# KREDITNA BANKA ZAGREB d.d.

## Financial statements as at 31 December 2009 together with the Independent Auditor's Report

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**Responsibility for the financial statements**

Pursuant to the Croatian Accounting Law (Official Gazette 109/07), the Board is responsible for ensuring that financial statements are prepared for each financial year in accordance with International Financial Reporting Standards (IFRS) as published by the International Accounting Standards Board (IASB) and statutory accounting regulations applicable to banks in Croatia, which give a true and fair view of the financial position and results of the Bank for that period.

The Board has a reasonable expectation that the Bank has adequate resources to continue in operational existence for the foreseeable future. For this reason, the Board continues to adopt the going concern basis in preparing the financial statements.

In preparing those financial statements, the responsibilities of the Board include ensuring that:

- appropriate accounting policies are selected and then applied consistently;
- judgments and estimates are reasonable and prudent;
- applicable accounting standards are followed, subject to any material departures disclosed and explained in the financial statements; and
- financial statements are prepared on the going concern basis unless it is inappropriate to presume that the Bank will continue in business.

The Board is responsible for keeping proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Bank and must also ensure that the financial statements comply with the Croatian Accounting Law (Official Gazette 109/07). The Board is also responsible for safeguarding the assets of the Bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Signed on behalf of the Management Board

Nelsi Rončević,
President of the Management Board

Ivan Dropulić,
Vice president of the Management Board

KREDITNA BANKA ZAGREB d.d.

**Kreditna banka Zagreb d.d.**
Ulica grada Vukovara 74
10000 Zagreb
Republic of Croatia

16 April 2010

**Independent Auditor's Report**

*To the Management Board and Shareholders of Kreditna banka d.d.*

We have audited the accompanying financial statements of Kreditna banka d.d. (herein below the Bank), which comprise of the balance sheet as at 31 December 2009, the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes as presented on pages 4 to 57.

*Management's Responsibility for the financial statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting regulations applicable to banks in Croatia. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

*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 Bank'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 Bank'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.

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*Opinion*

In our opinion, the financial statements presented on pages 4 to 57 give a true and fair view of the financial positions of the Bank as at 31 December 2009 and the results of its operations, changes in equity and cash flows for the year then ended in accordance with statutory accounting regulations applicable to banks in Croatia.

Nexia revizija d.o.o.
Koranska 16, Zagreb

Zagreb, 16 April 2010

NEXIA REVIZIJA d.o.o.
ZAGREB

Siniša Dušić
Certified auditor

Income statement
For the year ended 31 December 2009
(All amounts are expressed in thousands of kunas)

| | Note | 2009 | 2008 |
|---|---|---|---|
| Interest and similar income | 4 | 111,187 | 90,831 |
| Interest and similar expense | 5 | (59,261) | (47,119) |
| **Net interest income** | | **51,926** | **43,712** |
| Fee and commission income | 6 | 24,601 | 25,101 |
| Fee and commission expense | 6 | (12,277) | (10,918) |
| **Net fee and commission income** | | **12,324** | **14,183** |
| Net foreign exchange gains | 7 | 15,135 | 6,868 |
| Dividend income | | 13 | 14 |
| Net gain / (loss) from valuation of securities | | 1,044 | (1,332) |
| Other operating income | | 1,193 | 3,455 |
| **Operating income** | | **81,635** | **66,900** |
| Operating expenses | 8 | (61,408) | (53,392) |
| Impairment losses and provisions | 9 | (4,564) | 1,598 |
| **Profit before tax** | | **15,663** | **15,106** |
| Income tax expense | 10 | 3,476 | 3,550 |
| **Net profit for the year** | | **12,187** | **11,556** |

The financial statements as shown on pages 4 to 57 were approved and signed by the Management Board on 16 April 2010.

Management Board:

Nelsi Rončević,
President of the Management Board

Ivan Dropulić,
Vice president of the Management Board

KREDITNA BANKA ZAGREB d.d.

Balance sheet

As at 31 December 2009

(All amounts are expressed in thousands of kunas)

| | Note | 31.12.2009 | 31.12.2008 |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and balances with Croatian National Bank | 11 | 203,038 | 207,837 |
| Placements with other banks | 12 | 185,771 | 281,728 |
| Assets at fair value through profit or loss | 13 | 2,580 | 15,652 |
| Loans to customers | 14 | 1,074,437 | 843,781 |
| Investments held to maturity | 15 | 4,604 | 1,494 |
| Investments available for sale | 16 | 78,969 | 41,109 |
| Intangible assets | 17 | 12,634 | 8,199 |
| Tangible assets | 18 | 33,281 | 34,476 |
| Other assets | 19 | 51,691 | 51,463 |
| **Total assets** | | **1,647,005** | **1,485,739** |
| **LIABILITIES** | | | |
| Deposits from banks | | 5 | 8 |
| Deposits from customers | 20 | 1,144,895 | 1,197,602 |
| Borrowings | 21 | 193,514 | 90,088 |
| Other liabilities | 22 | 31,015 | 25,624 |
| Provisions for contingent liabilities | 26 | 1,522 | 1,902 |
| **Total liabilities** | | **1,370,951** | **1,315,224** |
| **SHAREHOLDERS' EQUITY** | | | |
| Share capital | 23 | 186,554 | 131,995 |
| Share premium | 23 | 44,763 | 1,116 |
| Unrealized (loss) / gain from assets available for sale | | 1,406 | (829) |
| Retained earnings and reserves | 24 | 31,144 | 26,677 |
| Profit for the year | | 12,187 | 11,556 |
| **Total shareholders' equity** | | **276,054** | **170,515** |
| **Total shareholders' equity and liabilities** | | **1,647,005** | **1,485,739** |

The financial statements as shown on pages 4 to 57 were approved and signed by the Management Board on 16 April 2010.

Management Board:

Nelsi Rončević,
President of the Management Board

KREDITNA BANKA ZAGREB d.d.

Ivan Dropulić,
Vice president of the Management Board

Statement of changes in equity

For the year ended 31 December 2009

(All amounts are expressed in thousands of kunas)

| | Note | Share capital | Share premium | Unrealized (loss) / gain from assets available for sale | Retained earnings and reserves | Profit for the year | Total |
|---|---|---|---|---|---|---|---|
| **Balance as at 1 January 2007** | | 131,995 | 1,116 | 108 | 22,384 | 11,290 | 166,893 |
| Profit for the year | | - | - | - | - | 11,556 | 11,556 |
| Gain / (loss) on assets available for sale | | - | - | (937) | - | - | (937) |
| *Total recognized income in 2008* | | - | - | *(937)* | - | *11,556* | *10,619* |
| Transfer to reserves | | - | - | - | 564 | (564) | - |
| Dividend for 2007 | | - | - | - | - | (6,997) | (6,997) |
| Transfer of profit to retained earnings | | - | - | - | 3,729 | (3,729) | - |
| **Balance as at 31 December 2008** | **23** | **131,995** | **1,116** | **(829)** | **26,677** | **11,556** | **170,515** |
| Profit for the year | | - | - | - | - | 12,187 | 12,187 |
| Gain / (loss) on assets available for sale | | - | - | 2,235 | - | - | 2,235 |
| *Total recognized income in 2009* | | - | - | *2,235* | - | *12,187* | *14,422* |
| Capital contribution | **23** | 54,559 | 43,647 | - | - | - | 98,206 |
| Transfer to reserves | **24** | - | - | - | 578 | (578) | - |
| Dividend for 2008 | **23** | - | - | - | - | (7,089) | (7,089) |
| Transfer of profit to retained earnings | **24** | - | - | - | 3,889 | (3,889) | - |
| **Balance as at 31 December 2009** | **23** | **186,554** | **44,763** | **1,406** | **31,144** | **12,187** | **276,054** |

| | Note | 2009 | 2008 |
|---|---|---|---|
| **Net cash flow from operating activities** | | | |
| Profit before tax | | 15,663 | 15,106 |
| Depreciation | | 2,777 | 3,227 |
| Increase / (decrease) in allowance for other assets | | 139 | (386) |
| Increase / (decrease) in allowance for loans | | 4,806 | (1,527) |
| Net gain / (loss) on fair value adjustments of assets available for sale | | 2,235 | (937) |
| (Decrease) / increase in contingent liabilities | | (381) | 315 |
| **Total items not affecting cash** | | **25,239** | **15,798** |
| Decrease / (increase) in receivables from Croatian National Bank and other banks | | 49,226 | (1,562) |
| Decrease in loans and advances to customers | | (235,462) | (79,318) |
| Increase in deposits from other banks | | (3) | - |
| (Decrease) / increase in deposits from customers | | (52,707) | 196,166 |
| Increase in other assets | | (3,975) | (20,618) |
| Increase / (decrease) in other liabilities | | 5,328 | (8,030) |
| Income tax paid | | 195 | (8,089) |
| **Net cash flow (used in) / generated from operating activities** | | **(212,159)** | **94,347** |
| **Cash flow from investing activities** | | | |
| Purchases of tangible and intangible assets | | (6,016) | (1,086) |
| Purchase of assets available for sale | | (37,860) | (32,718) |
| Proceeds from sale of assets at fair value through profit or loss | | 13,072 | 1,605 |
| Decrease of assets held to maturity | | (3,110) | (1,101) |
| **Net cash flow from investing activities** | | **(33,914)** | **(33,300)** |
| **Cash flow from financing activities** | | | |
| Proceeds from borrowings | | 11,666,273 | 8,188,115 |
| Repayments of borrowings | | (11,562,847) | (8,209,372) |
| Capital contribution | | 54,559 | - |
| Share premium from capital contribution | | 43,647 | - |
| Dividend paid | | (7,089) | (6,997) |
| **Net cash flow from / (used in) financing activities** | | **194,543** | **(28,254)** |
| **Net (decrease)/increase in cash and cash equivalents** | | **(51,530)** | **32,793** |
| Cash and cash equivalents at the beginning of the year | *28* | 327,623 | 294,830 |
| **Cash and cash equivalents at the end of the year** | *28* | **276,093** | **327,623** |

## 1. General information

Kreditna banka Zagreb d.d. ("the Bank") is incorporated as a joint stock company in accordance with applicable laws of the Republic of Croatia. It was registered at the Commercial Court in Zagreb in 1994. The Bank's headquarters is in Zagreb, Ulica grada Vukovara 74.

The principal activities of the Bank include all types of corporate and retail deposit and lending operations, domestic and foreign payment transactions, issuance of guarantees, bills of exchange and other forms of guarantees, securities trading and other banking services. The Bank operates only in banking sector and on the Croatian market.

The Bank performs insurance agency business in accordance with the insurance laws, in the part that relates to the bank insurance, based on the license dated 14 February 2007.

**Management Board**

| | |
|---|---|
| Nelsi Rončević | President of the Management Board |
| Ivan Dropulić | Vice president of the Management Board |

**Supervisory Board**

| | |
|---|---|
| Mirjana Krile | President of the Supervisory Board |
| Ankica Čeko | Vice president of the Supervisory Board |
| Nadira Eror | Member of the Supervisory Board |
| Gordana Letica | Member of the Supervisory Board |
| Irena Severin | Member of the Supervisory Board |

**2. Basis of preparation of the financial statements**

The principal accounting policies applied in preparation of these financial statements are summarized below. Where specific accounting policies are aligned with accounting principles set out in International Financial Reporting Standards ("IFRS"), reference may be made to certain Standards in describing the accounting policies of the Bank. Unless otherwise stated, these references are to Standards applicable as at 31 December 2009.

