ANNUAL REPORT 2010

Report of the Chairman of the Board of Directors
and Chief Executive Officer Report

Report of the Chairman of the Board of Directors

Dear clients, partners and shareholders,

On behalf of the Board of Directors, I have the honour to present the Annual Report of Hipotekarna banka AD Podgorica for the year 2010.

After a period of extreme international financial instability and global economic weakness, conditions improved materially in 2010. The international financial system stabilized and began the journey back to health. The global economy stopped contracting and began to grow, at a pace that surprised many observers. In the euro zone, fiscal tightening and economic rebalancing dampened growth in some countries. New regulatory requirements have become more concrete in the wake of the crisis. The "Basel III" rules, recently approved by the G20, are just the beginning.

The Board of Directors worked closely with the management team on a range of issues. The successful execution of our strategy requires us to focus on core market segments, customer engagement, cost leadership, capital efficiency and a prudent risk and funding profile. Carried out well, these attributes should enable the Bank to deliver earnings growth and shareholder value while achieving the aim of becoming recognized as one of the best financial services company in the country. We have a great platform for the future and have established a strong financial and operational trajectory and we are confident that we will be able to grow the business further over the coming years.

This report comes to you at the end of another successful year. A year in which we increased profitability. Again, we successfully managed to grow faster than the local market. The Bank increased its market share and all relevant parameters at the same time when we booked the profit growth of 22.46%. At the end of year 2010, the solvency ratio stood at 15.54%, along with the return on equity ratio of 5.97%.

As an organization, we made considerable progress in 2010, delivering good growth in our core business, returning to profitability and reducing the risk of the business. The Bank also strengthened its equity capital base. Thanks to the well-chosen operational models, the capital increase was carried out due to the increase in profitability in almost every aspect of business.

The Bank's capital strength will continue to be a top priority for the Board in the future. In doing so, we made substantial progress towards creating a strong and stable bank, one better able to serve our customers. Only by focusing on their needs and offering them products and services that address those needs, we can expect to remain successful in the future and deliver benefit to our shareholders and to our stakeholders at large.

I want to thank our employees for their dedication and effort over the past year, our customers and clients for giving us the opportunity to serve their needs, and our shareholders for their continued faith in the bright future of Hipotekarna banka.

Sigilfredo Montinari
Chairman of the Board of Directors

Report of Chief Executive Officer

Dear clients, partners and shareholders,

It is my great honour to present the Annual Report on operations of Hipotekarna banka AD Podgorica for the year 2010.

During the last year, global economy showed signs of recovery, a signal that the worst is already behind us, though leaving the consequences which must be dealt with successfully. Seeing the first signs of lessening of the economic crisis at a global scale and an adequate, long-term policy and strategy, with a high level of professionalism at work, the Bank managed to end the year 2010 with a growth in profits, even though it was a year of great challenges for a whole banking system in the country.

In 2010 a stabilization of the banking sector occurred in Montenegro. The initiatives were launched for the resolution of important issues that burden the banking sector. Results achieved so far are a promising step forward, primarily in the change of regulations, which required improvement and a gradual adaptation to international accounting standards. A significant effect in fighting unrealistically high interest rates on savings was also achieved, which led to increased interest rates for citizens and industry. The outflow of deposits from previous years as well as the loss in confidence in the banking sector also influenced the rise in interest rates. During 2010, this issue was mostly resolved, the downward trend in interest on savings is evident and is happening in all banks, and it indicates the period of cheap bank resources and better pay-off terms .

2010 was very successful for us. We achieved growth in each activity, and improvements of all the relevant success indicators in all areas of operating transactions. The increase in assets compared to last year was 29.32%, deposits increased by 22.08%, an increase of 31.67% of lending was achieved, and in the capital market last year's status was promoted by opening a new organizational unit with new services.

Throughout the year, the Bank maintained the required level of liquidity, maturity adjustment of financial assets and financial liabilities, foreign exchange compliance, and high levels of capital adequacy. Investing funds in financial instruments held for sale, created a portfolio of securities, which also serves as a secondary source of liquidity and as a source of additional profitability.

This year as well, we expect to continue using more favourable sources of finance. It is primarily related to funding from the European Investment Bank and other funds providing lines of credit to small and medium enterprises. Funds provided in this way are much cheaper than other sources, which are normally used, and Hipotekarna banka has shown with its results that it has risen to the challenge of becoming a healthy and economically viable for small and medium enterprises.

Hipotekarna banka will continue to encourage lending in all segments, with a reduction in interest rates and an adequate risk assessment. Special attention directed towards the process of change and innovation to improve efficiency and the quality of operations, enabling us to quickly and easily meet the needs of our clients. The highest standard of quality service, the ability to anticipate the needs of our customers and create a long-term sustainable business model, continue to be our orientation for the future.

Finally, on the behalf of the management of Hipotekarna banka, and on my own behalf, I wish to express my gratitude to our valued customers for their trust, respected owners for the expressed support, and all our associates and employees on their professionalism and cooperation.

Esad Žaimović
Chief Executive Officer

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1. Summary of the Montenegrin economy in 2010

Macroeconomy

Macroeconomic development in 2010 was characterized by low inflation, growth in industrial and forestry production, the growth in tourism services, trade, and some traffic segments over the previous year. Deposits and bank capital are increasing, while loans decreased. Net inflow of foreign direct investment for the eleven months of 2010 remains high, although lower than the same period last year, due to the absence of large privatization.

GDP

The economic activity stabilized in the first half of 2010, whereas it recorded growth during the last two quarters.

The physical industrial production volume, after some difficulties in the first half of the previous year, in eleven months reached the level which is 14.7% above the same period in 2009. The growth in production of the Aluminium plant and restored production growth trend in the steel mills is particularly important. The tourist turnover indicators, despite the impact of the crisis, indicate an improvement in the tourism offer and organization.

The number of overnights stays in the first ten months of 2010, increased by 5.5% which is by 5.2% higher than the same period in 2009.

Construction activity, being extremely affected by the illiquidity problem, is showing signs of recovery. It is still below the level generated in 2009 but the growth in the value of new construction contracts, in the third quarter against the previous quarter of last year, is encouraging. Significant growth in primary agricultural and forestry production is being recorded.

All of the above indicates the Montenegrin economy, after the real GDP decline in 2009 of 5.7%, in 2010 was recovering and strengthening the economic activity. In the third quarter, the leading indicators showed the real growth trend in the area. Current expectations are that the projected GDP growth of 0.5% achieved by the end of 2010 will be approximately 3,025 million EUR.

Economic Indicators Outlook

List of indicators	Trend 2010	Index 2010/2009		Commentary Total indicator
A. DEMAND AND TRADE				
1. Monthly payment operations (trend)	Slight decline	Down 5.9% (12 months)	▼	Steady decline from early 2008 with the slight recovery in the last quarter of 2010
2. Monthly retail trade (trend)	Slight increase in trend	Up 2.47 % (11 months)	▲	Steady slight increase from the beginning of the year.
3. Monthly imports	Stabilized in this year	Up 0.57 % (11 months)	=	Stable trend after a sharp tuning in 2009.
4. Consumer Price Index (CPI)	Increase in prices in last 3 months	Up 0.8 % (11 months)	=	Prices are stable with the slight increase in last quarter.
B. FISCAL REVENUES				
5. Monthly taxes on wages (trend)	Slight trend increase	Up 12.28 % (12 months)	▲	Increase in taxes on wages due to: introduction of taxation on other personal income, collection of outstanding liabilities.
6. Monthly indirect taxes (trend)	Slight trend decline	Up 0.72 % (12 months)	=	Slight trend decline due to slight declined in VAT collection in the last quarter.
C. PRODUCTION AND SUPPLY				
7. Manufacturing production	Trend increase	Up 11.4 % (11 months)	▲	Slight increase due to growth in mining production and electricity generation
8. Tourism nights (trend)	Trend stabilization	Up 5,4 % (11 months)	▲	Slight increase due to better summer tourist season.
9. Agriculture and fishery sales	Sharp trend decline	Down 14.9% (11 months)	▼	Sharp decline due to unfavorable climate conditions.
10. Road transportation	Slight trend decline	Down 1.8 % (11 months)	▼	Decline in transportation of goods level. *
11. Construction value	Slight decline	Down 4.5 % (9 months)	▼	Slight decline after sharp tuning in 2009.
12. Monthly exports (trend)	Sharp trend increase	Up 18,8 % (11 months)	▲	Sharp imports recovery in 2010 due to the increase in aluminum prices.
D. MONETARY DATA				
13. Private credits	Approved credits decline	Down 12,44 % (10 months)	▼	Lower level of approved credits.
14. Private deposits	Slight increase	Up 6.79 % (10 months)	▲	Deposits recovery due to significant increase in household deposits.
15. Commercial bank net assets	Decline	Down 38.6 % (10 months)	▼	Decline caused by credits transferred to external mother banks.
16. Accounts blocked - percentage	Further increase	Up 2,1 % (Oct./Oct.)	▲	Further accounts blocked increase in value and percentage.
E. LABOUR MARKET				
17. Employment **	Slight decline	Slight decline	▼	Employment decline after a temporary seasonal increase.
18. Unemployment	Slight increase	12.29% at the end of 2010.	=	Increase in the number of unemployed persons, stabilizing in the last month.
19. Average monthly gross wage	Slight increase	Up 3 % (11 months)	=	Increased caused by the changes to the tax regime.

** decline in the sector of transportation of goods is higher than data indication, due to temporary increase in transportation volume in November 2010 - ore transportation.*

*** ** due to changed data source, data obtained prior to April 2010 are not comparable with the later ones.*

Foreign direct investment

The net FDI inflow for the nine months of 2010, is at EUR 397.9 million, representing the indicator of a continuous investors interest in this area (projected inflow was EUR 400 million in 2010). It is evident that the structure of FDI inflow is subject to a positive change, with the strengthening of the share of investments in companies and banks, along with the reduction in, until recently, the dominant share of investment in real estate.

Inflation

Inflation, measured by CPI in November 2010, compared to December 2009, indicates growth of only 0.6%. CPI increased by 0.8% annually, while the average price growth rate in the period January - October 2010, compared to the same period in 2009, amounted to 0.5%, which under the conditions of relatively low aggregate demand and consumption level, represented a factor of macroeconomic stability. Prices in the last quarter recorded a slight growth, after stagnating for much of the year, and for the first time deflating in August. On an annual basis, the increase in the CPI will be below 1%.

