Intesa Sanpaolo Banka d.d. Bosna i Hercegovina

Financial statements for the year ended
31 December 2009
and Independent auditors' report

Contents

Responsibility for the Financial Statements

Pursuant to the Law on Accounting and Audit of Federation of Bosnia and Herzegovina (Official Gazette No. 32/05), the Management Board is responsible for ensuring that financial statements are prepared for each financial year in accordance with accounting regulations applicable to financial reporting of banks in the Federation of Bosnia & Herzegovina, which give a true and fair view of the state of affairs and results of the Intesa Sanpaolo Banka Bosna and Hercegovina d.d. for that period.

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

In preparing those financial statements, the responsibilities of the Management 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, subject to any material departures disclosed and explained in the financial statements; and
- the financial statements are prepared on the going concern basis unless it is inappropriate to presume that the Bank will continue in business.

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

Signed on behalf of the Management Board

Almir Krkalić, Director
Intesa Sanpaolo banka d.d. Bosna i Hercegovina
Obala Kulina bana 9a
71000 Sarajevo
Bosnia and Herzegovina

8 February 2010

Revsar d.o.o., Sarajevo **Ernst & Young Beograd d.o.o., Beograd**

INDEPENDENT AUDITORS' REPORT

To the shareholders of Intesa Sanpaolo Banka d.d. Bosna i Hercegovina:

We have audited the accompanying financial statements of Intesa Sanpaolo Banka d.d. Bosna i Hercegovina (the "Bank"), which comprise of the statement of financial position as of 31 December 2009, and the 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.

Management's responsibility for the financial statements

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

Auditor's responsibility

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

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

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Intesa Sanpaolo Banka d.d. Bosna i Hercegovina as of 31 December 2009, and its financial performance and its cash flows for the year then ended in accordance with accounting regulations applicable to financial reporting of banks in the Federation of Bosnia & Herzegovina.

Sarajevo, 8 February 2010

Alma Malinović
Certified Auditor
Revsar d.o.o., Sarajevo

DRUŠTVO ZA REVIZIJU »REVSAR« d.o.o. SARAJEVO

Belgrade, 8 February 2010

Mirjana Perendija Kovačević
Partner
Ernst & Young Beograd d.o.o.

(all amounts are expressed in thousands of KM)

	Notes	31 December 2009	31 December 2008
Interest income	5	66,556	62,404
Interest expense	6	(25,031)	(26,777)
Net interest income		**41,525**	**35,627**
Fee and commission income	7	11,507	10,585
Fee and commission expense	8	(2,784)	(2,784)
Net fee and commission income		**8,723**	**7,801**
Net trading income	9	878	1,745
Other operating income	10	1,380	4,825
Operating income		**2,258**	**6,570**
Personnel Expenses	12	(17,381)	(16,805)
Administrative expenses	13	(15,970)	(15,619)
Depreciation of tangible fixed assets	23	(4,240)	(3,562)
Operating Expense		**(37,591)**	**(35,986)**
PROFIT BEFORE IMPAIRMENT LOSSES, PROVISIONS AND INCOME TAX		**14,915**	**14,012**
Impairment losses and provisions	14	(14,739)	(15,220)
Recoveries of written off loans	11	3,842	4,911
PROFIT BEFORE INCOME TAX		**4,018**	**3,703**
Income tax	15	(527)	(912)
NET PROFIT FOR THE YEAR		**3,491**	**2,791**
Earnings per share (KM)	16	**7.71**	**7.47**

The accompanying notes form an integral part of these financial statements.

Approved by and signed on behalf of Intesa Sanpaolo Banka d.d. Bosna i Hercegovina on 8 February 2010:

Almir Krkalić
Director

Livio Mannoni
Executive Director of Finance

(all amounts are expressed in thousands of KM)

	31 December 2009	31 December 2008
Profit for the year	3,491	2,791
Other comprehensive income for the year		
Net (losses)/gains on financial assets available for sale:		
Gains arising during the year	41	266
Reclassification adjustments for gains included in the statement of income	(305)	-
Income tax relating to items of other comprehensive income	28	(24)
Total comprehensive income for the year, net of tax	3,255	3,033

The accompanying notes form an integral part of these financial statements.

Approved by and signed on behalf of Intesa Sanpaolo Banka d.d. Bosna i Hercegovina
on 8 February 2010:

Almir Krkalić
Director

Livio Mannoni
Executive Director of Finance

(all amounts are expressed in thousands of KM)

	Notes	31 December 2009	31 December 2008
ASSETS			
Cash and cash equivalents	17	100,503	26,805
Obligatory reserve with the Central Bank	18	88,772	116,696
Placements with other banks	19	134,678	105,459
Loans and receivables	20	798,795	727,146
Assets available for sale	21	542	801
Other assets	22	7,968	6,887
Property, plant and equipment	23	28,360	27,682
TOTAL ASSETS		**1,159,618**	**1,011,476**
LIABILITIES			
Due to banks and other institutions	24	361,270	332,384
Subordinated debt	25	1,404	11,356
Due to customers	26	662,741	534,381
Financial liabilities held for trading	27	761	-
Provisions for contingent liabilities and commitments	30	2,709	3,027
Other liabilities	28	5,537	6,126
Other provisions	29	2,046	1,840
TOTAL LIABILITIES		**1,036,468**	**889,114**
SHAREHOLDERS' EQUITY			
Share capital		45,296	45,296
Reserves and retained earnings		77,854	77,066
TOTAL SHAREHOLDER'S EQUITY		**123,150**	**122,362**
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		**1,159,618**	**1,011,476**
FINANCIAL COMMITMENTS AND CONTINGENCIES	30	120,332	127,885

The accompanying notes form an integral part of these financial statements.

Approved by and signed on behalf of Intesa Sanpaolo Banka d.d. Bosna i Hercegovina on 8 February 2010:

Almir Krkalić	Livio Mannoni
Director	Executive Director of Finance

Intesa Sanpaolo Banka, d.d. BiH
Statement of cash flows for the year ended 31 December 2009
(all amounts are expressed in thousands of KM)

	2009	2008
Operating activities		
Net Income	3,491	2,791
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	4,240	3,562
Impairment losses and provisions	14,739	15,220
Changes in other provisions, net	280	(60)
(Gain) / loss sale or disposal of property, plant and equipment	(343)	(1,074)
Changes in operating assets and liabilities:		
Net decrease in due from Central Bank	27,924	15,326
Net increase in placements with other banks, before impairment losses	(29,224)	(15,388)
Net increase in loans and receivables, before impairment losses	(85,777)	(200,593)
Net (increase)/decrease in other assets, before impairment losses	(2,010)	14
Net increase due to banks	4,885	61,660
Net increase in demand and term deposits	128,360	(125,065)
Net increase in other liabilities	98	(467)
NET CASH FROM/(USED IN) OPERATING ACTIVITIES	**66,663**	**(244,074)**
Investing Activities		
Net increase in assets available for sale, before impairment losses	28	734
Net purchases of property and equipment	(5,416)	(7,287)
Proceeds from sale of property, plant and equipment	841	1,812
NET CASH USED IN INVESTING ACTIVITIES	**(4,547)**	**(4,741)**
Financing Activities		
Net proceeds from borrowings	24,001	86,960
Net repayments of subordinated debt	(9,952)	(5,377)
Increase in share capital purchase of treasury shares	-	39,116
(Purchase)/sale of treasury shares	(2,467)	12
NET CASH PROVIDED BY FINANCING ACTIVITIES	**11,582**	**120,711**
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS	**73,698**	**(128,104)**
CASH AND CASH EQUIVALENTS AT 1 JANUARY	**26,805**	**154,909**
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	**100,503**	**26,805**

Operational cash flow from interest and dividends

Interest paid	25,045	26,453
Interest received	61,669	52,504
Dividend received	116	422

The accompanying notes form an integral part of these financial statements.

Approved by and signed on behalf of Intesa Sanpaolo Banka d.d. Bosna i Hercegovina
on 8 February 2010:

Almir Krkalić
Director

Livio Mannoni
Executive Director of Finance

(all amounts are expressed in thousands of KM)

	Share capital	**Treasury shares**	**Share Premium**	**Fair Value reserves**	**Retained earnings and reserves**	**Total**
Balance as at 31 December 2007	37,147	(2)	28,401	115	14,540	80,201
Total comprehensive income	-	-	-	127	2,906	3,033
Increase in share capital	8,149	-	30,967	-	-	39,116
Purchase/Sale of treasury shares	-	2	-	-	10	12
Balance as at 31 December 2008	**45,296**	**-**	**59,368**	**242**	**17,456**	**122,362**
Balance as at 31 December 2008	45,296	-	59,368	242	17,456	122,362
Total comprehensive income	-	-	-	(236)	3,491	3,255
Purchase/Sale of treasury shares	-	(514)	(1,953)	-	-	(2,467)
Balance as at 31 December 2009	**45,296**	**(514)**	**57,415**	**6**	**20,947**	**123,150**

The accompanying notes form an integral part of these financial statements.

Approved by and signed on behalf of Intesa Sanpaolo Banka d.d. Bosna i Hercegovina on 8 February 2010:

Almir Krkalić
Director

Livio Mannoni
Executive Director of Finance

(all amounts are expressed in thousands of KM)

1. GENERAL

History and incorporation

Intesa Sanpaolo Banka d.d. Bosna i Hercegovina, former UPI banka d.d. Sarajevo, Obala Kulina Bana 9a (the "Bank") is registered in Cantonal Court in Sarajevo on 20 October 2000.

The Bank was established in 1972 as an internal bank of the corporate system of the Udružena poljoprivreda, prehrambena industrija i promet (Associated Agriculture and Food Industries and Sales), aimed at supporting the operations of these sectors, which at the time employed more than 35,000 workers. Since 1990, a new phase is coming in the development of the Bank, when it was registered as a shareholding company and it is in a majority state ownership (92 %). The Bank starts with expansion of the network of corporate clients, focusing on the sector of small and medium entrepreneurship. As early as from 2000, through the emission of shares, the Bank was fully transferred into the hand of private capital.

In February 2006, Intesa Sanpaolo Holding International S.A. took over the major share package of UPI Banka d.d. Sarajevo, and became the major owner of the Bank's shares.

On 31 July 2007 LT Gospodarska banka d.d. Sarajevo (the "LTG Bank"), also subsidiary of Intesa Sanpaolo Holding, merged into the Bank, with the effect of the LTG Bank cancellation (without initiation of liquidation process), while the Bank became its legal successor.

On 20 August 2008 the Bank changed its name into Intesa Sanpaolo Banka d.d. Bosna i Hercegovina.

