HBOR

Annual Report

Contents:

LETTER OF THE PRESIDENT OF THE SUPERVISORY BOARD

Ladies and Gentlemen,

In 2010, the Government of the Republic of Croatia continued to implement measures for the maintenance of macroeconomic stability and the creation of preconditions for recovery and stable economic growth. Therefore, in January 2010, the Government made the Decision on Measures for Economic Recovery and Development – finance models. The main purpose of the adopted measures is to create conditions for sustainable economic growth in the long term with a focus on the maintenance of existing and creation of new jobs, boosting investment, ensuring a satisfactory level of liquidity of the Croatian economy and other conditions that enable preservation of a stable macroeconomic framework. As a result, in the reporting year, two new models of financing were launched with the support from the Government of the Republic of Croatia within the framework of the economic recovery programme. They are implemented through Hrvatska banka za obnovu i razvitak with an objective of improving the availability of liquid assets for the economy under favourable terms and conditions: the model for the financing of sustainable economic projects with an active participation of the state in co-financing banks' loan placements (Model A) and the model for the financing of sustainable economic projects through the guarantee fund for economic recovery and development by covering a portion of risk associated with bank loan placements (Model B). Through the Loan Programme for the Financing of Working Capital (Model A), whose goal is to increase the competitiveness of Croatian entrepreneurs, i.e. reach, maintain and improve liquidity as well as maintain and expand the existing businesses, HBOR and commercial banks approved to Croatian entrepreneurs altogether 589 loans totalling HRK 2.5 billion in 2010. In order to continue the implementation of the measures for economic recovery and development, the Government of the Republic of Croatia adopted, in January 2011, the decision on a new loan programme: Model A+. In the same month, the Parliament of the Republic of Croatia passed the Act on the Guarantee Fund for Economic Recovery and Development. The Croatian Government will continue with its efforts to create preconditions for economic recovery and sustainable development, and HBOR will, as a state development bank, play an active role in the implementation of these measures.

In addition to the aforementioned models, in 2010, HBOR launched three further loan programmes using its own funds in its endeavours to follow the needs of Croatian entrepreneurs. In the reporting year, Croatian entrepreneurs demonstrated a considerable interest in HBOR's loans, which is evidenced by 1,606 committed ones, an increase of 33.6 percent compared with 2009. The implementation of the Model A and three new loan programmes contributed significantly to this increase in the number of loans approved.

In the past year, HBOR raised EUR 384 million through special financial institutions and additional HRK 2 billion in co-operation with the Croatian commercial banks. It is particularly important to stress the fact that the funds were raised at the same terms and conditions that had been applied before the outbreak of the global economic and financial crisis, which enabled HBOR to keep its interest rates at the previous year's level. Such accomplishments in the international financial market confirm, from year to year, HBOR's strong reputation in financial circles.

On behalf of the Supervisory Board, I would like to express my satisfaction with the operations of HBOR in 2010. I am confident that the Bank will continue to successfully implement its loan programmes with an objective of promoting the sustainable development of the Croatian economy.

Martina Dalić
President of the Supervisory Board

LETTER OF THE PRESIDENT OF THE MANAGING BOARD

Ladies and Gentlemen,

Even though 2010 was a difficult and challenging year, the operations of Hrvatska banka za obnovu i razvitak can be assessed as successful. In times of economic crisis and overall liquidity problems, HBOR managed to prove its strength again as an institution recognised in international markets and succeeded in raising sufficient funds as a result of good co-operation with special financial institutions, thus ensuring favourable terms and conditions of loans for Croatian businessmen. In addition, as a development financial institution and the promoter of economic recovery of the Republic of Croatia, HBOR retained the interest rates charged on its loans on the level that had not been changed for years with an objective of providing entrepreneurs as reliable financial support as possible.

In 2010, HBOR increased its lending activity compared with the previous year. Altogether 1,606 loans were approved in a total amount of six billion six hundred million kuna, an increase of 7.5 percent compared with the previous year. Rising lending activity is a result of the implementation of the Loan Programme for the Financing of Working Capital and the programme for the issuing of guarantees for and on behalf of the Republic of Croatia with the purpose of covering part of the risk of banks' loan placements as well as of the successful borrowing of EUR 384 million from the European Investment Bank (EIB), German development bank (KfW) and the Council of Europe Development Bank (CEB) at terms and conditions that remained on the same level as those before the outbreak of the global economic and financial crisis. This made it possible for HBOR to keep most of its interest rates within the range of 2 to 6 percent p.a. like in previous years.

In the reporting period, most of the funds were extended for the financing of exports, of which almost three billion kuna for pre- and post-shipment export finance. For the financing of SMEs, 447 loans were approved totalling more than one billion kuna. In the field of export credit insurance, transactions worth more than two billion kuna were insured.
The fact that more than 78 percent of funds were approved for the purpose of financing working capital evidences difficulties confronting the economy in 2010. On the other hand, an increase of approximately 25 percent in the number of loans approved for investment purposes is encouraging. However, their total amount remained approximately on the previous year's level. Based on these data, it can be concluded that a mild recovery of investment climate has occurred as illustrated by an increasing number of small-scale investments.

In 2010, HBOR introduced five new loan programmes with an objective of adjusting its operations to the needs of Croatian businessmen and facilitating their access to funding: Programme for Micro, Small and Medium-Sized Enterprises (Loan Programme for the Development of Small and Medium-Sized Enterprises with EU Support), IPARD – Development of Rural Infrastructure (Loan Programme for IPARD Measure 301 Candidate Projects), IPARD – Development of Rural Economic Activities (Loan Programme for IPARD Measure 302 Candidate Projects), Working Capital (Model A) and Guarantees in Support of Measures for Economic Recovery and Development (Model B).

In July 2010, a new company Hrvatsko kreditno osiguranje d.d. started its operations as the only insurance company specialised in providing insurance for short-term receivables among business entities. By the end of the year, the Company entered into insurance contracts with 26 insured parties providing cover for the risks of receivables with respect to buyers in 42 countries.

Throughout the year, HBOR hosted significant international expert conferences. In March, HBOR organised the Conference on Micro-Lending under the auspices of the German development bank (KfW) gathering more than three hundred participants. The main topic of the Conference was the promotion of support to small companies and crafts businesses through micro-lending projects. In September, HBOR organised its ninth International Conference on Export Promotion. In the same month, HBOR organised and hosted the autumn meeting of the Prague Club for the second time gathering approximately sixty representatives of export–credit agencies. In October, HBOR received the representatives of Croatian innovators, who won innovator awards at the London Innovation Show, and introduced its programmes for the promotion of innovative entrepreneurship.

HBOR has been a member of the European Association of Public Banks only since 2007, and the election of myself as President of the EAPB in December 2010 is a major recognition of HBOR, its employees and the Republic of Croatia that was thus given an active role in European financial circles even before its formal accession to the European Union. The task of the President of the EAPB during the two-year term of office is to represent the interests of the Association and its members before EU bodies.

I would like now to thank all the employees of HBOR for their devoted work and efforts aimed at achieving good business results. I also thank the Members of the Croatian Parliament, the Croatian Government and the Members of the Supervisory Board for their continued support. In 2011, Hrvatska banka za obnovu i razvitak will continue to implement its existing programmes and to improve and introduce new ones in accordance with the needs of our entrepreneurs aiming to contribute to the faster recovery of the Croatian economy.

Anton Kovačev
President of the Managing Board

HBOR

HRVATSKA BANKA ZA OBNOVU I RAZVITAK

STATEMENT OF PERSONS RESPONSIBLE FOR THE PREPARATION OF THE ANNUAL REPORT

To the best of our knowledge, the 2010 Annual Report includes a fair review of the development, operating results and position of Hrvatska banka za obnovu i razvitak and the Group as well as a description of the principal risks and uncertainties to which Hrvatska banka za obnovu i razvitak and the Group are exposed.

Anton Kovačev	Mladen Kober
President of the Managing Board	Member of the Managing Board

Zagreb, 31st March 2011

INTRODUCTION

The Annual Report includes the summary of financial information, description of operations and audited Annual Financial Statements with the independent auditor's report for the year ended 31st December 2010.

Legal status
The Annual Report includes annual financial statements prepared in accordance with the International Financial Reporting Standards and the Accounting Act and audited in accordance with the International Standards on Auditing.

Exchange rate
For the purpose of translating amounts in foreign currencies into HRK, the following exchange rates of the Croatian National Bank have been applied:

31st December 2010	EUR 1 = HRK 7.385173	USD 1 = HRK 5.568252
31st December 2009	EUR 1 = HRK 7.306199	USD 1 = HRK 5.089300

ABBREVIATIONS

AZTN	Agencija za zaštitu tržišnog natjecanja (Croatian Competition Agency)
CEB	Council of Europe Development Bank
DEG	Deutsche Investitions- und Entwicklungsgesellschaft
EAPB	European Association of Public Banks
EIB	European Investment Bank
EIF	European Investment Fund
EUR	Euro
HAMAG	Hrvatska agencija za malo gospodarstvo (Croatian Agency for Small Business)
HNB	Hrvatska narodna banka (Croatian National Bank)
HOK	Hrvatska obrtnička komora (Croatian Chamber of Trades and Crafts)
KfW	Kreditanstalt für Wiederaufbau
KN	Croatian kuna
SME	Small and medium-sized enterprise
NEFI	Network of European Financial Institutions for SMEs
OeKB	Oesterreichische Kontrollbank AG

In the Annual Report, Hrvatska banka za obnovu i razvitak is referred to as HBOR and/or the Bank, and the Hrvatska banka za obnovu i razvitak Group as HBOR Group or the Group.

GENERAL INFORMATION

Establishment

HBOR was established on 12th June 1992 by the Act on Hrvatska kreditna banka za obnovu (HKBO). The Bank was renamed Hrvatska banka za obnovu i razvitak by changes and amendments to the above Act in December 1995. In December 2006, the Croatian Parliament passed a new Act on HBOR, which came into force on 28th December 2006. HBOR is the parent company of the Hrvatska banka za obnovu i razvitak Group that was formed in 2010. The subsidiary companies are Hrvatsko kreditno osiguranje d.d. (HKO d.d.) and Poslovni info servis d.o.o. (PIS d.o.o.) that constitute the Hrvatsko kreditno osiguranje Group (HKO Group).

Strategic goals of the Bank
In its operations, HBOR promotes, within the framework of its powers and authorisations, systematic, sustainable and balanced economic and social development pursuant to the overall strategic goals of the Republic of Croatia.

Main activities
- Financing the reconstruction and development of the Croatian economy
- Financing infrastructure
- Promoting exports
- Promoting SMEs
- Environmental protection, energy efficiency and renewable energy resources
- Export credit insurance of Croatian goods and services against non-market risks

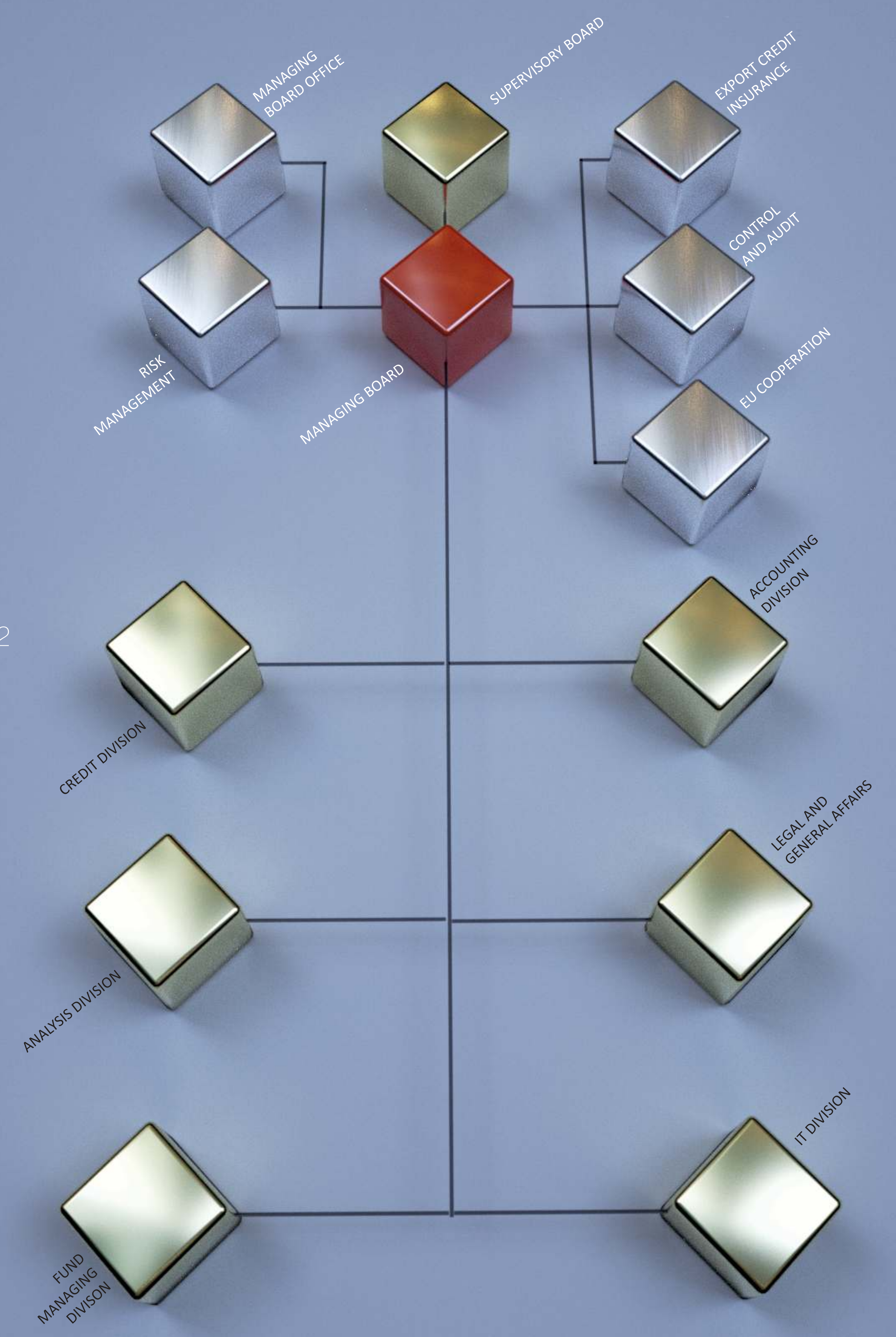
Audit
HBOR's separate and consolidated annual financial statements for 2010 were audited by the auditing firm Deloitte d.o.o., which expressed its unqualified opinion as an independent auditor.

Credit rating
- Baa3 by Moody's
- BBB - by Standard & Poor's

Regional offices
- Regional office for Slavonia and Baranja
- Regional office for Dalmatia
- Regional office for Istria
- Regional office for Lika
- Regional office for Primorje and Gorski Kotar

Number of employees
On 31st December 2010, there were 244 employees in HBOR.
On 31st December 2010, there were 253 employees in HBOR Group.

ORGANISATION STRUCTURE



CORPORATE GOVERNANCE

HBOR continuously monitors best practice in the field of corporate governance and integrates corporate governance principles in its operations pursuant to sound banking practices.

Corporate governance principles are implemented by HBOR through:

- **Principle of public operations**
  - Annual Financial Statements of HBOR on unconsolidated and consolidated basis are confirmed by the Supervisory Board and submitted to the Croatian Parliament for approval
  - Financial Statements of the Bank and the Group are regularly published on the web sites of the Ministry of Finance, the Zagreb Stock Exchange and HBOR
  - The rating of the Bank is issued by two international independent rating agencies on an annual basis (Standard & Poor's, Moody's)
  - Pursuant to the Access to Information Act, reports on received requests for information about the operations of the Bank are submitted to the Central State Office for Administration on an annual basis

- **Supervisory Board of HBOR, powers and composition**
  - The Supervisory Board determines the principles of operating policy and strategy, supervises the business activities of the Bank, adopts HBOR's lending policies, adopts the Annual Financial Statements, considers Internal Audit reports and reports drafted by external independent auditors and by the State Audit Office
  - The Supervisory Board monitors and controls the legality of the business activities of the Managing Board, and appoints and dismisses the President and the members of the Managing Board
  - The Supervisory Board consists of nine members: five Government ministers, three Members of Parliament and the President of the Croatian Chamber of Economy
  - The Supervisory Board has established the Audit Committee in accordance with the Audit Act

- **Managing Board of HBOR, powers and composition**
  - The Managing Board represents HBOR, conducts the Bank's business and administers its assets; it is obliged and authorised to undertake all actions and pass all resolutions it considers necessary for the legal and successful conduct of business
  - Powers of the Managing Board: managing and conducting the business of HBOR, adopting normative acts that determine the manner of operations and the internal organisation of HBOR, adopting loan programmes, making individual loan approval decisions and decisions on other financial transactions, making decisions on the appointment and dismissal of employees with special powers, making decisions on the rights and obligations of employees and reporting to the Supervisory Board
  - The Managing Board consists of three members appointed by the Supervisory Board, one of whom is appointed President; the President and the members of the Managing Board are appointed for a five-year term of office and may be reappointed thereafter; HBOR is represented by the Managing Board jointly by two of its members
  - For the purpose of ensuring efficient and effective risk management procedures and minimising the risk, the following bodies have been established with the Managing Board: Asset and Liability Management Committee, Credit Committee, Credit Risk Assessment and Measurement Committee and IT System Management Committee

- **Internal control system**
  - In order to ensure permanent monitoring, measuring, assessment and management of all risks HBOR is exposed to within the framework of its operations, an independent organisational unit for risk management has been established
  - HBOR's Internal Audit, as an independent organisation unit, is in charge of verifying the adequacy of risk management procedures and the internal control system, including risk monitoring, compatibility with regulations and the code of professional conduct, and implementing internal policies and Bank procedures as well as anti-money laundering activities
  - For the purpose of harmonising operations with the regulations of the EU, an organisation unit of EU Co-operation has been established within HBOR whose main task is the adjustment of HBOR's operations to the acquis communautaire of the EU

- **Co-operation between the Managing Board and the Supervisory Board of HBOR**
  - The Managing Board and the Supervisory Board successfully co-operate through open discussions; the timely submission of thorough written reports to the Supervisory Board represents the basis for this co-operation
  - The Act on HBOR, the By-laws of HBOR and decisions made by the Supervisory Board determine the activities that HBOR may perform only with prior consent of the Supervisory Board

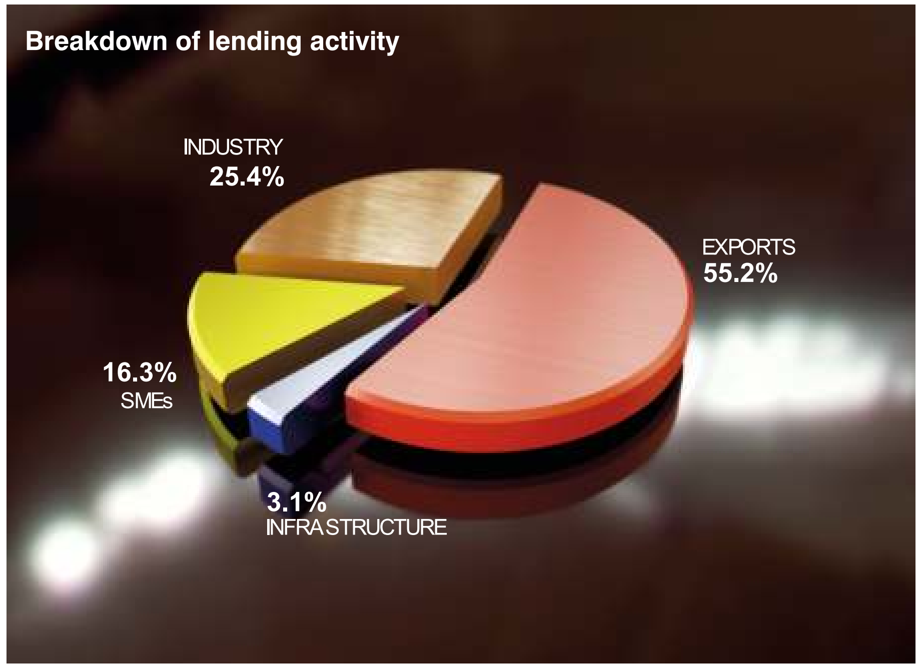
BUSINESS ACTIVITIES IN 2010

In 2010, HBOR approved 1,606 loans totalling HRK 6.62 billion, an increase of 7.5% compared with the previous year.
Most of the funds were extended for the financing of exports, of which almost HRK 3 billion for pre- and post-shipment export finance. For the financing of SMEs, 447 loans were approved totalling HRK 1.1 billion, an increase of 12% compared with 2009. These data relate to special loan programmes intended for SMEs. HBOR currently implements 24 loan programmes, of which 11 exclusively in support of small and medium-sized enterprises. Significant results were achieved also under export credit insurance programmes. In the reporting period, HBOR insured HRK 2.14 billion of export transactions.
In January 2010, the Government of the Republic of Croatia made the Decision on Measures for Economic Recovery and Development, in the implementation of which HBOR has played a significant role. Within the framework of these measures, HBOR has implemented the programme for the financing of working capital and the issuing of guarantees for and on behalf of the Republic of Croatia intended for the coverage of a portion of risk associated with bank loan placements. Both models have been implemented through auctions in which commercial banks participate.

Also in 2010, HBOR made efforts to raise funds from special financial institutions under as favourable terms and conditions as possible in order to provide quality financial support to the Croatian economy. The funds were raised from EIB, KfW and CEB. It is important to point out that the terms and conditions of HBOR's borrowings from these international financial institutions remained on the same level as those before the outbreak of the global financial crisis, which made it possible for HBOR to retain the same level of interest rates for final borrowers. In addition, HBOR entered into a club loan agreement with Croatian commercial banks for the financing of the measures for economic recovery and development introduced by the Government of the Republic of Croatia, i.e. the Model A.

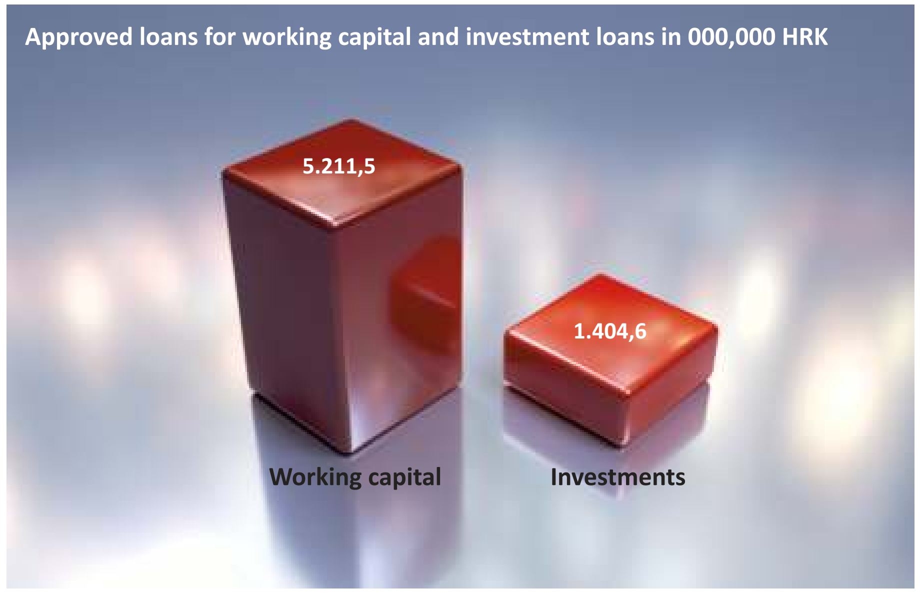
OVERVIEW OF LENDING ACTIVITY OF HBOR IN 2010

No.		APPROVED HRK	LOANS
1.	INDUSTRY	1,680,424,508.02	648
2.	EXPORTS	3,650,169,389.07	493
3.	INFRASTRUCTURE	206,383,952.07	18
4.	SMEs	1,079,131,670.59	447
	TOTAL	**6,616,109,519.75**	**1,606**



Within the framework of its business activities, HBOR is primarily orientated towards the long-term financing of investments targeted at raising the level of manufacturing activities, exports, employment and market competitiveness of the Croatian economy. Currently, 24 loan programmes are implemented in support of Croatian entrepreneurs, of which 17 programmes are focusing on long-term investments and 7 on working capital investments.

The consequences of the financial and economic crisis were reflected in the reduced capacity of entrepreneurs for new investments and the increased demand for quality sources of funding needed for the maintenance of current liquidity. In order to overcome the difficulties in the economy, preserve the operations of Croatian entrepreneurs and the existing jobs in the period of economic and financial crisis, HBOR directed, just like other development banks in the region, most of its loans in 2010 at the financing of working capital, thus contributing to the overcoming of liquidity problems.



More than 78% of funds were approved for the financing of crafts businesses. The number of loans approved for investments rose by about 25%, whereas the amount of loans approved remained approximately on the previous year's level. Based on these data, it can be concluded that a mild recovery of investment climate has occurred as illustrated by an increasing number of small-scale investments.

NEW LOAN PROGRAMMES

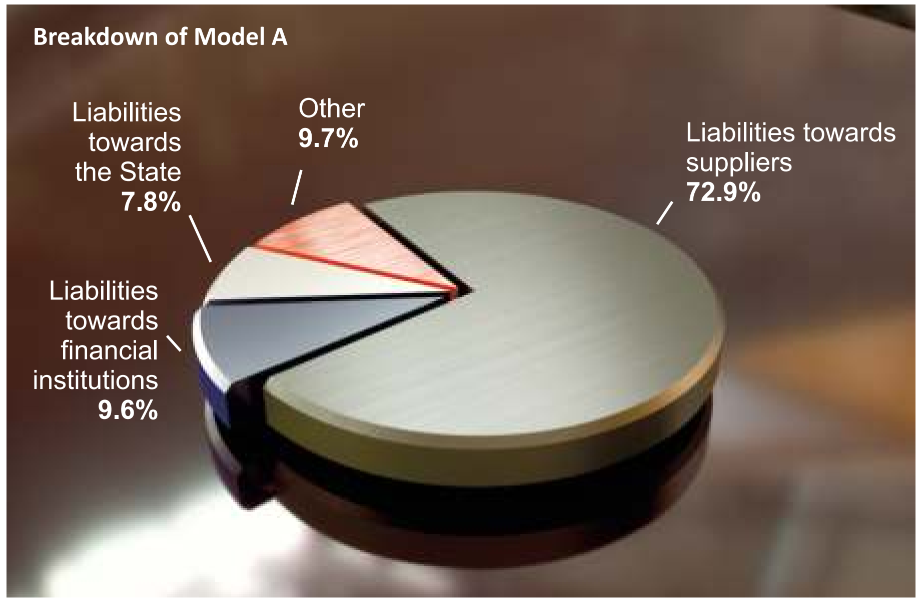
In its efforts to adapt to the requirements of Croatian businessmen, HBOR regularly monitors their needs, changes the terms and conditions of the existing loan programmes and introduces new products with an objective of promoting the development of entrepreneurship. As a result of such business practice, 5 new programmes were introduced in 2010.

Programme for Micro, Small and Medium-Sized Enterprises (Loan Programme for the Development of Small and Medium-Sized Enterprises with EU Support)
– goal: financing of micro, small and medium-sized enterprises for the purpose of self-employment, establishment of crafts businesses or companies, modernisation or expansion of existing operations, increasing the number of new jobs
The Programme has been prepared and is implemented in co-operation with KfW, CEB and the European Commission within the framework of the Small and Medium-Sized Enterprise Finance Facility (SMEFF), Phase 2.
In 2010, 108 loans were approved totalling HRK 34.6 million.

IPARD – Development of Rural Infrastructure (Loan Programme for IPARD Measure 301 Candidate Projects)
– goal: financing of projects implemented by local government units (municipalities and cities of up to 10,000 inhabitants) nominated for the co-financing from the funds of Component V of the Instrument for Pre-accession Assistance (IPA) – Rural Development – the so called IPARD Programme, Measure 301
Investments eligible for financing: investments in the sector of sewerage and wastewater treatment systems, investments in the sector of local unclassified roads, investments in the sector of heating plants, investments in the sector of firebreaks with elements of forest roads.

IPARD – Development of Rural Economic Activities (Loan Programme for IPARD Measure 302 Candidate Projects)
– goal: financing of candidate projects implemented by natural persons and legal entities (classified into the category of micro entities within the VAT system) to be nominated for the co-financing from the funds of Component V of the Instrument for Pre-Accession Assistance (IPA) – Rural Development – the so-called IPARD Programme, Measure 302
Investments eligible for financing: investments in the sector of rural tourism, traditional crafts, direct sale, freshwater fishery, services, onsite processing at farms, mushroom production and renewable energy resources.

Working capital (Model A)
– goal: increasing the competitiveness of Croatian entrepreneurs, reaching, maintaining and improving their liquidity as well as maintaining and expanding the existing businesses
The Loan Programme for the Financing of Working Capital (Model A) has been implemented in accordance with the Decision on Measures for Economic Recovery and Development made by the Government of the Republic of Croatia in co-operation with commercial banks (funds were provided by a commercial bank and HBOR in the proportion of 60% : 40%) since January 2010.
In 2010, HBOR and commercial banks approved to Croatian entrepreneurs altogether 589 loans totalling HRK 2.5 billion.



Guarantees in support of Measures for Economic Recovery and Development (Model B)
– goal: launching of investment projects supported by the establishment of a guarantee fund of the Republic of Croatia intended for the coverage of a portion of risk associated with new loan placements
Within the framework of Model B, the guarantees are issued by HBOR for and on behalf of the Republic of Croatia. In 2010, 1 guarantee was approved in the amount of HRK 15.0 million.

EXPORT PROMOTION

In addition to its role as a development bank, HBOR has been, for a number of years now, successfully performing the role of an export bank and an export credit agency through the system of financing and insuring export transactions and issuing demand guarantees on exporters' orders. Such a system provides Croatian exporters with equal competitive conditions in international markets. HBOR supports exporters in all segments – from pre-shipment export finance to the collection of payment for an export transaction.

Export finance

In 2010, through the pre-shipment export finance programme, 406 loans were approved totalling HRK 2.99 billion. The highest loan amounts under the above programme were committed for the benefit of the following industries: food processing (18.6%), chemicals and chemical products (9.9%), final metal products except machines and devices (7.2%), processing of wood and production of wood and cork products (6.2%).
In the reporting period, HBOR granted loans to exporters also under the programme Exports – IBRD, through which 36 loans were approved totalling HRK 417.7 million.
Through the programme for issuing demand guarantees at the request of an exporter, HBOR provides support for Croatian exporters when they enter into an export contract and complete an export transaction. In 2010, HBOR issued guarantees in the amount of HRK 4.3 million. The objective of the Programme is to issue bank guarantees for exporters participating in international tenders and entering into contracts for the purpose of exporting goods, works and services.
HBOR is implementing programmes for export promotion with an intention of increasing competitiveness and value of Croatian exports as well as improving recognisability and quality of Croatian products and services in the world market.

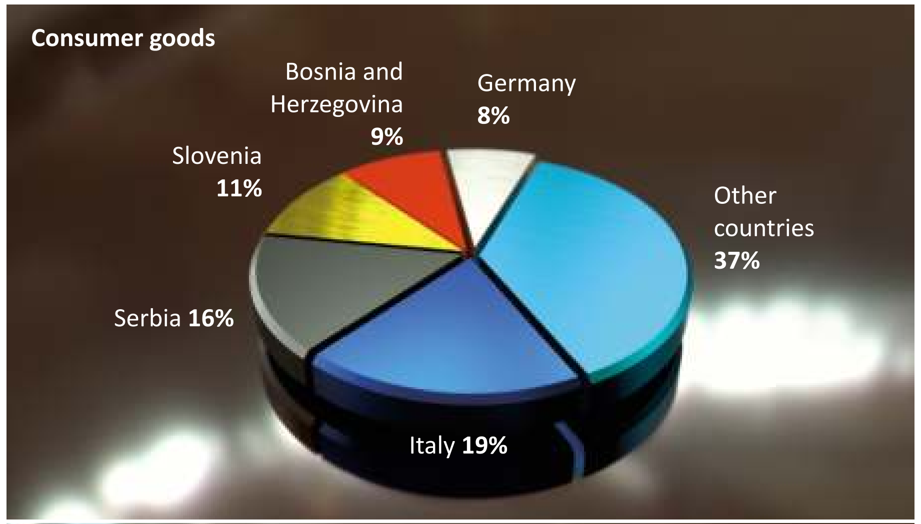
Export credit insurance and reinsurance

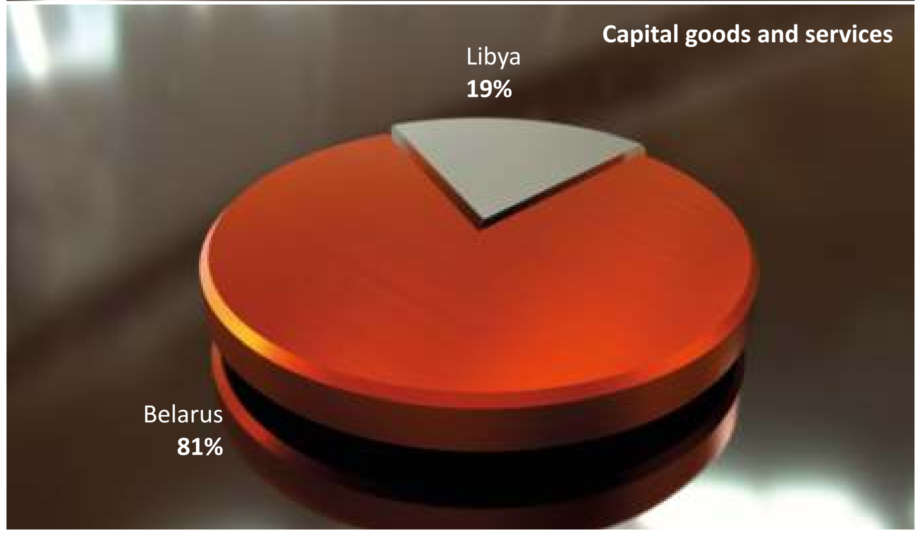
Export credit insurance programmes provide a comprehensive service to exporters and financial institutions covering commercial and political risks in all phases of an export transaction – from pre-shipment export finance to the collection of payment for an export transaction.

In order to provide comprehensive services, HBOR co-operates closely with other insurance providers, in particular with other national export-credit agencies, which is a prerequisite for covering larger joint project in the third market.

In 2010, although the prominent feature was still the negative influence of the global financial crisis, HBOR made to Croatian exporters new cover approvals for export transactions in the amount of HRK 968.7 million. For insurance and reinsurance of exports of consumer goods the amount of HRK 839.75 million was approved, for insurance of exports of capital goods and services the amount of HRK 118.49 million was approved and for insurance of pre-shipment export finance the amount of HRK 10.5 million was approved. By means of insurance and reinsurance, support was provided for the export of Croatian goods and services to 51 countries of the world and for 1202 customers. The most important insured export markets are Italy, Serbia, Belarus, Slovenia and Bosnia and Herzegovina. Total insured export turnover in 2010 amounted to 2.15 billion which represents a decrease of 12.5% compared to the year 2009. The decrease in insured transactions was affected by the separation of activities for and on behalf of the state (marketable risks) from operations on a commercial basis, as a result of which, marketable risks were insured by a private credit insurance company, majority-owned by HBOR. In 2010, the total collected premiums amounted to HRK 10.95 million, which represents an increase of 5% compared to the previous year.