Foreign exchange

Positive changes are occurring in foreign trade. The volume of foreign trade in January - October 2010, amounted to EUR 1,619.4 million, which is 2.1% above than the same period in 2009. The value of exported goods is higher by 14.1%, and the level of imported goods is higher by 0.2%. The trade deficit was EUR 1,104.0 million, being 2.6% lower compared to the deficit in 2009.

Unemployment

After the unemployment decline from the first quarter of 2010, as of August the unemployment rate steadily rose, stabilizing at the end of the year at 12.13 % or around 32,000 unemployed persons. The number of employees in the first nine months of this year lower by 3.7% over the same period last year on average, while the number employed in September compared to the previous year was higher by 2.7%. By sector, the highest growth was recorded in the real estate and leasing business 43%, other community, social and personal services 20%, financial mediation 8.7%, wholesale and retail trade, repair 7.8% and state administration and social security 0.7%. All other sectors recorded a fall in employment over the same period last year.

Eurobonds

For the first time, Montenegro issued Eurobonds, whereby investors showed trust in the Montenegrin financial system. It happened in a year of great instability for the European financial markets, and the crises in certain countries of the Euro zone, which make these results a success.

Montenegro debuted on the world's capital markets by issuing the Eurobonds worth EUR 200 million, on 7th September 2010. The entry into the Eurobonds market represents a very significant step in improving the status of the country as a competitive market player in the global economic scene.

The total demand for Montenegrin securities was around EUR 600 million. This is a unique case for a country which for the first time entering the bonds market, succeeded in achieving demand three times greater than supply. More than 140 investors from 25 countries in Europe, Asia and the United States were in the market for our securities. Bonds issued with maturity date of five years, and an interest rate fixed at 7.875%, were purchased by 125 investors. The security was traded on the secondary market the same day.

(Source: Monstat, The Central Bank of Montenegro, The Ministry of Finance)

2. Overview of the Bank's operations

Organization and staff

At 31.12.2010, the Bank had 155 employees who have the necessary skills and information-technological base to perform banking operations. Working with customers ("front office"), engages 56% of total employees. The number of employees increased by 16 (sixteen), compared to 31.12.2009. The average age of employees in the Bank is 35.3 and the average working experience of employees is 10.8 years.

An appropriate organizational structure had to be adapted to business development, therefore the Bank has introduced some organizational changes in order to achieve greater efficiency and optimum utilization of technical and human resources. During 2010, the Bank opened a branch in Podgorica, Djoka Miraševića M3, which employs 3 (three) employees. Also, the Board of Directors at its session held in December, passed the Decision on establishing a branch in Ulcinj which is expected to commence operations by the end of first quarter 2011, and should employ 4 (four) new employees.

Educational structure of employees: 4 (four) employees are Masters of Science (MSc), 75 (seventy five) employees with high education (university degree), 9 (nine) employees have a bachelor degree, 15 (fifteen) with a college diploma and 52 (fifty two) with secondary education.

Governing bodies

Governing bodies of the Bank: Assembly of Shareholders and the Board of Directors. General Assembly consists of all shareholders. Members of the Board of Directors, the Bank's management authorities, are elected and appointed by the Assembly of Shareholders. The Board of Directors of the Bank has 5 (five) members and the majority is not employed in the Bank. Standing Bodies of the Board of Directors of the Bank are the Audit Committee and the Credit Risk Management Committee. List of the Boards, its members and executive directors of the Bank

1. **The Board of Directors of Hipotekarna Bank AD:**
   - Sigilfredo Montinari, Chairman
   - Božana Kovačević, Deputy Chairman
   - Snježana Pobi, Member
   - Renata Vinković, Member
   - Esad Zaimović, Member

2. **Audit Committee of Hipotekarna Bank AD:**
   - Marko Žigmund, Chairman
   - Božana Kovačević, Member
   - Jovan Papić, Member

3. **Credit Risk Management Committee of Hipotekarna Bank AD:**
   - Renata Vinković, Chairman
   - Esad Zaimović, Member
   - Snježana Pobi, Member

4. **Executive Directors of Hipotekarna Bank AD:**
   - Esad Zaimović, Chief Executive Officer
   - Jelena Vuletić, Risk Management Executive Director
   - Ana Golubović, Executive Director of Commercial Affairs
   - Aleksandar Mitrović, Executive Director of Finance and Informatics

Shareholders Assembly

The Assembly of Shareholders held two sessions in 2010 which, considering materials that were subject to assessments and decisions had the character of regular (annual) meetings and extraordinary sessions.

At the 12 regular meetings (held on 23.06.2010) the Shareholders' Assembly reviewed the annual report of Hipotekarna Bank AD Podgorica for 2009 with the report of external auditors and adopted the Decision on profit distribution for 2009 which is used to cover losses from previous accounting periods.

At the extraordinary meeting of Shareholders (held on 20.12.2010), amendments to the Statute of the Hipotekarna Bank AD Podgorica had been voted on and the Bank acted in accordance with Art. 40. of Law on Amendments to the Banking Act and Statute of the Bank complied with the Act.

