



ANNUAL OPERATING REPORT FOR 2016

Belgrade, February 2017

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I DEVELOPMENT, ORGANISATIONAL STRUCTURE AND BUSINESS ACTIVITIES

1. ESTABLISHMENT

HALKBANK a.d. Belgrade operates in the Republic of Serbia since 2015 when Türkiye Halk Bankası A.S. has become a major owner of Cacanska banka which has been operating since 1956.

The Bank is registered in the Business Registers Agency of the Republic of Serbia under the number BD 54244 dated 13 September 2005.

Under the name of Halkbank a.d. Beograd Bank has been operating since 22 October 2015 when the change has been registered in the Business Registers Agency BD 89155/2015.

2. ORGANISATION OF OPERATIONS

HALKBANK a.d. Belgrade is a universal bank which provides all banking services for entrepreneurs and retail clients. The Bank encourages and finances the growth and development of the domestic economy, but is also a safe place for saving deposits for all clients. The primary goal is to create products that will completely satisfy all customer's expectations.

The Bank is registered in the Republic of Serbia to provide payment operations and credit and deposit operations in the country and abroad and it operates in compliance with the Law on Banks.

HALKBANK a.d. Belgrade successfully spreads business network and client base. Today the Bank offers services and product through business network of 20 branches, 8 sub-branches and 4 cash desks. As at 31 December 2016 the Bank was comprised of 5 branches in Belgrade, 2 branches in Čačak and 13 branches located in the towns of Jagodina, Gornji Milanovac, Kraljevo, Užice, Kragujevac, Kruševac, Aranđelovac, Valjevo, Šabac, Niš, Novi Sad, Pančevo and Novi Pazar and 8 sub-branches in Čačak, Paraćin, Požega, Topola, Ivanjica, Vrnjačka Banja, Leskovac and Mladenovac.

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3. BASIC OPERATING RATIOS

Income Statement (in RSD 000)	31 December 2015	31 December 2016	Plan for 2016
Net interest income	1,179,131	1,344,962	1,312,500
Net fee and commission income	575,732	576,556	600,000
Profit / Loss before taxation	(187,811)	136,080	13,375
Balance Sheet (in RSD 000)	31 December 2015	31 December 2016	Plan for 2016
Loans and advances to customers	19,099,192	23,962,060	24,375,000
Customers deposits	15,494,728	19,226,690	18,375,000
Equity	5,739,809	5,883,585	5,953,500
Balance sheet assets	31,934,812	34,985,811	36,963,625
Off-balance sheet items	52,289,482	56,934,323	54,060,000
Basic financial ratios	31 December 2015	31 December 2016	Plan for 2016
Operating expenses / Net interest, fee and commission income	66.77%	74.21%	75.00%
Capital adequacy	15.79%	15.64%	17.83%
Number of employees	31 December 2015	31 December 2016	Plan for 2016
	377	411	450
Exchange rate	31 December 2015	31 December 2016	Plan for 2016
RSD / EUR	121.6261	123.4723	125
Liquidity ratios	31 December 2015	31 December 2016	Plan for 2016.
Average liquidity ratio	2.55 _{1.70}		1.50
Average liquid asset ratio	28.78%	27.62%	24.00%

HALKBANK a.d. Belgrade made a positive operating result in the 2016 amounting to RSD 136,080 thousand.

Balance sheet assets amounted to RSD 34,985,811 thousand as at 31 December 2016, which is increase of 9.55% compared to the end of 2015.

Off-balance sheet assets as at 31 December 2016 came to RSD 56,934,323 thousand, which is increase of 8.88% compared to the end of 2015.

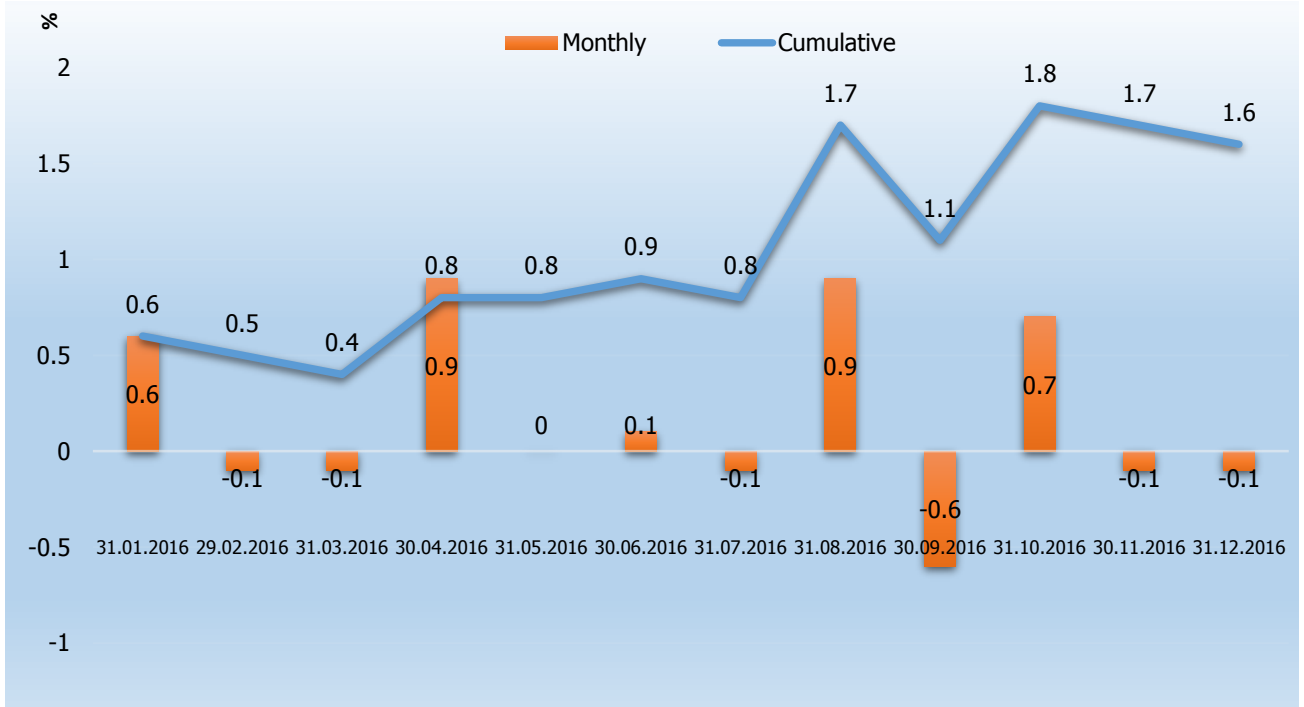
Commercial and retail loans as at 31 December 2016 increased by 25.46% compared to the end of 2015, while commercial and retail deposits increased by 24.09%.

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II FINANCIAL POSITION AND OPERATING RESULTS

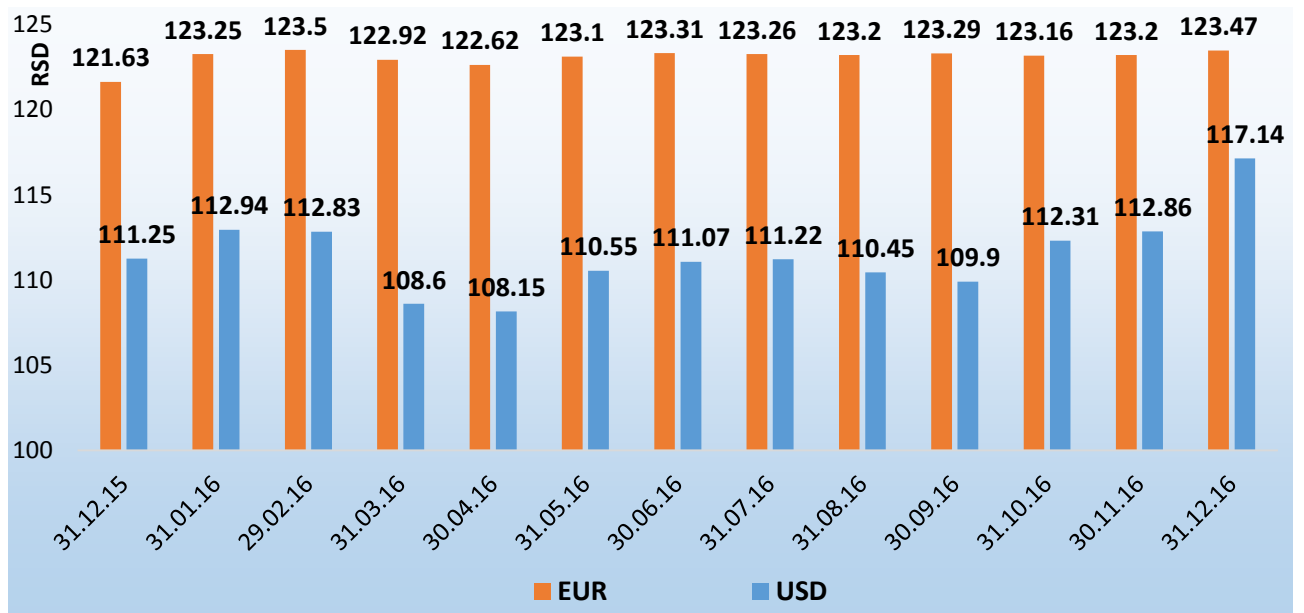
1. MACROECONOMIC ENVIRONMENT

Consumer prices growth in Serbia in 2016



During 2016 the growth of consumer prices equaled cumulatively 1.60%. The highest monthly growth was in April and August and it was 0.90%.

FX trend during 2016

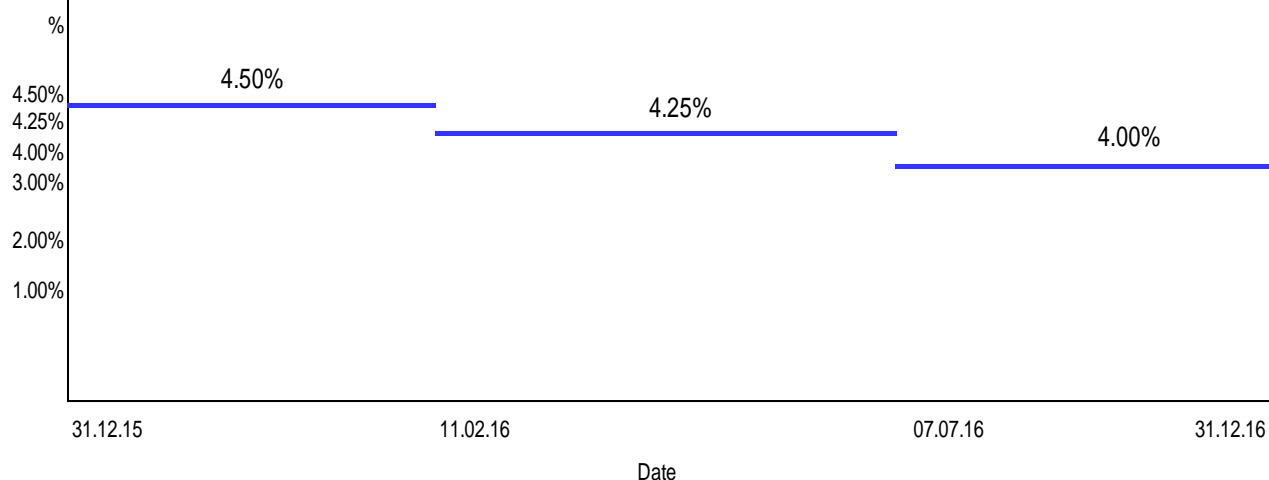


In the 2016 RSD depreciated against EUR by 1.51% and against USD by 5.29%.

