Part of the ProCredit Group

ProCredit Bank

# Disclosure Report 2016

# in accordance with Article 13 CRR

# ProCredit Bank a.d. Beograd

# Introduction

As a significant subsidiary of ProCredit Holding AG & Co. KGaA (ProCredit Holding), which is the superordinated company of the ProCredit Financial Holding Group (the ProCredit group, the group), ProCredit Bank a.d. Beograd (ProCredit Bank, the bank) has a duty of disclosure in accordance with Article 13 of EU Regulation No. 575/2013 (Capital Requirements Regulation, CRR).

The intention behind the regular disclosure of qualitative and quantitative information is to give the reader detailed insight into the current risk profile and risk management of the institution, and thus to create transparency and enhance market discipline. In this report ProCredit Bank discloses all qualitative and quantitative information required in accordance with the CRR as of 31 December 2016. As the CRR is not applied in Serbia, the information provided in this disclosure report is based on local regulations issued and overseen by the National Bank of Serbia (NBS).

This disclosure report is an additional document alongside the annual financial statements of ProCredit Bank, which are published on the bank's website. In particular, the report discloses information about own funds and credit risk. For further information related to the organisation of risk management, own funds and remuneration, please refer to the group disclosure report as well as the group annual report, which are published on the ProCredit Holding website.

Due to rounding, numbers and percentages presented throughout this report may not add up precisely to the totals provided.

# Article 437 CRR

# Own funds

The table below shows the reconciliation of the regulatory capital with the balance sheet in the audited financial statements.

| in '000 RSD | 31.12.2016 | 31.12.2015 |
|---|---|---|
| **Shareholders' equity (accounting value)** | **13,754,479** | **9,195,745** |
| Retained earnings | -2,709,929 | -1,826,671 |
| **Shareholders' equity (regulatory value)** | **11,044,550** | **7,369,075** |
| Deductions from core capital | -63,876 | -63,876 |
| **Total core capital (regulatory value)** | **10,980,674** | **7,305,199** |
| | | |
| **Supplementary capital (accounting value)** | **4,441,622** | **4,438,182** |
| A portion of revaluation reserves referring to fixed assets and share in capital | -61,398 | -66,777 |
| Subordinated liabilities | 0 | -729,757 |
| **Supplementary capital (regulatory value)** | **4,380,224** | **3,641,648** |
| Deductions from supplementary capital | -63,876 | -63,876 |
| **Total supplementary capital (regulatory value)** | **4,316,348** | **3,577,772** |
| | | |
| **Total regulatory capital** | **15,297,022** | **10,882,971** |

As at the end of December 2016, core capital had increased by RSD 3,675 million compared to the previous year. This change is the net result of a higher retained earnings than in previous periods (+RSD 738 million), a decrease in the required reserve for estimated losses on balance-sheet assets and off-balance sheet items of the bank (-RSD 2,934 million), and a decrease in intangible assets in the form of goodwill, licences, patents and trademarks (-RSD 3.3 million).

Supplementary capital increased by RSD 739 million due to a rise in subordinated liabilities which had been eligible for recognition as supplementary capital.

Regulatory capital increased by RSD 4,414 million due to the increase in both core capital and supplementary capital.

According to Serbian regulations, the capital of the bank is defined as the sum of its core capital and supplementary capital less deductibles from capital. In calculating its capital, the bank observes restrictions on certain elements of capital. The table below shows the report on capital elements.

| (in '000 RSD) | Amount regulatory capital 31.12.2016 | "Accounting" capital 31.12.2016 | Amount regulatory capital 31.12.2015 | "Accounting" capital 31.12.2015 |
|---|---|---|---|---|
| **CAPITAL** | **15,297,022** | **18,068,349** | **10,882,972** | **13,506,176** |
| **CORE CAPITAL** | **11,044,550** | **13,754,479** | **7,369,075** | **9,195,745** |
| Paid up portion of the share capital against equity stock of the bank, excluding cumulative preferred stock | 3,663,012 | 3,663,012 | 3,663,012 | 3,663,012 |
| Premium on issue against the bank's equity stock, excluding cumulative preferred stock | - | - | - | - |
| Share premium | 2,776,745 | 2,776,745 | 2,776,745 | 2,776,745 |
| Reserves from profit | 1,643,864 | 1,643,864 | 1,643,864 | 1,643,864 |
| A portion of retained earnings from the preceding years and from the current year as stated in the bank's annual financial statement, which the bank's assembly decided to allocate within the core capital | 3,246,390 | 5,956,319 | 2,508,390 | 4,335,060 |
| Losses from the preceding years | - | - | - | - |
| Profit from the current year | - | - | - | - |
| Losses posted in the current year | - | - | - | - |
| Intangible assets in the form of goodwill, licenses, patents and trademarks | 285,461 | 285,461 | 288,807 | 288,807 |
| Acquired own shares of the bank, excluding cumulative preferred stock | - | - | - | - |
| Regulatory value adjustment to international financial reporting standards and/or international accounting standards | - | - | 2,934,129 | 2,934,129 |
| Unrealized losses on securities available for sale | - | - | - | - |
| Other net negative revaluation reserves | - | - | - | - |
| Gains on bank liabilities measured at fair value reduced due to the change in the bank's credit assessment | - | - | - | - |
| Amount of required reserve for estimated losses on balance-sheet assets and off-balance sheet items of the bank | - | - | 2,934,129 | 2,934,129 |