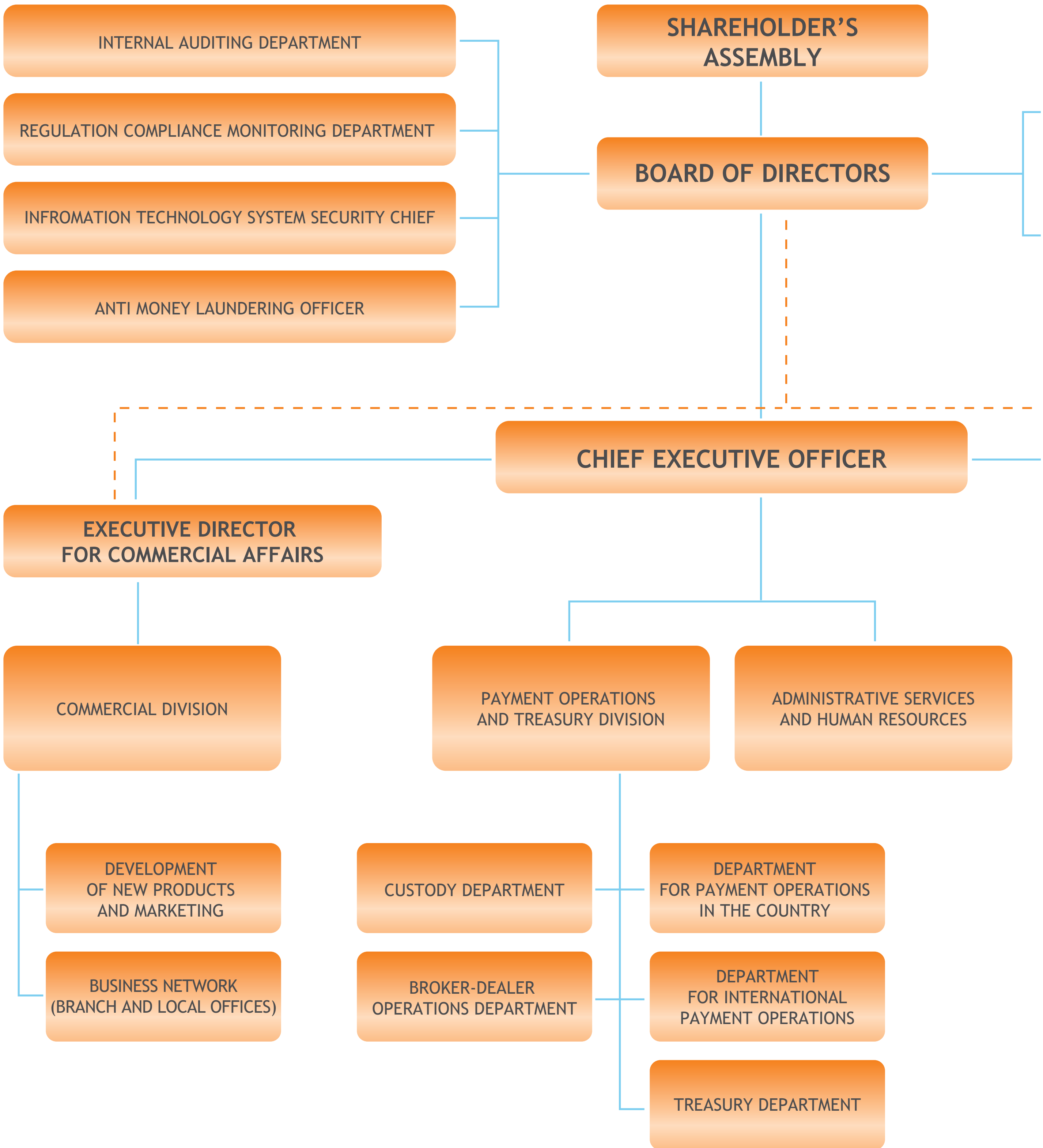
Board of Directors and Governing bodies

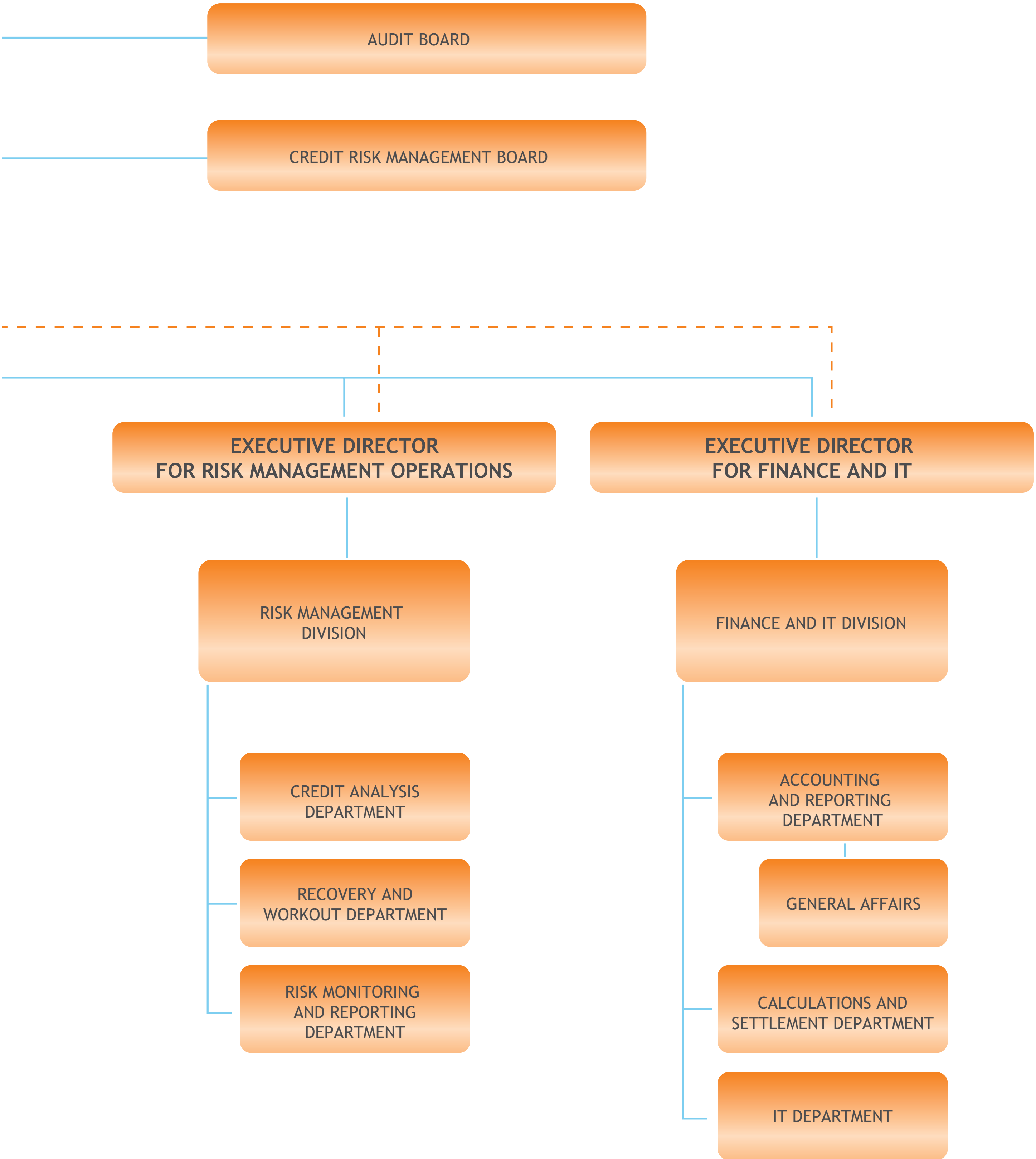
The Board of Directors of the Bank, in accordance with the Law on Banks ("Official Gazette of Montenegro no. 17/08, 44/10), held in 2010 a total of 13 sessions, of which 12 regular sessions (legal obligation is to maintain the session at least once a month) and one correspondent session.

As a permanent body of the Board of Directors, the Audit Committee and the Committee on risk management have regularly reported to the Board of Directors within its jurisdiction.

In addition to the permanent body, the Committee on Asset and Liability Management (ALCO) and the Committee on Development and management of information system of the Bank met at least once a month to set and discuss issues within the scope of its work and reported to the Board of Directors of the Bank.

ORGANIZATIONAL CHART OF HIPOTEKARNA BANKA AD PODGORICA




AUDIT BOARD
CREDIT RISK MANAGEMENT BOARD
EXECUTIVE DIRECTOR FOR RISK MANAGEMENT OPERATIONS
EXECUTIVE DIRECTOR FOR FINANCE AND IT
RISK MANAGEMENT DIVISION
FINANCE AND IT DIVISION
CREDIT ANALYSIS DEPARTMENT
RECOVERY AND WORKOUT DEPARTMENT
RISK MONITORING AND REPORTING DEPARTMENT
ACCOUNTING AND REPORTING DEPARTMENT
GENERAL AFFAIRS
CALCULATIONS AND SETTLEMENT DEPARTMENT
IT DEPARTMENT

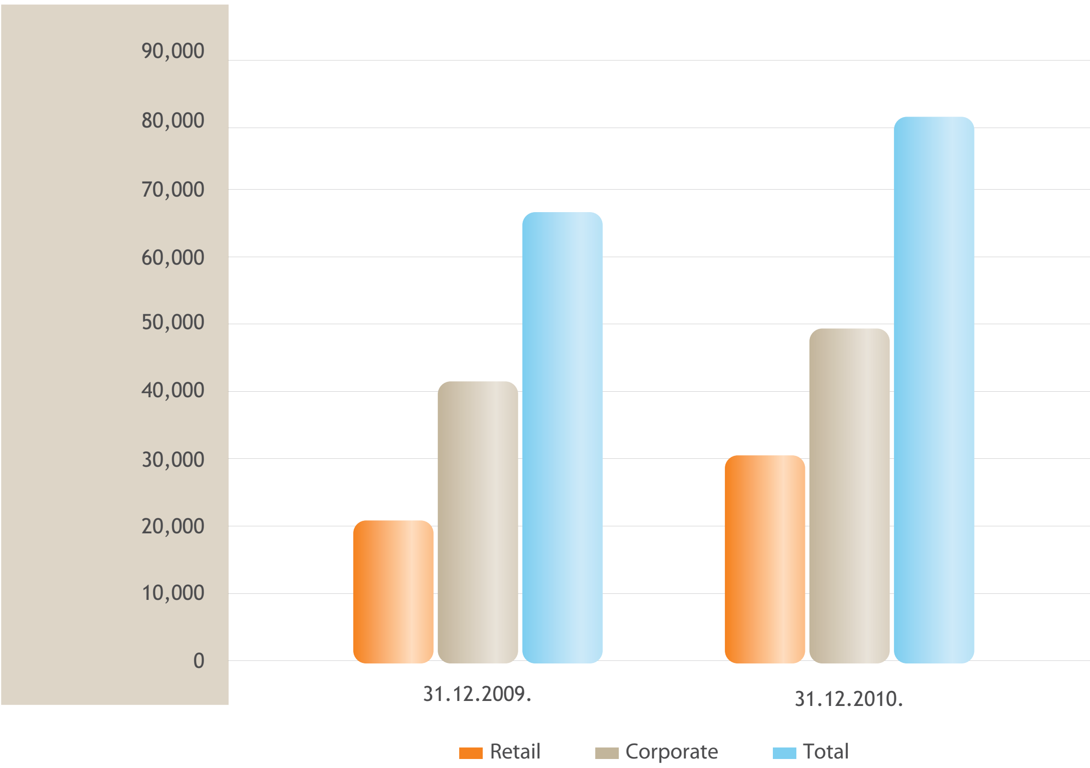
Business operations

Deposits

The macroeconomic environment in Montenegro during 2010 had an abundance of problems affecting the whole economy. This was a year of great challenges for the Montenegrin market as well.

Total deposits at the banking sector on an annual basis declined by 1.90%.

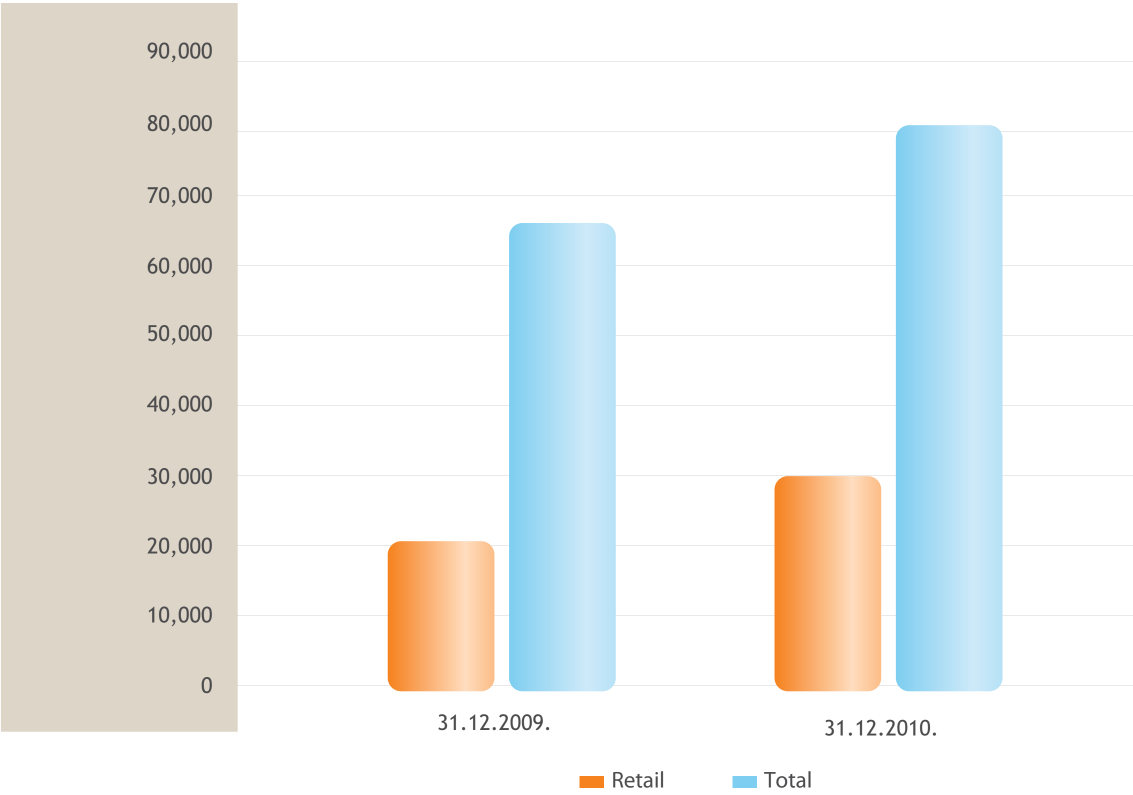
However, in 2010, Hipotekarna Bank continued an intensive campaign to increase savings, both retail and corporate. Recognized as a safe and highly liquid bank, is why the Bank's total deposits, compared to the previous year, increased by 22.08% and amounted to 85.13 million €.



In this business segment, the bank avoided the negative effects of the "crisis of confidence" that continue to affect the competition and significantly improved its market position. The percent of deposit growth achieved, shows the great confidence that citizens and companies have in Hipotekarna bank as well as an active approach to product sales, quality offer and a recognizable marketing approach.

