HRVATSKA POŠTANSKA BANKA GROUP

Consolidated Annual Report for 2016

Zagreb, April 2017

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Introduction

The Annual report includes a summary of financial information, description of operations and audited financial reports together with the independent auditor's opinion for the year ended December 31 2016, in Croatian and English language.

Legal Status

The Annual report includes the annual financial reports prepared in accordance with statutory accounting requirements for banks in Republic of Croatia and audited in accordance with International Standards on Auditing.

The Annual report has been prepared in accordance with the Accounting Act and the Companies Act that require reporting to shareholders at the annual shareholders' meeting of the Management Board. According to the Accounting Law the statutory financial reports are report of financial position, PNL report with a report of comprehensive income, report of changes in equity, cash flow report and notes to the financial reports, and the Companies Act, in accordance Article 250.a and 250.b, prescribes the obligation to submit an annual report on the state of the Bank, other members of the HPB Group and consolidated annual report of the Group.

Abbreviations

In the Annual report Hrvatska Poštanska Banka p.l.c. is referred to as «the Bank», «HPB» or "the parent company" (of the Group), Hrvatska Poštanska Banka Group is referred to as «the HPB Group» or just «the Group», the Croatian National Bank is referred to as «the CNB» and the Croatian Bank for Reconstruction and Development is referred to as «the HBOR».

Exchange Rates

For the purpose of translation of foreign currencies into Croatian kuna, the following exchange rates of the CNB were used:

December 31 2016	EUR1 = HRK7.557787	USD1 = HRK7.168536
December 31 2015	EUR1 = HRK7.635047	USD1 = HRK6.991801

HRVATSKA POŠTANSKA BANKA P.L.C. – 2016 OVERVIEW

RESULTS

- ✓ **Net profit: HRK188M** (+53% YoY)
- ✓ **Assets:** HRK19,338M (+9% YoY)
- ✓ **Net loans:** HRK11,398M (+12% YoY)
- ✓ **Deposits:** HRK16,282M (+11% YoY)

CLIENTS AND PRODUCTS

- ✓ **More than 640K clients**
- ✓ **429K retail current accounts**
- ✓ **9,592 corporate accounts**
- ✓ **727K HPB cards**
- ✓ **HRK8.7B of insured savings**
- ✓ **New products – SuperSmart HPB, online credit applications**

NETWORK

More than 60 business units:

- ✓ 10 corporate regional centers
- ✓ 8 retail regional centers
- ✓ 45 outlets
- ✓ 7 detached tellers

- ✓ 402 ATMs
- ✓ 1,016 post offices
- ✓ 180 FINA branches

AWARDS AND RECOGNITIONS

- ✓ **HPB one of the *rising stars*** (The Banker, September 2016)
- ✓ The best mobile application **SuperSmart HPB, SoMo Tech award** (*Weekend Media Festival*, Rovinj, September 2016)
- ✓ **mHPB best graded** bank application in Croatia (VIDI, February 2017)
- ✓ Certificate **„Employer Partner"** by Selectio (December 2016)

Summary of Operation and Key Financial Indicators

HRK million

Group	2016	2015	2014	2013	2012
Basic Indicators					
Profit/ (Loss) for the Year	191	125	(629)	36	102
Operating Profit	392	322	307	259	275
Total Assets	19,738	18,014	17,570	18,598	17,266
Loans to Customers	11,554	10,298	10,474	11,754	10,769
Received Deposits	16,534	14,851	14,459	15,103	13,634
Share Capital and Reserves	1,942	1,779	843	1,445	1,411
Other Indicators					
Return on Share Capital	15.68%	7.01%	-65.11%	3.70%	10.57%
Return on Assets	0.97%	0.69%	-3.58%	0.19%	0.59%
Operating Expenses[1] to Operating Income Ratio	53.74%	59.50%	60.36%	63.90%	63.61%

[1]*General and Administrative Expenses, Depreciation and Amortization and Other Costs*

Capital Indicators of the Group's Parent Company - Hrvatska Poštanska Banka p.l.c.

Bank	2016	2015	2014	2013	2012
Regulatory Capital	1,520	1,534	645	1,573	1,669
The Capital Adequacy	15.66%	15.85%	6.65%	13.51%	14.89%

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Statement of Condition by the President of the Management Board

Dear clients and shareholders,
On behalf of the Management Board I have a great honor to present business results of Hrvatska Poštanska Banka in 2016 which was the best year on record.

In previous year we faced many challenges in a form of announced or current regulatory changes but also evergrowing market competition amid general interest rates decline. HPB managed to adapt to the aforementioned conditions by quality sales management, price policy and process improvement. Moreover 2016 was the year of many initiatives and strategic projects (Super Smart HPB, CRM client relationship management tool, sale of past-due uncollected receivables, SEPA Credit Transfer etc.) which required engagement of human and financial resources.

Simultaneous commercial and market success does not depend solely on external factors but also on our internal characteristics. Therefore out of all successes in 2016 I take the most pride in growth of our client base. Today HPB has more than 640K clients while in 2016 around 33K new current accounts were opened, as well as over 1.5K corporate accounts. I see this growth as a result of our dedication to clients which is one of HPB's corporate values and we will continue to practice it in the future.

Financial Results of Hrvatska Poštanska Banka

Despite demanding operating activities the Bank increased its **net profit** in 2016 by 52.8% to HRK188.3M, the highest in the Bank's corporate history.

Operating profit in the amount of HRK387.7M is HRK66.6M or 20.7% higher than in 2015 due to better noninterest income and 4.6% lower expenses amid reorganization in 2015 and responsible cost management on all levels.

Net interest income is HRK514.4M which is 0.8% better than a year before. Mild increase amid general interest rates decline was due to increase in healthy part of the loan portfolio as well as optimization of financing sources' structure and cost.

Net income from commissions and fees is HRK184.8M which is 1.7% more than in previous year, in line with expectations. Substitution of cash transactions with other types of payments is inevitable and it reflected in lower revenue. On the other hand fees from account acquisitions and noncash payments were on the rise which makes an important contribution to sustainability of the Bank's future revenue.

Financial markets have been consistently making excellent results and **securities and FX trading gains** were more than doubled in 2016 (+146.2%). Even excluding one-off gains from sale of ownership in VISA Europe Ltd in the amount of HRK33.5M, gains were up by 74.9% compared to the previous year.

Other noninterest revenue are mostly one-off effects of sales of assets and other effects of collection of receivables. Considering the Bank did not have substantial revenue of the aforementioned sales and collections like in the previous year, other noninterest revenue was down by 68.9%. However we are dedicated to improving collection procedures and practices and at the same time maintaining social responsibility awareness.

Operating expenses were cut by 4.6% due to organizational and process improvements in 2015 and 2016. As a result the C/ I indicator was improved to 53.2%, the best in 12 years. Therefore HPB continues to converge to the Croatian sector average which was 50.6% in 2016 based on unaudited data.

Impairment and liabilities provision costs were up by 16.2% compared to 2016 but provisions' burden to the operating profit was virtually unchanged - around 60% in 2016 and 2015 – due to strong operating profit growth. On the structure front provisions for identified NPL losses were cut by 7.9%, while due to the Bank's growth there were substantial general reserves for A placements and potential liabilities (HRK13.5M in 2016 vs HRK6.0M revenue from cancelling provisions in 2015). Also by using conservative approach in line with the regulation, provisions for court cases and recognized impairments of nonfinancial assets were formed in the amount substantially higher than in 2015.

Despite decreasing NPL coverage from 64.3% to 62.6% amid sale of uncollected past-due receivables, the Bank was still largely in line with the sector average (63.5% at the end of 2016).

Amid profit in 2015 and even better result in 2016, the Bank met all preconditions for reliable estimation of the future taxed profit. From accumulated tax losses in 2014 deferred tax assets were recognized in the amount it could be used as a tax relief. Deferred tax assets from the mentioned item were recognized in the amount of HRK35.3M, while other items resulted with deferred tax assets expenditure in the amount of HRK8.8M.

Due to deposits inflow the **Bank's assets were up by 9.3%** to HRK19.3B in 2016 which is the highest annual growth in the last 5 years. The Bank increased its market share in all relevant balance sheet categories.

After 2015 which was marked by consolidation, reorganization and capital increase, **the Bank made substantial growth of its loan portfolio in 2016.** Total net loan and receivables portfolio was up by HRK1.2B or 11.9% at the same time the market loans were substantially down. Retail loans are still on the rise (+12.3%) due to 51.2% growth in housing loans. Corporate loans were up by 11.5% to HRK6.8B at the end of 2016. HPB has continued to support companies and sectors which create additional value for the national economy. The Bank has continued its cooperation and lending to corporates, government and local government units with an emphasis on the SMEs growth.

Total deposits were up by 11.3% to HRK16.2B although its structure was changed. Namely acquisition potential in corporate business segment was used and corporate deposits were up by 19.7%. Retail business also made its contribution to the Bank's deposit base growth: retail savings were increased by 4.7% and there were 33 newly opened current accounts.

The Croatian National Bank amid its regular supervisory estimate, set the regulatory capital rate of 15.35% (from November 2016 on) after previous 14.00%. In order to comply with the aforementioned measure amid capital shortfall the Bank optimized its risk exposure which were up minimally compared to the total assets growth. Therefore **capital adequacy rate was mildly decreased to 15.66%.**

Consolidated Financial Results of Hrvatska Poštanska Banka Group

HPB Group is comprised by the parent company Hrvatska Poštanska Banka, HPB Stambena Štedionica, HPB Invest (investment fund management company) and HPB Nekretnine (real-estate company). All subsidiaries made after-tax profit in 2016 and HPB Stambena Štedionica made HRK3.3M, HPB Nekretnine HRK630K, while HPB Invest made HRK1.8M net profit. Besides subsidiaries which were founded and are 100% owned by HPB, consolidated report of financial position also includes H1 TELEKOM in which the Bank controls 58.2% of ownership. This ownership stake was acquired in a process of the pre-bankruptcy settlement by debt to equity swap and is classified as assets available for sale.

Led by the parent company, HPB Group made an **after-tax profit** of HRK190.5M in 2016. Which is 52.7% more than in 2015. Besides the Bank, 2016 was also profitabile for all subsidiaries. HPB Stambena Štedionica made a HRK3.3M net profit, HPB Invest HRK1.8M, while HPB Nekretnine HRK630K.

The Group's assets are almost entirely the Bank's assets, so change in the latter reflects the change in the former, although there are certain consolidation differences due to internal transactions. The Group's assets were HRK19.7B at the end of 2016 which is 9.6% more than in 2016 while the Bank dominantly affected the Group's assets structure by optimizing return on assets.

Hrvatska Poštanska Banka Business Activity in 2017

Each year of my and my colleagues' mandate in the Management Board was challenging. The following year will be no exception. In 2017 the goal will be cooperation with Hrvatska Pošta in order to create the largest network of outlets for offering banking services in Croatia. Considering some of these outlets are in locations with no other banks, it will give local communities easier access to necessary financial services.

Moreover 2017 is the year of preparing for a huge wave of the new regulation which will be enacted on January 01 2018 and will create new operating, financial and equity challenges. Anyway the growth from 2016 could not be repeated without additional capital on which the final decision will be made by the Bank's shareholders. The Management Board can and will continue to do good business in order to achieve strategies with key focus on creating value for our shareholders, offering top services to our clients and supporting growth of our homeland.

In the name of Hrvatska Poštanska Banka I hereby express my greatest appreciation to our clients, shareholders, employees and all others which support the project of creating the best bank in our Motherland.

Tomislav Vuić

President of the Management Board

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Management Board of Hrvatska Poštanska Banka p.l.c.

Mr. Tomislav Vuić

Previous appointments:
• 2003 – 2014, Erste & Steiermärkische Bank d.d. – deputy CEO
• 2002 – 2003 Erste & Steiermärkische Bank d.d. – CEO
• 1997 – 2000 Trgovačka Banka – Board member / CEO in 2000

CEO

CEO since September 10 2014

Responsibilities:

- Retail Banking
- Corporate Banking
- Financial Markets
- Direct Banking
- Compliance and Board Support
- Human Resources Management
- Marketing
- Corporate Communications
- Legal Affairs

Mr. Domagoj Karadjole

Previous appointments:
• 2010 – 2014 Erste Serbia – executive director for Retail
• 2005 – 2010 Erste & Steiermärkische Bank d.d. – director of Small Businesses

CFO CRO

Board member since December 22 2014

Responsibilities:

- Risk Management
- Collection Management
- Financial Management
- Internal Audit
- Service Quality Management
- Assets and Liabilities Management
- Corporate Security (from January 25 2017)

Mr. Mladen Mrvelj

Previous appointments:
• 2007 – 2012 Erste & Steiermärkische Bank d.d. – director and CIO

CIO

Board member since December 17 2014

Responsibilities

- IT
- Business Support
- Organization and Project Management
- Procurement and General Affairs
- Corporate Security (until January 24 2017)

Macroeconomic Environment in the Republic of Croatia in 2016

Macroeconomic Indicators for Croatia

	2011.	2012.	2013.	2014.	2015.	2016.	Trend
Real GDP Growth (%)	(0.3)	(2.2)	(1.1)	(0.4)	1.6	2.9	↑
Average Annual Inflation Rate (%)	2.3	3.4	2.2	(0.2)	(0.5)	(1.1)	↑
Year End Employment (% YoY)	(0.9)	(2.0)	(2.2)	(0.2)	1.2	1.9	↑
Year End Unemployment Rate (%)	18.6	20.9	21.5	19.4	17.2	14.8	↓
Current Account of Balance of Payments (% GDP)	(0.8)	(0.2)	1.0	2.2	5.2	5,7*	↓
Operating Balance of Central Goverment and Off-Budget Funds (HRK billion)	(12.0)	(8.0)	(14.4)	(9.9)	(4.3)	0.6	↑
General Government Debt (% GDP)	65.2	70.7	82.2	86.6	86.7	84.2	↓
EUR/HRK on December 31	7.5304	7.5456	7.6376	7.6615	7.6350	7.5578	↓
Assets of Credit Institutions (HRK billion)	415.2	407.7	405.7	403.7	401.3	396.3	↓
Total Loans (HRK billion)	291.7	283.9	286.9	279.9	275.4	261.2	↓
Total Deposits (HRK billion)	287.6	282.1	289.2	292.8	300.8	300.9	=
NPL Share (%)	12.4	13.9	15.7	17.1	16.7	13.8	↓

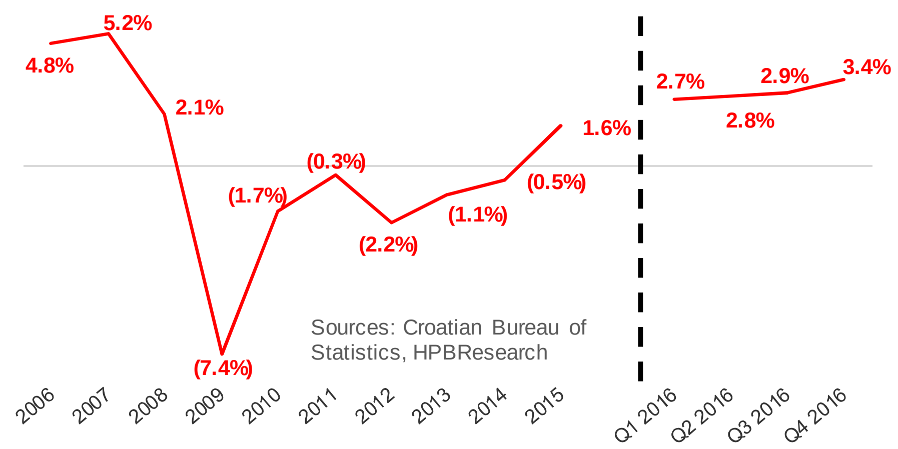
**Balance in the first 3 quarters of 2016 compared to 8.4% in the same period of 2015*

Sources: Croatian Bureau of Statistics, CNB, Croatian Pension Insurance Institute, HPBResearch

Faster Economic Recovery

Real GDP growth has stepped up from 1.6% in 2015 to 2.9% in 2016. The largest contribution to stronger growth came from the personal consumption (+1.9%) amid better tourist consumption and strong retail sales growth in Q4 before and amidst of the holidays due to improved consumer sentiment and expectations on economic and financial situation. Contribution of gross investments was +0.8% amid mild recovery in business environment and construction works, especially in Q4. Contribution of government spending was +0.4% and is positive for the first time since 2013 partially due to larger general government staff costs.

Annual Real GDP Growth Rates

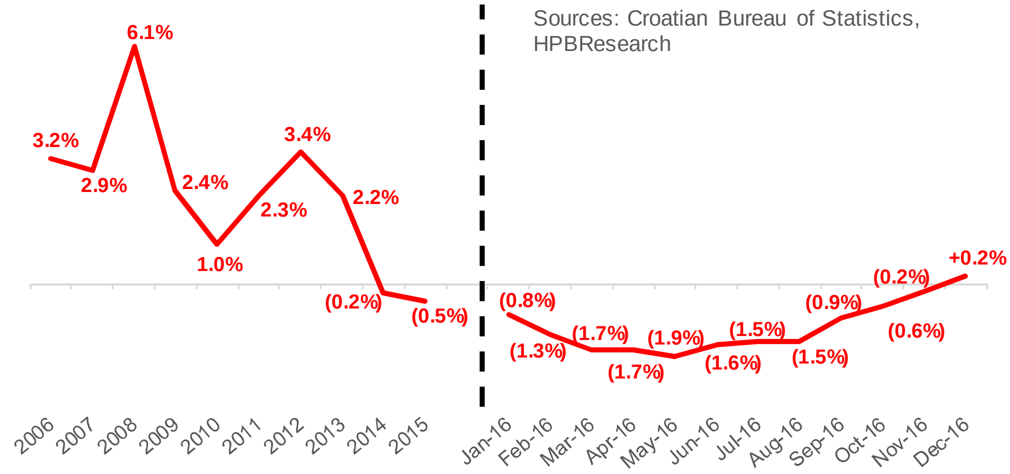


Net exports contribution in 2016 was negative (-0.1%), for the first time since 2011, which was due to faster imports growth compared to exports amid mildly stronger HRK vs EUR. Nevertheless net exports are still largely positive (+HRK7.2B) due to recovery of Eurozone aggregate demand.

Deflation Almost All Year

2016 was for the most part characterized by deflationary pressures amid largely external trends. Average annual inflation rate in 2016 was -1.1% which is the third consecutive deflation year. Price decline in 2016 was mostly effected by lower transport prices (-4.2%) amid increased competition, lower housing, energy and utilities (-2.5%) amid lower domestic demand and lower global energy prices, and communication prices (-2.3%) amid introduction of maximum prices for telecommunication providers in the EU.

Annual Inflation Rate – average by years, months in 2016

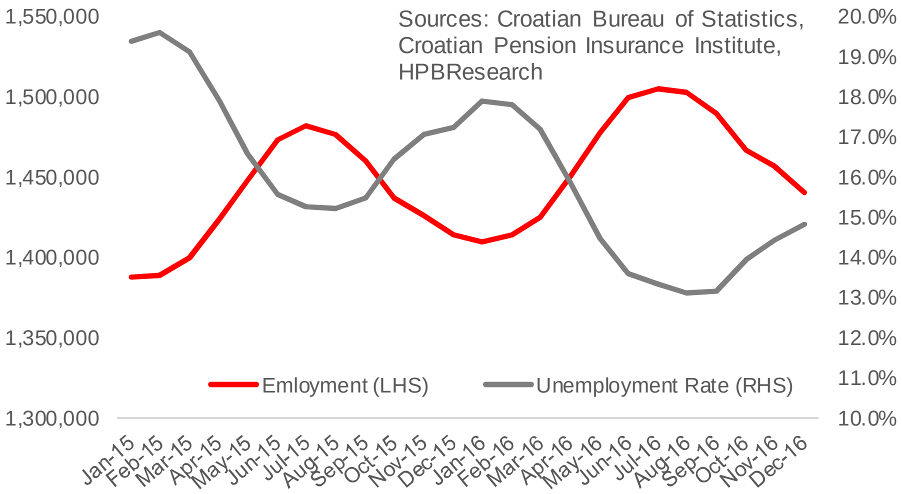


First 3 quarters of 2016 were marked by a strong deflation with inflation rate of -1.5% amid negative external movements, while deflationary pressures eased in Q4 and were nonexistent in December with YoY inflation rate of +0.2%. Price increase in Q4 was largely due to healthcare services, alcoholic drinks and tobacco, and food and beverages.

Employment Rises, Unemployment Declines

In 2016 employment had picked up compared to the previous year. At the end of 2016 26.6K more people were employed than at the end of 2015, while average YoY increase in the whole 2016 was 26.7K.

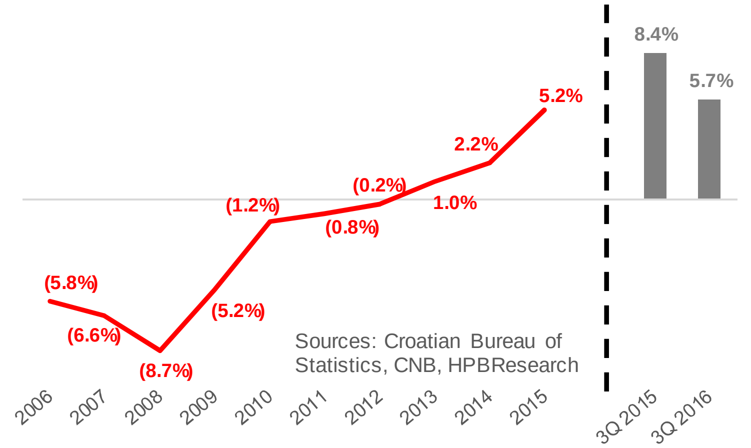
Employment and Unemployment Rate by Months



Unemployment rate had been falling during the whole year (YoY) and at the end of 2016 was 14.8% which is 2.4 pp lower than at the end of 2015.

Tourism Insufficient to Compensate Negative Investment Profit

Current Account of Balance of Payments (% GDP)

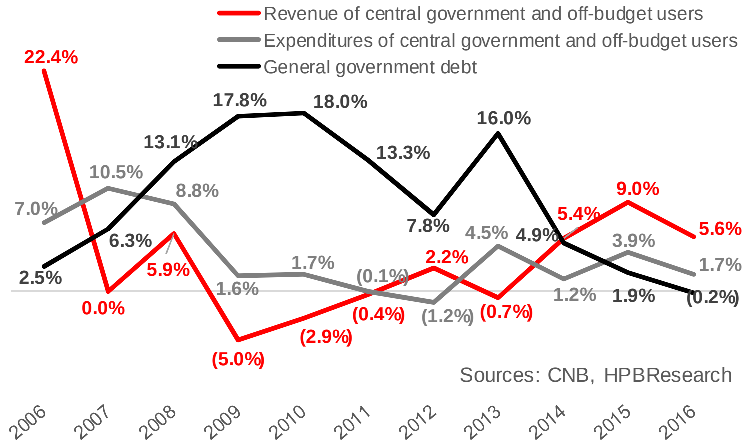


Current account of balance of payments as % GDP in the first 3 quarters of 2016 was 2.7 pp lower than in the same period of 2015 amid higher deficit in trading goods (+5.0%) and almost 4 times higher deficit of primary income (primarily due to increase in negative income from direct investments) which overshadowed 7.3% surplus in trading services (primarily tourism) and 4.0% surplus from secondary income.

Excellent Public Finance Movements

In 2016 revenue of central government and off-budget users were HRK135.8B which is 5.6% more than in previous year. The main reason for the better revenue is faster growth of economic activity which led to higher corporate profits in 2015 and consequently higher corporate tax in 2016. At the same time higher personal consumption and convenient tourist season led to increase in VAT and excise revenue.

Annual Changes in Public Finances



Expenditures of central government and off-budget users were HRK135.3B which is 1.7% more than in 2015. This increase was due to grants which include transfers to local government units among which for compensation of workers in elementary and high schools. At the end of 2016 an operating surplus of central government and off-budget users was recorded in the amount of HRK567.3M which is the best since 2008.

In 2016 part of the debt was refinanced although to lesser extent than in previous years which resulted with 2.5 pp better general government debt to GDP ratio of 84.2%. This points to a possible forming of a downward trend in general government debt.

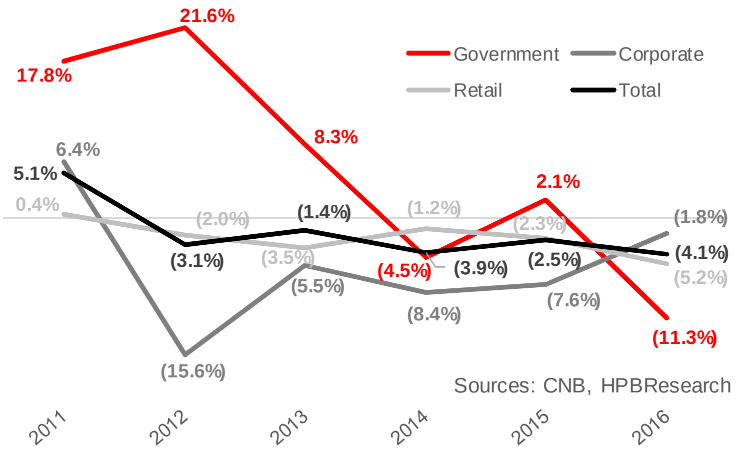
No Changes in Monetary Policy

In 2016 CNB continued its expansionary monetary policy with maintaining exchange rate stability and EUR/ HRK in its typical range of approximately 7.46-7.68 which is below +/ -1.5% fluctuation. Mid EUR/ HRK exchange rate of CNB at the end of 2016 was 7.558 which is 1.0% less than at the end of 2015. CNB continued to maintain bank liquidity through regular weekly reverse repo auctions with transactions of HRK9.0B in the whole year which is almost double the amount in 2015. In September repo rate was down by 3 bps to 0.47%, and in October by another 17bps to 0.3%. Together with regular repo transactions CNB carried 4 fine tuning operations (FX interventions) in which a total of EUR868.8M was bought from banks, and 4 structural repo operations with 4-year maturity where interest rate was lowered from 1.8% to 1.4%.

Bank Lending Decline Continues, Deposits Stagnate

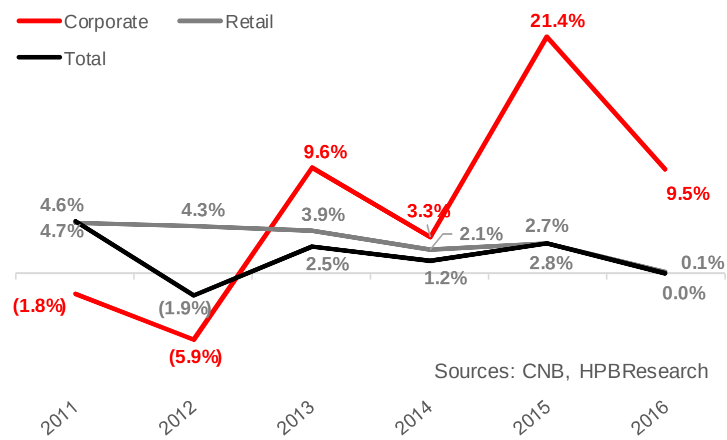
The total assets of banks (aggregated, credit institutions) at the end of 2016 were HRK396.3B which is 1.2% less than a year before. Decline was, as in previous years, a result of lower lending (-4.1%), while excess liquidity was placed in government bonds and liquid assets.

Annual Changes in Loans by Sectors



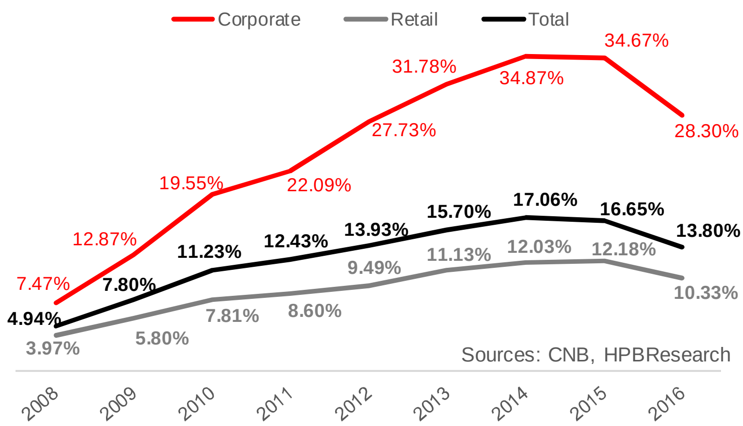
Government lending dropped substantially due to lower needs in taking bank loans by the Government. Decline in retail lending had accelerated due to continued deleveraging in spite of lower interest rates. Decline in corporate lending had slowed up substantially which points to slower deleveraging of companies after substantial bank credit receivables write-offs in previous years.

Annual Changes in Deposits by Sectors



Corporate deposits continued to increase amid higher transaction accounts due to better profitability and faster cash turnover. Retail deposits were almost unchanged, while deposits of financial institutions were down (-27.3%) which resulted with unchanged total deposits.

NPL Share by Sectors



Corporate NPL share was down due to write-offs and sale of bank credit receivables, and better corporate profitability. However NPL share of construction sector is still extremely high (65.7%).

Business Environment

Balance Sheet of Credit Institutions

Number of banks in Croatian market has been on a continuous decline amid discontinued business of small banks so currently there are 25 commcercial banks and one savings bank in Croatia with top 5 banks making ¾ of the market. One of characteristics of markets in Central and Eastern Europe is the foreign ownership of their banks with Croatia being no exception. 15 foreign owned banks hold 90.2% of the total assets, with domination of banks from the EU – Italian (largest Zagrebačka Banka is owned by Unicredit, while second largest Privredna Banka Zagreb is owned by Intesa Sanpaolo) and Austrian (third largest Erste & Steiermärkische, and fourth largest Raiffeisenbank).

HPB is one of the two remaining government owned banks, while the second being small Croatia Banka with assets share of only 0.8%. On December 31 2016 HPB was the seventh largest Croatian bank by assets, with the highest assets growth among top 10 banks in 2016.

Banking Sector – Overview of Selected Indicators 2014 – 2016

Assets, market share and capital adequacy							
HRK million		2014	2015	2016	YoY	Mkt Share	Capital Adequacy
1	Zagrebačka Banka	102,470	105,997	105,131	*(0.8%)*	*27.2%*	*26.1%*
2	Privredna Banka Zagreb	69,102	69,733	72,439	*3.9%*	*18.7%*	*22.5%*
3	Erste & Steiermärkische Bank	60,180	58,995	56,119	*(4.9%)*	*14.5%*	*21.6%*
4	Raiffeisenbank Austria	31,421	31,198	31,424	*0.7%*	*8.1%*	*22.2%*
5	Société Générale-Splitska Banka	28,765	27,067	27,066	*(0.0%)*	*7.0%*	*19.9%*
6	Addiko Bank	28,249	25,557	21,099	*(17.4%)*	*5.5%*	*29.9%*
7	**Hrvatska Poštanska Banka**	**17,370**	**17,713**	**19,358**	***9.3%***	***5.0%***	***15.7%***
	- total assets share		*4.5%*	*5.0%*			
8	OTP Banka Hrvatska	15,870	15,883	15,781	*(0.6%)*	*4.1%*	*15.6%*
9	Sberbank	10,266	9,736	9,266	*(4.8%)*	*2.4%*	*19.9%*
10	Kreditna Banka Zagreb	4,266	3,470	3,551	*(16.8%)*	*0.9%*	*17.3%*
	Top 10	**367,959**	**365,349**	**361,234**	***(1.1%)***	***93.4%***	***21.1%***
	Other banks (16)	27,279	28,045	25,537	*(8.9%)*	*6.6%*	*21.9%*
	Total	**395,238**	**393,394**	**386,771**	***(1.7%)***		***21.6%***

Source for sector: www.hnb.hr (audited business indicators of credit institutions on December 31 2014 and December 31 2015, unaudited business indicators on December 31 2016)
Source for HPB: audited BN form as per December 31 2016 (total sum corrected in line with the Bank's audited data)

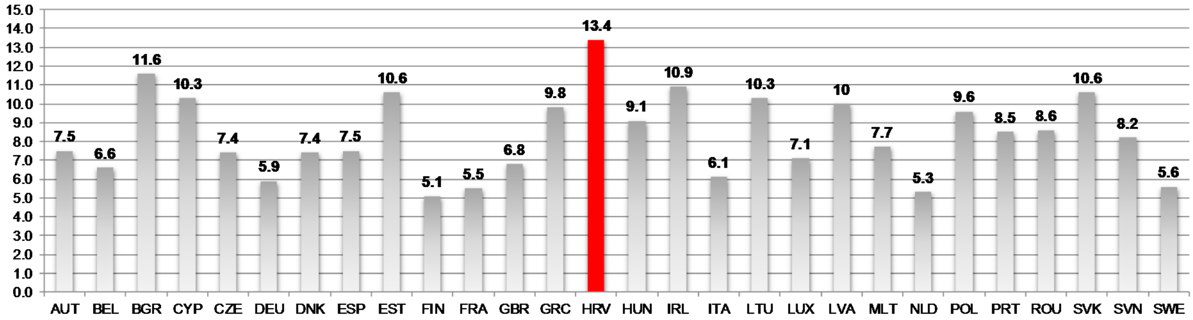
Total assets of Croatian banking sector was rising from 1999 to 2012 but from 2008 on the pace of growth was slowing due to financial crisis and economic downturn. Amid persistent negative market pressures and substantial rise in NPLs total assets were down in 2012 for the first time since 1999, and decline was continued in the following years. In 2016 declining trend was even more evident due to regulation on CHF loan conversion and nonexistent deposits growth, as opposed to previous years.

Banks continue to predominantly lend to households with retail loans making 45.1% of the total loans, while loans to nonfinancial companies make 28.3% and government loans 21.2% of total loans. NPLs currently make 13.8% of the total loans which is substantially higher than pre-crisis times but also somewhat lower than in previous years. Corporate NPL share is still quite high (28.3%). Lower loans in bank's balance sheets are a result of sale of receivables to nonbank financial institutions and specialists.

Retail and corporates also make the main source of bank's funding with 83.6% share in total deposits. Amid decline in interest rates deposits have been stagnant in line with systemic excess liquidity which cannot spill over to traditional placements like loans. As a result small banks are continuingly finding new ways for diversification of its placements and interest margin optimization which is primarily evident in increasing securities investments.

Historically Croatian banking sector has been one of the best capitalized in Europe in the last 10 years, while currently banks in Croatia have the lowest leverage among EU countries.

Capital to Assets Ratio of Banks in EU - 2016



Source: World Bank metadata, data.worldbank.org

Profitability of Credit Institutions

Despite balance sheet decline banks had made positive high rates of profit/ return until 2015 and had weathered the financial crisis relatively undamaged due to the regulator and monetary policy which required high levels of capital before the crisis.

After loss in 2015 due to conversion of CHF loans and write-offs banks continued with profitable business activity in 2016. Total pre-tax profit in 2016 was HRK6.4B, the largest in the history of Croatian banking system. Record pre-tax profit was made after HRK5.0B loss in 2015 amid substantial impairments and provisions primarily due to CHF loans.

Top 10 banks in 2016 made the record HRK6.5B pre-tax profit which is more than all 26 credit institutions combined.

Banking Sector Profitability 2014 – 2016

Pre-tax profit and ROA							
HRK million		**2014**	**2015**	**2016**	**2014**	**2015**	**2016**
1	Zagrebačka Banka	1,478	(662)	2,127	*1.4%*	-	*2.0%*
2	Privredna Banka Zagreb	821	208	1,982	*1.2%*	*0.3%*	*2.7%*
3	Erste & Steiermärkische Bank	266	(1,241)	830	*0.4%*	-	*1.5%*
4	Raiffeisenbank Austria	364	(311)	585	*1.2%*	-	*1.9%*
5	Société Générale-Splitska Banka	249	155	468	*0.9%*	*0.6%*	*1.7%*
6	Addiko Bank	(128)	(2,456)	79	-	-	*0.4%*
7	**Hrvatska Poštanska Banka**	**(637)**	**127**	**162**	**-**	***0.7%***	***0,8%***
	- total profit share	**-**	**-**	***2.8%***			
8	OTP Banka Hrvatska	13	(155)	155	*0.1%*	-	*1.0%*
9	Sberbank	42	(245)	70	*0.4%*	-	*0.8%*
10	Kreditna Banka Zagreb	(38)	9	17	-	*0.2%*	*0.5%*
	Top 10	**2,430**	**(4,572)**	**6,475**	***0.7%***	**-**	***1.8%***
	Other banks (16)	**(362)**	**(460)**	**(125)**	-	-	-
	Total	**2,068**	**(5,032)**	**6,350**	***0.5%***	**-**	***1.6%***

Source for sector: www.hnb.hr (audited business indicators of credit institutions on December 31 2014 and December 31 2015, unaudited business indicators on December 31 2016
Source for HPB: audited BN form on December 31 2016 (total sum corrected in line with the Bank's audited data)

Business Overview of Hrvatska Poštanska Banka p.l.c. and Subsidiaries

History and Development of Hrvatska Poštanska Banka p.l.c.

Foundation of Hrvatska Poštanska Banka p.l.c. in early 1990s is a result of a several-month dedicated work of group of enthusiasts and experts of Hrvatska Pošta i Telekomunikacije (hereafter: HPT). They used best work practices of post banks in Europe and newly created political environment to realize an idea of a post bank in independent Croatia.

HPB was founded in October 1991 with headquarters in Zagreb and first business address in 7 Tkalčićeva. HPB shares were subscribed by 50 founders/ shareholders, HPT's business partners, while HPT was the largest shareholder and had provided space and first human capital. As a „*universal banking organization*" HPB was registered in order to make „*all cash, deposit, credit and guarantee activities with corporates and all banking activities with population, also including payment activities*". The Bank was registered with the court's registry in early October 1991.

Due to retail and corporate needs for banking services, especially in local areas with no banks, the Bank had relied on around 1,100 HPT offices at the time where banking services were introduces including receiving retail deposits, corporate deposits – HPT-business partners. The Bank's first clients were HPT workers which received their paychecks in a form of savings books.

In May 1992 HPB started with FX payments and had received first FX deposits. During the year the Bank's advantages had started to be noticed by smaller private entrepreneurs which had started to get involved into HPB's deposit's sphere.

By *Statute on Collecting Debts, i.e. Receivables of Poštanska Štedionica Beograd – Croatian subsidiary, Zagreb* (March 25 1992, Official Gazette 15/ 92 HPB was named as legal successor of the mentioned subsidiary which made a substantial contribution to forming HPB's potential and activities (exchanging savings books and current accounts, taking savers and depositors, collecting receivables).

HPB's first years were marked by the war, decline in total economic and investment activities in Croatia, decline in living standard, high inflation (even hyperinflation), monetary indiscipline, higher fiscal expenditures which ended by the Stability program in May 1995 with ending inflationary pressures and stabilization of DEM/ HRK exchange rate. HPB was doing mostly retail business at the time by receiving HRD (dinar) and HRK retail savings, paying wages and pensions and placing excess liquidity on money markets, while making short-term lending to corporates supporting their working capital mostly HPT and its business partners and founders of HPB. Amid the highly complex working conditions HPB managed to record a constant balance sheet growth and profit, and was taking constant care about revaluation and maintaining founder's equity and clients' deposits.

In 1995 HPB bought a building in 4 Jurišićeva, the location of its headquarters today. The same year the Bank's acts were aligned with the Companies Act.

More than 10 years after its foundation up until opening an outlet in Split (March 2003) the Bank's solely outlets were in Zagreb, first in Praška and Kralja Držislava (from June 1995 to December 1999) and then 4 Jurišićeva. In July 2005 HPB founded a real estate company HPB Nekretnine and an asset management company HPB Invest. This formed the HPB Group which was expanded in 2006 by foundation of a residential savings bank HPB Stambena Štedionica. HPB as a parent company in the Group is also a 100% owner of all 3 companies. From July 29 2015 the Group also includes a telecommunication company H1 Telekom plc.

The Bank increased its equity by HRK550M through public share offering in September 2015. Pension funds, investment funds and other private investors have subscribed shares in the total amount of HRK305.9M which gave them 25.5% ownership stake.

At the same time the Republic of Croatia subscribed shares in the total amount of HRK244.1M and its ownership stake fell from 99% to 74.5%. This gives HPB the most diversified shareholders' structure among large banks in Croatia.

HPB's network today is comprised of 10 regional corporate centers (2 in Zagreb, Split, Dubrovnik, Pula, Varaždin, Osijek, Rijeka, Čakovec and Zadar), 45 outlets and 7 detached tellers in the whole country.

Market position and competition profile enables HPB to be the only bank in Croatia to offer basic financial services to households in the whole country, comprehensive financial services to the government and support to the economy, especially in the SME segment. In cooperation with Hrvatska Pošta, products and services are available through the post office network in all significant places in the country.

As the largest domestically owned bank HPB is strategically focused on the retail business activities in the whole country, as well as support of the national economic development, especially in the SME segment. Strategic determinants of the HPB's development are focused on increasing market share and development of organization and business processes in line with the best practices. HPB has been focused on implementing new attractive retail products and services with special emphasis on creation and innovation of offers adjusted to the SME needs.

Business Activity of Hrvatska Poštanska Banka

The Bank offers all banking and financial services with the main focus on retail and corporates, among which:

- all types of deposit and credit products and services for corporates and retail in domestic and foreign currency,
- transaction services (HRK and FX payments),
- issuing guarantees, avals and similar products,
- factoring, financial lease services,
- securities services,
- other banking products and services (safes, Western Union services).

Regulatory Framework

Conditions for the Bank's founding and business as a credit institution in the Republic of Croatia are regulated by the Credit Institutions Act (Official Gazette 159/ 2013, 19/ 2015, 102/ 2015) and the Companies Act (Official Gazette 152/ 2011, 111/ 2012, 68/ 2013 and 110/ 2015).

Offering of investment services and investment activities in the Republic of Croatia are regulated by the Capital Market Act (Official Gazette 88/ 2008, 146/ 2008, 74/ 2009, 54/ 2013, 159/ 2013, 18/ 2015 and 110/ 2015), and payment services offered by the Bank are regulated by the Payments Act (Official Gazette 133/ 2009 and 136/ 2012) together with certain by-laws. The Bank's core business is also regulated by the Croatian National Bank's by-laws.

Croatian National Bank is the top regulator which supervises credit institutions, while Croatian Financial Services Supervisory Agency supervises investment services and activities, together with supplementary services. State Agency for Deposit Insurance and Bank Resolution controls credit institutions in order for them to meet all the conditions of the Deposit Insurance Act (Official Gazette, 88/ 2015). In cooperation with the Croatian National Bank it sets procedures and instruments for credit institution resolution as regulated by the Credit and Investment Companies Resolution Act (Official Gazette 19/ 2015).

