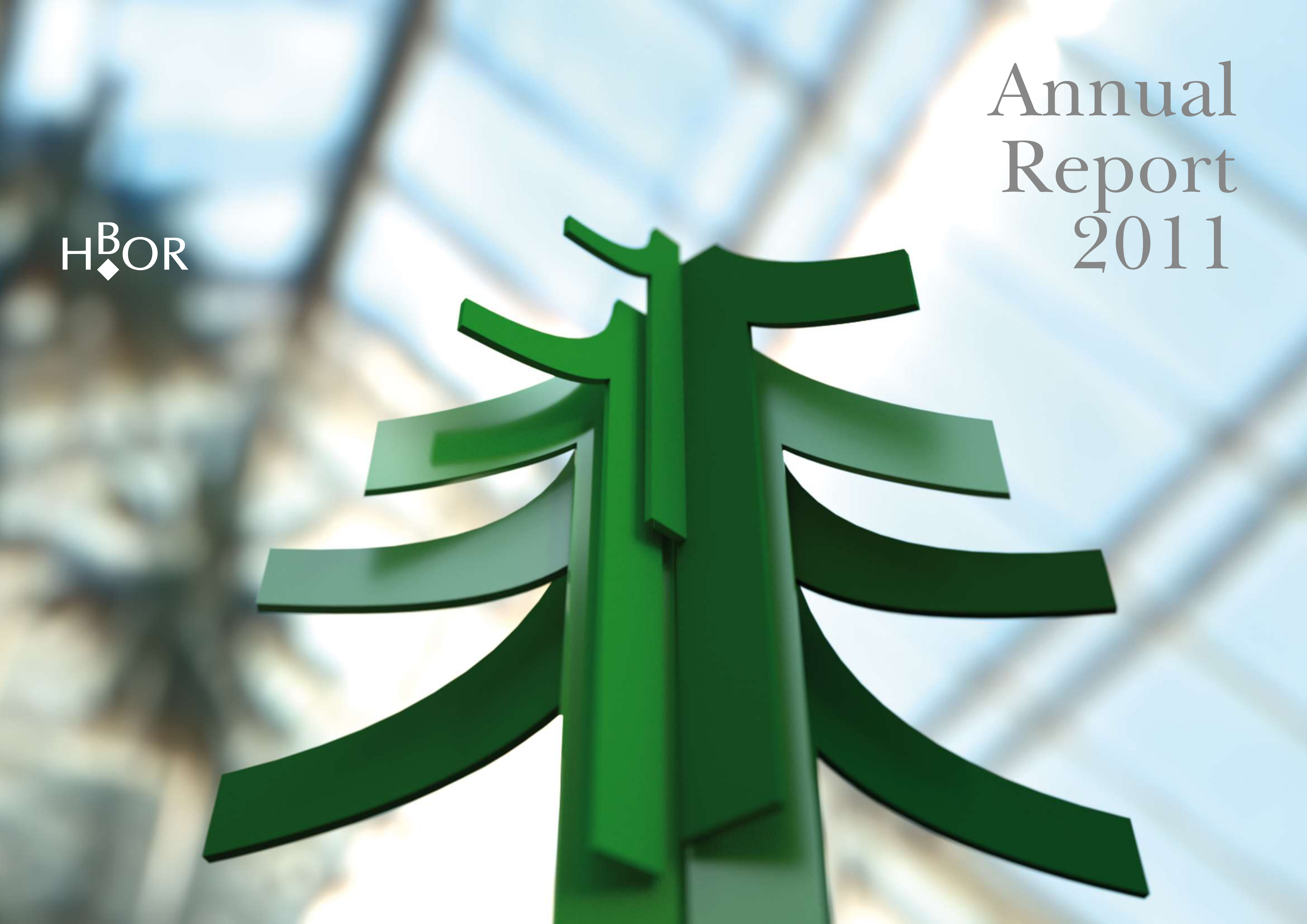


HBOR

Annual Report 2011

Annual Financial Statements of HBOR Group for 2011

Contents

LETTER OF THE PRESIDENT OF THE SUPERVISORY BOARD

Ladies and Gentelman,

Croatia is facing a severe economic crisis. The only way to overcome it is by instigating a new investment cycle, creating jobs and distributing the burden of the crisis equitably. Croatian government decided that its own target will be establishing a competitive, knowledge-based and export-oriented economy. The goal will be achieved in three strategic areas - economic growth and job creation, efficient government and a better and fairer society. Croatian Bank for Reconstruction and Development is a very important and accountable protagonist in the realisation of economic growth. The Government evidently counts on HBOR to take on an even more significant role in jump-starting the economy, since it, at the very beginning of its mandate, adopted a decision on a substantial increase in the amount of payment to the share capital of HBOR.

The consequences of the financial and economic crisis are reflected in entrepreneurs' reduced capacity for new investment and a growing need for quality sources of funds for liquidity maintenance. Therefore, in 2011 like in previous years, HBOR, as other development banks in the region, focused most of its lending activities on financing working capital in order to contribute to overcoming liquidity problems.

By launching new programmes, providing loans in HRK and extending loan repayment plans, HBOR made its services yet more flexible and varied. In doing so, it facilitated operations to businesses in relentlessly difficult economic conditions. It is important to point out, that, due to its successful long-term cooperation with special financial institutions, in the years of crisis HBOR managed to obtain favourable funding and offer low interest rates to entrepreneurs.

Since 1998, for the purpose of promoting exports as the driving force of the Croatian economy, HBOR has, being an export credit agency, provided export credit insurance for and on behalf of the Republic of Croatia. In 2011, new export credit insurance programmes were launched, and the total volume of export transactions insured by HBOR stood at HRK 1.7 billion, which represents coverage of 2.38 percent of the overall Croatian exports.

In addition to the above, altogether 1,331 loans totalling HRK 3.6 billion were granted to small and medium-sized enterprises through all HBOR's programmes in 2011, an increase of 15 percent compared with the previous year. The upgrading of entrepreneurial and investment climate as well as the strengthening of SMEs are among the key prerequisites for the development of the Croatian economy and among the top priorities of the Croatian Government.

In 2012, HBOR continued to harmonise its operations with the needs of the businessmen and further lowered its interest rates by 1 percentage point for new investments in strategic sectors such as tourism, industry, environmental protection and energy efficiency. In joint efforts of the Government of the Republic of Croatia, the Croatian National Bank, HBOR and commercial banks, a new loan programme for the financing of the development of the economy was launched. The programme is primarily intended for the entrepreneurs with development potential that face difficulties due to objective reasons resulting from the crisis, particularly with regard to the financing of working capital. This is an additional stimulus to the growth of companies aimed at accelerating the growth of economic activities.

On behalf of the Supervisory Board of the Croatian Bank for Reconstruction and Development, I would like to express my satisfaction with HBOR's successful operations in the last year. I am confident that the Bank will continue to successfully support Croatian businessmen and contribute to the development of the Croatian economy in the time to come.

Slavko Linić,

President of HBOR's Supervisory Board

LETTER OF THE PRESIDENT OF THE MANAGING BOARD

Ladies and Gentelman,

The Croatian Bank for Reconstruction and Development, as the development and export bank of the Republic of Croatia, continued to play a key role in supporting Croatian businessmen in 2011. Despite the challenging environment, HBOR operated successfully in the reporting period. When focusing on success, the focus is not only on profits but primarily on a significant number of loans approved at low interest rates, extended grace and repayment periods as well as an increased number of new investment loans.

In 2011, HBOR approved 1,534 loans in the amount of HRK 6.6 billion. Most of the funds were approved for export finance purposes, of which HRK 2.1 billion for pre- and post-shipment export finance. In the reporting period, the number of investment loans rose considerably, and the amount of loans extended for investment purposes stood at HRK 2.8 billion, almost twice the amount approved in the same period last year. We are particularly pleased to point out that investment activities of small and medium-sized enterprises contributed to this growth. HBOR's role in promoting the use of EU funds remained highly significant, which is confirmed by the fact that more than two thirds of all projects accepted under individual measures were financed from HBOR's funds. Through export credit insurance activities performed by HBOR for and on behalf of the Republic of Croatia, transactions worth HRK 1.7 billion were insured.

Since 2010, within the economic recovery measures introduced by the Republic of Croatia, HBOR had been implementing the Programme for the Financing of Working Capital (Model A), whose implementation continued in 2011 with some adjustments. Besides, four more loan programmes were launched: Preparation of Agricultural Production, Female Entrepreneurship, IPARD Measure 101 and 103, and Liquidity. In addition to introducing new loan programmes, HBOR improved the terms and conditions of existing ones and, among other changes, increased the loan-financed portion of investment from 50 per cent to 75 or 85 per cent, depending on the programme. Furthermore, interest rates were reduced under the following programmes: Environmental Protection, Infrastructure, Innovations, whereas a possibility of approving HRK loans was introduced for 13 loan programmes. Under individual loan programmes, grace periods were extended from 2 or 3 to 3 or 4 years, and repayment periods ranging from 10 to 15 years were extended to range from 12 to 17 years. The scope of eligible purposes under the Infrastructure Programme was extended to cover the possibility of including cadastral survey costs and the financing of cadastral survey works intended for the development of real estate cadastre, whereas a possibility of financing a higher percentage of working capital was introduced for the activities in the field of the development of software support solutions under the Innovations Programme.

In the reporting period, the implementation of the project with funds for economic co-operation (ECF) was continued, where HBOR was appointed qualified investor by decision of the Croatian Government. The basic principle of this project is a co-operation of private and public sectors, with the Republic of Croatia monitoring private investors via HBOR. In 2011, the management companies considered investing in 371 projects and decided to invest in 11 projects, out of which two investment decisions were adopted.

In 2011, as in previous years, HBOR continued co-operation with special financial institutions which approved favourable funds for the financing of the Croatian economy. We have concluded a contract in the amount of EUR 18 million with KfW to finance the water supply and wastewater disposal projects, and with the EIB a contract in the amount of EUR 250 million.

In September, the 10th anniversary International Conference on Export Promotion was held in Dubrovnik. The conference gathered more than 160 participants who discussed the challenges and opportunities for Croatian exporters as one of EU member states and the importance of innovative production and exports as the key to long-term development. In 2011, HBOR also hosted the Competition and Development Policy Committee of the European Association of Public Banks (EAPB), an association in which I have held the office of the president since 2010. At a meeting held in October, which was attended by the representatives of European development banks and financial institutions, the representatives of the European Investment Bank presented the conference participants with the JESSICA financial instrument and a method for the approval of project funds aimed at developing small and medium-sized enterprises.

In 2012, we continued to provide additional incentives to Croatian business entities. For example, for new investments in agriculture and fisheries, tourism, industry, environmental protection projects, introduction of renewable energy sources and improvement of energy efficiency, we additionally reduced interest rates by 1 percentage point. By introducing this interim measure, annual interest rates under **most of** our programmes are now 1, 3 or 5 per cent. We extended loans in Kuna under all programmes and also introduced new programmes: Manufacturing Finance, IPA III C Programme, IPA Programme, Loan Programme for the Development of the Economy which was developed in co-operation of the Government of the Republic of Croatia, the Croatian National Bank, HBOR and commercial banks. Entrepreneurs investing in raising the energy efficiency level of buildings and industry facilities were given the possibility to make use of the Grant funds under the European Commission Programme – Energy Efficiency Finance Facility for 2006 and 2007 which was developed and is implemented in co-operation with the European Investment Bank (EIB). We also introduced a new form of lending. By assuming a portion of risk we want to encourage commercial banks to increase loan placements in the industry sector and in this way start an investment cycle. I believe that all these measures taken will result in starting new investments with the final goal to increase the number of employed persons, increase in exports, and the gross domestic product.

On this occasion, I would like to thank all employees of HBOR for their dedicated work and efforts, the members of the Supervisory Board for their support and Croatian businessmen who recognised HBOR as a quality business partner. HBOR will continue to recognise the needs of Croatian business entities and adjust its business operations to such needs.

Anton Kovačev
President of the Managing Board of HBOR

STATEMENT OF PERSONS RESPONSIBLE FOR THE PREPARATION OF THE ANNUAL REPORT

To the best of our knowledge, the 2011 Annual Report includes a fair review of the development, operating results and position of Croatian Bank for Reconstruction and Development and the Group as well as a description of the principal and uncertainties to which Croatian Bank for Reconstruction and Development and the Group are exposed.

Anton Kovačev
President of the Managing Board

Emilija Nagj
Member of the Managing Board

Zagreb, 29th March 2012

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 2011. Revised Financial Statements are shown for HBOR Group and Croatian Bank for Reconstruction and Development.

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:

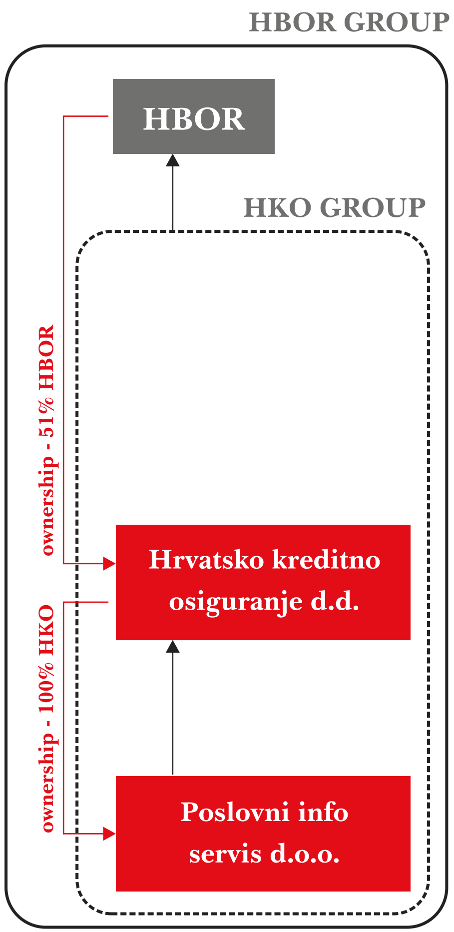
31st December 2011	EUR 1 = HRK 7.530420	USD 1 = HRK 5.819940
31st December 2010	EUR 1 = HRK 7.385173	USD 1 = HRK 5.568252

ABBREVIATIONS

In the Annual Report Croatian Bank for Reconstruction and Development is referred to as the Bank and/or HBOR, and the Croatian Bank for Reconstruction and Development Group as the Group or HBOR Group.

CEB Council of Europe Development Bank
EAPB European Association of Public Banks
EIB European Investment Bank
EIF European Investment Fund
EUR Euro
ECFs Economic Co-operation Funds
HAMAG Hrvatska agencija za malo gospodarstvo (Croatian Agency for Small Business)
HNB Hrvatska narodna banka (Croatian National Bank)
IDFC International Development Finance Club
KfW Kreditanstalt für Wiederaufbau
HRK Croatian kuna
MSP Small and medium-sized enterprise
NEFI Network of European Financial Institutions for SMEs
OeKB Oesterreichische Kontrollbank AG

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 (Croatian Bank for Reconstruction and Development) 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 a parent company of the HBOR Group that was formed in 2010. HBOR is a majority owner (51%) of Hrvatsko kreditno osiguranje d.d. (HKO d.d.) which is a 100% owner of Poslovni info servis d.o.o. (PIS d.o.o.), and the two 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.

Priority activity areas

- Promoting start-ups and development of SMEs
- Promoting exports
- Developing tourism
- Financing innovation and the development of new technologies
- Financing the development of agriculture
- Promotion of EU Funds utilisation
- Financing projects for environmental protection, energy efficiency and renewable energy resources

Audit

HBOR's separate and consolidated Annual Financial Statements for 2011 were audited by the auditing firm Deloitte d.o.o, which expressed its unqualified opinion in an independent auditor's report.

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 2011, there were 270 employees in HBOR.
On 31st December 2011, there were 281 employees in HBOR Group.

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 in the following manner:

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 HBOR's web sites.
- The rating of the Bank is issued by the 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 Croatian Personal Data Protection Agency 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 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.
- An independent compliance function organizes, coordinates and directs the activities concerning the compliance level of HBOR, advises on matters of compliance, controls measures taken to minimize compliance risk, incorporates information on compliance monitoring, identifies and assesses the risks of compliance and provides regular reports.

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.

OVERVIEW OF OPERATIONS OF HBOR GROUP IN 2011

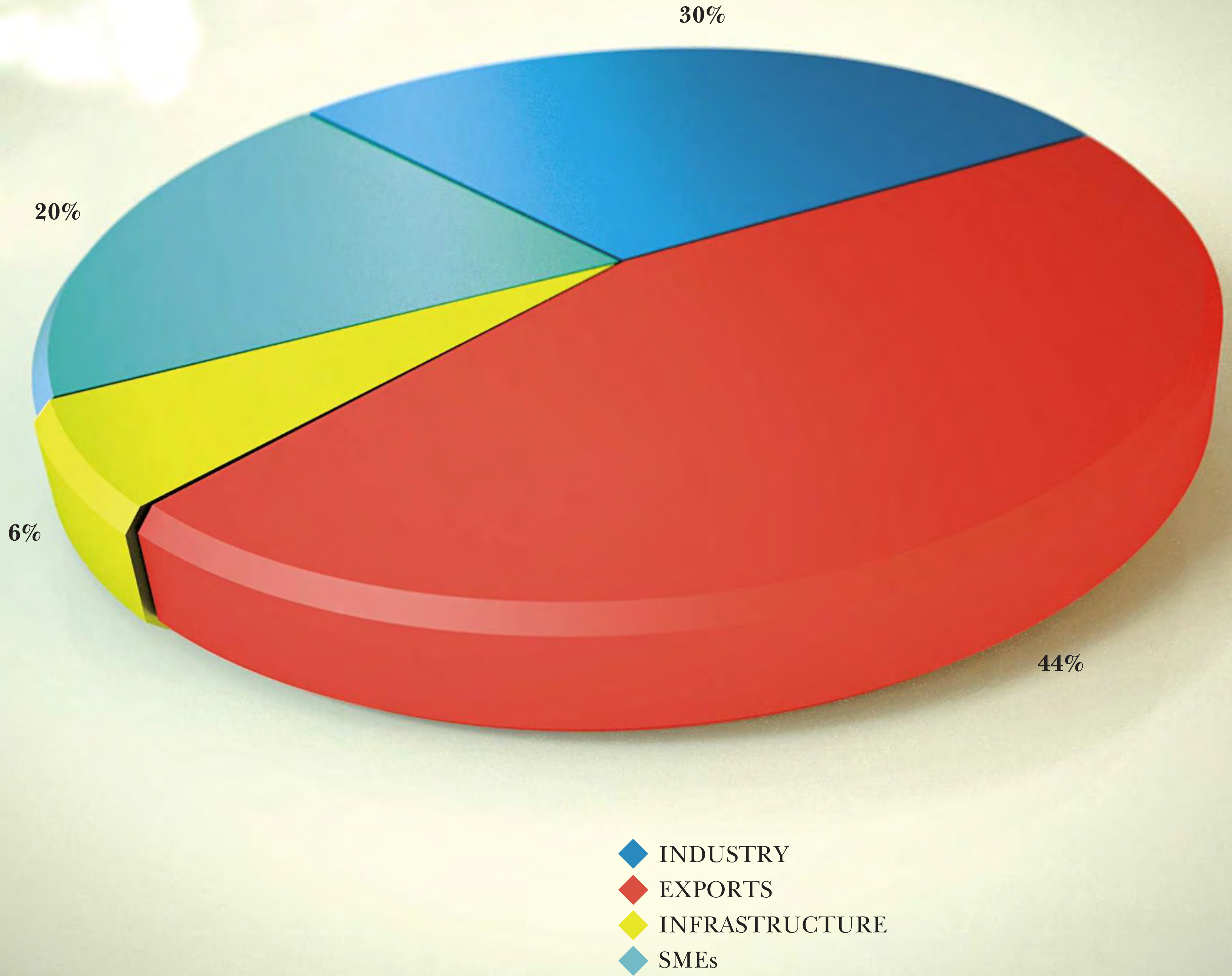
CROATIAN BANK FOR RECONSTRUCTION AND DEVELOPMENT (HBOR)

Within the framework of its business activities, HBOR is primarily focused on long-term financing of investments targeted at raising the level of production, exports, employment and market competitiveness of the Croatian economy. However, just like other development banks in the region, 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 continued directing most of its loans in 2011 at the financing of working capital, thus contributing to the overcoming of liquidity problems. Although the consequences of financial and economic crisis were reflected in the reduced capacity of entrepreneurs for new investments, 2011 still showed a significant increase in the share of investment loans, compared to the year 2010.
Despite the financial crisis which has shaken the EU zone and lowered the state's credit rating in late 2010, HBOR has managed, owing to its reputation and excellent co-operation with special international financial institutions, to provide inexpensive funds and low interest rates for Croatian businessmen in 2011, too. In order to facilitate business operations in 2011, HBOR continued to adjust the conditions of individual loan programmes for investment by means of reducing interest rates, extending the grace period and repayment terms and introducing new programmes which were partly aiming at maintaining and improving liquidity.

OVERVIEW OF LENDING ACTIVITIES OF HBOR IN 2011

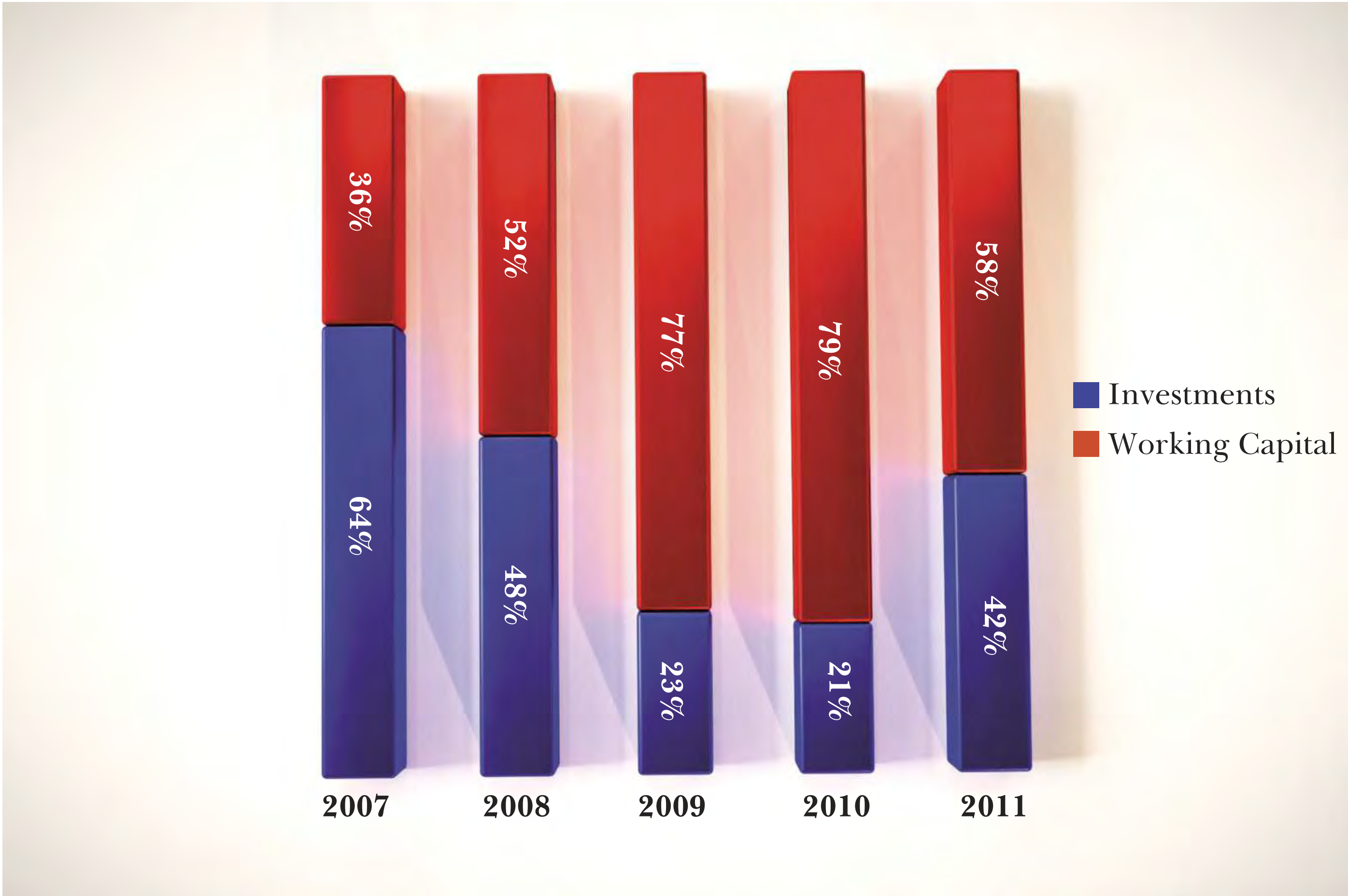
	APPROVED IN EURO	APPROVED IN HRK	LOANS
INDUSTRY	259,241,851.93	1,952,200,026.59	506
EXPORTS	388,349,331.69	2,924,433,574.35	342
INFRASTRUCTURE	54,438,574.41	409,945,329.51	27
SMEs	170,411,807.38	1,283,272,482.56	659
TOTAL LENDING ACTIVITIES	**872,441,565.41**	**6,569,851,413.01**	**1,534**

OWERVIEW OF LENDING ACTIVITIES OF HBOR IN 2011



AMOUNT OF INVESTMENT APPROVALS DOUBLED

In 2011, HBOR approved 1,534 loans totalling HRK 6.6 billion. Most of the funds, amounting to HRK 2.9 billion were extended for the financing of exports. The largest numbers of loans, 1,331 were approved for the financing of SMEs. Although there were no positive developments in Croatian macroeconomic indicators in 2011, and most of the loan proceeds continue to be directed to financing of working capital, the adjustments of loan programmes to suit investment financing has resulted in a significant increase of interest in these funds. Consequently, in 2011 the amount of investment approvals almost doubled, i.e. 661 loans amounting to HRK 2.8 billion were approved (in 2010, 401 loans amounting to HRK 1.4 billion were granted). The loans were used mainly by small and medium-sized enterprises, and although the average investment amount is lower compared to the period before 2008, the increase in their value is still noticeable.



Financing the preparation of agricultural production (Working capital for investments in agricultural production)

Purpose: financing of working capital needed for smooth agricultural production. The loan programme is aimed at financing working capital for current production activities (purchase of raw materials, base materials and other materials for agricultural production), and working capital for the purchase of agricultural products, i.e. covering the whole production cycle – from the preparation of agricultural production to collection of payment for delivered products.

