HIPOTEKARNA BANKA
A.D., PODGORICA

Financial Statements
December 31, 2010

Translation of the financial statements issued in Montenegrin language

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Translation of the financial statements issued in Montenegrin language

Ernst & Young

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This is an English translation of the Report originally issued in Montenegrin language (For management purposes only)

INDEPENDENT AUDITORS' REPORT
TO THE OWNERS OF HIPOTEKARNA BANKA A.D., PODGORICA

Report on Financial Statements

We have audited the accompanying financial statements of Hipotekarna banka A.D., Podgorica (hereinafter: the Bank), which comprise the balance sheet as at December 31, 2010, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the Law on Accounting and Auditing and regulations of the Central Bank of Montenegro governing the financial reporting of banks, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' 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 about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Bank as at 31 December 2010, and of its financial performance and its cash flows for the year then ended in accordance with the Law on Accounting and Auditing and regulations of the Central Bank of Montenegro governing financial reporting of banks.

Other matter

The financial statements of the Bank for the year ended 31 December 2009 were audited by another auditor who expressed an unmodified opinion on those statements on April 26, 2010.

Report on Other Legal and Regulatory Requirements

In accordance with the Law on Accounting and Auditing and the regulations of the Central Bank of Montenegro governing financial reporting of banks, the Bank's management has prepared analyses to the financial statements which are presented on pages 35 to 47. Information presented in the analyses to the financial statements do not form an integral part of the financial statements of the Bank. This information is the responsibility of the Bank's management. This information has been properly derived from the primary financial statements, which were prepared in accordance with the Law on Accounting and Auditing and regulations of the Central Bank of Montenegro governing financial reporting of banks as presented on pages 3-6 and is based on the underlying accounting records of the Bank.

Podgorica, April 12, 2011

Ernst & Young Montenegro d.o.o.
Podgorica, Crna Gora

Stephen Fish
Partner

Danijela Dimovski
Authorized auditor

ERNST & YOUNG MONTENEGRO

INCOME STATEMENT FOR THE YEAR ENDED DECEMBER 31, 2010

In thousands of EUR	Notes	2010.	2009.
Interest income	3.1, 4a	9,634	6,827
Interest expense	3.1, 4b	(3,433)	(2,523)
Net interest income		6,201	4,304
Provisions for losses	3.6, 5	(1,334)	(404)
Net income		4,867	3,900
Fee and commission income	3.1, 6a	3,105	2,087
Fee and commission expense	3.1, 6b	(465)	(346)
Net fee and commission income		2,640	1,741
NET INTEREST, FEE AND COMMISSION INCOME		7,507	5,641
Other income, net	7	399	987
General expenses	8	(6,827)	(5,591)
NET INCOME BEFORE EXTRAORDINARY ITEMS		1,079	1,037
Extraordinary income		263	37
Extraordinary expenses		(35)	(19)
		228	18
PROFIT BEFORE TAXATION	9	1,307	1,055
Income taxes	3.3, 9	(15)	-
NET PROFIT FOR THE YEAR		1,292	1,055

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

These financial statements are approved by management of Hipotekarna banka A.D., Podgorica, on January 17, 2011 in Podgorica.

Signed on behalf of Hipotekarna banka A.D., Podgorica:

Esad Zaimović
Chief Executive Officer

Aleksandar Mitrović
Executive Director of Finance and Informatics

BILANCE SHEET AS AT DECEMBER 31, 2010

In thousands of EUR	Notes	2010	2009
ASSETS			
Cash and deposit accounts held with depository institutions	10	24,247	19,917
Securities available for sale, other than shares		42	292
Loans and leases	11	98,352	74,698
Securities held to maturity	12	1,093	1,086
Receivables in respect of custody operations		23	19
Business premises and other fixed assets	13	1,742	1,473
Acquired assets	14	485	11
Equity investments in other legal entities	15	99	7
Other assets	16	3,190	2,347
Less: Provision for potential losses on other assets	16	(485)	(263)
Total assets		128,788	99,587
LIABILITIES			
Deposits	17	85,133	69,735
Liabilities in respect of custody operations		49	387
Loans and borrowings	18	15,000	4,000
Liabilities to the Government	19	2,716	2,248
Other liabilities	20	3,773	2,392
Provisions for potential losses on off-balance sheet credit exposures	21	494	495
Total liabilities		107,165	79,257
EQUITY			
Share capital	22	16,006	16,006
Share premium		7,444	7,444
Revaluation reserves		1	-
Accumulated loss		(1,828)	(3,120)
Total equity		21,623	20,330
Total liabilities		128,788	99,587
OFF-BALANCE-SHEET ITEMS	24	289,488	198,891

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HIPOTEKARNA BANKA A.D. PODGORICA

Esad Zaimović
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Executive Director of Finance and Informatics

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STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED DECEMBER 31, 2010

In thousands of EUR	Share Capital	Share premium	Other reserves	Revaluation reserves	Accumulated loss	Total
Balance, January 1, 2009	16,006	7,444	1,849	-	(6,024)	19,275
Transfer (Note 22)	-	-	(1,849)	-	1,849	-
Profit for the year	-	-	-	-	1,055	1,055
Balance, December 31, 2009	16,006	7,444	-	-	(3,120)	20,330
The effect of reducing the market value of securities available for sale	-	-	-	1	-	1
Profit for the year	-	-	-	-	1,292	1,292
Balance, December 31, 2010	16,006	7,444	-	1	(1,828)	21,623

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

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Esad Zaimović
Chief Executive Officer

Aleksandar Mitrović
Executive Director of Finance and Informatics

CASH FLOW STATEMENT FOR THE YEAR ENDED DECEMBER 31, 2010

In thousands of EUR	Notes	2010.	2009.
CASH FLOWS FROM OPERATING ACTIVITIES			
Interest, fees and commissions received		11,745	8,709
Other proceeds		88	2
Interest and commission paid		(2,669)	(2,907)
Cash paid to employees and suppliers		(7,098)	(4,974)
Net cash inflow before changes in operating assets and liabilities		2,066	830
Changes in operating assets and liabilities			
Increase in placements to customers, net		(24,226)	(16,174)
Increase/(decrease) in other assets, net		335	52
Increase in deposits from customers		15,398	26,729
Income from custody operations		26	368
Decrease in other liabilities		(2)	(10)
Net cash inflow / (outflow) used in operating activities		(8,469)	10,965
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of equipment and intangible assets		(1,155)	(332)
Net cash outflow used in operating activities		(1,155)	(332)
CASH FLOWS FROM FINANCING ACTIVITIES			
(Outflow)/ inflow from loans and borrowings		11,507	(3,801)
(Outflow)/ inflow from purchase and sale of securities, net		158	(5)
Inflow from equity investments in other legal entities, net		-	177
Outflow from securities held to maturity, net		-	(1,086)
Net cash generated from financing activities		11,665	(4,715)
Effects of foreign exchange gains and losses		223	(370)
Net increase in cash and cash equivalents		4,330	6,378
Cash and cash equivalents, beginning of year		19,917	13,539
Cash and cash equivalents, end of year		24,247	19,917
Components of cash and cash equivalents:			
Cash and deposit accounts held with depositary institutions	3.4, 10	24,247	19,917
		24,247	19,917

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

These financial statements are approved by management of Hipotekarna banka A.D., Podgorica, on January 17, 2011 in Podgorica.

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1. FOUNDATION AND BUSINESS ACTIVITY

Hipotekarna banka A.D. Podgorica (hereinafter: the "Bank") was registered in 1995 as a shareholding company. The registration number of the Bank as recorded in the Central Registry of the Commercial Court is 4-0004632/027. The Bank is included in the Register of Security Issuers maintained by the Securities Commission under the number 3 (Decision number 02/3-1/2-01). The Bank received an operating license from the Central Bank of Montenegro; pursuant to the Decision number 26 dated November 21, 2001.

In accordance with Law on Banks, Founding Agreement, Statute and Decision of the Central Bank of Montenegro, the Bank performs depositary and crediting operations for its own account. In addition to the above, the Bank performs the following activities:

- issuance of guarantees and undertaking other off-balance sheet liabilities,
- purchase, sale and recording of receivables (factoring, forfeiting etc.),
- issuance, processing and recording of payment instruments
  - operations of payment transactions performed aboard and in the country, in accordance with regulations regulating payment transfers,
- finance leases,
- operations involving securities, in accordance with the relevant regulations,
- trading in its own and the customer's account:
  a) with payments in foreign exchange, including exchange operations,
  b) financial derivates,
- depo transactions,
- preparation of analysis and provision of credit rating information and advice on legal entities and entrepreneurs and other issues related to business operations,
- rental of safety deposit boxes,
- activities which are the part of bank activities, activities accompanying banking activities and activities directly connected with Bank's activities, in accordance with Statute.

The Bank's management bodies include: the Shareholders Assembly and the Board of Directors. The Board of Directors has two permanent bodies: Audit Board and Credit Risk Management Board. The members of the Board of Directors are elected by the Bank's Shareholders Assembly. The Board of Directors has 5 (five) members the majority of which are not the Bank's employees.

The Bank is domiciled in the city of Podgorica, at 67 Josipa Broza Tita Street. At December 31, 2010, the Bank had 155 employees (December 31, 2009: 139 employees).

2. BASIS OF PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS

2.1. Basis of Preparation and Presentation of the Financial Statements

The Bank maintains its accounting records and prepares its statutory financial statements in conformity with the Accounting and Auditing Law of Montenegro ("Official Gazette of Montenegro," no. 69/2005 and no. 80/2008) and specifically, in accordance with the relevant decision pertaining to the application of International Accounting Standards ("IAS") in Montenegro ("Official Gazette of Montenegro," numbered 69/2002). Pursuant to these provisions, International Financial Reporting Standards ("IFRS") were applied for the first time as the Bank's primary basis of accounting for the reporting period commencing on January 1, 2003.

The financial statements are presented in the format required under Articles 17 and 18 of the Accounting and Auditing Law of Montenegro and the European Union Directive numbered 86/635/EEC of December 8, 1986 which relates to the annual reports of banks and other financial institutions. Such statements represent the complete set of financial statements as defined under the law, which differ from those defined under the provisions of IAS 1, "Presentation of Financial Statements."

The accounting policies adopted in the preparation and presentation of the financial statements for the year ended December 31, 2009 differ from the IFRS requirements in respect to the calculation of allowances for the impairment of financial instruments and in respect of disclosures of financial instruments in accordance with IFRS 7 "Financial Instruments: Disclosures." The Bank calculates the amount of allowance for impairment of financial instruments in accordance with the applicable Regulations of the Central Bank of Montenegro (Note 3.7). Such a policy might result in significant departures from the amounts which would be determined, had the allowances for impairment of financial instruments been estimated based on discounted expected future cash flows by applying the original effective interest rate, as required by IAS 39, "Financial Instruments: Recognition and Measurement." In addition, the Bank suspends the calculation of interest on loans classified in category C, D and E ("non-performing assets" in accordance with the Decision of the Central Bank of minimum standards for credit risk management in banks), where the decision also regulates the risk assets classified in category E to be written off from the balance sheet and be recorded in off balance sheet as "written off loans". "

Due to the potentially significant effects of the above-described matters on reality and objectiveness of financial statements of the Bank, these financial statements cannot be described as having been prepared in accordance with International Financial Reporting Standards.