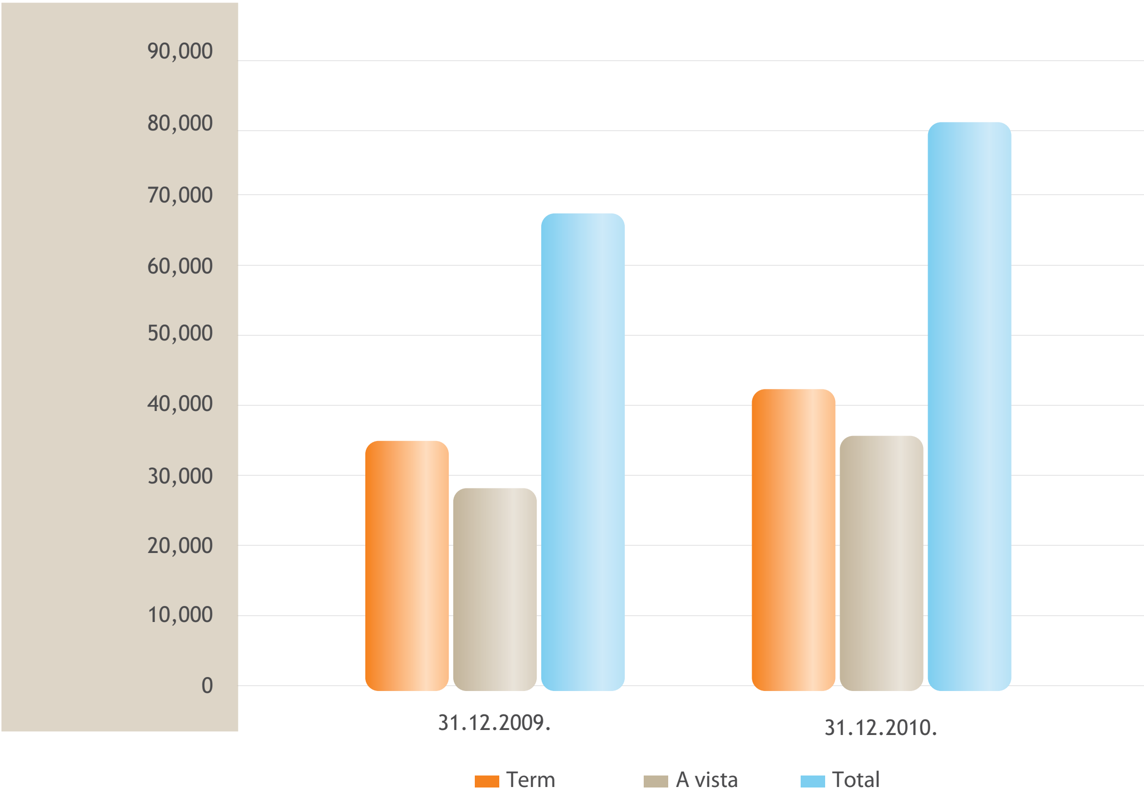
The growth in retail deposits as well as corporate deposits influenced the increase of total deposits.

The growth in retail deposits in comparison to 2009 was 33.28% and amounted to 33.07 mil €, while corporate deposits increased by 15.90% amounted to 52.06 mil €.



At the end of 2010, retail deposits accounted for 38.85% of total deposits, while the remaining 61.15% are corporate deposits.

At the end of 2010, term deposits participated in total deposits with 55.36%. In 2010 growth was recorded in a vista deposits of 22.53%, while term deposits increased by 21.72%.



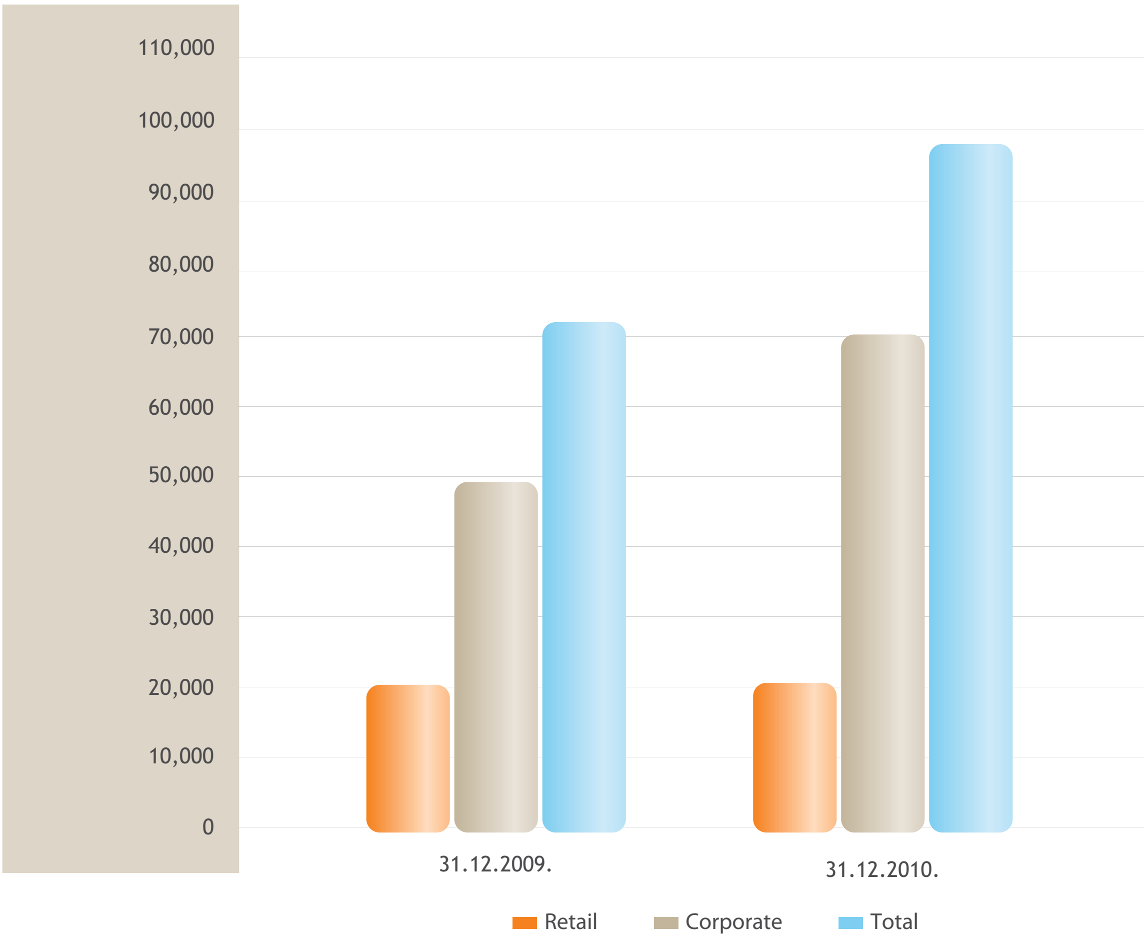
During 2010, the Bank considerably increased the number of clients. Approximately 7,400 retail accounts and approximately 1,400 corporate accounts were opened. Thanks to the innovative offer and different approach, together with a recognizable marketing campaign, during 2010 the Bank significantly increased the number of regular clients. The increase in number of customers is the result of a creative approach to marketing and expansion of the network.

Loans

In addition to the great challenges and consequences of the economic crisis which severely affected the economy and the banking sector, the Bank in this business segment achieved a score significantly better than planned in 2010.

In 2010, a year of great challenges, the Bank was very well prepared, using its stable financial position and experience in a very good assessment of the creditworthiness of their clients, putting quality before quantity. An unfavourable business environment during 2010 was a narrow framework for carrying out banking activity. In any case, Hipotekarna bank in this business segment achieved impressive results.

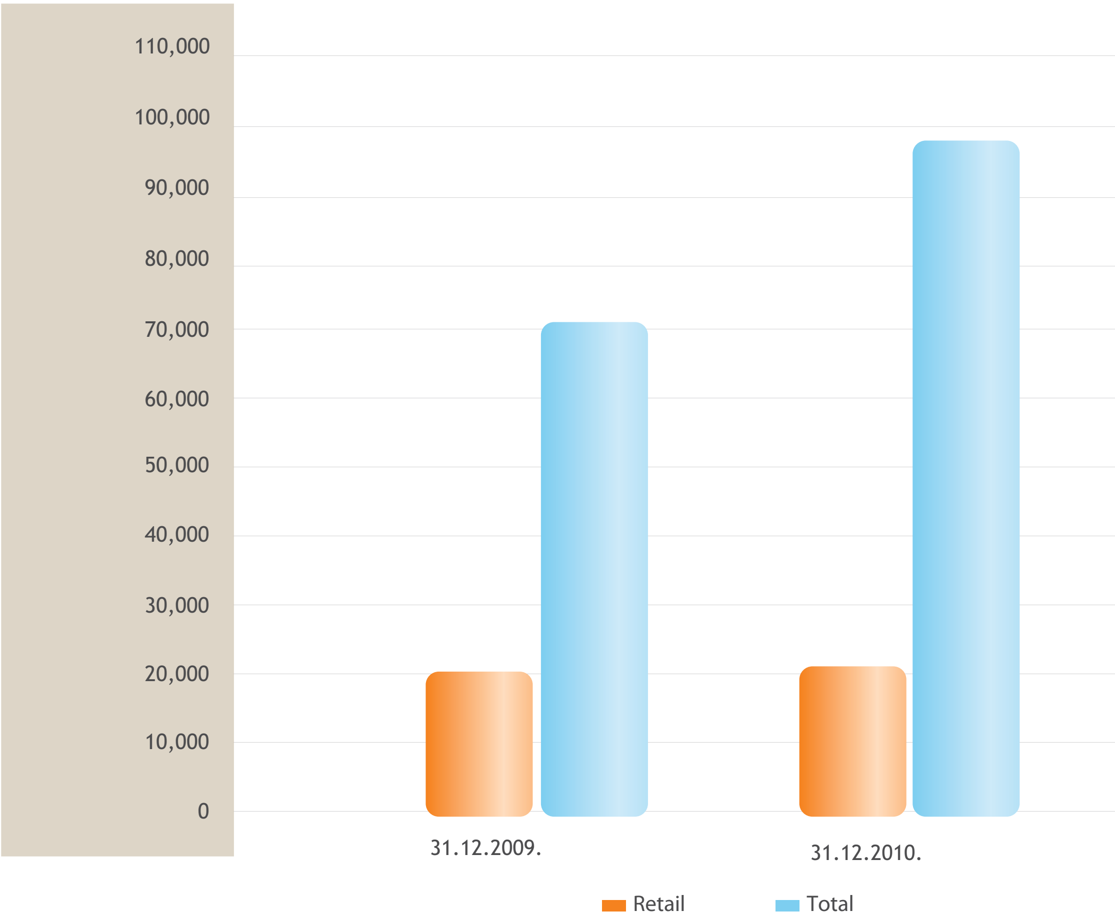
Gross loans at the end of 2010 amounted to 101.01 million € , which is an increase of 31.55% over the previous year. This figure is more impressive if we consider the fact that in the same period, the banking sector in this segment declined by 8.25%.