In 2011, 38 loans in the amount of HRK 103 million were approved under this loan programme.

IPARD (Loan programme for IPARD measures 101 and 103 candidate projects)

Purpose: financing candidate projects for co-financing through IPARD programme measure 101 and 103 – in such a way that the entire investment is financed within the framework of this programme.

In 2011, 27 loans in the amount of HRK 154 million were approved under this loan programme.

Liquidity (Loan programme for financing the improvement of liquidity)

Purpose: settlement of obligations towards suppliers, financial institutions and the state as well as settlement of short-term obligations. The goal of the programme is to maintain and improve the final borrower's liquidity.

In 2011, 7 loans in the amount of HRK 29 million were approved under this loan programme.

Female entrepreneurship (Loan programme for the financing of female entrepreneurship)

Goal: promotion of operation start-up and development of small and medium-sized economic entities majority owned by women, in line with the Action plan for the implementation of the Strategy for the development of female entrepreneurship in the Republic of Croatia for the period 2010 – 2013. In 2011, 32 loans amounting to HRK 15 million were approved under this loan programme.

Model A+ and Model B+

Since 2010, within the measures for economic revival of the Government of the Republic of Croatia, HBOR has been implementing the Loan programme for working capital (Model A) and issuing guarantees for and on behalf of the Republic of Croatia for partial coverage of risks of banking placements (Model B). With certain adjustments (Model A+ and Model B+), the activities under both of the models have been continued in 2011.

SMALL AND MEDIUM-SIZED ENTERPRISES

In 2011, one of HBOR's primary goals was to increase the availability of credit facilities to small and medium-sized enterprises with favourable interest rates and thus directly affect their competitiveness and liquidity as well as to encourage start-ups and development of SMEs. In 2011, small and medium-sized enterprises utilised the funds within the framework of 23 loan programs, implemented directly and via commercial banks.

In 2011, 1331 loans for small and medium-sized enterprises were approved, amounting to HRK 3.6 billion which is 15% more than in the year 2010. The information relates to approvals to small and medium-sized businesses across all programmes. The most significant increase in approvals for small and medium-sized enterprises was achieved within the framework of loan programmes for start-ups and development of enterprises and loan programmes for the development of tourism, i.e. 2.5 times more funds were approved than in the year 2010. It is significant that the investments by small and medium-sized businesses doubled, compared to the year 2010.

Under the Loan programme for agriculture and balanced development, a nearly 70% increase in approvals is recorded, and under the Loan programme for micro, small and medium-sized enterprises there was an increase of 150%, compared to the year 2010. The results achieved in the area of financing candidate projects for utilisation of EU funds are particularly significant.

SUPPORT FOR EU FUNDS UTILISATION

With the opening of the process of Croatian accession to the European Union, domestic and foreign companies are granted access to certain EU pre-accession funds. From the very beginning of the availability of these funds, HBOR was actively involved in their realisation and started implementing loan programmes aimed at utilisation of available funds. The objective of these loan programmes is to enable applicants - potential candidates, access to inexpensive loans for financing investments eligible under the IPARD programme.

In 2011, economic entities were able to avail themselves of loan programmes for financing candidate projects for co-financing under IPARD measure 1.1 and 1.2, or measure 101, 103 and measure 302. Within the above framework, 59 loans were approved in the amount of close to HRK 300 million.

From the start of implementation up to 31st December 2011, Agency for Payments in Agriculture, Fisheries and Rural Development has approved 80 applications for IPARD measure 101 and 103. More than 70% of all the approved projects under the IPARD pre-accession programme measures were funded via HBOR.

At the end of 2010, HBOR launched a loan programme for financing candidate projects for **IPARD measure 302** "Diversification and development of rural economic activities", which has also shown excellent results, i.e. HBOR funds were uses for 67% of all of the projects accepted so far.

TOURISM – INVESTMENT FINANCING TRIPLED

Tourism, which provides a significant contribution to increasing and strengthening of Croatian exports, plays a significant role in HBOR's operations, and the bank supports the development of tourist operators, regardless of their size.

In 2011, HBOR implemented four loan programmes intended solely for activities in tourism (Tourism, Preparation of the tourist season, IPARD measure 302 and Development of rural tourism), but other loan programmes were also open for financing of activities in tourism.

In 2011, a total of 119 loans in the amount of close to HRK 800 million were approved to enterprises in the tourist sector, which represents an increase of over 50% compared to the year 2010. In 2011, repayment terms were extended to 17 years plus grace period and the share of HBOR's loans in the investment was increased from 50 to 75%. It is significant that, in 2011, the amount of loan approvals for investment tripled (within the loan programme for tourism) in relation to the year 2010. During 2011, HRK 600 million were approved for this purpose (whereas in 2010, HRK 188 million were approved).

ECONOMIC CO-OPERATION FUNDS

In the second half of 2010, by the Decision of the Croatian Government, HBOR was appointed qualified investor for participation in the establishment of the Economic Co-operation Funds (ECFs), investing for itself and on behalf of the Croatian Government in each of the ECFs an amount equal to the amount invested in the ECF in question by the private investor. In accordance with the Regulations on the conditions and procedure for participation of the Croatian Government in the establishment of ECFs, it is set forth as follows:

- The beneficiaries of ECF's investment are companies with the seat in the Republic of Croatia that are active exclusively or predominantly in the Republic of Croatia
- Envisaged duration of an ECF is 10 years with the possibility of maximum extension of up to 2 years
- The maximum investment obligation of the Croatian Government towards one ECF amounts to HRK 300 million.

ECFs are established and operate in accordance with the Investment Funds Act (Official Gazette of the Republic of Croatia, No. 150/05), as open-end investment funds of private venture capital. At the beginning of 2011, 5 ECFs were established which met all the prescribed requirements and obtained HANFA's (Croatian Financial Services Supervisory Agency) approval for operation.

According to the comprehensive report on ECFs operations in 2011, the management companies considered investments in 371 businesses/projects. Most of the analysed projects are in the manufacturing industry (33%), followed by energy, food processing, services and IT. Most of the considered projects were in the category of small enterprises, as expected since those companies find it most difficult to meet their capital needs. Almost 50% of the companies currently under consideration have capital requirements for future business growth in the range of HRK 20 - 50 million.

In 2011, the ECFs management companies have made 17 preliminary decisions on investment in 11 projects, followed by adopting the decisions to invest in 2 projects.

EXPORT FINANCE

In the field of export promotion, HBOR developed a system of providing exporters with financial support through loan programmes, insurance and bank guarantees modelled on other export banks and export-credit agencies in order to provide Croatian exporters with equal competitive conditions in international markets.

Through the **Pre-shipment export finance programme**, HBOR contributes to the competitiveness of Croatian entrepreneurs and directly influences their success both in the domestic and in the foreign market. HBOR participates in all of the segments of the process of creating the Croatian export product - from pre-shipment to the collection of payment for an export transaction. In 2011, 270 loans amounting to HRK 2.1 billion were approved within the Pre-shipment export finance programme.

The highest loan amounts under the above programme were committed for the benefit of the following industries: food processing (16.9%), chemicals and chemical products (9.3%), final metal products except machinery and equipment (8.9%), wood processing and production of wood and cork products (7.2%).

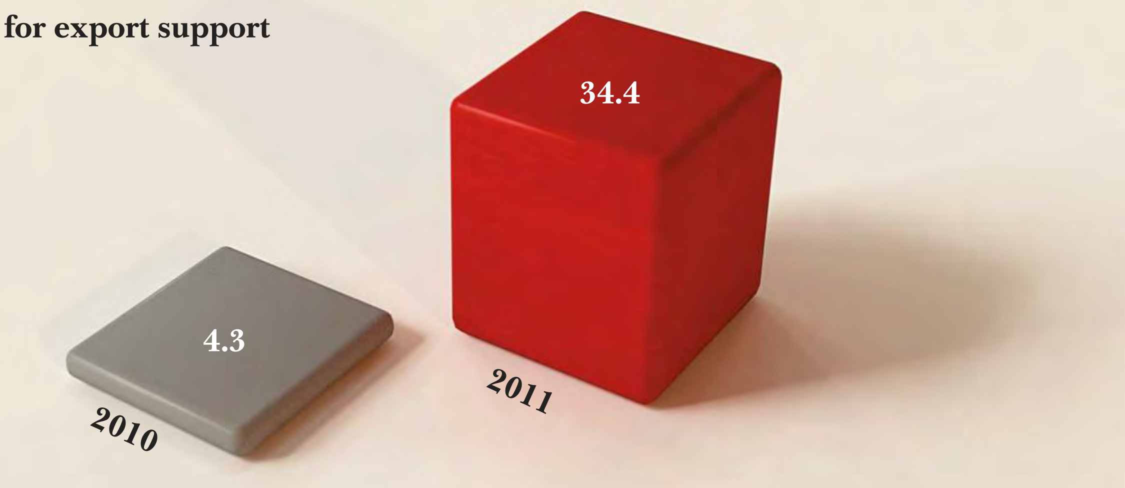
In the reporting period, HBOR also granted loans to exporters under the programme **Exports – IBRD**, in order to enable the borrowers to overcome the period of economic and financial crisis and preserve the present level or expand the volume of exports of goods and services which would affect the improvement of trade balance, employment and liquidity. In 2011, under the above programme

16 loans were approved totalling HRK 101.4 million.

Through the Programme for issuing bank guarantees at the request of an exporter, HBOR supports Croatian exporters for the purpose of winning or performing export contracts.

In 2011, HBOR issued 8 bank guarantees for export support in the amount of HRK 34.4 million (which represents a significant increase compared to the amount of HRK 4.3 million in 2010). The objective of the Programme is issuing bank guarantees for the purpose of winning and performing contracts for the export of goods, works and services.

Bank guarantees for export support
(in HRK million)



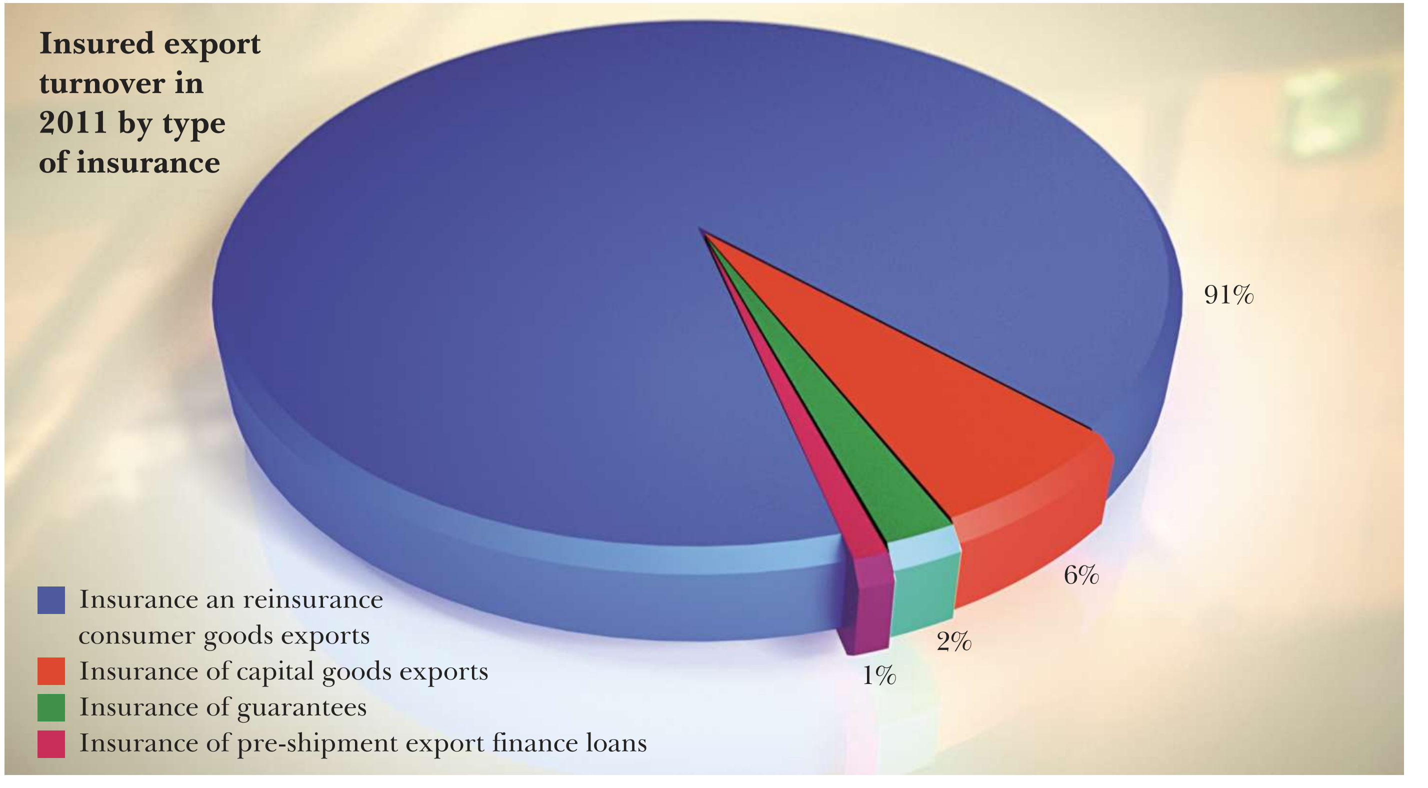
HBOR is implementing programmes for export promotion with an intention of increasing competitiveness and value of Croatian exports as well as improving recognisability and quality of Croatian products and services in the world market.

EXPORT CREDIT INSURANCE AGAINST NON-MARKETABLE RISKS IN 2011

HBOR provides insurance and reinsurance of export against non-marketable risks as an export-credit agency for and on behalf of the Republic of Croatia. HBOR has been carrying out the activities of export credit insurance since 1998, as an important support pillar for Croatian exporters. Export credit insurance programmes provide a comprehensive service covering commercial and political risks in all phases of an export transaction – from pre-shipment export finance to export and the collection of payment for an export transaction. Insurance services are intended for exporters directly as well as for financial institutions providing financing for export transactions.

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

Total insured export turnover backed by HBOR within the export credit insurance activities in 2011 amounted to HRK 1.70 billion which stands for 2.38% of Croatia's total exports. The insured export turnover recorded a 21% decrease compared to the year 2010, which is a result of the separation of activities on insurance against marketable risks performed on a commercial basis from operations performed for and on behalf of the Republic of Croatia (non-marketable risks).



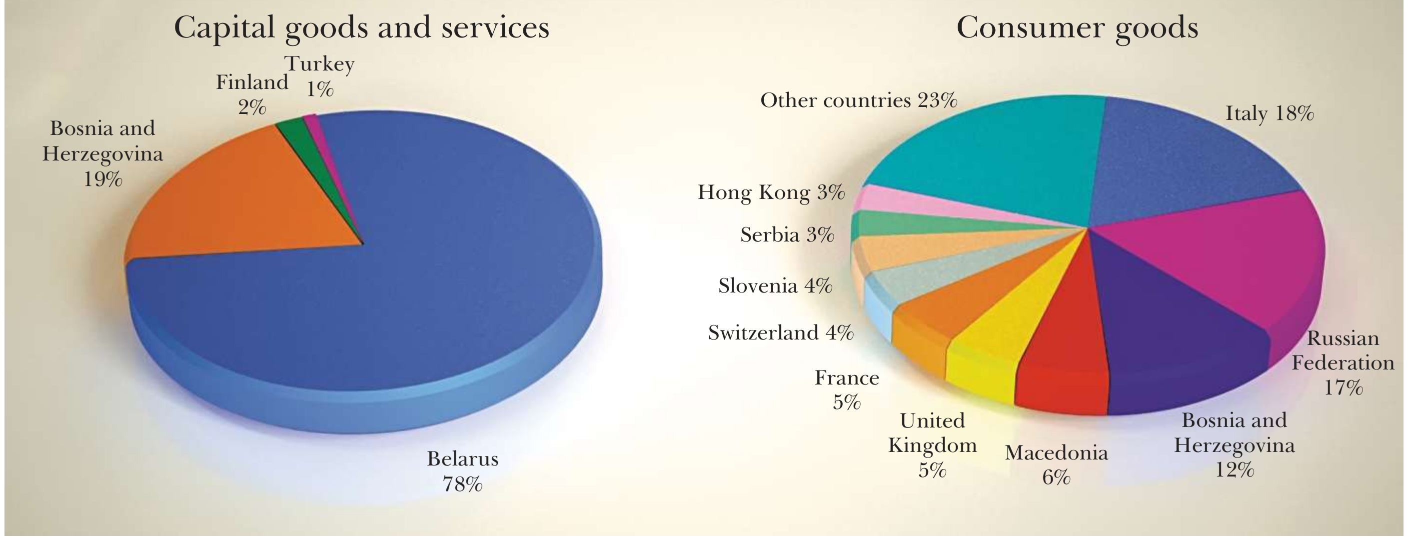
In order to support Croatian exports in the challenging business environment characterized by illiquidity and difficult access to finance, HBOR approved, in 2011, a new cover for export transactions in the amount of HRK 544 million for Croatian exporters and financial institutions supporting exporters. The amount of HRK 385 million was approved for the insurance and reinsurance of exports of consumer goods, which provided cover for an export turnover of HRK 1.54 billion mostly for exporters in the metal, non-metal, paper, pharmaceutical, textile, wood and construction industries. The amount of HRK 102 million was approved for the insurance of exports of capital goods and services, and the amount of HRK 23.5 million was approved for the insurance of pre-shipment export finance loans. The amount approved for the insurance of bank guarantees equalled HRK 34 million. In 2011, the most important export markets were Bosnia and

Herzegovina, Italy, Russian Federation, Belarus, Algeria and Macedonia. Through insurance, support was provided for the export of Croatian goods and services to 54 countries for altogether 693 foreign buyers.

NEW EXPORT CREDIT INSURANCE PROGRAMMES

In its endeavours to adequately respond to the needs of Croatian exporters, HBOR launched, in 2011, the Programme for the Insurance of Bank Guarantees Issued for the Purpose of Winning or Performing Export Contracts. The Programme offers exporters and their banks a possibility to insure the risk of payment under a guarantee, which facilitated exporters' access to increasingly demanding export markets. In 2011, the first insurance policy was issued under the Programme providing cover for the counter-guarantees issued in favour of investors for the export transaction of constructing a medical and surgical centre and a boarding school in Algeria.

Breakdown of amounts insured in 2011 by country and type of goods



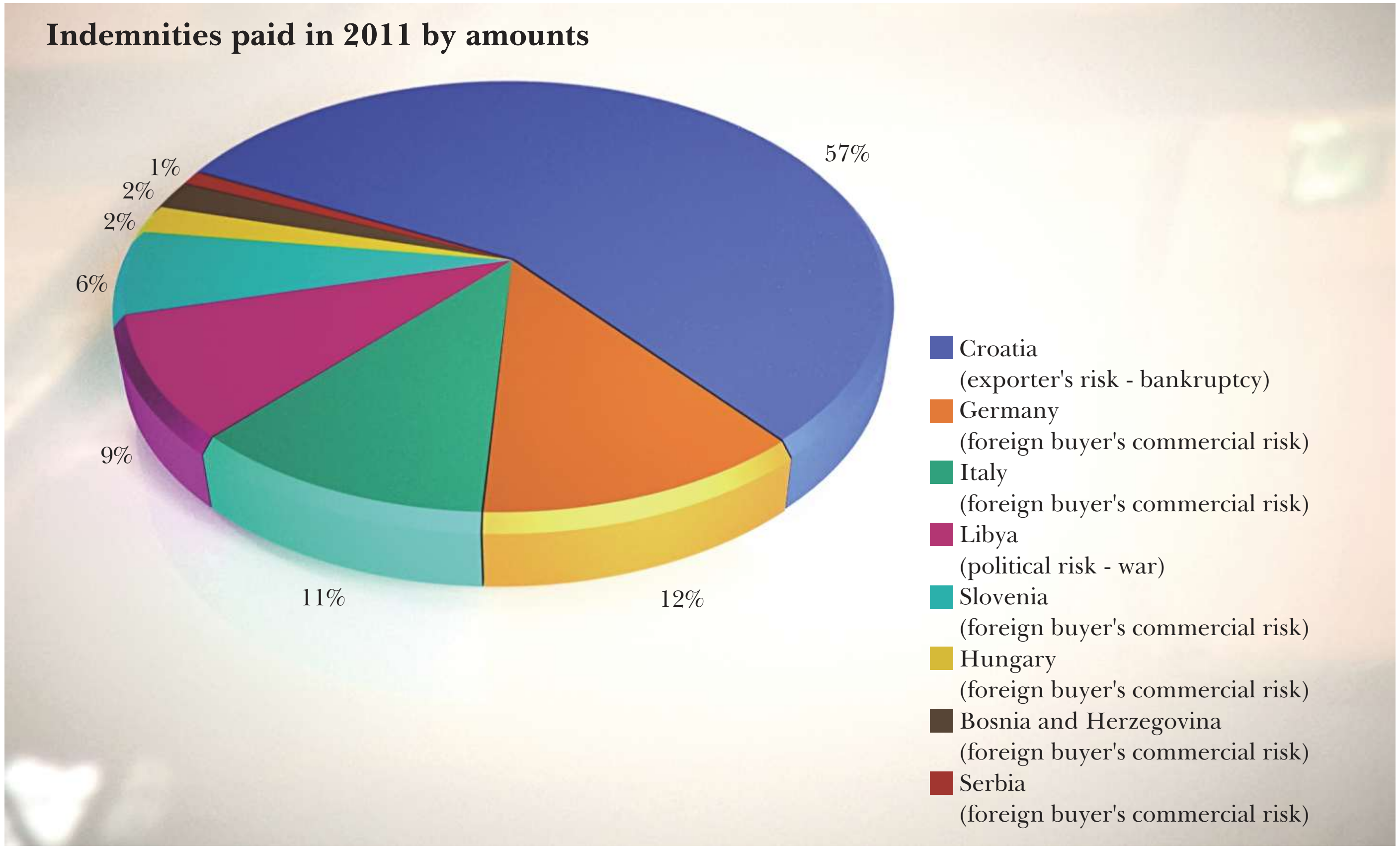
In 2011, the following significant capital projects of Croatian exporters were supported through export credit insurance programmes:

- Modernization of an oil refinery in Belarus
- Rehabilitation of hydro power plant "Rama" in Bosnia and Herzegovina
- Delivery of telecommunications equipment to Bosnia and Herzegovina
- Renovation and upgrade of generators for three hydro power plants in Finland
- Delivery of equipment for tunnels in Turkey
- Construction of a medical and surgical centre and a boarding school in Algeria

- Manufacture of machinery for the mines in the South African Republic

In 2011, HBOR issued two letters of intent for insurance, thus enabling Croatian exporters to participate in international tendering procedures for the following projects:

- Construction of a 400 kV transmission line Albania – Kosovo
- Construction of a 108 MW hydro power plant in Georgia



In 2011, altogether 18 indemnities were paid to the insured parties totalling HRK 13.25 million. Of the total amount of indemnities paid, 66% relates to the two largest individual indemnities, of which one was paid under the policy of insurance of pre-shipment export finance loan due to the bankruptcy of exporter, and the other was paid under the payment collection insurance policy due to the occurrence of political risk in Libya. The remaining 16 indemnities paid in 2011 in the amount of 4.5 HRK million resulted from the growing problems in operations and liquidity encountered by foreign buyers in previous years (2009 and 2010), which is a direct consequence of the global economic crisis and the situation in financial markets.

FUND RAISING

In 2011, HBOR continued negotiations with special financial institutions pertaining to the raising of long-term funding at the best possible terms and conditions.

In October 2011, HBOR and Kreditanstalt für Wiederafubau (KfW) entered into a EUR 18 million loan agreement for the financing of water supply and wastewater disposal projects in the Republic of Croatia.

In December 2011, the European Investment Bank (EIB) approved HBOR a new loan of EUR 250 million for the financing of small and medium-sized companies, medium-capitalised companies (mid-cap companies), environmental protection projects and infrastructure projects in the public and the private sector. In February 2012, the first tranche of the loan was signed in the amount of EUR 150 million, whereas it is expected that the second loan tranche of EUR 100 million will be signed in the third quarter of 2012.

In the second half of 2012, further loan agreements are expected to be signed with the Council of Europe Development Bank (CEB) for the purpose of financing SMEs and local governments of the Republic of Croatia, and with the International Bank for Reconstruction and Development (IBRD) for the financing of projects implemented by exporters and tourism companies.

RISK MANAGEMENT

Pursuant to the Act on HBOR, the Bank is obliged to reduce risks in its operations to the lowest level possible by applying the principles of banking operations. In the risk management process, the Bank continuously controls, identifies, assesses, measures and supervises all risks it is exposed to in its operations. The manner, actions and frequency of measurements and assessments in risk management are prescribed by the Bank's general documents. In its day-to-day operations, the Bank manages credit risk, liquidity risk, interest rate risk, currency 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 that 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, assessing, measuring, controlling and giving suggestions and recommendations for adequate management of exposure to credit and non-credit risks, by developing risk-related procedures and methodologies, by recommending and monitoring the adherence to the adopted exposure limits, by risk-related reporting to the Managing Board and other committees, etc.

When assessing and measuring risks, the Bank takes into account historical data, business plans, market conditions and the specific features of the Bank as a special financial institution. The results of measurements/assessments and analyses conducted in the field of risks are presented at the meetings of the risk management committees, the Managing Board and the Supervisory Board. A system of limits has been established for the purpose of managing, monitoring and controlling credit risk, liquidity risk, interest rate risk and currency risk. The Bank monitors risks by means of scenario analyses, sensitivity analyses and stress tests. Systems of proactive risk management are developed for the purpose of preventing the occurrence of potential risks.

The Managing Board of HBOR is responsible for implementing a risk management strategy and establishing and implementing an effective and reliable system for the management of all risks. For the purpose of accomplishing its function, the Managing Board has delegated its powers to three risk management committees:

The Asset and Liability Management Committee – manages liquidity risk, interest rate risk and currency risk within the prescribed policies and procedures regulating this area,

The Credit Risk Assessment and Measurement Committee – manages credit risk within the prescribed policies, procedures and other internal documents 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.

The risk management strategy aims to achieve and maintain a good and efficient system of risk management in line with the local and international banking practices and the recommendations of the Croatian National Bank and the Basel Committee.