| (in '000 RSD) | Amount regulatory capital 31.12.2016 | "Accounting" capital 31.12.2016 | Amount regulatory capital 31.12.2015 | "Accounting" capital 31.12.2015 |
|---|---|---|---|---|
| Minority participation in connected parties | - | - | - | - |
| Other negative consolidated reserves | - | - | - | - |
| Other positive consolidated reserves | - | - | - | - |
| **SUPPLEMENTARY CAPITAL** | **4,380,224** | **4,441,622** | **3,641,648** | **4,438,182** |
| Paid up portion of the share capital against the bank's cumulative preferred stock | - | - | - | - |
| Premium on issue against the bank's cumulative preferred stock | - | - | - | - |
| Share premium based on cumulative preferred stock | - | - | - | - |
| A portion of revaluation reserves referring to fixed assets and share in capital | 552,583 | 613,981 | 600,996 | 667,773 |
| Hybrid instruments | - | - | - | - |
| Subordinated liabilities | 3,827,641 | 3,827,641 | 3,040,653 | 3,770,409 |
| Over allocation of impairment allowances, provisions and required reserves relative to expected losses | - | - | - | - |
| Amount of capital that exceeds limitations for supplementary capital | - | - | - | - |
| Receivables in respect of balance-sheet assets and off-balance sheet items of the bank secured by a hybrid instrument or subordinated liability of the bank | - | - | - | - |
| Cumulative preferential shares of the bank which the bank received in pledge | - | - | - | - |
| Deductibles from the capital | 127,752 | 127,752 | 127,752 | 127,752 |
| from which: shall be deducted from core capital | 63,876 | 63,876 | 63,876 | 63,876 |
| from which: shall be deducted from supplementary capital | 63,876 | 63,876 | 63,876 | 63,876 |
| Direct or indirect investment in banks and other financial sector entities that exceed 10% of the capital of such banks and/or other financial sector entities | 127,752 | 127,752 | 127,752 | 127,752 |
| Investment in hybrid instruments and subordinated liabilities of other banks and financial sector entities in which the bank has direct or indirect investment that exceeds 10% of the capital of such entities | - | - | - | - |

| (in '000 RSD) | Amount regulatory capital 31.12.2016 | "Accounting" capital 31.12.2016 | Amount regulatory capital 31.12.2015 | "Accounting" capital 31.12.2015 |
|---|---|---|---|---|
| Total amount of direct and indirect investment in banks and other financial sector entities in the amount of up to 10% of their capital, as well as investment in their hybrid instruments and subordinated liabilities that exceeds 10% of the sum of core and supplementary capital of the bank for which the calculation of capital is made | - | - | - | - |
| The amount by which qualified participation in non-financial sector entities has been exceeded | - | - | - | - |
| Under allocation of impairment allowances, provisions and required reserves relative to expected losses | - | - | - | - |
| The amount of exposure to free deliveries if the counterparty failed to fulfil its obligation within four working days | - | - | - | - |
| Receivables and potential liabilities toward persons related to a bank or employees in the bank which the bank has negotiated under the terms that are more favorable than the terms negotiated with other parties that are not related to the bank and are not employees of the bank | - | - | - | - |
| Amount of required reserve for estimated losses on balance-sheet assets and off-balance sheet items of the bank in accordance with article 427 of Decision on capital adequacy of the bank | - | - | - | - |
| **TOTAL CORE CAPITAL:** | **10,980,674** | **13,690,603** | **7,305,199** | **9,131,869** |
| **TOTAL SUPPLEMENTARY CAPITAL:** | **4,316,348** | **4,377,746** | **3,577,772** | **4,374,306** |
| **NOTES** | **-** | **-** | **-** | **-** |
| Under allocation of impairment allowances, provisions and required reserves relative to expected losses referred to in paragraph 1, item 5) represent a positive difference between total expected losses calculated by applying the IRB Approach | - | - | - | - |
| Amount of under allocation of impairment allowances, provisions and required reserves relative to expected losses | - | - | - | - |
| From which - on group bases: | - | - | - | - |
| From which - on individual bases: | - | - | - | - |
| Amount of expected loses based on IRB approach | - | - | - | - |
| **Total amount of subordinated liabilities** | **3,827,641** | **3,827,641** | **3,770,409** | **3,770,409** |

There are differences between regulatory capital and "accounting" capital in the following positions:

- Core capital:
  - In the "accounting" capital position, a portion of retained earnings from the preceding years and from the current year, as stated in the bank's annual financial statements, was allocated by decision of the bank's general assembly to core capital
- Supplementary capital:
  - 90% of the regulatory capital position is made up of revaluation reserves for fixed assets and share capital
  - The "accounting" capital position for subordinated liabilities includes the gross amount of subordinated liabilities. The amount of subordinated liabilities included in the regulatory supplementary capital in the last five years before maturity of these obligations is reduced by 20% per year, and in the last year before this deadline subordinated liabilities are not included in supplementary capital.

The following tables show the key features of the capital instruments issued by ProCredit Bank.

