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BRODOGRAĐEVNA INDUSTRIJA SPLIT d.d.

Annual report of the Group
31 December 2016

CONTENT

Management report ……………………………………………………………………………………1-13

About the company………………………………………………………………………………………. 1

Share capital and ownership structure……………………………………………………………… 1

Supervisory Board and management…………………………………………………………………2

Organisation structure ……………………………………………………………………………… 3-5

Human resources………………………………………………………………………………………… 6

Actual production capacity ………………………………………………………………………….. 7

Financial operations ……………………………………………………………………………………. 8

Business risks …………………………………………………………………………………….…. 9-11

Research and development activities ……………………………………………………………. 11

Presumable future development of the company ………………………………………….. 12

Management activities for the year 2017 ……………………………………………………..13

Responsibilities of Management for the preparation of the Annual report……….……. 14

Independent Auditor's Report on the consolidated financial statements ….….…… 15–17

Consolidated financial statements ………………………………………………………..…….…. 18–65

Consolidated statement of comprehensive income ………………………………………… 18

Consolidated statement of financial position ……………………………………………..…… 19

Consolidated statement of changes in equity ……………………………………………….. 20

Consolidated statement of cash flows ……………………………………………………….. 21

Notes to the consolidated financial statements ………………………………………… 22-65

Group Management report

1. ABOUT THE COMPANY

Brodograđevna industrija Split d.d. (shorter: Brodosplit d.d.) is the parent of the 54 "daughter" companies (one in bankruptcy), and 20 "grandchildren" companies.

The most important activity of the Group Brodosplit is shipbuilding production: constructing and equipping various types of ships for the merchant marine, special purpose ships, as well as various products in the field of marine technology.

Within the Group, different programs have been developed like diesel-engine production, casting gray and nodular cast iron, the production of various products of metallic and non-metallic marine equipment, corrosion protection and other services. Brodosplit strongly stepped on to the market outside of shipbuilding in 2013, on which the company has been fully working in the upcoming years.

All the programs are implemented independently from contracting, design, production, testing to delivery.
The Company, through different organizational forms and under different names, has been operating since 1931. The many activity of the Company is shipbuilding.

2. SHARE CAPITAL AND OWNERSHIP STRUCTURE

The Company Brodograđevna industrija Split d.d. is registered in the register of the Commercial Court in Split under the registration number: 060175040, PIN: 18556905592.

The General Assembly of the Company at 31 December 2016 had the following structure:

SHARE HOLDER	SHARE No.	PERCENT
	UNITS	%
DIV BRODOGRADNJA D.O.O.	8.903.280	99,76
HRVATSKA GOSPODARSKA KOMORA	11.637	0,13
UNIQA D.D.	5.894	0,07
PHISICAL INDIVIDUALS	3.625	0,04
REPUBLIC OF CROATIA	1	0
TOTAL	**8.924.437**	**100%**

The share capital amounts to HRK 535,466,220.00, divided into 8,924,437 ordinary shares with a nominal value of HRK 60.00.

3. SUPERVISORY BOARD AND MANAGEMENT

Supervisory board

The Supervisory Board consists of 5 members. The General Assembly elects three members. One member is appointed by the employees in accordance with labour legislation. One member is appointed by the CERP. The mandate of members is four years with the possibility of re-election.

In 2015, the Supervisory Board was composed of:

1. Zdenko Šoš - Chairman
2. Željan Horvat - Deputy Chairman
3. Tomislav Pokaz - Member

After Mr. Tomislav Pokaz resigned from membership in the Supervisory Board on 9 February 2016, the board is composed of:

1. Zdenko Šoš - Chairman
2. Željan Horvat - Deputy Chairman

On 29 July 2016 Saša Vladić was appointed by the court as a member of the Supervisory Board and the Supervisory Board acts in the following composition:

1. Zdenko Šoš - Chairman
2. Željan Horvat - Deputy Chairman
3. Saša Vladić - Member

On 29 July 2016, CERP appointed Darko Bandula as member of the Supervisory Board and the Supervisory Board acts in the following composition:

1. Zdenko Šoš - Chairman
2. Željan Horvat - Deputy Chairman
3. Saša Vladić - Member
4. Darko Bandula - Member

On 31 August 2016 the Assembly elected a new member of the Supervisory Board, Teuta Duletić. As new member of the Supervisory Board has been chosen, Saša Vladić ceased to act as member of Supervisory Board. Until 31 December 2016 Supervisory Board consisted of:

1. Zdenko Šoš - Chairman
2. Željan Horvat - Deputy Chairman
3. Darko Bandula
4. Teuta Duletić

Management Board

The Management Board consists of three members - Chairman and two members. All three members of the Management Board represents the company individually and independently, and are appointed and recalled by the Supervisory Board. Management of Brodograđevna industrija Split d.d. in 2016 consists of the following members:

1. Tomislav Debeljak - Chairman of the Board since 2 May 2013
2. Darko Pappo - a board member since 2 May 2013
3. Vlatko Kvesić - a board member since 21 May 2015

4. ORGANISATION STRUCTURE

The Company is the parent company, which operates over below listed subsidiaries in which it has a 100% share interest:

1. Brodosplit – Brodogradilište specijalnih objekata d.o.o. - the main activity is the construction of ships;
2. Brodosplit – Metaloprema d.o.o. - in bankruptcy;
3. Brodosplit – Armature d.o.o. - primary activity is the production of reinforcement;
4. Brodosplit – Dizalice d.o.o. - core business is the construction of engines for lifts;
5. Brodosplit - Plovidba d.o.o. - core business is marine transportation;
6. Brodosplit – Tvornica dizel motora d.o.o. - core business is the production and modification of engines, turbines and power equipment;
7. Brodosplit - Izolacija d.o.o. - main activity is construction that requires special equipment, and construction and insulation works;
8. Brodosplit – Metalna oprema i konstrukcije d.o.o. - core business is the production and modification of metalic structures;
9. Brodosplit – Nemetalna oprema d.o.o. - core business is the production and modification of non-metallic structures;
10. Brodosplit – Antikorozivna zaštita d.o.o. - core business is corrosion protection, sandblasting and painting of ships;
11. Brodosplit - Boja d.o.o. - core business is the repair and maintenance of ships and boats;
12. Brodosplit - Blok d.o.o. - the main activity is the construction of ships and floating structures;
13. Brodosplit – Čelik d.o.o. - basic activity is the production of metal structures and their parts;
14. Brodosplit - Holding d.o.o. - the main activity is the construction of ships and floating structures;
15. Brodosplit - Montaža d.o.o. - basic activity is the production of metal structures and parts;
16. Brodosplit – Opremanje plovnih objekata d.o.o. - basic activity is the production of metal structures and parts;
17. Brodosplit - Stroj d.o.o. - main activity is machining;
18. Brodosplit – Transportna sredstva d.o.o. - core business is the rental and lease of other machinery, equipment and tangible goods;
19. Brodosplit - Trgovina d.o.o. - the main activity is the wholesale of other machinery and equipment;
20. Brodosplit - Trup d.o.o. - basic activity is the production of metal structures and their parts;
21. Brodosplit – Zaštita trupa od korozije d.o.o. - basic activity is the production of metal structures and their parts.

4. ORGANISATION STRUCTURE (continued)

The Company has 30% stake and management rights in the following companies:

1. Brodosplit – Alatnica d.o.o. - basic activity is machining;
2. Brodosplit – Atest d.o.o. - core business is service protection with the help of security systems;
3. Brodosplit – Automatizacija d.o.o. - core business is the management of computer facilities;
4. Brodosplit – Bravarija i limarija d.o.o. - core business is repair of metal products;
5. Brodosplit – Brodska i ostala oprema d.o.o. - basic activity is the production of metal structures and parts;
6. Brodosplit – Cjevarska izrada d.o.o. - core business is iron casting;
7. Brodosplit – Čišćenje d.o.o. - core business is other cleaning activities;
8. Brodosplit – Gradnja d.o.o. - core business is the construction of various buildings;
9. Brodosplit – Informatika d.o.o.- core business is the management of computer facilities;
10. Brodosplit – Interijer i završni radovi d.o.o. - core business is the installation of carpentry;
11. Brodosplit – Istraživanje i razvoj d.o.o. - core business is research and experimental development on natural sciences and engineering;
12. Brodosplit – Izvor energije vjetroparkova d.o.o. - the core business is the rental and lease (leasing) of other machinery, equipment and tangible goods;
13. Brodosplit – Klimatizacija i ventilacija d.o.o. - basic activity is the installation of water, sewage, and gas installations for heating and air-conditioning;
14. Brodosplit – Korporativna zaštita d.o.o. - core business is the private security;
15. Brodosplit – Laboratorij d.o.o.- core business is technical testing and analysis;
16. Brodosplit – Ljevaonica d.o.o. - core business is iron casting;
17. Brodosplit – Ljudski resursi d.o.o. - core business is providing human resources;
18. Brodosplit – Metalne konstrukcije d.o.o. - basic activity is the production of metal structures and their parts;
19. Brodosplit – Namještaj po mjeri d.o.o. - core business is the installation of carpentry;
20. Brodosplit – Oblaganje d.o.o. - basic activity is the construction of ships and floating structures;
21. Brodosplit – Održavanje d.o.o. - basic business is repairing machines;
22. Brodosplit – Optimizacija i ekologija d.o.o. - basic activity is the remediation activities and other waste management services;
23. Brodosplit – Otpremništvo d.o.o. - core business is the other support activities for transportation;
24. Brodosplit – Plovne dizalice d.o.o. - core business is the rental and leasing of water transport equipment;
25. Brodosplit – Najam vozila d.o.o. - core business activity is renting and lease (leasing) of cars and light motor vehicles;
26. Brodosplit – Privremena energetika d.o.o. - core business is the production of electricity;
27. Brodosplit – Produkt plinske elektrane d.o.o. - basic activity is the installation of water, sewage, and gas installations for heating and air-conditioning;

4. ORGANISATION STRUCTURE (continued)

28. Brodosplit – Računovodstvo i financije d.o.o. - core business is accounting, bookkeeping and auditing activities, tax consultancy;
29. Brodosplit – Servis brodova d.o.o. - core business is the repair and maintenance of ships and boats;
30. Brodosplit – Skela d.o.o. - basic activity is the production of metal structures and their parts;
31. Brodosplit – Snaga energije d.o.o. - core business is the production of electricity;
32. Brodosplit – Strojna obrada d.o.o. - basic activity is machining;
33. Brodosplit – Vjetrostupovi d.o.o. - basic activity is the production of metal structures and their parts.

A subsidiary, Brodosplit – Plovidba d.o.o. is the 100% owner of the following companies:

1. BS STAR SHIPPING INC.
2. BURIN WIND CRUISE SHIPPING INC.
3. GARBIN WIND CRUISE SHIPPING INC.
4. LEVANT WIND CRUISE SHIPPING INC.
5. MAESTRAL WIND CRUISE SHIPPING INC.
6. PULENAT WIND CRUISE SHIPPING INC.
7. GREEN4SEA SHIPPING 1 INC.
8. GREEN4SEA SHIPPING 2 INC.
9. GREEN4SEA SHIPPING 3 INC.
10. GREEN4SEA SHIPPING 4 INC.
11. DREAM ONE SHIPPING INC.
12. RIVER CRUISE SHIPPING
13. POLAR EXPEDITIONS B.V., Netherlands
14. POLAR EXPEDITIONS Inc., Marshall Islands
15. POLAR EXPLORER Inc.
16. XB AHTS COMPANION SHIPPING INC.
17. XB AHTS GUARDIAN SHIPPING INC.
18. XB AHTS HERO SHIPPING INC.
19. XB AHTS SUPPORTER SHIPPING INC.

A subsidiary, Brodosplit - Holding Ltd. the 100% owner of the company Brodosplit Italia, based in Italy.

5. HUMAN RESOURCES

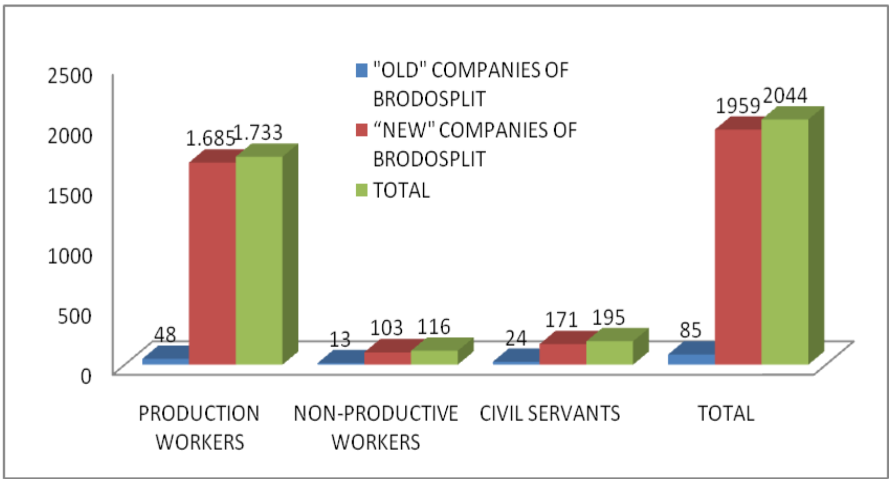
As at 31 December 2016, 2,044 employees were employed throughout the Group. Out of that, 85 employees were employed in so-called "old" companies and 1,959 employees in "new" companies. New contracts in "old" companies have 38 employees, and the cancellation period runs for another 13.