Credit risk

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 that determine the internal control systems aiming to act preventively.

HBOR's Managing Board conducts a conservative credit risk management policy. The credit risk management system represents the most important part of HBOR's business policy and an important factor of its business strategy. Therefore, this area is regulated by a separate document called the Credit Risk Management Procedures that applies to all phases of the credit process (from the development of new banking products, loan applications to final loan repayments). The Credit Risk Management Procedures represent a comprehensive document comprised of separate methodologies aimed at evaluating various client target groups.

In order to mitigate credit risk and reduce operating costs, the Bank, in accordance with the HBOR Act, on-lends part of its placements via commercial banks that assume the risk of collecting repayments from final borrowers. Generally, all direct placements are secured by mortgage on immovable property, and, if possible, the Bank requires guarantees issued by the HAMAG (Croatian Agency for Small Business) and other first-class guarantees for the purpose of providing security against credit risk. The Bank determines the required ratio between 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 development 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 regions and loan programmes. 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 activities.

Liquidity risk, currency risk and interest rate risk

The Bank ensures the management of liquidity, currency and interest rate risks through the Asset and Liability Management Committee. The management of these risks implies the minimising of interest rate risk, currency risk and liquidity risk. A significant number of Bank's organisational units is directly or indirectly included in the activities of the Asset and Liability Management Committee in order to ensure a high-quality, integrated and comprehensive risk management system.

Liquidity risk

Liquidity risk is a risk of financial loss arising from the Bank's present or expected inability to meet its financial liabilities when due. The basic principles for managing HBOR's liquidity risk are defined in the Liquidity Risk Management Procedures as well as in the decisions and conclusions made by the Supervisory Board, the Managing Board and the Asset and Liability Management Committee.

For the purpose of managing liquidity risk, i.e. in order to operate within the limits prescribed for liquidity risk management purposes, the Bank maintains the necessary level of liquidity reserves, continuously monitors current and planned liquidity, and provides sufficient kuna and foreign currency funds necessary for timely settlement of obligations and disbursements under committed loans and planned commitments. In terms of liquidity risk management, the Bank monitors and strives to achieve compatibility of existing and planned placements and sources according to maturity. The Bank monitors liquidity risk also through scenario analyses, sensitivity analyses and stress tests. In this way, both regular business operations and operations under stress are included. Early warning signals and procedures for liquidity crisis indication or occurrence are determined.

HBOR, as a special financial institution, is not profit oriented and does not use derivatives. Derivatives may only be used for the protection of its own positions.

Interest rate risk

Interest rate risk is the financial risk that occurs due to interest rate mismatch in the value and maturity of interest-sensitive assets, liabilities and off-balance sheet items. The basic principles for managing the Bank's interest rate risk are defined by the procedures, decisions and conclusions made by the Managing Board and the Asset and Liability Management Committee. For the purpose of measuring and monitoring interest rate risk, the Bank analyses the interest rate gap. The interest rate gap is analysed by specific periods on the basis of possibility of change in interest rates and it illustrates the sensitivity of the Bank to such changes in interest rates. Interest rates are elaborated in detail per currency, type and value of interest rate, and projections of developments in average weighted interest rates for Bank's sources and placements are prepared. 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 the matching of interest rates on sources and placements, the current market conditions and development projections for basic market indicators are also monitored.

Currency risk

Currency risk represents the exposure of the Bank to changes in foreign exchange rates and it arises, above all, out of asset and liability currency mismatch that could result in higher expenses and/or not realized projected income. The basic concepts and principles of HBOR's currency risk management are defined by the procedures, decisions and conclusions made by the Managing Board and the Asset and Liability Management Committee. The methods for the measurement/assessment, monitoring and management of currency risk have been established, the limits and procedures in the case of crisis indication or occurrence have been determined, and the reports necessary for overall currency

risk management have been defined.
For the measurement of currency risk exposure, the Bank monitors the open foreign currency position. In addition to the daily monitoring of the open foreign currency position, the Bank uses VaR model for the purpose of assessing and measuring currency risk and reports on maximum possible losses by significant currencies to the bodies in charge regularly. Scenario analyses, sensitivity analyses and stress tests are conducted.

Operational risk

Operational risk is the risk of loss arising from inadequate internal processes, human errors or external events. The Bank seeks to minimize operational risk by introducing controls into operating processes and by developing a unique and comprehensive information system.
For the supervision and monitoring of the IT system, HBOR's Information System Management Committee was established. The main task of the Committee is to manage information system resources and establish an adequate level of efficiency and security of the IT system in order to adequately manage risks arising from the use of IT technology. As significant operational risks arise from the use of the information technology, HBOR established the function of the Head of Information System Security.
Due to the presence of operational risk in all HBOR's business activities and for the purpose of compliance with banking regulations and good practice principles in the field of risk management, HBOR launched, in 2011, a procedure of public procurement of a comprehensive solution and consulting services for the upgrading of the operational risk management system.

CONTROL AND AUDIT

The unit Control and Audit is part of HBOR's supervision system in charge of monitoring overall operations based on the principles of legality, application of Croatian internal audit standards and HBOR internal documents. Control and Audit, as an organisation unit, carries out its tasks independently and determines the manner of operating and reporting as well as preparing its findings, opinions and recommendations on its own. It is directly responsible to the Managing Board, the Audit Committee and the Supervisory Board of HBOR, to which reports are submitted quarterly or semi-annually. Based on the audit report and according to the recommendations of the Control and Audit, the Managing Board makes the necessary decisions to take corrective measures and activities. The 2011 audit findings as well as the status of recommendations given and actions taken were submitted to the Managing Board, the Audit Committee and the Supervisory Board within the Control and Audit regular reporting scheme.

COMPLIANCE MONITORING FUNCTION

The function of monitoring compliance has been established as an independent and permanent function under the Managing Board of HBOR.

Compliance monitoring activities include the identification and assessment of compliance risk to which HBOR is or might be exposed, the advising of the Managing Board and other responsible persons on the manner of applying relevant laws, standards and regulations, including the information on the latest news regarding these issues.

The compliance monitoring function evaluates the impacts that the amendments to the relevant regulations will have on the operations of HBOR, assesses the compliance of new products or procedures with the relevant acts and regulations and with the amendments to the regulations, provides advice during the preparation of compliance-related training programmes and deals with complaints procedures.

The compliance monitoring function periodically reports to the Managing Board, the Audit Committee and the Supervisory Board of HBOR.

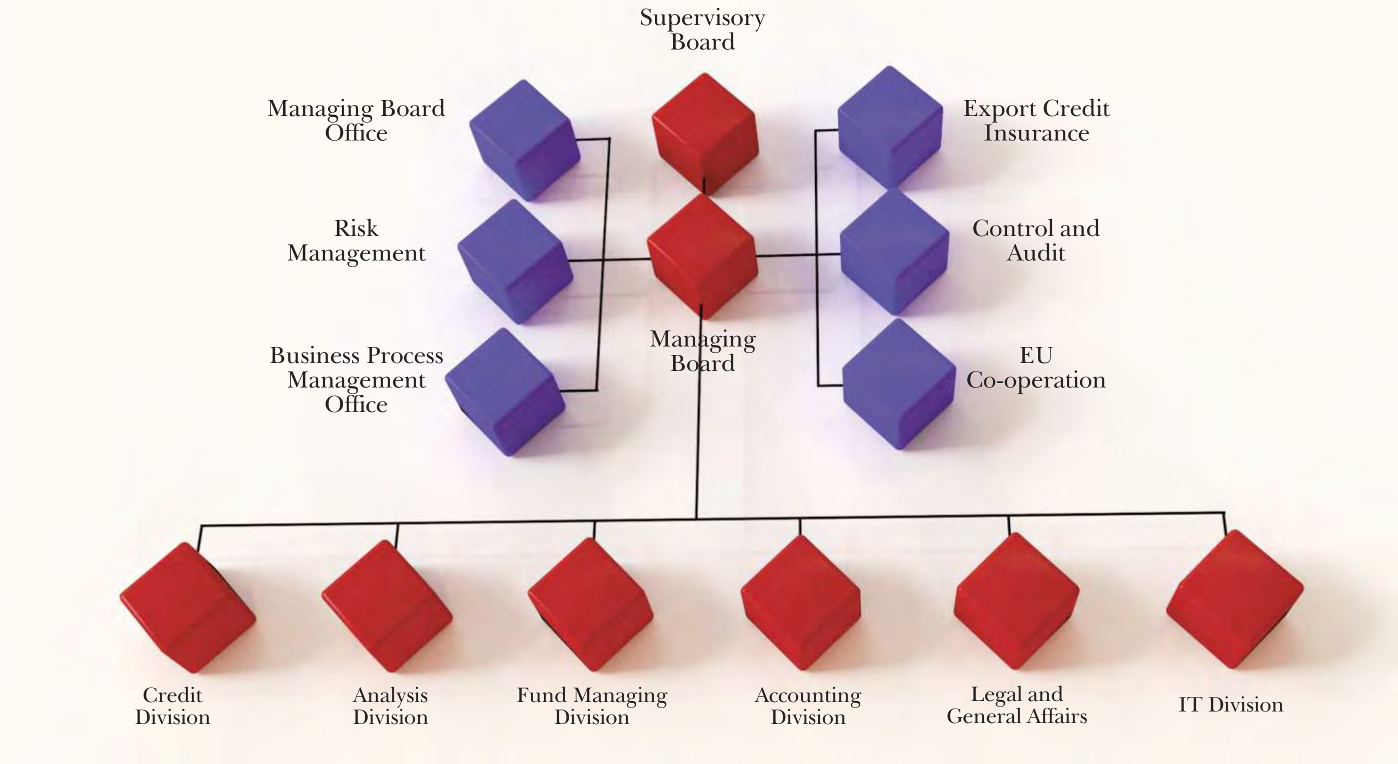
HUMAN RESOURCES

In the human resources development strategy, each individual should be given the opportunity to realise his/her personal and professional potentials so as to develop professional, motivated and satisfied employees who are an important segment of the process of socially responsible financing and almost 20 year old successful operations of the bank.

Beside numerous measures of human resources management that have been implemented and improved by HBOR for a number of years, in 2011, a new programme of in-house training of employees was introduced. The purpose of this programme is to exchange know-how and skills among employees. Through various internally developed programmes, specially trained employees from various organisational units transfer important information from their field of work to co-workers, thus enhancing communication, understanding and co-operation within the bank, and providing a broader picture on the purpose and manner of operation of the entire organisation to employees. Beside the classic training, a number of presentations was held for the purpose of advancing the knowledge and awareness about the changes in legislation and adjustment to the European Union regulations.

As recognition for excellent implementation of HR processes, HBOR has been assigned the Employer-Partner Certificate for this year also. The certificate is assigned by MojPosao and by the

Organisational structure of HBOR



Selectio group for excellence in human resources management.

From year to year, HBOR retains the structure of highly educated employees: on 31st December 2011, there were 270 employees, of which 82.22% with a university degree. The average age of employees is 40.

Regional offices

In 2011, in addition to their regular activities relating to the provision of information and advice to entrepreneurs on loan programmes and lending possibilities, the provision of support in the preparation of loan application documentation, site visits for the purpose of project control and preparation as well as contacts and agreements with commercial banks in the area, the regional offices participated in the presentations of HBOR's programmes in co-operation with the Croatian Chamber of Economy, the Croatian Chamber of Trades and Crafts, regional chambers, local government units and development agencies. Independently or together with local government units, they participated in the presentations of HBOR's operations in trade fairs.

A Co-operation Agreement was signed with the Rijeka Faculty of Economics in 2011. The purpose of the Agreement is to promote co-operation in the field of science and development through exchanging information, conducting thematic researches, organising seminars, workshops, round tables, conference and training programmes and implementing the pilot-project “Student Entrepreneurship”.

International co-operation

In the reporting period, HBOR participated actively as a member in numerous associations, clubs and chambers that gather institutions from EU member states.

As the President of the EAPB, Mr. Anton Kovačev represents the members of the Association towards the bodies of the European Union, particularly the European Commission, the European Parliament and the European financial institutions, and participates in the round table organised by the American European Community Association (AECA). In October 2011, HBOR hosted the meeting of EAPB's Competition and Development Policy Committee, on the occasion of which the representatives of the European Investment Bank (EIB) in charge of the JESSICA financial instrument and the granting of funding for SME development projects participated in the discussions.

HBOR is the only associated member of the Network of European Financial Institutions for SMEs (NEFI) coming from outside the European Union. It is a participant in the Permanent Working Group, whose meetings it joins regularly.

In April and September 2011, HBOR was part of the delegation of the Republic of Croatia to the

Spring Meetings and the Annual Meetings of the World Bank and the International Monetary Fund, and joined the Annual Forum of the European Bank for Reconstruction and Development in May.

Continuing the tradition of successfully gathering and connecting exporters and other distinguished representatives of Croatian companies, banks, foreign export banks, export credit agencies and international financial institutions, HBOR organised its 10th International Conference on Export Promotion in September 2011. The conference brought together more than 160 exporters and those who participate in the creation of export products and they exchanged experiences and practices aimed at competitiveness. In order to enable exporters to better prepare and organise their future businesses and strengthen export, special discussions were devoted to exports in the light of the imminent joining of the European Union, its consequences on Croatian exports and the experiences of new member states.

During the Conference, a debate took place on the manner of and possibilities for overcoming the obstacles that the exporters face in their operations, such as creation of innovative products and development of technological processes aiming to increase competitiveness in the foreign markets.

HBOR is one of the founders of the International Development Finance Club (IDFC) that started to operate at the meeting of 19 CEOs of national and regional development banks and financial institutions organised by KfW, the German development bank, in Washington in September 2011. The IDFC was established for the purpose of contributing to the promotion of energy efficiency and the mitigation of climate change in its member countries. The IDFC would like to promote the GCF (UN Green Climate Fund with a potential volume of several tens of billions of Euros) by presenting a mutual strategy and existing projects.

As one of the shareholders of the EIF, HBOR participates in the operational and institutional development of the EIF and is involved in all decision-making processes and projects of the European Union related to SMEs.

As an associate member, HBOR regularly participates in the work of the Club of Institutions of the European Union Specialising in Long-Term Credit (ISLTC Club).

Special attention is paid by HBOR to the co-operation with export banks and export credit agencies. During the reporting year, HBOR continued to implement the activities aimed at strengthening partnerships with similar institutions in Europe and worldwide and signed co-operation agreements with the following institutions: ABC International Bank plc (ABCIB), China Development Bank Corporation (CDB), Lebanese Credit Insurer s.a.l. (LCI), and Cassa Depositi e Prestiti (CDP).

Public disclosure of activities

Public disclosure of activities is considered by HBOR to be an important precondition for the credibility of its operations. Therefore, HBOR pays special focus on providing complete and understandable information to the public about its goals and the measures for their attainment as well as about the results of its activities. Through various forms of providing information, HBOR regularly informed the public in 2011 about all important activities. In the reporting period, HBOR published twenty press releases. Seven press conferences took place for the purpose of informing the public about operations, attained results, new loan programmes and amendments to the existing ones. All business information can be accessed by the public on HBOR's website, except for the information subject to Articles 168 and 169 of the Credit Institutions Act. During the reporting year, 38 public procurement procedures were published in the Electronic Public Procurement Classifieds, whereas all bidding announcements have been published on HBOR's website: www.hbor.hr since August 2010. In 2011, no requests for access to information pursuant to Article 25 of the Act on the Right of Access to Information were received.

HRVATSKO KREDITNO OSIGURANJE GROUP

HRVATSKO KREDITNO OSIGURANJE d.d. AND POSLOVNI INFO SERVIS d.o.o.

Hrvatsko kreditno osiguranje d.d. (hereinafter: HKO or the Company) is a joint-stock insurance company which started its operations on 1st July 2010. Therefore, 2011 is the first full year of the Company's operations.

HKO is the first insurance company in the Republic of Croatia specialised exclusively for the insurance of short-term receivables (payment terms up to 180 days, exceptionally up to 1 year) arisen from the sale of goods and services among business entities. The insurance covers political and commercial risks.

In 2011, HKO offered two main insurance products: insurance of export receivables and insurance of domestic receivables.

Total subscribed and paid-in capital of HKO amounts to HRK 37.5 million, and the founders and major shareholders are: HBOR, 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 49% share.

For the purpose of strategic support to business operations, on 26th October 2010 HKO established Poslovni info servis d.o.o. By establishing this company, HKO started to operate as the Hrvatsko kreditno osiguranje Group (hereinafter: the HKO Group) and to state its consolidated financials. Poslovni info servis d.o.o. (hereinafter: PIS) is in charge of the implementation of analysis and assessment of credit risks relating to the insurance transactions within the Group.

On 31st December 2011, there were 11 employees in the HKO Group, of which Hrvatsko kreditno osiguranje d.d. employed 9, and PIS 2. All employees of the HKO Group have a university degree. In comparison with the previous year, the Company increased the number of its employees by 2. In 2011, three new employees were employed, and one employee left the Company.

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 the Company.

The management bodies are:
The Managing Board
The Supervisory Board
The Shareholders' Meeting

The Managing Board
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 the Company.

The management bodies are:
The Managing Board
The Supervisory Board
The Shareholders' Meeting

The Managing Board
The Managing Board of HKO in 2011 remained unchanged and its members were as follows:
Edvard Ribarić, Chairman of the Managing Board
Anton Ludwig Steffko, Member of the Managing Board

Authorised representative
Ružica Adamović

HKO Supervisory Board
In 2011, there were no changes in the Supervisory Board and its members were as follows:
Branimir Berković, Chairman of the Supervisory Board
Helmut Hans Altenburger, Deputy Chairman of the Supervisory Board
Ante Artuković, Member of the Supervisory Board

Manager of Poslovni info servis d.o.o.

Ivana Paić-Mikulek

HKO Audit Committee

In 2011, the members of the Audit Committee were:
Branimir Berković, Chairman
Helmut Hans Altenburger, Deputy Chairman
Ante Artuković, Member
Katica Smojver, Member

Reporting to the supervisory bodies

In 2011, the company provided regular reports to the supervisory bodies pursuant to the Insurance Act, the regulations of the Croatian Financial Services Supervisory Agency and other regulations on all relevant facts and changes in the Company in force. The Company regularly met all requirements of the supervisory bodies in terms of operations control and submission of the Company's data, with no objection by the supervisory bodies.

OPERATIONS IN 2011

At the end of 2011, HKO had 36 concluded insurance contracts in its portfolio, 10 contracts more in comparison with the previous year. On 31st December 2011, 926 credit limits were covered by the insurance, 20% more in comparison with the previous year. In the total structure of limits, two credit limits relate to domestic receivables, and 924 credit limits relate to export receivables towards 46 countries. The total volume of insured transactions in 2011 amounted to HRK 2,284 million.

The structure of exposure by countries reflects the structure of Croatian exports, which means that 57.7% of total exposure related to the following 5 countries: Italy (21.5%), Germany (12.1%), Bosnia and Herzegovina (8.4%), Serbia (8.2%) and Slovenia (7.5%).

In 2011, the total charged premium amounted to HRK 6.7 million. The share of reinsurance in the charged premium amounted to 72.89%, which is slightly lower than the share in 2010 – 75.61%.

In 2011, the net premium earned from reinsurance amounted to HRK 1.25 million.

2 indemnities were paid in 2011, of which one was completely liquidated, whereas the total amount of payments for insured cases amounted to HRK 765.8 thousand. The paid indemnities relate to buyers

in Germany and Slovenia. In 2011, the arisen damage, net from reinsurance amounted to HRK 229.7 thousand. The share of damage in 2011 amounted to 55.8%.

Acquisition costs, administration costs and other operating expenses of the Group in 2011 amounted to HRK 4.3 million, whereas at the Company level, they amounted to HRK 3.7 million.

The business year 2011 is the first full year of operations, and the Group made expected loss of the current year in the amount of HRK 1.1 million on the Group level, in comparison with the loss of HRK 730.4 thousand in the previous year.

On 31st December 2011, the total assets of the HKO Group amounted to HRK 39 million, an increase by 0.3% in comparison with the previous year. As at 31st December 2011, the total capital amounted to HRK 35.7 million, and technical reserves net from reinsurance amounted to HRK 1.5 million.

INDICATORS OF INSURANCE BUSINESS

	2010.	2011.
Volume of insured transactions (in HRK '000)	802,041	2,284,219
Exposure, as at 31st December (in HRK '000)	671,694	842,704
Gross premium charged (in HRK '000)	1,551	6,687
Paid indemnities (in HRK '000)	-	766
Number of paid indemnities	0	2
Number of limits-buyers	771	926
Number of contracts	26	36
Number of insured parties	26	36

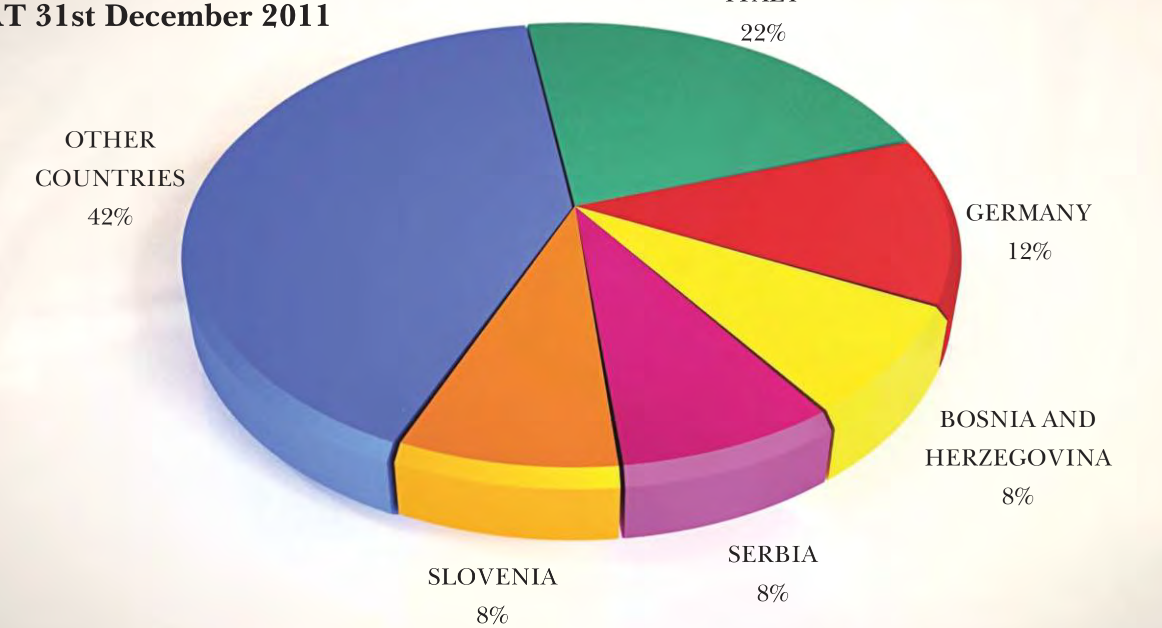
EXPOSURE BY LIMIT AMOUNT, 31st December 2011

Country	Amount (in HRK '000)	Share (%)
ITALYA	181,374	21.5
GERMANY	101,781	12.1
BOSNIA AND HERZEGOVINA	70,906	8.4
SERBIA	69,205	8.2
SLOVENIA	63,195	7.5
RUSSIA	43,594	5.2
BELGIUM	30,668	3.6
CROATIA	30,000	3.6
MACEDONIA	24,376	2.9
AUSTRIA	22,840	2.7
OTHER COUNTRIES	204,766	24.3
TOTAL	**842,704**	**100.0**

BY NUMBER OF APPROVED LIMITS, 31st December 2011

Country	Number of limits	Share (%)
ITALY	161	17.4
GERMANY	140	15.1
BOSNIA AND HERZEGOVINA	97	10.5
SLOVENIA	96	10.4
SERBIA	85	9.2
AUSTRIA	43	4.6
HUNGARY	43	4.6
MACEDONIA	26	2.8
FRANCE	24	2.6
MONTENEGRO	21	2.3
OTHER COUNTRIES	190	20.5
TOTAL	**926**	**100.0**

EXPOSURE BY COUNTRIES, AS AT 31st December 2011



PRINCIPLES OF FINANCIAL REPORTING

The HBOR Group prepares:

1. Separate financial statements of the parent company – Croatian Bank for Reconstruction and Development and
2. Consolidated financial statements that include HBOR and the companies under its control – subsidiary companies.

When preparing and presenting its annual financial statements, the HBOR Group applies International Financial Reporting Standards (IFRS). Consequently, all data and financial statements for consolidation are prepared by the members of the Group in accordance with the IFRSs.

Financial statements are prepared and presented with the objective to provide information on financial position, success in operations and changes in the financial position of HBOR and the HBOR Group in order to enable their users to make appropriate economic decisions.

Financial statements are prepared and presented with the purpose of availability of the information on financial position, success in operations and changes in the financial position of HBOR and the HBOR Group to their users on a regular basis as well as giving financial information about how the strategy of the HBOR Group is carried out.

In financial reporting and disclosures, the HBOR Group applies the following principles:

- **Transparency in disclosure** in order to enhance its users' understanding of the presented information,
- **Consistency in presentation** within each reporting period and between reporting periods,
- **Simplicity in disclosure** in order to allow the users to gain easier understanding of the financial position, business performance and changes in financial position as well as to ease decision-making,
- **Focusing on legal requirements** in order to ensure compliance,
- **Application of the best presentation practices** appropriate to the Group's activities with respect to the up-to-date international trends in financial reporting, as well as market requirements.

OVERVIEW OF FINANCIAL PERFORMANCE IN 2011

The HBOR Group was formed in 2010. It consists of Croatian Bank for Reconstruction and Development as the parent company and subsidiary companies Hrvatsko kreditno osiguranje d.d. and Poslovni info servis d.o.o. that constitute the Hrvatsko kreditno osiguranje Group (HKO Group).

The consolidated financial statements for 2010 were the first 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 separate, non-consolidated financial statements of the parent company are also presented.

The separate and consolidated Annual financial statements of HBOR for 2011 that can be found enclosed have been audited by the audit 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

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 separate statements of HBOR as the parent company.

Operating result of the Group

In 2011 as the first entire year of its operations, the HBOR Group made a profit after taxation in the amount of HRK 147.1 million.

Pursuant to the HBOR Act, the parent company is exempted from profit tax; therefore, profit tax obligation arise exclusively from the activities of other members of the Group.

