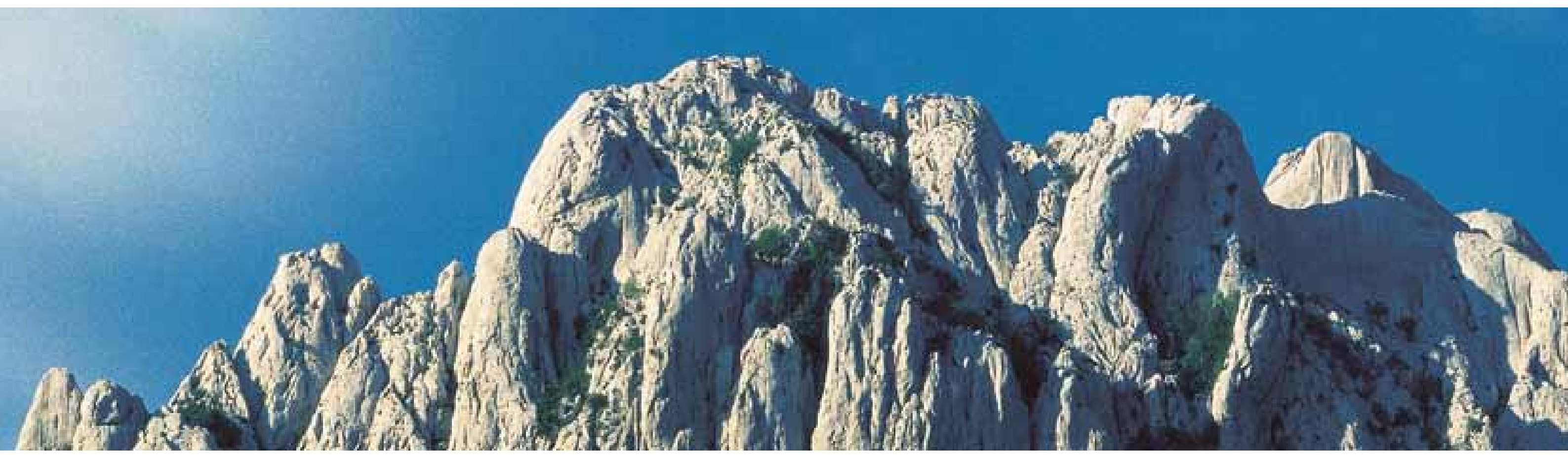
PRIVREDNA BANKA ZAGREB

Annual Report | 2012



PBZ, a bank of INTESA SANPAOLO

PBZ

Annual Report 2012

Gorski kotar - Klek

Table of contents

7 Who we are and what we do
8 Introduction
9 Five year summary and financial highlights
10 Report from the President of the Supervisory Board
13 Management Board report of the Status of the Bank
17 Management Board report on the Status of the Bank's subsidiaries and financial highlights of the Group
22 Review of the international and Croatian economy in 2012
32 Organisational chart
34 Business description of the Bank
42 The Group
48 Overview of the activities within the Corporate Social Responsibility programme of PBZ
52 Corporate governance
53 Statement on the implementation of the Code of Corporate Governance at Privredna banka Zagreb
64 Responsibilities of the Management and Supervisory Boards for the preparation and approval of the annual financial statements
66 Independent auditors' report to the shareholders of Privredna banka Zagreb d.d.
68 Income statement
69 Statement of comprehensive income
70 Statement of financial position
72 Statement of cash flows
74 Statement of changes in equity
76 Notes to the financial statements
168 Appendix 1 - Supplementary forms required by local regulation
185 Appendix 2 - Supplementary financial statements in EUR (unaudited)

Medvednica - Medvedgrad

Cetina - Omiška Dinara

Who we are and what we do

We are the leading Croatian financial services group engaged in retail and corporate banking, credit cards, investment banking, asset management, private banking, leasing and real estate activities and investment management services. We operate in the entire area of Croatia and employ over four thousand people.
Our mission is to permanently and effectively utilize all of the resources at our disposal to continuously improve all aspects of our business activities, including human resources, the technology and the business processes.
Our vision is to be the model company and the centre of excellence in creating new value, as well as provision of high-quality service in all of our activities for the benefit of our clients, the community, our stakeholders and our employees.

1,683 thousand
TOTAL CUSTOMERS

HRK 54.2 billion
TOTAL CUSTOMER LOANS

749 thousand
CURRENT ACCOUNTS

HRK 10.6 billion
TOTAL HOUSING LOANS

HRK 66.0 billion
TOTAL CUSTOMERS' FUNDS*

2,230 thousand
TOTAL CARDS ISSUED

HRK 2 billion
ASSETS UNDER MANAGEMENT

28,158
EFT POS

250 thousand
INTERNET BANKING USERS

670
ATM MACHINES

211
TOTAL BRANCHES

102
DAY AND NIGHT VAULTS

**Comprises customers deposits, assets under management and assets in custody*

Introduction

The Management Board of Privredna banka Zagreb d.d. has the pleasure of presenting its Annual report to the shareholders of the Bank. This comprises a summary of financial information, management reviews, the audited financial statements and the accompanying audit report, supplementary forms required by local regulation and unaudited supplementary statements in EUR. Audited financial statements are presented for the Bank and the Group.

Croatian and English version

This document comprises the Annual Report of Privredna banka Zagreb d.d. for the year ended 31 December 2012 in the English language. This report is also published in the Croatian language for presentation to shareholders at the Annual General Meeting.

Legal status

The Annual Report includes the annual financial statements prepared in accordance with International Financial Reporting Standards and audited in accordance with International Standards on Auditing.
The Annual Report is prepared in accordance with the provisions of the Companies Act and the Accounting Law, which require the Management Board to report to shareholders of the company at the Annual General Meeting.

Abbreviations

In this Annual Report, Privredna banka Zagreb d.d. is referred to as “the Bank” or “PBZ” or as “Privredna banka Zagreb”, and Privredna banka Zagreb d.d., together with its subsidiary undertakings are referred to collectively as “the Group” or “the Privredna banka Zagreb Group”. The central bank, the Croatian National Bank, is referred to as “the CNB”. The European Bank for Reconstruction and Development is referred to as "EBRD".
In this report, the abbreviations “HRK thousand”, “HRK million”, “USD thousand”, “USD million” and “EUR thousand” or “EUR million” represent thousands and millions of Croatian kunas, US dollars and Euros respectively.

Exchange rates

The following mid exchange rates set by the CNB ruling on 31 December 2012 have been used to translate balances in foreign currency on that date:

CHF 1 = HRK 6.245343
USD 1 = HRK 5.726794
EUR 1 = HRK 7.545624

Five year summary and financial highlights

in HRK milion	2012	2011	2010	2009	2008
Group					
Income statement and statement of financial position					
Total gross revenue	5,468	5,569	5,356	5,888	6,001
Net interest income	2,406	2,480	2,200	2,060	2,185
Net operating income	3,761	3,874	3,555	3,607	3,697
Net profit for the year	1,014	1,268	1,022	960	1,242
Total assets	72,554	74,154	74,409	71,541	71,227
Loans and advances to customers	49,960	51,398	49,418	47,356	46,032
Due to customers	48,143	47,431	47,054	45,049	44,591
Shareholders' equity	12,788	12,322	11,334	10,600	9,611
Other data (as per management accounts)					
Return on average equity	8.14%	10.86%	9.38%	10.09%	14.84%
Return on average assets	1.29%	1.61%	1.35%	1.29%	1.71%
Assets per employee	17.4	17.9	18.3	17.2	15.7
Cost income ratio	43.6%	44.00%	47.45%	47.18%	49.78%

in HRK million					
	2012	2011	2010	2009	2008
Bank					
Income statement and statement of financial position					
Total gross revenue	4,489	4,591	4,365	4,921	4,851
Net interest income	2,213	2,268	1,962	1,799	1,941
Net operating income	3,035	3,146	2,789	2,800	2,774
Net profit for the year	846	1,136	860	927	1,100
Total assets	68,411	67,481	67,352	64,519	63,740
Loans and advances to customers	46,918	46,691	44,585	42,271	41,715
Due to customers	46,973	44,081	43,602	41,903	40,935
Shareholders' equity	11,726	11,194	10,346	9,802	8,870
Other data (as per management accounts)					
Return on average equity	7.49%	10.65%	8.61%	10.45%	13.94%
Return on average assets	1.19%	1.61%	1.28%	1.41%	1.69%
Assets per employee	18.1	19.0	19.4	18.1	17.1
Cost income ratio	41.9%	41.96%	46.02%	44.49%	46.79%

