Banka Ekonomike

Annual Report 2016

Banka Ekonomike

Content

Message from the Chief Executive Officer

2016 was another successful year.

I am pleased to share with you bank's achievements for the past year. 2016 has been another successful year for Banka Ekonomike.

All key business objectives of 2016 have been exceeded and improvements have been achieved in a number of key performance indicators.

In addition to several years of successful performance, 2016 is characterized with the highest financial result ever achieved. Profit for 2016 reached the amount of 5 million euros, which represents an increase of 24 percent compared to 2015, and a return on equity of 23 percent.

Banka Ekonomike continues to be an important contributor to the economic development. Given the fact that the majority of enterprises in Kosovo belong to the category of small and medium enterprises, which directly impact country's economic development, Banka Ekonomike during 2016, in line with its strategy and the country's development strategy, continued to support small and medium-sized enterprises, including agriculture sector. However, special focus was dedicated to natural persons, providing products and services, which have helped in increasing their welfare.

We continued to have a prudent lending approach, with a further diversification of the portfolio, an approach reflected in the quality of lending and our new loan provisions, which had a downward trend, respectively 52 percent less compared to the previous year and an improvement in the level of non-performing loans from 6.72 percent in 2015 to 5.44 percent in 2016.

As a result of prudent growth in loans, Bank Ekonomike during 2016 marked an increase of 16 million euro in the loan portfolio, namely an increase of 12 percent and an increase of 39 million euro in Bank assets, namely 21 percent. Our clients' deposits have reached the highest growth ever, namely an increase of 35 million euros in 2016, reaching the level of 200 million euros. This level of deposits shows clients' confidence in the bank and in our services.

Thanks to the careful growth of net revenues and effective management of expenses, the efficiency indicator (cost/income ratio CIR) improved from 60 percent in 2015 to 55 percent in 2016.

2016 was also a year of investments in electronic banking services to enable our customers to perform banking services 24 hours 7 days a week. Some branches have been redesigned and standardized; we have opened four self-serving spaces, and launched the new E-banking platform.

We continue to pursue our vision, oriented to sustainable and quality growth, quality services and high standards of professionalism. Strengthening legal compliance, full compliance with applicable laws and regulations, have been some of the Bank's main activities and priorities.

In conclusion, none of the abovementioned achievements would have been possible without the support, commitment and loyalty of our Bank employees.

While appreciating the trust of our precious clients and the dedication of our employees, we will continue to remain committed to providing the best services and products for our clients and to improve the welfare of citizens.

Looking forward, we have pledged that 2017 will be another successful year.

Merita Gjyshinca Peja
Chief Executive Officer

LOANS
148 million euro
+12%

DEPOSITS
200 million euro
+22%

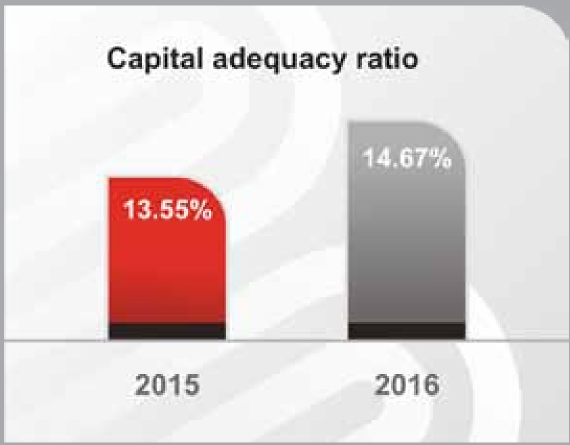
PROFIT
5 million euro
+24%

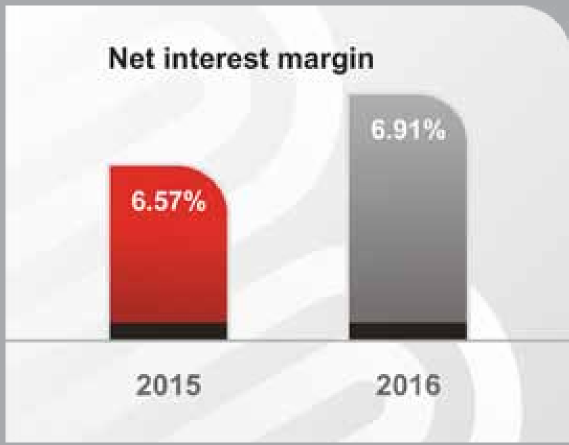
Return on Average Equity (ROAE)
23%

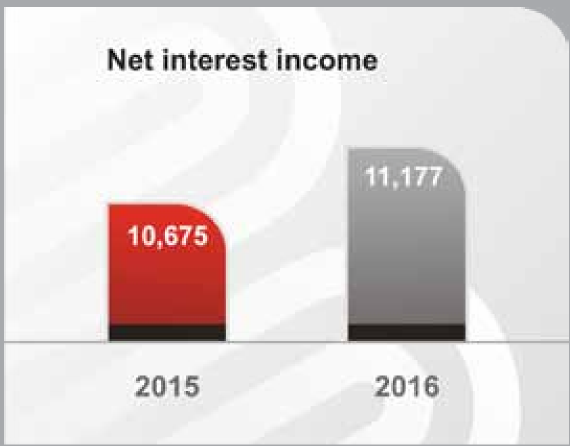
Executive Management

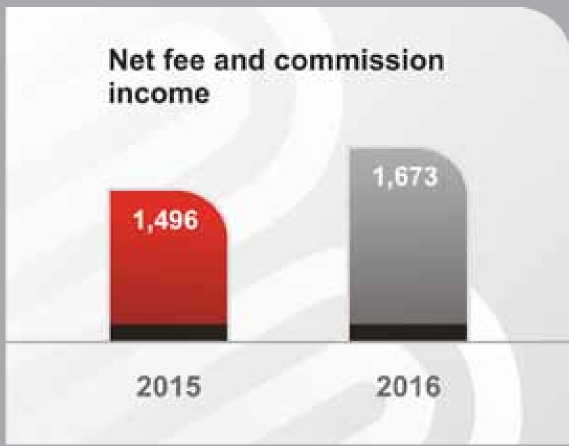
Merita Gjyshinca Peja
Chief Executive Officer

Hamide Pacolli Gashi
Deputy Chief Executive Officer

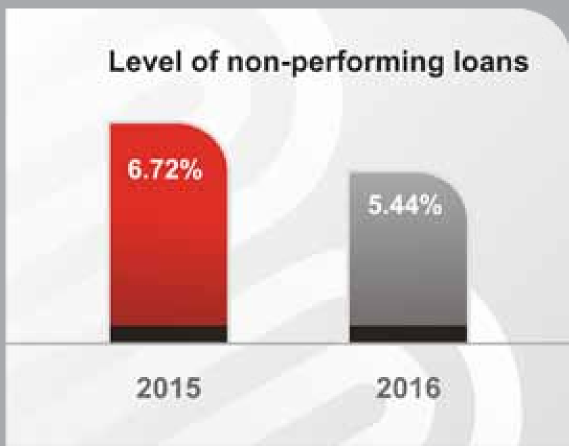

Capital adequacy ratio
13.55%
14.67%
2015
2016


Net interest margin
6.57%
6.91%
2015
2016


Net interest income
10,675
11,177
2015
2016


Net fee and commission income
1,496
1,673
2015
2016

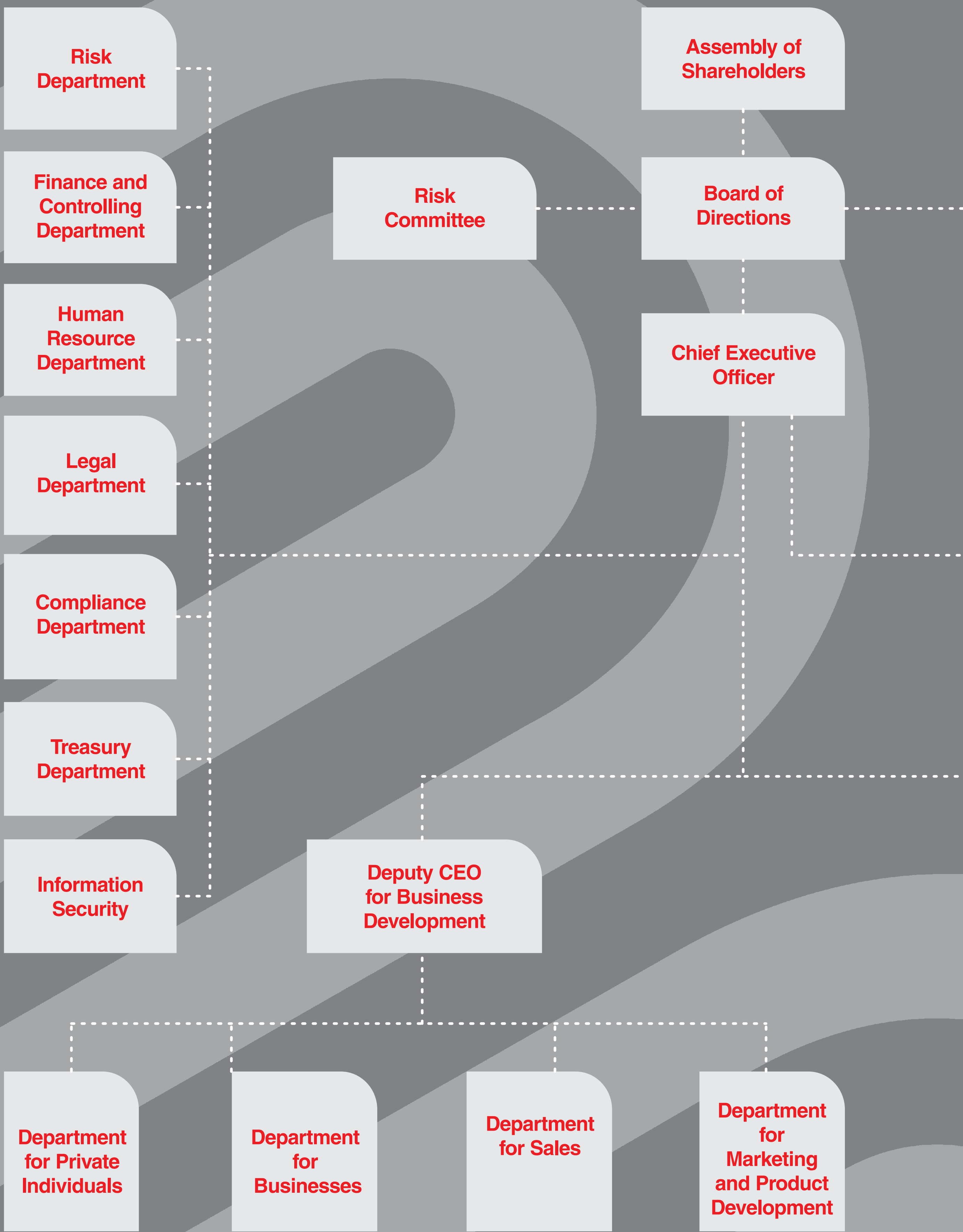

Operating expenses
7,350
7,734
2015
2016

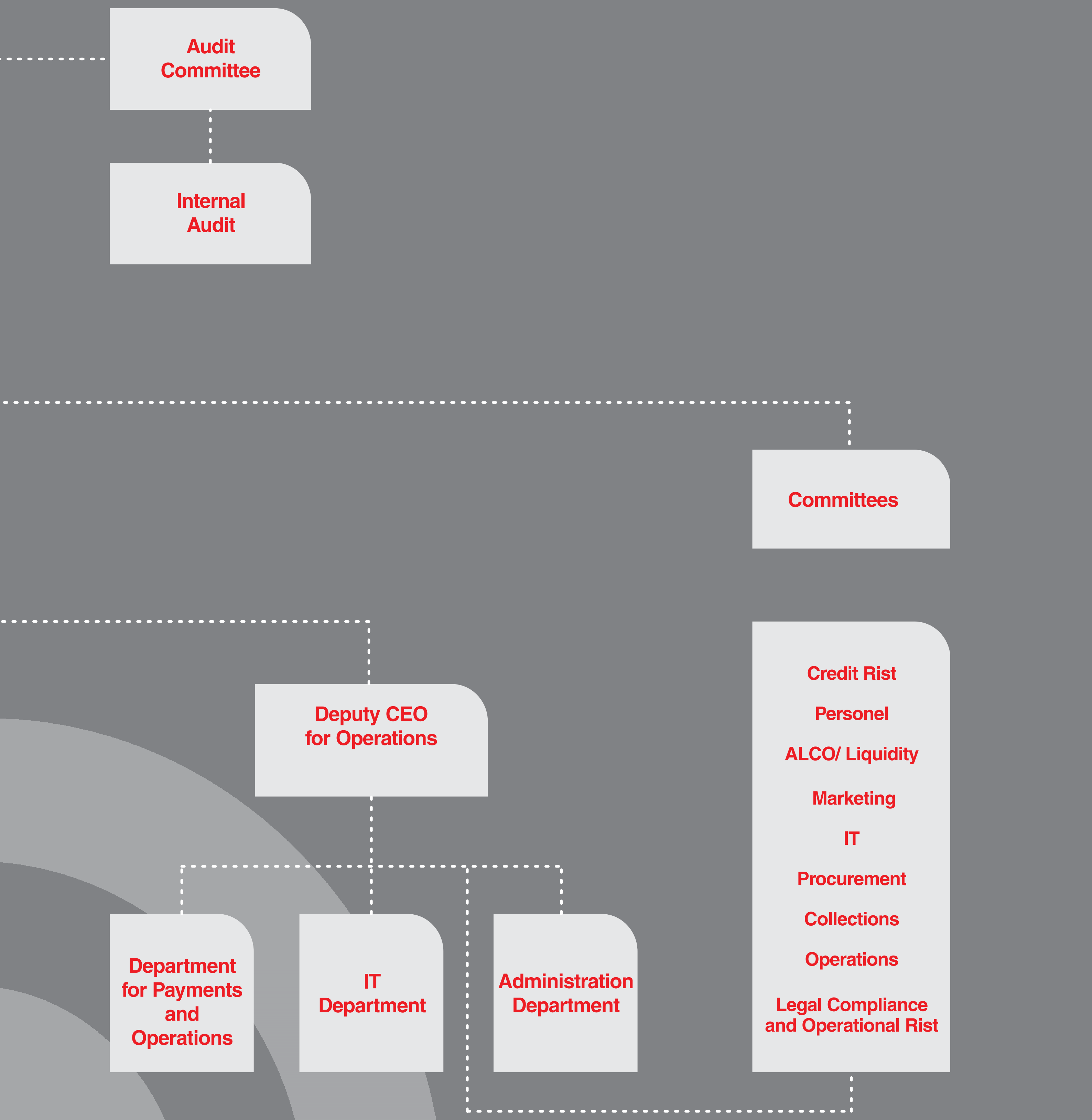

Level of non-performing loans
6.72%
5.44%
2015
2016


Cost/income ratio (CIR)
59.86%
54.83%
2015
2016


Profit before tax
4,037
5,011
2015
2016

Self-Service 24/7


Risk Department
Finance and Controlling Department
Human Resource Department
Legal Department
Compliance Department
Treasury Department
Information Security
Risk Committee
Assembly of Shareholders
Board of Directions
Chief Executive Officer
Deputy CEO for Business Development
Department for Private Individuals
Department for Businesses
Department for Sales
Department for Marketing and Product Development


Audit Committee
Internal Audit
Committees
Credit Rist
Personel
ALCO/ Liquidity
Marketing
IT
Procurement
Collections
Operations
Legal Compliance and Operational Rist
Deputy CEO for Operations
Department for Payments and Operations
IT Department
Administration Department

Vision

A bank oriented in sustainable and qualitative growth, qualitative services and high professional standards.

Mission

Being the role **MODEL** domestic bank, by:

Enabling our clients an easy and rapid access to the diversified banking products, increasing the value for clients, employees and shareholders;

Domestic provider of the electronic banking services;

Determined for professional development of our employees;

Ethics, respect and team work are our values;

Laws, policies and procedures are strictly observed!

Briefly on Banka Ekonomike

Banka Ekonomike commenced its operation as a licensed bank on 28.05.2001, being the only bank with 100 percent domestic capital.

Banka Ekonomike is an important factor in the banking market. Banka Ekonomike continues to stay close to its clients, to successfully maintain the support of loyal clients, bank associates and employees.

We have human resources with appropriate training and qualifications, whereby every employee is professionally prepared, works punctiliously for the market and for the institution, creating value in every action. Professional development of our employees has been our special focus in our journey as one of the main factors in providing professional services. We consider our 335 employees among the key assets of the bank.

The network of Banka Ekonomike has been developed according to market demands throughout the entire territory of Kosovo. As a result of this development we have 33 banking units out of which 7 branches are in Kosovo's main centers and 26 branches located in smaller regional units of our country.