The consolidated total income in 2011 amounted to HRK 958.1 million, and total expenses amounted to HRK 811.0 million.

In the structure of income of the Group, the major portion, i.e. 94% relates to interest income as a result of the operations of the parent company.

The major portion of total expenses, i.e. 70% relates to interest expenses arising from the operations of the parent company.

The consolidated operating expenses in 2011 amounted to HRK 100.2 million, and consisted of general and administrative expenses and other operating expenses.

As at 31st December 2011, there were 281 employees in the Group, whereas at the end of 2010, there were 253 employees.

Assets and liabilities of the Group

The Group's assets on consolidated basis amount to HRK 22,012.9 million and are by 4% lower in comparison with the beginning of the year.

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.

Liabilities of the Group, in the major portion, i.e. 61% consist of borrowings and bonds payable of the parent company.

At the end of 2011, total equity and guarantee fund on consolidated basis amounted to HRK 7,340.9 million and accounted for 33% 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 2011, HBOR generated a total income of HRK 953.8 million, expenses of HRK 805.7 million and profits of HRK 148.1 million.

Net interest income

Net interest income amounted to HRK 332.3 million, an increase of 16% on the previous year. Such trend is the result of decrease in interest expenses on year level and generated interest income at almost the same level as the previous year.

Interest income amounted to HRK 896.2 million, an increase of 1% on the previous year. This slight increase has been completely anticipated and planned due to the fact that HBOR, as the development bank and facilitator of the measures for economic recovery of the Republic of Croatia, has not changed its interest rates on loans for several years.

By maintaining the level of its interest rates unchanged, HBOR gave up a portion of its profits for the purpose of giving support to Croatian economy in the time of crisis conditions.

Interest expenses amounted to HRK 563.9 million, a decrease of 7% on the previous year as a result of increased borrowings from special financial institutions with lower interest rates and redemption of bonds on their maturity.

Net fee income

Net fee income amounted to HRK 11.0 million, an increase of 24% in comparison with the previous year. The increase is the result of higher generated fee income for agent transactions for and on behalf of the Republic of Croatia.

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 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 44.4 million, whereas in 2010, they amounted to HRK 17.8 million.

At the year level, the Croatian kuna depreciated by 2% against the euro and by 4.5% 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. It amounted to HRK 94.7 million, which represents an increase of 10% compared to the same period last year.

There were 270 employees on 31st December 2011, and 244 on 31st December 2010.

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 amounted to HRK 145.9 million.

Significant changes in business activities

The balance sheet total as at 31st December 2011 amounted to HRK 21,992.9 million, decreasing by 4% compared to the beginning of the year.

The slight decrease in the balance sheet total is the result of redemption of bonds in the amount of EUR 300.0 million, i.e. HRK 2,223.9 million and interest of HRK 108.4 million on their maturity on 10th February 2011. This occurrence resulted in the decrease of available short-term placements that were provided for the mentioned regular redemption of issued Eurobonds and in the decrease of liabilities under issued securities.

Cash on hand and due from banks

At the end of 2011, cash on hand and due from banks amounted to HRK 302.0 million, representing 1% of total assets. The significant decrease in cash on hand and due from banks relates to the utilisation of funds of the club deal with domestic commercial banks from the transaction account for special purposes with the Croatian National Bank for the purpose of realisation of 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 2011, these funds amounted to HRK 153.5 million.

Loans

Total net loans at the end of 2011 stood at HRK 20,484.4 million, a decrease of 4% compared to the previous year. In the total assets, net loans accounted for 93%.

Total gross loans amounted to HRK 23,005.9 million.

The decrease in gross loans was the result of use of the available short-term placements for the redemption of bonds issued upon their maturity date.

Assets available for sale

Assets available for sale represent a portion of HBOR's liquidity reserves.

They consist primarily of debt and to a lesser extent of equity securities.

At the end of 2011, assets available for sale amounted to HRK 1,081.4 million. The significant increase compared to the beginning of the year is the result of investments of available assets into treasury notes and bonds of the Ministry of Finance as a part of instruments of liquidity reserves pursuant to the Liquidity Risk Management Procedures and pursuant to the covenants in the contracts with foreign creditors.

Total liabilities

Total liabilities as at 31st December 2011 amounted to HRK 14,668.7 million, which represents 67% of total liabilities.

The major portion of total liabilities consists of HBOR foreign borrowings and bonds payable in the total amount of HRK 13,342.1 million.

Liabilities under loans taken rose by 16% compared to the beginning of the year as a result of withdrawal of funds under arranged loans in the previous years.

On 16th February 2011, HBOR concluded Addendum II to the Club Loan Agreement for the purpose of the extension of measures for economic recovery and development through the Programme for Economic Recovery and Development – Model A+.

In 2011, HBOR also concluded a Loan Agreement with KfW for the puropose of water supply and wastewater facilities financing in the Republic of Croatia (Phase III) in the amount of EUR 18.0 million, under which no disbursements were made in 2011.

In the reporting period, i.e. on 10th February 2011 HBOR made a bullet redemption of the issued bonds in the amount of HRK 2,223.9 million together with interest of HRK 108.4 million. Bonds were issued on 11th February 2004 pursuant to the agreement between HBOR and Deutsche Bank AG London and UBS Limited (lead arrangers) under the EMTN programme with the guarantee of the Republic of Croatia in the amount of EUR 300.0 million, with the repayment period of 7 years and fixed interest rate of 4.875%.

As in previous years, in 2011 HBOR maintained to raise funds for the specified purposes from similar special financial institutions.

Equity

HBOR's total equity is comprised of the Founder's capital contributed from the budget of the Republic of Croatia, retained earnings from the profits generated in the previous years, other reserves, and profits for the current year and supplemental capital.

In the reporting period, contributions from the budget of the Republic of Croatia amounted to HRK 180.0 million. The total amount of capital contributed from the budget of the Republic of Croatia amounted to HRK 4,917.1 million. The outstanding amount of capital to be paid in from the budget of the Republic of Croatia, up to the amount of Founder's capital prescribed by the HBOR Act (HRK 7,000.0 million), is HRK 2,082.9 million.

The total profit of the Bank generated for the business year is allocated to reserves, pursuant to the HBOR Act.

CROATIAN BANK FOR RECONSTRUCTION AND DEVELOPMENT

Annual financial statements
for 2011

Contents

Responsibility for the Financial Statements

Pursuant to the Accounting Act of the Republic of Croatia, the Managing Board of the Bank and the Group are 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 and the Group 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, 29 March 2012

Deloitte.

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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 2011, 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 2011 and of its financial performance and its cash flows for the year then ended in accordance with the International Financial Reporting Standards.

Deloitte
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ZagrebTower
Radnička cesta 80
10 000 Zagreb
MB 0700851

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

Zagreb, 29 March 2012

Financial statements of the Group

Consolidated Income Statement

for the year ended 31 December 2011

(All amounts are expressed in HRK thousand)

	Notes	2011 HRK '000	2010 HRK '000
Interest income	3	897,723	892,290
Interest expense	4	(563,861)	(604,927)
Net interest income		**333,862**	**287,363**
Fee income	5	13,614	10,728
Fee expense	5	(1,236)	(1,679)
Net fee income		**12,378**	**9,049**
Net gains/(losses) on financial operations	6	44,422	17,767
Other income		2,270	1,352
		392,932	**315,531**
Operating expenses	7	(100,148)	(88,114)
Impairment loss and provisions	8	(145,946)	(110,356)
Profit before income tax		**146,838**	**117,061**
Income tax	9	252	181
Profit for the year		**147,090**	**117,242**
Attributable to:			
Equity holders of the parent		147,626	117,603
Non-controlling interests		(536)	(361)
		147,090	**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 2011

(All amounts are expressed in HRK thousand)

	2011 HRK '000	2010 HRK '000
Profit for the year	**147,090**	**117,242**
Other comprehensive income		
Increase in fair value of assets available for sale	19,924	7,434
Decrease in fair value of assets available for sale	(32,046)	(8,812)
Net foreign exchange on available for sale equity instruments	249	139
Transfer of realized gains on assets available for sale to income statement	(1,966)	-
Deferred tax – other comprehensive income	1	-
Other comprehensive income	**(13,838)**	**(1,239)**
Total comprehensive income after income tax	**133,252**	**116,003**
Attributable to:		
Equity holders of the parent	133,791	116,364
Non-controlling interests	(539)	(361)
	133,252	**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 2011

(All amounts are expressed in HRK thousand)

	Notes	2011 HRK '000	2010 HRK '000
Assets			
Cash on hand and due from banks	10	267,723	1,258,729
Deposits with other banks	11	67,377	137,555
Loans to banks	12	14,299,705	15,449,447
Loans to other customers	13	6,184,717	5,796,393
Financial assets at fair value through profit or loss	14	519	500
Assets available for sale	15	1,083,467	187,710
Assets held to maturity	16	1,092	1,077
Investments in associates	18	-	-
Property, plant and equipment and intangible assets	19	68,401	71,839
Non-current assets held for sale	20	34,432	34,361
Other assets	21	5,430	4,465
Total assets		**22,012,863**	**22,942,076**
Liabilities			
Deposits	22	154,243	222,658
Borrowings	23	8,197,363	7,047,415
Bonds payable	24	5,144,724	7,482,253
Other liabilities	25	1,175,611	1,162,318
Total liabilities		**14,671,941**	**15,914,644**
Equity			
Founder's capital	26	5,343,739	5,163,739
Retained earnings and reserves		1,836,565	1,718,962
Other reserves		(16,813)	(2,978)
Profit for the year		147,626	117,603
Total equity attributable to equity holders of the parent		**7,311,117**	**6,997,326**
Non-controlling interests		17,475	18,014
Total equity		**7,328,592**	**7,015,340**
Guarantee fund	27	12,330	12,092
Total equity and Guarantee fund		**7,340,922**	**7,027,432**
Total liabilities, total equity and Guarantee fund		**22,012,863**	**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 29 March 2012 by:

Anton Kovačev
President of the Managing Board

HRVATSKA BANKA ZA OBNOVU I RAZVITAK HBOR ZAGREB 1

Irena Adžić-Jagodić
Accounting Division Executive Director

Consolidated Statement of Cash Flows

for the year ended 31 December 2011

(All amounts are expressed in HRK thousand)

	2011 HRK '000	2010 HRK '000
Operating activities		
Profit before income tax	146,838	117,061
Adjustments to reconcile to net cash from and used in operating activities:		
Depreciation	6,515	5,312
Income tax	(253)	(181)
Impairment loss and provisions	145,946	110,356
Accrued interest	(129,077)	4,831
Deferred fees	10,680	3,178
Operating profit before working capital changes	*180,649*	*240,557*
Changes in operating assets and liabilities:		
Net decrease/(increase) in deposits with other banks, before provision for impairment	71,486	(11,024)
Net decrease/(increase) in loans to banks, before provision for impairment	1,101,044	(643,848)
Net (increase) in loans to other customers, before provision for impairment	(484,510)	(528,419)
Net gain/(losses) on financial assets at fair value through profit or loss	(26)	-
Net realised gain on assets available for sale	(1,966)	-
Decrease of discount in assets available for sale and bonds payable	9,347	19,875
Net (increase) in non-current assets held for sale	(1,390)	(1,502)
Net decrease/(increase) in other assets, before provision for impairment	306	(562)
Net (decrease)/increase in deposits from banks and companies	(68,415)	17,817
Net increase in other liabilities, before provisions	33,509	27,688
Net cash used in operating activities	**840,034**	**(879,418)**
Investment activities		
(Purchase) of financial assets at fair value through profit or loss	(1,600)	(500)
Sale of financial assets at fair value through profit or loss	1,630	-
Net (purchase) of assets available for sale	(1,442,570)	(370,775)
Sale of assets available for sale	557,966	409,018
(Purchase) of assets held to maturity	-	(1,041)
Net (purchase) of property, plant and equipment and intangible assets	(4,584)	(10,147)
Net cash (used in) / provided by investment activities	**(889,158)**	**26,555**
Financing activities		
Increase in founder's capital	180,000	220,000
Increase in borrowings – withdrawn funds	1,547,066	4,110,062
(Decrease) in borrowings – repayments of principal	(516,386)	(2,331,935)
(Decrease) in bonds payable – repayment of amortizing note	(2,373,992)	(148,394)
Payments by non-controlling interests	-	18,375
Net cash provided by financing activities	**(1,163,312)**	**1,868,108**
Effect of foreign currency to cash and cash equivalents		
Net foreign exchange	212,331	129,946
Net effect	**212,331**	**129,946**
Net (decrease)/increase in cash and cash equivalents	(1,000,105)	1,145,191
Balance as of 1 January, before provisions	1,270,526	125,335
Net (decrease)/increase in cash	(1,000,105)	1,145,191
Balance as of 31 December, before provisions	**270,421**	**1,270,526**
Additional note - Operational cash flows		
Interest paid	628,131	578,610
Interest received	634,449	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 2011

(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**
Profit for the year	**-**	**-**	**-**	147,626	(536)	**147,090**
Other comprehensive income	-	-	(13,835)	-	(3)	**(13,838)**
Total comprehensive income	-	-	(13,835)	147,626	(539)	**133,252**
Capital paid-in from the State Budget (Note 26)	180,000	-	-	-	-	**180,000**
Transfer of profit 2010 to retained earnings	-	117,603	-	(117,603)	-	**-**
Increase in non-controlling interests	-	-	-	-	-	**-**
Balance as of 31 December 2011	**5,343,739**	**1,836,565**	**(16,813)**	**147,626**	**17,475**	**7,328,592**

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 2011

(All amounts are expressed in HRK thousand)

	Notes	2011 HRK '000	2010 HRK '000
Interest income	3	896,174	891,714
Interest expense	4	(563,861)	(604,926)
Net interest income		**332,313**	**286,788**
Fee income	5	12,247	10,537
Fee expense	5	(1,236)	(1,679)
Net fee income		**11,011**	**8,858**
Net gains/(losses) on financial operations	6	44,351	17,755
Other income		1,007	922
		388,682	**314,323**
Operating expenses	7	(94,756)	(86,105)
Impairment loss and provisions	8	(145,866)	(110,256)
Profit before income tax		**148,060**	**117,962**
Income tax	2	-	-
Profit for the year		**148,060**	**117,962**
Attributable to:			
Equity holders of the parent		**148,060**	**117,962**

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 2011

(All amounts are expressed in HRK thousand)

	2011 HRK '000	2010 HRK '000
Profit for the year	**148,060**	**117,962**
Other comprehensive income		
Increase in fair value of assets available for sale	19,840	7,434
Decrease in fair value of assets available for sale	(31,956)	(8,813)
Net foreign exchange on available for sale equity instruments	249	139
Transfer of realized gains on assets available for sale to income statement	(1,966)	-
Other comprehensive income	**(13,833)**	**(1,240)**
Total comprehensive income after income tax	**134,227**	**116,722**
Attributable to:		
Equity holders of the parent	**134,227**	**116,722**

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 2011

(All amounts are expressed in HRK thousand)

	Notes	2011 HRK '000	2010 HRK '000
Assets			
Cash on hand and due from banks	10	267,219	1,258,012
Deposits with other banks	11	34,811	103,284
Loans to banks	12	14,299,705	15,449,447
Loans to other customers	13	6,184,717	5,796,393
Assets available for sale	15	1,081,385	186,659
Investments in subsidiaries	17	19,125	19,125
Investments in associates	18	-	-
Property, plant and equipment and intangible assets	19	68,106	71,418
Non-current assets held for sale	20	34,432	34,361
Other assets	21	3,424	3,598
Total assets		**21,992,924**	**22,922,297**
Liabilities			
Deposits	22	154,243	222,658
Borrowings	23	8,197,363	7,047,415
Bonds payable	24	5,144,724	7,482,253
Other liabilities	25	1,172,353	1,160,195
Total liabilities		**14,668,683**	**15,912,521**
Equity			
Founder's capital	26	5,343,739	5,163,739
Retained earnings and reserves		1,836,924	1,718,962
Other reserves		(16,812)	(2,979)
Profit for the year		148,060	117,962
Total equity		**7,311,911**	**6,997,684**
Guarantee fund	27	12,330	12,092
Total equity and Guarantee fund		**7,324,241**	**7,009,776**
Total liabilities, total equity and Guarantee fund		**21,992,924**	**22,922,297**

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 29 March 2012 by:

Anton Kovačev
President of the Managing Board

HRVATSKA BANKA ZA OBNOVU I RAZVITAK HBOR ZAGREB 1

Irena Adžić-Jagodić
Accounting Division Executive Director

Unconsolidated Statement of Cash Flows

for the year ended 31 December 2011

(All amounts are expressed in HRK thousand)

	2011 HRK '000	2010 HRK '000
Operating activities		
Profit before income tax	148,060	117,962
Adjustments to reconcile to net cash from and used in operating activities:		
Depreciation	6,359	5,264
Impairment loss and provisions	145,866	110,256
Accrued interest	(128,511)	5,235
Deferred fees	10,680	3,178
Operating profit before working capital changes	*182,454*	*241,895*
Changes in operating assets and liabilities:		
Net decrease/(increase) in deposits with other banks, before provision for impairment	69,235	22,866
Net decrease/(increase) in loans to banks, before provision for impairment	1,101,044	(643,847)
Net (increase) in loans to other customers, before provision for impairment	(484,510)	(528,420)
Net realised gain on assets available for sale	(1,966)	-
Decrease of discount in assets available for sale and bonds payable	9,347	19,876
Net (increase) in non-current assets held for sale	(1,390)	(1,502)
Net decrease/(increase) in other assets, before provision for impairment	1,048	(58)
Net (decrease)/increase in deposits from banks and companies	(68,415)	17,818
Net increase in other liabilities, before provisions	32,414	25,664
Net cash (used in) operating activities	**839,261**	**(845,708)**
Investment activities		
(Increase) in investments in subsidiaries	-	(19,125)
Net (purchase) of assets available for sale	(1,441,624)	(369,725)
Sale of assets available for sale	557,966	409,018
Net (purchase) of property, plant and equipment and intangible assets	(4,554)	(9,678)
Net cash provided by/(used in) investment activities	**(888,212)**	**10,490**
Financing activities		
Increase in founder's capital	180,000	220,000
Increase in borrowings – withdrawn funds	1,547,066	4,110,062
(Decrease) in borrowings – repayments of principal	(516,386)	(2,331,936)
(Decrease) in bonds payable – repayment of amortizing note	(2,373,992)	(148,394)
Net cash provided by financing activities	**(1,163,312)**	**1,849,732**
Effect of foreign currency to cash and cash equivalents		
Net foreign exchange	212,371	129,960
Net effect	**212,371**	**129,960**
Net (decrease)/increase in cash and cash equivalents	(999,892)	1,144,474
Balance as of 1 January, before provisions	1,269,809	125,335
Net (decrease)/increase in cash	(999,892)	1,144,474
Balance as of 31 December, before provisions	**269,917**	**1,269,809**
Additional note - Operational cash flows		
Interest paid	628,131	578,610
Interest received	633,458	676,728

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 2011

(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 2010	**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**
Profit for the year	-	-	-	148,060	**148,060**
Other comprehensive income	-	-	(13,833)	-	**(13,833)**
Total comprehensive income	-	-	(13,833)	148,060	**134,227**
Capital paid-in from the State Budget (Note 26)	180,000	-	-	-	**180,000**
Transfer of profit 2010 to retained earnings	-	117,962	-	(117,962)	**-**
Balance as of 31 December 2011	**5,343,739**	**1,836,924**	**(16,812)**	**148,060**	**7,311,911**

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 2011, the Group had 281 employees (31 December 2010: 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 2011, there were 270 employees at the Bank (31 December 2010: 244 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:

During 2011, the Supervisory Board members were as follows:

- Martina Dalić, MSc, Minister of Finance – ex officio President of the Supervisory Board,
- 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.

The mandate of members of the Croatian Parliament elected to the Supervisory Board ceased on 22 December 2011, by which their membership in the Supervisory Board also terminated. The term of office of the members of the Supervisory Board who were also the members of the Croatian Government ceased on 23 December 2011.

Pursuant to the Act on Croatian Bank for Reconstruction and Development, the Supervisory Board consists of five ministers of the Government of the Republic of Croatia. The minister in charge of finances and the minister in charge of the economy are obligatory members of the Supervisory Board, whereas other three ministers are appointed to the Supervisory Board by the Government of the Republic of Croatia among the ministers in charge of development, tourism, agriculture, environmental protection and construction. The Croatian Parliament appoints three members of the Supervisory Board and their permanent deputies among the members of the Croatian Parliament. The President of the Croatian Chamber of Economy is ex officio member of the Supervisory Board.

On 23 December 2011, the Croatian Parliament reached the Decision on expression of confidence to the Government of the Republic of Croatia, and on 19 January 2012, in accordance with the provision of the Act on HBOR, the Government of the Republic of Croatia reached the Decision on the appointment of the President, Vice-President and some of the members of the Supervisory Board of the Bank. The Croatian Parliament made the Decision on the appointment of members of the Supervisory Board of the Bank on 27 January 2012. Pursuant to the above decisions, the Supervisory Board of HBOR consists of:

- Slavko Linić, Minister of Finance – ex officio President of the Supervisory Board,
- Radimir Čačić, Principal Deputy Prime Minister of the Republic of Croatia and Minister for Economic Affairs – ex officio Vice President of the Supervisory Board,
- Gordan Maras, Minister for Entrepreneurship and Crafts,
- Veljko Ostojić, Minister of Tourism,
- Tihomir Jakovina, Minister of Agriculture,
- Nadan Vidošević, President of the Croatian Chamber of Economy, ex officio member of the Supervisory Board,
- Dragica Zgrebec, Member of the Croatian Parliament,

1. General information (continued)

1.3. Bodies of the Bank and the Group (continued):

- Srđan Gjurković, MSc, Member of the Croatian Parliament,
- Ivan Šuker, Member of the Croatian Parliament.

MANAGING BOARD

In 2011, 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:

Until 23 December 2011, the Audit Committee was comprised of the following members:

- 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, Member of the Audit Committee,
- Ante Artuković, Executive Director of HBOR’s Analysis Division, Member of the Audit Committee.

On 13 February 2012, the Supervisory Board appointed new members of the Audit Committee as follows:

- Slavko Linić, Minister of Finance, President of the Supervisory Board of HBOR, President of the Audit Committee,
- Srđan Gjurković, MSc, Member of the Croatian Parliament, 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.

The economic environment in 2012 is difficult to fully predict, but the financial crisis will probably further 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 2011 (see Note 31.2. Credit risk – Loan restructuring). Such circumstances may consequently influence the amount of the provisions for impairment losses in 2012, including the valuation of collateral. Also, it is expected that loan applications for financing working and permanent working capital will further increase in order to strengthen the liquidity of companies. But, in 2011, the number of approved loan funds for investments increased in the approximate volume as those for the working capital.

Due to the impact of the economic and financial crisis, in 2011 HBOR launched new loan programs for the purpose of improving the liquidity, maintaining and extending the existing operations of business entities. The main program under which the mentioned purposes were financed was the Loan Program for Economic Recovery and Development (Model A and A+). The Program was introduced as an incentive measure for economic revival and development with an active participation of the state in the financing of sustainable business projects of economic entities through the Bank. The funds were provided to borrowers by the commercial bank and HBOR in the proportion 60%:40%. For the needs of co-financing of its 40% share in the financing under the Loan Program for the Financing of Working Capital, HBOR provided HRK 2,000,000 thousand through a loan obtained from several domestic commercial banks. Loans in the total amount of HRK 1,952,470 thousand were committed out of this amount.

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.

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 2011 was HRK 7.530420 per 1 Euro and HRK 5.819940 per 1 United States dollar (31 December 2010: HRK 7.385173 per 1 Euro and HRK 5.568252 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.

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.

When the subsidiary company ceases to meet the criteria of this definition, and it has still not become an associated company, such investment will be recognized pursuant to the International Accounting Standard 39 – Financial Instruments: Recognition and Measurement from the date when the company ceases to be a subsidiary company. In such case, the carrying amount of investment shall be deemed an investment cost on initial measurement pursuant to IAS 39.

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.

Unrealized 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.

When the associated company ceases to meet the criteria of this definition, such investment shall be recognised pursuant to the International Accounting Standard 39 – Financial Instruments: Recognition and Measurement from the date when the company ceases to be an associated company. In such case, the carrying amount of investment shall be deemed an investment cost on initial measurement pursuant to IAS 39.

(All amounts are expressed in HRK thousand)

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 proportionally recognized as an adjustment to the effective yield on the loan over the term of 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 and are recognized in the Statement of comprehensive income upon collection.

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.

Fee and commission income of non-interest income character (loan management fees for and on behalf of other parties, payment transaction fees, other fees of non-interest type) are recognized in the Statement of comprehensive income on the principle of invoiced services.

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:

	2011	2010
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 health protection 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.

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.

The Group recognizes provisions for other liabilities towards employees when there is a contractual obligation or practice in the past based on which the obligation has arisen. Further, the Group recognizes the liabilities for accumulated vacation allowances based on unutilised vacation days as of the date of the financial statements.

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 2011	EUR 1 = HRK 7.530420	USD 1 = HRK 5.819940
31 December 2010	EUR 1 = HRK 7.385173	USD 1 = HRK 5.568252

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.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Taxation (continued)

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.

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 instruments, 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.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Financial instruments (continued)

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.

The Bank does not make acquisitions of financial instruments and investments to attain gain 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 which corresponds to the 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.

Financial assets classified as assets available for sale are provided for the purposes of maintaining liquidity reserves or for the purpose of placement of available funds until their further placement in long-term loans. In the available-for-sale assets portfolio, investments in long-term securities and in other financial instruments are recorded, as well as equity instruments with original maturity over 90 days that are held for an unlimited period and shares in investment funds (bond-based, equity instruments-based or combined) that the Bank intends to held for a period of over 30 days.

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 instruments 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.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Financial instruments (continued)

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

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.

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.

Impairment losses on investments in equity instrument recognized in the profit or loss are not reversed through profit or loss. If in the coming period the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to the event occurred after the recognition of impairment loss into profit or loss, impairment loss shall be reversed, with the amount of the reversal recognized profit or loss. All subsequent changes in the fair value of equity instruments classified into this category of financial assets are recognized in the equity.

The objective evidence on impairment loss on certain investment in an equity instrument includes information on significant adverse changes with impact on the technological, market, economic or legal conditions of operation of the issuer and indicates that the cost of investment in debt instruments cannot be recovered.

Significant or prolonged decline in the fair value of investments into debt instruments below their cost is also an objective evidence of impairment.