Report from the President of the Supervisory Board

On behalf of the Supervisory Board of Privredna banka Zagreb, I am honoured to present you the business results of the Bank and Group for 2012.
Although 2012 was a challenging year for Privredna banka Zagreb and its Group, we managed to perform reasonably well. This achievement is a direct result ensuing from our thoughtfully planned strategy and its comprehensive execution along with momentous aide by our long-term strategic accomplices: the parent bank Intesa Sanpaolo and our strategic partner the European Bank for Reconstruction and Development.
From the macroeconomic perspective the past year will be remembered as uneasy. The falling trend of gross domestic product that had started in 2008 continued throughout 2012. This negative trend was mainly caused by a fall in domestic demand, primarily household consumption and investments. If it had not been for relatively dynamic export sector, especially tourism, the fall would have been even more pronounced. Lack of highly-awaited structural and fiscal reforms was the main driver that, for the first time since getting sovereign rating in 1996, the Croatian rating was pronounced speculative (by one of the globally-established rating agency). Fiscal adjustment was carried mainly on the revenues side, primarily by increasing the VAT rate and strengthening fiscal discipline, while the expenditure adjustment did not occur. In 2012, there were no major changes in monetary policy apart from small changes concerning banking regulation. Therefore, we are confident that maintaining the stability of the kuna exchange rate to euro will remain to be one of the main operative targets of the central bank in the future. As a result of negative trends in the real sector, unemployment continuously increased, while living standard decreased. The average annual inflation rate increased to 3.4 percent, contributing to the fall in real wages and purchasing power in 2012. One can hope that in 2013, especially with EU entry, the reform process will speed up, together with additional fiscal consolidation.
Despite such a harsh environment, the PBZ Group maintains a comfortable structural liquidity position, given its stable customer deposit base, appropriate sources of long-term funding and its shareholders' equity. Hence, the PBZ Group managed to achieve good results in 2012. We are truly proud of the strength and resiliency that have been proven in such circumstances. We have succeeded in meeting our goals and increasing the value of our bank. Total gross revenue for the PBZ Group amounted to HRK 5.5 billion. Consolidated net operating income equalled HRK 3.8 billion, whereas net profit recorded HRK 1,014 million. Our cost/income ratio, an efficiency key measure, closed once again below 50 percent, while the return on average equity reached 8.14 percent. These are all satisfactory figures consistently representing strong performance throughout the years.
In 2012, the PBZ Group further reinforced its position as one of Croatia's foremost banks in terms of productivity, returns and value creation for its shareholders. We are the second largest group in the country with a strong customer base. Looking ahead, the present economic climate suggests that the respective environment in 2013 will nevertheless remain challenging. Therefore, a continued focus by management on overseeing asset quality, maintaining sufficient liquidity as well as an active monitoring of operating costs will be crucial. We have the ability to overcome the near-term challenges. Furthermore, we are well positioned to earn benefits from the present and future trends in growing integration of the Croatian market into the global financial markets. Given our business model, strengthened by the alliance with Intesa Sanpaolo and the EBRD, these trends present a significant growth opportunity for us.

On behalf of the Supervisory Board, I would like to express my gratitude and appreciation to all the employees of the Group for their commitment and valued contribution. I would also like to thank the Management Board for its strong leadership and outstanding performance. Finally, I would like to express my great appreciation for the work to my former and new colleagues on the Supervisory Board, as well as to the Audit Committee members for their wise counsel and contribution.

Report on the performed supervision in the year 2012

In 2012 the Supervisory Board of the Bank performed duties in conformity with the law, the Bank's Articles of Association, and Rules of Procedure of the Supervisory Board of the Bank. During 2012 the Supervisory Board held four regular meetings and six meetings by letter in order to make decisions on the issues that had to be resolved without delay. In order to prepare the decisions that fall within its competence and supervise the implementation of the previously adopted decisions, the Supervisory Board of the Bank was provided with the assistance of the Executive Committee and Audit Committee, which regularly reported on their work at the meetings of the Supervisory Board.
In 2012, the Audit Committee held four meetings where it discussed the processes within its competence. In accordance with its legal responsibility, the Supervisory Board of the Bank has examined the Annual Financial Statements and Consolidated Annual Financial Statements of the Bank for 2012, Report on the Operation of the Bank and its Subsidiaries and Draft Decision on the Allocation of the Bank's Profit Earned in 2012, that were all submitted by the Management Board of the Bank. The Supervisory Board made no remarks on the submitted reports. In that respect, the Supervisory Board established that the Annual Financial Statements and Consolidated Annual Financial Statements were prepared in accordance with the balances recorded in the business books and that they impartially disclosed the assets and financial status of the Bank and the PBZ Group, which was also confirmed by the external auditor KPMG d.o.o., Zagreb, the company that had audited the financial statements for 2012. Since the Supervisory Board has given its consent regarding the Annual Financial Statements and Consolidated Annual Financial Statements of the Bank for 2012, the respective financial statements are considered to have been confirmed by the Management Board and by the Supervisory Board of Privredna banka Zagreb pursuant to the provisions of Art. 300.d of the Companies Act. The Supervisory Board of the Bank accepted the report of the Management Board on the operation of Privredna banka Zagreb and its subsidiaries and it agreed that HRK 844,048,262.40 of the Bank's net profit totalling HRK 845,559,206.81, earned in the year that ended on 31 December 2012, should be distributed by pay-out of dividends (or HRK 44.40 per share) whereas the remaining amount should be allocated to retained earnings.

Yours faithfully

26 March 2013
Dr. Gyorgy Suranyi

Gorski kotar

Management Board report of the Status of the Bank

Distinguished shareholders,
I am pleased to present you with the Annual Report and Financial Statements of Privredna banka Zagreb d.d. for the year ended on 31 December 2012.
In 2012 the international financial and economic crisis continued to dominate world macroeconomic developments. However, there were positive signs especially regarding the situation in the Eurozone where some tail risks decreased due to bold actions by policy makers, especially the European Central Bank. In Croatia, the situation was not favorable, but with the new Government in place, necessary reforms were sped up and we expect positive outcomes to materialize in the future. Nevertheless, the year 2012 was very challenging for Privredna banka d.d. Zagreb and its subsidiaries. Four years of stagnating or falling GDP has to have an impact on the real economy and, naturally, on the banking industry as a whole.
In spite of this, Privredna banka d.d. Zagreb and its subsidiaries, supported by our strategic partners Intesa Sanpaolo and European Bank for Reconstruction and Development, managed to perform better than many peers. In spite of a already mentioned unfavorable economic environment, we kept a steady course, also reflecting the resilience of our earnings power in challenging conditions and the strength of customer relations that we have continuously been building.

