-	-	-	23,872
Loans to financial institutions*	684,891	441,872	1,774,961	3,131,823	5,855,564	11,889,111
Loans to other customers	1,423,234	385,784	948,959	1,850,611	6,902,606	11,511,194
Financial assets at fair value through profit or loss	286	-	-	-	-	286
Assets available for sale	3,375,864	14,074	96	-	-	3,390,034
Assets held to maturity	-	10	4	-	1,408	1,422
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	57,305	57,305
Non-current assets held for sale	-	-	27	11,450	5,753	17,230
Other assets	6,225	748	530	620	999	9,122
Total assets (1)	**5,981,746**	**866,360**	**2,724,577**	**4,994,504**	**12,823,635**	**27,390,822**
Liabilities						
Deposits	75,581	-	12,687	46,407	8,169	142,844
Borrowings	355,456	237,339	1,017,892	3,060,113	8,720,949	13,391,749
Bonds payable	-	95,932	1,888,837	-	1,120,800	3,105,569
Other liabilities	151,186	29,918	105,330	194,459	227,059	707,952
Total liabilities	**582,223**	**363,189**	**3,024,746**	**3,300,979**	**10,076,977**	**17,348,114**
Equity						
Founder's capital	-	-	-	-	6,959,632	6,959,632
Retained earnings and reserves	-	-	-	-	2,682,127	2,682,127
Other reserves	-	-	-	-	73,733	73,733
Net profit for the year	-	-	-	-	314,841	314,841
Total equity attributable to equity holders of the parent	**-**	**-**	**-**	**-**	**10,030,333**	**10,030,333**
Guarantee fund	-	-	-	-	12,375	12,375
Total equity	-	-	-	-	**10,042,708**	**10,042,708**
Total liabilities and total equity (2)	**582,223**	**363,189**	**3,024,746**	**3,300,979**	**20,119,685**	**27,390,822**
Net assets/liabilities (1) – (2)	**5,399,523**	**503,171**	**(300,169)**	**1,693,525**	**(7,296,050)**	**-**
Net cumulative assets/liabilities	**5,399,523**	**5,902,694**	**5,602,525**	**7,296,050**	**-**	**-**

The items with undefined maturity are included in terms over 3 years.

** Receivables of HRK 232,489 thousand relate to reverse REPO agreements and were placed in the up to 1 month maturity category.*

31. Risk management (continued)

31.3. Liquidity risk (continued)

Group 2015	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Total HRK '000
Assets						
Cash on hand and due from banks	482,950	-	-	-	-	482,950
Deposits with other banks	205,177	-	154,220	-	-	359,397
Loans to financial institutions*	1,121,029	589,597	1,751,518	3,498,533	5,561,975	12,522,652
Loans to other customers	1,384,857	198,848	735,810	1,659,884	5,243,670	9,223,069
Financial assets at fair value through profit or loss	3,707	-	-	-	-	3,707
Assets available for sale	2,856,268	13,976	71	-	-	2,870,315
Assets held to maturity	-	10	4	-	1,437	1,451
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	62,238	62,238
Non-current assets held for sale	-	888	-	3,415	17,412	21,715
Other assets	3,175	1,057	504	-	542	5,278
Total assets (1)	**6,057,163**	**804,376**	**2,642,127**	**5,161,832**	**10,887,274**	**25,552,772**
Liabilities						
Deposits	112,993	-	5	101,555	22,083	236,636
Borrowings	74,834	195,163	1,527,267	2,499,200	7,181,623	11,478,087
Bonds payable	-	101,852	227,073	1,908,762	1,128,879	3,366,566
Other liabilities	169,362	36,280	120,393	223,958	256,946	806,939
Total liabilities	**357,189**	**333,295**	**1,874,738**	**4,733,475**	**8,589,531**	**15,888,228**
Equity						
Founder's capital	-	-	-	-	6,926,632	6,926,632
Retained earnings and reserves	-	-	-	-	2,475,862	2,475,862
Other reserves	-	-	-	-	43,283	43,283
Net profit for the year	-	-	-	-	206,265	206,265
Total equity attributable to equity holders of the parent	**-**	**-**	**-**	**-**	**9,652,042**	**9,652,042**
Guarantee fund	-	-	-	-	12,502	12,502
Total equity	**-**	**-**	**-**	**-**	**9,664,544**	**9,664,544**
Total liabilities and total equity (2)	**357,189**	**333,295**	**1,874,738**	**4,733,475**	**18,254,075**	**25,552,772**
Net assets/liabilities (1) – (2)	**5,699,974**	**471,081**	**767,389**	**428,357**	**(7,366,801)**	**-**
Net cumulative assets/liabilities	**5,699,974**	**6,171,055**	**6,938,444**	**7,366,801**	**-**	**-**

The items with undefined maturity are included in terms over 3 years.

** Receivables of HRK 606,930 thousand relate to reverse REPO agreements. The maturity of part of receivables was prolonged after the Statement of Financial Position date, and an amount of HRK 9,400 thousand was placed in the 1 up to 3 months maturity category.*

31. Risk management (continued)

31.3. Liquidity risk (continued)

The table below provides an analysis of total assets and total liabilities and equity as of 31 December 2016 and 31 December 2015 placed into relevant maturity groupings based on the remaining period as at the Statement of Financial Position date related to the contractual maturity date, as follows:

Bank 2016	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Total HRK '000
Assets						
Cash on hand and due from banks	490,695	-	-	-	-	490,695
Deposits with other banks	-	23,872	-	-	-	23,872
Loans to financial institutions*	684,891	441,872	1,774,961	3,131,823	5,855,564	11,889,111
Loans to other customers	1,423,234	385,784	948,959	1,850,611	6,902,606	11,511,194
Assets available for sale	3,329,585	13,989	-	-	-	3,343,574
Investments in subsidiaries	-	-	-	-	36,124	36,124
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	57,216	57,216
Non-current assets held for sale	-	-	27	11,450	5,753	17,230
Other assets	3,505	326	504	620	945	5,900
Total assets (1)	**5,931,910**	**865,843**	**2,724,451**	**4,994,504**	**12,858,208**	**27,374,916**
Liabilities						
Deposits	75,581	-	12,687	46,407	8,169	142,844
Borrowings	355,456	237,339	1,017,892	3,060,113	8,720,949	13,391,749
Bonds payable	-	95,932	1,888,837	-	1,120,800	3,105,569
Other liabilities	150,555	28,649	100,528	188,186	228,856	696,774
Total liabilities	**581,592**	**361,920**	**3,019,944**	**3,294,706**	**10,078,774**	**17,336,936**
Equity						
Founder's capital	-	-	-	-	6,959,632	6,959,632
Retained earnings and reserves	-	-	-	-	2,682,131	2,682,131
Other reserves	-	-	-	-	70,317	70,317
Net profit for the year	-	-	-	-	313,525	313,525
Capital	**-**	**-**	**-**	**-**	**10,025,605**	**10,025,605**
Guarantee fund	-	-	-	-	12,375	12,375
Total equity	**-**	**-**	**-**	**-**	**10,037,980**	**10,037,980**
Total liabilities and total equity (2)	**581,592**	**361,920**	**3,019,944**	**3,294,706**	**20,116,754**	**27,374,916**
Net assets/liabilities (1) – (2)	**5,350,318**	**503,923**	**(295,493)**	**1,699,798**	**(7,258,546)**	**-**
Net cumulative assets/liabilities	**5,350,318**	**5,854,241**	**5,558,748**	**7,258,546**	**-**	**-**

The items with undefined maturity are included in terms over 3 years.