In the preparation of the accompanying financial statements, the Bank has adhered to the accounting policies described in Note 3, which are in conformity with the accounting, banking and tax regulations prevailing in Montenegro.

The official currency in Montenegro and the Bank's functional currency is the Euro (EUR).

2.2. Use of Estimates

The presentation of financial statements requires the Bank's management to make the best possible estimates and reasonable assumptions that affect the value of assets and liabilities, as well as the disclosure of contingent liabilities and receivables as of the date of the preparation of the financial statements, and the income and expenses arising during the accounting period. Estimates and judgments relate to historical experience and other factors, including the expectations in respect to future events believed to be reasonable in the given circumstances, where the results provide goods grounds for the estimated carrying value of assets and liabilities that cannot be clearly derived from other sources. These estimations and assumptions are based on information available as of the financial statements' preparation date. However the Bank's operating results may vary from the estimated values.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

3.1. Interest, Fee and Commission Income and Expense Recognition

Interest income and interest expense, including penalty interest and other income and expenses related to interest bearing assets and liabilities are accounted for on an accrual basis. Fee and commission income and expenses from banking services are determined when due for settlement and/or collection.

Until January 1, 2009, origination fees for loans, guarantees and other sureties, as well as fee expenses charged to the Bank based of its borrowings had been included within income and expenses in the moment of service rendering or when such fees were due for settlement. As of the aforementioned date, origination fees for loans, guarantees and other sureties, as well as fee expenses charged to the Bank based of its borrowings are recognized in accordance with IAS 18, "Revenues" and IAS 39, "Financial Instruments: Recognition and Measurement," loan origination fees are considered to be an integral part of an ongoing involvement with the resultant financial instrument, which is deferred and recognized as an adjustment to the effective interest rate by applying the pro rata method.

3.2. Foreign Exchange Translation

Transactions denominated in foreign currencies are translated into euros at the official exchange rates prevailing on the Interbank Market, at the date of each transaction.

Assets and liabilities denominated in foreign currencies are translated into euros by applying the official exchange rates, as determined on the Interbank Market that are prevailing at the balance sheet date.

Net foreign exchange gains or losses arising upon the translation of transactions, and the assets and liabilities denominated in foreign currencies are credited or charged to the Income statement, as gains or losses due foreign exchange translation.

Commitments and contingent liabilities denominated in foreign currencies are translated into euros by applying the official exchange rates prevailing on the Interbank Market, at the balance sheet date.

3.3. Taxes and Contributions

Income Taxes

Current Income Taxes

Income taxes are calculated and paid in conformity with the income tax regulations defined under the Montenegro Tax Law ("Official Gazette of Montenegro," nos. 80/2004, 40/2008 and 86/09) as per the effective proportional tax rate of 9% on taxable income.

A taxpaying entity's taxable income is determined based upon the income stated in its statutory statements of income following certain adjustments to its income and expenses performed in accordance with Montenegro Tax Law (Articles 8 and 9, regarding the adjustment of income and Articles 10 to 20 pertaining to the adjustment of expenses).

Capital losses may be set off against capital gains earned in the same year. In case there are outstanding capital losses even after the set-off of capital losses against capital gains earned in the same year, these outstanding losses are available for carryforward in the ensuing 5 years.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3.3. Taxes and Contributions (continued)

Income Taxes (continued)

Current Income Taxes (continued)

Montenegro tax regulations do not envisage that any tax losses of the current period be used to recover taxes paid within a specific carryback period. However, any current year losses reported in the annual corporate income tax returns may be carried forward and used to reduce or eliminate taxes to be paid in future accounting periods, but only for an ensuing period of a maximum of five years.

Deferred Income Taxes

Deferred income tax is determined using the balance sheet liability method, for the temporary differences arising between the tax bases of assets and liabilities, and their carrying values in the financial statements. The currently-enacted tax rates at the balance sheet date are used to determine the deferred income tax amount. Deferred tax liabilities are recognized for all taxable temporary differences. Deferred tax assets are recognized for the deductible temporary differences, and the tax effects of income tax losses and credits available for carry forward, to the extent that it is probable that future taxable profit will be available against which deferred tax assets may be utilized.

Taxes, Contributions and Other Duties Not Related to Operating Results

Taxes, contributions and other duties that are not related to the Company's operating results, include property taxes, employer contributions on salaries, and various other taxes and contributions paid pursuant to republic and municipal regulations.

3.4. Cash and Cash Equivalents

For purposes of the cash flow statement, "Cash and cash equivalents" include cash and balances on the current accounts held with the Central Bank of Montenegro, including the obligatory reserve, and balances held on the accounts of other banks in the country and abroad.

3.5. Available-for-Sale Securities

Securities available for sale comprise securities that cannot be classified as trading securities or as securities held to maturity and comprise equity investments in other legal entities. Subsequent to initial recognition, securities available for sale are stated at fair value. The fair value of securities quoted on the stock exchange is based on their asking prices. Unrealized gains and losses from securities available for sale are recorded within revaluation reserves, until such security is sold, collected or realized in any other way or until such security has suffered permanent impairment. Upon the disposal of securities available for sale are disposed of or when their value has suffered an impairment, the accumulated fair value adjustments are recognized within equity and recorded in the income statement.

Dividends from securities available for sale are recognized in the income statement when the right to such receivable has been established.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3.6. Loans

Loans originated by the Bank are recorded in the books of account at the moment of the transfer of funds to the loan beneficiary.

Loans originated by the Bank are stated in the balance sheet in the amount of placement originally approved less net of principal repaid and an allowance for impairment which is based on an evaluation of the specifically-identified exposures which serves to cover any losses inherent in the Bank's loan portfolio. The Bank's management applies the methodology prescribed by the Central Bank of Montenegro in its evaluation of the risks and resulting estimations of such allowances (Note 3.7).

3.7. Allowances for Impairment and Provisions for Potential Losses

The Decision issued by Central Bank of Montenegro regarding to minimal standards for managing credit risk in banks ("Official Gazette of Montenegro," number 60/2008 and 41/2009) i.e. in accordance with Decision on temporary measures for managing credit risk in banks ("Official Gazette of Montenegro," number 64/2009, 87/2009 and 66/2010) set forth the following: elements of credit risk management, minimum criteria and manner of classifying assets and off-balance sheet items which render the Bank susceptible to interest rate risk, manner of calculation and suspension of unpaid interest, manner of determining the minimum provisions for potential losses contingent on the Bank's exposure to credit risk. The Bank's risk-weighted assets, within the meaning of this Decision, are comprised of loans, interest, fees and commission, lease receivables, deposits with banks, advances and all other items included in the balance sheet exposing the Bank to default risk, as well as guarantees issued, other sureties, effectuated letters of credit and approved, but undrawn loan facilities, as well as all other off-balance sheet items comprising the Bank's contingent liabilities.

Pursuant to the aforementioned Decision, loans and other risk-weighted assets are classified into the following categories:

- A category ("Pass") – including assets assessed as collectible in full and as agreed;
- B category ("Special Mention") – with B1 and B2 subcategories including items for which there is low probability of loss, but which, still the same, require special attention, as potential risk, if not adequately monitored, could diminish collectability;
- C category ("Substandard assets") – with C1, C2, C3 and C4 subcategories for which there is high probability of loss, due to the clearly identified collectability issues;
- D category ("Doubtful assets") – including items the collection of which is, given the creditworthiness of loan beneficiaries, quality of collaterals, highly unlikely;
- E category ("Loss") – including the items which are uncollectible in full, or will be collectible in an insignificant amount

The estimated amount of provision for potential losses is not computed for the Bank's placements classified in the category A. The estimated reserve for potential losses is calculated as 3% of the placements classified in category B, from 15% to 50% to the placements classified into category C, 75% to the placements of category D, and 100% of the placements under category E.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3.7. Allowances for Impairment and Provisions for Potential Losses (continued)

Moreover, as in accordance with the provisions of the aforecited regulation, the Bank is to suspend any accrued, uncollected interest and should terminate any further accruals of interest on its non-performing assets, with the exception of the non-performing assets that are secured by quality collateral and are in the process of collection, to the extent that such asset recoveries are anticipated within a reasonable period of time (generally defined as not exceeding three months). Following the suspension of interest accruals on non-performing assets, the Bank remains under an obligation to record the subsequent, matured interest on the same basis, on its off-balance sheet records and upon classification, designates the accrued income into E category. The Decision further prescribes that the risk-weighted assets be classified into E category be written off from the off-balance sheet records under the heading of "Loans written off."

Pursuant to the Decision, provision for potential losses contingent on assets is calculated based on the carrying value net of any deductible items of collaterals based on:

- Monetary deposits,
- Irrevocable guarantees of the Government of Montenegro and
- Irrevocable guarantees of the countries or central banks of the OESD member countries, the banks with credit rating better than A+ pursuant to the ratings of the agency Standard & Poor's, i.e., any equivalent rating of other internationally acclaimed rating agencies and legal entities whose business operations are under the control of Central Bank of Montenegro.

In accordance with amendments to the abovecited decisions on minimum standards for credit risk management in banks, the Bank has applied the following percentages and days of delay by risk categories:

Risk category	As at December 31, 2010		As at December 31, 2009	
	% reserves	Days of delay	% reserves	Days of delay
A	-	<30	-	<30
B1	3	31-90	3	31-60
B2	-	-	3	61-90
C1	15	91-150	20	91-110
C2	30	151-210	30	111-130
C3	50	211-270	40	131-150
C4	-	-	50	151-180
D	75	271-365	75	181-270
E	100	>365	100	>271

3.8. Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that an entity has the positive intention and ability to hold to maturity. In case the Bank sells a significant amount of held to maturity investments, the entire category is reclassified as available for sale.

3.9. Equity investments in other legal entities

Equity investments in other legal entities are carried at cost which is believed by the management to approximate the fair value of these instruments.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3.10. Business premises, other fixed assets and intangible assets

Business premises and other fixed assets are those assets whose useful life is more than one year. Business premises, other property, equipment and intangible assets at December 31, 2010 are stated at cost less accumulated depreciation and/or amortization. Cost represents the prices billed by suppliers together with all costs incurred in bringing the respective asset to the location and condition necessary for its intended use.

Additional costs: costs of replacing equipment parts (installation of new spare parts), the cost of repairs and general repair of business premises are recognized as increasing the present value of business premises i.e. equipment, if it is likely that on this basis to get to the inflow of future economic benefits and if those costs could be reliably measured.

The costs arising from maintenance of equipment: replacement and installation of small spare parts and supplies, as well as the costs of everyday repairs are considered expense when incurred.

Losses or gains incurred in the disposal or retirement of business premises and equipment are determined as the difference between the sales and the current value at which the business premises and equipment are lead, and recognized as the benefit or as a part of the income statement over the period in which the disposal occurred or retirements.

Intangible assets consist of software and licenses. Intangible assets acquired are capitalized at cost value of the transaction. After initial recognition, intangible assets are carried at cost value less accumulated depreciation and eventual impairment.

