HYPO ALPE ADRIA
SUPPORTIVE. FRIENDLY. FAIR.

Annual Report 2010.

Hypo Alpe-Adria-Bank a.d. Banja Luka

Bosnia and Herzegovina

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Mission and Principles

Headquartered in Banja Luka, Hypo Alpe-Adria-Bank a.d. Banja Luka is the largest bank in Republika Srpska and is also the most valuable brand in the domestic financial industry.

Working in partnership with citizens, local communities, small and medium enterprises, businesses and public institutions, we provide a wide range of financial solutions that are simple, creative and responsible, with the primary objective to bring the best result for around 200 thousand of our clients in over 40 municipalities in RS.

Two basic principles that guide us while carrying out our mission are:

- Success for all: working for our customers and shareholders
- Responsible banking: ethical and transparent business and consistent application of international standards.

Letter from the Management Board

A year of 2010 was definitely a year that represented the biggest turning point in the operations of Hypo Alpe-Adria-Bank a.d. Banja Luka since the beginning of its presence in the Republic of Srpska market.

All the consequences of the global financial crisis that started in mid-2007 had an overwhelming effect on the economy of Bosnia and Herzegovina and that of the Republic of Srpska, being a small market, with its institutions not sufficiently developed to cope at least a little successfully with the problems that the crisis caused to the economy. A decrease in exports resulted in the fall in industrial production and the lack of quality strategies with clearly outlined deadlines for their implementation, while the lack of investments resulted in intensive slowing down of the corporate sector activities. The negative trend did not avoid the segment of small and medium-sized enterprises either, altogether leading to increased unemployment and additionally decreasing the already low purchasing power of citizens.

All the above has resulted in an extensive increase in non-performing loans which required the strictest possible application of international accounting standards in the segment of risk managament, especially credit risk. This meant that the banking sector had to provide fresh capital in order to guarantee its own stability and safety, as well as safety of clients and of the market on the whole.

As the biggest lender in the domestic market, Hypo Alpe-Adria-Bank a.d. Banja Luka was the most exposed to the consequences of the crisis and to the increase in non-performing loans, mainly those from corporate sector.

Financial performance in 2010

While for some people crisis means a problem, for us in Hypo Bank Banja Luka crisis has proved to be both a challenge and an additional motivation to make our bank as functional and as efficient as possible, capable of bringing success to everyone: both clients and shareholders! Thus, the year 2010 was marked by attainment of the set goals and by fulfilment of most of very ambitious plans in all segments of operations. We primarily focused on the activities with the citizens and small and medium-sized enterprises and entrepreneurs as well as the public institutions. Our activities included advancing loans, although at a slower rate because we had to resort to stricter treatment of risk when approving new placements and seek clients who are creditworthy and with good security instruments. Something that makes us especially happy is the continuation of growth of citizens' savings as the primary local source of financing, and as a confirmation of big trust that the citizens place in Hypo Bank Banja Luka. This means that we were able to generate stable rate of revenues both from interest and commissions.

Thanks to everything stated above, the income generated before provisioning charges and income tax amounted to 26 million KM. It was this result from operating income that was of immense importance to us and the best indicator of functionality and efficiency of the system itself.

In the segment of corporate banking, which was hit the hardest by the crisis, the bank managed to accommodate its clients by rescheduling and refinancing of their operations. On the other hand, all the above challenges that the domestic market and the corporate sector in particular had to deal with, have resulted in enormous growth of provisioning charges, rising to as high as 110 percent compared to the end of 2009. Our bank allocated 71.4 million KM as provisioning charges and paid income tax in the amount of 3.2 million KM, therefore the final net result was negative and amounts to 48.6 million KM. Nevertheless, such a result is not worrying because we expect that, following successful continuation of loan portfolio restructuring and forecasted recovery of the domestic economy, as soon as in 2011 the Bank will restore its satisfactory profitability.

The Bank's total assets was in the amount of 1.5 billion KM which still makes Hypo Bank Banja Luka the biggest bank in the Republic of Srpska market and the fourth bank at the level of Bosnia and Herzegovina. Total loans amount to 1.24 billion KM, while total deposits amounted to 1.08 billion KM. Total equity of the bank is 211.6 million KM of which share capital is 175.5 million KM. In other words, capital adequacy was as high as 14.2 percent. With the power of capital, being one of the key banking segments and the most important compensation factor for the risk in banks, we have additionally confirmed our role of the biggest, completely stable and safe financial institution.

Responsible banking: ethical and transparent operations and consistent application of international accounting standards

As a member of Hypo Group Alpe Adria, which is 100-percent owned by the Republic of Austria, a member country of the European Union, the provisions made by Hypo

Bank Banja Luka were the biggest in the Republic of Srpska market and one of the biggest in the market of Bosnia and Herzegovina. This took place following the Bank's consistent application of international accounting standards and international financial reporting standards while particularly focusing on credit risk management. We were able to make these provisions successfully thanks to a timely capital increase in the amount of 50 million KM, that the Republic of Austria made in the Hypo Bank Banja Luka at the end of 2010 through Hypo Group. Therefore, we can say with full responsibility that the Bank's loan portfolio has been secured in a quality manner, guaranteeing safety to the bank itself, to shareholders, the clients and the market in which the bank operates. On the other hand, for the first time in the Republic of Srpska market financial reporting was done with the application of International Accounting Standard IAS39, fully applied by our bank, thus providing additional guarantee in terms of transparent operations.

The main tasks for 2011

We have already identified the key priorities for 2011 and the period after that. One of them is to improve the current model of servicing the clients by adding talented people and placing them to strategic positions in the key segments of the market, and by our continued investments in infrastructure. Another set of the priorities is in more intensive development of the segment of e-banking and mobile banking, that should position us as a leader bank in that field too. New generations of customers are coming who are able to make use of the advantages offered by modern technologies, and they will more and more ask that their financial services be delivered in the same way, that is to say, swiftly and efficiently. The introduction of state-of-the-art banking software, Temenos/T 24 will help us in that. Another important task is to continue investing in our own human resources, modern technologies and business network so as to be able to offer our clients a unique experience of the best quality banking service. One of the priorities will be to continue building an image of the bank as a source of new ideas and new activities. We wish to be the best in the segment of advising clients. This was the reason that in 2010 we established the Department of Economic Research led by the Chief Economist whose task, besides advising the Bank management, includes providing expert economic forecasts and analysis of macroeconomic trends as well as provide our customers with access to vitally important information in the market. There is no other financial institution at the moment that would be more knowledgeable in the domestic market than us. Our challenge is to make use of that knowledge so that our customers can benefit from it too.

We need to additionally connect with our clients. The power of Hypo brand in the Republic of Srpska is our great advantage. We continuously invest in our brand seeking the best way to connect with our clients. We will have to additionally work on the methodology of measuring both the satisfaction of our clients and of new detailed characteristics and needs.

We are growing at a time of digital and social utilities that help us understand what the clients want from their bank. We continue to invest in our people through numerous training and development programs.

The main goal of the mentioned investments is to try to sustain our strength and our competitive sharpness, to keep our market share and continue our organic growth. We work hard and wisely to try to make our bank safe in the future.

Conclusion

The year behind us has been full of challenges. Our task in the future will be to make sure that the coming years are even more prosperous – in terms of our servicing of clients, adding value for our shareholders and applying responsible banking.

We are confident that this can be done because we were witnesses to what our people were able to achieve in the past. Their relentless efforts helped us overcome the crisis. Leading Hypo Bank Banja Luka to a new stage will not be an easy task at all. True professionals always expect competition to be fierce and challenges daunting. But our people are on top of their task and therefore we wish to especially thank them for their hard work throughout 2010 as well as for the efforts that they will be making in the time to come.

We owe big gratitude to our clients, especially our savers, for their big support. We also wish to extend our thanks to the Supervisory Board, for their support, for their trust and good guidelines.

We especially wish to thank our owner, Hypo Group Alpe Adria, that is to say, the Republic of Austria, for their huge support and confidence they have placed in us. With their unreserved support we have managed to continuously service the needs of over 200 thousand of our clients at the same time reaffirming the status of the biggest bank in the domestic market.

Our task is to make Hypo bank even more profitable and prove that we are worthy of the confidence placed in us. With the continuance of restructuring of loan portfolio, expected decrease of provisions for non-performing loans and forecasted recovery of domestic economy, with the organic growth of income, as soon as in the first half of 2011 we expect to generate considerable profit that will be additionally increased at the end of 2011.

Change in the composition of the Management Board

In 2010 the composition of the Bank's Management Board changed. A Slovak, Samuel Vlčan was appointed the Bank's director, while Srećko Bogunović, the previous director of Hypo Alpe-Adria-Bank a.d. Banja Luka, left the Bank. Also, the management was joined by a new deputy director, Dragan Kovačević, and executive director, Goran Babić. Gerhard Lehner, the previous executive director, also left the Bank in 2010.

Management Board Hypo-Alpe-Adria-Bank a.d. Banja Luka

Goran Babić	**Dragan Kovačević**	**Samuel Vlčan**
Executive Director	Deputy Director	Director

Management Board Hypo-Alpe-Adria-Bank a.d. Banja Luka

Samuel Vlčan
Director

Areas of Responsibility:
Board Assistance Deaprtment
Credit Risk Management Department
Risk Controlling Department
Credit Processing Department
Rehabilitation Department
Product Management Department
Accounting and Financial Controlling Department
PR/Marketing Department
Human Resources Department
Research and Chief Economist BiH Department
NPL Management Department
Ombudsman

Dragan Kovačević
Deputy Director

Areas of Responsibility:
Retail + SME Department
Compliance Department
ORG/IT Department
Transaction Banking Department
Logistics Department

Goran Babić
Executive Director

Areas of Responsibility:
Corporate + Public Department
Legal Affairs Department
Treasury Department

Basic Economic Indicators for Bosnia and Herzegovina

Overview of economic movements in 2010 and the Projection

The most significant movement in the year 2010 was in the GDP, which developed from -2.9% in 2009 to a positive trend. The evaluation of the Chief Economist of the Hypo Bank BiH is that the GDP will be about 0.7% in 2010.

International markets' demand is still the main source of growth. As a result of the recovered markets in the Western European countries, to which Bosnia and Herzegovina is closely linked, a revived demand for alumina and steel and consequent thereon - increase of their prices, the largest BiH exporters, „Arcelor Mitala“ and „Birča“ boomed again, so that import – export coverage was at the end of 2010 - 50.5%, compared to 45.8% at the end of 2009. Industrial production increased by 1.6% at the end of 2010 and continued its upwards trend in January and February 2011 (by 6.6% compared to February 2009), driven mainly by processing production, which due to increased demand from international markets grew by 9.9%. The Projection 2011 relies on further development of export as a response to further revival of Western European markets.

Continuous growth of food price. Inflation rate was 3.1.% at the end of 2010, as a consequence of unexpected jump of food and housing price at the rate of 4%, i.e. 2.5%. The jump of prices was certainly caused among other things by the increased price of oil and oil derivates at the world market and harmonization of the EU excise rates for tobacco and tobacco products in BiH. The entities' governments limited margins on basic foodstuffs at the beginning of 2011, which decision however exerted no effect at all, having in consideration that inflation increased by 2.7% in January 2011 and by 3.3% in February 2001 as a result of the increase of the food price by 6%. According to the projection of the Chief Economist of the Hypo Bank, the consumer prices index/inflation will with corrections amount up to 3.5%, because she believes that the increase in Consumer price index (CPI) in 2011 should remain in line with trends from 2010 taking the expectations of the stagnation of wages determined by demand for goods, which again determines the weight of the CPI. Weak domestic demand is accompanied by the necessary structural adjustments to keep the level of core inflation at a modest scale.

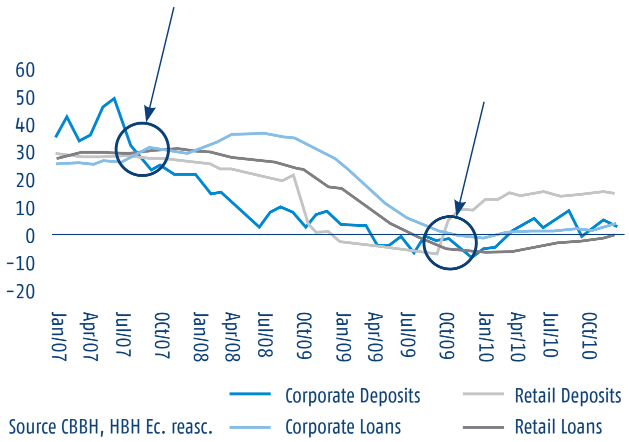
Negative tendencies at the labour market. The available household income has significantly dropped mainly as a result of decrease of the realistic growth rate of net salaries by 1.1% at the level of BH and decrease of cash inflow from abroad, accompanied on the other hand by jump of the unemployment rate from 24.1.% in 2009 to 27.2% in 2010, which is expected to further increase in the year 2011, even to 28.5%, if the entities' and the state governments pursue the idea of reducing the currently huge number of civil service employees. In addition, real sector is also expected to cut the number of workers, as a consequence of remnants from the past and the lack of support provided by the state in creation of a better business environment. However, this does not come as a surprise, especially having in mind a poor or even sluggish recovery rate of economy on one hand and on the other, the reduced budget deficit defined by the three-year stand-by arrangement signed with the IMF (-4.5% in 2010, compared to the defined deficit of -3% for 2011).

Request for reduction of mandatory reserve. With the aim of strengthening the liquidity of the real sector, the Central Bank BiH reduced the mandatory reserve rate for short-term deposits of up to one year from 14% to 10%, releasing in that manner additional KM 300 million, which measure, however, has not given the expected result, as the banks' funds exceeding the mandatory reserve still remained very high even after the mentioned release, clearly showing the lack of demand for loans in general. Loan placements of commercial banks to Corporate clients were in 2010 increased by 3% and to Retail clients by 1%.

Changed behaviour of consumers. The effects of the market volatility in global financial movements and effects of loan expansion from about 10 years ago were clearly reflected in behaviour of consumers, who became much more cautious in spending. The citizens' deposits displayed a negative tendency of -6.9% in September 2009, compared to the same period of the previous year, but in December 2010 an increase of 14.6% was visible compared to the end of 2009.

Continuous growth of non-performing loans. The non-performing loans in the banking sector of BiH and wider in entire region have been on a constant upturn, so that at the end of 2009, they amounted up to 5.9% and even up to 9.2% in September 2010, whereas they are expected to grow further as a result of the credit boom and constant further weakening of local

Loans vs. Deposits (YtoY %)



Source CBBH, HBH Ec. reasc.

economies, struggling with similar problems, that is a complete lack of willingness of local authorities to start strong structural reforms with the aim of securing financial and external sustainability as a pre-condition for economic self-sustainability. The Chief Economist of the Hypo Bank expects the non-performing loans to reach their peak in the 1Q 2011.

Banking sector outlook. According to the projection of the Chief Economist of the Hypo Bank, the year 2011 shall be a transitional year, in which a main focus shall be on cleansing the balance sheet, resolving the issues with the assets quality and particularly on preparation for the post-crisis development, as those who are well prepared for the post-crisis shall of course have the best effects when coming to the starting-point, that is – profitability and trend of further development and growth. The focus shall furthermore be placed on the strength of the banks' core capital and banks' preparedness to consistently apply local and international accounting standards in credit risk management. The banks, which try to play with the credit risk management, shall place themselves, but also the entire market at which they work in a very unfavourable position.

BiH Credit Rating 2010

If there is no end to the political agony, changes are possible. Bosnia and Herzegovina[1]:

	Foreign currency	Local currency
Governmental bonds rating	B2 / stabile prospects	B2 / stabile prospects
Country rating	Ba3 / stabile prospects	Ba1
Banks deposits rating	B3 / stabile prospects	Ba3

Moody's, January 2010

Current rating BiH:

	Moody's Investors Service	Standard & Poor's
Rating	B2 / stabile prospects	B+ / stabile prospects
Date	7. 1. 2010.	17. 12. 2010.
Activity	confirmed	confirmed

Suorce: CBBH, Moody's Investors Service, Standard & Poor's

Securities trading

Sarajevo Stock-exchange (SASE)

The trading at the Sarajevo Stock-exchange in 2010 amounted in total up to KM 108.554.379,41 or 38,38% of the total trading at all stock-exchanges in BiH. The total of 76.337.803 securities were traded with in 18.244 transactions.

Top 10 issuers	Trading	No. of transactions	% exchange-rate change
Bosnalijek d.d. Sarajevo	6,822,830.36 KM	2,293	-13.93%
BH Telecom d.d. Sarajevo	6,084,024.20 KM	2,216	-5.16%
FBiH obveznice ratna potraživanja ser. A	4,545,302.99 KM	798	56.00%
JP Elektroprivreda BIH d.d. Sarajevo	4,281,362.18 KM	828	-5.38%
FBiH obveznice ratna potraživanja ser. B	4,215,242.61 KM	694	66.13%
Vispak d.d. Visoko	3,797,516.86 KM	96	16.54%
ZIF BIG Investiciona grupa d.d. Sarajevo	3,390,020.91 KM	598	-29.18%
Fabrika duhana Sarajevo d.d. Sarajevo	3,255,323.31 KM	1,328	-32.90%
RMU Kamengrad d.d. Sanski Most	3,146,167.83 KM	88	0.31%
FBiH stara devizna štednja serija C	2,865,716.24 KM	464	-

Indices and market capitalisation	Last day of the previous period	Lat day of the current period	% change
Market capitalisation	7,158,678,913.80 KM	7,210,603,026.80 KM	0.73%
BIFX	1,839.08	1,520.80	-17.31%
SASX-10	1,053.10	944.07	-10.35%
SASX-30	1,097.17	925.95	-15.61%

Banja Luka Stock-exchange (BLSE)

The trading at the Banja Luka Stock-exchange in 2010 amounted in total up to KM 176.195.081 or 61,62% of the total trading at all stock-exchanges in BiH. The total of 16.735.005 securities were traded with in 10.164 transactions.

Top 10 issuers:

Securities symbol	Issuer	Price on 31/12/10	Average price	No. of transactions	Value (BAM)
BLKB-R-A	BALKAN INVESTMENT BANK AD B. LUKA	10	32.07	3	36,045,232
IEFB-R-A	MF BANKA AD BANJA LUKA	64.00	64.00	2	12,800,000
TRZN-R-A	TRŽNICA AD BANJA LUKA	1.40	1.37	539	7,960,913
RSRS-O-C	REPUBLIKA SRPSKA-izmirenje ratne štete 3	37.00	32.03	3,264	7,131,634
RSRS-O-D	REPUBLIKA SRPSKA-izmirenje ratne štete 4	37.98	31.08	2,980	6,290,374
TLKM-R-A	TELEKOM SRPSKE AD BANJA LUKA	1.38	1.38	1,600	5,570,331
VTNK-R-A	VITINKA AD KOZLUK	4.00	5.05	18	4,117,816
RSDS-O-C	RS-stara devizna štednja 3	80.500	81.44	357	3,736,138
KRIP-R-A	ZIF KRISTAL INVEST FOND AD B. LUKA	6.5	4.87	759	3,117,445
NOVB-R-E	NOVA BANKA AD BANJA LUKA	1	0.92	88	2,793,969

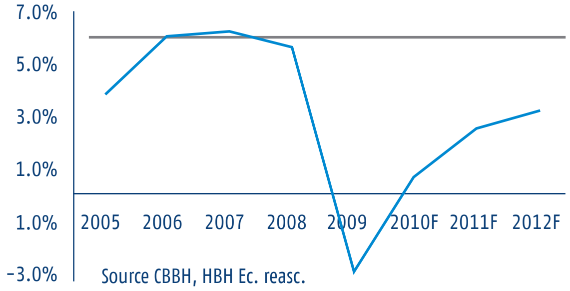
Indices and market capitalisation	Last day of the previous period	Lat day of the current period	% change
Market capitalisation	3,756,543,171KM	3,732,304,036 KM	-0.65%
BIRS	991.84	956.12	-3.60%
FIRS	1,864.62	1,632.46	-12.45%
ERS10	739.12	801.34	8.42%

Insurance

Reports 2010 shall be available in August 2011.