Interest earned whilst holding available for sale instruments 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 generally comprises instruments issued for a period exceeding one year, such as bonds, bills of exchange etc.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Financial instruments (continued)

c) Held-to-maturity financial assets (continued)

Financial assets held to maturity are initially recognised at fair value, increased by transaction costs. After initial recognition, assets held to maturity are measured and stated at amortized investment cost, i.e. acquisition cost (nominal value of purchased securities increased/decreased by a discount/premium and transaction costs) adjusted by amortized discount/premium.

If the issuer of securities indicates the method of revaluation, the carrying amount is stated pursuant to the conditions of issuer until its maturity.

Interest earned is recognized as interest receivable on the date of settlement and is not HBOR's income.

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 Group 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.

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 (see Note 31.2. Risk management – Credit risk).

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.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

Financial instruments (continued)

d) Loans to banks and other customers (continued)

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 2011, the Group's REPO deals amounted to HRK 2,712,136 thousand (2010: HRK 4,117,707 thousand) collateralized by securities in the amount of HRK 2,934,272 thousand (2010: HRK 4,393,074 thousand).

Property, plant and equipment and intangible assets

Property, plant and equipment and intangible assets are initially recognized and subsequently measured at acquisition 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:

	2011	2010
	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 presented 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.

The cases in which due to more difficult circumstances of sale because of objective circumstances and events beyond the Bank’s control, the sale will not be completed in the planned period, or the period necessary for the conclusion of sale should be prolonged even after the period of one year, and a decision of a authorised body on giving up the sale or the plan of sale has not been made, and the activities are further undertaken to find a buyer and there is enough evidence that the Bank has remained consistent with the plan of sale of such type of assets, do not exclude that the assets are still classified as non-current assets held-for-sale.

Bank's borrowings and bonds payable

Financial liabilities of the Bank and the Group arise from received loans and securities issued.

Financial liabilities are initially recognized at fair value, adjusted by transaction costs. After initial recognition, financial liabilities are measured at amortized cost determined using the effective interest rate method.

Financial liabilities are stated in the contracted currency translated to Kuna at the middle exchange rate of the Croatian National Bank, contract exchange rate or determined rate arising from business and financial transactions based on documentation.

The Group recognises interest expense related to borrowings and bonds payable in the Report on Comprehensive Income.

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, Ministry of the Economy, the Ministry of Regional Development and EU Funds, the Ministry of Agriculture, the Ministry for Maritime Affairs, Transport and Infrastructure, the Ministry for Entrepreneurship and Crafts 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.

2. Summary of significant accounting policies (continued)

2.1. Accounting policies (continued)

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.

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, Ministry for Entrepreneurship and Crafts, Ministry for Maritime Affairs, Transport and Infrastructure, Ministry of Agriculture, Ministry of Regional Development and EU Funds, 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. Summary of significant accounting policies (continued)

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. As a result of uncertainties which inherent in business activities, some items in the financial statements cannot be measured with precision but can only be estimated. The procedure of estimation includes the judgements based on latest reliable information available at the reporting date, so that actual amounts may differ from those estimated.

The changes in accounting estimates are adjustments of the carrying amount of some assets or liabilities or the pattern of consumption during useful life arising through the estimation of the current situation and expected future benefits and obligations associated with these assets and liabilities.

The use of reasonable estimations is essential part of the preparation of financial statements and does not undermine their reliability.

The changes in accounting estimates occur if there are changes in circumstances based on which the estimation was based as a result of new information or more experience. The changes in estimates do not relate to prior periods and is not the correction of an error.

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 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.

2. Summary of significant accounting policies (continued)

2.2. Significant accounting judgments and estimates (continued)

c) Loan impairment provisions (continued)

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.

Provisions for costs arising from initiated legal proceedings are reversed in the period in which legally valid sentence, arbitration award or settlement in the conciliation proceedings was made, pursuant to the procedures of monitoring legal cases against HBOR.

e) Provisions for retirement and jubilee benefits

In calculating provisions for retirement and jubilee benefits, the Group 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.

Provisions for regular retirement and jubilee benefits are calculated and determined by a licensed actuary.

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 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. The application of partial exemption contains same level of disclosures as in prior periods. The amended standard will not impact financial performance and financial statements.

2. Summary of significant accounting policies (continued)

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

- Amendments to IFRS 7 Financial Instruments: Disclosures – Transfer of financial assets (effective for periods beginning on or after 1 July 2011) amended the provisions of the existing standard to provide users of financial statements with information to enable them to evaluate risk exposures related to transfer of financial assets and the effect of those risks on the entity's financial position thus increasing the transparency of reporting on transfer transactions, particularly the transactions including the securitisation of financial assets. According to the amended provisions, disclosure is mandatory when the entity transfers all or a portion of financial assets only in case of transfer of contractual rights in order to receive cash flows from that financial assets or retains contractual rights to receive cash flows of that financial assets, but assumes a contractual obligation to pay the cash flows to one or more recipients. The amended standard does not affect the Group after initial application.

- IFRS 9 Financial Instruments: Classification and measurement (effective for periods beginning on or after 1 January 2015) is the first phase of International Accounting Standards Board (IASB) project to replace IAS 39, applicable for classification and measurement of financial assets as defined by IAS 39. In the following steps, IASB will define impairment, hedge accounting and de-recognition. Taking into account the comprehensiveness of the entire project to replace IAS 39, the envisaged phase and time duration, the Group will quantify the effects upon the completion of all project phases in order to project the full picture.

- IFRS 13 Fair Value Measurement (effective for periods beginning on or after 1 January 2013) provides a description of how an entity measures fair value when its application is required or permitted by the IFRSs. This Standard seeks to increase consistency and comparability in fair value measurements and related disclosures through a 'fair value hierarchy'. The hierarchy categorises the inputs used in valuation techniques into three levels. The hierarchy gives the highest priority to (unadjusted) quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. This Standard does not affect the financial statements of the Group after initial application since the Group presents categorisation of levels in accordance with the IFRS 7 Financial Instruments: Disclosures.

- Amended IAS 32 Financial Instruments: Presentation – Offsetting of Financial Assets and Liabilities (effective for periods beginning on or after 1 January 2014) which amends the provisions of the existing Standard with an objective of clarifying inconsistencies in the current practice when applying the offsetting criteria. The amendments clarify the meaning of the expression "currently has a legally enforceable right of set-off"" and the provision that some gross settlement systems may be considered equivalent to net settlement. This Standard will not affect the Group after initial application.

- Amended IFRS 7 Financial Instruments: Disclosures – Offsetting of financial assets and liabilities (effective for periods beginning on or after 1 January 2014) which amends the provisions of IAS 32 Financial Instruments: Presentation – Offsetting of Financial Assets and Liabilities by the required related disclosures. This Standard will not affect the Group after initial application.

2. Summary of significant accounting policies (continued)

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

In 2011, the International Accounting Standards Board (IASB) issued, owing to the financial crisis, three new standards and amended two existing ones: the standards regulating the preparation of consolidated and separate financial statements, the reporting on joint arrangements and the required disclosures of interests in other entities:

- IFRS 10 Consolidated Financial Statements (effective for periods beginning on or after 1 January 2013) which establishes principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entities. As of the date of preparing these statements, this standard does not affect the financial statements of the Group after initial implementation. For any new investment in ownership interest of less than 50%, the Group will, in the period up to the beginning of application and afterwards, carefully consider the substance of the influence, power and significant activities in order to determine the need for consolidation.
- The amended IAS 27 Separate Financial Statements (effective for periods beginning on or after 1 January 2013) applies in cases where the entity does not prepare consolidated financial statements but separate financial statements in accordance with the IFRSs. As of the date of preparing the statement, this standard will not affect the Group's financial statements after initial application regarding the requirements relating to the preparation of both separate financial statements of the parent company - the Bank and consolidated financial statements – the Group.
- IFRS 11 Joint Arrangements (effective for periods beginning on or after 1 January 2013) with the core principle that a party to a joint arrangement determines the type of joint arrangement in which it is involved by assessing its rights and obligations and accounts for those rights and obligations in accordance with that type of joint arrangement. As of the date of preparing these financial statements, this standard will not affect the Group's financial statements after initial implementation.
- The amended IAS 28 Investments in Associates and Joint Ventures (effective for periods beginning on or after 1 January 2013) prescribes the accounting for investments in associates and sets out the requirements for the application of the equity method when accounting for investments in associates and joint investment. The basic principle under the equity method, on initial recognition of investment in an associate or a joint venture is recognised at cost, and the carrying amount is increased or decreased to recognise the investor’s share in the profit or loss on the investee after the acquisition date. As of the date of preparing these financial statements, this standard will not affect the Group's financial statements after initial application since the investments in associates are accounted for under the equity method.
- IFRS 12 Disclosure of Interest in Other Entities (effective for periods beginning on or after 1 January 2013) accompanied IFRSs 10 and 11 and the amended IAS 28 regarding the fact that their provisions do not set out disclosures in financial statements. This standard introduced required disclosures to enable users of financial statements to evaluate the nature of and risks associated with entity’s interests in other entities and the impact of these on the financial position, financial performance and cash flows. As of the date of preparing these financial statements, this standard will not affect the Group's financial statements for the reporting year. Upon the beginning of the application of this standard, the Bank and the Group will, if necessary, include the required disclosures in financial statements according to the type of investment.

3. Interest income

Interest income by borrowers:

	Group 2011 HRK '000	Group 2010 HRK '000	Bank 2011 HRK '000	Bank 2010 HRK '000
Public sector	59,376	32,471	59,287	32,458
State-owned companies	42,096	63,739	42,096	63,739
Foreign companies	8,855	8,336	8,855	8,336
Domestic companies	331,176	301,906	331,176	301,906
Domestic banks	383,596	403,597	382,136	403,034
Foreign banks	1,350	1,714	1,350	1,714
Other	59,302	62,581	59,302	62,581
Penalty interest	11,972	17,946	11,972	17,946
	897,723	**892,290**	**896,174**	**891,714**

Interest income by type of facility:

	Group 2011 HRK '000	Group 2010 HRK '000	Bank 2011 HRK '000	Bank 2010 HRK '000
Interest on loans				
- banks	383,349	402,867	383,349	402,867
- other customers	483,367	463,569	483,367	463,569
	866,716	866,436	866,716	866,436
Investments in securities	27,205	13,737	27,116	13,161
Deposits	3,134	1,970	1,677	1,970
Due from domestic banks	668	10,147	665	10,147
	897,723	**892,290**	**896,174**	**891,714**

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 2011 amounts to HRK 206,665 thousand (2010: HRK 200,567 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.

4. Interest expense

Interest expense by type of payee:

	Group		Bank	
	2011	2010	2011	2010
	HRK '000	HRK '000	HRK '000	HRK '000
Domestic banks	40,777	22,588	40,777	22,587
Foreign banks	523,083	582,339	523,083	582,339
Other	1	-	1	-
	563,861	**604,927**	**563,861**	**604,926**

Interest expense by type of facility:

	Group		Bank	
	2011	2010	2011	2010
	HRK '000	HRK '000	HRK '000	HRK '000
Borrowings	230,470	174,030	230,470	174,030
Debt securities	333,390	430,896	333,390	430,896
Deposits	1	1	1	-
	563,861	**604,927**	**563,861**	**604,926**

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		Bank	
	2011	2010	2011	2010
	HRK '000	HRK '000	HRK '000	HRK '000
Fee income:				
From issued guarantees	3,467	3,846	3,467	3,846
From managed funds for and on behalf of third parties	8,354	6,070	8,354	6,070
From payment operations	189	328	189	328
Other	232	292	237	293
Reinsurance commission income	1,372	192	-	-
	13,614	**10,728**	**12,247**	**10,537**
Fee expense	(1,236)	(1,679)	(1,236)	(1,679)
Net fee income	**12,378**	**9,049**	**11,011**	**8,858**

6. Net gains/(losses) on financial operations

	Group 2011 HRK '000	Group 2010 HRK '000	Bank 2011 HRK '000	Bank 2010 HRK '000
Net foreign exchange gains/(losses) on foreign currency assets:				
Cash on hand, accounts at banks and due from banks	6,710	7,197	6,710	7,197
Loans given to banks and other customers	250,005	141,585	250,005	141,585
Assets held to maturity	21	14	-	-
Assets available for sale	4,950	1,412	4,926	1,412
Other	(146)	450	(153)	450
	261,540	150,658	261,488	150,644
Net foreign exchange gains/(losses) on foreign currency liabilities:				
Deposits	(889)	(3,663)	(889)	(3,663)
Borrowings and issued long-term securities	(219,981)	(132,334)	(219,980)	(132,334)
Other	(398)	(229)	(392)	(226)
	(221,268)	(136,226)	(221,261)	(136,223)
Net foreign exchange gains/(losses) on foreign currency assets and liabilities	40,272	14,432	40,227	14,421
Gains on assets at fair value through profit or loss and realized gain on assets available for sale	4,150	3,335	4,124	3,334
Net gains/(losses) on financial operations	**44,422**	**17,767**	**44,351**	**17,755**

7. Operating expenses

Operating expenses can be shown as follows:

	Group		Bank	
	2011 HRK '000	2010 HRK '000	2011 HRK '000	2010 HRK '000
General and administrative expenses:				
Employee expenses	59,133	48,983	56,644	48,088
Depreciation	6,515	5,312	6,359	5,264
Administration expenses	9,179	7,344	9,020	7,198
Material and services	19,830	21,385	18,440	20,783
	94,657	83,024	90,463	81,333
Other expenses:				
Taxes and contributions	281	281	277	277
Other expenses	5,210	4,809	4,016	4,495
	5,491	5,090	4,293	4,772
	100,148	**88,114**	**94,756**	**86,105**

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

	Group		Bank	
	2011 HRK '000	2010 HRK '000	2011 HRK '000	2010 HRK '000
Changes in claims provisions	3,224	440	-	-
Changes in claims provisions, share of reinsurance	(2,330)	(314)	-	-
Expenses of insurance operations	**894**	**126**	**-**	**-**

8. Impairment loss and provisions

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

		Group		Bank
	2011	2010	2011	2010
	HRK '000	HRK '000	HRK '000	HRK '000
Impairment losses on cash on hand and due from banks	(9,882)	11,445	(9,882)	11,445
Impairment losses on deposits with other banks	(691)	(408)	(691)	(408)
Impairment losses on loans to banks	63,297	55,489	63,297	55,489
Impairment losses on loans to other customers and interest	109,042	63,262	109,042	63,262
Impairment losses on non-current assets held for sale	1,319	3	1,319	3
Impairment losses on assets available for sale	1,367	15,344	1,367	15,344
Impairment losses on property, plant and equipment and intangible assets	1,507	-	1,507	-
Impairment losses on other assets	(832)	896	(874)	896
Total increase in provision for impairment losses on assets	165,127	146,031	165,085	146,031
Provision for guarantees and commitments	(25,019)	(56,548)	(25,057)	(56,548)
Other provisions	5,838	20,873	5,838	20,773
Total (decrease) in provision for guarantees and commitments and other provisions	(19,181)	(35,675)	(19,219)	(35,775)
Total increase of provisions	**145,946**	**110,356**	**145,866**	**110,256**

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.

		Group
	2011	**2010**
	HRK '000	**HRK '000**
Recognised in the income statement		
Deferred tax income	252	181
Income tax	**252**	**181**
Income tax reconciliation		
Profit/(loss) before tax	**(1,347)**	**(912)**
Income tax at 20% rate	270	182
Non-deductible expense	(18)	(1)
Income tax recognised in the income statement	**252**	**181**
Recognised in the Statement of Comprehensive Income		
Deferred tax income/(expenditure)	1	-
Income tax recognised in the Statement of Comprehensive Income	**1**	**-**
Recognised deferred tax assets	**253**	**181**

The Managing Board estimates that the total amount of recognised deferred tax assets can be utilised by using tax losses in the period of 5 years from the reporting period it was originated in.

10. Cash on hand and due from banks

	Group		Bank	
	2011	**2010**	**2011**	**2010**
	HRK 000	**HRK 000**	**HRK 000**	**HRK 000**
Account with the Croatian National Bank	153,613	1,157,164	153,613	1,157,164
Due from domestic banks in foreign currency	75	47	75	47
Due from foreign banks in foreign currency	116,229	112,598	116,229	112,598
Due from domestic banks in HRK	504	717	-	-
Accrued interest	-	783	-	783
	270,421	1,271,309	269,917	1,270,592
Provisions for impairment losses	(2,698)	(12,580)	(2,698)	(12,580)
	267,723	**1,258,729**	**267,219**	**1,258,012**

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 2011 amounts to HRK 153,480 thousand (31 December 2010: 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 154,000 thousand (2010: EUR 14,834 thousand).

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

	Group		Bank	
	2011	**2010**	**2011**	**2010**
	HRK 000	**HRK 000**	**HRK 000**	**HRK 000**
Balance as at 1 January	12,580	1,135	12,580	1,135
Increase of provision for impairment losses on amounts due from banks	-	11,445	-	11,445
Release of provision for impairment losses on amounts due from banks	(9,882)	-	(9,882)	-
Balance as at 31 December	**2,698**	**12,580**	**2,698**	**12,580**

Reconciliation with the Statement of cash flows:

	Group		Bank	
	2011	**2010**	**2011**	**2010**
	HRK 000	**HRK 000**	**HRK 000**	**HRK 000**
Total cash on hands and due from banks, before provisions	270,421	1,271,309	269,917	1,270,592
Accrued interest	-	(783)	-	(783)
Balance of cash on hands and due from banks reconciled with statement of cash flows	**270,421**	**1,270,526**	**269,917**	**1,269,809**

11. Deposits with other banks

	Group 2011 HRK '000	Group 2010 HRK '000	Bank 2011 HRK '000	Bank 2010 HRK '000
Deposits with foreign banks	15,132	84,367	15,132	84,367
Deposits with domestic banks	51,640	53,890	20,000	20,000
Accrued interest	997	381	71	-
	67,769	138,638	35,203	104,367
Provision for impairment losses	(392)	(1,083)	(392)	(1,083)
	67,377	**137,555**	**34,811**	**103,284**

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

	Group 2011 HRK '000	Group 2010 HRK '000	Bank 2011 HRK '000	Bank 2010 HRK '000
Balance as of 1 January	1,083	1,491	1,083	1,491
Increase of provision for impairment losses on deposits with other banks	-	-	-	-
Release of provision for impairment losses on deposits with other banks	(691)	(408)	(691)	(408)
Balance as of 31 December	**392**	**1,083**	**392**	**1,083**

12. Loans to banks

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

		Group		Bank
	2011	2010	2011	2010
	HRK '000	HRK '000	HRK '000	HRK '000
Loans due within one year	6,543,904	8,131,534	6,543,904	8,131,534
Loans due in over one year	8,561,056	8,058,064	8,561,056	8,058,064
Accrued interest	52,162	27,446	52,162	27,446
Deferred recognition of loan origination fees	(59,014)	(48,897)	(59,014)	(48,897)
	15,098,108	16,168,147	15,098,108	16,168,147
Provision for impairment losses	(798,403)	(718,700)	(798,403)	(718,700)
	14,299,705	**15,449,447**	**14,299,705**	**15,449,447**

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

		Group		Bank
	2011	2010	2011	2010
	HRK '000	HRK '000	HRK '000	HRK '000
Balance as of 1 January	718,700	658,447	718,700	658,447
Increase of provision for impairment losses on loans to banks	309,509	381,341	309,509	381,341
Release of provision for impairment losses on loans to banks	(246,212)	(325,852)	(246,212)	(325,852)
Net foreign exchange gains/(losses) on provision for impairment losses	8,538	4,764	8,538	4,764
Provisions transferred from loans to other customers	7,868	-	7,868	-
Balance as of 31 December	**798,403**	**718,700**	**798,403**	**718,700**

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		Bank
	2011 HRK 000	**2010 HRK 000**	**2011 HRK 000**	**2010 HRK 000**
Loan programme for reconstruction and development of the economy	4,223,091	4,229,206	4,223,091	4,229,206
Export financing	4,323,563	4,399,662	4,323,563	4,399,662
Loan programme for reconstruction and development of infrastructure in the Republic of Croatia	685,984	424,146	685,984	424,146
Loan programme for small and medium-sized enterprises	3,112,384	2,571,601	3,112,384	2,571,601
Loan programme for war-torn and demolished housing and business facilities	18,552	19,576	18,552	19,576
Other	2,741,386	4,545,407	2,741,386	4,545,407
Accrued interest	52,162	27,446	52,162	27,446
Deferred recognition of loan fees	(59,014)	(48,897)	(59,014)	(48,897)
	15,098,108	16,168,147	15,098,108	16,168,147
Provisions for impairment losses	(798,403)	(718,700)	(798,403)	(718,700)
	14,299,705	**15,449,447**	**14,299,705**	**15,449,447**

Average interest rates for total loans to banks are stated at 1.71% (2010: 1.84%) and for loans under HBOR loan programmes excluding the liquidity reserve at 1.59% (2010: 1.76%).

Average interest rates reflect the ratio of interest income generated from the mentioned placements and average assets.

Item “Other” refers to reverse REPO agreements in the total amount of HRK 2,712,136 thousand (2010: HRK 4,117,707 thousand). The above placements are collateralized by securities in the amount of HRK 2,934,272 thousand (2010: HRK 4,393,074 thousand).

13. Loans to other customers

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

		Group		Bank
	2011	**2010**	**2011**	**2010**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**
Domestic companies	5,533,789	4,822,390	5,533,789	4,822,390
State-owned companies	861,543	1,273,088	861,543	1,273,088
Public sector	595,063	415,254	595,063	415,254
Foreign companies	191,819	217,404	191,819	217,404
Non-profit institutions	14,961	13,217	14,961	13,217
Other	736,197	696,708	736,197	696,708
Accrued interest	36,607	22,151	36,607	22,151
Deferred recognition of loan origination fees	(62,217)	(60,617)	(62,217)	(60,617)
	7,907,762	7,399,595	7,907,762	7,399,595
Provision for impairment losses	(1,723,045)	(1,603,202)	(1,723,045)	(1,603,202)
	6,184,717	**5,796,393**	**6,184,717**	**5,796,393**

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

		Group		Bank
	2011	**2010**	**2011**	**2010**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**
Balance as of 1 January	1,603,202	1,527,769	1,603,202	1,527,769
Increase of provision for impairment losses on loans to other customers and interest	230,204	203,596	230,204	203,596
Release of provision for impairment losses on loans to other customers and interest	(119,222)	(139,942)	(119,222)	(139,942)
Net foreign exchange gains/(losses) on provision for impairment losses	22,092	11,903	22,092	11,903
Collection of off-balance sheet receivables	(1,940)	(392)	(1,940)	(392)
Provisions transferred from off-balance sheet	2,299	392	2,299	392
Write-offs	(5,722)	(124)	(5,722)	(124)
Provisions transferred to loans to banks	(7,868)	-	(7,868)	-
Balance as of 31 December	**1,723,045**	**1,603,202**	**1,723,045**	**1,603,202**

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 2011 HRK '000	Group 2010 HRK '000	Bank 2011 HRK '000	Bank 2010 HRK '000
Loan programme for reconstruction and development of the economy	3,323,278	2,724,118	3,323,278	2,724,118
Export financing	1,452,075	1,479,260	1,452,075	1,479,260
Loan programme for reconstruction and development of infrastructure in the Republic of Croatia	1,601,400	1,793,624	1,601,400	1,793,624
Loan programme for small and medium-sized enterprises	1,395,988	1,266,743	1,395,988	1,266,743
Other	160,631	174,316	160,631	174,316
Accrued interest	36,607	22,151	36,607	22,151
Deferred recognition of loan origination fees	(62,217)	(60,617)	(62,217)	(60,617)
	7,907,762	7,399,595	7,907,762	7,399,595
Provision for impairment losses	(1,723,045)	(1,603,202)	(1,723,045)	(1,603,202)
	6,184,717	**5,796,393**	**6,184,717**	**5,796,393**

Average interest rates on loans to other customers are stated at 2.15% (2010: 2.12%).

Average interest rates reflect the ratio of interest income from generated the mentioned placements and average assets.