Special focus is given to modernization of the branch network throughout Kosovo; therefore in 2016 we have re-designed the sub-branch in Fushë Kosovë and Gjakova branch, whereby the main purpose was to enhance the quality and services for our clients. A particular specificity is the 24/7 self-serving space containing the most advanced electronic and technological technology.

Banka Ekonomike continued to enhance the quality of services by developing and adapting products according to client's expectations. Following the rapid advancements in technology, we have continually improved and expanded our distribution channels, including the branch network, e-banking, call center, SMS banking, Points of sale (POS), ATMs, enabling clients 24/7 access to bank products and services.

The corporate social responsibility plays a significant role; our goal is to contribute to the social development of the country, with particular focus on supporting initiatives that improve the situation of different social categories and community in general.

Macroeconomic environment in Kosovo

Kosovo’s economy continued to record a positive growth rate even in 2016. GDP increased by 3.5 per cent in 2016.

Whereas the main funding sources of economic growth were domestic resources, such as bank lending and public/capital investments, revenues from external sector are characterized by a more unfavorable performance as a result of the decline in exports, remittances and foreign direct investments.

Kosovo continues to have a satisfactory level of fiscal stability, expressed through relatively low ratios of budget deficit and public debt to Gross Domestic Product.

Remittances continue to play an important role in the economy, both in terms of contributing to the growth of domestic consumption as well as in balancing national payment accounts. In addition, the country continued to strengthen the fiscal system by keeping the deficit below 1.5 percent of GDP and at the same time reduced the fiscal evasion, boosting the public budget stability. Inflation was estimated at about 1.3 percent in December 2016; however the main negative indicator remains the trade deficit, while imports reached 2.5 billion euros, whereas exports amount to 331 million euros.

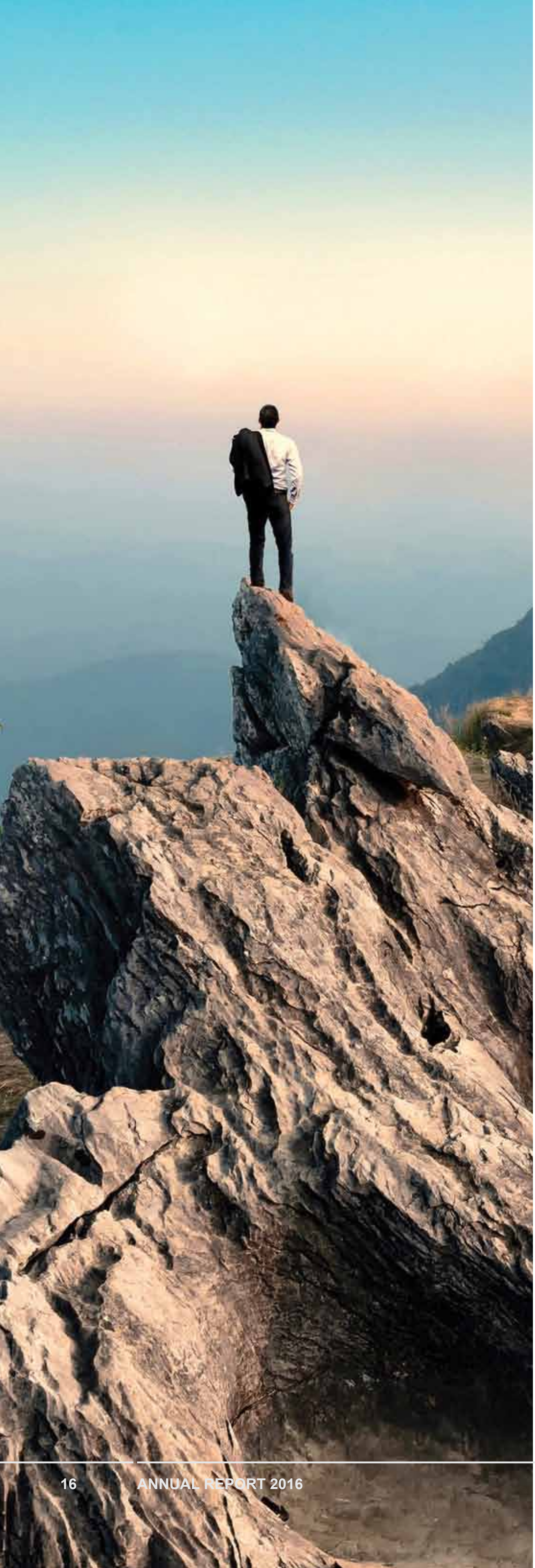
Forecasts for 2017 remain the same, with an increase of 3.5 percent, driven mainly by domestic sources, however, although the mid-term projections are positive, they are deemed to be insufficient for Kosovo’s needs.

Banking sector

The banking sector continued the stable growth. The capital adequacy ratio was over 18 percent, profitability remained at a satisfactory level. Liquid assets cover about 40 percent of short-term borrowings which is above the suggestions of international financial agencies. The quality of assets was further improved; it is thought that the involvement of private enforcement agents has had an impact on this, by reducing the level of non-performing loans from 6.2 percent in 2015 to 4.6 percent in 2016. The loan interest was reduced, but this was offset with reduction of bank expenses, which helped boost the demand, but again the penetration of loans in relation to Gross Domestic Product remained low, in response to this problem, the Credit Guarantee Fund was implemented, which partially secures loans that are not secured by collateral. The largest share of banking sector loans continues to consist of loans to enterprises, representing 64.8 percent of total loans, while household loans represent 35.0 percent of total loans.

Deposits continue to be the main source of funding for banking sector activities, which recorded an annual growth of 4.6 percent. The growth rate of deposits recoded a slowdown for the second year in a row, whereby the deposits of enterprises were characterized by a more pronounced slowdown in the growth rate, the main cause being the fall in the interest rate on deposits. Household deposits, which are a more stable source of funding in relation to other funding channels, continue to dominate the banking sector's deposit structure, representing 74.4 percent of total deposits.

[1] *Source:*
The following information is based on materials published by the Central Bank of the Republic of Kosovo - Financial Stability Report as well as from the International Monetary Fund



Positioning of Banka Ekonomike in Kosovo's banking market

Banka Ekonomike has marked a steady growth in all financial indicators. As of the end of 2016, the total assets of Banka Ekonomike were 223 million EUR. The assets of the bank increased by 39 million EUR in 2016 compared to the end of 2015 where the bank's assets level was 184 million Euros.

Participation in loans

Credit portfolio of Banka Ekonomike continued to grow steadily in 2016. Its participation on total loan market was 6.69%.

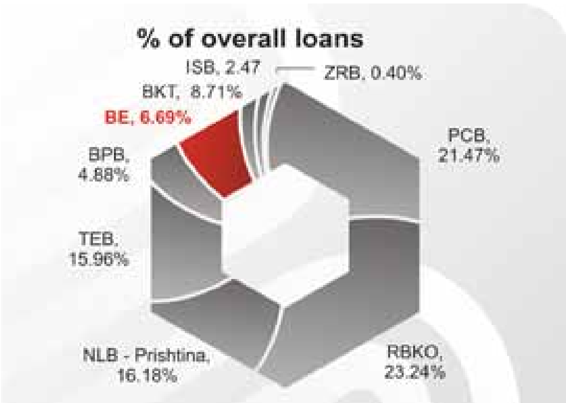


Figure 1: Participation by banks in total loans, 31 December 2016

Participation in deposits

Performance of deposit portfolio marked a record growth. In 2016, the deposit market at Kosovo level increased by 8.1%, whereas deposit growth rate of Banka Ekonomike in market was 21.0%. Consequently, participation of Banka Ekonomike in total market deposits was 7%.

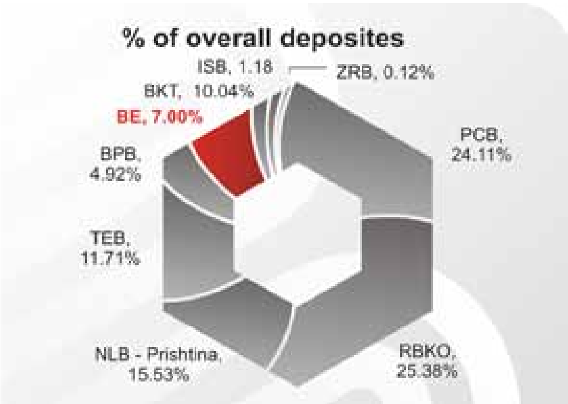


Figure 2: Participation of banks in total deposits, 31 December 2016.

This is a promising indicator which, one the one hand shows the increasing reliability of our clientele, while on the other hand, makes us believe that this trend will enable Banka Ekonomike to increase participation in the market over the future periods.

The efficiency indicator (cost to income ratio/ CIR) of Banka Ekonomike has also undergone significant changes in 2016. Namely, this ratio has been improved from 59.86% to 54.83%.

With improvement of Bank's processes and cost optimization, Banka Ekonomike will continually improve this important indicator.

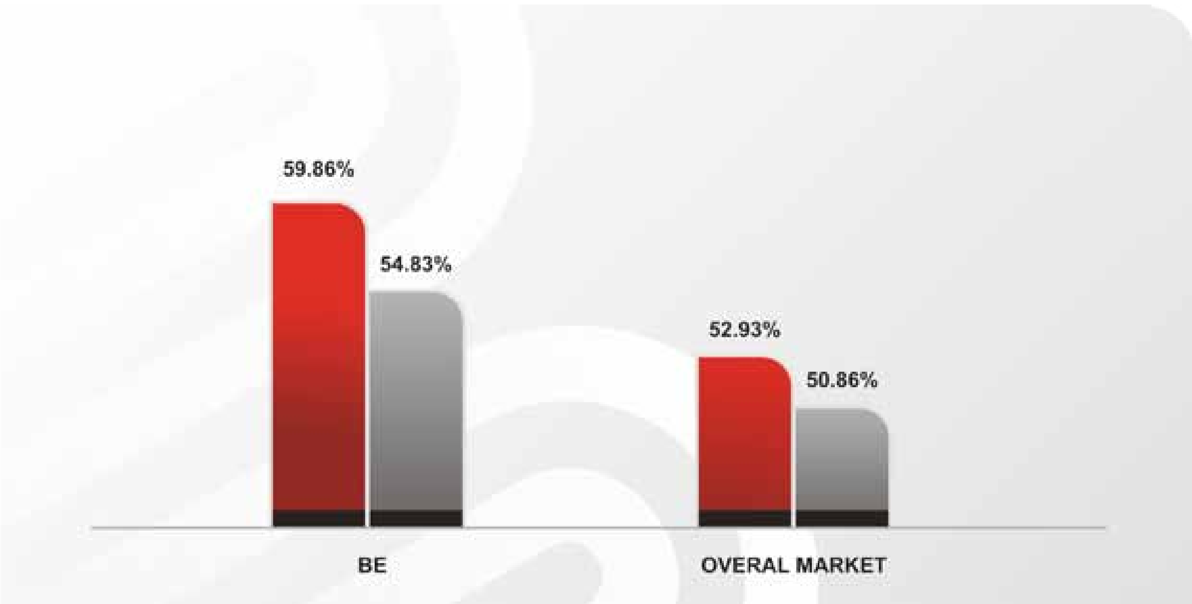


Figure 3: Cost to income ratio, CIR, 2015 and 2016.

Note: *Market analysis is based on financial data published by commercial banks (according to the rules of the Central Bank of Kosovo, CBK).*

Statement of Financial Position

All numbers are in '000 Euros!	As at 31 December 2016	As at 31 December 2015
Cash on hand and at banks	16,113	15,397
Balances with the Central Bank of Kosovo	36,867	17,572
Loans to customers	137,928	122,077
Investments in securities	24,770	21,610
Property and equipment	6,089	6,226
Intangible assets	394	271
Prepaid income tax	-	74
Other assets	843	692
Total assets	**223,004**	**183,919**
Liabilities		
Due to customers	197,708	163,751
Due to banks	2,196	1,393
Subordinated debt	1,050	1,050
Current tax liability	172	312
Other liabilities	439	535
Total liabilities	**201,565**	**167,041**
Equity and reserves		
Share capital	16,777	14,778
General risk reserve	102	102
Retained earnings/(Accumulated losses)	4,560	1,998
Total equity and reserves	**21,439**	**16,878**
Total liabilities, equity and reserves	**223,004**	**183,919**

Statement of Profit or Loss and Other Comprehensive Income

All numbers are in '000 Euros!	For the year ended December 31, 2016	For the year ended December 31, 2015
Interest income	13,450	13,571
Interest expense	(2,273)	(2,896)
Net interest income	**11,177**	**10,675**
Fee and commission income	2,356	1,950
Fee and commission expense	(683)	(454)
Net fee and commission income	**1,673**	**1,496**
Other operating income	31	53
Net foreign exchange losses	23	(68)
Revenue	**12,904**	**12,156**
Other operating expenses	(7,891)	(7,460)
Net impairment losses on loans	(2)	(659)
Total operating expenses	**(7,893)**	**(8,119)**
Profit before tax	5,011	4,037
Income tax	(451)	(327)
Net profit for the year	**4,560**	**3,710**
Other comprehensive income	**-**	**-**
Total comprehensive income for the year	**4,560**	**3,710**

Performance of Banka Ekonomike

The year 2016 for the Banka Ekonomike can be considered as the most successful year in all segments of business. All key business objectives of 2016 have been exceeded. Significant progress has been recorded in all key financial indicators, net interest income has increased by 502 thousand EUR, respectively, 4.7%, whereas fees and commission incomes have increased by 406 thousand EUR, or 21%, thus, indicating a qualitative progress in our bank's financial performance. Another determinant is the qualitative growth of loans, as well as credit risk diversification in small, micro and medium loans. Another positive indicator is the reduction of the level of reserves, through the reduction of nonperforming loans. In addition, the bank pursued a strategy of increasing combined services, wherein the primary purpose is to maintain customer satisfaction as the bank's main objective.

As a result of all these positive indicators, the bank managed to close the year with success, respectively, profit before tax was 5 million EUR.

Bank assets

As a result of positive trends of financial indicators, bank assets have increased by 21% compared to the previous year. Increased asset level is a result of good performance, quality offer, flexibility and swiftness at work, which significantly affected the bank's competitive ability in the market.

Figure 4: Assets of Banka Ekonomike, 2010- 2016.
All numbers are in'000 EUR.

Loan performance

In an increasingly competitive environment in the banking sector during 2016, Banka Ekonomike managed to have dynamic growth in the loan portfolio. The loan portfolio recorded a sustainable growth throughout all quarters of the year, including the private and business sector. Thus, during 2016, the loan portfolio increased by 12%, from 132.0 million EUR to 147.9 million at the end of 2016.

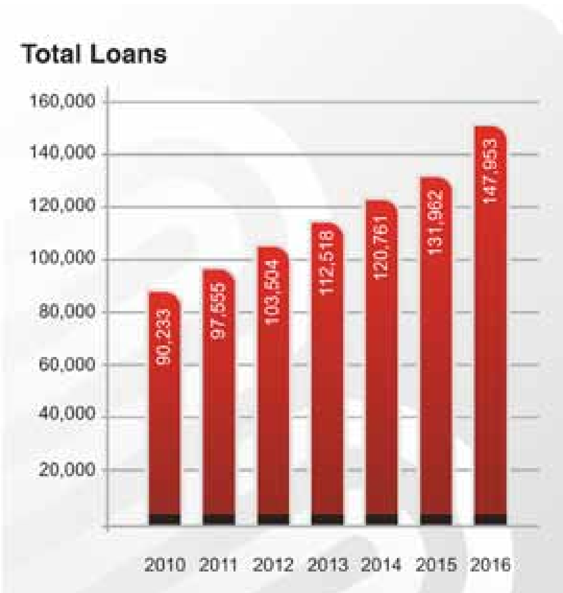


Figure 5: Loans Portfolio, 2010- 2016.
All numbers are in '000 EUR.

Deposit performance

Banka Ekonomike has continued with the controlled deposit growth strategy, seeking to maintain a satisfactory level of profitability.

During 2016, deposits increased by 35 million EUR. The deposits level was 165.1 million EUR in December 2015, and increased to 199.9 million EUR at the end of 2016. This indicates the bank stability and the trust our customers have toward the bank.

Figure 6.Customer deposits, Banka Ekonomike 2010-2016. All numbers are in"000 EUR.

During 2016, the Bank was more focused on the effective management of deposits. It is worth mentioning that deposits at the end of the year have exceeded the objectives set, maintaining an excellent level of loans to deposits ratio of 74.01%.