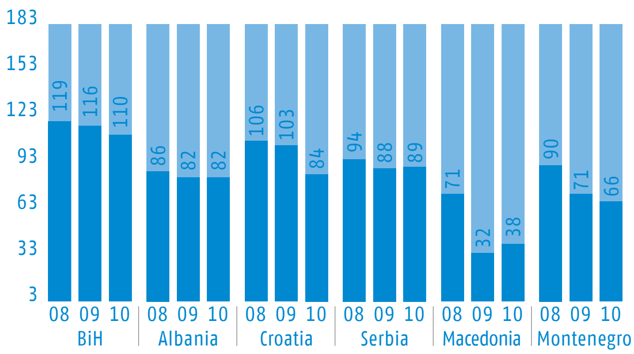
Slow economic recovery in BiH additionally jeopardized by political instability. Even tough the general elections were held in October 2010, governments have not been founded at all levels in BiH yet, except in Republika Srpska.
Promotion of economic stability is to some extent about avoiding economic and financial crisis and turbulences in economic activities, such as high inflation rate and too high volatility at the financial market. It is a well-known fact that political instability tremendously jeopardizes growth, whereas on the other hand, stabile political systems are a genuine catalyst of growth. Political instability is directly related to GDP growth and share of foreign and local investments in the GDP.
Due to persistent political instability in the country, we have after all corrected the GDP projection for 2011 and 2012 to 2% and 2.8%. Export is expected to remain the main generator of growth, as a result of further recovery of Western European markets and the announced investments in BiH. The local demand shall most probably not be significantly revived in a short period of time, particularly having in mind the changed and more cautious behaviour of consumers. Not even the planned growth is sufficient for a developing country as BiH is to start development and growth to such extent as to be reflected on the citizens' living standards. The acceptable potential growth would be 5.5%, even the rate of 6.5% is being mentioned.

Real GDP Growth BiH,%

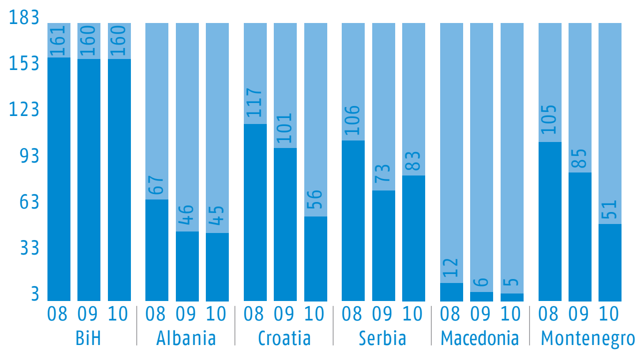


Strong political weaknesses and instability clearly influence the situation in BiH, which might be an additional aggravating element on the BiH way to the EU membership. This thesis is strongly supported by the below-presented World Bank Reports on movement of business terms and ranging of countries-signatories to the EU Association Agreement and on starting new business

Ease of Doing Business (Rank)



Starting a Business (Rank)



The research was made on 183 countries. The terms of business in BiH have in the time-period 2008 – 2010 slightly improved (BiH got from the 119th to 110th place), whereas the stagnation in starting new business have been strenghtened (from the 161st to the 160th place).

Corporate Social Responsibility

For several years, Hypo Alpe-Adria-Bank a.d. Banja Luka has been working on adjusting its business operations with the best practices of developed countries in the world, which define social responsibility of the organization on the issue of relation to employees, clients and business associates, shareholders, local community and protection of environment. Although there are still no clear directives in BiH and RS related to organize way of reporting for commercial companies in domain of the Corporate Social Responsibility - CSR, Hypo Bank wishes to introduce all interested parties with basic activities it undertakes in thefield of CSR.

Human Resources Management – HRM

Hypo Alpe-Adria-Bank a.d. Banja Luka, as member of multinational group working in 12 countries of the Alps- Adriatic region, is the employer fully dedicated to respecting individual values of each person regardless of his/her national, religious, race, gender or other civilization accepted differences. Hypo Bank, as the employer, fully respects and implements all positive legal regulations defining area of employment. All employees are employed fully and realize all legal rights upon annual leaves, sick leaves, personal earnings and contributions for health, social security, etc.

Also, the Bank enables employees to be engaged in sport and recreational activities through finance of lease in sports and recreational premises. All new employees go through organized training of acquaintance with the Bank, its vision, mission and strategy. All vacancies are fully adjusted to legal regulations and are always published in minimally 2 leading daily newspapers and the Bank's internet page. Adult-education process is constant, i.e. the Bank enabled employees to propose, in organized way, their education needs. The Bank, within its strong development in financial industry, organized, on annual level, series of seminars ad training sessions so bring employees to the latest knowledgein the aforementioned area.

In cooperation with employees, the Bank is doing annual report on self-assessment of each employee. The Bank ended 2010 with total of 517 employees, thus it is still the biggest employer in the RS financial industry.

Relationship to Customers and Business Associates

Hypo Alpe-Adria-Banka a.d. Banja Luka is deeply aware of the fact that loyal client is the biggest treasure of each financial institution bearing in mind the fact that business ethics takes very high place on the Bank's list of priorities.

The Bank intends to inform, on timely base, its clients and business associates on all changes related to its business, new products, services, interests, fee, commission, etc.

Also, through its marketing/PR actions, the Bank strictly complies with ethic code on truthfulness and factual state and it avoids any form of misleading client to make wrong conclusionsthrough disinformation or inconsistencies in contents. In the field of customers' rights, the Bank has enabled organized way of filing complaints on quality of services, products and general relation of the Bank to its clients via Bank's Ombudsman. Clients are able to submit their objections in all Bank's Branch Offices or by e-mail inform Hypo Ombudsman and to receive an official answer within the deadline of thirty days.

Relation to Local Community (Support to Culture, Art, Sports, Education and Health Public Institutions)

For many years, Hypo Bank has been supporting local communities, with significant funds from its budget, where it works through granting funds to education and health institutions and for events with goal to promote and preserve social values in the area of culture, art, non-commercial sports activities.

In 2010, Hypo Bank donated approximately 90.000,00 KM throughout RS. This money was donated to kindergartens, elementary and high schools, libraries, hospitals, and to education public institutions and associations of citizens taking care of children with special needs.

Last year also, Hypo Bank was one of leading financial supporters of many cultural and artistic events as well as noncommercial sports activities in RS through many sponsorshipactivities.

Goal of Hypo Bank is to be part of local identity in each community where it works and that the same community and its citizens can count on Hypo Bank and its understanding within its limits. Children are priority as well as institutions taking care of their organized educational development, social and health protection.

Bodies of the Bank

SUPERVISORY BOARD

Dipl. Kfm. MA Rainer Sichert, Chairman
Mag. Wolfgang Mösslacher, Deputy Chairman
Dipl. ek. Blaž Brodnjak, Member
Mag. Stephan Holzer, Member
Mag.rec.soc.oec. Sebastijan Firlinger, Member

AUDIT COMMITTEE:

Mag. Dr. Hans - Dieter Kerstnig, Chairman
Danijel Gregorić, Member
Nensi Marin, Member
Zoran Besak, Member
Vesna Pavlović, Member

MANAGEMENT BOARD:

Samuel Vlčan, Director
Dragan Kovačević, Deputy Director
Goran Babić, Executive Director

INTERNAL AUDITOR

Slavica Vukelić

SHAREHOLDERS WITH 5% OR MORE SHARES WITH VOTING RIGHTS:

Hypo Alpe-Adria-Bank International AG, Klagenfurt

Organization Chart

Financial Statements

for the year ended 31 December 2010

pwc

Independent auditor's report

To the shareholders and Board of directors of Hypo Alpe-Adria-Bank a.d.

We have audited the accompanying financial statements of Hypo Alpe-Adria-Bank a.d. Banja Luka, (the "Bank") which comprise the statement of financial position as at 31 December 2010 and the statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the Law on accounting and auditing in the Republic of Srpska, the Law on Banks and Banking Agency of Republic of Srpska decisions, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements, and plan and perform the audit to obtain reasonable assurance that the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to preparation and fair presentation of the Bank's financial statements in order to design audit procedures that are appropriate in the circumstances, and not for the purpose of expressing an opinion on the effectiveness of the Bank's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements present fairly, in all material respects the financial position of Hypo Alpe-Adria-Bank a.d. as at 31 December 2010, and its financial performance and its cash flows for the year then ended in accordance with the Law on accounting and auditing in the Republic of Srpska, the Law on Banks and Banking Agency of Republic of Srpska decisions.

PricewaterhouseCoopers d.o.o.

PricewaterhouseCoopers d.o.o. Sarajevo

"PRICEWATERHOUSECOOPERS" D.O.O. SARAJEVO

Selimović Alida

Alida Selimović, Certified auditor

Sarajevo, 7 March 2011

Statement of Comprehensive Income

Financial statements for the year ended 31 December 2010 (in 000 BAM)

	Notes	2010.	2009. Restated
Interest income		92,840	109,985
Interest expense		(40,247)	(49,938)
Net interest income	7	**52,593**	**60,047**
Fee and commission income		12,401	12,072
Fee and commission expense		(3,646)	(2,626)
Net fee and commission income	8	**8,755**	**9,446**
Foreign exchange gains, net		3,700	1,808
Other operating income	9	10,773	6,742
Other operating expenses	10	(49,821)	(40,066)
PROFIT BEFORE IMPAIRMENT LOSSES, PROVISIONS AND INCOME TAX		**26,000**	**37,977**
Impairment provisions for credit risk and potential other losses	11	(71,426)	(33,854)
(LOSS)/ PROFIT BEFORE TAX		**(45,426)**	**4,123**
Income tax expenses	12	(3,224)	(2,722)
NET (LOSS) / PROFIT FOR THE YEAR		**(48,650)**	**1,401**
Other comprehensive income			
Revaluation of property and investment property		801	-
Securities available for sale		1	1
Other losses recognised in equity		(3)	-
Income tax relating to components of other comprehensive income		(80)	-
TOTAL COMPREHENSIVE (LOSS) / INCOME FOR THE YEAR		**(47,931)**	**1,402**
(Loss) / earnings per share (in BAM) (Note 27)		(0.383)	0.012

Notes on following pages form an integral part of these financial statements.

Statement of Financial Position

Financial statements for the year ended 31 December 2010 (in 000 BAM)

	Notes	2010	2009 Restated
ASSETS			
Cash and balances with the Central Bank	13	169,699	170,079
Due from other banks	14	28,829	54,185
Loans to customers, net	15	1,243,920	1,347,733
Securities available-for-sale	16	1,080	1,078
Property and equipment	17	49,323	51,030
Intangible assets	18	12,642	6,465
Investment property	19	3,610	3,649
Other assets	20	6,635	10,670
Total assets		**1,515,738**	**1,644,889**
LIABILITIES			
Due to banks and other financial institutions	21	560,964	712,112
Due to customers	22	521,540	547,094
Borrowings	23	150,911	135,873
Subordinated debt	24	35,470	12,000
Other liabilities	25	26,927	23,623
Other provisions	28	8,301	4,306
Total liabilities		**1,304,113**	**1,435,008**
EQUITY			
Share capital	26	175,512	125,837
Share premium	26	64	64
Statutory reserves		74,317	73,855
Revaluation reserves		7,689	7,183
(Accumulated losses) / Retained earnings		(45,957)	2,942
Total equity		**211,625**	**209,881**
Total liabilities and equity		**1,515,738**	**1,644,889**
COMMITMENTS AND CONTINGENT LIABILITIES	28a	**113,008**	**134,296**

Notes on following pages form an integral part of these financial statements.

Management of the Bank has authorized these financial statements for issue on 28 February 2011.

Samuel Vlčan
Director

Goran Babić
Executive Director

Dragan Kovačević
Deputy Director

Statement of Changes in Equity

Financial statements for the year ended 31 December 2010 (in 000 BAM)

	Share capital	Share premium	Statutory reserves	Revaluation reserves	(Accumulated losses)/ Retained earnings	Total
1 January 2009	*120,837*	*64*	*10,143*	*7,414*	*17,280*	*155,738*
Allocation of profit from 2009	-	-	1,886	-	(1,886)	-
Dividends paid	-	-	-	-	(15,004)	(15,004)
Shares issued	5,000	-	-	-	-	5,000
Revaluation of property and investment properties	-	-	-	(230)	230	-
Revaluation of securities available-for-sale	-	-	-	(2)	-	(2)
Change of the deferred tax, net	-	-	-	1	-	1
Net profit for the year 2009	-	-	-	-	2,322	2,322
31 December 2009	**125,837**	**64**	**12,029**	**7,183**	**2,942**	**148,055**
Restatement of comparative information (Note 2.2)	-	-	61,826	-	-	61,826
31 December 2009 (Restated)	125,837	64	73,855	7,183	2,942	209,881
Allocation of profit from 2010	-	-	465	-	(465)	-
Dividends paid						-
Shares issued	49,675	-	-	-	-	49,675
Revaluation of property and investment properties	-	-	-	585	216	801
Revaluation of securities available-for-sale	-	-	-	1	-	1
Other losses	-	-	(3)	-	-	(3)
Net impact of deferred taxes	-	-	-	(80)	-	(80)
Net profit for the year 2010	-	-	-	-	(48,650)	(48,650)
31 December 2010	**175,512**	**64**	**74,317**	**7,689**	**(45,957)**	**211,625**

Notes on following pages form an integral part of these financial statements.

Cash Flow Statement (restated in accordance with the Law on accounting and audit)

Financial statements for the year ended 31 December 2010 (in 000 BAM)

	Note	2010	2009
Cash flows from operating activities			
Interest, fees and commission income from loans to customers		105,074	118,992
Interest expenses		(42,542)	(48,813)
Collected bad debts		9,732	5,559
Cash payments to employees and suppliers		(31,780)	(33,809)
Off-balance sheet payments		(8)	-
Payments in/ out extraordinary items		775	415
Loans and advances to customers		30,740	22,223
Clients' deposits		(152,094)	(294,727)
Paid income taxes		(3,365)	(2,269)
Net cash flows used in operating activities		**(83,468)**	**(232,429)**
Cash flows from investing activities			
Interest received		8	-
Dividends received		114	-
Purchase of securities available for sale		26	(162)
Purchase of intangible assets		(6,819)	(3,233)
Purchase of property and equipment		(1,172)	(3,755)
Purchase of other investments		(255)	205
Net cash flows used in investing activities		**(8,098)**	**(6,945)**
Cash flows from financing activities			
Proceeds from issued shares		49,646	5,000
Interest paid for borrowings		(2,881)	(4,194)
Proceeds from borrowings		26,233	69,182
Repayment of borrowings		(11,350)	(41,463)
Dividend paid		(15)	(14,962)
Net cash flows from financing activities		**61,633**	**13,563**
Net decrease in cash and cash equivalents		**(29,933)**	**(225,811)**
Cash and cash equivalents at beginning of year		**224,131**	**448,133**
Effect of foreign exchange differences		**4,297**	**1,809**
Cash and cash equivalents at end of year	13, 14	**198,495**	**224,131**
Cash and cash equivalents comprise the following balance sheet components:			
Cash and balances with the Central Bank	13	169,699	**170,079**
Due from other banks	14	28,829	**54,185**
Less: interest accrued and provisions		(33)	(133)
		198,495	**224,131**

Notes on following pages form an integral part of these financial statements.

Notes to Financial Statements

For the year ended 31 December 2010

1. General information

Hypo Alpe-Adria-Bank A.D., Banja Luka (the "Bank") is a legal successor of Kristal Banka A.D., Banja Luka which was initially registered as a separate legal entity on 30 September 1992, and subsequently transformed into a shareholders' company on 16 May 1997. Prior to its establishment as an independent bank, the Bank operated as a main branch of Jugobanka Jubanka d.d., Sarajevo, a related party of Jugobanka d.d., Beograd. Based on the decision of the Banja Luka Court (number U/I 2308/03) dated 9 October 2003, the Bank commenced its operations under its current registered name.

The Bank is 99.7131% owned by Hypo Alpe-Adria-Bank International AG, Klagenfurt, Austria, member of the Hypo Alpe-Adria Group. Ultimate parent of the Bank until end 2009 was Bayern LB, Germany. On 30 December 2009, the ultimate parent of the Bank became Republic of Austria, with 100% ownership of Hypo Alpe-Adria-Bank International AG. Please refer to Note 26 for further information.

The Bank is licensed in the Republic of Srpska to perform banking operations related to payment transfers, credit and deposit activities in the country and abroad, and in accordance with the Republic of Srpska banking legislation, it is to operate based on the principles of liquidity, solvency and profitability.

The Bank's registered head office is in Aleja Svetog Save, Banja Luka, Republic of Srpska. As of 31 December 2010, besides the head office located in Banja Luka, the Bank had 41 branch offices situated throughout the entity (31 December 2009: 6 branches, 39 branch offices and 2 sub-branches).

As at 31 December 2010, the Bank had 517 employees (2009: 548).

Management	
Director from 12 August 2010	Samuel Vlčan
Deputy director from 01 October 2010, executive director from 12 August 2010	Dragan Kovačević
Executive director from 12 August 2010	Goran Babić
Deputy director until 30 September 2010, director until 12 August 2010	Srećko Bogunović
Executive director until 12 August 2010	Gerhard Lehner
Supervisory board	
President from 04 November 2010	Dipl. Kfm. MA Rainer Maria Sichert
Vice president from 17 August 2010	Mag. Wolfgang Mösslacher
Member from 17 August 2010	Mag. Patrick Luger
Member from 17 August 2010	Mag. Stephan Holzer
Member from 17 August 2010	Ružica Topić, lawyer
President until 17 August 2010	Anton Knett, MBA
Vice president, until 17 August 2010	Mag. Wolfgang Peter
Member until 17 August 2010, president until 04 November 2010	Dipl. Kfm. Andreas Dorhofer
Member, until 17 August 2010	Mag. Dr. Christoph Schasche
Member, until 17 August 2010	DI. Božidar Špan
Member, until 17 August 2010	Thomas Morgl, MBA
Member, until 17 August 2010	Dr. Guenther Puchtler
Audit Committee	
President	Mag. Dr. Hans-Dieter Kerstnig
Member, until 14 April 2010	Monika Gotownik
Member	Nensi Marin
Member	Zoran Besak
Member	Vesna Pavlović
Member, from 14 April 2010	Danijel Gregorić

1. General information (continued)

1.1. Financial crisis impact

Recent volatility in global and Bosnia and Herzegovina financial markets

The ongoing global liquidity crisis which commenced in the middle of 2007 and escalated mid 2008, has resulted in, among other things, a lower level of capital market funding, lower liquidity levels across the banking sector, and, at times, higher interbank lending rates and very high volatility in stock markets. The uncertainties in the global financial markets have also led to bank failures and bank rescues in the United States of America, Western Europe, Russia and elsewhere. Indeed the full extent of the impact of the ongoing economic crisis is proving to be impossible to anticipate or completely guard against.