** Receivables of HRK 232,489 thousand relate to reverse REPO agreements and were placed in the up to 1 month maturity category.*

31. Risk management (continued)

31.3. Liquidity risk (continued)

Bank 2015	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Total HRK '000
Assets						
Cash on hand and due from banks	482,708	-	-	-	-	482,708
Deposits with other banks	205,177	-	151,174	-	-	356,351
Loans to financial institutions*	1,121,029	589,597	1,751,518	3,498,533	5,561,975	12,522,652
Loans to other customers	1,384,857	198,848	735,810	1,659,884	5,243,670	9,223,069
Assets available for sale	2,818,431	13,892	-	-	-	2,832,323
Investments in subsidiaries	-	-	-	-	36,124	36,124
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	62,083	62,083
Non-current assets held for sale	-	888	-	3,415	17,412	21,715
Other assets	2,528	410	501	-	312	3,751
Total assets (1)	**6,014,730**	**803,635**	**2,639,003**	**5,161,832**	**10,921,576**	**25,540,776**
Liabilities						
Deposits	112,993	-	5	101,555	22,083	236,636
Borrowings	74,834	195,163	1,527,267	2,499,200	7,181,623	11,478,087
Bonds payable	-	101,852	227,073	1,908,762	1,128,879	3,366,566
Other liabilities	168,827	34,611	116,993	218,297	258,312	797,040
Total liabilities	**356,654**	**331,626**	**1,871,338**	**4,727,814**	**8,590,897**	**15,878,329**
Equity						
Founder's capital	-	-	-	-	6,926,632	6,926,632
Retained earnings and reserves	-	-	-	-	2,476,903	2,476,903
Other reserves	-	-	-	-	41,182	41,182
Net profit for the year	-	-	-	-	205,228	205,228
Capital	**-**	**-**	**-**	**-**	**9,649,945**	**9,649,945**
Guarantee fund	-	-	-	-	12,502	12,502
Total equity	**-**	**-**	**-**	**-**	**9,662,447**	**9,662,447**
Total liabilities and total equity (2)	**356,654**	**331,626**	**1,871,338**	**4,727,814**	**18,253,344**	**25,540,776**
Net assets/liabilities (1) – (2)	**5,658,076**	**472,009**	**767,665**	**434,018**	**(7,331,768)**	**-**
Net cumulative assets/liabilities	**5,658,076**	**6,130,085**	**6,897,750**	**7,331,768**	**-**	**-**

The items with undefined maturity are included in terms over 3 years.

** Receivables of HRK 606,930 thousand relate to reverse REPO agreements. The maturity of part of receivables was prolonged after the Statement of Financial Position date, and an amount of HRK 9,400 thousand was placed in the 1 up to 3 months maturity category.*

31. Risk management (continued)

31.3. Liquidity risk (continued)

The table below indicates the remaining contractual maturity of financial liabilities of the Group in undiscounted amounts:

Group 2016	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Total HRK '000
Financial liabilities						
Deposits	75,581	-	12,687	46,407	8,169	142,844
Borrowings	382,184	208,630	1,261,178	3,598,035	9,694,025	15,144,052
Bonds payable	-	-	2,051,330	136,040	1,188,820	3,376,190
Other liabilities	151,186	29,918	105,330	194,459	227,059	707,952
Total	**608,951**	**238,548**	**3,430,525**	**3,974,941**	**11,118,073**	**19,371,038**

Group 2015	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Total HRK '000
Financial liabilities						
Deposits	112,993	-	5	101,555	22,083	236,636
Borrowings	102,360	176,106	1,736,070	3,160,537	8,796,440	13,971,513
Bonds payable	-	-	402,237	2,141,631	1,266,310	3,810,178
Other liabilities	169,362	36,280	120,393	223,958	256,946	806,939
Total	**384,715**	**212,386**	**2,258,705**	**5,627,681**	**10,341,779**	**18,825,266**

31. Risk management (continued)

31.3. Liquidity risk (continued)

The table below indicates the remaining contractual maturity of financial liabilities of the Bank in undiscounted amounts:

Bank 2016	**Up to 1 month**	**1 - 3 months**	**3 - 12 months**	**1 - 3 years**	**Over 3 years**	**Total**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**
Financial liabilities						
Deposits	75,581	-	12,687	46,407	8,169	142,844
Borrowings	382,184	208,630	1,261,178	3,598,035	9,694,025	15,144,052
Bonds payable	-	-	2,051,330	136,040	1,188,820	3,376,190
Other liabilities	150,555	28,649	100,528	188,186	228,856	696,774
Total	**608,320**	**237,279**	**3,425,723**	**3,968,668**	**11,119,870**	**19,359,860**

Bank 2015	**Up to 1 month**	**1 - 3 months**	**3 - 12 months**	**1 - 3 years**	**Over 3 years**	**Total**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**
Financial liabilities						
Deposits	112,993	-	5	101,555	22,083	236,636
Borrowings	102,360	176,106	1,736,070	3,160,537	8,796,440	13,971,513
Bonds payable	-	-	402,237	2,141,631	1,266,310	3,810,178
Other liabilities	168,827	34,611	116,993	218,297	258,312	797,040
Total	**384,180**	**210,717**	**2,255,305**	**5,622,020**	**10,343,145**	**18,815,367**

31. Risk management (continued)

31.4. Market risk

Management of market risks at the Bank implies the reduction of interest rate risk and the currency risk to a minimal level.

31.4.1. Interest rate risk

The interest rate risk management at the Bank implies the management of interest rate risk in the Bank's book. As development and export special financial institution, the Bank does not perform trading activities.

For the purpose of measurement and monitoring of interest rate risk, the Bank carries out interest rate gap analysis. Interest rate gap is calculated for certain periods according to the possibilities of interest rate changes (fixed or floating rates) and presents the sensitivity of the Bank to the changes in interest rates. Interest rates are structured per currency, type and value, and projections of average weighted interest rates for Bank's funds and placements are made.

Based on the mentioned reports, the sensitivity of Bank's statement of profit or loss and other comprehensive income to possible interest rate fluctuations is monitored simultaneously with the endeavours to match the interest bearing total assets, total liabilities and equity. In this way, the Bank reduces its market movement sensitivity as well as its sensitivity to reference interest rates fluctuations. Furthermore, current market conditions and movements in forecasted market indicators are also monitored.

The Bank continuously analyses net interest rate margins by preparing projections on the basis of selected scenarios and among other things, assesses the impact of the change in interest rates by Bank's loan programmes, change in interest reference rates and change in prices of fund sources. The result of the analyses performed are reported to the ALCO and the Management Board with the aim to act proactively and insure further operations in accordance with the set of limits established for the purpose of risk management.

As a special financial institution, the Bank is not profit driven and, consequently, does not use derivative instruments. The use of derivatives is allowed for the purpose of position hedging only.

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest rate risk (continued)

The following tables demonstrate the sensitivity of the Group to the interest rate risk as of 31 December 2016 and 2015 on the basis of known dates of changes in prices of assets and liabilities to which floating and fixed interest rates are applied. Periods of interest rates changes are determined on the basis of residual maturity and contracted period when interest rates change, depending on which is shorter.

Assets and liabilities on which interest is not charged are placed into the non-interest bearing category. The tables below demonstrate the estimation of Group's interest rate risk exposure as of 31 December 2016 and 2015 which may not be indicative for the positions in other periods.