Interest and non interest incomes

Euro '000	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**
Interest income	9,908	12,442	13,300	13,637	13,552	13,571	13,450
Deposit costs	3,626	4,859	5,398	5,557	4,116	2,896	2,273
Net interest income	**6,282**	**7,583**	**7,902**	**8,080**	**9,436**	**10,675**	**11,177**
Net fees and commission income	**1,204**	**1,321**	**1,370**	**1,425**	**1,482**	**1,496**	**1,673**

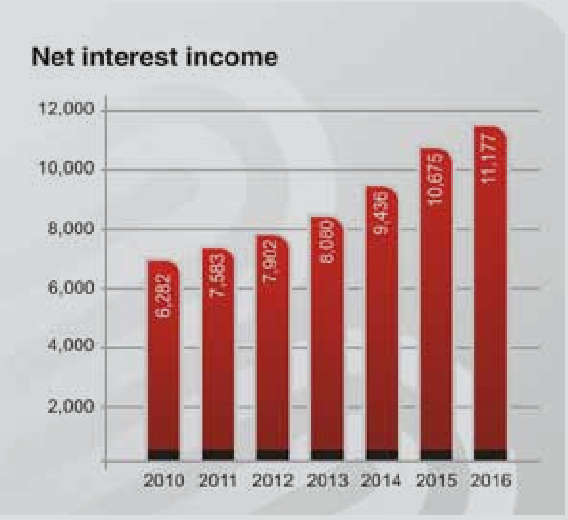


Figure 7: Net interest income, 2010- 2016
All numbers are in'000 EUR.

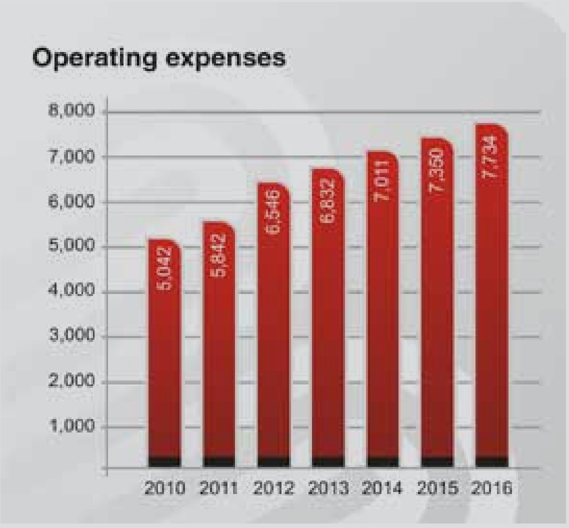


Figure 8: Operating expenses, 2010- 2016;
All numbers are in'000 EUR.

Operating expenses

EUR '000	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**
Administrative expenses	2,278	2,618	3,083	3,380	3,481	3,718	4,081
Personnel Expenses	2,180	2,640	2,639	2,454	2,520	2,787	2,793
Depreciation expenses	584	584	824	998	1,010	845	859
Total operating expenses	5,042	5,842	6,546	6,832	7,011	7,350	7,734

During 2016 we had a slight increase in operating expenses. The increase in these expenses is mainly attributable to administrative expenses, which are the result of more frequent engagement of consultants/ experts from abroad, increased presence in the market through various marketing campaigns, increase of the level of security and various investments in distribution channels.

Business development

The year 2016 is characterized by an increased dynamics of bank activities in terms of lending.

Our main focus was qualitative placement of loans in market. The quality and level of credit portfolio was increased in all business segments, including the private individuals segment. Particular focus was paid to small and medium enterprises, which are considered as main pillars of economic development in our country.

Doing business in a competitive environment, it is necessary to increase the efficiency of all bank operations, in particular the provision of qualitative and functional services to our customers. In this regard, in line with the needs and requirements of our clients, we have revised our policies and procedures, increased the number of credit products and service level. We have continued with various trainings for our employees, both inside and outside the country, which are necessary activities for long-term and sustainable business development and growth. In addition to investment in staff, we have also paid special attention to the bank's image, respectively, rebranding our branches and creating better conditions/environment for our customers. A particular feature in this process is the self-service areas, equipped with sophisticated technology, which makes us stand out from competition as an innovative bank with an advanced vision.

During 2016, we have continued with activities that are related to motivation of the staff, whether financial or nonfinancial motivation, including numerous socialization activities and empowerment of teamwork, as an integral part of our values.

Total loans

In full accordance with bank's strategy for a continuous and sustainable growth of loan portfolio, 2016 is characterized as one of the most successful years in the lending field. During 2016, over 95 million euro credit products were disbursed to more than 10,000 customers, resulting in a successful growth of the loan portfolio by 16 million euros or 12.1 percent compared to the previous year.

Adapting credit policies and procedures pursuant to the new circumstances created in the banking market, enhanced expeditiousness, customer-based orientation, tailored products for specific customer groups and quality services were just some of the reasons for the bank's success in this area.

During 2016, we have been very focused on portfolio diversification, with special focus on micro and agro businesses, the development of small and medium enterprises and individual customers, while we have had selective access to financing for amounts over 500 thousand Euros. All this is reflected in the following tables:

Loans by amount '000	2013	%	2014	%	2015	%	2016	%
Up to 100 thousand euros	43,827	39%	51,454	43%	64,669	49%	75,991	51%
100 up to 500 thousand euros	26,514	24%	30,269	25%	29,895	23%	30,985	21%
Over 500 thousand euros	19,231	17%	15,792	13%	15,021	11%	18,286	12%
Overdraft	22,946	20%	23,246	19%	22,377	17%	22,691	15%
Total loans	**112,518**	**100%**	**120,761**	**100%**	**131,962**	**100%**	**147,953**	**100%**

Loans by segments '000 Euro	2013	%	2014	%	2015	%	2016	%
Individuals	29,298	26%	35,136	29%	43,984	33%	50,016	34%
Businesses	83,220	74%	85,625	71%	87,978	67%	97,937	66%
Total loans	**112,518**	**100%**	**120,761**	**100%**	**131,962**	**100%**	**147,953**	**100%**

Micro businesses

The micro business segment is one of the most important segments of a country's economic development. Since most of the enterprises in Kosovo belong to the micro segment, our bank undertook concrete steps to support and finance this segment.

Banka Ekonomike, as the only bank with 100 % domestic capital, feels increased responsibility for active participation in local economy development and has designed all banking products and services tailored to small enterprises, micro and agro customers.

During 2016 we provided financial support facilities for agro clients, a sector that had difficulties in securing the collateral and consequently, through cooperation with USAID (Development Credit Authority, DCA), greater lending opportunities have been created.

Another important cooperation is the agreement reached with the Kosovo Credit Guarantee Fund, a cooperation that will help us resolve the lack of collateral for clients who have difficulties in this regard.

Our support to this sector is evidenced by the fact that we have an increase of credit limits by around 12 percent, compared to last year. Taking into account the geographic structure and the population distribution, where rural population dominates, the focus on agro business activities has been and remains the main focus in the years to come.

During 2016 we have increased the training activities for the staff responsible for this category of businesses and in cooperation with USAID we have organized additional trainings for our employees.

We continue to be oriented in this segment, with a special focus on increasing business transparency, raising awareness and financial literacy.

Small and medium enterprises

Small and medium enterprises are a key factor in the economic development of Kosovo, so our bank has designed different financial packages influencing their development and consequently contributing to the economic development of our country.

The main goal of the small and medium enterprise portfolio during this year was to identify the needs and requirements of each client, the modification and harmonization of internal procedures in order to adapt to the requirements of this important market segment.

In addition to credit products, the Banka Ekonomike worked on the development and design of other products such as E-Banking, debit and credit cards, SMS services as well as 24/7 self service areas with a modern design and look, adapted to the market needs and our customers, where special attention in these self service areas is given to the possibility of deposition and turnover, as well as national and international transfers 24/7, without being limited to the official schedule of the bank.

Individual customers

The development of the individual customer segment and the growth of the loan portfolio has been an essential part of the year 2016. The growth of customer base by 11.17 per cent and of the credit portfolio by 13.71 per cent shows the focus of the Banka Ekonomike in this segment in order to provide customers the opportunity to realize their respective plans and goals. This increase demonstrates the continued commitment of Banka Ekonomike to improving living conditions and standards of living.

Individual customers continue to be a key part of the bank's development, affecting the stability of the credit portfolio, deposits share and the use of banking services. This prompts the bank to pay particular attention to this category in order to provide adequate services and products, by simplifying processes, reducing time and being flexible to customer needs/requirements.

Development of products and Marketing

Even this year, the bank has paid particular attention to the field of marketing and promotion of various activities of importance for society. During 2016, we have realized and launched various campaigns in the marketing channels, both in the field of business and in the promotion of the bank as an important institution for Kosovo society.

The continued presence in social networks as well as standard marketing channels resulted in successful sales, creation of positive image and achievement of bank's overall objectives.

We have continued with the standardization of designs and advertisements in our branches and sub-branches. The Gjakova and Fushe Kosova branches have been relocated and designed according to the new brand and standard, thus providing a more convenient environment, better communication, easier and faster access to banking products and services.

In meeting the banking customers' needs, we have brought innovation to these branches, by creating 24/7 self-service areas which enable the delivery of services quickly and safely.

24/7 self-service areas contain high-tech equipment, enabling access to E-Banking. Also in ATMs for cash depositing, our business and individual customers can deposit money at any time, 24/7.

According to the new brand, external ATMs have been designed which have resulted in a more pronounced visibility. Special focus has also been on improving the social environment, whereby through the activities and initiatives with different social categories, we have managed to create a better environment for these categories of society.

Following the course of modern development of banking market, in order to provide the best, modern and safe services for our customers, Banka Ekonomike has developed and launched the new E-Banking platform, a very advanced platform that meets the requirements and needs of our customers.

A new feature of this platform is that clients can connect to many contracts, by authorizing several people with different levels of authorization.

Distribution Channels

Network of branches

Banka Ekonomike continues to have a high participation of its branches in the banking market, respectively 13 percent in the total branch network at the country level.

During 2016 in order to rationalize the branch network, 3 sub-branches were closed down, while two branches were located in more suitable environments, in order to increase the quality of services and to be closer to our customers.

High market participation indicates the determination of Banka Ekonomike to stay closer to customers and provide appropriate advice on banking products and services, as well as in raising the knowledge level on the benefits of using alternative channels.

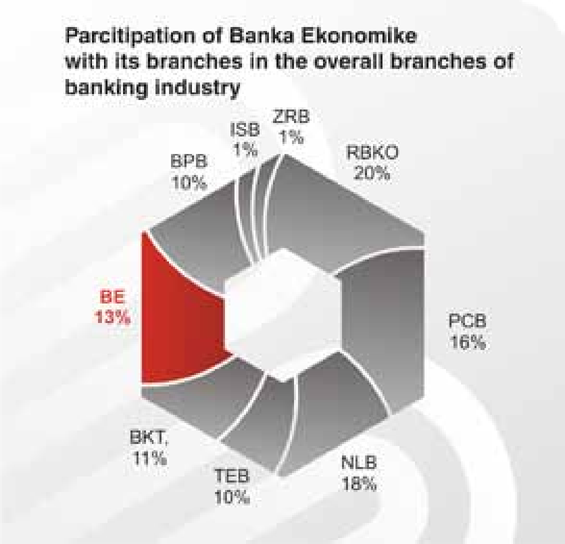


Figure 9: Parcitipation of Banka Ekonomike with its branches in the overall branches of banking industry

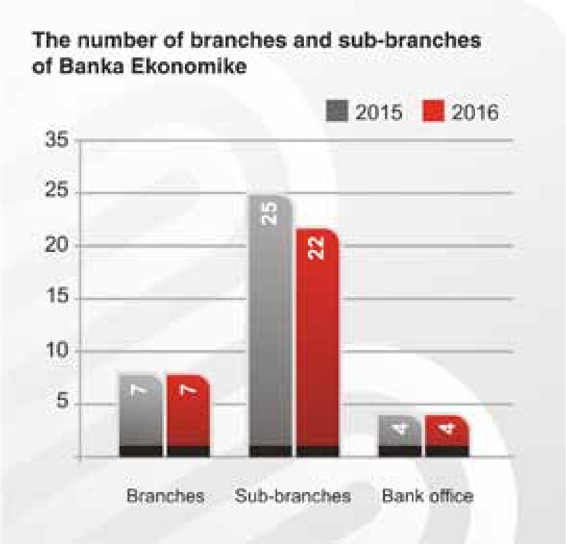


Figure 10: The number of branches and sub-branches of Banka Ekonomike

Alternative distribution channels

In addition to the extensive branch network, Banka Ekonomike has continuously developed and expanded other alterative channels.

One of the advantages of high quality services for the customers of Banka Ekonomike is the call centre with a dedicated team that provides services 24/7.

Banka Ekonomike continues to have a wide network of ATMs distributed throughout the territory of Kosovo. The number of ATMs at the end of 2016 has reached 52. Parts of self-service areas are no doubt our ATMs with the possibility to deposit funds at any time. The wide network of ATMs and distribution throughout the territory of Kosovo has enabled the number of transactions to increase by 33 percent compared to 2015.

During 2016, the Bank analyzed the performance of the point-of-sale (POS) terminals, by relocating them to traders who are frequented by our customers, in order to strengthen customer-bank relations, while the customer is allowed to make the installment payments free of charge.

Customer Care

The opinions and suggestions of the customers have played and will continue to play a key role in improving the quality of the services provided.

The Banka Ekonomike, through the customer care unit has addressed every request or suggestion with great dedication, as a guide to improve our processes and services.

The Banka Ekonomike continues to provide the client with the right financial advice through this unit so that customers can benefit from banking services that meet their needs by continuing long-term sound relationships.

Even during 2016, dedication to the swift and efficient handling of customers' requests and suggestions, alongside the improvement of processes, has been essential towards increasing the level of services to our customers.

Risk Management

Risk management is considered stable and with continuous improvements.

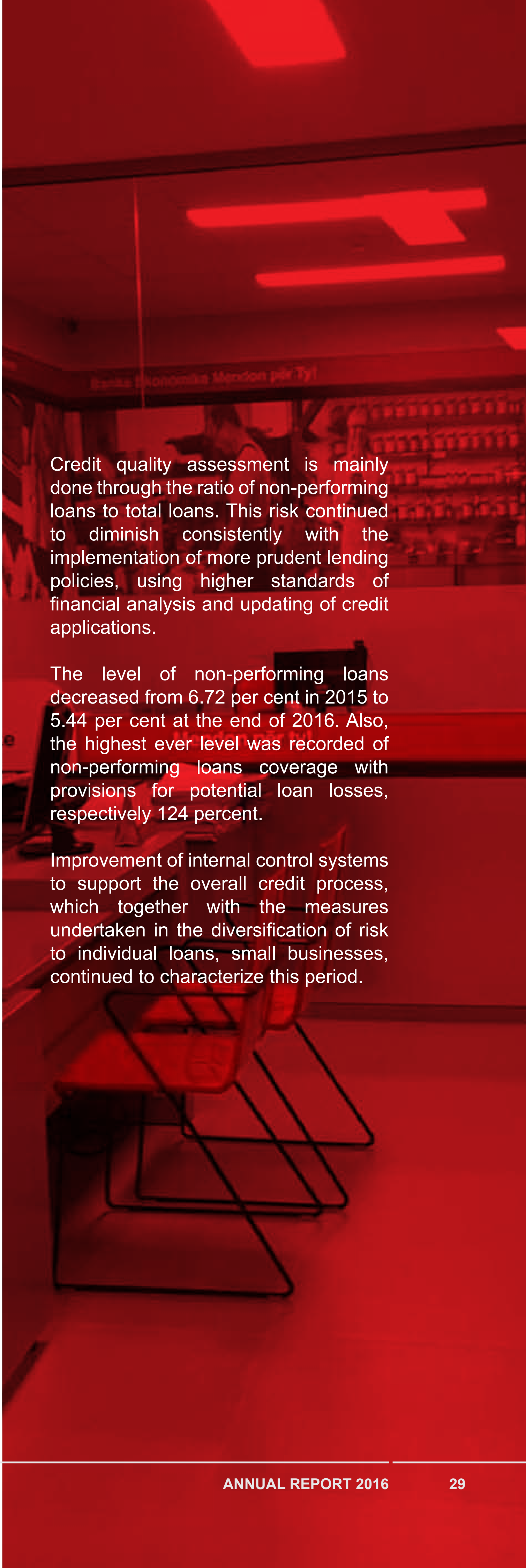
During 2016, all major risk indicators have been improved, such as creating provisions against specific risks, leverage ratio, solvency, profitability, liquidity and the capital adequacy ratio. All of these indicators are significantly higher than the minimum required by the regulator.

Work has been done with high commitment for continuous improvement of processes, establishment of internal control system, aiming at addressing the previously identified shortcomings, and the approximation of existing methods with best banking practices.

Credit Risk

During 2016, a new model of general provisions was established, according to the highest methodologies and standards of the banking industry.

Among with the general improvement of credit portfolio quality, the credit risk concentration rate has continued to decrease, and is expressed as a ratio of the total value of large exposures to tier capital. This decline the concentration in the overall value of large exposures and the number of large credit exposures.



Credit quality assessment is mainly done through the ratio of non-performing loans to total loans. This risk continued to diminish consistently with the implementation of more prudent lending policies, using higher standards of financial analysis and updating of credit applications.

The level of non-performing loans decreased from 6.72 per cent in 2015 to 5.44 per cent at the end of 2016. Also, the highest ever level was recorded of non-performing loans coverage with provisions for potential loan losses, respectively 124 percent.