Considering the Republic of Croatia directly or through other government owned companies control majority of the Bank's shares, the Bank's business is also regulated by the special regulation for companies with majority government stake.

The Bank uses the EU regulation which includes regulations adopted by the Parliament and the Council. The most important is Regulation (EU) 575/ 2013 of the European Parliament and of the Council of June 26 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) 648/ 2012 (Official Journal of the European Union L 176/ 2013). There are also delegated and implementing regulations of the European Commission which concern conducting business of credit institutions in Croatia, as well as other relevant acts which regulate corporate business activities in the Republic of Croatia, and corporates and credit institutions with headquarters in Croatia in part in which they conduct business with foreign entities (e.g. acts of other countries, international contracts related to anti-money laundry, international payments etc.).

Considering the Republic of Croatia directly or through other government owned companies control majority of the Bank's shares, the Bank's business is also regulated by the special regulation for companies with majority government stake.

Overview of HPB Group and the Bank's Position in the Group

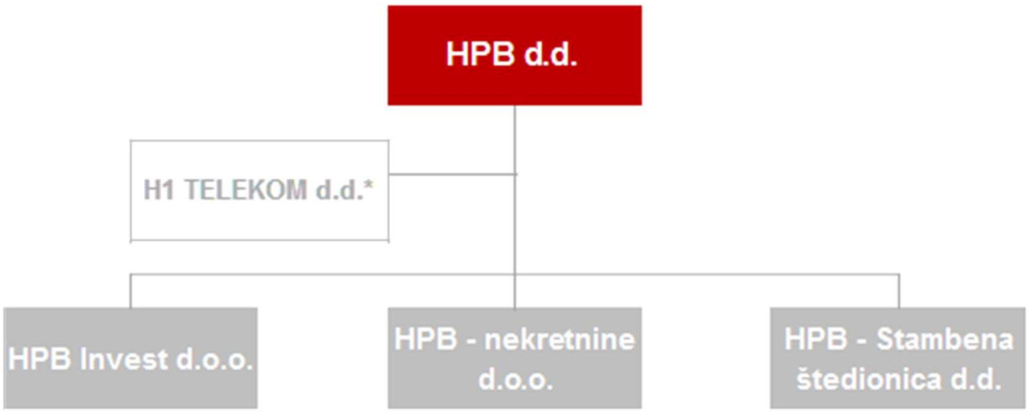
and is 100% owner of the following companies which make HPB Group:

- HPB Invest Ltd for managing investment funds, headquartered in Zagreb, Croatia
- HPB Nekretinine d.o.o. for real estate construction and sales, headquartered in Zagreb, Croatia
- HPB Stambena Štedionica d.d. for home savings, headquartered in Zagreb, Croatia

Together with the aforementioned companies, the Group is also comprised of the following company with 58.2% ownership stake by HPB from July 29 2015:

- H1 Telekom plc. for telecommunication services, headquartered in Split, Croatia

HPB Group's Structure



**HPB acquired the ownership stake in H1 TELEKOM by debt to equity swap. HPB will continue to compensate its investment primarily through sale, and not by exercising its controlling rights. Therefore this investment is classified as assets available for sale in accordance with the IFRS 5.*

Ownership Structure of Hrvatska Poštanska Banka p.l.c.

On December 31 2016 the Bank's ownership structure was as follows:

Shareholder	Ownership Stake
Republic of Croatia (Ministry of Government Assets)	42.43%
HP Hrvatska Pošta dd	11.93%
State Agency for Deposit Insurance and Bank Resolution	8.98%
Croatian Pension Insurance Institute (Ministry of Government Assets)	8.76%
Prosperus Invest d.o.o. for Prosperus Economic Development Fund	4.94%
PBZ CROATIA OSIGURANJE Mandatory Pension Fund (B Category)	4.12%
ERSTE d.o.o. for ERSTE PLAVI Mandatory Pension Fund (B Category)	3.90%
Allianz ZB d.o.o. for AZ Mandatory Pension Fund (B Category)	2.88%
CROATIA Osiguranje d.d.	2.47%
RAIFFEISEN D.D. for Raiffeisen Mandatory Pension Fund (B Category)	2.42%
NEK Fund	2.36%
Minorities	4.77%
Own shares	0.04%

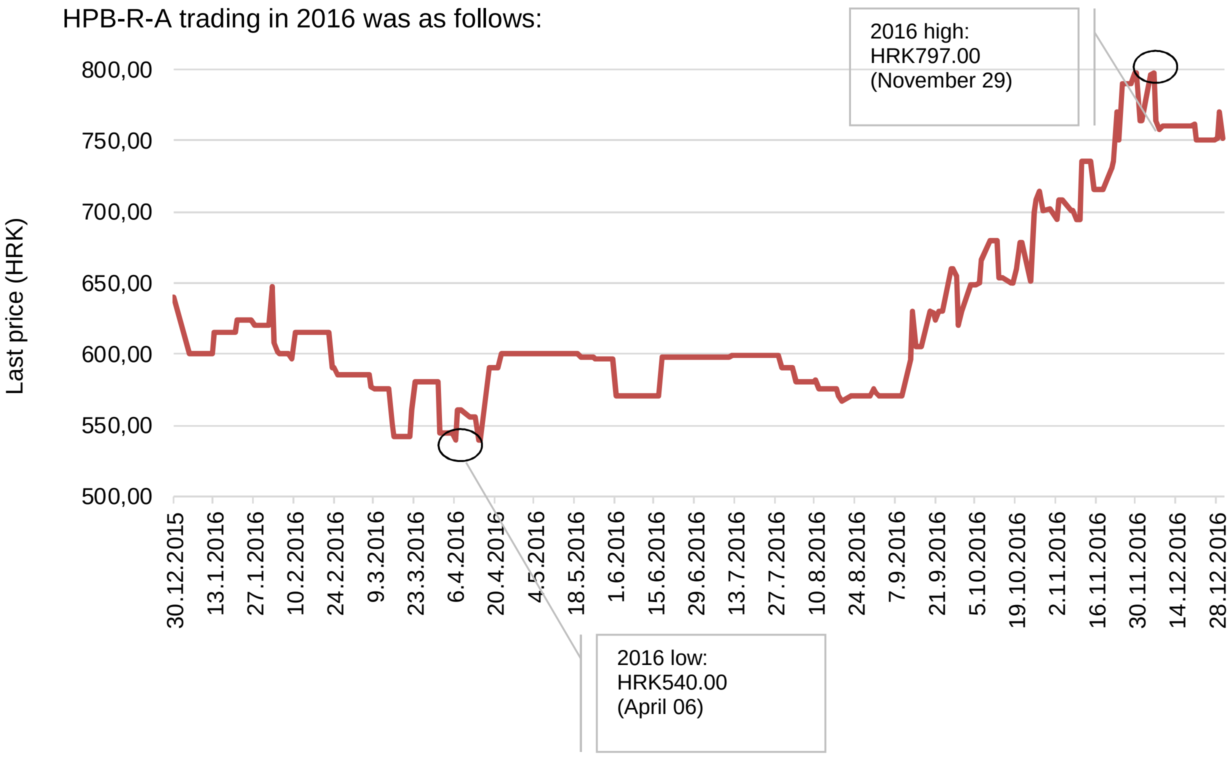
Source: Central Depository and Clearing Company

On December 31 2016 The Republic of Croatia through the Ministry of Government Assets and other government institutions controlled 74.5% of the equity and voting rights of the Bank.

HPB-R-A Share

HPB-R-A shares are listed on the ZSE Official Market. The last price per share at the end of 2016 was HRK751.00 (trading date December 30 2016) which is 17.3% more than at the end of 2015 (=HRK640.00 on December 30 2015).

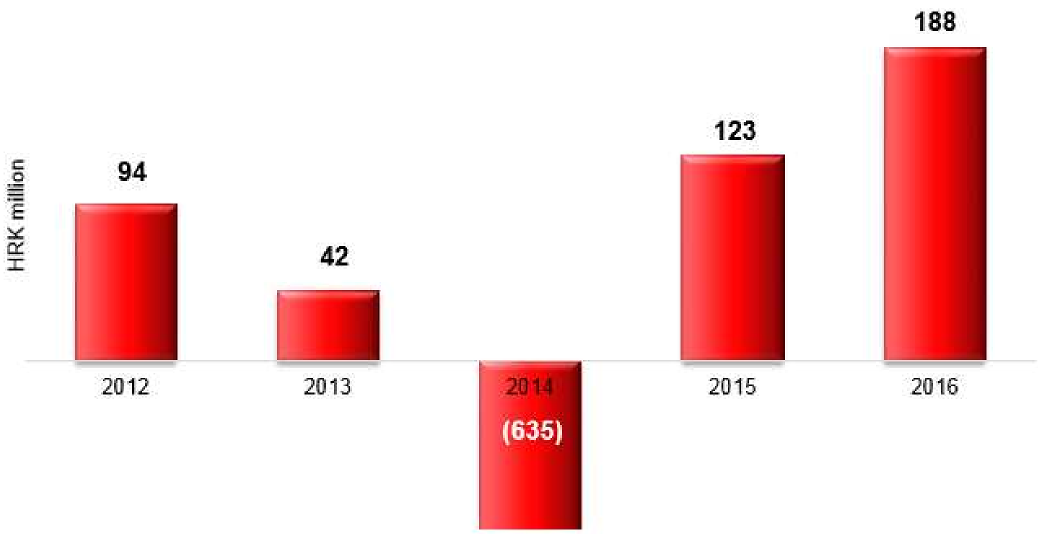
HPB-R-A trading in 2016 was as follows:



Business and Financial Overview

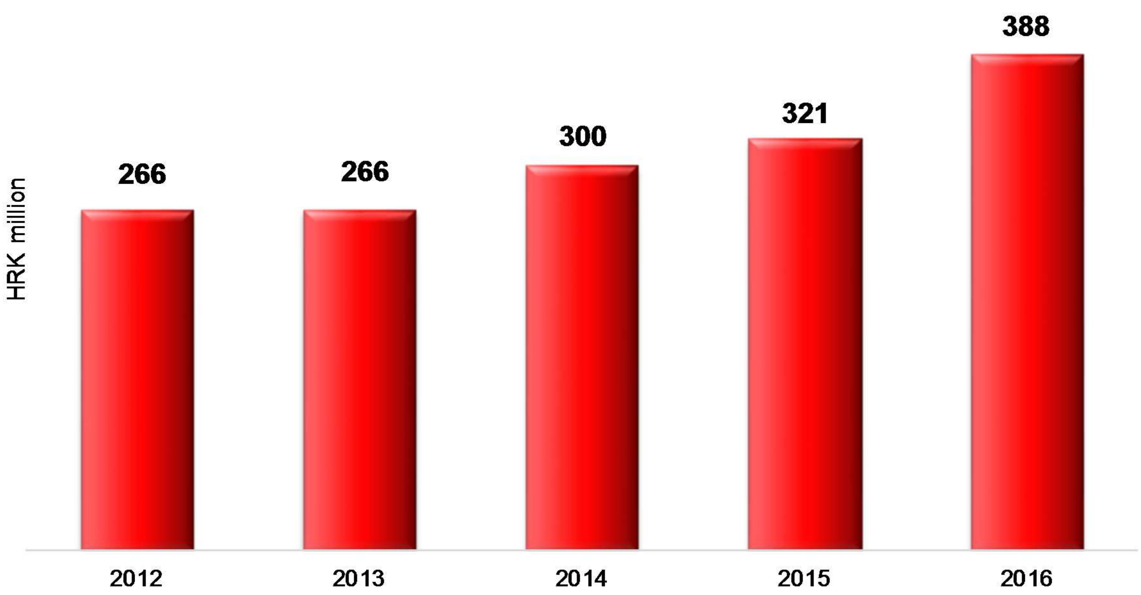
In 2016 the Bank made net profit in the amount of HRK188.3M, the best in the history.

Net Profit/ (Loss)



The Bank also made a record operating profit before provisions in the amount of HRK387.7M. Provisions for Loan Losses and Other Impairments of Financial and Non-Financial Assets were HRK200.6M, while Provisions for Liabilities and Costs were HRK25.4M.

Operating Profit Before Provisions

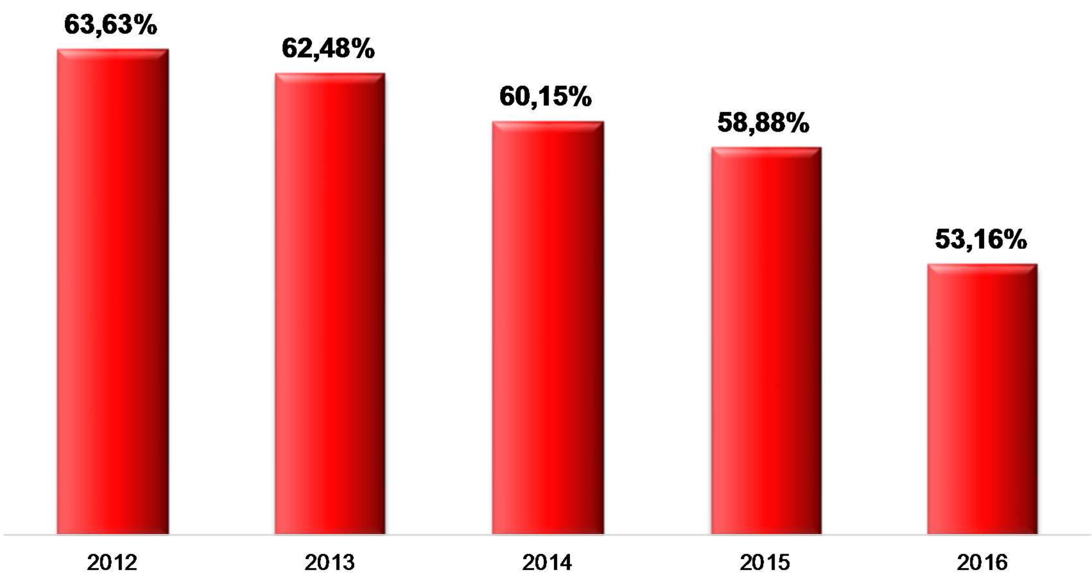


Total net operating income was up by 6.0%. Net Interest Income in the amount of HRK514.4M generated 62.1% of the total operating income.

Net Income Structure for a Period January 1 – December 31 2016

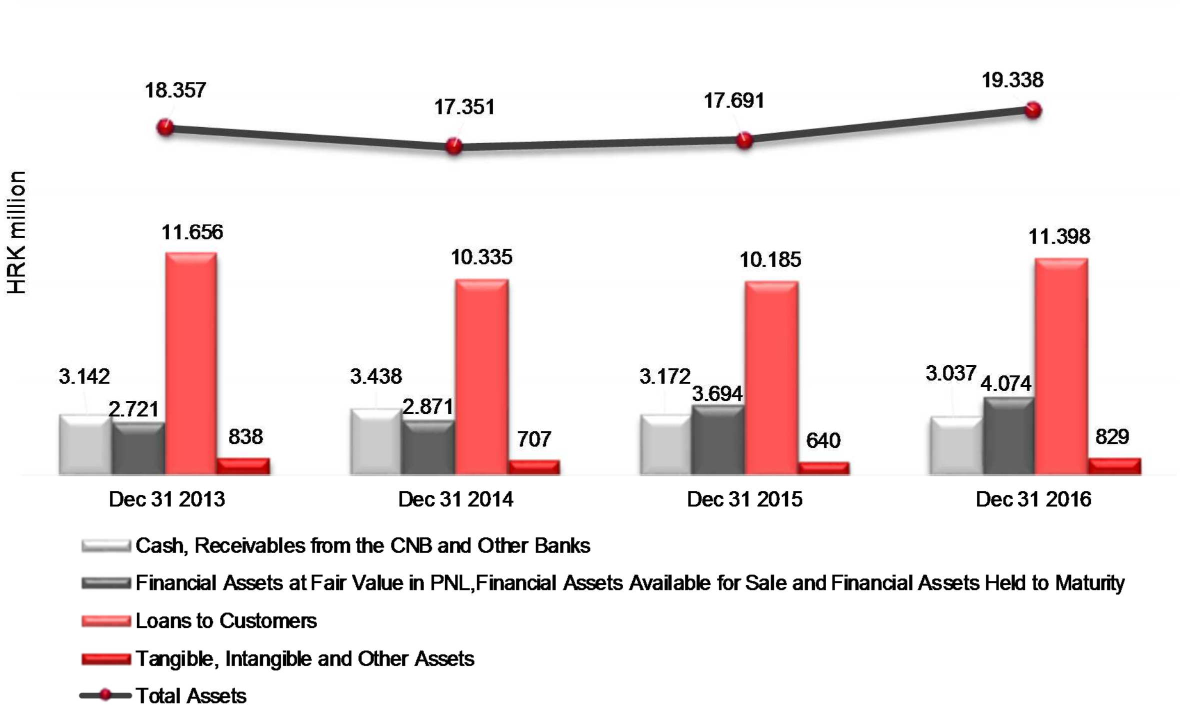
Processes in 2015 (reorganization and capital increase), as well as continued business rationalization in 2016 combined with better net operating income resulted with improved business efficiency which lowered the C/ I indicator by 5.7 pp to 53.2%.

Cost to Operating Income Ratio (C/ I Indicator)



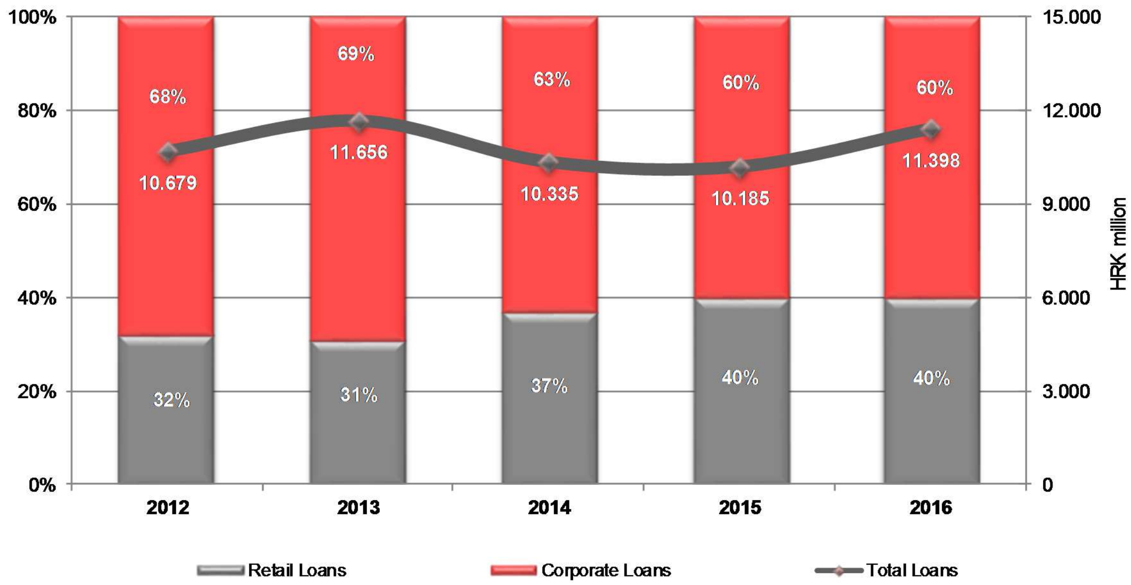
At the end of 2016 the Bank's assets were HRK19,338M which is HRK1,647M (+9.3%) more than at the end of 2015. Loans to Customers make the majority of the assets (58.9%). Share of the mandatory reserves at the CNB, loans to other banks and other cash is 15.7%, followed by financial assets available for sale with 14.2% share.

Movements and Assets Structure



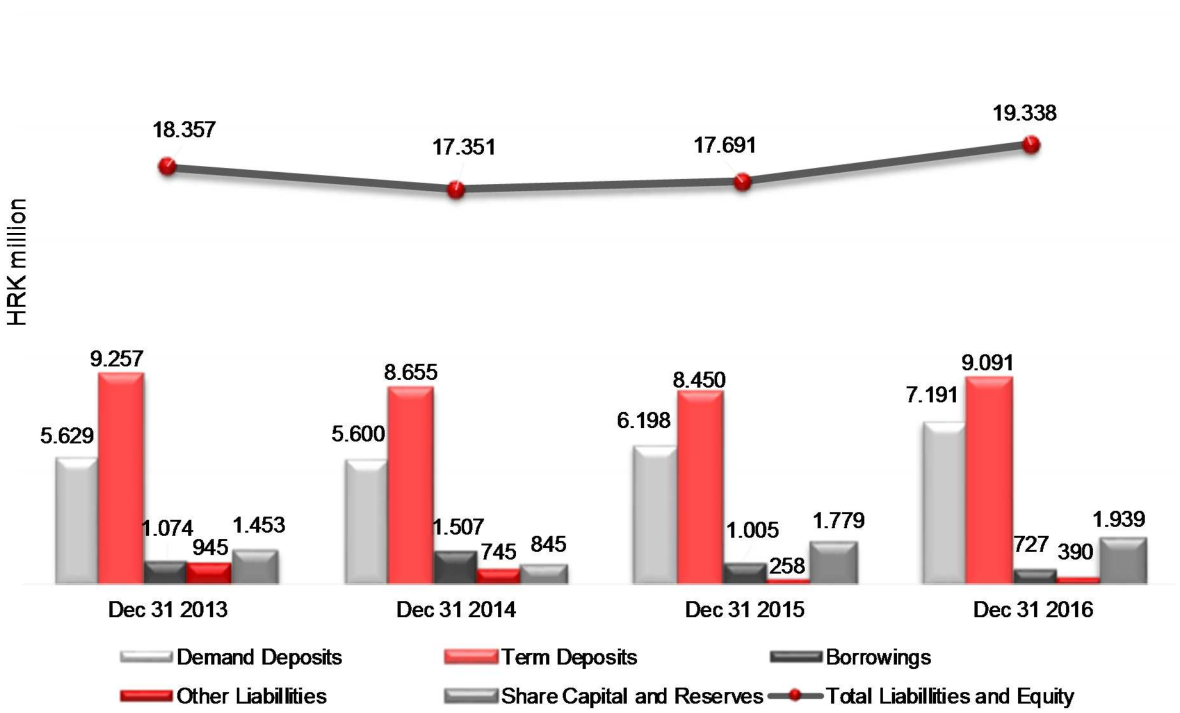
Total net loans were HRK11,398M and are HRK1,213M higher than in 2015. On the structure front, corporate loans make 60.3%, while retail loans make 39.7%.

Movements and Loan Structure



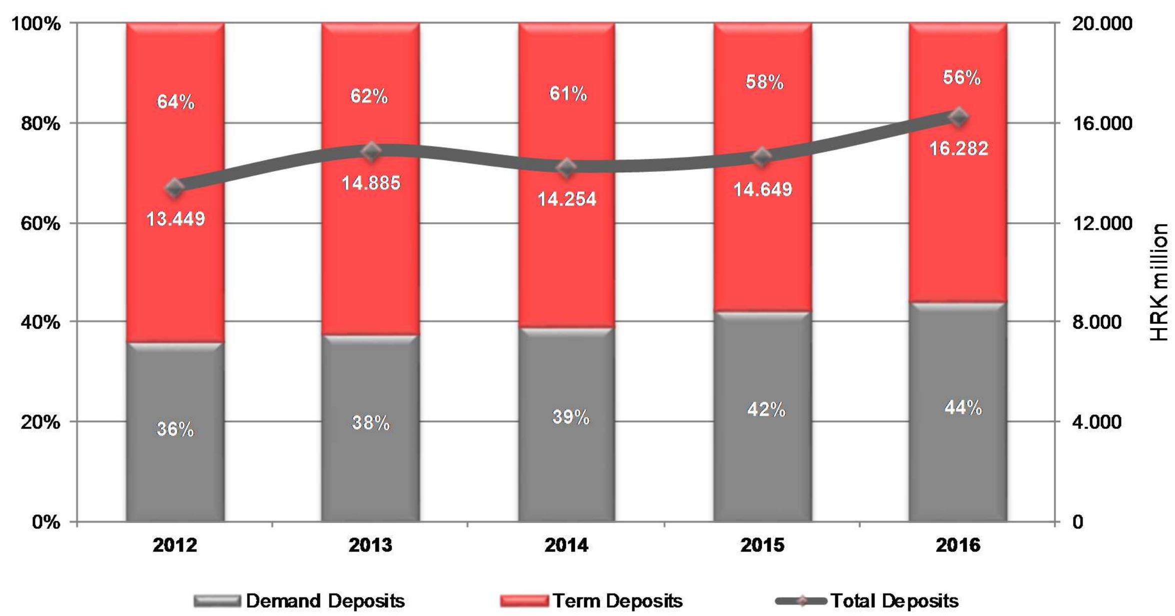
Term deposits make the largest share of the Bank's liabilities (47.0%). In 2016 demand deposits increased their share by 2.2 pp to 37.2%.

Movements and Structure of Liabilities



During 2016 client's deposits were up by 10.4% (HRK1,1481.6M) compared to the previous year. Total deposits growth (including banks' deposits) was HRK1,633.1M or 11.1%.

Movements and Structure of Deposits



Despite being dominant in the total deposits' structure, term deposits' share was down by 1.85 pp to 55.8%. Due to the 2016 growth, demand deposits' share was up from 42.3% to 44.2%.

Retail Business

Retail business is done through the Bank's own network of 8 regional centers, 45 outlets and 7 detached tellers, as well as HP's distribution channel with more than 1,000 post offices scattered across the Republic of Croatia.

In 2016 the Bank has improved its sales network by moving certain outlets to more convenient locations, opening of a new outlet in Zagreb and redecoration of several other outlets. At the same time the Bank has continued to develop and improve its direct banking distribution channel by implementing online account opening, online loan applications and introducing 35 new ATMs. At the end of 2016 the Bank had a network of 402 ATMs and 2,097 EFTPOS terminals.

The Bank has continued cooperation with its strategic partner Hrvatska Pošta and had introduced loan services in post offices. Also the Bank improved its cooperation with Croatia Osiguranje with record sale of insurance policies.

In 2016 25K new clients were acquired. The Bank made remarkable results by selling 164K products and opening more than 33K new accounts which resulted with 9% higher retail and card business revenue.

Retail deposits make 55.8% of total deposits. In 2016 they were up by 4.7% to HRK9.1B at the end of 2016. Demand deposits were HRK2.9B (+21.9%), while term deposits were HRK6.1B (-2.0%). Deposits growth is a result of quality services, customers' loyalty, excellent marketing and recognizing the Bank as a safe financial factor in Croatian banking system.

Total gross retail loan portfolio at the end of 2016 was HRK4.8B. In late 2016 the Bank sold an NPL portfolio in the amount of HRK4.8B. Retail loans make 37.5% of the total gross loans to customers. Multi-purpose loans make the majority of retail loans, while share of housing loans was on the rise. In 2016 the Bank issued almost HRK1.3B of new retail credit volume with housing loans up by HRK588M. This result was achieved by excellent offer of housing loans, especially fixed-rate HRK.

These results were achieved mainly by contribution of the sales staff, loyalty of existing and acquisition of new clients, quality of services, improved intra-sector cooperation and improved support.

Regular monitoring of the market, competition and new trends enables the Bank to introduce new products which differentiate it among competitors and supports its high competitiveness. In 2016 HPB created the SuperSmart account which enables account opening without going to a bank, the first of its kind in Croatia. It is possible to make online loan applications which enables the Bank to communicate with clients in a modern way. In early 2016 the Bank introduced preapproved loans. It will continue to develop its products to suit the clients' needs which are the Bank's top priority.

In mid-2016 the Bank implemented a new CRM system which greatly improved its management of clients' relationship. The new system enabled unification, monitoring and management of clients' interaction. Besides a number of marketing campaigns, new customer campaigns were introduced. The Bank has actively worked to increase the clients' satisfaction. Based on the CRM's clients' info, the Bank offered a special products to highly valuable clients. A new internal risk assessment system was introduced which enables far better assessments of clients' ratings. Payments system was adjusted to SEPA.

Overview of Retail Products and Services

	Product Group	Products and Services
Retail Products and Services	Accounts	Current Account
		Giro-Account
		FX Account
		Kids' Account
		Escrow Account
		SuperSmart HPB Account
	Savings	Demand Deposit
		Motiv Plus Savings
		Term HRK Savings
		Term FX Savings
		Term Savings with Multiple Deposits
		Kids' Savings (HPB Kockica)
		Annuity Savings
	Loans	**Housing Loans**
		HRK Housing Loans with Fixed and Variable Rate - Refinancing
		HRK Housing Loans with Fixed and Variable Rate
		EUR Linked Loans with Fixed and Variable Rate
		HRK Green Housing Loans
		EUR Linked Green Housing Loans
		HRK Housing Loans
		EUR Linked Housing Loans
		Supportive Housing + Housing Loans
		Supporting Housing Housing Loans (Program A)
		Purpose Loans
		Loans for Real Estate Legalization
		Loans for Tourist Season Preparation
		Loans for Paying Liabilities
		Loans for Paying Overdrafts
		Student Scholarship Loans
		Student Loans for Knowledge, Sport and Travel
		Purpose loans for Supporting Housing
		Consumer Loans Bontech d.o.o.
		Multipurpose Loans
		HRK Multipurpose Cash Loans
		EUR Linked Multipurpose Cash Loans
		HRK Multipurpose Loans with Fixed and Variable Rate
		HRK Multipurpose Loans for Pensioners
		EUR Linked Multipurpose Loans for Pensioners
		HPB Fixation Loans
		Lombard Loans Secured by Residential Savings in HPB Stambena Štedionica
		Lombard Loans Secured by Term Deposits
		Multipurpose Mortgage Loans
	Cards	Debit MasterCard Contactless Card
		Pošta & HPB MasterCard
		Maestro Current Account Card
		Maestro Giro-Account Card
		VISA Electron Current Account Card
		VISA Prepaid Card
		VISA Prepaid Card for Young People
		VISA Installment Card
		Credit MasterCard (revolving)
		Credit MasterCard (charge)
		Gold Credit MasterCard

Product Group	Products and Services
E-Banking	Internet Banking
	mBanking
	Text/ E-mail Service
	e-Građani
	eRačun
Other	HPB Kombinacija
	Dynamic FX Conversion at ATMs
	HPB Services in HP and FINA
	Safes
	Standing Orders
	Western Union

Corporate Business

Corporate Division offers banking services to around 8,700 clients and is thriving for constant improvement of its services with innovation in order to satisfy all the clients' needs.

2016 is characterized by a strong market growth in all segments of corporate business.

Gross corporate loans were up by 3.3% to HRK8.0B at the end of 2016 compared to the previous year. At the same time HRK0.7B of gross principal of matured uncollected loans were reclassified as assets available for sale. Largest part of the corporate loans make loans to companies and government funds, while HPB continues to support companies and sectors which create value for the national economy.

Total corporate deposits (excluding banks) on December 31 2016 were HRK6.7B. Demand deposits were up by 9.8%, while term deposits jumped 39.3% compared to 2015. This increase in deposits is a result of substantial acquisition of local governments, SMEs and large companies.

In 2016 the Bank faced many challenges in a form of general interest rates decline which was compensated by quality measures in managing loan volumes and deposit interest expenses.

Successful cooperation with CBRD and HAMAG-BICRO has been continued. In 2016 the Bank started cooperation with Croatia Osiguranje which includes sales of insurance policies to small companies with up to 20 employees with average premium of HRK2,200. Also new corporate products were designed in cooperation with Crafts Association of the City of Zagreb and Croatian Bar Association. Loans for co-owners of residential buildings were redesigned and development of agricultural short term and long term lines was approved.

The Bank will maintain intensive cooperation and credit support to corporates, government units including local government with emphasis on the SME growth in order to adjust to the market movements. Focus will be on increasing noninterest income with continued improvement of quality and extension of services.

The Bank is preparing new products for corporates including group of products, tourist loans, new credit lines in cooperation with the EBRD for SME lending, woman entrepreneur and improvement of energy efficiency, creating products for subsegments in cooperation with an association of dentists, pharmacists, association of accountants and corporate mobile banking.

Overview of Corporate Products and Services

	Product Group	Products and Services
Corporate Products and Services	Payments	Transaction Account
		Cash Payments
		Noncash Payments
		Reports on Account Balance and Changes
		Solvency Data (BON2)
		EUR Payment Orders (SEPA)
		International Payment Orders
	Short-term Financing	Loans for Working Capital (Liquidity Improvement)
		Loans for Working Capital Secured by Receivables from Prudential Companies
		Revolving Loans
		Discount of Promissory Notes by Prudential Companies
		Allowed Overdraft of Corporate Accounts
		Loans for Preparing Tourist Season
		Loans for Financing Stocks of Sugar, Wheat and Other Commodities
	Long-term Financing	Export Financing Loans
		Loans for Co-owners of Residential Buildings
		Loans for Permanent Working Capital
		Loans for Buying Equipment and Machinery
		Loans for Buying, Constructing, Reconstructing or Decorating Commercial Space
		Loans for Financing Residential Construction
		AGRO Corporate Loans
		Loans for Tourist Development
		Green Loans for Entrepreneurs
		Offer for Exporters
	Special Loan Arrangements	Loans in Cooperation with HAMAG-BICRO
		Credit Lines from CBRD pool
		Loans in Cooperation with the Association of crafts of the City of Zagreb
		Credit Lines for Member of the Croatian Bar Association
		Loans in Cooperation with MINPO, City of Zagreb and Counties-Measure 1
	Deposits	HRK and FX Multipurpose Deposits
		HRK and FX Purpose Deposits
		HRK and FX Demand Deposits
	Guarantees	Performance Guarantees
		Bid Guarantees
		Other Performance Guarantees
		Guarantees for Repairs in Guarantee Period
		Payment Guarantees
		Tariff Guarantees
		Guarantees for Repaying Advance Payments
		FX Guarantees
		Counterguarantees and Superguarantees
	Letters of Credit	Loro Letters of Credit
		Nostro Letters of Credit
		Documentary Collections
		Stand by Letters of Credit
	Cards	VISA Business Electron
		VISA Bonus Plus
		VISA Prepaid Business Card
		VISA Business
	E-Banking	mHPB
		mToken
		Internet Banking
		Text/ E-mail Services
	Other	Cash Pooling
		E-commerce

Financial Markets

Treasury

The most part of 2016 was market by high global markets liquidity due to quantitative easing of the world's most important central banks. In late 2016 expectations about significant rate hikes in the US in 2017 have risen sharply. The global liquidity spilled over to domestic market and the Bank concentrated to optimizing excess liquidity primarily by investments in domestically listed bonds.

In accordance with the new liquidity risk management regulation the Bank has actively managed the liquidity reserves by combining fixed-income, open-end investment funds and deposits investments.

The Bank is still one of the most significant players in domestic money markets with the most significant activities in periods of short-term seasonal volatility mostly on the excess liquidity front. Due to high liquidity the Bank did not participate in regular repo auctions organized by the CNB, nor in structural repo operations introduced in 2016, and had successfully maintained regulatory coefficients and liquidity ratios.

FX trading and exchange rate differences were excellent in 2016 despite the trading being under effect of narrower spreads. Risk product sales and FX trading has increased in the activity due to cooperation with corporates by arranging spot and forward FX transactions.

On the cash business front the Bank remains one of the most significant players. With wide network of outlets and authorized money exchange offices of the Bank, and in cooperation with FINA cash services the Bank offers competitive trading and cash supply service.

Investment Banking

The Bank offers brokerage services for domestic, regional and global financial instruments with a possibility of electronic trading and placing orders. Domestic and regional turnover had risen up a bit in 2016 due to revived optimism. Similar volume growth is recorded by the Bank on the brokerage and asset management front.

The Bank still regularly participates as one of the arrangers in bond issuances by the Republic of Croatia as was the case in 2016.

On the custody and pension and investment fund depositors front the Bank has continued to improve and harmonize services with a number of regulation requirements. Custody and depositors assets had increased in 2016.

Financial Market Products and Services

	Products	Description
Financial Markets Products and Services	Domestic Trading	Trading in domestic financial instruments Clients decide which stocks they will buy or sell and at which prices, as well as what will the structure of their look like Brokers are obliged to acquaint a client with potential risks, current stock price, specifics of each market, movements of certain stocks and to recommend a portfolio diversification
	Regional Trading	Trading in financial instruments in Montenegro, Serbia, Macedonia and Bosnia and Herzegovina Clients decide which stocks they will buy or sell and at which prices, as well as what will the structure of their look like Brokers are obliged to acquaint a client with potential risks, current stock price, specifics of each market, movements of certain stocks and to recommend a portfolio diversification
	Global Trading	Trading in leading global financial instruments Clients decide which stocks they will buy or sell and at which prices, as well as what will the structure of their look like Brokers are obliged to acquaint a client with potential risks, current stock price, specifics of each market, movements of certain stocks and to recommend a portfolio diversification
	Portfolio Management	Specialized service for clients which entrust its funds to the Bank Aimed at clients which in line with its own goals and limits want to invest in securities and other financial instruments with maturity over 1 year to earn extra returns Clients receive reports on changes of securities and balance funds in their portfolio each month or more often if necessary
	Investment Services	Investment advising and advising on equity structure, business strategy and similar, and advising on mergers and acquisitions, together with other investment banking services
	Securities Issuance	Issuance of the following financial instruments: a) debt – short-term (commercial bills) and long-term (bonds) b) equity - stocks The Bank offers services which cover the whole issuance process, i.e. include all activities related to organizing, preparing, subscription and payments of securities, together with other related activities in order to achieve successful issues

	Products	Description
Financial Markets Products and Services	Securities Custody	Primarily safeguarding assets, transactions settlement and corporate actions Custody users are active capital market participants including investment and pension funds and other institutional investors, as well as natural and legal persons which make financial investments Custody services: safeguarding assets, transaction settlement by client's order, asset valuation, corporate actions reporting, collecting revenue from financial instruments and reporting, representation at annual shareholders' meetings, reports on regulatory changes
	Depositor of UCITS/ AIF Investment or Pension Fund	Depositor is a credit institution headquartered in Croatia or a subsidiary from other EU member authorized by the CNB (or the regulator in domestic market) for safeguarding and administrating financial instruments on behalf of clients including custody and related services, which conducts fund's supervision, monitors funds' cash flow and safeguards funds' assets. Depositor takes care of funds' assets accounts and divides a fund's assets from other assets of other funds, depositors and other clients, and management company, ensures assets are invested in accordance with the regulation, reports to the regulator on fund's valuation, performs transactions for management company, reports on corporate actions, offers voting services at shareholders' meetings, takes funds' payments and insures all revenue is used in accordance with the regulation
	Moj broker - Web Trader	Moj broker – Web Trader enables securities trading and monitoring portfolio balance via Internet with no dependence on brokerage working hours Options are to place, change or cancel orders on ZSE, check portfolio balance, check brokerage account balance and turnover, check stock prices on ZSE with 50 best bids and offers in real time. All dana exchange is secured.
	Short-term HRK loans for Buying Financial Instruments (Margin Loans)	Loans for individuals and corporate with purpose of buying financial instruments included in the list of eligible financial instruments for margin loans in accordance with daily investment limits for each financial instrument Maturity up to 12 months Loans of up to 100% of collateral, minimum HRK50K and up to HRK2M
	Spot FX Buy/ Sell	Users are domestic and foreign individuals, corporates and financial institutions Purposes include FX buying or selling for international payments, FX deposits and FX conversion
	Forward FX Buy/ Sell	Users are domestic and foreign corporates and financial institutions Purposes include buying or selling FX at fixed rate on certain date which is at least T+3, FX buying or selling for international payments, FX deposits and FX conversion

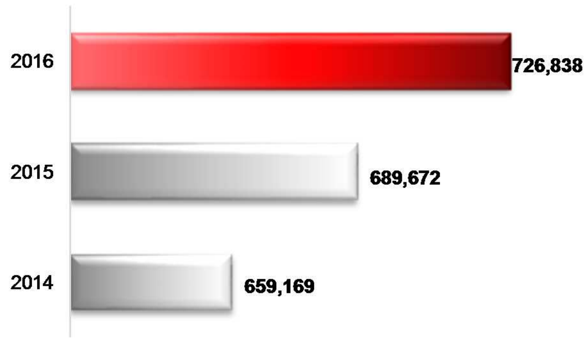
	Products	Description
Financial Markets Products and Services	FX Swap	Users are domestic and foreign corporates and financial institution Includes simultaneous FX buy and sell at fixed rates (spot and forward buy and sell transaction) where 2 currencies are swapped until maturity when they swapped again
	Cash Trading	The Bank's cash management where stocks of FX and HRK cash are maintained at optimal levels
	Given Deposits	Users are banks Purpose is short-term financing Maturities up to 12 months or more if necessary Available from payments to maturity
	Received Deposits	Users are domestic and foreign banks and financial institutions Purpose is to make returns on available HRK or FX Maturities are fixed mostly up to 12 months Not available during deposits term Early termination possible if contracted previously with financial institutions
	Repo/ Reverse Repo	Users are domestic corporates and financial institutions One side transfers a security to the other in exchange of cash flow. At the same time a reverse transaction on a fixed date is contracted. Contract includes 2 transactions – 1 buy and 1 sell of the security at fixed price. It is lending securities from one and lending cash flow from the other side. All risks and benefits of holding security remain with the original owner. Reverse repo includes 2 reverse transaction compared with original repo.
	Securities Trading (Bonds, Treasuries, CNB Bills, Commercial Bills, Stocks)	Users are domestic corporates and financial institutions Purpose is investing free cash in fixed-income securities issued by the government, local governments or corporates Maturities include short-term securities (up to 1 year) and long-term securities (more than 1 year)

Direct Banking Operations

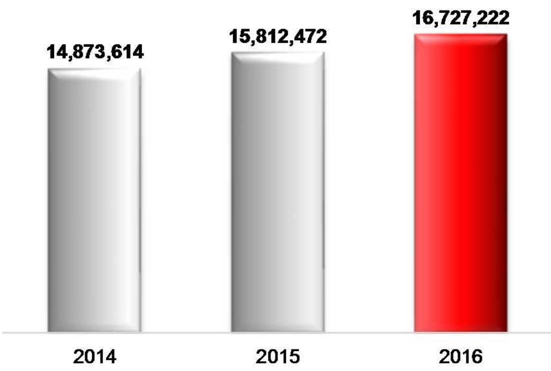
a) Card Business

At the end of 2016 the Bank had 17 different card products in its portfolio and had a total of 726,838 issued cards which is 5.39% more than in 2015. Cards issued to individuals make 98% of total issued cards, while 2% is issued to corporates.

Number of HPB Cards



Number of Transactions



During 2016 there were a total of 16.7M cards transactions (up 5.8% vs 2015) in the amount of HRK9.0B (up 6.9% vs 2015).
The Bank had a total of 402 ATMs at the end of 2016 out of which 352 were part of the Bank's network, while 50 were part of First Data's network. Number of ATM transaction was up by 5%. Number of EFTPOS terminals was increased to 2,097 with higher number and volume of transactions.