Group 2016	Up to 1 month	1 - 3 months	3 - 12 months	1 - 3 years	Over 3 years	Non-interest bearing	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Assets							
Cash on hand and due from banks	551	-	-	-	-	490,695	491,246
Deposits with other banks	-	23,871	-	-	-	1	23,872
Loans to financial institutions	652,666	836,489	1,873,910	2,926,641	5,562,538	36,867	11,889,111
Loans to other customers	1,517,371	824,285	1,081,418	1,506,407	6,522,314	59,399	11,511,194
Financial assets at fair value through profit or loss	-	-	-	-	-	286	286
Assets available for sale	2,431,379	-	-	-	-	958,655	3,390,034
Assets held to maturity	-	-	-	-	1,408	14	1,422
Investments in associates	-	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	-	57,305	57,305
Non-current assets held for sale	-	-	-	-	-	17,230	17,230
Other assets	-	-	-	-	-	9,122	9,122
Total assets (1)	**4,601,967**	**1,684,645**	**2,955,328**	**4,433,048**	**12,086,260**	**1,629,574**	**27,390,822**

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest rate risk (continued)

Group 2016	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Non-interest bearing HRK '000	Total HRK '000
Liabilities							
Deposits	-	-	-	-	-	142,844	142,844
Borrowings	355,442	171,450	1,020,722	3,059,168	8,720,949	64,018	13,391,749
Bonds payable	-	-	1,888,837	-	1,120,800	95,932	3,105,569
Other liabilities	-	-	-	-	-	707,952	707,952
Total liabilities	**355,442**	**171,450**	**2,909,559**	**3,059,168**	**9,841,749**	**1,010,746**	**17,348,114**
Equity							
Founder's capital	-	-	-	-	-	6,959,632	6,959,632
Retained earnings and reserves	-	-	-	-	-	2,682,127	2,682,127
Other reserves	-	-	-	-	-	73,733	73,733
Net profit for the year	-	-	-	-	-	314,841	314,841
Total equity attributable to equity holders of the parent	-	-	-	-	-	**10,030,333**	**10,030,333**
Guarantee fund	-	-	-	-	-	12,375	12,375
Total equity	-	-	-	-	-	**10,042,708**	**10,042,708**
Total liabilities and total equity (2)	**355,442**	**171,450**	**2,909,559**	**3,059,168**	**9,841,749**	**11,053,454**	**27,390,822**
Net assets/liabilities (1) – (2)	**4,246,525**	**1,513,195**	**45,769**	**1,373,880**	**2,244,511**	**(9,423,880)**	**-**

(All amounts are expressed in HRK thousand)

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest rate risk (continued)

Group 2015	Up to 1 month	1 to 3 months	3 months to 1 year	1 to 3 years	Over 3 years	Non-interest bearing	Total
Assets							
Cash on hand and due from banks	242	-	-	-	-	482,708	482,950
Deposits with other banks	204,986	-	154,174	-	-	237	359,397
Loans to financial institutions	1,114,347	1,075,199	1,915,320	3,233,354	5,170,599	13,833	12,522,652
Loans to other customers	1,442,435	620,953	1,008,086	1,195,079	4,908,612	47,904	9,223,069
Financial assets at fair value through profit or loss	-	-	-	-	-	3,707	3,707
Assets available for sale	2,102,226	-	-	-	-	768,089	2,870,315
Assets held to maturity	-	-	-	-	1,437	14	1,451
Investments in associates	-	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	-	62,238	62,238
Non-current assets held for sale	-	-	-	-	-	21,715	21,715
Other assets	-	-	-	-	-	5,278	5,278
Total assets (1)	**4,864,236**	**1,696,152**	**3,077,580**	**4,428,433**	**10,080,648**	**1,405,723**	**25,552,772**
Liabilities							
Deposits	-	-	-	-	-	236,636	236,636
Borrowings	74,834	127,590	1,531,085	2,495,382	7,181,623	67,573	11,478,087
Bonds payable	-	-	227,073	1,908,762	1,128,879	101,852	3,366,566
Other liabilities	-	-	-	-	-	806,939	806,939
Total liabilities	**74,834**	**127,590**	**1,758,158**	**4,404,144**	**8,310,502**	**1,213,000**	**15,888,228**
Equity							
Founder's capital	-	-	-	-	-	6,926,632	6,926,632
Retained earnings and reserves	-	-	-	-	-	2,475,862	2,475,862
Other reserves	-	-	-	-	-	43,283	43,283
Net profit for the year	-	-	-	-	-	206,265	206,265
Total equity attributable to equity holders of the parent	**-**	**-**	**-**	**-**	**-**	**9,652,042**	**9,652,042**
Guarantee fund	-	-	-	-	-	12,502	12,502
Total equity	**-**	**-**	**-**	**-**	**-**	**9,664,544**	**9,664,544**
Total liabilities and total equity (2)	**74,834**	**127,590**	**1,758,158**	**4,404,144**	**8,310,502**	**10,877,544**	**25,552,772**
Net assets/liabilities (1) – (2)	**4,789,402**	**1,568,562**	**1,319,422**	**24,289**	**1,770,146**	**(9,471,821)**	**-**

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest rate risk (continued)

The following tables demonstrate the sensitivity of HBOR to the interest rate risk as of 31 December 2016 and 2015 on the basis of known dates of changes in prices of assets and liabilities to which floating and fixed interest rates are applied. Periods of interest rates changes are determined on the basis of residual maturity and contracted period when interest rates change, depending on which is shorter.

Assets and liabilities on which interest is not charged are placed into the non-interest bearing category. The tables below demonstrate the estimation of HBOR's interest rate risk exposure as of 31 December 2016 and 2015 which may not be indicative for the positions in other periods.

Bank 2016	**Up to 1 month**	**1 - 3 months**	**3 - 12 months**	**1 - 3 years**	**Over 3 years**	**Non-interest bearing**	**Total**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**
Assets							
Cash on hand and due from banks	-	-	-	-	-	490,695	490,695
Deposits with other banks	-	23,871	-	-	-	1	23,872
Loans to financial institutions	652,666	836,489	1,873,910	2,926,641	5,562,538	36,867	11,889,111
Loans to other customers	1,517,371	824,285	1,081,418	1,506,407	6,522,314	59,399	11,511,194
Assets available for sale	2,385,835	-	-	-	-	957,739	3,343,574
Investments in subsidiaries	-	-	-	-	-	36,124	36,124
Investments in associates	-	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	-	57,216	57,216
Non-current assets held for sale	-	-	-	-	-	17,230	17,230
Other assets	-	-	-	-	-	5,900	5,900
Total assets (1)	**4,555,872**	**1,684,645**	**2,955,328**	**4,433,048**	**12,084,852**	**1,661,171**	**27,374,916**

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest rate risk (continued)

Bank 2015	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Non-interest bearing HRK '000	Total HRK '000
Liabilities							
Deposits	-	-	-	-	-	142,844	142,844
Borrowings	355,442	171,450	1,020,722	3,059,168	8,720,949	64,018	13,391,749
Bonds payable	-	-	1,888,837	-	1,120,800	95,932	3,105,569
Other liabilities	-	-	-	-	-	696,774	696,774
Total liabilities	**355,442**	**171,450**	**2,909,559**	**3,059,168**	**9,841,749**	**999,568**	**17,336,936**
Equity							
Founder's capital	-	-	-	-	-	6,959,632	6,959,632
Retained earnings and reserves	-	-	-	-	-	2,682,131	2,682,131
Other reserves	-	-	-	-	-	70,317	70,317
Net profit for the year	-	-	-	-	-	313,525	313,525
Capital	**-**	**-**	**-**	**-**	**-**	**10,025,605**	**10,025,605**
Guarantee fund	-	-	-	-	-	12,375	12,375
Total equity	**-**	**-**	**-**	**-**	**-**	**10,037,980**	**10,037,980**
Total liabilities and total equity (2)	**355,442**	**171,450**	**2,909,559**	**3,059,168**	**9,841,749**	**11,037,548**	**27,374,916**
Net assets/liabilities (1) – (2)	**4,200,430**	**1,513,195**	**45,769**	**1,373,880**	**2,243,103**	**(9,376,377)**	**-**

(All amounts are expressed in HRK thousand)

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest rate risk (continued)

