HYPO ALPE ADRIA
SUPPORTIVE. FRIENDLY. FAIR.

Annual Report 2010

Hypo Alpe-Adria-Bank d.d.

Slovenia

Contents

1 Introduction

Hypo Alpe-Adria-Bank d.d. with its headquarters at Dunajska cesta 117, Ljubljana, is a Slovenian public limited company, registered for the providing of universal banking services in the Slovenian market.

The Bank's sole owner is Hypo Alpe-Adria-Bank International AG, with its headquarters in Klagenfurt, Austria.

Current ownership of Hypo Alpe-Adria-Bank International AG (since 30 December 2009) is as follows:

- Republic of Austria (100 per cent holding).

1.1 Brief Review of the Bank's Operations

EUR '000

Key highlights	2010	2009
Number of clients	51,226	48,724
Number of branch offices	18	18
Number of employees	403	396
Balance sheet total	2,187,844	2,331,730
Market share	4.40 %	4.90 %
Core capital	174,037	174,037
Total capital	166,619	194,446
Net income from operations	59,617	56,298
Pre-tax profit	(32,404)	3,831
Interest rate margin	2.39 %	2.05 %
Pre-tax return on equity (ROE)	-16.56 %	1.89 %
Pre-tax return on assets (ROA)	-1.53 %	0.17 %
Cost/income ratio (CIR)	39.47 %	43.91 %
Number of ordinary shares	41,706	41,706

1.2 Significant Events in 2010

January
The Bank, together with its sister company Hypo Leasing, sponsored 49th Pokal Vitranc in Kranjska Gora as an official financial partner and major local sponsor.

March
The Bank established a Loyalty program. As a first step, we started to reward the users of MasterCard cards, issued by the Hypo Bank.

We launched the "e-invoice" project, which will be successfully completed by the end of 2010. With this service, we aim to provide our clients the service of transferring e-invoices from the payer to the issuer.

The Bank, together with Hypo Leasing, participated in the first real estate and investment fair ProPrio.

April
The Bank launched the project business debit card, which will be successfully completed in 2011.

Together with Hypo Leasing, the Bank started a major advertising campaign with the slogan Follow your dreams, related to the classification of our football team in the World Cup.

May
Conclusion of the prize draw as part of the "Follow your dreams campaign", with the main prize, a trip to South Africa to see the Slovenian national team.

June
As the general sponsor of the Slovenian national football team and working with the Friends of Youth, the Football Association of Slovenia and the web portal RTVSLO, the Bank and Hypo Leasing prepared an online football auction for the organization of a football camp for children from socially disadvantaged families from all over Slovenia.

The Bank, together with Hypo Leasing, supported the Franja Marathon 2010 event as its golden sponsor.

The Bank and Hypo Leasing organized a spring picnic for suppliers and clients where the participants were able to see the qualifying match between the national teams of Slovenia and the USA.

As the general sponsor of the Slovenian national football team and working with the Friends of Youth, the Bank together with Hypo Leasing, took 22 children to see the match between the national teams of Slovenia and New Zealand, where the children were also able to accompany the players on the football field.

At the traditional banking games, the Bank's employees reached seventh place as a group, out of 20 Slovenian banks.

July
As the sponsor of the 59th Ljubljana Festival, together with Hypo Leasing, the Bank sponsored the concert of world-renowned virtuoso Paco de Lucia.

August
The Bank introduced the new service MasterCard® SecureCode™, which provides our clients, holders of MasterCard cards, better protection for online shopping.

September
The Bank successfully executed the migration of standing orders into SEPA credit transfers. Sponsorship of the 43rd General MOS International Trade Fair in Celje.

October
For clients of the Bank – savings account holders, we held a reception at the Ljubljana Castle to celebrate World Savings Day.

November
On 1 November, we successfully implemented a universal payment order, which will eventually replace the special payment order. From this day onwards, we guarantee our clients availability for cross-border direct debits.

December
The Bank, together with Hypo Leasing, participated in a major charity campaign »Hypo pro futuro«, which was initiated by the President of the Management Board of the Hypo Group, dr. Gottwald Kranebitter and which functions as a social and cultural network in seven European countries. As part of the traditional Christmas donations, we enabled children from socially disadvantaged families to attend a ski school, as part of the project entitled »Let's enjoy childhood vitality in the snow.«

The Management Board

Matej Falatov, M.Sc.
Member of Management Board

Internal Audit
Corporate Banking
Retail & Private Banking
Central Region
West Region
East Region
Financial Markets & Balance Sheet Management

Dr. Alexander Picker
President of Management Board

Internal Audit
Marketing and Public Relations
Legal Affairs
Human Resources
Financial Controling
Organization, Business Integritiy & Compliance
Accounting
Logistics
Informatics
Transaction Banking
Credit Processing
Credit Risk Management
Risk Controling
Rehabilitation
Task Force

1.3 Address by the Management Board

For the banking sector, 2010 was a year of adapting to new economic conditions, a year of changes, a year when we were preparing the Bank for a new impetus, which was implemented at a Group level by the management of our parent bank (Hypo Alpe-Adria-Bank International AG, based in Klagenfurt) with a change introduced on 9 February 2011. They appointed a new Management Board of the Hypo Group in Slovenia - Matej Falatov was appointed Board member, Alexander Picker was appointed President of the Management Board, and the management of our sister company, Hypo Leasing, was taken over by Danijel Novak.

We accepted our new functions as well as the demanding work as a challenge and with the goal to strengthen Hypo Bank, which remains an important part of the Hypo Alpe Adria Group in the Alpine Adria region. We have full confidence of the Supervisory Board, which is an essential element for the management of any company.

The Management in its new form will focus primarily on the future and on our core business - the providing of banking services while adhering to the highest ethical and professional standards. We will work closely with our sister company Hypo Leasing, because we want both companies to operate as one, for the benefit of our Bank's clients, our leasing clients and our Owners.

The year 2010 was a very difficult year for the operations of all companies. Consumer prices in Slovenia increased by an annual average of 1.8 per cent. The unemployment was a cause for concern, since in October 2010 it reached new high point in the last seven years. The number of registered unemployed persons increased by 13.8 per cent at the end of 2010, compared with the year before and at the end of December, it reached 110,021. The Ljubljana Stock Exchange Index SBI TOP decreased by 13.5 per cent by mid-year and rose by 0.9 per cent in December, reaching 850 index points at the end of the year.

The negative developments in the economy also left their consequences on the banking system, where the situation deteriorated in 2010. This was most affected by the increase of credit and income risk and of refinancing risk. The balance sheet total of banks decreased by EUR 1.323 billion or 2.6 per cent in 2010 and amounted to EUR 50.290 billion. This decrease was most affected by the maturity of long-term refinancing operations with the Eurosystem, continued deleveraging with banks abroad, tighter financing conditions and the gradual withdrawal of government deposits. There were fewer short-term loans and an increased demand for long-term loans, especially by large companies.

Of course, all of these factors also affected our Bank's operations. The scope of operations in 2010 decreased slightly, compared to 2009, which was consistent with the situation in the Slovenian economic environment and the reduction of the total banking market.

The Bank's balance sheet total at the end of the year amounted to EUR 2,188 million, which is a 6 per cent nominal decline, compared to 2009. We still rank among the nine largest banks in Slovenia, which is encouraging for us. Compared to 2009, the Bank's income increased by 6 percent, amounting to EUR 59,617 thousand. The consequences of the strained situation on the financial and economic markets were also felt by the Bank, as we again formed impairments and provisions more conservatively, namely by as much as 147 per cent more than in 2009. This has led to negative operating results. The loss thus amounted to EUR 26,292 thousand.

Data from ordinary operations, however, indicate that the Bank is doing well, despite the difficult market conditions. The share of loans to the non-banking sector increased and with 88.7 per cent, it is the most significant share in the balance sheet structure. Financial assets held for trading increased by as much as 36 percent and amounted to EUR 24 million at the end of the year.

Proactive management of all types of risk continued to be one of the key focuses in 2010 and was given much attention. As part of a project managed by the parent bank, the Bank carried out an in-depth analysis of credit risk and defined the investment strategy for the period of one year for each client. As a result of this analysis, we formed sufficient impairments and provisions and managed the Bank's capital adequacy. The Bank has conducted regular stress scenarios of credit insurance reduction, which enabled us to implement timely, responsible and well-directed activities, designed especially to offer our customers greater security in their operations.

The goal of the new Management Board is to strengthen our Bank and renew its reputation. Business partners and clients are the focus of our operations and therefore the largest part of our attention is directed to you, your needs and possibilities. Trust is the key value required to achieve this goal and the way to achieve it is by fairness and professionalism in our activities. This can be achieved by upgrading our existing services and taking advantage of all the possible potentials we may have on the Slovenian market. Our branch network will continue to expand in the future and we will continue to add new employees to our staff. We are a very rational bank, which is shown by the factor of costs as regards to the income (CIR), which dropped below 40 per cent in 2010 and it remains one of the best in Slovenia and within the Hypo Group.

The capital and financial strength that we have acquired with the ownership of our parent bank in 2009 means greater reliability and security for our customers and the possibility of wider support and deeper cooperation. We maintain the concept of a universal bank and continue on our path independently and ambitiously. By the end of 2013 we intend to achieve a 6 per cent share of the total balance sheet of the Slovenian banking sector and rank among the five largest Slovenian banks.

The Bank's policy will be adapted to all areas of business - we will focus on companies, especially small and medium-sized and on the public sector through projects of so-called public-private partnerships. Given the increasing number of our clients, retail banking occupies a special place in our strategic choices. In the future, we will invest most of our energy in our comprehensive offer for retail clients with the goal to increase the sales of services per client, where we want to offer our clients maximum benefits for their money. We will also strengthen the sales of our savings and deposit services of all types, which will provide our clients security, adequate liquidity and, of course, reasonable return.

Major emphasis will be on the so-called cross selling of services between the fields of retail banking, corporate banking and, of course, leasing. We believe that our clients will benefit from a comprehensive offer that includes products and services from all the areas of the Bank's operations, as well as leasing.

To achieve these goals, we also need skilled employees, which our Bank undoubtedly has. Our employees are reputed to be working in a correct, professional and efficient manner in the market. They regard competition as a challenge and an opportunity for new successes.

The same can be said about our sponsored athletes, especially the Slovenian football team competing at world level and which we are very proud of. Supporting our athletes is also a part of our social responsibility activities. Year-round, we work in the social, humanitarian, cultural and sports fields, both on the national and local level. With sponsorships and donations we support top-level athletes and sporting events. We also support cultural events and help socially impaired families across Slovenia. At the suggestion of the President of the Management Board of Hypo Alpe-Adria-Bank International AG, dr. Gottwald Kranebitter, in 2010 we launched a charity project called »Hypo pro futuro«, which functions as a social and cultural network in seven European countries, where our Hypo Group is present.

We aim to offer our business partners more than just our services, so they are regularly included in our socially responsible activities as are our employees. For our business partners, this signifies strengthening of trust and partnership and for the employees, it is a further incentive and motivation.

We are confident that we will prove through our work that we can thrive in the most difficult times and continue to follow our goals and consistently achieve them. Together with our employees, we will strive to realize our new vision and strategy. We want to be SUPPORTIVE partners, working together with you in a FRIENDLY manner and, above all, FAIR and invite you to continue to stay with us in the future.

Management Board

Matej Falatov, M.Sc. **Dr. Alexander Picker**

1.4 Report from the Chairman of the Supervisory Board

In 2010, the owner of the Bank, Hypo Alpe-Adria-Bank International AG, Austria, proposed a new composition of the Supervisory Board. During the Shareholders' Meeting of 28 May 2010, the resignations of the now former members of the Supervisory Board were presented (Chairman: Božidar Špan; Deputy Chairman: Wolfgang Peter, M. Sc.; Members: dr. Wolfgang Felser, Andreas Dörhöfer and Franz Pinkl) and the new members of the Supervisory Board were appointed (Chairman: Johannes Leopold Proksch, M. Sc.; Deputy Chairman: Wolfgang Edelmüller, M. Sc.; Members: dr. Sebastian Firlinger and Aleš Rojs).

In the year 2010 the Supervisory Board of Hypo Alpe-Adria-Bank d.d. held four regular Supervisory Board meetings. It conducted its work in accordance with the Bank's Articles of Association and the Rules of Procedures of the Supervisory Board. The materials prepared in advance and explanations at meetings were given by the Management Board. Also, all the documentation based on conducted inspections of the Bank's operations by the Bank of Slovenia was conveyed to the Supervisory Board.

The consequences of the week financial and economic market environment affected the Bank and its level of risk provisions in 2010. In the end the bank had to close the fiscal year 2010 with a negative result.

As serious accusations related to certain business transactions in Slovenia have come to light, the entire Management Board of the bank was replaced on 9 February 2011, and a comprehensive investigation into the relevant facts and circumstances was launched. The Slovenian National Bank has granted a license to the new management of the business unit, so the company once again has a solid basis from which to operate.

In accordance with Article 282 of the Companies Act and based on current monitoring of the Bank's operations, on periodical reports by the Internal Audit department and on the unqualified opinion by the auditing company Ernst & Young d.o.o., Ljubljana, the Supervisory Board analyzed the report on operations of Hypo Alpe-Adria-Bank d.d. in 2010. In accordance with Article 230 of the Companies Act, it approved the proposal by the Management Board regarding appropriation of net result and recommended its adoption at the Bank's General Meeting of Shareholders.

Chairman of the Supervisory Board

Johannes Leopold Proksch, M.Sc.

2 Introduction of Hypo-Alpe-Adria-Bank in Slovenia

2.1 Mission and Vision of Hypo Alpe-Adria--Bank

The mission of Hypo Alpe-Adria-Bank d.d. is to provide excellent financial services that will satisfy both the clients and the shareholders.

Our vision is to, with a highly motivated team, rank among the first five banks in terms of reputation, market share and profitability.

Our mission as well as our vision is directed towards the most important element – our target clients who are our prime concern in all respects.

A client is anyone needing our services and/or products. The Bank deals with external and internal clients and we constantly strive to ensure their satisfaction.

We are focused on our target clients as they are the centre of our operations.

2.2 Milestones in the Company's History

1994 – entry of Hypo Leasing d.o.o. into Slovenian market
1999 – entry of Hypo Alpe-Adria-Bank d.d. into Slovenian market
2000 – Hypo Alpe-Adria-Bank d.d., Business Unit Celje
2001 – Hypo Alpe-Adria-Bank d.d., Business Unit Maribor
2002 – Hypo Alpe-Adria-Bank d.d., Business Unit Koper
2003 – Hypo Alpe-Adria-Bank d.d., Branch Tyrševa, Maribor
2003 – Hypo Alpe-Adria-Bank d.d., Business Unit Kranj
2004 – Hypo Alpe-Adria-Bank d.d., Ljubljana – new headquarters of the Bank
2004 – Hypo Alpe-Adria-Bank d.d., Branch Trg Osvobodilne fronte, Ljubljana
2004 – Hypo Alpe-Adria-Bank d.d., Business Unit Murska Sobota
2005 – Hypo Alpe-Adria-Bank d.d., Branch Domžale
2005 – Hypo Alpe-Adria-Bank d.d., Business Unit Novo mesto
2006 – Hypo Alpe-Adria-Bank d.d., Business Unit Nova Gorica
2007 – Hypo Alpe-Adria-Bank d.d., Branch Ptuj
2007 – Hypo Alpe-Adria-Bank d.d., Branch Center, Ljubljana
2008 – Hypo Alpe-Adria-Bank d.d., Branch Trbovlje
2008 – Hypo Alpe-Adria-Bank d.d., Branch Šiška, Ljubljana
2008 – Hypo Alpe-Adria-Bank d.d., Branch Brežice
2008 – Hypo Alpe-Adria-Bank d.d., Branch Velenje
2009 - Hypo Alpe-Adria-Bank d.d., Branch Jesenice

2.3 Corporate and Working Bodies

According to the Articles of Association, Hypo Alpe-Adria-Bank d.d. has the following corporate bodies:

- Management Board,
- Supervisory Board and
- Shareholders' Meeting.

According to the Articles of Association, the **Management Board** is composed of two or more members appointed by the Supervisory Board. As at 31 December 2010, the Management Board includes Mr Anton Romih, President of the Management Board, and Mr Urban Golob MSc. and Andrej Lah as the other two members of the Management Board.

On 9 February 2011, the Management Board in the above composition was discharged of its duties by the owner Hypo Alpe-Adria-International AG and the new Management Board composed of the following members was appointed: Mr Alexander Picker as the President and Matej Falatov as a Member of the Management Board.

As at 31 December 2010, the Supervisory Board is composed of five members as follows:

- Johannes Leopold Proksch, MSc. – Chairman,
- Wolfgang Edelmüller, MSc. – Deputy Chairman,
- Sebastian Firlinger, PhD – Member,
- Aleš Rojs – Member

Aleš Rojs was discharged of his duty as Member of the Supervisory Board on 9 February 2011.

Shareholders' Meeting

The Management Board convenes the Shareholders' Meeting in cases laid down by law or in the Articles of Association or when this benefits the Bank. In 2010, a regular General Meeting of Shareholders was held in May 2010.

At the Shareholders' Meeting, the shareholders exercise their rights in the matters concerning the Bank. Our Shareholders' Meeting is universal as the Bank only has one shareholder (Hypo Alpe- Adria International AG holds a 100 percent interest in the Bank).

Advisory bodies of the Management Board:

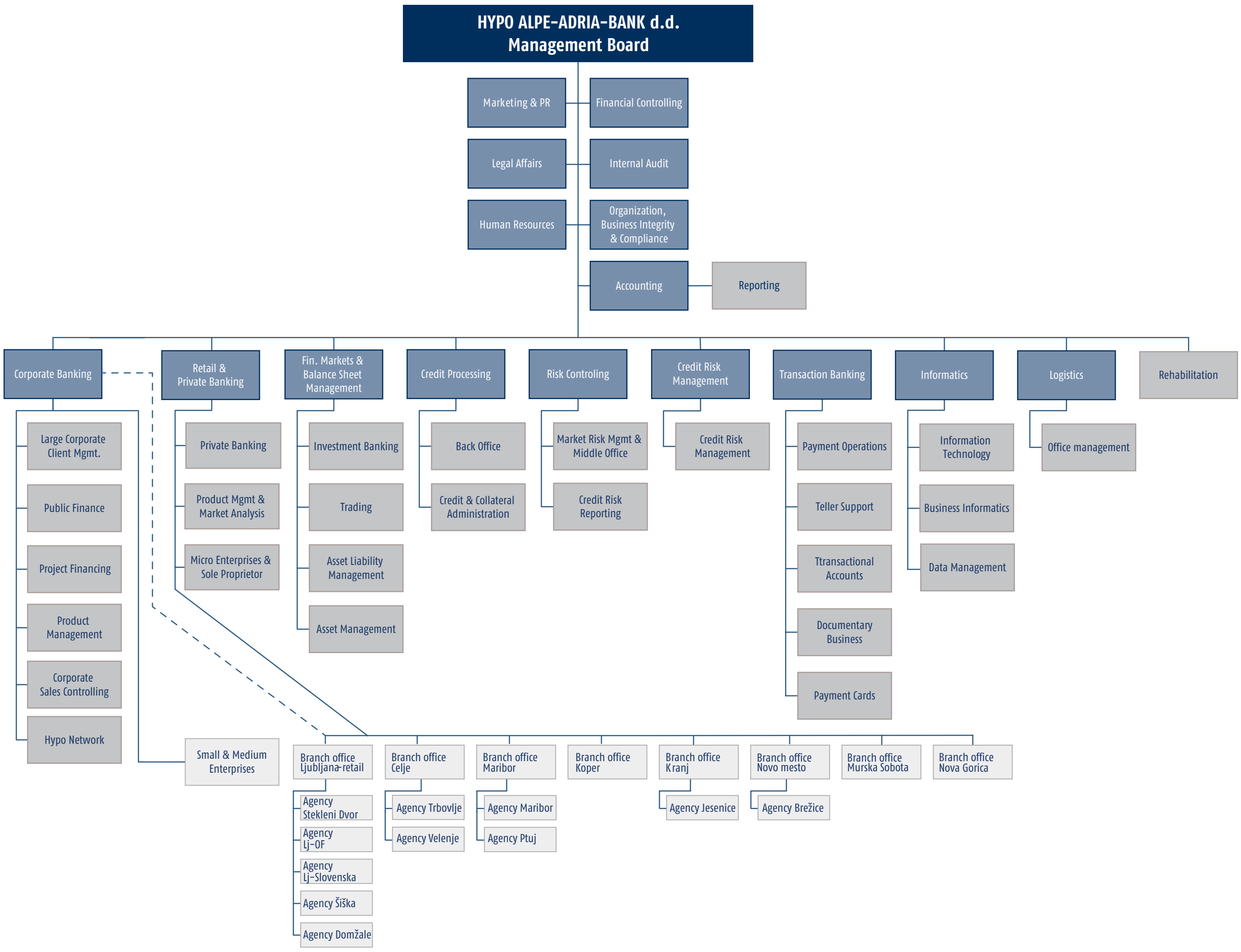
- Management Committee

Committees:

- Liquidity Committee,
- Bank's Credit Committee – PL (Performing Loans)
- Bank's Credit Committee – NPL (Non-Performing Loans),
- Bank's Credit Committee,
- Assets and Liability Committee - ALCO
- Risk Executive Committee – RECO,
- Investment Committee– INCO,
- Internal Control Committee – ICCO,
- Tax Committee – TCO,
- Portfolio Steering Committee – PSC.

The objectives, tasks, authorizations and composition of committees are laid down in the Rules on Organization and Job Systematization of Hypo Bank, as well as in the Rules on the Powers, Authorization and Signatories in Hypo Bank, while the operation of the corporate bodies is governed by individual rules of procedure.

2.4 Organizational Structure



2.5 Business Network

3 Business Report

3.1 General Economic Environment in 2010

Economic Environment

According to the data provided by the Statistical Office of the Republic of Slovenia (SORS), in the third quarter of the year, economic growth in Slovenia slowed down as was expected. This slowdown is very similar to that recorded in the euro zone. In the third quarter of 2010, the gross domestic product (GDP) rate of growth was 1.7 per cent which is primarily due to the increased foreign demand, whereas the rate of domestic consumer spending was gradually decreasing, reflecting uncertain conditions on the labour market. We can see a similar development also in the euro zone where consumer spending is also on the increase (on average, the difference in the dynamics is around 0.4 percentage point per quarter), however the difference is significantly lower compared to the increase in investments which, in the euro zone, recorded a 2.7 per cent quarterly growth whereas in Slovenia, the investment activity is largely stagnant. Construction sector and domestic tourism continue to be the critical activities. As a result of its severe decline, construction sector remains to be the one that most strongly inhibits economic growth. Key economic climate indicators show no imminent recovery or stabilization of economic conditions. In comparison to the euro zone, the growth could be further restricted by price and cost competitiveness of Slovenia as the calculations are less favourable.

On average, consumer prices rose by 1.8 per cent in 2010. Inflation rose by 0.1 per cent to 1.9 per cent compared to 2009, which is again relatively low compared to 2009 when inflation reached 1.8 per cent. Inflation increased primarily due to factors associated with the economic activity. According to the assessment of the Eurostat, consumer prices in the euro zone rose on average by 2.2 per cent in 2010.

The trend of deteriorating conditions on the labour market continued in 2010 as there is an increased discrepancy between the number of job seekers and employers which is reflected in the difference between the number of advertised positions and actual employment. In October, Slovenia recorded the highest unemployment rate in the past seven years. The unemployment rose in October mostly due to larger than usual seasonal inflow of newly registered unemployed. Unemployment rose to 10.9 per cent. Compared to the previous year, by the end of the year the number of registered unemployed rose by 13.8 per cent reaching a total of 110,021 unemployed by the end of December.

The Ljubljana stock exchange ceased the calculation of the LJSEX index (the successor of the SBI 20 and SBI indices) on 15 October 2010. This was replaced by the SBI TOP index. According to data published by the Bank of Slovenia (BS), bond market capitalization fell by 0.5 per cent on the Ljubljana stock exchange in December 2010 however, the interim rate was above the 73.3 per cent average recorded in the previous year. The annual volume of traded shares amounted to EUR 360.8 million in 2010. In December, the SBI TOP index grew by 0.9 per cent (although in interim terms it fell by 13.5 per cent), closing at 850 index points. In its first quotation, the price to earnings ratio (P/E) was 43.2 at the end of December. Monthly volume of traded shares reached EUR 45.5 million in December, which is the maximum amount recorded in 2010.

Banking Environment

Despite first signs of economic recovery, conditions in the banking environment further deteriorated in 2010. This was mainly due to increased credit and income risks as well as risk associated with refinancing. The balance sheet total of the banking system decreased in 2010 by EUR 1.323 billion (a 2.6 per cent decline) to EUR 50.290 billion. The major factor affecting decrease in the balance sheet total in 2010 was maturity of term refinancing within the Eurosystem, deleverage at foreign banks, tightened financing conditions and gradual withdrawal of government deposits.

The increase in the volume of lending in 2010 was lower than the previous year. Loans to non-banking sector grew by only 1.2 per cent and this is primarily due to loans extended to households. The volume of loans to non-financial institutions fell in 2010 by 2.6 per cent, as a result of the high increase in impairments and loan repayments.

The loan structure also changed in 2010. There was a decrease in short-term loans, while demand for long-term funding increased primarily in respect of large companies. There was no additional tightening of loan approval standards which is partly due to the fact that these standards were markedly tightened during the previous periods. Loans to households rose by 9.8 per cent as a result of increased mortgage demand in the local currency and relaxed tightening of loan approval standards. Loans to the government increased by 58.3 per cent or EUR 428 million in 2010.

Liabilities to the banking sector fell in 2010 by EUR 786 million, a decline of 4.9 per cent. In contrast, the volume of debt securities rose by 31.0 per cent, further increasing the borrowing of banks compared to the previous year. Deposits of the non-banking sector accounted for 46.7 per cent of total liabilities, or 75 million EUR lower compared to 2009. This reduction reflects a decline in government deposits, whereas household deposits rose on average by 3.6 per cent. In 2010, reduction in deposits by non-financial institutions is insignificant. There was also a decline in capital requirements which was contributed by low increase in capital requirements for credit risk as a result of the slackening of the loans to non-banking sector. Capital requirements grew primarily in relation to the local banks, whereas foreign banks recorded a decline in capital requirements. The volume of capital reduced by 3.3 per cent or EUR 141 million.

Increase in net interest in excess of the balance sheet total growth resulted in increased interest margin. Growth in net interest is the consequence of a 12.6 per cent reduction in interest expenses of the banking sector, whereas the 2.0 per cent growth in interest income in the banking sector is almost the same as it was in the previous year. Lower interest expenses are largely the consequence of lower deposit rates. There was no significant change in operating costs compared to 2009. In terms of interim decrease (comparing the two years 2009 and 2010), it reached 0.5 per cent, whereas the loss amounted to 48.0 million EUR. The loss was significantly affected by impairments and provisions which rose by 51.6 per cent compared to the previous year to EUR 757 million. Provisions were most significantly increased by a group of domestic banks.