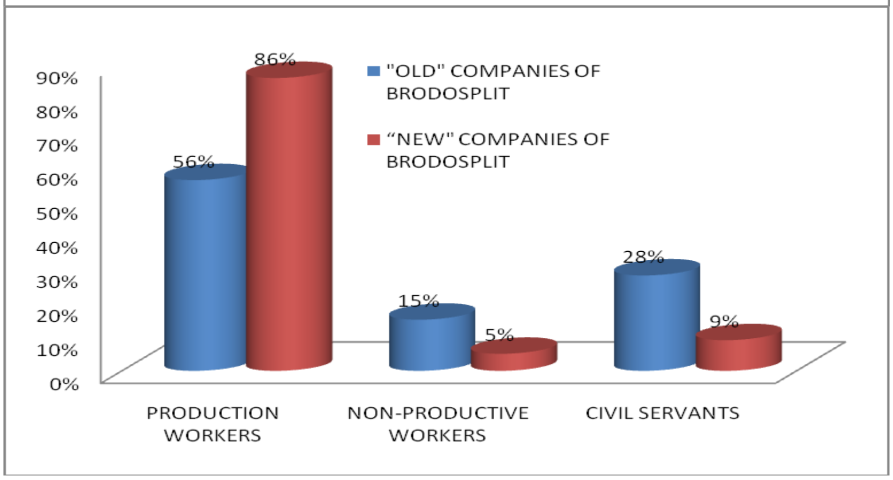
In total there were 1,733 production workers (85%), 116 non-productive workers (6%) and 195 clerks (10%).

Table: Number of employees per group:

31.12.2016.	PRODUCTION WORKERS		NON-PRODUCTIVE WORKERS		CIVIL SERVANTS		TOTAL	
	NUMBER	%	**NUMBER**	%	**NUMBER**	%	**NUMBER**	%
"OLD" COMPANIES OF BRODOSPLIT	**48**	56%	**13**	15%	**24**	28%	**85**	4%
"NEW" COMPANIES OF BRODOSPLIT	**1.685**	86%	**103**	5%	**171**	9%	**1.959**	96%
TOTAL	**1.733**	**85%**	**116**	**6%**	**195**	**10%**	**2.044**	**100%**

Number of employees in group on 31.12.2016.





5. HUMAN RESOURCES (continued)

	NEW				GONE			
GGMM	P	NP	C	**Grand Total**	P	NP	C	**Grand Total**
201601	20			**20**	36	3	3	**41**
201602	13		1	**14**	14	1	2	**17**
201603	9	1	2	**12**	16	2	1	**19**
201604	23			**23**	13	3	4	**20**
201605	4			**4**	14	2		**16**
201606	51		1	**52**	25	2	3	**30**
201607	33		1	**34**	29		2	**31**
201608	23		4	**27**	19	2	1	**22**
201609	18			**18**	25	2	2	**29**
201610	7		1	**8**	25	2	3	**30**
201611	15	1	5	**21**	23	4	3	**30**
201612	26		1	**27**	21		4	**25**
Grand Total	**242**	**2**	**16**	**260**	**260**	**23**	**28**	**311**

6. ACTUAL PRODUCTION CAPACITY

The following table states the realization of the production capacity of the main stages of building ships for the period from 2012 to 2016.

Num.	DESCRIPTION	Realized	Realized	Realized	Realized	Realized
br.		2012.	2013.	2014.	2015	2016
	SHIPBUILDING					
1.	Start process CM - pc	2	1	2	5	2
2.	Keel laying - pc	2	0	1	6	2
3.	Launching – pc	1	1	2	1	2
4.	Handover - pc	1	0	1	1	2

During 2016, the newbuilding 482 was successfully delivered - concrete boat for a domestic customer and a project for the construction of the hull and the superstructure of the nautical tourism newbuilding plant 539 was completed.

Brodograđevna industrija Split d.d. stepped on the market outside of shipbuilding in 2015 and in 2016 continued intensive work on building the steel barrier to defend Venice from flooding.
From non shipping projects, a project for the construction of residential containers and portal cranes for foreign buyers has been completed.

7. FINANCIAL OPERATIONS

Actual operating result of Brodosplit Group for the year 2016 recorded total comprehensive income in the amount of HRK 34 million, while in 2015 a comprehensive loss in the amount of HRK 156 million.

Profit is derived from regular operations profit in the amount of HRK 30 million and loss from financial activities in the amount of HRK 9 million.

On 31 December 2016, the capital of the Brodosplit Group amounts to HRK 925 million.

Based on the data on financial performance, certain performance indicators can be determined, of which the most important are shown in the table below:

	2016	**2015**
Current assets	707,293	621,935
Current liabilities	304,687	435,844
Current ratio	**2.32**	**1.43**
Money + receivables	454,412	334,595
Total liabilities	304,687	435,844
Quick ratio	**1,49**	**0.77**
Total liabilities	532,178	524,317
Total assets	1,456,528	1,411,003
Gearing	**0.37**	**0.37**
Total revenues	648,119	407,931
Total assets	1,456,528	1,411,003
Turnover ratio of total assets	**0.44**	**0.29**
Sales revenue	552,827	372,292
Receivables and accrued revenues	276,068	96,709
Turnover ratio of receivables	**2.00**	**3.85**

1. Current ratio = Current Assets / Current Liabilities, it is desirable that the coefficient is at least 2, which means that the company operates in liquidity.

2. Quick ratio = Cash + Current Receivables / Current Liabilities, it is desirable that the coefficient is at least 1.

3. Gearing = Total Liabilities / Total Assets shows the ratio in which the company is financed by foreign capital and how much by its own capital.

4. Asset turnover= Total Revenue / Total Assets shows how many times the total assets are converted into income. This shows the efficiency of the capital used to finance assets.

5. Receivables turnover = Sales Revenue / Receivables shows how many times a year the receivables are charged.

8. BUSINESS RISKS

Through its business, the Group is exposed to the following risks:
• Credit risk
• Fair values of cash flow or interest rate risk
• Currency risk
• Market risk
• Liquidity risk
• Regulation risk

Capital risk management

The Group manages its capital so as to ensure business continuity, while maximizing the return to shareholders through the optimization of the balance of debt and equity. The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

The capital structure of the Group consists of debt, which includes borrowings, cash and cash equivalents and equity, which includes the registered capital and accumulated losses. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

The Group monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt (borrowing) is calculated as total borrowings (including long-term and short-term in the balance sheet) less cash and cash equivalents and short-term deposits. Total capital is calculated in a way that net debt is added to capital and reserves shown in the balance sheet.

The ratio of net debt to capital (gearing ratio) on the reporting date was as follows:

(in thousands of HRK)	**2016**	**2015**
Debt (short-term loan)	(188,608)	(51,918)
Cash and cash equivalents	41,204	18,273
Net debt	(147,404)	(33,645)
Capital	(920,837)	(886,686)
Debt to equity ratio	16%	4%

Financial risk management

The Group is in the most important part exposed to the international market, and the Group is subject to the impact of changes in prices of the main raw materials on the world market which are dependent on the movement of foreign exchange rates, and is significantly exposed to the impact of exchange rate differences.

Financial risks include market risk (including currency risk and price risk), credit risk, liquidity risk and cash flow interest.

8. BUSINESS RISKS (continued)

Credit risk

Credit risk refers to the risk of default of counterparties, which will produce a financial loss to the Group. The Group has adopted a policy of only dealing with creditworthy counterparties, ensuring the necessary excess insurance to mitigate the risk of financial loss due to non-fulfillment of contractual obligations. The Group's exposure and the credit standing of counterparties are continuously monitored, and the total amount of the transaction is distributed among authorized parties.

Contracting the construction of a ship with customers of unknown or with lack of creditworthiness, estimated by the Group, will be secured with so-called Payment guarantees from first class banks. The Group's policy is that suppliers are paid advance payments of significant amounts only after the issuance of Refund Guarantees.

Interest rate risk

Most of the borrowings on which interest is charged are contracted at a fixed and floating interest rates. The risk is managed by maintaining a suitable combination between fixed and floating interest rates on lending. The Group is not protected from these risks at this time.

Currency risk

The Group is exposed to exchange rate risk with contract defined raw material prices related to foreign currency. The currency subject to risks is primarily EUR and USD. Group is not currently protected from this risk.

The following table presents the carrying amounts of monetary assets and monetary liabilities denominated in foreign currencies at the reporting date.

(in thousands of HRK)	**Liabilities**		**Assets**	
	2016	**2015**	**2016**	**2015**
EUR	239,831	45,244	88,497	81,325
USD	1,534	744	5,527	3,230
GBP	295	730	442	363
SEK	38	48	-	16
Other currencies	226	173	-	52

As at 31 December 2016, if EURO had weakened / strengthened by 1.00% against the HRK, with all other variables held constant, the loss for the reporting period would have been HRK 1,513 thousand lower / (higher), mainly as a result foreign exchange gains / (losses) on foreign exchange differences arising from the translation of receivables, payables, borrowings and foreign cash funds denominated in EUR.

According to estimates made by management, the impact of changes in other currency has no significant impact on the Group's financial statements.

Market risk

The Group and its operations are exposed to a significant price increase not only for ferrous metallurgy, but also prices of other raw materials. By contracting the so-called Safeguard clauses for ferrous metallurgy on the basis of which the inflow to the delivery of the ship increases by the amount which exceeded the cost of ferrous metallurgy in comparison to the estimated costs of the same when contracting the shipbuilding, relatively ensure the Group neutralizing the price risk.

8. BUSINESS RISKS (continued)

Liquidity risk

It refers to the risk that the proceeds will not be sufficient to cover current cash expenditures. The Group manages liquidity risk by maintaining adequate reserves, banking facilities and reserve borrowed funds, continuously monitoring forecast and actual cash flows and by comparing maturity profiles of financial assets and liabilities.

Regulatory risk

Considering the Croatian accession to the European Union, the Group is significantly exposed to regulatory risk, which is for the most part realized in changes in the legislative sphere of state aid. Namely, that the Group used the state aid in amounts significant for maintaining profitability and liquidity, this risk is considered to be significant and yet uncontrollable.

9. RESEARCH AND DEVELOPMENT ACTIVITIES

Much of the research and development activities, in the ranks of the development of innovative products and services, is in accordance with the thematic areas identified in the Strategy for smart specialization of Croatia 2016 – 2020. The Company and the Group positioned itself as the representative of the consortium with the aim of improving the innovation environment, intensifying research and development activities and increasing competitiveness, through collaborative cooperation with business partners and research institutions.

Effective cooperation is established in research and development projects with 4 scientific research institutions (Faculty of Mechanical Engineering and Naval Architecture, Faculty of Electrical Engineering, Mechanical Engineering and Naval Architecture, University of Split, Faculty of Maritime Studies and the Faculty of Civil Engineering, Architecture of the University of Split). Through planned projects we aim to reach the top of the global/ European manufacturers of sophisticated ships and floating structures on higher value-added markets and offer products according to the highest standards with efficient energy use and minimal environmental impact in mind.

Also, we have developed many different models of ships intended to significantly save fuel and reduce greenhouse gas emissions.

As a technological research and development organization that has human resources, material resources, infrastructure and experience in research, development and implementation of the most complex products and services for renowned clients, great emphasis is placed on innovation and research and development as a basis for competitive advantage and sustainable development in the industry as well as on exchange of knowledge and experience with higher education organizations. The Group has highly educated shipbuilders and engineers of various technical professions, with extensive experience in a wide range of projects for different types of ships.

10. PRESUMABLE FUTURE DEVELOPMENT OF THE GROUP

The main objective of the Brodosplit Group is to ensure long-term profitability and stable growth. Brodosplit group now has a total of nineteen new ships ordered, worth about HRK 1.8 billion. As for the market outside of shipbuilding, currently ordered is the construction of steel barriers to defend Venice from flooding.

The future development of the company and the Group is focused on shipbuilding. Part of it on developing and offering projects of different types of passenger ships, medium in size, approximately 100 to 250 m in length (cruise ships, polar expedition ships, ships / ferries to transport passengers, cars / trucks, mega yachts etc.), and on intensifying the bidding for the project “The coastal patrol ship” in the Middle Eastern markets.

As far as the non-shipbuilding market is concerned, the construction of 21 steel doors for the San Nicolo Sea Gate is currently contracted, totaling around HRK 190 million.

The part which is focused on markets outside of shipbuilding, future development focuses on more extensive infrastructure projects in Croatia and Europe, such as the Pelješac Bridge, LNG terminal plates, Krk LNG terminal, etc.

After the 2016 business year, work has intensified on the development of a project and discussions with customers regarding the construction of a cruise ship with a capacity of 60,000 GT for a European client. Potential contract signing is expected in September 2017.

Furthermore, in late 2016 and early 2017, activities have intensified on the project of constructing luxury yachts, 133 m in length, for a client from Saudi Arabia. and the imminent signature of a letter of intent and the continued development of the project is expected.

In conclusion:

- The Group has taken and is taking a series of actions to restructure the Group Brodosplit and is creating future profitable operations,
- The Group is working intensively on its employment capacity, in shipbuilding and in markets outside of shipbuilding,
- The Group has streamlined the number of employees and introduced a flexible organization.

11. MANAGEMENT OBJECTIVES FOR THE YEAR 2017

QUALITY:

1. To increase the share of own products and services in the final products of the Group,
2. To attract new customers and develop new products,
3. Introduction of energy management systems according to ISO 50001: 2011,
4. Transition to Quality Management System, version ISO 9001-2015,
5. Human resources training,
6. Increase in technological levels of processes with the improvement of infrastructure and working environment.

ENVIRONMENT:

1. Separate collection and disposal of various types of waste,
2. Reduction of emissions of volatile organic compounds into the atmosphere to targeted emissions,
3. Clean underwater shipyard in labour-intensive areas,
4. Arrangement of a disposal space for non-hazardous waste at the Point Šilo,
5. Implementation of Group waste water disposal obligations.