Management believes it is taking all the necessary measures to support the sustainability and growth of the Bank's business in the current circumstances, including the further deterioration of liquidity.

Impact on liquidity

Throughout 2010 the liquidity of banks was stable. Foreign debt has gradually decreased, while the local source of funding gradually increased. As on the other side there was no significant credit activity, the Bank's liquidity position was satisfactory during the year.

Impact on customers/borrowers

Implementation of a new loan process has had a significant impact on limiting and monitoring existing risks. By improving the loan process, impact on customers/ borrowers has been reduced to an optimized level, through the introduction of new standards related to client assessment. Debtors or borrowers of the Bank may be affected by the lower liquidity situation which could in turn impact their ability to repay the amounts owed. Deteriorating operating conditions for customers or borrowers may also have an impact on management's cash flow forecasts and assessment of impairment of financial and non-financial assets. To the extent that information is available, management has properly reflected revised estimates of expected future cash flows in their impairment assessments. The structure of Bank sources provides sufficient reserves for significant restructuring/ prolongation of the existing exposures towards clients.

Impact on collateral (especially real estate)

The amount of provision for impaired loans is based on management's estimate as of the balance sheet date after taking into consideration cash flows that may result from foreclosure of collateral, decreased for costs of obtaining and selling the collateral. The local market for many types of collateral, especially real estate, has been severely affected by the recent volatility in global financial markets resulting in a lower level of liquidity for certain types of assets. As a result, actual realizable value of collateral may differ from the value used for the purpose of estimating impairment allowances. The Bank performs a periodical evaluation of collaterals, in order to ensure that provisions are accurately estimated. The calculation process takes into account the current value of the collateral, applying the discounting method..

Fair value of financial assets and liabilities (excluding financial assets and liabilities directly related to the credit crisis, for example mortgage used as a guarantee)

Fair value of quoted investments in active markets is based on current bid prices (financial assets) or offer prices (financial liabilities). If there is no active market for a financial instrument, the Bank establishes fair value using different valuation techniques. These include the use of recent arm's length transactions between willing parties, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants. The valuation models reflect current market conditions at the measurement date which may not be representative of market conditions either before or after the measurement date. As of the balance sheet date management has reviewed its models to ensure they appropriately reflect current market conditions, including the relative liquidity of the market and credit spreads.

1. General information (continued)

Valuation of investment property at fair value
Many types of real estate have been severely affected by the recent volatility in global financial markets.

Fair value of land and buildings measured at revaluated amounts in accordance with IAS 16 has been updated to reflect market conditions at sufficient frequency to ensure that the carrying value does not differ significantly from the fair value at the end of reporting period.

In accordance with IAS 40, fair value of investment property is the price at which the property could be exchanged between knowledgeable, willing parties in an arm's length transaction. A 'willing seller' is not a forced seller prepared to sell at any price, nor someone who is ready to wait for the price that is not reasonable under the given market conditions. The best evidence of fair value is given by current prices in an active market for similar property in the same location and condition.

If, in exceptional cases, there is clear evidence that when the Bank first acquires an investment property (or when an existing property first becomes investment property following the completion of construction or development, or after a change in use) the fair value of the investment property is not reliably determinable on a continuous basis, then the Bank measures that investment property using the cost model in accordance with IAS 16.

The cost of an item of property, plant and equipment comprises:

- its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates.
- any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.
- the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period.

Examples of directly attributable costs are:

- costs of employee benefits (as defined in IAS 19 Employee Benefits) arising directly from the construction or acquisition of the item of property, plant and equipment;
- costs of site preparation;
- initial delivery and handling costs;
- installation and assembly costs;
- costs of testing whether the asset is functioning properly, after deducting the net proceeds from selling any items produced while bringing the asset to that location and condition (such as samples produced when testing equipment); and
- professional fees.

2. Basis for preparation and presentation of the financial statements and the accounting method

2.1. Basis for preparation and presentation of financial statements

These financial statements have been prepared under the Law on Accounting of the Republic of Srpska (Official Gazette of the Republic of Srpska, no. 36/09).

Based on the Law on Accounting and Auditing of the Republic of Srpska, standards applied in the Republic of Srpska are International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS), which are translated to Serbian language by the authorized accounting body.

The Bank applies all the IFRS and the amendments and interpretations which were published by the International Federation of Accountants (IFAC) and the International Accounting Standards Board (IASB) and translated into Serbian in the Republic of Srpska ("RS") as of 31 December 2008.

2. Basis for preparation and presentation of financial statements and the accounting method (continued)

The Bank's financial statements as of 31 December 2010 and 31 December 2009 have been prepared in accordance with the Article 14 of the Law on Banks of Republic of Srpska (Official Gazette of the Republic of Srpska, no. 44/03) and decisions of the Banking Agency of Republic of Srpska (BARS).

The Bank has not applied the following standards, amendments and interpretations, which are effective, not translated in the Republic of Srpska and not relevant for the Bank's operations:

- IFRS 3 (revised), 'Business combinations', and consequential amendments to IAS 27, 'Consolidated and separate financial statements', IAS 28, 'Investments in associates', and IAS 31, 'Interests in joint ventures', are effective prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009.
- IFRIC 17, 'Distributions of non-cash assets to owners', effective for annual periods beginning on or after 1 July 2009. This is not currently applicable to the Bank, as it has not made any non-cash distributions.
- IFRIC 18, 'Transfers of assets from customers', effective for transfer of assets received on or after 1 July 2009. This is not relevant to the Bank, as it has not received any assets from customers.
- IFRIC 19 'Extinguishing financial liabilities with equity instruments'.
- 'Additional exemptions for first-time adopters' (Amendment to IFRS 1) was issued in July 2009. The amendments are required to be applied for annual periods beginning on or after 1 January 2010.
- Improvements to International Financial Reporting Standards 2009 were issued in April 2009. The effective dates vary standard by standard but most are effective 1 January 2010.

The Bank has not early adopted the following standards, amendments and interpretations, which are not yet effective, nor translated in the Republic of Srpska:

- IFRS 9, 'Financial instruments', issued in December 2009. This addresses the classification and measurement of financial assets and is likely to affect the Bank's accounting for its financial assets. The standard is not applicable until 1 January 2013 but is available for early adoption. The Bank has not yet decided when to adopt IFRS 9.
- Revised IAS 24, 'Related party disclosures', issued in November 2009. It supersedes IAS 24, 'Related party disclosures', issued in 2003. The revised IAS 24 is required to be applied from 1 January 2011. Earlier application, in whole or in part, is permitted.
- 'Classification of rights issues' (Amendment to IAS 32), issued in October 2009. For rights issues offered for a fixed amount of foreign currency, current practice appears to require such issues to be accounted for as derivative liabilities. The amendment states that if such rights are issued pro rata to all the entity's existing shareholders in the same class for a fixed amount of currency, they should be classified as equity regardless of the currency in which the exercise price is denominated. The amendment should be applied for annual periods beginning on or after 1 February 2010. Earlier application is permitted.
- 'Prepayments of a minimum funding requirement' (Amendments to IFRIC 14), issued in November 2009. The amendments correct an unintended consequence of IFRIC 14, 'IAS 19 – The limit on a defined benefit asset, minimum funding requirements and their interaction'. Without the amendments, entities are not permitted to recognise as an asset some voluntary prepayments for minimum funding contributions. This was not intended when IFRIC 14 was issued, and the amendments correct the problem.

The amendments are effective for annual periods beginning 1 January 2011. Earlier application is permitted. The amendments should be applied retrospectively to the earliest comparative period presented.

- IFRIC 19, 'Extinguishing financial liabilities with equity instruments'. This clarifies the requirements of IFRSs when an entity renegotiates the terms of a financial liability with its creditor and the creditor agrees to accept the entity's shares or other equity instruments to settle the financial liability fully or partially. The interpretation is effective for annual periods beginning on or after 1 July 2010. Earlier application is permitted.

2. Basis for preparation and presentation of financial statements and the accounting method (continued)

- Improvements to International Financial Reporting Standards 2010 were issued in August 2009 and May 2010. The effective dates vary standard by standard but most are effective 1 January 2010.

The preparation of financial statements under IFRS requires the use of certain critical accounting estimates. It also requires the management to uses estimates in the process of applying the Bank's accounting policies (Note 4).

The financial statements of the Bank are presented in Convertible Marks (BAM) thousand.

The financial statements of the Bank are prepared in accordance with the accounting policies disclosed in Note 3 to the financial statements.

2.2. Comparative information

In the Republic of Srpska, based on new regulation effective starting from 01 January 2010, bookkeeping records and financial statements are required to be in accordance with the International Financial Reporting Standards/International accounting standards as adopted in the Republic of Srpska.

The principal change relates to implementation of IAS 39 – Financial instruments: Recognition and Measurement, when calculating risk provisions. The Bank is required to show net assets (risk provisions are deducted from gross assets), whereas in prior periods risk provisions were reported in liabilities, under provisions. Additionally in accordance with the requirements of IAS 32 – Financial instruments: Presentation, the Bank discloses financial instruments together with related interests and fees.

In the table below adjustments were made for provisions in accordance with IAS 39 as well as reclassification of accrued fees related to off-balance sheet operations from interest to fee income.

Income statement

	Note	2009	Restatement	2009 Restated
Interest income		111,066	(1,081)	109,985
Interest expense		(49,938)	-	(49,938)
Net interest income	7	61,128	(1,081)	60,047
Fee and commission income		10,991	1,081	12,072
Fee and commission expense		(2,626)	-	(2,626)
Net fee and commission income	8	8,365	1,081	9,446
Foreign exchange gains, net		1,808	-	1,808
Other operating income	9	9,487	(2,745)	6,742
Other operating expenses	10	(40,066)	-	(40,066)
Impairment losses	11	(35,678)	1,824	(33,854)
Profit before tax		5,044	(921)	4,123
Income tax expense	12	(2,722)	-	(2,722)
Net profit for the year		2,322	(921)	1,401

2. Basis for preparation and presentation of financial statements and the accounting method (continued)

Statement of financial position (balance sheet)

	Notes	2009	Restatement	2009 Restated
ASSETS				
Cash and balances with the Central Bank	13	170,015	64	170,079
Due from other banks	14	54,117	68	54,185
Loans to customers, net	15	1,363,566	(15,833)	1,347,733
Securities available-for-sale	16	1,078	-	1,078
Property and equipment	17	51,030	-	51,030
Intangible assets	18	6,465	-	6,465
Investment property	19	3,649	-	3,649
Other assets	20	16,163	(5,493)	10,670
Total assets		1,666,083	(21,194)	1,644,889
LIABILITIES				
Due to banks and other financial institutions	21	711,692	420	712,112
Due to customers	22	544,324	2,770	547,094
Borrowings	23	135,678	195	135,873
Subordinated debt	24	12,000	-	12,000
Other liabilities	25	28,862	(5,239)	23,623
Other provisions	28	85,472	(81,166)	4,306
Total liabilities		1,518,028	(83,020)	1,435,008
EQUITY				
Share capital	26	125,837	-	125,837
Share premium	26	64	-	64
Statutory reserves		12,029	61,826	73,855
Revaluation reserves		7,183	-	7,183
Retained earnings		2,942	-	2,942
Total equity		**148,055**	**61,826**	**209,881**
Total liabilities and equity		**1,666,083**	**(21,194)**	**1,644,889**
COMMITMENTS AND CONTINGENT LIABILITIES	28a	**134,296**	**-**	**134,296**

In addition to adjustments for IAS 39 and IAS 32, provisions in accordance with IAS 37 – Provisions, contingent liabilities and contingent assets, were reclassified from Other liabilities to Other provisions.

3. Summary of significant accounting policies

3.1 Basis for measurement

These financial statements have been prepared under the historical cost convention, as modified by the revaluation of buildings, securities held for trading at fair value through profit or loss and available for sale securities.

3.2 Interest income and expense

Interest income and expense for all interest-bearing financial instruments are recognised within interest income and interest expense in the income statement.

Interest income and expense are accounted for on an accrual basis.

Fee and commission income except for loan origination fees are recognized in full when earned.

Fees relating to loan origination are deferred and amortized over the life of the loan using the effective interest rate method.

The effective interest rate method is a method that calculates the costs of repayment of financial assets or financial liabilities and the costs of recognition of income or interest expense over a period. The effective interest rate is the rate that precisely discounts estimated future payments or receipts through the expected life of the financial instruments or, when appropriate, in shorter period to the net carrying value of financial assets or financial liabilities. When effective interest rate is calculated, the Bank estimates cash flows considering all contractual terms of the financial instrument (for example, the possibility of paying in advance), but does not consider future credit losses. The calculation includes all fees and amounts paid or received between two parties that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

3.3 Fee and commission income and expense

Fees and commissions are generally recognised on an accrual basis when due for collection i.e. when the service has been provided.

Fee and commission income relate to local payments and international payments operations, income from off balance sheet operations (issuing guarantees), brokerage and dealing operations etc.

Fee and commission expenses relate to fees paid to the Central Bank of Bosnia and Herzegovina for the local payments operations, SWIFT costs, costs of card business, fees paid to the Banking agency of Republic of Srpska for supervision of the banking sector and other fees (Note 8b).

3.4 Foreign currency translation

a) Functional and presentation currency

Items included in the financial statements are measured using the currency of the primary economic environment in which the Bank operates (‘the functional currency’).

The financial statements are presented in BAM which is the Bank’s functional and presentation currency.

b) Transactions and balances

Transactions denominated in foreign currencies are translated into BAM at official rates prevailing at the date of each transaction. Assets and liabilities denominated in foreign currencies on the balance sheet date are translated into BAM by applying official rates of exchange valid on that date. Contingent liabilities denominated in foreign currencies are translated into BAM at official exchange rates prevailing at the Statement of financial position date.

Foreign exchange gains or losses arising from translation are credited or charged to the income statement. The Bank does not have monetary securities denominated in foreign currency.

3. Summary of significant accounting policies (continued)

Exchange rates used in these financial statements are official rates established by the Central Bank of Bosnia and Herzegovina. On 31st of December the following exchange rates were used:

Exchange rate:	2010 BAM	2009 BAM
USD	1.472764	1.364088
EUR	1.955830	1.955830
CHF	1.567800	1.314600

3.5 Property and equipment

Property and equipment are carried at their fair value, as determined by certified appraisers, subsequently decreased by the accumulated depreciation.

A revaluation of the Bank's property was performed by an independent certified appraiser on 31 December 2010 based on the assets' market value for existing use. Revaluations are performed with sufficient regularity such that the carrying amount of the asset does not materially differ from that which is determined by applying the principle of fair value at the balance sheet date.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Increases in the carrying amount arising on revaluation of buildings and equipment are credited to equity as revaluation reserve. The increase is recognised in the income statement only to the extent that it reverses a revaluation decrease of the same asset previously recognised in profit or loss. If an asset's carrying amount is decreased as a result of a revaluation, the decrease is recognised in the income statement. The decrease is debited directly to revaluation reserve within equity to the extent of any credit balance existing in the revaluation surplus in respect of that asset.

Revaluation reserves included in equity in respect of property and equipment are transferred directly to retained earnings when the asset is derecognised. This may involve transferring the whole of the surplus when the asset is retired or disposed of.

Land is not depreciated. Depreciation on other assets is calculated using the straight - line method to allocate their cost or revaluated amounts to their residual values over their estimated useful lives:

	31 December 2010 and 2009
Buildings	35 to 75 years (1.33% - 2.86%)
Computer equipment	5 to 8 years (12.5% - 20%)
Furniture and other equipment	3 to 15 years (6.67% - 33.33%)
Vehicles	4 to 5 years (20% - 25%)

The Bank's management believes that depreciation rates applied fairly reflect the economic useful life of property and equipment.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within gains or losses from sale of property and equipment.

3. Summary of significant accounting policies (continued)

3.6 Intangible assets

Intangible assets include computer software and licenses. The initial cost of acquisition of assets is recognized as an asset and amortized on a straight-line basis, as follows:

	31 December 2010 and 2009
Intangible assets	5 to 7 years (14.29% - 20%)

3.7 Investment property

Investment property, which is property, held to earn rentals is carried at fair value, as determined by certified appraisers, subsequently decreased by the accumulated depreciation. The cost of purchased investment property comprises its purchase price, and any directly attributable expenditure.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within gains or losses from sale of investment property.

3.8 Impairment of non-financial assets

Assets that are subject to 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.

3.9 Financial assets

The Bank classifies allocates financial assets into the following categories: financial assets at fair value through profit or loss; loans and receivables; held-to-maturity investments; and available-for-sale financial assets. Management determines the classification of financial instruments at initial recognition.

As of 31 December 2010 and 2009, the Bank has only loans and receivables and available-for-sale financial assets.

a) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

b) Financial assets available for sale

Financial assets available for sale are those assets where intention is to be held for undefined period that can be sold in line with need for liquidity or changes in interest rate, exchange rates or change in price of capital.

c) The accounting treatment

Regular purchases and sales of financial assets at fair value through profit or loss, assets held to maturity and the assets available for sale are recognized on the transaction date and the date on which the Bank commits to purchase or sell the asset. Investments are initially recognized at fair value increased by transaction costs for all financial assets not carried at fair value through profit or loss. Financial resources are derecognised from the books at a time when the Bank has transferred substantially all the risks and rights arising from ownership or when the expiration of the right bank to receive cash flows arising from financial assets.

3. Summary of significant accounting policies (continued)

Available-for-sale financial assets are subsequently recognised at fair value. Loans and receivables are measured at amortised cost using the effective interest rate method. Gain or loss rising from change of fair value of available-for-sale financial assets, are directly stated in equity, until their disposal or impairment charges, when the cumulative income or expense previously recognized in equity is recognized in the statement of comprehensive income. However, interest calculated using the effective interest method, is recognised in the statement of comprehensive income. Dividends are recognised in the statement of comprehensive income when the entity's right to receive payment is established.

The fair value of securities that are listed are based on current bid prices. If the market for a financial asset (the market of securities which are not listed) is not active, the Bank establishes fair value by assessment techniques. It involves the application of recent transactions between independent parties, reference to other instruments that are substantially the same, discounted cash flow analysis and other valuation techniques.