3.2 Business Results

Financial Highlights

EUR '000

INDICATORS	31.12.2010	31.12.2009	31.12.2008
1. BALANCE SHEET			
Balance sheet total	2,187,844	2,331,730	2,262,014
Aggregate amount of deposits by non-banks	525,135	479,041	434,951
a) legal and other persons	336,254	304,192	258,776
b) retail	188,881	174,849	176,175
Aggregate amount of loans to non-banks	1,940,562	1,984,083	1,960,689
a) legal and other persons	1,389,004	1,468,833	1,477,854
b) retail	551,558	515,251	482,835
Total capital	166,619	194,446	204,422
Impairment of financial assets at amortized cost, and provisions	123,141	55,167	24,737
Off-balance-sheet items	570,226	772,663	661,677
2. INCOME STATEMENT			
Net interest	50,593	46,584	39,494
Net non-interest income	9,441	9,714	10,516
Labour costs, general and administrative expenses	21,566	22,718	21,479
Amortization/depreciation	1,967	2,000	1,759
Impairments and provisions	68,488	27,749	11,468
Pre-tax profit/loss from ordinary and discontinued operations	(32,404)	3,831	15,304
Income tax from ordinary and discontinued operations	6,113	1,118	4,350
3. PERFORMANCE RATIOS			
a) Capital			
Capital adequacy	11.26 %	12.11 %	11.31 %
b) Quality of assets			
Impairment of financial assets at amortized cost and provisions for commitments/reclassified items	5.10 %	2.29 %	1.12 %
c) Profitability			
Interest margin	2.39 %	2.05 %	1.77 %
Financial intermediation margin	2.83 %	2.48 %	2.39 %
Pre-tax return on assets	-1.53 %	0.17 %	0.73 %
Pre-tax return on equity	-16.56 %	1.89 %	8.25 %
Return on equity after tax	-13.44 %	1.34 %	5.91 %
d) Operating costs			
Operating costs/average assets	1.11 %	1.09 %	1.11 %
e) Liquidity			
Average liquid assets/average short-term deposits of non-banks	14.99 %	13.54 %	12.46 %
Average liquid assets/average assets	3.16 %	2.15 %	2.14 %
4. EMPLOYEES			
At year-end	403	396	389
5. SHARES AT YEAR-END			
Number of shareholders	1	1	1
Number of shares	41,706	41,706	41,706
Book value per share	4.00	4.66	4.90

Performance ratios are calculated using the Bank of Slovenia methodology.

Financial Situation

At 31 December 2010, **the Bank's balance sheet total** amounted to 2,188 million EUR, representing a 6 percent nominal decline as compared to 2009. Decrease in the balance sheet total of the banking sector reached on average 3 per cent in 2010 compared to an increase of 8 per cent recorded in the previous year.

In the **structure of assets**, the share of total loans accounts for 89.3 percent, a further slight increase as compared to the previous year. The share of loans to non-banks (88.7 per cent) accounts for the most significant share of the balance sheet structure and rose slightly over the previous year. Structural changes of other assets were very minor only reflected in a 1 percent drop in the share of loans to banks, while other assets retained the same share as in the previous year. Reduction in the share of cash with the Central Bank is of a transitional nature and represents a liquidity reserve as at the balance sheet date.

During the year the **structure of liabilities and equity** was changing, with the primary sources representing from 20 to 25 per cent share. The share of primary resources amounted to 24 per cent at the year-end. The structural capital share amounted to 7.6 per cent at the year-end.

Loans to banks decreased by 70 per cent in 2010 to EUR 14 million at the year-end, and at the same time the volume of cash on hand and balances with the Central Bank also decreased. At the end of 2010, loans to banks comprised A-vista deposits of total EUR 6 million, short-term loans of EUR 4 million and long--term loans amounting to EUR 4 million.

Loans to non-banks fell in 2010 by EUR 44 million or 2.0 per cent. However, despite the decline, they gained 3 percentage points in the structure of assets compared to the previous year. As at 31 December 2010, loans to non-banks amounted to EUR 1,941 million and include loans to the industry sector, the government, financial institutions excluding banks, and loans to retail clients, sole proprietors, non-profit service providers, loans to households and loans to non-residents.

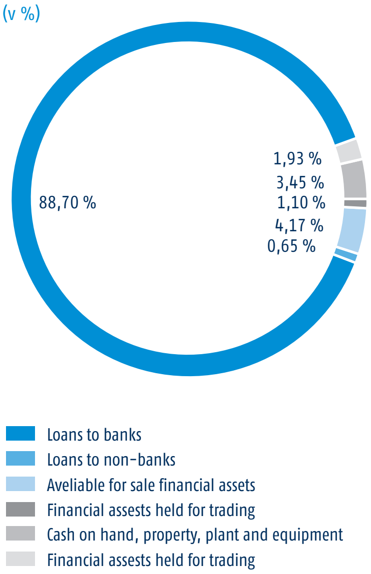
Financial assets held for trading decreased by 37 per cent in 2010 and reached EUR 24 million by the end of the year.

Available-for-sale financial assets remained at the level

Structure of assets

2010

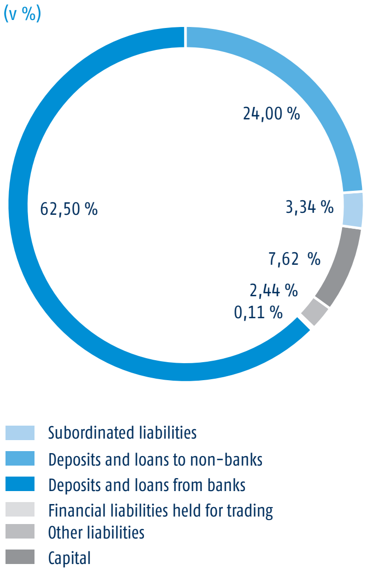
(v %)



Structure of liabilities and capital

2010

(v %)



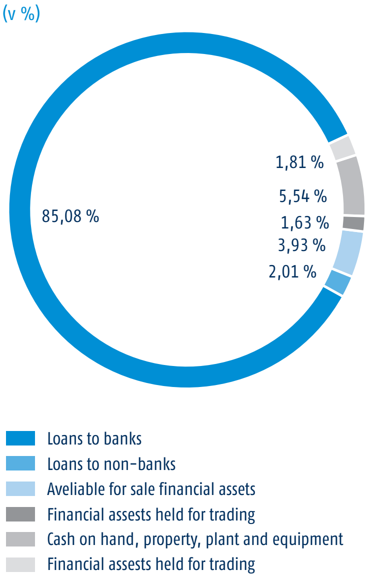
recorded in 2009. The portfolio balance at the end of 2010 amounted to EUR 91 million, accounting for 4 per cent in the structure of total assets.

Financial assets held to maturity increased by 0.5 per cent in 2010 or nominally for EUR 203 thousand. At the end of 2010 the portfolio balance amounted to EUR 42 million and retained its 2 per cent share in the structure of total assets.

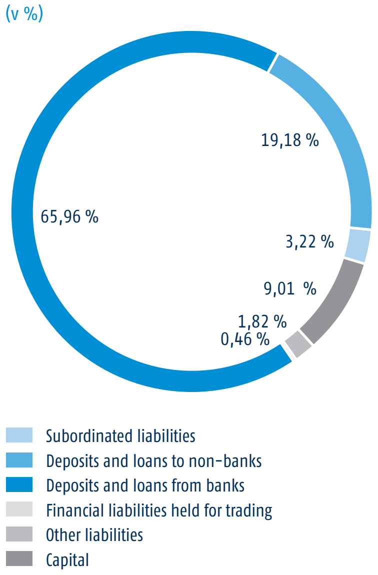
Financial liabilities to banks represent the largest share in the total structure of liabilities and capital with 65 per cent, and have, compared to the previous year, decreased by EUR 125 million. At the end of 2010 they amounted to EUR 1,480 million. These financial resources were mainly obtained from the parent bank, representing the key resource for financing the loans extended by the Bank in 2010. The majority of liabilities to banks represented deposits and loans in the aggregate amount of EUR 1,407 million. The subordinated liabilities amounted to EUR 73 million at the year- end.

Financial liabilities to non-banks increased by EUR 46 million or 10 per cent and amounted to EUR 525 million at the end of 2010. This increase is of great strategic importance, especially in times of difficult conditions on international monetary and capital markets.

Structure of assets
2009
(v %)



Structure of liabilities and capital
2009
(v %)



Financial Result

In line with the conditions in the Slovenian economic environment and reduction in the overall banking market, the volume of operations of the Bank decreased slightly in 2010 when compared with 2009.

The Bank's income of EUR 59,617 thousand represents an increase of 6 per cent compared to 2009. Administrative costs, labour costs and costs of depreciation and amortisation amounted to EUR 23,533 thousand , which is 5 per cent less than in 2009. The impairment of financial assets not measured at fair value through profit or loss and provisions for off-balance-sheet items totalled EUR 68,488 thousand at the year-end.

At the end of 2010, the result of the Bank's financial and operating activities was a loss of EUR 26,292 thousand and represents a significant drop compared to net profit of EUR 2,713 thousand reported in 2009. The reduction is largely due to additional impairment of loans, which increased by 123 per cent in 2010 as compared to 2009.

Net interest amounted to EUR 50,593 thousand at the end of 2010 and represents a 9 per cent increase over the previous year. Net interest income represented, with 89 per cent, the majority of total net income. In the net income structure, the share of net interest rose by 9 per cent, whereas the shares of net fees and commissions, and net result from financial assets held for trading decreased as a consequence of circumstances on capital markets and economic environment in 2010, and a more conservative Bank policy in this area.

Increase in the net interest rate resulted in higher interest margin which rose from 2.06 per cent in 2009, to 2.39 per cent in 2010.

In 2010, the Bank recorded EUR 911 thousand of dividend income; EUR 799 thousand of dividends from available-for-sale financial assets and EUR 111 thousand from financial assets held for trading. The dividends received in 2010 rose by 53 per cent.

Net received fees and commissions amounted to 8,055 thousand at the year-end and accounted for 14 per cent of the Bank's net income. Compared to 2009, they decreased by 5 per cent. In nominal and real terms, the major decrease was a consequence of reduced volume of fees and commissions from securities. The achieved net fees and commissions covered 37 per cent of the Bank's administrative costs, which is at the level recorded in the previous year. If only labour costs are considered, the coverage amounts to 61 per cent.

Realized loss from financial assets and liabilities not measured at fair value through profit or loss amounted to EUR 104 thousand at the end of 2010 and reflects a decrease in income from the sale of shares from the Bank book.

Net loss from financial assets and liabilities held for trading amounted to EUR 1,750 thousand, which is a rather large decrease in the result compared to previous year and is to a large extent a reflection of a rather modest volume of trading in shares in 2010 and also the result of trading in derivatives which was in terms of certain financial instruments highly influenced by a drop in prices on the secondary market.

The Bank realized EUR 761 thousand of net gains from foreign exchange differences against the loss of 238 thousand realized in 2009. This is a consequence of a significant exchange rate volatility experienced during 2010. Other net operating gains amounted to EUR 1,151 thousand, a decrease of 33 per cent as compared to 2009.

In 2010, administrative costs amounted to EUR 21,566 thousand, representing approximately 5 per cent decrease against 2009. A major portion of administrative costs is attributable to labour costs which accounted for 62 per cent or EUR 13,268 thousand. General and administrative expenses accounted for the remaining 38 per cent or EUR 8,298 thousand.

The depreciation cost amounted to EUR 1,967 thousand in 2010, which is EUR 33 thousand or 2 per cent less than in 2009.

The newly formed net provisions in the amount of EUR 4,192 thousand, represented provisions for net fees and commissions of EUR 30 thousand and provisions for off-balance-sheet liabilities in the amount of EUR 4,162 thousand. As compared to 2009, they increased by 64 per cent.

At the end of 2010, the net impairments of loans amounted to EUR 63,329 thousand. As compared to the previous year, the impairment of loans grew by 123 per cent. The off-balance-sheet total of adjustments of loan values increased by 123 per cent to EUR 115,784 thousand as compared to the previous year. This increase was largely attributed to additional formation of provisions as result of a more conservative policy of the Bank.

As a result of the realized loss, the assessed income tax for 2010 equals nil.

3.3 Bank's Operations by Segments

Corporate Banking

Strategy and Results of Operations in the Corporate Banking Sector

In 2010, economic recovery was extremely slow and uncertain. While export-oriented companies had already recorded growth, business was much slower for companies in the construction sector, real estate and financial sector. On the other hand, in 2010 the banks were subjected to more expensive sources of financing than in the years prior to the economic crisis. The consequences of this were a more conservative and cautious lending policy that resulted in a decline in lending to clients in the Corporate Banking sector. At the end of 2010, Slovenian banks reported 0.7 per cent decline in loans to corporates as compared to 2009.

The volume of loans approved to clients in the Corporate Banking sector by Hypo Alpe-Adria-Bank in 2010 fell by 2.5 per cent against the volume reported in 2009. Irrespective of this, increasing the market share of the loan portfolio remains the objective of this sector also in the future.

Increasing the share of non-interest income in total income of the sector, remains one of the key orientations of the sector. In 2010, non-interest income from the Corporate Banking sector amounted to EUR 5,357 thousand, which accounts for 51 per cent share of total non-interest income of the Bank. An increase will be achieved mostly by cross-selling of the remaining products (payment transactions, investment banking, derivatives, documentary businesses, and leasing services) and by strengthening the existing and introducing new products or services.

In the Corporate Banking sector, client deposits represent an important element in managing the Bank's liquidity. At the end of 2010, the volume of deposits rose by 9.0 per cent as compared to the end of 2009. In terms of deposits we expect a fair amount of »reserve« from eDepozit service, which we believe will strongly contribute to even better results of the Bank in this sector.

We succeeded in capitalizing internal reserves and further reducing costs of the sector. The cost/income ratio was therefore reduced from 17.0 per cent to 14.2 per cent.

The project of introducing a single strategy of the Corporate Banking sector to the entire Hypo Group characterized a large portion of 2009 and established a solid foundation for further operations. In 2010 we already felt some positive results in improved transparency of operations as well as in other areas.

The strategy of client relations management is one of the key factors of success and further successful operations of the Bank in the Corporate Banking sector. The key element of this strategy is precise task definition for managers of individual clients and groups of related companies (so called, global client trustee). The objective we pursue is deepening of our relations with clients and developing long-term partnership cooperation with them.

Distribution channels

One of our important competitive advantages remains cross-selling of various banking services within the Bank and within the Hypo Group Alpe Adria in Slovenia, which consists of our Bank and Hypo Leasing d.o.o.

Business cooperation with our sister banks within the Hypo Group Alpe Adria, which runs through the so called Hypo Group Network, is the added value which we can offer to our clients. The Hypo Group Network was established as a joint project of banks and leasing companies in the Hypo Group Alpe Adria with the purpose of helping the clients in the Hypo Group Alpe Adria to establish business partnerships in the Alpine Adria region.

The development of information technology also had an effect on banking, in that the traditional model of banking operations, carried out through branch offices, is increasingly being replaced by modern banking channels which use electronic communications between bank and client. Marketing of banking services with direct contact between bank adviser and client will continue to play an important role in deepening and developing of long-term partnership cooperation with our clients. Development of modern banking channels will enable the Bank to obtain also those clients who prefer such type of operations.

Objectives for 2011

We will continue our successful operations of the Corporate Banking sector of the past years also in 2011. We build our competitive advantages on solid foundations, which we established with a clear strategy, directed to:

- Acquiring new clients in the sector of small and medium-sized companies
- Offering structured services (cross-selling of combined banking services suitable for our business partners);
- Increasing the number of services per client; increasing the number of opened transaction accounts, increasing the volume of payment transactions with existing clients, increasing the market share in the area of letters of credit and deposits;
- Developing experienced and professional employees; and
- Adapting business processes and their optimization.

Retail Banking

Business Strategy

In Retail Banking, the Bank continued strengthening its relations with individual client segments and focusing on personal services, in accordance with a new business strategy which was introduced in 2009.

The results of changed strategy in dealing with retail clients can be observed in the number of products sold per client, per employee, and individual branch office. With this new strategy the Bank succeeded in raising the ratio of sales per client from 2.13 in 2009 to 2.26 in 2010. Accordingly, profitability per client also increased. Commission income on account of increased number of products per client and increased frequency of the use of individual products rose by over 16 per cent in 2010 as compared to 2009. The largest increase in commission income was recorded in relation to payment transactions, transaction accounts and card transactions.

Increased use of MasterCard debit and credit cards is the consequence of the introduction of the loyalty programme which the Bank began to actively market in 2010. The objective of the loyalty programme is to increase the volume of non-cash transactions and, by awarding points for credit card purchases, reward the clients' loyalty. A loyalty awards catalogue included services offered by the Bank as well as benefits which the Bank provided in cooperation with its contractual partners. What is particularly encouraging is the fact that, to a large extent, clients took advantage of these benefits to purchase, as a special offer, one of the products offered by the Bank in its loyalty awards catalogue.

In 2010, the Bank continued actively marketing its services of Private Banking offered by means of »Exclusive« package to its most demanding clients. The service was improved with the inclusion of legal advisory services, services of asset management and networking among clients themselves. At the year-end, the number of clients in the Private Banking segment exceeded 80 clients.

As with Private Banking, the Bank's objective in terms of transactions with Micro Enterprises and Sole Proprietors, was to increase the number of products sold per client and improve profitability of transactions per client. Both these objectives were achieved as commission income from this segment rose by more than 16 per cent.

The Bank's business strategy was based on increased versification of its credit portfolio by means of intense sales of consumer credits through introduction of new credit agents, by which the Bank secured increased interest margin and reduced risk through appropriate collateral.

During 2010 we cleared databases of inactive clients in the segment of Private Banking as well as the segment of Micro Enterprises and Sole Proprietors. By clearing these databases, the Bank has secured solid grounds for more active marketing of its services and real increase of active clients in the future.

Distribution Channels

In 2010, the Bank upgraded its network of distribution channels by introduction of new loan agents, especially in the area of car and furniture sales.

Based on the profitability analysis, the Bank reduced the number of automated teller machines in 2010 and began closing down those ATM's which did not achieve the minimum number of transactions per day. In doing this, the Bank followed the objective of cost efficiency of this distribution channel.

The e-bank HYPOnet was upgraded with services which were not available in the past. These include some types of deposits, savings, transaction review and introduction of a new UPN form that enables clients to make payments in the SEPA system. The most important acquisition of the e-bank was introduction of 3 D Secure, which ensures more secure payment of services by users of charge cards.

Service Development

The Bank included in its offer of service to private clients also financial leasing of movable property. The service, which was introduced in branch offices where the representative of leasing is not present, was provided under a leasing agreement concluded with Hypo Leasing.

Furthermore, at the end of 2010 the Bank obtained its licence for mediation in trading in gold and other precious metals. The Bank will begin trading in these services in 2011.

The Bank added the »Hypo plus fix deposit« to its saving products, which enables monthly savings with lower deposits on a long-term basis at fixed interest rates.

In the first phase of gradual modernisation of the credit application, the process of documentation transfer to back offices was shortened and the overall process from loan approval to payment is now much faster.

Objectives for 2011

The introduction of Maestro corporate card, which was not implemented in 2010, will be our priority in 2011.

The Bank's credit application will be further upgraded to enable electronic approval of loans, fusion of a variety of applications that are an integral part of the loan approval process and shorten the whole approval process, which will be reflected in reduced operating costs.

The Bank will introduce new »sweep« service and combined deposit and saving product to its range of savings products in cooperation with Grawe insurance undertaking.

For payments with MasterCard charge cards, the Bank is planning the introduction of a pre-payment card and sms security notices.

Special attention will be devoted to the development of services offered to Micro Enterprises and Sole Proprietors as well as to Private Banking clients.

Our principal objectives are to continue with the increase of the number of clients in all segments, the number of transaction accounts, and active sale of all types of products.

Financial Markets

Investment Banking

In terms of investment banking, in 2010 the Bank registered a drop in revenue as compared to 2009. The reasons are to be found in poor liquidity on the market, lack of interest of local investors in financial markets, and primarily, in fierce economic environment in Slovenia. The Bank's market share in the total volume of trading on the Ljubljana Stock exchange amounted to 1.97 per cent. In June, the Bank again introduced asset management services, offering its clients 4 different investment portfolios (in terms of their preference and profiles). In this particular segment, major focus will be placed on marketing activities also in the future. Towards the end of the year we offered portfolio optimization to our clients with the aim of restructuring portfolios – directing investments to markets with high potential for growth and better liquidity.

In 2011, major emphasis will be on increasing income from brokerage on foreign markets (portfolio optimization), introducing custody services (for major domestic and foreign investors), sale promotion with direct marketing, introducing new e-services for clients and, in particular, increasing the number of clients and assets in the asset management sector.

Trading

The year 2010 was not as successful for the Trading sector as was 2009. Whereas the number of clients increased, the volume of transactions and income decreased. Poorer performance of this sector is to a large extent due to difficult conditions on financial markets that deterred corporate clients from engaging in treasury transactions. In 2010, we continued with some existing projects and began developing new strategy of cooperation with clients. We continued to expand our range of services aimed at protecting against financial risks, and additionally strengthened our cooperation with the Corporate Banking sector and our sister company Hypo Leasing d.o.o. In the beginning of the year we began implementing a new sale strategy which is founded on quality processing of clients with emphasis on providing advice and searching for the right solutions. New sale strategy has already »reaped the fruits« as the response of clients is very positive and the number of transactions as well as realization, have both increased.

In 2011, we will focus our attention on cooperation with clients, directed towards giving quality advice and ensuring long-term cooperation; we will expand our database of target clients, and strengthen our analytical and advisory activity.

We will further consolidate our cooperation with Asset Liability Management, Corporate Banking and Credit Risk sector as well as with our sister company Hypo Leasing d.o.o. The Bank will continue to implement new instruments that will contribute to even better solutions for our esteemed clients. Great emphasis will be placed on training and education of our employees. Our aim for 2011 is to be among the top three Banks in Slovenia in terms of income and quality of services.

Asset Liability Management

In 2010, the Asset Liability Management department was responsible for assurance of the Bank's liquidity, the management of banking and trading book, as well as assets and liabilities management (ALM) in terms of the currency and interest rate risks. In 2010, the information system for overall management of liquidity risk was implemented and we began upgrading processes for the management of banking book and financial risk management.

Transaction Banking
Payment Services

The incorporation of Slovenia into the European payment systems brought numerous changes and activities in the sector of payment operations for the Bank. As early as in 2008, we signed the agreement to join the SEPA payment schemes with the help of the Bank of Slovenia, which provided availability, and on 28 January we ensured, as an indirect participant, fulfilment of obligations for the accession to the credit payments scheme. Thus we have provided clients with the option of SEPA cross-border payments of up to EUR 50,000 since 28 January 2008.

In 2009, these transfers were migrated to the new, so called SIMP (Sepa infrastructure small value transfers) infrastructure via Bankart. These transfers are called SEPA EKP (SEPA external credit transfers).

By establishing SIMP in Slovenia in 2009, we established an infrastructure also for the domestic clearing and settlement of SEPA credit transfers, which started operating on 4 March 2009. This system is called SEPA internal credit transfers (SEPA IKP), which enables execution of domestic small value (up to EUR 50,000) credit transfers among the system participants.

We joined the system immediately and thus offered our clients domestic SEPA credit transfers, which are executed 5 times a day in known settlements. The migration of payments from the Giro clearing system to SEPA IKP was finished on 31 July 2009, when the Giro clearing system officially stopped operating.

In 2010, we successfully executed the migration of payments with standing orders to SEPA IKP system. On 1 November 2010, we successfully introduced a universal payment order which will gradually replace a special payment order. Also in 2010, we began developing the e-Invoice project which we have successfully completed by the end of the year. The aim of this service is to provide e-Invoice services from the payer to the issuer.

Since 1 November 2010, we provide clients with the availability of cross-border direct debits.

In 2011, we will continue our efforts in the area of SEPA credit transfers by the migration of payments with standing orders and special payment orders to SEPA IKP system. Furthermore, we will actively continue with the SEPA direct debit project in accordance with the national SEPA plan.

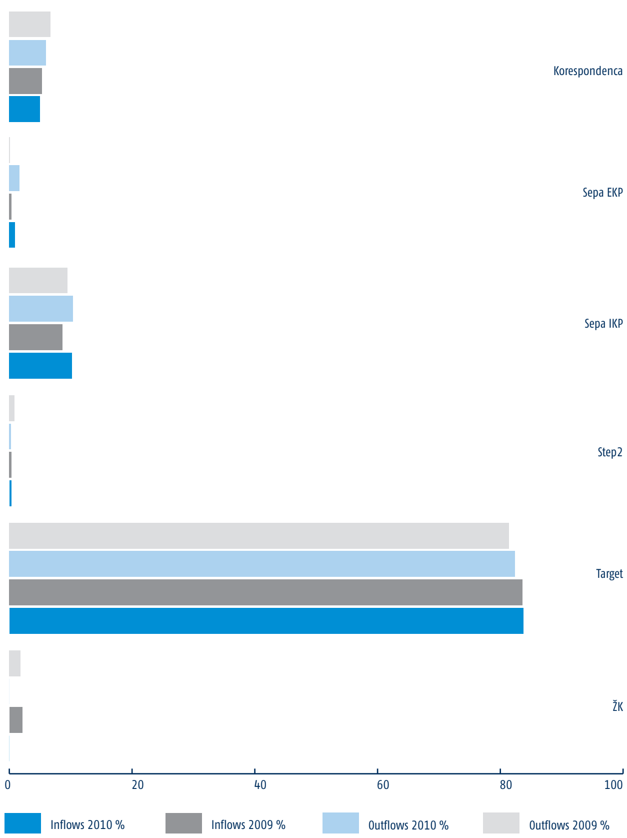
The volume of domestic payment operations in 2010 amounted to 3.3 billion EUR in SEPA IKP system, which is 25 per cent more than in 2009 in terms of the volume, whereas in terms of the number of transactions, we recorded an 11 per cent growth in inflows and 5 per cent increase in outflows. In 2010, the volume of payments into the TARGET2 system amounted to 26.6 billion EUR, which is an increase of 11 per cent as compared to the year 2009.

In SEPA EKP system, the percentage of executed transactions rose significantly from 78 per cent of total executed transactions to 95 per cent. This shows that clients are aware of the benefits and have taken advantage of dividing payments to EUR 50,000. In spite of this increase, in terms of the volume, around 83 per cent of all transactions are executed through the TARGET2 system.