HEALTH AND SAFETY AT WORK:

1. Prevention of work-related injuries,
2. An increase in the level of security for new buildings through the procurement of "safety" equipment,
3. The introduction of the full use of the safety operating voltage when working in enclosed metal spaces,
4. Improvement of fire protection systems in Group buildings.

ENERGY:

1. Prevention of inefficient and unnecessary use of energy,
2. Enhance the monitoring of consumption and use of energy sources through aspects and variables that depend on energy performance,
3. Improvement of consumer energy efficiency

Tomislav Debeljak	Darko Pappo	Vlatko Kvesić
Chairman of the Board	*Member of the Board*	*Member of the Board*

BRODOGRAĐEVNA INDUSTRIJA SPLIT
dioničko društvo, Split

Responsibilities of Management for the preparation of the Annual report

The Management Board is responsible for preparation of consolidated financial statements for each financial year which give a true and fair view of the financial position, results of operations and cash flows for the period in accordance with applicable accounting standard, and is responsible for maintaining proper accounting records to enable the preparation of such financial statements and consolidated financial statements at any time. The Management Board has a general responsibility for taking such steps which are reasonably available to it to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

The Management Board is responsible for selecting suitable accounting policies to conform with applicable accounting standards and then apply them consistently; make judgements and estimates that are reasonable and prudent; and prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Company and the Group will continue in business.

The Management Board is responsible for the preparation of the Management Report of the Group in accordance with applicable requirements of the Article 21 and 24. of the Croatian Accounting Act.

Management report set on pages 1 to 13 and the consolidated financial statements set out on pages 18 to 65 were authorised by the Management Board on 21 August 2017.

Tomislav Debeljak	Darko Pappo	Vlatko Kvesić
Chairman of the Board	*Member of the Board*	*Member of the Board*

BRODOGRAĐEVNA INDUSTRIJA SPLIT
dioničko društvo, Split

Independent auditors' report to the shareholders of Brodograđevna industrija Split d.d.

Opinion

We have audited the consolidated financial statements of Brodograđevna industrija Split d.d. ("the Company") and its subsidiaries („the Group"), which comprise the consolidated statement of financial position as at 31 December 2016, the consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2016, and of its consolidated financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards adopted by EU ("IFRS adopted by EU").

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing. Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the Financial Statements* section of our report.

We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in Croatia and we have fulfilled our other ethical responsibilities in accordance with these requirements.

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

Management report

Management is responsible for the Management report. Our opinion on the consolidated financial statements does not cover the Management report. In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated and whether the Annual report includes the disclosures required by Articles 21 and 24 of the Croatian Accounting Act.

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

- the information given in the Management report, containing the information referred to in Article 21, of the Croatian Accounting Act for the financial year for which the financial statements are prepared, is consistent, in all material respects, with the financial statements; and
- the Management report has been prepared, in all material respects, in accordance with the applicable legal requirements of the Croatian Accounting Act.

This version of our report is a translation from the original, which was prepared in Croatian language. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of the report takes precedence over translation.

Independent auditors' report to the shareholders of Brodograđevna industrija Split d.d. *(continued)*

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

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS adopted by EU and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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

Those charged with governance are responsible for overseeing the Company's and Group's financial reporting process.

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

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

As part of an audit in accordance with International Standards on Auditing, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

Independent auditors' report to the shareholders of Brodograđevna industrija Split d.d. *(continued)*

Auditors' Responsibilities for the Audit of the Financial Statements (continued)

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

KPMG Croatia d.o.o.

KPMG Croatia d.o.o. za reviziju
Croatian Certified Auditors
Eurotower, 17th floor
Ivana Lučića 2a
10000 Zagreb, Croatia
Zagreb, 21 August 2017

For and on behalf of KPMG Croatia d.o.o. za reviziju:

KPMG Croatia
d.o.o. za reviziju
Eurotower, 17. kat
Ivana Lučića 2a, 10000 Zagreb

Tony Ilijanić
Management board member
Croatian Certified Auditor

This version of our report is a translation from the original, which was prepared in Croatian language. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of the report takes precedence over translation.

BRODOGRAĐEVNA INDUSTRIJA SPLIT d.d.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 DECEMBER 2016

(in thousands of HRK)	**Note**	**2016**	**2015**
Revenue	*5*	552,827	372,292
Other operating income	*6*	77,259	17,495
Changes in inventories - work in progress and finished goods		66,557	140,503
Material expenses	*7*	(298,493)	(285,232)
Cost of goods sold		(5,979)	(1,856)
Employees costs	*8*	(224,385)	(238,909)
Depreciation and amortisation	*9*	(32,453)	(29,421)
Other operating expenses	*10*	(105,413)	(131,257)
Operating loss		**29,920**	**(156,385)**
Finance income	*11*	18,033	18,144
Finance costs	*12*	(27,086)	(25,819)
Net finance cost		**(9,053)**	**(7,675)**
Share in net loss of joint venture	*18*	(99)	(399)
Gain / (Loss) before tax		**20,768**	**(164,459)**
Income tax	*13*	8,286	3,940
Net loss		**29,054**	**(160,519)**
Other comprehensive income			
Revaluation of property, plant and equipment (net of tax)	*25 iii)*	4,739	3,924
Change in fair value of available for sale financial assets (net of tax)	*17*	7	109
Foreign exchange gains / (losses)		2	-
Total comprehensive income / (loss)		**33,802**	**(156,486)**
Profit / (loss) attributable to:			
Owners of the Company		27,984	(161,314)
Non-controlling interests		1,070	795
		29,054	**(160,519)**
Total comprehensive income / (loss) attributable to:			
Owners of the Company		32,732	(157,281)
Non-controlling interests		1,070	795
		33,802	**(156,486)**

Accompanying notes on pages 22 to 65 form an integral parts of these financial statements

BRODOGRAĐEVNA INDUSTRIJA SPLIT d.d.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2016

(in thousands of HRK)	Note	2016	2015
ASSET			
Intangible assets	*14*	13,969	1,465
Property, plant and equipment	*15*	682,013	651,039
Investment property	*16*	4,472	5,381
Non-current investments	*17*	343	343
Joint venture	*18*	11,960	9,560
Trade and other receivables	*19*	36,478	121,280
Non-current assets		**749,235**	**789,068**
Inventories	*21*	252,881	287,340
Trade and other recievables	*22*	413,208	316,322
Cash and cash equivalents	*23*	41,204	18,273
Current assets		**707,293**	**621,935**
TOTAL ASSETS		**1,456,528**	**1,411,003**
EQUITY AND LIABILITIES			
Share capital	*25 i)*	535,466	535,466
Reserves	*25 ii), iii), iv)*	230,203	257,134
Retained earnings		155,168	91,187
		920,837	**883,787**
Non-controlling interest		3,513	2,899
Total equity		**924,350**	**886,686**
Provisions	*26*	21,405	34,296
Trade payables	*28*	13,226	-
Loans and borrowings	*28*	151,156	-
Deferred tax liabilities	*13*	41,704	54,177
Non-current liabilities		**227,491**	**88,473**
Provisions	*27*	12,157	17,311
Loans and borrowings	*28*	37,452	51,918
Trade and other liabilities	*29*	255,078	366,615
Current liabilities		**304,687**	**435,844**
Total liabilities		**532,178**	**524,317**
TOTAL EQUITY AND LIABILITIES		**1,456,528**	**1,411,003**

Accompanying notes on pages 22 to 65 form an integral parts of these financial statements

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2016

(all amounts are expressed in thousands of HRK)	**Share capital**	**Legal reserves**	**Revaluation reserves**	**Reserves from the conversion of the exchange rate**	**Other reserves**	**Retained earnings**	**Total**	**Non-controlling interests**	**Total equity**
Balance st 1 January 2015	525,466	25,273	232,598	-	2,014	245,717	**1,031,068**	2,104	**1,033,172**
Profit/(loss) for the year	-	-	-	-	-	(161,314)	**(161,314)**	795	**(160,519)**
Other comprehensive income/(loss)	-	-	(14,231)	-	-	18,264	**4,033**	-	**4,033**
Total comprehensive income or loss	**-**	**-**	**(14,231)**	**-**	**-**	**(143,050)**	**(157,281)**	**795**	**(156,486)**
Increase in share capital	10,000	-	-	-	-	-	**10,000**	-	**10,000**
Reinvestment of profits	-	-	-	-	9,980	(9,980)	**-**	-	**-**
Transfer to legal reserves	-	1,500	-	-	-	(1,500)	**-**	-	**-**
Total transactions with owners of the Company, recognised directly in equity	**10,000**	**1,500**	**-**	**-**	**9,980**	**(11,480)**	**10,000**	**-**	**10,000**
Balance at 31 December 2015	**535,466**	**26,773**	**218,367**	**-**	**11,994**	**91,187**	**883,787**	**2,899**	**886,686**
Balance st 1 January 2016	535,466	26,773	218,367	-	11,994	91,187	**883,787**	2,899	**886,686**
Profit/(loss) for the year	-	-	-	-	-	27,984	**27,984**	1,070	**29,054**
Other comprehensive income/(loss)	-	-	(26,737)	2	-	35,997	**9,262**	-	**9,262**
Total comprehensive income or loss	**-**	**-**	**(26,737)**	**2**	**-**	**63,981**	**37,246**	**1,070**	**38,316**
Increase in share capital	-	-	-	-	-	-	**-**	-	**-**
Sales of a subsidiary	-	-	-	-	(196)	-	**(196)**	(456)	**(652)**
Transfer to legal reserves	-	-	-	-	-	-	**-**	-	**-**
Total transactions with owners of the Company, recognised directly in equity	**-**	**-**	**-**	**-**	**(196)**	**-**	**(196)**	**(456)**	**(652)**
Balance at 31 December 2016	**535,466**	**26,773**	**191,630**	**2**	**11,798**	**155,168**	**920,837**	**3,513**	**924,350**

Accompanying notes on pages 22 to 65 form an integral parts of these financial statements

BRODOGRAĐEVNA INDUSTRIJA SPLIT d.d.

CONSOLIDATED STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 31 DECEMBER 2016

	Note	2016	2015
Loss for the period		**29,054**	**(160,519)**
Adjustments for:			
- Depreciation		31,874	28,889
- Amortization		387	345
- Depreciation of investment property		192	188
- Loss on sale of subsidiary		736	-
- Impairment of non-current assets		438	522
- Impairment loss on investements		7	50
- Bad debts collected		(922)	(402)
- Impairment of receivables		4,873	5,272
- Release of provision for inventories		-	(1,840)
- Impairment of inventories		1,381	1,315
- Interest expense		22,360	21,523
- Interest income and discounting income		(10,065)	(9,860)
- Share in profits of joint venture		99	399
- FX difference		1,350	(921)
- Tax expense		(8,286)	(3,940)
- Net movements in provisions		(18,045)	(12,954)
		55,433	**(131,933)**
Changes in working capital			
- Change in inventories		33,078	(129,367)
- Change in trade and other receivables		(10,297)	160,139
- Change in trade and other payables		(104,411)	173,730
Cash generated from Operations		**(26,197)**	**72,569**
Interest paid		(15,941)	(14,150)
Income tax paid		(429)	(361)
Net cash generated from Operations		**(42,567)**	**58,058**
Cash flow from investing activities			
Acquisition of property, plant and equipment		(69,943)	(141,743)
Acquisition of intangible assets		(65)	(9)
Investment in joint venture		(2,499)	(5,219)
Proceeds from the sale of property, plant and equipment		327	-
Proceeds from other investments		201	-
Loans repaid		2,787	2,780
Net cash used in investing activities		**(69,192)**	**(144,191)**
Cash flow from financing activities			
Increase of share capital		-	10,000
Proceed from borrowings		319,839	186,960
Repayment of borrowings		(185,149)	(134,974)
Net cash used in financing activities		**134,690**	**61,986**
Net increase/(decrease) in cash and cash equivalents		22,931	(24,147)
Cash and cash equivalents at beginning of the year		18,273	42,420
Cash and cash equivalents at end of the year	*23*	**41,204**	**18,273**

Accompanying notes on pages 22 to 65 form an integral parts of these financial statements

NOTE 1 – GENERAL INFORMATION

Brodosplit Group (the „Group“) includes parent company BRODOGRAĐEVNA INDUSTRIJA SPLIT d.d., Split and 74 subsidiaries.

BRODOGRAĐEVNA INDUSTRIJA SPLIT d.d., Split (the „Company“) is registered with the Commercial Court in Split under Registration number (MBS): 060175040, PIN: 18556905592.

Share capital as at 31 December 2016 amounts to HRK 535,466,220. In accordance with the General Assembly's decision as of 3 March 2015 share capital was increased from HRK 525,466,140 for the amount of HRK 10,000,080 by cash contribution of shareholder DIV BRODOGRADNJA d.o.o., Samobor, Bobovica 10/A, MBS: 080812968, PIN: 44993645694, by issuance of 166,668 new shares as per series VII with exclusion of purchase rights of other shareholders. After the increase, share capital amounts to HRK 535,466,220.00 and is divided by 8,924,437 ordinary shares, nominal value of each being HRK 60.00.

The Company, through different organizational structures and under different names, operates since 1931. The core business of the Company is shipbuilding.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these financial statements are set out below.

2.1 Basis of preparation

These financial statements of the Group have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union ("IFRS as adopted by the EU").

Consolidated financial statements are presented for the Company and its subsidiaries. Unconsolidated financial statements of the Company, which are also prepared in accordance with IFRS, are issued separately.