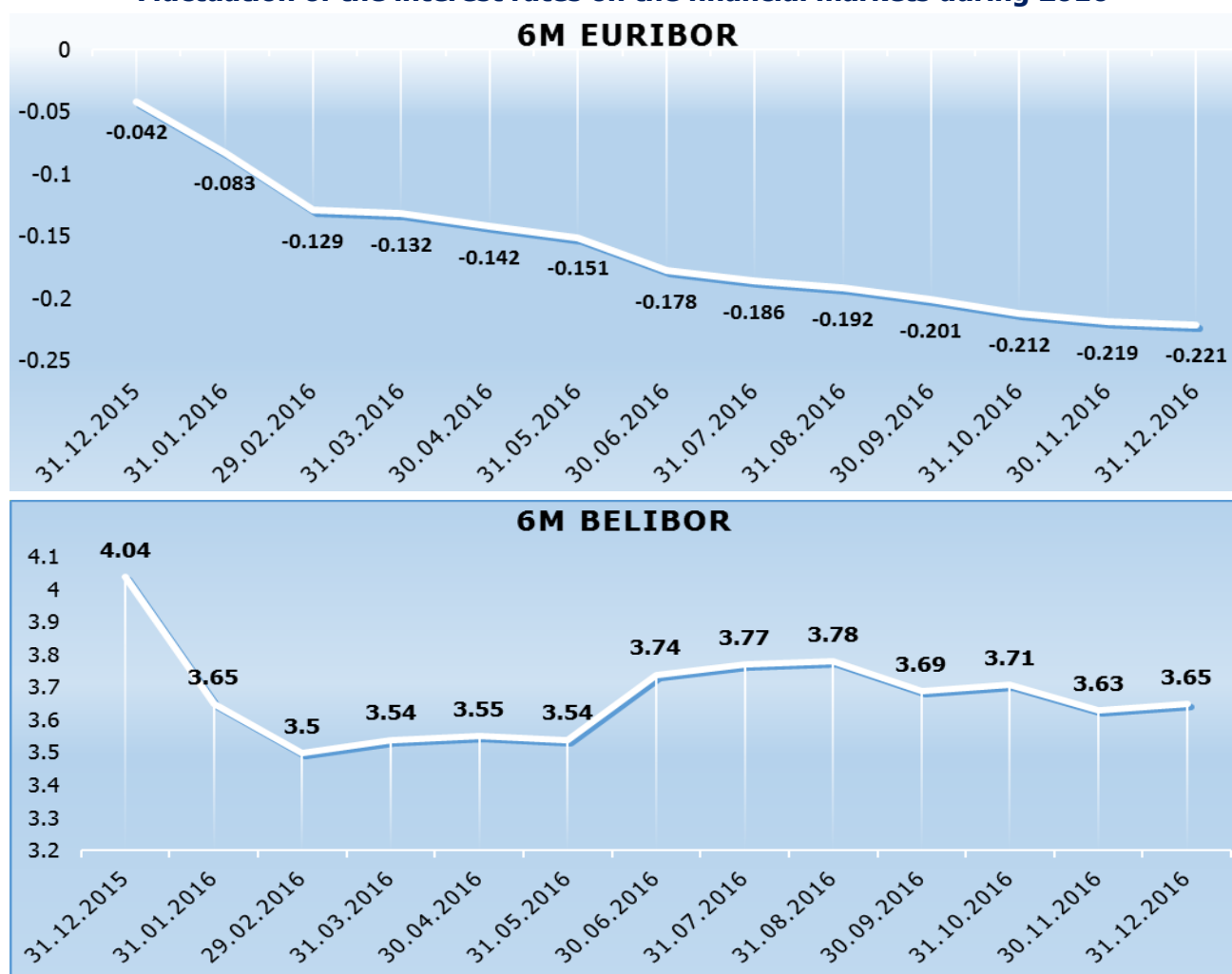
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Fluctuation of the NBS referent rate

During 2016 the Executive Board of National Bank of Serbia decreased reference rate two times, so



that the reference rate was reduced from 4.50% at the beginning of the year to 4.00% at the end of 2016.

Fluctuation of the interest rates on the financial markets during 2016

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2. IMPLEMENTATION OF BASIC OPERATING TARGETS

The targets set out in the Operating Policy for 2016 were implemented through the following activities:

1. In the 2016 the Bank opened 4 new branches – in Belgrade in Kalenić Street and in Milutina Milankovića 9e (in the new Headquarter building in New Belgrade), Branch in Pančevo and Branch in Novi Pazar. Also, in 2016 Sub-branch in Pivarska Street in Čačak became branch.
2. During the 2016 the Bank was successfully maintaining the average Liquidity Ratio and Liquid Assets Ratio above the planned values for 2016. Average Liquidity Ratio was 1.79 which is above plan according to which average value should not fall below 1.50. Also average Liquid Assets Ratio was 27.62% which is above the plan according which average value should not fall below 24%.
3. The Bank finished 2016 with a profit amounting to EUR 1,102 thousand, which is significantly higher than planned values for 2016.

Realized values regarding this objective are shown in following table:

Indicators	(in RSD thousand)	
	31 December 2016	Plan for 2016
Net interest and fees income	1,921,518	1,912,500
Net profit/losses on impairment of financial assets and credit risk-weighted off-balance sheet items	(389,289)	(450,000)
Operating costs (salaries, depreciation and other expenses)	(1,429,288)	(1,567,875)
Profit	136,080	13,375

4. Net loan portfolio increased in the amount of RSD 4,862,868 thousand, and realized 92.17% of planned annual growth of net loans in 2016.

5. Deposit potential at the end of 2016 increased by RSD 3,731,962 thousand comparing to the end of 2015. The deposits of the corporate clients increased by RSD 1,423,540 thousand and deposits of retail clients increased by RSD 2,308,422 thousand. In this way, the Bank realized 115.96% of the planned annual growth of corporate deposits and 139.68% of the planned annual growth of the retail deposits.

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3. BALANCE SHEET

As at 12 December 2016 the Bank's total assets came to RSD 34,985,811 thousand and account for a 9.55% increase to the end of 2015.

3.1 Assets

(in RSD thousand)

ASSETS	31 December 2015	31 December 2016	Plan for 31 December 2016
Cash, cash equivalents and assets held with the central bank	4,081,407	4,090,612	4,369,625
Pledged financial assets	584,834	90,000	-
Financial assets at fair value through income statement and held for trading	295,295	23,984	62,500
Financial assets available for sale	244,349	3,177,595	500,000
Financial assets held to maturity	3,449,188	1,353,325	4,000,000
Loans and receivables from banks and other financial organizations	3,057,235	1,018,760	2,264,375
Loans and receivables from clients	19,195,483	23,997,783	24,375,000
Intangible assets	28,085	73,976	235,375
Property, plant and equipment	628,570	818,446	779,000
Investment property	130,028	126,337	128,750
Deferred tax assets	62,393	62,393	62,500
Other assets	177,945	152,600	186,500
TOTAL ASSETS	31,934,812	34,985,811	36,963,625

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The following table presents the currency structure of assets:

Assets	31 December 2015	%	31 December 2016	%
Dinars	11,030,640	34.54%	12,893,942	36.85%
Foreign currency	20,904,172	65.46%	22,091,869	63.15%
Total:	31,934,812	100.00%	34,985,811	100.00%

3.1.1 Loans and receivables from clients

The structure of Balance Sheet item: 'Loans and receivables from clients' as at 31 December 2015 and 31 December 2016 is given in the following table:

(in RSD thousand)

Loans and receivables from clients	31 December 2015	31 December 2016	Plan for 2016	% of change
Total net loans:	19,099,192	23,962,060	24,375,000	25.46%
Corporate net loans (without NPL clients)	12,392,364	15,041,077	15,500,000	21.37%
Retail net loans (without NPL clients)	4,013,905	6,132,787	6,250,000	52.79%
NPL - net	2,692,923	2,788,196	2,625,000	3.54%
Receivables:	96,291	35,723	-	-62.90%
Receivables for accrued interest and fees under loans, deposits and other placements	96,291	35,723	-	-62.90%
Total loans and receivables from clients:	19,195,483	23,997,783	24,375,000	25.02%

The Bank's net loan portfolio consisting of corporate and retail loans increased during 2016 by 25.46%.

(in RSD thousand)

Net loans	Planned changes in 2016	Realized changes in 2016
Corporate net loans (without NPL clients)	3,107,636	2,648,713
Retail net loans (without NPL clients)	2,236,095	2,118,882
NPL - net	(67,923)	95,273
Total:	5,275,808	4,862,868

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In 2016 the Bank approved to corporate and retail clients RSD 16,727,048 thousand loans, of which RSD 4,164,831 thousand for loans up to one-year maturity and RSD 12,562,217 thousand to loans over one-year maturity.

-Gross loans and receivables from customers - Corporate

Gross corporate loans as at 31 December 2016 amounted to RSD 20,460,407 thousand with the following structure:

(in RSD thousand)

Loan type	Currency	31 December 2015	31 December 2016	% of change
Loans from the Bank's resources	RSD	3,121,736	3,543,383	13.51%
Loans from the Bank's resources-subsidies	RSD	527,625	23,430	-95.56%
Loans from the Bank's resources	EUR	9,465,679	11,684,941	23.45%
Loans - EBRD credit line	EUR	22,057	8,374	-62.03%
Loans to SMEs from the Revolving Credit Fund (EAR)	EUR	1,555,703	1,328,099	-14.63%
HIT loans from the EFSE credit line	EUR	747,858	346,709	-53.64%
Loans from the GGF credit line	EUR	25,611	11,164	-56.41%
Loans covered with EIF guarantee	EUR	200,419	46,533	-76.78%
HIT Energy loans from KfW facility	EUR	224,426	157,719	-29.72%
Loans from the EIB facility	EUR	3,608,236	2,901,172	-19.60%
Loans from the FMO facility	EUR	146,402	82,009	-43.98%
Investment loans from the Italian Government facility	EUR	86,768	26,462	-69.50%
Loans from the IFC facility	EUR	15,748	1,610	-89.78%
Demir-Halk Bank (Nederland) N.V.	EUR	-	298,803	100.00%
Total:		19,748,268	20,460,407	3.61%

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In third and fourth quarter of 2016, according to the Decision of Halkbank's Board of Directors and NBS Guidelines on implementation of IAS 39, the Bank has written-off RSD 2,042,043 thousands of gross corporate receivables that had 100% impairment. In 2016 the Bank had amended Accounting policies because of changes in regulations and practice introducing new definition of direct write-off and general debt release. In accordance to the Board of Directors Decisions the Bank has made direct write-off of receivables and moved it to off-balance sheet items. This does not relate to the Bank's waiver from the agreed obligations and legal rights arising from loans. All these loans were fully impaired.