Principal activities of the Bank

The Bank's main operations are as follows:

1. accepting deposits from the public and placing of deposits,
2. providing current and term deposit accounts,
3. granting short-term and long-term loans and guarantees to corporate customers, private individuals, local municipalities and other credit institutions dealing with finance lease and foreign exchange transactions,
4. money market activities,
5. performing local and international payments,
6. foreign currency exchange and other banking-related activities,
7. providing banking services through an extensive branch network in Bosnia and Herzegovina

Supervisory Board

Vojko Čok	Chairman from April 4, 2009
Massimo Pierdicchi	Vice-Chairman from April 4, 2009
Beata Kissne Foldi	Member from April 4, 2009
Ezio Salvai	Chairman until April 4, 2009
Ivan Krolo	Vice-Chairman until April 4, 2009
Giancarlo Miranda	Member until April 4, 2009
Massimo Malagoli	Member
Nora Kocsis	Member

(all amounts are expressed in thousands of KM)

1. GENERAL (continued)

Management Board

Almir Krkalić	Director
Livio Mannoni	Executive Director of Finance
Igor Bilandžija	Executive Director of Risk Management

Audit Committee

Giampiero Trevisan	Chairman
Gianluca Aliverti	Member from February 25, 2009
Cataldo Quatela	Member from April 28, 2009
Armando Sala	Member
Beata Kissne Foldi	Member until February 25, 2009
Alen Galavić	Member until February 25, 2009
Ivanka Petrović	Member

Internal Auditor

Muamera Zuko

The shareholding structure is as follows:

	31 December 2009			31 December 2008		
Shareholders	**No. of shares**	**Amount KM '000**	**%**	**No. of shares**	**Amount KM '000**	**%**
Intesa Sanpaolo Holding International S.A.	391,661	39,166	86.47	382,024	38,202	84.34
European Bank for Reconstruction and Development	32,478	3,248	7.17	32,478	3,248	7.17
Other	28,821	2,882	6.36	38,458	3,846	8.49
Total	**452,960**	**45,296**	**100.00**	**452,960**	**45,296**	**100.00**

1. GENERAL (continued)

All the shares (452,960) are issued and fully paid. Nominal value of one share is 100 KM.

During 2009 the Bank bought back 5,140 ordinary shares from some of the minority shareholders.

The Bank has 60 priority (preference) shares with priority right in receipt of dividends. Also the Bank does not have any shares held by the entity or by its subsidiaries and no share reserved for issue under options and contracts for sale.

In the position of Reserves and retained earnings the Bank includes:

- reserves for undistributed profit from previous years;
- fair value reserves deriving from the revaluation of the AFS investments;
- reserve for tax-deductible profit, in the measure of 15% of Bank's profit according to the then valid Income Tax Law;
- reserve for tax-deductible profit, in the measure of 75% of Bank's profit reinvested into fixed assets;
- reserve for undistributed dividends, following Supervisory Board decisions;
- revaluation reserve for fixed assets, according to valid Law;
- reserve for treasury shares.

2. ADOPTION OF NEW STANDARDS AND REVISED STANDARDS

2.1 Standards and Interpretations effective in the current period

- **IFRS 8 "Operating Segments"** (effective for annual periods beginning on or after 1 January 2009),
- **Amendments to IFRS 4 "Insurance contracts" and IFRS 7 "Financial Instruments: Disclosures"** - Improving disclosures about financial instruments (effective for annual periods beginning on or after 1 January 2009),
- **Amendments to IFRS 1 "First-time Adoption of IFRS" and IAS 27 "Consolidated and Separate Financial Statements"** – Cost of investment in a subsidiary, jointly-controlled entity or associate (effective for annual periods beginning on or after 1 January 2009),
- **Amendments to various standards and interpretations** resulting from the Annual quality improvement project of IFRS published on 22 May 2008 (IAS 1, IFRS 5, IAS 8, IAS 10, IAS 16, IAS 19, IAS 20, IAS 23, IAS 27, IAS 28, IAS 29, IAS 31, IAS 34, IAS 36, IAS 38, IAS 39, IAS 40, IAS 41) primarily with a view to removing inconsistencies and clarifying wording (most amendments are to be applied for annual periods beginning on or after 1 January 2009),
- **Amendments to IAS 32 "Financial Instruments: Presentation" and IAS 1 "Presentation of Financial Statements"** – Puttable financial instruments and obligations arising on liquidation (effective for annual periods beginning on or after 1 January 2009),
- **IAS 1 (revised) "Presentation of Financial Statements"** – A revised presentation (effective for annual periods beginning on or after 1 January 2009),
- **IAS 23 (revised) "Borrowing Costs"** (effective for annual periods beginning on or after 1 January 2009),
- **Amendments to IFRS 2 "Share-based Payment"** – Vesting conditions and cancellations (effective for annual periods beginning on or after 1 January 2009),
- **Amendments to IFRIC 9 "Reassessment of Embedded Derivatives" and IAS 39 "Financial Instruments: Recognition and Measurement"** -Embedded Derivatives (effective for annual periods ending on or after 30 June 2009),
- **IFRIC 13 "Customer Loyalty Programmes"** (effective for annual periods beginning on or after 1 July 2008),
- **IFRIC 15 "Agreements for the Construction of Real Estate"** (effective for annual periods beginning on or after 1 January 2009),
- **IFRIC 16 "Hedges of a Net Investment in a Foreign Operation"** (effective for annual periods beginning on or after 1 October 2008),

The adoption of these amendments to the existing standards and interpretations has not led to any changes in the Bank's accounting policies.

2. ADOPTION OF NEW STANDARDS AND REVISED STANDARDS

2.2 Standards and Interpretations in issue not yet adopted

At the date of authorisation of these financial statements the following standards, revisions and interpretations were in issue but not yet effective:

- **IFRS 9 "Financial Instruments"** (effective for annual periods beginning on or after 1 January 2013),
- **IFRS 1 (revised) "First-time Adoption of IFRS"** (effective for annual periods beginning on or after 1 July 2009),
- **IFRS 3 (revised) "Business Combinations"** (effective for annual periods beginning on or after 1 July 2009),
- **Amendments to IFRS 1 "First-time Adoption of IFRS"**- Additional Exemptions for First-time Adopters (effective for annual periods beginning on or after 1 January 2010),
- **Amendments to IFRS 2 "Share-based Payment"** - Group cash-settled share-based payment transactions (effective for annual periods beginning on or after 1 January 2010),
- **Amendments to IAS 24 "Related Party Disclosures" -** Simplifying the disclosure requirements for government-related entities and clarifying the definition of a related party (effective for annual periods beginning on or after 1 January 2011),
- **Amendments to IAS 27 "Consolidated and Separate Financial Statements"** (effective for annual periods beginning on or after 1 July 2009),
- **Amendments to IAS 32 "Financial Instruments: Presentation"** – Accounting for rights issues (effective for annual periods beginning on or after 1 January 2010)
- **Amendments to IAS 39 "Financial Instruments: Recognition and Measurement"** - Eligible hedged items (effective for annual periods beginning on or after 1 July 2009),
- **Amendments to various standards and interpretations** resulting from the Annual quality improvement project of IFRS published on 16 April 2009 (IFRS 2, IFRS 5, IFRS 8, IAS 1, IAS 7, IAS 17, IAS 18, IAS 36, IAS 38, IAS 39, IFRIC 9, IFRIC 16) primarily with a view to removing inconsistencies and clarifying wording, (most amendments are to be applied for annual periods beginning on or after 1 January 2010),
- **Amendments to IFRIC 14 "IAS 19 — The Limit on a defined benefit Asset, Minimum Funding Requirements and their Interaction" -** Prepayments of a Minimum Funding Requirement (effective for annual periods beginning on or after 1 January 2011),
- **IFRIC 17 "Distributions of Non-Cash Assets to Owners"** (effective for annual periods beginning on or after 1 July 2009),
- **IFRIC 19 "Extinguishing Liabilities with Equity Instruments"** (effective for annual periods beginning on or after 1 July 2010).

The Bank has elected not to adopt these standards, revisions and interpretations in advance of their effective dates. The Bank anticipates that the adoption of these standards, revisions and interpretations will have no material impact on the financial statements of the Bank in the period of initial application.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

These financial statements are prepared in accordance with accounting regulations applicable to financial reporting of banks in the Federation of Bosnia and Herzegovina.

As required by local legislation, the Bank prepares financial statements in accordance with International Financial Reporting Standards (IFRS) as published by the International Accounting Standards Board and as modified by the regulatory requirements prescribed by the Banking Agency of Federation of Bosnia and Herzegovina (FBA).

The financial statements have been prepared on the historical cost basis except for certain non-current assets and financial instruments which are reported at fair value. The principal accounting policies are set out below.

The financial statements are presented in thousands of convertible mark (KM '000) which is the functional currency of the Bank.

The financial statements are prepared on an accrual basis of accounting, under the going concern assumption.

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and their reported amounts of revenues and expenses during the reporting period. These estimates are based on the information available as at the balance sheet date and actual results could differ from those estimates.

The Bank maintains its books of accounts and prepares financial statements for regulatory purposes in accordance with the regulations of the Banking Agency of Federation of Bosnia and Herzegovina (FBA) and Law on Banks of the Federation of Bosnia and Herzegovina.

Interest Income and Expense

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

In accordance with regulations of FBA, the Bank is obligated to remove to off-balance sheet records accrued interest and to suspend recognition of further interest accruals on assets classified as non-performing assets (interest are due and have not been collected for over 90 days after the original maturity date). Such interest accruals are also recorded in off-balance sheet records.

Fee and commission income and expense

Fees and commissions consist mainly of fees earned on domestic and foreign payment transactions, and fees for loans and other credit instruments issued by the Bank.

Fees for payment transactions are recognized in the period when services are rendered.

Loan origination fees, after approval and drawdown of loans, are deferred (together with related direct costs) and recognized as an adjustment to the effective yield of the loan over its life.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Employee benefits

On behalf of its employees, the Bank pays pension and health insurance on and from salaries, which are calculated on the gross salary paid, as well as taxes, which are calculated on the net salary paid. The Bank is paying the above contributions into the Pension and Health Fund of the entities, as per the set legal rates during the course of the year on the gross salary paid. In addition, meal allowances, transport allowances and vacation bonuses are paid in accordance with the local legislation. These expenses are recorded in the income statement in the period in which the salary expense is incurred.

Retirement severance payments

According to the local legislation and internal Rulebook on employment, the Bank makes retirement severance payments of minimum 3 average monthly salaries of the employee in question or 3 average salaries of the Federation of Bosnia and Herzegovina paid in the period of the last three months, depending on what is more favourable to the employee.

Provision for retirement benefits is calculated by independent actuary. The liability recognized in the balance sheet is the present value of the obligation, determined by discounting estimated future outflows using the projected unit credit method. Actuarial gains and losses are recognized in income statement in the period in which they arise.

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax expense is based on taxable income for the year. Taxable income differs from net income as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Bank's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax basis used in the computation of taxable profit, and is accounted for using the balance sheet liability method.