BREAKDOWN OF AMOUNTS INSURED IN 2010 BY COUNTRY AND TYPE OF GOODS





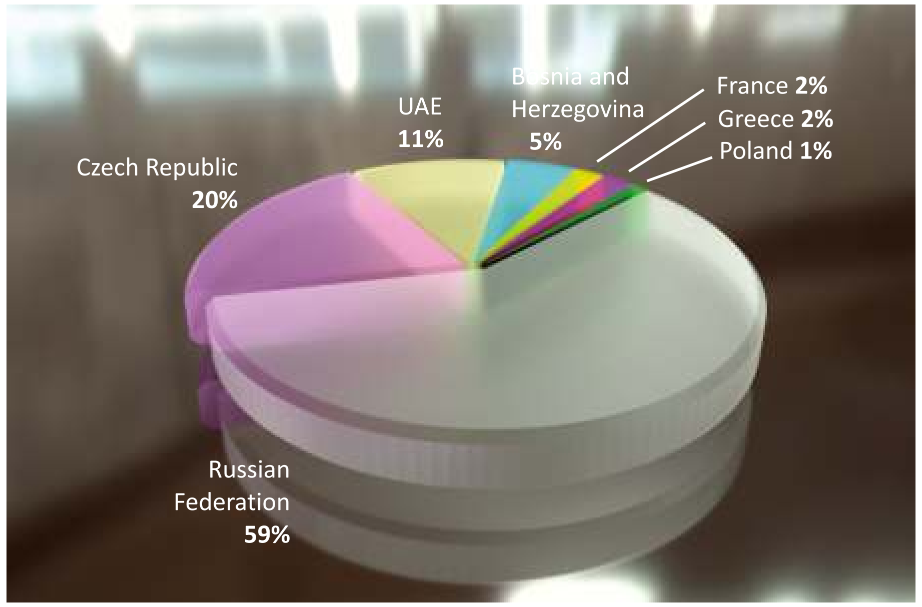
Within the framework of medium/long-term insurance programmes, HRK 118.5 million were insured during 2010 and particularly prominent were the following projects:

- Shipment of telecommunication equipment to Belarus – value of the insured export contract amounted to USD 17.3 million
- Seismic exploration in Libya – value of the insured export contract amounted to EUR 3 million
- Production of machinery for mines in the Republic of South Africa – value of the insured export contract amounted to HRK 10.5 million

Likewise, in order to enable Croatian exporters to participate in international tendering procedures, letters of intent were issued for the following projects:
- Construction of a hydro power-plant on Island
- Construction of a substation with cable mains in Belarus
- Rehabilitation of „Rama“ hydro power-plant in Bosnia and Herzegovina

The total value of 7 indemnities paid in 2010, amounted to HRK 1.83 million, which represented a decrease of 32.6% compared to the year 2009. All indemnities were paid to the exporters of consumer goods and the largest individual indemnities were paid because of prolonged non-payment of buyers from Russia, the Czech Republic and the United Arab Emirates. By number of indemnities paid in 2010, metal and non-metal industry accounted for the largest portion, 29%.

BREAKDOWN OF INDEMNITIES BY COUNTRY



FUND RAISING

During 2010, HBOR raised EUR 384 million through special financial institutions, and additional HRK 2 billion in co-operation with Croatian commercial banks.
In February 2010, HBOR signed a loan agreement with the Council of Europe Development Bank in the amount of EUR 50 million for financing of small and medium-sized enterprises.
In April 2010, HBOR signed a loan agreement with the European Investment Bank amounting to EUR 250 million for financing of small and medium-sized enterprises, medium-capitalized companies (the so-called Mid Cap companies), environmental projects and infrastructure projects in public and private sector, and a loan agreement amounting to EUR 34 million for financing the project for the construction of VCM and PVC plants with Dina Petrokemija d.d. Omisalj as investor.
In June 2010, HBOR signed a loan agreement with KfW amounting to EUR 30 million for financing tourism projects, and a loan agreement amounting to EUR 20 million for financing of small and medium-sized enterprises with the support of the European Union within the framework of the European Commission programme for financing small and medium-sized enterprises (SME Finance Facility)

RISK MANAGEMENT

Pursuant to the HBOR Act, the Bank is obliged to reduce the risk in its operations to the lowest level possible by applying the principles of banking operations. In the risk management process, the Bank continuously performs control, identification, assessment, measurement and supervision of all risks it is exposed to in its operation. The manner, actions and frequency of measurement and assessment of risk management are prescribed by the bank's general documents. In its day-to-day operations, the bank manages credit risk, market risk and operational risk through appropriate policies, procedures, limits, committees and controls.

The Bank has a functionally and organisationally separate and independent organisational unit for the control of business risks which is directly responsible to the Managing Board. The Risk Management Unit is responsible for the control, identification, assessment, measurement and supervision of all risks the bank is exposed to or might be exposed to in its operations. The Risk Management Unit performs its role by analysing, evaluating, measuring and giving suggestions and recommendations for adequate management of the bank's exposure to credit and non-credit risks, developing risk-related procedures and methodology, recommending and monitoring the adherence to exposure limits, reporting to the Managing Board and other committees on risks, etc.
For risk evaluation and measurement, the Bank takes notice of historical data, business plans, market conditions and the specific characteristics of the bank as a special financial institution. The results of measurement/assessment and analysis conducted in the field of risk are exhibited at the meetings of risk management committee, Management Board and the Supervisory Board. For risk monitoring and control, a system of limits is established for the purpose of managing credit risk, liquidity risk, interest rate risk and currency risk. The Bank monitors risks by means of scenario analysis, sensitivity analysis and stress testing. Systems of pro-active risk management are developed for the purpose of preventing potential risks.
The Managing Board of HBOR is responsible for establishing and implementing an effective and reliable risk management system. For the purpose of accomplishing its function, the Managing Board has delegated its authority to two risk management committees:
The Assets and Liabilities Management Committee manages liquidity risk, interest rate risk and currency risk within the framework of the prescribed policies and procedures regulating this area.
The Credit Risk Evaluation and Measurement Committee manages credit risk within the limits set through the policies, procedures and other internal documents related to credit risk.
HBOR's IT System Management Committee manages the resources of IT system with adequate management of risks arising from utilisation of IT.
The risk management strategy is directed towards achieving and maintaining good and efficient system of risk management in line with local and international banking practices and recommendations of the Croatian National Bank and the Basel Committee.

Credit risk

Credit risk encompasses loss derived from full or partial default, i.e. untimely discharge of a financial obligation by the client.
The Bank controls credit risk by way of credit policies and prescribed procedures which determine internal control systems aiming to act preventively.

The HBOR Managing Board conducts a conservative credit risk policy. The credit risk management system forms a crucial part of HBOR business policy and it is an important strategic factor, and therefore this area is regulated by separate Credit Risk Management Procedures, applied in all phases of the credit process (from development of a new banking product, credit application to the final repayment). Credit Risk Management Procedures represent a comprehensive document comprised of separate methodologies aimed at evaluating the various client target groups.
In order to mitigate credit risk and reduce operating costs, the Bank, in accordance with the HBOR Act, on-lends a part of its placements via commercial banks which assume the risk of collecting repayments from final borrowers. All direct placements are secured by mortgages on immovable property, and, if possible, for the purpose of providing security against credit risk, the Bank requires guarantees issued by the Croatian Agency for Small Business and other first-class guarantees. The Bank determines the required ratio between the placement value and insurance coverage according to the type of collateral, the loan programme, the general terms and conditions of insurance and the decision of the body in charge.
The Bank's developmental loan programmes cover the entire territory of the Republic of Croatia with a focus on the areas of special state concern. Credit risk is diversified by geographical region and developmental loan programme. By creating new loan programmes (products), the Bank aims at preventing the excessive concentration of credit risk and enabling the balanced development of all geographical regions in the Republic of Croatia in accordance with the state development strategy for individual occupations.

Market risk

The bank ensures quality management of liquidity, currency and interest rate risks through the Assets and Liabilities Management Committee. Management of those risks implies minimising interest rate risk, currency risk and liquidity risk. All organisational units are included in the Committee's operation in order to ensure a high-quality, integrated and comprehensive risk management system.

Liquidity risk

Liquidity risk is a risk of financial policies and loss that occurs if the bank is unable to meet its due liabilities. The basic principles for managing HBOR's liquidity are defined by the Liquidity Risk Management Procedures and the decisions made by the Supervisory Board, the Managing Board and the Assets and Liabilities Management Committee.
For the purpose of managing liquidity risk, the Bank maintains the necessary level of liquidity reserves, continuously monitors day-to-day liquidity, and provides sufficient kuna and foreign currency funds necessary for timely settlement of obligations and disbursements under committed loans and planned commitments. The current surplus of available funds is invested in liquidity management instruments in line with Liquidity Risk Management Procedures. In terms of long-term liquidity management, the Bank monitors and strives to achieve the maximum compatibility of sources and placements according to maturity. The Bank monitors liquidity risk through scenario analysis, sensitivity analysis and stress testing. In this way both cases of ordinary business operations as well as operations in terms of stress are included. Signals of early warning and procedures in case of indication and the occurrence of liquidity crisis are identified.
The Bank has prescribed limits for managing liquidity with commercial banks.
In its portfolio, HBOR does not hold financial instruments intended for trading purposes.
HBOR, as a special financial institution, is not profit oriented and does not trade in derivatives. Derivatives may only be used for the protection of its own position.

Interest rate risk

Interest rate risk is the financial risk that occurs due to interest rate mismatches in the value and maturity of interest-sensitive assets, liabilities and off-balance sheet positions. The basic concepts and principles of the Bank's interest rate risk management are established in the Procedures for interest rate risk management, which came into force in the reporting year and the decisions and conclusions of the Managing Board and the Asset and Liability Management Committee. For the purpose of measuring and monitoring interest rate risk, the Bank implements the interest rate gap analysis. The interest rate gap is analysed by specific periods on the basis of possibility of change in interest rates (fixed and variable) and illustrates the sensitivity of the Bank to such changes in interest rates. Detailed elaboration of interest rates per currency, type and value of interest rate and projections of movements of average weighted interest rates on assets and liabilities are also made. Depending on the level of the interest rate gap, the type of interest rates on future borrowings and placements is determined in order to reduce the gap to the lowest possible level. Besides matching interest rates on assets and liabilities, current market conditions and movements in forecasted market indicators are also monitored.

Currency risk

Currency risk is the exposure of a bank to foreign exchange gains/losses and arises primarily from the currency mismatch of assets and liabilities, which may result in costs and/or unrealised planned income. Basic concepts and principles of HBOR's currency risk management are prescribed by the Currency Risk Management Procedures and the decisions of the Managing Board and the Assets and Liabilities Management Committee. The Currency Risk Management Procedures identify the sources of currency risk and establish the methods of measurement/assessment, monitoring and management of currency risk, limits and procedures in case of a possible crisis or the occurrence of crisis, as well as necessary reports for overall currency risk management.
For the measurement of currency risk exposure, the Bank implements the straightforward calculation methodology prescribed by the Croatian National Bank. A report on open currency positions is generated on a daily basis. The total open foreign currency position of the Bank is the combination of the sum of all long or the sum of all short positions in each currency, depending on which of the two sums is higher. In addition to daily monitoring of the open foreign currency position, the Bank monitors currency risk through prescribed limits and balancing the currencies of assets and liabilities. Scenario analysis, sensitivity analysis and stress testing are implemented. Most of HBOR's loan placements include currency clauses, which in accumulation represents a means of currency risk protection.

Operational risk

Operational risk is the risk of loss arising from system failure, human error or external events. The Bank endeavours to reduce its operational risk to the lowest level possible by introducing controls to operating procedures and by developing a unique and comprehensive IT system. The Bank implements the Basel II Guidelines and IT system good management practices.
For the supervision and monitoring of the IT system, HBOR's IT System Management Committee was established with the main task of managing IT system resources and establishing an adequate level of efficiency and security of the IT system in order to ensure adequate management of risks arising from the use of IT technology. Since a significant part of operational risk arises from the IT system, HBOR designated a person responsible for the analysis and control of IT system security. Exposure to operational risk is reduced by continuous employee training, the monitoring of frequent errors and prevention measures.

INTERNAL CONTROL AND INTERNAL AUDIT SYSTEM

The Control and Audit organisation unit is part of HBOR's internal control system and is in charge of monitoring overall operations based on the principles of legality, application of the Croatian Internal Audit Standards and HBOR internal acts. The Control and Audit, as an organisation unit, carries out its tasks and determines the manner of its operations, reporting, and the preparations of its findings, opinions and recommendations independently. It is directly responsible to the Managing Board, the Audit Committee and the Supervisory Board of HBOR. Reports are submitted on a three-monthly basis or semi-annually. Based on the audit report and according to the recommendations of the Control and Audit, the Managing Board takes the necessary decisions to take corrective measures and activities. Individual reports were drafted on controls carried out in 2010 as well as on the status of given recommendations and undertaken activities and submitted to the Managing Board, Audit Committee and the Supervisory Board within the regular reporting scheme.

OTHER ACTIVITIES

In March 2010, HBOR organized a Conference on micro-lending under the auspices of the German development bank, KfW, which gathered over three hundred participants. The main topic of the Conference was promoting the importance of support to small companies and craftsmen through micro-lending projects. At the Conference, a new HBOR's loan programme for micro, small and medium-sized enterprises was announced and its implementation started in June 2010.
In order to promote innovative entrepreneurs and support Croatian inventors, in October 2010, HBOR received representatives of inventors who won prestigious awards at the 10th British innovation fair 2010.
Anton Kovačev, President of HBOR's Managing Board, was elected President of the European Association of Public Banks (EAPB) for a term of two years, in December 2010. The European Association of Public Banks (EAPB) was founded in 2000 with the aim of representing the interests of state-owned banks, development banks and agencies in relation to the EU legislation and the European Parliament. Since its establishment, the EAPB has increased the number of its members from 10 to present 38 and it represents the interest of 130 financial institutions. Today, the EAPB gathers institutions from different European countries which together hold 15 percent of the European market and have approximately 190 thousand employees. The total assets of its members amount approximately to EUR 3,500 billion. The members of the EAPB are financial institutions, agencies, state-owned banks and other similar institutions or associations of such institutions that have their headquarters in the EU member states as well as in Switzerland, Norway and Croatia. In the two coming years, Mr. Anton Kovačev will, as EAPB President, represent the interests of the Association and its members before EU bodies, which means that the Republic of Croatia will have an active role in European financial circles even before its formal accession to the EU.
Hrvatska banka za obnovu i razvitak has been a member of the EAPB since 2007, and the election of the President of its Managing Board as President of the EAPB is a major recognition of the activities of HBOR and the Republic of Croatia.
For the second time after 2001, HBOR was in September 2010 honoured to be the host of the autumn meeting of the Prague Club. Approximately sixty representatives of export–credit agencies from 25 countries around the world participated in the work of the meeting. At this particularly significant international event, participants exchanged practical knowledge and experience in the field of export credit insurance and investment.
In keeping with the tradition, the 9th International Conference on Export Promotion was organised in September and took place in Zagreb, like the previous one. More than 240 participants gathered at this year's conference to discuss the challenges of the new decade and set the foundations for export growth. It was pointed out that there is need for increasing the volume of lending to clients abroad purchasing Croatian products and provide the same or similar financing terms as available to exporters from other countries which are competing with Croatian exporters in the international market. A significant amount of knowledge and experience was exchanged and resulted in numerous proposals and recommendations for export promotion.
In 2010, besides signing Memorandums of Understanding and holding meetings and conferences, in April 2010, HBOR hosted interns from NRW.Bank, German Development Bank of the state of North Rhine-Westphalia. In October of the same year, HBOR received representatives of the Iraqi working group interested in HBOR's services related to SMEs.
During the reporting year, HBOR actively participated in numerous associations, clubs and chambers, as a member.
In March 2010, HBOR hosted workshops and working meetings of the permanent working group of NEFI, Network of European Financial Institutions for SMEs. In May 2010, HBOR hosted the working meeting of the Legal Affairs Committee of EAPB, the European Association of Public Banks.
In 2010, HBOR continued to implement the activities for strengthening partnerships with similar institutions in Europe and throughout the world. For this purpose, co-operation agreements were signed with the Estonian export credit agency – Credit and Export Guarantee Fund (KredEx), the Bulgarian Development Bank and the Export Development Bank of Egypt. Signing of the Co-operation Agreement with the latter was organised on the occasion of visit of the Croatian business delegation to Egypt in December 2010.
Public operation of HBOR is an important precondition for the credibility of its activities. Therefore, HBOR pays special attention to providing comprehensive and understandable information to the public about its goals and measures to achieve them, as well as about the results of its activities.
In 2010, HBOR regularly informed the public about all important activities through various ways of informing. Public announcements were regularly published immediately after passing of decisions on new programmes, changes of terms and conditions of the loan programmes, after the presentation of operating results, fund raising, and other measures taken for the purpose of achieving the goals of HBOR. In the reporting year, HBOR held 6 press conferences, where the public was informed about its operations, operating results and the introduction of new programmes. In the reporting year, 18 press releases were published. All information relating to the Bank's operations, except those subject to Articles 168 and 169 of the Act on Credit Institutions, are available to the public on HBOR's web site www.hbor.hr. In 2010, forty-one (41) public invitations to tender were published in the electronic public procurement gazette, and since August 2010, all invitations to tender can be found also on the HBOR web site, www.hbor.hr.

HUMAN RESOURCES

HBOR operates successfully owing to the expertise and high professionalism of its employees. In order to attract and keep professional, motivated and satisfied employees, HBOR continually develops and enhances various tools and processes that have a positive influence on people, environment, and job performance. This is supported by the fact that HBOR has been assigned the Employer-Partner Certificate by the group Selectio as recognition for excellence in human resources management on several occasions.
All employees of HBOR have the opportunity of further training and education in accordance with their needs. Specialist seminars and trainings, foreign language courses, IT courses, on-the-job training in the country and abroad, as well as various types of long-term professional education (graduate and post-graduate studies) are available to them. In-house

education workshops are also organised, where the Bank's employees transfer useful know-how and skills to one another. They are open to all interested employees, thus providing additional education, flow of information, co-operation and team work among the workers. On 31st December 2010, there were 244 employees in HBOR, of which the majority with a university degree (80.74%). The average age of employees is 41.

HRVATSKO KREDITNO OSIGURANJE (CROATIAN CREDIT INSURANCE J.S.C.)

Hrvatsko kreditno osiguranje d.d. (hereinafter: HKO) is a joint-stock insurance company registered in the Register of the Commercial court in Zagreb on 18th January 2010.
HKO was registered for carrying out the activities of credit insurance, and the Croatian Financial Services Supervisory Agency (HANFA) gave the authorisation for its operations on 24th September 2009.
The founders and main shareholders of HKO are: Hrvatska banka za obnovu i razvitak, Strossmayerov trg 9, Zagreb, the Republic of Croatia with 51% of the owner's share in the equity and OeKB Südosteuropa Holding Ges.m.b.H, Am Hof 4, Vienna, Austria, with the remaining 49% share.
As at 31st December 2010, total subscribed and paid-in capital of HKO amounted to HRK 37.5 million. Ordinary shares of the Company were issued in a non-materialised form and are registered and managed with the Central Depository & Clearing Company Inc. (Središnje klirinško depozitarno društvo) in Zagreb under HKOS-R-A. 37,500 shares were issued, with the nominal value of HRK 1,000 each.
The main activity of HKO is insurance of short-term export and domestic receivables of business entities relating to the delivery of goods and rendering of services, within the type of insurance called Credit Insurance. The insurance covers commercial and political risks with the maturity of up to 180 days, and exceptionally up to one year.
HKO started its operations on 1st July 2010.
In July 2010, HKO, with a prior consent of the Supervisory Board, made a decision on the establishment of the limited liability company Poslovni info servis d.o.o. (hereinafter: PIS). The activities of the company include credit risk assessment and providing credit reports. PIS is 100% owned by HKO, and was registered on 26th October 2010 with the equity capital of HRK 2 million. PIS will start its operations in 2011.
By establishing PIS, HKO started to operate as a Group and to state its consolidated financials (hereinafter: the Group or consolidated).
On 31st December 2010, there were 9 employees in the Group, of which HKO employed 7, and PIS 2 employees.
Taking into account the specific features of insurance of receivables against commercial and political risks, HKO has a direct approach to its clients, and therefore it has neither established nor has the intention to establish, regional offices.

Management

Legal status, organisation and management of the company, and all other issues important for the operations of the company, as well as other harmonisations pursuant to the Companies' Act and the Insurance Act are determined by the Statutes of HKO.
The management bodies are: the Managing Board, the Supervisory Board and the Shareholders' Meeting.
The Managing Board of Hrvatsko kreditno osiguranje d.d. is as follows:
Edvard Ribarić, Chairman of the Managing Board
Anton Ludwig Steffko, Member of the Managing Board
The manager of Poslovni info servis d.o.o. is Ivana Paić – Mikulek.
In 2010, the Supervisory Board members were:
Anton Kovačev, Chairman of the Supervisory Board (until 31st March 2010)
Branimir Berković, Chairman of the Supervisory Board
(since 31st March 2010)
Helmut Hans Altenburger, Deputy Chairman of the Supervisory Board
Ružica Adamović, Member of the Supervisory Board
(until 29th October 2010)
Ante Artuković, Member of the Supervisory Board
(since 2nd November 2010)
The Managing Board regularly monitors the operations of the subsidiary company Poslovni info servis d.o.o. in order to provide the compliance of its operations with business goals of the Group.

Operations in 2010

Hrvatsko kreditno osiguranje d.d. started its operations by the conclusion of its first insurance contracts in the second half of 2010, i.e. 1st July 2010. Until the end of 2010, insurance contracts were concluded with 26 insured parties, whereby risks of receivables from buyers in 42 countries in the world were covered. The structure of exposure by countries reflects to the large extent the structure of Croatian exports. This means that in the total limits approved, the major portion related to Italy (19.53%), Serbia (14.08%), Germany (12.76%), Slovenia (9.34%) and Bosnia and Herzegovina (7.42%). These five countries accounted for the total of 63.13% of total exposure, which as at 31st December 2010 amounted to HRK 672 million. In 2010, the total number of approved limits was 776, and as at 31st December 2010, the number of approved limits was 771.
In 2010, the total charged premium of HKO amounted to HRK 1.6 million, of which HRK 1.2 million were allocated to reinsurance. Gross reserves of transferred premiums amounted to HRK 820 thousand, whereas net premium earned amounted to HRK 69 thousand. In 2010, there were no payments of indemnities on the basis of insured transactions.

INDICATORS OF INSURANCE BUSINESS, as at 31st December 2010

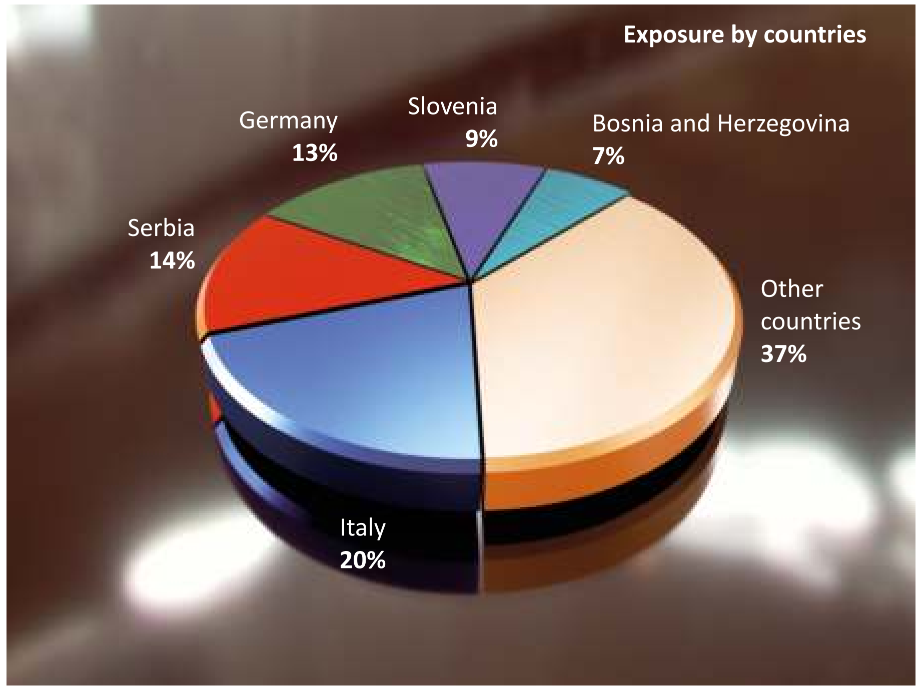
	HRK '000
Volume of insured transactions	802,041
Exposure	671,694
Gross premium charged	1,551
Paid indemnities	-
Number of paid indemnities	0
Gross recovery income	-
Number of limits-buyers	771
Number of contracts	26
Number of insured parties	26

BY NUMBER OF APPROVED LIMITS

Country	Number of limits	Share (%)
Germany	127	16.5
Italy	125	16.2
Slovenia	84	10.9
Serbia	79	10.3
Bosnia and Herzegovina	71	9.2
Hungary	39	5.1
Austria	33	4.3
Romania	30	3.9
Poland	21	2.7
Czech Republic	19	2.5
Other countries	143	18.6
Total	771	100.0

EXPOSURE BY LIMIT AMOUNT

Country	Amount in HRK '000	Share (%)
Italy	131,201	19.5
Serbia	94,641	14.1
Germany	85,683	12.8
Slovenia	62,708	9.3
Bosnia and Herzegovina	49,813	7.4
Croatia	30,000	4.5
Czech Republic	28,646	4.3
Belgium	25,985	3.9
Hungary	20,560	3.0
Austria	19,630	2.9
Other countries	122,827	18.3
Total	671,694	100.0



Business goals and plans

Business goals of HKO for 2011 are tied primarily to the strengthening of its presence and positioning in the Croatian market as a company specialised for short-term receivables insurance against political and commercial risks, familiarising of business entities with the service of receivables insurance, attracting of new insured parties and the beginning of work on the preparation of credit reports in Poslovni info servis, as well as further enhancement of services in accordance with market requirements and development.

HKO gives special importance to professional and expert standards in the performance of insurance business and to direct approach to the beneficiaries of its services, as well as to the quality, availability and promptness of service providing.

OVERVIEW OF FINANCIAL PERFORMANCE IN 2010

In 2010, the Hrvatska banka za obnovu i razvitak Group was formed, with the subsidiary companies Hrvatsko kreditno osiguranje d.d. and Poslovni info servis d.o.o. that constitute the Hrvatsko kreditno osiguranje Group. Further to this, the consolidated financial statements for 2010 are the first consolidated financial statements prepared by HBOR.
The financial statements include both HBOR and the Group. The financial statements of the Group consist of the consolidated financial statements of HBOR and its subsidiaries. However, the individual, non-consolidated financial statements of the parent company are also presented.
The subsidiary was established in January 2010, but it started its operations in the second half of 2010. Therefore, before the reporting date, the Group did not prepare its consolidated financial statements.
The individual and consolidated Annual financial statements of HBOR for 2010 that can be found enclosed were audited by the auditing company Deloitte d.o.o. which expressed an unqualified opinion in the Independent auditor's report.
In the text to follow, an overview of financial performance and operations is given separately for the Group and HBOR, as the parent company and entity subject to this report.

OVERVIEW OF OPERATIONS OF THE GROUP

The Group was formed in 2010, and, consequently, it is not practical to report trends in comparison with the previous business year.
Having in mind the size of the subsidiary companies and the volume of their operations compared with the operations with the parent company, their financial data in the first year of the Group are not significant so as to be separately highlighted within the framework of the consolidated financial statements. Consequently, they do not have a material effect on the consolidated financial statements in comparison with the individual statements of HBOR as the parent company.

Operating result of the Group

In the first year of its operations, the HBOR Group made a profit after taxation in the amount of HRK 117.2 million.
Pursuant to the HBOR Act, the parent company is not liable to pay profit tax; therefore, profit tax liabilities arise exclusively from the activities of other members of the Group.
The consolidated total income in 2010 amounted to HRK 922.1 million, and total expenses amounted to HRK 805.1 million, whereas recognised deferred tax assets amounted to HRK 0.2 million.
In the structure of income of the Group, the major portion, i.e. 97% relates to interest income as a result of the operations of the parent company.
The major portion of total expenses, i.e. 75% relates to interest expenses arising from the operations of the parent company.
The consolidated operating expenses in 2010 amounted to HRK 88.1 million, and consisted of general and administrative expenses and other operating expenses.
As at 31st December 2010, there were 253 employees in the Group.

Assets and liabilities of the Group

The Group's assets on consolidated basis amount to HRK 22.9 billion.
In the structure of assets, the major portion relates to the lending activities of the parent company, i.e. net loans account for 93% of assets.
In the liabilities of the Group, the major portion, i.e. 63% consists of borrowings and bonds payable of the parent company.
At the end of 2010, total equity and guarantee fund on consolidated basis amounted to HRK 7.027 billion and accounted for 31% of total liabilities of the Group.

OVERVIEW OF OPERATIONS OF HBOR

In the text to follow, there is an overview and explanations of significant changes in business operations and of the performance in the reporting year.

Operating performance

In 2010, HBOR generated a total income of HRK 921.0 million, expenses of HRK 803.0 million and profits of HRK 118.0 million.

Net interest income
Net interest income amounted to HRK 286.8 million, a decrease of 14% on the previous year. Interest income amounted to HRK 891.7 million, a decrease of 4% on the previous year. Such a tendency has been completely expected and planned due to the fact that HBOR, as the development bank and implementer of the measures for economic recovery of the Republic of Croatia, has not changed its interest rates on loans for several years.
Interest expenses amounted to HRK 604.9 million, an increase of 2% on the previous year as a result of new borrowings during the reporting and previous years.

Net fee income
Net fee income amounted to HRK 8.9 million, a decrease of 34% in comparison with the same period last year. The decrease was for the major part a result of decreased volume of guarantees issued.

Net gains/(losses) on financial operations
Net gains/(losses) on financial activities are comprised of net foreign exchange gains/losses on the principal amount of receivables and liabilities, net gains or losses arising out of loan contracts with an embedded call option, gains/(losses) of value adjustments of assets at fair value through profit or loss and realised gains/(losses) on assets available for sale. In the reporting period, net gains from financial activities amounted to HRK 17.8 million, whereas net losses of HRK 6.6 million were recorded in the same period last year.
At the year level, the Croatian kuna depreciated by 1.1% against the euro and by 9.4% against the USD.
Foreign currency or foreign currency indexed assets and sources of funds are converted by HBOR into HRK equivalent value in accordance with the exchange rate of the Croatian National Bank at the Balance Sheet date. Foreign currency revenues and expenditures are converted in accordance with the exchange rate at the transaction date. The resulting foreign exchange gains or losses are recorded in the Income Statement in net figures.

Operating expenses
Operating expenses include general and administrative expenses and other expenses and amounted to HRK 86.1 million, which represents a decrease of 2% compared to the same period last year.
There were 244 employees on 31st December 2010, and 241 on 31st December 2009.

Impairment loss and provisions
In accordance with the regulations and internal decrees, HBOR determines the amount of impairment loss and provisions and maintains it at the level it considers adequate for the coverage of possible future risks.
In the reporting period, net impairment loss on placements amounted to HRK 110.3 million.

Significant changes in business activities
The balance sheet total as at 31st December 2010 amounted to HRK 22.9 billion, which is an increase of 10% compared to the beginning of the year.

Cash on hand and due from banks
As at 31st December 2010, cash on hand and due from banks amounted to HRK 1.4 billion, representing 6% of total assets. The significant increase in cash on hand and due from banks is a result of unutilised funds of the club deal with domestic commercial banks on the transaction account for special purposes with the Croatian National Bank for the purpose of the realisation of the Measures for economic recovery and development comprised in the Decision of the Government of the Republic of Croatia dated 14th January 2010 and the Conclusion of the Government of the Republic of Croatia dated 28th January 2010. At the end of 2010, these funds amounted to HRK 1.145 billion.

Loans to banks and other customers
An increase in loans to banks and other customers was continued in 2010. Total net loans at the end of 2010 stood at HRK 21.246 billion, an increase of 5.2% compared to the previous year. In the total assets, net loans accounted for 93%. Total gross loans amounted to HRK 23.568 billion.

Assets available for sale
Assets available for sale consisted primarily of debt and to a lesser extent of equity securities held by the Bank mostly for the purpose of liquidity management. This item amounted to HRK 186.6 million, a decrease of 22% compared to the beginning of the year due to the redemption of bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-103A) as regularly due on 8th March 2010 and due to the redemption of the Treasury bills of the Ministry of Finance as regularly due in the course of the year.

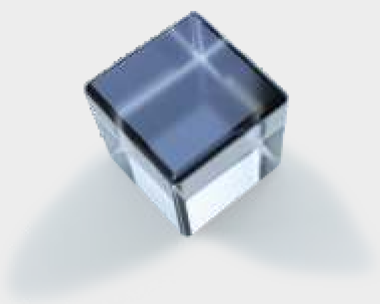
Investments in associates
Investments in associates are a constituent part of the Programme for Equity Investments in Companies – small and medium enterprises – or are carried out in accordance with special decisions of HBOR. They were stated at acquisition cost in the amount of HRK 23.7 million.
The investment value was fully impaired in previous years because of its estimated un-recoverability.

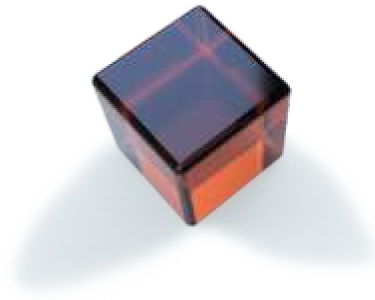
Total liabilities
Total liabilities as at 31st December 2010 amounted to HRK 15.913 billion, which represents 69% of total liabilities. The major portion of total liabilities consists of HBOR foreign borrowings and bonds payable in the total amount of HRK 14.530 billion.

Liabilities under loans taken rose by 35% compared to the beginning of the year as a result of withdrawal of funds under previously arranged loans and new borrowings raised in the reporting year:
- Club loan agreement concluded on 18th February 2010 with several domestic commercial banks aimed to HBOR's 40% of share in the financing through the Loan Programme for the Financing of Working Capital (Model „A“) in the amount of HRK 2.0 billion,
- Credit line with the Council of Europe Development Bank (CEB) for small and medium-sized companies in the amount of EUR 50.0 million,
- Credit lines with the European Investment Bank (EIB) for the financing of SMEs, environmental projects and infrastructure projects in the public and private sector of EUR 250.0 million and for the financing of project for the restarting of VCM plant and the construction of new PVC plant in the amount of EUR 34.0 million, and
- Credit line with Kreditanstalt für Wiederaufbau (KfW) for small and medium-sized enterprises and micro-lending in the amount of EUR 20.0 million and for the tourism in the amount of EUR 30.0 million.