### Details on capital instruments

| No. | Main features | | |
|---|---|---|---|
| 1 | Issuer | ProCredit Bank a.d. Beograd | ProCredit Bank a.d. Beograd |
| 2 | Unique identifier (e.g. CUSIP, ISIN or Bloomberg identifier for private placement) | ISIN: RSPCBSE49440 | N/A |
| 3 | Governing law(s) of the instrument | Serbian Law | German Law |
| | Regulatory treatment | | |
| 4 | Transitional CRR rules | Core capital | Supplementary capital |
| 5 | Post-transitional CRR rules | Core capital | Supplementary capital |
| 6 | Eligible at solo/(sub-)consolidated/ solo&(sub-)consolidated | Solo and consolidated | Solo and consolidated |
| 7 | Instrument type (types to be specified by each jurisdiction) | Core capital (ordinary shares) | Supplementary capital |
| 8 | Amount recognized in regulatory capital (Currency in million, as of most recent reporting date) | RSD 6,440 million | RSD 1,859 million |
| 9 | Nominal amount of instrument | RSD 6,440 million | RSD 1,859 million (equal to EUR 15 million) |
| 9a | Issue price | RSD 1,000 | 100% |
| 9b | Redemption price | RSD 1,000 | 100% |
| 10 | Accounting classification | Shareholders' equity (common shares) | Liability - amortized cost |
| 11 | Original date of issuance | Several dates of issuance (from 2001-2008) | 26.12.2007 |
| 12 | Perpetual or dated | Perpetual | Dated |
| 13 | Original maturity date | No maturity | 31.5.2022 |
| 14 | Issuer call subject to prior supervisory approval | No | Yes |
| 15 | Optional call date, contingent call dates and redemption amount | N/A | Any day, 100% |
| 16 | Subsequent call dates, if applicable | N/A | Any day |
| *Coupons / dividends* | | | |
| 17 | Fixed or floating dividend/coupon | Floating | Floating |
| 18 | Coupon rate and any related index | Depends on profit amount | Euribor 6M + 6.3% |
| 19 | Existence of a dividend stopper | No | No |

| | | | |
|---|---|---|---|
| 20a | Fully discretionary, partially discretionary or mandatory (in terms of timing) | Fully discretionary | Mandatory |
| 20b | Fully discretionary, partially discretionary or mandatory (in terms of amount) | Fully discretionary | Mandatory |
| 21 | Existence of step up or other incentive to redeem | No | No |
| 22 | Noncumulative or cumulative | N/A | Noncumulative |
| 23 | Convertible or non-convertible | N/A | Convertible |
| 24 | If convertible, conversion trigger(s) | N/A | No conversion trigger |
| 25 | If convertible, fully or partially | N/A | Fully |
| 26 | If convertible, conversion rate | N/A | 1:1 |
| 27 | If convertible, mandatory or optional conversion | N/A | Optional, at the option of both the holders and the issuer |
| 28 | If convertible, specify instrument type convertible into | N/A | Common Equity Tier 1 |
| 29 | If convertible, specify issuer of instrument it converts into | N/A | ProCredit Bank a.d. Beograd |
| 30 | Write-down features | No | No |
| 31 | If write-down, write-down trigger(s) | N/A | N/A |
| 32 | If write-down, full or partial | N/A | N/A |
| 33 | If write-down, permanent or temporary | N/A | N/A |
| 34 | If temporary write-down, description of write-up mechanism | N/A | N/A |
| 35 | Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument) | Supplementary capital | |
| 36 | Non-compliant transitioned features | N/A | N/A |
| 37 | If yes, specify non-compliant features | N/A | N/A |

| No. | Main features | | |
|---|---|---|---|
| 1 | Issuer | ProCredit Bank a.d. Beograd | ProCredit Bank a.d. Beograd |
| 2 | Unique identifier (e.g. CUSIP, ISIN or Bloomberg identifier for private placement) | N/A | N/A |
| 3 | Governing law(s) of the instrument | German Law | German Law |
| | Regulatory treatment | | |
| 4 | Transitional CRR rules | N/A | N/A |
| 5 | Post-transitional CRR rules | N/A | N/A |
| 6 | Eligible at solo/(sub-)consolidated/ solo&(sub-)consolidated | Solo and consolidated | Solo and consolidated |
| 7 | Instrument type (types to be specified by each jurisdiction) | Supplementary capital | Supplementary capital |
| 8 | Amount recognized in regulatory capital (Currency in million, as of most recent reporting date) | RSD 1,239 million | RSD 743 million |
| 9 | Nominal amount of instrument | RSD 1,239 million (equal to EUR 10 million) | RSD 743 million (equal to EUR 6 million) |
| 9a | Issue price | 100% | 100% |
| 9b | Redemption price | 100% | 100% |
| 10 | Accounting classification | Liability - amortized cost | Liability - amortized cost |
| 11 | Original date of issuance | 23.12.2011 | 18.10.2013 |
| 12 | Perpetual or dated | Dated | Dated |
| 13 | Original maturity date | 01.06.2025 | 18.10.2023 |
| 14 | Issuer call subject to prior supervisory approval | Yes | Yes |
| 15 | Optional call date, contingent call dates and redemption amount | Any day, 100% | Any day, 100% |
| 16 | Subsequent call dates, if applicable | Any day | Any day |
| *Coupons / dividends* | | | |
| 17 | Fixed or floating dividend/coupon | Floating | Floating |
| 18 | Coupon rate and any related index | Euribor 6M + 6.3% | Euribor 6M + 6.25% |
| 19 | Existence of a dividend stopper | No | No |

