

ERSTE BANK A.D. NOVI SAD

**CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2017
AND INDEPENDENT AUDITOR'S REPORT**

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INDEPENDENT AUDITOR'S REPORT

To the shareholders of Erste Bank a.d. Novi Sad

We have audited the accompanying consolidated financial statements of Erste Bank a.d. Novi Sad (the "Bank") and its subsidiary (the "Group") which comprise the consolidated balance sheet as of 31 December 2017 and the consolidated income statement, consolidated statement of other comprehensive income, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with Law on Auditing and auditing regulation effective in the Republic of Serbia. This regulation requires that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

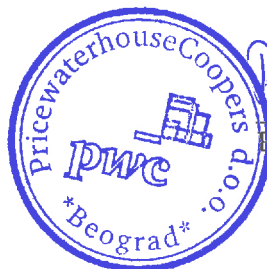
Opinion

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2017, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Saša Todorović

Saša Todorović
Licensed Auditor

Belgrade, 13 March 2018



PricewaterhouseCoopers d.o.o. Beograd

PricewaterhouseCoopers d.o.o. Beograd

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

CONSOLIDATED INCOME STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2017

POSITION	Note	<i>(in RSD thousand)</i>	
		2017	2016
Interest income	4	7,740,108	7,239,279
Interest expense	4	(1,386,166)	(1,317,933)
Net interest income		6,353,942	5,921,346
Fees and commission income	5	2,294,654	2,187,934
Fees and commission expense	5	(787,891)	(703,912)
Net fee and commission income		1,506,763	1,484,022
Net income from financial assets held for trading	6	281,304	198,957
Net gains from hedging	7	2,067	1,238
Net income from foreign currency exchange difference and effects of contractual foreign currency clause	8	213,998	204,495
Other operating income	9	254,083	272,254
Net income from impairment of financial assets and credit risk-weighted off-balance sheet items	10	41,310	-
Net expense from impairment of financial assets and credit-weighted risk off-balance sheet items	10	-	(605,711)
TOTAL NET OPERATING INCOME		8,653,467	7,476,601
Costs of salaries, contributions and other personnel expenses	11	(2,006,206)	(1,870,076)
Depreciation costs	12	(293,554)	(266,926)
Other expenses	13	(3,472,391)	(3,129,899)
PROFIT BEFORE TAX		2,881,316	2,209,700
Income tax	14	(166,319)	(11,739)
Deferred tax expense	14	(42,976)	(88,346)
PROFIT FOR THE YEAR	30	2,672,021	2,109,615
Profit attributable to the parent entity		2,622,076	2,098,441
Profit attributable to non-controlling interests		9,945	11,174

The accompanying notes are an integral part of these financial statements.

Novi Sad, 28 February 2018



Stevan Čomić
Director of Accounting and
Controlling Sector



Aleksandra Radić
Member of the Executive
Board



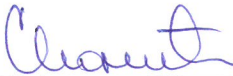
Slavko Carić
President of the Executive Board

CONSOLIDATED STATEMENT OF OTHER COMPREHENSIVE INCOME FOR THE YEAR ENDED DECEMBER
31, 2017

POSITION	<i>(in RSD thousand)</i>		
	Note	2017	2016
PROFIT FOR THE YEAR	29	<u>2,672,021</u>	<u>2,109,615</u>
Components of other comprehensive income that cannot be reclassified to profit or loss:			
Actuarial gains/(losses)		11,360	(2,282)
Other		(246)	-
Components of other comprehensive income that can be reclassified to profit or loss:			
Positive effects of changes in fair value of financial assets available for sale		152,793	78,298
Unrealized losses on securities available for sale		(9,527)	(474)
Loss from taxes related to other comprehensive income		(19,984)	(11,673)
Total other comprehensive income		<u>134,396</u>	<u>63,869</u>
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		<u>2,806,417</u>	<u>2,173,484</u>
Total comprehensive income attributable to the parent entity		<u>2,796,452</u>	<u>2,162,122</u>
Total comprehensive income attributable to non-controlling interests		<u>9,965</u>	<u>11,201</u>

The accompanying notes are an integral part of these financial statements.

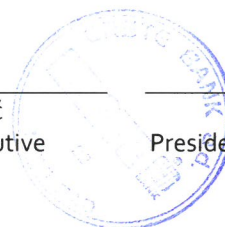
Novi Sad, 28 February 2018

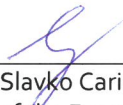


Stevan Čomić
Director of Accounting and
Controlling Sector



Aleksandra Radić
Member of the Executive
Board





Slavko Carić
President of the Executive Board

CONSOLIDATED BALANCE SHEET AS AT 31 DECEMBER 2017

ASSETS*(in RSD thousand)*

	Note	31.12.2017	31.12.2016	1.1.2016.
			<i>restated</i>	<i>restated</i>
Cash and cash funds held with the central bank	15	20,774,027	19,246,670	18,523,428
Financial assets at fair value through profit and loss, held for trading	16	11,539,464	13,048,357	8,363,472
Financial assets available for sale	17	12,488,593	7,182,702	3,446,272
Financial assets held to maturity	18	8,284,452	8,635,103	7,008,412
Loans and receivables due from banks and other financial institutions	19	2,198,970	1,210,065	2,733,309
Loans and receivables due from customers	20	110,472,729	96,462,922	79,043,876
Investments in subsidiaries		118	118	118
Intangible assets	21	255,553	281,395	351,826
Property, plant and equipment	21	1,078,617	817,267	741,139
Investment property	21	-	232,417	238,508
Current tax assets		3,386	6,513	17,163
Deferred tax assets	14	2,261	61,745	161,764
Non-current assets held for sale and assets from discontinued operations		12,288	56,695	443
Other assets	22	1,154,111	864,863	658,957
TOTAL ASSETS		168,264,569	148,106,832	121,288,687
LIABILITIES AND EQUITY				
LIABILITIES				
Financial liabilities carried at fair value through profit and loss, held for trading	23	44,458	54,69	94,235
Deposits and other liabilities due to banks, other financial institutions and the central bank	24	51,859,707	51,428,201	42,677,959
Deposits and other liabilities due to customers	25	91,982,128	75,290,829	59,618,511
Subordinated liabilities	26	1,354,523	1,764,606	1,824,946
Provisions	27	766,609	690,714	551,405
Current tax liabilities	14	160,965	1,09	-
Deferred tax liabilities	14	5,248	-	-
Other liabilities	28	1,030,505	622,694	440,944
TOTAL LIABILITIES		147,204,143	129,852,823	105,208,000
EQUITY				
Share capital	29	10,164,475	10,164,475	10,164,475
Retained earnings		2,732,925	2,135,770	1,226,785
Reserves		8,098,170	5,898,872	4,645,736
Non-controlling interest		64,856	54,892	43,691
TOTAL EQUITY		21,060,426	18,254,009	16,080,687
TOTAL LIABILITIES AND EQUITY		168,264,569	148,106,832	121,288,687

The accompanying notes are an integral part of these financial statements.

Novi Sad, 28 February 2018



Stevan Čomić
Director of Accounting and
Controlling Sector



Aleksandra Radić
Member of the Executive
Board



Slavko Carić
President of the Executive Board

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2017

(in RSD thousand)

	Share capital	Share premium	Other reserves	Revaluation reserves	Retained earnings	Total	Non-controlling interest	Total
Balance as at 1 January 2016	10,040,000	124,475	4,461,189	220,287	1,191,045	16,036,969	43,691	16,080,687
Total operating result	-	-	-	63,681	-	63,681	27	63,708
Profit for the year	-	-	-	-	2,098,441	2,098,441	11,173	2,109,614
Transfer of profit to reserves	-	-	1,191,044	-	(1,191,044)	-	-	-
Balance as at 31 December 2016	10,040,000	124,475	5,652,233	283,968	2,098,442	18,199,118	54,892	18,254,009
Balance as at 1 January 2017	10,040,000	124,475	5,652,233	283,968	2,098,442	18,199,118	54,892	18,254,009
Total operating result	-	-	-	134,378	-	134,378	19	134,397
Profit for the year	-	-	-	-	2,662,076	2,662,076	9,945	2,672,021
Transfer of profit to reserves	-	-	2,098,441	-	(2,098,441)	-	-	-
Other	-	-	(70,850)	-	70,850	-	-	-
Balance as at 31 December 2017	10,040,000	124,475	7,679,824	418,345	2,732,925	20,995,570	64,856	21,060,426

The accompanying notes are an integral part of these financial statements.

Novi Sad, 28 February 2018

Stevan Čomić
Director of Accounting and
Controlling Sector

Aleksandra Radić
Member of the Executive
Board

Slavko Carić
President of the Executive Board

CONSOLIDATED STATEMENT OF CASH FLOW FOR THE PERIOD FROM 01 JANUARY 2017 TO 31 DECEMBER 2017

	<i>(in RSD thousand)</i>	
	<u>2017</u>	<u>2016</u>
A. Cash flows from operating activities		
Cash inflows from operating activities	13,915,940	12,501,865
Inflow from interest	7,684,432	7,033,057
Inflow from fees	2,311,849	2,190,537
Inflow from other operating income	3,919,410	3,277,869
Inflow from dividends and share in profit	249	401
Cash outflows from operating activities	12,620,539	11,501,018
Outflow from interest	1,436,964	1,416,762
Outflow from fees	772,163	684,704
Outflow from gross salaries, wages and other personnel expenses	1,990,394	1,827,985
Outflow from taxes, contributions and other duties charged to income	397,528	426,969
Outflow from other operating income	8,023,489	7,144,598
Net cash inflows from operating activities before increase or decrease in placements and deposits	1,295,401	1,000,847
Decrease in placements and increase in deposits and other liabilities	7,435,595	17,706,959
Increase in deposits and other liabilities to banks, other financial institutions, Central bank and clients	7,435,595	17,706,959
Increase in placements and decrease in deposits and other liabilities	17,132,466	18,153,975
Increase in loans and receivables from banks, other financial institutions, Central bank and clients	13,962,615	12,966,385
Increase in financial assets initially recognized at fair value through Income statement, financial assets held for sale and other non-investment securities	3,169,852	5,187,590
Net cash inflows from operating activities before income tax	-	553,831
Net cash outflows from operating activities before income tax	8,401,470	-
Net cash inflows from operating activities	-	553,831
Net cash outflows from operating activities	8,401,470	-

CONSOLIDATED STATEMENT OF CASH FLOW FOR THE PERIOD FROM 01 JANUARY 2017 TO 31
DECEMBER 2017

	<i>(in RSD thousand)</i>	
	<u>2017</u>	<u>2016</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Cash inflows from investment activities	<u>308,029</u>	-
Inflow from purchase of investment securities	34,475	-
Outflows from purchase of investment properties	<u>273,554</u>	-
Cash outflows from investment activities	<u>423,408</u>	<u>4,915,704</u>
Outflows from purchase of investment securities	-	4,624,630
Outflows from purchases of intangible assets, property, plant and equipment	9,496	1,977
Outflows from purchase of investment properties	<u>413,912</u>	<u>289,097</u>
Net cash outflows from investment activities	<u>115,379</u>	<u>4,915,704</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Cash inflows from financing activities	<u>11,609,089</u>	<u>8,198,720</u>
Inflow from loans taken	10,645,504	6,936,799
Other cash inflows from financing activities	<u>959,585</u>	<u>1,261,922</u>
Cash outflows from financing activities	<u>1,986,848</u>	<u>1,468,033</u>
Cash outflow from subordinated liabilities	410,083	60,342
Outflow from loans taken	739,365	406,955
Outflows from securities issued	<u>837,401</u>	<u>1,000,736</u>
Net cash inflows from financing activities	<u>9,622,241</u>	<u>6,730,687</u>
TOTAL NET CASH INFLOW	<u>33,268,653</u>	<u>38,407,544</u>
TOTAL NET CASH OUTFLOW	<u>32,163,261</u>	<u>36,038,731</u>
NET INCREASE IN CASH	<u>1,105,392</u>	<u>2,368,813</u>
NET DECREASE IN CASH	-	-
CASH AT THE BEGINNING OF YEAR	<u>11,300,417</u>	<u>8,726,264</u>
POSITIVE FOREIGN EXCHANGE DIFFERENCES	<u>10,214,318</u>	<u>6,676,853</u>
NEGATIVE FOREIGN EXCHANGE DIFFERENCES	<u>9,989,258</u>	<u>6,471,513</u>
CASH AND CASH EQUIVALENTS AT THE END OF YEAR	<u><u>12,630,868</u></u>	<u><u>11,300,417</u></u>

The accompanying notes are an integral part of these financial statements.

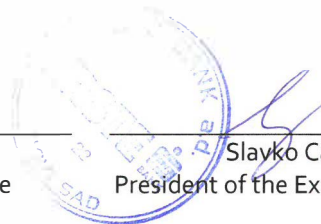
Novi Sad, 28 February 2018



Stevan Čomić
Director of Accounting and
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Aleksandra Radić
Member of the Executive
Board



Slayko Carić
President of the Executive Board

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

1. CORPORATE INFORMATION

Erste Bank a.d., Novi Sad (hereinafter referred to as "the Bank") was founded on 25 December 1989, under the name of Novosadska banka a.d., Novi Sad. At the beginning of August 2005, subsequent to the successful finalization of privatization process, it became a member of Erste Bank Group.

In accordance with the Decision of the Business Registers Agency no. BD 101499/2005 dated 21 December 2005, the change of the previous name Novosadska banka a.d., Novi Sad to Erste Bank a.d. Novi Sad was registered.

The Bank's shareholders are EGB (Erste Group Bank) CEPS HOLDING GMBH, Vienna, with 74% interest and Steiermärkische Bank und Sparkassen AG, Graz, with 26% interest in the Bank's share capital. In order to simplify the Erste Group Bank AG, a transfer of ownership of shares, which were owned by EBG CEPS in European, banks to the Erste Group. In doing so, Erste Group became the direct shareholder of the Bank with a 74% share in the share capital. The decision of the General Assembly to amend the founding acts was made on 30 June 2015, and the change in the APR were carried out on 22 June 2015.

As of 15 January 2014, under the Agreement on Purchase and transfer of Equity Interest executed by and between Steiermärkische Bank und Sparkassen AG and Erste Group Immorent International Holding GMBH, the Bank acquired a 75% equity interest in the company S-Leasing d.o.o. while the remaining 25% are held by Steiermärkische Bank und Sparkassen AG. Moreover, in 2014 the Bank acquired a 19% equity interest in S-Rent d.o.o., Serbia.

Through this transaction, both companies still remained members of Erste Group.

The accompanying financial statements and notes to the financial statements represent the Group's consolidated financial statements. The Bank is the Parent Entity of the Group and as such, in accordance with the requirements of the Law on Banks, it is obligated to prepare consolidated financial statements as of and for the year ended 31 December 2016. The consolidated financial statements include the financial statements of the Leasing, which is 75%-owned by the Bank.

The Bank is registered in the Republic of Serbia to provide banking services of payment transfers in the country and abroad, lending and depositary activities in the country, payment card transactions, operations involving securities and broker-dealer activities. In accordance with the Law on Banks, the Bank operates on the principles stability and security.

The Bank is headquartered in Novi Sad, Bulevar Oslobođenja 5. The Bank operates through 7 business centres, 46 branches, 9 sub-branches and 4 counters.

As of 31 December 2017 the Bank had 1,075 employees (December 31, 2016: 1,021 employees).

The Bank's corporate ID number is 08063818, and its tax ID number (fiscal code) is 101626723.

The Bank's SWIFT code is GIBARS22 and its website is www.erstebank.rs.

The S-Leasing d.o.o. Beograd was established in June 2003.

The Company is organized as a limited liability company and is registered with the Business Registers Agency Decision no. BD 33349/2005 dated 7 June 2005.

The main activity of the Company is the provision of financial leasing of movable assets to individuals and legal entities on the territory of the Republic of Serbia.

The Company's Head Office is in Belgrade, Milutina Milankovica no. 3a.

Company registration number is 17488104. Its tax identification number is 102941384.
The Company had 42 employees as at 31 December 2017 (31 December 2016: 41 employees).

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

2.1. Basis of Preparation and Presentation of the Consolidated Financial Statements

The Group's financial statements (the "financial statements") for 2017 have been prepared in accordance with the International Financial Reporting Standards ("IFRS") and the regulations of the National Bank of Serbia governing the financial reporting of banks.

The accompanying financial statements are presented in the format prescribed under the Decision on the Forms and Contents of the Items in the Forms of the Financial Statements of Banks (Official Gazette of RS nos. 71/2014 and 135/2014).

The Bank holds a 75% interest in the equity of its subsidiary S-leasing d.o.o., Serbia (25% is held by Steiermärkische Bank und Sparkassen AG). In these consolidated financial statements, the Group stated its equity investment held in the subsidiary at cost.

These financial statements were prepared at historical cost principle, except for the following items measured at fair value: financial assets at fair value through profit and loss, held for trading, financial assets available for sale and derivatives

Figures in the accompanying financial statements are stated in thousands of dinars, unless otherwise specified. Dinar (RSD) represents the Group's functional and presentation currency. All transactions executed in other than functional currencies are treated as foreign currency transactions.

The accompanying financial statements have been prepared on a going concern basis, which entails that the Group will continue to operate in the foreseeable future.

In the preparation of the accompanying financial statements, the Group adhered to the accounting policies described further in Note 2.

A) New and amended standards and interpretations

The new and amended IFRSs, set out below, shall enter into force on 1 January 2017:

• **IAS 7 Cash Flow Statement (Amendment): Disclosure**

The standard is applicable starting from or after 1 January 2017, with the possibility of early application. The aim of this amendment is to enable users of financial statements to assess changes in the obligations arising from financing activities, including changes arising both from monetary and non-monetary changes. The amendment defines that the only way to meet the disclosure requirement is a tabular presentation of the opening and closing balance sheet balances for liabilities arising from financing activities, including changes in cash flows from financing activities, changes arising from the acquisition of control and the sale of a share or interest, exchange rate effect, change in fair value and other changes. It is not expected that changes to this standard will have an impact on the Group's financial statements.

- The International Accounting Standards Board issued the **Annual Improvements to IFRS 2014-2016**, which is a set of amendments to existing IFRSs. Amendments to Standards are Applicable for periods beginning from or after 1 January 2017 for IFRS 12 Disclosure of interest in other entities and for periods beginning from or after 1 January 2018 for IFRS 1 First-time adoption of International Financial Reporting Standards and IAS 28 Investments in Associated Entities. The possibility of earlier application is permitted for IAS 28 Investments in associated Entities. It is not expected that changes to this standard will have an impact on the Group's financial statements.

- IFRS 1 First-time Adoption of International Financial Reporting Standards: The given improvement removes short-term exemptions in connection with disclosures about financial instruments, employee benefits and investment entities, applicable when first-time standards apply.
- IAS 28 Investments in Associated Entities: Amendments clarify that the application of fair value through income statement to an associate entity by an investment capital organization or another qualified entity is available for each investment in associated entities on an individual investment basis after an initial recognition.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

A) New and amended standards and interpretations (continued)

• **IAS 12 Income Tax (Amendment): Recognition of deferred tax assets for unrealized losses**

The amendments are applicable starting from or after 1 January 2017, with the possibility of early application. The aim of these amendments is to clarify the calculation of deferred tax assets for unrealized losses, in order to respond to the different implementation of IAS 12 in practice. Specific problems for which there are different solutions in practice relate to cases where a deductible temporary difference arises after the decrease in fair value, then to a recovery of an asset higher than its carrying amount, to a probable future taxable profit, and a combined estimate against a single estimate. It is not expected that changes to this standard will have an impact on the Group's financial statements.

B) Standards issued but not yet entered into force and have not been adopted before

International Financial Reporting Standard 9 Financial Instruments

On July 2014 IASB issued IFRS 9 Financial Instruments, a standard that will replace IAS 39 from January 1, 2018. IFRS 9 addresses the three main areas of accounting for financial instruments: classification and measurement of financial assets and liabilities, introduces new principles for hedge accounting and a new impairment model for financial assets.

The Bank has established an Implementation Team ("Team") with members from risk, finance and operations teams for the preparation and implementation of IFRS 9 ("Project"). The sponsor of the project is a member of the Executive Committee responsible for risks and finances, which regularly reports to the Supervisory Board of the Bank, and the project is managed in the framework of the Bank's transformation. The Bank's C & M team defined the FV / AC checking process in the initial credit recognition as well as the subsequent modification of the loan. All changes and alignment of the primary bank system required to support the process were carried out in 2017. Regarding the impairment of financial assets, the Bank in parallel with the development of parameters, worked on the methodology, processes and technical solution for defining the level and calculation of reserves in accordance with the new standard.

IFRS 9 introduces two criteria for the classification and measurement of financial assets: 1) an entity's business model for managing the financial assets and 2) the contractual cash flow characteristics of the financial assets. As a result, a financial asset is measured at amortized cost ("AC") only if both of the following conditions are met: a) the asset is held within a business model whose objectives to hold assets in order to collect contractual cash flows ('held to collect') and (b) the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest ("SPPI") on the principal amount outstanding. Measurement at fair value through other comprehensive income ("FVOCI") is applicable to financial assets held within a business model whose objective is achieved by both collecting of contractual cash flows and selling the assets ("hold and sell") while the condition b) is also fulfilled. All other financial assets are measured at fair value through profit or loss ("FVTPL").

In respect of the business model criterion, the Bank has to assess the expected selling activity of financial assets. Sales due to increases in credit risk, sales close to assets' maturity, infrequent sales triggered by a non-recurring event (such as changes in regulatory environment, severe liquidity crisis) are considered as not contradicting the "held to collect" business model. Other kinds of sales are expected to be insignificant as to their volume. As a result, sales are incidental in the "held to collect" business model.

Regarding the contractual cash flows characteristics criterion, the Bank concluded that the vast majority of its loan portfolio, which is currently classified as loans and receivables, will continue to be measured at AC.

Investments in equity instruments that are currently categorised as available-for-sale will be categorised as FVTPL.

When it comes to classification and measurement of financial liabilities, upon transition to IFRS 9, there are no changes in classification and valuation in relation to IAS 39.

The hedge accounting model is not relevant to the Bank since we do not apply the hedge accounting.

The new impairment model requires recognition of credit loss allowances ('CLA') based on expected credit losses ('ECL') rather than only incurred credit losses, as is the case under IAS 39. It applies to credit risk exposures stemming from debt instruments at AC or FVOCI, lease receivables, financial guarantee contracts and certain loan commitments.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

B) Standards issued but not yet entered into force and have not been adopted before (continued)

International Financial Reporting Standard 9 Financial Instruments (continued)

For credit risk exposures that are not credit-impaired at initial recognition, the bank will recognize CLA at an amount equal to the 12-month ECL (referred to as "Stage 1") for as long as no significant increase in credit risk since initial recognition ("SICR") is identified at the reporting date. In the other cases, CLA is measured at lifetime ECL and the related instruments are referred to as "Stage 2", unless they are found to be credit-impaired at the reporting date (referred to as "Stage 3"). For purchased or originated credit-impaired financial assets ('POCI'), only adverse changes in lifetime ECL after the initial recognition are distinctly recognized as CLA, whilst favourable changes are recognized as impairment gains increasing the carrying amount of the related POCI assets.

For lease receivables and trade receivables containing a significant financing component (where the Bank also includes its factoring receivables), IFRS 9 allows a simplified impairment approach, whereby credit loss allowances are always measured at lifetime ECL. The Bank will not apply this simplification.

In the area of ECL modelling and CLA calculation, the Bank has identified a number of key drivers, as follows:

a) the "credit-impaired" definition

In respect of applying the "credit impaired" concept of IFRS 9, the Bank generally adopted the approach of aligning it with the regulatory concept of "default" for lending exposures. If the default status exists already at an exposure's initial recognition (e.g. in the context of a significant distressed restructuring), then that exposure is identified as POCI.

b) the SICR indicators applicable to not-credit impaired exposures

Across portfolios and product types, a number of quantitative and qualitative SICR indicators have been defined, in addition to the SICR indicator of 30 days-past-due.

Thus, SICR is quantitatively measured by reference to the adverse change, since instrument's initial recognition, in the current annualised remaining lifetime probability of default ('PD') and in the current 12-month PD. Significance of such change is assessed by reference to a combination of relative and absolute change thresholds. The thresholds are established at PD segment level or client rating level, as appropriate, and are subject to initial and on-going validation.

Qualitative SICR indicators include forbearance-type flags, a work-out transfer flag, information from early-warning-system that is not sufficiently reflected in rating grades, as well as fraud indicators. The assignment of some specific qualitative indicators inherently relies on experienced credit risk judgment being exercised adequately and timely. Besides the qualitative indicators defined on client level, the assessment of significant increase in credit risk is performed on portfolio level if the increase in credit risk on individual instrument or client level is only available with a certain time lag or is observable exclusively on portfolio level.

Upon transition to IFRS 9, the SICR has to be determined in respect of PDs which existed at instruments' initial recognition. Where retrospective identification PDs at initial recognition was not possible without undue cost or effort, the bank implemented the following sequence of approximation methods: closest rating to initial recognition, re-rating based on historic data with current rating model, best possible rating for the relevant portfolio at the time, first available rating.

Application of the "low credit risk exemption" allowed by IFRS 9 for "investment grade" or other "low risk" –deemed assets (and resulting in 12 months expected credit losses being calculated irrespective of SICR quantitative measures) will be limited to particular types of debt securities and counterparty categories, and only if supported by sufficient "low risk" evidence at local level.

c) ECL modelling

The key risk parameters used in the measurement of ECLs - PD, loss given default ('LGD') and exposures at default ('EAD') - are derived from internally developed statistical models and other historical data that leverage regulatory models.

The PD describes a probability that a client will default on the related loan obligation. The 12-month PD reflects the estimated probability of default within one year from the reporting date, whilst the lifetime PD indicates the estimated probability of default until instrument's maturity and cumulates conditional marginal 12-month PD estimates attributable to each year until maturity. The PD estimation methods used in Erste Group depend on the segmentation criteria defined by the relevant local strategic risk management units. The applicable estimation methods include average default rate analysis and an internal/external migration matrices and consider adjustments to the point-in-time estimate where applicable due to the time frame of the history of the data used for the assessment.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

B) Standards issued but not yet entered into force and have not been adopted before (continued)

International Financial Reporting Standard 9 Financial Instruments (continued)

The LGD captures the loss rate in the case of default. In general, the selection of estimation method depends on portfolio, and whether the curve is defined on LGD segment, client or account level. The LGD estimation methods applicable in Erste Group include a simple scenario approach and an advanced multiple scenario approach. For defaulted exposures, the calculation methodology used is based on secured/unsecured characteristics of the account, the applied values are expert-based, regulated in accordance with the LLP backtesting, and the estimation of the LGD is ongoing and will be completed and implemented in 2018.

The EAD that is attributable to any given future year throughout an on-balance exposure's remaining maturity is approximated on the basis of exposure's current gross carrying amount multiplied by an amortization coefficient that depends on the exposure's contractual repayment type. For off-balance not credit-impaired exposures, the EAD approximation is based on the current nominal amount of the exposure, multiplied by the credit conversion factor.

d) Consideration of forward-looking information ("FLI")

Measurement of ECL and SICR assessment requires further consideration of FLI, which the Bank has addressed by introducing a baseline forecast and a number of alternative scenarios for selected macroeconomic variables. These are derived, together with their probabilities of occurrence, as a deviation from baseline forecasts, where the baseline forecasts are, with a few exceptions, internally determined by the research department of Erste Group. Taking into account multiple scenarios, the "neutral" PDs (and also LGD, with a few exceptions) are adjusted through macro models which link relevant macroeconomic variables with risk drivers. Thus, the unbiased, probability-weighted ECL is derived with the weights representing the occurrence probabilities of each macroeconomic scenario.

Typical macroeconomic variables may include real gross domestic product, unemployment rate, inflation rate, production index as well as market interest rates. The selection of variables also depends on the availability of reliable forecasts for the given local market. FLI is not initially applied in the Bank and is planned to be implemented in 2018.

Transition to IFRS 9 is expected to result in an increase of the 2018 opening balance of credit loss allowances compared to the 2017 closing balance of loan loss provision under IAS 39 (including provisions for off-balance exposures treated under IAS 37) by approximately RSD 664 million, out of which RSD 659 million relates to the Bank and RSD 5 million to S-Leasing.

In addition to the above mentioned effect, the Bank's management expect the following effects as a result of the transition to IFRS 9: decrease of equity in approximate amount of RSD 31 million resulting from retrospective application of modification losses, increase of equity in approximate amounts of RSD 87 million and RSD 5 million as a result of collected suspended interest and change in equity instruments measurement, respectively, whereas the expected tax impact is approximately RSD 10 million.

• **IFRS 15 Revenue from contracts with customers**

The standard is applicable starting from or after 1 January 2018. IFRS 15 establishes a five-step model to be applied to contract revenue with customers (with a limited number of exceptions), regardless of the type of revenue or industry. Standard requirements will also apply to the recognition and measurement of gains and losses on the sale of some non-financial assets, which is not a consequence of the Group's usual activities (e.g. sale of fixed tangible or intangible assets). The standard requires detailed disclosures, including the classification of total revenues, information on the performance obligations of the contract, changes in the status of assets and liabilities under the contracts between periods, and key estimates. The Group's management is currently in the process of assessing the potential impact of the requirements of this standard on the Group's financial statements.

• **IFRS 15 Revenue from contracts with customers (clarifications)**

The clarifications of the standards will apply starting from or after 1 January 2018, with the permitted prior application. The objective is to clarify the intention of the International Accounting Standards Committee to define the requirements of IFRS 15 Revenue from contracts with customers, especially in the part relating to the accounting coverage of identified performance commitments, clarifying the principle of "individual identification", the principal-agent problem whether the Company is a principal or agent), as well as the application of control access and licensing, providing additional guidance for the accounting treatment of intellectual property and copyrights. Clarifications also provide additional practical advice to the Group that will apply IFRS 15 completely retrospectively, or which will choose the application of a modified retrospective approach. It is not expected that the requirements of this standard will have a significant impact on the Group's financial statements.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

B) Standards issued but not yet entered into force and have not been adopted before (continued)

• **IFRS 16 Leasing**

The standard is applicable starting from or after 1 January 2019. IFRS 16 defines the initial recognition, measurement and disclosure of leasing for both parties to the contract, i.e. for the buyer ("borrower") and for the supplier ("the lender"). A new standard requires the borrower to recognize most of the loans in their financial statements. Lenders will have one accounting model for all types of leasing, with some exceptions. The lender's accounting remains essentially unchanged. The Group's management is in the process of determining the effects that the application of this standard will have on the Group's financial statements.

• **IFRS 10 Consolidated Financial Statements and IAS 28 Investments in Associates: Selling assets between an Investor and a Subsidiary (Amendment)**

Amendments indicate a known disagreement between the requirements in IFRS 10 and those in IAS 28 relating to the sale or entry of assets between the investor and its subsidiaries and joint ventures. The result of the amendment is that the total loss or gain is recognized when the transaction affects the business, whether it is a subsidiary or not. A partial gain or loss is recognized when a transaction is tangible to assets that are not essential for the conduct of a business, even when these assets are part of a subsidiary. In December 2015, the International Accounting Standards Board postponed the date of application of this standard pending the outcome of the survey on the method of participation. It is not expected that changes to this standard will have an impact on the Group's financial statements.

• **IFRS 2: Classification and evaluation of share payments (Amendment)**

Amendments to the standards are applicable for a period beginning on or after 1 January 2018, with the possibility of early application. Amendments to the standards relate to the requirements for the accounting presentation of the effects of the fulfilment and non-fulfilment of the conditions for acquiring in the valuation of transactions in cash-based transactions, in the payment transactions of shares with net settlement characteristics when calculating the tax-deductible tax liability and in changing the terms and conditions of payment for shares changing the classification of the transaction from cash-based payment transactions for equity-based equity. It is not expected that changes to this standard will have an impact on the Group's financial statements.

• **IAS 40: Transfer to Investment Property (Amendments)**

Amendments to the standards are applicable for a period beginning on or after 1 January 2018, with the possibility of early application. Amendments to Standards indicate when an entity needs to perform a property transfer, including assets in preparation or development in, or from investment property. Amendments state that a change in use occurs when the asset fills up, or ceases to fulfil, the definition of an investment property, and there is evidence of a change in its use. Changing the intention of the management regarding the way of using the property does not provide evidence of changing its use. It is not expected that changes to this standard will have an impact on the Group's financial statements.

• **IFRS 17: Insurance Contracts**

The standard is applicable for a period beginning on or after 1 January 2021, with the possibility of early application. IFRS 17 replaces IFRS 4, which has given companies dispensation to carry on accounting for insurance contracts using existing practices. As a consequence, it was difficult for investors to compare and contrast the financial performance of otherwise similar insurance companies. IFRS 17 is a single principle-based standard to account for all types of insurance contracts, including reinsurance contracts that an insurer holds. The standard requires recognition and measurement of groups of insurance contracts at: (i) a risk-adjusted present value of the future cash flows (the fulfilment cash flows) that incorporates all of the available information about the fulfilment cash flows in a way that is consistent with observable market information; plus (if this value is a liability) or minus (if this value is an asset) (ii) an amount representing the unearned profit in the group of contracts (the contractual service margin). Insurers will be recognising the profit from a group of insurance contracts over the period they provide insurance coverage, and as they are released from risk. If a group of contracts is or becomes loss-making, an entity will be recognising the loss immediately. It is not expected that changes to this standard will have an impact on the Bank's financial statements.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017****2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)****B) Standards issued but not yet entered into force and have not been adopted before (continued)****• IFRIC Interpretation 22: Foreign Currency Transactions and Advance Review**

The interpretation is applicable for a period beginning on or after 1 January 2018, with the possibility of early application. This interpretation considers how to determine the date of the transaction when applying the standard on foreign currency transactions, IAS 21. The interpretation applies where an entity either pays or received consideration in advance for foreign currency-denominated contracts. The interpretation specifies that the date of transaction is the date on which the entity initially recognizes the non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration. If there are multiple payments or receipts in advance, the Interpretation requires an entity to determine the date of transaction for each payment or receipt of advance consideration. It is not expected that changes to this standard will have an impact on the Bank's financial statements.

