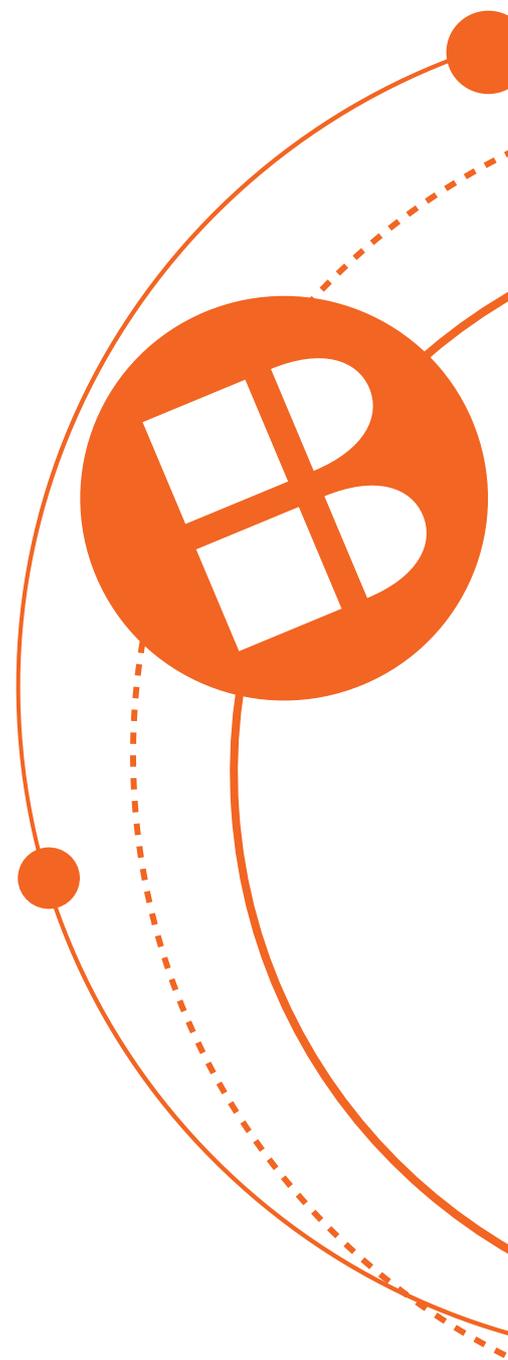


# ANNUAL REPORT 2017



 **HIPOTEKARNA  
BANKA**  
*Vama posvećena*

# ANNUAL REPORT

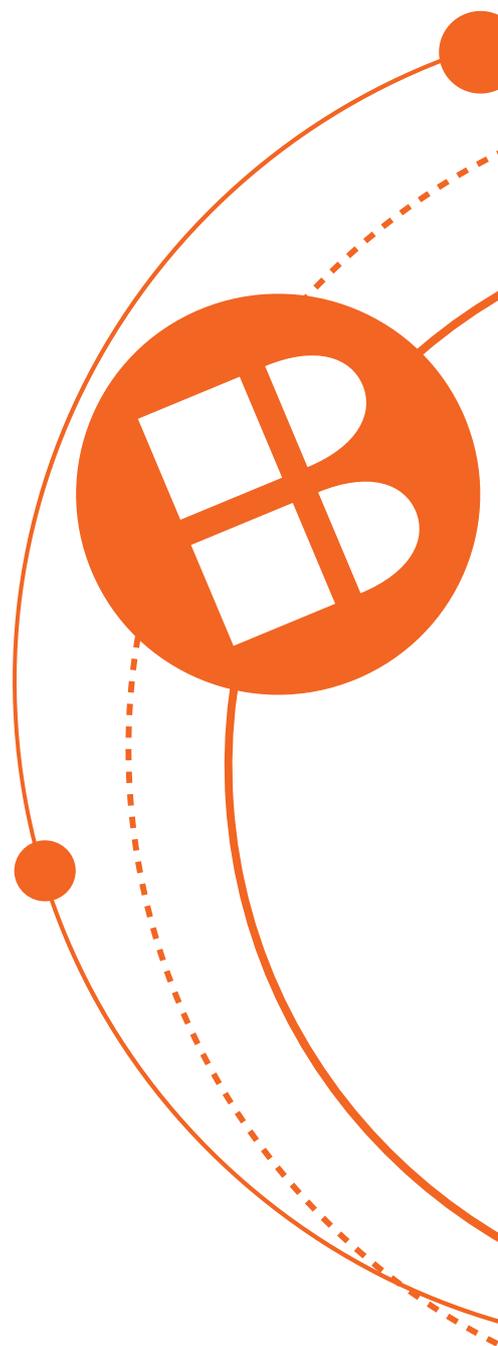
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2017

Report of the Chairman of the  
Board of Directors and  
Report of the Chief Executive Officer

 **HIPOTEKARNA  
BANKA**

*Vama posvećena*



## REPORT OF THE CHAIRMAN OF THE BOARD OF DIRECTORS

Dear clients, partners, and shareholders,

On behalf of the Board of Directors, I am honoured to present to you the Hipotekarna Bank AD Podgorica 2017 Annual Report.

Following the years of unprecedented interest rates, last year was the year of facing the reality filled with market and economic challenges. The first half of 2017 saw an overall improvement in the political and economic setting, which followed a long-term optimistic trend that had commenced a few years before. In the second half of the year, the audit of accounting and regulatory standards concerning every material aspect of the banking business, together with the introduction of MSFI 9 within a short time frame, remained among the most widely discussed issues of the banking sector in Montenegro and beyond, across the continent.

The Board of Directors co-operated closely with the management team on a series of issues. For our strategy to be fully implemented, we need to focus on key segments of the market, customer care, expenditure leadership, capital efficiency and thorough profiling of the Bank from the point of view of risk and financing. It is these attributes that should guide the Bank towards achieving a growth in revenues and capital value and its overall objective to be recognised as one of the best financial companies in the country. Given the challenges in the Bank's immediate environment, we are happy to have increased revenues, profit and market share in a large number of our operations.

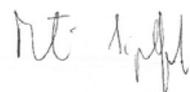
This report comes at the end of another successful year. The year which saw a growth in our profitability. Again, we managed to grow faster than our local competitors. The Bank increased its market share and all the relevant business parameters and recorded a 16.34% profit growth at the same time. The solvency coefficient at year end was 12.36%, together with a 9.36% capital return.

While maintaining a high solvency level, we demonstrated solid competences in assets and risk management, which is yet another indicator that the Bank remains committed to its strategic objective of long-term successful operation. We have made a substantial progress towards developing into a strong and stable bank, a bank better suited to cater for its client needs.

Investment into human capital is part and parcel of any sustainable business success. Hipotekarna Bank AD Podgorica offers ongoing professional development courses to its workforce, bearing in mind at all times that professional workforce and commitment to our clients are among the top priorities of our organisation.

Let me conclude by thanking first to our employees for their full commitment over the past year, as well as our clients who give us the opportunity to serve their needs, but also to our shareholders for their trust in Hipotekarna Bank prosperous future.

Sigilfredo Montinari  
Chairman of the Board of Directors



## REPORT OF THE CHIEF EXECUTIVE OFFICER

Dear clients, partners, and shareholders,

On behalf of Hipotekarna Bank management, and my own behalf, I have the honour of sharing with you our successful business results achieved in 2017.

Competition in Montenegro's banking sector is getting ever stronger, with an increased share of medium-size banks compared to that of relatively big banks as a result. Some of the issues the banks had been facing over the years, such as a sudden deposits outflow and illiquidity of some banks, seem to have almost disappeared since for a long period of time now both individual and system level liquidity indicators have been above prudential limits. The reasons for added optimism are also to be found in the preparation for the introduction of challenging international accounting standards in banking business as well as positive developments in the EU integration process, which is conducive to a positive image of Montenegro in the international community and improves the business environment in the country.

2017 saw a growth in all of the Bank activities in every segment of its operations compared to 2016. Assets and deposits grew by 15.4% and 17.7% respectively, while loan placements were at 222 million, with the Bank being positioned as the leader in terms of the scope of activities in financial markets in Montenegro's banking sector. All measurement and stress testing indicated that the Bank stood above applicable standards. Throughout the year, the Bank maintained a prescribed liquidity level, assets and liabilities term conformity, currency positions were harmonised, capital adequacy rates were stable, and securities portfolio was increased, which also served as a secondary source of liquidity and a source of additional profitability. We expect this positive trend to continue in 2018 and to maintain last year's levels.

Hipotekarna Bank AD Podgorica did not face any major challenges with loans servicing. In taking decisions on loan placements, we were guided by the assessment of client's good standing, and placed much less emphasis on security instruments in the absence of a positive quality assessment for the projects to be financed. We showed readiness and openness to finance all quality projects that were realistic and promised profitability.

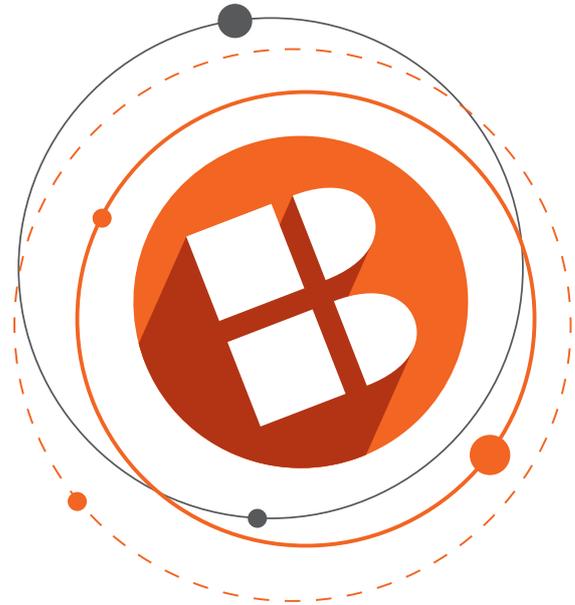
Hipotekarna Bank AD Podgorica will continue supporting quality investment projects and expand the scope of its loan activities in all segments, with reduced interest rates and adequate risk assessment. We will specially target innovations aiming to improve efficiency and quality of business in order to meet the needs of our clients in the simplest possible way. In the coming period, we will develop and optimise our business network, strengthen our market share and continue recruiting specialised workforce able to respond to challenges brought about by the market reality.

The best indicator of Bank success is the results achieved. Our success is an indicator of trust that our clients have in the Bank, which comes as a result of the Bank's responsible attitude to its clients and commitment of the Bank's entire motivated team. Following up on our earlier positive experience, training and professional development of our workforce will remain our top priority so that the Bank can maintain its long-term partnership with its clients, and reflected this relationship into Bank's ongoing commitment to fully meeting their needs and maintaining continuity in successful business operations that put the Bank in the leading position among Montenegro's most efficient banks.

I would like to avail myself of this opportunity to thank my colleagues in the Board of Directors, the management, and entire staff of Hipotekarna Bank for a successful 2017. On behalf of the management, I would like to thank our shareholders for their support and all our clients and partners for their trust and co-operation.

Esad Zaimović  
Chief Executive Officer





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# 1 INDEPENDENT AUDIT REPORT



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Svetlane Kane Radević 3  
81000 Podgorica  
Montenegro

Tel./Fax: +382 (0)20 20 14 80  
www.kpmg.com/me

## **TRANSLATION**

TO THE SHAREHOLDERS

HIPOTEKARNA BANKA AD, PODGORICA

### **Independent Auditors' Report**

We have audited the accompanying financial statements of Hipotekarna banka AD, Podgorica (hereinafter: "the Bank"), which comprise the balance sheet as at 31 December 2017, the income statement, statement of changes in equity and cash flow statement for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

#### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and true and fair view of these financial statements in accordance with the applicable Law on Accounting of Montenegro and other legislation that regulates financial reporting of banks in Montenegro and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

#### *Auditor's Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the applicable legislation that regulates audit in Montenegro. Those legislations that regulate accounting and audit require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error.

In making those risk assessments, we consider internal control relevant to the preparation and true and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting principles used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

*Opinion*

In our opinion the financial statements give true and fair view of the financial position of the Bank as at 31 December 2017, and of its financial performance and its cash flows for the year then ended in accordance with the applicable Law on Accounting of Montenegro and other legislation that regulates financial reporting of banks in Montenegro.

*Other Matter*

*Annual Management Report*

Management is responsible for the preparation and presentation of the Annual Management Report.

Our opinion on the financial statements does not cover the Annual Management Report and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the Annual Management Report and, in doing so, consider whether the Annual Management Report is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

In accordance with the requirements of the Law on Accounting in Montenegro we considered whether the Annual Management Report has been prepared in accordance with the requirements of Articles 11, 12, 13 and 14 of that Law.

Based solely on the work required to be undertaken in the course of the audit of the financial statements and the procedure above, in our opinion:

- the information given in the Annual Management Report for the financial year for which the financial statements are prepared, is consistent with the financial statements;
- the Annual Management Report has been prepared in accordance with the requirements of Articles 11, 12, 13 and 14 of the Law on Accounting in Montenegro.

In addition, in light of the knowledge and understanding of the Bank and its environment obtained in the course of the audit, we are also required to report if we have identified material misstatements in the Annual Management Report. We have nothing to report in this respect.

Podgorica, 28 May 2018

KPMG d.o.o. Podgorica

(L.S.)

Branko Vojnović  
Certified auditor

*This is a translation of the original Independent Auditor's Report issued in the Montenegrin language. All due care has been taken to produce a translation that is as faithful as possible to the original. However, if any questions arise related to interpretation of the information contained in the translation, the Montenegrin version of the document shall prevail. We assume no responsibility for the correctness of the English translation of the Bank's financial statements.*

Podgorica, 28 May 2018

KPMG d.o.o. Podgorica



Branko Vojnović  
Certified auditor

**HIPOTEKARNA BANKA A.D., PODGORICA**  
**TRANSLATION**

**INCOME STATEMENT**  
**for the year ended December 31, 2017**  
**(Thousands of EUR)**

	<b>Note</b>	<b>2017</b>	<b>2016</b>
Interest income	3.1., 5a	17,547	17,704
Interest expense	3.1., 5b	(4,685)	(5,316)
<b>Net interest income</b>		<b>12,862</b>	<b>12,388</b>
Dividend income		72	71
Impairment losses	3.7., 6	(3,426)	(2,811)
Provision charges	3.7., 6	207	(670)
Fee and commission income	3.1., 7a	12,972	10,644
Fee and commission expense	3.1., 7b	(5,880)	(4,463)
<b>Net fee and commission income</b>		<b>7,092</b>	<b>6,181</b>
Net gains on investment securities		300	203
Foreign exchange gains, net		652	775
Staff costs	8	(4,807)	(4,622)
General and administrative expenses	9	(8,224)	(7,008)
Depreciation/amortization charge	10	(836)	(849)
Other expenses	11	(38)	(218)
Other income	12	497	545
<b>OPERATING PROFIT</b>		<b>4,351</b>	<b>3,985</b>
Income taxes	3.4, 13	(408)	(361)
<b>PROFIT FOR THE YEAR</b>		<b>3,943</b>	<b>3,624</b>
Earnings per share / in EUR	34	125.95	115.76

Notes are an integral part of these financial statements

These financial statements were approved by the management of Hipotekarna banka A.D., Podgorica, in Podgorica, as at May 3, 2018.