Consolidated financial results of the Bank
The consolidated net profits for 2012 amounted to HRK 1,014 million, representing a decrease of 20 percent compared to 2011. This good result was achieved despite the influence of negative elements: increase of non-performing portfolio resulting in an increase in loan provisions and stagnation of product placements resulting in a decrease in net interest income and net fee and commission income. We have still been benefiting from the strategic decisions that had been made prior to 2008, in which we anticipated the commencement of the macroeconomic crisis. These decisions enabled us to strengthen our capital base and secure stable liquidity sources thus, reducing our costs of funding and allowing us to adopt customer driven practices that resulted in an improvement of our products and services.
Therefore, our net interest income was reduced by 3 percent, mostly affected by a stronger decrease in average interest rates on the asset side than on the liability side. Net fee and commission income was reduced by less than 2 percent. It was influenced by sluggishness of product placements, resulting with a stagnation of fee and commission income, and accession of card operations costs, resulting in growth of fee and commission expense. Provisions and impairment losses increased by 60 percent due to deterioration of the loan portfolio and adopted conservative and realistic approach to provisions measurement.

As a reflection of such trends, the Group’s earnings per share shrank from HRK 66.7 in 2011 to HRK 53.4. The Group's return on average equity in 2012 was 8.14 percent, while return on average assets was 1.29 percent. Assets per employee equaled 17.4 million, whereas the cost to income ratio, according to the consolidated financial statements, remained significantly below the 50 percent threshold (43.6 percent).
The balance sheet of the PBZ Group slightly contracted by 2 percent, amounting to HRK 72.6 billion (in 2011 HRK 74.2 billion). The most significant portion of our assets are loans and advances to customers which experienced marginally higher reduction in outstanding amount than the overall assets due to lack of demand for loans caused by the challenging economic situation that affected our clients, both corporate and retail. We continue practicing a well-diversified loan portfolio policy, having similar volume of placements to retail customers on one side and placements to public and corporate clients on the other. Although non-performing loans rose by 11 percent all risks were promptly spotted and covered by sufficient provisions. As we are well aware that excellence in customer orientation can only be accomplished if one stands by its customers during troubled times, we continue developing comprehensive initiatives aimed at helping our customers during crises. From the liabilities perspective, our balance sheet is mainly funded by customer deposits with the retail segment playing the most significant role. In 2012, we experienced an increase in customer deposits that was related to increased activity of the retail segment even though it was partly offset by a decrease in corporate client deposits. Shareholders' equity increased by 3.8 percent to HRK 12.8 billion.
The Group's capital management policies and practices, among other tools, are based on an internal capital adequacy assessment process (ICAAP). In this process, the Group regularly identifies its risks and determines the amount of free available capital in stress scenarios. I am pleased to report that the PBZ Group is one of the leading, well capitalized banking groups in the country, with more than sufficient capital shield compared to internal capital requirement in a stress scenario.

Unconsolidated financial results of the Bank

The Bank's net result in 2012 was HRK 845.6 million, representing a decline of 25.6 percent compared to the preceding year. Defying the crisis grasp, net interest income was slightly reduced, by 2 percent, mostly affected by a humble decrease in average interest rates on the asset side, further affirming us to continue practicing our dedication to fulfillment of overall client requirements. This strategy was accompanied by efficient and omnipresent cost management enterprise carried within all organizational units enabling us to control the expense side of our business successfully. Hence, we were able to maintain our cost to income ratio significantly below 50 percent (i.e. 41.9 percent) threshold. Notwithstanding the success of our achievements, the crisis took its toll on net profit by increasing provisions and impairment losses by 71 percent compared to 2011. Such an increase is also the result of our prompt and orthodox approach to identifying all risks arising from our business ventures.
The overall Bank’s balance sheet ascent was by 1 percent, reaching a level of HRK 68.4 billion. Considering the total structure of the balance sheet, the customer deposits equal 68.7 percent. The total loan to deposit ratio of the Bank equals 99.9 percent emphasizing the stability and conservative nature of our ventures.

Briefly on the Bank's subsidiaries

After numerous years of successful business collaboration and affiliation with the PBZ Group, as of 30 November 2012, Međimurska banka was merged to Privredna banka Zagreb in such a way that all assets and liabilities of Međimurska banka were transferred to Privredna banka Zagreb. The merger endowed the existing and future clients of Međimurska banka with even wider range of products and services developed by Privredna banka Zagreb. During the whole process of the merger, the clients of Međimurska banka were continuously kept informed about the statutory changes and modifications in products' functionalities and services offered by Privredna banka Zagreb. The merger was carried out within the predefined timeframe and has been successfully completed.

In 2012, the PBZ Group members coped well with the crisis which resulted in positive financial outcomes. Therefore, Međimurska banka achieved a net profit of HRK 33.4 million (as of 30 November 2012), PBZ Card HRK 219.6 million, PBZ Leasing HRK 14.5 million, PBZ Stambena štedionica HRK 15.9 million, PBZ Invest HRK 5.7 million, whereas PBZ Croatia osiguranje, our jointly-owned pension fund management company, earned a profit of HRK 14.8 million. ISP Card, an associated company established in 2009, earned net profit of HRK 26.8 million.

Outlook

Forecasts are always very difficult and unreliable, but for 2013 we anticipate growth in Croatia to be around zero. We hope that expected modest growth in the second part of 2013 in our environment (especially in Eurozone), combined with investment plans of the Croatian Government and private businesses, will have a positive impact on our economy, and we look towards the second half of 2013 with more optimism, than we do at the first two quarters. This does not mean immediate return to "pre crisis" growth years. We should all adapt to "new normal" benchmarks meaning lower growth, but more fiscal discipline and speedier structural reforms. For Croatia, the expected EU full membership by mid-2013 should have an additional positive impact on our economy, however not a very strong one in the short-run.

Within this framework, we have defined our plans focusing on strengthening our position as fully client oriented providers of financial services. Responsible growth will continue to be our main strategic choice. Needless to say, we will continue to respect all regulatory changes, as well as following technological developments and changes in business environment in refining our strategy.

Conclusion

The PBZ Group is well-fitted not only to face up to challenges, but also to seize opportunities. We have a strong capital base, liquidity and funding positions, preparing us for potential market uncertainties and for tighter regulation. We are continuously transiting to a better balanced, more diversified and lower-risk business model.

In the end, I would like to take this opportunity to express gratefulness to all my colleagues and all employees of the PBZ Group for their dedication and true professionalism which enabled us safely to sail through these troubled times. Furthermore, I would like to thank all our acclaimed clients and business partners for putting their trust in our hands. Also, I would like to express my most sincere gratitude to all the members of the Supervisory Board for their encouragement in conducting our business affairs.