• IFRIC Interpretation 23: Uncertainty over Income Tax Treatments

The interpretation is applicable for a period beginning on or after 1 January 2019. IAS 12 specifies how to account for current and deferred tax, but not how to reflect the effects of uncertainty. The interpretation clarifies how to apply the recognition and measurement requirements in IAS 12 when there is uncertainty over income tax treatments. An entity should determine whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments based on which approach better predicts the resolution of the uncertainty. An entity should assume that a taxation authority will examine amounts it has a right to examine and have full knowledge of all related information when making those examinations. If an entity concludes it is not probable that the taxation authority will accept an uncertain tax treatment, the effect of uncertainty will be reflected in determining the related taxable profit or loss, tax bases, unused tax losses, unused tax credits or tax rates, by using either the most likely amount or the expected value, depending on which method the entity expects to better predict the resolution of the uncertainty. An entity will reflect the effect of a change in facts and circumstances or of new information that affects the judgments or estimates required by the interpretation as a change in accounting estimate. Examples of changes in facts and circumstances or new information that can result in the reassessment of a judgment or estimate include, but are not limited to, examinations or actions by a taxation authority, changes in rules established by a taxation authority or the expiry of a taxation authority's right to examine or re-examine a tax treatment. The absence of agreement or disagreement by a taxation authority with a tax treatment, in isolation, is unlikely to constitute a change in facts and circumstances or new information that affects the judgments and estimates required by the Interpretation.

The following other new pronouncements are not expected to have any material impact on the Bank's financial statements:

- Annual Improvements to IFRSs 2014-2016 cycle – Amendments to IFRS 1 and IAS 28 (issued on 8 December 2016 and effective for annual periods beginning on or after 1 January 2018).
- Prepayment Features with Negative Compensation – Amendments to IFRS 9 (issued on 12 October 2017 and effective for annual periods beginning on or after 1 January 2019).
- Long-term Interests in Associates and Joint Ventures – Amendments to IAS 28 (issued on 12 October 2017 and effective for annual periods beginning on or after 1 January 2019).
- Annual Improvements to IFRSs 2015-2017 cycle – amendments to IFRS 3, IFRS 11, IAS 12 and IAS 23 (issued on 12 December 2017 and effective for annual periods beginning on or after 1 January 2019).
- Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts – Amendments to IFRS 4 (issued on 12 September 2016 and effective, depending on the approach, for annual periods beginning on or after 1 January 2018 for entities that choose to apply temporary exemption option, or when the entity first applies IFRS 9 for entities that choose to apply the overlay approach).

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.2. Basis for consolidation

The accompanying consolidated financial statements include the financial statements of the Bank and of the company under the Bank's control. Control exists if the Bank has the power to manage the financial and operating policies of the subsidiary in such a manner that it can realize benefits from its activities. Control is achieved if the Bank has exposure to or rights to variable returns from its involvement with the investee and has the ability use its power over the investee to affect the amount of returns.

Income and expenses of the subsidiary are included in the consolidated income statement and other comprehensive income from the effective date of control acquisition. Financial statements of the subsidiary are adjusted as appropriate so as to align its accounting policies with those applied by the Bank as the Parent Entity of the Group. All balances receivable or payable, income and expenses arising from intra-group transactions are eliminated in full upon consolidation. The non-controlling interest represents a share in the profit or loss and equity of the subsidiary of which the Bank is neither direct nor indirect owner. The non-controlling interest is presented separately in the Group's income statement and within equity in the statement of financial position, separately from the Bank's equity.

2.3. Business Combinations

As at 31 December 2017 the Bank holds 75% ownership of the Leasing. At the date of acquisition, total assets of the Leasing amounted to RSD 3,092,233 thousand, total equity amounted to RSD 60,455 thousand while the loss amounted to RSD 113,284 thousand. On 31 December 2017, total assets of the Leasing amounted to RSD 6,671,465 thousand, total equity amounted to RSD 67,500 thousand while the profit amounts to RSD 191,494 thousand.

A business combination including entities or operations under joint control is a business combination in which the said entities are under joint control of the same party, both before and after the business combination, and such control is not transitory, since IFRS 3 does not apply to business combinations of entities under joint control, in accordance with IAS 8, the Group adopted an accounting policy whereby such transactions are accounted for using the pooling of interest method.

Application of the method is as follows:

- The assets and liabilities of the entity being acquired are shown at carrying value as presented in the separate financial statements of the Parent Entity;
- There are no new estimates of fair value or recognition of any new assets or liabilities, adjustments are only carried out in order to harmonize accounting policies;
- Goodwill arising on acquisition is not recognized;
- The difference between the consideration paid / transfer and "acquired" capital is shown in the equity section;
- The income statement reflects the result of all companies for the whole financial year, if the combination took place earlier at the start of the year and the deviation is immaterial;
- Comparatives are not restated.

2.4. Interest Income and Expenses

Interest income and expenses, including penalty interest and other income and other expenses from interest bearing assets, i.e. liabilities are recognized on an accrual basis under obligatory terms defined by a contract executed between the Group and a customer.

For all financial instruments measured at amortized cost and interest-bearing financial instruments classified as available for sale, interest income and expense are recognized using the effective interest rate, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability.

The calculation of the effective interest rate takes into account all contractual terms of the financial instrument but not future credit losses.

2.5. Fee and Commission Income and Expenses

The Group earns/pays fee and commission income from rendering and using banking services. Fees and commissions are generally recognized on an accrual basis when the service has been provided, i.e. rendered.

Fees and commission income are earned from a diverse range of banking services provided to clients. Fee income can be divided into the three following categories:

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.5. Fee and Commission Income and Expenses (continued)

/i/ Fee Income Earned from Services Rendered Over a Certain Period of Time

Fees earned for the provision of services over time are deferred over the period of service rendering.

Loan origination fees for loans likely to be drawn down and other loan-related fees are deferred (together with any incremental costs) and recognized as adjustment to the loan effective interest rate.

/ii/ Fee Income Earned from Transaction Services

Fees or components of fees that are linked to the performance of certain transactions are recognized upon fulfilment of the corresponding criteria.

/iii/ Dividend Income

Dividend income is recognized when the Group's right to receive the payment is established.

2.6. Foreign Exchange Translation

Financial statement items are stated using the currency of the Group's primary economic environment (functional currency). The accompanying financial statements are stated in thousands of dinars (RSD).

Transactions denominated in foreign currencies are translated into dinars at the official middle exchange rates determined at the Interbank Foreign Exchange Market and effective at the date of each transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are into dinars at the official middle exchange rates determined at the Interbank Foreign Exchange Market prevailing as of that date.

Net foreign exchange positive or negative effects arising upon the translation of transactions, and the assets and liabilities denominated in foreign currencies are credited or charged to the income statement as foreign exchange gains or losses and positive or negative currency clause effects.

Gains or losses realized/incurred upon translation of financial assets and liabilities with a currency clause index are recorded within the income statements as foreign exchange gains or losses and positive or negative currency clause effects.

Commitment and contingent liabilities in foreign currencies are translated into dinars at official middle exchange rates of the National Bank of Serbia effective as at the reporting date.

2.7. Financial Instruments

All financial instruments are initially recognized at fair value (except for financial assets and financial liabilities at fair value through profit and loss), increased by transaction costs that are directly attributable to their acquisition or issue.

Financial assets and financial liabilities are recognized in the Group's statement of the financial position on the date upon which the Group becomes counterparty to the contractual provisions of a specific financial instrument. All regular way purchases and sales of financial assets are recognized on the settlement date, i.e. the date the assets is delivered to the counterparty.

"Day 1" Profit

When the transaction price in an inactive market is different to the fair value from other observable current market transactions in the same instrument or based on a valuation technique whose variables include data from observable markets, the Group immediately recognizes the difference between the transaction price and fair value ("Day 1" profit) in the income statement.

Classification of Financial Instruments

The Group's management determines the classification of its financial instruments at initial recognition. Classification of financial instruments upon initial recognition depends on the purposes for which financial instruments have been obtained and their characteristics.

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

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.7. Financial Instruments (continued)

Subsequent measurement of financial assets depends on their classification as follows:

2.7.1. Financial Assets at Fair Value through Profit and Loss

This category includes two sub-categories: financial assets held for trading and those designated at fair value through profit or loss.

Financial assets are classified as held for trading if they have been primarily acquired for generating profit from short-term price fluctuations or are derivatives. Trading securities are stated in the statement of financial position at fair value.

The Group also has derivatives classified as assets at fair value through profit and loss.

The management did not classify financial instruments, on initial recognition, into the category of the financial assets stated at fair value through profit or loss.

Securities held for trading comprise the Republic of Serbia Government savings bonds and Treasury bills.

All realized or unrealized gains and losses arising upon measurement and sale of financial assets at fair value are stated in the income statement.

2.7.2. Financial Assets Held to Maturity

Securities held to maturity are financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity and that do not meet the criteria of the definition of loans and receivables.

After initial recognition, securities held-to-maturity are subsequently measured at amortized cost using the effective interest rate method, less any allowance for impairment or impairment losses, if any. Amortized cost is calculated by taking into account any discount or premium on acquisition, over the period to maturity.

Interest accrued on such instruments is credited to interest income in the profit and loss account using the effective interest method. Fees that are part of the effective interest on these instruments are recognized in the income statement over the life of the instrument.

The Group performs individual assessment in order to determine whether there is objective evidence on impairment of the investment into securities held-to-maturity.

If there is objective evidence that such securities have been impaired, the amount of impairment loss for investments held to maturity is calculated as the difference between the investment's carrying amount and the present value of expected future cash flows discounted at the investment's original effective interest rate and stated in the income statement as losses from impairment of financial assets.

If, in a subsequent year, the amount of the estimated impairment loss decreases as a consequence of an event occurring after the impairment was recognized, the previously recognized impairment loss is reduced and effects are credited to the income statement. Reversal of the impairment allowance will not result in the carrying value of an asset in excess of the amortized cost as if the asset had not been impaired.

2.7.3. Loans and Receivables due from Banks and Customers

Loans and receivables are assets that the Group does not intend to sell in the near term and those that are not classified, after initial recognition, as financial assets at fair value through profit and loss or financial assets available for sale.

After initial recognition, loans and receivables are measured at their amortized cost using the effective interest method less impairment, if any. Amortized cost is calculated by taking into account any discount or premium on acquisition and any issue costs and that are integral part of the effective interest rate. Interest income in respect of these instruments are recorded and presented under interest income within the income statement. Any impairment losses are recognized within net losses from impairment of financial assets within the income statement.

Loans in dinars for which risk protection has been agreed by linking the dinar exchange rate against the foreign currency are revalued in accordance with the specific contract for each loan. The difference between the value of the outstanding principal and the amount calculated using the currency clause is recorded within the given loans and deposits. Gains and losses arising from the application of a foreign currency clause are recorded in the income statement as income/expense foreign exchange rate differences based on the contractual currency clause.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.7. Financial Instruments (continued)

2.7.3. Loans and Receivables due from Banks and Customers (continued)

Derecognition of Financial Assets and Liabilities

The Group derecognizes financial assets when it loses control over the contractual rights over such instruments, which occurs when the when the contractual rights to the cash flows from the financial asset have been realized, cancelled or ceded or they expire. When the Group transfers the contractual rights to the cash flows from a financial asset or executes a contract on such transfer, and thereby the Group neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset, the asset is recognized to the extent of the Group's involvement in respect of the asset. Any further involvement of the Group in the transferred asset, in the form of a guarantee for the asset transferred, is measured at the lower of the asset's original carrying value and the maximum amount of the consideration the Group will need to pay.

In case of significant modifications of contractual terms (such as reprogramming), the Group ceases to recognize the old asset and recognize a new, modified asset.

A financial liability is derecognized when its contractual obligation is discharged, cancelled or expired. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of the existing liability are substantially modified, such an exchange or modification is treated as derecognition of the original liability and the simultaneous recognition of a new liability, with the difference between the respective carrying amounts recognized in the income statement.

Impairment of Financial Assets and Risk Provisions

In accordance with the Group's internal policy, at each reporting date the Group assesses whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred "loss event") and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated.

Evidence of impairment may include indications that a borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganization and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults. Initially, the Group assesses impairment on a group (portfolio) basis before deterioration of a borrower's creditworthiness is identified (e.g. increased number of days past due).

In assessing impairment of loans and receivables due from banks and customers measured at amortized cost, in instances of identified deterioration in borrowers' creditworthiness, the Group assesses individually whether objective evidence of impairment exists for financial assets that are individually significant, or collectively for financial assets that are not individually significant.

If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes an asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be recognized, are not included in a collective assessment of impairment.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.7. Financial Instruments (continued)

2.7.3. Loans and Receivables due from Banks and Customers (continued)

Impairment of Financial Assets and Risk Provisions (continued)

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the assets' carrying amount and its recoverable value, being the present value of estimated future cash flows, discounted at the original effective interest rate for that particular financial asset. If a loan has a variable interest rate, current effective interest rate is applied.

The calculation of the present value of the estimated future cash flows of a collateralized financial asset, in addition to the cash flows from the borrower's operating activities, reflects the cash flows that may result from collateral foreclosure.

For the purpose of group (collective) impairment assessment, financial assets are grouped on the basis of the Group's internal classification system that takes into account credit risk characteristics such as the borrower's financial situation, loan type, operating segment the borrower belongs to, existence of the other receivables matured due from the same borrower, past-due status and other relevant factors.

Future cash flows on a group of financial assets that are collectively assessed for impairment are estimated on the basis of expert opinion supported by historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the years on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently.

The Group reviews the methodology and assumptions used for estimating future cash flows on an annual basis in order to reduce any differences between loss estimates and actual loss experience.

The carrying amount of the loan is reduced through the use of an allowance account and the amount of the impairment loss arising from impairment of loans and receivables, as well as other financial assets measured at amortized cost, is recognized in the income statement within net losses from impairment of financial assets and credit risk-weighted off-balance sheet assets. A financial assets is deemed irrecoverable when the Group has no realistic expectation of its recovery. Indicators of probable irrecoverability include: borrower's delay in liability settlement, instigation of the bankruptcy or liquidation procedures, deletion of the borrower from the Business Entity Register, borrower's contestation of the Group's receivables upon balance reconciliation of receivables and liabilities, etc.

Receivables are written off only when all available sources of collection have been exhausted (e.g. bankruptcy proceedings ended, lawsuit completed, all available collaterals activated, borrower's assets cross-checked). Loans and the related impairment allowances are derecognized (written off) when considered uncollectable. Write-offs are either recorded against the impairment allowance account or directly expensed. Irrecoverable receivables are written off under the competent court ruling, the relevant decision of the Group's Assembly of Executive Board when there is no realistic prospect of their future recovery and all collaterals have been activated.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognized in the income statement as gain on the reversal of impairment of financial assets and credit risk-weighted off-balance sheet terms. Reversal of the impairment allowance will not result in the carrying value of an asset in excess of the amortized cost as if the asset had not been impaired.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.7. Financial Instruments (continued)

2.7.4. Rescheduled Loans

Where possible, the Group seeks to reschedule or restructure loans rather than foreclose collaterals. This may involve extending the payment terms or any other modification to the original loan agreement provisions. Rescheduling or restructuring may be business rescheduling or forbearance as per EBA definition.

Business loan rescheduling entails alteration to the originally agreed loan terms not caused by the borrower's financial position deterioration, or mitigation of the consequences of the deteriorated financial position of the borrower, and does not represent restructuring. It is rather a result of a changed market situation (customers, suppliers, competitors) and the need to adjust the loan repayment schedule and terms to the newly arisen situation.

Forbearance represents restructuring caused by:

- the borrower's inability to fulfil its contractual obligations due to financial difficulties and
- the need of the Group to make certain concessions to enable the borrower to service its liabilities.

Once the terms have been renegotiated, the loan is no longer considered past due, but if after restructuring evidence of impairment arises, the client will again be assigned the default status. The Group continuously monitors rescheduled/restructured loans to ensure that all criteria are met, as well as that future payments are made or default status assigned in a timely manner to the clients not complying with the re-defined criteria.

2.7.5. Financial Assets Available for Sale

Securities intended to be held for an indefinite period of time, which may be sold or pledged with the National Bank of Serbia as security, in response to needs for liquidity or changes in interest rates, exchange rates or equity prices are classified as "available-for-sale". Available-for-sale securities include other legal entities' equity instruments and debt securities.

Subsequent to the initial measurement, these securities are measured at fair value. The fair values of securities quoted in active markets are based on current bid prices. Unrealized gains and losses are recognized within other comprehensive income until such a security is sold, collected or otherwise realized, or until it is impaired. In case of disposal of securities or their impairment, cumulative fair value adjustments are recognized in the statement of other comprehensive income.

Equity investments in other legal entities that do not have a quoted market price in an active market and for which other methods of reasonably estimating fair value are inappropriate are exempt from market fair value measurement and are stated at cost less any impairment allowance.

Dividends earned whilst holding available-for-sale financial instruments are recognized within other operating income and dividend income and income from equity investments when the right to receipt of dividend has been established.

For investments in shares and other securities available for sale, at the reporting date, the Group assesses if there is significant evidence of impairment of one or more investments. The Group records impairment charges on available-for-sale equity investments when there has been a significant or prolonged decline in the fair value below their cost.

When there is objective evidence of impairment, cumulative loss, measured as the difference between the cost and the current fair value of the asset, less any impairment loss of the investment previously recognized within profit and loss is reclassified from equity to profit or loss. Impairment allowances of available-for-sale investments are not reversed through profit and loss; subsequent increases of fair value, after recognition of impairment, are credited to equity.

Impairment allowances of equity investments, which are not quoted in an active market and whose fair value cannot be determined with certainty, are measured as the difference between the book value and the present value of expected future cash flows, and are recognized in the income statement and are not reversed before derecognition.

In case of debt securities that are classified as available for sale, impairment is assessed based on the same criteria as for financial assets carried at amortized cost. If there is an increase in fair value in the subsequent year, and if that increase may objectively refer to an event that occurred after the impairment loss had been recognized in the income statement, the impairment loss is reversed through profit or loss.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.7. Financial Instruments (continued)

2.7.6. Issued Financial Instruments and Other Financial Liabilities

Issued financial instruments or their components are classified as liabilities where the substance of the contractual arrangement results in the Group having an obligation either to deliver cash or another financial asset to the holder, or to satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity shares.

Components of compound financial instruments that contain both liability and equity elements are accounted for separately, with the equity component being assigned the residual amount after deducting from the instrument as a whole the amount separately determined as the fair value of the liability component on the date of issue.

Subsequent measurement of financial liabilities depends on their classification as follows:

Deposits and Other Liabilities due to Banks and Customers

All deposits from other banks and customers and interest-bearing financial liabilities are initially measured at fair value less transaction costs, except for the financial liabilities at fair value through profit and loss. After initial recognition, interest-bearing deposits and borrowings are subsequently measured at amortized cost.

Borrowings

Borrowings are recognized initially at fair value net of transaction costs incurred. Borrowings are subsequently stated at amortized cost. Borrowings are classified as current liabilities, unless the Group has the undisputable right to postpone the settlement of obligations for at least 12 months after the reporting date.

Other Liabilities

Trade payables and other current operating liabilities are stated at nominal value.

2.8. Offsetting Financial Assets and Financial Liabilities

Financial assets and liabilities are offset and the net amount reported in the statement of financial position if, and only if when there is a currently enforceable legal right to offset the recognized amounts and the Group has an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

2.9. Cash and Cash Equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise balances on the Group's and Lessor's RSD current accounts and cash in hand (both in dinars and foreign currency) and foreign currency accounts and deposits with up to 3-month maturities held with other domestic and foreign banks.

2.10. Repurchase Transactions ("Reverse Repo" Transactions)

Securities purchased under agreements to repurchase at a specified future date ('repos') are recognized in the statement of financial position.

The corresponding cash given, including accrued interest, is recognized in the balance sheet. The difference between the sale and repurchase prices is treated as interest income and is accrued over the life of the agreement.

2.11. Investments in subsidiaries

A dependent legal entity is the entity over which the Group has control. Control is established when the Group is exposed, or is entitled to, variable returns on the basis of participating in the entity in which it has invested and has the ability to influence those benefits based on the power it has over the entity in which it has invested.

On 31 December 2017, the Group owns 75% of the ownership of the company S Leasing doo, Belgrade. Participation in the capital of the said dependent legal entity is stated at the cost less any allowance for impairment in the individual financial statements of the Group.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017****2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)****2.12. Intangible Assets**

Intangible assets are measured at cost, less accumulated amortization and impairment losses, if any. Intangible assets comprise licenses and other intangible assets.

The useful lives of intangible assets are assessed to be either finite or indefinite.

The amortization period and the amortization method for an intangible asset with a finite useful life are reviewed at least once a year, at the financial year-end.

Changes in the expected useful life or the expected pattern of consumption of future economic benefits embedded in the asset are accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates.

Amortization of intangible assets is calculated using the straight-line method to write off the cost of intangible assets over their estimated useful lives, as follows:

Software licenses	Up to 10 years
Other intangible assets	4 years

The amortization cost on intangible assets with finite lives is recognized in the income statement.

Costs associated with developing and maintaining computer software programs are recognized as expenses when incurred.

2.13. Property, Plant and Equipment and Investment Property

Property, plant and equipment and investment property are stated at cost less accumulated depreciation and impairment losses, if any.

Costs include all expenses directly related to purchase of property, plant and equipment.

Subsequent expenditures are included in the asset's carrying amount or are recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance costs are charged to income statement of the financial period in which they are incurred.

The Group has investment property held to earn rental income or capital appreciation. Investment property is measured at cost less accumulated depreciation and impairment losses, if any.

Depreciation is provided for on a straight-line basis to the cost of fixed assets, using the following prescribed annual rates, in order to write them off over their useful lives:

Buildings	40 years
Computer equipment	up to 4 years
Other equipment	5 to 10 years

Changes in the expected useful lives of assets are accounted for as changes in the accounting estimates.

Calculation of depreciation of property and equipment commences at the beginning of month following the month when an asset is placed into use. Assets under construction are not depreciated. The depreciation charge is recognized as an expense for the period in which incurred.

Leasehold improvements are depreciated over the period of usage pursuant to the relevant lease contracts.

Gains from the disposal of property and equipment are credited directly to other income, whereas any losses arising on the disposal of property and equipment are charged to other operating expenses.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.14. Impairment of Non-Financial Assets

In accordance with the adopted accounting policy, at each reporting date, the Group's management reviews the carrying amounts of the Group's intangible assets and property, plant and equipment. If there is any indication that such assets have been impaired, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. If the recoverable amount of an asset is estimated to be less than its carrying value, the carrying amount of the asset is reduced to its recoverable amount, being the higher of an asset's fair value less costs to sell and value in use. Impairment losses, representing a difference between the carrying amount and the recoverable amount of tangible and intangible assets, are recognized in the income statement as required by IAS 36 "Impairment of Assets".

Non-financial assets (other than goodwill) that have suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

2.15. Leases

The determination of whether an arrangement is a lease, or contains lease elements, is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and whether the arrangement transfers the right to use the assets.

(a) Finance Lease – the Group as a Lessee

Finance leases, which transfer to the Group substantially all the risks and rewards incidental to ownership of the leased item, are capitalized at the inception of the lease at the lower of the fair value of the leased asset or the present value of the minimum lease payments and included in property and equipment with the corresponding liability to the lessor included in other liabilities.

Leased assets are depreciated over the shorter of the estimated useful life of the assets and the lease term, if there is no reasonable certainty that the Group will obtain ownership by the end of the lease term.

Lease payments are apportioned between the cost of financing and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Cost of financing is charged directly in the income statement as an interest expense.

(b) Operating Lease – the Group as Lessee

A lease is classified as an operating lease if it does not transfer to the Group substantially all the risks and rewards incidental to ownership.

Payments made under operating leases are charged to other operating expenses in the income statement (when they occur) on a straight-line basis over the period of the lease.

2.16. Provisions, Contingent Liabilities and Contingent Assets

Provisions are recognized when the Group has a present obligation (legal or constructive) as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. In order to be maintained, the best possible estimates of provisions are considered, determined and, if necessary, adjusted at each reporting date. Provisions are measured at the present value of estimated future cash outflows necessary to settle the liabilities arising thereof, using the discount rate which reflects the current market estimate of the value of money.

When the outflow of the economic benefits is no longer probable in order to settle legal or constructive liabilities, provisions are reversed by cancelation of the current year's expenses, i.e., reversed to income if the provision was made in the previous period. Provisions are taken into account in accordance with their type and they can be used only for the expenses they were initially recognized for. Provisions are not recognized for future operating losses.

Contingent liabilities are not recognized in the financial statements. They are disclosed in notes to the financial statements, unless the possibility of an outflow of resources embodying economic benefits is remote.

Contingent assets are not recognized in the financial statements. They are disclosed in notes to the financial statements if an inflow of resources embodying economic benefits is probable.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.17. Employee Benefits

(a) Employee social Security Taxes and Contributions – Defined Benefit Plans

In accordance with the Republic of Serbia regulatory requirements, the Group is obligated to pay contributions to tax authorities and to various state social security funds, which guarantee social security insurance benefits to employees. These obligations involve the payment of taxes and contributions on behalf of the employee, by the employer, in the amounts computed by applying the specific, legally prescribed rates. The Group is also legally obligated to withhold contributions from gross salaries to employees, and on behalf of its employees, to transfer the withheld portions directly to government funds. The Group has no legal obligation to pay further benefits due to its employees by the Pension Fund of the Republic of Serbia upon their retirement. These contributions payable on behalf of the employee and employer are charged to expenses in the period in which they arise.

(b) Other Employee Benefits – Retirement Benefits and Jubilee Awards

In accordance with the Labour Law and Collective Bargaining Agreement the Group is obligated to pay its vesting employees retirement benefits in the amount of three average monthly salaries paid in the Republic of Serbia in the month prior to the month of the retirement according to the most recent data published by the Republic of Serbia Statistical Office or three average salaries paid by the Group in the month prior to the month of the retirement, or 3 monthly salaries of the employee prior to the month of the retirement, whichever arrangement is most favourable for the retiree.

In addition, in accordance with the Collective Bargaining Agreement, employees are entitled to jubilee awards for ten, twenty, thirty and forty consecutive years of service with the Group. Jubilee awards are paid in the respective amounts of one, two or three average salaries paid by the Group in the month prior to the date of payment, depending on duration of the continuous service with the employer.

Expenses and liabilities for the plans are not funded. Liabilities for benefits and related expenses are recognized in the amount of present value of estimated future cash flows using the actuarial projected unit credit method.

Actuarial gains and losses and past service costs are recognized in the income statement when realized/incurred, while actuarial gains and losses in respect of retirement benefits upon retirement are recognized in other comprehensive income.

(c) Short-Term Compensated Absences

Accumulating compensated absences (annual vacation leaves) may be carried forward and used in future periods if the current period's entitlement is not used in full. Expenses for compensated absences are recognized at the amount the Group expects to pay as a result of the unused entitlement that has accumulated at the reporting date. In the case of non-accumulating compensated absences, an obligation or expense is recognized when the absences occur.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.18. Financial Guarantees

In the ordinary course of business, the Group issues financial guarantees, consisting of payment guarantees and performance bonds, letters of credit, acceptances and other warranties. Financial guarantees are contracts which obligate the issuer of a guarantee to perform the payment or compensate the loss to the holder of a guarantee, incurred if a certain client fails to settle its liabilities in due time as required under the terms of the contract.

Financial guarantees are initially recognized in the financial statements at fair value as at the date the guarantee is issued. Subsequent to initial recognition, the Group's liability under each guarantee is measured at the higher of the amortized premium and the best estimate of expenditure required to settle any financial obligations arising as a result of the guarantee.

Any increase in the liability relating to the financial guarantees is recognized in the income statement. The premium received is recognized in the income statement within the fee and commission income on a straight-line basis over the life of the guarantee.

The contractual guarantees are contracts that provide compensation if the other party fails to fulfil its contractual obligation. Such contracts are transferred, in addition to the credit and non-financial risks of execution. Performance guarantees are initially recognized at fair value, which is usually proven by the amount of compensation received. This amount is amortized diligently during the term of the contract. At the end of each reporting period, performance guarantees contracts are measured in excess of (i) the unamortised amount at initial recognition and (ii) the best estimate of the cost of the needs for the settlement of the contract at the end of the reporting period discounted to the present value.

2.19. Assets acquired through receivables collection

The Group assumes assets (collaterals) as a form of collection in cases of lending with problems in repayment. The basic reasons are to enable collateral control and protect collateral value in illiquid or problematic markets by setting the market base and, as a defence strategy, a strategy against losing property at auction at an inadequate price. The conversion of bad placements into tangible assets is also seen as a measure to improve the cost control per Group and to avoid further deterioration of value.

Assets acquired in such a way can be classified as:

- 1) Tangible assets held by the Group for their use (IAS 16, Assets, plant and equipment)
- 2) Investment property (IAS 40 Investment Property)
- 3) Assets acquired through collecting receivables (IAS 2 Inventory)
- 4) Fixed assets held for sale (IFRS 5)

Assets acquired through collecting receivables are recorded at the purchase price in RSD.

Tangible assets of the Group used by the Group are recorded at cost and depreciated in accordance with the Group's Accounting Policy and the IFRS Accounting Manual Erste Bank ad Novi Sad

An investment property is a property owned by the owner for the purpose of generating rental income. The original investment is recognized at cost and amortized in accordance with the Group's Accounting Policy and the IFRS Accounting Manual Erste Bank ad Novi Sad

In accordance with IAS 2, inventories are valued at the lower of the following two values, purchase price / cost and net realizable value (selling prices less for the cost of sales).

From the balance sheet date, the Group's management analyses the value of the inventory according to which the assets of the Group are disclosed. If there is an indication that a property is impaired, the recoverable amount of the asset is estimated to determine the amount of the impairment. If it is estimated that the recoverable amount of the property is lower than the value at which the property is disclosed, the present value of such assets is reduced to the amount of the realisable value.

The Risk Management Department performs evaluation. The write-offs of inventories to the net generated value, as well as the losses of inventories, are recognized as the expense of the period during which the write-off occurred and the occurrence of the loss.

Fixed assets intended for sale are valued at a lower value than the carrying amount that would have been classified as held for sale (cost) and fair value less costs to sell. These assets are not depreciated because this classification implies fast and certain sale.

If, during the holding of assets, the criteria for the classification of assets for sale are not met, it is necessary to reclassify and adjust its carrying amount and effects recognized in the income statement for the period when the reclassification occurred.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.20. Taxes and Contributions

(a) Income Taxes

Current Income Tax

Current income tax represents an amount calculated in accordance with the Republic of Serbia Corporate Income Tax Law. During the year, the Group pays income tax in advance in monthly instalments determined on the basis of the prior year income tax return. The ultimate tax base to which the prescribed income tax rate of 15% is applied is determined in the Group's income tax statement and reported in the annual tax return.

In order to arrive at the taxable profit, the accounting profit is adjusted for certain permanent differences and reduced for certain investments made during the year, as shown in the tax return. The tax return is submitted to the tax authorities within 180 days after expiry date of the financial year, i.e. until 31 December of the following year.

Taxpayers that had acquired the entitlement to a tax credit for capital expenditures up to 2014 in accordance with the Republic of Serbia Corporate Income Tax Law may reduce up to 33% of the calculated income tax. The unused portion of the tax credit may be carried forward and used against the income tax of the future periods but only for a duration of no longer than ten ensuing years, or up to the amount of the tax credit carried forward.

The tax regulations in the Republic of Serbia do not envisage that any tax losses of the current period be used to recover taxes paid within a specific carry back period. However, any current year losses may be used to reduce or eliminate taxes to be paid in future periods, but only for a duration of no longer than five ensuing years.

Deferred Income Taxes

Deferred income taxes are provided using the balance sheet liability method for the temporary differences arising between the tax bases of assets and liabilities and their carrying values in the financial statements. The tax rate used to calculate deferred tax amounts equals 15%.

Deferred tax liabilities are recognized for all taxable temporary differences, except where the deferred tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and in respect of taxable temporary differences associated with investments in subsidiaries and associates, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognized for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilized except where the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and in respect of deductible temporary differences associated with investments in subsidiaries and associates when deferred tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized. Unrecognized deferred tax assets are reassessed at each balance sheet date and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Current and deferred taxes are recognized as income or expenses and are included in the net profit/ (loss) for the period.

Deferred income taxes related to items that are recorded directly in equity are also recognized in equity.