Impairment of financial assets

a) Assets carried at amortized cost

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. The criteria that the Bank uses to determine that there is objective evidence of an impairment loss include:

- delays in payment of the agreed repayment of principal or interest;
- if the borrower has difficulty with cash flow (capital indicators, the percentage of net sales);
- violation of contractual obligations;
- initiating bankruptcy proceedings;
- deterioration of the competitive position of the debtor;
- decrease in value of collateral.

The estimated period between a loss occurring and its identification is determined by local management for each identified portfolio. In general, the periods used vary between three months and twelve months; in exceptional cases, longer periods are warranted.

The Bank first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

The amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the consolidated income statement.

The calculation of the present value of the estimated future cash flows of a collateralized financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (that is, on the basis of the Bank's grading process that considers asset type, industry, geographical location, collateral type, past-due status and other relevant factors). Those characteristics are relevant to the estimation of future cash

3. Summary of significant accounting policies (continued)

flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the Bank and historical loss experience for assets with credit risk characteristics similar to those in the Bank. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not currently exist.

Estimates of changes in future cash flows for groups of assets should reflect and be directionally consistent with changes in related observable data from period to period (for example, changes in unemployment rates, property prices, payment status, or other factors indicative of changes in the probability of losses in the Bank and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Bank to reduce any differences between loss estimates and actual loss experience.

When a loan is uncollectible, it is written off against the related allowance for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the consolidated income statement.

Estimation of potential losses for financial assets in accordance with the requirements of the Banking Agency of the Republic of Srpska
In accordance with the Decision of the Banking Agency of the Republic of Srpska classification of assets and off balance sheet items according to the degree of collectability, the Bank is required to classify loans, placements and other balance sheet and off-balance sheet exposure to the Bank's risk in categories A, B, C, D and E in accordance with the assessment of recoverability of loans and other placements based on the timeliness of settling the obligation of the debtor, debtor's financial position and collateral receivables. Estimated amount of reserves for potential losses were calculated using the following percentages: 2% on loans classified as category A, 5% - 15% of the loans in category B, 16% - 40% on loans in category C, 41 - 60% on loans in category D and 100% placements in category E.

The difference between allowances determined in the manner disclosed in Note 3.9 and estimated provisions for potential losses on loans classified into categories described above, is recorded in the provision account, included in statutory reserves, in equity and allocation of these provisions is made from retained earnings up to the level of retained earnings. A Bank cannot use these provisions to cover losses, but must disclose a shortfall. As of 31 December 2010, the Bank's current period loss does not exceed the amount of provisions included in Bank's reserves (please see Statement of changes in equity).

b) Assets available for sale
The Bank assesses at each date of the statement of financial position whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity investments classified as available for sale, a significant or prolonged decline in the fair value of the security below its cost is objective evidence of impairment resulting in the recognition of an impairment loss. If any such evidence exists for available for sale 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 consolidated income statement. Impairment losses recognised in the consolidated income statement on equity instruments are not reversed through the consolidated income statement. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the consolidated income statement.

3. Summary of significant accounting policies (continued)

3.10 Investment in associates and other equity investments

Associated entities are those legal entities in which the Bank has a significant influence, and which are neither dependant entities nor joint investments. Investment in an associate is initially recognized at cost (purchase price) and on the balance date.

3.11 Cash and cash equivalents

For purposes of the cash flow statement, cash, balances with the Central Bank, foreign currency accounts with foreign and domestic banks and term deposits up to 90 days held with foreign and domestic banks are all considered to be cash equivalents.

3.12 Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowing using the effective interest method.

3.13 Provisions

Provisions for restructuring costs and legal claims are recognized when:

- the Bank 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;
- the amount has been reliably estimated.

Where there is a number of similar obligations, the likelihood that an outflow will be required in a settlement is determined by considering the class of obligations as a whole. A provision is recognized 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.

3.14 Employee benefits

Short-term employee benefits

Short-term benefits include salaries and all contributions for employees, paid to the Republic of Srpska Social Security and Pensions Funds, and calculated by applying the specific percentages stipulated under relevant regulations. Short term employee benefits are recognized as expense in the period in which they were incurred.

Retirement benefits and vacation entitlement

According to the Collective Agreement with the Bank's employees, employees are entitled to receive benefits upon retirement. The retirement benefit obligation recognized in the balance sheet represents the present value of the defined benefit obligations as determined by actuarial calculations.

Provisions for retirement benefits and vacation entitlement are disclosed in the balance sheet within "Other liabilities".

Retirement benefits provisions are based on actuarial reports and are used only for the purposes they are designated. At the end of each year, an assessment of appropriateness of the amounts of provisions for retirement benefits and vacation entitlements is performed. Additional provision or release of provision is recognized in the income statement, under "Other operating income" or "Other operating expenses".

Benefits falling due more than 12 months after the balance sheet date are discounted to their present value.

3.15 Income taxes

Current income tax

Income tax is calculated in accordance with the tax regulations of the Republic of Srpska. From 1 January 2007, income tax is calculated and paid according to the new Law on Corporate Income Tax (Official Gazette of Republic of Srpska no. 91/06) and

3. Summary of significant accounting policies (continued)

Regulations on Corporate Income Tax Law Application (Official Gazette of Republic of Srpska no. 129/06, 110/07 and 114/07). Estimated monthly advance payments of income tax are calculated based on prior year tax return.

The final statutory tax basis, upon which a 10% income tax rate is applicable, is determined based on the taxable balance. Income tax presented in the taxable balance is calculated based on the profit for the period, presented in the statutory income statement, together with any adjustments for permanent differences made thereto, as defined by the Law.

Deferred income taxes

Deferred income taxes are calculated on all temporary differences between tax base of assets and liabilities and their carrying amounts in financial statements of the Bank. Deferred tax liabilities are recognized for all taxable temporary differences between tax base of assets and liabilities at balance sheet date and carrying values reported in the financial statements, which will result in taxable amounts for following periods.

Deferred tax assets are calculated for all deductable temporary differences, unused tax assets and unused tax losses up to the amount for which it is likely to be used by future taxable income for realization of deductible temporary differences, unused tax assets and unused tax losses.

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

Current and deferred taxes are recognized as income and expense and are included in net profit for the period.

3.16 Share capital and reserves

Share capital consists of ordinary shares. Share capital is stated in BAM at nominal value.

Dividends from shares are recognized as liabilities in the period in which a decision on dividend distribution is made.

3.17 Revaluation reserves

Revaluation surpluses are credited to revaluation reserves (Note 3.5). The revaluation surplus included in equity in respect of property and equipment is transferred directly to retained earnings in the amount which represents the difference between the depreciation charge before and after the appraisal. However, the increase is recognized in profit or loss to the extent that is reverses a revaluation decrease of the same asset previously recognized in profit or loss. The revaluation deficit is charged to revaluation reserves accumulated for that particular asset, whereas upon sale and disposal of items of property and equipment, the outstanding balance of appraisal surplus included in the revaluation reserves, is entirely transferred to retained earnings.

3.18 Fair value

The accompanying financial statements are prepared on a historical cost basis, including adjustments and provisions made to reduce assets to their estimated recoverable amounts.

It is the policy of the Bank to disclose the fair value information of those financial assets and financial liabilities for which published market information is readily and reliably available, and whose fair value is materially different from their recorded amounts. Sufficient market experience, stability and liquidity do not exist for the purchase and sale of loans and other financial assets or liabilities, given that published market information is not readily available. Hence, fair value cannot reliably be determined.

3.19 Related party transactions

According to IAS 24 related parties are parties that represent:

- The parties which directly, or indirectly through one or more intermediaries, control are controlled by, or is under common control with, the entity;
- Parties in which the Bank has an interest in the entity that gives it significant influence over the entity and that are neither related parties nor joint investment;

3. Summary of significant accounting policies (continued)

- Private individuals who directly or indirectly have voting power in the Bank that gives them significant influence over the Bank, or any other subject which is expected to influence or be influenced by a related party to the Bank;
- Members of the key management personnel i.e. individuals with authorizations and responsibilities for planning, managing and controlling the Bank's operations, including directors and key management.

When taking into account each possible transaction with a related party, attention is focused on basis of relationship not just legal form (Note 29).

3.20 Custody operations

Assets and income arising from operating activities, where the Bank performs custody operations, which include holding or keeping the funds for the benefit of individuals, creditors and other institutions are included in Bank's financial statements.

3.21 Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments.

A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns different from those of segments operating in other economic environments.

The Bank is monitoring its performance by business segments (public, retail, corporate) and by geographical segments (branches) for Group controlling purposes and such reports do not reconcile with the financial statements presentation. Therefore the Bank does not disclose segment reporting.

4. Critical accounting estimates and judgements

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgments are continually evaluated and based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Impairment losses on loans, deposits with other banks and other risk-weighted assets and off-balance sheet items

The Bank reviews its loan portfolio and other risk-weighted assets and off-balance sheet items to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the income statement, the Bank makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans and guarantees before the decrease can be identified with an individual exposure in that portfolio. The methodology and assumptions used for estimating impairment provision in accordance with BARS regulations is disclosed in Note 3.9.

Retirement benefits

Expenses for long-term provisions related to the future outflows regarding retirement of employees are assessed based on the actuarial calculation done in accordance with IAS 19. For the purposes of the assessment, the Bank engages a certified actuary, who performs the calculation based on the data from HR department of the Bank based on the estimated time of employees' retirement. The present value of the future liabilities is calculated by applying a discount rate. These provisions are only used to settle expenses that they have originally been formed for. At the end of each year the Bank assesses these provisions. If the amount recorded is higher / lower than estimated amount, the difference is released through profit or loss.

4. Critical accounting estimates and judgements (continued)

The certified actuary has performed a new actuarial calculation during 2010 in accordance with IAS 19. Following the new calculation the Bank has decreased previously recognised provisions by crediting the income statement. An assessment of short term provisions for unused annual holidays is done in accordance with the number of days of unused annual holidays as of balance sheet date and the average monthly employee's gross salary.

Litigations
The Bank's management assesses the amount of provisions for outflows based on the litigations. The assessment is based on the estimated probability of future cash outflows, arising from the past contractual or legal obligation (Note 28c).

Income taxes
The Bank is subject to income taxes in the Republic of Srpska and Bosnia and Herzegovina. The Bank recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions.

Deferred tax assets disclosed at 31 December 2010 are based on assumptions about the profitability for the period of the next five years. In the case of a change in assumptions about profitability, adjustment of disclosed tax assets can occur.

5. Financial risk management

Risk management strategy of the Bank is to maintain stable performance in the future. The Bank applies policies and strategies of credit and market risk. The Bank controls a variety of risks with respect to the data structure, methodology adopted, reporting and limits arising in the decision making process. The Bank has an internal risk management model. The most important tools and methods used in the model for internal risk management are: internal credit rating system (for Corporate, Retail and Banks), collaterals, internal indicators in respect of provision / bad debts, etc. The use of risk management has a large impact on asset quality, structural liquidity, efficiency ratios and early warnings, and it reduces exposure to all types of risks.

The Bank is exposed to the following major types of risks: credit risk, market risk, liquidity risk, operational risk.

a) Credit risk management
The Bank is exposed to credit risk which is the risk that a counterparty will be unable to pay amounts in full when due. The Bank structures the levels of credit risk it undertakes by identifying possible level of credit loss, i.e. general credit risk and potential credit loss.

Assessment of impairment losses is performed for both individual borrowers and groups of related-party borrowers. Such risks are monitored on a continuous basis in accordance with the internal programs and policies, as well as BARS regulations.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing lending limits where appropriate. This is done in accordance with set procedures for credit approval, additional lending, investment activities, and assessment of potential out-of-balance liabilities. Exposure to credit risk is also managed in part by reduction of all kinds of possible risk sources related to quality, concentration, guarantees of payment (all loans are insured with collaterals and corporate and personal guarantees), maturity and currency.

On 1 October 2009, the Bank has established a new department – Department for credit risk management, dedicated to risk monitoring for Corporate and Retail clients, as defined by the Hypo Alpe Adria Group ("HGAA" or the "Group") policies. By introducing new policies and establishing a new department, the Bank managed to put in place clearer and more strictcriteria for new financing granted. The Bank has also increased the level of awareness of its employees related to continuous

5. Financial risk management (continued)

monitoring of clients, early risk identification and steps taken to address the risk. In order to increase the quality of credit risk assessment, responsibility for credit risk monitoring was delegated to an individual level (not only the credit committee level).

The Bank approves loans in accordance with a defined process for loan approval, and based on the creditworthiness of clients and security instruments.

Creditworthiness of a borrower must be presented in the document "Loan proposal" based on which lending decisions are made. Loan proposal has to include the assessment of Market department and Risk management department.

Loan decisions are made based on limits defined at the Group level.

There are eight levels of authority for approving the placements of which the highest is Supervisory Board of the Parent (HBInt). Department for credit risk management has the right to vote in each committee.

In order to ensure business activities, and on the basis of assessed risk of potential losses, the Bank performs the calculation of provisions, based on risk exposure arising from loans and off-balance sheet receivables. The level of provision is determined by the degree of placement risk.

System of Corporate clients ranking
Rating system in the Bank (as in the whole Group) must be presented in accordance with the rating system of the Group (five rating classes and five levels within the class.). All internal ratings count one-year probability of default (PD) based on a weighted average of the following risk parameters:

- financial indicators (hard facts)
- sector and management (soft facts)

In addition, other factors such as the regularity of settlement of liabilities, assessment of creditworthiness affect the final client rating.

Client rating is calculated for each loan request. After the initial calculation, the rating of the client is updated based on annual client monitoring (at least once a year).

Maximum exposure to credit risk is as follows:

	2010	2009
Cash and balances with the Central Bank	169,699	170,079
Due from other banks, net	28,829	54,185
Loans to customers, net	1,243,920	1,347,733
Securities available-for-sale	1,080	1,078
Other financial assets, net	4,908	4,109
	1,448,436	**1,577,184**

5. Financial risk management (continued)

Loans to customers, net and due from other banks are summarised as follows:

	Banks	Financial institutions	Corporate	Retail	Government	Total
31 December 2010						
Not past due	28,831	3,859	303,472	445,296	80,633	862,091
Past due between 1 and 90 days	-	-	114,271	91,268	-	205,539
Past due over 90 days	-	-	314,654	61,354	-	376,008
Gross	**28,831**	**3,859**	**732,397**	**597,918**	**80,633**	**1,443,638**
SRP	(2)	-	(122,975)	(12,200)	-	(135,177)
PRP	-	(111)	(10,754)	(24,767)	(80)	(35,712)
Less: allowance for impairment	**(2)**	**(111)**	**(133,729)**	**(36,967)**	**(80)**	**(170,889)**
Net	**28,829**	**3,748**	**598,668**	**560,951**	**80,553**	**1,272,749**

	Banks	Financial institutions	Corporate	Retail	Government	Total
31 December 2009						
Not past due	54,189	7,110	341,569	473,089	86,639	962,596
Past due between 1 and 90 days	-	-	190,174	94,582	-	284,756
Past due over 90 days	-	-	218,064	38,218	-	256,282
Gross	**54,189**	**7,110**	**749,807**	**605,889**	**86,639**	**1,503,634**
SRP	(4)	-	(77,705)	(5,482)	-	(83,191)
PRP	-	(113)	(8,464)	(9,946)	(2)	(18,525)
Less: allowance for impairment	**(4)**	**(113)**	**(86,169)**	**(15,428)**	**(2)**	**(101,716)**
Net						
	54,185	**6,997**	**663,638**	**590,461**	**86,637**	**1,401,918**

Exposure to credit risk from loans to customers, net and due from other banks per rating is as follows:

	Banks		Corporate		Retail		Total	
	Gross	Risk provision	Gross	Risk provision	Gross	Risk provision	Gross	Risk provision
31 December 2010								
No rating	84	-	22,078	(19,381)	397	(324)	22,559	(19,705)
1A – 1E	953	-	-	-	-	-	953	-
2A – 2E	27,188	-	13,629	(101)	7	-	40,824	(101)
3A – 3E	374	-	233,079	(1,391)	538,875	(18,917)	772,328	(20,308)
4A – 4E	232	(2)	142,528	(1,655)	1,580	(56)	144,340	(1,713)
5A – 5E	-	-	405,565	(111,384)	57,069	(17,678)	462,634	(129,062)
Total	**28,831**	**(2)**	**816,879**	**(133,912)**	**597,928**	**(36,975)**	**1,443,638**	**(170,889)**
Total (net)		**28,829**		**682,967**		**560,953**		**1,272,749**

5. Financial risk management (continued)

	Banks		Corporate		Retail		Total	
	Gross	Risk provision	Gross	Risk provision	Gross	Risk provision	Gross	Risk provision
31 December 2009								
No rating	88	-	22,533	(19,406)	361	(329)	22,982	(19,735)
1A – 1E	40,107	(1)	-	-	-	-	40,107	(1)
2A – 2E	12,618	(1)	25,178	(249)	2	-	37,798	(250)
3A – 3E	933	(1)	242,915	(3,132)	391,400	(2,343)	635,248	(5,476)
4A – 4E	443	(1)	262,348	(2,480)	133,926	(1,548)	396,717	(4,029)
5A – 5E	-	-	290,540	(61,017)	80,242	(11,208)	370,782	(72,225)
Total	**54,189**	**(4)**	**843,514**	**(86,284)**	**605,931**	**(15,428)**	**1,503,634**	**(101,716)**
Total net		**54,185**		**757,230**		**590,503**		**1,401,918**

Provisions for impairment and provisioning policy

Impaired loans and securities are those loans and securities for which the Bank determines that it is not likely it will be able to collect all principal and accrued interest under the provisions of the loan agreement / securities. Individually impaired assets are those assets that are individually assessed to have been impaired and have estimated losses recognized.

The Bank assesses impairment of receivables for incurred losses in the credit portfolio.

Classification of receivables is based on an analysis of delays in settlement of obligations and indicators of return.

In the case of single loan impairment, future estimated cash flows are discounted in accordance with the requirements of IAS 39, to arrive at an appropriate amount of provision.

Impairment policy

Impairment policy is managed very carefully with previous analysis of pricing options, where the Bank has estimated that the collection of receivables is not possible. Impairment proposal is given by the department in charge of the client at any time by the assessment that some receivables are uncollectible. Final write-off of receivables is the responsibility of the Management Board and Supervisory Board, depending on the write-off amount.

