

Raiffeisenbank Austria d.d.

**Annual Report
for the year ended 31 December 2017**

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Macroeconomic environment

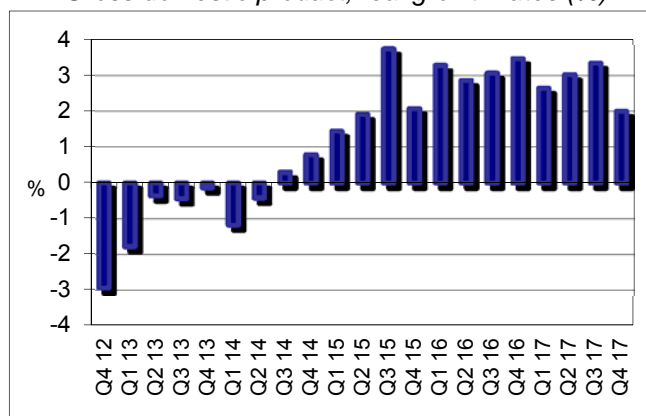
Raiffeisenbank Austria d.d. Zagreb

- Economic review

In 2017, the economy realized a real growth rate of 2.8 percent. Positive contribution to GDP growth comes from domestic demand, primarily from the increase in personal consumption, which grew by 3.6 percent year-on-year. Government consumption increased by 2.0 percent, while growth of 3.4 percent in investments in fix capital did not meet expectations. Personal income growth was positively influenced by the reduction of the income tax rate as well as the fall in interest rates on consumer loans, which facilitated the burden of debt repayments for indebted households. During the year the realization of investment slowed down due to the crisis in Agrokor, so the realized growth rate fell by two percentage points in relation to last year. The negative contribution to growth comes from foreign trade, as the solid growth in exports of goods and services by 6.1 percent is exceeded by the 8.1 percent growth of imports.

Business activities in the country were under the influence of favorable conditions in external trading partners. In the euro area, the monetary expansion has continued. In addition to the historically low levels of the core interest rate, the European Central Bank has further increased liquidity in financial markets by non-orthodox measures of purchasing securities on the secondary markets. Resulting liquidity growth increased the loan supply and maintained downward pressure on market interest rates. Over the lending channel, the European Central Bank promoted growth in consumption, investment and employment, with the aim of increasing the inflation rate up to the targeted two percent. By increasing the liquidity in the euro area, the risk aversion of investors was reduced, and supply of capital at historically low interest rates spread to markets with higher risk levels. Consequently, the price of capital for debtors in Croatia has also decreased in 2017.

Gross domestic product, real growth rates (%)



Sources: CNB, Raiffeisen research

The credit rating of the Republic of Croatia remained below the investment level in 2017, with a change in the outlook from stable to positive. In January 2018, one of three credit rating agencies (Fitch) raised the rating of the Republic of Croatia for one notch, which is not enough to reach the investment level. However, during the year, investors at financial markets made decisions on the Croatian debt prices in line with the growing optimism in assessing the state's capability to repay public debt. Hence, the Croatian government's debt price fell to the level at which countries in surrounding with the lowest investment rating are able to borrow funds. The reduced risk assessment is primarily the result of successful fiscal consolidation. In addition to regular refinancing operations, in the second half of 2017 the government refinanced part of undue debt in highway and road sector, thus used the opportunity to reduce the future financing costs of public debt.

At the beginning of the year, the largest business system in Croatia (Agrokor) lost the confidence of creditors. Expected loss of business ability has threatened for the discontinuation of supply chains between the local agricultural producers, food and other processing industries, and the retailers supplied through Agrokor wholesale network.

Macroeconomic environment (continued)

The spread of negative effects from crisis in Agrokor to the entire economy was prevented by the adoption of special law by which the management of Agrokor was taken over by a trustee appointed by the Commercial court. For the credit institutions that are creditors of Agrokor, this regulation introduced a moratorium on the collection of outstanding receivables from Agrokor companies, and procedures for enforced collection were also disabled. In expectancy of final settlement, creditors have estimated the losses in value of receivables; both from Agrokor and subordinated companies that are temporarily protected against the collection of receivables, as well as from companies that are economically dependent on Agrokor's operations. In the amount of estimated losses they made impairments and thus reduced the operating result for 2017.

Consumer price index (inflation rate), annual changes (%)



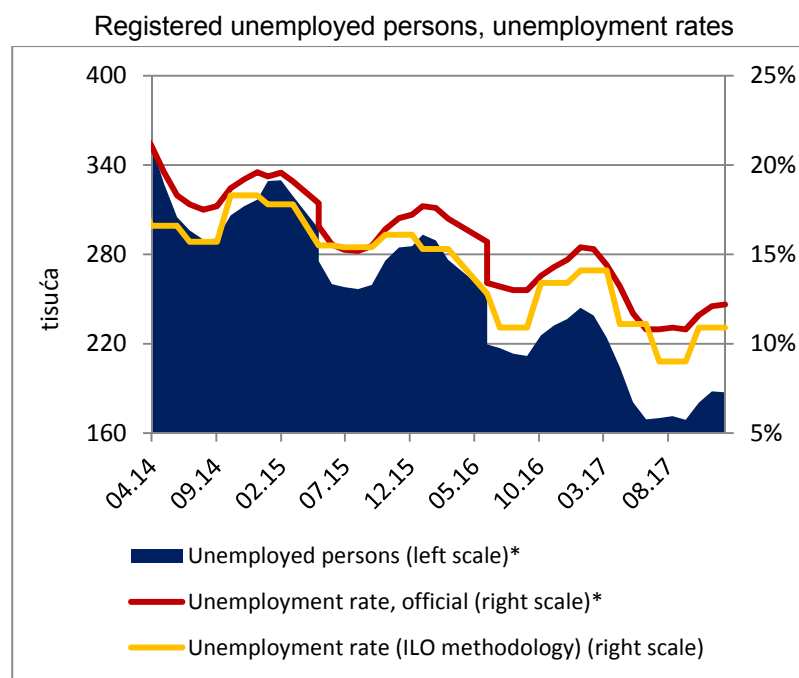
Sources: CNB, Raiffeisen RESEARCH

- Macroeconomic indicators

Over the past three years in a period period of achieving solid GDP growth rates, therowth has slowed down in 2017 due to the unfavorable impact of Agrokor crisis on business activities in the corporate segment. Solid growth was achieved on the basis of an increase in total exports and personal consumption, while investment activities slowed down due to the uncertainty about the final result in the restructuring process in Agrokor and in the settlement with its creditors. The most important component of GDP is household consumption, Stable growth rates in consumption are spilled over from the growing tourist spending to the entire economy. Growing exports of goods and services have been driven by a high level of optimism on European and regional markets. However, the relatively high imports dependence of exports results in the negative contributions of net exports to the economic growth in total.

Labor market in 2017. Was marked by continuing tendency of reducing the registered unemployment rate with the usual seasonal movements. During summer months the rate dropped to historically low 10.8 percent. By the end of central part of tourist season, the usual rise in unemployment started, with an average rate of 12.2 percent at the end of year. Seasonally adjusted data suggesting a trend of change, suggest a steady decline in unemployment rates over the year. However, changes in the rules for unemployment registration and the strengthening of emigration movements reduce the usability of unemployment rate indicators for the assessment of movement in the labor market and indicators of employment. Regardless the indicator of employment observed, according to labor market indicators Croatia is at the low level in the EU list. Labor market is burdened by the structural problems of mismatch between supply and demand, decline in the working population and the demographic aging process. Therefore, the economic growth is increasingly hampered by the shortage of labour despite the relatively high rate of unemployment.

Macroeconomic environment (continued)

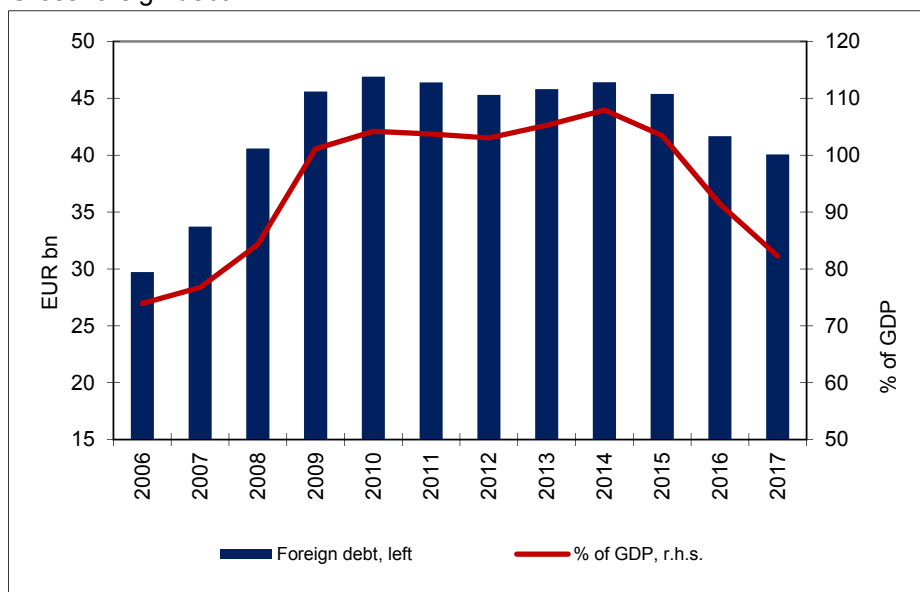


Sources: CBS, CES

* broken series as of Jan2015 (due to new CBS's methodology)

Positive movements in the balance of payments continued with a noticeable surplus on current and capital accounts. In 2017, the current account surplus was achieved at the level of 3.7 percent of GDP. Growing deficits on the goods foreign trade account is realized despite the increase in goods exports, as imports of goods grew strongly. A negative balance on the goods account was neutralized by increasing of surplus at service account. The main contribution comes from tourism revenues amounting to EUR 9.5 billion. The absorption of funds from EU funds increases the positive balance of payments balance. Additionally, in 2017, the Agrokor-linked impairments in banks have increased, with one-off negative impact on banking sector profits. Since the predominant part of banking sector is owned by non-residents, the decrease in banks' earnings had a positive impact on the primary income account as well as on the current account of balance of payments.

Gross foreign debt



Sources: CNB, Raiffeisen research

Macroeconomic environment (continued)

- Fiscal and monetary movements

In June 2017, Croatia came out of the excessive deficit procedure. The procedure started in 2014, on the basis of a deficit of -5.3 percent of GDP in 2013 and was completed in 2017 after the deficit of general government in 2016 declined to -0.9 percent. In fiscal year 2017, the consolidation process continued and a slight surplus of general government revenue growth was achieved. Thanks to the balanced budget, the growth in public debt was stopped in absolute terms, and with the growth of economy the public debt to GDP ratio fell to 82 percent.

Structurally, the public finance consolidation was achieved under favorable cyclical conditions and with minimal structural changes. On the revenue side of budget, there has been a significant increase in revenues from indirect taxes (VAT) and social contributions, which is the result of growth in business activities and employee contributions. Total revenues from direct taxes have increased due to higher income tax revenues, while revenues from income taxes were reduced in line with the tax reform.

In the structure of budget expenditure side, there were no changes linked to the unrealized implementation of structural measures. Government borrowing costs recognized through interest expense are lowered due to the general fall in market interest rates and the realized refinancing of road sector debt. Reduced investment spending stems from the slowdown in the country's investment activity. However, due to the alignment of pensions, the social security expenditures have risen. Agreement between the Government and worker unions in administration sector and the spread of that agreement to all employed persons in public services has resulted in a rise of expenses for salaries and other employee compensations.

In 2017 the monetary policy kept its expansionary character. The CNB intervened five times at foreign exchange market and with the purchase of foreign currency it neutralized the rising appreciation pressures. In addition to reduced fiscal risks and significant foreign currency inflows, the support for domestic currency has also come from a solid surplus on the current account of balance of payments, the positive net-foreign position of banks, as well as the growing demand for loans in kuna.

In autumn 2017 the Government and the CNB jointly presented the Strategy for the introduction of euro. Favorable tendencies in public finances allow for conditional fulfillment of quantitative criteria for entry into the ERM II, a kind of waiting room for entry into the Euro area. For the passing through ERM II is not enough to meet the economic criteria only, but there is also a need for qualitative improvements in economic policies as well as a positive political decision by other euro area members. Therefore, the strategy did not set deadlines for Croatia to access the Euro area. However, due to unquestionable positive effects on growth and financial stability on the one hand, and the minor potentially negative effects on prices on the other hand, the commitment to move faster to the Euro area should have a decisive impact on monetary and fiscal policy measures in the coming years.

Macroeconomic environment (continued)

Summary of macroeconomic indicators for from the years ended from 2013 to 2017

| | 2017 | 2016 | 2015 | 2014 | 2013 |
|---|--------|--------|--------|--------|--------|
| GDP & Production | | | | | |
| Gross Domestic Product, % (constant prices) | 2.8 | 3.2 | 2.3 | -0.1 | -0.6 |
| GDP at current prices (EUR millions) | 48,766 | 46,381 | 44,525 | 43,395 | 43,733 |
| GDP per capita at current prices (EUR) | 11,728 | 11,033 | 10,511 | 10,244 | 10,276 |
| Retail trade, % real annual changes | 4.7 | 4.0 | 2.4 | 0.4 | -0.5 |
| Industrial production, % annual changes | 1.4 | 5.3 | 2.7 | 1.2 | -1.8 |
| Prices, Employment and Budget | | | | | |
| Consumer Prices, %, eop | 1.2 | 0.2 | -0.6 | -0.5 | 0.3 |
| %, average | 1.1 | -1.1 | -0.5 | -0.2 | 2.2 |
| Producer Prices, %, eop | 2.1 | -0.1 | -4.4 | -3.4 | -2.6 |
| %, average | 2.1 | -4.1 | -3.9 | -2.7 | 0.5 |
| Unemployment rate (official rate, avg)* | 12.4 | 14.8 | 17.0 | 19.6 | 20.2 |
| Unemployment rate (ILO, avg) | 11.7 | 13.1 | 16.2 | 17.3 | 17.3 |
| Average net wage, in HRK* | 6,015 | 5,685 | 5,594 | 5,534 | 5,515 |
| General Government Balance, % of GDP 1 | -0.5 | -0.9 | -3.3 | -5.1 | -5.3 |
| Public debt, HRK billion 1 | 300.2 | 289.1 | 289.6 | 284.2 | 270.8 |
| Public debt, % of GDP 1 | 82.6 | 84.2 | 86.7 | 86.6 | 82.2 |
| Balance of Payment and External Debt | | | | | |
| Good's and Services Exports, EUR million | 24,958 | 22,776 | 21,472 | 19,677 | 18,768 |
| % change | 9.6 | 6.1 | 9.1 | 4.8 | 2.5 |
| Good's and Services Imports, EUR million | 23,554 | 21,429 | 20,439 | 18,849 | 18,599 |
| % change | 9.9 | 4.8 | 8.4 | 1.3 | 2.6 |
| Current Account Balance, % of GDP | 3.7 | 2.5 | 4.5 | 2.0 | 0.9 |
| Official International Reserves, EUR million, eop | 15,706 | 13,514 | 13,707 | 12,688 | 12,908 |
| Official International Reserves, in terms of months of imports of goods and services, eop | 8.0 | 7.6 | 8.0 | 8.1 | 8.3 |
| Foreign Direct Investment, EUR million 2 | 1,750 | 1,699 | 189 | 2,297 | 737 |
| Tourism - nightstays, % change | 10.6 | 9.1 | 7.8 | 2.6 | 3.4 |
| External debt, EUR billion | 40.3 | 41.7 | 45.4 | 46.4 | 45.8 |
| External debt, as % of GDP | 82.6 | 89.8 | 101.9 | 106.9 | 104.7 |
| External debt, as % export of goods and services | 161.5 | 182.9 | 211.4 | 235.9 | 244.1 |
| Monetary and Financial Data | | | | | |
| Exchange rate, eop, USD / HRK | 6.36 | 7.17 | 6.99 | 6.30 | 5.55 |
| avg, USD / HRK | 6.54 | 6.80 | 6.86 | 5.75 | 5.71 |
| Exchange rate, eop, EUR / HRK | 7.50 | 7.56 | 7.64 | 7.66 | 7.64 |
| avg, EUR / HRK | 7.45 | 7.53 | 7.61 | 7.63 | 7.57 |
| Money (M1), HRK billion, eop | 99.4 | 83.5 | 70.6 | 63.4 | 57.9 |
| % change | 19.1 | 18.2 | 11.4 | 9.6 | 11.5 |
| Broadest money (M4), HRK billion, eop | 307.2 | 300.9 | 287.3 | 273.2 | 264.8 |
| % change | 2.1 | 4.7 | 5.2 | 3.2 | 4.0 |
| Credits, HRK billion | 219.4 | 221.5 | 230.0 | 237.0 | 240.8 |
| % change | -0.9 | -3.7 | -3.0 | -1.6 | -0.5 |
| ZIBOR 3m, %, avg | 0.6 | 0.9 | 1.2 | 1.0 | 1.5 |
| Treasury bills rate 12m, %, avg | 0.4 | 0.9 | 1.4 | 1.9 | 2.5 |

1 according to the ESA 2010 methodology

2 including round-tripping

eop - end of period; pa - period average

* series broken as of January 2015 (new CBS's methodology)

Values marked red are estimates made by RBA research (final data is unavailable)

Source: Croatian National Bank, Ministry of Finance, Croatian Bureau of Statistics

Management report

1. Market position

The Bank and members of local group are registered for operations in the Republic of Croatia. The Bank is a fourth ranked credit institution at local market with the significant market share per total assets at the end of 2017. Raiffeisen Stambena Štedionica is a credit institution licensed for providing services defined by special regulations. It is subordinated to the Bank and has significant role at the local housing market. The Bank also has subordinate financial institutions for leasing and factoring, and investment and pension management companies. These subordinate financial institutions are significant for the local market, while Raiffeisen Pension Insurance Company is the only registered for this activity at local market.

Operation results of the Bank and the Group are dependent on the business conditions that prevails at financial markets and processes in the real economy. Assets under management of investment and pension funds increased in 2017 due to the growth in value of debt and equity investments. The real economic growth and the high liquidity in financial sector have improved the collection of due receivables, which has had a positive impact on the operation results of credit institutions and financial institutions that offer loan substitutes.

The beginning of the year was marked by a crisis in Agrokor, a company that has the largest domestic retailer chain (Konzum). Directly or indirectly through this retailer is realized a significant part of production in domestic companies, mostly from the suppliers in agricultural sector and food&beverages industry. Agrokor's inability to finance further business operations has jeopardized the survival of economically-dependent companies and amplified the threat of spreading the negative effects on economy as a whole. Therefore, in the urgent parliamentary procedure, the Law on Extraordinary Administration Procedure in Companies of Systemic Importance for the Republic of Croatia was adopted. On the basis of that act the Government of the Republic of Croatia proposed, and the Commercial Court in Zagreb appointed an extraordinary commissioner for Agrokor. The Commercial Court prohibited the initiation and management of any civil, enforcement, administrative and insurance proceedings against Agrokor and its 24 affiliated and subsidiary companies in Croatia, thereby enabling the continuity of operations in Agrokor and their companies. On April 10, the Commissioner took over the management of the Group and conducted a financial restructuring of the Group, which could last for a maximum of 15 months. In that period, Agrokor should achieve an agreement with creditors and enable further business operations for all members of the group without the risk of forced collection of receivables being initiated after the extraordinary administration procedure.

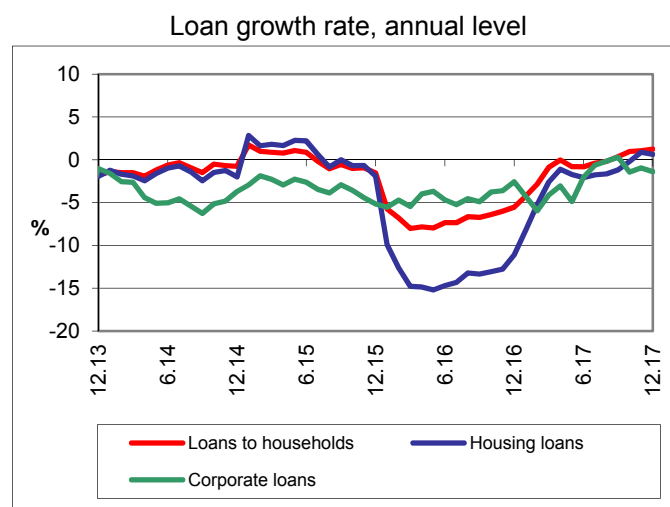
At the end of first half 2017, the CNB as regulator requested the banks to form the loss provisions at least at the 50 percent of the exposure to Agrokor and subordinated companies. In addition, banks have been asked to form loss provisions to companies that are significantly dependent of Agrokor. In this way, Agrokor's suppliers were included in the assessment of losses. But, following the suspension of the forced collection of claims from Agrokor, the supplier companies continued to operate unprotected from the proceedings of their creditors. As a result, part of the suppliers could not continue the business and thus initiated bankruptcy or prebankruptcy proceedings. In the second half of year, the Commissioner published to creditors the additional information about the prospects for collecting receivables from Agrokor. Based on this information the creditors reestimated losses on receivables and, in line with these estimates, formed additional loss provisions.

In previous period Agrokor significantly increased the debt to suppliers due to extended payment deadlines for the delivered goods and services, so, the suppliers have offered Agrokor's receivables to the financial institutions for redemption. This resulted in significant demand for factoring services. Consequently, the share of Agrokor debt in the overall operations in factoring companies has significantly increased. After the introduction of extraordinary commissioner, the collection of

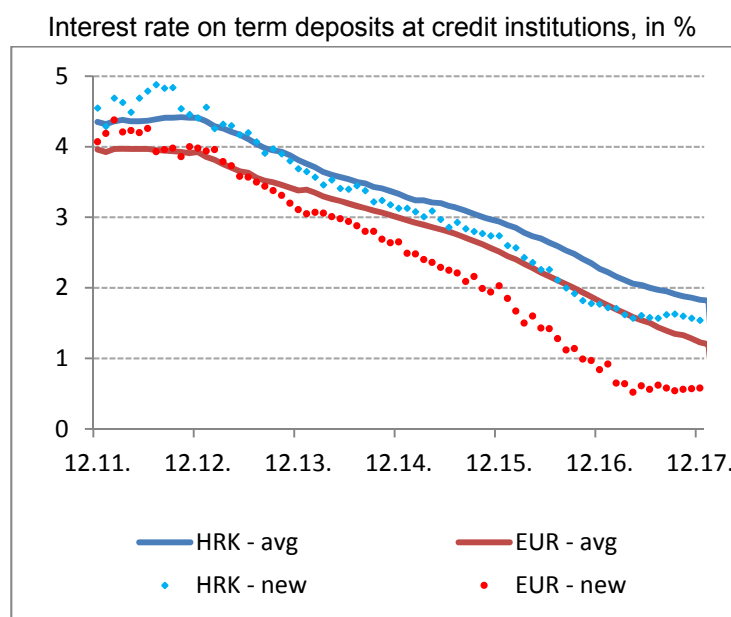
Agrokor's receivables was suspended, as well as contracting new transactions between Agrokor, suppliers and factoring companies. As a result, total assets of factoring companies declined sharply and by the end of year fell to less than half of assets at the beginning of year. It turns out that the problems in Agrokor's business affected factoring companies the most. In banks, one-off loss provisions related to Agrokor have increased, which reduced the operating result in 2017, but did not significantly affect the total loans portfolio.

Management report (continued)

1. Market position (continued)



Sources: CNB, Raiffeisen research



Source: CNB

Additional provision for exposure to Agrokor and related companies represents a one-off breakdown in the general positive trend in credit risk mitigation that has been present on the Croatian financial market over the last three years. The annual expenses from loss provisions increased 50 percent compared to the previous year due to the formation of additional loss provisions on loans related to Agrokor. Consequently, aggregated profits of credit institutions in 2017 after taxation amounted to HRK 3.6 billion, which is 29 percent lower on the year-on-year basis.

Along with the negative impact of the crisis in Agrokor, the operating conditions of the Croatian financial market in 2017 were marked by the high liquidity in financial sector. Inflation was subdued by demand-side developments, and excess liquidity has exacerbated pressure on capital prices. Money market interest rates have fallen to the historically lowest level. Consequently, interest rates were lowered, first on money market, followed by deposits, and finally on loans, which had a positive effect on the companies and households disposable income and their capability for investment and consumption. Consequently, the debtors ability to settle loan obligations has improved.

Management report (continued)

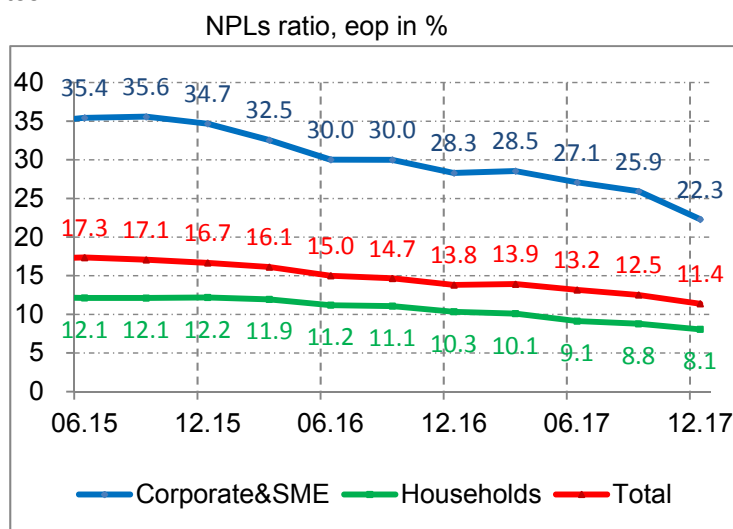
1. Market position (continued)

The excess of the deposit supply was reflected in interest yields. On demand deposits, banks have not offered interest yields for years. On new long-term deposits in euros at the end of 2017, offered annual yields were less than half a percent. Clients' motivation to contract term deposits depends on the offered returns, ie interest rates. After expiration of term deposit period, clients prefer the holding of funds on demand accounts rather than the contracting a new term deposit. Consequently, during 2017 the share of time deposits in total customers deposits in banks decreased by 7.6 percentage points, and at the end of the year has fallen to 51.6 percent.

Changes in the maturity structure of deposit also reflect to the currency structure. Deposits in foreign currency prevail in the total time deposits. Although their participation is gradually decreasing, at the end of year they still had a significant 78 percent of total time deposits. However, in the case of demand deposits, the participation of kuna deposits is over a half. Due to the uneven currency structure in time deposits and demand deposits, the reduction of time deposits participation in total deposits results and the increase in the share of kuna deposits in total.

Changes in the currency structure of deposits correspond to changes in demand for loans, as the growth of kuna deposits supports the increased demand for loans in kuna. However, in the conditions of historically low interest rates on loans, demand for longer maturity and fixed interest rates has increased. For clients it is a tool to fix low-cost financing in the later phase of loan repayments when they expect an increase in market interest rates. The increased usage of long-term kuna loans with fixed interest rates (in the initial repayment period or till maturity) results in the spread of the gap in the maturity structure in banks' balance sheet due to the simultaneous reduction of average maturity on the financing sources.

The expected normalization of monetary policy in the euro area after reaching the target inflation level could result in an increase in the core interest rate. As a result, the local ranking regulator (CNB) at the end of September published Recommendations for reducing interest rate risk for consumers and interest-induced credit risk for banks, that arises from long-term consumer lending with contracted variable interest rates. The regulator recommends that banks settle fixed interest rates with consumers on long-term loans, especially for loans with a maturity of more than seven years. However, the difference between the fixed interest rates in relation to the variable is growing rapidly with an increase in the repayment period. Therefore, borrowers with a debt maturity of more than seven years decide mainly to contract a variable interest rate. In the initial period of loan repayment, while the interest rate risk is still low, they use temporary fixed interest rates. After the contractual protection period expired, loan users could face a significant increase in repayment rate if the market interest rates increase in the meantime. The choice of consumers depends on the price and risk ratio, and CNB's recommendations did not affect the structure of consumer demand for loans according to the criterion of contracted interest rates.



Source: CNB

Management report (continued)

1. Market position (continued)

On the funding side, the fall in interest rates did not result in significant outflows of deposits from banks to investments that could achieve higher levels of yield. Namely, the tendency of falling market interest rates has also affected the narrowing of yield on investments. This reduced the attractiveness of alternative types of investment, so banks' deposits did not decrease. On the other hand, the crisis in Agrokor slowed down the recovery of credit activity started a year earlier. After the appointment of an extraordinary commissioner, the credit growth continued. At the same time, banks accelerated the clearing of the loan portfolio through the collection of receivables. In addition to settlement with debtors, the sale of non-performing loans (NPLs) to the companies specializing in the collection of receivables increased. In 2017, a total of HRK 8,392 million was sold. Realized sales had a negative impact on the level of total loans in the balance sheets of credit institutions, but at the same time accelerated the reduction in the non-performing loans ratio to total loans. At the end of 2017, the non-performing loans ratio of dropped to 11.4 percent, which is 2.4 percentage points lower than a year ago.

The increase of customer deposits in relation to loans has enabled banks to reduce secondary funding sources. The resulting sufficiency of primary sources for financing lending operations results in a reduction in capital prices on domestic financial markets, as the dependence of capital cost on the domestic financial market risk premium has lowered. Consequently, banks could offer to high ranked-clients the loan at prices below the government's borrowing price with the same maturity. This has allowed the banks to transfer favorable conditions from the financial markets to the real economy and to accelerate the fall in interest rates on corporate loans.

At the households segment the demand for loans and the preference for savings depend on the real income growth and the expected value of citizen assets. The real burden of loan repayments fell due to lower interest rates on loans, while real income was increased due to reduction in income tax. Positive shifts in disposable income increase the demand for loans, but in 2017 the positive growth in total amount of household loans was recorded only in the last quarter.

Banking system is significantly exposed to the risk of the Republic of Croatia. Factors of a high level of government risk in bank assets are rising from the direct or indirect state borrowing on the domestic financial market, but also from the regulation by which the central bank maintains financial stability. Additional factors of state risk exposure are the excess liquidity held by banks on the CNB's accounts and the investing activity in debt instruments of the Republic of Croatia, direct state borrowing from banks and other financial institutions, and state guarantees for loans used by public or private companies. Based on the reserve requirement, the banks keep a part of liquid assets on the accounts with the Croatian National Bank. By the end of 2017, the required reserve amounted to 12 percent of the bank's liabilities. The CNB does not pay any interest on the required reserve assets.

Bank's credit policy was slightly relaxed last year, in line with changed conditions at the financial markets. Market conditions enhanced the realization of credit policy goals, as the average risk in corporate sector was reduced, and the economic growth took place. In the households segment, the long-term trend of falling employment has been stopped and real wages have increased. Quality of the loan portfolio in households segment is better than in corporate. With the exception of problems in Agrokor, the favorable business movements reduce the credit risks in corporate segment.

Management report (continued)

2. Business activities of the Bank

Raiffeisenbank Austria d.d. Zagreb was registered in December 1994, as the first bank in Croatia to have been founded by foreign capital. Its business strategy is focused on developing and offering its customers a comprehensive range of financial services. Along with the expansion of its branch network, since 1999, Raiffeisenbank Austria has established financial service companies for the fields governed by special regulations (the local Raiffeisen Group). At the end of 2017, Raiffeisenbank Austria served customers via 68 branches, 438 ATMs in its own network and 703 ATMs from Euronet network and over 7,000 thousand POS devices contracted with merchants in Croatia and through additional digital sales channels.

To achieve its vision of a comprehensive range of products and services, Raiffeisenbank Austria has often led the way in the development of the Croatian financial market. Since its founding, it has developed through organic growth – initially by increasing sales of banking products and services, and then by setting up subsidiary companies specializing in specific financial services.

In the period leading to the incorporation of the Croatian banking system into the European banking union, in which all European banks operate under common rules and a single supervisor, Raiffeisenbank Austria operated in accordance with the rules of the local regulators for supervising the operations of credit institutions (Croatian National Bank) and for supervising financial services (Croatian Financial Services Supervisory Agency). All members of the local Raiffeisen Group are registered in Croatia and operate under Croatian regulations.

Raiffeisenbank Austria has been adjusting to market changes and customer demand for financial service since the time it was founded. Since 2010, it has implemented the recognized Lean corporate culture of business process improvement, aimed at achieving the highest level of excellence and customer service value, while simultaneously increasing internal efficiency. The strategic goal is to increase customer satisfaction, achieved through dynamic organization development, service quality improvement, teamwork and employee motivation.

At the end of the year, Raiffeisenbank Austria had 2,011 employees, 41 fewer than in the previous year. The number and structure of employees are defined by long-term strategic planning, and have been aligned with regulatory demands and business plans. Raiffeisenbank Austria is managed by the Management Board, consisting of six members.

3. Financial result of the Bank

Total assets at the end of 2017 amount to HRK 31,379 million for the Bank stand alone. As compared to the previous period, it decreased by HRK 37 million. At the customer loans is realized growth of HRK 240 million, while liquid assets decreased by HRK 307 million. Total amount or composition of assets has not changed significantly. The share of liquid assets in total assets is maintained at 43 percent and the share of loans to customers at 52 percent.

Total loans to customers amounted to HRK 16,453 million at the end of year. On an annual basis, they increased by 1 percent. Credit growth in the corporate segment was negatively affected by the crisis in Agrokor in the first half, which spread through economically dependent companies to a significant part of the economy. In the retail segment, demand for loans also slowed down due to the announced state subsidies for housing loans, so potential users of subsidies delayed their borrowing decisions. In the second part of year the uncertainty surrounding the survival of the business operations in Agrokor Group was reduced and consequently the credit activity in the business segment has increased. Realization of housing loans with state subsidies has began in October. To all debtors who meet the prescribed criteria and procedures for the usage of state subsidies, a state would pay back a half of instalment during the first four years of loan repayment.

In the households segment, the change in the currency structure of loan portfolio started three years ago. Loans linked to foreign currency are predominantly linked to the euro. At the same time, new clients are dominantly using loans in kuna, and consequently the share of kuna-denominated loans is rising, wherever the share of euro-denominated loans is decreasing. Loans denominated in foreign currency declined by 11 percent in the annual period while kuna loans increased by 7 percent. By the end of year, kuna loans reached 61 percent of total household loans.

Management report (continued)

3. Financial result of the Bank (continued)

In the households segment the demand for hedge against the interest rate risk has increased. Demanded hedges are offered through loans with fixed interest rates. For consumer loans offered with a repayment period of two to seven years, clients contract loans with interest rates fixed until the maturity. However, in the case of housing loans with a longer repayment period, the use of variable rate loans continues to prevail. Favorable pricing for the hedge of interest rate risk motivated clients to contract a temporary fixed interest rate in the initial period of repayment, up to a maximum of seven years.

In the corporate segment the long-term tendency to reduce the share of foreign currency loans in total loan portfolios has been halted. Last year, foreign currency loans increased by 8 percent, and the share of kuna loans fell to 27 percent of total corporate loans. In the second half-year was achieved the growth of loans in parallel with the realization of the sale of part of the nonperforming loans.

Total customer deposits fell by HRK 265 million in 2017. As a result, corporate and other non-credit company deposits fell by 3 percent, while deposits of households remained at the same level. Deposits at the end of the year amounted to HRK 13,203 million, with a share of 49 percent in the total Bank's liabilities. In conditions of constant liquidity surplus, the Bank reduced its yields on time deposits, which downed the customer motivation to contract the term deposits. Consequently, after the annual decline in time deposits by 16 percent, their share in total deposits fell to 55 percent.

Total capital and reserves of HRK 4,458 million remained at the same level as at the beginning of year. At the end of year, the capital adequacy ratio for the Bank stand alone was 22.48 percent.

Bank financial highlights for the period from 2013 to 2017

| | Bank 2017 HRK million | Bank 2016 HRK million | Bank 2015 HRK million | Bank 2014 HRK million | Bank 2013 HRK million |
|--|-----------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| From Balance Sheet as at 31 December | | | | | |
| Total assets | 31,379 | 31,416 | 31,181 | 31,419 | 33,005 |
| Shareholders' equity | 4,458 | 4,450 | 4,014 | 4,827 | 5,343 |
| Customer accounts | 23,020 | 23,285 | 22,964 | 22,698 | 21,914 |
| Loans to customer | 16,453 | 16,213 | 17,387 | 19,035 | 22,090 |
| From Income Statement for the year ended 31 December | | | | | |
| Operating income | 1,439 | 1,557 | 1,448 | 1,604 | 1,614 |
| Operating expenses | 1,105 | 1,481 | 822 | 853 | 835 |
| Profit before tax | 475 | 585 | (311) | 364 | 327 |
| Net profit for the year | 396 | 460 | (241) | 294 | 276 |
| Ratios | % | % | % | % | % |
| Return on average shareholders' funds | 9.74 | 11.46 | (5.75) | 6.48 | 5.09 |
| Return on average assets | 1.26 | 1.47 | (0.77) | 0.91 | 0.81 |
| Capital adequacy ratio (in accordance with the Croatian National Bank methodology) | 22.48 | 22.18 | 21.13 | 21.33 | 18.73 |
| | HRK | HRK | HRK | HRK | HRK |
| Earnings per share | 109 | 127 | (66) | 81 | 76 |

Management report (continued)

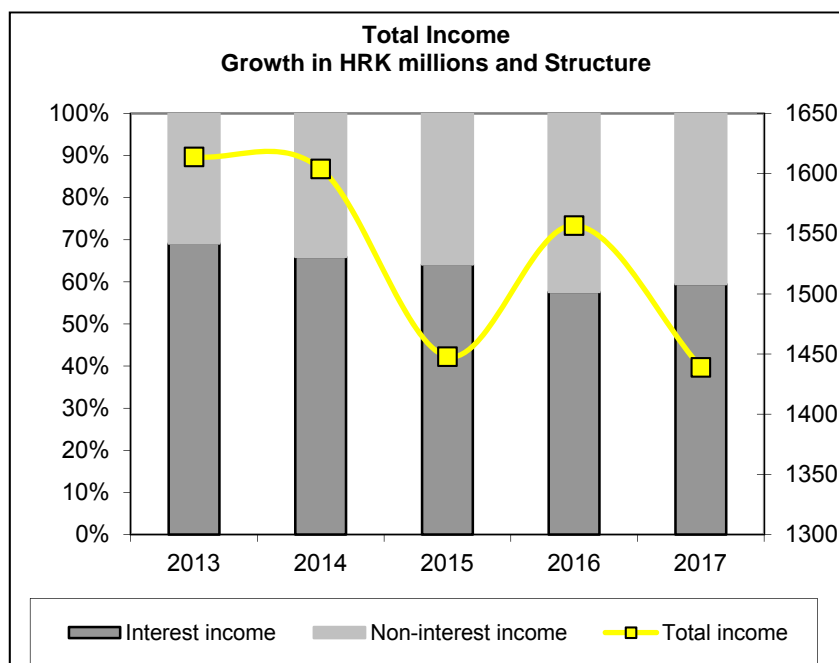
3. Financial result of the Bank (continued)

In 2017, the Bank realized profit after taxation of HRK 396 million. As the high liquidity prevailed at the financial markets, the resulting reduction in interest rates motivated the Bank to decrease contracted interest rates on the assets side but also on the liabilities side. The fall in yield on debt investments has enabled the positive gains on revaluation of portfolio that is valued at market prices.

Net interest income declined by 5 percent year-on-year due to falling interest rates on loans and debt instruments. Net income from fees increased by 4 percent, while net income from trading in financial instruments and other income decreased by 25 percent. The one-off negative impact on the business result was revaluation of shares in the subordinated company Raiffeisen Factoring, which due to exposure to Agrokor subsidiary companies and to Agrokor economically-dependent suppliers suffered significant operating losses.

Total operating expenses amounted to HRK 1,105 million, down by 25 percent year-on-year. However, a significant impact on operating costs had one-off costs. In the base period the cost of conversion amounted to HRK 655 million. In the current period the cost related to decrease of value of investments in subordinates in the amount of HRK 268 million is result of the loss realized in the company Raiffeisen Factoring. If one-time impacts are excluded on costs in both periods, total regular operating costs have been up year-on-year as the same rate as the inflation - one percent. Personnel costs increased by three percent, while material and other administrative costs fell by one percent.

Deposit insurance premiums are calculated on the basis of insured deposits amount. But, the premium rate depends on the Bank's risk profile. Realized changes in the Bank's assets enabled the reduction of premium liability for deposit insurance and the cost of establishing a banks' resolution fund. Compared with the previous year, premiums were down by 5 percent.



Based on the risks costs result, the Bank made a positive contribution to the business result in the amount of HRK 141 million. Risk provision expenses are reduced under the favorable impact of the economic recovery. In the conditions of excess liquidity the positive impact spills to improve the collection of receivables. The growth in demand on real estate market enables the realization of gains from the sale of property previously taken over for the collection of placements secured by pledge on property. In addition, part of the nonperforming loans portfolio was sold to agencies specialized in the collection of receivables. In accordance with the restrictive rules for classifying risk exposures, significant impairment of NPLs was formed in the previous three years. Therefore, the gain on the transaction of selling non-performing loans was realized on the basis of difference between the amount realized and the carrying value of the assets sold.

Management report (continued)

4. Business development of the Bank

The founder of Raiffeisenbank Austria d.d. is Raiffeisen Bank International (RBI), an Austrian banking group managing a network of banks and related financial institutions in the region of Central and Eastern Europe (CEE). Membership of a powerful international banking group with a broad range of financial services allows the transfer of experience from many years of operations in developed financial markets and developing markets. Positive synergy effects are created when introducing more advanced operational support and in setting high quality standards when working with customers, thus enhancing the product range and encouraging innovation among employees.

Along with the activities aimed at increasing operating income, the business development also includes measures to improve work productivity and safety standards, technological improvements and further develop the business process management. All professional, organizational and technological resources available are focused on increasing service quality and reducing unit costs per transaction. Investment in technology and the development of business processes forms the basis of Raiffeisenbank Austria's innovative product range and the development of financial services that are responsive to customer demand.

The priorities of the development function include enhanced functionality of the support system for the purpose of compliance with regulatory changes in the operation of credit and other financial institutions. Additional improvements are made in order to align business processes within the affiliated international financial group (RBI), as well as regarding the competitiveness of the local market offer.

The economic growth accelerated in 2017. Positive changes in market conditions reduced the level of customer risk aversion. However, the restrictiveness of the credit policies of other banks operating in the local market was also loosened. Raiffeisenbank Austria d.d. is expecting further growth of demand for kuna loans in the future, so it will focus its efforts on strengthening the primary sources of funding for kuna financing in order to efficiently manage risks.

Other strategic goals in the business development include the introduction of innovative sales channels for not only the standard, but also new types of services created on digital platforms. Thus, the Bank and the local Group are adjusting to customer demands, while taking due care to maintain a high level of service quality and security in customer transactions.

5. Events after the end of the financial year

In 2018, the application of improved financial reporting standards (IFRS9) has begun [to have](#) an impact on asset valuation. The application of the new standard does not significantly affect the capital adequacy of the Bank.

6. Research and development activities

In 2017, the Bank worked on improving its business processes and support, but did not participate in any research and development activities. It maintained its position among the leading financial institutions with regard to the application of modern technologies in their approach to the customers.

7. Information on repurchase of own shares

The Bank did not repurchase its own shares in 2017.

8. Bank subsidiaries

The Bank commenced operations on the Croatian financial market in December 1994, when it founded a universal commercial bank. Since 1999, it has developed its local Group of subsidiary legal entities. The Group's developmental goal is to offer its customers a comprehensive financial service.

Management report (continued)

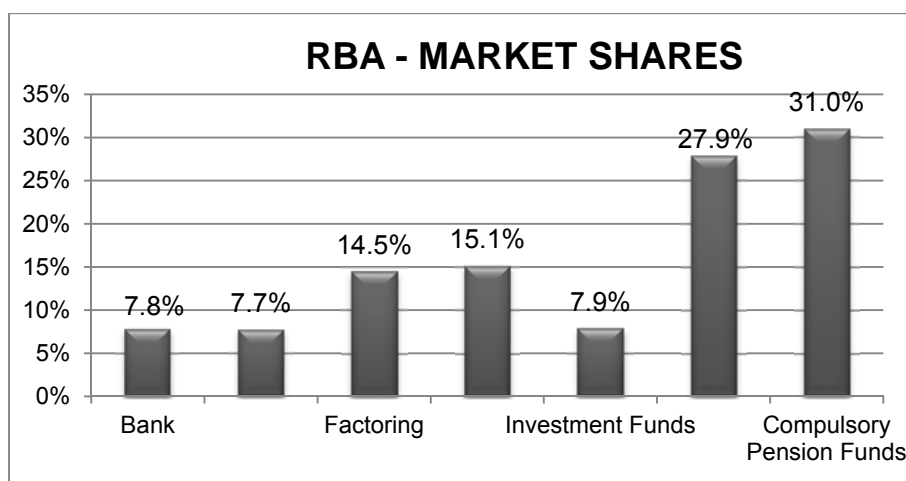
8. Bank subsidiaries (continued)

At the end of 2017, the local Group consisted of the following legal entities, which are 100% owned by the Bank:

- Raiffeisen stambena štedionica d.d. (building society).
- Raiffeisen društvo za upravljanje obveznim i dobrovoljnim mirovinskim fondovima d.d. Raiffeisen mirovinsko osiguravajuće društvo d.d. (pension insurance company)
- Raiffeisen Invest d.o.o.
- Raiffeisen Factoring d.o.o.
- Raiffeisen Leasing d.o.o.
- Raiffeisen Consulting d.o.o.