Improvement of internal control systems to support the overall credit process, which together with the measures undertaken in the diversification of risk to individual loans, small businesses, continued to characterize this period.

Operational risk

To identify banking risks, we have considered changes in internal and external factors, including: bank structure, nature and complexity of processes, changes in the banking industry, technological advancements, etc. To this end, the bank has built several mechanisms, one of which is setting and monitoring the limits of the key operational risk indicators. Determining KRI and setting their limits is an important tool in the management of operational risk used to improve risk monitoring and mitigation. Also, many management activities have been held in order to raise awareness in Bank level and prevention and reduction of risks.

Liquidity Risk

During 2016, Banka Ekonomike also had a satisfactory level of liquidity, with a high level of highly liquid assets. Key indicators of liquidity have been continuously monitored. Also, liquidity stress tests have been carried on regular basis, in order to have details about potential positions, based on different scenarios.

The ratio of liquid assets to short-term liabilities is used as an assessor of the bank's ability to cover the immediate liquidity needs that may arise as a result of potential short-term liquidity shocks. A higher rate means that the bank has available assets to cover the immediate demands of depositors, or other bank's creditors.

Foreign currency risk management

The Bank has relatively low tolerance to this risk and does not conduct speculative trading activities. Foreign currencies are mainly used for business continuity needs with correspondent banks. Open positions in foreign currencies are managed on a daily basis, including foreign currency exchange movements, continuously, so the foreign currency risk remains very low.

The Banka Ekonomike manages foreign currency positions in accordance with foreign currency risk management policy and in compliance with CBK regulations, which have never been exceeded during 2016.

The Banka Ekonomike, by year-end, had an open position of all currencies of 0.03 percent with tier capital.

Operations

2016 has been a year of change and adaptation of many processes to the country's legal requirements, without departing from the bank's strategy of procedural facilitation and efficiency enhancement.

The new CIF (client account management platform) has enabled the Bank to comply with legal requirements in the process of opening accounts and updating customer information.

During the second quarter, the bank has begun the process of updating the accounts, a process that will continue in 2017. Through this project, the bank will have a secure, complete, qualitative client portfolio and reduce the operational risk, by recognizing its customer (KYC). Also, this project will help build customer - banking cooperation, provide quality services and compliance with applicable rules and laws.

Local transfers

During 2016, the Central Bank of Kosovo (CBK) has modernized the country's internal payment infrastructure by shifting to the KIPS/ATS payment system, which includes the execution of RTGS payments (normal and priority payments, including giro payments, taxes, wages and so on).

The Banka Ekonomike has adapted the system, continuing to provide services according to the new requirements in the local payments circulation, always aiming at the optimization of processes, where the continuity of this segment has yielded considerable results. The development of the new payment system has enabled speeds in executing client transfer orders, the automation of many work processes, and consequently the reduction of operational risk.

The total amount of incoming transfers through the national payment system has increased by 8 percent compared to the previous year, while national outgoing transfers have increased by 3 percent.

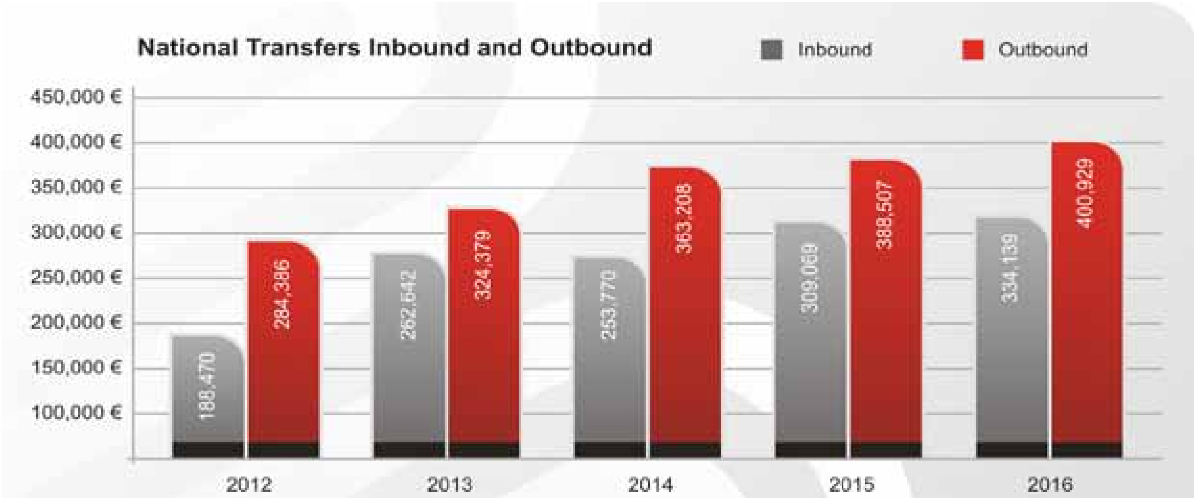


Figure 15: National, Inbound and Outbound Transfers;
All numbers are in '000 Euros!

International transfers

As a result of building long-term relationships with customers and the development of banking infrastructure, the Banka Ekonomike has paid equal importance to the development and improvement of international payment processing, thus increasing co-operation with new correspondent banks. The total value of international transfers during 2016 has increased by 20 percent compared to the previous year.

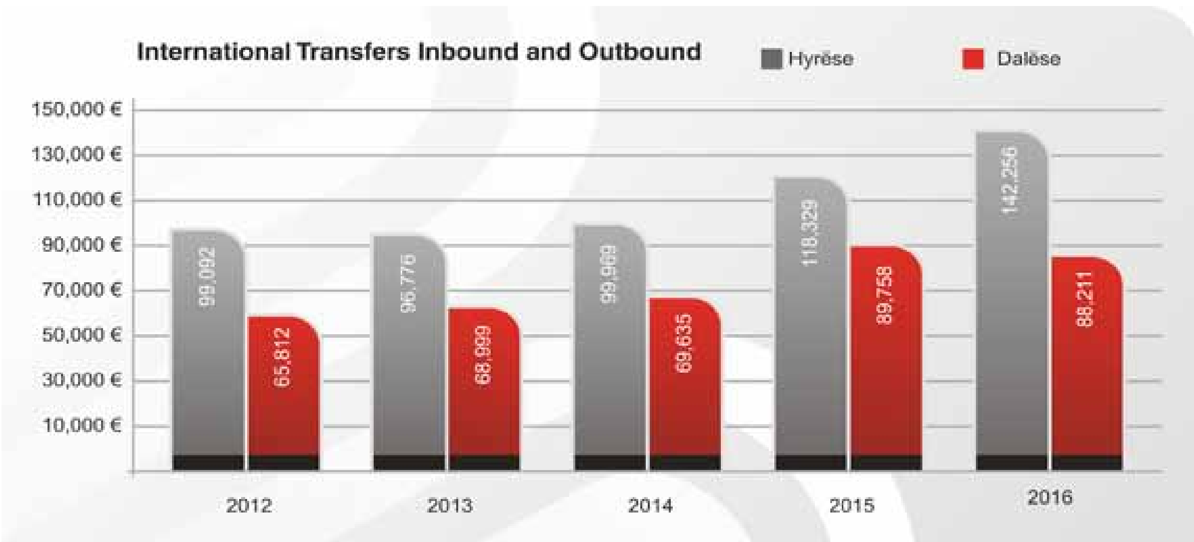


Figure 16: International, Inbound and Outbound Transfers;
All numbers are in '000 Euros!

Information Technology

The Information Technology Department is an important factor for the continued success of the bank. During 2016, a number of new projects have been completed, and information systems have been continuously updated, including numerous upgrades and advancements in the Bank’s main software.

The automation of many reports has improved the reporting process, the internal control process, and has lowered operational risk from potential human errors.

Within the information technology activities, the implementation of the new e-banking platform, the implementation of the new RTGS local payment system, and a large number of other internal developments have been implemented, which have helped to improve a number of processes within the bank.

Management and staff training

The Human Resources Department continues to be a strategic business partner as an important factor in developing and realizing the overall business goals.

During 2016, the main priority has been the professional upgrading of employees, as one of the main business interests of the Banka Ekonomike. Continuous trainings, both internally and abroad have positively impacted the level of professionalism, service to our clients, as well as a good progress and performance of the institution.

The Human Resources Department pays special attention to the recruitment and selection process of professional and competent staff. Improving teamwork, empowering the team, socializing and motivating our employees through various rewards and acknowledgments programs have also been one of the top priorities and activities.

The Banka Ekonomike has also been very active in the development of the internship program. The purpose of the internship program is to offer students the opportunity to gain practical experience in the banking system, where only in 2016 over 70 students were part of this multi-month program.

At the Banka Ekonomike we strongly believe in gender equality, so the gender-based staffing rate is almost the same, with a slight female dominance, included in the managerial and executive positions of the bank!

Years	2012	2013	2014	2015	2016
Number of employees over the years	352	303	321	323	335

BANKA EKONOMIKE SH.A.

Financial Statements prepared in accordance with the accounting rules and regulations of the Central Bank of the Republic of Kosovo for the year ended 31 December 2016 (with independent auditors' report thereon)

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Deloitte.

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors and Shareholders of Banka Ekonomike sh.a.

Opinion

We have audited the financial statements of Banka Ekonomike sh.a. (the "Bank"), which comprise the statement of financial position as at December 31, 2016, and the statement of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements of the Bank are prepared, in all material respects, in accordance with the Article 53, of the Law No.04/L-093, dated 11 May 2012, "Law on banks, microfinance institutions and non-bank financial institutions" (the "Banking Law") as described in Note 2 to the financial statements.

Basis for Opinion

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

Other Matter

The financial statements of Banka Ekonomike sh.a. for the year ended December 31, 2015 were audited by another auditor who expressed an unmodified opinion on those statements on April 12, 2016. The Bank has prepared a separate set of financial statements for the year ended December 31, 2016 in accordance with the International Financial Reporting Standards.

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

Management is responsible for the preparation of the financial statements in accordance with the Banking Law and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

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

Deloitte.

Auditor's Responsibilities for the Audit of the Financial Statements

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

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

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

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

Deloitte Kosova Sh.p.k.

Deloitte Kosova sh.p.k.
Str. Ali Hadri, nn,
Prishtina, Republika e Kosoves
Registration No: 80452632
April 14, 2017

Statement of Financial Position

(Amounts in EUR thousand)

	Note	As at 31 December 2016	As at 31 December 2015
Assets			
Cash on hand and at banks	6	16,113	15,397
Balances with the Central Bank of Kosovo	7	36,867	17,572
Loans to customers	8	137,928	122,077
Investments in securities	9	24,770	21,610
Property and equipment	10	6,089	6,226
Intangible assets	11	394	271
Prepaid income tax		-	74
Other assets	12	843	692
Total assets		**223,004**	**183,919**
Liabilities			
Due to customers	13	197,708	163,751
Due to banks	14	2,196	1,393
Subordinated debt	15	1,050	1,050
Current tax liability		172	312
Other liabilities	16	439	535
Total liabilities		**201,565**	**167,041**
Equity and reserves			
Share capital	17	16,777	14,778
General risk reserve	17	102	102
Retained earnings/(Accumulated losses)		4,560	1,998
Total equity and reserves		**21,439**	**16,878**
Total liabilities, equity and reserves		**223,004**	**183,919**

The Statement of Financial Position is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 5 to 42.

These financial statements have been approved by the Board of Directors of the Bank and signed on April 14, 2017, on its behalf by:

Ms. Merita Gjyshinca Peja
General Manager

Ms. Syzane Kaçaniku Kusari
Finance Manager

Statement of Profit or Loss and Other Comprehensive Income

(Amounts in EUR thousand)

	Note	For the year ended December 31, 2016	For the year ended December 31, 2015
Interest income	18	13,450	13,571
Interest expense	18	(2,273)	(2,896)
Net interest income		**11,177**	**10,675**
Fee and commission income	19	2,356	1,950
Fee and commission expense	19	(683)	(454)
Net fee and commission income		**1,673**	**1,496**
Other operating income	20	31	53
Net foreign exchange losses		23	(68)
Revenue		**12,904**	**12,156**
Other operating expenses	21	(7,891)	(7,460)
Net impairment losses on loans	8	(2)	(659)
Total operating expenses		**(7,893)**	**(8,119)**
Profit before tax		5,011	4,037
Income tax	22	(451)	(327)
Net profit for the year		**4,560**	**3,710**
Other comprehensive income		**-**	**-**
Total comprehensive income for the year		**4,560**	**3,710**

The Statement of Profit or Loss and Other Comprehensive Income is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 5 to 42.

Statement of Changes in Equity

(Amounts in EUR thousand)

	Share capital	General risk reserve	Retained earnings/ (Accumulated losses)	Total equity and reserves
At 1 January 2015	**14,778**	**102**	**(1,712)**	**13,168**
Transactions with owners	-	-	-	-
Total comprehensive income for the year				
Profit for the year	-	-	3,710	3,710
Other comprehensive income for the year	-	-	-	-
Total comprehensive income for the year	**-**	**-**	**3,710**	**3,710**
At 31 December 2015	**14,778**	**102**	**1,998**	**16,878**
At 1 January 2016	**14,778**	**102**	**1,998**	**16,878**
Transactions with owners recorded directly in equity				
Contributions by and distributions to owners	1,998	-	(1,998)	-
Total transactions with owners recorded in equity	1,998	-	(1,998)	-
Transactions with owners				
Total comprehensive income for the year	-	-	-	-
Profit for the year	-	-	4,560	4,560
Other comprehensive income for the year	-	-	-	-
Total comprehensive income for the year	**-**	**-**	**4,560**	**4,560**
At 31 December 2016	**16,777**	**102**	**4,560**	**21,439**

The Statement of Changes in Equity is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 5 to 42.

Statement of Cash Flows

(Amounts in EUR thousand)

	Note	For the year ended December 31, 2016	For the year ended December 31, 2015
Operating activities			
Profit before taxation	22	5,011	4,037
Adjustment for:			
Amortization and depreciation	10,11	858	845
Net impairment loss on loans to customers	8	2	659
Loss on disposal of property and equipment		-	2
Interest income	18	(13,450)	(13,571)
Interest expense	18	2,273	2,896
Loss before changes in operating assets and liabilities		**(5,306)**	**(5,132)**
Changes in operating assets and liabilities			
Statutory reserves	6	(1,301)	(2,592)
Loans to customers	8	(15,887)	(12,512)
Other assets	12	(151)	(23)
Due to customers	13	34,142	7,308
Due to banks	13	803	1,303
Other liabilities	16	(100)	85
		12,200	**(11,563)**
Interests paid		(2,458)	(3,618)
Interests received		13,608	13,613
Income tax paid		(519)	(89)
Net cash generated from/(used in) operating activities		**22,831**	**(1,657)**
Investment activities			
Purchase of property and equipment and intangible assets	10,11	(857)	(651)
Net redemptions / (purchase) of securities	9	(3,264)	6,548
Net cash (used in) / generated from investing activities		**(4,121)**	**5,897**
Net increase/(decrease) in cash and cash equivalents		**18,710**	**4,240**
Cash and cash equivalents, beginning of the year		19,462	15,222
Cash and cash equivalents, end of the year	**6**	**38,172**	**19,462**

The Statement of cash flows is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 5 to 42.

Notes to the financial statements for the year ended 31 December 2016

(Amounts in thousands of EUR, unless otherwise stated)

1. Introduction

Banka Ekonomike Sh.a ("the Bank") is a Shareholding Company incorporated in the Republic of Kosovo. The address of its registered Head Office is Mother Teresa Square, 10000 Prishtina, Republic of Kosovo.

In accordance with the Central Bank of Kosovo ("CBK") regulations, the Bank obtained a license for banking activities on 28 May 2001 and commenced operations on 5 June 2001. The Bank operates as a commercial and savings bank for all categories of customers within Kosovo, through its network of 7 main branches in Prishtina, Gjakova, Peja, Prizren, Ferizaj, Mitrovica and Gjilan.

2. Basis of preparation

(a) Statement of compliance

These financial statements are prepared in accordance with Article 53 of the Law No. 04/L-093, dated 11 May 2012, "Law on banks, microfinance institutions and non-bank financial institutions" (the "Banking Law"). These financial statements are prepared for regulatory purposes and reflect the accounting rules and regulations of the Central Bank of the Republic of Kosovo ("CBK Rules"). CBK Rules are based on the relevant legal decision defining the mandatory application of International Financial Reporting Standards ("IFRS") in Kosovo, but CBK rules also specifically require the application of certain accounting treatments which are not in accordance with the specific requirements of IFRS. Consequently, these financial statements should be read as being prepared in accordance with the accounting standards and regulations prevailing in Kosovo as disclosed in the significant accounting policies set out in Note 3 below.

(b) Basis of preparation

The financial statements have been prepared on the historical cost basis, except for available-for-sale financial assets which are measured at fair value.

(c) Functional and presentation currency

These financial statements are presented in EUR, which is the Bank's functional currency. All amounts have been rounded to the nearest thousands, except when otherwise indicated.