As in the previous year, in 2010 HBOR continued to raise funds for the specified purposes from similar special financial institutions.

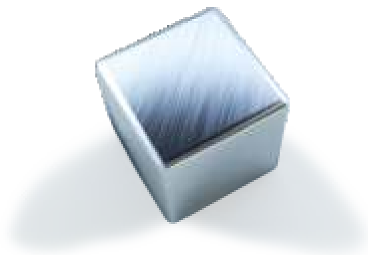
Equity
Equity and guarantee fund amounted to HRK 7.010 billion, representing 31% of total liabilities, equity and guarantee fund. HBOR's total equity is comprised of the Founder's capital contributed from the budget of the Republic of Croatia, retained earnings, other reserves, and profits for the current year and supplemental capital. In the reporting period, contributions from the budget to the Founder's capital amounted to HRK 220.0 million.
The total amount of capital contributed from the budget of the Republic of Croatia amounted to HRK 4.7 billion. The outstanding amount of capital to be paid from the budget of the Republic of Croatia, up to the amount of the Founder's capital prescribed by the HBOR Act (HRK 7.0 billion), is HRK 2.3 billion.
The Bank's profit for the year, pursuant to the HBOR Act, is allocated to reserves.





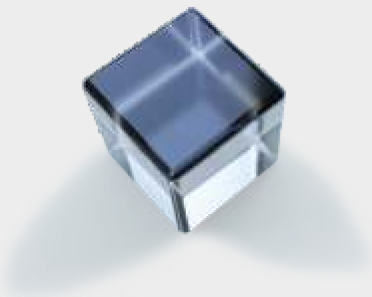
CROATIAN BANK FOR RECONSTRUCTION AND DEVELOPMENT

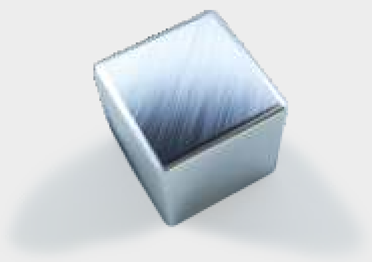
Annual financial statements
for the year ended 31 December 2010



Zagreb, March 2011

Contents





Responsibility for the Financial Statements

Pursuant to the Accounting Act of the Republic of Croatia, the Managing Board of the Bank is obliged to ensure that the financial statements for each financial year are prepared in accordance with the International Financial Reporting Standards (IFRS), as published by the International Accounting Standards Board (IASB), so as to give a fair view of the position and operating results of the Croatian Bank for Reconstruction and Development (the Bank) and the Group for that period.

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

In preparing the consolidated and separate financial statements, the responsibilities of the Managing Board include ensuring that:

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

The Managing Board is responsible for keeping proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Bank and the Group, and must also ensure that the financial statements comply with the Croatian Accounting Act. The Managing Board is also responsible for safeguarding the assets of the Bank and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Signed on behalf of the Managing Board:

Anton Kovačev

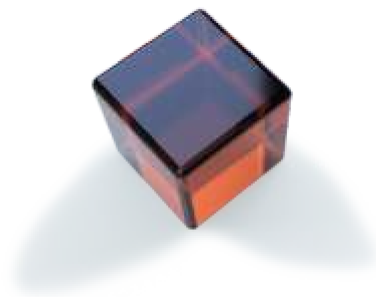
President of the Managing Board

Croatian Bank for Reconstruction and Development

Strossmayerov trg 9

10 000 Zagreb

Zagreb, 31 March 2011



Deloitte.

Deloitte d.o.o.
ZagrebTower
Radnička cesta 80
10 000 Zagreb
Hrvatska
OIB: 11686457780

Tel: +385 (0) 1 2351 900
Fax: +385 (0) 1 2351 999
www.deloitte.com/hr

Independent Auditor's Report

To the owner of the Croatian Bank for Reconstruction and Development:

We have audited the accompanying unconsolidated and consolidated financial statements of the Croatian Bank for Reconstruction and Development ("the Bank") and its subsidiaries ("the Group"), respectively which comprise the Statement of Financial Position as at 31 December 2010, and Income Statement, Statement of Comprehensive Income, Statement of Changes in Equity and Statement of Cash Flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Responsibility for the Financial Statements

The Managing Board is responsible for the preparation and fair presentation of these financial statements in accordance with accounting legislation in the Republic of 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 entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the 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.

Opinion

In our opinion the unconsolidated and consolidated financial statements give a true and fair view of the financial position of the Bank and the Group, respectively as at 31 December 2010 and of its financial performance and its cash flows for the year then ended in accordance with the International Financial Reporting Standards.

Branislav Vrtačnik, Member of the Board and Certified Auditor
Deloitte d.o.o.

Zagreb, 31 March 2011

Deloitte d.o.o.
Zagrebtower
Radnička cesta 80
10 000 Zagreb
MB 0700851

Financial statements of the Group

Consolidated Income Statement

For the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

	Notes	2010 HRK '000
Interest income	3	892,290
Interest expense	4	(604,927)
Net interest income		**287,363**
Fee income	5	10,728
Fee expense	5	(1,679)
Net fee income		**9,049**
Net gains/(losses) on financial operations	6	17,767
Other income		1,352
		315,531
Operating expenses	7	(88,114)
Impairment loss and provisions	8	(110,356)
Profit before income tax		**117,061**
Income tax	9	181
Profit for the year		**117,242**
Attributable to:		
Equity holders of the parent		117,603
Non-controlling interests		(361)
		117,242

The accompanying accounting policies and notes are an integral part of this Income Statement.

Consolidated Statement of Comprehensive Income

For the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

	2010 HRK '000
Profit for the year	**117,242**
Other comprehensive income	
Increase in fair value of assets available for sale	7,434
Decrease in fair value of assets available for sale	(8,812)
Net foreign exchange on available for sale equity securities	139
Other comprehensive income	**(1,239)**
Total comprehensive income after income tax	**116,003**
Attributable to:	
Equity holders of the parent	116,364
Non-controlling interests	(361)
	116,003

The accompanying accounting policies and notes are an integral part of this Statement of Comprehensive Income.

Consolidated Statement of Financial Position

As of 31 December 2010

(All amounts are expressed in HRK thousand)

	Notes	2010 HRK '000
Assets		
Cash on hand and due from banks	10	1,258,729
Deposits with other banks	11	137,555
Loans to banks	12	15,449,447
Loans to other customers	13	5,796,393
Financial assets at fair value through profit or loss	14	500
Assets available for sale	15	187,710
Assets held to maturity	16	1,077
Investments in associates	18	-
Property, plant and equipment and intangible assets	19	71,839
Non-current assets held for sale	20	34,361
Other assets	21	4,465
Total assets		**22,942,076**
Liabilities		
Deposits	22	222,658
Borrowings	23	7,047,415
Bonds payable	24	7,482,253
Other liabilities	25	1,162,318
Total liabilities		**15,914,644**
Equity		
Founder's capital	26	5,163,739
Retained earnings and reserves		1,718,962
Other reserves		(2,978)
Profit for the year		117,603
Total equity attributable to equity holders of the parent		**6,997,326**
Non-controlling interests		18,014
Total equity		**7,015,340**
Guarantee fund	27	12,092
Total equity and Guarantee fund		**7,027,432**
Total liabilities, total equity and Guarantee fund		**22,942,076**

The accompanying accounting policies and notes are an integral part of this Statement of Financial Position.

Signed on behalf of the Croatian Bank for Reconstruction and Development on 31 March 2011 by:

Anton Kovačev
President of the Managing Board

Irena Adžić-Jagodić
Accounting Division Executive Director

Consolidated Statement of Cash Flows

For the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

	2010 HRK '000
Operating activities	
Profit before income tax	117,061
Adjustments to reconcile to net cash from and used in operating activities:	
Depreciation	5,312
Impairment loss and provisions	110,356
Accrued interest	4,831
Deferred fees	3,178
Income tax paid	-
Operating profit before working capital changes	
Changes in operating assets and liabilities:	
Net (increase) in deposits with other banks, before provision for impairment	(11,024)
Net (increase) in loans to banks, before provision for impairment	(643,848)
Net (increase) in loans to other customers, before provision for impairment	(528,419)
Net decrease of discount in assets available for sale and bonds payable	19,875
Net (increase) in other assets, before provision for impairment	(743)
Net (increase) in non-current assets held for sale	(1,502)
Net increase in deposits from banks and companies	17,817
Net increase in other liabilities, before provisions	27,688
Net cash used in operating activities	**(879,418)**
Investment activities	
Net (purchase) of financial assets at fair value through profit or loss	(500)
Net (purchase) of assets available for sale	
Net sale of assets available for sale	
Net (collection) on redemption of assets held to maturity	(1,041)
Net (purchase) of property, plant and equipment and intangible assets	(10,147)
Net cash (used in) / provided by investment activities	**26,555**
Financing activities	
Net increase in founder's capital	220,000
Increase in borrowings – withdrawn funds	4,110,062
(Decrease) in borrowings – repayments of principal	(2,331,935)
(Decrease) in bonds payable – repayment of amortizing note	(148,394)
Payments by non-controlling interests	18,375
Net cash provided by financing activities	**1,868,108**
Effect of foreign currency to cash and cash equivalents	
Net foreign exchange	129,946
Net effect	**129,946**
Net increase in cash and cash equivalents	1,145,191
Balance as of 1 January, before provisions	125,335
Net increase in cash	1,145,191
Balance as of 31 December, before provisions	**1,270,526**
Additional note - Operational cash flows	
Interest paid	578,610
Interest received	676,906

The accompanying accounting policies and notes are an integral part of this Statement of Cash Flows

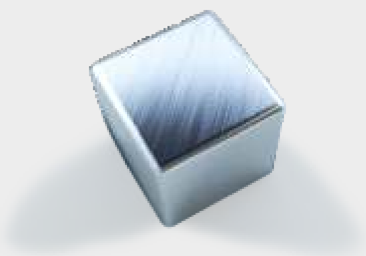
Consolidated Statement of Changes in Equity

For the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

	Founder's capital HRK '000	Retained earnings and reserves HRK '000	Other reserves HRK '000	Net profit for the year HRK '000	Non-controlling interests HRK '000	Total equity HRK '000
Balance as of 1 January 2010	**4,943,739**	**1,553,432**	**(1,739)**	**165,530**	**-**	**6,660,962**
Profit for the year	-	-	-	117,603	(361)	**117,242**
Other comprehensive income	-	-	(1,239)	-	-	**(1,239)**
Total comprehensive income	-	-	(1,239)	117,603	(361)	**116,003**
Capital paid-in from the State Budget (Note 26)	220,000	-	-	-	-	**220,000**
Transfer of profit 2009 to retained earnings	-	165,530	-	(165,530)	-	**-**
Increase in non-controlling interests	-	-	-	-	18,375	**18,375**
Balance as of 31 December 2010	**5,163,739**	**1,718,962**	**(2,978)**	**117,603**	**18,014**	**7,015,340**

The accompanying accounting policies and notes are an integral part of this Statement of Changes in Equity.



Financial statements of the Bank

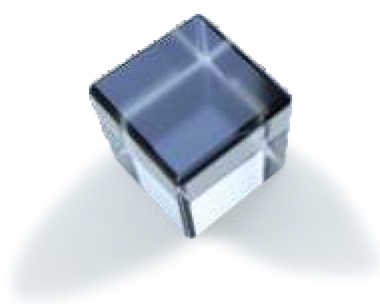
Unconsolidated Income Statement

For the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

	Notes	2010 HRK '000	2009 HRK '000
Interest income	3	891,714	927,255
Interest expense	4	(604,926)	(592,945)
Net interest income		**286,788**	**334,310**
Fee income	5	10,537	14,953
Fee expense	5	(1,679)	(1,432)
Net fee income		**8,858**	**13,521**
Net gains/(losses) on financial operations	6	17,755	(6,608)
Other income		922	1,340
		314,323	**342,563**
Operating expenses	7	(86,105)	(88,013)
Impairment loss and provisions	8	(110,256)	(89,020)
Profit before income tax		**117,962**	**165,530**
Income tax	2	-	-
Profit for the year		**117,962**	**165,530**
Attributable to:			
Equity holders of the parent		**117,962**	**165,530**

The accompanying accounting policies and notes are an integral part of this Income Statement.



Unconsolidated Statement of Comprehensive Income

For the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

	2010 HRK '000	2009 HRK '000
Profit for the year	**117,962**	**165,530**
Other comprehensive income		
Increase in fair value of assets available for sale	7,434	21,067
Decrease in fair value of assets available for sale	(8,813)	(17,020)
Net foreign exchange on available for sale equity securities	139	(32)
Other comprehensive income	**(1,240)**	**4,015**
Total comprehensive income after income tax	**116,722**	**169,545**
Attributable to:		
Equity holders of the parent	**116,722**	**169,545**

The accompanying accounting policies and notes are an integral part of this Statement of Comprehensive Income.

Unconsolidated Statement of Financial Position

As of 31 December 2010

(All amounts are expressed in HRK thousand)

	Notes	2010 HRK '000	2009 HRK '000
Assets			
Cash on hand and due from banks	10	1,258,012	124,200
Deposits with other banks	11	103,284	127,055
Loans to banks	12	15,449,447	14,866,066
Loans to other customers	13	5,796,393	5,329,841
Assets available for sale	15	186,659	238,188
Investments in subsidiaries	17	19,125	-
Investments in associates	18	-	-
Property, plant and equipment and intangible assets	19	71,418	67,004
Non-current assets held for sale	20	34,361	32,862
Other assets	21	3,598	4,436
Total assets		**22,922,297**	**20,789,652**
Liabilities			
Deposits	22	222,658	204,840
Borrowings	23	7,047,415	5,216,141
Bonds payable	24	7,482,253	7,525,143
Other liabilities	25	1,160,195	1,170,603
Total liabilities		**15,912,521**	**14,116,727**
Equity			
Founder's capital	26	5,163,739	4,943,739
Retained earnings and reserves		1,718,962	1,553,432
Other reserves		(2,979)	(1,739)
Profit for the year		117,962	165,530
Total equity		**6,997,684**	**6,660,962**
Guarantee fund	27	12,092	11,963
Total equity and Guarantee fund		**7,009,776**	**6,672,925**
Total liabilities, total equity and Guarantee fund		**22,922,297**	**20,789,652**

The accompanying accounting policies and notes are an integral part of this Statement of Financial Position.

Signed on behalf of the Croatian Bank for Reconstruction and Development on 31 March 2011 by:

Anton Kovačev
President of the Managing Board

Irena Adžić-Jagodić
Accounting Division Executive Director

Unconsolidated Statement of Cash Flows

For the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

	2010 HRK '000	2009 HRK '000
Operating activities		
Profit before income tax	117,962	165,530
Adjustments to reconcile to net cash from and used in operating activities:		
Depreciation	5,264	6,057
Impairment loss and provisions	110,256	89,020
Accrued interest	5,235	45,567
Deferred fees	3,178	377
Operating profit before working capital changes	*241,895*	*306,551*
Changes in operating assets and liabilities:		
Net decrease in deposits with other banks, before provision for impairment	22,866	700,936
Net (increase) in loans to banks, before provision for impairment	(643,847)	(2,826,467)
Net (increase)/decrease in loans to other customers, before provision for impairment	(528,420)	151,600
Net decrease/(increase) of discount in assets available for sale and bonds payable	19,876	(48,320)
Net (increase)/decrease in other assets, before provision for impairment	(58)	1,718
Net (increase)/decrease in non-current assets held for sale	(1,502)	2,050
Net increase/(decrease) in deposits from banks and companies	17,818	(233,974)
Net increase in other liabilities, before provisions	25,664	58,409
Net cash (used in) operating activities	**(845,708)**	**(1,887,497)**
Investment activities		
Net (increase) in investments in subsidiaries	(19,125)	-
Net (purchase) of assets available for sale	(369,725)	(72,705)
Net sale of assets available for sale	409,018	-
Net (purchase) of property, plant and equipment and intangible assets	(9,678)	(6,970)
Net cash provided by/(used in) investment activities	**10,490**	**(79,675)**
Financing activities		
Net increase in founder's capital	220,000	220,000
Increase in borrowings – withdrawn funds	4,110,062	2,594,961
(Decrease) in borrowings – repayments of principal	(2,331,936)	(2,382,626)
Increase in bonds payable – new issues	-	1,837,888
(Decrease) in bonds payable – repayment of amortizing note	(148,394)	(146,245)
(Decrease) in Guarantee fund – write off	-	(427)
Net cash provided by financing activities	**1,849,732**	**2,123,551**
Effect of foreign currency to cash and cash equivalents		
Net foreign exchange	129,960	(45,106)
Net effect	**129,960**	**(45,106)**
Net increase in cash and cash equivalents	1,144,474	111,273
Balance as of 1 January, before provisions	125,335	14,062
Net increase in cash	1,144,474	111,273
Balance as of 31 December, before provisions	**1,269,809**	**125,335**
Additional note - Operational cash flows		
Interest paid	578,610	501,640
Interest received	676,728	708,303

The accompanying accounting policies and notes are an integral part of this Statement of Cash Flows

Unconsolidated Statement of Changes in Equity

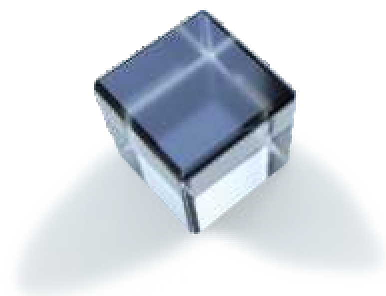
For the year ended 31 December 2010

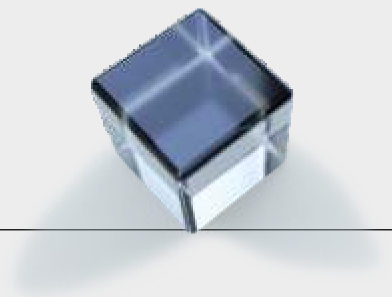
(All amounts are expressed in HRK thousand)

The accompanying accounting policies and notes are an integral part of this Statement of Changes in Equity.

	Founder's capital HRK '000	Retained earnings and reserves HRK '000	Other reserves HRK '000	Net profit for the year HRK '000	Total equity HRK '000
Balance as of 1 January 2009	**4,723,739**	**1,378,526**	**(5,754)**	**174,906**	**6,271,417**
Profit for the year	-	-	-	165,530	165,530
Other comprehensive income	-	-	4,015	-	4,015
Total comprehensive income	-	-	4,015	165,530	**169,545**
Capital paid-in from the State Budget (Note 26)	220,000	-	-	-	**220,000**
Transfer of profit 2008 to retained earnings	-	174,906	-	(174,906)	**-**
Balance as of 31 December 2009	**4,943,739**	**1,553,432**	**(1,739)**	**165,530**	**6,660,962**
Profit for the year	-	-	-	117,962	**117,962**
Other comprehensive income	-	-	(1,240)	-	**(1,240)**
Total comprehensive income	-	-	(1,240)	117,962	**116,722**
Capital paid-in from the State Budget (Note 26)	220,000	-	-	-	**220,000**
Transfer of profit 2009 to retained earnings	-	165,530	-	(165,530)	**-**
Balance as of 31 December 2010	**5,163,739**	**1,718,962**	**(2,979)**	**117,962**	**6,997,684**

The accompanying accounting policies and notes are an integral part of this Statement of Changes in Equity.





1. General information

1.1. Group:

The Croatian Bank for Reconstruction and Development ("HBOR" or "the Bank") is the parent company of the Croatian Bank for Reconstruction and Development Group ("Group") that operates in the Republic of Croatia. The Group primarily performs banking activities and, to the lesser extent, insurance activities and credit risk assessment activities. These Financial Statements include separate and consolidated financial statements of the Bank and the Group as defined in the International Accounting Standard 27: Consolidated and Separate Financial Statements.

The legal address of the Bank is Strossmayerov trg 9, Zagreb, Croatia.

The Group was formed in 2010; the Bank's subsidiary companies are *Hrvatsko kreditno osiguranje d.d.* and *Poslovni info servis d.o.o.* that constitute the Hrvatsko kreditno osiguranje Group ("HKO Group").

The legal address of the HKO Group is Zagreb, Bednjanska 12.

As of 31 December 2010, the Group had 253 employees.

1.2. Bank:

The Croatian Bank for Reconstruction and Development ("HBOR" or "the Bank") was established on 12 June 1992 under the Act on the Croatian Credit Bank for Reconstruction ("HKBO"). In December 1995, the Bank changed its name to Croatian Bank for Reconstruction and Development. The founder and 100% owner of HBOR is the Republic of Croatia.

The Republic of Croatia guarantees HBOR's liabilities unconditionally, irrevocably and on first call, without issuing any particular guarantee. The responsibility of the Republic of Croatia as guarantor for HBOR´s liabilities is joint and unlimited.

With the new Act on the Croatian Bank for Reconstruction and Development passed in December 2006, HBOR's founding capital was HRK 7 billion, the payment schedule of which is determined by the State budget.

As of 31 December 2010, there were 244 employees at the Bank (31 December 2009: 241 employees).

1.2.1. Activities of the Bank:

The principal activities of the Bank comprise the following:

- financing of the reconstruction and development of the Croatian economy,
- financing of infrastructure,
- promoting exports,
- providing support to the development of SMEs,
- promoting environmental protection, and
- providing domestic goods and services export insurance against non-market risks for and on behalf of the Republic of Croatia

HBOR may perform other financial activities according to the decisions of the Government of the Republic of Croatia if, in their opinion, it is in the best interest of the Republic of Croatia.

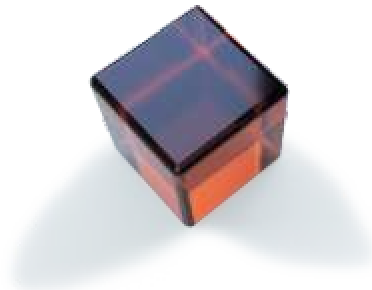
1. General information (continued)

1.3. Bodies of the Bank and the Group:

In 2010, the Supervisory Board members were as follows:

- Martina Dalić, MSc, Minister of Finance – ex officio President of the Supervisory Board since 30 December 2010,
- Ivan Šuker, Deputy Prime Minister of the Republic of Croatia and Minister of Finance - ex officio President of the Supervisory Board (until 30 December 2010),
- Đuro Popijač, Minister of the Economy, Labour and Entrepreneurship – ex officio Vice President of the Supervisory Board,
- Božidar Pankretić, MSc, Deputy Prime Minister of the Republic of Croatia and Minister of Regional Development, Forestry and Water Management,
- Damir Bajs, Minister of Tourism,
- Božidar Kalmeta, Minister of the Sea, Transport and Infrastructure,
- Nadan Vidošević, President of the Croatian Chamber of Economy, ex officio Member of the Supervisory Board,
- Goran Marić, Ph.D., Member of the Croatian Parliament,
- Dragan Kovačević, Ph.D., Member of the Croatian Parliament,
- Dragica Zgrebec, Member of the Croatian Parliament.

MANAGING BOARD



In 2010, members of the Managing Board were as follows:

- Anton Kovačev, President of the Managing Board,
- Emilija Nagj, Member of the Managing Board,
- Mladen Kober, Member of the Managing Board.

Audit Committee:

In 2010, the Audit Committee was comprised of the following members:

- Ivan Šuker, Minister of Finance, President of the Supervisory Board of HBOR, President of the Audit Committee,
- Nadan Vidošević, President of the Croatian Chamber of Economy, Member of the Audit Committee,
- Ante Artuković, Executive Director of HBOR's Analysis Division, Member of the Audit Committee.

On 26 January 2011, the Supervisory Board appointed new members of the Audit Committee as follows:

- Martina Dalić, MSc, Minister of Finance, President of the Supervisory Board of HBOR, President of the Audit Committee,
- Nadan Vidošević, President of the Croatian Chamber of Economy, Vice President of the Audit Committee,
- Ante Artuković, Executive Director of HBOR's Analysis Division, Member of the Audit Committee.

1. General information (continued)

1.4. Current economic situation and its impact on the Bank

So far, the economic situation in Croatia has not had a significant impact on the financial position and performance of the Bank. The Bank monitors closely the credit, liquidity, interest rate and foreign exchange risk on a regular basis. The highest exposure of credit portfolio is the one towards banks, which minimizes the level of credit risk due to strictly regulated banking sector by the central bank. Available-for-sale financial assets are not materially significant and the Bank does not acquire securities and investments for the purpose of short-term selling in order to realize gains/losses from trading activities, and due to that deteriorating capital markets had no significant impact to the “fair” value of assets and Bank's operations.

The economic environment in 2011 is difficult to fully predict, but the financial crisis will probably impact certain industries (i.e. tourism, construction, processing industries, real estate sector) and the abilities of some customers to meet their loan obligations. Due to that, the Managing Board continues to expect an increase in applications for loan restructuring as it was the case in 2010. Such circumstances may consequently influence the amount of the provisions for impairment losses in 2011, including the valuation of collateral. Also, it is expected that loan applications for financing working and permanent working capital to increase in order to strengthen the liquidity of companies.

It has to be taken into account, that HBOR, as a state-owned development financial institution, has a significant role in the implementation of “Measures for economic recovery and development – financing models” passed by the Government of the Republic of Croatia, the implementation of which started in 2010 and is expected to continue in 2011 (see Note 36 Events after the reporting period date).

The Bank has sufficient funds and high level of liquidity for financing planned loan activities, meeting obligations and liabilities and maintaining required level of liquidity.

1.5. The first consolidated statements

The consolidated statements for 2010 were the first consolidated statements prepared by the Bank. The unconsolidated financial statements for the year ended 31 December 2009 are to be considered as comparatives to the 2010 consolidated financial statements.

Detailed information on the Group and the basis of consolidation are given in Notes 1.1. and 2.1.

Having in mind the size of the subsidiary companies and the volume of their operations compared with the operations of the parent company, their financial data within the first year of operations of the Group are not significant and therefore they are not separately disclosed in these consolidated financial statements.

The Group was formed in 2010, and, consequently, it is not practical to state parallel financial data for the previous year. Even though the subsidiary company was established in January 2010, it started its operating activities in the second half of 2010, and the Group did not prepare consolidated financial statements before the reporting date.

2. Summary of significant accounting policies

2.1. Accounting policies

Principal accounting policies applied when preparing these financial statements are summarized below. Accounting policies were consistently applied to all periods presented in these financial statements.

Basis of accounting

The Bank and the Group maintain their accounting records in HRK in accordance with Croatian law and the accounting principles and practices observed by financial institutions in the Republic of Croatia.

Statement of compliance

These consolidated and separate financial statements are prepared in accordance with International Financial Reporting Standards (IFRS), as published by the International Accounting Standards Board.

Basis of financial statements presentation

The financial statements are prepared under the historical cost convention, with an exception of certain financial assets and financial liabilities that are measured at fair value.

The financial statements are prepared on an accrual and a going concern basis.

Reporting currency

The financial statements of the Bank and the Group are prepared in Croatian Kuna (HRK) as the functional and reporting currency of the Bank and the Group.

Amounts presented are rounded to a nearest thousand, unless otherwise stated.

The effective exchange rate of HRK as of 31 December 2010 was HRK 7.385173 per 1 Euro and HRK 5.568252 per 1 United States dollar (31 December 2009: HRK 7.306199 per 1 Euro and HRK 5.089300 per 1 United States dollar), unless otherwise contracted.

Basis of consolidation

The financial statements include the Bank and the Group. The financial statements of the Group include the consolidated financial statements of the Bank and its subsidiary companies. Separate non-consolidated financial statements of the parent company are also stated.

Subsidiary companies

Subsidiary companies are all those companies, in which the Bank is entitled to govern the financial and operating policies, i.e. in which it holds more than a half of voting rights.
Subsidiary companies are included into consolidated financial statements in accordance with the full consolidation method from the moment when the actual control is transferred to the Bank. The consolidation ceases from the moment they are sold or liquidated, i.e. from the moment when the control is lost.

Investments in subsidiary companies are stated at investment cost, i.e. in accordance with the cost method.

(All amounts are expressed in HRK thousand)

2. Summary of significant accounting policies

2.1. Accounting policies (continued)

Basis of consolidation (continued)

Subsidiary companies (continued)

When preparing data and consolidated financial statements, the amount of the parent's investment in each subsidiary and the parent's portion of equity of each subsidiary are eliminated, and intragroup balances and transactions, revenues and expenditures as well as unrealised gains and losses are eliminated in full.

The accounting policies of subsidiary companies are in line with those of the parent company in order to ensure comparability at the level of the Group.

Non-controlling interests in the net assets of consolidated subsidiaries are identified separately from the parent's ownership interests in them. Non-controlling interests in the net assets consist of the amount of those non-controlling interests at the date of the initial recognition of investment in the subsidiary company and the non-controlling interests' share of changes in equity since the date of acquisition of the interest. Losses incurred by a subsidiary company will be allocated between controlling and non-controlling interests even if losses exceed the non-controlling equity investment in the subsidiary.

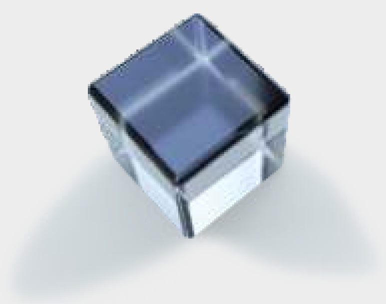
Associated companies

Associated companies are all those companies, in which the Group has a significant influence, i.e. is entitled to participate in decisions on the financial and operating policies of the investee, but does not have control over such policies. The Group has a significant influence if it holds, directly or indirectly, between 20 % and 50 % of voting rights of a company.

Investments in associated companies are recognised using the equity method in the consolidated financial statements, i.e. at acquisition cost in the non-consolidated financial statements of the parent company.

Unrealised gains on transactions with associated companies are eliminated to the extent of the Group's interest in such companies. Unrealised losses are eliminated in the same way as unrealised gains, but only if there are no indications of investment value impairment.

The operating results of associated companies are included into the consolidated financial statements until the date when the investment in the company is sold, i.e. until the date when the parent company loses its significant influence over the related company.



2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Interest income and expense

Interest income and expense are recognized in the income statement when earned or incurred. Interest income and expense are recognized in the income statement for all interest-bearing instruments on an accrual basis using the effective interest rate, which is the rate that discounts estimated future cash payments or receipts through the expected life of the financial instrument or on a shorter period, where appropriate. Interest income includes coupons earned on fixed income investments.

Loan origination fees, together with estimated related costs, are deferred and recognized as an adjustment to the effective yield on the loan.

Notional interest is recognized on impaired loans and other financial assets based on the rate used to discount future cash flows to their net present value.

Fee and commission income

Fee and commission income is comprised mainly of fees receivable from companies for guarantees granted and other services rendered by the Group, together with commissions for managing funds for and on behalf of legal entities and fees for foreign and domestic payment transactions. Fees and commissions are generally recognized in the period when the related service is rendered.

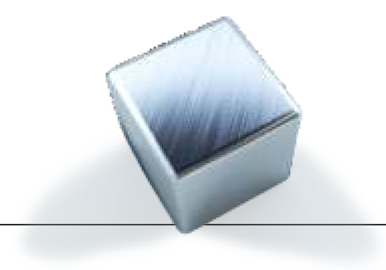
Fees on issued financial/payment guarantees are deferred and proportionally recognized as income over the term of guarantee.

Employee benefits

Pursuant to local legislation, the Group is obliged to pay contributions to the State Pension and Health Insurance Funds. This obligation relates to full-time employees and provides for paying contributions as certain percentages determined on the basis of the gross salary as follows:

	2010	2009
Contributions for state health insurance fund	15,00%	15,00%
Contributions for employment fund	1,60%	1,60%
Special contribution for employment of disabled persons	0,20%	0,20%
Contribution for injuries at work	0,50%	0,50%

The Group is also obliged to withhold and pay contributions from gross pay on behalf of the employees to the State Pension Fund and Mandatory Pension Fund.



(All amounts are expressed in HRK thousand)

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Employee benefits (continued)

The Group does not have pension arrangements separate from the state pension system of the Republic of Croatia. This system requires that current contributions by the employer be calculated as a percentage of current gross salary payments; these expenses are charged to the income statement in the period the related compensation is earned by the employee. The contributions on behalf of employees and on behalf of the employer are charged to expense in the period to which they relate. The Group calculates and pays required personal income tax and surtax on personal income tax from gross salary for each employee.

Foreign currency transactions and foreign currency clause

Assets and liabilities expressed in foreign currencies are converted into HRK at the exchange rates quoted by the Croatian National Bank at the Statement of Financial Position date or at the contract exchange rates. Income and expense arising in foreign currencies are converted at the rate of exchange on the transaction date. The resulting foreign exchange gains and losses are recorded in the income statement.

The Bank has assets originated in HRK and linked to a foreign currency with a one-way currency clause. Due to this clause, the Bank has the option to revalue the asset using a foreign exchange rate, if beneficial for the Bank valid as of the date of maturity, compared to the foreign exchange rate valid as of the date of origination of asset.

Changes arising from one-way currency clause contracts, based on which the value of receivables and liabilities denominated in a functional currency is changed with regard to the respective contract foreign currency (embedded derivatives – weighted exchange rate) imply changes in the fair value of embedded derivatives.

The Bank has assets originated in HRK that are linked to a foreign currency with two-way currency clause. These assets are translated to HRK as if they were originated in foreign currency.

The principal rates of exchange set forth by the Croatian National Bank and used in the preparation of the financial statements at the reporting dates were as follows:

31 December 2010	EUR 1 = HRK 7.385173	USD 1 = HRK 5.568252
31 December 2009	EUR 1 = HRK 7.306199	USD 1 = HRK 5.089300

Taxation

Based on Article 9 of the Act on the Croatian Bank for Reconstruction and Development, the parent company is exempt from income tax.

Income tax liabilities arise exclusively from the activities of the other members of the Group.

Income tax is charged on taxable profits in accordance with tax regulations and at the statutory tax rate.

Income tax expense is comprised of current and deferred tax. The amount of the income tax is reported in the Income Statement except for the income tax that relates to the items that are recognised directly in equity and reserves when income tax is recognised in equity and reserves.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Taxation (continued)

Current tax is the expected tax payable charged on the taxable amount of profits for the year by applying the tax rates in effect at the reporting date and all tax liability adjustments for previous periods.

The amount of deferred tax is calculated by applying the balance sheet liability method, providing for all temporary differences between the carrying amounts of assets and liabilities recorded for reporting purposes and the amounts used for tax calculation purposes. Deferred tax is calculated at the tax rates that are expected to apply on temporary differences when remunerated or settled in accordance with the regulations in force or in effect at the Statement of Financial Position date.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. Deferred tax liabilities are reviewed at each reporting date and reduced to the extent that it is no longer probable that the related tax benefits will be realisable.