**2.1. Compliance of statutory requirements for accounting of banks in Croatia and IFRS**

The financial statements have been prepared in accordance with statutory accounting requirements for banks in Croatia. The Banks operations in Croatia are subjected to the Law on credit institutions, in accordance with which the Bank's financial reporting is regulated by the Croatian National Bank ("the CNB") which is the central monitoring institution of the banking system in Croatia. These financial statements have been prepared in accordance with these banking regulations.

The main difference between the requirements of the International Financial Reporting Standards („IFRS") and the accounting regulations of the CNB relates to the recognition of the impairment losses of financial assets calculated on the portfolio basis. In accordance with the regulations of the CNB, banks with registered seat in Croatia should recognize impairment on the portfolio basis by the prescribed rates from 0.85% to 1.20% on the balance sheet and off-balance sheet exposure exposed to credit risk of the debtors for which impairment on individual basis is not determined, while IFRS requires that the provision on portfolio basis should be determined for existing, but unidentified losses on the basis of valuation models taking into account individual characteristics of the Bank and debtors in the portfolio (i.e. collaterals, type and rating of a debtor and similar).

Additionally, the CNB prescribes minimal levels of impairment losses against certain specifically identified impaired exposures, which may be different from the impairment loss required to be recognized in accordance with IFRS.

**2.2. Basis of preparation**

The financial statements are presented in thousands of kunas („HRK"), unless otherwise stated.

The financial statements have been prepared on the accrual basis, as well as under going concern assumption.

## 3. Summary of significant accounting policies

### 3.1 Interest and similar income and expenses

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

Loan origination fees for loans which are probable of being drawn down are deferred (together with related direct costs) and recognized as an adjustment to the effective yield of the loan and as such adjust the interest income.

When loans become impaired, they are written down to their recoverable amounts and interest income thereafter recognized based on the rate of interest that was used to discount the future cash flows for the purpose of measuring the recoverable amount. Other fees receivable are recognized when earned. Dividend income is recognized when decision of General Assembly is made.

### 3.2 Fee and commission income

Fee and commission income is comprised mainly of fees receivable from enterprises for loans and guarantees granted and other services provided by the Bank, together with commissions from managing funds on behalf of legal entities and individuals and fees for foreign and domestic payment transactions.

Fees and commissions are recognized on an accrual basis. Loan origination fees for loans which are likely of being drawn down, are deferred and recognized as an adjustment to the effective yield on the loan.

### 3.3 Operating income

Operating income includes net interest income, net fee and commission income, foreign exchange trading gains, realized gains on securities classified as assets available for sale, foreign exchange revaluation, gains from disposal of fixed assets, dividends received and other income.

### 3.4 Foreign currencies

Income and expenditure arising from transactions in foreign currencies are translated to HRK at the official rates of exchange on the transaction date. Assets and liabilities denominated in foreign currencies are translated to HRK at the mid market exchange rate of the CNB on the last day of the accounting period. Gains and losses resulting from the foreign currency translation are included in the income statement for the year.

The Bank has receivables and liabilities originated in HRK, which are linked to foreign currencies with one-way currency clause. Due to this clause the Bank has an option to revalue the asset by the higher of: foreign exchange rate valid as of the due date or foreign exchange rate valid as of the date of origination of the financial instrument. In case of the liability linked to this clause, the counterparty has this option. Due to the specific conditions of the market in Republic of Croatia the fair value of this option can not be calculated as the forward rates for HRK for periods over 6 months are generally not available.

**3. Summary of significant accounting policies (continued)**

**3.4 Foreign currencies (continued)**

As such the Bank revalue its receivables and liabilities linked to this clause by the agreed reference rate valid at the date of the balance sheet or foreign exchange rate agreed by the option (rate valid at origination), whichever is higher.

**3.5 Personnel social contributions**

According to the local legislation the Bank is obliged to pay contributions to the Pension Funds and the State Health Fund. This obligation relates to all employees and provides for paying contributions in the amount of certain percentages determined on the basis of the gross salary as follows:

| | **2009** | **2008** |
|---|---|---|
| Contributions for Pension Fund | 20% | 20% |
| Contributions for State Health Fund | 15% | 15% |
| Contributions for Unemployment Fund | 1.7% | 1.7% |
| Occupational injury | 0.5% | 0.5% |

The contributions on behalf of employees and on behalf of employer are charged to expenses in the period in which they are incurred.

**3.6 Income tax**

Income tax expense represents the sum of the tax currently payable and deferred tax. Current tax expense is based on taxable income for the year. Taxable income differs from net income as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Bank's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date. Deferred tax is the tax expected to be payable or recoverable based on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, calculated using the liability method. Deferred tax liabilities are generally recognized for all taxable temporary differences and deferred tax assets are recognized to the extent that it is probable that future taxable profit will be available on the possible use of deductible temporary differences.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is not likely to be available a sufficient amount of taxable income for the refund of all or part of the asset.

Deferred tax assets and liabilities are offset when they relate to income taxes charged by the same taxation authority and the Bank intends to settle its current tax assets and liabilities on a net basis.

The Bank is subject to various indirect taxes which are included in administrative expenses.

**3. Summary of significant accounting policies (continued)**

**3.6 Income tax (continued)**

Deferred tax is calculated at the tax rates that are expected to be applicable in the period in which the liability will be settled or the asset realized. Deferred tax is charged or credited to the income statement, except when it relates to items recorded directly in equity, when the deferred tax is also dealt with in equity.

**3.7 Cash and cash equivalents**

For the purposes of reporting cash flows, cash and cash equivalents include cash, balances with the CNB, balances per gyro accounts and term deposits with banks with maturity of less than 90 days.

Cash and cash equivalents excludes the statutory reserves with the CNB, as the reserve funds are not available to the Bank's day to day operations. Obligatory reserves with the CNB is the amount required by all commercial banks licensed to operate in the Republic of Croatia.

**3.8 Financial assets and liabilities**

The Bank’s financial assets and financial liabilities recorded on the balance sheet include cash and cash equivalents, marketable securities, trade and other accounts receivable and payable, long-term loans, deposits and investments. The accounting principles for these items are disclosed in the respective accounting policies.

The Bank recognizes financial assets and liabilities on its balance sheet when, and only when, it becomes a party to the contractual provisions of the instrument.

Financial assets and liabilities held by the Bank are categorized into portfolios in accordance with the Bank’s intent on the acquisition and pursuant to the Bank’s investment strategy. Financial assets and liabilities are classified as „At fair value through profit or loss“, "Held to maturity", "Assets available for sale" or as "Loans and receivables". The principal difference among the portfolios relates to the measurement of financial assets and the recognition of their fair values in the financial statements as described below.

Financial assets and liabilities are offset and the net amount is reported in the balance sheet when there is a legally enforceable right to set off the recognized amounts and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously.

Regular way transactions with financial instruments are accounted for at the date when they are transferred (settlement date). Under settlement date accounting, while the underlying asset or liability is not recognized until the settlement date, changes in fair value on the underlying asset or liability are recognized starting from trade date.

When a financial asset or financial liability is recognized initially, the Bank measures it at its fair value plus, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

**3. Summary of significant accounting policies (continued)**

**3.8 Financial assets and liabilities (continued)**

*Assets at fair value through profit or loss*

Upon initial recognition designated by the Bank as at fair value through profit or loss in accordance with the Bank's investment policy any financial asset within the scope of IAS 39 can be classified as designated at fair value through profit or loss except for investments in equity instruments that do not have a quoted market price in an active market, and whose fair value cannot be reliably measured.

Measurement:
Subsequent to initial recognition, financial assets at fair value through profit or loss are accounted for and stated at fair value which approximates the price quoted on recognized stock exchanges or acceptable valuation models. The Bank includes unrealized gains and losses in 'Net profit/(loss) on financial operations'. Interest earned on assets at fair value through profit or loss is accrued on a daily basis and reported as 'Interest income' in the profit and loss statement.

*Held to maturity investments*

Investments held to maturity are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Bank has the positive intent and ability to hold to maturity. This portfolio comprises debt securities. Held to maturity investments are carried at amortized cost using the effective interest rate method, less any allowance for impairment.

The Bank assesses on a regular basis whether there is any objective evidence that an investment held to maturity may be impaired. A financial asset is impaired if its carrying amount is greater than its estimated recoverable amount which is equal to the present value of the expected future cash flows discounted at the financial instrument's original effective interest rate. The amount of the impairment loss for assets carried at amortized cost is calculated as the difference between the asset's carrying amount and the present value of the expected future cash flows discounted at the financial instrument's original effective interest rate. When an impairment of assets is identified, the Bank recognizes allowances through the profit and loss statement line 'Allowance for impairment losses on securities'.

*Assets available for sale*

Available-for-sale financial assets are those non-derivative financial assets that are designated as available for sale or are not classified as (a) loans and receivables, (b) held-to-maturity investments or (c) financial assets at fair value through profit or loss.

**3. Summary of significant accounting policies (continued)**

**3.8 Financial assets and liabilities (continued)**

This portfolio comprises equity securities, as well as receivables under factoring and forfeiting arrangements. Subsequent to initial recognition, available-for-sale financial assets are re-measured at fair value based on quoted prices. In circumstances where the quoted market prices are not readily available, the fair value of unquoted equity instruments is estimated using applicable price/earnings or price/cash flow ratios refined to reflect specific circumstances of the issuer. Financial assets are derecognized when the rights to receive cash flows from the financial assets have expired or where the Bank has transferred substantially all risks and rewards of ownership.

For available-for-sale assets, gains and losses arising from changes in fair value are recognized directly in equity under the caption "Reserves and retained earnings", until the security is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognized in equity is included in the profit or loss for the period.

Dividends on securities available for sale are recorded as declared and included as a receivable in the balance sheet line ‘Other assets’.

*Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than (a) those that the Bank intends to sell immediately or in the near term, which shall be classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss; (b) those that the Bank upon initial recognition designates as available for sale; or (c) those for which the Bank may not recover substantially all of its initial investment, other than because of credit deterioration, which shall be classified as available for sale. This portfolio comprises loans provided to customers.

Loans originated by the Bank by providing money directly to the borrower are categorized as loans granted by the Bank and are carried at amortized cost, less any allowance for impairment. Third party expenses, such as legal fees, incurred in securing a loan are treated as part of the cost of the transaction. Loan origination fees for loans which are probable of being drawn down, are deferred (together with related direct costs) and recognized as an adjustment to the effective yield of the loan and as such adjust the interest income. All loans and advances are recognized when loans are issued, or cash is advanced to borrowers.

An allowance for loan impairment is established if there is objective evidence that the Bank will not be able to collect all amounts due. The amount of the allowance is the difference between the carrying amount and the recoverable amount, being the present value of expected cash flows, including amounts recoverable from guarantees and collateral, discounted based on the interest rate at inception.

**3. Summary of significant accounting policies (continued)**

**3.8 Financial assets and liabilities (continued)**

The loan loss allowance also covers losses where there is objective evidence that probable losses are present in components of the loan portfolio at the balance sheet date. These have been estimated based upon historical patterns of losses in each component, the credit ratings allocated to the borrowers and reflecting the current economic climate in which the borrowers operate.

When a loan is uncollectible, it is fully written off. Subsequent recoveries are credited to income from collection of bad and doubtful debts in the income statement.