During the year, the Bank carried out a recapitalization of the subsidiary Raiffeisen Factoring totaling HRK 255 million. The total value of the Bank's investment after recapitalization increased from the initial HRK 15 million to HRK 270 million. Due to the losses incurred in the subsidiary's operations, the Bank has carried out an impairment loss of HRK 268 million and the remaining value of the investment after the adjustment amounts to HRK 2 million.

At the end of 2017, Group assets totaled HRK 34,178 million and decreased annually by 3 percent on annual level. In the structure of assets, loans to customers were reduced by HRK 759 million, while liquid assets decreased by HRK 241 million.



Decrease in Group assets was primarily due to the fall in the business activities of subsidiary company Raiffeisen Factoring. Until 2017, factoring services on the local market developed mainly for the purchase of invoices and bills of exchange from companies that were suppliers to Agrokor Group. After the appointment of the Extraordinary Commissioner for Agrokor, the way of financing the Agrokor's business has changed. New orders have been funded from new credit lines with a privileged repayment status. Receivables based on the invoices and bills of exchange of Agrokor and its suppliers that were made prior to the appointment of the Commissioner have become uncollectible until the moratorium is terminated, after which they will be collected with significant impairment. Consequently, Raiffeisen Factoring faced two problems simultaneously: reducing the market for factoring services and significant asset loss. On annual basis the assets decreased by 74 percent.

At the end of 2017, the assets under management in the three compulsory pension funds amounted to HRK 28,506 million, and in one open and six closed voluntary pension funds an additional HRK 1,329 million. In the structure of pension fund assets under the management of company, 96 percent refers to the assets of compulsory pension funds. The number of members at Raiffeisen Pension Funds at year-end was as follows: 556 thousand in compulsory and 73 thousand in voluntary pension funds. The annual growth of assets under management of 11 percent is based on contributions paid by fund members and on fund returns.

Management report (continued)

8. Bank subsidiaries (continued)

Assets in investment funds decreased by 13 percent and amounted to HRK 1,460 million at the end of year. Historically low interest rates on the money market have lowered the attractiveness of investment into cash funds that invest assets in short-term debt instruments. During the year, yields on investments in long-term debt securities were also reduced, which reduced interest in investing in bond funds. The crisis in Agrokor had a negative impact on stock prices on the local market, so there was a fall in interest in investing in equity funds. Consequently, the interest of clients for investments in investment funds managed by Raiffeisen Invest decreased.

Building societies are credit institution specialized in the offering special purpose savings and housing loans. These are long-term savings with state subsidies and a fixed-rate housing loan. Customer interest in housing savings and loans depends on the alternative market offer and state subsidies for housing savings. State subsidies are calculated on the basis of realized market interest rates. Due to the fall in interest rates, the level of state subsidies decreases. For 2015, they accounted for 4.9 percent of the savings realized in the accounting year, by 2016, down to 4.1 percent, and by 2017 to 3.3 percent. On the housing loans, the attractiveness of loans in banks offered to customers is strengthening. Banks are offering fixed-term housing loans with the possibility of using state subsidy programs. Consequently, the attractiveness of loans in building societies was reduced, resulting in Raiffeisen stambena štedionica assets fall by 3 percent on yearly basis.

Raiffeisen Group financial highlights for the period from 2013 to 2017

| | Group 2017 HRK million | Group 2016 HRK million | Group 2015 HRK million | Group 2014 HRK million | Group 2013 HRK million |
|--|------------------------------|------------------------------|------------------------------|------------------------------|------------------------------|
| From Balance Sheet as at 31 December | | | | | |
| Total assets | 34,178 | 35,364 | 35,058 | 35,887 | 36,152 |
| Shareholders' equity | 4,685 | 4,890 | 4,394 | 5,052 | 5,467 |
| Customer accounts | 23,780 | 24,144 | 23,640 | 23,527 | 21,672 |
| Customer loans | 17,745 | 18,504 | 19,626 | 21,780 | 23,812 |
| From Income Statement for the year ended 31 December | | | | | |
| Operating income | 1,874 | 2,062 | 1,990 | 2,158 | 2,106 |
| Operating expenses | 1,212 | 1,877 | 1,231 | 1,286 | 1,230 |
| Profit before tax | 290 | 695 | (182) | 465 | 384 |
| Net profit for the year | 188 | 535 | (150) | 364 | 295 |
| Ratios | % | % | % | % | % |
| Return on average shareholders' funds | 3.84 | 12.17 | (3.35) | 6.94 | 5.85 |
| Return on average assets | 0.54 | 1.52 | (0.42) | 1.01 | 0.79 |
| Capital adequacy ratio (in accordance with the Croatian National Bank methodology) | 20.48 | 20.19 | 19.30 | 18.87 | 17.66 |
| | HRK | HRK | HRK | HRK | HRK |
| Earnings per share | 52 | 147 | (43) | 100 | 85 |

Management report (continued)

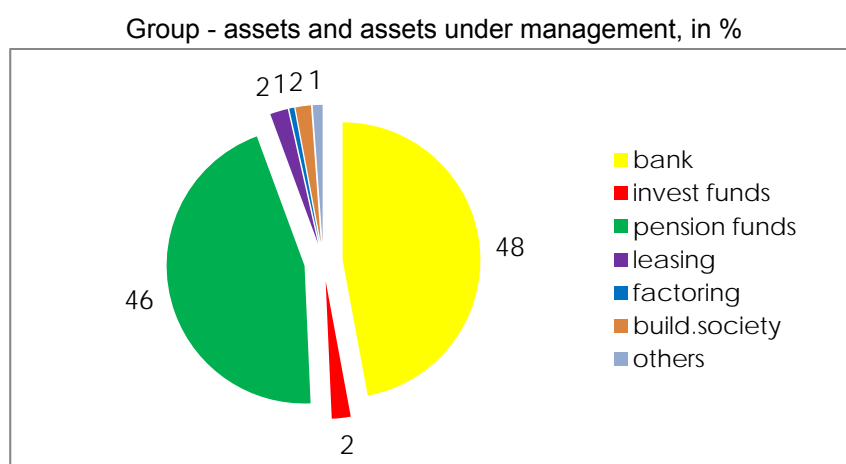
8. Bank subsidiaries (continued)

In 2017, total Group liabilities decreased by HRK 981 million. The share of customer deposits in the Group's total liabilities is 81 percent and the share of secondary funding sources decreased to 15 percent of total liabilities. Borrowed funds have been partially repaid to banks in the RBI group and to other banks. Borrowings at the end of year amounted to HRK 2,752 million, while deposits with banks amounted to HRK 1,056 million. Total customer deposits amounted to HRK 23,780 million. As a result, the share of households' deposits in total liabilities is 48 percent. At the end of 2017, the Group capital amounted to HRK 4,685 million, and the capital adequacy indicator remained at almost the same level.

The Group ended 2017 with a profit for after tax of HRK 188 million. Positive results were achieved by the Bank and all other Group members except Raiffeisen Factoring. Within the Group, Raiffeisen Pension Company achieved a significant profit. A solid business result was achieved by Raiffeisen Building Society, while Raiffeisen leasing, Raiffeisen Pension Insurance Company, Raiffeisen Invest and Raiffeisen Consulting, produced immaterial contribution to the Group's result.

Net interest income of the Group amounted to HRK 913 million, which is 8 percent less than last year. At the Group level, the negative impact on net interest income was due to the decrease in loans and other assets for which interest income was accounted for. Net fee and commission income amounted to HRK 469 million; on annual basis increased by 7 percent. Fee income is the basic income of the Group's members who manage the assets of pension and investment funds. The largest non-bank segment revenues are realized from compulsory pension funds management. Increase in pension funds' assets is based on realized contributions and yields that expand the base for calculating fund manager remuneration. The level of management compensation for mandatory pension funds is determined by the regulator. In 2017, management fee was 0.39%, while in the previous year it was 0.419%. Reducing the rate for the compensation calculation neutralizes the positive contribution of the increased base on the company's revenue.

Other non-interest income amounted to HRK 492 million, down 23 percent compared to the previous period. On trading income, profit amounted to HRK 192 million and other operating income HRK 300 million. Trading gains were generated by the increase in the value of financial assets that are valued at market prices and on the sale of assets. Other income includes operating lease rental income of HRK 95 million and gross premiums written on pension insurance amounting to HRK 151 million.



The Group realized the total revenues of HRK 1,874 million. Compared to previous year revenues decreased by HRK 188 million. Operating expenses amounted to HRK 1,122 million, of which the administrative expenses of technical provisions for pension insurance amounted to HRK 137 million, and an additional HRK 38 million for the cost increase.

Management report (continued)

8. Bank subsidiaries (continued)

If one-off conversion costs are excluded in the base period, then the operating costs decreased in relation to the previous year by 1 percent. Operating expenses account for 65 percent of Group's total revenue.

The Group realized impairment loss of HRK 386 million. The negative result was recorded at the value of receivables at Raiffeisen Factoring, where one-off adverse impacts resulting from the restructuring process of Agrokor resulted in a decrease in asset value by HRK 510 million. There was a positive result on the collection of unanticipated loans at the Bank. In total the Group achieved a positive business result of HRK 188 million. Compared to previous year, the result was reduced by 65 percent.

9. Financial instruments and related risks

Raiffeisenbank Austria and the local Raiffeisen Group invest assets into financial instruments, thus exposing themselves to risks. Risk management is the responsibility of the Bank's Management Board, while its operational implementation is the task of the organizational unit in charge of risk management and risk control. As at 31 December 2017, Raiffeisenbank Austria's assets were invested in different financial instruments, with customer loans and debt securities having a major share.

The most significant types of financial risks to which Raiffeisenbank Austria and the local Raiffeisen Group are exposed are credit risk, liquidity risk and market risk. Market risk includes exchange rate risk, interest rate risk and equities price risk.

At the Group level, there is a comprehensive risk management system of policy and procedure implementation, setting of limits for risk levels that are acceptable to the Group. The limits are set according to the amount of regulatory capital and are applied to all risk types. The Group has also developed methods and models of operational risk management.

Credit risk

Credit risk is the risk that counterparty in a transaction made by the Group may cease to pay its liabilities or contingent liabilities. On the reporting date, the total credit risk exposure of Raiffeisenbank Austria to all customer sectors was HRK 29,202 million in assets and HRK 7,691 million in off-balance items. At the Group level, the exposure to credit risk was HRK 31,496 million in assets and HRK 7,919 million in off-balance items.

Positive trends achieved in the economy were reflected in the decline in non-performing loans and their drop was further affected by portfolio sales of nonperforming loans. At the end of 2017, Raiffeisenbank Austria's total non-performing loans classified as risk groups B and C accounted for HRK 2,089 million. Loan loss provisions of HRK 1,318 million cover 63 per cent of non-performing loans. At the Group level, total non-performing loans allocated to risk groups B and C amount at HRK 2,781 million. Loan loss provisions of HRK 1,878 million cover 68 per cent of non-performing loans.

Liquidity risk

Maturity transformation is a function conventionally performed by banks in the financial market. It results in continued reporting discrepancies between the inflows and outflows recorded by banks achieve in specific time periods (liquidity gap). Liquidity discrepancies (gaps) create exposure to liquidity risk. They occur in the form of a risk that Raiffeisenbank Austria will not be able to finance (refinance) its positions under acceptable conditions at appropriate maturities, or as a risk that it will not be able to effectively cash in on its assets within the appropriate period of time.

Raiffeisenbank Austria and the local Raiffeisen Group harmonize their business activities with the legal provisions that regulate liquidity risk, as well as Group and internal documents for the liquidity reserve maintenance. At the end of 2017, the liquidity risk exposure of Bank and Group assets was insignificant.

Management report (continued)

9. Financial instruments and related risks (continued)

Market risk

Market risk is the risk of a negative impact of changes in market parameters, such as interest rates or foreign currency exchange rates, on the Group's income or on the value of its positions in financial instruments. The assessment of exposure to market risk is based on changes in the foreign currency exchange rates, interest rates, credit spreads, equities and commodities prices, as well as other market parameters.

Interest rate risk

Financial assets of Raiffeisenbank Austria and the local Raiffeisen Group are mainly interest-bearing, as is the case with most financial liabilities. Assets and liabilities mature or their interest rates change in different periods and in different amounts. To a certain extent, Bank and Group profit is vulnerable to the interest rate developments. The profit is also affected by the currency structure of assets, liabilities, and capital and reserves. Raiffeisenbank Austria and the Group hold a significant share of interest-bearing assets and liabilities in foreign currencies.

Exchange rate risk

A portion of the assets of Raiffeisenbank Austria and the Raiffeisen Group is denominated in foreign currencies, predominantly in euros. The exposure to the risk of exchange rate fluctuations characterizes the risk of losses incurred in open foreign currency positions. To protect themselves from the currency risk, Raiffeisenbank Austria and the Group use derivative financial instruments.

The exposure to the risk of exchange rate volatility stems from the transactions involving the loans denominated in foreign currencies, deposits denominated in foreign currencies, and investment and market activities. That exposure is monitored on a daily basis, in line with the internal limits set at the level of individual currency and in the total amount of maximum open foreign currency position allowed. The exposure of Raiffeisenbank Austria and the Raiffeisen Group to exchange rate risk on the reporting date was insignificant.

Equities price risk

Equities price risk is the risk of equities price fluctuations, which will affect the fair value of equities investments and other instruments, whose value is derived from equities investments. The primary exposure to price risk stems from the equities that are stated at fair value in the income statement. The exposure of Raiffeisenbank Austria and the Raiffeisen Group to equities price risk on the reporting date was insignificant.

Based on the Croatian Accounting Law, the Management of Raiffeisenbank Austria d.d. Zagreb (hereinafter referred to as "the Bank") shall ensure that the financial statements for each financial year are prepared in accordance with the international financial reporting standards adopted by the European Union (hereinafter "IFRS Adopted by the EU"), so that they give a true and fair view of the bank's balance sheet, business results and cash flows for 2017.

After appropriate controls have been carried out, the management expects the bank to have adequate resources available for the foreseeable future and therefore continues to adopt the principle of timeless business continuity when preparing the financial statements.

Responsibilities of the Management Board in the preparation of financial statements include:

- selection and consistent application of appropriate accounting policies;
- giving justified and prudent judgments and assessments;
- acting in accordance with the applicable accounting standards, with the disclosure and explanation of all material deviations in the financial statements and;
- the preparation of financial statements under the assumption of a going concern, unless the assumption that the bank will continue the business is inappropriate.

Management report (continued)

9. Financial Instruments and Related Risks (continued)

The Management Board of the Bank is responsible for conducting the appropriate accounting records, which at any time, with justified accuracy, outline the position of the bank as well as the consolidated position of the group. The management is responsible for the financial statements to be in accordance with Croatian Accounting Law. In addition, the Management Board is responsible for taking the right steps to prevent and detect fraud and other irregularities.

The Management Board is also responsible for the preparation and contents of the management report in accordance with Croatian Accounting Law. The management report was approved for issue by the Bank's Management Board and was signed in accordance with this.

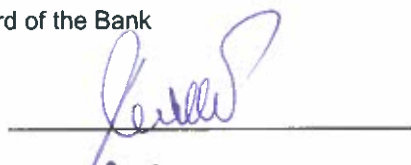
10. Non-financial information

The Bank implemented the exemption allowed under the Accounting Act Article 21a paragraph 7, and does not declare a separate non-financial statement.

Non-financial information regulated under the EU Directive 2014/95 that include the Bank and the members of the local Group were published by RBI on its web site on the link (https://www.rbinternational.com/eBusiness/01_template1/829189266947841370-829188968716049154_923778918747875269_923779208926603950-923779208926603950-NA-2-EN.html).

Signed on behalf of the Management Board of the Bank

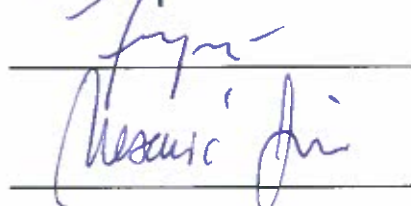
Michael Georg Müller
President of the Management Board



Daniel Mitteregger
Member of the Management Board



Marko Jurjević
Member of the Management Board



Liana Keserić
Member of the Management Board



Zoran Koščak
Member of the Management Board



Ivan Žižić
Member of the Management Board



Responsibilities of the Management and Supervisory Board for the preparation and approval of the annual report

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

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

The Management Board is responsible for the submission to the Supervisory Board of its annual financial statements on the Bank and the Group for acceptance. If the Supervisory Board approves the annual financial statements, they are given to General assembly for acceptance.

The Management Board is also responsible for preparation and presentation of supplementary schedules prepared in accordance with the Decision on the Structure and Content of the Annual Financial Statements of Credit Institution (Official Gazette 30/17 and 44/17).

The separate and consolidated financial statements set out on pages 31 to 164 as well as supplementary regulatory consolidated schedules for the Croatian National Bank on pages 167 to 172 and reconciliation of the statutory financial statements with the supplementary schedules for the Croatian National Bank, set out on pages 173 to 176, were authorised by the Management Board on 31 March 2017 for issue to the Supervisory Board and are signed below to signify this.

The Management Board is also responsible for the preparation and content of the Management Report as required by the Croatian Accounting Law, and for other information that include the Macroeconomic Environment presented on pages 1 to 5 and the Management report presented on pages 6 to 19 were approved by the Management Board on 31 March 2017 and are signed below.

Signed on behalf of the Raiffeisenbank Austria d.d.

Michael Georg Mueller
President of the Management Board

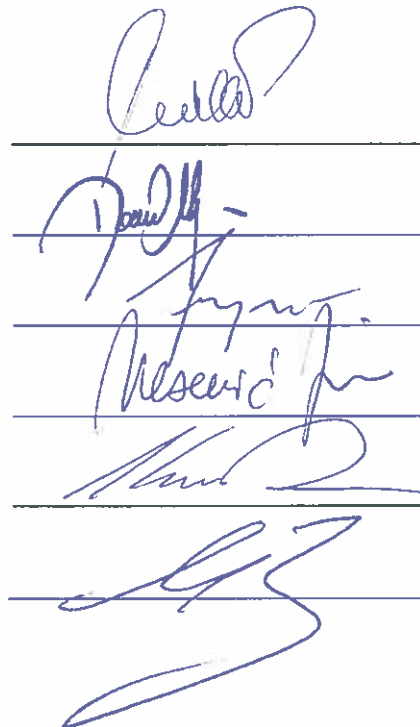
Daniel Mitteregger
Member of the Management Board

Marko Jurjević
Member of the Management Board

Liana Keserić
Member of the Management Board

Zoran Koščak
Member of the Management Board

Ivan Žižić
Member of the Management Board





Independent Auditors' Report to the shareholders of Raiffeisenbank Austria d.d.

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Raiffeisenbank Austria d.d. ("the Bank") and its subsidiaries ("the Group"), which comprise the statements of financial position of the Bank and the Group as at 31 December 2017, and the statements of comprehensive income, changes in equity and cash flows of the Bank and the Group for the year then ended, and notes, comprising significant accounting policies and other explanatory information ("the financial statements").

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank and the Group as at 31 December 2017 and of their financial performance and their cash flows for the year then ended in accordance with statutory accounting requirements for banks in Croatia.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing. Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Bank and the Group in accordance with the ethical requirements that are relevant to our audit of the financial statements in Croatia and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.



Independent Auditors' Report to the shareholders of Raiffeisenbank Austria d.d. (continued)

Report on the Audit of the Financial Statements (continued)

Key Audit Matters

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

Impairment of loans and advances to customers

As at 31 December 2017, in the consolidated financial statements gross loans and advances to customers amount to HRK 19,766 million, related impairment allowance amounts to HRK 2,021 million and impairment loss recognised in the income statement amounts to HRK 369 million (31 December 2016: gross loans and advances: HRK 21,222 million, impairment allowance: HRK 2,718 million, impairment loss recognised in the income statement: HRK 86 million).

As at 31 December 2017, in the separate financial statements gross loans and advances to customers amount to HRK 17,914 million, impairment allowance amounts to HRK 1,461 million and reversal of impairment loss recognised in the income statement amounts to HRK 139 million (31 December 2016: gross loans and advances: HRK 18,824 million, impairment allowance: HRK 2,611 million, impairment loss recognised in the income statement: HRK 87 million).

Refer to pages 60 and 63 and 65 (Accounting policies), pages 71 and 72 (Significant accounting estimates and judgements), pages 84 - 87 (note 11 Loans and advances to customers), and pages 131 to 135 (credit risk section of the note 47 Financial risk management policies).

| Key audit matter | How our audit addressed the matter |
|---|--|
| Impairment allowances represent the Management Board's best estimate of the credit losses incurred within the loans and advances portfolio at the reporting date. We focused on this area as the determination of impairment allowances requires a significant amount of judgment from the Management Board over both the timing of recognition and the amounts of any such impairment. | <p>Our audit procedures in this area included, among others:</p> <ul style="list-style-type: none">• Testing of the design and operating effectiveness of the controls over determination of loan and advances impairment and the estimation of provisions against such assets. The controls tested included, among others, those over:<ul style="list-style-type: none">- calculation of days in arrears;- timely identification of impaired loans and advances, and classification into appropriate risk grades based on the requirements of the CNB;- collateral valuation estimates. |



Independent Auditors' Report to the shareholders of Raiffeisenbank Austria d.d. (continued)

Report on the Audit of the Financial Statements (continued)

Key Audit Matters (continued)

| Key audit matter | How our audit addressed the matter |
|---|--|
| <p>Specific impairment allowances for individually significant exposures (retail exposures in excess of HRK 1.5 million, individually and all corporate exposures) are determined on an individual basis by means of a discounted cash flows analysis.</p> <p>The process involves a high level of subjectivity and reliance on a number of significant assumptions, including those in respect of the probable sale proceeds from collateral, as well as specific guidance of the Croatian National Bank (the CNB) regarding minimum haircuts to be applied on the estimated value of collateral and minimum period of realisation of collateral.</p> <p>Individually non-significant exposures are assessed for impairment on a collective (portfolio) basis. The collective provisioning model considers the minimum loss rates prescribed by the CNB based on the days in arrears.</p> <p>For assets not specifically identified as impaired (including sovereign risk) the Bank recognises the provision with considering the minimum rates prescribed by the CNB (general allowance).</p> | <ul style="list-style-type: none"> • For impairment allowances that are calculated individually: <ul style="list-style-type: none"> - Selecting a sample of individual loans and advances, with focus on those with the greatest potential impact on the financial statements due to their magnitude and/or risk characteristics, which we independently assessed as high-risk, such as watchlisted, restructured or rescheduled exposures, loans to clients operating in higher risk industries, non-performing exposures with low provision coverage and unsecured exposures; - For the sample selected, critically assessing, by reference to the underlying documentation (loan files) and through discussion with the responsible loan officers and credit risk management personnel, the existence of any impairment triggers as at 31 December 2017; - For those loans where impairment triggers were identified, challenging key assumptions applied in the Bank's estimates of future cash flows used in the impairment calculation, such as discount rates and collateral values; - Where different assumptions could be reasonably made in respect of haircuts to collateral and time to dispose, independently recalculating the provision on that basis and comparing the results to the Bank's assessment in order to assess whether there was any indication of an error or management bias; - Assessing whether the specific CNB minimum provisioning requirements were complied with. • For individually non-significant exposures specifically identified as impaired, on a portfolio basis, testing whether the Bank complied with the minimum loss rates prescribed by the CNB based on days in arrears. |



Independent Auditors' Report to the shareholders of Raiffeisenbank Austria d.d. (continued)

Report on the Audit of the Financial Statements (continued)

Key Audit Matters (continued)

| Key audit matter | How our audit addressed the matter |
|------------------|---|
| | <ul style="list-style-type: none">• For impaired loans disposed of in 2017 as part of a portfolio debt sale (including both those provisioned on an individual and on a portfolio basis), comparing sales proceeds with net carrying amounts immediately prior to the sale to assess whether there are any indications that the provisions recognised by the Bank for the disposed loans were not sufficient,• With respect to assets not identified as individually impaired, independently recalculating the Bank's estimation of the general allowance and assessing whether the Bank complied with the minimum loss rate prescribed by the CNB.• Critically assessing the overall reasonableness of the impairment allowances, including both the share of the gross non-performing exposures in total gross exposure and the non-performing loans provision coverage, by benchmarking them against the publicly available industry data. |

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Independent Auditors' Report to the shareholders of Raiffeisenbank Austria d.d. (continued)

Report on the Audit of the Financial Statements (continued)

Key Audit Matters (continued)

Impairment of investments in subsidiaries in the separate financial statements

As at 31 December 2017, investments in subsidiaries in the separate financial statements amount to HRK 395 million (cost HRK 663 million and impairment allowance HRK 268 million) (31 December 2016: HRK 408 million, gross and net); related impairment loss recognised in the income statement amounts to HRK 268 million (2016: nil).

Refer to page 65 (Significant accounting policies), page 74 (Significant accounting estimates and judgements) and page 89 (note 13 Investments in subsidiaries).

| Key audit matter | How our audit addressed the matter |
|---|---|
| <p>The Bank has investments in subsidiaries operating in various industries (leasing, factoring, pension fund management, investment fund management, real estate management and pension insurance). In the Bank's separate financial statements investments in these subsidiaries are stated at cost, less any related impairment.</p> <p>On an annual basis, the Bank performs an assessment of the existence of impairment indicators for the individual subsidiaries. For those subsidiaries, for which impairment indicators were identified, the Bank performs an assessment of the investment's recoverable amount, by reference to its fair value determined via a range of valuation techniques, such as, but not limited to, discounted cash flows, discounted dividend model and use of multipliers.</p> <p>The determination of the investments' recoverable amounts requires the Management Board to apply significant judgement, and to use complex and subjective assumptions. Due to the above factors, as well as the fact that significant impairment losses were recognised during the year, as discussed in Note 13 to the separate financial statements, we consider this area to be a key audit matter.</p> | <p>Our audit procedures in this area included, among others:</p> <ul style="list-style-type: none">Assessing the Bank's identification of impairment indicators, based on our experience with the particular subsidiary, industry in which they operate as well as the Bank's decision making process, considering factors such as, but not limited to: unfavourable developments in the industry, changing laws and regulations, declining financial performance, capital requirements, unsustainable level of debt, financial difficulties of key customers, changing business models and net carrying amount of the Bank's investment in excess of the Bank's share in net assets. |



Independent Auditors' Report to the shareholders of Raiffeisenbank Austria d.d. (continued)

Report on the Audit of the Financial Statements (continued)

Key Audit Matters (continued)

| Key audit matter | How our audit addressed the matter |
|------------------|--|
| | <ul style="list-style-type: none">• For the subsidiaries for which impairment indicators were identified:<ul style="list-style-type: none">- assessing the appropriateness of valuation methods applied by the Bank against the requirements of the relevant financial reporting standards and current market practice;- assessing experience, objectivity and competence of the Bank's internal valuation officers;- assisted by our own valuation specialists, challenging key assumptions used in the Bank's estimates of recoverable amounts, such as cash flows (including, but not limited to the inspection of historical financial performance, quality of budgeting process, past and expected future market developments etc.) and discount rates (including, but not limited to assessing whether the cost of debt and cost of equity used are stated within the reasonable range, given the specific industry, country risk, financial position of company, whether the pre-tax rate was applied to pre-tax cash flows (or post-tax rate to post tax cash flows), and making corroborating inquiries of the Bank's Management Board and its valuation officers;- performing, where considered appropriate, alternative valuations to challenge the management valuations of individual subsidiaries.• for the subsidiaries which are in the process of sale, discussing the process with the Bank's Management Board and inspecting the offers received to date to evaluate whether there are any indications that the carrying amounts of these subsidiaries in the Bank's separate financial statements may be in excess of their recoverable amount;• Assessing the accuracy and completeness of the related disclosures included in note 13 of the separate financial statements. |

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Independent Auditors' Report to the shareholders of Raiffeisenbank Austria d.d. (continued)

Report on the Audit of the Financial Statements (continued)

Other Information

Management is responsible for the other information. The other information comprises the Management Report and Macroeconomic environment included in the Annual Report of the Bank and the Group, but does not include the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

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

With respect to the Management Report, we also performed procedures required by the Accounting Act in Croatia ("Accounting Act"). Those procedures include considering whether the Management Report has been prepared in accordance with the requirements of Articles 21 and 24 of the Accounting Act.

Based solely on the work required to be undertaken in the course of the audit of the financial statements and procedures above, in our opinion:

- the information given in the Management Report for the financial year for which the financial statements are prepared, is consistent, in all material respects, with the financial statements;
- the Management Report has been prepared, in all material respects, in accordance with the requirements of Articles 21 and 24 of the Accounting Act;

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

Responsibilities of Management and Those Charged with Governance for the Financial Statements

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

In preparing the financial statements, management is responsible for assessing the Bank's and the 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 or the Group or to cease operations, or has no realistic alternative but to do so.

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

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Independent Auditors' Report to the shareholders of Raiffeisenbank Austria d.d. (continued)

Report on the Audit of the Financial Statements (continued)

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' 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 International Standards on Auditing will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls.
- 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 the Group's internal controls.
- 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 the 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 auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Bank and the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the financial statements of the Group. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.



Independent Auditors' Report to the shareholders of Raiffeisenbank Austria d.d. (continued)

Report on the Audit of the Financial Statements (continued)

Auditors' Responsibilities for the Audit of the Financial Statements (continued)

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

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' 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.



Independent Auditors' Report to the shareholders of Raiffeisenbank Austria d.d. (continued)

Report on Other Legal and Regulatory Requirements

Pursuant to the Decision of the Croatian National Bank on the Structure and Content of the Annual Financial Statements of credit institutions (Official Gazette 30/17 and 44/17), the Management Board of the Bank has prepared the schedules ("the Schedules"), which comprise an alternative presentation of the consolidated statement of financial position as of 31 December 2017, and of the consolidated income statement, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a reconciliation ("the Reconciliation") of the Schedules with the consolidated financial statements. The schedules are set out on pages 167 – 172, and the Reconciliation is set out on pages 173 to 176. The Management Board of the Bank is responsible for the Schedules and the Reconciliation. The financial information in the Schedules is derived from the Group's financial statements set out on pages 31 to 164 on which we have expressed an opinion as set out above.

We were appointed by those charged with governance on 4 May 2017 to audit the financial statements of the Bank and the Group for the year ended 31 December 2017. Our total uninterrupted period of engagement is 3 years, covering the periods ended 31 December 2015 to 31 December 2017.

We confirm that:

- our audit opinion is consistent with the additional report presented to the Audit Committee of the Bank dated 31 March 2018;
- We have not provided non-audit services, hence, we have not provided any prohibited non-audit services (NASs) referred to in Article 44 of the Audit Act. We also remained independent of the audited entity in conducting the audit;

KPMG Croatia d.o.o. za reviziju
Hrvatski ovlašteni revizori
Eurotower
Ivana Lučića 2a
10000 Zagreb
Hrvatska

31 March 2018


Goran Horvat
Director, Croatian Certified Auditor

KPMG Croatia
d.o.o. za reviziju
Eurotower, 17. kat
Ivana Lučića 2a, 10000 Zagreb

Consolidated statement of financial position

As at 31 December

| | | Group 2017 | Group 2016 |
|---|--------------|-----------------------|-----------------------|
| Assets | Notes | HRK millions | HRK millions |
| Cash and current accounts with banks | 6 | 4,708 | 3,721 |
| Obligatory reserve with the Croatian National Bank | 7 | 1,739 | 1,675 |
| Financial assets at fair value through profit or loss | 8 | 951 | 2,515 |
| Placements with and loans to other banks | 9 | 894 | 1,332 |
| Financial assets available for sale | 10 | 5,937 | 5,217 |
| Loans and advances to customers | 11 | 17,745 | 18,504 |
| Financial investments held to maturity | 12 | 279 | 293 |
| Property, plant, equipment and property investments | 14 | 1,309 | 1,496 |
| Intangible assets | 15 | 239 | 240 |
| Deferred tax asset | 16 | 86 | 86 |
| Other assets | 17 | 291 | 285 |
| Total assets | | 34,178 | 35,364 |

The accounting policies and other notes on pages 45 to 164 form an integral part of these financial statements.

Consolidated statement of financial position (continued)

As at 31 December

| | | Group 2017 | Group 2016 |
|--|--------------|-----------------------|-----------------------|
| Liabilities | Notes | HRK millions | HRK millions |
| Financial liabilities at fair value through profit or loss | 18 | 59 | 97 |
| Deposits from banks | 19 | 1,056 | 441 |
| Deposits from companies and other similar entities | 20 | 9,549 | 9,891 |
| Deposits from individuals | 21 | 14,231 | 14,253 |
| Borrowings | 22 | 2,572 | 3,992 |
| Provisions for liabilities and charges | 23 | 173 | 187 |
| Income tax liabilities | | 70 | - |
| Other liabilities | 24 | 951 | 776 |
| Subordinated liabilities | 25 | 832 | 837 |
| Total liabilities | | 29,493 | 30,474 |
| Equity | | | |
| Share capital | 35 | 3,621 | 3,621 |
| Share premium | | 12 | 12 |
| Capital reserve | | 1 | 1 |
| Legal reserve | | 181 | 181 |
| Fair value reserve | | 48 | 58 |
| Retained earnings | | 822 | 1,017 |
| Total equity attributable to owners of the parent | | 4,685 | 4,890 |
| Total liabilities and equity | | 34,178 | 35,364 |

The accounting policies and other notes on pages 45 to 164 form an integral part of these financial statements.

Consolidated statement of comprehensive income

For the year ended 31 December

| | Notes | Group 2017 HRK millions | Group 2016 HRK millions |
|--|-------|----------------------------------|----------------------------------|
| Interest income | 26 | 1,139 | 1,305 |
| Interest expense | 27 | (226) | (317) |
| Net interest income | | 913 | 988 |
| Fee and commission income | 28 | 794 | 694 |
| Fee and commission expense | 29 | (325) | (257) |
| Net fee and commission income | | 469 | 437 |
| Net trading gains, gains from financial assets available for sale and foreign exchange differences from translation of monetary assets and liabilities | 30 | 192 | 315 |
| Other operating income | 31 | 300 | 322 |
| Trading and other income | | 492 | 637 |
| Operating income | | 1,874 | 2,062 |
| Operating expenses | 32 | (1,212) | (1,877) |
| Impairment losses | 33 | (386) | (107) |
| Reversal of provisions for liabilities and charges | 23 | 14 | 617 |
| Profit before tax | | 290 | 695 |
| Income tax expense | 34 | (102) | (160) |
| Profit for the year | | 188 | 535 |

The accounting policies and other notes on pages 45 to 164 form an integral part of these financial statements.

Consolidated statement of comprehensive income (continued)

For the year ended 31 December

| | Notes | Group 2017 HRK millions | Group 2016 HRK millions |
|--|-------|----------------------------------|----------------------------------|
| Profit for the year | | 188 | 535 |
| Other comprehensive income | | | |
| Items that are or may be reclassified to profit or loss | | | |
| Change in fair value of financial assets available for sale, net of tax and realised amounts | | (10) | (24) |
| Other comprehensive loss for the year, net of tax | | (10) | (24) |
| Total comprehensive profit for the year | | 178 | 511 |
| Profit for the year | | | |
| Attributable to: | | | |
| - Owners of the parent | | 188 | 535 |
| Earnings per share attributable to the equity holders of the parent in HRK | 39 | 51.80 | 147.44 |

The accounting policies and other notes on pages 45 to 164 form an integral part of these financial statements.

Consolidated statement of changes in equity

| | Share capital | Share premium | Capital reserves | Legal reserve | Fair value reserve | Retained earnings | Total | Non- controlling interest | Total |
|--|------------------|------------------|---------------------|------------------|-----------------------|----------------------|-----------------|---------------------------------|-----------------|
| | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions |
| At 1 January 2016 | 3,621 | 12 | 1 | 180 | 82 | 430 | 4,326 | 68 | 4,394 |
| Other comprehensive loss | - | - | - | - | (24) | - | (24) | - | (24) |
| Increase in legal reserve | - | - | - | 1 | - | (1) | - | - | - |
| Profit for the year | - | - | - | - | - | 535 | 535 | - | 535 |
| Acquisition of remaining equity stake in the company Raiffeisen Leasing d.d. | - | - | - | - | - | 53 | 53 | (68) | (15) |
| At 31 December 2016 | 3,621 | 12 | 1 | 181 | 58 | 1,017 | 4,890 | - | 4,890 |
| Other comprehensive loss | - | - | - | - | (10) | - | (10) | - | (10) |
| Other movements | - | - | - | - | - | 2 | 2 | - | 2 |
| Profit for the year | - | - | - | - | - | 188 | 188 | - | 188 |
| Dividend paid | - | - | - | - | - | (385) | (385) | - | (385) |
| At 31 December 2017 | 3,621 | 12 | 1 | 181 | 48 | 822 | 4,685 | - | 4,685 |

The accounting policies and other notes on pages 45 to 164 form an integral part of these financial statements.

Consolidated statement of cash flows

For the year ended 31 December

| | Notes | Group 2017 HRK millions | Group 2016 HRK millions |
|--|-------|----------------------------------|----------------------------------|
| Cash flows from operating activities | | | |
| Profit before tax | | 290 | 695 |
| <i>Adjustments for:</i> | | | |
| - Amortization | 32 | 147 | 191 |
| - Foreign exchange differences from translation of monetary assets and liabilities | 30 | (141) | 9 |
| - Realised gains on financial assets available for sale | 30 | (25) | (99) |
| - Impairment losses (excluding cash and cash equivalents) and provisions for liabilities and charges | 23,33 | 369 | (522) |
| - Net interest income | 26,27 | (913) | (988) |
| <i>Changes in operating assets and liabilities</i> | | | |
| Net decrease/(increase) in financial assets at fair value through profit or loss | | 1,526 | (213) |
| Net decrease/(increase) in placements with banks, with original maturity more than three months | | 21 | (18) |
| Net (increase)/decrease in obligatory reserve with the Croatian National Bank | | (62) | 308 |
| Net decrease in loans and advances to customers | | 471 | 1,110 |
| Net decrease/(increase) in other assets | | (1) | 120 |
| Net decrease/(increase) of financial investments held to maturity | | 12 | (11) |
| Net decrease in financial liabilities at fair value through profit or loss | | (44) | (40) |
| Net increase in deposits from banks | | 627 | 191 |
| Net (decrease)/increase in deposits from companies and other similar entities | | (276) | 1,105 |
| Net increase/(decrease) in deposits from individuals | | 248 | (494) |
| Net increase/(decrease) in other liabilities | | 176 | (4) |
| Decrease in non-controlling interest | | - | (68) |
| Interest received (excluding financial assets available for sale and financial investments held to maturity) | | 1,062 | 1,031 |
| Interest paid | | (219) | (287) |
| Net cash from operating activities before tax | | 3,268 | 2,016 |
| Income tax paid | | (28) | (33) |
| Net cash from operating activities | | 3,240 | 1,983 |

Consolidated statement of cash flows (continued)

For the year ended 31 December

| | | Group 2017 HRK millions | Group 2016 HRK millions |
|---|--------------|--|--|
| | Notes | | |
| Cash flows from investing activities | | | |
| Interest received from financial assets available for sale and financial investments held to maturity | | 165 | 152 |
| Net purchase of financial assets available for sale | | (946) | (235) |
| Purchase of property, plant and equipment and intangible assets | | (161) | (446) |
| Proceeds from disposal of property, plant and equipment and intangible assets | | 41 | 191 |
| Net cash from investing activities | | (901) | (338) |
| Cash flows from financing activities | | | |
| Receipts from borrowings | 22 | 3,457 | 2,085 |
| Repayment of borrowings | 22 | (4,846) | (2,310) |
| (Repayment of)/receipts from subordinated liabilities | | - | (1) |
| Dividend paid | | (385) | - |
| Net cash from financing activities | | (1,774) | (226) |
| Effects of foreign exchange differences on cash and cash equivalents | | (4) | 27 |
| Net increase in cash and cash equivalents | | 561 | 1,446 |
| Cash and cash equivalents at the beginning of the year | | 4,968 | 3,522 |
| Cash and cash equivalents at the end of the year | 40 | 5,529 | 4,968 |

The accounting policies and other notes on pages 45 to 164 form an integral part of these financial statements.

Separate statement of financial position

As at 31 December

| Assets | Notes | Bank 2017 HRK millions | Bank 2016 HRK millions |
|---|--------------|---------------------------------------|---------------------------------------|
| Cash and current accounts with banks | 6 | 4,707 | 3,717 |
| Obligatory reserve with the Croatian National Bank | 7 | 1,739 | 1,675 |
| Financial assets at fair value through profit or loss | 8 | 573 | 2,151 |
| Placements with and loans to other banks | 9 | 905 | 1,384 |
| Financial assets available for sale | 10 | 5,617 | 4,921 |
| Loans and advances to customers | 11 | 16,453 | 16,213 |
| Investments in subsidiaries | 13 | 395 | 408 |
| Property, plant and equipment | 14 | 492 | 478 |
| Intangible assets | 15 | 204 | 206 |
| Deferred tax asset | 16 | 84 | 83 |
| Current tax asset | | - | 1 |
| Other assets | 17 | 210 | 179 |
| Total assets | | 31,379 | 31,416 |

The accounting policies and other notes on pages 45 to 164 form an integral part of these financial statements.

Separate statement of financial position (continued)

As at 31 December

| Liabilities | Notes | Bank 2017 HRK millions | Bank 2016 HRK millions |
|--|--------------|---------------------------------------|---------------------------------------|
| Financial liabilities at fair value through profit or loss | 18 | 61 | 97 |
| Deposits from banks | 19 | 1,093 | 520 |
| Deposits from companies and other similar entities | 20 | 9,817 | 10,090 |
| Deposits from individuals | 21 | 13,203 | 13,195 |
| Borrowings | 22 | 1,237 | 1,759 |
| Provisions for liabilities and charges | 23 | 162 | 176 |
| Income tax liabilities | | 79 | - |
| Other liabilities | 24 | 437 | 292 |
| Subordinated liabilities | 25 | 832 | 837 |
| Total liabilities | | 26,921 | 26,966 |
| Equity | | | |
| Share capital | 35 | 3,621 | 3,621 |
| Share premium | | 12 | 12 |
| Capital reserve | | 1 | 1 |
| Legal reserve | | 173 | 173 |
| Fair value reserve | | 33 | 36 |
| Retained earnings | | 618 | 607 |
| Total equity | | 4,458 | 4,450 |
| Total liabilities and equity | | 31,379 | 31,416 |

The accounting policies and other notes on pages 45 to 164 form an integral part of these financial statements.

Separate statement of comprehensive income

For the year ended 31 December

| | Notes | Bank 2017 HRK millions | Bank 2016 HRK millions |
|--|-------|---------------------------------|---------------------------------|
| Interest income | 26 | 1,026 | 1,148 |
| Interest expense | 27 | (170) | (251) |
| Net interest income | | 856 | 897 |
| Fee and commission income | 28 | 629 | 543 |
| Fee and commission expense | 29 | (320) | (246) |
| Net fee and commission income | | 309 | 297 |
| Net trading gains, gains from financial assets available for sale and foreign exchange differences from translation of monetary assets and liabilities | 30 | 173 | 270 |
| Other operating income | 31 | 101 | 93 |
| Trading and other income | | 274 | 363 |
| Operating income | | 1,439 | 1,557 |
| Operating expenses | 32 | (1,105) | (1,481) |
| Reversal of / (impairment) loss | 33 | 127 | (108) |
| Reversal of provisions for liabilities and charges | 23 | 14 | 617 |
| Profit before tax | | 475 | 585 |
| Income tax expense | 34 | (79) | (125) |
| Profit for the year | | 396 | 460 |

The accounting policies and other notes on pages 45 to 164 form an integral part of these financial statements.

Separate statement of total comprehensive income (continued)

For the year ended 31 December

| | | Bank | Bank |
|--|--------------|-----------------|-----------------|
| | | 2017 | 2016 |
| | | HRK | HRK |
| | Notes | millions | millions |
| Profit for the year | | 396 | 460 |
| Other comprehensive income | | | |
| Items that are or may be reclassified to profit or loss | | | |
| Change in fair value of financial assets available for sale, net of tax and realised amounts | | (3) | (24) |
| Other comprehensive loss for the year, net of tax | | (3) | (24) |
| Total comprehensive profit for the year | | 393 | 436 |
| Earnings per share attributable to the equity holders of the parent | 39 | 109.24 | 127.08 |

The accounting policies and other notes on pages 45 to 164 form an integral part of these financial statements.

Separate statement of changes in equity

| | Share capital | Share premium | Capital reserve | Legal reserve | Fair value reserve | Retained earnings | Total |
|----------------------------|------------------|------------------|--------------------|------------------|--------------------------|----------------------|-----------------|
| | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions |
| At 1 January 2016 | 3,621 | 12 | 1 | 173 | 60 | 147 | 4,014 |
| Other comprehensive loss | - | - | - | - | (24) | - | (24) |
| Profit for the year | - | - | - | - | - | 460 | 460 |
| At 31 December 2016 | 3,621 | 12 | 1 | 173 | 36 | 607 | 4,450 |
| Other comprehensive loss | - | - | - | - | (3) | - | (3) |
| Profit for the year | - | - | - | - | - | 396 | 396 |
| Dividend paid | - | - | - | - | - | (385) | (385) |
| At 31 December 2017 | 3,621 | 12 | 1 | 173 | 33 | 618 | 4,458 |

The accounting policies and other notes on pages 45 to 164 form an integral part of these financial statements.