The preparation of the financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires that the management exercise its judgment in the process of applying the Group's and the Company's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in note 'Key accounting estimates and judgments'.

2.2 Consolidation

(a) Subsidiaries

Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights and those with less then 50% of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. In accordance with IFRS 10, the Company reassessed the conditions for consolidation of the subsidiaries. There were no changes in comparisson to previous treatment.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.2 Consolidation (continued)

(a) Subsidiaries (continued)

Inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated on consolidation. Unrealised losses are also eliminated, unless there is evidence of impairment of transferred assets. Accounting policies of subsidiaries are changed where necessary to ensure consistency with the policies adopted by the Group.

(b) Joint ventures

The Group's interest in a jointly controlled entity is accounted for using the equity method of accounting and is initially recognised at cost. Under the equity method, the Group's share of post-acquisition profits or losses is recognised in the income statement, whereas its share of post-acquisition movements in other comprehensive income is recognised in other comprehensive income. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment.

2.3 Foreign currencies

(a) Functional and presentation currency

The consolidated financial statements are presented in Croatian kuna (HRK), which is the Group's functional and presentation currency.

(b) Transactions and balances in foreign currency

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.4 Property, plant and equipment

Property, plant and equipment comprises land, buildings, leasehold improvements, plant, transport vehicles, tools, books and art that are recognised in the balance sheet of the Group when the following conditions are fulfilled:

- the Group owns and uses the asset in its business process (core business);
- assets are expected to be used during more than one period;
- when it is probable that future economic benefits associated with the item will flow to the Group;
- the cost of the item can be measured reliably.

Property, plan and equipment is initialy recognised at cost which comprises the purchase price per supplier's invoice, import duties, non-refundable purchase taxes and all other costs directly attributable to bringing the asset to the condition necessary for its intended use.

Following initial recognition at cost, property, plant and equipment are carried at a revalued amount which is the fair value at the date of the revaluation less any subsequent accumulated depreciation on buildings and accumulated impairment losses.

Any impairment loss decreases revaluation reserve up to the amount of revaluation reserve of the specific asset.

Revaluations shall be made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period. If an asset's carrying amount is increased as a result of a revaluation, the increase shall be accumulated in equity under the heading of revaluation surplus and if the asset's carrying amount is decreased as a result of a revaluation, the decrease is recognized as an expense. The increase shall be recognised in profit or loss to the extent that it reverses a revaluation decrease of the same asset previously recognised as an expense in profit or loss. Revaluation decrease shall reduce the revaluation reserve to the extent of any credit balance existing in respect of that asset.

The carrying amount of an item of property, plant and equipment shall be derecognized on disposal or when no future economic benefits are expected from its use or disposal. The gain or loss arising from the derecognition of an item of property, plant and equipment shall be included in profit or loss as a difference between sale price and carrying value of the asset.

If some significant parts of property, plant and equipment require replacement at regular intervals, the Group recognizes such parts as a separate assets with specific useful life and depreciation. Furthermore, in the event of major repairs and maintenance, an entity recognises in the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if the recognition criteria are met. All other repair and maintenance costs are charged to profit or loss when incurred.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.4 Property, plat and equipment (continued)

Land and assets under construction are not depreciated. Depreciation of other assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

DESCRIPTION	2016	2015
	years	years
Buildings	20 – 100	20 – 100
Plant an machinery	10 – 33	10 – 33
Furniture, tools and other equipment	10 – 33	10 – 33
Ships	20	20

2.5 Intangible assets

Intangible assets relate to IT software initially recognized at purchased cost and amortised at straight line basis over its estimated useful life.

Following initial recognition at cost, intangible assets are carried at a revalued amount which is the fair value at the date of the revaluation less any subsequent accumulated depreciation and accumulated impairment losses. Any impairment loss decreases revaluation reserve up to the amount of revaluation reserve of the specific asset.

Revaluations shall be made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period. If an asset's carrying amount is increased as a result of a revaluation, the increase shall be accumulated in equity under the heading of revaluation surplus and if the asset's carrying amount is decreased as a result of a revaluation, the decrease is recognized as an expense. However, the increase shall be recognised in profit or loss to the extent that it reverses a revaluation decrease of the same asset previously recognised as an expense in profit or loss. Revaluation decrease shall reduce the revaluation reserve to the extent of any credit balance existing in respect of that asset.

Internally generated intangible assets, excluding capitalized costs of development, are not capitalized and are recognized as an expense in profit and loss as incurred. Useful life of an intangible asset is assessed as a finite or an indefinite.

Intangible assets with a finite useful life is amortised over the useful life of 10 years and is impaired if deemed necessary. Amortisation period and method of intangible assets with a finite useful life are reviewed at least at each reporting date.

Amortisation expense of an intangible assets with a finite useful life is recognized as an expense in profit or loss in accordance with an intended use of the asset. An intangible asset with an indefinite useful life is not amortised, but is annually tested for impairment either on an individual basis or on cash generating unit bases.

The useful life of an intangible asset shall be reviewed each period to determine whether events and circumstances continue to support an indefinite useful life assessment for that asset. If they do not, the change in the useful life assessment from indefinite to finite shall be accounted when possible.

NOTE 2 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.6 Investment property

Investment property mainly relates to flats that are held for long-term rental yields or appreciation. Investment property is treated as a long-term investment unless it is intended to be sold in the next year and a buyer has been identified, in which case it is classified within current assets.

Investment property is carried at revalued value less accumulated depreciation and provision for impairment, where required. Depreciation of buildings is calculated using the straight-line method to allocate cost over estimated useful life of 33 years.

Subsequent costs are capitalised only when it is probable that future economic benefits associated with it will flow to the Group and the cost can be measured reliably. All other repairs and maintenance costs are expensed when incurred. If an investment property becomes owner-occupied by one of the Group companies, it is reclassified to property, plant and equipment, and its carrying amount at the date of reclassification becomes its deemed cost to be subsequently depreciated.

2.7 Impairment of non-financial assets

Assets that have an indefinite useful life (such as land or goodwill) which are not subject to amortisation are tested annually for impairment. Assets that are subject to amortisation and depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

NOTE 2 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.8 Financial assets

The Group classify their financial assets in the following categories: at fair value through profit or loss, available-for-sale financial assets and loans and receivables. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

(a) Financial assets at fair value through profit or loss

Financial assets valued at fair value through profit or loss are financial assets held for trading. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term and are classified as current assets.

Financial assets valued at fair value through profit or loss are initially recognised at fair value with the transaction costs expensed in the income statement.

Gains or losses arising from changes in the fair value of the financial assets at fair value through profit or loss' category are presented in the income statement within the line item 'other (losses)/gains – net in the period in which they arise.

(b) Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date. Available-for-sale financial assets are carried at fair value and the transaction costs are recorded in the income statement.

Changes in the fair value of monetary securities and non-monetary securities classified as available-for-sale are recognised in other comprehensive income.

In the case of equity securities classified as available for sale, a significant or prolonged decline in the fair value of the security below its cost is considered as an indicator that the securities are impaired. If any such evidence exists for financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the income statement.

When securities classified as available-for-sale are sold or impaired, the accumulated fair value adjustments recognised in equity are included in the income statement in 'other operating expenses'.

Interest on available-for-sale securities calculated using the effective interest rate method is recognised in the income statement. Dividends on available-for-sale securities are recognised in the income statement when the right to receive payment is established.

The Group assess at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement.

NOTE 2 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.8 Financial assets (continued)

(c) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the balance sheet date which are classified as non-current assets. Loans and receivables are carried at amortised cost using the effective interest method.

Trade and loan receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy, and default or delinquency in payments are considered indicators that the receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate. The amount of the provision is recognised in the income statement within "other operating expenses". Subsequent recoveries of the provision for impairment of trade receivables are recorded in the income statement within "other operating income".

2.9 Government grants

Government grant is recognised when there is reasonable assurance that the entity will comply with the conditions attaching to it and that the grant will be received. Consequently, the Company does not recognise government grants until there is reasonable assurance that the Company will comply with the conditions attached to them and that the grants will be received. Once a government grant is recognised, any related contingent liability or contingent asset is treated in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets.

Government grants are recognised in profit or loss on a systematic basis over the periods necessary to match them with the related costs. A government grant that becomes recievable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the entity with no future related costs shall be recognised in profit or loss of the period in which it becomes receivable. Grants related to tangible assets are recognised in profit or loss over the periods and in the proportions in which depreciation on those assets is recognised. In the statement of financial position, government grant is recognised as deferred income that is recognised in profit or loss on a systematic basis over the useful life of the asset.

2.10 Leases

Assets under an operating lease where the Group is the lessor are depreciated over their expected useful lives on a basis consistent with similar owned assets. Rental income is recognised on a straight-line basis over the lease term, even if the proceeds are not balanced, unless there is an alternative basis representing the time frame in which the benefits of the lease and the depreciation of the leased property are matched.

NOTE 2 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.11 Inventories

Inventories of raw materials and spare parts are stated at the lower of cost or net realisable value. Cost is determined using the weighted average method. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

The cost of work-in-process and finished goods comprise raw materials, direct labor, other direct costs and related production overheads (based on normal operating capacity).

Small inventory and tools are expensed when put into use.

2.12 Construction contracts

Contract costs are recognised when incurred.

When the outcome of a construction contract cannot be estimated reliably, contract revenue is recognised only to the extent of contract costs incurred that are likely to be recoverable.

When the outcome of a construction contract can be estimated reliably and it is probable that the contract will be profitable, contract revenue is recognised over the period of the contract. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately.

The Group uses the percentage of completion method to determine the appropriate amount to recognise in a given period. The stage of completion is measured by reference to the contract costs incurred up to the balance sheet date as a percentage of total estimated costs for each contract. Costs incurred in the year in connection with future activity on a contract are excluded from contract costs in determining the stage of completion. Costs are presented as inventories, prepayments or other assets, depending on their nature.

For all contracts in progress for which the costs incurred plus recognised profits (less recognized losses) exceed progress billings, the Group presents the gross amounts due from customers as assets. Progress billings not yet paid by customers and retention are included within trade and other receivables.

For all contracts in progress for which progress billings exceed costs incurred plus recognised profits (less recognised losses), the Group presents the gross amount due to customers for contract work as a liability.

2.13 Cash and cash equivalents

Cash and cash equivalents comprise cash in hand, deposits held at call with banks and other short-term highly liquid instruments with original maturities of three months or less.

NOTE 2 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.14 Share capital

Ordinary shares are classified as share capital. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

2.15 Income tax

The tax expense for the year comprises current and deferred tax. Tax is recognised in the income statement, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case the tax is also recognised in other comprehensive income or directly in equity, respectively.

The current tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the Group operate and generate taxable income. The tax base represents the difference between income and expenses, as determined by the applicable law. Management of the Group periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulations are subject to interpretation and consider establishing provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

2.16 Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates/laws that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference is controlled by the Company and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are offset when there is legally enforceable right to offset current tax assets against current tax liabilities and when deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

NOTE 2 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.17 Trade and other payables

Trade and other payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

2.18 Employee benefits

(a) Pension obligations and post-employment benefits

In the normal course of business through salary deductions, the Group makes payments to mandatory pension funds on behalf of its employees as required by law. All contributions made to the mandatory pension funds are recorded as salary expense when incurred.

(b) Termination benefits

Termination benefits are payable when employment is terminated by the Group before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Group recognises termination benefits when it is demonstrably committed to either terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal, or providing termination benefits as a result of an offer made to encourage voluntary redundancy. Benefits falling due more than 12 months after the balance sheet date are discounted to their present value.

2.19 Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount can be reliably estimated.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

NOTE 2 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.20 Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sale of goods and services in the ordinary course of the Group's activities. Revenue is shown net of value-added tax, estimated returns, rebates and discounts. The Group recognise revenue when the amount of revenue can be reliably measured, it is probable that future economic benefits will flow to the entity and specific criteria have been met for each of the Group's activities as described below.

(a) Services

Revenue from services are recognised in profit or loss based on percentage of completion in relation to reporting date. Percentage of completion is determined based on review of work done.

(b) Revenue from construction contracts

Revenue from construction contracts consists of initially agreed amount increased by variations from contracted work, complaints and other incentives when it is probable that the contract will be profitable and the profits will be measurable. When the outcome of a construction contract can be estimated reliably, contract revenue and expenses related to construction contract are recognised as revenue and expenses based on percentage of completion.

Percentage of completion is valued based on overview of work done by the reporting date. When the outcome of a construction contract cannot be estimated reliably, contract revenue is recognised only to the extent of contract costs incurred that are likely to be recoverable. Expected loss from construction contract is recognised in profit or loss imidiately.

(c) Sales of goods

Revenues from the sale of goods are recognised when the Group has delivered products to the customer, the customer has accepted the products and collectability of the related receivables is reasonably assured.

(d) Interest income

Interest income is recognised on a time-proportion basis using the effective interest method. When a receivable is impaired, the Group reduce the carrying amount to its recoverable amount, being the estimated future cash flow discounted at original effective interest rate of the instrument, and continues unwinding the discount as interest income. Interest income on impaired loans is recognised using the original effective interest rate.

(e) Dividend income

Dividend income is recognised when the right to receive payment is established.

NOTE 2 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.21 Dividend distributions

Dividend distributions to the Company's shareholders are recognised as a liability in the financial statements in the period in which the dividends are approved by the General Assembly of the Company's shareholders.