In 2016 the Bank made 6.2% higher total income from card business mostly due to DCC service revenue.

During 2016 the Bank had developed a new card product – VISA Business Prepaid card. A cooperation with a company First Data on building and managing specialized ATM DCC network resulted with 50 newly installed ATMs. The Bank has also intensified a process of optimizing its own ATM network. In late 2016 a project of connecting the Bank's card business with mStart system was successfully completed which enabled using mStart company in a form of an information intermediary. Also a pilot production with Konzum was initiated which includes acceptance of the Bank's cards at Konzum selling points. Furthermore the Bank started to change the cards acceptance at EFTPOS terminals and had introduced a new model of using information intermediaries in building its private network.

b) Direct Banking

1. Internet Banking

On December 31 2016 a number of individual Internet banking users was 64,446 which is 13.59% more than in 2015. A number of Internet banking transactions by individuals in 2016 was 889,155 which is 4.22% more than in 2015. Size of transactions by individual Internet banking users in 2016 was HRK714,124,034.09 which is 26.46% more than in 2015.

Number of corporate users of Internet banking increased 19.28%, while a number of their transaction was up by 33.24%, and size of transaction by 36.73%.

2. Mobile Banking

A number of mobile banking users on December 31 2016 was 58,114 which is 36.94% more than in 2015.

3. Text Messaging

A number of users of text message services at the end of 2016 was 92,037 which is 23.88% more than in 2015.

New products created in 2016 primarily include: (I) SuperSmart Account – unique product in Croatia which offers account opening without going to a bank, and (II) Online Loan Applications – making cash loan applications without going to a bank.

All direct banking channels from mid-2016 support SEPA credit transfer.

c) Call Center

In 2016 Call Center received 260,078 calls with call efficiency above 80%.

HPB Voice machines (IVR) handled 1,161,740 calls out of which 91% were related to checking account/ card balances while 8% were related to dates of income payments (pensions, child support, maternity benefits, disability benefits).

In 2016 the Bank had successfully implemented a new product Super Smart HPB Account. This was a step forward for the Call Center as the Bank gained another selling channel.

Internal Controls System and Internal Audit

Internal controls are part of the managing process of management and all the Bank's employees.
Internal controls are rational guarantee that business goals will be delivered in appropriate way, within set time limits and by satisfying all regulatory standards.

Basic principles of internal controls system are:

- Clear lines of responsibility
- Separating responsibilities and duties
- Specific control procedures
- Internal audit function

The management and all employees are responsible for the implementation and application of the elements of internal control systems. The elements of internal control systems are described in the internal regulations and implementing documents of business areas. Internal Audit provides an independent assessment of the adequacy and effectiveness of internal controls of audited areas.

Internal Audit

Internal audit is organized as an independent organizational part, and is based on professional principles of internal auditing, alongside associated regulations. Management and responsibilities of internal audit were set by dual responsibility. Administratively it responds to the Management Board, while functionally it responds to the Supervisory Board, and Board of Auditors.

Internal Audit Charter insures organizational independence of internal audit. Access to data, information on persons and spaces is direct and unlimited.

External valuation of internal audit is conducted in accordance with the internal audit standards.

Internal audit procedures are performed in accordance with general internal audit standards and regulatory requirements, in four phases which include planning, research, reporting, and results monitoring.

Planning is based on documented risk assessment and Yearly Operational Program is adopted by the Management Board with prior consent of the Audit Committee and the Supervisory Board. Internal Audit covers all business areas of the Bank and is structurally divided into audit of retail, general audit, audit of information system and audit of the financial markets.

Report on audit results is submitted to accountable person within the subject of internal audit, and member of the Bank's Management Board in-charge, and Audit Committee. Each individual report is subject to discussion during MB session, thus ensuring that MB is aware of the audit's result, recommendations, as well as deadlines to implement recommendations and measures.

Internal audit prepares the report on work on semi-annual and quarterly basis and submits it to the Management Board, Audit Committee and the Supervisory Board.

The report contains information on the achievement of annual work plan, a summary of the most important facts established during the audits carried out, the recommendations and the status of execution and removal of the recommendations and measures identified during the audit.

Development Plan of Hrvatska Poštanska Banka

Our strategy aims at creating the leading financial institution in Croatia by using its comparative advantages in full and in line with our vision to take the best care of financial security and well-being of our clients and communities, by at the same time complying with all regulation, requirements and limits.

Led by our corporate values, primarily clients' dedication, responsibility and excellence, we are focused on achieving sustainable growth based on loans and deposits business.
The most important strategic guidelines, goals we want to achieve, and activities we will take are as follows:

GUIDELINES	GOALS	ACTIVITIES
CLIENT BASE GROWTH	• market share growth in retail loans • market share growth in retail deposits • increase in the number of current & business accounts • increase in the number of clients using m-banking and net-banking services	Growth and sales with emphasis on acquiring younger population, clients with higher income and higher cross-selling potential, but at the same time taking care of existing clients. Offer all basic products in post offices. Focus on digital banking.
SHAREHOLDER VALUE	• achieving return for shareholders and increasing share value • Optimal risk management & operating excellence and market share growth	Profitability growth by organic sustainable market share growth and responsible risk management, and professional cost management.
VALUE FOR THE ECONOMY	• Better involvement in corporate lending, especially SME and 'mid' segments, agriculture, tourism, IT and exports industry • to be a relevant bank under Croatian ownership	Specialization for industries which create value, continued cooperation with government and local units. Further development of the strong Croatian bank image.

Taking responsibility is also one of our corporate values. Therefore we will insist in responsibility towards following 4 groups:

1) responsibility toward clients – with no clients there is no bank, and quality of service and dedication to clients are the best tools for acquiring and maintaining clients,
2) responsibility toward shareholders – return on invested capital with best business practices are bare minimum expected by shareholders,
3) responsibility toward society – HPB offers and will continue to offer banking services to clients which develop socially responsible and commercially viable projects
4) responsibility toward employees – without satisfaction of our employees there is no satisfaction of clients so the performance system introduced in 2016 will reward the best employees for achieving goals

Corporate Segment

Strategic focus of the corporate business includes intensive expansion of cooperation with existing and acquisition of new clients based on the best banking practices. A special emphasis will be on equalizing commercial opportunities and the Bank's need to follow its conservative risk management approach. The ultimate goal is to ensure a moderate long-term growth without exposure to potentially damaging situations.

The Bank's current service model will be improved further by geographic market segmentation and subsegmentation of clients based on the level of their income (micro, small and medium clients, large companies, local government units and central government). The aim of this approach is to create special sales and client relationship model which will satisfy clients' needs and expectations in the best possible manner. This will put an emphasis on the Bank's ability to create optimum combinations of commercial returns for given risk portfolios related to each group of clients.

At the same time the Bank will performs further sector specialization in order to increase quality of the whole business relationship with clients. It will also take into account a maximum credit exposure to certain sectors in accordance with sectoral macroeconomic indicators.

Targeted acquisition groups of clients are all prudential clients with transaction accounts and stable business relationships with other banks – SMEs, large companies, government and local units. Segmentation approach will offer the best solution for new clients and maintain security for the purpose of risk management.

Using different acquisition tools (clients' bases, pre-clearances, selling actions etc) will enable access to new clients and relationship expansion with existing clients. The Bank plans to fully coordinate quality of credit process, authorization powers for certain products and clients, as well as product offer from high-level flexible products to of-the-shelf products. Automation and digitalization are fully embraced trends which helps create modern sales infrastructure. Development process are in progress and in the following period a number of automatic mobile services will be introduced. This enables the Bank to do corporate business in a faster and simpler manner with quality long-term business relationship management.

One of the strategic guidelines for the following period will be stronger portfolio diversification in favor of private sector, especially SMEs. This will ensure higher flexibility in portfolio management, smaller concentration and more balanced growth.

We see HRK lending as one of the Bank's best comparative advantages and we will keep collecting HRK deposits. This requires focus on FX and maturity mismatch of the Bank's balance sheet. Synergies of corporate business and ALM lines will contribute to transparent matches between supply and demand, financing sourcing and placements in the sales network. This will provide guidelines to structure and quality of corporate lending.

Of the main focuses will remain in expanding business cooperation and lending to clients and sectors which contribute the most to the national GDP. It includes manufacturing, tourism, crafts and exporters with different lending programs in cooperation with the CBRD, HAMAG-BICRO, ministries, counties, local government units, associations and other institutions. Due to quality risk management it is necessary to make individual approach for each client in order to evaluate its financial strength, sector growth potential and specifics of the corporate business transaction.

In order to achieve the best market position, offer the best service and optimize revenue, corporate business will take an opportunity to develop cooperation with strategic partner Hrvatska Pošta. Substantial potential of Hrvatska Pošta's distribution channel offers an opportunity for increasing sales of products and services, primarily in payments and card products which will have an impact on noninterest income.

The Bank will keep developing cooperation with FINA as one of the most dominant partners when it comes to total payments and revenue. We are preparing activities aimed at improving cash management business, increasing 24/ 7 safes, and cash manipulation of large companies which have deposit needs. Special attention will be given to improving over-the-counter business for the Bank clients in FINA through mutual projects which should enable easier cash disposal after making payments in FINA locations.

On the deposit front the emphasis will be on expansion of transaction business with SMEs and large companies but also on maintaining relationships with government and public companies, local government units and their companies. At the same time we will take into count optimum ratio of interest expense and the Bank's liquidity needs. On this front high interest rates have been constantly adjusting without consequences for total deposits balance. The Bank has been recognized as a trustworthy partner in corporate business which keeps new inflow of term and demand deposits.

In the following period macroeconomic changes, stabilization and sustainability of economic recovery will lead to higher investment activity and loan demand. In order to satisfy the market demand the Bank is ready to make additional organizational adjustments, process improvement and introduce new and improve existing financing products.

The Bank's ambition is to remain a safe partner to clients which will use the Bank's expertise for improving their businesses. The Bank aims to achieve a sustainable profitability growth with low risk levels of credit portfolios. These will be key business guidelines in the future period which ensures Hrvatska Poštanska Banka to become one of the leading credit institutions in Croatia.

Retail Segment

In 2016 HPB has successfully gained substantial part of retail market share. This puts a great deal of responsibility and the Bank will continue to develop new services in order to continue reaching plans in the future period. Nevertheless we aim to diversify our clients' structure by acquiring younger population and clients with higher income which have better cross-selling potential.

Sole lending products are not enough but it is necessary to follow the trends and constantly improve existing and introduce new products in line with market needs. The most important products of the future period will be related to modern applications and digitalization.

Apart from the mentioned services, part of the focus and resources will be aimed at improving collection of individual accounts on the collateral status monitoring front which includes application support and automated reports.

After introducing new model of cooperation with Hrvatska Pošta in 2015 and 2016, following years should bring substantial new HPB clients' acquisition and revenue stream for both partners. Due to HP being the channel with the largest acquisition potential a new product mix will be created and adjusted if necessary to fit HP.

Price policy i sin focus of all business segments including retail business. The Bank plans to increase current accounts and its balances, together with term deposits which will require adequate balancing between attractive price for clients and optimum cost for the Bank.

Financial Markets segment

Financial market activities will primarily be focused on supporting business goals of the Bank with dominant part being in ensuring stability and liquidity, and portfolio management revenue. The Bank will also organize and participate in securities issuances which have potential to partially compensate interest income decline amid lower yields with noninterest revenue.

Domestic money markets are expected to remain highly liquid and the Bank will use every opportunity to intensify trading by combining short-term deposits and repos.

On the FX position management front the Bank will continue to actively use all available instruments in order to maintain its position as one of the FX market leaders. Structure of the Bank's financing sources, including FX positions, are substantially different from other leading banks in Croatia which poses greater challenges in FX management. However the Bank is expected to maintain successful FX risk management and achieve goals amid turnover decline and narrowing of domestic FX spreads. In order to neutralize the mentioned movements Financial Markets will intensify cooperation with other business lines and the higher cross selling volume could maintain or marginally increase FX trading profit.

On EUR money market we expect EURIBOR rates to remain negative at least by the end of 2017 which will put pressure to costs of nostro accounts with foreign banks. In order to reduce paying negative interests the Bank will intensively look for new appropriate liquid money market instruments. This makes a great challenge for the Bank and the whole system amid negative market returns.

On the money exchange front a declining trend evident in the last several years was disrupted due to the excellent tourist season when most of the revenue is made. In case of no external shocks we expect good profitability to continue until Croatia adopts the euro.

In line with expected stabilization and economic recovery, Croatian capital market is also expected to recover. Therefore investment banking activities will be focused on expanding clients' network and growing revenue from commissions and fees in investment and custody services.

Risk Management

HPB manages its risks by risk management system comprised of a number of procedures and methods aimed at determining, measuring, monitoring, justifying and management of risks to which HPB is or could be exposed. Risk control system aims at curbing risks and mitigating its unwanted consequences to ensure the Bank's business stability (including meeting all obligations). It is worth to note that even with the best risk management system the Bank or any other credit institution is no table to fully mitigate any business risk. The risk management system is regularly updated (qualitative and quantitative components) and was formed in line with the following principles:

- Defining acceptable levels of risk exposure based on internal individual risk exposure limits and regulatory requirements,
- Continued improvement of procedure for determining, measuring, evaluating and monitoring risks to which the Bank is exposed,
- Continued development of measuring and monitoring risk procedures and methods in line with development of control risk function and development of certain IT support.

HPB by the nature of its business takes risks in business with every client. By taking and managing risks HPB ensures the following:

- Stable and secure growth due to using efficient risk management system,
- Improved risk profile,
- Comprehensive HPB Group management system due to using harmonized methods and procedures by all members of the Group.

Considering the size and complexity of its activities HPB defined substantial risks which are monitored through the risk management system in the most detail:

- Credit Risk,
- Market Risk,
- Liquidity Risk,
- Interest Risk in the Bank’s book
- Operational Risk

HPB currently conducts and plans to introduce substantial improvements of all parts of the risk management system.

Credit Risk

Credit risk assumes loss incurred due to debtor's default. This risk is take by HPB as part of the regular business activities and it makes the single most significant risk.

Therefore the most attention goes to managing credit risks in a form of policies, procedure and other internal documentation.

The goal of credit risk management is to ensure quality credit portfolio, profit and lending growth with maximum returns and acceptable risk/ return ratio, together with risk/ cost ratio.

Credit risk management is organized through:

- The Management Board,
- Authorized committees (Credit Committee) and persons,
- Operating and organizational separation between front and back office activities,
- Risk control function.

Credit risk appetite is determined by internal credit risk limits. For the purpose of credit risk control and management the Bank monitors different risk indicators (e.g. creditworthiness of clients including track record of paying credit liabilities, quality of collateral, capital adequacy, portfolio quality) and makes different estimates (e.g. credit risk estimate before loan approval, loan recoverability estimate).
Credit risk is also related to concentration risk and currency induced credit risk which HPB manages in the same way as it manages credit risk.

Market Risk

Market risks include position risk, FX and commodity risk.

- Position risk assumes loss due to price change of financial instruments or financial derivatives
- FX risk assumes loss due to change in exchange rate or price of gold
- Commodity risk assumes loss due to price change of commodities.

Market risk management is organized through:

- The Management Board,
- Operating and organizational separation of front and back office trading activities,
- Assets and Liabilities Office,
- Risk control function.

Market risk appetite is determined by internal market risk limits. In order to mitigate market risks the Bank uses certain limits for portfolio, sub-portfolio and instruments (based on its nature). Also there are stop loss limits by each equity classified as assets held for trading.

In measuring and valuing market risk exposure the Bank uses a methodology based on value at risk (VaR) method, duration and PV01 (internal model).

Liquidity Risk

Liquidity risk assumes loss due to inability to fulfill liabilities at maturity. Liquidity risk is related to the following two risks and the Bank considers them as one for the purpose of risk management:

- Funding Liquidity Risk assumes credit institution's inability to fulfill current and future cash needs or collateral needs without effecting its daily business or financial results
- Market Liquidity Risk assumes credit institution's inability to offset positions or eliminate them at market price due to market disruptions or shallowness.

Liquidity risk management is organized through:

- The Management Board,
- Assets and Liabilities Office,
- The Assets and Liabilities Committee (Liquidity Subcommittee),
- Risk control function,
- Financial Markets Department.

Methodology of measuring, i.e. estimating exposure to liquidity risk is based on the calculation of liquidity coefficients, calculation of structural liquidity exposure indicators, determining internal capital requirements for liquidity risk and calculation of liquidity coverage ratio (LCR).

Liquidity risk appetite is determined by liquidity risk limits. For mitigating liquidity risk there are certain limits related to liquidity coefficient, assets and liabilities maturity mismatch and structural liquidity limits. There are also limits in accordance with the Decision on Mandatory Reserves and Decision on Minimally Required FX Receivables by the CNB.

Interest Risk in the Bank's Book

Interest risk in the Bank's book assumes loss due to changes in interest rates which affect nontrading positions.
Managing interest risk in the Bank's book is organized through

- The Management Board,
- The Assets and Liabilities Committee,
- Risk control function.

Interest risk appetite is determined by internal exposure limits.

Methodology of measuring, i.e. estimating exposure to interest risk in the Bank's book is based on the simplified calculation of estimated change in economic value of the Bank's book as set by the CNB's Decision on Managing Interest Risk in the Bank's Book. The Bank also calculates interest risk exposure from the profit perspective.

For mitigating interest risk in the Bank's book there are certain limits related to change in the economic value of the Bank's book and regulatory capital related to change (decrease) of net interest income.

Operational Risk

Operational risk assumes losses due to inadequate or failed internal processes, human capital or system, or due to external effects including legal risk.

Operational risk management is organized through:

- The Management Board,
- Structure of operational risk management (Operational risk manager, Support persons for operational risk management, Connection persons),
- Operational Risk Management Committee,
- Assets and Liabilities Committee,
- Corporate Security Office,
- Compliance Office,
- Risk control function.

Methodology of measuring, i.e. estimating operational risk exposure is based on collecting and analyzing data on events due to operational risk, self-assessment of risk and controls, estimated IT risk, results of analysis of business effects taking into count implemented going concern plan and estimation of externalized risks. Also the Bank estimates effect of introducing new products to its risk profile.

The Bank primarily uses measures for mitigating operational risk through internal control system and risk transfer measures (hedge) in cases where applicable. Also there is going concern management system.

Other Risks

Other risks, although evident in the Bank's business, are less important than previously described and their methodology and managing is less complex.

Concentration Risk assumes every single, direct or indirect exposure to one person, group of linked persons or exposure pool interconnected with same risk determinants including same sector, geographical area, business or products, i.e. using techniques to for lowering credit risk, including risks related to indirect credit exposure to same collateral provider which can lead to losses that could jeopardize credit institution's going concern or make material change to its risk profile.

Collateral Value Risk assumes inconvenient market movements of assets used as collateral which will be a collateral trigger.

Government Risk assumes government bodies or the central bank will not be able to meet its obligations toward other countries or foreign lenders and that other debtor of the country will not be able to meet their obligation to foreign lenders.

Strategic Risk assumes loss due to wrong business decisions, inflexibility to economic changes etc.

Management Risk assumes loss due to credit institution having limited capacity in forming sophisticated management system, mechanism and controls.

Credit Value Adjustment Risk assumes portfolio value adjustment at mid-market value (this risk is related to all OTC derivatives for all business activities except credit derivatives recognized for reduction of credit risk weighted exposure). Credit value adjustment reflects current market value of counterparty credit risk for the institution but does not reflect current market value credit risk for the counterparty.

The Bank regularly reports on credit value adjustment risk which is not relevant in size for the Bank's business.

Compliance Risk assumes potential measures or sanctions and risk of significant financial loss or reputation loss borne by the institution due to noncompliance with regulation, standards, codices or internal documentation.

Business Risk assumes negative sudden change in business and/ or profit margins which could lead to losses or decrease in the Bank's market value. Business risk can occur if market environment deteriorates substantially or due to changes in competition or consumer behavior.

Legal Risk assumes legal procedures against the Bank due to not meeting legally binding conditions, and business decision which are not applicable or have a negative effect on the Bank's business and financial position.

Regulatory Risk assumes regulation change which can affect the Bank's business and profitability.

Social Responsibility

As the largest government owned bank HPB accepts responsibility for not only economic but also social national flows and is contributing to their development.

Human Rights

On the human rights principles front in 2016 HPB continued its activities related to business information security, as well as security, education and care of its employees.

The Bank is constantly taking care of expertise and education of its employees as the base of its market competitive strength. Moreover the Bank's employees are compelled to maintain their expertise in line with professional and regulatory requirements. HPB supports and promotes lifelong learning which creates additional value for the company and enables each employee to gain adequate skills for his job. There are employee education on and off work through expert consultancies, workshops, seminars, congresses, specialization and language and IT courses.

The Bank continued to use e-Classroom system constantly available to all employees regardless of time and location.

Education system through internal trainers provides education for new and existing employees for certain jobs in order to have employees which are capable and adequately prepared for performing all regular work.

The Bank continued its systemic educations which programs and contents are adjusted to new employees – probationers in order for them get direct acquaintance with the Bank's business in all areas and as a whole in order to get better work preparation. At the end of the education program all probationers must take probationary exam which defines their further work status and they are directed to business areas where they could get the best results.

Additional care for employees includes periodical work satisfaction surveys. In 2015 the Bank started a comprehensive work and organization satisfaction questionnaires in order to gain insight in employees' perception of the Bank, its strengths and weaknesses and how they feel by working for the Bank. The mentioned activities have intensified in 2016 on all levels. The aim is to identify key points in everyday work environment and ways it can be improved in order to get better work satisfaction, engagement of employees and quality of the whole organization climate. Survey results are also important guideline in initiating plans and activities in order to improve organization processes and work environment.

On the employees general awareness about internal and external movements front the Bank continued to issue an internal paper My HPBank 4 times a year. This electronic paper is aimed at employees and it follows the most important movements within HPB Group, interviews, charity work of employees, information about new employees, actions and new products but also more casual themes. The aim of the paper is to improve vertical and horizontal communication within the Bank and enable employees across the country to get acquainted with its colleagues.

Beside internal paper there is also HPB internal web portal, the official information channel available to all HPB Group's employees. It contains regular publication of all acts and decisions by the Bank, as well as other work related news and notifications. The Intranet is a place where employees can get important information on the Bank's business and possibilities of work education. Each organization unit has a mutual space (team page) for sharing contents and other materials for everyday work.

The Intranet is constantly improved and developed in order to offer more contents and new functions.

The Bank sees itself as an institution which can participate and contribute to improving financial literacy, especially when it comes to students. Therefore in the last 2 years the Bank has been engaged in conducting research on importance of timely and complete awareness of the citizens, acquaintance with financial risks and quality personal finance management.

One of the Bank's priorities includes increasing awareness on good clients' finance management, together with finance management of other citizens, corporates, and public sector participants. The Bank also puts an emphasis on increasing cooperation with student associations, high schools and other institutions by taking part in lectures, discussion and competitions.

Environment

The Bank has strategically chosen to buy the most technologically advanced equipment in terms of ecology efficiency. All desktop computers are all-in-one with all components being integrated in one case so that their write-offs will pose considerably less electronic waste. Electronic waste is taken care of in accordance with all regulatory requirements and agreements with suppliers so the buying price reflects the price of waste. Every electronic equipment write-off results with electronic equipment transfer to ecological dump.

HPB has continued the virtualization trend of its service providers which enables one physical server to have several logical servers in order to save energy for supply and cooling.

Electronic banking, computerization and automation of office activities has been continued with lowering paper consumption and printing needs. The Bank has implemented an electronic invoice which replaces physical invoices for telecommunication, utilities and other services with electronic ones which reduces volume of printed papers.

Also the Bank has completed a documentation classification project which enables archiving and documentation digitalization and complete electronic documentation in the medium term.

Under the Green Office initiative since 2012 the Bank has been involved in activities to reduce all negative environmental impact of everyday office work and increase work efficiency. Since the initiative started the Bank managed to gain substantial energy savings with most progress made in paper consumption.

By information page on our Intranet – Green Board the Bank continued to educate and advise employees on measures of Green Office related to paper consumption reduction, optimum temperature in working environment, rational water and lights consumption, separating old papers and old toners in special boxes etc.

The Bank's clients have an option to receive their reports on account changes and card consumption via e-mail.

Anticorruption

The Bank has continued with the activities to promote business integrity and transparency by:

- improving corporate management,
- improving relationship and communication with clients by stronger satisfaction and loyalty, as well as intensified relationship,
- business compliance with regulation, acts and standards,
- improving internal control systems and performance of control functions,
- encouraging ethical behavior and treatment.

Quality Service Management Office is responsible for improving relationship and communication with clients by conducting surveys and research on clients' satisfaction and suggesting quality service improvements to certain business areas. The Office also handles complaints and other clients' requests.

In accordance with the Anti Money Laundry and Terrorism Financing Act the Bank:

- conducts measures and activities from the Act and other related regulation,
- systemically develops and improves software support for identifying and preventing money laundering and terrorism financing,
- has organized a number of subject related educations.

HP – Hrvatska Pošta conducts measures and activities in accordance with the Anti Money Laundry and Terrorism Financing Act in offering payments on behalf of the Bank in order to ensure same anti money laundry standards the Bank:

- conducts education of HP's internal trainers,
- checks compliance of HP's acts with the Bank's standards,
- monitors effective implementation of the measures and procedures in detecting and preventing money laundering and terrorism financing

Report on Application of the Corporate Governance Codex

Application of the Corporate Governance Codex

In accordance with article 272.p of Commercial Companies Law the Management Board and the Supervisory Board state that the Bank voluntarily implements the Corporate Governance Codex which was established by Croatian Financial Services Supervisory Agency and Zagreb Stock Exchange („ZSE"). Also, the Bank implemented the Corporate Governance Codex for Commercial Companies in which the Republic of Croatia has shares or stakes which was established by the Croatian Government (Official Gazette 112/ 2010).

Constituent part of this Report is Annual Questionnaire for 2016. The questionnaire is also available on the Bank's website and it reflects corporate management practice used in the Bank in accordance with the recommendation from the Corporate Governance Codex and detailed treatment explanations.

With recommendations of the mentioned codices and in accordance with the credit institutions regulation, the Bank is actively improving its corporate management in line with the Bank's structure and organization, strategy and business goals, distribution of privileges and duties with a special emphasis on effective procedures for determining, measuring, monitoring and reporting of risks associated with the Bank's business, as well as setting up corresponding internal control mechanisms.

Description of basic characteristics associated with internal supervision and risk management can be found in the Bank's business description in the Note 2.

Significant Shareholders and Limited Share Rights

The Republic of Croatia is the most significant shareholder of the Bank with 42.43% stake. Together with Croatian Pension Insurance Institute, Croatian Post, State Agency for Deposit Insurance and Bank Resolution, and NEK Fund the Government controls more than 74% of equity and voting rights.
In line with the Bank's Statute, voting rights are not limited, nor are there limits for realizing voting rights.

Rules for the Appointment or Removal of the Management Board, Statute Changes and Special Authorizations of the Management Board

In accordance with the Bank's Statute the Management Board should have at least 2 and no more than 5 members with the Supervisory Board deciding on the number. Members and the president of the Management Board are appointed by the Supervisory Board to a maximum of 5 years, and can be reappointed without time limit. Member of the Management Board must fulfill all the necessary conditions as set by the regulation on the Bank's business, as well as get the nomination approval by the CNB. The Supervisory Board can decide to remove the president or Management Board members should it have an important reason, while president and members of the Management Board are entitled to make written resignations. The Bank's Statute can only be changed by the decision of the General Meeting. Decision is approved if voted by ¾ of the equity holders. A proposed Decision on amendments to the Statue is submitted by the Management Board to the Supervisory Board, which is authorized to accept the proposal and submit it to the General Assembly for consideration.

Supervisory Board Members and Activities

The Supervisory Board can have a maximum of 7 members appointed and removed by the General Meeting. Member of the Management Board must fulfill all the necessary conditions as set by the regulation on the Bank's business, as well as get the nomination approval by the CNB

Supervisory Board's authorizations are regulated by Commercial Companies Act, Credit Institutions Act and the Bank's Statute. The Supervisory Board has set up an Audit Committee, Committee for receipts, Nomination Committee and the Risk Committee as supporting bodies.

From January 1 to July 30 2016 the Supervisory Board had the following 4 members:

- Dražen Kobas, president
- Nada Karaman Aksentijević, PhD, vice president
- Marin Palada, member
- Niko Raič, Msc, member

After July 30 2016 the Supervisory Board was acting in accordance with the Resolution of Commercial Court in Zagreb Number 76.R1-252/ 2016 of August 10 2016 for a period between August 10 to September 5 2016 and in accordance with the Resolution Number 28.R1-281/ 16 of September 21 2016 for a period between September 21 and December 14 2016, and had following 3 members:

- Dražen Kobas, president
- Nada Karaman Aksentijević, PhD, vice president
- Niko Raič, Msc, member

Members of the Supervisory Board do not own the Bank's shares or any other securities issued by the Bank.

Management Board Members and Activities

Privileges, duties and responsibilities of the Bank's Management Board are described in the Commercial Companies Act, Credit Institutions Act, the Bank's Statute and the Board's Work Regulations. The Board establishes permanent and temporary boards and commissions. The Bank's permanent boards are Credit Board, Assets and Liabilities Management Board and Operational Risk Management Board.

In a period from January 1 to May 24 2016 the Management Board had 4 following members:

- Tomislav Vuić, president
- Dubravka Kolarić, member
- Mladen Mrvelj, member
- Domagoj Karadjole, member.

In a period from May 24 to December 31 2016 the Management Board had 4 following members:

- Tomislav Vuić, president
- Mladen Mrvelj, member
- Domagoj Karadjole, member.

Members of the Management Board do not own the Bank's shares or any other securities issued by the Bank.

Overview of Diversity Policy

There is no discrimination by sex, age or any other basis in procedure of selecting members of the Management Board, Supervisory Board or other bodies. The Bank has relatively high percentage of female managers, as well as persons with different level of experience. The Bank will keep the current policy of sex and age diversity.

Collective experience of the Bank's management is a combination of needed knowledge and skills for fulfilling activities of a certain function and the Bank's goals.

Management by Sex	Number 2015	Number 2016	Share 2015	Share 2016
Male	**25**	**23**	**58.1%**	**53.5%**
Female	**18**	**20**	**41.9%**	**46.5%**

CORPORATE GOVERNANCE CODEX

ANNUAL QUESTIONNAIRE

All questions from this questionnaire are related to a period of one business year in line with annual financial reports.

COMMITMMENT TO PRINCIPLES OF CORPORATE GOVERNANCE AND SOCIAL RESPONSIBILITY

1. Has the company accepted application of the Corporate Governance Codex or it has own corporate governance policy?

YES

2. Are principles of the Corporate Governance Codex part of internal company policies?

YES

3. Does the company report principles of Corporate Governance Codex within its annual financial reports based on "do or explain" principle?

YES

4. Does the company's decision process take into count interests of all its shareholders in accordance with the principles of the Corporate Governance Codex?

YES

SHAREHOLDERS AND SHAREHOLDERS' MEETING

5. Is the company part of the mutual shareholding with other companies? (if yes, please explain)

NO

6. Does every share give one voting right? (if no, please explain)

YES

7. Is the company treating all shareholders equally? (if no, please explain)

YES

8. Is authorization to vote at the shareholders' meeting extremely simple and without formal requirements? (if no, please explain)

YES

9. Has the company secured, without special charges, authorized voting persons for all shareholders who were not able to vote by themselves but according to their instructions? (if no, please explain)

There were no such demands.

10. Has the Management Board of the Board of Directors while arranging the shareholders' meeting determined a date for registered shares and based on which the voting right may be determined in a way the date is not set more than 6 days before the shareholders' meeting? (if no, please explain)

YES

11. Are shareholders' meeting schedule and all the data relevant for the daily agenda published on the company's website and put at disposal to shareholders in the company's premises right after the first publication of the daily agenda? (if no, please explain)

YES

12. Does dividend payout or prepayment resolution contain date on which the dividend right will be obtained together with the date on which the dividend will be paid? (if not, explain)

YES

13. Is the dividend payout or prepayment set 30 or less days after the resolution is made? (if no, please explain)

YES

14. Have certain shareholders been in more convenient position in relation to other shareholders during dividend payout or prepayment? (if yes, please explain)

NO

15. Are shareholders able to vote at the shareholders' meeting by using contemporary communication technology? (if no, please explain)

NO

There were no such demands by shareholders.

16. Are conditions for participation at the shareholders' meeting and using voting rights set (no matter whether set according to the act or the statute), such as preregistration of participation, attesting authorization etc? (if yes, please explain)

YES

Due to optimal organization and arrangement of the shareholders' meeting every shareholder is needed to register its participation at the meeting, while authorizations are needed to be attested in order to determinate valid voting rights.

17. Did the company's management board publish decisions of the shareholders' meeting?

YES

18. Did the company publish information about potential lawsuits that deny these decisions? (if no, please explain)

NO

There were no lawsuits related to denying the decisions.

MANAGEMENT AND SUPERVISORY BOARDS

- **STATE MANAGEMENT BOARD MEMBERS AND THEIR FUNCTIONS**

  Tomislav Vuić, president of the Board

  Dubravka Kolarić, Board member, until May 24 2016

  Domagoj Karadjole, Board member

  Mladen Mrvelj, Board member

- **STATE SUPERVISORY BOARD MEMBERS AND THEIR FUNCTIONS**

  Dražen Kobas, president of the Board

  Nada Karaman Aksentijević, vice president of the Board

  Niko Raič, Board member

  Marin Palada, Board member, until July 30 2016

19. Did supervisory board or board of directors make a decision on approximate working plan which includes a list of sessions and data which is regularly needed to be supplied to the supervisory board members?

YES

CORPORATE GOVERNANCE CODEX

ANNUAL QUESTIONNAIRE

All questions from this questionnaire are related to a period of one business year in line with annual financial reports.

20. Did the supervisory board or the board of directors enact internal working rules? (if not, please explain)

YES

21. Is the supervisory board or non-executive directors of the board of directors made mostly out of independent members? (if no, please explain)

NO

According to the Credit Institutions Act, a bank's supervisory board must have one independent member. The Supervisory Board of HPB has 2 independent members.

22. Does the company have a long-term succession plan? (if no, please explain)

NO

The Bank does not have it due to regulation which determines appointment of the president and members of the management boards in companies and other persons in legal entities which are of strategic and special importance to the Government.

23. Are compensation schemes of supervisory boards or board of directors partially or fully performance-based? (if no, please explain)

NO

According to the Shareholders' Meeting Decision compensations to the members of the Supervisory Board is determined by the Government Decision on Compensation to Members of Supervisory Board and Board of Directors.

24. Are compensation schemes to the members of the supervisory board and the board of directors determined by the shareholders' meeting decision or the statute? (if no, please explain)

YES

25. Is information on compensation from the company and company-linked entities for every single member of the supervisory board and the board of directors, together with the compensation structure, publicly available? (if no, please explain)

NO

Information on compensation for the members of the Supervisory Board are publicly available on the individual basis in the Shareholders' Meeting Decision which determines compensation for their work. Compensation for the Management Board members, higher management and linked persons is available in a special note within the annual financial report in line with the International Financial Reporting Standards. The annual financial reports are available on the Bank's website.

26. Is every member of the supervisory board or the board of directors notifying the company about any changes related to their acquiring or dismissal of the company shares at the latest of five trading days after the change is being made?

NO

Members of the Supervisory Board do not own the Bank's shares.

27. Are all activities in which participated members of the supervisory board or the board of directors or their linked persons clearly stated in company reports?

NO

Aggregated data on transactions with linked persons are stated in the annual financial reports which are based on the International Financial Reporting Standards.

28. Do contracts between members of the supervisory board or the board of directors exist?

YES

Contracts exist as part of the regular business activities.

29. Are they authorized by the supervisory board or board of directors? (if no, please explain)

YES

Yes if authorization is needed.

30. Are all important elements of such contracts stated in the annual financial report? (if no, please explain)

NO

Aggregated data on transactions with linked persons are stated in the annual financial reports which are based on the International Financial Reporting Standards.

31. Did the supervisory board or the board of directors establish the nomination commission?

YES

32. Did the supervisory board or the board of directors establish the remuneration commission?

YES

33. Did the supervisory board or the board of directors establish the audit commission?

YES

34. Are most members of the commission also independent members of the supervisory board? (if no, please explain

NO

Commission members are also members of the supervisory board but supervisory board according to the Credit Institutions Act needs to have one independent member. Out of established commissions Receipts Board has the most independent members.

35. Did the commission follow the integrity of the company's financial information, in particular correctness and consistency of accounting policies used by the company and its group including consolidation criteria for the companies which are part of a group? (if no, please explain)

YES

36. Did the commission estimate the quality of the internal control and risk management system in order for the main risks faced by the company (including regulatory risks) to be properly identified, published and managed? (if no, please explain)

YES

37. Did the commission work on maintaining efficiency of the internal audit system, especially by making recommendations during selection, nomination, renomination and changing directors of internal audit, as well as financial means at its disposal, and estimates of director's activities related to recommendations of the internal audit? (if no, please explain)

YES

Audit Committee follows efficiency of the internal audit system through individual and quarterly reports and reports on monitoring application of recommendations by internal audit. In accordance with the Credit Institutions Act a person authorized for internal audit control function can be named or replaced solely by the Supervisory Board's approval.

38. If the company does not have an internal audit did the commission make an evaluation of needs for establishing such function? (if no, please explain)

NO

The Bank has the internal audit function.

39. Did the commission supervise independence and objectiveness of external auditor, especially in relation to rotation of authorized auditors within the auditing company and fees paid for the auditing services? (if no, please explain)

YES

40. Did the commission monitor nature and volume of services which are not auditing but are received from the auditing company or linked persons?

YES

41. Did the commission make rules about which services external auditor and linked persons cannot provide to the companies, which services it can provide with previous approval by the commission and which services it can provide without previous approval by the commission? (if no, please explain)

NO

It is described within the national legislature

42. Did the commission consider efficiency of the external audit and procedures of higher management considering the recommendation made by the external auditor? (if no, please explain)

YES

43. Did the audit commission secure delivery of quality information of dependent and independent entities and third persons (like tax consultants)? (if no, please explain)

YES

44. Is the work-related documentation delivered to all members of the supervisory board or the board of directors in a timely manner? (if no, please explain)

YES

45. Do all minutes from the meetings of the supervisory board or the board of directors contain all enacted decisions with voting results? (if no, please explain)

YES

46. Did the supervisory board or the board of directors make evaluation of its work in the previous period which includes valuing contribution and competence of each member, as well as mutual work of boards, estimate of the work done by commissions and estimate of realized versus planned company goals?

NO

47. Did the company publish report on compensation scheme for the management board, the board of directors and the supervisory board in its annual report? (if no, please explain)

NO

See answer 48.

48. Is report on compensation scheme of the Management Board and executive directors permanently published on company's website? (if no, please explain)

NO

Report on compensation scheme is publicly available as part of the public announcement of rating and other requirements in accordance with the Credit Institutions Act and Regulation 575/ 2013.

49. Is all information about compensation of the members of the Management Board and executive directors detailed and publicly available in the annual company report? (if no, please explain)

NO

Aggregated data on transactions with linked persons and the Bank's management are stated in the annual financial reports which are based on the International Financial Reporting Standards.

50. Are all sorts of compensation received by the members of the management board and the supervisory board, together with options and other benefits, publicly available as detailed items and persons in the annual company report? (if no, please explain)

NO

See answer 49.

51. Are all activities in which members of the management board or executive directors or their linked persons took place with company or company-linked entities clearly mentioned in company reports? (if no, please explain)

NO

See answer 49.

52. Do reports by the supervisory board or the board of directors to the shareholders' meeting, besides contents defined by legislation, contain evaluation of total business performance of the company, management and their cooperation with the management board?

YES

CORPORATE GOVERNANCE CODEX

ANNUAL QUESTIONNAIRE

All questions from this questionnaire are related to a period of one business year in line with annual financial reports.

AUDIT AND INTERNAL CONTROL MECHANISMS

53. Does the company have an external auditor?

YES

54. Is external auditor linked to the company?

NO

55. Did the external auditor or its linked entities offer other services to the company?

YES

56. Did the company publish fees paid to external auditors for auditing and other services? (if no, please explain)

NO

The auditor audited financial reports of the Bank and its subsidiaries in line with contracted price conditions which is in accordance with its general business conditions.

57. Does the company have internal auditors and established internal control system?

YES

TRANSPARENCY AND BUSINESS OPENNESS

58. Are annual, semi-annual and quarterly reports available to shareholders?

YES

59. Did the company make the calendar with most important events?

NO

All important events and information are publicly available as soon as the exact dates are determined.

60. Did the company establish mechanism for making sure the persons which have or get in contact with privileged information understand the nature, importance and limitations related to this information?

YES

61. Did the company establish mechanism for monitoring the privileged information flow and their potential misuse?

YES

62. Did someone suffer negative consequences because it pointed to supervisory bodies or internal bodies to some deficiencies in applying regulation and ethical standards within the company?