Separate statement of cash flows

For the year ended 31 December

| | Notes | Bank 2017 HRK millions | Bank 2016 HRK millions |
|--|-------|---------------------------------|---------------------------------|
| Cash flows from operating activities | | | |
| Profit before tax | | 475 | 585 |
| <i>Adjustments for:</i> | | | |
| - Amortization and depreciation | 32 | 74 | 68 |
| - Foreign exchange differences from translation of monetary assets and liabilities | 30 | (139) | 37 |
| - Impairment losses (excluding cash and cash equivalents) and provisions for liabilities and charges | 23,33 | (144) | (521) |
| - Realised gains from financial assets available for sale | 30 | (14) | (94) |
| - Value adjustment of investment in subsidiary | | 268 | - |
| - Net interest income | 26,27 | (856) | (897) |
| - Dividend income from subsidiaries | 31 | (72) | (72) |
| <i>Changes in operating assets and liabilities</i> | | | |
| Net decrease/(increase) in financial assets at fair value through profit or loss | | 1,546 | (180) |
| Net decrease/(increase) in placements with banks, with original maturity more than three months | | 65 | (20) |
| Net (increase)/decrease in obligatory reserve with the Croatian National Bank | | (62) | 308 |
| Net (increase)/ decrease in loans and advances to customers | | (114) | 1,080 |
| Net (increase)/decrease in other assets | | (48) | 90 |
| Net decrease in financial liabilities at fair value through profit or loss | | (42) | (40) |
| Net increase in deposits from banks | | 586 | 181 |
| Net (decrease)/increase in deposits from companies and other similar entities | | (208) | 822 |
| Net increase/(decrease) in deposits from individuals | | 276 | (411) |
| Net increase/(decrease) in other liabilities | | 146 | (25) |
| Interests received (excluding financial assets available for sale) | | 951 | 981 |
| Interests paid | | (167) | (239) |
| Net cash from operating activities before tax | | 2,521 | 1,653 |

Separate statement of cash flows (continued)

For the year ended 31 December

| | Notes | Bank 2017 HRK millions | Bank 2016 HRK millions |
|--|-------|---------------------------------|---------------------------------|
| Income tax paid | | - | - |
| Net cash from operating activities | | 2,521 | 1,653 |
| Cash flows from investing activities | | | |
| Interest received from financial assets available for sale | | 138 | 121 |
| Additional investment in subsidiaries/acquisition of share in subsidiary from the minority shareholder | | (255) | (42) |
| Net outflow from disposal of available-for-sale financial instruments | | (922) | (233) |
| Dividend received | 31 | 72 | 72 |
| Purchase of property, plant, equipment and intangible assets | | (86) | (106) |
| Net cash from investing activities | | (1,053) | (188) |
| Cash flows from financing activities | | | |
| Receipts from borrowings | 22 | 2,682 | 8,270 |
| Repayment of borrowings | 22 | (3,198) | (8,302) |
| (Receipts from subordinated liabilities | | - | (1) |
| Dividend paid | | (385) | - |
| Net cash from financing activities | | (901) | (33) |
| Effects of foreign exchange differences on cash and cash equivalents | | (3) | 26 |
| Net increase in cash and cash equivalents | | 564 | 1,458 |
| Cash and cash equivalents at the beginning of the year | | 4,964 | 3,506 |
| Cash and cash equivalents at the end of the year | 40 | 5,528 | 4,964 |

The accounting policies and other notes on pages 45 to 164 form an integral part of these financial statements.

Notes to the financial statements

1. General information

Raiffeisenbank Austria d.d. ("the Bank" or "the Parent") is a joint stock company incorporated and domiciled in Croatia. The Bank is the parent of the Raiffeisenbank Austria Group ("the Group"). These financial statements are the financial statements of the Bank and the Group as defined in International Accounting Standard 27: "Consolidated and Separate Financial Statements" and International Financial Reporting Standard 10: "Consolidated Financial Statements".

Composition of the Group (Note 13):

Raiffeisenbank Austria d.d.
Raiffeisen stambena štedionica d.d.
Raiffeisen Leasing d.o.o.
Raiffeisen društvo za upravljanje obveznim i dobrovoljnim mirovinskim fondovima d.d.
Raiffeisen Consulting d.o.o.
Raiffeisen mirovinsko osiguravajuće društvo d.d.
Raiffeisen Factoring d.o.o.
Raiffeisen Invest d.o.o.
Raiffeisen Bonus d.o.o.

These financial statements were authorised by the Management Board on 31 March 2017 for issue to the Supervisory Board. This is English translation of statutory financial statements issued in Croatian.

The principal accounting policies applied in the preparation of these financial statements are summarized below. Where specific accounting policies are aligned with accounting principles set out in International Financial Reporting Standards as adopted by the EU, reference may be made to certain Standards in describing the accounting policies of the Group; unless otherwise stated, these references are to Standards applicable at 31 December 2017.

2. Basis of preparation

a) *Statement of compliance*

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

The accounting regulations of the CNB are based on International Financial Reporting Standards as adopted by the EU. The principal differences between the accounting regulations of the CNB and recognition and measurement requirements of International Financial Reporting Standards as adopted by the EU are as follows:

- The CNB requires banks to recognise impairment losses on assets not identified as impaired (including sovereign risk assets) at prescribed rates (excluding assets carried at fair value). In line with the above mentioned regulations, the Group recognised portfolio based provisions in the amount of HRK 272 million (2016: HRK 293 million) (Bank at HRK 261 million and HRK 271 million), and reversal of provisions in profit or loss in the amount of HRK 21 million (2016: HRK 17 million) (Bank in 2017 recognised reversal of provisions of HRK 10 million and in 2016 HRK 14 million). Group's portfolio based provisions for off-balance sheet items as at 31 December 2017 amounted to HRK 77 million (31/12/2016: HRK 80 million) (Bank 31/12/2017: HRK 77 million and per 31/12/2016: HRK 80 million) and the Group recognised reversal of provisions in profit or loss in the amount of HRK 3 million (2016: reversal of provisions in profit or loss HRK 5 million) (Bank 2017: reversal of provisions in profit or loss HRK 3 million and 2016: expense HRK 5 million). Although, in accordance with International Accounting Standard 39 "Financial instruments: Recognition and Measurement" ("IAS 39"), such provisions should more properly be presented as an appropriation within equity, the Group continues to recognise such provisions as a substitute for existing but unidentified impairment losses calculated in accordance with the requirements of IAS 39.
- Additionally the CNB prescribes minimum levels of impairment losses against certain specifically identified impaired exposures, regardless of the net present value of expected future cash flows, which may be different from the impairment loss required to be recognised in accordance with the IAS 39 requirements.

Notes to the financial statements (continued)

2. Basis of preparation (continued)

a) Statement of compliance (continued)

- In accordance with local regulations, interest income on impaired exposures is recognised on a cash basis, as opposed to IAS 39, which prescribes recognition of interest income on impaired exposures through unwinding of the discount.
- In accordance with local regulations, the Group recognises provisions for court cases incorporating the likelihood of the loss into measurement of the provision (i.e. if the likelihood of the loss is estimated to be 10%, the provision will be calculated as 10% of the potential loss), which is contrary to IFRS, which prescribes recognition of the full amount of potential loss, once it is probable that the court case will be lost.
- According to the CNB instructions in 2015, the Bank has recognised the expected loss of CHF conversion for loans subject to conversion in the amount of HRK 617 million presented within Provisions for liabilities and charges in the statement of financial position and in the income statement. Under IAS 39 such a loss would be offset against the loans and advances to customers. During 2016, the Bank released the provisions in the amount of HRK 611 million (note 23) upon carrying out the conversion. In the year 2017 the Bank released the remaining provisions for the CHF loans conversion in the amount of HRK 6 million.

b) Measurement

The financial statements are prepared on a fair value basis for derivative financial instruments, financial assets and trading liabilities, other financial assets and liabilities at fair value through profit or loss and financial assets available for sale, except those equity investments available for sale for which a reliable measure of fair value is not available and are measured at cost less impairment. Other financial assets and liabilities, and non-financial assets and liabilities, are stated at amortised or historical cost.

c) Basis of consolidation

Business combinations

The Group accounts for business combinations using the acquisition method when control is transferred to the Group. The transferred consideration in the acquisition is generally measured at fair value, as are the identifiable net assets acquired. Any goodwill that arises is tested annually for impairment. Any gain on a bargain purchase relating to negative goodwill is immediately recognised in profit or loss. Transaction costs are expensed as incurred in profit or loss, except if related to the issue of debt or equity securities. The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognised in profit or loss.

Any contingent consideration is measured at fair value at the date of acquisition. If an obligation to pay contingent consideration that meets the definition of a financial instrument is classified as equity, then it is not remeasured and settlement is accounted for within equity. Otherwise, subsequent changes in the fair value of the contingent consideration are recognised in profit or loss. If share-based payment awards (replacement awards) are required to be exchanged for awards held by the acquiree's employees (acquiree's awards), then all or a portion of the amount of the acquirer's replacement awards is included in measuring the transferred consideration in the business combination. This determination is based on the market-based measure of the replacement awards compared with the market-based measure of the acquiree's awards and the extent to which the replacement awards relate to pre-combination service.

Business combinations involving entities under common control are recognised at their carrying amounts, and the difference is recognised directly in equity, as discussed in the section Acquisition of entities under common control.

Subsidiaries

Subsidiaries are entities controlled by the Group. The Group controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date on which control commences until the date on which control ceases.

In its separate financial statements, the Bank accounts for its investments in subsidiaries are carried at cost less any impairment.

Notes to the financial statements (continued)

2. Basis of preparation (continued)

c) *Basis of consolidation (continued)*

Associates

Associates are entities over which the Group has significant influence but no control. Investments in associates are accounted for using the equity method of accounting in the consolidated financial statements and are initially recognised at cost. The Group's investments in associates include goodwill (net of any accumulated impairment loss) identified on acquisition. In the Bank's separate financial statements investments in associates are accounted at cost less impairment.

The Group's share of its associates' post-acquisition gains or losses is recognised in the income statement and its share of their post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise any further losses, unless it has incurred obligations or has made payments on behalf of the associate.

Dividends received from associates are treated as a decrease of investment in the associate in the Group's consolidated statement of financial position and as dividend income in the Bank's unconsolidated income statement.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associate. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the assets transferred. The accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

Non-controlling interests

Non-controlling interests are measured at their proportionate share of the acquiree's identifiable net assets at the date of acquisition. Changes in the Group's interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions.

Non-controlling interests in subsidiaries are included in the total equity of the Group.

Loss of control

When the Group loses control over a subsidiary, it derecognises the assets and liabilities of the subsidiary, and any related non-controlling interests and other components of equity. Any resulting gain or loss is recognised in profit or loss. Any interest retained in the former subsidiary is measured at fair value when control is lost.

Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated. Unrealised gains arising from transactions with equity accounted investees are eliminated against the investment to the extent of the Group's interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

Acquisition of entities under common control

Business combinations arising from the transfer of shares in entities that are under the control of the shareholder that controls the Group are recognised at their carrying amounts since the acquisition. The acquired assets and liabilities are recognised at the carrying amounts recognised previously in the financial statements of the acquired company. Parts of the capital of the acquired companies are added to the respective positions of equity in addition to the issued capital. Differences arising from the acquisition are recognised in retained earnings. The Group does not restate comparative information as if the Group's member was always a member of the RBI Group, but the acquisition is shown from the date of acquisition.

d) *Functional and presentation currency*

These financial statements are presented in Croatian Kuna (HRK), which is the functional currency. Amounts are rounded to the nearest million (unless otherwise stated).

The effective exchange rate as at 31 December 2017 was HRK 7.513648 to EUR 1 (2016: HRK 7. 557787); HRK 6.269733 to USD 1 (2016: HRK 7.168536) and HRK 6.431816 to CHF 1 (2016: HRK 7. 035735).

Notes to the financial statements (continued)

2. Basis of preparation (continued)

e) Use of judgments and estimates

In preparing the financial statements, Management has made judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, and disclosure of commitments and contingencies at date of reporting, as well as amounts of income and expenses for the period. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances and information available at the date of the preparation of the financial statements, the results of which form the basis of making judgements about carrying amounts of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of revision and future periods if the revision affects both current and future periods. Judgments made by management in the application of applicable standards that have significant effects on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in Note 4.

The accounting policies have been consistently applied to all periods presented in these financial statements.

f) Global financial market situation and the impact on Croatia

By the expansive monetary policy measures, the European Central Bank strives to stimulate price rise towards the target level of 2% annually, through increase in loan offer and decrease in interest rates. The expected outcome is an accelerated growth in economy and employment based on stronger consumption. The expansiveness of the ECB monetary policy is evident from the 0% ECB key interest rate that did not change in 2017, and the interest rate on the Euro-area banks' deposits held with the ECB was -0.4%. Further, by its unconventional monetary policy measures, the ECB raised liquidity in the Euro-area financial markets. In the first quarter of 2017 the target amount of the monthly bond repurchase programme in the secondary financial market was EUR 80 billion. In the remaining three quarters the ECB lowered the monthly repurchase amount to EUR 60 billion. In 2018 over the first three quarters the ECB will repurchase EUR 30 billion each month and after that the implementation of unconventional measures is expected to end.

The policy of the European Central Bank (ECB) considerably impacts the highly euroized financial markets outside the euro area, such as Croatia. As a consequence of the ECB expansion policy, interest rates have been decreasing. In the euro financial markets interest rates remained negative throughout the year, and yields on bonds of first-grade issuers from the euro area with 5-year maturity were also negative throughout the entire year. At mid-year also 10-year issues had negative yields.

The negative market interest rates in the euro area reduced yields to financial assets. Total loans in the euro area could not absorb the excess liquidity in the market. Banks could have hold on to extra liquidity at ECB with -0,4% yield or could invest the means into first class bonds with even lower yields. Therefore, the banks sought investment opportunities at higher yields outside the euro area. High-risk customer loans were offered at lowered but still positive interest rates.

In 2017 the Croatian financial market was flooded by excess liquidity. In the past three years the banks cancelled their loans, which process was completed already at the beginning of the year. The room for any adjustments in the offer of interest rates on customer deposits with banks was also used up quickly. From the middle of 2017 interest rates on term deposits hit the bottom and have been stagnant on low levels since then.

The banks' lowering of term deposit interest rates demotivates customers to make term deposits, and thus also to convert them from kuna into euro deposits. Consequently, a vista HRK financing sources increased, which allowed banks to increase kuna placements. Thus, the offer of loans in the kuna became competitive to the offer of loans in the euro, resulting in an increased demand for kuna loans.

The rates of real economic growth in the euro area rose above 2.0%, and price rise remained low because of the slow growth in lending. Economic stability in the euro area positively reflected on the demand for products and services from Croatia. Because of an increase in the GDP, Croatia saw a rise in budget revenues, and the fiscally responsible RH Government kept budgetary expenses under control. Budget balancing provided for the stabilization of public finance so the country's financing prices in the external capital markets dropped.

Notes to the financial statements (continued)

2. Basis of preparation (continued)

g) Standards, interpretations and amendments to published standards that are not yet effective and were not used in preparation of these financial statements

1. IFRS 9 Financial Instruments

The Bank will as well as the other Raiffeisenbank International AG members, apply the IFRS 9 Financial Instruments as issued in July 2014 initially on 1 January 2018 and will early adopt the amendments to IFRS 9 on the same date.

In keeping with the RBI policy and options allowed under the IFRS 9, the Bank has not opted to modify the comparable data for the year 2017.

On the basis of the analyses conducted so far, reserve increase arising from the implementation of the new standard does not have a material impact on the Bank's capital adequacy.

The European Parliament has issued as of 27. December 2017 a regulation (EU) 2017/2395 on transition requirements for the implementation of IFRS 9. The regulation allows a choice of two approaches to the recognition of the impact of adoption of the standard on regulatory capital:

1. Phasing in the full impact on a straight-line basis over a five-year period; or
2. Recognizing the full impact on the day of adoption.

RBI has decided to adopt the second approach and the Bank will act accordingly as well.

In the process of aligning with the IFRS 9 requirements the Bank gives due attention to local specifics and requirements of the Croatian National Bank, besides considering accounting policies and judgments of the RBI.

The new standard will require RBI to revise its accounting processes and internal controls, and these changes are not yet complete.

The Bank has not finalized the testing and assessment of controls over its new IT systems.

The systems and the associated controls that are in place to comply with the new requirements have been implemented only since the end of 2017 and are still in the process of development.

The new accounting policies, assumptions, judgments and estimation techniques employed are subject to change until RBI and the Bank finalize their first financial statements that include the date of initial application.

2. Classification and measurement in general

IFRS 9 contains a new classification and measurement approach for financial assets that reflect the business model in which assets are managed and their cash flow characteristics.

For the Bank and the Group four classification categories for financial assets will be applied:

- Financial assets measured at amortized cost (AC)
- Financial assets measured at fair value through OCI (FVOCI) and
- Financial assets mandatorily measured at fair value through profit or loss (FVTPL) and
- Financial assets designated measured at fair value through profit or loss (FVTPL)

A financial asset shall be measured at amortized cost if both of the following conditions are met:

- The asset is held within a business model whose objective is to hold assets in order to collect contractual cash flows
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

A business model's objective can be to hold financial assets to collect contractual cash flows even when some sales of financial assets have occurred or are expected to occur. IFRS 9 gives the following examples of sales that may be consistent with the hold-to-collect business model

- The sales are due to an increase in the credit risk of a financial asset;
- The sales are infrequent (even if significant), or are insignificant individually and in aggregate (even if frequent);
- The sales take place close to the maturity of the financial asset and the proceeds from the sales approximate the collection of the remaining contractual cash flows;

For RBI, the sale of more than 10% of the portfolio (carrying value) during a rolling 3 year period will potentially be considered 'more than infrequent' unless these sales are immaterial as a whole. The Bank adopted the same materiality threshold.

A maturity less than 3 month, in keeping with the RBI definition, can be seen as close to maturity.

Notes to the financial statements (continued)

2. Basis of preparation (continued)

g) Standards, interpretations and amendments to published standards that are not yet effective and were not used in preparation of these financial statements (continued)

A financial asset is classified as subsequently measured at FVOCI if it is held within a business model whose objective is both collecting contractual cash flows and selling financial assets; and the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

On initial recognition of an equity instrument that is not held for trading, Banka may irrevocably elect to present subsequent changes in fair value in OCI. This election is made on an investment – by – investment basis for each investment and essentially covers strategic interests that are not fully consolidated. All other financial assets – i.e. financial assets that do not meet the criteria for classification as subsequently measured at either amortised cost or FVOCI – are classified as subsequently measured at fair value, with changes in fair value recognised in profit or loss. In addition, Banka has the option at initial recognition to irrevocably designate a financial asset as at FVTPL if doing so eliminates or significantly reduces a measurement or recognition inconsistency – i.e. an ‘accounting mismatch’ – that would otherwise arise from measuring assets or liabilities, or recognising the gains and losses on them, on different bases.

Financial liabilities are classified into measurement categories by amortized cost or by fair value through the profit and loss account, and in this respect there are no differences with regard to the IFRS 39, save for allocation and recognition through other overall profit of a part of the fair value change that refers to own credit risk for financial liabilities at fair value through the profit and loss account.

2.1 Business model assessment

The Bank will make an assessment of the objective of the business model in which a financial asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management.

The following will be considered as evidence when assessing which business model is relevant:

- How the performance of the business model (and the financial assets held within that business model) are evaluated and reported to the entity’s key management personnel;
- How the risks that affect the performance of the business model (and the financial assets held within that business model) and especially the way those risks are managed;
- How managers of the business are compensated – e.g. whether the compensation is based on the fair value of the assets managed or the contractual cash flows collected;
- the frequency, value and timing of sales in prior periods, the reasons for such sales, and its expectations about future sales activity; and
- the evaluation whether sales activity and the collection of contractual cash flows are each integral or incidental to the business model (“hold-to-collect” versus “hold and sell” business model);

Financial assets that are held for trading and those that are managed and whose performance is evaluated on a fair value basis will be measured at FVTPL.

2.2 Analysis of contractual cash flows characteristics

Once the Bank determines that the business model of a specific portfolio is to hold the financial assets to collect the contractual cash flows (or by both collecting contractual cash flows and selling financial assets), it must assess whether the contractual terms of the financial asset give rise on specific dates to cash flows that are solely payments of principal and interest on the principal amount outstanding. For this purpose, interest is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs, as well as a profit margin. This assessment will be carried out on an instrument by instrument basis on the date of initial recognition of the financial asset.

In assessing whether the contractual cash flows are solely payments of principal and interest Banka will consider the contractual terms of the instrument. This will include assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition

- Prepayment, extension terms
- Leverage features
- Claim is limited to specified assets or cash flows
- Contractually linked instruments

Notes to the financial statements (continued)

2. Basis of preparation (continued)

g) Standards, interpretations and amendments to published standards that are not yet effective and were not used in preparation of these financial statements (continued)

In 2018 IASB issued an IFRS 9 amendment regarding prepayment features with negative compensation. Negative compensation arises where the contractual terms permit the borrower to prepay the instrument before its contractual maturity, but the prepayment amount could be less than unpaid amounts of principal and interest. However, to qualify for amortised cost measurement, the negative compensation must be “reasonable compensation for early termination of the contract”. Banka does not expect a significant volume of negative prepayment features with negative compensation which have to be measured mandatorily at FVTPL.

2.3 Modification and time value of money and benchmark test

Time value of money is the element of interest that provides consideration for only the passage of time. It does not take into account other risks (credit, liquidity etc.) or costs (other administrative expenses) associated with holding a financial asset.

In some cases, the time value of money element may be modified (imperfect). That would be the case, for example, if a financial asset's interest rate is periodically reset but the frequency of that reset does not match the tenor of the interest rate. In this case units must assess the modification as to whether the contractual cash flows still represent solely payments of principal and interest, i.e. the modification term does not significantly alter the cash flows from a 'perfect' benchmark instrument. This assessment is not an accounting policy choice and cannot be avoided simply by concluding that an instrument, in the absence of such an assessment, will be measured at fair value. For the following main contractual features that can potentially modify the time value of money a benchmark test will be applied:

- Reset rate frequency does not match interest tenor
- Lagging indicator
- Smoothing clause)
- Grace period
- Secondary market yield reference

2.4 Impact assessment

Loans and advances to banks and to customers that are classified as loans and receivables measured at amortized cost under IAS 39 will in general also be measured at amortized cost under IFRS 9. Only an insignificant portfolio has to be measured mandatorily at FVTPL due to failing the SPPI or Benchmark test.

Held to maturity financial assets measured at amortized cost under IAS 39 will in general also be measured at amortized cost under IFRS 9. Only an insignificant portfolio will be reclassified to the business model “hold and sell” and measured at FVOCI.

Available for Sale debt instruments measured at fair value through Equity under IAS 39 will in general also be measured at FVOCI under IFRS 9.

3. Hedge accounting

IFRS 9 grants accounting options for hedge accounting. The Bank plans to continue to apply the provisions on hedge accounting pursuant to IAS 39 while, however, taking into account the changes in the disclosures in the notes pursuant to IFRS 7.

4. Impairment general

The calculation of expected credit losses requires the use of accounting estimates which, by definition, will rarely equal the actual results. Management also needs to exercise judgement in applying the Group's accounting policies.

Notes to the financial statements (continued)

2. Basis of preparation (continued)

g) Standards, interpretations and amendments to published standards that are not yet effective and were not used in preparation of these financial statements (continued)

The Bank assesses on a forward-looking basis the expected credit losses associated with its debt instrument assets carried at amortised cost and FVOCI and with the exposure arising from loan commitments, leasing receivables and financial guarantee contracts. The Bank recognises a loss allowance for such losses at each reporting date.

5. Measurement of expected credit losses

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

The measurement of the expected credit loss allowance for financial assets measured at amortised cost and debt assets at fair value through other comprehensive income is an area that requires the use of complex models and significant assumptions about future economic conditions and credit behaviour. Significant judgements are required in applying the accounting requirements for measuring expected credit losses these are:

- Determining criteria for significant increase in credit risk
- Choosing appropriate models and assumptions for the measurement of expected credit losses
- Establishing the number and relative weightings of forward-looking scenarios for each type of product/market and the associated expected credit losses
- Establishing groups of similar financial assets for the purposes of measuring expected credit losses

For credit risk comes from the risk of suffering financial loss, should any of the Bank clients fail to fulfil their contractual obligations to the Bank. Credit risk arises mainly from interbank, commercial and consumer loans and advances, and loan commitments arising from such lending activities, but can also arise from credit enhancement provided, such as, financial guarantees, letters of credit, and acceptances.

The Bank is also exposed to other credit risks arising from investments in debt securities and other exposures arising from its trading activities ('trading exposures') including non-equity trading portfolio assets and derivatives as well as settlement balances with market counterparties and reverse repurchase agreements. The estimation of credit exposure for risk management purposes is complex and requires the use of models, as the exposure varies with changes in market conditions, expected cash flows and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring, of the associated loss ratios and of default correlations between counterparties. The Bank measures credit risk using probability of default (PD), exposure at default (EAD) and loss given default (LGD). This is the predominant approach used for the purposes of measuring expected credit losses under IFRS 9. IFRS 9 prescribes a three-stage model for impairment based on changes in credit quality since initial recognition. This model requires that a financial instrument that is not credit-impaired on initial recognition is classified in Stage 1 and has its credit risk continuously monitored. If a significant increase in credit risk since initial recognition is identified, the financial instrument is moved to Stage 2 but is not yet deemed to be credit-impaired. If the financial instrument is credit-impaired, the financial instrument is then moved to Stage 3.

Financial instruments in Stage 1 have their expected credit loss measured at an amount equal to the portion of lifetime expected credit losses that result from default events possible within the next 12 months. Instruments in Stages 2 or 3 have their expected credit losses measured based on expected credit losses on a lifetime basis. According to IFRS 9 when measuring expected credit losses it is necessary to consider forward-looking information. Purchased or originated credit-impaired financial assets are those financial assets that are credit-impaired on initial recognition. Their expected credit loss is always measured on a lifetime basis.

Notes to the financial statements (continued)

2. Basis of preparation (continued)

g) Standards, interpretations and amendments to published standards that are not yet effective and were not used in preparation of these financial statements (continued)

6. Significant Increase in Credit Risk

In keeping with the RBI Group policies, the Bank considers a financial instrument to have experienced a significant increase in credit risk when one or more of the following quantitative, qualitative or backstop criteria have been met:

6.1 Quantitative Criteria

The Bank uses quantitative criteria as the primary indicator of significant increase in credit risk for all material portfolios. For quantitative staging the Bank compares the lifetime PD curve at measurement data with the forward lifetime PD curve at the date of initial recognition. For the estimation of the lifetime PD curve at the date of initial recognition assumptions are made about the structure of the PD curve. On the one hand in the case of highly rated financial instruments it is assumed that the PD curve will deteriorate over time. On the other hand for low rated financial instruments it is assumed that the PD curve will improve over time. The degree of improvement or deterioration will depend on the level of the initial rating. In order to make the two curves comparable the PDs are scaled down to annualized PDs. In general a significant increase in credit risk is considered to have occurred with a relative increase in the PD of up to 250% although this amount can be lower due to several limiting factors such as closeness to maturity and portfolios of products.

RBI or the Bank are not aware of any generally accepted market practice for the level at which a financial instrument has to be transferred to Stage 2. From this perspective it is expected that the increase in PD at reporting date which is considered significant will develop over a period of time as a result of an iterative process between market participants and supervisors.

In the retail segment, quantitative criteria are applied for unsecured consumer loans and secured housing loans, for which portfolios the Bank was able to develop statistical models for lifetime PD assessment on the basis of own historical data, and according to the RBI group directive for developing the statistical IFRS 9 risk parameter assessment model. The result of the lifetime PD model are lifetime PD curves for individual ratings of a placement/credit product, as well as the materiality threshold for an individual product. Thus obtained materiality threshold is used to determine whether at the time of observing (reporting date) there has been a material increase in probability of default in the remaining repayment period with regard to the initial probability of default assessment for the remaining repayment period as on the observed reporting date. The lifetime PD assessment models, including the materiality threshold assessment, were validated by RBI and will be reviewed/re-estimated once a year, or developed with respect to the results of the annual predictivity evaluation and overall model adequacy.

6.2 Qualitative Criteria

In keeping with the RBI policies, the Bank uses qualitative criteria as a secondary indicator of significant increase in credit risk for all material portfolios. A movement to Stage 2 takes place when the criteria below are met.

For sovereign, bank, corporate and project finance portfolios, if the borrower meets one or more of the following criteria:

- External market indicators
- Changes in contract terms
- Changes to management approach
- Expert judgment

Notes to the financial statements (continued)

2. Basis of preparation (continued)

f) Standards, interpretations and amendments to published standards that are not yet effective and were not used in preparation of these financial statements (continued)

The assessment of significant increase in credit risk incorporates forward-looking information and is performed on a quarterly basis at a deal level for all non-retail portfolios.

For retail portfolios, if the borrower meets one or more of the following criteria:

- Forbearance
- placement in default for over 30 days,
- client has another placement in default (in the PI segment, the default status is determined on the basis of placement not client)
- Expert judgment, (engl. Holistic flag) of the Retail Provisioning Committee

The assessment of significant increase in credit risk incorporates forward-looking information and is performed on a monthly basis at a deal level for all retail portfolios

6.3 Backstop

A backstop is applied and the financial instrument considered to have experienced a significant increase in credit risk if the borrower is more than 30 days past due on its contractual payments. In some limited cases the presumption that financial assets which are more than 30 days past due are to be shown in Stage 2 is rebutted. In the retail segment, such rebutting is possible only exceptionally, due to technical reasons because of which a placement has over 30 days as the client's payment was not processed in the Bank's system on time.

6.4 Low Credit Risk Exemption

The Bank has not used the low credit risk exemption for any lending business, however it selectively uses the low credit risk exemption for debt securities of issuers with high external credit rating.

7. Definition of Default and Credit-Impaired Assets

The Bank defines a financial instrument as in default, which is fully aligned with the definition of credit-impaired, when it meets one or more of the following criteria:

7.1. Quantitative criteria

The borrower is more than 90 days past due on its contractual payments. No attempt is made to rebut the presumption that financial assets which are more than 90 days past due are to be shown in Stage 3.

7.2. Qualitative criteria

The borrower meets unlikelihood to pay criteria, which indicates the borrower is in significant financial difficulty. These are instances where:

- The borrower is in long-term forbearance (distressed restructuring)
- The borrower is deceased
- The borrower is insolvent
- The borrower is in breach of financial covenants
- An active market for that financial asset has disappeared because of the borrower's financial difficulties
- Concessions have been made by the lender relating to the borrower's financial difficulty
- It is becoming probable that the borrower will enter bankruptcy
- Financial assets are purchased or originated at a deep discount that reflects the incurred credit losses
- Client's fraud was detected in connection to creditworthiness/security instruments

The criteria above have been applied to all financial instruments held by RBI and are consistent with the definition of default used for internal credit risk management purposes. The default definition has been applied consistently to model the Probability of Default (PD), Exposure at Default (EAD) and Loss given Default (LGD) throughout the expected loss calculations of the Bank.

An instrument is considered to no longer be in default (i.e. to have cured) when it no longer meets any of the default criteria for a consecutive period of a minimum of 3 months or longer for distressed restructured exposures. This period of 3 months has been determined based on an analysis which considers the likelihood of a financial instrument returning to default status after cure using different possible cure definitions.

Notes to the financial statements (continued)

2. Basis of preparation (continued)

f) *Standards, interpretations and amendments to published standards that are not yet effective and were not used in preparation of these financial statements (continued)*

8 Explanation of inputs, assumptions and estimation techniques

The expected credit loss is measured on either a 12-month or lifetime basis depending on whether a significant increase in credit risk has occurred since initial recognition or whether an asset is considered to be credit-impaired. Forward-looking economic information is also included in determining the 12-month and lifetime PD, EAD and LGD. These assumptions vary by product type. Expected credit losses are the discounted product of the probability of default (PD), loss given default (LGD), exposure at default (EAD) and discount factor (D).

8.1 Probability of Default

The probability of default represents the likelihood of a borrower defaulting on its financial obligation either over the next 12 months or over the remaining lifetime of the obligation. In general the lifetime probability of default is calculated using the regulatory 12 month probability of default, stripped of any margin of conservatism, as a starting point. Thereafter various statistical methods are used to generate an estimate of how the default profile will develop from the point of initial recognition throughout the lifetime of the loan or portfolio of loans. The profile is based on historical observed data and parametric functions.

Different models have been used to estimate the default profile of outstanding lending amounts and these can be grouped into the following categories:

- Sovereign, local and regional governments, insurance companies and collective investment undertakings the default profile is generated using a transition matrix approach. Forward looking information is incorporated into the probability of default using the Vasicek one factor model
- Corporate customers, project finance and financial institutions the default profile is generated using a parametric survival regression (Weibull) approach. Forward looking information is incorporated into the probability of default using the Vasicek one factor model
- Retail mortgages and other retail lending the default profile is generated using parametric survival regression in competing risk frameworks. Forward looking information is incorporated into the probability of default using satellite models.

In the limited circumstances where some inputs are not fully available grouping, averaging and benchmarking of inputs is used for the calculation.

8.2 Loss Given Default

Loss given default represents the Bank's expectation of the extent of loss on a defaulted exposure. Loss given default varies by type of counterparty and product. Loss given default is expressed as a percentage loss per unit of exposure at the time of default. Loss given default is calculated on a 12-month or lifetime basis, where 12-month loss given default is the percentage of loss expected to be made if the default occurs in the next 12 months and lifetime loss given default is the percentage of loss expected to be made if the default occurs over the remaining expected lifetime of the loan.

Different models have been used to estimate the loss given default of outstanding lending amounts and these can be grouped into the following categories:

- Sovereign the loss given default is found by using market implied sources
- Corporate customers, project finance, financial institutions, local and regional governments, insurance companies the loss given default is generated by discounting cash flows collected during the workout process. Forward looking information is incorporated into the loss given default using the Vasicek model.

Notes to the financial statements (continued)

2. Basis of preparation (continued)

f) Standards, interpretations and amendments to published standards that are not yet effective and were not used in preparation of these financial statements (continued)

- Retail mortgages and other retail lending the loss given default is generated by stripping the downturn adjustments and other margins of conservatism from the regulatory loss given default. Forward looking information is incorporated into the loss given default using various satellite models
- In the limited circumstances where some inputs are not fully available alternative recovery models, benchmarking of inputs and expert judgment is used for the calculation.

8.3 Exposure at Default

Exposure at default is based on the amounts the Bank expects to be owed at the time of default, over the next 12 months or over the remaining lifetime. The 12-month and lifetime EADs are determined based on the expected payment profile, which varies by product type. For amortising products and bullet repayment loans, this is based on the contractual repayments owed by the borrower over a 12-month or lifetime basis. Where relevant early repayment/refinance assumptions are also considered in the calculation.

For revolving products, the exposure at default is predicted by taking current drawn balance and adding a credit conversion factor which allows for the expected drawdown of the remaining limit by the time of default. The prudential regulatory margins are removed from the credit conversion factor. In the limited circumstances where some inputs are not fully available benchmarking of inputs is used for the calculation.

8.4 Discount Factor

In general for on balance sheet exposure which is not leasing or (POCI) the discount rate used in the expected credit loss calculation is the effective interest rate or an approximation thereof.

8.5 Calculation

The expected credit loss is the product of PD, LGD and EAD times the probability not to default prior to the considered time period. The latter is expressed by the survivorship function S. This effectively calculates future values of expected credit losses, which are then discounted back to the reporting date and summed. The calculated values of expected credit losses are then weighted by forward looking scenario.

Different models have been used to estimate the Stage 3 provisions of outstanding lending amounts and these can be grouped into the following categories:

- Sovereign, corporate customers, project finance, financial institutions, local and regional governments, insurance companies and collective investment undertakings the Stage 3 provisions are calculated by workout managers who discount expected cash flows by the appropriate effective interest rate
- Retail mortgages the Stage 3 provision is generated by calculating the discounted collateral realization value
- Other retail lending the Stage 3 provision is generated by calculating the statistically derived best estimate of expected loss which has been adjusted for indirect costs.
No attempt is made to rebut the presumption that financial assets which are more than 90 days past due are to be shown in Stage 3.

9 Forward Looking Information

The assessment of significant increase in credit risk and the calculation of expected credit losses both incorporate forward-looking information. The RBI Group and the Bank have performed historical analysis and identified the key economic variables impacting credit risk and expected credit losses for each portfolio.

Notes to the financial statements (continued)

2. Basis of preparation (continued)

f) Standards, interpretations and amendments to published standards that are not yet effective and were not used in preparation of these financial statements (continued)

These economic variables and their associated impact on the probability of default, loss given default and exposure at default vary by category type. Expert judgment has also been applied in this process. Forecasts of the economic variables, or the base economic scenario, are created by the Raiffeisen Research on the basis of data and in co-operation with the Bank's Economic and Financial Research quarterly, which are also a constituent part of the RBI Group Research. Distribution of responsibilities by individual variables is regulated and defined under the internal document „RBI Group Research Rulebook“, and the best estimate of economy for the next three years is based on these. After three years, to project the economic variables out for the full remaining lifetime of each instrument, a mean reversion approach has been used, which means that economic variables tend to either a long run average rate or a long run average growth rate until maturity. The impact of these economic variables on the probability of default, loss given default and exposure at default has been determined by performing statistical regression to understand the impact changes in these variables have had historically on default rates and on the components of loss given default and exposure at default.

In addition to the base economic scenario, Raiffeisen Research also provide a best case and worst case scenario after which the scenarios are co-ordinated and, if necessary, reviewed in co-operation with the Bank's Economic and Financial Research analysts. The scenarios are based on the base economic scenario in the form of departures from the respective scenario. The departures have probabilities that correspond to the probabilities on the 25th and the 27th percentile of the corresponding probability distribution function. In accordance with its own experience and that of the RBI group, the Bank concluded that non-linearities are represented in three scenarios at the most in the most adequate manner. The scenario weightings are determined by a combination of statistical analysis and expert credit judgement, taking account of the range of possible outcomes each chosen scenario is representative of. The probability-weighted expected credit losses are determined by running each scenario through the relevant expected credit loss model and multiplying it by the appropriate scenario weighting.

As with any economic forecasts, the projections and likelihoods of occurrence are subject to a high degree of inherent uncertainty and therefore the actual outcomes may be significantly different to those projected. The Bank considers these forecasts to represent its best estimate of the possible outcomes and cover any potential non-linearities and asymmetries within the different Bank's portfolios.

9.1 Sensitivity analysis

The most significant assumptions affecting the expected credit loss allowance are as follows:

- Corporate portfolios
- Gross domestic product
- Unemployment rate
- Long term government bond rate
- Inflation rate
- Retail portfolios
- Gross domestic product
- Unemployment rate
- Real estate prices

10 Interim Provisions and Alignment with the Requirements of the Croatian National Bank

Changes in accounting policies resulting from the adoption of the IFRS 9 will generally be applied retrospectively, except as described below.

- The Bank will take advantage of the exemption allowing it not to restate comparative information for prior periods with respect to classification and measurement (including impairment) changes. Differences in the carrying amounts of financial assets and financial liabilities resulting from the application of IFRS 9 are recognized in retained earnings as of 1 January 2018.
- The following assessments must be made on the basis of the facts and circumstances that exist at the date of initial application:
 - o determination of the business model in which a financial asset is held
 - o designation and revocation of previous designations of certain financial assets and financial liabilities measured at FVTPL.
 - o designation of certain strategic investments not held for trading as at FVOCI.

Notes to the financial statements (continued)

2. Basis of preparation (continued)

f) *Standards, interpretations and amendments to published standards that are not yet effective and were not used in preparation of these financial statements (continued)*

- In the Retail segment, the Bank will apply average provision coverage for the Stages 1 and 2 in accordance with the CNB methodology. Statistical models of lifetime PD assessment are based on own historical data in keeping with the RBI group directive for developing statistical risk parameter assessment models according to the IFRS 9.
- As the CNB's requirements are greater than the ones obtained on the basis of the statistical models of lifetime PD assessment in keeping with the RBI group directive, in the legal financial statements the Bank will apply the minimal 0.8% rate for exposures in the Stages 1 and 2 for the overall non-retail segment.

3. Significant accounting policies

The accounting policies summarized below have been applied consistently for all periods presented in these financial statements

Interest income and expense

Interest income and expense are recognised in profit or loss as they accrue, for all interest bearing financial instruments including those measured at amortised cost, at fair value through profit or loss, available for sale, and the interest income component of finance lease receivables, using the effective interest rate method except for financial instruments at fair value through profit or loss, where interest is accrued at the coupon rate. Such income and expense is presented as interest income or interest expense in profit or loss. Interest income and expense also include fee and commission income and expense in respect of loans provided to customers or borrowings from other banks, premium or discount amortisation, and other differences between the initial carrying amount of an interest bearing financial instrument and its value at maturity, recognised on an effective interest basis. Interest income and expense on all trading assets and liabilities are presented as interest income or expense.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and method of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that discounts estimated future cash payments or receipts over the expected life of the financial instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group does not consider future credit losses. The calculation includes all fees and percentage points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Fee and commission income and expense

Fee and commission income and expense arises on financial services provided by the Group and received by the Group, and mainly comprises fees related to domestic and foreign payments, the issue of guarantees and letters of credit, credit card business and other services provided by and to the Group including asset management and custodial services. Fee and commission income and expense are recognised in profit or loss when the related service is performed.

Loan commitment fees for loans that are likely to be drawn down are deferred (together with related direct costs) and recognised as an adjustment to the effective interest rate on the loan. Commitment fees in relation to facilities where draw down is not probable are recognised over the term of the commitment. Loan syndication fees are recognised as revenue when the syndication has been completed and the Group has retained no part for itself, or has retained a part at the same effective interest rate as the other participants. Portfolio and other management advisory and service fees are recognised based on the applicable service contracts. Asset management fees related to investment fund management are recognised on an accruals basis over the period in which the service is provided. The same principle is applied for custody services that are continuously provided over an extended period of time.

Notes to the financial statements (continued)

3. Significant accounting policies (continued)

Dividend income

Dividend income from equity securities or, in the case of the Parent's separate financial statements, investments in subsidiaries, is recognised in profit or loss when the rights to receive the dividend are established.

Gains less losses from trading and investment financial instruments

Gains less losses from trading securities include unrealized and realized gains and losses arising from derivative financial instruments, trading debt securities and other financial instruments initially designated at fair value through profit or loss.

Gains less losses arising from investment securities comprise of realised gains and losses from financial assets available for sale.

Gains less losses arising from dealing in foreign currencies

Gains less losses from dealing in foreign currencies include unrealized and realized gains and losses arising from spot trading in foreign currencies.

Foreign currency transactions

Transactions in foreign currencies are translated to the functional currency at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate at that date. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated to the functional currency at the exchange rate at the date that the fair value was determined. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of transaction and are not retranslated. Foreign currency differences arising on translation are recognised in profit or loss, except for differences arising on the translation of available for sale equity instruments, which are recognised in profit or loss (refer below).

Changes in the fair value of monetary (debt) securities denominated in or linked to foreign currency classified as available for sale are analysed between translation differences resulting from changes in the amortised cost of the security and other changes in the carrying amount of the security. Translation differences are recognised in income as a part of the foreign exchange gains or losses on the revaluation of monetary assets and liabilities presented within financial income or financial expense in the profit or loss. Other changes in the carrying amounts are recognised in profit or loss. The translation differences on revaluation of non-monetary financial assets denominated in or linked to foreign currency classified as available for sale are recognised in other comprehensive income, along with other changes in their fair value.

Notes to the financial statements (continued)

3. Significant accounting policies (continued)

Financial instruments: classification

The Group classifies its financial instruments in the following categories: at fair value through profit or loss, loans and receivables, available for sale, held to maturity or other financial liabilities. The classification depends on the purpose for which the financial instruments were acquired. The management determines the classification of financial instruments upon initial recognition, and, where appropriate, re-evaluates this designation at every reporting date.

a) Financial assets and financial liabilities at fair value through profit or loss

This category comprises: financial instruments held for trading (including derivatives), and those designated by management as at fair value through profit or loss at inception. The Group designates financial assets and liabilities at fair value through profit or loss when:

- the assets or liabilities are managed, evaluated and reported internally on a fair value basis;
- the designation eliminates or significantly reduces an accounting mismatch that would otherwise arise; or
- the asset or liability contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

Financial instruments at fair value through profit or loss include debt and equity securities, investments in investment funds and derivatives.

b) Loans and receivables

This category comprises non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money to a debtor with no intention of trading with the receivable and include loans to and receivables from banks, loans to and receivables from customers, and the obligatory reserve with the CNB.

c) Financial instruments held to maturity

This category comprises non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group has the positive intention and ability to hold to maturity. These include purchased loans and receivables and some debt securities.

The Group will not classify financial assets as held to maturity if during the current financial year or during the previous two financial years, more than an insignificant amount of financial instruments held to maturity was sold or reclassified from financial instruments, other than sales or reclassifications that:

- are close to maturity and date of the call for sale of financial assets;
- arise after the Group mainly collected all the original principal of the financial assets through planned payments or early settlement; or
- can be linked to an isolated event beyond the control of the Group which is not repeated and that could not be reasonably anticipated by the Group.

d) Financial assets available for sale

This category comprises non-derivative financial assets which are designated as available for sale or are not designated as loans and receivables, held-to-maturity investments, or financial assets at fair value through profit or loss. Financial assets designated as available for sale are intended to be held for an indefinite period of time, but may be sold in response to needs for liquidity or changes in interest rates, foreign exchange rates, or equity prices. Available-for-sale financial assets include certain debt and equity securities.

e) Other financial liabilities

Other financial liabilities comprise all financial liabilities which are not designated at fair value through profit or loss.