2.22 Value added tax

The Tax Authorities require the settlement of VAT on a net basis. VAT related to sales and purchases is recognised and disclosed in the balance sheet on a net basis. Where a provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

2.23 Maritime domain and concession

In accordance with the Resolution to change the "Resolution on concession of maritime domain" issued on 5 July 2007 and the Resolution issued on 2 August 2007, Brodograđevna industrija Split d.d. and its subsidiaries use land (580,589 m²) and sea (222,319 m²) under concession for the Company's commercial use. The concession was given by the Republic of Croatia for a period of 32 years, starting as of 19 April 2000.

Issues regarding the maritime domain and concessions are regulated by Maritime Law, Law on Maritime Domain and Seaports, as well as the Croatian Government resolution on concession of maritime domain for the purpose of commercial exploitation of special purpose ports and the agreement between the concession grantor and the authorised concessioner regarding maritime concessions. There is a certain amount of uncertainty for Brodograđevna industrija Split Group regarding ownership and the treatment of maritime domain (the territory which boarders with the sea) which is currently owned by the Croatian government. Buildings located on the land represent maritime domain as well.

The general maritime domain concession agreement for the purpose of commercial exploitation of special purpose ports was concluded on 19 April 2000 (and subsequently updated on 2 August 2007 and 6 August 2007, Official Gazette No. 72/07 and 81/07) with the concession grantor, the Croatian government, and contains the following elements:

Subject of the agreement

The concession grantor authorises the authorised concessioner the right to commercially use the maritime domain, the special purpose port, with a land surface in the amount of 563,549 m² and 222,319 m² of water surface, amounting to a total amount of 785,868 m² of maritime domain surfaces.

Right to use

The concession grants the right to commercially use the special purpose port – shipyard Split, located in the Splitsko-dalmatinska county along with adjacent buildings.

Concession service time

The concession is granted on a period of 32 years commencing on the agreement date.

NOTE 2 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.23 Maritime domain and concession (continued)

Concession payment

The authorised concessioner must pay the concession grantor an annual fee which consist of two portions:

a) a fixed portion in the amount of HRK 0.50 per square meter of land used per annum;

b) a variable portion in the amount of 1% of the annual profits of the company, after tax.

The concession fee portions are paid as described below:

a) the fixed portion – in the first and last year the payments made are relative to the months the concession was used. For all other years, it is payable no later than 1 April for the current year;

b) the variable portion must be paid by 30 April for the previous year.

If the authorised concessioner forfeits the concession before the service time expires a fee in the amount of three years' worth of the fixed portion of the fee must be paid out to the concession granter.

Concession untransferability

The authorised concessioner cannot transfer the concession rights, or part of said rights, to a third legal or physical entity without prior approval from the concession grantor.

The concession for the use of maritime domain is calculated based on the conditions stated in the concluded agreements, beginning with the year 2000, and is charged to the operating expenses of the reporting periods.

Changes to the maritime domain concession agreement

On 11 February 2011 the Company and the concession grantor, the Croatian Government, have signed addition #1 of the maritime concession agreement for the commercial use of the special purpose port- shipyard Split, by which the following changes were made:

Concession payment

The authorised concessioner must pay the concession grantor an annual fee which consist of two portions:

a) a fixed portion in the amount of HRK 3.00 per square meter of land used per annum;

b) a variable portion in the amount of 1% of the annual profits of the company

The concession fee portions are paid as described below:

a) The fixed portion of the fee for the current year is paid no later than 45 days of signing the addition to the concession agreement. The fixed portion for subsequent years is paid in advance, no later than 15 April for the following year.

b) The variable portion of the fee is paid for previous periods and in two instalments: no later than 30 September for the first half of the current year, till 30 April for the second half of the previous year.

NOTE 3 – FINANCIAL RISK MANAGEMENT

3.1 Financial risk factors

The Group’s operations are exposed to the following risks:

- Credit risk
- Cash flow fair value or interest rate risk
- Foreign exchange risk
- Market risk
- Liquidity risk
- Regulatory risk

Capital risk management

The Company manages its capital by ensuring the continuity of its business with maximising the return on investment for its shareholders though optimising debt and capital.

The Capital structure of the Company consists of debt which includes loans and borrowings, cash and cash equivalents and equity. Equity includes share capital and losses carried forward.

Financial risk management

Group is, in the most part, exposed to the international market. Respectively, the Group is influenced by price changes on the world market of the main raw materials, which are dependent on exchange rate fluctuations. In accordance with the aforementioned, the Company is substantially exposed to exchange rate changes.

Financial risks include market risk (including currency risk and pricing risk), credit risk, liquidity risk and interest cash flow risk.

Credit risk

Credit risk refers to the risk of a contracting party not paying the commitment and thus causing a financial loss to the Group. The Group has adopted the policy in which it conducts business exclusively with creditworthy contracting parties, ensuring collateral as a means to minimize the risk of financial loss due to the unfulfillment of contract agreements. The Group' exposure and credit position of contracting parties is constantly monitored and the total amount of completed transactions is distributed between approved contracting parties.

The contracting of a ship with unknown buyers or buyers who, in the view of the Group, are not creditworthy is conditioned with the issue of a so called „Payment guarantee“ from a first grade bank. Group’s policy is that significant advance payments are made to suppliers only after the issue of advance payments guarantees.

Trade receivables are accounted by a small number of buyers who are located in different geographical locations. The continuous valuation of receivables is carried out based on the financial position of the buyer and, when necessary, receivables guarantee is acquired or another financial instrument which ensures payment.

The credit risk of liquidity assets and derivative financial instruments is limited duo to the fact that the contracting parties are represented by banks with high credit ratings defined by international credit risk determining agencies.

NOTE 3 – FINANCIAL RISK MANAGEMENT (continued)

3.1 Financial risk factors (continued)

Interest risk

Most of the interest bearing loans are contracted with a fixed, as well as fluctuating interest rate. Risk is managed by maintaining an appropriate combination between the fixed and variable interest rate on borrowings. The company is currently not protected against such risks.

Currency risk

Due to the currency structure of assets and their sources as well as the currency structure of future economic flows, the Group is exposed to a substantial risk of exchange rate fluctuations. In order to reduce this risk the Group is attempting to establish a balance between currency inflows and outflows. Additionally, sales conducted in recent years are agreed in a mixture of currencies (USD and EUR), this reduces the exchange rate loss and expenses when converting currencies in order to pay liabilities as most of the foreign expenses are in EUR. Group continuously follows the exchange rates and the currency structure of any planed outflows and arranges the currency credit funds accordingly.

Group is exposed to a currency risk by contract prices for raw materials agreed in foreign currencies. The currencies most exposed to this risk are EUR and USD. The company is currently not protected against such risk.

Group plans to implement more active and better policies for eliminating currency risk. The Group's plan is to use financial instruments (forward transactions, FX options, etc.) which are available today on both the domestic and foreign financial markets. The cost of such financial instruments would be included in the total costs of the ship.

The following table shows the Group's accounting amounts of monetary assets and liabilities in foreign currency on the reporting date.

(in thousands of HRK)	**Liabilities**		**Assets**	
	2016	**2015**	**2016**	**2015**
EUR	239,831	45,244	88,497	81,325
USD	1,534	744	5,527	3,230
GBP	295	730	442	363
SEK	38	48	-	16
Other	226	173	-	52

As at 31 December 2016, if the EUR would increase/decrease in value for 1.00% relative to the HRK, under the assumption that all other variables remain constant, the loss for the reporting date would be HRK 1531 thousand smaller/(larger). This change would be a direct result of positive/(negative) exchange rate changes to the trade receivables, trade payables, borrowings and money deposits in EUR.

According to the management, changes in the value of other currencies does not have a significant effect on the financial reports of the Group.

NOTE 3 – FINANCIAL RISK MANAGEMENT (continued)

3.1 Financial risk factors (continued)

Market risk

The company is exposed to a substantial rise in the prices of ferrous metallurgy as well as the prices of other raw materials. The Group has, for the most part, neutralized this risk by arranging a so called “safeguard clause for the ferrous metallurgy” which states that the income per ship delivered is increased by the amount of expenses incurred due to the rise of ferrous metallurgy between the delivery and the time the ship was ordered.

Liquidity risk

Group manages liquidity risk by maintaining appropriate reserves, bank and borrowed funds reserves as well as continuous monitoring of the expected and actual cash flows and comparing the maturity dates of financial assets and liabilities.

The time mismatch of financial inflows and outflows is bridged by using credit funds and “borrowing” funds from other projects in order to minimize financial expenses related to the construction of individual projects.

The tables below show the contractual maturities of financial liabilities and financial assets reported in the consolidated statement of financial position at the end of each reporting period. Tables below have been prepared based on undiscounted cash flows to maturity and include both interest and principal.

Liabilities

as at 31 December 2016	Carrying amount	Contractual cash flows	Less than 1 year	1-2 years	2-5 years	Over 5 years
			(in thousands of HRK)			
Non-interest bearing liabilities						
Other payables	110,010	110,010	110,010	-	-	-
Payables to related parties	11,000	11,000	11,000	-		
Trade payables	150,141	150,141	136,915	13,226	-	-
	271,151	**271,151**	**257,925**	**13,226**	**-**	**-**
Interest bearing liabilities						
Factoring	2,156	4,647	4,647	-	-	-
Borrowings	177,608	190,776	37,711	153,065	-	-
	179,764	**195,423**	**42,358**	**153,065**	**-**	**-**
	450,915	**466,574**	**300,283**	**166,291**	**-**	**-**

NOTE 3 – FINANCIAL RISK MANAGEMENT (continued)

3.1 Financial risk factors (continued)

Liquidity risk (continued)

as at 31 December 2015	Carrying amount	Contractual cash flows	Less than 1 year	1-2 years	2-5 years	Over 5 years
			(in thousands of HRK)			
Non-interest bearing liabilities						
Other payables	222,140	222,140	222,140	-	-	-
Trade payables	144,475	144,475	144,475	-	-	-
	366,615	**366,615**	**366,615**	**-**	**-**	**-**
Interest bearing liabilities						
Borrowings	51,918	53,473	53,473	-	-	-
	51,918	**53,473**	**53,473**	**-**	**-**	**-**
	418,533	**420,088**	**420,088**	**-**	**-**	**-**

Assets

as at 31 December 2016	Carrying amount	Contractual cash flows	Less than 1 year	1-2 years	2-5 years	Over 5 years
			(in thousands of HRK)			
Non-interest earning assets						
Other receivables	298,023	298,023	298,023	-	-	-
Trade receivables	108,707	108,707	92,417	5,845	8,767	1,678
	406,730	**406,730**	**390,440**	**5,845**	**8,767**	**1,678**
Interest earning interest						
Loans given and deposits	39,414	39,533	19,389	11	20,133	-
Cash and cash equivalents	41,204	41,204	41,204	-	-	-
	80,618	**80,737**	**60,593**	**11**	**20,133**	**-**
	487,348	**487,467**	**451,033**	**5,856**	**28,900**	**1,678**

as at 31 December 2015	Carrying amount	Contractual cash flows	Less than 1 year	1-2 years	2-5 years	Over 5 years
			(in thousands of HRK)			
Non-interest earning assets						
Other receivables	282,336	282,336	186,008	86,958	8,314	1,056
Trade receivables	72,497	72,497	72,497	-	-	-
	354,833	**354,833**	**258,505**	**86,958**	**8,314**	**1,056**
Interest earning interest						
Loans given and deposits	82,769	85,841	65,461	-	20,380	-
Cash and cash equivalents	18,272	18,417	18,417	-	-	-
	101,041	**104,258**	**83,878**	**-**	**20,380**	**-**
	455,874	**459,091**	**342,383**	**86,958**	**28,694**	**1,056**

NOTE 3 – FINANCIAL RISK MANAGEMENT (continued)

3.1 Financial risk factors (continued)

Regulatory risk

Taking into account the joining of Republic of Croatia to the European Union, the Company is significantly exposed to regulatory risk that is mostly related to changes in the areas of government grants regulations. Since the Company utilised significant government grants to maintain the profitability and liquidity, this risk is considered significant and uncontrollable.

3.2 Capital management

The Company aims to manage capital in such a way as to maintain the going concern and be able to provide a return on investment to its shareholders and benefits to all other interested parties. The company aims to maintain the optimal capital structure in order to reduce the cost of capital.

In order to maintain or harmonise the capital structure, the Company can change the dividend amount which is paid out to shareholders, provide a return on investment to its shareholders, issue new stocks or sell assets in order to reduce debt.

The Company controls capital through supervision of debt. This indicator is calculated as the net debt divided by the total capital. Net debt (borrowings) are calculated as the total loans received (non-current and current as shown in the trial balance) reduced by the amount of cash and cash equivalents as well as current deposits. The total capital is calculated by adding the net amount of borrowings to capital and reserves.

The relation between net borrowings and capital (Gearing ratio) on the reporting date was as follows:

(in thousands of HRK)	**2016**	**2015**
Debt (long-term and short-term loans)	(188,608)	(51,918)
Cash and cash equivalents	41,204	18,273
Net debt	(147,404)	(33,645)
Equity	(920,837)	(886,686)
Debt to equity ratio	16%	4%

NOTE 3 – FINANCIAL RISK MANAGEMENT (continued)

3.3 Fair value estimation

IFRS 7 states that fair value evaluations must be presented in levels under the following hierarchy:

Quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1).

Inputs which do not represent quoted prices included in level 1 but represent observable inputs for assets or liabilities, be it directly (as a price) or indirectly (derived from price) (level 2).

Inputs for assets or liabilities that are not based on observable market data (invisible inputs) (level 3).