(d) Use of judgments and estimates

In preparing these financial statements, management has made judgements, estimates and assumptions that affect the application of the Bank's accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognised prospectively.

Information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are described in notes 4, 5 and 25.

3. Significant accounting policies

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

a) Interest

Interest income and expense are recognised in profit or loss using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or financial liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not future credit losses.

The calculation of the effective interest rate includes transaction costs and fees and points paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or financial liability.

3. Significant accounting policies (continued)

a) Interest (continued)

Interest income and expense presented in the statement of profit or loss and Other Comprehensive Income (OCI) include:

- interest on financial assets and financial liabilities measured at amortised cost calculated on an effective interest basis; and
- interest on available-for-sale investment securities calculated on an effective interest basis.

(b) Fees and commissions

Fees and commission income and expense that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Other fees and commission income, including account servicing fees, fund transfer fees, sales commission and placement fees are recognised as the related services are performed. When a loan commitment is not expected to result in the draw-down of a loan, the related loan commitment fees are recognised on a straight-line basis over the commitment period.

Other fees and commission expense relate mainly to transaction and service fees, which are expensed as the services are received.

(c) Lease payments

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

d) Tax expense

Tax expense comprises current and deferred tax. Current tax and deferred tax are recognised in profit or loss except to the extent that they relate to items recognised directly in equity or in other comprehensive income.

(i) Current tax

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

(ii) Deferred tax

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for temporary differences on the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting, nor taxable profit or loss.

The measurement of deferred tax reflects the tax consequences that would follow the manner in which the Bank expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, using tax rates enacted or substantively enacted at the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to taxes levied by the same tax authority. Additional taxes that arise from the distribution of dividends by the Bank are recognised at the same time as the liability to pay the related dividend is recognised.A deferred tax asset is recognised for unused tax losses, tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which it can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

3. Significant accounting policies (continued)

(d) Tax expense (continued)

(iii) Tax exposures

In determining the amount of current and deferred tax, the Bank takes into account the impact of uncertain tax positions and whether additional taxes and interest may be due. This assessment relies on estimates and assumptions and may involve a series of judgements about future events. New information may become available that causes the Bank to change its judgement regarding the adequacy of existing tax liabilities; such changes to tax liabilities will impact tax expense in the period that such a determination is made.

e) Foreign currency transactions

Transactions in foreign currencies are translated into the respective functional currency of the Bank at the spot exchange rates at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the spot rate exchange rate at that date.

The foreign currency gain or loss on monetary items is the difference between amortised costs in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the year.

Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined. Non-monetary items that are measured based on historical cost in a foreign currency are translated using the spot exchange rate at the date of the transaction. Foreign currency differences arising on retranslation are recognised in profit or loss.

f) Financial assets and financial liabilities

(i) Recognition

The Bank initially recognises loans and advances, held-to-maturity and available-for sale investments, deposits and subordinated debt on the date that they are originated. Regular way purchases and sales of financial assets are recognised on the trade date at which the Bank commits to purchase or sell the asset. All other financial assets and liabilities are recognised initially on the trade date, which is the date that the Bank becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value plus transaction costs that are directly attributable to its acquisition or issue.

(ii) Classification

Financial assets

The Bank classifies its financial assets into one of the following categories:

- loans and receivables; and
- held-to-maturity.
- available-for-sale

See notes 3 (j), (h) and (i).

Financial liabilities

The Bank classifies its financial liabilities as measured at amortised cost. See note 3.(k).

(iii) Derecognition

Financial assets

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the

3. Significant accounting policies (continued)

(f) Financial assets and financial liabilities (continued)

Bank neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognised as a separate asset or liability. On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset transferred), and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in other comprehensive income is recognised in profit or loss. The Bank derecognises a financial liability when its contractual obligations are discharged, cancelled or expire.

(iv) Offsetting

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Bank has a legal right to set off the amounts and it intends either to settle them on a net basis or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRS, or for gains and losses arising from a group of similar transactions such as in the Bank's trading activity.

(v) Amortised cost measurement

Financial assets or liabilities are subsequently measured at amortised cost which is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

(vi) Fair value measurement

'Fair value' is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

When available, the Bank measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. If there is no quoted price in an active market, then the Bank uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price – i.e. the fair value of the consideration given or received. If the Bank determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

If an asset or a liability measured at fair value has a bid price and an ask price, then the Bank measures assets and long positions at a bid price and liabilities and short positions at an ask price.

The fair value of a demand deposit is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.

The Bank recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

3. Significant accounting policies (continued)

(f) Financial assets and financial liabilities (continued)

(vii) Identification and measurement of impairment

Loans and advances to customers are reported net of impairment (or net of provisions for loan losses). At each reporting date the Bank assesses whether there is objective evidence that financial assets are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows of the asset.

In addition, provisions for loan losses include possible future losses estimated by the management in relation to existing loans, which may become uncollectible due to the economic conditions, credit quality, inherent risks in the loan portfolio and other relevant factors.

Objective evidence that financial assets are impaired can include default or delinquency by a borrower, restructuring of a loan or advance by the Bank on terms that the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers, or economic conditions that correlate with defaults in the Bank.

Provisions for loan losses are created pursuant to the Regulation "Credit Risk Management", which was approved by CBK on 26 April 2013. The regulation requires the Bank to classify exposures into five risk categories. The Bank considers evidence of impairment for loans and advances at both a specific asset and collective level.

For each risk category, the following minimum rates of specific provision are applied:

Category	Minimum provision rate
Substandard	20%
Doubtful	50%
Loss	100%

Provisions created for possible losses on loans classified as standard and watch are classified as general provisions. In accordance with the internal provisioning policies of the Bank, the rate that is applied for the standard and watch categories is 1.2% (2015: 1.2%).

Losses are recognised in profit or loss and reflected in an allowance account against loans and advances. The loans are written off after reasonable collection measures have been taken in accordance with the Bank's established policy. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

Impairment of available-for-sale financial assets

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available for - sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from other comprehensive income and recognised in the profit or loss. Impairment losses recognised in the profit or loss on equity instruments are not reversed through the profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the profit or loss.

(g) Cash and cash equivalents

Cash and cash equivalents include notes and coins on hand, unrestricted balances held with central banks and highly liquid financial assets with original maturities of three months or less from the acquisition date that are subject to an insignificant risk of changes in their fair value, and are used by the Bank in the management of its short-term commitments. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

3. Significant accounting policies (continued)

h) Investments held-to-maturity

Investment securities are initially measured at fair value plus incremental direct transaction costs, and subsequently accounted for depending on their classification as held to maturity.

Held-to-maturity investments are non-derivative assets with fixed or determinable payments and fixed maturity which are quoted on active markets, that the Bank has the positive intent and ability to hold to maturity, and which are not designated as at fair value through profit or loss or as available for sale.

Held-to-maturity investments are carried at amortised cost using the effective interest method, less any impairment losses (see Note 3.(f).(vii)). A sale or reclassification of a more than insignificant amount of held-to-maturity investments would result in the reclassification of all held-to-maturity investments as available for sale, and would prevent the Bank from classifying investment securities as held to maturity for the current and the following two financial years. However, sales and reclassifications in any of the following circumstances would not trigger a reclassification:

- sales or reclassifications that are so close to maturity that changes in the market rate of interest would not have a significant effect on the financial asset's fair value;
- sales or reclassifications after the Bank has collected substantially all of the asset's original principal; and
- sales or reclassifications attributable to non-recurring isolated events beyond the Bank's control that could not have been reasonably anticipated.

i) Available for sale investments

Available-for-sale investments are non-derivative investments that are designated as available-for-sale or are not classified as another category of financial assets. Available-for-sale investments comprise equity securities and debt securities. Unquoted equity securities whose fair value cannot be measured reliably are carried at cost. All other available-for-sale investments are measured at fair value after initial recognition.

Interest income is recognised in profit or loss using the effective interest method. Dividend income is recognised in profit or loss when the Bank becomes entitled to the dividend. Foreign exchange gains or losses on available-for-sale debt security investments are recognised in profit or loss. Impairment losses are recognised in profit or loss (see (f)(vii)).

Other fair value changes, other than impairment losses are recognised in other comprehensive income and presented in the fair value reserve within equity. When the investment is sold, the gain or loss accumulated in equity is reclassified to profit or loss.

j) Loans and receivables

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Bank does not intend to sell immediately or in the near term. Loans and advances to banks and to customers are classified as loans and receivables.

Loans and advances are initially measured at fair value plus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method.

k) Deposits and subordinated debt

Deposits and subordinated debts are the Bank's main sources of debt funding.

Deposits and subordinated debts are initially measured at fair value minus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method.

i) Property and equipment

(i) Recognition and measurement

Items of property and equipment are measured at cost less accumulated depreciation and any accumulated impairment losses.

3. Significant accounting policies (continued)

i) Property and equipment (continued)

(i) Recognition and measurement (continued)

Cost includes expenditure that is directly attributable to the acquisition of the asset. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

When parts of an item of property or equipment have different useful lives, they are accounted for as separate items (major components) of property and equipment.

Any gain or loss on disposal of an item of property and equipment (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognised within other income in profit or loss.

(ii) Subsequent costs

Subsequent expenditure is capitalised only when it is probable that the future economic benefits of the expenditure will flow to the Bank. Ongoing repairs and maintenance are expensed as incurred.

(iii) Depreciation

Items of property and equipment are depreciated from the date they are available for use. Depreciation is calculated to write off the cost of items of property and equipment less their estimated residual values over their estimated useful lives. Depreciation is recognised in profit or loss.

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property and equipment. The estimated useful lives for the current and comparative periods are as follows:

	Useful life 2016	Useful life 2015
Buildings	40 years	40 years
Computers and related equipment	5 years	5 years
Motor vehicles	5 years	5 years
Furniture, fixtures and equipment	5 years	5 years

Leasehold improvements are depreciated using the straight-line basis over the shorter of the lease term and their useful lives. Depreciation methods, useful lives and residual values are reassessed at each reporting date and adjusted if appropriate.

m) Intangible assets

Software acquired by the Bank is measured at cost less accumulated amortisation and any accumulated impairment losses. Subsequent expenditure on software assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Amortisation is recognised in profit or loss over the estimated useful life of the asset, from the date that it is available for use.

Software is amortised using the straight-line method over the estimated useful life of five years. Amortisation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

n) Impairment of non-financial assets

The carrying amounts of the Bank's non-financial assets, other than deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. An impairment loss is recognised if the carrying amount of an asset exceeds its recoverable amount.

3. Significant accounting policies (continued)

n) Impairment of non-financial assets (continued)

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

Impairment losses are recognised in profit or loss. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

o) Provisions

A provision is recognised if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. The unwinding of the discount is recognised as finance cost.

p) Employee benefits

(i) Defined contribution plans

Obligations for contributions to defined contribution pension plans are recognised as an expense in profit or loss when they are due. The Bank makes only compulsory social security contributions that provide pension benefits for employees upon retirement. The local authorities are responsible for providing the legally set minimum threshold for pensions in Kosovo under a defined contribution pension plan.

(ii) Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A provision is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Bank has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

q) Financial guarantees and loan commitments

Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. Loan commitments are firm commitments to provide credit under pre-specified terms and conditions. Such financial commitments are recorded in the statement of financial position if and when they become payable.

r) Dividends

Dividends on ordinary shares are recognised in equity in the period in which they are approved by the Bank's shareholders. Dividends for the year that are declared after the reporting date are disclosed as events after the end of the reporting period.

3. Significant accounting policies (continued)

s) Adoption of new and revised standards

(i) Standards and Interpretations effective in the current period

The following standards, amendments to the existing standards and interpretations issued by the International Accounting Standards Board (IASB) are effective for the current period:

- **IFRS 14 "Regulatory Deferral Accounts"** (effective for annual periods beginning on or after 1 January 2016),
- **Amendments to IFRS 10 "Consolidated Financial Statements", IFRS 12 "Disclosure of Interests in Other Entities" and IAS 28 "Investments in Associates and Joint Ventures"** - Investment Entities: Applying the Consolidation Exception (effective for annual periods beginning on or after 1 January 2016),
- **Amendments to IFRS 11 "Joint Arrangements" –** Accounting for Acquisitions of Interests in Joint Operations (effective for annual periods beginning on or after 1 January 2016),
- **Amendments to IAS 1 "Presentation of Financial Statements"** - Disclosure Initiative (effective for annual periods beginning on or after 1 January 2016),
- **Amendments to IAS 16 "Property, Plant and Equipment" and IAS 38 "Intangible Assets"** - Clarification of Acceptable Methods of Depreciation and Amortisation (effective for annual periods beginning on or after 1 January 2016),
- **Amendments to IAS 16 "Property, Plant and Equipment" and IAS 41 "Agriculture"** - Bearer Plants (effective for annual periods beginning on or after 1 January 2016),
- **Amendments to IAS 27 "Separate Financial Statements"** - Equity Method in Separate Financial Statements (effective for annual periods beginning on or after 1 January 2016),
- **Amendments to various standards "Improvements to IFRSs (cycle 2012-2014)"** resulting from the annual improvement project of IFRS (IFRS 5, IFRS 7, IAS 19 and IAS 34) primarily with a view to removing inconsistencies and clarifying wording (amendments are to be applied for annual periods beginning on or after 1 January 2016).

The adoption of these amendments to the existing standards and interpretations has not led to any changes in the Bank's accounting policies.

(ii) Standards and interpretations in issue not yet effective

At the date of authorisation of these financial statements the following standards, amendments to existing standards and interpretations were in issue, but not yet effective:

- **IFRS 9 "Financial Instruments"** (effective for annual periods beginning on or after 1 January 2018),
- **IFRS 15 "Revenue from Contracts with Customers"** and further amendments (effective for annual periods beginning on or after 1 January 2018),
- **IFRS 16 "Leases"** (effective for annual periods beginning on or after 1 January 2019),
- **Amendments to IFRS 2 "Share-based Payment" -** Classification and Measurement of Share-based Payment Transactions (effective for annual periods beginning on or after 1 January 2018),
- **Amendments to IFRS 4 "Insurance Contracts"** - Applying IFRS 9 "Financial Instruments" with IFRS 4 "Insurance Contracts" (effective for annual periods beginning on or after 1 January 2018 or when IFRS 9 "Financial Instruments" is applied first time),
- **Amendments to IFRS 10 "Consolidated Financial Statements" and IAS 28 "Investments in Associates and Joint Ventures"** - Sale or Contribution of Assets between an Investor and its Associate or Joint Venture and further amendments (effective date deferred indefinitely until the research project on the equity method has been concluded),
- **Amendments to IAS 7 "Statement of Cash Flows"** - Disclosure Initiative (effective for annual periods beginning on or after 1 January 2017),
- **Amendments to IAS 12 "Income Taxes"** - Recognition of Deferred Tax Assets for Unrealised Losses (effective for annual periods beginning on or after 1 January 2017),
- **Amendments to IAS 40 "Investment Property"** - Transfers of Investment Property (effective for annual periods beginning on or after 1 January 2018),

The Bank has elected not to adopt these standards, revisions and interpretations in advance of their effective dates. The

Bank anticipates that the adoption of these standards, revisions and interpretations will have no material impact on the financial statements of the Company in the period of initial application.

3. Significant accounting policies (continued)

s) Adoption of new and revised standards (continued)

ii) Standards and interpretations in issue not yet effective (continued)

- **Amendments to various standards "Improvements to IFRSs (cycle 2014-2016)"** resulting from the annual improvement project of IFRS (IFRS 1, IFRS 12 and IAS 28) primarily with a view to removing inconsistencies and clarifying wording (amendments to IFRS 12 are to be applied for annual periods beginning on or after 1 January 2017 and amendments to IFRS 1 and IAS 28 are to be applied for annual periods beginning on or after 1 January 2018),
- **IFRIC 22 "Foreign Currency Transactions and Advance Consideration"** (effective for annual periods beginning on or after 1 January 2018).

The Company has elected not to adopt these standards, revisions and interpretations in advance of their effective dates. The Company anticipates that the adoption of these standards, revisions and interpretations will have no material impact on the financial statements of the Company in the period of initial application.

4. Use of estimates and judgments

Management discusses with the Audit Committee and the Board of Directors the development, selection and disclosure of the Bank's critical accounting policies and their application, and assumptions made relating to major estimation uncertainties. Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment within the next financial year and about critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the separate financial statements is disclosed below.
These disclosures supplement the commentary on financial risk management (see Note 26).

a) Impairment

Assets accounted for at amortised cost are evaluated for impairment on a basis described in Note 3.(f)(vii).

The Bank reviews its loan portfolios to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the profit or loss, the Bank makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the Bank.

Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows.