NO

63. Did the management board have meetings with interested investors during previous year?

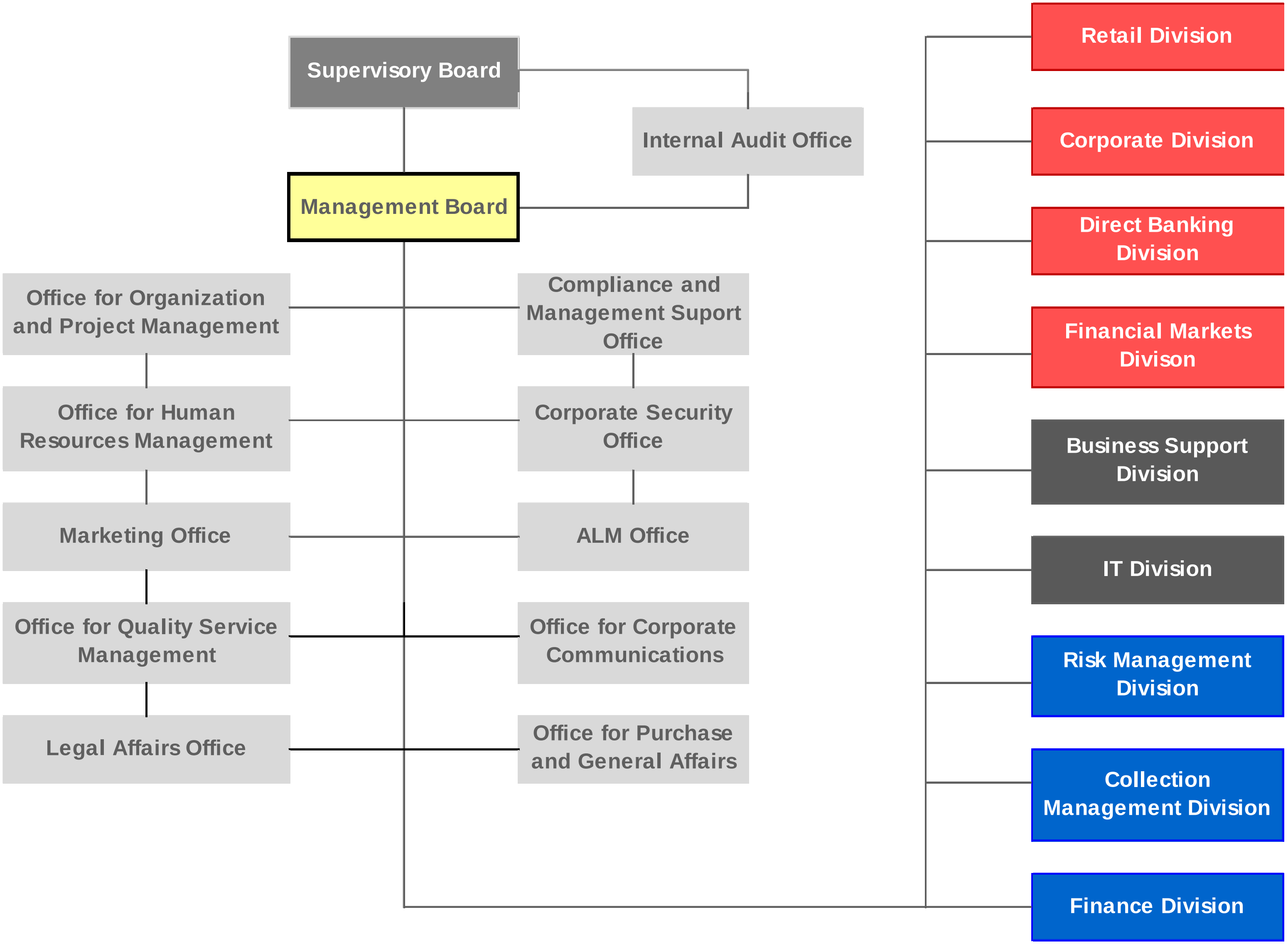
NO

64. Do all members of the management board and supervisory board or the board of directors agree the information provided in answers to this questionnaire are completely true to the best of their knowledge?

YES

Organizational Scheme of Hrvatska Poštanska Banka p.l.c.

The Bank's business is organized in 20 organizational units – 11 offices and 9 divisions. The Bank's organizational scheme is as follows:



The Bank's organizational unites are divided into 4 basic business areas including:

1. Professional support to the Management Board,
2. Profit centers,
3. Operating business support,
4. Risk, collection and financial management.

Business area functionally and technologically connects certain Bank's organization units to ensure efficient management and business organization.

1. PROFESSIONAL SUPPORT TO THE MANAGEMENT BOARD includes a group of activities which offer professional support to the Management Board in achieving business goals, organization and the Bank's management.

This business area includes:

- Internal Audit Office,
- Compliance and Management Support Office,
- Office for Corporate Communications,
- Office for Organization and Project Management,
- Office for Human Resources Management,
- Marketing Office
- Corporate Security Office
- Office for Quality Service Management,
- Legal Affairs Office,
- Office for Purchase and General Affairs, and
- ALM Office.

The Internal Audit Office is the Bank's organization unit which evaluates internal control and risk management system, compliance function and performs IT audit.

Compliance and Management Support Office is the Bank's organization unit which supports the Bank's bodies, follows regulation, ensures compliance of the Bank's business with regulation and manages the anti money laundering and terrorism financing system.

Office for Corporate Communications is the Bank's organization unit responsible for corporate communications.

Office for Organization and Project Management is the Bank's organization unit which analyses and improves organization and business processes and manages projects**.**

Office for Human Resources Management is the Bank's organization unit involved in supply, development and rewarding employees. It also regulates legal working affairs with employees and government bodies.

Marketing Office is the Bank's organization unit which prepares and conducts marketing and promotional activities.

Corporate Security Office is the Bank's organization unit which ensures safety of IT, workers and assets.

Office for Quality Service Management is the Bank's organization unit which manages quality of services offered to clients by continuous surveys and research on clients' satisfaction and suggesting improvements on that front.

Legal Affairs Office is the Bank's organization unit involved in legal support to all organization units.

Office for Purchase and General Affairs is the Bank's organization unit involved in asset purchase and management, together with other general affairs.

ALM Office is the Bank's organization unit responsible for managing assets and liabilities, FX positions, market risk and liquidity risk positions.

2. **PROFIT CENTER** includes a group of activities which sell the Bank's products and services.

This business area includes:

- Retail Division,
- Corporate Division,
- Financial Markets Division, and
- Direct Banking Division.

Retail Division is the Bank's organization unit which offers market based banking and financial services to households and coordinates work of retail regional centers, outlets and HP-Hrvatska Pošta as a distribution channel.

Corporate Division is the Bank's organization unit which offers market based banking and financial services to legal persons, natural persons and crafts which conduct independent and permanent economic activity.

Financial Markets Division is the Bank's organization unit which trades in financial instruments on behalf of the Bank, manages liquidity and FX position and offers investment services and activities, together with supplementary services to clients.

Direct Banking Division is the Bank's organization unit which ensures undisturbed functioning and development of direct distribution channels and card business (ATM, POS, WEB, CC, mBanking and eBanking, card business).

3. **OPERATING BUSINESS SUPPORT** includes a group of activities which offer support to sales and the Bank's whole business.

This business area includes

- Business Support Division, and
- IT Division.

Business Support Division is the Bank's organization unit offering operating support to profit centers and making domestic and FX payments, cash management and supply activities of the Bank's business network and Hrvatska Pošta with cash.

IT Division is the Bank's organization unit offering IT support to all organization units.

4. **RISK, COLLECTION AND FINANCIAL MANAGEMENT** includes a group of activities for risk, collection and financial management.

This business area includes

- Risk Management Division,
- Collection Management Division, and
- Finance Division.

Risk Management Division is the Bank's organization unit which measures, evaluates and controls all the risks the Bank is or could be exposed with an aim of reducing potential exposure to all kinds of risks and ensuring safety and business efficiency.

Collection Management Division is the Bank's organization unit which performs receivables restructuring and activities of early and forced collection.

Finance Division is the Bank's organization unit which manages the Bank's accounting system, performs regulatory reports, financial controls and develops management reporting system.

Human Resources Management in HPB p.l.c.

Improving standards in human resources management enables support to vision, mission and the Bank's corporate values. It is mostly reflected in acquiring new quality employees, but also in help to business areas in identifying and keeping existing excellent employees. In line with the Bank's corporate values a model of key competences was developed which combines skills, opinions and behavior for the management and employees in order to successfully achieve set targets.

Also the Bank puts an emphasis on increasing usage of knowledge and skills by control and systemic supervision of work performance adjusted to specifics of each business area.

In 2016 a new work performance management model was introduced which is characterized by transparency and objectivity in evaluating and rewarding employees.

The model enables monitoring and evaluation of organizational and individual performance based on key performance indicators. Individual level also includes development goals for employees. This completes motivational and development purpose of the model which is the base for career management of the Bank's employees.

Increase in intellectual capital, and contribution of employees to the Bank's results is achieved by timely definition of education needs in order to improve sales, technical, communication, management and other business skills which increase sales and business efficiency. In line with education needs in 2016 there were a number of education programs and intensified processes of internal and external education of employees and management.

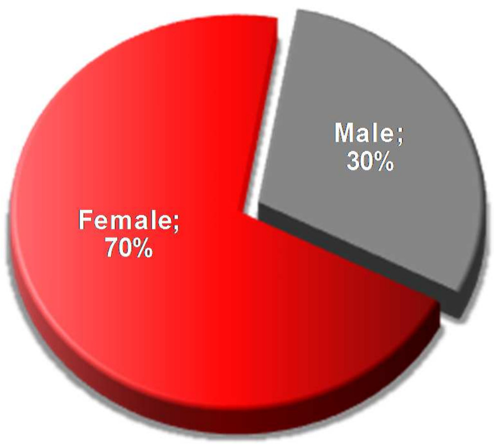
Investment in HR processes resulted with Employer Partner certificate by Selectio in December 2016. When the Certificate was being awarded it was stated the Bank had developed human resources management in line with the best practices.

Number of Employees in the Bank 2013 - 2016

Number of Employees	Dec 31 2013	Dec 31 2014	Dec 31 2015	Dec 31 2016
Based on the Working Hours	**875**	**850**	**823**	**833**
At the end of the Period	**1,075**	**1,084**	**1,067**	**1,067**

All jobs in HPB are located in the Republic of Croatia.

Structure of HPB's Employees by Sex on December 31 2016:

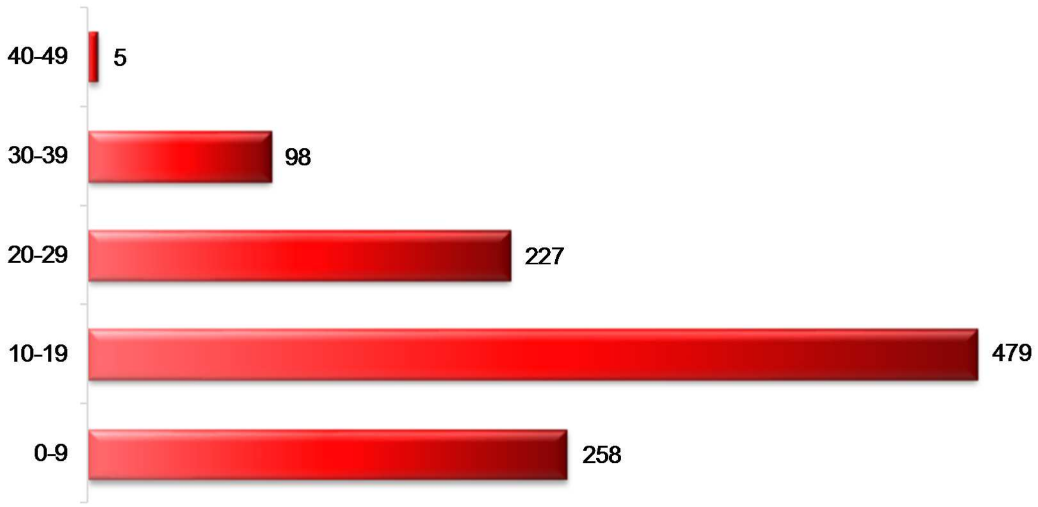


Education and Skills of Employees 2013 – 2016

Employees with undergraduate and graduate qualifications dominate the qualifications structure.

Qualification	Dec 31 2013	Dec 31 2014	Dec 31 2015	Dec 31 2016
Postgraduate/ Doctorate	17	15	15	16
Graduate	432	436	445	445
Undergraduate	164	170	169	169
High School	459	460	436	435
Elementary or Secondary School	3	3	2	1
Total	**1,075**	**1,084**	**1,067**	**1,067**

Number of Employees Based on Years of Service as of December 31 2016:



Operations of Subsidiaries

HPB Invest Ltd

HPB Invest Ltd (hereafter „the Company“) is an investment fund management company registered on July 19 2005 and is 100% owned by the Bank. The Company officially started with operations on October 5 2005 with shareholders' equity of HRK5.0M.

As of December 31 2016 the Company had 5 open-end investment funds with public offer under management. The Company also had Umirovljenički Fond, which is a special purpose fund, established by the Croatian Government for repaying pensioners' debt.

Total assets under management were HRK773M.

Structure of the assets under management is as follows:

Fund	**Assets under management HRK'000**	**2016 Return in %**
HPB Dionički Fond	31,400	14.21%
HPB Global Fond	70,262	13.31%
HPB Novčani Fond	448,299	0.39%
HPB Obveznički Fond	209,721	5.76%
HPB Euronovčani	13,798	0.21%

As of December 31 2016 the Company's balance sheet was HRK8.3M. In 2016 the Company made net profit of HRK1,835K. At the end of 2016 the Company had 11 employees.

Development Plan

The Company's main activities will remain in the field of professional asset management and high quality of services in order to ensure sustainable return on clients' assets.

Continuing improvement of the Company's development policy will be directed towards continuing professional, human resource, organizational and technological improvements. Together with continuing improvement of the Company's development policy and ever-growing legal and regulatory requirements, the Company will continue to attract clients with long-term attractive pallet of funds and investment products which can satisfy all of their needs differentiated by goals, investment horizon and risk appetites.

On top of all the things mentioned, the Company's development policy assumes continuing improvement and focus on the two most important sales channels – Croatian Post and HPB.

Risks Exposure

The most important types of risks the Company is exposed to are credit risk, market risk, liquidity risk and operational risk. On the reporting date the Company did not have substantial exposure to market and liquidity risks. The main part of the Company's credit risk exposure is related to fair value of instruments reported in the report on financial position.

The Company is exposed to operational risks in its regular business activities. The Company manages its operational risks with quarterly and annual management reports about events which can be classified as operational risks.

Risks which can affect the Company's regular business activities include assets decrease risk amid clients' funds withdrawal or amid asset value depreciation.

The Company puts special emphasis on the internal control system which monitors business efficiency, regulatory compliance and risks to which the Company is exposed.

HPB Stambena Štedionica d.d.

HPB Stambena Štedionica (hereafter: “the Savings Bank“) is a credit institution which collects long-term savings with a purpose to resolve housing needs of depositors. Furthermore, it approves housing loans bearing fixed interest rates and with state subsidies.

The Savings Bank has change its General Business Conditions 2 times during 2016 (in April and September) related to automatic roll-over of savings and interest rates changes.

Last year was marked by recovery of lending activity (+14.2%) and lower interest rates for interfinancing and regular loans. Deposits have continued on the positive note (+15.4%) despite the interest rates decline. During 2016 the Savings Bank had brokered 9,862 new housing savings contracts with HPB being the primary sales channel. Contracts are also available in Hrvatska Pošta and the Savings Bank's headquarters.

Value of the total housing loans at the end of 2016 was HRK163.5M which is HRK20.3M more than a year before.

Value of total housing deposits was HRK280.2M which is HRK37.4M more than a year before.

At the end of 2016 the Savings Banks’ total assets amounted to HRK331.9M (2015: HRK292.1M) which is a 13.6% increase in 2016.

The Savings Bank recorded net profit in the amount of HRK3.3.M.

At the end of 2016 the Savings Bank had 19 employees.

Development Plan

On business planning front the Savings Bank plans to make positive effects for the whole HPB Group by strengthening its market position and delivering own results. This is planned to achieve by constant cooperation improvement with HPB and intensified cooperation with Hrvatska Pošta.

Considering the housing savings system has stabilized in the last 2 years by introducing variable rate for state subsidies and determining amount of subsidies for each year upfront, the Savings Bank expects new housing savings to increase in volume.

Risk Exposure

Risk management system of the Savings Bank is accomplished by internal risk management acts, through organizational structure with clearly defined responsibilities and authorizations with regard to risk management, through risk management process and through effective internal control system. The Savings Bank expresses its risk tolerance by defining targeted risk profile, while taking into account all demands impacting adequacy of available regulatory capital.

The most important risks to which the Savings Bank is exposed are non-trading book interest rate risk, liquidity risk, market risks, credit risk and operational risk.

The Savings Bank is exposed to non-trading interest risk in the amount of which interest-bearing assets or liabilities mature or change interest rates. Most of the interest-bearing assets and total interest-bearing liabilities have fixed rates which require special attention.

The Savings Bank is exposed to credit risk by lending and investments. Individual credit risk assessment ensures loans to customers are provided in line with the clients' creditworthiness, quality and value of their collateral and credit history.

Liquidity risk management includes operating management of daily liquidity, operating short-term liquidity management and structural liquidity management.

Determining and evaluating operational risk is done by collecting and analyzing internal dana on events due to operational risk, self-assessment of operational risk and quality of controls, assessment of externalization risks, IT risk and analysis of resource unavailability effect on critical processes within going concern management.

The Saving Bank's risk exposure during the whole year was in line with regulatory limits.

HPB Nekretnine d.o.o.

HPB Nekretnine d.o.o. (hereafter “the Company”) is a company specialized in real estate business which started its business activities in August 2005, and is fully owned by the Bank. Shareholders’ equity amounts to HRK0.5M.

Primary business activities of HPB Nekretnine are real estate value estimation, advisory services, project development and real estate transactions.

As of December 31 2015 balance sheet of HPB Nekretnine amounted to HRK9.6M, with net profit of HRK629.9K. At the end of 2015 the Company had 9 employees.

Development Plan

In the upcoming period focus will be on the active market promotion and on further improvements in quality of services rendered. The Company’s business and development policy will be built on expected rise in market demand for specific services which the Company offers, as well as for testing market potential for new consulting and engineering services, which the Company is equipped to offer. The Company should therefore contribute to Group becoming more recognizable, and a synergy effect will be accomplished.

Risks Exposure

Most significant types of risk that the Company is exposed to are: market and liquidity risk. Market risk takes into account that demand volume for specific services offered by the Company is difficult to foresee, especially appraisal of property. Linked directly to this is the liquidity risk due to high share of these services in the Company’s overall offer. The Company manages its risks according to prescribed policies and procedures of HPB described in Note 2.

The Company owns 2 real estates, in Osijek and Vinkovci. Vinkovci real estate poses business risk since the ownership gives 357/ 900 share in dilapidated commercial building with total area of around 10,000 sqm. In the future period a complete reconstruction may be needed and it assumes substantial investment amount relative to the Company's business volume.

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Responsibilities of the Management and Supervisory Boards for the Preparation and Approval of the Annual Financial Reports

The Management Board of the Bank is required to prepare unconsolidated and consolidated financial reports of Hrvatska Poštanska Banka p.l.c. and its subsidiaries for each financial year. These reports give a true and fair view of financial position of the Group and of the results of their operations and cash flows, in accordance with applicable accounting standards. The Management Board is also responsible for maintaining proper accounting records needed for preparation of such financial reports at any given time. Also, the Board is responsible for the whole annual report of the Bank and the Group. The Management Board has a general responsibility for taking available measures aiming to safeguard the Group's assets, 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 reports 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 report on the Group, together with annual financial reports, for acceptance. If the Supervisory Board approves annual financial reports, they are deemed confirmed by the Management and Supervisory Board.

The Management Board is responsible for preparation and contents of the annual report in accordance with the Accounting Act (Official Gazette 109/07, 54/13).

Consolidated financial reports set out on pages between 80 and 185 were approved by the Management Board on April 12 2017 for their issue to the Supervisory Board, which is confirmed by the signature below:

Signed in the name of Hrvatska Poštanska Banka p.l.c.

Tomislav Vuić President of the Management Board	Domagoj Karadjole Member of the Management Board

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Deloitte.

Deloitte d.o.o.
ZagrebTower
Radnička cesta 80
10 000 Zagreb
Croatia
TAX ID: 11686457780

Tel: +385 (0) 1 2351 900
Fax: +385 (0) 1 2351 999
www.deloitte.com/hr

INDEPENDENT AUDITOR'S REPORT

To the owners of Hrvatska poštanska banka dd, Zagreb

Report on the Audit of the Consolidated Financial Statements

Qualified Opinion

We have audited the accompanying consolidated financial statements of Hrvatska poštanska banka dd Group (the Group), which comprise the consolidated statements of financial position as at 31 December 2016, the consolidated statement of profit or loss, consolidated statement of other comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies.

In our opinion, except for the effects of the matter described in the Basis for Qualified Opinion section of our report, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2016, and its financial performance and its cash flows for the year then ended in accordance with statutory accounting requirements for banks in Croatia.

Basis for Qualified Opinion

As explained in Note 12, H1 TELEKOM d.d. ("the Company"), a subsidiary in which the Group holds a controlling interest of 58.2 percent and which was acquired in a debt-to-equity swap as part of the pre-bankruptcy settlement arrangement, is classified as a non-current asset held for sale in accordance with International Financial Reporting Standard 5. The Company has generated a loss in the amount of HRK 26 million and its total liabilities exceed its total assets for the year ended 31 December 2016 by HRK 128 million. The amounts that fell due in accordance with the repayment schedule defined as part of the pre-bankruptcy settlement arrangement in early 2017 have not been entirely settled, and their full settlement depends on whether the sale of the Company, which is currently under way, will be concluded or not. If the sale is not concluded, the ability to raise sufficient funds to settle the outstanding liabilities will become doubtful. This indicates a significant uncertainty that may cast significant doubt as to the ability of the Company to continue as a going concern and consequently the realisation of its assets and the settlement of its liabilities included in the consolidated financial statements of the Group in the amount of HRK 132 million. We were unable to assess at this stage and could not determine whether any adjustments is necessary regarding this matter.

We conducted our audit in accordance with Audit Act and International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Annual Financial Statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together 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 and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

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

INDEPENDENT AUDITOR'S REPORT (continued)

Report on the Audit of the Consolidated Financial Statements (continued)

Key Audit Matters (continue)

Impairment losses on loans to customers

Refer to Notes 3 on pages 138 of the consolidated financial statements for the accounting policies and Note 11 on pages 148 and 149 for the additional information respectively.

Loans are evaluated based on the credit risk associated to the borrower. Impairment losses are recognized on incurred loss basis if there is an objective evidence of impairment. The objective evidence that an impairment loss has been incurred relates to the loss events such as significant financial difficulty of the borrower, inability to repay part or all loan obligations or other breaches of a loan contract. Loss event might be also associated with the situations, if it is becoming probable, that the borrower will enter into pre-bankruptcy or bankruptcy procedures. The assessment of the level of impairment losses depends on the amount of present value of expected future cash flows, which requires significant amount of judgement and use of reasonable estimates from the management on the timing and amount of expected future cash flows. Impairment allowances represent management's best estimate of the losses incurred within the loan portfolios at the balance sheet date.

The Bank recognizes both collective and specific (individual) impairment losses on loans, in accordance with the statutory accounting requirements for banks in Croatia and Croatian National Bank's Decision on the classification of placements and off-balance sheet liabilities of credit institutions (Official Gazette no. 41/14) (the CNB's Decision).

Because of the materiality of the balances, and the subjective nature and significance of judgements over both timing of recognition of impairment and the estimation of the size, impairment losses on loans to customers is a key area of focus.

How our audit addressed the key audit matter

We have obtained the understanding of the provisioning process and relevant controls and control activities that the Bank has designed, implemented and maintained, in relation to the process of loan impairment losses.

Operating effectiveness of controls

We evaluated the design and implementation, and operating effectiveness of the key controls in the process such as:

- Timely identification of the impairment events and potentially impaired loans;
- Controls over the impairment calculation models including data inputs and process of determining key assumptions and estimates;
- Controls over the collateral valuation estimates;
- Governance over the process including the continuous re-assessment by management to make sure that the impairment calculations are still appropriate for the impairment risks associated with both the collective impairment and specific impairment;
- The review and approval process that the management put in place for the outputs generated by the Bank's impairment models.

Further to the procedures related to the operating effectiveness of controls, we challenged the appropriateness of management's processes and key assumptions used in the calculations of impairment for loans and advances and assessed whether the provisions are in accordance with the statutory accounting requirements for banks in Croatia and CNB's decision.

INDEPENDENT AUDITOR'S REPORT (continued)

Report on the Audit of the Consolidated Financial Statements (continued)

Key Audit Matters (continued)

Impairment losses on loans to customers (continued)

How our audit addressed the key audit matter (continued)

Individually impaired loans

Based on the selected sample of loans including loans that had not been identified by the management as potentially impaired, we challenged the impairment losses recognized on those loans. In determining the sample for our substantive procedures, we analysed the population in order to identify our focus areas. We have selected a sample of loans considering, but not limited to, credit risk groups and changes in the credit risk groups of the borrower, the number of days past due, industry of the borrower, unsecured exposures, restructured exposures, understanding of the business of individual borrowers from prior audits, pre-bankruptcies and bankruptcies loan cases. Special attention has been given in respect of the non-performing loans that were not derecognized at 31 December 2016 but have been considered for sale of non-performing loans during the year.

On the selected sample of loans, we assessed critically the criteria for determining whether an impairment event had occurred and therefore whether there was a requirement to calculate an impairment provision. We tested a sample of performing loans with the features of potential loss events in order to challenge the management's identification of such events. On the sample of individually impaired loans, we gained understanding of the current borrower's financial position and latest developments and considered whether the key assumptions and estimates properly addressed the borrower's circumstances. We tested the key inputs in the impairment calculation, including valuation reports of the collateral (if they were conducted in accordance with the local regulation), realization period and value of the collateral at the projected realization date and level of the expected cash flows from borrower's operations. We have also considered the specific requirements of the CNB Decision regarding the loans that are non-performing for over 90 days.

In some cases we applied our own judgment to assess the inputs to the calculation of impairment losses on loans and compared our own calculation of the impairment losses per selected loans with the one obtained from the Bank.

Collective impairment losses

We have gained an understanding of the Bank's provisioning process, methodology and parameters used in the calculation of collective impairment losses on loans in order to evaluate the overall adequacy of the collective impairment level.

We have recalculated the management's calculation to assess whether the Bank, for performing loans (class A under the CNB's Decision), adheres to the minimum of 0.80% of the total exposure.

INDEPENDENT AUDITOR'S REPORT (continued)

Report on the Audit of the Consolidated Financial Statements (continued)

Key Audit Matters (continued)

Selling part of non-performing portfolio

Refer to Note 12 on pages 150 and 151 of the consolidated financial statements for the accounting policies.

At the year end, the Bank finished the process of selling part of its non-performing corporate and retail loan portfolio and signed the sale and purchase agreement covering both portfolios. As at year-end the sale of the retail non-performing portfolio was realised and it was derecognised in the statement of financial position as at 31 December 2016. The sale of corporate non-performing portfolio was realized in the first month of 2017, and this portfolio was presented as non-current assets held for sale in accordance with the International Financial Reporting Standard 5 (the "IFRS5") in the statement of the financial position as at 31 December 2016.

We considered the measurement and derecognition of each portfolio and accounting treatment of this event as a key audit matter because of its size and complexity. The key audit matter refers to the appropriate classification of the non-performing loan portfolio with a specific focus on adequate measurement.

How our audit addressed the key audit matter

We gained an understanding of the transaction and the key dates such as closing date and other circumstances surrounding the transaction. We have challenged the accounting policies and applied accounting treatment for both retail and corporate portfolio. We have investigated if the accounting treatment adequately reflects derecognition of retail portfolio and classification and presentation of the corporate portfolio disclosed in accordance with IFRS 5 as of 31 December 2016 and if the treatment itself was in accordance with the statutory accounting requirements for banks in Croatia.

Based on our understanding of the transaction and information obtained from the Bank, we assessed if the measurement of the corporate portfolio presented as IFRS5 was in accordance with the statutory accounting requirements for banks in Croatia.

We performed the audit procedures after the reporting date for the purpose of ascertaining the occurrence of subsequent events for the corporate portfolio, i.e. payment made by the buyer, that were essential to a fair presentation of the considered corporate non-performing portfolio as of 31 December 2016.

We also reviewed the disclosures included in the Bank's financial statements to assess if they contain sufficient information to make the transaction understandable to users of the financial statements.

Deloitte.

INDEPENDENT AUDITOR'S REPORT (continued)

Report on the Audit of the Consolidated Financial Statements (continued)

Key Audit Matters (continued)

Foreclosed assets

Refer to Note 3 on pages 134 to 138 of the consolidated financial statements for the accounting policies and Notes 15 and 18 on pages 155 to 159 for the additional information respectively.

Foreclosed assets relate to tangible assets acquired in exchange for the uncollected loan receivables. In prior years, these assets were measured at the lower of its carrying amount and fair value less costs to sell, in accordance with the IFRS 5. In 2016, the Bank changed the accounting treatment and ceased to classify the assets as held for sale, because the criteria of a highly probable sale was not met. Subsequently, foreclosed assets were recognized in accordance with the International accounting standard 40 "Investment property" (the "IAS 40") and measured at fair value.

For the last three consecutive years, the Bank has been recognising significant impairment losses on these assets, as a result of subsequent measurement based on the independent valuation reports.

The management estimated the fair value of the Bank's foreclosed assets to be HRK 87 million as at 31 December 2016 with a loss of HRK 9 million recognised in the statement of profit and loss for the year ended 31 December 2016. The independent external valuations were obtained in order to the support management's estimates. The valuations are dependent on certain key assumptions that require significant management judgement including the capitalisation rates, market rent for the properties and the market transaction prices for land.

There were changes in the key assumptions this financial year that took into consideration the current situation on the market for each respective real estate and resulted in the decrease of fair values of the appraised real estates.

The key audit matter refers to the appropriate classification and measurement of the material investment properties.

How our audit addressed the key audit matter

Our procedures in relation to the value of the investment properties included:

- Evaluation of the independent external valuers' competence, capabilities and objectivity;
- Assessing the methodologies applied and the appropriateness of the key assumptions based on our knowledge of the property use and location using our in-house valuation experts; and
- Checking, on a sample basis, the accuracy and relevance of the input data used;

We have evaluated the available evidence used for key assumptions such as, available market rates applied. We challenged if the applied markets rates were supported by most recent renewals and capitalisation rates. We also challenged if the methodologies in the land appraisals reflected the market transaction prices and other assumptions proscribed by local regulations. Special attention has been given in respect of the foreclosed that were recognized in the statement of financial position as at 31 December 2016 but have been considered for sale during the year.

Deloitte.

INDEPENDENT AUDITOR'S REPORT (continued)

Report on the Audit of the Consolidated Financial Statements (continued)

Other Information

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

Our opinion on the financial statements does not cover the other information.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. With respect to the Management Board Report and the Declaration of application of the Code of Corporate Governance, which are included in the Annual Report, we have also performed the procedures prescribed by the Accounting Act.

These procedures include examination of whether the Management Board Report and Declaration of application of the Code of Corporate Governance include required disclosures as set out in Articles 21, 22 and 24 of the Accounting Act and whether the Declaration of application of the Code of Corporate Governance includes the information specified in Articles 22 and 24 of the Accounting Act.

Based on the procedures performed during our audit, to the extent we are able to assess it, we report that:

1) Information included in the other information is, in all material respects, consistent with the consolidated financial statements.
2) Management Board Report for the year 2016 has been prepared, in all material respects, in accordance with Article 21 and Article 24 of the Accounting Act.
3) Declaration of application of the Code of Corporate Governance has been prepared, in all material aspects, in accordance with Article 22, paragraph 1, items 3 and 4 and Article 24 of the Accounting Act, and also includes the information from Article 22, paragraph 1, points 2, 5, 6 and 7 and Article 24, paragraph 2.

Based on the knowledge and understanding of the Group and its environment, which we gained during our audit of the consolidated financial statements, we have not identified material misstatements in the other information. We have nothing to report in this respect.

Responsibilities of the Management and Supervisory Boards for the Consolidated Financial Statements

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

In preparing the consolidated financial statements, the Management Board is responsible for assessing 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 Group or to cease operations, or has no realistic alternative but to do so.

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

Auditor's Responsibilities for the Audit of the Financial Statements

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

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

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

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

Deloitte.

INDEPENDENT AUDITOR'S REPORT (continued)

Report on the Audit of the Consolidated Financial Statements (continued)

Auditor's Responsibilities for the Audit of the Financial Statements (continued)

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

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

Branislav Vrtačnik

President of the Management Board

Vanja Vlak

Certified auditor

Deloitte d.o.o.

Zagreb, 12 April 2017

Radnička cesta 80,

10 000 Zagreb,

Croatia

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Consolidated Report of Financial Position
at December 31 2016

	Notes	2016 HRK'000	2015 HRK'000
ASSETS			
Cash and Amounts Due from Banks	5	1,554,612	1,630,115
Mandatory Reserve with the Croatian National Bank	6	1,300,796	1,279,570
Loans to and Receivables from Banks	7	182,087	261,913
Financial Assets at Fair Value in PNL	8	1,019,441	1,019,694
Financial Assets Available for Sale	9	2,753,938	2,221,310
Financial Assets Held to Maturity	10	444,825	571,764
Loans and Receivables from Customers	11	11,554,215	10,298,014
Assets Held for Sale	12	89,349	7,930
Property and Equipment	13	140,765	142,236
Investment Property	14	96.518	9,568
Intangible Assets	15	107,360	117,010
Deferred Tax Assets, Net	16	39,189	10,750
Tax Prepayment		347	371
Other Assets	17	454,384	443,828
TOTAL ASSETS		**19,737,826**	**18,014,073**
LIABILITIES			
Financial Liabilities at Fair Value in PNL	18	3,641	-
Deposits from Banks	19	509,133	357,639
Customer Deposits	20	16,024,804	14,493,594
Borrowings	21	726,660	1,005,383
Provisions for Liabilities and Expenses	22	60,787	36,723
Corporate Tax Liability		58	-
Other Liabilities	23	467,439	341,903
TOTAL LIABILITIES		**17,792,522**	**16,235,242**
EQUITY			
Share Capital	24	1,214,775	1,214,775
Capital Gain	24	-	-
Own Shares	24	(477)	(477)
Reserves for Own Shares	24	4,477	477
Statutory Reserve	24	6,161	-
Other Reserves	24	358,306	358,306
Fair Value Reserve	24	84,690	82,089
Revaluation Reserve	24	839	877
Retained Earnings	24	86,030	(1,993)
Profit for the Year		190,503	124,777
TOTAL EQUITY		**1,945,304**	**1,778,831**
TOTAL LIABILITIES AND EQUITY		**19,737,826**	**18,014,073**

The significant accounting policies and other notes on pages 85-185 form an integral part of these financial reports.

Consolidated PNL Report
for the Year Ended December 31 2016

	Notes	2016 HRK'000	2015 HRK'000
Interests and Similar Income	25	733,389	792,827
Interests and Similar Expense	26	(213,940)	(278,497)
Net Interest Income		**519,449**	**514,330**
Fees and Commissions Income	27	508,934	495,327
Fees and Commissions Expense	28	(310,183)	(302,343)
Net Fees and Commissions Income		**198,751**	**192,985**
Gains Less Losses Arising from Securities at Fair Value in PNL	29	26,249	6,042
Gains Less Losses Arising from Securities Available for Sale	30	48,596	1
Gains Less Losses Arising from Dealing in Foreign Currencies		43,408	40,656
Other Operating Income	31	10,082	41,923
Trading and Other Income		**128,335**	**88,622**
Operating Income		**846,535**	**795,936**
General and Administrative Expenses	32	(409,497)	(427,524)
Depreciation and Amortization	13,14,15	(45,416)	(46,053)
Impairment Losses on Loans and Receivables from Customers and Other Assets	33	(201,293)	(184,657)
Provisions for Liabilities and Expenses	22	(25,384)	(9,023)
Total Expenses and Provisions		**(681,590)**	**(667,257)**
PROFIT BEFORE TAX		**164,945**	**128,679**
Deferred Income Tax (Expense)/ Income	34	25,558	(3,902)
PROFIT FOR THE YEAR		**190,503**	**124,777**

The significant accounting policies and other notes on pages 85-185 form an integral part of these financial reports.

Consolidated Report of Comprehensive Income for the Year Ended December 31 2016

	2016	2015
	HRK'000	HRK'000
Profit/ (Loss) for the Year	**190,503**	**124,777**
Other Comprehensive Income		
Items that will not be reclassified subsequently to profit or loss:		
Revaluation Reserve	(73)	(73)
Income Tax Relating to Items That Will Not Be Reclassified Subsequently	35	63
	(38)	**(10)**
Items that may be reclassified subsequently to profit or loss:		
Gains from Financial Assets Available for Sale	45,506	11,525
Sale of Financial Assets Available for Sale	(44,836)	-
Income Tax Relating to Items That May Be Reclassified Subsequently	1,931	(2,303)
	2,601	**9,222**
Other Comprehensive Gains for the Year	**2,563**	**9,212**
Total Comprehensive Income for the Year, Net of Income Tax	**193,066**	**133,989**

	2016	2015
	HRK'000	HRK'000
Profit/ (Loss) for the Year	**190,503**	**124,777**
The Bank's Owners	190,503	124,777
Profit/ (Loss) Per Share		
From active and discontinued operations:		
Basic (in HRK per Share)	94.13	86.00
Diluted (in HRK per Share)	94.13	86.00

The significant accounting policies and other notes on pages 85-185 form an integral part of these financial reports.

Consolidated Report of Changes in Equity for the Year Ended December 31 2016

	Share Capital	Capital Gain	Own Shares	Reserve for Own Shares	Other Reserves	Fair Value Reserve	Revaluation Reserve	Retained Earnings	Profit/ (Loss) for the Year	Total
	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000
Balance at January 1 2015	**966,640**	**228,136**	**(875)**	**875**	**10,578**	**72,867**	**887**	**193,010**	**(629,390)**	**842,728**
Revaluation Reserve	-	-	-	-	-	-	(73)	-	-	**(73)**
Change in the Fair Value of Financial Assets Available for Sale	-	-	-	-	-	11,525	-	-	-	**11,525**
Deferred Tax	-	-	-	-	-	(2,303)	63	-	-	**(2,240)**
Net Profit (Loss) for 2015	-	-	-	-	-	-	-	-	124,777	**124,777**
Total Comprehensive Income for the Year 2015	**-**	**-**	**-**	**-**	**-**	**9,222**	**(10)**	**-**	**124,777**	**133,989**
Transfer of 2014 Loss	-	-	-	-	-	-	-	(629,390)	629,390	**-**
Loss Coverage from 2014	-	-	-	-	-	-	-	-	-	**-**
-Transfer from Statutory Reserve	-	-	-	-	(10,578)	-	-	10,578	-	**-**
- Transfer from Capital Gain	-	(228,136)	-	-	-	-	-	228,136	-	**-**
Decrease of Share Capital	-	-	-	-	-	-	-	-	-	**-**
-Coverage of Uncovered Loss	(195,673)	-	-	-	-	-	-	195,673	-	**-**
-Transfer to Other Reserves	(358,306)	-	-	-	358,306	-	-	-	-	**-**
Increase of Share Capital	802,114	-	-	-	-	-	-	-	-	**802,114**
Other Changes	-	-	398	(398)	-	-	-	-	-	**-**
Balance at December 31 2015	**1,214,775**	**-**	**(477)**	**477**	**358,306**	**82,089**	**877**	**(1,993)**	**124,777**	**1,778,831**
Balance at January 1 2016	**1,214,775**	**-**	**(477)**	**477**	**358,306**	**82,089**	**877**	**(1,993)**	**124,777**	**1,778,831**
Revaluation Reserve	-	-	-	-	-	-	(73)	-	-	**(73)**
Change in the Fair Value of Financial Assets Available for Sale	-	-	-	-	-	45,506	-	-	-	**45,506**
Sale of Financial Assets Available for Sales	-	-	-	-	-	(44,836)	-	-	-	**(44,836)**
Deferred Tax	-	-	-	-	-	1,931	35	-	-	**1,966**
Net Profit for 2016	-	-	-	-	-	-	-	-	190,503	**190,503**
Total Comprehensive Income for the Year 2016	**-**	**-**	**-**	**-**	**-**	**2,601**	**(38)**	**-**	**190,503**	**181,760**
Distribution of 2015 Profit	-	-	-	-	-	-	-	-	-	**-**
- Transfer to Retained Earnings	-	-	-	-	-	-	-	83,854	(83,854)	**-**
- Transfer to Statutory Reserves	-	-	-		6,161	-	-	-	(6,161)	**-**
- Trasfer to Reserves of Own Shares	-	-	-	4,000	-	-	-	-	(4,000)	**-**
- Dividend Payments	-	-	-	-	-	-	-	-	(30,762)	**(30,762)**
- Other Changes	-	-	-	-	-	-	-	4,169	-	**4,169**
Balance at December 31 2016	**1,214,775**	**-**	**(477)**	**4,477**	**364,467**	**84,690**	**839**	**86,030**	**190,503**	**1,945,304**

The significant accounting policies and other notes on pages 85-185 form an integral part of these financial reports.

	Notes	2016 HRK'000	2015 HRK'000
Cash Flows from Operating Activities			
Profit/ (Loss) Before Taxation		164,945	128,679
Adjusted by:			
- Depreciation and Amortization	13,14,15	45,416	46,053
- Foreign Exchange Gains	31	(4,682)	(9,669)
- Net Impairment Losses on Loans and Receivables from Customers and Other assets	33	201,293	184,657
- Provisions for Liabilities and Expenses	22	25,384	9,023
- Net Unrealized Gains on Financial Assets at Fair Value in PNL	29	(25,655)	(7,916)
Changes in Operating Assets and Liabilities			
Net Decrease in Loans to and Receivables from Banks		13,253	69,740
Net (Increase)/ Decrease in Financial Assets at Fair Value in PNL		25,908	(629,977)
Net (Increase)/ Decrease in Loans to and Receivables from Customers		(1,500,963)	(18,281)
Net Decrease in Other Assets		97,523	51,744
Net Decrease in Deposits from Banks		151,494	(17,111)
Net Increase/ (Decrease) in Customer Deposits		1,532,603	414,977
Net Decrease in Other Liabilities		5,329	(235,416)
Net Cash (Outflow)/ Inflow from Operating Activities Before Tax		**731,848**	**(13,497)**
Income Tax Paid		(171)	(318)
Net Cash (Outflow)/ Inflow from Operating Activities		**731,677**	**(13,815)**
Cash Flows from Investing Activities			
Purchases of Property, Equipment and Intangible Assets		(42,415)	(18,982)
Disposal of Financial Assets Available for Sale		731,876	670,446
Acquisition of Financial Assets Available for Sale		(1,263,834)	(882,317)
Maturity of Financial Assets Held to Maturity		128,028	23,394
Dividends Received		827	1,073
Net Cash Outflow from Investing Activities		**(445,518)**	**(206,386)**
Cash Flows from Financing Activities			
Dividend Payment		(30,762)	-
Increase in Borrowings		80,604	44,384
Repayments of Borrowings		(359,327)	(546,328)
Increase in Share Capital		-	550,000
Net Cash Inflow from Financing Activities		**(309,485)**	**48,056**
Effect of Foreign Exchange Differences on Cash and Cash Equivalents		813	2,999
Net (Decrease)/ Increase in Cash and Cash Equivalents		**(22,513)**	**(169,146)**
Cash and Cash Equivalents at the Beginning of the Year	37	**3,247,114**	**3,416,260**
Cash and Cash Equivalents at the End of the Year	37	**3,224,601**	**3,247,114**

The significant accounting policies and other notes on pages 85-185 form an integral part of these financial reports.

1. SIGNIFICANT ACOUNTING POLICIES

Hrvatska Poštanska Banka p.l.c. Zagreb is a joint stock company incorporated and domiciled in the Republic of Croatia, Jurišićeva 4, Zagreb. The Bank is the parent of the Hrvatska Poštanska Banka Group.