The following table shows Group assets per fair value level at 31 December 2016 and 31 December 2015:

(in thousands of HRK)	Level 1	Level 2	Level 3	Total
As at 31 December 2015				
Property, plant and equipment	-	-	651,039	651,039
Intangible assets	-	-	1,465	1,465
Investment property	-	-	5,381	5,381
Financial assets available for sale	-	-	-	-
Listed companies	205	-	-	205
Unlisted companies	-	138	-	138
Total	**205**	**138**	**657,885**	**658,228**

(in thousands of HRK)	Level 1	Level 2	Level 3	Total
As at 31 December 2016				
Property, plant and equipment	-	-	682,013	682,013
Intangible assets	-	-	13,969	13,969
Investment property	-	-	4,472	4,472
Financial assets available for sale	-	-	-	-
Listed companies	211	-	-	211
Unlisted companies	-	132	-	132
Total	**211**	**132**	**700,454**	**700,797**

NOTE 4 – KEY ACCOUNTING ESTIMATES AND JUDGMENTS

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, rarely equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are outlined below.

(a) Revenue recognition

The Group uses the percentage-of-completion method in accounting for its revenue from construction contracts to determine the appropriate amount to recognise in a given period. The stage of completion is measured by reference to the contract costs incurred up to the balance sheet date as a percentage of total estimated costs for each contract.

(b) Impairment of loans and receivables

The Group reviews the portfolio of loans and receivables on an annual basis to assess impairment. While assessing the recognition of impairment in the statement of comprehensive income, the Group assesses whether there is observable data indicating the existence of a measurable decrease in future cash flows of the portfolio of loans and receivables before establishing the impairment of certain loans and receivables in the stated portfolio.

(c) Work in progress and revenue

The revenues and costs reflected in the financial statements are based on the Company’s engineering and financial best estimates of the stage of contract completion and profit to be realised upon completion. Construction work in progress is based on estimates of expected future costs and profit. As the project progresses, these estimates may change significantly should unexpected costs or unforeseen project difficulties occur.

d) Useful life of property, plant and equipment

The Company managements determine and reassess the useful lives and related depreciation charge for tangible assets. This assessment is based on the estimated remaining useful life of assets and could significantly change as a result of technical innovation and activities of competitors. Management will increase the depreciation charge if it assesses that the useful life of assets is lower than prior to estimates, or it will write off obsolete and discarded property.

(e) Revaluation

Valuation of property, plant and equipment, intangible assets and investment property was conducted on 31 December 2016 by an independent appraiser. The estimate was made on the basis of market value and determining the cost of the assets replacement. Revaluation surplus decreased by relating deferred tax liability is recognized as revaluation reserve within equity.

(f) Legal claims and disputes

Provisions for legal claims and disputes are recorded based on Management's best estimate of probable losses after consultation with legal counsel.

(g) Warranties

The Group recognizes provision for warranties for all products under warranty at the reporting date. The provision is based on historical warranty data relating to defective products.

(h) Loss making contracts

The Group recognizes provision for onerous contracts when the expected benefits of the contract are lower than unavoidable expenses of fulfillment of the contracted obligations.

NOTE 4 – KEY ACCOUNTING ESTIMATES AND JUDGMENTS (continued)

(i) Government grants

Government grants are recognised when there is reasonable assurance that the Company will comply with the conditions attaching to them; and the grants will be received. Receipt of a grant does not of itself provide conclusive evidence that the conditions attaching to the grant have been or will be fulfilled. Income arising on grants for restructuring that are received based on the Restructuring programe depends on conditions defined in Contract on sale and transfer of shares. The Management Board believes that the defined conditions will be fulfilled and thus income from government grants for restructuring in prior periods.

NOTE 5 – REVENUE

(in thousands of HRK)	**2016**	**2015**
Revenue from shipbuilding	237,044	106,244
Revenue from off shore and steel construction	272,393	163,965
Revenue from services	15,336	76,345
Other revenue	28,054	25,738
	552,827	**372,292**

Revenue from shipbuilding are calculated in accordance with IAS 11 – *Construction contracts*, where percentage of completion is calculated using cost model, by comparing total actual costs during the period and budgeted cost for each construction. Transactions with related parties are disclosed in note 'Related party transactions'.

NOTE 6 – OTHER OPERATING INCOME

(in thousands of HRK)	**2016**	**2015**
Income from arbitration	46,156	-
Income from additional rebates from suppliers	1,934	589
Income from charged penalties	1,699	-
Income from collection of receivables	922	207
Inventory surpluses	2,096	2,149
Release of provision for inventories	-	1,840
Income from liability write-off	-	1,271
Release of waranty provision	3,138	-
Release of provision for court cases	14,248	-
Release of other provisions	4,730	9,270
Other	2,336	2,169
	77,259	**17,495**

NOTE 7 - MATERIAL EXPENSES

(in thousands of HRK)	**2016**	**2015**
Raw materials	237,880	204,471
Energy	10,691	8,558
Small inventory, spare parts and tires	2,744	2,857
Material expenses	**251,315**	**215,886**
External cooperation and other production services	13,276	35,007
Management fees	13,347	13,360
Security services	1,140	1,372
Repairs and maintenance	2,082	3,199
Transport	445	1,950
Other external expenses	16,888	14,458
Cost of services	**47,178**	**69,346**
Total material expenses	**298,493**	**285,232**

The cost of external cooperation and other production services relate to services by external and internal cooperation provided since the initial phase of development to the launching of the ship. The above mentioned services include drafting of the project, anticorrosion protection, carpentry work, galvanizing and other similar services.

NOTE 8 – EMPLOYEE COSTS

(in thousands of HRK)	**2016**	**2015**
Net salaries	139,596	148,975
Taxes and contributions from salaries	48,591	51,072
Contributions on salaries	36,198	38,862
	224,385	**238,909**

Taxes and contribution from salaries include contributions paid into obligatory pension funds amounting to HRK 40,177 thousand (2015: HRK 39,998 thousand) Contributions are calculated as a percentage of gross salaries.

As at 31 December 2016 the Group had 2,044 employees (31 December 2015: 2,235 employees).

NOTE 9 – DEPRECIATION AND AMORTISATION

(in thousands of HRK)	2016	2015
Property, plant and equipment	31,874	28,888
Intangible assets	387	345
Investment property	192	188
	32,453	**29,421**

NOTE 10 – OTHER OPERATING EXPENSES

(in thousands of HRK)	2016	2015
Impairment of work in progress	24,407	35,034
Other employee related costs	20,339	21,223
Warranty provision	-	9,912
Loss on termination of contract	-	6,432
Concession expense	6,964	6,585
Severance payments	6,236	5,055
Impairment of trade receivables	4,873	5,272
Insurance costs	2,394	5,776
Bank fees and charges	3,519	4,400
Business trips	3,553	4,229
Damages	2,006	-
Fines and penalties	1,958	2,265
Intelectual services	10,500	3,258
Impairment of inventories	1,381	1,315
Utilities	1,989	1,989
Entertainment	944	829
Impairment of invenstment in subsidiaries	736	-
Impairment of property, plant and equipment	438	238
Impairment of other financial assets available for sale	7	159
Provision for court cases	1,605	3,431
Intelectual services	5,626	2,531
Other	5,938	11,324
	105,413	**131,257**

NOTE 11 – FINANCE INCOME

(in thousands of HRK)	**2016**	**2015**
Interest income	4,840	1,641
Foreign exchange gains	7,965	5,002
Other finance income	3	-
Income from unwinding of discount	5,225	11,501
	18,033	**18,144**

NOTE 12 – FINANCE COSTS

(in thousands of HRK)	**2016**	**2015**
Interest expense	22,360	21,523
Foreign exchange losses	4,726	4,296
	27,086	**25,819**

NOTE 13 – INCOME TAX

Income tax expense/(benefit) consists of:

(in thousands of HRK)	**2016**	**2015**
Current income tax	713	626
Deferred income tax	(8,999)	(4,566)
Income tax expense/(benefit)	**(8,286)**	**(3,940)**

(in thousands of HRK)	**2016**	**2015**
Profit/(loss) before tax	**20,768**	**(164,459)**
Income tax at tax rate of 20%	4,154	(32,892)
Effect of non-deductable expenses	184	169
Effect of non-taxable income	(1)	-
Effects of other tax incentives	(119)	(5)
Temporary differences (not recognized as deferred tax asset)/utilised	8,344	3,232
Tax losses not recignised as deferred tax asset	1,342	26,432
Tax losses utilized not previously recognised as deferred tax asset	(22,190)	(876)
Income tax expense/(benefit)	**(8,286)**	**(3,940)**

NOTE 13 – INCOME TAX (continued)

Tax losses

Deferred tax assets according to tax-adjusted losses carried forward is as follows:

(in thousands of HRK)	**2016**	**2015**
Tax loss from year 2011 - expires 31 December 2016	-	5,442
Tax loss from year 2012 - expires 31 December 2017	6,641	6,784
Tax loss from year 2013 - expires 31 December 2018	17,116	20,456
Tax loss from year 2014 - expires 31 December 2019	18,398	33,702
Tax loss from year 2015 - expires 31 December 2020	23,915	26,493
Tax loss from year 2016 - expires 31 December 2021	6,633	-
	72,703	**92,877**

Due to historical uncertainties regarding taxable profit and the amount of future taxable profit, the Group has not recognized deferred tax assets.

Unrecognised deferred tax assets related to temporary differences amounted to HRK 14,107 thousand (2015: HRK 23,688 thousand). Temporary differences mainly relate to adjustments to inventories and provisions.

In accordance with the regulations of the Republic of Croatia, the Tax Authority may at any time inspect the Company's books and records within 3 years following the year in which the tax liability is reported, and may impose additional tax liabilities and penalties.

At the beginning of 2017, a new income tax act came in the effect in the Republic of Croatia, reducing the income tax rate from 20% to 18% as of January 2017. In accordance with International Accounting Standards, Company recognised deferred tax asset as at 31 December 2016 at the tax rate of 18%, i.e. the rate at which the asset will be realised in the future.

Deferred tax liability

During the year, the Group recognized deferred tax liability on revaluation of the assets. Movement in deferred tax liability is shown in the following table.

Due to changes of tax rate, Company recognised deferred tax asset as at 31 December 2016 at the tax rate of 18%, i.e. the rate at which the asset will be realised in the future.

NOTE 13 – INCOME TAX (continued)

Movement in deferred tax liability

(in thousands of HRK)	1 January 2016	Recognised in other comprehensive income	Recognised in profit or loss	Effect of tax rate change	31 December 2016
Property, plant and equipment	52,926	1,154	(66)	(13,240)	40,774
Intangible assets	201	15	(8,895)	8,815	136
Investment property	1,050	(129)	(38)	(89)	794
	54,177	**1,040**	**(8,999)**	**(4,514)**	**41,704**

NOTE 14 – INTANGIBLE ASSETS

(in thousands of HRK)	Software	Assets under construction	Total
Cost or valuation			
As at 1 January 2015	**1,976**	**285**	**2,261**
Additions	9	-	9
Impairment	-	(285)	(285)
Revaluation	109	-	109
As at 31 December 2015	**2,094**	**-**	**2,094**
As at 1 January 2016	**2,094**	**-**	**2,094**
Transfer from tangible assets	65	-	65
Transfer from tangible assets	-	12,750	12,750
Impairment	(1)	-	(1)
Revaluation	77	-	77
As at 31 December 2016	**2,235**	**12,750**	**14,985**
Accumulated amortization			
As at 1 January 2015	**284**	**-**	**284**
Charge for the year	345	-	**345**
As at 31 December 2015	**629**	**-**	**629**
As at 1 January 2016	**629**	**-**	**629**
Charge for the year	387	-	**387**
As at 31 December 2016	**1,016**	**-**	**1,016**
Carrying amount			
As at 1 January 2016	**1,465**	**-**	**1,465**
As at 31 December 2016	**1,219**	**12,750**	**13,969**

Intangible assets under construction relates to software

NOTE 15 – PROPERTY, PLANT AND EQUIPMENT

(in thousands of HRK)	Land	Buildings	Leasehold improvement	Plant and equipment	Tools and vehicles	Ships	Other equipment	Assets under construction	Total
Cost or valuation									
As at 1 January 2015	**264**	**19,936**	**110,892**	**212,869**	**214,711**	**-**	**350**	**15,938**	**574,960**
Additions	-	-	-	250	304	-	-	141,189	**141,743**
Transfers	-	-	-	1,190	5,670	-	-	(6,860)	**-**
Impairment	(14)	(5)	(7)	(46)	(157)	-	(8)	-	**(237)**
Revaluation	-	(172)	(41)	4,203	700	-	-	-	**4,690**
As at 31 December 2015	**250**	**19,759**	**110,844**	**218,466**	**221,228**	**-**	**342**	**150,267**	**721,156**
As at 1 January 2016	**250**	**19,759**	**110,844**	**218,466**	**221,228**	**-**	**342**	**150,267**	**721,156**
Additions	-	-	-	-	-	-	-	69,943	**69,943**
Transfers	-	-	5,384	2,727	2,016	108,148	-	(118,275)	**-**
Transfers to intangibles	-	-	-	-	-	-	-	(12,750)	**(12,750)**
Sales	-	-	-	(329)	-	-	-	-	**(329)**
Impairment	(2)	-	(3)	(84)	(345)	-	(3)	-	**(437)**
Revaluation	-	(167)	142	3,028	3,416	-	-	-	**6,419**
As at 31 December 2016	**248**	**19,592**	**116,367**	**223,808**	**226,315**	**108,148**	**339**	**89,185**	**784,002**
Accumulated depreciation									
As at 1 January 2015	-	263	4,419	22,277	14,269	-	-	-	41,228
Charge for the year	-	278	1,277	13,436	13,898	-	-	-	**28,889**
As at 31 December 2015	**-**	**541**	**5,696**	**35,713**	**28,167**	**-**	**-**	**-**	**70,117**
As at 1 January 2016	-	541	5,696	35,713	28,167	-	-	-	70,117
Charge for the year	-	276	1,337	14,104	14,288	1,869	-	-	**31,874**
Sales	-	-	-	(2)	-	-	-	-	**(2)**
As at 31 December 2016	**-**	**817**	**7,033**	**49,815**	**42,455**	**1,869**	**-**	**-**	**101,989**
Carrying amount									
As at 1 January 2016	**250**	**19,218**	**105,148**	**182,753**	**193,061**	**-**	**342**	**150,267**	**651,039**
As at 31 December 2016	**248**	**18,775**	**109,334**	**173,993**	**183,860**	**106,279**	**339**	**89,185**	**682,013**

NOTE 15 – PROPERTY, PLANT AND EQUIPMENT (continued)

Property, plant and equipment in the amount of HRK 263,324 thousand (2015: HRK 99,609 thousand) are pledged as security against bank loan (note "Loans and borrowings"). Property, plant and equipment in the amount of HRK 263,324 thousand (2015: HRK 99,609 thousand) are pledged as security based on being a co-debtor for the parent company's loan. Asset under construction relate to their own fleet.