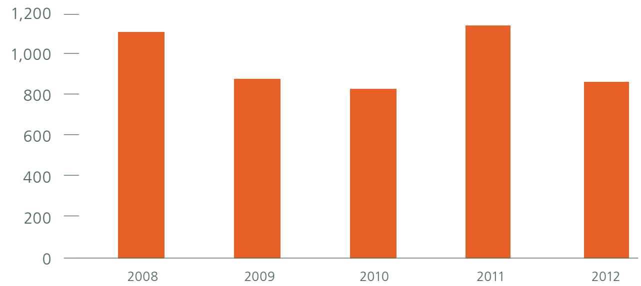
Božo Prka, M.S.
President of the Management Board

26 March 2013

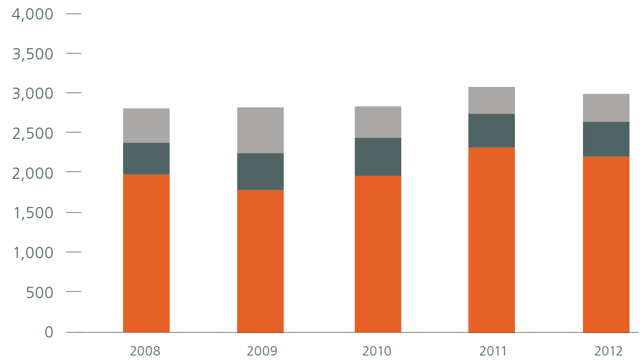
Marjan

Management Board report on the Status of the Bank's subsidiaries and financial highlights of the Group

Pursuant to the Capital Market Act, Article 407 and Rules of the Zagreb Stock Exchange approved by the Croatian Agency for Supervision of Financial Services, the Management Board states that best to its knowledge the Report of the Status of the Group and the Bank for 2012 represents a true view of operations, risks and financial results as well as financial positions of Privredna banka Zagreb and its subsidiaries.

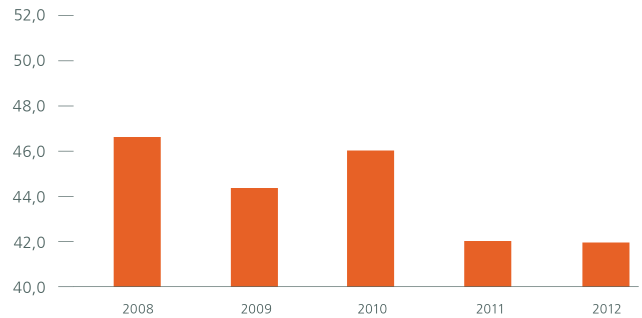


Net profit for the year - Bank
in HRK million



Net operating income - Bank
in HRK million

Other operating income
Net fee and commission income
Net interest income



Cost income ratio - Bank
in %

Cost income ratio

Privredna banka Zagreb

In 2012 Privredna banka Zagreb recorded excellent business results in the challenging environment. Below we provide an overview of these results together with results achieved by the Bank's subsidiaries.
We recorded profit before taxes of HRK 1,028 million, while net profit for the year of HRK 845.6 million represents a decrease of 25.6 percent compared to the previous year. The decrease in profit was primarily affected by increasing Provisions for loans by 71 percent compared to 2011, which is the result of macroeconomic developments in the country but it also demonstrates that the Bank is clearly focused on the additional protection of its loan portfolio.
The Bank realised gross revenue of HRK 4,489 million, which includes HRK 3,550 million of interest income, HRK 623 million of fees and commissions and HRK 316 million of other income. During 2012, the Bank managed to record net interest income of HRK 2,213 million representing a 2.4 percent decrease compared to the previous year.
Due to innovative offerings of non-interest related products and efficient business processes, net fee and commission income reached HRK 506 million which is slightly below 2011.
In spite the difficult market condition, PBZ's management strategy, combining good revenue drive and cost containment, enabled the Bank to record HRK 3,035 million in operating income, 3.5 percent below the year before. Moreover, PBZ in 2012 adequately managed the risks it is exposed to, in particular credit risk, which allows us to anticipate all essential changes in the portfolio and consequently make appropriate provisions for the coverage of losses. Throughout the year the Bank set aside HRK 603 million for impairments and loss provisions.
Other operating expenses amounted to HRK 1,280 million, slightly above 2011. Cost income ratio was 41.9 percent, significantly below the 50 percent threshold and stable.
For 2012, the Bank recorded 1.4 percent increase in total assets, which at year-end amounted to HRK 68 billion. Loans and advances to customers represent the most significant component of the financial position with 69 percent of the total balance. Other important items include loans and advances to banks which represent 9 percent of total assets, and balances with the CNB which represent 8 percent share of the total assets. At the year end, PBZ held HRK 10,115 million of cash and

cash equivalents, which indicates a robust liquidity position of the Bank.
Total liabilities amounted to HRK 57 billion at the end of 2012. Customer deposits represent the main source of funding, representing 69 percent of total liabilities, 6.6 percentage points above the year before, whereas interest-bearing borrowings represent 12 percent of total liabilities of the Bank. Total shareholders' equity at the end of 2012 stood at HRK 12 billion, 3.8 percent higher than in 2011.

PBZ Card
PBZ Card is the national leader in providing charge and credit card services to retail clients, small businesses and corporations, along with merchant services business, which includes signing merchants to accept cards. The company also continues to offer a full range of travel services, including airfares, hotels, cruises and full vacation packages. In recent years, the company has focused its efforts on increasing the use of cards for everyday spending and also continued its mission to achieve that cards are accepted even in industries where cash is the predominant form of payment. In addition, merchant satisfaction is a key goal of merchant services business. The company focuses on understanding and addressing factors that influence merchant satisfaction, including developing and executing innovative programmes that increase card usage; using technology resources and expanding the range of services that help them meet their business goals.
The company's results for 2012 have decreased compared to 2011 due to reduced consumer spending. PBZ Card core business maintained its high levels despite a challenging economic environment. Net operating margin for 2012 reached 426 million, 5 percent decrease compared to 2011. Main contributors to these results were fees charged to merchants, revenue earned from annual card membership fees and other fees.
Total operating costs reached 155 million, which is in line with the previous year. In addition to funding and operating costs, other major expense categories are related to marketing and reward programmes that add new card members and promote card member loyalty and spending. Net profit for the year amounted to HRK 220 million, which makes the company the second most profitable segment of the PBZ Group. Total assets in 2012 amounted to 2.2 billion, which represents a 6 percent increase compared to 2011.
The above presented results met the company's targets and PBZ Card will continue its business model which focuses on generating revenues primarily by stimulating higher turnover on various card brands and investing in greater value-added services for merchants and card members.

PBZ Leasing
PBZ Leasing is one of the leading Croatian companies engaged in lease transactions with clients.
The Company had a good year, especially considering the hard economic developments that have significantly influenced the Croatian leasing industry. Its net profit for the year amounted to HRK 14.5 million, which is a 11 percent decrease compared to the previous year. This result was mainly driven by a lower interest spread which was affected by higher financing costs and lower rental income from operating lease portfolio.
In 2012, the company realized new leasing placements in the amount of HRK 662 million which is the highest amount of new placements achieved in the Croatian leasing industry.
The total portfolio of the Company comprises assets in operating leases in the amount of HRK 435 million and receivables from finance leases in the amount of HRK 882 million at the end of 2012.
The business activities of PBZ Leasing in 2013 will be focused on ensuring balanced and steady growth of its balance sheet. PBZ Leasing is committed to maintain its market share and improve its range of products and services.

PBZ Nekretnine
PBZ Nekretnine in 2012 continues to be affected by the economic developments in Croatia, especially in the real estate market. Nevertheless, PBZ Nekretnine maintained its presence on the real estate market by realising more than 5.2 thousand appraisals, which is 13 percent less than in the year before.
During 2013, PBZ Nekretnine will continue to promote its activities with the aim of becoming the centre of excellence for real estate operations not only within the PBZ Group but in the whole country.