The Bank has control over following subsidiaries that make the HPB Group:

	Industry	**State**	**Ownership as of December 31 2016 %**
HPB Invest Ltd	Investment Funds Management	Croatia	100.00
HPB Nekretnine d.o.o.	Real Estate Agency and Construction	Croatia	100.00
HPB Stambena Štedionica d.d.	Savings Bank	Croatia	100.00

In addition to investments in subsidiaries, consolidated financial position includes the following investment held for sale:

	Industry	**State**	**Ownership as of December 31 2016 %**
H1 Telekom plc.	Telecommunications	Croatia	58.17

Investment in H1 Telekom plc. is provided in Note 12.

These financial reports comprise consolidated financial reports of the Group as defined in International Financial Reporting Standard 10 “Consolidated Financial Report”.

These financial reports were approved by the Management Board on April 12 2017 for submission to the Supervisory Board.

The principal accounting policies used for preparation of these financial reports are summarized below. Where specific accounting policies are aligned with accounting principles of International Financial Reporting Standards, in describing the accounting policies of the Group, it can refer to certain standards; and unless otherwise stated, these references are for standards applicable at December 31 2016.

1. SIGNIFICANT ACOUNTING POLICIES (continued)

a) Statement of Compliance

These financial reports are prepared in accordance with the legal requirements applicable to accounting for banks in the Republic of Croatia. The Group's financial reporting is regulated by the Croatian National Bank which is the central supervisory institution of Croatian banking system. These financial reports have been prepared in accordance with the above-mentioned banking regulations.
These statutory financial reports are prepared for the purpose of compliance with legal requirements and for general information and not for any specific purpose or transaction. Accordingly, users should not rely exclusively on these financial reports and should undertake other appropriate inquiries before making decisions.

The accounting regulations of the CNB rely on International Financial Reporting Standards ("IFRSs") adopted by European Union. The principal differences between the accounting regulations of the CNB and recognition and measurement requirements of International Financial Reporting Standards are as follows:

- Although the Group calculates impairment losses on corporate lending as the present value of the expected future cash flows, discounted at the instrument's original effective interest rate, in accordance with International Financial Reporting Standards, the CNB requires the amortization of the discount calculated to be presented in the PNL report within the movement on impairment losses on loans and receivables to customers and other assets, rather than as interest income, as required by International Financial Reporting Standards.

- Suspended interests are accrued but not paid interests on individually impaired assets. At the moment of reclassification the Group impairs the total adjusted value of accrued but not paid interests in PNL report. Furthermore, further financial position accrual is suspended, with interests being booked off-balance sheet until the debtor makes a payment. This accounting procedure is not in line with the IFRS 18 “Revenue” and IFRS 39 “Financial Instruments: Recognition and Measurement” which require the interest revenue from impaired financial assets to be calculated by using effective interest rate method.

- In line with amendments to CNB's Decision on the classification of placements and off-balance sheet liabilities of credit institutions, in force from October 1 2013, CNB prescribes minimum levels of impairment losses for certain specifically identified impaired exposures, which may be different from impairment loss calculated in accordance with International Financial Reporting Standards (IFRSs).

- In line with the CNB's Decision on Provisions for Court Cases Agains the Credit Institution of March 31 2010 there are minimum requirements for the provisions for court cases the credit institution is obliged to keep. In line with the Decision a credit institution must diversify court cases into risk categories depending on the loss probability and form provisions accordingly. However in certain cases required reserves may differentiate from the ones calculated on the basis of the International Financial Reporting Standards (IFRS).

The accounting policies are the same as in the preparation of annual financial reports for the year ended December 31 2015.

1. SIGNIFICANT ACOUNTING POLICIES (continued)

b) Basis of Preparation

These financial reports represent the general-purpose financial reports of the Group. The financial reports were prepared for the reporting period from January 1 2016 to December 31 2016 in compliance with existing accounting regulations applicable in Croatia.

The financial reports are prepared on the fair value basis for financial assets and liabilities at fair value in PNL, assets available for sale, derivative financial instruments and property and repossessed assets except those for which a reliable fair value measurement is not available. Other financial assets and liabilities, and non-financial assets and liabilities, are stated at amortized or historical cost.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the Group takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date. Fair value for measurement and/ or disclosure purposes in these consolidated financial reports is determined on such a basis, except for share-based payment transactions that are within the scope of IFRS 2, leasing transactions that are within the scope of IAS 17, and measurements that have some similarities to fair value but are not fair value, such as net realizable value in IAS 2 or value in use in IAS 36.

In addition, for financial reporting purposes, fair value measurements are categorized into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

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

1. SIGNIFICANT ACOUNTING POLICIES (continued)

b) Basis of Preparation (continued)

In preparing the financial reports, management is required to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities and disclosure of commitments and contingencies at the reporting date, as well as amounts of income and expense for the period. Estimates and underlying assumptions are based on historical experience and various other factors that are believed to be reasonable under current circumstances, the results of which form the basis of making the judgments about the carrying amounts of assets and liabilities that are not readily apparent from other sources. Actual results may differ from those estimates.

Estimates and underlying assumptions are reviewed on a regular basis. Revisions to accounting estimates are recognized 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 financial reports and estimates with a significant risk of material adjustment in the next year are discussed in Note 2.

1. SIGNIFICANT ACOUNTING POLICIES (continued)

b) Basis of Preparation (continued)

New Standards, Interpretation and Changes of Published Standards

(I) New and changed International Financial Reporting Standards are referred to the reporting period with evaluated effect on financial reports:

- **IFRS 14 Regulatory Deferral Accounts** (in effect for annual period on and after January 1 2016),
- **Changes of IFRS 10 Consolidated Financial Statements, IFRS 12 Disclosure of Interests in Other Entities, and IFRS 28 Investments in Associates and Joint Ventures** – „Investment Entities: Applying the Consolidation Exception" adopted by the EU on September 22 2016 (in effect for annual periods on and after January 1 2016),
- **Changes of IFRS 11 Joint Arrangements** – „Accounting for Acquisitions of Interests in Joint Operations" adopted by the EU on November 24 2015 (in effect for annual periods on and after January 1 2016),
- **Changes of IAS 1 Presentation of Financial Reports** – „Disclosure Initiative" adopted by the EU on December 18 2015 (in effect for annual periods on and after January 1 2016),
- **Changes of IAS 16 Property, Plant and Equipment, and IAS 38 Intangible Assets** – „Clarification of Acceptable Methods of Depreciation and Amortization" adopted by the EU on December 2 2015 (in effect for annual periods on and after January 1 2016),
- **Changes of IAS 16 Property, Plant and Equipment, and IAS 41 Agriculture** – „Bearer Plants" adopted by the EU on December 17 2014 (in effect for annual periods on and after January 1 2016),
- **Changes of IAS 27 Consolidated and Separate Financial Reports** – „Equity Method in Separate Financial Reports" adopted by the EU on December 18 2015 (in effect for annual periods on and after January 1 2016),
- **Changes of multiple standards under Annual Improvements to IFRSs 2010-2012 Cycle** are a result of improving IFRSs (IFRS 2, IFRS 3, IFRS 8, IFRS 13, IFRS 16, IFRS 24 and IFRS 38) mainly for the purpose of removing incongruity and text clarification adopted by the EU on December 17 2014 (in effect for annual periods on and after February 1 2016),
- **Changes of multiple standards under Annual Improvements to IASs 2012-2014 Cycle** are a result of improving IASs (IAS 5, IAS 7, IAS 19 and IAS 34) mainly for the purpose of removing incongruity and text clarification adopted by the EU on December 15 2015 (in effect for annual periods on and after January 1 2016).

The aforementioned changes did not have materially significant effect on the Group's financial reports.

1. SIGNIFICANT ACOUNTING POLICIES (continued)

b) Basis of Preparation (continued)

New Standards, Interpretation and Changes of Published Standards

(II) The new and revised published standards which take effect after the reporting period:

- **MSFI 9 Financial Instruments**, adopted by the EU on December 22 2016 (in effect for annual periods on and after January 1 2018 with possible earlier application)

The standard replaces the IAS 39 Financial Instruments: Recognition and Measurement and contains requirements for recognition and measurement, impairment, derecognition and hedge accounting.

Classification and measurement – IFRS 9 introduces a new approach in classifying financial assets based on cash flow and business model of the certain financial assets. New approach implies a unique impairment model applied for all financial instruments.

Impairment – IFRS 9 introduces a new impairment model based on expected losses which enables timely recording of expected credit losses.
Hedge accounting – IFRS 9 introduces a substantially improved hedge accounting model which assumes more information on risk management activities.

The Bank has started the IFRS 9 project in 2016. The project assumes following phases:

- A number of educations in order to familiar the Bank's employees with the IFRS 9 and its requirements
- Gap analysis with focus on a gap between the current condition and the IFRS 9 classification and measurement requirements
- Determining business models
- Determining characteristics of contracted cash flows
- Gap analysis with focus on a gap between the current condition and the IFRS 9 impairments
- Analysis of the IFRS 9 quantitative effect
- Creating functional specifications for certain application, i.e. introduction of a proper software
- Creating impairment methodology in accordance with the Bank's business models – creating a model for calculating risk parameters used in calculating expected credit losses according to the IFRS 9.

On the classification and measurement front the Bank considers options of defining business models and other IFRS 9 requirements in line with determined gaps and activities which assume their narrowing.

On the impairment front the Bank works on defining a methodology for calculating expected credit losses and modelling risk parameters which includes all parameters needed for forecasting future movements of certain factors.

On the classification and measurement front the quantitative effect of the standard on the Bank's financial reports will be determined in 2017. The impairment effect depends on methodology for calculating expected credit losses and modelling risk parameters based on expected credit losses.

On the reporting front this standard will have a substantial impact on the Bank's financial reports. The Management has undertaken certain activities to assure all the needed data and methodology for preparing financial results will be applicable in the future periods.

1. SIGNIFICANT ACOUNTING POLICIES (continued)

b) Basis of Preparation (continued)

New Standards, Interpretation and Changes of Published Standards (continued)

(II) The new and revised published standards which take effect after the reporting period (continued):

Certain number of changes in standards by the EU Commission is in progress.

- **IFRS 15 Revenue from Contracts with Customers and changes to the IFRS 15 „Effective IFRS 15 Date“** adopted by the EU on September 22 2016 (in affect for annual periods on and after January 1 2018). This standard affects the model for recognizing revenue from contracts with customers.

With current business strategy adoption of the mentioned IFRS will have no effect on the Group after the initial application.

(III) The new and revised published but not yet adopted standards which will take effect after the reporting period:

IFRSs adopted by the EU have few changes compared to the regulation by the International Accounting Standards Board (IASB), which include following standards, changes and interpretations which were not yet adopted as of March 23 2017 (following effective dates relate to the IFRSs as a whole):

- **IFRS 16 Leases** (will take effect for annual periods on and after January 1 2019). The Standard is still not adopted by the EU. It determines principles of recognition, measurement, stating and reporting leases for the both parties lessor and the lessee.

With current business strategy adoption of the mentioned IFRS will have no effect on the Group after the initial application.

- **Changes of IFRS 2 Share-Based Payment** - „Classification and measurement of share-based payment transactions“ (will take effect for annual periods on and after January 1 2018 or the ones when financial instruments are first used),

- **Changes of IFRS 4 Insurance Contracts –** „Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts“ (will take effect for annual periods on and after January 1 2018),

- **Changes of IFRS 10 Consolidated Financial Statements and IFRS 28 Investments in Associates and Joint Ventures –** sale or investing assets between an investor and its dependent entity or joint venture and further changes (initial effect date is postponed until the research project on applying share method is completed),

- **Changes of IAS 7 Statement of Cash Flows** – „Disclosure Initiative“ (will take effect for annual periods on and after January 1 2017),

- **Changes of IAS 40 Investment Property – „Transfer of Investment Property“** (will take effect for annual periods on and after January 1 2018),

1. SIGNIFICANT ACOUNTING POLICIES (continued)

b) Basis of Preparation (continued)

New Standards, Interpretation and Changes of Published Standards (continued)

(III) The new and revised published but not yet adopted standards which will take effect after the reporting period (continued):

- **Changes of multiples standards under Annual Improvements to IFRSs 2014-2016 Cycle** are a result of improving IFRSs (IFRS 1, IFRS 12 and IFRS 28) mainly for the purpose of removing incongruity and text clarification (Changes for IFRS 12 will take effect for annual periods on and after January 1 2017, while IFRS 1 and IFRS 28 on and after January 1 2018),

- **Interpretation of IFRIC 22 Foreign Currency Transactions and Advance Consideration** (will take effect for annual periods on and after January 1 2018).

The Group does not expect the aforementioned changes to have substantial impact on financial results after the initial application.

- **Changes of IAS 12 Income Taxes** – „Recognition of deferred tax assets for unrealized losses“ (will take effect for annual periods on and after January 1 2017).

The Group does not expect the aforementioned change to have substantial impact on financial results after the initial application

c) ***Functional and Presentation Currency***

The Group's financial reports are presented in Croatian kuna (HRK), which is the functional currency. Amounts are rounded to the nearest thousand (unless otherwise stated).

d) Changes in Presentation or Classification of the Items in the Financial Reports

There were no changes in the classification of the significant amounts or items in the financial reports in the reporting period with the exception of:

(I) reclassification of HRK81,419K in loans and receivables to financial assets available for sale. The Group has contracted a sale of the reclassified receivables portfolio, and up until receiving proceeds of the sale (in January 2017) the Group classifies the assets in accordance with the IFRS 5: Noncurrent Assets Held for Sale and Discontinued Operations, and

(II) in late 2016 the Group has reclassified fixed assets acquired by converting uncollected receivables in the amount of HRK186,017K to property investments. Impairments of the reclassified assets were HRK98,808K and the book value of the assets were HRK87,209K. The assets were initially recognized as available for sale but due to holding it long-term and inability to make a sale in a reasonable period it no longer fulfills criteria to be classified as available for sale according to the IFRS 5: Noncurrent Assets Held for Sale and Discontinued Operations.

1. SIGNIFICANT ACOUNTING POLICIES (continued)

e) Basis of Consolidation

Financial reports are presented for the Group. The Group financial reports comprise the consolidated financial reports of the parent company and its subsidiaries: HPB Nekretnine d.o.o., a real estate agency; HPB Invest Ltd, an investment fund management company; and HPB Stambena Štedionica d.d., a specialized financial institution involved in collecting deposits from retail customers and granting subsided housing loans to Croatian citizens in the Republic of Croatia. In the consolidated financial position the results of the company H1 Telekom plc. are included, in which the parent company has a controlling ownership interest of 58.17% gained in the process of the pre-bankruptcy settlement through the debt to equity swap, and it is classified as an asset held for sale. In addition to this majority stake, all other subsidiaries are 100% owned by the parent company, and all have been established and domiciled in Croatia.

Investments in subsidiaries are disclosed at purchase cost, minus possible impairments, with the exception of investments in H1 Telekom plc. which are disclosed at the lower of carrying amount and fair value in the separate financial reports of the parent company. Investments in subsidiaries are consolidated in the consolidated financial reports of the Group.

Subsidiaries

Subsidiaries are all enterprises controlled by the Group's parent company. Consolidation of a subsidiary begins when the Company obtains control over the subsidiary and ceases when the Company loses control of the subsidiary. Specifically, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated report of profit or loss and other comprehensive income from the date the Company gains control until the date when the Company ceases to control the subsidiary. Profit or loss and each component of other comprehensive income are attributed to the owners of the Company and to the non-controlling interests. Total comprehensive income of subsidiaries is attributed to the owners of the Company and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance. When necessary, adjustments are made to the financial reports of subsidiaries to bring their accounting policies into line with the Group's accounting policies, except for H1 Telekom plc. which is acquired in pre-bankruptcy settlement and classified as an asset held for sale.

Transactions Eliminated on Consolidation

All intragroup assets and liabilities, equity, income and expenses relating to transactions between members of the Group are eliminated in full on consolidation, except for H1 Telekom plc.

The purchase cost method of accounting is used to account for the acquisition of subsidiaries at the Group. The cost of acquiring a subsidiary is measured at fair value of assets given, equity instruments issued and of liabilities incurred or assumed as of the date of exchange, increased by all costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair value at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired, including intangible assets, is recorded as goodwill.

If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized directly in the PNL report.

1. SIGNIFICANT ACOUNTING POLICIES (continued)

e) Basis of Consolidation (continued)

Intragroup balances and any unrealized gains and losses or income and expenses arising from intragroup transactions, are eliminated in preparing the consolidated financial reports.

Company H1 Telekom plc. is consolidated in line with IFRS 5 „Non-current Assets Held for Sale and Discontinued Operations". According to IFRS 5, H1 Telekom plc. is classified as discontinued operation acquired exclusively with an intent to be disposed of through sale.

In line with Guidelines for application of IFRS 5, which include shortcut method of consolidation for a subsidiary held exclusively for sale, company H1 Telekom plc. is consolidated by shortcut method. Shortcut method of consolidation is permitted because it avoids the burden of full disclosure of fair value according to IFRS 3 „Business combinations", and therefore enables that subsidiaries be treated as one-off investments.

In order for the Group to be in line with the main concept of shortcut consolidation by which H1 Telekom plc. is treated one-off investment by following guidelines:

- at inception the Group measured acquired assets at fair value less costs to sell, plus fair value of ascertainable liabilities,
- as per the date of preparation of reports the Group has measured acquired assets at fair value less costs to sell, plus fair value of ascertainable liabilities,
- as per the date of report the Group presented above mentioned assets and liabilities apart from its other assets and liabilities within the consolidated financial report,
- in PNL the Group presents total profit or loss after tax from subsequent measurement of discontinued operation acquired exclusively with an intent to sell.

The telecom company was not acquired as an investment but during a pre-bankruptcy procedure through a debt-to-equity swap, and company's results are not stated in profit or loss report since equity of H1 Telekom plc. is negative.

1. SIGNIFICANT ACOUNTING POLICIES (continued)

f) Interest Income and Expense

Interest income and expense are recognized in the PNL as they accrue for all interest-bearing financial instruments, including those measured at amortized cost, at fair value in PNL and available for sale, using the effective interest rate method. Such income and expense is presented as interest and similar income or interest expense and similar charges in the PNL. Interest income and expense also includes fees and commissions income and expense in respect of loans provided to customers or borrowings from other banks, premium or discount amortization, and other differences between the initial carrying amount of an interest-bearing financial instrument and its value at maturity, recognized on a basis of effective interest rate. Interest income and expense on all trading assets and liabilities are presented as interest income or expense.

g) Fees and Commissions Income and Expense

Fees and commissions income and expense arise on financial services provided by the Group and received by the Group, and mainly comprise 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. Fees and commissions income and expense are recognized in the PNL 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 recognized as an adjustment to the effective interest rate on the loan. Commitment fees in relation to facilities where draw down is not probable are recognized over the term of the commitment. Loan syndication fees are recognized 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 recognized based on the applicable service contracts. Asset management fees related to investment fund management are recognized on an accrual 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.

h) Dividend Income

Dividend income on equity investments is recognized in the PNL report when the right to receive dividends is established.

1. SIGNIFICANT ACOUNTING POLICIES (continued)

i) Gains Less Losses from Financial Instruments at Fair Value in PNL and Financial Instruments Available for Sale

Gains less losses from financial instruments at fair value in PNL include unrealized and realized gains and losses arising from derivative financial instruments, trading debt securities and other financial instruments designated at fair value in PNL.

Gains less losses arising from financial instruments available for sale comprise realized gains from financial instruments available for sale.

Financial assets available for sale are assessed for indicators of impairment at the end of each reporting period. Financial assets are considered to be impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been affected.

For AFS equity investments, a significant or prolonged decline in the fair value of the security below its cost is considered to be objective evidence of impairment.

For all other financial assets, objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty, or
- breach of contract, such as a default or delinquency in interest or principal payments, or
- it becoming probable that the borrower will enter bankruptcy or financial reorganization, or
- disappearance of an active market for that financial asset because of financial difficulties.

In respect of AFS equity securities, impairment losses previously recognized in profit or loss are not reversed in PNL. Any increase in fair value subsequent to an impairment loss is recognized in other comprehensive income and accumulated under the heading of investments revaluation reserve. In respect of AFS debt securities, impairment losses are subsequently reversed in PNL if an increase in the fair value of the investment can be objectively related to an event occurring after the recognition of the impairment loss.

j) 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 dealings in foreign currencies.

1. SIGNIFICANT ACOUNTING POLICIES (continued)

k) Foreign Currencies

Transactions in foreign currencies are translated into HRK at the rate of exchange applicable at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated into HRK at the foreign exchange rate applicable at that date. Foreign exchange differences arising on translation are recognized in the PNL report. Non-monetary assets and liabilities denominated in foreign currency that are stated at fair value are translated in HRK at the foreign exchange rates applicable at the dates when the fair values were determined. Non-monetary assets and items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction and are not retranslated.

The fair value of AFS monetary financial assets denominated in a foreign currency is determined in that foreign currency and translated at the spot rate prevailing at the end of the reporting period. The foreign exchange gains and losses that are recognized in profit or loss are determined based on the amortized cost of the monetary asset. Other foreign exchange gains and losses are recognized in other comprehensive income.

l) Financial Instruments

i) Classification

The Group classifies its financial instruments in the following categories: at fair value in PNL, loans and receivables, available for sale and held to maturity. The classification depends on the purpose for which the financial instruments were acquired. The Management Board determines the classification of financial instruments upon initial recognition.

Financial Assets and Liabilities at Fair Value in PNL

This category comprises two subcategories: financial instruments held for trading (including derivatives), and those designated by management as at fair value in PNL at inception. The Group designates financial assets and liabilities at fair value in PNL when:

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

Financial assets at fair value in PNL include equity and debt securities, units/ shares in investment funds and derivative financial instruments.

Loans and Receivables

Loans and receivables comprise 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 mandatory reserve with the CNB.

1. SIGNIFICANT ACOUNTING POLICIES (continued)

l) Financial Instruments (continued)

i) Classification (continued)

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. This category includes debt securities.

Financial Assets Available for Sale

This category comprises non-derivative financial assets which are defined as available for sale or are not included in loans and receivables or held to maturity investments, or classified as financial assets at fair value in PNL. Financial assets 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 debt and equity securities.

Other Financial Liabilities

Other financial liabilities include all financial liabilities not designated as at fair value in PNL.

ii) Recognition and Derecognition

Purchases and sales of financial assets and financial liabilities at fair value in PNL, and financial assets held to maturity and available for sale, are recognized on the settlement date. Loans and receivables and financial liabilities at amortized cost are recognized when advanced to borrowers or received from lenders.

The Group derecognizes 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 instrument.

This occurs when the Group transfers substantially all the risks and rewards of ownership to another business entity or when the rights are realized, surrendered or have expired. The Group derecognizes 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 recognizing that liability and will instantaneously recognize a new financial liability, with new terms and conditions.

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

iii) Initial and Subsequent Measurement

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

1. SIGNIFICANT ACOUNTING POLICIES (continued)

l) Financial Instruments (continued)

iii) Initial and Subsequent Measurement (continued)

After initial recognition, the Group measures financial instruments at fair value in PNL and financial assets available for sale at their fair value, without any deduction for costs of sale. Instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are initially recognized at acquirement cost, and afterwards measured applying internal models of fair value estimation.

Loans and receivables and held to maturity investments and financial liabilities not designated at fair value in PNL are measured at amortized cost.

iv) Gains and Losses

Gains and losses on changes in the fair value of financial assets at fair value in PNL are recognized in the PNL report.

Gains or losses arising from a change in the fair value of available for sale monetary assets are recognized directly within equity and are disclosed in the report of changes in equity. Impairment losses, foreign exchange differences, interest income and amortization of premium or discount on available for sale monetary assets are recognized in the PNL report. Foreign exchange differences on equity instruments are part of the fair value of these instruments and are recognized in equity.

Dividend income is recognized in the PNL report. Upon sale or other derecognition of available for sale assets, any cumulative gains or losses on the instrument are transferred to the PNL report.

Gains or losses arising from financial instruments carried at amortized cost may also be recognized in the PNL report when a financial instrument is derecognized or when its value is impaired.

v) Determination of Fair Value of Financial Instruments

The fair value of quoted financial assets in an active market is based on their closing price. 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. Such models include the use of prices achieved in recent transactions, by 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-traded derivatives is estimated at the amount that the Group would receive or pay to terminate the contract at the reporting date, taking into account current market conditions, its own credit risk and the current creditworthiness of the counterparties.

1. SIGNIFICANT ACOUNTING POLICIES (continued)

l) Financial Instruments (continued)

vi) Impairment of Financial Assets

Impairment of Assets Identified as Impaired

Financial assets are reviewed at financial reports date to determine whether there is objective evidence of impairment. If any such indication exists, the recoverable amount of an item is estimated.

The Group estimates and performs impairment of all financial assets, except financial assets at fair value in PNL.

If any objective evidence of impairment exists for available for sale financial assets, the cumulative loss measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognized in profit or loss, is removed from equity and recognized in the PNL report. Impairment losses recognized in the PNL report on equity instruments are not reversed in the PNL report.

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 recognized in profit or loss, the impairment loss is reversed in the PNL report.

The recoverable amount of financial instruments measured at amortized cost is calculated as the present value of the expected future cash flows, discounted at the instrument's original interest rate. Short-term balances are not discounted. Allowances for uncollectibility are made against the carrying amount of loans and advances that are identified as being impaired based on regular reviews of outstanding balances to reduce these loans and advances to their recoverable amounts (or lower amount if required by applicable CNB regulations). The expected cash flows for portfolio of similar assets are estimated based on previous experience. Also taken into considering are: credit rating of the underlying customers, and delays in payments of interests or penalties. Increases of impairment allowances are recognized in the PNL report. When a loan is identified as uncollectable, all the necessary legal procedures have been completed, and the final loss has been determined, the loan is written off directly. If in a subsequent period the amount of impairment loss decreases, and the decrease can be linked objectively to an event occurring after the write-down, the write-down or impairment loss is reversed through the PNL report.

Impairment of Assets Not Individually Identified as Impaired

In addition to recognized impairment losses on assets, the Group recognizes in its PNL report latent losses on its on-balance sheet and off-balance sheet items exposed to credit risk at a level not lower than 0.80% of the total placements and off-balance sheet exposures in accordance with the CNB regulations.

At the reporting date, debt securities carried at fair value at the reporting date, initially recognized as financial assets at fair value in PNL, as well as financial assets available for sale, are excluded from the calculation basis of these impairments.

1. SIGNIFICANT ACOUNTING POLICIES (continued)

l) Financial Instruments (continued)

vii) Reclassifications

According to IFRSs, the Group has the possibility to reclassify certain financial instruments out of the category at fair value in PNL into available for sale or held to maturity instruments.

m) Specific Financial Instruments

Cash and Cash Equivalents

Cash and cash equivalents comprise cash balances on hand, cash deposited with CNB, placements with other banks with original maturities of three months or less, and items in course of collection.

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. In accordance with its investment policies, the Group does not hold or issue derivative financial instruments for the purpose of speculative trading. Hedge accounting has not been applied and consequently, all derivative agreements are classified as financial instruments at fair value in PNL.

Derivative financial instruments include foreign currency agreements, forward agreements, futures and other financial derivatives and are initially recognized 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 the discounted cash flow. 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 as an embedded derivative. Except as required to the contrary by the CNB, when the economic characteristics and risks of embedded derivatives are not closely related to those of the host contract and when the hybrid contract is not itself carried at fair value in PNL, the embedded derivative is treated as a separate derivative and classified at fair value in PNL with all unrealized gains and losses recognized in the PNL report, unless there is no reliable measure of their fair value.

Changes in the fair value of derivatives are included in gains less losses arising from dealing securities.

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 at fair value in PNL or as available for sale assets, and are carried at fair value. Treasury bills and debt securities that the Group has the intent and ability to hold to maturity are classified as held to maturity assets.

1. SIGNIFICANT ACOUNTING POLICIES (continued)

m) Specific Financial Instruments (continued)

Equity Securities and Investments in Open-End Investment Funds

Equity securities and investments in open-ended investment funds are classified as at fair value in PNL or as available for sale assets.

Placements with Banks

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

Loans and Receivables from Customers

Loans and receivables from customers are presented net of impairment losses. Purchased loans that the Group has the intent and ability to hold to maturity are classified as held to maturity assets.

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

Investments in Subsidiaries

In the parent company's separate financial reports, investments in subsidiaries are recorded at cost, except for H1 Telekom plc. which is, as assets held for sale, recorded at the lower of carrying amount and fair value.

Borrowings

Interest-bearing borrowings are recognized initially at fair value, less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortized cost with any difference between proceeds (net of transaction costs) and redemption value being recognized in the PNL report over the period of the borrowings as interest. The amount is subsequently reduced by not deferred portion of the fee paid at the point of loan approval.

Repurchase Agreements and Linked Transactions

The Group enters into purchases/ (sales) of investments under agreements to resell (repurchase) essentially identical investments, or in a series of linked sales and buy-back transactions at a certain future date at a fixed price. The amounts paid are recognized in loans and advances to either banks or customers. The receivables are shown as collateralized by the underlying security. Investments sold under repurchase agreements continue to be recognized in the report of financial position and are measured in accordance with the accounting policy for the relevant financial asset at amortized 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 amount is recognized on an accrual basis over the period of the transaction and is included in interest income or expense.

1. SIGNIFICANT ACOUNTING POLICIES (continued)

n) Corporate Tax

Corporate tax expense represents the sum of the tax currently payable and deferred tax.

Current tax payable is based on taxable profit for the year. Taxable profit differs from 'profit before tax' as reported in the PNL report and report of other comprehensive income because of items of income or expense that are taxable or deductible in other years and items that are never taxable or deductible. The Group's current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax is recognized on temporary differences between the carrying amounts of assets and liabilities in financial reports and corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognized for all taxable temporary differences. Deferred tax assets are generally recognized for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilized. Such deferred tax assets and liabilities are not recognized if the temporary difference arises from the initial recognition (other than in a business combination) of assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognized for taxable temporary differences associated with investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognized to the extent that it is probable that there will be sufficient taxable profits against which to utilize the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realized, based on tax rates and tax laws that have been enacted or substantively enacted by the end of the reporting period.

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

The measurement of deferred tax liabilities and assets reflects the amount that the Group expects, at the end of the financial reports date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are not discounted and are classified in the report of financial position as non-current assets and/ or non-current liabilities. Deferred tax assets are recognized only to the extent that it is probable that the related tax benefit will be realized. At each reporting date, the Group reviews the unrecognized potential tax assets and the carrying amount of the recognized tax assets.

o) Property and Equipment

Property and equipment are tangible assets that are held for use in the supply of services or other administrative purposes.

Recognition and Measurement

An item of property whose fair value can be measured reliably is subsequently carried at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Revaluation is made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the reporting date. The fair value of land and buildings is determined by the independent professional surveyor.

Any revaluation increase arising on the revaluation of such land and buildings is recognized in other comprehensive income and accumulated in equity, except to the extent that it reverses a revaluation decrease for the same asset previously recognized in profit or loss, in which case the increase is credited to profit or loss to the extent of the decrease previously expensed. A decrease in the carrying amount arising on the revaluation of such land and buildings is recognized in profit or loss to the extent that it exceeds the balance, if any, held in the properties revaluation reserve relating to a previous revaluation of that asset. Depreciation is recognized in the PNL report on a straight-line basis over the estimated useful lives of each part of an item of property and equipment. Land is not depreciated.

Equipment is measured at cost, less accumulated depreciation and accumulated impairment losses.

The estimated useful lives are as follows:

	2016	**2015**
Buildings	40 years	40 years
Computers	3 years	3 years
Furniture and Equipment	3-4 years	3-4 years
Motor Vehicles	5 years	5 years
Other Assets	10 years	10 years

Depreciation methods and useful lives are reassessed at reporting date. Gains and losses on disposal are determined by comparing the proceeds with the carrying amount, and are included in the PNL report.

p) Investment Property

Investment properties are properties which are held by the Group either to earn rentals or for capital appreciation, or both. Investment property is carried at cost less accumulated depreciation and any impairment losses. Depreciation is provided on all investment property, except for investment property not yet brought into use, on a straight-line basis at prescribed rates designed to write off the cost over the estimated useful life of the asset as follows:

	2016	**2015**
Investment Property	40 years	40 years

q) Intangible Assets

Intangible assets are carried at cost less accumulated amortization and impairment. Development costs are capitalized if all the requirements specified in IAS 38 "Intangible Assets" are met.

The Group intends to capitalize internal employee project costs in the future under a condition of meeting requirements by the IFRS 38. During 2016 it started the preparation activities for the mentioned purpose. Durability of the mentioned intangible assets will correspond to the estimated useful life and its future economic benefits.

Amortization is provided on a straight-line basis over the estimated useful life of an intangible asset. Maintenance costs are recognized as an expense when they are incurred. Depreciation methods and useful lives are reassessed at reporting date. Gains and losses on disposal are determined by comparing the proceeds with the carrying amount, and are included in the PNL report.

Amortization method and estimated useful life are reassessed on the date of preparing financial reports. Gains and losses from disposal are determined by comparing realized sale price and book value of assets and is included in the profit or loss report.

Amortization of intangible assets is provided on a straight-line basis over the estimated useful life of an asset as follows:

	2016	**2015**
Leasehold Improvements	4 years	4 years
Software	3-10 years	3-10 years
Licenses	3-10 years	3-10 ears

r) Impairment of Non-Financial Assets

The recoverable amount of property and equipment, investment property and intangible assets is the higher of the asset's fair value less costs to sell and value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows ("cash-generating units"). In assessing value in use, the estimated future cash flows are discounted to their 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 or cash-generating unit.

Non-financial assets that have suffered impairment are reviewed for possible reversal of the impairment at each reporting date. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount and to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no impairment loss had been recognized.

s) Non-Current Assets Available for Sale

Tangible assets gained in exchange for uncollected receivables the Group records as assets available for sale in accordance with the International Financial Reporting Standard 5 (IFRS 5). Only exceptionally, if the assets can be used for the Group's business operations decision on using the assets and accounting treatment will be in accordance with the International Financial Reporting Standard 16. Properties which do not fulfill the IFRS 5 recognition criteria will be reclassified as Property Investment in accordance with the International Account Standard 40.

The Group initially recognizes (classifies) non-current assets as assets available for sale if its value will be gained by sale, rather than used for the purpose of conducting business activities through depreciation. Such assets are classified at the lower of carrying amount or fair market value less costs to sell.

Subsequent measurement of assets available for sale is carried at the lower of carrying value and the current fair market value less sale costs.

Should an event which may extend the completion of the sale occur the assets still need to be classified as available for sale if the circumstances were beyond the Group's control and there is evidence the Group will continue to sell the assets as planned.

The Group does not amortize non-current tangible assets classified as available for sale.

Impairment losses arising on the subsequent measurement of assets is recorded in the Group's PNL report.

Subsequent gains from increase in the fair value of previously impaired assets will be recognized in the PNL report at the time of sale.

If it is determined that the non-current assets classified as available for sale do not meet the criteria for initial recognition of the Group does not recognize those assets as assets available for sale.

The Group does not recognize assets available for sale in the event that such property is sold. Gains or losses on sale of assets available for sale are recognized in the PNL report.

t) Provisions for Liabilities and Expenses

The Group recognizes a provision when it has a present obligation as a result of a past event, and when it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and if a reliable estimate can be made of the obligation. Provisions are also made for off-balance sheet credit risk exposures on a portfolio basis.

Provision for liabilities and charges represents the best estimate of the expenditures needed to settle the present obligation at the reporting date. 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 recognized at inception. If the outflow of economic benefits to settle the obligations is no longer probable, the provision is reversed.

u) Operating Lease

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 recognized in the PNL report on a straight-line basis over the term of the lease.

The Group leases office space under operating leases. Payments under operating leases are recognized in the PNL report over the term of the underlying lease. Lease incentives received are recognized in the PNL report as an integral part of the total lease expense. The Group does not have operating lease contracts with the termination period longer than one year.

v) Employee Benefits

Defined Pension Contributions

The Group pays contributions to pension-insurance funds on a mandatory, contractual basis. The Group has no further payment obligations once the contributions have been paid. The contributions are recognized as employee benefit expense when they are due.

Provisions for Severance Payments and Jubilee Awards

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

Equity Payment Scheme Plan

The Group has set a equity payment scheme policy but does not have an equity payment scheme plan as conditions for payments in 2016 or later have not been met yet.

w) Share Capital and Reserves

Share Capital and Reserves

Share capital is denominated in the Croatian kuna and stated at nominal value. The amount of fees paid on repurchase of share capital, including directly attributable costs, is recognized as a deduction from equity and classified as treasury shares.

Dividends

Dividends are recognized as a liability in the period in which they are declared.

Retained Earnings/ Accumulated Losses

All income for the year, retained after appropriations, is transferred to reserves, in accordance with the decision of the General Assembly.

Loss for the period is charged on the accumulated retained earnings. Any remaining loss is allocated in accordance with the regulations applicable to trading companies in the Republic of Croatia.

During the reduction of the share capital of the Group's parent company in 2015 remaining amount after loss coverage from the previous period has been allocated to retained earnings based on the Decision of the General Assembly and in accordance with the regulations applicable to trading companies in the Republic of Croatia.

Earnings per Share

The Group's parent company presents earnings or loss per share data for its ordinary shares. Earnings/ loss per share is calculated by dividing the profit or loss attributable to ordinary shareholders of the parent company by the weighted average number of ordinary shares outstanding during the period.

x) Contingencies and Commitments

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 report of financial position if and when they become payable.

y) Funds Managed for and on Behalf of Third Parties

The Group manages funds for and on behalf of corporate and retail customers. These amounts do not represent the Group's assets and are excluded from the report of financial position. For the services rendered, the Group charges a fee which is recognized in the PNL on an accruals basis. The Group also manages five open-end funds with a public offering: HPB Equity Fund, HPB Global Fund, HPB Cash Fund, HPB Bond Fund, and HPB Eurocash Fund.

Investment funds assets that is managed by the Group is not part of consolidated reports of the Group.

The investment of the parent company in the investment funds of the parent company are stated at fair value in PNL.

z) Segment Reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment) which achieves economic benefits or costs, including the transactions with other parts of the Group. During 2015 the Group did not use internal transfer prices in determining the success of the segments.

The Group has identified four major segments: Corporate Banking; Retail Banking; Financial Markets, (including treasury and investment banking, together with custody services (business segment)) and Direct Banking. The business segments and their financial performance are presented in Note 4 to the financial reports.

The Group's operations, its total assets as well as the majority of its clients are based in Croatia.

2. RISK MANAGEMENT

This note details the Group's risk exposures as well as the methods applied by the management to identify, measure and manage those risks for the purpose of preserving capital. The most important types of financial risk to which the Group is exposed are credit risk, liquidity risk, interest rate risk in the Bank's non-trading book, market risk and operational risk. Market risk includes currency risk, interest rate risk and price risk.

An integrated system of risk management is established at the Group level by introducing a set of policies, procedures and manuals, determining the limits of risk levels acceptable to the Group and monitoring their implementation. The limits are set with respect to the amount of regulatory capital and are applied to all types of risk. Additionally, the Bank sets limits for annual potential losses measured by Value-at-Risk techniques for its market risk exposure. Internal methodologies and models for managing other types of risks are also being developed.

The responsibility for determining the framework of the Group's risk management lies with the Bank's Management Board which has delegated the risk management tasks to the Assets and Liabilities Management Committee, Credit Committee and Operational Risk Management Committee.

2.1 Credit Risk

The Group is subject to credit risk through its lending and investing activities and in cases where it acts as an intermediary on behalf of customers or other third parties.

The risk that counterparties to financial instruments might default on their obligations is monitored on an ongoing basis. To manage the level of credit risk, the Group evaluates debtors' creditworthiness, and in order to minimize credit risk, obtains appropriate collateral.

At reporting date, the Group's credit risk exposure to financial instruments classified as at fair value in PNL is presented by the positive fair value of these instruments, as recorded in the report of financial position. Notional amounts disclosed in the notes to the financial reports do not represent the amounts to be exchanged by the parties in derivative transactions and do not measure the Group's exposure to credit or market risks. The amounts to be exchanged are based on the terms of the derivatives.

The Group is exposed to credit risk primarily through loans and receivables from customers. The amount of credit exposure in this regard, as well as held to maturity debt securities recognized at amortized cost, is represented by the carrying amounts of the assets on the balance sheet. In addition, the Group is exposed to the credit risk through off-balance sheet items, i.e. through commitments arising from unused facilities and guarantees issued, as disclosed in Note 39.

Credit risk management comprises assessment of placements' credit risk, subsequent monitoring, supervision, and assessment of recoverability of placements and off-balance sheet commitments, as well as formation of required impairments and provisions for identified losses on placements and off-balance sheet commitments, and reporting to the Bank's Management Board.

2. RISK MANAGEMENT (continued)

2.1. Credit Risk (continued)

2.1.1 Credit Risk Assessment

Assessment of the individual credit risk exposure comprises the following:

- debtors' creditworthiness,
- debtors' timeliness in meeting their obligations,
- collateral quality.

Monitoring of credit risk includes continuous assessment whether elements exist which would indicate a deterioration of the client's financial position, the client's exposure to currency risk or an increase in risk due to the decrease of collateral value.

2.1.2. Classification of Placements in Risk Categories

The Group classifies placements into risk categories depending on the estimated recovery rate of placements, and in accordance with the Croatian National Bank's Decision on Classification of Placements and Off-balance Sheet Liabilities of Credit Institutions. All placements that the Group estimates are fully recoverable are classified in risk category A. Upon initial approval, the Group classifies all placements into risk category A. Placements that the Group estimates are partly recoverable are classified into risk category B, depending on the loss percentage: in subcategory B1 (loss is estimated at below 30% of nominal carrying value of the placement), in subcategory B2 (loss is estimated at between 30% and 70% of nominal carrying value of the placement), and in subcategory B3 (loss is estimated at above 70%, but below 100% of nominal carrying value of the placement). Placements estimated to be fully irrecoverable are classified into risk category C.

2.1.3. Placements Impairment Policy

When estimating the recoverable amount of placements, the Group separates placements between small and large portfolios.

Small portfolio represents placements and off-balance sheet commitments whose gross value (before any impairment loss) does not exceed HRK700K towards a single debtor or a single group of related parties at the date of estimation.

Generally, the Group estimates the recoverability of placements to retail customers according to criteria established for the small portfolio, whereas the recoverability of placements to corporate clients is estimated according to criteria which do not apply to the small portfolio.

2. RISK MANAGEMENT (continued)

2.1. Credit Risk (continued)

2.1.3. Impairment Policy on Placements (continued)

Individual Assessment

The recoverable amount of placements that are not classified within the small loan portfolio of the Group is estimated on an individual basis according to the following criteria:

- debtors' creditworthiness,
- debtors' timeliness in meeting their obligations, and
- collateral quality.