*Collateral pending sale*

The Bank occasionally acquires real estate in settlement of certain loans and advances. Real estate is stated at the lower of cost of the related loans and advances and the current fair value of such assets. Gains or losses on disposal are recognized in the income statement. Real estate used as collateral for loans given to customers can be sold only by distrait.

*Sale and repurchase agreements*

Securities sold under sale and repurchase agreements (repos) are retained in the financial statements and the counterparty is included in due to banks or customers as appropriate. Securities purchased under agreements to resell (reverse repo) are recorded as due from banks and loans and advances to customers as appropriate. The difference between the sale and repurchase price is treated as interest and accrued over the life of repo agreements.

**3.9 Tangible and intangible assets**

Property and equipment are started at cost less accumulated depreciation and accumulated impairment losses, if any. Cost includes the purchase price and directly associated cost of bringing the asset to a working condition for its intended use. Maintenance and repairs, replacements and improvements of minor importance are expensed as incurred. Items of tangible and intangible assets with a unit value less than HRK 2,000 are expensed when put into use.

Depreciation is computed under the straight-line method over the estimated useful life of the assets according to the following annual rates:

| **Description** | **%** |
|---|---|
| Buildings | 3.03 |
| Computer hardware | 15 |
| Furniture and equipment | 10 |
| Motor vehicles | 20 |
| Computer software | 10 |
| Leasehold improvements | 10 |

**3. Summary of significant accounting policies (continued)**

**3.9 Tangible and intangible assets (continued)**

Land is not depreciated.

The Bank periodically tests its assets for impairment. Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down to its recoverable amount. Gains and losses on disposal of assets are determined by reference to their carrying amount and are recognized in the income statement line 'Other income/(expense)' in the year of disposal. Repairs and maintenance are charged to the income statement when the expenditure is incurred.

**3.10 Foreign currency translation**

The financial statements are presented in Croatian Kuna ("HRK") and rounded to the nearest thousand. The year-end exchange rates were as follows:

| | | |
|---|---|---|
| 31 December 2008 | 1 EUR = 7.324425 HRK | 1 USD = 5.155504 HRK |
| 31 December 2009 | 1 EUR = 7.306199 HRK | 1 USD = 5.089300 HRK |

Transactions in foreign currencies are translated at the foreign exchange rate ruling at the date of the transaction. Monetary assets and monetary liabilities in foreign currencies and linked to foreign currencies are translated at the mid exchange rates of the Croatian National Bank valid on the balance sheet date. Foreign exchange differences arising on translation are recognized in the income statement.

**3.11 Off-balance sheet financial instruments**

In the ordinary course of business, the Bank enters into arrangements and commitments, comprising primarily guarantees, letters of credit and undrawn loan commitments. Such financial instruments are reported on the Bank's balance sheet if and when they become payable.

**3.12 Provisions**

Provisions are recognized when the Bank has a present obligation as a result of a past event, and it is probable that an outflow of resources will be required to settle the obligation, and the amount of the obligation can be measured reliably.

**3.13 Derivative financial instruments**

As at 31 December 2009 and 31 December 2008, the Bank had not purchased any derivative financial instruments. The Bank has assets and liabilities originated in HRK, which are linked to foreign currency with a one-way currency clause. Due to this clause the Bank has an option to revalue the asset by the greater of: foreign exchange rate valid as of the date of maturity, or foreign exchange rate valid as of the date of origination of the financial instrument. Due to the special circumstances of the market in Republic of Croatia the fair value of this option cannot be calculated as the forward rates for HRK for periods over 6 months are not available.

**3. Summary of significant accounting policies (continued)**

**3.13 Derivative financial instruments (continued)**

As such, the Bank values its assets and liabilities related to this clause by middle rate of Croatian National Bank valid at the date of balance sheet or foreign exchange rate agreed by the option (rate valid at origination) if higher.

**3.14 Cash flow statement**

For the purpose of reporting cash flows, cash and cash equivalents include cash and balances with banks, placements with other banks with maturity of less than 90 days.

**3.15 Managed funds**

The Bank manages funds on behalf of legal entities and individuals, for which it charges a fee. As these amounts do not represent the Bank's assets and liabilities, they are excluded from the accompanying balance sheet (Note 27).

**3.16 Accounting for financial guarantee contracts**

The IASB has also amended IAS 39 Financial Instruments: Recognition and Measurement to require certain financial guarantee contracts issued by the Bank to be accounted for in accordance with that Standard. Financial guarantee contracts that are accounted for in accordance with IAS 39 are measured initially at their fair values, and subsequently measured at the higher of:

- the amount of the obligation under the contract, as determined in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets; and
- the amount initially recognized less, where appropriate, cumulative amortization recognized in accordance with the revenue recognition policies.

The management of the Bank has assessed that adoption of this amendment to IAS 39 does not materially impact the amounts reported in the previous periods.

**3. Summary of significant accounting policies (continued)**

**3.17 Significant accounting judgments and estimates**

*Judgments*

In the process of applying the Bank's accounting policies, management has made the following judgments, apart from those involving estimations, which have the most significant effect on the amounts recognized in the financial statements:

*Held to maturity investments*

The Bank follows the guidance of IAS 39 on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held to maturity. This classification requires significant judgment. In making this judgment, the Bank evaluates its intention and ability to hold such investments to maturity. If the Bank fails to keep this investments to maturity other than for the specific circumstances (such as selling an insignificant amount close to maturity) it will be required to reclassify the entire class as available for sale and measure it at fair value instead of amortized cost.

*Estimation uncertainty*

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

*Allowances for impairment of loans and receivables*

The Bank regularly reviews its loans and receivables to assess impairment. The Bank uses its experienced judgment to estimate the amount of any impairment loss in cases where a borrower is in financial difficulties and there are few available historical data relating to similar borrowers. Similarly, the Bank estimates changes in future cash flows based on the observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the group of loans and receivables. The Bank uses its experienced judgment to adjust observable data for a group of loans or receivables to reflect current circumstances.

## 4. Interest and similar income

| | 2009 | 2008 |
|---|---|---|
| Loans to corporate clients | 73,706 | 52,569 |
| Loans to retail clients | 30,990 | 28,564 |
| Placements with other banks | 1,778 | 5,429 |
| Croatian National Bank | 762 | 1,088 |
| Debt securities | 2,035 | 1,936 |
| Other companies | 1,916 | 1,245 |
| | **111,187** | **90,831** |

### a) Analysis by product

| | 2009 | 2008 |
|---|---|---|
| Loans to customers | 106,612 | 82,378 |
| Placements with banks | 2,540 | 6,517 |
| Debt securities | 2,035 | 1,936 |
| | 111,187 | **90,831** |

## 5. Interest and similar expense

| | 2009 | 2008 |
|---|---|---|
| Retail clients | 32,427 | 22,393 |
| Corporate clients | 11,115 | 9,724 |
| Banks | 9,570 | 6,484 |
| Other companies | 5,567 | 8,500 |
| Other borrowed funds | 582 | 18 |
| | **59,261** | **47,119** |

### a) Analysis by product

| | 2009 | 2008 |
|---|---|---|
| Deposits | 49,078 | 40,546 |
| Borrowings | 10,183 | 6,573 |
| | **59,261** | **47,119** |

## 6. Fee and commission income and expense

| | 2009 | 2008 |
|---|---|---|
| **Fee and commission income** | | |
| Commission income from corporate clients | 16,160 | 16,900 |
| Commission income from retail clients | 4,616 | 4,709 |
| Commission income from banks | 3,825 | 3,492 |
| | **24,601** | **25,101** |
| **Fee and commission expense** | | |
| Commission for domestic payments | 8,659 | 8,420 |
| Other fees and commissions | 3,618 | 2,498 |
| | **12,277** | **10,918** |

## 7. Net foreign exchange gains

| | 2009 | 2008 |
|---|---|---|
| Income from foreign currency trading | 15,972 | 7,820 |
| Translation losses | (837) | (952) |
| | **15,135** | **6,868** |

## 8. Operating expenses

| | 2009 | 2008 |
|---|---|---|
| Personnel expenses (Note 8.1) | 26,382 | 25,216 |
| Material and services | 27,197 | 20,370 |
| Depreciation (Note 17 and 18) | 2,777 | 3,227 |
| Marketing and administration expenses | 1,941 | 1,678 |
| Insurance premiums | 1,038 | 998 |
| Taxes and contributions | 626 | 580 |
| Other expenses | 1,447 | 1,323 |
| | **61,408** | **53,392** |

### 8.1. Personnel expenses

| | 2009 | 2008 |
|---|---|---|
| Net salaries | 13,916 | 13,166 |
| Taxes and contributions from salaries | 7,587 | 7,568 |
| Contributions on salaries | 3,699 | 3,541 |
| Other personnel expenses | 1,180 | 941 |
| | **26,382** | **25,216** |

The number of employees as at 31 December 2009 was 176 (2008:163).

### 9. Impairment losses and provisions

| | *Note* | 2009 | 2008 |
|---|---|---|---|
| Loans to customers | *14* | (7,686) | (8,027) |
| Interest | *19* | (784) | (423) |
| Other assets | *19* | (331) | (540) |
| Contingent liabilities | *26* | (222) | (418) |
| | | **(9,023)** | **(9,408)** |
| *Less: amounts collected and reversed* | | | |
| Loans to customers | *14* | 3,476 | 9,116 |
| Interest | *19* | 188 | 861 |
| Other assets | *19* | 192 | 926 |
| Contingent liabilities | *26* | 603 | 103 |
| **Total** | | **(4,564)** | **1,598** |

## 10. Income tax

Income tax is determined by applying the rate of 20% to taxable profits (2008: 20%).

Reconciliation of income tax:

| | 2009 | 2008 |
|---|---|---|
| Current tax | 3,122 | 4,143 |
| Deferred tax | 354 | (593) |
| | **3,476** | **3,550** |

Tax returns remain open and subject to tax audit at least over a three-year period. The management is confident that the Bank has made adequate provisions for tax obligations in the accompanying financial statements. However, the risk remains that the relevant authorities could take a different view with regard to the interpretation of the applicable provisions.

Reconciliation between accounting profit and taxable profit is as follows:

| | 2009 | 2008 |
|---|---|---|
| Accounting profit before tax | 15,663 | 15,106 |
| Expected tax rate of 20% | 3,133 | 3,021 |
| Tax effect of non-taxable income | 1,757 | 1,511 |
| Tax effect of tax deductible costs | (1,414) | (982) |
| **Income tax expense** | **3,476** | **3,550** |
| **Effective tax rate** | **22.26%** | **23.50%** |

## 11. Cash and balances with Croatian National Bank

| | 31.12.2009 | 31.12.2008 |
|---|---|---|
| Cash in hand | 34,505 | 33,801 |
| Instruments in the course of collection | 17 | 13 |
| **Total cash** | **34,522** | **33,814** |
| Cash account with the Croatian National Bank | 57,632 | 12,081 |
| Obligatory reserve in HRK | 95,870 | 83,621 |
| Obligatory reserve in foreign currency | 15,014 | 18,267 |
| Other deposits with the Croatian National Bank | - | 60,054 |
| **Total assets with the Croatian National Bank** | **168,516** | **174,023** |
| **Total cash and balances with the Croatian National Bank** | **203,038** | **207,837** |

The CNB determines the requirement for banks to calculate an obligatory reserve, which is required to be deposited with the CNB and held in the form of other liquid receivables.

The obligatory reserve requirement as at 31 December 2009 amounted to 14% (until 10 December 2008: 17%) of kuna and foreign currency deposits, borrowings and issued debt securities.