- Gross loans and receivables from customers – Retail

The total gross retail placements including non-performing loans as at 31 December 2016 amounted to RSD 6,253,866 thousand with the following structure:

(in RSD thousand)

Type of loan	31 December 2015	31 December 2016	% of increase/decrease
Consumer loans – EE/RE - GGF	532,662	361,660	-32.10%
Consumer loans – vehicle purchase	60,413	31,609	-47.68%
Consumer loans – other purposes	133,971	326,756	143.90%
Cash loans	1,309,843	2,761,504	110.83%
Mortgage loans	1,893,575	2,530,638	33.64%
Receivables related to DinaCard credit card	16,090	10,265	-36.20%
Allowed overdraft	83,246	105,163	26.33%
Disallowed overdraft and due loan receivables	113,450	126,271	11.30%
Total:	4,143,250	6,253,866	50.94%

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3.2 Liabilities

Total liabilities as at 31 December 2016 came to RSD 34,985,811 thousand with the following structure:

(in RSD thousand)

LIABILITIES	31 December 2015	31 December 2016	Plan for 2016
Deposits and other liabilities to banks, other financial organizations and central bank	702,699	2,715,013	1,550,000
Deposits and other liabilities to other clients	23,373,380	26,101,052	27,918,125
Subordinated liabilities	1,851,741	-	1,250,000
Provisions	91,639	42,466	92,000
Other liabilities	175,544	243,695	200,000
Total liabilities	26,195,003	29,102,226	31,010,125
Share capital	4,248,483	4,248,483	4,248,483
Profit	-	138,153	13,375
Loss	(185,467)	-	-
Reserves	1,676,793	1,496,949	1,691,642
Total Capital	5,739,809	5,883,585	5,953,500
TOTAL LIABILITIES	31,934,812	34,985,811	36,963,625

In terms of currency structure, there was the following balance:

(in RSD thousand)

Liabilities	31 December 2015	%	31 December 2016	%
Dinars	10,958,796	34.32%	12,955,023	37.03%
Foreign currency	20,976,016	65.68%	22,030,788	62.97%
Total:	31,934,812	100.00%	34,985,811	100.00%

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3.2.1 Deposits and other liabilities to banks, other financial organizations and central bank

The structure of the item Deposits and other liabilities to banks, other financial organizations and central bank and a comparative analysis as at 31 December 2015 and 31 December 2016 is presented in the following table:

(in RSD thousand)

Item	31 December 2015	31 December 2016	% of change
Transaction and other deposits	246,477	1,715,327	595.94%
- transaction deposits	19,922	15,544	-21.98%
- other deposits	226,555	1,699,783	650.27%
Borrowed loans in foreign currency:	381,385	617,362	61.87%
- EBRD	81,663	-	-100.00%
- IFC	86,876	-	-100.00%
- FMO	212,846	-	-100.00%
- Demir-Halk Bank (Nederland) N.V.	-	617,362	100.00%
Other liabilities	74,837	382,324	410.88%
Total:	702,699	2,715,013	286.37%

The biggest part of position other deposits refers to deposit from Turkiye Halk Bankasi A.S. in amount of EUR 10 million.

3.2.2 Deposits and other liabilities to other customers

The structure of the item Deposits and other liabilities to other customers and a comparative analysis as at 31 December 2015 and 31 December 2016 is presented in the following table:

(in RSD thousand)

Item	31 December 2015	31 December 2016	% of change
Transaction and other deposits	15,494,728	19,226,690	24.09%
- transaction deposits	7,243,837	8,446,234	16.60%
- other deposits	8,250,891	10,780,456	30.66%
Borrowed loans in foreign currency:	7,778,540	6,744,982	-13.29%
- EAR long-term deposits	1,504,058	1,268,190	-15.68%
- KfW	442,277	336,743	-23.86%
- EIB	5,418,202	4,892,052	-9.71%
- Italian Republic Government	82,572	23,895	-71.06%
- GGF	331,431	224,102	-32.38%
Other liabilities	100,112	129,380	29.23%
Total:	23,373,380	26,101,052	11.67%

In 2016 the Bank paid the principle of long-term loans to IFI's on a regular basis. During 2016 the Bank repaid the total amount of EUR 17,874 thousand and withdrawn EUR 5,413 thousand. Beside this the Bank repaid EUR 15,000 thousand to EFSE as subordinated loan.

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Repayments relate to EBRD EUR 671 thousand, to IFC EUR 714 thousand, to FMO EUR 1,750 thousand, to KfW EUR 909 thousand, to EIB EUR 6.627 thousand (withdrawal amounted to EUR 1,700 thousand), to Italian Republic Government EUR 485 thousand and to GGF EUR 910 thousand. Also, in respect of long-term deposit from EAR the Bank repaid EUR 5,808 thousand (withdrawal amounted to EUR 3,713 thousand).

The total deposit base of the Bank, comprising of corporate and retail deposits, amounted to RSD 19,226,690 thousand and had the following structure:

(in RSD thousand)

Deposit base	31 December 2015	31 December 2016	Plan for 2016	% of change
Corporate clients	7,552,336	8,975,876	8,780,000	18.85%
Retail clients	7,942,392	10,250,814	9,595,000	29.06%
Total:	15,494,728	19,226,690	18,375,000	24.09%

(in RSD thousand)

Deposit base	31 December 2015	31 December 2016	% of change
Transaction deposits	7,243,837	8,446,234	16.60%
- Corporate clients	5,090,341	5,998,671	17.84%
- Retail clients	2,153,496	2,447,563	13.66%
Other deposits	8,250,891	10,780,456	30.66%
- Corporate clients	2,461,995	2,977,205	20.93%
- Retail clients	5,788,896	7,803,251	34.80%
Total:	15,494,728	19,226,690	24.09%

3.2.3 Capital

The capital of the Bank as at 31 December 2016 amounted to RSD 5,883,585 thousand and comprised of the following:

(in RSD thousand)

	31 December 2015	31 December 2016
Share capital – ordinary shares	1,819,820	1,819,820
Share capital – preference shares	1,340	1,340
Share capital - preference non-accumulative shares	600,000	600,000
Share premium	1,827,323	1,827,323
Revaluation reserves	317,051	322,675
Reserves from profit	1,359,742	1,174,274
Retained earnings	-	138,153
Loss up to the level of capital	(185,467)	-
Total capital:	5,739,809	5,883,585

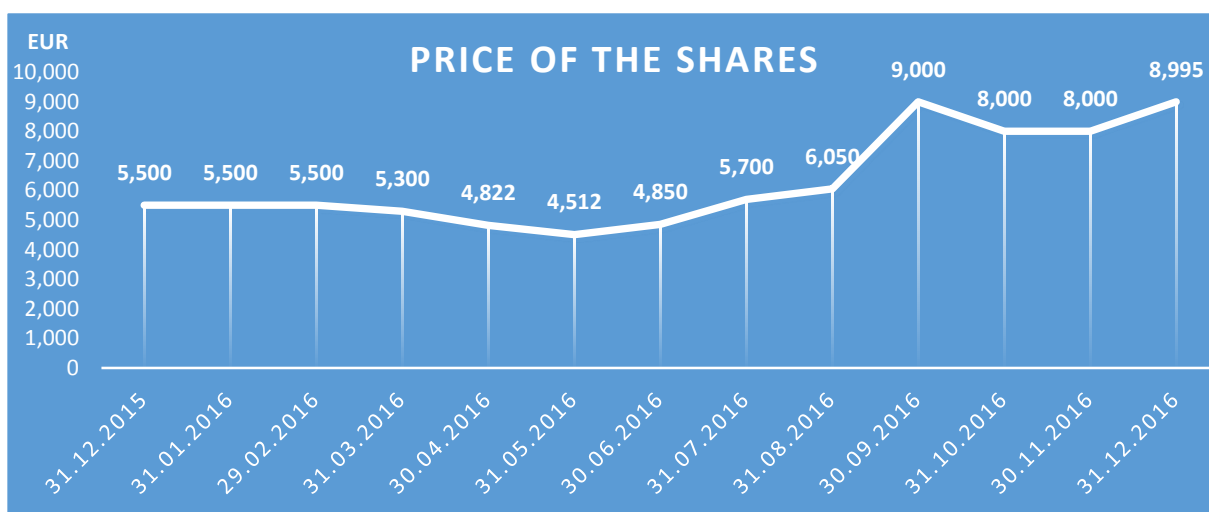
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The position "Retained earnings" comprises profit from operating activities in 2016 in amount of RSD 136,080 thousand and from cancelation of revalorization reserves recorded as benefit of retained earnings from previous years based on selling of business premises in amount of RSD 3,206 thousand and booking out actuary loss from cancelation of jubilee awards as charge to retained earnings from previous years in amount of RSD 1,133 thousand.

The information about the number of shareholders and the basic information of shares is presented in the following table:

Information of shares	31 December 2015	31 December 2016
Number of shareholders	409	407
Number of shares	242,116	242,116
Nominal value per share	10,000	10,000
Book value per share (in EUR)	23,706.85	24,300.68

The price of Bank's shares as at 31 December 2016 was RSD 8,995 accounting for a 63.55% increase relative to the price at the beginning of the year.