| | | | |
|---|---|---|---|
| 20a | Fully discretionary, partially discretionary or mandatory (in terms of timing) | Mandatory | Mandatory |
| 20b | Fully discretionary, partially discretionary or mandatory (in terms of amount) | Mandatory | Mandatory |
| 21 | Existence of step up or other incentive to redeem | No | No |
| 22 | Noncumulative or cumulative | Noncumulative | Noncumulative |
| 23 | Convertible or non-convertible | Convertible | Convertible |
| 24 | If convertible, conversion trigger(s) | No conversion trigger | No conversion trigger |
| 25 | If convertible, fully or partially | Fully | Fully |
| 26 | If convertible, conversion rate | 1:1 | 1:1 |
| 27 | If convertible, mandatory or optional conversion | Optional, at the option of both the holders and the issuer | Optional, at the option of both the holders and the issuer |
| 28 | If convertible, specify instrument type convertible into | Common Equity Tier 1 | Common Equity Tier 1 |
| 29 | If convertible, specify issuer of instrument it converts into | ProCredit Bank a.d. Beograd | ProCredit Bank a.d. Beograd |
| 30 | Write-down features | No | No |
| 31 | If write-down, write-down trigger(s) | N/A | N/A |
| 32 | If write-down, full or partial | N/A | N/A |
| 33 | If write-down, permanent or temporary | N/A | N/A |
| 34 | If temporary write-down, description of write-up mechanism | N/A | N/A |
| 35 | Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument) | | |
| 36 | Non-compliant transitioned features | N/A | N/A |
| 37 | If yes, specify non-compliant features | N/A | N/A |

Compared to previous year, the major change is that one of the subordinated debts of (RSD 1,859 million) was transferred from the previous lender (EFSE) to a new lender (ProCredit Holding). Therefore, it is similar to the other two subordinated loans. At the same time it contains changes in the maturity and interest margin.

The National Bank of Serbia made changes in its Decision on capital adequacy of banks that allow banks to prematurely repay subordinated debts, with previous NBS approval.

# Article 438 CRR

# Capital requirements

The capital requirements according to Serbian regulations are shown in the following table.

| in RSD m | 31.12.2016 | | 31.12.2015 | |
|---|---|---|---|---|
| | **Risk-weighted assets** | **Capital requirements** | **Risk-weighted assets** | **Capital requirements** |
| **Credit Risk** | **72,775** | **8,733** | **60,927** | **7,312** |
| Exposures to central governments or central banks | - | - | - | - |
| Exposures to regional governments or local authorities | - | - | - | - |
| Exposures to public sector entities | - | - | - | - |
| Exposures to multilateral development banks | - | - | - | - |
| Exposures to international organizations | - | - | - | - |
| Exposures to banks | 79 | 9 | 155 | 19 |
| Exposures to corporates | 46,477 | 5,577 | 33,985 | 4,078 |
| Retail exposures | 21,384 | 2,566 | 23,220 | 2,786 |
| Exposures secured by mortgages on immovable property | - | - | - | - |
| Exposures in default | 1,205 | 145 | 124 | 15 |
| Exposures associated with particularly high risk | - | - | - | - |
| Exposures in the form of covered bonds | - | - | - | - |
| Items representing securitization positions | - | - | - | - |
| Exposures to institutions and corporates with a short-term credit assessment | - | - | - | - |
| Exposures in the form of units or shares in collective investment undertakings (“CIUs”) | - | - | - | - |
| Equity exposures | - | - | - | - |
| Other items | 3,630 | 436 | 3,443 | 414 |
| **Market risks (foreign currency risk)** | **305** | **-** | **256** | **31** |
| **Operational risk** | **6,380** | **957** | **8,350** | **1,002** |
| **CVA risk** | **-** | **-** | **-** | **-** |
| **Total** | **79,460** | **9,690** | **69,533** | **8,344** |

There are several reasons for the increase in the total risk-weighted assets. Apart from the increase in the business segment, which is in line with the strategic orientation of the bank, there were essential changes in terms of the exposures classified as being in default, which additionally led to the increase of risk-weighted assets. Namely, the National Bank of Serbia made changes in its Decision on classification of the balance sheet assets and off-balance sheet items (August 2016) which enabled local banks with non-performing loans (NPL) up to 10% to exclude the reserves required by the NBS from the calculation of risk-weighted assets. Due to the respective change, the bank changed the definition of NPL exposures by widening it to encompass not only the exposures past due (90+ days in arrears), but also the exposures to entities in bankruptcy proceedings, entities deleted from the Serbian Business Agency’s Registry, entities classified in risk class 8, fraud case exposures, cases in litigation and the restructured impaired exposures. Due to this change in definition, the gross amount of exposures considered as being in default has risen, and considering the largest risk weights applied in accordance with the regulation, risk-weighted assets increased as a result. Consequently, since the change in definition enabled the bank to exclude the reserves required by the NBS from the calculation of the net amount of exposures used as the base for the calculation of risk-weighted assets on the total portfolio, an additional increase of risk-weighted assets in general was incurred. Accordingly, the increase in the risk-weighted assets resulted in an increase of the capital requirements by RSD 1,346 million in 2016 compared to the requirements for 2015.

The table below shows the regulatory capital ratios as of 31 December 2015 and 31 December 2016.

| | **Risk-weighted assets** | **Total capital ratio** | **Tier 1 capital ratio** | **Common equity Tier 1 capital ratio** |
|---|---|---|---|---|
| | in RSD m | in % | in % | in % |
| 31.12.2016 | 80,750 | 18.9 | 13.6 | 13.6 |
| 31.12.2015 | 69,533 | 15.7 | 10.5 | 10.5 |

At the end of December 2016, there was an increase in capital adequacy compared to the end of December 2015. The change was primarily due to the significant increase in Tier 1 capital and consequently Total Regulatory Capital. Namely, Tier 1 capital increased by RSD 3,675 million in 2016 compared to 2015, while Total Regulatory Capital increased by RSD 4,414 million in 2016 compared to 2015 due to the cancellation of the NBS's required reserve as a deductible item in the calculation of regulatory capital. Consequently, a greater increase in capital than the one incurred in the risk-weighted assets resulted in the increase of the capital ratios.