Deferred tax liabilities are generally recognized for all taxable temporary differences and deferred tax assets are recognized to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilized.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the asset to be recovered. Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realized. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the Bank has the ability and intention to settle on a net basis.

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

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Cash and cash equivalents

For the purpose of reporting cash flows, cash and cash equivalents are defined as cash, balances with the Central Bank ("CBBH") and current accounts with other banks.

Cash and cash equivalents excludes the compulsory minimum reserve with the Central Bank as these funds are not available for the Bank's day to day operations. The compulsory minimum reserve with the CBBH is a required reserve to be held by all commercial banks licensed in Bosnia and Herzegovina.

Financial assets

Financial assets are recognized and derecognized on a trade date where the purchase or sale of an investment is under a contract whose terms require delivery of the instrument within the timeframe established by the market concerned, and are initially measured at fair value, net of transaction costs, except for those financial assets classified as at fair value through profit or loss, which are initially measured at fair value.

Financial assets are classified into the following specified categories: financial assets as 'at fair value through profit or loss' (FVTPL), 'held-to-maturity investments', 'available-for-sale' (AFS) financial assets and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Financial assets at FVTPL

Financial assets are classified as at FVTPL where the financial asset is either held for trading or it is designated as at FVTPL.

A financial asset is classified as held-for-trading if:

- it has been acquired principally for the purpose of selling in the near future; or
- it is a part of an identified portfolio of financial instruments that the Bank manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

A financial asset other than a financial asset held for trading may be designated as at FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial asset forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Bank's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- It forms part of a contract containing one or more embedded derivatives, and IAS 39 permits the entire combined contract (asset or liability) to be designated as at FVTPL

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial assets (continued)

Financial assets at FVTPL are stated at fair value, with any resultant gain or loss recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any dividend or interest earned on the financial asset.

The fair values of financial assets and financial liabilities are determined as follows:

- the fair value of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market prices or dealer price quotation (bid price for long position and ask price for short position), without any deduction for transaction costs (so called 'first level' of fair value);
- the fair value of other financial assets and financial liabilities (excluding derivative instruments) are determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions (so called ' second level' of fair value which uses only insignificant adjustments to the market inputs);
- the fair value of derivative instruments, are calculated using quoted prices. Where such prices are not available use is made of discounted cash flow analysis using the applicable yield curve for the duration of the instruments for non-optional derivatives, and option pricing models for optional derivatives (so called 'second level' of fair value'), and
- Certain financial instruments are recorded at fair value using valuation techniques in which current market transactions or observable market data are not available. Their fair value is determined from input not directly visible on the market or prices of similar assets or deduced from non-active markets that are subject to significant adjustments (so called "third level" of fair value)

Financial liabilities are classified into the following specified categories: financial liabilities 'at fair value through profit or loss' (FVTPL), or "other financial liabilities".

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset or, where appropriate, a shorter period.

AFS financial assets

Unlisted shares are classified as being AFS and are stated at fair value. Gains and losses arising from changes in fair value are recognised directly in equity in the investments revaluation reserve with the exception of impairment losses, interest calculated using the effective interest method and foreign exchange gains and losses on monetary assets, which are recognised directly in profit or loss. Where the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously recognised in the investments revaluation reserve is included in profit or loss for the period.

Dividends on AFS equity instruments are recognised in profit or loss when the Bank's right to receive the dividends is established.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial assets (continued)

Loans and receivables

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

Loan and receivables are measured at initial recognition at fair value, and are subsequently measured at amortised cost using the effective interest method, less any allowance for impairment. Third party expenses, such as legal fees, incurred in securing a loan are treated as part of the cost of the transaction as well as fees received from customers.

Impairment of financial assets and provisions for contingent liabilities and commitments

According to the Federal Banking Agency requirements, the Bank classifies loans, other receivables, as well as contingent liabilities and commitments into the following categories:

A – Performing assets;
B – Special mention;
C – Substandard;
D – Doubtful loan and
E – Loss.

The classification into one of the above mentioned categories depends from credit standing of the Borrower, timely performance or repayment, type of collaterals obtained and days of default in servicing the loan.

For loans, receivables and off-balance sheet exposures classified as performing, a general allowance/provision equal to 2% of the outstanding exposure is made.

For exposures classified into categories from B to D the following range of provision apply:

B – Special mention	from 5 to 15%
C – Substandard	from 15 to 40%
D – Doubtful	from 41 to 60%
E – Loss	100%

Assets regarded as non-collectable are classified into category "E" written-off against the related allowance for impairment and recorded off-balance sheet. Subsequent recoveries are credited to “Collected write offs” in income statement.

Derecognition of financial assets

The Bank derecognises a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Bank neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Bank recognises its retained interest in the asset and an associated liability for amounts it may have to pay. In addition, the Bank derecognises financial assets when they are classified in the category E in accordance with the Federal Banking Agency requirements as described above.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial liabilities and equity instruments issued by the Bank

Classification as debt or equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

Equity instruments

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Bank are recorded at the proceeds received, net of direct issue costs.

Compound instruments

The component parts of compound instruments issued by the Bank are classified separately as financial liabilities and equity in accordance with the substance of the contractual arrangement. At the date of issue, the fair value of the liability component is estimated using the prevailing market interest rate for a similar non-convertible instrument. This amount is recorded as a liability on an amortised cost basis using the effective interest method until extinguished upon conversion or at the instrument's maturity date. The equity component is determined by deducting the amount of the liability component from the fair value of the compound instrument as a whole. This is recognised and included in equity, net of income tax effects, and is not subsequently remeasured.

Financial liabilities

Financial liabilities are classified as either financial liabilities "at FVTPL" or "other financial liabilities".

Financial liabilities at FVTPL

Financial liabilities are classified as at FVTPL where the financial liability is either held for trading or it is designated as at FVTPL.

A financial liability is classified as held for trading if:

- it has been incurred principally for the purpose of repurchasing in the near future; or
- it is a part of an identified portfolio of financial instruments that the Bank manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

A financial liability other than a financial liability held for trading may be designated as at FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial liability forms part of a Bank's portfolio of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Bank's documented risk management or investment strategy, and information about the Bank is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IAS 39 *Financial Instruments: Recognition and Measurement* permits the entire combined contract (asset or liability) to be designated as at FVTPL.

(all amounts are expressed in thousands of KM)

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial liabilities and equity instruments issued by the Bank (continued)

Financial liabilities at FVTPL (continued)

Financial liabilities at FVTPL are stated at fair value, with any resultant gain or loss recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any interest paid on the financial liability.

Fair value is determined in the manner described in notes 4 and 31.

Other financial liabilities

Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability or, where appropriate, a shorter period.

Derecognition of financial liabilities

The Bank derecognizes financial liabilities when, and only when, the Bank's obligations are discharged, cancelled or they expire.

Property and equipment

Property and equipment are stated at cost less accumulated depreciation and accumulated impairment losses, if any. Cost includes the purchase price and directly associated cost of bringing the asset to a working condition for its intended use. Maintenance and repairs, replacements and improvements of minor importance are expensed as incurred. Significant improvements and replacement of assets are capitalised. Gains or losses on the retirement or disposal of property and equipment are included in the statement of income in the period in which they occur.

Properties in the course of construction are carried at cost, less impairment loss, if any. Depreciation commences when the assets are ready for their intended use. Depreciation is calculated on a straight-line basis over the estimated useful life of the applicable assets and based upon the application of the following annual percentages to historical costs:

	31 December 2009	31 December 2008
Buildings	1.30%	1.30%
Furniture and other equipment	10.00% - 20.00%	10.00% - 20.00%
Computers	20.00%	20.00%
Leasehold improvements	20.00%	20.00%
Software	20.00%	20.00%

Property and equipment is derecognised on disposal or when no future economic benefits are expected from its use. Any gain or loss on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is recognised in 'Other operating income' in the income statement in the year the asset is derecognised.

(all amounts are expressed in thousands of KM)

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Foreign currency translation

Transactions in currencies other than Bosnia and Herzegovina KM are initially recorded at the rates of exchange prevailing on the dates of the transactions. Monetary assets and liabilities are translated at the rates prevailing on the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated. Profits and losses arising on translation are included in the statement of income for the period.

The Bank values its assets and liabilities by middle rate of Central Bank of Bosnia and Herzegovina valid at the date of balance sheet. The principal rates of exchange set forth by the Central Bank and used in the preparation of the Bank's balance sheet at the reporting dates were as follows:

31 December 2009	EUR 1= KM 1.95583	USD 1 = KM 1.364088
31 December 2008	EUR 1= KM 1.95583	USD 1 = KM 1.387310

Off-balance sheet commitments

In the ordinary course of business, the Bank enters into credit related commitments which are recorded in off-balance sheet accounts and primarily include guarantees, letters of credit and undrawn loan commitments. Financial guarantee contract liabilities are measured initially at their fair values and are subsequently measured at the higher of:

- the amount of the provision assessed in accordance with the Federal Banking Agency requirements as described above; and
- the amount initially recognised less, where appropriate, cumulative amortisation recognised in accordance with IAS 18, *Revenue*.

Provisions

Provisions are recognised when the Bank has a present obligation as a result of a past event, and it is probable that the Bank will be required to settle that obligation. Management Board estimates the provisions based at the best estimate of expenditure to settle the Bank's obligation. Provisions are discounted to present value where the effect is material.

Reclassification

Certain amounts in the previous year financial statements have been reclassified to conform to the current year presentation:

In 2009 the Bank reclassified gain from foreign exchange transaction from Fee and commission income to Net trading Income. For consistency reasons, a similar item of 1,326 thousand KM has been reclassified in the 2008 Statement of Income.

In 2009 the Bank reclassified part of Commission fee – Banking Agency of FBiH services from Fee and commission expense to Administrative expenses (amount of 622 thousand KM was reclassified for 2008).

Segment reporting

Management has monitored the operating results of the Bank as a single segment for the purpose of making decisions about resource allocations and performance assessment.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Regulatory requirements

The Bank is subject to the regulatory requirements of the Banking Agency of Federation of Bosnia and Herzegovina. These regulations include limits and other restrictions pertaining to minimum capital adequacy requirements, classification of loans and off balance sheet commitments and forming allowances to cover credit risk, liquidity, interest rate and foreign currency position. At year end the Bank was substantially in compliance with all regulatory requirements.

4. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the Bank's accounting policies, which are described in note 3, the directors are required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Key sources of estimation uncertainty

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

Useful lives of property, plant and equipment

As described above, the Bank reviews the estimated useful lives of property, plant and equipment at the end of each annual reporting period as described in Note 3.

Impairment losses on loans and other placements

The Bank reviews its problem loans and other placements at each reporting date to assess amounts of allowances for impairment and provisions for contingent liabilities and commitments which should be recorded in the income statement. Such estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowances and provisions.