Approved by and signed on behalf of Hipotekarna banka A.D., Podgorica by:

\_\_\_\_\_  
Esad Zaimović  
Chief Executive Officer

\_\_\_\_\_  
Božo Đurašković  
Executive Director for Business Support

**BALANCE SHEET**  
**as at December 31, 2017**  
**(Thousands of EUR)**

	<u>Note</u>	<u>December 31, 2017</u>	<u>December 31, 2016</u>
<b>ASSETS</b>			
Cash and deposit accounts held with central banks	3.6., 14	131,166	99,455
Loans and receivables from banks	3.6, 15	50,152	15,481
Loans and receivables from customers	3.5, 16	215,438	216,049
Investment securities			
- available for sale	3.5, 17	92,572	75,809
- held to maturity	3.5, 17	-	16,785
Investments in associates and joint ventures at equity method		8	8
Property, plant and equipment	3.8, 18	1,437	1,501
Intangible assets	19	1,658	1,498
Current tax assets		-	48
Deferred tax assets	13c	38	33
Other financial receivables	20	984	842
Other operating receivables	21	1,082	1,281
<b>TOTAL ASSETS</b>		<b><u>494,535</u></b>	<b><u>428,790</u></b>
<b>LIABILITIES</b>			
Deposits due to banks	22	3,059	303
Deposits due to customers	23	391,657	333,350
Borrowings from other customers	24	29,936	35,331
Provisions	25	1,636	2,004
Current tax liabilities		451	389
Deferred tax liabilities	13c	311	114
Other liabilities	26	8,692	8,490
Subordinated debt	27	14,012	9,967
<b>TOTAL LIABILITIES</b>		<b><u>449,754</u></b>	<b><u>389,948</u></b>
<b>EQUITY</b>			
Share capital	28	16,006	16,006
Share issue premium		7,444	7,444
Retained earnings		8,774	5,462
Other reserves		12,557	9,930
<b>TOTAL EQUITY</b>		<b><u>44,781</u></b>	<b><u>38,842</u></b>
<b>TOTAL EQUITY AND LIABILITIES</b>		<b><u>494,535</u></b>	<b><u>428,790</u></b>
<b>OFF-BALANCE SHEET ITEMS</b>	30	<b><u>574,581</u></b>	<b><u>542,974</u></b>

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Approved by and signed on behalf of Hipotekarna banka A.D., Podgorica by:

\_\_\_\_\_  
Esad Zaimović  
Chief Executive Officer

\_\_\_\_\_  
Božo Đurašković  
Executive Director for Business Support

**HIPOTEKARNA BANKA A.D., PODGORICA**  
**TRANSLATION**

**STATEMENT OF CHANGES IN EQUITY**  
**for the year ended December 31, 2017**  
**(Thousands of EUR)**

	<u>Share Capital</u>	<u>Share Issue Premium</u>	<u>Retained earnings</u>	<u>Other Reserves</u>	<u>Total</u>
<b>Balance at December 31, 2016</b>	16,006	7,444	2,729	8,226	<b>34,405</b>
Effects of fair value adjustment of available-for sale securities	-	-	-	813	<b>813</b>
Transfer of profit	-	-	(891)	891	-
Profit for the year	-	-	3,624	-	<b>3,624</b>
<b>Balance at December 31, 2016</b>	<b><u>16,006</u></b>	<b><u>7,444</u></b>	<b><u>5,462</u></b>	<b><u>9,930</u></b>	<b><u>38,842</u></b>
Effects of fair value adjustment of available-for sale securities	-	-	-	1,996	<b>1,996</b>
Transfer of profit	-	-	(631)	631	-
Profit for the year	-	-	3,943	-	<b>3,943</b>
<b>Balance at December 31, 2017</b>	<b><u>16,006</u></b>	<b><u>7,444</u></b>	<b><u>8,774</u></b>	<b><u>12,557</u></b>	<b><u>44,781</u></b>

Notes are an integral part of these financial statements

These financial statements were approved by the management of Hipotekarna banka A.D., Podgorica, in Podgorica, as at May 3, 2018.

Approved by and signed on behalf of Hipotekarna banka A.D., Podgorica by:

\_\_\_\_\_  
Esad Zaimović  
Chief Executive Officer

\_\_\_\_\_  
Božo Đurašković  
Executive Director for Business Support

**STATEMENT OF CASH FLOWS**  
**for the year ended December 31, 2017**  
*(Thousands of EUR)*

	<u>2017</u>	<u>2016</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Inflows from interest and similar income	17,608	17,878
Outflows from interest and similar expenses	(4,814)	(4,768)
Inflows from fee and commission	12,972	10,644
Outflows from fees and commissions	(5,880)	(4,463)
Cash paid to employees and suppliers	(13,504)	(13,579)
Increases in loans and other assets	(1,890)	(27,977)
Inflows from deposits and other liabilities	61,903	18,149
Income taxes paid	(902)	(845)
Other inflows	(14,462)	(8,644)
<b>Net cash inflow/(outflow) from operating activities</b>	<u><b>51,031</b></u>	<u><b>(13,605)</b></u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchase of property, plant and equipment	(519)	(449)
Purchase of intangible assets	(688)	(689)
Treasury bills	17,422	(12,820)
Inflows from sales of tangible and fixed assets	3	127
<b>Net cash (outflow) from investing activities</b>	<u><b>16,218</b></u>	<u><b>(13,831)</b></u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Increase in borrowings	(1,372)	(5,837)
<b>Net cash inflow/(outflow) from financing activities</b>	<u><b>(1,372)</b></u>	<u><b>(5,837)</b></u>
Effect of foreign exchange in cash and cash equivalents	651	775
<b>Net increase/(decrease) in cash and cash equivalents</b>	66,528	(32,498)
<b>Cash and cash equivalents at the beginning of the year</b>	<u>116,468</u>	<u>148,966</u>
<b>Cash and cash equivalents at the end of the year (Note 31)</b>	<u><b>182,996</b></u>	<u><b>116,468</b></u>

Notes are an integral part of these financial statements

These financial statements were approved by the management of Hipotekarna banka A.D., Podgorica, in Podgorica, as at May 3, 2018.

Approved by and signed on behalf of Hipotekarna banka A.D., Podgorica by:

\_\_\_\_\_  
 Esad Zaimović  
 Chief Executive Officer

\_\_\_\_\_  
 Božo Đurašković  
 Executive Director for Business Support



## EQUITY

The Bank's total equity was €44.780 million on 31/12/2017, up by 15.29% over the previous year.

On 31 Dec 2017, the nominal value of shareholders' equity was €16.006 million.

Shareholders' equity consists of 31,305 shares, €511.29 nominal value each.

Corporate and retail clients account for 78% of Bank's ownership structure, while the remaining equity is held by domestic corporate and retail entities.

## PROFIT AND LOSS ACCOUNT

In 2017, the Bank earned a profit of €3.943 million. Interest income dropped by 0.88% over the previous year and amounted to EUR17,547 million, which came as a result of declining loan activities and a drop in interest rates.

Fee revenues rose by 21.87% over the previous year and amounted to €12.972 million. Net fee revenues accounted for 41.64% of Bank's total net operating income.

Other revenues dropped by 4.67% over the previous year and amounted to €1.520 million.

Operating expenses, including depreciation, were €13.905 million and rose by 9.51% over the previous year. The rise in operating expenses results from the network expansion, new recruitments, as well as an increase in other expenses relating to Bank's growth and development.

The assessment of credit risk, making provisions for risky loans and Bank's potential liabilities are based on the application of principles of conservative policy and implementation of applicable regulations.

Total allocated reserves for assets and liabilities amounted to €15.307 million on 31 Dec 2017.

## PROFIT DISTRIBUTION

The Board of Directors, upon the initiative of the Bank management, proposes to the Shareholders Assembly not to distribute the 2017 profit in order to increase the Bank's overall capital.

## INDICATORS

Based on latest publicly available data from financial reports of all banks in Montenegro as of 31/12/2017, the Bank's ranking within Montenegro's banking sector is as follows

- Rank according to market share: the Bank holds 2nd position, i.e. 11.83% market share;
- Rank according to loan portfolio: the Bank holds 5th position, or 9.55% market share;
- Rank according to investment securities: the Bank hold 1st position, or 20.24% market share;
- Rank according to deposit portfolio: the Bank holds 2nd position, or 11.97 market share;
- Rank according to net profit: the Bank holds 5th position.

**INVESTMENT  
INTO  
ENVIRONMENT  
PROTECTION**

The Bank, within the scope of its own rights and obligations, engages in environment protection. In this context, the Bank is committed to prevention or restriction of environmental impacts resulting indirectly from its banking activities, or directly from its business as a whole.

The Bank's business practices do not target financing or co-financing projects that pollute or degrade the environment. The Bank, however, finances and actively supports/participates in funding projects that protect the environment, particularly by way of energy efficient technologies. In addition, the Bank's business practice is to find clients' projects/business objectives with the least possible level of risk for the environment.

In its business dealings, the Bank sees that natural resources are used rationally and that environment protection measures are duly implemented.

This aspect of our work was under particular focus during the implementation of credit facilities from European institutions, primarily the European Bank for Reconstruction and Development (EBRD).

**PLANS FOR  
FUTURE  
DEVELOPMENT**

Based on data available for 2017, a high liquidity and solvency level, together with a growth of key balance indicators is what describes Montenegro's banking sector and contributes to its smooth operations, and so also to strengthening financial stability. A stable banking sector and positive macro-economic trends in 2017 are encouraging prerequisites for future growth and development in 2018.

It is our estimate that in 2018, the legal framework that banks are governed by, on the one hand, and needs of our clients, on the other, will become even more challenging.

Given that there is an obvious demand among both retail clients and businesses for modern financial services, primarily due to a drastic drop of interest rates, we plan to continue with our business activities that are based on creativity and inventiveness. We are therefore focusing on generating new financial services to fill that gap, all in line with applicable regulatory framework and best practices. We are preparing services that are linked to instruments characterised by liquidity and flexibility compared to traditional banking products. Instead of deposits as standard products that we have offered to both retail and corporate clients, we plan to offer our clients a new form of investment. Professional consultancy and client asset management will be part of our range of services given our long-term experience that we have developed over the years in investment, creation and management of Bank's financial assets, but also given our professional workforce that has specialist knowledge gained in international markets.

**RESEARCH,  
DEVELOPMENT  
AND  
INVESTMENT IN  
WORKFORCE  
PROFESSIONAL  
DEVELOPMENT**

The Bank continually monitors and takes part in market research, as well as surveys published by renowned agencies and uses such data for brand positioning.

A key to our success and organisational culture is knowledge, skills and commitment of our workforce. The Bank therefore makes plans for ongoing professional development of its workforce both through organised education programmes, making use of experienced and competent staff members, but also through hiring renowned foreign consultants and consultancy firms specialised in human resources management. We wish to place a special emphasis on specialist training seminars intended for our retail officers and other positions that involve direct communication with our clients, all with a view to improving their communication skills, their ability to adjust their style of communication to various stages, and further development of skills in understanding client needs in their best interest. In addition, the Bank is committed to the concept of continuous professional development of workforce in managerial positions and hires external consultancy teams to improve their skills up to modern standards.





# 2 OVERVIEW OF 2017 MONTENEGRIN ECONOMY

## GROSS NATIONAL PRODUCT

Montenegro's macroeconomic performance, as reflected in 2017 indicators, made a significant improvement over the previous year. Intensified activities linked to major infrastructural projects in construction and energy sectors along with a big increase in the number of tourists, resulted in a high GDP growth rate. Preliminary MONSTAT data based on quarterly surveys show that throughout 2017 Montenegrin economy made a 4.4% growth. During this time period, substantial activity growth was recorded in construction industry, but also in tourism, forestry, trade and most modes of transportation. A negative industrial production trend from the previous year continued, while the number of both employed and unemployed people went up.

**INFLATION RATE** Annual inflation rate, measured by consumer price index, was 1.9% in December 2017, while the average annual inflation rate was 2.4%.

**INDUSTRIAL PRODUCTION** In 2017, industrial production dropped by 4.2% over 2016. Processing industry saw a 3% and electricity, gas and steam supply a 24.6% drop in production, while mining and quarrying saw a 113.9% growth.

**TOURISM, CONSTRUCTION, TRANSPORT, FORESTRY** Tourism sector recorded a continued positive trend in visits and overnight stays. In 2017, 2 million tourists visited Montenegro, up by 10.3% over the previous year. A total of 12 million overnight stays was recorded, up by 6.3% over 2016. Construction industry recorded a significant growth of 51.5% in the value of implemented works as well as a growth in effective work hours by 24.5% compared to 2016. Also, 2017 recorded a growth in most modes of transport, while production in the forestry sector grew by 15.8%.

**BANKING SECTOR** Banking sector accounts for a significant share of the entire financial sector. Throughout 2017, the banking sector was stable, solvent and liquid. All the security prudential indicators for the sector were above the statutory minimum. A continuous drop in bad loans and liabilities from the earlier period continued as a positive trend. A high level of liquid assets, a growth of overall deposits and loans, as well as the recapitalisation of a number of banks enhanced the stability of the banking sector. At year end, all the banks had a solvency coefficient above the 10% statutory minimum, while the aggregate coefficient was 16.37%. The banking sector made positive financial results in 2017, totalling €35.1 million. Twelve banks ended the year with a profit, while three banks operated with a loss. Five biggest banks recorded a profit growth over the previous year. The multi-annual trend of reducing concentration in the banking sector was recorded also in 2017. Measured by Hirschman-Herfindahl index, the situation has changed from what was an exceptionally

concentrated market with the dominant share of the three biggest banks to a market which today is closer to the so-called competitive market.