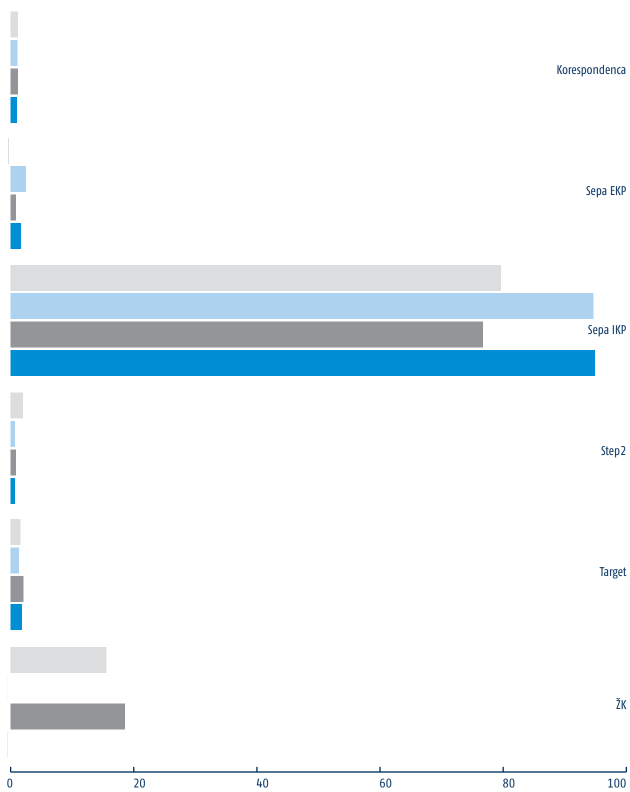
In SEPA EKP system, the volume of payments amounted to EUR 482.5 million in 2010, which is a 5 fold increase over 2009. In the STEP2 system, the Bank executed EUR 142.4 million, which is 55 per cent less than in 2009. These data show that payments are sufficiently swiftly transferred from STEP2 system to SEPA EKP system.

The Bank is still executing approximately EUR 1.73 billion through correspondence network and within the Hypo Group which is similar to the volume executed in 2009.

The amount of transactions



Number of transactions



The quality of Bank operations in the area of other payment transactions depends considerably on good cooperation with other banks in the Hypo Group as well. Connection between the Banks in the Group and their mutual cooperation concerning the satisfaction of client's needs and demands is provided by Alpe-Adria coordinators, appointed in each country for this purpose. This kind of cooperation provides the client with fast service, which gives the Bank an important competitive advantage. In addition to the personal approach and quick response to client's needs at any bank in the Group, cheaper payment transactions for the client's operations within the group Hypo Alpe-Adria-Bank are also a competitive advantage.

Bank's Internal Development

In the financial year 2010, the Bank concluded many projects that complement the existing systems of the Bank's management. In terms of the business strategy execution, the Bank continued the development of new services, while at the same time improving the processes of risk management (the project of renovation of the credit process, the project of survey and analysis of the Bank's business processes, introduction of new rating tools, renovation of tools for the management of operational risks, etc.). Furthermore, in the area of information technology security, the Bank followed the principles of good practice and continued procedures for maximum consolidation with recommendations of the competent institutions.

In accordance with the Decision of the Bank of Slovenia on business books and annual reports of banks and savings banks, the Bank discloses that, in 2010, it kept regular accounts and carried out all services, which are covered by the issued licences of the Bank of Slovenia. The Bank keeps in its regular offer to clients all services that are in accordance with the Bank of Slovenia licences.

In the financial year 2010, the Bank also obtained a licence for intermediation in trading with precious metals, so that it can, on the basis of licences granted by the Bank of Slovenia, perform the following services:

- acceptance of deposits,
- giving loans, including:
  - consumer loans,
  - mortgage loans,
  - financing of receivables on a recourse or non-recourse basis (factoring),
  - financing of commercial operations, including export trade financing on the basis of discount financing without recourse for long-term non-matured receivables, insured by financial instrument (forfeiting),
- transaction operation services according to Payment Transactions Act, except for services of transaction systems management,
- issue and management of payment instruments (for example credit cards and travellers checks),
- issue of guarantees and other pledges,
- trading for its own account or for the clients' account:
  - with instruments of monetary market,
  - foreign means of payment, including exchange operations,
  - standardized futures and options,

    - with interest rate and currency financial instruments, with transferable securities,
- cooperation in issuing of securities and related services,
- consulting and services related to mergers and acquisitions of companies,
- investment management and related consulting,
- credit reference services, collection, analysis and transfer of information on credit worthiness of legal persons; rental of safes;
- investment services and operations (the permit includes services of accepting and intermediation of orders related to one or more instruments, carrying our orders on behalf of clients, management of financial instruments, investment consulting, realization of first and further sale of financial instruments, with the obligation of buyout or without this obligation), and auxiliary investment services and operations (the permit includes services of keeping financial instruments for the client's account, investment research and financial analysis or other forms of general recommendations related to financial instruments operations, services related to realization of first or further sale of financial instruments - with the obligation of buyout, and services and operations of the same kind as investment and auxiliary investment services that are related to basic instruments of derivatives) in accordance with the Financial Instruments Market Act,
- intermediation with the sales of insurance policies according to the insurance legislation,
- intermediation in financial leasing,
- intermediation in trading in precious metals

Business Network

The business network of the Bank has not expanded compared to the previous year; the Bank has 18 branch offices in 14 locations. In financial year 2010, the Bank began and completed partial renovation of its branch offices in Novo mesto, Domžale and Maribor.

Informatics

In 2010, the Informatics sector, which is responsible for maintenance, development and sector availability of the information system of the Bank, devoted most of its attention and time to the development projects. Great importance was also dedicated to activities aimed at ensuring continuous operation of information technology infrastructure in crisis situations.

We joined the Business Informatics department and the Development Process and Technology department into the Business Informatics and Technology Department, where we established three teams separate in terms of the content. We transferred a part of the team into the Data Management department. This way we simplified the internal flow of information among departments, and joined expert or business contents inside individual teams.

In the area of development, we focused our operations on reducing the number of minor developmental claims and on putting emphasis on project development approach.

As regards legislative and regulatory requirements, the key adjustments were made in the areas of ECB reporting, SEPA environment (UPN order), reporting to SISBON (in accordance with ZBAN3), and providing support to the Consumer Credit Act.

In the area of software development, we developed a new solution for syndicated loans, stock brokerage support in Xetra environment, and e-invoices within the e-bank.

We also introduced software improvements for the needs of RISK and credit rating service.

In the field of system and communication management, we expanded the segment of business applications in the centre of reserve capacities, and carried out documentation procedures and trainings of employees for work in the centre of reserve capacities. Several drills of individual system and entire system shutdown were also made and successfully completed.

Logistics

For 2010, the Logistics division planned the establishment of one new branch office in Ljubljana (Moste), which is planned to open in the first quarter of 2011. Furthermore, in the same period, two existing branch offices in Maribor and Koper are planned to be moved to new locations in the city centre.

In 2010, there were also activities taking place on projects, which will continue in 2011. Among these, it is necessary to highlight the e-archiving project, within which Internal rules, which provide the Bank with e-archiving service and elimination of documentary materials in paper form, were created.

3.4 Expectations for the Future

The Bank sees its opportunity as a strategic market of one of the most important financial groups in the Alps-Adriatic region. The objective of Hypo Group Alpe Adria is to continue with its growth, development and integration in this geographic region. To our clients, the capital and financial strength of the banking group represents higher reliability and security, and a possibility of broader support and in-depth cooperation. However, the integration in financial group brings also many other advantages and synergies to the Bank, involving the domain of the transfer of know-how, technology, and utilization of the international business network, as well as the domain of acquisition of new business partners. At the end of 2009, the international financial group Hypo Group Alpe Adria came into 100 per cent ownership by the Republic of Austria. Improved capital and financial strength of the Group has enhanced the long-term security of investors and established the basis for further growth and development.

The Bank retains the concept of a universal bank and also in the future plans a harmonious and stable growth of operations in all business sectors, as well as continued gradual development of the branch network. Thereby, the Bank will endeavour towards increasing versatility and quality of its services, and will pursue the principles of security and operational profitability. The commitment of the Bank to create a secure and reliable environment is a fundamental starting point for all activities of the Bank.

In the next mid-term period, the Bank will continue with the strategy of independent, organic, yet ambitious growth of its operations. By the end of 2013, the Bank aims to achieve a 6 per cent market share according to the aggregate balance sheet total of the Slovenian banking sector, and be ranked high – among the first five banks in terms of respect, market share and profitability. The Bank intends to retain the existing high structural share of loans and, along with the growing business volume, maintain an adequate level of the portfolio quality. At the same time, the Bank will considerably strengthen the collecting of assets or deposits from non-banks. Special attention will be devoted to retail banking and to small and medium-sized enterprises.

The key objectives of the next period are as follows:

- Increase the business volume,
- The growth of profits and profitability as the long-term target,
- Gradual increase in return on equity indicator,
- Further development of the active process of the asset liability management (ALM), i.e. active interest and currency positioning of the Bank in line with the anticipated market developments,
- Increase in the quality of the existing products and, in line with the market demands, development of new ones, which are already offered or will be offered by the Bank to the existing and potential clients,
- Adjusted expansion of the business unit network and smaller branch offices within the scope of individual business units,
- Comprehensive offer to clients in all banking sectors and utilization of effects from cross-selling,
- Improvement of responsiveness and adaptability of the Bank to the environmental changes,
- Improvement of the internal business efficiency.

Key success factors are as follows:

Development of services and products	We are quick to follow and a niche leader.
Sales	We take care of continuously obtaining new clients and of having the largest number of sold products/services per target client.
Organization and operating processes	We take care of continuously adapting to the growth and development of the Bank
Information support	We support transparency and effectiveness of operations.
Leadership	We support target leadership with authorizations and responsibility on all levels.
Human resources	We take care of the systematic development and learning of all employees.

The Banking activities will be primarily oriented towards Retail Banking sector, as well as Micro Enterprises and Sole Proprietor sector. The Bank will keep its role in housing financing, and it will actively expand the activity also to other types of loan financing. Special attention will be devoted to the collection of deposits in domestic currency and an increase in the number of holders of transaction accounts, as well as to the development and upgrading of personal banking services, along with constant expansion of the volume and quality of the offered services related to insurance, mutual funds, savings, mobile banking, and internet banking. The attention and concern devoted to our clients will be reflected in the business policies, customized to different client profiles, organizational restructuring, and further automation of operations. Further contributions will come from the utilization of synergies of the Hypo Group Alpe Adria, from a large network of subcontractors, sale of insurance policies, of the Hypo Group funds, funds run by contractual partners, as well as from further expansion of the branch office network.

In the Corporate Banking sector, primary emphasis in 2011 will be laid on Medium Enterprises and the higher segment of Small Enterprises, which represent the major market potential. Since also in the future, our major concern will be devoted to the maintenance of the quality portfolio, we will continue activities oriented towards the completion of insurance portfolio. Moreover, we also expect an increase in the volume of operations with the public sector, which will ensure an appropriate growth of the balance sheet total at a relatively low risk. An important target will be the expansion of the volume of payment transactions through collection of new transaction accounts and documentary operations. The Bank's Financial Market sector will develop and offer a set of derivatives in order to manage the interest rate and currency risk. The organizational structure will gradually adapt to the new business policies by sectors, the processing of the Bank's clients will be upgraded by the customized approach, the automation of operations will further continue, whereby the Bank's adaptability to the client's needs will remain, to the greatest possible extent, unchanged.

3.5 Social Responsibility

At the Bank, we are aware of the fact that responsibility for our activities, with which we influence our internal and external environment, is of crucial importance. Thus, we feel our responsibility and care for employees, owners, clients, community and supervisors.

Responsibility to Employees

Care for our employees is one of the Bank's values, which has become even more meaningful in the time of the difficult economic situation. We concluded the year 2010 with 403 employees, representing a small increase in the number of employees compared to the previous year. In 2011, we plan to further increase the number of employees to 414.

Movement of employees during the years is shown in the table below:

Year	No. of employees as at Dec 31
2007	333
2008	389
2009	396
2010	403

Recruitment and selection

The recruitment and selection of new employees are supported by clearly defined requirements and targets of an individual organizational unit. Priority is given to the internal labour market, and the desires and ambitions of employees are taken into account. The selection of employees is systematized in several circles of structured interviews carried out with the job applicants. Where certain job positions are concerned, the candidates have to undergo testing by a professional external partner. The final decision is made on the basis of the analysis of their expertise and personal competences needed for successful performance on a specific post.

Education and training

In the Bank, there is constant need for new expertise, as well as for knowledge from the field of personal development, because we want to follow the new development dictated by the market. Each year, more employees participate in educational training, as compared to the previous year. To achieve business objectives, we have set key educational domains for the development of banking business which arise from strategic requirements.

Each year, we organize various internal trainings in accordance with our needs. In 2010, we carried out training on recovery, some product and process trainings and continued with language courses. For all employees that join the Bank during the year, we carry out a training called HYPO 1, which is intended to present all the Bank's sectors and concludes with an exam.

Certain internal trainings are also organized by the Hypo Group, namely from the areas of managerial staff training, as well as for specific work fields, such as project management. These trainings are especially useful because they allow exchange of experience and flow of knowledge within the Hypo Group. In 2010 we organized, with the parent bank, 7-day training course entitled Business risk analysis and Corporate finance, which were attended by all employees from the Risk Management sector, Corporate Banking sector and many others.

Besides internal trainings, employees often participate in seminars, conferences or debates, organized by the Bank Association of Slovenia or other relevant institutions. In t2010, some of the employees passed the exam or obtained the licence for insurance intermediaries and for the sale of investment coupons or shares of investment funds. Besides the above-mentioned, the Bank often co-finances the part-time studies or acquiring of different licences in the financial field.

The employees transfer the knowledge, obtained through education or self-education, to their colleagues, or they themselves hold lectures on seminars or they publish expert articles.

The education structure of the Bank employees is at a very high level, since more than 58 percent of the employees have higher or university education, as shown in the table below.

	Employees
Level of education	No. of employees by level of education in 2010
IV.	3
V.	163
VI.	26
VII./1	91
VII./2	108
VIII.	12
31. 12. 2010	403

Competency leadership model

Also in 2010, we carried out an evaluation of leaders' conduct on the basis of a competency leadership model. The evaluation itself was composed of self-assessment, assessment of the leader's superior and assessments of all subordinate colleagues. The leaders thus received feedback information, and were able to analyse their strengths and weaknesses at the strategic workshop, thus designing a plan for improvement on a personal level.

Leadership is a skill, which can be improved by an individual over a longer period of time. The progress of each leader will be monitored each year also in the future. Quality leadership is one of the key factors of success.

Yearly interviews and management by objectives

The aim of yearly interviews is to ensure, on a long-term basis, successful operations of the Bank. Yearly interviews enable us to systematically set new targets, to review the implementation of the agreed targets in the previous year, and to provide for systematic professional and personal development of the managerial staff and associates. The yearly interview is first held by the head with their superior or the Management Board, and is followed by an interview of the head with the subordinates. After the conclusion of the interviews, the head and the subordinate are responsible for the implementation of the agreed targets, while the human resources department provides for the organization of agreed trainings and implementation of the development plans in line with the strategy of the Bank. Target interviews are being held twice a year and development interviews once a year.

Remuneration system

The variable component of remuneration is divided into group, individual, and project remuneration. Individual remuneration is closely linked to management by objectives. By applying individual and project remuneration, we want to incite the development of an individual employee, while the group remuneration aims at better motivation for team work and achievement of targets. Even though we have fewer assets for remuneration than in the previous years, we believe it is important to keep the remuneration system, which contributes to more successful operations of the Bank.

Having future in mind, we include our employees in the collective voluntary pension insurance.

Measuring of organizational climate and satisfaction

In 2010, for the fourth time in a row, we included all employees in the measurement of organizational climate and satisfaction. In the Bank, we are aware that employees cannot be motivated only externally, but that such atmosphere and conditions can be created, that contribute to the well-being of the employees and to successful achievement of objectives. As expected, the results of measurement were lower than in the previous year, reflecting both the internal and external environment in which we operate. In the present time of major challenges, it is very important to know about our advantages, as well as opportunities for improvement. We will continue to use the instrument for organizational climate and satisfaction measurement also in the future, because we want to continuously improve the working environment of our employees.

Informal socializing also contributes to the well-being of employees; therefore the Bank organizes a New Year party each year. By donating, the Bank actively contributes to the development of Hypo Sports and Culture Association, which enables its members to participate in chosen sports and cultural activities at very favourable prices. By doing this, we strengthen the connection and cooperation of employees also outside of the working environment.

Plans for future

In 2011 , we will continue with development and upgrade of the human resources function in the Bank. We plan formation of competency model for all marketers of the Bank, based on which we will organize trainings of marketing skills and assessment of marketers' conduct. In terms of education and development projects, we increasingly cooperate with sister company Hypo Leasing d.o.o.

Responsibility to Owners

Responsibility to the owner is expressed by daily communication with them, regular monthly reports, publishing of annual report and cooperation with the Supervisory Board. The Bank has a single owner, to whom it used to pay the total profit after taxes decreased by statutory reserves totalling five percent of the profit until 2009. However, in 2009, the Bank transferred the total realized profit to reserves and did not pay out dividends. In 2010, the Bank failed to realize the profit.

	2010	2009
Dividend payout in thousand EUR	0	0
Dividend payout per share in EUR	0	0

Responsibility to Clients

The Bank demonstrates responsibility to its clients through a wide range of its products and services. The relations between the Bank and its clients are based on trust and understanding of the client's needs. The Bank adapts to clients' needs by improving the existing and developing new banking services through modern business channels and approaches. In operations, the protection of the client's personal data and client's rights present one of the most important principles of the Bank. Of course, along with that, the soft factors of cooperation, aimed at keeping the clients or further improving the professional relationship with them, are of key importance. One of such approaches is the organization of various events for clients (of cultural, sports or business nature), by which we demonstrate our appreciation for their trust and loyalty.

In accordance with the banking legislation, the Bank guaranteed for the payout of the banking deposits in the sum of EUR 22,000 until 11 November 2008. After that date, the banks, savings banks and the Republic of Slovenia guaranteed for unlimited net deposits of investors until 31 December 2010. As of 1 January 2011, such guarantee applies for the payout of the banking deposits totalling up to EUR 100,000.

EUR '000

	2009	2010	Index 10/09
Advertising expenses	613	674	109

Responsibility to the Wider Communities

The resources that the Bank dedicated to sponsorship and donations in 2009 and 2010 are presented in the following table.

EUR '000

	2009	2010	Index 10/09
Sponsorships	235	263	112
Donations	165	69	42

With its branch offices across the country, the Bank is present on the entire territory of Slovenia. Therefore, we nurture the relationships with local, as well as with wider social environment. We maintain our integration in the social community through sponsorship and donation activities in the humanitarian, sports and culture fields.

The Bank dedicated 16 per cent of the total resources for donation and sponsorships to humanitarian activities. We regularly work with the Association of friends of youth of Slovenia with donations for the families in need throughout Slovenia or in towns where our branch offices are located.

At the initiative of dr. Gottwald Kranebitter, President of the Management Board of Hypo Alpe-Adria-Bank International AG, we started with the project called "Hypo pro future", which operates as social and cultural network in seven European countries, where Hypo is present.

Each company of the Hypo Group selected a humanitarian project to help children in their country with a special, one-time donation. We are aware that there are too many children who never come to see the sunny side of life; hence we want to bring a smile to their face. In Slovenia, we decided to support the project "Let's enjoy childhood vitality on the snow" – a winter camp for children from socially deprived families. Donation by Hypo Slovenija ensured them accommodation in Kranjska Gora, teacher attendance and organization of entertaining and animated workshops to enrich days and evenings.

This project was also supported by the OK Pokal Vitranc, which has been our partner in the sponsorship area for many years. At one of the meetings of the Board of parallel activities organization, an initiative was made for a humanitarian activity on the occasion of such a jubilee. The idea of ski school for 50 children was quickly connected with the already planned project with the Association of friends of youth of Slovenia. The Pokal Vitranc presented the activity to other donators – ASK Kranjska Gora, RTC Žičnice, Intersport Bernik, Šport Point, who cheerfully agreed with the initiative. ASK Kranjska Gora provided ski teachers and transportation for children, RTC Žičnice contributed ski passes for the entire duration of ski school, and Intersport Bernik and Šport Point ensured free hire of complete ski equipment.

With this deed, the donators proved that the saying "unity makes strength" is true, as we all contributed to a more quality life of these children, even if for just a few days. The main donator of this project is the Hypo Group, which is also the biggest local sponsor and official financial partner for the 11th year, thus proving that quality cooperation of two business partners brings benefit not only for the two of them but such cooperation is reflected also in socially responsible behaviour.

The Bank intended 70 per cent of its total donation funds for ensuring better living conditions to socially deprived families. We made these donations through the Association of friends of youth of Slovenia.

We understand the support of sports and sporting activities as our contribution for healthier and better quality life. With sponsorship funds, we are included in the lives of those who represent our country in Europe and worldwide. In this way we demonstrate our support to athletes, their endurance, discipline, competitiveness, and desire to accomplish goals. Thus, the Bank dedicated 17 per cent of all donations to sports activities. We also supported with sponsorship funds the Slovenian football team, the fastest Slovenian Matic Osovnikar, the event Pokal Vitranc and other local sport events and athletes. To them, we dedicated 83 per cent of total sponsorship funds.

With its donation and sponsorship contributions, the Bank is actively involved also in the cultural happening in the Slovenian area. Help and support of cultural events, festivals and performances is becoming a part of our activities. By donating, we express our support to cultural activity as one of the most important spheres of social life. In these cultural events, we also include our clients, thus adding value to our relationship with them. In 2010, 4 per cent of our donation funds and 11 per cent of sponsorship funds were allocated to cultural activities or organizations.

Responsibility to Supervisors

In accordance with the Banking Act, the supervision of banking operations is carried out by the Bank of Slovenia within the framework of reviews at the supervised bank's headquarters and through reports that the bank sends regularly each month. This way, permanent supervision over banks and savings banks is assured, which enables the safety and stability of the financial system in Slovenia.

Within the framework of cooperation with the financial system supervisory institutions and external auditors, the Bank obtains appropriate assurances that its operations are within the framework of the legislation of the Republic of Slovenia and within the framework of general norms, in effect for well-regulated and stable members of financial system. The Bank builds the cooperation with institutions on an open and fair relationship, which leads to cooperative search for solutions. This, according to independent supervisors and consultants, assures long-term stability of the Bank's operations. In case of substantial changes in the systems of the Bank's operations, the Bank attempts to obtain in advance positive opinions on the planned solutions, which it intends to implement in its operating environment, with the purpose of obtaining reassurance, that these are in accordance with the legislation, and that they do not present significant threat to the Bank's development. In the framework of cooperation, the Bank strives to obtain independent opinions for all key risks from at least one independent body. The costs of auditing and consulting services, which the Bank hired in 2009 and 2010, are presented in the following table.

EUR '000

	2009	2010	Index 10/09
Auditing and consulting costs	249	211	84

The biggest share of the above costs represent the costs of the annual supervision of the Bank of Slovenia and The Securities Agency. The share of costs intended for the assurance of independent supervision of the Bank in the total administrative costs of the Bank represents 0.97 per cent.

Internal Control System

In 2010, the Bank continued with regular and efficient operating compliance function operation, which has been carried out in the Bank since 2007. By doing this, the Bank aims for its entire set of operations to be compliant with the legislation, rules, instructions, codices and any other regulations besides the compulsory ones. The compliance function is primarily oriented towards preventive actions, so that while performing banking operations, no breaches of any kind occur which could potentially cause loss of good reputation, measures taken by the supervisory bodies or any other consequences. Preventive character of the operations compliance function is thereby focused particularly on counselling (both in the process of developing new products and services, as well as for existing products and services, which are continuously supplemented and improved) and training/educating, in order to ensure adequate understanding of the purpose and goals of each regulation, and supervision. The compliance function is coordinated and led by the Compliance department together with all other Bank's organizational units and all employees.

Here are some of the most important tasks carried out within the compliance function framework in accordance with the adopted strategy:

- Consistency with internal procedures, represented by the "Control plan", regular self-assessment of key internal controls functioning,
- Ensuring data quality, which is done with regular supervision of logical correctness and harmonization of data in financial reports and risk reports,
- Ensuring security, which is done with regular monitoring of physical and technical safety and protection of information and personal data,
- Consistency of operations with the legislation (the Banking Act, the Payment Services and Systems Act, the Prevention of Money Laundering and Terrorist Financing Act, the Financial Instruments Markets Act, the Consumer Credit Act with all subordinated regulations and all other acts, which influence the Bank's operations),
- Ensuring consistency with accounting standards through regular procedures of supervising the compliance of accounting procedures with the standards.

In the 2010 financial year, the Bank successfully adjusted its operations to the new Consumer Credit Act, which transferred into our legal system the European directive regulating consumer credits and laying down clear rules regarding the provision of information to future borrowers, and regarding the advertising of credits and mandatory parts of loan contracts, thus representing bigger transparency and a higher level of legal certainty for borrowers.

Also, the Bank approached the renewal of security policies and their adjustment to the class of ISO standards 27000, and the compliance assurance with the PCI DSS standard. Furthermore, the Bank upgraded the HYPOnet online bank security. All these measures are intended to protect our clients and their assets, as well as to protect the reputation and safety of the Bank.

In 2009, the Bank also made an important step towards central and more effective procedure of managing client complaints by adopting a revised Book of rules on solving client complaints, which defines in details the procedure about a complaint, the committee which decides about a complaint, and informing a complainant. In 2010, the Bank further upgraded the client complaint management procedure with an application, into which all claims or complaints are entered and which enables monitoring the settlement of claims and complaints and records of corresponding reports, which are the base for the improvement of Bank's products and services.

In the field of education and training of our employees, we carried out all planned educations and trainings, followed by an e-test – web application enabling examination through the web, which is more efficient, faster and less stressful for education/training attendants.

Internal Audit

The Internal Audit department, in accordance with the Banking Act, reports to the Supervisory Board about the realization of annual plan, adequacy and efficiency of risk management, adequacy and efficiency of internal controls systems operations, and about important findings and their realization. The Internal Audit department's annual report is submitted to the Bank's Meeting of Shareholders.

In accordance with the Banking Act, the Bank also established the Audit Committee in 2009, which met four times in 2010. In accordance with the Companies Act, the Audit Committee also monitors the efficiency of internal audit.

The Internal Audit department also cooperates with the internal audit department of the parent bank, which at regular meetings sets directives for harmonized operations and reporting. The Internal Audit department employs 4 internal auditors, 2 of which have obtained the title of a certified internal auditor, and 1 is in the final stage of the training course to obtain the title.

In 2010, the Internal Audit department made self-assessment of its operations, which confirms compliance with standards in all its more important parts. Based on the findings, the department will carry on implementing activities to upgrade the quality of operations.

4 Financial Report

4.1 Statement of Management Board's Responsibility

The Management Board approves the financial statements for the year ended 31 December 2010, and the used accounting policies, estimates and notes to financial statements.

The Management Board is responsible for the preparation of the financial statements that give a true and fair presentation of the financial position of the Bank and of its financial performance for the year ended 31 December 2010. The Management Board is also responsible for the appropriate accounting system and adoption of measures to secure the assets, and to prevent and detect fraud and other irregularities and/or illegal acts.

The Management Board confirms that the appropriate accounting policies were consistently applied, and that the accounting estimates were made under the principle of prudence and the diligence of a good manager. The Management Board also confirms that the financial statements and notes thereof have been compiled under the assumption of the Bank's continued operation, and in accordance with the current legislation and International Financial Reporting Standards, effective in the EU.