Long-term employee benefits

The cost of the long-term employee benefits is determined using actuarial valuation. The actuarial valuation involves making assumptions about discount rates, future salary increases, and future turnover rates. Due to the long term nature of these plans, such estimates are subject to significant uncertainty.

4. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY (continued)

Fair value of financial assets and liabilities

The directors use their judgment in selecting an appropriate valuation technique for financial instruments not quoted in an active market. Valuation techniques commonly used by market practitioners are applied. Financial instruments are valued using a discounted cash flow analysis based on assumptions supported, where possible, by observable market prices or rates. The estimation of fair value of unlisted shares includes some assumptions not supported by observable market prices or rates.

It is the opinion of the management of the Bank that the fair value of the Bank's financial assets and liabilities are not materially different from the amounts stated in the balance sheets as at 31 December 2009 and 31 December 2008. In estimating the fair value of the Bank's financial instruments, the following methods and assumptions were used:

Cash balances with the Central bank

The carrying values of cash and balances with the Central bank are generally deemed to approximate their fair value.

Due from banks

The estimated fair value of amounts due from banks that mature in 180 days or less approximates their carrying amounts. The fair value of other amounts due from banks is estimated based upon discounted cash flow analyses using interest rates currently offered for investments with similar terms (market rates adjusted to reflect credit risk).

Loans and advances to customers

The fair value of variable yield loans that regularly reprice, with no significant change in credit risk, generally approximates their carrying value. The fair value of loans at fixed interest rates is estimated using discounted cash flow analyses, based upon interest rates currently offered for loans with similar terms to borrowers of similar credit quality.

Amounts due to banks and customers

The fair value of term deposits payable on demand represents the carrying value of amounts payable on demand as at the balance sheet date. The fair value of term deposits at variable interest rates approximates their carrying values as at the balance sheet date. The fair value of deposits at fixed interest rates is estimated by discounting their future cash flows using rates currently offered for deposits of similar remaining maturities.

(all amounts are expressed in thousands of KM)

5. INTEREST INCOME

	31 December 2009	31 December 2008
Companies	25,313	22,898
Individuals	38,920	32,939
Domestic banks	1,074	2,516
Foreign banks	576	3,893
Government	673	152
Other	-	6
	66,556	**62,404**

6. INTEREST EXPENSE

	31 December 2009	31 December 2008
Individuals	8,088	7,601
Banks and other financial institutions	6,106	10,838
Companies	9,682	7,640
Government	1,155	698
	25,031	**26,777**

7. FEE AND COMMISSION INCOME

	31 December 2009	31 December 2008
Domestic payment transactions	2,621	2,866
Credit card activities	2,667	2,286
Foreign payment transactions	1,837	1,858
FX transactions	775	260
Guarantees	1,300	1,296
Agency services	185	241
Other	2,122	1,778
	11,507	**10,585**

(all amounts are expressed in thousands of KM)

8. FEE AND COMMISSION EXPENSE

	31 December 2009	31 December 2008
Credit card operations	2,003	2,149
Central Bank BiH services	191	205
Domestic payment transactions	454	324
E-banking service	136	106
	2,784	**2,784**

9. NET FOREIGN EXCHANGE INCOME

	31 December 2009	31 December 2008
Gains on foreign exchange transactions and translations	29,744	34,653
Loss on foreign exchange transactions and translations	(28,866)	(32,908)
	878	**1,745**

10. OTHER OPERATING INCOME

	31 December 2009	31 December 2008
Rental income	1	112
Dividend income	116	422
Gain on sale of AFS investments	355	2,170
Gain on sale of property	343	1,074
Other income	565	1,047
	1,380	**4,825**

Included in 'Gain on sale of AFS investments' are the amounts transferred from equity to the income statement on the derecognition of the available-for-sale investment

(all amounts are expressed in thousands of KM)

11. RECOVERIES OF WRITTEN OFF LOANS

	31 December 2009	31 December 2008
Suspended Interest	666	1,379
Principal	3,111	3,356
Other	65	176
	3,842	**4,911**

12. PERSONNEL EXPENSES

	31 December 2009	31 December 2008
Wages and salaries	11,731	11,493
Social security costs	5,509	5,498
Provisions (note 29)	31	(356)
Other expenses	110	170
	17,381	**16,805**

The Bank does not have pension arrangements separate from Bosnia and Herzegovina pension system. This system requires that current contributions by the employer be calculated as a percentage of current gross salary payments and taxes on net salary; these expenses are charged to the profit and loss statement in the period the related compensation is earned by the employee.

The average number of personnel employed by the Bank during the years ended 31 December 2009 and 2008 was 505 and 499 respectively.

13. ADMINISTRATIVE EXPENSES

	31 December 2009	31 December 2008
Rent and other rent related expense	2,996	2,641
Telecommunication and post expense	2,263	2,241
Saving deposit insurance and other insurance charges	1,454	1,564
Provisions, net (Note 29)	249	296
Material expenses	609	971
Representation and marketing expense	899	869
Consultancy and Banking Agency of FBiH expenses	1,326	1,335
Energy	674	615
Maintenance Expenses	2,096	1,767
Security and transport costs	1,324	1,037
Other expenses	2,080	2,283
	15,970	**15,619**

(all amounts are expressed in thousands of KM)

14. IMPAIRMENT LOSSES AND PROVISIONS

	31 December 2009	31 December 2008
Additions on impairment losses on placements with other banks	5	17
Additions on impairment losses on loans and advances originated by the Bank	14,128	13,796
Release of impairment losses on assets available for sale	(5)	(10)
Additions on provision for other assets	79	564
Additions on provision for commitments and contingent liabilities	532	853
	14,739	**15,220**

Detail of additions on impairment losses on loans and advances to customers (Note 20):

	31 December 2009	31 December 2008
Corporate Lending	7,540	3,396
Retail Lending	4,294	5,669
Credit and debit Cards	2,294	4,731
	14,128	**13,796**

15. INCOME TAX

	31 December 2009	31 December 2008
Profit before income tax	4,018	3,703
Non-deductible expenses and taxable income relieves	1,255	5,416
Taxable income	*5,273*	*9,119*
Income tax liability at the rate of 10%	**527**	**912**

Tax liability is based on accounting income before restatement taking into the account non-deductible expenses and non-taxable income. Tax income rate for the years ended 31 December 2009 and 2008 was 10%.

Based on management's review and assessment as of 31 December 2009, there are no temporary differences which would qualify for recognition of deferred tax assets or liabilities (2008: tax liabilities in treatment of KM 24 thousand relating to temporary difference arising from valuation of financial assets available for sale).

(all amounts are expressed in thousands of KM)

16. EARNINGS PER SHARE

	31 December 2009	31 December 2008
Net profit	3,491	2,791
Weighted average number of ordinary shares outstanding	452,960	373,417
Basic earnings per share	**0.00771**	**0.00747**

The Bank does not have dilutive potential ordinary shares.

17. CASH AND CASH EQUIVALENTS

	31 December 2009	31 December 2008
Current account in domestic currency with the Central Bank	78,238	5,645
Cash on hand in domestic currency	12,984	10,398
Cash on hand in foreign currency	6,676	8,985
Correspondent accounts with banks in foreign currency	2,605	1,777
	100,503	**26,805**

18. OBLIGATORY RESERVE WITH THE CENTRAL BANK

	31 December 2009	31 December 2008
Obligatory reserve	88,772	116,696
	88,772	**116,696**

Minimum obligatory reserve as of 31 December 2009 is calculated in amount of 14% for deposits and borrowings with maturity up to one year and 7% for deposits and borrowings with maturity over one year (as of 31 December 2008: 14%) for each working day during 10 calendar days following the period of maintaining the obligatory reserve. Mandatory reserve does not include local inter-bank deposits, short term and long term deposits from non-residents and short term and long term loans from non-residents, with effect from 1 November 2008.

(all amounts are expressed in thousands of KM)

19. PLACEMENTS WITH OTHER BANKS

	31 December 2009	31 December 2008
Short-term placements with banks from OECD countries	134,701	105,477
Less: Provisions for impairment	(23)	(18)
	134,678	**105,459**

The average interest rate for placements in EUR was 1.33% p.a. and 3.6% p.a. and for placements in USD 0.57% p.a. and 2.27% p.a. as of 31 December 2009 and 31 December 2008, respectively.

The movements in the provision for impairment of placements with other banks are summarized as follows:

	31 December 2009	31 December 2008
Balance as at 1 January	**18**	**1**
Provisions	699	59
Reversal of provisions	(694)	(42)
Balance as at 31 December	**23**	**18**

20. LOANS AND RECEIVABLES

	31 December 2009	31 December 2008
Short-term loans in domestic currency	262,222	235,510
Short-term loans in foreign currency	1,431	1,775
Current portion of long-term loans	117,783	104,145
Total short-term loans	*381,436*	*341,430*
Long-term loans in domestic currency	220,622	176,667
Long-term loans in foreign currency	353,809	346,806
(Current portion of long-term loans)	(117,783)	(104,145)
Total long-term loans	*456,648*	*419,328*
Total loans before provisions	*838,084*	*760,758*
Provision for impairment	(39,289)	(33,612)
	798,795	**727,146**

Short-term loans are granted for periods of up to 365 days. The majority of short-term loans in domestic currency are granted to clients for working capital financing. Long-term loans are mostly granted to individuals for housing and vehicle purchases, and to corporate clients for investment purposes.

(all amounts are expressed in thousands of KM)

20. LOANS AND RECEIVABLES (continued)

The movements in the provision for impairment of loans are summarized as follows:

	31 December 2009	31 December 2008
Balance as at 1 January	**33,612**	**31,346**
Provisions charged	30,460	34,082
Reversal of provision	(16,332)	(20,286)
Write-offs	(8,451)	(11,530)
Balance as at 31 December	**39,289**	**33,612**

Total amount of non-performing loans on which interest was suspended as at 31 December 2009 and 2008 was KM thousand 31,585 and KM 26,445 thousand, respectively.

	31 December 2009	31 December 2008
Manufacturing industry	133,354	119,715
Trade	170,220	118,878
Construction industry	34,222	24,263
Services, finance, sport, tourism	30,540	40,071
Administrative and other public institutions	7,297	2,680
Agriculture, forestry, mining and energy	21,641	19,550
Transport and telecommunications	22,432	17,481
Other	13,211	14,387
Citizens	405,167	403,733
	838,084	**760,758**

	31 December 2009	31 December 2008
Corporate Lending	432,917	357,025
Consumer Lending	241,801	251,235
Residential Mortgages	114,190	105,873
Credit and Debit Cards	49,176	46,625
	838,084	**760,758**

(all amounts are expressed in thousands of KM)

20. LOANS AND RECEIVABLES (continued)

Interest rates for granted loans as at 31 December 2009 and 2008 are summarized as follows:

	31 December 2009		31 December 2008	
	KM '000	**Annual interest rate**	**KM '000**	**Annual interest rate**
Domestic currency				
Companies	419,220	2.00% - 15.00%	338,498	3.00% - 12.00%
Citizens	63,625	4.00% - 14.50%	73,679	4.00% - 14.75%
Foreign currency				
Companies	13,697	3.59% - 9.53%	18,527	5.79% - 11.22%
Citizens	341,542	3.00% - 10.99%	330,054	4.00% - 11.00%
	838,084		**760,758**	

21. ASSETS AVAILABLE FOR SALE

	31 December 2009	**31 December 2008**
Gross value	553	817
Impairment	(11)	(16)
	542	**801**

Assets available for sale include investments of 20.03% in share capital of Bamcard d.d. Sarajevo in the amount of KM 488 thousand (2008: KM 488 thousand).