Deferred tax assets and liabilities are not discounted; they are recognised as long-term assets and/or long-term liabilities.

Cash and cash equivalents

For the purposes of the cash flows reporting, cash and cash equivalents comprise cash and current accounts with the Croatian National Bank and other banks less provisions for impairment and un-collectable amounts.

Financial instruments

Financial assets and financial liabilities presented in the Statement of Financial Position include cash and cash equivalents, debt securities, trade and other accounts receivable and payable, long-term loans and leases, deposits and investments.

The Group classifies its own financial instruments into following categories:

- financial assets at fair value through profit or loss,
- available-for-sale financial assets,
- held-to-maturity financial assets,
- loans and receivables.

Financial instruments are classified into the above categories pursuant to the intention at acquisition. Classification of financial instruments at initial recognition and accounting principles of their measurement are prescribed by accounting policies brought by the Managing Board.

The principal difference among the categories relates to the measurement approach of financial assets and the recognition of their fair values in the financial statements that is described in the text below.

All securities held by the Group are recognized using settlement date accounting and are initially measured at cost and directly attributable transaction costs when investments are not recognised at fair value through the Income Statement.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Financial instruments (continued)

The Bank does not make acquisitions of securities and investments to attain gain/loss from short term trading activities.

a) Financial assets at fair value through profit or loss

The above category is divided into two sub-categories: financial instruments held for trading purposes and those initially classified by the management into this category that are not traded actively. Financial assets classified into this category that are not intended for trading purposes have been acquired primarily for the purpose of maintaining the liquidity reserve and managing the short-term liquidity.

Upon initial recognition, financial assets carried at fair value through profit or loss are accounted for and presented at fair value based on the closest quoted prices or amounts obtained by the application of acceptable valuation models. When measuring the fair value of shares in cash investment funds, the price that is applied is the price of the share in the fund as of a given date acquired from the investment fund management company. The Group includes unrealized gains and losses in 'Net gains/(losses) on financial operations'.

b) Available-for-sale financial assets

Assets available for sale are financial assets designated as available for sale or not classified as either held to maturity or carried at fair value through profit or loss or loans and receivables.

This portfolio comprises equity and debt securities and investment funds shares acquired for liquidity maintenance or acquired for placement of available funds up to the moment of further long term placements to loans with original due date over one year that are intended to be held for an indefinite period of time.

Subsequent to initial recognition, available-for-sale financial assets are re-measured at fair value based on quoted prices or amounts derived from cash flow models. In circumstances where the quoted market prices are not readily available, the fair value of debt securities is estimated using various valuation techniques including the use of present value of future cash flows and mathematical models, while the fair value of unquoted equity instruments is estimated using applicable price/earnings or price/cash flow ratios refined to reflect the specific circumstances of the issuer.

For available for sale assets, unrealized gains and losses arising from changes in fair value are recognized directly in equity, until their disposal or impairment, at which time the cumulative gain or loss previously recognized in equity is included in the profit or loss for the period.

Impairment losses on assets available for sale are presented in the Income Statement. If the fair value of an equity instrument subsequently increases, the increase will be recognized as other comprehensive income, and will not be subsequently reversed in the Income Statement. Impairment losses recognized in profit or loss for debt instruments are subsequently reversed if an increase in the fair value of the instrument can be objectively related to an event occurring after the recognition.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Financial instruments (continued)

b) Available-for-sale financial assets (continued)

When a decline in the fair value of available-for-sale financial assets has been recognized in equity and there is an objective evidence that the asset is impaired according to IAS 39 provisions, the cumulative loss that has been recognized in equity shall be reclassified from equity to profit or loss as a reclassification adjustment, even though the financial asset has not been derecognized.

Interest earned whilst holding available for sale securities is accrued on a daily basis and is reported as 'Interest income' in the Income Statement.

Foreign exchange gains/(losses) related to available for sale equity instruments held in foreign currency are recognized together with fair value gains and losses in equity until the financial asset is sold. Foreign exchange gains/(losses) related to available-for-sale debt instruments in foreign currency are reported in the income statement.

c) Held-to-maturity financial assets

Investments held-to-maturity are financial assets with fixed or identifiable payments and fixed maturities for which the Group has the intent and ability to hold to maturity. This portfolio comprises treasury bills and debt securities. Held-to-maturity financial assets are carried at amortized cost using the effective yield method, less any provision for impairment.

The Group 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 provisions through the income statement under 'Impairment loss and provisions'.

d) Loans to banks and other customers

Amounts paid-out by HBOR in providing funds directly to the borrower at drawdown are categorized as loans to customers and are carried at amortized cost derived from using the effective interest method and adjusted for possible impairment.

The amount of the subsidized interest provided for the final user under the Programme of Preferential Financing through HBOR's Loan Programmes is presented as deferred interest income in other liabilities and released over the term of the loan and is shown in the income statement on a time basis during the repayment of the loan applying effective interest rate method.

All loans and advances are recognized when cash is paid-out to borrowers.

(All amounts are expressed in HRK thousand)

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Financial instruments (continued)

d) Loans to banks and other customers (continued)

Provision for impairment is performed if there is objective evidence that HBOR will not be able to collect all amounts due. The Managing Board of HBOR determines the adequacy of the provision based upon analysis of various factors, the structure of the loan portfolio and past experience.

The amount of the provision is the difference between the carrying and recoverable amounts of the balance outstanding, being the present value of expected cash flows, including amounts recoverable from guarantees and collateral, discounted based on the effective interest rate.

The loan loss provision is also assessed on portfolio basis covering losses where there is objective evidence that possible losses are present, specifically identified in components of the loan portfolio at the Statement of Financial Position 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).

If there is no objective evidence that an impairment loss has been incurred, whether it is significant or not, the financial asset is classified into the group of assets with similar credit risk characteristics and all assets from this group are subject to joint estimation for the purpose of a collective evaluation of impairment. Contracted cash flows and historical loss experience for assets with similar credit risk characteristics are subject to collective evaluation of expected cash flows.

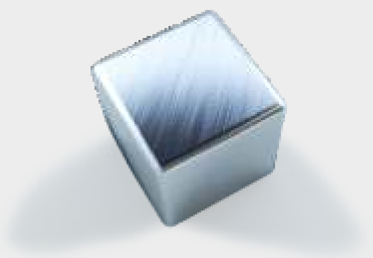
When a loan is deemed uncollectible, it is written off against the related provision for impairment. Subsequent recoveries of these loans are recognized in the Income Statement.

Securities purchased under agreements to purchase and resell ('reverse repos') are recorded as assets in the Statement of Financial Position under 'Loans to banks'. Interest earned in the period from the purchase until the resale of the security is accrued on a daily basis and reported as 'Interest income' in the Income Statement.

At the end of 2010, the Group's REPO deals amounted to HRK 4,117,707 thousand (2009: HRK 2,847,363 thousand) collateralized by securities in the amount of HRK 4,393,074 thousand (2009: HRK 2,991,902 thousand).

Property, plant and equipment and intangible assets

Property, plant and equipment and intangible assets are recognized at cost. Depreciation is charged using the linear method, by applying the annual rates ranging from 3.03% to 33.3% to the cost of assets over their estimated useful lives.



2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Property, plant and equipment and intangible assets (continued)

Estimated useful lives are as follows:

	2010	2009
	years	years
Buildings	33	33
Computers	3	3
Furniture and Equipment	5 - 8	5 - 8
Vehicles	3	3
Other assets and investments not mentioned	5	5
Intangible Assets	3 – 5	3 - 5

Depreciation is not charged on property, plant and equipment and intangible assets in the course of construction, until they are available for use. Repairs and maintenance are expensed in the Income Statement as incurred. Expenditure that increases the future economic benefits of existing tangible and intangible assets (improvements) is capitalized.

Impairment of assets

An assessment of financial assets is made at the reporting date to determine whether there is objective evidence that a specific financial asset may be impaired. If such evidence exists, the estimated recoverable amount of that asset and any impairment loss, based on the net present value of future anticipated cash flows including anticipated recoveries from guarantees and collateral instruments, discounted by the original effective interest rate, is recognized in the Income Statement.

Property, plant and equipment and intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Whenever the carrying amount of an asset exceeds its recoverable amount, an impairment loss is recognized in the Income Statement for items of property, plant and equipment and intangible assets carried at cost, or it is treated as a revaluation decrease for assets that are carried at re-valued amount to the extent that the impairment loss does not exceed the amount held in the revaluation surplus for the same assets. The recoverable amount is the higher of an asset's net selling price and its value in use.

Non-current assets held for sale

Non-current assets held for sale consist of property, plant and equipment that the Group acquired in settlement of uncollected receivables. The Group expects that the carrying amount of these assets will be recovered principally through a sale transaction rather than through continuing use.

This category of assets is initially stated at fair value less estimated expected costs to sell.

The Group measures these assets at the lower of its carrying amount and fair value (determined by an independent assessor) less estimated expected costs to sell.

Depreciation on these assets is not charged.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Non-current assets held for sale (continued)

The Bank recognises an impairment provision for any initial or subsequent partial write-off of these assets up to the fair value less costs to sell. It recognises a gain for any subsequent increase in fair value of assets less costs to sell up to the amount of cumulative impairment provision that has been recognised.

Impairment provisions are recognized in the Income Statement, as well as gains/losses upon subsequent measurement and on sale of the non-current assets.

Bank's borrowings and bonds payable

Borrowings and bonds payable are measured at amortized cost determined using the ef fective interest method. The Group recognises interest expense related to borrowings and bonds payable in the Income Statement.

Government grants

Interest for the borrowers qualifying for subsidized interest under the Programme of Preferential Financing through HBOR's Loan Programmes, the Development and Employment Programme, the Programme for Regional Development of the Republic of Croatia, the Financing Model for the Reconstruction and Modernisation of the Fishing Fleet, the Renewable Energy Resources Project, the Programme of Issuing Bank Guarantees and investments into entrepreneurial zones is subsidized by the Republic of Croatia – the Ministry of Finance, the Fund for Development and Employment, the Regional Development Fund of the Republic of Croatia, the Ministry of Agriculture, Fisheries and Rural Development, the Ministry of the Sea, Transport and Infrastructure, the Ministry of the Economy, Labour and Entrepreneurship and the Environment and Energy Efficiency Fund during the entire loan repayment period.

The discounted amount of the interest subsidies provided for the final user is presented as deferred interest income in other liabilities and is recognized in the Income Statement on a time basis during the repayment of the loan. Consequently, loans are measured at amortized cost by using interest rate without taking into account the effects of subsidies contributed by the State.

Guarantees and other loan related commitments

In the ordinary course of business, the Bank issues financial guarantees, including letters of credit that are recorded off-balance sheet. Financial guarantee contracts are initially measured at their fair values. Subsequent to initial recognition, guarantees are measured at fair value at the higher of the amount of the obligation under the contract and the amount initially recognized less, where appropriate, cumulative amortization recognized in accordance with the revenue recognition policies.

Contingent liabilities under guarantees are mostly collateralized by the guarantees of the Government of the Republic of Croatia, while letters of credit are fully covered by the deposits.

Provisions for commitments upon undrawn loans and issued guarantees are maintained at a level considered as adequate by the Managing Board in order to absorb potential losses.

Provisions are recognized when the Bank has a present legal or contractual obligation as a result of past events, when it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and when a reliable estimate of the amount of the obligation can be made.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Segment reporting

The Segment is a unique component of the Group and its operations are the supply of products or services (business segment) or the supply of products or services within a certain business environment (geographical segment) subject to unique risks and benefits, different from the ones in other segments.

The general format of business segments is based on the decision of the Managing Board and the stated segments are in line with financial statements which are prepared in accordance with the International Financial Reporting Standards.

The Group has identified three main segments: banking activities, insurance activities and other activities.

Since the Group predominantly operates in the Republic of Croatia, there are no secondary (geographical) segments.

Managed funds for and on behalf of third parties

The Bank manages significant assets for and on behalf of the Ministry of Finance, Ministry of the Economy, Labour and Entrepreneurship, Ministry of the Sea, Transport and Infrastructure, Ministry of Agriculture, Fisheries and Rural Development, Ministry of Regional Development, Forestry and Water Management, the Environment and Energy Efficiency Fund, Vodovod i kanalizacija d.o.o., Split and the Croatian Agency for Small Business ("HAMAG"), that are used for the financing of reconstruction and development programmes.

These amounts do not represent assets of HBOR and are excluded from the Bank's Statement of financial position but are recorded separately from the Bank's operations.

Revenues and expense relating to this business activity are charged to third parties, and the Bank does not have other liabilities nor bears any risks. For services provided within the framework of some of the programmes, the Bank charges a fee, whereas other programmes are performed by the Bank free of charge See Note 29.

2.2. Significant accounting judgments and estimates

For the preparation of financial statements in accordance with IFRS's, the Managing Board is required to give estimations and make assumptions that influence the reported balances of assets and liabilities and to disclose contingent amounts of assets and liabilities at the date of financial statements, and present income and expense for the reporting period. Estimations are based on information available at the reporting date, so that actual amounts may differ from those estimated.

In the process of applying the Bank's accounting policies, the management has made judgments and estimates in determining the amounts recognized in the financial statements. The most significant use of judgments and estimates are as follows:

a) Fair value of financial instruments

If there is no active market for a certain financial instrument, or if for any other reason the fair value of financial assets and financial liabilities presented in the Statement of Financial Position cannot be reliably measured by the market price, the Group determines the fair value by using various valuation techniques including the use of

2. Summary of significant accounting policies (continued)

2.2. Significant accounting judgments and estimates (continued)

a) Fair value of financial instruments (continued)

mathematical models. The input data for these models are taken from other recognizable markets where possible, but if it is not possible, there is a certain degree of judgment required in determining fair values.

b) Valuation of financial instruments

The Bank's accounting policy on fair value measurements is discussed in Note 32 Fair Value of Financial Instruments.

c) Loan impairment provisions

The Bank regularly monitors its loans and receivables to assess impairment. The Bank uses its experience of judgments to estimate the amount of any impairment loss in cases where a borrower is in financial difficulties and there are several available sources of historical data relating to similar borrowers.

Similarly, the Bank estimates changes in future cash flows using the data indicating 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.

The management uses estimates based on the 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 experience and judgment to adjust available data for a group of loans or receivables according to current market conditions.

d) Provisions for legal cases

The Group performs a risk classification of legal cases taking into consideration the legal basis of the claim, prior legal practice, opinions of relevant in-house lawyers, opinions of the outsourced attorneys and the Bank's own experience.

The Group makes provisions for legal cases in proportion with the total amount and estimated likelihood of not winning the case. In estimating provisions, the Bank takes into account the due legal process in the Republic of Croatia, which allows a multiple appeal procedure in certain cases.

e) Provisions for retirement and jubilee benefits

In calculating provisions for retirement and jubilee benefits, the Bank discounts expected future cash flows in respect of the liabilities, using discount rates that, in the opinion of the Bank's management, best represent the time value of the money.

2.3. Adoption of new and amended International financial reporting standards

The following is a review of adopted standards which are not effective as at the date of publishing the Group's financial statements. The Group will apply the standards relevant to its operations when they become effective.

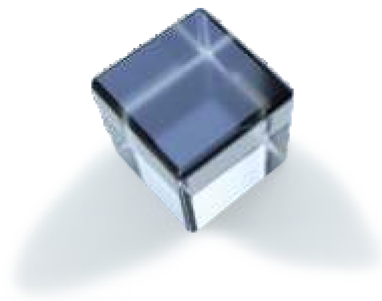
- Amendments to IAS 24 Related party disclosures (effective for periods beginning on or after 1 January 2011) clarified the definition of related parties and introduced partial exemption for government-related entities. The standard provided for a partial exemption of related party disclosures for transactions between government-related entities as well as with the government itself. Instead of general disclosure requirements, the standard allows for alternative disclosures that require: the name of the

2. Summary of significant accounting policies (continued)

2.3. Adoption of new and amended International financial reporting standards (continued)

government and the nature of its relationship with the reporting entity, the nature and amount of each individually significant transaction, a qualitative or quantitative indication of the extent of other transactions that are collectively, but not individually significant. Although the standard permits the early application for either partial exemption for government-related entities or for the entire revised standard, the Group assessed that application of partial exemption would contain same level of disclosures as in prior periods. The amended standard will not impact financial performance and financial statements.

- Amendments to IAS 32 Financial instruments: Presenting – Classifications of rights issues (effective for periods beginning on or after 1 February 2010) which supplements the definition of liabilities by the classification of rights issues (and certain options or variations) as equity instruments if such rights are issued pro rata to an entity's all existing shareholders in the same class of the entity's non-derivate equity instruments or in order to acquire a fixed amount of entity's own equity instruments for a fixed amount in any currency. The above Standard does not affect the Group after initial implementation.
- IFRS 9 Financial instruments: Classification and measurement (effective for periods beginning on or after 1 January 2013) is the first phase of IASB's project to replace IAS 39, applicable for the classification and measurement of financial assets as defined by IAS 39. In the following steps, IASB will define the classification and measurement of financial liabilities, accounting protection and derecognition. The finalisation of this project is expected in the first segment of 2011. The Group will quantify the effects together with other phases in order to project the full picture.
- Amended interpretation (IFRIC) 14 Prepayments of a minimum funding requirement (effective for periods beginning on or after 1 January 2011 and applicable for earlier periods) providing guidelines for the assessment of the recoverable amount of net pension assets. The amendments allow for the entity to treat its prepayments of minimum funding requirement as an asset. These amendments will not affect the Group's financial statements.
- Interpretation (IFRIC) 19 Extinguishing financial liabilities with equity instruments (effective for periods beginning on or after 1 July 2010) clarifies that equity instruments issued to a creditor to extinguish a financial liability are classified as “consideration paid”. Issued equity instruments should be measured at fair value. In case fair value is not reliably determinable, the equity instruments issued are measured at fair value of the liability extinguished. The profit or loss is recognised immediately in the Income statement. The application of this interpretation will not affect the Group's financial statements.



Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

3. Interest income

Interest income by borrowers:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Public sector	32,471	32,458	44,921
State-owned companies	63,739	63,739	83,761
Foreign companies	8,336	8,336	7,946
Domestic companies	301,906	301,906	296,503
Domestic banks	403,597	403,034	430,786
Foreign banks	1,714	1,714	5,348
Other	62,581	62,581	47,741
Penalty interest	17,946	17,946	10,249
	892,290	**891,714**	**927,255**

Interest income by type of facility:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Interest on loans			
- banks	402,867	402,867	430,835
- other customers	463,569	463,569	476,905
	866,436	866,436	907,740
Investments in securities	13,737	13,161	10,250
Deposits	1,970	1,970	9,265
Due from domestic banks	10,147	10,147	-
	892, 290	**891,714**	**927,255**

The difference between interest income and interest received or collected (see Statement of Cash Flows) mostly relates to the income in respect to interest subsidies inflows that are recorded upon payment. The discounted amount of the interest subsidies provided for the final user is presented as deferred interest income (see note 25 Other liabilities) and is recognized in the Income Statement on a time basis during the repayment of the loan. Interest income earned on this basis in 2010 amounts to HRK 200,567 thousand (2009: HRK 197,792 thousand).

Further, the difference between interest income and interest collected relates to the amount of loan fees and accrued interest. Loan fees are collected after origination of the loan, but their recognition in the Income Statement is performed using effective interest rate method. Accrued interest is recognized in the Income Statement on a time basis.

Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

4. Interest expense

Interest expense by type of payee:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Domestic banks	22,588	22,587	38,705
Foreign banks	582,339	582,339	554,239
Other	-	-	1
	604,927	**604,926**	**592,945**

Interest expense by type of facility:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Borrowings	174,030	174,030	253,908
Debt securities	430,896	430,896	338,417
Deposits	1	-	620
	604,927	**604,926**	**592,945**

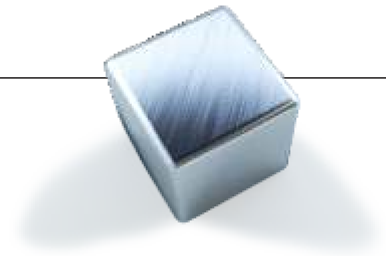
The difference between interest expense and interest paid (see the Statement of Cash Flows) mostly relates to the changes in the amount of the interest accrued in relation to the prior year and the amortization of discount for issued debt securities.

5. Net fee income

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Fee income:			
From issued guarantees	*3,846*	*3,846*	*7,127*
From managed funds for and on behalf of third parties	*6,070*	*6,070*	*7,080*
From payment operations	*328*	*328*	*661*
Other	*292*	*293*	*85*
Reinsurance commission income	*192*	*-*	*-*
	10,728	**10,537**	**14,953**
Fee expense	(1,679)	(1,679)	(1,432)
Net fee income	**9,049**	**8,858**	**13,521**

6. Net gains/(losses) on financial operations

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Net foreign exchange gains/(losses) on foreign currency assets:			
Cash on hand, accounts at banks and due from banks	*7,197*	*7,197*	*(10,939)*
Loans given to banks and other customers	*141,585*	*141,585*	*(39,591)*
Assets held to maturity	*14*	*-*	*-*
Assets available for sale	*1,412*	*1,412*	*52*
Other	*450*	*450*	*1,468*
	150,658	150,644	(49,010)
Net foreign exchange gains/(losses) on foreign currency liabilities:			
Deposits	*(3,663)*	*(3,663)*	*(3,534)*
Borrowings and issued long-term securities	*(132,334)*	*(132,334)*	*44,490*
Other	*(229)*	*(226)*	*(420)*
	(136,226)	(136,223)	40,536
Net foreign exchange gains/(losses) on foreign currency assets and liabilities	14,432	14,421	(8,474)
Gains on assets at fair value through profit or loss	3,335	3,334	1,866
Net gains/(losses) on financial operations	**17,767**	**17,755**	**(6,608)**



7. Operating expenses

Operating expenses can be shown as follows:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
General and administrative expenses:			
Employee expenses	48,983	48,088	52,117
Depreciation	5,312	5,264	6,057
Administration expenses	7,344	7,198	7,056
Material and services	21,385	20,783	17,147
	83,024	81,333	82,377
Other expenses:			
Taxes and contributions	281	277	291
Other expenses	4,809	4,495	5,345
	5,090	4,772	5,636
	88,114	**86,105**	**88,013**

Other expenses of the Group presented contain changes in technical reserves:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Changes in claims provisions	440	-	-
Changes in claims provisions, share of reinsurance	(314)	-	-
Expenses of insurance operations	**126**	**-**	**-**

Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

8. Impairment loss and provisions

The provision for impairment losses on placements may be summarized as follows:

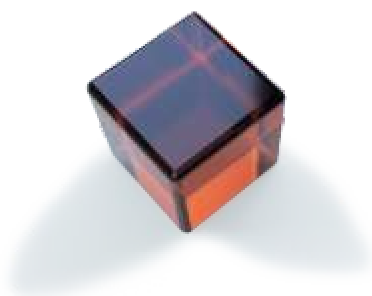
	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Impairment losses on cash on hand and due from banks	11,445	11,445	1,093
Impairment losses on deposits with other banks	(408)	(408)	(6,942)
Impairment losses on loans to banks	55,489	55,489	(54,396)
Impairment losses on loans to other customers and interest	63,262	63,262	167,515
Impairment losses on non-current assets held for sale	3	3	6,529
Impairment losses on assets available for sale	15,344	15,344	13
Impairment losses on other assets	896	896	3,449
Total increase in provision for impairment losses on assets	146,031	146,031	117,261
Provision for guarantees and commitments	(56,548)	(56,548)	(36,042)
Other provisions	20,873	20,773	7,801
Total (decrease) in provision for guarantees and commitments and other provisions	(35,675)	(35,775)	(28,241)
Total increase of provisions	**110,356**	**110,256**	**89,020**

9. Income tax

Based on Article 9 of the Act on the Croatian Bank for Reconstruction and Development, the parent company is exempt from income tax. Income tax liabilities arise exclusively from the activities of the other members of the Group.

	2010 Group HRK '000
Recognised in the income statement	
Deferred tax income	181
Income tax	**181**
Income tax reconciliation	
Profit/(loss) before tax	**(912)**
Income tax at 20% rate	182
Non-deductible expense	(1)
Income tax recognised in the income statement	**181**
Recognised in the Statement of Comprehensive Income	
Deferred tax income/(expenditure)	-
Income tax	-
Recognised deferred tax assets	**181**

The total amount of recognised deferred tax assets for subsidiaries tax loss is going to be carried forward to future periods, in the next five years from the reporting period it was originated in, falls due in 2015.



10. Cash on hand and due from banks

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Account with the Croatian National Bank	1,157,164	1,157,164	12,028
Due from domestic banks in foreign currency	47	47	677
Due from foreign banks in foreign currency	112,598	112,598	112,630
Due from domestic banks in HRK	717	-	-
Accrued interest	783	783	-
	1,271,309	1,270,592	125,335
Provisions for impairment losses	(12,580)	(1,135)	(12,580)
	1,258,729	**1,258,012**	**124,200**

Funds in the account with the Croatian national bank are funds drawn from the club deal with domestic commercial banks for the purpose of the implementation of Measures for economic recovery and development comprised in the Decision of the Government of the Republic of Croatia dated 14 January 2010 and the Conclusion of the Government of the Republic of Croatia dated 28 January 2010.

The balance of undisbursed funds in the transaction account with the Croatian national bank as at 31 December 2010 amounts to HRK 1,144,572 thousand.

Due from foreign banks in foreign currency represents the amount drawn from a loan tranche approved by the International Bank for Reconstruction and Development (IBRD) under the credit line „Croatia Export Finance Intermediation Loan Project" and amounts to EUR 14,834 thousand.

The movements in the provision for impairment losses on amounts due from banks may be summarized as follows:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Balance as at 1 January	1,135	1,135	42
Increase of provision for impairment losses on amounts due from banks	11,445	11,445	1,093
Release of provision for impairment losses on amounts due from banks	-	-	-
Balance as at 31 December	**12,580**	**12,580**	**1,135**

Reconciliation with the Statement of cash flows:

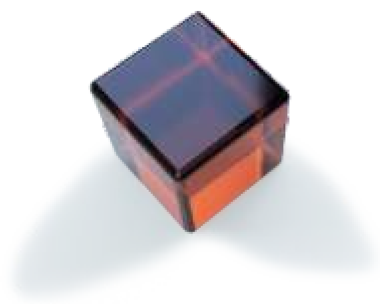
	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Total cash on hands and due from banks, before provisions	1,271,309	1,270,592	125,335
Accrued interest	(783)	(783)	-
Balance of cash on hands and due from banks reconciled with statement of cash flows	**1,270,526**	**1,269,809**	**125,335**

11. Deposits with other banks

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Deposits with foreign banks	84,367	84,367	25,447
Deposits with domestic banks	53,890	20,000	101,786
Accrued interest	381	-	1,313
	138,638	104,367	128,546
Provision for impairment losses	(1,083)	(1,083)	(1,491)
	137,555	**103,284**	**127,055**

The movements in the provision for impairment losses on deposits with other banks may be summarized as follows:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Balance as of 1 January	1,491	1,491	8,433
Increase of provision for impairment losses on deposits with other banks	-	-	550
Release of provision for impairment losses on deposits with other banks	(408)	(408)	(7.492)
Balance as of 31 December	**1,083**	**1,083**	**1,491**



Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

12. Loans to banks

Loans to banks, net of provision for impairment losses, may be summarized as follows:

	Group HRK '000	2010 Bank HRK '000	2019 Bank HRK '000
Loans due within one year	8,131,534	8,131,534	7,822,965
Loans due in over one year	8,058,064	8,058,064	7,718,022
Accrued interest	27,446	27,446	31,344
Deferred recognition of loan origination fees	(48,897)	(48,897)	(47,818)
	16,168,147	16,168,147	15,524,513
Provision for impairment losses	(718,700)	(718,700)	(658,447)
	15,449,447	**15,449,447**	**14,866,066**

The movements in the provision for impairment losses on loans to banks may be summarized as follows:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Balance as of 1 January	658,447	658,447	713,507
Increase of provision for impairment losses on loans to banks	381,341	381,341	164,540
Release of provision for impairment losses on loans to banks	(325,852)	(325,852)	(218,936)
Net foreign exchange gains/(losses) on provision for impairment losses	4,764	4,764	(664)
Balance as of 31 December	**718,700**	**718,700**	**658,447**

Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

12. Loans to banks (continued)

Loans to banks, net of provision for impairment losses, by purpose of the loan programme may be summarized as follows:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Loan programme for reconstruction and development of the economy	4,229,206	4,229,206	4,763,580
Export financing	4,399,662	4,399,662	5,255,572
Loan programme for reconstruction and development of infrastructure in the Republic of Croatia	424,146	424,146	393,567
Loan programme for small and medium-sized enterprises	2,571,601	2,571,601	1,958,999
Loan programme for war-torn and demolished housing and business facilities	19,576	19,576	21,374
Other	4,545,407	4,545,407	3,147,895
Accrued interest	27,446	27,446	31,344
Deferred recognition of loan fees	(48,897)	(48,897)	(47,818)
	16,168,147	16,168,147	15,524,513
Provisions for impairment losses	(718,700)	(718,700)	(658,447)
	15,449,447	**15,449,447**	**14,866,066**

Interest rates for loans approved during 2010 and 2009 are for the most part within the range of 0.5% - 5%, depending on the purpose of the loan and the investment location.

Item “Other” refers to reverse repo placements in the total amount of HRK 4,117,707 thousand (2009: HRK 2,783,895 thousand). The above placements are collateralised by securities in the amount of HRK 4,393,074 thousand (2009: HRK 2,991,902 thousand).

Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

13. Loans to other customers

Loans to other customers, net of provision for impairment losses, may be summarized as follows:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Domestic companies	4,822,390	4,822,390	4,087,232
State-owned companies	1,273,088	1,273,088	1,456,801
Public sector	415,254	415,254	484,892
Foreign companies	217,404	217,404	213,924
Non-profit institutions	13,217	13,217	8,510
Other	696,708	696,708	646,111
Accrued interest	22,151	22,151	18,361
Deferred recognition of loan origination fees	(60,617)	(60,617)	(58,221)
	7,399,595	7,399,595	6,857,610
Provision for impairment losses	(1,603,202)	(1,603,202)	(1,527,769)
	5,796,393	**5,796,393**	**5,329,841**

The movements in the provision for impairment losses on loans to other customers may be summarized as follows:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Balance as of 1 January	1,527,769	1,527,769	1,368,372
Increase of provision for impairment losses on loans to other customers and interest	203,596	203,596	278,324
Release of provision for impairment losses on loans to other customers and interest	(139,942)	(139,942)	(108,327)
Net foreign exchange gains/(losses) on provision for impairment losses	11,903	11,903	(3,912)
Collection of off-balance sheet receivables	(392)	(392)	(2,482)
Provisions transferred from off-balance sheet	392	392	2,482
Write-offs	(124)	(124)	(656)
Transfer to off-balance sheet – loans	-	-	(6,032)
Balance as of 31 December	**1,603,202**	**1,603,202**	**1,527,769**

Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

13. Loans to other customers (continued)

Loans to other customers, net of provision for impairment losses, may be summarized by loan programme as follows:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Economic reconstruction and development	2,724,118	2,724,118	2,068,765
Export	1,479,260	1,479,260	1,495,799
Infrastructure reconstruction and development in the Republic of Croatia	1,793,624	1,793,624	1,943,255
Small and medium enterprises	1,266,743	1,266,743	1,134,074
Other	174,316	174,316	255,577
Accrued interest	22,151	22,151	18,361
Deferred recognition of loan origination fees	(60,617)	(60,617)	(58,221)
	7,399,595	7,399,595	6,857,610
Provision for impairment losses	(1,603,202)	(1,603,202)	(1,527,769)
	5,796,393	**5,796,393**	**5,329,841**

Interest rates on loans approved in 2010 and 2009 ranged, mostly, from 2% to 6% annually, depending on the purpose of the loan and area of investments.

Notes to the Financial Statements (continued)

for the year ended 31 December 2010

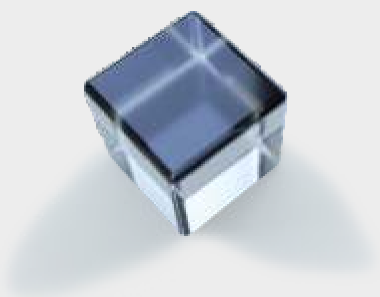
(All amounts are expressed in HRK thousand)

14. Financial assets at fair value through profit or loss

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Shares in investment funds recognised at fair value through profit or loss	500	-	-
Balance as at 31 December	**500**	**-**	**-**

15. Assets available for sale

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Debt securities:			
Listed debt securities:			
Bonds of the Ministry of Finance of the Republic of Croatia	131,618	131,618	153,311
Treasury bills of the Ministry of Finance of the Republic of Croatia	39,966	39,966	69,525
Accrued interest	1,970	1,970	2,442
	173,554	**173,554**	**225,278**
Equity securities:			
Unlisted equity securities:			
Investments in shares of foreign legal entities	23	23	20
Investments in financial institutions shares	161	161	161
Shares of foreign financial institutions – EIF (Note 28)	12,921	12,921	12,729
Investments in company's shares	29,030	29,030	13,686
Provision for impairment losses	(29,030)	(29,030)	(13,686)
	13,105	**13,105**	**12,910**
Investments in investment funds:			
Shares classified as assets available for sale	1,051	-	-
	1,051	**-**	**-**
Balance as at 31 December	**187,710**	**186,659**	**238,188**



15. Assets available for sale (continued)

The movements in the provision for impairment losses on assets available for sale may be summarized as follows:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Balance as at 1 January	13,686	13,686	13,673
Transferred from off-balance sheet	-	-	-
Increase of provisions for impairment losses on assets available for sale	19,049	19,049	1,367
Release of provisions for impairment losses on assets available for sale	(3,705)	(3,705)	(1,354)
Balance as at 31 December	**29,030**	**29,030**	**13,686**

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-125A) issued with foreign currency clause on 23 January 2003 are repayable over 9 years with an interest rate of 6.875%. As of 31 December 2010, the value of these outstanding bonds amounted to HRK 46,083 thousand (31 December 2009: HRK 45,810 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-19BA) issued with foreign currency clause on 29 November 2004 are repayable over 15 years with an interest rate of 5.375%. As of 31 December 2010, the value of these outstanding bonds amounted to HRK 9,542 thousand (31 December 2009: HRK 10,594 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-142A) issued with foreign currency clause on 10 February 2004 are repayable over 10 years with an interest rate of 5.5%. As of 31 December 2010, the value of these outstanding bonds amounted to HRK 75,993 thousand (31 December 2009: HRK 73,792 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-103A) issued in HRK on 8 March 2005 are repayable over 5 years with an interest rate of 6.75% were realised as regularly due on 8 March 2010 (31 December 2009: HRK 23,115 thousand).

Treasury Bills of the Ministry of Finance (RHMF-T-101A) issued in HRK auctioned on 5 October 2010 mature after 91 days and bear an interest rate of 1.95%. As of 31 December 2010 the value of these outstanding treasury bills amounted to HRK 9,997 thousand and they were realised as regularly due on 7 January 2011.