NOTE 16 – INVESTMENT PROPERTY

(in thousands of HRK)	**Investment property**
Cost or valuation	
As at 1 January 2015	**5,645**
Revaluation	106
As at 31 December 2015	**5,751**
As at 1 January 2016	**5,751**
Revaluation	(717)
As at 31 December 2016	**5,034**
Accumulated amortization	
As at 1 January 2015	**182**
Charge for the year	188
As at 31 December 2015	**370**
As at 1 January 2016	**370**
Charge for the year	192
As at 31 December 2016	**562**
Carrying amount	
As at 1 January 2016	**5,381**
As at 31 December 2016	**4,472**

NOTE 17 – NON-CURRENT INVESTMENTS

(in thousands of HRK)	**31 December 2016**	**31 December 2015**
Financial assets available for sale	343	343
	343	**393**

Movement in non-current investments is shown in table below:

(in thousands of HRK)	**Financial assets available for sale**
Balance at 1 January 2016	343
Increase	7
Change in fair value	-
Impairment	(7)
Balance at 31 December 2016	**343**

The value adjustment of investments made in subsidiaries was recognised in profit or loss, while the fair value adjustment of financial assets available for sale was recognised within income statement and other comprehensive income.

NOTE 17 – NON-CURRENT INVESTMENTS (continued)

List of investments in subsidiaries that are managed by the Company is as follows:

Name of subsidiary	Share in % 2016	Business Activity
Brodosplit - Plovidba d.o.o.	100	Sea and coastal water transport of freight
Brodosplit - Brodogradilište specijalnih objekata d.o	100	Building of ships and floating structures
Brodosplit - Metalna oprema i konstrukcije d.o.o.	100	Manufacture of metal structures and parts of structures
Brodosplit - Dizalice d.o.o.	100	Manufacture of lifting and handling equipment
Brodosplit - Nemetalna oprema d.o.o.	100	Manufacture of other builders' carpentry and joinery
Brodosplit - Armature d.o.o.	100	Manufacture of metal structures and parts of structures
Brodosplit - Tvornica dizel motora d.o.o.	100	Manufacture of engines and turbines, except aircraft, vehicle and cycle engines
Brodosplit - Antikorozivna zaštita d.o.o.	100	Treatment and coating of metals
Brodosplit - Izolacija d.o.o.	100	Other construction installation
Brodosplit - Trgovina d.o.o.	100	Wholesale of other machinery and equipment
Brodosplit - Zaštita brodskog trupa od korozije d.o.	100	Manufacture of metal structures and parts of structures
Brodosplit - Transportna sredstva d.o.o.	100	Renting and leasing of other machinery, equipment and tangible goods
Brodosplit - Čelik d.o.o.	100	Manufacture of metal structures and parts of structures
Brodosplit - Opremanje plovnih objekata d.o.o.	100	Manufacture of metal structures and parts of structures
Brodosplit - Trup d.o.o.	100	Manufacture of metal structures and parts of structures
Brodosplit - Stroj d.o.o.	100	General mechanical engineering
Brodosplit - Montaža d.o.o.	100	Manufacture of metal structures and parts of structures
Brodosplit - Boja d.o.o.	100	Repair and maintenance of ships and boats
Brodosplit - Holding d.o.o.	100	Building of ships and floating structures
Brodosplit - Blok d.o.o.	100	Building of ships and floating structures
Brodosplit - Računovodstvo i financije d.o.o.	30	Accounting, book-keeping and auditing activities; tax consultancy
Brodosplit - Informatika d.o.o.	30	Computer facilities management activities
Brodosplit - Laboratorij d.o.o.	30	Technical testing and analysis
Brodosplit - Atest d.o.o.	30	Security systems service activities
Brodosplit - Ljudski resursi d.o.o.	30	Other human resources provision
Brodosplit - Plovne dizalice d.o.o.	30	Renting and leasing of water transport equipment
Brodosplit - Privremena energetika d.o.o.	30	Production of electricity
Brodosplit - Čišćenje d.o.o.	30	Other cleaning activities
Brodosplit - Optimizacija i ekologija d.o.o.	30	Remediation activities and other waste management services
Brodosplit - Alatnica d.o.o.	30	General mechanical engineering
Brodosplit - Održavanje d.o.o.	30	Repair of machinery
Brodosplit - Skela d.o.o.	30	Manufacture of metal structures and parts of structures
Brodosplit - Cjevarska izrada d.o.o.	30	Casting of iron
Brodosplit - Bravarija i limarija d.o.o.	30	Repair of fabricated metal products
Brodosplit - Automatizacija d.o.o.	30	Computer facilities management activities
Brodosplit - Snaga energije d.o.o.	30	Production of electricity
Brodosplit - Izvor energije vjetroparkova d.o.o.	30	Renting and leasing of other machinery, equipment and tangible goods
Brodosplit - Produkt plinske elektrane d.o.o.	30	Renting and leasing of other machinery, equipment and tangible goods
Brodosplit - Vjetrostupovi d.o.o.	30	Manufacture of metal structures and parts of structures
Brodosplit - Klimatizacija i ventilacija d.o.o.	30	Plumbing, heat and air conditioning installation
Brodosplit - Brodska i ostala oprema d.o.o.	30	Manufacture of metal structures and parts of structures
Brodosplit - Metalne konstrukcije d.o.o.	30	Manufacture of metal structures and parts of structures
Brodosplit - Namještaj po mjeri d.o.o.	30	Joinery installation
Brodosplit - Interijer i završni radovi d.o.o.	30	Joinery installation
Brodosplit - Strojna obrada d.o.o.	30	General mechanical engineering
Brodosplit - Ljevaonica d.o.o.	30	Casting of iron
Brodosplit - Istraživanje i razvoj d.o.o.	30	Other research and experimental development on natural sciences and engineering
Brodosplit - Korporativna zaštita d.o.o.	30	Private security activities
Brodosplit - Gradnja d.o.o.	30	Construction of residential and non-residential buildings
Brodosplit - Otpremništvo d.o.o.	30	Other transportation support activities
Brodosplit - Najam Vozila d.o.o.	30	Renting and leasing of cars and light motor vehicles
Brodosplit - Oblaganje d.o.o.	30	Building of ships and floating structures
Brodosplit - Servis brodova d.o.o.	30	Repair and maintenance of ships and boats

Through subsidiary Brodosplit - Plovidba d.o.o., Company has control over: BS STAR SHIPPING Inc, BURIN WIND CRUISE SHIPPING Inc, GARBIN WIND CRUISE SHIPPING Inc, LEVANT WIND CRUISE SHIPPING Inc, MAESTRAL WIND CRUISE SHIPPING Inc, PULENAT WIND CRUISE SHIPPING Inc, GREEN4SEA SHIPPING 1 Inc, GREEN4SEA SHIPPING 2 Inc, GREEN4SEA SHIPPING 3 Inc, GREEN4SEA SHIPPING 4 Inc, DREAM ONE SHIPPING Inc, RIVER CRUISE SHIPPING, POLAR EXPEDITIONS B.V. Netherland, POLAR EXPEDITIONS Inc Marshall Islands, POLAR EXPLORER Inc, XB AHTS COMPANION SHIPPING Inc, XB AHTS GUARDIAN SHIPPING Inc, XB AHTS HERO SHIPPING Inc and XB AHTS SUPPORTER SHIPPING Inc.

Through subsidiary Brodosplit – Holding d.o.o., Company has control over Brodosplit Italia.

NOTE 18 – INVESTMENTS IN JOINT VENTURES

(in thousands of HRK)	**2016**	**2015**
At the beginning of the period	9,560	4,740
Additional investment	2,499	5,219
Share in loss	(99)	(399)
At the end of the period	**11,960**	**9,560**

The Group has 50% share in company Kamen-dent d.o.o., Bosnia and Herzegovina.

Financial information of the investment in joint ventures can be summarized as follows:

(in thousands of HRK)	**Assets**	**Liabilities**	**Revenue**	**Net loss**
Kamen-dent d.o.o.	14,862	(1,265)	5	(198)

NOTE 19 – NON-CURRENT RECEIVABLES

(in thousands of HRK)	**31 December 2016**	**31 December 2015**
Non-current receivables from the state (i)	-	84,389
Loans receivables from employees (ii)	9,772	11,940
Deposits (iii)	20,188	20,322
Other receivables	6,518	4,629
	36,478	**121,280**

(i) Non-current receivables from the state as at 31 December 2015 related to non-current portion of receivables for government grants. Receivables are discounted using discount rate of 5.46%. As at 31 December 2016 all receivables are current.

(ii) Interest rate on loans to employees amounts to 1%-2%. Receivables are discounted using discount rate of 4.14%.

(iii) Deposits are deposited on a period of 3 to 4 years. During the year, the effective interest rates were between 0.05% and 0.1%. Deposits in the amount of HRK 18,547 are secured against bank loan of the parent company. Deposits in the amount of HRK 1,584 relate to performance guarantee.

NOTE 20 – FINANCIAL INSTRUMENTS BY CATEGORY

Accounting policies for financial instruments relate to the following:

(in thousands of HRK)	31 December 2016	31 December 2015
Financial assets		
Trade receivables	90,099	72,497
Accrued income	185,969	24,212
Loans given	30,896	74,295
Other receivables	2,539	4,326
Financial asset available for sale	343	343
Cash and cash equivalents	41,204	18,273
	351,050	**193,946**

Financial assets do not include tax receivables and advances given.

(in thousands of HRK)	31 December 2016	31 December 2015
Financial liabilities		
Trade payables	139,061	144,476
Other payables	72,004	82,916
	211,065	**227,392**

Financial liabilities do not include liabilities for taxes, liabilities towards employees, contributions and advances.

NOTE 21 – INVENTORIES

(in thousands of HRK)	31 December 2016	31 December 2015
Raw materials	125,424	163,031
Work in progress	103,291	102,184
Advances for inventories	19,681	18,431
Commercial goods	4,477	3,686
Finished goods	8	8
	252,881	**287,340**

Included in work in progress is an uncompleted vessel for which the contract has been terminated in 2015. The uncompleted vessel has been written down to an estimated net realizable value of HRK 98,251 thousand. (2015.: 99,255)

As at 31 December 2016 there are no pledged inventories as security for bank loan (2015.: 58,429) (note "Loans and borrowings").

NOTE 22 – CURRENT TRADE AND OTHER RECIEVABLES

(in thousands of HRK)	**31 December 2016**	**31 December 2015**
Related party trade receivables	50,473	61,537
Trade receivables - non-related	54,516	22,476
Decreased by: impairment of trade receivables	(14,890)	(11,516)
Trade receivables - net	90,099	72,497
Receivables from the state (i)	111,046	149,025
Loans given to subsidiaries (ii)	18,806	60,032
Accrued revenues (iii)	185,969	24,212
Accrued revenues - other	-	139
Loans receiveables from employees	2,318	2,323
Prepaid expenses	1,115	-
Deposits	420	2,415
Receivables from employees	305	309
Advances given to related parties	-	294
Income tax receivable	591	750
Other receivables	2,539	4,326
	413,208	**316,322**

(i) Receivables from the state include current portion of receivables for government grants in the amount of HRK 89,000 thousand (2015: HRK 135,000).

(ii) Loans given to related parties has been issued with a 5.14% interest rate (2015: loans given to related parties has been issued with a 7% interest rate which was changed to 3% as of 31 October 2015).

(iii) Accrued revenues relate to receivables from customers for construction contracts (note “Work in progress”).

NOTE 22 – CURRENT TRADE AND OTHER RECIEVABLES (continued)

Movement in provision for impairment of trade receivables is as follows:

(in thousands of HRK)	2016	2015
Balance at 1 January	11,516	10,738
Collected	(922)	(207)
Write-off	(577)	(4,287)
Increase	4,873	5,272
Balance at 31 December	**14,890**	**11,516**

The ageing of due trade receivables that have not been impaired is as follows:

(in thousands of HRK)	31 December 2016	31 December 2015
0 to 90 days	37,278	7,738
91 to 180 days	1,388	2,714
above 181 days	51,433	62,045
Balance at 31 December	**90,099**	**72,497**

NOTE 23 – CASH AND CASH EQUIVALENTS

(in thousands of HRK)	31 December 2016	31 December 2015
Cash at banks	40,495	15,993
Deposits	-	2,207
Petty cash	709	73
	41,204	**18,273**

Deposits are deposited on a period less than 3 months. During the year, the effective interest rates were between 0.5% and 2%. Deposit is given as a guarantee for the quality of work performed.