Also, assets available for sale include investments of less than 1% in various companies in Bosnia and Herzegovina recognized at cost of KM 65 thousand (2008: KM 63 thousand).

During 2009 Bank sold investment in VISA Inc. in the amount 305 thousand KM.

The movements in the provision for impairment of financial assets available for sale are summarized as follows:

	31 December 2009	**31 December 2008**
Balance as at 1 January	**16**	**26**
Provisions	1	5
Reversal of provision	(6)	(15)
Balance as at 31 December	**11**	**16**

(all amounts are expressed in thousands of KM)

22. OTHER ASSETS

	31 December 2009	31 December 2008
Prepaid income taxes	3,197	2,812
Payment to the Cantonal Privatization Agency for privatization of "Projekt" d.d. Sarajevo	1,200	1,200
Prepaid expenses	2,026	1,348
Fees receivable	422	343
Receivables from card operations	336	195
Other assets	1,377	1,638
Total other assets	*8,558*	*7,536*
Provision for impairment	(590)	(649)
	7,968	**6,887**

The movements in the provision for impairment of other assets are summarized as follows:

	31 December 2009	31 December 2008
Balance as at 1 January	**649**	**391**
Provisions	428	1,216
Reversal of provision	(349)	(652)
Write-offs	(138)	(306)
Balance as at 31 December	**590**	**649**

(all amounts are expressed in thousands of KM)

23. PROPERTY, PLANT AND EQUIPMENT

	Land and Buildings	Computers and other equipment	Software	Constr-uction in progress	Leasehold improve-ments	Building out of use	Total
Cost value							
31 December 2007	13,665	13,093	2,665	1,583	4,562	368	**35,936**
Additions	-	4	-	7,283	-	-	**7,287**
Disposals	(192)	(1,117)	(25)	(9)	-	(368)	**(1,711)**
Transfers from construction in progress	171	4,779	991	(7,727)	1,786	-	**-**
Transfer from other assets	(55)	55	-	-	-	-	**-**
31 December 2008	**13,589**	**16,814**	**3,631**	**1,130**	**6,348**	**-**	**41,512**
Additions		-		5,416	-	-	**5,416**
Disposals	(673)	(857)	-	-	(7)	-	**(1,537)**
Transfers from construction in progress	24	2,563	1,925	(6,322)	1.810	-	**-**
31 December 2009	**12.940**	**18.520**	**5.556**	**224**	**8.151**	**-**	**45.391**
Accumulated Depreciation							
31 December 2007	1,193	6,324	1,985	-	1,734	5	**11,241**
Transfer from other assets	(25)	25	-	-	-	-	**-**
Depreciation for the period	179	1,998	446	**-**	935	4	**3,562**
Disposals	(26)	(913)	(25)	-	-	(9)	**(973)**
31 December 2008	**1,321**	**7,434**	**2,406**	**-**	**2,669**	**-**	**13,830**
Depreciation for the period	174	2,370	525	-	1,171	-	**4,240**
Disposals	(246)	(793)	-	-	-	-	**(1,039)**
31 December 2009	**1,249**	**9,011**	**2,931**	**-**	**3,840**	**-**	**17,031**
Net book value: 31 December 2009	**11,691**	**9,509**	**2,625**	**224**	**4,311**	**-**	**28,360**
Net book value: 31 December 2008	**12,268**	**9,380**	**1,225**	**1,130**	**3,679**	**-**	**27,682**

(all amounts are expressed in thousands of KM)

24. DUE TO BANKS AND OTHER INSTITUTIONS

	31 December 2009	31 December 2008
Current portion of long-term borrowings	106,521	24,811
Total short-term borrowings	*106,521*	*24,811*
Long-term borrowings from foreign banks and other institutions	234,625	208,439
Long-term borrowings from domestic banks and other institutions	10,670	12,855
Current portion of long-term borrowings	(106,521)	(24,811)
Total long-term borrowings	*138,774*	*196,483*
Current accounts in domestic currency	3	18
Current accounts in foreign currency	-	1
Total current accounts	*3*	*19*
Short-term deposit	112,472	68,454
Long-term deposits	3,500	42,617
	361,270	**332,384**

(all amounts are expressed in thousands of KM)

24. DUE TO BANKS AND OTHER INSTITUTIONS (continued)

Long-term borrowings from international banks and non-banking financial and non-financial institutions as at 31 December 2009 and 31 December 2008 were as follows:

	31 December 2009	**31 December 2008**
Commerzbank Ag Frankfurt, Germany	68,690	69,458
Societe Europeenne De Banque S.A., Luxembourg	29,485	39,454
European Fund for Southeast Europe (EFSE), Luxembourg	44,599	26,861
Intesa Sanpaolo SPA Milan, Italy	22,429	26,279
European Investment Bank	48,998	20,498
Vseobecna Uverova Banka A.S. Bratislava	19,560	19,564
Federalni zavod za zapošljavanje, Sarajevo	3,816	3,819
Razvojna banka Federacije Bosne i Hercegovine d.o.o. Sarajevo	1,228	3,368
European Bank for Reconstruction and Development, London, UK	-	2,497
Federalno ministarstvo finansija, Sarajevo	2,442	2,437
Vlada SBH/ŽSB, Travnik	2,126	2,117
OPEC FUND for International Development, Vienna, Austria	763	1,274
Hrvatska banka za obnovu i razvitak (HBOR), Zagreb, Croatia	-	1,133
Federalno ministarstvo šumarstva i vodoprivrede, Sarajevo	1,028	1,028
Privredna banka Zagreb d.d., Zagreb, Croatia	-	806
Partners for Development, Sarajevo	102	615
USAID Business Finance Office Sarajevo	-	-
Služba za zapošljavanje SBK / ŽSB	29	86
	245,295	**221,294**

Interest rates for long-term borrowings from banks and other institutions were in the range from 0% to 3.73% per annum and from 0% to 8.11% per annum as of 31 December 2009 and 31 December 2008, respectively.

Interest rate for short term deposits were in the range from 1% to 2.75% per annum and from 2.60% to 4.90% per annum as of 31 December 2009 and 31 December 2008, respectively.

(all amounts are expressed in thousands of KM)

25. SUBORDINATED DEBT

	31 December 2009	31 December 2008
USAID / MINISTARSTVO FINANSIJA TREZORA BiH	1,404	1,568
VSEOBECNA UVEROVA BANKA A.S.	-	9,788
	1,404	**11,356**

The subordinated loan from USAID as of 31 December 2008 and 31 December 2009 respectively amounting to KM 1,565 thousand and KM 1,404 thousand was received in August 2003 in the amount of KM 2,408 thousand, and it is repayable in 60 quarterly instalments starting from 1 December 2003 until 1 September 2018. Interest rate is fixed at 2.3163 % p.a.

The subordinated loan from VUB (Vseobecna Uverova Banka) amounting to 9,779 KM thousand was received on 27 June 2008 and having interest payable quarterly starting from 27 June 2008 until 27 June 2013 (Interest rate is 3M EURIBOR + 3.54%). Principal has been repaid in advance on 1 July 2009 in the amount of KM 9,779 thousand.

According to the approval of the Banking Agency of Federation of Bosnia and Herzegovina, the subordinated debt may be used as additional capital for calculation of regulatory capital.

26. DUE TO CUSTOMERS

	31 December 2009	31 December 2008
Demand deposits:		
Citizens:		
In KM	41,298	42,942
In foreign currencies	23,152	22,014
Subtotal	*64,450*	*64,956*
Legal entities:		
In KM	271,337	169,216
In foreign currencies	54,748	38,515
Subtotal	*326,085*	*207,731*
Total demand deposits	**390,535**	**272,687**
Term deposits:		
Citizens:		
In KM	26,210	26,282
In foreign currencies	128,648	125,397
Subtotal	*154,858*	*151,679*
Legal entities:		
In KM	93,974	63,916
In foreign currencies	23,374	46,099
Subtotal	*117,348*	*110,015*
Total term deposits	**272,206**	**261,694**
	662,741	**534,381**

During 2009 interest rates for demand deposits were from 0.00% to 3.00% (during 2008 were from 0.00% to 2.50%). Short-term deposit interest rates were from 0.00% to 8.19% and from 0.00% to 7.40% during 2009 and 2008, respectively. Long-term deposit interest rates were from 0.00% to 8.00% and from 0.00% to 8.00% during 2009 and 2008, respectively.

(all amounts are expressed in thousands of KM)

26. DUE TO CUSTOMERS (continued)

Included in 'Due to Customers' are deposits held as collateral for deposits, guarantee and L/C in the amount of KM 17,125 thousand (2008: KM 21,163 thousand).

	31 December 2009	31 December 2008
Large Corporate customers:	*385,554*	264,372
Current Accounts	283,800	162,265
Term Deposits	101,754	102,107
Small and medium-sized enterprises:	*57,879*	53,374
Current Accounts	42,285	45,466
Term Deposits	15,594	7,908
Retail Customers:	*219,308*	*216,635*
Current Accounts	64,450	64,956
Term Deposits	154,858	151,679
	662,741	**534,381**

27. FINANCIAL LIABILITIES HELD FOR TRADING

	31 December 2009	31 December 2008
OTC derivatives	761	-
	761	**-**

In 2009 a forward deal was made with Intesa Sanpaolo Milano where the Bank bought USD and sold EUR currency. Value date and maturity date of this transaction are 13.02.2009 and 17.02.2010, respectively. These derivatives are valued using valuation techniques based on observable market data.

28. OTHER LIABILITIES

	31 December 2009	31 December 2008
Loan repayments received before due dates	2,394	2,899
Liabilities to vendors	1,045	1,447
Liabilities for employees bonuses	550	496
Managed fund difference (Note 31)	-	14
Credit card liabilities	106	191
Liabilities to shareholders	149	149
Deferred tax liability	-	24
Other liabilities	1,293	906
	5,537	**6,126**

(all amounts are expressed in thousands of KM)

29. OTHER PROVISIONS

	31 December 2009	31 December 2008
Provisions for litigations with the Tax authorities and clients	1,620	1,445
Provisions for retirement employee benefits and other short-term employee benefits	426	395
	2,046	**1,840**

Provisions for litigations are made based on the uncertainty in the outcomes of the ongoing court case with the tax authority and other proceedings.