Bank 2015	Up to 1 month	1 to 3 months	3 months to 1 year	1 to 3 years	Over 3 years	Non-interest bearing	Total
Assets							
Cash on hand and due from banks	-	-	-	-	-	482,708	482,708
Deposits with other banks	204,986	-	151,174	-	-	191	356,351
Loans to financial institutions	1,114,347	1,075,199	1,915,320	3,233,354	5,170,599	13,833	12,522,652
Loans to other customers	1,442,435	620,953	1,008,086	1,195,079	4,908,612	47,904	9,223,069
Assets available for sale	2,065,045	-	-	-	-	767,278	2,832,323
Investments in subsidiaries	-	-	-	-	-	36,124	36,124
Investments in associates	-	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	-	62,083	62,083
Non-current assets held for sale	-	-	-	-	-	21,715	21,715
Other assets	-	-	-	-	-	3,751	3,751
Total assets (1)	**4,826,813**	**1,696,152**	**3,074,580**	**4,428,433**	**10,079,211**	**1,435,587**	**25,540,776**
Liabilities							
Deposits	-	-	-	-	-	236,636	236,636
Borrowings	74,834	127,590	1,531,085	2,495,382	7,181,623	67,573	11,478,087
Bonds payable	-	-	227,073	1,908,762	1,128,879	101,852	3,366,566
Other liabilities	-	-	-	-	-	797,040	797,040
Total liabilities	**74,834**	**127,590**	**1,758,158**	**4,404,144**	**8,310,502**	**1,203,101**	**15,878,329**
Equity							
Founder's capital	-	-	-	-	-	6,926,632	6,926,632
Retained earnings and reserves	-	-	-	-	-	2,476,903	2,476,903
Other reserves	-	-	-	-	-	41,182	41,182
Net profit for the year	-	-	-	-	-	205,228	205,228
Capital	**-**	**-**	**-**	**-**	**-**	**9,649,945**	**9,649,945**
Guarantee fund	-	-	-	-	-	12,502	12,502
Total equity	**-**	**-**	**-**	**-**	**-**	**9,662,447**	**9,662,447**
Total liabilities and total equity (2)	**74,834**	**127,590**	**1,758,158**	**4,404,144**	**8,310,502**	**10,865,548**	**25,540,776**
Net assets/liabilities (1) – (2)	**4,751,979**	**1,568,562**	**1,316,422**	**24,289**	**1,768,709**	**(9,429,961)**	**-**

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest rate risk (continued)

Total assets, total liabilities and equity on the basis of a possibility of changes in interest rates (fixed or variable):

		Group		Bank
	2016	**2015**	**2016**	**2015**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**
Assets				
Fixed interest rate assets	23,991,858	22,176,481	23,944,355	22,134,621
Variable interest rate assets	1,769,390	1,970,568	1,769,390	1,970,568
Non-interest bearing	1,629,574	1,405,723	1,661,171	1,435,587
Total assets	**27,390,822**	**25,552,772**	**27,374,916**	**25,540,776**
Liabilities				
Fixed interest rate liabilities	16,333,589	14,667,593	16,333,589	14,667,593
Variable interest rate liabilities	3,779	7,635	3,779	7,635
Non-interest bearing	11,053,454	10,877,544	11,037,548	10,865,548
Total liabilities and total equity	**27,390,822**	**25,552,772**	**27,374,916**	**25,540,776**

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest rate risk (continued)

Sensitivity analysis

Assumptions used in preparing the interest risk sensitivity analysis relate to possible changes in reference interest rates in order to assess the hypothetical effect on HBOR's profit.

Volatility of reference interest rates for 2016 has been determined using the standard deviation method on the daily changes of the reference interest rates linked to EUR and USD. On the basis of the above volatility, possible changes in reference interest rates linked to EUR and USD have been established and used in the sensitivity analysis.

The analysis presents the sensitivity of interest rates to reasonably expected changes in basis points of variable interest rates. All other variables remain constant.

The sensitivity of profit is influenced by hypothetical changes in interest rates during a period of one year based on interest bearing assets and liabilities with a variable interest rate.

Currency	Increase in b.p. in 2016	Effect on profit in 2016	Increase in b.p. in 2015	Effect on profit in 2015
		HRK '000		HRK '000
EUR	+4	535	+40	7,237
USD	+11	472	+11	161

Currency	Decrease in b.p. in 2016	Effect on profit in 2016	Decrease in b.p. in 2015	Effect on profit in 2015
		HRK '000		HRK '000
EUR	-4	(535)	-40	(7,237)
USD	-11	(472)	-11	(161)

31. Risk management (continued)

31.4. Market risk (continued)

31.4.2. Currency risk

By the internal documents, the Bank has established the methods for the assessment, i.e. measurement, monitoring, management and control of the currency risk, as well as the limits and proceedings both in cases indicating to a crisis and in crisis conditions. Responsibilities and accountabilities have been determined for those organisational units of the Bank that participate in the currency risk management as well as reports necessary for comprehensive perception of this risk.

Exposure to currency risk is monitored daily on the basis of the total open foreign currency position and on the basis of the open foreign currency positions in significant currencies. In addition to the daily monitoring of open foreign currency positions, the projections of their developments are also prepared. The projections of the developments in the open foreign currency positions provide the basis for the Asset and Liability Management Committee to adopt guidelines and resolutions and for the Management Board to make decisions in order to secure the timely undertaking of activities aiming to maintain the Bank's operations within the established currency risk management limits. For the measurement/assessment of currency risk, the Bank uses VaR model as an auxiliary model and regularly reports to the bodies in charge on maximum possible losses on significant currencies.

The Bank performs stress tests under the assumption of extensive appreciation/depreciation of HRK against significant currencies and reports on test results to the ALCO and the Management Board.

31. Risk management (continued)

31.4. Market risk (continued)

31.4.2. Currency risk (continued)

Total assets, total liabilities and equity as of 31 December 2016 and 31 December 2015 in HRK and foreign currencies can be shown as follows:

Group 2016	USD HRK '000	EUR HRK '000	Other foreign currencies HRK '000	Total foreign currencies HRK '000	HRK HRK '000	Total HRK '000
Assets						
Cash on hand and due from banks	1,606	301,338	1,584	304,528	186,718	491,246
Deposits with other banks	20,581	-	3,291	23,872	-	23,872
Loans to financial institutions	-	6,655,483	-	6,655,483	5,233,628	11,889,111
Loans to other customers	527,661	7,768,328	-	8,295,989	3,215,205	11,511,194
Financial assets at fair value through profit or loss	-	286	-	286	-	286
Assets available for sale	14,686	1,100,197	-	1,114,883	2,275,151	3,390,034
Assets held to maturity	-	1,422	-	1,422	-	1,422
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	57,305	57,305
Non-current assets held for sale	-	-	-	-	17,230	17,230
Other assets	-	369	-	369	8,753	9,122
Total assets (1)	**564,534**	**15,827,423**	**4,875**	**16,396,832**	**10,993,990***	**27,390,822**
Liabilities						
Deposits	48,380	42,778	3,459	94,617	48,227	142,844
Borrowings	315,434	13,076,315	-	13,391,749	-	13,391,749
Bonds payable	-	3,105,569	-	3,105,569	-	3,105,569
Other liabilities	163	9,664	2,885	12,712	695,240	707,952
Total liabilities	**363,977**	**16,234,326**	**6,344**	**16,604,647**	**743,467**	**17,348,114**
Equity						
Founder's capital	-	-	-	-	6,959,632	6,959,632
Retained earnings and reserves	-	-	-	-	2,682,127	2,682,127
Other reserves	-	-	-	-	73,733	73,733
Net profit for the year	-	-	-	-	314,841	314,841
Total equity attributable to equity holders of the parent	**-**	**-**	**-**	**-**	**10,030,333**	**10,030,333**
Guarantee fund	-	12,375	-	12,375	-	12,375
Total equity	**-**	**12,375**	**-**	**12,375**	**10,030,333**	**10,042,708**
Total liabilities and total equity (2)	**363,977**	**16,246,701**	**6,344**	**16,617,022**	**10,773,800**	**27,390,822**
Net assets/liabilities (1) – (2)	**200,557**	**(419,278)**	**(1,469)****	**(220,190)**	**220,190**	**-**

** Amounts linked to a one-way currency clause represent HRK 249,278 thousand.*

*** Reported gap is a result of provisions made for issued foreign currency guarantees in other foreign currencies stated under "Other liabilities".*