5. Financial risk management (continued)

The following table presents maximum credit risk exposure for on-balance items:

	Total carrying value	Without impairment	Individual impairment (SRP)	Collective impairment (PRP)	Total net carrying value
31 December 2010					
Cash and balances with the Central Bank	169,699	169,699	-	-	169,699
Due from other banks	28,831	27,269	(2)	-	28,829
Loans to customers, net	1,414,807	363,791	(135,175)	(35,712)	1,243,920
Securities available-for-sale	1,080	1,080	-	-	1,080
Other financial assets	6,305	4,125	(1,377)	(20)	4,908
	1,620,722	**565,964**	**(136,554)**	**(35,732)**	**1,448,436**
31 December 2009					
Cash and balances with the Central Bank	170,079	170,079	-	-	170,079
Due from other banks	54,189	18,999	(4)	-	54,185
Loans to customers, net	1,449,445	562,622	(83,187)	(18,525)	1,347,733
Securities available-for-sale	1,078	1,078	-	-	1,078
Other financial assets	5,518	3,384	(1,409)	-	4,109
	1,680,309	**756,162**	**(84,600)**	**(18,525)**	**1,577,184**

Loans to customers, net with impairment provisions are as follows:

	Loans to customers, gross	Impairment	Loans to customers, net
31 December 2010			
Portfolio risk provision (PRP)	1,044,470	(35,712)	1,008,758
Specific risk provision (SRP)	370,337	(135,175)	235,162
	1,414,807	**(170,887)**	**1,243,920**
31 December 2009			
Portfolio risk provision (PRP)	1,254,192	(18,525)	1,235,667
Specific risk provision (SRP)	195,253	(83,187)	112,066
	1,449,445	**(101,712)**	**1,347,733**

5. Financial risk management (continued)

The breakdown of the gross amount of individually impaired loans to customers and due from other banks, along with the fair value of related collateral held by the Bank as security is as follows:

	Banks	Corporate	Retail	Government	Total
31 December 2010					
Gross amount	1,564	335,501	34,838	-	371,903
Individually impaired loans	(2)	(122,975)	(12,198)	-	(135,175)
Fair value of collateral	-	204,169	21,292	-	225,461
31 December 2009					
Gross amount	32,255	178,573	16,679	-	227,507
Individually impaired loans	(4)	(77,703)	(5,480)	-	(83,187)
Fair value of collateral	-	86,589	10,228	-	96,817

Collaterals

For the majority of placements, the Bank requires securities. Securities are usually not required for loans to banks.

Securities usually include one or a combination of following items:

- cash deposits in BAM or foreign currency,
- guarantees issued by Government, Government funds or banks, first class,
- guarantees issued by the parent company, other legal and individuals;
- letter of support issued by the parent company,
- mortgage over property,
- pledge of movable property,
- own blank promissory notes,
- pledge of shares and equity shares
- a pledge of other securities (bonds), or precious metals,
- transfer of receivables (with or without notice),
- takeover of rights from insurance policy.

The Bank reserves the right to request any other type of instrument (or variations of the instruments stated above) that it considers necessary.

Assessment of fair value of impaired assets is based on the value of the security at the time of loan approval, and is updated periodically in accordance with the relevant credit policy.

5. Financial risk management (continued)

Credit exposure and collaterals

	Retail		Corporate		Total	
	Maximum credit risk exposure	Fair value of collaterals	Maximum credit risk exposure	Fair value of collaterals	Maximum credit risk exposure	Fair value of collaterals
31 December 2010						
Loans to customers, net	560,845	236,035	683,075	525,892	**1,243,920**	**761,927**
31 December 2009						
Loans to customers, net	573,855	232,532	773,878	594,782	**1,347,733**	**827,314**

An analysis of the Bank's financial assets by industrial sectors at gross and net principle (less provision) is presented into the following table:

	2010		2009	
	'000 BAM	%	'000 BAM	%
Retail	598,251	36.91%	605,876	36.06%
Trade	286,660	17.69%	280,611	16.70%
Mining and industry	212,453	13.11%	235,322	14.00%
Services, tourism and catering	183,255	11.31%	219,327	13.05%
Transport and communications	82,973	5.12%	88,792	5.28%
Real estate	69,052	4.26%	55,743	3.32%
Agriculture, hunting, fishing	50,351	3.11%	52,104	3.10%
Construction	49,259	3.04%	53,934	3.21%
Finance	31,480	1.94%	37,957	2.26%
Energy	19,783	1.22%	18,894	1.12%
Administration, other public services	6,135	0.38%	6,595	0.39%
Other	31,070	1.92%	25,153	1.50%
Less: Provision for impairment	(172,286)		(103,125)	
	1,448,436		1,577,183	

Problematic assets

Problematic assets are Bank's assets classified as C, D and E category, or assets with specific risk provisions in accordance with IAS ("NPL placements"). Assets in B category have additional monitoring but are not considered as NPL placements. Managing problematic assets is centralized and is under jurisdiction of the Rehabilitation department, and monitoring of portfolio is done by Unit for restructuring and collection and Unit for liquidation. Rehabilitation department is processing problematic loans with aim to enable possibility of restructuring of total receivables, if recovery of client is possible, and if not than they are in charge for activation of collaterals. In 2010, the Bank recognized an increased risk in all business segments, which resulted in forming the Unit for non performing loans ("NPL") responsible for significant part of Corporate department clients with largest risk. Collection of Retail department clients was transferred from Market department to Rehabilitation department.

5. Financial risk management (continued)

Reprograms and restructuring

Considering the worsening economic environment in which the Bank operates, wide range of overall debt reprogramming is enabled, with respect of financial issues of corporate clients and reduced creditworthiness of retail clients.

When reprogramming particular attention is paid to current business cooperation as well as assessing the certainty of economic recovery which should occur in the future.

Restructured placement is a placement that is refinanced, reprogrammed or otherwise converted, or placement in which, due to the user's changed conditions and repayment capabilities, or his inability to make repayment in line with initially agreed repayment plan; or because of the revised (lower) current market rate, previously agreed deadlines (period or repayment plan) and / or other conditions subsequently changed so that the Bank can improve the client's debt service.

Restructured problematic assets are assets when the Bank grants one or more rebates and concessions to the debtor with financial difficulties. Concessions and rebates include:

- taking other assets, that is debtor's property as total or partial collection of Bank's receivables,
- extending the deadline for principal receivable and/or interest,
- reduction of receivables interest rate,
- reduction of debt, principal mature receivable and /or interest,
- other similar concessions.

Restructured and refinanced loans as of 31 December 2010 and 2009 can be summarised as follows:

	Number of restructured loans	Amount
31 December 2010		
Corporate	60	122,987
Retail and SME	30	1,083
Total	**90**	**124,070**
31 December 2009		
Corporate	54	110,100
Retail and SME	11	338
Total	**65**	**110,438**

In 2010, the Bank performed additional analysis of the portfolio and assessed additional provisions in accordance with the negative business trends and reported problems in the regularity of servicing loans which is obvious from the results achieved. Forming additional provisions in excess of the plan in early 2010 is the result of the Bank's policy to "clean-up" the balance sheet and identify all current and potential risks to define recovery strategies to improve its existing position in the market with a new tailored approach to clients.

5. Financial risk management (continued)

Off-balance sheet items

(a) Loan commitments

Timing of contractual amounts of the Bank's off-balance sheet financial instruments that it commits to extend credit to customers and other facilities are summarized in the table below.

	Up to 1 year	From 1 to 5 years	Over 5 years	Total
As at 31 December 2010				
Loan commitments	43,864	10,808	19,946	**74,618**
As at 31 December 2009				
Loan commitments	79,005	3,715	5,683	**88,403**

(b) Other financial liabilities

Other financial liabilities are also included in the table below, based on the earliest contractual maturity date.

	Up to 1 year	From 1 to 5 years	Over 5 years	Total
As at 31 December 2010				
Other financial facilities	24,399	11,537	2,454	**38,390**
As at 31 December 2009				
Other financial facilities	27,130	16,312	2,451	**45,893**

b) Market risk

Market risks consist of potential losses due to a change in market prices. The Bank classifies market price risks according to the risk factors in changes to interest rates, credit spread, currency, volatility and share price risks, as well as risks from alternative investments. Market price risks may result from securities (and products similar to securities), money and foreign currency products, derivatives, currency exchange and results hedging, assets similar to equity or from management of assets and liabilities. Besides market risks, market liquidity risks may also be incurred if, in the event of low market demand, the Bank is unable to liquidate trading positions during liquidity shortfalls (or due to risk-based offsetting requirements) in the short term. For existing positions, these are taken into account as part of the risk limitations for market risks.

General requirements

The Bank develops its market risk strategy on the basis of strategic discussions between the treasury units in charge and Risk controlling. Decisions on combined business and risk strategies are only made in the Asset-Liability Committee (ALCO).
As part of the daily reporting procedure, the Management board receives value-at-risk and performance figures for trading transactions on a daily basis and figures on banking book investments and market risk steering on a weekly basis. There is also a daily report to the Management board in which the key risk and performance figures of the subsidiaries are communicated. In these, the value-at-risk at the subsidiary level is compared to the defined limits.Limit breaches initiate defined escalation processes up to Management board level.

The subsidiaries of HGAA calculate risk as per HGAA specifications for the respective portfolios. The results are presented to the Management board as part of ongoing reporting for HGAA. This is also applicable for the Bank, as a subsidiary of HGAA.

5. Financial risk management (continued)

Risk measurement

The Bank calculates its market risk as part of daily monitoring with value-at-risk methods on the basis of a one-day holding period, with a confidence level of 99 percent in full accordance to group standards. The main instrument used in this process is the Monte Carlo simulation with an exponentially weighted history of 250 days.

For the purpose of determining risk capital requirements for the risk bearing capacity calculation, values are scaled to the uniform confidence level of 99.895 percent, assuming liquidation over a time period of 126 days.

The models calculate potential losses taking into account historic market fluctuations (volatilities) and market context (correlations). In 2010, the calculation of specific interest risk was further refined, also against the background of the increased significance of interest risk in the current market situation.

The reliability of market risk measurement methods is regularly examined with regard to the quality of individual risk methods. As part of back testing, the risk forecast is compared with the result (profit or loss). In accordance with the Basel 'traffic light' approach, the forecast quality of the risk model is appropriate.

While the VaR that is determined for monitoring requirements is used to forecast potential losses under normal market conditions, future-oriented analyses using extreme assumptions are also carried out. Market positions are subjected to exceptional market price changes, crisis situations and worst case scenarios as part of so-called "stress tests", and analysed for hazardous risk potentials using the simulated results. The stress scenarios are monitored for appropriateness and adjusted if required. The Bank does not currently use its own internal risk models for regulatory purposes. Instead, it uses the standard Group method.

The interest rate change risk in the investment book is determined as a present value risk, as are all market risks at the Bank. The risk of interest rate changes in the investment book is for the most part integrated into ongoing risk monitoring of market risk controlling as per value-at-risk.

Contractual cancellation rights are modelled as an option, and flow into the risk calculation. All stochastic positions are accounted for in accordance with internal models.

As per Basel II specifications, a 200 basis point interest rate shock scenario is calculated for the interest rate change risk in the investment book. The cash value changes calculated in relation to the regulatory equity are well below under the so-called "outlier criterion". In addition, a large number of possibly occurring market fluctuations can be calculated and illustrated through a calculation of standard, forward, historic and extreme scenarios.

Risk mitigation

In accordance with the new risk strategy from the Group, which was adopted in August 2010, a limit of ten per cent of risk capital has been set for market risk. The amount of risk capital set represents the maximum loss that may be incurred for absorbing market risk. Market risk capital is distributed over individual market risk factors (interest rate, currency, shares, credit spread, volatility and alternative investments) by setting risk factor limits. Risk factor limits are also further defined and differentiated through defined partial portfolios. In addition a limit system also provides support through defined warning levels, which show negative developments early on.

Risk controlling and monitoring

All market risks are centrally monitored by Risk controlling, which is independent of all trading activities. In addition to regulatory requirements, this unit also ensures risk transparency and regular reporting to the Management board member responsible for this area. The Management board also receives a separate monthly report on the actual market risk situation as well as on back testing and stress test results with a commentary on potentially significant developments.

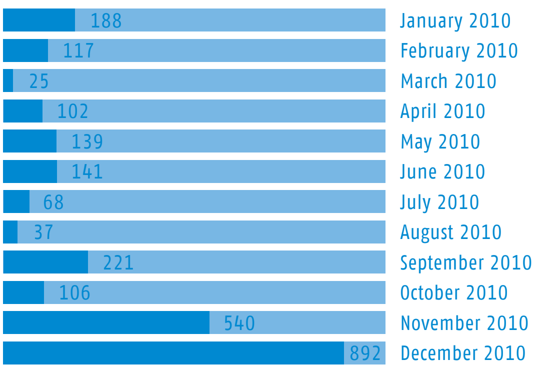
The control of interest rate risk is carried out on an institutionalised basis in compliance with the regulatory requirements related to interest rate risk statistics. The Asset Liability Committee, which consists of the Management board as well as key staff in Treasury, Risk Control and Financial Controlling, meets on a regular basis to analyse and decide on measures related to balance sheet structure and liquidity controlling.

5. Financial risk management (continued)

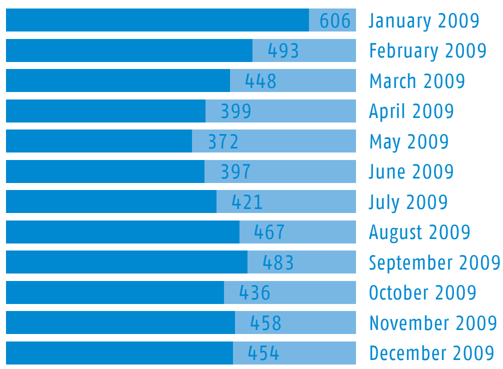
Overview of market risk

The table shows the progression of interest rate risk (including the interest rate risk of the trading book) for the Bank in 2010. The fixed-interest period statement for the Bank contains
all interest rate relevant on and off balance sheet items with their next interest rate fixing date. The stochastic cash flows are illustrated with uniform standards given by the Group and with local models for country-specific transactions. The graph shows the interest rate change risk for the Bank at overall Bank level (trading book and banking book).

Interest rate risk
(trading book + Bank book)
2010 in 000 BAM

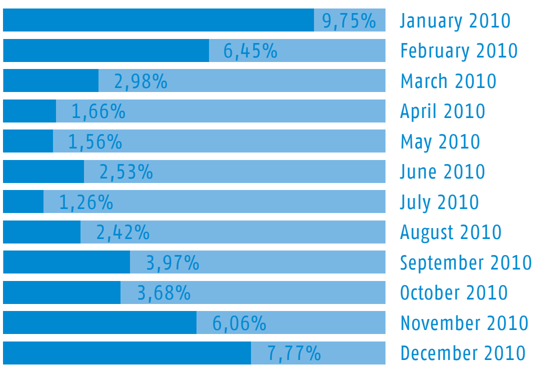


Interest rate risk
(trading book + Bank book)
2009 in 000 BAM

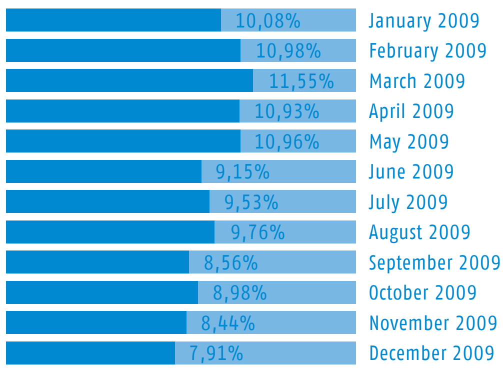


The methodology of the interest risk calculation is oriented to the specifications of the Austrian National Bank (Oesterreichische Nationalbank - OeNB) regarding the calculation of interest risk statistics. Initially, interest risks per defined currency are determined on the basis of the Bank's fixed interest period statement; a second step calculates the risk equity ratio as a percentage of capital resources.

Interest risk equity ratio in % - 2010



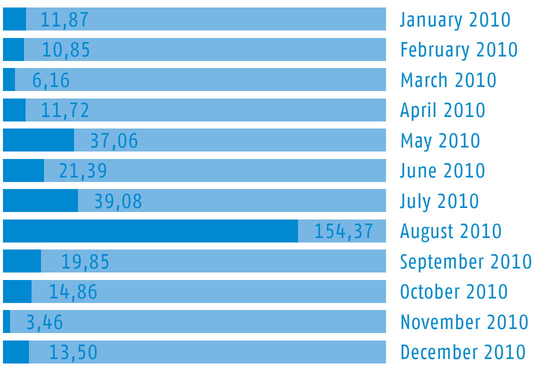
Interest risk equity ratio in % - 2009



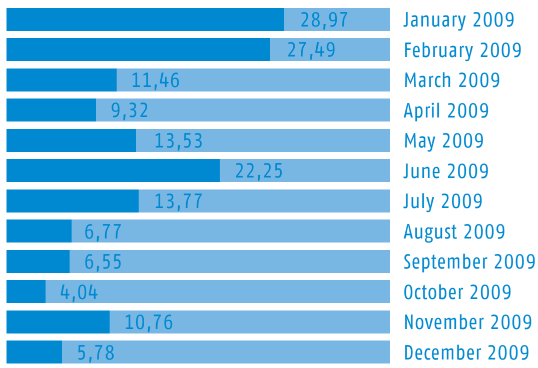
5. Financial risk management (continued)

The data basis for determining the value-at-risk for open foreign currency positions at the Bank level is based on the figures of the OeNB report and contains operational business activities. The value-at-risk for this foreign currency risk was approximately BAM 13.5 thousand (EUR 6.90 thousand) per day as at 31 December 2010, at a confidence interval of 99%.

Change in VAR – open foreign currency positions –
2010 in 000 BAM

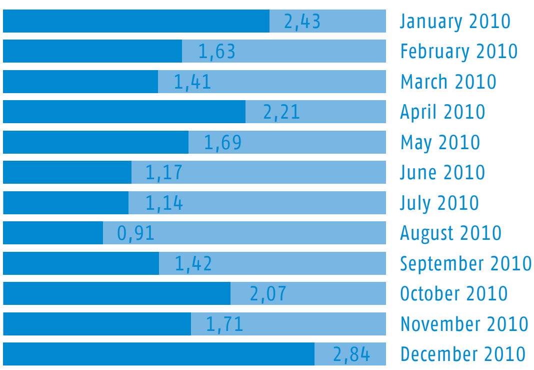


Change in VAR – open foreign currency positions –
2009 in 000 BAM

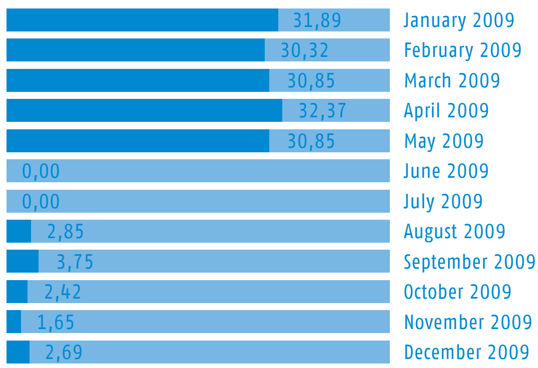


The Alternative Investment risk within the Bank at year-end 2010 stands at BAM 2.84 thousand (EUR 1.45 thousand), with a 1-day value-at-risk and a confidence level of 99%.