Treasury Bills of the Ministry of Finance (RHMF-T-103A) issued in HRK auctioned on 19 October 2010 mature after 91 days and bear an interest rate of 2.00%. As of 31 December 2010 the value of these outstanding treasury bills amounted to HRK 29,969 thousand and they were realised as regularly due on 20 January 2011.

Treasury Bills of the Ministry of Finance (RHMF-T-037E) issued with foreign currency clause auctioned on 15 September 2009 mature after 364 days and bear an interest rate of 7.2% were realised as regularly due on 16 September 2010 (31 December 2009: HRK 20,867 thousand).

Treasury Bills of the Ministry of Finance (RHMF-T-040E) issued with foreign currency clause auctioned on 6 October 2009 mature after 364 days and bear an interest rate of 6.8% were realised as regularly due on 7 October 2010 (31 December 2009: HRK 34,733 thousand).

15. Assets available for sale (continued)

Treasury Bills of the Ministry of Finance (RHMF-T-044E) issued with foreign currency clause auctioned on 3 November 2009 mature after 364 days and bear an interest rate of 5,9% were realised as regularly due on 4 November 2010 (31 December 2009: HRK 13,925 thousand).

In February 2007, HBOR made acquisitions of three, and in July 2007 of two more, shares of the European Investment Fund (EIF). The payment made represents 20% of the nominal amount of purchased shares and the other 80% makes a contingent liability towards EIF. On 31 December 2010 this contingent liability was EUR 4 million (Note 28).

The General Meeting, acting on a proposal from the Board of Directors, may require payment of the subscribed but not paid capital to the extent required for the Fund to meet its liabilities towards its creditors. Such payment shall be effected within 90 days from the decision of the General Meeting.

Corporate shares comprise shares in capital of the company for the production of agricultural products, Vinka d.d. and of the shipyard company Brodogralište Viktor Lenac d.d., Rijeka. The shares were acquired within restructuring measures for those companies in exchange for a portion of receivables.

In March 2010, when all preconditions were met, HBOR's receivables were partly turned into an ownership share in the company Vinka d.d., Vinkovci amounting to HRK 16,725 thousand, representing a 5.1823% of the ownership share belonging to HBOR in the company's equity. At the 94th meeting of HBOR's Supervisory Board, held on 26 May 2009, the decision has been reached approving the transformation of a part of HBOR's receivables into ownership share in the company, within the framework of the implementation of the Decision of the Government of the Republic of Croatia on ownership restructuring and financial consolidation of the company Lipovac d.d., Lipovac dated 7 April 2005, the Decision of the Government of the Republic of Croatia on changes and amendments to the Decision on ownership restructuring and financial consolidation of the company Lipovac d.d., Lipovac dated 22 March 2007 and the Decision of the Government of the Republic of Croatia on changes and amendments to the Decision on ownership restructuring and financial consolidation of the company Vinka d.d., Vinkovci dated 31 July 2008. HBOR debited its income and effected a 100% impairment of value for the complete amount of receivables from the company, since they were estimated uncollectable.

The shares of the company Vinka d.d., Vinkovci (LPVC-R-B) are not listed.

Upon the commencement of bankruptcy proceedings of the company Brodogradilište Viktor Lenac d.d. in December 2003, HBOR effected a 100% impairment of value for the complete amount of receivables from the company, since they were estimated uncollectable, and the receivables were classified as bad and doubtful receivables.

On the conclusion of the bankruptcy proceedings in April 2008, the equity of the shipyard company was divided into 12,407,813 common shares in the nominal value of HRK 10.00 per share, issued in the procedure of conclusion of the bankruptcy proceedings by registration of rights – receivables in cash. HBOR registered a part of recognized receivables in the amount of HRK 13,673 thousand from the bankruptcy proceedings into the equity of the debtor, by which the Bank acquired 11.0194% of the equity of the company. The conversion of a portion of receivables into the equity in the above mentioned amount has been recorded and stated with a 100% value adjustment, transferred from off-balance sheet. The company's shares (VLEN-R-B) were listed in 2008 at the Zagreb Stock Exchange, and trade started in May 2009. Quoted price per share as of 31 December 2010 amounted to HRK 9,00.

Pursuant to the decision of the subsidiary's management dated 28 December 2010, shares in investment funds were classified as assets available for sale.

16. Assets held to maturity

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Debt securities:			
Listed debt securities:			
Bonds of the Ministry of finance of the Republic of Croatia	1,055	-	-
Accrued interest	22	-	-
Balance as at 31 December	**1,077**	**-**	**-**

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-142A) issued with foreign currency clause on 10 February 2004 are repayable over 10 years with an interest rate of 5.5%. As of 31 December 2010, the value of these outstanding bonds amounted to HRK 1,055 thousand (31 December 2009: HRK 0 thousand).

17. Investments in subsidiaries

As at 31 December 2010, the Bank's subsidiaries are as follows:

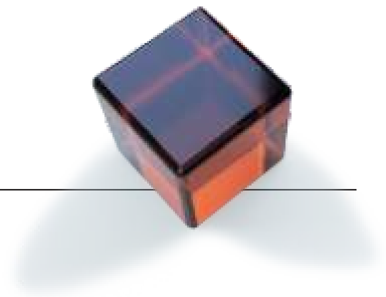
	Activity	Ownership 2010	Ownership 2009	Investment 2010	Investment 2009
Direct share					
Hrvatsko kreditno osiguranje d.d. Zagreb, Republic of Croatia	Providing insurance for company's foreign and domestic short-term receivables regarding shipments of goods and services	51%	-	19,125	-
TOTAL				**19,125**	**-**

On 24 September 2009, Croatian Financial Services Supervisory Agency (HANFA) gave authorization to start-up a new company under the name Hrvatsko kreditno osiguranje dioničko društvo za osiguranje (Hrvatsko kreditno osiguranje d.d.).

The company was registered in the court register on 18 January 2010. The first payment of HBOR's share in owner's equity amounted to HRK 15.3 million and was carried out on 29 January 2010 and the remaining share of HRK 3,825 thousand was paid-in by HBOR on 12 April 2010.

The remaining 49% interest in Hrvatsko kreditno osiguranje d.d. belongs to the Austrian export-credit agency, Oesterreichische Kontrolbank Südosteuropa Holding Ges.m.b.H.

On 26 October 2010, the subsidiary Hrvatsko kreditno osiguranje d.d. established a company Poslovni info servis d.o.o., which is 100% owned by Hrvatsko kreditno osiguranje d.d. and the equity investment amounted to HRK 2,000 thousand. The activities of the company Poslovni info servis d.o.o. are providing analysis, credit risk assessment and information on creditworthiness.



Notes to the Financial Statements (continued)
for the year ended 31 December 2010
(All amounts are expressed in HRK thousand)

18. Investments in associates

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Investments in associates	23,687	23,687	23,687
Value adjustments	(23,687)	(23,687)	(23,687)
	-	-	-

Investments in associates were carried out within a Program of investments in the equity of companies – small and medium sized entrepreneurs or pursuant to single decisions of authorized bodies of HBOR. The investments were made for a period ranging from 4 to 6 years with the right of HBOR to sell the shares after the contracted term of holding an equity stake. HBOR has a significant influence in the associated companies through its representative in the Supervisory Board.

	Line of business	% ownership in 2010	% ownership in 2009
	Production of plastic products	17,96%	17,96%
THC d.d., Obrovac	Production of metal products	38,45%	38,45%
Tri D Drvo d.o.o., Vrhovine	Wood processing, production of wood products	26,00%	26,00%
Pounje d.d., Hrvatska Kostajnica	Textile industry – clothes production	18,36%	18,36%
Metal-Sint Oklaj d.d., Oklaj	Metal industry sintered products and composed material production	40,84%	40,84%

The value of investment was 100 % adjusted in prior years due to assessed un recoverability of the investment.

Notes to the Financial Statements (continued)
for the year ended 31 December 2010
(All amounts are expressed in HRK thousand)

19. Property, plant and equipment and intangible assets

Group 2010	Buildings HRK '000	Computers HRK '000	Furniture, equipment and vehicles HRK '000	Property, plant and equipment and intangible assets not ready for use HRK '000	Total property, plant and equipment HRK '000	Intangible assets HRK '000	Total HRK '000
Cost							
At 31 December 2009	**51,047**	**14,547**	**11,903**	**21,304**	**98,801**	**14,381**	**113,182**
Additions	-	-	-	10,193	10,193	-	10,193
Transfer from assets not yet ready for use	25,131	859	960	(28,554)	(1,604)	1,604	-
Disposals	-	(3,335)	(263)	(38)	(3,636)	-	(3,636)
At 31 December 2010	**76,178**	**12,071**	**12,600**	**2,905**	**103,754**	**15,985**	**119,739**
Accumulated depreciation							
At 31 December 2009	**12,545**	**11,861**	**10,076**	**-**	**34,482**	**11,696**	**46,178**
Depreciation for 2010	1,610	1,418	847	-	3,875	1,437	5,312
Disposals	-	(3,334)	(256)	-	(3,590)	-	(3,590)
At 31 December 2010	**14,155**	**9,945**	**10,667**	**-**	**34,767**	**13,133**	**47,900**
Net book value at 31 December 2010	**62,023**	**2,126**	**1,933**	**2,905**	**68,987**	**2,852**	**71,839**
Net book value at 31 December 2009	**38,502**	**2,686**	**1,827**	**21,304**	**64,319**	**2,685**	**67,004**

19. Property, plant and equipment and intangible assets (continued)

Bank 2010	Buildings HRK '000	Computers HRK '000	Furniture, equipment and vehicles HRK '000	Property, plant and equipment and intangible assets not ready for use HRK '000	Total property, plant and equipment HRK '000	Intangible assets HRK '000	Total HRK '000
Cost							
At 31 December 2009	**51,047**	**14,547**	**11,903**	**21,304**	**98,801**	**14,381**	**113,182**
Additions	-	-	-	9,750	9,750	-	9,750
Transfer from assets not ready for use	25,131	859	926	(28,111)	(1,195)	1,195	-
Disposals	-	(3,335)	(345)	(38)	(3,718)	-	(3,718)
At 31 December 2010	**76,178**	**12,071**	**12,484**	**2,905**	**103,638**	**15,576**	**119,214**
Accumulated depreciation							
At 31 December 2009	**12,545**	**11,861**	**10,076**	**-**	**34,482**	**11,696**	**46,178**
Depreciation for 2010	1,610	1,418	845	-	3,873	1,391	5,264
Disposals	-	(3,334)	(312)	-	(3,646)	-	(3,646)
At 31 December 2010	**14,155**	**9,945**	**10,609**	**-**	**34,709**	**13,087**	**47,796**
Net book value at 31 December 2010	**62,023**	**2,126**	**1,875**	**2,905**	**68,929**	**2,489**	**71,418**
Net book value at 31 December 2009	**38,502**	**2,686**	**1,827**	**21,304**	**64,319**	**2,685**	**67,004**

19. Property, plant and equipment and intangible assets (continued)

Bank 2009	Buildings HRK '000	Computers HRK '000	Furniture, equipment and vehicles HRK '000	Property, plant and equipment and intangible assets not ready for use HRK '000	Total property, plant and equipment HRK '000	Intangible assets HRK '000	Total HRK '000
Cost							
At 31 December 2008	**50,957**	**11,920**	**12,127**	**19,052**	**94,056**	**12,505**	**106,561**
Additions	-	-	-	6,976	6,976	-	6,976
Transfer from assets not ready for use	90	2,649	109	(4,724)	(1,876)	1,876	-
Disposals	-	(22)	(333)	-	(355)	-	(355)
At 31 December 2009	**51,047**	**14,547**	**11,903**	**21,304**	**98,801**	**14,381**	**113,182**
Accumulated depreciation							
At 31 December 2008	**11,000**	**10,009**	**9,314**	**-**	**30,323**	**10,147**	**40,470**
Depreciation for 2009	1,545	1,874	1,089	-	4,508	1,549	6,057
Disposals	-	(22)	(327)	-	(349)	-	(349)
At 31 December 2009	**12,545**	**11,861**	**10,076**	**-**	**34,482**	**11,696**	**46,178**
Net book value at 31 December 2009	**38,502**	**2,686**	**1,827**	**21,304**	**64,319**	**2,685**	**67,004**
Net book value at 31 December 2008	**39,957**	**1,911**	**2,813**	**19,052**	**63,733**	**2,358**	**66,091**

20. Non-current assets held for sale

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Non-current assets held for sale	34,361	34,361	32,862
	34,361	**34,361**	**32,862**

In 2010, HBOR took over non-current assets held for sale of HRK 2,465 thousand (2009: HRK 5,693 thousand) comprised of: land HRK 196 thousand (2009: HRK 1,366 thousand), buildings of HRK 2,269 thousand (2009: HRK 2,373 0 thousand), apartments of HRK 0 thousand (2009: HRK 1,954 thousand). Fair value of taken over non–current assets held for sale amounts to HRK 2,530 thousand (2009: HRK 4,735 thousand), of which: land HRK 193 thousand (2009: HRK 1,222 thousand), buildings HRK 2,337 thousand (2009: HRK 1,966 thousand) and apartments HRK 0 thousand (2009: HRK 1,547 thousand).

In 2010, HBOR sold non-current assets held for sale of HRK 964 thousand (2009: HRK 6,175 thousand) comprised of: land of HRK 182 thousand (2009: HRK 142 thousand), buildings of HRK 557 thousand (2009: HRK 3,555 thousand), apartments of HRK 225 thousand (2009: HRK 2,478 thousand).

The movements in the provision for impairment losses on non-current assets held for sale may be summarized as follows:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Balance as of 1 January	6,739	6,739	284
Increase of provisions for impairment losses on non-current assets held for sale	3	3	6,529
Write-offs	-	-	(74)
Derecognition of impairment due to the sale of non-current assets held for sale	(243)	(243)	-
Balance as of 31 December	**6,499**	**6,499**	**6,739**

21. Other assets

	Group HRK 000	2010 Bank HRK 000	2009 Bank HRK 000
Fees receivable	2,560	2,560	2,420
Premium receivables	459	-	-
Receivables for reinsurance commissions	172	-	-
Receivables for risk assessment fees	76	-	-
Deferred tax assets	181	-	-
Other assets	5,513	5,534	5,635
	8,961	**8,094**	**8,055**
Provision for impairment losses	(4,496)	(4,496)	(3,619)
	4,465	**3,598**	**4,436**

The movements in the provision for impairment losses on other assets may be summarized as follows:

	Group HRK 000	2010 Bank HRK 000	2009 Bank HRK 000
Balance as at 1 January	3,619	3,619	148
Increase of provision for impairment losses on other assets	2,434	2,434	3,871
Release of provision for impairment losses on other assets	(1,528)	(1,528)	(355)
Collection of off-balance sheet receivable items	(10)	(10)	(67)
Provisions transferred from off-balance sheet	10	10	67
Write-offs	(8)	(8)	(14)
Transfer to off-balance sheet	(21)	(21)	(31)
Balance as of 31 December	**4,496**	**4,496**	**3,619**

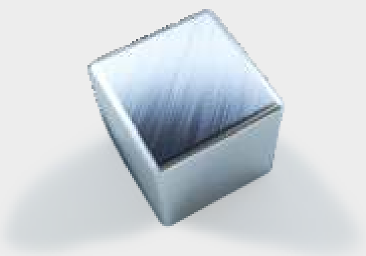
22. Deposits

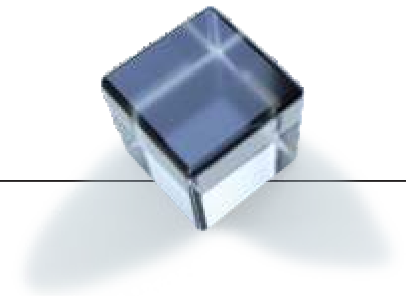
	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Bank deposits	718	718	598
Foreign currency accounts of the companies	171	171	99
Foreign currency account of the Ministry of Finance of the Republic of Croatia	26,847	26,847	19,519
Foreign currency special purpose accounts of the companies	1,500	1,500	797
Deposits by local authorities and state funds	60,463	60,463	57,902
Deposits by state institutions	132,959	132,959	125,925
	222,658	**222,658**	**204,840**

The foreign currency account of the Ministry of Finance of the Republic of Croatia relates to the Export Insurance Guarantee Fund comprising of reinsurance premiums paid for export insurance operations of HRK 13,442 thousand (2009: HRK 12,822 thousand), grant funds provided by the Global Environment Facility (GEF) aimed at the Renewable Energy Resources Project of HRK 8,394 thousand (2009: HRK 2,117 thousand), the grant funds provided by the GEF aimed at the Programme of issuing bank guarantees for energy efficiency projects within the Energy Efficiency Project of HRK 5,011 thousand (2009: HRK 4,580 thousand), all managed by HBOR for and on behalf of the Republic of Croatia.

Demand deposits by State institutions relate to the Bank's operations carried out for and on behalf of, the Ministry of Finance of the Republic of Croatia, the Ministry of the Economy, Labour and Entrepreneurship, the Ministry of the Sea, Transport and Infrastructure, the Ministry of Agriculture, Fisheries and Rural Development, the Fund for Development and Employment, Regional Development Fund of the Republic of Croatia, Vodovod i kanalizacija d.o.o., Split and the Croatian Agency for Small Business ('HAMAG').

HBOR does not pay interest on the above deposits, except on bank deposits and deposits from foreign financial institutions.





23. Borrowings

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Balance as of 1 January	5,186,993	5,186,993	4,994,207
New borrowings	4,110,062	4,110,062	2,594,961
Repayments	(2,331,936)	(2,331,936)	(2,382,626)
Net foreign exchange gains/(losses)	50,715	50,715	(19,549)
	7,015,834	7,015,834	5,186,993
Accrued interest	31,581	31,581	29,148
Balance as of 31 December	**7,047,415**	**7,047,415**	**5,216,141**

Interest rates on borrowings in 2010 and 2009, respectively, ranged from 2% fixed per annum to variable interest rates on the International money market (LIBOR EUR; EURIBOR) increased by 0.225 – 3.25 percentage points annually.

The Bank is subject to different financial covenants arising from contracts. During 2010, the Bank was in compliance with all the required contractual financial covenants.

24. Bonds payable

The book value of bonds includes interest.

Group and Bank	Effective interest rate %	Fair value 2010 HRK '000	Net book value 2010 HRK '000	Fair value 2009 HRK '000	Net book value 2009 HRK '000
Bonds EUR 100 million	5,899	300,411	295,407	438,942	438,372
Bonds EUR 300 million	5,021	2,220,005	2,215,185	2,211,148	2,188,359
Bonds EUR 150 million	4,836	1,075,288	1,106,969	1,028,917	1,094,927
Bonds EUR 250 million	5,076	1,769,785	1,838,839	1,724,875	1,818,228
Bonds EUR 250 million	8,58	1,928,361	1,809,553	1,908,544	1,770,649
Accrued interest		-	216,300	-	214,608
		7,293,850	**7,482,253**	**7,312,426**	**7,525,143**

24.Bonds payable (continued)

According to the Agreement dated 28 November 2002 between HBOR and J.P. Morgan Europe Limited (as lead manager), HBOR issued Amortizing Notes due in 2008 - 2012 under the EMTN program on 4 December 2002, with a guarantee of the Republic of Croatia of EUR 100,000 thousand (HRK 295,407 thousand as at 31 December 2010 and HRK 438,372 thousand as at 31 December 2009) and with a maturity period of 10 years and a fixed interest rate of 5.75%. Interest is paid annually, in arrears. The first instalment was due and paid in December 2008 and the amount outstanding as at 31 December 2010 was HRK 295,407 thousand (EUR 40,000 thousand). Bonds are listed in Luxembourg Stock Exchange quotation.

According to the Agreement between HBOR and Deutsche Bank AG London and UBS Limited (as joint lead managers), HBOR issued bonds under the EMTN program on 11 February 2004, with a guarantee of the Republic of Croatia of EUR 300,000 thousand (HRK 2,215,185 thousand as at 31 December 2010 and HRK 2,188,359 thousand as at 31 December 2009) and with a maturity period of 7 years and a fixed interest rate of 4.875%. Interest is paid annually, in arrears (see Note 35.3.). Bonds are listed in Luxembourg Stock Exchange and Zagreb Stock Exchange quotation (see Note 36.3.).

According to the Agreement between HBOR and Deutsche Bank AG London (as lead manager), HBOR issued bonds on 11 July 2006 of EUR 150,000 thousand (HRK 1,106,969 thousand as of 31 December 2010 and HRK 1,094,927 thousand as at 31 December 2009) with a maturity period of 10 years and a fixed interest rate of 4.807% and amortized repayment in the period from 2012 to 2016. Interest is paid annually, in arrears. Bonds are listed in London Stock Exchange quotation.

According to the Agreement between HBOR and UBS Investment Bank and Deutsche Bank AG London (as joint lead managers), HBOR issued bonds on 14 June 2007 of EUR 250,000 thousand (HRK 1,838,839 thousand as at 31 December 2010 and HRK 1,818,228 thousand as at 31 December 2009) with maturity period of 10 years and fixed interest rate of 5.0%. Interest is paid annually, in arrears. Bonds are listed in Luxembourg Stock Exchange quotation.

According to the Agreement between HBOR and Deutsche Bank AG London, HBOR issued bonds on 3 September 2009 of EUR 250,000 thousand (HRK 1,809,553 thousand as at 31 December 2010 and HRK 1,770,649 thousand as at 31 December 2009) with maturity period of 3 years and fixed interest rate of 7.25%. Interest is paid annually, in arrears. Bonds are listed in Frankfurt Stock Exchange quotation.

Notes to the Financial Statements (continued)
for the year ended 31 December 2010
(All amounts are expressed in HRK thousand)

25. Other liabilities

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Deferred recognition of interest income	786,057	786,057	790,317
Liabilities in respect of subsidized interest	258,279	258,279	201,623
Provisions for guarantees and commitments	53,856	53,856	110,204
Liabilities for preferential financing of housing loans with State support	-	-	32,410
Provisions for other liabilities	46,012	45,912	25,139
Accrued salaries	3,870	3,764	4,098
Deferred recognition of income from fees on issued guarantees	2,782	2,782	3,079
Liabilities to suppliers	1,341	1,168	1,100
Liabilities for prepaid receivables	5,089	5,089	417
Deferrable premium	309	-	-
Provisions for claims	126	-	-
Liabilities to re-insurers	969	-	-
Other liabilities	3,628	3,288	2,216
	1,162,318	**1,160,195**	**1,170,603**

Liabilities in respect of subsidized interest represent advances taken in respect of interest subsidies on loans, which are provided for final customers at a lower interest rate in accordance with the following programmes implemented by HBOR for and on behalf of the Republic of Croatia (see Note 29). These liabilities include:

- HRK 244,920 thousand in respect of the Programme of Preferential Financing through HBOR's Loan Programmes (2009: HRK 185,899 thousand),
- HRK 11,079 thousand in respect of the Financing Model for the Reconstruction and Modernisation of the Fishing Fleet (2009: HRK 12,689 thousand),
- HRK 1,800 thousand in respect of the Environmental protection and energy efficiency fund and Energy efficiency project (2009: HRK 1,207 thousand),
- HRK 480 thousand (2009: HRK 1,828 thousand) in respect of loans granted to the borrowers investing into entrepreneurial zones.

25. Other liabilities (continued)

Deferred recognition of interest income of HRK 786,057 thousand (2009: HRK 790,317 thousand) consists of state subsidies for interest in respect of loans which are provided and drawn down by final borrowers at lower interest rates (see Note 2) but are not yet in repayment stage, amounting to HRK 115,551 thousand (2009: HRK 148,963 thousand), and in respect of those already in repayment stage amounting to HRK 670,506 thousand (2009: HRK 641,354 thousand) (see Note 2).

Provisions for guarantees and commitments represent the best estimation of the outflow for settlement of the outstanding liabilities at the Statement of Financial Position date and are determined in accordance with IAS 37 – Provisions, contingent liabilities and contingent assets.

Out of the total provisions for guarantees and commitments, HRK 31,692 thousand relates to banks (2009: HRK 14,229 thousand), HRK 14,644 thousand relates to domestic companies (2009: HRK 79,712 thousand), HRK 2,787 thousand relates to state-owned companies (2009: HRK 6,197 thousand), HRK 150 thousand relates to the public sector (2009: HRK 183 thousand), HRK 0 thousand relates to foreign companies (2009: HRK 1,773 thousand), HRK 0 thousand relates to non-profit institutions (2009: HRK 105 thousand) and HRK 4,583 thousand relates to others (2009: HRK 8,005 thousand).

Movements in the provision for guarantees, commitments and other liabilities may be summarized as follows:

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Balance as at 1 January	110,204	110,204	145,797
Increase in provision for guarantees and commitments	88,616	88,616	203,356
Release in provision for guarantees and commitments	(145,164)	(145,164)	(239,398)
Net foreign exchange gains/(losses) on provision for impairment losses	200	200	449
Provision for guarantees and commitments	**53,856**	**53,856**	**110,204**
Balance as at 1 January	25,139	25,139	17,338
Increase in provision for other liabilities	25,057	24,957	7,801
Release in provision for other liabilities	(4,184)	(4,184)	-
Provisions for other liabilities	**46,012**	**45,912**	**25,139**
Balance as at 31 December	**99,868**	**99,768**	**135,343**

26. Founder's capital and reserves

Under the HBOR Act, the prescribed founder's capital should amount to HRK 7,000,000 thousand, paid from the State Budget and from other sources as specified by separate laws.

The schedule of annual amounts of payment and the time schedule of payments out of the State Budget into the capital is not set in advance, but is determined by the Croatian Parliament as part of the process of adoption of the State Budget of the Republic of Croatia.

Within its Accounting policies, the Group has set out its objectives of capital management, as well as measuring and assessing the policies for capital management. Capital management is described and presented in Note 34.

Founder's capital of the subsidiary Hrvatsko kreditno osiguranje d.d. amounts to HRK 37,500 thousand and is 51% owned by the Bank, and the founder's capital of the company Poslovni info servis amounts to HRK 2,000 thousand and is 100% owned by Hrvatsko kreditno osiguranje d.d. The capital of both companies is subscribed and paid in full.

27. Guarantee fund

Group and Bank	HRK '000
Balance as of 1 January 2009	**12,423**
Write-off	(427)
Net foreign exchange	(33)
Balance as of 31 December 2009	**11,963**
Write-off	-
Net foreign exchange	129
Balance as of 31 December 2010	**12,092**

The Guarantee fund, of HRK 12,092 thousand and HRK 11,963 thousand as of 31 December 2010 and 2009 respectively, relates to funds of the guarantee fund from Deutsche Investitions- und Entwicklungsgesellschaft (DEG) in respect of a financial contribution (granted funds) for the account of the German Government, which are used for covering contingent losses on guarantees issued for loans granted under the Programme for financing business start-ups in Croatia. The funds of the Guarantee fund are unconditionally contributed and have no maturity. The funds of the Guarantee fund give the Government of the Federal Republic of Germany neither controlling rights nor a right to a share of the operating results of the Group."

Recognised increase compared to the previous year is due to foreign exchange gains amounting to HRK 129 thousand.

28. Guarantees and commitments

In its regular activities, the Bank contracts various commitments and contingent liabilities. The purpose of these instruments is to ensure that the funds are available to a customer when required.

These obligations contain credit risk and are therefore part of the overall risk of the Group although they are not recognised in the Statement of financial position.

	Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
Guarantees issued in HRK	518	518	518
Guarantees issued in foreign currency	352,685	352,685	693,340
Issued bills of exchange	28,472	28,472	34,597
Undrawn loans	951,951	951,951	1,076,475
EIF – subscribed, not called up capital (note 15)	29,541	29,541	29,225
	1,363,167	1,363,167	1,834,155
Provisions for guarantees and commitments	(53,856)	(53,856)	(110,204)
	1,309,311	**1,309,311**	**1,723,951**

Guarantees

Issued guarantees oblige the Bank to make payments on behalf of customers if the customer is unable to honour its commitments towards third parties or in the event of a specific act, generally related to the export or import of goods and other purposes specified in the contracts with the customers. Guarantees bear the same credit risk as loans.

Bank guarantees are for the most part guaranteed by the Government of the Republic of Croatia.

Commitments upon undrawn loans

The Bank has an obligation to disburse funds for loans and revolving loans upon committed undrawn loans. The expiry date of disbursement or other termination clause is determined by the contract. Disbursements are exercised in several withdrawals, depending on the purpose of the loan, phase of the project or documentation needed for disbursement. Since commitments may expire without being drawn upon, the total contractual amounts do not necessarily represent future cash outflows.

Committed undrawn loans include less potential credit risk than loans, since most commitments depend upon meeting specific terms and conditions by the customers in order to use the funds. The Bank monitors the terms to maturity of loan commitments.

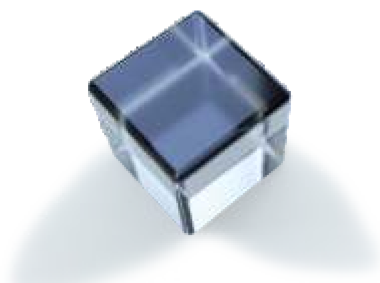
Notes to the Financial Statements (continued)
for the year ended 31 December 2010
(All amounts are expressed in HRK thousand)

29. Managed funds for and on behalf of third parties

The Group manages funds on behalf of and for the account of the Ministry of Finance, the Ministry of the Economy, Labour and Entrepreneurship, the Ministry of the Sea, Transport and Infrastructure, the Ministry of Agriculture, Fisheries and Rural Development, the Ministry of Regional Development, Forestry and Water Management, the Environmental and Energy Efficiency Fund, Vodovod i kanalizacija d.o.o., Split and the Croatian Agency for Small Businesses ("HAMAG"), that are mainly used for various reconstruction and development programmes. These assets are separated from the Group's assets. The income and expense relating to these transactions are charged to the beneficiary, and the Group does not have any other liabilities. The Group charges a fee for part of the services and part of the services are performed free of charge depending on the contract with the customer and taking into account that the stated amounts are insignificant for the Group.

Agency business funds per individual programmes amount to:

Programme	**2010 HRK '000**
Development and Reconstruction of Rural Housing	71,117
Employment of Former Soldiers	528,864
Emergency Reconstruction Project (loan IBRD 3760 - HR)	228
Loans to companies having difficulties – Ministry of Finance funds	49,519
Municipal Environmental Infrastructure Investment Program – MEIP	753,298
Collection of receivables under HAMAG guarantees	264
Insurance of export transactions	217,675
Programme of Preferential Financing through HBOR's Loan Programmes	244,920
Programme for Development and Employment - loans	99,175
Programme for Regional Development of the Republic of Croatia - loans	25,446
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of the Economy, Labour and Entrepreneurship	38,293
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of the Sea, Transport and Infrastructure	40,326
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of Agriculture, Fisheries and Rural Development	51,779
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of the Economy, Labour and Entrepreneurship - interest subsidy	384
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of the Sea, Transport and Infrastructure - interest subsidy	1,561
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of Agriculture, Fisheries and Rural Development - interest subsidy	9,134
Renewable Energy Resources Project	22,122
VIK – EKO account A – dedicated water charge	437,346
VIK – EKO account B - VAT	121,509
The Environment and Energy Efficiency Fund - interest subsidy	800
Programme of Issuing Bank Guarantees for Energy Efficiency Projects – IBRD	5,011
HBOR Loan Programme for the Energy Efficiency Projects – interest subsidy	1,000
Interest subsidies for the loans to the entrepreneurs who invest in entrepreneurial	480
Operational Programme for the development of cattle-breeding production	45,530
Operational Programme for the development of pig-breeding production	28,231
	2,794,012



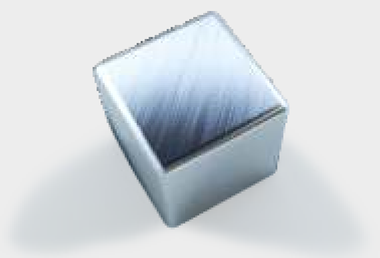
29. Managed funds for and on behalf of third parties (continued)

Beside the mentioned transactions for and on behalf of its principles, the Bank manages assets for the coverage of technical provisions of its subsidiary company, Hrvatsko kreditno osiguranje d.d. These funds are managed separately from the Bank's assets. Revenues and expenses relating to these transactions are charged to the principal, and the Bank does not have other liabilities. For the services provided, the Bank charges a fee.

Agency business funds per individual programmes amount to:

Bank

Programme	2010 HRK '000	2009 HRK '000
Development and Reconstruction of Rural Housing	71,117	78,796
Employment of Former Soldiers	528,864	503,952
Emergency Reconstruction Project (loan IBRD 3760 - HR)	228	291
Loans to companies having difficulties – Ministry of Finance funds	49,519	67,500
Municipal Environmental Infrastructure Investment Program – MEIP	753,298	733,298
Collection of receivables under HAMAG guarantees	264	275
Insurance of export transactions	217,675	206,336
Programme of Preferential Financing through HBOR's Loan Programmes	244,920	185,899
Programme for Development and Employment - loans	99,175	275,420
Programme for Regional Development of the Republic of Croatia - loans	25,446	27,614
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of the Economy, Labour and Entrepreneurship	38,293	38,293
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of the Sea, Transport and Infrastructure	40,326	40,326
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of Agriculture, Fisheries and Rural Development	51,779	51,779
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of the Economy, Labour and Entrepreneurship - interest subsidy	384	854
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of the Sea, Transport and Infrastructure - interest subsidy	1,561	2,031
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of Agriculture, Fisheries and Rural Development - interest subsidy	9,134	9,804
Renewable Energy Resources Project	22,122	9,052
VIK – EKO account A – dedicated water charge	437,346	395,531
VIK – EKO account B - VAT	121,509	110,063
The Environment and Energy Efficiency Fund - interest subsidy	800	207
Programme of Issuing Bank Guarantees for Energy Efficiency Projects – IBRD	5,011	4,580
HBOR Loan Programme for the Energy Efficiency Projects – interest subsidy	1,000	1,000
Interest subsidies for the loans to the entrepreneurs who invest in entrepreneurial zones	480	1,828
Operational Programme for the development of cattle-breeding production	45,530	19,470
Operational Programme for the development of pig-breeding production	28,231	8,704
HKO – Funds for the coverage of technical provisions	1,077	-
	2,795,089	**2,772,903**



Notes to the Financial Statements (continued)
for the year ended 31 December 2010
(All amounts are expressed in HRK thousand)

30. Related-party transactions

Related parties are companies that directly or indirectly, through one or more intermediaries, control, or are controlled by, the reporting company.

The majority of related-party transactions relate to the transactions with the Republic of Croatia, the 100% owner of the Bank and state-owned companies (in which the Republic of Croatia holds 51% or more of the ownership).

All transactions stated were carried out under usual/regular conditions of the Bank.