31. Risk management (continued)

31.4. Market risk (continued)

31.4.2. Currency risk (continued)

Group 2015	USD HRK '000	EUR HRK '000	Other foreign currencies HRK '000	Total foreign currencies HRK '000	HRK HRK '000	Total HRK '000
Assets						
Cash on hand and due from banks	72,536	302,044	775	375,355	107,595	482,950
Deposits with other banks	-	350,813	5,538	356,351	3,046	359,397
Loans to financial institutions	-	6,951,331	-	6,951,331	5,571,321	12,522,652
Loans to other customers	152,223	5,325,845	-	5,478,068	3,745,001	9,223,069
Financial assets at fair value through profit or loss	-	2,690	-	2,690	1,017	3,707
Assets available for sale	14,629	1,073,568	-	1,088,197	1,782,118	2,870,315
Assets held to maturity	-	1,451	-	1,451	-	1,451
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	62,238	62,238
Non-current assets held for sale	-	-	-	-	21,715	21,715
Other assets	-	495	-	495	4,783	5,278
Total assets (1)	**239,388**	**14,008,237**	**6,313**	**14,253,938**	**11,298,834***	**25,552,772**
Liabilities						
Deposits	75,197	89,531	6,135	170,863	65,773	236,636
Borrowings	-	10,731,184	-	10,731,184	746,903	11,478,087
Bonds payable	-	3,366,566	-	3,366,566	-	3,366,566
Other liabilities	95	8,541	9,960	18,596	788,343	806,939
Total liabilities	**75,292**	**14,195,822**	**16,095**	**14,287,209**	**1,601,019**	**15,888,228**
Equity						
Founder's capital	-	-	-	-	6,926,632	6,926,632
Retained earnings and reserves	-	-	-	-	2,475,862	2,475,862
Other reserves	-	-	-	-	43,283	43,283
Net profit for the year	-	-	-	-	206,265	206,265
Total equity attributable to equity holders of the parent	**-**	**-**	**-**	**-**	**9,652,042**	**9,652,042**
Guarantee fund	-	12,502	-	12,502	-	12,502
Total equity	**-**	**12,502**	**-**	**12,502**	**9,652,042**	**9,664,544**
Total liabilities and total equity (2)	**75,292**	**14,208,324**	**16,095**	**14,299,711**	**11,253,061**	**25,552,772**
Net assets/liabilities (1) – (2)	**164,096**	**(200,087)**	**(9,782)****	**(45,773)**	**45,773**	**-**

** Amounts linked to a one-way currency clause represent HRK 347,235 thousand.*

*** Reported gap is a result of provisions made for issued foreign currency guarantees in other foreign currencies stated under "Other liabilities".*

31. Risk management (continued)

31.4. Market risk (continued)

31.4.2. Currency risk (continued)

Total assets, total liabilities and equity as of 31 December 2016 and 31 December 2015 in HRK and foreign currencies can be shown as follows:

Bank 2016	USD	EUR	Other foreign currencies	Total foreign currencies	HRK	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Assets						
Cash on hand and due from banks	1,606	301,338	1,584	304,528	186,167	490,695
Deposits with other banks	20,581	-	3,291	23,872	-	23,872
Loans to financial institutions	-	6,655,483	-	6,655,483	5,233,628	11,889,111
Loans to other customers	527,661	7,768,328	-	8,295,989	3,215,205	11,511,194
Assets available for sale	14,686	1,089,520	-	1,104,206	2,239,368	3,343,574
Investments in subsidiaries	-	-	-	-	36,124	36,124
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	57,216	57,216
Non-current assets held for sale	-	-	-	-	17,230	17,230
Other assets	-	-	-	-	5,900	5,900
Total assets (1)	**564,534**	**15,814,669**	**4,875**	**16,384,078**	**10,990,838***	**27,374,916**
Liabilities						
Deposits	48,380	42,778	3,459	94,617	48,227	142,844
Borrowings	315,433	13,076,316	-	13,391,749	-	13,391,749
Bonds payable	-	3,105,569	-	3,105,569	-	3,105,569
Other liabilities	-	2,895	2,840	5,735	691,039	696,774
Total liabilities	**363,813**	**16,227,558**	**6,299**	**16,597,670**	**739,266**	**17,336,936**
Equity						
Founder's capital	-	-	-	-	6,959,632	6,959,632
Retained earnings and reserves	-	-	-	-	2,682,131	2,682,131
Other reserves	-	-	-	-	70,317	70,317
Net profit for the year	-	-	-	-	313,525	313,525
Capital	**-**	**-**	**-**	**-**	**10,025,605**	**10,025,605**
Guarantee fund	-	12,375	-	12,375	-	12,375
Total equity	**-**	**12,375**	**-**	**12,375**	**10,025,605**	**10,037,980**
Total liabilities and total equity (2)	**363,813**	**16,239,933**	**6,299**	**16,610,045**	**10,764,871**	**27,374,916**
Net assets/liabilities (1) – (2)	**200,721**	**(425,264)**	**(1,424)****	**(225,967)**	**225,967**	**-**

** Amounts linked to a one-way currency clause represent HRK 249,278 thousand.*

*** Reported gap is a result of provisions made for issued foreign currency guarantees in other foreign currencies stated under "Other liabilities".*

31. Risk management (continued)

31.4. Market risk (continued)

31.4.2. Currency risk (continued)

Bank 2015	USD	EUR	Other foreign currencies	Total foreign currencies	HRK	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Assets						
Cash on hand and due from banks	72,536	302,044	775	375,355	107,353	482,708
Deposits with other banks	-	350,813	5,538	356,351	-	356,351
Loans to financial institutions	-	6,951,331	-	6,951,331	5,571,321	12,522,652
Loans to other customers	152,223	5,325,845	-	5,478,068	3,745,001	9,223,069
Assets available for sale	14,629	1,063,164	-	1,077,793	1,754,530	2,832,323
Investments in subsidiaries	-	-	-	-	36,124	36,124
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	62,083	62,083
Non-current assets held for sale	-	-	-	-	21,715	21,715
Other assets	-	-	-	-	3,751	3,751
Total assets (1)	**239,388**	**13,993,197**	**6,313**	**14,238,898**	**11,301,878***	**25,540,776**
Liabilities						
Deposits	75,197	89,531	6,135	170,863	65,773	236,636
Borrowings	-	10,731,184	-	10,731,184	746,903	11,478,087
Bonds payable	-	3,366,566	-	3,366,566	-	3,366,566
Other liabilities	-	1,795	9,917	11,712	785,328	797,040
Total liabilities	**75,197**	**14,189,076**	**16,052**	**14,280,325**	**1,598,004**	**15,878,329**
Equity						
Founder's capital	-	-	-	-	6,926,632	6,926,632
Retained earnings and reserves	-	-	-	-	2,476,903	2,476,903
Other reserves	-	-	-	-	41,182	41,182
Net profit for the year	-	-	-	-	205,228	205,228
Capital	-	-	-	-	**9,649,945**	**9,649,945**
Guarantee fund	-	12,502	-	12,502	-	12,502
Total equity	-	**12,502**	-	**12,502**	**9,649,945**	**9,662,447**
Total liabilities and total equity (2)	**75,197**	**14,201,578**	**16,052**	**14,292,827**	**11,247,949**	**25,540,776**
Net assets/liabilities (1) – (2)	**164,191**	**(208,381)**	**(9,739)****	**(53,929)**	**53,929**	-

** Amounts linked to a one-way currency clause represent HRK 347,235 thousand.*

*** Reported gap is a result of provisions made for issued foreign currency guarantees in other foreign currencies stated under "Other liabilities".*

31. Risk management (continued)

31.4. Market risk (continued)

31.4.2. Currency risk (continued)

Sensitivity analysis

Sensitivity analysis of the Bank's total assets and total liabilities to fluctuations in foreign exchange rates is carried out for those foreign currencies that represent Bank's significant currencies as at the reporting date.

An assumption of reasonably possible fluctuations in EUR exchange rates against HRK was used in the foreign currency risk sensitivity analysis, with the other variables remaining stable, in order to assess the hypothetical effect on HBOR's profit as of 31 December 2016.

Volatility of the exchange rate EUR/HRK, determined using the standard deviation method on the changes of the foreign exchange rate EUR/HRK, equalled 1.5% in 2016 (31 December 2015: 1.9%).

The effect of the assumed changes in the foreign exchange rate EUR/HRK by total asset, total liabilities and equity items denominated or indexed to EUR on HBOR's profits is stated below.