14. Financial assets at fair value through profit or loss

	Group		Bank	
	2011 HRK '000	2010 HRK '000	2011 HRK '000	2010 HRK '000
Shares in investment funds recognised at fair value through profit or loss	519	500	-	-
Balance as at 31 December	**519**	**500**	**-**	**-**

15. Assets available for sale

	Group		Bank	
	2011 HRK '000	2010 HRK '000	2011 HRK '000	2010 HRK '000
Debt instruments:				
Listed debt instruments:				
Bonds of the Ministry of Finance of the Republic of Croatia	332,546	131,618	331,563	131,618
Treasury bills of the Ministry of Finance of the Republic of Croatia	728,748	39,966	728,748	39,966
Accrued interest	8,188	1,970	8,167	1,970
	1,069,482	**173,554**	**1,068,478**	**173,554**
Equity instruments:				
Unlisted equity instruments:				
Investments in shares of foreign legal entities	25	23	25	23
Investments in financial institutions shares	161	161	161	161
Shares of foreign financial institutions – EIF (Note 28)	12,721	12,921	12,721	12,921
Investments in company's shares	30,397	29,030	30,397	29,030
Provision for impairment losses	(30,397)	(29,030)	(30,397)	(29,030)
	12,907	**13,105**	**12,907**	**13,105**
Investments in investment funds:				
Shares classified as assets available for sale	1,078	1,051	-	-
	1,078	**1,051**	**-**	**-**
Balance as at 31 December	**1,083,467**	**187,710**	**1,081,385**	**186,659**

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		Bank	
	2011	**2010**	**2011**	**2010**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**
Balance as at 1 January	29,030	13,686	29,030	13,686
Increase of provisions for impairment losses on assets available for sale	5,865	19,049	5,865	19,049
Reversal of provisions for impairment losses on assets available for sale	(4,498)	(3,705)	(4,498)	(3,705)
Balance as at 31 December	**30,397**	**29,030**	**30,397**	**29,030**

The text to follow contains investment breakdown:

	Date of issue	Date of maturity	Interest rate (%)	Group 2011 HRK '000	Group 2010 HRK '000	Bank 2011 HRK '000	Bank 2010 HRK '000
Debt instruments:							
Listed debt instruments: Bonds of the Republic of Croatia indexed to foreign currency:							
RHMF-O-125A	23.01.2003.	23.05.2012.	6.875	45,700	46,083	45,700	46,083
RHMF-O-142A	10.02.2004.	10.02.2014.	5.5	75,630	75,993	75,630	75,993
RHMF-O-19BA	29.11.2004.	29.11.2019.	5.375	9,860	9,542	9,860	9,542
RHMF-O-227E	22.07.2011.	22.07.2022.	6.5	132,453	-	132,453	-
RHMF-O-157A	14.07.2005.	14.07.2015.	4.25	983	-	-	-
Bonds of the Republic of Croatia in foreign currency:							
XS0645940288	08.07.2011.	09.07.2018.	5.875	47,466	-	47,466	-
Bonds of the Republic of Croatia in HRK:							
RHMF-O-167A	22.07.2011.	22.07.2016.	5.75	20,454	-	20,454	-
Treasury bills in HRK up to 91 days			1.95 - 2	-	39,966	-	39,966
Treasury bills in HRK up to 182 days			3.6 –5.25	216,604	-	216,604	-
Treasury bills in HRK up to 364 days			2.7 – 4.5	512,144	-	512,144	-
Accrued interest				8,188	1,970	8,167	1,970
				1,069,482	**173,554**	**1,068,478**	**173,554**
Equity instruments:							
Unlisted equity instruments: Investments in shares of foreign legal entities in foreign currency				25	23	25	23
Investments in financial institutions' shares				161	161	161	161
Investments in shares of foreign financial institutions in foreign currency				12,721	12,921	12,721	12,921
Investments in companies' shares				30,397	29,030	30,397	29,030
Provisions for impairment losses				(30,397)	(29,030)	(30,397)	(29,030)
				12,907	**13,105**	**12,907**	**13,105**
Investments in investments funds in the Republic of Croatia				**1,078**	**1,051**	**-**	**-**
Total				**1,083,467**	**187,710**	**1,081,385**	**186,659**

15. Assets available for sale (continued)

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 2011, the value of these outstanding bonds amounted to HRK 45,700 thousand (31 December 2010: HRK 46,083 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 2011, the value of these outstanding bonds amounted to HRK 75,630 thousand (31 December 2010: HRK 75,993 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 2011, the value of these outstanding bonds amounted to HRK 9,860 thousand (31 December 2010: HRK 9,542 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-227E) issued with foreign currency clause on 22 July 2011 are repayable over 11 years with an interest rate of 6.5%. As of 31 December 2011, the value of these outstanding bonds amounted to HRK 132,453 thousand (31 December 2010: HRK 0 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-157A) issued with foreign currency clause on 14 July 2005 are repayable over 10 years with an interest rate of 4.25%. As of 31 December 2011, the value of these outstanding bonds amounted to HRK 983 thousand (31 December 2010: HRK 0 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (XS0645940288) issued in foreign currency on 08 July 2011 are repayable over 7 years with an interest rate of 5.875%. As of 31 December 2011, the value of these outstanding bonds amounted to HRK 47,466 thousand (31 December 2010: HRK 0 thousand).

Bonds of the Ministry of Finance of the Republic of Croatia (RHMF-O-167A) issued in kuna on 22 July 2011 are repayable over 5 years with an interest rate of 5.75%. As of 31 December 2011, the value of these outstanding bonds amounted to HRK 20,454 thousand (31 December 2010: HRK 0 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 equity share in the company Vinka d.d., Vinkovci amounting to HRK 16,725 thousand, representing a 5.1823% of the equity share belonging to HBOR in the company's equity.

HBOR effected a 100% impairment of value for the complete amount of the equity share since it was estimated uncollectable.

15. Assets available for sale (continued)

In 2011, however, owing to an increase in capitalisation, the percentage of HBOR's share in the company's equity was changed to 0.9365%. 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.

In 2011, owing to an increase in capitalisation, the percentage of HBOR's share in the company's equity was changed to 8.1321%. The shares of the company (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 2011 amounted to HRK 10.00 (31 December 2010: HRK 9.00 per share).

Pursuant to the decision of the subsidiary's management dated 08 June 2011, shares in investment funds were classified as assets available for sale.

16. Assets held to maturity

	Group 2011 HRK '000	Group 2010 HRK '000	Bank 2011 HRK '000	Bank 2010 HRK '000
Debt instruments:				
Listed debt instruments:				
Bonds of the Ministry of finance of the Republic of Croatia	1,069	1,055	-	-
Accrued interest	23	22	-	-
Balance as at 31 December	**1,092**	**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 2011, the value of these outstanding bonds amounted to HRK 1,069 thousand (31 December 2010: HRK 1,055 thousand).

17. Investments in subsidiaries

As at 31 December 2011, the Bank's subsidiaries are as follows:

Consolidated company	Activity	Ownership 2011	Ownership 2010	Investment 2011	Investment 2010
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%	51%	19,125	19,125
TOTAL				**19,125**	**19,125**

18. Investments in associates

	Group 2011 HRK '000	Group 2010 HRK '000	Bank 2011 HRK '000	Bank 2010 HRK '000
Investments in associates	23,687	23,687	23,687	23,687
Value adjustments	(23,687)	(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 2011	% ownership in 2010
Bila boja d.o.o., Grohote	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, in bankruptcy	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 non-recoverability of the investment

19. Property, plant and equipment and intangible assets

Group 2011	Buildings	Computers	Furniture, equipment and vehicles	Property, plant and equipment and intangible assets not ready for use	Total property, plant and equipment	Intangible assets	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Cost							
At 31 December 2010	**76,178**	**12,071**	**12,600**	**2,905**	**103,754**	**15,985**	**119,739**
Additions	-	-	-	4,595	4,595	-	4,595
Transfer from assets not yet ready for use	924	1,674	1,387	(4,595)	(610)	610	-
Disposals and write-offs	-	(78)	(1,446)	(1,507)	(3,031)	(40)	(3,071)
At 31 December 2011	**77,102**	**13,667**	**12,541**	**1,398**	**104,708**	**16,555**	**121,263**
Accumulated depreciation							
At 31 December 2010	**14,155**	**9,945**	**10,667**	**-**	**34,767**	**13,133**	**47,900**
Depreciation for 2011	2,310	1,664	810	-	4,784	1,731	6,515
Impairment	-	-	-	1,507	1,507	-	1,507
Disposals and write-offs	-	(78)	(1,435)	(1,507)	(3,020)	(40)	(3,060)
At 31 December 2011	**16,465**	**11,531**	**10,042**	**-**	**38,038**	**14,824**	**52,862**
Net book value at 31 December 2011	**60,637**	**2,136**	**2,499**	**1,398**	**66,670**	**1,731**	**68,401**
Net book value at 31 December 2010	**62,023**	**2,126**	**1,933**	**2,905**	**68,987**	**2,852**	**71,839**

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

Group 2010	Buildings	Computers	Furniture, equipment and vehicles	Property, plant and equipment and intangible assets not ready for use	Total property, plant and equipment	Intangible assets	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	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 **2011**	**Buildings**	**Computers**	**Furniture, equipment and vehicles**	**Property, plant and equipment and intangible assets not ready for use**	**Total property, plant and equipment**	**Intangible assets**	**Total**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**
Cost							
At 31 December 2010	**76,178**	**12,071**	**12,484**	**2,905**	**103,638**	**15,576**	**119,214**
Additions	-	-	-	4,565	4,565	-	4,565
Transfer from assets not ready for use	924	1,659	1,387	(4,565)	(595)	595	-
Disposals and write-offs	-	(78)	(1,446)	(1,507)	(3,031)	(40)	(3,071)
At 31 December 2011	**77,102**	**13,652**	**12,425**	**1,398**	**104,577**	**16,131**	**120,708**
Accumulated depreciation							
At 31 December 2010	**14,155**	**9,945**	**10,609**	**-**	**34,709**	**13,087**	**47,796**
Depreciation for 2011	2,310	1,657	798	-	4,765	1,594	6,359
Impairment	-	-	-	1,507	1,507	-	1,507
Disposals and write-offs	-	(78)	(1,435)	(1,507)	(3,020)	(40)	(3,060)
At 31 December 2011	**16,465**	**11,524**	**9,972**	**-**	**37,961**	**14,641**	**52,602**
Net book value at 31 December 2011	**60,637**	**2,128**	**2,453**	**1,398**	**66,616**	**1,490**	**68,106**
Net book value at 31 December 2010	**62,023**	**2,126**	**1,875**	**2,905**	**68,929**	**2,489**	**71,418**

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

Bank **2010**	**Buildings**	**Computers**	**Furniture, equipment and vehicles**	**Property, plant and equipment and intangible assets not ready for use**	**Total property, plant and equipment**	**Intangible assets**	**Total**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**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**

20. Non-current assets held for sale

	Group 2011 HRK '000	Group 2010 HRK '000	Bank 2011 HRK '000	Bank 2010 HRK '000
Non-current assets held for sale	34,432	34,361	34,432	34,361
	34,432	**34,361**	**34,432**	**34,361**

In 2011, HBOR took over non-current assets held for sale of HRK 1,195 thousand (2010: HRK 2,465 thousand) comprised of: land HRK 0 thousand (2010: HRK 196 thousand) and buildings of HRK 1,195 thousand (2010: HRK 2,269 thousand). Fair value of taken over non–current assets held for sale amounts to HRK 2,379 thousand (2010: HRK 2,530 thousand), of which: land HRK 0 thousand (2010: HRK 193 thousand) and buildings HRK 2,379 thousand (2010: HRK 2,337 thousand).

In 2011, HBOR sold non-current assets held for sale of HRK 804 thousand (2010: HRK 964 thousand) comprised of: land of HRK 444 thousand (2010: HRK 182 thousand), buildings of HRK 47 thousand (2010: HRK 557 thousand) and apartments of HRK 313 thousand (2010: HRK 225 thousand).

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

	Group 2011 HRK '000	Group 2010 HRK '000	Bank 2011 HRK '000	Bank 2010 HRK '000
Balance as of 1 January	6,499	6,739	6,499	6,739
Increase of provisions for impairment losses on non-current assets held for sale	1,319	3	1,319	3
Derecognition of impairment due to the sale of non-current assets held for sale	(84)	(243)	(84)	(243)
Transfer from loans	1,741	-	1,741	
Balance as of 31 December	**9,475**	**6,499**	**9,475**	**6,499**

21. Other assets

	Group 2011 HRK 000	Group 2010 HRK 000	Bank 2011 HRK 000	Bank 2010 HRK 000
Fees receivable	1,490	2,560	1,490	2,560
Premium receivables	1,681	459	-	-
Receivables for reinsurance commissions	235	172	-	-
Receivables for risk assessment fees	183	76	-	-
Deferred tax assets	439	181	-	-
Other assets	5,542	5,513	5,534	5,534
	9,570	**8,961**	**7,024**	**8,094**
Provision for impairment losses	(4,140)	(4,496)	(3,600)	(4,496)
	5,430	**4,465**	**3,424**	**3,598**

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

	Group 2011 HRK 000	Group 2010 HRK 000	Bank 2011 HRK 000	Bank 2010 HRK 000
Balance as at 1 January	4,496	3,619	4,496	3,619
Increase of provision for impairment losses on other assets	1,272	2,434	726	2,434
Release of provision for impairment losses on other assets	(1,601)	(1,528)	(1,595)	(1,528)
Collection of off-balance sheet receivable items	(5)	(10)	(5)	(10)
Provisions transferred from off-balance sheet	5	10	5	10
Write-offs	(27)	(8)	(27)	(8)
Transfer to off-balance sheet	-	(21)	-	(21)
Balance as of 31 December	**4,140**	**4,496**	**3,600**	**4,496**

22. Deposits

	Group		Bank	
	2011 HRK '000	**2010 HRK '000**	**2011 HRK '000**	**2010 HRK '000**
Bank deposits	1,252	718	1,252	718
Foreign currency accounts of the companies	85	171	85	171
Foreign currency account of the Ministry of Finance of the Republic of Croatia	20,059	26,847	20,059	26,847
Foreign currency special purpose accounts of the companies	2,027	1,500	2,027	1,500
Deposits by local authorities and state funds	54,855	60,463	54,855	60,463
Deposits by state institutions	73,967	132,959	73,967	132,959
Other deposits	1,998	-	1,998	-
	154,243	**222,658**	**154,243**	**222,658**

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 6,860 thousand (2010: HRK 13,442 thousand), grant funds provided by the Global Environment Facility (GEF) aimed at the Renewable Energy Resources Project of HRK 7,961 thousand (2010: HRK 8,394 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 5,238 thousand (2010: HRK 5,011 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, the Ministry of the Economy, the Ministry for Entrepreneurship and Crafts, the Ministry for Maritime Affairs, Transport and Infrastructure, the Ministry of Agriculture, the Ministry of Regional Development and EU Funds, the Environmental Protection and Energy Efficiency Fund, the company 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		Bank	
	2011 HRK '000	**2010 HRK '000**	**2011 HRK '000**	**2010 HRK '000**
Balance as of 1 January	7,015,834	5,186,993	7,015,834	5,186,993
New borrowings	1,547,066	4,110,062	1,547,066	4,110,062
Repayments	(516,386)	(2,331,936)	(516,386)	(2,331,936)
Net foreign exchange gains/(losses)	108,941	50,715	108,941	50,715
	8,155,455	7,015,834	8,155,455	7,015,834
Accrued interest	41,908	31,581	41,908	31,581
Balance as of 31 December	**8,197,363**	**7,047,415**	**8,197,363**	**7,047,415**

Interest rates on borrowings 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 2011 and as at 31 December 2011, 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 2011 HRK '000**	**Net book value 2011 HRK '000**	**Fair value 2010 HRK '000**	**Net book value 2010 HRK '000**
Bonds EUR 100 million	5.899	150,593	150,609	300,411	295,407
Bonds EUR 300 million	5.021	-	-	2,220,005	2,215,185
Bonds EUR 150 million	4.836	1,074,565	1,128,962	1,075,288	1,106,969
Bonds EUR 250 million	5.076	1,684,611	1,876,029	1,769,785	1,838,839
Bonds EUR 250 million	8.58	1,898,871	1,867,005	1,928,361	1,809,553
Accrued interest		-	122,119	-	216,300
		4,808,640	**5,144,724**	**7,293,850**	**7,482,253**

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 150,609 thousand as at 31 December 2011 and HRK 295,407 thousand as at 31 December 2010) and with a maturity period of 10 years and a fixed interest rate of 5.75% and amortized repayment in the period from 2008 to 2012. Interest is paid annually, in arrears. The first instalment was due and paid in December 2008 and the amount outstanding as at 31 December 2011 was HRK 150,609 thousand (EUR 20,000 thousand). Bonds are listed in Luxembourg Stock Exchange quotation.

In the reporting period, on 10 February 2011, HBOR redeemed long-term securities of HRK 2,223,853 thousand together with interest of HRK 108,413 thousand, on its regular maturity date. The bonds had been issued on 11 February 2004 according to the Agreement between HBOR and Deutsche Bank AG London and UBS Limited (as joint lead managers) under the EMTN Program with a guarantee of the Republic of Croatia in the amount of EUR 300,000 thousand (HRK 2,215,185 thousand as of 31 December 2010) with a maturity period of 7 years and a fixed interest rate of 4.875%.

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 1,128,962 thousand as of 31 December 2011 and HRK 1,106,969 thousand as at 31 December 2010) 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 1,876,029 thousand as at 31 December 2011 and HRK 1,838,839 thousand as at 31 December 2010) 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 1,867,005 thousand as at 31 December 2011 and HRK 1,809,553 thousand as at 31 December 2010) 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.

25. Other liabilities

	Group 2011 HRK '000	Group 2010 HRK '000	Bank 2011 HRK '000	Bank 2010 HRK '000
Deferred recognition of interest income	941,090	786,057	941,090	786,057
Liabilities in respect of subsidized interest	137,898	258,279	137,898	258,279
Provisions for guarantees and commitments	28,940	53,856	28,940	53,856
Provisions for other liabilities	51,889	46,012	51,750	45,912
Accrued salaries	4,626	3,870	4,540	3,764
Deferred recognition of income from fees on issued guarantees	1,745	2,782	1,745	2,782
Liabilities to suppliers	1,262	1,341	1,184	1,168
Liabilities for prepaid receivables	1,809	5,089	1,809	5,089
Deferrable premium	375	309	-	-
Provisions for claims	923	126	-	-
Provisions for return premiums	80	-	-	-
Liabilities to re-insurers	1,349	969	-	-
Other liabilities	3,620	3,628	3,397	3,288
Deferred tax liabilities	5	-	-	-
	1,175,611	**1,162,318**	**1,172,353**	**1,160,195**

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 122,608 thousand in respect of the Programme of Preferential Financing through HBOR's Loan Programmes (2010: HRK 244,920 thousand),
- HRK 11,080 thousand in respect of the Financing Model for the Reconstruction and Modernisation of the Fishing Fleet (2010: HRK 11,079 thousand),
- HRK 1,850 thousand in respect of the Environmental protection and energy efficiency fund and Energy efficiency project (2010: HRK 1,800 thousand),
- HRK 219 thousand (2010: HRK 480 thousand) in respect of loans granted to the borrowers investing into entrepreneurial zones.
- HRK 2,141 thousand (2010: HRK 0 thousand) in respect of the Loan Programme for the Financing of Female Entrepreneurship

25. Other liabilities (continued)

Deferred recognition of interest income of HRK 941,090 thousand (2010: HRK 786,057 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 210,990 thousand (2010: HRK 115,551 thousand), and in respect of those already in repayment stage amounting to HRK 730,100 thousand (2010: HRK 670,506 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 15,099 thousand relates to banks (2010: HRK 31,692 thousand), HRK 9,842 thousand relates to domestic companies (2010: HRK 14,644 thousand), HRK 2,511 thousand relates to state-owned companies (2010: HRK 2,787 thousand), HRK 56 thousand relates to the public sector (2010: HRK 150 thousand) and HRK 1,432 thousand relates to others (2010: HRK 4,583 thousand).

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

		Group		Bank
	2011 HRK '000	**2010 HRK '000**	**2011 HRK '000**	**2010 HRK '000**
Balance as at 1 January	53,856	110,204	53,856	110,204
Increase in provision for guarantees and commitments	65,992	88,616	65,992	88,616
Release in provision for guarantees and commitments	(91,049)	(145,164)	(91,049)	(145,164)
Net foreign exchange gains/(losses) on provision for impairment losses	141	200	141	200
Provision for guarantees and commitments	**28,940**	**53,856**	**28,940**	**53,856**
Balance as at 1 January	46,012	25,139	45,912	25,139
Increase in provision for other liabilities	10,390	25,057	10,252	24,957
Release in provision for other liabilities	(4,513)	(4,184)	(4,414)	(4,184)
Provisions for other liabilities	**51,889**	**46,012**	**51,750**	**45,912**
Balance as at 31 December	**80,829**	**99,868**	**80,690**	**99,768**

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 2010	**11,963**
Write-off	-
Net foreign exchange	129
Balance as of 31 December 2010	**12,092**
Write-off	-
Net foreign exchange	238
Balance as of 31 December 2011	**12,330**

The Guarantee fund, of HRK 12,330 thousand and HRK 12,092 thousand as of 31 December 2011 and 2010 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 238 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		Bank
	2011	**2010**	**2011**	**2010**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**
Guarantees issued in HRK	518	518	518	518
Guarantees issued in foreign currency	325,112	352,685	325,112	352,685
Issued bills of exchange	22,782	28,472	22,782	28,472
Undrawn loans	1,151,477	951,951	1,151,477	951,951
EIF – subscribed, not called up capital (note 15)	30,122	29,541	30,122	29,541
Open letters of credit in foreign currency	1,912	-	1,912	-
	1,531,923	1,363,167	1,531,923	1,363,167
Provisions for guarantees and commitments	(28,940)	(53,856)	(28,940)	(53,856)
	1,502,983	**1,309,311**	**1,502,983**	**1,309,311**

Guarantees

Issued guarantees and open letters of credit represent the liability to 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 and letters of credit bear the same credit risk as loans.

Bank guarantees are for the most part guaranteed by the Government of the Republic of Croatia, whereas letters of credit are entirely covered by deposits (Note 22).

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.

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, the Ministry for Entrepreneurship and Crafts, the Ministry for Maritime Affairs, Transport and Infrastructure, the Ministry of Agriculture, the Ministry of Regional Development and EU Funds, the Environmental Protection and Energy Efficiency Fund, the company Vodovod i kanalizacija d.o.o., Split and the Croatian Agency for Small Business ("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:

Group

Programme	2011 HRK '000	2010 HRK '000
Development and Reconstruction of Rural Housing	61,988	71,117
Employment of Former Soldiers	478,451	528,864
Emergency Reconstruction Project (loan IBRD 3760 - HR)	191	228
Loans to companies having difficulties – Ministry of Finance funds	14,518	49,519
Municipal Environmental Infrastructure Investment Program – MEIP	773,298	753,298
Collection of receivables under HAMAG guarantees	262	264
Insurance of export transactions	218,956	217,675
Programme of Preferential Financing through HBOR's Loan Programmes	122,608	244,920
Programme for Development and Employment - loans	87,550	99,175
Programme for Regional Development of the Republic of Croatia - loans	23,385	25,446
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of the Economy	22,738	38,293
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry for Maritime Affairs, Transport and Infrastructure	24,771	40,326
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of Agriculture	36,225	51,779
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of the Economy - interest subsidy	384	384
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry for Maritime Affairs, Transport and Infrastructure - interest subsidy	1,561	1,561
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of Agriculture - interest subsidy	9,135	9,134
Renewable Energy Resources Project	22,642	22,122
VIK – EKO account A – dedicated water charge	484,922	437,346
VIK – EKO account B – VAT	134,685	121,509
The Environment and Energy Efficiency Fund - interest subsidy	850	800
Programme of Issuing Bank Guarantees for Energy Efficiency Projects – IBRD	5,238	5,011
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	219	480
Operational Programme for the development of cattle-breeding production	50,631	45,530
Operational Programme for the development of pig-breeding production	32,913	28,231
Financing the Establishment of Fishing Infrastructure – Ministry for Maritime Affairs, Transport and Infrastructure	46,665	-
Loan Programme for the Financing of Female Entrepreneurship – Ministry for Entrepreneurship and Crafts – interest subsidy	2,141	-
Transactions related to investments in the Funds for Economic Co-operation*	154,654	-
	2,812,581	**2,794,012**

*The fair value of net assets value of the Funds for Economic Co-operation is recognised on the basis of the latest available data and does not represent the final fair value.

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	2011 HRK '000	2010 HRK '000
Development and Reconstruction of Rural Housing	61,988	71,117
Employment of Former Soldiers	478,451	528,864
Emergency Reconstruction Project (loan IBRD 3760 - HR)	191	228
Loans to companies having difficulties – Ministry of Finance funds	14,518	49,519
Municipal Environmental Infrastructure Investment Program – MEIP	773,298	753,298
Collection of receivables under HAMAG guarantees	262	264
Insurance of export transactions	218,956	217,675
Programme of Preferential Financing through HBOR's Loan Programmes	122,608	244,920
Programme for Development and Employment - loans	87,550	99,175
Programme for Regional Development of the Republic of Croatia - loans	23,385	25,446
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of the Economy	22,738	38,293
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry for Maritime Affairs, Transport and Infrastructure	24,771	40,326
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of Agriculture	36,225	51,779
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of the Economy - interest subsidy	384	384
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry for Maritime Affairs, Transport and Infrastructure - interest subsidy	1,561	1,561
Financing Model for the Reconstruction and Modernisation of the Fishing Fleet - Ministry of Agriculture - interest subsidy	9,135	9,134
Renewable Energy Resources Project	22,642	22,122
VIK – EKO account A – dedicated water charge	484,922	437,346
VIK – EKO account B - VAT	134,685	121,509
The Environment and Energy Efficiency Fund - interest subsidy	850	800
Programme of Issuing Bank Guarantees for Energy Efficiency Projects – IBRD	5,238	5,011
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	219	480
Operational Programme for the development of cattle-breeding production	50,631	45,530
Operational Programme for the development of pig-breeding production	32,913	28,231
Financing the Establishment of Fishing Infrastructure – Ministry for Maritime Affairs, Transport and Infrastructure	46,665	-
Loan Programme for the Financing of Female Entrepreneurship – Ministry for Entrepreneurship and Crafts – interest subsidy	2,141	-
Transactions related to investments in the Funds for Economic Co-operation*	154,654	-
HKO – Funds for the coverage of technical provisions	2,069	1,077
	2,814,650	**2,795,089**

*The fair value of net assets of the Funds for Economic Co-operation is recognised on the basis of the latest data available and does not represent the final fair value.

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 2011 and 31 December 2010, 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	Exposure	Liabilities	Income	Expense
	2011 HRK '000	2011 HRK '000	2011 HRK '000	2011 HRK '000	2010 HRK '000	2010 HRK '000	2010 HRK '000	2010 HRK '000
Owner	1,424,260	163,195	52,914	2,434	291,261	315,172	22,498	16
Government funds, executive authorities and agencies	96,817	23,460	9,231	6	163,463	96,450	11,903	377
State-owned companies	849,267	898	45,881	637	1,535,581	1,655	72,116	-
Non-controlling interests	711	733	1,109	3,207	106	708	124	937
Associates	24	-	363	-	3	-	100	-
Key management personnel	3,443	-	117	9	2,578	-	95	7
Total	**2,374,522**	**188,286**	**109,615**	**6,293**	**1,992,992**	**413,985**	**106,836**	**1,337**

Bank	Exposure	Liabilities	Income	Expense	Exposure	Liabilities	Income	Expense
	2011 HRK '000	2011 HRK '000	2011 HRK '000	2011 HRK '000	2010 HRK '000	2010 HRK '000	2010 HRK '000	2010 HRK '000
Owner	1,424,260	163,195	52,914	2,434	291,261	315,172	22,498	16
Government funds, executive authorities and agencies	96,817	23,460	9,231	6	163,463	96,450	11,903	377
State-owned companies	849,267	898	45,881	637	1,535,581	1,655	72,116	-
Subsidiary companies	19,127	-	17	-	19,149	-	-	-
Associates	24	-	363	-	3	-	100	-
Key management personnel	3,050	-	102	9	2,167	-	88	3
Total	**2,392,545**	**187,553**	**108,508**	**3,086**	**2,011,624**	**413,277**	**106,705**	**396**

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 reversal of impairment losses and provisions.

Expense includes impairment losses and provisions.