The bank has established a process for internal capital adequacy assessment, in accordance with Serbian regulations, which includes the following phases:

1. Identification (determination) of materially significant risks
2. Calculation of internal capital requirements for individual risks
3. Determination of total internal capital requirements
4. Determination of available internal capital
5. Comparison of the following elements:
   - amount of capital calculated in accordance with the NBS's Decision on capital adequacy of banks with the amount of available internal capital
   - minimum capital requirements calculated in accordance with the NBS's Decision on capital adequacy of banks and internal capital requirements for individual risks
   - sum of the minimum capital requirements calculated in accordance with the NBS's Decision on capital adequacy of banks and total internal capital requirements

Based on the comparisons, the bank analyses, presents and documents existing differences as part of the material prepared for the Assets and Liability Management Committee.

When determining the materially significant risks to which the bank is exposed and which are included in the process of internal capital adequacy assessment, the bank takes into account the type, scope, and complexity of business operations, as well as the specificity of the markets in which the bank operates. Previous experience regarding risk management in the bank and the ProCredit Group is also taken into consideration, as well as historical data on negative effects on the bank's financial result and capital.

Materially significant risks which are included in the calculations undertaken as part of internal capital adequacy assessment process:

- Credit risk: The bank calculates the regulatory capital requirement for credit risk in accordance with the NBS's Decision on capital adequacy of banks (standardised approach); the bank also calculates its internal capital requirement for credit risk using an internal model and compares it with the results of the calculation using the regulatory model in order to avoid a possible underestimation of credit risk due to the implementation of the standardised approach. The bank also performs a stress test for credit risk in order to avoid a possible underestimation of this risk due to the implementation of the standardised approach during a crisis.

- Counterparty risk: The bank calculates the regulatory capital requirement for counterparty risk in accordance with the NBS's Decision on capital adequacy of banks (standardised approach); the bank also calculates its internal capital requirement for counterparty risk using an internal model and compares it with the results of the calculation using the regulatory model in order to avoid possible underestimation of this risk due to the implementation of the standardised approach.

- Foreign currency risk (FX Risk): The bank calculates the regulatory capital requirement for foreign exchange risk in accordance with the NBS's Decision on capital adequacy of banks (standardised approach); the bank also calculates its internal capital requirement for foreign currency risk using an internal model (including a stress test scenario) and compares it with the results of the calculation using the regulatory model in order to avoid possible underestimation of this risk due to the implementation of the standardised approach.

- Operational risk: The bank calculates the regulatory capital requirement for operational risk in accordance with the NBS's Decision on capital adequacy of banks (basic indicator approach); the bank also calculates its internal capital requirement for operational risk using an internal model and compares it with the results of the calculation using the regulatory model in order to avoid possible underestimation of this risk due to the implementation of the basic indicator approach.

- Interest rate risk: Interest rate is inherent to banking business. Since the NBS's Decision on capital adequacy of banks does not envisage a regulatory capital allocation for this risk, it is assessed as significant in the internal capital adequacy assessment process. The bank defines the internal capital requirement for this risk by calculating the negative impact of interest rate changes on the economic value of the bank.

- Concentration risk: The bank is exposed to concentration risk on the basis of exposure to large clients, as well as on the basis of exposure concentration in certain business sectors and activities, and consequently in its internal capital adequacy assessment process, the bank assesses concentration risk to be materially significant. Since concentration risk is not covered by the regulatory capital requirement, the bank calculates its internal capital requirement for concentration risk on the basis of an internal model.

- Foreign currency risk included in credit risk: The bank uses an internal model to calculate its internal capital requirement for foreign currency risk included in credit risk.

For risks that cannot be quantified precisely (liquidity risk, strategic risk, business and macroeconomic environment risk) the bank has defined a set of guidelines, methods, criteria and processes for making and implementing decisions on acceptance, avoidance, reduction, control and transfer of risk.

In addition, the bank allocates 3% of the available internal capital for materially significant risks that cannot be precisely quantified, taking into account the ways in which the abovementioned risks are managed.

To conclude, the bank has identified the possibility of underestimating the risk from Pillar 1 (risks for which the minimum capital requirements are calculated in accordance with the NBS's Decision on capital adequacy of banks) when calculating regulatory capital adequacy due to application of the standardised approach for credit risk, counterparty risk and foreign currency risk, and the basic indicator approach for operational risk, which is why the bank calculates the risk exposure in line with internal models and in the case of underestimation allocates additional capital by calculating the required level of internal capital. The bank's capital adequacy remains sufficient as per the internal capital adequacy assessment model, as of the end of 2016.

## Article 440 CRR

## Capital buffer

According to current Serbian regulations, no capital buffers are required.