(b) Indirect Taxes and Contributions

Indirect taxes and contributions include property taxes, value added tax, payroll contributions charged to the employer and various other taxes, contributions and duties payable under the republic and municipal tax regulations. These are included under operating and other expenses within the income statement.

2.21. Segment Reporting

The Group's management monitors operating segments in accordance with the methodology and segmentation defined at the level of Erste Group and on such basis makes decisions about, allocates resources to and assesses the performance of the individual segments. Segment reporting is performed and the report is prepared in compliance with FINREP reporting methodology used in Erste Group where there are departures within certain items from the result stated using the local NBS methodology.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.22. Managed Funds

The funds that the Group manages on behalf of and for the account of third parties are disclosed within off-balance sheet items. The Group bears no risk in respect of such funds.

2.21. Reclassification of comparative information

During the preparation of these financial statements, the Group became aware that as at 31 December 2016 an amount of RSD 340 thousand was erroneously classified in Loans and receivables to customers instead of Loans and receivables to banks and other financial institutions, and that amount of RSD 9,612,501 thousand was erroneously classified in Deposits and other liabilities to other customers instead of Deposits and other liabilities to banks, other financial institutions and Central Bank.

The amounts represent receivables and liabilities from credit arrangements with European Investment Bank (EIB) and European Bank for Reconstruction and Development (EBRD).

These financial statements were restated to reclassify this amount in the balance sheet as of 31 December 2016. In addition, the third statement of financial position as of 1 January 2016 is presented in these financial statements as a result of the above described changes in presentation, in which the amount of RSD 8,676,882 thousand has been reclassified from Deposits and other liabilities to other customers to Deposits and other liabilities to banks, other financial institutions and Central Bank.

3. KEY ACCOUNTING ESTIMATES AND JUDGMENTS

The preparation and presentation of the financial statements requires the Group's management to make best estimates and reasonable assumptions that influence the assets and liabilities amounts, as well as the disclosure of contingent liabilities and receivables as of the date of preparation of the financial statements, and the income and expenses arising during the accounting period.

These estimations and assumptions are based on information available, as of the date of preparation of the financial statements. Actual results may vary from these estimates. Estimates and assumptions are subject to constant review and when adjustments become necessary, they are stated within the income statement for periods in which they became known.

What follows are the key assumptions in respect of the future events and other sources of estimations, uncertainties as of the balance sheet date which represent risk from material adjustments to the amounts of balance sheet items in the following fiscal year.

(a) Impairment of loans and receivables

The Group assesses at each reporting date whether there is objective evidence that the value of a financial asset or group of financial assets has suffered impairment. A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

With regards to the assessment of impairment losses on loans, the Group reviews the credit portfolio at least on a monthly basis for collective impairment assessment (whether the loans are in the default status or not). Individual impairment assessment is performed in accordance with the changes in assumptions for calculation of the future cash flows. These assumptions are reviewed at least quarterly.

In the process of determining whether an impairment loss needs to be accounted for within the income statement, the Group assesses whether there is reliable evidence showing a measurable decrease in the estimated future cash flows from the credit portfolio before the impairment, which can be identified within individual loans comprised in the portfolio. The Group makes assessment based on its experience with losses incurred on loans from prior periods for all assets susceptible to credit risk and showing evidence of impairment similar to the one that existed in the credit portfolio at the time of planning future cash flows. The methodology and assumptions used in the assessment of amounts and time of future cash flows are subject to regular reviews with the aim to decrease differences between the estimated and actually incurred losses.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

3. KEY ACCOUNTING ESTIMATES AND JUDGMENTS (continued)

(a) Impairment of Financial Assets (continued)

The Group reviews its loan portfolio in respect of possible impairment (impairment) at least on a quarterly basis. In order to determine whether any impairment loss should be recognised in the income statement, the Group assesses whether there is any evidence that would indicate any measurable impairment of the estimated expected cash flows associated with the loan portfolio. Methodology and assumptions are regularly reviewed (based on which the estimated amounts of cash flows are determined and their estimated period). Impairment losses on individually significant receivables are based on estimates of discounted future cash flows of individual receivables, taking into account the repayment and realisation of any property held as collateral on the basis of such receivables. If the present value of the estimated cash flows for portfolio loans and receivables deemed impaired, changes of +/- 10%, the estimated value of loans and receivables would either be reduced by RSD 193,503 thousand or increase RSD 170,350 thousand respectively. This estimate was made for a portfolio of impaired individually significant loans and receivables on the basis of future cash flows based on repayment and collection from collateral.

(b) Determining the Fair Value of Financial Instruments

The fair value of financial instruments traded on an active market at the reporting date are based on the quoted market bid and ask prices, before the decrease by transaction costs. The fair value of financial instruments which are not listed on an active market are determined using adequate measurement techniques including techniques of net present value, comparison with similar instruments for which there are market prices and other relevant models.

When market inputs are unavailable, these are determined through assessments that include a certain degree of judgments in the fair value assessment. Models of estimates reflect the current market situation at the date of assessment and do not have to correspond to the market terms before or after the date of measuring. Hence, measurement techniques are revised periodically so they would best reflect current market terms.

Detailed disclosure is found in Note 32.4 (sensitivity limits) and 32.10 (fair valuation and levels).

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
4. INTEREST INCOME AND EXPENSES

	2017	RSD thousand 2016
Interest income		
– Banks	142,972	150,880
– Public companies	125,565	163,358
– Corporate customers	2,361,768	2,311,482
– Entrepreneurs	73,669	59,742
– Public sector	1,591,203	1,383,649
– Retail customers	3,364,614	3,064,138
– Non-residents	35,131	25,821
– Agricultural producers	19,968	27,110
– Other customers	25,218	53,099
Total	7,740,108	7,239,279
Interest expenses		
– Banks	369,320	365,093
– Public companies	29,432	10,039
– Corporate customers	74,380	121,399
– Entrepreneurs	1,880	2,281
– Public sector	162,678	110,244
– Retail customers	131,341	221,151
– Non-residents	390,589	386,929
– Other customers	226,546	100,797
Total	1,386,166	1,317,933
Net interest income	6,353,942	5,921,346

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
4. INTEREST INCOME AND EXPENSES (continued)

Interest income and expenses per classes of financial instruments are presented as follows:

	2017	RSD thousand 2016
Interest income		
Cash and cash funds held with the central bank	116,253	109,311
Bonds and other securities with fixed yield – held to maturity	742,723	755,984
Bonds and other securities with fixed yield – available for sale	484,189	333,918
Bonds and other securities with fixed yield – trading assets	289,977	248,708
Placements and receivables due from customers	5,293,316	5,148,623
Placements and receivables due from financial organizations	24,260	8,105
Interest-bearing swap	26,952	11,584
Other interest income	519,600	432,262
Per deposits	178	-
Per other placements	242,660	190,784
Total	7,740,108	7,239,279
Interest expenses		
Subordinated liabilities	59,197	68,529
Deposits due to banks	320,003	328,517
Deposits due to customers	739,197	719,454
Securities available for sale	40,089	24,566
Securities held to maturity	96,613	74,131
Interest-bearing swap	20,805	9,945
Per borrowings	109,789	92,223
Per other liabilities	473	569
Total	1,386,166	1,317,933
Net interest income	6,353,942	5,921,346

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
5. FEE AND COMMISSION INCOME AND EXPENSES

	2017	RSD thousand 2016
Fee and commission income		
Domestic and foreign payment transaction services	1,293,211	1,205,964
Lending activities	3,805	78,429
Deposits operation	720,980	619,294
Payment cards operations	51,436	53,923
Guarantees and other sureties	135,558	123,984
Other fees and commissions	89,664	106,341
Total	2,294,654	2,187,934
Fee and commission expenses		
Domestic and foreign payment transaction services	501,746	433,193
Other fees and commissions	286,145	270,719
Total	787,891	703,912
Net fee and commission income	1,506,763	1,484,022

6. NET GAINS ON FINANCIAL ASSETS HELD FOR TRADING

	2017	RSD thousand 2016
Gains on financial assets held for trading		
Gains on the sale of securities and other financial assets	95,519	77,744
Gains on the fair value adjustments of securities and other financial assets	161,649	198,002
Gains on the fair value adjustment of derivatives	491,972	302,740
Total	749,140	578,486
Losses on financial assets held for trading		
Losses on the sale of securities and other financial assets	927	4,425
Losses on the fair value adjustments of securities and other financial assets	139,407	186,597
Losses on the fair value adjustment of derivatives	327,502	188,507
Total	467,836	379,529
Net gains on financial assets held for trading	281,304	198,957

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
7. NET INCOME FROM HEDGING

	2017	RSD thousand 2016
Gain from hedging		
Income of changes in value of investments and receivables	2,715	2,137
Total	2,715	2,137
Losses from hedging		
Expense of changes in value of investments and receivable	648	899
Total	648	899
Net gains from hedging	2,067	1,238

Net gains on hedging is the result of changes in value of investments that are contracted to follow the growth of retail prices.

8. NET FOREIGN EXCHANGE GAINS AND POSITIVE CURRENCY CLAUSE EFFECTS

	2017	RSD thousand 2016
Positive foreign exchange difference	9,572,591	4,911,385
Negative foreign exchange difference	(6,159,269)	(5,621,476)
Positive currency clause effects	973,216	1,834,619
Negative currency clause effects	(4,172,540)	(920,033)
Net Income of Foreign Exchange and currency clause effects	213,998	204,495

9. OTHER OPERATING INCOME

	2017	RSD thousand 2016
Other income from operating activities	63,111	88,977
Income from reversal of unused provisions for bonuses	2,736	20,290
Income from reversal of unused other provisions	1,279	48,475
Income from sale of buildings	23,936	17,352
Income from sale of equipment - cars	21,424	-
Income from sale of problematic receivables	83,532	64,241
Income from sale of real estate held for sale	20,663	-
Other operating income	34,690	31,925
Income from changes in value of financial liabilities	-	717
Income from changes in value of fixed assets, investment property and intangible assets	2,712	277
Total	254,083	272,254

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
10. NET INCOME/(EXPENSES) FROM IMPAIRMENT ON FINANCIAL ASSETS AND CREDIT RISK-WEIGHTED OFF-BALANCE SHEET ITEMS

	2017	RSD thousand 2016
Income from reduction of impairment of financial assets and credit risky off-balance sheet items		
Income from reversal of indirect impairment of on-balance sheet items	7,475,707	9,984,342
Income from reversal of provision for off-balance sheet items	2,430,790	2,824,067
Total	9,906,497	12,808,409
Expense from reduction of impairment of financial assets and credit risky off-balance sheet items		
Expense from reversal of impairment losses of on-balance sheet items	7,379,374	10,520,753
Net income/(expense) from reversal of provision for off-balance sheet items	2,485,813	2,893,367
Total	9,865,187	13,414,120
Net income/(expense) from impairment of financial assets and credit risky off-balance sheet items	41,310	(605,711)

10.a NET INCOME/(EXPENSES) FROM IMPAIRMENT OF FINANCIAL ASSETS AND CREDIT RISK-WEIGHTED OFF-BALANCE SHEET ITEMS

	2017	RSD thousand 2016
Expenses from indirect impairment of financial assets and provisions		
Expense from indirect impairment of on- balance sheet items:		
– Receivables for financial instruments held by maturity (Note 18)	(45,434)	-
– Receivables for financial instruments available for sale (Note 17)	(4)	-
– Loans and receivables banks and other financial institutions (Note 19(b))	(6,539)	(6,242)
– Loans and receivables to customers (Note 20)	(2,455,390)	(3,515,353)
– Other assets (Note 22)	(80,695)	(42,638)
	(2,588,062)	(3,564,233)
Provisions for losses of off-balance sheet assets (Note 27)	(2,485,813)	(2,893,367)
Total expenses from impairment of financial assets and credit risk-weighted off-balance sheet items	(5,073,875)	(6,457,600)
Income from the impairment of financial placements and credit risk-weighted off-balance sheet items		
Income from indirect impairment of on-balance sheet items:		
– Receivables for financial instruments held by maturity	-	-
– Receivables for financial instruments available for sale (Note 17)	924	288
– Loans and receivables to banks and other financial institutions (Note 19(b))	5,853	9,181
– Loans and receivables to customers (Note 20)	2,647,829	2,936,144
– Other assets (Note 22)	28,428	32,972
	2,683,034	2,978,586
Provisions for losses on off-balance sheet assets (Note 27)	2,430,790	2,824,067
Total income from impairment of financial assets and credit risk-weighted off-balance sheet items	5,511,824	5,802,653
Net income/(expenses) from the impairment of financial placements and credit risk-weighted off-balance sheet items	39,949	(654,947)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
11. COST OF SALARIES, CONTRIBUTIONS AND OTHER PERSONNEL EXPENSE

	2017	RSD thousand 2016
Cost of net salaries	1,253,054	1,181,830
The costs of taxes and contributions payable by employee	475,594	449,026
Redundancy costs, jubilee awards, bonuses and reimbursements	234,123	214,555
Other personnel expense	43,435	24,665
Total	2,006,206	1,870,076

12. DEPRECIATION COSTS

	2017	RSD thousand 2016
Depreciation expense:		
– Tangible assets (Note 21)	166,309	108,153
– Intangible assets (Note 21)	127,245	158,773
Total	293,554	266,926

13. OTHER EXPENSES

	2017	2016
Professional services	1,189,064	992,665
Donations and sponsorships	29,520	40,568
Advertising and marketing	264,649	243,067
Post and Telecommunication services	57,243	63,308
Insurance premiums	426,394	358,832
Rental cost	348,136	402,725
Material costs	132,700	110,101
Taxes and contributions	111,006	87,166
Maintenance of tangible assets and software	379,977	277,201
Losses on sale and disposal of fixed and intangible assets	9,077	723
Payroll contributions payable by employer	285,092	261,154
Per diems and travel expenses	76,588	84,306
Education and counselling	47,323	21,017
Other expenses	115,623	187,065
Total	3,472,391	3,129,899

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

14. INCOME TAXES

(a) Components of Income Tax

Total tax (expense)/benefit is comprised of:

	2017	RSD thousand 2016
Current income tax	(116,319)	(11,739)
Income from deferred tax assets and decrease of deferred tax liabilities	39	1,840
Loss from deferred tax assets and increase of deferred tax liabilities	(43,015)	(90,186)
Total	(209,295)	(100,085)

(b) Reconciliation of the Total Tax Expense disclosed in the Income Statement and Profit Before Tax Multiplied by the Statutory Income Tax Rate

	2017	RSD thousand 2016
Profit before tax	2,881,317	2,209,701
Income tax at the rate of 15%	432,198	331,456
Tax effects of expenses not recognized for the tax purposes	48,914	17,725
Tax credits for investment in fixed assets	(30,821)	(1,086)
Recognition of deferred tax assets with respect to tax loss carry forwards	-	(136,213)
Non-taxable income (interest on securities issued by the Republic of Serbia, the autonomous province, LS or NBS)		
interest on securities issued by the Republic of Serbia, the autonomous province, LS or NBS)	(241,841)	(203,433)
Other	846	93,145
Total (expense)/income tax reported in the Income Statement	3,090,613	2,125,005
Effective tax rate	107.26%	-96.17%

(c) Deferred Tax Components

	RSD thousand	
	31 December 2017	
	Temporary difference amount	Deferred tax amount
Deductible temporary difference for difference between the carrying value and tax base value of fixed assets – deferred tax assets	53,741	8,061
Deductible temporary difference for adjustment of securities to fair value – deferred tax liabilities	(448,441)	(67,266)
Deductible temporary difference for prior years' tax loss carryforwards – deferred tax assets	-	-
Deductible temporary difference for provisions for litigation - deferred tax assets	175,183	26,277
Deductible temporary difference for impairment losses to be recognized for tax purposes in the ensuing year – deferred tax assets	1,292	194
Deductible temporary difference for provisions for jubilee awards - deferred tax assets	122,805	18,421
Deductible temporary difference for provisions for retirement benefits - deferred tax assets	89,374	13,406
Total balance as at December 31	(6,047)	(907)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
14. INCOME TAXES (continued)**(c) Deferred Tax Components (continued)****31 December 2016**

	Temporary difference amount	Deferred tax amount
Deductible temporary difference per difference between the carrying value and tax base of fixed assets – deferred tax assets	71,139	10,671
Deductible temporary difference per adjustment of securities to fair value – deferred tax liabilities	(303,403)	(45,510)
Deductible temporary difference per prior years' tax loss carryforwards – deferred tax assets	280,872	42,131
Deductible temporary difference for impairment losses to be recognized for tax purposes in the ensuing year – deferred tax assets	473	71
Deductible temporary difference for provisions for litigation - deferred tax assets	176,377	26,457
Deductible temporary difference for provisions for jubilee awards - deferred tax assets	102,977	15,447
Deductible temporary difference for provisions for retirement benefits - deferred tax assets	83,197	12,480
Total balance as at December 31	411,632	61,745

(d) Changes in deferred taxes

	2017	RSD thousand 2016
Balance of deferred tax assets as at January 1	61,745	161,764
The effect of temporary tax differences credited to the Income Statement	(42,976)	(88,346)
The effect of temporary tax differences credited to the capital	(21,756)	(11,673)
Balance of deferred tax assets/(liabilities) as at December 31	(2,987)	61.745

(e) Tax credit carried forward, expiring in ensuing years

	Amount 31 Dec 2017	Final Year of Use	RSD thousand Amount 31 Dec 2016
based on of unused transferable tax credit for investment in fixed assets	-	-	3,712
Per tax losses incurred after 1 January 2014	-	-	280,872

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
15. CASH AND CASH FUNDS HELD WITH THE CENTRAL BANK

	31 Dec 2017	RSD thousand 31 Dec 2016
In RSD		
Current account	8,681,382	8,276,530
Cash on hand	1,610,883	1,441,409
	10,292,265	9,717,939
In foreign currency		
Cash on hand	1,188,011	1,124,746
Obligatory foreign currency reserve held with NBS	9,293,751	8,403,985
	10,481,762	9,528,731
 Total receivables	 20,774,027	 19,246,670
Value correction	<u> </u>	<u> </u>
Balance at 31 December	20,774,027	19,246,670

Obligatory reserve represents the minimum reserve in RSD set aside in accordance with the National Bank of Serbia on mandatory reserves with the National Bank of Serbia ("Official Gazette of the Republic of Serbia", no. 3/2011, 31/2012, 57/2012, 78/2012, 87/2012, 107/2012, 62/2013, 125/2014, 135/2014, 4/2015, 78/2015 and 102/2015), which provides that banks calculate obligatory Reserves at the rate of 5% on the average daily balance of local currency liabilities with agreed maturity up to two years, or at the rate of 0% on the average daily balance local currency liabilities with agreed maturity of over two years, during one calendar month.

During the period the Bank is required to maintain the average daily balance of required reserve on its bank account.

The calculated obligatory reserve whose level has to be maintained on the bank account for the period from 18 December 2017 to 17 January 2018 amounted to RSD 7,002,670 thousand.

The average interest rate on the amount of bank reserves during the year 2017 amounted to 1.75% per annum.

The obligatory foreign currency reserve represents the minimum foreign currency reserve set aside in accordance with the NBS Decision on Required Reserves of Banks with the National Bank of Serbia (Official Gazette of RS, nos. 3/11, 31/12, 57/12, 78/12, 87/12, 107/12, 62/13, 125/14, 135/14, 4/2015, 78/2015 and 102/2015), which prescribes that banks calculate the obligatory foreign currency reserve at the following rates: 20% on the average daily balance of foreign currency liabilities maturing within 2 years, and exceptionally at the rate of 100% on the portion of RSD liabilities indexed to a currency clause maturing within 2 years; 13% on the average daily balance of foreign currency liabilities with maturities of over 2 years, and exceptionally at the rate of 100% on the portion of RSD liabilities indexed to a currency clause with maturities of over 2 years during a calendar month.

The calculated foreign currency obligatory reserves for the period from 18 December 2017 to 17 January 2018 amounted to EUR 78,446 thousand.

The National Bank of Serbia does not pay interest on the amount of the average balance of the allocated foreign currency reserve.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

16. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS FOR TRADING

	31 Dec 2017	RSD thousand 31 Dec 2016
In RSD		
Financial assets at fair value through profit or loss		
- treasury bills	-	196,192
- bonds	4,623,991	3,669,730
- receivables arising from derivatives held for trading	6,154	92,822
	4,630,145	3,958,744
In foreign currency		
Financial assets at fair value through profit or loss		
- treasury bills	-	1,964,904
- bonds	6,837,548	7,065,377
- receivables arising from derivatives held for trading	71,771	59,332
	6,909,319	9,089,613
Balance as at 31 December	11,539,464	13,048,357

17. FINANCIAL ASSETS AVAILABLE FOR SALE

	31 Dec 2017	RSD thousand 31 Dec 2016
In RSD		
Financial assets available for sale		
- treasury bills	-	237,537
- bonds	5,438,554	2,015,011
- share in capital	28,804	136,084
	5,512,358	2,388,632
In foreign currency		
Financial assets available for sale		
- treasury bills	6,804,487	4,879,783
- other securities available for sale	171,755	34,943
	6,976,242	4,914,726
Gross financial assets available for sale	12,488,600	7,303,358
Less: Allowance for impairment	(7)	(120,656)
Balance as at	12,488,593	7,182,702

Movements in allowance for impairment during the year are as follows:

	31 Dec 2017	RSD thousand 31 Dec 2016
Balance as at 1 January	120,656	119,448
New provisions	4	-
Reversal of provisions	(924)	(288)
Write off for provisions	(57,289)	-
Recalculating AfS on fair value	(65,965)	-
Foreign exchange differences	3,235	1,496
Balance as at 31 December	7	120,656

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
18. FINANCIAL ASSETS HELD TO MATURITY

	31 Dec 2017	RSD thousand 31 Dec 2016
In RSD		
Financial assets held to maturity:		
- treasury bills	7,861,382	8,635,103
- bonds	<u>7,861,382</u>	<u>8,635,103</u>
In foreign currency		
Financial assets held to maturity:		
- bonds	468.487	-
	<u>468.487</u>	<u>-</u>
Total financial assets	<u>8,329,869</u>	<u>8,635,103</u>
Less: Allowance for impairment		(45,417)
-		
Balance as at 31 December		<u>8,284,452</u>
<u>8,635,103</u>		

Movements in allowance for impairment during the year are as follows:

	31 Dec 2017	RSD thousand 31 Dec 2016
Balance as at 1 January 2017	-	-
New provisions	45,434	-
Reversal of provisions	-	-
Foreign exchange differences	(17)	-
Balance as at 31 December	<u>45,417</u>	<u>-</u>

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

19. LOANS AND RECEIVABLES TO BANKS AND OTHER FINANCIAL INSTITUTIONS

	31 December 2017			31 December 2016			RSD thousand
	Short-term	Long-term	Total	Short-term	Long-term	Total	
In RSD							
Loans	-	7,104	7,104	25,087	383	25,470	
Deposits	-	-	-	8,008	-	8,008	
	-	7,104	7,104	32,095	383	33,478	
Foreign currency							
Foreign currency bank account	1,151,048	-	1,151,048	458,769	-	458,769	
Loans	2,690	322,234	324,924	78,566	209,531	288,097	
Deposits	709,981	-	709,981	427,587	-	427,587	
Other placements	18,600	-	18,600	14,428	-	14,428	
	1,882,319	322,234	2,204,553	979,350	209,531	1,188,881	
Gross loans and receivables	1,882,319	329,338	2,211,657	1,102,445	209,914	1,222,359	
Less: Allowance for impairment			(12,687)			(12,294)	
			(12,687)			(12,294)	
Balance as at 31 December			2,198,970			1,209,065	

Loans with foreign currency clause are presented within loans and receivables in foreign currency.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

19. LOANS AND RECEIVABLES TO BANKS AND OTHER FINANCIAL INSTITUTIONS (continued)

(a) Overview by types of user of loans and deposits

	31 December 2017			31 December 2016			RSD thousand
	Short-term	Long-term	Total	Short-term	Long-term	Total	
In RSD							
Insurance companies	-	182	182	-	175	175	
Auxiliary activities of financial services and insurance	-	6,702	6,702	-	71	71	
Other loan and financing services	-	58	58	25,125	99	25,224	
Foreign banks	-	162	162	8,008	-	8,008	
	-	7,104	7,104	33,133	345	33,478	
Foreign currency							
Domestic Banks	639.971	-	639.971	175,722	-	175,722	
Finance lease	-	154.022	154.022	-	208,879	208,879	
Auxiliary activities of financial services and insurance	37.300	168.212	205.512	19,367	652	20,019	
Other loan and financing services	-	-	-	76,369	-	76,369	
Foreign banks	1.151.048	-	1.151.048	707,892	-	707,892	
	1.882.319	322.234	2.204.553	979,350	209,531	1,188,881	
Gross loans and receivables	1.882.319	329.338	2.211.657	1,012,483	209,876	1,222,359	
Less: Allowance for impairment	-	-	(12.687)	-	-	(12.294)	
Balance as at 31 December	-	-	2.198.970	-	-	1,210,065	

Loans with foreign currency clause are presented within loans and receivables in foreign currency.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
19 LOANS AND RECEIVABLES TO BANKS AND OTHER FINANCIAL INSTITUTIONS (continued)
b) Maturity of loans and receivables to banks and other financial services

Maturity of loans and receivables to banks and other financial institutions based on the remaining period on the balance sheet date to the contractual maturity date, as at 31 December 2017 and 31 December 2016, is as follows:

	31 Dec 2017	RSD thousand 31 Dec 2016
Without defined maturity	1,173,568	579,643
Under 30 days	693,977	430,680
From 1 to 3 months	-	2,160
From 3 to 12 months	13,961	-
Over 1 year	330,151	209,876
	<u>2,211,657</u>	<u>1,222,359</u>

Changes of allowance for impairment during year are presented in the following table:

	31 Dec 2017	RSD thousand 31 Dec 2016
Opening balance	10,618	13,737
New provisions	6,539	6,242
Reversal of impairment losses	(5,853)	(9,181)
Write-offs on the allowance	(76,518)	-
Foreign exchange differences	77,901	1,486
Balance as at 31 December	<u>12.687</u>	<u>12,294</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017

20. LOANS AND RECEIVABLES TO CUSTOMERS

	31 December 2017			31 December 2016			RSD thousand
	Short-term	Long-term	Total	Short-term	Long-term	Total	
In RSD							
Loans	2,234,464	23,109,007	25,343,471	1,272,822	19,233,022	20,505,844	
Other placements	2,701,462	4,138,171	6,839,633	3,311,786	3,455,348	6,767,134	
	4,935,926	27,247,178	32,183,104	4,584,608	22,688,370	27,272,978	
Foreign currency							
Loans	8,345,517	73,729,282	82,074,799	7,246,303	67,980,895	75,227,198	
Deposits	85,735	-	85,735	101,322	-	101,322	
Other placements	339,585	48,454	388,039	171,877	524,225	696,102	
	8,770,837	73,777,736	82,548,573	7,519,502	68,505,120	76,024,622	
Gross loans and receivables	13,706,763	101,024,914	114,731,677	12,104,110	91,193,490	103,297,600	
Less: Impairment allowance							
- Individual assessment			(2,068,517)			(3,056,826)	
- Collective assessment			(2,190,431)			(3,777,852)	
			(4,258,948)			(6,834,678)	
Balance as at 31 December			110,472,729			96,462,922	

Loans with foreign currency clause are presented within loans and receivables in foreign currency.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

20. LOANS AND RECEIVABLES TO CUSTOMERS (continued)

(a) Overview by types of users of loans and deposit

	31 December 2017			31 December 2016			RSD thousand
	Short-term	Long-term	Total	Short-term	Long-term	Total	
In RSD							
Holdings	-	-	-	-	687	687	
Public enterprises	380,071	767,038	1,147,109	104,478	271,415	375,893	
Other companies	3,465,244	3,571,951	7,037,195	3,266,434	3,495,533	6,761,967	
Entrepreneurs	112,508	586,021	698,529	150,760	364,516	515,276	
Public sector	763,337	2,630	765,967	676,856	624	677,480	
Retail customers	195,698	22,142,404	22,338,102	255,533	18,524,635	18,780,168	
Foreign entities	28	11,725	11,753	2	-	2	
Agriculture producers	12,798	24,605	37,403	34,902	7,827	42,729	
Other customers	6,242	140,804	147,046	95,643	23,133	118,776	
	4,935,926	27,247,178	32,183,104	4,584,608	22,688,370	27,272,978	
In foreign currency							
Holdings	-	-	-	520,947	121,590	642,537	
Public enterprises	-	2,183,335	2,183,335	4,323	2,791,685	2,796,008	
Other companies	8,364,250	42,017,895	50,382,145	6,536,719	44,787,539	51,324,258	
Entrepreneurs	65,785	600,776	666,561	41,952	388,782	430,734	
Public sector	187,407	2,663,149	2,850,556	162,832	2,313,408	2,476,240	
Retail customers	5,124	25,433,419	25,438,543	3,455	16,585,325	16,588,780	
Foreign entities	91,955	92,689	184,644	112,326	64,099	176,425	
Agriculture producers	13,637	175,784	189,421	29,602	208,086	237,688	
Other customers	42,679	610,689	653,368	107,346	1,244,606	1,351,952	
	8,770,837	73,777,736	82,548,573	7,519,502	68,505,120	76,024,622	
Gross loans and receivables	13,706,763	101,024,914	114,731,677	12,104,110	91,193,490	103,297,600	
Less: Impairment allowance							
- Individual assessment			(2.068.517)			(3.056.826)	
- Collective assessment			(2.190.431)			(3.777.852)	
			(4,258,948)			(6,834.678)	
Balance as at 31 December			110,472,729			96.462.922	

Loans with foreign currency clause are included in the review of loans and deposits in foreign currency.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
20. LOANS AND RECEIVABLES TO CUSTOMERS (continued)
b) Maturity of loans and receivables due from customers

Maturities of loans and receivables due from customers per outstanding maturity as of 31 December 2017 and 31 December 2016, in gross amount, are presented in the table below:

	31 Dec 2017	RSD thousand 31 Dec 2016
Without defined maturity	469,619	546,446
Under 30 days	269,022	221,699
From 1 to 3 months	754,074	754,615
From 3 to 12 months	12,235,607	10,581,350
Over a year	101,066,094	91,193,490
	114,794,416	103,297,600

Movements on the impairment allowance accounts during the year are presented below:

	31 Dec 2017	RSD thousand 31 Dec 2016
Balance at beginning of year	6,784,373	7,912,965
New provisions	2,455,390	3,515,353
Reversal of impairment losses	(2,647,829)	(2,936,144)
Write-offs on the allowance	(1,632,284)	(1,752,867)
Foreign exchange differences	(700,702)	95,371
Balance as at 31 December	4,258,948	6,834,678

c) Concentration of Loans and Receivables due from Banks, Other Financial Institutions and Customers

Concentration of loans and receivables due from banks, other financial institutions and customers presented in gross amounts as of 31 December 2017 and 31 December 2016 is significant with the following industries:

	31 Dec 2017	RSD thousand 31 Dec 2016
Holding companies	-	643,224
Trade	11,531,156	9,825,337
Processing industry	14,730,940	15,575,366
Construction industry	10,849,591	11,440,550
Power generation and supply	5,677,218	8,546,887
Tourism and services industry	14,160,502	12,681,838
Agriculture and food industry	2,439,537	2,314,694
Retail customers	47,880,851	35,433,052
Domestic and foreign banks and other financial institutions	2,211,901	1,222,019
Public sector	4,632,590	3,524,926
Non-resident corporate customers	91,946	112,663
Agricultural producers	224,723	280,417
Other customers	1,276,944	1,972,977
Entrepreneurs	1,235,435	946,009
	116,943,334	104,519,959

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
20. LOANS AND RECEIVABLES DUE FROM CUSTOMERS (continued)
d) Finance Lease Receivables

	<u>31 Dec 2017</u>	<u>RSD thousand 31 Dec 2016</u>
Minimum lease payments	7,341,132	6,120,111
Less: Interest receivables not matured	<u>(511,035)</u>	<u>(395,933)</u>
Finance lease receivables	<u>6,830,097</u>	<u>5,724,178</u>
Interest receivables matured	14,878	15,954
Other receivables from finance lease activities	<u>47,083</u>	<u>49,559</u>
	<u>6,892,058</u>	<u>5,789,691</u>
Less: Deferred income from finance lease origination fees	(63,557)	(50,748)
	<u>6,828,502</u>	<u>5,738,943</u>
Less: Impairment allowance of		
- finance lease receivables	(271,282)	(337,277)
- interest receivables matured	(14,857)	(15,905)
- other receivables from finance lease activities	<u>(46,895)</u>	<u>(49,123)</u>
	<u>(333,033)</u>	<u>(402,305)</u>
	<u>6,495,468</u>	<u>5,336,638</u>