	Provisions for legal proceedings	Provisions for retirement employee benefits and other short term employee benefits	Total
Balance at 31 December 2008	**1,445**	**395**	**1,840**
Additional provision recognised	249	52	301
Release of provision	-	(21)	(21)
Reductions arising from payments	(74)	-	(74)
Balance at 31 December 2009	**1,620**	**426**	**2,046**

Calculation of provisions for retirement benefits of KM 183 thousand as of 31 December 2009 (2008: KM 157 thousand) is performed by independent actuary, applying a discount rate of 6% and 3% expected rate of increase in salaries, to working life and average salary of each employee.

Provisions for unused days of vacation of KM 243 thousand as of 31 December 2009 (2008: KM 238 thousand) are calculated for every employee, taking as a basis his/her salary and unused days of vacation.

(all amounts are expressed in thousands of KM)

30. FINANCIAL COMMITMENTS AND CONTINGENCIES

In the ordinary course of business, the Bank has been involved in a number of legal proceedings to recover collateral or outstanding credit balances, as well as related interest and expenses from defaulted credit customers and interbank counterparts. The management of the Bank believes that any legal proceedings pending as at 31 December 2009 will not result in material loss to the Bank.

In the ordinary course of business, the Bank enters into credit related commitments which are recorded in off-balance sheet accounts and primarily include guarantees, letters of credit and undrawn loan commitments.

	31 December 2009	31 December 2008
Contingent liabilities		
Payment guarantees	17,496	17,880
Performance guarantees	27,452	26,050
Letters of credit	4,237	1,150
Total contingent liabilities	**49,185**	**45,080**
Commitments		
Unused portion of overdraft loans	71,147	82,805
Total commitments	**71,147**	**82,805**
Total contingent liabilities and commitments	**120,332**	**127,885**

Provisions for contingent liabilities are recognised when the Bank has a present obligation as a result of a past event, and it is probable that the Bank will be required to settle that obligation. Management Board estimates the provisions based at the best estimate of expenditure to settle the Bank's obligation.

Movements in provision for contingent liabilities and commitments are as follows:

	31 December 2009	31 December 2008
Balance as at 1 January	**3,027**	**3,027**
Increase in provisions	5,272	5,483
Reversal of provision	(4,740)	(4,630)
Write offs	(850)	(853)
Balance as at 31 December	**2,709**	**3,027**

31. RELATED-PARTY TRANSACTIONS

Related parties, as defined by IAS 24, are those counter parties that represent:

a. enterprises that directly, or indirectly through one or more intermediaries, control, or are controlled by, or are under common control with, the reporting enterprise (This includes holding companies, subsidiaries and fellow subsidiaries);

b. associates – enterprises in which the Bank has significant influence and which is neither a subsidiary nor a joint venture of the investor;

c. individuals owning, directly or indirectly, an interest in the voting power of the Bank that gives them significant influence over the Bank, and anyone expected to influence, or be influenced by, that person in their dealings with the Bank;

d. key management personnel, that is, those persons having authority and responsibility for planning, directing and controlling the activities of the Bank, including directors and officers of the Bank and close members of the families of such individuals; and

e. enterprises in which a substantial interest in the voting power is owned, directly or indirectly, by any person described in (c) or (d) or over which such a person is able to exercise significant influence. This includes enterprises owned by directors or major shareholders of the Bank and enterprises that have a member of key management in common with the Bank.

(all amounts are expressed in thousands of KM)

31. RELATED-PARTY TRANSACTIONS (continued)

In considering each possible related party relationship, attention is directed to the substance of the relationship, and not merely the legal form.

	31 December 2009	31 December 2008
Receivables		
Key management personnel and close family members	249	232
Bank accounts – Intesa Sanpaolo Group	16,367	41,417
Other receivables – Intesa Sanpaolo Group	77	18
Other receivables from European Bank for Reconstruction and Development (EBRD)	-	20
	16,693	**41,687**
Liabilities		
Deposits – Key management personnel and close family members	514	462
Borrowings – Intesa Sanpaolo Group	179,044	202,654
Other liabilities – Intesa Sanpaolo Group	497	1,165
Borrowings and other liabilities to European Bank for Reconstruction and Development (EBRD)	-	2,498
	180,055	**206,779**
Financial commitments and contingencies		
Guarantees issued in favour of Intesa Sanpaolo Group	2,208	3,523
Commitmets to lend – Intesa Sanpaolo Group	170	-
	2,378	**3,523**
Financial liabilities held for trading		
OTC derivates with Intesa Sanpaolo Group	761	-
	761	**-**
Income		
Interest income - Key management personnel and close family members	22	17
Interest income – Intesa Sanpaolo Group	626	731
Other Income – Intesa Sanpaolo Group	129	101
	777	**849**

(all amounts are expressed in thousands of KM)

32. RELATED-PARTY TRANSACTIONS (continued)

	31 December 2009	31 December 2008
Expenses		
Interest expense - Key management personnel and close family members	7	8
Interest expense – Intesa Sanpaolo Group	3,983	7,851
Interest expense – European Bank for Reconstruction and Development (EBRD)	75	265
Other expenses – Intesa Sanpaolo Group	1,843	540
Other expense - European Bank for Reconstruction and Development (EBRD)	21	25
	5,929	**8,689**

Intesa Sanpaolo Holding International S.A. is the majority shareholder and exercises control over the Bank's operations.

EBRD is one of the Bank's majority shareholders.

No exposure towards related parties has been classified as non-performing. Expenses for those exposures during the period relates only to the establishment of the 2% generic provision.

A number of banking transactions are entered into with related parties in the normal course of business. These transactions were carried out on commercial terms and conditions and at market rates.

The remuneration of directors and other members of key management were as follows:

	31 December 2009	31 December 2008
Compensation for directors and other key management	552	746
Taxes and contributions on compensation	407	463
Bonuses to Management board – Accrued expenses	336	250
Compensations for Supervisory Board members	22	-
Other Management benefits	314	175
	1,631	**1,634**

The Bank has:

- neither guarantee with any director or other member of key management,
- nor exposure towards director or key management has been classified as non-performing.

Expenses for those exposures during the period relates only to the establishment of the 2% generic provision.

(all amounts are expressed in thousands of KM)

33. MANAGED FUNDS

The Bank manages assets on behalf of third parties. These assets are recorded separately from the Bank's assets. For its services, the Bank charges a fee amounting from 0.0% to 2.5% p.a. (in 2008 from 0.2% to 2.50% p.a.) of the total amount contributed

	31 December 2009	31 December 2008
Liabilities		
Investment Bank of Bosnia and Herzegovina	1,828	1,924
Companies	13,880	15,989
Investment Guarantee Agency - IGA	1,703	2,073
Managed on behalf and for the account of the Sarajevo Canton, Ministry of Finance	42	82
Total	**17,453**	**20,068**
Assets		
Loans to companies	16,071	16,493
Loans to citizens	1,382	3,561
Total	**17,453**	**20,054**
Amounts due to original creditors – managed funds (Note 28)	**-**	**14**

The Bank has not issued any guarantees related to managed funds.

34. FINANCIAL INSTRUMENTS

Capital management

The Bank's objectives when managing capital, which is a broader concept than the 'equity' on the face of balance sheets, are:

- To comply with the capital requirements set by the regulators of the banking markets;
- To safeguard the Bank's ability to continue as a going concern so that it can continue to provide returns for shareholders and benefits for other stakeholders; and
- To maintain a strong capital base to support the development of its business.

The Bank expects to maintain its debt to capital ratio. Solvency indicators were as follows:

	31 December 2009	31 December 2008
Debt (i)	1,024,011	866,765
Cash on hand, balances with the Central bank and placements with other banks	(323,953)	(248,960)
Net debt	700,058	617,805
Capital (ii)	124,554	133,718
Net debt to capital ratio	**5,62**	**4.62**

34. FINANCIAL INSTRUMENTS (continued)

Capital management (continued)

Debt (i) is defined as liabilities to banks and clients presented in detail in Notes and Capital (ii) includes total capital, Bank's reserves, retained earnings and subordinated debt.

Capital adequacy and the use of regulatory capital are monitored daily by the Bank's management, employing techniques based on the guidelines developed by Banking Agency of Federation of Bosnia and Herzegovina (FBA) for supervisory purposes. The required information is filed with the FBA on a quarterly basis.

The FBA requires each bank to:

(a) hold the minimum level of the regulatory capital of KM 15,000,000, and
(b) maintain a ratio of total regulatory capital to the risk-weighted asset at or above the minimum of 12% for 2009. From 31 December 2008 Federal Banking Agency requested banks to include in the calculation of capital adequacy a charge for operational risk.

As of 31.12.2009 Federal Banking Agency changed the methodology for the calculation of the charge for operational risk, which is now based on gross income instead of net income as before.

The Bank's regulatory capital is divided into two tiers:

- Tier 1 capital or Core Capital: share capital (net of any book values of the treasury shares), share premium, retained earnings and reserves created by appropriations of retained earnings; and
- Tier 2 capital or Supplementary Capital: qualifying principle of subordinated loan capital, collective impairment allowances and unrealised gains arising on the fair valuation of equity instruments held as available for sale.

The risk-weighted assets are measured by means of a hierarchy of four weights classified according to the nature of – and reflecting an estimate of credit, market and other risks associated with – each asset and counterparty, taking into account any eligible collateral or guarantees. A similar treatment is adopted for off-balance sheet exposure, with some adjustments to reflect the more contingent nature of the potential losses.

(all amounts are expressed in thousands of KM)

34. FINANCIAL INSTRUMENTS (continued)

Capital management (continued)

Charge for operational risk has been introduced since 31 December 2008. The table below summarises the composition of regulatory capital and the ratios of the Bank for the years ended 31 December. During those two years the Bank complied with all of the externally imposed capital requirements to which they are subject:

	31 December 2009	31 December 2008
Tier 1 capital		
Share Capital	45,296	45,296
Treasury shares	(514)	-
Share Premium	57,415	59,368
Statutory reserves	614	614
Retained Earnings	11,306	8,514
Other reserves not related to assets valuation	5,536	5,537
Revaluation reserve – available for sale investments	6	242
Items to be deducted: Intangible assets	(2,669)	(1,243)
Total qualifying Tier 1 Capital	*116,990*	*118,328*
Tier 2 capital		
Qualifying subordinated loan capital	1,404	11,344
Generic provisions for performing assets	17,291	16,226
Profit for the year	3,491	2,791
Total qualifying Tier 2 Capital	*22,186*	*30,361*
Total regulatory capital	**139,176**	**148,689**
Risk weighted assets		
On balance sheet	854,008	767,407
Off balance sheet	67,117	69,586
Total	**921,125**	**836,993**
Operational risk	**49,605**	**2,417**
Total weighted risk	**970,730**	**839,410**
Capital adequacy ratio	**14,33%**	**17.70%**

34. FINANCIAL INSTRUMENTS (continued)

Financial risk management objectives

Main purpose of Risk management Department is to support financial operations, coordinate access to domestic and international financial markets, overlooking and manage financial risk trough internal risk reports including analysis by size and level of the risk. Financial risk management includes: market risk (FX risk, interest rate risk, and pricing risk), credit risk, liquidity risk and interest rate cash flow risk.

