BANKA PËR BIZNES SH.A.

FINANCIAL STATEMENTS PREPARED IN ACCORDANCE
WITH THE INTERNATIONAL FINANCIAL REPORTING STANDARDS
FOR THE YEAR ENDED 31 DECEMBER 2017
WITH INDEPENDENT AUDITORS' REPORT THEREON

Table of contents

Building a better working world

Ernst & Young Certified Auditors Ltd - Kosovo
Rr. Pashko Vasa 16/7
Prishtine, Kosova

Tel +381 38 220 155
Fax +381 38 220 155
ey.com

INDEPENDENT AUDITOR'S REPORT

To the shareholders of Banka për Biznes Sh.a

Report on the audit of the financial statements

Opinion

We have audited the financial statements of Banka për Biznes Sh.a ("the Bank"), which comprise the statement of financial position as at 31 December 2017, and the statement of 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 presents fairly, in all material respects the financial position of the Bank as at 31 December 2017, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS").

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 International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in Kosovo, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other information included in Banka për Biznes Sh.a 2017 Annual Report

Other information consists of the information included in Bank's 2017 Annual Report other than the financial statements and our auditor's report thereon. Management is responsible for the other information. The Bank's 2017 Annual Report is expected to be made available to us after the date of this auditor's report.

Our opinion on the financial statements does not cover the other information and we will not express any form of assurance conclusion thereon.

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

Responsibilities of management and those charged with governance for the financial statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS 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.

Responsibilities of management and those charged with governance for the financial statements (continued)

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.

Auditor's Responsibility for 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.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance of Banka për Biznes Sh.a 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.

Ernst & Young Certified Auditors Kosovo

Ernst & Young Certified Auditors Kosovo sh.p.k.

April 17, 2018
Prishtina, Kosovo

Banka për Biznes Sh.a.
Statement of Comprehensive Income
For the year ended 31 December 2017

In thousands of EUR	Note	2017	2016
Interest income	6	11,387	9,821
Interest expense	6	(1,741)	(1,670)
Net interest income		**9,646**	**8,151**
Fee and commission income	7	2,309	2,000
Fee and commission expense	7	(653)	(522)
Net fee and commission income		**1,656**	**1,478**
Recoveries of loans previously written off		690	583
Net foreign exchange gain		12	(2)
Gain from sale of securities available for sale	14	1,065	1,878
Other operating income	8	790	35
Total operating income		**13,859**	**12,123**
Impairment losses	15	(543)	(830)
Net reversal of provisions for guarantees		27	10
Repossessed assets write-downs	18	(197)	(529)
Other provisions	23	(123)	(622)
Other operating expenses	9	(6,885)	(5,622)
Total operating expenses		**(7,721)**	**(7,593)**
Profit before income tax		**6,138**	**4,530**
Income tax expense	10	(631)	(387)
Net profit for the year		**5,507**	**4,143**
Other comprehensive income			
Items that are or may be reclassified to profit or loss			
Fair value reserve (available-for-sale financial assets)		2	(14)
Total comprehensive income for the year		**5,509**	**4,129**

The Statement of 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 59.

Banka për Biznes Sh.a.
Statement of Financial Position
As at 31 December 2017

In thousands of EUR	Note	2017	2016
Assets			
Cash on hand and at banks	11	17,833	12,691
Balances with Central Bank of Kosovo	12	33,998	27,248
Loans and advances to banks	13	1,450	600
Available-for-sale financial assets	14	17,152	18,267
Loans and advances to customers	15	132,551	103,149
Other financial assets	16	143	237
Other assets	17	815	141
Repossessed assets	18	155	898
Intangible assets	19	338	226
Property and equipment	20	1,725	980
Total assets		**206,160**	**164,437**
Liabilities			
Due to customers	21	177,780	140,598
Subordinated debt	22	840	1,845
Borrowings	22	4,143	4,248
Other liabilities	23	1,673	1,346
Other provisions	23	506	404
Deferred tax liability	10	124	126
Total liabilities		**185,066**	**148,567**
Equity			
Share capital	24	11,247	11,247
Other capital reserve	24	857	857
Revaluation reserve	24	96	96
Fair value reserve		(30)	(32)
Retained earnings		8,924	3,702
Total equity		**21,094**	**15,870**
Total liabilities and equity		**206,160**	**164,437**

These financial statements were approved by the management of the Bank on 10 April 2018 and signed on its behalf by:

Arton Celina
Chief Executive Officer

Avni Berisha
Head of Finance Department

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 59.

In thousands of EUR	Share capital	Other capital reserve	Revaluation reserve	Retained Earnings\ (Accumulated losses)	Fair value reserve	Total
Balance at 1 January 2016	**11,247**	**857**	**96**	**(441)**	**(18)**	**11,741**
Transactions with owners of the Bank						
Total comprehensive income for the year	-	-	-	-	-	-
Revaluation reserve	-	-	-	-	-	-
Profit for the year	-	-	-	4,143	-	**4,143**
Other comprehensive income	-	-	-	-	(14)	**(14)**
Total comprehensive income /(loss)	-	-	-	**4,143**	**(14)**	**4,129**
Balance at 31 December 2016	**11,247**	**857**	**96**	**3,702**	**(32)**	**15,870**
Transactions with owners of the Bank						
Dividends to equity holders	-	-	-	(285)	-	**(285)**
Total comprehensive income for the year	-	-	-	-	-	-
Profit for the year	-	-	-	5,507	-	**5,507**
Other comprehensive income	-	-	-	-	2	**2**
Total comprehensive income /(loss)	-	-	-	**5,222**	**2**	**5,224**
Balance at 31 December 2017	**11,247**	**857**	**96**	**8,924**	**(30)**	**21,094**

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 59.

In thousands of EUR	**Note**	**2017**	**2016**
Cash flows from operating activities			
Profit for the year before tax		6,138	4,530
Non-cash items in the financial statements:			
Depreciation	20	351	321
Amortisation	19	133	77
Gain from disposal of property and equipment and repossessed assets		(160)	(21)
Gain from repossession of collateral		(601)	-
Impairment losses from loans	15	543	830
Write down of repossessed assets	18	197	529
Other provisions		123	395
Gain from sale of AFS		(1,065)	(1,878)
Interest expense	6	1,741	1,670
Interest income	6	(11,387)	(9,821)
		(3,987)	**(3,368)**
Changes in:			
Loans and advances to banks	13	(850)	360
Loans and advances to customers	15	(28,884)	(16,524)
Restricted balances with the CBK	12	(2,674)	(3,248)
Other assets	17	(674)	(19)
Other financial assets	16	94	54
Repossessed assets	18	694	-
Due to customers	21	37,056	24,723
Other liabilities and provisions		313	643
Interest received		11,288	9,967
Interest paid	14	(1,746)	(1,684)
Income tax paid	10	(565)	(290)
Net cash generated from operating activities		**10,065**	**10,614**
Cash flows from investing activities			
Proceeds/(Investments) from/in available-for-sale investments		1,886	(7,927)
Purchase of property and equipment	20	(1,105)	(276)
Purchase of intangible assets	19	(245)	(156)
Proceeds from sale of property and equipment		2	37
Net cash used in investing activities		**538**	**(8,322)**
Cash flows from financing activities			
Repayment of borrowings	22	(2,600)	(800)
Receipts from borrowings	22	1,500	2,000
Dividend Distributed		(285)	-
Net cash generated from financing activities		**(1,385)**	**1,200**
Net increase in cash and cash equivalents		**9,218**	**3,492**
Cash and cash equivalents at beginning of the year	**11**	**27,646**	**24,154**
Cash and cash equivalents at the end of the year	**11**	**36,864**	**27,646**

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 59.

1. INTRODUCTION

The Bank for Private Business sh.a obtained a license for banking activities on 29 March 2001 and commenced operations on 24 April 2001.

Based on the decision of the Board of Directors dated 28 February 2005, and the final approval from the Central Bank of Kosovo ("CBK") dated 22 March 2005, the Bank changed its name to Banka per Biznes (Bank for Business) (the "Bank"). In 2006, the Bank was registered as a joint stock company ("sh.a"). The Bank operates as a commercial and savings bank to all categories of customers within Kosovo through its network of 8 branches and 19 sub branches located throughout Kosovo (2016: 7 branches and 19 sub branches).

2. BASIS OF PREPARATION

a) Statement of compliance

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as issued by the International Accounting Standards Board (IASB).

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 thousand, 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 26.

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.

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.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

d) Tax expense (continued)

(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.

(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.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

f) Financial assets and financial liabilities

(i) Recognition

The Bank initially recognises loans and advances, held-to-maturity and available-for-sale investments, deposits, borrowings 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
- available-for-sale financial assets.
  See notes 3.(h) and (i).

Financial liabilities

The Bank classifies its financial liabilities as measured at amortised cost.

(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 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.

Financial liabilities

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.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

f) Financial assets and financial liabilities (continued)

Financial liabilities (continued)

(v) Amortised cost measurement

The amortised cost of a financial asset or liability 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

Impairment of loans and advances

At each reporting date the Bank assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. A financial asset or a group of financial assets is impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s), and that the loss event has an impact on the future cash flows of the asset(s) that can be estimated reliably.

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

The Bank considers evidence of impairment for loans and advances at both a specific asset and collective level. All individually significant loans and advances are assessed for specific impairment. Those found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and advance with similar risk characteristics.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (type and amount of the loan). Based on historical data for each of these groups a loss factor is calculated. These expected loss factors are adjusted for management's judgment as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical trends, and then they are applied to estimate impairment loss on each group. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

Impairment losses on assets measured at amortised cost are calculated as the difference between the carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate.

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower then an assessment is made whether the financial asset should be derecognised. If the cash flows of the renegotiated asset are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case the original financial asset is derecognised and the new financial asset is recognised at fair value.

The impairment loss is measured as follows:

- If the expected restructuring does not result in derecognition of the existing asset, the estimated cash flows arising from the modified financial asset are included in the measurement of the existing asset based on their expected timing and amounts discounted at the original effective interest rate of the existing financial asset.
- If the expected restructuring results in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

Impairment losses are recognised in profit or loss and reflected in an allowance account against loans and advances. When an event occurring after the impairment was recognised causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

f. Financial assets and financial liabilities (continued)

(vii) Identification and measurement of impairment (continued)

Impairment of loans and advances (continued)

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, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be related objectively to an event occurring after the impairment loss was recognized, then the impairment loss is reversed through profit or loss; otherwise, any increase in fair value is recognized through OCI.

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.

h) Available-for-sale financial assets

Investment securities are initially measured at fair value plus incremental direct transaction costs.

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 debt securities. All 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. 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 (see (f)(vii)), are recognised in OCI 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.

i) Loans and receivables

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

j) Deposits, borrowings and subordinated debt

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

Deposits, borrowings 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.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

k) Repossessed assets

Repossessed assets are acquired through enforcement of security over non-performing loans and advances to customers that do not earn rental, and are not used by the Bank and are intended for disposal in a reasonably short period of time. Repossessed assets are measured at the lower of cost and net realizable value and any write-down is recognized in the profit or loss.

l) Property and equipment

(i) Recognition and measurement

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

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
Buildings	20 years
Computer and related equipment	5 years
Vehicles	5 years
Furniture, fixtures and equipment	5 years

Leasehold improvements are depreciated using the straight-line basis over the shorter of the lease term and their useful lives. The estimated useful life of the leasehold improvements is 5 years.