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

21. PROPERTY, PLANT, EQUIPMENT, INVESTMENT PROPERTY AND INTANGIBLE ASSETS

							RSD thousand
	<u>Land and buildings</u>	<u>Equipment</u>	<u>Equipment underfinance lease</u>	<u>Investment property</u>	<u>Equipment under construction</u>	<u>Total Tangible assets</u>	<u>Intangible assets</u>
COST							
Balance as at 1 January 2016	778,086	728,112	41,108	243,633	-	1,790,938	1,136,684
Additions	-	2,987	(1,144)	-	287,464	289,307	2,473
Transfers	9,612	109,652	82,331	-	(287,464)	(85,869)	85,869
Disposal and retirement	(43,989)	(11,701)	-	-	-	(55,690)	(144)
Balance as at 31 December 2016	743,709	829,049	122,295	243,633	-	1,938,686	1,224,882
Additions	-	9,647	(3,878)	-	527,446	533,215	-
Transfers	16,322	255,193	140,326	-	(506,282)	(94,441)	101,402
Disposal and retirement	(7,385)	(77,883)	(4,570)	(243,633)	-	(333,471)	(9,225)
Balance as at 31 December 2017	752,646	1,016,006	254,173	-	21,164	2,043,989	1,317,059
ACCUMULATED DERPECIATION							
Balance as at 1 January 2016	263,694	541,810	663	5,125	-	811,291	784,859
Charge for the year (Note 12)	19,013	69,670	13,380	6,091	-	108,153	158,772
Disposal and retirement	(20,412)	(8,887)	(1,144)	-	-	(30,442)	(144)
Balance as at 31 December 2016	262,295	602,593	12,899	11,216	-	889,003	943,487
Charge for the year (Note 12)	18,494	104,185	42,471	1,159	-	166,309	127,245
Disposal and retirement	(2,201)	(70,803)	(4,561)	(12,375)	-	(89,940)	(9,225)
Balance as at 31 December 2017	278,587	635,975	50,810	-	-	965,372	1,061,507
NET BOOK VALUE							
- 31 December 2017	474,059	380,031	203,364	-	21,164	1,078,617	255,553
- 31 December 2016	481,414	226,456	109,396	232,417	-	1,049,684	281,395

There were no mortgage liens assigned over the Group's building properties to securitize repayment of borrowings. As of 31 December 2017 the net book value of the Group's equipment mostly comprised of computers and computer equipment, telecommunication equipment and office furniture. As of 31 December 2017 the net book value of the Group's intangible assets mostly comprised software and licenses. In the assessment of the Group's management, there were no indications that property, plant, equipment and intangible assets had suffered impairment as of 31 December 2017.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
22. OTHER ASSETS

	31 Dec 2017	RSD thousand 31 Dec 2016
In RSD		
<i>Financial assets:</i>		
- Receivables for accrued commission and compensation	16,212	36,233
- Receivables from sale	2,045	1,070
- Other receivables from regular business as a basis for income calculation	29,582	101,013
- Other receivables from regular business	197,165	109,365
<i>Non-financial assets:</i>		
- Advances paid	2,928	16,701
- Receivables from employees	698	1,192
- Receivables for prepaid taxes and contributions	725	725
- Inventories	93,887	59,849
- Other receivables	13,603	13,800
- Other investments	27,006	29,169
<i>Prepayments and accrued income:</i>		
- Deferred expenses of insurance premium	542,593	314,986
- Coupon interest from bonds	-	42,366
- Other prepayments	166,210	178,955
	1,092,654	905,424
In foreign currency		
<i>Other receivables:</i>		
- Receivables for accrued commission and compensation	-	18
- Receivables from sale	30,993	30,105
- Other receivables from standard operations	24	60
- Other receivables	49,202	54,057
<i>Non-financial assets:</i>		
- Advances paid	121,156	91,141
- Receivables from employees	22	1,247
- Other receivables	2,031	58,457
<i>Prepayments and accrued income:</i>		
- Other prepayments	34,552	34,576
	237,980	269,661
Gross other assets	1,330,634	1,175,085
Less: Impairment allowance	(176,523)	(310,222)
Balance as at 31 December	1,154,111	864,863

Changes of the allowances for impairment are presented in the following table:

	31 Dec 2017	RSD thousand 31 Dec 2016
Balance at beginning of period	309,750	397,187
New provisions	80,695	42,638
Reversal of impairment losses	(28,428)	(32,972)
Write-offs on the allowance	(69,703)	(67,346)
Participation adjustment to fair value	(2,140)	-
Foreign exchange differences	(113,651)	(29,285)
Balance as at 31 December	176,523	310,222

23. FINANCIAL LIABILITIES AT FAIR VALUE THROUGH PROFIT AND LOSS HELD FOR TRADING

	31 Dec 2017	RSD thousand 31 Dec 2016
In RSD		
Liabilities per derivatives held for trading	14,750	11,556
	14,750	11,556
In foreign currencies		
Liabilities per derivatives held for trading	29,708	43,134
	29,708	43,134
Balance as at 31 December	44,458	54,690

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
24. DEPOSITS AND OTHER LIABILITIES TO BANKS, OTHER FINANCIAL INSTITUTIONS AND CENTRAL BANK

	31 December 2017			31 December 2016			RSD thousand
	Short-term	Long-term	Total	Short-term	Long-term	Total	
In RSD							
<i>Deposits and borrowings</i>							
Transaction deposits	292,843	-	292,843	8,883	-	8,883	
Deposits placed for loan approved	-	247	247	-	247	247	
Earmarked deposits	86,554	-	86,554	1,075	-	1,075	
Other deposits	4,361,319	345,000	4,706,319	3,750,530	390,000	4,140,530	
Total	4,740,716	345,247	5,085,963	3,760,488	390,247	4,150,735	
In foreign currencies							
<i>Deposits and borrowings</i>							
Transaction deposits	375,863	-	375,863	871,930	-	871,930	
Deposits placed for loan approved	-	189,556	189,556	-	1,171,456	1,171,456	
Earmarked deposits	21,246	18,955	40,201	18,214	3,704	21,918	
Other deposits	6,317,658	1,512,836	7,830,494	15,631,839	1,678,180	17,310,019	
Overnight deposits	2,262,829	-	2,262,829	-	-	-	
Borrowings	2,130,419	33,916,419	36,046,838	1,733,826	26,110,695	27,844,521	
Other financial liabilities	27,963	-	27,963	57,622	-	57,622	
Total	11,135,978	35,637,766	46,773,744	18,313,431	28,964,035	47,277,466	
Balance as at 31 December	15,876,694	35,983,013	51,859,707	22,073,919	29,354,282	51,428,201	

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
**24. DEPOSITS AND OTHER LIABILITIES DUE TO BANKS, OTHER FINANCIAL INSTITUTIONS AND
THE CENTRAL BANK (Continued)**

A breakdown of other deposits per type of customer is presented in the table below:

	31 Dec 2017	RSD thousand 31 Dec 2016
Central bank	1	3
Domestic banks	6,981,815	9,309,202
Insurance companies	2,647,290	2,953,351
Pension funds	-	170,534
Finance lessors	2,567,369	1,629,846
Auxiliary activities within financial services and insurance	3,207,703	1,579,820
Trusts, investment and similar funds	-	14,672
Other crediting and financing service providers	2,855	8,448
Foreign banks	36,452,674	35,762,325
Balance as at 31 December	<u>51,859,707</u>	<u>51,428,201</u>

Foreign banks' deposits mostly relate to the deposit of Erste Group Bank AG in the amount of RSD 16,359,604 thousand and a deposit of European Investment Bank in the amount of RSD 11,094,645 thousand.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

25. DEPOSITS AND OTHER LIABILITIES DUE TO CUSTOMERS

	31 December 2017			31 December 2016			RSD thousand
	Short-term	Long-term	Total	Short-term	Long-term	Total	
In RSD							
<i>Liabilities arising from deposits and loans</i>							
Transactional deposits	17,706,708	-	17,706,708	14,335,266	-	14,335,266	
Revocable deposits			-				
Saving deposits:	532,109	542,425	1,074,534	648,934	483,830	1,132,764	
Deposits based on given loans	237,930	189,160	427,090	194,079	96,928	291,007	
Earmarked deposits	2,829,348	18,750	2,848,098	2,539,874	18,750	2,558,624	
Other deposits	6,926,343	7,359	6,933,702	4,715,869	8,900	4,724,769	
Total	28,232,438	757,694	28,990,132	22,434,022	608,408	23,042,430	
In foreign currency							
<i>Liabilities arising from deposits and loans</i>							
Transactional deposits	34,154,483	-	34,154,483	23,793,190	-	23,793,190	
Revocable deposits	-	-	-	-	-	-	
Saving deposits:	8,190,424	11,953,885	20,144,309	8,588,238	13,053,687	21,641,925	
Deposits based on given loans	103,768	2,058,284	2,162,052	477,827	2,253,017	2,730,844	
Earmarked deposits	3,259,784	314,590	3,574,374	767,393	344,020	1,111,413	
Other deposits	1,082,998	124,996	1,207,994	533,112	25,895	559,007	
Borrowings	-	1,291,788	1,291,788	-	2,100,459	2,100,459	
Other financial liabilities	456,996	-	456,996	311,561	-	311,561	
Total	47,248,453	15,743,543	62,991,996	34,471,321	17,777,078	52,248,399	
Balance as at 31 December			91,982,128			75,290,829	

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
25. DEPOSITS AND OTHER LIABILITIES TO OTHER CUSTOMERS (continued)

A breakdown of other deposits per type of customer is presented in the table below:

	31 Dec 2017	RSD thousand 31 Dec 2016
Holding companies	-	51,308
Public companies	2,057,397	965,665
Corporate customers	26,848,840	18,855,062
Public sector	2,691,673	2,152,296
Retail customers	45,729,756	40,394,298
Non-residents	2,467,769	3,851,638
Entrepreneurs	2,195,108	1,814,183
Agricultural producers	397,437	471,626
Other customers	9,594,148	6,734,753
Balance as at 31 December	91,982,128	75,290,829

26. SUBORDINATED LIABILITIES

	31 Dec 2017	RSD thousand 31 Dec 2016
In foreign currencies		
Subordinated liabilities	1,354,523	1,764,606
	1,354,523	1,764,606
Balance as at 31 December	1,354,523	1,764,606

The balance of subordinated borrowings as of December 31, 2017 and December 31, 2016 is presented in more detail in the table below, without deferred interest per subordinated liabilities:

Creditor	Currency	Loan amount	Maturity	Interest rate	31 Dec 2017	31 Dec 2016
Erste Group Bank AG, Austria	EUR	15,000,000	27 Dec 2021	3m Euribor+3.65% pa	1,353,974	1,763,890
Total		15,000,000			1,353,974	1,763,890

Subordinated liabilities relate to a subordinated long-term loan approved to the Bank by Erste GCIB Finance, Amsterdam on 27 December 2011 in the amount of EUR 15,000,000 for a period of 10 years with a 5-year grace period and interest rate equal to 3-month EURIBOR increased by 3.65% per annum. In accordance with the Agreement, the loan principal is to be repaid in 21 equal quarterly instalment, the first of which is due upon grace period expiry.

The Bank may include subordinated liabilities in its supplementary capital (Note 32.9), after the National Bank of Serbia, on the basis of the submitted documentation and the Agreement, establishes that the conditions for granting approval to include subordinate liabilities in the supplementary capital of the Bank. The National Bank of Serbia, the Banking Supervision Department, submitted the said approval on 6 December 2011, and based on the Bank's request of 7 October 2011.

On the basis of the Transfer and Transfer Agreement on 16 December 2015, the change of the creditor was made, and the new creditor of Erste Group Bank AG, Austria. All other terms of the contract have remained unchanged.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
27. PROVISIONS

	31 Dec 2017	RSD thousand 31 Dec 2016
Provisions for losses per off-balance sheet items (a)	326,073	277,482
Provisions for long-term employee benefits (b):		
– retirement benefits	76,224	83,874
– jubilee awards	111,997	106,232
Provisions for litigations (c)	185,274	172,445
Other long-term provisions	67,041	50,681
Balance as at 31 December	766,609	690,714

- (a) According to the Group's internal policy, provisions for commitments and other risk-weighted off balance sheet items (guarantees, acceptances, undrawn loan facilities etc.) are made when it is probable that an outflow of resources will be required to settle the obligation arising from the Group's commitments.

Evidence based on which the Group performs the individual assessment of impairment are: payments effected on the Group's accounts with respect to commitments arising from guarantees, bills of guarantees, etc., late payments for other liabilities, and the customers has been classified in accordance with the Group's internal classification criteria into default status category.

Individual assessment of impairment of off-balance sheet items is performed in the same manner as for the balance sheet assets. Commitments and other risk-weighted off-balance sheet items, for which the Group does not expect any outflow of resources and/or it estimates that in the case of an outflow of resources all receivables will be fully collected, the Group collectively assesses them for impairment, in a similar way as for balance sheet items, using the credit conversion factors for off-balance sheet items.

- (b) The Group also formed provisions for litigations involving the Group as a defendant, where the Group's expert team expects negative outcomes.

Movements on provision accounts during the year are provided below:

	31 Dec 2017	RSD thousand 31 Dec 2016
Provisions for losses per off-balance sheet exposures		
Balance at the beginning of the year	277,482	205,727
Provisions for the year (Note 10)	2,485,813	2,893,367
Reversal of unused provisions (Note 10)	(2,430,790)	(2,824,067)
Other movements	(6,433)	2,455
	326,072	277,482
Provisions for other long-term employee benefits		
Balance at the beginning of the year	198,088	198,586
Interest expenses and current service costs	19,177	22,403
Compensations payments during the year	(28,157)	(31,326)
Actuarial losses/(gains) on jubilee awards	10,151	983
Actuarial losses/(gains) on retirement benefits	(11,038)	2,442
Other	-	5,000
	188,221	198,088
Provisions for litigations		
Balance, beginning of year	172,445	126,600
Provisions for the year	22,141	55,506
Released during the year	(9,313)	(9,661)
	185,273	172,445
Other long-term provisions		
Balance at the beginning of the year	42,700	20,491
Provisions for the year	51,971	35,084
Released during the year	(27,628)	(12,875)
	67,043	42,700
Balance as at 31 December	766,609	690,714

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
28. OTHER LIABILITIES

	31 Dec 2017	RSD thousand 31 Dec 2016
In RSD		
<i>Non-financial liabilities:</i>		
Trade payables	4,807	2,123
Advances received	26,733	20,904
Liabilities for net salaries and benefits	6,727	194
Liabilities for taxes, contributions and other duties payable	76,186	3,769
<i>Accrued expenses and deferred revenue:</i>		
- accrued liabilities for unused annual leaves	21,078	13,952
-accrued liabilities for MBU processing	15,936	15,483
-accrued liabilities for IT services	13,753	1,085
-accruals for expenses	117,044	47,338
- other accruals	368,167	288,903
Liabilities to retailers for POS terminals	51,748	13,941
Liabilities for closing of accounts (in RSD)	21,685	18,113
Obligations from forcibly sold shares synergy - natural persons	24,414	25,514
Other liabilities	173,177	16,618
	921,455	467,938
In foreign currencies		
<i>Financial assets:</i>		
Liabilities for unpaid assets on lease	783	-
<i>Non-financial assets:</i>		
Compensation and commission fees	60	25
Suppliers	5,734	6,439
Advances received	10,634	15,414
<i>Accruals:</i>		
- other accruals	36,485	47,065
Covers by nostro remittances	27,937	71,780
Other liabilities	27,417	14,033
	109,050	154,756
Balance as at 31 December	1,030,505	622,694

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
29. EQUITY**(a) Structure of the Group's' Equity**

The total equity structure of the **Group** is presented as follows:

	31 Dec 2017	RSD thousand 31 Dec 2016
Share capital - ordinary shares	10,040,000	10,040,000
Share premium	124,475	124,475
Special Reserves for Estimated Losses	7,679,824	5,614,904
Revaluation reserves	418,346	283,968
Retained earnings	2,732,925	2,135,770
Owners without rights of control	64,856	54,892
Balance as at 31 December	21,060,426	18,254,009

/i/ Share Capital

As of 31 December 2017 the Bank's subscribed and paid in capital comprised 1,004,000 ordinary shares with the par value of RSD 10,000 per share (31 December 2016: 1,004,000 ordinary shares with the par value of RSD 10,000 per share). During 2017 and 2016 there were no changes in the share capital.

The major shareholder of the Bank is Erste Group, Vienna, with a shareholding of 74% at 31 December 2017. The shareholder structure of the Bank as of 31 December 2017 is presented below:

Shareholder	Share Count	In %
EGB CEPS HOLDING GMBH	742,960	74.00
Steiermärkische Bank und Sparkassen AG, Graz	261,040	26.00
Total	1,004,000	100.00

/ii/ Share Premium

Share premium amounting to RSD 124,475 thousand as at 31 December 2017 and 31 December 2016 resulted from a positive difference between the selling price of the shares and their nominal value.

/iii/ Reserves from Profit and Other Reserves

As of 31 December 2017 reserves from profit formed for estimated loss per risk-weighted balance sheet and off-balance sheer exposures amounted to RSD 7,679,825 thousand. As of 31 December 2016 the required reserve for estimated losses amounted to RSD 5,614,904 thousand. Pursuant to the Group Shareholder Assembly's Decision dated 31 March 2017, gains from 2016 in amount of RSD 2,064,920 thousand was allocated to other reserves.

/iv/ Revaluation Reserves

Revaluation reserves amounting to RSD 418,023 thousand as of 31 December 2017 (31 December 2016: RSD 283,703 thousand) were formed as a result of the market value adjustment of the securities available for sale, adjusted for the effects of deferred taxes arising from revaluation of these securities and the adjustment of liabilities based on the actuary calculation in accordance with IAS 19.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
30. OFF-BALANCE SHEET ITEMS

The Bank records mortgages, securities from custody operations and unwinding interest within the framework of other off-balance sheet items.

	31 Dec 2017	RSD thousand 31 Dec 2016
Managed funds (a)	640,935	696,990
Guarantees and other irrevocable commitments (b)	37,230,852	22,006,926
Other off-balance sheet items (c)	215,361,570	163,964,286
Balance as at 31 December	253,233,357	186,668,202

(a) Managed Funds

	31 Dec 2017	RSD thousand 31 Dec 2016
Investments on behalf of third parties		
In RSD		
- short-term	14,006	13,674
- long-term	626,929	683,316
Balance as at 31 December	640,935	696,990

Short-term funds managed on behalf of third parties relate to funds of the Ministry of Agriculture in the amount of RSD 8,106 thousand. Long-term funds managed on behalf of third parties relate to long-term housing loans insured with National Mortgage Insurance Corporation amounting RSD 615,923 and long-term loans to agricultural producers in the amount of RSD 10,885 thousand.

(b) Guarantees and Other Irrevocable Commitments

	31 Dec 2017	RSD thousand 31 Dec 2016
In RSD		
Payment guarantees	1,046,722	40,457
Performance bonds	4,780,880	3,810,201
Acceptances	-	872
Irrevocable commitments for undrawn loan facilities	5,567,655	2,914,003
Other off-balance items	653,801	270,741
	12,049,058	7,036,274
In foreign currencies		
Payment guarantees	1,511,097	457,393
Performance bonds	4,869,481	3,835,280
Irrevocable commitments for undrawn loan facilities	17,010,434	10,570,648
Letters of credit	187,855	53,779
Other off-balance items	1,602,927	53,552
	25,181,794	14,970,652
Balance as at 31 December	37,230,852	22,006,926

Irrevocable commitments relate to the undrawn loans approved that cannot be unilaterally cancelled such as current account overdrafts approved, corporate loans, framework loans and other irrevocable commitments.

Irrevocable commitments are usually indexed to fixed expiry dates or other provisions related to expiry. Since irrevocable commitments may expire before loans are drawn by customers, the total amount agreed upon does not represent definite future cash outflows.

The Group monitors maturity periods of credit commitments and undrawn loan facilities because longer term commitments bear a greater degree of credit risk than short-term commitments.

As at 31 December 2017, the Group's provisions for guarantees and other irrevocable commitments amounted to RSD 326,072 thousand (31 December 2016: RSD 277,482 thousand).

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

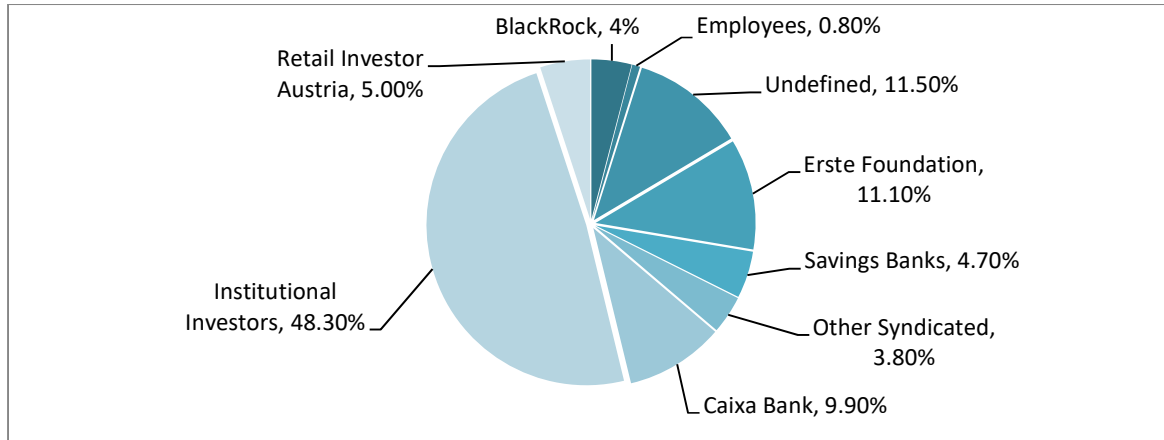
31. RELATED PARTY DISCLOSURES

In its regular business the Group has transactions with its shareholders and other related parties.

Other parties are considered as the related parties if they are under common control, or if one party controls other, or if it can make the significant impact on the other party while making financial and business decisions.

Shareholders of the Bank are Erste Group AG Wien and Steirmärkische Bank and Sparkassen AG, Graz.

Shareholders structure of Erste Group is presented below:



Long-term loans with maturity up to 5 years are taken with the interest rate of 6MEURIBOR +1.86%, or LIBOR +1.8%, while the subordinated loan taken with the interest rate of 3MEURIBOR +3.65% for 10 years.

Cross-banking business activities (overnight and short-terms loans) are being published at the prices in range from 0.29% - 11%, depending on the currency in which business is operated.

Guarantees fees with the related parties are in range from 0.98 - 1.6%.

Other transactions on the market (swap transactions, forward transactions, cash purchase), and also the transactions for which there is fee that needs to be paid and received, are being operated according to market conditions and prices out of hands.

Interest rate for deposits and other liabilities to banks and commitments are in range from 0.15% to 9.2%.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
31. RELATED PARTY DISCLOSURES (continued)

Balances of receivables and payables as of 31 December 2017 and 31 December 2016 as well as income and expenses arising from transactions with entities within Erste Group are provided in tables below:

	31 December 2017		RSD thousand 31 December 2016	
	Shareholders	Other members of Erste Group	Shareholders	Other members of Erste Group
Receivables				
Financial assets at fair value through profit and loss, held for trading	12,842	-	74,982	-
Loans and receivables due from banks and other financial institutions	1,158,880	12,846	684,919	255,167
Loans and receivables due from customers	-	153	-	288
Investments in dependent companies	-	93,560	-	93,560
Other receivables	168,518	30,833	18,967	28,013
	1,340,240	137,392	778,868	377,028
Liabilities				
Financial liabilities at fair value through profit and loss, held for trading	40,956	-	49,915	-
Deposits and liabilities due to banks and other financial institutions	16,359,513	143,282	19,336,606	794,664
Deposits and liabilities due to customers	-	51,913	-	111,903
Subordinated liabilities	1,354,523	-	1,764,605	-
Provisions	191	149	205	314
Other liabilities	13,923	199,263	22,265	121,396
	17,769,105	394,606	21,173,597	1,028,278
Off-balance sheet items				
Guarantees and other warranties	1,038,214	227,487	262,701	544,510
Irrevocable commitments	-	2,904	196,904	2,848
Other off-balance sheet items	10,323,119	653,012	15,399,712	-
	11,361,333	883,403	15,859,317	547,358

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for the year ended 31 December 2017
31. RELATED PARTY DISCLOSURES (continued)

	31 December 2017		31 December 2016	
	Shareholders	Other members of Erste Group	Shareholders	Other members of Erste Group
Interest income	21,421	2,490	13,904	1,689
Interest expense	(288,509)	(5,080)	(284,337)	(2,293)
Fees and commission income	44,456	15,446	75,154	1,961
Fees and commission expense	(201,716)	-	(164,454)	-
Net gains on the financial assets held for trading	27,645	-	87,505	-
Net income from exchange rate differences and the effects of foreign currency clause	-	1,737	-	1,461
Net income from exchange rate differences and the effects of foreign currency clause	(15,488)	-	(48,236)	-
Net income from impairment of financial assets and credit-risky off-balance sheet items	359	-	1,162	-
Net expenses from impairment of financial assets and credit-risky off-balance sheet items	-	(9,882)	-	(1,983)
Other operating income	5,932	32,479	10,450	30,485
Other expenses	(157,101)	(640,463)	(147,159)	(517,583)

Fees on cross-border loans in 2017 amounted to RSD 3,383 thousand (2016: RSD 28,593 thousand).

Through cross-border loans the Bank gives the customers opportunity to borrow directly from abroad, while all the activities in the approval process and administration of loans are performed by the Bank. Such services provide the customers more favourable terms of borrowings while the Bank earns fee income on related services. The Bank acts strictly as agent in cross-border loan deals and does not bear any credit risk.

(a) As at 31 December 2017 and 31 December 2016 loans due from related parties were not impaired.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
31. RELATED PARTY DISCLOSURES (Continued)

(b) In its regular course of operations, the Group enters into business relationships and arrangements with the members of the Executive Board, other key personnel and persons related to them. Balances at the end of the year and effects of those transactions are presented as follows:

	Balance as at 31 December 2017	Income/ (Expenses) 2017	Balance as at 31 December 2016	RSD thousand Income/ (Expenses) 2016
Current account overdrafts, credit cards, cash and consumer loans	2,535	165	950	141
Housing loans	70,159	3,476	40,711	2,796
Accrued fees	(83)	-	-	-
Other placements and receivables	562	23	258	118
Total impairment allowances	(153)	389	(333)	(89)
Deposits	57,844	(409)	54,045	(318)
Other liabilities	701	(3,028)	57	(385)
Unused credit limit	857	-	324	-

(c) Salaries and other benefits of the Executive Board's members and the Management Board's members (stated in gross amounts), during 2017 and 2016, are presented in the table below:

	31 Dec 2017	RSD thousands 31 Dec 2016
Salaries and benefits of the Management Board members	16,776	5,957
Salaries and benefits of the Executive Board members	113,788	109,888
Accrued income of the Executive Board members	67,041	42,670
Total	197,605	158,515

32. RISK MANAGEMENT
32.1. Introduction

The Group manages risks inherent in banking operations through the processes of ongoing risk identification, measurement and monitoring, restriction and risk limit definition and application of other controls.

Due to the nature of its activities, the Group is exposed to the following major risks: credit risk, liquidity risk and market risk (which includes equity price risk, foreign exchange risk and commodity risk). The Group is also exposed to operating risk and concentration risk, which particularly entails the risk of the Group's exposure to a single entity or a group of related entities, interest rate risk, risk of Group's investments in other entities and own fixed assets, counterparty country risk and other risks the Group monitors on an ongoing basis.

The Group's risk management is a comprehensive process that includes identification, assessment, rating and control of all types of business risks (credit, interest rate, foreign exchange and other market risks, investment and operational risks). The aim of the risk management process is to establish an adequate system for identifying, measuring, assessing and monitoring the risks the Group is exposed to in its business operations, as well as an adequate response in order to minimize potential adverse effects to the Group's capital and financial performance

The Group has adopted policies and procedures that provide control and application of all internal acts of the Group in relation to risk management, as well as regular reporting to the Group in relation to risk management. Risk management processes are vital to the continuous profitable business operations of the Group and each individual within the Group is, within his/her remit, accountable for risk exposure. Such risk management system allows timely and full reporting to the governing bodies on all risks that occur or may occur and enables adequate and prompt response to such risks.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.1. Introduction (continued)

An independent risk management process does not cover business risks which comprise changes in the environment, technology and industry. The Group monitor these risks through the strategic planning process.

The Management Board and the Executive Board are ultimately responsible for identifying and controlling risks while the operational responsibility is delegated to the Risk Management Division. In addition, the Group has established separate independent bodies for managing and monitoring risks.

The key roles in risk management belong to the following units:

Management Board and Executive Board

The Management Board and Executive Board are responsible for the overall risk management approach and for approving the risk management strategies and principles. Their decisions are made based on the proposals of the Credit Risk Management Division and Strategic Risk Management Department, Assets and Liabilities Management Committee and other relevant organizational units of the Group.

Assets and Liability Management Committee

Assets and Liability Management Committee (ALMC) has overall responsibility for the development of a comprehensive risk management strategy and implementation of the principles, framework, policies and limits. ALMC is responsible for fundamental findings in respect of risks and for managing and monitoring of relevant decisions related to risk, principally for interest rates, foreign exchange and other market risks. ALMC has an advisory role and its decisions in the form of proposals are sent for approval to the Executive Board.

The Committee for the management of non-financial risks

The aim of the Committee for the management of non-financial risks is to consider, propose decisions and validate issues in the area of operational risk management of the Group, with the application of the Decision on the basis of expected profit of exposure to risk and the implementation of corrective measures and actions to mitigate risks to manage non-financial risks (operational risk, reputational risk, compliance risk, legal risk, information security) in a proactive manner.

Asset and Liability Management Unit

Asset and Liability Management Unit is organized as an independent organizational unit that is directly responsible to the Executive Board of the Group. In addition, it is primarily responsible for funding and liquidity of the Group. Asset and Liability Management Unit prepares reports related to assets and liabilities management for the purposes of the Groups units as well as a report for the Asset and Liability Management Committee.

Internal audit

Internal audit is established with the aim to ensure that the Group's operations take place in accordance with the standards providing the function of an independent, objective assurance and advisory activities based on best practices. Through systematic and disciplined approach, internal audit helps the Group accomplish its objectives by evaluating and improving the effectiveness of risk management, control and managerial processes.

Risk management processes throughout the Group are audited at least annually by the internal audit function, which examines both the adequacy of the procedures and the Group's compliance with such procedures. Internal audit discusses the results of all assessments with the Group and S-Leasing management and reports its findings and recommendations to the Audit Committee and the Management Board.

Risk Management and Reporting System

In accordance with the Law on Banks in the Group was established internal organisation which defines the organizational unit within its authority and responsibility has the task of risk management. The objective of risk management system is to identify and quantify the risks to which the Group is exposed in the course of its business activities.

The functions of monitoring and risk management are the responsibility of the Risk Management Division as a separate organizational unit within the Group. Risk management policies, risk management strategies as well as strategies for managing capital are linked to the Group 's strategy, and include defining the types of risks, the management of these risks and the level of risk that the Group is willing to accept in order to achieve their business goals. Special attention is paid to full compliance with the relevant regulations of the National Bank of Serbia (NBS).

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.1. Introduction (continued)

Risk Management and Reporting System (continued)

The responsibilities of the Risk Management Division include the following:

- Identification and measurement or assessment of Group's exposure to certain types of risks;
- Risk monitoring, including its monitoring and control, analysis and reports on the amount of individual risks, their causes and consequences;
- Measurement and evaluation as well as management of the Group's risk profile and capital adequacy;
- Tracking of parameters that influence the position of the Group's exposure to risks, primarily including management and optimization of asset quality and the cost of risk;
- Development and application of quantitative risk management models as elements in the process of advanced business decision making and pricing risk;
- Strategies development and limit proposals for the Group's exposure to the individual types of risks and their control;
- Quantifying the impact of changes in the economic cycle or stress events on the Group's financial position;
- Risk assessment of new products introduction and outsourcing activities;
- Development of methodologies, procedures and policies for risk management in accordance with relevant legislation, standards of Erste Group, good business practice and the special needs of the Group;
- Development and implementation of various technical platforms and tools.

Bearing in mind the diversity of areas covered, in order to increase the performance of their roles, the risk management function is divided between the departments managing the strategic risks and Credit Risk Management Division, which consists of the following organizational units:

- Department of Corporate risk management;
- Department of Retail risk management;
- Restructuring and workout/Collections Department.

Information gathered from all business activities are examined and processed in order to identify, analyse and control the risks to which the Group is or may be exposed.

The Group and its operations are particularly exposed to: credit risk, concentration risk, market risk, liquidity risk, operational risk. The obtained information is presented and explained to the Board of Directors, Executive Committee, Asset and Liability Committee and the heads of all business units. Reports are sent to the authorities on a daily, weekly, monthly and quarterly basis, and in accordance with their requirements.

Comprehensive report on risks are quarterly presents to the Board of Directors that includes all relevant information needed to estimate the risks the Group is exposed to.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017****32. RISK MANAGEMENT (continued)****32.2. Credit Risk**

Credit risk is the risk that credit beneficiaries will not be able to fulfil contractual obligations to the Group, whether fully or partially that will generate the loss for the Group.

The Group's credit risk is caused by the debtor's credit capacity, good credit history, as well as quality of collateral, and is being identified, estimated and monitored in accordance with the internal by-laws for credit risk management, as well as in accordance with decisions that regulate the classification of the balance sheet assets and off-balance sheet items and capital adequacy.

By its business policy, the Group requires and assesses the maximum credit risk protection, as most important risk in banking.