PBZ Invest

PBZ Invest is a well-recognised and highly respectable fund management company in Croatia.
PBZ Invest's net profit for the year reached HRK 5.7 million showing evidence of recovery, but well below the pre-crisis levels. Total amount of assets invested through investment funds under the Company's management reached HRK 2.44 billion. Furthermore, total number of clients increased by 7 percent, reaching 42 thousand clients.
Its development strategy for 2012 was oriented at maintaining its status within public investment in the country as well as attracting new investors. The outlook for 2013 still appears challenging and thus difficult to forecast precisely. However, the company expects to retain all funds currently under its management, maintain appropriate liquidity level and further exploit synergies within the PBZ Group. Finally, it is important to stress that PBZ Invest participates in the "Regional Hub" project of Intesa Sanpaolo aimed at international partnership of investment fund management companies within the ISP Group in the region. We expect this project to be completed during March 2013 when the company will join the Asset Management enterprise within the ISP Group.

PBZ Stambena štedionica

In 2012 net profit of PBZ Stambena štedionica reached HRK 15.9 million, which represents a HRK 6 million increase compared to the year before. Components that drove this increase in net profit include higher net interest income due to return deposits and repurchase agreements with PBZ d.d. and income made from release of provisions. By means of the PBZ's large branch network and through its own sales channels, PBZ Stambena štedionica reached more than 117 thousand clients at the end of 2012.
As at 31 December 2012, PBZ Stambena štedionica reached HRK 1,461 million in total assets.
The business activities of PBZ Stambena štedionica throughout 2013 will continue to be oriented at keeping those depositors whose savings contracts are about to expire and by attracting new clients. The company also expects a large number of present customers who meet the set criteria to take housing loans in 2013, in accordance with the terms of contract. Finally, the company will be focused on maintaining targeted profitability levels.

PBZ Croatia osiguranje

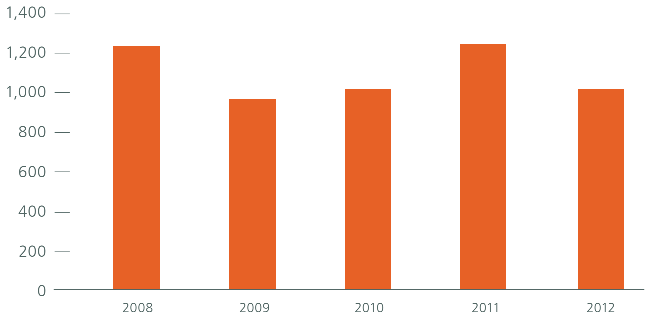
PBZ Croatia osiguranje continues to achieve positive financial results. In 2012, the company reached net profit of HRK 14.8 million, which is lower than the result in 2011 due to significant reduction of fee percentage for the management of the pension fund by the decision of the Regulator. At the same time, cost income ratio stands at 44.7 percent which is higher comparing to 2011 due to the above mentioned decrease of the management fee.
Total assets on 31 December 2012 reached HRK 160 million, which represents a 13 percent increase.
PBZ Croatia osiguranje increased the number of its fund members from 286 thousand in 2011 to nearly 295 thousand in 2012, which is an increase of 3 percent.
PBZ Croatia osiguranje is a well-recognised and highly respectable pension fund management company in Croatia. Its development strategy for 2013 will be oriented at maintaining its status within the general public in the country as well as attracting new members.

Intesa Sanpaolo Card Zagreb

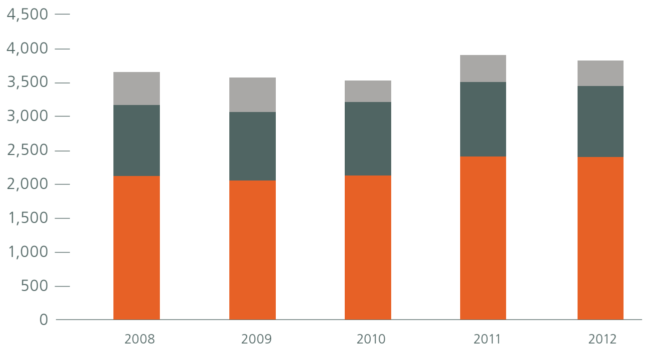
On a consolidated level, Intesa Sanpaolo Card Zagreb recorded profit before income taxes of HRK 33 million, while net profit for the year amounted to HRK 27 million.
Total assets on 31 December 2012 reached HRK 280 million.

Financial highlights of the PBZ Group

On a consolidated level Group recorded profit before income tax expense of HRK 1,272 million, while net profit for the year amounted to HRK 1,014 million which represents a decrease of 20 percent compared to the previous year.
By presenting more detailed figures, we may emphasise that in 2012 PBZ Group recorded interest income amounting to HRK 3,850 million, which compared to 2011 represents a decline of 2 percent. At the same time, the Group reported 11 million kuna lower interest expenses amounting to HRK 1,444 million, or 1 percent less compared to the year before. This is a result of efficient management of financing costs by anticipating the possibility of lower financing costs and timely refinancing of its obligations with the parent bank. Given the above, PBZ Group recorded net interest income of HRK 2,406 million, which is an annual drop of 3 percent.
As for the non-interest operating income, PBZ Group recorded net fee and commission income of HRK 1,090 million, which constitutes a 2 percent decrease compared to the figures in 2011.
The PBZ Group adequately manages the risks it is exposed to, in particular credit risk which allows it to anticipate all essential changes in its portfolio and consequently make appropriate provisions for the coverage of losses. Throughout the year the Group set aside HRK 589 million for impairment losses and provisions.
Other operating expenses of the PBZ Group have recorded a 0.2 percent decrease compared to last year's figures. During the last several years, the Group increased its efforts in efficient cost containment and rationalisation of business processes at all levels. The result of such activities has ensured an adequate operating expenses to operating income ratio, which stood at 43.6 percent in 2012.
At the end of the reporting period, the balance sheet of the PBZ Group amounted to HRK 73 billion. Loans and advances to customers account for 65 percent of the Group’s assets. At the end of 2012, loans and advances to customers stood at HRK 50 billion, which accounts for a decline of HRK 1 billion, or 3 percent compared to last year's figures. The share of the balance with the Croatian National Bank accounts for 8 percent of the Group’s total assets,

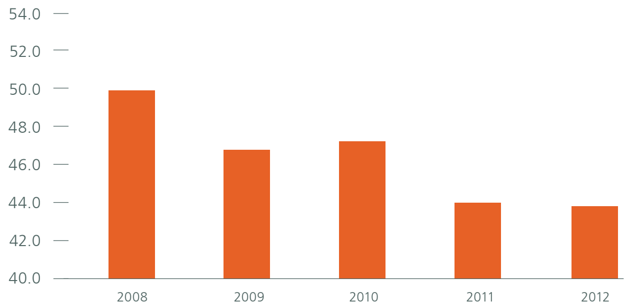


Net profit for the year - Group
in HRK million



Net operating income - Group
in HRK million

- Other operating income
- Net fee and commission income
- Net interest income



Cost income ratio - Group
in %

Group results by business segment (in HRK million)	2012	2011
Banking	3,155	3,269
Card services	626	637
Leasing	99	111
Other financial services	48	51
Non-financial services	9	8
Consolidation adjustments	(176)	(202)
Operating income	**3,761**	**3,874**

followed by loans and advances to banks with a share of 9 percent.
On the liabilities side, the total equity has recorded a growth of 4 percent reaching a total of HRK 13 billion. The deposits to customers of the PBZ Group account for 66 percent of the total liabilities and equity and are followed by shareholders' equity with a share of 18 percent and interest-bearing borrowings with a share of 12 percent.
Below we provide an overview of business segments of the PBZ Group presented per core lines of business of the Group members.
As apparent from the above table the banking segment continues to be the strongest contributor to the consolidated results.
It's operating income reached HRK 3,155 million. The major individual contribution to results of the Group was realised by Privredna banka Zagreb. Net profit of the Bank amounted to HRK 846 million (2011: HRK 1,136 million). Subsidiaries and associates contributed by HRK 304 million (2011: HRK 305 million) to the consolidated profit of the Group.