30. Related-party transactions (continued)

b) Collateral received

	Group		Bank	
	2011	**2010**	**2011**	**2010**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**
The Republic of Croatia	975,688	1,430,722	750,139	1,245,355
State agencies	422,608	364,901	422,608	364,901
Total	**1,398,296**	**1,795,623**	**1,172,747**	**1,610,256**

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 2011, salaries for the Group amounted to HRK 7,748 thousand (2010: HRK 4,762 thousand), and for the Bank HRK 6,753 thousand (2010: HRK : 4.324 thousand).

Remuneration for the work of the members of the Supervisory Board in 2011 amounted to HRK 434 thousand for the Group and the Bank (2010: HRK 242 thousand) 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 most significant types of risk the Bank is exposed to: credit risk, liquidity risk, interest rate risk and foreign exchange risk as well as operational risk. These risks are managed daily in accordance with the policies, procedures, methodologies and limit systems that regulate this area as well as through the operations of the bodies of the Bank in charge.

Risk management structure

The Supervisory Board is responsible for monitoring the appropriateness and effectiveness of the risk management process in the Bank. The Supervisory Board adopts the Risk Management Strategies that lay out the main principles and standards of risk management and define the tendency towards risk-taking.

The Managing Board of the Bank is responsible for implementing risk management strategies and establishing an effective and reliable risk management system. In order to accomplish its task, the Managing Board delegated their risk management authority to three 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 the Risk Management unit as 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 in the course of its business. The Risk Management unit carries out its role by performing analyses, evaluations, measurements, controls, by giving suggestions and recommendations, by developing risk management-related procedures and methodologies, recommending and monitoring accepted exposure limits, as well as reporting on risks to the bodies in charge, 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, systems of limits are 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 that participate in risk management and that 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 continuously developed for the purpose of minimizing potential future risks.

Bodies 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, possible losses by significant currencies, interest rate gap, average weighted rates for Bank sources and placements as well as a number of liquidity status indicators and projections, etc. The reporting dynamics and the risk measurement/assessment methodologies are prescribed within the framework of the procedures for the management of the aforementioned risks.

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 on-lends part of its placements via commercial banks the assessment of which is based on the Methodology for the Assessment and Selection of Banks and the Methodology for the Assessment 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 Economic Revival and Development (Model A+) that has been introduced as a measure for 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 the effect of mitigation through collateral received:

	Group		Bank	
	Gross highest exposure 2011 HRK '000	Gross highest exposure 2010 HRK '000	Gross highest exposure 2011 HRK '000	Gross highest exposure 2010 HRK '000
Assets				
Cash on hand and due from banks	267,719	1,258,725	267,215	1,258,008
Deposits with other banks	67,377	137,555	34,811	103,284
Loans to banks	14,299,705	15,449,447	14,299,705	15,449,447
Loans to other customers	6,184,717	5,796,393	6,184,717	5,796,393
Financial assets at fair value through profit or loss	519	500	-	-
Assets available for sale	1,083,467	187,710	1,081,385	186,659
Assets held to maturity	1,092	1,077	-	-
Other assets	3,941	3,083	2,374	2,388
Total	**21,908,537**	**22,834,490**	**21,870,207**	**22,796,179**
Guarantees and commitments				
Issued guarantees in domestic currency	513	513	513	513
Issued guarantees in foreign currency	317,723	345,184	317,723	345,184
Issued bills of exchange	22,554	28,187	22,554	28,187
Open letters of credit in foreign currency	1,893	-	1,893	-
Undrawn loans	1,130,178	905,886	1,130,178	905,886
EIF – subscribed, not called up capital	30,122	29,541	30,122	29,541
Total	**1,502,983**	**1,309,311**	**1,502,983**	**1,309,311**
Total credit risk exposure	**23,411,520**	**24,143,801**	**23,373,190**	**24,105,490**

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 2011, the highest credit exposure of the Group to one debtor equalled HRK 1,505,175 thousand (31 December 2010: HRK 1,496,302 thousand), and of the Bank HRK 1,472,105 thousand (31 December 2010: HRK 1,461,313 thousand) after the effect of mitigation through 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.

As a special financial institution, the Bank performs its development role by granting loans to final borrowers via commercial banks with which it has entered into co-operation agreements. In its operations, the Bank abides by the HBOR Act. The regulations of the Croatian National Bank that apply to the Bank have been incorporated into the internal documents used also for the monitoring of the exposure towards the commercial banks and their associated entities. Since the exposure towards some of the banks has reached the maximum permitted level, the Bank obtained, at the end of the reporting year, in order to be able to continue performing its development role and make the loans accessible to as many final borrowers as possible, an approval from the Supervisory Board for an increase in the exposure towards the banks and their associated entities that have, in accordance with HBOR's internal methodology, been assigned a high rating. The exposure level approved by the Supervisory Board will be maintained by using all instruments and techniques available for mitigating HBOR's exposure towards the banks. This exposure increase approved by the Supervisory Board was not used by the Bank in 2011. It is a preparation for the operations in 2012.

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 the effect of mitigation through collateral received, is as follows:

Group 2011	Republic of Croatia HRK '000	EU countries HRK '000	Other countries HRK '000	Total HRK '000
Assets				
Cash on hand and due from banks	152,652	113,180	1,887	267,719
Deposits with other banks	52,396	-	14,981	67,377
Loans to banks	14,298,613	-	1,092	14,299,705
Loans to other customers	6,000,323	-	184,394	6,184,717
Financial assets at fair value through profit or loss	519	-	-	519
Assets available for sale	1,070,721	12,746	-	1,083,467
Assets held to maturity	1,092	-	-	1,092
Other assets	3,941	-	-	3,941
Total	**21,580,257**	**125,926**	**202,354**	**21,908,537**
Guarantees and commitments				
Issued guarantees in domestic currency	513	-	-	513
Issued guarantees in foreign currency	317,723	-	-	317,723
Issued bills of exchange	-	22,554	-	22,554
Open letters of credit in foreign currency	1,893	-	-	1,893
Undrawn loans	1,130,178	-	-	1,130,178
EIF – subscribed, not called up capital	-	30,122	-	30,122
Total	**1,450,307**	**52,676**	**-**	**1,502,983**
Total credit risk exposure	**23,030,564**	**178,602**	**202,354**	**23,411,520**

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 the effect of mitigation through collateral received (continued):

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**

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 the effect of mitigation through collateral received (continued):

Bank 2011	**Republic of Croatia HRK '000**	**EU countries HRK '000**	**Other countries HRK '000**	**Total HRK '000**
Assets				
Cash on hand and due from banks	152,148	113,180	1,887	267,215
Deposits with other banks	19,830	-	14,981	34,811
Loans to banks	14,298,613	-	1,092	14,299,705
Loans to other customers	6,000,323	-	184,394	6,184,717
Assets available for sale	1,068,639	12,746	-	1,081,385
Other assets	2,374	-	-	2,374
Total	**21,541,927**	**125,926**	**202,354**	**21,870,207**
Guarantees and commitments				
Issued guarantees in domestic currency	513	-	-	513
Issued guarantees in foreign currency	317,723	-	-	317,723
Issued bills of exchange	-	22,554	-	22,554
Open letters of credit in foreign currency	1,893	-	-	1,893
Undrawn loans	1,130,178	-	-	1,130,178
EIF – subscribed, not called up capital	-	30,122	-	30,122
Total	**1,450,307**	**52,676**	**-**	**1,502,983**
Total credit risk exposure	**22,992,234**	**178,602**	**202,354**	**23,373,190**

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 the effect of mitigation through 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**

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 the effect of mitigation through collateral received, is as follows:

Group	Gross highest exposure	Net highest exposure	Gross highest exposure	Net highest exposure
	2011 HRK '000	2011 HRK '000	2010 HRK '000	2010 HRK '000
Financial intermediation and insurance	15,579,394	-	17,481,349	-
Water and electric supply and other infrastructure	1,190,430	856,125	1,375,778	991,431
Tourism	721,195	9,110	822,274	37,924
Transport, warehousing and connections	681,200	218,409	726,658	21,311
Shipbuilding	499,900	170,015	569,708	122,868
Agriculture and fishery	495,771	75,187	438,583	79,329
Food industry	494,068	184,596	381,534	101,962
Construction industry	413,023	91,129	342,487	90,674
Other industry	417,795	62,821	308,388	89,334
Public administration	1,060,399	1,060,399	172,701	172,701
Education	115,304	112,747	134,369	132,542
Manufacture of basic metals and fabricated metal products, except machinery and equipment	163,833	3,810	178,336	13,763
Manufacture of chemicals and chemical products	85,153	25,966	180,333	633
Manufacture of other non-metallic mineral products	201,465	53,467	181,843	35,001
Other	1,292,590	285,208	849,460	227,138
Total credit risk exposure	**23,411,520**	**3,208,989**	**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 the effect of mitigation through collateral received, is as follows:

Bank	Gross highest exposure	Net highest exposure	Gross highest exposure	Net highest exposure
	2011 HRK '000	2011 HRK '000	2010 HRK '000	2010 HRK '000
Financial intermediation and insurance	15,544,730	1	17,444,835	12
Water and electric supply and other infrastructure	1,190,430	856,125	1,375,778	991,431
Tourism	721,195	9,110	822,274	37,924
Transport, warehousing and connections	681,200	218,409	726,658	21,311
Shipbuilding	499,900	170,015	569,708	122,868
Agriculture and fishery	495,771	75,187	438,583	79,329
Food industry	494,068	184,596	381,534	101,962
Construction industry	413,023	91,129	342,487	90,674
Other industry	417,795	62,821	308,388	89,334
Public administration	1,060,399	1,060,399	172,701	172,701
Education	115,304	112,747	134,369	132,542
Manufacture of basic metals and fabricated metal products, except machinery and equipment	163,833	3,810	178,336	13,763
Manufacture of chemicals and chemical products	85,153	25,966	180,333	633
Manufacture of other non-metallic mineral products	201,465	53,467	181,843	35,001
Other	1,288,924	281,542	847,663	225,341
Total credit risk exposure	**23,373,190**	**3,205,324**	**24,105,490**	**2,114,826**

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").

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.

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 2011 amounted to HRK 20,202,531 thousand (2010: HRK 22,027,190 thousand) and for the Bank HRK 20,167,866 thousand (2010: HRK 21,990,664 thousand).

In the total net highest exposure of the Bank in 2011, the credit risk of HRK 2,392,924 thousand (2010: HRK 1,409,048 thousand) is not covered with ordinary collateral, but it relates to receivables and received funds from the Republic of Croatia of HRK 485,927 thousand (2010: HRK 270,002 thousand), from local (regional) authorities of HRK 132,108 thousand (2010: HRK 141,121 thousand), state-owned companies for whose commitments the Republic of Croatia guarantees jointly and unconditionally of HRK 86,464 thousand (2010: HRK 134,121 thousand), government funds of HRK 9,161 thousand (2010: HRK 11,251 thousand), government bonds and Treasury bills of the Ministry of Finance of HRK 1,068,478 thousand (2010: HRK 173,554 thousand). In addition, an amount of HRK 610,786 thousand (2010: HRK 678,999 thousand) relates to receivables from a majority 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 (%) 2011	Historical default rate (%) 2010	Group 2011 HRK '000	Group 2010 HRK '000	Bank 2011 HRK '000	Bank 2010 HRK '000
A	1.12%	1.43 %	21,763,832	22,397,582	21,725,502	22,359,271
B	16.61%	15.11 %	1,647,688	1,746,219	1,647,688	1,746,219
C	82.74%	73.13 %	-	-	-	-
	Total		**23,411,520**	**24,143,801**	**23,373,190**	**24,105,490**

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 a 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 2011 gross loans, before provision for impairment losses, that were restructured amounted to HRK 1,257,767 thousand (2010: HRK 1,112,087 thousand), and the value of the restructured loans after provision for impairment losses amounted to HRK 649,322 thousand (2010: HRK 760,077 thousand).

Restructured loans to banks, before provision for impairment losses, account for 37% (2010: 55%) of total restructured loans or 65% after provision for impairment losses (2010: 76%). In this case, commercial banks bear the default risk of the ultimate borrower.

31. Risk management (continued)

31.2. Credit risk (continued)

Credit risk quality according to type of financial assets

Credit risk analysis, before and after the effect of mitigation through 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 2011	Gross exposure of portfolio of risk group A	Gross exposure of portfolio of risk group B	Gross exposure of portfolio of risk group C	Gross exposure of total portfolio	Net exposure of portfolio of risk group A	Net exposure of portfolio of risk group B	Net exposure of portfolio of risk group C	Net exposure of total portfolio
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Assets								
Cash on hand and due from banks	267,719	-	-	267,719	-	-	-	-
Deposits with other banks	67,377	-	-	67,377	-	-	-	-
Loans to banks	13,779,530	520,175	-	14,299,705	-	-	-	-
Loans to other customers	5,102,374	1,082,343	-	6,184,717	1,868,112	101,594	-	1,969,706
Financial assets at fair value through profit or loss	519	-	-	519	-	-	-	-
Assets available for sale	1,083,467	-	-	1,083,467	1,069,482	-	-	1,069,482
Assets held to maturity	1,092	-	-	1,092	1,092	-	-	1,092
Other assets	3,924	17	-	3,941	3,904	17	-	3,921
Total	**20,306,002**	**1,602,535**	-	**21,908,537**	**2,942,590**	**101,611**	**-**	**3,044,201**
Guarantees and commitments								
Issued guarantees in domestic currency	513	-	-	513	-	-	-	-
Issued guarantees in foreign currency	289,108	28,615	-	317,723	6,951	28,615	-	35,566
Issued bills of exchange	22,554	-	-	22,554	-	-	-	-
Open letters of credit in foreign currency	1,893	-	-	1,893	-	-	-	-
Undrawn loans	1,113,640	16,538	-	1,130,178	126,391	2,831	-	129,222
EIF – subscribed, not called up capital	30,122	-	-	30,122	-	-	-	-
Total	**1,457,830**	**45,153**	-	**1,502,983**	**133,342**	**31,446**	-	**164,788**
Total credit risk exposure	**21,763,832**	**1,647,688**	**-**	**23,411,520**	**3,075,933**	**133,057**	**-**	**3,208,989**

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 the effect of mitigation through 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):

Group **2010**	**Gross exposure of portfolio of risk group A**	**Gross exposure of portfolio of risk group B**	**Gross exposure of portfolio of risk group C**	**Gross exposure of total portfolio**	**Net exposure of portfolio of risk group A**	**Net exposure of portfolio of risk group B**	**Net exposure of portfolio of risk group C**	**Net exposure of total portfolio**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**	**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	14,945,550	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 the effect of mitigation through 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 2011	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	267,215	-	-	267,215	-	-	-	-
Deposits with other banks	34,811	-	-	34,811	-	-	-	-
Loans to banks	13,779,530	520,175	-	14,299,705	-	-	-	-
Loans to other customers	5,102,374	1,082,343	-	6,184,717	1,868,111	101,594	-	1,969,705
Assets available for sale	1,081,385	-	-	1,081,385	1,068,478	-	-	1,068,478
Other assets	2,357	17	-	2,374	2,336	17	-	2,353
Total	**20,267,672**	**1,602,535**	**-**	**21,870,207**	**2,938,925**	**101,611**	**-**	**3,040,536**
Guarantees and commitments								
Issued guarantees in domestic currency	513	-	-	513	-	-	-	-
Issued guarantees in foreign currency	289,108	28,615	-	317,723	6,951	28,615	-	35,566
Issued bills of exchange	22,554	-	-	22,554	-	-	-	-
Open letters of credit in foreign currency	1,893	-	-	1,893	-	-	-	-
Undrawn loans	1,113,640	16,538	-	1,130,178	126,391	2,831	-	129,222
EIF – subscribed, not called up capital	30,122	-	-	30,122	-	-	-	-
Total	**1,457,830**	**45,153**	-	**1,502,983**	**133,342**	**31,446**	-	**164,788**
Total credit risk exposure	**21,725,502**	**1,647,688**	**-**	**23,373,190**	**3,072,267**	**133,057**	**-**	**3,205,324**

In the total net highest exposure of the Group and the Bank, the amount of loans to other customers of HRK 1,323,234 thousand is not covered by ordinary collateral, but it relates to receivables and received funds from the Republic of Croatia of HRK 484,725 thousand, local (regional) authorities of HRK 132,108 thousand, public companies for whose liabilities the Republic of Croatia guarantees jointly and unconditionally of HRK 86,464 thousand and the government funds of HRK 9,151 thousand. An additional amount of HRK 610,786 thousand relates to receivables from majority (51%) state-owned companies.

The amount of assets available for sale and held to maturity is not covered by ordinary collateral but it relates to government bonds and treasury bills of the Ministry of Finance of HRK 1,070,574 thousand for the Group and HRK 1,068,478 thousand for the Bank.

Other assets of HRK 1,213 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 the effect of mitigation through 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	Gross exposure of portfolio of risk group B	Gross exposure of portfolio of risk group C	Gross exposure of total portfolio	Net exposure of portfolio of risk group A	Net exposure of portfolio of risk group B	Net exposure of portfolio of risk group C	Net exposure of total portfolio
	HRK ‘000	HRK ‘000	HRK ‘000	HRK ‘000	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	14,945,550	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 quality according to the gross exposure of the type of financial assets on positions of assets and guarantees and commitments by risk category:

Group 2011	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	267,719	-	-	267,719
Deposits with other banks	67,377	-	-	67,377
Loans to banks	13,580,769	198,761	520,175	14,299,705
Loans to other customers	4,956,084	146,290	1,082,343	6,184,717
Financial assets at fair value through profit or loss	519	-	-	519
Assets available for sale	1,083,467	-	-	1,083,467
Assets held to maturity	1,092	-	-	1,092
Other assets	3,661	263	17	3,941
Total	**19,960,688**	**345,314**	**1,602,535**	**21,908,537**
Guarantees and commitments				
Issued guarantees in domestic currency	513	-	-	513
Issued guarantees in foreign currency	289,108	-	28,615	317,723
Issued bills of exchange	22,554	-	-	22,554
Open letters of credit in foreign currency	1,893	-	-	1,893
Undrawn loans	1,113,640	-	16,538	1,130,178
EIF – subscribed, not called up capital	30,122	-	-	30,122
Total	**1,457,830**	**-**	**45,153**	**1,502,983**
Total credit risk exposure	**21,418,518**	**345,314**	**1,647,688**	**23,411,520**

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):

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 **2011**	**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	267,215	-	-	267,215
Deposits with other banks	34,811	-	-	34,811
Loans to banks	13,580,769	198,761	520,175	14,299,705
Loans to other customers	4,956,084	146,290	1,082,343	6,184,717
Assets available for sale	1,081,385	-	-	1,081,385
Other assets	2,094	263	17	2,374
Total	**19,922,358**	**345,314**	**1,602,535**	**21,870,207**
Guarantees and commitments				
Issued guarantees in domestic currency	513	-	-	513
Issued guarantees in foreign currency	289,108	-	28,615	317,723
Issued bills of exchange	22,554	-	-	22,554
Open letters of credit in foreign currency	1,113,640	-	16,538	1,130,178
Undrawn loans	30,122	-	-	30,122
EIF – subscribed, not called up capital	1,893	-	-	1,893
Total	**1,457,830**	**-**	**45,153**	**1,502,983**
Total credit risk exposure	**21,380,188**	**345,314**	**1,647,688**	**23,373,190**

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 2010	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	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
Total	**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)

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

	Up to 2 days 2011 HRK '000	3 to 45 days 2011 HRK '000	46 to 90 days 2011 HRK '000	Over 90 days 2011 HRK '000	Total 2011 HRK '000	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
Assets										
Loans to banks	175,563	13,321	2,372	7,505	198,761	31,320	16,298	8,077	74	55,769
Loans to other customers	120,722	1,008	1,529	23,031	146,290	33,947	894	2,336	2,248	39,425
Other assets	4	105	115	39	263	315	30	-	-	345
Total	**296,289**	**14,434**	**4,016**	**30,575**	**345,314**	**65,582**	**17,222**	**10,413**	**2,322**	**95,539**

From total due and not impaired loans to banks in 2011, an amount of HRK 14,781 thousand or 7% relates to not executed extensions of revolving loans under framework contracts within the export credit financing programme.

If the total amount of due and not impaired loans to banks is reduced by the debt of banks under the export credit finance programme, the remaining debt equals HRK 183,980 thousand.

Unlike in the previous year, when the balance of overdue receivables from banks was mostly a consequence of approved not executed extensions under the export credit finance programme, at the end of 2011, the increase was mostly a consequence of maturities falling due on 31 December 2011 that was not a working day.

From total due and not impaired loans to other customers in 2011, an amount of HRK 120,722 thousand or 83% relates to delays of up to 2 days, of which the amount of HRK 6,166 thousand, i.e. 5%, was guaranteed by the Republic of Croatia.

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

If the total amount of due and not impaired loans to banks is reduced by the debt of banks under the export credit finance programme, the remaining debt equals HRK 13,119 thousand.

From total due and not impaired loans to other customers in 2010, an amount of HRK 33,947 thousand or 86% relates to delays of up to 2 days, of which the amount of HRK 6,596 thousand, i.e. 17%, was guaranteed by 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 companies' equity instruments, 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 assignment of receivables instead 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 on islands, in areas of special concern and hill or mountain areas, 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)

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 arises from the Bank's present or expected inability to fund its financial liabilities when due.

The basic principles for managing the Bank's liquidity risk are defined by the Liquidity Risk Management Procedures and decisions/conclusions 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. Subsequently, a correction of plans of inflow and outflow is made in case of need or the appearance of new circumstances.

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.

The Bank does not hold deposits of citizens and is therefore not exposed to wide daily fluctuations in liquidity.

As a special financial institution the Bank is not profit driven and is in that sense not using derivative instruments. 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 2011 and 31 December 2010 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 2011	**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	179,029	39,600	49,094	-	-	267,723
Deposits with other banks	29,863	4,948	32,566	-	-	67,377
Loans to banks*	1,159,624	2,823,018	2,241,496	3,258,832	4,816,735	14,299,705
Loans to other customers	445,574	189,990	895,933	2,072,874	2,580,346	6,184,717
Financial assets at fair value through profit or loss	519	-	-	-	-	519
Assets available for sale	1,075,300	8,167	-	-	-	1,083,467
Assets held to maturity	-	23	-	-	1,069	1,092
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	68,401	68,401
Non-current assets held for sale	-	-	23,918	10,514	-	34,432
Other assets	3,224	1,486	281	-	439	5,430
Total assets (1)	**2,893,133**	**3,067,232**	**3,243,288**	**5,342,220**	**7,466,990**	**22,012,863**
Liabilities						
Deposits	154,012	13	63	69	86	154,243
Borrowings	55,656	91,025	372,197	1,823,733	5,854,752	8,197,363
Bonds payable	-	122,119	2,243,406	451,585	2,327,614	5,144,724
Other liabilities	171,266	49,369	170,434	375,262	409,280	1,175,611
Total liabilities	**380,934**	**262,526**	**2,786,100**	**2,650,649**	**8,591,732**	**14,671,941**
Equity						
Founder's capital	-	-	-	-	5,343,739	5,343,739
Retained earnings and reserves	-	-	-	-	1,836,565	1,836,565
Other reserves	-	-	-	-	(16,813)	(16,813)
Net profit for the year	-	-	-	-	147,626	147,626
Total equity attributable to equity holders of the parent	**-**	**-**	**-**	**-**	**7,311,117**	**7,311,117**
Non-controlling interests	-	-	-	-	17,475	17,475
Total Equity	**-**	**-**	**-**	**-**	**7,328,592**	**7,328,592**
Guarantee fund	-	-	-	-	12,330	12,330
Total equity and Guarantee fund	**-**	**-**	**-**	**-**	**7,340,922**	**7,340,922**
Total liabilities, equity and Guarantee fund (2)	**380,934**	**262,526**	**2,786,100**	**2,650,649**	**15,932,654**	**22,012,863**
Net assets/liabilities (1) – (2)	**2,512,199**	**2,804,706**	**457,188**	**2,691,571**	**(8,465,664)**	**-**
Net cumulative assets/liabilities	**2,512,199**	**5,316,905**	**5,774,093**	**8,465,664**	**-**	**-**

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

** Receivables of HRK 2,712,136 thousand relate to reverse REPO agreements. The maturity of part of receivables was prolonged after the Statement of Financial Position date, and an amount of HRK 2,050,684 thousand was placed in the 1 up to 3 months maturity category.*

Receivables from Credo banka d.d. in bankruptcy proceedings, are reported in the period of up to 1 month because all amounts became due on the date of opening the bankruptcy proceedings, on 16th January 2012 (see note 36.1).

31. Risk management (continued)

31.3. Liquidity 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	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 agreements. 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.*

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 2011 and 31 December 2010 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 2011	**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	178,525	39,600	49,094	-	-	267,219
Deposits with other banks	29,863	4,948	-	-	-	34,811
Loans to banks*	1,159,624	2,823,018	2,241,496	3,258,832	4,816,735	14,299,705
Loans to other customers	445,574	189,990	895,933	2,072,874	2,580,346	6,184,717
Assets available for sale	1,073,218	8,167	-	-	-	1,081,385
Investments in subsidiaries	-	-	-	-	19,125	19,125
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	68,106	68,106
Non-current assets held for sale	-	-	23,918	10,514	-	34,432
Other assets	2,511	632	281	-	-	3,424
Total assets (1)	**2,889,315**	**3,066,355**	**3,210,722**	**5,342,220**	**7,484,312**	**21,992,924**
Liabilities						
Deposits	154,012	13	63	69	86	154,243
Borrowings	55,656	91,025	372,197	1,823,733	5,854,752	8,197,363
Bonds payable	-	122,119	2,243,406	451,585	2,327,614	5,144,724
Other liabilities	171,013	47,902	169,160	374,861	409,417	1,172,353
Total liabilities	**380,681**	**261,059**	**2,784,826**	**2,650,248**	**8,591,869**	**14,668,683**
Equity						
Founder's capital	-	-	-	-	5,343,739	5,343,739
Retained earnings and reserves	-	-	-	-	1,836,924	1,836,924
Other reserves	-	-	-	-	(16,812)	(16,812)
Net profit for the year	-	-	-	-	148,060	148,060
Total Equity	**-**	**-**	**-**	**-**	**7,311,911**	**7,311,911**
Guarantee fund	-	-	-	-	12,330	12,330
Total equity and Guarantee fund	**-**	**-**	**-**	**-**	**7,324,241**	**7,324,241**
Total liabilities, equity and Guarantee fund (2)	**380,681**	**261,059**	**2,784,826**	**2,650,248**	**15,916,110**	**21,992,924**
Net assets/liabilities (1) – (2)	**2,508,634**	**2,805,296**	**425,896**	**2,691,972**	**(8,431,798)**	**-**
Net cumulative assets/liabilities	**2,508,634**	**5,313,930**	**5,739,826**	**8,431,798**	**-**	**-**

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

** Receivables of HRK 2,712,136 thousand relate to reverse REPO agreements. The maturity of part of receivables was prolonged after the Statement of Financial Position date, and an amount of HRK 2,050,684 thousand was placed in the 1 up to 3 months maturity category.*

Receivables from Credo banka d.d. in bankruptcy proceedings, are reported in the period of up to 1 month because all amounts became due on the date of opening the bankruptcy proceedings, on 16th January 2012 (see note 36.1).