#### FOREIGN DIRECT INVESTMENT

According to preliminary data, net FDI in 2017 was €473.3 million, up by 27.6% over the previous year. The total FDI inflow was €649.2 million, of which owner investment was €366.9 million, while the inflow in the form of intercompany debt was €247.1 million. Withdrawals made by residents for investment abroad were €35.2 million. In total inflow of FDI, the share of intercompany debt was 38.1%, and of investment into companies and banks 33.8%, while the share of real estate investment was 22.7%. Total FDI outflow was €174.9 million or 44.6% down compared to 2016.

#### EMPLOYMENT

Total workforce in 2017 was 182.368 on average, or up by 2.5% compared to the year before, while the total number of employees in December 2017 was 177,627, or up by 0.1% compared to December 2016. Employment growth in 2017 was recorded in thirteen out of nineteen sectors, with the biggest growth registered in administrative and support services (17.7%), and lowest in IT and communications sector (0.1%). A decline in employment was registered in six sectors, of which the biggest decline of 5.8% was in agriculture, forestry and fisheries, and the smallest one was 0.4% in mining and quarrying sectors. At year end, the Employment Agency recorded 51,262 unemployed persons, up by 3.6% compared to the same month the year before. The number of registered unemployed persons in 2017 was 50,510 on average, or 17.9% more than the previous year. The unemployment rate as published by the Employment Agency of Montenegro was 22.09% in December 2017, or up by 0.76 percentage points compared to December 2016.

#### AVERAGE WAGE

MONSTAT data show that the 2017 average gross salary in Montenegro was €765, or up by 1.9% compared to 2016. The average salary net of taxes and contributions was €510, or up by 2.2% over the previous year. Real pays net of taxes and contributions in 2017 were down by 0.2%.

#### PROJECTIONS FOR 2018

According to the Central Bank of Montenegro (CBCG) model projections, GDP growth in 2018 will fluctuate between 2.7 and 3.2%, or 3% on average. The key driver of economic growth in the period to come will be extensive investment activity coming from capital investment planned for the construction of Smokovac-Matasevo highway, as well as investment in tourism, energy, telecommunications, etc. Expected growth in the export of goods and services is based on the growth of tourism expenditure boosted by the construction of new tourist developments, stabilization and investment planned in industrial and agricultural production that will

substitute a portion of imports with domestic products. However, any further growth in imports will depend on investor need to import equipment and construction material for capital infrastructural and tourism projects. In addition, continued implementation of fiscal consolidation measures in 2018 may lead to a drop in private and public expenditure. Therefore, maintaining a balance between the developmental component and budget sustainability in the upcoming mid-term period will be the key fiscal policy challenge.

*Source:* Central Bank of Montenegro, 2017 Macro-Economic Report







# 3 BUSINESS ACTIVITIES AND BANK'S ORGANOGRAM

## BANK PROFILE

Hipotekarna Bank provides the widest possible range of banking and financial products and services to both legal and physical persons in Montenegro, in line with the licenses issued by competent authorities.

The requirements governing the establishment and operation of banks in Montenegro are regulated by the Banks Act and Companies Act as well as the secondary legislation of the CBCG.

The securities market services provision that the Bank is engaged in is governed by the Securities Act and secondary legislation of the Securities Commission (dated 2018, the Capital Market Commission). The Bank also conducts payment operations as regulated by the Payment Operations Act, including the accompanying secondary legislation of the CBCG.

The Bank also provides insurance agency services, governed by the Securities Act and the relevant secondary legislation of the Insurance Supervision Agency.

The Bank is subject to the control and supervision of the CBCG, Securities Commission and Insurance Supervision Agency.

## BANK MANAGEMENT BODIES

The Bank management bodies include the following: General Assembly of Shareholders and the Board of Directors. The General Assembly is composed of its shareholders.

Members of the Board of Directors, as the Bank's management body, are elected and appointed by the General Assembly of Shareholders.

### GENERAL ASSEMBLY OF SHAREHOLDERS

The Bank's General Assembly is made up of its shareholders.

The Bank's equity is €16,005,933.45, composed of 31,305 ordinary registered shares. Par value of a single share is €511.29;

Shares are dematerialized, transferrable without limitation, and registered in owner's name. The extract from the register with the Central Depository Agency AD Podgorica is the only proof of ownership over the shares;

- Bank's shareholders holding ordinary shares have the following rights:
  - right to attend Shareholders Assembly,
  - management rights, in proportion to the equity share for this class of shares,
  - right to dispose of the shares, in line with applicable regulations,
  - pre-emptive right of purchase for shares from new emissions,
  - right to shares free of charge in case the equity's increase from the Bank's own funds, in proportion to the shares,
  - right to dividend, after the distribution of privileged shares to the owners,

when the Shareholders Assembly takes a decision for the dividend to be paid out,

- right of receipt, upon personal request, of a copy of the balance sheet and income statements, as well as of the external auditor's report,
- right of inspection, thirty days before the Shareholders Assembly, as well as at the Assembly itself, of the financial reports, including the reports of the external auditor, and
- right to a proportional share in the assets in the event of the Bank's liquidation and other rights and privileges, in line with applicable regulations.
- There are no limitations to the transfer of shares or securities;
- Acquisition of shares by workforce is subject to applicable laws and other regulations;
- There are no restrictions to the right of vote, such as the restriction of the voting rights of the owner of a certain percentage of securities, or a certain number of shares, deadlines for the exercise of the voting right, etc.;
- There is no agreement between the shareholders that the issuer is aware of and that may result in any restrictions on the securities transfer and/or voting rights;
- The procedures for the appointment and removal of the members of the Board of Directors are defined by applicable laws and other regulations;
- Powers of the members of the Board of Directors are defined by applicable laws and other regulations;
- There are no material agreements that the issuer is a party to and that have legal effect, are amended or terminated after the takeover of issuer following the public bid for the takeover and their legal effects, unless where the agreements are of such nature that their publication could have significant harmful effects to the issuer, on condition that the issuer is under no explicit obligation to publish such data according to legislation;
- The structure of the Bank's biggest shareholders is as follows as of 31/12/2017:

Generali Financial Holdings FCP-Sif	16.8695 %
Cerere S.P.A. - Italy	13.9275 %
Lorenzo Gorgoni - Italy	12.9788 %
Antonia Gorgoni - Italy	10.0016 %
Miljan Todorović - Italy	7.3982 %
Podravska Banka Dd - Croatia	6.5389 %
Ibis Srl - Italy	4.8682 %
Dario Montinari - Italy	4.6159 %

Sigilfredo Montinari - Italy	4.6159 %
Piero Montinari - Italy	4.6127 %
Andrea Montinari - Italy	4.6127 %

The Bank's Board of Directors manages the Bank. Members of the Board of Directors are elected and appointed by the General Assembly of Shareholders.

The Bank's Board of Directors has 5 members with majority of them not being employed with the Bank.

External bodies of the Bank's Board of Directors include the Audit Committee and Credit Risk Management Committee.

**BANK'S  
GENERAL  
ASSEMBLY OF  
SHAREHOLDERS  
- ACTIVITIES  
IN 2017**

The Bank's Shareholders Assembly had one session in 2017, which, given the materials addressed and subject to decision making, had the character of a regular (annual) session.

At its XIX regular session (held on 29/06/2017), Shareholders' Assembly reviewed the 2016 Hipotekarna Bank AD Podgorica annual report, together with the external audit report, and passed the Decision on profit allocation for 2016. It was established under that Decision that the Bank's profit after taxation amounted to €3,624,047.48. On 31/12/2016, a provision gap was identified in accordance with Article 49 of the Decision on Minimum Standards for Credit Risk Management in Banks ("Official Gazette of Montenegro, No. 22/12 of 23/04/2012, No. 55/12 of 02/11/2012 and No. 57/13 of 16/12/2013") ("Decision"). Namely, there is a difference between the amount of reservations for potential losses and the sum of corrected values for the balance assets positions and reservations for off-balance items in the amount of €7,654,825.96. Following the Bank's obligations as set forth in Art. 49a of the Decision, part of 2016 profit in the amount of €631,779.61 has to be transferred onto the reservations account for anticipated losses in line with the regulatory requirement - account 3025 - to serve as coverage of part of the identified provision gap.

In addition, at its XIX regular session (held on 29/06/2017), the Bank's Shareholders Assembly passed a Decision on the II (second) issuance of Hipotekarna Bank AD Podgorica subordinated bonds by way of a restricted offer addressed to a previously identified number of persons in order to raise additional capital of the Bank in line with the provisions of the Bank's Capital Adequacy Decision ("Official Gazette of Montenegro" Nos. 38/11 and 55/12). On this basis 40,000 (forty thousand) bonds of identical category and class were issued with the individual par value of €100.00 (a hundred euros and 00/100), with 6 (six) year maturity. The issued bonds were dematerialised, freely transferrable debt securities that represent direct and unconditional obligation of the Bank on the basis of which the bond owner has the right to collect, within the maturity term, the nominal value of the bond together with the stipulated interest. The bond owner is also entitled to all the other rights and obligations subject to

applicable regulations. The Bank pays a 5.9% interest rate (five point nine percent) on issued bonds annually, with semi-annual calculation and payment of interest. The calculation of interest is made by a proportionality method, by using the actual number of days in the period for which interest is calculated and the actual number of days in a given year. For the implementation of bond issuance, the Bank made an abridged prospectus pursuant to the Securities Act (“Official Gazette of the Republic of Montenegro”, Nos. 59/00, 10/01, 43/05, 28/06, “OG of Montenegro”, Nos. 53/09, 73/10, 40/11 and 06/13) and the Rules on the content of an abridged prospectus on the methodology and procedures for recording closed bids for ownership and long-term debt securities (“OG of the Republic of Montenegro”, No. 34/07 of 8/06/2007 and OG of Montenegro, No. 39/08) that includes the data on all previously identified buyers or potential investors communicated to the Securities Commission and publicly available, in line with the regulations governing personal data protection.

**BOARD OF  
DIRECTORS,  
BODIES  
AND BANK'S  
EXECUTIVE  
OFFICERS**

**Hipotekarna Bank AD Podgorica Board of Directors:**

- Sigilfredo Montinari, Chairperson
- Božana Kovačević, Deputy Chairperson
- Renata Vinković, Member
- Goran Varat, Member
- Esad Zaimović, Member

**Hipotekarna Bank AD Podgorica Audit Committee:**

- Draško Popović, Chairperson
- Božana Kovačević, Member
- Marko Žigmund, Member

**Hipotekarna Bank AD Podgorica Credit Risk Management Committee:**

- Renata Vinković, Chairperson
- Sigilfredo Montinari, Member
- Esad Zaimović, Member

**Hipotekarna Bank AD Podgorica executive officers:**

- Esad Zaimović, Chief Executive Officer
- Aleksandar Mitrović, Executive Officer for Business Support Operations, up to 16/06/2017
- Božo Djurašković, Executive Officer for Business Support Operations, as of 17/06/2017.

## BANK MANAGEMENT

### EXECUTIVE OFFICERS

Esad Zaimović, Chief Executive Officer

Aleksandar Mitrović, Executive Officer for Business Support Operations,  
up to 16/06/2017

Božo Djurašković, Executive Officer for Business Support Operations, as  
of 17/06/2017.

### INTERNAL AUDIT SECTOR

Veselin Ivanović, Chief internal auditor

### EXPERT FUNCTION MONITORING REGULATORY COMPLIANCE

Danka Dragičević

### ANTI-MONEY LAUNDERING AND TERRORIST FINANCE SECTOR

Mirjana Jovanović

### HEAD OF IT SECURITY SECTOR (CISO)

Haris Dizdarević

### SECTORS

Ana Golubović, Director of Corporate Sector

Nikola Špadijer, Director of Retail Sector

Mirza Vodopić, Director of Financial Market Sector

Jelena Vuletić, Director of Credit Risk Management Sector

Nataša Lakić, Director of Payment Operations Sector

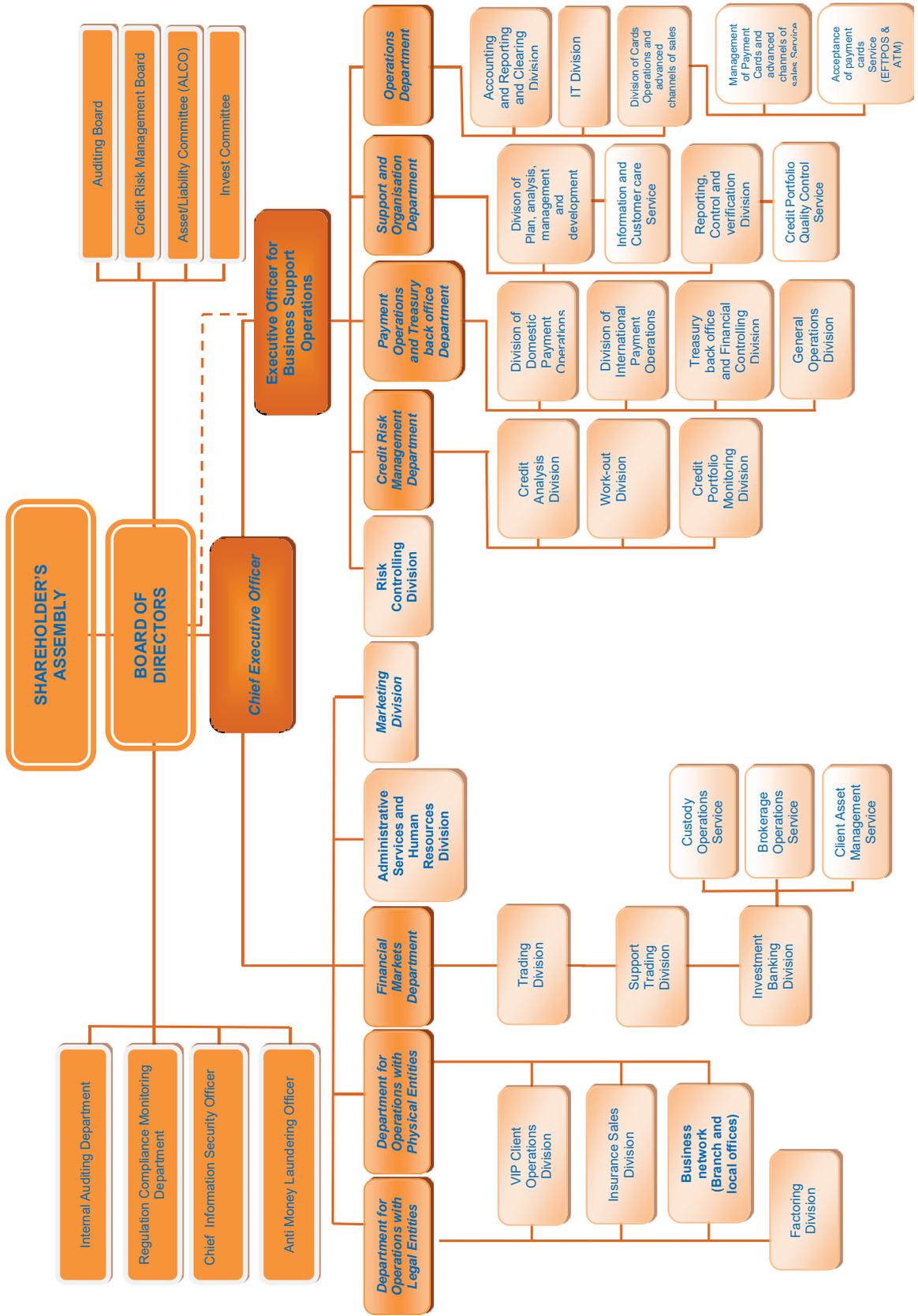
Nikola Milović, Director of Support and Organisation Sector