Change in VAR – Alternative Investments -
2010. godina in 000 BAM



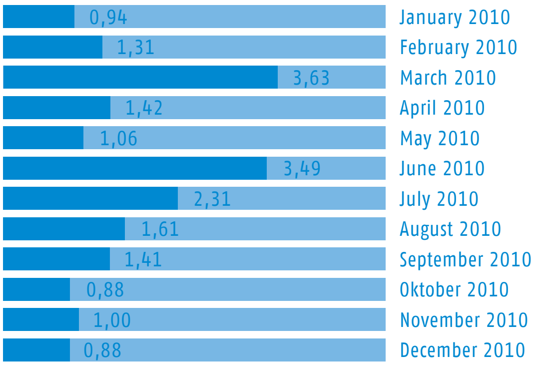
Change in VAR – Alternative Investments -
2009 in 000 BAM



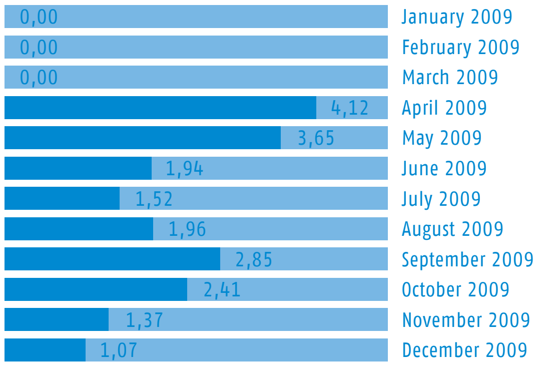
5. Financial risk management (continued)

The credit spread risk for the Bank at year-end 2010 stands at BAM 0.88 thousand (EUR 0.45 thousand), with a 1-day value-at-risk and a confidence level of 99%.

Change in Credit Spread Risk – 2010 in 000 BAM



Change in Credit Spread Risk – 2009 in 000 BAM



c) Foreign currency risk

Foreign currency risk is Bank's exposure to possible impact of change in foreign currency exchange rate and danger that unfavourable changes may result in loss denominated in BAM (domestic currency). The level of risk is a function of height and length of the Bank's exposure to possible changes of foreign exchange rates, and depends on the amount of Bank borrowing in foreign currency and the degree of alignment of assets and liabilities of the bank's balance sheet and off-balance sheet, for example the degree of compliance of its currency flows. Foreign currency risk exposure arises from credit, deposit, investment and trading activities. It is controlled daily in accordance with legislation and the internally set limits for each currency and for the assets and liabilities denominated in foreign currencies. During the year opened currency positions were held within the limits prescribed by the Decisions of BARS and the internal limits set according to the Group methodology.

Currency adjustment of financial assets and financial liabilities is held through the activities of all currency trading, contracting deposits with foreign currency and monitoring approvals of loans in foreign currency. Activities and responsibilities for the Management of Foreign currency risks are identified by the Program for Foreign Exchange Currency Management of the Bank.

5. Financial risk management (continued)

Foreign currency position of Bank's assets and liabilities:

	EUR	USD	CHF	Other	Total foreign currencies	Total local currency	Total
As of 31 December 2010							
ASSETS							
Cash and balances with the Central Bank	8,147	583	1,254	1,092	11,076	158,623	169,699
Due from other banks	21,414	5,378	931	1,106	28,829	-	28,829
Loans to customers, net	770,142	-	323,367	-	1,093,509	150,411	1,243,920
Securities available for sale	24	344	-	-	368	712	1,080
Other financial assets	786	59	-	3	848	4,060	4,908
Total assets	**800,513**	**6,364**	**325,552**	**2,201**	**1,134,630**	**313,806**	**1,448,436**
LIABILITIES							
Due to banks	230,691	9	302,133	-	532,833	28,131	560,964
Due to customers	328,003	6,066	4,030	1,251	339,350	182,190	521,540
Borrowings	150,911	-	-	-	150,911	-	150,911
Subordinated debt	35,470	-	-	-	35,470	-	35,470
Other financial liabilities	5,830	8	2,177	-	8,015	18,912	26,927
Total liabilities	**750,905**	**6,083**	**308,340**	**1,251**	**1,066,579**	**229,233**	**1,295,812**
Net balance sheet position	**49,608**	**281**	**17,212**	**950**	**68,051**	**84,573**	**152,624**
As of 31 December 2009							
ASSETS							
Cash and balances with the Central Bank	6,471	305	964	1,131	8,871	161,208	170,079
Due from other banks	34,595	5,370	11,673	1,175	52,813	1,372	54,185
Loans to customers, net	822,057	102	342,809	-	1,164,968	182,765	1,347,733
Securities available for sale	24	319	-	-	343	735	1,078
Other financial assets	1,079	351	-	-	1,430	2,679	4,109
Total assets	**864,226**	**6,447**	**355,446**	**2,306**	**1,228,425**	**348,759**	**1,577,184**
LIABILITIES							
Due to banks	309,696	2	358,895	-	668,593	43,519	712,112
Due to customers	369,196	5,672	2,662	1,052	378,582	168,512	547,094
Borrowings	135,873	-	-	-	135,873	-	135,873
Subordinated debt	12,000	-	-	-	12,000	-	12,000
Other financial liabilities	952	18	939	-	1,909	21,713	23,622
Total liabilities	**827,717**	**5,692**	**362,496**	**1,052**	**1,196,957**	**233,744**	**1,430,701**
Net balance sheet position	**36,509**	**755**	**(7,050)**	**1,254**	**31,468**	**115,015**	**146,483**

5. Financial risk management (continued)

d) Interest rate risk

The Bank's operations are influenced by changes in interest rates to the extent to which interest-bearing assets and liabilities mature or have interest rates changing at different times or in different amounts.

In the case of variable rate assets and liabilities of the Bank are subject to basis risk, which is the difference in pricing of various variable rate indexes, such as savings rate, a six-month EURIBOR and the different types of interest. Risk management activities are aimed at optimizing net interest income in accordance with the Bank's business strategies, given the market interest rates.

The Bank has developed a policy for managing market risks, with aim to control and limit the potential loss of the Bank due to changes in foreign and domestic interest rates that affect the economic and market value of the Bank.

To achieve objective of the Policy for Interest rate risk Management, Bank identifies positions that are sensitive to interest rate changes, prepares the data for the calculation of interest-sensitive positions, establishes methods of measuring risk, establishes control mechanisms, and sets limits, determines the authorizations and responsibilities and reports.

The purpose of managing interest rate risk, as a segment of asset and liability management, is to determine the optimal interest rate, and therefore the income of the Bank, taking into account market conditions and competitive environment, while at the same time the interest rate adjusts with the Bank's assets and liabilities. Given this objective, it is important to assess the sensitivity of revenues to the rapid changes in market interest rates.

In order to protect against exposure to interest rate risk, the Bank contracts the variable interest rate, adjust the structure of interest bearing assets and liabilities on which interest is paid, and used other means of managing interest rate risk

The Bank manages interest risk by:

- adequately determining the level of interest margin, that is, reconciling the level of interest rates at assets and liabilities' items sensitive to interest rate, with the same maturity and time interval within which the level of interest rate is re determined and/or
- determining maturity reconciliation of assets and liabilities sensitive to interest rate (when fixed interest rate is determined) that is, reconciles maturity (time interval for re determining of interest rates in case floating interest rate is applied).

The Bank is exposed to risks which affect its financial position and cash flows through the effects of changes in market interest rates level.

Interest risk presents unfavourable change of active interest rates in relation to the level of borrowings rates.

While managing credit risk the Bank uses simulation of expected and extreme changes in interest rates and the influence of these changes on the income statement.

Definition

The Bank defines liquidity risk as the risk of not being able to meet due payment obligations on time or, in full amount; or – in the event of a liquidity crisis – only being able to procure refinancing at increased market rates, or only being able to sell assets at a discount to market prices.

General requirements

The strategic principles of handling liquidity risks at the Bank are defined in the risk strategy. The overriding objective of liquidity risk management and controlling is to ensure that the Bank maintains its capacity to make payments and undertake refinancing activities at any time. The content-related and organisational conditions for the management and controlling of liquidity risks are governed by a liquidity manual which applies across the entire HGAA.

In the Bank, liquidity steering and management are the responsibility of the Treasury function. The Treasury unit is responsible for operational liquidity steering and liquidity off-sets. Liquidity risk controlling is the responsibility of the Risk Controlling of the Bank. Risk measurement, limitation as well as timely and consistent reporting are carried out.

5. Financial risk management (continued)

The Bank has in place emergency liquidity planning which has been set out in written form. It sets out the processes and control or hedging instruments which are required to avert imminent or tackle acute crises. In the event of a liquidity crisis, the priorities of the Bank are to rigorously maintain the capacity to pay and to prevent damage to the Bank's reputation.

Risk measurement

The main methodological tool for measuring, analysing, monitoring and reporting on liquidity risk within the Bank is the liquidity overview. It is used to illustrate liquidity gaps resulting from deterministic and modelled future payment flows and the realisable liquidity coverage potential in firmly defined time bands.

The liquidity potential quantifies the capacity of the Bank – in amounts and dates – to procure liquid funds at the earliest opportunity and at cost-effective terms and conditions.

It highlights possibilities regarding the coverage of liquidity gaps and hence all liquidity risks related to payment flows.

The most important components of liquidity potential are as follows:

- free access to CBBH and interbank funds,
- other available and eligible securities,
- issue potential in cover register
- senior bond issues
- committed lines of parent company, as well as
- securitisation potential.

In addition to the normal scenario, other scenario analyses under stress conditions, such as name crises (rating deterioration, reputation risks) as well as market crises (restrictive funding options on capital markets, increased cash flow outflow as well as transfer limits), supplement the risk measurement spectrum.

On the basis of the liquidity overviews, key indicators are determined for the different scenarios, which allow a compact assessment of the liquidity situation. Liquidity ratios (showing tightest liquidity position) and "time-to-wall" key figures (showing maximum liquidity time horizon) for up to one year are calculated to evaluate the liquidity situation – although particular importance is attached to the utilisation over the first 4 weeks.

For the purpose of limiting structural liquidity, cash value losses in the event of an increase in the funding spread due to a rating deterioration are compared in the risk-bearing capacity calculation to the economic equity.

Risk controlling

A bundle of different liquidity reserves ensures that the Bank maintains its ability to pay even during crisis situations. They are subjected to different stresses in order to maintain an overview of available liquidity resources through the respective units even during crisis situations.

5. Financial risk management (continued)

Moreover, the Bank holds its own liquidity buffer for stress situations, composed of securities eligible in accordance with requirements of the European Central Bank (ECB) and/or securities that can be quickly liquidated as well as guaranteed interbank lines of credit.

A cash flow statement composed of deterministic, stochastic and forecast data forms the basis of this process. Short term forecast data is elicited directly from client transactions by the operating units for the purposes of short-term controlling, while planned budget information is used for medium-term controlling.

Any occurring gaps are compared to the liquidity potential – a well-diversified bundle of liquidity reserves available for liquidity management. The liquidity reserves are subjected to a regular review and stresses, depending on the market situation (as described above).

Controlling department focuses on meeting the minimum reserve as well as 1st and 2nd grade liquidity reserves.

Risk monitoring

The monitoring of liquidity risk is carried out, on the one hand, on the basis of the liquidity ratio and "time-to-wall" key indicators (maximum liquidity time horizon) under normal and stress conditions, and on the other hand, through the integration of the structural liquidity risk into overall bank controlling (risk-bearing capacity).

Limits for short-term liquidity as well as for the limitation of long-term structural liquidity have been set, both at Group level and for the individual subsidiaries, and are monitored constantly.

To ensure that existing liquidity gaps can be closed at any time through the mobilisation of the liquidity potential, threshold values are being defined for all scenarios and if these are exceeded, measures must be introduced to reduce the identified liquidity risks.

The liquidity overviews as well as other relevant key indicators form a part of regular risk reports to the Management board and the controlling units responsible for liquidity risk.

Overview – liquidity situation

At the beginning of 2010, the situation in the international money and capital markets was still heavily influenced by the events in 2009. The markets only functioned in a limited way at the beginning; the situation improved in the course of the year, trust between the banks grew and investors were also prepared to make liquid funds available for longer periods of time. HGAA's and the Bank's situation were made more difficult in this environment, because of the discussions about its shareholder structure and the charges arising on the lending business.

5. Financial risk management (continued)

Maturity analysis for financial assets and liabilities

The following table presents analysis of assets and liabilities by maturity based on remaining period from balance sheet date to agreed due date.

	Up to 1 month	From 1 to 3 months	From 3 to 12 months	Over 1 year	Total
31 December 2010					
Assets					
Cash and balances with the Central Bank	169,699	-	-	-	169,699
Due from other banks	28,829	-	-	-	28,829
Loans to customers	205,072	49,077	188,555	801,216	1,243,920
Securities available for sale	-	13	13	1,054	1,080
Other financial assets	4,908	-	-	-	4,908
Total	**408,508**	**49,090**	**188,568**	**802,270**	**1,448,436**
Liabilities					
Due to banks	17,210	8,360	6,101	529,293	560,964
Due to customers	237,534	50,260	160,463	73,283	521,540
Loan liabilities	560	1,210	4,939	144,202	150,911
Subordinated debt	-	-	-	35,470	35,470
Other financial liabilities	26,927	-	-	-	26,927
TOTAL	**282,231**	**59,830**	**171,503**	**782,248**	**1,295,812**
Liquidity gap	**126,277**	**(10,740)**	**17,065**	**20,022**	**152,624**
31 December 2009					
Assets					
Cash and balances with the Central Bank	170,079	-	-	-	170,079
Due from other banks	54,185	-	-	-	54,185
Loans to customers	183,297	70,401	203,319	890,716	1,347,733
Securities available for sale	-	-	-	1,078	1,078
Other financial assets	4,108	-	-	-	4,108
Total	**411,669**	**70,401**	**203,319**	**891,794**	**1,577,183**
Liabilities					
Due to banks	25,309	11,338	11,758	663,707	712,112
Due to customers	199,547	113,831	165,234	68,482	547,094
Loan liabilities	422	779	3,847	130,825	135,873
Subordinated debt	-	-	-	12,000	12,000
Other financial liabilities	23,622	-	-	-	23,622
TOTAL	**248,900**	**125,948**	**180,839**	**875,014**	**1,430,701**
Liquidity gap	**162,769**	**(55,547)**	**22,480**	**16,780**	**146,482**

5. Financial risk management (continued)

Fair value of financial assets and liabilities

The table below summarizes the carrying amounts and fair values of those financial assets and liabilities not presented on the Bank's Statement of financial position at their fair value:

	Carrying value		Fair value	
	2010	2009	2010	2009
Assets				
Due from banks, net	198,528	224,264	198,528	224,264
Loans to customers, net	1,243,920	1,347,733	1,245,005	1,351,553
Liabilities				
Due to banks and customers	1,082,503	1,259,206	1,082,649	1,259,097
Borrowings	150,911	135,873	150,911	135,873
Subordinated debt	35,470	12,000	35,470	12,000

(i) Due from banks

Due from banks includes inter-bank placements.

Fair value of deposits with variable interest rate and "overnight" deposits is their stated value.

The estimated fair value of fixed interest-bearing deposits not quoted in an active market is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

(ii) Loans to customers, net

Loans are presented net of charges for impairment. The estimated fair value of loans represents the discounted amount of estimated future cash flows expected to be received. Expected cash flows are discounted at current market rates to determine fair value.

(iii) Deposits from other banks, clients, other deposits, other borrowings and subordinated debt

The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand. The estimated fair value of fixed interest-bearing deposits not quoted in an active market is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

Fair value of term deposits with variable interest rate approximates the carrying value as of reporting date.

Subordinated debt with variable interest rate approximates the carrying value as of reporting date.

Operating risks

Operating risk management is an important part of the Bank's operations, which allows its long-term successful business and the preservation of reputation.

As part of Operating risk framework, the Bank implemented the following activities:

- defining and identification of operating risk
- development and application of methods and systems for measurement, analysis, limitations and control of operating risks in accordance with regulatory and Group requirements
- measuring, analysis and supervision of operating risk in line with minimal standards for operating risk management
- maintenance of database on losses from operating risks – regular data collection and reporting on incidents
- regular updates of new and existing policies, manuals and procedures in accordance with regulations and Group standards
- managing the Plan for continuous business operations
- employee education on dealing with operating risks.

5. Financial risk management (continued)

In order to improve processes for managing operational risk in the Bank, the following activities are planned:

- initiation of activities for adequate operational risk management for all projects, developing new products, processes and systems;
- testing the Business continuity plan;
- education for employees involved in issuing the Reports and all employees of the Bank;
- establishment of the Committee for the management of operational risks in the Bank, in terms of exercising control over operational risk management and development.

e) Capital management

In accordance with the Law on Banks (Official Gazette of the Republic of Srpska 44/03), the minimum amount of a bank's paid equity and the lowest level of equity a bank has to maintain, cannot be less than BAM 15,000 thousand. The Bank's equity is BAM 175,512 thousand and is in line with these provisions.

The Bank's equity comprises basic capital less items deductible from basic capital and additional capital.

The Bank's basic capital includes paid share capital and reserves. Deductible items include: intangible assets, uncovered loss from previous years and current year loss, carrying amount of the Bank's treasury shares, the amount of missing provisions for credit losses under BARS requirements.

Additional capital includes general provision for risk balance sheet items from A category, current net profit confirmed by an independent auditor, subordinated debt up to 50% of the basic capital.

Regarding capital management the Bank aims to:

- provide consistency with the BARS requirements,
- provide consistency with Hypo Group standards,
- provide solid equity basis as a support for further development of Bank's operations
- provide possibility of long-term business cooperation while providing income for shareholders.

The Bank has to maintain equity solvency at the minimum of 12% and basic capital at the minimum of 50% of total equity. To do so the Bank has to adjust the scope and structure of its operations to business indicators defined by the Decision on minimum standards for bank capital management ("Official Gazette of RS" no. 12/03, 29/03, 115/06, 61/08) and other BARS decisions relating to supervision and control of banks performance and Law on Banks RS ("Official Gazette of Republic of Srpska" no. 43/03 and 74/04).

Bank Management monitors adequacy indicators and other business indicators on a regular basis. Reports on indicators are submitted to BARS quarterly in a prescribed form.

The Bank manages equity and performs reconciliations in accordance with its goals, market changes and risks typical for Bank's operations. Depending on the primary goal, the Bank adjusts equity structure as follows:

- by adjustment of dividend amount paid to shareholders, that is, by increase in share capital arising from profit,
- by increase of capital reserves arising from profit,
- new issue of shares which can be private and public,
- increase in additional equity items.

5. Financial risk management (continued)

As at 31 December 2010 and 31 December 2009, the Bank's equity indicators were in compliance with applicable regulations.

	31 December	31.decembar 2009.
Basic capital	137,131	139,268
Additional capital	54,521	37,829
Deductible items from capital	(1,743)	-
Capital, net	**189,909**	**177,097**
Total weighted risk assets	1,173,531	1,279,804
Total weighted risk off-balance items	70,442	84,655
Weighted operating risk	93,429	13,493
Total weighted risk assets and off-balance items	**1,337,402**	**1,377,952**
Capital adequacy as at 31 December	**14.2%**	**12.9%**

6. Critical accounting estimates and judgements

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgments are continually evaluated and based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

(a) Impairment losses on loans and advances, deposits with other banks and other risk-weighted assets and off-balance sheet items
The Bank reviews its loan portfolio and other risk-weighted assets and off-balance sheet items to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the income statement, the Bank makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans and guarantees before the decrease can be identified with an individual exposure in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the Bank.

Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

(b) Impairment of available-for-sale equity investments
The Bank determines that available-for-sale equity investments are impaired when there has been a significant or prolonged decline in the fair value below its cost.
This determination of what is significant or prolonged requires judgment. In making this judgment, the Bank evaluates among other factors, the volatility in share price. In addition, objective evidence of impairment may be deterioration in the financial health of the investee, industry and sector performance, changes in technology, and operational and financing cash flows.
Had all the declines in fair value below cost been considered significant or prolonged, the Bank would have recognized an additional BAM 78 thousand loss in its 2010 financial statements.

6. Critical accounting estimates and judgements (continued)

(c) Fair value of property and investment property

The fair value of property and investment property is assessed against market values of similar properties in similar locations, by certified appraisers on a regular basis. The fair value is assessed using the earnings method (income capitalisation method) taking into account actual or estimated annual income per item, which is compared to the actual value of that item. Actual annual income is decreased for maintenance, depreciation and tax expenses, as well as for risk of not being able to generate income if property not leased or used. Specific factors used are those applicable to the Bosnia and Herzegovina market. The carrying value as of 31 December 2010 represents the fair value assessed (Note 17).

7. Net interest income

a) Interest income

	2010	2009 Restated
Loans to retail customers	47,178	50,272
Loans to corporate and public sector customers	44,884	57,679
Balances with the Central Bank and other banks	585	1,383
Due from other banks	193	651
	92,840	**109,985**

b) Interest expense

	2010	2009
Due to banks	23,956	28,959
Deposits from retail customers	10,745	10,507
Deposits from public sector	3,015	6,757
Deposits from corporate customers	2,407	2,903
Deposits from other customers	124	812
	40,247	**49,938**
	52,593	**60,047**

8. Net fee and commission income

a) Fee and commission income

	2010	2009 Restated
Fee and commission income arising from domestic payment transfers	5,427	5,084
Fee and commission earned on VISA card operations	2,360	2,388
Fee and commission income arising from international payments transfers	2,056	2,296
Charges for early loan repayment and sending letters of warning	916	585
Fees from issued guarantees, letters of credit and other contingent liabilities	819	1,083
Fee and commission income from currency conversions	438	357
Brokerage fees	95	170
Other fee and commission income	290	109
	12,401	**12,072**

b) Fee and commission expense

	2010	2009
Fees for funds available for liquidity purposes	1,792	675
Fee and commission expense incurred on payment card operations	631	651
Fees and commission from loans, issued guarantees and other contingent liabilities	591	705
Fee and commission expense incurred on domestic payment transfers	486	429
Fee and commission expense incurred on international payment transfers	122	129
Fee and commission expense incurred on stock exchange operations and Central Register fees	24	37
	3,646	**2,626**
	8,755	**9,446**

9. Other operating income

	2010	2009 Restated
Collection of receivables previously written off	9,765	3,868
Rental income	590	576
Income from dividends	114	-
Income from dormant customer current accounts	95	133
Decrease in provisions from retirement benefits and other employee benefits (unused vacation days) (Note 23)	30	582
Capital gains	9	54
Income from release of provisions for bonuses	-	980
Other income	170	549
	10,773	**6,742**

9. Other operating income (continued)

Income from dormant accounts relates to accounts where there has been no accountholder activity, either deposit to or withdrawal from the account by the accountholder, for a period of one year from the date of the last accountholder activity, and in the case of Time Deposits, one year beyond the maturity date, in accordance with the Law on Banks of Republic of Srpska.

10. Other operating expenses

	2010	2009
Staff costs	17,259	19,166
Loss upon revaluation of property and investment property	6,184	-
Losses upon recognised provisions for legal proceedings (Note 28)	5,176	-
Depreciation and amortization	3,762	3,702
Materials and services	3,500	3,899
Insurance and property security	2,893	2,968
Telecommunications	1,650	1,576
Advertising, marketing and entertainment	1,460	2,125
Fees to the Banking Agency of the Republic of Srpska	1,241	1,272
Maintenance	1,166	1,114
Indirect taxes and contributions	950	1,198
Loss upon recognised other provisions (Note 28)	813	-
Professional services from related banks	677	487
Rent	640	761
Loss upon revaluation of property and investment property	635	-
Court expenses and fees	477	229
Per diems and other travel costs	456	517
Sponsorships and humanitarian aid	270	474
Non-material expenses	162	146
Membership fees and commissions	131	148
Disposals and write-offs of property and equipment	11	55
Other expenses	308	229
	49,821	**40,066**

Staff costs can be further analysed as follows:

	2010	2009
Net salaries	8,905	9,497
Salary taxes and contributions	6,031	6,277
Other employee benefits	2,323	1,952
Restructuring provisions	-	1,440
	17,259	**19,166**

11. Impairment provisions for credit risk and potential other losses

	2010	2009 Restated
Loans to customers, net (Note 15)	72,920	30,912
Other assets (Note 20)	(12)	1,287
Provisions for commitments and contingencies (Note 28)	(1,749)	2,131
Due from other banks (Note 14)	1	(476)
Direct write-offs	**266**	**-**
	71,426	**33,854**

12. Income tax expense

a) Components of income tax

	2010	2009
Current income tax	3,247	3,115
Deferred tax income	(23)	(393)
	3,224	**2,722**

b) Reconciliation of the income tax and profit before tax and prescribed interest rates

	2010	2009
(Loss) / profit before tax	(45,427)	4,123
Income tax at the statutory tax rate of 10%	(4,543)	412
Adjustments		
Tax effect of expenses not included in determining taxable profit	8,474	3,001
Tax effect of income not included in determining taxable profit	(90)	(204)
Tax effect of recognised provisions for potential losses representing 20% of the tax basis	(649)	(623)
Non deductible representation expenses	3	5
Non deductible penalties	35	25
Non-allowable depreciation and amortization	10	2
(Allowable) / non-allowable provision for employee benefits	(16)	104
Income tax expense	**3,224**	**2,722**
Effective tax rate	**(7%)**	**66%**

Tax effect of expenses not included in determining taxable profit in the amount of BAM 8,474 thousand represents 10% of expenses not allowed for tax purposes, in accordance with the Law on corporate income tax of Republic of Srpska, including risk provision charges, other provision charges, impairment losses from revaluations and other various expenses.

13. Cash and balances with the Central Bank

	2010	2009 Restated
Cash on hand:		
- in local currency	10,224	11,755
- in foreign currencies	11,076	8,871
Balances with the Central Bank (in local currency)		
- obligatory reserve	104,986	116,346
- giro account	43,413	33,107
	169,699	**170,079**

Cash and balances with Central Bank as at 31 December 2010 include accompanying interest and fee in total amount of BAM 35 thousand (2009: BAM 65 thousand).

The obligatory reserve represents amounts required to be deposited with the Central Bank of Bosnia and Herzegovina. Pursuant to the Law on the Central Bank of Bosnia and Herzegovina, starting from 1 May 2009 the obligatory reserve requirement represents 14 % of average ten-day deposits and borrowings expressed due within one year and 7% of those due after a year in BAM.

The obligatory reserve is maintained as the average balance on the current account with the Central Bank of Bosnia and Herzegovina.

This reserve is available for liquidity purposes. The Central Bank of Bosnia and Herzegovina pays a fee on the obligatory reserve in the manner specified by Law.

14. Due from other banks

	2010	2009 Restated
Foreign currency accounts with foreign banks and banks within the country	7,115	16,484
Up to 7 days term deposits	21,632	36,245
Up to 90 days term deposits	-	1,372
Foreign currency cheques in the course of collection	84	88
Provision for impairment	(2)	(4)
	28,829	**54,185**

Due from other banks as at 31 December 2010 includes accompanying interest in total amount of BAM 0 thousand (2009 – BAM 72 thousand).

Foreign currency accounts represent non-interest bearing accounts held with foreign and domestic banks.

As at 31 December 2010, term deposits with maturity up to 7 days relate to deposits in domestic banks and banks in the European Union in BAM and in foreign currencies bearing interest from 0.24% to 0.25% p.a. (2009 – 0.15% to 0.25% p.a.)

As at 31 December 2010, term deposits with maturity up to 90 days relate to deposits in BAM and EUR placed with related banks bearing interest from 6% to 6.5% p.a. (2009 – 4% to 6.5% p.a.).

14. Due from other banks (continued

For movement of provisions please see table below:

	2010	2009
1 January	4	480
Charge for the year	83	3
Release of provisions	(82)	(479)
Charge for the year net of release of provisions	*1*	*(476)*
Foreign exchange differences, net	(3)	-
31 December	**2**	**4**

Starting from 1 January 2010, in accordance with the local regulations, the Bank calculates risk provisions in original currency and discloses net foreign exchange differences, separately from the related provision charge.

15. Loans to customers, net

	2010	2009 Restated
Up to one year:		
- in local currency	293,694	275,103
- in foreign currencies	14,441	16,195
Over one year:		
- in local currency	908,280	971,733
- in foreign currencies	3,004	3,076
Current portion of long-term loans:		
- in local currency	189,508	177,679
- in foreign currencies	288	254
Receivables arising on issued guarantees:		
- in local currency	2,130	2,186
- in foreign currencies	3,462	3,219
Provision for impairment	(170,887)	(101,712)
	1,243,920	**1,347,733**

Loans to customers as at 31 December 2010 include accompanying interest and fee in the total amount of BAM 26,928 thousand (2009 – BAM 28,912 thousand)

The majority of loans up to one year in BAM relate to overdrafts on current accounts extended to corporate customers of BAM 98,891 thousand (2009 – BAM 112,476 thousand), with annual interest rates ranging from 4.25% to 15.49% (2009 – 6% to 12.50% p.a.).

Movement in provision for impairment can be presented as follows:

15. Loans to customers, net (continued)

	2010	2009
1 January	*101,712*	75,321
Charge for the year	111,895	62,601
Release of provisions	(38,975)	(31,689)
Charge for the year, net	*72,920*	30,912
Foreign exchange differences, net	2,396	-
Write-off	**(6,141)**	**(4,521)**
31 December	**170,887**	**101,712**

Charge for the year includes the foreign exchange impact relating to these items.

The remaining part mainly relates to short-term loans extended to enterprises in the amount of BAM 57,523 thousand with annual interest rates ranging from 4% to 11.5% (2009 – BAM 78,551 thousand with interest 7% to 12% p.a.), short-term consumer loans approved to retail customers in the amount of BAM 20,664 thousand with annual interest rates ranging from 6% to 13.99% (2009 – BAM 18,820 thousand with interest from 7% to 15.45% p.a.) and short term loans to SME customers in the amount of BAM 61 thousand with annual interest rates in the range from 9.10% to 11.50% (2009: BAM 86 thousand with interest from 8% to 11.75%). The remaining BAM 116,555 thousand are long term matured loans to retail and corporate customers comprised of BAM 94,503 thousands (2009: BAM 39,223 thousand) and due interest and fees to corporate and retail in amount of BAM 22,052 thousand (2009: BAM 25,946 thousand).

Loans over one year in BAM were primarily extended to corporate customers, with interest rates ranging from 6-month EURIBOR plus the margin of minimum 2.75% and 6 months LIBOR plus margin of minimum 4 percent, and from 2% to 13.99 % per annum, respectively (2009 – interest rates ranging from 6M EURIBOR + 2.75% p.a., 6M LIBOR + 4% p.a. minimum and 2 to 12.99% p.a. respectively).

At 31 December 2010, loans over one year in BAM include the loans extended to retail customers totalling BAM 515,075 thousand (including the current portion thereof) (2009 – BAM 530,821 thousand). These loans can be analysed as follows:

	Maturity	Interest rate	Total
31 December 2010			
Consumer loans	Up to 10 years	5.99 % -13.99 %	232,856
Residential loans	Up to 30 years	3.60 % -11.25%	166,907
Mortgage and Lombard loans	Up to 20 years	2.50 % -11.75 %	70,572
Investment loans	Up to 10 years	4.75 % -11.50 %	28,227
Loans to Bank employees	Up to 30 years	2.00 % -11.25 %	15,226
Auto loans	Up to 10 years	7.20 % -10.75 %	1,287
			515,075
31 December 2009			
Consumer loans	Up to 10 years	9.00% - 12.00%	251,679
Residential loans	Up to 30 years	6.50% - 10.95%	155,711
Mortgage and Lombard loans	Up to 20 years	4.50%-11.75%	79,457
Investment loans	Up to 10 years	6.50% - 11.50%	26,930
Loans to Bank employees	Up to 30 years	2.00% - 9.25%	15,142
Auto loans	Up to 10 years	9.00% - 12.00%	1,902
			530,821

15. Loans to customers, net (continued)

The geographic sector risk concentrations within the customer loan portfolio mostly relates to clients domiciled in the Republic of Srpska.

16. Securities available for sale

	2010	2009
Investments in associates		
- Kristal Konsalting a.d., Banja Luka	151	151
Investments in financial institutions		
- Euroaxis Bank, Moscow, Russia	344	319
- Banjalučka berza A.D., Banja Luka	175	175
- Kristal Invest a.d., Banja Luka	78	78
- Centralni registar hartije od vrednosti a.d., Banja Luka	30	30
- Other financial institutions	145	143
Investments in non-financial entities	26	26
Investments in debt securities	131	156
	1,080	**1,078**

On 8 February 2011, the Bank's Supervisory board decided to sell the Bank's shares in Kristal Konsalting and Kristal Invest a.d., Banja Luka for BAM 530 thousand to a private investor.

17. Property and equipment

	Land and buildings	Equipment and other assets	Investments in progress	Total
Cost				
Balance at 1 January 2009	*47,236*	*15,479*	*2,609*	*65,324*
Additions	15	362	3,024	3,401
Transfers	1,464	1,265	(3,000)	(271)
Transfers to other classes	40	(65)	(1,456)	(1,481)
Write-off	-	(561)	-	(561)
Sales	-	(34)	-	(34)
Balance at 31 December 2009	**48,755**	**16,446**	**1,177**	**66,378**
Balance at 1 January 2010	*48,755*	*16,446*	*1,177*	*66,378*
Additions	28	185	998	1,211
Transfers	1,373	493	(1,866)	-
Transfers to other classes	-	-	(5)	(5)
Revaluation	(2,517)	-	-	(2,517)
Write-off	-	(689)	-	(689)
Sales	-	(181)	-	(181)
Balance at 31 December 2010	**47,639**	**16,254**	**304**	**64,197**
Accumulated depreciation				
Balance at 1 January 2009	*8,035*	*4,822*	-	*12,857*
Depreciation for the period	641	2,402	-	3,043
Transfers to other classes	-	(25)	-	(25)
Write-off	-	(508)	-	(508)
Sales	-	(19)	-	(19)
Balance at 31 December 2009	**8,676**	**6,672**	**-**	**15,348**
Balance at 1 January 2010	*8,676*	*6,672*	-	*15,348*
Depreciation for the period	665	2,419	-	3,084
Revaluation	(2,718)	-	-	(2,718)
Write-off	-	(679)	-	(679)
Sales	-	(161)	-	(161)
Balance at 31 December 2010	**6,623**	**8,251**	**-**	**14,874**
Net book value				
31 December 2010	**41,016**	**8,003**	**304**	**49,323**
31 December 2009	**40,079**	**9,774**	**1,177**	**51,030**

The Bank's property as of 31 December 2010, included land and buildings with carrying amount of BAM 2,706 thousand, for which the Bank was not in possession of appropriate title deeds (2009 - BAM 2,734 thousand).

The Bank has not pledged any component of its property or equipment as collateral for loan repayment as of 31 December 2010 or 31 December 2009.

The Bank revalues its property depending on market price sensitivity, but at least once every two and half years. Last revaluation was performed as of 31 December 2010 and total net effect of this revaluation is an increase in revaluation reserves of BAM 801 thousand and expense of BAM 584 thousand.

18. Intangible assets

	License and software
Cost	
Balance at 1 January 2009	*4,387*
Additions	3,766
Write-off	(6)
Disposals	(421)
Balance at 31 December 2009	**7,726**
Balance at 1 January 2010	*7,726*
Additions	6,798
Disposals (write-offs)	(370)
Balance at 31 December 2010	**14,154**
Accumulated amortisation	
Balance at 1 January 2009	*1,074*
Amortisation for the period	608
Disposals	(421)
Balance at 31 December 2009	**1,261**
Balance at 1 January 2010	*1,261*
Amortisation for the period	621
Disposals (write-offs)	(370)
Balance at 31 December 2010	**1,512**
Net book value	
31 December 2010	**12,642**
31 December 2009	**6,465**

19. Investment property

	Buildings
Cost	
Balance at 1 January 2009	*3,814*
Additions	10
Transfers	271
Balance at 31 December 2009	**4,095**
Balance at 1 January 2010	*4,095*
Revaluation	(200)
Balance at 31 December 2010	**3,895**
Accumulated depreciation	
Balance at 1 January 2009	394
Charge for the year	52
Balance at 31 December 2009	**446**
Balance at 1 January 2010	*446*
Charge for the year	57
Revaluation	(218)
Balance at 31 December 2010	**285**
Net book value	
31 December 2010	**3,610**
31 December 2009	**3,649**

As of 31 December 2010 investment property includes land with carrying amount of BAM 113 thousand, for which the Bank is not in possession of appropriate title deeds (2009 – BAM 23 thousand).

20. Other assets

	2010	2009 Restated
In local currency:		
Receivables from clients in litigations	1,453	1,449
Foreclosed assets	1,446	6,261
Receivables from realised collaterals	962	162
Deferred tax assets	540	490
Receivables from income tax	531	531
Receivables from dealing with credit cards	377	314
Prepaid expenses	338	261
Consumables and fixtures	280	300
Advances paid	23	42
Receivables from clients for rent	55	79
Prepaid interest	18	92
Other receivables	877	1,283
In foreign currencies:		
Receivables from dealing with credit cards	496	486
Prepaid expenses	76	114
Prepaid interest	46	-
Other receivables	514	215
Provision for impairment	(1,397)	(1,409)
	6,635	**10,670**

As of 31 December 2010 BAM 1,726 thousand relates to non financial assets (2009: BAM 6,561 thousands) out of total other assets.

Movement in provision for impairment can be presented as follows:

	2010	2009
1 January	*1,409*	122
Charge for the year	-	1,287
Release of provisions	(12)	-
Charge for the year net of release of provisions (Note 11)	*(12)*	*1,287*
31 December	**1,397**	**1,409**

21. Due to banks and other financial institutions

	2010	2009 Restated
Demand deposits in local currency:		
– domestic banks and financial institutions	15,001	11,118
Demand deposits in foreign currencies:		
– foreign related banks	512	1,190
– domestic banks and financial institutions	372	639
Short-term deposits in local currency:		
– domestic banks and financial institutions	7,460	25,115
Long-term deposits in local currency:		
– domestic banks and financial institutions	17,361	11,423
Long-term deposits in foreign currencies:		
– from related banks	520,258	662,627
	560,964	**712,112**

Due to banks and other financial institutions as at 31 December 2010 includes accompanying interest in the total amount of BAM 372 thousand (2009: BAM 420 thousand)

Long-term deposits in foreign currencies totalling BAM 520,258 thousand relate to deposits from Hypo Alpe-Adria-Bank International AG, Klagenfurt having 36 to 108 months maturity, and interest rates calculated based on the EURIBOR/LIBOR (1M, 3M, 6M and 1Y and 7Y p.a.) rate plus interest margin ranging from 0.9% to 4% (2009 – 0.9% to 2.13% p.a.).