Costs that could be directly linked with certain software and will generate economic benefits for a period longer than one year are recorded as intangible assets. Maintenance and development of computer software are recorded as an expense as incurred.

Depreciation is provided for on a straight-line basis to the cost of business premises and other fixed assets in order to write them off over their expected useful lives. Depreciation is calculated using the following prescribed annual rates:

Items	Depreciation rate (%)	Rate recognized in taxable income (%)
Buildings	2.00	5.00
Motor vehicles	15.00	15.00
Furniture and equipment	15.00	15.00–20.00
Computers and computer equipment	33.33	30.00
Intangible assets	20	20.00-30.00

In accordance with Article 13 paragraph 6 of the Income Tax Law ("Official Gazette of Montenegro" no. 80/2004, 40/2008 and 86/2009) amortization of licenses, other intangible assets and buildings for tax purposes is calculated using the proportional method, i.e. equipment and application software using digressive method for the entire period, regardless of the date of activation.

The calculation of depreciation of business premises and other fixed assets commences when an asset is placed into use.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3.11. Equity

The Bank's equity includes share capital, share premium, the Bank's reserves, as well as retained earnings (accumulated loss).

The share capital of the Bank is formed from the assets invested by the founders and shareholders of the Bank in the pecuniary or non-pecuniary form. The Law on Securities sets forth that securities are dematerialized and exist in an electronic form in the system of the Central Depositary Agency. The excerpt obtained from the Registry of the Central Depositary Agency is the only and exclusive proof of ownership over securities.

Once all reserves available have been exhausted, the Bank uses capital for performing its banking operations, for equity investment in other legal entities, as well as to cover risks.

As in accordance with the Decision on capital adequacy in banks ("Official Gazette of Montenegro," nos. 60/2008 and 41/2009), the Bank's own assets represent the sum of the Bank's core capital, its supplementary capital I and supplementary capital II, net of deductibles.
The Bank's core capital is comprised of basic elements of the Bank's own funds: collected share premiums; reserves allocated profit before taxation (legal, statutory and other disclosed reserves); prior year retained earnings; profit for the year for which the Shareholding Assembly enacted a Decision to be included within the Bank's core capital and capital gains realized in the purchase and sale of the Bank's own shares. Deductibles applied in the calculation of the Bank's core capital include prior period losses; loss for the year; capital losses incurred based on the acquisition and sale of own shares; intangible assets in the form of goodwill, licenses, patents, trademarks and concessions; nominal amounts of own shares acquired, exclusive of cumulative preferred shares and outstanding portion of provisions for potential losses determined in the process control.

Supplementary capital I is comprised of nominal value of preferred cumulative shares; general reserves up to 1.25% of the Bank's total risk-weighted assets; revaluation reserves; and subordinated debt, if any; hybrid instruments; and revaluation reserves. Deductibles applied in calculating supplementary capital involve the acquired own preferred cumulative shares and receivables and contingent liabilities secured by hybrid instruments or subordinated debts up to the amount in which these instruments are included in supplementary capital I.

Supplementary capital of a bank includes subordinated debts, meeting the following conditions: debt has been repaid in full; the bank does not guarantee debt repayment in any way; in case of the bank's bankruptcy or liquidation, such debt is settled after all other amounts owed to creditors; the relevant agreement includes a clause banning the payment of interest and principal, even upon debt maturity, if the settlement of such debt would reduce the bank's assets below the prescribed level; debt maturity is determined in advance, is longer than two years and cannot be repaid in advance of the agreed maturity date; the written agreement governing subordinated debt contains clause stipulating that subordinated debt is not to be considered as a deposit.

In order to cover risk inherent in operations, the Bank's provisions are formed. Provisions are formed based on the Decision issued by the Board of Directors of the Bank from the portion of profit earned by the Bank in its operations.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3.12. Employee benefits

Employee taxes and contributions for social security

Pursuant to the regulations effective in Montenegro, the Bank has an obligation to pay contributions to various state social security funds. These obligations involve the payment of contributions on behalf of an employee, by the employer, in an amount calculated by applying the specific, legally-prescribed rates. The Bank is also legally obligated to withhold contributions from gross salaries to employees, and on their behalf to transfer the withheld portions directly to the appropriate government funds. These contributions payable on behalf of the employee and employer are charged to expenses in the period in which they arise.

Retirement benefits or other long-term employee benefits

In accordance with the Collective Bargaining Agreement, the Bank is under obligation to pay retirement benefits to an employee upon his/her regular retirement in the amount of 6 net average salaries earned by the Bank's employees in the month in which payment is made. The Bank's financial statements as of and for the year ended December 31, 2009 include provisions calculated by an independent certified actuary and as at December 31, 2010, based on the estimated present value of assets to be used for retirement benefits payable to vesting employees.

3.13. Fair Value

In accordance with International Financial Reporting Standards, the fair value of financial assets and liabilities should be disclosed in the Notes to the Financial Statements. For these purposes, the fair value is defined as an amount at which an asset can be exchanged, or a liability settled, between knowledgeable willing parties in an arm's-length transaction. The Bank should disclose the fair value information of those components of assets and liabilities for which published market information is readily available, and for which their fair value is materially different from their recorded amounts.

In Montenegro, sufficient market experience, stability and liquidity do not exist for the purchase and sale of receivables, investments and other financial assets or liabilities, for which published market information is presently not readily available. Fair value cannot readily be determined in the absence of active capital and financial markets, as generally required under the provisions of IFRS/IAS. In the opinion of the Bank's management, the reported carrying amounts are the most valid and useful reporting values under the present market conditions in accordance with the accounting regulations of Montenegro and regulations of the Central Bank of Montenegro governing the financial reporting in banks.

4. INTEREST INCOME AND EXPENSE

a) Interest Income

In thousands of EUR	2010	2009
Deposits with::		
- foreign banks	51	22
- Central bank	11	18
	62	40
Loans to:		
- corporate customers	6,463	4,129
- retail customers	3,109	2,658
	9,572	6,787
	9,634	6,827

b) Interest Expense

In thousands of EUR	2010	2009
Deposits with:		
- financial institutions	1,077	303
- state organisation	120	88
- corporate customers	837	595
- retail customers	1,314	1,127
- other	85	21
	3,433	2,134
Loans and other borrowings	-	389
	3,433	2,523

5. PROVISIONS FOR LOSSES

a) Charge for the year

In thousands of EUR	2010	2009
Net, provisions / (reversal of provisions):		
- deposits in foreign banks	4	-
- loans and leases	1,220	257
- equity investments in other legal entities	-	(2)
- interest receivables	147	17
- country risk	45	(3)
- off-balance sheet items	20	(111)
- employee benefits (note 20)	3	-
- other receivables of the debtor who has started a process of reorganization (note 16)	(112)	247
- other	7	(1)
	1,334	404

5. PROVISIONS FOR LOSSES (continued)

b) Movements on the accounts of allowance for impairment of bad debts and provisions

In thousands of EUR	Deposits in foreign banks (note 10)	Loans and leases (note 11)	Equity investments in other legal entities (note 15)	Interest receivables (note 16)	Country risk (note 16)	Other receivables of the debtor who has started a process of reorganization (note 16)	Acquired assets (notes 14 and 16)	Other receivables (note 16)	Off-balance sheet items (note 21)	Total
Balance, January 1, 2009	-	2,879	2	10	12	-	-	2	306	3,211
Charge for the year	-	257	-	17	-	247	-	-	-	521
Reversal of provisions	-	-	(2)	-	(3)	-	-	(1)	(111)	(117)
Transfer to off-balance sheet items	-	(1,051)	-	(21)	-	-	-	-	-	(1,072)
Balance, December 31, 2009	-	2,085	-	6	9	247	-	1	195	2,543
Charge for the year	4	1,220	-	147	45	-	-	7	20	1,443
Reversal of provisions	-	-	-		-	(112)	-	-	-	(112)
Transfer to/from off-balance sheet items	-	(648)	-	(143)	-	-	268	10	-	(513)
Balance, December 31, 2010	4	2,657	-	10	54	135	268	18	215	3,361

6. FEE AND COMMISSION INCOME AND EXPENSE

a) Fee and Commission Income

In thousands of EUR	2010	2009
Loan origination fees	707	531
Fee and commission income from off-balance-sheet operations	348	151
Fee and commission income from payment transfers	1,530	830
Fee and commission income from brokerage services	4	125
Fee and commission income from custody services	12	180
Fee and commission income from credit cards	181	73
Other fee and commission income	323	197
	3,105	2,087

b) Fee and Commission Expense

In thousands of EUR	2010	2009
Fees and commissions payable to the Central Bank	159	141
Fee and commission expense from other banks	70	46
Fee and commission for deposit insurance	187	119
Other fee and commission expense	49	40
	465	346

7. OTHER INCOME, NET

In thousands of EUR	2010	2009
Net gains on unrealized and realized foreign exchange fluctuations	223	(4)
Collected receivables previously written off	83	741
Income from trading securities	88	248
Gains on acquired assets sold, net	5	-
Miscellaneous income	-	2
	399	987

8. GENERAL EXPENSES

In thousands of EUR	2010	2009
Net salaries	1,684	1,369
Taxes and contributions on salaries	1,181	876
Meals and transport	47	68
Remunerations to the members of the Board of Directors and Audit Board	91	98
Severance payments for voluntary leave	27	42
Costs for processing center services	60	35
Business trip expenses	75	79
Entertainment	95	51
Rentals	1,010	878
Maintenance of property and equipment	269	194
Depreciation and amortization charge:		
- property, plant and equipment (note 13)	368	293
- intangible assets (note 16)	238	185
Security services costs	223	142
Insurance premiums	63	58
Taxes	67	32
Advertising	250	248
Professional services costs	211	217
CDA and brokerage services costs	30	228
Telecommunication and postage	174	136
Electricity, fuel and water charges	57	67
Office material	83	68
Temporary engagement compensations	47	25
Sponsorship	92	12
Migration expenses	25	-
Write off bad debt receivables	32	-
Bills and checks expenses	30	27
Miscellaneous expenses	298	163
	6,827	5,591

9. INCOME TAXES

a) Components of Income Taxes

In thousands of EUR	2010	2009
Current income tax expenses	-	-
Deferred income tax expenses	15	-
	15	-

9. INCOME TAXES (continued)

b) Numerical Reconciliation between Tax Expense and the Product of Accounting Results Multiplied by the Applicable Tax Rate

In thousands of EUR	2010	2009
Net profit before tax	1,307	1,055
Income tax at the statutory tax rate of 9%	118	95
Unrecognized tax assets arising from tax loss carry forwards	(121)	(131)
Tax effect of expenditures not recognized for tax purposes	3	-
Other	15	36
Tax effects on the income statement	15	-
Effective income tax rate	1.15%	0.00%

c) Deferred Tax Liabilities

Deferred tax liabilities as at December 31, 2010 in the amount of EUR 26 thousand (December 31, 2009: EUR 11 thousand) (Note 20) are associated with the taxable temporary differences arising between the tax base at which business premises and other fixed assets are recognized in the tax balance and the carrying value of such assets in Bank's financial statements.