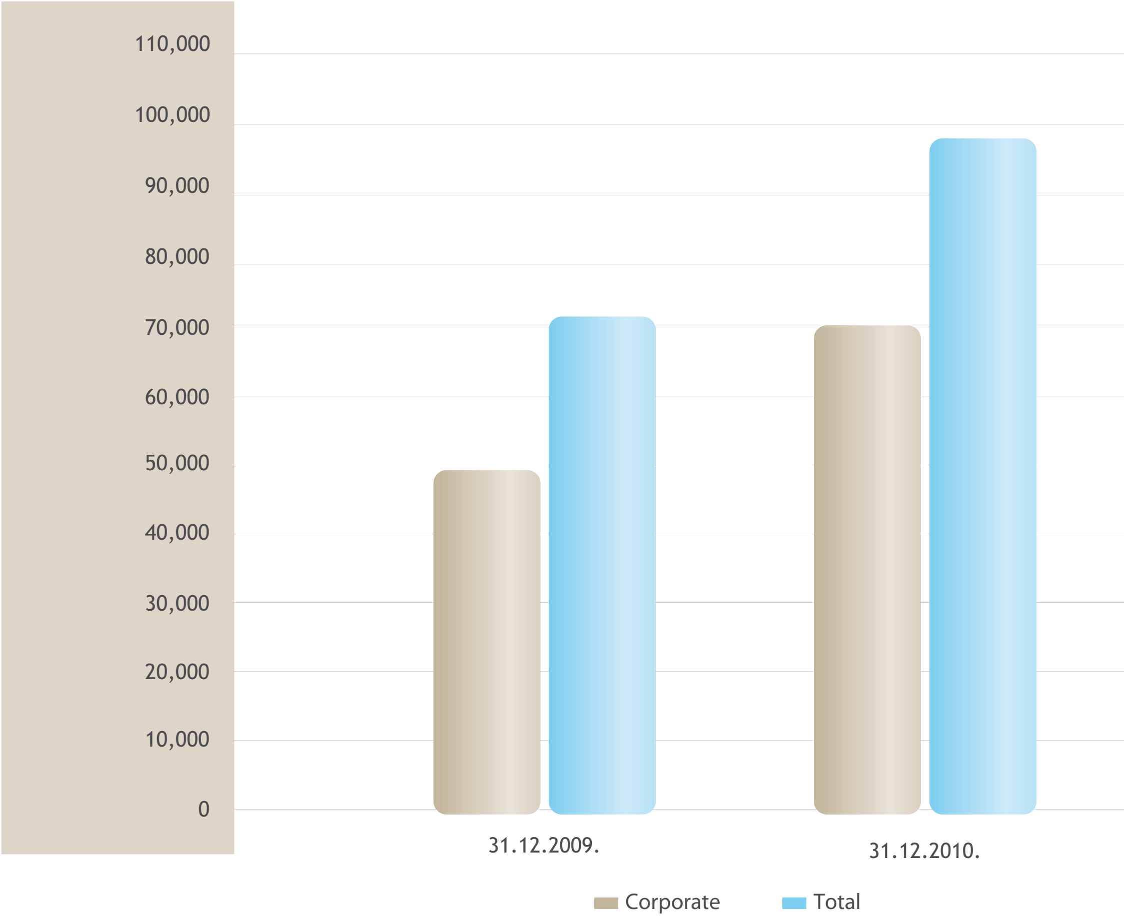


The growth in retail loans as well as corporate loans influenced the increase of total loans granted.

The amount of corporate loans increased by 43.45% at the end of 2010 amounting to € 75.52 million, while the amount of retail loans increased 5.60% and amounted to 25.49 million €.

In the structure of total loans, the retail loans account for 25.23% while the the corporate loans accounts for 74.77%.





Hipotekarna bank, in its business operations, mainly aims to provide credit to retail and small and medium enterprises. Hipotekarna bank, thanks to continuous lending and high liquidity, in the best way succeeded in meeting the needs of clients, both corporate and retail, in these circumstances. Due to this, a number of reputable Montenegrin companies have become our customers.

	31.12.2009	31.12.2010	Changes
GROSS LOANS	76,783	101,009	31.55%
PROVISIONS	1,980	2,657	34.19%
NET LOANS	**74,803**	**98,352**	**31.48%**

In cooperation with the European Investment Bank (EIB), Hipotekarna bank placed nearly 10 million € in 2010 and provided to small and medium enterprises (SMEs) loans at extremely favourable conditions regarding interest rate and repayment terms.

With the credit instruments of the EIB, the Bank finances the projects of small and medium enterprises in the fields of:

- industry,
- services,
- tourism,
- protection of wildlife, the environment and energy saving,
- infrastructure, etc...

In 2010, the bank granted 3,516 retail loans, 624 corporate loans and 950 guarantees to corporate, and fully implemented sales forecasts.

	No. of granted loans	Amount in €	Average amount in €	No. of approved guarantees	Amount in €	Average amount in €
RETAIL	624	99,937,379	160,156	950	28,199,245	29,683
CORPORATE	3,516	15,354,027	4,367	950	28,199,245	29,683

On the other hand, the bank's customers have justified their confidence by timely completing their obligations, so that the rate of collection of claims is above the average for the banking sector.

Business network and distribution channels

Concerning the fact that one of the aims of Hipotekarna bank AD Podgorica is strengthening and consolidating its business network, in 2010 a branch of the Bank was opened in Podgorica. This Branch of Hipotekarna bank directed its business activities on SMEs (Small and Medium Enterprise) and it is located in Blok VI, Đoka Miraševića M3 Street.

Also, the recent office in Kotor was relocated by opening a new branch which is located in a functional and modern space - Shopping Center Camellia - Square Mata Petrovic.

Both areas are in accordance with strict standards that include a process of adaptation of the latest banking standards and thus its position provides excellent access to customers.

The Bank business network consist of 8 branches and 6 offices, which represents a good base to produce good results in the forthcoming year.
In accordance with the constant expansion of the branch network, for the first quarter of 2011 opening new branches in Ulcinj, in November 26 Street is planned.

Hipotekarna bank will continue to be accessible to its clients through the expansion of the branch network and improvement of distribution channels.
Also, the Bank offers all types of guarantees, both for corporate and retail.

Advanced channels of distribution

In addition to the expanded business network, the bank is accessible to its clients also through the other channels of distribution – cash points, EFTPOS terminals, SMS and internet banking through Hb click service.

Hipotekarna Bank in the course of 2010 achieved growth in client numbers and increased the use of other distribution channels.

The ATM and POS terminal network is constantly expanding, so at the end of the year the bank had 13 ATMs and 250 EFTPOS terminals. Expanding the ATM and EFTPOS terminal network and development projects in this area directly influenced the increase in multi-scale acceptance of credit cards.

Hbklik services is another important segment of the Bank's offer, thus the number of users of this service is constantly increasing. In the course of 2010 the number of clients using this service increased by about 200%.

In the field of SMS banking a significant increase in the number of users was recorded. During 2010, 5,012 clients began using these services, thereby continuing the growth trend in this segment. With a desire to meet the needs of customers who use all the benefits of this service as effective ways to control their accounts, the bank continues to work on improvement and development of supply in this part, with the aim of providing better conditions for customers' business.

New products and services

Focusing on the requests and needs of its clients, the Bank continuously works on the improvement of its current offer, and the development of new products and services, endeavouring to achieve and maintain quality and competitiveness in the market.

The retail loan offer has increased with a new kind of loan intended for students "Pure 10" which at the same time provides payment of tuition fees for three years of study and term deposit.
Also, the offer is extended by loans based on life insurance policies, as well as the "JOKER" loans that provide many benefits that can be used during the repayment period.

Clients who, as a result of the economic crisis, encountered difficulties in payment obligations, were offered the possibility to restructure loans by the bank.

Also in 2010, the Bank expanded its standard offer of saving products with several appropriate actions with the aim of stimulating the term saving of retail as well as corporate. One of those actions is the week of savings, which Hipotekarna bank, now traditionally, performs in cooperation with the Central Bank of Montenegro.

The bank's policy is to always try to meet the expectations of existing customers and attract new clients, while minimizing risks and ensuring increased security investments.

Corporate Social Responsibility

Hipotekarna bank as a socially responsible company, donated again this year nearly 10% of its net profit for the activities in this field. Adhering to these principles, Hipotekarna bank conducted the following acitivities in year 2010:

- Donated the funds for purchasing medical equipment for the Clinical Center of Montenegro, Department of Ginecology
- Sponsored an international festival of short stories, “Where I’m Calling From”
- Sponsored an exhibition of photographs
- A children’s edition book “Disney”;
- Kindergarten “Đina Vrbica “
- Amateur Radio Club
- Sponsored two fashion shows,
- And a premier basketball league, “Hipotekarna bank”, and the women’s handball club “Budućnost”

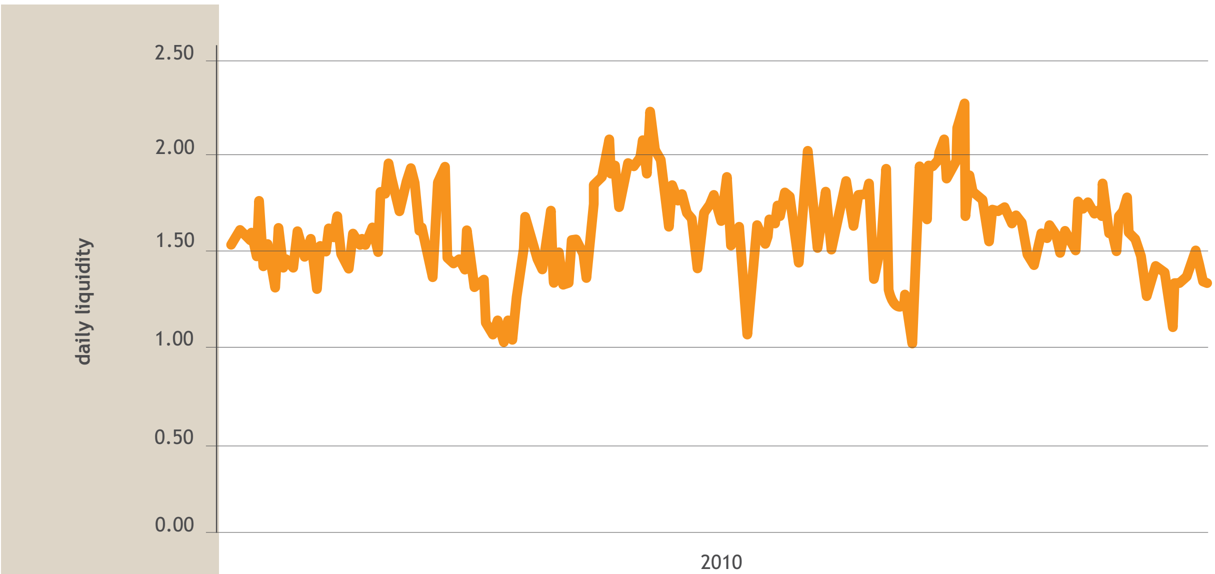
Realizing the importance of implemented activities and our role in society, Hipotekarna bank will in continue with this practice in the future.