FX Value-at-Risk is individual, concise, statistic measurement of possible losses in the portfolio. Value-at-Risk is loss measurement in normal movements of risk factors on the market. Losses higher than the Value-at-Risk occur only with a low indicated likelihood.
The main model assumptions are:

- Being based on the Historical methodology,
- 99 percent as a confidence interval for VaR computation,
- One-day held period.

The model covers foreign currency risk – valid for foreign currency transactions and positions denominated on foreign currencies; resulting from foreign currency rate volatility.

The model can compute VaR at different aggregation levels – from a single position to any sub-portfolio level. Therefore, the model allows a detailed analysis of risk profiles of multi-level portfolio hierarchy and diversity effects occurring. Furthermore, VaR measurement can be expounded based on risk source (risk factors). These features of a more detailed risk monitoring allow determining an efficient limit structure which can be compared through different organisational units.

Key data and their sources, necessary for daily VaR computation based on this model are the following:

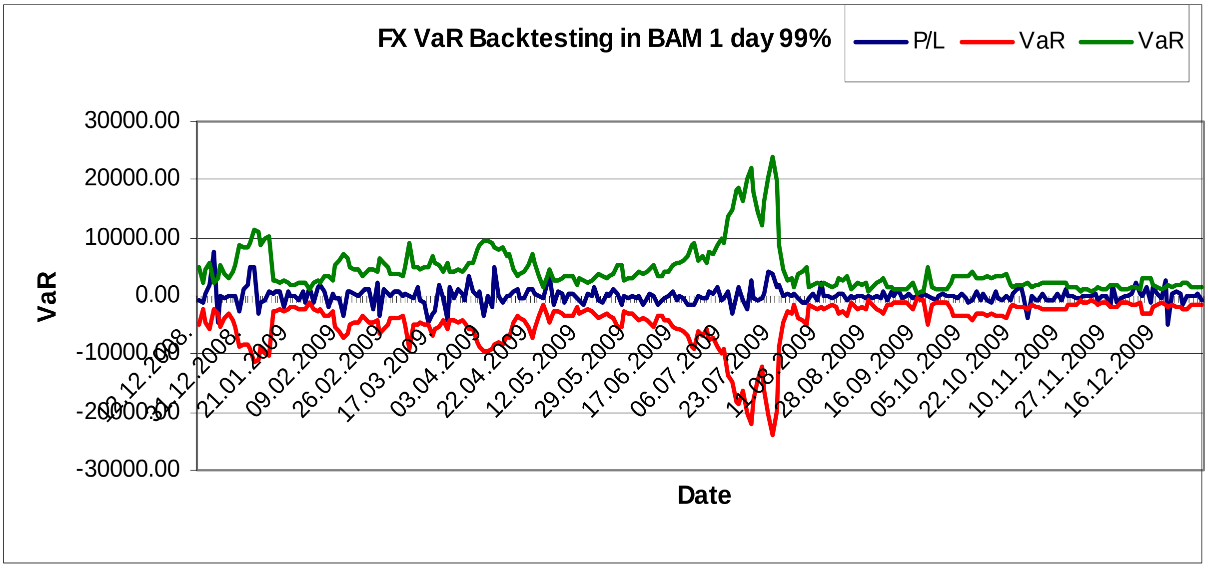
- **Open foreign currency position** – prepared by the Planning and Control Department, checked by the Integrated Risk Management Department, and sent to the Parent Company,
- **Market data:**
- **Local market data –** all local market data unavailable to the Integrated Risk Management Department shall be prepared on a daily basis by the Treasury Division, sent to the Integrated Risk Management Department and to the Parent Company,
- **International market data** – all international market data unavailable to the Integrated Risk Management Department shall be prepared on a daily basis by the Treasury Division, sent to the Integrated Risk Management Department and to the Parent Company.

(all amounts are expressed in thousands of KM)

34. FINANCIAL INSTRUMENTS (continued)

Financial risk management objectives (continued)

The quality of the implemented risk measurement model must be constantly assessed. Backtesting is way to achieve this goal. The essence of backtesting procedure is comparing the computed VaR measure with the P&L for the same period. Based on backtesting results opinion on the internal model quality shall be created.



During 2009, the Bank recorded three back-testing exceptions (2008: one exception), when actual losses exceeded daily Var amount.

Foreign currency risk

The Bank is exposed to foreign currency risk when there is no matching between assets and liabilities due to cash flows denominated in foreign currencies. Portfolio exposure to foreign currency risk arises from portfolio sensitivity to fluctuations in exchange rate values. The degree of foreign currency risk depends on the amount of open positions and the degree of potential change in foreign currency rates.

The carrying amounts of the Bank's foreign currency denominated monetary assets and liabilities at the reporting date are as follows:

	Assets		Liabilities	
	31 December 2009	31 December 2008	31 December 2009	31 December 2008
EUR	730,959	636,279	758,008	430,160
USD	13,965	20,604	13,832	22,729
CHF	1,241	1,338	1,105	2,012
HRK	1,322	1,541	1,291	1,629
GBP	186	196	224	190
Other	697	665	623	1,040

(all amounts are expressed in thousands of KM)

34. FINANCIAL INSTRUMENTS (continued)

Financial risk management objectives (continued)

Foreign currency sensitivity analysis

The Bank is not exposed to foreign currency risk related to EUR due to the fact that Convertible Mark is pegged to EURO (1 EUR = KM 1.955830). Change in the exchange rate would require the amendments of the law and approval by Parliamentary Assembly of Bosnia and Herzegovina. Exposure is more prominent for USD and CHF. The following table details the Bank's sensitivity to a 10% increase or decrease in foreign currency rates against the relevant local currencies. The sensitivity rate of 10% is used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the reasonably possible change in foreign exchange rates.

Result of KM thousand profit/loss on USD position at 31.12.2009 is the result of having the Bank open position in USD equal to 133 KM thousand (USD assets 13,965 thousand KM and liabilities 13,832 thousand KM). If we take in consideration foreign currency movements and predict 10% positive or negative change applied to an open position of 133 KM thousand, the Bank is exposed to a FX risk in the amount of 13,3 KM thousand. In case of a long position with a positive market movements the Bank will record a profit and loss in the opposite case.

	USD Effect (KM '000)		**CHF Effect (KM '000)**	
	31 December 2009	**31 December 2008**	**31 December 2009**	**31 December 2008**
Profit or Loss	13,3	4,9	13,6	(1)

The analysis outlined above is used on open foreign currency position of the Bank, which includes all asset and liability items.

If the currency position of a foreign currency is "long" (assets exceeding liabilities) and the exchange rate for this currency increases in relation to the KM, the Bank will experience a foreign exchange gain.

If the currency position of a foreign currency is "long" (assets exceeding liabilities) and the exchange rate for this currency decreases in relation to the KM, the Bank will experience a foreign exchange loss.

If the currency position of a foreign currency is "short" (liabilities exceeding assets) and the exchange rate for this currency increases in relation to KM, the Bank will experience a foreign exchange loss.

If the currency position of a foreign currency is "short" (liabilities exceeding assets) and the exchange rate for this currency decreases in relation to KM, the Bank will experience a foreign exchange gain.

The Bank takes on exposure to effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Bank monitors its foreign exchange (FX) position for compliance with the regulatory requirements of the Banking Agency of Federation of Bosnia and Herzegovina established in respect of limits on open positions. The Bank seeks to match assets and liabilities denominated in foreign currencies to avoid foreign currency exposures.

34. FINANCIAL INSTRUMENTS (continued)

Interest rate risk management

The Bank is exposed to interest rate risk as the Bank borrows funds at both fixed and floating interest rates. The risk is managed by the Bank by maintaining an appropriate mix between fixed and floating rate borrowings.

The Bank's exposures to interest rates on financial assets and financial liabilities are detailed in the liquidity risk management section of this note.

Interest rate risk reflects the possibility of loss of profit and/or erosion of capital due to a change in interest rates. It relates to all products and balances that are sensitive to changes in interest rates. This risk comprises two components: income component and investment component.

The income component arises from a lack of harmonization between the active and passive interest rates of the Bank (interest on placements is fixed, interest for liabilities is variable and vice versa).

The investment component is a consequence of the inverted relationship between price and interest rate fluctuations of securities.

The Bank strives to protect itself from interest rate risk by harmonizing the type of interest rate (fixed and variable), currency, related interest rate and the date of interest rate change for all products for which it concludes contracts (which are sensitive to interest rate changes). Any incongruity among the abovementioned elements results in exposure of the Bank to interest rate risk.

The sensitivity analyses below have been determined based on the exposure to interest rates for both derivatives and non-derivative instruments at the balance sheet date. For floating rate liabilities, the analysis is prepared assuming the amount of liability outstanding at the balance sheet date was outstanding for the whole year. A 200 basis point increases or decrease is used when reporting interest rate risk internally to key management personnel and represents management's assessment of the reasonably possible change in interest rates.

If changes in interest rates market moving had been 200 basis points (2.00%) higher/lower and all other variables were held constant, the Bank's:

- profit for the year ended 31 December 2009 with parallel interest rate shock in 200 bps would decrease 1,930 / 1,930 increase (2008: decrease/increase by KM 2,778 thousand). This is mainly attributable to the Bank's exposure to interest rates on its variable rate borrowings

34. FINANCIAL INSTRUMENTS (continued)

Credit risk management

The Bank takes on exposure to credit risk which is the risk upon credit approval and when counterparty will be unable to pay amounts in full when due. The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees.

Making decision on exposure to credit risk is, according to the Bank's policy, centralised and concentrated in the Credit Committee for the retail and business. Decisions of the Credit Committees are made upon consideration of proposal provided by the Risk Management Department. The terms for approval of each corporate loan are determined individually depending on client type, loan's purpose, estimated credit worthiness and current market situation. Terms of security that accompany each loan are also determined according to a client credit worthiness analysis, type of credit risk exposure, term of the placement as well as the placement amount.

Commitments arising from the issuance of letters of credit, documentary letters of credit, which are written irrevocable undertakings by the Bank on behalf of a customer (mandatory) authorising a third party (beneficiary) to draw drafts on the Bank up to a stipulated amount under specific terms and conditions, are collateralised by the underlying shipments of goods to which they relate and therefore have significantly less risk. Cash requirements under open letters of credit are considerably less than the commitments under issued guarantees or stand-by letters of credit. However, the Bank records provisions against these instruments on the same basis as is applicable to loans.