The Group controls and manages credit risk by establishing rigorous process for determining minimal credit capacity of the debtor in the process of credit approval, as well as by regular monitoring during credit contract life, by defining the different level of decision during loan approval (which reflects knowledge and experience) and by establishing limits, by which the level of acceptable risk is determined on the individual client basis, geographical basis and industries, and risk monitoring accordingly.

By its internal by-laws, policies and procedures, the Group has implemented the adequate system of credit risk management so as to reduce the credit risk to an acceptable level.

In accordance with the Group's Risk management policy, Credit Policy and Procedures for managing the credit risk, the process of credit risk management for individual placements and risks at the portfolio level, i.e., the procedures of identification, measurement and monitoring (control) of placements, especially those with increased risk levels, has been defined.

The process of monitoring the quality of loan enables the Group to assess the potential losses as a result of which is exposed to risk and to take corrective measures.

Approval of loan products is based on the credit quality of the customer, the type of credit product, collateral, additional system requirements and other factors to minimize credit risk.

Assessment of risk of default by the counterparty of the Group is based on the likelihood of the client entering the status of default (PD). For each credit risk exposure, the credit decision is determined by the Group's internal rating, which is a unique measure of the risk of occurrence of the status of the counterparties. The internal rating of each client is updated on a regular basis, at least once a year. At the quantitative level, the internal ratings affect the cost of the required risk, and not the formation of provisions for credit risks. Internal ratings take into account all the available information needed for risk assessment of the client's entry in the status of default (default-a). For clients from the corporate segment, internal ratings take into account the financial strength of the client (profitability ratios, the adequacy of the maturity structure of certain elements of assets and liabilities, the adequacy of cash flows, indebtedness, credit-exposure to foreign exchange risk, the industry in which the borrower operates, the position of the debtor market, the specific characteristics of the debtor and other relevant indicators). For the retail segment and micro clients, internal ratings are based mainly on behavioural and application scoring, but also used demographic and financial information. It is used to restrict the rating depending on the membership in the group of economically related parties and the main economic activity of the country.

The Group complies with all standards of Erste Group AG from the perspective of the internal rating model development and maintenance process. All new models and modifications of existing models within the Group (rating models and risk parameters) and methodological standards are reviewed by the Commission's group, the so-called. Holding Model Committee (HMC), which ensures the integrity throughout the Group as well as the consistency of the model and methodology.

Models are also approved by local management. The internal rating system complies with Erste Group AG's system, which distinguishes between "performing" and "non-performing" clients. For the "performing" clients (clients that are not in the status of default) The Group uses a scale score of 8 (A1/A2/B1/B2/C1/C2/D1/D2) for customers from the retail segments, or a 13 rating scale (1/2/3/4a/4b/4c/5a/5b/5c/6a/6b/7/8) for all other categories. For customers in the status of default The Group uses a scale score of 5 (R1-R5). For reporting purposes, internal ratings are grouped into the following 4 categories of risk:

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Low risk – clients with established good and longer cooperation with the Group, as well as many internationally recognized customers. Strong financial position with no anticipated financial difficulties in the future. Clients from the retail segment who have a long history of cooperation with the Group or clients who use a wide range of products. Clients who do not have delays in the payment of dues currently or in the past 12 months. At the same time, new contracts are generally signed with customers from this category.

Management attention - clients with barely satisfactory or unsatisfactory financial situation. Maintenance of credit positions very uncertain in the medium term. Negative qualitative criteria are present. Clients from the retail segment with limited savings or likely problems in paying that trigger reminders for early payment.

Sub-standard - clients sensitive to negative financial and economic impacts.

Non-performing – clients who recorded one or more criteria for the activation of the default status, in accordance with the definition laid down in the precise internal regulations of the Group and Erste Group AG: uncertain payments, late payments with a materially significant exposure for more than 90 days, a restructuring that has caused a loss for the Group, realization of credit loss or the initiation of bankruptcy proceedings. In order to determine the default status, The Group applies a client level approach, including retail clients; if the client is in the default status for one product, then all other products from the client are classified as problematic claims.

Monitoring and control of credit risk

With the aim of timely credit risk management a regular analysis of the risk of the client is performed, which includes regular status ratings, serviceability of obligations towards the Group, reviewing collaterals and compliance with contractual terms.

The Group aims to promptly identify any deterioration in the quality of the loan portfolio, which may result in material losses for the Group, therefore, the Group, through the process of regular re-approval, analyses the overall status of the debtor. The importance of regular re-approval of credit exposure is in the regular client monitoring and portfolio quality, and represents an additional measure to optimize credit risk exposure of the Group.

The Group conducts evaluation of credit quality based on customer information, also taking into account all the client information and previous credit history between the group and the client.

Early Warning Signals

Systems and processes are used to detect early warning indications of negative developments, in order to provide proactive measures to reduce the risk. The Group applies methods of early detection of increased credit risk in order to increase successful collection even in case of deterioration of the credit portfolio quality, which is revealed by monitoring all relevant information and predicting changes in variables in the future which primarily includes the client's behaviour up to that point in settling obligations and monitoring of market information.

EWS control function within the Group is organized within a separate organizational unit within the Directorate of credit risk management of legal entities (Department of EWS and monitoring).

Default status

Definition of the default status within the Group follows the regulatory requirements of the Group by translating them into five groups of events of default status:

- Default event E1 - Small chance of settling the obligations entirely due to the decrease of credit quality of borrowers
- Default event E2 - A delay longer than 90 days after a materially significant amount of debt
- Default event E3 - Modifications to the originally agreed terms of repayment due to the assessment of the worsening economic situation of the client
- Default event E4 - Credit loss
- Default event E5 - Bankruptcy

The Group has established a systematic process to ensure identification and recognition of status of default on client level. This means that in case a default status of any credit risk exposure of individual investments of a client, the total balance sheet or off-balance sheet exposure that the Group has for the client, including products that are not related to lending, are classified in the default status. The foregoing is applicable to all clients from the retail banking segment, as well as clients from other corporate segments.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017****32. RISK MANAGEMENT (continued)****32.2. Credit Risk (continued)****Default status (continued)**

In the case of undertaken loan commitments that are part of the Group's off-balance sheet assets, the exposure in the status of default is presented in the nominal amount of the liability, which, in case of the withdrawal of funds, or the activation, leads to risk exposure based on the default status without the realization of collaterals.

In the case of given financial guarantees, exposure in the status of default represents the total nominal amount based on which there is a risk that may arise in the event of the occurrence of default status of partial or total guaranteed exposure.

Default events can be activated either at the level of exposure of individual investments or on the client level, but the general rule that applies to all cases, requires that the client is granted the status of default for all individual exposures, and be given an internal rating of "R", regardless whether the default event triggered at individual exposures level or at the client level.

All clients of the Group are located in the status of default and therefore they are given the appropriate internal rating (R1 - R5) if there has been a realization of at least one of the default events E1 - E5.

If, in the judgment of the Group, the criteria that are a precondition for assigning events leading to the status of default are no longer applicable and the client is able to continue to repay the debt in accordance with the defined terms of the contract, the Group will change the rating of the client due to the fact that the client who is no longer in the status of default.

Minimum general requirements that must be met before leaving the status of default and the "R" rating are the following:

- none of the default events E1 - E5 are valid with the client and additional losses in not expected on its individual credit exposures and
- the monitoring period is successfully over.

Each event has a default precisely defined minimum duration and termination of the default status is acceptable only after the successful completion of the monitoring period which automatically follows the expiry / termination of default events E1 - E5 in clients who have any type of credit obligations and which lasts 3 months thereafter. Specifically, in order to successfully complete the monitoring period, during this time, the client is not allowed to start or have any criteria that may initiate by one of the predefined default events E1 - E5.

Write off of receivables

The Group, in accordance with the Regulations on the write-off of receivables and the transfer of receivables from the balance sheet to the off-balance sheet, performs write-offs of bad debts after they have exhausted all the possibilities for recovery. In addition, write-offs can be taken into consideration in a situation where further court proceedings are not economically viable due to higher costs compared to the collection amount, where further action of any kind is not effective. Write-off of receivables is performed only for doubtful loans that are impaired. For claims under litigation or bankruptcy which are fully impaired (for which a correction of 100% has been performed), and for which it is assessed that the litigation or bankruptcy will take too long and therefore will be a burden to the Group's balance sheet records, a decision is made on the transfer of receivables from the balance sheet to the off balance sheet but the debt is not forgiven, more precisely the Group does not waive contractual and legal rights for the claim.

In addition, the Group in accordance with the Decision of the National Bank of Serbia on the accounting write-off of the balance sheet assets of the Bank "Official Gazette of the Republic of Serbia", no. 77/2017 of 10 August 2017, performs an accounting write-off of problematic receivable in the case when the amount of the impairment of that receivable was recorded by the bank in favour of impairment of the value of 100% of its gross carrying amount.

Maximum exposure to credit risk in balance sheet and off-balance sheet items.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Overview of the maximum exposure to credit risk is shown in both gross and net amounts, without taking into account collaterals and other items that the Group does not consider as exposed to credit risk in accordance with the positions of the balance sheet as at 31 December 2017 is presented in the table below:

	Assets at based on which the Group is exposed to credit risk			The assets based on which the Group is not exposed to credit risk	RSD
	Gross amount	Accumulated allowance for impairment / provisions	Net amount		thousand
					Value from the balance sheet
Cash and assets with the central bank	9,293,751	-	9,293,751	11,480,276	20,774,027
Financial assets at fair value through the income statement held for trading	11,539,464	-	11,539,464	-	11,539,464
Financial assets available for sale	12,488,599	6	12,488,593	-	12,488,593
Financial assets held to maturity	8,329,870	45,418	8,284,452	-	8,284,452
Loans and receivables from banks and other financial institutions	2,211,657	12,687	2,198,970	-	2,198,970
Loans and receivables from customers	114,731,677	4,258,948	110,472,729	-	110,472,729
Investments in associates and joint ventures	-	-	-	118	118
Intangible assets	-	-	-	255,553	255,553
Property, plant and equipment	-	-	-	1,078,617	1,078,617
Investment property	-	-	-	0	0
Current tax assets	-	-	-	3,386	3,386
Deferred tax assets	-	-	-	2,261	2,261
Fixed assets held for sale and assets from discontinued operations	-	-	-	12,288	12,288
Other assets	756,671	57,331	699,340	454,771	1,154,111
On-Balance exposure	159,351,689	4,374,390	154,977,299	13,287,270	168,264,569
Guarantees and warranties	12,396,034	148,158	12,247,876	-	12,247,876
Assumed future liabilities	24,834,817	177,825	24,656,992	-	24,656,992
Other off-balance sheet exposure	-	-	-	216,002,505	216,002,505
Off-Balance exposure	37,230,851	325,983	36,904,868	216,002,505	252,907,373
Total exposure	196,582,540	4,700,373	191,882,167	229,289,775	421,171,942

In accordance with the business policy of the Group, the primary source of credit risk the Group considers portfolio of loans and receivables from customers, banks and other financial institutions, as well as off-balance sheet exposures in the form of financial guarantees and committed future liabilities. A detailed review of these exposures¹ in terms of sectors and categories of claims, status and impairment, maturity and the value of collaterals is provided below.

¹ Other items from the balance sheet that the Group considers exposed to credit risk primarily arising from activities that support the core business of the Group (the formation of liquidity reserves, and short-term liquidity management, as well as the optimization of interest income by managing assets and liabilities) and are characterized by high credit quality.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Overview of securities

Balance as at 31 December 2017

	Securities			
	Gross value	Of which: impaired	Accumulated value adjustments	Of which: impairment losses on impaired receivables
Financial assets at fair value through profit and loss for trading	11,539,464	-	-	-
Of which: State bonds of the Republic of Serbia	11,213,908	-	-	-
Of which: Other	325,556	-	-	-
Financial assets available for sale	12,488,600	-	7	-
Of which: State bonds of the Republic of Serbia	12,385,371	-	-	-
Of which: Other	103,229	-	7	-
Financial assets held to maturity	8,329,869	-	45,417	-
Of which: State bonds of the Republic of Serbia	8,329,869	-	45,417	-
Of which: Other	-	-	-	-
Total exposure	32,357,933	-	45,424	-

As at 31 December 2017, 98.7% of securities exposures refer to the exposure based on government bonds of the Republic of Serbia, which, in accordance with the valid Decision on capital adequacy of the bank, allocates a risk weight of 0%.

Credit rating of the Republic of Serbia for long-term borrowing as at 31 December 2017:

- Moody's Investors Service Ba3 / stable outlook
- Fitch Ratings BB / stable outlook
- Standard and Poor's BB / stable outlook

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Maximum exposure to credit risk, in gross and net amount, without collaterals, as well as other items Bank does not consider to be exposed to credit risk, in accordance with Balance sheet items as of 31 December 2016 is presented in the following table:

	Assets exposed to credit risk			Assets not exposed to credit risk	RSD thousand
	Gross value	Accumulated allowance for impairment / provisions	Net value		Balance sheet
Cash and funds at Central Bank	8,403,985	-	8,403,985	10,842,685	19,246,670
Financial assets through profit and loss held for trading	13,048,357	-	13,048,357	-	13,048,357
Financial assets available for sale	7,303,359	120,657	7,182,702	-	7,182,702
Financial assets held to maturity	8,635,103	-	8,635,103	-	8,635,103
Loans and receivables from banks and other financial organizations	1,222,018	12,293	1,209,725	-	1,209,725
Loans and receivables from customers	103,247,635	6,784,373	96,463,262	-	96,463,262
Investments in subsidiaries	-	-	-	118	118
Intangible assets	-	-	-	281,395	281,395
Property, plant and equipment	-	-	-	817,267	817,267
Investment property	-	-	-	232,417	232,417
Current tax assets	-	-	-	6,513	6,513
Deferred tax assets	-	-	-	61,745	61,745
Non-current assets held for sale and discontinued operations	-	-	-	56,695	56,695
Other assets	1,088,979	242,410	846,569	18,294	864,863
Balance sheet	142,949,436	7,159,733	135,789,703	12,317,129	148,106,832
Guarantees and warranties	8,197,983	109,112	8,088,871	-	8,088,871
Assumed contingent liabilities	13,808,943	168,369	13,640,574	-	13,640,574
Other off-balance exposure	-	-	-	165,945,394	165,945,394
Off-balance sheet	22,006,926	277,481	21,729,445	165,945,394	187,674,838
Total exposure	164,956,362	7,437,214	157,519,148	178,262,523	335,781,670

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Overview of securities:

Balance as at 31 December 2016	Securities			
	Gross value	Of which: impaired	Accumulated value adjustments	Of which: impairment losses on impaired receivables
Financial assets at fair value through profit and loss for trading	13,048,357	-	-	-
Of which: State bonds of the Republic of Serbia	12,591,622	-	-	-
Of which: Other	456,735	-	-	-
Financial assets available for sale	7,303,359	118,219	120,657	118,219
Of which: State bonds of the Republic of Serbia	7,072,110	-	-	-
Of which: Other	231,249	118,219	120,657	118,219
Financial assets held to maturity	8,635,103	-	-	-
Of which: State bonds of the Republic of Serbia	8,635,103	-	-	-
Of which: Other	-	-	-	-
Total exposure	28,986,819	118,219	120,657	118,219

As at 31 December 2016, 97.6% of securities exposures refer to the exposure based on government bonds of the Republic of Serbia, which, in accordance with the valid Decision on capital adequacy of the bank, allocates a risk weight of 0%.

Credit rating of the Republic of Serbia for long-term borrowing as at 31 December 2016:

- Moody's Investors Service Ba3 / stable outlook
- Fitch Ratings BB- / stable outlook
- Standard and Poor's BB- / positive outlook

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Loans and receivables from customers, banks and other financial institutions

(a) Overview by credit quality of receivables and non-problematic value of collaterals by which they are insured as at 31 December 2017:

	<u>The credit quality of non-problematic receivables</u>			<u>Problematic receivables</u>	<u>Value of collaterals</u>	
	<u>High</u>	<u>Medium</u>	<u>Low</u>		<u>Non-problematic receivables</u>	<u>Problematic receivables</u>
Receivables from retail clients	40,507,076	4,640,748	1,075,184	1,583,972	19,444,751	543,120
Housing loans	23,266,017	946,128	352,993	794,528	18,899,076	540,434
Consumer and Cash Loans	14,893,934	3,322,491	628,129	600,733	99,035	1,350
Transactional and Credit Card	652,117	104,604	20,339	20,190	1,533	136
Other receivables	1,695,008	267,525	73,723	168,520	445,106	1,200
Receivables from corporate clients	56,454,519	3,739,280	482,239	1,607,122	20,040,958	925,359
Large entities	9,042,234	76,635	-	416,685	4,683,766	415,599
Small and medium-sized entities	36,231,069	1,052,534	102,368	774,044	11,258,820	238,114
Micro enterprises and entrepreneurs	9,355,457	1,069,814	208,832	354,509	1,957,212	252,768
Agricultural producers	101,920	95,154	37,516	59,547	127,905	18,877
Public companies	1,723,840	1,445,143	133,523	2,336	2,013,254	-
Receivables from other clients	5,437,940	734,171	1	681,084	662,414	439,619
Total receivables	102,399,534	9,114,198	1,557,423	3,872,177	40,148,123	1,908,098

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Loans and receivables from customers, banks and other financial institutions

(a) Overview by credit quality of receivables and non-problematic value of collaterals by which they are insured as at 31 December 2016:

	The credit quality of non-problematic receivables			Problematic receivables	Value of collaterals*	
	High	Medium	Low		Non-problematic receivables	Problematic receivables
						(gross value in RSD thousand)
Receivables from retail clients	27,027,961	4,847,136	1,166,584	2,337,082	13,052,496	570,421
Housing loans	14,070,281	917,149	504,475	866,526	12,574,769	561,611
Consumer and Cash Loans	10,498,291	3,379,768	535,574	1,120,044	117,400	2,447
Transactional and Credit Card	654,322	127,814	30,325	54,731	2,235	258
Other receivables	1,805,066	422,406	96,211	295,781	358,093	6,104
Receivables from corporate clients	52,538,994	6,449,718	260,461	3,136,263	21,808,769	1,318,471
Large entities	9,999,932	109,068	0	40,998	2,929,485	36
Small and medium-sized entities	32,053,876	2,636,818	182,941	1,939,649	13,241,641	909,081
Micro enterprises and entrepreneurs	10,334,479	788,423	41,807	755,070	2,826,810	371,544
Agricultural producers	145,596	77,216	35,713	75,796	132,952	37,809
Public companies	5,111	2,838,193	-	324,750	2,677,880	-
Receivables from other clients	1,784,330	3,490,687	397	1,430,040	785,883	718,452
Total receivables	81,351,286	14,787,542	1,427,441	6,903,385	35,647,147	2,607,343

*Effects of securities on increase of allowance impairment is calculated by simulating LGD parameters and excluding securities. Simulations refer to general provisions and special provisions for the specific important clients (the collateral does not affect the value of LGD for impaired exposures that are not considered as individually significant).

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

(b) Overview of the gross and net credit exposure by sectors and categories of receivables, according to the type of impairment, the maturity and the value of collaterals as at 31 December 2017:

	RSD thousand										
	Non-impaired receivables ²		Impaired receivables ³		Total gross receivables	Accumulated impairment			Total net receivables	Value of collaterals	
	Not due	Due	Individually impaired	Collectively impaired		Impairment of non-impaired receivables	Individually impaired	Collectively impaired		Non-impaired receivables	Impaired receivables
By sectors											
Receivables from retail	46,155,127	221,949	655,491	774,413	47,806,980	785,714	347,388	513,018	46,160,859	19,506,668	481,202
Housing loans	24,602,320	37,469	639,428	80,449	25,359,666	293,798	334,685	33,032	24,698,150	18,960,418	479,091
Consumer and Cash Loans	18,785,960	135,143	1,370	522,814	19,445,288	434,183	1,343	336,830	18,672,931	99,610	775
Transactional and Credit Card	775,535	1,825	101	19,788	797,249	15,341	101	13,576	768,231	1,533	136
Other receivables	1,991,312	47,512	14,592	151,362	2,204,777	42,392	11,258	129,580	2,021,548	445,106	1,200
Receivables from corporate clients	60,411,289	264,749	1,543,495	63,626	62,283,158	773,628	1,153,339	52,080	60,304,111	20,040,958	925,359
Large entities	9,079,181	39,687	416,085	599	9,535,554	107,383	314,970	240	9,112,961	4,683,766	415,599
Small and medium-sized entities	37,235,782	150,190	743,963	30,080	38,160,016	404,714	601,331	28,654	37,125,317	11,258,821	238,114
Micro enterprises and entrepreneurs	10,573,434	60,668	332,290	22,220	10,988,612	212,336	197,510	15,622	10,563,143	1,957,212	252,768
Agricultural producers	226,712	7,877	51,157	8,390	294,136	9,574	39,528	5,228	239,806	127,906	18,877
Public companies	3,296,179	6,326	-	2,336	3,304,841	39,620	-	2,336	3,262,885	2,013,254	-
From other clients	6,073,752	98,360	658,012	23,072	6,853,196	55,605	567,790	23,072	6,206,729	662,414	439,619
Total exposure	112,640,167	585,058	2,856,998	861,111	116,943,334	1,614,947	2,068,517	588,170	112,671,699	40,210,041	1,846,180
By category of receivables											
Non-problematic receivables	112,488,758	583,061	-	-	113,071,157	1,598,251	-	-	111,472,906	40,148,123	-
of which: Restructured	305,860	2,354	-	-	308,213	26,501	-	-	281,712	115,711	-
Problematic receivables	151,409	2,659	2,856,998	861,111	3,872,177	16,696	2,068,517	588,170	1,198,794	61,918	1,846,180
of which: Restructured	148,867	2,501	1,493,105	153,119	1,797,591	16,572	1,104,810	73,002	603,208	61,086	1,085,126
Total exposure	121,640,167	585,058	2,856,998	861,111	116,943,334	1,614,947	2,068,517	588,170	112,671,699	40,210,041	1,846,180

² By non-impaired receivables, the Group considers receivables which are not in the default status and receivables without indicators of impairment

³ By impaired receivables, the Group considers receivables which are in default status with impairment indicator

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

(a) Overview of the gross and net credit exposure by sectors and categories of receivables, according to the type of impairment, the maturity and the value of collaterals as at 31 December 2016:

	RSD thousand										
	Non-impaired receivables		Impaired receivables		Total gross receivables	Accumulated impairment			Value of collaterals		
	Not due	Due	Individually impaired	Collectively impaired		Impairment of non-impaired receivables	Individually impaired	Collectively impaired	Total net receivables	Non-impaired receivables	Impaired receivables
By sectors											
Receivables from retail	33,015,887	190,447	667,710	1,504,720	35,378,763	799,135	276,982	1,227,088	33,075,558	13,115,775	507,142
Housing loans	15,547,007	33,588	623,938	153,897	16,358,431	197,374	238,041	102,166	15,820,849	12,637,321	499,060
Consumer and Cash Loans	14,376,386	107,152	30,275	1,019,865	15,533,677	499,014	30,276	831,148	14,173,239	118,127	1,720
Transactional and Credit Card	810,953	1,908	175	54,155	867,191	28,496	175	47,949	790,570	2,235	258
Other receivables	2,281,541	47,799	13,321	276,803	2,619,464	74,251	8,490	245,824	2,290,900	358,093	6,104
Receivables from corporate clients	59,038,872	215,964	2,877,336	253,264	62,385,436	876,025	2,176,146	243,235	59,090,030	21,814,154	1,313,085
Large entities	10,100,421	8,580	40,783	215	10,149,999	178,807	38,668	275	9,932,248	2,929,485	36
Small and medium-sized entities	34,725,505	148,269	1,819,284	120,226	36,813,283	496,662	1,403,274	115,488	34,797,859	13,241,780	908,942
Micro enterprises and entities	11,124,191	46,042	656,078	93,468	11,919,780	186,846	408,275	88,566	11,236,092	2,832,057	366,298
Agricultural producers	246,534	11,991	38,876	36,920	334,321	5,577	19,349	36,471	272,924	132,952	37,809
Public companies	2,842,222	1,082	322,315	2,435	3,168,054	8,132	306,580	2,435	2,850,907	2,677,880	-
From other clients	5,162,496	111,244	991,720	438,320	6,703,780	78,618	783,156	334,608	5,507,398	785,883	718,452
Total exposure By category of receivables	97,217,255	517,654	4,536,765	2,196,304	104,467,979	1,753,777	3,236,284	1,804,931	97,672,987	35,715,812	2,538,679
Non-problematic receivables of which:	97,049,676	514,918	-	-	97,564,594	1,746,031	-	-	95,818,563	35,647,147	-
Restructured	541,551	9,613	-	-	551,165	19,739	-	-	531,426	398,235	-
Problematic receivables of which:	167,579	2,736	4,536,765	2,196,304	6,903,385	7,746	3,236,284	1,804,931	1,854,425	68,664	2,538,679
Restructured	162,046	2,574	1,501,657	590,997	2,257,274	7,670	1,103,757	402,355	743,491	64,997	1,171,368
Total exposure	97,217,255	517,654	4,536,765	2,196,304	104,467,979	1,753,777	3,236,284	1,804,931	97,672,987	35,715,812	2,538,679

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

(v) Data on exposure to credit risk by sectors and categories of receivables, according to the impairment status and number of days past due as at 31 December 2017:

	Non-impaired receivables					Impaired receivables					RSD thousand
	Not in delay	Within 30 days	From 31 to 60 days	From 61 to 90 days	Over 91 days	Not in delay	Within 90 days	From 91 to 180 days	From 180 to 360 days	Over 360	
Receivables from retail	39,274,174	6,765,043	260,212	77,619	25	259,536	285,562	162,355	180,140	542,311	
Housing loans	23,846,586	689,213	86,358	17,632	-	159,098	116,131	45,294	72,050	327,304	
Consumer and Cash Loans	13,211,849	5,527,812	130,416	51,027	-	87,036	144,565	98,054	84,827	109,702	
Transactional and Credit Card	755,392	3,192	15,399	3,377	-	4,326	2,172	4,709	3,620	5,063	
Other receivables	1,460,347	544,827	28,040	5,584	25	9,076	22,694	14,297	19,643	100,242	
Receivables from corporate clients	56,432,105	4,190,660	46,205	7,069	-	396,400	40,518	12,895	17,426	1,139,882	
Large entities	9,037,418	81,450	1	-	-	599	-	-	-	416,085	
Small and medium-sized entities	34,709,525	2,660,612	15,835	-	-	278,297	28,312	12	16,010	451,412	
Micro enterprises and entities	9,203,054	1,400,820	23,612	6,617	-	117,497	6,429	1,785	168	228,631	
Agricultural producers	211,088	21,581	1,470	451	-	8	5,776	11,098	1,248	41,417	
Public companies	3,271,021	26,197	5,287	-	-	-	-	-	-	2,336	
From other clients	6,136,974	35,138	-	-	-	1	17	-	207	680,859	
Total exposure	101,843,254	10,990,840	306,418	84,688	25	655,938	326,097	175,250	197,773	2,363,051	
By category of receivables	-	-	-	-	-	-	-	-	-	-	
Non-problematic receivables	101,790,865	10,937,676	260,511	82,105	-	-	-	-	-	-	
of which: restructured	237,970	67,156	2,942	146	-	-	-	-	-	-	
Problematic receivables	52,389	53,164	45,907	2,583	25	655,938	326,097	175,250	197,773	2,363,051	
of which: restructured	51,313	51,821	45,702	2,532	-	528,870	109,750	21,326	18,124	968,153	
Total exposure	101,843,254	10,990,840	306,418	84,688	25	655,938	326,097	175,250	197,773	2,363,051	

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

(v) Data on exposure to credit risk by sectors and categories of receivables, according to the impairment status and number of days past due as at 31 December 2016:

	Non-impaired receivables					Impaired receivables					RSD thousand
	Not in delay	Within 30 days	From 31 to 60 days	From 61 to 90 days	Over 91 days	Not in delay	Within 90 days	From 91 to 180 days	From 180 to 360 days	Over 360	
Receivables from retail	27,615,908	5,244,935	265,672	79,794	25	258,699	242,609	243,158	237,163	1,190,800	
Housing loans	14,748,687	705,120	101,428	25,360	-	161,499	79,253	95,318	63,144	378,621	
Consumer and Cash Loans	10,482,711	3,840,623	117,901	42,303	-	82,872	141,213	109,733	138,314	578,008	
Transactional and Credit Card	787,771	3,787	17,530	3,773	-	3,481	1,943	6,491	6,708	35,706	
Other receivables	1,596,739	695,405	28,813	8,358	25	10,846	20,201	31,616	28,997	198,464	
Receivables from corporate clients	55,217,014	3,975,960	49,308	9,574	2,980	389,005	147,680	284,834	236,831	2,072,250	
Large entities	10,051,187	57,813	-	-	-	215	-	32,781	-	8,001	
Small and medium-sized entities	32,037,422	2,813,387	21,205	1,620	139	213,076	100,840	14,851	202,362	1,408,381	
Micro enterprises and entities	10,083,756	1,062,617	17,164	3,855	2,840	11,105	46,045	237,153	23,504	431,738	
Agricultural producers	208,191	42,142	4,093	4,099	-	3,519	794	48	10,965	60,470	
Public companies	2,836,458	-	6,846	-	-	161,090	-	-	-	163,660	
From other clients	5,252,816	20,924	-	-	-	26,755	383,351	-	51,941	967,993	
Total exposure	88,085,738	9,241,819	314,980	89,368	3,005	674,458	773,640	527,992	525,936	4,231,043	
By category of receivables											
Non-problematic receivables	87,988,286	9,200,589	296,458	79,262	-	-	-	-	-	-	
of which: restructured	426,008	120,760	1,458	2,939	-	-	-	-	-	-	
Problematic receivables	97,452	41,230	18,522	10,106	3,005	674,458	773,640	527,992	525,936	4,231,043	
of which: restructured	95,433	40,729	18,353	10,106	-	355,339	521,772	163,423	222,643	829,476	
Total exposure	88,085,738	9,241,819	314,980	89,368	3,005	674,458	773,640	527,992	525,936	4,231,043	

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
32. RISK MANAGEMENT (continued)
32.2. Credit Risk (continued)
(g) Data on problematic receivables as at 31 December 2017:

	RSD thousand						
	The gross value of receivables	Accumulated allowance for impairment of total receivables	The gross value of problematic receivables		Accumulated allowance for impairment of problematic receivables	% of problematic receivables	The value of collaterals of problematic receivables
			Total	of which: restructured receivables			
Retail receivables	47,806,978	1,646,119	1,583,972	463,530	877,101	3.31	543,120
Housing loans	25,359,666	661,519	794,528	260,854	376,474	3.13	540,434
Consumer and Cash Loans	19,445,288	772,354	600,733	189,359	345,949	3.09	1,350
Transactional and Credit Card	797,249	29,018	20,190	-	13,688	2.53	136
Other receivables	2,204,776	183,228	168,520	13,317	140,990	7.64	1,200
Receivables from corporate clients*	57,283,690	1,823,185	1,511,500	1,018,873	1,135,650	2.64	896,131
Sector A	2,429,555	103,212	73,908	47,243	52,450	3.04	19,474
Sector B, C, E	14,470,866	667,157	671,567	621,159	503,767	4.64	551,545
Sector D	5,674,910	79,971	-	-	-	-	-
Sector F	10,677,961	189,842	123,168	119,208	116,730	1.15	25,697
Sector G	11,479,578	524,837	493,152	224,072	360,071	4.30	212,477
Sector H, I, J	5,700,486	94,997	18,161	-	14,009	0.32	5,487
Sector L, M, N	6,850,334	163,169	131,543	7,191	88,624	1.92	81,452
Receivables from other clients	11,852,665	802,331	776,706	315,188	660,632	6.55	468,846
Total receivables	116,943,334	4,271,635	3,872,177	1,797,591	2,673,383	3.31	1,908,098

* Sector A - Electricity, gas, steam and air conditioning

Sector B, C, E - Construction

Sector D - Agriculture, forestry, fishing

Sector F - Mining, manufacturing, water supply, waste water, process control waste management and remediation activities

Sector G - Wholesale and retail trade, repair of motor vehicles and motorcycles

Sector H, I, J - Transportation and warehousing, accommodation and food services, information and communication

Sector L, M, N - Real estate, professional, scientific and technical activities, administrative and support service activities, arts

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

(g) Data on problematic receivables as at 31 December 2016:

	The gross value of receivables	Accumulated allowance for impairment of total receivables	The gross value of problematic receivables		Accumulated allowance for impairment of problematic receivables	% of problematic receivables	RSD thousand The value of collaterals of problematic receivables
			Total	of which: restructured receivables			
Retail receivables	35,378,763	2,303,204	2,337,082	483,494	1,511,606	6.61	570,421
Housing loans	16,358,431	537,581	866,526	266,328	344,567	5.30	561,611
Consumer and Cash Loans	15,533,677	1,360,438	1,120,044	196,261	864,327	7.21	2,447
Transactional and Credit Card	867,191	76,620	54,731	-	48,138	6.31	258
Other receivables	2,619,464	328,564	295,781	20,905	254,573	11.29	6,104
Receivables from corporate clients*	57,910,058	2,782,317	2,597,445	1,098,488	1,940,547	4.49	1,241,118
Sector A	2,505,384	175,721	185,425	50,542	143,849	7.40	51,482
Sector B, C, E	15,955,584	914,772	933,258	262,981	691,874	5.85	338,735
Sector D	5,875,234	101,494	-	-	-	-	0
Sector F	10,643,058	408,067	324,719	136,784	267,986	3.05	135,110
Sector G	9,829,060	831,531	900,321	618,700	685,195	9.16	562,763
Sector H, I, J	7,954,467	165,751	99,947	22,348	45,647	1.26	68,077
Sector L, M, N	5,147,271	184,982	153,774	7,133	105,996	2.99	84,951
Receivables from other clients	11,179,159	1,709,471	1,968,858	675,292	1,596,869	17.61	795,804
Total receivables	104,467,979	6,794,991	6,903,385	2,257,274	5,049,021	6.61	2,607,343

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

(d) Data on changes of problematic receivables in 2017:

	Gross value at beginning of year	New problematic receivables	Decrease of problematic receivables				Other changes ⁴	Gross value at end of year	Net value at end of year	RSD
			Total	of which: charged	of which: transferred to the category of non-problematic receivables	of which: written off				thousand
Retail receivables	2,337,082	782,543	1,562,968	317,533	366,532	878,903	27,314	1,583,971	706,874	
Receivables from corporate and other clients	4,566,303	110,099	2,497,364	941,677	165,393	1,390,295	109,169	2,288,206	491,924	
Total receivables	6,903,385	892,642	4,060,332	1,259,209	531,925	2,269,198	136,482	3,872,177	1,198,798	

Data on changes of problematic receivables in 2016:

	Gross value at beginning of year	New problematic receivables	Reduction of problematic receivables				Other changes	Gross value at year end	Net value at year end	RSD
			Total	which from: collected	of which: transferred to non-problematic category	which from: write-off				thousand
Receivables from retail clients	2,667,369	905,859	1,386,098	395,399	572,906	417,793	149,952	2,337,082	825,476	
Receivables from corporate and other clients	6,334,920	506,728	2,547,480	1,127,170	15,265	1,405,045	272,135	4,566,303	1,028,888	
Total receivables	9,002,289	1,412,586	3,933,578	1,522,568	588,171	1,822,838	422,087	6,903,385	1,854,364	

⁴ Other changes relate to foreign exchange differences and increased exposure based on existing of problematic claims.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Collaterals and other means of protection against credit risk

During the process of credit approval, the Group expects to collect primarily from future cash flows of borrowers. As a supplement to this form of collection, and to reduce the potential losses due to the occurrence of the status of default of the debtor, the Group takes various security instruments (collaterals) as protection. The Group takes as much collaterals as possible, whereby the preferred collateral that can be quickly and easily realized. The possibility of taking collateral depends on current market situation and business competition. The effectiveness of credit risk mitigation technique is measured and controlled by monitoring the time taken for the realization of collateral and the deviation of realized value of collateral and the expected amount.