With respect to this, credit rating of the debtor and/ or other parties in the loan business (guarantors, co-debtors etc) is taken into account, as well as days-past-due in debt settlement and type and appraised value of the available collateral. By taking this into consideration, as well as other available information, the Group estimates loan recoverability by evaluating future cash flows arising from the placement, which are discounted and compared with placement's book value. Required impairments are determined in this way. The Group complies with regulations from *Decision on the Classification of Placements and Off-Balance Sheet Liabilities of Credit Institutions* with respect to procedures for restructured placements, placements whose repayment is based on collateral, placements that are not secured by adequate collateral, as well as other regulations regarding eligibility of collateral and appropriate discount factors used for impairment calculus.

Portfolio Based Assessment

The Group estimates the recoverable amount of exposures that are classified on a portfolio basis by having regard principally to the debtors' timeliness in meeting their obligations. In arriving at the recoverable amount, the present value of future cash flows from the placements is estimated by reducing the principal by reference to the loan type and the number of days in default.

The following tables present the classification of exposures into risk categories for the Group and the allocation of the corresponding impairment losses as a percentage of gross principal.

2. RISK MANAGEMENT (continued)

2.1. Credit Risk (continued)

2.1.3 Impairment Policy on Placements (continued)

%	**Loans and Receivables from Customers**	Impairment Allowance	**Loans to and Receivables from Banks**	Impairment Allowance	**Financial Assets Held to Maturity**	Impairment Allowance	**Balances with the Croatian National Bank**	Impairment Allowance	**Fees Receivable**	Impairment Allowance
2016										
A	83.98	0.97	99.73	-	99.09	1.51	100.00	-	62.00	-
A - 90 days	-	0.28	-	-	-	-	-	-	-	-
B and C	16.02	61.80	0.27	100.00	0.91	34.76	-	-	37.99	100.00
2015										
A	73.75	1.00	99.81	-	95.38	1.43	100.00	-	55.39	-
A - 90 days	0.12	1.00	-	-	-	-	-	-	-	-
B and C	26.13	64.47	0.19	100.00	4.62	83.92	-	-	44.61	100.00

2. RISK MANAGEMENT (continued)
2.1. Credit Risk (continued)

2.1.3 Impairment Policy on Placements (continued)

Maximum Exposure to Credit Risk before Consideration of Collateral

The table below shows the maximum exposure of the Group to credit risk as at December 31 2016 and December 31 2015, not considering the collateral, if any. The exposures presented below are net of impairment losses and provisions.

Maximum Exposure	Note	**2016 HRK'000**	**2015 HRK'000**
Giro Account with the CNB and Other Banks	5	1,133,248	1,217,930
Mandatory Reserve with the CNB	6	1,300,796	1,279,570
Loans to and Receivables from Banks	7	182,087	261,913
Held to Maturity Investments	10	444,825	571,764
Loans and Receivables from Customers	11	11,552,549	10,298,014
Fees Receivable	18	13,340	15,538
Off-Balance Sheet Exposure	40	**2,364,932**	**1,896,190**
Undisbursed Lending Commitments		1,636,818	1,334,010
Guarantees		710,846	522,627
Other Contingent Liabilities		17,268	39,553
Total Credit Exposure		**16,991,777**	**15,540,919**

2. RISK MANAGEMENT (continued)

2.1. Credit Risk (continued)

2.1.4. Assets Exposed to Credit Risk

2016	Loans to and Receivables from Customers	Loans to and Receivables from Banks	Financial Assets Held to Maturity	Balances with the Croatian National Bank	Fees Receivable
	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000
Loans Neither Overdue nor Impaired	10,865,509	182,087	448,896	1,841,823	13,339
Overdue Loans Not Impaired	358	-	-	-	1
Impaired Loans	2,072,827	500	4,139	-	8,173
Total Gross	**12,938,694**	**182,587**	**453,035**	**1,841,823**	**21,513**
Individually Identified Losses	(1,280,962)	(500)	(1,439)	-	(8,173)
Portfolio Based Losses	(105,183)	-	(6,772)	-	-
Total Identified Losses	**(1,386,145)**	**(500)**	**(8,211)**	-	**(8,173)**
Total	**11,552,549**	**182,087**	**444,824**	**1,841,823**	**13,340**

2015	Loans and Receivables from Customers	Loans to and Receivables from Banks	Financial Assets Held to Maturity	Balances with the Croatian National Bank	Fees Receivable
	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000
Loans Neither Overdue nor Impaired	9,215,915	261,913	575,541	1,767,612	15,538
Overdue Loans Not Impaired	14,843	-	-	-	-
Impaired Loans	3,264,932	500	27,859	-	12,514
Total Gross	**12,495,690**	**262,413**	**603,400**	**1,767,612**	**28,052**
Individually Identified Losses	(2,104,998)	(500)	(23,380)	-	(12,514)
Portfolio Based Losses	(92,678)	-	(8,256)	-	-
Total Identified Losses	**(2,197,676)**	**(500)**	**(31,636)**	**-**	**(12,514)**
Total	**10,298,014**	**261,913**	**571,764**	**1,767,612**	**15,538**

2. RISK MANAGEMENT (continued)

2.1. Credit Risk (continued)

2.1.4. Assets Exposed to Credit Risk (continued)

In accordance with applicable acts, the Group utilizes the following common types of collateral: bank guarantees; HAMAG-BICRO (Croatian Agency for SMEs, Innovation and Investments) and other corporate guarantees; bills of exchange accepted by a bank; pledged property and equipment; insurance policies; pledged shares, bonds, commercial papers, and units in open-ended investment funds; assignment of receivables (cessions) from corporate clients and the Government; pledged concessions; pledged industrial and intellectual property; and other common financial execution instruments, such as bills of exchange and promissory notes.

Collateral value is reviewed along the lines of internal policies and procedures, and in accordance with good business practice and current market trends.

Collateral value in the table below relates to recorded collateral value based on valuation made by certified appraisers without adjustments for discount factors but excluding burdens listed before the Bank and limiting to the amount of exposure which it collateralizes.

Asset Type	Collateral Type	2016 HRK'000	2015 HRK'000
Financial Assets Held to Maturity		**25,821**	**25,703**
	Deposits	25,821	25,703
Loans to and Receivables from Customers		**4,988,823**	**4,800,698**
	Deposits	188,045	156,415
	Debt Securities	81,580	71,165
	Guarantees and Warranties of the Republic of Croatia	1,216,947	1,136,185
	Real Estate – Non-Business Purposes	1,729,269	1,308,913
	Real Estate – Business Purposes	1,381,209	1,537,552
	Movable Property (Equipment, Supplies, Vehicles, Ships etc)	75,313	207,888
	Equity Investments (Single-Stocks and Funds)	77,025	65,190
	Land	239,436	317,390
Total		**5,014,644**	**4,826,401**

2. RISK MANAGEMENT (continued)

2.1. Credit Risk (continued)

2.1.4. Assets Exposed to Credit Risk (continued)

Below is presented an overview of due and undue receivables aging structure based on days-past-due, with regard to the principal of the loans:

HRK'000	Total	Undue Exposure to Credit Risk	Days Past Due 1-30	Days Past Due 31-60	Days Past Due 61-90	Days Past Due 91-180	Days Past Due 180+
31 Dec 2016							
Government	4,023,904	4,021,914	1,986	-	-	-	4
Other Corporate Clients	3,913,148	2,662,028	76,209	38,183	5,064	7,887	1,123,777
Retail	4,951,372	4,676,596	24,308	6,961	3,466	35,183	204,858
Total	**12,888,424**	**11,360,538**	**102,503**	**45,144**	**8,530**	**43,070**	**1,328,640**
31 Dec 2015							
Government	3,677,815	3,671,961	1,994	-	1,946	1,912	2
Other Corporate Clients	4,004,502	2,132,519	34,753	4,970	12,501	163,981	1,655,778
Retail	4,763,360	4,152,921	8,599	4,023	17,322	9,554	570,942
Total	**12,445,678**	**9,957,401**	**45,345**	**8,993**	**31,769**	**175,447**	**2,226,722**

2. RISK MANAGEMENT (continued)

2.1. Credit Risk (continued)

2.1.4. Assets Exposed to Credit Risk (continued)

(a) Assets exposed to credit risk but not impaired (risk category A)

2016 HRK'000	Government Units	Financial Institutions (Excl. Banks)	Companies	Housing Loans	Mortgage Loans	Credit Cards	Other Loans	**Total Loans and Receivables from Customers**	**Loans to and Receivables from Banks**	**Financial Assets Held to Maturity**	**Balances with the Croatian National Bank**	**Fees Receivable**
Gross Amount	4,031,561	81,631	2,156,073	1,561,967	415	146,655	2,887,207	**10,865,509**	182,087	448,896	1,841,823	13,339
Total Portfolio Based Losses	(38,960)	(791)	(20,976)	(15,053)	(5)	(1,421)	(27,977)	**(105,182)**	-	(6,772)	-	-
Net Amount	**3,992,601**	**80,840**	**2,135,098**	**1,546,914**	**410**	**145,234**	**2,859,230**	**10,760,327**	**182,087**	**442,124**	**1,841,823**	**13,339**
Collateral Value	654,804	81,580	1,362,133	1,457,315	415	-	242,190	**3,798,437**	-	25,821	-	-
Collateral Coverage (%)	16.40	100.92	63.80	94.21	101.11	-	8.47	**35.30**	-	5.84	-	-

2015 HRK'000	Government Units	Financial Institutions (Excl. Banks)	Companies	Housing Loans	Mortgage Loans	Credit Cards	Other Loans	**Total Loans and Receivables from Customers**	**Loans to and Receivables from Banks**	**Financial Assets Held to Maturity**	**Balances with the Croatian National Bank**	**Fees Receivable**
Gross Amount	3,475,938	71,182	1,626,689	1,056,083	856	147,732	2,837,435	**9,215,915**	261,913	575,541	1,767,612	15,538
Total Portfolio Based Losses	(34,925)	(715)	(16,431)	(10,455)	(9)	(1,484)	(28,510)	**(92,529)**	-	(8,256)	-	-
Net Amount	**3,441,013**	**70,467**	**1,610,259**	**1,045,628**	**847**	**146,248**	**2,808,925**	**9,123,386**	**261,913**	**567,285**	**1,767,612**	**15,538**
Collateral Value	858,793	71,165	856,186	974,943	856	-	223,951	**2,985,894**	-	25,703	-	-
Collateral Coverage (%)	24.96	100.99	53.17	93.24	101.06	-	7.97	**32.73**	-	4.53	-	-

2. RISK MANAGEMENT (continued)

2.1. Credit Risk (continued)

2.1.4. Assets Exposed to Credit Risk (continued)

(b) Assets exposed to credit risk in the risk category A that are past due beyond 90 days but not impaired

The gross balance and the coverage of those assets with collateral at fair value, presented as a percentage of net placements is as follows:

	Loans and Receivables from Customers					
2016 HRK'000	Government Units	Companies	Housing Loans	Other Loans	**Total**	**Fee Receivable**
Gross Amount	134	223	1	358	1	134
Total Portfolio Based Losses	(1)	-	-	(1)	-	(1)
Net Amount	**133**	**223**	**1**	**357**	**1**	**133**
Collateral Value	-	-	110	110	-	-
Collateral Coverage (%)	-	-	-	30.81	-	-

	Loans and Receivables from Customers					
2015 HRK'000	Government Units	Companies	Housing Loans	Other Loans	**Total**	**Fee Receivable**
Gross Amount	-	14,843	-	-	14,843	-
Total Portfolio Based Losses	-	(149)	-	-	(149)	-
Net Amount	**-**	**14,694**	**-**	**-**	**14,694**	**-**
Collateral Value	-	12,456	-	-	12,456	-
Collateral Coverage (%)	-	84.77	-	-	84.77	-

2. RISK MANAGEMENT (continued)

2.1. Credit Risk (continued)

2.1.4. Assets Exposed to Credit Risk (continued)

(c) Credit risk on impaired assets in risk categories B and C

Tables below show the amount of loans with impairments, both individual and portfolio based, as well as coverage of these placements by corresponding collateral at fair value in percentage and in relation to net placements as following:

2016 HRK'000	**Loans to Customers**								
	Companies	Housing Loans	Mortgage Loans	Credit Cards	Other Loans	**Total**	**Loans to and Receivables from Banks**	**Financial Assets Held to Maturity**	**Fees Receivable**
Gross Amount	1,673,400	40,448	53	7,628	351,298	**2,072,827**	500	4,139	8,173
Total Identified Losses	(1,057,221)	(19,560)	(5)	(5,928)	(198,248)	**(1,280,962)**	(500)	(1,439)	(8,173)
Net Amount	**616,179**	**20,888**	**48**	**1,700**	**153,050**	**791,865**	**-**	**2,700**	**-**
Collateral Value	1,031,668	37,291	53	**-**	121,039	**1,190,051**	**-**	**-**	**-**
Collateral Coverage (%)	167.43	178.53	110.42	**-**	79.08	150.28	**-**	**-**	**-**

2015 HRK'000	**Loans to Customers**								
	Companies	Housing Loans	Mortgage Loans	Credit Cards	Other Loans	**Total**	**Loans to and Receivables from Banks**	**Financial Assets Held to Maturity**	**Fees Receivable**
Gross Amount	2,498,704	44,597	60	12,660	708,911	**3,264,932**	500	27,859	12,514
Total Identified Losses	(1,547,154)	(19,885)	(6)	(11,039)	(526,914)	**(2,104,998)**	(500)	(23,380)	(12,514)
Net Amount	**951,550**	**24,712**	**54**	**1,621**	**181,997**	**1,159,934**	**-**	**4,479**	**-**
Collateral Value	1,578,486	39,041	60	-	184,761	**1,802,348**	**-**	**-**	**-**
Collateral Coverage (%)	165.89	157.98	111.11	-	101.52	155.38	**-**	**-**	**-**

2. RISK MANAGEMENT (continued)

2.1. Credit Risk (continued)

2.1.4. Assets Exposed to Credit Risk (continued)

(d) Prolonged and rescheduled loans to customers

Prolongation of a loan is approved to customers because of common and current financing needs of their business activities.

Loans are most often rescheduled when borrowers' business operations are disrupted, with considerable changes made to the previously agreed lending terms and conditions.

	2016 HRK'000	**2015 HRK'000**
Gross Loans to Customers		
Corporates	653,698	1,232,341
Retail	63,954	86,546
Total	**717,652**	**1,318,887**

2.1.5. Credit Risk Concentration by Industry

An analysis of the concentration of credit risk by industry is presented in the table below:

	2016 HRK'000	**2015 HRK'000**
Public Administration, Defense and Compulsory Social Security	3,352,833	2,724,818
Manufacturing	1,020,081	1,225,856
Construction	1,014,397	1,332,131
Transportation and Storage	348,132	358,387
Wholesale and Retail Trade; Motor Vehicles and Motorcycles Repair	459,407	557,988
Professional, Scientific and Technical Activities	523,031	149,661
Accommodation and Food Service Activities	311,152	232,141
Agriculture, Forestry and Fishing	239,259	239,189
Information and Communications	150,274	198,165
Electricity and Gas Supply and Air-Conditioning	72,339	98,522
Arts, Entertainment and Recreation	110,500	95,425
Administrative and Auxiliary Services	29,613	42,059
Other	306,034	427,976
Total Gross Corporate Loans	**7,937,052**	**7,682,318**
Gross Retail Loans	**4,951,372**	**4,763,360**
Collateralized	**4,988,823**	**4,800,698**
Accrued Interests	51,936	50,012
Provisions for Impairment Losses	(1,386,145)	(2,197,676)
Total	**11,554,215**	**10,298,014**

2. RISK MANAGEMENT (continued)

2.2. Liquidity Risk

Liquidity risk arises in the general funding of the Group's activities and in the management of its positions. The main categories of liquidity risk to which the Group is exposed are as follows:

- liquidity funding risk (structural liquidity risk): risk that the Group will not be able to meet efficiently its expected and unexpected present and future cash and collateral requirements without impacting its day-to-day operations or its own financial result,
- market liquidity risk, risk that the Group will not be able to offset its positions or liquidate positions at market price due to a market disturbance or the market being insufficiently deep.

The Group manages liquidity risk in accordance with the legal and regulatory requirements. In addition to those requirements, liquidity risk management is governed by the following internal regulations:

- Risk Management Policy,
- Liquidity Risk Management Manual.

The system for managing liquidity risk, in line with defined polices, includes:

- estimation and measurement of liquidity risk exposure;
- setting liquidity risk exposure limits,
- reporting and monitoring the limits used,
- the mechanism for the distribution of liquidity costs and benefits,
- control function.

Liquidity risk management is realized through:

- operational management of daily liquidity,
- operational management of short-term liquidity,
- structural liquidity management.

Operational management of daily and short-term liquidity is performed through:

- planning and projecting daily/ ten-day/ monthly cash flows
- maintaining minimum weekly and monthly liquidity coefficient in HRK, total of all convertible currencies and non-convertible currencies individually, and total minimum weekly and monthly liquidity coefficient, calculated according to CNB's Decision on Liquidity Risk Management, within the prescribed limit.

Structural liquidity management is performed through:

- maintaining positions depending on gap limits between receivables and liabilities according to remaining contractual maturity,
- maintaining positions in accordance with liquidity risk exposure limits,
- diversification of sources of funding.

2. RISK MANAGEMENT (continued)

2.2. Liquidity Risk (continued)

Risk Management Division is reporting monthly about liquidity risk and liquidity risk exposure limits during sessions of Assets and Liabilities Management Committee.

The Group submits monthly reports to the CNB in form and in deadline prescribed by Decision on Liquidity Risk Management, with end-of-the-month status. Prescribed quantitative requirements consist of following reports: about the amount of highly liquid assets (presently marketable assets), about the maturity gap of assets and liabilities (expected inflows and outflows form), about the level of minimal liquidity coefficient and funds concentration within total liabilities. Information is delivered for two periods: up to one week and up to one month, separately for HRK, convertible currencies and each non-convertible currency individually (if they represent a significant amount) and on portfolio basis for HRK and convertible currencies. The Group have maintained all limits above prescribed levels during 2016. The Group maintains mandatory reserve and minimal foreign currency receivables within limits prescribed by Decision on Reserve Requirements and Decision on Minimum Required Amount of Foreign Currency Claims.

Financial Markets Division reports monthly to Assets and Liability Management Committee about planned outflows and inflows.

Ultimate responsibility for liquidity risk management rests with the Bank's Management Board. The Bank’s Asset and Liability Committee is authorized by the Management Board to manage liquidity risk. The Committee makes decisions and conclusions regarding liquidity management in its sessions. Each sector to which these decisions and conclusions made by the committee relate, is obliged to enact them.

As a part of liquidity risk management system, authority, responsibilities and procedures in conditions of liquidity crisis are determined separately.

The Group prescribes and implements stress tests of its liquidity. The Risk Management Division conducts tests of immunity to stress by taking into account all the factors specific to the Group (internal factors) and market factors (external factors).

Stress tests are conducted on minimal liquidity coefficient for HRK and total convertible currencies, for periods up to a week and up to a month.

Long-term liquidity is managed by maintaining positions in accordance with the limits of exposure to liquidity risk.

2.2.1 Maturity Analysis

A maturity analysis of assets and liabilities, as well as equity, of the Group, based on their remaining contractual maturity, except for financial assets at fair value through profit and loss that are analyzed as current based on their classification and the Group’s trading intention, as at December 31 2016 and December 31 2015, is presented in the tables below.

2. RISK MANAGEMENT (continued)

2.2. Liquidity Risk (continued)

2.2.1. Maturity Analysis (continued)

2016
HRK'000

	0-30 Days	31-90 Days	91-360 Days	1 to 3 Years	Over 3 Years	Total
ASSETS						
Cash and Amounts Due from Banks	1,554,612	-	-	-	-	1,554,612
Mandatory Reserve with the Croatian National Bank	1,300,796	-	-	-	-	1,300,796
Loans to and Receivables from Banks	161,913	20,074	-	100	-	182,087
Financial Assets at Fair Value in PNL	1,009,597	9,844	-	-	-	1,019,441
Financial Assets Available for Sale	99,971	23,392	707,953	272,059	1,650,563	2,753,938
Financial Assets Held to Maturity	2,159	219,500	208,442	14,724	-	444,825
Loans and Receivables from Customers	1,662,215	300,885	2,453,237	2,448,674	4,689,204	11,554,215
Assets Available for Sale	81,419	-	-	7,930	-	89,349
Properties and Equipment	-	-	-	-	140,765	140,765
Investment Properties	-	-	-	-	96,518	96,518
Intangible Assets	-	-	-	-	107,360	107,360
Deferred Tax Assets, Net	-	-	448	-	38,741	39,189
Tax Prepayment	-	-	347	-	-	347
Other Assets	293,043	139	8,087	21,000	132,115	454,384
TOTAL ASSETS	**6,165,725**	**573,834**	**3,378,514**	**2,764,487**	**6,855,266**	**19,737,826**
LIABILITIES						
Financial Liabilities at Fair Value in PNL	-	3,641	-	-	-	3,641
Deposits from Banks	234,855	104,331	169,947	-	-	509,133
Customer Deposits	7,973,966	1,591,786	4,925,135	1,280,036	253,881	16,024,804
Borrowings	53,884	104,677	84,771	156,913	326,415	726,660
Corporate Tax Liability	17,209	921	36,892	4,778	987	60,787
Provisions for Liabilities and Expenses	58	-	-	-	-	58
Other Liabilities	256,022	16,844	36,342	14,964	143,267	467,439
Total Equity	-	-	-	-	1,945,304	1,945,304
TOTAL LIABILITIES AND EQUITY	**8,535,994**	**1,822,200**	**5,253,087**	**1,456,691**	**2,669,854**	**19,737,826**
MATURITY GAP	**(2,370,269)**	**(1,248,366)**	**(1,874,573)**	**1,307,796**	**4,185,412**	**-**
CUMMULATIVE MATURITY GAP	**(2,370,269)**	**(3,618,635)**	**(5,493,208)**	**(4,185,412)**	**-**	**-**
OFF-BALANCE SHEET	*611,463*	*295,844*	*963,608*	*457,668*	*132,137*	*2,364,932*
Derivatives	-	*95,788*	-	-	-	-
Off-Balance Sheet Contingent Liabilities	*611,463*	*200,056*	*963,608*	*457,668*	*132,137*	*2,364,932*

2. RISK MANAGEMENT (continued)

2.2. Liquidity Risk (continued)

2.2.1. Maturity Analysis (continued)

2015
HRK'000

	0-30 Days	31-90 Days	91-360 Days	1 to 3 Years	Over 3 Years	Total
ASSETS						
Cash and Amounts Due from Banks	1,630,115	-	-	-	-	1,630,115
Mandatory Reserve with the Croatian National Bank	1,279,570	-	-	-	-	1,279,570
Loans to and Receivables from Banks	193,492	35,036	-	33,385	-	261,913
Financial Assets at Fair Value in PNL	1,016,415	3,279	-	-	-	1,019,694
Financial Assets Available for Sale	-	27,429	1,127,074	255,346	811,461	2,221,310
Financial Assets Held to Maturity	45,461	-	360,395	151,073	14,835	571,764
Loans and Receivables from Customers	1,445,319	327,128	1,654,477	3,291,819	3,579,271	10,298,014
Assets Available for Sale	-	-	-	7,930	-	7,930
Properties and Equipment	-	-	-	-	142,236	142,236
Investment Properties	-	-	-	-	9,568	9,568
Intangible Assets	-	-	-	-	117,010	117,010
Deferred Tax Assets, Net	-	-	-	-	10,750	10,750
Tax Prepayment	-	-	371	-	-	371
Other Assets	193,410	777	11,538	7,558	230,545	443,828
TOTAL ASSETS	**5,803,782**	**393,649**	**3,153,855**	**3,747,111**	**4,915,676**	**18,014,073**
LIABILITIES						
Financial Liabilities at Fair Value in PNL	-	-	-	-	-	-
Deposits from Banks	236,661	5,678	115,300	-	-	357,639
Customer Deposits	6,983,856	1,417,744	4,491,227	1,412,130	188,637	14,493,594
Borrowings	6,351	18,945	77,905	630,707	271,475	1,005,383
Provisions for Liabilities and Expenses	14,160	6,614	12,026	2,479	1,444	36,723
Other Liabilities	171,013	19,318	17,074	8,325	126,173	341,903
Total Equity	-	-	-	-	1,778,831	1,778,831
TOTAL LIABILITIES AND EQUITY	**7,412,041**	**1,468,299**	**4,713,532**	**2,053,641**	**2,366,560**	**18,014,073**
MATURITY GAP	**(1,608,259)**	**(1,074,650)**	**(1,559,677)**	**1,693,470**	**2,549,116**	**-**
CUMMULATIVE MATURITY GAP	**(1,608,259)**	**(2,682,909)**	**(4,242,586)**	**(2,549,116)**	**-**	**-**
OFF-BALANCE SHEET	***550,711***	***118,497***	***923,542***	***235,609***	***67,831***	***1,896,190***
Derivatives	-	-	-	-	-	-
Off-Balance Sheet Contingent Liabilities	*550,711*	*118,497*	*923,542*	*235,609*	*67,831*	*1,896,190*

2. RISK MANAGEMENT (continued)

2.3 Market Risk

The exposure to market risk occurs with respect to balance sheet and off-balance sheet positions recognized at fair value:

- financial assets held for trading,
- financial assets available for sale,
- positions denominated in foreign currency (including placements and liabilities linked to foreign currencies).

All trading instruments are subject to market risk, which is the risk that future changes in market conditions may make an instrument less valuable or more onerous (i.e. impaired). Trading financial instruments are recognized at fair value, and all changes in market conditions directly affect trading income. The Group manage their use of trading instruments in response to changing market conditions. Exposure to market risk is formally managed through acquisitions or disposals of financial instruments in accordance with the risk limits set in Market Risk Management Guidelines.

Market risk management of the Group is conducted in accordance with regulatory requirements, as is defined by internal policies and procedures regarding market risks which are regularly revised by the Risk Management Division.

The Risk Management Division daily calculates market risk exposure figures, usage of exposure to market risk limits and capital requirements for exposure to market risks.

In the measurement of the market risk exposure, the Group rely on regulations set out by the Croatian National Bank and monitors:

- Capital requirement calculated by the standard method calculated in accordance with the Croatian National Bank's Decision on the capital adequacy of financial institutions,
- Value at Risk (VaR) which represents the maximum potential loss that the Group could incur as a result of changes in market risk factors (interest rates, exchange rate and share prices) for a period of retaining the same position for 10 days at statistical accuracy of 99%. VaR is calculated at the end of the day and does not include daily exposure arising from a change in position. To calculate VaR, a database containing 250 historical figures is used,
- Capital requirement calculated by an internal model (VaR x multiplying factor depending on the backward number of overdrafts in the test results - *backtesting*).

In addition the Group uses the following internally prescribed measures in measuring exposure to debt instrument position risks:

- Duration (measure of the sensitivity of debt security prices to changes in interest rates),
- PV01 which represents the decline of portfolio value in a scenario where interest rates increase by 0.01%.

The Risk Management Division reports daily to the Financial Markets Division on the usage of market risk exposure limits, daily to the Financial Management Division regarding the capital requirements for currency risk and position risks, and monthly to the Assets and Liabilities Management Committee on market risk exposure.

2. RISK MANAGEMENT (continued)

2.3 Market Risk (continued)

a) Trading Portfolio

The table below shows the movements in those measures at December 31 2016 and December 31 2015.

2016	**Position HRK'000**	**VaR**
FX Risk	44,103	(331)
Fixed-Income Position Risk	644,736	(6,885)
Equity Position Risk	39,393	(2,684)
Investment Fund Position Risk	186,541	(960)
Correlation Effect	-	3,287
Market Risk	-	**(7,572)**
2015		
FX Risk	44,801	(390)
Fixed-Income Position Risk	407,197	(1,248)
Equity Position Risk	33,947	(2,276)
Investment Fund Position Risk	469,309	(1,259)
Correlation Effect	-	1,645
Market Risk		**(3,528)**

2. RISK MANAGEMENT (continued)

2.3 Market Risk (continued)

b) Available for Sale Portfolio

The available for sale portfolio consists of fixed-income and equity securities.

The table below shows market value and VaR movements for the portfolio of fixed-income and equity securities available for sale.

Fixed-Income	Market Value HRK'000	VaR HRK'000
2016	2,734,202	(23,700)
2015	2,179,064	(8,788)

Equity	Market Value HRK'000	VaR HRK'000
2016	19,736	(525)
2015	42,246	(1,447)

2. RISK MANAGEMENT (continued)

2.4 Interest Rate Risk in the Bank's Non-Trading Book

Interest rate risk in the Bank's non-trading book is a risk which can have a negative effect on economic value of the Group's book and earnings (net interest income), because of variation of market interest rates. Exposure to interest rate risk in the Bank's non-trading book arises as a consequence of:

- mismatch between assets and liabilities distributed according to the possibility of interest rate change criterion (repricing gaps),
- various natures of interest rates (reference rates) applied by the Group in arranging its lending and borrowing activities.

Accordingly, all interest rate sensitive items in the Bank's non-trading book are exposed to interest rate risk.

The Group manages interest rate risk in the Bank's non-trading book in accordance with the legal and regulatory requirements. In line with the Croatian National Bank's Decision on the Management of Interest rate risk in the Bank's non-trading book, the Group is required to submit quarterly reports to the Croatian National Bank about the interest rate risk in the Bank's non-trading book, on unconsolidated and consolidated basis both.

Apart from those regulations, managing interest rate risk in the Bank's non-trading book is regulated by:

- Risk Management Policy, and
- Manual on Managing Interest Rate Risk in the Bank's non-trading book.

The Manual on Managing Interest Rate Risk in the Bank's non-trading nook defines the management process, assessment methods and measures of exposure to interest rate risk in the Bank's non-trading book, as well as exposure limits, manner and frequency of reporting about the Groups exposure to that risk.

The Group assesses interest rate risk in the Bank's non-trading book by observing this risk from two perspectives:

- Perspective of economic value: a potential market value decrease of the Bank's non-trading book because of interest rate movements in the market,
- Profit perspective: a potential decrease of net interest income because of movements in market interest rates.

Perspective of Economic Value of Capital

The Group uses simplified calculation of estimated change in economic value of the Bank's book by applying standard interest shock on non-trading book positions which are exposed to interest rate risk, for all significant currencies separately and other currencies jointly. Interest sensitive positions of the non-trading book are distributed in 13 time zones, whereby positions with fixed interest rate, variable interest rate and interest rate that can be changed by Management Board's decision (administrative interest rate) are distinguished, and estimates a change in market value of the Bank's non-trading book by applying basic simulation of parallel interest rates movements by 2 basis points. The Group calculates a ratio between the change in economic value of the non-trading book and regulatory capital, and maintains it on a level below 18% (legal ratio prescribed by the Croatian National Bank's Decision equals 20%). Change in economic value of capital amounts to HRK108,552K or 6.98% of regulatory capital as per 2016 year-end.

2. RISK MANAGEMENT (continued)

2.4 Interest Rate Risk in the Bank's Non-Trading Book (continued)

Profit Perspective

The profit perspective takes into account the potential decrease in net interest income as a result of a change in market interest rates. To measure interest rate risk from the profit perspective, the Group simulates basic parallel movements in interest rates ± 2% in a period of 12 months, and the potential decrease in net interest income is to be maintained within a 10% limit of realized net interest income for the observed period (from beginning of the year) projected to a yearly basis. Potential change in net interest income amounts to HRK52,425K representing 10.22% of net interest income (2015: change by HRK47,633K, or 9.34% of net interest income).

Additionally, at least once a year stress tests are conducted, whereby the Group tests effects of adverse interest rate movements for specific product types on the market, on net interest income, by assuming a decrease of active interest rates and an increase of passive interest rates.

Risk Management Division is reporting monthly to the Assets and Liabilities Management Committee about exposure of the interest rate risk in the Bank's non-trading book.

2.5 Foreign Exchange Risk

The Group is exposed to FX risk through transactions in foreign currencies.

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

The Group conducts business activities trying to minimize the gap between assets and liabilities denominated in or linked to foreign currency.

The Group manages the currency risk by setting principles and limits for foreign currency exposures and monitoring exposures against these limits. The Group directs their business activities towards trying to minimize the gap between assets and liabilities denominated in or linked to a foreign currency, and maintaining daily business activities within the internal and regulatory limits per currency.

The Group is primarily exposed to changes in the euro exchange rate. At December 31 2016, value of the Group's assets denominated in euros or euro-linked currencies amounted to HRK6,420,270K (2015: HRK6,518,720K), while liabilities denominated in euros or euro-linked currencies amounted to HRK6,498,412K (2015: HRK6,364,946). Hence, a 1% decline in the EUR/ HRK currency pair (appreciation of the HRK) would affect the result in the amount of –HRK781K (2015: +HRK1,538K).

2.5.1 FX Position Analysis

The following tables illustrate the value of total assets and liabilities of the Groupon December 31 2016 and December 31 2015 in HRK and foreign currencies (values denominated in HRK with foreign currency clause are mostly linked to EUR).

2. RISK MANAGEMENT (continued)

2016

HRK'000	HRK	HRK Linked to Foreign Currencies	EUR	Other Foreign Currencies	Total
ASSETS					
Cash and Amounts Due from Banks	870,141	-	542,078	142,393	1,554,612
Mandatory Reserve with the Croatian National Bank	1,300,796	-	-	-	1,300,796
Loans to and Receivables from Banks	20,168	-	725	161,194	182,087
Financial Assets at Fair Value in PNL	524,640	175,457	315,565	3,780	1,019,442
Financial Assets Available for Sale	1,223,857	301,295	1,067,095	161,691	2,753,938
Financial Assets Held to Maturity	429,802	15,023	-	-	444,825
Loans and Receivables from Customers	7,528,193	2,450,111	1,519,949	55,962	11,554,215
Assets Available for sale	89,349	-	-	-	89,349
Property and Equipment	140,765	-	-	-	140,765
Investment Properties	96,518	-	-	-	96,518
Intangible Assets	107,360	-	-	-	107,360
Deferred Tax Assets, Net	39,189	-	-	-	39,189
Tax Prepayment	347	-	-	-	347
Other Assets	415,111	930	32,042	6,301	454,384
TOTAL ASSETS	**12,789,156**	**2,942,816**	**3,477,454**	**531,321**	**19,737,826**
LIABILITIES					
Financial Liabilities at Fair Value in PNL	-	-	-	3,641	3,641
Deposits from Banks	336,030	-	145,634	27,469	509,133
Customer Deposits	9,757,309	280,055	5,483,135	504,305	16,024,804
Borrowings	144,693	493,521	88,446	-	726,660
Provisions for Liabilities and Expenses	60,779	8,00	-	-	60,787
Corporate Tax Liability	58	-	-	-	58
Other Liabilities	455,369	-	7,613	4,457	467,439
Total Equity	1,945,304	-	-	-	1,945,304
TOTAL LIABILITIES AND EQUITY	**12,699,542**	**773,584**	**5,724,828**	**539,872**	**19,737,826**
NET FOREIGN EXCHANGE POSITION	**86,693**	**2,169,232**	**(2,247,374)**	**(8,551)**	**-**

2. RISK MANAGEMENT (continued)

2015

HRK'000	HRK	HRK Linked to Foreign Currencies	EUR	Other Foreign Currencies	Total
ASSETS					
Cash and Amounts Due from Banks	817,537	-	641,649	170,929	1,630,115
Mandatory Reserve with the Croatian National Bank	1,172,198	-	107,372	-	1,279,570
Loans to and Receivables from Banks	213,444	-	1,063	47,406	261,913
Financial Assets at Fair Value in PNL	550,795	165,786	303,113	-	1,019,694
Financial Assets Available for Sale	1,108,044	381,613	589,077	142,576	2,221,310
Financial Assets Held to Maturity	556,639	15,125	-	-	571,764
Loans and Receivables from Customers	5,983,461	2,873,795	1,389,876	50,882	10,298,014
Assets Available for Sale	7,930	-	-	-	7,930
Property and Equipment	142,236	-	-	-	142,236
Investment Properties	9,568	-	-	-	9,568
Intangible Assets	117,010	-	-	-	117,010
Deferred Tax Assets, Net	10,750	-	-	-	10,750
Tax Prepayment	371	-	-	-	371
Other Assets	387,477	346	49,905	6,100	443,828
TOTAL ASSETS	**11,077,460**	**3,436,665**	**3,082,055**	**417,893**	**18,014,073**
LIABILITIES					
Financial Liabilities at Fair Value in PNL	-	-	-	-	-
Deposits from Banks	273,749	-	62,140	21,750	357,639
Customer Deposits	8,756,338	288,026	5,057,423	391,807	14,493,594
Borrowings	76,649	481,578	447,156	-	1,005,383
Hybrid Instruments	-	-	-	-	-
Provisions for Liabilities and Expenses	36,722	1,00	-	-	36,723
Other Liabilities	295,898	-	28,622	17,383	341,903
Total Equity	1,778,831	-	-	-	1,778,831
TOTAL LIABILITIES AND EQUITY	**11,218,187**	**769,605**	**5,595,341**	**430,940**	**18,014,073**
NET FOREIGN EXCHANGE POSITION	**(140,727)**	**2,667,060**	**(2,513,286)**	**(13,047)**	**-**

2. RISK MANAGEMENT (continued)

2.6. Operational Risk Management

Operational risk is inherent to all activities, processes, products and systems of the Group. The Group ensures appropriate operational risk management by applying procedures and a system of authorizations and responsibilities specified in detail in its internal by-laws, the Risk Management Policy and the Internal Operational Risk Management Manual as root documents. The operational risk management system has been established through appropriate bodies of the Group and an efficient internal control system.

The Group defines operational risk as a risk of an event which, as a consequence, exposes the Group to financial losses, with the cause being inadequate or ineffective internal processes, systems, human resources, or external influences. This definition includes legal risk. Significant operational risk is a risk of an event resulting in significant loss because of operational risk.

In order to efficiently manage the overall exposure to operational risk, the Group applies the following:

- Collecting and analyzing internal data about operational risk events,
- Self-assessment of risks and controls,
- Assessment of information technology risk, and
- Business Impact Analysis of unavailability of key business processes.

The Group assesses the outsourcing risk as an additional exposure to all significant risks arising from the fact that the Group does not itself perform the outsourced activities, but rather that those activities are performed by external vendors; hence, the impact of outsourcing on the Group's risk profile is assessed.

The Group assesses the impact of introducing a new product on its risk profile, which includes exposure to all significant risks.

For the purpose of efficient operational risk management, the Group has set up the Operational Risk Management Committee. Based on the reports on the Bank's exposure to operational risk, the Operational Risk Management Committee draws conclusions and makes decisions about appropriate measures necessary to undertake in order to overmaster the exposure to operational risk.

The Group applies the Standardized Approach in calculating the capital requirement for operational risk.

2.7. Capital Management

Capital requirement calculations are based on exposures to customers classified into the prescribed exposure categories, which are then weighted according to risk depending on the exposure category of the customer (exposure to sovereign debt, to institutions, public bodies, individuals, etc), remaining maturity, type of collateral (i.e. residential or commercial property), diversification of loans, identified number of days past due and the amount of provisions made.

The Group manages capital in line with the Internal Capital Adequacy Assessment Process (ICAAP). The Group determines risks to which it is or may be exposed, calculates and evaluates necessary capital requirements for exposure to certain risks, together with determining total necessary (internal) capital for current and following period in line with the business plan. In line with such capital needs capital planning is performed while items of available capital are solely items recognized for regulatory capital calculations.

2. RISK MANAGEMENT (continued)

2.7 Capital Management (continued)

In planning capital needs it is necessary to take into account capital adequacy, i.e. regulatory capital requirements for exposures to credit, market and operational risk.

Minimum regulatory capital adequacy defined by law on December 31 2016 was 8%. Maintaining conservation capital buffer of 2.5% and systemic risk capital buffer of 1.5% is mandatory by law. On top of all mentioned, the Group of credit institutions including the Bank and the Savings Bank is required by the supervisor to maintain an additional capital requirement equaling 3.35%. This brings total regulatory requirements to 15.35% on December 31 2016.

Capital information of the Bank and the Credit Institutions Group is presented below:

Bank (The Group's Parent Company)	**2016**	**2015**
	HRK'000	**HRK'000**
OWN FUNDS		
Tier-1 Capital	1,520,355	1,533,579
Common Equity Tier-1 Capital	*1,520,355*	*1,533,579*
Tier-2 Capital	-	-
Total Own Funds	1,520,355	**1,533,579**
Credit Risk Exposure Using Standardized Approach	7,695,697	7,353,639
Exposure to FX and Position Risk	580,229	940,430
Exposure to Operational risk	1,429,432	1,381,297
Exposure to Credit Value Adjustment Risk	1,258	109
Total Risk Exposure	**9,706,615**	**9,675,475**
Total Capital Adequacy Ratio	**15.66%**	**15.85%**

Credit Institutions Group	**2016**	**2015**
	HRK'000	**HRK'000**
OWN FUNDS		
Tier-1 Capital	1,519,628	1,532,463
Common Equity Tier-1 Capital	*1,519,628*	*1,532,463*
Tier-2 Capital	-	-
Total Own Funds	**1,519,628**	**1,532,463**
Credit Risk Exposure Using Standardized Approach	7,754,994	7,328,677
Exposure to FX and Position Risk	628,556	1,000,282
Exposure to Operational risk	1,451,068	1,402,563
Exposure to Credit Value Adjustment Risk	1,258	109
Total Risk Exposure	**9,835,877**	**9,731,630**
Total Capital Adequacy Ratio	**15.45%**	**15.75%**

3. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS

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 Group's portfolio exposed to credit risk represents the major source of estimation uncertainty. This and other key sources of estimations uncertainty, that have a significant risk of causing a possible material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below.

Impairment Losses on Loans and Receivables

The Group monitors the creditworthiness of its customers on an ongoing basis. In accordance with CNB regulations, the need for impairment of the Group's on and off-balance sheet credit risk exposure is assessed at least quarterly. Impairment losses are made mainly against the carrying amount of loans and advances to corporate and retail customers (summarized in Note 11), and as provisions for liabilities and expenses arising from off-balance sheet risk exposure to customers, mainly in the form of guarantees, documentary credits and undrawn loan commitments (summarized in Notes 22 and 38). Impairment losses are also considered for credit risk exposures to banks, and for other assets not carried at fair value, where the primary risk of impairment is not credit risk.