The Bank determines that available-for-sale investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgment. In making this judgment, the Bank evaluates among other factors, the normal volatility in share price. In addition, impairment may be appropriate when there is evidence of deterioration in the financial health of the investee, industry and sector performance, changes in technology, and operational and financing cash flows.

b) Determining fair values
The determination of fair value for financial assets and financial liabilities for which there is no observable market price requires the use of valuation techniques as described in Note 3.(f)(vi). For financial instruments that trade infrequently and have little price transparency, fair value is less objective, and requires varying degrees of judgement depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument.

4. Use of estimates and judgments (continued)

(b) Determining fair values

The Bank measures fair values using the following hierarchy of methods:

- Level 1: Quoted market price in an active market for an identical instrument.
- Level 2: Valuation techniques based on observable inputs. This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.
- Level 3: Valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs could have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments. The estimation of the fair value is disclosed in note 5.

5. Disclosure and estimation of fair value

Fair value estimates are based on existing financial instruments on the Bank's financial position statement without attempting to estimate the value of anticipated future business and the value of assets and liabilities not considered financial instruments.

Financial instruments measured at fair value – fair value hierarchy

The following table analyses financial instruments measured at fair value at the reporting date, by the level in the fair value hierarchy into which the fair value measurement is categorized. The amounts are based on the values recognized in the statement of financial position. Fair value of investment securities is based on market prices or broker/dealer price quotations. Where this information is not available, fair value has been estimated using a discounted cash flow model based on a current yield curve appropriate for the remaining term to maturity.

Available for sale financial assets	Carrying amount	Fair Value Level 1	Fair Value Level 2	Fair Value Level 3
31 December 2016	21,922	-	21,922	-
31 December 2015	987	-	987	-
Total Assets	22,909	-	22,909	-

Financial instruments not measured at fair value – fair value hierarchy

The following table sets out the fair values of financial instruments not measured at fair value and analyses them by the level in the fair value hierarchy into which each fair value measurement is categorized.

	Carrying value		Fair value	
			Level 2	Level 2
Assets	**2016**	**2015**	**2016**	**2015**
Cash on hand and at banks	16,113	15,397	16,113	15,397
Balance with CBK	36,867	17,572	36,867	17,572
Loans to customers	137,928	122,077	142,135	125,420
Investments in securities	2,848	20,623	2,848	20,616
Liabilities				
Due to customers	197,708	163,751	199,291	164,729
Due to banks	2,196	1,393	2,196	1,393
Subordinated Debt	1,050	1,050	1,027	995

Fair values for financial assets and liabilities above have been determined using Level 2 input described above.

5. Disclosure and estimation of fair value (continued)

Financial instruments not measured at fair value – fair value hierarchy (continued)

Fair value estimates are based on existing financial instruments on the Bank's statement of financial position without attempting to estimate the value of anticipated future business and the value of assets and liabilities not considered financial instruments.

Balances with banks

Due from other banks include inter-bank placements and accounts. As balances with banks are short term, their fair value is considered to equate to their carrying amount.

Treasury Bills available-for-sale

Treasury Bills available-for-sale include treasury bills issued by the Government of Kosovo that are neither held for trading, nor held to maturity

Treasury Bills held to maturity

Treasury Bills held-to-maturity include treasury bills issued the Government of Kosovo which are bought with the intention to hold till maturity. As Treasury Bills are short term, their fair value is considered not significantly different from carrying amount.

Bonds held-to-maturity

Bonds held-to-maturity include treasury bonds issued by the Government of Kosovo which are bought with the intention to hold till maturity. Quoted prices in active markets were not available for these securities. However, there was sufficient information available to measure the fair values of these securities based on observable market inputs and using a discounted cash flow model based on a current yield curve appropriate for the remaining term to maturity.

Bonds available for sale

Bonds available-for-sale include treasury bonds issued by the Government of Kosovo that are neither held for trading, nor held to maturity. Fair value of these investment securities is based on market prices or broker/dealer price quotations.

Loans and advances to customers

Where available, the fair value of loans and advances is based on observable market transactions. Where observable market transactions are not available, fair value is estimated using valuation models, such as discounted cash flow techniques. Input into the valuation techniques includes expected lifetime credit losses, interest rates and prepayment rates. To improve the accuracy of the valuation estimate for retail and smaller commercial loans, homogeneous loans are grouped into portfolios with similar characteristics. There are no cases of loans that are valued based on observable inputs.

Due to customers and subordinated debt

The fair value of subordinated debt and balances due to customers is estimated using discounted cash flow techniques, applying the rates that are offered for deposits and subordinated debt of similar maturities and terms. The fair value of deposits payable on demand is the amount payable at the reporting date. The deposits have an estimated fair value which approximates the carrying amount due either to their short term nature or to underlying interest rates which approximate market rates. The majority of deposits is subject to re-pricing within a year.

6. Cash on hand and at banks

	As at December 31, 2016	As at December 31, 2015
Cash on hand	8,191	7,908
Current accounts with banks	7,922	7,489
	16,113	**15,397**

Cash and cash equivalents comprise the following:

	As at December 31, 2016	As at December 31, 2015
Cash on hand and at banks	16,113	15,397
Balances with the CBK (Note 7)	36,867	17,572
Statutory reserves	(14,808)	(13,507)
	38,172	**19,462**

In accordance with the CBK requirements relating to the deposits reserve for liquidity purposes, the Bank should maintain a minimum of 10% of customer deposits with maturities up to one year, as statutory reserves. The statutory reserves represent highly liquid instruments, including cash on hand, accounts at the CBK or at other banks in Kosovo, and the amounts held at the CBK should not be less than half of the total statutory reserves.

The assets with which the Bank may satisfy its liquidity requirement are deposits in EUR with the CBK and 50% of the EUR equivalent of cash denominated in readily convertible currencies. Deposits with the CBK must not be less than 5% of the applicable deposit base.

7. Balances with the Central Bank of Kosovo

	As at December 31, 2016	As at December 31, 2015
Statutory reserves with the CBK	14,808	13,507
Current accounts	22,059	4,065
	36,867	**17,572**

8. Loans to customers

	As at December 31, 2016	As at December 31, 2015
Loans	123,516	108,202
Overdraft facilities	24,361	23,760
	147,877	**131,962**
Accrued interest	804	744
Deferred disbursement fees	(725)	(627)
	147,956	**132,079**
Allowance for impairment	(10,028)	(10,002)
Loans to customers	**137,928**	**122,077**

Loans are presented at nominal value, accrued interest are based on nominal interest rates, while deferred disbursement fees are incremental fees which are part of effective interest rate.

Maturities of long term loans are in the range of 1 to 20 years (2015: 1 to 20 years). In 2016, the interest rates on loans to customers ranged from 1.5% to 24% p.a (2015: 1.5% to 24% p.a). The Bank has granted few loans with interest rates at the minimum limit shown above, which are lower than the rates that are generally offered by the Bank, and are covered by cash collaterals.

The movements in the allowance for impairment are as follows:

	2016	2015
Allowance for impairment at 1 January	10,002	10,684
Loans written off	(916)	(2,063)
Recoveries of loans previously written off	944	722
Charge for the year	(2)	659
Allowance for impairment at 31 December	**10,028**	**10,002**

8. Loans to customers (continued)

Category	At amortized cost	Allowance for impairment	Net balance	At amortized cost	Allowance for impairment	Net balance
Standard	135,822	1,753	**134,069**	118,372	1,527	**116,845**
Watch	2,001	24	**1,977**	3,505	270	**3,235**
Sub-standard	2,078	700	**1,378**	1,318	265	**1,053**
Doubtful	1,029	525	**504**	1,849	928	**921**
Loss	7,026	7,026	**-**	7,035	7,012	**23**
Total	**147,956**	**10,028**	**137,928**	**132,079**	**10,002**	**122,077**

9. Investments in securities

	As at December 31, 2016	As at December 31, 2015
Held-to-maturity		
Government Treasury bills	-	18,375
Government Bonds	2,812	2,044
Accrued Interest	36	204
Total securities held-to-maturity	**2,848**	**20,623**
Available-for-sale		
Government Treasury bills	11,638	986
Government Bonds	10,219	-
Accrued Interest	65	1
Total securities available-for-sale	**21,922**	**987**
Total Investments in Securities	**24,770**	**21,610**

10. Property and equipment

	Buildings	Leasehold improvements	Furniture, fixtures and equip-ment	Computers and related equipment	Motor vehicles	Total
Cost						
At 1 January 2015	**5,634**	**661**	**3,272**	**1,214**	**528**	**11,309**
Additions	-	54	165	333	28	580
Disposals	-	(18)	(45)	(30)	-	(93)
At 31 December 2015	**5,634**	**697**	**3,392**	**1,517**	**556**	**11,796**
Additions	-	139	254	156	62	611
Disposals	-	(29)	(367)	(195)	(76)	(667)
At 31 December 2016	**5,634**	**807**	**3,279**	**1,478**	**542**	**11,740**
Accumulated depre-ciation						
At 1 January 2015	**705**	**522**	**2,451**	**855**	**388**	**4,921**
Charge for the year	141	49	366	130	54	740
Disposals	-	(18)	(43)	(30)	-	(91)
At 31 December 2015	**846**	**553**	**2,774**	**955**	**442**	**5,570**
Charge for the year	141	54	327	164	51	737
Disposals	-	(29)	(361)	(190)	(76)	(656)
At 31 December 2016	**987**	**578**	**2,740**	**929**	**417**	**5,651**
Carrying amount						
At 31 December 2016	**4,647**	**229**	**539**	**549**	**125**	**6,089**
At 31 December 2015	**4,788**	**144**	**618**	**562**	**114**	**6,226**

As at 31 December 2016 and 2015 the Bank does not have any property or equipment pledged as collateral.

The carrying amount of tangible and intangible assets of the Bank at 31 December 2016 was EUR 6,484 thousand representing 31.55% of Tier 1 capital (2015: EUR 6,497 thousand representing 39.59% of Tier 1 capital). The maximum regulatory limit is 50% of Tier 1 capital. No breach of such ratio was reported in 2015, nor in 2016.

11. Intangible assets

	Software
Cost	
At 1 January 2015	**760**
Additions during the year	71
Disposals	-
At 31 December 2015	**831**
Additions for the year	246
Disposals	(2)
At 31 December 2016	**1,075**
Accumulated amortization	
At 1 January 2015	455
Charge for the year	105
At 31 December 2015	560
Charge for the year	121
At 31 December 2016	681
Carrying amount	
At 1 January 2015	305
At 31 December 2015	271
At 31 December 2016	394

12. Other assets

	As at December 31, 2016	As at December 31, 2015
Prepayments	354	329
Other	489	363
Total	**843**	**692**

13. Due to Customers

	As at December 31, 2016	As at December 31, 2015
Time Deposits	99,631	86,189
Current accounts	72,123	54,405
Savings accounts	12,717	12,110
Flexi deposits	8,324	7,958
Blocked accounts	3,482	1,473
Accrued interest	1,431	1,616
Total	**197,708**	**163,751**

Current accounts are non-interest bearing. The average effective interest rates for time deposits during 2016 and 2015 were as follows:

Year	1 month	3 months	6 months	1 year	18 months	2 -5 years
2016	0.071%	1.320%	1.788%	1.835%	3.064%	2.307%
2015	0.124%	2.047%	2.061%	2.601%	2.325%	3.73%

14. Due to banks

Balances due to banks amounting EUR 2,196 thousand (2015: EUR 1,393 thousand) represent current accounts from local banks. The current accounts are non-interest bearing

15. Subordinated debt

	2016	2015
Subordinated Debt	1,000	1,000
Accrued Interest	50	50
Total	**1,050**	**1,050**

During 2014, the Bank signed an agreement for subordinated debt with Mabetex Properties Sha. The subordinated debt of EUR 1,000 thousand bears an annual interest rate of 7.5% and matures on 30 April 2020.

16. Other liabilities

	As at December 31, 2016	As at December 31, 2015
Accrued expenses	238	290
Other taxes payable	67	91
Pension and social assistance charges	22	21
Provisions for litigations	50	80
Other deferred income	41	36
Provision for losses from guarantees	21	17
Total	**439**	**535**

The movement in the provision for losses from guarantees issued by the Bank is as follows:

	2016	2015
Provisions as at 1 January	17	34
Creation/(release) for the year	4	(17)
Provisions as at 31 December	21	17

17. Share Capital and reserves

The authorised and paid up share capital of the Bank comprises 65,534 ordinary shares (2015: 57,729) with par value of EUR 256 each (2015: 256). The shareholding structure of the Bank is as follows:

	As at December 31, 2016		As at December 31, 2015	
	%	Amount	%	Amount
Behgjet Pacolli	35	5,843	35	5,147
Afrim Pacolli	33	5,528	33	4,870
Selim Pacolli	14	2,319	14	2,043
Xhabir Kajtazi	12	1,986	12	1,749
Ismet Gjoshi	3	563	3	496
Hasan Hajdari	1	169	1	149
Zyhra Hajdari	1	162	1	143
Others with less than 1%	1	207	1	181
	100	**16,777**	**100**	**14,778**

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share. All shares rank equally with regard to the Bank's residual assets.

In accordance with Law no. 04/L-093 on "Banks, Microfinance Institutions and Non-Bank Financial Institutions", the minimum paid-in capital for domestic banks operating in Kosovo is EUR 7 million.

The general risk reserves of EUR 102 thousand (2015: EUR 102 thousand) were created through appropriation of retained earnings with the purpose of covering general risks faced by the Bank during the normal course of business.

18. Net Interest income

	Year ended December 31, 2016	Year ended December 31, 2015
Interest income		
Loans to customers	13,041	13,182
Deposits and balances with banks	3	-
Investments in securities	406	389
Total Interest income	13,450	13,571
Interest expense		
Due to customers	(2,198)	(2,821)
Subordinated debt	(75)	(75)
Total Interest expense	(2,273)	(2,896)
Net interest income	11,177	10,675

The Bank does not recognise interest income for nonperforming loans with more than 90 days in arrears.

19. Net fee and commission income

	Year ended December 31, 2016	Year ended December 31, 2015
Banking services	2,295	1,839
Guarantees	61	111
Fee and commission income	2,356	1,950
Swift expenses	(678)	(444)
License and other regulatory fees	(5)	(10)
Fee and commission expenses	(683)	(454)
Net fee and commission income	1,673	1,496

20. Other operating income

	Year ended December 31, 2016	Year ended December 31, 2015
Capital gains	9	-
Release of provisions for losses from guarantees (see note 16)	-	17
Other income	22	36
Total	31	53

21. Other operating expenses

	Year ended December 31, 2016	Year ended December 31, 2015
Personnel (see below)	2,807	2,735
Security	994	921
Depreciation	737	740
Rent	688	698
Advertising and marketing	349	295
Repair and maintenance	293	251
Deposit insurance fees	279	173
Utilities and fuel	240	242
Provisions for litigations	182	80
Professional charges and legal fees	141	231
IT services	135	129
Communication	123	116
Amortization	121	105
Office materials	45	35
Printing	10	8
Travel	6	9
Other assets written off	-	71
Other	741	621
Total	**7,891**	**7,460**

The number of employees as at 31 December 2016 is 335 (2015: 323).

	Year ended December 31, 2016	Year ended December 31, 2015
Wages and salaries	2,615	2,537
Pension contributions	131	128
Other compensations	61	70
Total	**2,807**	**2,735**

22. Income tax

Income tax in Kosovo is assessed at the rate of 10% (2015: 10%) of taxable income.

	Year ended December 31, 2016	Year ended December 31, 2015
Current tax charge	451	327
Total	**451**	**327**

The following represents a reconciliation of the accounting result to the income tax:

	Year ended December 31, 2016	Year ended December 31, 2015
Profit before income tax	5,011	4,037
Tax at the rate of 10%	501	404
Adjusted for:		
Non-deductible expenses	31	20
Additional tax deductible interest expenses	(40)	(58)
Exempt Income	**(41)**	**(39)**
Income tax expense for the year	**451**	**327**

23. Commitments and Contingencies

The Bank issues guarantees for its customers. These instruments bear a credit risk similar to that of loans granted to customers. Based on management's estimate, no material losses related to guarantees outstanding at 31 December 2016 will be incurred.

Guarantees	Year ended December 31, 2016	Year ended December 31, 2015
Secured by cash deposits	615	712
Secured by other collateral	1,388	1,373
	2,003	2,085
Credit Commitments		
Approved but not disbursed loans	3,364	786
Unused portion of credit lines	8,898	8,577
Unused credit card facilities	12,262	9,363

Other collaterals pledged for guarantees, include mainly pledge and real estate properties.

Commitments represent the undrawn balances of loans, overdraft and card limits granted to the customers.

Operating Lease commitments

The Bank has entered into non-cancelable lease commitments as follows:

	Year ended December 31, 2016	Year ended December 31, 2015
Within one year	339	111
	339	111

23. Commitments and Contingencies (continued)

Banks significant lease agreements include the rent commitment in the main branches located in the cities of Prishtina, Gjakova, Peja, Prizren, Mitrovica, Gjilan, Ferizaj and Headhquater, excluding the offsite branches in this location. Contingent rent payables for this significant rents is determined based on the non-cancellable rent commitments according to the contract. The Bank has ensured that the rental contracts have protective clauses, at least 60 days for cases of unexpected termination of leases. No restrictions are imposed from the rent agreements that would have an impact on the rent commitment.