In the context of strategic risk management departments, the Department for collateral management, which is responsible for the entire collateral management process - from the preliminary analysis to the completion of its implementation. The process is divided into 3 phases:

Analysis phase of collaterals represents the initial phase of the process of collateral management. It begins with the identification and analysis of potential collateral and collecting necessary information and documentation, and ends with the records of the collateral in the system for recording collateral.

Monitoring phase of collaterals refers to monitoring of restitution and value of collaterals. One of its main function is to record, monitor, update and control data on collaterals in the system for recording collateral.

Realization phase of collaterals represents the last phase of the process, when it comes to the realization of collateral (e.g. its sales in order to close placements) and the closing of collateral in the system for recording collateral. It also includes the phase of data collection for the calculation of the average Collateral Recovery Ratio.

Each phase is regulated by the Procedure of collateral management that defines the assignments and responsibilities of the organizational units involved in the process.

In addition to the process, the Collateral management department is responsible for the process of selection, monitoring and removal of appraisers from the list of acceptable appraisers by the Group, and to define the minimum content of the report on valuation, as well as control the application of appropriate methodology in the valuation of collateral, in order to provide a more accurate value of collaterals. Detailed rules for standards and valuation methodology are included in the Policy of the collateral management.

Reviewing the value of collaterals is done periodically, depending on the method of the verification and the type of collateral. Reviewing the value of collaterals can be separated into valuation by an external appraisers or government body authorized to determine the value (re-evaluation, Tax statement) and the internal monitoring of collaterals' value by the employees in the Department of collateral management (monitoring). The dynamics of the review of the value of collateral is defined depending on the type of collateral, and in accordance with local and internal regulations.

Within the process of calculating the capital requirement for credit risk, the Department for Management of strategic risk, after checking the compliance with applicable legal regulations defined by the Decision on capital adequacy of banks, determines whether a particular instrument is accepted as collateral to mitigate credit risk. Items of collateral which are eligible as instruments for credit risk mitigation are explained in detail in a special internal procedure of the Group which defines applicable instruments to mitigate credit risk as well as conditions for the recognition of credit risk mitigation instruments.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Basic types of credit protection instruments

The Group applies primarily cash and cash equivalents deposited with the Group as instruments of material credit protection.

At the moment, the Group does not apply balance and off-balance netting as credit risk reduction technique.

Primary types of credit risk protection on the basis of guarantees and credit derivatives

Guarantees applied as immaterial credit protection are provided by:

- Government – as at 31 December 2017 to mitigate credit risk-weighted assets is used guarantee provided by Republic of Serbia. Preferential credit risk ponder of 0% was applied in accordance with Decision on capital adequacy prescribed by NBS;
- Commercial banks of sufficient credit quality – exposures secured by a bank guarantee

In its portfolio of acceptable means of collateral the Group has no credit derivatives, thus they are not used as instruments of credit protection.

Exposures secured by mortgages on real estate

Real estate is recognized as a protection instrument when all the requirements defined by the Decision on the capital adequacy of banks are met. The fulfilment of the prescribed requirements is a prerequisite for classifying the given exposure into a special class of exposure, exposures secured by mortgages on real estate, which are given a more favourable credit risk weight, instead of recognizing the effects of credit risk mitigation techniques. Group exposure or parts of exposure with a fully secured mortgage on a residential property in which the owner resident or has leased that real estate under an appropriate contract (or intends to reside or lease it) - assigns a risk weight of 35% or exposures fully secured to mortgages on business real estate, assigns a risk weight of 50%.

Other types of credit protection instruments

Similar means of collateral in the form of financial assets for all approaches and methods are considered cash and cash equivalents deposited with the bank when all the requirements defined by the Decision on the capital adequacy of banks are fulfilled.

In addition to the above mentioned, the Group applies the following credit protection instruments, but they were not taken into account in the calculation of risk-weighted assets:

- pledge on movable property;
- pledge on receivables;
- pledge on shares and bonds;
- other types as defined in the Group Catalogue of collaterals.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Data on the type and value⁵ of collateral and guarantees by sector providers and categories of receivables as at 31 December 2017:

	Type of collateral up to amount of receivables (as it is in KA4)				RSD thousand
	Deposits	Residential real estate	Other real estate	Other assets	Guarantees issued by the state
Receivables from retail	69,863	19,349,080	203,014	365,913	-
Housing loans	28,057	19,276,792	134,661	-	-
Consumer and Cash Loans	40,136	41,307	18,941	-	-
Transactional and Credit Card	1,670	-	-	-	-
Other receivables	-	30,980	49,412	365,913	-
Receivables from corporate clients	1,006,614	399,970	13,167,610	4,968,524	1,423,601
Large entities	-	-	4,594,590	504,775	-
Small and medium-sized entities	695,762	252,921	7,333,823	3,214,431	-
Micro enterprises and entities	309,764	134,602	1,106,358	659,256	-
Agricultural producers	1,088	12,448	132,839	408	-
Public companies	-	-	-	589,653	1,423,601
From other clients	134,313	77,207	833,916	56,598	-
Total exposure	1,210,789	19,826,257	14,204,540	5,391,035	1,423,601
According to categories of receivables	-	-	-	-	-
Non-problematic receivables	1,210,653	19,208,700	12,919,521	5,385,651	1,423,601
of which: restructured	-	112,366	3,345	-	-
Problematic receivables	136	617,558	1,285,019	5,384	-
of which: restructured	-	181,246	964,967	-	-
Total exposure	1,210,789	19,826,257	14,204,540	5,391,035	1,423,601

⁵ The value of collaterals is determined based on estimation of authorized estimator (or based on some other document according to the type of collateral), with possible internal correction, after which the effective rate (collateral haircut) is used in accordance with the catalog of collateral and decreased for the previous load.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Data on the type and value of collateral and guarantees by sector providers and categories of receivables as at 31 December 2016:

	Type of collateral up to amount of receivables (as in KA4)				RSD thousand
	Deposits	Residential real estate	Other real estate	Other assets	Guarantees issued by the state
Receivables from retail	56,995	13,130,492	159,691	275,739	-
Housing loans	709	13,047,937	87,735	-	-
Consumer and Cash Loans	53,736	44,635	21,475	-	-
Transactional and Credit Card	2,493	-	-	-	-
Other receivables	57	37,921	50,481	275,739	-
Receivables from corporate clients	2,300,550	663,321	13,382,283	4,309,850	2,471,235
Large entities	464,658	0	2,055,498	409,365	-
Small and medium-sized entities	1,497,902	378,762	9,216,994	3,057,065	-
Micro enterprises and entities	337,990	255,560	1,968,667	636,138	-
Agricultural producers	0	28,999	141,125	638	-
Public companies	0	0	0	206,645	2,471,235
From other clients	161,850	33,765	1,274,234	34,486	-
Total exposure	2,519,395	13,827,578	14,816,208	4,620,074	2,471,235
According to categories of receivables					-
Non-problematic receivables	2,518,664	12,989,411	13,060,355	4,607,483	2,471,235
of which: restructured	0	145,485	252,750	-	-
Problematic receivables	731	838,168	1,755,854	12,592	-
of which: restructured	-	257,284	979,081	-	-
Total exposure	2,519,395	13,827,578	14,816,208	4,620,074	2,471,235

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
32. RISK MANAGEMENT (continued)
32.2. Credit Risk (continued)

During 2017, the Group had the following assets acquired through collection of receivables.

Types of assets acquired through collection of receivables	RSD thousand		
	Residential real estate	Other assets acquired through collection	Total
Gross amount at the beginning of the period*	13,901	364	14,265
Acquired during the period	-	-	0
Sold during the period	1,828	-	1,828
Gross amount at the end of the period	12,073	364	12,437
Accumulated impairment	12,073	14	12,087
of which: allowance for impairment during the period	-	14	14
Net value at period end	-	350	350

During 2016, the Group had the following assets acquired through collection of receivables.

Types of assets acquired through collection of receivables	RSD thousand		
	Residential real estate	Other assets acquired through collection	Total
Gross amount at the beginning of the period*	85,785	406	86,191
Acquired during the period	-	67	67
Sold during the period	71,884	-	71,884
Gross amount at the end of the period	13,901	473	14,374
Accumulated impairment	13,009	109	13,118
of which: allowance for impairment during the period	-	109	109
Net value at period end	892	364	1,256

Basic principles of takeover and management of pledged property are regulated by the Procedure on the takeover of pledged asset in enforced collection procedure. Overtaken objects are mostly real estate and movable assets.

Basic principles to overtake assets (fixed and mobile) which have to be taken in consideration include analysis of market value and potential marketability of assets taken into consideration, which must be supported with expected sales revenue, which will lead uncollected receivable to the highest level possible. In case when the Group make a decision on overtake the asset, analysis are done with the net present value method. Depending on the characteristics of assets, type of asset (real estate, movable property) can be further divided into primary and secondary when takeover is taken into consideration, depending on their purpose and other characteristics, such as location, type, technical standards, equipment, year of construction and similar, as well as market situation in terms of supply and demand of certain type of collaterals. All above-mentioned parameters affect the final decision on implementation of the takeover procedure.

As strategies for management of assets collected through collection of receivables, the Group applies sale, rent, development, retention, respectively combination of mentioned strategies. Suggestion of strategy must involve a real plan in terms of implementation of strategy. Estimated related expenses, income and effect on profit and loss must be taken in consideration. In case of suggesting retention strategy, cost of maintenance must be clearly presented in assets strategy.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
32. RISK MANAGEMENT (continued)
32.2. Credit Risk (continued)
LTV ratio

The table below presents the so-called "LTV" ratio for housing loans, which represent a part of total retail loans.

	RSD thousand	
Value of the LTV indicator	The value of receivables secured by mortgages on real estate as at 31 Dec 2017	The value of receivables secured by mortgages on real estate as at 31 Dec 2016
below 50%	3,823,580	2,731,984
from 50% to 70%	5,736,344	3,608,271
from 70% to 90%	11,506,367	5,136,903
from 90% to 100%	643,842	621,895
from 100% to 120%	1,064,246	1,229,669
from 120% to 150%	996,352	1,166,782
over 150%	1,588,935	1,842,702
Total exposure	25,359,666	16,338,208
Average LTV	78.5%	91.8%

Assessment of impairment of financial assets

The Group assesses impairment, or the calculation of impairment recognized in the Balance Sheet and the provision for losses on off-balance sheet items in accordance with International Accounting Standards (hereinafter: IAS) / International Financial Reporting Standards (hereinafter: IFRS).

The calculation of the impairment of the Group includes a Special provision (individually or based on rules) and the General provision (on a group basis).

Special provisions are made to clients' exposures in the status of default, or impaired exposures. Exposure is considered impaired when it is probable that the Group will not be able to collect all contractual amounts or when the client is in the status of default. More specifically, the Group through an analysis of impairment determines whether there is objective evidence of impairment of receivables from clients.

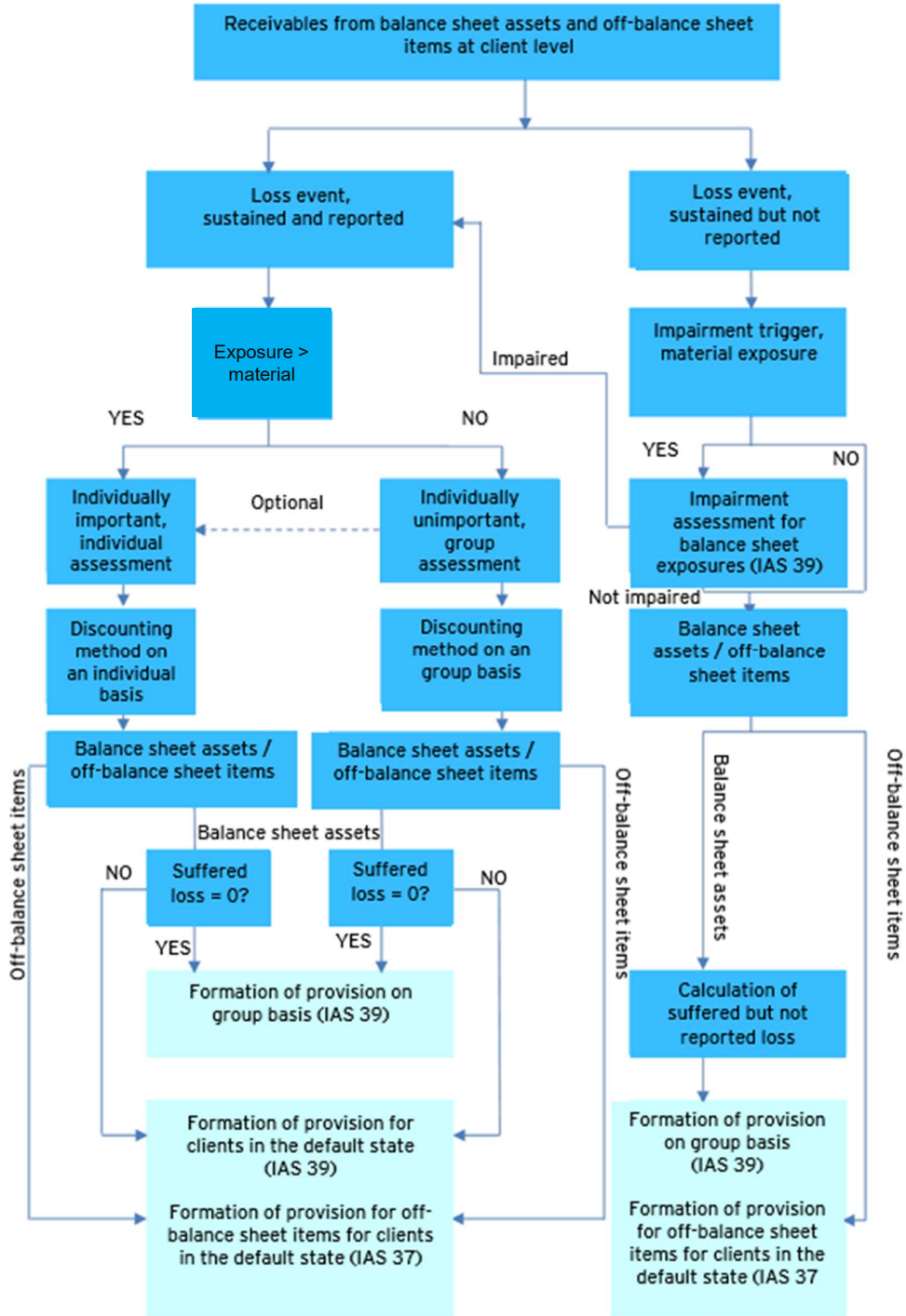
General provision (on a group basis) are applied to receivables where there is no objective evidence of impairment and is formed to cover the incurred but not detected loss, or in a situation where the right impairment is not yet created. For these receivables, the impairment is calculated even though there is no evidence of impairment, since experience shows that some of them will eventually enter the status of default. Allowance for impairment on a group basis is formed for loans that were subject to individual assessment but were not identified as impairment.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

The process of forming impairment applied within the Group is shown here:



**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

If client (or client's financial asset) is impaired, then he should already be in default status or he should have his rating reduced to default rating, if client had been previously assigned with „performing“ rating. On the other side, if client is in default status, he does not have to be impaired, but impairment process is started.

Beside clients who are in default status, when impairment process is automatically started, for „performing“ clients, impairment test is being carried out, if any of defined impairment drivers has been triggered, for individually significant clients. Impairment test as comparison of gross book value and discounted, estimated cash flow, is relevant only for balance sheet exposure.

Calculation of special provision

For every impaired exposure above threshold of materiality allowance for impairment is calculated by discounting cash flows. The Group considers client as individually important if his exposure is above RSD 5,000,000.

According to discontinued cash flow method, expected cash flow from client's operations and on basis of realisation of collateral are estimated by authorized employee of Department for restructuring and collection of loans (Workout manager) and Department for collection of receivables from corporate clients. Allowance for impairment is difference between book value of impaired loan and current value of expected cash flows, discounted with effective interest rate for that loan.

For impaired exposures that are not considered individually important, calculation is being done automatically based on the rules. Clients who are part of this sub-portfolio are classified by criteria of regularity in payment of liabilities.

Calculation of general provision

Receivables that do not provide objective evidence of impairment are classified in groups on basis of similar credit risk characteristics and their appropriate group allowance for impairment is calculated in compliance with group characteristics and credit risk level.

The Group uses the formula $PLL = EaD \times PD \times LGD \times LIP$ to calculate the resulting but unreported loss, where:

- EaD – Exposure at default
- PD – Probability of default
- LGD – Loss given default
- LIP – Loss identification period

PD is a probability that performing client will get in default in a 12 month period, minimal standards for valuation of model and monitoring processes are set and described in Group's Policy for framework of classification and rules of classification (rating).

For performing portfolio, LGD is determined on basis of expert opinion of Group's management (taking care of collateral coverage) and parameters of standard approach according to Basel II.

The Group verifies methodology and assumptions used for estimating future cash flows in order to reduce differences between estimated and occurred losses through Back-testing analysis that is conducted once a year.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Information on changes of impaired receivables in 2017:

	Gross value at the beginning of the period	Receivables that are impaired during the year		Receivables that have ceased to be impaired during the year		Other changes	RSD thousand	
		Total	of which: impaired on an individual basis	Total	of which: were impaired on an individual basis		Gross value at period end	Net value at period end
Receivables from retail	2,172,429	548,250	115,355	312,486	64,810	(978,289)	1,429,904	569,502
Housing loans	777,836	164,668	115,355	106,447	64,810	(116,179)	719,877	352,160
Consumer and Cash Loans	1,050,140	315,139	-	169,519	-	(671,576)	524,184	186,013
Transactional and Credit Card	54,330	14,054	-	7,413	-	(41,081)	19,890	6,212
Other receivables	290,124	54,389	-	29,107	-	(149,453)	165,953	25,117
Receivables from corporate clients	3,115,624	79,307	60,325	284,113	250,440	(1,303,697)	1,607,122	401,698
Large entities	32,997	-	-	-	-	383,688	416,685	101,475
Small and medium-sized entities	1,932,552	52,093	48,975	101,913	76,785	(1,108,689)	774,044	144,056
Micro enterprises and entities	749,529	9,664	-	19,153	12,565	(385,531)	354,509	141,376
Agricultural producers	75,796	17,549	11,350	1,957	-	(31,841)	59,547	14,791
Public companies	324,750	-	-	161,090	161,090	(161,324)	2,336	-
From other clients	1,445,017	1,634	-	52,125	50,810	(713,443)	681,084	90,222
Total receivables	6,733,070	629,191	175,680	648,723	366,060	(2,995,429)	3,718,109	1,061,422

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Information on changes of impaired receivables in 2016:

	Gross value at the beginning of the period	Receivables that are impaired during the year		Receivables that have ceased to be impaired during the year		Other changes	RSD thousand	
		Total	of which: impaired on an individual basis	Total	of which: were impaired on an individual basis		Gross value at period end	Net value at period end
Receivables from retail	2,524,068	627,012	152,331	437,992	75,909	(540,659)	2,172,429	668,360
Housing loans	781,992	191,790	117,536	120,117	75,909	(75,829)	777,836	437,628
Consumer and Cash Loans	1,314,167	337,369	29,302	228,404	-	(372,992)	1,050,140	188,716
Transactional and Credit Card	89,734	17,578	-	16,564	-	(36,418)	54,330	6,205
Other receivables	338,175	80,275	5,492	72,907	-	(55,420)	290,124	35,811
Receivables from corporate clients	3,974,850	606,698	558,123	271,926	179,664	(1,179,021)	3,130,601	711,220
Large entities	7,082	32,997	32,781	-	-	919	40,998	2,055
Small and medium-sized entities	2,637,512	424,866	397,996	179,429	136,541	(943,439)	1,939,510	420,748
Micro enterprises and entities	872,144	142,812	127,346	74,949	40,153	(190,460)	749,546	252,705
Agricultural producers	124,445	6,024	-	17,548	2,969	(37,124)	75,796	19,976
Public companies	333,667	-	-	-	-	(8,916)	324,751	15,735
From other clients	2,341,583	64	-	493,630	476,773	(417,977)	1,430,040	312,276
Total receivables	8,840,501	1,233,774	710,454	1,203,548	732,345	(2,137,657)	6,733,070	1,691,855

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Information on changes of impaired receivables in 2017:

	Accumulated allowance for impairment at the beginning of year	Allowances for impairment recognized during the period	Reversal of impairment during the period	Other changes	RSD thousand Accumulated allowance for impairment at the end of year
Receivables from retail	2,303,204	3,051,833	2,798,175	(910,743)	1,646,119
Housing loans	537,581	1,175,263	940,417	(110,912)	661,516
Consumer and Cash Loans	1,360,438	1,597,650	1,568,150	(617,582)	772,357
Transactional and Credit Card	76,620	124,069	137,966	(33,705)	29,018
Other receivables	328,564	154,851	151,643	(148,544)	183,228
Receivables from corporate clients	3,295,405	3,132,679	3,303,221	(1,145,815)	1,979,048
Large entities	217,751	382,834	426,751	248,760	422,593
Small and medium-sized entities	2,015,423	1,914,794	2,009,308	(886,211)	1,034,698
Micro enterprises and entities	683,687	685,628	557,402	(386,444)	425,470
Agricultural producers	61,397	57,514	33,845	(30,734)	54,331
Public companies	317,147	91,909	275,915	(91,185)	41,956
From other clients	1,196,382	775,659	939,264	(386,309)	646,467
Total receivables	6,794,991	6,960,171	7,040,661	(2,442,867)	4,271,634
By category of receivables					
Non-problematic receivables	1,745,971	4,455,869	4,760,395	156,807	1,598,252
of which: restructured	19,739	45,891	57,620	18,491	26,501
Problematic receivables	5,049,021	2,504,302	2,280,266	(2,599,675)	2,673,382
of which: restructured	1,513,782	541,282	349,570	(511,111)	1,194,383
Total receivables	6,794,991	6,960,171	7,040,661	(2,442,867)	4,271,634

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Information on changes of impaired receivables in 2016:

					RSD thousand
	Accumulated allowance for impairment at the beginning of year	Allowances for impairment recognized during the period	Reversal of impairment during the period*	Other changes	Accumulated allowance for impairment at the end of year
Receivables from retail	2,346,209	3,925,440	3,710,452	(257,993)	2,303,204
Housing loans	382,048	1,433,887	1,278,203	(150)	537,581
Consumer and Cash Loans	1,477,316	1,914,917	1,807,334	(224,461)	1,360,438
Transactional and Credit Card	104,629	185,940	200,345	(13,604)	76,620
Other receivables	382,215	390,697	424,570	(19,778)	328,564
Receivables from corporate clients	3,802,498	4,340,030	3,985,255	(861,867)	3,295,406
Large entities	117,025	521,421	420,921	226	217,751
Small and medium-sized entities	2,497,411	2,749,058	2,573,136	(657,908)	2,015,424
Micro enterprises and entities	749,734	796,862	691,208	(171,701)	683,687
Agricultural producers	103,493	76,031	69,469	(48,658)	61,397
Public companies	334,835	196,659	230,521	16,174	317,147
From other clients	1,777,554	1,137,707	1,207,746	(511,134)	1,196,382
Total receivables	7,926,261	9,403,178	8,903,454	(1,630,993)	6,794,991
By category of receivables					
Non-problematic receivables	1,355,834	5,328,666	5,254,719	316,190	1,745,971
of which: restructured	5,344	47,581	31,567	(1,620)	19,739
Problematic receivables	6,570,427	4,074,511	3,648,735	(1,947,183)	5,049,021
of which: restructured	1,430,071	908,456	625,799	(198,945)	1,513,782
Total receivables	7,926,261	9,403,178	8,903,454	(1,630,993)	6,794,991

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Information on the calculated interest income and the interest collected

	RSD thousand			
	Income from Interest	Collected interest	Interest income on impaired receivables	Collected interest on impaired receivables
Receivables from retail	3,027,019	2,764,069	289,789	51,275
Housing loans	790,550	727,825	68,687	10,499
Consumer and Cash Loans	1,968,255	1,802,786	178,355	33,373
Transactional and Credit Card	148,193	129,360	20,878	2,350
Other receivables	120,021	104,099	21,869	5,053
Receivables from corporate clients	2,499,980	2,175,225	163,157	11,329
Large entities	357,747	342,473	14,225	-
Small and medium-sized entities	1,450,123	1,348,123	85,942	7,465
Micro enterprises and entities	546,890	346,068	51,096	2,694
Agricultural producers	30,341	19,949	11,799	1,170
Public companies	114,879	118,611	95	-
From other clients	1,847,155	1,783,817	44,314	1,038
Total receivables	7,374,155	6,723,111	497,260	63,641
By category of receivables				
Non-problematic receivables	6,867,207	6,649,033	2,250	-
of which: restructured	16,830	14,788	478	-
Problematic receivables	506,948	74,079	495,010	63,641
of which: restructured	104,465	20,459	93,496	11,079
Total receivables	7,374,155	6,723,111	497,260	63,641

Interest income on loans accounted for in accordance with IAS 39 on effective interest rate, which is the rate that discounts estimated future payments or receipts through the expected life of the loans to the net present value of investments.

In determining the effective interest rate all contractual terms relating to the financial instrument are taken into account, but not future credit losses.

With impaired loans, revenue is recognized in the income level specified using the effective interest rate on the net book value (book value minus the impairment).

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017****32. RISK MANAGEMENT (continued)****32.2. Credit Risk (continued)*****Required reserves for estimated losses***

The Group additionally, in accordance with the Decision of the National Bank of Serbia on the Classification of Balance Sheet Assets and Off-balance sheet items calculates reserves for estimated losses that may occur on balance sheet assets and off-balance sheet items and determines the amount of required reserves for potential losses, which is the sum of the positive difference between the reserve for estimated losses calculated and the determined amount of impairment of balance sheet assets and provisions for losses on off-balance sheet items at the level of the debtor.

The required reserve for estimated losses on balance sheet assets and off-balance sheet items, is presented as a deduction on the Group's equity in accordance with the decision on capital adequacy of banks, except in the case when the term from clause 34a of the Decision of the National Bank of Serbia on the Classification of Balance Sheet Assets and Off-balance sheet items is satisfied ("Official Gazette RS", no. 94/2011, 57/2012, 123/2012, 43/2013, 113/2013, 135/2014, 25/2015, 38/2015, 61/2016, 69/2016, 91/2016 и 101/2017 и 114/2017). In accordance with the stated above, the Group does not classify required reserves for estimated losses as a deductible items of the capital.

Restructured loans

Where possible, the Group seeks to restructure loans rather than realize collaterals. This may involve extending the payment or any other modification of the initial conditions of lending. Reprogramming can be a business restructuring or forbearance by definition of EBA.

Business reprogramming includes changes to the initial contractual terms, which are not conditioned by the worsening financial position of the debtor, or the mitigation of the deteriorating financial position and does not constitute restructuring. It is the result of a changed situation on the market (customers, suppliers, competitors) and the need for the existing dynamics and conditions of the loan to be adjusted to the new situation.

Forbearance presents a restructuring caused by:

- the debtors' inability to meet their contractual obligations due to financial difficulties and
- the Groups need to make certain compromises so the client could service his contractual obligations.

Performing forbearance - is the starting category within the forbearance principle and is granted in case of a defined deterioration in the financial position of the client, or his creditworthiness, registered delay over 30 days in the last 3 months before applying for reprogramming or other non-compliance with contractual terms towards the Group. The minimum validity period of this status is 2 years, during which the client must pay a min % of the total debt yearly and at the end of the period must not have a delay of over 30 days (during this period of delay shall not exceed 90 days).

Performing forbearance under probation - the subcategories within the Performing Forbearance status in which the client moves from Non performing forbearance or Defaulted forbearance status after the expiry of the monitoring period, in which conditions must be met cumulatively: the maximum delay during the monitoring period, no days of delay at the end of the monitoring period and recorded positive financial developments which indicates that the ability of the borrower to regularly meet contractual obligations in the future. Performing Forbearance under probation lasts for a maximum of 2 years, and upon expiry, if all conditions are fulfilled, the client leaves the Forbearance status.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Restructured loans (continued)

Non performing forbearance status is granted in the following cases:

- the client does not carry out the final restructuring after a period of 18 m from giving the status of "temporary measures";
- the occurrence of any events of default which are not related to restructuring during the performing forbearance status;
- delays over 30 days with a client who is Performing Forbearance under probation status;
- If a client under Performing Forbearance under probation status, is granted a new reprogramming in the second year of the status

Monitoring period for clients with NPF status lasts for one year after which, in case of fulfilment of the defined conditions, it moves into the Performing forbearance under probation status.

Distress reprogramming / restructuring (defaulted forbearance) is a form of restructuring in which the client receives the status of default. This way, the entire scope of exposure (or its biggest part) and is always conditioned by a significant deterioration in the creditworthiness of the client. Distress reprogramming is granted every time a client has rating of R at the time of approval of reprogramming, when the client is not employed (only for individuals), and when the client is approved with a second reprogramming, and it's been less than 2 years from the initial authorization of rescheduling.

Temporary measures - temporary measures do not imply the final restructuring but a middle step to the final implementation of the restructuring. It usually occurs in situations when there is a larger number of lenders with a specific client and a longer period of time is required due to internal processes and procedures of each creditor, in order to define the final model of the restructuring (example – in situations resorting in stand-still agreements or moratorium as a transitional solution to the final restructuring). The duration of interim measures is limited to 18 months.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

The Group continuously reviews restructured loans to ensure the fulfilment of all criteria, as well as future payments or timely assignment of the default status to a client who fails to comply with defined criteria.

Information on restructured receivables as at 31 December 2017:

	The gross value of total receivables	Accumulated allowance for impairment of total receivables	The gross value of restructured receivables		Accumulated allowance for impairment restructured receivables	% Of restructured receivables	RSD thousand
			Total	of which: problematic receivables			Value of the collaterals of restructured receivables *
Receivables from retail clients	47,806,978	1,646,119	742,951	463,530	189,385	1.55	284,190
Housing loans	25,359,666	661,519	442,664	260,854	114,017	1.75	283,080
Consumer and Cash Loans	19,445,288	772,354	280,277	189,359	67,433	1.44	1,109
Transactional and Credit Card	797,249	29,018	-	-	-	-	-
Other receivables	2,204,776	183,228	20,010	13,317	7,934	0.91	-
Receivables from corporate clients	57,283,690	1,823,185	1,042,041	1,018,873	755,991	1.82	699,352
Sector A	2,429,555	103,212	70,411	47,243	41,244	2.90	0
Sector B, C, E	14,470,866	667,157	621,159	621,159	451,343	4.29	551,080
Sector D	5,674,910	79,971	-	-	-	-	-
Sector F	10,677,961	189,842	119,208	119,208	113,046	1.12	25,697
Sector G	11,479,578	524,837	224,072	224,072	148,919	1.95	115,384
Sector H, I, J	5,700,486	94,997	0	0	0	0.00	0
Sector L, M, N	6,850,334	163,169	7,191	7,191	1,440	0.10	7,191
Receivables from other clients	11,852,909	802,331	320,813	315,188	275,508	2.71	278,381
Total receivables	116,943,578	4,271,635	2,105,804	1,797,591	1,220,884	1.80	1,261,923

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

The Group continually reviews restructured loans to ensure the fulfilment of all criteria, as well as future payments or timely assignment of default status of a client who fails to comply with defined criteria.