Following tables represent the summary of impairment losses of loans to and receivables from customers, as well as provisions for off-balance sheet exposures:

	Notes	2016 HRK'000	2015 HRK'000
Impairment Losses on Loans to and Receivables from Customers	11	1,386,144	2,197,676
Provisions for Off-Balance Sheet Exposures	22	22,269	20,143
Total		**1,408,413**	**2,217,819**

3. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

Financial Assets at Amortized 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, when and where these changes can be correlated with defaults.

The Group takes into consideration the combined effect of several events when assessing impairment and uses its experienced judgment 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 also has regard to the ranges of specific impairment loss rates prescribed by the CNB.

Gross value of specifically impaired loans and other interests receivables classified in risk groups B and C, and the rates of recognized impairment losses, were as follows as per year end:

	2016	2015
Gross Exposures (in HRK'000)	**2,085,639**	**3,305,805**
Impairment Loss (in HRK'000)	1,291,073	2,141,392
Impairment Rate	**61.90%**	**64.78%**

Each additional increase of one percentage point in the impairment rate on the gross portfolio at December 31 2016 would lead to recognition of additional impairment loss for the Group in the amount of HRK20,856K (2015: HRK33,058K).

The Group also seeks to recognize impairment losses which are known to exist at the reporting date, but which have not yet been specifically identified. In assessing impairment losses on a portfolio basis, historical loss rates are used which are determined in accordance with an internal methodology. The Group considers impairment losses depending on the type of assets, whereby the overall impairment rate may not be below 0.80% of the total on-balance sheet and off-balance sheet credit risk exposure, except in the case of available for sale assets at fair value in PNL. The amounts assessed as impaired on an individual basis are excluded from this calculation.

3. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

Financial Assets at Amortized Cost (continued)

The amount of impairment allowance at December 31 2016 estimated on a portfolio basis amounted to HRK133,973K (2015: HRK120,365K) of relevant on and off-balance sheet exposure of the Group classified in the risk category A. At the minimum rate set by the CNB, portfolio based impairment allowances would be HRK3,335K (2015: HRK4,223K) lower than the amount recognized by the Group.

If the Group did not have its internal methodology for assessing latent losses on a portfolio basis, it would have to apply the impairment rate equal to 1.00 percent of the relevant on-balance sheet and off-balance sheet credit risk exposure. In that case, impairment losses on a portfolio basis would be HRK29,356K (2015: HRK24,812K) higher than the amount recognized by the Group.

Market Value of Pledged Property and Foreclosed Assets

As disclosed (in Note 2.1.4 (c)), loans and receivables to customers include exposures with a carrying value of HRK2,085,639K (2015: HRK3,305,805K) classified by the Group as impaired in view of delinquencies in payment. A proportion of these loans is secured with collateral in the form of property, plant and equipment. When assessing loan recoverability based on pledged property, market value of pledged property is discounted to present value by applying discount factors and periods prescribed by internal acts, and in accordance with the CNB decision. Furthermore, as disclosed in Note 14, other assets at December 31 2016 include property, plant and equipment with gross book value of HRK186,017K representing assets collected in settlement of non-performing debt. At the end of the reporting period these assets were reclassified from assets available for sale to property investments. The Group recognized a HRK9,224K loss due to the assets impairments (2015: -). The net book value of the repossessed assets as of December 31 2016 was HRK87,209K (2015: HRK103,135K, Assets Available for Sale under Other Assets).

Information and fair value hierarchy of foreclosed assets of the Group as of December 31 2016 and December 31 2015 is presented below:

December 31 2016 Investment Properties (Note 14)	Level 1	Level 2	Level 3	Fair Value as of December 31 2016
	HRK'000	HRK'000	HRK'000	HRK'000
- Land	-	-	17,252	17,252
- Buildings	-	-	64,010	64,010
- Equipment	-	-	5,947	5,947
TOTAL	**-**	**-**	**87,209**	**87,209**

December 31 2015 Assets Available for Sale (Note 17 Other assets)	Level 1	Level 2	Level 3	Fair Value as of December 31 2015
- Land	-	-	31,868	31,868
- Buildings	-	-	65,320	65,320
- Equipment	-	-	5,947	5,947
TOTAL	**-**	**-**	**103,135**	**103,135**

3. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

Fair value of properties which make more than 80% of the Group's property investments is determined based on the value estimated in November 2016, while the rest of the property investment portfolio is based on the valuation from December 2014. Valuations in 2016 were done by HPB Nekretnine, a subsidiary of the Group. HPB Nekretnine valuators performed valuations as independent court experts with necessary skills and new experience in property valuation and no interest in the assets or their estimated value. Fair value is estimated in accordance with the Property Valuation Act (Official Gazette 78/ 2015) and corresponding Rulebook on Property Valuation Methods (Official Gazette 105/ 2015) with appropriate methods determined by the law, and by taking into count a number of factors for determining present market value. The valuation method was not changed during the year.

During the year there were no items which could be reclassified from level 3 to level 1 or vice versa.

Fair Value of Derivatives

Fair value of OTC derivatives that are quoted on active market is determined using their closing market price. For derivatives that are not traded on active markets, the Group determines contractual value applying internally developed models for fair value assessment.

Fair Value of Treasury Bills

The Group determines the fair value of treasury bills issued by the Ministry of Finance of the Republic of Croatia using an internal model which takes into account their remaining maturity and latest available auction prices of equivalent instruments. As at December 31 2016, the Group had HRK315,565K treasury bills classified as financial assets at fair value in PNL (2015: HRK303,114K). As at December 31 2016, carrying amount of treasury bills classified as financial assets available for sale amounted to HRK686,021K (2015: HRK675,525K).

Provisions for Court Cases Initiated Against the Group

In calculating provisions for court expenses the Group discounts expected future cash flows with respect to the liabilities using the CNB’s discount rate.

Taxation

The Group recognizes tax liabilities in accordance with the tax laws of the Republic of Croatia. Tax returns are subject to the approval of tax authorities that are entitled to carry out subsequent inspections of taxpayers’ records.

4. SEGMENT REPORTING

The Group's business segments represent the primary reportable segments. The primary format is based on the Group's management and internal reporting structure. As the Group does not allocate overhead expenses and equity to segments, segment profitability is not reported.

Business Segments

The Group comprises the following primary reportable segments:

- *Corporate Banking* — Includes loans, deposits and other transactions and balances with corporate customers,
- *Retail Banking* — Includes loans, deposits and other transactions and balances with retail customers,
- *Financial Markets* — Group financing operations and the aggregate liquidity and foreign exchange risk activities in respect of borrowings, transactions with debt securities, use of derivatives and investments in liquid assets. It also includes asset management, securities custody and brokerage services.
- *Direct Banking* — Includes undisturbed functioning and development of all the Group's direct products and services distribution channels, and card operations

The Group does not apply internal transfer prices in determining the financial results of segments.

Classification of individual sectors for the purposes of notes on the results and position of segments differs from other parts of the financial reports. This primarily refers to the owner of small enterprises, who are part of Corporate Banking in the report of segmentation, while in the financial reports part of positions related to the Retail Banking.

4. SEGMENT REPORTING (continued)

	Corporate	Retail	Financial Markets	Direct Banking	Unallocated	2016 HRK'000 Total
Net Interest Income	229,245	184,806	105,398	-	-	519,449
Net Fees and Commissions Income	59,530	93,536	3,523	23,967	18,195	198,751
Trading and Investment Income	-	-	118,253	-	-	118,253
Other Income	2,944	1,241	5,897	-	-	10,082
Operating Income	**291,719**	**279,583**	**233,071**	**23,967**	**18,195**	**846,535**
General and Administrative Expenses	(25,138)	(176,352)	(6,641)	(39,776)	(161,591)	(409,497)
Depreciation and Amortization	-	-	-	-	(45,416)	(45,416)
Impairment Losses on Loans and Other Assets	(175,054)	(8,564)	1	-	(17,676)	(201,293)
Provisions for Liabilities and Expenses	-	-	-	-	(25,384)	(25,384)
Operating Expenses	**(200,191)**	**(184,916)**	**(6,639)**	**(39,776)**	**(250,068)**	**(681,590)**
Profit Before Taxation					-	164,945
Deferred Income Tax	-	-	-	-	25,558	25,558
Profit for the Year	**-**	**-**	**-**	**-**	**25,558**	**190,503**
Segment Assets	7,420,928	5,262,290	6,481,490	192	-	19,164,900
Unallocated Assets	-	-	-	-	572,926	572,926
Total Assets	**7,420,928**	**5,262,290**	**6,481,490**	**192**	**572,926**	**19,737,826**
Segment Liabilities	7,652,281	9,405,091	382,406	1,420	-	17,441,198
Unallocated Equity and Liabilities	-	-	-	-	2,296,628	2,296,628
Total Equity and Liabilities	**7,652,281**	**9,405,091**	**382,406**	**1,420**	**2,296,628**	**19,737,826**

4. SEGMENT REPORTING (continued)

	Corporate	Retail	Financial Markets	Direct Banking	Unallocated	2015 HRK'000 Total
Net Interest Income	261,169	141,173	111,988	-	-	514,330
Net Fees and Commissions Income	51,070	86,272	5,474	29,254	20,915	192,985
Trading and Investment Income	-	-	46,698	-	-	46,698
Other Income	19,581	10,961	11,381	-	-	41,923
Operating Income	**331,820**	**238,406**	**175,541**	**29,254**	**20,915**	**795,936**
General and Administrative Expenses	(22,298)	(155,632)	(5,895)	(24,653)	(219,045)	(427,524)
Depreciation and Amortization	-	-	-	-	(46,053)	(46,053)
Impairment Losses on Loans and Other Assets	(117,431)	(54,713)	(5,061)	-	(7,451)	(184,657)
Provisions for Liabilities and Expenses	-	-	-	-	(9,023)	(9,023)
Operating Expenses	**(139,729)**	**(210,345)**	**(10,956)**	**(24,653)**	**(281,572)**	**(667,257)**
Profit Before Taxation	**-**	-	-	-		128,679
Deferred Income Tax	-	-	-	-	(3,902)	(3,902)
Profit for the Year	**-**	**-**	**-**	**-**	**(3,902)**	**124,777**
Segment Assets	6,577,530	4,726,538	6,176,454	-	-	17,480,522
Unallocated Assets	-	-	-	-	533,551	533,551
Total Assets	**6,577,530**	**4,726,538**	**6,176,454**	**-**	**533,551**	**18,014,073**
Segment Liabilities	6,637,616	8,963,639	500,648	-	-	16,101,903
Unallocated Equity and Liabilities	-	-	-	-	1,912,170	1,912,170
Total Equity and Liabilities	**6,637,616**	**8,963,639**	**500,648**	**-**	**1,912,170**	**18,014,073**

5. CASH AND RECEIVABLES FROM BANKS

	2016 HRK'000			2015 HRK'000		
	HRK	Foreign Currency	Total	HRK	Foreign Currency	Total
Cash in Hand						
Held by the Group	201,942	92,231	294,173	199.050	82.673	281.723
Held by Other Parties	127,173	-	127,173	130.445	-	130.445
Cheques in the Course of Collection	-	18	18	-	17	17
	329,115	**92,249**	**421,364**	**329.495**	**82.690**	**412.185**
Amounts Due from Banks						
Current Accounts with Domestic Banks	-	1,070	1,070	-	67.848	67.848
Current Accounts with Foreign Banks	-	591,151	591,151	-	662.040	662.040
Giro Account with the CNB	502,603	38,424	541,027	488.042	-	488.042
	502,603	**630,645**	**1,133,248**	**488.042**	**729.888**	**1.217.930**
Total	**831,718**	**722,894**	**1,554,612**	**817.537**	**812.578**	**1.630.115**

6. MANDATORY RESERVE WITH CROATIAN NATIONAL BANK

			2016 HRK'000			2015 HRK'000
	HRK	Foreign Currency	Total	HRK	Foreign Currency	Total
Mandatory Reserve	1,300,796	-	1,300,796	1,172,199	107,371	1,279,570
Total	**1,300,796**	**-**	**1,300,796**	**1,172,199**	**107,371**	**1,279,570**

The mandatory reserve with the CNB represents the amount required to be deposited with the CNB.

The mandatory reserve requirement was set at 12 percent of HRK and foreign currency deposits, borrowings and issued debt securities (December 31 2015: 12%).

As at December 31 2016 required minimum rate of maintenance of the HRK mandatory reserve with the CNB equaled 70% (2015: 70%), whereas the remaining 30 percent (2015: 30%) could be held in the form of other liquid receivables.

The CNB's Decision taking effect on January 13 2016 has cancelled the FX reserve requirements which left HRK107.4M to the Bank.

The CNB does not pay the fee on mandatory reserve fund and mandatory reserve funds.

7. LOANS TO AND RECEIVABLES FROM BANKS

	2016 HRK'000	2015 HRK'000
Short-Term Placements with Domestic Banks	20,000	80.000
Short-Term Placements with Foreign Banks	148,389	134.959
Total Short-Term Placements and Loans Banks	**168,389**	**214.959**
Guarantee Deposits with Foreign Banks	13,524	13.492
Long-Term Placements with Domestic Banks	-	-
Long-Term Loans to Domestic Banks - CBRD	-	33.022
Total Short-Term Placements and Loans Banks	**13,524**	**46.514**
Short-Term Placements with Domestic Non-Banking Financial Institutions	500	500
Long-Term Placements with Domestic Non-Banking Financial Institutions	100	363
Long-Term Placements with Domestic Non-Banking Financial Institutions	**600**	**863**
Provisions for Impairment Losses (Non-Banking Financial Institutions)	**(500)**	**(500)**
Accrued Interests Not Yet Due	74	77
Total Interests Receivable	**74**	**77**
Total	**182,087**	**261.913**

In 2016 long-term CBRD loan had matured (2015: HRK33,022K).

Guarantee deposits mainly relate to deposits for card operations.

Movements in Impairment Allowance

No changes in impairment allowance for loans and receivables from banks occurred in 2016 (2015: -).

	2016 HRK'000	2015 HRK'000
Balance at January 1	500	500
(Decrease)/ Increase in Impairment Losses on Loans to and Receivables from Banks	-	-
Balance at December 31	**500**	**500**

8. FINANCIAL ASSETS AT FAIR VALUE IN PNL

	2016 HRK'000	2015 HRK'000
Trading Instruments		
Listed Debt Securities		
Treasury Bills of the Ministry of Finance	315,565	303,113
Bonds of the Ministry of Finance	466,838	208,800
Listed Debt Securities	**782,403**	**511,913**
Listed Shares of Investment Funds	**187,801**	**470,555**
Listed Equity Securities	**39,393**	**33,947**
Total	**1,009,597**	**1,016,415**
Fair Value of Forwards	3,780	-
Accrued Interests Not Yet Due	6,064	3,279
Total	**1,019,441**	**1,019,694**

9. FINANCIAL ASSETS AVAILABLE FOR SALE

	2016 HRK'000	2015 HRK'000
Debt Securities Not Listed		
Bonds of the Ministry of Finance	1,502,626	1,396,368
Corporate Bonds	127,957	79,742
Foreign Government Bonds	394,206	-
	2,024,789	**1,476,110**
Debt Securities Not Listed		
Treasury Bills of the Croatian Ministry of Finance	686,021	675,525
Equity Securities Not Listed		
- Corporate	15,414	38,930
- Non-Banking Financial Institutions	-	1,670
	15,414	**40,600**
Listed Equity Securities		
- Corporate	7,241	6,706
- Non-Banking Financial Institutions	2,141	-
Provisions for Impairment Losses on Equity Securities	(5,060)	(5,060)
	4,322	**1,646**
Accrued Interests Not Yet Due	23,392	27,429
Total	**2,753,938**	**2,221,310**

In accordance with the applicable accounting policies, the Group recognizes available for sale financial assets at fair value with changes in fair value recognized within a fair value reserve in other comprehensive income.

9. FINANCIAL ASSETS AVAILABLE FOR SALE (continued)

Movement in Impairment Allowance for Financial Assets Available for Sale

	Individually Identified Losses	Portfolio Based Losses	2016 HRK'000 Total	Individually Identified Losses	Portfolio Based Losses	2015 HRK'000 Total
At January 1	**5,060**	**-**	**5,060**	**40,168**	**-**	**40,168**
Increase/ (Decrease) of Impairment Losses	-	-	**-**	5,060	-	**5,060**
Other (Conversion of Wholly Impaired Receivables into Equity Stake or Loans Based on Pre-Bankruptcy Settlement)	-	-	**-**	(40,168)		(40,168)
At December 31	**5,060**	-	**5,060**	**5,060**	**-**	**5,060**

10. FINANCIAL ASSETS HELD TO MATURITY

	2016 HRK'000	2015 HRK'000
Bonds of the Ministry of Finance	172,768	277,473
Bills of Exchange	277,273	320,226
	450,041	**597,699**
Accrued Interests Not Yet due	2,994	5,700
Provisions for Impairment Losses	**(1,439)**	**(23,380)**
Portfolio Based Impairment Allowance for Identified Losses	**(6,771)**	**(8,255)**
Total	**444,825**	**571,764**

Movement in Impairment Allowance for Financial Assets Held to Maturity

The movements in the impairment allowance for financial assets held to maturity were as follows:

	Individually Identified Losses	Portfolio Based Losses	2016 HRK'000 Total	Individually Identified Losses	Portfolio Based Losses	2015 HRK'000 Total
At January 1	**23,380**	**8,255**	**31,635**	**23,104**	**5,746**	**28,850**
Increase/ (Decrease) of Impairment Losses	395	(1,484)	**(1,089)**	276	2,509	**2,785**
Write-Offs and Other	(22,336)	**-**	**(22,336)**	-	-	-
At December 31	**1,439**	**6,771**	**8,210**	**23,380**	**8,255**	**31,635**

11. LOANS TO AND RECEIVABLES FROM CUSTOMERS

	2016 HRK'000	2015 HRK'000
Short-Term Loans		
Corporate	1,997,205	2,376,908
Retail	841,341	1,166,199
Total Short-Term Loans	**2,838,546**	**3,543,107**
Long-Term Loans		
Corporate	5,939,847	5,305,410
Retail	4,110,031	3,597,161
Total Long-Term Loans	**10,049,878**	**8,902,571**
Total Gross Loans	**12,888,424**	**12,445,678**
Accrued Interests Due	11,259	11,269
Accrued Interests Not Yet Due	40,676	38,743
Provisions for Impairment Losses	**(1,280,961)**	**(2,104,998)**
Portfolio Based Impairment Allowance for Identified Losses	**(105,183)**	**(92,678)**
Total	**11,554,215**	**10,298,014**
Total Impairment Allowance and Provisions as a Percentage of Gross Loans to Customers	9.94%	16.91%

11. LOANS TO AND RECEIVABLES FROM CUSTOMERS (continued)

Movements in Impairment Allowance

Movements in the impairment allowance on loans to and receivables from customers were as follows:

	Individually Identified Losses	Portfolio Based Losses	2016 HRK'000 Total	Individually Identified Losses	Portfolio Based Losses	2015 HRK'000 Total
At January 1	**2,104,998**	**92,678**	**2,197,676**	**1,974,201**	**101,815**	**2,076,016**
Increase/ (Decrease) of Impairment Losses	170,294	12,505	**182,799**	177,196	(9,137)	**168,059**
Reclassification	(620,973)	-	**(620,973)**	-	-	**-**
Net Foreign Exchange Loss/ (Gain)	(5,534)	-	**(5,534)**	(5,716)	-	**(5,716)**
Write-Offs and Other	(367,824)	-	**(367,824)**	(40,683)	-	**(40,683)**
At December 31	**1,280,961**	**105,183**	**1,386,144**	**2,104,998**	**92,678**	**2,197,676**

12. ASSETS AVAILABLE FOR SALE

a) The Group's Assets Available for Sale

Assets Available for Sale include loans and receivables and equity stakes in companies which are intended to be sold and are classified in accordance with the IFRS 5: Non-current Assets Available for Sale and Discontinued Operations.

Equity stakes in companies available for sale are as follows:

	Industry	Domicile	Ownership at December 31 2016 %
H1 Telekom plc.	Telecommunications	Croatia	58.17
Drvna Industrija Spačva d.d.	Other Carpentry and Components Production	Croatia	26.48

The Group plans to compensate its investment in the aforementioned companies by sale and not by realizing its share rights. These investments are currently up for sale and the Group has made all the necessary measures in order to sell them in an acceptable time period usual for these types of transactions.

The Group did not recognize additional impairments on its assets available for sale in the PNL report during the reporting period (2015: -).

Investment in H1 Telekom plc.

On 25 March 2008 the Bank made an agreement with H1 Telekom plc. to convert credit receivables from long-term loan into the company's equity. This agreement brought HPB 41.25% equity stake in the company. The stake was increased to 58.17% after converting receivables from bond, long-term loan and interests receivables into equity after the completion of the pre-bankruptcy settlement on 29 July 2015.

Financial position of H1 TELEKOM is included in the consolidated financial position of HPB Group by using shortcut consolidation procedure as described in IFRS 5 Non-current Assets Available for Sale and Discontinued Operations. Consolidation of H1 TELEKOM is shown in the Note 18 Other Assets and Note 25 Other Liabilities.

Loans and Receivables

On December 29 2016 the Bank made an agreement on receivables sale with a financing company APS Delta S.A. owned by APS Holding after getting approval by the CNB on meeting sale conditions of materially important placements. Rights and benefits of the assets are transferred to the buyer upon receiving payments, and these assets were reclassified from loans to customers to financial assets available for sale. The assets were payed after the balance sheet date on January 19 2017 when the assets were transferred to the buyer.

b) Assets Available for Sale are as follows:

	2016 HRK'000	2015 HRK'000
Equity Stakes	7,930	7,930
Loans and Receivables	81,419	-
Total as of December 31	**89,349**	**7,930**

c) Movements in Assets Available for Sale:

	2016 HRK'000	2015 HRK'000
Balance at January 31	**7,930**	**7,930**
Less Impairments	-	-
Reclassification from Loans and Receivables to Assets Available for Sale	81,419	-
Balance at December 31	**89,349**	**7,930**

13. PROPERTY AND EQUIPMENT

2016	**Land and Buildings HRK'000**	**Computers, Equipment and Motor Vehicles HRK'000**	**Assets Under Construction HRK'000**	**Total HRK'000**
Cost or Estimated Value				
Balance at January 1 2016	**167,517**	**306,242**	**3,121**	**476,880**
Revaluation of Land and Buildings	-	-	-	-
Additions	-	-	15,514	15,514
Amounts Written-Off	-	(35,747)	-	(35,747)
Brought Into Use	78	14,745	(14,823)	-
Balance at December 31 2016	**167,595**	**285,244**	**3,812**	**456,647**
Accumulated Depreciation				
Balance at January 1 2016	**(60,395)**	**(274,249)**	**-**	**(334,644)**
Charge for the Year	(3,025)	(13,796)	-	(16,821)
Revaluation	-	-	-	-
Amounts Written-Off	-	35,582	-	35,582
Balance at December 31 2016	**(63,420)**	**(252,463)**	**-**	**(315,883)**
Net Book Value				
Balance at January 1 2016	**107,122**	**31,993**	**3,121**	**142,236**
Balance at December 31 2016	**104,175**	**32,777**	**3,812**	**140,764**

2015	**Land and Buildings HRK'000**	**Computers, Equipment and Motor Vehicles HRK'000**	**Assets Under Construction HRK'000**	**Total HRK'000**
Cost or Estimated Value				
Balance at January 1 2015	**167,521**	**303,068**	**9,282**	**479,871**
Revaluation of Land and Buildings	(73)	-	-	(73)
Additions	-	-	6,788	6,788
Amounts Written-Off	-	(9,706)	-	(9,706)
Brought Into Use	69	12,880	(12,949)	-
Balance at December 31 2015	**167,517**	**306,242**	**3,121**	**476,880**
Accumulated Depreciation	**(57,444)**	**(269,202)**	**-**	**(326,646)**
Balance at January 1 2015	(2,951)	(14,717)	**-**	(17,668)
Charge for the Year	-	-	**-**	-
Revaluation	-	9,670	**-**	9,670
Amounts Written-Off	**(60,395)**	**(274,249)**	**-**	**(334,644)**
Balance at December 31 2015				
Net Book Value	**110,077**	**33,866**	**9,282**	**153,225**
Balance at January 1 2015	**107,122**	**31,993**	**3,121**	**142,236**
Balance at December 31 2015	**167,521**	**303,068**	**9,282**	**479,871**

As at December 31 2016, assets in the course of construction comprise equipment at cost of HRK3,876K (2015: HRK3,184K). The carrying value of land owned by the Group as at December 31 2016 was HRK45,895K (2015: HRK45,895K).

Group's property is in no way pledged to nor are there mortgage rights in favor of third parties.

14. INVESTMENT PROPERTIES

	Note	2016 HRK'000	2015 HRK'000
Cost			
Balance at January 1		11,744	11,744
Additions		-	-
Amounts Written-Off	17	186,017	-
Disposals		-	-
Balance at December 31		**197,761**	**11,744**
Accumulated Depreciation			
Balance at January 1		(2,176)	(1,916)
Charge for the Year		(259)	(260)
Balance at December 31		**(2,435)**	**(2,176)**
Impairment Loss			
Balance at January 1		-	**-**
Reclassification from Other Assets	17	(98,808)	**-**
Balance at December 31		**(98,808)**	**-**
Net Book Value			
Balance at January 1		9,568	9,828
Balance at December 31		**96,518**	**9,568**

In late 2016 the Group has reclassified fixed assets acquired by converting uncollected receivables in the amount of HRK186,017K to property investments. Impairments of the reclassified assets were HRK98,808K and the book value of the assets were HRK87,209K. The assets were initially recognized as available for sale but due to holding it long-term and inability to make a sale in a reasonable period it no longer fulfills criteria to be classified as available for sale according to the IFRS 5: Noncurrent Assets Held for Sale and Discontinued Operations.

Fair value hierarchy of investment properties as of December 31 2016 was as follows:

	Level 1 HRK'000	Level 2 HRK'00	Level 3 HRK'000	Fair Value as of December 31 2016 HRK'000
- Land	-	-	17,252	17,252
- Buildings	-	-	80,380	80,380
- Equipment	-	-	5,947	5,947
TOTAL	**-**	**-**	**103,579**	**103,579**

Fair value hierarchy of investment properties as of December 2015 was as follows:

	Level 1 HRK'000	Level 2 HRK'000	Level 3 HRK'000	Fair Value as of December 31 2015 HRK'000
- Buildings			27,141	27,141
TOTAL	-	**-**	**27,141**	**27,141**

Properties are assessed in accordance with the Property Assessment Act (Official Gazette 78/ 2015) and the Rulebook on Property Assessment Methods (Official Gazette 105/ 2015) by using appropriate methods with taking into count a number of factors for determining present market value. The assessment method was not changed during the year.

During the year there were no items which could be reclassified from level 3 to level 1 or vice versa.

15. INTANGIBLE ASSETS

2016	Software HRK'000	Leasehold Improvements HRK'000	Licenses HRK'000	Assets Under Construction HRK'000	Total HRK'000
Cost					
Balance at January 1 2016	**228,415**	**77,255**	**65,648**	**17,916**	**389,234**
Additions	-	-	-	26,992	26,992
Brought Into Use	12,389	13,021	3,754	(29,164)	-
Amounts Written-Off	(69)	(7,022)	(22)	(8,306)	(15,419)
Balance at December 31 2016	**240,735**	**83,254**	**69,380**	**7,438**	**400,807**
Accumulated Amortization					
Balance at January 1 2016	**(149,053)**	**(70,537)**	**(52,634)**	**-**	**(272,224)**
Charge for the Year	(19,551)	(5,134)	(3,651)	-	(28,336)
Amounts Written-Off	69	7,022	22	-	7,113
Balance at December 31 2016	**(168,535)**	**(68,649)**	**(56,263)**	**-**	**(293,447)**
Net Book Value					
Balance at January 1 2016	**79,362**	**6,718**	**13,014**	**17,916**	**117.010**
Balance at December 31 2016	**72.200**	**14,605**	**13,117**	**7,438**	**107,360**

2015	Software HRK'000	Leasehold Improvements HRK'000	Licenses HRK'000	Assets Under Construction HRK'000	Total HRK'000
Cost					
Balance at January 1 2015	**227,129**	**77,732**	**65,404**	**17,598**	**387.863**
Additions	-	-	-	12,231	12.231
Brought Into Use	1,287	2,945	244	(4,476)	-
Amounts Written-Off	-	(3,422)	-	(7,437)	(10.859)
Balance at December 31 2015	**228,416**	**77,255**	**65,648**	**17,916**	**389.235**
Accumulated Amortization					
Balance at January 1 2015	**(129,009)**	**(69,456)**	**(49,056)**	**-**	**(247.521)**
Charge for the Year	(20,044)	(4,504)	(3,578)	-	(28.126)
Amounts Written-Off	-	3,422	-	-	3.422
Balance at December 31 2015	**(149,053)**	**(70,538)**	**(52,634)**	**-**	**(272.225)**
Net Book Value					
Balance at January 1 2015	**98,120**	**8,276**	**16,348**	**17,598**	**140,342**
Balance at December 31 2015	**79,363**	**6,717**	**13,014**	**17,916**	**117,010**

As at December 31 2016 assets in ongoing construction comprise application software, licenses and leasehold improvements at a cost of HRK17,438K (2015: HRK17,916K) which are being prepared for use by the Group.

16. NET DEFERRED TAX ASSETS

a) Recognized Deferred Tax Assets and Liabilities - Group

Changes in the temporary differences and portions of deferred tax assets and deferred tax liabilities, and the related balances at the Group in 2016 are presented below:

2016	2016 HRK'000	Recognized as Income/ (Expense) in the PNL Report HRK'000	Recognized as Other Comprehensive Income HRK'000	2015 HRK'000
Deferred Tax Assets				
Loans and Advances to Customers	8,601	(1,260)	-	9,861
Other Provisions	3	(14)	-	17
Financial Assets	14,833	(7,641)	-	22,474
Recognized Tax Loss	35,303	35,303	-	-
Deferred Tax Liability				
Borrowings	(401)	22	-	(423)
Revaluation Reserve	(184)	-	184	(219)
Fair Value Reserve	(18,591)	-	1,931	(20,522)
Prepaid Expenses	(375)	63	-	(438)
Deferred Tax Assets, Net	**39,189**	**26,473**	**2,115**	**10,750**

Due to corporate tax change for periods on and after January 1 2017 the tax deferred assets and liabilities' effect in the PNL report is HRK2,708K lower than without the corporate tax change (expenditure). Also the effect in other comprehensive income is HRK2,086K higher than without the change (revenue).

Changes in the temporary differences and portions of deferred tax assets and deferred tax liabilities, and the related balances at the Group in 2015 are presented below:

2015	2015 HRK'000	Recognized as Income/ (Expense) in the PNL Report HRK'000	Recognized as Other Comprehensive Income HRK'000	2014 HRK'000
Deferred Tax Assets				
Loans and Advances to Customers	9,861	(1,044)	-	10,905
Other Provisions	17	(1,123)	-	1,140
Financial Assets	22,474	(1,582)	-	24,056
Deferred Tax Liability				
Borrowings	(423)	45	-	(468)
Revaluation Reserve	(219)	-	63	(282)
Fair Value Reserve	(20,522)	-	(2,303)	(18,219)
Prepaid Expenses	(438)	91	-	(529)
Deferred Tax Assets, Net	**10,750**	**(3,613)**	**(2,240)**	**16,603**

17. OTHER ASSETS

	2016 HRK'000	2015 HRK'000
Fees Receivable	24,202	28,052
Foreclosed Tangible Assets	-	192,719
Items in Course of Collection	220,731	122,424
Deferred Fee Expenses	366	681
Prepaid Expenses	10,525	5,744
Receivables Arising from Syndicated Loans	57,636	55,475
Other Receivables	33,498	28,831
Total Other Assets, Gross	**346,958**	**433,926**
Impairment Loss	**(22,707)**	(110,621)
Total Other Assets	**324,251**	**323,305**
Discontinued Operations	130,133	**120,523**
Total	**454,384**	**443,828**

Items in course of collection mainly relate to HRK and foreign currency receivables from corporations in course of settlement, amounting to HRK38,725K (2015: HRK55,713K), as well as other receivables in course of settlement (card operations, payment services, currency trade).

Item discountinued operations relates to Bank's share in total liabilities of a company held for sale, minus intercompany transactions between the Bank and the Company. As per December 31 2016 the Company's total liabilities were HRK226,389K (2015: HRK217,758K), while the Bank's share was HRK131,680K (2015: HRK126,660K), minus internal transactions in the amount of HRK1,547K (2015: HRK6,108K).

Movements in Impairment Allowance

Movements in the impairment allowance on other assets were as follows:

	2016 HRK'000	2015 HRK'000
Balance at January 1	110,201	120,989
Increase in Impairment Losses	10,632	3,191
Disposal of Repossessed Assets	-	(13,188)
Reclassification of Foreclosed Assets	(98,808)	-
Foregin Exchange Currencies	141	-
Used Impairments and Other	541	(791)
Balance at December 31	**22,707**	**110,201**

17. OTHER ASSETS (continued)

In late 2016 tangible assets acquired by converting uncollected debt were reclassified to property investment. The assets were initially classified as available for sale but due to long term holding and inability of sale in a reasonable period it no longer meets the criteria to be classified as available for sale according to the IFRS 5 Non-current Assets Held for Sale and Discontinued Operations.

After previously mentioned reclassification the Group did not have tangible assets acquired by converting uncollected debt classified as available for sale (2015: book value was HRK192,719K and it included HRK131,820K of properties, HRK48,885K of land and HRK12,038K of equipment).

The Group recognized a loss on the mentioned assets in the amount of HRK9,224K (2015: 0).

Movements in Foreclosed Tangible Assets

The following table represents movements in foreclosed assets during 2016:

Gross Carrying Value	Note	**2016 HRK'000**	**2015 HRK'000**
Balance as at January 1		**192,719**	**258,180**
Repossessed		-	1,144
Leased Out		-	-
Disposal of Repossessed Assets		(6,724)	(68.691)
Investment Property (or Investments in Facilities) and Other		22	2,086
Reclassification of Investment in Property	14	(186,017)	
Balance as at December 31		**-**	**192,719**
Impairment Losses			
Balance as at January 1		**(89,584)**	**(102,772)**
Impairment Loss in the PNL Report		(9,224)	-
Leased Out		**-**	-
Disposal of Repossessed Assets		**-**	13,188
Reclassification of Property Investments	14	98,808	-
Balance as at December 31		**-**	**(89,584)**
Net Carrying Value			
Balance as at January 1		**103,135**	**155,408**
Balance as at December 31		**-**	**103,135**

The Group has sold repossessed assets with a value of HRK814K during 2016 (2015: HRK55,503K). Also assets in the amount of HRK5,911K (2015: -) were put in financial lease during the year.

Income arising from disposal of assets amounted to HRK254K during 2016 (2015: income of HRK14,935K).

18. FINANCIAL LIABILITIES AT FAIR VALUE IN PNL

	2016 HRK´000	2015 HRK´000
Negative Fair Value of Forward Foreign Exchange Contracts	3,641	-
Negative Fair Value of Cross Currency Swaps	-	-
Balance at December 31	**3,641**	-

19. DEPOSITS FROM BANKS

	2016 (HRK'000)			2015 (HRK'000)		
	HRK	Foreign Currency	Total	HRK	Foreign Currency	Total
Demand Deposits	35,265	142,158	177,423	13,361	65,001	78,362
Term Deposits	300,011	30,872	330,883	259,800	18,800	278,600
Interests Payable Not Yet Due	754	73	827	587	90	677
Total	**336,030**	**173,103**	**509,133**	**273,748**	**83,891**	**357,639**

20. DEPOSITS FROM CUSTOMERS

	2016 (HRK'000)			2015 (HRK'000)		
	HRK	Foreign Currency	Total	HRK	Foreign Currency	Total
Demand Deposits						
Retail	2,294,830	629,288	2,924,118	2,003,645	392,668	2,396,313
Corporate	1,856,532	502,471	2,359,003	1,308,272	210,111	1,518,383
Restricted Deposits						
Retail	5,972	4,651	10,623	6,006	4,613	10,619
Corporate	1,624,973	66,177	1,691,150	1,939,895	237,440	2,177,335
	5,782,307	**1,202,587**	**6,984,894**	**5,257,818**	**844,832**	**6,102,650**
Term Deposits						
Retail	2,461,295	3,938,531	6,399,826	2,414,822	4,072,615	6,487,437
Corporate	1,764,676	818,869	2,583,545	1,344,321	486,665	1,830,986
	4,225,971	**4,757,400**	**8,983,371**	**3,759,143**	**4,559,280**	**8,318,423**
Interests Payable Not Yet Due	29,239	27,300	56,539	32,928	39,593	72,521
Total	**10,037,517**	**5,987,287**	**16,024,804**	**9,049,889**	**5,443,705**	**14,493,594**

Restricted deposits mainly relate to clients' deposits which are predetermined for special purposes, such as those based on court orders.

21. BORROWINGS

	2016 (HRK'000)			2015 (HRK'000)		
	HRK	Foreign Currency	Total	HRK	Foreign Currency	Total
Short-Term Loans from Other Financial Institutions	-	-	-	-	394	394
Short-Term Loans from the CBRD	14,777	-	14,777	-	-	-
Long-Term Bank Borrowings	-	88,426	88,426	-	446,650	446,650
Long-Term Borrowing from the CBRD	620,995	-	620,995	557,730	-	557,730
Accrued Interests Due	2,126	-	2,126	189	-	189
Accrued Interests Not Yet due	316	20	336	309	111	420
Total	**638,214**	**88,446**	**726,660**	**558,228**	**447,155**	**1,005,383**

In accordance with their terms, borrowings from the CBRD are used to fund loans to customers of the Group for financing eligible reconstruction and development projects at preferential interest rates.

22. PROVISIONS FOR LIABILITIES AND EXPENSES

	2016 HRK'000	2015 HRK'000
Litigation Provisions	37,217	15,230
Provisions for Contingent Liabilities	250	712
Provisions for Other Liabilities	1,301	1,350
Provisions for Off-Balance Sheet Exposures	22,019	19,431
Balance at December 31	**60,787**	**36,723**

Movements in Provisions for Liabilities and Expenses

The movements in provisions for liabilities and expenses were as follows:

	2016 HRK'000	2015 HRK'000
Balance at January 1	36,723	29,758
Increase/ (Decrease) in Provisions in the PNL Report	25,384	9,023
Amounts Utilized/ Reversed During the Reporting Period	(1,320)	(2,058)
Balance at December 31	**60,787**	**36,723**

23. OTHER LIABILITIES

	2016 HRK'000	2015 HRK'000
Trade Accounts Payable	17,494	14,904
Salaries, Amounts to be Withheld from Salaries, Taxes and Contributions	102,902	15,771
Provisions for Retirement Benefits, Termination Benefits and Similar Liabilities	3,885	4,964
Fees Payable	14,534	12,809
Items in Course of Settlement	83,438	70,277
Prepaid Deferred Income	16,144	15,144
Other Liabilities	93,999	102,476
Provisions for Awards to Employees	3,517	-
Total Continued Operations	**335,913**	**236,345**
Discontinued Operations	**131,526**	**105,558**
Total	**467,439**	**341,903**

Item *disontinued operations* relates to Bank's share in total liabilities of the company held for sale H1 TELEKOM, minus intercompany transactions between the Bank and the Company. Accordingly, as per December 31 2016 total liabilities of the company held for sale amount to HRK226,389K (2015: HRK217,758K), with the Bank's share amounting to HRK131,680K (2015: HRK126,660K, minus elimination of intercompany transactions in the amount of HRK154K (2015: HRK21,102K)

24. EQUITY

a) Share Capital

On December 31 2016, the authorized, subscribed and fully paid-in capital amounted to HRK1,214,755K (2015: HRK1,214,755K) and comprised of 2,024,625 (2015: 2,024,625) of authorized ordinary shares with a face value of HRK600 each.

At December 31 2016 the Group's parent company held 795 treasury shares (2015: 795) amounting to HRK477K (2015: HRK477K).

The Shareholders' Meeting decided in 2016 to use 2015 profit in a form of reserves of own shares in the amount of HRK4,000K which increased reserves of own shares to HRK4,477K at the end of 2016 (2015: HRK477K).

24. EQUITY (continued)

The ownership structure is as follows:

	Paid-In Capital HRK'000	2016 Ownership (%)	Paid-In Capital HRK'000	2015 Ownership (%)
Republic of Croatia	515,421	42.43%	515,421	42.43%
Hrvatska Pošta d.d.	144,966	11.93%	144,966	11.93%
State Agency for Deposit Insurance and Bank Resolution	109,091	8.98%	109,091	8.98%
Croatian State Pension Insurance Fund	106,387	8.76%	106,387	8.76%
Fund NEK	28,727	2.36%	28,456	2.34%
Others	310,184	25.53%	310,454	25.56%
Total	**1,214,775**	**100.00%**	**1,214,775**	**100.00%**

b) Capital Gain

Capital gain is the excess amount paid with respect to nominal value of shares at the issue of new shares. In 2016 there were no capital gains from emitting new shares (2015: -).

c) Fair Value Reserve

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

The movements of fair value reserve during 2016 and 2015 were as follows:

	2016 HRK'000	**2015** HRK'000
Balance at January 1	**82,089**	72,867
Net Unrealized Gain from Financial Assets Available for Sale	45,506	11,527
The Cumulative Gain on the Sale of Available for Sale Assets was Transferred to the PNL Report.	(44,836)	-
Deferred Taxes in Respect of Profits on Revaluation of Available For Sale Financial Assets	(134)	(2,305)
Corporate Tax Rate Change Effect on Deferred Tax of Profits from Impairments of Financial Assets Available for Sale	2,065	-
Balance at December 31	**84,690**	**82,089**

24. EQUITY (continued)

d) Revaluation Reserve

A revaluation reserve in the amount of HRK839K (2015: HRK877K), net of tax, arises from the revaluation of land and buildings of the Group.

In 2016 change on the position of revaluation reserve amounts to HRK38K (2015: decrease by HRK10K). The movements of revaluation reserve in 2016 and 2015 were as follows:

	2016 HRK'000	**2015** HRK'000
Balance at January 1	**877**	**887**
Decrease in the Revaluation Reserve on Depreciation of Assets	(73)	(73)
Deferred Tax in Respect of the Revaluation Reserve	15	63
Corporate Tax Change Effect on Deferred Tax Related to Lower Revaluation Reserve	20	
Balance at December 31	**839**	**877**

e) Proposed Dividends

Dividends payable are not accounted for until they have been ratified at the Shareholders' Meeting. In 2016 dividend payments amounted to HRK30,762K (2015: -) based on the Decision from the Shareholder's Meeting on May 16 2016 for paying HRK15.2 dividend per share from 2015 profit.

f) Statutory Reserves

The Group's parent company and the Savings Bank as its subsidiary are required to build legal reserves by appropriating 5% of net profit for the year until these reserves reach 5% of share capital. The balance of legal reserve at December 31 2016 amounted to HRK6,161K (2015: -), i.e. 0.5% of share capital.