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4. OFF-BALANCE SHEET ITEMS

During the 2016 the Bank issued performance and payment guarantees and opened letters of credit for its customers. The structure of off-balance sheet items as at 31 December 2015 and 31 December 2016 is presented in the following table:

(in RSD thousand)

Item	31 December 2015	31 December 2016	Plan for 31 December 2016
Operations performed for and behalf of third parties	291,791	295,879	310,000
Contingent liabilities (guarantees, avals, acceptances and irrevocable liabilities)	5,364,952	5,735,364	5,750,000
Other off-balance sheet items	46,632,739	50,903,080	48,000,000
Total:	52,289,482	56,934,323	54,060,000

The following table compares the structure of the item guarantees, avals, acceptances and irrevocable liabilities as at 31 December 2015 and 31 December 2016:

(in RSD thousand)

Guarantees, avals, acceptances and irrevocable liabilities	31 December 2015	31 December 2016	% of increase / decrease
Payment guarantees	1,662,313	1,436,821	-13.56%
Issued uncovered letters of credit in foreign currencies	14,067	50,440	258.57%
Issued letters of credit in foreign currencies confirmed by the Bank	-	500,062	100.00%
Performance guarantees	2,272,345	2,475,221	8.93%
Pledged securities	584,834	90,000	-84.61%
Unused limits which cannot be revoked	831,393	1,182,820	42.27%
Total:	5,364,952	5,735,364	6.90%

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In the following table position "Other off-balance sheet items" is presented:

(in RSD thousand)

Other off-balance sheet items	31 December 2015	31 December 2016	Change
Receivables for evidencing interest	3,721,064	4,081,544	9.69%
Republic of Serbia bonds by maturities	1,121,657	840,019	-25.11%
The unused amount of revolving loans	1,626,760	1,838,612	13.02%
The unused amount of off-balance framework	201,062	289,881	44.17%
Loan frame	1,255,752	1,585,658	26.27%
Received material assets of collateral in favor of the Bank	37,619,581	38,411,093	2.10%
Received guarantees and other collaterals for settlement of obligations by the Bank's borrowers	875,464	1,282,965	46.55%
Other off-balance sheet items	211,399	531,266	151.31%
Write-off of receivables – directly write-off of receivables in accordance with MRS 39	-	2,042,043	100.00%
Total	46,632,739	50,903,080	9.16%

By the Decisions of Halkbank's Board of Directors and in accordance with the latest amendments to the NBS Decision on Classification of Balance Sheet Assets and Off-Balance Sheet Items of the Bank for application of MRS 39, all the receivables on the basis of loans and interest, which was a 100% impaired are written-off from balance sheet assets and moved to the off-balance sheet items in amount of RSD 2,042,043 thousand.

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5. STATEMENT OF PROFIT AND LOSS FOR THE PERIOD

The Bank calculated items of the Statement of profit and loss for the period from 1 January to 31 December 2016 in compliance with the Law on Accounting, IFRS and NBS regulations.

The Bank finished its operations in the 2016 with a profit of RSD 136,080 thousand.

(in RSD thousand)

	31 December 2015	31 December 2016	Plan for 2016	% of plan accomplished
Interest income	1,626,812	1,604,833	1,712,500	93.71%
Interest expenses	(447,681)	(259,871)	(400,000)	64.97%
Net interest income	1,179,131	1,344,962	1,312,500	102.47%
Fee and commission income	659,033	663,889	675,000	98.35%
Fee and commission expenses	(83,301)	(87,333)	(75,000)	116.44%
Net fee and commission income	575,732	576,556	600,000	96.09%
Net gains on financial assets held for trading	26,321	11,646	25,000	46.58%
Net gains/(losses) on exchange rate and effects of contracted index clause	(10,487)	498	-	-
Other operating income	44,416	20,995	93,750	22.39%
Net gains/(losses) on impairment of financial assets and credit risk- weighted off-balance sheet items	(761,752)	(389,289)	(450,000)	86.51%
TOTAL NET OPERATING INCOME	1,053,361	1,565,368	1,581,250	98.99%
Salaries, salary compensation and other personal expenses	(526,929)	(584,536)	(650,000)	89.93%
Depreciation costs	(95,925)	(106,915)	(160,750)	66.51%
Other expenses	(618,318)	(737,837)	(757,125)	97.45%
PROFIT / LOSS BEFORE TAXATION	(187,811)	136,080	13,375	1,017.42%

Net interest income was 2.47% higher than the plan for the 2016 and net fee and commission income was by 3.91% lower than the plan for the 2016. The total net operating income is lower than the plan for 2016 by 1.01%.

Salaries, depreciation and other expenses were higher in the 2016 by 15.16% comparing to 2015 and 8.84% lower than the anticipated values for the 2016.

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5.1 Income

The income structure during the 2015 and 2016 was as follows:

(in RSD thousand)

Income	31 December 2015	31 December 2016	% of change
Interest income	1,626,812	1,604,833	-1.35%
Fee and commission income	659,033	663,889	0.74%
Net gains on financial assets held for trading	36,790	24,282	-34.00%
- net gains on the sale of securities	1	5,063	506,200.0%
- net gains on the change in fair value of securities	36,789	19,219	-47.76%
Net gains on exchange rate and effects of contracted index clause	3,397,889	2,524,436	-25.71%
- net exchange rate gains	2,098,677	1,480,764	-29.44%
- net gains exchange rate gains under contracted index clause	1,299,212	1,043,672	-19.67%
Income on reversal provision of jubilee awards*	-	19,523	100.00%
Other operating income	44,416	20,995	-52.73%
- income from operations	3,910	4,099	4.83%
- income on the sale of fixed assets and intangible investments	2,200	3,994	81.55%
- dividend income	1,058	3,144	197.16%
- surpluses	9,321	9,731	4.40%
- other income	103	-	-100.00%
- income on changes in value of liabilities	3,266	-	-100.00%
- income on reversal provision of severance payment	24,558	27	-99.89%
Net income on impairment of financial assets and credit risk-weighted off-balance sheet items	678,162	662,938	-2.24%
- income on reversal of impairment of balance sheet items	675,246	659,760	-2.29%
- income on reversal of provisions for off-balance sheet items	2,815	1,772	-37.05%
- income on collected written-off receivables	101	1,406	1.292.08%
Total:	6,443,102	5,520,896	-14.31%

*In Statement of profit and loss position "Salaries, salary compensation and other personal expenses" is shown in net amount decreased for income on reversal provision of jubilee awards

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The structure of the position "Interest income" is presented in the following table:

(in RSD thousand)

Interest income	31 December 2015	31 December 2016	% of change
Corporate	1,105,460	839,314	-24.08%
Retail	393,792	451,982	14.78%
Securities	74,076	175,457	136.86%
Other	53,484	26,376	-50.68%
Unwinding*	-	111,704	100.00%
Total	1,626,812	1,604,833	-1.35%

*Interest income on impaired loans which are measured at amortized cost

The most significant influence on decrease of interest income from loans to the corporate clients had the high liquidity of the banking sector which was not followed with adequate demand, which had effected decreasing of interest rates on loans in the banking market.

For the first time, the Bank has valued interest income on impaired loans using effective interest rate on depreciated value of loans (net value) – unwinding, with correction on positions "Interest income" and "Net losses on impairment of financial assets and credit risk-weighted off-balance sheet items" in Statement of profit and loss. The effect is increase of interest income for corporate clients amounted to RSD 109,792 thousand and for retail clients to RSD 1,912 thousand.

The fees and commissions income was higher by 0.74% in 2016 compared to 2015 and lower by 1.65% than planned for 2016.

(in RSD thousand)

Fee and commission income	31 December 2015	31 December 2016	% of change
Fees from Bank-insurance	3,776	2,634	-30.24%
Brokers fees	5,394	3,452	-36.00%
Fees from checks and payment cards	25,400	29,011	14.22%
Fees from payment operations	386,709	403,984	4.47%
Fees from Western Union	3,410	2,678	-21.47%
Fees from FX changes	89,041	76,099	-14.53%
Fees from guarantees	95,211	83,301	-12.51%
Fees from SWAP	6,516	27,393	320.40%
Fees from loan processing	38,859	31,246	-19.59%
Other fees	4,717	4,091	-13.27%
Total	659,033	663,889	0.74%

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5.2 Expenses

Expenses had the following structure in 2015 and 2016:

(in RSD thousand)

Expenses	31 December 2015	31 December 2016	% of change
Interest expenses	447,681	259,871	-41.95%
Fee and commission expenses	83,301	87,333	4.84%
Net losses on financial assets held for trading	10,469	12,636	20.70%
- losses on the sale of securities	-	290	100.00%
- losses on change in fair value of securities	10,469	12,346	17.93%
Net losses on exchange rate and effects of contracted index clause	3,408,376	2,523,938	-25.95%
- net losses on exchange rate differences	2,195,362	1,706,983	-22.25%
- exchange rate losses under contracted index clause	1,213,014	816,955	-32.65%
Net losses on impairment of financial assets and credit risk-weighted off-balance sheet items	1,439,914	1,052,228	-26.92%
- losses on impairment of balance sheet assets	1,436,403	1,042,406	-27.43%
- losses on provisions for off-balance sheet items	1,772	9,333	426.69%
- losses on write-off of unrecoverable receivables	1,739	489	-71.88%
Salaries, salary compensations and other personal expenses	526,929	604,059	14.64%
- net salaries	526,929	599,829	13.83%
- provisions for severance payment and jubilee awards	-	4,230	100.00%
Depreciation costs	95,925	106,915	11.46%
Other expenses	618,318	737,837	19.33%
Operating expenses	558,649	734,472	31.47%
- material costs	52,144	57,151	9.60%
- production services	177,357	321,164	81.08%
- tax and contribution costs	96,208	106,164	10.35%
- intangible and other operating expenses	232,940	249,993	7.32%
Other operating expenses	59,669	3,365	-94.36%
- provisions for litigation	36,958	3,001	91.88%
- provisions for severance payment	981	-	-100.00%
- losses on changes in value of liabilities	20,366	-	-100.00%
- other expenses	1,364	364	-73.31%
Total:	6,630,913	5,384,817	-18.79%

The costs of production services increased mostly because of increasing in rental costs and advertising costs. The rental costs in 2016 were higher for RSD 62,990 thousand compared to 2015 because of relocation of the Headquarter from Čačak to Belgrade and opening new branches. Advertising costs increased for RSD 68,254 thousand in 2016 compared to 2015.

During 2016 the Bank strengthened deposit base with proactive approach, which created conditions for early repayment of subordinated loan to EFSE with maintaining of the planned level of liquidity. Situation on the market allowed collecting deposits with interest rates lower than 1%, while on subordinated loan the Bank was paying 6% interest rate. The direct effect of these activities is decrease of interest expenses by 41.95% compared to the previous year.

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The structure of the position "Interest expense" is presented in the following table:

(in RSD thousand)

Interest expense	31 December 2015	31 December 2016	% of change
Borrowings (International Financial Institutions)	247.196	104.970	-57,54%
Loans from the banks in RSD	13	4.439	-
Banks deposits	13.360	17.270	29,27%
Deposits – corporate	72.817	58.271	-19,98%
Deposits – retail	114.295	74.471	-34,84%
Ukupno	447.681	259.871	-41,95%

During 2016 the Bank strengthened deposit base with proactive approach, which created conditions for early repayment of subordinated loan to EFSE with maintaining of the planned level of liquidity. Situation on the market allowed collecting deposits with interest rates lower than 1%, while on subordinated loan the Bank was paying 6% interest rate. The direct effect of these activities is decrease of interest expenses by 41.95% compared to the previous year.