Notes to the financial statements (continued)

3. Significant accounting policies (continued)

Financial instruments: reclassification

No transfers of derivatives and financial instruments initially designated as at fair value through profit and loss are allowed to other portfolios. Financial assets held for trading may be reclassified from this category in the case when both of the following two conditions are met: a change in the intended purpose of the assets and an extraordinary event. In such case, the fair value at the reclassification date becomes the new cost/amortised cost. Reclassification is possible to the available-for-sale portfolio, the held-to-maturity portfolio and the loans and receivables portfolio. Transfers from other portfolios to the portfolio at fair value through profit and loss are not possible.

Financial asset classified as available for sale that would have met the definition of loans and receivables (if it had not been designated as available for sale) may be reclassified out of the available-for-sale category to the loans and receivables category if the entity has the intention and ability to hold the financial asset for the foreseeable future or until maturity. For a financial asset reclassified out of the available-for-sale category, any previous gain or loss on that asset that has been recognised in other comprehensive income shall be amortised to profit or loss over the remaining life of the asset using the effective interest method.

Financial instruments: recognition and de-recognition

Purchases and sales of financial assets and financial liabilities at fair value through profit or loss, and financial assets held to maturity and available for sale, are recognised on the settlement date. Loans and receivables and financial liabilities at amortised cost are recognised when loaned or borrowed.

The Group de-recognises financial instruments (in full or part) when the rights to receive cash flows from the financial instrument have expired or when it loses control over the contractual rights over financial assets. It occurs when the Group transfers substantially all the risks and rewards of ownership to another business entity or when the rights are realised, surrendered or have expired.

The Group de-recognises financial liabilities only when the financial liability ceases to exist, i.e. when it is discharged, cancelled or has expired. If the terms of a financial liability change, the Group will cease recognising that liability and will instantaneously recognise a new financial liability, with new terms and conditions.

Realised gains and losses from the disposal of financial instruments are calculated by using the weighted average cost method.

Notes to the financial statements (continued)

3. Significant accounting policies (continued)

Financial instruments: initial and subsequent measurement

Financial assets and liabilities are recognised initially at their fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

After initial recognition, the Group measures financial instruments at fair value through profit or loss and available for sale at their fair value, without any deduction for selling costs. Equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are measured at cost, less impairment if needed.

Loans and receivables and held-to-maturity investments and financial liabilities not designated at fair value through profit or loss are measured at amortised cost using the effective interest method, less eventually impairment.

Financial instruments: gains and losses

Gains or losses arising from a change in the fair value of financial assets or financial liabilities at fair value through profit or loss are recognised in profit or loss.

Gains or losses from a change in the fair value of available-for-sale monetary assets are recognised directly in a fair value reserve within other comprehensive income and are disclosed in the statement of changes in equity. Impairment losses, foreign exchange gains and losses, interest income and amortisation of premium or discount using the effective interest method on available-for-sale monetary assets are recognised in profit or loss. Foreign exchange differences on equity instruments are part of the fair value of these instruments and are recognised in other comprehensive income. Dividend income is recognised in profit or loss. Upon sale or other derecognition of available-for-sale assets, any cumulative gains or losses on the instrument are transferred to profit or loss.

Gains or losses arising from financial assets and financial liabilities carried at amortised cost are recognised as interest in profit or loss over the period of amortisation. Gains or losses may also be recognised in profit or loss when a financial instrument is derecognised or when its value is impaired.

Netting

Financial assets and liabilities are offset and the net amount is reported in the statement of financial position when the Group has a legally enforceable right to set off the recognised amount and the transactions are intended to be settled on a net basis, or to release the assets and settle the liabilities simultaneously.

Fair value measurement principles

The fair value of quoted financial instruments in an active market is based on their closing bid prices. If there is no active market for the financial instrument, or if, due to any other reason, the fair value cannot be reliably measured by the market price, the Group uses an internal evaluation model for fair value estimation as described in Note 48. Such models include the use of prices achieved in recent transactions, reference to similar financial instruments, and discounted cash flow analysis, making maximum use of market inputs and relying as little as possible on entity-specific inputs. Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimate and the discount rate is a market rate.

The fair value of non-exchange-traded derivatives is estimated at the amount that the Group would receive or pay to terminate the contract on date of reporting taking into account current market conditions and the current creditworthiness of the counterparties.

Notes to the financial statements (continued)

3. Significant accounting policies (continued)

Impairment of financial assets

Financial assets carried at amortised cost and finance lease and operating lease receivables

The Group assesses at each reporting date whether there is objective evidence that a financial asset or group of financial assets not carried at fair value through profit or loss is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a "loss event") and that loss event (or events) has an impact on the estimated future cash flows of the financial asset that can be reliably estimated. Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the Group about the following loss events:

- i) significant financial difficulty of the borrower;
- ii) a breach of contract, such as a default or delinquency in interest or principal payments;
- iii) the restructuring of a loan or advance by the Group on terms that the Group would not otherwise consider;
- iv) significant restructuring due to financial difficulty or expected bankruptcy of the borrower;
- v) the disappearance of an active market for the financial asset because of financial difficulties;

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity investments carried at amortised cost has incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate or using the rates prescribed by Croatian National Bank. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. Provisions for impairment losses on a collective basis are calculated based on percentage prescribed by the CNB for the Raiffeisenbank Austria d.d. Zagreb and Raiffeisen Building Society d.d. and based on RBI methodology for other subsidiaries.

If in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.

When a loan is uncollectible, it is written off through the related provisions for impairment losses. Loans are written off after all the necessary procedures and determining the amount of loss. Additional collection of the previous written off amounts are recognised as reversal of the impairment loss in the income statement.

When possible, the Bank seeks to restructure loans rather than to take possession of collateral. This can prolong the payback deadline and change of loan terms. Once the terms have been renegotiated any impairment is measured using the original effective interest rate as calculated before the modification of terms and the loan is no longer considered past due. Management continually reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, if they are not already impaired on individual or collective basis, using the loan's original effective interest rate. Similar analysis is undertaken for finance and operating lease receivables, related predominantly to subsidiary Raiffeisen Leasing.

Financial assets available for sale

The Group assesses at each reporting date whether there is objective evidence that a financial asset available for sale is impaired. In the case of equity investments classified as available for sale, a significant or prolonged decline in the fair value of the investment below its cost is considered in determining whether the assets are impaired. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the income statement. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is subsequently recognised in other comprehensive income rather than profit or loss until final derecognition.

Notes to the financial statements (continued)

3. Significant accounting policies (continued)

Specific financial instruments

a) Cash and cash equivalents

Cash and cash equivalents comprise cash balances on hand, cash deposited with central banks, placements with other banks with original maturities of three months or less and items in course of collection and are carried at amortised cost in the statement of financial position.

b) Derivative financial instruments

The Group uses derivative financial instruments to hedge economically its exposure to currency risk and interest rate risk arising from operating, financing and investing activities and through hedge accounting. In accordance with its investment policies, the Group holds or issues a limited number of derivative financial instruments for the purpose of trading.

Derivative financial instruments include foreign currency agreements, forward and forward rate agreements, futures, interest rate swaps, cross currency swaps, options and other financial derivatives and are initially recognised at fair value which is the value of consideration paid to acquire the instrument less transaction costs. Subsequent to initial recognition, derivatives are measured at fair value. The fair value is determined based on the quoted market price or, if more appropriate, based on discounted cash flow calculations. All derivative instruments are presented as assets if their fair value is positive and as liabilities if their fair value is negative.

Some hybrid contracts contain both a derivative and a non-derivative component. In such cases, the derivative component is termed an embedded derivative. An embedded derivative is treated as a separate derivative and classified at fair value through profit or loss, except where its recognition is not in conflict with the requirements of the CNB, when the economic characteristics and risks of the embedded derivatives are not closely related to the host contract and where the hybrid contract itself is not measured at fair value through profit or loss with the presentation of all unrealised gains and losses in profit or loss unless there is a reliable fair value measure.

Changes in the fair value of derivatives are included in net trading income.

Hedge accounting

At the inception of a hedge relationship, the Group formally designates and documents the hedge relationship to which it wishes to apply hedge accounting and the risk management objective and strategy for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the effectiveness of changes in the hedging instrument's fair value in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk. Such hedges are expected to be highly effective in achieving offsetting changes in fair value or cash flows and are assessed on an ongoing basis to determine that they actually have been highly effective throughout the financial reporting periods for which they were designated.

Hedges that meet the strict criteria for hedge accounting are accounted for and further described in the below sections.

Fair value hedge

Fair value hedges are hedges of the Group's exposure to changes in the fair value of a recognised asset or liability or an unrecognised firm commitment, or an identified portion of such an asset, liability or firm commitment, that is attributable to a particular risk and could affect profit or loss.

Changes in fair value of derivatives designated and eligible as fair value hedges are recognised immediately in profit or loss, together with any changes in fair value of the hedged items i.e. hedged liability which can be associated with hedged risk. The change in the fair value of a hedge instrument is recognised in profit or loss, together with the change in the fair value of a hedge item related to risk being hedged.

The Group discontinues fair value hedge accounting if the hedging instrument expires or is sold, terminated or exercised, the hedge no longer meets the criteria for hedge accounting or the Group revokes the designation. Since that day any adjustment of a carrying amount of a hedge item referring to the changes of a fair value related to risk being hedged is amortized through profit and loss.

If the hedged item is derecognize, the unamortized fair value is recognized immediately in profit and loss.

Notes to the financial statements (continued)

3. Significant accounting policies (continued)

Specific financial instruments (continued)

c) Treasury bills and debt securities

Treasury bills and debt securities that the Group holds for the purpose of short-term profit taking are classified as trading financial instruments, included as financial instruments at fair value through profit or loss at inception. Treasury bills that the Group has the intent and ability to hold to maturity are classified as held-to-maturity assets. Other treasury bills and debt securities are classified as available for sale.

d) Equity securities and investments in open ended investment funds

Equity securities and investments in open ended investment funds are classified as at fair value through profit or loss or available for sale.

e) Placements with banks

Placements with banks are classified as loans and receivables and are carried at amortised cost less impairment losses.

f) Loans and advances to customers

Loans and advances are presented at amortised cost less net of impairment losses.

In accordance with CNB requirements, the amortisation of any discounts included within impairment losses is included in impairment losses.

g) Investments in subsidiaries and associates

Investments in subsidiaries and associates are accounted at cost less impairment in the separate financial statements of the Bank. Investments in subsidiaries are fully consolidated in the consolidated financial statements of the Group whilst investments in associates are accounted for under the equity method.

h) Borrowings

Interest-bearing borrowings are recognised initially at fair value, less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between proceeds (net of transaction costs) and redemption value being recognised in profit or loss over the period of the borrowings on an effective interest basis.

Notes to the financial statements (continued)

3. Significant accounting policies (continued)

Specific financial instruments (continued)

i) Repurchase and sale buy-back agreements

The Group enters into purchases/(sales) of investments under agreements to resell (repurchase) substantially identical investments at a certain date in the future at a fixed price. Investments purchased subject to such commitments to resell them at future dates are not recognised. The amounts paid are recognised in loans and advances to either banks or customers. The receivables are shown as collateralised by the underlying security. Investments sold under repurchase agreements continue to be recognised in the statement of financial position and are measured in accordance with the accounting policy for the relevant financial asset at amortised cost or at fair value as appropriate. The proceeds from the sale of the investments are reported as liabilities to either banks or customers.

The difference between the sale and repurchase consideration is recognised on an accrual basis over the period of the transaction and is included in interest income or expense.

The Group also enters into linked sale and buy-back transactions. In accordance with their substance, these are similarly accounted for as transactions under repurchase or resale agreements, as described above.

j) Current accounts and deposits from banks and customers

Current accounts and deposits are classified as other liabilities and initially measured at fair value plus transaction costs, and subsequently stated at their amortised cost using the effective interest method.

Income tax

The income tax charge is based on taxable profit for the year and comprises current and deferred tax. Income tax is recognised in profit or loss except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity. Current tax is the expected tax payable on the taxable income for the year, using the tax rates enacted or substantially enacted at date of reporting, and any adjustments to tax payable in respect of previous years.

Deferred taxes are calculated by using the balance sheet liability method. Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Deferred tax assets and liabilities are measured by using the tax rates expected to apply to taxable profit in the years in which those temporary differences are expected to be recovered or settled based on tax rates enacted or substantially enacted at date of reporting.

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

Deferred tax assets and liabilities are not discounted and are classified as non-current assets and/or liabilities in the statement of financial position. Deferred tax assets are recognised when it is probable that sufficient taxable profits will be available against which the deferred tax assets can be utilised. At each statement of financial position date, the Group reassesses unrecognised potential deferred tax assets and the carrying amount of recognised deferred tax assets.

Additional income taxes that arise from the distribution of dividends are recognised at the same time as the liability to pay the related dividend.

Notes to the financial statements (continued)

3. Significant accounting policies (continued)

Property, plant and equipment

Items of property, plant and equipment are stated at historical cost or deemed cost, less accumulated depreciation and, if any, impairment losses.

The Group recognises in the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if it is probable that future economic benefits embodied with the item will flow to the Group and the cost of the item can be measured reliably. All other expenditure on repairs and maintenance is expensed as incurred.

Leases in terms of which the Group as a lessor assumes substantially all the risks and rewards of ownership are classified as operating leases. Plant and equipment acquired in connection with such leases are stated at an amount equal to the lower of their fair value and the present value of the minimum lease payments at inception of the leases, less accumulated depreciation and impairment losses. Assets under operating leases are depreciated on a straight line basis so as to write down the cost of the assets over the estimated lease period to their recoverable residual value.

Depreciation is provided on a straight-line basis to allocate the costs of assets to their residual values over their estimated economic useful life. Land and assets under construction or developed are not depreciated. The estimated useful lives are as follows.

| | 2017 | 2016 |
|--|--------------|--------------|
| Buildings | 50 years | 50 years |
| Equipment | 4 – 10 years | 4 – 10 years |
| Office furniture | 4 years | 4 years |
| Assets under operating leases (depending on the duration of the contract, depreciated to the residual value) | 2 – 20 years | 2 – 20 years |

The assets' residual values, depreciation method and useful lives are reviewed, and adjusted if appropriate, at each statement of financial position date. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses on disposals are determined by comparing proceeds with carrying amount, and are included in profit or loss.

Property investments

Investment property held by the Group to earn rentals or for capital appreciation, including assets under construction for the intended use, is initially measured at cost, and subsequently reduced by accumulated depreciation and any impairment losses.

Subsequent cost of replacing part of an existing asset is recognized in the carrying amount of an investment property at the time that cost is incurred, when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are expensed during the period in which they are incurred. Where parts of property and equipment of significant value have different useful lives, they are accounted for as separate items of property, plant and equipment.

Land and assets under construction are not depreciated. Depreciation is provided on other investment property on a straight-line basis at prescribed rates designed to write off the cost over the estimated useful life of the asset.

| The estimated useful life of the assets is as follows: | 2017 | 2016 |
|--|----------|----------|
| Leased property | 50 years | 50 years |

Remaining value, depreciation methods and the estimated useful life are reviewed periodically and reconciled, if necessary, at every financial position reporting date. If the carrying amount of the assets is found to be higher than the assessed recoverable amount, it is immediately written-off to the recoverable amount. Gains and losses from alienation are assessed by comparing sale revenues against the book amount and recorded in the comprehensive income.

Notes to the financial statements (continued)

3. Significant accounting policies (continued)

Inventory and foreclosed assets

The Group occasionally acquires real estate and other asset in settlement of certain loans and advances and finance and operating lease contracts, which also includes returned leased assets of the subsidiary Raiffeisen Leasing d.o.o.. Such real estate and other assets are stated at the lower of the net carrying of the related loans and advances and the current fair value of such assets. Subsequent measurement is at the lower of cost and recoverable amount. The Group's intention is mainly to sell such assets, however, such assets in certain limited cases may end up being used by the Group. Gains or losses on disposal are recognised in profit or loss.

Intangible assets

Intangible assets are stated at cost less accumulated amortisation and impairment losses. Expenditure on development activities are capitalised if all of the features required by IAS 38 "Intangible assets" are satisfied. Depreciation is provided on a straight-line basis over the estimated useful lives of intangible assets. Costs associated with developing or maintaining intangible assets are recognised as an expense as incurred. In accordance with CNB regulations, intangible assets include leasehold improvements.

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

| | 2017 | 2016 |
|------------------------|--------------|--------------|
| Leasehold improvements | 1 - 20 years | 1 - 20 years |
| Software | 5 - 8 years | 5 - 8 years |

Impairment of non-financial assets

The carrying amounts of the Group's non-financial assets, other than deferred tax assets are tested for impairment at each reporting date.

If any indication exists, the asset's recoverable amount is estimated. For assets that have an indefinite useful life and intangible assets that are not yet available for use and goodwill, the recoverable amount is estimated at each reporting date.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that are largely independent from the Group's other assets and liabilities. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of cash-generating units are allocated to reduce the carrying amount of the assets in the unit (group of units) on a pro rata basis.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their net present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised. Once recognised impairment loss of goodwill is not subsequently reversed.

Notes to the financial statements (continued)

3. Significant accounting policies (continued)

Provisions for liabilities and charges

The Group recognises a provision when it has a present obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the obligation.

Provisions are recognised when the Group has a present obligation as a result of a past event, and it is probable that the Group will be required to settle that obligation. The management determines the adequacy of the provision based upon reviews of individual items, recent loss experience, current economic conditions, the risk characteristics of the various categories of transactions and other pertinent factors.

Provisions are released only for such expenditure in respect of which provision are recognised at inception. If the outflow of economic benefits to settle the obligations is no longer probable, the provision is reversed.

Leases-Group as lessor

a) Finance leases

Leases where the Group as lessor transfers substantially all the risks and rewards incidental to ownership to the lessee are classified as finance leases. A receivable at an amount equal to the present value of the lease payments, including any guaranteed residual value, is recognised. The difference between the gross receivable and the present value of the receivable is unearned finance income and is recognised over the term of the lease using the effective interest rate method. Finance lease receivables are included in loans and advances to customers.

b) Operating leases

Leases where the Group as lessor retains substantially all the risks and rewards incidental to ownership are included in tangible and intangible assets at cost net of accumulated depreciation. Rental income under operating leases is recognised in profit or loss on a straight-line basis over the term of the lease.

Employee benefits

a) Defined pension contributions

The Group pays contributions to mandatory pension plans on a mandatory, contractual basis. The Group has no further payment obligations once the contributions have been paid. The contributions are recognised as employee benefit expense when they are due. Since the Group records severance payments and jubilee awards based on actuarial calculations, all gains and losses from increases and decreases in the present value of the defined benefit obligation, which arise from actuarial risks, are recorded through other comprehensive income.

b) Long-term service benefits

The Bank provides employees with one-off retirement awards. The liability and costs of these benefits are determined by using a projected unit credit method. The projected unit credit method considers each period of service as giving rise to an additional unit of benefit entitlement and measures each unit separately to build up the final obligation. The liability is measured at the present value of estimated future cash flows using a discount rate that is similar to the interest rate on government bonds where the currency and terms of the government bonds are consistent with the currency and estimated terms of the benefit obligation.

Notes to the financial statements (continued)

3. Significant accounting policies (continued)

Employee benefits (continued)

c) Pension insurance

Pension insurance provisions of subsidiary Raiffeisen mirovinsko osiguravajuće društvo d.o.o. have been computed by the company's licensed actuary, in accordance with the method prescribed by the Law on Pension Insurance Companies and Payment of Pensions based on Individual Capitalised Savings.

Dividends

Dividends are recognised when declared by shareholders in General Assembly meeting.

Share capital

Share capital represents the nominal value of paid-in ordinary and non-redeemable noncumulative preference shares classified as equity, on which dividends are payable at the discretion of the ordinary shareholders, and are stated in HRK at nominal value.

Treasury shares

When the Bank repurchases ordinary or preference shares, the consideration paid is deducted from equity attributable to the Bank's equity holders until the shares are cancelled, reissued or disposed of. When such shares, which are classified as treasury shares, are subsequently sold or reissued, any consideration received, net of transaction costs, is included in equity attributable to the Bank's equity holders.

Retained earnings

Any profit for the year after appropriations is transferred to reserves, in accordance with General Assembly decisions.

Earnings per share

The Bank presents earnings per share (EPS) data for its ordinary shares. EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the period.

Off-balance-sheet commitments and contingent liabilities

In the ordinary course of business, the Group enters into credit related commitments which are recorded in off-balance-sheet accounts and primarily include guarantees, letters of credit and undrawn loan commitments. Such financial commitments are recorded in the Group's statement of financial position if and when they become payable.

Managed funds for and on behalf of third parties

The Group manages assets on behalf of other companies and individuals for which a fee is charged. As these assets do not represent assets of the Group, they are excluded from the statement of financial position.

Notes to the financial statements (continued)

4. Significant accounting estimates and judgments

The Group makes estimates and assumptions about uncertain events, including estimates and assumptions about the future. Such accounting assumptions and estimates are regularly evaluated, and are based on historical experience and other factors such as the expected flow of future events that can be rationally assumed in existing circumstances, but nevertheless necessarily represent sources of estimation uncertainty. The estimation of impairment losses in the Bank's credit risk portfolio represents the major source of estimation uncertainty. This and other key sources of estimation uncertainty, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below. Significant judgments made in determining the most appropriate methodology for estimating the fair value of financial instruments carried at fair value, and other significant judgments affecting how items and transactions are accounted for, are also described below.

Impairment allowance on loans and receivables

The Bank monitors the creditworthiness of its customers on an ongoing basis. In accordance with CNB regulations, the need for impairment of the Bank's on- and off-balance-sheet credit risk exposure is assessed at least quarterly. Impairment losses are made mainly against the carrying value of loans and advances to corporate and retail customers (summarised in Note 11), placements with and loans to other banks (Note 9) and as provisions for liabilities and charges arising from off-balance-sheet risk exposure to customers, mainly in the form of guarantees and documentary letters of credits (summarised in Notes 23 and 43). Impairment losses are also considered for other assets not carried at fair value, where the primary risk of impairment is not credit risk. Reduction of provisions for impairment losses from on-balance-sheet exposure for the Bank and the Group in 2017 refers primarily to the Bank selling a part of the non-performing credit portfolio.

| Summary of impairment allowance | Notes | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|---|----------------|--|--|---|---|
| Impairment provisions for on-balance-sheet exposure | 6,7,9,11,12,17 | 2,134 | 2,853 | 1,563 | 2,737 |
| Provision for off-balance-sheet exposure | 23 | 93 | 103 | 93 | 103 |
| | | 2,227 | 2,956 | 1,656 | 2,840 |

Financial assets carried at amortised cost

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

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

Notes to the financial statements (continued)

4. Significant accounting estimates and judgements (continued)

Financial assets carried at amortised cost (continued)

The Group takes into consideration the combined effect of several events when assessing impairment and uses its experienced judgement in cases where the observable data required to estimate impairment is limited. In estimating impairment losses on items individually or collectively assessed as impaired, the Group, gives due regard to the ranges prescribed by the CNB based on the past due days. In estimating impairment losses on items individually assessed as impaired for corporate portfolio the Group uses discounted cash flow model.

At the year end, gross carrying amount of specifically impaired loans to customers, contractual and contingent liabilities and other assets, and the rate of impairment were as follows:

| | 2017 | | | 2016 | | |
|--|-----------|--------|-------|-----------|--------|-------|
| | Corporate | Retail | Total | Corporate | Retail | Total |
| The Group | | | | | | |
| Gross carrying amount (in HRK millions) | 1,714 | 1,067 | 2,781 | 2,265 | 1,099 | 3,364 |
| Impairment rate (in %) | 71 | 62 | 68 | 78 | 74 | 77 |
| The Bank | | | | | | |
| Gross carrying amount (in HRK millions) | 1,043 | 1,046 | 2,089 | 2,168 | 1,081 | 3,249 |
| Impairment rate (in %) | 64 | 62 | 63 | 78 | 74 | 77 |

As previously clarified, decrease in gross exposure from non-performing loans refers primarily to the sale of a share in the Bank's non-performing credit portfolio in 2017, which resulted also in lowered average loan loss provision ratio and coverage in 2017, as these were high-provision loans.

Each additional increase of one percentage point in the impairment rate on the gross carrying amount of specifically identified impaired loans at 31 December 2017 would lead to the recognition of an additional impairment loss of HRK 20.9 million (2016: HRK 32.5 million) at the Bank level and an additional impairment loss of HRK 27.8million (2016: HRK 33.6 million) at the Group level.

The amount of impairment losses at 31 December 2017 estimated on a portfolio basis amounted to HRK 338 million (2016: HRK 351 million) of the relevant on-and off-balance-sheet exposure. The total of these portfolio based impairment losses amounted to 1.15% (2016: 1.24%) of Loans and advances to customers and to 1% (2016: 1%) on off-balance-sheet exposure, in both cases net of amounts individually assessed as impaired.

Fair value of derivatives

The fair value of OTC derivatives are determined by using valuation techniques. Where valuation techniques (for example, models) are used to determine fair values, they are validated and periodically reviewed by qualified personnel independent of the area that created them. All models are certified before they are used, and models are calibrated to ensure that outputs reflect actual data and comparative market prices.

Notes to the financial statements (continued)

4. Significant accounting estimates and judgments (continued)

a) Fair value of treasury bills

The Group and the Bank determine the fair value of treasury bills issued by the Ministry of Finance of the Republic of Croatia, using an internal model which considers their remaining maturity and the latest available auction prices of equivalent instruments. As at 31 December 2017, the carrying amount of treasury bills classified as financial assets at fair value through profit or loss and financial assets available for sale was HRK 909 million for the Group (2016: HRK 603 million) and HRK 821 million for the Bank (2016: HRK 537 million).

b) Provisions for severance payments

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

c) Provisions for court cases

Provisions are recognized when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of the obligation can be made. Provisions are maintained at the level that the Group's management considers sufficient for absorption of incurred losses and determines the sufficiency of provisions on the basis of insight into specific items, current legal circumstances, as well as other relevant factors.

According to the CNB decision a credit institution shall allocate litigation to risk groups A (no risk of loss established or a cash flow outflow or less than 10% of the total estimated amount), B (a risk of loss established or a cash outflow between 10% and 70% of total amount estimated) or C (high risk of loss established or a cash outflow of more than 70% of the total amount estimated). In determining the current value of future cash flows, taking into account all factors that have influenced or will influence the time value of money, the Bank applies legal penalty interest and CNB discount rate applicable for the last day of the half year preceding the current half year increased by 8 basis points for court cases led against the Bank by corporate entities, and 5 basis points for all other court cases led against the Bank.

Provisions for court cases are booked in profit or loss for the period in which the provision is recognized.

The Group and the Bank (Note 23) made a provision for court cases (for principal and interest) in the amount of HRK 68 million (2016: HRK 66 million) or HRK 59 million (2016: HRK 57 million). The management believes that the amount of provision created is sufficient. This amount represent the best estimate of the Group for litigation losses, although the actual loss of legal proceeding against the Group may be significantly different. It is not practical for the management to assess the financial impact of changes in the assumptions on the basis of which the management will assess the requirement for provisions.

d) Pension insurance

In accordance with the legal framework, the Group provides an opportunity for members of voluntary and mandatory pension funds to transfer funds, when the conditions are met, into pension insurance company of their choice. Raiffeisen mirovinsko osiguravajuće društvo d.d. is currently the only pension insurance company in Croatia. The pension company pays out pensions, in accordance with the Act on Pension Insurance Companies and conditions of concluded pension contracts under mandatory and voluntary pension insurance. Pensions are paid from the assets covering technical provisions calculated by the certified actuary of the pension insurance company and in accordance with the good actuarial practice and law. The Management believes that the calculated technical provisions are sufficient.

e) Deferred taxes

Deferred taxes are recognised in respect of tax losses and deductible temporary differences to the extent that it is probable that taxable profit will be available against which the losses can be utilised. The Management believes that the deferred tax assets recognised by the Bank and the Group are completely recoverable.

Notes to the financial statements (continued)

4. Significant accounting estimates and judgements (continued)

f) Classification of lease contracts

The Group is the lessor in operating and finance leases. Lease where the Group as lessor transfer substantially all the risks and rewards to the lessee than the contract is classified as finance lease. All other leases are classified as operating lease and included in property and equipment under operating leases at cost net of accumulated depreciation. The requirements of IAS 17 Leases are taken into consideration to determine whether lease should be classified as finance or operating lease.

g) Determination of control

In accordance with requirements of IFRS 10 Consolidated Financial Statements, the Group regularly reassess whether they have control over significant activities of debtors in financial difficulties which are unable to regularly service its liabilities to the Group. The Group concluded in 2017 that there are no debtors which should be consolidated, which is consistent with the conclusion reached in 2016.

h) Impairment of subsidiaries

The Bank assessed that investment in the subsidiary Raiffeisen Factoring d.o.o. underwent impairment due to considerable credit losses realised from factoring agreements with the Agrokor concern companies, which is under extraordinary management, and their economically connected suppliers and due to a fall in the factoring business volume. Total declared impairment was HRK 268 million in the Bank's separate financial statement. The Management believes that other investments in the subsidiaries are recoverable in full.

Notes to the financial statements (continued)

5. Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which are subject to risks and rewards that are different from those of other segments. Limited segment information is presented in respect of the Group's business segments. The primary format of business segments is based on the Bank's management and internal reporting structure.

Business segments

The Group comprises the following main business segments:

| | |
|--------------------------|---|
| <i>Corporate Banking</i> | Includes loans, deposits and other transactions and balances with corporate customers, and leasing activities at Group level; |
| <i>Retail Banking</i> | Includes loans, deposits and other transactions and balances with retail customers; |
| <i>Treasury</i> | Undertakes the Group's funding and centralised risk management activities through borrowings, issues of debt securities, use of derivatives for risk management purposes and investing in liquid assets such as short-term placements and corporate and government debt securities; |
| <i>Asset management</i> | Includes management of investment and pension funds under Group management; |
| <i>Shared services</i> | Undertakes Group property management activities and centralised advertising and marketing services for the Group. |

Notes to the financial statements (continued)

5. Segment reporting (continued)

| 2017 Group HRK millions | Corporate | Retail | Treasury | Asset manage- ment | Shared services | Unallocated | Total 2017 |
|---|---------------|---------------|---------------|--------------------------|--------------------|--------------|----------------|
| Net interest income | 243 | 517 | 106 | 24 | 23 | - | 913 |
| Net fee and commission income | 161 | 121 | 15 | 168 | 4 | - | 469 |
| Trading and other income | 214 | 27 | 70 | 162 | 19 | - | 492 |
| Operating income | 618 | 665 | 191 | 354 | 46 | - | 1,874 |
| Operating expenses | (377) | (477) | (66) | (242) | (35) | (15) | (1,212) |
| Impairment losses on Loans and advances to customers and other assets | (431) | 44 | - | - | 1 | - | (386) |
| Provisions for liabilities and charges | 10 | 6 | - | - | - | (2) | 14 |
| Operating expenses | (798) | (427) | (66) | (242) | (34) | (17) | (1,584) |
| Profit/(loss) before tax | (180) | 238 | 125 | 112 | 12 | (17) | 290 |
| Income tax expense | - | - | - | - | - | (102) | (102) |
| Profit/(loss) for the year | (180) | 238 | 125 | 112 | 12 | (119) | 188 |
| Segment assets | 8,085 | 9,300 | 12,931 | 624 | 1,178 | - | 32,118 |
| Unallocated assets | - | - | - | - | - | 2,060 | 2,060 |
| Total assets | 8,085 | 9,300 | 12,931 | 624 | 1,178 | 2,060 | 34,178 |
| Segment liabilities | 11,354 | 13,368 | 2,917 | 472 | 1,158 | 224 | 29,493 |
| Equity | - | - | - | - | - | 4,685 | 4,685 |
| Total equity and liabilities | 11,354 | 13,368 | 2,917 | 472 | 1,158 | 4,909 | 34,178 |

Notes to the financial statements (continued)

5. Segment reporting (continued)

| 2016 Group HRK millions | Corporate | Retail | Treasury | Asset manage-ment | Shared services | Unallocated | Total 2016 |
|---|---------------|---------------|---------------|----------------------|--------------------|--------------|----------------|
| Net interest income | 304 | 513 | 123 | 25 | 23 | - | 988 |
| Net fee and commission income | 164 | 117 | 2 | 151 | 3 | - | 437 |
| Trading and other income | 278 | 103 | 97 | 139 | 15 | 5 | 637 |
| Operating income | 746 | 733 | 222 | 315 | 41 | 5 | 2,062 |
| Operating expenses | (456) | (1.121) | (43) | (220) | (35) | (2) | (1.877) |
| Impairment losses on Loans and advances to customers and other assets | (123) | 2 | 13 | - | 1 | - | (107) |
| Provisions for liabilities and charges | 11 | 609 | (3) | - | - | - | 617 |
| Operating expenses | (568) | (510) | (33) | (220) | (34) | (2) | (1.367) |
| Profit/(loss) before tax | 178 | 223 | 189 | 95 | 7 | 3 | 695 |
| Income tax expense | - | - | - | - | - | (160) | (160) |
| Profit/(loss) for the year | 178 | 223 | 189 | 95 | 7 | (157) | 535 |
| Segment assets | 8.820 | 9.309 | 13.107 | 601 | 1.181 | - | 33.018 |
| Unallocated assets | - | - | - | - | - | 2.346 | 2.346 |
| Total assets | 8.820 | 9.309 | 13.107 | 601 | 1.181 | 2.346 | 35.364 |
| Segment liabilities | 12.867 | 13.341 | 2.432 | 436 | 1.206 | 192 | 30.474 |
| Equity | - | - | - | - | - | 4.890 | 4.890 |
| Total equity and liabilities | 12.867 | 13.341 | 2.432 | 436 | 1.206 | 5.082 | 35.364 |

Notes to the financial statements (continued)

5. Segment reporting (continued)

| 2017 Bank HRK millions | Corporate | Retail | Treasury | Unallocated | Total 2017 |
|---|------------------|---------------|-----------------|--------------------|-----------------------------|
| Net interest income | 233 | 517 | 106 | - | 856 |
| Net fee and commission income | 173 | 121 | 15 | - | 309 |
| Trading and other income | 105 | 27 | 142 | - | 274 |
| Operating income | 511 | 665 | 263 | - | 1,439 |
| Operating expenses | (280) | (477) | (66) | (282) | (1,105) |
| Impairment losses | 83 | 44 | - | - | 127 |
| Provisions for liabilities and charges | 10 | 6 | - | (2) | 14 |
| Operating expenses | (187) | (427) | (66) | (284) | (964) |
| Profit/(loss) before tax | 324 | 238 | 197 | (284) | 475 |
| Income tax expense | - | - | - | (79) | (79) |
| Profit/(loss) for the year | 324 | 238 | 197 | (363) | 396 |
| Segment assets | 7,926 | 9,300 | 12,931 | - | 30,157 |
| Unallocated assets | | | | 1,222 | 1,222 |
| Total assets | 7,926 | 9,300 | 12,931 | 1,222 | 31,379 |
| Segment liabilities | 10,412 | 13,368 | 2,917 | 224 | 26,921 |
| Equity | - | - | - | 4,458 | 4,458 |
| Total equity and liabilities | 10,412 | 13,368 | 2,917 | 4,682 | 31,379 |
| 2016 Bank HRK millions | Corporate | Retail | Treasury | Unallocated | Total 2016 |
| Net interest income | 261 | 513 | 123 | - | 897 |
| Net fee and commission income | 178 | 117 | 2 | - | 297 |
| Trading and other income | 86 | 103 | 169 | 5 | 363 |
| Operating income | 525 | 733 | 294 | 5 | 1,557 |
| Operating expenses | (315) | (1,121) | (43) | (2) | (1,481) |
| Impairment losses | (123) | 2 | 13 | - | (108) |
| Provisions for liabilities and charges | 11 | 609 | (3) | - | 617 |
| Operating expenses | (427) | (510) | (33) | (2) | (972) |
| Profit/(loss) before tax | 98 | 223 | 261 | 3 | 585 |
| Income tax expense | - | - | - | (125) | (125) |
| Profit/(loss) for the year | 98 | 223 | 261 | (122) | 460 |
| Segment assets | 7,692 | 9,309 | 13,107 | - | 30,108 |
| Unallocated assets | - | - | - | 1,308 | 1,308 |
| Total assets | 7,692 | 9,309 | 13,107 | 1,308 | 31,416 |
| Segment liabilities | 11,000 | 13,341 | 2,432 | 193 | 26,966 |
| Equity | - | - | - | 4,450 | 4,450 |
| Total equity and liabilities | 11,000 | 13,341 | 2,432 | 4,643 | 31,416 |

Notes to the financial statements (continued)

6. Cash and current accounts with banks

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|---|----------------------------------|----------------------------------|---------------------------------|---------------------------------|
| Cash in hand | 804 | 712 | 804 | 712 |
| Items in the course of collection | - | 1 | - | 1 |
| Giro account with the Croatian National Bank | 3,851 | 2,969 | 3,851 | 2,969 |
| Current accounts with other banks | | | | |
| - with parent bank | 10 | 4 | 9 | 3 |
| - with other Raiffeisen Bank International AG ("the RBI") group banks | 4 | 5 | 4 | 5 |
| - with other banks | 78 | 66 | 78 | 63 |
| | 4,747 | 3,757 | 4,746 | 3,753 |
| Impairment allowance | (39) | (36) | (39) | (36) |
| | 4,708 | 3,721 | 4,707 | 3,717 |

a) Movement in impairment allowance for cash and current accounts with banks

| | Group 2017 HRK millions | Group 2016 HRK millions | Unidentified losses Bank 2017 HRK millions | Bank 2016 HRK millions |
|---|----------------------------------|----------------------------------|--|---------------------------------|
| At 1 January | 36 | 24 | 36 | 24 |
| Net charge recognised in profit or loss (Note 33) | 3 | 12 | 3 | 12 |
| At 31 December | 39 | 36 | 39 | 36 |

7. Obligatory reserve with the Croatian National Bank

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|---|----------------------------------|----------------------------------|---------------------------------|---------------------------------|
| Obligatory reserve in domestic currency | 1,757 | 1,695 | 1,757 | 1,695 |
| | 1,757 | 1,695 | 1,757 | 1,695 |
| Impairment allowance | (18) | (20) | (18) | (20) |
| | 1,739 | 1,675 | 1,739 | 1,675 |

Notes to the financial statements (continued)

7. Obligatory reserve with the Croatian National Bank (continued)

a) Movement in impairment allowance for obligatory reserve with the Croatian National Bank

| | Unidentified losses | | | |
|--|----------------------------------|----------------------------------|---------------------------------|---------------------------------|
| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
| At 1 January | 20 | 25 | 20 | 25 |
| Net (release)/charge recognised in profit or loss (Note 33) | (2) | (5) | (2) | (5) |
| At 31 December | 18 | 20 | 18 | 20 |

The Croatian National Bank ("the CNB") determines the requirement for banks to calculate obligatory reserve which is required to be deposited with the CNB and maintained in the form of liquid assets. The obligatory reserve requirement as at 31 December 2017 represented 12% (2016:12%) of relevant HRK and foreign currency deposits and borrowings.

As at 31 December 2017 the required rate of HRK denominated part of the obligatory reserve to be deposited with the CNB amounted to 70% (2016:70%), while the remaining 30% had to be maintained in the form of liquid receivables. 75% of foreign currency obligatory reserve was required to be held in HRK, and this is added to the HRK portion of the obligatory reserve.

Banks are required to maintain 2% of their foreign currency reserve requirement, as the average daily balance of funds on their own foreign currency settlement accounts with the CNB.

Notes to the financial statements (continued)

8. Financial assets at fair value through profit or loss

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|---|----------------------------------|----------------------------------|---------------------------------|---------------------------------|
| Trading instruments | | | | |
| Debt securities: | | | | |
| - Domestic government bonds, listed | 243 | 714 | 243 | 714 |
| - Foreign government bonds, listed | - | 779 | - | 779 |
| - Treasury bills issued by the Ministry of Finance | 233 | 74 | 233 | 74 |
| - Bonds issued by banks, listed | - | 315 | - | 315 |
| - company securities, listed | 14 | - | 14 | - |
| | 490 | 1,882 | 490 | 1,882 |
| Equity instruments, listed | 1 | 5 | 1 | 5 |
| Positive fair value of OTC derivative instruments | 29 | 108 | 34 | 116 |
| Positive fair value of OTC spot transactions | 4 | 1 | 4 | 1 |
| | 33 | 109 | 38 | 117 |
| Accrued interest | 2 | 21 | 3 | 21 |
| Total trading assets | 526 | 2,017 | 532 | 2,025 |
| Financial assets designated at fair value through profit or loss | | | | |
| Debt securities: | | | | |
| - Domestic government bonds, listed | 272 | 266 | - | - |
| - Bonds issued by banks, listed | 4 | 22 | 4 | 22 |
| - Securities issued by companies, listed | 59 | 127 | 36 | 103 |
| - Treasury bills issued by the Ministry of Finance | 68 | 66 | - | - |
| | 403 | 481 | 40 | 125 |
| Equity investments | 2 | 2 | - | - |
| Investments in investment funds managed by related and third parties | 14 | 9 | - | - |
| Accrued interest | 6 | 6 | 1 | 1 |
| Total financial assets designated at fair value through profit or loss | 425 | 498 | 41 | 126 |
| TOTAL | 951 | 2,515 | 573 | 2,151 |

The amount of HRK 68 million (2016: HRK 66 million) treasury bills issued by the Ministry of Finance represent the guarantee deposit in accordance with the Law on Mandatory and Voluntary Pension Funds.

Notes to the financial statements (continued)

9. Placements with and loans to other banks

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|--|----------------------------------|----------------------------------|---------------------------------|---------------------------------|
| Loans | 41 | 235 | 78 | 286 |
| Deposits | 862 | 1,111 | 836 | 1,111 |
| Deposits with the Croatian National Bank | - | 8 | - | 8 |
| | 903 | 1,354 | 914 | 1,405 |
| Impairment allowance | (9) | (22) | (9) | (21) |
| | 894 | 1,332 | 905 | 1,384 |

Deposits with the Croatian National Bank are related to guarantee deposits linked to repurchase agreements (Note 42).

a) Movement in impairment allowance for placements and loans to other banks

| Group | Identified losses HRK millions | Unidentified losses HRK millions | 2017 Total HRK millions | Identified losses HRK millions | Unidentified losses HRK millions | 2016 Total HRK millions |
|---|---|---|----------------------------------|---|---|----------------------------------|
| At 1 January | 5 | 17 | 22 | 5 | 13 | 18 |
| Net charge/(release) recognised in profit or loss (Note 33) | - | (8) | (8) | - | 4 | 4 |
| Write-off | (5) | - | (5) | - | - | - |
| At 31 December | - | 9 | 9 | 5 | 17 | 22 |

| Bank | Identified losses HRK millions | Unidentified losses HRK millions | 2017 Total HRK millions | Identified losses HRK millions | Unidentified losses HRK millions | 2016 Total HRK millions |
|---|---|---|----------------------------------|---|---|----------------------------------|
| At 1 January | 5 | 16 | 21 | 5 | 12 | 17 |
| Net charge/(release) recognised in profit or loss (Note 33) | - | (7) | (7) | - | 4 | 4 |
| Write offs | (5) | - | (5) | - | - | - |
| At 31 December | - | 9 | 9 | 5 | 16 | 21 |

Notes to the financial statements (continued)

10. Financial assets available for sale

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|--|--|--|---|---|
| Debt securities: | | | | |
| - Domestic government bonds, listed | 1,917 | 1,491 | 1,621 | 1,198 |
| - Bonds issued by banks, listed | 1,135 | 1,040 | 1,135 | 1,040 |
| - Foreign government bonds, listed | 2,198 | 2,150 | 2,198 | 2,150 |
| Treasury bills issued by the Ministry of Finance | 608 | 463 | 588 | 463 |
| Equity securities, not listed | 25 | 21 | 25 | 21 |
| Equity securities, listed | 6 | 8 | 6 | 8 |
| Accrued interest | 48 | 44 | 44 | 41 |
| | 5,937 | 5,217 | 5,617 | 4,921 |

Government bonds and treasury bills issued by foreign government consist of financial instruments issued by the Republic of Germany, the Republic of Austria, the Republic of France, the Republic of Poland, the Kingdom of the Netherlands, the United States of America, the Republic of Slovenia and the Republic of Ireland.