Other reserves as at December 31 2016 amounted to HRK358,306K (2015: HRK358,306K).

g) Retained Earnings/ (accumulated losses)

The Decision on the Shareholders' Meeting in 2016 was to distribute part of 2015 profit after transfer to statutory reserves, reserves of own shares and dividend payments, in the amount of HRK82,294K to retained earnings (2015: 0). Shareholders' meetings of subsidiaries, except H1 TELEKOM, in 2016 resulted with decisions on retaining 2015 earnings.

h) Financial Leverage Ratio

In line with article 429 of Regulation EU 575/ 2013 from January 01 2014, calculus of financial leverage ratio between common tier-1 equity and total exposure is mandatory for each credit institution.

Financial leverage ratio for the parent company of the Credit Institutions Group is as follows:

	2016	**2015**
Financial Leverage Ratio (%)	6.93	7.83

25. INTERESTS AND SIMILAR INCOME

a) Analysis by Product:

	2016 HRK'000	2015 HRK'000
Loans and Advances to Customers		
- Corporate	284,424	341,851
- Individuals	317,880	311,069
	602,304	**652,920**
Loans and Advances to Customers	750	3,276
Debt Securities	114,181	119,309
Bills of Exchange	16,154	17,322
Total	**733,389**	**792,827**

b) Analysis by Source:

	2016 HRK'000	2015 HRK'000
Corporate	153,790	193,914
Retail	317,880	311,069
Government and Public Sector	259,257	278,372
Banks and Other Financial Institutions	1,833	3,953
Other Organizations	629	5,519
Total	**733,389**	**792,827**

26. INTERESTS AND SIMILAR EXPENSE

a) Analysis by Product

	2016 HRK'000	2015 HRK'000
Borrowings	18,857	29,592
Customer Deposits		
- Corporate	55,695	71,962
- Retail	136,427	172,130
	192,122	**244,092**
Deposits from Banks	2,896	4,762
Other	65	51
Total	**213,940**	**278,497**

26. INTERESTS AND SIMILAR EXPENSE (continued)

b) Analysis by Recipient

	2016 HRK'000	2015 HRK'000
Corporate	27,393	30,561
Retail	136,427	172,130
Government and Public Sector	14,076	21,366
Banks and Other Financial Institutions	31,805	48,609
Others	4,239	5,831
Total	**213,940**	**278,497**

27. FEES AND COMMISSIONS INCOME

	2016 HRK'000	2015 HRK'000
Cash Payment Operations	280,106	286,552
Non-Cash Payment Operations	48,640	44,291
Retail and Credit Card Operations	127,554	117,299
Letters of Credit, Guarantees and Foreign Exchange Payment Operations	22,149	19,623
Other Fees and Commissions Income	30,485	27,562
Total	**508,934**	**495,327**

28. FEES AND COMMISSIONS EXPENSE

	2016 HRK'000	2015 HRK'000
Cash Payment Operations	248,829	251,790
Non-Cash Payment Operations	14,202	14,676
Card Operations	36,874	28,046
Other Fees and Commissions Expense	10,278	7,831
Total	**310,183**	**302,343**

29. GAINS LESS LOSSES FROM FINANCIAL ASSETS AT FAIR VALUE IN PNL

	2016 HRK'000	2015 HRK'000
Net Unrealized Losses/ (Gains) on Financial Assets at Fair Value in PNL		
Realized Gains/ (Losses)		
- Debt securities	1,277	383
- Investment Funds	1,009	478
- Forward Contracts, OTC	(1,692)	(2,735)
	594	**(1,874)**
Unrealized Gains/ (Losses)		
- Debt Securities	11,881	2,584
- Equity Securities	8,030	360
- Investment Funds	5,446	4,446
- Futures	158	18
- Forward Contracts, OTC	140	508
	25,655	**7,916**
Total	**26,249**	**6,042**

30. GAINS LESS LOSSES FROM FINANCIAL ASSETS AVAILABLE FOR SALE

	2016 HRK'000	2015 HRK'000
Realized Gains on Disposal of Debt securities Available for Sale	15,112	1
Realized Gains on Disposal of Equity Securities Available for Sale	33,484	-
Total	**48,596**	1

31. OTHER OPERATING INCOME

	2016 HRK'000	2015 HRK'000
Dividend Income	827	1,073
Net Foreign Exchange Gain from Translation of Monetary Assets and Liabilities	4,682	9,669
Income on Dormant Customer Accounts	29	32
Income Arising from Sale of Repossessed Assets	254	14,935
Income from Paid Insurance Premium	-	8,000
Other Income	4,290	8,214
Total	**10,082**	**41,923**

32. GENERAL AND ADMINISTRATIVE EXPENSES

	2016 HRK'000	2015 HRK'000
Materials and Services	131,594	140,401
Administration and Marketing	16,483	18,044
Postage and Telecommunications	23,662	26,071
Staff costs	186,059	188,183
Savings Deposit Insurance Costs	34,691	35,194
Other General and Administrative Expenses	17,008	19,631
Total	**409,497**	**427,524**

a) Staff Costs

	2016 HRK'000	2015 HRK'000
Net Salaries, Termination and Other Employee Benefit Costs	97,264	91,366
Taxes and Contributions (Including Contributions Payable by Employers)	75,082	84,185
Other Fees to Employees	9,632	12,038
Provisions for Variable Bonuses to Employees	3,517	-
Fees to Supervisory Board Members	564	594
Total	**186,059**	**188,183**

As at December 31 2016, 1,106 persons were employed in the Group (2015: 1,102 employees).

33. IMPAIRMENT LOSSES ON LOANS TO AND RECEIVABLES FROM CUSTOMERS AND OTHER ASSETS

	Notes	2016 HRK'000	2015 HRK'000
Individually Identified Impairment Losses			
Loans and Receivables from Customers	11	(170,294)	(177,196)
Interests Receivable		(10,272)	(3)
Financial Assets Available for Sale	9	-	(5,060)
Financial Assets Held to Maturity	10	(395)	(276)
Other Assets	17	(1,408)	(3,191)
Tangible and Intangible Assets	13,14,15	(8,306)	(7,437)
Gains from Recovery of Placements Written-Off in Previous Years		403	1,878
Total Charge		**(190,272)**	**(191,285)**
Portfolio Based Provisions for Identified Losses			
Loans and Receivables from Customers	11	(12.505)	9,137
Financial Assets Held to Maturity	10	1.484	(2,509)
Total Reversal		**(11.021)**	**6,628**
Total Portfolio Based and Individually Identified Losses			
Loans and Receivables from Customers	11	(182,799)	(168,059)
Interests Receivable		(10,272)	(3)
Financial Assets Available for Sale	9	-	(5,060)
Financial Assets Held to Maturity	10	1,089	(2,785)
Other Assets	18	(1,408)	(3,191)
Tangible and Intangible Assets	13,14,15	(8,306)	(7,437)
Gains from Recovery of Placements Written-Off in Previous Years		403	1,878
Total Charge		**(201,293)**	**(184,657)**

34. CORPORATE TAX

Total recognized corporate tax expense, calculated at the corporate tax rate of 20%, comprises corporate tax expense recognized in the PNL and movements in deferred tax recognized in equity, as follows:

Income Tax Expense Recognized in the PNL report

	2016 HRK'000	**2015 HRK'000**
Current Tax*	(928)	(289)
Recognized Deferred Tax Assets	35,303	-
Deferred Tax Income/ (Expense) in Respect of Origination and Reversal of Temporary Differences	(8,817)	(3,613)
Total Current Tax Recognized	**25,558**	**(3,902)**

**The Bank's subsidiaries – HPB Invest Ltd and HPB Nekretnine d.o.o. – were liable to corporate income tax subsequent to net profit realized during 2016 and 2015*

Movements in the Income Tax Recognized in Other Comprehensive Income:

	2016 HRK 000	**2015 HRK 000**
Deferred Tax Expense from Unrealized Losses on Available for Sale Assets Not Recognized in the Fair Valuation Reserve	(134)	(2,303)
Corporate Tax Rate Change Effect on Deferred Tax Expense Related to Unrealized Loss from Assets Available for Sale in Fair Value Reserves	2,065	-
Deferred Tax Income from Property Impairments	15	63
Corporate Tax Change Effect on Deferred Tax Expense Related to Revaluation Reserve*	20	
Total Tax Expense Recognized Directly in Equity	**1,966**	**(2,240)**

Reconciliation of Income Tax Expense

The reconciliation between income tax expense and profit before tax is shown as follows:

	2016 HRK 000	**2015 HRK 000**
Profit/ (Loss) Before Taxation	164,945	128,679
Income Tax at the Rate of 20%	(32,989)	(25,736)
Tax Non-Deductible Expenses	(21,276)	(15,407)
Non-Taxable Income	14,751	8,198
Effect of Unrecognized Deferred Tax	32,477	29,043
Effect of Changes in Income Tax Rate on Recognized Deferred Tax Assets*	(2,708)	-
Recognized Deferred Tax Assets	35,303	-
	25,558	**(3,902)**
Effective Income Tax Rate	(15.5%)	3.0%

**Effective from January 1 2017 corporate tax rate was lowered from 20% to 18%. The Bank has recognized tax assets and liabilities based on the newly set corporate tax rate considering it will be applied in future periods.*

34. CORPORATE TAX (continued)

Unrecognized Deferred Tax in Respect of Tax Losses Disposable in Prospective Periods

At December 31 2016 the Group's parent company had HRK196,129K (2015: HRK355,413K) accumulated tax losses available for utilization until December 31 2019. After 2016 pre-tax profit of HRK161,7M, the Group's parent company has recognized deferred tax assets based on the remaining unused tax loss at rate of 18% in accordance with the IFRS 12 Income Taxes, article 34 (Official Gazette 136/ 09) which states "A deferred tax asset shall be recognized for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilized".

In the last 2 years the Group has surpassed a planned operating profit from strategic guidelines and has created a trend of achieving plan. It is probable the Group will make taxable profits in the future and unused tax losses may be used as tax relief. Therefore unused tax losses were recognized as deferred tax assets.

Tax effect of deferred tax assets transferrable to future periods are shown in the table below. Losses are usable in a period of 5 years from the reporting date but the Group plans to use them until 2018.

		Bank
	2016 **HRK'000**	**2015** **HRK'000**
December 31 2017	192,975	34,735
December 31 2018	3,154	2,728
	196,129	**37,463**

35. EARNINGS/ (LOSS) PER SHARE

For the purposes of determining earnings/ losses per share, earnings (losses) represent the Bank's net profit/ (loss) for the year attributable to the 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. The weighted average number of ordinary shares used in determining the basic earnings/ (losses) per shares was 2,023,830 (2015: 1,450,900). As there is no impact of any options, convertible bonds or similar effects, the weighted average number of ordinary shares used in determining diluted earnings/ (losses) per share would be equal as the one used in determining basic earnings/ (losses) per share i.e. 2,023,830 (2015: 1,450,900).

a) Basic Earnings Per Share

Profit and weighted average number of ordinary shares outstanding:

	2016 **HRK 000**	**2015** **HRK 000**
Current Year Profit/ (Loss) Distributable to the Bank's Owners	190,503	123,217
Profit Used to Calculate Basic Earnings Per Share	190,503	**123,217**
Weighted Average Ordinary Shares Outstanding Used to Calculate Basic Earnings Per Share	2,023,830	1,450,900
Basic Earnings Per Share from Active Operations	**HRK 94.13**	**HRK 84.92**

35. EARNINGS/ (LOSS) PER SHARE (Continued)

b) Diluted Earnings Per Share

Profit used to calculate diluted Earnings Per Share

	2016 HRK 000	2015 HRK 000
Profit Used to Calculate Earnings Per Share	190,503	124,777
Adjustments	-	-
Profit/ (Loss) Used to Calculate Diluted Earnings Per Share	**190,503**	**124,777**

Adjustments of weighted average ordinary shares outstanding used to calculate diluted earnings per share compared to weighted average ordinary shares outstanding used to calculate earnings per share:

	2016	2015
Weighted Average Ordinary Shares Outstanding Used to Calculate Earnings Per Share	2,023,830	1,450,900
Shares Issued Without Cost:		
- Options for Employees	-	-
- Partially Payed Ordinary Shares	-	-
- Convertible Bonds	-	-
- Other	-	-
Weighted Average Ordinary Shares Outstanding Used to Calculate Diluted Earnings Per Share	**2,023,830**	**1,450,900**
Diluted Earnings Per Share	**HRK 94.13**	**HRK 84,92**

36. CONCENTRATION OF ASSETS AND LIABILITIES

The assets and liabilities of the Group are significantly concentrated on amounts directly due from and to the Republic of Croatia. The amounts at year end, including accrued interests, are as follows:

	Notes	2016 HRK'000	2015 HRK'000
Giro Account with the CNB	5	502,603	488,042
Mandatory Reserve with the Croatian National Bank	6	1,300,796	1,279,570
Bonds of the Republic of Croatia		2,169,263	1,915,457
Treasury Bills of the Croatian Ministry of Finance		1,001,586	978,638
Loans and Advances to the Republic of Croatia		3,282,435	2,545,676
Deposits from the Republic of Croatia		(1,897,921)	(2,380,346)
Total		**6,358,762**	**4,827,037**

The Group's exposure towards local government and state institutions not directly funded by the State Budget (excluding state owned companies) is presented below:

	2016 HRK'000	2015 HRK'000
Loans	759,509	942,304
Deposits	(513,578)	(162,705)
Total	**245,931**	**779,599**

37. CASH AND CASH EQUIVALENTS

	Notes	2016 HRK'000	2015 HRK'000
Cash and Amounts Due from Banks	5	1,554,612	1,630,115
Mandatory Reserve with Croatian National Bank	6	1,300,796	1,279,570
Deposits with Banks with Original Maturities up to 90 Days		148,462	215,036
Items in Course of Collection	17	220,731	122,393
Total		**3,224,601**	**3,247,114**

38. CONTINGENT LIABILITIES

	2016 HRK'000	2015 HRK'000
Guarantees Denominated in HRK	321,418	304,855
Guarantees Denominated in Foreign Currency	389,428	217,772
Letters of Credit	17,268	39,553
Undrawn Lending Commitments	1,636,818	1,334,010
Total	**2,364,932**	**1,896,190**

At December 31 2016, the Group recognized portfolio based provisions for off-balance sheet items arising from the issue of guarantees, letters of credit and undrawn lending commitments in the amount of HRK22,019K (2015: HRK19,431K), which is included in Provisions for liabilities and expenses (see Note 22).

39. DERIVATIVE INSTRUMENTS AND DEALINGS IN FOREIGN CURRENCIES

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

	Notional Amount, Remaining Life					Fair Value	
2016	**Up to 3 Months HRK'000**	**3 to 12 Months HRK'000**	**1 to 5 Years HRK'000**	**Over 5 Years HRK'000**	**Total HRK'000**	**Assets HRK'000**	**Liabilities HRK'000**
Forward Foreign Exchange contracts - OTC	(95,788)	-	-	-	(95,788)	3,780	3,641
Cross Currency Swap contracts - OTC	-	-	-	-	-	-	-
Futures	-	-	-	-	-	-	-
	(95,788)	**-**	**-**	**-**	**(95,788)**	**3,780**	**3,641**

	Notional Amount, Remaining Life					Fair Value	
2015	**Up to 3 Months HRK'000**	**3 to 12 Months HRK'000**	**1 to 5 Years HRK'000**	**Over 5 Years HRK'000**	**Total HRK'000**	**Assets HRK'000**	**Liabilities HRK'000**
Forward Foreign Exchange Contracts - OTC	-	-	-	-	-	-	-
Cross Currency Swap Contracts - OTC	-	-	-	-	-	-	-
Futures	-	-	-	-	-	-	-
	-	-	-	-	-	-	-

40. RELATED PARTY TRANSACTIONS

The Bank is the parent of the Hrvatska Poštanska Banka Group.

Key shareholders of the Group are the Republic of Croatia as the largest shareholder with an ownership stake of 42.43 percent, and Hrvatska Pošta d.d. ("HP") with a stake of 11.93 percent.

Other significant state-owned shareholders include: State Agency for Deposits Insurance and Bank Resolution, the Croatian Pension Insurance Institute ("HZMO") and Fund for financing the decommissioning of the Krško Nuclear Power Plant and the disposal of NEK radioactive waste and spent nuclear fuel ("NEK fund"). These shareholders together own 74.46% of the Bank's shares. The remaining 25.54% (2015: 25.54%) are publicly traded.

a) Key transactions with related parties

Hrvatska Pošta d.d. ("HP") performs domestic payment transactions for and on behalf of the Group's parent company. Exposure to Hrvatska Pošta d.d. mainly comprises fees receivable based on domestic payment transactions performed for and on behalf of the parent company, as well as placements in debt securities issued by Hrvatska Pošta d.d. Liabilities towards Hrvatska Pošta d.d. mainly relate to demand and term deposits. Income and expenses mostly relate to commissions for services provided.

Exposure to the state is shown in Note 36, *Concentration of assets and liabilities*.

The exposure to members of HPB Group mainly consists of investment into share capital. The Group's parent company performs payments on behalf of its subsidiaries and, accordingly, recognizes income. Expenses payable to HPB Nekretnine relate to the services performed by the subsidiary in respect of estimation of collateral.

Key management personnel held no ordinary shares at the year-end (2015: -).

40. RELATED-PARTY TRANSACTIONS (continued)

b) Amounts arising from transactions with related parties

Assets and liabilities and off-balance sheet exposure and income and expense as at and for the years ended December 31 2016 and December 31 2015 of the Group, arising from transactions with related parties were as follows:

Group 2016	**Exposure* HRK'000**	**Liabilities HRK'000**	**Income HRK'000**	**Expenses HRK'000**
Key Shareholders				
Republic of Croatia	-	-	-	-
Hrvatska Pošta d.d.	77,621	252,494	298,257	288,161
Assets Available for Sale				
H1 TELEKOM	-	-	2,275	3,406
Key Management Personnel				
Short-Term Benefits (Bonuses, Salaries and Fees)	1,214	3,395	33	18,983
Long-Term Benefits (Loans and Deposits)	14,255	233	589	1
Companies under Significant Influence	**54,703**	**3,879**	**1,577**	**12**
Total	**147,793**	**260,001**	**302,731**	**310,563**

Group 2015	**Exposure* HRK'000**	**Liabilities HRK'000**	**Income HRK'000**	**Expenses HRK'000**
Key Shareholders				
Republic of Croatia	-	-	-	-
Hrvatska Pošta d.d.	98,385	119,204	301,184	292,849
Assets Available for Sale				
H1 TELEKOM	-	-	2,229	3,518
Key Management Personnel				
Short-Term Benefits (Nonuses, Salaries and Fees)	1,212	6,740	34	18,988
Long-Term Benefits (Loans and Deposits)	16,722	453	646	3
Companies under Significant Influence	**54,703**	**3,879**	**2,473**	**24**
Total	**171,022**	**130,276**	**306,566**	**315,382**

*****Exposure comprises amounts advanced in cash or kind, commitments and contingencies, interests and other receivables, and includes HRK13,361K (2015: HRK20,980K) of off-balance sheet exposure.

Exposure to key members of the Group's Management include loans receivables in the amount of HRK15,469K (HRK17,934K).

Expenses do not include impairments nor provisions for losses.

40. RELATED-PARTY TRANSACTIONS (continued)

c) State owned companies

Major shareholders of the parent company, which together own 74.46% of its shares, are state agencies or state owned companies, all mainly funded from the State Budget. Accordingly, transactions and balances with other state owned companies, including credit risk exposures guaranteed by the state, also represent related party relationships. The parent company has a significant exposure to these parties, which is disclosed in Note 36.

41. REPURCHASE AND RESALE 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 derecognized and the proceeds are accounted for as interest-bearing borrowings. At the end of the year assets sold under repurchase agreements were as follows:

	Fair Value of Securities HRK'000	Carrying Amount of Corresponding Liabilities HRK'000	Repurchase Date	Repurchase Price HRK'000
Debt Securities at Fair Value in PNL - Repurchase Agreements				
2016	-	-	-	-
2015	395	380	August 2016	379

Related transactions, according to IAS 39 *Financial instruments Recognition and Measurement* are recognized as repurchase agreements.

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 repurchase agreements 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 recognized.

Loans to Customers – Reverse Repo Agreements	Fair Value of Receivables HRK'000	Carrying Amount of Collaterals HRK'000	Repurchase Date	Repurchase Price HRK'000
2016	81,630	68,760	January 2016	71,666
2015	71,182	67,228	January 2016	71,206

42. FUNDS MANAGED FOR AND ON BEHALF OF CORPORATE AND RETAIL CUSTOMERS

The parent company provides trust and custody services to companies, individuals, and investment funds (the Group's investment funds) whereby it holds and manages assets or invests funds received in various financial instruments at the direction of the customer. The parent company receives fee income for providing these services. Trust assets are not assets of the parent company and are not recognized in the Bank's report of financial position. The parent company is not exposed to any credit risk relating to such placements, nor does it guarantee for investments.

At December 31 2016, the total assets under custody held by the parent company on behalf of customers, including the funds within the HPB Group, amounted to HRK4.95B (2015: HRK4.16B).

In addition, at December 31 2016, total assets of investment and pension funds to which the parent company acts as a depository bank, amounted to HRK4.73B (2015: HRK3.95B).

Furthermore, the parent company manages loan exposures of other parties as follows:

	2016 HRK'000	2015 HRK'000
Assets		
Corporate	59,521	65,653
Retail	545,389	569,376
Giro Accounts	403,046	346,909
Total assets	**1,007,956**	**981,938**
Liabilities		
Croatian Employment Office	70,245	71,910
Counties	11,386	15,129
Government of the Republic of Croatia	919,797	889,501
CBRD	3,846	3,787
Other Liabilities	2,681	1,610
Total Liabilities	**1,007,956**	**981,938**

43. AVERAGE INTEREST RATES

Average interest rates calculated as the weighted average of each category of interest-earning asset and interest-bearing liability, are presented below:

Assets	**Average Interest Rates 2016**	**Average Interest Rates 2015**
Cash and Amounts Due from Banks	0.02%	0.01%
Loans to and Receivables from Banks	0.29%	0.76%
Financial Assets at Fair Value in PNL	2.99%	3.79%
Financial Assets Available for Sale	3.35%	4.12%
Financial Assets Held to Maturity	2.63%	3.66%
Loans and Receivables from Customers	5.48%	6.25%
Liabilities		
Deposits from Banks	1.62%	1.31%
Customer Deposits	1.26%	1.72%
Borrowings	2.18%	2.36%

44. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is the amount for which an asset could be exchanged, or a liability settled, in an arm's-length transaction.

Financial instruments at fair value in PNL or available for sale financial assets are measured at fair value. Loans and receivables, and held to maturity investments are measured at amortized cost less impairments. Financial assets at fair value in PNL and financial assets available for sale are disclosed at their fair value that arises from price quotes of these instruments on active markets. Financial liabilities at fair value in PNL are disclosed at fair values calculated on the basis of available conditions of these instruments.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the Group takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date. Fair value for measurement and/ or disclosure purposes in these consolidated financial reports is determined on such a basis, except for share-based payment transactions that are within the scope of IFRS 2, leasing transactions that are within the scope of IAS 17, and measurements that have some similarities to fair value but are not fair value, such as net realizable value in IAS 2 or value in use in IAS 36.

In addition, for financial reporting purposes, fair value measurements are categorized into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

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

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

Loans

The fair value of loans and advances is calculated based on discounted expected future cash flows. Loan repayments are assumed to occur at contractual repayment dates, where applicable. Expected future cash flows are estimated considering credit risk and any indication of impairment including portfolio based provisions for performing (i.e. A-risk rated) loans calculated at rates prescribed by the CNB. 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. The Group has a limited portfolio of loans with fixed rates, where there is a difference between the fair value and the carrying amount.

44. FAIR VALUE OF FINANCIAL INSTRUMENTS

Investments Carried at Cost

For equity investments for which a quoted market price is not available, fair value is, where possible, estimated using discounted cash flow techniques. Estimated future cash flows are based on management's best estimates and the discount rate is a market related rate for a similar instrument at the reporting date. Where discounted cash flow techniques provide insufficiently reliable valuations due to a number of uncertainties related to estimations of future cash flows, investments are carried at cost less impairment.

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 the reporting date. 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 the reporting date to the Group for new debt of similar type and remaining maturity.

The following table represents the Group's estimate of the fair value hierarchy of financial instruments as of December 31 2016 and December 31 2015:

44. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

2016 (HRK'000)	Fair Value	Fair Value Level	Valuation Technique(s) and Key input(s)	Book Value	Unrecognized Gains/ (Losses)
Financial Assets					
Cash and Receivables from Banks	**1,554,612**	**Level 1**	**Cash and Cash Equivalents**	**1,554,612**	**-**
Mandatory Reserve with the Croatian National Bank	**1,300,796**	**Level 1**	**Cash Equivalent**	**1,300,796**	**-**
Loans to and Receivables from Banks	**182,073**	**Level 3**	**Cash Equivalent Other than Assets with a Defined Maturity > 30 days at a Fixed Rate, Where the Fair Value is the Present Value of Discounted Cash Flows**	**182,087**	**(14)**
Financial Assets at Fair Value in PNL	**1,019,441**			**1,019,441**	**-**
- Ministry of Finance Treasury Bills	315,565	Level 3	Ministry of Finance Treasury Bills	315,565	-
- Ministry of Finance Bonds	466,838	Level 1	*Mark-to-Market* According to the Prices Quoted in an Active Market	466,838	-
- Open-End Investment Fund Investments	187,801	Level 1	*Value of an Individual Share on Given Date*	187,801	-
- Equity Securities	39,393	Level 1	*Mark-to-Market* According to the Prices Quoted in an Active Market	39,393	-
- Fair Value of Forwards	3,780	Level 3	Internal Valuation Model for FX Contracts Using Future Cash Flows	3,780	-
- Interest Receivables	6,064	Not Applicable	Not Applicable	6,064	-
Financial Assets Available for Sale	**2,753,938**			**2,753,938**	**-**
- Ministry of Finance Treasury Bills	686,021	Level 3	*Mark-to-Model* Using Internal Model for Determining the Present Values of Future Cash Flows	686,021	-
- Ministry of Finance Bonds	1,502,626	Level 1	*Mark-to-Market* According to the Prices Quoted in an Active Market	1,502,626	-
-Foregin Country Securities	394,206	Level 1	*Mark-to-Model* Using Internal Model for Determining the Present Values of Future Cash Flows	394,206	-
- Corporate Bonds of State-Run Companies	127,957	Level 1	*Mark-to-Market* According to the Prices Quoted in an Active Market	127,957	-
- Corporate Bonds of State-Other Companies	-	Level 3	*Mark-to-Model* Using Internal Model for Determining the Present Values of Future Cash Flows	-	-
- Equity Securities – Not Listed	15,414	Level 3	Method of Comparable Companies, Using the Average of Standard Multiples EV/ EBITDA, P/ E, P/ S, P/ B.	15,414	-
- Equity Securities - Listed	4,322	Level 1	*Mark-to-Market* According to the Prices Quoted in an Active Market	4,322	-
- Interest Receivables	23,392	Not Applicable	Not Applicable	23,392	-
Financial Assets Held to Maturity	**440,541**	**Level 3**	**Present Value of Future Discounted Cash Flows**	**444,825**	**(4,284)**
Loans and Receivables from Customers	**11,461,875**	**Level 3**	**Present Value of Future Discounted Cash Flows**	**11,554,215**	**(92,340)**
Total Financial Assets	**18,713,275**			**18,809,914**	**(96,639)**
FINANCIAL LIABILITIES					
Financial Assets at Fair Value in PNL	**3,641**	**Level 3**	Internal Valuation Model for FX Contracts Using Future Cash Flows	**3,641**	**-**
Deposits from Banks	**507,514**	**Level 3**	**Present Value of Discounted Cash Flows under the Currently Effective Interest Rates**	**509,133**	**1,619**
Customer Deposits	**15,959,853**	**Level 3**	**Present Value of Discounted Cash Flows under the Currently Effective Interest Rates**	**16,024,804**	**64,951**
Borrowings	**724,933**	**Level 3**	**Present Value of Discounted Cash Flows under the Currently Effective Interest Rates**	**726,660**	**1,727**
Total Financial Liabilities	**17,195,940**			**17,264,238**	**68,298**
TOTAL					**(28,341)**

44. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

2015 (HRK'000)	Fair Value	Fair Value Level	Valuation Technique(s) and Key input(s)	Book Value	Unrecognized Gains/ (Losses)
Financial Assets					
Cash and Receivables from Banks	**1,630,115**	**Level 1**	**Cash and Cash Equivalents**	**1,630,115**	**-**
Mandatory Reserve with the Croatian National Bank	**1,279,570**	**Level 1**	**Cash Equivalent**	**1,279,570**	**-**
Loans to and Receivables from Banks	**262,301**	**Level 3**	**Cash Equivalent Other than Assets with a Defined Maturity > 30 days at a Fixed Rate, Where the Fair Value is the Present Value of Discounted Cash Flows**	**261,913**	**388**
Financial Assets at Fair Value in PNL	**1,019,694**			**1,019,694**	**-**
- Ministry of Finance Treasury Bills	303,113	Level 3	*Mark-to-Model* Using Internal Model for Determining the Present Values of Future Cash Flows	303,113	
- Ministry of Finance Bonds	208,800	Level 1	*Mark-to-Market* According to the Prices Quoted in an Active Market	208,800	-
- Open-End Investment Fund Investments	470,555	Level 1	*Value of an Individual Share on Given Date*	470,555	-
- Equity Securities	33,947	Level 1	*Mark-to-Market* According to the Prices Quoted in an Active Market	33,947	-
- Fair Value of Forwards	-	Level 3	Internal Valuation Model for FX Contracts Using Future Cash Flows	-	-
- Interest Receivables	3,279	Not Applicable	Not Applicable	3,279	-
Financial Assets Available for Sale	**2,221,310**			**2,221,310**	**-**
- Ministry of Finance Treasury Bills	675,525	Level 3	*Mark-to-Model* Using Internal Model for Determining the Present Values of Future Cash Flows	675,525	-
- Ministry of Finance Bonds	1,396,368	Level 1	*Mark-to-Market* According to the Prices Quoted in an Active Market	1,396,368	-
- Corporate Bonds of State-Run Companies	79,742	Level 1	*Mark-to-Market* According to the Prices Quoted in an Active Market	79,742	-
- Equity Securities – Not Listed	35,592	Level 3	*Mark-to-Model* Using Internal Model for Determining the Present Values of Future Cash Flows	35,592	-
- Equity Securities - Listed	6,654	Level 1	*Mark-to-Market* According to the Prices Quoted in an Active Market	6,654	-
- Interest Receivables	27,429	Not Applicable	Not Applicable	27,429	-
Financial Assets Held to Maturity	**553,140**	**Level 3**	**Present Value of Future Discounted Cash Flows**	**571,764**	**(18,624)**
Loans and Receivables from Customers	**10,244,797**	**Level 3**	**Present Value of Future Discounted Cash Flows**	**10,298,014**	**(53,217)**
Total Financial Assets	**17,210,928**			**17,282,380**	**(71,453)**
FINANCIAL LIABILITIES					
Deposits from Banks	**356,892**	**Level 3**	**Present Value of Discounted Cash Flows under the Currently Effective Interest Rates**	**357,639**	**747**
Customer Deposits	**14,412,274**	**Level 3**	**Present Value of Discounted Cash Flows under the Currently Effective Interest Rates**	**14,493,594**	**81,320**
Borrowings	**1,002,105**	**Level 3**	**Present Value of Discounted Cash Flows under the Currently Effective Interest Rates**	**1,005,383**	**3,278**
Total Financial Liabilities	**15,771,271**			**15,856,616**	**85,345**
TOTAL					**13,893**

45. ENCUMBERED ASSETS OF THE CREDIT INSTITION

The CI Group* considers the following types of assets under the term encumbered assets: pledged assets, assets given as a collateral, assets subject to some form of securitization or assets used for credit enhancement of financial position which can not be freely exited. Furthermore, assets that are placed at facilities and that can not be freely withdrawn are also considered encumbered.

Within the assets' structure, the CI Group has encumbered assets amounting to HRK2,808,262K (2015: HRK3,047,392K).

Book value of encumbered assets represents 14.31% of the Group's total assets.

Calculated mandatory reserve with the Croatian National Bank is also included in encumbered assets, as well as balances on nostro accounts on which mandatory reserve is maintained, totaling HRK2,042,133K (2015: HRK1,853,243K).

Remainder of encumbered assets relates to loans that are given out as collateral for a foreign borrowing, and to securities given out as collateral for deposits received from customers.

*The CI Group relates to group of credit institutions, and includes the Bank and HPB Stambena Štedionica, for whom reporting on encumbered assets is a regulatory obligation.

	2016		2015	
CI Group (HRK'000)	**Book Value**	**Fair Value**	**Book Value**	**Fair Value**
Equity Instruments	-	-	-	-
Securities	110,160	110,160	135,411	135,411
Mandatory Reserve and Balances on Nostro Accounts on which Mandatory Reserve is Maintained	2,042,133	2,042,133	1,853,243	1,853,243
Loans to Customers and Other Assets	655,969	655,969	1,058,738	1,058,738
Total	**2,808,262**	**2,808,262**	**3,047,392**	**3,047,392**

46. EVENTS AFTER DATE OF REPORT OF FINANCIAL POSITION

In 2017 before the approval of the financial reports a number of events had occurred which had a negative impact on the ability of servicing debt for certain group of debtors. The group of debtors makes a substantial individual exposure for the Group. In 2017 the Group made regular assessments of the mentioned placements, and based on future cash flows estimates and occurred events determined the future cash flows will not be sufficient for servicing the placements in full. Therefore the Group made impairments of the placements on March 31 2017.

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Hrvatska Poštanska Banka p.l.c.

HEADQUARTERS	
Address:	Jurišićeva 4 10 000 Zagreb
tel.:	072 472 472 0800 472 472 01 4890 365
fax:	01 4810 773
e-mail:	hpb@hpb.hr
SWIFT:	HPBZHR2X
web site:	www.hpb.hr
OFFICE ZAGREB - JURIŠIĆEVA	
Address:	Jurišićeva 4 10 000 Zagreb
tel.:	01 4804 615 / 551
fax:	01 4804 522
OFFICE ZAGREB - BRITANSKI TRG	
Address:	Ilica 81 10 000 Zagreb
tel.:	01 4686 001
fax:	01 4686 009
OFFICE ZAGREB - DUBRAVA	
Address:	Avenija Dubrava 47 10 040 Zagreb
tel.:	01 2908 971
fax:	01 2908 978
OFFICE VMD	
Address:	Strojarska cesta 16 10 000 Zagreb
tel.:	01 6323 550
fax:	01 6323 569
BRANCH GAJNICE	
Address:	Huzjanova 2 10 000 Zagreb
tel.:	01 3466 930
fax:	01 3466 947
OFFICE ZAGREB - SESVETE	
Address:	Trg D. Domjanića 8 10 360 Zagreb
tel.:	01 2019 270
fax:	01 2019 287

OFFICE ZAGREB - MAKSIMIRSKA

Address:	Maksimirska 105
tel.:	01 2383 782
fax:	01 2383 789

OFFICE ZAGREB - SAVSKA

Address:	Savska 58
tel.:	01 5553 501
fax:	01 5553 506

OFFICE ZAGREB - ŠPANSKO

Address:	Trg Ivana Kukuljevića 5 10 000 Zagreb
tel.:	01 5551 958 / 962
fax:	01 5551 967

OFFICE ZAPREŠIĆ

Address:	Drage Švajcara 5 10 290 Zaprešić
tel.:	01 3340 271
fax:	01 3340 287

OFFICE VELIKA GORICA

Address:	Trg kralja Petra Krešimira IV br. 1 10 410 Velika Gorica
tel.:	01 6238 600
fax:	01 6238 614

OFFICE STRMEC, Hoto Center

Address:	Ulica dr. Franje Tuđmana 4 10 434 Strmec
tel.:	01 3369 650
fax:	01 3369 660

OFFICE SISAK

Address:	Stjepana i Antuna Radića 34 44 000 Sisak
tel.:	044 556 012
fax:	044 556 019

OFFICE SREDIŠĆE

Address:	Ivana Šibla 15 10 000 Zagreb
tel.:	01 5550 971
fax:	01 5550 979

OFFICE KARLOVAC

Address:	Ivana Gorana Kovačića 4 47 000 Karlovac
tel.:	047 555 040
fax:	047 555 049

OFFICE VARAŽDIN

Address:	Ivana Kukuljevića 9a 42 000 Varaždin
tel.:	042 215 320
fax:	042 215 330

OFFICE ČAKOVEC

Address:	Masarykova 28 40 000 Čakovec
tel.:	040 555 010
fax:	040 555 019

OFFICE GOSPIĆ

Address:	Trg S. Radića bb 53 000 Gospić
tel.:	053 617 101
fax:	053 617 109

OFFICE BJELOVAR

Address:	Vladimira Nazora 1a 43 000 Bjelovar
tel.:	043 555 095
fax:	043 555 099

OFFICE KOPRIVNICA

Address:	Florijanski trg 13 48 000 Koprivnica
tel.:	048 555 092
fax:	048 555 099

OFFICE SLAVONSKI BROD

Address:	Kralja Petra Krešimira IV br.3 35 000 Slavonski Brod
tel.:	035 212 530
fax:	035 212 539

OFFICE POŽEGA

Address:	Cehovska 8 34 000 Požega
tel.:	034 410 130 / 133
fax:	034 410 139

OFFICE VIROVITICA

Address:	Trg kralja Zvonimira 3 33 000 Virovitica
tel.:	033 740 060
fax:	033 740 068

OFFICE VINKOVCI

Address:	Trg dr. Franje Tuđmana 2 32 100 Vinkovci
tel.:	032 455 502
fax:	032 455 508

OFFICE VUKOVAR

Address:	J.J. Strossmayerova 16 32 000 Vukovar
tel.:	032 451 012
fax:	032 451 019

OFFICE OSIJEK

Address:	Trg Ante Starčevića 7 31 000 Osijek
tel.:	031 284 887
fax:	031 284 888

OFFICE VALPOVO

Address:	Trg kralja Tomislava 17 31 550 Valpovo
tel.:	031 654 041
fax:	031 654 042

BRANCH DONJI MIHOLJAC

Address:	Vukovarska 4 31 540 Donji Miholjac
tel.:	031 620 040
fax:	031 620 041

OFFICE ĐAKOVO

Address:	Bana J.Jelačića 8 31 400 Đakovo
tel.:	031 815 156
fax:	031 815 158

BRANCH NAŠICE

Address:	J.J.Strossmayera 2 31 500 Našice
tel.:	031 615 162
fax:	031 615 173

OFFICE OSIJEK 2

Address:	Prolaz J. Benešića 2 31 000 Osijek
tel.:	031 555 262
fax:	031 555 269

BRANCH BELI MANASTIR

Address:	Imre Nagya 2E 31 300 Beli Manastir
tel.:	031 701 412
fax:	031 701 414

OFFICE PULA

Address:	Anticova 9 52 100 Pula
tel.:	052 300 602
fax:	052 300 609

BRANCH BANJOLE

Address:	Banjole Kamnik 24 52 100 Pula
tel.:	052 573 409
fax:	052 573 378

OFFICE POREČ

Address:	Trg slobode 14 52 440 Poreč
tel.:	052 703 222
fax:	052 703 229

OFFICE RIJEKA

Address:	Korzo 13 51 000 Rijeka
tel.:	051 301 280
fax:	051 301 288

OFFICE RIJEKA - ULJARSKA

Address:	Uljarska 4 A 51 000 Rijeka
tel.:	051 555 570 / 571
fax:	051 555 589

OFFICE ZADAR

Address:	Zrinsko - Frankopanska 8 23 000 Zadar
tel.:	023 350 000
fax:	023 350 018

OFFICE ŠIBENIK

Address:	Fra Jerolima Milete 6 22 000 Šibenik
tel.:	022 556 012
fax:	022 556 019

OFFICE KNIN

Address:	Kralja Zvonimira 9 22 300 Knin
tel.:	022 556 000
fax:	022 556 009

OFFICE SPLIT - BIHAĆKA

Address:	Bihaćka 2 21 000 Split
tel.:	021 340 626
fax:	021 340 629

OFFICE SPLIT - DUBROVAČKA

Address:	Dubrovačka 31 21 000 Split
tel.:	021 401 620
fax:	021 401 639

OFFICE SPLIT – III

Address:	Ruđera Boškovića 18a 21 000 Split
tel.:	021 555 854
fax:	021 555 873

OFFICE KAŠTEL STARI

Address:	Ivana Danila 12 21 216 Kaštel Stari
tel.:	021 246 184
fax:	021 246 199

OFFICE TROGIR

Address:	Kardinala Alojzija Stepinca 42 21 220 Trogir
tel.:	021 555 728
fax:	021 555 743

OFFICE SINJ

Address:	Trg kralja Tomislava 1 21 230 Sinj
tel.:	021 708 080
fax:	021 708 097

BRANCH TRILJ

Address:	Bana Josipa Jelačića 8 21 240 Trilj
tel.:	021 830 410
fax:	021 830 427

OFFICE IMOTSKI

Address:	Šetalište S. Radića 19 21 260 Imotski
tel.:	021 555 280
fax:	021 555 289

OFFICE MAKARSKA

Address:	Trg 4. svibnja 533 br.1 21 300 Makarska
tel.:	021 695 760
fax:	021 695 768

OFFICE DUBROVNIK

Address:	Dr. Ante Starčevića 24 20 000 Dubrovnik
tel.:	020 362 045
fax:	020 362 048

OFFICE KONAVLE

Address:	Gruda 43 20 215 Gruda
tel.:	020 450 800
fax:	020 450 802

BRANCH CAVTAT

Address:	Trumbićeva 10 20 210 Cavtat
tel.:	020 450 810
fax:	020 450 811

Members of the HPB Group:

HPB Invest Ltd

Address:	Strojarska cesta 20 10 000 Zagreb
tel.:	0800 472 472
fax:	01 4804 599
e-mail:	hpb.invest@hpb-invest.hr
web site:	www.hpb-invest.hr

HPB STAMBENA ŠTEDIONICA d.d.

Address:	Savska 58 10 000 Zagreb
tel.:	0800 232 332
fax:	01 5553 905
e-mail:	hpb.stedionica@hpb-stedionica.hr
web site:	www.hpb-stedionica.hr

HPB NEKRETNINE d.o.o.

Address:	Amruševa 8 10 000 Zagreb
tel.:	01 5553 920
fax:	01 4839 235
e-mail:	hpb.nekretnine@hpb.hr
web site:	www.hpb-nekretnine.hr