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6. CASH FLOWS

(in RSD thousand)

Position	January - December 2015	January – December 2016	Change
Cash inflows from operating activities	2,235,992	2,103,275	(132,717)
Cash outflows from operating activities	(1,629,726)	(1,769,790)	140,064
Net cash inflows from operating activities	606,266	333,485	(272,781)
Decrease of loans and increase of deposits	2,756,389	5,545,204	2,788,815
Increase of loans and decrease of deposits and other liabilities	(756,494)	(2,105,951)	(1,349,457)
Net cash inflows from operating activities before tax	2,606,161	3,772,738	1,166,577
Cash inflows from investment activities	7,200	5,126,244	5,119,044
Cash outflows from investment activities	(3,521,342)	(5,781,285)	2,259,943
Net cash outflows from investment activities	(3,514,142)	(655,041)	(2,859,101)
Cash inflows from financing activities	1,200,000	-	(1,200,000)
Cash outflows from financing activities	(1,194,411)	(2,762,096)	1,567,685
Cash inflows/(outflows) from financing activities	5,589	(2,762,096)	(2,767,685)
NET INCREASE OF CASH	-	355,601	355,601
NET DECREASE OF CASH	(902,392)	-	(902,392)
CASH AND CASH EQUIVALENTS ON THE BEGINNING OF THE YEAR	3,386,542	2,509,121	(877,421)
Positive FX changes	192,160	110,946	(81,214)
Negative FX changes	(167,189)	(92,455)	(74,734)
CASH AND CASH EQUIVALENTS ON THE END OF THE PERIOD	2,509,121	2,883,213	374,092

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Cash flows from operating activities during 2015 and 2016 are presented in the tables below:

(in RSD thousand)

	January - December 2015	January – December 2016	Increase/ decrease
Cash inflows from operating activities	2,235,992	2,103,275	(132,717)
Interest	1,569,026	1,433,910	(135,116)
Fees	661,861	662,217	356
Other operating income	4,047	4,004	(43)
Dividend and share in profit	1,058	3,144	2,086
Cash outflows from operating activities	(1,629,726)	(1,769,790)	140,064
Interest	(470,213)	(283,866)	(186,347)
Fees	(74,701)	(80,365)	5,664
Salaries	(526,929)	(650,582)	123,653
Tax and contribution	(108,441)	(122,546)	14,105
Other operating expenses	(449,442)	(632,431)	182,989
Net cash inflows from operating activities	606,266	333,485	(272,781)

Cash inflows from operating activities in 2016 decreased by RSD 132,717 thousand compared to 2015, mostly because of reduced inflows from interest in the amount of RSD 135,116 thousand.

Cash outflows from operating activities increased by RSD 140,064 thousand compared to 2015, mostly because of increase in outflows from salaries in the amount of RSD 123,653 thousand and increase in other operating activities outflows in amount of RSD 182,989 thousand on one side and reduced interest outflows in the amount of RSD 186,347 thousand on the other side. Outflows from salaries increased because of growth of expenses for salaries by RSD 77,130 thousand and increase in outflows for severance payments in the amount of RSD 46,523 thousand.

Outflows from other operating expenses are increased mostly because of higher amount of rental costs (RSD 62,990 thousand) and advertising costs (RSD 68,254 thousand).

Net cash inflows from operating activities in the 2016 amounted to RSD 333,485 thousand. Net cash inflows from the operating activities cumulatively decreased in 2016 by RSD 272,781 thousand comparing to 2015.

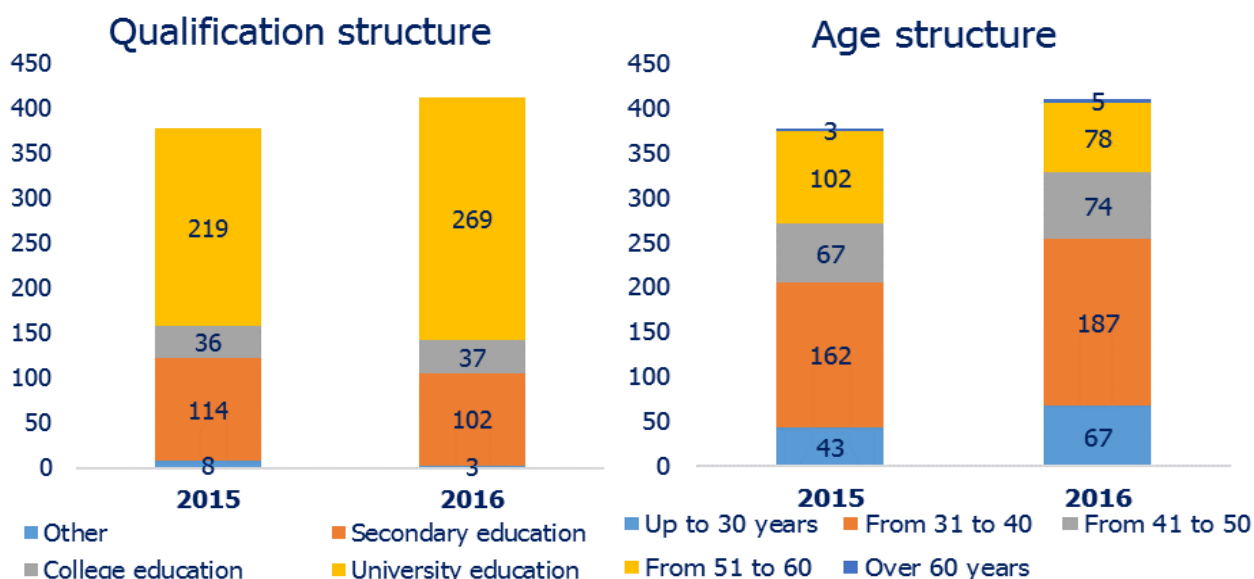
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7. HUMAN RESOURCES

The number of employees in the Bank's head office and branches as at 31 December 2016 is presented in the following table:

Number of employees	31 December 2015	31 December 2016	Plan for 2016
Headquarter	184	190	185
Branches and sub-branches	193	221	265
Total:	377	411	450

The following graphs show the qualification and age structure of employees as at 31 December 2015 and 31 December 2016.



Regarding the qualification structure of employees at the end of 2016, the Bank met anticipated share of employees with university degree accounting for 65.45% of the total. The share of staff younger than 40 years was 61.80%.

Expenses for salaries, salary compensation and other personal expenses in 2016 amounted to RSD 599,829 thousand and accounting for 92.28% of the total budget planned.

The amount of RSD 3,294 thousand was spent for staff training in the 2016. The average training costs per employee in 2016 was RSD 8 thousand.

In 2016 the annual rate of fluctuation of employees was around 19%. The main reason for the high fluctuation was organizational changes from relocation of Headquarter from Čačak to Belgrade. In 2016, 77 employees stopped working for the Bank, out of which 45 due to organizational changes. Also 111 new employees were hired in 2016 (53 in business network and 58 in Headquarter in Belgrade).

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8. INVESTMENT PLAN

During the 2016 total investments in fixed assets, investment property and intangible investments amounted to RSD 343,086 thousand.

Changes at these balance sheet items are presented in the following table:

(in RSD thousand)

	Buildings	Equipment	Investment property	Intangible investments	Total	Plan for 2016*
Balance – 01 January 2016	503,746	124,824	130,028	28,085	786,683	786,683
Increase:	9,151	248,330	-	85,605	343,086	570,875
IT	-	180,313	-	85,605	265,918	463,875
Adaption of business premises	9,151	41,619	-	-	50,770	72,000
Other	-	26,398	-	-	26,398	34,500
Decrease:	(21,539)	(46,066)	(3,691)	(39,714)	(111,010)	(190,750)
Amortization	(17,447)	(46,063)	(3,691)	(39,714)	(106,915)	(160,750)
Sale	(4,092)	(3)	-	-	(4,095)	(30,000)
Balance 31 December 2016	491,358	327,088	126,337	73,976	1,018,759	1,166,808

The biggest part of intangible investments refers to Microsoft licenses in amount of RSD 58,031 thousand. A part of planned investments for 2016 which refers to innovative and technologically advanced model of payment cards will be used in 2017.

The biggest part of investment in IT equipment refers to purchasing of hardware and software for increasing of Storage System, also for improving data security and e-mail communication security in the amount of RSD 151,749 thousand.

In line with the expansion plans of the business network of the Bank, during 2016 it was invested in adaptation of business premises for opening of branches in Pančevo, in Kalenić street and Bulevard Milutin Milanković in Belgrade and in Novi Pazar. Also, there was a relocation of Headquarter of the Bank in a new building in Bulevard Milutin Milanković in New Belgrade, renovated and relocated of branches in Šabac and renovated of branch in Cara Dušana Street in Belgrade.

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9. COMPLIANCE OF OPERATIONS WITH THE NBS REGULATIONS AND IFI AGREEMENTS

During 2016 all the operating ratios of the Bank were within the limits prescribed by the Law on Banks and NBS decisions.

Ratio	The values prescribed by the NBS regulations	Values as at 31 December 2016
Bank's equity	Min 10,000,000 €	32,192,443 €
Capital adequacy ratio	min 12%	15.64%
Foreign exchange risk ratio	max 20%	2.28%
Liquidity ratio	min 1	1.76
Narrow liquidity ratio	min 0,7	1.38
Exposure to one person or group of related persons	max 25%	11.13%
Total exposure to group of related persons	max 25%	10.93%
Sum of large exposures	max 400%	17.92%
Investing into non-financial persons	max 10%	0%
Total investments into non-financial persons and fixed assets of the Bank	max 60%	23.77%

Compliance with the covenants from the agreements concluded with the international financial institutions (IFIs)

Pursuant to the defined limits in the agreements concluded with the IFIs - German Development Bank (KfW), Green for Growth Fund (GGF), the Bank is required to comply with certain financial covenants until the final repayment of the loans. As at 31 December 2016 the Bank was not complied with open credit exposure ratio because of amendments on Decision of National Bank of Serbia on classification of balance sheet and off-balance sheet items referring to the part where coefficient for decreasing of required reserve is used.

Financial institution	Indicator	Prescribed value	Value at 31 December 2016
GGF	Open credit exposure ratio	10.00%	23.78%

According to the loan agreements, the Bank regularly reports to the international financial institutions of its financial ratios in accordance with its financial liabilities, with detailed elaboration on each exceeded limit. The Bank does not expect any negative reactions by the creditors regarding this matter, considering that the Bank received written confirmation that it will be performed correction on defined value of indicator (it will be 30%).

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10. REPORT ON BOARD OF DIRECTORS MEETINGS IN 2016

During 2016 the Board of Directors held 9 meetings in 2016.