## Article 442 CRR

## Credit risk adjustments

For quantitative information on the bank's exposure to credit risk and dilution risk, please refer to the following tables, which show the risk broken down by categories, industry and residual contractual maturities.

| in RSD m | Average amount of exposures of the 4 quarters 2016 | Total amount of exposures 31.12.2016 | Average amount of exposures of the 4 quarters 2015 | Total amount of exposures 31.12.2015 |
|---|---|---|---|---|
| Exposures to central governments or central banks | 6,628 | 3,703 | 9,422 | 8,499 |
| Exposures to regional governments or local authorities | 0 | 0 | - | - |
| Exposures to public sector entities | 302 | - | 492 | 385 |
| Exposures to multilateral development banks | - | - | - | - |
| Exposures to international organizations | - | - | - | - |
| Exposures to institutions | 623 | 362 | 745 | 1,152 |
| Exposures to corporates | 59,911 | 65,938 | 37,326 | 51,939 |
| Retail exposures | 36,713 | 35,173 | 37,480 | 37,988 |
| Exposures secured by mortgages on immovable property | - | - | - | - |
| Exposures in default | 2,044 | 1,877 | 2,182 | 2,097 |
| Exposures associated with particularly high risk | - | - | - | - |
| Exposures in the form of covered bonds | - | - | - | - |
| Items representing securitization positions | - | - | - | - |
| Exposures to institutions and corporates with a short-term credit assessment | - | - | - | - |
| Exposures in the form of units or shares in collective investment undertakings (“CIUs”) | - | - | - | - |
| Equity exposures | - | - | - | - |
| Other items | 154,898 | 156,752 | 153,780 | 160,275 |
| **Total** | **261,118** | **263,806** | **241,427** | **262,335** |

According to Serbian regulations, all on-balance sheet asset positions and all off-balance sheet items must be included in the total exposures. Also, off-balance sheet collateral items assigned to a low-risk category (0%) have no impact on risk-weighted assets and the capital requirement for credit risk. As of December 2015, the bank has included in client exposures an off-balance sheet position for a credit framework agreement (low-risk category (0%); no impact on risk-weighted assets or the capital requirement for credit risk). This change, required by the National Bank of Serbia, led to an increase in total exposures to businesses compared with the year 2014. The same principle remained in 2016, i.e. credit framework agreements remained included in client exposure. There were no significant changes compared to the year 2015.

| **31.12.2016**<br>in RSD m | **Financial institution, government and central bank** | **Agri-culture** | **Industry and other production** | **Trade** | **Services** | **Other** |
|---|---|---|---|---|---|---|
| Exposures to central governments or central banks | 3,703 | - | - | - | - | - |
| Exposures to regional governments or local authorities | 0 | - | - | - | - | - |
| Exposures to public sector entities | - | - | - | - | - | - |
| Exposures to multilateral development banks | - | - | - | - | - | - |
| Exposures to international organizations | - | - | - | - | - | - |
| Exposures to institutions | 362 | - | - | - | - | - |
| Exposures to corporates | - | 16,053 | 18,100 | 19,826 | 6,884 | 5,076 |
| Thereof SME | - | 7,126 | 16,126 | 18,332 | 6,464 | 3,603 |
| Retail exposures | - | 13,954 | 3,199 | 4,177 | 4,201 | 9,642 |
| Thereof SME | - | 162 | 1,888 | 2,824 | 2,314 | 1,266 |
| Exposures secured by mortgages on immovable property | - | - | - | - | - | - |
| Exposures in default | 233 | 262 | 457 | 412 | 204 | 308 |
| Exposures associated with particularly high risk | - | - | - | - | - | - |
| Exposures in the form of covered bonds | - | - | - | - | - | - |
| Items representing securitization positions | - | - | - | - | - | - |
| Exposures to institutions and corporates with a short-term credit assessment | - | - | - | - | - | - |
| Exposures in the form of units or shares in collective investment undertakings (“CIUs”) | - | - | - | - | - | - |
| Equity exposures | - | - | - | - | - | - |
| Other items | - | - | - | 1 | 24 | 156,727 |
| **Total** | **4,298** | **30,269** | **21,756** | **24,416** | **11,313** | **171,754** |

| **31.12.2015**<br>in RSD m | **Financial institution, government and central bank** | **Agri-culture** | **Industry and other production** | **Trade** | **Services** | **Other** |
|---|---|---|---|---|---|---|
| Exposures to central governments or central banks | 8,499 | - | - | - | - | - |
| Exposures to regional governments or local authorities | - | - | - | - | - | - |
| Exposures to public sector entities | 385 | - | - | - | - | 0 |
| Exposures to multilateral development banks | - | - | - | - | - | - |
| Exposures to international organizations | - | - | - | - | - | - |
| Exposures to banks | 1,152 | - | - | - | - | - |
| Exposures to corporates | - | 12,960 | 9,972 | 17,209 | 6,556 | 5,241 |
| Thereof SME | - | 6,335 | 8,970 | 15,700 | 6,027 | 2,881 |
| Retail exposures | - | 14,260 | 3,248 | 5,336 | 5,988 | 9,157 |
| Thereof SME | - | 232 | 1,691 | 3,316 | 3,169 | 1,202 |
| Exposures secured by mortgages on immovable property | - | - | - | - | - | - |
| Exposures in default | - | 337 | 263 | 482 | 508 | 507 |
| Exposures associated with particularly high risk | - | - | - | - | - | - |
| Exposures in the form of covered bonds | - | - | - | - | - | - |
| Items representing securitization positions | - | - | - | - | - | - |
| Exposures to institutions and corporates with a short-term credit assessment | - | - | - | - | - | - |
| Exposures in the form of units or shares in collective investment undertakings (“CIUs”) | - | - | - | - | - | - |
| Equity exposures | - | - | - | - | - | - |
| Other items | - | - | - | 10 | 30 | 160,235 |
| **Total** | **10,036** | **27,557** | **13,483** | **23,037** | **13,082** | **175,140** |

The breakdown of the loan portfolio according to economic sector did not change significantly compared to the previous year.

Please note that the local definition for SMEs is used, i.e. the category SME includes companies classified according to Serbian accounting and auditing rules.