10. CASH AND DEPOSIT ACCOUNTS HELD WITH DEPOSITORY INSTITUTIONS

In thousands of EUR	December 31, 2010	December 31, 2009
Cash on hand:		
- in EUR	1,626	1,683
- in foreign currency	103	135
Gyro account	6,928	8,462
Correspondent account with foreign banks	8,961	4,328
Obligatory reserves with the Central Bank of Montenegro	3,444	3,443
Time deposits with foreign banks	3,014	1,819
Deposits with domestic banks	175	47
	24,251	19,917
Minus: Allowance for impairment (note 5)	(4)	-
	24,247	19,917

The Bank's obligatory reserves at December 31, 2010 were set aside in accordance with the Decision of Central Bank of Montenegro Regulation with respect to the "Reserve Requirements for Banks to Be Held with the Central Bank of Montenegro" (Official Gazette of Montenegro no. 9/2007, 5/2008, 15/2009 and 41/2009). Pursuant to the aforecited, the obligatory reserve is to be calculated by applying the reserve percentages of 10%.

The obligatory reserve is to be calculated by applying the aforementioned ratios on an average amount on sight and time deposits from the first accounting period in June 2009. If the average amount of deposits is lower than the average amount of deposits from the first accounting period in June 2009, the calculation of the obligatory reserve is made by applying a rate of 10% on the average amount of total demand and time deposits.

10. CASH AND DEPOSIT ACCOUNTS HELD WITH DEPOSITORY INSTITUTIONS (continued)

The Bank's obligatory reserves represent the minimum deposits set aside onto domestic accounts of obligatory reserves and/or onto the accounts of the Central Bank of Montenegro held abroad. In accordance with the aforementioned Decision, the Bank can hold up to 25% of the Bank's obligatory reserve requirements issued by the Government of Montenegro. For the amount of 25% of the obligatory reserve requirement deposited by banks, the Central Bank calculates interest at the annual rate of 1% up to the eighth day of the month for the preceding month. The obligatory reserve is held in EUR.

As of December 31, 2010, time deposits with foreign banks in the total amount of EUR 3,014 thousand mostly relate to a deposit placed with Pro Bank D.D., Maribor – Republic of Slovenia in the amount of EUR 3,012 thousand over the period of one to six months with an annual interest rate of 1.8%.

As of December 31, 2010, time deposits with domestic banks in the total amount of EUR 175 thousand mostly relate to a non interest deposit for VISA and MASTER credit cards in the amount of EUR 121 thousands and a non interest deposit in the amount of EUR 50 thousands placed with Atlas bank A.D., Podgorica.

11. LOANS AND LEASES

In thousands of EUR	December 31, 2010	December 31, 2009
Matured loans:		
- state-owned corporate entities	-	251
- privately-owned corporate entities	1,865	802
- non-profit organizations	810	615
- retail customers	851	609
- other	9	-
Short-term loans:		
- privately-owned corporate entities	26,358	20,517
- non-profit organizations	119	60
- municipalities (public organisations)	85	-
- corporate entities with majority state-ownership	3,317	2,007
- retail customers	2,065	4,299
- other	434	70
Long-term loans, including current portions:		
- privately-owned corporate entities	39,332	27,523
- corporate entities with majority state-ownership	3,523	719
- non-profit organizations	49	75
- retail customers	22,158	19,236
- municipalities (public organisations)	34	
	101,009	76,783
Minus: Allowance for impairment (note 5)	(2,657)	(2,085)
	98,352	74,698

11. LOANS AND LEASES (continued)

Short-term loans to corporate entities with majority state-ownership are approved for current assets and mature over the period from 3 to 12 months, while long-term loans are approved for the period from 12 to 180 months and are mostly originated to corporate entities involved in trade, transport, warehousing, postal services and telecommunications and civil engineering. Short-term loans to corporate entities are mostly approved at an interest rate ranging between 5.5% and 16.5% annually and the same interest rate is applied to long-term loans. If the customer takes a loan based on 100% of the time deposit, interest rate is a deposit/passive interest of + 2% -4%. The interest rate on loans approved to customers whose guarantees are realized ranged from 19.5% to 23.25% per annum.

Short-term loans to retail customers are approved from one to twelve month maturities. Long-term loans to retail customers encompass loans for the renovation of housing and business premises, loans for the purchase of consumables and other purposes, approved for the period from 13 months to 20 years, at an interest rate ranging from 1% to 2% on monthly basis.

The geographic risk concentration within the customer loan portfolio mainly includes customers domiciled in Montenegro and Republic of Croatia.

The concentration of total gross loans to customers per separate fields of industry as of December 31, 2010 and 2009 was as follows:

In thousands of EUR	December 31, 2010	December 31, 2009
Agriculture, hunting and fishing	1,000	-
Civil engineering	4,094	2,705
Energy and mining	64	2,087
Trade	28,948	24,620
Services, tourism, accommodation industry	1,967	891
Transport, warehousing, postal services and communication	11,347	9,289
Administration and other public services	3,800	949
Real estate trade	3,209	477
Banks and other financial institutions	742	1,141
Retail customers	25,491	24,142
Other	20,347	10,482
	101,009	76,783

12. SECURITIES HELD-TO-MATURITY

Securities held to maturity as at December 31, 2010 in the amount of EUR 1,093 thousand (December 31, 2009: EUR 1,086 thousand) relate to treasury bills of the Government of Montenegro, whose expiry term is March 1, 2011. Treasury bills earned interest rate of 3.95% per annum. The bank holds 11,000 bills, with a total nominal value amounts to EUR 1,100 thousand.

Up to the date of preparation of these financial statements, the Bank has reinvested the funds in the purchase of 11.000 new bills the Government of Montenegro which mature on August 3, 2011 with interest rate of 3.65% per annum.

13. BUSINESS PREMISES AND OTHER FIXED ASSETS

The movements for 2010 and 2009 are shown in the following table:

In thousands of EUR	Buildings	Computer equipment	Other equipment	Construction progress	Total
Cost					
Balance, January 1, 2009	377	712	1,089	161	2.339
Additions	-	-	134	231	365
Transfers	-	77	177	(254)	-
Sales and disposals	-	(64)	(27)	-	(91)
Balance, December 31, 2009	377	725	1,373	138	2,613
Additions	1	60	-	594	655
Transfers	-	213	492	(705)	-
Sales and disposals	-	(42)	(52)	-	(94)
Balance, December 31, 2010	378	956	1,813	27	3,174
Accumulated depreciation					
Balance, January 1, 2009	38	590	309	-	937
Charge for the year (note 8)	7	95	191	-	293
Sales and disposals	-	(64)	(26)	-	(90)
Balance, December 31, 2009	45	621	474	-	1,140
Charge for the year (note 8)	8	106	254	-	368
Sales and disposals	-	(42)	(34)	-	(76)
Balance, December 31, 2010	53	685	694	-	1,432
Net book value:					
- December 31, 2010	325	271	1,119	27	1,742
- December 31, 2009	332	104	899	138	1,473

At December 31, 2010 there were no encumbrances over the Bank's assets to serve as collateral for timely and regular repayment of loans and other liabilities.

14. ACQUIRED ASSETS

Acquired collaterals as at December 31, 2010 amounted to EUR 485 thousand (December 31, 2009: EUR 11 thousand) and totally relate to acquired collaterals that are expressed in the value of total outstanding receivables. The Bank has as of December 31, 2010 shown impairment of acquired value of these collaterals in the amount of EUR 268 thousand (Notes 5 and 16).

15. EQUITY INVESTMENTS IN OTHER LEGAL ENTITIES

In thousands of EUR	December 31, 2010	December 31, 2009
Equity investments in financial institutions:		
- Tržište novca A.D., Beograd	2	2
- S.W.I.F.T. SRL	5	5
	7	7
Equity investments in non financial institutions abroad:		
- Naftna industrija Srbije („NIS“) A.D., Novi Sad – Republic of Serbia	47	-
Equity investments in domestic non financial institutions:		
- Bridgemont D.O.O., Podgorica	2	-
- Crnogorski Telekom A.D, Podgorica	32	-
- Zetatrans A.D , Podgorica	3	-
- Prenos A.D., Podgorica	5	-
- Kombinat aluminijuma Podgorica A.D., Podgorica	2	-
- Luka Bar A.D., Bar	1	-
	45	-
	99	7

16. OTHER ASSETS

In thousands of EUR	December 31, 2010	December 31, 2009
Interest receivables	952	550
Fee and commission receivables	147	124
Intangible assets	705	555
Prepayments	566	141
Advances paid	80	13
Other receivables from the debtor in the process of reorganization	449	846
Receivables for reimbursements of costs	89	62
Receivables from employees	135	36
Other receivables	67	20
	3,190	2,347
Allowance for potential losses contingent on other assets		
- interest (note 5)	10	6
- country risk (note 5)	54	9
- other receivables from the debtor in the process of reorganization (note 5)	135	247
- acquired assets (note 5)	268	1
- sundry assets	18	-
	485	263
	2,705	2,084

16. OTHER ASSETS (continued)

The movements on intangible assets for 2010 and 2009 were as follows:

In thousands of EUR	2010	2009
Cost		
Balance, January 1,	968	910
Additions	390	58
Disposals	(13)	-
Balance, December 31,	1,345	968
Accumulated depreciation		
Balance, January 1,	413	228
Charge for the year (note 8)	238	185
Disposals	(11)	-
Balance, December 31,	640	413
Net book value		
- December 31,	705	555

At December 31, 2010, intangible assets in the amount of EUR 705 thousand mainly related to investment in software totalling EUR 285 thousand, the license in the amount of EUR 143 thousand and leasehold improvements in the amount of EUR 277 thousand.

17. DEPOSITS

In thousands of EUR	December 31, 2010	December 31, 2009
Sight deposits:		
- government agencies	1,732	1,447
- funds	34	250
- municipalities (public organizations)	72	105
- corporate entities with majority state - ownership	6,109	900
- privately-owned corporate entities	15,511	19,749
- banks	165	435
- other financial institutions	925	366
- non-profit organizations	2,303	1,747
- retail customers	11,111	5,348
- other	42	670
Short-term deposits:		
- government agencies	1,240	508
- funds	800	100
- corporate entities with majority state - ownership	639	2,332
- privately-owned corporate entities	11,518	5,492
- banks	2,725	6,078
- other financial institutions	6,636	3,551
- non-profit organizations	682	711
- retail customers	19,452	13,677
Long-term deposits:		
- privately-owned corporate entities	781	457
- non-profit organizations	23	21
- other financial institutions	121	-
- retail customers	2,512	5,791
	85,133	69,735

Sight deposits placed by retail customers denominated in EUR accrue interest at the rate ranging from 0.25% to 1% annually. Retail sight deposits in foreign currency are deposited at an interest rate ranging from 0.2% to 1.1% annually, depending on the currency.

Short-term and long-term deposits of retail customers denominated in EUR are placed at an interest rate ranging from 0.1% to 9% annually, depending on the amount of deposit being placed and chosen savings arrangement (up to EUR 5 thousand, from EUR 50 thousand and over EUR 50 thousand). Short-term and long-term deposits of retail customers in foreign currencies are placed at an interest rate ranging from 0.9% to 6.1% annually, depending on the currency.