Božo Prka, M.S.

26 March 2013
President of the Management Board


Slunj

Review of the international and Croatian economy in 2012

From macroeconomic perspective, 2012 will not be remembered as a good year

Unfortunately, from the macroeconomic perspective, the year 2012 will not be remembered as a good one. The same as three years that preceded it. The fundamental reasons why 2012 is considered a bad year are as follows:

1. After stagnation of GDP in 2011, in 2012 the falling trend that started in Q1 2008 continued. Cumulatively, since the beginning of the crisis GDP fell by more than 10%. Other European countries did not escape the World economic crisis, but very few of them (Greece apart), had continuous negative trend since the beginning of the crisis. In 2012, the GDP decline (by 2.0%) was caused by fall in domestic demand, primarily personal consumption and investment. Were it not for relatively dynamic export sector, especially tourism, the fall would be even bigger.

2. After Parliamentary elections and formation of the new Government at the beginning of 2012, it was expected that necessary structural reforms will follow. Some reforms took place, but looking backwards, they were insufficient and slow. As a proof of that statement, Croatia, for the first time since getting sovereign rating in 1996, when it got investment grade, was rated as speculative grade (by one rating agency). Main reasons for this downgrade are fiscal.

3. In spite of the fact that consolidated general government deficit in 2012 fell to 4.7% of GDP, we cannot be complacent with that number. Adjustment happened on the revenues side, primarily by increasing VAT rate, increased fiscal discipline (which by itself is welcome, but increases effective tax burden in recession) while, according to general consensus expenditure adjustment did not happen. Furthermore, when compared with 2011 the deficit was lowered by only 0.7% of GDP, which is modest. Public debt is estimated at 53% of GPD, but what is worrisome is its rapid increase, so Croatia can soon be in a situation of public debt of more than 60% of GDP.

4. In 2012 there were no major changes in monetary policy. By mid-year new Governor and management of the Central bank were elected, but policy stayed more or less the same. There were small changes, especially concerning bank regulation. For example, in January reserve requirement rate was increased, but in May it was lowered to 13.5%. During the year the central bank intervened several times on the foreign exchange market by both buying and selling foreign exchange and as a result of that kuna depreciated only slightly towards the euro. All those fluctuations were within expected range from the last two decades. We are confident that maintaining the (relative) stability of the exchange rate of kuna towards euro will remain to be one of the main operative targets in the future, as this is the way to maintain price stability.

5. As a result of negative trends in the real sector, living standard of households decreased. This is not surprising if we take into account that unemployment is continuously increasing (if we take out seasonal decline during tourist seasons). Furthermore, real income has declined because of increased costs. Administratively controlled prices (especially energy prices like electric energy and gas), as well as food prices increase due to droughts, plus general increase of commodities prices on world markets were the main culprits. Average annual inflation rate increased to 3.4%, which is higher than long-term average. This has contributed to the fall in real wages and purchasing power in 2012. But in our view there is no risk of accelerating inflation as those pressures arise from the cost side, with very weak domestic demand. When we talk about unemployment, the negative fact is that its growth was generated by private sector only, while in the public sector number of employed slightly increased.

6. During 2012 international environment was very unfavorable, especially in the Euro area, which is our main trading partner. This has, undoubtedly, negatively impacted our macroeconomic results. The good news is that in the second half of 2012 risks of Euro area disintegrating have decreased significantly, so the market volatility has decreased as well.

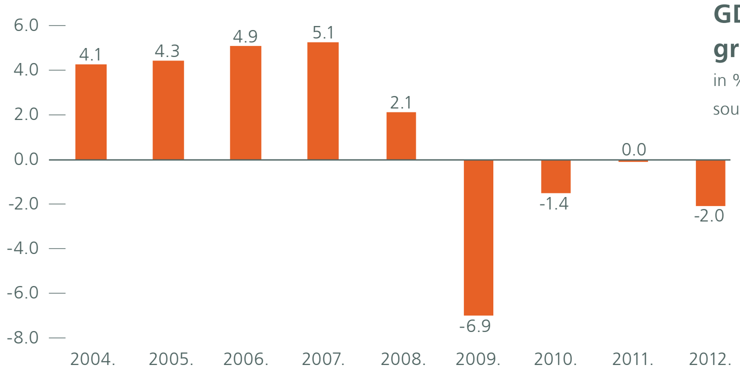
7. It is true that the Croatian Government did a certain number of reforms (e.g. decrease of the health contribution rate, some quasi-fiscal expenditures were decreased, fiscal discipline has increased, reforms in some public companies are initiated like Croatian Railroads, etc.) but for the time being overall reform activities can be judged as: moving in the right direction, but insufficient and relatively slow. One can hope that in 2013, especially with EU entry and after the local elections (in May 2013) reform process will speed up, together with additional fiscal consolidation.

8. Within such a framework, banking sector could not produce good results. Its outcome can be summarized in a few words: weak growth or decline in some banking aggregates and continuation of deterioration in quality of banking assets. The total banking assets and gross loans have decreased. The only item that grew were deposits and only households deposits, while those of companies dwindled. Of course, bad loans increased as well and their share in total loans increased to 13.8% by the end of 2012. As a consequences provisions increased and profits of banks (for those that did have positive results) fell. But, it is important to point out that the banking sector remains strongly capitalized (with capital adequacy ratio above 20%) and is an important factor of increased stability both of the financial and economic system.

9. Bank lending interest rates were on a small downward trend during 2012. Actually, one could have expected a more significant decrease, when having in mind relatively high indebtedness of households and corporate sector and their intention to deleverage. In other words, demand for loans was very weak. But increase in risk assessment and raise in bad loans (linked with increased provisioning), and relatively high costs of funding plus high regulatory costs did not allow for more decrease in lending rates. Weak demand for loans can be illustrated by high liquidity of the system during 2012. Therefore, interest rates on interbank market were very low during the whole year, with little volatility. As an illustration, interest rates on overnight loans oscillated around 1% (with minor exceptions), which means it was negative in real terms. Interest rates on Government securities on all maturities had a negative trend as well. At the last auction in December 2012, interest rate on 1Y T-bills was only 2.6%, which most probably will mean negative yield in real terms as we expect inflation above that level.

10. Beside all those numbers, we have to mention that the biggest structural problem of Croatian economy, high current account deficit, which before the crisis was almost double digit, fell to probably below 0.5% of GDP by the end of 2012. The adjustment happened via fall in imports. However, very high total external debt, which is more than 100% of GDP, remains to be a serious constraint to the existing growth model. It did not shrink considerably in 2012 owing to a great surge in external government borrowing. Nevertheless, high level of international reserves is a guarantor of stable exchange rate and regular servicing toward external creditors.

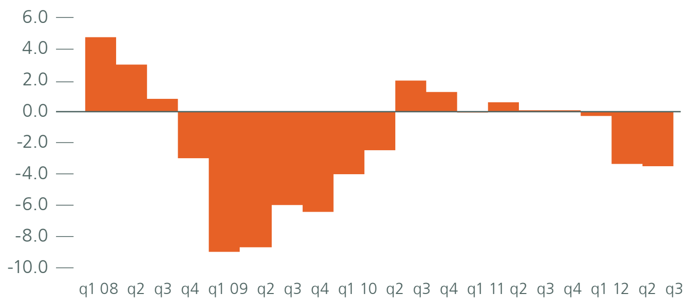
Accordingly, 2012 is a year that should be put behind as quickly as possible in the hope that the trend will change in 2013.