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.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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.

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.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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.

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2017, and have not been applied in preparing these financial statements. Those that may be relevant to the Bank are set out below. The Bank does not plan to adopt these standards and amendments early.

The standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Bank financial statements are disclosed below. The Bank intends to adopt these standards, if applicable, when they become effective.

s) Equity reserves

The reserves recorded in equity (OCI) on the Bank's statement of financial position include:

- Available-for-sale reserve, which comprises changes in fair value of available-for-sale investments;
- Other capital reserve, which comprises difference between accumulated losses in accordance with IFRS and CBK;
- Revaluation reserve, which comprises on repossessed collateral recognized in Property and equipment from Bank.

4. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS

4.1 Standards and interpretations issued but not yet effective

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2017, and have not been applied in preparing these financial statements. The Bank does not plan to adopt these standards and amendments early.

IFRS 9 *Financial Instruments*

In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early adoption permitted. It replaces IAS 39 Financial Instruments: Recognition and Measurement.

In October 2017, the IASB issued Prepayment Features with Negative Compensation (Amendments to IFRS 9). The amendments are effective for annual periods beginning on or after 1 January 2019, with early adoption permitted.

The Bank apply IFRS 9 as issued in July 2014 initially on 1 January 2018 and amendments to IFRS 9 on 1 January 2019. Based on assessments undertaken to date, the Bank estimates that adoption of IFRS 9 on 1 January 2018, will bring no changes to the classification and measurement of financial assets. The Bank is in process of assessing its preliminary results related to impairment requirements. The Bank expects the impairment allowance on loans to advances and investments in debt securities to increase, however for loans and advances it is not expected to exceed in total its current provisions calculated for regulatory purposes, which on December 31, 2017 are 34% higher than the IFRS provisions. On the other hand, investments in debt securities of the Kosovo Government are not provided under the regulatory purpose, however these investment are not expected to have deteriorated credit risk and any impairment will be calculated only for 12 months expected losses.

The above assessment is preliminary because not all transition work has been finalised. The actual impact of adopting IFRS 9 on 1 January 2018 may change because:

- IFRS 9 require the Bank to revise its accounting processes and internal controls and these changes are not yet complete;
- the Bank has not finalised the testing and assessment of controls over its new IT systems and changes to its governance framework;
- the Bank is refining and finalizing its models for ECL calculations; and
- the new accounting policies, assumptions, judgements and estimation techniques employed are subject to change until the Bank finalises its first financial statements that include the date of initial application.

Changes to classification and measurement

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

IFRS 9 includes three principal classification categories for financial assets: measured at amortised cost, FVOCI and FVTPL. It eliminates the existing IAS 39 categories of held to maturity, loans and receivables and available for sale. A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- it is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest (SPPI) on the principal amount outstanding.

4. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS (CONTINUED)

4.1 Standards and interpretations issued but not yet effective (continued)

IFRS 9 *Financial Instruments (continued)*

Changes to classification and measurement (continued)

A financial asset is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:

- it is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

All financial assets not classified as measured at amortised cost or FVOCI as described above are measured at FVTPL. In addition, on initial recognition the Bank may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

A financial asset is classified into one of these categories on initial recognition. See (vii) for the transition requirements relating to classification of financial assets.

Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of IFRS 9 are not separated. Instead, the hybrid financial instrument as a whole is assessed for classification. The Bank does not presently have any derivative or hybrid financial instruments.

Business model assessment

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

- the stated policies and objectives for the portfolio and the operation of those policies in practice, including whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of assets;
- how the performance of the portfolio is evaluated and reported to the Bank's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
- how managers of the business are compensated – e.g. whether compensation is based on the contractual cash flows collected or the total gain realised from the portfolio; and
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Bank's stated objective for managing the financial assets is achieved and how cash flows are realised.

Assessment whether contractual cash flows are solely payments of principal and interest.

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money, for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as a profit margin.

4. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS (CONTINUED)

4.1 Standards and interpretations issued but not yet effective (continued)

IFRS 9 *Financial Instruments (continued)*

Changes to classification and measurement (continued)

In assessing whether the contractual cash flows are solely payments of principal and interest, the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Bank considers:

– contingent events that would change the amount and timing of cash flows;
– leverage features;
– prepayment and extension terms;
– terms that limit the Bank’s claim to cash flows from specified assets – e.g. non-recourse asset arrangements; and
– features that modify consideration for the time value of money – e.g. periodic reset of interest rates.

Interest rates on retail loans made by the Bank are based on standard fixed rates that are set at the discretion of the Bank. In these cases, the Bank assess whether the SFR set are in line with market rates and provide the Bank with sufficient returns to cover for the:

- time value of money,
- credit risk associated with the principal amount outstanding during a particular period of time, and
- other basic lending risks and costs, as well as a profit margin.

All of the Banks retail loans contain prepayment features. A prepayment feature is consistent with the SPPI criterion if the prepayment amount substantially represents unpaid amounts of principal and interest on the principal amount outstanding, which may include reasonable compensation for early termination of the contract.

Impact assessment

The Bank has estimated that, the adoption of IFRS 9 at 1 January 2018, will not bring changes to its current measurement of the financial assets under IAS 39. The classification of its financial assets held as at 1 January 2018 will change as follows.

– Loans and advances to banks and to customers that are classified as loans and receivables and measured at amortised cost under IAS 39 will in general also be measured at amortised cost under IFRS 9.
– Debt investment securities that are classified as available-for-sale under IAS 39 will be measured at FVOCI, under IFRS 9, as these assets meet the SPPI conditions and the Bank’s current business model is to hold these assets for the purpose of both collecting contractual cash flows and selling financial assets.

Changes to the impairment calculation

IFRS 9 replaces the ‘incurred loss’ model in IAS 39 with a forward-looking ‘expected credit loss’ (‘ECL’) model. This will require considerable judgement over how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis. In addition to loans and receivables, the new impairment model applies also to the following financial instruments that are not measured at FVTPL:

– financial assets that are debt instruments; and
– loan commitments and financial guarantee contracts issued (previously, impairment was measured under IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*).

4. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS (CONTINUED)

4.1 Standards and interpretations issued but not yet effective (continued)

IFRS 9 *Financial Instruments (continued)*

Changes to the impairment calculation (continued)

IFRS 9 requires a loss allowance to be recognised at an amount equal to either 12-month ECLs or lifetime ECLs depending on the assessment of the risk of default. Lifetime ECLs are the ECLs that result from all possible default events over the expected life of a financial instrument, whereas 12-month ECLs are the portion of ECLs that result from default events that are possible within the 12 months after the reporting date. The Bank recognises loss allowances at an amount equal to lifetime ECLs, except in the following cases, for which the amount recognised will be 12-month ECLs:

- debt investment securities that are determined to have low credit risk at the reporting date. The Bank considers a debt security to have low credit risk when its credit risk rating is equivalent to the globally understood definition of 'investment-grade'; and
- loans and debt investment securities for which credit risk has not increased significantly since initial recognition.

The impairment requirements of IFRS 9 are complex and require management judgements, estimates and assumptions, particularly in the following areas, which are discussed in detail below:

- assessing whether the credit risk of an instrument has increased significantly since initial recognition; and
- incorporating forward-looking information into the measurement of ECLs.

ECLs are a probability-weighted estimate of credit losses and will be measured as follows:

- *financial assets that are not credit-impaired at the reporting date:* the present value of all cash shortfalls – i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive;
- *financial assets that are credit-impaired at the reporting date:* the difference between the gross carrying amount and the present value of estimated future cash flows;
- *undrawn loan commitments:* the present value of the difference between the contractual cash flows that are due to the Bank if the commitment is drawn down and the cash flows that the Bank expects to receive; and
- *financial guarantee contracts:* the present value of the expected payments to reimburse the holder less any amounts that the Bank expects to recover.

Financial assets that are credit-impaired are defined by IFRS 9 in a similar way to financial assets that are impaired under IAS 39. Under IAS 39, no provision is presently recognized for undrawn loan commitments and financial guarantee contracts, unless evidence of impairment is observed.

Definition of default

Under IFRS 9, the Bank considers a financial asset to be in default when:

- the borrower is unlikely to pay its credit obligations to the Bank in full, without recourse by the Bank to actions such as realising security (if any is held); or
- the borrower is more than 90 days past due on any material credit obligation to the Bank.

4. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS (CONTINUED)

4.1 Standards and interpretations issued but not yet effective (continued)

IFRS 9 *Financial Instruments (continued)*

This definition is largely consistent with the definition used for regulatory purposes for loans classified as doubtful or lost.

In assessing whether a borrower is in default, the Bank considers indicators that are consistent with the risk regulatory requirements for classification of loans as doubtful or lost:

- qualitative: e.g. breaches of contractual covenant;
- quantitative: e.g. overdue status and non-payment of another obligation of the same borrower to the Bank; and
- regulatory risk classification of the same borrowers in other banks.

Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances.

Credit risk grades

The Bank allocates each exposure to a credit risk grade based on requirements set forth by Credit Risk Management regulation by using qualitative and quantitative factors that are indicative of the risk of default. In addition to the risk classes introduced for regulatory purposes, the Bank identifies and monitors separately standard loans in past due from standard loans not in past due.

Each exposure is allocated to a credit risk grade on initial recognition based on available information about the borrower. Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different credit risk grade.

Determining whether credit risk has increased significantly from origination

Under IFRS 9, when determining whether the credit risk (i.e. risk of default) on a financial instrument has increased significantly since initial recognition, the Bank considers reasonable and supportable information that is relevant and available without undue cost or effort, including both quantitative and qualitative information and analysis based on the Bank’s historical experience, expert credit assessment and forward-looking information.

The Bank primarily identifies whether a significant increase in credit risk has occurred for an exposure that changes the regulatory risk classification from standard to watch assessed in line with the Bank’s policy for regulatory risk classification. All loans showing significant increase in credit risk are classified in Stage 2.

As a backstop, and as required by IFRS 9, the Bank presumptively considers that a significant increase in credit risk occurs no later than when an asset is more than 30 days past due. The Bank determines days past due by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received.

4. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS (CONTINUED)

4.1 Standards and interpretations issued but not yet effective (continued)

IFRS 9 *Financial Instruments (continued)*

Determining whether credit risk has increased significantly from origination (continued)

The Bank monitors the effectiveness of the criteria used to identify significant increases in credit risk by regular reviews to confirm that:

- the criteria are capable of identifying significant increases in credit risk before an exposure is in default;
- the average time between the identification of a significant increase in credit risk and default appears reasonable; and
- Exposures are not generally transferred directly from 12-month ECL measurement to credit-impaired.

Modified financial assets

The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. An existing loan whose terms have been modified may be derecognised and the renegotiated loan recognised as a new loan at fair value.

Under IFRS 9, when the terms of a financial asset are modified and the modification does not result in derecognition, the Bank considers whether the asset's credit risk has increased significantly by analysing quantitative and qualitative factors affecting risk of default.

The Bank renegotiates loans to customers in financial difficulties (referred to as 'forbearance activities') to maximise collection opportunities and minimise the risk of default. Under the Bank's forbearance policy, loan forbearance is granted on a selective basis if the debtor is currently in default on its debt or if there is a high risk of default, there is evidence that the debtor made all reasonable efforts to pay under the original contractual terms and the debtor is expected to be able to meet the revised terms.