As of 31 December 2010 and 31 December 2009, balances arising from transactions with related parties, including the Bank's key management personnel, include the following:

a) Related-party transactions

Group	Exposure	Liabilities	Income	Expense
	2010 HRK '000	2010 HRK '000	2010 HRK '000	2010 HRK '000
Owner	291,261	315,172	22,498	16
Government funds, executive authorities and agencies	163,463	96,450	11,903	377
State-owned companies	1,535,581	1,655	72,116	-
Non-controlling interests	106	708	124	937
Associates	3	-	100	-
Key management personnel	2,578	-	95	7
Total	**1,992,992**	**413,985**	**106,836**	**1,337**

Bank	Exposure	Liabilities	Income	Expense	Exposure	Liabilities	Income	Expense
	2010 HRK '000	2010 HRK '000	2010 HRK '000	2010 HRK '000	2009 HRK '000	2009 HRK '000	2009 HRK '000	2009 HRK '000
Owner	291,261	315,172	22,498	16	339,157	280,423	25,358	-
Government funds, executive authorities and agencies	163,463	96,450	11,903	377	208,012	92,910	26,876	-
State-owned companies	1,535,581	1,655	72,116	-	2,055,735	867	100,816	-
Subsidiary companies	19,149	-	-	-	-	-	-	-
Associates	3	-	100	-	14	-	187	1
Key management personnel	2,167	-	88	3	1,837	-	71	2
Total	**2,011,624**	**413,277**	**106,705**	**396**	**2,604,755**	**374,200**	**153,308**	**3**

Exposures include loans to other customers, available-for-sale assets, assets held to maturity, other assets and off-balance sheet exposure relating to guarantees, letters of credit and commitments.

Liabilities include deposits and other liabilities.

Income includes interest income, fee income and decrease in impairment loss and provisions.

Expense includes impairment loss and provisions.

30. Related-party transactions (continued)

b) Collateral received

	2010 Group HRK '000	2010 Bank HRK '000	2009 Bank HRK '000
The Republic of Croatia	1,430,722	1,245,355	1,880,979
State agencies	364,901	364,901	349,400
Total	**1,795,623**	**1,610,256**	**2,230,379**

Collateral received relates to first-class collateral instruments received as security for HBOR's placements comprising the Republic of Croatia guarantees, HAMAG guarantees, insurance policies of export transactions against political and/or commercial risks and statutory guarantees in cases when the Republic of Croatia or other state executive body guarantees the liabilities of certain borrowers pursuant to provisions of certain laws.

HBOR issues reinsurance policies for and on behalf of the Republic of Croatia, i.e. covers a proportional part (quota reinsurance) of political and commercial risks of export loans and receivables arising from export of goods and services. The reinsurer covers all non-marketable (non-market) risks underwritten by the Insurer or *Hrvatsko kreditno osiguranje*, d.d. in the percentage of 70% of an insured amount.

c) Salaries of key management personnel

Salaries include compensation paid for regular work, annual vacation, national holidays, paid leave, sick leave, jubilee awards. In 2010, salaries for the Group amounted to HRK 4,762 thousand and for the Bank HRK 4,324 thousand (2009: HRK 5,666 thousand).

Remuneration for the work of the members of the Supervisory Board in 2010 amounted to HRK 242 thousand for the Group, and 242 thousand (2009: HRK 267 thousand) for the Bank and it relates to the HBOR Supervisory Board member eligible for remuneration and members of supervisory boards at associates who were appointed by HBOR.

31. Risk management

31.1. Introduction

Based on the Act on the Croatian Bank for Reconstruction and Development, the Bank is obliged to mitigate business risks directed by the principles of banking operations.

In the process of risk management, the Bank identifies the sources of risks, continuously measures, estimates, manages and controls all risks to which it is or might be exposed in the course of business. The mode, methods and frequency of measurement and evaluation of risk are prescribed by the general acts of the Bank. The Bank manages credit, market and operating risks using policies, procedures, limits, committees and controls on a daily basis.

Risk management structure

The Supervisory Board is responsible for monitoring the appropriateness and effectiveness of the risk management process in the Bank.

The Managing Board of the Bank is responsible for establishing and implementing an effective and reliable risk management system. The Managing board establishes acts, makes decisions and gives instructions which regulate all areas of business. In order to accomplish its task, the Managing Board delegated their risk management authority to two committees.

Risk management boards

- **Assets and Liabilities Management Committee (ALCO)** – manages liquidity risk, interest rate risk and currency risk within the framework of the Liquidity Risk Management Procedures, the Currency Risk Management Procedures and the Interest Rate Risk Management Procedures as well as other documents of the Bank that regulate this area.
- **Credit Risk Evaluation and Measurement Committee** – manages credit risk within the framework set through accepted Loan Policies, Credit Risk Management Procedures, methodologies and other internal acts that cover issues related to credit risk.
- **HBOR Information System Management Committee** – manages the resources of the information system and adequately manages the risks that result from the use of information technology.

Risk Management Unit

The Bank formed a functionally and organizationally separate and independent organizational unit for the control of business risks, which is directly responsible to the Managing Board. The Risk Management unit is responsible for defining, measuring, monitoring and controlling all risks to which the Bank is exposed or might be exposed. The Risk Management unit carries out its role by performing analyses, evaluations, measurements, controls, by giving suggestions and recommendations for the adequate management of Bank's exposure to risks, by developing risk-related procedures and methodologies, recommending and monitoring accepted exposure limits, assessing the quality of the loan portfolio, reporting to the Managing Board and committees on risks, etc.

The risk management strategy is directed towards achieving and maintaining the system that would provide quality and efficiency in risk management complied with domestic and international banking practices and Croatian National Bank and Basel Committee recommendations.

31. Risk management (continued)

31.1. Introduction (continued)

Organizational Unit for Control and Audit

Control and audit is organized as a separate organizational unit, functionally and organizationally independent from the activities subject to its audit and other organizational units of HBOR. The Control and Audit unit is responsible to the Managing Board, Supervisory Board and Audit committee. The Control and Audit unit verifies the application and efficiency of the procedures and methodologies for risk management. Their role is achieved through testing of the risk management system according to the principles of operational stability, including managing IT resources and other associated technologies.

Organizational Unit for EU Co-operation

The Bank established separate organizational unit EU Co-operation. Within this unit, an independent function of compliance with laws, regulations and professional standards as well as of defining and assessing compliance risk was set up in 2009. Its role is to support the managing bodies of the Bank with compliance risk management and controls and report periodically to the Managing Board and Supervisory Board. Within this function following risks are monitored and controlled: legal and regulatory risks (risk of disobedience of the laws, legislation and professional practice), sanction risk (risk of court, administrative or disciplinary sanctions and/or measures resulted from breaches of law, legislation, rules or contractual provision) and the reputation risk.

Risk measurement and reporting systems

When assessing and measuring risk, the Bank takes into account historical data, business plans, market conditions and the specific characteristics of the Bank as a special financial institution. The results of risk measurements, assessments and analyses carried out are presented at the meetings of the Risk Management Committee, the Managing Board and the Supervisory Board. For risk monitoring and control, a system of limits is introduced for the management of credit risk, liquidity risk, interest rate risk and currency risk. These limits are adopted by the Managing Board and regularly reviewed by the Risk Management Unit, and they are communicated to those organizational units in which risk is generated and which are obliged to comply with them.

The Bank monitors risks also through scenario analyses, sensitivity analyses and stress tests. Systems of pro-active risk management are developed for the purpose of minimizing potential future risks.

Within the framework of managing credit risk, liquidity risk, interest rate risk and currency risk, exposure to these risks is measured and reported through the system of limits and other indicators, whereas reporting frequency and measurement methodologies are determined by the management procedures for these risks.

Management bodies and committees in charge are systematically reported on the quality of the loan portfolio, high exposure and the highest permissible exposure, capital adequacy, collection of risk placements, measures taken and receivables collected, changes in internal ratings and measures taken in case of rating deterioration, open foreign currency positions, interest rate gap as well as liquidity status indicators and projections.

31. Risk management (continued)

31.2. Credit risk

Risk mitigation

The Bank, as a special financial institution, is not profit-oriented and therefore does not trade in derivatives. Derivatives can be used only for hedging of the Bank's positions.

Credit risk encompasses losses derived from full or partial default, i.e. an untimely discharge of a financial obligation by the client.

The Bank controls credit risk by way of credit policies and prescribed procedures which determine internal control systems aiming to act preventively.

The credit risk management system is a crucial part of the Bank's business policy and it is an important strategic factor of business conduct, and therefore this area is regulated by a separate act - Credit risk management procedures, that are applied in all phases of the credit process (from the development of new bank products or from the credit application until its final repayment).

Credit risk management procedures are included in a comprehensive document comprised of separate methodologies aimed at the evaluation of different targeted groups of clients:

- Credit risk evaluation methodology which encompasses collateral valuation methodology,
- Credit scoring methodology,
- Methodology for evaluation and selection of banks,
- Methodology for evaluation and selection of foreign banks.

In the case of direct clients, the Bank uses the Credit risk evaluation methodology (for loans over HRK 700 thousand) or the Credit scoring methodology (for loans below HRK 700 thousand) to determine creditworthiness. The Credit scoring methodology is used to determine creditworthiness of clients that belong to the “small portfolio” is advanced, containing three scoring models: placements up to HRK 200 thousand, placements from HRK 200 thousand to HRK 700 thousand to companies and placements from HRK 200 thousand to HRK 700 thousand to all other entrepreneurs.

Pursuant to the HBOR Act, the Bank approves the part of its placements on-lending via commercial banks and uses Banks evaluation and selection methodology and Methodology for evaluation and selection of foreign banks.

The Bank controls related party risk on the occasion of credit approval and for the duration of a business relationship when it is requested from the clients to state their related parties. The information thereby gathered is verified and the type and nature of intra-relationship is determined as well as the existence of a group of related parties and the occurrence of the influence of the improvement or worsening of economic and financial conditions of one related party to the economic or financial position of the other related party.

31. Risk management (continued)

31.2. Credit risk (continued)

The Bank, as a developmental financial institution, supports growth and development of the Croatian economy through investment construction. For this reason, the clients mainly approach the Bank with applications for credit financing of investment projects. In order to minimize risk and objectively estimate economic sustainability of the project as well as a return on investment, the Bank is constantly improving existing organizational and technical solutions, reports and internal acts and proposes new organization regulations and implementation instructions.

Due to the impact of the economic and financial crisis, HBOR introduced new loan programmes with the objective of improving liquidity and maintaining and expanding the existing scope of the economic entities operations. One of the programmes is the Loan Programme for the Financing of Working Capital aimed at overcoming difficulties in the economy that was introduced as a measure for economic revival and development through the promotion of lending activities with active participation of the state in the financing of sustainable business projects of economic entities and HBOR's sharing of risk with commercial banks in proportion 60% : 40% (commercial bank : HBOR).

By continuous monitoring and evaluation of the clients' businesses, the Bank makes an effort to identify difficulties in their operation on a timely basis. For clients with difficulties, the Bank tries to find appropriate ways to collect receivables by considering the possibilities of alternative repayment terms with a view to continue the production process and employment increase. Special emphasis is placed on identifying and monitoring reasons for bad debts, and procedures for prevention are built in operational procedures with a view to decreasing the share of high risk placements of the Bank.

Also, large exposure limits as well as highest amount of credit risk exposure toward single client and his related parties and concentration (aggregate of large exposures) risk limits were determined.

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and highest credit risk exposure

The table below shows the highest gross credit risk exposures existing in the Statement of Financial Position and in Guarantees and commitments as of the reporting date, before considering collateral received:

	Group Gross highest exposure 2010 HRK '000	Bank Gross highest exposure 2010 HRK '000	Bank Gross highest exposure 2009 HRK '000
Assets			
Cash on hand and due from banks	1,258,725	1,258,008	124,197
Deposits with other banks	137,555	103,284	127,055
Loans to banks	15,449,447	15,449,447	14,866,066
Loans to other customers	5,796,393	5,796,393	5,329,841
Financial assets at fair value through profit or loss	500	-	-
Assets available for sale	187,710	186,659	238,188
Assets held to maturity	1,077	-	-
Other assets	3,083	2,388	3,425
Total	**22,834,490**	**22,796,179**	**20,688,772**
Guarantees and commitments			
Issued guarantees in domestic currency	513	513	513
Issued guarantees in foreign currency	345,184	345,184	682,628
Issued bills of exchange	28,187	28,187	34,251
Undrawn loans	905,886	905,886	977,334
EIF – subscribed, not called up capital	29,541	29,541	29,225
Total	**1,309,311**	**1,309,311**	**1,723,951**
Total credit risk exposure	**24,143,801**	**24,105,490**	**22,412,723**

31. Risk management (continued)

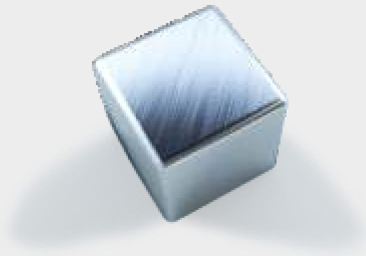
31.2. Credit risk (continued)

Concentration of risk and highest credit risk exposure (continued)

The Bank, with its developmental loan programmes, covers the entire Republic of Croatia with a special emphasis on special concern areas. Credit risk is diversified across geographical areas and developmental credit programmes. Through development of new loan programmes (products), the Bank takes into account concentration of credit risk with a view to evenly develop all areas of the Republic of Croatia.

Through financing of different sectors by stimulating production and development with the purpose of developing the Croatian economy, the Bank is creating a better base for repayment of loans and minimization of risk.

As of 31 December 2010, the highest credit exposure of the Group to one debtor was HRK 1,496,302 thousand and of the Bank was HRK 1,461,313 (31 December 2009: HRK 1,528,299 thousand) after considering collateral received, as the client is included in the risk group "A", i.e. the client is a first class debtor. The collateral policy is disclosed further in note 31.2.



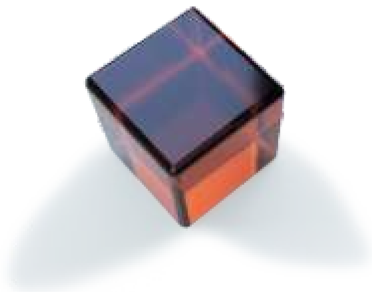
31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and highest credit risk exposure (continued)

Concentration of assets and guarantees and commitments, according to geographical segments, before considering collateral received, is as follows:

Group 2010	Republic of Croatia HRK '000	EU countries HRK '000	Other countries HRK '000	Total HRK '000
Assets				
Cash on hand and due from banks	1,147,254	109,719	1,752	1,258,725
Deposits with other banks	54,031	50,448	33,076	137,555
Loans to banks	15,443,405	-	6,042	15,449,447
Loans to other customers	5,596,981	-	199,412	5,796,393
Financial assets at fair value through profit or loss	500	-	-	500
Assets available for sale	174,766	12,944	-	187,710
Assets held to maturity	1,077	-	-	1,077
Other assets	3,083	-	-	3,083
Total	**22,421,097**	**173,111**	**240,282**	**22,834,490**
Guarantees and commitments				
Issued guarantees in domestic currency	513	-	-	513
Issued guarantees in foreign currency	345,184	-	-	345,184
Issued bills of exchange	-	28,187	-	28,187
Undrawn loans	905,886	-	-	905,886
EIF – subscribed, not called up capital	-	29,541	-	29,541
Total	**1,251,583**	**57,728**	**-**	**1,309,311**
Total credit risk exposure	**23,672,680**	**230,839**	**240,282**	**24,143,801**



Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

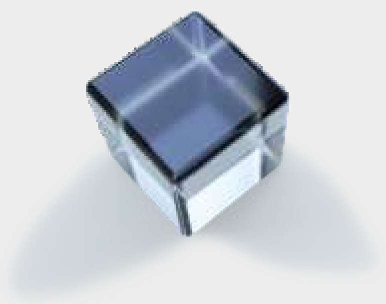
31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and highest credit risk exposure (continued)

Concentration of assets and guarantees and commitments, according to geographical segments, before considering collateral received (continued):

Bank 2010	Republic of Croatia HRK '000	EU countries HRK '000	Other countries HRK '000	Total HRK '000
Assets				
Cash on hand and due from banks	1,146,537	109,719	1,752	1,258,008
Deposits with other banks	19,760	50,448	33,076	103,284
Loans to banks	15,443,405	-	6,042	15,449,447
Loans to other customers	5,596,981	-	199,412	5,796,393
Assets available for sale	173,715	12,944	-	186,659
Other assets	2,388	-	-	2,388
Total	**22,382,786**	**173,111**	**240,282**	**22,796,179**
Guarantees and commitments				
Issued guarantees in domestic currency	513	-	-	513
Issued guarantees in foreign currency	345,184	-	-	345,184
Issued bills of exchange	-	28,187	-	28,187
Undrawn loans	905,886	-	-	905,886
EIF – subscribed, not called up capital	-	29,541	-	29,541
Total	**1,251,583**	**57,728**	**-**	**1,309,311**
Total credit risk exposure	**23,634,369**	**230,839**	**240,282**	**24,105,490**



Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

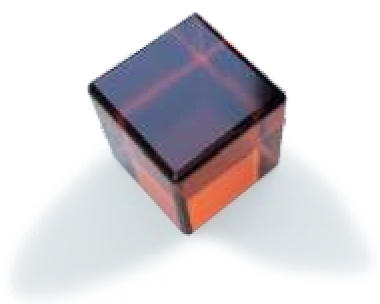
31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and highest credit risk exposure (continued)

Concentration of assets and guarantees and commitments, according to geographical segments, before considering collateral received (continued):

Bank 2009	Republic of Croatia HRK '000	EU countries HRK '000	Other countries HRK '000	Total HRK '000
Assets				
Cash on hand and due from banks	12,586	109,921	1,690	124,197
Deposits with other banks	101,904	-	25,151	127,055
Loans to banks	14,850,534	-	15,532	14,866,066
Loans to other customers	5,123,502	-	206,339	5,329,841
Assets available for sale	225,439	12,749	-	238,188
Other assets	3,405	20	-	3,425
Total	**20,317,370**	**122,690**	**248,712**	**20,688,772**
Guarantees and commitments				
Issued guarantees in domestic currency	513	-	-	513
Issued guarantees in foreign currency	682,628	-	-	682,628
Issued bills of exchange	-	34,251	-	34,251
Undrawn loans	957,025	-	20,309	977,334
EIF – subscribed, not called up capital	-	29,225	-	29,225
Total	**1,640,166**	**63,476**	**20,309**	**1,723,951**
Total credit risk exposure	**21,957,536**	**186,166**	**269,021**	**22,412,723**



31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and highest credit risk exposure (continued)

Concentration of assets and guarantees and commitments, according to industry, before and after considering collateral received, is as follows:

Group	Gross highest exposure 2010 HRK '000	highest exposure 2010 HRK '000
Financial intermediation and insurance	17,481,349	-
Water and electric supply and other infrastructure	1,375,778	991,431
Tourism	822,274	37,924
Transport, warehousing and connections	726,658	21,311
Shipbuilding	569,708	122,868
Agriculture and fishery	438,583	79,329
Food industry	381,534	101,962
Construction industry	342,487	90,674
Other industry	308,388	89,334
Public administration	172,701	172,701
Education	134,369	132,542
Manufacture of basic metals and fabricated metal products, except machinery and equipment	178,336	13,763
Manufacture of chemicals and chemical products	180,333	633
Manufacture of other non-metallic mineral products	181,843	35,001
Other	849,460	227,138
Total credit risk exposure	**24,143,801**	**2,116,611**

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and highest credit risk exposure (continued)

Concentration of assets and guarantees and commitments, according to industry, before and after considering collateral received, is as follows:

Bank	Gross highest exposure 2010 HRK '000	Net highest exposure 2010 HRK '000	Gross highest exposure 2009 HRK '000	Net highest exposure 2009 HRK '000
Financial intermediation and insurance	17,444,835	12	15,941,328	110
Water and electric supply and other infrastructure	1,375,778	991,431	1,572,140	1,157,456
Tourism	822,274	37,924	871,285	46,522
Transport, warehousing and connections	726,658	21,311	778,303	14,716
Shipbuilding	569,708	122,868	939,044	116,692
Agriculture and fishery	438,583	79,329	373,922	116,248
Food industry	381,534	101,962	345,008	108,494
Construction industry	342,487	90,674	175,956	77,555
Other industry	308,388	89,334	168,786	24,240
Public administration	172,701	172,701	223,080	223,080
Education	134,369	132,542	156,015	155,672
Manufacture of basic metals and fabricated metal products, except machinery and equipment	178,336	13,763	186,324	14,330
Manufacture of chemicals and chemical products	180,333	633	588	588
Manufacture of other non-metallic mineral products	181,843	35,001	73,406	542
Other	847,663	225,341	607,538	110,450
Total credit risk exposure	**24,105,490**	**2,114,826**	**22,412,723**	**2,166,695**

Concentration of assets and guarantees and commitments according to industry for both years has been compiled in accordance with the National Classification of Activities 2007 („NKD 2007“). A new national classification was passed in 2007 and in the transitional period until 31 December 2009, the national classification of activities from 2002 was used simultaneously. Since as of 31 December 2010 two comparable periods were in place, the Group started to use NKD 2007 in complete.

In the preparation of the note, a combined approach is applied, which takes into consideration business activities of a debtor, retains the names of activities different from those in the National Classification of Activities and unites similar business activities.

(All amounts are expressed in HRK thousand)

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and highest credit risk exposure (continued)

The fair value of collateral for the Group in 2010 amounted to HRK 22,027,190 thousand and for the Bank HRK 21,990,664 thousand (2009: HRK 20,246,028 thousand).

In the total net exposure of the Bank in 2010, the credit risk of HRK 1,409,048 thousand (2009: HRK 1,614,139 thousand) is not covered with ordinary collateral, but it relates to receivables and received funds from the Republic of Croatia of HRK 270,002 thousand (2009: HRK 275,693 thousand), from local (regional) authorities of HRK 141,121 thousand (2009: HRK 151,502 thousand), state-owned companies for whose commitments the Republic of Croatia guarantees jointly and unconditionally of HRK 134,121 thousand (2009: HRK 193,184 thousand), government funds of HRK 11,251 thousand (2009: HRK 14,314 thousand), government bonds and Treasury bills of the Ministry of Finance of HRK 173,554 thousand (2009: HRK 225,278 thousand). In addition, an amount of HRK 678,999 thousand (2009: HRK 754,168 thousand) relates to receivables from a state-owned company (51%).

Part of the placements with net exposure relates to placements provisionally and partially covered with collateral and the further increase in exposure has been stopped pending the submission of the full collateral necessary for compliance with the requested collateral coverage ratio.

Financial intermediation includes mainly commercial banks; the operation and collateral quality for placements with commercial banks is described further in note 31.2 under Collateral for placements with commercial banks.

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and highest credit risk exposure (continued)

Credit risk exposure by internal credit rating:

Internal credit rating	Historical default rate (%) 2010	Historical default rate (%) 2009	Group 2010	Bank 2010	Group 2009	Bank 2009
A	1.43 %	1.02 %	22,397,582	22,359,271	-	20,352,810
B	15.11 %	13.58 %	1,746,219	1,746,219	-	2,059,913
C	73.13 %	65.57 %	-	-	-	-
	Total		24,143,801	24,105,490	-	22,412,723

The internal methodology is not comparable with rating agencies' methodology, and the stated credit ratings are not comparable with the ratings of world recognized rating agencies.

Credit risk assessment internal methodology

For the evaluation of various target groups of clients, the Bank has prescribed internal methodologies. They represent the basis for decisions on approval of loans, guarantees and letters of credit and one of criteria for determination of the placement risk category.

The methodology for evaluation of credit ratings is applied for the evaluation of credit risk for direct placements to companies over HRK 700 thousand. It comprises two main evaluation areas: client evaluation and project/investment evaluation and the combination of these two evaluations. All evaluation areas consist of three basic parts: financial, non-financial analysis and correction of evaluation based on currency-induced credit risk (VIKR). Clients are classified in 10 ratings depending on total points given through the criteria of the client's creditworthiness, evaluation of project criteria and exposure to VIKR criteria.

Methodologies of credit scoring are used during credit risk evaluation for all direct placements below HRK 700 thousand where the Bank is exposed to credit risk. The final result of scoring determines whether the client is acceptable for credit placement. The quality and value of collateral for the placement are a part of the credit scoring procedure.

The Methodology for evaluation and selection of banks and the Methodology for evaluation and selection of foreign banks are used for evaluation of domestic and foreign banks. The methodologies include the estimation of the financial risk (quantitative evaluation), the estimation of business risks for banks analyzed (qualitative evaluation) and the estimation of reputation risk.

The result of application of the methodologies for the evaluation of banks is the internal rating of the bank.

31. Risk management (continued)

31.2. Credit risk (continued)

Concentration of risk and highest credit risk exposure (continued)

Impairment loss and provisions

The Bank forms provisions for identified losses in accordance with International Financial Reporting Standards and internal procedures. Forming provisions is under the competence of the Credit risk evaluation and measurement committee.

Provisioning on an individual basis

Provisioning on an individual basis represents impairment of partly recoverable and irrecoverable investments (risk groups "B" and "C"). Allocation of placements on an individual basis into risk groups is performed by the following criteria: creditworthiness and the debtors' regularity of repayment upon maturity and the quality of placement collateral. Placements that represent the portfolio of small loans are classified by the criteria of regular repayment upon maturity. The Bank does not determine the present value of discounted cash flows for partially recoverable placements where the expected inflow is expected within one year of the financial statements date.

Provisioning on the collective basis

Provisions on a collective basis are formed for fully recoverable placements or placements and commitments allocated in risk group "A". Allocation of debtors within the risk group is performed according to credit worthiness, industry risk factor, type and the debtor's foreign currency alignment.

Investments which are at least 80% covered by first class collateral are allocated in risk group "A".

The Managing Board of HBOR believes that the policies and procedures of forming provisions are adequate and that they ensure sufficient provisions for losses.

Loan restructuring

Under restructuring of placements, the Managing Board means the creation of a new HBOR placement to a borrower instead of an already existing placement, but with significant changes in the agreed terms and conditions of the placement. Without such changes, the level of credit risk in the portfolio would increase as a result of an increase in liabilities due and/or a decrease in placement value. Changes in the terms and conditions are primarily caused by deterioration of the debtor's financial standing, with the purpose of such changes being the reduction of the debtor's liabilities arising from the repayment of loans and/or payment of interest and other fees. Restructuring of a placement means a prolongation of the principal repayment period by simultaneous undertaking of at least one of the following activities: capitalisation of interest, reduction of interest rate due to a weak financial standing of the debtor, decrease of debt level, takeover of other assets for a partial or complete settlement of debt, and other similar activities for the purpose of reducing a possible occurrence of increased credit risk.

In 2010 gross loans, before provision for impairment losses, that were restructured amounted to HRK 1,112,087 thousand (2009: HRK 587,451 thousand), and the value of the restructured loans after provision for impairment losses amounted to HRK 760,077 thousand (2009: HRK 313,691 thousand).

Restructured loans to banks, before provision for impairment losses, account for 55% (2009: 45%) of total restructured loans or 76% after provision for impairment losses (2009: 80%). In this case, commercial banks bear the default risk of the ultimate borrower.

Notes to the Financial Statements (continued)
for the year ended 31 December 2010
(All amounts are expressed in HRK thousand)

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial assets

Credit risk analysis, before and after considering the collateral received according to the type of financial assets on positions of assets and guarantees and commitments by internal credit rating, is as follows:

Group 2010	Gross exposure of portfolio of risk group A HRK '000	Gross exposure of portfolio of risk group B HRK '000	Gross exposure of portfolio of risk group C HRK '000	Gross exposure of total portfolio HRK '000	Net exposure of portfolio of risk group A HRK '000	Net exposure of portfolio of risk group B HRK '000	Net exposure of portfolio of risk group C HRK '000	Net exposure of total portfolio HRK '000
Assets								
Cash on hand and due from banks	1,258,725	-	-	1,258,725	-	-	-	-
Deposits with other banks	137,555	-	-	137,555	-	-	-	-
Loans to banks	14,945,550	503,897	-	15,449,447	-	-	-	-
Loans to other customers	4,613,441	1,182,952	-	5,796,393	1,588,685	184,431	-	1,773,116
Financial assets at fair value through profit or loss	500	-	-	500	-	-	-	-
Assets available for sale	187,710	-	-	187,710	173,554	-	-	173,554
Assets held to maturity	1,077	-	-	1,077	1,077	-	-	1,077
Other assets	3,071	12	-	3,083	2,218	12	-	2,230
Total	**21,147,629**	**1,686,861**	-	**22,834,490**	**1,765,534**	**184,443**	-	**1,949,977**
Guarantees and commitments								
Issued guarantees in domestic currency	513	-	-	513	-	-	-	-
Issued guarantees in foreign currency	317,673	27,511	-	345,184	38,902	27,511	-	66,413
Issued bills of exchange	28,187	-	-	28,187	-	-	-	-
Undrawn loans	874,039	31,847	-	905,886	100,202	19	-	100,221
EIF – subscribed, not called up capital	29,541	-	-	29,541	-	-	-	-
Total	**1,249,953**	**59,358**	-	**1,309,311**	**139,104**	**27,530**	-	**166,634**
Total credit risk exposure	**22,397,582**	**1,746,219**	-	**24,143,801**	**1,904,638**	**211,973**	-	**2,116,611**

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial assets (continued)

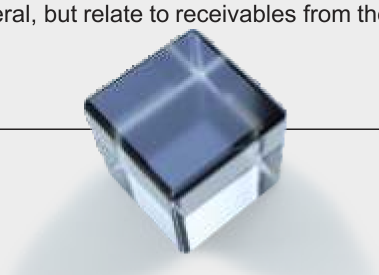
Credit risk analysis, before and after considering the collateral received according to the type of financial assets on positions of assets and guarantees and commitments by internal credit rating, is as follows (continued):

Bank 2010	Gross exposure of portfolio of risk group A HRK '000	Gross exposure of portfolio of risk group B HRK '000	Gross exposure of portfolio of risk group C HRK '000	Gross exposure of total portfolio HRK '000	Net exposure of portfolio of risk group A HRK '000	Net exposure of portfolio of risk group B HRK '000	Net exposure of portfolio of risk group C HRK '000	Net exposure of total portfolio HRK '000
Assets								
Cash on hand and due from banks	1,258,008	-	-	1,258,008	-	-	-	-
Deposits with other banks	103,284	-	-	103,284	-	-	-	-
Loans to banks	14,945,550	503,897	-	15,449,447	-	-	-	-
Loans to other customers	4,613,441	1,182,952	-	5,796,393	1,588,685	184,431	-	1,773,116
Assets available for sale	186,659	-	-	186,659	173,554	-	-	173,554
Other assets	2,376	12	-	2,388	1,510	12	-	1,522
Total	**21,109,318**	**1,686,861**	**-**	**22,796,179**	**1,763,749**	**184,443**	**-**	**1,948,192**
Guarantees and commitments								
Issued guarantees in domestic currency	513	-	-	513	-	-	-	-
Issued guarantees in foreign currency	317,673	27,511	-	345,184	38,902	27,511	-	66,413
Issued bills of exchange	28,187	-	-	28,187	-	-	-	-
Undrawn loans	874,039	31,847	-	905,886	100,202	19	-	100,221
EIF – subscribed, not called up capital	29,541	-	-	29,541	-	-	-	-
Total	**1,249,953**	**59,358**	**-**	**1,309,311**	**139,104**	**27,530**	**-**	**166,634**
Total credit risk exposure	**22,359,271**	**1,746,219**	**-**	**24,105,490**	**1,902,853**	**211,973**	**-**	**2,114,826**

In the total net highest exposure of the Group and the Bank, the amount of loans to other customers of HRK 1,234,777 thousand is not covered by ordinary collateral, but it relates to receivables and received funds from the Republic of Croatia of HRK 269,334 thousand, local (regional) authorities of HRK 141,121 thousand, public companies for whose liabilities the Republic of Croatia guarantees jointly and unconditionally of HRK 134,121 thousand and the government funds of HRK 11,202 thousand. An additional amount of HRK 678,999 thousand relates to receivables from majority (51%) state-owned companies.

The amount of assets available for sale is not covered by ordinary collateral but it relates to government bonds and treasury bills of the Ministry of Finance of HRK 174,631 thousand for the Group and HRK 173,554 thousand for the Bank.

Other assets of HRK 717 thousand are not covered by ordinary collateral, but relate to receivables from the Republic of Croatia and the government funds.



31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial asset (continued)

Credit risk analysis, before and after considering the collateral received according to the type of financial assets on positions of assets and guarantees and commitments by internal credit rating, is as follows (continued):

Bank 2009	Gross exposure of portfolio of risk group A HRK '000	Gross exposure of portfolio of risk group B HRK '000	Gross exposure of portfolio of risk group C HRK '000	Gross exposure of total portfolio HRK '000	Net exposure of portfolio of risk group A HRK '000	Net exposure of portfolio of risk group B HRK '000	Net exposure of portfolio of risk group C HRK '000	Net exposure of total portfolio HRK '000
Assets								
Cash on hand and due from banks	124,197	-	-	124,197	-	-	-	-
Deposits with other banks	127,055	-	-	127,055	-	-	-	-
Loans to banks	14,300,217	565,849	-	14,866,066	-	110	-	110
Loans to other customers	3,999,582	1,330,259	-	5,329,841	1,512,624	258,898	-	1,771,522
Assets available for sale	238,188	-	-	238,188	225,278	-	-	225,278
Other assets	3,410	15	-	3,425	1,878	15	-	1,893
Total	**18,792,649**	**1,896,123**	**-**	**20,688,772**	**1,739,780**	**259,023**	**-**	**1,998,803**
Guarantees and commitments								
Issued guarantees in domestic currency	513	-	-	513	-	-	-	-
Issued guarantees in foreign currency	656,427	26,201	-	682,628	42,428	26,201	-	68,629
Issued bills of exchange	34,251	-	-	34,251	-	-	-	-
Undrawn loans	839,745	137,589	-	977,334	59,722	39,541	-	99,263
EIF – subscribed, not called up capital	29,225	-	-	29,225	-	-	-	-
Total	**1,560,161**	**163,790**	**-**	**1,723,951**	**102,150**	**65,742**	**-**	**167,892**
Total credit risk exposure	**20,352,810**	**2,059,913**	**-**	**22,412,723**	**1,841,930**	**324,765**	**-**	**2,166,695**

In 2009, in the total net highest exposure, the amount of loans to other customers of HRK 1,388,861 thousand is not covered by ordinary collateral, but it relates to receivables and received funds from the Republic of Croatia of HRK 275,693 thousand, local (regional) authorities of HRK 151,502 thousand, public companies for whose liabilities the Republic of Croatia guarantees jointly and unconditionally of HRK 193,184 thousand and the government fund of HRK 14,314 thousand. An additional amount of HRK 754,168 thousand relates to receivables from majority (51%) state-owned companies.

The amount of assets available for sale is not covered by ordinary collateral but it relates to government bonds and treasury bills of the Ministry of Finance of HRK 225,278 thousand.