GDP, real growth rates

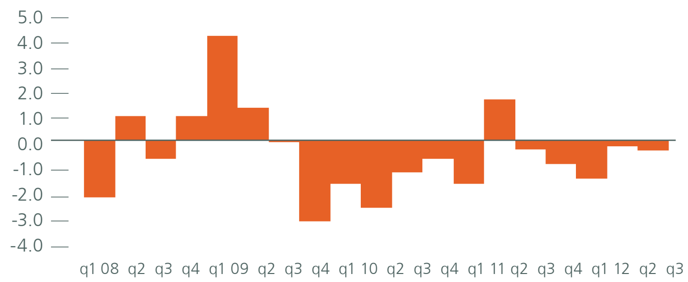
in %

source: CBS



Personal consumption, constant prices (2000 referent year), % yoy

source: CBS



Government consumption, constant prices (2000 referent year), % yoy

source: CBS

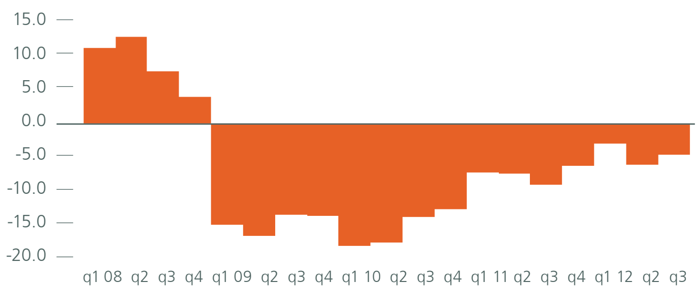
2012 – the return of recession

After the stagnating 2011, last year - 2012 – was marked by the return of recession and drop in GDP of 2.0% at an annual level. Contraction of domestic demand was so strong that even a relatively successful tourist season in third quarter (income growth by 2.9%) could not soften it.

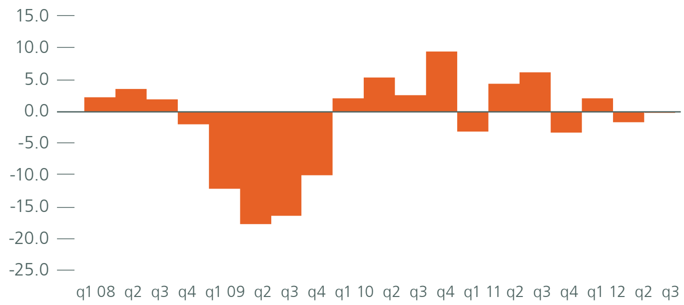
Negative rates of domestic demand during the entire year, followed primarily negative trends noted at the labour market, but also strong deleveraging of citizens and companies. During the entire 2012, personal consumption was greatly influenced by negative trends in the labour market and negative expectations of consumers in terms of future developments. All is said about the suppressed personal consumption if we look at data that show drop in retail trade by 4.2% in real terms during 2012, and the fact that retail trade is currently at 13% lower volume than in 2008.

At the same time, retaining the public spending at practically the same levels (about 41.5% of GDP) and stronger tax pressure led to drop in deficit, that at the level of consolidated general government amounted to 4.7% of GDP. Lack of fiscal consolidation i.e. cut in expenditures was penalised by rating agencies that lowered the credit rating at speculative or “junk” level.

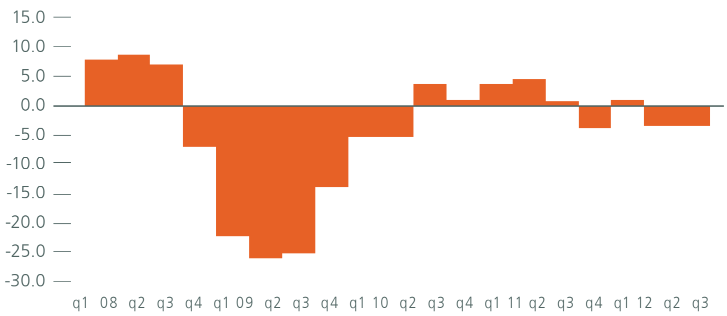
Negative expectations of consumers and companies did not change considerably during 2012, and it is no surprise that data show practically no investment activities. During 2012, the construction works marked an average drop of 11% in relation to 2011, while in relation to 2008, this drop amounts to a high 36%. Inactive real-estate market, a large number of built, but unsold apartments and deleveraging of citizens and lack of investments are only some of the burdens that put pressure on investment activities in the last couple of years.
Extremely low domestic and a slightly more dynamic foreign demand are basic determinants of trends in trade during 2012, similar to the year before. Partially due to base effect and growth slowdown in EU towards the end of year, as well as obvious lag in competitiveness, exports of goods and services in the first three quarters marked only a slight real growth of 0.2%. However, as imports continued to mark a decrease (-1.9% realistic), there was a marked positive impact of net foreign demand. In 2012, exports of goods were primarily determined by a nominal 30% lower exports of other transportation means (mostly shipbuilding), but also growth in imports of food, petroleum products, as well as machines and electrical equipment. If we exclude shipbuilding and oil derivatives, exports marked an increase of almost 5% at an annual level.



Gross fixed capital formation, constant prices (2000 referent year)
in %
source: CBS

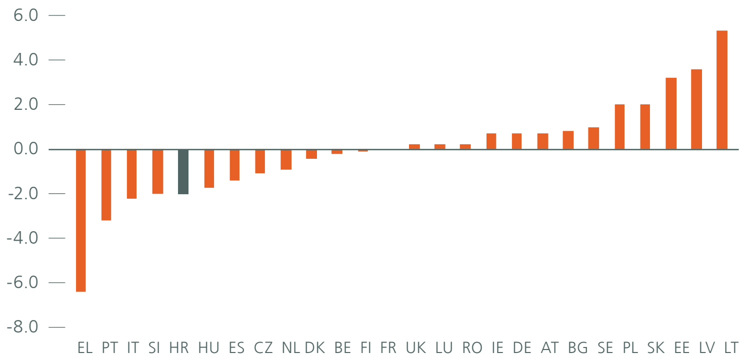


Exports of goods and services, constant prices (2000 referent year), % yoy
source: CBS



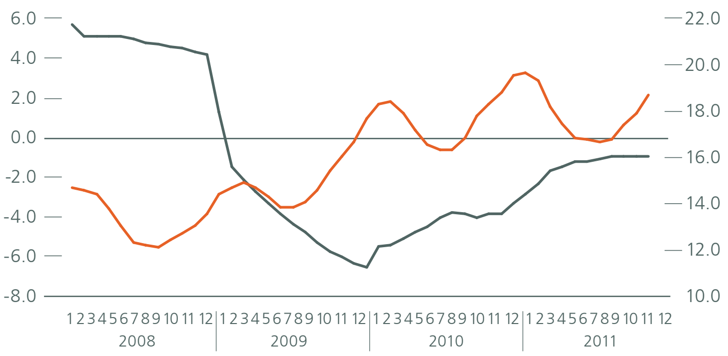
Imports of goods and services, constant prices (2000 referent year), % yoy

source: CBS



GDP, real rate of change 2012/2011

Source: Eurostat



Employment and registered unemployment rate, % yoy

source: CBS

Wages, real annual rate of change, % yoy

source: CBS, PBZ

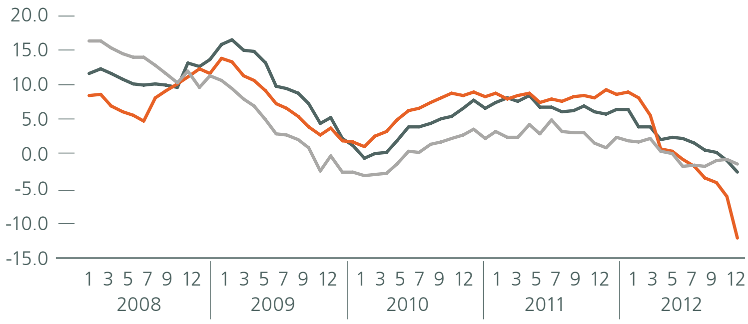
Unfortunately, negative trends grew stronger during 2012 and pushed Croatia to the bottom end of the European countries list according to realised economic growth, namely into the company of the so called peripheral countries. Reaching sustainable positive growth rates is almost impossible without structural reforms that would significantly improve the business climate in the country and strengthen competitiveness and production capacities.