Notes to the financial statements (continued)

11. Loans to customers

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|--|--|--|---|---|
| Loans to companies and similar entities | | | | |
| - denominated in domestic currency | 2,560 | 3,506 | 2,103 | 3,333 |
| - denominated in or linked to foreign currency | 5,709 | 6,238 | 5,761 | 5,336 |
| Loans to individuals | | | | |
| - denominated in domestic currency | 6,173 | 5,773 | 6,080 | 5,673 |
| - denominated in or linked to foreign currency | 4,536 | 5,010 | 3,940 | 4,435 |
| Finance lease receivables, denominated in or linked to foreign currency | 749 | 633 | - | - |
| - accrued interest | 94 | 137 | 83 | 119 |
| - deferred income | (55) | (75) | (53) | (72) |
| | 19,766 | 21,222 | 17,914 | 18,824 |
| Impairment allowance | (2,021) | (2,718) | (1,461) | (2,611) |
| | 17,745 | 18,504 | 16,453 | 16,213 |

Notes to the financial statements (continued)

11. Loans to customers (continued)

a) Movement in impairment allowance for loans to customers (including finance lease receivables):

| Group | Identified losses HRK millions | Unidentified losses HRK millions | 2017 Total HRK millions | Identified losses HRK millions | Unidentified losses HRK millions | 2016 Total HRK millions |
|---|--------------------------------------|--|----------------------------------|--------------------------------------|--|----------------------------------|
| At 1 January | 2,500 | 218 | 2,718 | 2,578 | 245 | 2,823 |
| Increase in/(reversal of) impairment losses | 589 | (14) | 575 | 156 | (27) | 129 |
| Amounts recovered during the year | (206) | - | (206) | (43) | - | (43) |
| Net charge/(release) recognised in profit or loss (Note 33) | 383 | (14) | 369 | 113 | (27) | 86 |
| Net foreign exchange loss | (5) | - | (5) | (6) | - | (6) |
| Write offs and sale | (1,061) | - | (1,061) | (185) | - | (185) |
| At 31 December | 1,817 | 204 | 2,021 | 2,500 | 218 | 2,718 |

Notes to the financial statements (continued)

11. Loans to customers (continued)

b) Movement in impairment allowance for loans to customers (including finance lease receivables):

| Bank | Identified losses HRK millions | Unidentified losses HRK millions | 2017 Total HRK millions | Identified losses HRK millions | Unidentified losses HRK millions | 2016 Total HRK millions |
|---|--------------------------------------|--|----------------------------------|--------------------------------------|--|----------------------------------|
| At 1 January | 2,412 | 199 | 2,611 | 2,491 | 223 | 2,714 |
| Increase in/(reversal of) impairment losses | 69 | (4) | 65 | 150 | (24) | 126 |
| Collection of non-performing loans | (204) | - | (204) | (39) | - | (39) |
| Net charge/(release) recognised in profit or loss (Note 33) | (135) | (4) | (139) | 111 | (24) | 87 |
| Net foreign exchange loss | (5) | - | (5) | (6) | - | (6) |
| Write offs and sale | (1,006) | - | (1,006) | (184) | - | (184) |
| At 31 December | 1,266 | 195 | 1,461 | 2,412 | 199 | 2,611 |

In the year the 2017 Bank sold a part of the non-performing loans portfolio, of HRK 818.2 million gross value (of which loans to companies and similar entities in the amount of HRK 660.3 mn and loans to individuals HRK 157.9 mn), or of HRK 94.0 million net (of which loans to companies and similar entities in the amount of HRK 93.6 mn and loans to individuals HRK 0.4 mn). Realised sell price indicated that the Bank had sufficient provisions for these loans.

c) Finance lease receivables

The Group acts as a lessor under finance leases, mainly of plant and equipment. The leases typically run for a period of one to seven years, with transfer of ownership of the leased asset at the end of the lease term. Interest is charged over the period of the lease based on market related interest rates. The receivables are secured by the underlying assets. Loans and advances to customers include the following finance lease receivables:

| | Group 2017 HRK millions | Group 2016 HRK millions |
|---|----------------------------------|----------------------------------|
| Gross investment in finance leases | 806 | 680 |
| Deferred fee income | (2) | (2) |
| Unearned finance income | (55) | (45) |
| Net investment in finance leases | 749 | 633 |
| Impairment losses | (21) | (71) |
| Net investment in finance leases | 728 | 562 |

Notes to the financial statements (continued)

11. Loans to customers (continued)

c) *Finance lease receivables (continued)*

This disclosure is illustrative since there are no non-cancellable leases.

| | Group 2017 HRK millions | Group 2016 HRK millions |
|---|-------------------------------|-------------------------------|
| Gross investment in finance lease, with remaining maturities | | |
| Less than one year | 298 | 293 |
| More than one and less than five years | 494 | 376 |
| More than five years | 14 | 11 |
| | 806 | 680 |

12. Financial investments held to maturity

| | Group 2017 HRK millions | Group 2016 HRK millions |
|----------------------------|----------------------------------|----------------------------------|
| Debt securities | | |
| - Government bonds, listed | 275 | 289 |
| Accrued interest | 6 | 6 |
| | 295 | 285 |
| Impairment allowance | (2) | (2) |
| | 279 | 293 |

Notes to the financial statements (continued)

12. Financial investments held to maturity (continued)

a) Movement in impairment allowance for financial investments held to maturity

| Group | Identified losses HRK millions | Unidentified losses HRK millions | 2017 Total HRK millions | Identified losses HRK millions | Unidentifie d losses HRK millions | 2016 Total HRK millions |
|-----------------------|---|---|--|---|--|--|
| At 1 January | - | 2 | 2 | - | 2 | 2 |
| Movements | - | - | - | - | - | - |
| At 31 December | - | 2 | 2 | - | 2 | 2 |

Notes to the financial statements (continued)

13. Investments in subsidiaries

The Group and the Bank had the following investments in subsidiaries, all incorporated in Croatia, as at 31 December 2017 and 31 December 2016:

| Business activity | | Ownership | | Acquisition cost | Impairment | Investments in subsidiaries | Acquisition cost | Impairment | Investments in subsidiaries |
|--|---|-----------|------|------------------|--------------|-----------------------------|------------------|--------------|-----------------------------|
| | | 2017 | 2016 | 2017 | 2017 | 2017 | 2016 | 2016 | 2016 |
| | | % | % | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions |
| Investment in subsidiaries | | | | | | | | | |
| Direct holding | | | | | | | | | |
| Raiffeisen društvo za upravljanje obveznim i dobrovoljnim mirovinskim fondovima d.d. | Pension fund management | 100 | 100 | 144 | - | 144 | 144 | - | 144 |
| Raiffeisen stambena štedionica d.d. | Savings bank | 100 | 100 | 56 | - | 56 | 56 | - | 56 |
| Raiffeisen Consulting d.o.o. | Financial and consulting services | 100 | 100 | 105 | - | 105 | 105 | - | 105 |
| Raiffeisen Leasing d.o.o. | Leasing | 100 | 100 | 57 | - | 57 | 57 | - | 57 |
| Raiffeisen mirovinsko osiguravajuće društvo d.d. | Pension insurance | 100 | 100 | 23 | - | 23 | 23 | - | 23 |
| Raiffeisen Invest d.o.o. | Investment fund management | 100 | 100 | 8 | - | 8 | 8 | - | 8 |
| Raiffeisen Factoring d.o.o. | Factoring | 100 | 100 | 270 | (268) | 2 | 15 | - | 15 |
| Indirect holding | | | | | | | | | |
| Raiffeisen Bonus d.o.o. | Insurance and re-insurance intermediary | 100 | 100 | - | - | - | - | - | - |
| Total | | n/p | n/p | 663 | (268) | 395 | 408 | - | 408 |

During the year 2017 the Bank increased capital of the company Raiffeisen Factoring d.o.o. in the amount of HRK 255 million so that it would meet the regulatory requirements for minimal capital and reserves of factoring companies.

On account of the exposure to the Agrokor group companies and their economically connected suppliers, the company Raiffeisen Factoring d.o.o. realised a considerable loss, and there was a major fall in the factoring business volume, so the Bank made value adjustments for the investment in the amount of HRK 268 million.

Notes to the financial statements (continued)

14. Property, plant, equipment and property investments

| Group | Land and buildings | Equipment | Office furniture | Assets under operating lease | Property investments | Assets under construction | Total |
|--|-----------------------|-----------------|---------------------|---------------------------------------|-------------------------|------------------------------|-----------------|
| 2017 | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions |
| Gross carrying amount | | | | | | | |
| At 1 January 2017 | 886 | 425 | 77 | 946 | 113 | 20 | 2,467 |
| Additions | - | - | - | - | - | 118 | 118 |
| Disposals | - | (32) | (3) | (297) | - | - | (332) |
| Transfers into other assets | - | (3) | - | (12) | (14) | - | (29) |
| Transfers into use | 24 | 34 | 1 | 48 | 19 | (126) | - |
| At 31 December 2017 | 910 | 424 | 75 | 685 | 118 | 12 | 2,224 |
| Accumulated depreciation and impairment | | | | | | | |
| At 1 January 2017 | 249 | 344 | 74 | 301 | 3 | - | 971 |
| Charge for the year (Note 32) | 15 | 26 | 1 | 60 | 3 | - | 105 |
| Disposals and transfers | - | (35) | (3) | (123) | - | - | (161) |
| At 31 December 2017 | 264 | 335 | 72 | 238 | 6 | - | 915 |
| Carrying amount | | | | | | | |
| At 1 January 2017 | 637 | 81 | 3 | 645 | 110 | 20 | 1,496 |
| At 31 December 2017 | 646 | 89 | 3 | 447 | 112 | 12 | 1,309 |

Of which:

| | 2017 HRK millions | 2016 HRK millions |
|-------------------------------|----------------------|----------------------|
| Property, plant and equipment | 1,197 | 1,386 |
| Property investments | 112 | 110 |
| Total | 1,309 | 1,496 |

There were no capitalized borrowing costs related to the acquisition of property, plant and equipment during current and previous year.

A building with the carrying amount of approximately HRK 214 million (2016: HRK 218 million) has been pledged to secure borrowings of the Group (see Note 22).

Carrying value of land stated under the land and buildings, not subject to amortization amounted to HRK 53 million (2016: HRK 55 million).

Notes to the financial statements (continued)

14. Property, plant, equipment and property investments (continued)

| Group | Land and buildings | Equipment | Office furniture | Assets under operating lease | Property investments | Assets under constructi on | Total |
|--|-----------------------|-----------------|---------------------|---------------------------------------|-------------------------|-------------------------------------|-----------------|
| 2016 | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions |
| Gross carrying amount | | | | | | | |
| At 1 January 2016 | 883 | 441 | 79 | 1,026 | 32 | 5 | 2,466 |
| Additions | - | - | - | - | - | 361 | 361 |
| Disposals | (6) | (55) | (3) | (291) | - | - | (355) |
| Transfers into other assets | (1) | - | - | - | (4) | - | (5) |
| Transfers into use | 10 | 39 | 1 | 211 | 85 | (346) | - |
| At 31 December 2016 | 886 | 425 | 77 | 946 | 113 | 20 | 2,467 |
| Accumulated depreciation and impairment | | | | | | | |
| At 1 January 2016 | 241 | 374 | 76 | 293 | - | - | 984 |
| Charge for the year (Note 32) | 14 | 23 | 1 | 111 | 3 | - | 152 |
| Disposals and transfers | (6) | (53) | (3) | (103) | - | - | (165) |
| At 31 December 2016 | 249 | 344 | 74 | 301 | 3 | - | 971 |
| Carrying amount | | | | | | | |
| At 1 January 2016 | 642 | 67 | 3 | 733 | 32 | 5 | 1,482 |
| At 31 December 2016 | 637 | 81 | 3 | 645 | 110 | 20 | 1,496 |

Notes to the financial statements (continued)**14. Property, plant, equipment and property investments (continued)*****Future minimum lease payments under operating lease***

The Group acts as a lessor under operating leases, mainly of plant and equipment. The leases typically run for a period of two to twenty years. Future minimum lease payments for operating lease (disclosure is only illustrative as there are no non-cancellable lease contracts) at 31 December 2017 were as follows:

| | Group 2017 HRK millions | Group 2016 HRK millions |
|--|--|--|
| Up to one year | 79 | 127 |
| More than one and less than five years | 136 | 236 |
| Over five years | 2 | 5 |
| | 217 | 368 |

Notes to the financial statements (continued)

14. Property, plant, equipment and property investments (continued)

Bank

| 2017 | Land and buildings HRK millions | Equipment HRK millions | Office furniture HRK millions | Assets under construction HRK millions | Total HRK millions |
|----------------------------------|--|------------------------------|--|--|--------------------------|
| Gross carrying amount | | | | | |
| At 1 January 2017 | 508 | 405 | 74 | 19 | 1,006 |
| Additions | - | - | - | 49 | 49 |
| Disposals | - | (32) | - | - | (32) |
| Transfer to intangible assets | - | (3) | - | - | (3) |
| Transfers into use | 24 | 32 | 1 | (57) | - |
| At 31 December 2017 | 532 | 402 | 75 | 11 | 1,020 |
| Accumulated depreciation | | | | | |
| At 1 January 2017 | 123 | 334 | 71 | - | 528 |
| Charge for the year (Note 32) | 9 | 24 | 1 | - | 34 |
| Transfer to intangible assets | - | (2) | - | - | (2) |
| Disposals | - | (32) | - | - | (32) |
| At 31 December 2017 | 132 | 324 | 72 | - | 528 |
| Carrying amount | | | | | |
| At 1 January 2017 | 385 | 71 | 3 | 19 | 478 |
| At 31 December 2017 | 400 | 78 | 3 | 11 | 492 |

Assets under construction relates to equipment at cost of HRK 10 million (2016: HRK 17 million) and office furniture of HRK 1 million (2016: -). Additionally, in 2016 HRK 2 million (2017: -) relates to buildings.

There were no capitalized borrowing costs related to the acquisition of property, plant and equipment during the year (2016: -).

Book value of land stated under the land and buildings, not subject to amortization, amounted to HRK 28 million (2016: HRK 28 million).

Notes to the financial statements (continued)

14. Property, plant, equipment and property investments (continued)

Bank

| 2016 | Land and buildings HRK millions | Equipment HRK millions | Office furniture HRK millions | Assets under construction HRK millions | Total HRK millions |
|---------------------------------|--|------------------------------|--|--|--------------------------|
| Gross carrying amount | | | | | |
| At 1 January 2016 | 505 | 415 | 73 | 5 | 998 |
| Additions | - | - | - | 55 | 55 |
| Disposals | - | (47) | - | - | (47) |
| Transfers into use | 3 | 37 | 1 | (41) | - |
| At 31 December 2016 | 508 | 405 | 74 | 19 | 1,006 |
| Accumulated depreciation | | | | | |
| At 1 January 2016 | 114 | 356 | 70 | - | 540 |
| Charge for the year (Note 32) | 9 | 21 | 1 | - | 31 |
| Disposals | - | (43) | - | - | (43) |
| At 31 December 2016 | 123 | 334 | 71 | - | 528 |
| Carrying amount | | | | | |
| At 1 January 2016 | 391 | 59 | 3 | 5 | 458 |
| At 31 December 2016 | 385 | 71 | 3 | 19 | 478 |

Notes to the financial statements (continued)

15. Intangible assets

| Group | Goodwill | Leasehold improvement | Software | Assets under construction | Total |
|---------------------------------|--------------|-----------------------|--------------|---------------------------|--------------|
| 2017 | | | | | |
| | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions |
| Gross carrying amount | | | | | |
| At 1 January 2017 | 27 | 203 | 619 | 12 | 861 |
| Additions | - | - | - | 45 | 45 |
| Disposals | - | - | (17) | - | (17) |
| Transfer from tangible assets | - | - | 3 | - | 3 |
| Transfer into use | - | 8 | 43 | (51) | - |
| At 31 December 2017 | 27 | 211 | 648 | 6 | 892 |
| Accumulated depreciation | | | | | |
| At 1 January 2017 | - | 146 | 475 | - | 621 |
| Charge for the year (Note 32) | - | 9 | 33 | - | 42 |
| Transfer from tangible assets | - | - | 2 | - | 2 |
| Disposals | - | - | (12) | - | (12) |
| At 31 December 2017 | - | 155 | 498 | - | 653 |
| Carrying amount | | | | | |
| At 1 January 2017 | 27 | 57 | 144 | 12 | 240 |
| At 31 December 2017 | 27 | 56 | 150 | 6 | 239 |

Assets under construction comprise software in the process of installation in the amount of HRK 6 million (2016: HRK 11 million) and leasehold improvement in 2016 of HRK 1 million (2017: -).

Notes to the financial statements (continued)

15. Intangible assets (continued)

| Group | | | | | |
|---------------------------------|--------------|-----------------------|--------------|---------------------------|--------------|
| 2016 | Goodwill | Leasehold improvement | Software | Assets under construction | Total |
| | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions |
| Gross carrying amount | | | | | |
| At 1 January 2016 | - | 196 | 580 | 9 | 785 |
| Additions | 27 | - | - | 58 | 85 |
| Disposals | - | (2) | (7) | - | (9) |
| Transfers into use | - | 9 | 46 | (55) | - |
| At 31 December 2016 | 27 | 203 | 619 | 12 | 861 |
| Accumulated depreciation | | | | | |
| At 1 January 2016 | - | 138 | 452 | - | 590 |
| Charge for the year (Note 32) | - | 9 | 30 | - | 39 |
| Smanjenje | - | (1) | (7) | - | (8) |
| At 31 December 2016 | - | 146 | 475 | - | 621 |
| Carrying amount | | | | | |
| 1 January 2016 | - | 58 | 128 | 9 | 195 |
| At 31 December 2016 | 27 | 57 | 144 | 12 | 240 |

Notes to the financial statements (continued)

15. Intangible assets (continued)

| Bank | Leasehold improvement | Software | Assets under construction | Total |
|---------------------------------|-----------------------|--------------|---------------------------|--------------|
| 2017 | HRK millions | HRK millions | HRK millions | HRK millions |
| Gross carrying amount | | | | |
| At 1 January 2017 | 193 | 572 | 10 | 775 |
| Additions | - | - | 41 | 41 |
| Transfer from tangible assets | - | 3 | - | 3 |
| Disposals | - | (17) | - | (17) |
| Transfer into use | 7 | 39 | (46) | - |
| At 31 December 2017 | 200 | 597 | 5 | 802 |
| Accumulated amortisation | | | | |
| At 1 January 2017 | 137 | 432 | - | 569 |
| Charge for the year (Note32) | 9 | 31 | - | 40 |
| Transfer from tangible assets | - | 2 | - | 2 |
| Disposals | - | (13) | - | (13) |
| At 31 December 2017 | 146 | 452 | - | 598 |
| Carrying amount | | | | |
| At 1 January 2017 | 56 | 140 | 10 | 206 |
| At 31 December 2017 | 54 | 145 | 5 | 204 |

Assets under construction comprise software in the process of installation in the amount of HRK 5 million (2016: HRK 10 million).

Notes to the financial statements (continued)

15. Intangible assets (continued)

| Bank | Leasehold improvement | Software | Assets under construction | Total |
|---------------------------------|--------------------------|-----------------|---------------------------------|--------------|
| 2016 | HRK millions | HRK millions | HRK millions | HRK millions |
| Gross carrying amount | | | | |
| At 1 January 2016 | 185 | 533 | 8 | 726 |
| Additions | - | - | 55 | 55 |
| Disposals | - | (6) | - | (6) |
| Transfer into use | 8 | 45 | (53) | - |
| At 31 December 2016 | 193 | 572 | 10 | 775 |
| Accumulated amortisation | | | | |
| At 1 January 2016 | 128 | 410 | - | 538 |
| Charge for the year (Note 32) | 9 | 28 | - | 37 |
| Disposals | - | (6) | - | (6) |
| At 31 December 2016 | 137 | 432 | - | 569 |
| Carrying amount | | | | |
| At 1 January 2016 | 57 | 123 | 8 | 188 |
| At 31 December 2016 | 56 | 140 | 10 | 206 |

Notes to the financial statements (continued)

16. Deferred tax asset

Recognised deferred tax asset and liabilities

Movements in temporary differences and underlying positions for deferred tax assets and deferred tax liabilities are as follows:

| Group | Assets | | Liabilities | | Net income/(charge) in profit or loss | | Net profit/(loss) in other comprehensive profit | |
|---|-----------------|---------------------|-----------------|---------------------|--|-----------------|---|-----------------|
| | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 |
| | HRK millions | HRK million s | HRK millions | HRK million s | HRK millions | HRK millions | HRK millions | HRK millions |
| Property, plant and equipment | - | - | (2) | (2) | - | 1 | - | - |
| Deferred fee and commission expense | - | - | (2) | (3) | 1 | (1) | - | - |
| Tax lossees carried forward | - | 33 | - | - | (33) | (102) | - | - |
| Deferred fee and commission income | 11 | 15 | - | - | (4) | (5) | - | - |
| Recognised deferred tax assets for the Group | 48 | - | - | - | 48 | - | - | - |
| Unrealized losses on financial instruments at fair value through profit or loss | 17 | 27 | - | - | (10) | (22) | - | - |
| Other provisions | 21 | 26 | - | - | (5) | 1 | - | - |
| Deferred tax assets /(liabilities) | 97 | 101 | (4) | (5) | (3) | (128) | - | - |
| Unrealized loss from financial assets available for sale | (7) | (10) | - | - | - | - | 3 | 7 |
| Off-set | (4) | (5) | 4 | 5 | - | - | - | - |
| Net deferred tax assets | 86 | 86 | - | - | (3) | (128) | 3 | 7 |

Notes to the financial statements (continued)

16. Deferred tax asset (continued)

Recognised deferred tax asset and liabilities (continued)

Movements in temporary differences and underlying positions for deferred tax assets and deferred tax liabilities are as follows:

| Bank | Assets | | Liabilities | | Net income/(charge) in profit or loss | | Net profit/(loss) in other comprehensive profit | |
|---|-----------|-----------|-------------|------------|---------------------------------------|--------------|---|----------|
| | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 |
| | HRK | HRK | HRK | HRK | HRK | HRK | HRK | HRK |
| | millions | millions | millions | millions | millions | millions | millions | millions |
| Deferred fee and commission expense | - | - | (1) | (1) | - | - | - | - |
| Deferred fee and commission income | 10 | 13 | - | - | (3) | (6) | - | - |
| Unrealized loss on financial instruments at fair value through profit or loss | 16 | 26 | - | - | (10) | (20) | - | - |
| Value adjustment of investments in subsidiary | 48 | - | - | - | 48 | - | - | - |
| Tax losses carried forward | - | 33 | - | - | (33) | (101) | - | - |
| Other provisions | 17 | 19 | - | - | (2) | 2 | - | - |
| Deferred tax assets /(liabilities) | 91 | 91 | (1) | (1) | - | (125) | - | - |
| Unrealized profit/(loss) from financial assets available for sale | (6) | (7) | - | - | - | - | 1 | 7 |
| Off-set | (1) | (1) | 1 | 1 | - | - | - | - |
| Net deferred tax assets | 84 | 83 | - | - | - | (125) | 1 | 7 |

Deferred tax assets for value adjustment of investments in subsidiary refers to the investment in the affiliated company Raiffeisen Factoring d.o.o. for which the Bank conducted value adjustment and formed deferred tax assets for the respective amount of HRK 48 million.

Notes to the financial statements (continued)

17. Other assets

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|---|--|--|---|---|
| Accrued fee and commission receivables | 31 | 33 | 16 | 19 |
| Deferred fee and commission expenses | 1 | 6 | 1 | 1 |
| Inventory and foreclosed assets | 96 | 101 | 72 | 58 |
| Prepayments | 54 | 62 | 56 | 62 |
| Receivables from credit and debit card business | 47 | 49 | 47 | 49 |
| Receivables from operating lease | 9 | 11 | - | - |
| Government housing savings subsidies receivables | 3 | 5 | - | - |
| Receivables for unsettled securities sold | - | 1 | - | 1 |
| Receivables from repurchase of domestic currency cash | 16 | 4 | 16 | 4 |
| Other | 79 | 68 | 38 | 34 |
| | 336 | 340 | 246 | 228 |
| Impairment allowance | (45) | (55) | (36) | (49) |
| | 291 | 285 | 210 | 179 |

Notes to the financial statements (continued)

17. Other assets (continued)

Movement in impairment allowance

| Group | Identified loss HRK millions | Unidentified loss HRK millions | 2017 Total HRK millions | Identified loss HRK millions | Unidentified loss HRK millions | 2016 Total HRK millions |
|--|---------------------------------------|---|----------------------------------|---------------------------------------|---|----------------------------------|
| At 1 January | 55 | - | 55 | 71 | 1 | 72 |
| Provision charged during the year | 27 | - | 27 | 28 | - | 28 |
| Provision released during the year | (3) | - | (3) | (17) | (1) | (18) |
| Net charge / (release) in profit or loss (Note 33) | 24 | - | 24 | 11 | (1) | 10 |
| Write offs | (34) | - | (34) | (27) | - | (27) |
| At 31 December | 45 | - | 45 | 55 | - | 55 |

| Bank | Identified loss HRK millions | Unidentified loss HRK millions | 2017 Total HRK millions | Identified loss HRK millions | Unidentified loss HRK millions | 2016 Total HRK millions |
|---|---------------------------------------|---|----------------------------------|---------------------------------------|---|----------------------------------|
| At 1 January | 49 | - | 49 | 65 | 1 | 66 |
| Charges | 21 | - | 21 | 28 | - | 28 |
| (Release) | (3) | - | (3) | (17) | (1) | (18) |
| Net charge/(release) recognised in profit or loss (Note 33) | 18 | - | 18 | 11 | (1) | 10 |
| Write offs | (31) | - | (31) | (27) | - | (27) |
| At 31 December | 36 | - | 36 | 49 | - | 49 |

Notes to the financial statement (continued)

18. Financial liabilities at fair value through profit or loss

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|---|----------------------------------|----------------------------------|---------------------------------|---------------------------------|
| Trading instruments | | | | |
| Negative fair value of OTC derivative instruments | 42 | 89 | 44 | 89 |
| Negative fair value of OTC spot transactions | 11 | 1 | 11 | 1 |
| Fair value hedge | 4 | 6 | 4 | 6 |
| Accrued interest | 2 | 1 | 2 | 1 |
| | 59 | 97 | 61 | 97 |

Notes to the financial statements (continued)

19. Deposits from banks

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|---|--|--|---|---|
| Current accounts and demand deposits | | | | |
| - from parent bank | 57 | 27 | 57 | 27 |
| - from RBI Group banks other than parent bank | 8 | 7 | 45 | 16 |
| - from other banks | 242 | 212 | 242 | 212 |
| Time deposits | | | | |
| - from parent bank | 263 | - | 263 | - |
| - from other RBI Group banks | - | - | - | 70 |
| - from other banks | 486 | 195 | 486 | 195 |
| | 1,056 | 441 | 1,093 | 520 |

20. Deposits from companies and other similar entities

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|--------------------------------------|--|--|---|---|
| Current accounts and demand deposits | 8,973 | 8,448 | 9,247 | 8,646 |
| Time deposits | 571 | 1,435 | 564 | 1,435 |
| Accrued interest | 5 | 8 | 6 | 9 |
| | 9,549 | 9,891 | 9,817 | 10,090 |

Notes to the financial statements (continued)

21. Deposits from individuals

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|--------------------------------------|--|--|---------------------------------------|---------------------------------------|
| Current accounts and demand deposits | 5,989 | 4,589 | 5,989 | 4,589 |
| Time deposits | 8,209 | 9,616 | 7,181 | 8,558 |
| Accrued interest | 33 | 48 | 33 | 48 |
| | 14,231 | 14,253 | 13,203 | 13,195 |

22. Borrowings

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|---|--|--|---|---|
| From ultimate parent bank | 811 | 662 | 27 | 39 |
| From RBI Group bank other than Parent bank | - | 604 | - | - |
| From other banks | 889 | 1,396 | 456 | 469 |
| From HBOR | 866 | 976 | 751 | 901 |
| From companies and other financial institutions | - | 347 | - | 347 |
| Accrued interest | 7 | 9 | 5 | 6 |
| Less deferred charge | (1) | (2) | (2) | (3) |
| | 2,572 | 3,992 | 1,237 | 1,759 |

In the year 2017 presentation of borrowings was changed and borrowings from the Croatian Reconstruction and Development Bank (HBOR) were declared as a separate category (the change was applied to the year 2016, as well).

Movements of outstanding borrowings

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|------------------------------|--|--|---------------------------------------|---------------------------------------|
| At 1 January | 3,992 | 4,251 | 1,759 | 1,802 |
| New borrowings | 3,457 | 9,578 | 2,682 | 8,270 |
| Repayment of borrowings | (4,846) | (9,803) | (3,198) | (8,302) |
| Foreign exchange differences | (31) | (34) | (6) | (11) |
| At 31 December | 2,572 | 3,992 | 1,237 | 1,759 |

Borrowings from companies and other financial institutions in 2016 relate to repurchase agreements.

Notes to the financial statements (continued)

23. Provisions for liabilities and charges

| Group | Total | Off balance sheet exposure identified | Off balance sheet exposure unidentified | Provision for pension insurance | Provisions for unused holiday | Provision for court cases | Provisions for CHF conversion |
|--|--------------|---------------------------------------|---|---------------------------------|-------------------------------|---------------------------|-------------------------------|
| | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions |
| At 1 January 2017 | 187 | 23 | 80 | 3 | 9 | 66 | 6 |
| Provision released during the year | (16) | (7) | (3) | - | - | - | (6) |
| Provision created during the year | 2 | - | - | - | - | 2 | - |
| <i>(Release)/charge recognised in profit or loss</i> | <i>(14)</i> | <i>(7)</i> | <i>(3)</i> | <i>-</i> | <i>-</i> | <i>2</i> | <i>(6)</i> |
| At 31 December 2017 | 173 | 16 | 77 | 3 | 9 | 68 | - |

| Group | Total | Off balance sheet exposure identified | Off balance sheet exposure unidentified | Provision for pension insurance | Provisions for unused holiday | Provision for court cases | Provisions for CHF conversion |
|--|--------------|---------------------------------------|---|---------------------------------|-------------------------------|---------------------------|-------------------------------|
| | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions |
| At 1 January 2016 | 804 | 43 | 75 | 2 | 8 | 59 | 617 |
| Provision released during the year | (631) | (20) | - | - | - | - | (611) |
| Provision created during the year | 14 | - | 5 | 1 | 1 | 7 | - |
| <i>(Release)/charge recognised in profit or loss</i> | <i>(617)</i> | <i>(20)</i> | <i>5</i> | <i>1</i> | <i>1</i> | <i>7</i> | <i>(611)</i> |
| At 31 December 2016 | 187 | 23 | 80 | 3 | 9 | 66 | 6 |

Notes to the financial statements (continued)

23. Provisions for liabilities and charges (continued)

In September 2015 the amendments to the regulations (Consumer Lending Act, and Credit Institutions Act) came into force, whereunder the borrowers of loans pegged to the CHF are allowed to convert the loans from the CHF to the EUR. The Bank has the obligation to perform the prescribed conversion, and generates conversion cost in respect of reduced principal and interest paid on converted loans. Therefore the Bank formed HRK 617 million of provisions in 2015 for the conversion of 5,176 loans for which the obligation to offer conversion applied. In 2016 the conversion procedure was undertaken on 4857 loans, and the Bank reversed HRK 611 million of provisions in respect of converted loans. The remaining HRK 6 million of provisions related to 66 loans for which the conversion was neither performed nor rejected by customers in 2016. In 2017 the Bank converted 51 loans. It is expected in the forthcoming period that customers may apply for conversion of the remaining 15 loans for which they neither requested nor rejected the conversion by the end of 2017. In that case the Bank will convert those loans in accordance with applicable regulations and generate conversion costs. As the probability of additional conversion costs is insignificant, the Bank reversed the remaining HRK 6 million of provisions relating to conversion obligation in 2017.

Notes to the financial statements (continued)

23. Provisions for liabilities and charges (continued)

| Bank | Total | Off balance sheet exposure identified | Off balance sheet exposure unidentified | Provision for pension insurance | Provisions for unused holiday | Provision for court cases | Provisions for CHF conversion |
|---|--------------|---------------------------------------|---|---------------------------------|-------------------------------|---------------------------|-------------------------------|
| | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions |
| At 1 January 2017 | 176 | 23 | 80 | 3 | 7 | 57 | 6 |
| Provision released during the year | (16) | (7) | (3) | - | - | - | (6) |
| Provision created during the year | 2 | - | - | - | - | 2 | - |
| (Release)/charge recognized in profit or loss | (14) | (7) | (3) | - | - | 2 | (6) |
| At 31 December 2017 | 162 | 16 | 77 | 3 | 7 | 59 | - |

| Bank | Total | Off balance sheet exposure identified | Off balance sheet exposure unidentified | Provision for pension insurance | Provisions for unused holiday | Provision for court cases | Provisions for CHF conversion |
|---|--------------|---------------------------------------|---|---------------------------------|-------------------------------|---------------------------|-------------------------------|
| | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions | HRK millions |
| At 1 January 2016 | 793 | 43 | 75 | 2 | 6 | 50 | 617 |
| Provision released during the year | (631) | (20) | - | - | - | - | (611) |
| Provision created during the year | 14 | - | 5 | 1 | 1 | 7 | - |
| (Release)/charge recognised in profit or loss | (617) | (20) | 5 | 1 | 1 | 7 | (611) |
| At 31 December 2016 | 176 | 23 | 80 | 3 | 7 | 57 | 6 |

Notes to the financial statements (continued)

24. Other liabilities

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|--|-------------------------------|-------------------------------|------------------------------|------------------------------|
| Technical reserves for pension insurance | 437 | 403 | - | - |
| Liabilities in respect of credit and debit card business | 120 | 101 | 120 | 101 |
| Liabilities to employees | 59 | 60 | 51 | 51 |
| Liabilities to suppliers | 85 | 73 | 79 | 67 |
| Deferred fee and commission income prepayments | 19 | 17 | 7 | 7 |
| Liabilities for prepaid loans and advances | 34 | 45 | 23 | 33 |
| Repurchase of domestic currency cash | 6 | 4 | 6 | 4 |
| Government housing savings subsidies | 3 | 5 | - | - |
| Other liabilities | 188 | 68 | 151 | 29 |
| | 951 | 776 | 437 | 292 |

Technical reserves for pension insurance provisions have been computed by the Group's licensed actuary, in accordance with the method prescribed by the Law on Pension Insurance Companies and Payment of Pensions based on Individual Capitalised Savings.

The Management believes that the current level of technical reserves is sufficient to meet all liabilities which may arise from the pension insurance contracts concluded by 31 December 2017.

25. Subordinated liabilities

The Bank has signed a subordinated loan agreement with RBI amounting to EUR 60 million as of 31 January 2014 and EUR 50 million as of 26 May 2015. The Bank used the subordinated loan to increase its Tier 2 Capital. Repayment of the loan matures on 20 February 2021 and 28 May 2022. Interest agreed consists of 3M EURIBOR increased by interest margin and 6.75% fixed.

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|------------------|-------------------------------|-------------------------------|------------------------------|------------------------------|
| Loan | 826 | 831 | 826 | 831 |
| Accrued interest | 6 | 6 | 6 | 6 |
| | 832 | 837 | 832 | 837 |

Notes to the financial statements (continued)

26. Interest income

a) Analysis by product

| | Group 2017 HRK millions | Group 2016 HRK millions | Bank 2017 HRK millions | Bank 2016 HRK millions |
|---|--|--|---|---|
| Derivative financial instruments | 3 | 5 | 6 | 8 |
| Other financial assets at fair value through profit or loss | 41 | 58 | 28 | 45 |
| Financial assets available for sale | 38 | 50 | 31 | 36 |
| Placements with banks | 2 | 3 | 4 | 5 |
| Loans and advances to customers and similar entities | 336 | 410 | 296 | 331 |
| Loans and advances to individuals | 702 | 763 | 661 | 723 |
| Financial instruments held to maturity | 17 | 16 | - | - |
| | 1,139 | 1,305 | 1,026 | 1,148 |

b) Analysis by source

| | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|--|---|---|--|--|
| Companies | 323 | 396 | 280 | 241 |
| Individuals | 702 | 763 | 661 | 723 |
| State and the public sector | 108 | 139 | 77 | 169 |
| Banks and other financial institutions | 6 | 7 | 8 | 15 |
| | 1,139 | 1,305 | 1,026 | 1,148 |

Interest income on placements advanced to HBOR in 2017 is stated within the state and public sector (previously stated in banks and other financial institutions) and the year 2016 has been adjusted accordingly.

Notes to the financial statements (continued)

27. Interest expense

a) Analysis by product

| | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|---|---------------------------------------|---------------------------------------|--------------------------------------|--------------------------------------|
| Derivative financial instruments | 18 | 21 | 18 | 21 |
| Derivative financial instruments in fair value hedges | 2 | 2 | 2 | 2 |
| Deposits from banks | 7 | 7 | 7 | 7 |
| Deposits from companies and other similar entities | 14 | 27 | 15 | 28 |
| Deposits from individuals | 80 | 141 | 54 | 111 |
| Borrowings | 51 | 64 | 20 | 27 |
| Subordinated liabilities | 54 | 55 | 54 | 55 |
| | 226 | 317 | 170 | 251 |

b) Interest expense - analysis by recipient

| | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|--|---------------------------------------|---------------------------------------|--------------------------------------|--------------------------------------|
| Companies | 14 | 26 | 14 | 27 |
| Individuals | 80 | 141 | 54 | 111 |
| State and public sector | 17 | 1 | 17 | 24 |
| Banks and other financial institutions | 115 | 149 | 85 | 89 |
| | 226 | 317 | 170 | 251 |

Interest expense on borrowings from HBOR is stated in the state and public sector (previously stated in banks and other financial institutions) and the year 2016 has been adjusted accordingly.

Notes to the financial statements (continued)

28. Fee and commission income

| | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|--|---|---|--|--|
| Domestic payment transactions | 103 | 102 | 104 | 102 |
| Investment management, custody and consultancy fees | 196 | 173 | 34 | 22 |
| Credit cards | 291 | 215 | 291 | 215 |
| Foreign exchange payment transactions | 63 | 69 | 63 | 69 |
| Partial recharge of credit insurance costs (Note 29) | 21 | 19 | 21 | 19 |
| Guarantees and letter of credits | 30 | 32 | 30 | 32 |
| Loans and accounts administration fee | 40 | 43 | 39 | 38 |
| Other fees and commission income | 50 | 41 | 47 | 46 |
| | 794 | 694 | 629 | 543 |

29. Fee and commission expense

| | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|---|---|---|--|--|
| Credit card related charges | 251 | 176 | 251 | 176 |
| Domestic payment transactions | 21 | 22 | 21 | 22 |
| Partially rechargeable credit insurance costs (Note 28) | 31 | 29 | 31 | 29 |
| Other fees and commission expense | 22 | 30 | 17 | 19 |
| | 325 | 257 | 320 | 246 |

Based on loan insurance contracts the Bank pays premium to insurance companies, which is partially recharged to customers.

Notes to the financial statements (continued)

30. Net trading gain (loss) and gain on financial assets available for sale and foreign exchange differences from translation of monetary assets and liabilities

| | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|--|---------------------------------|---------------------------------|--------------------------------|--------------------------------|
| Gains (less losses) from trading financial instruments | | | | |
| Debt securities | (8) | 7 | (8) | 7 |
| Equity securities | - | (1) | - | (1) |
| Derivative financial instruments | (79) | 87 | (81) | 90 |
| | (87) | 93 | (89) | 96 |
| Gains (less losses) from financial assets designated at fair value through profit or loss | | | | |
| Realised gain/(loss) on disposal of: | | | | |
| - debt securities | - | 15 | (1) | 13 |
| - treasury bills | - | 1 | - | - |
| Unrealised gain/(loss) on: | | | | |
| - debt securities | 8 | 13 | 1 | - |
| - equity securities | (2) | - | - | - |
| | 6 | 29 | - | 13 |
| Net gains from financial assets available for sale | 25 | 99 | 14 | 94 |
| Net gains arising from trading in foreign currencies | 107 | 103 | 109 | 104 |
| Gains less losses arising from revaluation of monetary assets and liabilities, which are not trading with securities | | | | |
| - foreign exchange translation gain on assets and liabilities in foreign currency | 238 | 126 | 187 | 70 |
| - foreign exchange translation loss on assets and liabilities with foreign currency clause | (97) | (135) | (48) | (107) |
| Total foreign exchange differences | 141 | (9) | 139 | (37) |
| | 192 | 315 | 173 | 270 |

Net (loss)/gain on derivative instruments include net trading losses from interest rate swaps, futures, forwards and forward rate agreements.

Notes to the financial statements (continued)

31. Other operating income

| | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|---|---------------------------------|---------------------------------|--------------------------------|--------------------------------|
| Rental income from operating leases | 95 | 156 | - | - |
| Revenue from service and construction contracts | 1 | 1 | - | - |
| Premium on pension insurance contracts | 151 | 122 | - | - |
| Dividend from subsidiaries | - | - | 72 | 72 |
| Other income | 53 | 43 | 29 | 21 |
| | 300 | 322 | 101 | 93 |

32. Operating expenses

| | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|---|------------------------------|------------------------------|-----------------------------|-----------------------------|
| Personnel expenses | 430 | 420 | 369 | 359 |
| Expenses for pension contract payments | 130 | 119 | - | - |
| Depreciation on property, plant and equipment | 105 | 152 | 34 | 31 |
| IT expenses | 83 | 92 | 77 | 85 |
| Increase in technical reserve for pension insurance | 38 | 28 | - | - |
| Office space expenses | 70 | 72 | 80 | 81 |
| Legal, advisory and consulting expenses | 66 | 57 | 58 | 51 |
| Deposit insurance expense | 40 | 43 | 37 | 39 |
| Amortisation of intangible assets | 42 | 39 | 40 | 37 |
| Communication expenses | 33 | 36 | 29 | 31 |
| Advertising, PR and promotional expenses | 34 | 30 | 29 | 25 |
| Resolution fund fee | 21 | 20 | 21 | 20 |
| REGOS, HANFA expenses | 26 | 25 | - | - |
| Loss on disposal of assets under operating lease | 3 | 4 | - | - |
| Loan conversion expenses | 8 | 655 | 8 | 655 |
| Investment in subsidiary | - | - | 268 | - |
| Other administrative expenses | 83 | 85 | 55 | 67 |
| | 1,212 | 1,877 | 1,105 | 1,481 |

Notes to the financial statements (continued)

32. Operating expenses (continued)

Personnel expenses of the Group include HRK 68 million (2016: HRK 68 million) of defined pension contributions paid or payable into obligatory pension plans. Contributions are calculated as a percentage of employees' gross salaries. The Group had 2,261 employees at 31 December 2017 (2016: 2,309 employees).

Personnel expenses of the Bank include HRK 58 million (2016: HRK 59 million) of defined pension contributions paid or payable into obligatory pension plans. Contributions are calculated as a percentage of employee's gross salaries. The Bank had 2,011 employees at 31 December 2017 (2016: 2,052 employees).

33. Impairment losses

| | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|---|---------------------------------------|---------------------------------------|--------------------------------------|--------------------------------------|
| Cash and current accounts with banks (Note 6) | 3 | 12 | 3 | 12 |
| Obligatory reserve with the Croatian National Bank (Note 7) | (2) | (5) | (2) | (5) |
| Placements with and loans to other banks (Note 9) | (8) | 4 | (7) | 4 |
| Loans and advances to customers (Note 11) | 369 | 86 | (139) | 87 |
| Other assets (Note 17) | 24 | 10 | 18 | 10 |
| | 386 | 107 | (127) | 108 |
| Hereof: | | | | |
| Identified losses | 407 | 124 | (117) | 122 |
| Unidentified losses | (21) | (17) | (10) | (14) |

Notes to the financial statements (continued)

34. Income tax expense

| | Note | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|---|------|---------------------------------|---------------------------------|--------------------------------|--------------------------------|
| Recognised in the statement of comprehensive income | | | | | |
| - Current tax expense | | (99) | (32) | (79) | - |
| - Deferred tax expense | 16 | (3) | (128) | - | (125) |
| Income tax expense | | (102) | (160) | (79) | (125) |
| Reconciliation of income tax expense at 18% | | | | | |
| (Loss)/profit before tax | | 290 | 695 | 475 | 585 |
| Income tax at 18% | | (52) | (139) | (86) | (117) |
| Adjustment of income tax from the previous year in the current year | | (3) | (3) | (3) | (3) |
| Non-deductible expenses | | (100) | (17) | (5) | (15) |
| Tax incentives and tax exempt income | | 8 | 9 | 15 | 20 |
| Newly recognized tax assets on Group level | | 45 | - | - | - |
| Changes in statutory tax rate (20% to 18%) | | - | (10) | - | (10) |
| Income tax expense | | (102) | (160) | (79) | (125) |
| Effective income tax rate | | 35.17% | 23.02% | 16.63% | 21.37% |

Deferred tax assets

In 2017 the Bank used the previous year tax loss (2016: HRK 183 million), and subsidiaries had HRK 7 million of tax losses (2016: HRK 28 million). Such tax losses may only be used by the company that incurred the loss to reduce taxable profits of the following five years. The expiry dates for unused tax losses were as follows:

| | Group Gross tax losses 2017 HRK million | Group Tax benefit 2017 HRK million | Group Gross tax losses 2016 HRK million | Group Tax benefit 2016 HRK million |
|------------------|--|---|--|---|
| 31 December 2017 | - | - | 25 | 5 |
| 31 December 2018 | 1 | - | 2 | - |
| 31 December 2019 | - | - | - | - |
| 31 December 2020 | - | - | 184 | 33 |
| 31 December 2021 | - | - | - | - |
| 31 December 2022 | 6 | - | - | - |
| | 7 | - | 211 | 38 |

Notes to the financial statements (continued)

34. Income tax expense (continued)

| | Bank Gross tax losses 2016 HRK million | Tax benefit 2016 HRK million |
|------------------|---|---|
| 31 December 2019 | - | - |
| 31 December 2020 | 183 | 33 |
| | 183 | 33 |

Until the submission of the tax balance on 30 April 2017 the Bank has to include all events occurring after reporting date when they relate to the previous year, therefore in the current year 2017 the tax loss from previous years was adjusted in the amount of HRK million 168, and used in 2017.