As at 31 December 2009, the required rate for the kuna part of the obligatory reserve to be deposited with the CNB amounted to 70% (2008: 70%), while the remaining 30% (2008: 30%) had to be held in the form of other liquid receivables. This includes the part of foreign currency obligatory reserve required to be held in HRK (see below).

60% of the foreign currency part of the obligatory reserve (2008: 60%) is deposited with the CNB, while the remaining 40% (2008: 40%) must be held in the form of other liquid receivables, after adjusting for the obligatory reserve requirement arising from foreign currency funds from non-residents and related parties (which is required to be held in full with the CNB). From 14 January 2009 75% (2008: 50%) of the foreign currency obligatory reserve is required to be held in HRK and is added to the kuna part of the obligatory reserve (see above).

Compulsory CNB bills had to be subscribed if growth of eligible assets and off-balance-sheet items was in excess of thresholds determined by the CNB. This measure was introduced in 2007. The rate of purchase of compulsory CNB bills was 75% with maturity of 360 days from the date of subscription. The interest rate was 0.25%. The decision requiring purchase of CNB bills was abolished on 23 November 2009.

## 12. Placements with other banks

| | 31.12.2009 | 31.12.2008 |
|---|---|---|
| **Current accounts with other banks** | | |
| - denominated in foreign currency | 86,914 | 107,737 |
| **Loans and time deposits with other banks** | | |
| - denominated in foreign currency | 98,857 | 123,991 |
| - denominated in HRK | - | 53,349 |
| **Total placements with other banks** | **185,771** | **285,077** |
| Provisions for impairment losses | - | (3,349) |
| **Total placements with other banks, net** | **185,771** | **281,728** |

Of the total amount of placements with other banks 1,832 thousand relates to guarantee deposits at Erste Bank with original maturities greater than 3 months.

**Movements in provision:**

| | 2009 | 2008 |
|---|---|---|
| **Balance as at 1 January** | **3,349** | **3,349** |
| New impairment losses | - | - |
| Amounts collected | - | - |
| Amounts written off | 3,349 | - |
| **Balance as at 31 December** | **-** | **3,349** |

During the year the Bank has made a write-off of previously fully impaired receivables from Gold štedionica d.o.o in bankruptcy and Mediteran štedionica d.o.o in bankruptcy.

**12. Placements with other banks (continued)**

Loans to other banks comprises of loans as follows:

| Bank | Interest rate | 31.12.2009 | Interest rate | 31.12.2008 |
|---|---|---|---|---|
| Privredna banka Zagreb d.d. | - | - | 2.5% | 35,000 |
| Karlovačka banka d.d. | - | - | 2.5% | 15,000 |
| **Total** | **-** | **-** | **-** | **50,000** |

***Geographical analysis:***

| | 31.12.2009 | 31.12.2008 |
|---|---|---|
| Belgium | 304 | 205 |
| Germany | 5,962 | 45,317 |
| Italy | 5,262 | 30,384 |
| Croatia | 7,432 | 57,722 |
| Switzerland | 4,765 | 38,800 |
| Sweden | 572 | 133 |
| Denmark | 34,820 | 37,261 |
| The Netherlands | 1,310 | 7,886 |
| Austria | 50,949 | 4,776 |
| USA | 20,999 | 23,160 |
| Spain | 50,799 | 35,951 |
| Canada | 2,551 | 93 |
| Norway | 46 | 40 |
| | **185,771** | **281,728** |

All placements are kept with first-class international banks.

## 13. Assets at fair value through profit or loss

| | 31.12.2009 | 31.12.2008 |
|---|---|---|
| Bonds from Government of Croatia – listed on stock exchange | 2,580 | 15,652 |
| **Total** | **2,580** | **15,652** |

As at 31 December 2009, assets at fair value through profit or loss consists of foreign currency bond issued by the Government of Croatia, with a total nominal value in currency of EUR 353 thousand (2008: EUR 334 thousand) which is listed on stock exchange.

During 2009 the Bank has sold two bonds from Government of Croatia and realized net gain of HRK 15 thousand.

In the period from 7th December to 14th December 2009. the Bank has bought and sold foreign currency bond from Agrokor d.d. and achieved a net profit of HRK 530 thousand.

The Bank incurred net profit on fair measurement of those bonds in the amount of HRK 470 thousand (2008: net loss in the amount of HRK 1,342 thousand).

Investments in securities classified at fair value through profit or loss are as follows:

| Bonds | Maturity date | Interest rate | Currency | 31.12.2009 | 31.12.2008 |
|---|---|---|---|---|---|
| XS0163495004 | 24.02.2010 | 4.625% | EUR | 2,580 | 2,449 |
| RHMF-O-125A3 | 23.05.2012 | 6.875% | EUR | - | 3,754 |
| RHMF-O-172A5 | 28.02.2017 | 4.75% | HRK | - | 9,449 |
| | | | | **2,580** | **15,652** |

## 14. Loans to customers

### a) Analysis of lending portfolio

| | 31.12.2009 | 31.12.2008 |
|---|---|---|
| Retail clients | 317,008 | 321,327 |
| Corporate clients | 780,435 | 573,559 |
| Other companies | 1,463 | 212 |
| Financial institutions | 5,600 | - |
| **Gross loans and advances** | **1,104,506** | **895,098** |
| Less: impairment allowance | (30,069) | (51,317) |
| **Total loans to customers** | **1,074,437** | **843,781** |

**14. Loans to customers (continued)**

Loans are secured by specific pledges on properties, deposits, guarantees, securities and other types of collaterals.

In the period from 1 January to 31 December 2009, the interest rates on loans to corporate clients were set at 9% to 12.9% (2008: 8% to 12.5%), and for loans to retail clients at 6 % to 13.99% (2008: 6.25% to 13.99%).

**b) Changes in the principal of statutory substandard and non-performing loans**

| | 2009 | | 2008 | |
|---|---|---|---|---|
| | **Statutory substandard loans** | **Statutory non-performing loans** | **Statutory substandard loans** | **Statutory non-performing loans** |
| **As at 1 January** | **34,973** | **30,588** | **49,154** | **46,244** |
| Transfer from performing loans | 6,252 | 1,755 | 7,423 | 279 |
| Transfer from fully unrecoverable loans | 35 | - | 61 | - |
| Transfer from partly recoverable loans | - | 42 | - | 2,806 |
| Transfer to performing loans | (230) | (61) | (6,824) | (426) |
| Transfer to fully unrecoverable loans | (42) | - | (2,806) | - |
| Transfer to partly recoverable loans | - | (35) | - | (61) |
| Amounts collected | (4,808) | (1,334) | (11,934) | (1,632) |
| Amounts written off | - | (23,100) | - | (16,650) |
| Other increases | - | 75 | 3 | 503 |
| Other decreases | (265) | (109) | (104) | (475) |
| **As at 31 December** | **35,915** | **7,821** | **34,973** | **30,588** |

**14. Loans to customers (continued)**

**c) Movements in provisions**

| | Specific provision | Impairment allowance on collective assessment basis | Total |
|---|---|---|---|
| **Balance as at 31 December 2007** | **58,660** | **10,322** | **68,982** |
| New impairment losses (Note 9) | 4,991 | 3,036 | 8,027 |
| Amounts collected (Note 9) | (7,379) | (1,737) | (9,116) |
| Amounts written off | (16,613) | - | (16,613) |
| Foreign exchange differences | 37 | - | 37 |
| **Balance as at 31 December 2008** | **39,696** | **11,621** | **51,317** |
| New impairment losses (Note 9) | 7,241 | 445 | 7,686 |
| Amounts collected (Note 9) | (426) | (3,050) | (3,476) |
| Amounts written off | (25,766) | - | (25,766) |
| Foreign exchange differences | 308 | - | 308 |
| **Balance as at 31 December 2009** | **21,053** | **9,016** | **30,069** |

**d) Deferred fee income recognized as an adjustment to the effective yield**

| | 31.12.2009 | 31.12.2008 |
|---|---|---|
| **As at 1 January** | **7,497** | **4,678** |
| Collected and deferred fees | 6,629 | 8,733 |
| Fees recognized | (7,856) | (5,914) |
| **As at 31 December** | **6,270** | **7,497** |

**e) Concentration of credit risk**

The Bank has a diversified lending portfolio that covers various industries, with the largest concentration in the retail sector, which was 19.2% (2008: retail sector 32.3%) of the total credit portfolio at the year-end.

**14. Loans to customers (continued)**

| | 31.12.2009 | | 31.12.2008 | |
|---|---|---|---|---|
| | **Amount** | **%** | **Amount** | **%** |
| Manufacturing | 233,187 | 12.1 | 127,931 | 13.5 |
| Trade | 296,095 | 15.4 | 155,975 | 16.4 |
| Retail customers | 367,163 | 19.1 | 306,186 | 32.3 |
| Financial intermediaries | 290,162 | 15.1 | 35,809 | 3.8 |
| Construction industry | 141,235 | 7.3 | 112,149 | 11.8 |
| Transport, storage and communication | 91,253 | 4.7 | 55,502 | 5.9 |
| Services | 261,685 | 13.6 | 99,721 | 10.5 |
| Agriculture and forestry | 29,025 | 1.5 | 23,179 | 2.4 |
| Tourism, hotels and restaurants | 4,468 | 0.2 | 3,453 | 0.4 |
| Other | 211,884 | 11.0 | 28,439 | 3.0 |
| | **1,926,157** | **100.0** | **948,344** | **100.0** |

**15. Investments held to maturity**

| | **31.12.2009** | **31.12.2008** |
|---|---|---|
| **Investments held to maturity** | | |
| Corporate bills of exchange | 4,677 | 1,567 |
| Allowance for impairment losses | (73) | (73) |
| **Total investments held to maturity** | **4,604** | **1,494** |

Bills of exchange were issued by different corporate entities, with an interest rate from 9.7% to 11.5% and are due over the period to 20 October 2010. Bills of exchange are carried at amortized cost less any allowance for impairment. As at 31 December 2009, HRK 73 thousand of the total amount of bills of exchange became due (2008: HRK 73 thousand).

In the year 2009 and 2008, there have been no changes in the movement of provisions of financial assets available for sale.

**16. Investments available for sale**

| | **31.12.2009** | **31.12.2008** |
|---|---|---|
| Debt securities available for sale | 32,320 | 40,324 |
| Equity securities available for sale | 46,649 | 785 |
| | **78,969** | **41,109** |

**16. Investments available for sale (continued)**

**Debt securities available for sale**

| | 31.12.2009 | 31.12.2008 |
|---|---|---|
| Treasury bills from Ministry of Finance | 23,959 | - |
| Factoring | 1,825 | 5,303 |
| Commercial bills | 6,536 | - |
| | **33,320** | **5,303** |
| Listed | 30,495 | - |
| Unlisted | 1,825 | 5,303 |

**Equity securities available for sale**

| | 31.12.2009 | 31.12.2008 |
|---|---|---|
| Participation in investment fund | 45,840 | 35,021 |
| Securities listed on stock exchange | 62 | 38 |
| Securities unlisted on stock exchange | 747 | 747 |
| | **46,649** | **35,806** |

Unlisted equity securities comprise a certain number of small individual investments presented at cost less impairment. There is no market for these investments and account for less than 1% of the share capital of those entities. In the opinion of the Bank's management, the fair values do not differ substantially from their carrying amounts.