Commitments to extend credit, undrawn loan commitments, unutilised overdrafts and approved overdraft loans. The primary purpose of commitments to extend credit is to ensure that funds are available to a customer as required. Commitments to extend credit represent unused portions of authorisations to extend credits in the form of loans, guarantees or stand-by letters of credit. Commitments to extend credit issued by the Bank represent issued loan commitments or guarantees, undrawn portions of and approved overdrafts loans. Commitments to extend credit or guarantees issued by the Bank which are contingent upon customers maintaining specific credit standards (including the condition that a customer’s solvency does not deteriorate) are revocable commitments. Irrevocable commitments represent undrawn portions of authorised loans and approved overdraft facilities because they result from contractual terms and conditions in the credit agreements.

(all amounts are expressed in thousands of KM)

34. FINANCIAL INSTRUMENTS (continued)

Credit risk management (continued)

Financial assets

31 December 2009	**Total gross carrying amount**	**Unimpaired assets**	**Individually impaired assets**	**Provisions for losses**	**Total net carrying amount**
Cash and balances with other banks	100,503	100,503	-	-	100,503
Obligatory reserve with the Central Bank	88,772	88,772	-	-	88,772
Placements with other banks	134,701	134,701	-	(23)	134,678
Loans and advances to customers	838,084	792,562	45,522	(39,289)	798,795
Assets available for sale	553	553	-	(11)	542
	1,162,613	**1,117,091**	**45,522**	**(39,323)**	**1,123,290**
31 December 2008					
Cash and balances with other banks	26,805	26,805	-	-	26,805
Obligatory reserve with the Central Bank	116,696	116,696	-	-	116,696
Placements with other banks	105,477	105,477	-	(18)	105,459
Loans and advances to customers	760,758	719,648	41,110	(33,612)	727,146
Assets available for sale	817	817	-	(16)	801
	1,010,553	**969,443**	**41,110**	**(33,646)**	**976,907**

(all amounts are expressed in thousands of KM)

34. FINANCIAL INSTRUMENTS (continued)

Credit risk management (continued)

Credit exposure and collateral

31 December 2009		**Credit risk exposure**		
Description	**Loans given**	**Undrawn loan commitments and unutilized overdrafts**	**Commitments / Guarantees issued**	**Fair value of the collateral**
Legal entity	432,917	28,120	49,185	325,203
Retail	405,167	43,027		119,149
Total	**838,084**	**71,147**	**49,185**	**444,352**
31 December 2008				
Legal entity	357,025	34,125	45,080	233,556
Retail	403,733	48,680	-	115,278
Total	**760,758**	**82,805**	**45,080**	**348,834**

Fair value of the collateral

	31.12.2009	**31.12.2008**
Property	432,877	329,092
Deposits	11,475	19,742
	444,352	**348,834**

The Collateral Policy of the Bank defines the type of collateral, way of estimating fair value of collaterals and procedure for collection of receivable through collaterals. Type of prescribed collaterals and their respective amount are based on evaluation of every client's credit worthiness. Main categories or accepted collaterals are: cash, real estate, movable property and personal guarantees.

The Bank collateral policy defines also the process of recovery of non-performing loans through collaterals in order to decrease credit risk. The property that the Bank acquired through its collection process (land and buildings in the amount of KM 29 thousand; 2008: KM 36 thousand) is not shown among the Bank's property plant and equipment but it is recorded in "Other assets" position.

(all amounts are expressed in thousands of KM)

34. FINANCIAL INSTRUMENTS (continued)

Credit risk management (continued)

Fair value of the collateral (continued)

Delays

	Gross total loans and advances given to customers	Undue	Until 30 days	31 - 90 days	91 - 180 days	181 - 270 days	Over 270 days
31 December 2009							
Legal entities	432,917	413,461	3,396	931	450	1,703	12,976
Retail	405,167	398,507	4,300	782	926	651	1
Total	**838,084**	**811,968**	**7,696**	**1,713**	**1,376**	**2,354**	**12,977**
31 December 2008							
Legal entities	357,025	340,070	4,193	508	984	747	10,523
Retail	403,733	395,920	4,317	838	1,838	820	-
Total	**760,758**	**735,990**	**8,510**	**1,346**	**2,822**	**1,567**	**10,523**

Renegotiated loans

Where possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment agreements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to impairment assessment. The amount of renegotiated loans in 2009 was KM 42,004 thousand and in 2008 was KM 33,210 thousand.

Loans and other assets written off and recorded off-balance sheet

Movements in loans and other assets written off and recorded off-balance sheet are as follows:

	Loans and receivables	Assets available for sale	Other assets	Commitments	TOTAL
31 December 2008	26,892	857	3,562	2,452	33,763
Write-offs in 2009	8,451	-	138	850	9,439
Collections	(3,419)	-	(65)	(358)	(3,842)
Total Write offs	(38)	-	(68)	(6)	(112)
31 December 2009	**31,886**	**857**	**3,567**	**2,938**	**39,248**

(all amounts are expressed in thousands of KM)

34. FINANCIAL INSTRUMENTS (continued)

Liquidity risk management

Liquidity risk is a measure of the extent to which the Bank may be required to raise funds to meet its commitments associated with financial instruments. The Bank maintains its liquidity profiles in accordance with regulations laid down by the Banking Agency of Federation of Bosnia and Herzegovina.

The Bank is exposed to daily calls on its available cash resources from overnight deposits, current accounts, maturing deposits, loan draw downs, guarantees and from margin and other calls on cash-settled derivatives. The Bank does not maintain cash resources to meet all of these needs as experience shows that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty. The Bank sets limits on the minimum proportion of maturing funds available to meet such calls and on the minimum level of interbank and other borrowing facilities that should be in place to cover withdrawals at unexpected levels of demand.

The following tables detail the Bank's remaining contractual maturity for its financial assets and non-derivative financial liabilities. The tables have been drawn up based on the undiscounted cash flows of financial assets / liabilities based on the earliest date on which the Bank can be required to receive or pay. The table includes both interest and principal cash flows.

	Less than 1 month	**1-3 months**	**3 months to 1 year**	**1-5 years**	**5+ years**	**Total**
31.12.2009						
Cash and balances with Central bank	189,293	-	-	-	-	189,293
Placement with other banks	134,092	-	-	-	-	134,092
Loans and receivables	49,200	55,271	268,330	412,982	330,998	1,116,781
Assets available for sale			498	55		553
Other financial assets	7,285				2,352	9,637
TOTAL ASSETS	**379,870**	**55,271**	**268,828**	**413,037**	**333,350**	**1,450,356**
31.12.2008						
Cash and balances with Central bank	143,555	-	-	-	-	143,555
Placement with other banks	105,487	-	-	-	-	105,487
Loans and receivables	43,049	53,378	232,647	373,173	339,226	1,041,473
Assets available for sale			478	62		540
Other financial assets	6,683	-	-	-	2,967	9,650
TOTAL ASSETS	**298,774**	**53,378**	**233,125**	**373,235**	**342,193**	**1,300,705**

(all amounts are expressed in thousands of KM)

34. FINANCIAL INSTRUMENTS (continued)

Liquidity risk management (continued)

	Less than 1 month	1-3 months	3 months to 1 year	1-5 years	5+ years	Total
31.12.2009						
Due to banks and other institutions	16,701	68,706	139,732	116,687	46,684	388,510
Subordinated debit	-	40	123	719	813	1,695
Due to customers	392,477	33,492	158,598	81,853	5,773	672,193
Other financial liabilities	7,736	-	-	-	152	7,888
TOTAL LIABILITIES	**416,914**	**102,238**	**298,453**	**199,259**	**53,422**	**1,070,286**
31.12.2008						
Due to banks and other institutions	50,693	32,920	50,393	196,427	46,220	376,653
Subordinated debit	-	40	124	11,866	1,281	13,311
Due to customers	280,122	17,708	122,623	125,468	6,798	552,719
Other financial liabilities	6,000	-	-	-	136	6,136
TOTAL LIABILITIES	**336,815**	**50,668**	**173,140**	**333,761**	**54,435**	**948,819**

The following tables details the Bank's remaining contractual maturity for its commitments and contingent liabilities.

	Less than 1 month	1-3 months	3 months to 1 year	1-5 years	5+ years	Total
31.12.2009						
Payment guarantees	622	4,193	9,143	3,538	-	17,496
Performance guarantees	801	3,547	17,277	5,683	144	27,452
Letter of credit	2,783	1,256	198	-	-	4,237
Unused portion of loans	46,607	2,149	17,961	2,321	2,109	71,147
	50,813	**11,145**	**44,579**	**11,542**	**2,253**	**120,332**
31.12.2008						
Payment guarantees	1,517	5,155	6,735	4,473	-	17,880
Performance guarantees	1,049	4,631	14,293	5,933	144	26,050
Letter of credit	505	396	249	-	-	1,150
Unused portion of loans	48,939	5,633	14,968	7,102	6,163	82,805
	52,010	**15,815**	**36,245**	**17,508**	**6,307**	**127,885**

(all amounts are expressed in thousands of KM)

34. FINANCIAL INSTRUMENTS (continued)

Liquidity risk management (continued)

The following tables details the Bank's commitments and contingent liabilities allocated according to the earliest date they can be drawn:

	Less than 1 month	1-3 months	3 months to 1 year	1-5 years	5+ years	Total
31.12.2009						
Payment guarantees	1,466	3,983	8,686	3,361	-	17,496
Performance guarantees	2,133	3,370	16,413	5,399	137	27,452
Letter of credit	2,856	1,193	188	-	-	4,237
Unused portion of loans	49,061	1,934	16,165	2,089	1,898	71,147
	55,516	**10,480**	**41,452**	**10,849**	**2,035**	**120,332**
31.12.2008						
Payment guarantees	2,335	4,897	6,398	4,250	-	17,880
Performance guarantees	2,299	4,399	13,578	5,637	137	26,050
Letter of credit	537	376	237	-	-	1,150
Unused portion of loans	52,326	5,070	13,471	6,391	5,547	82,805
	57,497	**14,742**	**33,684**	**16,278**	**5,684**	**127,885**

The Bank has access to sources of financing with total unused amount of KM 117,426 thousand (2008 - KM 48,134 thousand) at the balance sheet date. The Bank expects to meet its other obligations from operating cash flows and proceeds of maturing financial assets.

35. EVENTS AFTER THE BALANCE SHEET DATE

No events have occurred since the balance sheet data, which significantly affect the state of affairs of the Bank at the balance sheet date or which require additional disclosure.

36. APPROVAL OF THE FINANCIAL STATEMENTS

These financial statements were approved for issue by the Management Board. The Bank's Supervisory Board and the General Assembly have the power to amend these financial statements after issue.

Approved by and signed on behalf of the Management Board:

Almir Krkalić,
Director

Livio Mannoni
Executive director of Finance