	Change in currency rate in 2016 %	Effect on profit in 2016 HRK' 000	Change in currency rate in 2015 %	Effect on profit in 2015 HRK' 000
EUR	+1.5%	5,912	+1.9%	6,823
EUR	-1.5%	(5,020)	-1.9%	(6,056)

31.5. Operational risk

The Bank has established a framework for operational risk management that is, to a considerable extent, aligned with regulations prescribed by the Croatian National Bank applicable to the Bank's business and good banking practices in the area of risk management and that was introduced in 2012.

The basic principles of operational risk management were identified in the umbrella act, Operational Risk Management Policies which prescribes the elements of the system for management of these risks, which include identifying, measuring, assessing, containing and monitoring operational risk. A structure of management and accountability in the system has been set up, an approach for the calculation of capital requirements for operational risk has been determined and a reporting system has been established.

A particular feature of operational risk compared to other types of risk is reflected in the presence of this risk throughout the entire organisation and the management of this risk in all organisational parts of the Bank.
Monitoring of operational risks is supported by a software solution that enables recording of operational risk events.

31. Risk management (continued)

31.5. Operational risk (continued)

Overall evaluation of operational risk is performed through the Operational Risk Map, which identifies and evaluates operational risk the Bank is exposed to, in order to identify further risk containment measures.

The operational risk is assessed also on the occasion of introducing new products and business changes and on the occasion of outsourcing business activities.

The Bank is trying to minimise the operational risk by active monitoring, management and control of operational risk exposures.

The Committee for the management of information system of HBOR was established in order to monitor IT system performance with the purpose of IT resources management by setting the appropriate level of efficiency and security of IT for providing, among other things, appropriate management of risks arising from IT technology utilisation. Considering the significant level of operational risk arising from IT utilisation, the Bank has established a function for the control of IT system security. Within this function, a system for the management of business continuity was established for the purpose of ensuring the recovery of operations and limiting the adverse effects in the case of significantly impaired or discontinued operations.

31.6. Outsourcing risk

The aim of outsourcing is to reduce the operating costs, to achieve a higher level of services and to use the professional know-how of service providers in the performance of daily activities.
The Bank manages the outsourcing risk on the basis of internal documents that are in compliance with the regulations prescribed by the Croatian National Bank and good banking practices applicable to the Bank's business.
In addition to the management of this risk, the internal documents determine also the procedures for the outsourcing of activities to the service providers, the rules for the management of relations with the service providers and the obligation to reduce the risk to the lowest level possible.
Central records of outsourced activities have been established and reports on materially significant outsourced activities are submitted to the Management Board and the Supervisory Board of the Bank on an annual basis.

(All amounts are expressed in HRK thousand)

32. Fair value of financial assets and financial liabilities

The accounting policy on fair value measurements is discussed in Note 2.

32.1. Fair value of financial assets and financial liabilities initially recognized and measured at fair value

The Group measures certain financial assets and financial liabilities at fair value at the end of each reporting period:

Group			**2016**			**2015**
	Level 1	**Level 2**	**Level 3**	**Level 1**	**Level 2**	**Level 3**
Financial assets at fair value through profit or loss:						
Shares in investment funds recognised at fair value through profit or loss	286	-	-	3,707	-	-
Total financial assets at fair value through profit or loss	**286**	**-**	**-**	**3,707**	**-**	**-**
Assets available for sale:						
Debt instruments:						
Listed debt instruments:						
Bonds of the Ministry of Finance of the Republic of Croatia	925,887	-	-	679,617	-	-
Financial institution bonds	910	-	-	930	-	-
Corporate bonds	1,161	-	-	396	-	-
Treasury bills of the Ministry of Finance of the Republic of Croatia	1,500,420	-	-	-	1,418,963	-
Accrued interest	14,495	-	-	14,441	-	-
Unlisted debt instruments:						
Corporate bonds	-	-	502	-	-	-
Accrued interest	-	-	99	-	-	-
Total debt instruments	**2,442,873**	**-**	**601**	**695,384**	**1,418,963**	**-**
Equity instruments:						
Listed equity instruments:						
Corporate shares	10,938	-	-	-	-	-
Unlisted equity instruments:						
Investment in shares of foreign companies	-	32	-	-	26	-
Investment in financial institutions shares	-	161	-	-	161	-
Shares of foreign financial institutions – EIF	-	25,815	-	-	24,420	-
Corporate shares	-	-	-	-	-	-
Total equity instruments	**10,938**	**26,008**	**-**	**-**	**24,607**	**-**
Investments in investment funds:						
Shares classified as assets available for sale	909,614	-	-	729,010	-	-
Total investments in investment funds	**909,614**	**-**	**-**	**729,010**	**-**	**-**
Total assets available for sale	**3,363,425**	**26,008**	**601**	**1,424,394**	**1,443,570**	**-**

In the reporting period, Debt Instruments: Treasury Bills of the Ministry of Finance of the Republic of Croatia were reclassified from Level 2 into Level 1 because credit institutions in the country started to list prices at Bloomberg, and quoted market price was used as the valuation technique instead of a discounted cash flow.

Debt Instruments: Corporate Bonds were classified within Level 3 of the fair value hierarchy. The valuation technique used was the method of the discounted cash flows based on market interest rates, spread linked to internal credit-rating and internally determined spread linked to financial instrument liquidity.

(All amounts are expressed in HRK thousand)

32. Fair value of financial assets and financial liabilities (continued)

32.1. Fair value of financial assets and financial liabilities initially recognized and measured at fair value (continued)

In the past reporting periods, this investment was valued at acquisition costs and was not presented in the fair value hierarchy table.

In 2016, Equity Instruments: Corporate Shares were classified within Level 1 of the fair value hierarchy, and quoted market price was used as the valuation technique.

Bank			2016			2015
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Assets available for sale:						
Debt instruments:						
Listed debt instruments:						
Bonds of the Ministry of Finance of the Republic of Croatia	884,914	-	-	644,532	-	-
Treasury bills of the Ministry of finance of the Republic of Croatia	1,500,420	-	-	-	1,418,963	-
Accrued interest	13,890	-	-	13,862	-	-
Unlisted debt instruments:						
Corporate bonds	-	-	502	-	-	-
Accrued interest	-	-	99	-	-	-
Total debt instruments	**2,399,224**	**-**	**601**	**658,394**	**1,418,963**	**-**
Equity instruments:						
Listed equity instruments:						
Corporate shares	10,938	-	-	-	-	-
Unlisted equity instruments:						
Investment in shares of foreign companies	-	32	-	-	26	-
Investment in financial institutions shares	-	161	-	-	161	-
Shares of foreign financial institutions – EIF	-	25,815	-	-	24,420	-
Corporate shares	-	-	-	-	-	-
Total equity instruments	**10,938**	**26,008**	**-**	**-**	**24,607**	**-**
Investments in investment funds:						
Shares classified as assets available for sale	906,803	-	-	728,778	-	-
Total investments in investment funds	**906,803**	**-**	**-**	**728,778**	**-**	**-**
Total assets available for sale	**3,316,965**	**26,008**	**601**	**1,387,172**	**1,443,570**	**-**

In the reporting period, Debt Instruments: Treasury Bills of the Ministry of Finance of the Republic of Croatia were reclassified from Level 2 into Level 1 because credit institutions in the country started to list prices at Bloomberg, and quoted market price was used as the valuation technique instead of a discounted cash flow.

Debt Instruments: Corporate Bonds were classified within Level 3 of the fair value hierarchy. The valuation technique used was the method of the discounted cash flows based on market interest rates, spread linked to internal credit-rating and internally determined spread linked to financial instrument liquidity.

32. Fair value of financial assets and financial liabilities (continued)

32.1. Fair value of financial assets and financial liabilities initially recognized and measured at fair value (continued)

In the past reporting periods, this investment was valued at acquisition costs and was not presented in the fair value hierarchy table.

In 2016, Equity Instruments: Corporate Shares were classified within Level 1 of the fair value hierarchy, and quoted market price was used as the valuation technique.