The 7th meeting of the Board of Directors was held in Barbaros Mahallesi Sebboy Sokak No:4 Atasehir / Istanbul on 8 January 2016 with following agenda:

1. Opening the meeting and adoption of the Minutes of the 6th meeting;
2. Passing a decision on granting authorization to the EB for the sale of receivables from problematic client of the Bank, "Jugoagent" a.d.;
3. Passing a decision on granting authorization to the EB for the sale of receivables from problematic client of the Bank, "FRA" a.d.;
4. Passing a decision on adopting the Annual Report on Inventory of Assets and Assets Sources of Halkbank a.d. Belgrade on 31 December 2015;
5. Miscellaneous

The 8th meeting of the Board of Directors was held in Belgrade, Boulevard Milutina Milankovića 9ž on 16 March 2016 with following agenda:

1. Opening the meeting and adoption of the Minutes of the 7th meeting;
2. Information for the Board of Directors about Balance Sheet and Statement of profit and loss of the Bank;
3. Reviewing the report of the Internal Audit Department for the period from 1 July to 31 December 2015, with regard to the Annual Plan 2015 implementation and monitoring non-compliance for 2015;
4. Annual report on compliance controls in 2015 with identified and assessed major compliance risks and the introduction of the plan of training of employees for 2016;
5. Reporting on the Audit Committee Activities in the period from 1 November – 31 December 2016;
6. Passing a decision on adopting of credit procedures guidelines;
7. Information about decisions passed by the Executive Board under the authorization of the Board of Directors in the period from 1 November 2015 -31 December 2016;
8. Passing a decision on opening correspondent account at Halkbank a.d. Skopje;
9. Passing a decision on Amending the Capital Management Strategy and Plan;
10. Passing a decision on preliminary approval of the Board of Directors for the Bank's exposure over 10% of the capital to the Unipromet d.o.o. Čačak;
11. Annual report on Risk Management Adequacy and Internal Control of the Bank in 2015;
12. Miscellaneous

The 9th meeting of the Board of Directors was held in Barbaros Mahallesi Sebboy Sokak No:4 Atasehir / Istanbul on 18 April 2016 with following agenda:

1. Opening the meeting and adoption of the Minutes of the 8th meeting;
2. Passing a decision on granting authorization to the EB for drawing subordinated loan in amount of EUR 10 million on up to 7-year maturity;
3. Passing a decision on IT investments in amount of EUR 3,500 thousand (with VAT), which consists of investment in equipment (EUR 1.509 thousand) and investments in software and licenses (EUR 1,991 thousand)
4. The proposal for the adoption of the Operating report for 2015, as well as the submission of the report to the Assembly;

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5. The proposal for the adoption of Report of the external auditor KPMG d.o.o. Belgrade on audit of the financial statements of the Bank for 2015, as well as the submission of the report to the Assembly;
6. The proposal for the adoption of the Bank's Financial Statements for 2015, as well as the submission of the proposal to the Assembly;
7. The proposal to cover loss (according to the Bank's Financial Statements for 2015) from the reserves formed by profit from previous years and the submission of the proposal to the Assembly;
8. The proposal for the adoption of Decision on the Bank's Operating Policy for 2016 and the submission of the proposal to the Assembly;
9. The proposal on appointing an external auditor to audit the Bank's Financial Statements for 2016 and the submission of the proposal to the Assembly;
10. The proposal for submitting to the Assembly of the Bank on the amendments of Statute of the Bank;
11. Proposal for submitting to the Assembly of the Bank on amendments to the Agreement Establishing the Bank;
12. Consideration of information about fees in 2015 for members of Board of Directors and members of Executive Board and the submission to the Assembly;
13. Making decision about scheduling XXXIV Assembly of the Bank regular meeting and establishing proposals of decisions that will be discussed at the meeting;
 - 13.1. Opening the meeting and appointment of the Commissions for voting and Scorer;
 - 13.2. Reporting of Commission report for voting;
 - 13.3. The adoption of the report on the operations of the Bank for 2015;
 - 13.4. External auditor's report on the audit of financial statements for 2015;
 - 13.5. The adoption of the financial statements for 2015;
 - 13.6. Making decisions on covering the loss for the Financial Statements for 2015;
 - 13.7. Adoption of the Business Policy for 2016 with accompanying decisions;
 - 13.8. Making decisions on appointing an external auditor to audit the final statements for the year 2016;
 - 13.9. Making decisions on amendments to the Statute of the Bank;
 - 13.10. Making decisions on changes and amendments to the Agreement Establishing of the Bank;
 - 13.11. Information on the income of members of Board of Directors and the Executive Board in 2015 and the proposal for remuneration for 2016;
 - 13.12. Making decisions on the dismissal and appointment of members of the Board, as well as the proposal of the Decision on remuneration of the Board of Directors.
14. Passing a decision on adopting Report on Internal capital adequacy assessment process (ICAAP) for 2015;
15. The proposal to the Assembly of the bank on the dismissal and appointment of the President of the Board of Directors, as well as proposal of decision on fees for the members of the Board of Directors;
16. Miscellaneous

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The 10th meeting of the Board of Directors was held in Belgrade, Boulevard Milutina Milankovića 9ž on 11 May 2016 with following agenda:

1. Opening the meeting and adoption of the Minutes of the 9th meeting;
2. Adoption of the Operating report for the first quarter of 2016;
3. Passing a decision on amendments the Country Risk Management Policy;
4. Passing a decision on giving approval for exposure and limit proposal for Bosnia and Herzegovina;
5. Passing a decision on making exposure limit in amount of EUR 10 million, and not above 25% of Bank's capital to Halkbank a.d. Skopje, Makedonija;
6. Passing a decision on making exposure limit in amount of EUR 10 million, and not above 25% of Bank's capital to ZiraatBank BH dd, Bosina and Herzegovina;
7. Passing a decision on granting authorization to the EB for cession of the Bank's loan receivables from "Grafocard" company;
8. Passing a decision on granting authorization to the EB for cession of the Bank's loan receivables from "Metal Sistemi" company;
9. Passing a decision on limit increase to the "TEKLAS Automotive";
10. Passing a decision on amendments of organizational scheme;
11. Passing a decision on granting authorization to the EB for making sub-branches into branches if it is necessary;
12. Miscellaneous

The 11th meeting of the Board of Directors was held in Belgrade, Boulevard Milutina Milankovića 9ž on 3 August 2016 with following agenda:

1. Opening the meeting and adoption of the Minutes of the 10th meeting;
2. Information about collection of problematic loans process;
3. Passing a decision on abrogation of Decision of Board of Directors number 3772 from 28 August 2015 and amendments parts 2 and 3 of Decision number 7099 from 17 December 2013:
4. Passing a decision on participation of the Bank in public sale "TC Kocka" from Paraćin, which belongs TRPS group;
5. Passing a decision on giving approval about increase of exposure limit for group "Truck Stop Tomy" d.o.o. Šimanovci;
6. Passing a decision on giving approval about increase of exposure limit for group "Kompanija Jovanović";
7. Passing a decision on revision of PR and fixed assets budget;
8. Passing a decision on granting authorization to the EB for making sub-branch "Pivarska" into Branch "Pivarska";
9. Passing a decision on amendments the Country Risk Management Policy;
10. Reporting on the Audit Committee Activities in the period from 01 February – 30 April 2016;
11. Reviewing the report of the Internal Audit Department for the period from 01 January – 30 June 2016;
12. Bank's Operating report for the period 1 January – 30 June 2016;
13. Management Letter provided by the external auditor KPMG d.o.o. Belgrade
14. Passing a decision on adopting Business conduct and ethical principles Code;
15. Passing a decision on adopting of Preventing Corruption Policy;
16. The proposal to the Assembly of the Bank on changing Headquarter place of Halkbank a.d. Belgrade;

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17. The proposal for adopting to the Assembly of the Bank on the amendments of Statute of the Bank
18. Proposal for adopting to the Assembly of the Bank on amendments to the Agreement Establishing the Bank;
19. The proposal to the Assembly of the Bank on the dismissal and appointment of an independent member of the Board of Directors;
20. Making decision about scheduling IX Assembly of the Bank extraordinary meeting and establishing proposals of decisions that will be discussed at the meeting:
 - 20.1. Opening of the meeting and appointment of the Commission for voting and Socer;
 - 20.2. Reporting of Commission report for voting;
 - 20.3. Adoption of Minutes of the regular meeting of the Assembly XXXIV HALK Bank, Belgrade;
 - 20.4. Making decisions on changing the seat of the Bank;
 - 20.5. Making decisions on changes and amendments to the Statute of the Bank;
 - 20.6. Making decisions on changes and amendments to the Agreement Establishing of the Bank;
 - 20.7. Making decisions on the dismissal and appointment of the independent members of Board;
 - 20.8. Miscellaneous.
21. Information of the decisions passed by the Executive Board under the authorization of the Board of Directors in the period from 01 February – 30 April 2016;
22. Passing a decision on the dismissal and appointment of member of Executive Board;
23. Passing a decision on approving decision limit of Credit sub-committee
24. Passing a decision on approving offer from Asseco company in amount of EUR 1,237,500 without VAT;
25. Miscellaneous

The 12th meeting of the Board of Directors was held in Barbaros Mahallesi Sebboy Sokak No:4 Atasehir / Istanbul on 03 August 2016 with following agenda:

1. Opening the meeting and adoption of the Minutes of the 11th meeting;
2. Passing a decision on direct write-off balance sheet items receivables and transfer these receivables into off-balance sheet items:
3. Miscellaneous

The 13th meeting of the Board of Directors was held in Halkbank a.d. Beograd, Branch in Novi Pazar, Street AVNOJ-a 10 on 14 October 2016 with following agenda:

1. Opening the meeting and adoption of the Minutes of the 12th meeting;
2. Passing a decision on granting authorization to the Executive Board to participate in purchasing property – house in Paraćin;
3. Passing a decision on adopting of Recovery Plan of the Bank;
4. Information about delivered statements of member of Executive Board and Board of Directors from task 78 on Law on Banks;
5. Passing a decision on adopting new Organizational scheme;
6. Passing a decision on appointment president and members of Credit Committee and ALCO committee;
7. Passing a decision on the dismissal and appointment of Head of Internal Audit Department;
8. Passing a decision on giving preapproval for the client Demir-Halk Bank Netherland;

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9. Passing a decision on borrowing from Demir-Halk Bank Netherland in amount of EUR 5 million;
10. Passing a decision on giving preapproval for the client "Aster Tekstil" d.o.o. Niš;
11. Passing a decision on giving preapproval for the client "TEKLAS Automotive" d.o.o. Vladičin Han;
12. Passing a decision on amendments of Decision of Board of Directors about giving authorization to the Executive Board of the Halkbank a.d. Beograd to make decisions about some questions which are in jurisdiction of Board of Directors;
13. Miscellaneous

The 14th meeting of the Board of Directors was held in Belgrade, Boulevard Milutina Milankovića 9e on 28 November 2016 with following agenda:

1. Opening the meeting and adoption of the Minutes of the 13th meeting;
2. Passing a decision on amendments of Management and collection of problematic loans Strategy;
3. Passing a decision on adopting the Bank's Operating report for the period 1 January - 30 September 2016;
4. Report on the liquidity ratio stress tests in the period from 01 September – 131 October 2016;
5. Passing a decision on adopting the plan of Internal Audit Department for 2017, with adopted changes of the plan for 2016;
6. Passing a decision on adopting Work Plan for Internal Audit Department;
7. Reporting on the Audit Committee Activities in the period from 01 May – 30 September 2016;
8. Passing a decision on adopting the guidelines for preparing Bank's Operating policy for 2017;
9. Passing a decision on giving preapproval on total Bank's exposure to the client "DIPeM" d.o.o. Čačak can be higher than EUR 1,500,000, or maximum limit in amount of EUR 2,200,000;
10. Passing a decision on giving preapproval on total Bank's exposure to the group of related clients "DECO" d.o.o. Vrnjačka Banja can be higher than EUR 1,500,000, or maximum limit in amount of EUR 2,500,000;
11. Passing a decision on sale of Bank's receivables from "Metal Sistemi" d.o.o. Kragujevac in bankruptcy, in minimal amount EUR 2,000,000;
12. Passing a decision on giving approval to the Executive Board for passing a decision on opening two new branches in Belgrade;
13. Passing a decision on adopting annual Work Plan of Compliance and AML Department for 2017 with plan of employees' education;
14. Passing a decision on adopting Program for compliance monitoring of the Bank's operations;
15. Passing a decision on direct write-off balance sheet items receivables and transfer these receivables for receivables from "Farmakom MB" d.o.o.;
16. Miscellaneous