During the year 2009, the Bank made an investment in the investment fund Agram Cash in the amount of HRK 6,400 thousand and in Agram Euro Cash in the amount of HRK 2,270 thousand. During the year the Bank also had investment in the investment fund Erste Cash in the amount of HRK 4,000 thousand and made net income in the amount of HRK 91 thousand.

Movement in equity securities during the year:

| | 2009 | 2008 |
|---|---|---|
| **As at 1 January** | **35,806** | **828** |
| Change in fair value of shares | 24 | (43) |
| Investment fund stake purchase | 12,670 | 35,850 |
| Investment fund stake sale | (4,000) | - |
| Increase in fair value of stake | (8,640) | (4,023) |
| Foreign exchange differences | 10,789 | 3,194 |
| **As at 31 December** | **46,649** | **35,806** |

**17. Intangible assets**

| | Software and other rights | Assets acquired but not brought into use | Total |
|---|---|---|---|
| **Cost** | | | |
| **At 31 December 2007** | **9,330** | **5,913** | **15,243** |
| Additions | - | 914 | 914 |
| Brought into use | 1,399 | (1,399) | - |
| **At 31 December 2008** | **10,729** | **5,428** | **16,157** |
| Additions | - | 4,942 | 4,942 |
| Brought into use | 350 | (350) | - |
| **At 31 December 2009** | **11,079** | **10,020** | **21,099** |
| **Accumulated depreciation** | | | |
| **At 31 December 2007** | **7,401** | **-** | **7,401** |
| Charge for the year | 557 | - | 557 |
| **At 31 December 2008** | **7,958** | **-** | **7,958** |
| Charge for the year | 507 | - | 507 |
| **At 31 December 2009** | **8,465** | **-** | **8,465** |
| **Net book value** | | | |
| **At 31 December 2008** | 2,771 | 5,428 | 8,199 |
| **At 31 December 2009** | **2,614** | **10,020** | **12,634** |

At the beginning of 2009, the Management Board made a decision to launch development of "Split 3" software and to establish a project team for that purpose. During the year, a contract on technical cooperation was signed with Dialog d.o.o. Osijek for development of components for software application and for implementation of the application. Deadline for the finish of the project is 1 March 2012, and it is expected it will be met.

## 18. Tangible assets

| | Buildings | Computers | Furniture and equipment | Vehicles | Assets acquired but not brought into use | Total |
|---|---|---|---|---|---|---|
| **Cost** | | | | | | |
| **At 31 December 2007** | **47,272** | **5,067** | **14,301** | **938** | **1,826** | **69,404** |
| Additions | - | - | - | - | 172 | 172 |
| Brought into use | 1,785 | 46 | 156 | - | (1,987) | - |
| Disposals | - | - | - | (286) | - | (286) |
| **At 31 December 2008** | **49,057** | **5,113** | **14,457** | **652** | **11** | **69,290** |
| Additions | - | - | - | - | 1,075 | 1,075 |
| Brought into use | - | 536 | 486 | 17 | (1,039) | - |
| **At 31 December 2009** | **49,057** | **5,649** | **14,943** | **669** | **47** | **70,365** |
| **Accumulated depreciation** | | | | | | |
| **At 31 December 2007** | **15,745** | **4,247** | **11,555** | **883** | **-** | **32,430** |
| Charge for the year | 1,481 | 348 | 786 | 55 | - | 2,670 |
| Disposals | - | - | - | (286) | - | (286) |
| **At 31 December 2008** | **17,226** | **4,595** | **12,341** | **652** | **-** | **34,814** |
| Charge for the year | 1,486 | 207 | 574 | 3 | - | 2,270 |
| **At 31 December 2009** | **18,712** | **4,802** | **12,915** | **655** | **-** | **37,084** |
| **Net book value** | | | | | | |
| **At 31 December 2008** | **31,831** | **518** | **2,116** | **-** | **11** | **34,476** |
| **At 31 December 2009** | **30,345** | **847** | **2,028** | **14** | **47** | **33,281** |

There are no pledges on property for borrowings as at 31 December 2009

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## 19. Other assets

| | 31.12.2009 | 31.12.2008 |
|---|---|---|
| Accrued interest | 15,804 | 14,043 |
| Repossessed assets | 11,603 | 11,603 |
| Fees and commissions | 2,020 | 2,819 |
| Receivables from card operations | 1,678 | 1,550 |
| Prepaid expenses | 4,467 | 5,061 |
| Bails | 6,929 | 4,798 |
| Other receivables | 14,066 | 13,699 |
| | **56,567** | **53,573** |
| Less allowance for impairment: | | |
| - other assets | (4,876) | (2,110) |
| **Total other assets** | **51,691** | **51,463** |

**Changes in allowances**

| | Interest | Other assets |
|---|---|---|
| **Balance as at 31 December 2007** | **-** | **2,602** |
| New allowances (Note 9) | 423 | 540 |
| Amounts collected (Note 9) | (861) | (926) |
| Amounts written off | (423) | (106) |
| Other | 861 | - |
| **Balance as at 31 December 2008** | **-** | **2,110** |
| New allowances (Note 9) | 784 | 331 |
| Amounts collected (Note 9) | (188) | (192) |
| Amounts written off | (784) | (710) |
| Other | 188 | - |
| **Balance as at 31 December 2009** | **-** | **1,539** |

All funds are due within one year.

## 20. Deposits from customer

| | 31.12.2009 | 31.12.2008 |
|---|---|---|
| **Demand deposits** | | |
| Retail clients | 75,307 | 76,347 |
| Corporate clients | 115,578 | 160,545 |
| Other companies | 42,152 | 32,213 |
| **Total demand deposits** | **233,037** | **269,105** |
| | | |
| **Term deposits** | | |
| Retail clients | 627,943 | 540,407 |
| Corporate clients | 140,964 | 240,186 |
| Other companies | 142,951 | 147,904 |
| **Total term deposits** | **911,858** | **928,497** |
| **Total deposits from customers** | **1,144,895** | **1,197,602** |

The interest rate on demand deposits varied from 0.5% to 0.75% during the year 2009 and 2008.
The interest rate on time retail deposits varied from 1 % to 8.8 % and from 1% to 8.5% during the year 2009 and 2008, respectively while the interest rate for time corporate deposits varied from 2% to 10% during the year 2009.

## 21. Borrowings

| | 31.12.2009 | 31.12.2008 |
|---|---|---|
| Denominated in HRK | 156,983 | 90,088 |
| Denominated in foreign currency | 36,531 | - |
| **Total borrowed funds** | **193,514** | **90,088** |

Interest rate on loans from the Croatian Bank for Reconstruction and Development denominated in HRK varied from 2.75% to 5.20%, while for the end user the interest rate varied from 4% to 7% during the year 2009.

**21. Borrowings (continued)**

Loans received comprise of borrowings as follows:

| | 2009 | 2008 |
|---|---|---|
| Istarska kreditna banka d.d. | 4,000 | 5,000 |
| Šted banka d.d. | 7,000 | - |
| Privredna banka Zagreb d.d. | 10,000 | - |
| Croatia banka d.d. | 11,000 | - |
| Banka kovanica d.d. | 15,000 | 6,000 |
| Slatinska banka d.d. | 5,000 | - |
| Podravska banka d.d. | 27,500 | - |
| Obrtnička štedna banka d.d. | 2,000 | - |
| Jadranska banka d.d. | 20,000 | - |
| Erste&steiermärkische bank d.d. | 7,000 | - |
| Hypo Alpe Adria bank d.d. | 7,000 | - |
| Hrvatska poštanska banka d.d. | 15,000 | 25,000 |
| Adria bank ag Wien | 36,531 | |
| HBOR d.d. | 26,483 | 28,588 |
| BKS bank d.d. | - | 3,000 |
| Banka Brod d.d. | - | 3,500 |
| Samoborska banka d.d. | - | 4,000 |
| Imex banka d.d. | - | 15,000 |
| | **193,514** | **90,088** |

Borrowing costs are recognized when incurred. The repayment of the loans is secured by the Bank's bills of exchange and statements on account garnishment.

The loans from the Croatian Bank for Reconstruction and Development (HBOR) relate to loans placed by HBOR through the Bank in accordance with its financing programmes.

*Collaterals*

No collaterals have been provided for the loans referred to above, as these are overnight loans. The relationship between the Bank and HBOR is subject to a separate agreement.

## 22. Other liabilities

| | 31.12.2009 | 31.12.2008 |
|---|---|---|
| Accrued interest | 18,042 | 12,705 |
| Liabilities to suppliers | 1,852 | 2,468 |
| Deferred income | 7,770 | 7,497 |
| Liabilities for card operations | 673 | 1,041 |
| Other liabilities | 2,678 | 1,913 |
| **Total other liabilities** | **31,015** | **25,624** |

## 23. Share capital

Based on decision from General Assembly held on 30 June 2008 and HANFA's Resolution on approval of prospect for issuing shares with an private offer dated 11 December, capital increase has been made during January 2009.
The share capital has increased by issuing of 545,587 new ordinary shares (KBZ-R-A) with nominal value of HRK 100. In this way the share capital has increased from HRK 131,994,500 to HRK 186,553,200 and comprises of 1,865,532 ordinary shares (KBZ-R-A) with nominal value of HRK 100.

The following shareholders held over 5% of the Bank's equity at 31 December 2009 and 31 December 2008:

| **Shareholders'** | **Percentage of share capital held (%)** | |
|---|---|---|
| | **31.12.2009** | **31.12.2008** |
| Euroherc osiguranje d.d. | 18.38 | 19.90 |
| Jadransko osiguranje d.d. | 16.79 | 16.93 |
| Agram životno osiguranje d.d. | 16.40 | 16.66 |
| Euroleasing d.o.o. | 11.79 | 11.42 |
| Euro Daus d.d. | 9.18 | 8.89 |
| Others | 27.46 | 26.20 |
| **Total share capital** | **100.00** | **100.00** |

The Bank's shares are listed on Zagreb Stock Exchange. At 31 December 2009 the share price of the Bank's ordinary shares quoted on the Zagreb Stock Exchange was HRK 209.

**23. Share capital (continued)**

**Share premium**

As a result of the share issue in January 2009, the Bank recognised share premium in an amount of HRK 43,647 thousand representing the excess of the paid-in amount over the nominal value of the issued shares.

**Dividend**

On General Shareholders Meeting as of 10 July 2009 the Shareholders of Kreditna banka Zagreb d.d., took a decision on the distribution of a dividend of HRK 7,089 thousand. The dividend amounted HRK 3.8 per share.

**Regulatory capital**

Regulatory capital according to CNB requirements, calculated for the Bank only, is as follows:

| | 31.12.2009<br>HRK`000 | 31.12.2008<br>HRK`000 |
|---|---|---|
| **Basic capital** | | |
| Issued share capital | 230,200 | 131,995 |
| Legal, statutory and other reserves | 32,256 | 26,964 |
| **Total basic capital** | **262,456** | **158,959** |
| **Supplementary capital** | | |
| Specific reserves for unidentified losses | 14,585 | 13,523 |
| **Gross additional share** | **14,585** | **13,523** |
| **Deductions** | | |
| Specific reserves for unidentified losses that are not included in supplementary capital | (14,585) | (13,523) |
| **Total deductions from supplementary capital** | **(14,585)** | **(13,523)** |
| **Total supplementary capital (gross supplementary capital less deductions)** | **-** | **-** |
| **Gross regulatory capital** | **262,456** | **158,959** |
| | | |
| **Risk weighted assets** | | |
| Credit risk weighted assets | 1,609,244 | 1,260,062 |
| Other weighted assets | 18,354 | 9,267 |
| **Total risk weighted assets** | **1,627,598** | **1,269,329** |
| **Capital adequacy ratio** | **16.13%** | **12.52 %** |

## 24. Retained earnings and reserves

Retained earnings include accumulated profits from prior years.