32.2. Fair value of financial assets and financial liabilities carried at amortized cost

The Management Board estimates that their carrying amounts of financial assets and financial liabilities carried at amortized cost are a reasonable approximation of fair value. The fair value of bonds payable that is determined by using adjusted observable prices is presented in Note 24 as disclosed in Note 2.

33. Reporting by segments

General information on segments is given in relation to business segments of the Group.
Since the Group does not allocate administrative costs and interest by segments, the profitability of segments is not presented.

Assets and liabilities by segments are presented in net terms, i.e. gross after impairment and provisioning, and before the effect of mitigation through collateral received.

Business operations of segments are divided in terms of organisation and management. Each segment as a whole provides various products and services and operates in various markets.

Business segments:

The Group has following business segments:

Segment:	**Business activities of the segment include:**
Banking activities	Financing reconstruction and development of the Croatian economy, financing of infrastructure, export promotion, support for the development of small and medium-sized companies, environmental protection, and export credit insurance of Croatian goods and services against non-market risks for and on behalf of the Republic of Croatia.
Insurance activities	Insurance of foreign and domestic short-term receivables of business entities relating to deliveries of goods and services.
Other	Preparation of analyses, credit risk assessment and providing information on creditworthiness.

33. Reporting by segments (continued)

2016	Banking activities HRK '000	Insurance activities HRK '000	Other activities HRK '000	Unallocated HRK '000	Total HRK '000
Net interest income	417,671	1,641	-	-	419,312
Net fee income	25,067	1,032	1,070	-	27,169
Net income/(expenses) from financial operations	7,312	178	6	-	7,496
Net premiums earned	-	5,681	-	-	5,681
Other income	18,016	76	285	(300)	18,077
Income from operating activities	**468,066**	**8,608**	**1,361**	**(300)**	**477,735**
Operating costs	(152,227)	(5,219)	(1,073)	301	(158,218)
Impairment loss and provisions	(2,314)	(64)	5	-	(2,373)
Expenses for insured cases	-	(1,591)	-	-	(1,591)
Net change in provisions	-	34	-	-	34
Other expenses	-	(513)	-	-	(513)
Operating expenses	**(154,541)**	**(7,353)**	**(1,068)**	**301**	**(162,661)**
Profit/(loss) before income tax	**313,525**	**1,255**	**293**	**1**	**315,074**
Income tax	-	(176)	(57)	-	(233)
Profit/(loss) for the year	**313,525**	**1,079**	**236**	**1**	**314,841**
Assets of segment	27,374,916	51,667	895	(36,656)	27,390,822
Total assets	**27,374,916**	**51,667**	**895**	**(36,656)**	**27,390,822**
Liabilities of segment	17,336,936	11,049	159	(30)	17,348,114
Total equity and guarantee fund	10,037,980	3,119	436	1,173	10,042,708
Total liabilities and total equity	**27,374,916**	**14,168**	**595**	**1,143**	**27,390,822**

Intra-group transactions are presented under "Unallocated".

For the purposes of this Note, Net income/(expense) from financial operations is reported as an income item, regardless the actual realization, to enable comparison of the amounts stated in the Statement of profit or loss and other comprehensive income.

The Group decided to apply a simple approach of stating operating segments by taking into consideration the main business model of each member of the Group as previously described in this Note.

33. Reporting by segments (continued)

2015	Banking activities HRK '000	Insurance activities HRK '000	Other activities HRK '000	Unallocated HRK '000	Total HRK '000
Net interest income	398,079	1,388	-	-	399,467
Net fee income	18,453	1,366	1,027	-	20,846
Net income/(expenses) from financial operations	21,868	379	34	-	22,281
Net premiums earned	-	5,933	-	-	5,933
Other income	3,520	69	286	(302)	3,573
Income from operating activities	**441,920**	**9,135**	**1,347**	**(302)**	**452,100**
Operating costs	(131,840)	(5,332)	(1,186)	303	(138,055)
Impairment loss and provisions	(104,852)	51	2	-	(104,799)
Expenses for insured cases	-	(1,167)	-	-	(1,167)
Net change in provisions	-	(1,481)	-	-	(1,481)
Other expenses	-	(172)	-	-	(172)
Operating expenses	**(236,692)**	**(8,101)**	**(1,184)**	**303**	**(245,674)**
Profit/(loss) before income tax	**205,228**	**1,034**	**163**	**1**	**206,426**
Income tax	-	(129)	(32)	-	(161)
Profit/(loss) for the year	**205,228**	**905**	**131**	**1**	**206,265**
Assets of segment	25,540,776	48,043	612	(36,659)	25,552,772
Total assets	**25,540,776**	**48,043**	**612**	**(36,659)**	**25,552,772**
Liabilities of segment	15,878,329	9,828	103	(32)	15,888,228
Total equity and guarantee fund	9,662,447	716	209	1,172	9,664,544
Total liabilities and total equity	**25,540,776**	**10,544**	**312**	**1,140**	**25,552,772**

Intra-group transactions are presented under "Unallocated"

34. Capital management

The primary objectives of the Bank's capital management are to ensure the presumptions of going concern and to respect regulatory and contracted demands imposed by creditors regarding a certain capital adequacy level.

The Bank has identified own funds as a manageable capital category.

Own funds have to be, at every moment, at least at the level of share capital or at the level that ensures that the capital adequacy ratio is at least 8%, and that is sufficient for covering capital requirements regarding business risks.

Own funds consist of original own funds (Tier 1) and additional own funds (Tier 2), and is calculated in accordance with bank regulations in the Republic of Croatia.

The Bank has determined measures for the implementation and monitoring of the capital management policy as follows:

- At the reporting date, own funds have to be at least at the level of founder's capital for the reporting period.
- The capital adequacy ratio at the reporting date has to be at the level prescribed for the banks in the Republic of Croatia as well as at the level stated within regular financial covenants determined in loan contracts and contracts with special financial institutions that HBOR has concluded as a borrower.

The calculation of the capital adequacy ratio is performed in line with the regulations prescribed for the banks in the Republic of Croatia and does not significantly differ from international banking practice.

		Group		**Bank**
	2016	**2015**	**2016**	**2015**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**
Original own funds – Tier 1	9,956,604	9,609,800	9,955,288	9,608,763
Additional own funds – Tier 2	333,571	302,203	333,571	302,203
Total own funds	**10,290,175**	**9,912,003**	**10,288,859**	**9,910,966**
Risk weighted assets	16,415,582	12,798,794	16,447,428	12,830,126
Capital requirements for currency risk	609,631	696,133	597,377	681,095
Total capital requirements	**17,025,213**	**13,494,927**	**17,044,805**	**13,511,221**
	%	**%**	**%**	**%**
Capital ratio (Tier 1)	**58.48**	**71.21**	**58.41**	**71.12**
Capital adequacy ratio	**60.44**	**73.45**	**60.36**	**73.35**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**
Own funds needed for ensuring capital adequacy according to regulatory requirements	**1,362,017**	**1,079,594**	**1,363,584**	**1,080,898**

Minimum capital adequacy ratio at the end of 2016 was 8% (31 December 2015: 8%).

34. Capital management (continued)

Due to the extensive changes in the existing support application for the Bank's operations, the Management Board has prolonged a transitional period for the implementation and testing of new applications and the use will begin with respect to the first reporting period after the implementation of the software solution for the calculation of the adequacy ratio of own funds. Until then, the capital adequacy and exposure calculations will be made in the existing manner.

The Management Board of the Group does not expect any adverse effects on the level of capital adequacy as a result of application of the new regulations for credit institutions, taking into account that the bank's capital adequacy ratio at the end of 2016 was 8 times higher than the prescribed one. This was primarily due to the model of operation and its orientation to the lending operations.

35. Earnings per share

Pursuant to the HBOR Act, the equity capital of the Bank consists of one share in the company that may not be divided, transferred or pledged and is owned solely by the Republic of Croatia.
For the purpose of calculation of earnings per share, earning is presented as net profit after taxation.

36. Events after the reporting period date

36.1. Management Board of HBOR

After the reporting period date, by the decision of the Supervisory Board of HBOR dated 25 January 2017, the President and the Members of the Management Board of HBOR were dismissed as at 31 January 2017, i.e. Dušan Tomašević was dismissed from the position of President of the Management Board, and Martina Jus and Goran Filipić were dismissed from the positions of Members of the Management Board of HBOR.