The 15th meeting of the Board of Directors was held in Barbaros Mahallesi Sebboy Sokak No:4 Atasehir / Istanbul on 23 December 2016 with following agenda:

1. Opening the meeting and adoption of the Minutes of the 14th meeting;
2. Passing a decision on adopting Guidelines for preparing business plan of the Bank for 2017 with macroeconomic analyses and analyses of the banking sector in Serbia;

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3. Passing a decision on amendments to the Accounting policies;
4. Reviewing and/or adopting of Risk Management Strategies and policies:
 - 4.1. Risk management strategy;
 - 4.2. Strategy and plan for capital management;
 - 4.3. The policy of credit risk management;
 - 4.4. The policy of liquidity risk management;
 - 4.5. Policy of market risk;
 - 4.6. The policy of strategic risk management;
 - 4.7. Reputational Risk Management Policy;
 - 4.8. Operational Risk Management Policy;
 - 4.9. The policy of interest rate risk management;
 - 4.10. Country risk management policy;
 - 4.11. Privacy Risk Management environment and society;
 - 4.12. Privacy Risk Management concentration.
5. Adopting of IS development strategy;
6. Adopting of internal documents for Bank's business continuity management;
 - 6.1. Adoption of recovery strategies in the event of a business interruption;
 - 6.2. Adoption of the Business Continuity Plan (BCP);
 - 6.3. Adoption of the Plan of recovery activities in the event of a disaster (DRP).
7. Proposal of the Decision on dismissal and appointment member of the board of Directors;
8. Making decision about scheduling X Assembly of the Bank extraordinary meeting and establishing proposals of decisions that will be discussed at the meeting;
 - 8.1. Opening of the meeting and appointment of the Commission for voting and Socer;
 - 8.2. Reporting of Commission report for voting;
 - 8.3. Approval of the Minutes of the ninth extraordinary session of the Assembly;
 - 8.4. Making decisions on the dismissal and appointment of members of the Management Board;
 - 8.5. Information on submitted statements by members of the Executive and Management Committee referred to in Article 78 of the Law on Banks;
 - 8.6. Miscellaneous.
9. Information of the decisions passed by the Executive Board under the authorization of the Board of Directors in the period from 01 May 2016 – 30 November 2016;
10. Reporting on the Audit Committee Activities in the period from 1 October – 31 October 2016;
11. Report on the liquidity ratio stress tests in the period from 01 November – 30 November 2016;
12. Miscellaneous

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III INVESTMENT FOR THE PURPOSE OF ENVIRONMENTAL PROTECTION

The Bank is particularly cautious to invest only in the projects that do not cause any environmental and social harm. Environmental and social (E&S) protection includes, besides ecological aspects, the issues of a local community and employee protection.

The aim of managing E&S risk is identification, assessment and control of the risks that may cause E&S harm and it is carried out in accordance with the E&S Risk Management Policy and Procedure BPI-751-503 E&S Risk Management.

The following bodies are responsible for managing the E&S risk in the Bank:

- Board of Directors that establishes and at least once a year reviews E&S Risk Management Policy and identifies the need for any amendments thereto,
- Executive Board that establishes and implements the E&S Risk Management Procedure,
- Credit Committees that make decisions on loan disbursement on the basis of the E&S information available and the opinion of the Creditworthiness Appraisal Department,
- The Credit Division that assesses the impact of the activity and the project during the process of appraising customers' creditworthiness,
- The Portfolio Management Department that monitors loans by their activities, industrial sectors and E&S risk categories

When processing individual clients' applications, E&S risk is classified for the basic activity of the client and the activity which is subject to financing.

There are the following E&S risk categories:

- High – Exclusion List
- High – Referral List
- High – Category A
- High
- Medium
- Low

If the activity which is subject to financing is included in the Exclusion List, the application will be rejected. In the event that they are classified in high risk category A, the Environmental Impact Assessment will be provided from the client, and the person appointed by the Executive Board for the SEMS maintenance will provide a prior consent for financing the project.

When reviewing application with the decision draft for the relevant credit committee, the Credit Division verifies classification of the activity with regard to E&S risk and the data about the E&S impact of the client and the financed activity.

In the events anticipated by the Procedure, the integral part of the application analysis will be the opinion of the Credit Division about how the client submitting the application complies with E&S regulations and standards. Loan agreements and agreements on other exposures contain E&S provisions that should be obeyed by both the client and the Bank.

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Environmental risk

Overview of the Bank's exposures by environmental and social risk categories

(in RSD thousand)

Risk category	Number of clients		Amount of placements (balance and off-balance)		Increase/ decrease
	31 December 2015	31 December 2016	31 December 2015	31 December 2016	
High – Exclusion List	-	-	-	-	-
High – Category A	7	7	188,990	112,766	(76,224)
High	229	204	6,324,463	6,576,746	252,283
Medium	1,074	956	9,022,943	10,979,399	1,956,456
Low	2,224	1,923	12,811,870	12,053,862	(758,008)
Total:	3,534	3,090	28,348,266	29,722,773	1,374,507

The exposure to the clients which financed activity is in "High – exclusion list" category does not exist neither on 31 December 2016 neither on 31 December 2015.

IV MATERIAL EVENTS AFTER THE END OF BUSINESS YEAR

In accordance with the Decision G.Nb. 963 from 1 February 2017, National Bank of Serbia started controlling activities on 20 February 2017 in the part related to the Credit Risk and control of Capital Adequacy Ratio calculation as at 31 December 2016, as well as control of bank management.

V ANTICIPATED FUTURE DEVELOPMENT

When preparing the Major Financial Indicators and Guidelines for Business Plan 2017, it was presumed increase in balance sheet equal to 27% (in EUR).

It is planned 3 new branches and consequently increasing in the number of employees. The plan is to increase loan portfolio for EUR 63 million (loans to corporate clients for EUR 38 million and loans to retail clients for EUR 25 million). On the passive side, the increase in capital in amount of EUR 20 million is planned and increase of deposits in the amount of EUR 38 million. Also, one source of funding will be credit lines from international institutions in the amount of EUR 25 million.

VI RESEARCH AND DEVELOPMENT ACTIVITIES

The Bank carries out a regular financial market research, analyses customers' financial needs and investigates a degree of satisfaction of the users of financial services.

The Marketing Division of Halkbank continuously develops new products and services and endeavors, on the basis of the information and conclusions acquired upon the market research and customers' needs, to develop and place at the market modified existing products, as well as completely new products and services.

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VII INFORMATION ON PURCHASE OF OWN SHARES

The Bank never owned its own shares and did not acquire them during 2016.

VIII EXISTENCE OF AFFILIATES

As at 31 December 2016 the Bank operates in Head office and of 5 branches in Belgrade, 14 branch offices located in the towns of Jagodina, Gornji Milanovac, Čačak, Kraljevo, Užice, Kragujevac, Kruševac, Arandelovac, Valjevo, Šabac, Niš, Novi Sad, Pančevo and Novi Pazar, and 9 sub-branches in Paraćin, Požega, Topola, Ivanjica, Vrnjačka Banja, Leskovac, Mladenovac and Čačak (2 branches).

IX RISK MANAGEMENT ADEQUACY

The Bank's targets in risk management are identification, measuring, mitigating and monitoring all types of risks and thus minimizing the Bank's exposure to such risks.

Credit Risk

The Bank measures and monitors the credit risk level through assessing the clients' solvency and controlling the loan portfolio through the calculation of a loan loss reserve pursuant to the NBS regulations and impairment and provisions pursuant to the IFRS.

Structure of gross risk-weighted assets in terms of classification categories

(in RSD million)

Classification categories	Classified amount 31 December 2015	% of the share in gross risk-weighted assets	Plan for 31 December 2016						
			Classified amount 31 December 2016	% of the share in gross risk-weighted assets		Classified amount	% of the share in gross risk-weighted assets		
A	16,879	49.72%	74.54%	18,838	50.85%	75.70%	19,946	50.97%	79.11%
B	8,425	24.82%		9,207	24.85%		11,014	28.14%	
V	821	2.42%	2.42%	3,009	8.12%	8.12%	815	2.08%	2.08%
G	1,157	3.41%	23.04%	1,620	4.38%	16.18%	819	2.09%	18.81%
D	6,664	19.63%		4,370	11.80%		6,538	16.72%	
Total:	33,946	100.00%		37,044	100.00%		39,132	100.00%	

Compared to 31 December 2015 the participation of receivables classified in A and B categories increased by 1.17 p.p.

The participation of receivables classified in the V category increased by 5.68 p.p. mostly because deteriorated classification of receivables which had banking guarantees as collateral. These banks' rating changed in 2016, so those guarantees cannot be treated as first-class collateral.

The share of receivables classified in the G and D category decreased by 6.85 p.p. The share of receivables classified in D category decreased by 7.83 p.p. as the result of collection of doubtful receivables and write-off of receivables which were 100% impaired.

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Pursuant to the Procedure for Credit Risk Management at the portfolio level, the Bank amortized the high level of the credit risk measured through the assets quality by establishing adequate reserves.

Loan loss reserve pursuant to the NBS Decision on Classification

(in RSD thousand)

	31 December 2015	31 December 2016	Plan for 2016
Loan loss reserve under balance sheet assets	7,187,307	5,221,924	7,087,052
Loan loss reserve under off-balance sheet items	43,797	75,616	38,104
Total:	7,231,104	5,297,540	7,125,156

Provisions according to the Bank's internal methodology in accordance with IAS 39

(in RSD thousand)

	31 December 2015	31 December 2016	Plan for 2016
Impairment of balance sheet assets to be classified	4,860,701	2,818,811	5,305,785
Provisions for losses under off-balance sheet items	2,008	9,569	6,918
Impairment of other financial assets	21,073	12,249	
Total:	4,883,782	2,840,629	5,312,703

The biggest influence on decreasing of impairment of classified assets in 2016 had direct write-off of receivables which were 100% impaired as well as good collection of NPL. The performed write-off was not included in the planned figures for 2016.