22. Due to customers

	2010	2009 Restated
Demand deposits in local currency:		
- Enterprises	27,711	30,184
- Government institutions	30,513	9,429
- Foreign entities	1,330	740
- Other customers	9,069	8,158
- Citizens	64,751	61,759
Demand deposits in foreign currencies:		
- Enterprises	6,701	8,803
- Government institutions	62	442
- Foreign entities	2,590	3,457
- Other customers	629	1,022
- Citizens	56,596	56,212
Short-term deposits in local currency:		
- Enterprises	1,122	7,938
- Government institutions	28,685	2,545
- Other customers	575	442
- Citizens	10,137	13,293
Short-term deposits in foreign currencies:		
- Enterprises	11,302	2,656
- Government institutions	7,302	99,350
- Foreign entities	-	119
- Other customers	-	5
- Citizens	38,809	50,590
Long-term deposits in local currency		
- Enterprises	9,125	34,196
- Government institutions	14,167	15,005
- Other customers	634	135
- Citizens	26,188	18,408
Long-term deposits in foreign currencies:		
- Enterprises	5,603	1,862
- Government institutions	28,870	-
- Foreign entities	-	4,179
- Other customers	1,122	870
- Citizens	137,947	115,295
	521,540	547,094

Due to customers as at 31 December 2010 includes accompanying interest in the total amount of BAM 1,680 thousand (2009: BAM 2,770 thousand). Demand deposits in BAM comprise current account balances of enterprises, government institutions and other entities, bearing an annual interest rate from 0.1% to 4.1% (2009 – 0.5% to 3.65% p.a.). In accordance with the Bank's policy demand deposits in foreign currency bear annual interest rate ranging to 0.1% to 3.85% p.a. (2009 – 0% to 3.85% p.a.). In accordance with its interest rate policy, the Bank pays interest on short-term deposits from citizens in BAM and in foreign currencies ranging from 0.10% to 3.85% p.a. depending

22. Due to customers (continued)

on the maturity date and the of deposited amount (2009 – 1% to 5.3% p.a.). As of 31 December 2010 short-term deposits from customers in the amount of BAM 6,498 thousand represents cash collateral for the loans and guarantees extended by the Bank (2009 – BAM 3,668 thousand). Long-term deposits in BAM and foreign currencies bear annual interest rates between 0.45% and 5.1% p.a., based on the type of currency and maturity of deposits (2009 – 2.5% to 6.5% p.a.). As of 31 December 2010, long-term deposits from customers in the amount of BAM 6,152 thousand represent cash collateral for the loans and guarantees extended by the Bank (2009 – BAM 6,323 thousand).

23. Borrowings

	2010.	2009 Restated
In foreign currency:		
European Investment Bank, Luxembourg	49,062	49,048
Council of Europe Development Bank, France	19,614	19,601
	68,676	68,649
In local currency:		
Housing Fund of the Republic of Srpska, Banja Luka	38,144	30,325
Republic of Srpska Development and Employment Fund, Banja Luka	31,823	29,598
Fund for Development of eastern part of the Republic of Srpska, Banja Luka	12,268	7,301
	82,235	**67,224**
	150,911	**135,873**
Current portion of borrowings	*6,487*	*4,853*

Borrowings as at 31 December 2010 include accompanying interest in the total amount of BAM 222 thousand (2009: BAM 195 thousand).

European Investment Bank, Luxembourg loan was disbursed for financing investments in legal entities. Repayable in two equal instalments on 23 March 2015 and 23 March 2017, bearing interest at the rate of 6 month EURIBOR + 0.094% and 0.119% p.a. (2009 – 1.23% and 1.25% p.a.).

Loan from Council of Europe Development Bank, France was disbursed for financing of SME loans. It is repayable in 40 equal monthly instalments from 06 January 2011 until 06 October 2020, bearing interest at the rate of EURIBOR + 0.18% p.a.

Republic Srpska Development and Employment Fund, Banja Luka financed development projects. The repayment is in accordance with the repayment schedules to the end users of the loans. Interest is charged at the rate of 6M EURIBOR reduced in accordance with the criteria for reduction of interest rates on IRB RS ad Banja Luka credit lines.

Fund for Development of the Eastern region of the Republic of Srpska, Banja Luka was disbursed for providing support to development projects in the eastern part of Republic of Srpska. The repayment is in accordance with the repayment schedules to the end users of the loans. Interest is charged at the rate of 6M EURIBOR reduced in accordance with the criteria for reduction of interest rates on IRB RS ad Banja Luka credit lines.

Housing Fund of the Republic of Srpska, Banja Luka has provided a loan to the Bank for financing of the purchase of state-owned flats. The repayment is in accordance with the repayment schedules to the end users of the loans. Interest is charged at the rate of 6M EURIBOR reduced in accordance with the criteria for reduction of interest rates on IRB RS ad Banja Luka credit lines.

24. Subordinated debt

Subordinated debt in the amount of BAM 35,470 thousand refers to received funds from the Bank's major shareholder Hypo Alpe-Adria-Bank International AG Klagenfurt in the equivalent amount of EUR 18,135,502 based on the Subordinated debt agreement dated 31 December 2008. Pursuant to the Decision 03-1408-4/08 dated 18 December 2008, the Banking Agency of the Republic of Srpska gave pre-approval for the inclusion of the subordinated debt in the Bank's additional capital. The subordinated debt is deposited for an indefinite period and the Bank is not obliged to repay the deposited amount. According to the agreement, subordinated debt bears interest at the rate of EURIBOR + 7% p.a. The second was signed on 30 September 2010. Pursuant to the Decision 03-1060-4/108 dated 29 September 2010 the Banking Agency of the Republic of Srpska gave pre-approval for the inclusion of the subordinated debt in the Bank's additional capital. The subordinated debt is deposited for an indefinite period and the Bank is not obliged to repay the deposited amount. According to the agreement, subordinated debt bears fixed interest of 10%.

25. Other liabilities

	2010	2009 Restated
Liabilities in local currency:		
Deferred other fees	8,954	9,180
Early loan repayments	7,857	6,362
Due to employees	3,921	2,556
Liabilities for taxes and contributions	2,949	2,110
Deferred interest income	735	755
Accounts payable	359	439
Unrealized payments for establishment of companies by third parties	156	160
Deferred tax liabilities	192	85
Accrued expenses	100	78
Liabilities for dividends	71	85
Provisions for unused vacation days	63	78
Other liabilities	1,135	1,025
Foreign currency liabilities:		
Accounts payable	277	484
Deferred other fees	52	-
Early loan repayments	15	12
Other liabilities	91	214
	26,927	**23,623**

As of 31 December 2010 Bank did not have any non-financial liabilities.

Changes in provisions for unused vacation days are presented as follows:

	2010	2009
Balance as of 1 January	78	257
Release of provision	(15)	(179)
Balance as of 31 December	**63**	**78**

26. Share capital

The Bank's share capital includes initial shareholder investments and subsequent share emissions. The Bank's shareholders are entitled to take part in the management of the Bank, as well as in the distribution of profit.

As of 31 December 2010, the Bank's share capital included 175,511,897 ordinary shares with an individual par value of BAM 1 (2009 – 125,837,352 ordinary shares). All of the Bank's shares have been fully paid up.

Pursuant to the Shareholders' Assembly Decision on the XI share emission through public offerings on the stock exchange (number S-II-3/2010 dated 22 October 2010) the procedure for increasing the Bank's share capital by BAM 49,873,665 was initiated. The Securities and financial exchange Commission of the Republic of Srpska on 9 November 2010 approved the share emission (Resolution number 01-UP-031-3071/10). Pursuant to the decision 01-03-PE-3507/10 dated 24 December 2010 the share emission was registered with the Securities and Financial Exchange Commission of the Republic of Srpska.

The Bank's majority shareholder is Hypo Alpe-Adria Bank International AG Klagenfurt with participation of 99.7131% (31 December 2009: 99.6 %).

Share premium in the amount of BAM 64 thousand represents the difference between the sales price of shares (BAM 2.11) and their nominal value (BAM 1.00) for 57,560 shares issued during the IX share issuance in 2008.

As at 31 December 2010, the Bank holds 27,996 own shares, acquired on 21 December 2010.

27. (Loss) / earnings per share

Bank shares are traded publicly on stock exchange. The Bank is calculating and disclosing earnings per share in accordance with IAS 33. Basic earnings per share are calculated by dividing net profit attributable to the ordinary shareholders by the weighted average number of ordinary shares for the period.

	2010	In BAM Year ended 31 December 2009
(Loss) / Profit	(48,650,424)	1,400,867
Weighted average number of ordinary shares	126,926,109	121,070,229
Basic earnings per share	**(0.383)**	**0.012**

The Bank has no dilutive potential ordinary shares such as convertible debt and share options. Therefore, the Bank does not calculate diluted earnings per share.

28. Other provisions

As of 31 December 2010, other provisions are as follows:

	2010	2009
Legal proceedings	5,176	-
Restructuring	1,227	1,440
Other provisions	813	-
Severance payments	383	415
	7,599	1,855
Provision for contingent liabilities	702	2,451
	8,301	**4,306**

28. Other provisions (continued)

	Restructuring	Severance payments	Legal proceedings	Other	Total
1 January 2010	**1,440**	**415**	**-**	**-**	**1,855**
Charge for the year	-	25	5,176	813	6,014
Release of provisions	(213)	(15)	-	-	(228)
Payments during the period	-	(42)	-	-	(42)
31 December 2010	**1,227**	**383**	**5,176**	**813**	**7,599**

Increases in provisions for legal proceedings and other provisions are included in Other operating expenses, Note 10. Movement in provision for contingent liabilities is as follows:

	2010	2009 Restated
1 January	*2,451*	*320*
Charge for the year	1,444	2,631
Release of provisions	(3,193)	(500)
Charge for the year net of release of provisions (Note 11)	*(1,749)*	*2,131*
31 December	**702**	**2,451**

29. Commitments and contingent liabilities

a) Commitments and contingent liabilities

	2010.	2009.
Loan commitments	74,618	*88,403*
Payment guarantees	34,325	42,500
Performance guarantees	3,499	2,394
Letters of credit and other guarantees	566	999
	113,008	**134,296**

b) Litigation

In order to collect its receivables and realize its other rights the Bank is engaged in various lawsuits as of 31 December 2010. In a certain number of cases, administrative litigations have been initiated with the aim of annulment of certain acts passed during the administrative processes. Also, as of 31 December 2010, several legal and physical entities have brought lawsuits against the Bank.

In order to collect its receivables, which relate to loans, issued guarantees and letters of credit, the Bank is engaged in 164 court proceedings against legal entities, for approximately BAM 120.6 million as of 31 December 2010 (2009 - 180 court proceedings, with total value of approximately BAM 87.6 million).

In order to collect receivables from individuals, which relate to housing and consumer loans, current accounts, credit cards and damage compensations, the Bank is engaged in 578 proceedings with total amount of approximately BAM 21.6 million as at 31 December 2010 (2009 - 320 proceedings with total amount of approximately BAM 8.9 million).

As of 31 December 2010, the legal proceedings filed against the Bank amounted to BAM 63,788 thousand (2009 – BAM 19,203 thousand). This amount does not include any penalty interest that might be assessed, given that the Bank's management

29. Commitments and contingent liabilities

was unable to estimate with any certainty the possible effects of penalty interest as of the date of issuance of these financial statements. Management of the Bank did not account for a provision for potential losses arising on the aforementioned litigation given that the Bank's management judges that the final outcome of the filed legal proceedings will be favourable, and that no material losses will result from the settlement of the aforementioned litigations.

The Bank constantly monitors legal risks, and evaluates the expected costs from the legal proceedings, and based on this forms adequate provisions (Note 28).

Based on the above fact, none of the proceedings initiated against the Bank are significant enough to imperil the Bank's operations.

c) Operating lease commitments

Where the Bank is the lessee, the future minimum lease payments under non cancellable operating leases, are summarized in the table below.

	2010	2009
No later than 1 year	654	606
Later than 1 year and not later than 5 years	1,506	1,141
Later than 5 years	428	532
	2,588	**2,279**

d) Capital investment commitments

The Bank has signed a contract for the purchase of new software 'BEST' from Zajednički informacioni sistemi d.o.o. Beograd, a related party, which will result in additional liabilities of BAM 2,033 thousand in 2011 (2009 – BAM 2,606 thousand in 2010).

30. Related party transactions

	2010	2009.
Assets:		
Foreign currency accounts:		
- HYPO ALPE-ADRIA-BANK International AG, Klagenfurt, Austria	4,798	12,696
- HYPO ALPE-ADRIA-BANK d.d., Ljubljana, Slovenia	249	56
- HYPO ALPE-ADRIA-BANK SPA, Udine, Italy	216	144
- HYPO ALPE-ADRIA-BANK d.d., Zagreb, Croatia	188	248
- HYPO ALPE-ADRIA-BANK d.d., Mostar	100	110
Term deposits:		
- HYPO ALPE-ADRIA-BANK International AG, Klagenfurt, Austria	21,632	4,365
- HYPO ALPE-ADRIA-BANK d.d., Mostar	-	1,300
Other assets:		
- HYPO ALPE-ADRIA-BANK d.d., Mostar	60	66
- HYPO ALPE-ADRIA-BANK a.d., Podgorica, Montenegro	11	5
- HYPO ALPE-ADRIA-BANK a.d., Beograd, Serbia	7	5
	27,261	**18,995**
Liabilities:		
Demand deposits:		
- Hypo Alpe-Adria-Leasing d.o.o., Sarajevo	739	1
- HYPO ALPE-ADRIA-BANK International AG, Klagenfurt, Austria	204	177
- HYPO ALPE-ADRIA-BANK a.d., Podgorica, Montenegro	149	47
- HYPO ALPE-ADRIA-BANK d.d., Zagreb, Croatia	91	91
- HYPO ALPE-ADRIA-BANK AG, Klagenfurt, Austria	67	874
- Hypo Alpe-Adria-Immobilien-Beteiligungs GMBH	1	1
Long-term deposits:		
- HYPO ALPE-ADRIA-BANK International AG, Klagenfurt, Austria	520,257	662,628
- Hypo Alpe-Adria-Immobilien-AG, Klagenfurt	-	29,337
Subordinated debt		
- HYPO ALPE-ADRIA-BANK International AG, Klagenfurt, Austria	35,470	12,000
Other liabilities:		
- HYPO ALPE-ADRIA-BANK International AG, Klagenfurt, Austria	177	114
- HYPO ALPE-ADRIA-BANK a.d., Beograd, Serbia	158	121
- HYPO ALPE-ADRIA-BANK d.d.,Mostar	116	149
- HYPO ALPE-ADRIA-BANK d.d., Zagreb, Croatia	77	55
- ZIS Beograd, Serbia	7	304
- HYPO ALPE-ADRIA-BANK a.d., Podgorica, Montenegro	3	8
- Hypo Alpe-Adria-Immobilien-AG, Klagenfurt, Austria	-	1,582
	557,516	**707,489**

30. Related party transactions (continued)

	2010.	2009.
Interest income:		
- HYPO ALPE-ADRIA-BANK International AG, Klagenfurt, Austria	37	183
- HYPO ALPE-ADRIA-BANK d.d., Mostar	6	78
- HYPO ALPE-ADRIA-BANK SPA, Udine, Italy	5	-
Fee and commission income:		
- HYPO ALPE-ADRIA-BANK d.d., Mostar	169	190
- HYPO ALPE-ADRIA-BANK AG, Klagenfurt, Austria	29	69
- HYPO ALPE-ADRIA-BANK SPA, Udine, Italy	13	25
- HYPO ALPE-ADRIA-BANK International AG, Klagenfurt, Austria	2	-
Other operating income		
- HYPO ALPE-ADRIA-BANK International AG, Klagenfurt, Austria	48	-
- Hypo Alpe-Adria-Leasing d.o.o., Sarajevo	25	-
	334	**545**
Interest expenses:		
- HYPO ALPE-ADRIA-BANK International AG, Klagenfurt, Austria	(20,338)	(25,447)
- Hypo Alpe-Adria-Immobilien AG, Klagenfurt, Austria	(333)	(1,582)
Fee and commission expense		
- HYPO ALPE-ADRIA-BANK International AG, Klagenfurt, Austria	(2,347)	(1,328)
- HYPO ALPE-ADRIA-BANK d.d., Mostar	(88)	(71)
- HYPO ALPE-ADRIA-BANK, d.d Zagreb, Croatia	(28)	(26)
- HYPO ALPE-ADRIA-BANK SPA, Udine, Italy	(1)	(2)
- Hypo-Alpe-Adria Bank d.d., Ljubljana, Slovenia	(1)	(1)
- HYPO ALPE-ADRIA-BANK AG, Klagenfurt, Austria	(1)	-
- Hypo Alpe-Adria-Leasing d.o.o., Sarajevo	-	(1)
Other operating expenses:		
- HYPO ALPE-ADRIA-BANK International AG, Klagenfurt, Austria	(951)	(722)
- ZIS Beograd, Serbia	(784)	(812)
- HYPO ALPE-ADRIA-BANK d.d., Zagreb, Croatia	(523)	(531)
- Hypo Alpe-Adria Consultant, Sarajevo	-	(82)
- HYPO ALPE-ADRIA-BANK, Mostar	-	(31)
- Hypo Alpe-Adria-Immobilien AG, Klagenfurt, Austria	-	(2)
	(25,395)	**(30,638)**
	(25,061)	**(30,093)**

The Bank received significant funding from its parent company in the form of demand deposits, short-term deposits, long term deposits and subordinated debt representing 36.68% of its total sources of funding (2009 – 41.03%).

Management remuneration

	2010	2009
Net salaries	287	*176*
Taxes and contributions	161	99
	448	**275**

31. Regulatory requirements

The Bank was obliged to harmonize its operations with the Republic of Srpska Accounting Regulations and with the regulations prescribed by the Banking Agency of the Republic of Srpska, serving as the supervisory body of the banking sector in the Republic of Srpska.

At 31 March 2008, BARS has adopted new Decision regarding minimum standards for bank liquidity management which altered request for term reconciliation of rest of terms till maturity date of asset and liability instruments

New decision states that Bank has to:

- Engage at least 85% (previously 100%) of assets with maturity up to 30 days in placements with maturity up to 30 days
- Engage at least 80% (previously 100%) of assets with maturity up to 90 days in placements with maturity up to 90 days
- Engage at least 75% (previously 95%) of assets with maturity up to 180 days in placements with maturity up to 180 days.

As at 31 December 2010 and 31 December 2009, foreign currency compliance indicators of financial assets and liabilities, as set out by the BARS were within the prescribed limits.

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