Information on restructured receivables as at 31 December 2016:

	RSD thousand						
	The gross value of total receivables	Accumulated allowance for impairment of total receivables	The gross value of restructured receivables		Accumulated allowance for impairment restructured receivables	% Of restructured receivables	Value of the collaterals of restructured receivables *
			Total	of which: problematic receivables			
Receivables from retail clients	35,378,763	2,303,204	733,777	483,494	172,826	2.07	267,190
Housing loans	16,358,431	537,581	444,292	266,328	79,890	2.72	266,463
Consumer and Cash Loans	15,533,677	1,360,438	262,263	196,261	77,534	1.69	727
Transactional and Credit Card	867,191	76,620	-	-	-	-	-
Other receivables	2,619,464	328,564	27,223	20,905	15,402	1.04	-
Receivables from corporate clients*	57,910,058	2,782,317	1,389,051	1,098,488	825,674	2.40	912,521
Sector A	2,505,384	175,721	151,453	50,542	38,160	6.05	151,453
Sector B, C, E	15,955,584	914,772	392,963	262,981	182,449	2.46	144,487
Sector D	5,875,234	101,494	-	-	-	-	-
Sector F	10,643,058	408,067	136,784	136,784	127,233	1.29	35,139
Sector G	9,829,060	831,531	678,370	618,700	462,628	6.90	561,744
Sector H, I, J	7,954,467	165,751	22,348	22,348	14,585	0.28	12,565
Sector L, M, N	5,147,271	184,982	7,133	7,133	618	0.14	7,133
Receivables from other clients	11,179,159	1,709,471	685,611	675,292	535,022	6.13	454,889
Total receivables	104,467,979	6,794,991	2,808,438	2,257,274	1,533,521	2.69	1,634,600

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Information on changes in restructured receivables in 2017:

						RSD thousand	
	Gross amount at beginning of the period	Receivables restructured during the period	Receivables which ceased to be restructured during the period	Other changes	Gross amount at period end	Net amount at period end	
Receivables from retail	733,777	273,968	154,729	(110,065)	742,951	553,567	
Housing loans	444,292	130,404	93,689	(38,342)	442,664	328,648	
Consumer and Cash Loans	262,263	134,037	56,734	(59,288)	280,277	212,844	
Other receivables	27,223	9,527	4,305	(12,435)	20,010	12,075	
Receivables from corporate clients	1,592,923	55,765	526,574	(54,601)	1,067,513	296,327	
Large entities	-	-	-	416,085	416,085	101,115	
Small and medium-sized entities	1,180,141	10,281	330,165	(406,059)	454,198	86,318	
Micro enterprises and entities	237,845	45,484	35,183	(59,314)	188,832	104,648	
Agricultural producers	13,711	-	-	(5,313)	8,398	4,246	
Public companies	161,225	-	161,225	-	-	-	
Receivables from other clients	481,739	-	-	(186,398)	295,341	35,027	
Total receivables	2,808,438	329,733	681,302	(351,064)	2,105,805	884,921	

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Information on changes in restructured receivables in 2016:

						RSD thousand	
	Gross amount at beginning of the period	Receivables restructured during the period	Receivables which ceased to be restructured during the period	Other changes	Gross amount at period end	Net amount at period end	
Receivables from retail	386,447	437,490	71,123	(19,037)	733,777	560,952	
Housing loans	238,755	239,328	27,801	(5,989)	444,292	364,402	
Consumer and Cash Loans	97,721	197,180	21,860	(10,779)	262,263	184,729	
Other receivables	49,971	983	21,462	(2,269)	27,223	11,821	
Receivables from corporate clients	1,646,710	372,952	154,648	(272,091)	1,592,923	585,664	
Small and medium-sized entities	1,065,706	325,508	48,020	(163,052)	1,180,141	461,426	
Micro enterprises and entities	389,184	37,099	93,721	(94,717)	237,845	112,231	
Agricultural producers	16,285	10,345	12,907	(12)	13,711	12,008	
Public companies	175,535	-	-	(14,310)	161,225	-	
Receivables from other clients	257,456	434,035	174,034	(35,719)	481,739	128,301	
Total receivables	2,290,613	1,244,478	399,806	(326,847)	2,808,438	1,274,917	

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Information on the structure of restructured receivables by restructuring measures in 2017:

							RSD thousand
	Capitalization of delay	Grace period	Extension of the repayment period	Change of interest rate	A partial write-off	Other measures	Total
Receivables from retail	531,655	8,856	515,304	615,951	62,831	-	742,951
Housing loans	315,783	8,530	216,435	322,131	62,108	-	442,664
Consumer and Cash Loans	211,479	326	278,919	275,414	724	-	280,277
Transactions and credit cards	-	-	-	-	-	-	-
Other receivables	4,393	-	19,950	18,406	-	-	20,010
Receivables from corporate clients	937,564	701,744	1,039,413	827,857	125,884	2,279	1,067,513
Large entities	416,085	416,085	416,085	416,085	-	-	416,085
Small and medium-sized entities	351,433	239,760	454,198	276,418	98,700	-	454,198
Micro enterprises and entities	161,648	42,553	165,664	130,301	27,184	-	188,832
Agricultural producers	8,398	3,345	3,466	5,053	-	2,279	8,398
Public companies	-	-	-	-	-	-	-
Receivables from other clients	295,341	295,341	295,341	295,341	295,341	295,341	295,341
Total Receivables	1,764,560	1,005,941	1,850,058	1,739,149	484,056	297,620	2,105,805

Overview according to restructuring measures is presented by each applied measure, regardless of whether any other measures is applied.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Information on the structure of restructured receivables by restructuring measures in 2016:

							RSD thousand
	Capitalization of delay	Grace period	Extension of the repayment period	Change of interest rate	A partial write-off	Other measures	Total
Receivables from retail	501,338	15,267	502,853	546,207	45,996	-	733,777
Housing loans	288,487	14,821	218,316	266,248	41,333	-	444,292
Consumer and Cash Loans	211,304	446	257,707	256,581	4,663	-	262,263
Other receivables	1,546	-	26,830	23,378	-	-	27,223
Receivables from corporate clients	833,942	801,740	1,300,887	1,049,328	613,676	568,913	1,592,923
Small and medium-sized entities	746,528	740,364	1,001,469	807,407	423,649	307,804	1,180,141
Micro enterprises and entities	73,702	53,581	133,934	75,136	28,801	97,527	237,845
Agricultural producers	13,711	7,796	4,259	5,559	-	2,356	13,711
Public companies	-	-	161,225	161,225	161,225	161,225	161,225
Receivables from other clients	434,035	434,035	481,739	479,487	-	-	481,739
Total Receivables	1,769,315	1,251,043	2,285,478	2,075,022	659,672	568,913	2,808,438

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Loan Concentration Risk

The concentration risk is the risk of incurring losses due to an excessive volume of Group's placements into a certain group of debtors or individual debtor. The concentration occurs when a significant number of debtors belong to the similar industry or the same geographical area or when they have similar economic characteristics, they are exposed to the same factors that affect the income and expenditures, which may affect their ability to settle their contractual obligations in case of changes in economic, political or some other circumstances that affect them equally. In order to minimize the credit risk, safety measures are established through defining levels of exposures and credit limits and regular monitoring of compliance with the established limits. Also, on a regular annual basis the Group carries out a detailed and comprehensive analysis of concentrations of credit (and other) risks across different dimensions (exposure classes, economic sectors, collateral, products, etc.).

The Group manages the concentration risk of the credit portfolio through the framework set by the Concentration risk management policy (with belonging Procedure), regulatory limits are defined by the Decision on Risk Management of the Bank, internally defined limits and limits defined by the Policy for determining exposure limits (with belonging Procedure).

Using the Concentration risk management policy the Group has defined monitoring exposures to credit risk by each of the following categories: concentrations by classes of exposure (Basel exposure classes), concentration by clients rating, concentration by corporate clients, real estate and micro clients, by industry sector, concentration by exposures to individual clients in the overall loan portfolio, the portfolio of corporate clients, banks and states, concentration of collaterals, concentration by currency and by product. For the purposes of determining the concentration of credit risk the Herfindahl-Hirschman Index (HHI) and Moody's matrix are being used.

According to the Decision on the management of risks, the Group analyses exposure to credit risk through the following two indicators:

- Exposure to a single entity or group of related entities that cannot be higher than 25% of the Group's capital,
- The sum of large exposures, which cannot be higher than 400% of the Group capital.

In addition, for monitoring purposes the Group has retained as an internal limit an indicator that was previously defined by regulations, and by which exposure to related entities of the Group cannot be higher than 20% of the Group capital.

By the Policy for managing credit risks, the Group has defined monitoring concentrations of credit risk for corporate customers, financial institutions and states at the following levels: maximum limit of exposure, maximum exposure limit based on rating and operating maximum limit of exposure.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Information on sectoral and the geographical concentration of exposure as at 31 December 2017:

	RSD thousand											
	Belgrade region		Region of Vojvodina		Region: Sumadija and West Serbia		Region: South and East Serbia		Region: Kosovo and Metohija		Foreign countries	
	Non-problematic receivables	Problematic receivables	Non-problematic receivables	Problematic receivables	Non-problematic receivables	Problematic receivables	Non-problematic receivables	Problematic receivables	Non-problematic receivables	Problematic receivables	Non-problematic receivables	Problematic receivables
Receivables from retail customers	17,505,175	438,753	18,860,440	685,439	6,223,002	318,020	3,174,294	140,334	453,989	1,401	6,106	24
Housing loans	11,478,867	209,464	9,542,436	365,807	2,422,224	151,157	1,069,363	68,099	46,193	-	6,055	-
Consumer and Cash Loans	5,210,635	167,627	7,979,112	253,033	3,368,872	123,022	1,899,887	55,661	386,049	1,391	-	-
Transactional and Credit Card	145,052	5,080	467,842	9,677	108,698	3,331	51,401	2,101	4,066	-	-	-
Other receivables	670,622	56,581	871,049	56,922	323,208	40,509	153,643	14,473	17,682	11	52	24
Receivables from corporate clients*	26,860,748	681,734	17,974,425	479,604	6,880,845	161,912	4,055,342	188,248	830	-	-	-
Sector A	526,878	1,161	1,756,728	52,878	21,682	2	50,359	19,867	-	-	-	-
Sector B, C, E	2,292,745	424,206	5,975,966	157,419	3,024,870	40,230	2,505,718	49,711	-	-	-	-
Sector D	2,697,882	-	273,440	-	2,034,904	-	668,683	-	-	-	-	-
Sector F	7,382,984	3,317	2,723,837	8,237	272,512	3	175,461	111,611	-	-	-	-
Sector G	5,438,922	162,507	4,124,531	212,564	894,261	112,354	527,883	5,728	830	-	-	-
Sector H, I, J	3,190,404	4,706	1,832,058	3,116	551,931	9,323	107,932	1,016	-	-	-	-
Sector L, M, N	5,330,933	85,837	1,287,864	45,390	80,687	-	19,307	315	-	-	-	-
Receivables from other clients	5,251,408	185,058	3,755,518	376,143	418,168	185,555	407,710	29,950	-	-	1,243,156	-
Total exposure	49,617,332	1,305,545	40,590,382	1,541,187	13,522,015	665,487	7,637,346	358,532	454,819	1,401	1,249,263	24

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Information on sectoral and the geographical concentration of exposure as at 31 December 2016:

	RSD thousand											
	Belgrade region		Region of Vojvodina		Region: Sumadija and West Serbia		Region: South and East Serbia		Region: Kosovo and Metohija		Foreign countries	
	Non-problematic receivables	Problematic receivables	Non-problematic receivables	Problematic receivables	Non-problematic receivables	Problematic receivables	Non-problematic receivables	Problematic receivables	Non-problematic receivables	Problematic receivables	Non-problematic receivables	Problematic receivables
Receivables from retail customers	10,919,978	679,497	14,489,069	996,618	5,012,906	456,358	2,345,036	202,727	266,228	1,870	8,464	12
Housing loans	6,026,950	232,081	7,014,390	397,691	1,705,729	164,726	722,678	72,027	13,744	0	8,414	-
Consumer and Cash Loans	4,070,506	334,216	5,954,633	462,921	2,776,574	220,610	1,371,208	100,529	240,712	1,768	-	-
Transactional and Credit Cards	146,477	13,044	496,411	31,118	115,430	6,279	51,800	4,261	2,342	29	-	-
Other receivables	676,045	100,155	1,023,635	104,888	415,172	64,743	199,351	25,909	9,430	73	50	12
Receivables from corporate clients*	27,051,427	949,224	18,448,085	964,448	6,165,812	474,653	3,647,289	209,110	-	10	-	-
Sector A	421,636	1,051	1,855,821	19,684	17,575	112,992	24,926	51,697	-	-	-	-
Sector B, C, E	3,366,291	389,434	5,850,701	332,781	3,029,737	200,904	2,775,597	10,139	-	-	-	-
Sector D	2,833,815	-	984,963	-	1,569,964	-	486,492	-	-	-	-	-
Sector F	6,909,309	183,080	2,962,305	13,390	426,567	3	20,157	128,247	-	-	-	-
Sector G	3,704,921	218,827	4,428,119	516,162	548,453	150,998	247,246	14,325	-	10	-	-
Sector H, I, J	5,676,100	56,353	1,556,385	30,103	553,294	9,756	68,742	3,734	-	-	-	-
Sector L, M, N	4,139,355	100,479	809,791	52,328	20,222	-	24,129	968	-	-	-	-
Receivables from other clients	4,006,165	762,395	3,456,970	821,029	747,686	219,038	170,919	166,396	-	-	828,562	-
Total exposure	41,977,570	2,391,116	36,394,123	2,782,095	11,926,404	1,150,048	6,163,243	578,234	266,228	1,880	837,026	12

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.2. Credit Risk (continued)

Credit-related Risks

Credit risk includes residual risk, dilution risk, settlement / delivery risk, counterparty risk and foreign exchange credit risk. The Group overcomes risks which are related to credit risk using the same control processes and procedures which are used for credit risk.

Counterparty risk

The Group operates with derivative financial instruments which gives way to the exposure to counterparty risk, i.e. the risk of default of the counterparty in the transaction before the final settlement of cash flows arising from the transaction.

Credit risk of derivatives is limited by determining the maximum limit for each derivative financial instrument, based on its type, maturity and credit quality of the client.

32.3. Liquidity Risk and Funding Management

Liquidity risk is the risk that the Group would not be able to discharge its liabilities when they fall due. To reduce or to limit this risk, management has arranged diversified funding sources, manages assets with liquidity in mind, and monitors future cash flows and liquidity on a daily basis.

This incorporates an assessment of expected cash flows in Dinars and foreign currency and the availability of high grade collateral which could be used to secure additional funding, if required. The Group manages its assets and liabilities in such a way that it can meet its due liabilities at all time, as well as to have customers disposing their funds held with the Group in accordance with agreed terms.

Liquidity risk management in the Group is defined by policies, procedures and regulations approved by the Managing Committee and Executive Committee and which are in compliance with the risk management strategy at the level of Erste Group, as well as with all relevant laws and regulations of the Republic of Serbia. The audit of policies, procedures and regulations are carried out in when needed, but at least once a year.

Liquidity risk management process is organized through the Asset and Liability Management Committee, Market Risk Management Department and Asset and Liability Management Department.

The Assets and Liability Committee and the Operating Liquidity Committee (OLC Committee) are responsible for monitoring liquidity risk, managing the liquidity risk and for recommending to the Executive Board the measures and activities to maintain the liquidity, adjustment of the maturity structure, financing plan for reserves and other measures important for the financial stability of the Group. The department for asset and liability management and department for market risk management and liquidity risk management monitors the liquidity ratio (LIK) on daily basis so that the daily liquidity ratio is within the limits prescribed by the Business plan in case of extraordinary circumstances (liquidity crisis) ("PFNS"). Apart from this, PFNS defines other indicators and their limits as well as personnel/department in charge of their monitoring and reporting. The trend of these indicators is presented semi-weekly on OLC meetings, or more often in case of overriding the PFNS limits or change in liquidity status.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.3. Liquidity Risk and Funding Management (continued)

The Group maintains a portfolio comprised of liquid securities and diversified assets that can be easily modified in cash in case of non-predictable and negative oscillations in cash flow of the Group. The Group maintains the required level of local and foreign currency reserves, in accordance with the demands of National Bank of Serbia.

The level of liquidity is expressed using the liquidity ratio which is determined as the proportion of the sum of the liquid assets of the first (cash, gold and other noble metals, assets on accounts with other banks with available credit rating which corresponds to the level of credit quality 3 or better determined in accordance with the decision on capital adequacy (investment grade); deposits with the National Bank of Serbia, receivables in the process of realization, irrevocable lines of credit granted to the Group, stock and quoted debt securities, 90% of the fair value of securities denominated in dinars, without a currency clause, issued by the Republic of Serbia and with a minimum maturity of three months or 90 days, and classified as securities held for trading or securities available for sale) and second level (other receivables due within a month) and the sum of liabilities on demand without determined maturity date (40% Bank's demand deposits, 20% on demand deposits from other depositors, 10% savings deposits, 5% guarantees and other forms of guarantees and 20% undrawn irrevocable credit lines) and liabilities with fixed maturity up to a month.

In addition to the broader liquidity indicator, the Bank also monitors the narrow liquidity indicator.

The narrow liquidity indicator represents the ratio of liquid receivables of the Bank of the first order, on the one hand and the sum of on demand liabilities of the bank or without a contracted maturity and liabilities of the Bank with a fixed maturity within the next month following the date of the calculation, on the other hand.

During 2017 and 2016, the Bank had an indicator of daily liquidity above the legally prescribed level.

As of 30 June 2017, on the basis of the Decision on the Bank's liquidity management, adopted by the National Bank of Serbia, the banks are obliged to calculate and report on the value of the Indicator of Coverage with liquid assets (hereinafter PPLA) on a monthly basis. PPLA represents the ratio of the bank's liquidity layer to the bank and the net outflow of liquid assets that would arise during the next 30 days from the date of calculating this indicator under the assumed stress conditions. The Bank is obliged to keep PPLA, in all currencies, at a level not lower than 100%.

A set of policies and other internal acts adopted by the Managing and Executive Boards describe in more detail the issues of jurisdiction, methodology of calculation, limits and escalation. In addition to the defined regulatory limit, the Bank has established and monitors the internal limits for PPLA.

The Department for Market Risk Management and Liquidity Risk within the Strategic Risk Management Department is responsible for calculating the indicators. On December 31, 2017 and on December 31, 2016 Bank had PPLA ratio above prescribed limit.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.3. Liquidity Risk and Funding Management (continued)

Maturity Analysis of Financial Liabilities

The table below presents the ageing analysis of the Group's financial liabilities as at 31 December 2017 and 31 December 2016 based on of contractual, not discounted payments.

The Group expects that most customers will not withdraw deposits on the due date set in the contract.

						RSD thousand
	From 0-1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Total 2017
Borrowings, deposits and securities	20,795,323	20,329,138	44,798,747	49,884,593	11,989,544	147,797,345
Subordinated liabilities	-	96,978	286,911	1,076,577	-	1,460,466
Total	20,795,323	20,426,116	45,085,658	50,961,171	11,989,544	149,257,811

						RSD thousand
	From 0-1 month	Up to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Total 2015
Borrowings, deposits and securities	20,361,774	21,545,528	32,563,558	39,900,610	11,011,950	125,383,417
Subordinated liabilities	-	105,095	311,314	1,535,165	-	1,951,573
Total	20,361,771	21,650,623	32,874,872	41,435,775	11,011,950	127,334,991

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for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.3. Liquidity Risk and Funding Management (continued)

Maturity Analysis of Financial Liabilities (continued)

The table below presents the ageing analysis of guarantees, letters of credit and other irrevocable commitments:

	Up to 14 days	From 15 days to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	RSD thousand Total 2017
Contingent liabilities	804,154	498,480	2,291,039	4,421,168	4,363,004	220,085	12,597,930
Irrevocable commitments and letters of credit	9,187,841	136,759	674,876	3,482,742	7,922,839	3,227,864	24,632,921
Total	9,991,995	635,239	2,965,915	7,903,910	12,285,843	3,447,949	37,230,851

	Up to 14 days	From 15 days to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	RSD thousand Total 2016
Contingent liabilities	288,049	187,672	1,571,984	3,984,921	2,026,646	138,711	8,197,983
Irrevocable commitments and letters of credit	45,581	84,093	430,349	4,721,418	7,090,084	1,437,418	13,808,943
Total	333,630	271,765	2,002,333	8,706,339	9,116,730	1,576,129	22,006,926

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.3. Liquidity Risk and Funding Management (continued)

Maturity Analysis of Financial Liabilities (continued)

The Bank expects that not all contingencies and commitments would be withdrawn prior to expiry of their maturity.

For financing small and medium enterprises and small and medium infrastructure projects implemented by municipalities, the Bank has used the funds of the European Investment Bank ("EIB") and German Development Bank ("KfW").

The Bank has signed three agreements with EIB - in 2010, 2012 and in 2015 for the aggregate amount of EUR 125 million.

By signing a contract with the German Development Bank, KfW, at the end of 2012, the Bank provided funds in the amount of 10 million Euros for financing micro, small and medium enterprises and energy efficiency / renewable energy projects.

By signing a contract with the German Development Bank, KfW, signed in 2014, the Bank provided funds for the financing of micro, small and medium enterprises and energy efficiency / renewable energy projects in the amount of a total of EUR 30 million.

On December 3, 2015, the Bank signed a long-term loan agreement with Erste Group Bank AG for the financing of loans to legal entities in the amount of EUR 100 million. At the end of 2017, a new long-term loan contract was signed for an amount of 53 million euros.

At the end of 2017, the Bank signed a new contract with KfW in the amount of 23 million euros for financing energy efficiency and renewable energy.

At the beginning of 2018, a new contract with the EIB of EUR 50 million was signed for the needs of financing small and medium enterprises, as well as small and medium-sized infrastructure projects implemented by municipalities

Signing a new contract with the EBRD for the financing of energy efficiency projects in the housing sector is planned.

The balance of loans received from foreign credit institutions in 2017 amounted to RSD 33,916,419 thousand (2016: RSD 26,110,695 thousand) (note 24).

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.3. Liquidity Risk and Financial Assets Management (continued)

Maturity Analysis of Financial Liabilities (continued)

Liquidity Gap Analysis – Financial Assets and Liabilities

The table below provides an analysis of the maturities of assets and liabilities of the Group based on contractual terms of payment. Contractual maturities of assets and liabilities are determined based on the remaining period at the balance sheet date to the contractual maturity date. Maturity structure of assets and liabilities as at 31 December 2017 is presented as follows:

	RSD thousand						
	Up to 14 days	From 15 days to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Total 2017
ASSETS							
Cash and assets with the central bank	20,774,027	-	-	-	-	-	20,774,027
Financial assets at fair value through the income statement for trading	21,481	158,488	1,871,347	1,751,880	7,524,670	211,598	11,539,464
Financial assets available for sale	548,062	-	714,407	407,970	9,469,507	1,348,647	12,488,593
Financial assets held to maturity	-	-	-	1,790,337	4,910,962	1,583,153	8,284,452
Loans and receivables from banks and other financial institutions	1,862,127	-	9,845	134,947	65,831	126,221	2,198,970
Loans and receivables from customers	1,652,963	128,354	2,042,207	13,874,057	32,935,280	59,839,869	110,472,730
Other assets	280,575	2,304	4,858	12,947	14,471	10,068	325,223
Total assets	25,139,234	289,146	4,642,664	17,972,138	54,920,721	63,119,556	166,083,459
EQUITY AND LIABILITIES							
Financial liabilities at fair value through the income statement for trading	14,752	-	-	-	2,826	26,880	44,458
Deposits and other liabilities to banks and other financial organisations and central bank	5,222,991	2,323,139	3,567,273	6,811,843	20,672,836	13,261,626	51,859,706
Deposits and other liabilities to other customers	65,109,561	1,522,273	7,387,218	14,255,364	2,600,668	1,107,044	91,982,128
Subordinated liabilities	-	-	85,173	253,870	1,015,480	-	1,354,523
Other liabilities	783	-	-	-	-	-	783
Total Liabilities	70,348,087	3,845,411	11,039,663	21,321,077	24,291,810	14,395,550	145,241,599
Total equity	-	-	-	-	-	18,128,002	18,128,002
Total equity and liabilities	70,348,087	3,845,411	11,039,663	21,321,077	24,291,810	32,523,552	163,369,601
Maturity mismatch as at:							
31 December 2017	(45,208,853)	(3,556,265)	(6,397,000)	(3,348,939)	30,628,911	30,596,004	
31 December 2016	(32,766,081)	(4,864,773)	(11,550,302)	(374,739)	29,640,935	19,914,960	

The maturity mismatch is the result of an increase in the volume of sight deposits compared to the planned funds for up to 14 days. The Group monitors maturity compliance using statistical models of deferred sight deposits at expected maturities.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS for the year ended 31 December 2017

32. RISK MANAGEMENT (continued)

32.4. Market Risks

Market risk is the risk that changes in the value of balance sheet and off-balance sheet items arising from movements in market prices will have negative effects on the Group's financial result and equity.

The Group's operations are, among other risks, exposed to market risks, including foreign exchange risk, price risk on debt and equity securities and merchant banking risk.

The general price risk on debt securities is the risk of debt securities price changes due to changes in the general level of interest rates.

To calculate the capital requirements of the general price risk, the Bank applies the maturity method.

Maturity method is based on the classification of all net positions in debt securities into maturity classes or zones according to the outstanding maturity and coupon (interest) rate as per the table prescribed by the NBS Decision governing the Bank's capital adequacy.

The Bank calculates capital requirements for market risks arising from items of trading book using the methodology and guidelines prescribed by the NBS Decision governing the Bank's capital adequacy.

Market risk management in the Group is defined by policies, procedures and rulebooks approved by the Management Board and Executive Board, which are in compliance with the risk management strategy at the level of Erste Group, as well as with all relevant laws and regulations of the Republic of Serbia. Policies, procedures and regulations are reviewed when necessary or at least once a year.

Market risk management process is organized through the Asset and Liability Management Committee ("ALCO"), Market and Liquidity Risk Management Department and Asset and Liability Management Unit.

Identification, measurement, analysis and reporting of market risk exposures are managed by a separate organizational unit, i.e., Market and Liquidity Risk Management Department. ALM Unit and Market Risk Management Department monitor foreign exchange ratio on a daily basis with ALM Unit reporting to ALCO on a monthly basis.

Furthermore, the Market and Liquidity Risk Management Department monitors and manages market risks through control of the set trading book limits, changes to the currently effective and definition of new limits and through assessment of the relevant risks arising from the introduction of new products and complex transactions.

There are two types of limits:

- VaR limit
- Limits of sensitivity (PVBP, CR01)

Value at Risk (VaR) measures the maximum expected loss of value of risk assets or portfolios during a predetermined holding period for a given confidence interval. The calculation of VaR is carried out using the historical simulation method with a one-sided confidence level of 99%, a one-day holding period and a two-year simulation period. Exposure monitoring is done on a daily basis.

VaR in RSD thousand	as at 31 December 2017	as at 31 December 2016
<i>Interest risk</i>	25,126	11,397
<i>Foreign currency risk</i>	9,090	119
Total	25,987	11,428

From January 1, 2017 on the Erste Group level, a new technical solution for the calculation of VaR was implemented. During the year 2017, there were methodological changes.

Two sensitivity limits, PVBP and CR01 are set.

Price Value of a Basis Point (PVBP) is the assumed change in the price of trading book positions due to the parallel shift of the yield curve by 1 basis point. The limit is defined by currencies (RSD, EUR, USD, and OTH) and at the total level.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.4. Market Risks (continued)

Credit PV01 (CR01) is the assumed change in the value of securities due to the parallel shift of the credit spread by one basis point. Exposure is monitored at the level of an individual issuer for the entire portfolio of securities (trading book and bank book).

The mentioned limits are approved by the Bank's Executive Board, on the proposal of the Strategic Risk Management Department, and Erste Group's Market Risk Committee.

In case of exceeding the internally prescribed limits, the process of escalation and measures for returning to the limits of the limits are defined.

32.4.1 Interest Rate Risk

Interest risk is the risk of an adverse impact on the Group's financial result and capital due to changes in market interest rates. The Group is exposed to this risk based on items from the banking book, and it assesses the aforementioned risk in the aggregate and per each significant foreign currency for whose definition it has established criteria. In accordance with these criteria, the Group considers RSD and EUR to be materially significant currencies.

In determining interest rates the Group considers market interest rates and their movements to which the Group's interest rates are regularly adjusted. Interest rate changes result in increases or decreases in interest margins. Interest risk management has as its goal optimization of this influence, increasing the net interest revenue on one end and economic value of equity on the other.

ALCO manages maturity matching of assets and liabilities based on the Group's guidelines, macroeconomic analyses and forecasts, forecasts of the liquidity, analyses and forecasts of interest rate market trends for different segments of assets and liabilities.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
32. RISK MANAGEMENT (continued)
32.4. Market Risk (continued)
32.4.1 Interest Rate Risk (continued)

The following table shows the Group's exposure to risk from changes of interest rates (Repricing Gap) on 31 December 2017. Assets and liabilities and currency swaps from off-balance sheet items are presented after the date of re-pricing of interest or maturity date, depending on which date is earlier.

Category						RSD thousand	
	Within a month	From 1 to 3 months	From 3 to 6 months	From 6 to 12 months	Over a year	Total non-interest bearing	Total
Cash	-	-	-	-	-	5,275,221	5,275,221
Correspondent accounts	-	-	-	-	-	-	-
Obligatory reserve	7,002,670	-	-	-	-	9,293,751	16,296,421
Securities	11,474,801	1,219,625	1,513,050	685,255	17,313,384	-	32,206,115
Loans due from banks	705,730	-	-	-	-	-	705,730
Loans due from customers	86,140,785	2,671,960	2,048,385	2,709,345	16,548,994	-	110,792,063
Other assets	-	-	-	-	-	2,989,020	2,989,020
Total balance sheet assets	105,323,986	3,891,585	4,234,028	3,394,601	33,862,378	17,557,992	168,264,569
<i>FX Swaps</i>	2,432,484	-	-	-	-	-	2,432,484
Total assets	107,756,470	3,891,585	4,234,028	3,394,601	33,862,378	17,557,992	170,697,053
Liabilities to banks	-	-	-	-	-	-	-
Liabilities to financial institutions	12,316,064	8,944,992	15,633,02	1,285,270	7,490,713	-	45,670,642
AVISTA deposits	4,949,671	9,899,342	14,849,013	6,781,951	24,932,457	-	61,412,435
Term deposits	6,005,748	8,248,163	6,529,252	10,398,750	5,379,743	-	36,561,655
Issued bonds	-	-	-	-	-	-	-
Other liabilities	-	-	-	-	-	3,559,411	3,559,411
Equity	-	-	-	-	-	21,060,426	21,060,426
Total balance sheet liabilities and equity	23,271,483	27,092,497	37,011,867	18,465,972	37,802,913	24,619,837	168,264,569
<i>FX Swaps</i>	2,445,342	-	-	-	-	-	2,445,342
Total liabilities and equity	25,716,826	27,092,497	37,011,867	18,465,972	37,802,913	24,619,837	170,709,911
Net interest risk exposure as at 31 December 2017	82,039,645	(23,200,912)	(32,777,839)	(15,071,371)	(3,940,535)	(7,061,845)	(12,858)
Net interest risk exposure as at 31 December 2016	74,578,402	(26,932,269)	(22,151,856)	(19,060,829)	(2,480,900)	(3,886,918)	65,630

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
32. RISK MANAGEMENT (continued)
32.4. Market Risk (continued)
32.4.1 Interest Rate Risk (continued)

Interest rate risk is also monitored by sensitivity analysis- scenario analysis, i.e. by observing the effect of interest rate fluctuations to the Group's income and expenses.

The following table presents the Group's income statement's sensitivity to the reasonably possible changes of interest rates (1%) with other variables held constant. The income statement's sensitivity represents the effect of predicted changes in interest rates on net interest income in one year on financial assets and liabilities based on interest rates as at 31 December 2017 and 31 December 2016.

Currency	Change in percentage	Income statement sensitivity 2017	Change in percentage	RSD thousand Income statement sensitivity 2016
<i>Increase of percentage:</i>				
RSD	1%	161,123	1%	127,015
EUR	1%	341,201	1%	241,738
<i>Decrease of percentage:</i>				
RSD	1%	(164,677)	1%	(127,017)
EUR	1%	(409,916)	1%	(201,393)

32.4.2. Foreign Exchange Risk

Foreign currency risk is the risk of change of the value of financial instruments and occurrence of adverse effect to the Group's financial result and equity due to the fluctuations in foreign exchange rates. The banking operations in different foreign currencies cause the exposure to fluctuation in foreign exchange rates.