Required loan loss reserve

(in RSD thousand)

	31 December 2015	31 December 2016	Plan for 2016
Required reserve	2,419,056	1,648,182	4,223,996

A required loan loss reserve is the sum of positive differences between the estimated loan loss reserve and the established impairment of the balance sheet and provisions for off-balance sheet losses at the borrower's level. As at 31 December 2016 the required reserve was RSD 2,497,245 thousand but it is corrected using coefficient for decreasing by 34%. Required reserve calculated as about mentioned represents deductible item from the Bank's regulatory capital and as of 31,12,2016 it amounted to RSD 1,648,182 thousand. The calculation defined by the National Bank of Serbia Decision on classification of balance and off-balance sheet items took into force from 30 September 2016.

Coefficient for decreasing of amount of required loan loss reserve is calculated on the basis of decreased NPL ratio from non-financing and non-government sector as at 31 December 2016 comparing to 30 June 2016.

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Liquidity Risk**Liquidity Ratio and Narrow Liquidity Ratio proscribed by NBS in the 2016**

	Liquidity Ratio	Narrow Liquidity Ratio
Value as of 31/12/16	1.76	1.38
Average	1.79	1.30
Maximum	2.75	1.70
Minimum	1.20	0.90
Daily NBS limit	Min 0.80	Min 0.50
NBS limit on monthly level	Min 1.00	Min 0.70

The limits of the National Bank of Serbia are regulated by the Decision on risk management. Liquidity ratios of the Bank during 2016 were in accordance with the prescribed limits.

In order to adequately manage liquidity risk, the Bank monitors internally established indicators of structural liquidity, besides the limits proscribed by the NBS.

Additional liquidity ratios in the 2016

	Min.	Max.	Average	Limit
Liquid assets ratio	22.07%	35.67%	27.62%	Min 20.00%
Net loans to total deposits ratio	93.45%	124.84%	108.89%	Max 200.00%
Customers' deposits to total deposits ratio	92.28%	100.00%	99.42%	Min 75.00%
Deposit concentration ratio	17.80%	25.91%	20.87%	Max 30.00%

The Bank was within internally proscribed liquidity limits during 2016.

Foreign exchange risk**FX Risk ratio in 2016**

Value as of 31/12	2.28%
Average	3.07%
Maximum	11.90%
Minimum	0.30%
Limit NBS	Max 20%

Foreign currency risk measured by FX Risk ratio was mostly located in the low risk category in 2016. The average value of the foreign currency risk ratio amounted to 3.07%.

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Interest rate risk

Interest rate risk management is carried out in the Risk Management Department through measurement and monitoring of revaluation risk of interest rates (repricing risk), the base interest rate risk, yield curve risk and option risk.

The impact of changes in interest rates on the economic value of the Bank is monitored through total net weighted position of the banking book. The total net weighted position shows how much is the change of the economic value of the Bank in the event of changes in interest rates of all maturities by 200 basis points. The Bank manages its assets and liabilities so that total net weighted positions expressed in absolute amount does not exceed 20% of its capital.

Total net weighted position of the Bank as of 31 December 2016

	(in 000 RSD)
Total net weighted position	5,077
Equity	3,974,875
Total net weighted position and equity ratio	0.13%

Interest rate risk was monitored through weighted value of interest rate GAP in relation to equity. As of 31 December 2016 the value of the weighted interest rate GAP, amounted to 0.13% of its equity, which is well below the limit of 20% of the prescribed by Procedure for managing interest rate risk.

Operational risk

In 2016 it was recorded 134 operational risk events, i.e. 68 events more than in 2015.

The largest number of operational risk events referred to the cash shortage or cash surpluses, and they were successfully resolved (80 events of cash shortage, 32 events of cash surplus). The remaining 22 operational risk events were related to: the cases of external fraud, errors in the transmission of orders, incomplete documentation, failures in working with applications.

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From the remaining amount of 22 cases, 4 cases of external fraud is more significant with total gross loss of 85 thousand EUR. For 3 from 4 cases the Bank still leads court processes while remaining 18 cases of operating risk were completely solved with net loss of 0 RSD. The Bank does not expect in this moment negative finalization of cases raised against the Bank and according to this the Bank did not formed provisions at the year end.

01 January 2016 – 31 December 2016.		Level of risk defined by internal methodology
Number of events	134	
Of which: Cash shortage	80	Critical (over 71 events)
Of which: Cash surplus	32	Medium (31 to 50 events)
Of which: Other	22	Low (up to 30 events)
Gross loss in EUR	167.159	
Net loss in EUR	978	

According to the criterion of the number of events of the same kind during the one year, the type of event the cash shortfall was in the category of critical risks, while type of event the cash surplus was in the category of medium risk.

In relation to the type of event, 120 operational risk events were related to the execution, delivery and management processes, 9 events were related to clients, products and business practices, 4 were related to the case of external fraud and activities and 1 event was related to expense of the fixed assets.

The Bank also performs risk assessment on entrusting activities to the third parties (outsourcing), based on the contracts concluded with these persons which have clearly defined rights and obligations.

When introducing new products, processes and systems or new business activities the Bank performs assessment and identification of operational risk.

Exposure risk

The Bank's exposure to persons related to the Bank and its large exposures as of 31 December 2016

	(in 000 RSD)	% of equity	Limit NBS
Persons related to the Bank	434,398	10.93%	Max 25%
Large exposures	712,488	17.92%	Max 400%

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Exposure of the Bank to entities related to the Bank on the date 31 December 2016. was within the prescribed limits of the National Bank of Serbia of 25% of regulatory capital, as well as the sum of large exposure within the limit of 400%, while in the context of internally prescribed limits the sum of all large exposures was in low risk category (up to 200% of regulatory capital).

For all large exposures, the Bank have the decisions of the Board of Directors on loan approval and defining exposure limits.

Loan concentration risk

	31 December 2015	31 December 2016	Prescribed value
Concentration ratio of 20 largest clients/groups of related parties	23.84%	21.20%	Max 30.00%

Concentration ratio of 20 largest exposures as at 31 December 2016 amounted to 21.20% and was within the internally prescribed value. The ratio decreased by 2.64 p.p. compared to 31 December 2015.

Investment Risk

The Bank's investments into non-financial persons were in a low risk category (below 6% of equity). Total investments into non-financial persons and fixed assets were also in a low risk category (below 45% of equity).

Bank's investments into non-financial sectors and fixed assets as at 31 December 2016

	Investments into non- financial sectors	Investments into fixed assets	Total
Amount (000 RSD)	-	944,783	944,783
Share in equity	0%	23.77%	23.77%
Limit NBS	Max 10%	-	Max 60%

Country Risk

The Bank establishes a system for classifying the countries according to the level of country risk which was based on international credit rating (Moody's, Standard & Poor's and Fitch).

As at 31 December 2016 according to an internal model of risk categories the bank is exposed to a satisfactory level within category of low and medium risk.

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Review of countries of clients whose exposure enters to country risk as at 31 December 2016.

Country	Risk category
Germany	Low
USA	Low
Macedonia	Medium
Montenegro	Medium
Turkey	Medium

Securities portfolio

The total value of the securities held for trade, available for sale and securities held to maturity as at 31 December 2016 was RSD 4,644,904 thousand.

Item	31 December 2015	31 December 2016
Financial assets recognized at fair value through income statement and held for trading:	295,295	23,984
- Shares of banks and other financial institutions	8,344	519
- Shares of companies	18,805	23,465
- Bonds of the Republic of Serbia - deposited foreign currency savings	268,146	-
Financial assets available for sale	244,349	3.177,595
- Municipal bonds	92,056	86,269
- Republic of Serbia bonds available for sale in RSD	-	1,947,447
- Treasury bills issued by the Republic of Serbia in RSD	-	207,069
- Treasury bills issued by the Republic of Serbia in foreign currency	152,293	936,810
Financial assets held to maturity	3,449,188	1,353,325
- Treasury bills issued by the Republic of Serbia in RSD	598,823	2,772,295
- Bonds of the Republic of Serbia in RSD	569,881	255,507
- Treasury bills issued by the Republic of Serbia in foreign currency	-	241,089
- Bonds of the Republic of Serbia in foreign currency	184,621	180,297
Pledged financial assets	584,834	90,000
- Treasury bills issued by the Republic of Serbia in foreign currency	358,154	-
- Bonds of the Republic of Serbia - deposited foreign currency savings	226,680	90,000
Total:	4,573,666	4,644,904

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Collection and coverage of NPLs

Gross NPLs based on the methodology of reporting to the National Bank of Serbia is shown in the following table:

Ratio	31 December 2015	31 December 2016	% of change
Gross NPL	7,038,905	5,151,898	-26.81%

Gross NPL as of 31 December 2016 was reduced by 1,887,007 thousand RSD compared to 31 December 2015.

In 2016 the Bank has collected 394,804 thousand RSD of NPLs: 361,185 thousand RSD from companies and 33,619 thousand RSD of retail clients.

In addition to the collection of NPLs, reduction of NPLs has been influenced by write-offs that were conducted during the year 2016.

Share of NPLs in total Bank's loans

Ratio	31 December 2015	31 December 2016	Plan for 31.12.2016
Share of gross NPLs in total gross loans	29.98%	19.48%	28.90%
Share of net NPLs in total net loans	14.17%	11.40%	13.33%

The Strategy for NPL Management and Collection defines basic ratios and their values for ensuring satisfactory coverage of NPLs, as well as the level of loan loss reserves that enables minimizing negative effects of any deterioration of asset quality on the Bank's capital adequacy.

In accordance with this Strategy, the bank's target is to maintain NPL coverage ratio by impairment of total loans above 55%.

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NPL coverage

Ratio	31 December 2015	31 December 2016	Plan for 31 December 2016
Impairment, loan loss provisions on off-balance sheet items and required reserve / NPL	103.45%	103.33%	>100%
Impairment of total loans / NPL	63.28%	54.88%	>55%

Compared to the 31 December 2015 as at 31 December 2016, the ratio of NPL coverage by impairment, loan loss provisions on off-balance sheet items and required reserve for estimated losses, decreased by 0.12 p.p, and the ratio of NPL coverage by impairment decreased by 8.40 p.p. due to write off fully impaired receivables.

Portfolio of acquired assets as at 31 December 2016

Acquired assets	Acquisition date	Net carrying value		Comment
		31 December 2015	31 December 2016	
Material assets acquired upon collection of receivables		1,390	6,205	
- Business premises, counter hall, area 48 m ² , KO Šume, Ivanjica	26 December 2014	1,390	1,415	Decision of EB about sale has been adopted on 10.11.2015
-Apartment, Cacak, Filipa Filipovica 19, 87 square metres	01 September 2016	-	4,790	The apartment is taken from the main debtor, on the basis of the Court Decision from Cacak on 10.08.2016

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X CORPORATE GOVERNANCE RULES

Corporate governance rules of Halkbank a.d. Beograd are regulated in the following by-laws:

- Statute;
- Foundation Agreement;
- Corporate Governance Code;
- Business Code of Board of Directors Members and
- General Operating Conditions.
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These documents are publicly available at the Bank's website: <http://www.halkbank.rs/>

HALKBANK AD BEOGRAD

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Erturk Sumer

Chairman of the Executive Board
Kenan Bozkurt

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