35. Share capital

| Group and Bank | 2017 Total of ordinary shares HRK million | 2016 Total share HRK million |
|-------------------------|--|---|
| Share capital | 3,621 | 3,621 |
| Nominal value per share | HRK 1,000 | HRK 1,000 |
| Number of shares | 3,621,432 | 3,621,432 |

The parent bank of the Group is Raiffeisen Bank International AG, a company founded in Austria.

| | 2017 Ordinary Shares % | 2016 Ordinary Shares % |
|------------------------------------|---|---|
| Raiffeisen SEE Region Holding GmbH | 100 | 100 |
| | 100 | 100 |

Notes to the financial statements (continued)

36. Other reserves

Share premium

The share premium represents the accumulated positive difference between the nominal value and amount received upon issue of share capital.

Legal reserve

The legal reserve represents accumulated transfers from retained earnings in accordance with the Croatian Companies Act, which requires a minimum of 5% of the Group's net profit to be transferred to a non-distributable statutory reserve until the reserve (including share premium) reaches 5% of the Group's registered share capital. The legal reserve may be used to cover prior period losses if the losses are not covered by current year profits or if other reserves are not available.

Fair value reserve

The fair value reserve includes unrealised gains and losses on changes in the fair value of financial assets available for sale, net of deferred tax.

37. Proposed dividends

Dividends payable are not accounted for until they have been ratified at the General Meeting of Shareholders.

At a meeting held on 4 May 2017, a dividend of HRK 106.37 per ordinary share, totaling HRK 385 million was proposed and paid in May 2017.

Payment of dividend amounting to HRK 396 million (HRK 109.24 per share) is expected to be determined by the Supervisory Board and confirmed by the General Assembly meeting by the end of April 2018.

During 2017 the subsidiaries proposed and paid HRK 72 million of dividends from retained earnings (2016: HRK 72 million).

The Bank's expected dividend payment from subsidiaries in 2018 amounts to HRK 71 million.

Notes to the financial statements (continued)

38. Non-controlling interest

| | Group 2016 HRK million |
|---|------------------------------|
| At 1 January | 68 |
| Share of retained profit for the year | - |
| Distribution of dividend | - |
| Acquisition of the remaining equity stake in Raiffeisen Leasing d.o.o | (68) |
| At 31 December | - |

39. Earnings per share attributable to equity holders of the parent

For the purpose of calculating earnings per share, earnings are calculated as the profit for the period attributable to equity holders of the Bank. The number of ordinary shares is the weighted average number of ordinary shares outstanding during the year after deducting the number of ordinary treasury shares. Given that there is no effect of options, convertible bonds or similar effect, the weighted average number of ordinary shares used for diluted earnings per share was the same as used to calculate basic earnings per share. Also, since there is no preferred shares and therefore neither dividends, available profit is equal to profit for the year after tax attributable to owners of the Bank.

| | Group 2017 | Group 2016 | Bank 2017 | Bank 2016 |
|--|---------------|---------------|---------------|---------------|
| Net profit for the year attributable to owners of the parent net of proposed dividend on preference shares | 188 | 535 | 396 | 460 |
| Weighted average number of ordinary shares outstanding during the year | 3,621,432 | 3,621,432 | 3,621,432 | 3,621,432 |
| Earnings per share attributable to owners of the parent in HRK | 51.80 | 147.44 | 109.24 | 127.08 |

40. Cash and cash equivalents

| | Notes | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|--|-------|---------------------------------|---------------------------------|--------------------------------|--------------------------------|
| Cash in hand | 6 | 804 | 712 | 804 | 712 |
| Items in the course of collection | 6 | - | 1 | - | 1 |
| Gyro account with the Croatian National Bank | 6 | 3,851 | 2,969 | 3,851 | 2,969 |
| Current accounts with other banks | 6 | 92 | 75 | 91 | 71 |
| Placements with and loans to other banks with original maturity up to three months | | 830 | 1,262 | 830 | 1,262 |
| Impairment allowance | | (48) | (51) | (48) | (51) |
| | | 5,529 | 4,968 | 5,528 | 4,964 |

Notes to the financial statements (continued)

41. Concentration of assets and liabilities

The Group's and Bank's assets are significantly concentrated on amounts due from the Republic of Croatia, as follows:

| | Notes | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|--|---------|------------------------------|------------------------------|-----------------------------|-----------------------------|
| Giro account with the Croatian National Bank | 6 | 3,851 | 2,969 | 3,851 | 2,969 |
| Deposits with the Croatian National Bank | 9 | - | 8 | - | 8 |
| Obligatory reserve with the Croatian National Bank | 7 | 1,757 | 1,695 | 1,757 | 1,695 |
| Government bonds, direct exposure | 8,10,12 | 2,739 | 2,804 | 1,886 | 1,944 |
| Treasury bills issued by the Ministry of Finance | 8,10,12 | 909 | 603 | 821 | 537 |
| Loans and advances to customers | 11 | 562 | 865 | 489 | 752 |
| Unidentified impairment losses | | (62) | (67) | (61) | (64) |
| Borrowings | | (913) | (1,078) | (913) | (1,078) |
| Deposits from the Republic of Croatia | | (41) | (80) | (41) | (80) |
| | | 8,802 | 7,719 | 7,789 | 6,683 |

In 2017 the borrowings include the liabilities to HBOR, therefore the amounts stated for 2016 have been reclassified accordingly.

In addition, the Bank had indirect exposure to the Republic of Croatia in respect of loans and advances to public funds and off-balance-sheet exposures as follows:

| | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|--|------------------------------|------------------------------|-----------------------------|-----------------------------|
| Loans and advances to customers guaranteed by the State | 289 | 523 | 216 | 410 |
| Guarantees, letters of credit and undrawn lending facilities | 8 | 8 | 8 | 8 |
| | 297 | 531 | 224 | 418 |

The total net direct and indirect on and off-balance-sheet exposure to Republic of Croatia represents 22% of the total assets and off-balance-sheet exposure of the Group (2016: 19%) and 20% of the total assets and off-balance-sheet exposure of the Bank (2016: 18%).

Notes to the financial statements (continued)

42. Repurchase and reverse repurchase agreements

The Group raises funds by selling financial instruments under agreements to repay the funds by repurchasing the instruments at future dates at the same price plus interest at a predetermined rate.

Repurchase agreements are commonly used as a tool for short-term financing of interest-bearing assets, depending on the prevailing interest rates. The financial instruments sold are not derecognised and the proceeds are accounted for as interest bearing borrowings. At the year-end assets sold under repurchase agreements were as follows:

| Group/Bank | Fair value of underlying assets HRK million | Carrying amount of corresponding liabilities HRK million | Repurchase date | Repurchase price HRK million |
|--|--|--|--|------------------------------------|
| 2017 | | | | |
| Securities at fair value through profit or loss | 175 | 160 | February 2020 November 2022 | 160 |
| 2016 | | | | |
| Securities at fair value through profit or loss | 248 | 241 | February-May 2017 February 2020 | 246 |
| Financial assets available for sale | 322 | 309 | January-March 2017 February 2020 | 314 |

Borrowings from EBRD in the amount of HRK 202 million (2016: HRK 249 million) are secured by financial instruments in the amount of HRK 249 million (2016: HRK 318 million).

The Group also purchases financial instruments under agreements to resell them at future dates ("reverse repurchase agreements"). The seller commits to repurchase the same or similar instruments at an agreed future date. Reverse repurchases are entered into as a facility to provide funds to customers and are accounted for as loans and advances to customers; the underlying financial instruments are not recognised. At year end assets purchased subject to agreements to resell them were as follows:

| Group and Bank | Fair value of assets held as collateral HRK million | Carrying amount of corresponding assets HRK million | Repurchase date | Repurchase price HRK million |
|--|--|---|------------------------|------------------------------------|
| Loans and advances to customers | | | | |
| 2017 | 86 | 75 | January- March 2018 | 75 |
| 2016 | 208 | 184 | January-May 2017 | 185 |

Notes to the financial statements (continued)

43. Commitments and contingent liabilities

The aggregate amounts of outstanding guarantees, letters of credit and undrawn loan commitments at 31 December were:

| | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|----------------------------|---------------------------------------|---------------------------------------|--------------------------------------|--------------------------------------|
| Guarantees | 2,439 | 2,897 | 2,444 | 2,904 |
| Letters of credit | 108 | 58 | 108 | 58 |
| Undrawn lending facilities | 5,465 | 5,254 | 5,232 | 5,120 |
| | 8,012 | 8,209 | 7,784 | 8,082 |

At 31 December 2017, the Group and the Bank recognised portfolio based provisions for off-balance-sheet risks arising from the issue of guarantees, letters of credits and undrawn lending commitments, in the amount of HRK 93 million (2016: HRK 103 million), which are included in provisions for liabilities and charges (see Note 23).

Group as a lessee

The Group leases certain business premises and other assets under operating lease arrangements. Lease payments are originally denominated in CHF. In accordance with IAS 39 "Financial Instruments: Recognition and Measurement", such lease commitments should be accounted for as an embedded derivative. Since market rates for forward CHF currency agreements in excess of six months are currently not easily available in Croatia, the Group is not able to calculate the fair value of the embedded option. Accordingly, gains and losses will be recognised through statement of profit or loss upon payment of the lease instalment.

Notes to the financial statements (continued)

44. Assets and liabilities managed on behalf of third parties

The Group provides trust and custody services to companies, banks, individuals, and investment and pension funds (all non-Group) whereby it holds and manages assets or invests funds received in various financial instruments at the direction of the customer. The Group receives fee income for providing these services. Trust assets are not assets of the Group and are not recognised in the consolidated statement of financial position. The Group is not exposed to any credit risk relating to such placements, as it does not guarantee these investments.

At 31 December 2017, the total assets under custody held by the Group on behalf of customers were HRK 5,201 million (2015: HRK 6,100 million).

In addition, at 31 December 2017, total assets of investment and pension funds under Group management amounted to HRK 31,310 million (2016: HRK 27,464 million).

During 2017 the Group made income in the amount of HRK 172 million (2016: HRK 161 million) of fees on trust activities provided to companies, banks and individuals, and management of investment and pension funds.

As at 31 December the Group and the Bank managed loans on behalf of third parties as follows:

| | 2017 HRK million | 2016 HRK million |
|--------------------------|---------------------|---------------------|
| Assets | | |
| - Loans to companies | 119 | 132 |
| Total assets | 119 | 132 |
| Liabilities | | |
| - Financial institutions | 119 | 132 |
| Total liabilities | 119 | 132 |

Notes to the financial statements (continued)

45. Derivative instruments and foreign currency trading

The Group and the Bank had the following derivative contracts accounted for as trading instruments open at year-end.

| Group | Notional amount | | Fair value | |
|--|-----------------|--------------|--------------------------|-------------------------------|
| | Assets | Liabilities | Assets HRK million | Liabilities HRK million |
| 2017 | | | | |
| - Forward foreign exchange contracts - OTC | 1,741 | 3,633 | 24 | 26 |
| - Cross-currency swaps - OTC | 99 | - | - | 5 |
| - Interest rate swaps - OTC | 543 | 481 | 5 | 11 |
| | 2,383 | 4,114 | 29 | 42 |
| Unsettled FX trade - OTC | 1,237 | 2,080 | 4 | 11 |

| Group | Notional amount | | Fair value | |
|--|-----------------|--------------|--------------------------|-------------------------------|
| | Assets | Liabilities | Assets HRK million | Liabilities HRK million |
| 2016 | | | | |
| - Forward foreign exchange contracts - OTC | 5,861 | 3,888 | 102 | 28 |
| - Cross-currency swaps- OTC | 114 | - | - | 6 |
| - Interest rate swaps - OTC | 325 | 883 | 6 | 51 |
| - Futures | - | 531 | - | 4 |
| | 6,300 | 5,302 | 108 | 89 |
| Unsettled FX trade – OTC | 1,217 | 1,183 | 1 | 1 |

Notes to the financial statements (continued)

45. Derivative instruments and foreign currency trading (continued)

| Bank | Notional amount | | Fair value | |
|--|-----------------|--------------|--------------------------|-------------------------------|
| | Assets | Liabilities | Assets HRK million | Liabilities HRK million |
| 2017 | | | | |
| - Forward foreign exchange contracts - OTC | 1,982 | 3,946 | 24 | 28 |
| - Cross-currency swaps - OTC | 99 | - | - | 5 |
| - Interest rate swaps - OTC | 685 | 481 | 10 | 11 |
| | 2,766 | 4,427 | 34 | 44 |
| Unsettled FX trade - OTC | 1,237 | 2,080 | 4 | 11 |

| Bank | Notional amount | | Fair value | |
|--|-----------------|--------------|--------------------------|-------------------------------|
| | Assets | Liabilities | Assets HRK million | Liabilities HRK million |
| 2016 | | | | |
| - Forward foreign exchange contracts - OTC | 5,865 | 4,057 | 103 | 28 |
| - Cross-currency swaps- OTC | 114 | - | - | 6 |
| - Interest rate swaps - OTC | 443 | 883 | 13 | 51 |
| - Futures | - | 531 | - | 4 |
| | 6,422 | 5,471 | 116 | 89 |
| Unsettled FX trade – OTC | 1,217 | 1,183 | 1 | 1 |

Notes to the financial statements (continued)

45. Derivative instruments and foreign currency trading (continued)

The Group and the Bank modified the presentation in 2017, so the buy and purchase trades are stated separately.

Fair value hedging

| | Average fixed interest rate | | Nominal amount | | Fair value | |
|--|-----------------------------|------|----------------|-------------|-------------|-------------|
| | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 |
| | % | % | HRK million | HRK million | HRK million | HRK million |
| Hedged instrument - loans from and advances to customers | 7.14 | 7.14 | 121 | 122 | 4 | 6 |
| Hedging instrument - Interest rate swap 1 to 5 years | 1.11 | 1.11 | 121 | 122 | (4) | (6) |

The hedge effectiveness ratio for the year ended was 99.83% (2016: 99.87%).

Notes to the financial statements (continued)

46. Related party transactions

Raiffeisenbank Austria d.d. and its subsidiaries are directly owned by Raiffeisen Bank International AG ("the RBI"), a Company founded in Austria. The ultimate parent bank is RBI, incorporated in Austria, to which and to whose affiliates (collectively "the RBI Group") the Group provides banking services. The Bank considers that it has an immediate related party relationship with its subsidiaries and associates, main shareholders, the Supervisory and Management Board members and other executive management of the Bank and its subsidiaries (together "key management personnel"), close family members of key management personnel, and entities controlled, jointly controlled or significantly influenced by key management personnel and their close family members. Key management personnel of the Group include members of Management Boards and Supervisory Boards of Group companies.

Key transactions with related parties

Assets and liabilities and off balance sheet exposures and income and expenses as at and for the year ended 31 December, arising from transactions with related parties were as follows:

| | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|--|---|---|--|--|
| Statement of total comprehensive income | | | | |
| <i>Interest, fee and commission income</i> | | | | |
| - Raiffeisen Leasing d.o.o. | - | - | 18 | 20 |
| - Raiffeisen Stambena štedionica d.d. | - | - | 4 | 5 |
| - Raiffeisen Consulting d.o.o. | - | - | 5 | 5 |
| - Raiffeisen društvo za upravljanje obveznim i dobrovoljnim mirovinskim fondom d.d. | - | - | 2 | 1 |
| - Raiffeisen mirovinsko osiguravajuće društvo d.d. | - | - | 2 | 1 |
| - Raiffeisen Factoring d.o.o. | - | - | - | 3 |
| - Raiffeisen Invest d.o.o. | - | - | 3 | 2 |
| - RBI | 4 | 3 | 4 | 3 |
| Total | 4 | 3 | 38 | 40 |
| <i>Interest, fee and commission expense</i> | | | | |
| - Raiffeisen stambena štedionica d.d. | - | - | - | (1) |
| - Raiffeisen društvo za upravljanje obveznim i dobrovoljnim mirovinskim fondovima d.d. | - | - | (1) | (1) |
| - RBI | (86) | (99) | (73) | (82) |
| - RBI Group | (13) | (20) | (9) | (10) |
| Total | (99) | (119) | (83) | (94) |

Notes to the financial statements (continued)

46. Related party transactions (continued)

| | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|--|---------------------------------|---------------------------------|--------------------------------|--------------------------------|
| Trading and other income | | | | |
| - Raiffeisen Leasing d.o.o. | - | - | 1 | 1 |
| - Raiffeisen stambena štedionica d.d. | - | - | 1 | 1 |
| - Raiffeisen društvo za upravljanje obveznim i dobrovoljnim mirovinskim fondovima d.d. | - | - | 67 | 67 |
| - Raiffeisen mirovinsko osiguravajuće društvo d.d. | - | - | 5 | 5 |
| - Raiffeisen Consulting d.o.o. | - | - | 2 | 2 |
| - Raiffeisen Factoring d.o.o. | - | - | 1 | 2 |
| - RBI | 105 | 1 | 105 | 1 |
| - RBI Group | 1 | - | 1 | - |
| Total | 106 | 1 | 183 | 79 |
| Operating expenses | | | | |
| - Raiffeisen Leasing d.o.o. | - | - | (4) | (4) |
| - Raiffeisen Consulting d.o.o. | - | - | (19) | (20) |
| - RBI | (37) | (38) | (37) | (38) |
| Total | (37) | (38) | (60) | (62) |
| Assets | | | | |
| Current accounts and placements with banks | | | | |
| - Raiffeisen stambena štedionica d.d. | - | - | 36 | 51 |
| - RBI | 57 | 22 | 57 | 22 |
| - RBI Group | 4 | 5 | 4 | 5 |
| Total | 61 | 27 | 97 | 78 |
| Loans from and advances to customers | | | | |
| - Raiffeisen Consulting d.o.o. | - | - | 87 | 82 |
| - Raiffeisen Leasing d.o.o. | - | - | 312 | 334 |
| Total | - | - | 399 | 416 |
| Accrued income and other assets | | | | |
| - Raiffeisen Leasing d.o.o. | - | - | 5 | 5 |
| - Raiffeisen Consulting d.o.o. | - | - | - | 8 |
| - RBI | 22 | 27 | 22 | 27 |
| Total | 22 | 27 | 27 | 40 |

Notes to the financial statements (continued)

46. Related party transactions (continued)

| | Group 2017 HRK million | Group 2016 HRK million | Bank 2017 HRK million | Bank 2016 HRK million |
|---|---------------------------------|---------------------------------|--------------------------------|--------------------------------|
| Liabilities | | | | |
| Deposits | | | | |
| - Raiffeisen Leasing d.o.o. | - | - | 26 | 61 |
| - Raiffeisen stambena štedionica d.d. | - | - | 38 | 79 |
| - Raiffeisen društvo za upravljanje obveznim i dobrovoljnim mirovinskim fondovima d.d. | - | - | 75 | 64 |
| - Raiffeisen mirovinsko osiguravajuće društvo d.d. | - | - | 40 | 27 |
| - Raiffeisen Factoring d.o.o. | - | - | 160 | 97 |
| - Raiffeisen Invest d.o.o. | - | - | 13 | 11 |
| - RBI | 320 | 27 | 320 | 27 |
| - RBI Group | 8 | 8 | 8 | 8 |
| Total | 328 | 35 | 680 | 374 |
| Borrowings and subordinated liabilities | | | | |
| - RBI | 1,644 | 1,493 | 859 | 869 |
| - RBI Group | - | 605 | - | - |
| Total | 1,644 | 2,098 | 859 | 869 |
| Accruals and other liabilities | | | | |
| - RBI | 43 | 89 | 43 | 89 |
| - RBI Group | 1 | 1 | 1 | 1 |
| Total | 44 | 90 | 44 | 90 |
| Off-balance sheet exposure | | | | |
| Derivative instruments | | | | |
| - Raiffeisen Leasing d.o.o. | - | - | 41 | 8 |
| - Raiffeisen stambena štedionica d.d. | - | - | 75 | - |
| - Raiffeisen društvo za upravljanje obveznim i dobrovoljnim mirovinskim fondovima d.d. | - | - | 113 | - |
| - Raiffeisen Consulting d.o.o. | - | - | 266 | 280 |
| - Raiffeisen Factoring d.o.o. | - | - | 237 | - |
| - Raiffeisen mirovinsko osiguravajuće društvo d.d. | - | - | 4 | - |
| - RBI | 4,000 | 6,006 | 4,000 | 6,006 |
| - RBI Grupa | - | 2 | - | 2 |
| Total | 4,000 | 6,008 | 4,736 | 6,296 |

Notes to the financial statements (continued)

46. Related party transactions (continued)

| 2017 | Exposure HRK million | Liabilities HRK million | Income HRK million | Expense HRK million |
|---|-------------------------|----------------------------|-----------------------|------------------------|
| Group | | | | |
| Key management personnel | | | | |
| Short-term benefits (salaries and fees) | - | 17 | - | 40 |
| Long-term benefits | - | - | - | 6 |
| Loans and advances | 26 | - | - | - |
| Deposits | - | 18 | - | - |
| Total | 26 | 35 | - | 46 |
| Bank | | | | |
| Key management personnel | | | | |
| Short-term benefits (salaries and fees) | - | 14 | - | 17 |
| Long-term benefits | - | - | - | 3 |
| Loans and advances | 7 | - | - | - |
| Deposits | - | 5 | - | - |
| Total | 7 | 19 | - | 20 |

| 2016 | Exposure HRK million | Liabilities HRK million | Income HRK million | Expense HRK million |
|---|-------------------------|----------------------------|-----------------------|------------------------|
| Group | | | | |
| Key management personnel | | | | |
| Short-term benefits (salaries and fees) | - | 16 | - | 40 |
| Long-term benefits | - | - | - | 4 |
| Loans and advances | 27 | - | 1 | - |
| Deposits | - | 18 | - | - |
| Total | 27 | 34 | 1 | 44 |
| Bank | | | | |
| Key management personnel | | | | |
| Short-term benefits (salaries and fees) | - | 13 | - | 17 |
| Long-term benefits | - | - | - | 2 |
| Loans and advances | 5 | - | - | - |
| Deposits | - | 2 | - | - |
| Total | 5 | 15 | - | 19 |

Notes to the financial statements (continued)

47. Risk management

This section provides details of the Group's exposure to risk and describes the methods used by management to control risk. The most important types of financial risk to which the Group is exposed are credit risk, liquidity risk and market risk. Market risk includes currency risk, interest rate risk and equity price risk.

An integrated system of risk management is established at the Group level by introducing a set of policies and procedures, determining the limits of risk levels acceptable to the Group. The limits are set according to the amount of regulatory capital and apply to all types of risk. Methodologies and models for managing operational risk have been developed by the Group.

Credit risk

The Group is exposed to credit risk through its trading, lending, economic hedging and investing activities and in cases where it acts as an intermediary on behalf of customers or other third parties or issues guarantees. The risk that counterparties to derivative or other instruments might default on their obligations is monitored on an ongoing basis. To manage the level of credit risk, the Group deals with counterparties of good credit standing, and when appropriate, obtains collateral.

The Group's primary exposure to credit risk arises through its loans and advances. The amount of credit exposure in this regard is represented by the carrying amounts of the assets on the statement of financial position. In addition, the Group is exposed to off-balance-sheet credit risk through unutilized part of loans granted and guarantees issued – refer to Note 43.

Exposure to credit risk is managed in accordance with the Group's policies. Credit exposures to portfolios and individual risk groups are reviewed on a regular basis. Breaches of set limits are reported to appropriate authority level. Any substantial increases in credit exposure are authorized by the Credit Committee. The Credit Committee and Problem Loan Committee monitor changes in the creditworthiness of borrowers.

In case the analysis of borrower's creditworthiness proves to be inadequate a workout officer calculates and recommends creation of individual loan loss provisions. Problem loan committee decides upon individual loan loss provisions. Credit risk assessment is an ongoing process designed to facilitate the early identification of impairment of credit exposures.

The Group applies a prudent approach to credit risk assessment. When a credit exposure is classified as „Work-out“ („WO“) for the first time it has to be transferred to the Collections and Workout Division and reported to the Problem Loan Committee. However, in the case of default, the client has to be evidenced in the Default Data Base (DDB) and immediately transferred to Work-out Department.

According to local methodology (CNB) for those placements, Bank uses the following classification into the appropriate risk groups:

A group – placements that are fully recoverable

B group – placements that are partially recoverable

1) subgroup B-1 - value adjustment at least 1% but not higher than 30% of each placement

2) subgroup B-2 - value adjustment more than 30%, but not higher than 70% of each placement

3) subgroup B-3 - value adjustment more than 70% but less than 100% of each placement

C group – placements that are fully unrecoverable - 100% value adjustment

The Bank uses an early warning system for identifying potentially doubtful accounts among its non-retail customers. This is a kind of support to timely identify any changes in the risk level of a particular customer. Monitoring is performed on a monthly basis. Once an early warning is provided, it is acted upon by analysing its value and root cause. Depending on the risk level rating of a customer (1-4), the customer remains within the Corporate Division (1 - regular customer and 2 - pre-workout customer) or is transferred to the Loan Workout Division (3 - Early workout stage or 4 - Late workout stage or legal action).

Early Warning System is also used for Micro segment. The EWS output is mainly based on an evaluation of the customer's behavior and the monitoring is performed on a monthly basis. Customers are classified according to their risk profile (low, medium, high) and appropriate actions are taken as per their category.

Notes to the financial statements (continued)

47. Risk management (continued)

Credit risk (continued)

The Credit Committee has the authority to approve new limit to the clients of risk status 1 and 2. The decision of the Credit Committee can be reversed only by the Supervisory Board. The Problem Loan Committee has the authority for credit reviews of the clients with risk status 3 and 4, and is in charge of determination of individual loan loss provisions.

The Group's credit policies contain retail and corporate customer lending guidelines. The credit policies define the criteria for providing funds to e.g. target industries, structuring portfolios in line with customer ratings, by type of collateral, and similar. The Group has internal policies in place that regulate acceptable types of collateral and their valuation. Most frequently provided security instruments comprise real estate, cash deposits, movable property, inventories, listed securities and other assets.

Concentration of risk and maximum exposure to credit risk

The table below shows the maximum exposure to credit risk for the components of the statement of financial position:

| | Notes | 2017 Group HRK million | 2016 Group HRK million | 2017 Bank HRK million | 2016 Bank HRK million |
|---|-------|---------------------------------|---------------------------------|--------------------------------|--------------------------------|
| Cash and current accounts with banks | 6 | 3,904 | 3,008 | 3,903 | 3,004 |
| Obligatory reserve with the Croatian National Bank | 7 | 1,739 | 1,675 | 1,739 | 1,675 |
| Financial assets at fair value through profit or loss | 8 | 948 | 2,508 | 572 | 2,146 |
| Placements with, and loans and advances to banks | 9 | 894 | 1,332 | 905 | 1,384 |
| Loans and advances to customers | | | | | |
| Corporate | 11 | 7,822 | 8,660 | 7,205 | 7,028 |
| Retail (individuals) | | 9,923 | 9,844 | 9,248 | 9,185 |
| Financial assets available for sale | 10 | 5,906 | 5,188 | 5,586 | 4,892 |
| Financial investments held to maturity | 12 | 279 | 293 | - | - |
| Other assets | 17 | 81 | 101 | 44 | 44 |
| | | 31,496 | 32,609 | 29,202 | 29,358 |

The table below shows the maximum exposure to credit risk for the components of the off balance:

| | Notes | 2017 Group HRK millions | 2016 Group HRK millions | 2017 Bank HRK millions | 2016 Bank HRK millions |
|--|-------|----------------------------------|----------------------------------|---------------------------------|---------------------------------|
| Contingent liabilities and commitments | | | | | |
| Guarantees | 43 | 2,439 | 2,897 | 2,444 | 2,904 |
| Letters of credit and undrawn lending facilities | 43 | 5,573 | 5,312 | 5,340 | 5,178 |
| | | 8,012 | 8,209 | 7,784 | 8,082 |
| Impairment losses | | (93) | (103) | (93) | (103) |
| | | 7,919 | 8,106 | 7,691 | 7,979 |

Notes to the financial statements (continued)

47. Risk management (continued)

Credit risk (continued)

Concentration of risk and maximum exposure to credit risk (continued)

Concentration of credit risk by geographic region and industry

The Group and Bank have a diversified portfolio within Croatia covering all sectors of the economy. The majority of commercial lending is to companies and individuals domiciled in Croatia. The Group and Bank have the following gross credit risk concentration by geographic region and industry:

| | 2017 | | 2016 | | 2017 | | 2016 | |
|---------------------------|------------------------------------|--|------------------------------------|--|------------------------------------|---|------------------------------------|---|
| | Balance sheet exposure HRK million | Group Off-balance sheet exposure HRK million | Balance sheet exposure HRK million | Group Off-balance sheet exposure HRK million | Balance sheet exposure HRK million | Bank Off-balance sheet exposure HRK million | Balance sheet exposure HRK million | Bank Off-balance sheet exposure HRK million |
| Geographic region: | | | | | | | | |
| Croatia | 29,164 | 7,977 | 29,732 | 8,089 | 26,299 | 7,749 | 26,366 | 7,962 |
| Rest of EU | 3,351 | 29 | 4,466 | 114 | 3,351 | 29 | 4,466 | 114 |
| Non EU | 81 | 5 | 240 | 5 | 81 | 5 | 240 | 5 |
| Other | 1,034 | 1 | 1,024 | 1 | 1,034 | 1 | 1,023 | 1 |
| Total | 33,630 | 8,012 | 35,462 | 8,209 | 30,765 | 7,784 | 32,095 | 8,082 |
| Impairment losses | (2,134) | (93) | (2,853) | (103) | (1,563) | (93) | (2,737) | (103) |
| | 31,496 | 7,919 | 32,609 | 8,106 | 29,202 | 7,691 | 29,358 | 7,979 |

Concentration of credit risk by industry:

| | Group 2017 % | Group 2016 % | Bank 2017 % | Bank 2016 % |
|------------------------------|--------------|--------------|-------------|-------------|
| Individuals | 28 | 27 | 29 | 28 |
| Financial services | 19 | 18 | 21 | 20 |
| Trade | 9 | 10 | 9 | 9 |
| Central and local government | 14 | 16 | 12 | 15 |
| Construction | 5 | 6 | 5 | 6 |
| Food and drink industry | 3 | 4 | 3 | 3 |
| Non-metal industry | 5 | 5 | 4 | 5 |
| Electronics | 3 | 2 | 3 | 2 |
| Wood and paper industry | 1 | 1 | 1 | 1 |
| Craft and services | 10 | 8 | 10 | 8 |
| Other business activities | 3 | 3 | 3 | 3 |
| Total credit risk | 100 | 100 | 100 | 100 |

Notes to the financial statements (continued)

47. Risk management (continued)

Credit risk (continued)

Concentration of risk and maximum exposure to credit risk (continued)

Concentration of risk assets related to risk groups including balance sheet and off-balance sheet exposure

| Rating | 2017 Group | Impairment allowances | Net exposure | 2016 Group | Impairment allowances | Net exposure |
|--------------|----------------------------------|--------------------------|---------------|----------------------------------|--------------------------|---------------|
| | Total exposure HRK million | | | Total exposure HRK million | | |
| A | 38,861 | 349 | 38,512 | 40,307 | 373 | 39,934 |
| B1 | 708 | 94 | 614 | 389 | 73 | 316 |
| B2 | 617 | 393 | 224 | 667 | 377 | 290 |
| B3 | 512 | 447 | 65 | 1,137 | 962 | 175 |
| C | 944 | 944 | - | 1,171 | 1,171 | - |
| Total | 41,642 | 2,227 | 39,415 | 43,671 | 2,956 | 40,715 |

| Rating | 2017 Bank | Impairment allowances | Net exposure | 2016 Bank | Impairment allowances | Net exposure |
|--------------|----------------------------------|--------------------------|---------------|----------------------------------|--------------------------|---------------|
| | Total exposure HRK million | | | Total exposure HRK million | | |
| A | 36,460 | 338 | 36,122 | 36,929 | 351 | 36,578 |
| B1 | 638 | 88 | 550 | 369 | 72 | 296 |
| B2 | 356 | 200 | 156 | 665 | 376 | 289 |
| B3 | 503 | 438 | 65 | 1,131 | 957 | 174 |
| C | 592 | 592 | - | 1,084 | 1,084 | - |
| Total | 38,549 | 1,656 | 36,893 | 40,178 | 2,840 | 37,337 |

Notes to the financial statements (continued)

47. Risk management (continued)

Credit risk (continued)

Maturity structure of loans to customers

| Loans to customers (HRK millions) | Group 2017 | Group 2016 | Bank 2017 | Bank 2016 |
|--|-----------------------|-----------------------|------------------|------------------|
| Neither past due nor impaired | 8,994 | 9,385 | 7,586 | 8,519 |
| Past due but not impaired | 8,173 | 7,618 | 8,388 | 7,454 |
| Impaired loans and advances to customers | 2,599 | 4,219 | 1,940 | 2,851 |
| | 19,766 | 21,222 | 17,914 | 18,824 |
| Impairment losses | (2,021) | (2,718) | (1,461) | (2,611) |
| | 17,745 | 18,504 | 16,453 | 16,213 |

Thereof loans to companies and similar entities

| (HRK millions) | Group 2017 | Group 2016 | Bank 2017 | Bank 2016 |
|-------------------------------|-------------------|-------------------|------------------|------------------|
| Neither past due nor impaired | 3,300 | 3,008 | 1,893 | 2,146 |
| Past due but not impaired | 4,919 | 4,143 | 5,138 | 4,442 |
| Impaired loans to customers | 1,505 | 3,323 | 867 | 2,161 |
| | 9,724 | 10,474 | 7,898 | 8,749 |
| Impairment losses | (1,255) | (1,814) | (703) | (1,721) |
| | 8,469 | 8,660 | 7,195 | 7,028 |

Thereof loans to individuals

| (HRK millions) | Group 2017 | Group 2016 | Bank 2017 | Bank 2016 |
|-------------------------------|-------------------|-------------------|------------------|------------------|
| Neither past due nor impaired | 5,694 | 6,377 | 5,693 | 6,373 |
| Past due but not impaired | 3,254 | 3,475 | 3,250 | 3,012 |
| Impaired loans to customers | 1,094 | 896 | 1,073 | 690 |
| | 10,042 | 10,748 | 10,016 | 10,075 |
| Impairment losses | (766) | (904) | (758) | (890) |
| | 9,276 | 9,844 | 9,258 | 9,185 |

Ageing of past due but not impaired receivables

| | Group 2017 | Group 2016 | Bank 2017 | Bank 2016 |
|----------------------|------------------------|-----------------------|------------------------|------------------------|
| | HRK million | HRK million | HRK million | HRK million |
| Up to 30 days | 8,167 | 7,241 | 8,388 | 7,199 |
| Up to 31 - 90 days | 6 | 258 | - | 255 |
| Up to 91 - 180 days | - | 1 | - | - |
| Up to 181 - 365 days | - | 10 | - | - |
| Over 365 days | - | 108 | - | - |
| | 8,173 | 7,618 | 8,388 | 7,454 |

The Note is prepared on the basis of total amount past due, not according to the portion past due.

Notes to the financial statements (continued)

47. Risk management (continued)

Liquidity risk

Important role which banks perform in financial markets is maturity transformation. The need for the maturity transformation comes from the fact that the banks depositors' require quick and short term access to their deposited funds while on the other hand other group of bank clients requires funding via long term loans. This situation gives rise to the persistent discrepancies between inflows and outflows of the bank in various time bands (liquidity gaps). In order to manage these discrepancies or gaps, the bank engages in various transactions with other members of the financial market, taking into consideration not only contractual maturity, but also experientially maturity of assets and liabilities. Hence, liquidity gaps result in liquidity risk which manifests itself in the form of the risk that the bank won't be able to finance (refinance) its positions under acceptable terms and in the form of the risk that the bank won't be able to efficiently liquidate its assets in acceptable time period.

The Group continually assesses liquidity risk by identifying and monitoring changes in the level of mismatch between inflows and outflows on total and on currency level, and changes in the availability of funds needed for achieving defined business and strategic goals. In addition, the Group maintains a portfolio of liquid assets which can, if needed, be used as a source of fresh funds. The liquidity risk is managed through alignment of assets and liabilities, through setup of market, credit and liquidity gaps limits and through achieving appropriate levels of liquidity indicator, including holding of sufficiently large liquidity buffer, stress tests based on different scenarios, and liquidity contingency plan.

All these measures, assessments and analyses are discussed regularly in the Asset/Liability Committee meetings.

The Group aligns its business activities in line with legal regulation concerning liquidity risk and in line with the internal and the RBI Group acts concerning the management of liquidity reserve.

Special attention is devoted to Basel III liquidity risk measures, especially Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR). The ratios are monitored on daily (LCR) and quarterly (NSFR) basis. Both, LCR and NSFR were maintained above internal targets set for both ratios at 100%.

Short term liquidity gap is also analysed through liquidity surplus and the ratio of expected (modelled) cash inflows and counterbalancing capacity to cash outflows and selected maturities are shown on cumulative basis. Analyses include all balance and off balance sheet positions.

| In HRK million | 2017 | | | 2016 | | |
|-----------------|--------|---------|--------|--------|---------|--------|
| | 7 days | 30 days | 1 year | 7 days | 30 days | 1 year |
| Liquidity gap | 6,258 | 7,034 | 6,893 | 6,428 | 6,568 | 6,640 |
| Liquidity ratio | 183% | 179% | 137% | 208% | 168% | 131% |

To further control and limit the liquidity risk, target loan/deposits ratios are reviewed for certain members of the Group, taking into account the requirements of Basel III. The Group also conducts liquidity stress-tests analysis on daily level in order to determine the necessary liquidity buffer.

Special attention is devoted to defining the Group's financial plans that include a wide variety of financing for mitigation funding liquidity risks. Funds are raised using a broad range of instruments including deposits, borrowings, and share capital. Different funding sources are mutually coordinated and optimized.

Notes to the financial statements (continued)

47. Risk management (continued)

Maturity analysis

The remaining contractual maturity of the Group and Bank assets and liabilities as at 31 December 2017 and as at 31 December 2016 is presented in the tables below:

The items with undefined maturity are included in terms over 5 years, obligatory reserve in the category up to one month and not according to the maturity of the related liabilities. Demand deposits from retail and corporate customers are shown in the category up to one month although the Bank's experience is that these deposits have much longer maturity. Mismatch in the category up to one year would have been eliminated if their maturity was presented in accordance with expected maturities, and liquid financial assets at fair value through profit or loss for which there is an active secondary market in category 1-3 months and 3-13 months.

| Group | Up to 1 month HRK million | 1-3 months HRK million | 3-12 months HRK million | 1-5 years HRK million | Over 5 years HRK million | Total HRK million |
|--|--|---|--|--|---|----------------------------------|
| 2017 | | | | | | |
| Assets | | | | | | |
| Cash and current accounts with banks | 4,708 | - | - | - | - | 4,708 |
| Obligatory reserve with the Croatian National Bank | 1,739 | - | - | - | - | 1,739 |
| Financial assets at fair value through profit or loss | 584 | 2 | 365 | - | - | 951 |
| Placements with and loans to other banks | 869 | 25 | - | - | - | 894 |
| Financial assets available for sale | 261 | 592 | 1,910 | 2,760 | 414 | 5,937 |
| Loans to customers | 2,358 | 784 | 2,870 | 7,150 | 4,583 | 17,745 |
| Financial investments held to maturity | 2 | - | 56 | 190 | 31 | 279 |
| Property, plant and equipment | - | - | - | - | 1,309 | 1,309 |
| Intangible assets | 7 | - | - | - | 232 | 239 |
| Deferred tax asset | - | - | - | 86 | - | 86 |
| Other asset | 150 | 6 | 5 | 128 | 2 | 291 |
| Total assets | 10,678 | 1,409 | 5,206 | 10,314 | 6,571 | 34,178 |
| Liabilities and equity | | | | | | |
| Financial liabilities at fair value through profit or loss | 59 | - | - | - | - | 59 |
| Deposits from banks | 1,056 | - | - | - | - | 1,056 |
| Deposits from companies and other similar entities | 9,101 | 146 | 199 | 78 | 25 | 9,549 |
| Deposits from individuals | 6,917 | 1,560 | 4,116 | 1,580 | 58 | 14,231 |
| Borrowings | 35 | 115 | 774 | 1,398 | 250 | 2,572 |
| Provisions for liabilities and charges | 1 | 1 | 23 | 145 | 3 | 173 |
| Other liabilities | 455 | 32 | 88 | 205 | 171 | 951 |
| Income tax | - | - | 70 | - | - | 70 |
| Subordinated liabilities | - | - | 6 | - | 826 | 832 |
| Equity attributable to the equity holders of the parent | - | - | - | - | 4,685 | 4,685 |
| Total liabilities and equity | 17,624 | 1,854 | 5,276 | 3,406 | 6,018 | 34,178 |
| Maturity gap | (6,946) | (445) | (70) | 6,908 | 553 | - |

Notes to the financial statements (continued)

47. Risk management (continued)

Maturity analysis (continued)

| Group | Up to 1 month HRK million | 1-3 months HRK million | 3-12 months HRK million | 1-5 years HRK million | Over 5 years HRK million | Total HRK million |
|--|------------------------------------|---------------------------------|----------------------------------|--------------------------------|-----------------------------------|-------------------------|
| 2016 | | | | | | |
| Assets | | | | | | |
| Cash and current accounts with banks | 3,721 | - | - | - | - | 3,721 |
| Obligatory reserve with the Croatian National Bank | 1,675 | - | - | - | - | 1,675 |
| Financial assets at fair value through profit or loss | 2,078 | - | 437 | - | - | 2,515 |
| Placements with and loans to other banks | 1,253 | - | 79 | - | - | 1,332 |
| Financial assets available for sale | 256 | 199 | 1,034 | 3,581 | 147 | 5,217 |
| Loans from and advances to customers | 2,476 | 1,464 | 3,035 | 7,215 | 4,314 | 18,504 |
| Financial investments held to maturity | 3 | 2 | 33 | 145 | 110 | 293 |
| Property, plant and equipment | - | - | - | - | 1,496 | 1,496 |
| Intangible assets | 4 | - | - | - | 236 | 240 |
| Deferred tax asset | - | - | - | 86 | - | 86 |
| Other tax asset | 150 | 7 | 8 | 120 | - | 285 |
| Total assets | 11,616 | 1,672 | 4,626 | 11,147 | 6,303 | 35,364 |
| Liabilities and equity | | | | | | |
| Financial liabilities at fair value through profit or loss | 97 | - | - | - | - | 97 |
| Deposits from banks | 441 | - | - | - | - | 441 |
| Deposits from companies and other similar entities | 8,924 | 241 | 607 | 84 | 35 | 9,891 |
| Deposits from individuals | 5,763 | 1,791 | 4,759 | 1,870 | 70 | 14,253 |
| Borrowings | 139 | 498 | 1,444 | 1,642 | 269 | 3,992 |
| Provisions for liabilities and charges | - | 7 | 31 | 146 | 3 | 187 |
| Other liabilities | 319 | 28 | 91 | 217 | 121 | 776 |
| Subordinated liabilities | - | - | 6 | - | 831 | 837 |
| Equity attributable to the owners of the parent | - | - | - | - | 4,890 | 4,890 |
| Total liabilities and equity | 15,683 | 2,565 | 6,938 | 3,959 | 6,219 | 35,364 |
| Maturity gap | (4,067) | (893) | (2,312) | 7,188 | 84 | - |

Notes to the financial statements (continued)

47. Risk management (continued)

Maturity analysis (continued)

| Bank | Up to 1 month HRK million | 1-3 months HRK million | 3-12 months HRK million | 1-5 years HRK million | Over 5 years HRK million | Total HRK million |
|--|------------------------------------|---------------------------------|----------------------------------|--------------------------------|-----------------------------------|-------------------------|
| 2017 | | | | | | |
| Assets | | | | | | |
| Cash and current accounts with banks | 4,707 | - | - | - | - | 4,707 |
| Obligatory reserve with the Croatian National Bank | 1,739 | - | - | - | - | 1,739 |
| Financial assets at fair value through profit or loss | 518 | 1 | 54 | - | - | 573 |
| Placements with and loans to other banks | 869 | - | - | - | 36 | 905 |
| Financial assets available for sale | 55 | 591 | 1,910 | 2,718 | 343 | 5,617 |
| Loans to customers | 2,305 | 519 | 2,627 | 6,761 | 4,241 | 16,453 |
| Investments in subsidiaries | - | - | - | - | 395 | 395 |
| Property, plant and equipment | - | - | - | - | 492 | 492 |
| Intangible assets | - | - | - | - | 204 | 204 |
| Deferred tax asset | - | - | - | 84 | - | 84 |
| Other and Current tax asset | 131 | 1 | 2 | 74 | 2 | 210 |
| Total assets | 10,324 | 1,112 | 4,593 | 9,637 | 5,713 | 31,379 |
| Liabilities and equity | | | | | | |
| Financial liabilities at fair value through profit or loss | 61 | - | - | - | - | 61 |
| Deposits from banks | 1,093 | - | - | - | - | 1,093 |
| Deposits from companies and other similar entities | 9,375 | 145 | 220 | 52 | 25 | 9,817 |
| Deposits from individuals | 6,901 | 1,534 | 4,002 | 709 | 57 | 13,203 |
| Borrowings | 35 | 42 | 174 | 789 | 197 | 1,237 |
| Provisions for liabilities and charges | - | - | 23 | 136 | 3 | 162 |
| Income tax | - | - | 79 | - | - | 79 |
| Other liabilities | 415 | - | 14 | 8 | - | 437 |
| Subordinated liabilities | - | - | 6 | - | 826 | 832 |
| Equity | - | - | - | - | 4,458 | 4,458 |
| Total liabilities and equity | 17,880 | 1,721 | 4,518 | 1,694 | 5,566 | 31,379 |
| Maturity gap | (7,556) | (609) | 75 | 7,943 | 147 | - |

Notes to the financial statements (continued)

47. Risk management (continued)

Maturity analysis (continued)

| Bank | Up to 1 month HRK million | 1-3 months HRK million | 3-12 months HRK million | 1-5 years HRK million | Over 5 years HRK million | Total HRK million |
|--|------------------------------------|---------------------------------|----------------------------------|--------------------------------|-----------------------------------|-------------------------|
| 2016 | | | | | | |
| Assets | | | | | | |
| Cash and current accounts with banks | 3,717 | - | - | - | - | 3,717 |
| Obligatory reserve with the Croatian National Bank | 1,675 | - | - | - | - | 1,675 |
| Financial assets at fair value through profit or loss | 2,024 | - | 127 | - | - | 2,151 |
| Placements with and loans to other banks | 1,254 | - | 79 | 15 | 36 | 1,384 |
| Financial assets available for sale | 75 | 199 | 1,034 | 3,544 | 69 | 4,921 |
| Loans from and advances to customers | 2,297 | 644 | 2,423 | 6,819 | 4,030 | 16,213 |
| Investments in subsidiaries | - | - | - | - | 408 | 408 |
| Property, plant and equipment | - | - | - | - | 478 | 478 |
| Intangible assets | - | - | - | - | 206 | 206 |
| Deferred tax asset | - | - | - | 83 | - | 83 |
| Other and Current tax asset | 112 | 1 | 4 | 63 | - | 180 |
| Total assets | 11,154 | 844 | 3,667 | 10,524 | 5,227 | 31,416 |
| Liabilities and equity | | | | | | |
| Financial liabilities at fair value through profit or loss | 97 | - | - | - | - | 97 |
| Deposits from banks | 450 | - | 70 | - | - | 520 |
| Deposits from companies and other similar entities | 9,121 | 238 | 648 | 60 | 23 | 10,090 |
| Deposits from individuals | 5,744 | 1,750 | 4,561 | 1,080 | 60 | 13,195 |
| Borrowings | 63 | 255 | 390 | 808 | 243 | 1,759 |
| Provisions for liabilities and charges | - | 6 | 30 | 137 | 3 | 176 |
| Other liabilities | 269 | - | 16 | 7 | - | 292 |
| Subordinated liabilities | - | - | 6 | - | 831 | 837 |
| Equity | - | - | - | - | 4,450 | 4,450 |
| Total liabilities and equity | 15,744 | 2,249 | 5,721 | 2,092 | 5,610 | 31,416 |
| Maturity gap | (4,590) | (1,405) | (2,054) | 8,432 | (383) | - |

Notes to the financial statements (continued)

46. Risk management (continued)

Market risk

Market risk is the risk of experiencing losses due to adverse changes in market prices, i.e. risk that changes in market prices, such as interest rates, foreign exchange rates and others could affect the Group's income or the value of its holdings of financial instruments. Market risk estimates are based on changes in exchange rates, interest rates, credit spreads, equity and commodity prices, and other market parameters. The Objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return on risk.