Short-term deposits of corporate entities denominated in EUR are placed at interest rates ranging from 0.25% to 8.5% annually, depending on the depositing period and the amount of deposit being placed (up to EUR 50,000 thousand, from 50,000 thousand to 100,000 thousand and over 100,000 thousand). Short-term deposits of corporate entities in foreign currencies accrue interest at rates ranging from 0.75% to 2.7%.

Long-term deposits of corporate entities were placed at an interest rate ranging from 0.1% to 8% annually, depending on the depositing period and currency.

Sight deposits of corporate entities, public and other organizations bear interest at the rate ranging from 0% to 2.25% annually.

18. LOANS AND BORROWINGS

In thousands of EUR	Period/ Year	Anally interest rate	December 31, 2010	December 31, 2009
Long-terms loans approved by domestic creditors				
The European Fund for Southeast Europe ("EFSE") Montenegro B.V.	5	5.43%	3,000	-
			3,000	-
Long-terms loans approved by foreign creditors				
European Investment Bank ("EIB")	12	4.032%	2,600	2,600
EIB	12	3.923%	1,400	1,400
EIB	12	3.604%	4,000	-
EIB	12	3.168%	2,010	-
EIB	12	3.019%	1,990	-
			12,000	4,000
			15,000	4,000

During 2010, EFSE approved to the Bank a loan in the amount of EUR 5,000 thousand with an interest rate of 5.43% for the period of five years, with a grace period of 12 months i.e. till March 22, 2012. In the period until December 31, 2010, the Bank used EUR 3,000 thousand. The loan is repaid in equal semi-annual instalments. In accordance with the provisions of the agreement concluded with EFSE, the Bank is obliged to operate in accordance with certain financial ratios/covenants. At December 31, 2010, the Bank's financial ratios are in line with the terms delineated in the relevant agreements. The Bank's commitments arising thereof amounted to EUR 2,000 thousand as of December 31, 2010. The loan approved to the Bank for the purpose of financing sub loans on condition that an individual sub loan does not exceed EUR 100 thousand, or total amount of approved sub loans to the group of related party entities does not exceed EUR 300 thousand.

As at December 31, 2010, the Bank had liabilities towards the EIB based on long-term loans totalling EUR 12,000 thousand (December 31, 2009: EUR 4,000 thousand). EIB approved to the Bank a loan in the amount of EUR 16,000 thousand and Bank's commitments arising thereof amounted to EUR 4,000 thousand as of December 31, 2010. Loans are granted to promote the development of small and medium enterprises in Montenegro, with a grace period of maximum 2 years. Loans are repaid in semi-annual annuities. As collateral against these commitments, the Bank provided the guarantee of the Government of Montenegro.

19. LIABILITIES TO THE GOVERNMENT

In thousands of EUR	Period/ Year	Annual interest rate	December 31, 2010	December 31, 2009
Investment and Development Fund of Montenegro	4-10	2%-5%	2,195	1,757
Directorate for development of small and medium-sized enterprises	5-8	0-1%	521	491
			2,716	2,248

19. LIABILITIES TO THE GOVERNMENT (continued)

At December 31, 2010, the amount of EUR 2,716 thousand owed to the Government of Montenegro is associated with payables arising from long-term borrowings from the Investment and Development Fund of Montenegro for financing small and medium enterprises with a grace period from 1 to 2 years, and payables arising from long-term borrowings in the amount of EUR 521 from the Directorate for development of small and medium-sized enterprises with a grace period from 12 to 18 months.

20. OTHER LIABILITIES

In thousands of EUR	December 31, 2010	December 31, 2009
Liabilities for accrued interest	1,263	768
Deferred loan origination fees	732	432
Accounts payable (suppliers)	149	133
Tax payables	53	10
Deferred tax liabilities (Note 9)	26	11
Liabilities for advance collection of loans	1,439	848
Provisions for employee benefits	57	54
Other liabilities	54	136
	3,773	2,392

As at December 31, 2010, provisions for employee benefits in the amount of EUR 57 thousand (December 31, 2009: 54 thousand) were determined based on the present value of future expected retirement benefits to qualifying employees.

The present value of expected future cash payments towards the employees qualified to receive retirement benefits is determined in accordance with actuarial estimation principles of an independent certified actuary as at December 31, 2010. Technical bases applied in calculating the present value of expected future retirement benefits include implementation of the following:

a) cumulative figures, prepared in accordance with the calculated possible age of the population of the Republic of Montenegro included in the population census dating from 1980 to 1982, and
b) annual interest rates of 12% used to discount future retirement payments to employees.

The movements on provisions for employee benefits are as shown in the following table:

In thousands of EUR	2010	2009
Beginning of the year	54	54
Provisions for the period (Note 5)	3	-
End of the year	57	54

21. PROVISIONS FOR POTENTIAL LOSSES CONTINGENT ON OFF-BALANCE SHEET CREDIT EXPOSURES

In thousands of EUR	December 31, 2010	December 31, 2009
Provisions for losses contingent on:		
- off-balance sheet items (Note 5)	215	195
- operational risk	279	300
	494	495

22. SHARE CAPITAL

At December 31, 2010 and 2009, the Bank's share capital was comprised of 31,305 ordinary shares with the par value of EUR 511.29. The Law on Banks ("Official Gazette of Montenegro," no. 17/2008 and 44/2010) defines that the minimum cash amount of initial capital may not be less that EUR 5,000 thousand. At December 31, 2009, the Bank's capital complied with the prescribed minimum capital requirements.

In accordance with the Decision on Minimum Standards for Credit Risk Management in Banks ("Official Gazette of Montenegro" no. 60/2008 and 41/2009), during 2009 the Bank reversed the provisions for general credit risk of EUR 1,849 thousand, which were formed in prior years, in accordance with the then Decision on the Classification of Assets in Banks, Provisions and Reserves for Credit Losses ("Official Gazette of Montenegro" no. 59/2007).

The ownership structure of the Bank's share capital as of December 31, 2010 and 2009 was as follows:

	December 31, 2010			December 31, 2009		
Shareholder	Number of shares	In thousands ofEUR	% share	Number of shares	In thousands ofEUR	% share
Flandria Participations Financieres	5,000	2,556	15.97%	5,000	2,556	15.97%
Cerere s.r.l	4,360	2,229	13.93%	4,360	2,229	13.93%
Gorgoni Antonia	3,131	1,601	10.00%	3,131	1,601	10.00%
Gorgoni Lorenzo	2,591	1,325	8.28%	2,591	1,325	8.28%
Todorović Miljan	2,316	1,184	7.40%	2,316	1,184	7.40%
Others	13,907	7,111	44.42%	13,907	7,111	44.42%
	31,305	16,006	100%	31,305	16,006	100%

23. COMPLIANCE WITH THE REGULATIONS OF THE CENTRAL BANK OF MONTENEGRO

The Bank is required to maintain certain ratios pertaining to the volume of its activities and composition of risk assets in compliance with the Law on Banks and regulations of the Central Bank of Montenegro.

In accordance with the Decision on Capital Adequacy in Banks ("Official Gazette of Montenegro," nos. 60/2008 and 41/2009), the Bank's capital comprised of the Bank's core capital and supplementary capital, minus deductions. The Bank's capital as of December 31, 2010 amounted to EUR 20,916 thousand (December 31, 2009: EUR 19,776 thousand).

The Bank's core capital formed in accordance with the Decision on Capital Adequacy in Banks, as of December 31, 2010 amounted to EUR 20,916 thousand (December 31, 2009: EUR 19,776 thousand). The Bank's capital as of December 31, 2010 is comprised of the following components: paid-in share capital at nominal value, collected share premiums and current year retained earnings as decreased by the amount of prior period losses and amount of intangible assets.

As of December 31, 2010 the Bank had no supplementary capital.

Risk-weighted balance sheet assets and off-balance sheet items formed pursuant to the Decision on Capital Adequacy in Banks, as of December 31, 2010 amounted to EUR 108,477 thousand (December 31, 2009: EUR 70,197 thousand). In accordance with the Decision on Capital Adequacy in Banks of the Central Bank of Montenegro, the Bank is under obligation to maintain the minimum capital adequacy ratio of 10%. The solvency ratio calculated by the Bank as of December 31, 2010 amounted to 15.54%

At December 31, 2010, none of the Bank's ratios departed from the minimum legal requirements set forth by the Central Bank of Montenegro.

24. OFF-BALANCE SHEET ITEMS

In thousands of EUR	December 31, 2010	December 31, 2009
Guarantees, sureties and irrevocable commitments::		
Guarantees to corporate entities:		
- payment guarantees	16,212	6,654
- performance bonds	1,047	356
- other types of guarantees	6,338	3,458
Commitments arising from undrawn loans	2,476	2,266
Letters of credit	96	120
Other off-balance sheet items:		
- commission banking services	131	131
- custody and brokerage-dealer services	14,415	7,243
- collaterals	246,954	176,949
- written-off loans receivables	1,819	1,714
	289,488	198,891

25. RELATED PARTY TRANSACTIONS

The Law on Banks ("Official Gazette of Montenegro," no. 17/2008) defines that significant influence on the Bank's operations is exercised by those persons appointing at least one representative in the Board of Directors or some similar body, either though shareholding, through agreement with the owners or otherwise. In accordance with the Law on Banks, related party transactions are presented in the following tables:

In thousands of EUR	December 31, 2010	December 31, 2009
Payables		
Demand deposits:		
- Miljan Todorović	-	6
- Gorgoni Lorenzo	12	8
	12	14
Time deposits		
- Miljan Todorovic	530	3,700
	530	3,700
Interest payables:		
- Miljan Todorović	-	3
	-	3
Total payables	542	3,717

Expenses from transactions with related parties during 2010 amounted to EUR 95 thousands (2009: EUR 363 thousands).

As at December 31, 2010, receivables from employees amounted to EUR 1,249 thousand (at December 31, 2009: EUR 909 thousand), which refer to the approved loans, claims for overdraft on bank accounts and credit cards.

During 2010, total gross remunerations paid to persons with special authorities and responsibilities amounted to EUR 556 thousand (2009: 530 thousand).

26. LIQUIDITY GAP BETWEEN FINANCIAL ASSETS AND LIABILITIES

The Bank is exposed to daily calls on its available cash resources which influence the available cash resources held on the current accounts or from deposits. The Bank does not maintain cash resources to meet all of these needs since historical experience demonstrates that a minimum level of reinvestment of maturing funds can be predicted with a high degree of certainty.