Treasury

In 2010, Hipotekarna Bank placed an emphasis on stabilizing domestic sources of funding, expansion of the client base, reducing short-term in favour of long-term sources of funding and withdrawal of new credit lines from foreign banks and international financial institutions.

In 2010, the Payment operation and Treasury Division, especially Treasury Department succeeded to maintain liquid assets and the overall liquid position of the Bank at a satisfactory level. In addition, the Treasury department performed a reconciliation of sources of funds with placements by daily, weekly, decadal and monthly scheduling of available liquid assets. All of the above enabled the Bank to regularly fulfil its obligations toward creditors as well as fulfil every customer requirement in the shortest time.

The daily liquidity ratio, which is calculated by the methodology recommended by the Central Bank of Montenegro varied throughout the 2010, above the legally required minimum of 0.90.



Considering that the effects of global economic crisis significantly felt throughout 2010 and taking into account the customers' cautiousness when it comes to the disposal of their own funds, it can be concluded that in these circumstances Hipotekarna Bank has been recognized as one of the most reliable and liquid banks in banking system of Montenegro. To support this claim, data shows that at the end of 2009, total deposits of the Bank were amounted to 69.7 million EUR and at the end of 2010, total deposits of the Bank amounted to 85.1 million EUR, which represents an annual growth of 22.09%. Liquidity surpluses, except through credit activity, were placed in marketable securities.

In 2010, Hipotekarna Bank participated in auctions of government securities where, in accordance with the decision of the Central Bank of Montenegro, up to 25% of funds from obligatory reserve were placed. Through the activities of the Custody Department and Brokerage-Dealer Department, Hipotekarna Bank placed assets in other securities that are traded on the Montenegro stock exchange as well as stock exchanges in the region.

There were large fluctuations in exchange rates in 2010, in particular the currency pair EUR/USD, which had the greatest impact on the Bank's exposure to the exchange rate risk. In these circumstances the Treasury Department managed to achieve remarkable results regarding income from realized exchange rate differences as a result of adequate exchange rate risk management. The total net result at the end of 2010, from foreign exchange differences amounted to 223 thousand EUR which had a significant impact on final financial result of the Bank.

At the beginning of 2010, necessary corrections and additions to existing internal regulations were made as well as the adoption of new documents that define the jurisdiction and responsibilities of the Treasury Department, all in accordance with valid legislation in Montenegro and modern banking practices.

Payment operations and the Treasury Division expanded cooperation with foreign banks as well as with international financial institutions. In the course of 2010, Hipotekarna Bank concluded two arrangements with the European Investment Bank for the project of financing small and medium enterprises, based on arrangement between the Government of Montenegro and the European Investment Bank. Also, the Bank concluded credit arrangement with the international financial organization European Fund for Southeast Europe. Considering these arrangements, Hipotekarna Bank provided credits to the market with lower interest rates and with longer terms.

Payment operations

The Bank's overall payment operations in 2010 were characterized by the growth of all parameters which define the Bank's business operations in this segment. All business plans which had been previously set up were completely exceeded which clearly shows the Bank's efficiency and progress over the previous year.

Domestic payments

The main characteristic of domestic payment operations in 2010 was the raise in the efficiency in processing payment operation transactions both at the Bank counters and electronics payment operations, growth in the number of clients and especially the number of opened accounts for retail.

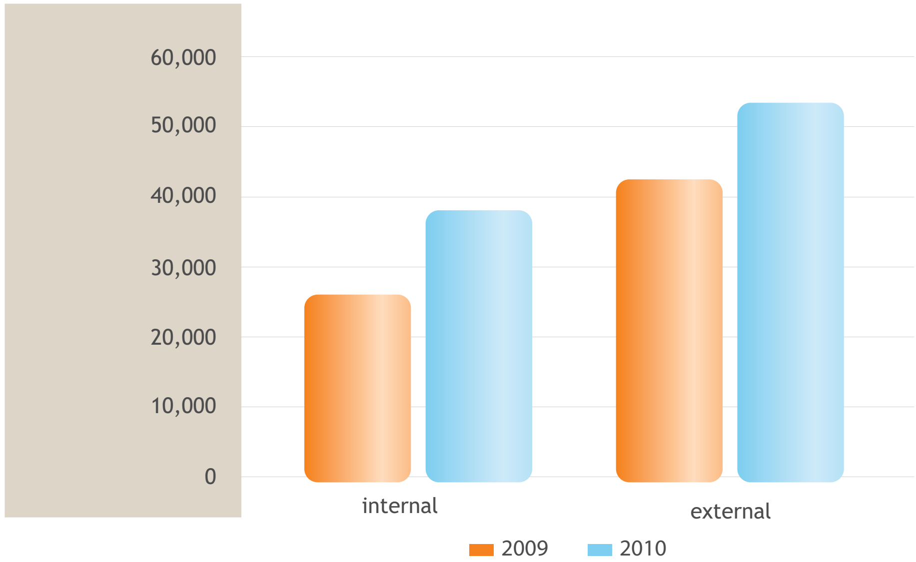
The total number of opened client accounts rose by 57% in comparison to 2009. The highest increase was accounts opened by private individuals. The number of accounts opened by private individuals rose by 67% and for legal entities this increase was 7%. More than half of accounts opened by private individuals were accounts for their regular earnings. The increase in this type opened accounts was 133%.

The number of payment transactions rose by 31% in comparison to 2009. The highest increase was achieved in the number of internal payment transactions between the bank's clients. This increase was 43% in comparison to the previous year which clearly shows the raise in the number of the bank's clients which execute their payments within payment system of the Bank i.e. internally.
The Bank achieved the raise of external outgoing payment transactions in favour of other domestic bank's clients which rose by 23% in comparison to 2009. As to the structure of the external outgoing payments the participation of 'low value' payments (< EUR 1,000 rose by 21%) and 'high value' payments (> EUR 1,000 rose by 27%) were almost equal.

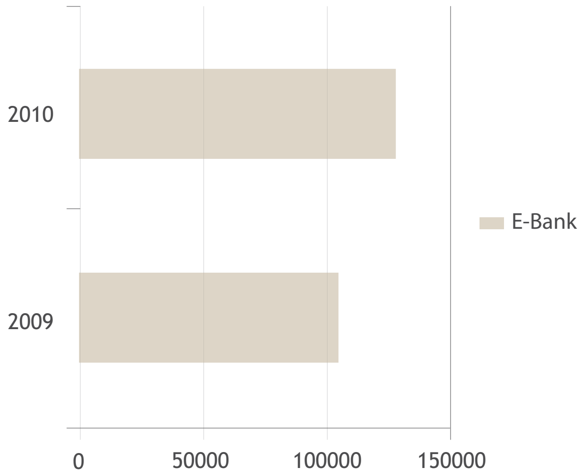
Incoming payments from clients of other domestic banks also rose by 15% in comparison to the previous year.

The significant increase was achieved in the number of electronic outgoing payment transactions (e-bank) which means that clients more often used electronic payments orders. This raise was 27% in comparison to the previous year.

Domestic payment transactions



Domestic outgoing e-payment transactions



International payments

International payments in 2010 featured growth in all types of payment transactions, incoming and outgoing, documentary operations and other transactions.

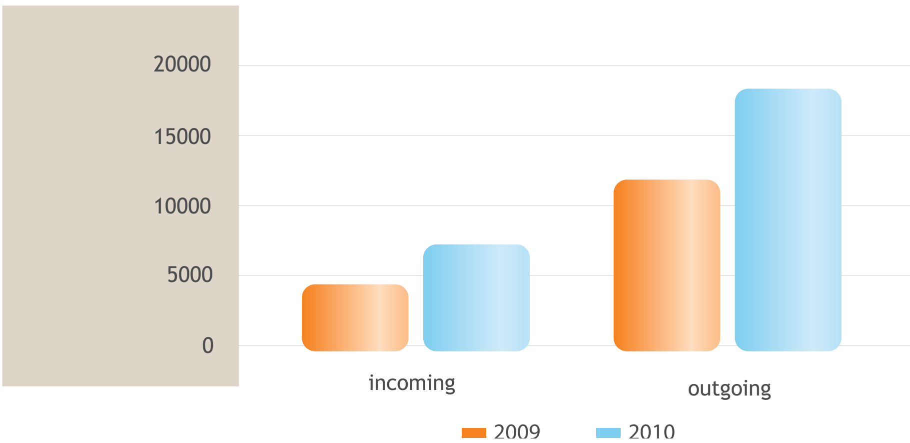
The total number of accounts opened rose by 37%. The number of accounts opened by private individuals rose by 54% while this number for legal entities rose by 13% in comparison to 2009.

All type of transactions increased in comparison to the previous year. The Bank has already been recognized as an efficient and reliable partner by other foreign banks.

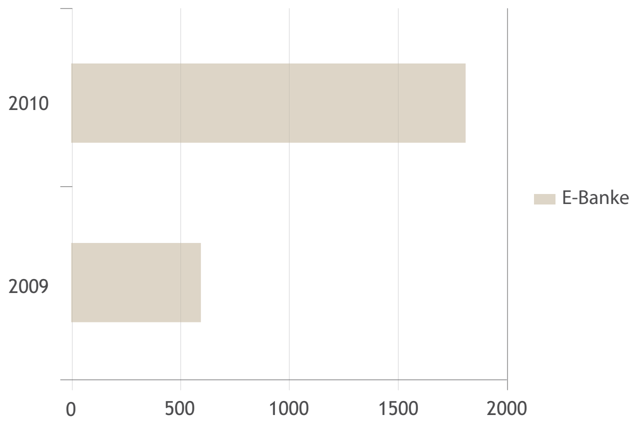
The number of outgoing payment transactions rose by 51%. The highest growth was achieved in the number of electronic outgoing payment transactions by using the e-bank application in comparison to 2009 which rose by 189%.