31. Risk management (continued)

31.3. Liquidity risk (continued)

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**	**2,555,762**	**725,645**	**5,424,961**	**13,686,191**	**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 agreements. 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.*

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 2011	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	154,012	13	63	69	86	154,243
Borrowings	58,454	111,002	598,778	2,389,914	6,957,955	10,116,103
Bonds payable	-	-	2,536,983	715,863	2,642,584	5,895,430
Other liabilities	171,266	49,369	170,434	375,262	409,280	1,175,611
Total	**383,732**	**160,384**	**3,306,258**	**3,481,108**	**10,009,905**	**17,341,387**

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 2011	Up to 1 month	1 - 3 months	3 - 12 months	1 - 3 years	Over 3 years	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Financial liabilities						
Deposits	154,012	13	63	69	86	154,243
Borrowings	58,454	111,002	598,778	2,389,914	6,957,955	10,116,103
Bonds payable	-	-	2,536,983	715,863	2,642,584	5,895,430
Other liabilities	171,013	47,902	169,160	374,861	409,417	1,172,353
Total	**383,479**	**158,917**	**3,304,984**	**3,480,707**	**10,010,042**	**17,338,129**

Bank 2010	Up to 1 month	1 - 3 months	3 - 12 months	1 - 3 years	Over 3 years	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	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**

31. Risk management (continued)

31.4. Market risk

Management of market risks at the Bank implies the reduction of interest rate risk and the currency risk to a minimal level.

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 and decisions/conclusions 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, and projections of average weighted interest rates for Bank's funds and placements are made. Based on the mentioned reports, the sensitivity of Bank's income statement to possible interest rate fluctuations is monitored simultaneously with the endeavours to match the interest rates receivable and payable. In this way, the Bank reduces its market movement sensitivity as well as its sensitivity to reference interest rates fluctuations. Furthermore, current market conditions and movements in forecasted market indicators are also monitored.

The Bank continuously analyses interest rate margins by preparing a number of scenarios. Among other things, the impact of the following changes is assessed: change in interest rates by Bank's loan programmes, change in interest reference rates and change in prices of fund sources. The Risk Management unit reports to the ALCO and the Managing Board on the results of the analyses performed.

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 2011 and 2010 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 2011 and 2010 which may not be indicative for the positions in other periods.

Group 2011	**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	504	-	-	-	-	267,219	267,723
Deposits with other banks	29,801	4,940	31,640	-	-	996	67,377
Loans to banks	1,111,199	3,541,833	2,780,935	2,744,984	4,069,218	51,536	14,299,705
Loans to other customers	400,864	343,419	1,808,113	1,650,167	1,948,968	33,186	6,184,717
Financial assets at fair value through profit or loss	-	-	-	-	-	519	519
Assets available for sale	1,074,200	-	-	-	-	9,267	1,083,467
Assets held to maturity	-	-	-	-	1,069	23	1,092
Investments in associates	-	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	-	68,401	68,401
Non-current assets held for sale	-	-	-	-	-	34,432	34,432
Other assets	-	-	-	-	-	5,430	5,430
Total assets (1)	**2,616,568**	**3,890,192**	**4,620,688**	**4,395,151**	**6,019,255**	**471,009**	**22,012,863**

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest risk (continued)

Group 2011	**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	6	13	63	69	-	154,092	154,243
Borrowings	55,656	440,699	1,089,816	1,737,799	4,831,485	41,908	8,197,363
Bonds payable	-	-	2,243,406	451,585	2,327,614	122,119	5,144,724
Other liabilities	-	-	-	-	-	1,175,611	1,175,611
Total liabilities	**55,662**	**440,712**	**3,333,285**	**2,189,453**	**7,159,099**	**1,493,730**	**14,671,941**
Equity							
Founder's capital	-	-	-	-	-	5,343,739	5,343,739
Retained earnings and reserves	-	-	-	-	-	1,836,565	1,836,565
Other reserves	-	-	-	-	-	(16,813)	(16,813)
Net profit for the year	-	-	-	-	-	147,626	147,626
Total equity attributable to equity holders of the parent	**-**	**-**	**-**	**-**	**-**	**7,311,117**	**7,311,117**
Non-controlling interests	-	-	-	-	-	17,475	17,475
Total Equity	**-**	**-**	**-**	**-**	**-**	**7,328,592**	**7,328,592**
Guarantee fund	-	-	-	-	-	12,330	12,330
Total equity and Guarantee fund	**-**	**-**	**-**	**-**	**-**	**7,340,922**	**7,340,922**
Total liabilities, equity and Guarantee fund	**55,662**	**440,712**	**3,333,285**	**2,189,453**	**7,159,099**	**8,834,652**	**22,012,863**
Net assets/liabilities (1) – (2)	**2,560,906**	**3,449,480**	**1,287,403**	**2,205,698**	**(1,139,844)**	**(8,363,643)**	**-**

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest risk (continued)

Group 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	27,970	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**

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest risk (continued)

Group 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	-	-	-	-	-	1,162,318	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)**	**-**

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 2011 and 2010 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 2011 and 2010 which may not be indicative for the positions in other periods.

Bank 2011	**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	-	-	-	-	-	267,219	267,219
Deposits with other banks	29,801	4,940	-	-	-	70	34,811
Loans to banks	1,111,199	3,541,833	2,780,935	2,744,984	4,069,218	51,536	14,299,705
Loans to other customers	400,864	343,419	1,808,113	1,650,167	1,948,968	33,186	6,184,717
Assets available for sale	1,073,218	-	-	-	-	8,167	1,081,385
Investments in subsidiaries	-	-	-	-	-	-	-
Investments in associates	-	-	-	-	-	19,125	19,125
Property, plant and equipment and intangible assets	-	-	-	-	-	68,106	68,106
Non-current assets held for sale	-	-	-	-	-	34,432	34,432
Other assets	-	-	-	-	-	3,424	3,424
Total assets (1)	**2,615,082**	**3,890,192**	**4,589,048**	**4,395,151**	**6,018,186**	**485,265**	**21,992,924**

31. Risk management (continued)

31.4. Market risk (continued)

31.4.1. Interest rate risk (continued)

Bank 2011	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	6	13	63	69	-	154,092	154,243
Borrowings	55,656	440,699	1,089,816	1,737,799	4,831,485	41,908	8,197,363
Bonds payable	-	-	2,243,406	451,585	2,327,614	122,119	5,144,724
Other liabilities	-	-	-	-	-	1,172,353	1,172,353
Total liabilities	**55,662**	**440,712**	**3,333,285**	**2,189,453**	**7,159,099**	**1,490,472**	**14,668,683**
Equity							
Founder's capital	-	-	-	-	-	5,343,739	5,343,739
Retained earnings and reserves	-	-	-	-	-	1,836,924	1,836,924
Other reserves	-	-	-	-	-	(16,812)	(16,812)
Net profit for the year	-	-	-	-	-	148,060	148,060
Total Equity	**-**	**-**	**-**	**-**	**-**	**7,311,911**	**7,311,911**
Guarantee fund	-	-	-	-	-	12,330	12,330
Total equity and Guarantee fund	**-**	**-**	**-**	**-**	**-**	**7,324,241**	**7,324,241**
Total liabilities, equity and Guarantee fund	**55,662**	**440,712**	**3,333,285**	**2,189,453**	**7,159,099**	**8,814,713**	**21,992,924**
Net assets/liabilities (1) – (2)	**2,559,420**	**3,449,480**	**1,255,763**	**2,205,698**	**(1,140,913)**	**(8,329,448)**	**-**

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
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**

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)

Sensitivity analysis

Assumptions used in preparing the interest risk sensitivity analysis relate to possible changes in reference interest rates in order to assess the hypothetical effect on HBOR's profit.

Volatility of reference interest rates for 2011 has been determined using the standard deviation method on the daily changes of the reference interest rates linked to EUR. On the basis of the above volatility, possible changes in reference interest rates linked to EUR have been established and used in the sensitivity analysis.

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 2011	Effect on profit in 2011	Increase in b.p. in 2010	Effect on profit in 2010
		HRK '000		HRK '000
EUR	+50	7,526	+17	2,352
USD	-	-	+34	16

Currency	Decrease in b.p. in 2011	Effect on profit in 2011	Decrease in b.p. in 2010	Effect on profit in 2010
		HRK '000		HRK '000
EUR	-50	(7,526)	-17	(2,352)
USD	-	-	-34	(16)

* *Sensitivity analysis has not been performed for the items with reference interest rates linked to USD since such items are not a constituent element of the Bank's assets and liabilities as of 31 December 2011.*

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/conclusions of the Managing Board and the Asset and liabilities management committee.

Currency risk management procedures determine: methods for the measurement/assessment, monitoring and management of this risk, limits and proceedings both in cases indicating to a crisis and in crisis conditions as well as reports necessary for comprehensive perception of currency risk.

The Bank monitors open foreign currency positions when assessing currency risk exposure. A report on open foreign currency positions is generated on a daily basis and, in addition to the daily monitoring; the projections of their developments are also prepared. For the measurement/assessment of currency risk, the Bank uses VaR model and the bodies in charge report on maximum possible losses on significant currencies regularly. The currency risk is monitored through prescribed limits of currency risk exposure.

The Bank performs stress tests on profits under the assumption of extensive appreciation/depreciation of HRK against significant currencies and reports on test results to the ALCO and the Managing Board.

31. Risk management (continued)

31.4. Market risk (continued)

31.4.2. Currency risk (continued)

Total assets and liabilities as of 31 December 2011 and 31 December 2010 in HRK and foreign currencies can be shown as follows:

Group **2011**	**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	375	113,383	1,382	115,140	152,583	267,723
Deposits with other banks	14,981	221	-	15,202	52,175	67,377
Loans to banks	-	9,243,340	-	9,243,340	5,056,365	14,299,705
Loans to other customers	34,349	3,137,532	-	3,171,881	3,012,836	6,184,717
Financial assets at fair value through profit or loss	-	93	-	93	426	519
Assets available for sale	-	333,027	-	333,027	750,440	1,083,467
Assets held to maturity	-	1,069	-	1,069	23	1,092
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	68,401	68,401
Non-current assets held for sale	-	-	-	-	34,432	34,432
Other assets	-	235	-	235	5,195	5,430
Total assets (1)	**49,705**	**12,828,900**	**1,382**	**12,879,987**	**9,132,876***	**22,012,863**
Liabilities						
Deposits	21,407	3,890	37	25,334	128,909	154,243
Borrowings	-	6,237,961	-	6,237,961	1,959,402	8,197,363
Bonds payable	-	5,144,724	-	5,144,724	-	5,144,724
Other liabilities	2,293	5,194	5	7,492	1,168,119	1,175,611
Total liabilities	**23,700**	**11,391,769**	**42**	**11,415,511**	**3,256,430**	**14,671,941**
Equity						
Founder's capital	-	-	-	-	5,343,739	5,343,739
Retained earnings and reserves	-	-	-	-	1,836,565	1,836,565
Other reserves	-	-	-	-	(16,813)	(16,813)
Net profit for the year	-	-	-	-	147,626	147,626
Total equity attributable to equity holders of the parent	**-**	**-**	**-**	**-**	**7,311,117**	**7,311,117**
Non-controlling interests	-	-	-	-	17,475	17,475
Total Equity	**-**	**-**	**-**	**-**	**7,328,592**	**7,328,592**
Guarantee fund	-	12,330	-	12,330	-	12,330
Total equity and Guarantee fund	**-**	**12,330**	**-**	**12,330**	**7,328,592**	**7,340,922**
Total liabilities, equity and Guarantee fund (2)	**23,700**	**11,404,099**	**42**	**11,427,841**	**10,585,022**	**22,012,863**
Net assets/liabilities (1) – (2)	**26,005**	**1,424,801**	**1,340**	**1,452,146**	**(1,452,146)**	**-**

** Amounts linked to a to one-way currency clause represent HRK 1,243,189 thousand.*

31. Risk management (continued)

31.4. Market risk (continued)

31.4.2. Currency risk (continued)

Total assets and liabilities as of 31 December 2011 and 31 December 2010 in HRK and foreign currencies can be shown as follows (continued):

Group 2010	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	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.*

31. Risk management (continued)

31.4. Market risk (continued)

31.4.2. Currency risk (continued)

Total assets and liabilities as of 31 December 2011 and 31 December 2010 in HRK and foreign currencies can be shown as follows (continued):

Bank **2011**	**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	375	113,383	1,382	115,140	152,079	267,219
Deposits with other banks	14,981	-	-	14,981	19,830	34,811
Loans to banks	-	9,243,340	-	9,243,340	5,056,365	14,299,705
Loans to other customers	34,349	3,137,532	-	3,171,881	3,012,836	6,184,717
Assets available for sale	-	331,475	-	331,475	749,910	1,081,385
Investments in subsidiaries	-	-	-	-	19,125	19,125
Investments in associates	-	-	-	-	-	-
Property, plant and equipment and intangible assets	-	-	-	-	68,106	68,106
Non-current assets held for sale	-	-	-	-	34,432	34,432
Other assets	-	192	-	192	3,232	3,424
Total assets (1)	**49,705**	**12,825,922**	**1,382**	**12,877,009**	**9,115,915***	**21,992,924**
Liabilities						
Deposits	21,407	3,890	37	25,334	128,909	154,243
Borrowings	-	6,237,961	-	6,237,961	1,959,402	8,197,363
Bonds payable	-	5,144,724	-	5,144,724	-	5,144,724
Other liabilities	2,293	3,882	-	6,175	1,166,178	1,172,353
Total liabilities	**23,700**	**11,390,457**	**37**	**11,414,194**	**3,254,489**	**14,668,683**
Equity						
Founder's capital	-	-	-	-	5,343,739	5,343,739
Retained earnings and reserves	-	-	-	-	1,836,924	1,836,924
Other reserves	-	-	-	-	(16,812)	(16,812)
Net profit for the year	-	-	-	-	148,060	148,060
Total Equity	**-**	**-**	**-**	**-**	**7,311,911**	**7,311,911**
Guarantee fund	-	12,330	-	12,330	-	12,330
Total equity and Guarantee fund	**-**	**12,330**	**-**	**12,330**	**7,311,911**	**7,324,241**
Total liabilities, equity and Guarantee fund (2)	**23,700**	**11,402,787**	**37**	**11,426,524**	**10,566,400**	**21,992,924**
Net assets/liabilities (1) – (2)	**26,005**	**1,423,135**	**1,345**	**1,450,485**	**(1,450,485)**	**-**

** Amounts linked to a to one-way currency clause represent HRK 1,243,189 thousand.*

31. Risk management (continued)

31.4. Market risk (continued)

31.4.2. Currency risk (continued)

Total assets and liabilities as of 31 December 2011 and 31 December 2010 in HRK and foreign currencies can be shown as follows (continued):

Bank **2010**	**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	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)

Sensitivity analysis

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

An assumption of reasonably possible fluctuations in EUR exchange rates against HRK was used in the foreign currency risk sensitivity analysis, with the other variables remaining stable, in order to assess the hypothetical effect on HBOR's profit as of 31 December 2011.

Volatility of the exchange rate EUR/HRK, determined using the standard deviation method on the monthly changes of the foreign exchange rate EUR/HRK, equalled 1.6% in 2011 (2010: 2.1%).

The effect of the assumed changes in the foreign exchange rate EUR/HRK by asset and liability items denominated or indexed to EUR on HBOR's profits is stated below.

	Change in currency rate in % 2011	Effect on profit in 2011 HRK' 000	Change in currency rate in % 2010	Effect on profit in 2010 HRK' 000
EUR	+1.6	44,339	+2.1	31,784
USD	-	-	+14.6	9,707
EUR	-1.6	(26,137)	-2.1	(22,410)
USD	-	-	-14.6	(9,707)

**Sensitivity analysis has not been performed for the asset and liability items denominated or indexed to USD since USD is no longer considered to be a significant currency of the Bank as of 31 December 2011.*

31.5. Operational risk

Operational risk is the risk of loss arising from inadequate internal processes, people and systems or external events, legal risk included. HBOR seeks to minimize operational risk by implementing controls in operating processes and by building a unique and comprehensive IT system. HBOR 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 system performance 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 arising from IT system utilisation, HBOR has established a function for analysis and control of IT system security.

Due to the presence of operational risk in all business activities, HBOR in 2011 launched a procedure of public procurement of a complete solution for the introduction of operational risk management framework together with the appropriate IT support.

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 2011 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 analysed 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 instruments 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 instruments' value from the regulated capital market, and if the latest price is not available, the concluding price will be taken for evaluation.

The evaluation of fair value of financial instruments is performed as follows:

- For equity instruments, the Zagreb Stock Exchange (ZSE) closing market price for the last working day of the month, and if the above has not been published, the last realized price before the last working day of the month for which the revaluation is done.
- For bonds of the Ministry of Finance of the Republic of Croatia issued in the domestic market, bid price of instruments quoted on the ZG-Fixing on the last working day of the month will be used. If the above is not available, the concluding price of instruments realized at ZSE on the last working day of the month will be used, and if neither of the above are available, the closing price per institutional transaction will be used. 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.
- For Croatian Securities issued abroad (i.e. Eurobonds) and for all other foreign issuers' securities, or securities issued outside of the Republic of Croatia, bid price for a security quoted at the adequate Bloomberg site on the last working day of the month will be used for evaluation purposes.

32. Fair value of financial instruments (continued)

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

- Fair value of treasury bills of the Ministry of Finance of the Republic of Croatia and of the Croatian National Bank with the remaining maturity period over 90 days is calculated based on the yield achieved at the last auction of treasury bills of the Ministry of Finance of the Republic of Croatia held before the last working day of the month for which the revaluation is made. Yields are calculated by linear interpolation for the time period of the remaining maturity of instruments. Fair value of treasury bills of the Ministry of Finance of the Republic of Croatia and of the Croatian National Bank with the remaining maturity under 91 days is calculated based on the linear interpolation of ZIBOR interest rate set on the last business day of each month.

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.

In case of evaluation of fair value for shares in investment funds (cash funds), the price of shares in the fund on a particular day is acquired from the investment fund management company.

The Bank has chosen to present comparative information for both reporting and prior period.

32. Fair value of financial instruments (continued)

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

Group			2011 HRK '000			2010 HRK '000
	Level 1	Level 2	Level 3	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	519	-	-	500	-	-
Total financial assets at fair value through profit or loss	**519**	**-**	**-**	**500**	**-**	**-**
Assets available for sale:						
Debt instruments:						
Listed debt instruments:						
Bonds of the Ministry of Finance of the Republic of Croatia	332,546	-	-	131,618	-	-
Treasury bills of the Ministry of Finance of the Republic of Croatia	728,748	-	-	39,966	-	-
Accrued interest	8,188	-	-	1,970	-	-
Total debt instruments	**1,069,482**	**-**	**-**	**173,554**	**-**	**-**
Equity instruments:						
Investment in shares of foreign companies	-	25	-	-	23	-
Investment in financial institutions shares	-	161	-	-	161	-
Shares of foreign financial institutions – EIF	-	12,721	-	-	12,921	-
Corporate shares	-	-	-	-	-	-
Total equity instruments	**-**	**12,907**	**-**	**-**	**13,105**	**-**
Investments in investment funds:						
Shares classified as assets available for sale	1,078	-	-	1,051	-	-
Total investments in investment funds	**1,078**	**-**	**-**	**1,051**	**-**	**-**
Total assets available for sale	**1,070,560**	**12,907**	**-**	**174,605**	**13,105**	**-**
Assets held to maturity:						
Debt instruments:						
Bonds of the Ministry of Finance of the Republic of Croatia	1,069	-	-	1,055	-	-
Accrued interest	23	-	-	22	-	-
Total assets held to maturity	**1,092**	**-**	**-**	**1,077**	**-**	**-**

32. Fair value of financial instruments (continued)

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

Bank			2011 HRK '000			2010 HRK '000
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Assets available for sale						
Debt instruments:						
Listed debt instruments:						
Bonds of the Ministry of Finance of the Republic of Croatia	331,563	-	-	131,618	-	-
Treasury bills of the Ministry of finance of the Republic of Croatia	728,748	-	-	39,966	-	-
Accrued interest	8,167	-	-	1,970	-	-
Total debt instruments	**1,068,478**	**-**	**-**	**173,554**	**-**	**-**
Equity instruments:						
Investment in shares of foreign companies	-	25	-	-	23	-
Investment in financial institutions shares	-	161	-	-	161	-
Shares of foreign financial institutions – EIF	-	12,721	-	-	12,921	-
Corporate shares	-	-	-	-	-	-
Total equity instruments	**-**	**12,907**	**-**	**-**	**13,105**	**-**
Total assets available for sale	**1,068,478**	**12,907**	**-**	**173,554**	**13,105**	**-**

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. Reporting by segments

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.

Assets and liabilities by segments are presented in net terms, i.e. gross after impairment and provisioning, and before the effect of mitigation through 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)

2011	Banking activities HRK '000	Insurance activities HRK '000	Other activities HRK '000	Unallocated HRK '000	Total HRK '000
Net interest income	332,313	1,538	11	-	333,862
Net fee income	11,011	858	514	(5)	12,378
Net income from financial operations	44,351	52	19	-	44,422
Net premiums earned	-	1,248	-	-	1,248
Other income	1,007	76	-	(61)	1,022
Income from operating activities	**388,682**	**3,772**	**544**	**(66)**	**392,932**
Operating costs	(94,756)	(3,658)	(641)	66	(98,989)
Impairment loss and provisions	(145,866)	(38)	(42)	-	(145,946)
Expenses for insured cases and changes	-	(230)	-	-	(230)
Net change in provisions	-	(894)	-	-	(894)
Net expenses from financial operations	-	-	-	-	-
Other expenses	-	(35)	-	-	(35)
Operating expenses	**(240,622)**	**(4,855)**	**(683)**	**66**	**(246,094)**
Profit/(loss) before income tax	**148,060**	**(1,083)**	**(139)**	**-**	**146,838**
Income tax	-	227	25	-	252
Profit/(loss) for the year	**148,060**	**(856)**	**(114)**	**-**	**147,090**
Assets of segment	21,992,924	39,172	1,922	(21,155)	22,012,863
Total assets	**21,992,924**	**39,172**	**1,922**	**(21,155)**	**22,012,863**
Liabilities of segment	14,668,683	3,214	67	(23)	14,671,941
Total equity and guarantee fund	7,324,241	(1,542)	(145)	18,368	7,340,922
Total liabilities, equity and guarantee fund	**21,992,924**	**1,672**	**(78)**	**18,345**	**22,012,863**

Intra-group transactions are presented under "Unallocated".

33. Reporting by segments (continued)

2010	Banking activities HRK '000	Insurance activities HRK '000	Other activities HRK '000	Unallocated HRK '000	Total HRK '000
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)	(1,816)	(64)	(3)	(87,988)
Impairment loss and provisions	(110,256)	(100)	-	-	(110,356)
Expenses for insured cases and changes	-	-	-	-	-
Net change in provisions	-	(126)	-	-	(126)
Net expenses from financial operations	-	-	-	-	-
Other expenses	-	-	-	-	-
Operating expenses	**(196,361)**	**(2,042)**	**(64)**	**(3)**	**(198,470)**
Profit/(loss) before income tax	**117,962**	**(848)**	**(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 core capital (Tier 1) and supplementary 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.

	Group		Bank	
	2011	**2010**	**2011**	**2010**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**
Core capital – Tier 1	7,327,752	6,999,942	7,328,722	7,000,662
Supplementary capital – Tier 2	255,504	272,252	255,504	272,252
Total liable capital	**7,583,256**	**7,272,194**	**7,584,226**	**7,272,914**
Risk weighted assets	9,123,408	8,935,610	9,133,539	8,946,342
Capital requirements for currency risk	2,822,529	2,509,388	2,819,899	2,507,459
Total capital requirements	**11,945,937**	**11,444,998**	**11,953,438**	**11,453,801**
	%	**%**	**%**	**%**
Capital ratio (Tier 1)	**61.34**	**61.16**	**61.31**	**61.12**
Capital adequacy ratio	**63.48**	**63.54**	**63.45**	**63.50**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**
Liable capital needed for ensuring capital adequacy according to regulatory requirements	**1,433,512**	**1,373,400**	**1,434,413**	**1,374,456**

Minimum capital adequacy ratio at the end of 2011 was 12% as well as in 2010. 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 method 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 prolonged a transitional period for the implementation and testing of new applications until the end of 2012. 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 2011 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. Bankruptcy proceedings for Credo banka d.d.

On 16th January 2012, the Commercial Court in Split, issued a decision on opening bankruptcy proceedings against the debtor, Credo banka d.d. under involuntary liquidation proceedings Split. As at 31st December 2011, HBOR's total gross receivables from the debtor-bank accounted for 0.6% of its total gross portfolio, before provisioning.

In accordance with the provisions of the interbank loan contract concluded between the Bank and the debtor-bank, in case of debtor-bank's insolvency or threat of bankruptcy, even if the above is not determined by court decision, delay or default on its obligations pursuant to the interbank loan contract and bankruptcy proceedings or liquidation of the debtor-bank, the Bank may notify the debtor bank, by delivery of a written unilateral notification, that as of the receipt of notification, the assignment of claims shall have the effect of assignment of claims instead of performance. Starting from the moment when cession takes effect of assignment of claims instead of performance, the final borrower carries on the obligation to make all payments pursuant to the ceded claims directly to HBOR. The final borrower will be informed in writing by the debtor-bank and HBOR about the change in the effect of cession.

Reconciliation of balances and review of relevant loan documentation in order to assume direct creditor-debtor relations with final borrowers is underway. Consequently, HBOR's existing exposure to the commercial bank will be allocated to direct borrowers.