The contractual maturities of the Bank's asset and liability components as of December 31, 2010 were as follows:

In thousands of EUR	Up to one month	From 1 to 3 month	From 3 to 6 month	From 6 to 12 month	From 1 to 5 years	Over 5 years	Total
Financial assets							
Cash and deposit accounts with depository institutions	22,741	1,506	-	-	-	-	24,247
Assets for trade and available for trade, no shares	42	-	-	-	-	-	42
Loans and other receivables	8,500	15,310	13,703	20,970	32,486	10,040	101,009
Securities held to maturity	-	1,093	-	-	-	-	1,093
Other financial assets including investments in shares	1,962	-	-	74	484	-	2,520
Total	33,245	17,909	13,703	21,044	32,970	10,040	128,911
Financial liabilities							
Deposits	21,444	27,830	13,650	18,863	2,928	418	85,133
Obligations based on loans and other borrowings	-	-	-	101	6,692	8,207	15,000
Obligations to the Government	90	31	59	96	1,706	734	2,716
Other financial liabilities	471	237	589	428	504	155	2,384
Total	22,005	28,098	14,298	19,488	11,830	9,514	105,233
Maturity gap:							
- December 31, 2010	11,240	(10,189)	(595)	1,556	21,140	526	23,678
- December 31, 2009	8,166	(7,664)	466	(786)	20,871	801	21,854
Cumulative GAP:							
- December 31, 2010	11,240	1,051	456	2,012	23,152	23,678	
- December 31, 2009	8,166	502	968	182	21,053	21,854	
% of total liquidity-bearing assets:							
- December 31, 2010	10.7%	1.0%	0.4%	1.9%	22.0%	22.5%	
- December 31, 2009	10.5%	0.6%	1.2%	0.2%	27.0%	28.0%	

The Bank's liquidity, as its ability to settle its liabilities when due, principally depends upon the Bank's balance sheet structure, as well as the matching between inflows and outflows of assets.

27. INTEREST RATE RISK

The Bank is exposed to various risks associated with the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest rate risk requires special treatment under the existing local circumstances of frequent interest rate movements, and irregular capital supply and demand. Interest rate risk is unfavourable when there is fluctuation in the price of a loan in relation to the level of the effective interest rates on deposits, and the potential of a reduction in the optimal difference between the average interest rates applied to loans on one side, and to deposits on the other.

The table below shows the Bank's exposure to interest rate risk as of December 31, 2010.

In thousands of EUR	Less than One Month	From 1 to 3 Months	From 3 to 6 Months	From 6 to 12 Months	Over 1 year	Total
Interest rate sensitive assets						
Interest-bearing deposits in other institutions	2,367	1,506	-	-	-	3,873
Interest bearing securities	-	1,093	-	-	-	1,093
Loans and other receivables	8,500	15,310	13,703	20,970	42,526	101,009
Other interest-bearing assets	975	-	-	-	-	975
Total	11,842	17,909	13,703	20,970	42,526	106,950
% of the total interest-bearing assets	11.07%	16.75%	12.81%	19.61%	39.76%	100.00%
Interest rate sensitive liabilities						
Interest-bearing deposits	9,226	10,444	17,125	23,787	15,511	76,093
Interest-bearing borrowings	89	31	59	196	17,341	17,716
Total	9,315	10,475	17,184	23,983	32,852	93,809
% of the total interest-bearing liabilities	9.93%	11.17%	18.32%	25.57%	35.02%	100.00%
Interest rate exposure:						
- December 31, 2010	2,527	7,434	(3,481)	(3,013)	9,674	13,141
- December 31, 2009	6,136	2,757	(1,539)	(3,452)	14,330	18,232
Cumulative GAP:						
- December 31, 2010	2,527	9,961	6,480	3,467	13,141	
- December 31, 2009	6,136	8,893	7,354	3,902	18,232	

28. CURRENCY RISK

The following table summarizes the net foreign currency position of the Bank as of December 31, 2010. The Bank takes on exposure resulting from fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The management establishes limitations on the exposure levels per currencies and aggregately, and monitors such exposure on regular basis.

28. CURRENCY RISK (continued)

In thousands of EUR	RSD	USD	GBP	CHF	Other	Total
Assets in foreign currencies	-	4,482	37	53	14	4,586
Liabilities in foreign currencies	-	4,648	13	50	3	4,714
Net foreign exchange position:						
- December 31, 2010	0	(166)	24	3	11	
- December 31, 2009	-	5	(1)	-	8	
% of first- tier capital:						
- December 31, 2010	0%	(0.71%)	0.10%	0.02%	0.05%	
- December 31, 2009	-	0.02%	0.00%	0.00%	0.03%	
Aggregate open position:						
- December 31, 2010	(127)					
- December 31, 2009	12					
% of first-tier capital:						
- December 31, 2010	(0.54%)					
- December 31, 2009	0.05%					

29. LEGAL PROCEEDINGS

As of December 31, 2010, the Bank is defendant in a certain number of legal proceedings, initiated by retail and corporate clients. The final outcome of the ongoing legal proceedings is uncertain. However, the Bank's management as well as legal consultant does not expect negative outcome of such litigations as well as material affects on financial statements as of December 31, 2010. Total amount of litigations in which the Bank acts as prosecutor as of December 31, 2010 is EUR 996 thousand.

30. EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the annual net gain that is attributable to holders of ordinary shares, divided by the weighted average number of ordinary shares that were outstanding during the period. The Bank is registered as a limited company whose share capital is consisting of 31.305 ordinary shares. Earnings per ordinary share at December 31, 2010 was equal to EUR 0.04 thousand (December 31, 2009: EUR 0.03 thousand).

31. EXCHANGE RATES

The official exchange rates for major currencies used in the translation of balance sheet items denominated in foreign currencies, into euros as at December 31, 2010 and 2009 were as follows:

	December 31, 2010	December 31, 2009
USD	0.7530	0.6974
CHF	0.8016	0.6721
GBP	1.1625	1.1062

FOR INTERNAL USE OF
CENTRAL BANK OF MONTENEGRO

ANALYSIS TO THE FINANCIAL STATEMENTS FOR 2010

Translation of the Analysis to the financial statements for 2010 issued in Montenegrin language

A ANALYSIS TO FINANCIAL STATEMENTS

I INTRODUCTION

Financial Statements of Hipotekarna banka A.D., Podgorica (hereinafter the „Bank"), which were subject of audit have been prepared in accordance with Accounting standards and regulations of Montenegro and regulations of Central Bank of Montenegro governing financial reporting of banks. The prescribed forms of financial statements were submitted in due time to the Central Bank of Montenegro.

II INCOME STATEMENT AND BALANCE SHEET ANALYSIS

Detailed analysis of the balance sheet and income statement is provided within Notes from 4 to 31 to the financial statements.

B REVIEW AND EVALUATION OF QUALITY AND FINANCIAL POSITION OF THE BANK

I QUALITY OF THE BANK'S ASSET

Classification of asset and the corresponding balance sheet items, in terms of determining asset quality, was carried out in accordance with the Decision of the classification of bank assets, provisions and reserves for loan losses issued by the Central Bank of Montenegro („Official Gazette of Montenegro", no. 60/2008 and 41/2009) and the Decision of the Central Bank of Montenegro on temporary measures for managing credit risk in banks ("Official Gazette of Montenegro" no. 64/2009, 87/2009 and 66/2010). On the basis of classification performed and in accordance with internal policies, the Bank has made provisions for potential losses as at December 31, 2010 in amount of EUR 3,637 thousand (December 31, 2009: EUR 2,843 thousand).

Based on audit performed and classification of the selected sample of bank's debtor checked, the auditor, based on relevant Decisions of the Central Bank of Montenegro, has confirmed the classification performed by the Bank.

Classification of the Bank is verified by auditors on a sample covering 69.23 % of the total credit risk exposure at December 31, 2010 (excluding loans granted to retail customers).

Available information on indicators of business of the debtor are taken into account when determining the classification of assets and the required reserves for potential losses of the Bank, as well as the quality of debt service, renewal of loans to the same debtors during the year, the quality of the collection instruments and evidence of credit and interest charges in 2010 and up to day of preparing financial statements for 2010.

Summing up the results of a quality of balance sheet and off-balance sheet assets of the Bank from the point of payment collection and the need to create reserves for the provision of the Bank from potential losses in accordance with the stated approach, the following relations and parameters were provided:

B REVIEW AND EVALUATION OF QUALITY AND FINANCIAL POSITION OF THE BANK (Continued)

I QUALITY OF THE BANK'S ASSET (Continued)

- Risk-weighted balance sheet and off-balance sheet assets of the Bank as of December 31, 2010 and 2009 consists of the following:

	2010			2009		
In thousand of EUR	**Amount**	**In %**	**Formed reserve**	**Amount**	**In %**	**Formed reserve**
Loans	101,009		3,142	76,783		2,085
Less: Loans secured by cash deposit	(5,176)		-	(7,958)		-
	95,833	76.90%	3,142	68,825	73.3	2,085
Accrued interest	950	0.76%	-	470	0.2	6
Other asset items	3,698	2.97%	-	-	9.0	257
Taken over and potential obligations	24,135	19.37%	495	11,802	17.4	495
Total exposure to risk	124,616	100.00%	3,637	81,097	100.0	2,843

- As at December 31, 2010, the structure of the Bank's investments made by risk categories after decreased for cash deposits is as follows:

In thousand of EUR

Category	Loans	Accrued interest	off-balance sheet records	Total	In %
A	40,400	399	14,940	55,739	49.09%
B	42,945	379	7,151	50,475	44.45%
C	6,910	6	10	6,926	6.10%
D	402	-	-	402	0.35%
	90,657	784	22,101	113,542	100.00%

- As at December 31, 2009, the structure of the Bank's investments made by risk categories after decreased for cash deposits is as follows:

In thousand of EUR

Category	Loans	Accrued interest	off-balance sheet records	Total	In %
A	37,746	274	7,034	45,054	56
B	25,645	194	4,619	30,458	38
C	5,219	2	149	5,370	6
D	215	-	-	215	-
	68,825	470	11,802	81,097	100

B REVIEW AND EVALUATION OF QUALITY AND FINANCIAL POSITION OF THE BANK (Continued)

Risk-weighted balance sheet and off-balance sheet assets comprising the total sum of assets classified from the point of collection, as at December 31, 2010, represented 67.64% (December 31, 2009: 60.28% total assets (before impairment for loan loss provisions and impairment losses on other assets).

The loan policy of the Bank is in compliance with the Decision of the Central Bank of Montenegro on minimum standards for the management of loans concentration and doing business with related entities.

II EQUITY AND ADEQUACY OF EQUITY

As of December 31, 2010 and 2009 the share capital of the Bank comprises of 31,305 common shares with nominal value of EUR 511.29.

As of December 31, 2010, retained earnings amount to EUR 1,828 thousand (December 31, 2009: 3,120 thousand).

Pursuant to the Decision on minimum standards for managing credit risk in banks ("Official Gazette of Montenegro" no. 60/2008 and 41/2009), in 2009 the Bank abolished provisions for general credit risks in the amount of EUR 1,849 thousand, formed in previous years, in accordance with than applicable Decision on classification of Bank assets, provisions and reserves for loan losses ("Official Gazette of Montenegro" no. 59/2007)

Bank's own funds as at December 31, 2010 amounted to EUR 20,916 thousand (December 31, 2009: EUR 19,776 thousand).

The core equity of the Bank established in accordance with the Decision on Adequacy of equity of the Bank ("Official Gazette of Montenegro" no. 60/2008, 41/2009) as at December 31, 2009 amounted to EUR 19,776 thousand. The core equity of the Bank as at December 31, 2009 constitutes the essential elements of its own funds: paid share capital at nominal value, collected share premium and the amount of net profit from the current year, less the amount of uncovered loss from previous years and the amount of intangible assets.