Legal entities are classified as “Small” if they meet more than two of the following conditions:

1. average number of employees: 10
2. operating income: EUR 700,000
3. average value of operating assets: EUR 350,000

But they may not exceed two of the following criteria:

1. average number of employees: 50
2. operating income: EUR 8.8 million
3. average value of operating assets: EUR 4.4 million

Legal entities are classified as “Medium” if they meet more than two of the following conditions:

1. average number of employees: 50
2. operating income: EUR 8.8 million
3. average value of operating assets: EUR 4.4 million

But they may not exceed two of the following criteria:

1. average number of employees: 250
2. operating income: EUR 35 million

Average value of operating assets: EUR 17.5 million

| **31.12.2016**<br>in RSD m | **<1 Year** | **1-5 Years** | **>5 Years** | **Without maturity** |
|---|---|---|---|---|
| Exposures to central governments or central banks | 23 | - | - | 3,680 |
| Exposures to regional governments or local authorities | - | - | - | 0 |
| Exposures to public sector entities | - | - | - | - |
| Exposures to multilateral development banks | - | - | - | - |
| Exposures to international organizations | - | - | - | - |
| Exposures to institutions | 30 | 10 | - | 322 |
| Exposures to corporates | 21,698 | 19,336 | 12,167 | 12,738 |
| Retail exposures | 9,906 | 13,325 | 7,850 | 4,093 |
| Exposures secured by mortgages on immovable property | - | - | - | - |
| Exposures in default | 1,091 | 281 | 130 | 376 |
| Exposures associated with particularly high risk | - | - | - | - |
| Exposures in the form of covered bonds | - | - | - | - |
| Items representing securitization positions | - | - | - | - |
| Exposures to institutions and corporates with a short-term credit assessment | - | - | - | - |
| Exposures in the form of units or shares in collective investment undertakings (“CIUs”) | - | - | - | - |
| Equity exposures | - | - | - | - |
| Other items | 18 | 16 | - | 156,718 |
| **Total** | **32,765** | **32,967** | **20,146** | **177,928** |

| 31.12.2015<br>in RSD m | <1 Year | 1-5 Years | >5 Years | Without maturity |
|---|---|---|---|---|
| Exposures to central governments or central banks | - | - | - | 8,499 |
| Exposures to regional governments or local authorities | - | - | - | - |
| Exposures to public sector entities | - | - | - | 385 |
| Exposures to multilateral development banks | - | - | - | - |
| Exposures to international organizations | - | - | - | - |
| Exposures to banks | 46 | - | - | 1,105 |
| Exposures to corporates | 17,493 | 16,938 | 5,538 | 11,970 |
| Retail exposures | 9,971 | 17,040 | 7,057 | 3,920 |
| Exposures secured by mortgages on immovable property | - | - | - | - |
| Exposures in default | 1,251 | 515 | 178 | 153 |
| Exposures associated with particularly high risk | - | - | - | - |
| Exposures in the form of covered bonds | - | - | - | - |
| Items representing securitization positions | - | - | - | - |
| Exposures to institutions and corporates with a short-term credit assessment | - | - | - | - |
| Exposures in the form of units or shares in collective investment undertakings ("CIUs") | - | - | - | - |
| Equity exposures | - | - | - | - |
| Other items | 12 | 32 | - | 160,231 |
| **Total** | **28,773** | **34,526** | **12,773** | **186,263** |

The breakdown of the portfolio according to exposure maturity increased slightly compared to 2015. In absolute values, the biggest increases are related to the corporate sector, which also had an increase in portfolio in 2016 compared to 2015, but the share of exposure maturities in this sector is stable.

A materially significant amount is an amount higher than 1% of a single account receivable of the bank, but not lower than RSD 1,000 if the borrower is a private individual client or RSD 10,000 if the borrower is a legal entity.

For accounting purposes impaired exposures are all individual past due items for which the obligor is in arrears between 30 and 91 days.

At each balance sheet date or, if deemed necessary, ad hoc the bank assesses whether signs of impairment can be identified. The impairment loss is then determined. Depending on the size of the credit exposure, such losses are either calculated on an individual credit exposure basis (specific provision) or are collectively assessed for a portfolio of credit exposures (general provision). The regular assessment for objective evidence of impairment is applicable for all on-balance sheet credit exposures, regardless of their size. Accordingly, the following indicators are signs of impairment:

- arrears of more than 30 days
- the bank has initiated court procedures
- bankruptcy proceedings have been initiated
- breach of covenants or conditions, unless the bank has decided to waive or modify the covenant or condition
- all or part of the off-balance sheet exposure of a client shows signs of impairment
- any specific information on the client's business or changes in the client's market environment that has or is expected to have a negative impact on the future cash flow

Individually assessed credit exposures include credit exposures that show signs of impairment, for which an impairment test is performed and where an impairment loss has been confirmed. They are provisioned according to the impairment loss that is determined by an assessment for specific individual impairment.

Credit exposures for which the bank determines that no objective evidence of impairment exists are collectively assessed (portfolio-based).