Tax authorities can in following 5 years from calculation of income tax for financial year end review company’s operation which can consequently cause additional tax liabilities, delay penalties and penalties from tax income or other taxes. Management of the company is not familiar with any circumstances which could cause potential liabilities from income tax.

Last review of income tax calculation from tax authorities was in year 2008 when they rewiewed income tax calculation for year 2006.

Management Board

Matej Falatov, M.Sc.
Member of the Management Board

Dr. Alexander Picker
President of the Management Board

4.2 Independant Auditor's Report

ERNST & YOUNG

This is a translation of the original report in Slovene language

INDEPENDENT AUDITOR'S REPORT

To the shareholder of Hypo Alpe-Adria-Bank d.d., Ljubljana

Report on the Financial Statements

We have audited the accompanying financial statements of Hypo Alpe-Adria-Bank d.d., which comprise the statement of financial position as at December 31, 2010, and the statement of income, statement of comprehensive income, statement of changes in shareholders' equity and statement of cash flows 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 International Financial Reporting Standards as adopted by the European Union and with the requirements of the Slovenian Companies Act related to the preparation of the financial statements, 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 whether 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 judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting 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 d.d., as of December 31, 2010, and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union and with the requirements of the Slovenian Companies Act related to the preparation of the financial statements.

Other maters

The financial statements as at December 31, 2009, were audited by another Auditor, who issued an unqualified audit report on March 31, 2010.

Report on Other Legal and Regulatory Requirements

Management is also responsible for preparing the business report in accordance with the Slovenian Companies Act. Our responsibility is to assess whether the business report is consistent with the audited financial statements. Our work regarding the business report is performed in accordance with ISA 720, and restricted to assessing whether the business report is consistent with the financial statements and does not include reviewing other information originated from non-audited financial records.

The business report is consistent with the audited financial statements.

Ljubljana, March 31, 2011

ERNST & YOUNG
Revizija, poslovno
svetovanje d.o.o., Ljubljana

Janez Uranič
Director

Simon Kolenc
Certified Auditor

Ernst & Young d.o.o.
Dunajska 111, Ljubljana

4.3 Financial statement

Income Statement

EUR '000

	Note	2010	2009
Interest and similar income	1	85,203	90,919
Interest and similar expenses	1	(34,610)	(44,335)
Net interest income		**50,593**	**46,584**
Dividend income	2	911	596
Fee and commission income		10,489	10,797
Fee and commission expenses		(2,434)	(2,293)
Net fee and commission income	**3**	**8,055**	**8,504**
Realized gains (losses) on financial assets and liabilities not measured at fair value through profit or loss	4	(104)	(2,855)
Net gains / (losses) on financial assets and liabilities held for trading	5	(1,750)	2,023
Net gains / (losses) on currency translation differences	6	762	(238)
Net gains / (losses) on derecognition of assets excluding non-current assets held for trading		(1)	(36)
Other net operating income / (losses)	7	1,151	1,720
Administrative costs	8	(21,566)	(22,718)
Depreciation and amortization	9	(1,967)	(2,000)
Provisions	10	(4,192)	(2,558)
Impairments	11	(64,296)	(25,191)
PROFIT / (LOSS) FROM ORDINARY ACTIVITY		**(32,404)**	**3,831**
Income tax	12	6,112	(1,118)
NET PROFIT / (LOSS) FOR THE YEAR		**(26,292)**	**2,713**

The accompanying notes form an integral part of the financial statements and should be read in conjunction with them.

Statement of Comprehensive Income

EUR '000

	2010	2009
NET PROFIT / (LOSS) FOR THE YEAR	**(26,292)**	**2,713**
OTHER COMPREHENSIVE INCOME AFTER TAX	**(1,535)**	**3,295**
Net gains / (losses), recognized as revaluation reserve relating to available-for-sale financial assets	**(1,919)**	**4,119**
Gains / (losses), recognized as revaluation reserve	(2,887)	4,119
Transfer of gains / (losses) from revaluation reserve to profit and loss	968	-
Income tax relating to components of other comprehensive income	**384**	**(824)**
TOTAL NET COMPREHNSIVE INCOME FOR THE YEAR	**(27,827)**	**6,008**

The accompanying notes form an integral part of the financial statements and should be read in conjunction with them.

Statement of Financial Position

EUR '000

	Note	31.12.2010	31.12.2009
Cash and balances with Central Bank	13	55,507	113,122
Financial assets held for trading	14	24,092	38,062
Available-for-sale financial assets	15	91,280	91,470
Loans		1,954,752	2,031,012
- to banks	16	14,191	46,929
- to clients	17	1,940,561	1,984,083
Financial assets held to maturity	19	42,315	42,112
Property, plant and equipment	20	6,016	6,140
Intangible assets	21	4,216	3,668
Income tax assets		6,564	2,997
- tax assets		308	2,853
- deferred tax assets	28	6,256	144
Other assets	22	3,101	3,147
TOTAL ASSETS		**2,187,843**	**2,331,730**
Financial liabilities to Central Bank	23	40,010	80,276
Financial liabilities held for trading	24	2,450	2,863
Financial liabilities measured at amortized cost	25	1,965,469	2,044,077
- deposits from banks	25a	1,218,646	1,338,695
- deposits from clients	25a	524,302	479,041
- borrowings from banks	25b	148,683	153,336
- borrowings from non-banks	25b	833	-
- subordinated liabilities	26	73,005	73,005
Provisions	27	7,357	3,178
Income tax liabilities		445	829
- deferred tax liabilities	28	445	829
Other liabilities	29	5,493	6,061
TOTAL LIABILITIES	30	2,021,224	2,137,284
Share capital	30	174,037	174,037
Capital surplus	30	2,696	2,696
Revaluation reserve	30	1,660	3,196
Revenue reserve	30	1,862	1,862
Retained earnings / (accumulated loss) (including net profit / (loss) for the year		(13,637)	12,655
TOTAL EQUITY		166,619	194,446
TOTAL EQUITY AND LIABILITIES		**2,187,843**	**2,331,730**

The accompanying notes form an integral part of the financial statements and should be read in conjunction with them.

The Management Board of Hypo Alpe-Adria-Bank d.d. has approved the financial statements and notes thereto.

Management Board

Matej Falatov, M.Sc.

Dr. Alexander Picker

Ljubljana, 31 March 2011

Statement of Changes in Equity

EUR '000

	Note	Share capital	Capital surplus	Revaluation reserve	Revenue reserve	Retained earnings (including net profit /loss for the year	Total equity
Balance on 1 January 2009		**174,037**	**2,696**	**(99)**	**7,234**	**20,554**	**204,422**
Comprehensive income for the year after tax	30	-	-	3,295	-	2,713	6,008
Payment (settlement) of dividends	30	-	-	-	(5,542)	(10,442)	(15,984)
Allocation of net profit to revenue reserves	30	-	-	-	170	(170)	-
Balance at 31 December 2009		**174,037**	**2,696**	**3,196**	**1,862**	**12,655**	**194,446**
Comprehensive income for the year after tax	30	-	-	(1,535)	-	(26,292)	(27,827)
Balance on 31 December 2010		**174,037**	**2,696**	**1,660**	**1,862**	**(13,637)**	**166,619**

The accompanying notes form an integral part of the financial statements and should be read in conjunction with them.

Cash Flow Statement

EUR '000

	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Net profit (loss) before tax	(32,404)	3,831
Depreciation and amortization	1,967	2,000
Net (gains) / losses from currency translation	(762)	238
Net (gains) / losses on sale of property, plant and equipment and investment property	1	36
Other (profit) / loss from investing	(1,669)	-
Other (profit) / loss from financing	1,676	2,422
Net unrealized profit in equity or from revaluation reserve of available-for-sale financial assets (excluding the deferred tax effect)	1,919	4,119
Other adjustments of profit before tax	6,909	8,265
Operating cash flows before changes of operating assets and liabilities	**(22.363)**	**20,911**
(Increase) / decrease of operating assets (excluding cash equivalents)	**122.732**	**(81,274)**
Net (increase) / decrease of assets with Central Bank	(1,101)	(2,357)
Net (increase) / decrease of financial assets held for trading	12,221	(21,160)
Net (increase) / decrease of available-for-sale financial assets	(2,698)	(25,070)
Net (increase) / decrease of loans	114,275	(31,236)
Net (increase) / decrease of other assets	35	(1,451)
Increase / (decrease) of operating liabilities	**(184,548)**	**76,333**
Net increase / (decrease) of financial liabilities to Central Bank	(40,266)	50,007
Net increase / (decrease) of financial liabilities held for trading	(413)	(1,293)
Net increase / (decrease) of deposits and loans measured at amortized cost	(143,291)	38,078
Net increase / (decrease) of other liabilities	(578)	(10,459)
Cash flow from operating activities	**(84,179)**	**15,970**
(Paid) / reimbursed corporate income tax	**2,545**	**(3,947)**
Net cash flow from operating activities	**(81,634)**	**12,023**
CASH FLOWS FROM INVESTING ACTIVITIES		
Receipts from investing activities	**1,855**	**604**
Proceeds from sale of property, plant and equipment and investment property	389	302
Proceeds from non-current assets or liabilities held for sale	-	130
Other proceeds from investing activities	1,466	172
Disbursements from investing activities	**(2,781)**	**(2,614)**
(Disbursements for acquisition of property, plant and equipment and investment property)	(1,600)	(1,408)
(Disbursements for acquisition of intangible assets)	(1,181)	(1,076)
(Disbursements for acquisition of non-current assets or liabilities held for trading)	-	(130)
Net cash flow from investing activities	**(926)**	**(2,010)**
CASH FLOWS FROM FINANCING ACTIVITIES		
Expenses for financing activities	**(1,676)**	**(18,577)**

	2010	2009
(Dividends paid)	-	(15,983)
(Repayments of subordinated debt)	(1,676)	(2,422)
(Other payments relating to financing activities)	-	(172)
Net cash flow from financing activities	**(1,676)**	**(18,577)**
Effects of exchange-rate changes on cash and cash equivalents	1,820	39
Net increase of cash and cash equivalents	**(84,236)**	**(8,564)**
Cash and cash equivalents at the beginning of period	**137,447**	**145,971**
Cash and cash equivalents at the end of the period	**55,031**	**137,446**

The accompanying notes form an integral part of the financial statements and should be read in conjunction with them.

EUR '000

	Note	2010	2009
Cash and cash equivalents comprise:			
Cash and balances with Central Bank	13	44,840	103,555
Loans to banks with maturity up to three months	16	10,191	33,891
TOTAL		**55,031**	**137,446**

Cash equivalents comprise of as cash (excluding obligatory reserves with the Central Bank) and loans to banks with maturity of up to 90 days.

Cash flows from incomes and dividends

EUR '000

	Note	2010	2009
Interests paid		8,382	10,965
Interests income		72,268	87,873
Dividends paid		-	15,983
Dividends income		1,037	885

4.4 Notes to Financial Statements

Basic Information

Hypo Alpe-Adria-Bank d.d. is a Slovenian public limited company registered for providing universal banking services on the Slovenian market.

Full address of the Bank is: Hypo Alpe-Adria-Bank d.d., Dunajska cesta 117, Ljubljana, Slovenia.

The Bank's sole owner is Hypo Alpe-Adria-Bank International AG, Klagenfurt, Austria, member of the Hypo Alpe-Adria Group. Until 29 December 2009, the ultimate parent of the Bank was Bayern LB, Germany. On 30 December 2009, the ultimate parent of the Company became the Republic of Austria, with 100 per cent ownership of Hypo Alpe-Adria-Bank International AG.

Consolidated financial statements can be obtained at the following headquarters or on their web pages:

Hypo Alpe-Adria-Bank d.d.
Dunajska cesta 117
1000 Ljubljana
Slovenia
www.hypo-alpe-adria.si

Hypo Alpe-Adria-bank International AG
Alpen-Adria-Platz 1
9020 Klagenfurt
Austria
www.hypo-alpe-adria.com

All the amounts in the financial statements and the accompanying notes are stated in thousands EUR unless stated otherwise.

Significant Accounting Policies

The following significant accounting guidelines have been applied in the preparation of the financial statements.

1. Basis for the Preparation of Financial Statements

The financial statements were prepared in accordance with the International Financial Reporting Standards (hereinafter: IFRS) as adopted by the European Union.

The Bank prepares its financial statements (with the exception of cash flow information) on the accrual basis of accounting.

The financial statements of the Bank have been prepared under the historical cost convention and modified by the revaluation of available-for-sale financial assets, financial assets and financial liabilities measured at fair value through profit or loss, and all derivatives.

The Bank's Annual report includes information and notes as prescribed by the Companies Act, IFRS as adopted by the EU, and the Decision on books of account and annual reports of banks and savings banks.

The preparation of financial statements under IFRS requires the use of estimates and fundamental accounting assumptions such as going concern and accrual. Under these assumptions, the effects of transactions and other business events are recognized on accrual and not when they are paid, and are recorded and reported for periods to which they refer.

The significant accounting estimates and assumptions are presented in the Section 21.

The estimates and assumptions are continuously reviewed and are based on the latest information or latest developments or past experience.

The financial statements have been prepared on the going concern basis, which assumes continuity of normal business activities and the realization of assets and the settlement of liabilities in the ordinary course of business.

1.a) Going concern assumption

The financial statements have been prepared on the going concern basis, which assumes continuity of normal business activities and the realisation of assets and the settlement of liabilities in the ordinary course of business.

The ability of the Bank to continue as a going concern is dependent upon the continued funding and support from its shareholder Hypo Alpe-Adria-Bank International AG, Klagenfurt, Austria (the Parent) under the currently agreed financial terms. To this extent, the Parent has provided funding to the Bank to support its operations. This support includes agreeing not to seek repayment, other than originally contracted, of intercompany loans made by them to the Bank for a period of at least 12 months from the date of these financial statements.

Following the acquisition of 100 per cent of the shares in the Hypo Alpe-Adria-Bank International AG by the Republic of Austria completed on 30 December 2009, Hypo Alpe-Adria-Bank International AG and its subsidiaries (together Hypo Group Alpe Adria or HGAA) is currently in the process of restructuring.

The previous owner of HGAA made contributions towards the restructuring as part of its disinvestment. Furthermore, the Republic of Austria announced another injection of capital. This took place through the subscription of the issue of EUR 450,0m of share certificates late in June 2010.

The European Commission provisionally approved the measures put forward by the Republic of Austria on 23 December 2009 for a period of up to six months and instructed the Republic of Austria to present an in depth restructuring plan for HGAA in the first half of 2010, to enable it to judge whether the aid measures are consistent with EU laws on state aid.

The European Commission will check whether the measures planned can return HGAA to long-term profitability, whether support from the state is kept to the required minimum, whether the own contribution made will be appropriate and whether sufficient measures have been undertaken, to limit the distortion to competition caused by the financial assistance given. The European Commission has also announced that it will examine whether the previous owner has contributed sufficiently to the restructuring costs.

A formal restructuring plan has been prepared by the Parent for the European Union approval process for government aid. HGAA will be redimensioned on the basis of this restructuring plan and this will also lead to a significant number of the HGAA member companies being relinquished.

In this context, the restructuring and exit from the market costs are anticipated by the current business plan for the period from 2011 until 2015, and these costs – depending on the timing of the exit and the then existing market environment – may have a corresponding negative impact on the future periods. These expenses may be considered in accordance with IFRS only when the specific criteria according to IFRS 5 are fulfilled, and especially the most likely disposal within the period of 12 months.

On 22 June 2010, the provisional approval of capital measures was prolonged „until making the final decision about the restructuring plan regarding Hypo Alpe Adria“. However, the Commission reserved its right to give its final approval after examining the restructuring plan submitted to the Commission by the Republic of Austria in mid-April 2010.

With its decision as of 4 August 2010, the EU gave its approval for the acquisition of Hypo Alpe Adria by the Republic of Austria required under the merger control law.

At the time of finalizing these financial statements, it cannot be estimated with any degree of certainty when the EU proceedings will be concluded and whether the European Commission will accept the restructuring plan for HGAA.

Hypo Alpe-Adria-Bank International AG as the subject of the procedure stated that it is ready for a full cooperation with the Commission.

2. Segmental Reporting

In accordance with IFRS 8, the Bank is not required to report per individual business segments as it has not issued either debt or equity instruments that are traded publicly (on domestic or foreign stock exchange or outside the stock market inclusive of local or regional markets) and has not submitted or is not in the process of submitting its financial statements to the Securities and Exchange Commission or another administrative organization with intention to issue any group of instruments on a public market.

3. Foreign Currencies Translation

Functional and Presentation Currency

The financial statement items of the Bank are measured using the currency of the primary economic environment in which the Bank operates. The Bank measures the financial statement items in Euros, which is functional and presentation currency of the Bank.

Translation of Foreign Currency Transactions

Foreign currency transactions are translated into the functional currency on the trade day using the reference exchange rate of ECB published by the Bank of Slovenia on its web page. The rate published after 2 p.m. is used from midnight of the next day.

Translation gains and losses resulting from the settlement of foreign currency transactions and from the translation of monetary items recorded in a foreign currency are recognized in the profit or loss.

Translation gains and losses resulting from the change of the amortized cost of monetary securities nominated in foreign currency that are classified as available-for-sale financial assets, are recognized in the profit or loss. Translation gains and losses resulting from non-monetary securities, such as equities, classified as available-for-sale financial assets, are recognized in the revaluation reserves together with the fair value measurement effect.

Gains and losses resulting from purchase and sale of foreign currencies are recognized as net profit from financial assets and liabilities held for trading in the profit or loss.

The exchange rate used in the translation to the functional currency as at 31 December 2010 was 1 EUR=1.3280 USD (2009:1 EUR =1.4406 USD); 1.2475 CHF (2009:1 EUR=1.4836 CHF); 0.8602 GBP (2009: 1 EUR=0.8810 GBP).

4. Interest Income and Expense

Interest income from debt securities is recognized in the profit or loss using the effective interest method.

The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments.

Interest income and expenses for other interest bearing financial instruments are recognized in the profit or loss in the charged amounts on the basis of the amounts, deadlines and methods prescribed by the Bank's interest rates price list.

Once a financial asset or a group of similar financial assets has been written down as a result of impairment, interest income is recognized in the amount of the liquid part of the asset.

Interest income includes regular, default and deferred interest for interest bearing financial instruments and prepaid fees for approved loans and are transferred to income using a classic linear method of deferral, which represents a deviation from the IFRS requirements. However, the Management believes that the difference does not represent a significant deviance for a fair presentation of financial statements.

Interest on liabilities for deposits and borrowings are recognized as interest expenses.

5. Fee and Commission Income and Expense

Fees and commissions are generally recognized on an accrual basis when the service has

been provided. Fees and commissions for services that are performed continuously in a certain period of time are recognized proportionally over the period in which the service is performed.

Fees and commissions include primarily fees for payment transactions, commissions on loan transactions (loan management fees, costs of reminders), commissions on brokerage transactions and warranty fees.

Fees resulting from approval of loans are recognized as interest income and expenses.

6. Dividend Income

Dividends are recognized in the income statement when they are declared.

7. Financial Assets

a) Classification

On initial recognition, the Bank classifies the financial assets to the following groups according to the purpose of acquisition, duration of possession and type of financial instrument: financial assets held to maturity, available-for-sale financial assets, financial assets at fair value through profit or loss, loans and receivables.

Held-to-maturity financial assets

Held-to-maturity financial asset are non-derivative financial assets with fixed or determinable payments that an entity intends and is able to hold to maturity and that do not meet the definition of loans and receivables and are not designated on initial recognition as assets at fair value through profit or loss or as available for sale. Held-to-maturity financial assets are measured at amortized cost. If the Bank sells other than in insignificant amounts of held-to-maturity financial assets, or as a consequence of a non-recurring, isolated event beyond its control that could not be reasonably anticipated, all of its other held-to-maturity financial assets must be reclassified as available-for-sale in the current and next two financial years.

In accordance with the internal decision of the Hypo Group, in 2010 the Bank did not classify its financial instruments to financial assets held to maturity. The financial assets reported in the Statement of Financial Position as at 31 December 2010, were recognized prior to the above mentioned decision of the Group. The Bank will hold these financial assets until their maturity.

Available-for-Sale Financial Assets

Available-for-sale financial assets are non-derivative financial assets, which the Bank intends to hold for indefinite period of time and which may be sold in response to liquidity requirements, changes of interest rates, currency exchange rates or prices of financial instruments.

The bank can exceptionally be allowed to use evaluation model for measurement of the fair value of defined financial instruments, if it is able to prove, that the existing market for these financial assets is not active.To define if a market is active or inactive, one must define the key parameters, which indicate market activity. It is also important to follow up the trends in those parameters. The parameters should be used consistenly according to the content and in time, so that as much of subjective judgement in interpretation of the given results can be eliminated as possible.

The bank should take into the account in the conditions of inactive market all risk parameters, which would be, under the condition of the active market, required by the participants on the market, especially the issuer credit risk and the premium for liquidity.

Financial Assets at Fair Value Through Profit or Loss

Financial assets measured at fair value through profit or loss are further classified as financial assets held for trading and financial assets which are, on initial recognition, designated as measured at fair value through profit or loss.

Financial Assets Held for Trading:

A financial asset is classified as held-for-trading if it is acquired principally for sale in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking. Derivative financial assets are also classified as held for trading unless they are designated as hedging instruments.

In the statement of financial position, derivative financial instruments are initially recognized at cost which is equal to the fair value of consideration received or granted. They are measured at fair value which is determined on a daily basis using generally accepted financial methodology, whereby quotations/prices of entry values (e.g. zero coupon yield curve, FRA, interest rate differentials of currencies, etc.) are obtained from information systems (Reuters, Bloomberg).

Fair values of derivatives are recognized either within assets or liabilities. All derivative financial instruments of the Bank are classified as financial assets held for trading and are not used in hedge accounting.

Financial assets are designated a**t fair value through profit or loss** only if the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets and liabilities or recognizing gains or losses on them on a different basis. Financial assets designated at fair value through profit or loss include some instruments such as equity instruments which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and which are reported to the key management on this basis, and the financial assets and liabilities containing one or several embedded derivatives that could significantly impact cash flows of the host instrument.

The Bank did not classify financial instruments to a subgroup of financial assets which are upon initial recognition designated at fair value through profit or loss.

Loans and Receivables

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

b) Initial recognition and measurement

All financial assets are recognized on the date of trading at fair value (usually at cost), increased by (instruments that are not recognized at fair value through profit or loss) costs that are directly attributable to the transaction, whereas for financial assets at fair value through profit or loss, costs of the transaction are reported in the profit or loss. Subsequent measurement of a financial asset reflects its initial designation.

Financial assets held for trading and available-for-sale financial assets are recognized at fair value. Gains or losses on financial assets at fair value and held for trading are recognized in the profit or loss of the period in which they accrued.

Gains or losses on available-for-sale financial assets designated at fair value are recognized in the comprehensive income until the asset is derecognized or impaired, in which case gains and losses are transferred to profit or loss. Interest accrued on the basis of effective interest rate method and exchange-rate differences from cash items classified as available-for-sale financial assets are recognized directly in profit or loss.

Loans and receivables, and financial assets held to maturity are carried at amortized cost.

»Day one profit«

When the value of a transaction in an inactive market for the same financial instrument significantly differs from its fair value at another comparable market or, if the value of transaction significantly deviates from the valuation model that considers assumptions from an active market, the Bank immediately recognizes the difference between the transaction value and fair value in profit or loss as net gains or losses on trading as »day one profit«. When the market value is irrelevant, the difference between the value of transaction and the valuation model is recognized in profit and loss only when the market becomes significant or on disposal of a financial instrument.

c) Reclassification of financial assets

Financial instruments may only be reclassified from held-for-trading group in exceptional circumstances. The fair value at the reclassification date becomes financial instrument's new amortized cost. Reclassification of an asset from the group of financial assets held to maturity is not allowed.

In 2010, the Bank did not reclassify any of its financial instruments to another group.

d) Derecognition

Derecognition of financial assets is carried out when contractual rights to cash flows expire, or when they are transferred to another party and where such transfer fulfils the criteria for derecognition (an entity has transferred all risks and benefits of the asset).

e) Principles Applied in Fair Value Valuation

The calculation of the fair value of financial assets traded on the active market is based on the published market value on day of the statement of financial position, namely the price that represents the highest demand value excluding the transaction costs. The fair value valuation of financial assets that are not traded in an active market is based on an external expert's valuation. The Bank verifies the external expert's valuation and in case the verification is positive the valuation is taken into consideration. In case there is no external expert's valuation an internal valuation is prepared. Internal valuations are prepared using standard valuation methods such as discounted future cash flow model, peer-to-peer analysis (direct comparison with companies that are publicly traded) and liquidation value. Final valuation of the financial asset takes into account all approaches, but using different weights, depending on industry, financial stability of the company and other factors that can affect fair value of financial instruments.

f) Temporary Purchases of Securities (Reverse Repo)

Temporary purchases of securities (reverse repo) are recognized in the balance sheet as approved loans. The difference between the sale price and the repurchase price is recognized in the financial statements as interest income and is accrued throughout the duration of the contract.

8. Impairment of Financial Assets

a) Financial Assets at Amortized Cost

General:

The Bank makes an assessment of its financial assets portfolio at amortized cost and off-balance exposure on a monthly basis using its own methodology:

- The necessary impairment is recognized for financial assets at amortized cost, and
- The required provisions are formed for off-balance-sheet exposures.

The method used to create the necessary impairment of financial assets at amortized cost depends primarily on the exposure (the Bank distinguishes between individually relevant exposures and individually irrelevant exposures) and on formal status of financial assets. The Bank distinguishes between the financial assets that are subjected to breaches of material factors defined by the Bank as objective factors indicating an impairment of the financial asset, and the financial assets where no such factors are detected.

In accordance with the methodology of the HGAA Group, the Bank treats each client, whose total exposure exceeds 150,000 EUR, as individually relevant exposure.

Distinguishing Between Different Methods of Impairment of Financial Assets at Amortized Cost

Financial assets at amortized costs are classified into one of the following segments for the purpose of impairment:

1. Individually relevant exposures, in relation to which a breach of at least one objective factor indicating the impairment of the financial asset at amortized cost is detected;
2. Individually irrelevant exposures, in relation to which a breach of at least one objective factor indicating the impairment of the financial asset at amortized cost is detected;
3. All exposures where no breach of any of the objective factors indicating the impairment of the financial asset at amortized cost is detected and where an individual impairment is not required.

In its internal policies, the Bank specified the following objective factors indicating the impairment of the financial asset at amortized cost:

- Materially important delay in settlement of contractual obligations lasting over 90 days;
- Bankruptcy or compulsory settlement of the client;
- Existence of proof of client's serious financial problems, including also:
    - Reprogramming due to client's economic, legal or other problems,
    - Irregular settlement of liabilities within the group of related entities;
    - Poor client's internal rating; or
    - Significant economic problems in the client's industry.