In accordance with the local legislation 5 percent of the net profit of the Bank is required to be transferred to a non-distributable legal reserve to equal 5 percent of the share capital of the Bank. The legal reserve, in the amount of up to 5% of issued share capital, can be used for covering current and prior years losses.

Based on General Assembly's decision from 10 July 2009 the Bank allocated the amount of HRK 3,889 thousand into retained earnings and the amount of HRK 578 thousand into legal reserves.

## 25. Earnings per share

**Basic**

For the purposes of calculating earnings per share, earnings are calculated as the profit for the period attributable to equity holders of the Bank. For the reconciliation of profit after tax which is distributed to ordinary shareholders please see below:

| | 2009 | 2008 |
|---|---|---|
| Profit for the year in HRK | 12,186,822 | 11,555,600 |
| Profit attributable to equity holders of the Bank | 12,186,822 | 11,555,600 |
| Weighted average number of ordinary shares in issue | 1,865,532 | 1,319,945 |
| **Earnings per share in HRK** | **6.53** | **8.75** |

**Diluted**

Given that there is no effect of options, convertible bonds or similar effect, the weighted average number of ordinary shares used for diluted earnings per share was the same as used to calculate basic earnings per share

## 26. Contingences and commitments

### a) Legal proceedings

There are several legal proceedings outstanding against the Bank. There are no provisions made for these legal proceedings due to Bank’s management judgment of likelihood of outcome of the legal proceedings.

**26. Contingences and commitments (continued)**

**b) Guarantees and credit commitments**

As at 31 December 2009 and 31 December 2008, the total amount of guarantees, letters of credit and unused revolving credits was as follows:

| | 31.12.2009 | 31.12.2008 |
|---|---|---|
| Guarantees in HRK | 85,576 | 68,517 |
| Guarantees in foreign currency | 935 | 5,684 |
| Letters of credit | 8,564 | 20,123 |
| Credit commitments | 83,929 | 129,440 |
| **Total guarantees and credit commitments** | **179,004** | **223,764** |

**c) Movements in provisions**

| | 2009 | 2008 |
|---|---|---|
| **Balance as at 1 January** | **1,903** | **1,588** |
| New provisions (Note 9) | 222 | 418 |
| Decreases (Note 9) | (603) | (103) |
| **Balance as at 31 December** | **1,522** | **1,903** |

**27. Managed funds**

The Bank manages assets for and on behalf of legal entities and citizens. Related income and expense are charged to the customer, and the Bank does not bear any liabilities.

Net assets and liabilities from operations in the name and on behalf of third parties are as follows:

| | 31.12.2009 | 31.12.2008 |
|---|---|---|
| Assets | | |
| Retail clients | 89 | 89 |
| Corporate clients | 598 | 598 |
| **Total assets** | **687** | **687** |
| Liabilities | | |
| Retail clients | 53 | 53 |
| Corporate clients | 634 | 634 |
| **Total liabilities** | **687** | **687** |

## 28. Cash and cash equivalents

Cash and cash equivalents comprise the following items with an original maturity of up to 3 months:

| | 31.12.2009 | 31.12.2008 |
|---|---|---|
| Cash account at Croatian National Bank (Note 11) | 57,632 | 12,081 |
| Cash in hand (Note 11) | 34,505 | 33,801 |
| Instruments in the course of collection (Note 11) | 17 | 13 |
| Placements with other banks (Note 12) | 183,939 | 281,728 |
| **Total cash and cash equivalents** | **276,093** | **327,623** |

## 29. Risk management

This note provides details of the Bank's exposure to risk and describes the methods used by management to control risk. The most important types of financial risk to which the Bank is exposed are credit risk, liquidity risk and market risk. Market risk includes currency risk, interest rate risk and equity price risk. An integrated system of risk management is being established by introducing a set of policies and procedures, determining the limits of risk levels acceptable to the Bank. Methodology and models for managing operational risk have been developed.

### a) Credit risk

The Bank takes on exposure to credit risk which is the risk upon that the counter party will be unable to pay amounts in full when due. The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review. Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees.

*Credit related commitments*

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit, which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Documentary and commercial letters of credit, which are written undertakings by the Bank on behalf of a customer authorizing a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions, are collateralized by the underlying shipments of goods to which they relate and therefore carry less risk than a direct borrowing.

**29. Risk management (continued)**

**a) Credit risk (continued)**

Loans are classified into the following three main groupings, in accordance with the regulations of the Croatian National Bank:

- performing loans – A Risk Group – measured on a collective basis
- substandard loans – B Risk Group – measured on an individual basis, or an a collective basis for a „small loans portfolio" that are not sued
- non-performing loans (bad debt) – C Risk Group – measured on an individual basis, or an a collective basis for a „small loans portfolio" that are not sued

All three levels contain sub-categories, which are mandatory for the substandard loans. The Bank's policy is to require suitable collateral to be provided by certain customers prior to the disbursement of approved loans. Collateral for loans, guarantees and letters of credit is usually in the form of deposits, pledge, listed investments, bills of exchange, mortgages over residential properties, and mortgages over business properties, promissory notes or other assets.

Commitments to extend credit represent unused portions of authorizations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments since most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Bank monitors the term to maturity of credit commitments because long-term commitments generally have a greater degree of credit risk than short-term commitments.

**b) Liquidity risk**

The Bank is exposed to daily calls on its available cash resources from overnight deposits, current accounts, maturing deposits and loan drawdown's.
The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Bank. It is unusual for banks ever to be completely matched since business transacted is often of uncertain term and of different types. An unmatched position potentially enhances profitability, but can also increase the risk of losses.

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest–bearing liabilities as they mature, are important factors in assessing the liquidity of the Bank and its exposure to changes in interest rates and exchange rates. Liquidity requirements to support calls under guarantees and standby letters of credit are considerably less than the amount of the commitment because the Bank does not generally expect the third party to draw funds under the agreement. The total outstanding contractual amount of commitments to extend credit does not necessarily represent future cash requirements, since many of these commitments will expire or terminate without being funded.
The liquidity risk analysis is presented within the maturity analysis of assets and liabilities at 31 December 2009 and 31 December 2008 (see Note 29).

**29. Risk management (continued)**

**c) Market risk**

Most trading instruments are subject to market risk, which is the risk that future changes in market conditions may make an instrument less valuable or more onerous. The instruments are recognized at fair value, and all changes in market conditions directly affect net trading income. The Bank manages its use of trading instruments in response to changing market conditions.
The limits are defined following the needs and strategy of the Bank and in accordance with the senior management risk policy indications.

The exposure to market risk is formally managed in accordance with the risk limits approved by the senior management and revised at least annually. The exposure figures and limit utilization are delivered to the Treasury Division on a daily basis.

**d) Interest rate risk**

The Bank is exposed to various risks associated with the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest rate gap table summarizes the Bank's exposure to interest rate risks. Included in the table are the Bank's assets and liabilities at carrying amounts, categorized by the earlier of contractual re pricing or maturity dates (see Note 32).

**e) Currency risk**

The Bank takes on exposure to effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Bank sets limits on the level of exposure by currency and in total for both overnight and intra-day positions.

Foreign currency balance sheet and foreign exchange risk table summarizes the Bank's exposure to foreign currency exchange rate risk at 31 December 2009 and 31 December 2008. Included in the table are the Bank's assets and liabilities at carrying amounts, categorized by domestic currency and foreign currency (see Note 33).

**f ) Equity price risk**

Equity price risk is the possibility that equity prices will fluctuate affecting the fair value of equity investments and other derivative instruments.
The primary exposure to equity prices arises from the Bank's holding of equity instruments available for sale. The Bank does not actively trade in equity securities.

**29. Risk management (continued)**

**g) Operational risk**

The operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. This definition includes legal risk but excludes strategic and reputation risk. In order to efficiently measure and manage the operational risk exposure at the Bank level, the Bank is developing internal models for the operational risk exposure management in line with the Basel II prescribed framework. The main goals of this internal model are: to implement techniques enabling a detailed insight in the profile of the risk exposure of the Bank such as (quantitative 'ex-post' and qualitative 'ex-ante' risk exposure assessment); to support the management decision making process by developing efficient policies for the management and mitigation of the operational risk at the Bank level; adjustment of the pricing/provisioning policy by incorporating the expected losses and allocating the adequate economic/regulatory capital for unexpected losses.

## 30. Credit risk

### a) Total credit risk exposure – balance sheet and off- balance sheet

| As at 31 December 2009 | Gross placements | Specific provisions | General provisions | Net placements |
|---|---|---|---|---|
| **A. Balance sheet exposure** | | | | |
| Cash and balances with Croatian National Bank | 168,516 | - | 1,432 | 167,084 |
| Placements with other banks | 185,771 | - | 1,580 | 184,191 |
| Assets available for sale | 78,870 | - | 670 | 78,200 |
| Assets held to maturity | 4,604 | 73 | 39 | 4,492 |
| Loans to customers | **1,104,506** | **21,053** | **9,016** | **1,074,437** |
| - performing loans | 1,060,694 | - | 9,016 | 1,051,678 |
| - substandard loans | 35,991 | 13,232 | - | 22,759 |
| - non-performing loans | 7,821 | 7,821 | - | - |
| Interest, fees and other assets | 38,424 | 1,539 | 325 | 36,560 |
| **Total balance sheet exposure** | **1,580,691** | **22,665** | **13,062** | **1,544,964** |
| **B. Off-balance sheet exposure** | | | | |
| Other banks | - | - | - | - |
| Customers | 179,004 | - | 1,522 | 177,482 |
| - fully recoverable | 179,004 | - | 1,522 | 177,482 |
| - partially recoverable | - | - | - | - |
| - completely irrecoverable | - | - | - | - |
| **Total off-balance sheet exposure** | **179,004** | **-** | **1,522** | **177,482** |
| **TOTAL EXPOSURE (A+B)** | **1,759,695** | **22,665** | **14,584** | **1,722,446** |

**30. Credit risk (continued)**

**a) Total credit risk exposure – balance sheet and off-balance sheet (continued)**

| As at 31 December 2008 | Gross placements | Specific provisions | General provisions | Net placements |
|---|---|---|---|---|
| **A. Balance sheet exposure** | | | | |
| Cash and balances with Croatian National Bank | 207,837 | - | 1,473 | 206,364 |
| Placements with other banks | 285,077 | 3,349 | 2,395 | 279,333 |
| Assets at fair value through profit or loss | 15,652 | - | - | 15,652 |
| Assets available for sale | 41,109 | - | 349 | 40,760 |
| Assets held to maturity | 1,567 | 73 | 13 | 1,481 |
| Loans to customers | 894,994 | 39,696 | 7,078 | 848,220 |
| - performing loans | 832,782 | - | 7,078 | 825,704 |
| - substandard loans | 34,973 | 12,457 | - | 22,516 |
| - non-performing loans | 27,239 | 27,239 | - | - |
| Interest, fees and other assets | 37,527 | 2,112 | 319 | 35,096 |
| **Total balance sheet exposure** | **1,483,763** | **45,230** | **11,627** | **1,426,906** |
| **B. Off-balance sheet exposure** | | | | |
| Other banks | - | - | - | - |
| Customers | 255,176 | - | 1,914 | 253,262 |
| - fully recoverable | 255,176 | - | 1,914 | 253,262 |
| - partially recoverable | - | - | - | - |
| - completely irrecoverable | - | - | - | - |
| **Total off-balance sheet exposure** | **255,176** | **-** | **1,914** | **253,262** |
| **TOTAL EXPOSURE (A+B)** | **1,738,939** | **45,230** | **13,541** | **1,680,168** |