### INDEPENDENT SERVICES

Goran Smolović, Director of Risk Control Service

Ana Ristić, Director of Marketing Sector

# BANK'S ORGANOGRAM



## BUSINESS NETWORK

### Call Centar (+382 202) 19905

#### Hipotekarna Bank Head Office

Address: Ul. Josipa Broza Tita br. 67  
81000 Podgorica  
E-mail: [hipotekarna@hb.co.me](mailto:hipotekarna@hb.co.me)  
Tel: +382 (0) 77 700 001  
Fax: +382 (0) 77 700 071

### BRANCHES

#### Podgorica Branch

Address: Ul. Slobode br. 91  
81000 Podgorica  
E-mail: [filijala.podgorica@hb.co.me](mailto:filijala.podgorica@hb.co.me)

#### Nikšić Branch

Address: Trg Save Kovačevića bb  
81400 Nikšić  
E-mail: [filijala.niksic@hb.co.me](mailto:filijala.niksic@hb.co.me)

#### Bar Branch

Address: Ul. Maršala Tita bb  
85000 Bar  
E-mail: [filijala.bar@hb.co.me](mailto:filijala.bar@hb.co.me)

#### Budva Branch

Address: Mediteranska br. 4  
85310 Budva  
E-mail: [filijala.budva@hb.co.me](mailto:filijala.budva@hb.co.me)

#### Kotor Branch

Address: SC Kamelija, Trg M. Petrovića bb  
85330 Kotor  
E-mail: [filijala.kotor@hb.co.me](mailto:filijala.kotor@hb.co.me)

#### Herceg Novi Branch

Address: Ul. Njegoševa br. 52  
85340 Herceg Novi  
E-mail: [filijala.hercegnovi@hb.co.me](mailto:filijala.hercegnovi@hb.co.me)

#### Bijelo Polje Branch

Address: Ul. Slobode bb  
84000 Bijelo Polje  
E-mail: [filijala.bijelopolje@hb.co.me](mailto:filijala.bijelopolje@hb.co.me)

#### Berane Branch

Address: Ul. Mojsija Zečevića bb  
84300 Berane  
E-mail: [filijala.berane@hb.co.me](mailto:filijala.berane@hb.co.me)

#### Ulcinj Branch

Address: Ul. 26.Novembar bb  
85360 Ulcinj  
E-mail: [filijala.ulcinj@hb.co.me](mailto:filijala.ulcinj@hb.co.me)

#### Danilovgrad Branch

Address: Baja Sekulića br. 8  
81410 Danilovgrad  
E-mail: [filijala.danilovgrad@hb.co.me](mailto:filijala.danilovgrad@hb.co.me)

### SUB-BRANCHES

#### Sub-branch Podgorica 24/7

Address: Bul.Svetog Petra Cetinjskog br.130  
Podgorica  
E-mail: [ekspozitura.podgorica1@hb.co.me](mailto:ekspozitura.podgorica1@hb.co.me)

#### Sub-branch Podgorica 2 (Blok VI)

Address: Ul. Đoka Miraševića M3  
81000 Podgorica  
E-mail: [ekspozitura.podgorica2@hb.co.me](mailto:ekspozitura.podgorica2@hb.co.me)

#### Sub-branch Podgorica 3 (Alliance)

Address: Cetinjski put bb  
81000 Podgorica  
E-mail: [ekspozitura.podgorica3@hb.co.me](mailto:ekspozitura.podgorica3@hb.co.me)

#### Sub-branch Tuzi

Address: Tuzi bb  
81206 Tuzi  
E-mail: [ekspozitura.tuzi@hb.co.me](mailto:ekspozitura.tuzi@hb.co.me)

#### Sub-branch Cetinje

Address: Ul. Bajova br. 74  
81250 Cetinje  
E-mail: [ekspozitura.cetinje@hb.co.me](mailto:ekspozitura.cetinje@hb.co.me)

#### Sub-branch Tivat

Address: Ul. 21. Novembra br. 21  
85320 Tivat  
E-mail: [ekspozitura.tivat@hb.co.me](mailto:ekspozitura.tivat@hb.co.me)

#### Sub-branch Tivat – Porto Montenegro

Address: Porto Montenegro, zgrada Teuta,  
Obala bb  
85320 Tivat  
E-mail: [ekspozitura.porto.montenegro@hb.co.me](mailto:ekspozitura.porto.montenegro@hb.co.me)

## WORKFORCE

As of 31/12/2017, the Bank had a workforce of 172 people with qualifications and IT skills required for quality conduct of bank operations.

Continuous education and professional development are set as Bank's top priorities. In 2017, a large number of employees underwent training in both internal and external programmes on various areas relevant to the Bank operations. The Bank hires young professionals who can contribute to Bank's effective development.

Educational background of the Bank's workforce as of 31/12/2017 is as follows: 12 hold a MSc, 90 university, and 33 a Bachelor of Science degrees, while 13 have two-year post-secondary, and 50 a secondary school education.





# 4 BUSINESS OPERATIONS

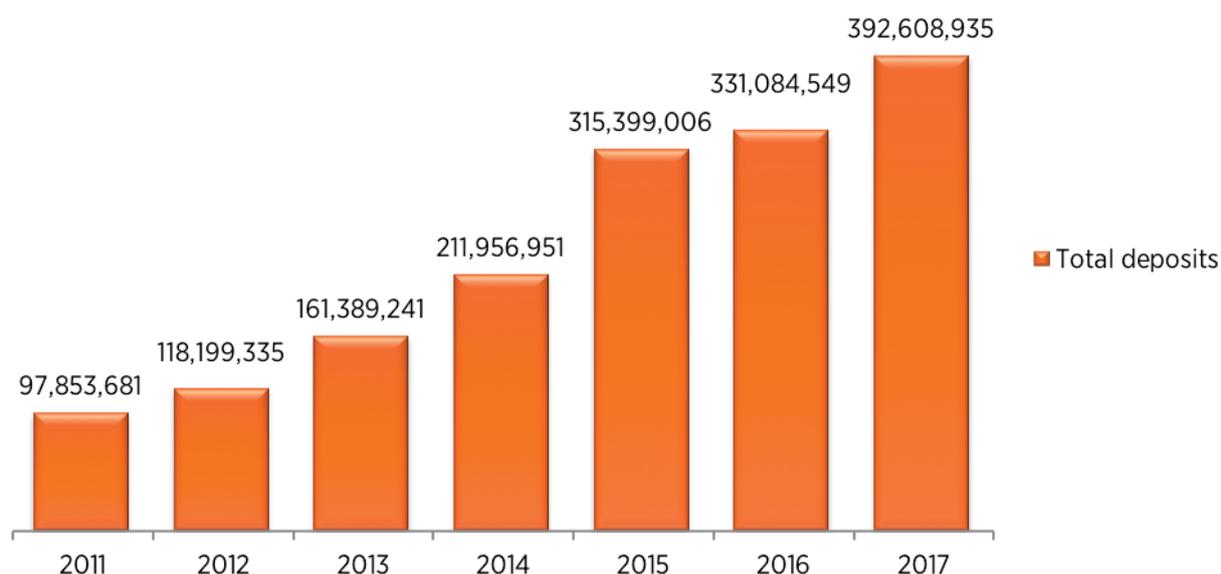
## DEPOSITS

2017 saw a 18.58% growth in deposits over 2016, which reflects a continued trend of growing confidence among both citizens and businesses from previous years in spite of a high level of deposits in the previous year. All deposits remained stable, while sight deposits saw a particularly striking growth of 36.70%.

The Bank maintained an adequate term and sight deposits to overall deposits ratio.

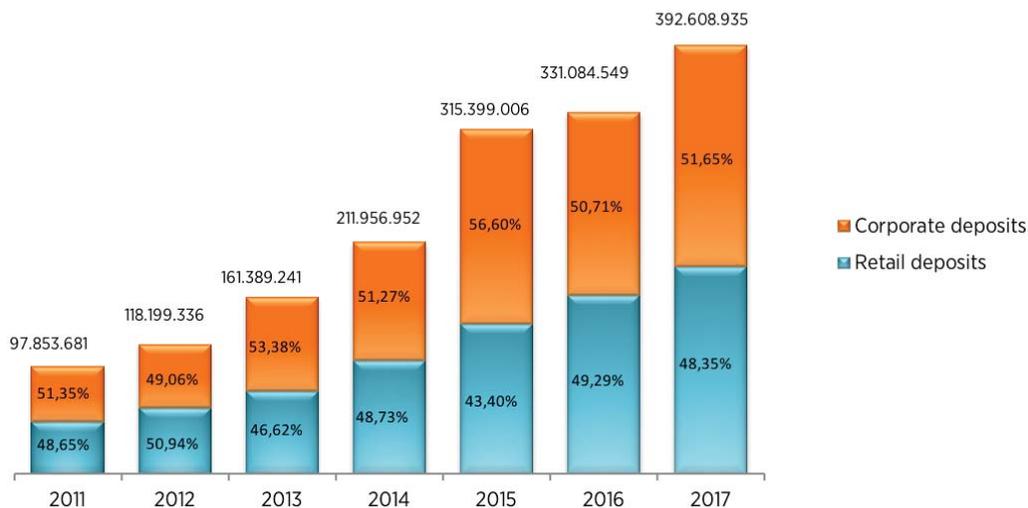
Deposits total

	<b>Total deposits</b>	<b>% change</b>
2011	97,853,681	15.00%
2012	118,199,335	20.79%
2013	161,389,241	36.54%
2014	211,956,951	31.33%
2015	315,399,006	48.80%
2016	331,084,549	4.97%
2017	392,608,935	18.58%



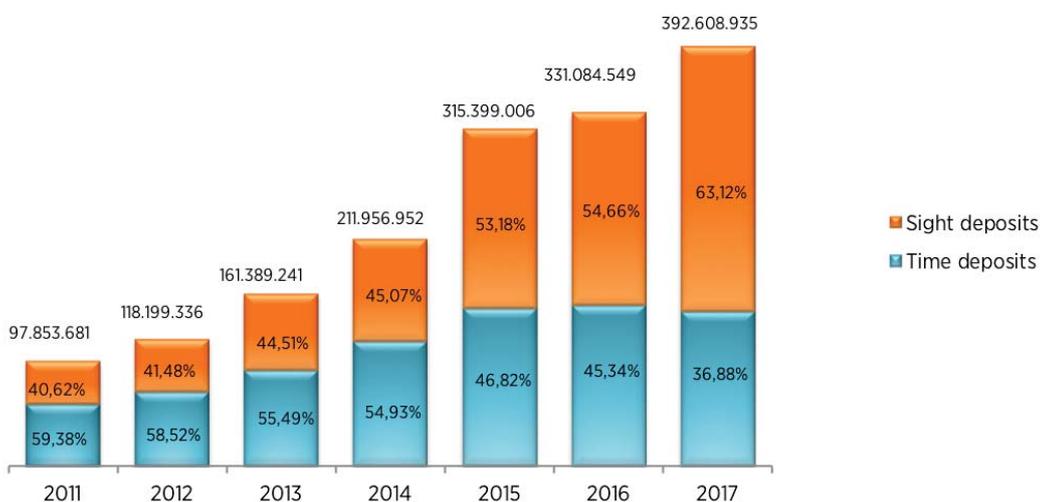
The said deposit growth came as a result of rising client numbers as well as a higher level of confidence in the Bank. Thanks to the Hipotekarna Bank's major strengths, such as security, professionalism and quality services offered, we are recognised as a Bank worthy of confidence. As a result, the positive trends of deposit growth continued.