Market risk management of the Group and the Bank is conducted in accordance with legislative requirements and directives of domestic and foreign regulators, which is defined in internal policies and procedures which are regularly revised by risk division.

Group, within RBI Group, uses a comprehensive risk management approach for both the trading book and non-trading book (total-return approach). Market risks are managed consistently in the trading and non-trading book. The following values are measured and limited on a daily basis in the market risk management system:

- Value-at-Risk (confidence level 99%, holding period 1 day)

Value-at-risk (VaR) is the most important instrument in measuring market risks in normal situation. It represents maximum expected loss that is acceptable for the bank at a certain point of time. The VaR risk measure is a statistically defined estimate of the worst potential loss of a current portfolio, for a specified confidence level, over a given period during which positions can be closed. The Group is using a combination of a hybrid Monte Carlo and historical methods for VaR calculation. This methodology has been developed internally in the RBI Group to monitor the interest rate risk, foreign exchange risk, price risk, basis risk and the credit spread risk on the basis of a one-day holding period and a confidence level of 99%. This confidence level is used for internal monitoring. VaR Sensitivity gives a relation between sensitivities of risk factors and VaR change and is used for daily monitoring of VaR and risk management.

The quality of the VaR model is continuously monitored by backtesting and by Distributional test which is performed once a year.

- Stress test

Value-at-risk number provides the maximum losses that will not be exceeded at a certain confidence level under normal market conditions, but does not provide additional information on potential effects in the case of extreme market movements. So, in order to take these events into account as well, Group carries out daily stress tests. In this way the Bank simulates possible crisis situations and their impact on the current positions. Stress testing is used to assess the impact of market risk on the portfolio of the Group's total positions and limits in extraordinary circumstances (market shocks).

Stress testing is conducted on a daily basis, and the results are included in the regular daily reports.

- Positions and sensitivities limits (to changes in exchange rates, interest rates, etc.)

Sensitivity limits are used to avoid clustering in normal market situations and are the main management instruments in stress situations or in markets that are illiquid or structurally difficult to measure.

- Stop-loss limits

This limit supports traders' discipline in measuring proprietary trading positions and severely limiting losses rather than allowing them to accumulate.

High-water mark year-to-date stop loss limits are applied to the cumulative profit and losses on a year-to date basis. S/L limits have to be defined and applied for all positions classified under IFRS as AFS, AFV, and HFT.

The limit resets to zero at the beginning of each calendar year, whereas the loss has to be calculated versus the maximum profit in the year-to-date period (total return).

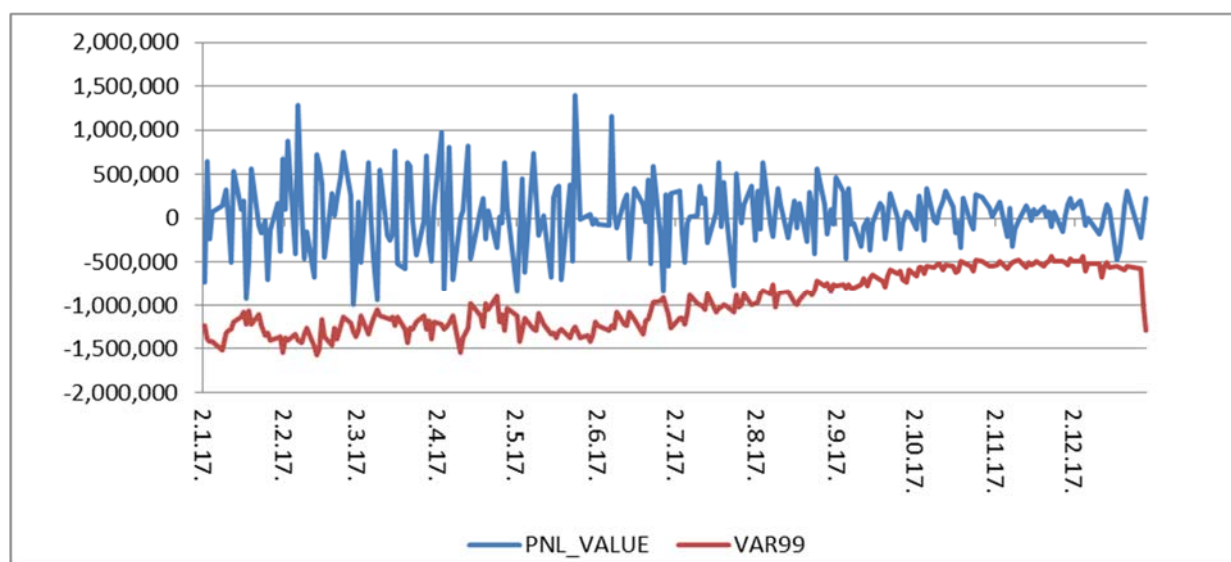
Notes to the financial statements (continued)

47. Risk management (continued)

Market risk (continued)

Value-at-Risk for Year 2017 and Year 2016

| HRK millions | December 2017 | December 2016 | Average | Min | Max |
|--------------------|---------------|---------------|-------------|-------------|--------------|
| Interest rate risk | | | | | |
| - trading book | 0,96 | 1,65 | 1,60 | 0,35 | 3,17 |
| - banking book | 1,60 | 10,81 | 6,75 | 1,44 | 11,70 |
| Currency risk | 1,47 | 0,18 | 0,65 | 0,08 | 2,05 |
| Credit Spread Risk | 9,49 | 2,53 | 2,31 | 1,25 | 9,49 |
| Price risk | 0,07 | 0,13 | 0,10 | 0,07 | 0,15 |
| Total VaR | 9,75 | 9,57 | 7,29 | 3,27 | 11,69 |



The efficiency of VaR model is periodically tested with backtesting procedures. Backtesting methods comprise comparison of 1-day VaR figures with appropriate (hypothetical) statement of comprehensive income figures as seen on the next working day (i.e. over the horizon for which the VaR figure was calculated). Backtesting breach is recorded on date on which (hypothetical) statement of comprehensive income is negative and its absolute value is higher than the VaR calculated for that date (i.e. when the hypothetical loss is greater than the VaR). The high number of backtesting breaches detected during a certain period, in an amount that is higher than the one expected considering the confidence level chosen during the calculation of VaR figures, can indicate that there are certain deficiencies in the VaR model.

As the figure shows, during 2017 no backtesting breaches were recorded.

Notes to the financial statements (continued)

a. Risk management (continued)

a) *Interest rate risk*

Interest rate risk is reflected as negative impact of interest rates on the present value of future cash flows, and hence the net interest income and other cash flows are sensitive to interest rate changes.

The primary sources of interest rate risk are as follows:

- repricing risk is a result of a timing differences in the maturity (for fix-rate) and repricing mismatch (for floating-rate) of assets and liabilities as well as off-balance-sheet positions;
- yield curve risk arises when unanticipated shifts of the yield curve have adverse effect on a bank's income or underlying economic value;
- basis risk arises from imperfect correlation in the adjustment of the rates earned and paid on different instruments with otherwise similar repricing characteristics (except the type of interest rate);
- optionality risk

Risk management activities are aimed at optimizing net interest income, given market interest rate levels, consistent with the Group's business strategies. To achieve its risk management objectives, the Group also uses interest rate derivatives.

Notes to the financial statements (continued)

47. Risk management (continued)

Interest rate repricing, gap analysis and amounts subject to fixed interest rates

The following tables present the Group's and the Bank's assets and liabilities and equity analysed according to repricing periods determined as the earlier of remaining contractual maturity and contractual repricing. The tables are management's estimate of the interest rate risk for the Group and the Bank as at 31 December 2017 and as at 31 December 2016 and are not necessarily indicative of the positions at other times but provide some indication of the sensitivities of the Group's and the Bank's earnings to movements in interest rates. Earnings will also be affected by the currency of the assets and liabilities and equity. The Group and the Bank have a significant proportion of interest-earning assets and interest-bearing liabilities in foreign currency.

| Group | Non-interest bearing | Up to 1 month | 1-3 months | 3-12 months | Over 12 months | Total | Fixed interest rates |
|--|----------------------|---------------|----------------|----------------|----------------|---------------|----------------------|
| | HRK million | HRK million | HRK million | HRK million | HRK million | HRK million | HRK million |
| 2017 | | | | | | | |
| Assets | | | | | | | |
| Cash and current accounts with banks | 4,707 | 1 | - | - | - | 4,708 | - |
| Obligatory reserve with the Croatian National Bank | 1,739 | - | - | - | - | 1,739 | - |
| Financial assets at fair value through profit or loss | 36 | 720 | 118 | 77 | - | 951 | 915 |
| Placements with and loans to other banks | 14 | 855 | 25 | - | - | 894 | 916 |
| Financial assets available for sale | 574 | 27 | 622 | 2,010 | 2,704 | 5,937 | 4,951 |
| Loans from and advances to customers | 54 | 12,692 | 644 | 612 | 3,743 | 17,745 | 7,295 |
| Financial investments held to maturity | 4 | 63 | 27 | 20 | 165 | 279 | 275 |
| Property, plant and equipment | 1,309 | - | - | - | - | 1,309 | - |
| Intangible assets | 239 | - | - | - | - | 239 | - |
| Deferred tax asset | 86 | - | - | - | - | 86 | - |
| Other asset | 291 | - | - | - | - | 291 | - |
| Total assets | 9,053 | 14,358 | 1,436 | 2,719 | 6,612 | 34,178 | 14,352 |
| Liabilities and equity | | | | | | | |
| Financial liabilities at fair value through profit or loss | 59 | - | - | - | - | 59 | - |
| Deposits from banks | 276 | 780 | - | - | - | 1,056 | 748 |
| Deposits from companies and other similar entities | 3,695 | 5,438 | 123 | 216 | 77 | 9,549 | 601 |
| Deposits from individuals | 84 | 6,894 | 1,508 | 4,115 | 1,630 | 14,231 | 8,203 |
| Borrowings | 20 | 733 | 583 | 435 | 801 | 2,572 | 1,135 |
| Provisions for liabilities and charges | 173 | - | - | - | - | 173 | - |
| Income tax | 70 | - | - | - | - | 70 | - |
| Other liabilities | 951 | - | - | - | - | 951 | - |
| Subordinated liability | 5 | - | 451 | - | 376 | 832 | - |
| Equity attributable to the owners of the parent | 4,685 | - | - | - | - | 4,685 | - |
| Total liabilities and equity | 10,018 | 13,845 | 2,665 | 4,766 | 2,884 | 34,178 | 10,687 |
| Interest rate gap | (965) | 513 | (1,229) | (2,047) | 3,728 | - | 3,665 |

Notes to the financial statements (continued)

47. Risk management (continued)

Interest rate repricing, gap analysis and amounts subject to fixed interest rates (continued)

| Group | Non- interest bearing | Up to 1 month | 1-3 months | 3-12 months | Over 12 months | Total | Fixed interest rates |
|--|-----------------------------|------------------|----------------|----------------|-------------------|----------------|----------------------------|
| | HRK million | HRK million | HRK million | HRK million | HRK million | HRK million | HRK million |
| 2016 | | | | | | | |
| Assets | | | | | | | |
| Cash and current accounts with banks | 3,717 | 4 | - | - | - | 3,721 | - |
| Obligatory reserve with the Croatian National Bank | 1,675 | - | - | - | - | 1,675 | - |
| Financial assets at fair value through profit or loss | 380 | 2,000 | 53 | 82 | - | 2,515 | 1,614 |
| Placements with and loans to other banks | 144 | 586 | 545 | 57 | - | 1,332 | 1,189 |
| Financial assets available for sale | 693 | 688 | 901 | 2,806 | 129 | 5,217 | 4,147 |
| Loans from and advances to customers | 62 | 12,833 | 616 | 1,099 | 3,894 | 18,504 | 5,885 |
| Financial investments held to maturity | 4 | 50 | 21 | 51 | 167 | 293 | 289 |
| Property, plant and equipment | 1,496 | - | - | - | - | 1,496 | - |
| Intangible assets | 240 | - | - | - | - | 240 | - |
| Deferred tax asset | 86 | - | - | - | - | 86 | - |
| Other asset | 285 | - | - | - | - | 285 | - |
| Total assets | 8,782 | 16,161 | 2,136 | 4,095 | 4,190 | 35,364 | 13,124 |
| Liabilities and equity | | | | | | | |
| Financial liabilities at fair value through profit or loss | 97 | - | - | - | - | 97 | - |
| Deposits from banks | 249 | 192 | - | - | - | 441 | 192 |
| Deposits from companies and other similar entities | 245 | 8,748 | 210 | 617 | 71 | 9,891 | 1,355 |
| Deposits from individuals | 48 | 5,731 | 1,790 | 4,756 | 1,928 | 14,253 | 9,601 |
| Borrowings | 52 | 1,513 | 860 | 1,008 | 559 | 3,992 | 1,308 |
| Provisions for liabilities and charges | 187 | - | - | - | - | 187 | - |
| Other liabilities | 776 | - | - | - | - | 776 | - |
| Subordinated liability | 6 | - | 453 | - | 378 | 837 | 378 |
| Equity attributable to the owners of the parent | 4,890 | - | - | - | - | 4,890 | - |
| Total liabilities and equity | 6,550 | 16,184 | 3,313 | 6,381 | 2,936 | 35,364 | 12,834 |
| Interest rate gap | 2,232 | (23) | (1,177) | (2,286) | 1,254 | - | 290 |

Notes to the financial statements (continued)

47. Risk management (continued)

Interest rate repricing, gap analysis and amounts subject to fixed interest rates (continued)

| Bank | Non- interest bearing | Up to 1 month | 1-3 months | 3-12 months | Over 12 months | Total | Fixed interest rates |
|--|-----------------------------|------------------|----------------|----------------|-------------------|----------------|----------------------------|
| 2017 | HRK million | HRK million | HRK million | HRK million | HRK million | HRK million | HRK million |
| Assets | | | | | | | |
| Cash and current accounts with banks | 4,707 | - | - | - | - | 4,707 | - |
| Obligatory reserve with the Croatian National Bank | 1,739 | - | - | - | - | 1,739 | - |
| Financial assets at fair value through profit or loss | 43 | 530 | - | - | - | 573 | 530 |
| Placements with and loans to other banks | 14 | 855 | - | - | 36 | 905 | 891 |
| Financial assets available for sale | 571 | - | 583 | 1,891 | 2,572 | 5,617 | 4,648 |
| Loans from and advances to customers | 52 | 12,696 | 344 | 490 | 2,871 | 16,453 | 6,367 |
| Investments in subsidiaries | 395 | - | - | - | - | 395 | - |
| Property, plant and equipment | 492 | - | - | - | - | 492 | - |
| Intangible assets | 204 | - | - | - | - | 204 | - |
| Deferred tax asset | 84 | - | - | - | - | 84 | - |
| Other and Current tax asset | 210 | - | - | - | - | 210 | - |
| Total assets | 8,511 | 14,081 | 927 | 2,381 | 5,479 | 31,379 | 12,436 |
| Liabilities and equity | | | | | | | |
| Financial liabilities at fair value through profit or loss | 61 | - | - | - | - | 61 | - |
| Deposits from banks | 313 | 780 | - | - | - | 1,093 | 748 |
| Deposits from companies and other similar entities | 3,649 | 5,752 | 123 | 216 | 77 | 9,817 | 601 |
| Deposits from individuals | 84 | 6,878 | 1,482 | 4,001 | 758 | 13,203 | 7,175 |
| Borrowings | 20 | 187 | 174 | 314 | 542 | 1,237 | 876 |
| Provisions for liabilities and charges | 162 | - | - | - | - | 162 | - |
| Income tax | 79 | - | - | - | - | 79 | - |
| Other liabilities | 437 | - | - | - | - | 437 | - |
| Subordinated liabilities | 5 | - | 451 | - | 376 | 832 | 376 |
| Equity | 4,458 | - | - | - | - | 4,458 | - |
| Total liabilities and equity | 9,268 | 13,597 | 2,230 | 4,531 | 1,753 | 31,379 | 9,776 |
| Interest rate gap | (757) | 484 | (1,303) | (2,150) | 3,726 | - | 2,660 |

Notes to the financial statements (continued)

47. Risk management (continued)

Interest rate repricing, gap analysis and amounts subject to fixed interest rates (continued)

| Bank | Non- interest bearing | Up to 1 month | 1-3 months | 3-12 months | Over 12 months | Total | Fixed interest rates |
|--|-----------------------------|------------------|----------------|----------------|-------------------|----------------|----------------------------|
| | HRK million | HRK million | HRK million | HRK million | HRK million | HRK million | HRK million |
| 2016 | | | | | | | |
| Assets | | | | | | | |
| Cash and current accounts with banks | 3,717 | - | - | - | - | 3,717 | - |
| Obligatory reserve with the Croatian National Bank | 1,675 | - | - | - | - | 1,675 | - |
| Financial assets at fair value through profit or loss | 387 | 1,764 | - | - | - | 2,151 | 1,600 |
| Placements with and loans to other banks | 145 | 586 | 545 | 72 | 36 | 1,384 | 1,239 |
| Financial assets available for sale | 692 | 660 | 859 | 2,710 | - | 4,921 | 3,931 |
| Loans from and advances to customers | 62 | 11,305 | 319 | 1,037 | 3,490 | 16,213 | 5,094 |
| Investments in subsidiaries | 408 | - | - | - | - | 408 | - |
| Property, plant and equipment | 478 | - | - | - | - | 478 | - |
| Intangible assets | 206 | - | - | - | - | 206 | - |
| Deferred tax asset | 83 | - | - | - | - | 83 | - |
| Other and current asset | 180 | - | - | - | - | 180 | - |
| Total assets | 8,033 | 14,315 | 1,723 | 3,819 | 3,526 | 31,416 | 11,864 |
| Liabilities and equity | | | | | | | |
| Financial liabilities at fair value through profit or loss | 97 | - | - | - | - | 97 | - |
| Deposits from banks | 258 | 192 | 30 | 40 | - | 520 | 262 |
| Deposits from companies and other similar entities | 184 | 8,947 | 210 | 668 | 81 | 10,090 | 1,416 |
| Deposits from individuals | 48 | 5,711 | 1,749 | 4,558 | 1,129 | 13,195 | 8,542 |
| Borrowings | 51 | 110 | 230 | 809 | 559 | 1,759 | 1,308 |
| Provisions for liabilities and charges | 176 | - | - | - | - | 176 | - |
| Other liabilities | 292 | - | - | - | - | 292 | - |
| Subordinated liabilities | 6 | - | 453 | - | 378 | 837 | 378 |
| Equity | 4,450 | - | - | - | - | 4,450 | - |
| Total liabilities and equity | 5,562 | 14,960 | 2,672 | 6,075 | 2,147 | 31,416 | 11,906 |
| Interest rate gap | 2,471 | (645) | (949) | (2,256) | 1,379 | - | (42) |

Notes to the financial statements (continued)**47. Risk management (continued)*****Average effective interest rates***

The average effective interest rates set out below represent the weighted average yield on financial instruments at the end of the reporting period, and are not necessarily representative of the yield at other times during the year.

The major part of liabilities and interest earning assets are denominated in or linked to foreign currency.

| | Group 2017 % | Group 2016 % | Bank 2017 % | Bank 2016 % |
|--|-----------------------------|-----------------------------|----------------------------|----------------------------|
| Assets | | | | |
| Financial assets at fair value through profit and loss | 3.15 | 3.67 | 2.64 | 3.49 |
| Placements with and loans to banks | (0.11) | (0.07) | (0.19) | 0.10 |
| Available-for-sale financial assets | 2.86 | 3.22 | 2.68 | 2.70 |
| Loans to customers | 5.09 | 5.92 | 5.11 | 6.14 |
| Held to maturity financial investments | 5.79 | 5.72 | - | - |
| Liabilities | | | | |
| Deposits from banks | 0.68 | 0.28 | 0.68 | 0.37 |
| Deposits from companies and other similar entities | 0.07 | 0.26 | 0.07 | 0.27 |
| Deposits from individuals | 0.48 | 0.76 | 0.30 | 0.59 |
| Borrowings | 1.36 | 1.23 | 1.30 | 1.26 |
| Subordinated liabilities | 6.47 | 6.48 | 6.47 | 6.48 |

Notes to the financial statements (continued)

47. Risk management (continued)

Interest rate risk (continued)

Interest rate risk in trading book

The following two tables show the largest present value changes in the trading book (BPV in currencies for which this change is material) for 2017 and 2016:

| BPV / Currency in HRK | EUR | USD | HRK |
|-----------------------|-------------|-------------|--------------|
| 31 December 2017 | (52,662.53) | (27,030.54) | (3,217.62) |
| Average | 100,798.91 | (16,359.93) | (96,391.45) |
| Minimum | (52,662.53) | (57,995.61) | (158,081.87) |
| Maximum | 201,188.07 | (5,049.43) | (3,217.62) |

| BPV / Currency in HRK | EUR | USD | HRK |
|-----------------------|--------------|-------------|--------------|
| 31 December 2016 | 67,153.96 | (56,703.81) | (93,402.91) |
| Average | 23,348.27 | (39,838.61) | (152,238.77) |
| Minimum | (134,971.49) | (66,766.25) | (212,469.80) |
| Maximum | 143,019.03 | (17,720.74) | (90,463.69) |

Total BPV for trading book at 31 December 2017 was HRK 88.9 thousands as compared to 30 December 2016 when it was HRK 222.2 thousands.

Interest rate risk in non-trading book

Asset-liability risk management activities are conducted in the context of the Group's sensitivity to interest rate changes. Decisions are based on various interest income analyses and simulations that ensure proper interest rate sensitivity in line with expected changes in market rates and overall risk appetite.

The following two tables show the largest present value changes for the non-trading book (BPV in currencies for which this change is material) for 2017 and 2016:

| BPV / Currency in HRK | HRK | EUR | USD |
|-----------------------|--------------|----------------|-------------|
| 31 December 2017 | (59,567.68) | (97,318.23) | 65,968.65 |
| Average | (242,810.66) | (1,047,555.54) | 26,040.91 |
| Minimum | (372,670.36) | (1,594,795.86) | (41,954.74) |
| Maximum | (59,567.68) | (44,333.21) | 67,191.53 |

| BPV / Currency in HRK | HRK | EUR | USD |
|-----------------------|--------------|----------------|-------------|
| 31 December 2016 | (147,047.54) | (1,574,210.70) | (40,893.67) |
| Average | (183,067.74) | (1,357,173.73) | (22,877.42) |
| Minimum | (386,451.57) | (1,831,099.88) | (68,375.30) |
| Maximum | 40,704.73 | (198,149.30) | 6,639.52 |

Total BPV for non-trading book at 29 December 2017 was HRK 236.7 thousand, as compared to 30 December 2016 when it was HRK 1.77 million.

Notes to the financial statements (continued)

47. Risk management (continued)

Interest rate risk (continued)

Interest rate risk in the banking book is not only measured in a value-at-risk framework but also managed by the traditional tools of nominal and interest rate gap analyses. For the purpose of managing and monitoring of interest rate risk exposures via analyses of the effect on the economic value of equity, the Bank applies an externally defined Basel II methodology, which implies measuring the effects of a (parallel) shift in the reference yield curve for one of the following scenarios (one that has the most disadvantageous effect on the bank):

- 200 bp shift
- shift by the 1st and 99th percentile of observed one-day interest rate changes on the bank's economic value of equity.

| HRK | 31 December 2017 | 31 December 2016 |
|--------------|------------------|------------------|
| EUR | 108,320 | 159,616 |
| HRK | 79,568 | 16,022 |
| Other | (20,289) | (8,220) |
| Total | 167,599 | 167,418 |
| % | 3.83% | 3.77% |

The Group measures interest rate risk exposure and impact on net interest income in accordance with the Decision on Management of Interest Rate Risk in the Banking Book and with EBA Guidelines on the management of interest rate risk. The report has been in effect since 30.6.2017.

| | |
|---------------------|------------------|
| in HRK | 31 December 2017 |
| Net interest income | 112,273 |

Equity price risk

Equity price risk is the possibility that equity prices will fluctuate, affecting the fair value of equity investments and other instruments that derive their value from a particular equity investment. The primary exposure to equity prices arises from equity securities measured at fair value through profit and loss.

Equity Delta is the indicator of the Bank's exposure to equity price risk arising from positions in equity securities and equity derivatives held for trading. The Bank has established equity delta limits per position in a single instrument and a total equity delta limit as well as VaR limit for equity positions in trading book portfolio.

For the monitoring of its equity portfolio the Bank analyses the equity portfolio's sensitivity through Equity delta limits and VaR limits.

Exchange rate risks

The Group is exposed to currency risk/exchange rate risk which denotes the risk that one suffers losses due to open foreign exchange position.

Foreign currency exposure arises from foreign-currency denominated credit, deposit-taking, investment and trading activities. It is monitored daily in accordance to legislation and internally set limits, for each currency and for the total statement of financial position denominated in or linked to foreign currency.

The Group manages its currency risk by setting principles and limits for foreign currency exposures and by monitoring these limits (including stop-loss limits). The Group directs its business activities towards trying to minimize the gap between assets and liabilities denominated in or linked to foreign currency, and maintaining daily business activities within daily allowed open limits per currency.

The Group is primarily exposed to EUR. In order to protect itself against currency risk, Group uses derivative financial instruments.

Notes to the financial statements (continued)

47. Risk management (continued)

Currency analysis

| Group | EU HRK million | EUR linked HRK million | CHF HRK million | CHF linked HRK million | Other foreign currencies HRK million | Total foreign currencies HRK million | Domestic currency HRK million | Total currencies HRK million |
|--|----------------------|---------------------------------|-----------------------|------------------------------|--|---|--|---------------------------------------|
| 2017 | | | | | | | | |
| Assets | | | | | | | | |
| Cash and current accounts with banks | 121 | - | 31 | - | 87 | 239 | 4,469 | 4,708 |
| Obligatory reserve with the Croatian National Bank | - | - | - | - | - | - | 1,739 | 1,739 |
| Financial assets at fair value through profit or loss | 186 | 388 | - | - | 2 | 576 | 375 | 951 |
| Placements with and loans to other banks | 867 | - | - | - | 2 | 869 | 25 | 894 |
| Financial assets available for sale | 3,039 | 778 | - | - | 830 | 4,647 | 1,290 | 5,937 |
| Loans from and advances to customers | 2,206 | 8,211 | - | 18 | 48 | 10,483 | 7,262 | 17,745 |
| Financial investments held to maturity | 11 | 237 | - | - | - | 248 | 31 | 279 |
| Property, plant and equipment | - | - | - | - | - | - | 1,309 | 1,309 |
| Intangible assets | - | - | - | - | - | - | 239 | 239 |
| Deferred tax asset | - | - | - | - | - | - | 86 | 86 |
| Other asset | 21 | 19 | - | - | 1 | 41 | 250 | 291 |
| Total assets | 6,451 | 9,633 | 31 | 18 | 970 | 17,103 | 17,075 | 34,178 |
| Liabilities and equity | | | | | | | | |
| Financial liabilities at fair value through profit or loss | 15 | - | 1 | - | 6 | 22 | 37 | 59 |
| Deposits from banks | 282 | - | 23 | - | 501 | 806 | 250 | 1,056 |
| Deposits from companies and other similar entities | 2,737 | 46 | 15 | - | 499 | 3,297 | 6,252 | 9,549 |
| Deposits from individuals | 8,280 | 901 | 280 | - | 1,522 | 10,983 | 3,248 | 14,231 |
| Borrowings | 1,541 | 333 | - | - | - | 1,874 | 698 | 2,572 |
| Provisions for liabilities and charges | 10 | - | - | - | - | 10 | 163 | 173 |
| Income tax | - | - | - | - | - | - | 70 | 70 |
| Other liabilities | 29 | 350 | - | - | 1 | 380 | 571 | 951 |
| Subordinated liability | 832 | - | - | - | - | 832 | - | 832 |
| Equity attributable to the owners of the parent | - | - | - | - | - | - | 4,685 | 4,685 |
| Total liabilities and equity | 13,726 | 1,630 | 319 | - | 2,529 | 18,204 | 15,974 | 34,178 |
| Currency gap | (7,275) | 8,003 | (288) | 18 | (1,559) | (1,101) | 1,101 | - |

Notes to the financial statements (continued)

47. Risk management (continued)

Currency analysis (continued)

| Group | EU HRK million | EUR linked HRK million | CHF HRK million | CHF linked HRK million | Other foreign currencies HRK million | Total foreign currencies HRK million | Domestic currency HRK million | Total currencies HRK million |
|--|----------------------|---------------------------------|-----------------------|------------------------------|--|---|--|---------------------------------------|
| 2016 | | | | | | | | |
| Assets | | | | | | | | |
| Cash and current accounts with banks | 92 | - | 13 | - | 89 | 194 | 3,527 | 3,721 |
| Obligatory reserve with the Croatian National Bank | - | - | - | - | - | - | 1,675 | 1,675 |
| Financial assets at fair value through profit or loss | 1,182 | 459 | - | - | 197 | 1,838 | 677 | 2,515 |
| Placements with and loans to other banks | 972 | - | - | - | 201 | 1,173 | 159 | 1,332 |
| Financial assets available for sale | 2,770 | 883 | - | - | 925 | 4,578 | 639 | 5,217 |
| Loans from and advances to customers | 1,896 | 9,165 | 37 | 27 | 124 | 11,249 | 7,255 | 18,504 |
| Financial investments held to maturity | 7 | 238 | - | - | - | 245 | 48 | 293 |
| Property, plant and equipment | - | - | - | - | - | - | 1,496 | 1,496 |
| Intangible assets | - | - | - | - | - | - | 240 | 240 |
| Deferred tax asset | - | - | - | - | - | - | 86 | 86 |
| Other asset | 14 | 28 | - | - | 1 | 43 | 242 | 285 |
| Total assets | 6,933 | 10,773 | 50 | 27 | 1,537 | 19,320 | 16,044 | 35,364 |
| Liabilities and equity | | | | | | | | |
| Financial liabilities at fair value through profit or loss | 62 | - | 5 | - | 17 | 84 | 13 | 97 |
| Deposits from banks | 121 | - | 23 | - | 130 | 274 | 167 | 441 |
| Deposits from companies and other similar entities | 2,400 | 61 | 14 | - | 607 | 3,082 | 6,809 | 9,891 |
| Deposits from individuals | 8,507 | 957 | 298 | - | 1,647 | 11,409 | 2,844 | 14,253 |
| Borrowings | 2,484 | 424 | - | - | 7 | 2,915 | 1,077 | 3,992 |
| Provisions for liabilities and charges | 15 | 1 | - | - | - | 16 | 171 | 187 |
| Other liabilities | 14 | 370 | - | - | 1 | 385 | 391 | 776 |
| Subordinated liability | 837 | - | - | - | - | 837 | - | 837 |
| Equity attributable to the owners of the parent | - | - | - | - | - | - | 4,890 | 4,890 |
| Total liabilities and equity | 14,440 | 1,813 | 340 | - | 2,409 | 19,002 | 16,362 | 35,364 |
| Currency gap | (7,507) | 8,960 | (290) | 27 | (872) | 318 | (318) | - |

Notes to the financial statements (continued)

47. Risk management (continued)

Currency analysis (continued)

| Bank | EUR HRK million | EUR linked HRK million | CHF HRK million | CHF linked HRK million | Other foreign currencies HRK million | Total foreign currencies HRK million | Domestic currency HRK million | Total currencies HRK million |
|--|-----------------------|---------------------------------|-----------------------|---------------------------------|--|--|--|---------------------------------------|
| 2017 | | | | | | | | |
| Assets | | | | | | | | |
| Cash and current accounts with banks | 121 | - | 31 | - | 87 | 239 | 4,468 | 4,707 |
| Obligatory reserve with the Croatian National Bank | - | - | - | - | - | - | 1,739 | 1,739 |
| Financial assets at fair value through profit or loss | 128 | 191 | - | - | 2 | 321 | 252 | 573 |
| Placements with and loans to other banks | 867 | - | - | - | 2 | 869 | 36 | 905 |
| Financial assets available for sale | 3,039 | 661 | - | - | 830 | 4,530 | 1,087 | 5,617 |
| Loans from and advances to customers | 2,206 | 7,195 | - | 18 | 48 | 9,467 | 6,986 | 16,453 |
| Investments in subsidiaries | - | - | - | - | - | - | 395 | 395 |
| Property, plant and equipment | - | - | - | - | - | - | 492 | 492 |
| Intangible assets | - | - | - | - | - | - | 204 | 204 |
| Deferred tax asset | - | - | - | - | - | - | 84 | 84 |
| Other and Current tax asset | 21 | - | - | - | 1 | 22 | 188 | 210 |
| Total assets | 6,382 | 8,047 | 31 | 18 | 970 | 15,448 | 15,931 | 31,379 |
| Liabilities and equity | | | | | | | | |
| Financial liabilities at fair value through profit or loss | 17 | - | 1 | - | 6 | 24 | 37 | 61 |
| Deposits from banks | 291 | - | 23 | - | 501 | 815 | 278 | 1,093 |
| Deposits from companies and other similar entities | 2,780 | - | 15 | - | 499 | 3,294 | 6,523 | 9,817 |
| Deposits from individuals | 8,281 | 4 | 280 | - | 1,522 | 10,087 | 3,116 | 13,203 |
| Borrowings | 326 | 333 | - | - | - | 659 | 578 | 1,237 |
| Provisions for liabilities and charges | 10 | - | - | - | - | 10 | 152 | 162 |
| Income tax | - | - | - | - | - | - | 79 | 79 |
| Other liabilities | 29 | 11 | - | - | 1 | 41 | 396 | 437 |
| Subordinated liability | 832 | - | - | - | - | 832 | - | 832 |
| Equity | - | - | - | - | - | - | 4,458 | 4,458 |
| Total liabilities and equity | 12,566 | 348 | 319 | - | 2,529 | 15,762 | 15,617 | 31,379 |
| Currency gap | (6,184) | 7,699 | (288) | 18 | (1,559) | (314) | 314 | - |

Notes to the financial statements (continued)

47. Risk management (continued)

Currency analysis (continued)

| Bank | EUR HRK million | EUR linked HRK million | CHF HRK million | CHF linked HRK million | Other foreign currencies HRK million | Total foreign currencies HRK million | Domestic currency HRK million | Total currencies HRK million |
|--|-----------------------|---------------------------------|-----------------------|---------------------------------|--|--|--|---------------------------------------|
| 2016 | | | | | | | | |
| Assets | | | | | | | | |
| Cash and current accounts with banks | 92 | - | 13 | - | 89 | 194 | 3,523 | 3,717 |
| Obligatory reserve with the Croatian National Bank | - | - | - | - | - | - | 1,675 | 1,675 |
| Financial assets at fair value through profit or loss | 1,147 | 247 | - | - | 197 | 1,591 | 560 | 2,151 |
| Placements with and loans to other banks | 987 | - | - | - | 201 | 1,188 | 196 | 1,384 |
| Financial assets available for sale | 2,770 | 647 | - | - | 925 | 4,342 | 579 | 4,921 |
| Loans from and advances to customers | 1,896 | 7,220 | 37 | 27 | 124 | 9,304 | 6,909 | 16,213 |
| Investments in subsidiaries | - | - | - | - | - | - | 408 | 408 |
| Property, plant and equipment | - | - | - | - | - | - | 478 | 478 |
| Intangible assets | - | - | - | - | - | - | 206 | 206 |
| Deferred tax asset | - | - | - | - | - | - | 83 | 83 |
| Other and Current tax asset | 14 | - | - | - | 1 | 15 | 165 | 180 |
| Total assets | 6,906 | 8,114 | 50 | 27 | 1,537 | 16,634 | 14,782 | 31,416 |
| Liabilities and equity | | | | | | | | |
| Financial liabilities at fair value through profit or loss | 63 | - | 5 | - | 17 | 85 | 12 | 97 |
| Deposits from banks | 121 | - | 23 | - | 130 | 274 | 246 | 520 |
| Deposits from companies and other similar entities | 2,474 | - | 14 | - | 607 | 3,095 | 6,995 | 10,090 |
| Deposits from individuals | 8,508 | 4 | 298 | - | 1,647 | 10,457 | 2,738 | 13,195 |
| Borrowings | 331 | 424 | - | - | 7 | 762 | 997 | 1,759 |
| Provisions for liabilities and charges | 15 | 1 | - | - | - | 16 | 160 | 176 |
| Other liabilities | 14 | 11 | - | - | 1 | 26 | 266 | 292 |
| Subordinated liability | 837 | - | - | - | - | 837 | - | 837 |
| Equity | - | - | - | - | - | - | 4,450 | 4,450 |
| Total liabilities and equity | 12,363 | 440 | 340 | - | 2,409 | 15,552 | 15,864 | 31,416 |
| Currency gap | (5,457) | 7,674 | (290) | 27 | (872) | 1,082 | (1,082) | - |

Notes to the financial statements (continued)

47. Risk management (continued)

Operational risk

Operational risk is defined as the risk of financial losses resulting from inadequate or failed internal processes, people and systems or from external events. Operational risk includes legal risk, but excludes strategic and reputational risk.

With the aim of efficient operational risk management, the RBI Group built system based on standards and principles defined in EU directives and Regulations, Credit Institutions Act and CNB Decisions, Basel Committee documents and RBI Group Directives.

The Group's Operational Risk Management Framework consists of processes, structures, controls for the governance, identification, measurement, management, monitoring, capital computation and attribution, risk control and mitigation of loss resulting from inadequate or failed internal processes, people and systems or from external events.

The Operational Risk Management Framework is structured to increase transparency of operational risks across the Group, strengthen management of operational risk exposures and ensure full compliance with regulatory requirements.

Roles and Responsibilities

RBI Group fosters an open environment and culture, while all employees of the Group, through their individual roles and responsibilities, contribute to maintaining an effective Operational Risk Management Framework. Whilst ultimate responsibility for risk resides with the Management Board member responsible for Risk management, system of responsibilities for managing operational risk is based on three lines of defense which contribute in maintaining an effective Operational Risk Management framework.

The first line of defense is the risk originating units whose business activities give rise to risk. The risk originating units own operational risk.

The second line of defense provides an independent assessment of operational risk, oversight and challenges the first line of defense. The second line of defense is comprised of:

- RBI Group Chief Risk Officer & RBA Chief Risk Officer – representing the applicable Management Board provides strategic direction, leadership and ensure that operational risks are appropriately managed.
- The Operational Risk Management Committees on RBI Group and RBA level are a decision making body which oversees the entire Operational Risk Management Framework
- RBI Group Operational Risk Controlling develops and maintains the Group Operational Risk Management Framework and together with RBA Operational Risk Control ensures that operational risks are proactively identified, measured, managed and monitored.
- RBA Operational Risk Control provides leadership and subject matter expertise for operational risk management on RBA level. RBA Operational Risk Control is responsible for ensuring that minimum standards are adhered to and operational risks are proactively identified, measured, managed and monitored.

The third line of defense is Internal Audit, it reviews effectiveness and suitability of the general risk management processes.

Risk identification, measurement, mitigation and monitoring

Operational Risk is managed within the Risk Management cycle, which encompasses the identification, measurement, management and monitoring of risk.

Identification of operational risks includes analysing the below attributes to understand material operational risk types to which the business may be exposed. Operational risks in the Group are identified on a proactive and regular basis within: products, processes, systems and external factors.

Operational Risk measurement can be both quantitative and qualitative in nature and include the following instruments:

- *Risk assessments* serve to increase operational risk awareness, identify operational risks and mitigate identified operational risks. The risk assessment determines the net risk of a process, risk originating unit or activity that is relevant as a target value for measures of qualitative risk management. The results of Risk Assessments are the basis for the Operational Risk Profile.

Notes to the financial statements (continued)

47. Risk management (continued)

Operational risk (continued)

- *Early Warning Indicators* are used for the on-going monitoring and reporting of operational risk exposures. They provide an early warning signal for potential issues or changes in Operational Risk Profile that may warrant management action.
- *Event Data Collection* and analysis of internal operational risk events provides meaningful information for measuring the impact of operational risk events and the effectiveness of the internal control environment.
- *Scenario Analysis* is a process by which the Group considers the impact of extreme, but plausible events on its operations and assigns likelihood and severity estimations to the range of possible outcomes. Scenario analysis aims to provide a prospective method for capturing 'tail events' that may not have occurred in the Bank's own loss history, and raise awareness and educate management by providing perspective on different types of risk, and drive risk mitigation action and investment plans.

Monitoring is focused on regularly reviewing the Operational Risk Management cycle and the Operational Risk Management instruments and methods to ensure their relevance and validity in assessing Operational Risk and ensuring that mitigation measures, which are implemented are functioning effectively, reviewed regularly and that necessary adjustments occur.

Reporting supports the Operational Risk Management cycle by ensuring constant and timely information flow to the relevant decision making bodies. In this way, operational risk reporting supports risk transparency and the integration of Operational Risk Management activities into day-to-day business operations.

Risk mitigation represents managing the risk exposure, by taking the one of the following actions: risk avoidance (removing the risk source), risk reduction (changing the likelihood or consequences by applying controls or other mitigation activities), risk transfer (sharing the risk with another party or parties) and risk acceptance (accepting the risk by informed decision). The Group defined triggers within risk identification tools which result in mandatory mitigation actions, however the development of mitigation actions is conducted as part of everyday business activities whenever they are identified.

All members of the Group currently calculate regulatory capital requirement for operational risk using the Standardized Approach.

Notes to the financial statements (continued)

48. Fair value of financial instruments

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal (or most advantageous) market at the measurement date under current market condition (i.e. an exit price) regardless of whether that price is directly observable or estimated using another valuation technique.

Financial instruments at fair value through profit or loss and available for sale instruments are measured at fair value. Loans and receivables and held-to-maturity assets are measured at amortised cost less impairment.

The carrying amounts of cash and current accounts with banks, placements with banks, deposits from banks and deposits from companies and similar entities, reflect their fair value due to the short-term maturity.

The following summarises the major methods and assumptions used in estimating the fair values of financial instruments.