**30. Credit risk (continued)**

**b ) Past due claims**

Past due claims consist from placements for which impairment has not been made for both not due and due principle. They are arranged according to the age based on the individual placement including non-collected and not due interest and other income related to the principle. Item other due claims consist from non-collected interest, not due interest and claims that are written-off for which collection is still in progress. The amount of overall individual placement is arranged in the range between the oldest and the youngest past due claim, regardless whether the principle or the interest is due.

| As at 31 December 2009 | Due up to 30 days | Due between 31 and 90 days | Due between 91 and 180 days | Due between 181 and 365 days | Due between 1 and 2 years | Due between 2 and 3 years | Due over 3 years |
|---|---|---|---|---|---|---|---|
| Placements with other banks | - | - | - | - | - | - | - |
| Loans to customers | 654,533 | 95,069 | 29,897 | 38,298 | 18,355 | 4,462 | 30,693 |
| - retail customers | 111,303 | 29,766 | 6,563 | 8,692 | 3,395 | 2,409 | 3,894 |
| - corporate customers | 543,230 | 65,303 | 23,334 | 29,606 | 14,960 | 2,053 | 26,799 |
| - public and other sectors | - | - | - | - | - | - | - |
| Other past due claims | 21,774 | 3,165 | 1,129 | 6,905 | 2,616 | 5,767 | 159,662 |
| **Total past due claims** | **676,307** | **98,234** | **31,026** | **45,203** | **20,971** | **10,229** | **190,355** |

| As at 31 December 2008 | Due up to 30 days | Due between 31 and 90 days | Due between 91 and 180 days | Due between 181 and 365 days | Due between 1 and 2 years | Due between 2 and 3 years | Due over 3 years |
|---|---|---|---|---|---|---|---|
| Placements with other banks | - | - | - | - | - | - | 3,349 |
| Loans to customers | 89,510 | 47,282 | 52,595 | 18,030 | 4,648 | 675 | 69,998 |
| - retail customers | 28,850 | 4,379 | 4,049 | 4,201 | 2,469 | 244 | 5,257 |
| - corporate customers | 60,660 | 42,904 | 48,546 | 13,829 | 2,179 | 431 | 64,741 |
| - public and other sectors | - | - | - | - | - | - | - |
| Other past due claims | 2,008 | 1,532 | 1,694 | 9,996 | 4,302 | 1,202 | 105,631 |
| **Total past due claims** | **91,518** | **48,815** | **54,289** | **28,026** | **8,950** | **1,877** | **178,978** |

**30. Credit risk (continued)**

**c) placements secured by collaterals**

| As at 31 December 2009 | Deposits | Housing mortgage | Business mortgage | Other instruments | No collateral |
|---|---|---|---|---|---|
| **A. Balance sheet exposure** | | | | | |
| Cash and balances with Croatian National Bank | - | - | - | - | 167,084 |
| Derivative financial assets | | | | | |
| Placements with other banks | - | - | - | - | 184,191 |
| Loans to customers | 85,523 | 31,029 | 138,319 | 370,796 | 448,770 |
| Assets available for sale | - | - | - | - | 78,200 |
| Assets held to maturity | - | - | - | - | 4,492 |
| Other assets | - | - | - | - | 36,560 |
| **Total balance sheet exposure** | **85,523** | **31,029** | **138,319** | **370,796** | **919,297** |
| **B. Off-balance sheet exposure** | | | | | |
| Other banks | - | - | - | - | - |
| Clients | 13,616 | 723 | - | - | 163,143 |
| **Total off-balance sheet exposure** | **13,616** | **723** | **-** | **-** | **163,143** |
| **Total exposure (A+B)** | **99,139** | **31,752** | **138,319** | **370,796** | **1,082,440** |

| As at 31 December 2008 | Deposits | Housing mortgage | Business mortgage | Other instruments | No collateral |
|---|---|---|---|---|---|
| Total balance sheet exposure | **46,597** | **39,836** | **128,659** | **247,735** | **924,742** |
| Total off-balance sheet exposure | **13,616** | **723** | **-** | **-** | **240,837** |
| **Total exposure** | **60,213** | **40,559** | **128,659** | **247,735** | **1,165,579** |

**30. Credit risk (continued)**

**d) Provision ratio in loans to customers**

| | 31.12.2009 | | 31.12.2008 | |
|---|---|---|---|---|
| | **Loans to customers (%)** | **Provision ratio (%)** | **Loans to customers (%)** | **Provision ratio (%)** |
| Performing loans | 96 | 0.85 | 93 | 0.85 |
| Substandard loans | 3 | 32.59 | 4 | 35.62 |
| Non-performing loans | 1 | 100.00 | 3 | 100.00 |
| **Total** | **100** | | **100** | |

## 31. Liquidity risk

The amount of the total assets and liabilities was analyzed according to the most conservative assumption of remaining maturity from the balance sheet date to the contractual maturity.

| As at 31 December 2009 | 0- 30 days | 1-3 months | 3-12 months | 1 - 2 years | 2 - 3 years | Over 3 years | Total |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| Cash and balances with Croatian National Bank | 127,709 | 14,765 | 40,709 | 10,288 | 3,603 | 5,965 | 203,039 |
| Placements with other banks | 150,240 | 41,131 | - | - | - | - | 191,371 |
| Treasury bills from Ministry of finance | - | 7,909 | 16,050 | - | - | - | 23,959 |
| Assets at fair value through profit or loss | - | 2,580 | - | - | - | - | 2,580 |
| Loans to customers | 166,848 | 165,158 | 285,557 | 105,653 | 79,872 | 261,701 | 1,064,789 |
| Investments available for sale | 47,850 | 6 | 6,600 | 102 | 125 | 1,037 | 55,720 |
| Investments held to maturity | 1,367 | 1,050 | 2,187 | - | - | - | 4,604 |
| Tangible and intangible assets | 166 | 66 | 36 | 105 | 301 | 45,241 | 45,915 |
| Repossessed property | - | - | 11,603 | - | - | - | 11,603 |
| Other assets | 37,403 | 1,877 | 1,231 | 755 | 834 | 1,325 | 43,425 |
| **Total assets** | **531,583** | **234,542** | **363,973** | **116,903** | **84,735** | **315,269** | **1,647,005** |
| **Liabilities** | | | | | | | |
| Deposits from banks | 5 | - | - | - | - | - | 5 |
| Deposits from customers | 386,467 | 119,290 | 429,604 | 108,569 | 38,019 | 62,946 | 1,144,895 |
| Borrowings | 145,440 | 36,911 | 1,558 | 2,047 | 37,667 | 5,540 | 229,163 |
| Other liabilities | 6,123 | 18,259 | 1,852 | 1,349 | 1,082 | 2,351 | 31,016 |
| Provisions for other liabilities | 819 | 269 | 290 | 98 | 29 | 17 | 1,522 |
| | **538,854** | **174,729** | **433,304** | **112,063** | **76,797** | **70,854** | **1,406,601** |
| **Maturity gap** | **(7,271)** | **59,813** | **(69,331)** | **4,840** | **7,938** | **244,415** | **240,404** |

| As at 31 December 2008 | 0- 30 days | 1-3 months | 3-12 months | 1 - 2 years | 2 - 3 years | Over 3 years | Total |
|---|---|---|---|---|---|---|---|
| Total assets | 607,476 | 81,727 | 355,183 | 108,191 | 85,686 | 247,475 | 1,485,739 |
| Total liabilities | 433,177 | 174,425 | 331,688 | 192,164 | 104,766 | 79,004 | 1,315,224 |
| **Maturity gap** | **174,299** | **(92,698)** | **23,495** | **(83,973)** | **(19,080)** | **168,472** | **170,515** |

## 32. Interest rate risk

The Bank is exposed to various risks associated with the effect of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. The following table is the Management's estimate of the interest rate risk for the Bank at 31 December 2009 and 31 December 2008 and is not necessarily indicative of the positions at other times. The table provides some indication of the sensitivity of the Bank's earnings to movements in interest rates. Earnings will also be affected by the currency of the assets and liabilities.

| As at 31 December 2009 | 0 - 30 days | 1-3 months | 3-12 months | 1 - 3 years | Over 3 years | Non-interest bearing | Total |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| Cash and balances with Croatian National Bank | 168,516 | - | - | - | - | 34,522 | 203,038 |
| Placements with other banks | 144,640 | 41,131 | - | - | - | - | 185,771 |
| Assets at fair value through profit or loss | - | 2,580 | - | - | - | - | 2,580 |
| Loans to customers | 1,074,437 | - | - | - | - | - | 1,074,437 |
| Investments available for sale | 78,969 | - | - | - | - | - | 78,969 |
| Investments held to maturity | - | - | - | - | - | 4,604 | 4,604 |
| Repossessed property | - | - | - | - | - | 11,603 | 11,603 |
| Tangible and intangible assets | - | - | - | - | - | 45,915 | 45,915 |
| Other assets | - | - | - | - | - | 40,088 | 40,088 |
| **Total assets** | **1,466,562** | **43,711** | **0** | **0** | **0** | **136,732** | **1,647,005** |
| **Liabilities** | | | | | | | |
| Deposits from banks | - | - | - | - | - | 5 | 5 |
| Deposits from customers | 552,761 | 86,386 | 340,220 | 107,207 | 46,950 | 11,371 | 1,144,895 |
| Borrowings | 193,514 | - | - | - | - | - | 193,514 |
| Provisions for contingent liabilities | 819 | 269 | 290 | 127 | 17 | - | 1,522 |
| Other liabilities | - | - | - | - | - | 31,016 | 31,016 |
| Of which at fixed interest rate | **331,095** | **86,386** | **340,220** | **107,207** | **46,950** | **-** | **911,858** |
| **Total liabilities** | **747,094** | **86,655** | **340,510** | **107,334** | **46,967** | **42,392** | **1,370,952** |

| As at 31 December 2008 | 0 - 30 days | 1-3 months | 3-12 months | 1 - 3 years | Over 3 years | Non-interest bearing | Total |
|---|---|---|---|---|---|---|---|
| Total assets | 1,299,532 | - | - | - | 15,652 | 170,555 | 1,485,739 |
| Total liabilities | 836,615 | 52,385 | 205,612 | 127,521 | 60,697 | 32,394 | 1,315,224 |

**32. Interest rate risk (continued)**

The following table summarizes the effective average interest rate by major currencies for monetary financial instruments as follows:

| | 31.12.2009 | | 31.12.2008 | |
|---|---|---|---|---|
| | HRK % | Foreign currency % | HRK % | Foreign currency % |
| **Assets** | | | | |
| Cash and balances with Croatian National Bank | 0.125 | 0.55 | 0.39 | 0.81 |
| Placements with other banks | 6.26 | 1.11 | 2.5 | 1.43 |
| Assets at fair value through profit or loss | - | 4.625 | 5.35 | 4.625 |
| Loans to customers | 10.83 | 4.29 | 9.4 | 8.59 |
| Investments available for sale | 10.33 | - | 7 | - |
| Investments held to maturity | 10.28 | - | 10 | - |
| Tangible and intangible assets | - | - | - | - |
| Other assets | - | - | - | - |
| Of which at fixed interest rate | 8.63 | 4.625 | 6.07 | 4.625 |
| **Total assets** | 9.59 | 1.20 | 7.45 | 0.87 |
| **Liabilities** | | | | |
| Deposits from banks | - | - | - | - |
| Deposits from customers | 4.07 | 5.21 | 3.78 | 4.47 |
| Borrowings | 3.975 | 2.19 | 3.56 | - |
| Provisions for contingent liabilities | - | - | - | - |
| Other liabilities | - | - | - | - |
| Of which at fixed interest rate | 5.2 | 4.94 | 5.08 | 4.91 |
| **Total liabilities** | 4.05 | 5.04 | 3.76 | 4.47 |