The number of incoming payment transactions rose by 43% in comparison to the previous year.

International payment transactions



International outgoing e-payment transactions



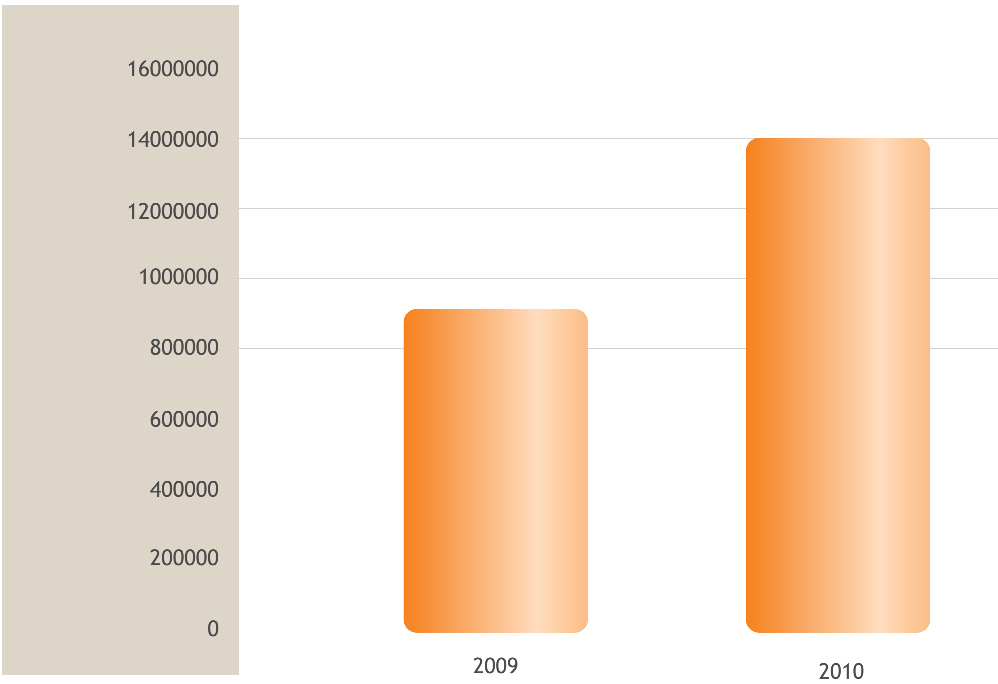
Regarding international relations, the Bank is already recognized as a professional partner and has already gained a significant international reputation. Therefore, the continued increase in the number of documentary operations is not a surprise.

The number of opened Letters of Credit rose by 24% in comparison to the previous year.

The highest growth was accomplished in the number of issued Letters of guarantee which rose by 70% in comparison to the previous year.

The overall payment operations increased compared to the previous year. The efforts made by all employees to raise their working efficiency with the use of efficient technical and software solutions and supports created the growth in all payment operations parameters.

The total revenues of the commissions of payment operation services rose by 48% in comparison to 2009. The increase of the revenues of the domestic payment operations commissions rose by 47% and for the international payment services commissions rose by 59% in comparison to the previous year.



Information technology

In 2010, Hipotekarna Bank significantly upgraded its information system both in areas of reliability and security, as well as in the area of efficiency. The result of the aforementioned is a positive report by the auditor Ernst & Young, which states the high quality of the information system.

In 2010, the Board of Directors of Hipotekarna Bank adopted procedures on controlling physical access, monitoring performance of suppliers, classification of data, monitoring of system events, Internet usage, managing incidents, etc.

In line with these procedures, regular monitoring of end users and administrators on all levels has started. System performance and capacity, incidents and problems occurring in the information system, as well as the performance of suppliers are regularly monitored.

Within the area of infrastructure projects, a monitoring system of all Bank services was implemented, along with e-mail and SMS notification on all system events. A new e-mail platform has been implemented which allows the archiving of all outgoing and incoming e-mail traffic, keeping all messages server side, centralized administration, etc. IBM Tivoli centralized backup appliance has also been implemented, which allows backup of all client computers, as well as backup of the complete server infrastructure.

The Bank worked on improving data centres at primary location and disaster recovery location. Climate control appliances were installed on both locations, in line with standards. On both locations a system for automatic fire fighting has been implemented, which uses FM-200 gas which is harmless to computer equipment and personnel.

The number of services which are available at the disaster recovery location were expanded, therefore the Bank has all important services at the disaster recovery location, ensuring undisturbed operation in case of problems with the primary location.

Redundant communication equipment has been put in service in every segment, and taking into account that redundant links to branch offices were already in place, maximum communication availability has been provided.

It is important to emphasize the fact that new members of IT sector were employed in 2010 regardless of the crisis, in order to achieve a proper segregation of duties, thus ensuring the quality and safety of the information system.

Investment banking

2010 was marked by a drastic turnover decline followed by a price stagnation in the Montenegrin capital market. Gross turnover was 54.73 million EUR, which is almost two-thirds less compared to the critical year 2008, when gross turnover came to 157.26 million EUR. Turnover was lower compared to 2009, when the partial privatization of Elektroprivreda Crne Gore AD Nikšić took place, when total turnover amounted to 421.42 million EUR, or compared to the record year 2007, when the gross turnover amounted to 729.49 million euro.

The reason for this dramatic decline lies in fact that in the past year none of the major privatization enterprise occurred, which would enable the increase the turnover of shares which are not State held. Also, the funds gained from the partial privatization of Elektroprivreda Crne Gore AD Nikšić which was conducted in 2010, have not remained on capital market at the expected volume.

A hope for higher turnover volume in the year 2011 lies in the stock exchange - Montenegroberza, which started its activity on 1st January 2011. This made Montenegro no longer an exception in the region with two capital markets, with more or less, the same securities traded on both of them. That was, among the other issues, a major reason why major foreign investors avoided the Montenegrin market, often because in the reports from two stock exchanges one could find different prices for some shares. Unification of these two stock exchanges should bring a reduction in expenses in this market segment.

At both Montenegrin stock exchanges, three types of securities are traded: company shares, privatization-investment fund shares and bonds. These include: Old Currency Savings Bonds, Restitution Fund Bonds and Local Self-Government Bonds. Our Bank was one of the leaders in terms of turnover of all types of securities in the Montenegrin capital and debt market.

2010 was successful for the Custody department, while the Brokerage-Dealer Department of Hipotekarna bank, established at the very beginning of 2010, due to the procedure of getting the working permit, started its activities in April of 2010. Despite that fact, until the end of the year total turnover amount was 11.2 million EUR, which provided a market share of 10.2% in just 9 months. With this figure, Hipotekarna bank positioned itself fourth on the Montenegrin capital market by total turnover volume.

A total turnover of 11.2 million EUR was made through 465 transactions, with the commission income of about 60,000 EUR in the previous year. In 2010, 971 trade orders were received, and 196 orders were executed completely.
Hipotekarna Bank started its activities as a dealer in the IV quarter of 2010.

Risk management

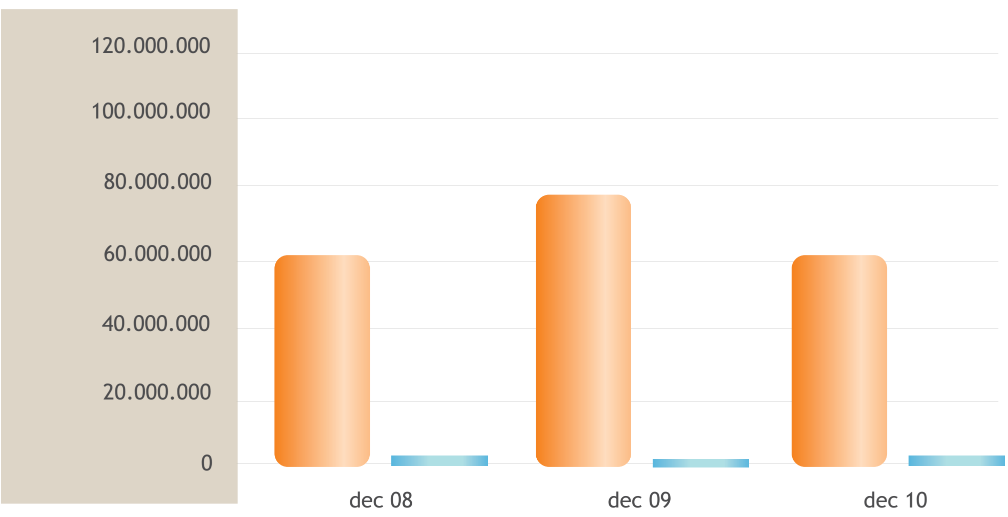
Risk management focuses primarily on the identification, measurement, monitoring and controlling the risks that bank faces in its operations. With an active approach to those issues, the risk department implemented the techniques and procedures in order to create a modern system for managing risks in accordance with legislation of the Central Bank of Montenegro. According to this, the Risk Department systematically and continuously monitors the following types of risk: credit risk, market risk, liquidity risk, country risk and operational risk.

Credit risk

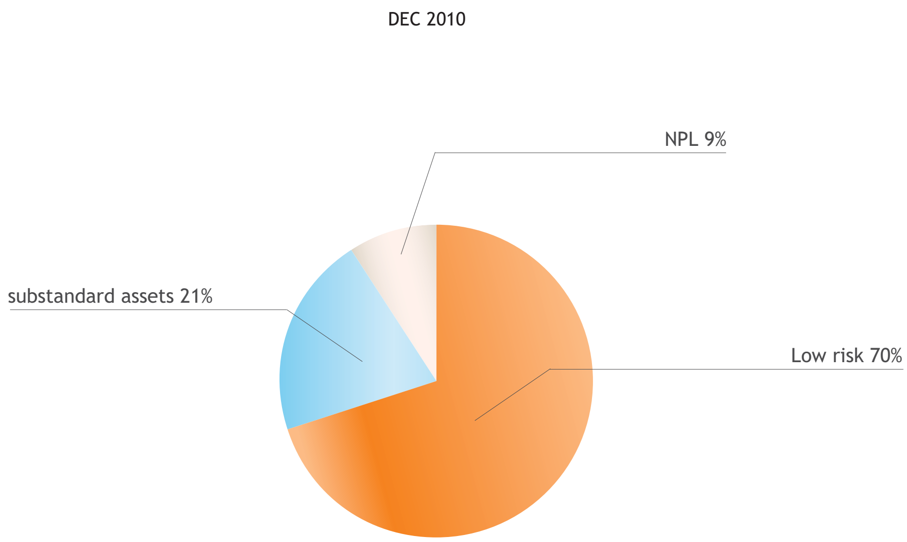
The Bank is managing credit risk on two complementary levels: at individual level and at portfolio level. In this way the Bank has established an effective system for identifying, measuring, monitoring and controlling credit risk, which provides a timely assessment of the impact of the credit activity on available capital and projected financial result of the bank.