As at December 31, 2009, the Bank didn't have additional equity.

Risk-weighted balance sheet and off-balance sheet assets, formed in accordance with the Decision on Adequacy of equity of the Bank at December 31, 2010 amounted to EUR 108,477 thousand (As at December 31, 2009: EUR 70,197 thousand).

In accordance with the Decision on Adequacy of equity of the banks, the Bank is in obligation to maintain a minimal level of solvency ratio of 10%. The solvency ratio of the Bank, as at December 31, 2009 amounted to 15.54% (as at December 31, 2009: 21.58%) and is higher than prescribed minimum.

As at December 31, 2010 no indicator of Bank's doing business did not deviate from prescribed minimum as required by legislation Central bank of Montenegro.

B REVIEW AND EVALUATION OF QUALITY AND FINANCIAL POSITION OF THE BANK (Continued)

III LIQUIDITY OF THE BANK

Liquidity risk management is defined by the Procedure for managing liquidity risk which defines that the responsibilities in managing the Bank's liquidity bear the following authorities of the Bank:

- Management of the Bank
- Asset and liability Committee (ALCO)
- Payments and funds management department, other Bank's departments and services

The Bank maintains its liquidity by constantly monitoring the alignment of resources and placements in order to be able to all its and commitments of their depositors, settles when mature, while at the same time trying to meet the needs of the founder and business customers in approving the loans, i.e. to adjust maturities of loans with borrower's needs.

Liquidity of the Bank as at December 31, 2010 and 2009 can be closely looked from the following indicators:

				2010.	2009.
Loans ---------------------- Deposits	=	101,009 ---------------------- 85,133	x 100 =	118.65%	110.11%
Liquid assets ---------------------- Deposits	=	24,247 ---------------------- 85,133	x 100 =	28.48%	28.56%
Liquid assets ---------------------- Total assets	=	24,247 ---------------------- 128,788	x 100 =	18.83%	20.00%
Liquid assets ---------------------- Short-term liabilities	=	24,247 ---------------------- 83,889	x 100 =	28.90%	29.07%

Maturity alignment of financial assets and Bank's liabilities as at December 31, 2010 has been shown in note 26 to the financial statements.

IV INTEREST RATE RISK

Existing interest rates are determined by a Decision on the interest rate. This decision defines the basic goals and guidelines for interest rate policy, principles and methods of determining the interest rates, by which the Bank arranges agreements, calculate and charge interest on loans and other receivables, i.e. pays on deposits and other funds received.

The Bank is exposed to various risks associated with the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. As a result of such changes, an interest margin of the Bank could be increased, but also decrease and loss in a case of unexpected interest rate fluctuation can occur.

Interest rate risk as at December 31, 2010 is shown in note 27 to the financial statements.

B REVIEW AND EVALUATION OF QUALITY AND FINANCIAL POSITION OF THE BANK (Continued)

IV INTEREST RATE RISK (Continued)

In accordance with the policy for managing market risks, the Bank controls the risk of interest rate fluctuations by establishing internal limitations for the ratio of total bank exposure to interest rate changes.

Defining the limits established boundaries for the level of exposure to interest rate risk in the following manner, and in accordance with the Policy of managing market risks in Hipotekarna Banka A.D., Podgorica:

- The average interest margin must not fall below 40% of the average lending interest rates.
- The Bank follows and establishes the average lending and deposit interest rates, by putting the ratio of earned interest income for the reference period with an average interest bearing assets for the reference period to determine the average lending interest rates, as well as by putting in relation actual interest expense for the observed period with an average interest bearing liabilities for the reference period in order to establish the average deposit interest rate. The difference got by subtracting the average deposit interest rate from the average lending interest rate, represents the interest margin, which must not fall below 40% of the average lending interest rate, calculated in the manner aforecited.
- The above calculation is done for a particular month, as well as cumulatively for the period from the beginning of the year until the reference period, according to provided data, movement of average lending and deposit interest rates and movement of the interest margin for the reference month and period can be followed.

In a case that an average interest margins fall under 40% of the average lending interest rates, Risk management department, i.e. Risk monitoring and reporting department will inform the ALCO Committee, which is obliged to recommend measures for maintaining operations within the defined limits:

- The total annual cumulative difference for the position in EUR must not exceed 45% of total assets, i.e. 45% of total liabilities,
- The total semi-annual cumulative difference for the position in EUR must not exceed 36% of total assets, i.e. 36% of total liabilities,
- The total annual and semi-annual cumulative difference for the position for particular currencies must not exceed 9% of total assets, i.e. 9% of total liabilities,
- Observed aggregation for the position in all currencies, the total annual cumulative difference must not exceed 54% of total assets, i.e. 54% of total liabilities,
- Observed aggregation for the position in all currencies, the total semi-annual cumulative difference must not exceed 45% of total assets, i.e. 45% of total liabilities.

B REVIEW AND EVALUATION OF QUALITY AND FINANCIAL POSITION OF THE BANK (Continued)

IV INTEREST RATE RISK (Continued)

Lending interest rates applied to loans granted to corporate entities during 2010 are as follows:

Type of a loan	Interest rate per a year
Overdraft	13.0 - 16.5
Cash loans	11.0 - 14.5
Revolving loans	11.5 - 15.0
Loans for payment obligations to the suppliers	10.5 - 14.0
Factoring loans	11.5 - 15.0
Car loans	11.0 - 14.5
Refinancing loans to other bank liabilities	10.5 - 14.0
Loans based on 100% time deposit	deposit interest rate + 2.0 - 4.0
Loans for financing export receivables	10.0 - 13.5
Loans to financing the purchase of equipment	10.0 - 13.5
Loans to financing and adoption of business premises	10.0 - 13.5
Loans to financing the purchase of fixed assets	10.0 - 13.5
Loans for the preparation of tourist season	13.0
Mortgage loans	12.5 - 15.0

Lending interest rates applied to loans granted to retail customers during 2010 are as follows:

Type of a loan	Interest rate
Cash loans	1.2 – 1.5 p.m.
Mortgage loans	1.2 p.m.
Loans for renovation and construction	1.0 p.m.
Car loans with the deposit of 20%	1.1 – 1.4 p.m.
Loans for tourism development	1.2 p.m.
Loans for marines	1.0 – 1.2 p.m.
Loans for students	1.2 p.m.
Loans for retired	1.2 p.m.
Customer loans	1.1 – 1.4 p.m.
Overdraft	14.6 p.a.
Sprint loans	1.2 – 1.5 p.m.
Agricultural loans	1.1 p.m.
Loans for the purchase of goods	1.2 p.m.
Lombard loans on collateral securities	1.0 – 1.2 p.m.
Lombard loans based on collateral of term deposits of 100%	+2.5 p.m. to deposit interest rate

B REVIEW AND EVALUATION OF QUALITY AND FINANCIAL POSITION OF THE BANK (Continued)

IV INTEREST RATE RISK (Continued)

Deposit interest rates which were applicable on corporate entities during 2010 are as follows:

Deposit type	Interest rate per a year
Demand deposits to corporate entities	0.2 – 0.5
Time deposits in dollars - USD	1.2 – 3.5
Time deposits in euros - €	1.2 – 6.0
Time deposits in foreign currencies (AUD,CAD,CHF,GBP)	1.0 – 3.1

Deposit interest rates which were applicable on retail customers during 2010 are as follows:

Deposit type	Interest rate per a year
Children's savings Mravac - time cumulative savings	3.0 – 6.2
Time cumulative savings	3.0 – 6.2
Time savings in $, Time cumulative savings in $, Children's savings Mravac - time cumulative savings in $, Rent savings in $	1.2 – 2.0
Time savings in €	3.0 – 6.2
Time savings, Time cumulative savings, Children's savings Mravac - time cumulative savings, Rent savings – in foreign currencies (AUD, CAD, CHF, GBP)	1.2 – 2.0
Rent savings	3.0 – 6.2
Demand deposits	0.2 – 0.4

V CURRENCY RISK

The Decision issued by the Central Bank of Montenegro regarding minimal standards for management of credit risks in banks establishes the following limits regarding the open foreign currency position:

- Individual open position at the end of the day for the currencies of daily exchange rate on the reference list of the European Central Bank - max 15% of the core capital.
- The aggregate open position at the end of the day for the currencies of daily exchange rate on the reference list of the European Central Bank - max 20% of the core capital
- The net open positions at the end of the day for other currencies, may amount to no more than 5% of the core capital on an individual basis (currencies which are not at the reference exchange rate list of the European Central Bank)
- The net open positions at the end of the day for other currencies, may amount to no more than 10% of the core capital on an aggregate basis.

B REVIEW AND EVALUATION OF QUALITY AND FINANCIAL POSITION OF THE BANK (Continued)

V CURRENCY RISK (Continued)

As at December 31, 2010, foreign currency exposure of the Bank was as follows:

In thousands of EUR	RSD	USD	GBP	CHF	Other	Total
Assets in foreign currencies	-	4,482	37	53	14	4,586
Liabilities in foreign currencies	-	4,648	13	50	3	4,714
Net foreign exchange exposure:						
- December 31, 2010	-	(166)	24	3	11	
- December 31, 2009.	-	5	(1)	-	8	
% of first-tier capital:						
- December 31, 2010	0%	(0.71%)	0.10%	0.02%	0.05%	
- December 31, 2009.	-	0.02%	0.00%	0.00%	0.03%	
Aggregate open position:						
- December 31, 2010	(127)					
- December 31, 2009.	12					
% of first-tier capital:						
- December 31, 2010	(0.54%)					
- December 31, 2009.	0.05%					

VI COUNTRY RISK

In accordance with the Decision of the Central Bank of Montenegro on methodology for measuring country risk in the banks ("Official Gazette of Montenegro" no. 60/2008), the Bank has adopted a Policy and Procedures of country risk management. Country risk presents a probability of incurring losses to the Bank, due to the inability to collect receivables from entities outside Montenegro because of political, social and economic reasons of the country where the seat of the debtor is.

Country risk as at December 31, 2010 was calculated using the current methodology Rating of debtor countries. Country risk management policy defines the following percentages of reserves in line with the "rating" of land the bank has exposure to (Standard & Poors):

Risk categories	Risk weight
Non-risk countries	0%
Low-risk countries	50-100%
Medium-risk countries	150-250%
High-risk countries	minimum 300%

As at December 31, 2010, the Bank has presented income from cancellation of reserves from the Bank's exposure to country risk in the amount of EUR 54 thousand (December 31, 2009: EUR 9 thousand).

B REVIEW AND EVALUATION OF QUALITY AND FINANCIAL POSITION OF THE BANK (Continued)

VII OPERATIONAL RISK

In accordance with the Decision of the Central Bank of Montenegro on minimum standards for operational risk management in banks ("Official Gazette of Montenegro" no. 24/2009), which was adopted at the Council meeting of the Central Bank of Montenegro, held on February 23 and 24, 2009 the Bank has adopted a Policy for managing operational risk.

Operational risk is defined as the risk of loss due to improper or inappropriate conduct and actions of employees, inadequate and / or errors in processes and organization, inadequate and / or errors in systems and infrastructure or due to external factors and influences.