Cash at banks includes cash in the amount of HRK 2,269 thousand that Company can not use because these funds are moved to special bank account due to legal cases (2015: HRK 626 thousand).

NOTE 24 – WORK IN PROGRESS

(in thousands of HRK)	**2016**	**2015**
Contract costs incurred up to the reporting date	616,146	700,846
Recognized (losses)/gains till the reporting date	83,483	(134,707)
	699,629	566,139
Less: invoicing in progress and advances received	(545,950)	(607,191)
Receivables from / (liabilities to) the client for the contracted work	**153,679**	**(41,052)**
Reclasified to (accrued revenue)/advances received from suppliers	(153,679)	41,052

Adjustment of revenues from construction contracts

(in thousands of HRK)	**2016**	**2015**
Revenues from construction contracts	657,330	470,703
Less revenues from construction contracts recognized in previous years	(167,236)	(263,694)
	490,094	**207,009**

NOTE 25 – SHARE CAPITAL AND RESERVES

i) Share capital

In accordance with the General Assembly's decision as of 3 March 2015 share capital was increased from HRK 525,466,140 for the amount of 10,000,080 by cash contribution of shareholder DIV BRODOGRADNJA d.o.o., Samobor, Bobovica 10/A, MBS: 080812968, PIN: 44993645694, by issuance of 166,668 new shares with exclusion of purchase rights of other shareholders. After the increase, share capital amounts to HRK 535,466,220.00 and is divided by 8,924,437 ordinary shares, nominal value of each being HRK 60.00.

As at 31 December 2016 the shareholder structure is as follows:

	Number of shares	Share amount
Shareholder	units	%
DIV – Brodogradnja d.o.o.	8,903,280	99.76%
Croatian chamber of commerce	11,637	0.13%
Uniqa d.d.	5,894	0.07%
Private persons	3,625	0.04%
Republic of Croatia	1	0.00%
Total	**8,924,437**	**100%**

ii) Legal reserves

The legal reserve is required under Croatian law and must be built up at a minimum of 5% of the profit for the year until the total legal reserve reaches 5% of the Company's share capital and amounts HRK 26,773 thousand (2015: HRK 26,773 thousand). Legal reserves are not distributable.

iii) Revaluation reserves

(in thousands of HRK)	Revaluation of assets	Fair value of asset available for sale	Other	Total
1 January 2016	216,581	5	1,781	218,367
Revaluation - gross	5,779	-	-	**5,779**
Revaluation - tax	(1,040)	-	-	**(1,040)**
Depreciation transfer to retained earnings - gross	(44,996)	-	-	**(44,996)**
Depreciation transfer to retained earnings - tax	8,999	-	-	**8,999**
Reconciliation of tax rate - defferd tax liability	4,514	-	-	**4,514**
Change in AFS	-	7	-	**7**
31 December 2016	**189,837**	**12**	**1,781**	**191,630**

NOTE 26 – NON-CURRENT PROVISIONS

Non-current provisions relate to provisions for fines and court cases. Movement in provision is shown in table below.

(in thousands of HRK)	**2016**	**2015**
Balance at 1 January	34,296	31,490
Recognised during period	5,304	22,255
Utilized during period	(1,761)	(1,538)
Released during period	(16,434)	(17,911)
Balance at 31 December	**21,405**	**34,296**

NOTE 27 – CURRENT PROVISIONS

(in thousands of HRK)	**Warranty**	**Termination benefits**	**Total**
Balance at 1 January 2016	12,702	4,609	17,311
Recognised during period	357	36	393
Released during period	(4,538)	(1,009)	(5,547)
Balance at 31 December 2016	**8,521**	**3,636**	**12,157**

NOTE 28 – LOANS AND BORROWINGS

(in thousands of HRK)	**31 December 2016**	**31 December 2015**
Long term loans and borrowings		
Bank loans	151,156	-
	151,156	**-**
Current loans and borrowings		
Bank loans	26,452	51,918
Related parties loans	11,000	-
	37,452	**51,918**

Non current liabilities toward banks relate to non current bank loan for financing shipbuilding in the amount of EUR 20 million with 3M EURIBOR interest rate + 5% per annum. The loan is repayed at once on the delivery of the ship and no later than 31 March 2018. Newbuilding which is financed is pledged as a security against the loan, as well as 2 ships over which the Group has ownership and one debenture for each subsidiary of a loanholder Brodosplit – Holding d.o.o. and co-borrower: DIV d.o.o., Brodosplit d.d. and Brodosplit – Brodogradilište specijalnih objekata d.o.o.

NOTE 28 – LOANS AND BORROWINGS (continued)

Liabilities toward banks relates to current revolving loan in the amount of EUR 3.5 million with interest rate of 3M EURIBOR + 5.2% per annum. Yacht and debenture is pledged as a security against the loan. (2015: loan with 3M EURIBOR + 6.2% variable interest rate per annum. Property of the company is pledged as security against the loan).

Loans to related parties include a non-interest-bearing liabilities from the parties related to owners of the Company in the amount of HRK 11,000 thousand (2015: none).

The Company has revolving loan available in the amount of EUR 9 million which is available until 31 October.

NOTE 29 – TRADE AND OTHER LIABILITIES

(in thousands of HRK)	**31 December 2016**	**31 December 2015**
Trade payables - non-related	82,410	89,871
Related party trade payables	56,651	54,605
Liability for concession fee	23,457	30,892
Advances received	5,837	103,848
Prepayments	26,453	28,368
Liabilites for taxes, contributions and similar	25,661	22,294
Liabilities towards employees	12,213	13,060
Accrued expenses	16,520	9,960
Accrued penalty interests	524	9,398
Liabilities from court decisions	-	1,516
Liabilities towards banks and smiliar institutions	75	93
Liabilities for income tax	302	22
Other current liabilities	4,975	2,688
	255,078	**366,615**

Advances received relates to advances received from customers for construction contracts (Note – ‘Work in progress’).

NOTE 30 – RELATED PARTY TRANSACTIONS

Parties are considered to be related if one of the parties has the power to exercise control over the other party, is under common control or if it has significant influence over the other party's operations.

Total amounts of related parties transactions, receivables and payables at year end and related party expenses and income are as follows:

Sales revenue

(in thousands of HRK)	2016	2015
DIV d.o.o.	1,369	9,323
Debeljak Industrija Vijaka d.o.o., Sarajevo	1,088	-
Marine and Energy Solutions DIV d.o.o.	205	238
PTC Krka Knin	5	-
Brodosplit - Projekt d.o.o.	12	-
Total	**2,679**	**9,561**

Other operating income

(in thousands of HRK)	2016	2015
DIV d.o.o.	2	4
Debeljak Industrija Vijaka d.o.o., Sarajevo	94	-
Brodosplit - Projekt d.o.o.	424	-
Total	**520**	**4**

Material expenses

(in thousands of HRK)	2016	2015
Debeljak Industrija Vijaka d.o.o., Sarajevo	2,022	3
DIV d.o.o.	6,437	5,946
Shanghai Vida Industry & Trading Co.Ltd	31	-
Total	**8,490**	**5,949**

Cost of goods sold

(in thousands of HRK)	2016	2015
Debeljak Industrija Vijaka d.o.o., Sarajevo	23	-
DIV d.o.o.	116	1,392
Marine Consulting d.o.o.	159	-
Brodosplit - Projekt d.o.o.	9	-
Total	**307**	**1,392**

NOTE 30 – RELATED PARTY TRANSACTIONS (continued)

Costs of services

(in thousands of HRK)	**2016**	**2015**
DIV d.o.o.	14,495	18,981
Debeljak Industrija Vijaka d.o.o., Sarajevo	1,226	738
Marine and Energy Solutions DIV d.o.o.	4,926	4,859
Brodosplit - Projekt d.o.o.	5,389	-
Total	**26,036**	**24,578**

Other operating expenses

(in thousands of HRK)	**2016**	**2015**
DIV d.o.o.	383	198
Marine and Energy Solutions DIV d.o.o.	12	-
Shanghai Vida Industry & Trading Co.Ltd	192	-
Brodosplit - Projekt d.o.o.	673	-
Total	**1,260**	**198**

Finance income

(in thousands of HRK)	**2016**	**2015**
DIV d.o.o.	2,967	1,611
DIV SARAJEVO DEBELJAK INDUSTRIJA VIJAKA D.O.O.	25	2
Shanghai Vida Industry & Trading Co.Ltd	2	-
Total	**2,994**	**1,613**

Finance costs

(in thousands of HRK)	**2016**	**2015**
DIV d.o.o.	-	78
DIV SARAJEVO DEBELJAK INDUSTRIJA VIJAKA D.O.O.	14	-
Shanghai Vida Industry & Trading Co.Ltd	2	-
Total	**16**	**78**

NOTE 30 – RELATED PARTY TRANSACTIONS (continued)

Trade receivables

(in thousands of HRK)	31 December 2016	31 December 2015
Marine and Energy Solutions DIV d.o.o.	265	294
Kamen Dent d.o.o.	587	-
Brodosplit - Projekt d.o.o.	10	-
DIV d.o.o.	49,611	61,523
Total	**50,473**	**61,817**

Loans given

(in thousands of HRK)	31 December 2016	31 December 2015
DIV d.o.o.	18,806	60,032
Total	**18,806**	**60,032**

Trade payables

(in thousands of HRK)	31 December 2016	31 December 2015
DIV Brodogradnja d.o.o.	33,750	33,750
DIV d.o.o.	18,370	19,783
Brodosplit - Projekt d.o.o.	3,448	-
Debeljak Industrija Vijaka d.o.o., Sarajevo	10	179
Marine and Energy Solutions DIV d.o.o.	1,073	891
Total	**56,651**	**54,603**

Loans received

	31 December 2016	31 December 2015
Božidar Debeljak	4,000	-
Vjera Debeljak	4,000	-
Vedrana Debeljak	1,500	-
Danijela Debeljak	1,500	-
Total	**11,000**	**-**

NOTE 30 – RELATED PARTY TRANSACTIONS (continued)

Key management remuneration

Key management remuneration for 2016 amounted to HRK 13,369 thousand and relate to 39 employees (2015.: HRK 9,167 thousand and relate to 44 employees).

NOTE 31 – SALE OF SUBSIDIARY

During the year, subsidiary Brodosplit – Projekt d.o.o. was sold to the ultimate parent DIV d.o.o.

Sale of subsidiary had the following impact:

(in thousands of HRK)	**2016**
Trade and other receivables	1,540
Cash and cash equivalents	1
Assets	**1,541**
Trade and other payables	168
Other liabilities	435
Liabilities	**603**
Net assets disposed	**938**
Revenue from sale of subsidiary	202
Loss from sale of subsidiary	**(736)**

NOTE 32 – CONTINGENT LIABILITIES

Government grants

The contract on the sale and transfer of shares defined particularly important parts of the restructuring program; the share of own contribution to the overall restructuring costs, adjustment of shipbuilding production capacity of the Company, limiting of the production of ships in CGT (compensated gross tonnage) and achievement of sustainability; whose failure can result in an order to the Company and its subsidiaries for the return of all government grants received after 1 March 2006, increased by statutory penalty interest.

The share of the own contribution implies the obligation of the buyer (DIV Brodogradnja d.o.o.) in accordance with the restructuring program, which amounts to 40% of the total restructuring costs. Part of the total cost refers to the obligation of the share capital increase in the total amount of HRK 50 million by the dynamics of HRK 20 million in 2013, HRK 20 million in 2014 and HRK 10 million in 2015 (Note “Share capital”).

Adjustment of production capacity and production limit depending on the tonnage defined by the restructuring program and the agreement on the limitation of production for the period until 31 December 2022 in which the production can not be higher than agreed.

Achieving sustainability include the following measures: maintaining at least 2,000 employees in the Company and its subsidiaries at the end of each month during the implementation of the restructuring program, the maintenance of a minimum number of hours at defined levels by the end of the ninth month of 2017, the maintenance of a minimum quantity of processed steel at a defined level by the end of the ninth month of 2017, maintaining the defined level of capital and reserves at the end of the year ending with 2017 and positive consolidated operations at the end of 2016 and 2017. Evaluation of sustainability is provided by the competent authority (European Commission) which, if it considers that no sustainability has been achieved, may order the Company to refund grants.

Court cases

In the ordinary course of operations, the Group was plaintiff and defendant in several legal disputes. Based on Management Board and legal counsel believes, provision have been created for those court cases that will result with losses and were those losses can be estimated (Note 26). In addition to those court cases for which provision have been made there are some legal disputes will not result in significant losses.

Issued warranties

As at 31 December 2016, the Group is exposed to potential liabilities arising from issued warranties in the amount of HRK 131,862 thousand (2015: HRK 122,832 thousand). Warranties are related to advance payments and security for the quality of work performed.

NOTE 33 – SUBSEQUENT EVENTS

On 3 April 2017, a long-term loan amounting EUR 37 million was given by financial institution to related party Polar expeditions Inc for financing the new agreed ship construction. Construction of the ship will be carried out by the Company, which is, alongside with DIV d.o.o., co-guarantee.

On 5 April 2017, a short-term loan amounting EUR 4.2 million was signed. The loan was approved for financing of working capital. Co-guarantors are parent company Brodograđevna industrija Split d.o.o. and the ultimate parent company DIV d.o.o. .

Following the Management Board's decision, Brodosplit-Holding d.o.o. will be merged into the parent company Brodograđevna industrija Split d.o.o. in the middle of 2017. All rights and obligations of the affiliated company will be transferred to the acquirer company upon the merger date.

Tomislav Debeljak	Darko Pappo	Vlatko Kvesić
Chairman of the Board	*Member of the Board*	*Member of the Board*

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