The revised terms usually include extending the maturity, changing the timing of interest payments and amending the terms of loan covenants. Both retail and business loans are subject to the forbearance policy. Generally, forbearance is a qualitative indicator of default and credit impairment and expectations of forbearance are relevant to assessing whether there is a significant increase in credit.

Following forbearance, a customer needs to demonstrate consistently good payment behavior over *eight* months before the exposure is measured at an amount equal to 12-month ECLs. This assumption is also consistent with regulatory guidelines.

Inputs into measurement of ECLs

The key inputs into the measurement of ECLs are likely to be the term structures of the following variables:

- PD;
- loss given default (LGD); and
- exposure at default (EAD).

4. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS (CONTINUED)

4.1 Standards and interpretations issued but not yet effective (continued)

IFRS 9 ***Financial Instruments (continued)***

Modified financial assets (continued)

These parameters are derived from internally developed statistical models and other historical data that leverage regulatory models. They are adjusted to reflect forward-looking information as described below.

Credit risk grades are a primary input into the determination of the term structure of PD for exposures. The Bank employs statistical models to analyse the data collected and generate estimates of the remaining lifetime PD of exposures and how these are expected to change as a result of the passage of time.

This analysis includes the identification and calibration of relationships between changes in default rates and changes in key macro-economic factors, as well as in-depth analysis of the impact of certain other factors (e.g. forbearance experience) on the risk of default. For most exposures, key macro- economic indicators are likely to include GDP growth, interest rates and unemployment. The Bank's approach to incorporating forward-looking information into this assessment is discussed below.

LGD is the magnitude of the likely loss if there is a default. The Bank estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties. The LGD models consider the structure, collateral, seniority of the claim and recovery costs of any collateral that is integral to the financial asset. For loans secured by retail property, loan-to-value (LTV) ratios are likely to be a key parameter in determining LGD.

LGD estimates are calibrated for different economic scenarios and, for real estate lending, to reflect possible changes in property prices. They are calculated on a discounted cash flow basis using the effective interest rate as the discounting factor.

EAD represents the expected exposure in the event of a default. The Bank derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract, including amortisation, and prepayments. The EAD of a financial asset is the gross carrying amount at default. For lending commitments and financial guarantees, the EAD is considered to be the amount drawn, as well as potential future amounts that may be drawn or repaid under the contract, which are estimated based on historical observations and forward-looking forecasts.

The Bank measures ECLs considering the risk of default over the maximum contractual period (including any borrower's extension options) over which it is exposed to credit risk, even if, for risk management purposes, the Bank considers a longer period. The maximum contractual period extends to the date at which the Bank has the right to require repayment of an advance or terminate a loan commitment or guarantee.

For retail overdrafts and credit card facilities and certain corporate revolving facilities that include both a loan and an undrawn commitment component, the Bank measures ECLs over a period longer than the maximum contractual period if the Bank's contractual ability to demand repayment and cancel the undrawn commitment does not limit the Bank's exposure to credit losses to the contractual notice period. These facilities do not have a fixed term or repayment structure and are managed on a collective basis. The Bank can cancel them with immediate effect but this contractual right is not enforced in the normal day-to-day management, but only when the Bank becomes aware of an increase in credit risk at the facility level. This longer period is estimated taking into account the credit risk management actions that the Bank expects to take and that serve to mitigate ECLs. These include a reduction in limits and cancellation of the facility.

4. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS (CONTINUED)

4.1 Standards and interpretations issued but not yet effective (continued)

IFRS 9 ***Financial Instruments (continued)***

Modified financial assets (continued)

Where modelling of a parameter is carried out on a collective basis, the financial instruments are grouped on the basis of shared risk characteristics that include: instrument type; and credit risk grading.

The groupings are subject to regular review to ensure that exposures within a particular group remain appropriately homogeneous. For investments in debt securities in respect of which the Bank has limited historical data, external benchmark information published by recognised external credit rating agencies such as Moody’s is used to supplement the internally available data.

Forward-looking information

Under IFRS 9, the Bank incorporates forward-looking information into both its assessment of whether the credit risk of an instrument has increased significantly since initial recognition and its measurement of ECLs. The Bank will formulate a ‘base case’ view of the future direction of relevant economic variables and a representative range of other possible forecast scenarios based on advice from the Bank Risk Committee and economic experts and consideration of a variety of external actual and forecast information. This process involves developing two or more additional economic scenarios and considering the relative probabilities of each outcome. External information may include economic data and forecasts published by governmental bodies and monetary authorities in the countries where the Bank operates, supranational organisations such as the Organisation for Economic Co-operation and Development and the International Monetary Fund, and selected private sector and academic forecasters.

The base case represents a most-likely outcome and be aligned with information used by the Bank for other purposes, such as strategic planning and budgeting. The other scenarios represent more optimistic and more pessimistic outcomes. The Bank also periodically carries out stress-testing of more extreme shocks to calibrate its determination of these other representative scenarios. The Bank has identified and documented key drivers of credit risk and credit losses for each portfolio of financial instruments and, using an analysis of historical data, has estimated relationships between macro-economic variables and credit risk and credit losses. These key drivers include interest rates, unemployment rates and GDP forecasts. Predicted relationships between the key indicators and default and loss rates on various portfolios of financial assets have been developed based on analysing historical data over the past 5 years. The economic scenarios used are approved by the Bank Credit Committee.

4. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS (CONTINUED)

4.1 Standards and interpretations issued but not yet effective (continued)

IFRS 9 ***Financial Instruments (continued)***

Transition

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

- The Bank has taken the advantage of the exemption allowing it not to restate comparative information for prior periods with respect to classification and measurement (including impairment) changes. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 will be recognised in retained earnings and reserves as at 1 January 2018.
- The determination of the business model within which a financial asset is held will be made on the basis of the facts and circumstances that exist at the date of initial application.

IFRS 15 ***Revenue from Contracts with Customers***

Effective for annual periods beginning on or after 1 January 2018

Key requirements

IFRS 15 replaces all existing revenue requirements in IFRS (IAS 11 Construction Contracts, IAS 18 Revenue, IFRIC 13 Customer Loyalty Programmes, IFRIC 15 Agreements for the Construction of Real Estate, IFRIC 18 Transfers of Assets from Customers and SIC 31 Revenue – Barter Transactions Involving Advertising Services) and applies to all revenue arising from contracts with customers, unless the contracts are in the scope of other standards, such as IAS 17 Leases (or IFRS 16 Leases, once applied). Its requirements also provide a model for the recognition and measurement of gains and losses on disposal of certain non-financial assets, including property, plant and equipment and intangible assets. The Bank is assessing the potential impact on its financial statements resulting from IFRS 15, however it does not expect to be material since it has not material revenues than fall under the scope of this standard.

IFRS 16 ***Leases***

IFRS 16 was issued in January 2016 and it replaces IAS 17 Leases, IFRIC 4 Determining whether an Arrangement contains a Lease, SIC-15 Operating Leases-Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for all leases under a single on-balance sheet model similar to the accounting for finance leases under IAS 17. The standard includes two recognition exemptions for lessees – leases of ’low-value’ assets (e.g., personal computers)

and short-term leases (i.e., leases with a lease term of 12 months or less). At the commencement date of a lease, a lessee will recognise a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset). Lessees will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset.

Lessees will be also required to remeasure the lease liability upon the occurrence of certain events (e.g., a change in the lease term, a change in future lease payments resulting from a change in an index or rate used to determine those payments). The lessee will generally recognise the amount of the remeasurement of the lease liability as an adjustment to the right-of-use asset.

Lessor accounting under IFRS 16 is substantially unchanged from today’s accounting under IAS 17. Lessors will continue to classify all leases using the same classification principle as in IAS 17 and distinguish between two types of leases: operating and finance leases.

IFRS 16 also requires lessees and lessors to make more extensive disclosures than under IAS 17.

4. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS (CONTINUED)

4.1 Standards and interpretations issued but not yet effective (continued)

IFRS 16 *Leases (continued)*

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted, but not before an entity applies IFRS 15. A lessee can choose to apply the standard using either a full retrospective or a modified retrospective approach. The standard's transition provisions permit certain reliefs. An indication of current operating lease agreements is provided in Operating Lease Commitments in Note 25.

IFRS 17 Insurance Contracts

In May 2017, the IASB issued IFRS 17 Insurance Contracts (IFRS 17), a comprehensive new accounting standard for insurance contracts covering recognition and measurement, presentation and disclosure. Once effective, IFRS 17 will replace IFRS 4 Insurance Contracts (IFRS 4) that was issued in 2005. IFRS 17 applies to all types of insurance contracts (i.e., life, non-life, direct insurance and re-insurance), regardless of the type of entities that issue them, as well as to certain guarantees and financial instruments with discretionary participation features.

IFRS 17 is effective for reporting periods beginning on or after 1 January 2021, with comparative figures required.

IFRIC Interpretation 22 *Foreign Currency Transactions and Advance Consideration*

Foreign Currency Transactions and Advance Consideration is effective for annual periods beginning on or after 1 January 2018.

IFRIC Interpretation 23 *Uncertainty over Income Tax Treatment*

Uncertainty over Income Tax Treatments is effective for annual periods beginning on or after 1 January 2019.

IFRS 2 Classification and Measurement of Share-based Payment Transactions - *Amendments to IFRS 2*

Classification and Measurement of Share-based Payment Transactions amendments are effective for annual periods beginning on or after 1 January 2018, with early application permitted.

Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts-*Amendments to IFRS 4*

The amendments address concerns arising from implementing the new financial instruments standard, IFRS 9, before implementing IFRS 17 Insurance Contracts, which replaces IFRS 4.

Transfers of Investment Property — *Amendments to IAS 40*

Transfers of Investment Property is effective for annual periods beginning on or after 1 January 2018.

Amendments to IFRS 10 and IAS 28: *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*

Sale or Contribution of Assets between an Investor and its Associate or Joint Venture and further amendments its effective date deferred indefinitely until the research project on the equity method has been concluded.

Long-term interests in associates and joint ventures - *Amendments to IAS 28*

The amendment is effective for annual periods beginning on or after 1 January 2019. This amendment is not applicable to the Bank.

4. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS (CONTINUED)

4.2 Standards issued and effective for the annual period

IAS 7 Disclosure Initiative – *Amendments to IAS 7*

The amendment is effective for annual periods beginning on or after 1 January 2017. The amendments to IAS 7 Statement of Cash Flows are part of the IASB's Disclosure Initiative and help users of financial statements better understand changes in an entity's debt. The amendments require entities to provide disclosures about changes in their liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes (such as foreign exchange gains or losses). On initial application of the amendment, entities are not required to provide comparative information for preceding periods. Early application is permitted. The amendments are intended to provide information to help investors better understand changes in an entity's debt. The Bank has implemented the amendment and has presented additional disclosures about changes in liabilities arising from financing activities in Note 22.1.

IAS 12 Recognition of Deferred Tax Assets for Unrealised Losses – *Amendments to IAS 12*

The amendment is effective for annual periods beginning on or after 1 January 2017. This amendment is not applicable to the Bank.