In accordance with the Decision of the Central Bank of Montenegro, the Bank is obliged to inform the Central Bank of losses arising from operational risk exceeding 1% of venture capital, at the latest within eight working days from the date of loss.

As at December 31, 2010, the provisions for operational risk amount to EUR 279 thousand (December 31, 2009: EUR 300 thousand).

VIII INTERNAL CONTROL AND INTENAL AUDIT SYSTEM

Organizational structure of the Bank establishes levels and lines of authority and responsibility with a clear delimitation between the function of management and leadership function. The management bodies are: the Assembly of the Bank and the Board of Directors of the Bank.

Bank is managed by the General Executive Director of the Bank.

The Bank, as a separate organizational unit, organized Internal Audit department. Internal audit department performs its activities in accordance with the internal audit procedures and annual plan of activities.

In accordance with these internal procedures the internal audit activities include but are not limited to:

- Compliance with relevant rules, guidelines, instructions and standards;
- Evaluation of the reliability of rules and division of duties within the banking operations;
- Review and estimation of effectiveness and benefits of financial and administrative controls;
- Monitoring the adequacy, reliability, safety integrity of accounting and other management information systems;
- Review of effectiveness and efficiency of banking operations;
- Testing the validity of measures used to achieve banking operations;
- Test and evaluation of the adequacy and effectiveness of internal control system;
- Review of application and effectiveness of risk management procedures and assessment of the methodology of risk assessment;
- Assessment of information systems, with special emphasis on electronic information systems and banking application;

B REVIEW AND EVALUATION OF QUALITY AND FINANCIAL POSITION OF THE BANK (Continued)

VIII INTERNAL CONTROL AND INTENAL AUDIT SYSTEM (Continued)

- Assessment of the accuracy and reliability of accounting financial statements;
- Assessment of the banking system in the determination of capital in relation to the estimated risk;
- Testing of transactions and functioning of specific internal control procedures;
- Adherence to legal and statutory regulations, code of ethics, implementation of policies and procedures;
- Conducting special investigations.

When reporting to the Bank's management, internal audit operates independently in order to establish and report on the adequacy, reliability and effectiveness of controls used by the Bank's risk management, which has a preventive effect on achievement of the objectives of banking, and reporting whether the banking resources are used efficiently and effectively in achieving the objectives of banking.

C REVIEW OF BANK'S ORGANIZATIONAL STRUCTURE

The Bank performs its activity in central office in Podgorica and branch offices in Podgorica, Bijelo Polje, Budva, Nikšić, Bar, Herceg Novi, Berane and Kotor, as well as in branches in Podgorica, Tivat, Tuzi and Cetinje.

The Bank carries on business activities through the following bodies and organizational components:

1. Assembly of Shareholders

2. The Board of Directors
2.1 The Audit Committee
2.2 Credit Risk Management Committee
2.3 Internal Audit Department
2.4 Department for monitoring compliance with regulations
2.5 The authorized person for the prevention of money laundering and terrorist financing.
2.6 Head of Information Systems Security

3. Chief Executive Officer
3.1 Administrative and HR Service
3.2 Payments and fund management
3.3 Domestic payments
3.4 International Payments
3.5 Fund management service
3.6 Custody service
3.7 Brokerage service sector

4. Executive Director of Commercial Affairs
4.1 Commercial Sector
4.2 New products development Service and Marketing
4.3 Business Network

5. Risk Management Executive Director
5.1. Risk Management Sector
5.2. Loan Analysis Sector
5.3. Sector for managing risk assets
5.4. Risk monitoring and reporting sector

C REVIEW OF BANK'S ORGANIZATIONAL STRUCTURE (Continued)

6. Executive Director of Finance and Informatics
6.1. Division of Finance and Informatics
6.2. Accounting and Reporting
6.3. Department of General Affairs
6.4. Service Billing
6.5. IT Department

As of December 31, 2010, the Bank had 155 employees (December 31, 2009: 139 employees).

Qualification structure of the Bank, as at December 31, 2010 and 2009 were as follows:

	No. of employees	In %	No. of employees	In %
Masters	4	3	2	2
University degree (four years)	75	48	66	47
College degree (two years)	15	10	17	12
Bachelor	9	6	8	6
High school degree	52	33	45	32
Qualified			1	1
	155	100	139	100

The members of Board of Directors as at December 31, 2010 were:

Name	Function
Sigilfredo Montinari	President
Božana Kovačević	Vice president
Snježana Pobi	Member
Renata Vinković	Member
Esad Zaimović	Member

The members of Credit Risk Management Committee, as at December 31, 2010 were:

Name	Function
Renata Vinković	President
Esad Zaimović	Member
Snježana Pobi	Member

The members of the Audit Board, as at December 2010, were:

Name	Function
Marko Žigmund	President
Božana Kovačević	Member
Jovan Papić	Member

As at December 31, 2010 the Chief Executive Officer was Mr. Esad Zaimović.

As at December 31, 2010 Chief Internal Auditor was Mr. Veselin Ivanović.

D REPORT IN SHORT FORM

In accordance with the Decision on Reports which banks submit to the Central Bank of Montenegro, the report in a short form consists of Auditor's opinion on financial statements of the bank, Income Statement and Balance Sheet, data on the composition of the Board of Directors, the Committee on Credit Risk Management and Supervisory Committee, information about the Chief Executive Officer, Chief Internal Auditor of the Bank and data on performance indicators.

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This is an English translation of the Report originally issued in Montenegrin language (For management purposes only)

INDEPENDENT AUDITORS' REPORT TO THE OWNERS OF HIPOTEKARNA BANKA A.D., PODGORICA

Report on Financial Statements

We have audited the accompanying financial statements of Hipotekarna banka A.D., Podgorica (hereinafter: the Bank), which comprise the balance sheet as at December 31, 2010, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the Law on Accounting and Auditing and regulations of the Central Bank of Montenegro governing the financial reporting of banks, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' 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 about whether the financial statements are free from material misstatement.

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

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

ERNST & YOUNG

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Bank as at 31 December 2010, and of its financial performance and its cash flows for the year then ended in accordance with the Law on Accounting and Auditing and regulations of the Central Bank of Montenegro governing financial reporting of banks.

Other matter

The financial statements of the Bank for the year ended 31 December 2009 were audited by another auditor who expressed an unmodified opinion on those statements on April 26, 2010.

Podgorica, April 12, 2011

Ernst & Young Montenegro d.o.o.
Podgorica, Crna Gora

Stephen Fish
Partner

Danijela Dimovski
Authorized auditor

ERNST & YOUNG MONTENEGRO DOO PODGORICA

INCOME STATEMENT FOR THE YEAR ENDED DECEMBER 31, 2010

In thousands of EUR	Notes	2010.	2009.
Interest income	3.1, 4a	9,634	6,827
Interest expense	3.1, 4b	(3,433)	(2,523)
Net interest income		6,201	4,304
Provisions for losses	3.6, 5	(1,334)	(404)
Net income		4,867	3,900
Fee and commission income	3.1, 6a	3,105	2,087
Fee and commission expense	3.1, 6b	(465)	(346)
Net fee and commission income		2,640	1,741
NET INTEREST, FEE AND COMMISSION INCOME		7,507	5,641
Other income, net	7	399	987
General expenses	8	(6,827)	(5,591)
NET INCOME BEFORE EXTRAORDINARY ITEMS		1,079	1,037
Extraordinary income		263	37
Extraordinary expenses		(35)	(19)
		228	18
PROFIT BEFORE TAXATION	9	1,307	1,055
Income taxes	3.3, 9	(15)	-
NET PROFIT FOR THE YEAR		1,292	1,055

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

These financial statements are approved by management of Hipotekarna banka A.D., Podgorica, on January 17, 2011 in Podgorica.

Signed on behalf of Hipotekarna banka A.D., Podgorica:

Esad Zaimović
Chief Executive Officer

Aleksandar Mitrović
Executive Director of Finance and Informatics

BILANCE SHEET AS AT DECEMBER 31, 2010

In thousands of EUR	Notes	2010.	2009.
ASSETS			
Cash and deposit accounts held with depository Institutions	10	24,247	19,917
Securities available for sale, other than shares		42	292
Loans and leases	11	98,352	74,698
Securities held to maturity	12	1,093	1,086
Receivables in respect of custody operations		23	19
Business premises and other fixed assets	13	1,742	1,473
Acquired assets	14	485	11
Equity investments in other legal entities	15	99	7
Other assets	16	3,190	2,347
Less: Provision for potential losses on other assets	16	(485)	(263)
Total assets		128,788	99,587
LIABILITIES			
Deposits	17	85,133	69,735
Liabilities in respect of custody operations		49	387
Obligations based on loans and borrowings	18	15,000	4,000
Obligations to the Government of Montenegro	19	2,716	2,248
Other liabilities	20	3,773	2,392
Provisions for potential losses on off-balance sheet credit exposures	21	494	495
Total liabilities		107,165	79,257
EQUITY			
Share capital	22	16,006	16,006
Share premium		7,444	7,444
Revaluation reserve		1	-
Uncovered loss		(1,828)	(3,120)
Total equity		21,623	20,330
Total liabilities		128,788	99,587
OFF-BALANCE-SHEET ITEMS	24	289,488	198,891

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

These financial statements are approved by management of Hipotekarna banka A.D., Podgorica, on January 17, 2011 in Podgorica.

Signed on behalf of Hipotekarna banka A.D., Podgorica:

HIPOTEKARNA BANKA A.D. PODGORICA

Esad Zaimović
Chief Executive Officer

Aleksandar Mitrović
Executive Director of Finance and Informatics

Translation of the financial statements issued in Montenegrin language

DATA ON BOARD OF DIRECTORS COMPOSITION, CREDIT RISK MANAGEMENT COMMITTEE, SUPERVISORY COMMITTEE, CHIEF EXECUTIVE OFFICER AND CHIEF INTERNAL AUDITOR OF THE BANK

As at December 31, 2010 the members of Bank's Board directors were:

Name	Function
Sigilfredo Montinari	President
Božana Kovačević	Vice President
Snježana Pobi	Member
Renata Vinković	Member
Esad Zaimović	Member

As at December 31, 2010 the members of Bank's Board directors were:

Name	Function
Renata Vinković	President
Esad Zaimović	Member
Snježana Pobi	Member

The members of the Audit Board, as at December 31, 2010 were:

Name	Function
Marko Žigmund	President
Božana Kovačević	Member
Jovan Papić	Member

As at December 31, 2010 the Chief Executive Officer was Mr. Esad Zaimović.

As at December 31, 2010 the Chief Internal auditor was Mr. Veselin Ivanović.

BANK'S PERFORMANCE INDICATORS AS AT DECEMBER 31, 2010

Bank's performance indicators as at December 31, 2010 and 2009 were as follows:

Indicators	2010	2009
Core equity	EUR 20,916 thousand	EUR 19,776 thousand
Additional equity	-	-
Bank's funds	EUR 20,916 thousand	EUR 19,776 thousand
Weighted balance sheet assets	EUR 108,477 thousand	EUR 70,197 thousand
Solvency ratio	15.54%	21.58%
Return on average assets	1.13%	1.21%
Return on average equity	6.16%	5.33%