Corporate deposits accounted for 51.65%, and retail deposits for 48.35% of overall deposits, as shown in the following graph:



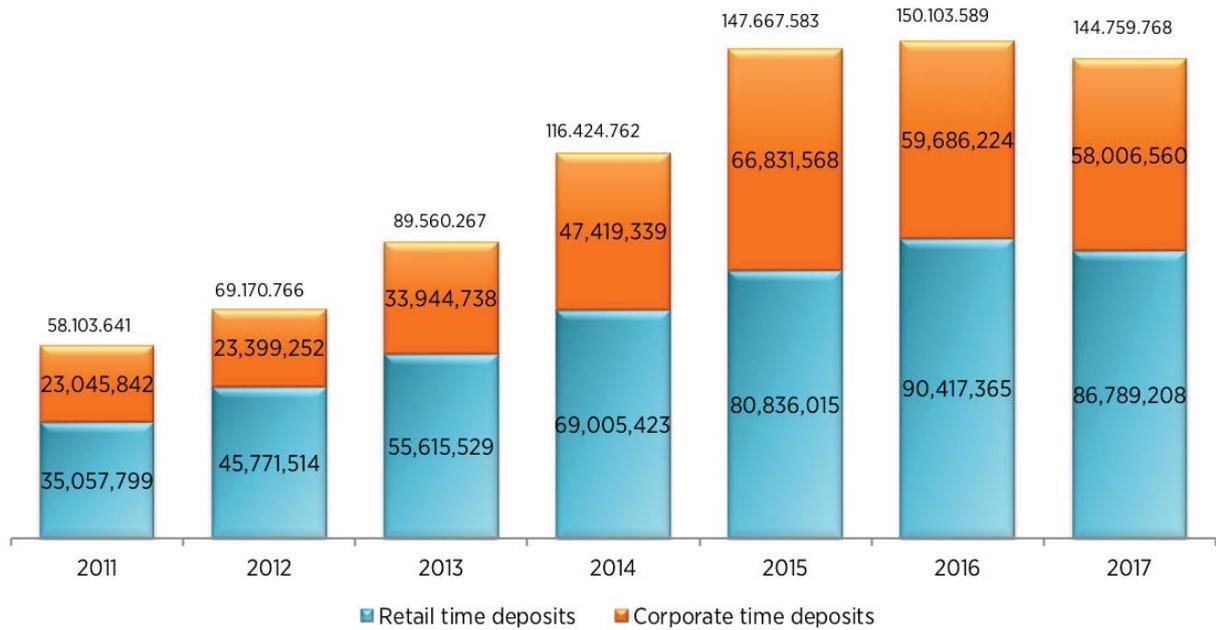
Share in overall deposits	2011	2012	2013	2014	2015	2016	2017
Retail deposits	47,604,421	60,204,983	75,236,948	103,276,531	136,890,858	163,175,605	189,810,140
Corporate deposits	50,249,260	57,994,353	86,152,293	108,680,421	178,508,148	167,908,944	202,798,795
Total	97,853,681	118,199,336	161,389,241	211,956,952	315,399,006	331,084,549	392,608,935

Time deposits accounted for 36.88%, and sight deposits for 63.12% of overall deposits.

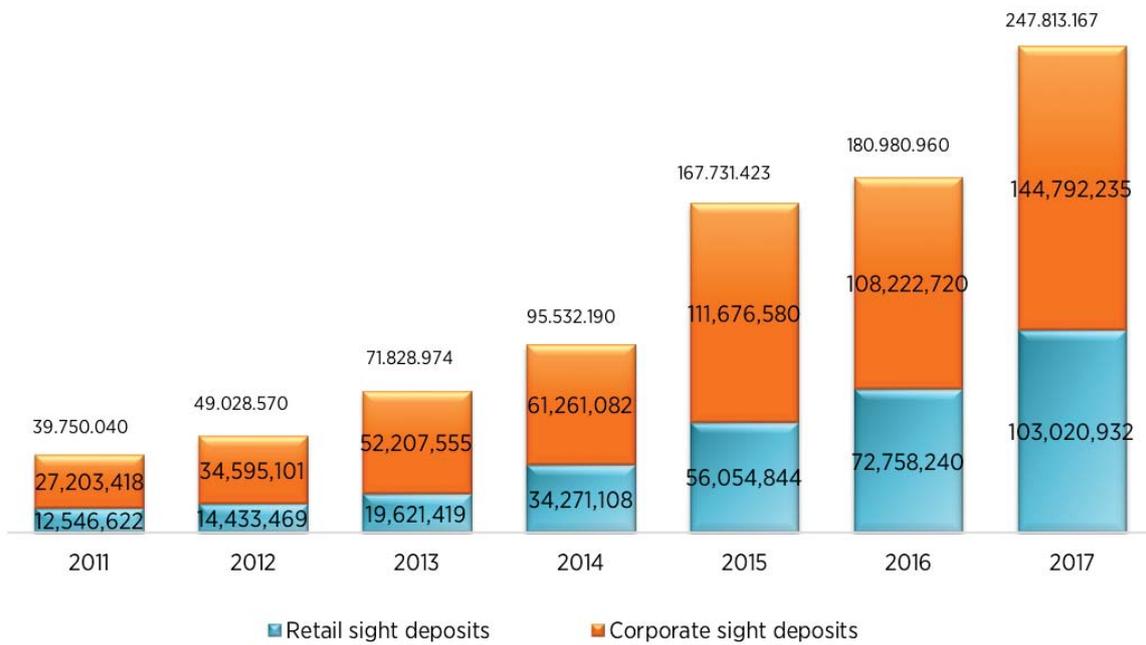


	2011	2012	2013	2014	2015	2016	2017
Time deposits	58,103,641	69,170,766	89,560,267	116,424,762	147,667,583	150,103,589	144,795,768
Sight deposits	39,750,040	49,028,570	71,828,974	95,532,190	167,731,423	180,980,960	247,813,167
Total	97,853,681	118,199,336	161,389,241	211,956,952	315,399,006	331,084,549	392,608,935

In line with the overall deposit trend, both time and sight deposits recorded a growth in 2017 compared to 2016, as shown in the graphs below:



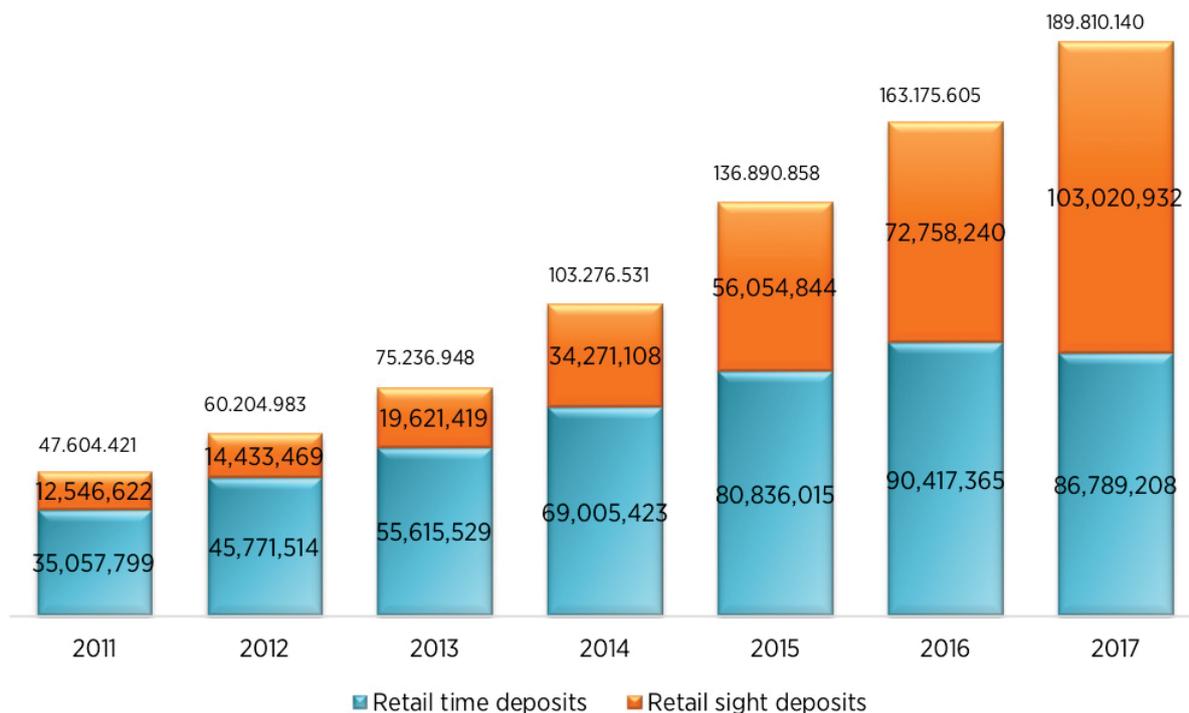
	2011	2012	2013	2014	2015	2016	2017
Retail time deposits	35,057,799	45,771,514	55,615,529	69,005,423	80,836,015	90,417,365	86,789,208
Corporate time deposits	23,045,842	23,399,252	33,944,738	47,419,339	66,831,568	59,686,224	58,006,560
Total	58,103,641	69,170,766	89,560,267	116,424,762	147,667,583	150,103,589	144,795,768



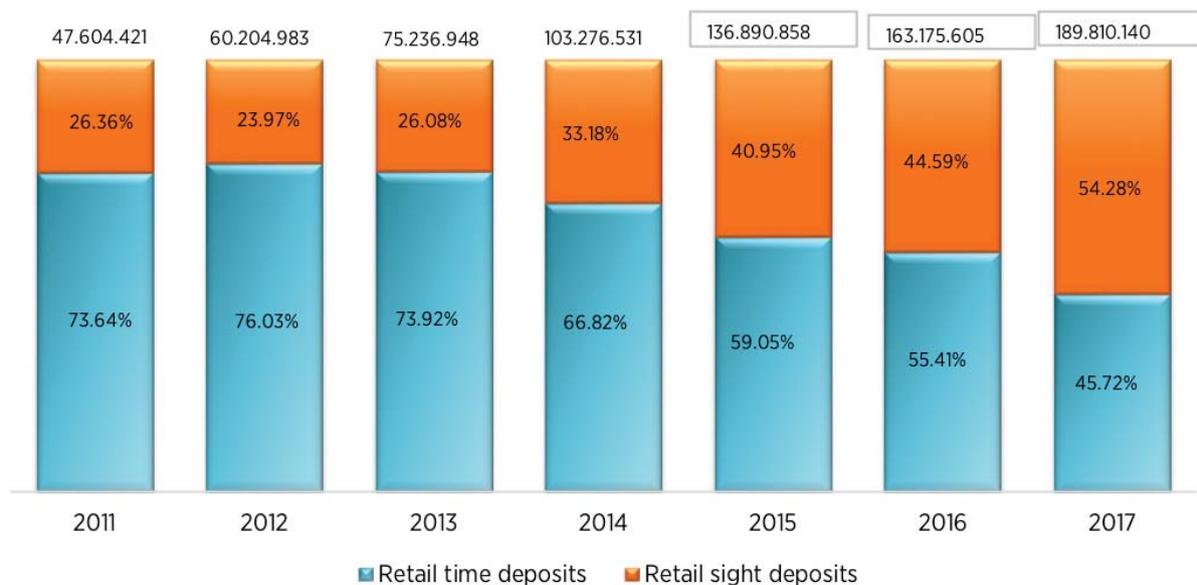
	2011	2012	2013	2014	2015	2016	2017
Retail sight deposits	12,546,622	14,433,469	19,621,419	34,271,108	56,054,844	72,758,240	103,020,932
Corporate sight deposits	27,203,418	34,595,101	52,207,555	61,261,082	111,676,580	108,222,720	144,792,235
Total	39,750,040	49,028,570	71,828,974	95,532,190	167,731,423	180,980,960	247,813,167

## RETAIL DEPOSITS

At the end of 2017, total retail deposits recorded a 16.32% growth compared to 2016. Sight deposit growth was as high as 41.59%.

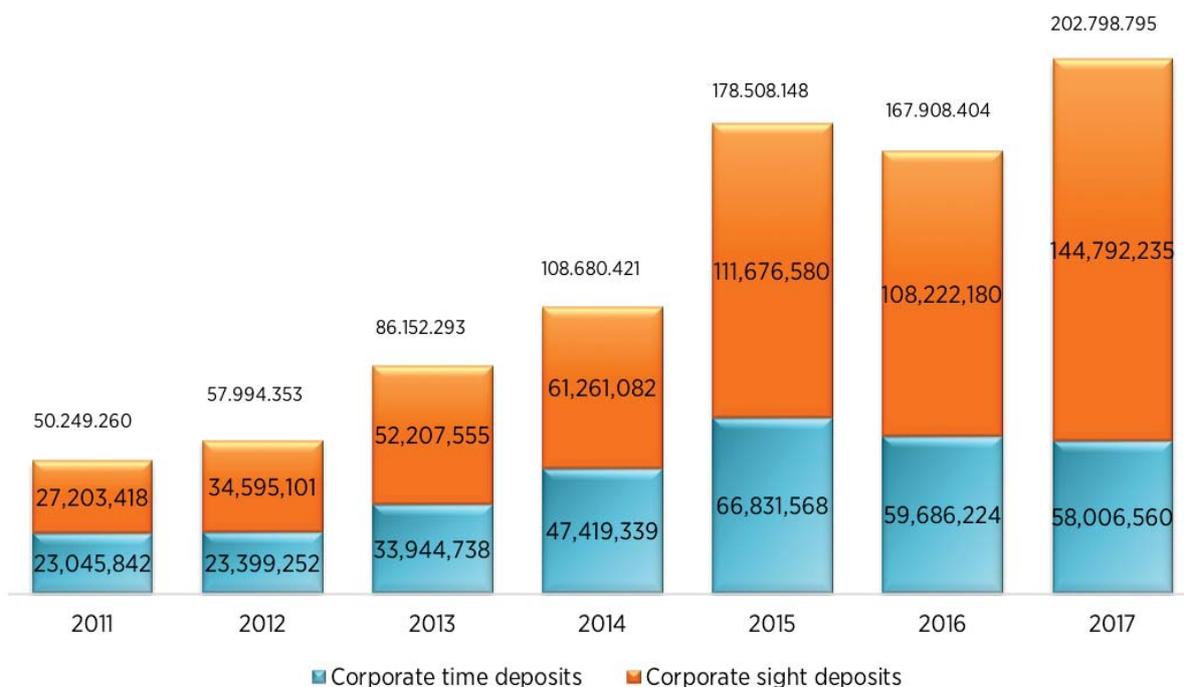


In the overall structure of retail deposits, time deposits accounted for 45.72%, while sight deposits accounted for 54.28%.



## CORPORATE DEPOSITS

Corporate deposits totalled €202,798,795 on 31/12/2017, which is a 20.78% growth compared to 2016. The graph below shows the deposit structure by type:



U ukupnoj strukturi depozita pravnih lica, učešće oročenih depozita je iznosilo 35,55%, dok su a vista depoziti učestvovali sa 64,45%.

	2011	2012	2013	2014	2015	2016	2017
Corporate time deposits	23,045,842	23,399,252	33,944,738	47,419,339	66,831,568	59,686,224	58,006,560
Corporate sight deposits	27,203,418	34,595,101	52,207,555	61,261,082	111,676,580	108,222,720	144,792,235
TOTAL	50,249,260	57,994,353	86,152,293	108,680,421	178,508,148	167,908,404	202,798,795

Time deposits accounted for 28.60% and sight deposits for 71.40% of the overall corporate deposits.