IFRS Practice Statement 2: *Making Materiality Judgements*

Companies are permitted to apply the guidance in the Practice Statement (PS) to financial statements prepared any time after 14 September 2017. The PS contains non-mandatory guidance to help entities making materiality judgements when preparing general purpose IFRS financial statements. The PS may also help users of financial statements to understand how an entity makes materiality judgements in preparing such financial statements. The PS comprises guidance in three main areas:

- General characteristics of materiality
- A four-step process that may be applied in making materiality judgements when preparing financial statements. This process describes how an entity could assess whether information is material for the purposes of recognition, measurement, presentation and disclosure.
- How to make materiality judgements in specific circumstances, namely, prior period information, errors and covenants and in the context of interim reporting.

Furthermore, the PS discusses the interaction between the materiality judgements an entity is required to make and local laws and regulations. The PS includes examples illustrating how an entity might apply the guidance. Since the PS is a non-mandatory document, it does not change or introduce any requirements in IFRS. However, the PS provides helpful guidance for entities making materiality judgements and thus may improve the communication effectiveness of financial statements.

Amendments to IFRS 1 and IAS 28 due to "*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 1 and IAS 28 are to be applied for annual periods beginning on or after 1 January 2018.

Amendments to various standards due to "*Improvements to IFRSs (cycle 2015-2017)*

Resulting from the annual improvement project of IFRS (IFRS 3, IFRS 11, IAS 12 and IAS 23) primarily with a view to removing inconsistencies and clarifying wording is effective for annual periods beginning on or after 1 January 2019.

5. USE OF ESTIMATES AND JUDGMENTS

Management discusses with the Audit Committee 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 on a regular 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 methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

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) Net realizable value of repossessed assets

The Bank has established a policy with respect to the fair values of repossessed assets which are being measured at the lower of cost and net realizable value, which is the estimated selling price of the properties less costs to sell. The estimated selling price is derived from fair value measurements that include the use of external, independent property valuers, having appropriate recognized statutory professional qualifications, which is subsequently reviewed from the Bank Management for significant unobservable inputs and any required write down adjustments.

The Bank does not present repossessed property in the statement of financial position for periods longer than 5 years. The fair value measurements involved in determination of the net realizable value of the Bank's repossessed assets are categorized into Level 3 of the fair value hierarchy.

Valuation techniques and significant unobservable inputs

The following table shows the valuation technique used in measuring the fair value of repossessed assets, as well as the significant unobservable inputs used.

Valuation technique	Significant unobservable inputs
Reference to the current market: The valuation model uses prices and other relevant information generated by market transactions involving identical or comparable (similar) assets, liabilities, or a group of assets and liabilities (e.g. a business)	Market prices were modified to reflect the following: • The level of market transactions when the market activity is low or the price for an identical property is difficult to obtain • Specific condition of each property (construction, position etc.)

(Amounts in thousands of EUR, unless otherwise stated)

5. USE OF ESTIMATES AND JUDGMENTS (CONTINUED)

c) 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.

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 d) below.

d) 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 – fair value hierarchy

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

	2017			2016		
	Carrying value	Fair value Level 2	Fair value Level 3	Carrying value	Fair value Level 2	Fair value Level 3
Financial assets measured at fair value						
Available-for-sale	17,152	17,181	-	18,267	18,299	-
Financial assets not measured at fair value						
Cash on hand and at banks	51,831	-	51,831	39,939	-	39,939
Loans and advances to banks	1,450	-	1,450	600	-	600
Loans and advances to customers	132,551	-	131,081	103,149	-	102,005
Other financial assets	143	-	143	237	-	237
Financial liabilities not measured at fair value						
Due to customers	177,780	-	178,415	140,598	-	141,101
Subordinated debt	840	-	838	1,845	-	1,839
Borrowings	4,143	-	3,531	4,248	-	3,620
Other financial liabilities	1,656	-	1,656	1,346	-	1,346

5. USE OF ESTIMATES AND JUDGMENTS (CONTINUED)

d) Disclosure and estimation of fair value (continued)

Financial instruments – fair value hierarchy

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

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.

Balances with banks

Due from other banks include inter-bank placements and accounts. As loans, advances and deposits are short term and at floating rates, their fair value is considered to equate to their carrying amount.

Treasury Bills

Treasury Bills include treasury bills issued by the Government of Kosovo which are bought with the intention to hold till maturity. The fair value has been estimated using a discounted cash flow model based on a current yield curve appropriate for the remaining term to maturity.

Bonds

Bonds include 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.

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.

The Bank's loan portfolio has an estimated fair value approximately equal to its book value due either to their short term nature or to underlying interest rates which approximate market rates. The majority of the loan portfolio is subject to re-pricing within a year.

Due to customers, borrowings and subordinated debt

The fair value of subordinated debt and 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.

(Amounts in thousands of EUR, unless otherwise stated)

6. NET INTEREST INCOME

Net interest income is composed as follows:

	2017	2016
Interest income		
Loans and advances to customers	11,203	9,716
Loans and advances to banks	50	7
Available-for-sale investments	134	98
	11,387	**9,821**
Interest expenses		
Due to customers	(1,463)	(1,347)
Subordinated debt	(150)	(203)
Borrowings	(128)	(120)
	(1,741)	**(1,670)**
Net interest income	**9,646**	**8,151**

7. NET FEE AND COMMISSION INCOME

	2017	2016
Fee and commission income		
Payment transfers and transactions	1,702	1,525
Account maintainance fees	548	433
Other fees and commissions	59	42
Total fee and commission income	**2,309**	**2,000**
Fees and commissions on bank accounts	(557)	(422)
Fees and commissions on social aid distribution	(49)	(49)
Other fees and commissions	(47)	(51)
Total fee and commission expense	**(653)**	**(522)**
Net fee and commission income	**1,656**	**1,478**

8. OTHER OPERATING INCOME

	2017	2016
Income from repossession of Gjakova Building	580	-
Gain from sale of reppossed assets	168	-
Other income	42	35
Total	**790**	**35**

The Gjakova Building relates to a loan that has been written off several years ago. The repossession process was not completed until 2017 and the building was recognized against income in the current year.

(Amounts in thousands of EUR, unless otherwise stated)

9. OTHER OPERATING EXPENSES

	2017	2016
Personnel expenses (see below)	3,472	2,717
Rent	641	623
Depreciation and Amortisation	484	398
Insurance and security	306	290
Utilities and fuel	168	168
Repairs and maintenance	160	148
Communications	235	137
Consultancy	167	74
Legal expense	141	196
Card issuance costs	252	190
Advertising and marketing expenses	251	161
Cleaning expenses	48	42
Office materials	58	54
Board member remuneration	40	42
Travel	21	15
Other expenses	441	367
Total	**6,885**	**5,622**

The number of employees as at 31 December 2017 is 340 (31 December 2016: 327).

Personnel expenses are detailes as follows:

	2017	2016
Wages and salaries	2,741	2,323
Pension contribution	141	119
Accrued bonusses	545	250
Other compensations	45	25
Total	**3,472**	**2,717**

(Amounts in thousands of EUR, unless otherwise stated)

10. INCOME TAXES

The income tax charge differs from the theoretical amount that would arise using the weighted average tax rate applicable to profits of the bank as follows:

	Effective tax rate	**2017**	**Effective tax rate**	**2016**
Profit before tax		**6,138**		**4,530**
Tax calculated at 10%	10%	614	10%	453
Adjustment due to difference on provision for loans based on Central Bank of Kosovo rules	-	-	-	-
Written off loans tax effect	0.78%	48		
Tax effect of non-deductible expenses	0.70%	43	-	-
Tax effect of the accrued interest on term deposits	0.15%	9	-	-
Adjustments to other income	1.35%	(83)	0.44%	21
Utilisation of tax loss carried forward	-	-	(1.92%)	(87)
Income tax	**10.3%**	**631**	**8.5%**	**387**

Deferred tax is calculated based on the enacted tax rate of 10%. Deferred tax assets are recognised only to the extent that realisation of the related tax benefit is probable. As at 31 December 2017, a net deferred tax asset of EUR Nil (2016: EUR Nil thousand) has not been recognized due to the uncertainty that sufficient taxable profits will be available to allow the benefit of that deferred tax asset to be utilized.

	2017	**2016**
Liability at the beginning	202	105
Additions during the year	631	387
Payments during the year	(565)	(290)
Liability at the end	**268**	**202**

The carry forward period for any tax losses in accordance with the Kosovo Tax Law is six years.

Income tax is assessed at the rate of 10% (2016: 10%) of taxable income. The following represents a reconciliation of the accounting profit to the income tax:

	2011	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**
Tax losses unrecognized (utilized) during the year	1,160	2,232	(87)	(789)	(1,814)	(869)	-
Tax losses carried forward	1,327	3,559	3,472	2,683	869	-	-

The movements in deferred tax liabilities are presented as follows:

	2016	**Movement during 2017**	**2017**
Provisions for loan impairment	126	(2)	124
Deferred tax liability at the end of the year	**126**	**(2)**	**124**

(Amounts in thousands of EUR, unless otherwise stated)

11. CASH ON HAND AND AT BANKS

	2017	2016
Cash on hand	9,981	5,743
Cash at banks	7,852	6,948
Total	**17,833**	**12,691**

Cash and cash equivalents consist of the following:

	2017	2016
Cash on hand and at banks	17,833	12,691
Unrestricted balances with CBK (note 12)	19,031	14,955
Total	**36,864**	**27,646**

12. BALANCES WITH CENTRAL BANK OF KOSOVO

	2017	2016
Statutory reserves	14,967	12,293
Current accounts	19,031	14,955
Total	**33,998**	**27,248**

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 EUR deposits 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.

13. LOANS AND ADVANCES TO BANKS

	2017	2016
Term deposits		
Zirat Bankasi	1,000	**-**
IS Bankasi	350	**-**
	1,350	-
Blocked accounts:		
Raiffeisen Bank International	100	600
	100	**600**
Total	**1,450**	**600**

Loans and advances to banks include blocked accounts on behalf of guarantees from customers.

14. AVAILABLE-FOR-SALE INVESTMENTS

	2017	2016
Treasury Bills	5,224	10,720
Government Bonds	11,928	7,547
Total	**17,152**	**18,267**

During the year 2017 Bank has sold approximatly 19 financial instruments. Financial instruments all were sold with higher price compared to purchase price. The only buyer of financial instruments was Central Bank of Kosovo. Gain was recognized through profit and loss in the amount of EUR 1,065 thousand (2016: 1,878 thousand).

(Amounts in thousands of EUR, unless otherwise stated)

15. LOANS AND ADVANCES TO CUSTOMERS

	2017	2016
Loans and advances to customers	136,789	107,904
Accrued interest	658	561
Deferred disbursement fees	(902)	(649)
Total	**136,545**	**107,816**
Allowance for impairment losses on loans and advances to customers	(3,994)	(4,667)
Loans and advances to customers, net	**132,551**	**103,149**

Movements in the allowance for impairment losses on loans and advances to customers are as follows:

	2017	2016
At January 1	4,667	4,415
Loan loss provision	543	830
Loans written off	(1,216)	(578)
At December 31	**3,994**	**4,667**

The Bank manages individual counterparty exposures in order to be compliant with the rules of the Central Bank that require individual counterparty exposures not to exceed 15% of Tier I Capital (or EUR 19,628k).

As at 31 December 2017 and 2016 there are no counterparty exposures above 15% of the limit. In addition, the cumulative exposure of the top 10 clients of the bank is EUR 9,324k or 7% of the loan portfolio (2016: EUR 9,757k and 9%).