Detailed Presentation of Individual Methods of Impairment of Financial Assets at Amortized Cost

Individual impairment

Individually relevant exposures are addressed individually; in the event of a breach of at least one of previously determined factors that objectively indicate the impairment of an individual financial asset at amortized cost, such exposures are impaired individually. The Bank individually assesses expected cash flows for repayment (it evaluates expected cash flows from regular loan repayment as well as expected cash flows from realization of collateral); in the event of negative difference between the discounted value of all expected cash flows and the book value of receivable the Bank creates individual impairment.

Realization of collateral is recognized as potential future cash flow in cases where the collateral fulfils the required formal criteria with regards to the degree of legal certainty and realizability. Impairment of such exposures is referred to individual impairment (also known as Specific Risk Provisions – SRP).

Based on the available information, the Bank makes individual assessment in terms of the time and amount of expected repayment, whereas current value of expected cash flows is calculated with the use of discounted effective interest rate (for loans that were granted at a fixed interest rate) or initial contractual interest rate (for loans that were approved at a variable interest rate).

Collective impairments

Individually irrelevant exposures that also fulfil at least one of the previously determined factors are grouped into groups with similar characteristics, and collectively impaired using the formula that reflects the fact that at least one factor, which objectively indicates the impairment of individual financial asset, was breached. The amount of impairments created depends primarily on the scope of relevant collateral (it is the exposed part of the investment that is subject to collective impairment) and on the segment into which the exposure is allocated. The loans and other financial assets at amortized cost granted to the following borrowers are designated by the Bank as groups of loans with similar attributes:
Group of financial assets granted to enterprises for their regular operations;
Group of financial assets granted to sole proprietors;
Group of financial assets granted to public sector entities and budget users;
Group of financial assets granted to individuals.

The impairments for the above exposures are called Collective Impairments - CI.

Group Impairments (Latent losses)

Group impairments (Latent losses) are recognized for exposures that as of the balance sheet date do not violate any of the objective factors indicating the impairment of the financial asset and for individually treated exposures where no individual impairment is required. When creating group impairments, we also calculate the required scope of impairments on the basis of the mathematical formula; in this case, however, the formula reflects the fact that no objective factor, which objectively indicates the impairment of individual financial asset, has been breached. The mathematical formula derives from the Basel II methodology, adjusted for the assessment of the scope of realized but not yet identified losses in the Bank's portfolio. The adjustment relates mainly to the acknowledgment of collateral and determination of the time period in which the Bank is capable to detect the occurrence of the loss.

Relevant Value of Collateral:

The relevant value of collateral used by the Bank is the market value of collateral decreased for:

- Expected costs of realization of such collateral;
- Expected decrease of the collateral's value due to the realization process;
- Considering the time component of the realization of collateral (discounting).

The cumulative effect of all three factors, which cause that the current value of expected cash flows from realization of collateral is normally lower than it's the current market value, is reported by the Bank in its calculations through special coefficients, in accordance with the policy of the HGAA Group.

In order for collateral to be recognized as relevant, it should fulfil at least three minimum criteria with regards the degree of legal certainty and realizability. Furthermore, the Bank has to obtain an authentic assessment of the market value of collateral.

Probability of Default

The Bank assesses the probability of default on the basis of internal rating tools. According to the Hypo Group policy, different rating tools are used for individual segments of clients. Regardless of the tool applied, the final results are transferred to a single 25-level scale that determines the probability of default for each client separately.

Loss Given Default

The expected scope of loss in the event of default (Loss Given Default) is shown using a LGD coefficient, which shows what part of unsecured exposure the Bank can expect to lose in the event of default. The coefficients are compliant with the HGAA Group policies and follow the conservative assessment of expected losses in the IRB approach of the new Capital Directive CAD III.

Segment	LGD (Basel II Standard)
Banks	0.50
Regional government and local authorities	0.45
Central government and central banks	0.45
Individuals	0.90
Legal entities	0.70
Public sector entities	0.50
Project financing	0.75

Period in which the Bank Identifies the Realization of Loss in its Portfolio

The Bank has defined the period, in which it recognizes the realization of loss in its portfolio (Loss identification period), as a period during which the Bank can detect that the client breaches one of the objective indicators of impairment of the financial asset. The Bank has implemented a monitoring system by means of which it believes that it is capable of detecting the negative events for most of its clients in relatively short time. The Bank uses the LIP factor of 1.0 for financial assets where regardless of the sufficient frequency in monitoring of the portfolio, the Bank is unable to with sufficient probability, assess potential loss since the regularity of repayments of liabilities does not reflect the ability of clients to repay loans when they mature. Such transactions include above all overdraft facilities on transaction accounts, credit lines, guarantees, loans with a single repayment or loans with a moratorium. For all other exposure the Bank uses the LIP factor 0.5.

b) Available-for-Sale Financial Assets

The Bank assesses on a monthly basis whether there are any indications of impairment of available-for-sale financial assets. If there is objective evidence that an impairment loss on financial assets available for sale has been incurred, the cumulative impairment loss is transferred from equity to profit or loss.
Impairment losses included in profit or loss as equity instruments are not derecognized through profit or loss. If the value of a debt instrument classified as available-for-sale increases and the increase can be related objectively to an event occurring after the impairment loss was recognized, the previously recognised impairment loss is reversed through profit or loss.

The Bank applies the following criteria to determine whether available-for-sale financial assets have been impaired:

- For debt instruments: fair value is lower than 90 per cent of the purchase value (which represents the value of 100 per cent),
- For equity instruments: significant decrease of the fair value lasting more than 9 months, and the fair value falls more than 20 per cent below the purchase value.

c) Restructured Loans

The Bank assesses the restructured loans individually at the time of approval of restructured loan in order to determine the need for impairment. If the Bank assesses that loan restructuring is commercially justified and represents a part of the Bank's regular operations, the Bank does not consider such restructuring as impartial proof of impairment of financial assets; such loans are treated equally as other investments of the Bank.

When a loan is restructured due to client's economic, legal or other problems that significantly affect the client's future ability to repay its obligations, the Bank accordingly reclassifies such client to lower rating grade and individually assesses on a monthly basis the need for individual impairment. If the Bank does not detect the need for individual impairment, the client is considered within a group using the same methodology as for other investments of the Bank.

9. Offset

In the statement of financial position, the financial assets are offset with liabilities when there exists a legal right and upon the intent of a net offset or on the basis of simultaneous realization of assets and settlement of liabilities.

10. Property, Plant and Equipment, and Intangible Assets

Property, plant and equipment and intangible assets are stated at cost in the financial statements less accumulated depreciation and impairment losses.

On initial recognition, the cost of an asset includes all expenditures that are directly attributed to the acquisition and are necessary to make the asset ready for its intended use. Subsequent expenditure incurred on an item of property, plant and equipment is added to the cost of the assets and recognized only if it is probable that the future economic benefits embodied in the item of property, plant and equipment will flow to the entity and if these costs can be reliably measured. All other expenditure is recognized in profit or loss as an expense when incurred.

Depreciation and amortization expense is accounted for individually on a straight-line basis so that the costs of the assets are allocated to the residual value over the useful lives of the assets.

The depreciation (amortization) rates applied are as follows:

	2010	2009
Buildings	2.5 %	2.5 %
Computer hardware	20 to 33.3 %	20 to 33.3 %
Furniture and other equipment	5 to 50 %	5 to 50 %
Cars	20 %	20 %
Investments in leasehold improvements	5 to 50 %	5 to 50 %
Intangible assets	10 to 20 %	10 to 20 %

The residual values of assets and their useful lives are reviewed as of the day of the statement of financial position and are adjusted accordingly, if expectations differ from the previous assessments.

The land is recognized separately from the buildings. As it normally has unlimited useful life, the Bank does not depreciate it.

The assets are derecognized upon their disposal or when no additional future economic benefits can be expected from their use. Gains and losses resulting from disposal of assets represent the difference between the net gain on disposal and the carrying amount of the asset.

Depreciation of an asset begins on the first day of the following month after the asset is made ready for its use.

The Bank assesses on each day of the statement of financial position, whether there is any impartial evidence that an assets might be impaired. If there are indications that an asset may be impaired, the assessment of the recoverable amount is made. The recoverable amount is the higher of the value in use or net sale value of the asset. If the recoverable value is higher than the carrying amount, the impairment of assets is not required, whereas if the contrary is true, a loss is recognized in profit and loss in the amount of the difference between the recoverable and carrying amount of the assets.

There were no reasons for impairment of assets in 2010.

11. Leases

A lease is a contractual relationship in terms of which the lessor transfers the right to the asset for an agreed period of time to the lessee, in exchange for a payment or a line of payments. The key factor for classifying a lease is the scope in which the risks and rewards of ownership are transferred from the lessor to the leasee.

The Bank as a lessee

The Bank mostly enters into lease contracts where the lessor bears majority of the risks and awards relating to the ownership of the asset (operating lease). Payments made in respect of the operating lease are included in profit or loss proportionately to the duration of the contract. If operating lease is terminated prematurely all payments, requested by the lessor, are recognized as cost in the period of termination of the contract.

12. Cash and Cash Equivalentsi

In the statement of cash flows, cash and cash equivalents comprise of: cash on hand and balances with the Central Bank (excluding the obligatory reserves), and loans to banks with initial maturity of up to 90 days.
Cash and cash equivalents are measured at amortized costs.

13. Provisions

A provision is recognized when the Bank has a present legal or constructive obligation as a result of a past event that may be reliably measured, and it is probable that an outflow of economic benefits will be required to settle the obligation.

Where there are a number of similar obligations, the likelihood that an outflow will be required for the 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.

The Bank recognizes the provisions in respect of potential credit-related obligations (financial and service guarantees, provisions for undrawn part of the loan) and employees' benefits (jubilee awards, termination benefits upon retirement).

14. Taxes

The corporate income tax is accounted for at the tax rate applicable on the date of the statement of financial position. Tax is levied on the tax basis determined in accordance with the Corporate Income Tax Act. The tax rate applicable for 2010 is 20 per cent.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes; deferred tax is recognized using tax rates enacted at the date when temporary differences are expected to be eliminated. A deferred tax asset is recognised only to the extent that it is probable that future taxable profit will be available against which the deductible temporary differences can be utilized.

The Bank formed the deferred taxes in respect of the differences resulting from different depreciation rates of assets used for operating and tax purposes, revaluations and impairment of available-for-sale securities, provisions for employees' benefits and in respect of the amount of tax losses and tax allowances which the Bank was unable to utilize in the current tax return due to the loss incurred.

The deferred tax, associated with the valuation of available-for-sale financial instruments, is recognized directly in the equity.

15. Employee Benefits

In accordance with the law, the Bank provides to its employees jubilee awards and termination benefits upon retirement, which are legally prescribed benefits. An independent actuary calculates the provisions on the date of the statement of financial position. The significant assumptions applied in the calculation are as follows:

- Discount factor: 4.90 per cent annually;
- Number of employees entitled to receive the payment: 403
- Growth of the average salary in the Republic of Slovenia: 3.5 per cent annually
- Assessment of staff turnover

The calculation of the termination benefits upon retirement is tied to the pension qualifying period of each individual employee. Employees are entitled to receive the jubilee award once every ten years.

The Bank pays social security contributions at the rate of 8.85 per cent in accordance with the Slovenian legislation. These payments are recognized in the financial statements as labour costs in the period they refer to.

16. Financial Liabilities

The financial liabilities are recognized at fair value (normally at cost) on the trade date. The costs of transaction are recognized in the profit or loss. After initial measurement they are recognized at amortized cost. A financial liability is derecognized only when the contractual obligation is fulfilled, cancelled or expired.

17. Share Capital and Reserves

The share capital is recognized in the nominal amount and was subscribed or paid by its owners.

Dividends on shares decrease the equity in the period in which they are approved by the owners of the Bank.

18. Financial Guarantee Contracts

Financial guarantee contracts require the issuer to make specified payments to reimburse the holder for a loss it incurs if a specified debtor fails to make payment when due under the original or modified terms of a debt instrument. Such guarantees are issued to banks, financial institutions, and other entities as means of securing loans, overdrafts and other banking facilities. Financial guarantee contracts are initially recognized at fair value which is equal to the fee received under the »Other liabilities«. Fees received are amortized to profit or loss using the straight-line method.

19. Transactions on Behalf and for the Account of Third Parties

The Bank also offers its clients securities brokerage services and asset management services. Operations are conducted through a separate account. The client assumes the operational risk. A commission charged for these services to clients is recorded in the Note number 1. These assets are not included in the statement of financial position but are recorded in the off-balance-sheet items as authorized operations.

Assets and liabilities of clients from the intermediary operations as well as fee and commission income and expenses related to the intermediary operations are recorded in the Note number 3b in accordance with the local legislation.

20. New Standards and Interpretations

a) The following standards, amendments and interpretations become effective on or after 1 January 2010

Standard / Interpretation	Content	Applicable for periods beginning on or after
IFRS 3	Business Combination	1 July 2009
IAS 27	Consolidated and Separate Statements	1 July 2009
IFRIC 17	Distributions of Non-cash Assets to owners	1 July 2009
IFRIC 18	Transfers of Assets from Customers	1 July 2009
IFRS 1 (amendment)	First-time adoption of International Financial Reporting Standards	1 January 2010
IFRS 2 (amendment)	Share-based payment	1 January 2010
IFRIC 15	Agreements for the construction of real estate	1 January 2010
IFRIC 9	Reassessment of Embedded Derivatives	1 January 2010
IFRIC 16	Hedges of a Net Investment in a Foreign Operation	1 January 2010
IFRS 5 (amendment)	Non-current assets held for sale and discontinued operations	1 January 2010
IFRS 8 (amendment)	Operating segments	1 January 2010
IAS 1 (amendment)	Presentation of financial statements	1 January 2010
IAS 7 (amendment)	Statement of cash flows	1 January 2010
IAS 17 (amendment)	Leases	1 January 2010
IAS 18 (amendment)	Revenue	1 January 2010
IAS 36 (amendment)	Impairment of assets	1 January 2010
IAS 38 (amendment)	Intangible Assets	1 January 2010
IAS 39 (amendment)	Financial instruments: recognition and measurement	1 January 2010

The International Accounting Standards Board issued its amendments to IFRS 2, IFRS 5, IFRS 8, IAS 1, IAS 7, IAS 17, IAS 18, IAS 36, IAS 38 and IAS 39 on 16 April 2009, primarily with a view to removing inconsistencies and clarifying wording.

The adoption of these amendments and new interpretations did not result in any changes in the Bank's accounting policies.

b) The following new and amended standards and interpretations issued by the International Accounting Board and endorsed by the EU will be adopted in future periods

Standard / Interpretation	Content	Applicable for periods beginning on or after
IAS 24 (amendment)	Related party disclosures	1 January 2011
IAS 32 (amendment)	Financial instruments: presentation	1 February 2010
IFRS 1 (amendment)	First-time adoption of International Financial Reporting Standards	1 July 2010
IFRIC 14 (amendment)	The limit on a defined benefit assets, minimum funding requirements and their interaction	1 January 2011
IFRIC 19	Extinguishing financial liabilities with equity instruments	1 July 2010

The following standard is relevant to the Bank:

IAS 24, »Related Party Disclosures«

IAS 24 was endorsed by the European Union on 19 July 2010. The objective of the amended standard is to simplify disclosure requirements for entities associated with the government and interprets definition of a related party.

The Bank has decided not to adopt any standards, amendments or interpretations before they come into effect.

c) The following new and amended standards and interpretations issued by the International Accounting Board have so far not been endorsed by the EU

Standard / Interpretation	Content	Applicable for periods beginning on or after
IFRS 9	Financial instruments part 1: Classification and measurement	1 January 2013
IFRS 7 (amendment)	Financial instruments: Disclosures – transfer of financial assets	1 January 2011
IAS 34 (amendment)	Interim Financial reporting	1 January 2011
IAS 12 (amendment)	Income Taxes	1 January 2011
IFRS 3 (amendment)	Business Combinations	1 January 2011
IFRS 7 (amendment)	Financial Instruments: Disclousures	1 January 2011
IAS 1 (amendment)	Presentation of Financial Statements	1 January 2011
IAS 27 (amendment)	Consolidated and Separate Financial Statements	1 January 2011
IFRIC 13 (amendment)	Accounting for customer loyalty programmes	1 January 2011

The following standard is expected to be relevant to the Bank:

IFRS 9, »Financial instruments part 1: Classification and measurement«
IFRS 9 was issued in November 2009 and replaces those parts of IAS 39 relating to the classification and measurement of financial assets.
Key features are as follows:

- Financial assets are required to be classified into two measurement categories: those to be measured subsequently at fair value, and those to be measured subsequently at amortized cost. The decision is to be made at initial recognition. The classification depends on the bank's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument.
- An instrument is subsequently measured at amortized cost only if it is a debt instrument and both the objective of the entity's business model is to hold the asset to collect the contractual cash flows, and the asset's contractual cash flows represent only payments of principal and interest (that is, it has only 'basic loan features'). All other debt instruments are to be measured at fair value through profit or loss.
- All equity instruments are to be measured subsequently at fair value. Equity instruments that are held for trading will be measured at fair value through profit or loss. For all other equity investments, an irrevocable election can be made at initial recognition, to recognize unrealized and realized fair value gains and losses through other comprehensive income rather than profit or loss. There is to be no recycling of fair value gains and losses to profit or loss. This election may be made on an instrument-by-instrument basis. Dividends are to be presented in profit or loss, as long as they represent a return on investment.
- While adoption of IFRS 9 is mandatory as of 1 January 2013, earlier adoption is permitted.

The International Accounting Standards Board issued its amendments to IFRS 2, IFRS 7, IAS 1, IAS 27 on May 2010, primarily with a view to removing inconsistencies and clarifying wording.

The Bank did not apply early any standards or interpretations that are not yet effective.

The Bank is reviewing the not yet effective standards and interpretations and at this stage cannot reasonably assess the impact of the new requirements. The Bank will comply with the new standards and interpretations as and when effective.

21. Significant Accounting Policies and Estimates

a) Impairment of Loans and Receivables

The Bank assesses its portfolio of financial assets valued at amortized cost and off-balance-sheet exposure on a monthly basis. In consideration of the objective factors indicating the impairment of the financial asset valued at amortized cost, the Bank assesses the need for its impairment. The objective factors are above all: irregular settlement of liabilities and material delay over 90 days; deterioration of economic conditions in the operating industry; reprogramming due to a client's economic, legal or other problems. If any client fulfils any of the objective criteria the Bank individually assesses the anticipated cash flows for repayment (it evaluates both the expected cash flows from regular loan repayments as well as potential cash flows resulting from realization of collateral). In the case of negative difference between the discounted value of all expected cash flows and the carrying amount of the receivable, the Bank makes individual impairments. The Bank makes an assessment of the other clients collectively using its own methodology and parameters, which are reviewed on a regular basis to decrease the differences between estimated and actual losses.

Key assumptions affecting the need for additional impairment in 2011 are the following:

1. Probability of Default (PD): in case of further portfolio deterioration as a result of worsening of economic conditions, the Bank could expect higher default rates than anticipated, which would require additional impairment. As a result, the Bank assesses a possibility of further deterioration of PD in credit portfolio where an average PD could increase by 40 per cent. This would lead to an estimated 6.6 million EUR of additional impairments. Applying sensitivity of PD increased by 50 per cent or 60 per cent would lead to an estimated 8.3 million EUR or 9.9 million EUR of additional impairments.
2. Collaterals: in case of declining market value of collaterals the Bank could expect reduced cash-flows from sold collaterals and therefore additional impairment would be required. Collaterals are on the other hand seen as potential risk mitigator and the Bank put huge efforts on improving the current portfolio collateralization rate. For this reason, the Bank is considering the possibility to increase the portfolio collateralization by 20 per cent. This would lead to an estimate of 2.8 million EUR of lower impairments. Applying sensitivity of portfolio collateralization increased by 30 per cent or 40 per cent would lead to an estimate of 4 million EUR or 4.5 million EUR lower impairments.

b) Impairment of Available-for-Sale Financial Assets

Available-for-sale financial assets are impaired if there is a material or prolonged decrease of their fair value below their cost. Duration and the amount of decrease of their fair value is taken into consideration. The need for impairment may also be indicated by evidence of the deterioration in the financial position of the financial instrument's issuer and the industry sector in which the issuer operates.

Criteria applied in recognition of impairment are described in detail in Note 8 Significant accounting policies – Available-for-sale financial assets

Key assumptions affecting the need for additional impairment in 2011:

1. Instruments tied to equity securities;
   The worsening of issuer's credit quality as a consequence of further deterioration in certain industries (construction, financial holdings) and their slow recovery.
2. Instruments tied to debt securities:
   The worsening of issuer's credit quality and unfavoruable movement of market parameters, especially interest rates, as a consequence of inflation pressure in the EU area.

c) Going Concern

The Bank compiled these financial statements on a going concern basis. In making this judgment, the Management considered the Bank's financial position, current intentions, profitability of operations and access to financial resources, substantial part of which is provided by the Bank's parent company, and analyzed the impact of the recent financial crisis on the future operations of the Bank.

22. Events After the Date of the Statement of Financial Position

No significant circumstances or events occurred after the balance sheet date that would require adjustments of the financial statements, additional notes to the financial statements or explanatory notes to the shareholders.

On 9 February 2011, the Supervisory Board appointed interim Management Board of the Bank pursuant to the decisions of the relevant bodies of the parent bank. Accordingly, Alexander Picker was appointed new President of the Management Board and Matej Falatov new Member of the Management Board. Bank of Slovenia granted them licences as of 16 March 2011. New management is currently reviewing past activities of the Company. While the results of this review are not yet finalised, management do not believe this review will have any impact on the financial statements as currently presented.

The Supervisory Board approved this Annual report on 14 April 2011.

Notes

1. Interest Income and Expense

EUR '000

	2010	2009
Interest income and similar income		
Deposits with Central Bank	231	208
Financial assets held for trading	1,654	1,074
Available-for-sale financial assets	2,135	2,522
Bank loans and deposits	524	1,263
Loans and deposits from clients	78,841	80,495
Temporary purchased securities	18	2,699
Financial assets held to maturity	1,669	1,638
Other financial assets	131	1,020
Total interest income and similar income	**85,203**	**90,919**
Interest expense and other expenses		
Bank sight deposits	1	3
Sight deposits from clients	119	150
Bank deposits	16,796	25,885
Deposits from clients	10,077	10,824
Bank loans	4,353	4,034
Interest on financial liabilities held for trading	1,573	1,019
Subordinated debt	1,676	2,418
Interest on other financial liabilities	15	2
Total interest expense and other expenses	**34,610**	**44,335**
Net interest	**50,593**	**46,584**

2. Dividend Income

EUR '000

	2010	2009
Dividends from financial assets held for trading	112	-
Dividends from available-for-sale financial assets	799	596
Total dividend income	**911**	**596**

3. Fee and Commission Income and Expense

EUR '000

	2010	2009
Total fee and commission income	10,489	10,797
Total fee and commission expense	2,434	2,293
Net fee and commission (a+b)	**8,055**	**8,504**

a) Fee and commission income from trading for Bank's own account

EUR '000

	2010	2009
Fee and commission income		
Payment transactions	4,973	4,502
Loan transactions	2,028	2,022
Granted warranties	848	811
Other transactions	2,450	2,193
Total fee and commission income	**10,299**	**9,528**
Fee and commission expense		
Payment transactions	595	529
Loan transactions	3	20
Other transactions	1,767	1,538
Total fee and commission expense	**2,365**	**2,087**
Net fee and commission from transactions for bank's account	**7,934**	**7,440**

b) Fee and commission income from investing services and operations for clients' account

EUR '000

	2010	2009
Fee and commission income from investing and auxiliary investing services and operations for clients' account		
Receiving, brokerage and processing of orders	138	1,143
Financial instruments' management	5	14
Book-entry securities account management for clients	47	112
Total fee and commission from investing and auxiliary investing services and operations for clients' account	**190**	**1.269**
Fee and commission expense from investing and auxiliary investing services and operations for clients' account		
Fee and commission paid to KDD and similar organizations	28	73
Fee and commission paid to the stock exchange and similar organizations	41	133
Total fee and commission expense from investing and auxiliary investing services and operations for clients' account	**69**	**206**
Net fee and commission from investing and auxiliary investing services and operations for clients' account	**121**	**1.063**

4. Realized Gains (Losses) from Financial Assets and Liabilities not Measured at Fair Value Through Profit Or Loss

EUR '000

	2010	2009
Available-for-sale financial assets	(35)	(2,792)
Loans	-	(2)
Other financial assets and liabilities	(69)	(61)
Total	**(104)**	**(2,855)**

Gains and losses from available-for-sale financial assets comprise realized gains and losses on derecognition; gains and losses resulting from changes of fair value of available-for-sale financial assets are recognized directly in »Statement of Comprehensive Income«.

5. Net Gains (Losses) from Financial Assets and Liabilities Held for Trading

EUR '000

	2010	2009
Equity securities	(8,289)	5,379
Foreign currency purchase and sale	151	184
Derivatives	6,389	(3,540)
Other financial assets	(1)	(1)
Total	**(1,750)**	**2,023**

6. Net Gains (Losses) from Currency Translation Differences

EUR '000

	2010	2009
Items in foreign currency	(45,481)	(817)
Items in foreign exchange	46,243	579
Total	**762**	**(238)**

The currency translation differences in the table above refer to financial assets and liabilities measured at amortized cost. The currency translation differences resulting from financial assets measured at fair value are recognized as part of net gains or net losses from financial assets and liabilities classified as held for trading.

7. Other Net Operating Income / (Expenses)

EUR '000

	2010	2009
Other operating income		
Non-banking services	60	84
Other	1,505	2,072
Total other operating income	**1,565**	**2,156**
Other operating expenses		
Membership fees	(95)	(111)
Taxes and other duties	(147)	(102)
Other	(172)	(223)
Total other operating expenses	**(414)**	**(436)**
Net other operating income (expenses)	**1,151**	**1,720**

The item »Other« in other operating income comprises income from legal proceedings, compensation received and other operating income.

The most significant item under other operating expenses relates to assets earmarked as donations

8. Administrative Expenses

EUR '000

	2010	2009
Employee costs	**13,268**	**14,711**
Gross wages and salaries	9,371	9,390
Social security contributions	624	623
Pension insurance contributions	842	843
Other contributions levied on gross wages and salaries	65	66
Other labour costs	2,366	3,789
- Meal and travel allowance	832	835
- Bonuses	803	2,257
- Pay for annual leave	713	694
- Other	18	3
General and administrative expenses	**8,298**	**8,007**
Costs of materials	888	1,029
Costs of rentals	1,431	1,477
Services provided by third persons	1,486	1,491
Costs of business trips	94	95
Costs of maintenance	1,583	1,520
Costs of advertising	1,064	877
Costs of hospitality	211	190
Costs of consulting	712	599
Education fees	225	190
Insurance premiums	400	389
Other administrative costs	204	150
Total administrative expenses	**21,566**	**22,718**

As at 31 December 2010, the Bank employed 403 staff (31 December 2009: 396)

The main part of rental expenses (1,107 thousand EUR) relates to real estate (2009: 1,186 thousand EUR). The Bank has no non--cancellable lease contracts. Agreement have been concluded for an indefinite period; rentals are adjusted to 3-monthly Euribor.