## LOANS

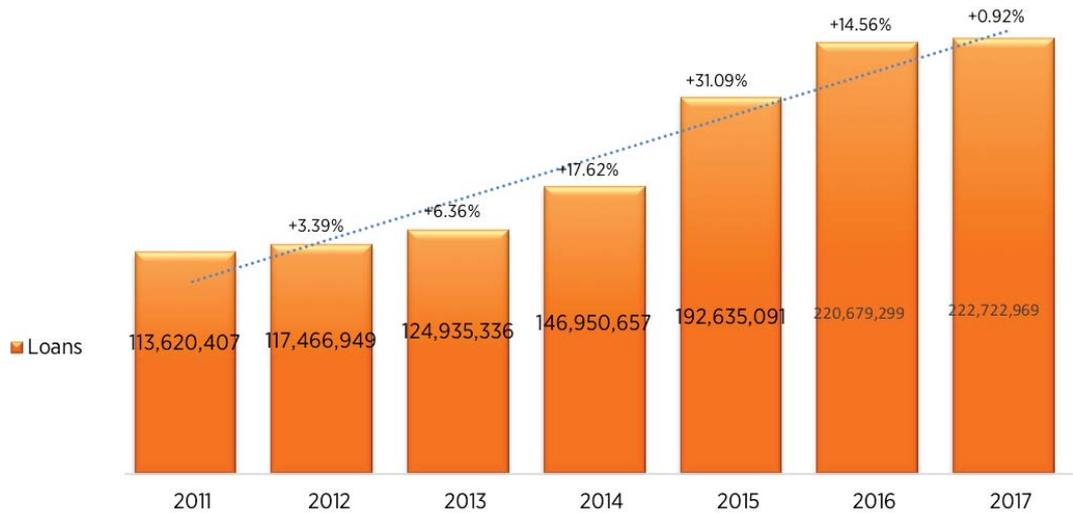
Following the trends of earlier years, in 2017 the Bank granted loans to a large number of new clients. A continuous support and further expansion of the existing pool of clients is the Bank's top priority and our workforce focuses on anticipating client needs and offering optimum arrangements and tariffs to existing clients.

One of the Bank's striking features is that in addition to providing loans it also provides consultancy services, all with a view to improving overall business operations and achieving positive business results of both the Bank and its clients.

Despite the conservative loan policy that the Bank had pursued for years, total loans portfolio increased by 0.92% over the previous year.

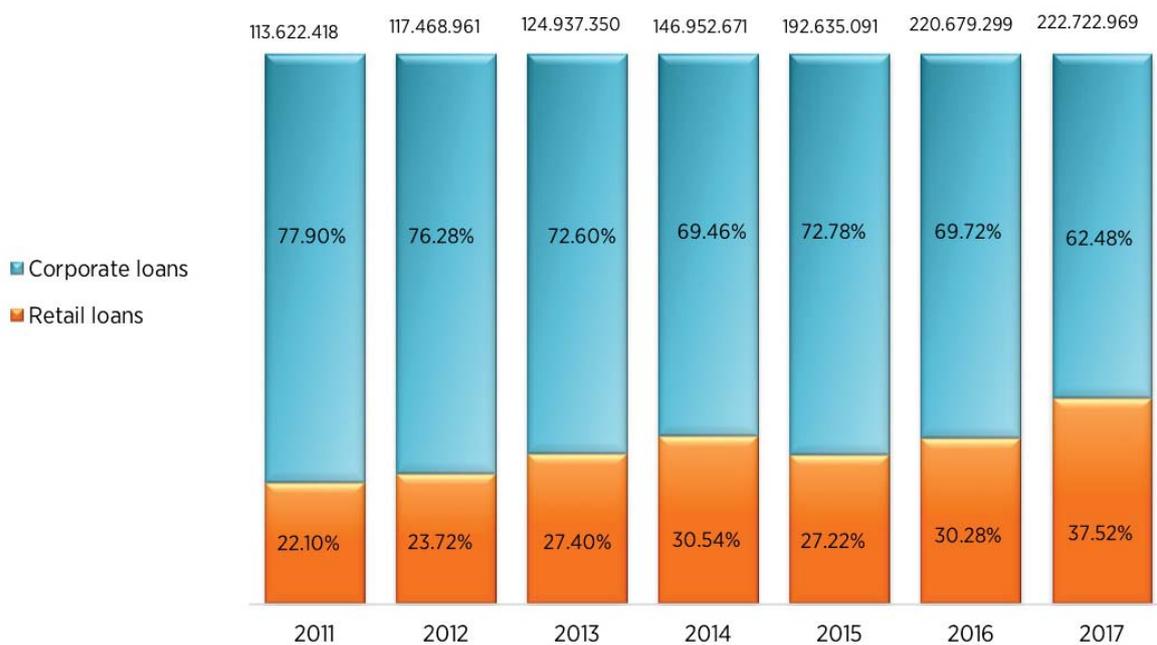
Retail loans portfolio growth was 25.03%.

	Loans	Change %
2011	113,620,407	0.00%
2012	117,466,949	3.39%
2013	124,935,336	6.36%
2014	146,950,657	17.62%
2015	192,635,091	31.09%
2016	220,679,299	14.56%
2017	222,701,289	0.92%



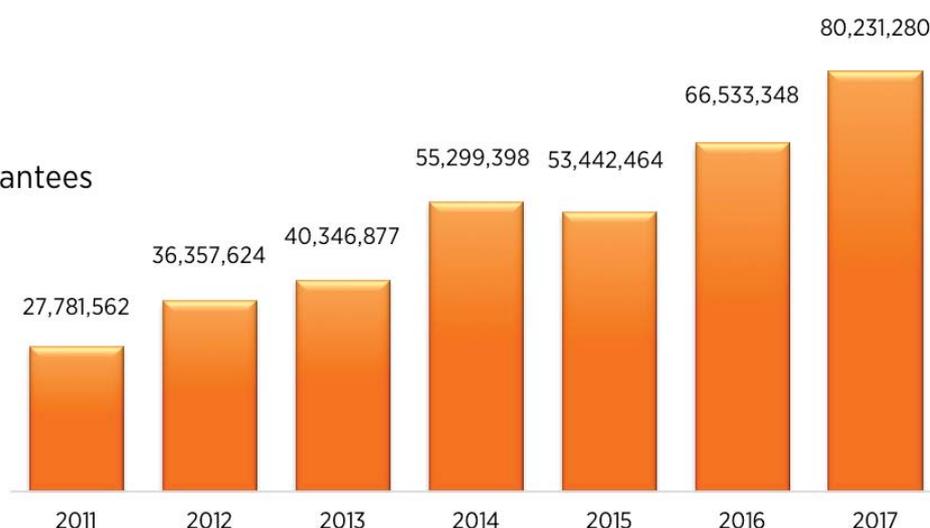
	2011	2012	2013	2014	2015	2016	2017
Retail loans	25,110,235	27,867,176	34,227,877	44,875,954	52,436,433	66,825,085	83,550,069
Corporate loans	88,510,172	89,599,773	90,707,460	102,074,703	140,198,658	153,854,215	139,151,220
Total	113,620,407	117,466,949	124,935,336	146,950,657	192,635,091	220,679,299	222,701,289

Retail loans account for 37.52% and corporate loans for 62.48% in overall loan portfolio.



Overview of guarantees in 2017:

## Overview of guarantees



Overall guarantees were up by 20.59% compared to the previous year.

	2011	2012	2013	2014	2015	2016	2017
Guarantees total	27,781,562	36,357,624	40,346,877	55,299,398	53,442,464	66,533,348	80,231,280

The Bank continued its successful cooperation with Investment and Development Fund (IDF) to grant loans under preferential terms.

In addition, the Bank started discussions with renowned foreign investors (EBRD, EFSA, etc.) in order to identify sources and arrangements for loan support to meet the needs of our clients.

The Bank's range of services offered to corporate clients includes cash loans, revolving loans, loans intended for settlement of obligations towards suppliers, for car purchase, refinancing of debts with other banks, financing export liabilities, for purchase of equipment, refurbishment of office space, preparation for tourist season, overdraft loans, factoring, as well as all types of guarantees.

The Bank also offers a wide spectrum of retail loans: cash loans, specific purpose loans, student loans, car purchase loans, reconstruction and refurbishment loans, sailor loans, tourism loans, agriculture loans, overdraft loans, consumer instalment loans, etc. as well as all types of guarantees.

## PAYMENT OPERATIONS

The Bank overall payment operations in 2017 were characterized by the growth of all parameters defining business operations of this segment. All business plans previously set for business operations were achieved, which clearly demonstrates the Bank's efficiency and progress over the previous year.

## DOMESTIC PAYMENT OPERATIONS

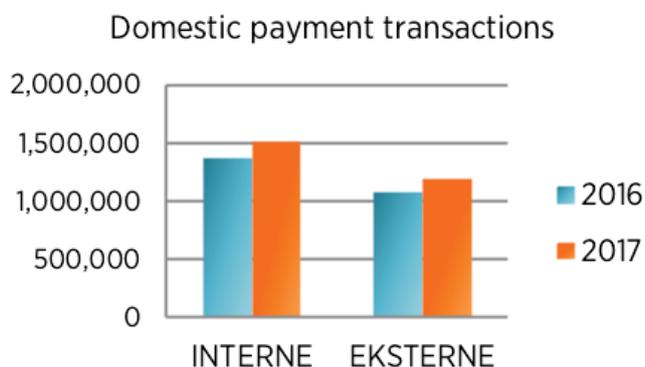
Overall domestic payment operations of the Bank recorded a growth in 2017.

The total number of domestic payment transactions rose by 11% over 2016. Of this figure, the biggest growth was recorded in the number of internal transactions in the Bank, 11% compared to the previous year. External transactions also recorded an 11% growth over the previous year.

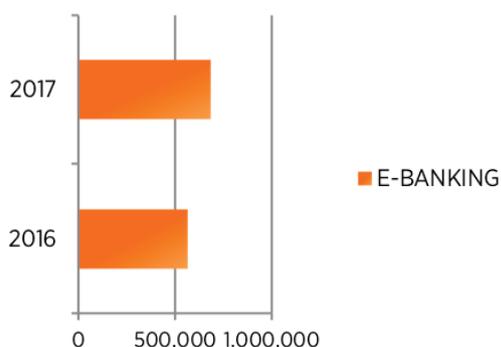
Within the external payment orders there was also a growth of 'small' payments (< EUR1.000, an increase of 11%) as well as 'high value' payments (> EUR1.000, a 10% growth).

Incoming payments from other banks rose by 9% over the previous year.

A significant increase was also recorded in the number of electronic (e-banking) transactions, which means that clients are turning more and more to electronic applications and make payments by electronic orders. The number of domestic electronic payments grew by 21% over the previous year.



**Domestic e-payments**



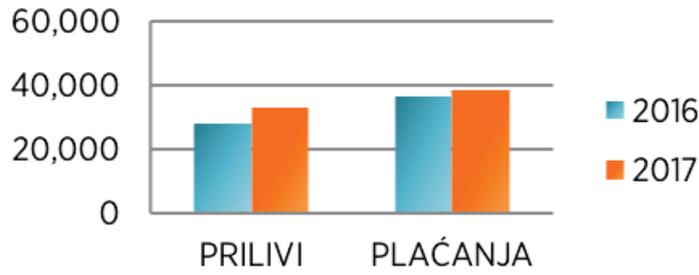
## FOREIGN PAYMENT OPERATIONS

Foreign payment operations in 2017 were characterized by the fact that a high level of transactions was maintained, as well as by an increase in incoming payments and payments by e-banking, and in other operations that make an integral part of foreign payment operations.

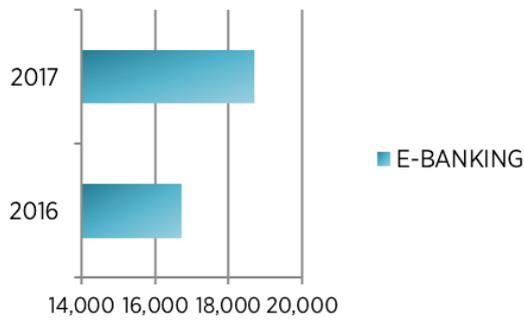
The Bank has long since been recognised by international banks as an efficient and reliable partner.

The number of outgoing payment operations grew by 5% compared to the previous year. The number of electronic outgoing payment transactions made by HB-klik (e-banking) rose by 12% over 2016. The number of incoming transactions rose by 18% over the previous year.

Foreign currency payment transactions  
- INFLOW/PAYMENT



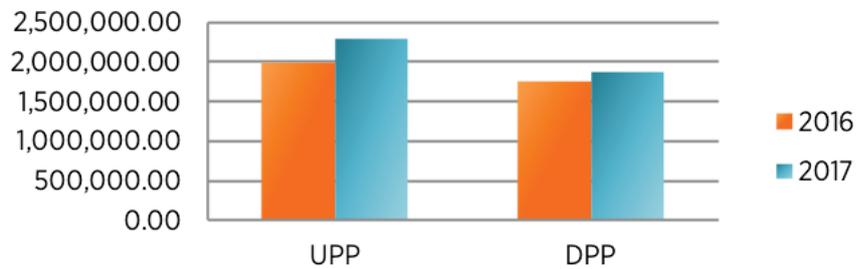
Outgoing e-payments

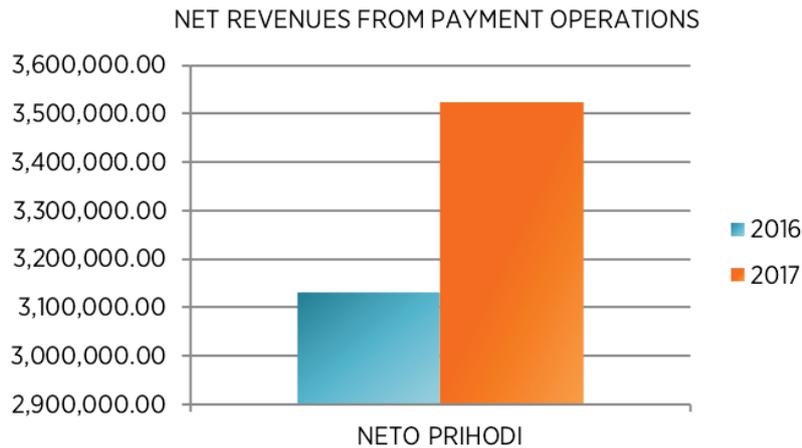


Total revenues from commissions on payment operations increased by 11% over 2016. The revenues from domestic payment operations rose by 15%, and from foreign payment operations by 6%.