The Group manages foreign exchange risk, striving to prevent adverse effects of changes of cross-currency rates and foreign exchange rates comparing to the dinar (foreign currency losses) on the Group's financial result, as well as on customers' ability to repay loans in foreign currency.

For the purposes of protection against the foreign currency risk, the Group monitors the changes in foreign currency exchange rate on the financial market on a daily basis, carries out the policy of low level exposure to foreign currency risk and contracts the foreign currency clause with its customers.

The Asset and Liability Management Unit and Treasury Department monitor daily movements of the overall foreign currency risk, as well as risk by specific currencies. The Risk control unit daily monitors movements in indicators of foreign exchange risk. The positions are monitored on a daily basis to ensure positions are maintained within established limits.

In accordance with the National Bank of Serbia's requirements, the Group regularly maintains its foreign currency position - foreign exchange risk indicator within maximal regulatory limits, determined in proportion to capital, in accordance to which the Group is obligated to ensure that its total net open foreign currency position does not exceed 20% of its regulatory capital.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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32. RISK MANAGEMENT (continued)
32.4. Market Risk (continued)
32.4.2. Foreign Exchange Risk (continued)

During 2017, the Group continuously paid attention to keep the foreign currency risk indicator within the prescribed limit. The foreign currency indicator, at the end of each working day, was lower than 20% comparing to the Group's capital.

The following table presents the Group's exposure to foreign currency risk as at 31 December 2017 and 31 December 2016 of its non-trading assets and liabilities.

The analysis presented calculates the effect of the reasonable changes in the exchange rate with other variables held constant. Negative values refer to potential decreases in the income statement or equity, while the positive values refer to its increases.

RSD thousand				
Currency	Changes in the exchange rate (depreciation in %) 2017.	Effect to the income statement before taxation 2017.	Changes in the exchange rate (depreciation u %) 2016.	Effect to the income statement before taxation 2016.
EUR	2%	22,508	2%	(8,003)
CHF	2%	30	2%	142
USD	2%	285	2%	269

The following table presents the Group's exposure to foreign exchange risk as at 31 December 2017. The table includes assets and liabilities at their carrying amounts.

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32. RISK MANAGEMENT (continued)
32.4. Market Risk (continued)

							RSD thousand
	<u>EUR</u>	<u>USD</u>	<u>CHF</u>	<u>Other currencies</u>	<u>Total foreign currencies</u>	<u>Total in RSD</u>	<u>Total</u>
ASSETS							
Cash and assets with the central bank	10,151,379	71,119	118,959	140,305	10,481,762	10,292,265	20,774,027
Financial assets at fair value through the income statement for trading	6,909,319	-	-	-	6,909,319	4,630,145	11,539,464
Financial assets available for sale	6,803,611	172,631	-	-	6,976,242	5,512,351	12,488,593
Financial assets held to maturity	465,848	-	-	-	465,848	7,818,604	8,284,452
Loans and receivables from banks and other financial institutions	533,017	1,443,877	2,942	213,129	2,192,965	6,005	2,198,970
Loans and receivables from customers	84,830,254	467,268	957,498	-	86,255,020	24,217,709	110,472,729
Investments in subsidiaries	-	-	-	-	-	118	118
Investments in related parties	-	-	-	-	-	-	-
Intangible assets	-	-	-	-	-	255,553	255,553
Property, plant and equipment	-	-	-	-	-	1,078,617	1,078,617
Investment property	-	-	-	-	-	-	-
Current tax assets	-	-	-	-	-	3,386	3,386
Deferred tax assets	-	-	-	-	-	2,261	2,261
Non-current assets held for sale and assets of discontinued operations	-	-	-	-	-	12,288	12,288
Other assets	113,081	216	3,036	-	117,083	1,037,028	1,154,111
Total assets	109,807,259	2,155,111	1,082,435	353,434	113,398,239	54,866,330	168,264,569

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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32. RISK MANAGEMENT (continued)
32.4. Market Risk (continued)
EQUITY AND LIABILITIES

Financial liabilities at fair value through the income statement for trading	29,708	-	-	-	29,708	14,750	44,458
Deposits and other liabilities to banks and other financial organisations and central bank	45,984,385	49,121	663,341	29,508	46,726,355	5,133,352	51,859,707
Deposits and other liabilities to other customers	57,970,402	3,280,640	1,279,027	461,927	62,991,996	28,990,132	91,982,128
Subordinated liabilities	1,354,523	-	-	-	1,354,523	-	1,354,523
Provisions	7,847	-	-	-	7,847	758,762	766,609
Current tax liabilities	-	-	-	-	-	160,965	160,965
Other liabilities	-	-	-	-	-	5,248	5,248
Total liabilities	<u>105,424,470</u>	<u>3,330,762</u>	<u>1,943,845</u>	<u>491,535</u>	<u>111,190,612</u>	<u>36,013,531</u>	<u>147,204,143</u>
Total equity	-	-	-	-	-	21,060,426	21,060,426
Total equity and liabilities	<u>105,424,470</u>	<u>3,330,762</u>	<u>1,943,845</u>	<u>491,535</u>	<u>111,190,612</u>	<u>57,073,957</u>	<u>168,264,549</u>
Net foreign currency position as at:							
- 31 December 2017	<u>4,382,789</u>	<u>(1,175,651)</u>	<u>(861,410)</u>	<u>(138,101)</u>	<u>2,207,627</u>		
- 31 December 2016	<u>2,732,084</u>	<u>(2,266,773)</u>	<u>(302,971)</u>	<u>(123,232)</u>	<u>39,108</u>		

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32. RISK MANAGEMENT (continued)

32.5. Group's Risk Concentration

This is a risk of the Group's exposures to a single entity or a group of related entities and exposures to an entity related to the Group.

Monitoring the exposure risk is mandatory part of the procedures in the loan approval stage in the sense that a committee that approves a loan has at its disposal information on the total Group's exposure to a customer or a group of related customers relative to the Group's capital.

During 2017, the Group maintained the exposure risk indicators within the prescribed values. By implementing appropriate activities stipulated by the relevant procedures and decisions on loan approval, the Group kept the adequacy of its loans and receivables and investments in line with the performance indicators prescribed by the National Bank of Serbia (see Note 29(b)) and with the internal limits.

In accordance with the Risk management policies, the Group's management approves the exposures and limits, i.e. the loan concentration on certain legal entities or a group of related entities, and parties related to the Group.

The procedures of exposure risk management are the subject of internal audit and the compliance function.

32.6. Group's Investment Risks

The Group's investment risks include the Group's equity investments held in other entities and investments made in fixed assets.

In accordance with the National Bank of Serbia legislation, the level of the Group's investment and the level of regulatory capital is being monitored in order to ensure that the Group's investments in a single non-financial sector entity do not exceed 10% of its capital, while the total investments of the Group in non-financial entities and in tangible assets cannot exceed 60% of its regulatory capital.

The Group's investment risk exposure arising on investments into other legal entities and property and equipment is monitored by the organizational unit or the Group's body competent for procurement of tangible assets and investing in legal entities familiar with the current exposure and the amount of capital for the purposes of acting in timely manner in accordance with the prescribed limits.

During 2017, the Group maintained the investment risk indicators within the prescribed values and it ensured that investments were reconciled with the indicators prescribed by the National Bank of Serbia.

The procedures of exposure risk management are subject to internal audit and the compliance control function.

32.7. Country Risk

Country risk is the risk related to the country of origin of a counterparty the Group is exposed to and includes adverse effects which may influence the financial result and capital of the Group, as the Group might not be able to collect receivables from this counterparty, as a result of political, economic or social situation in the country of its origin.

The Group mostly approves funds to the customers from the Republic of Serbia, while it is exposed to the country risk in the portion of assets it keeps on the accounts with foreign banks.

The Group monitors its exposure on geographic basis by applying the limits determined by the parent bank and based on country ratings.

The Group's exposure to the country risk is low, due to insignificant participation of non-residents in the total loan portfolio of the Group.

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for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.8. Operational Risk

Operational risk is the risk of the adverse effects on the Group's financial result and equity due to failures in the employees' performance, inadequate internal procedures and processes, inadequate information and other systems in the Group or unforeseen external events.

The Group has established a comprehensive system of managing operational risk through the identification and recording, evaluation and monitoring of operational risks in all material products, activities, processes and systems. Operational risk management is the responsibility of all employees of the Group.

Committee for Operational Risk Management of the Group, in addition to an independent department for operational risk management and other control functions, actively contributes to the improvement of operational risk management function.

Reporting system for operational risk events is used for early identification of operational risk events, while the approximation process provides completeness, coherence and comprehensiveness of operational risk events that have occurred in the Group. Operational risk events are collected in a single database and further analysed and monitored.

The Group continually carries out training of all employees in the area of operational risk by raising awareness of employees about the risk, improving quantitative and qualitative tools for identifying and measuring risk exposure (such as self-assessment, key indicators of operational risk, scenario analysis, etc.), and it establishes and promotes the adequate preventive and corrective measures in order to reduce the exposure to operational risk to an acceptable level.

The Group has defined and regularly reviewed and updated internal acts which regulate the management area the Group's exposure to operational risk, taking into account the compliance with the applicable regulatory framework and Group standards.

The Group, through the Program of insurance from operational risks insured against classical risk and specific banking risks. Classical risks include damage to property, burglary, theft (valuable property) and general responsibility. Specific risks include the Group's internal and external fraud, technological risks and civil liability.

The Group performs continuous estimation of the risks arising in the process of introducing new products / services, projects and risk assessment resulting from entrusting third parties. Improvement of internal control mechanisms is a necessary element in all activities of operational risk management.

The Group calculates capital requirements under Pillar 1 for operational risk using the basic indicator approach while under Pillar 2 it applies advanced approach by using an internal model.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (continued)

32.9. Capital Management

The Group permanently manages its capital, which is a broader concept than "capital" on the face of the balance sheet, in order to:

- comply with the capital requirements set by the National Bank of Serbia;
- to ensure that the level and composition of capital that can support the expected growth in placements;
- ensure the possibility of a long-term going concern of operations with providing of profit to shareholders and benefits to other stakeholders; and
- provide a solid capital base to support the development of its business.

The Group manages the capital structure and performs adjustments in accordance with changes in economic conditions and risk related to the Group's operations. The Group's management monitors regularly the Group's capital adequacy ratios and other ratios established by the National Bank of Serbia and delivers quarterly reports on achieved values of ratios.

In accordance with the Law on Banks and relevant decisions of the National Bank of Serbia, banks are obliged to maintain minimal capital in the amount of EUR 10 million, in RSD counter value exchanged at the official median exchange rate, a capital adequacy ratio of at least 12%, as well as to comply the volume and structure of its operations with ratios prescribed by the Decision on risk management ("Official Gazette of the Republic of Serbia", no. 45/2011, 94/2011, 119/2012 and 123/2012, 23/2013, 43/2013, 92/2013, 33/2015, 61/2015 and 61/2016) and the Decision on capital adequacy ("Official Gazette of the Republic of Serbia", no. 46/2011, 6/2013 and 51/2014).

The Decision on the capital adequacy of banks, adopted by the National Bank of Serbia, establishes the method of calculating the capital adequacy. The Group's total capital comprises Tier 1 and Tier 2 capital, and by prescribed deductible items, while the risk weighted on balance sheet assets and off-balance sheet items are determined in accordance with the prescribed risk ratios for all types of assets.

The capital of the Group is the sum of the basic and additional capital, where the basic capital makes the sum of the basic share capital and additional share capital. The capital adequacy ratio of the Group is equal to the ratio of the bank's capital and the collection of credit risk weighted assets, the capital requirement for price risk from the activities in the book of trade multiplied by the reciprocal value of the capital adequacy ratio (prescribed 8%), the capital requirement for foreign exchange risk multiplied by the reciprocal value of the capital adequacy ratio, the capital requirement for the risk of adjusting the credit exposure multiplied by the reciprocal value of the capital adequacy ratio, the capital requirement for operational risk multiplied by the reciprocal value of the capital adequacy ratios and the risk weighted exposure for the risk of the counterparty.

The Group conducts a process of internal capital adequacy assessment process (ICAAP), determine available internal capital and makes a distribution, and develop a strategy and plan for capital management in accordance with the risk management of the Group.

In accordance with the Banking Law and the Decision on recovery plans for banks and banking groups ("Official Gazette of RS", no. 71/2015), the Group has prepared and submitted to the National Bank of Serbia Recovery Plan, which is the main pillar for strengthening the financial resistance of the Group and achieving stability in situations of serious financial distress.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017
32. RISK MANAGEMENT (continued)
32.9. Capital Management (continued)

The table below summarizes the structure of the Group's capital as at 31 December 2017, as well as the capital adequacy ratio:

	RSD thousand
	31 December 2017
<i>Basic capital</i>	
Basic share capital	10,040,000
The amount of the basic share capital paid	124,475
Related emission premium with basic equity instruments	1,442,454
Profit from the current period that meets the requirements for inclusion in the share capital	495,357
Revaluation reserves and other unrealized gains	(77,334)
Unrealized losses	7,679,825
Other reserves	16,875
Additional value adjustments	(24,072)
Other intangible assets before deduction for related deferred tax liabilities	(255,553)
	19,442,026
<i>Supplementary capital</i>	
Subordinated obligations	572,575
	572,575
<i>Capital:</i>	20,014,601
Risky balance and off-balance assets	
Capital requirement for credit risk, counterparty risk and risk of delivery / delivery on the basis of free delivery	7,868,795
Capital requirement for price risk	177,449
Capital requirement for foreign exchange risk	92,209
Capital requirement for operational risk	1,102,422
Capital requirement for the risk of adjusting credit exposure	13,102
<i>Adequacy of basic share capital</i>	16.81
<i>Adequacy of share capital</i>	16.81
<i>Capital adequacy</i>	17.30

The Group is in compliance with all regulatory requirements regarding capital adequacy at all levels.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017****32. RISK MANAGEMENT (Continued)****32.9. Capital Management (continued)**

Reserve for estimated losses that may arise on the basis of balance sheet assets and off-balance sheet items is determined in accordance with the Decision of the National Bank of Serbia on classification of balance sheet assets and off-balance sheet items of the bank ("Official Gazette of the Republic of Serbia", No. 94/2011, 57/2012, 123 / 2012 43 / 2013, 113 / 2013, 135/2014, 25 / 2015, 38 / 2015, 61/2016, 69/2016, 91/2016, 101/2017 and 114/2017).

Calculation of reserves for estimated losses is carried out in order to cover the estimated losses on the basis of balance sheet assets and off-balance sheet items. The calculation of the reserve for estimated losses is based entirely on the criteria and rules defined in the Decision of the National Bank of Serbia on the classification of balance sheet assets and off-balance sheet items.

The classification of debtors' claims into categories A to D is performed on the basis of the following groups of criteria:

- assessment of the financial condition, i.e. the creditworthiness of the borrower;
- timely settlement of debtor's obligations;
- other specific criteria (restructured receivables, newly established companies and claims based on project financing, promptness of the loan dossier, real estate acquired through collecting receivables, etc.)
- the quality of collateral.

Based on the classification of receivables, in accordance with the aforementioned Decision of the National Bank of Serbia, the reserve for estimated losses is calculated using the following percentages on balance sheet receivables and off-balance sheet items that are classified: A (0%), B (2%), V (15%), G (30%) and D (100%).

In order to calculate the required reserve for estimated losses, the Group deducts the estimated loss reserves according to the Decision of the National Bank of Serbia for the correction of the balance sheet assets and provisions for losses on off-balance sheet items disclosed at the expense of expenses in the income statement. All positive differences will represent the necessary reserve for estimated losses on balance sheet assets and off-balance sheet items. In accordance with the Decision on Capital Adequacy of the Bank, the required reserve for estimated losses is considered a deductible item of equity, except in cases when the condition from item 34a of the Decision on classification of balance sheet assets and off-balance sheet items of the bank ("Official Gazette of the Republic of Serbia" No. 94 / 2011, 57/2012, 123/2012, 43/2013, 113/2013, 135/2014, 25/2015, 38/2015, 61/2016, 69/2016, 91/2016, 101/2017 and 114/2017). In accordance with the above, the Group dated March 31, the required reserve requirement for the estimated losses is not treated as a deductible item of capital.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (Continued)

32.10. Fair value of the financial assets and liabilities

The fair value calculation in EBS is based primarily on external source data (listing of dealers for government bonds and available stock prices from the stock exchange). OTC derivatives are valued using the model. By using the model, bonds are also valued if there is no adequate number of quotations or quotations are not up-to-date.

Evaluation model

Bonds

Bonds for which quotations are not available in an adequate number or quotation are not sufficiently up to date are discounted by future cash flows using a predefined curve for the respective currency.

OTC derivatives

Valuation is aimed at discounting future cash flows using defined yield curves for a particular product and a specific currency. The derivative value thus obtained is adjusted for the Credit Valuation Adjustment (CVA) and the Debt Valuation Adjustment (DVA), as the credit default of the other counterparty and its own credit risk are not taken into account. CVA refers to credit risk adjustment of other agreements of the parties, while DVA refers to adjusting for own credit risk. The value of these adjustments depends on PD, LGD and exposure (NPV).

Hierarchy of instruments that are valued at fair value

In accordance with IFRS 13, the EBS quarterly allocates appropriate levels to all positions in assets and liabilities that are valued at fair value or whose fair value must be disclosed in notes to the financial statements. Levels are allocated depending on how the market value of the instrument is derived. There are 3 levels.

Level 1

The fair value of financial instruments assigned to Level 1 hierarchy is determined on the basis of market quotations. The fair value determined on the basis of quotations can be Level 1 if the frequency and scope of trading is satisfactory and there is price consistency.

Level 1 classifies derivatives traded on an organized market, as well as stocks and bonds for which there is an active market.

Level 2

Instruments for which there are market quotations, but whose market can not be considered active due to limited liquidity, are classified as Level 2. If market quotations are not available, fair value is determined using a valuation model (discounting future cash flows), and all parameters for the model (yield curves, spurs) are available on the market, Level 2 is also assigned.

OTC derivatives and less liquid stocks and bonds are classified as Level 2 instruments.

Level 3

Instruments whose fair value is determined on the basis of quotations that are not sufficiently up-to-date or by using a model whose all inputs are not commercially available are classified as Level 3 hierarchy. Market unavailable parameters are most often related to credit spreads that are derived from internally calculated measures - PD and LGD.

Shares for which there are no quotations, illiquid bonds, as well as loans and deposits are classified as Level 3.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

32. RISK MANAGEMENT (Continued)

32.10. Fair value of the financial assets and liabilities (continued)

The following table shows fair value of financial instruments designated at fair value in financial statements:

	2017				2016				RSD thousand
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total	
FINANCIAL ASSETS	9,186,810	13,275,013	1,566,234	24,028,057	1,144,215	18,387,062	678,792	20,210,069	
Financial assets held for trading	5,237,855	5,946,575	355,033	11,539,464	577,001	11,811,358	659,998	13,048,357	
Republic of Serbia Treasury bills	4,976,963	5,881,910	355,033	11,213,907	319,405	11,612,220	659,998	12,591,623	
Government bonds of Republic of Montenegro	260,892	-	-	260,892	257,596	-	-	257,596	
EBRD bonds	-	-	-	-	-	60,380	-	60,380	
Derivatives	-	64,665	-	64,665	-	138,758	-	138,758	
Financial assets available for sale	3,948,955	7,328,438	1,211,201	12,488,593	567,214	6,575,704	18,794	7,161,712	
Republic of Serbia Treasury bills	3,934,915	7,267,013	1,183,444	12,385,371	555,695	6,516,415	-	7,072,110	
EBRD bonds	-	60,378	-	60,378	-	59,289	-	59,289	
Quoted shares	14,040	1,047	-	15,087	11,519	-	654	12,173	
Shares that are not quoted	-	-	27,757	27,757	-	-	18,140	18,140	
	-	44,458	-	44,458	-	54,690	-	54,690	
FINANCIAL LIABILITIES									
Financial liabilities at fair value through profit and loss held for trading	-	44,458	-	44,458	-	54,690	-	54,690	

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
32. RISK MANAGEMENT (continued)
32.10. Fair Value of Financial Assets and Liabilities (continued)

In level 3 is one RS bond with ISIN RSMFRSD56740 was issued on 25 December 2017. The bank bought EUR 13 million (HFT EUR 3 million + AFS EUR 10 million).

The valuation method is defined for each bond in the front office system of the bank, within the scope for the given bond. When initially entered in the system, the bond is valued on the basis of the corresponding yield curve (depending on the currency). Subsequently, checking whether there are adequate quotations for individual bonds (in terms of the number of available quotes and the dynamics of price updates) available on Reuters. If there are adequate quotations, the valuation method in Kondor is changed and the bond is valued on the basis of quotations rather than using the yield curve.

The bond is therefore initially valued through the yield curve, shortly after the valuation method has changed and now quotes are quoted from Reuters directly for that bond. However, given that the bond was emitted at the end of the year (five working days before the end of the year), the valuation method for the end of the year remained the same as initially defined. It was subsequently changed when banks began to quote the price and when it was estimated that quotations were adequate. This ISIN is by no means specific in relation to other RS bonds

The table below shows the comparison, by classes, the carrying amount and fair value of financial instruments that are not recognized at fair value in the financial statements. The table does not include the fair value of non-financial assets and non-financial liabilities.

FINANCIAL ASSETS	31 December 2017		31 December 2016	
	Carrying value	Fair value	Carrying value	Fair value
Securities held to maturity	8,284,452	8,284,452	8,635,103	8,635,103
Loans and receivables due from banks	2.198.970	2.198.970	1,210,065	1,205,331
Loans and receivables due from customers	110.472.729	119.642.384	96,462,922	102,576,895
Construction objects	474,059	474,059	481,414	481,414
Investment property	-	-	232,417	232,417
Fixed assets intended for sale	-	-	-	-
FINANCIAL LIABILITIES				
Deposits due to banks	51,859,707	53,821,976	51.428.201	52.036.859
Deposits due to customers	91,982,128	92,618,096	75.290.829	74.352.992

The calculation of the fair value of financial instruments that are not recognized at fair value in the financial statements is carried out using the QRM as a standard of Erste Group.

The fair value of loans to customers and credit institutions is calculated by discounting future cash flows taking into account the effects of interest and credit spreads. The effect of interest rate changes is calculated on the basis of market interest rates, while changes in credit are derived from PDs and LGDs used for internal risk quantification. For the purposes of calculating fair value, loans are grouped into homogeneous portfolios based on the rating method, rating and residual maturity.

The fair value of the deposit is assessed on the basis of market conditions as well as its own credit risk. For demand deposits, book value is the lowest possible fair value.

In 2017, there were no reclassifications within the financial asset position.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

33. COMMITMENTS AND CONTINGENT LIABILITIES

(a) Operating Lease Commitments

The Group has executed operating lease contract on the lease of computer equipment and automobiles used by the Group.

The minimum future payments of non-cancellable operating lease liabilities are presented in the table below

	RSD thousand	
	<u>31 December 2017</u>	<u>31 December 2016</u>
Within a year	30,133	35,975
From 1 to 5 years	<u>53,257</u>	<u>38,981</u>
	<u>83,390</u>	<u>74,956</u>

(b) Litigations

As at 31 December 2017, the Group had 148 initiated litigations in the total amount of RSD 1,706,339 thousand in which it had the status of the respondent (31 December 2016: RSD 426,520 thousand). Penalty interest from litigations led against the Group amounts to RSD 231.200 thousand (31 December 2016: RSD 259,012 thousand).

Based on the assessment of Group's legal representatives for the above mentioned disputes, the Group made a provision in the amount of RSD 185,105 thousand (RSD 172,445 thousand as at 31 December 2016), for disputes that are expected to fall at the Group's expense on this date.

(c) Taxation Risks

The Republic of Serbia tax legislation is in the process of ongoing reviews and changes occur frequently. In different circumstances, tax authorities may apply different approaches to certain matters and entities may be assessed additional taxes, penalties and interest. The Group's management believes that the Group's tax liabilities recorded in these financial statements are appropriately stated in accordance with the effective regulations.

34. RECONCILIATION OF OUTSTANDING RECEIVABLES AND LIABILITIES BALANCES

In accordance with Article 18 of the Law on Accounting, the Group reconciled its balances of payables and receivables with its debtors and creditors and has valid documentation thereof.

The Group sent its customers outstanding items statements (OIS) as of 31 October 2017 in total amount of RSD 118,697,373 thousand. Confirmed receivables amounted to RSD 106,905,234 thousand.

The amount of disputed receivables amounted to RSD 31 thousand and the Group is in contact with clients in order to resolve conflicts.

The amount of unconfirmed OIS amounted to RSD 11,792,109 thousand because of the incorrect address – Client moved to another address without reporting it to Group or client does not exist on address reported to APR or Group.

The Group is still working on reconciliation of OIS for which replies were not received.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**

35. SEGMENT REPORTING

Management of the Group views operating segments in accordance with the methodology and segmentation defined at the entire Erste Group level and, on such basis, makes decisions in respect of, allocates resources to and assesses performance of individual segments. The report on segment results is aligned with FINREP methodology for financial reporting used within Erste Group where there are departures in certain items from the result as stated under the local NBS methodology.

a) Structure of Operating Segments

Segment report is comprised of six basic segments reflecting the governance structure of Erste bank a.d. Novi Sad



b) Definition of Operating Segments

Retail Segment

This segment comprises business activities within the scope of responsibilities of the Sales Managers from the Sales Network of the Retail Department. Target customers are mostly individuals, entrepreneurs and freelance professionals. Operations of the segment are mostly managed by the Group, which is focused on the simplicity of products offered – investment products, current accounts, savings, credit cards and additional products such as leases, insurance, and social security products.

Small and Medium Enterprises (SME)

This segment includes legal entities within the scope of responsibilities local corporate commercial centres, mostly comprised of companies with annual turnover of EUR 1 million to EUR 50 million. In addition, there are clients performing public activity or participating in the work of the public sector.

Commercial Project Financing (CRE)

This segment refers to operations involving investments in real estate for the purpose of generating income from lease out of certain properties or entire real estate complexes, development and construction of properties and complexes for realization of capital gains through the sale of individual constructed properties and property complexes, services of asset management, construction services and construction for the Group's own purposes.

Large Corporate Clients (LC)

This segment includes clients with consolidated annual turnover above EUR 50 million.

Financial Markets Segment (GM)

This segment involves activities comprised of trading and market service rendering. Trading and market services are activities related to the risk assumption and management within the Bank's trading book for the purposes of market creation, short-term liquidity management, custody operations, commercial operations and all other activities performed in the capital market. Specific income and gains on the fair value adjustment that are not directly related to the client transactions (which may also be operations of matching assets and liabilities) and general risk premiums as fees for the work done also belong to this segment.

Other

This segment encompasses all the activities of asset and liability management and internal service rendering on a non-profit basis. It also includes the Bank's available capital (defined as the difference between the total average capital in accordance with IFRS and average economic capital allocated to the operating segments).

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017**
35. SEGMENT REPORTING (continued)

RSD thousand	Retail		SME		Commercial real estate funding		Large corporate clients		Financial markets		Other		Group	
	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016
B. Profit and loss statement														
Net interest income	3,941,120	3,407,949	1,500,932	1,346,278	496,000	491,792	446,785	544,905	236,559	281,907	(251,998)	(131,689)	6,369,408	5,941,151
Dividend income	-	-	-	-	-	-	-	-	-	-	249	401	249	401
Net result from equity method investments	-	-	-	-	-	-	-	-	-	-	23,481	19,826	23,481	19,826
Rental income from investment properties and other operating lease	-	-	2,488	2,054	-	-	8,445	28,169	-	-	(15,929)	8,980	(4,996)	39,202
Net fee and commission income	1,068,915	1,042,097	304,372	267,222	14,689	23,297	134,330	130,678	26,891	22,339	(178,502)	(119,094)	1,370,695	1,366,939
Net trading result and the adj. to FV	131,531	101,821	28,771	31,907	10,800	10,528	10,191	10,271	223,357	192,539	97,980	59,264	502,629	406,330
General administrative expenses	(4,172,072)	(3,782,307)	(794,842)	(705,645)	(107,206)	(77,059)	(226,621)	(225,125)	(118,248)	(104,716)	(52,135)	(55,037)	(5,471,125)	(4,949,889)
Net loss on impairment of fin. assets not measured at fair value through profit or loss	(234,218)	(204,024)	156,062	(371,181)	66,856	2,757	203,537	65,204	(0)	(287)	(43,787)	(3,198)	(148,450)	(510,729)
Realised gains/losses from financial institutions that are not measured at fair value through profit or loss	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Gains / losses on financial assets and financial liabilities not measured at fair value through profit and loss, net	4,563	1,487	45,119	51	-	-	-	-	-	-	11,541	15,874	61,223	17,421
Net impairment losses on investments and non-financial institutions that are not measured at fair value through profit and loss	(1,666)	(1,533)	(714)	50	(0)	-	(0)	(0)	-	-	(7,501)	47,854	(9,881)	46,371
Other operating result	31,641	(13,548)	(42,110)	27,474	(5,300)	(893)	4,375	(33,164)	(2,628)	(697)	(66,257)	(122,241)	(80,279)	(143,068)
Profit before tax from regular activities	769,812	551,944	1,200,079	598,618	475,839	450,423	581,042	520,939	365,930	391,084	(482,849)	(279,062)	2,909,854	2,333,947
Income tax	(55,364)	(23,638)	(87,073)	(22,453)	(35,337)	(20,050)	(40,666)	(21,550)	(26,317)	(16,749)	35,463	12,018	(209,295)	(92,423)
Profit/loss for the year	714,448	528,306	1,113,006	576,166	440,502	430,373	540,376	499,389	339,613	374,335	(447,386)	(267,044)	2,700,559	2,141,524
Net result attributable to minority interest (non-controlling)	-	-	-	-	-	-	-	-	-	-	(9,945)	(13,097)	(9,945)	(13,097)
Net result available to the owner of the parent company	714,448	528,306	1,113,006	576,166	440,502	430,373	540,376	499,389	339,613	374,335	(457,331)	(280,142)	2,690,613	2,128,427
Operating income	5,141,565	4,551,868	1,836,564	1,647,870	521,490	525,617	599,751	714,023	486,806	496,784	(324,710)	(162,313)	8,261,466	7,773,850
Operating expenses	(4,172,072)	(3,782,307)	(794,842)	(705,645)	(107,206)	(77,059)	(226,621)	(225,125)	(118,248)	(104,716)	(52,135)	(55,037)	(5,471,125)	(4,949,889)
Operating result	969,493	769,561	1,041,722	942,224	414,283	448,558	373,130	488,898	368,558	392,068	(376,933)	(217,350)	2,790,341	2,823,960
A. Balance sheet														
Total assets (end of period)	51,906,453	37,771,574	37,771,574	33,222,311	12,872,863	11,697,209	11,876,823	16,521,135	11,852,407	13,287,144	42,443,290	35,687,421	168,538,066	148,186,794
Total liabilities without capital (end of period)	58,364,359	51,272,821	51,272,821	22,547,161	9,610,850	3,272,865	11,229,909	10,244,945	2,724,198	6,223,974	37,547,854	37,255,883	148,187,623	130,817,649
Capital	3,596,939	2,929,836	3,379,903	2,636,098	1,067,849	928,867	1,514,604	1,715,229	1,461,990	1,550,321	9,329,158	7,616,488	20,350,443	17,376,839
C. Key Indicators / Parameters														
Cost and income ratio	81%	83%	43%	43%	21%	15%	38%	32%	24%	21%	16%	34%	66%	63%
Credit and deposit ratio (net)	90%	74%	275%	330%	138%	547%	649%	905%	0%	0%	18%	5%	114%	126%
Return on average allocated capital	20%	18%	33%	22%	41%	46%	36%	29%	23%	24%	-5%	-4%	13%	12%

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017****36. ADDITIONAL CASH FLOW INFORMATION**

	RSD thousand	
	31 December 2017	31 December 2016
Cash	2,798,893	2,566,155
Gyro account	8,681,382	8,276,530
Loans to banks	<u>1,150,593</u>	<u>457,731</u>
Balance as at 31 December	<u>12,630,868</u>	<u>11,300,417</u>

The mandatory reserves with the National Bank of Serbia are not available for day-to-day operations and therefore are not part of cash and cash equivalents (Note 15).

37. EVENTS AFTER THE REPORTING PERIOD

There were no events after the balance sheet date that would require corrections or disclosures in the individual financial statements for 2017.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2017

38. EXCHANGE RATES

The official middle exchange rates of the National Bank of Serbia for major currencies as determined in the interbank foreign exchange market and used in the translation of the statement of financial position components denominated in foreign currencies into functional currency as of December 31, 2017 and December 31, 2016 were as follows:

	<u>31.12.2017</u>	<u>In RSD</u> <u>31.12.2016</u>
EUR	118.4727	123.4723
USD	99.1155	117.1353
CHF	101.2847	114.8473

Novi Sad, 28 February 2018

Approved by the Management of Erste Bank a.d., Novi Sad



Stevan Ćomić
Head of Accounting and
Controlling Department



Aleksandra Radić
Member of the Executive
Board




Slavko Ćarić
President of the Executive Board