A further disclosure with regard to the rent agreements as at December 31, 2016 and 2015 is given below:

31 December 2016

Branch	Operat-ing lease amount	Base for tax on rent	Tax on rent	Minimum lease payments	Sublease payments	Contingent rents
Branch of Prishtina	204	199	18	204	33 33	36
Banch of Gjakova	57	108	10	58	-	8
Branch of Peja	86	81	7	86	3 4	65
Branch of Prizren	42	42	4	42	-	38
Branch of Mitrovica	54	54	5	54	6 6	12
Branch of Gjilan	72	69	6	72	-	70
Branch of Ferizaj	77	75	7	77	21 21 21	62
Headquarters	95	81	7	95	-	48
Total	**687**	**709**	**64**	**688**	**148**	**339**

31 December 2015

Branch	Operat-ing lease amount	Base for tax on rent	Tax on rent	Minimum lease payments	Sublease payments	Contingent rents
Branch of Prishtina	212	185	17	212	33 33	50
Banch of Gjakova	88	87	8	88	-	13
Branch of Peja	95	90	8	95	1 2	4
Branch of Prizren	46	46	4	46	-	8
Branch of Mitrovica	54	54	5	54	6 6	6
Branch of Gjilan	72	69	6	72	-	12
Branch of Ferizaj	77	76	7	77	- - -	14
Headquarters	55	48	4	55		4
Total	**699**	**655**	**59**	**699**	**81**	**111**

Litigations

As at 31 December 2016, there are certain legal proceedings raised against the Bank. The Bank has recognized provisions from potential losses amounting EUR 50 thousand during 2016, regarding legal proceedings at the reporting date. Various legal actions and claims may be asserted in the future against the Bank from litigations and claims incident to the ordinary course of business. Related risks have been analyzed by management as to likelihood of occurrence. Although the outcome of these matters cannot always be ascertained with precision, management believes that no additional material liabilities are likely to result.

24. Related party transactions

In accordance with IAS 24 "Related Party Disclosures", a related party is any party that has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions.

Related party transactions were made on terms equivalent to those that prevail in arm's length transactions.

In the course of conducting its banking business, the Bank entered into various business transactions with related parties and the balances with the shareholders and affiliated individuals and entities at 31 December 2016 and 2015 are as follows:

	Board of Directors		Key management		Major shareholders and other parties related to them		Total	
	2016	2015	2016	2015	2016	2015	2016	2015
Loans to customers								
Loans to customers, gross	9	15	153	71	3,469	3,218	3,631	3,304
Allowance for impairment	-	-	(2)	(1)	(4)	(1)	(6)	(2)
Loans to customers, net	**9**	**15**	**151**	**70**	**3,465**	**3,217**	**3,625**	**3,302**
Cash collateral	(9)	-	(148)	-	(3,431)	(3,154)	(3,588)	(3,154)
Net exposure	**-**	**15**	**3**	**70**	**34**	**63**	**37**	**148**
Guarantees	-	-	-	-	455	662	455	662
Cash collateral	-	-	-	-	(455)	(611)	(455)	(611)
Net exposure	-	-	-	-	-	51	-	51
Due to customers	16	2	227	43	16,808	17,497	17,051	17,542
Subordinated debt	-	-	-	-	1,050	1,050	1,050	1,050

The total estimated value of real estate collateral obtained from related parties at 31 December 2016 was EUR 7,500 thousand. Such value as at December 31, 2015 amounted to EUR 7,277 thousand.

The unused credit commitments with related parties at 31 December 2016, are EUR 220 thousand (2015: EUR 708 thousand).

24. Related party transactions (continued)

Due to related parties represent 8.6% (2015: 10.7%) of total balances due to customers. Transactions with related parties during 2016 and 2015 are as follows:

	Board of Directors		Key management		Major shareholders and other parties related to them		Total	
	2016	2015	2016	2015	2016	2015	2016	2015
Interest income	1	1	6	5	156	133	163	139
Fee and commission income	-	-	-	-	22	26	22	26
Interest expense	-	-	-	3	379	428	379	431
	1	**1**	**6**	**8**	**557**	**587**	**564**	**596**

Total remuneration to the Bank's key management is as follows:

	2016	2015
Short-term employee benefits for Board of Directors	54	62
Short-term employee benefits for key management	207	209
	261	**271**

25. Financial risk management

(a) Introduction and overview

The Bank has exposure to the following risks from its use of financial instruments:

- **market risk**
- **credit risk**
- **liquidity risk**

This note presents information about the Bank's exposure to each of the above risks, the Bank's objectives, policies and processes for measuring and managing risk, and the Bank's management of capital.

The Bank has the following categories of financial instruments:

- financial assets at fair value through profit or loss, showing separately (i) those designated as such upon initial recognition and (ii) those classified as held for trading in accordance with IAS 39;
- held-to-maturity investments;
- loans and receivables;
- available-for-sale financial assets;
- financial liabilities at fair value through profit or loss, showing separately (i) those designated as such upon initial recognition

and (ii) those classified as held for trading in accordance with IAS 39; and
- financial liabilities measured at amortised cost.

Risk management framework

The Board of Directors ("the Board") has overall responsibility for the establishment and oversight of the Bank's risk management framework. The Board has established the Asset and Liability Committee ("ALCO"), Liquidity Committee Credit Committee, Audit Committee, and Risk Committee, which are responsible for developing and monitoring the Bank's risk management policies in their specified areas. All Board committees have both executive and non-executive members and report regularly to the Board of Directors on their activities.

(a) Introduction and overview

The Bank's risk management policies are established to identify and analyse the risks faced by the Bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered.

The Bank aims to develop a constructive control environment, in which all employees understand their roles and obligations.

The Bank's Audit Committee is responsible for monitoring compliance with the Bank's risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Bank. The Bank's Audit Committee is assisted by the Internal Audit Department. Internal Audit undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee.

The Bank operates in the condition of a dynamically developing global financial and economic crisis. Its further extension might result in negative implications on the financial position of the Bank. The management of the Bank performs daily monitoring over all positions of assets and liabilities, income and expenses, as well as the development of the international financial markets. Based on this, the management analyses profitability, liquidity and the cost of funds and implements adequate measures in respect to credit, market (primarily interest rate) and liquidity risk, thus limiting the possible negative effects from the global financial and economic crisis. In this way the Bank responds to the challenges of the market environment, maintaining an adequate capital and liquidity position.

(b) Credit risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Bank's loans and advances to customers and to other banks. For risk management reporting purposes, the Bank considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk).

Management of credit risk

The Board of Directors has delegated responsibility for the oversight of credit risk to its Credit Committee. A separate Credit Risk Department is responsible for the management of the Bank's credit risk. The management of the credit risk exposures to borrowers is conducted through regular analysis of the borrowers' credit worthiness. Exposure to credit risk is also managed in part by obtaining collateral and guarantees.

Analysis of credit quality

The tables below set out information about the credit quality of financial assets and the allowance for impairment/loss held by the Bank against those assets.

The table below represents a worst case scenario of credit risk exposure of the Bank at 31 December 2016 and 2015, without taking into account any collateral held or other credit enhancements attached. For financial assets, the exposures set out below represent the net carrying amounts as reported in the statement of financial position.

	Loans to customers		Investments in securities		Balances with banks and with CBK		Financial guarantees	
	2016	2015	2016	2015	2016	2015	2016	2015
Maximum exposures to credit risk								
Carrying amount	137,928	122,077	24,770	21,610	44,789	25,061	-	-
Amount committed/ guaranteed	-	-	-	-	-	-	2,003	2,085
	137,928	**122,077**	**24,770**	**21,610**	**44,789**	**25,061**	**2,003**	**2,085**
At amortized cost								
Standard	135,822	118,372	24,770	21,610	44,789	25,061	-	-
Watch	2,001	3,505	-	-	-	-	-	-
Substandard	2,078	1,318	-	-	-	-	-	-
Doubtful	1,029	1,849	-	-	-	-	-	-
Loss	7,026	7,035	-	-	-	-	-	-
Total	**147,956**	**132,079**	**24,770**	**21,610**	**44,789**	**25,061**	**-**	**-**
Allowance for impairment (individual and collective)	(10,028)	(10,002)	-	-	-	-	-	-
Net carrying amount	**137,928**	**122,077**	**24,770**	**21,610**	**44,789**	**25,061**	**-**	**-**
Off balance: maximum exposure								
Financial guarantees: Low - fair risk	-	-	-	-	-	-	2,003	2,085
Total committed/ guaranteed	**-**	**-**	**-**	**-**	**-**	**-**	**2,003**	**2,085**
Provisions recognized as liabilities	-	-	-	-	-	-	(21)	(17)
Total exposure	**-**	**-**	**-**	**-**	**-**	**-**	**1,982**	**2,068**

	2016				2015			
	Indi-vidu-als	Micro	Corpo-rate	Total Loans	Indi-viduals	Micro	Corpo-rate	Total Loans
Loans and advances to customers								
Total gross amount	50,014	25,915	72,027	147,956	40,866	22,753	68,460	132,079
Allowance for impairment (individual and collective)	(2,048)	(2,236)	(5,744)	(10,028)	(1,727)	(1,921)	(6,354)	(10,002)
Net carrying amount	**47,966**	**23,679**	**66,283**	**137,928**	**39,139**	**20,832**	**62,106**	**122,077**
At amortised cost								
Standard	47,827	23,084	64,912	135,823	38,691	20,084	59,597	118,372
Watch	407	445	1,149	2,001	617	553	2,335	3,505
Substandard	147	367	1,563	2,077	177	231	910	1,318
Doubtful	377	275	377	1,029	316	528	1,005	1,849
Loss	**1,256**	**1,744**	**4,026**	**7,026**	**1,065**	**1,357**	**4,613**	**7,035**
Total Gross	**50,014**	**25,915**	**72,027**	**147,956**	**40,866**	**22,753**	**68,460**	**132,079**

Less: allowance for individually impaired loans	(1,479)	(1,955)	(4,817)	(8,251)	(1,265)	(1,673)	(5,266)	(8,204)
Less: allowance for collectively impaired loans	(569)	(281)	(927)	(1,777)	(462)	(248)	(1,088)	(1,798)
Total Allowance for impairment	**(2,048)**	**(2,236)**	**(5,744)**	**(10,028)**	**(1,727)**	**(1,921)**	**(6,354)**	**(10,002)**
Loans with renegotiated terms								
Carrying amount	**359**	**715**	**3,743**	**4,817**	**266**	**852**	**4,608**	**5,726**
Allowance for impairment	**(125)**	**(442)**	**(2,555)**	**(3,123)**	**(64)**	**(440)**	**(2,947)**	**(3,451)**
Net carrying amount	**234**	**273**	**1,188**	**1,694**	**202**	**412**	**1,661**	**2,275**
Loans by past due days								
Not past due	**46,676**	**21,871**	**60,599**	**129,146**	**38,036**	**18,822**	**57,672**	**114,530**
Past due 1-30 days	**1,428**	**1,450**	**5,711**	**8,589**	**846**	**1,496**	**5,209**	**7,551**
Past due 31 - 90 days	**532**	**723**	**2,334**	**3,589**	**724**	**723**	**1,303**	**2,750**
Past due 91 – 365 days	**480**	**504**	**252**	**1,236**	**582**	**748**	**1,420**	**2,750**
Past due over 365 days	**898**	**1,367**	**3,131**	**5,396**	**678**	**964**	**2,856**	**4,498**
	50,014	**25,915**	**72,027**	**147,956**	**40,866**	**22,753**	**68,460**	**132,079**

25. Financial risk management (continued)

(b) Credit risk (continued)
Analysis of credit quality (continued)

Impairment and provisioning

The total allowances that are required by the CBK Regulation on 'Credit Risk Management' (see 3.(f)(vii), include losses that have been incurred at the reporting date (the 'incurred loss model') and expected losses.

The Bank assesses the probability of default of the counterparties, using internal rating tools tailored to the various categories of counterparties. Such tools combine statistical analysis and judgment and are validated, where appropriate, by comparison with externally available data.

Counterparties are segmented into five rating classes and the Bank's rating scale, which is shown below, reflects the range of default probabilities defined for each rating class. Exposures migrate between classes as the assessment of their probability of default changes. The rating tools are continuously reviewed, upgraded and validated by the Bank.

Loans are rated from A to E in the Bank's internal credit risk rating system:

- A Standard
- B Watch
- C Sub-standard
- D Doubtful
- E Loss

The Bank reports the classification of its borrowers to the CBK and the Credit Register of Kosovo. The provisioning policy for these loans is detailed in Note 3.(f) (vii).

Individual and collective assessment of loan portfolio

For internal management purpose, the Bank segregates the loans into loans that are assessed individually for impairment: these are loans that are classified as substandard-list or lower. All other loans are analysed collectively for impairment assessment purposes.

The Bank's policy requires the review of individual loans and advances to customers that are above materiality thresholds of EUR 100 thousand (2015: EUR 100 thousand) at least quarterly when individual circumstances demand it.

Past due but not impaired loans

Loans and securities, where contractual interest or principal payments are past due, but the Bank believes that impairment is not appropriate on the basis of the level of security / collateral available and / or the stage of collection of amounts owed to the Bank.

Loans with renegotiated terms

Loans with renegotiated terms are loans that have been restructured due to deterioration in the borrower's financial position and where the Bank has made concessions that it would not otherwise consider. Once the loan is restructured it remains in this category independent of satisfactory performance after restructuring.

Write-off policy

The Bank writes off a loan (and any related allowances for impairment) with the decision of the Board of Directors, in accordance with the regulations of Central Bank of Kosovo. The write-off decision is taken after considering information such as the occurrence of significant changes in the borrower issuer's financial position, such that the borrower / issuer can no longer pay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure. The total amount written off during 2016, is EUR 916 thousand (2015: EUR 2,063 thousand).

25. Financial risk management (continued)

(b) Credit risk (continued)

Analysis of credit quality (continued)

Due from banks

Interbank exposures are closely monitored on a daily basis by risk management and the Treasury Department. The Bank limits its deposits and other banking transactions to sound local or international banks. Before a business relationship is initiated with a given bank, the management and the Risk Department carry out an analysis of the institution's financial standing. The financial performance of the counterparties is continuously monitored. Moreover, all correspondent banks as well as bond issuers in which the Bank has investment exposures are continuously monitored for their ratings by international rating agencies like: Standard & Poor's (S&P), Fitch and Moody's.

In accordance to the new regulation on large exposures of the Central Bank of Republic of Kosovo, banks shall not have any aggregate credit risk exposure to related counterparties exceeding 15% of Tier 1 Regulatory Capital.

Loans and advances to banks are granted without collateral. The table below presents the Bank's current accounts and time deposits with corresponding banks by credit ratings:

At 31 December	2016	2015
AA+ to AA-	4,948	3,389
A+ to A-	-	3,973
BBB+ to B-	770	1
Not Rated	92	126
Local Banks	2,112	-
	7,922	**7,489**

Investments in securities

Investments in debt securities are only with the Kosovo Government. These securities are not rated. The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the statement of financial position.

Lending commitments and financial guarantees

The maximum exposure from financial guarantees represents the maximum amount that the Bank should pay if the guarantee is called on, which may be significantly greater than the amount recognised as a liability. The maximum credit exposure for lending commitments is the full amount of the commitment.

Risk limit control and mitigation policies

The Bank manage limits and controls the concentrations of credit risk wherever they are identified in particular to individual counterparties and groups, and to affiliates.

The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to a single borrower, or group of borrowers, and to geographical and industry segments. Such risks are monitored on a regular basis and subject to an annual or more frequent review, if necessary.

Exposure to credit risk is also managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Other controls and mitigation measures are outlined below.

25. Financial risk management (continued)

(b) Credit risk (continued)

Risk limit control and mitigation policies

Collateral held and other credit enhancements, and their financial effect

The Bank holds collateral against loans and advances to customers in the form of mortgage interests over property and other movable assets. Estimates of fair value are based on the value of collateral assessed at the time of borrowing. Collateral generally is not held over loans and advances to banks. An estimate of the fair value of collateral and other security enhancements held against loans is shown below:

	2016		2015	
	Loans and advances to customers	FV of collateral	Loans and advances to customers	FV of collateral
Mortgages	33,492	33,419	22,697	22,520
Cash collateral	4,169	4,168	4,604	4,509
Pledge	64,508	53,841	51,600	44,241
Mixed (mortgages and pledge)	41,198	41,138	50,444	50,054
Not collateralised	4,589	-	2,734	-
Total	147,956	132,566	132,079	121,324

Concentration of credit risk

As at 31 December 2016, one exposures that exceed 10% of Tier 1 capital represent 1.55% (2015: 3.16%) of the total loans portfolio. The exposures to related parties at 31 December 2016, represent 19.93% (2015: 28.5%) of the Tier 1 Capital. The majority of the exposures to related parties are covered by cash collateral representing 17.54% (2015: 5.5%) of the Tier 1 Capital.