Net revenues from overall payment operations rose by 12% over the previous year.

Revenue from domestic and foreign payment operations





## DEVELOPMENT OF NEW PRODUCTS AND SERVICES

The Bank maintained, throughout 2017, its continuity in launching innovative products comprising both modern day banking services and traditional loan products.

**MasterCard Premium Gift card**, the first card of this time in Montenegro's market which:

- Requires no bank account opening procedure
- Offers discounts in over 1200 outlets in Montenegro, Premium Programme partners
- Options to make payment in the country and abroad at all points of sale with the MasterCard sign
- Is ideal for Internet payments
- Makes an ideal gift for family and friends

**Super payment card:**

- Belongs to the group of Platinum MasterCard cards
- Co brand contactless payment card
- Payment in both POS terminals and online, with a points collection function
- Travel health insurance free of charge
- Cash withdrawals in POS terminals and cash points.

**Consumer loans granted without a visit to the bank, 0% interest rate: Hipotekarna Bank and Tehnomax**

A unique product in the market.

- No interest rates
- No processing fees
- No visit to the Bank

Hipotekarna Bank, in co-operation with Tehnomax, grants citizens consumer loans in up to 24 instalments without interest rates, processing fees or a need to visit the bank. They are intended for:

- Employees whose employers or trade unions have concluded a business co-operation contract with Tehnomax for consumer goods and
- Persons that Tehnomax has a positive experience with based on their prior deferred payment purchases.

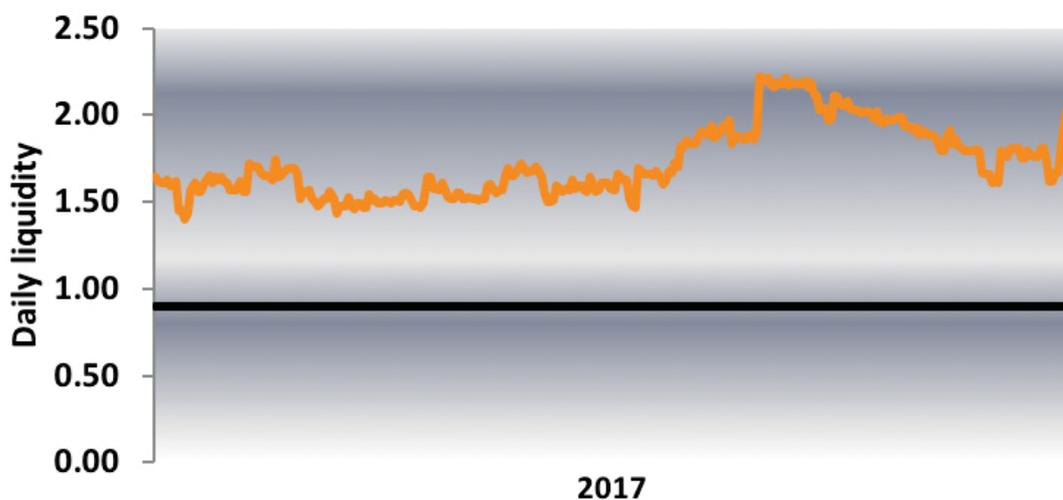
## ASSET MANAGEMENT

Providing optimal liquidity is a basic requirement for safe and efficient operations of each bank. To maintain an appropriate liquid assets to total liabilities ratio, the Bank applies rational management of assets and liabilities.

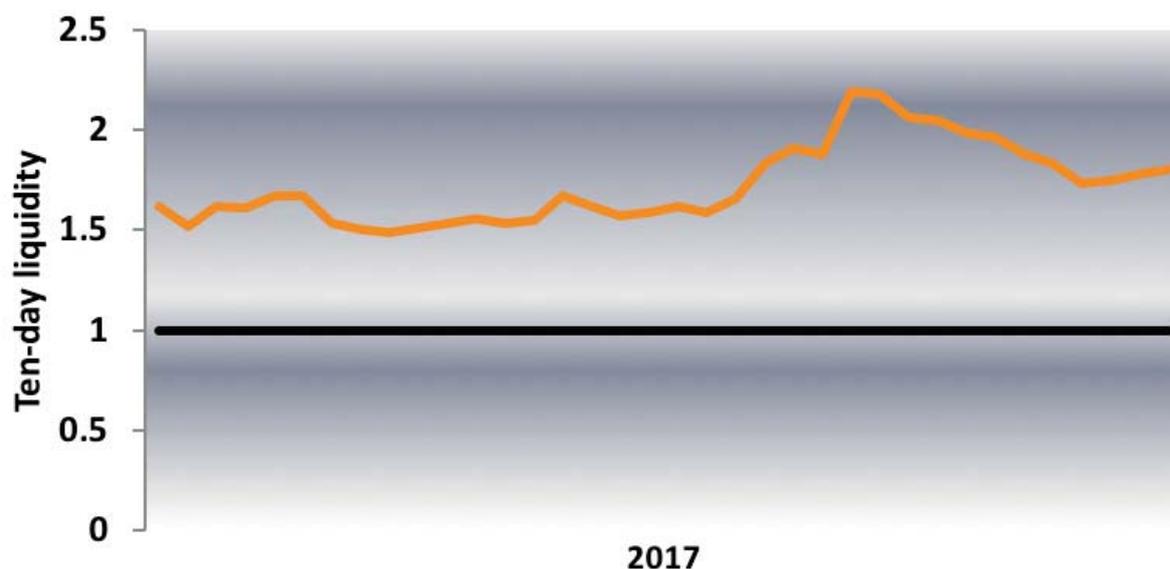
In 2017 the Bank also put emphasis on stabilising domestic sources of funding and expanding its client base, reducing short-term sources in favour of long-term sources of funding and taking new credit lines from foreign banks and international financial institutions

The treasury back office operating as part of the Financial Market Sector succeeded throughout 2017 thanks to its rational liquidity management to maintain liquid assets and overall liquid position of the Bank at a satisfactory level. In addition, the office performed reconciliation of sources of funds with placements by daily, weekly, ten-day and monthly scheduling of available liquid assets. Adequate allocation of funds was performed through close cooperation with other sectors and services in the Bank. All this allowed the Bank to regularly fulfil its obligations towards creditors, as well as to accommodate client requests within the shortest terms possible.

The daily liquidity ratio, which is calculated by the methodology set by the CBCG, was considerably above the legally required minimum of 0.90 throughout 2017.



Furthermore, the ten-day liquidity ratio was above the legal requirement of 1.00

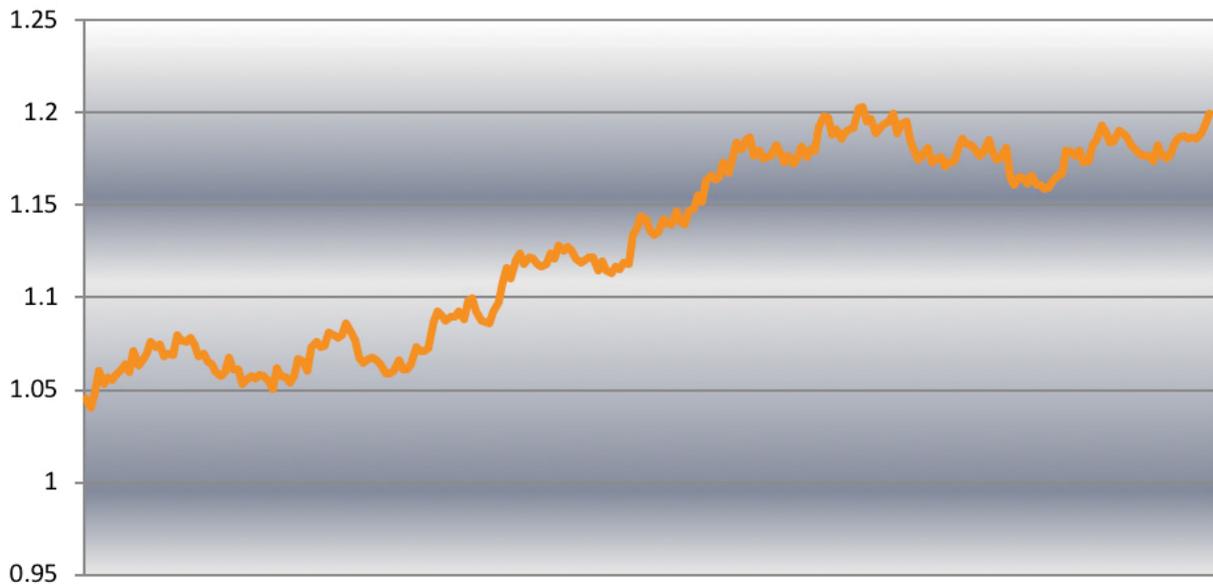


In order to manage tenor liquidity, the Bank regularly monitored structural liquidity indicators through the tenor adjustment of financial assets and liabilities, the review of maturity dates of larger deposits and through the establishment of a stable part of sight deposits thanks to an internally developed model and maintained it at satisfactory levels.

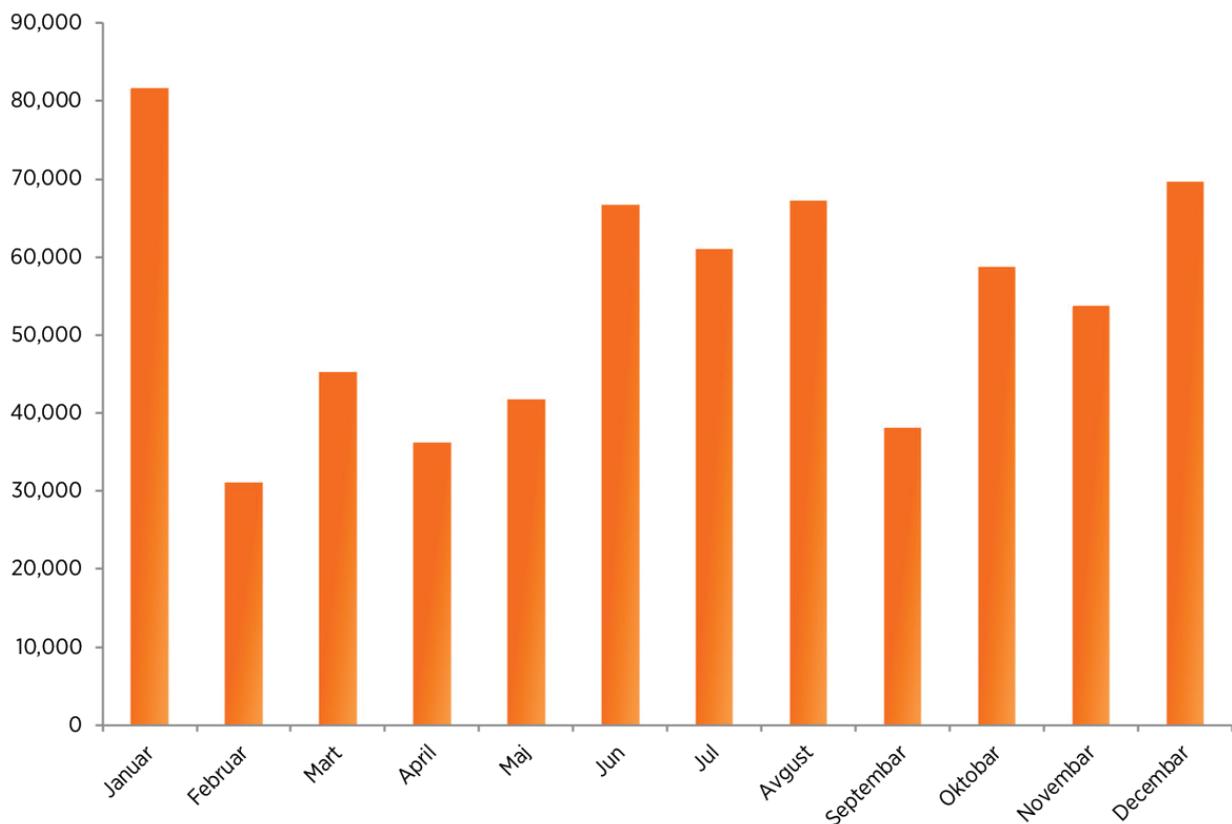
Given that 2017 was marked by a drop in client deposit interest rates and taking into account the caution with which customers now use their own funds, it may be concluded that in these circumstances, the Bank was recognized as one of the most reliable and most liquid of the banks in Montenegro's banking system. This statement is supported by the data that indicate that at the end of 2016 total deposits of the Bank were € 331.09 million and at the end of 2017, € 392.61 million, which is an 18.58% annual growth. Liquidity surpluses, except from credit activities, were also placed in marketable securities.

In 2017, the Bank participated in government securities auctions and made satisfactory return. Also, through activities of the Financial markets sector, the Bank invested assets in other securities in the country and the region.

2017 was marked by considerable fluctuations in exchange rates, particularly when it comes to EUR/USD, which has the strongest impact on the Bank's exposure to exchange rates fluctuations.



In spite of these circumstances, Treasury back office managed to achieve remarkable results in revenue from realised exchange rate differences as a result of adequate exchange rate risk management. At the end of 2017, total revenue from foreign exchange differences amounted to €652 thousand, which had a significant impact on the Bank's final financial results.



Revenues from exchange rate differences in 2017

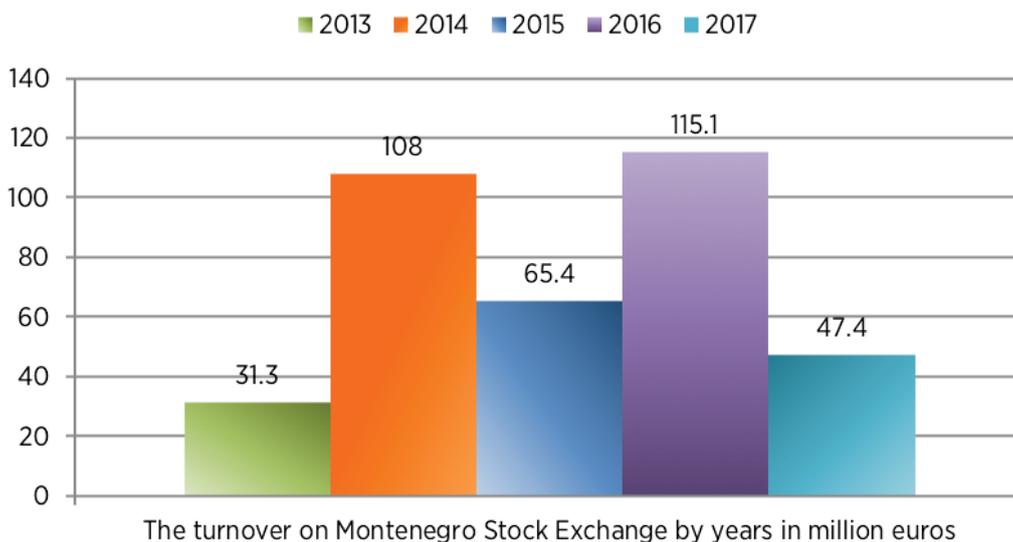
## INVESTMENT BANKING

### MONTENEGRO STOCK EXCHANGE

In 2017, Montenegro Stock Exchange had a trading volume of €47,445,355, down by 58% compared to 2016. The causes are most likely linked to inactive primary market, which did not have a single new issue of shares and bonds.