Other assets of HRK 474 thousand are not covered by ordinary collateral but by receivables from government funds.

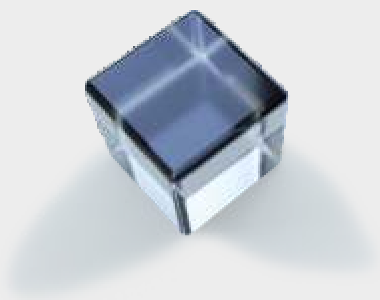
31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial asset (continued)

Credit risk quality according to the gross exposure of the type of financial assets on positions of assets and guarantees and commitments by risk category:

Group 2010	Gross exposure neither past due nor impaired	Gross exposure past due not impaired	Gross exposure individually impaired	Total
	HRK '000	HRK '000	HRK '000	HRK '000
Assets				
Cash on hand and due from banks	1,258,725	-	-	1,258,725
Deposits with other banks	137,555	-	-	137,555
Loans to banks	14,889,781	55,769	503,897	15,449,447
Loans to other customers	4,574,016	39,425	1,182,952	5,796,393
Financial assets at fair value through profit or loss	500	-	-	500
Assets available for sale	187,710	-	-	187,710
Assets held to maturity	1,077	-	-	1,077
Other assets	2,726	345	12	3,083
Total	**21,052,090**	**95,539**	**1,686,861**	**22,834,490**
Guarantees and commitments				
Issued guarantees in domestic currency	513	-	-	513
Issued guarantees in foreign currency	317,673	-	27,511	345,184
Issued bills of exchange	28,187	-	-	28,187
Undrawn loans	874,039	-	31,847	905,886
EIF – subscribed, not called up capital	29,541	-	-	29,541
Total	**1,249,953**	**-**	**59,358**	**1,309,311**
Total credit risk exposure	**22,302,043**	**95,539**	**1,746,219**	**24,143,801**



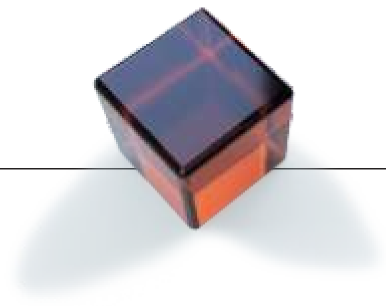
31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial asset (continued)

Credit risk quality according to the gross exposure of the type of financial assets on positions of assets and guarantees and commitments by risk category (continued):

Bank 2010	Gross exposure neither past due nor impaired	Gross exposure past due not impaired	Gross exposure individually impaired	Total
	HRK '000	HRK '000	HRK '000	HRK '000
Assets				
Cash on hand and due from banks	1,258,008	-	-	1,258,008
Deposits with other banks	103,284	-	-	103,284
Loans to banks	14,889,781	55,769	503,897	15,449,447
Loans to other customers	4,574,016	39,425	1,182,952	5,796,393
Assets available for sale	186,659	-	-	186,659
Other assets	2,031	345	12	2,388
	21,013,779	**95,539**	**1,686,861**	**22,796,179**
Guarantees and commitments				
Issued guarantees in domestic currency	513	-	-	513
Issued guarantees in foreign currency	317,673	-	27,511	345,184
Issued bills of exchange	28,187	-	-	28,187
Undrawn loans	874,039	-	31,847	905,886
EIF – subscribed, not called up capital	29,541	-	-	29,541
Total	**1,249,953**	**-**	**59,358**	**1,309,311**
Total credit risk exposure	**22,263,732**	**95,539**	**1,746,219**	**24,105,490**



31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial asset (continued)

Credit risk quality due to the gross exposure of the type of financial assets on positions of assets and guarantees and commitments by risk category (continued):

Bank 2009	Gross exposure neither past due nor impaired HRK '000	Gross exposure past due not impaired HRK '000	Gross exposure individually impaired HRK '000	Total HRK '000
Assets				
Cash on hand and due from banks	124,197	-	-	124,197
Deposits with other banks	127,055	-	-	127,055
Loans to banks	14,030,770	269,447	565,849	14,866,066
Loans to other customers	3,964,344	35,238	1,330,259	5,329,841
Assets available for sale	238,188	-	-	238,188
Other assets	2,292	1,118	15	3,425
Total	**18,486,846**	**305,803**	**1,896,123**	**20,688,772**
Guarantees and commitments				
Issued guarantees in domestic currency	513	-	-	513
Issued guarantees in foreign currency	656,427	-	26,201	682,628
Issued bills of exchange	34,251	-	-	34,251
Undrawn loans	839,745	-	137,589	977,334
EIF – subscribed, not called up capital	29,225	-	-	29,225
Total	**1,560,161**	**-**	**163,790**	**1,723,951**
Total credit risk exposure	**20,047,007**	**305,803**	**2,059,913**	**22,412,723**

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial asset (continued)

Aging analysis of past due but not impaired loans per class of financial asset:

	Up to 2 days 2010 HRK '000	3 to 45 days 2010 HRK '000	46 to 90 days 2010 HRK '000	Over 90 days 2010 HRK '000	Total 2010 HRK '000	Up to 2 days 2009 HRK '000	3 to 45 days 2009 HRK '000	46 to 90 days 2009 HRK '000	Over 90 days 2009 HRK '000	Total 2009 HRK '000
Assets										
Loans to banks	31,320	16,298	8,077	74	55,769	7,150	151,276	100,736	10,285	269,447
Loans to other customers	33,947	894	2,336	2,248	39,425	23,988	940	1,100	9,210	35,238
Other assets	315	30	-	-	345	483	35	53	547	1,118
Total	**65,582**	**17,222**	**10,413**	**2,322**	**95,539**	**31,621**	**152,251**	**101,889**	**20,042**	**305,803**

From total due and not impaired loans to banks in 2010, an amount of HRK 42,650 thousand or 76% relates to approved but not executed extensions of revolving loans under framework contracts within the export credit financing programme.

Excluding these receivables from the due and impaired debt of banks, overdue receivables from banks under the export credit financing programme amount to HRK 13,119 thousand.

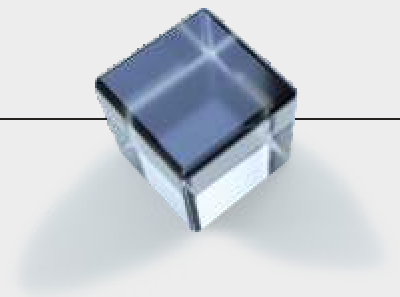
Out of total due and not impaired loans to other customers in 2010, an amount of HRK 33,947 thousand or 86% relates to delays of two days. Part of these receivables of HRK 6,596 thousand or 17% is covered by guarantees of the Republic of Croatia.

From total due and not impaired loans to banks in 2009, an amount of HRK 236,050 thousand or 88% relates to approved but not executed extensions of revolving loans under framework contracts within the export credit financing programme.

Excluding these receivables from the due and impaired debt of banks, overdue receivables from banks under the export credit financing programme amount to HRK 33,397 thousand.

By 15 January 2010 HRK 18,350 thousand of extensions were executed. Approved not executed extensions of revolving loans amount to HRK 134,455 thousand. A portion of loan agreements under this loan programme in the amount of HRK 83,245 thousand is expected to be repaid out of funds granted through the new credit line.

Out of total due and not impaired loans to other customers in 2009, an amount of HRK 23,988 thousand or 68% relates to delays of two days. Part of these receivables of HRK 12,692 thousand or 36% is covered by the guarantees of the Republic of Croatia.



31. Risk management (continued)

31.2. Credit risk (continued)

Collateral and other instruments

Collateral for the Bank's placements are:

1. obligatory (bills of exchange and promissory notes),
2. ordinary (property, ships, airplanes, bank guarantees, guarantees from the Republic of Croatia, guarantees from the local (regional) authorities, guarantees from HAMAG (Croatian Agency for Small Business), insurance policy from political and/or commercial risks), and
3. other collateral (movable property, bills of exchange or guarantees form other companies with solid creditworthiness, fiduciary or pledge of securities or shares in companies, repossession of cash receivables or assignment for collectible receivables, deposit repossession, restriction of transferability on insurance policy of assets and/or person, pledge on a trademark, etc.).

All Bank placements have to be secured with obligatory collateral. The Bank secures placements by property transfer or mortgage (super-mortgage) on real estate/movables.
Acceptable standard and other collateral are classified according to quality in five groups. The evaluation of collateral is based on quality, estimated based on marketability, documentation and possibility of supervision by the Bank as well as the possibility of enforced collection. Only the acceptable collateral is evaluated while the sixth group of collateral is unacceptable.
When deciding on loan approval, weak creditworthiness cannot be replaced by quality collateral, except when the insurance instruments are first class instruments: guarantees from the Republic of Croatia, guarantees of local/regional authorities (JLS), guarantees from HAMAG, insurance policy against political and/or commercial risks and when the Republic of Croatia, JLS or other government bodies guarantee for clients implicitly (through legal acts).

Collateral for placements with commercial banks

For the purpose of mitigation of credit risk and reduction of business costs, and in compliance with the Act on the Croatian Bank for Reconstruction and Development, the Bank approves part of its placements with commercial banks. As collateral for placements approved to final customers through commercial banks, the Bank uses mandatory collateral from commercial banks. The commercial bank is obliged to deliver them based on the Mutual business cooperation agreement, but not for each individual placement to the final customer based on that Agreement. In the individual contracts for placements to the final customers, the use of obligatory collateral delivered with the Agreement on mutual business cooperation is contracted. As the commercial bank takes on the risk of default by the final customer, it is given the option to contract sufficient collateral with the final customer.

Where the loan approved through a commercial bank is higher than HRK 700 thousand, depending on the commercial bank's internal rating, the Bank contracts a super-mortgage. In this case, either the commercial bank transfers the ownership over the collateral, while the Bank takes a mortgage over the same collateral, or the commercial bank forms a mortgage on the collateral, while the Bank takes a super-mortgage on the same collateral.

31. Risk management (continued)

31.2. Credit risk (continued)

Collateral and other instruments (continued)

Collateral for placements with commercial banks (continued)

By signing the Agreement on mutual business cooperation, a transfer of any claims the commercial bank may have towards the final customer is made to HBOR. Pursuant to the Agreement, the commercial bank authorises HBOR to unilaterally inform the bank in written form that, in the case of the commercial bank's insolvency or threat of liquidation, untimely repayments or default on the commitments agreed in the individual contract on interbank loan or actual (insolvent or regular) liquidation, the Bank assumes the receivable towards the final customer from the commercial bank, with the effect of a assignment of receivables in the place of contract fulfilment.

Additionally, based on the Agreement on mutual business cooperation and based on the said unilateral statement, the commercial bank authorises HBOR to transfer ownership over all collateral that the bank had agreed with the final customer on the particular placement, without having to obtain any additional approvals or permissions from the bank.

From the moment of the assignment, the final customer is obliged to make all payments related to the assigned receivable directly to HBOR. Should the commercial bank receive any payments in the name of collection of receivables per particular placement, the bank is obliged to immediately transfer the funds to HBOR.

Collateral for direct placements

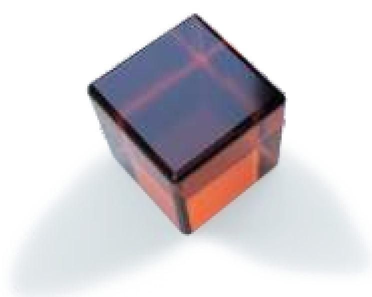
All direct placements are mainly secured with a mortgage over real estate and, if that is possible, the Bank obtains as security against credit risk a guarantee from HAMAG, a guarantee from the local (regional) authority, a guarantee from the Republic of Croatia, etc.

The Bank has the right to review the appraisal of the collateral value and such a confirmed appraisal is considered as the final collateral value.

Depending on the type of collateral, the credit programme, the general terms of insurance or the decision of an authorised body, the Bank has determined the necessary ratio of placements and collateral.

For real estate, the necessary ratio between the amount of placement and the appraised value of the real estate is 1:1,5 except for investments in areas of special concern, where the ratio is 1:1,3. For movable property, the necessary ratio between the amount of placement and the appraised value of the movable is 1:2.

The insured amount for insurance policies against political and/or commercial risks should cover at least 80% of the principal of the placement.



31. Risk management (continued)

31.2. Credit risk (continued)

Collateral and other instruments (continued)

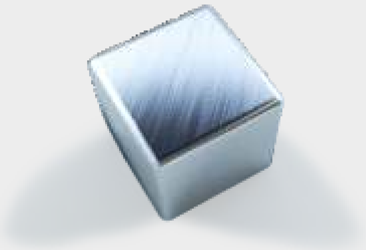
Collateral for direct placements (continued)

The Bank continuously monitors the value of the collateral by verification/statistical evaluation: Monitoring of the value of mortgaged real estate is performed once a year for business real estate, and every three years for residential buildings. The Bank has formed a special organizational unit for:

- evaluation and verification of already appraised and offered collateral (real estate and movables),
- technical and technological analysis of investment projects, and
- supervision over the withdrawal of loan funds for the purpose of the construction of the investment project.

In the event that it is not possible for the Bank to collect from regular operations, the Bank starts collection from the collateral at its disposal. This encompasses initiating collection from the obligatory collateral, and then from the mortgage or fiduciary ownership of the real estate or movable property, including their repossession with a view to decreasing or fully settling the Bank's receivables. The Bank does not use repossessed assets for business purposes.

For monitoring and dealing with problem loans, the Bank has loan workout organizational unit that is independent from loan granting activities. Loan workout unit finds appropriate ways of placement collection for the clients who are facing problems of existential, financial and business nature, taking into consideration possibilities of new repayment terms and conditions in order to alleviate the maintenance of production process, employment increase or recovery.



31. Risk management (continued)

31.3. Liquidity risk

Liquidity risk is a risk of financial loss which occurs if the Bank is unable to fund their due liabilities.

The basic principles for managing the Bank's liquidity risk are defined by the Liquidity Risk Management Procedures and decisions made by the Supervisory Board, the Managing Board and the ALCO.

In order to manage liquidity risk, the Bank maintains the necessary level of liquidity reserve, continuously monitors current and planned liquidity, ensures sufficient HRK and foreign currency funds necessary for timely settlement of liabilities and for disbursements of approved loans and planned loan approvals. The current surplus of available funds is placed in instruments for maintaining liquidity pursuant to the provisions of the Liquidity Risk Management Procedures.

The Bank's liquidity reserve is set in the amount of at least 10% of net assets.

The Bank manages liquidity risk through monitoring of daily, weekly, monthly, quarterly, annual and multi-annual cash flows compatibility. Plans of inflow and outflow of liquidity are made on an annual basis and stated at monthly level, and the realization of such plans is monitored on a monthly basis.

Managing short term liquidity encompasses monitoring and managing daily liquidity, planning liquidity for the next 5 weeks and for 1-year period. Within the framework of short-term liquidity risk management, incompatibility of cash flows in the mentioned periods is monitored as well as the compliance with short-term liquidity risk management.

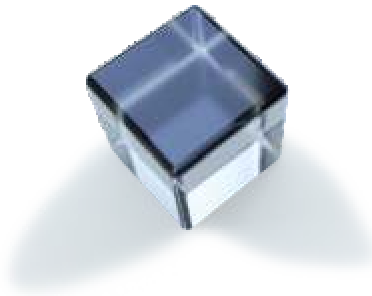
By long term liquidity risk management, the Bank monitors and aims to achieve maturity compatibility of existing and planned placements and sources in the period over one year.

The Bank monitors liquidity risk through scenario analyses, sensitivity analyses and stress tests. This includes both cases in the regular operating conditions and operating-under-stress conditions. Early warnings signals, proceedings in indication cases and in crisis conditions are determined.

The Bank has prescribed liquidity management limits in operations with commercial banks.

The Bank does not hold trading financial instruments.

As a special financial institution the Bank is not profit driven and therefore is not involved in derivative instruments trading. The use of derivatives is allowed for the purpose of position hedging, only.



31. Risk management (continued)

31.3. Liquidity risk (continued)

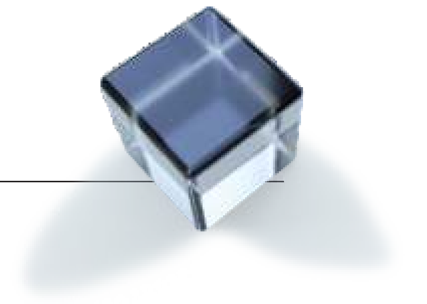
The table below provides an analysis of the Bank's assets and liabilities as of 31 December 2010 and 31 December 2009 placed into relevant maturity groupings based on the remaining period as at the Statement of Financial Position date related to the contractual maturity date, as follows:

Group 2010	**Up to 1 month HRK '000**	**1 - 3 months HRK '000**	**3 - 12 months HRK '000**	**1 - 3 years HRK '000**	**Over 3 years HRK '000**	**Total HRK '000**
Assets						
Cash on hand and due from banks	152,867	58,627	1,047,235	-	-	1,258,729
Deposits with other banks	83,524	19,760	34,271	-	-	137,555
Loans to banks*	3,286,288	2,559,731	1,927,215	2,988,409	4,687,804	15,449,447
Loans to other customers	332,848	133,513	696,033	1,952,213	2,681,786	5,796,393
Financial assets at fair value through profit or loss	500	-	-	-	-	500
Assets available for sale	185,740	1,970	-	-	-	187,710
Assets held to maturity	-	22	-	-	1,055	1,077
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	71,839	71,839
Non-current assets held for sale	-	411	20,842	13,108	-	34,361
Other assets	3,631	627	207	-	-	4,465
Total assets (1)	**4,045,398**	**2,774,661**	**3,725,803**	**4,953,730**	**7,442,484**	**22,942,076**
Liabilities						
Deposits	222,656	2	-	-	-	222,658
Borrowings	-	81,621	422,319	1,718,581	4,824,894	7,047,415
Bonds payable	-	2,431,484	147,703	2,400,044	2,503,022	7,482,253
Other liabilities	307,511	44,317	156,195	319,679	334,616	1,162,318
Total liabilities	**530,167**	**2.557,424**	**726,217**	**4,438,304**	**7,662,532**	**15,914,644**
Equity						
Founder's capital	-	-	-	-	5,163,739	5,163,739
Retained earnings and reserves	-	-	-	-	1,718,962	1,718,962
Other reserves	-	-	-	-	(2,978)	(2,978)
Net profit for the year	-	-	-	-	117,603	117,603
Total equity attributable to equity holders of the parent	**-**	**-**	**-**	**-**	**6,997,326**	**6,997,326**
Non-controlling interests	-	-	-	-	18,014	18,014
Total Equity	**-**	**-**	**-**	**-**	**7,015,340**	**7,015,340**
Guarantee fund	-	-	-	-	12,092	12,092
Total equity and Guarantee fund	**-**	**-**	**-**	**-**	**7,027,432**	**7,027,432**
Total liabilities, equity and Guarantee fund (2)	**530,167**	**2,557,424**	**726,217**	**4.438.304**	**14,689,964**	**22,942,076**
Net assets/liabilities (1) – (2)	**3,515,231**	**217,237**	**2,999,586**	**515,426**	**(7,247,480)**	**-**
Net cumulative assets/liabilities	**3,515,231**	**3,732,468**	**6,732,054**	**7,247,480**	**-**	**-**

The items with undefined maturity are included in terms over 3 years.

** Receivables of HRK 4,117,707 thousand relate to reverse repo transactions. The maturity of part of receivables was prolonged after the Statement of Financial Position date, and an amount of HRK 2,491,756 thousand was placed in the 1 up to 3 months maturity category.*

Notes to the Financial Statements (continued)
for the year ended 31 December 2010
(All amounts are expressed in HRK thousand)



31. Risk management (continued)

31.3. Liquidity risk (continued)

The table below provides an analysis of the Bank's assets and liabilities as of 31 December 2010 and 31 December 2009 placed into relevant maturity groupings based on the remaining period as at the Statement of Financial Position date related to the contractual maturity date, as follows:

Bank 2010	**Up to 1 month HRK '000**	**1 - 3 months HRK '000**	**3 - 12 months HRK '000**	**1 - 3 years HRK '000**	**Over 3 years HRK '000**	**Total HRK '000**
Assets						
Cash on hand and due from banks	152,150	58,627	1,047,235	-	-	1,258,012
Deposits with other banks	83,524	19,760	-	-	-	103,284
Loans to banks*	3,286,288	2,559,731	1,927,215	2,988,409	4,687,804	15,449,447
Loans to other customers	332,848	133,513	696,033	1,952,213	2,681,786	5,796,393
Assets available for sale	184,689	1,970	-	-	-	186,659
Investments in subsidiaries	-	-	-	-	19,125	19,125
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	71,418	71,418
Non-current assets held for sale	-	411	20,842	13,108	-	34,361
Other assets	2,936	455	207	-	-	3,598
Total assets (1)	**4,042,435**	**2,774,467**	**3,691,532**	**4,953,730**	**7,460,133**	**22,922,297**
Liabilities						
Deposits	222,656	2	-	-	-	222,658
Borrowings	-	81,621	422,319	1,718,581	4,824,894	7,047,415
Bonds payable	-	2,431,484	147,703	2,400,044	2,503,022	7,482,253
Other liabilities	307,082	43,295	155,623	319,561	334,634	1,160,195
Total liabilities	**529,738**	**2,556,402**	**725,645**	**4,438,186**	**7,662,550**	**15,912,521**
Equity						
Founder's capital	-	-	-	-	5,163,739	5,163,739
Retained earnings and reserves	-	-	-	-	1,718,962	1,718,962
Other reserves	-	-	-	-	(2,979)	(2,979)
Net profit for the year	-	-	-	-	117,962	117,962
Total Equity	**-**	**-**	**-**	**-**	**6,997,684**	**6,997,684**
Guarantee fund	-	-	-	-	12,092	12,092
Total equity and Guarantee fund	**-**	**-**	**-**	**-**	**7,009,776**	**7,009,776**
Total liabilities, equity and Guarantee fund (2)	**529,738**	**2,556,402**	**725,645**	**4,438,186**	**14,672,326**	**22,922,297**
Net assets/liabilities (1) – (2)	**3,512,697**	**218,065**	**2,965,887**	**515,544**	**(7,212,193)**	**-**
Net cumulative assets/liabilities	**3,512,697**	**3,730,762**	**6,696,649**	**7,212,193**	**-**	**-**

The items with undefined maturity are included in terms over 3 years.

** Receivables of HRK 4,117,707 thousand relate to reverse repo transactions. The maturity of part of receivables was prolonged after the Statement of Financial Position date, and an amount of HRK 2,491,756 thousand was placed in the 1 up to 3 months maturity category.*

Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

31. Risk management (continued)

31.3. Liquidity risk (continued)

Bank 2009	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Total HRK '000
Assets						
Cash on hand and due from banks	124,200	-	-	-	-	124,200
Deposits with other banks	90,881	36,174	-	-	-	127,055
Loans to banks*	3,485,983	1,878,994	2,133,629	2,489,677	4,877,783	14,866,066
Loans to other customers**	222,007	151,443	550,493	1,485,305	2,920,593	5,329,841
Assets available for sale	235,746	2,442	-	-	-	238,188
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	67,004	67,004
Non-current assets held for sale	-	-	20,440	12,420	2	32,862
Other assets	3,521	651	264	-	-	4,436
Total assets (1)	**4,162,338**	**2,069,704**	**2,704,826**	**3,987,402**	**7,865,382**	**20,789,652**
Liabilities						
Deposits	204,830	1	9	-	-	204,840
Borrowings	219,186	391,470	1,456,100	1,167,236	1,982,149	5,216,141
Bonds payable	-	214,608	146,124	4,470,241	2,694,170	7,525,143
Other liabilities	245,919	46,002	199,061	319,634	359,987	1,170,603
Total liabilities	**669,935**	**652,081**	**1,801,294**	**5,957,111**	**5,036,306**	**14,116,727**
Equity						
Founder's capital	-	-	-	-	4,943,739	4,943,739
Retained earnings and reserves	-	-	-	-	1,553,432	1,553,432
Other reserves	-	-	-	-	(1,739)	(1,739)
Net profit for the year	-	-	-	-	165,530	165,530
Total Equity	**-**	**-**	**-**	**-**	**6,660,962**	**6,660,962**
Guarantee fund	-	-	-	-	11,963	11,963
Total equity and Guarantee fund	**-**	**-**	**-**	**-**	**6,672,925**	**6,672,925**
Total liabilities, equity and Guarantee fund (2)	**669,935**	**652,081**	**1,801,294**	**5,957,111**	**11,709,231**	**20,789,652**
Net assets/liabilities (1) – (2)	**3,492,403**	**1,417,623**	**903,532**	**(1,969,709)**	**(3,843,849)**	**-**
Net cumulative assets/liabilities	**3,492,403**	**4,910,026**	**5,813,558**	**3,843,849**	**-**	**-**

The items with undefined maturity are included in terms over 3 years.

** Receivables of HRK 2,783,895 thousand relate to reverse repo transactions. The maturity of part of receivables was prolonged after the Statement of Financial Position date, and an amount of HRK 266,531 thousand was placed in the 1 up to 3 months maturity category.*

*** Receivables of HRK 63,469 thousand relate to reverse repo transactions. The maturity of part of receivables was prolonged after the Statement of Financial Position date, and an amount of HRK 52,363 thousand was placed in the 1 up to 3 months maturity category.*

Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

31. Risk management (continued)

31.3. Liquidity risk (continued)

The table below provides an analysis of the Group's undiscounted financial liabilities placed into the relevant maturity groupings based on the remaining period as at the Statement of Financial Position date related to the contractual maturity date:

Group 2010	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Total HRK '000
Financial liabilities						
Deposits	222,656	2	-	-	-	222,658
Borrowings	2,969	108,731	580,580	2,153,126	5,563,983	8,409,389
Bonds payable	-	2,323,193	444,111	2,822,874	2,936,180	8,526,358
Other liabilities	307,511	44,317	156,195	319,679	334,616	1,162,318
Total	**533,136**	**2,476,243**	**1,180,886**	**5,295,679**	**8,834,779**	**18,320,723**

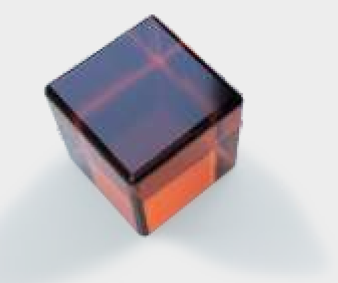
31. Risk management (continued)

31.3. Liquidity risk (continued)

The table below provides an analysis of the Bank's undiscounted financial liabilities placed into the relevant maturity groupings based on the remaining period as at the Statement of Financial Position date related to the contractual maturity date:

Bank 2010	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Total HRK '000
Financial liabilities						
Deposits	222,656	2	-	-	-	222,658
Borrowings	2,969	108,731	580,580	2,153,126	5,563,983	8,409,389
Bonds payable	-	2,323,193	444,111	2,822,874	2,936,180	8,526,358
Other liabilities	307,082	43,295	155,623	319,561	334,634	1,160,195
Total	**532,707**	**2,475,221**	**1,180,314**	**5,295,561**	**8,834,797**	**18,318,600**

Bank 2009	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Total HRK '000
Financial liabilities						
Deposits	204,830	1	9	-	-	204,840
Borrowings	227,659	405,384	1,552,539	1,481,687	2,916,108	6,583,377
Bonds payable	-	106,853	447,764	5,155,168	3,256,170	8,965,955
Other liabilities	245,919	46,002	199,061	319,634	359,987	1,170,603
Total	**678,408**	**558,240**	**2,199,373**	**6,956,489**	**6,532,265**	**16,924,775**



Notes to the Financial Statements (continued)
for the year ended 31 December 2010
(All amounts are expressed in HRK thousand)

31. Risk management (continued)

31.4. Market risk

Management of market risks implies the reduction of interest rate risk and the currency risk to a minimal level. By including a large number of organizational units in the operations of the Assets and liabilities management committee directly or indirectly, the Bank tries to ensure the quality as well as an integrated and comprehensive Risk management system.

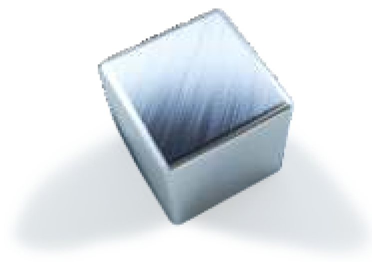
31.4.1. Interest rate risk

Interest rate risk is the financial risk that occurs due to interest rate mismatching of the value and maturity of interest-sensitive assets, liabilities and off balance sheet positions.

The basic principles for managing the Bank's interest rate risk are defined by the Interest Rate Risk Management Procedures that came into force in the reporting year and decisions made by the Managing Board and the ALCO.

For the purpose of measurement and monitoring of interest rate risk, the Bank carries out interest rate gap analysis. Interest rate gap is calculated for certain periods according to the possibilities of interest rate changes (fixed or floating rates) and presents the sensitivity of the Bank to the changes in interest rates. Interest rates are structured per currency, type and value is made. Projections of average weighted interest rates for Bank's funds and placements are also carried out.

Based on mentioned reports matching of interest rate received and payable is monitored. Depending on the level of the interest gap, the type of interest rates on future borrowings and on new loan approvals is determined in order to reduce the gap to the lowest level. From the funds that bear certain types of interest rate, funds with the same interest rate increased by a margin are placed. In this way the Bank reduces its market movement sensitivity as well as its sensitivity to reference interest rates. Furthermore, current market conditions and movements in forecasted market indicators are also monitored.



Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

31. Risk management (continued)

31.4. Market risk (continued)

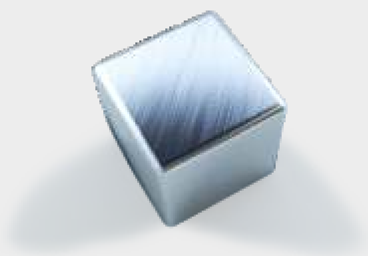
31.4.1. Interest rate risk (continued)

The following tables demonstrate the sensitivity of HBOR Group to a reasonable possible change in interest rates as of 31 December 2010 and 2009 on the basis of known dates of changes in prices of assets and liabilities to which floating and fixed interest rates are applied. Periods of interest rates changes are determined on the basis of residual maturity and contracted period when interest rates change, depending on which is shorter.

Assets and liabilities on which interest is not charged are placed into the non-interest bearing category.

The tables below demonstrate the estimation of HBOR´s Group interest rate risk exposure as of 31 December 2010 and 2009 which may not be indicative for the positions in other periods.

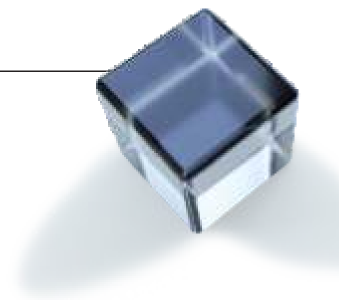
Group 2010	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Non interest bearing HRK '000	Total HRK '000
Assets							
Cash on hand and due from banks	27,970	58,608	1,047,194	-	-	124,957	1,258,729
Deposits with other banks	83,524	20,111	33,920	-	-	-	137,555
Loans to banks	3,282,824	3,267,499	2,312,662	2,583,239	3,976,107	27,116	15,449,447
Loans to other customers	303,873	305,113	1,780,666	1,470,250	1,914,804	21,687	5,796,393
Financial assets at fair value through profit or loss	-	-	-	-	-	500	500
Assets available for sale	184,689	-	-	-	-	3,021	187,710
Assets held to maturity	-	22	-	-	1,055	-	1,077
Investments in associates	-	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	-	71,839	71,839
Non-current assets held for sale	-	-	-	-	-	34,361	34,361
Other assets	-	-	-	-	-	4,465	4,465
Total assets (1)	**3,882,880**	**3,651,353**	**5,174,442**	**4,053,489**	**5,891,966**	**287,946**	**22,942,076**



Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)



31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest risk (continued)

Group 2010	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Non interest bearing HRK '000	Total HRK '000
Liabilities							
Deposits	3	2	-	-	-	222,653	222,658
Borrowings	-	699,936	1,069,483	1,409,802	3,836,613	31,581	7,047,415
Bonds payable	-	2,215,185	147,703	2,400,044	2,503,021	216,300	7,482,253
Other liabilities	-	-	-	-	-	1,162,318	1,162,318
Total liabilities	**3**	**2,915,123**	**1,217,186**	**3,809,846**	**6,339,634**	**1,632,852**	**15,914,644**
Equity							
Founder's capital	-	-	-	-	-	5,163,739	5,163,739
Retained earnings and reserves	-	-	-	-	-	1,718,962	1,718,962
Other reserves	-	-	-	-	-	(2,978)	(2,978)
Net profit for the year	-	-	-	-	-	117,603	117,603
Total equity attributable to equity holders of the parent	**-**	**-**	**-**	**-**	**-**	**6,997,326**	**6,997,326**
Non-controlling interests	-	-	-	-	-	18,014	18,014
Total Equity	**-**	**-**	**-**	**-**	**-**	**7,015,340**	**7,015,340**
Guarantee fund	-	-	-	-	-	12,092	12,092
Total equity and Guarantee fund	**-**	**-**	**-**	**-**	**-**	**7,027,432**	**7,027,432**
Total liabilities, equity and Guarantee fund	**3**	**2,915,123**	**1,217,186**	**3,809,846**	**6,339,634**	**8,660,284**	**22,942,076**
Net assets/liabilities (1) – (2)	**3,882,877**	**736,230**	**3,957,256**	**243,643**	**(447,668)**	**(8,372,338)**	**-**

Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest rate risk (continued)

The following tables demonstrate the sensitivity of HBOR to a reasonable possible change in interest rates as of 31 December 2010 and 2009 on the basis of known dates of changes in prices of assets and liabilities to which floating and fixed interest rates are applied. Periods of interest rates changes are determined on the basis of residual maturity and contracted period when interest rates change, depending on which is shorter.

Assets and liabilities on which interest is not charged are placed into the non-interest bearing category.

The tables below demonstrate the estimation of HBOR´s interest rate risk exposure as of 31 December 2010 and 2009 which may not be indicative for the positions in other periods.