Audit fees

EUR '000

	Ernst & Young		Other auditing companies	
	2010	2009	2010	2009
Audit of the annual report	45	-	45	85
Other services counselling	12	-	-	6
Tax counselling	-	-	-	-
Other non-audit services	-	-	-	-
Total audit fees	**57**	**-**	**45**	**91**

9. Depreciation and Amortization Expense

EUR '000

	Note	2010	2009
Property, plant and equipment	8	1,334	1,422
Intangible assets	9	633	578
Total depreciation and amortization expense		**1,967**	**2,000**

10. Provisions

EUR '000

	Note	2010	2009
Provisions for off-balance-sheet receivables	15	(4,161)	(2,471)
Provisions for employee benefits	15	(31)	(87)
Total provisions		**(4,192)**	**(2,558)**

11. Impairment

EUR '000

	Note	2010	2009
Available-for-sale financial assets	3a	(968)	3,248
Financial assets at amortized cost		(63,328)	(28,439)
- Government		(23)	5
- General public		(6,189)	(176)
- Other clients		(57,116)	(28,268)
Total impairment		**(64,296)**	**(25,191)**

12. Corporate Income Tax

EUR '000

	Note	2010	2009
Corporate income tax		0	439
Deferred tax	16	(6,113)	679
Total corporate income tax		**(6,113)**	**1,118**
Difference between the income tax and tax determined using basic tax rate:			
Profit before tax		(32,404)	3,831
Tax calculated using the applicable tax rate of 20 per cent (2009:21 per cent)		(6,481)	805
Income not recognized for tax purposes		(470)	(365)
Expenses not recognized for tax purposes		829	774
Income that increases the tax basis		9	14
Other		-	(110)
Total corporate income tax		**(6,113)**	**1,118**

The majority of income not recognized for tax purposes refers to exemption of received dividends and exclusion of income that was included in the tax basis in previous years.

The bulk of expenses not recognized for tax purposes relates to exemption of donations, hospitality costs and other costs.

The effective tax rate for 2010 is 18.87 per cent (2009: 29.18 per cent).

Notes to the statement of financial position

13. Cash and Balances with the Central Bank

EUR '000

	31.12.2010	31.12.2009
Cash	6,019	6,554
Balances with Central Bank excluding obligatory reserves	38,820	97,001
Cash and cash equivalents	**44,839**	**103,555**
Other short-term deposits at Central Bank - guarantee scheme	1,612	930
Obligatory reserves with Central Bank	9,056	8,637
Total cash and balances with Central Bank	**55,507**	**113,122**

Slovenian banks are required to maintain obligatory reserves with the Bank of Slovenia; the amount of obligatory reserve depends on the scope and structure of received deposits.

Currently, the Bank of Slovenia requires banks to calculate obligatory reserve in the amount of 2 per cent for all deposits with maturity of up to 2 years.

14. Financial Assets Held for Trading

EUR '000

	31.12.2010	31.12.2009
Derivatives		
Forward contracts	**5,930**	**2,290**
- foreign exchange	109	550
- equities	5,821	1,740
Options	**-**	**35**
- foreign exchange	-	35
Swaps	**2,524**	**1,948**
- foreign exchange	-	254
- interest	2,524	1,694
Total derivatives	**8,454**	**4,273**
Securities		
Shares	15,598	33,723
Other securities	40	66
Total securities	**15,638**	**33,789**
Total financial assets held for trading	**24,092**	**38,062**

As at 31 December 2010 and 2009, the Bank did not possess any pledged securities designated as held for trading.

Of the total value of the securities portfolio classified as held for trading, the securities in the amount of 9,205 thousand EUR were quoted on the stock exchange as at 31 December 2010 (31 December 2009: 22,774 thousand EUR).

The contractual values of derivatives are presented in the Note 19a.

15. Available-for-Sale Financial Assets

EUR '000

	31.12.2010	31.12.2009
Bonds	**65,091**	**62,399**
– Republic of Slovenia	20,328	15,164
– banks	30,636	32,154
– other issuers	14,127	15,081
Shares	**27,157**	**29,071**
– banks	280	218
– other issuers	26,877	28,853
Impairment	**968**	**-**
Total	**91,280**	**91,470**

Available-for-sale securities in the total amount EUR 89,648 thousand were quoted on the stock exchange as at 31 December 2010 (31 December 2009: 89,062 thousand EUR).

As at 31 December 2010, the Bank had pledged available-for-sale securities for settlements in relation to STEP2 and long-term refinancing operations. The total value of the pledged available-for-sale financial assets amounted to EUR 53,092 thousand (31 December 2009: EUR 50,236 thousand).

Fair values of available-for-sale financial assets are disclosed in the Note 4.8.c.

a) Movement of available-for-sale financial assets

EUR '000

	Note	2010	2009
Balance on 1 January		**91,470**	**59,033**
Purchases		4,994	39,408
Sales		-	(12,975)
Maturity		(2,403)	(1,202)
Interest accrued		107	(2,709)
Interest paid		-	2,548
Changes of fair value		(1,920)	4,119
Impairment	11	(968)	-
Reversal of impairment	11	-	3,248
Balance on 31 December		**91,280**	**91,470**

b) Revaluation reserve for available-for-sale financial assets

EUR '000

	Note	2010	2009
Balance on 1 January		**3,196**	**(99)**
Net gains on fair value changes		(2,888)	4,119
Transfer of (gains)/losses to profit or loss on disposal or impairment of securities		968	-
Deferred tax	16	384	(824)
Balance on 31 December		**1,660**	**3,196**

16. Loans and Deposits to Banks

EUR '000

	31.12.2010	31.12.2009
Sight deposits	6,291	6,887
Term deposits	3,900	2,002
Loans	4,000	38,040
Total	**14,191**	**46,929**

Loans to banks in the amount of EUR 3,912 thousand (31 December 2009: EUR 3,945 thousand) have a residual value of more than twelve months.

Loans to banks in the amount of EUR 10,191 thousand (31 December 2009: EUR 33,891 thousand) have the original maturity of up to three months and are considered cash equivalents.

17. Loans to Clients

EUR '000

	Note	31.12.2010	31.12.2009
Loans		2,029,070	2,006,122
Temporary purchased securities		4,386	9,736
Credit lines		15,294	13,360
Credit cards receivables		2,779	2,446
Receivables for collateral granted		2,725	2,326
Other		2,091	2,082
Impairment	6	(115,784)	(51,989)
Total		**1,940,561**	**1,984,083**

With regards to temporary purchased securities, the Bank acquires the security as collateral (it becomes its legal owner), whereas the coupon interest and dividends from such securities belong to the borrower.

Loans to clients in the amount of EUR 1,174,556 thousand (31 December 2009: EUR 1,070,240 thousand) have residual maturity of more than twelve months.

As at 31 December 2010, the Bank had pledged loans for long-term refinancing operations and settlements in relation to STEP2. The total value of pledged loans was EUR 39,174 thousand (EUR 31 December 2009: 36,459 thousand).

Other disclosures in relation to loans are presented in the Note 4.5, 4.6, 4.7, 4.8.

18. Movement of Impairment of Loans to Banks, Loans to Clients and Other Assets

EUR '000

	Loans to government	Loans to clients	Loans to other clients
Balance on 1 January 2009	**(8)**	**(2.679)**	**(21.391)**
Impairment	4	(3)	(27.912)
Balance on 31 December 2009	**(4)**	**(2.682)**	**(49.303)**
Impairment	(22)	(6.176)	(57.597)
Balance on 31 December 2010	**(26)**	**(8.858)**	**(106.900)**

19. Financial Assets Classified as Held to Maturity

EUR '000

	31.12.2010	31.12.2009
Bonds issued by the Republic of Slovenia	42,315	42,112
TOTAL	**42,315**	**42,112**

a) Movement of financial assets classified as held to maturity

EUR '000

	31.12.2010	31.12.2009
Balance on 1 January	**42,112**	**41,940**
Interest	203	172
Balance on 31 December	**42,315**	**42,112**

As at 31 December 2010, financial assets classified as held to maturity in the total amount of EUR 42,315 thousand were quoted on the stock exchange (31 December 2009: EUR 42,112 thousand).

Financial assets classified as held to maturity in the amount of EUR 36,298 thousand have a residual maturity of more than twelve months (31 December 2009: EUR 42,112 thousand).

As at 31 December 2010, the Bank had pledged securities classified as held to maturity for long-term refinancing operations and settlements in relation to STEP2. The total value of the pledged financial assets held to maturity was EUR 36,298 thousand (31 December 2009: EUR 36,141 thousand).

Fair values of assets classified as held to maturity are disclosed in the Note 4.8.

20. Property, Plant and Equipment

2010 EUR '000

	Note	Land	Buildings	Computer hardware	Furniture and other equipment	Motor vehicles	Leasehold improvements	Fixed assets in progress	Total
Purchase cost									
Balance on 1 January 2010		**367**	**2,242**	**3,677**	**5,565**	**525**	**151**	**40**	**12,567**
Increase of assets in progress		-	-	-	-	-	-	1,211	1,211
Transfer to assets		-	-	409	605	-	100	(1,114)	-
Disposals		-	-	(353)	(36)	-	-	-	(389)
Balance on 31 December 2010		**367**	**2,242**	**3,733**	**6,134**	**525**	**251**	**137**	**13,389**
Accumulated depreciation									
Balance on 1 January 2010		**-**	**(182)**	**(2,630)**	**(3,378)**	**(226)**	**(11)**	**-**	**(6,427)**
Depreciation	9	-	(56)	(528)	(639)	(103)	(8)	-	(1,334)
Disposals			-	353	35	-	-	-	388
Balance on 31 December 2010		**-**	**(238)**	**(2,805)**	**(3,982)**	**(329)**	**(19)**	**-**	**(7,373)**
Carrying amount									
Balance on 1 January 2010		**367**	**2,060**	**1,047**	**2,187**	**299**	**140**	**40**	**6,140**
Balance on 31 December 2010		**367**	**2,004**	**928**	**2,152**	**196**	**232**	**137**	**6,016**

2009 EUR '000

	Note	Land	Buildings	Computer hardware	Furniture and other equipment	Motor vehicles	Leasehold improvements	Fixed assets in progress	Total
Purchase cost									
Balance on 1 January 2009		**336**	**1,513**	**3,441**	**5,322**	**587**	**151**	**680**	**12,030**
Increase of assets in progress		-	-	-	-	-	-	838	838
Transfer to assets		31	729	309	409	-	-	(1,478)	-
Disposals		-	-	(73)	(166)	(62)	-	-	(301)
Balance on 31 December 2009		**367**	**2,242**	**3,677**	**5,565**	**525**	**151**	**40**	**12,567**
Accumulated depreciation									
Balance on 1 January 2009		**-**	**(127)**	**(2,128)**	**(2,847)**	**(136)**	**(2)**	**-**	**(5,240)**
Depreciation	9	-	(55)	(575)	(668)	(115)	(9)	-	(1,422)
Disposals		-	-	73	137	25	-		235
Balance on 31 December 2009		**-**	**(182)**	**(2,630)**	**(3,378)**	**(226)**	**(11)**	**-**	**(6,427)**
Carrying amount									
Balance on 1 January 2009		**336**	**1,386**	**1,313**	**2,475**	**451**	**149**	**680**	**6,790**
Balance on 31 December 2009		**367**	**2,060**	**1,047**	**2,187**	**299**	**140**	**40**	**6,140**

The Bank did not have any pledged assets in the period under review.

In 2010, the Bank wrote-off property, plant and equipment with the present value of 1 thousand EUR (2009: 44 thousand EUR). In the profit or loss, the write-off effect is recognized as part of net losses on derecognition of the assets excluding non-current assets held for sale.

The cost of property, plant and equipment that are fully depreciated but continue to be used by the Bank amounts to EUR 3,599 thousand (2009: EUR 3,182 thousand).

21. Intangible Assets

2010 EUR '000

	Note	Software	Long-term deferred development costs	Other intangible assets	Intangible assets in installation process	Total
Purchase cost						
Balance on 1 January 2010		**5,888**	**32**	**42**	**182**	**6,144**
Acquisitions		1,359	-	-	-	1,359
Disposals		(19)	-	-	(178)	(197)
Balance at 31 December 2010		**7,228**	**32**	**42**	**4**	**7,306**
Accumulated amortization						
Balance on 1 January 2010		**(2,402)**	**(32)**	**(42)**	**-**	**(2,476)**
Amortization	6	(633)	-	-	-	(633)
Disposals		19	-	-	-	19
Balance at 31 December 2010		**(3,016)**	**(32)**	**(42)**	**-**	**(3,090)**
Carrying amount						
Balance on 1 January 2010		**3,486**	**-**	**-**	**182**	**3,668**
Balance at 31 December 2010		**4,212**	**-**	**-**	**4**	**4,216**

2009 EUR '000

	Note	Software	Long-term deferred development costs	Other intangible assets	Intangible assets in installation process	Total
Purchase cost						
Balance on 1 January 2009		**4,661**	**32**	**42**	**44**	**4,779**
Acquisitions		1,277	-	-	138	1,415
Disposals		(50)	-	-	-	(50)
Balance at 31 December 2009		**5,888**	**32**	**42**	**182**	**6,144**
Accumulated amortization						
Balance on 1 January 2009		**(1,874)**	**(32)**	**(42)**	**-**	**(1,948)**
Amortization	9	(578)	-	-	-	(578)
Disposals		50	-	-	-	50
Balance at 31 December 2009		**(2,402)**	**(32)**	**(42)**	**-**	**(2,476)**
Carrying amount						
Balance on 1 January 2009		**2,787**	**-**	**-**	**44**	**2,831**
Balance at 31 December 2009		**3,486**	**-**	**-**	**182**	**3,668**

The cost of fully amortized intangible assets which continue to be used by the Bank amounts to EUR 683 thousand (2009: EUR 615 thousand).

In the year under review, no items of fixed assets were pledges as collateral.

22. Other Assets

EUR '000

	31.12.2010	31.12.2009
Other financial assets		
Fee and commission receivables	230	224
Receivables due from clients	19	11
Accrued income	50	755
Other receivables	484	295
Total other financial assets	**783**	**1,285**
Other non-financial assets		
Pre-payments made	18	19
Tax assets	2	2
Deferred costs	2,298	1,841
Total non-financial assets	**2,318**	**1,862**
Total	**3,101**	**3,147**

Deferred costs comprise insurance premiums, sponsorships, costs of professional literature and newspapers, lease costs, and costs of agents; these were paid in 2010 but relate to 2011.

23. Financial Liabilities to the Central Bank

EUR '000

	31.12.2010	31.12.2009
Short-term loans	40.010	80.276
Total financial liabilities to Central Bank	**40.010**	**80.276**

Financial liabilities to the Central Bank relate to long-term refinancing operations, which provide additional long-term refinancing to ensure daily liquidity. These are reverse transactions with regular maturity of three months organized on a monthly basis and which are carried out under standard tenders based on the previously published schedule.

24. Financial Liabilities Classified as Held for Trading

EUR '000

	31.12.2010	31.12.2009
Derivatives		
Forward contracts	**153**	**1,391**
- foreign exchange	110	544
- equities	43	847
Options	**-**	**35**
- foreign exchange	-	35
Swaps	**2,297**	**1,437**
- foreign exchange	13	7
- interest	2,284	1,430
Total derivatives	**2,450**	**2,863**

The contractual values of the derivatives are presented in the Note 19a.

25. Deposits and Borrowings

a) Deposits of banks and clients

EUR '000

	31.12.2010	31.12.2009
Sight deposits by	**102,783**	**111,177**
- banks	350	234
- clients	102,433	110,943
Deposits received from	**1,640,165**	**1,706,559**
- banks	1,218,296	1,338,461
- clients	421,869	368,098
Total	**1,742,948**	**1,817,736**

Deposits in the amount of 930,059 thousand EUR (31 December 2009: 820,952 thousand EUR) have a residual maturity of more than 12 months.

b) Borrowings from banks and clients

EUR '000

	31.12.2010	31.12.2009
Short-term borrowings from	**(13)**	**658**
- banks	(13)	658
Long-term borrowings from	**149,529**	**152,678**
- banks	148,696	152,678
- clients	833	-
Total	**149,516**	**153,336**

Borrowings in the amount of 131,473 thousand EUR (31 December 2009: 135,128 thousand EUR) have a residual maturity of more than twelve months.

26. Subordinated Liabilities

EUR '000

	Currency	Maturity	Interest rate	31.12.2010		31.12.2009	
				Principal	Interest	Principal	Interest
Subordinated loans	EUR	25.06.2016	3mEUR+ 0.80 %	20,000	1	20,000	1
	EUR	21.02.2017	6mEUR+ 0.65 %	38,000	2	38,000	2
	EUR	30.10.2018	3mEUR+ 4.00 %	15,000	2	15,000	2
Total				**73,000**	**5**	**73,000**	**5**
Total amortized cost				**73,005**		**73,005**	

Pursuant to the Decision on capital adequacy of banks and savings banks, subordinated long-term loans are included in bank's Tier 2 capital.

The issued loan contracts do not include any provisions on the conversion to capital or any other liabilities.

The subordinated liabilities of 73,000 thousand EUR (31 December 2009: 73,000 thousand EUR) have a residual maturity of more than twelve months.

Fair values are disclosed in the Note 4.8.

27. Provisions

EUR '000

	Provisions for off-balance-sheet liabilities		Provisions for employee benefits			Provisions for Fixed Assets received free of charge	Total
	Provisions for guarantees	Provisions for undrawn loans	Termination benefits upon retirement	Jubilee awards	Management severance payments		
Balance on 1 January 2009	**108**	**-**	**330**	**64**	**155**	**2**	**659**
Made during the year	1,713	1,507	73	16	-	2	3,311
Extinguished during the year	164	174	-	-	-	-	338
Utilized during the year	-	410	33	8	-	3	454
Balance on 31 December 2009	1,657	923	370	72	155	1	3,178
Made during the year	4,952	9,354	10	22	-	1	14,339
Extinguished during the year	3,123	7,022	-	-	-	-	10,145
Utilized during the year	-	-	7	6		2	15
Balance on 31 December 2010	**3,486**	**3,255**	**373**	**88**	**155**	**0**	**7,357**

28. Deferred Tax

EUR '000

	Note	31.12.2010	31.12.2009
Tax rate		**20 %**	**20 %**
Deferred tax assets			
Available-for-sale financial assets		26	25
Available-for-sale financial assets (impairment)		194	-
Different depreciation rates for operating and tax purposes		69	58
Provisions for employee benefits		58	61
Tax loss		5,823	-
Unutilized tax allowance		86	-
Total deferred tax assets		**6,256**	**144**
Deferred tax liabilities			
Available-for-sale financial assets (through special capital revaluation adjustment)		441	823
Different depreciation rates for operating and tax purposes		4	6
Total deferred tax liabilities		**445**	**829**
Net deferred tax assets / liabilities		**5,811**	**685**
Included in the profit or loss		**6,113**	**(679)**
Available-for-sale financial assets (impairment)		194	(682)
Different depreciation rates for operating and tax purposes		13	14
Provisions for employee benefits		(3)	(11)
Tax loss and reliefs		5,909	-
Included in equity		**383**	**(824)**
Available-for-sale financial assets (through special capital revaluation adjustment)		383	(824)

29. Other Liabilities

EUR '000

	31.12.2010	31.12.2009
Other financial liabilities		
Fees and commission payable	71	149
Payables to suppliers	712	596
Wages and salaries payable	513	482
Other liabilities from business relationships	2,304	1,681
Deferred income	272	220
Total other financial liabilities	**3,872**	**3,128**
Other non-financial liabilities		
Tax and contributions payable	479	455
Accrued expenses	1,142	2,478
Total other non-financial liabilities	**1,621**	**2,933**
Total	**5,493**	**6,061**

All the above stated financial liabilities are measured at amortized cost.

30. Equity

EUR '000

	31.12.2010	31.12.2009
Share capital	174,037	174,037
Capital surplus	2,696	2,696
Revaluation reserve	1,660	3,196
Revenue reserves (including retained earnings)	14,518	11,974
– obligatory reserves	1,862	1,862
– retained earnings / (accumulated loss)	12,656	10,112
Net profit for the year	(26,292)	2,543
Total	**166,619**	**194,446**
Interim dividends	-	15,984

The Bank's sole owner (100 per cent) is Hypo Alpe-Adria-Bank International AG, with its headquarters in Klagenfurt, Austria.

Share capital

Share capital is recorded in nominal values and has been subscribed and paid-up by the owners.

There were no changes of share capital in 2010 as compared to 2009.

The last increase in share capital was carried out in 2008, when the Bank raised 60,000 thousand EUR by issuing 14,378,489 of no-par value shares representing 52.61 per cent increase in the subscribed capital.

After the entry of shares, 41,706,318 no-par value shares labelled HYPG are registered with the central register of book-entry securities. In terms of their rights, all shares are ordinary registered no-par value shares

Capital surplus

The share premium of the Bank comprises 93 thousand EUR of surplus capital paid-up above the minimum amount of share issue (31 December 2009: 93 thousand EUR) and amounts resulting from elimination of the general capital revaluation adjustment of total 2,603 thousand EUR (31 December 2009: 2,603 thousand).

Capital surplus is not distributable.

Revaluation reserve

The revaluation reserve relates to enhancement or impairment of available-for-sale financial assets.

As at 31 December 2010, the revaluation reserve amounted to 1,660 thousand EUR (31 December 2009: 3,196 thousand EUR).

Revenue reserves

Revenue reserves may only be made from the amounts of net profit for the year and retained earnings. They are intended primarily for settlement of potential losses in the future. They are classified as obligatory reserves, reserves for treasury shares, treasury shares, statutory reserves and other revenue reserves.

According to the provisions of the Companies Act, the amount of the Bank's legal reserves, which comprise obligatory reserves and capital surplus, has to be equal to 10 per cent of the share capital of the Bank or equal to a higher percentage if so defined by the statute. When obligatory reserves and capital surplus together do not amount to the above stated amount of the share capital, the Bank has to transfer 5 per cent of net profit less the amount used to cover potential losses brought forward, to the obligatory reserves at the balance sheet preparation.

Revenue reserves in the amount of 1,862 thousand EUR (31 December 2009: 1,862 thousand EUR) represent obligatory. As at 31 December 2010, the Bank did not recognize any other revenue reserves (31 December 2009: the bank had no other revenue reserves).

Capital surplus and obligatory reserves (time reserves) may only be used under the following conditions:

a) if the total amount of these reserves does not reach the percentage of the share capital deter-mined by law or the articles of association, they may only be used:

- to cover a net loss for the financial year if it cannot be covered from retained earnings or from other revenue reserves,
- to cover a loss brought forward if it cannot be covered from the net profit for the financial year or from other revenue reserves;

b) if the total amount of these reserves exceeds the percentage of the share capital determined by law or the articles of association, the surplus amount of these reserves may be used:

- to increase the share capital from the company's assets,
- to cover a net loss for the financial year if it cannot be covered from retained earnings, provided that revenue reserves are not simultaneously used for a payout of profit to the members, and
- to cover a net loss brought forward if it cannot be covered from a net profit for the financial year, provided that revenue reserves are not simultaneously used for a payout of profit to the members

Other revenue reserves may be used for any purpose, unless stated otherwise in the statute.

Net profit / loss for the year

Net profit for the year may be used to:

- Create obligatory reserves,
- Create reserves for treasury shares,
- Create statutory reserves and
- Create other revenue reserves.

The Bank is required to cover net loss of the year within the next five years from future income and thereafter from write-offs of amounts derived from equity components.
The table below shows the appropriation of retained earnings for 2009:

EUR '000

	2010	2009
Net profit /(loss) of the year	(26,292)	2,713
Increase of revenue reserves	-	170
- legal reserves	-	170
Total retained earnings/loss	**(26,292)**	**2,543**
- retained earnings	-	2,543

The Bank has recorded a loss for the financial year 2010 in the amount of 26,292 thousand EUR (2009: net profit in the amount of 2,713 thousand EUR). The Bank's Supervisory Board has proposed to the Bank's General Meeting of Shareholders that the net loss of 2010 in the amount of 26,292 thousand EUR remains unsettled so that it may be covered in future years from the relevant profits.

31. Contingent Liabilities and Assumed Financial Obligations

EUR '000

	31.12.2010	31.12.2009
Guarantees	**86,057**	**67,653**
Service guarantees	**55,154**	**39,118**
Short-term	19,013	10,982
Long-term	36,141	28,136
Financial guarantees	**30,903**	**28,535**
Short-term	17,786	14,793
Long-term	13,117	13,742
Assumed obligations from approved loans	**107,707**	**153,684**
Approved loans	**58,844**	**67,765**
Short-term	49,013	43,750
Long-term	9,831	24,015
Approved credit lines	**48,863**	**85,919**
Derivatives	**198,592**	**287,148**
Total	**392,356**	**508,485**

Assumed liabilities from approved loans can be withdrawn within one year at the latest.
Residual maturities of financial guarantees are presented in the Note 4.6.

a) Contractual and fair values of derivative assets and liabilities by types

EUR '000

	Contractual value		Fair value 31.12. 2010		Fair value 31.12. 2009	
Type of derivatives	31.12. 2010	31.12. 2009	Assets	Liabilities	Assets	Liabilities
Forward contracts	30,048	77,012	5,930	153	2,290	1,391
– foreign exchange	4,902	41,330	109	110	550	544
– equities	25,146	35,682	5,821	43	1,740	847
Options	–	2,130	–	–	35	35
– foreign exchange	–	2,130	–	–	35	35
Swaps	168,544	208,006	2,524	2,297	1,948	1,437
– foreign exchange	4,600	60,222	–	13	254	7
– interest	163,944	147,784	2,524	2,284	1,694	1,430
Total derivatives	**198,592**	**287,148**	**8,454**	**2,450**	**4,273**	**2,863**

Nominal value indicate derivatives recorded in the off-balance-sheet, whereas the fair value indicate the carrying amount of the derivative recorded in the balance sheet; the assets are included in the financial assets held for trading, and the liabilities are included in the financial liabilities held for trading and represent a negative evaluation of the derivatives.

Other notes

32. Operating on Behalf and for Account of Third Parties

In accordance with the local legislation, this note includes presentation of assets and liabilities of clients resulting from intermediary operations. As at 31 December 2010, the Bank managed assets of total 202 thousand EUR (31 December 2009: 346 thousand EUR) on account of intermediary operations on behalf and for the account of third parties. These assets are recorded separately from the bank's own assets in the off-balance-sheet records as authorized operations.