Collectively assessed credit exposures are provisioned as follows:

- Portfolio-based provisions – individually insignificant and individually significant credit exposures that do not show signs of impairment are provisioned according to the results of the migration analysis and according to their similar risk characteristics. Individually insignificant and individually significant credit exposures that display signs of impairment and for which the impairment test showed no impairment are also included in this group and provisioned accordingly.
- Lump-sum specific provisions – individually insignificant credit exposures that show signs of impairment and for which an impairment test in the form of an assessment for specific individual impairment is not performed because the operational expenses do not justify this are provisioned according to the results of the migration analysis and according to their similar risk characteristics. All credit exposures for which the bank determines that they belong to a cluster of clients that are considered to be impaired due to external influences and/or extraordinary events are also grouped here and lump-sum specific provisions are determined.

| **31.12.2016**<br>in RSD m | **Past-due but not impaired exposures** | **Impaired exposures** | **Individual specific provisions** | **Lump-sum specific provisions** | **Portfolio-based provisions** | **Charges for specific credit risk adjustments** |
|---|---|---|---|---|---|---|
| Financial institution, government and central bank | - | - | - | - | - | - |
| Agriculture | 262 | 103 | 86 | 53 | 211 | - |
| Industry and other production | 457 | 36 | 160 | 28 | 144 | - |
| Other | 308 | 57 | 99 | 549 | 189 | - |
| Services | 204 | 62 | 51 | 45 | 65 | - |
| Trade | 412 | 48 | 158 | 66 | 150 | - |
| **Total 2015** | **1,644** | **306** | **553** | **741** | **759** | **-** |

| **31.12.2015**<br>in RSD m | **Past-due but not impaired exposures** | **Impaired exposures** | **Individual specific provisions** | **Lump-sum specific provisions** | **Portfolio-based provisions** | **Charges for specific credit risk adjustments** |
|---|---|---|---|---|---|---|
| Financial institution, government and central bank | - | - | - | - | - | - |
| Agriculture | 337 | 106 | 118 | 192 | 246 | 20 |
| Industry and other production | 263 | 59 | 122 | 64 | 112 | -4 |
| Other | 507 | 27 | 13 | 193 | 138 | -25 |
| Services | 508 | 105 | 165 | 144 | 103 | 17 |
| Trade | 482 | 67 | 204 | 128 | 174 | 3 |
| **Total 2015** | **2,097** | **365** | **622** | **720** | **774** | **10** |

| **31.12.2016**<br>in RSD m | **Specific provisions** | **General provisions** |
|---|---|---|
| Carrying amount as at 1 January 2016 | 668 | 1,447 |
| Additions | 812 | 3,138 |
| Utilization | - | 280 |
| Releases | 885 | 2,820 |
| Transfers | - | - |
| Unwinding effects | 51 | - |
| Exchange rate adjustments | 9 | 16 |
| Carrying amount as at 31 December 2016 | 553 | 1,501 |

| **31.12.2015**<br>in RSD m | **Specific provisions** | **General provisions** |
|---|---|---|
| Carrying amount as at 1 January 2015 | 557 | 1,549 |
| Additions | 1,161 | 3,052 |
| Utilization | - | 185 |
| Releases | 1,054 | 2,933 |
| Transfers | - | - |
| Unwinding effects | 42 | - |
| Exchange rate adjustments | - | 11 |
| Carrying amount as at 31 December 2015 | 622 | 1,494 |

| | **Increase of risk provisioning** | | **Release of risk provisioning** | | **Direct write-offs** | **Recoveries of write-offs** | **Total** |
|---|---|---|---|---|---|---|---|
| in RSD m | **Specific provisions** | **General provisions** | **Specific provisions** | **General provisions** | | | |
| Total 2016 | 812 | 3,138 | 885 | 2,820 | 27 | 203 | 69 |
| Total 2015 | 1,161 | 3,052 | 1,096 | 3,118 | 29 | 250 | -221 |

# Article 450 CRR

# Remuneration policy

The HR Committee is the main body overseeing HR questions. It meets 12 times per year. The same body decides on remuneration once per year (in May).

The HR Committee consists of two representatives of the Executive Board, one member of the HR department, and two managers from the business structure/network.

ProCredit Bank does not use the services of external consultants. The salary structure is in line with the salary scheme defined by ProCredit Holding for all ProCredit banks. All members of the HR Committee have an equal role and equal rights in the decision-making process.

The following table shows the remuneration of the members of the Executive Board and the risk-takers (according to delegated act (EU) No. 604/2014) of the bank.

| 31.12.2016 | Fixed remuneration | Variable remuneration | | | | Number of beneficiaries |
|---|---|---|---|---|---|---|
| in '000 EUR | | Cash | Shares | Share-linked instruments | Other types | |
| Management body | 288 | - | - | - | - | 5 |
| Other "risk takers" | 797 | - | - | - | - | 27 |

The following remuneration components are not applicable for ProCredit Bank: outstanding deferred remuneration; deferred remuneration awarded during the financial year, paid out and reduced through performance adjustments; signed-on payments and severance payments for the year 2016.

# Article 451 CRR

# Leverage

According to current Serbian regulations, no requirements have been published concerning the leverage ratio.

Nevertheless, the bank, as a group member, follows group standards and monitors leverage ratio. The leverage ratio according to the CRR equals to 12.0% as at 31 December 2016. The limit established is 5%.

# Article 453 CRR

# Credit risk mitigation techniques

To modify the risk-weighted exposure amounts for credit risk by the effects of risk mitigation techniques, a bank may use the following credit protection instruments:

1. funded credit protection instruments:
   - financial collateral
   - on-balance sheet netting
   - master netting agreements
   - other funded credit protection instruments
2. unfunded credit protection instruments:
   - guarantees, other forms of surety and counter-guarantees (including other similar instruments of unfunded credit protection)
   - credit derivatives

For the purpose of calculating risk-weighted assets ProCredit Bank did not apply risk mitigation techniques that are available (financial collateral – cash deposit and guarantees issued by banks).