Bank 2010	Up to 1 month	1 - 3 months	3 - 12 months	1 - 3 years	Over 3 years	Non interest bearing	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Assets							
Cash on hand and due from banks	27,324	58,608	1,047,194	-	-	124,886	1,258,012
Deposits with other banks	83,524	19,760	-	-	-	-	103,284
Loans to banks	3,282,824	3,267,499	2,312,662	2,583,239	3,976,107	27,116	15,449,447
Loans to other customers	303,873	305,113	1,780,666	1,470,250	1,914,804	21,687	5,796,393
Assets available for sale	184,689	-	-	-	-	1,970	186,659
Investments in subsidiaries	-	-	-	-	-	19,125	19,125
Investments in associates	-	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	-	71,418	71,418
Non-current assets held for sale	-	-	-	-	-	34,361	34,361
Other assets	-	-	-	-	-	3,598	3,598
Total assets (1)	**3,882,234**	**3,650,980**	**5,140,522**	**4,053,489**	**5,890,911**	**304,161**	**22,922,297**

Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest risk (continued)

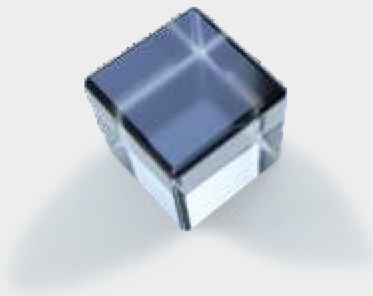
Bank 2010	Up to 1 month	1 - 3 months	3 - 12 months	1 - 3 years	Over 3 years	Non interest bearing	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Liabilities							
Deposits	3	2	-	-	-	222,653	222,658
Borrowings	-	699,936	1,069,483	1,409,802	3,836,613	31,581	7,047,415
Bonds payable	-	2,215,185	147,703	2,400,044	2,503,021	216,300	7,482,253
Other liabilities	-	-	-	-	-	1,160,195	1,160,195
Total liabilities	**3**	**2,915,123**	**1,217,186**	**3,809,846**	**6,339,634**	**1,630,729**	**15,912,521**
Equity							
Founder's capital	-	-	-	-	-	5,163,739	5,163,739
Retained earnings and reserves	-	-	-	-	-	1,718,962	1,718,962
Other reserves	-	-	-	-	-	(2,979)	(2,979)
Net profit for the year	-	-	-	-	-	117,962	117,962
Total Equity	**-**	**-**	**-**	**-**	**-**	**6,997,684**	**6,997,684**
Guarantee fund	-	-	-	-	-	12,092	12,092
Total equity and Guarantee fund	**-**	**-**	**-**	**-**	**-**	**7,009,776**	**7,009,776**
Total liabilities, equity and Guarantee fund	**3**	**2,915,123**	**1,217,186**	**3,809,846**	**6,339,634**	**8,640,505**	**22,922,297**
Net assets/liabilities (1) – (2)	**3,882,231**	**735,857**	**3,923,336**	**243,643**	**(448,723)**	**(8,336,344)**	**-**

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest risk (continued)

Bank 2009	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Non interest bearing HRK '000	Total HRK '000
Assets							
Cash on hand and due from banks	-	-	-	-	-	124,200	124,200
Deposits with other banks	90,881	34,876	-	-	-	1,298	127,055
Loans to banks	3,485,584	2,678,167	2,122,587	2,284,069	4,264,691	30,968	14,866,066
Loans to other customers	200,700	324,847	1,806,977	1,096,854	1,882,933	17,530	5,329,841
Assets held to maturity	-	-	-	-	-	-	-
Assets available for sale	235,746	-	-	-	-	2,442	238,188
Investments in associates	-	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	-	67,004	67,004
Non-current assets held for sale	-	-	-	-	-	32,862	32,862
Other assets	-	-	-	-	-	4,436	4,436
Total assets (1)	**4,012,911**	**3,037,890**	**3,929,564**	**3,380,923**	**6,147,624**	**280,740**	**20,789,652**



31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest risk (continued)

Bank 2009	Up to 1 month HRK '000	1 - 3 months HRK '000	3 - 12 months HRK '000	1 - 3 years HRK '000	Over 3 years HRK '000	Non interest bearing HRK '000	Total HRK '000
Liabilities							
Deposits	-	1	9	-	-	204,830	204,840
Borrowings	219,186	2,408,058	663,808	274,859	1,621,082	29,148	5,216,141
Bonds payable	-	-	146,124	4,470,241	2,694,170	214,608	7,525,143
Other liabilities	-	-	-	-	-	1,170,603	1,170,603
Total liabilities	**219,186**	**2,408,059**	**809,941**	**4,745,100**	**4,315,252**	**1,619,189**	**14,116,727**
Equity							
Founder's capital	-	-	-	-	-	4,943,739	4,943,739
Retained earnings and reserves	-	-	-	-	-	1,553,432	1,553,432
Other reserves	-	-	-	-	-	(1,739)	(1,739)
Net profit for the year	-	-	-	-	-	165,530	165,530
Total Equity	**-**	**-**	**-**	**-**	**-**	**6,660,962**	**6,660,962**
Guarantee fund	-	-	-	-	-	11,963	11,963
Total equity and Guarantee fund	**-**	**-**	**-**	**-**	**-**	**6,672,925**	**6,672,925**
Total liabilities, equity and Guarantee fund	**219,186**	**2,408,059**	**809,941**	**4,745,100**	**4,315,252**	**8,292,114**	**20,789,652**
Net assets/liabilities (1) – (2)	**3,793,725**	**629,831**	**3,119,623**	**(1,364,177)**	**1,832,372**	**(8,011,374)**	**-**

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest risk (continued)

Sensitivity analysis

Assumptions used in preparing the interest risk sensitivity analysis relate to changes in basis points (b.p.) in relation to higher or lower movements in reference interest rates than expected in order to assess the hypothetical effect on HBOR's profit and equity.

Volatility of 17% for 2010 (2009: 21%) on the daily changes of the interest rates linked to EUR has been determined using the standard deviation method. Based on such determined volatility used in the sensitivity analysis for 2010, the hypothetical impact of changes of the interest rate linked to EUR by 17 basis points (2009: 25 basis points) has been analyzed.

Volatility of 34% for 2010 (2009: 36.3%) on the daily changes of the interest rates linked to USD has been determined using the standard deviation method. Based on such determined volatility used in the sensitivity analysis for 2010, the hypothetical impact of the changes of the interest rate linked to USD by 34 basis points (2009: 40 basis points) has been analyzed.

The analysis presents the sensitivity of interest rates to reasonably expected changes in basis points. All other variables remain constant.

The sensitivity of profit is influenced by hypothetical changes in interest rates during a period of one year based on interest bearing assets and liabilities with a variable interest rate.

Currency	Increase in b.p. in 2010	Effect on profit and equity in 2010	Increase in b.p. in 2009	Effect on profit and equity in 2009
		HRK '000		HRK '000
EUR	+17	2,352	+25	(1,886)
USD	+34	16	+40	100

Currency	Decrease in b.p. in 2010	Effect on profit and equity in 2010	Decrease in b.p. in 2009	Effect on profit and equity in 2009
		HRK '000		HRK '000
EUR	-17	(2,352)	-25	1,886
USD	-34	(16)	-40	(100)

Notes to the Financial Statements (continued)
for the year ended 31 December 2010
(All amounts are expressed in HRK thousand)

31. Risk management (continued)

31.4. Market risk (continued)

31.4.2. Currency risk

Currency risk represents the exposure of the Bank to changes in foreign exchange rates and arises, above all, out of asset and liability currency mismatch that could result in higher expenses and/or not realized projected income.

Basic rules and principles in currency risk management of the Bank are determined in Currency risk management procedures and the decisions of the Managing Board and the Asset and liabilities management committee.

Currency risk management procedures determine: sources of currency risk, methods for measurement/assessment, monitoring and currency risk management, limits, proceedings in indication cases and in crisis conditions cases as well as reports necessary for comprehensive management of this risk.

The Bank uses a methodology prescribed by the Croatian National Bank, a simple calculation method when assessing currency risk exposure. A report on open foreign currency positions is generated on a daily basis. The total open foreign currency position of the Bank (including options) is the combination of the sum of all other long positions and the sum of all short positions in each currency, depending which of the two sums is higher. In addition, for the measurement/assessment of currency risk, the Bank uses VaR model. The currency risk is monitored through prescribed limits of currency risk exposure. Scenario analyses, sensitivity analyses and stress tests are carried out.

Most of HBOR's loan placements include currency clauses which represents a means of currency risk protection.

Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

31. Risk management (continued)

31.4. Market risk (continued)

31.4.2. Currency risk (continued)

Total assets and liabilities as of 31 December 2010 and 31 December 2009 in HRK and foreign currencies can be shown as follows:

Group	USD	EUR	Other foreign currencies	Total foreign currencies	HRK	Total
2010	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Assets						
Cash on hand and due from banks	265	109,766	1,487	111,518	1,147,211	1,258,729
Deposits with other banks	33,076	50,699	-	83,775	53,780	137,555
Loans to banks	4,745	9,907,916	-	9,912,661	5,536,786	15,449,447
Loans to other customers	50,517	3,219,315	-	3,269,832	2,526,561	5,796,393
Financial assets at fair value through profit or loss	-	400	-	400	100	500
Assets available for sale	-	146,732	-	146,732	40,978	187,710
Assets held to maturity	-	1,077	-	1,077	-	1,077
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	71,839	71,839
Non-current assets held for sale	-	-	-	-	34,361	34,361
Other assets	-	-	-	-	4,465	4,465
Total assets (1)	**88,603**	**13,435,905**	**1,487**	**13,525,995**	**9,416,081***	**22,942,076**
Liabilities						
Deposits	21,640	7,560	36	29,236	193,422	222,658
Borrowings	-	5,047,415	-	5,047,415	2,000,000	7,047,415
Bonds payable	-	7,482,253	-	7,482,253	-	7,482,253
Other liabilities	2,194	3,106	-	5,300	1,157,018	1,162,318
Total liabilities	**23,834**	**12,540,334**	**36**	**12,564,204**	**3,350,440**	**15,914,644**
Equity						
Founder's capital	-	-	-	-	5,163,739	5,163,739
Retained earnings and reserves	-	-	-	-	1,718,962	1,718,962
Other reserves	-	-	-	-	(2,978)	(2,978)
Net profit for the year	-	-	-	-	117,603	117,603
Total equity attributable to equity holders of the parent	**-**	**-**	**-**	**-**	**6,997,326**	**6,997,326**
Non-controlling interests	-	-	-	-	18,014	18,014
Total Equity	**-**	**-**	**-**	**-**	**7,015,340**	**7,015,340**
Guarantee fund	-	12,902	-	12,092	-	12,092
Total equity and Guarantee fund	**-**	**12,902**	**-**	**12,092**	**7,015,340**	**7,027,432**
Total liabilities, equity and Guarantee fund (2)	**23,834**	**12,552,426**	**36**	**12,576,296**	**10,365,780**	**22,942,076**
Net assets/liabilities (1) – (2)	**64,769**	**883,479**	**1,451**	**949,699**	**(949,699)**	**-**

** Amounts linked to a to one-way currency clause represent HRK 1,640,667 thousand.*

Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

31. Risk management (continued)

31.4. Market risk (continued)

31.4.2. Currency risk (continued)

Total assets and liabilities as of 31 December 2010 and 31 December 2009 in HRK and foreign currencies can be shown as follows (continued):

Bank	USD	EUR	Other foreign currencies	Total foreign currencies	HRK	Total
2010	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Assets						
Cash on hand and due from banks	265	109,766	1,487	111,518	1,146,494	1,258,012
Deposits with other banks	33,076	50,448	-	83,524	19,760	103,284
Loans to banks	4,745	9,907,916	-	9,912,661	5,536,786	15,449,447
Loans to other customers	50,517	3,219,315	-	3,269,832	2,526,561	5,796,393
Assets available for sale	-	146,532	-	146,532	40,127	186,659
Investments in subsidiaries	-	-	-	-	19,125	19,125
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	71,418	71,418
Non-current assets held for sale	-	-	-	-	34,361	34,361
Other assets	-	-	-	-	3,598	3,598
Total assets (1)	**88,603**	**13,433,977**	**1,487**	**13,524,067**	**9,398,230***	**22,922,297**
Liabilities						
Deposits	21,640	7,560	36	29,236	193,422	222,658
Borrowings	-	5,047,415	-	5,047,415	2,000,000	7,047,415
Bonds payable	-	7,482,253	-	7,482,253	-	7,482,253
Other liabilities	2,194	2,651	-	4,845	1,155,350	1,160,195
Total liabilities	**23,834**	**12,539,879**	**36**	**12,563,749**	**3,348,772**	**15,912,521**
Equity						
Founder's capital	-	-	-	-	5,163,739	5,163,739
Retained earnings and reserves	-	-	-	-	1,718,962	1,718,962
Other reserves	-	-	-	-	(2,979)	(2,979)
Net profit for the year	-	-	-	-	117,962	117,962
Total Equity	**-**	**-**	**-**	**-**	**6,997,684**	**6,997,684**
Guarantee fund	-	12,092	-	12,092	-	12,092
Total equity and Guarantee fund	**-**	**12,092**	**-**	**12,092**	**6,997,684**	**7,009,776**
Total liabilities, equity and Guarantee fund (2)	**23,834**	**12,551,971**	**36**	**12,575,841**	**10,346,456**	**22,922,297**
Net assets/liabilities (1) – (2)	**64,769**	**882,006**	**1,451**	**948,226**	**(948,226)**	**-**

** Amounts linked to a to one-way currency clause represent HRK 1,640,667 thousand.*

31. Risk management (continued)

31.4. Market risk (continued)

31.4.2. Currency risk (continued)

Total assets and liabilities as of 31 December 2010 and 31 December 2009 in HRK and foreign currencies can be shown as follows (continued):

Bank 2009	USD HRK '000	EUR HRK '000	Other foreign currencies HRK '000	Total foreign currencies HRK '000	HRK HRK '000	Total HRK '000
Assets						
Cash on hand and due from banks	246	110,461	1,466	112,173	12,027	124,200
Deposits with other banks	25,155	65,726	-	90,881	36,174	127,055
Loans to banks	12,936	9,646,665	-	9,659,601	5,206,465	14,866,066
Loans to other customers	63,513	3,610,483	-	3,673,996	1,655,845	5,329,841
Assets available for sale	-	214,419	-	214,419	23,769	238,188
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	67,004	67,004
Non-current assets held for sale	-	-	-	-	32,862	32,862
Other assets	-	-	-	-	4,436	4,436
Total assets (1)	**101,850**	**13,647,754**	**1,466**	**13,751,070**	**7,038,582***	**20,789,652**
Liabilities						
Deposits	13,533	7,439	41	21,013	183,827	204,840
Borrowings	-	5,216,141	-	5,216,141	-	5,216,141
Bonds payable	-	7,525,143	-	7,525,143	-	7,525,143
Other liabilities	2,005	3,784	-	5,789	1,164,814	1,170,603
Total liabilities	**15,538**	**12,752,507**	**41**	**12,768,086**	**1,348,641**	**14,116,727**
Equity						
Founder's capital	-	-	-	-	4,943,739	4,943,739
Retained earnings and reserves	-	-	-	-	1,553,432	1,553,432
Other reserves	-	-	-	-	(1,739)	(1,739)
Net profit for the year	-	-	-	-	165,530	165,530
Total Equity	**-**	**-**	**-**	**-**	**6,660,962**	**6,660,962**
Guarantee fund	-	11,963	-	11,963	-	11,963
Total equity and Guarantee fund	**-**	**11,963**	**-**	**11,963**	**6,660,962**	**6,672,925**
Total liabilities, equity and Guarantee fund (2)	**15,538**	**12,764,470**	**41**	**12,780,049**	**8,009,603**	**20,789,652**
Net assets/liabilities (1) – (2)	**86,312**	**883,284**	**1,425**	**971,021**	**(971,021)**	**-**

** Amounts linked to a to one-way currency clause represent HRK 2,109,102 thousand.*

31. Risk management (continued)

31.4. Market risk (continued)

31.4.2. Currency risk (continued)

Sensitivity analysis

Sensitivity analysis was performed for the foreign currency risk which HBOR was exposed to on the reporting date.

Assumptions used in preparing the foreign currency risk sensitivity analysis relate to movements in exchange rates in respect to movements of the EUR/HRK and USD/HRK exchange rates, higher or lower than the actual rates, in order to assess the hypothetical effect on HBOR's profit and equity during a period of one year.

Volatility of 2.1% for 2010 (2009: 2.7%) on the monthly changes of the foreign exchange rate EUR/HRK have been determined using the standard deviation method. Based on such determined volatility and asset liability ratio in EUR as stated in this note within the sensitivity analysis in 2010, a rate of increase of 2.1% (2009: 3.0%) has been applied.

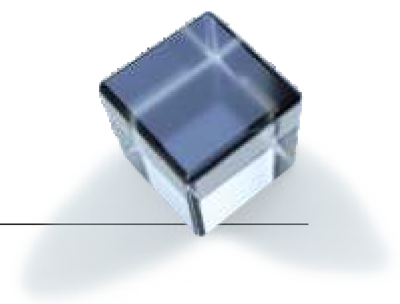
Volatility of 14.6% for 2010 (2009: 9.6%) on the monthly changes of the foreign exchange rate USD/HRK have been determined using the standard deviation method. Based on such determined volatility and asset liability ratio in USD as stated in this note within the sensitivity analysis in 2010, a rate of increase of 14.6% (2009: 10.0%) has been applied.

The effect of the assumed changes of the foreign exchange rate on the assets and liabilities in EUR and USD currency and with two-way and one-way currency clauses is stated below. The treatment of one-way currency clauses was described in Note 2.

	Change in currency rate in % 2010	Effect on profit and equity in 2010 HRK '000	Change in currency rate in % 2009	Effect on profit and equity in 2009 HRK '000
EUR	+2,1	31,784	+3,0	43,877
USD	+14,6	9,707	+10,0	8,631
EUR	-2,1	(22,410)	-3,0	(26,922)
USD	-14,6	(9,707)	-10,0	(8,631)

31.5. Operational risk

Operational risk is the risk of loss arising from system failure, human errors or external events. The Bank seeks to minimize operational risk by implementing controls in operating procedures and by building a unique and comprehensive IT system. The Bank applies the guidelines of Basel II and good IT system management practice.



31. Risk management (continued)

31.5. Operational risk (continued)

The Committee for IT management was established in order to monitor IT with the purpose of IT resources management by setting the appropriate level of efficiency and security of IT for providing, among other things, appropriate management of risks arising from IT technology utilisation. Considering the significant level of operational risk occurring in IT, the Bank has an officer in charge of analysis and control of IT security.

In order to reduce its exposure to operational risk that is present in day-to-day operations, the Bank constantly educates its employees, monitors the frequency of errors and implements controls for the prevention of errors.

32. Fair value of financial instruments

Fair value represents the amount at which an asset may be exchanged or a liability settled in an arm's-length transaction. If there is no active market for the financial assets and liabilities, or if due to any other reason, the fair value cannot be reliably measured by the market price, the Managing Board uses an evaluation technique for fair value estimation. Such techniques include prices achieved in recent transactions agreements between informed and willing sides, reference to similar financial instruments, and discounted cash flow analysis, making maximum use of market inputs and relying on entity-specific inputs.

The carrying amounts of cash and balances with the Croatian National Bank approximately present their fair values.

The estimated fair value of deposits approximates their carrying amounts since all deposits mature up to 90 days.

Loans and advances to banks and to other customers are presented net of provisions for impairment. The estimated fair value of loans and advances represents the discounted amount of estimated future cash flows expected to be received. The interest subsidies that are recognized as deferred income in discounted amounts and presented within other liabilities are taken into account in estimating fair value. The fair value of HRK loans with one-way foreign currency clause is assessed as described under the “Foreign currency transactions and foreign currency clause” paragraph.

The Bank's long-term borrowings have no quoted market price, and their fair value is estimated as the present value of future cash flows, discounted at interest rates in effect at the Statement of Financial Position date for new borrowings of a similar nature and with a similar remaining maturity. As the Bank's long-term borrowings mostly bear variable interest, the Bank estimates that its carrying amount is a reasonable approximation of fair value.

The fair value of bonds issued by HBOR on 31 December 2010 is stated in Note 24.

32. Fair value of financial instruments (continued)

32.1. Fair value of financial instruments initially recognized and measured at fair value

In the table below, financial instruments initially recognized and measured at fair value are analyzed and classified in three groups depending on whether used input data about fair value are observable or not:

Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities,

Level 2: inputs about fair value other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices), and

Level 3: inputs for the asset or liability that are derived by valuation methods for assets and liabilities based on observable market data (unobservable inputs).

Out of financial instruments in the Bank's portfolio, only assets available for sale that were initially and subsequently carried at fair value are classified in Level 1 and Level 2.

The evaluation of fair value of quoted securities in the active market is based on the recent prices provided directly from the regulated capital market (Zagreb Stock Exchange or other regulated capital market). In case of direct acceptance of securities' value from the regulated capital market, and if the latest price is not available, the concluding price will be taken for evaluation. If both the final and the concluding price are available for an individual security per institutional transaction, the latest price in the regular business will be used for the purpose of evaluation.

The same approach in the evaluation of fair value is also applied in case when the trust over the securities investment portfolio is given to a trustee.

If there is no active market for a financial instrument, or if due to any other reason, the fair value cannot be reliably measured by the market price, the Bank uses an evaluation technique for fair value estimation. Such technique includes prices achieved in recent transactions by reference to similar financial instruments, and discounted cash flow analysis, making maximum use of market inputs. When the discounted cash flow technique is used, the estimated future cash flows are based on the best evaluation of the Managing Board, and the discounted rate is market rate for similar instruments.

The Bank has chosen to present comparative information relating three-level fair value hierarchy disclosure for both reporting and prior period.

Notes to the Financial Statements (continued)

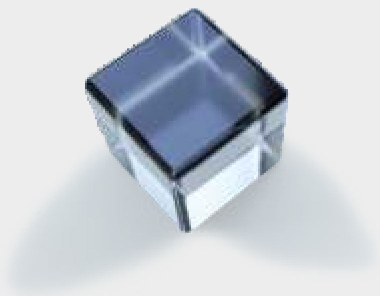
for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

32. Fair value of financial instruments (continued)

32.1. Fair value of financial instruments initially recognized and measured at fair value (continued)

Group		2010 HRK '000	
	Level 1	Level 2	Level 3
Financial assets at fair value through profit or loss			
Shares in investment funds recognised at fair value through profit or loss	500	-	-
Total financial assets at fair value through profit or loss	**500**	**-**	**-**
Assets available for sale:			
Debt securities:			
Listed debt securities:			
Bonds of the Ministry of Finance of the Republic of Croatia	131,618	-	-
Treasury bills of the Ministry of Finance of the Republic of Croatia	39,966	-	-
Accrued interest	1,970	-	-
Total debt securities	**173,554**	**-**	**-**
Equity securities:			
Investment in shares of foreign companies	-	23	-
Investment in financial institutions shares	-	161	-
Shares of foreign financial institutions – EIF	-	12,921	-
Corporate shares	-	-	-
Total equity securities	**-**	**13,105**	**-**
Investments in investment funds:			
Shares classified as assets available for sale	1,051	-	-
Total investments in investment funds	**1,051**	**-**	**-**
Total assets available for sale	**174,605**	**13,105**	**-**
Assets held to maturity:			
Debt securities:			
Bonds of the Ministry of Finance of the Republic of Croatia	1,055	-	-
Accrued interest	22	-	-
Total assets held to maturity	**1,077**	**-**	**-**



Notes to the Financial Statements (continued)

for the year ended 31 December 2010

(All amounts are expressed in HRK thousand)

32. Fair value of financial instruments (continued)

32.1. Fair value of financial instruments initially recognized and measured at fair value (continued)

		2010 HRK '000			2009 HRK '000	
Bank	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Assets available for sale						
Debt securities:						
Listed debt securities:						
Bonds of the Ministry of Finance of the Republic of Croatia	131,618	-	-	153,311	-	-
Treasury bills of the Ministry of finance of the Republic of Croatia	39,966	-	-	69,525	-	-
Accrued interest	1,970	-	-	2,442	-	-
Total debt securities	**173,554**	**-**	**-**	**225,278**	**-**	**-**
Equity securities:						
Investment in shares of foreign companies	-	23	-	-	20	-
Investment in financial institutions shares	-	161	-	-	161	-
Shares of foreign financial institutions – EIF	-	12,921	-	-	12,729	-
Corporate shares	-	-	-	-	-	-
Total equity securities	**-**	**13,105**	**-**	**-**	**12,910**	**-**
Total assets available for sale	**173,554**	**13,105**	**-**	**225,278**	**12,910**	**-**

32.2. Fair value of financial instruments carried at amortized cost

The Managing Board estimates that their carrying amounts of financial assets and liabilities carried at amortized cost are a reasonable approximation of fair value, except for the fair value of bonds payable (Note 24.). Fair value of liabilities upon bonds payable is determined according to adjusted quoted prices.

33. Segment reporting

General information on segments is given in relation to business segments of the Group.

Since the Group does not allocate administrative costs and interest by segments, the profitability of segments is not presented.

The tables below include the data on profit and loss account, total assets, liabilities and capital by business operation segments of the Group as at 31 December 2010. Taking into account that two of the total of three business operation segments started to operate in the course of 2010, it is not convenient to present comparative financials for the previous year.

Assets and liabilities by segments are presented in net terms, i.e. gross after impairment and provisioning, and before consideration of collateral received.

Business operations of segments are divided in terms of organisation and management. Each segment as a whole provides various products and services and operates in various markets.

Business segments:

The Group has following business segments:

Segment:	**Business activities of the segment include:**
Banking activities	Financing reconstruction and development of the Croatian economy, financing of infrastructure, export promotion, support for the development of small and medium-sized companies, environmental protection, and export credit insurance of Croatian goods and services against non-market risks for and on behalf of the Republic of Croatia.
Insurance activities	Insurance of foreign and domestic short-term receivables of business entities relating to deliveries of goods and services
Other	Preparation of analyses, credit risk assessment and providing information on creditworthiness

33. Reporting by segments (continued)

2010	HRK '000 Banking activities	HRK '000 Insurance activities	HRK '000 Other activities	HRK '000 Unallocated	HRK '000 Total
Net interest income	286,788	575	-	-	287,363
Net fee income	8,858	192	-	(1)	9,049
Net income from financial operations	17,755	12	-	-	17,767
Net premiums earned	-	69	-	-	69
Other income	922	364	-	(3)	1,283
Income from operating activities	**314,323**	**1,212**	**-**	**(4)**	**315,531**
Operating costs	(86,105)	(1,798)	(64)	(3)	(87,970)
Impairment loss and provisions	(110,256)	(100)	-	-	(110,356)
Expenses for insured cases and changes	-	-	-	-	-
Net change in provisions	-	(144)	-	-	(144)
Net expenses from financial operations	-	-	-	-	-
Other expenses	-	-	-	-	-
Operating expenses	**(196,361)**	**(2,042)**	**(64)**	**(3)**	**(198,470)**
Profit/(loss) before income tax	**117,962**	**(830)**	**(64)**	**(7)**	**117,061**
Income tax	-	168	13	-	181
Profit/(loss) for the year	**117,962**	**(662)**	**(51)**	**(7)**	**117,242**
Assets of segment	22,922,297	38,953	1,987	(21,161)	22,942,076
Total assets	**22,922,297**	**38,953**	**1,987**	**(21,161)**	**22,942,076**
Liabilities of segment	15,912,521	2,115	37	(29)	15,914,644
Total equity and guarantee fund	7,009,776	(662)	(50)	18,368	7,027,432
Total liabilities, equity and guarantee fund	**22,922,297**	**1,453**	**(13)**	**18,339**	**22,942,076**

34. Capital management

The primary objectives of the Bank's capital management are to ensure the presumptions of going concern and to respect regulatory and contracted demands imposed by creditors regarding a certain capital adequacy level.

The Bank has identified liable capital as a manageable capital category.

Liable capital has to be, at every moment, at least at the level of share capital or at the level that ensures that the capital adequacy ratio is at least 12%, and that is sufficient for covering capital requirements regarding business risks.

Liable capital consists of main capital (Tier 1) and additional capital (Tier 2), and is calculated in accordance with bank regulations in the Republic of Croatia.

The Bank has determined measures for the implementation and monitoring of the capital management policy as follows:

- At the reporting date, liable capital has to be at least at the level of founder's capital for the reporting period.
- The capital adequacy ratio at the reporting date has to be at the level prescribed for the banks in the Republic of Croatia as well as at the level stated within regular financial covenants determined in loan contracts and contracts with special financial institutions that HBOR has concluded as a borrower.

The calculation of the capital adequacy ratio is performed in line with the regulations prescribed for the banks in the Republic of Croatia and does not differ from international banking practice.

	2010 Group HRK '000	2010 Bank HRK '000	2009 Group HRK '000	2009 Bank HRK '000
Core capital – Tier 1	6,999,942	7,000,662	-	6,662,700
Supplementary capital – Tier 2	272,252	272,252	-	252,374
Total liable capital	**7,272,194**	**7,272,914**	**-**	**6,915,074**
Risk weighted assets	8,935,610	8,946,342	-	8,295,245
Capital requirements for currency risk	2,509,388	2,507,459	-	2,867,561
Total capital requirements	**11,444,998**	**11,453,801**	**-**	**11,162,806**
	%	**%**	**%**	**%**
Capital ratio (Tier 1)	**61,16**	**61,12**	**-**	**59,69**
Capital adequacy ratio	**63,54**	**63,50**	**-**	**61,95**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**
	000 kuna	**000 kuna**	**000 kuna**	**000 kuna**
Liable capital needed for ensuring capital adequacy according to regulatory requirements	**1,373,400**	**1,374,456**	**-**	**1,116,281**

Minimum capital adequacy ratio at the end of 2010 was 12% (2009: 10%). From the second quarter of 2010 and onwards, the regulatory minimum for the liable capital adequacy ratio is increased to 12%. Apart from the increase of the minimum ratio percentage, the new regulations require a change of methodology for the calculation of capital adequacy. Pursuant to the new requirement for liable capital adequacy ratio maintenance

34. Capital management (continued)

capital management requirement are being amended as follows: liable capital has to be at least at the level of founder's capital for the reporting period and liable capital adequacy ratio at the reporting date has to be at least at the level of 12 % and level sufficient for coverage of capital risk requirements.

Due to the extensive changes in the support application for the Bank's operations, the Managing Board has introduced a transitional period for the implementation of new applications until the end of 2011. In this period, the capital adequacy and exposure calculations will be made in the existing manner.

The Managing Board of the Group does not expect any adverse effects on the level of capital adequacy as a result of application of the new regulations for credit institutions, taking into account that the bank's capital adequacy ratio at the end of 2010 was 5.3 higher than the prescribed one. This was primarily due to the model of operation and its orientation to the lending operations.

35. Earnings per share

Pursuant to the HBOR Act, the equity capital of the Bank consists of one share in the company that may not be divided, transferred or pledged and is owned solely by the Republic of Croatia.

For the purpose of calculation of earnings per share, earning is presented as net profit after taxation.

36. Events after the reporting period date

36.1. Activities and role in the implementation of the Government's measures in the economic recovery and development of the Republic of Croatia – continued implementation of Model „A" and utilisation of the club-loan funds

Pursuant to the Decision of the Government of the Republic of Croatia on measures for economic recovery and development dated 14 January 2010 and the Conclusion of the Government of the Republic of Croatia dated 28 January 2010 on the acceptance of Measures for economic recovery and development, the implementation of model "A" started during 2010.

The Republic of Croatia has determined its participation in model „A" via HBOR and funds for eligible borrowers are provided for from both commercial banks and HBOR in 60 % : 40 % ratio. For the purpose of this model, the Bank signed the club-loan agreement on 18 February 2010 with several domestic commercial banks in the amount of HRK 2,000,000 thousand aimed to the Bank's 40 % of share in financing through the Loan Programme for financing working capital.

By Addendum I to the Club loan agreement dated 22 November 2010, the prolongation of the disbursement period of the club loan funds until 30 June 2011 has been regulated for all loans to final borrowers approved until 31 December 2010.

Unutilised funds under the Club loan agreement from 2010 in the amount of cca. HRK 1,100,000 thousand will be utilised in the course of 2011 for continuing the implementation of model „A" in the form of modified model „A", through the Programme for economic recovery and development – Model A+ that was accepted by the Government of the Republic of Croatia on 27 January 2011 for the purpose of continuing the implementation of measures for economic recovery and development.

For this purpose, HBOR entered into Addendum II to the Club loan agreement dated 16 February 2011.

The recent circumstances have been taken into consideration for disclosures in regard to liquidity risk and interest rate risk.

36. Events after the reporting period date (continued)

36.2. Investment in the Funds for economic co-operation on behalf of the Government of the Republic of Croatia

On 14 January 2010, the Government of the Republic of Croatia reached the Decision on the intention to participate in the establishment of Funds for economic co-operation. By this Decision, it has been determined that the Government of the Republic of Croatia shall participate in the establishment of funds for economic co-operation („FGS“) – open investment funds of venture capital with private placement, for the purpose of promoting the economy development, preserving the existing and creating new jobs, strengthening the existing and initiating new business entities, through ownership restructuring by additional capital investment, in co-operation with interested private investors. By this decision, the Government of the Republic of Croatia has determined that the total amount of Croatia's participation in the establishment of FGSs shall be up to HRK 1 billion.

Pursuant to Article V of the above mentioned Decision on intention to participate in the establishment of FGSs, the minister in charge of the economy passed the Regulations on terms and conditions of participation of the Government of the Republic of Croatia in the establishment of Funds for economic co-operation. These Regulations stipulate that the liability of the Qualified investor shall be guaranteed by the Government of the Republic of Croatia jointly and severally.

On 23 February 2010, the Government of the Republic of Croatia published the Public invitation for participation in the establishment of FGSs, with the intention to invite all natural and legal persons interested in the participation of FGS establishment.

On 4 August 2010, the Government of the Republic of Croatia reached the Decision on the appointment of a qualified investor for the participation in the establishment of funds for economic co-operation. By this Decision, HBOR is appointed as qualified investor that will, in its own name, and on behalf of the Government of the Republic of Croatia, invest in each FGS an amount corresponding to the amount to be invested in the same FGS by a private investor. However, the annual obligation of the qualified investor to pay its share in a single FGS shall not exceed 1/5 of the amount of the total assumed obligation of payment in a single FGS, being in line with the amount of funds provided in the Budget of the Republic of Croatia for the participation in FGSs for the year.

On 26 January 2011, the Republic of Croatia – the Croatian Government and HBOR signed the Agreement on agent transactions intended for investments in funds for economic co-operation.

In five established funds for economic co-operation, the Bank shall, by order of the Government of the Republic of Croatia, invest HRK 1,000,000 thousand. HBOR shall manage these financial resources separately from the Bank's assets. Income and expenses under these activities are charged to the principal and the Bank does not have any other liabilities.

36.3. Redemption of an bond issue upon maturity

After the year end, on 10 February 2011 the Bank settled the bonds due of HRK 2,223,853 thousand and the interest of HRK 108,413 thousand.

The bonds were issued on 11 February 2004 pursuant to the agreement between HBOR and Deutsche Bank AG London and UBS Limited (lead arrangers) under the EMTN programme with the Croatian Government guarantee, in the amount of EUR 300,000 thousand (HRK 2,215,185 thousand as at 31 December 2010) with the maturity of 7 years and fixed interest rate of 4.875%.

Publisher:
Hrvatska banka za obnovu i razvitak
Strossmayer Square 9
HR-10000 Zagreb, Croatia
Tel: +385 (1) 4591 666
Fax: +385 (1) 4591 721
ured-uprave@hbor.hr
www.hbor.hr

Concept, design, press:
STUDIO INTERNATIONAL d.o.o.

ISSN 1332-2893

WWW.HBOR.HR