A reconciliation of the allowance for impairment losses for loans and advances, by class, is, as follows:

	2017			2016		
	Non-Retail	**Retail**	**Total**	**Non-retail**	**Retail**	**Total**
At 1 January	**3,950**	**717**	**4,667**	**3,885**	**530**	**4,415**
Charge for the year	626	(83)	543	643	187	830
Amounts written off	(897)	(319)	(1,216)	(578)	-	(578)
At 31 December	**3,679**	**315**	**3,994**	**3,950**	**717**	**4,667**

16. OTHER FINANCIAL ASSETS

	2017	2016
Receivables from customers	14	14
Accrued income from banking services	40	84
Accrued fees and commissions	54	55
Receivables from guarantees (Note 23)	-	70
Other receivables	35	14
Total	**143**	**237**

17. OTHER ASSETS

	2017	2016
Prepaid expenses	815	141
Total	**815**	**141**

(Amounts in thousands of EUR, unless otherwise stated)

18. REPOSSESED ASSETS

Repossesed assets are properties acquired through enforcement of security over loans and advances to customers. The Bank intends and is taking steps to sell these within a reasonable short period of time.

	2017	2016
Residential real estate	558	572
Commercial real estate	1,008	1,688
Total	**1,566**	**2,260**
Less: write-down for impairment	(1,411)	(1,362)
Net carrying value	**155**	**898**

The fair value of these assets is determined with reference to market values by independent external valuers. The values are further written down depending on their location, maintenance and conditions to reflect delays in likely settlement and the length of time for holding the assets.

Movements in the values written down are as follows:

	2017	2016
At January 1	1,362	833
Charge for the year	197	529
Reversal on disposal	(148)	-
At December 31	**1,411**	**1,362**

19. INTANGIBLE ASSETS

	Software
Cost	
At 1 January 2016	**894**
Additions	156
At 31 December 2016	**1,050**
Additions	245
At 31 December 2017	**1,295**
Accumulated amortisation	**-**
At 1 January 2016	**747**
Charge for the year	77
At 31 December 2016	**824**
Charge for the year	133
At 31 December 2017	**957**
Net carrying amount	**-**
At 31 December 2016	**226**
At 31 December 2017	**338**

(Amounts in thousands of EUR, unless otherwise stated)

20. PROPERTY AND EQUIPMENT

	Buildings	Leasehold improvements	Furniture, fixtures and equipment	Computers and related equipment	Vehicles	Total
Cost						
At 1 January 2016	**109**	**774**	**545**	**1,180**	**597**	**3,205**
Additions during the year	**-**	71	19	113	73	276
Disposals during the year	(13)	(18)	(79)	(13)	(17)	(140)
At 31 December 2016	**96**	**827**	**485**	**1,280**	**653**	**3,341**
Additions during the year	587	173	62	186	97	1,105
Disposals during the year	-	(53)	(30)	(26)	-	(109)
At 31 December 2017	**683**	**947**	**517**	**1,440**	**750**	**4,337**
Accumulated depreciation						
At 1 January 2016	**15**	**461**	**441**	**873**	**374**	**2,164**
Charge for the year	2	90	42	94	93	321
Disposals for the year	(13)	(16)	(21)	(24)	(50)	(124)
At 31 December 2016	**4**	**535**	**462**	**943**	**417**	**2,361**
Charge for the year	3	119	51	122	56	351
Disposals for the year	-	(46)	(29)	(25)	-	(100)
At 31 December 2017	**7**	**608**	**484**	**1,040**	**473**	**2,612**
Carrying amounts						
At 31 December 2016	**92**	**292**	**23**	**337**	**236**	**980**
At 31 December 2017	**676**	**339**	**33**	**400**	**277**	**1,725**

As at 31 December 2017 and 2016, the Bank does not have any property pledged as collateral.

Included in property and equipment as of 31 December 2017 are buildings with a carrying amount of EUR 676 thousand (2016: EUR 92 thousand) which represent repossessed collaterals and which management is using in its day to day activities.

Below are items of Property and Equipment that are fully depreciated but still in use as at 31 December 2017:

Category	**Cost**	**Accumulated**	**Net Book Value**
Buildings	9	9	**-**
Leasehold improvements	418	418	**-**
Furniture, fixtures and	511	511	**-**
Computers and related	674	674	**-**
Vehicles	237	237	**-**
Software	771	771	**-**
Total	**2,620**	**2,620**	**-**

(Amounts in thousands of EUR, unless otherwise stated)

21. DUE TO CUSTOMERS

	2017	2016
Current accounts	**70,685**	**60,214**
In EUR	67,132	58,565
In foreign currencies	3,553	1,649
Time deposits	**107,095**	**80,384**
In EUR	106,368	78,388
In foreign currencies	727	1,996
Total	**177,780**	**140,598**

22. SUBORDINATED DEBT AND BORROWINGS

	2017	2016
Subordinated debt		
EBRD	-	1,005
Individuals:		
Valon Budima	420	420
Armend Skeja	420	420
Total	**840**	**1,845**

During the year 2017, the Bank has fully paid the subordinated debt to EBRD in amount of EUR 1,000 thousand, in advance of its contractual maturity, along with interest in amount of EUR 25 thousand, and prepayments fee of EUR 20 thousand. The prepayment is done after the approval from CBK.

Subordinated debt was provided by the above parties to enable the Bank to maintain the minimum regulatory capital requirements.

The subordinated debt from individuals is repayable on 26 December 2023. This debt has no specific covenants attached to the agreements.

Borrowings	2017	2016
Borrowings from EFSE	3,128	3,240
Borrowings from EBRD	1,015	1,008
Total	**4,143**	**4,248**

During the year 2016, the Bank entered into a borrowing agreement with EBRD (European Bank for Reconstruction and Development) for a total of EUR 1,000 thousand. The purpose is to support the private individuals and SME loan portfolio related with energy efficiency programme. The borrowing bears an interest rate of 3.6% annually, and is repayable within five years. The interest is payable on quarterly basis.

During the year 2015, the Bank entered into a borrowing agreement with EFSE (European Fund for Southeastern Europe) for a total of EUR 4,000 thousand. The purpose is to support the private individuals and the SME loans portfolios. The borrowing bears an interest rate of 3.4% annually, and is repayable within three years. The interest is payable on a quarterly basis.

(Amounts in thousands of EUR, unless otherwise stated)

22. SUBORDINATED DEBT AND BORROWINGS (CONTINUED)

22.1 Changes in liabilities arising from financing activities are presented as follows:

	1 January 2017	Cash inflows	Cash outflows	Accruals of Interest	Declaration of Dividends	31 December 2017
Subordinated debt	1,845	-	(1,005)	-	-	840
Borrowings	4,248	1,500	(1,595)	(10)	-	4,143
Dividends payable	-	-	(285)	-	285	-
Total liabilities from financing activities	**6,093**	**1,500**	**(2,885)**	**(10)**	**285**	**4,983**

23. OTHER LIABILITIES AND PROVISIONS

	2017	2016
Payables on behalf of third parties	712	593
Provisions for letters of guarantee issued by the Bank	19	-
Payable on behalf of Ministry of Labour and Social Welfare	630	450
Payable on behalf of Ministry of Economy and Finance	121	78
Due to suppliers	191	225
Total Other Liabilities	**1,673**	**1,346**
Other provisions (see note below)	506	404
Total	**2,179**	**1,750**

The Bank acts as an agent for the transactions performed on behalf of government institutions with third parties. These include payments on behalf of the Ministry of Labour and Social Welfare and Ministry of Economy and Finance.

Other provisions include reserve for third-party active claims. Based on its policies and procedures, the bank determines in each quarter the current reserve through the reassesment of each claim individually.

Following is presented the movement of provision as of 31 December:

	2017	2016
At the beginning	404	642
Additions during the year	123	622
Utilized during the year	(21)	(860)
At the end	**506**	**404**

(Amounts in thousands of EUR, unless otherwise stated)

24. SHAREHOLDER'S EQUITY AND RESERVES

Share capital

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

At 31 December 2017, the subscribed capital was divided into 28,530 ordinary shares (2016: 28,530 ordinary shares) with a nominal value of EUR 394.2 each. The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Bank. All shares rank equally with regard to the Bank's residual assets.

The structure of subscribed capital is as follows:

		2017		**2016**	
	Name of shareholder	**%**	**EUR ('000)**	**%**	**EUR ('000)**
1	Afrim Govori	21.27	2,392	21.27	2,392
2	Rrustem Aliaj	17.27	1,942	17.27	1,942
3	Shaqir Palushi	11.81	1,328	9.91	1,115
4	EBRD	10.00	1,125	10.00	1,125
5	Mejdi Rexhepi	9.35	1,052	9.35	1,052
6	Moneta sh.p.k	7.15	804	5.35	601
7	Nazmi Viça	6.89	775	6.89	775
8	Kareman Limani	4.85	545	4.85	545
9	Banka di Cividale	4.62	520	4.62	520
10	Ahmet Arifi	2.39	269	2.39	269
11	Ismet Sylejmani	1.90	214	1.90	214
12	Naser Aliu	0.50	57	0.62	70
13	Besnik Vrella	0.50	57	0.62	70
14	Agim Bilalli	0.50	57	0.62	70
15	Luani Limited	0.44	49	0.44	49
16	Sokol Krasniqi	0.38	42	0.38	42
17	Flamur Bryma	0.09	10	0.09	10
18	Naim Abazi	0.09	9	0.44	50
19	Rasim Gashi	-	-	1.54	173
20	Riza Mikullovci	-	-	1.45	163
	Total	**100.00**	**11,247**	**100.00**	**11,247**

Other capital reserve

Other capital reserve was created as of 31 December 2011 as the difference between accumulated losses in accordance with IFRS and CBK which were written off through a reduction in the share capital. As a result, these reserves are restricted and not distributable.

Revaluation reserve

During 2014, the Bank decided to include in the Property and equipment a building which has been previously obtained as repossessed collateral. The building was recognized by the Bank in Property and equipment with a corresponding amount in the revaluation reserve in equity.

(Amounts in thousands of EUR, unless otherwise stated)

25. COMMITMENTS AND CONTINGENCIES

The Bank issues guarantees for its customers. These instruments bear a credit risk similar to that of loans granted. Guarantees issued in favour of customers are secured by cash collateral, and non cash collateral (real estate and movable collateral).

Guarantees extended to customers	**2017**	**2016**
Secured by cash deposits	591	828
Secured by collateral (real estate and movable collateral)	713	604
Unsecured	-	794
Less: Provision recognised as liabilities	(29)	(58)
Total	**1,275**	**2,168**

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

Credit commitments	**2017**	**2016**
Approved but not disbursed loans	51	420
Unused overdraft limits approved	5,395	4,779
Unused credit card facilities	453	416
Total	**5,899**	**5,615**

Legal

The Bank is involved in routine legal proceedings in the ordinary course of business at 31 December 2017 and 2016. The Bank's management is of the opinion that no material losses will be incurred in relation to legal claims, except for those already provided for and recognized in profit or loss as disclosed in Note 23.

Lease commitments

The Bank has entered into non-cancelable lease commitments, which are composed as follows:

	2017	**2016**
Not later than 1 year	138	510
Later than 1 year and not later than 5 years	504	113
Total	**642**	**623**

26. 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.

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 Audit Committee and Risk Committee, which are responsible for developing and monitoring the Bank's risk management policies in their specified areas.

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, through its training and procedures and policies for management, 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 in these functions 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).