By the decision of the Supervisory Board of HBOR dated 25 January 2017, Tamara Perko, MSc was appointed President of the Management Board of HBOR and Martina Jus was appointed Member of the Management Board of HBOR with effect from 1 February 2017 until the implementation of the selection and appointment procedure for the members of the Management Board of HBOR pursuant to the Decree on the Criteria for the Implementation of the Selection and Appointment Procedures for Presidents and Members of Management Boards of Companies and other Legal Entities of Strategic and Special Interest for the Republic of Croatia (Official Gazette of the Republic of Croatia, nos. 33/16, 43/16 and 109/16), however, the duration of the appointments shall not exceed six months.

36.2. Collateral valuation

In Q2 2017, during the Asset Quality Review (AQR) of HBOR, independent assessors will reassess the collateral and the results will be stated in the semi-annual consolidated financial statements as at 30 June 2017.

Appendix - financial performance of the HKO Group
Statement of Profit or Loss and Other Comprehensive Income
for the year ended 31 December 2016

(All amounts are expressed in HRK thousand)

	2016 HRK '000	2015 HRK '000
Premium earned		
Gross premium written	11,814	12,167
Premium impairment allowance originated and reserved on collection	-	20
Gross outward reinsurance premium	(4,964)	(5,849)
Net premium written	**6,850**	**6,338**
Changes in the gross unearned premium reserve	(1,649)	(558)
Changes in the gross unearned premium reserve, reinsurer's share	480	173
Net premium earned	**5,681**	**5,953**
Fee and commission income	2,102	2,393
Net investment income	1,824	1,812
Other operating income	60	52
Net income	**9,667**	**10,210**
Gross expense for returned premiums	(1,117)	(372)
Reinsurer's share	604	200
Gross reserve for returned premiums	(2)	(588)
Reinsurer's share	(43)	238
Net expense and reserve for returned premiums	**(558)**	**(522)**
Claims incurred	(1,713)	(2,187)
Claims incurred, reinsurer's share	122	1,020
Change in the claims provision	2,253	(2,785)
Change in the claims provision, reinsurer's share	(2,174)	1,654
Net claims incurred	**(1,512)**	**(2,298)**
Marketing and provision expenses	(822)	(708)
Administrative expenses	(5,023)	(5,313)
Other operating expenses	(205)	(161)
Net exchange differences other than those on financial instruments	1	(11)
Profit before income tax	**1,548**	**1,197**
Income tax	(233)	(161)
Profit for the year	**1,315**	**1,036**
Other comprehensive income		
Items that are not transferred subsequently to profit or loss:		
Deferred tax – adjustment for previous period	-	-
Total items that are not transferred subsequently to profit or loss	-	-
Items that may be reclassified subsequently to profit or loss:		
Gains on revaluation of financial assets available for sale	2,374	1,626
Decrease in the fair value of financial assets available for sale	(562)	(1,011)
Transfer of realized gains on asset available for sale to statement of profit or loss	(236)	(405)
Deferred tax	(262)	(42)
Total items that may be reclassified subsequently to profit or loss:	**1,314**	**168**
Other comprehensive income after income tax	**1,314**	**168**
Total comprehensive income after income tax	**2,629**	**1,204**
Attributable to:		
Equity holder of the parent	2,629	1,204

Appendix - financial performance of the HKO Group

Statement of Financial Position

for the year ended 31 December 2016

(All amounts are expressed in HRK thousand)

	2016 HRK '000	2015 HRK '000
Assets		
Non-current assets		
Property and equipment	86	148
Intangible assets	5	9
Held to maturity investments	1,422	1,451
Deferred tax	54	230
Total non-current assets	**1,567**	**1,838**
Current assets		
Investments available for sale	46,459	37,993
Investments at fair value through profit or loss	286	3,707
Deposits with banks	-	3,047
Receivables from insurance operations	985	1,133
Other receivables	2,185	164
Cash and cash equivalents	551	242
Total current assets	**50,466**	**46,286**
Total assets	**52,033**	**48,124**
Equity and liabilities		
Equity		
Share capital	37,500	37,500
Accumulated losses	(148)	(1,184)
Other reserves	2,188	874
Profit for the year	1,315	1,036
Total equity	**40,855**	**38,226**
Technical provisions		
Gross technical provisions	14,225	14,827
Technical provisions, reinsurer's share	(6,419)	(8,156)
	7,806	**6,671**
Current liabilities		
Liabilities from insurance operations	1,190	1,603
Other liabilities	2,182	1,624
Total liabilities	**3,372**	**3,227**
Total equity and liabilities	**52,033**	**48,124**

Appendix - financial performance of the HKO Group
Statement of Cash Flows
for the year ended 31 December 2016
(All amounts are expressed in HRK thousand)

	2016 HRK '000	2015 HRK '000
Operating activities		
Profit before income tax	1,548	1,197
Adjustments to reconcile to net cash from and used in operating activities:		
Depreciation	70	180
Impairment loss and provisions	59	(53)
Income tax	233	161
Accrued interest	22	(139)
Operating profit before working capital changes	*1,932*	*1,346*
Changes in operating assets and liabilities:		
Net decrease in deposits with other banks	3,000	13,920
Net realized (gain) on assets available for sale	(236)	(406)
Decrease of discount in assets available for sale and assets held to maturity	406	251
Net gain on financial assets at fair value through profit or loss	(121)	(84)
Premium receivables	148	822
Net (increase) in other assets	(2,570)	(143)
Net decrease of assets and liabilities from insurance operations	(413)	(59)
Net increase in technical provisions	1,135	1,865
Net increase in other liabilities	497	69
Net cash provided by operating activities	**3,778**	**17,581**
Investment activities		
Net (purchase) of financial assets at fair value through profit or loss	(8,990)	(24,417)
Net sale of financial assets at fair value through profit or loss	12,488	22,928
Net (purchase) of assets available for sale	(9,669)	(23,903)
Net sale of assets available for sale	2,532	7,905
(Purchase) of assets held to maturity	-	-
Collection of assets held to maturity when due	-	-
Net (purchase) of property, plant and equipment and intangible assets	(3)	(50)
Net cash (used in) investment activities	**(3,642)**	**(17,537)**
Effect of foreign currency to cash and cash equivalents		
Net foreign exchange	173	65
Net effect	**173**	**65**
Net increase in cash and cash equivalents	309	109
Balance as of 1 January	242	133
Net increase in cash	309	109
Balance as of 31 December	**551**	**242**

Appendix - financial performance of the HKO Group

Statement of Changes in Equity

for the year ended 31 December 2016

(All amounts are expressed in HRK thousand)

	Share capital HRK '000	Accumulated losses HRK '000	Other reserves HRK '000	Profit/(loss) for the year HRK '000	Total equity attributable to the equity holders of the Company HRK '000	Total equity HRK '000
Balance as of 1 January 2015	**37,500**	**(2,068)**	**706**	**884**	**37,022**	**37,022**
Profit for the year	-	-	-	1,036	**1,036**	**1,036**
Other comprehensive income	-	-	168	-	**168**	**168**
Total comprehensive income	-	-	168	1,036	**1,204**	**1,204**
Transfer of profit 2014 to retained earnings	-	884	-	(884)	-	-
Balance as of 31 December 2015	**37,500**	**(1,184)**	**874**	**1,036**	**38,226**	**38,226**
Balance as of 1 January 2016	**37,500**	**(1,184)**	**874**	**1,036**	**38,226**	**38,226**
Profit for the year	-	-	-	1,315	**1,315**	**1,315**
Other comprehensive income	-	-	1,314	-	**1,314**	**1,314**
Total comprehensive income	-	-	1,314	1,315	**2,629**	**2,629**
Transfer of profit 2015 to retained earnings	-	1,036	-	(1,036)	-	-
Balance as of 31 December 2016	**37,500**	**(148)**	**2,188**	**1,315**	**40,855**	**40,855**