EUR '000

	31. 12. 2010	31. 12. 2009
ASSETS	**202**	**346**
Receivables of the settlement account or transaction accounts for clients' assets	**32**	**90**
From financial instruments (31.a.)	28	44
To Central Securities Clearing Corporation or bank's settlement account for sold financial instruments	4	9
To other settlement systems and institutions for sold (clients') financial instruments	-	37
Clients' cash	**170**	**256**
On the settlement account for client's assets	170	256
Liabilities	**202**	**346**
Liabilities of the settlement account or transaction accounts for clients' assets	**202**	**346**
To clients from cash and financial instruments	174	301
To other settlement systems and institutions for purchased (suppliers') financial instruments	24	2
To bank or bank's settlement account for commission, costs and similar items	4	43

a) Receivables of the settlement account or transaction accounts for clients' assets

EUR '000

	31. 12. 2010	31. 12. 2009
Off-balance-sheet records		
1. Clients' financial instruments, separately by services	28	44
Receiving, brokerage and processing orders	4	44
Custody services	24	-

33. Related party transactions

Bank's exposure to entities in special relationship with the Bank

EUR '000

	Members of the Management Board and their close family members, staff with individual contracts of employment and the members of management of related parties		Members of the Supervisory Board	
	2010	2009	2010	2009
Granted loans				
Balance on 1 January	**2,113**	**1,694**	**-**	**-**
New loans	321	684	-	-
Repayments	358	406	-	-
Balance on 31 December	**2,076**	**2,113**	**-**	**-**
Interests and fee income	30	42		
Received deposits				
Balance on 1 January	**687**	**766**	**-**	**-**
Balance on 31 December	**725**	**687**	**-**	**-**
Interests expences	2	24		
Approved overdrafts and loans				
Balance on 1 January	200	94	-	-
Balance on 31 December	183	200	-	-
Earnings				
Salaries and other short-term benefits	1,910	1,834	-	-
Awards	141	164	-	-
Attendance fees and annual compensation	-	-	8	8
Provisions for employees benefits	110	107	-	-

Earnings of members of the Management Board in 2010 are presented in the table below

	Romih Anton- President of the Management Board	Golob Urban- Member of the Management Board	Lah Andrej- Member of the Management Board
Salaries	188	160	130
Variables	-	-	-
Reimbursements	1	1	1
Insurance	1	1	1
Other	-	-	-

Remuneration of the Management Board is based on the Supervisory Board's assessment, which is based on the annual accounts of the Bank for the previous year and on the achievements of the yearly plan and agreed objectives of the Bank for the previous year.

In accordance with the Rules of procedure of the Supervisory Board of Hypo Alpe-Adria-Bank d.d, members of the Supervisory Board who are employed in Hypo Group Alpe Adria, are not entitled to attendance fees or incentives. Accordingly, for the year 2010, attendance fees were paid only to the member of the Supervisory Board, who is not an employee of Hypo Group Alpe Adria.

Bank's exposure to related parties

EUR '000

	Controlling company		Related parties	
	2010	2009	2010	2009
Assets				
1. Financial assets held for trading				
Balance on 1 January	321	–	–	–
Balance on 31 December	375	321	–	–
2. Loans				
2.1. Loans to banks				
2.1.1. Sight deposits				
Balance on 1 January	3,553	6,029	272	7
Balance on 31 December	4,798	3,553	290	272
Other loans				
Balance on 1 January	25,002	74,457	–	–
New loans	717,998	743,033	–	–
Repayments	743,000	792,488	–	–
Balance on 31 December	–	25,002	–	–
2.2. Loans to clients				
2.2.1. Long-term loans				
Balance on 1 January	–	–	–	–
New loans	–	–	–	–
Repayments	–	–	–	–
Balance on 31 December	–	–	–	–
3. Other assets				
Balance on 1 January	–	–	33	474
Balance on 31 December	–	–	37	33
Liabilities				
1. Financial liabilities held for trading				
Balance on 1 January	1,438	793	–	–
Balance on 31 December	2,005	1,438	58	–
2. Financial liabilities at amortized cost				
2.1. Deposits				
2.1.1. Sight deposits				
Balance on 1 January	–	–	7,350	10,903
Balance on 31 December	4	–	1,309	7,350
2.1.2. Short-term deposits				
Balance on 1 January	20,601	20,002	20,500	10,128
Increases	112,500	20,600	–	514,741
Decreases	110,600	20,001	–	504,369
Balance on 31 December	21,501	20,601	5,747	20,500
2.1.3. Long-term deposits				

	Controlling company		Related parties	
	2010	2009	2010	2009
Balance on 1 January	1,317,605	1,329,511	-	22
Increases	610,700	123,741	-	-
Decreases	750,047	135,647	-	22
Balance on 31 December	1,178,258	1,317,605	-	-
2.2. Loans from banks				
2.2.1. Short-term loans				
Balance on 1 January	658	-	-	-
Increases	-	1,124	-	-
Decreases	658	466	-	-
Balance on 31 December	-	658	-	-
2.3. Subordinated debt				
Balance on 1 January	73,005	73,009	-	-
Increases	1,676	2,422	-	-
Decreases	1,676	2,426	-	-
Balance on 31 December	73,005	73,005	-	-
3. Other liabilities				
Balance on 1 January	120	266	1	19
Balance on 31 December	35	120	6	1
OFF-BALANCE-SHEET ITEMS				
Issued guarantees				
Balance on 1 January	406	549	1,250	935
Balance on 31 December	270	406	1,793	1,250
INCOME STATEMENT				
Interest income	**225**	**566**	**140**	**317**
Interest expenses	**20,879**	**28,728**	**217**	**214**
Commission income	**-**	**-**	**115**	**89**
Commission expenses	**-**	**-**	**23**	**83**
Other income	**5**	**-**	**-**	**-**
Other expenses	**266**	**217**	**1,130**	**1,201**
Trading results	**(559)**	**(515)**	**(11)**	**-**

The Bank is a 100 per cent subsidiary of Hypo Alpe Adria International AG with registered office in Klagenfurt, Austria, and has no investments in subsidiaries or associates, or banks. However, the Bank is indirectly connected with the banks and enterprises in the Hypo Group through its parent bank.

The Bank cooperates with its parent bank, related banks and enterprises in the area of loans, deposits, issuing of letters of credit and warranties as shown in the table above.

In accordance with Article 545 of the Companies Act, we hereby declare that to the extent of circumstances known to it, the Bank performs services between related parties under the market conditions.

4.5 Financial Risk Management

Risk awareness and proactive focus on risk management are the two key elements, which are reflected in the operating activities of the Hypo Group.

Risk management process in Hypo Alpe-Adria-Bank d.d. comprises three components:
- The controlling component, which consists of identification, measurement (analyzing, valuation), monitoring of risks from portfolio's point of view and risk reporting;
- The risk limiting component;
- The risk managing component, which consists of risk acceptance, risk avoidance and mitigation, transfer and risk diversification.

Risk management unit continues to actively assess the efficiency of the risk management process by:
- Identifying individual risks the Bank is exposed to;
- Defining the measurement methods for materially important risks;
- Drafting guidelines for managing individual risks;
- Suggesting limits for individual risk exposure; and
- Performing other activities aimed at managing risks the Bank is exposed to.

The Bank's Management Board defines the Bank's strategy and goals and is responsible for assumed risks (within the Group's strategy and goals). The strategy is explained in more details at the ALCO (Asset and Liabilities Committee) meetings. Business departments are responsible for implementing business goals and are liable for risk management related to these goals. Risk is managed actively on all levels and within the valid risk limits (defined by departments/functions that are independent in respect of operating sectors) by performing activities for assuming risk, avoiding risk and mitigating, transferring and diversifying risk.

In 2010, the Bank continued the appropriate internal capital adequacy assessment process as defined by the second pillar of the new capital directive (Basel II). The Bank monitored some specific key indicators of economic development (GPD, consumer's spending index, industrial orders and similar) through its RECO committee that deals with all important risks comprehensively and in one place; the Bank's intention was to identify those industrial sectors, where the enterprises faced the biggest problems that influenced their ability to service granted loans thus increasing the risk level in the Bank's credit portfolio. On the basis of this information, the board suggested guidelines for adjustment of Bank's operating policy and its risk management strategy.

The Bank has implemented a new credit process pursuant to the guidelines and the parent bank's policies. Most of Bank's attention was put on managing problematic investments, as the poor payment discipline of companies consistently aggravated throughout 2010. This led to the increase of clients and loans exposures in delay, deterioration in the Bank's loan portfolio, and consequently high value of impairments.

In 2010, the Bank made in-depth analysis of the loan portfolio within the framework of the project managed by the parent bank. The Bank defined investment strategy for the period of one year for each client separately in particular by checking the credit rating of individual clients, their business plans and value of collaterals. The main goal of carried out activities was creating a sufficient amount of impairments and managing the Bank's capital adequacy. The key goal of the Bank for 2011 is efficient management and control of risk-weighted assets and their optimization, and consequent capital management.

The Bank is aware of the effect the global decline of economic activity has on collaterals, above all on values of real estate property and securities; this is why it regularly runs the so-called "stress scenarios" in respect of decrease of the credit collateral and studies the results of these simulations. Once the value of the collateral falls below the internally defined minimum ratio, the Bank calls upon its clients to either provide additional collateral or repay the loan. Management of collateral is the key to managing the Bank's capital and required impairments of the Bank's credit portfolio.

In respect of the liabilities related to obtaining additional financing sources, the Bank acts pursuant to instructions of the parent bank in Austria. The agreed credit lines are compliant with the plans for continuing growth of the credit portfolio in the middle and small enterprise's segment. On the other hand, the Bank plans to acquire new assets for financing of investments through received deposits from legal entities as well as individuals, as set in the planned goals.

The Bank does not expect a significant improvement of financial markets and economic environment in 2011. Active monitoring and risk management (above all credit risk) in respect of the clients and collateral continues to be the Bank's primary task for the future.

The Bank manages its capital adequacy from a regulatory perspective as well as from the internal planning perspective (ICAAP – Internal Capital Adequacy Assessment Process) on a monthly basis. Comprehensive overview of current and planned capital adequacy is presented at quarterly RECO meetings (Risk Executive Committee), where the Management Board is present to ensure that all necessary strategic decisions in terms of business and risk are made in a timely manner. For assuring appropriate level of capital adequacy, the Bank has set the RWA (Risk Weighted Assets) limits for controlling the growth.

Especially in ICAAP process, the Bank manages its capital adequacy based on internal systems and methodology and constant validation of the risk parameters.

Credit Risk

Credit risk is a risk of financial loss resulting from the debtor's inability to fulfil his financial or contractual obligation towards the Bank in part or in full for any reason. Credit risk management is a key component of the Bank's diligent and safe operations. Diligent credit risk management comprises prudent management of the relationship between risk and return and supervision and reduction of credit risk through different perspectives, such as quality, concentration, currency, maturity, collateral and type of loans.

Throughout the duration of the credit relationship with the client, the Bank monitors client's operations and quality of the financial asset's collateral or the assumed liability.

The starting point for monitoring and classification of clients is a systematic review of the Bank's portfolio. The Bank classifies the financial assets measured at amortized costs or assumed liabilities in the off-balance sheet items on the basis of the internal methodology.

In 2010, the Bank has, in accordance with the decisions of the Bank of Slovenia, considered all the exposures, where the Bank's exposure to a single debtor exceeded EUR 150,000, as individually relevant financial asset or assumed liability in the off-balance-sheet items and has regularly and individually evaluated them.

Other key indicators of the potential impairment of the financial asset, which are used by the Bank as criteria for individual assessment of the debtor, are:

- The client is in delay with repayment of its obligations in the materially important amount for at least 90 days;
- Bankruptcy or compulsory settlement of the client;
- Proof of client's serious financial problems, including amongst other reprogramming due to the client's economic, legal or other problems, irregular settlement of liabilities within the group of related entities and significant economic problems in the client's industry.

For clients that represent individually insignificant exposure for the Bank or for clients for which the Bank estimates, upon individual assessment, that individual impairment of the financial asset is not required, a collective calculation of the portfolio impairment of the financial asset is made. The Bank recognizes the percentage of the group impairment as loss for the year.

The Bank has adopted additional measures designed to ensure the appropriate supervision over credit risks. New tools were implemented to the investment decision procedure in this respect; these tools are used for credit rating classification of clients.

The table of the Bank's internal credit ratings mapped pursuant to the credit ratings of external credit rating agencies.

Internal Rating	PD	S & P	Moodys	Fitch	Investment grade
1A	0,000 %	AAA, AA+	Aaa, Aa1	AAA, AA+	Investment grade
1B	0,014 %	AA	Aa2	AA	Investment grade
1C	0,028 %	AA-	Aa3	AA-	Investment grade
1D	0,042 %	A+	A1	A+	Investment grade
1E	0,056 %	A	A2	A	Investment grade
2A	0,070 %				Investment grade
2B	0,105 %	A-	A3	A-	Investment grade
2C	0,158 %	BBB+	Baa1	BBB+	Standard monitoring
2D	0,236%	BBB	Baa2	BBB	Standard monitoring
2E	0,354 %	BBB-	Baa3	BBB-	Standard monitoring
3A	0,532 %				Standard monitoring
3B	0,797 %	BB+	Ba1	BB+	Standard monitoring
3C	1,196 %	BB	Ba2	BB	Standard monitoring
3D	1,800 %	BB-	Ba3	BB-	Standard monitoring
3E	2,700 %				Standard monitoring
4A	4,050 %	B+	B1	B+	Standard monitoring
4B	6,075 %				Standard monitoring
4C	9,113 %	B	B2	B	Standard monitoring
4D	13,669 %	B-	B3	B-	Standard monitoring
4E	20,503 %	CCC+, CCC, CCC-, CC, C	Caa1, Caa2, Caa3, Ca, C	CCC+, CCC, CCC-, CC, C	Special monitoring
5A	100,000 %	D	D	D	Default
5B	100,000 %	D	D	D	Default
5C	100,000 %	D	D	D	Default
5D	100,000 %	D	D	D	Default
5E	100,000 %	D	D	D	Default

The Bank also places much attention to identification and monitoring of credit risk concentration. The risk management department prepares regular monthly reports on risks in the credit portfolio of the Bank for the decision makers; part of this report is notification on exposure to excessive concentration above all in specific industries, credit rating groups and type of collateral.

The total exposure of the Bank from the credit risk as at 31 December 2010 amounts to EUR 2,454,092 thousand. The capital requirement in respect of the credit risks is presented in the Equity calculation table.

Different overviews of the credit risk exposures as at 31 December 2010 are presented below:

a) The highest (maximum) credit risk exposure without taking into consideration the collateral or other improvements (the carrying value of the receivable decreased for potential impairment losses; in the case of financial assets at fair value, the amounts in the table below show present fair value and not the risk resulting from the future change of the fair value)

			2010			2009
	Gross	Adjustments	Net	Gross	Adjustments	Net
I. Balance sheet items	**2,99,080**	**116,709**	**2,182,371**	**2,342,210**	**51,990**	**2,290,221**
1. Cash and balances with Central Bank	55,507	0	55,507	113,122	--	113,122
2. Loans to banks	14,191	0	14,191	46,929	--	46,929
3. Loans to clients	**2,057,271**	**116709**	**1,940,562**	**2,036,072**	**51,990**	**1,984,083**
3a. Loans to individuals	**560,401**	**8,844**	**551,558**	**517,895**	**2,678**	**515,218**
-Housing loans	405,974	1,025	404,949	353,737	744	352,993
-Consumer credits	144,191	7,502	136,690	155,055	1,896	153,159
-Other	10,236	317	9,919	9,104	38	9,066
3b. Corporate loans	**1,496,870**	**107,866**	**1,389,004**	**1,518,177**	**49,312**	**1,468,865**
-Large enterprises	537,837	43,404	494,433	584,221	17,236	566,985
-Small and medium enterprises	346,010	13,235	332,775	288,123	8,256	279,867
-Other	613,022	51,226	561,796	645,833	23,821	622,012
4. Financial assets held for trading	18,619	0	18,619	11,220	-	11,220
5. Financial assets held to maturity and available-for-sale financial assets	133,596	0	133,596	133,582	-	133,582
6. Other financial assets	19,897	0	19,897	1,285	-	1,285
II. Off-balance-sheet items	**155,012**	**3,845**	**151,167**	**182,221**	**1,824**	**180,397**
1. Financial guarantees	30,903	976	29,927	28,535	503	28,032
2. Undrawn loans	124,109	2,869	121,240	153,686	1,320	152,365
Total maximum exposure to credit risk	**2,454,092**	**120,554**	**2,333,538**	**2,524,431**	**53,813**	**2,470,618**

b) Overview of the exposure and impairment percentage for individual credit ratings segments

		2010		2009
Credit rating	Gross value (%)	Percentage of impairments (%)	Gross value (%)	Percentage of impairments (%)
Investment grade	4.16 %	0.26 %	5.81 %	0.11 %
Standard monitoring	71.88 %	15.26 %	86.94 %	46.23 %
Special monitoring	0.80 %	0.25 %	0.59 %	0.39 %
Default	23.16 %	84.23 %	6.67 %	53.27 %
	100.00 %	**100.00 %**	**100.00 %**	**100.00 %**

The Bank values the received collateral pursuant to the internal manual on management and valuation of the collateral. The value of collateral depends above all on market conditions, time remaining to the realization of the collateral and related costs. Conditions for the appropriate insurance of the exposures are defined in the Bank's internal acts. The Bank pays special attention to continuous improvement of all conditions for legal executability of collaterals. In the case of the payment default the Bank is entitled to sell the assets received as collateral in accordance with the contractual and legal provisions.

c) Credit risk concentration as per geographic location

31.12.2010	Slovenia	Other EU countries	Countries of former Yugoslavia	Other	Total
Content					
I. Balance sheet items	**2,290,076**	**6,458**	**136**	**2,410**	**2,299,080**
1. Cash and balances with Central Bank	55,507	0	0	0	55,507
2. Loans to banks	14,191	0	0	0	14,191
3. Loans to clients	**2,051,709**	**3,015**	**136**	**2,410**	**2,057,271**
3a. Loans to individuals	**559,947**	**241**	**136**	**77**	**560,401**
-Housing loans	405,764	134	0	76	405,974
-Consumer credits	144,012	53	126	1	144,191
-Other	10,172	54	10	0	10,236
3b. Corporate loans	**1,491,762**	**2,774**	**0**	**2,333**	**1,496,870**
-Large enterprises	537,837	0	0	0	537,837
-Small and medium enterprises	346,010	2,774	0	0	346,010
-Other	607,915	0	0	2,333	613,022
4. Financial assets held for trading	15,176	3,443	0	0	18,619
5. Financial assets held to maturity and available-for-sale financial assets	133,596	0	0	0	133,596
6. Other financial assets	19,897	0	0	0	19,897
II. Off-balance-sheet items	**154,547**	**235**	**229**	**2**	**155,012**
1. Financial guarantees	30,456	235	212	0	30,903
2. Undrawn loans	124,091	0	17	2	124,109
Total maximum exposure to credit risk	**2,444,623**	**6,693**	**365**	**2,412**	**2,454,092**

31.12.2009	Slovenia	Other EU countries	Countries of for-mer Yugoslavia	Other	Total
Content					
I. Balance sheet items	**2,300,720**	**37,935**	**761**	**2,794**	**2,342,210**
1. Cash and balances with Central Bank	113,122	-	-	-	113,122
2. Loans to banks	15,458	30,769	189	513	46,929
3. Loans to clients	**2,029,889**	**3,376**	**572**	**2,235**	**2,036,072**
3a. Loans to individuals	**517,895**	**-**	**-**	**-**	**517,895**
-Housing loans	353,737	-	-	-	353,737
-Consumer credits	155,055	-	-	-	155,055
-Other	9,104	-	-	-	9,104
3b. Corporate loans	**1,511,994**	**3,376**	**572**	**2,235**	**1,518,177**
-Large enterprises	584,221	-	-	-	584,221
-Small and medium enterprises	288,123	-	-	-	288,123
-Other	639,650	3,376	572	2,235	645,833
4. Financial assets held for trading	7,384	3,790	-	46	11,220
5. Financial assets held to maturity and available-for-sale financial assets	133,582	-	-	-	133,582
6. Other financial assets	1,285	-	-	-	1,285
II. Off-balance-sheet items	**181,705**	**429**	**85**	**1**	**182,221**
1. Financial guarantees	28,044	429	62	0	28,535
2. Undrawn loans	153,661	-	23	1	153,686
Total maximum exposure to credit risk	**2,482,425**	**38,364**	**846**	**2,796**	**2,524,431**

d) Credit risk concentration as per industries

31.12.2010	Financial institutions	Manufacturing	Real estate	Wholesale and retail trade	Public sector	Other industries	Individuals	Total
I. Balance sheet items	**294,753**	**304,585**	**339,210**	**190,348**	**67,347**	**542,435**	**560,401**	**2,299,080**
1. Cash and balances with Central Bank	55,507	0	0	0	0	0	0	55,507
2. Loans to banks	**14,191**	**0**	**0**	**0**	**0**	**0**	**0**	**14,191**
3. Loans to clients	**67,792**	**301,368**	**338,670**	**189,345**	**67,347**	**532,347**	**560,401**	**2,057,271**
3a. Loans to individuals	**0**	**0**	**0**	**0**	**0**	**0**	**560,401**	**560,401**
-Housing loans	0	0	0	0	0	0	405,974	405,974
-Consumer credits	0	0	0	0	0	0	144,191	144,191
-Other	0	0	0	0	0	0	10,236	10,236
3b. Corporate loans	**67,792**	**301,368**	**338,670**	**189,345**	**67,347**	**532,347**	**0**	**1,496,870**
-Large enterprises	29,510	180,210	54,176	115,337	0	158,604	0	537,837
-Small and medium enterprises	30,340	91,462	67,119	50,702	2,792	103,596	0	346,010
-Other	7,942	29,695	217,375	23,307	64,555	270,147	0	613,022
4. Financial assets held for trading	3,771	3,217	540	1,003	0	10,088	0	18,619
5. Financial assets held to maturity and available-for--sale financial assets	133,596	0	0	0	0	0	0	133,596
6. Other financial assets	19,897	0	0	0	0	0	0	19,897
II. Off-balance-sheet items	**5,891**	**30,293**	**39,349**	**22,777**	**504**	**56,198**	**0**	**155,012**
1. Financial guarantees	466	5,495	2,255	8,312	17	14,359	0	30,903
2. Undisbursed loans	5,425	24,798	37,094	14,464	488	41,839	0	124,109
Total maximum exposure to credit risk	**300,645**	**334,878**	**378,560**	**213,125**	**67,852**	**598,633**	**560,401**	**2,454,092**

31.12.2009	Financial institutions	Manufacturing	Real estate	Wholesale and retail trade	Public sector	Other indu-stries	Individuals	Total
I. Balance sheet items	**267,041**	**311,322**	**316,955**	**219,697**	**114,027**	**594,817**	**518,351**	**2,342,210**
1. Cash and balances with Central Bank	113,122	-	-	-	-	-	-	113,122
2. Loans to banks	**46,929**	**-**	**-**	**-**	**-**	**-**	**-**	**46,929**
3. Loans to clients	**61,068**	**310,436**	**316,550**	**193,404**	**56,751**	**579,967**	**517,895**	**2,036,072**
3a. Loans to individuals	**-**	**-**	**-**	**-**	**-**	**-**	**517,895**	**517,895**
-Housing loans	-	-	-	-	-	-	353,737	353,737
-Consumer credits	-	-	-	-	-	-	155,055	155,055
-Other	-	-	-	-	-	-	9,104	9,104
3b. Corporate loans	**61,068**	**310,436**	**316,550**	**193,404**	**56,751**	**579,967**	**-**	**1,518,177**
-Large enterprises	38,785	185,058	31,482	130,035	-	198,861	-	584,221
-Small and medium enter-prises	11,698	85,026	68,162	36,098	3,381	83,758	-	288,123
-Other	10,586	40,352	216,905	27,271	53,370	297,348	-	645,833
4. Financial assets held for trading	4,420	887	405	756	-	4,297	456	11,220
5. Financial assets held to maturity and available-for--sale financial assets	40,217	-	-	25,536	57,276	10,553	-	133,582
6. Other financial assets	1,285	-	-	-	-	-	-	1,285
II. Off-balance-sheet items	**11,692**	**45,338**	**46,079**	**16,452**	**259**	**49,520**	**12,882**	**182,221**
1. Financial guarantees	3,891	7,093	609	6,262	17	10,664	-	28,535
2. Undisbursed loans	7,802	38,245	45,470	10,189	242	38,856	12,882	153,686
Total maximum exposure to credit risk	**278,733**	**356,660**	**363,034**	**236,149**	**114,286**	**644,337**	**531,232**	**2,524,431**

As at 31 December 2010, the total Bank exposure to credit risk amounted to EUR 2,454,092 thousand. The credit risks exposure towards clients amounts to EUR 2,057,271 thousand. The biggest share in the loans to individuals segment belongs to housing loans (72.44 per cent); in the corporate segment, the biggest share belongs to the other industry sectors (40.95 per cent). The biggest share of receivables relates to enterprises located in the Republic of Slovenia and accounts for 99.61 per cent of the total exposure.

The Bank continuously monitors the movement of the Bank's credit portfolio and assesses the possibilities of excessive concentration in individual industries by using SWOT analysis of individual industries. These analyses are the basis for adoption of business decisions affecting the Bank's investment policy in respect of reduction of excessive exposure in industries with identified increased credit risk. Thorough analyses are prepared on a quarterly basis and are a part of regular reporting and discussion at the risk management committee.

e) Overview of the credit risk for the item »Loans to banks« and »Loans to clients«

		2010		2009
Exposure	Loans to banks	Loans to clients	Loans to banks	Loans to clients
Exposure that is neither past due nor impaired	14,648	436,055	47,430	542,124
Exposure that is past due but is not individually impaired	0	54,663	-	45,942
Exposure that is not past due and is grouply impared	0	1,302,734	-	1,495,662
Exposure that is individually impaired	0	418,374	-	171,390
Total	**14,648**	**2,211,827**	**47,430**	**2,255,118**
Value of adjustments (impairments)	**0**	**120,554**	**0**	**53,813**
Net	**14,648**	**2,091,297**	**47,430**	**2,201,305**
Individual impairments	0	95,221	-	30,248
Group impairments	0	25,309	-	23,565
Total	**0**	**120,530**	**-**	**53,813**

* The table includes the balance sheet and off-balance sheet exposure, excluding service guarantees.

f) Loans and advances neither past due nor impaired

	Loans to clients							
31.12.2010	Loans to individuals			Corporate loans				
Credit rating	Housing loans	Consumer credit	Other	Large enterprises	Medium and small enterprises	Other	Total loans to clients	Loans to banks
Investment grade	0	0	0	0	20,087	0	20,087	779
Standard grade	165,406	100,015	14,729	21,955	61,532	41,865	405,502	13,875
Special monitoring	805	331	104	0	0	333	1,573	12
Default class	293	304	75	5,036	1,118	2,066	8,893	0
Total	**166,504**	**100,650**	**14,909**	**26,992**	**82,737**	**44,264**	**436,055**	**14,648**

	Loans to clients							
31.12.2009	Loans to individuals			Corporate loans				
Credit rating	Housing loans	Consumer credit	Other	Large enterprises	Medium and small enterprises	Other	Total loans to clients	Loans to banks
Investment grade	-	-	-	-	208	15,466	15,674	2,043
Standard grade	180,382	105,179	12,842	43,118	66,427	95,000	502,948	45,376
Special monitoring	675	289	17	-	-	86	1,067	12
Default class	387	400	35	66	2,894	18,652	22,434	0
Total	**181,443**	**105,868**	**12,894**	**43,185**	**69,529**	**129,205**	**542,124**	**47,430**

* The tables include the balance sheet and off-balance sheet exposure, excluding service guarantees.

g) Loans and advances past due but not impaired

31.12.2010	Loans to individuals		
	Housing loans	Consumer credit	Other
Delay up to 30 days	835	155	2,381
Delay from 31 to 60 days	5,289	2,972	58
Delay from 61 to 90 days	62	15	49
Total	**6,187**	**3,141**	**2,488**
Internal collateral value	5,951	2,992	2,062
Unsecured part of the exposure	236	149	426

31.12.2010	Corporate loans		
	Large enterprises	Small and medium enterprises	Other
Delay up to 30 days	2,520	5,797	1,940
Delay from 31 to 60 days	0	1,638	4,033
Delay from 61 to 90 days	636	0	248
Total	**3,156**	**7,435**	**6,221**
Internal collateral value	3,155	7,100	6,108
Unsecured part of the exposure	1	335	113

31.12.2009	Loans to individuals		
	Housing loans	Consumer credit	Other
Delay up to 30 days	311	194	1.778
Delay from 31 to 60 days	6,075	2,917	71
Delay from 61 to 90 days	37	14	33
Total	**6,423**	**3,125**	**1,882**
Internal collateral value	6,410	3,087	-
Unsecured part of the exposure	13	38	1,882

31.12.2009	Corporate loans		
	Large enterprises	Small and medium enterprises	Other
Delay up to 30 days	10,787	5,665	9,679
Delay from 31 to 60 days	710	174	1,572
Delay from 61 to 90 days	0	720	15,443
Total	**11,497**	**6,559**	**26,694**
Internal collateral value	11,497	6,559	26,694
Unsecured part of the exposure	0	0	0

Collateral value is calculated up to the exposure value of the loan. In cases where unsecured part of the exposure is 0, amounts of past due loans are fully collateralized.