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

b) Credit risk (continued)

Management of credit risk

The Board of Directors has delegated the responsibility for the management of credit risk in respect to lending authority to its Credit Risk Department for the following categories: business loans (Corporate, SME, and Micro – including also the Agro Segment) and personal loans (PI) up to EUR 50 thousand which are approved by the Credit Risk Department.

Credit exposures larger than EUR 50 thousand and less than 10% of the Bank's Tier I Capital are approved by the Credit Risk Department / Credit Committee, while exposures over 10% of the Bank's Tier I Capital are approved by the Board of Directors according to the Credit Risk Policy.

Based on the request of the regulatory authority, during 2017, the Bank has made changes on the responsibilities of risk management and specifically in credit risk management. As of March 2017, according to the Regulation on Corporate Governance of Banks, new organizational structure has been introduced and Risk Department has been divided into two separated departments, the Risk Management Department, and the Credit Risk Department.

Risk Management Department is responsible for drafting or reviewing policies and procedures related to risk and at the same time is responsible for the process of property valuations, credit monitoring process, credit classification and weighting of risk capital under the Capital Adequacy Regulation and identification of credit risk arising from new products / processes involving lending. Risk Management Department is organized in three sectors including Credit Risk Sector, the Market and Liquidity Risk Sector as well as the Operational Risk Sector.

Credit Risk Department is responsible for managing the process of assessing the creditworthiness and credit capacity, the assessment of collateral adequacy, the decision making process, monitoring/managing arrears of problematic and nonperforming loans, including loans in loss and write-off managed by outsourced companies, as well as identification of credit risk arising from new products / processes involving lending. Credit Risk Department includes the lending sector and collection.

The Bank has followed the strategy of further diversification and growth in loan portfolio according to the defined segments of the loans, particularly in the individual loans segment - PI, the MICRO and AGRO segment and SME loans segment. During 2017, the bank has made a significant increase in the credit portfolio both by volume and by number, and the increase was mainly due to the targeted loan segments, respectively the PI, MICRO and AGRO loans segment. To support the growth strategy in small loans, the bank was supposed to increase the number of staff especially in the branch level, whereas it had recruited many experienced credit analysts mainly coming from the largest banks operating in the country.

The segmentation of the credit (loan) portfolio is based on the type and size of the subject (borrower), and in general it is grouped in Retail and Business clients.

Retail clients or Private Individuals (PI) are all types of customers who have their main source of repayment from income as wages, stable rents, royalties and other verifiable revenues.

Business clients are segregated in three main segments; MICRO, SME and Corporate. There is also a subcategory of agribusiness clients who are grouped as AGRO clients, which are allocated according to the procedures of segregation between main sectors in MICRO AGRO and SME AGRO.

Business clients are considered all types of customers who have their main source of income from business activity. Segregation between the business segments is based on the annual turnover. All business clients that have annual turnover up to EUR 300 thousand are considered as MICRO clients. All business clients that have annual turnover from 301 thousand up to EUR 2 milion are considered SME clients, while all business clients that have annual turnover above EUR 2 milion are considered as Corporate clients.

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

b) Credit risk (continued)

Management of credit risk (continued)

Regarding the regulatory requirements for reporting under IFRS 9, the bank has started the implementation project and it is in the process. During 2017, the bank has hired external consultant to assist in the development of methodology and the implementation of software. The bank is in the process of developing the model and the first draft with methodology is expected to be finalized in the first quarter of 2018.

In line with the bank's strategy to increase its portfolio and its business in Micro and SME segments, the Bank signed an agreement with the Kosovo Credit Guarantee Fund (“KCGF”) for the partial coverage of loans to MSME customers (Micro, Small and Medium Enterprises) disbursed by BPB. This fund or this credit guarantee is provided to facilitate the lending growth by the bank for MFIs in Kosovo, by improving the conditions and increasing the volume of loans in MSME-s.

In August 2016, the bank entered into the first contract worth EUR 1.5 million with the KCGF. Given the constant growth, this fund was fully utilized, and in June 2017, the new agreement for additional EUR 1.5 million guarantees was signed, reaching the guaranteed value at EUR 3 million.

During 2017, the bank continued to maintain its relations with different International Financial Institutions (EBRD, EFSE, IFC, and Blue ORCHARD Finance Ltd), where it has also received a credit line from EFSE in the amount of 1.5 EUR million. During 2017, the Bank also implemented a Technical Assistance from EFSE, which was mainly dedicated to the Risk Management Department. Through this assistance, all existing documents have been reviewed, new documents have been created for some areas of risk, new and existing processes have been revised and advanced, and various trainings have been organized for risk and business staff, addressing the process lending, financial analysis and arrears management.

The bank has enhanced the lending process by developing a software for loan applications management. The development has been divided in three phases with the objective to cover the whole life of loans from application to liquidation. The first phase or module has been developed and during 2017 was fully functionalized. This module has enabled the automation and digitalizing of the lending process, which has increased the speed of approval and at the same time has increased the quality, quantity, availability and access to information for clients. This development has also enabled advanced multi level analysis and full control of lending process to the ultimate detail.

During 2017, has also started the second phase of the development of the application which has the objective to cover the Monitoring process. The concept idea has been introduced and development of the software is taking place. This module will cover the monitoring of financial exposures and will serve as an early warning system not only to manage and retain credited clients but also to prevent and foresee deteriorations of financial conditions of the clients.

In following months the third phase of development will take place with the objective to cover the arrears management and collection. This module will be developed to support the process of arrears management and collection by providing structured management of data, correspondences, alerts and notifications.

By developing these three main modules, all the data related to the loans and loan clients will be available in one place, structured and interrelated. This will enable a holistic approach in credit risk management, monitoring and control.

In addition to the growth of the loan portfolio and the reduction of large exposures, the bank has continued with the further improvement of credit quality, in line with the trend of loans improvement at the level of the banking industry. Regarding the loan quality indicator – Non-performing loans (NPL), while in 2016 it was 4.94%, in 2017 this indicator was improved to 2.97% and was better than the average of the banking industry of 3.10%. There were also improvements in other categories of loans, problematic loans (C, D, E) and overdue loans (B, C, D, E).

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

b) Credit risk (continued)

Management of credit risk (continued)

Regarding the improvement of loan quality, the bank has strengthened the processes of managing the arrears and has increased the activities and commitments, which have resulted in recoveries of previously written off loans that generaly offset the effect of provision charges during the year. In this regard, during 2017, the bank has revised and extended contracts with two outsource debt management companies, especially for old loans in Loss and Write off categories, mainly for the amounts up to EUR 10 thousand.

The Bank reviews all credit exposures on a regular basis, while the classification and reporting of loans is performed on a monthly basis in accordance with the requirements of the Central Bank.

Credit exposures above EUR 50,000 are reviewed quarterly, and monitored biannualy. Exposures below EUR 50,000 are monitored on a yearly basis and include analyzing the client's financial position, including analyzing the state of collateral, exposures to other banks, and other factors that may affect the borrower's financial performance.

During 2017, the forms of monitoring were modified and improved, and new mechanisms were created in order to obtain relevant information on time. At the same time, the automation and digitalization of monitoring has continued, which will be finalized in the Bleta application.

(Amounts in thousands of EUR, unless otherwise stated)

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

b) Credit risk (continued)

Analysis of credit quality

The table below represents a worst case scenario of credit risk exposure of the Bank at 31 December 2017 and 2016, 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.

	Cash and balances with banks and CBK		Investments (AFS)		Loans and advances to customers		Other financial assets		Financial guarantees	
	2017	**2016**	**2017**	**2016**	**2017**	**2016**	**2017**	**2016**	**2017**	**2016**
Maximum exposure to credit risk										
Carrying amount	51,831	39,939	17,152	18,267	132,551	103,149	143	237	-	-
Amount committed/guaranteed	-	-	-	-		-	-	-	7,203	7,841
	51,831	**39,939**	**17,152**	**18,267**	**132,551**	**103,149**	**143**	**237**	**7,203**	**7,841**
At amortised cost										
Neither past due nor impaired	51,831	39,939	17,152	18,267	118,804	89,017	143	237	-	-
Past due but not impaired	-	-	-	-	12,493	12,490	-	-	-	-
Individually impaired	-	-	-	-	5,248	6,309	-	-	-	-
Total	**51,831**	**39,939**	**17,152**	**18,267**	**136,545**	**107,816**	**143**	**237**	**-**	**-**
Allowance for impairment (individual and collective)	-	-	-	-	(3,994)	(4,667)	-	-	-	-
Net carrying amount	**51,831**	**39,939**	**17,152**	**18,267**	**132,551**	**103,149**	**143**	**237**	**-**	**-**
Off balance: maximum exposure										
Credit commitments: Low - fair risk	-	-	-	-	-	-	-	-	5,899	5,615
Financial guarantees: Low - fair risk	-	-	-	-	-	-	-	-	1,304	2,226
Total committed/guaranteed	-	-	-	-	-	-	-	-	**7,203**	**7,841**
Provisions recognised as liabilities	-	-	-	-	-	-	-	-	(29)	(58)
Total exposure	-	-	-	-	-	-	-	-	**7,174**	**7,783**

(Amounts in thousands of EUR, unless otherwise stated)

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

b) Credit risk (continued)

Analysis of credit quality (continued)

	2017			2016		
Loans and advances to customers	**Retail**	**Corporate**	**Total Loans**	**Retail**	**Corporate**	**Total Loans**
Total gross amount	55,571	80,974	136,545	41,628	66,188	107,816
Allowance for impairment (individual and collective)	(315)	(3,679)	(3,994)	(717)	(3,950)	(4,667)
Net carrying amount	**55,256**	**77,295**	**132,551**	**40,911**	**62,238**	**103,149**
At amortised cost						
Neither past due nor impaired	53,976	64,828	118,804	39,772	49,245	89,017
Past due but not impaired	1,522	10,971	12,493	1,726	10,764	12,490
Individually impaired	73	5,175	5,248	130	6,179	6,309
Total Gross	**55,571**	**80,974**	**136,545**	**41,628**	**66,188**	**107,816**
Less: allowance for individually impaired loans	(26)	(2,098)	(2,124)	(75)	(2,738)	(2,813)
Less: allowance for collectively impaired loans	(289)	(1,581)	(1,870)	(642)	(1,212)	(1,854)
Total Allowance for impairment	**(315)**	**(3,679)**	**(3,994)**	**(717)**	**(3,950)**	**(4,667)**
Loans with renegotiated terms						
Carrying amount	164	6,026	6,190	292	6,127	6,419
From which: Impaired	26	5,000	5,026	110	4,497	4,607
Allowance for impairment	8	2,765	2,773	90	3,030	3,120
Net carrying amount	**156**	**3,261**	**3,417**	**202**	**3,097**	**3,299**
Neither past due nor impaired	53,976	64,828	118,804	39,772	49,245	89,017
Past due but not impaired						
Past due 0-30 days	1,074	9,062	10,136	983	8,954	9,937
Past due 31 - 90 days	255	1,468	1,723	239	856	1,095
Past due 91 – 180 days	72	159	231	106	88	194
Past due over 180 days	121	282	403	398	866	1,264
	1,522	**10,971**	**12,493**	**1,726**	**10,764**	**12,490**
Individually impaired						
Past due 0 – 30 days	60	1,017	1,077	-	947	947
Past due 31 - 90 days	-	993	993	-	2,330	2,330
Past due 91 – 180 days	-	1,890	1,890	80	1,683	1,763
Past due over 180 days	13	1,275	1,288	50	1,219	1,269
	73	**5,175**	**5,248**	**130**	**6,179**	**6,309**

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

b) Credit risk (continued)

Analysis of credit quality (continued)

Impaired loans

Impaired loans are loans for which the Bank determines that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the loan. These loans are graded A to E in the Bank's internal credit risk grading system where A is Standard while E is Loss. 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 50 thousand (2016: EUR 50 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 2017 is EUR 1,216 thousand (2016: EUR 578 thousand).