The portfolio of the Hipotekarna banka at December 31, 2010 amounted to EUR 101,009,877.00. This is an increase of EUR 24,227,108.00 or 31.55% compared to December 31, 2009. Provisions for loan losses at December 31, 2010 were EUR 2,656,844.00 or 2.63% of the loan portfolio. Compared to the end of 2009 provisions increased by EUR 676,539.00 or 34.16%.

Portfolio/provisions 2008-2010



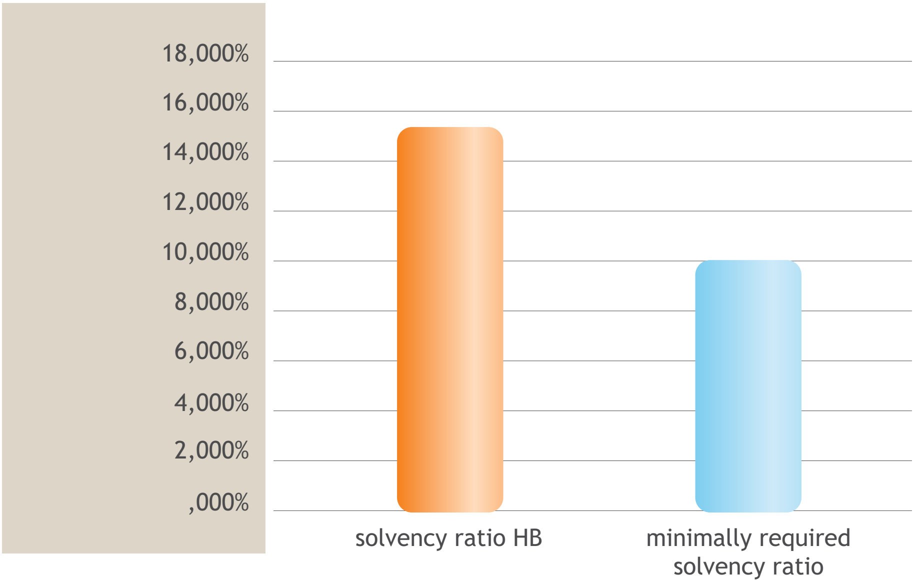
From the total loan portfolio of the bank, 70% is in high quality assets (A and B1 rating grade); 21% substandard assets (B2 rating grade) and on the NPL (non performing loans: C1;C2;C3;D and E (Write off)) 9%.



The amount of loans with delinquency in repayments over 30 days at December 31, 2010 amounted to EUR 5,068,406.00 or 5% of the Bank’s total loan portfolio. At the end of 2009 the amount of loans in arrears was EUR 2,860,800.00 or 3.73% of the bank’s total loan portfolio.

Solvency ratio

At December 31, 2010 the solvency ratio was above the statutory limit (10%), and amounted to 15.54%. The solvency ratio is the most important indicator of confidence in the bank and it serves as a protector of the deponents, creditors and business partners of the bank.



Equity

Total equity in 2010 amounted to 21.623 million EUR. Compared to the previous year, equity increased by 6.36%. At 31 December 2010, the nominal value of shareholders' equity amounted to 16,006 million. Shareholders' equity consists of 31,305 shares, each with a nominal value of 511.29 Euros. By ownership structure, foreigners own 86% of equity, while the remaining equity is owned by domestic entities and individuals.

Income statement

In 2010, the Bank achieved a profit amounting to 1,292 million EUR. Interest income in the previous year increased by 41.12% to 9,634 million EUR as a result of increased lending activity. Fee and commission income in the previous year increased by 48.78% to 3,105 million EUR. Net interest, fee and commission income creates 82.60% (35.17%) of all Bank's incomes from current operations. Other income in the previous year decreased by 59.57% to 399 thousand EUR.

Operating expenses, including depreciation, amounted to 6,827 million EUR and increased by 22.11% over the previous year. Increase in costs is the result of the expanded branch network, employment of new staff and the increase in other expenses that accompany the bank's growth and development.

Assessment of the credit risk and making provisions for risky loans and the potential liabilities for the Bank, are based on the application of the principles of conservative policy and implementation of applicable laws. Total allocated reserves for assets and liabilities amounted to 3,142 (3,637) million EUR as at 31 December 2010.

Distribution of profit

The Bank's management suggests to the Board of Directors to jointly propose at the Shareholders' Meeting that the total profit in 2010 be used to cover the losses from the previous period.

3.] Financial Statements for the year ended December 31, 2010 together with the Independent Auditor's Report

Ernst & Young Montenegro d.o.o.
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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.

PIB - 02759080 • Matični broj - 02759080 • Upisan i unijet osnovni kapital: 5.000,00 EUR
Registarski broj: 5-0537154/001 kod Centralnog registra Privrednog suda u Podgorici
Poslovni račun: 2325011-02759080 kod Crnogorske Komercijalne Banke AD Podgorica

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.

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

	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 interest, 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 Extraordinary expenses		**263**	**37**
Vanredni rashod		**(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 Bank A.D., Podgorica, on January 17, 2011 in Podgorica.

Balance sheet
as at december 31, 2010

	Notes	2010	2009
ASSETS			
Cash and deposit accounts held with depository institution	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**

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

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Statement of changes in equity for the year ended december 31, 2010

	Capital	Share premium	Share reserves	Other reserves	Revaluetion Accumula-ted	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.

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

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 Bank A.D., Podgorica, on January 17, 2011 in Podgorica.

Notes to the financial statements

1. FOUNDATION AND BUSINESS ACTIVITY

Hipotekarna Bank 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.

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.

3.6. 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.

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:

	As at December 31, 2010		As at December 31, 2009	
Risk category	% 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.

3.10. 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.

3.11. 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.

3.12. 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. Concurrently, employees are entitled to jubilee awards for each 10, 20 and 30 consecutive years of service within the Bank. 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 and jubilee awards 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

31. decembra	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**

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

In thousand 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 and brokerage dealer 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	**-**

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. 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**

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	Construc-tion pro-gress	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	-
	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**

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-	-
LONG-TERMS LOANS APPROVED BY FOREIGN CREDITORS				
European Investment Bank ("EIB")	12	4.032%	2,600	2,600
European Investment Bank ("EIB")	12	3.923%	1,400	1,400
European Investment Bank ("EIB")	12	3.604%	4,000	-
European Investment Bank ("EIB")	12	3.168%	2,010	-
European Investment Bank ("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	Anally 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**

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

	2010.	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:

	2010.			2009.		
Shareholder	**Number of shares**	**In thousands ofEUR**	**% share**	**Number of shares**	**In thousands ofEUR**	**% share**
Flandria Participations Financieres						
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 broker dealer services	13,614	7,243
- collaterals	246,954	176,949
- written-off loans receivables	1,819	1,714
- current contracts for transactions with foreign currency / prompt sale of foreign currency	801	-
	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
Interest payables:	530	3,700
- Miljan Todorović		
Total payables	-	3
	-	3
Ukupno obaveze	**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.

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	-	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

A. ANALYSIS TO FINANCIAL STATEMENTS FOR 2010

I Introduction

Financial Statements of Hipotekarna Bank 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:

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

In thousand of EUR

	2010			2009		
	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**	**100.00%**

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.

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. 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 Bank 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.

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

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

Odlukom Centralne banke o minimalnim standardima za upravljanje tržišnim rizicima u bankama uspostavljeni su sljedeći limiti koji se odnose na otvorenu deviznu poziciju:

- 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.

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

In thousand 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).

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;
- 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.

IV
Rizik zemlje

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
    5.4. Služba za nadzor i izvještavanje o rizicima

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	In %	3	In %	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.

DATA ON BOARD OF DIRECTORS COMPOSITION, CREDIT RISK MANAGEMENT COMMITTEE, SUPERVISORY COMMITTEE, GENERAL DIRECTOR AND 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%

4. About the Bank

Bank's management and organizational structure

Board of directors
Sigilfredo Montinari, Chairman
Božana Kovačević, Deputy Chairman
Snježana Pobi, Member
Renata Vinković, Member
Esad Zaimović, Member

Audit Board
Marko Žigmund, Chairman
Božana Kovačević, Member
Jovan Papić, Meber

Credit Risk Board
Renata Vinković, Chairman
Esad Zaimović, Member
Snježana Pobi, Member

Bank's Executives
Esad Zaimović CEO
Aleksandar Mitrović
Jelena Vuletić
Ana Golubović

Chief Internal Auditor
Veselin Ivanović

AML officer
Mirjana Jovanović

Administrative service and Human Resources
Boban Ličina

Compliance
Slavko Rakočević

Security of IT system
Haris Dizdarević

Divisions
Payment operations and Treasury, Esad Zaimović CEO
Commercial, Ana Golubović
Risk, Jelena Vuletić
Finance and IT, Aleksandar Mitrović

Retail Network

P O D G O R I C A – Head office, Josipa Broza Tita, No. 67
P O D G O R I C A, Slobode No. 19
P O D G O R I C A – Vektra, Bulevar revolucije, No. 2A
P O D G O R I C A - Blok VI, Djoka Mirasevica M3
TUZI, Tuzi bb
N I K Š I Ć, Save Kovacevica No. 6
BIJELO POLJE, Slobode bb
B A R, Marsala Tita, No. 15
B U D V A, Mediteranska, No. 4
C E T I N J E, Bajova, No. 74
K O T O R, Shopping Center Kamelija - Trg Mata Petrovica
T I V A T, 21. novembra, No. 21
HERCEG NOVI, Njegoseva, No. 52
B E R A N E, Mojsija Zecevica bb