The Bank issued a new series of subordinated HBO2 bonds last year. It was a restricted issue, open only to previously identified buyers. The value of the issue was 4 million euros. Along with HBO1, Hipotekarna Bank AD Podgorica corporate bonds showed good liquid in secondary market, with a volume of €2.1 million.

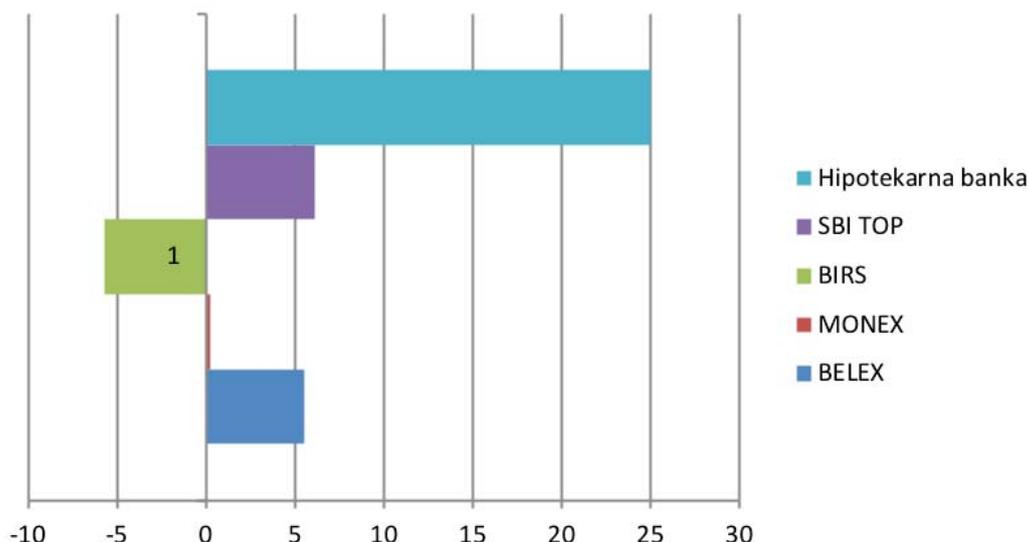
In 2017, MONEX 10 continued a downfall trend and recorded a drop of 16.61% and was at 776.69 percentage points on the last trading day. On 31 March, the index reached its maximum annual value of 985.98 points, while its lowest value in the previous year was recorded on 27 December at 746.97 points. MONEX recorded a drop by 11.6% in the previous year, and was at 10,175 percentage points on the last trading day.



### BROKERING

In 2017, the Hipotekarna Bank Brokerage Unit generated a turnover of EUR12.28 million at Montenegro Stock Exchange, with Hipotekarna Bank maintaining its leading position in the Montenegrin capital market.

The 2017 turnover made by Hipotekarna Bank brokers in foreign markets was 21.75 million euros



### DEALER OPERATIONS

Hipotekarna Bank total investments in equity securities were EUR5.067 million as of 31/12/2017. Its revenues from dividend and realised capital gains were €252 thousand in 2017.

### CUSTODY OPERATIONS

As of 31/12/2017, Hipotekarna Bank clients held €43.89 million worth of securities in Bank's. Hipotekarna Bank remains the leading custody bank in Montenegro. The revenues made by Custody Unit were €211.53 thousand. The Unit's operating income was €87 thousand.

## RISK MANAGEMENT

The risk management department addresses risk centrally, at the level of the Bank.

Risk management includes risk identification, measurement, monitoring and reporting. The department develops risk management policies and procedures as well as risk measurement methodologies and procedures.

The risk management department reports monthly to ALCO committee on the levels of risk taken by the Bank. Based on this information the Committee assesses management performance in risk management.

The risk management department develops reports on Bank's vulnerability to various types of risks and informs the Committee decisions on the limits.

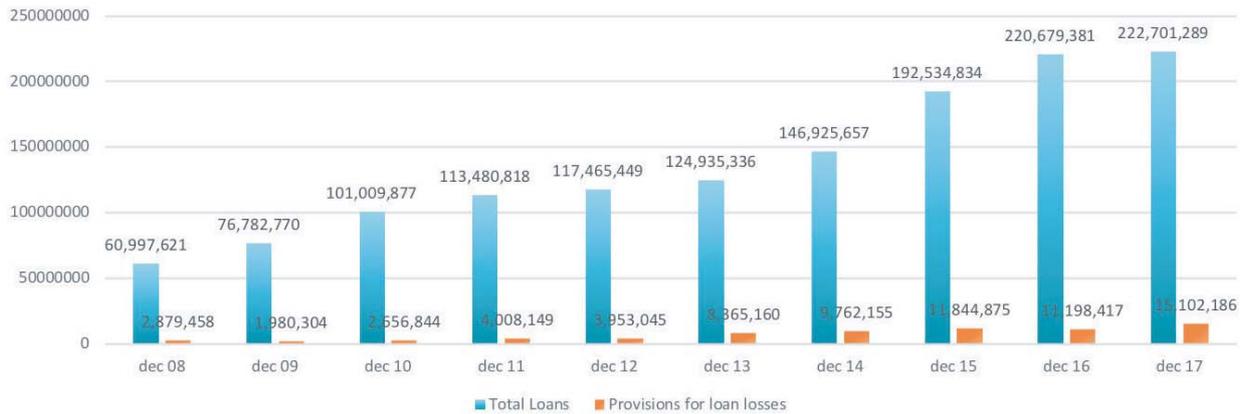
### CREDIT RISK

The Bank manages credit risk at both portfolio and individual levels.

Hipotekarna Bank portfolio on 31/12/2017 was €222,701,289, or up by €2,021,908, or 0.9%, compared to late 2016.

Provisions for loan losses on 31/12/2017 were €15,102,186, or 6.78% of portfolio. Compared to late 2016, the provisions rose by €1,091,968 or 24.86%.

Portfolio / provisions 2008-2017



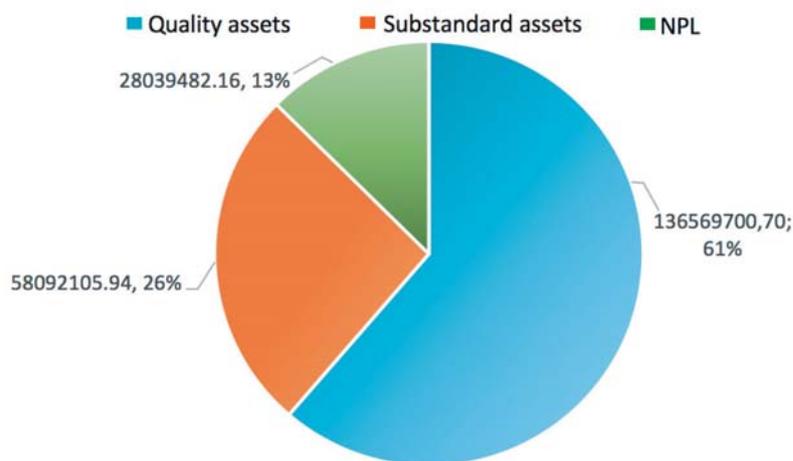
Loan value corrections on 31/12/2017 amounted to €8,924,774, or 4.01% of the portfolio. Compared to late 2016, provisions went up by €2,375,093, or 38%.

2017 Trends in provisions according to an internal model

MODEL	March 17	June 17	Sep 17	Dec 17
Portfolio	218.398.833	220.513.852	221.466.727	222.701.289
Reservations	7.610.760	8.261.824	8.108.659	8.924.774
	3,48%	3,75%	3,66%	4,01%

In the Bank’s overall portfolio, quality assets (A and B1) account for 61.32%, substandard (B2) for 26.09%, and NPLs (C, D and E) for 12.59%.

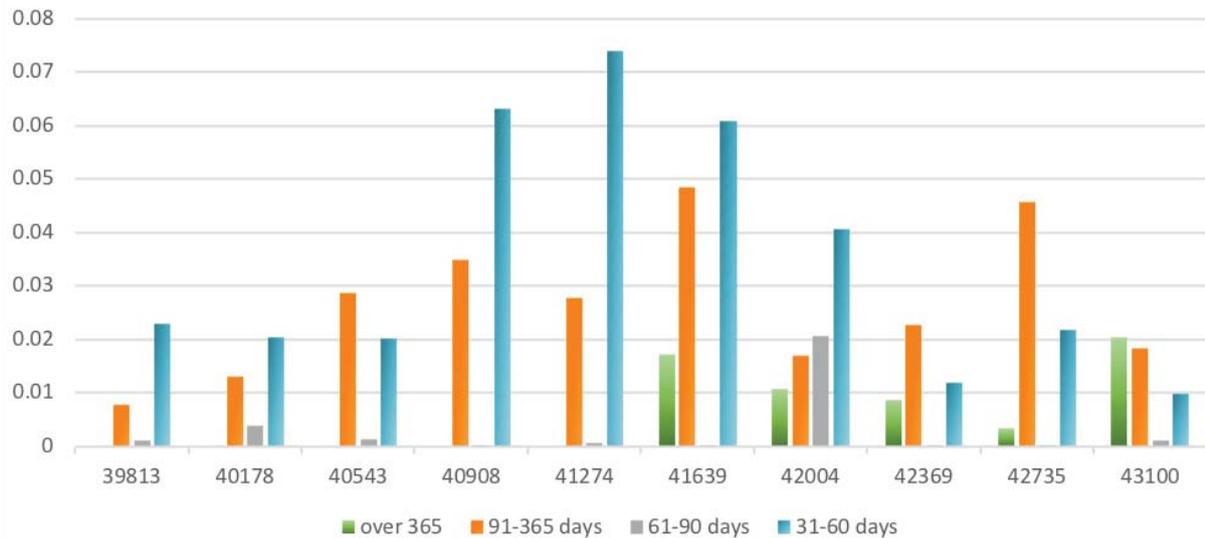
Assets by quality - Dec 2016



NPLs in arrears over 30 days amounted to €11,055,208, or 4.96% of Bank’s total portfolio, on 31/12/2017, while on 31/12/2016 they were €15,650,190 and made 7.09% of overall portfolio.

On 31/12/2017, NPLs in arrears over 90 days amounted to €8,610,333, or 3.87% of Bank portfolio, while on 31/12/2016 they were €10,838,052, or 4.91% of the Bank's overall portfolio.

Claims by category of arrears / total loans



Client migratory movement in Dec 2017 (%)

	A	B1	B2	C	D	E	(closed / internal)
A	94,46%	0,35%	0,03%	0,00%	0,00%	0,00%	0,00%
B1	1,27%	92,29%	1,05%	0,47%	0,00%	0,00%	0,00%
B2	0,09%	0,11%	70,03%	14,54%	0,00%	0,00%	0,00%
C	0,20%	0,01%	0,17%	96,02%	3,56%	0,00%	0,00%
D	1,25%	0,90%	0,00%	2,16%	91,64%	3,87%	0,00%
E	1,58%	0,00%	0,00%	0,00%	22,65%	67,80%	7,90%

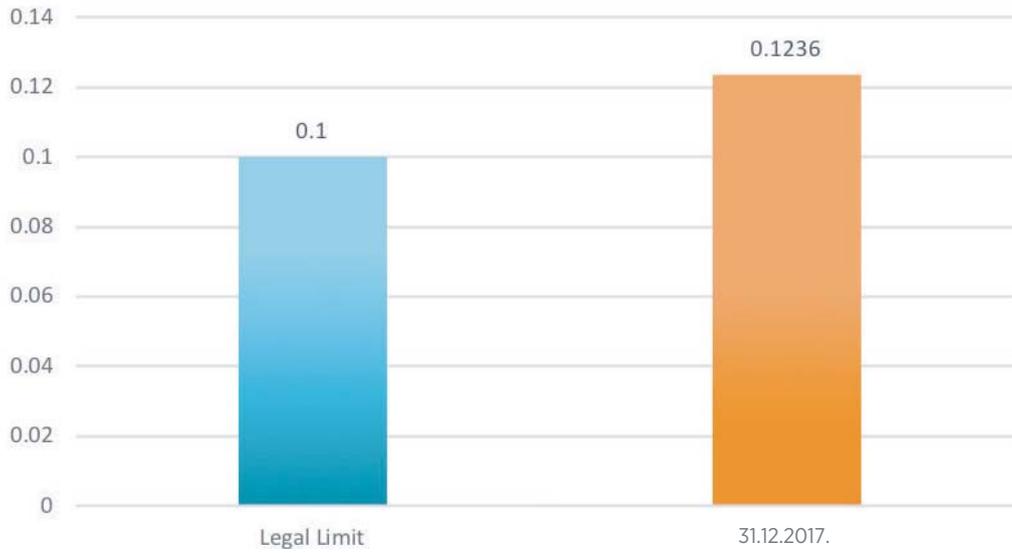
**SECURITIES – WITHIN CREDIT RISK**

On 31 Dec 2017, the Bank's banking book was composed of equity based and debt based financial instruments. In December, all the positions in the banking book were within the limits set by law and bank internal rules. The total value of securities owned by Bank as of 31/12/2017 was €92.572 million, all of which securities available for sale.

**SOLVENCY RATIO**

On 31/12/2017, the solvency ratio was above the statutory limit (10%), or 12.36%. The solvency ratio is the most important indicator of client confidence and serves as protection to Bank's depositors, creditors, and business partners.

### Solvency ratio for 2017



### Structure of equity required to cover all the risks