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 I Regulatory Capital.

(Amounts in thousands of EUR, unless otherwise stated)

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

b) Credit risk (continued)

Analysis of credit quality (continued)

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:

	2017	2016
A+ to A-	1,492	2,252
BBB+ to B-	767	1,868
Not rated	7,043	3,428
At 31 December	**9,302**	**7,548**

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.

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 and on subsequent valuations, when applicable. 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 financial assets is shown below:

Loans and advances to customers	Maximum exposure to credit risk	Property	Cash Collateral	Equipment	Total collateral used	Surplus collateral	Net uncollaterized exposure
31 December 2017	136,545	240,564	5,666	57,869	93,114	(197,133)	43,431
31 December 2016	107,816	231,244	3,905	51,130	77,927	(178,463)	28,889

(Amounts in thousands of EUR, unless otherwise stated)

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

b) Credit risk (continued)

Concentration of credit risk

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:

	Cash and balances with Banks and CBK		Loans and advances to banks		Available-for-sale financial assets		Loans and advances to customers		Other financial assets		Financial guarantees	
	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016
Concentration by sector												
Corporate	-	-	-	-	-	-	77,295	62,238	-	-	7,203	7,841
Banks	51,831	39,939	1,450	600	17,152	18,267	-	-	-	-	-	-
Retail	-	-	-	-	-	-	55,256	40,911	143	237	-	-
Total	**51,831**	**39,939**	**1,450**	**600**	**17,152**	**18,267**	**132,551**	**103,149**	**143**	**237**	**7,203**	**7,841**
Concentration by location												
EU countries	2,158	3,519	100	600	-	-	-	-	-	-	-	-
Republic of Kosovo	49,160	35,426	1,350	-	17,152	18,267	132,551	103,149	143	237	7,203	7,841
Other countries	513	994	-	-	-	-	-	-	-	-	-	-
Total	**51,831**	**39,939**	**1,450**	**600**	**17,152**	**18,267**	**132,551**	**103,149**	**143**	**237**	**7,203**	**7,841**

(Amounts in thousands of EUR, unless otherwise stated)

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

c) Market risk

Market risk is the risk that changes in market prices, such as interest rates, equity prices, exchange rates will affect 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 optimizing the return on risk. The relevant market risks that the bank deals with are foreign currency risk and interest rate risk in the banking book and these risk are managed in accordance with their respective policies.

Interest rate risk

Interest rate risk is the risk of suffering losses due to the fluctuation of interest rates in financial instruments and is mainly as a result of maturity mismatches between assets and liabilities. Consequently, this can increase bank's funding costs compared to the return obtained from assets which might remain unchanged and thus, potentially decrease the interest margin.

In order to mitigate this risk, the bank measures and monitors interest rate risk based on repricing gap analysis between assets and liabilities in order to limit its exposure to this risk and ensure compliance with CBK regulation on Interest rate risk on banking book which was enforced since 1st of January 2017. For the purpose of measuring interest rate risk, bank's assets and liabilities are distributed within time buckets according to their maturities and then maturity/ repricing gaps are analyzed. The interest rate gap is supplemented by monitoring the sensitivity of the Bank's financial assets and liabilities to various standard and non-standard interest rate scenarios. These scenarios aim to simulate interest rate fluctuations in order to measure the impact on banks financial result and capital. Standard scenarios include a 2% parallel shift in the yield curve as required by the CBK regulation.

The results from these scenarios are reported on a monthly basis to bank's Liquidity Risk Management Committee ("LRMC") and on quarterly basis to Risk Committee on board level. As a result, bank's exposure to interest rate risk remains in line with bank's risk profile and within internal and regulatory limits as set by the CBK.

The average effective yields of significant categories of financial assets and liabilities of the Bank as at 31 December 2017 and 2016 are as follows:

	USD		*EUR*	
Assets	**2017**	**2016**	**2017**	**2016**
Cash at banks	0.65%	0.65%	-	-
Loans and advances to banks	1.34%	-	0.93%	-
Loans to customers	-	-	8.45%	9.29%
Available-for-sale financial assets	-	-	1.69%	1.03%
Liabilities				
Due to customers	-	0.04%	1.41%	1.39%
Subordinated debt	-	-	10.04%	10.04%
Borrowings	-	0.65%	3.50%	3.50%

(Amounts in thousands of EUR, unless otherwise stated)

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

c) Market 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:

2017	**up to 1 Year scenarios**		**over 1 Year scenarios**	
	100 bp Increase	100 bp Decrease	100 bp Increase	100 bp Decrease
Estimated Profit (loss) effect	(571)	571	686	(686)
2016	**up to 1 Year scenarios**		**over 1 Year scenarios**	
	100 bp Increase	100 bp Decrease	100 bp Increase	100 bp Decrease
Estimated Profit (loss) effect	(493)	493	555	(555)

Effect on other comprehensive income	**up to 1 Year scenarios**		**over 1 Year scenarios**	
	10 bp Increase	10 bp Decrease	10 bp Increase	10 bp Decrease
2017: Estimated Available for sale effect	5	(5)	56	(56)
2017: Total effect on equity	(566)	566	742	(742)

Based on the analysis above if interest rates increses with 10 basis point, fair value decreases with EUR 61 thousand.

The effect of interest rate risk on equity is similar to that on Profit and Loss.

(Amounts in thousands of EUR, unless otherwise stated)

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

c) Market risk (continued)

The following table shows the interest bearing and non-interest bearing financial instruments by repricing date.

31 December 2017		Up to 1 month	1-3 Month	3-6 Month	6-12 Month	Over 1 year	Total
Assets							
Cash on hand and at banks							
Non-interest bearing		13,516	-	-	-	-	**13,516**
Interest bearing	*Fixed*	4,317	-	-	-	-	**4,317**
Balances with CBK							
Non-interest bearing		33,998	-	-	-	-	**33,998**
Loans and advances to banks							
Interest bearing	*Fixed*	-	-	-	1,450	-	**1,450**
Investment securities							
Interest bearing	*Fixed*	50	-	340	4,983	11,779	**17,152**
Loans to customers							
Interest bearing	*Fixed*	5,358	6,459	13,039	24,572	83,123	**132,551**
Other financial assets							
Non-interest bearing		143	-	-	-	-	**143**
Total		**57,382**	**6,459**	**13,379**	**31,005**	**94,902**	**203,127**
Liabilities							
Deposits from customers							
Interest bearing	*Fixed*	18,834	4,628	9,110	50,122	23,605	**106,299**
Non-interest bearing		71,481	-	-	-	-	**71,481**
Subordinated debt							
Interest bearing	*Fixed*	-	-	-	40	800	**840**
Borrowings							
Interest bearing	*Variable*	-	1,114	-	1,114	1,915	**4,143**
Other liabilities							
Non-interest bearing		1,673	-	-	-	-	**1,673**
Total		**91,988**	**5,742**	**9,110**	**51,276**	**26,320**	**184,436**
Gap		**(34,606)**	**717**	**4,269**	**(20,271)**	**68,582**	**18,691**
Cumulative gap		**(34,606)**	**(33,889)**	**(29,620)**	**(49,891)**	**18,691**	

(Amounts in thousands of EUR, unless otherwise stated)

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

c) Market risk (continued)

31 December 2016		Up to 1 month	1-3 Month	3-6 Month	6-12 Month	Over 1 year	Total
Assets							
Cash on hand and at banks							
Non-interest bearing		12,691	-	-	-	-	**12,691**
Balances with CBK							
Non-interest bearing		27,248	-	-	-	-	**27,248**
Loans and advances to banks							
Interest bearing	*Fixed*		350	-	200	50	**600**
Investment securities							
Interest bearing	*Fixed*	-	70	3,743	7,128	7,326	**18,267**
Loans to customers							
Interest bearing	*Fixed*	4,282	6,616	8,761	17,724	65,766	**103,149**
Other financial assets							
Non-interest bearing		237	-	-	-	-	**237**
Total		**44,458**	**7,036**	**12,504**	**25,052**	**73,142**	**162,192**
Liabilities							
Deposits from customers							
Interest bearing	*Fixed*	16,371	3,424	10,512	37,520	12,557	**80,384**
Non-interest bearing		60,214	-	-	-	-	**60,214**
Subordinated debt							
Interest bearing	*Fixed*	-	4	41	-	1,800	**1,845**
Borrowings							
Interest bearing	*Variable*	-	45	48	800	3,355	**4,248**
Other liabilities							
Non-interest bearing		1,346	-	-	-	-	**1,346**
Total		**77,931**	**3,473**	**10,601**	**38,320**	**17,712**	**148,037**
Gap		**(33,473)**	**3,563**	**1,903**	**(13,268)**	**55,430**	**14,155**
Cumulative gap		**(33,473)**	**(29,910)**	**(28,007)**	**(41,275)**	**14,155**	

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

c) Market risk (continued)

Exposure to currency risk

Currency risk is the risk of potential losses from open position in foreign currencies due to fluctuations in exchange rates. 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 bank manages and monitors currency risk against the limits set in its risk policy and in CBK regulation on Foreign Exchange Risk.

Exposure to currency risk is discussed and reported on monthly basis to liquidity and market risk committee.The foreign currencies the Bank deals with, are predominantly United States Dollars (USD), Swiss Franc (CHF) and Great Britain Pounds (GBP). In regards to GBP the bank has stopped accepting this currency, however the remaining balance is managed closely. The rates used for translation as at 31 December 2017 and 2016 are as follows:

	2017	2016
CURRENCY	**EUR**	**EUR**
1 USD	0.8338	0.9487
1 CHF	0.8546	0.9312
1 GBP	1.1271	1.1680

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

in thousands of EUR	**USD**		**CHF**		**GBP**	
	2017	**2016**	**2017**	**2016**	**2017**	**2016**
Sensitivity rates	5%	5%	5%	5%	5%	5%
Profit or loss						
+5% of Euro	2.97	10.85	2.02	51.60	0.24	7.3
- 5% of Euro	(2.97)	(10.85)	(2.02)	(51.60)	(0.24)	(7.3)

The Bank's exposure to foreign currency risk is as follows:

All amounts are translated in thousands of EUR

31 December 2017	**EUR**	**USD**	**CHF**	**GBP**	**Total**
Financial Assets					
Cash on hand and at banks	13,451	1,657	2,720	5	**17,833**
Balances with CBK	33,998	**-**	**-**	**-**	**33,998**
Available-for-sale investments	17,152	**-**	**-**	**-**	**17,152**
Loans and advances to banks	1,450	-	-	-	**1,450**
Loans and advances to customers	132,551	-	-	-	**132,551**
Other financial assets	143				**143**
Total financial assets	**198,745**	**1,657**	**2,720**	**5**	**203,127**
Financial Liabilities					
Due to customers	173,502	1,598	2,680	-	**177,780**
Subordinated debt	840	**-**	**-**	**-**	**840**
Borrowings	4,143	**-**	**-**	**-**	**4,143**
Other liabilities	1,673	**-**	**-**	**-**	**1,673**
Total financial liabilities	**180,158**	**1,598**	**2,680**	**-**	**184,436**
Net foreign currency position	**18,587**	**59**	**40**	**5**	**18,691**

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

c) Market risk (continued)

All amounts are translated in thousands of EUR

31 December 2016	EUR	USD	CHF	GBP	Total
Financial Assets					
Cash on hand and at banks	7,225	1,785	3,565	116	**12,691**
Balances with CBK	27,248	-	-	-	**27,248**
Loans and advances to banks	600	-	-	-	**600**
Loans and advances to customers	103,149	-	-	-	**103,149**
Available for Sale investments	18,267	-	-	-	**18,267**
Other financial assets	237	-	-	-	**237**
Total financial assets	**156,726**	**1,785**	**3,565**	**116**	**162,192**
Financial Liabilities					
Due to customers	136,953	1,030	2,592	23	**140,598**
Subordinated debt	1,845	-	-	-	**1,845**
Other liabilities	4,248	-	-	-	**4,248**
Total financial liabilities	1,346	-	-	-	**1,346**
Total financial liabilities	**144,392**	**1,030**	**2,592**	**23**	**148,037**
Net foreign currency position	**12,334**	**755**	**973**	**93**	**14,155**

d) Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulties in meeting its obligations as they come due and to meet any unexpected demands for funds by its depositors or other creditors. Moreover, liquidity risk includes also the risk that the bank will be unable to fund the growth of assets.