The following table displays sensitivity of interest bearing assets and liabilities on variation of interest rate. For the calculation of the sensitivity of interest rate on profit and loss account of the Bank, the assumption used by the Bank was increase of interest rate by 1% except for cash and balances at Central National Bank. If the interest rates would decrease by the same percentage, the result would be interest income in the same amount.

| | Assumed interest rate growth | Impact on profit and loss account 2009 | Impact on profit and loss account 2008 |
|---|---|---|---|
| **Assets** | | | |
| Cash and balances with Croatian National Bank | -% | - | - |
| Placements with other banks | 1.00% | 1,858 | 2,817 |
| Loans to customers | 1.00% | 10,744 | 8,438 |
| Other assets | -% | - | - |
| **Liabilities** | | | |
| Due to banks | 1.00% | - | - |
| Due to customers | 1.00% | 9,794 | 10,130 |
| Other borrowed funds | 1.00% | 1,935 | 989 |
| **Impact on net interest income** | | **873** | **136** |

## 33. Currency risk

As at 31 December 2009, the Bank had following foreign exchange position:

| | EUR | USD | Other foreign currencies | Total foreign currencies | HRK | Total |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Cash and balances with Croatian National Bank | 20,887 | - | - | 20,887 | 182,151 | 203,038 |
| Placements with other banks | 150,936 | 23,930 | 10,905 | 185,771 | - | 185,771 |
| Assets at fair value through profit or loss | 2,580 | - | - | 2,580 | - | 2,580 |
| Loans to customers | 533,187 | 1,486 | - | 534,673 | 539,764 | 1,074,437 |
| Investments available for sale | 39,359 | - | - | 39,359 | 39,610 | 78,969 |
| Investments held to maturity | - | - | - | - | 4,604 | 4,604 |
| Tangible and intangible assets | - | - | - | - | 45,915 | 45,915 |
| Repossessed property | - | - | - | - | 11,603 | 11,603 |
| Other assets | 5,059 | 9 | - | 5,068 | 35,020 | 40,088 |
| **Total assets** | **752,008** | **25,425** | **10,905** | **788,338** | **858,667** | **1,647,005** |
| **Liabilities** | | | | | | |
| Deposits from banks | 5 | - | - | 5 | - | 5 |
| Deposits from customers | 683,268 | 21,241 | 40,476 | 744,985 | 399,910 | 1,144,895 |
| Borrowings | 48,214 | - | - | 48,214 | 145,299 | 193,513 |
| Other liabilities | 13,642 | 575 | - | 14,217 | 16,799 | 31,016 |
| Provisions for contingent liabilities | - | - | - | - | 1,522 | 1,522 |
| | **745,129** | **21,816** | **40,476** | **807,421** | **563,530** | **1,370,951** |
| **Net foreign exchange position** | **6,879** | **3,609** | **(29,571)** | **(19,083)** | **295,137** | **276,054** |
| Contingent liabilities and commitments | 11,433 | 6,752 | - | 18,184 | 160,820 | 179,004 |

**33. Currency risk (continued)**

As at 31 December 2008, the Bank had following foreign exchange position:

| | EUR | USD | Other foreign currencies | Total foreign currencies | HRK | Total |
|---|---|---|---|---|---|---|
| Total assets | 233,218 | 24,832 | 5,040 | 263,090 | 1,222,649 | 1,485,739 |
| Total liabilities | 417,760 | 26,180 | 10,981 | 454,921 | 860,303 | 1,315,224 |
| **Net foreign exchange position** | **(184,542)** | **(1,348)** | **(5,941)** | **(191,831)** | **362,346** | **170,515** |
| Contingent liabilities and commitments | 15,146 | 10,380 | 285 | 25,811 | 197,953 | 223,764 |

The table below presents the sensitivity of the Bank's net assets and profit or loss to fluctuations in the CNB's middle exchange rate. If the same assumed percent change would be applied to the decrease in the middle exchange rate of the CNB, the impact on profit or loss by individual currency on a net basis would be equal and opposite, that is, the total impact on all currencies would be a charge to the 2009. The result of the exchange rate changes is reflected in the income statement as foreign exchange gains or losses.

| Currency as at 31 December 2009 | Assumed increase of CNB's middle exchange rate | Impact on profit and loss account | Impact on profit and loss account | Impact on profit and loss account |
|---|---|---|---|---|
| | | Assets | Liabilities | Net |
| EUR | 0.41% | 28 | 24 | 4 |
| USD | 2.30% | 6 | 3 | 3 |
| Other currencies | | 2 | 7 | -5 |

| Currency as at 31 December 2008 | Assumed increase of CNB's middle exchange rate | Impact on profit and loss account | Impact on profit and loss account | Impact on profit and loss account |
|---|---|---|---|---|
| | | Assets | Liabilities | Net |
| EUR | 0.34% | 1,804 | 2,097 | (293) |
| USD | 1.86% | 476 | 544 | (68) |
| Other currencies | | 57 | 53 | 4 |

## 34. Fair value of financial assets and liabilities

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Financial instruments designated at fair value through profit or loss and available for sale are measured at fair value. Originated loans and receivables and held to maturity assets are measured at amortized cost less impairment. Management believes that the carrying amounts of these instruments are not significantly different from their fair values.

The following summarizes the major methods and assumptions used in estimating the fair values of financial instruments.

**Loans**

Fair value of loans is calculated based on discounted expected future principal and interest cash flows. Loan repayments are assumed to occur at contractual repayment dates, where applicable. For loans with no fixed repayment dates, repayments are estimated based on experience in previous periods when interest rates were at levels similar to current levels, adjusted for any differences in interest rate outlook. Expected future cash flows are estimated considering credit risk and any indication of impairment. Expected future cash flows for homogeneous categories of loans, such as residential mortgage loans, are estimated on a portfolio basis and discounted at current rates offered for similar loans to new borrowers with similar credit profiles. The estimated fair values of loans reflect changes in credit status since the loans were originated and changes in interest rates in the case of fixed rate loans. As the Bank has a very limited portfolio of loans and advances with fixed rates and longer maturity, the fair values of loans and advances are not significantly different from their carrying amounts.

**Deposits from banks and customers**

For demand deposits and deposits with no defined maturities, fair value is taken to be the amount payable on demand at the balance sheet date. The estimated fair value of fixed-maturity deposits is based on discounted cash flows using rates currently offered for deposits of similar remaining maturities. The length of relationship with depositors is not taken into account in estimating the fair value. As most of the Bank’s deposits are given with variable rate, being market rate, there is no significant difference between the fair value of these deposits and their carrying amount.

**Borrowings**

As majority of the Bank’s borrowings are given with variable interest rate, there is no significant difference between their carrying and fair values.

## 35. Related party transactions

On 8 February 2006, the Croatian National Bank approved the acquisition of the controlling interest in ordinary shares of Kreditna Banka Zagreb d.d., Zagreb (1,190,726 ordinary shares, accounting for 90.21% of the total share capital) by the Agram Group of companies.

Parties are considered to be related if one party has the ability to control the other, or exercise significant influence over the other party in making financial or operational decisions.

At the beginning of the 2009 increase in share capital was made by previous major shareholders.

As at 31 December 2009 and 31 December 2008, the major part of the Bank's share capital is held by Agram Group companies (Euroherc osiguranje d.d., Jadransko osiguranje d.d., Agram životno osiguranje d.d., Euro daus d.d.d i Euroleasing d.o.o.).

In the normal course of business, a number of banking transactions are entered into with related parties and carried out on commercial terms and at market rates. The volumes of related party transactions, outstanding balances at the year-end, and relating expense and income for the year are as follows:

| | Board members | | Related companies | |
|---|---|---|---|---|
| **Transaction type** | **2009** | **2008** | **2009** | **2008** |
| **Loans** | | | | |
| Opening balance | 1,693 | 486 | 25,422 | 65,173 |
| New loans granted | 51 | 1,302 | 161,838 | 257,025 |
| Loans repaid | (90) | (95) | (154,425) | (296,776) |
| **Closing balance** | **1,654** | **1,693** | **32,835** | **25,422** |
| Interest income | 77 | 71 | 4,048 | 10,665 |
| **Loans and deposits received** | | | | |
| Opening balance | 1,610 | 1,636 | 136,905 | 174,776 |
| New deposits and loans received | 578 | - | 348,849 | 399,174 |
| Deposits and loans repaid | 0 | (26) | (384,772) | (437,045) |
| **Closing balance** | **2,188** | **1,610** | **100,982** | **136,905** |
| Interest expense | (21) | (50) | (3,938) | (9,277) |
| Fee and rental income | 1 | 7 | 660 | 4,404 |
| Fee and other expenses | - | - | (10,032) | (11,847) |
| Personnel and fee expenses | (846) | (843) | - | - |
| **Total income** | **78** | **78** | **4,708** | **15,069** |
| **Total expenses** | **(867)** | **(893)** | **(13,970)** | **(21,124)** |
| **Dividends paid** | **-** | **-** | **7,089** | **3,947** |
| **Fee and other receivables** | | | | |
| Interest and fees receivables | - | - | 746 | 1,116 |
| Other receivables | - | - | 7,666 | 14,476 |
| **Liabilities** | | | | |
| Interest payable | - | - | - | 69 |
| Liabilities to suppliers | **-** | **-** | 414 | 110 |
| Liabilities for credit cards operations | **-** | **-** | 586 | - |
| **Off-balance sheet items** | | | | |
| Guarantees issued | - | - | 18,267 | 40,645 |
| Revolving loans | - | - | 2,276 | 1,623 |

**35. Related party transactions (continued)**

In the year 2009, remunerations to the Supervisory Board members amounted to HRK 486 thousand (2008.: HRK 486 thousand).

**36. Contracted liabilities for operating lease of vehicles and equipment**

As at 31 December 2009 the Bank has 74 operating lease agreements for vehicles and equipments. Contracted annual operating lease liabilities are as follows:

| | 2009 | 2008 |
|---|---|---|
| Within a year | 2,962 | 3,415 |
| From two to five years | 6,005 | 9,731 |
| | **8,967** | **13,146** |

**37. Contracted liabilities for business premises leases**

As at 31 December 2009 the Bank has 16 lease agreements for business premises. Contracted annual lease liabilities for business premises are as follows:

| | 2009 | 2008 |
|---|---|---|
| Within a year | 6,361 | 2,634 |
| From two to five years | 25,043 | 10,536 |
| From five to ten years | 31,255 | 13,170 |
| | **62,659** | **26,340** |

## 38. Approval of financial statements

The financial statements as shown on pages 4 to 57 were approved and signed by the Management Board on 16 April 2010.

**Signed by the Management Board:**

President

Nelsi Rončević

Vice president

Ivan Dropulić