The Bank monitors concentrations of credit risk by sector and by geographic location. An analysis of concentrations of credit risk at the reporting date is shown below:

	Loans to customers		Investments in securities		Balances with banks and CBK		Financial guarantees	
	2016	2015	2016	2015	2016	2015	2016	2015
Concentration by sector								
Corporate	66,283	62,106	-	-	-	-	1,198	1,922
Government	-	-	24,770	21,610	-	-	-	-
Banks	-	-	-	-	44,789	25,061	-	-
Individuals	47,966	39,139	-	-	-	-	-	-
Micro-enterprises	23,679	20,832	-	-	-	-	805	163
Total	**137,928**	**122,077**	**24,770**	**21,610**	**44,789**	**25,061**	**2,003**	**2,085**
Concentration by location								
EU countries	-	-	-	-	5,810	7,363	-	-
Republic of Kosovo	137,928	122,077	24,770	21,610	38,979	17,698	2,003	2,085
Total	**137,928**	**122,077**	**24,770**	**21,610**	**44,789**	**25,061**	**2,003**	**2,085**

25. Financial risk management (continued)

(c) Market risk

Market risk is the risk that changes in market prices, such as interest rates, foreign exchange rates and credit spreads (not relating to changes in the obligor's/issuer's credit standing) will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

Interest rate risk

Interest rate risk is comprised of the risk that the value of a financial instrument will fluctuate due to changes in market interest rates and the risk that the maturities of interest bearing assets differ from the maturities of the interest bearing liabilities used to fund those assets. The length of time for which the rate of interest is fixed on a financial instrument therefore indicates to what extent it is exposed to interest rate risk. The assets and customer term deposits of the Bank carry fixed interest rates.

The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest-bearing assets and liabilities mature or reprice at different times or in differing amounts. The Bank attempts to mitigate this risk by monitoring the repricing dates of its assets and liabilities. In addition, the actual effect will depend on a number of other factors, including the extent to which repayments are made earlier or later than the contracted dates and variations in interest rate sensitivity within repricing periods and among currencies. Bank's exposures are based on Kosovo marked interest rates and the Bank faces only repricing risk.

On quarterly basis are held the Operational Risk Management Meetings, where are discussed the following issues:

- The report on the Operational Risk- the report is prepared from the Department of Risk
- The report on the Liquidity and Market Risk- the report is prepared from the Department of Risk
- The report on Interest rate risk - the report is prepared from the Department of Risk. The report details the interest rates of the Bank in comparison to the market interest rates and gives details of the changes in the interest rates in the market, any unusual fluctuations etc.

The Department of Treasury on a constant basis monitors the interest rates risk through monitoring the market conditions and taking necessary re- pricing or reallocation decisions with the approval of the Asset and Liability Committee. A report with regard to this monitoring is prepared and presented in the meeting of Assets and Liabilities Committee. Necessary measures are taken whether interest rates are changing adversely. The report includes analysis on the top depositors, their impact of the rates of deposits, investments on securities analysis, average interest rates on client accounts, GAP analysis on liquidity risk, etc.

Exposure to interest rate risk

The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest-earning assets and interest-bearing liabilities mature or reprice at different times or in differing amounts. In the case of floating rate assets and liabilities, the Bank is also exposed to basis risk, which is the difference in repricing characteristics of the various floating rate indices, such as the savings rate, LIBOR and different types of interest. Risk management activities are aimed at optimising net interest income, given market interest rate levels consistent with the Bank's business strategies.

Asset-liability risk management activities are conducted in the context of the Bank's sensitivity to interest rate changes. In decreasing interest rate environments, margins earned will narrow as liabilities interest rates will decrease with a lower percentage compared to assets' interest rates. However, the actual effect will depend on various factors, including stability of the economy, environment and level of the inflation.

25. Financial risk management (continued)

(c) Market risk (continued)

Exposure to interest rate risk (continued)

The average effective yields of significant categories of financial assets and liabilities of the Bank as at 31 December 2016 and 2015 are as follows:

	USD		EUR		CHF	
Assets	**2016**	**2015**	**2016**	**2015**	**2016**	**2015**
Cash on hand and at banks	-	0.01	0.02	-	(0.27)	
Balances with CBK	-	-	(0.40)	-	-	-
Loans to customers	-	-	9.20	10.88	-	-
Investment securities held-to-maturity	-	-	2.94	1.45	-	-
Investment securities available for sale	-	-	0.69	1.40	-	-
Liabilities						
Customer deposits	0.23	0.33	1.09	1.4	-	0.01
Subordinated debt	-	-	7.50	7.5	-	-

The management of interest rate risk against interest rate gap limits is supplemented by monitoring the sensitivity of the Bank's financial assets and liabilities to various standard and non-standard interest rate scenarios. Standard scenarios include a 1% parallel fall or rise in all yield curves.

25. Financial risk management (continued)

(c) Market risk (continued)

Exposure to interest rate risk (continued)

An analysis of the Bank's sensitivity to an increase or decrease in market interest rates (assuming no asymmetrical movement in yield curves and a constant statement of financial position) is as follows:

Estimated Profit (loss) effect	up to 1 Year scenarios		over 1 Year scenarios	
	100 bp	100 bp	100 bp	100 bp
	Increase	Decrease	Increase	Decrease
2016	(37)	41	45	(45)
2015	(32)	29	47	(47)

The following table shows the interest bearing and non-interest bearing financial instruments by maturity date:

31 December 2016	Up to 1 month	1-3 Month	3-6 Month	6-12 Month	1-5 years	Over 5 years	Non-interest bearing	Totali
Assets								
Cash on hand and at banks	-	-	-	-	-	-	16,113	16,113
Balances with CBK	-	-	-	-	-	-	36,867	36,867
Investments in securities - fixed rate	-	-	7,544	507	4,654	12,065	-	24,770

Loans to cus-tomers - fixed rate	3,693	3,641	4,796	19,351	72,719	33,728	-	137,928
Other assets	-	-	-	-	-	-	489	489
Total	**3,693**	**3,641**	**12,340**	**19,858**	**77,373**	**45,793**	**53,469**	**216,167**

Liabilities

Due to Cus-tomers – fixed rate	101,422	3,569	7,942	46,953	37,790	32	-	197,708
Due to Banks	2,196	-	-	-	-	-	-	2,196
Subor-dinated debt – fixed rate	-	-	-	-	-	1,050	-	1,050
Other li-abilities	-	-	-	-	-	-	238	238
Total	**103,618**	**3,569**	**7,942**	**46,953**	**37,790**	**1,082**	**238**	**201,192**
Gap	**(99,925)**	**72**	**4,398**	**(27,095)**	**39,583**	**44,711**	**53,231**	**14,975**
Cumula-tive gap	**(99,925)**	**(99,853)**	**(95,455)**	**(122,550)**	**(82,967)**	**(38,256)**	**14,975**	**-**

25. Financial risk management (continued)

(c) Market risk (continued)

Exposure to interest rate risk (continued)

31 December 2015	Up to 1 month	1-3 Month	3-6 Month	6-12 Month	1-5 years	Over 5 years	Non-interest bearing	Totali
Assets								
Cash on hand and at banks	-	-	-	-	-	-	15,397	15,397
Balances with CBK	-	-	-	-	-	-	17,572	17,572
Investments in securities - fixed rate	2,498	10,119	3,735	4,256	1,002	-	-	21,610
Loans to customers - fixed rate	2,326	3,131	6,676	14,669	69,331	25,944	-	122,077
Other assets	-	-	-	-	-	-	363	363
Total	**4,824**	**13,250**	**10,411**	**18,925**	**70,333**	**25,944**	**33,332**	**177,019**
Liabilities								
Due to Customers – fixed rate	25,487	3,005	6,924	34,957	36,985	514	55,879	163,751
Due to Banks	-	-	-	-	-	-	1,393	1,393
Subordinated debt – fixed rate	-	-	-	-	1,050	-	-	1,050
Other liabilities	-	-	-	-	-	-	290	290
Total	**25,487**	**3,005**	**6,924**	**34,957**	**38,035**	**514**	**57,562**	**166,484**
Gap	**(20,663)**	**10,245**	**3,487**	**(16,032)**	**32,298**	**25,430**	**(24,230)**	**10,535**
Cumulative gap	**(20,663)**	**(10,418)**	**(6,931)**	**(22,963)**	**9,335**	**34,765**	**10,535**	**-**

25. Financial risk management (continued)

(c) Market risk (continued)

Exposure to currency risk (continued)

The Bank is exposed to currency risk through transactions in foreign currencies. The Bank ensures that the net exposure is kept to an acceptable level by buying or selling foreign currency at spot when necessary to address short-term balances.

The currency risk is not significant, as the majority of transactions of the Bank are in local currency. The foreign currencies the Bank deals with are predominantly United States Dollars (USD) and Swiss Franc (CHF). The rates used for translation as at 31 December 2016 and 2015 are as follows:

	2016	2015
Currency	EUR	EUR
1 USD	0.9487	0.9185
1 CHF	0.9312	0.9229
1 GBP	1.1680	1.3624

An analysis of the Bank's sensitivity to an increase or decrease in foreign currency rates is as follows:

	USD		CHF		GBP	
	2016	2015	2016	2015	2016	2015
Sensitivity rates	5%	5%	5%	5%	5%	5%
Profit or loss						
+5% of Euro	(0.30)	(0.25)	-	0.80	-	-
- 5% of Euro	0.30	0.25	-	(0.80)	-	-

The Bank's exposure to foreign currency risk, expressed in EUR equivalents is as follows:

31 December 2016	EUR	USD	CHF	GBP	Totali
Assets					
Cash on hand and at banks	8,625	4,123	3,173	192	16,113
Balances with CBK	36,867	-	-	-	36,867
Investments in securities	24,770	-	-	-	24,770
Loans to customers	137,928	-	-	-	137,928
Other assets	489	-	-	-	489
	208,679	**4,123**	**3,173**	**192**	**216,167**
Liabilities					
Due to customers	190,214	4,129	3,173	192	197,708
Due to banks	2,196	-	-	-	2,196
Subordinated debt	1,050	-	-	-	1,050
Other liabilities	238	-	-	-	238
	193,698	**4,129**	**3,173**	**192**	**201,192**
Net foreign currency position	**14,801**	**(6)**	**-**	**-**	**14,795**
31 December 2015					
Assets					
Cash on hand and at banks	8,194	2,832	4,314	57	15,397
Balances with CBK	17,572	-	-	-	17,572
Investments in securities	21,610	-	-	-	21,610
Loans to customers	122,077	-	-	-	122,077
Other assets	363	-	-	-	363
	169,816	**2,832**	**4,314**	**57**	**177,019**
Liabilities					
Due to customers	156,564	2,832	4,299	56	163,751
Due to banks	1,393	-	-	-	1,393
Subordinated debt	1,050	-	-	-	1,050
Other liabilities	290	-	-	-	290
	159,297	**2,832**	**4,299**	**56**	**166,484**
Net foreign currency position	**10,519**	**-**	**15**	**1**	**10,535**

25. Financial risk management (continued)

(d) Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations from its financial liabilities.
The Bank's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Bank's reputation.

The Bank monitors its liquidity on a daily basis in order to manage its obligations as and when they fall due.

Exposure to liquidity risk

Funds are raised using a range of instruments including customers' deposits, subordinated debt and share capital.

Flexibility limits dependence on any one source of funds and generally lowers the cost of funds. The Bank strives to maintain a balance between continuity of funding and flexibility through the use of liabilities with a range of maturities. The Bank continually assesses liquidity risk by identifying and monitoring changes in funding required to meet business goals and targets set in terms of the overall Bank strategy. In addition, the Bank holds a portfolio of liquid assets as part of its liquidity risk management strategy.

Management of liquidity risk

Residual contractual maturities of financial assets and liabilities

The following tables show the discounted cash flows of the Bank's financial liabilities on the basis of their earliest possible contractual maturity. The Bank's expected cash flows of these instruments vary significantly from this analysis. For example, demand accounts are expected to maintain a stable or increasing balance.

31 December 2016	Up to 1 month	1-3 months	3-6 months	6-12 months	1-5 years	Over 5 years	Undetermined maturity	Total
Assets								
Cash on hand and at banks	16,113	-	-	-	-	-	-	16,113
Balances with CBK	22,058	-	-	-	-	-	14,808	36,866
Investments in securities	-	-	7,545	507	4,654	12,065	-	24,771
Loans to customers	3,693	3,641	4,796	19,351	72,719	33,728	-	137,928
Other assets	489	-	-	-	-	-	-	489
Total	**42,353**	**3,641**	**12,341**	**19,858**	**77,373**	**45,793**	**14,808**	**216,167**
Liabilities								
Due to customers	101,422	3,569	30,192	24,703	37,790	32	-	197,708
Due to banks	2,196	-	-	-	-		-	2,196
Subordinated debt	-	-	-	-	-	1,050	-	1,050
Other liabilities	238	-	-	-	-	-	-	238
Total	**103,856**	**3,569**	**30,192**	**24,703**	**37,790**	**1,082**	-	**201,192**
Liquidity gap	**(61,503)**	**72**	**(17,851)**	**(4,845)**	**39,583**	**44,711**	14,808	**14,975**
Cumulative gap	**(61,503)**	**(61,431)**	**(79,282)**	**(84,127)**	**(44,544)**	**167**	14,975	**-**

25. Financial risk management (continued)

(d) Liquidity risk (continued)

31 December 2015	Up to 1 month	1-3 months	3-6 months	6-12 months	1-5 years	Over 5 years	Un-determined maturity	Total
Assets								
Cash on hand and at banks	15,397	-	-	-	-	-	-	15,397
Balances with CBK	4,065	-	-	-	-	-	13,507	17,572
Investments in securities	2,498	10,119	3,735	4,256	1,002	-	-	21,610
Loans to customers	2,326	3,131	6,676	14,669	69,331	25,944	-	122,077
Other assets	363	-	-	-	-	-	-	363
Total	**24,649**	**13,250**	**10,411**	**18,925**	**70,333**	**25,944**	**13,507**	**177,019**
Liabilities								
Due to customers	81,366	3,005	6,924	34,957	36,985	514	-	163,751
Due to banks	1,393	-	-	-	-	-	-	1,393
Subordinated debt	-	-	-	-	1,050	-	-	1,050
Other liabilities	290	-	-	-	-	-	-	290
Total	**83,049**	**3,005**	**6,924**	**34,957**	**38,035**	**514**	-	**166,484**
Liquidity gap	**(58,400)**	**10,245**	**3,487**	**(16,032)**	**32,298**	**25,430**	**13,507**	**10,535**
Cumulative gap	**(58,400)**	**(48,155)**	**(44,668)**	**(60,700)**	**(28,402)**	**(2,972)**	**10,535**	**-**

(e) Capital risk management

The Bank manages its capital to ensure that the Bank will be able to continue as a going concern while maximizing the return to shareholders through the optimisation of the debt and equity balance.

The equity structure of the Bank comprises share capital, reserves and retained earnings.

Regulatory capital

The Bank monitors the adequacy of its capital using, among other measures, the rules and ratios established by the Central Bank of Kosovo (“CBK”). The Capital Adequacy Ratio is the proportion of the regulatory capital to risk weighted assets, off balance-sheet items and other risks, expressed as a percentage. The minimum required Capital Adequacy Ratio is 8% for Tier 1 capital and 12% for total own funds.

Risk-Weighted Assets (RWAs)

Assets are weighted according to broad categories of national risk, being assigned a risk weighting according to the amount of capital deemed to be necessary to support them. Six categories of risk weights (0%, 20%, 50%, 75%, 100%, and 150%) are applied; for example cash and money market instruments have a zero risk weighting which means that no capital is required to support the holding of these assets. Property and equipment carries a 100% risk weighting, meaning that it must be supported by capital (Tier 1) equal to 8% of the carrying amount. Off-balance-sheet credit related commitments are taken into account. The amounts are then weighted for risk using the same percentages as for on-balance-sheet assets.

	2016	2015
Total risk weighted assets	141,556	124,914
Total risk weighted assets for operational risk	13,590	12,325
Total	**155,146**	**137,239**
Regulatory capital (Total Capital)	**22,763**	**18,601**
Capital adequacy ratio (Total Capital)	**14.67%**	**13.55%**

There have been no significant changes in the Bank's management of capital during the period.

25. Financial risk management (continued)

(e) Capital risk management (continued)

Gearing ratio

The Bank's risk management committee reviews the capital structure on a continuously basis. As part of this review, the committee considers the cost of capital and the risk associated with each class of capital. Based on the CBK regulations, the minimum leverage ratio is 7%.

The leverage ratio at the year ended was as follows:

	2015	2014
Total Assets	223,004	183,919
Total Equity	21,439	16,878
Leverage ratio	**9.61%**	**9.18%**

26. Subsequent events

There are no significant events after the reporting date that may require adjustment or disclosure in the financial statements.