Loans and advances

The fair value of loans and advances is calculated based on discounted expected future principal and interest cash flows. Expected future cash flows are estimated considering credit risk and any indication of impairment including portfolio based impairment allowances for performing loans calculated at rates prescribed by the CNB. Expected future cash flows for homogeneous categories of loans, such as residential mortgage loans, are estimated on a portfolio basis and discounted at current rates offered for similar loans to new borrowers with similar credit profiles. The estimated fair values of loans reflect changes in credit status since the loans were made and changes in interest rates in the case of fixed rate loans. As the Group has a very limited portfolio of loans and advances with fixed rates and longer-term maturity, the fair value of loans and advances is not significantly different from their carrying value based on the estimate of the Management. Differences between the fair value of future losses from currently performing loans in the portfolio and the effect of the portfolio based provisions recognised in accordance with CNB rules, are not taken into account.

Bank and customer deposits

For demand deposits and deposits with no defined maturities, fair value is taken to be the amount payable on demand at date of reporting. The estimated fair value of fixed-maturity deposits is based on discounted cash flows using rates currently offered for deposits of similar remaining maturities. The value of long-term relationships with depositors is not taken into account in estimating fair values.

Borrowings

Most of the Group's long-term debt has no quoted market price and fair value is estimated as the present value of future cash flows, discounted at interest rates available at date of reporting to the Group for new debt of similar type and remaining maturity.

Notes to the financial statements (continued)

48. Fair value of financial instruments (continued)

The table below provides an analysis of financial instruments which are stated at their fair value after initial recognition and classified in three categories according to availability of observable indicators of fair value (data presented in the table do not include interest, unlike the presentation in the related notes):

- Level 1 available observable inputs: The fair value of financial instruments is based on their (unadjusted) quoted market prices available in an active market for equivalent assets and equivalent liabilities;
- Level 2 available observable inputs: The fair value is determined based on information other than level 1 quoted prices by directly observing assets and liabilities and by reference to their prices, or the fair value is derived indirectly from the prices .; and
- Level 3 inputs: The fair value data are derived by applying valuation techniques which are using information on assets and liabilities which are not based on market-observable information (unobservable inputs).

| Group 2017 HRK millions | Carrying amount | Fair value | | | Total fair value |
|---|-----------------|--------------|------------|---------------|---------------------|
| | | Level 1 | Level 2 | Level 3 | |
| Cash and current accounts with banks | 4,708 | - | - | 4,708 | 4,708 |
| Obligatory reserve with the Croatian National Bank | 1,739 | - | - | 1,739 | 1,739 |
| Financial assets at fair value through profit or loss | | | | | |
| Held for trading instruments | | | | | |
| Debt securities | 492 | 372 | 120 | - | 492 |
| Equity instruments | 1 | 1 | - | - | 1 |
| Derivative financial assets | 29 | - | 29 | - | 29 |
| Fair value of contracted OTC spot transactions | 4 | - | 4 | - | 4 |
| Financial assets initially designated at fair value through profit and loss | | | | | |
| Debt securities | 409 | 86 | 323 | - | 409 |
| Equity instruments | 2 | 2 | - | - | 2 |
| Investment fund units | 14 | 14 | - | - | 14 |
| Placements with and loans to banks | 894 | - | - | 894 | 894 |
| Available-for-sale financial assets | | | | | |
| Debt securities | 5,906 | 5,787 | 119 | - | 5,906 |
| Equity instruments | 31 | 7 | 22 | 2 | 31 |
| Loans to customers | 17,745 | - | - | 18,083 | 18,083 |
| Held to maturity financial investments | 281 | 314 | - | - | 314 |
| Total | 32,251 | 6,583 | 613 | 25,426 | 32,626 |
| Financial liabilities at fair value through profit and loss | | | | | |
| Derivative financial liabilities | 48 | - | 48 | - | 48 |
| Fair value of contracted OTC spot transactions | 11 | - | 11 | - | 11 |
| Deposits from banks | 1,056 | - | - | 1,056 | 1,056 |
| Deposits from companies and similar entities | 9,549 | - | - | 9,548 | 9,548 |
| Deposits from private individuals | 14,231 | - | - | 14,188 | 14,188 |
| Borrowings | 2,572 | - | - | 2,564 | 2,564 |
| Subordinated liabilities | 832 | - | - | 815 | 815 |
| Total | 28,299 | - | 59 | 28,171 | 28,230 |

Notes to the financial statements (continued)

48. Fair value of financial instruments (continued)

| Group 2016 HRK million | Carrying amount | Fair value | | | Total fair value |
|--|-----------------|--------------|------------|---------------|---------------------|
| | | Level 1 | Level 2 | Level 3 | |
| Cash and current accounts with banks | 3,721 | - | - | 3,721 | 3,721 |
| Obligatory reserve with the Croatian National Bank | 1,675 | - | - | 1,675 | 1,675 |
| Financial assets at fair value through profit or loss | | | | | |
| Held for trading instruments | | | | | |
| Debt securities | 1,902 | 1,862 | 40 | - | 1,902 |
| Equity instruments | 5 | 5 | - | - | 5 |
| Derivative financial assets | 109 | - | 109 | - | 109 |
| Fair value of contracted OTC spot transactions | 1 | - | 1 | - | 1 |
| Financial assets initially designated at fair value through profit and loss | | | | | |
| Debt securities | 487 | 369 | 115 | 3 | 487 |
| Equity instruments | 2 | 2 | - | - | 2 |
| Investment fund units | 9 | 9 | - | - | 9 |
| Placements with and loans to banks | 1,332 | - | - | 1,332 | 1,332 |
| Available-for-sale financial assets | | | | | |
| Debt securities | 5,188 | 5,188 | - | - | 5,188 |
| Equity instruments | 29 | 8 | 17 | 4 | 29 |
| Loans to customers | 18,504 | - | - | 18,644 | 18,644 |
| Held to maturity financial investments | 293 | 257 | - | - | 257 |
| Total | 33,257 | 7,700 | 282 | 25,379 | 33,361 |
| Financial liabilities at fair value through profit and loss | | | | | |
| Derivative financial liabilities | 96 | - | 96 | - | 96 |
| Fair value of contracted OTC spot transactions | 1 | - | 1 | - | 1 |
| Deposits from banks | 441 | - | - | 441 | 441 |
| Deposits from companies and similar entities | 9,891 | - | - | 9,879 | 9,879 |
| Deposits from private individuals | 14,253 | - | - | 14,233 | 14,233 |
| Borrowings | 3,992 | - | - | 3,983 | 3,983 |
| Subordinated liabilities | 837 | - | - | 820 | 820 |
| Total | 29,511 | - | 97 | 29,356 | 29,453 |

Notes to the financial statements (continued)

48. Fair value of financial instruments (continued)

| Bank 2017 HRK millions | Carrying amount | Fair value | | | Total fair value |
|--|-----------------|--------------|------------|---------------|---------------------|
| | | Level 1 | Level 2 | Level 3 | |
| Cash and current accounts with banks | 4,707 | - | - | 4,707 | 4,707 |
| Obligatory reserve with the Croatian National Bank | 1,739 | - | - | 1,739 | 1,739 |
| Financial assets at fair value through profit or loss | | | | | |
| Held for trading instruments | | | | | |
| Debt securities | 492 | 372 | 120 | - | 492 |
| Equity instruments | 1 | 1 | - | - | 1 |
| Derivative financial assets | 35 | - | 35 | - | 35 |
| Fair value of contracted OTC spot transactions | 4 | - | 4 | - | 4 |
| Financial assets initially designated at fair value through profit and loss | | | | | |
| Debt securities | 41 | 14 | 27 | - | 41 |
| Placements with and loans to banks | 905 | - | - | 909 | 909 |
| Available-for-sale financial assets | | | | | |
| Debt securities | 5,586 | 5,487 | 99 | - | 5,586 |
| Equity instruments | 31 | 7 | 22 | 2 | 31 |
| Loans to customers | 16,453 | - | - | 16,804 | 16,804 |
| Investments in subsidiaries | 395 | - | - | 395 | 395 |
| Total | 30,389 | 5,881 | 307 | 24,556 | 30,744 |
| Financial liabilities at fair value through profit and loss | | | | | |
| Derivative financial liabilities | 50 | - | 50 | - | 50 |
| Fair value of contracted OTC spot transactions | 11 | - | 11 | - | 11 |
| Deposits from banks | 1,093 | - | - | 1,093 | 1,093 |
| Deposits from companies and similar entities | 9,817 | - | - | 9,816 | 9,816 |
| Deposits from private individuals | 13,203 | - | - | 13,191 | 13,191 |
| Borrowings | 1,237 | - | - | 1,229 | 1,229 |
| Subordinated liabilities | 832 | - | - | 815 | 815 |
| Total | 26,243 | - | 61 | 26,144 | 26,205 |

Notes to the financial statements (continued)

48. Fair value of financial instruments (continued)

| Bank 2016 HRK millions | Carrying amount | Fair value | | | Total fair value |
|--|-----------------|--------------|------------|---------------|---------------------|
| | | Level 1 | Level 2 | Level 3 | |
| Cash and current accounts with banks | 3,717 | - | - | 3,717 | 3,717 |
| Obligatory reserve with the Croatian National Bank | 1,675 | - | - | 1,675 | 1,675 |
| Financial assets at fair value through profit or loss | | | | | |
| Held for trading instruments | | | | | |
| Debt securities | 1,902 | 1,862 | 40 | - | 1,902 |
| Equity instruments | 5 | 5 | - | - | 5 |
| Derivative financial assets | 117 | - | 117 | - | 117 |
| Fair value of contracted OTC spot transactions | 1 | - | 1 | - | 1 |
| Financial assets initially designated at fair value through profit and loss | | | | | |
| Debt securities | 126 | 98 | 25 | 3 | 126 |
| Placements with and loans to banks | 1,384 | - | - | 1,385 | 1,385 |
| Available-for-sale financial assets | | | | | |
| Debt securities | 4,892 | 4,892 | - | - | 4,892 |
| Equity instruments | 29 | 8 | 17 | 4 | 29 |
| Loans to customers | 16,213 | - | - | 16,379 | 16,379 |
| Investments in subsidiaries | 408 | - | - | 408 | 408 |
| Total | 30,469 | 6,865 | 200 | 23,571 | 30,636 |
| Financial liabilities at fair value through profit and loss | | | | | |
| Derivative financial liabilities | 96 | - | 96 | - | 96 |
| Fair value of contracted OTC spot transactions | 1 | - | 1 | - | 1 |
| Deposits from banks | 520 | - | - | 520 | 520 |
| Deposits from companies and similar entities | 10,090 | - | - | 10,085 | 10,085 |
| Deposits from private individuals | 13,195 | - | - | 13,175 | 13,175 |
| Borrowings | 1,759 | - | - | 1,750 | 1,750 |
| Subordinated liabilities | 837 | - | - | 820 | 820 |
| Total | 26,498 | - | 97 | 26,350 | 26,447 |

Notes to the financial statements (continued)

48. Fair value of financial instruments (continued)

The following table shows adjustment between initial and final balance for measurement of fair value in level 3 inside hierarchy of fair values:

| Group/Bank | <i>Trading instruments</i> | <i>Financial assets designated at fair value through profit or loss</i> | <i>Financial assets available for sale</i> |
|---|--------------------------------|---|--|
| | Equity instruments | Debt securities issued by companies | Equity securities |
| At 1 January 2016 | 2 | 3 | 60 |
| Gains and losses in other comprehensive income | (2) | - | (53) |
| Reclassification to Level 1 | | | (3) |
| At 31 December 2016 | - | 3 | 4 |
| Gains and losses stated in profit and loss | - | (3) | - |
| Gains and losses in other comprehensive income | - | - | (2) |
| At 31 December 2017 | - | - | 2 |

Notes to the financial statements (continued)

49. Capital management

From 1 January 2014 credit institutions are obliged to calculate and report prudential requirements according to Capital Requirements Regulation (EU) No 575/2013 ("CRR"), Directive 2013/36/EU (CRD IV"), technical standards and other relevant regulations prescribed by European Banking Authority ("EBA") and local regulator CNB.

The Group's and the Bank's regulatory capital requirements are based on Basel III methodology.

Group, in accordance with the regulatory requirements of CNB and EBA regulations, comprises Raiffeisenbank Austria and its subsidiaries that form group of credit institutions. For the purpose of regulatory capital calculation the Group consist of: Raiffeisenbank Austria d.d, Raiffeisen stambena štedionica d.d., Raiffeisen Leasing d.o.o., Raiffeisen Consulting d.o.o., Raiffeisen Factoring d.o.o., (2016: Raiffeisen Invest d.o.o. and Raiffeisen Bonus d.o.o.).

Regulatory capital consist of Common Equity Tier 1 ("CET1") capital and Tier 2 ("T2") capital. CET1 include ordinary shares and related share premium, retained earnings, reserves, deductions for intangible assets, unrealised fair value losses on financial instruments designated at available for sale portfolio and value adjustment for prudent valuations and goodwill resulting from acquisition of a 100% interest in company Raiffeisen Leasing d.o.o.. T2 capital includes qualifying subordinated liabilities.

Prescribed minimal capital ratios (Article 92 CRR) are:

- Common Equity Tier 1 capital ratio of 4.5% of the total risk exposure amount
- Tier 1 capital ratio of 6% of the total risk exposure amount
- Total capital ratio of 8% of the total risk exposure amount.

In accordance to Article 129 and 133 of Directive 2013/36/EU and Article 117 and 130 of CNB Credit Institutions Act, the Group and the Bank are obliged to maintain capital buffers:

- Capital conservation buffer of 2.5% of the total risk exposure amount
- Systemic risk buffer in the amount of 3% of the total risk exposure amount.

Notes to the financial statements (continued)

49. Capital management (continued)

| HRK millions | Group 2017 | Group 2016 | Bank 2017 | Bank 2016 |
|--|---------------|---------------|---------------|---------------|
| Regulatory capital | | | | |
| <i>Tier 1 capital</i> | | | | |
| <i>Common Equity Tier 1 ("CET1") capital</i> | | | | |
| Issued share capital | 3,621 | 3,621 | 3,621 | 3,621 |
| Share premium | 12 | 12 | 12 | 12 |
| Retained earnings (excluding profit for the period) | 558 | 408 | 222 | 147 |
| Net profit for the period | (245) | - | - | - |
| Legal, statutory and other reserves | 173 | 173 | 173 | 173 |
| Non-controlling interests | - | - | - | - |
| Deductions, in accordance with the CNB regulations | | | | |
| Intangible assets | (215) | (220) | (209) | (214) |
| Value adjustment due to prudent valuations | (28) | (22) | (26) | (21) |
| Goodwill | (27) | (27) | - | - |
| Unrealised losses on financial assets available for sale | (11) | (13) | (11) | (11) |
| Deductions for investments in banks and financial institutions | (23) | (23) | (23) | (23) |
| Total Common Equity Tier 1 capital | 3,815 | 3,909 | 3,759 | 3,684 |
| Tier 2 capital | 614 | 753 | 614 | 753 |
| Total Own Funds | 4,429 | 4,662 | 4,373 | 4,437 |
| Total risk-weighted assets | 21,624 | 23,085 | 19,449 | 20,004 |
| Capital adequacy ratio | 20.48% | 20.19% | 22.48% | 22.18% |

During the year 2017, the capital adequacy ratio of the Group and the Bank was maintained above the prescribed minimum.

Officers of the Bank

The Bank's operations are controlled by the Supervisory Board and the Management Board. The officers of the Bank serving during the 2017 year, were as follows:

Members of the Supervisory Board

Andreas Gschwentner (Chairman from 31 May 2017)
Karl Sevelda (Chairman until 31 May 2017)
Peter Jacenko (Deputy Chairman from 8 June 2017, previously member)
Peter Lennkh (Deputy Chairman until 8 June 2017)
Lovorka Penavić (Member)
Marcus Kirchmair (Member)
Robert Fritz (Member until 31 May 2017)
Kemal Kozarić (Member)
Sabine Zucker (Member from 31 May 2017)
Harald Kreuzmair (Member from 31 May 2017)

Members of the Management Board

Michael Georg Mueller (Chairman)
Ivan Žižić (Member)
Vesna Ciganek-Vuković (Member until 31 December 2017)
Daniel Mitteregger (Member from 1 January 2018)
Liana Keserić (Member)
Zoran Koščak (Member)
Marko Jurjević (Member)

Chief executives

Vesna Muratović (until 30.04.2017)
Emilija Sertć (from 01.05.2017)

Robert Mamić

Nikola Karin

Dubravko Lukač

Ivan Vidaković

Robert Kuzmanić

Vesna Valić (until 16.11.2017)
Enkelejd Zotaj (from 17.11.2017)

Zoran Vučićević

Irena Bašić-Štefanić

Gordana Šaban

Boris Vuksan

Vesna Ćebetarević

Srđan Šverko

Toni Jurčić

Ines Knapić

Ivana Hobolja Škrtić

Ivica Jerkić

Tanja Ožbolt Šterle

Ivana Jelaš

Renata Gecan Milek

Nikolina Bogati

Ena Badanjak (until 23.08.2017)
Iva Bakija (from 01.11.2017)

Tomislav Ilijaš

Damir Jandrašek

Ivica Tonči Krvavica

Igor Mataić

Vera Miletić Fras

Zrinka Živković Matijević

Department

Financial Institution and Cash Management

Financial Markets and Investment Banking

Financial products

Credit Risk Management

Private Individuals Sales Network

Accounting and Tax Finance

IT

Legal

Human Resources

Internal Audit

Financial Control

Operation Services

Large and International Corporate Customers

SME and Mid Market Sales Network

Collection and Workout

CRM and Digital Channels

Transaction Services

Risk Controlling

Asset and Liability Management

Private Banking

Marketing and Public Relation

Executive and Participation Management

Organisation, Process and Project Management

Procurement, Facility Management and General Services

Security

Financial Advisory

Compliance

Economic and Financial Research

Appendix I – Supplementary schedules for the Croatian National Bank

Pursuant to the Croatian Accounting Law (Official Gazette 109/07) Croatian National Bank issued the Decision on Structure and Contents of Reports of Credit Institutions (Official Gazette 30/17 and 44/17). The following tables present financial statements (schedules) prepared in accordance to the above mentioned Decision:

Consolidated income statement

| | 2017 HRK million | 2016 HRK million |
|---|---------------------|---------------------|
| 1. Interest income | 1,138 | 1,305 |
| 2. (Interest expenses) | (274) | (369) |
| 3. Net interest income (1.-2.) | 864 | 936 |
| 4. Commission and fee income | 794 | 695 |
| 5. (Commission and fee expenses) | (325) | (249) |
| 6. Net commission and fee income (4.-5.) | 469 | 446 |
| 7. Gain/(loss) from investments in subsidiaries, affiliated companies and joint ventures | - | - |
| 8. Gain/(loss) from trading activities | 19 | 196 |
| 9. Gain/(loss) from embedded derivatives | (2) | 1 |
| 10. Gain/(loss) from financial assets not actively traded, but designated at fair value through profit and loss | 6 | 27 |
| 11. Gain/(loss) from financial assets available for sale | 26 | 80 |
| 12. Gain/(loss) from financial assets held to maturity | - | 27 |
| 13. Gain/(loss) from hedging transactions | 2 | (1) |
| 14. Income from investments in subsidiaries, affiliated companies and joint ventures | - | - |
| 15. Income from other equity investments | - | 1 |
| 16. Gain/(loss) from foreign exchange differences | 137 | (15) |
| 17. Other income | 519 | 368 |
| 18. Other expenses | (81) | (129) |
| 19. General and administrative expenses, depreciation and amortisation | (1,105) | (1,133) |
| 20. Net income before value adjustments and provisions for losses (3.+6.+7.+8.+9.+10.+11.+12.+13.+14.+15.+16.+17.-18.-19.) | 854 | 804 |
| 21. Expenses from value adjustments and provisions for losses | (564) | (109) |
| 22. Profit/(loss) before tax (20.-21.) | 290 | 695 |
| 23. Income tax | (102) | (160) |
| 24. Current year profit/(loss) (22.-23.) | 188 | 535 |
| 25. Earnings per share | 52 kn | 147 kn |

Appendix to the Income statement

| | 2017 | 2016 |
|---|------|------|
| Current year profit/(loss) | 188 | 535 |
| Attributable to the parent company shareholders | 188 | 535 |
| Non-controlling interest | - | - |

Appendix I – Supplementary schedules for the Croatian National Bank (continued)

Statement of Other Comprehensive Income

| | 2017 HRK million | 2016 HRK million |
|---|------------------------|------------------------|
| 1. Current year profit/(loss) | 188 | 535 |
| 2. Other comprehensive profit (2.1+ 2.2) | (11) | (23) |
| 2.1 Items not to be reclassified to profit or loss (2.1.1+2.1.2+2.1.3+2.1.4+2.1.5+2.1.6) | 2 | 1 |
| 2.1.1 Tangible assets | - | - |
| 2.1.2 Intangible assets | - | - |
| 2.1.3 Actuarial gains or (-) losses on remeasurement of defined benefit plans | - | - |
| 2.1.4 Non-current assets and disposal groups held for sale | - | - |
| 2.1.5 Share of other recognised income and expense from subjects accounted for using the equity method | 2 | 1 |
| 2.1.6 Tax on items not to be reclassified to profit or loss | - | - |
| 2.2 Items to be reclassified to profit or loss (2.2.1+2.2.2+2.2.3+2.2.4+2.2.5+2.2.6+2.2.7) | (13) | (24) |
| 2.2.1 Hedges of net investments in foreign operations (effective portion) (2.2.1.1+2.2.1.2.+2.2.1.3) | - | - |
| 2.2.1.1 Gains or losses (-) in equity | - | - |
| 2.2.1.2 Amount transferred to profit or loss | - | - |
| 2.2.1.3 Other reclassifications | - | - |
| 2.2.2 Foreign currency translation differences (2.2.2.1+2.2.2.2+2.2.2.3) | - | - |
| 2.2.2.1 Gains or losses (-) in equity | - | - |
| 2.2.2.2 Amount transferred to profit or loss | - | - |
| 2.2.2.3 Other reclassifications | - | - |
| 2.2.3 Cash flow hedges (effective portion) (2.2.3.1+2.2.3.2+2.2.3.3+2.2.3.4) | - | - |
| 2.2.3.1 Gains or losses (-) in equity | - | - |
| 2.2.3.2 Amount transferred to profit or loss | - | - |
| 2.2.3.3 Transferred to opening carrying amount of hedged items | - | - |
| 2.2.3.4 Other reclassifications | - | - |
| 2.2.4 Available-for-sale financial assets (2.2.4.1+2.2.4.2+2.2.4.3) | (16) | (33) |
| 2.2.4.1 Gains or losses (-) in equity | (10) | 66 |
| 2.2.4.2 Amount transferred to profit or loss | (4) | (99) |
| 2.2.4.3 Other reclassifications | (2) | - |
| 2.2.5 Non-current assets and disposal groups held for sale (2.2.5.1+2.2.5.2+2.2.5.3) | - | - |
| 2.2.5.1 Gains or losses (-) in equity | - | - |
| 2.2.5.2 Amount transferred to profit or loss | - | - |
| 2.2.5.3 Other reclassifications | - | - |
| 2.2.6 Share of other recognised income and expenses from investments in subsidiaries, associates and joint ventures | - | - |
| 2.2.7 Tax on items to be reclassified to profit or loss (-) | 3 | 9 |
| 3. Total comprehensive income for the year (1.+2.) | 177 | 512 |
| 4. Attributable to non-controlling interests | - | - |
| 5. Attributable to equity holders of the Bank | 177 | 512 |

Appendix I – Supplementary schedules for the Croatian National Bank (continued)

Consolidated statement of financial position (balance sheet)

| | 2017 HRK million | 2016 HRK million |
|---|---------------------------------|---------------------------------|
| Assets | | |
| 1. <i>Cash and deposits with CNB (1.1+1.2)</i> | 6,357 | 5,337 |
| 1.1. Cash | 805 | 712 |
| 1.2. Deposits with CNB | 5,552 | 4,625 |
| 2. Deposits with banking institutions | 946 | 1,154 |
| 3. Treasury bills of Ministry of Finance and treasury bills of CNB | 309 | 105 |
| 4. Securities and other financial instruments held for trading | 554 | 1,853 |
| 5. Securities and other financial instruments available for sale | 5,586 | 5,173 |
| 6. Securities and other financial instruments held to maturity | 275 | 287 |
| 7. Securities and other financial instruments which are not actively traded, but are classified at fair value through profit and loss | 349 | 420 |
| 8. Derivative financial assets | 33 | 115 |
| 9. Loans to financial institutions | 63 | 290 |
| 10. Loans to other customers | 17,661 | 18,369 |
| 11. Investments in subsidiaries, affiliated companies and joint ventures | - | - |
| 12. Repossessed assets | 91 | 78 |
| 13. Tangible and intangible assets (minus depreciation and amortisation) | 1,335 | 1,765 |
| 14. Interest, fees and other assets | 642 | 436 |
| A. Total assets (1.+2.+3. Do 14.) | 34,201 | 35,382 |
| Liabilities and equity | | |
| 1. <i>Borrowings from financial institutions (1.1+1.2)</i> | 1,385 | 2,396 |
| 1.1. Short-term borrowings | 542 | 889 |
| 1.2. Long-term borrowings | 843 | 1,507 |
| 2. <i>Deposits (2.1+2.2+2.3)</i> | 24,492 | 24,114 |
| 2.1. Deposits on giro-accounts and current accounts | 8,149 | 7,541 |
| 2.2. Savings deposits | 6,826 | 5,359 |
| 2.3. Term deposits | 9,517 | 11,214 |
| 3. <i>Other borrowings (3.1+3.2)</i> | 1,174 | 1,582 |
| 3.1. Short-term borrowings | - | 354 |
| 3.2. Long-term borrowings | 1,174 | 1,228 |
| 4. Liabilities arising from derivatives and other liabilities held for trading | 46 | 94 |
| 5. <i>Issued debt securities (5.1+5.2)</i> | - | - |
| 5.1. Issued short-term debt securities | - | - |
| 5.2. Issued long-term debt securities | - | - |
| 6. Issued subordinated instruments | 826 | 831 |
| 7. Issued hybrid instruments | - | - |
| 8. Interest, fees and other assets | 1,585 | 1,467 |
| B. Total liabilities (1.+2.+3.+4.+5.+6.+7.+8.) | 29,508 | 30,484 |
| Equity | | |
| 1. Share capital | 3,633 | 3,633 |
| 2. Current year profit/(loss) | 188 | 535 |
| 3. Retained earnings/(loss) | 635 | 483 |
| 4. Legal reserves | 181 | 181 |
| 5. Statutory and other capital reserves | 7 | 8 |
| 7. Unrealised gain/(loss) on value adjustment of available-for-sale financial assets | 49 | 58 |
| C. Total equity (1.+2.+3.+4.+5.+6.+7.) | 4,693 | 4,898 |
| D. Total liabilities and equity (B+C) | 34,201 | 35,382 |

Appendix to statement of financial position (balance sheet)

| | 2017 | 2016 |
|---|-------------|-------------|
| Total equity | 4,693 | 4,898 |
| Total equity attributable to equity holders | 4,693 | 4,898 |
| Minority interest | - | - |

Appendix I – Supplementary schedules for the Croatian National Bank (continued)

Consolidated statement of cash flows

| | 2017 HRK million | 2016 HRK million |
|---|---------------------|---------------------|
| Operating activities | | |
| 1.1. Gain/(loss) before tax | 290 | 695 |
| 1.2. Value adjustments and provisions for losses | 369 | (522) |
| 1.3. Depreciation and amortization | 147 | 191 |
| 1.4. Net unrealised (gain)/loss from financial assets and liabilities at fair value through profit and loss | 38 | (36) |
| 1.5. Gain/(loss) from sale of tangible assets | - | - |
| 1.6. Other (gains)/losses | (1,054) | (1,047) |
| 1. Operating cash flow before movement in operating assets (1.1.- 1.6.) | (210) | (719) |
| 2.1. Deposits with CNB | (42) | 315 |
| 2.2. Treasury bills of Ministry of Finance and treasury bills of CNB | (203) | 14 |
| 2.3. Deposits with banking institutions and loans to financial institutions | 28 | (28) |
| 2.4. Loans to other clients | 254 | 908 |
| 2.5. Securities and other financial instruments held for trading | 1,276 | (155) |
| 2.6. Securities and other financial instruments available for sale | (543) | (220) |
| 2.7. Securities and other financial instruments which are not actively traded, but are designated at fair value through profit and loss | 62 | (24) |
| 2.8. Other operating assets | 1,207 | 1,241 |
| 2. Net (increase)/decrease in operating assets (1.1. - 2.8.) | 2,039 | 2,051 |
| Increase/(decrease) in operating liabilities | | |
| 3.1. Demand deposits | 608 | 1,073 |
| 3.2. Savings and term deposits | 121 | (417) |
| 3.3. Liabilities arising from derivatives and other liabilities held for trading | (49) | (13) |
| 3.4. Other liabilities | (186) | (179) |
| 3. Net increase/(decrease) in operating liabilities (3.1.- 3.4.) | 494 | 464 |
| 4. Net cash flows from operating activities before income taxes paid (1.+2.+3.) | 2,323 | 1,796 |
| 5. (Income tax paid) | (28) | (33) |
| 6. Net cash inflows/(outflows) from operating activities (4.-5.) | 2,295 | 1,763 |
| Investment activities | | |
| 7.1. Receipts from sale of/(payments to acquire) tangible and intangible assets | (120) | (255) |
| 7.2. Receipts from sale /(payments for purchase) of investments in subsidiaries, affiliated companies-associates and joint ventures | - | - |
| 7.3. Receipts from sale/(payments to acquire) of securities and other investments held to maturity | 11 | (11) |
| 7.4. Received dividends | - | - |
| 7.5. Other receipts/(payments) from investment activities | 154 | 152 |
| 7. Net cash flow from investment activities (7.1. - 7.5.) | 45 | (114) |
| Financing activities | | |
| 8.1. Net increase/(decrease) in borrowings | (1,389) | (231) |
| 8.2. Net increase/(decrease) in issued debt securities | - | - |
| 8.3. Net increase/(decrease) in subordinated and hybrid instruments | - | - |
| 8.4. Share premium | - | - |
| 8.5. (Payment of dividend) | (385) | - |
| 8.6. Other receipts/(payments) from financial activities | - | - |
| 8. Net cash flow from financing activities (8.1. - 8.6.) | (1,774) | (231) |
| 9. Net increase/(decrease) in cash and cash equivalents (6.+7.+8.) | 566 | 1,418 |
| 10. Effects of foreign exchange differences on cash and cash equivalents | (5) | 27 |
| 11. Net increase/(decrease) in cash and cash equivalents (9.+10.) | 561 | 1,445 |
| 12. Cash and cash equivalents at the beginning of the year | 4,968 | 3,523 |
| 13. Cash and cash equivalents at the year end | 5,529 | 4,968 |

Appendix I – Supplementary schedules for the Croatian National Bank (continued)

Consolidated statement of changes in equity

| (All amounts in HRK million) | Share capital | Treasury shares | Legal, statutory and other reserves | Retained earnings/(loss) | Current year profit/loss | Unrealised gain/losses from revaluation of financial assets available for sale | Minority interest | Total capital and reserves |
|--|---------------|-----------------|-------------------------------------|--------------------------|--------------------------|--|-------------------|----------------------------|
| 1. Balance at 1 January 2017 | 3,633 | - | 189 | 1,018 | - | 58 | - | 4,898 |
| 2. Changes in accounting policies and error correction | - | - | - | - | - | - | - | - |
| 3. Restated balance at 1 January 2017 (1.+2.) | 3,633 | - | 189 | 1,018 | - | 58 | - | 4,898 |
| 4. Disposal of financial assets available for sale | - | - | - | - | - | - | - | - |
| 5. Change in fair value of financial assets available for sale | - | - | - | - | - | (9) | - | (9) |
| 6. Tax on items directly recognised or transferred from capital and reserves | - | - | - | - | - | - | - | - |
| 7. Other gains or losses directly recognised in capital and reserves | - | - | - | - | - | - | - | - |
| 8. Net gains/losses directly recognised in capital and reserves (4.+5.+6.+7.) | - | - | - | - | - | (9) | - | (9) |
| 9. Current year gain/(loss) | - | - | - | - | 188 | - | - | 188 |
| 10. Total income and expenses recognised for the current year (8.+9.) | - | - | - | - | 188 | (9) | - | 179 |
| 11. Increase/ (decrease) in share capital | - | - | - | - | - | - | - | - |
| 12. Acquisition/(disposal) of treasury shares | - | - | - | - | - | - | - | - |
| 13. Other movements | - | - | (1) | 2 | - | - | - | 1 |
| 14. Transfer to reserves | - | - | - | - | - | - | - | - |
| 15. Dividends paid | - | - | - | (385) | - | - | - | (385) |
| 16. Distribution of profit (11.+12.+13.+14.+15.) | - | - | (1) | (383) | - | - | - | (384) |
| 17. Balance at 31 December 2017 (3.+10.+ 16.) | 3,633 | - | 188 | 635 | 188 | 49 | - | 4,693 |

Appendix I – Supplementary schedules for the Croatian National Bank (continued)

Consolidated statement of changes in equity

(continued)

| (All amounts in HRK million) | Share capital | Treasury shares | Legal, statutory and other reserves | Retained earnings/(loss) | Current year profit/loss | Unrealised gain/losses from revaluation of financial assets available for sale | Minority interest | Total capital and reserves |
|--|---------------|-----------------|-------------------------------------|--------------------------|--------------------------|--|-------------------|----------------------------|
| 1. Balance at 1 January 2016 | 3,633 | - | 199 | 430 | - | 82 | 68 | 4,412 |
| 2. Changes in accounting policies and error correction | - | - | - | - | - | - | - | - |
| 3. Restated balance at 1 January 2016 (1.+2.) | 3,633 | - | 199 | 430 | - | 82 | 68 | 4,412 |
| 4. Disposal of financial assets available for sale | - | - | - | - | - | - | - | - |
| 5. Change in fair value of financial assets available for sale | - | - | - | - | - | (24) | - | (24) |
| 6. Tax on items directly recognised or transferred from capital and reserves | - | - | - | - | - | - | - | - |
| 7. Other gains or losses directly recognised in capital and reserves | - | - | - | - | - | - | - | - |
| 8. Net gains/losses directly recognised in capital and reserves (4.+5.+6.+7.) | - | - | - | - | - | (24) | - | (24) |
| 9. Current year gain/(loss) | - | - | - | - | 535 | - | - | 535 |
| 10. Total income and expenses recognised for the current year (8.+9.) | - | - | - | - | 535 | (24) | - | 511 |
| 11. Increase/ (decrease) in share capital | - | - | - | - | - | - | - | - |
| 12. Acquisition/(disposal) of treasury shares | - | - | - | - | - | - | - | - |
| 13. Other movements | - | - | (11) | 54 | - | - | (68) | (25) |
| 14. Transfer to reserves | - | - | 1 | (1) | - | - | - | - |
| 15. Dividends paid | - | - | - | - | - | - | - | - |
| 16. Distribution of profit (11.+12.+13.+14.+15.) | - | - | (10) | 53 | - | - | (68) | (25) |
| 17. Balance at 31 December 2016 (3.+10.+ 16.) | 3,633 | - | 189 | 483 | 535 | 58 | - | 4,898 |

Appendix II – Reconciliation of the statutory financial statements with the supplementary schedules for the Croatian National Bank

Considering the difference between data classification in the schedules prepared in accordance with the CNB requirements and presentation in the statutory financial statements prepared pursuant to legal requirements for the accounting in banks in the Republic of Croatia, the data are reconciled in the below tables.

Reconciliation for the income statement for years ended 31 December 2017 and 31 December 2016:

| | 2017 CNB schedules HRK million | 2017 Statutory financial statements HRK million | 2017 Difference HRK million | 2016 CNB schedules HRK million | 2016 Statutory financial statements HRK million | 2016 Difference HRK million |
|--|--|--|--------------------------------------|--|--|--------------------------------------|
| Interest income | 1,138 | 1,139 | (1) | 1,305 | 1,305 | 0 |
| Interests expense | (274) | (226) | (48) | (369) | (317) | (52) |
| Net interest income | 864 | 913 | (49) | 936 | 988 | (52) |
| Fee and commission income | 794 | 794 | - | 695 | 694 | 1 |
| Fee and commission expense | (325) | (325) | - | (249) | (257) | 8 |
| Net commission and fee income | 469 | 469 | - | 446 | 437 | 9 |
| Gains/(losses) from trading activities | 19 | 192 | (173) | 196 | 315 | (119) |
| Gains/(losses) from embedded derivatives | (2) | - | (2) | 1 | - | 1 |
| Gains/(losses) from assets which are not actively traded, but are designated at fair value through P&L | 6 | - | 6 | 27 | - | 27 |
| Gains/(losses) from activities related to available-for-sale financial assets | 26 | - | 26 | 80 | - | 80 |
| Gains/(losses) from activities related to held to maturity investments | - | - | - | 27 | - | 27 |
| Gains/(losses) from hedging transactions | 2 | - | 2 | (1) | - | (1) |
| Income from other equity investments | - | - | - | 1 | - | 1 |
| Gains/(losses) from foreign exchange differences | 137 | - | 137 | (15) | - | (15) |
| Other income | 519 | 300 | 219 | 368 | 322 | 46 |
| Total other income | 707 | 492 | 215 | 684 | 637 | 47 |
| General and administrative expenses, depreciation and amortisation | (1,105) | (1,212) | 107 | (1,133) | (1,877) | 744 |
| Value adjustments impairment losses and provisions | (564) | (372) | (192) | (109) | 510 | (619) |
| Other expenses | (81) | - | (81) | (129) | - | (129) |
| Total expenses | (1,750) | (1,584) | (166) | (1,371) | (1,367) | (4) |
| Profit before tax | 290 | 290 | - | 695 | 695 | - |
| Income tax | (102) | (102) | - | (160) | (160) | - |
| Profit for the year | 188 | 188 | - | 535 | 535 | - |
| Earning per share (in HRK) | 52 | 52 | - | 147 | 147 | - |

Appendix II – Reconciliation of the statutory financial statements with the supplementary schedules for the Croatian National Bank (continued)

- In the CNB schedule, expenses for deposit guarantee scheme and resolution fund are presented in the position interest expense, and in the statutory financial statements those expenses are classified as administrative expenses. Negative interest on deposits with banks and factoring fee are categorized in the item *General administrative expenses, depreciation and amortisation* in the CNB schedule, and in the statutory financial statements they are presented in *Interest expense*.
- In the CNB schedule, net exchange differences are presented within the following items: *Gains/(losses) from foreign exchange differences, Net interest income, Net fee and commission income* and *Impairment losses and provisions*. In the statutory financial statements all foreign exchange differences are disclosed in item *Net Gain/(loss) from trading activities, from available-for-sale financial assets and from foreign exchange differences on translation of monetary assets and liabilities*. Also, the remaining items presented within total other income in the CNB schedules are classified as *Net Gain/(loss) from trading activities, from available-for-sale financial assets and from foreign exchange differences on translation of monetary assets and liabilities* in the statutory financial statements.
- Debt sale proceeds are disclosed as *Other income* in the CNB schedules, while being stated in *Impairment losses* in the statutory financial statements. In addition, the *Other income* item in the CNB schedules includes the income resulting from change of technical reserve, whereas this income is disclosed within *General administrative expenses, depreciation and amortisation* in the statutory financial statements.
- Other expenses and costs, costs of donations, advertising, promotions and entertainment are classified as a separate item *Other expenses*, and in the statutory financial statements all such expenses are presented as *General administrative expenses, depreciation and amortisation*.

Appendix II – Reconciliation of the statutory financial statements with the supplementary schedules for the Croatian National Bank (continued)

Reconciliation for the consolidated balance sheet at 31 December 2017 and 31 December 2016:

| | 2017 CNB schedules | 2017 Statutory financial statements | 2017 Differenc e | 2016 CNB schedules | 2016 Statutory financial statements | 2016 Difference |
|---|--------------------------|--|------------------------|--------------------------|--|--------------------|
| | HRK million | HRK million | HRK million | HRK million | HRK million | HRK million |
| Assets | | | | | | |
| Cash and deposits with CNB | 6,357 | 6,447 | (90) | 5,337 | 5,396 | (59) |
| Deposits with credit institutions | 946 | 894 | 52 | 1,154 | - | 1,154 |
| Treasury bills and CNB bills | 309 | - | 309 | 105 | 1,332 | (1,227) |
| Securities and other financial instruments held for trading | 554 | 951 | (397) | 1,853 | 2,515 | (662) |
| Securities and other financial instruments available for sale | 5,586 | 5,937 | (351) | 5,173 | 5,217 | (44) |
| Securities and other financial instruments held to maturity | 275 | 279 | (4) | 287 | 293 | (6) |
| Securities and other financial instruments which are not actively traded, but are designated at FVTPL | 349 | - | 349 | 420 | - | 420 |
| Derivative financial assets | 33 | - | 33 | 115 | - | 115 |
| Loans to financial institutions | 63 | - | 63 | 290 | - | 290 |
| Loans to other customers | 17,661 | 17,745 | (84) | 18,369 | 18,504 | (135) |
| Reposessed assets | 91 | - | 91 | 78 | - | 78 |
| Tangible assets (less depreciation) | 1,335 | 1,309 | 26 | 1,765 | 1,496 | 269 |
| Intangible assets | - | 239 | (239) | - | 240 | (240) |
| Deferred tax assets | - | 86 | (86) | - | 86 | (86) |
| Interest, fee and other assets | 642 | 291 | 351 | 436 | 285 | 151 |
| Total assets | 34,201 | 34,178 | 23 | 35,382 | 35,364 | 18 |
| Liabilities | | | | | | |
| Borrowings from financial institutions | 1,385 | 2,572 | (1,187) | 2,396 | 3,992 | (1,596) |
| Deposits | 24,492 | 24,836 | (344) | 24,114 | 24,585 | (471) |
| Other borrowings | 1,174 | - | 1,174 | 1,582 | - | 1,582 |
| Liabilities arising from derivatives and other liabilities held for trading | 46 | 59 | (13) | 94 | 97 | (3) |
| Issued subordinated instruments | 826 | 832 | (6) | 831 | 837 | (6) |
| Provisions for liabilities and costs | - | 173 | (173) | - | 187 | (187) |
| Income tax charge | - | 70 | (70) | - | - | - |
| Interest, fees and other liabilities | 1,585 | 951 | 634 | 1,467 | 776 | 691 |
| Total liabilities | 29,508 | 29,493 | 15 | 30,484 | 30,474 | 10 |
| Equity | | | | | | |
| Share capital | 3,633 | 3,633 | - | 3,633 | 3,633 | - |
| Net (loss)/profit for the year | 188 | 188 | - | 535 | 535 | - |
| Retained earnings/(loss) | 635 | 634 | 1 | 483 | 482 | 1 |
| Legal reserve | 181 | 181 | - | 181 | 181 | - |
| Statutory and other capital reserves | 7 | 1 | 6 | 8 | 1 | 7 |
| Unrealised gain/(loss) on value adjustment of available-for-sale financial assets | 49 | 48 | 1 | 58 | 58 | - |
| Total equity | 4,693 | 4,685 | 8 | 4,898 | 4,890 | 8 |
| Total liabilities and equity | 34,201 | 34,178 | 23 | 35,382 | 35,364 | 18 |

Appendix II – Reconciliation of the statutory financial statements with the supplementary schedules for the Croatian National Bank (continued)

- The difference in total assets and total liabilities and equity at 31 December 2017 in the amount of HRK 22 million (2016: HRK 18 million) resulted from the difference in the presentation of advance payment of income tax and income tax charge in the balance sheet prepared according to the CNB schedule and in the statutory financial statements, where these items are presented within the income tax liability.
- Interest receivable is disclosed within *Interest, fee and other assets* in the CNB schedules, while being presented as part of respective financial instruments in the statutory financial statements.

- The item *Cash and balances with CNB* in the CNB schedules does not include balances on accounts with other banks which are presented within *Deposits with other credit institutions*. Placements with banks are disclosed partly within Loans to financial institutions and partly within Deposits with credit institutions in the CNB schedules.
- Treasury bills with maturity up to 12 months are presented in a separate item *Treasury bills and CNB bills* in the CNB schedule, while being classified as *Financial assets available for sale* and *Financial assets at fair value through profit and loss (FVTPL)* in the statutory financial statements.
- Repossessed assets are disclosed separately in the CNB schedules, and in the statutory financial statements repossessed assets are presented as *Other assets*.
- In the CNB schedules intangible assets are stated within *Interest, fees and other assets*, while being disclosed as a separate line item in the statutory financial statements. Deferred tax assets are also disclosed separately in the statutory balance sheet, whereas in the CNB schedule they are presented within *Interest, fees and other assets*.
- Advance payment on leases and assets designated for sale are presented within *Tangible assets (minus depreciation)* in the CNB schedule, while being disclosed in the statutory financial statements within *Other assets*.
- Interest payable is disclosed within *Interest, fees and other liabilities* in the CNB schedule, while being classified as part of related financial instruments.
- The *Deposits* item in the statutory financial statements includes, besides the interest payable, the liabilities for escrow account deposits and restricted deposits, which are included within *Interest, fees and other liabilities* in the CNB schedule.
- Provisions for liabilities and charges income tax charge are presented in the statutory financial statements as separate line items, while in the CNB schedules, they are included in *Interest, fees and other liabilities*.
- In the statutory financial statements reserves created by closing of inactive customer deposit accounts are presented in *Other liabilities*, while in the CNB schedules they are disclosed within *Statutory and other capital reserves*.