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. For this purpose, on daily basis the bank monitors its liquidity position and market conditions. Moreover, continuously 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.

In order to ensure an effective management of liquidity risk, and ensure that no liquidity shortfalls occur, the Bank keeps its deposit base diversified. As such, the bank aims to raise funds using a broad range of instruments such as customers' deposits, or funding from IFIs which will ensure that funding base remains stable.

In addition to daily reporting, the bank monitors liquidity risk on monthly basis also. This monitoring includes the liquidity position under normal circumstances and also under stress tests. The results are discussed in Liquidity Risk Management Committee ("LRMC").

Furthermore, the bank has also a liquidity contingency plan which enables the effective management of liquidity in case of unexpected circumstances.

(Amounts in thousands of EUR, unless otherwise stated)

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

d) Liquidity risk (continued)

Management of liquidity risk

The bank measures liquidity risk using liquidity gap analysis which represents the residual maturities of financial assets and liabilities. The residual maturity is the period between the contractual due date of the asset/ liability and the balance sheet date.

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

31 December 2017	Up to 1 Month	1 to 3 Months	3 to 6 Months	6 to 12 Months	Over 12 Months	Total
Financial Assets						
Cash on hand and at banks	17,833	-	-	-	-	**17,833**
Balances with CBK	33,998	-	-	-	-	**33,998**
Loans and advances to banks	-	-	-	1,450	-	**1,450**
Loans and advances to customers	5,358	6,459	13,039	24,572	83,123	**132,551**
Available-for-sale financial assets	50	-	340	4,983	11,779	**17,152**
Other financial assets	143	-	-	-	-	**143**
Total	**57,382**	**6,459**	**13,379**	**31,005**	**94,902**	**203,127**
Financial Liabilities						
Due to customers	90,315	4,628	9,110	50,122	23,605	**177,780**
Subordinated debt	-	-	-	40	800	**840**
Borrowings	-	1,114	-	1,114	1,915	**4,143**
Other liabilities	1,673	-	-	-	-	**1,673**
Guarantees issued	1,275	-	-	-	-	**1,275**
Unused credit commitments	5,899	-	-	-	-	**5,899**
Total	**99,162**	**5,742**	**9,110**	**51,276**	**26,320**	**191,610**
Liquidity gap	**(41,780)**	**717**	**4,269**	**(20,271)**	**68,582**	**11,517**

31 December 2016	Up to 1 Month	1 to 3 Months	3 to 6 Months	6 to 12 Months	Over 12 Months	Total
Financial Assets						
Cash on hand and at banks	12,691	-	-	-	-	**12,691**
Balances with CBK	27,248	-	-	-	-	**27,248**
Loans and advances to banks	-	350	-	200	50	**600**
Loans and advances to customers	4,282	6,616	8,761	17,724	65,766	**103,149**
Available for sale investments	-	70	3,799	7,016	7,382	**18,267**
Other financial assets	237	-	-	-	-	**237**
Total	**44,458**	**7,036**	**12,560**	**24,940**	**73,198**	**162,192**
Financial Liabilities						
Due to customers	76,585	3,424	10,512	37,520	12,557	**140,598**
Subordinated debt	-	4	41	-	1,800	**1,845**
Subordinated debt	-	45	48	800	3,355	**4,248**
Other liabilities	1,346	-	-	-	-	**1,346**
Contingent liabilities from guarantees	2,168	-	-	-	-	**2,168**
Unused credit commitments	5,615	-	-	-	-	**5,615**
Total	**85,714**	**3,473**	**10,601**	**38,320**	**17,712**	**155,820**
Liquidity gap	**(41,256)**	**3,563**	**1,959**	**(13,380)**	**55,486**	**6,372**

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

e) Operational risk

In line with CBK regulation, operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people, systems, or external events. This definition includes legal risk, but excludes strategic and reputational risk. In order to ensure effective management of operational risk the bank has implemented an operational risk framework which includes policies and procedures, techniques and tools for identifying, assessing, mitigating/ controlling and monitoring operational risk.

In order to improve and increase the effectiveness of internal controls in bank's processes and record all operational risk losses, the bank has established a "loss event database" where all events that cause operational losses or potential risks that may cause losses are registered. Limits and reporting lines of these losses are determined in operational risk management policy. Furthermore, operational risk procedure describes in details the steps that the bank undertakes from collected information on operational risk loss event database.

This database is considered to be the best source of information for the development of models for measuring bank's exposure to operational risk as it offers information on the causes of loss. Furthermore, through the information gathered from this database corrective or preventive measures are set in order to mitigate/ control this risk.

Yearly assessment for different processes in bank is part of bank's operational risk management framework. Through this assessment the bank collects useful information for determining bank's operational risk profile and assesses the risks the bank is exposed to, including the degree of control implementation. This enables the improvement of control processes through different measures, thus reducing the impact of losses from operational risk.

Effective management of operational risk means knowing bank's position and risk profile. Therefore, for this purpose, the bank is using Key Risk Indicators (KRIs) to monitor drivers of exposures associated with key risks. These indicators are monitored on regular (monthly/quarterly) basis in order to facilitate operational risk management by providing early warning signals for the changes that may be indicative of risk concerns.

In establishing an effective management of operational risk, the bank has undertaken different activities related to increasing risk awareness mainly through trainings, which are provided for all bank staff on an annual basis. These trainings aim to enhance the knowledge regarding operational risk management through discussion of different scenarios on previous operational risk events. Furthermore, the trainings address the channels through which operational risk events are to be monitored and reported.

In addition, the bank has implemented a process for ensuring that changes in products, services or processes (existing or new) go through risk review and approval. This will ensure that the operational risk that comes from processes, products or new services in the bank is monitored and dealt with promptly.

The bank calculates the capital charge for operational risk using the Basic Indicator Approach (BIA) as defined by the Central Bank regulation on Operational risk management.

(Amounts in thousands of EUR, unless otherwise stated)

26. FINANCIAL RISK MANAGEMENT (CONTINUED)

f) 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 Bank's overall strategy remains unchanged from 2015.

The equity structure of the Bank comprises share capital, reserves and retained earnings. The Bank's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The impact of the level of capital on shareholder return is also recognised and the Bank recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

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%, 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.

	2017	**2016**
Total risk weighted assets	126,575	99,926
Total risk weighted off balance exposures	713	1,398
Total risk weighted assets for operational risk	12,747	10,545
Total	**140,035**	**111,869**
Regulatory capital (Total Capital)	21,617	16,526
Capital adequacy ratio (Total Capital)	**15.44%**	**14.77%**

(Amounts in thousands of EUR, unless otherwise stated)

27. RELATED PARTY TRANSACTIONS

Parties are considered to be related if one of them has the ability to control the other or exercise significant influence over the one making financial and operating decisions. Ultimate controlling parties are shareholders listed in the Note 24 shareholders equity and reserves.

In considering each possible related party relationship, attention is directed to the substance of the relationship and not merely to the legal form.

A summary of related party balances at the end of year are as follows:

	31 December 2017		31 December 2016	
Assets: *Loans outstanding at end of year with shareholders and key management*	CBK Rating*		CBK Rating*	
Enrad-Ex Newco Jugo Term	A	1,542	A	1,553
Eng Office	A	501	A	613
Ismet Sylejmani (Vatani shpk)	A	100	A	95
Uniprojekt	A	113	A	187
Naser Aliu-Uniprojekt	A	17	A	12
Besnik Vrella- Uniprojekt	A	9	A	13
Agim Bilalli-Uniprojekt	A	12	A	3
Sokol Krasniqi	A	-	A	3
Brymako	A	12	A	21
Ahmet Arifi	A	1	A	16
Naim Abazi (Medianam shpk)	A	205	A	167
Other shareholders and management	A	110	A	98
Total		**2,622**		**2,781**
Guarantees and letters of credit with shareholders	A	11	A	40
Loans and advances to Banka Di Cividale		**-**		**-**

*) A: Standard category; B: Watch category; C: Substandard category

Loans to related parties are given at commercial terms.

	2017	**2016**
Loans to shareholders, gross	2,512	2,683
Allowance for impairment	(4)	(12)
Total Loans to shareholders, net	**2,508**	**2,671**
Exposure covered with cash collateral	(2,026)	(2,525)
Net exposure to shareholders	**482**	**146**

	2017	**2016**
Loans to management and BoD members, gross	110	98
Loans to management, net	**110**	**98**
Cash collateral	(48)	(69)
Net exposure to management	**62**	**29**

(Amounts in thousands of EUR, unless otherwise stated)

27. RELATED PARTY TRANSACTIONS (CONTINUED)

	31 December 2017	31 December 2016
Liabilities:		
Customer accounts with shareholders		
Caffe group n.t.sh	26	29
Mejdi Rexhepi	307	227
Enrad	3	-
Rrustem Aliaj	72	20
Malesia Reisen	42	44
Frutex sh.p.k	202	40
Shaqir Palushi	132	3
Naser Aliu - Uniprojekt	4	-
Besnik Vrella- Uniprojekt	5	15
Ahmet Arifi	1	-
Vatani Sh.p.k	1	1
Moneta sh.p.k	1	227
Nazmi Viça	20	-
Sokol Krasniqi	2	3
Medianam Sh.p.k	37	1
ENG Office	8	-
Other shareholders and management	157	62
Total	**1,020**	**672**
Borrowing from EBRD/KOSEP	1,000	2,000
Total liabilities	**2,020**	**2,672**

Following are the transactions made with related parties during the year.

	2017	2016
Income		
Interest income from loans and advanes	56	117
Total interest income	**56**	**117**
Expenses		
Interest expenses for subordinated debt from EBRD	69	112
Key management compensation	350	342
Board of directors compensation	42	38
Total expenses	**461**	**492**

28. SUBSEQUENT EVENTS

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