* The tables include the balance sheet and off-balance sheet exposure, excluding service guarantees.

h) Loans and advances to clients past due and impaired

Only individually impaired assets are taken into consideration. Collective impairments are calculated and treated as portfolio risk provisions.

	Loans to individuals			Corporate loans			
31.12.2010	Housing loans	Consumer credit	Other	Large enterprises	Medium and small enterprises	Other	Total
Individually impaired exposure	1.034	14.021	157	179,982	42,858	180,412	418,374
Individual impairments	263	7.382	148	36,477	9,231	41,719	95,221
Internal collateral value	784	4.481	0	58,193	17,763	77,019	158,240

	Loans to individuals			Corporate loans			
31.12.2009	Housing loans	Consumer credit	Other	Large enterprises	Medium and small enterprises	Other	Total
Individually impaired exposure	-	5,554	67	45,028	21,554	99,187	171,390
Individual impairments	-	1,697	30	9,250	4,407	14,865	30,248
Internal collateral value	-	1,437	-	5,662	5,842	53,892	66,832

The table consists of:

- Exposure of loans which are individually impaired before taking collaterals into consideration Amounts of individual impairments,
- Internal value of collateral for loans which are individually impaired up to the exposure.

The share of exposure that is not past due and is not impaired represents 23.20 per cent of the total exposure of "Loans to clients". Exposures that are past due but are not impaired represent 2.66 per cent of the total exposure of "Loans to clients".

* The tables include the balance sheet and off-balance sheet exposure, excluding service guarantees.

i) Loans and advances renegotiated

EUR '000

	2010	2009
Renegotiated loans and advances to clients	281,581	131,226
- Continuing to be individually impaired after restructuring	242,361	112,311

j) Debt securities

The tables below present an analysis of bank book and trading book securities by rating grades.

At 31 December 2010	Available-for-sale financial assets	Financial investments classified as held to maturity
Investment grade	57,000	42,315
Standard monitoring	8,091	
Total	**65,091**	**42,315**

At 31 December 2009	Available-for-sale financial assets	Financial investments classified as held to maturity
Investment grade	43,719	42,112
Standard monitoring	18,681	-
Total	**62,400**	**42,112**

k) Repossessed collateral

EUR '000

	31.12.2010	31.12.2009
Nature of assets	Carrying amount	Carrying amount
Quoted shares (Ljubljana Stock Exchange)	24,557	26,662

In general, the Bank will dispose of assets, which are not readily convertible in cash, when the Bank is estimating to achieve the highest possible selling price for these assets with the goal to achieve the highest possible repayment of its claims or even achieve additional profit. The Bank in general does not use these assets in its operations.

Liquidity risk

Liquidity risk is a risk that the Bank is not able to timely and fully fulfil its financial obligations. It derives from time inconsistency between received assets and liabilities. The importance of effective controlling and managing of the liquidity risk has increased at the time of the financial crisis.

The Bank manages short-term liquidity risk on the basis of weekly cash flows planning for the period of one year. Based on the contractual maturity of assets and liabilities and considering the requirements of liquidity reserves, the new system support "Liquidity Tool" enables reporting on requirements for additional liquidity sources on the basis of different scenarios for general and special liquidity crisis prepared in advance.

The Bank's liquidity is managed in the department of the Asset Liability Management where all known liability flows are recorded.

Realization of the liquidity management is reviewed at monthly ALCO meetings, where the following information is presented:

- The amount and implementation of the obligatory reserve,
- Achieved liquidity ratios,
- Status of refinancing by the parent bank and
- Access to the primary liquidity of the Central Bank.

The table below presents the cash flows of financial assets and financial liabilities by residual maturities at the balance sheet date. The amounts disclosed in the table are the contractual and undiscounted cash flows. Financial guarantees are presented as gross contractual amounts per the earliest date they could be called.

Balance sheet items as per mismatch of terms at 31 December 2010

EUR '000

	Sight	Up to 30 days	From 31 up to 90 days	From 91 days up to 1 year	From 1 up to 5 years	Over 5 years	Total
Financial assets	**335,378**	**4,450**	**192,174**	**869,053**	**685,182**	**478,290**	**2,564,527**
Financial liabilities							
Financial liabilities to Central Bank	-	-	40,010	-	-	-	40,010
Financial liabilities held for trading	2,450	-	-	-	-	-	2,450
Financial liabilities measured at amortized cost	145,021	209,914	218,943	248,827	886,512	321,636	2,030,853
Other financial liabilities	14	5,279	-	200	-	-	5,493
Total financial liabilities	**147,485**	**215,193**	**258,953**	**249,027**	**886,512**	**321,636**	**2,078,806**
Financial guarantees	**-**	**-**	**3,880**	**6,999**	**14,439**	**5,585**	**30,903**
Loan commitments	**33,896**	**-**	**32,914**	**35,437**	**17,671**	**4,189**	**124,107**

Balance sheet items as per mismatch of terms at 31 December 2009

EUR '000

	Sight	Up to 30 days	From 31 up to 90 days	From 91 days up to 1 year	From 1 up to 5 years	Over 5 years	Total
Financial assets	**244,985**	**76,596**	**204,025**	**641,239**	**763,013**	**490,576**	**2,420,434**
Financial liabilities							
Financial liabilities to Central Bank	–	–	–	80,407	–	–	80,407
Financial liabilities held for trading	2,863	–	–	–	–	–	2,863
Financial liabilities measured at amortized cost	171,998	159,249	166,314	518,916	909,222	122,904	2,048,603
Other financial liabilities	–	2,979	–	149	–	–	3,128
Total financial liabilities	**174,861**	**162,228**	**166,314**	**599,472**	**909,222**	**122,904**	**2,135,001**
Financial guarantees	**–**	**444**	**8,591**	**15,811**	**3,489**	**200**	**28,535**
Loan commitments	**–**	**67,765**	**17,184**	**68,735**	**–**	**–**	**153,684**

The Bank calculates the liquidity ratios on a daily basis in accordance with the Decision of the Bank of Slovenia on minimum requirements for ensuring an adequate liquidity position of banks and savings banks.
The ratios are calculated as ratio of investments to liabilities following the principle of residual maturity. The first class liquidity ratio (maturity from 0 up to 30 days) cannot be lower than 1.

The joint liquidity ratios as per 31 December 2010 are as follows:

First class investments/assets (0–30 days)	1.15
Second class investments/assets (0–180 days)	0.86

The joint liquidity ratios as per 31 December 2009 are as follows:

First class investments/assets (0–30 days)	1.15
Second class investments/assets (0–180 days)	1.31

Market Risk

Market risk represents a potential loss that occurs due to changed market conditions in respect of the Bank's exposure to individual market parameters or risk factors (currency exchange rates, interest rates, share quotations, credit spreads).

Managing market risks in a bank is a procedure that comprises identification, measuring and monitoring of individual market risks designed to minimize the potential negative financial consequences. The set of rules, methodologies and responsibilities in respect of market risk management is written in the Framework Risk Policy and the Framework Manual for Risk Management.

The Bank is exposed to different market risks through its daily operations, amongst other to position risk, currency risk and interest risk; considering the scale of risk it manages them through periodical reporting on utilization of limits and achieved operations' results.

Market risks limits are determined pursuant to the annual plan and the appetite for assuming market risks; the competent departments of the parent bank and of the Bank work in close cooperation to determine these limits at least once a year. The procedure of confirmation of limits is formally concluded with acceptance of the suggested limits by the parent bank's management and the Management of the Bank.

a) Trading book

The Bank's trading book serves primarily for ensuring services to clients. The Bank offers its clients a possibility of concluding implemented derivatives, which, in line with confirmed limits for market risk, it closes immediately and thus minimizes market risks. By doing this, the Bank exposes itself to counter-party credit risk, which is mitigated with the amount of limit for credit exposure to each individual client, while it is measured and reported in accordance with the standardized approach. The Bank conducts foreign currency purchase/sale transactions in order to serve its clients and to balance its overall foreign currency position. Equity securities are mainly forward sold, while a minor net position is represented only by the Hypo funds. The Bank maintains the latter in the trading book for the purpose of selling them to clients.

For measuring position risk in the trading book, the Bank uses the value at risk (VaR) method. This method gives information with a specific level of probability (which is defined with a confidence interval) that maximum expected loss within a defined time horizon (a period of holding a position) shall not exceed the calculated amount. As a system support for calculation of risk value, the Bank uses the PMS system (Portfolio Risk and Management System), for whose development and improvement is responsible the department of Information technology and Market Risk Controlling of the parent bank. In order to determine the risk parameters, the Bank uses its own, exponentially weighted history of 250 days. The used methodology for calculation of value at risk is the Monte Carlo method with 10,000 simulations and a 99 per cent interval of trust (1-day position holding).

Movement of VaR value for HBS for 2010 — EUR

	Maximum	Minimum	Average
Equity securities	762	196	411
Derivatives	616	329	445

Movement of VaR value for HBS for 2009 — EUR

	Maximum	Minimum	Average
Equity securities	10,914	311	1.568
Derivatives	1,688	144	350

Besides the value at risk limits, the entire system of position risks is supplemented by volume limits, limits of the maximum permitted loss and sensitivity limits, among which are, for example, the minimum rating of the securities issuer, allowed forms of products, allowed markets for trading, and which ensure that the positions are in line with the outlined business strategy.

b) Interest rate risk in the banking book

Interest rate risk represents the risk of loss, which derives from the interest sensitive assets, which have different maturities or different dynamics of variable interest rate changing, than appropriate resources for financing these assets.

Management of the interest rate risk, which results from the trading book items, is already included in the management of positioning risk of the trading book. For the purpose of management of interest rate risk, which results from the items of the banking book and off-balance sheet items, the Bank uses methodology of interest rate gaps with respect to the date of the next change of interest rate.

The result of monthly measuring of the Bank's exposure to interest rate risk is the net present value of differences between assets and liabilities, which are subject to market interest rate change in the given time period. With respect to the Basel II guidelines, the Bank regularly checks the influence of interest rate shock in the amount of 200 basis points and internally tightens a 20 percent absorption effect of net equity of the Bank at the prescribed interest rate shock. Besides the described interest rate shock with the parallel shift of the yield curve, the Bank measures also the effect of other interest rate shocks on a monthly basis.

The interest rate shock in the amount of 200 basis points would absorb approximately 5.95 per cent of the Bank's equity at the end of 2010 (2009: 6.57 per cent).

Effect of yield curve shift by different scenarios (excluding non-interest bearing items at 31 December 2010)

EUR '000

	Effect of yield curve shift
+ 10 bps parallel shift	-774
– 10 bps parallel shift	774
+ 1 bp parallel shift	-77
– 1 bp parallel shift	77
Rotation (ON-3M -> +60BP, 3M-5Y -> -20 BP, 5Y -> -50 BP)	698
Rotation (ON-3M -> -60BP, 3M-5Y -> +20 BP, 5Y -> +50 BP)	-772

Effect of yield curve shift by different scenarios (excluding non-interest bearing items at 31 December 2009)

EUR '000

	Effect of yield curve shift
+ 10 bps parallel shift	-959
– 10 bps parallel shift	959
+ 1 bp parallel shift	-96
– 1 bp parallel shift	96
Rotation (ON-3M -> +60BP, 3M-5Y -> -20 BP, 5Y -> -50 BP)	4,282
Rotation (ON-3M -> -60BP, 3M-5Y -> +20 BP, 5Y -> +50 BP)	-4,372

c) Currency risk

Currency risk is a risk of a loss arising from mismatch of the currency sub-balance and inconsistencies of foreign currencies.

The Bank monitors on a daily basis exposure to foreign currency risks and limits them by setting volume limits by individual currencies, groups of currencies and total open position. The measurement method is based on the principle of net open position, which is reported in domestic currency. Group of volume limits is rounded up by the VaR limit on total open position. VaR methodology is the same as the methodology in the trading book (250-day history – ECB fixed rate, exponentially weighted daily changes of exchange rate, 99-per cent confidence interval and 1-day holding period).

Narrow volume limits by individual currencies, groups of currencies and total open position indicate a conservative approach to managing currency risks. According to the regulatory capital requirement for currency risk, the Bank does not have to calculate a capital requirement for currency risk, as its total position in foreign currencies does not exceed 2 per cent of its capital.

Movement of VaR value for total open FX position for 2010

EUR

	Maximum	Minimum	Average
VaR-correlated	40,067	1,002	6,595

Movement of VaR value for total open FX position for 2009

EUR

	Maximum	Minimum	Average
VaR-correlated	48,738	2,394	17,832

Exposure to currency risk on 31 December 2010

EUR '000

	USD	CHF	GBP	Other currencies	Domestic currency	Total
Financial assets						
Cash on hand and balances with Central Bank	179	381	46	96	54,805	55,507
Financial assets held for trading	–	22	–	–	24,070	24,092
Available-for-sale financial assets	–	–	–	–	91,280	91,280
Loans	5,155	373,695	808	185	1,574,909	1,954,752
Financial assets held to maturity	–	–	–	–	42,315	42,315
Other financial assets	–	–	–	–	783	783
Total financial assets	**5,334**	**374,098**	**854**	**281**	**1,788,162**	**2,168,729**
Financial liabilities						
Financial liabilities to Central Bank	–	–	–	–	40,010	40,010
Financial liabilities held for trading	–	21	–	–	2,429	2,450
Financial liabilities measured at amortized cost	5,890	370,168	761	63	1,588,587	1,965,469
Other financial liabilities	–	2	–	–	3,870	3,872
Total financial liabilities	**5,890**	**370,191**	**761**	**63**	**1,634,896**	**2,011,801**

Exposure to currency risk on 31 December 2009

EUR '000

	USD	CHF	GBP	Other currencies	Domestic currency	Total
Financial assets						
Cash on hand and balances with Central Bank	150	166	56	117	112,633	113,122
Financial assets held for trading	–	20	–	–	38,042	38,062
Available-for-sale financial assets	–	–	–	–	91,470	91,470
Loans	3,935	380,936	514	731	1,644,896	2,031,012
Financial assets held to maturity	–	–	–	–	42,112	42,112
Other financial assets	–	–	–	–	1,285	1,285
Total financial assets	**4,085**	**381,122**	**570**	**848**	**1,930,438**	**2,317,063**
Financial liabilities						
Financial liabilities to Central Bank	–	–	–	–	80,276	80,276
Financial liabilities held for trading	–	18	–	–	2,845	2,863
Financial liabilities measured at amortized cost	4,388	441,418	535	512	1,597,224	2,044,077
Other financial liabilities	12	2	–	–	3,114	3,128
Total financial liabilities	**4,400**	**441,438**	**535**	**512**	**1,683,459**	**2,130,344**

Net open balance sheet position in CHF is closed with a forward leg of FX swap.

Fair Values of Assets and Liabilities

a) Financial instruments not measured at fair value

The table below summarizes the carrying amounts and fair values of those financial assets and financial liabilities that are not reported in the Bank's statement of financial position at fair values.

EUR '000

	2010		2009	
	Carrying amount	Fair value	Carrying amount	Fair value
Financial assets				
1. Cash and balances with Central Bank	55,507	55,507	113,122	113,122
2. Loans to banks	14,191	14,191	46,929	46,929
3. Loans to clients	1,940,561	1,929,810	1,984,083	1,993,814
4. Financial assets held to maturity	42,315	42,594	42,112	41,732
5. Other financial assets	783	783	1,285	1,285
Financial liabilities				
1. Financial liabilities to Central Bank	40,010	40,010	80,276	80,276
2. Financial liabilities to banks measured at amortized cost	1,440,334	1,440,334	1,565,036	1,565,957
3. Financial liabilities to non-banks measured at amortized cost	525,135	524,958	479,041	479,085
4. Other financial liabilities	3,872	3,872	3,128	3,128

- Financial assets held to maturity: the fair value is based on the quoted market price;
- Loans (to banks and clients): for short-term assets, the fair value is not calculated as it is assumed that the carrying amount represents a reasonable approximation of the fair value; carrying amount of assets at variable interest also represents reasonable approximation of the fair value if the repricing dates are no longer than 12 months; for long-term assets at fixed interest, the fair value is calculated (zero coupon yield is used for discounting the future cash flows).
- Liabilities measured at amortized cost: the assessed fair value is based on discounted contractual values, using the market interest rates that should be currently paid by the Bank for replacement of these liabilities by new debts with similar residual maturity.
- For short-term receivables and liabilities it is expected (according to the standard) that the carrying amount is a reasonable approximation of the fair value.

b) Fair value hierarchy

IFRS 7 specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources; unobservable inputs reflect market assumptions made by the Bank. The two types of inputs have resulted in the following fair value hierarchy:

- Level 1 – quoted prices (unadjusted) in active markets for identical assets or liabilities. This level includes listed equity securities on stock exchanges (for example London Stock Exchange, Frankfurt Stock Exchange, New York Stock Exchange) and traded derivatives such as futures (for example Nasdaq, S&P 500).
- Level 2 – Inputs other than quoted prices included within Level 1; these observable inputs relate to assets and liabilities either directly (as prices) or indirectly (as derived from prices). Level 2 includes the majority of the OTC derivative contracts, traded loans and issued structured bonds. The sources of input parameters such as yield curves or the relevant increases for credit risk are Bloomberg and Reuters.
- Level 3 – Inputs for the assets and liabilities that are not based on observable market data (unobservable inputs). This level includes equity investments and debt instruments with significant unobservable components.

This hierarchy required the use of observable market data when they are available. The Bank considers significant and observable market prices in its valuations whenever possible.

There were no transfers between Level 1 and Level 2 of the fair value hierarchy.

c) Financial instruments measured at fair value

The fair value of financial instruments not traded in an active market is based on values obtained from an external expert. The Bank verifies the values and if confirmed, the assessed values are taken into account. Values of investments presented in Level 3 are obtained using standard valuation techniques such as discounted expected future cash flows, mark to market (comparative entities listed on the stock exchange – direct comparison with entities quoted in an organized market) and liquidation value approach. Final estimated value of financial instruments considers all approaches, taking into consideration different assessments of importance in respect of activity, financial stability of an entity as well as other factors that could impact the fair value of financial instruments.

The effect of changes in key assumptions would not have a significant impact on the financial statements.

EUR '000

31. December 2010	Level 1	Level 2	Level 3	Total
Financial assets				
1. Financial assets held for trading	6,136	8,079	9,877	24,092
2. Available-for-sale financial assets	80,356	9,292	1,632	91,280
Financial liabilities				
1. Financial liabilities held for trading	2,450	-	-	2,450

EUR '000

31. December 2009	Level 1	Level 2	Level 3	Total
Financial assets				
1. Financial assets held for trading	22,774	4,274	11,014	38,062
2. Available-for-sale financial assets	79,139	-	12,331	91,470
Financial liabilities				
1. Financial liabilities held for trading	-	2,863	-	2,863

d) Analysis of changes in fair values (Level 3)

Financial year 2010

EUR '000

	Opening balance	Total gains / (losses for the period recognized in profit or loss	Changes in valuations	Purchases	Sales	Closing balance
Financial assets held for trading						
Shares and other non fixed-interest securities	11,014	-	3,484	20,203	24,824	9,877
Total financial assets held for trading	**11,014**	**-**	**3,484**	**20,203**	**24,824**	**9,877**
Available-for-sale financial assets						
Shares and other non fixed-interest securities	2,408	-	(776)	-	-	1,632
Bonds and other fixed-interest securities	9,923	-	(9,923)	-	-	-
Total available-for-sale financial assets	**12,331**	**-**	**(10,699)**	**-**	**-**	**1,632**

Financial year 2009

EUR '000

	Opening balance	Total gains / (losses for the period recognized in profit or loss	Changes in valuations	Purchases	Sales	Closing balance
Financial assets held for trading						
Shares and other non fixed-interest securities	12,801	-	-	26,709	(28,496)	11,014
Total financial assets held for trading	**12,801**	**-**	**-**	**26,709**	**(28,496)**	**11,014**
Available-for-sale financial assets						
Shares and other non fixed-interest securities	2,600	-	(192)	-	-	2,408
Bonds and other fixed-interest securities	9,875	48	-	-	-	9,923
Total available-for-sale financial assets	**12,475**	**48**	**(192)**	**-**	**-**	**12,331**

Capital Risk

The Bank is required to have adequate capital at any time, as a provision for different risks to which it is exposed in the course of its operations. This is an ongoing process of determining and maintaining a sufficient volume and quality of capital, taking into consideration the assumed risks, which is defined in the Bank's capital management policy.

Regulatory capital adequacy is the ratio between own funds and risk-weighted assets that has to be at least 8 per cent.

The table below shows the calculation of regulatory capital and the capital adequacy ratio

Item	31.12.2010	31.12.2009
Subscribed paid-up capital	174,037	174,037
Capital surplus	2,696	2,696
Reserves and retained earnings or accumulated loss	(11,883)	11,974
- Intangible assets	(4,216)	(3,668)
- Unrecorded impairments and provisions due to recording lag	(307)	(179)
CAPITAL I	**160,327**	**184,860**
Subordinated debt	**73,000**	**73,000**
Adjustment of revaluation reserve associated with available-for-sale financial assets – equity instruments	1,850	2.758
CAPITAL II	**74.850**	**75.758**
TOTAL CAPITAL (for the capital adequacy purposes)	235,177	260,618
Capital requirement for credit risk, counter party risk and settlement risk	158,318	165,464
Capital requirement for settlement risk	3,109	-
Capital requirement for position risk and currency risk	406	975
Capital requirement for operational risk	7,276	5,645
Capital requirement for exceeding the exposure from the trading activities	-	-
TOTAL CAPITAL REQUIREMENTS	**169,109**	**172,084**
CAPITAL ADEQUACY RATIO (per cent)	**11.13**	**12.11**

The Bank's capital is calculated as the sum of share capital and supplementary capital, whereby the share capital consists of: subscribed share capital, capital surplus, reserves and retained earnings, loss of the period and revaluation reserve; supplementary capital is composed of: subordinated debt and adjustments of revaluation reserve in association with available-for-sale financial assets.

In 2010, the Bank fully complied with the legal requirements regarding capital. As at the end of year 2010, the Bank's capital amounted to EUR 235,177 thousand, tier 1 or core capital amounted to EUR 160,327 thousand, the capital surplus amounted to EUR 66,068 thousand, while the capital adequacy ratio was 11.13 per cent.

In 2010, the Bank calculated capital requirements for:

- Credit risk in accordance with the Decision on the Calculation of Capital Requirement for Credit Risk according to a standardized approach for banks and savings banks,
- Market risk in accordance with the Decision on the Calculation of Capital Requirement for Market Risks for banks and savings banks, whereby it does not use internal models;
- Operational risk in accordance with the Decision on the Calculation of Capital Requirement for Operational Risk for banks and savings banks, whereby it uses a simple approach.

The amount of an individual capital requirement is evident from the calculation of regulatory capital and capital adequacy ratio.

In accordance with the Internal Capital Adequacy Assessment Process (ICAAP) of the Bank, the capital adequacy ratio was 8.44 per cent as at 31 December 2010.

Operational Risk

The Bank includes in the definition of operational risk also legislative risk and model risk, as well as the reputation risk. Business and strategic risks are not included in the operational risk as they are addressed separately.

To calculate the capital requirement for operational risk, the Bank continues to use a simple approach. However, this year it adopted the operational risk management strategy in which it intends to calculate the capital requirement according to standardized approach in the future.

As the Bank is aware of the importance of operational risk management, it decided that in addition to satisfying legally prescribed general standards for risk management, it will perform activities that are carried out in more advanced approaches in accordance with the decision on risk management.

Assessment and measurement of operational risk is based on the collection of damage events that are registered in the central database of damage events. This allows for a more efficient reporting of occurred damage events, their causes and proposed measures.

All damage events which present an actual direct or indirect financial loss for the Bank, are registered, regardless of whether financial damages occurred during the event or subsequently. Registered are also events which could present potential loss for the Bank.

In 2010, the Bank recorded 44 damage events. The Bank defined as damage event any event whose gross loss exceeds EUR 50. At the end of the year, the balance of gross losses that are not connected with impairments or provisions resulting from credit risk, amounted to EUR 361 thousand.

Preventive assessment of potential operational risk is performed with the procedure of detecting risk scenarios and with methods of self-assessment of critical operational risk factors, whose risk profile is assessed annually with renewed assessment of business effects as part of the regular process of business continuity planning.

The Bank measures and monitors individual risk indicators on the basis of which, in the event of unacceptable deviations, it plans control activities.

Based on perceived and assessed operational risk and damage that occurred, for significant risk, the Bank plans and carries out activities to prevent, mitigate, transfer or accept the risk.

As part of the development of applicative support, the Bank upgraded the application for managing operational risk in accordance with the renewed management policy.

The Bank reports regularly on quarterly basis to the ICCO committee about all important perceived risks, risk indicators, and damage events, as well as about the status of implementation of risk control measures. In case of significant losses or exposures, the Management Board and upper management are notified immediately.

In 2010, the Bank continued to regularly upgrade the policy of the Group information protection, and at the same time continued its operational processes of information protection and processes of business continuity for the Bank's most critical functions. Furthermore, the Bank carried out functional tests of critical business functions and verified the accuracy of existing business continuity plans.

As part of the ICAAP process, the Bank believes that in terms of the risk profile, the highest risk is presented by incorrect and inappropriate actions of employees. This risk is managed by procedures described in the section Responsibility towards employees.

5 Useful Information

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