The result of the above described trends in the real sector is depression at the labour market that recorded a drop in employment fourth year in a row (-2.5% on average) and the increase in unemployment rate (from average 17.9% in 2011 to 19.1%). Consequently, we mark a real drop in net salaries by 2.6% yoy. In this year, we expect the continuation of unfavourable trends in terms of high unemployment rates and repeated drop in average net salaries in real terms.

The increase of VAT by 2 p.p. (from 23% to 25%, since March), strong correction of the administratively regulated energy prices (electricity and gas for about 20%, since May), weaker kuna, the food prices (due to drought) and fuel prices increase at the domestic and world markets, led to stronger inflationary pressures in 2012. At the same time, the industrial producer prices on the domestic market marked an annual growth rate of 7%. Therefore, despite ongoing weak domestic demand, there was a jump in consumer prices and the average inflation rate reached 3.4%. In 2013, we expect strong pressures to continue, due to correction of VAT (replacement of zero with 5% rate), excises and possible further energy prices' increase, as well as potentially pronounced volatility of food and fuel prices at world markets.

Prices, average annual rate of change, in %

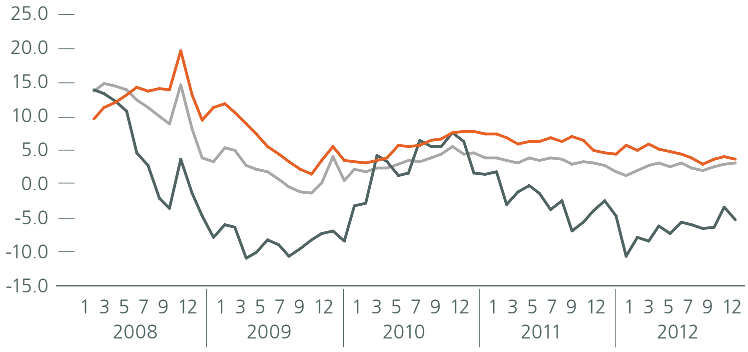
source: CBS



Loans, yoy % change

source: CNB

- Retail
- Total
- Companies



Deposits, yoy % change

source: CNB

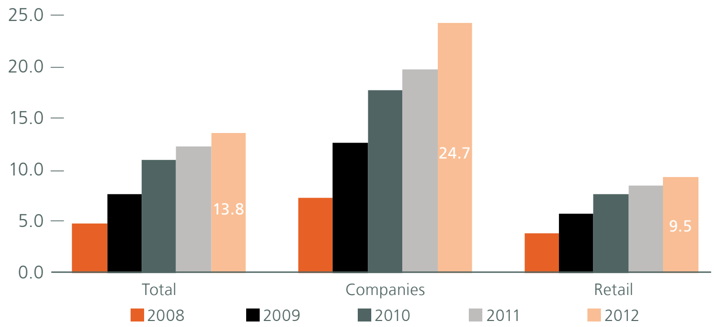
- Total
- Companies
- Retail

Severe fall of banks' profits

Slow increase, i.e. drop in banking aggregates and the continued trend of asset quality decline, were developments that marked the banking business in 2012. At the end of December, the consolidated banks' assets were 2% lower at annual level, gross loans were by 3% yoy lower, while deposits realised an annual increase by 3% yoy. The continued economy contraction led to decrease in demand for loans of both corporate and retail (-13, i.e. -2% yoy). At the same time loans to central government recorded an increase of 26%, that is for the major part the result of the shipyards' debt assumption by MoF in first part of last year. Moreover, the latter is also the reason for decrease in loans to corporate sector, beside the transfer of loans (HRK 5.6bn) by one domestic bank to an undertaking within the Group.
Total deposits in banks reached the increase of only 3% yoy, due to severe fall of company deposits (-5%) that indicate the continued deteriorated liquidity of the sector. Retail deposits posted annual increase of 4%, that is partially the result of the weaker kuna and accrued interest credited to the accounts, and for the minor part the result of inflow of new deposits into the system.

Same as in the previous year, the rates of changes in banking aggregates were partially influenced by exchange rates, considering that, at year end, kuna was by 1% yoy weaker to Swiss franc and stabile towards euro on annual level.
With projection of GDP in range from mild recovery to mild recession in 2013, we expect stagnation to slight decrease of loans and moderate increase of deposits.

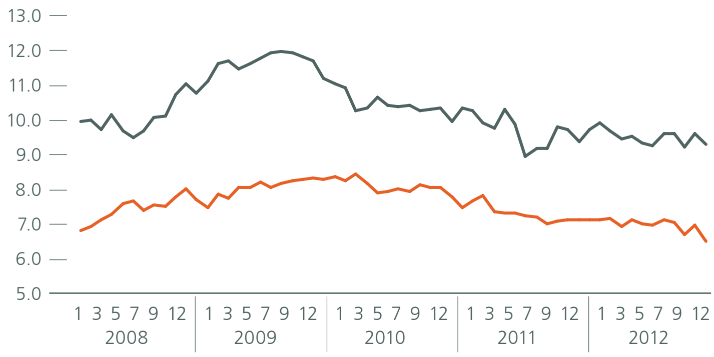
The strong recession trends and the depreciation of kuna led to increase in share of bad loans in overall loans from 12.4% at the end of 2011 to 13.8% at the end of 2012, when they reached 9.5% in retail and 24.7% in corporate. Weaker quality of loans portfolio resulted in the increase in provisions' costs that combined with increased interest expenses and stagnation of interest income led to decrease in net profit of the banking system by 27% at an annual level.



Share of NPLs in total loans

in %

source: CNB



Interest rates on loans, new business, monthly average, in %

source: CNB

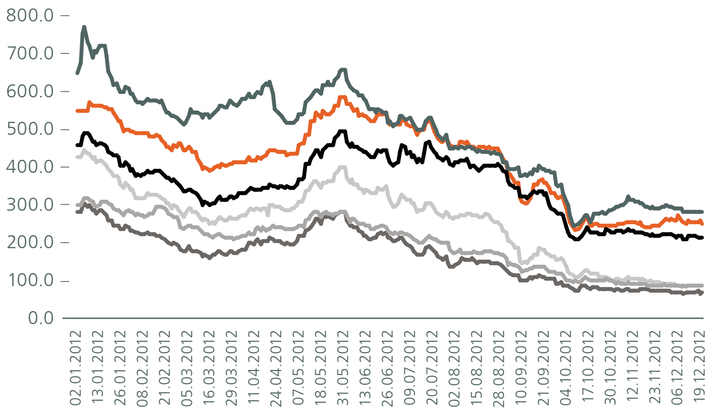
Lower, in some cases even historically the lowest reference interest rates and decline of CDS spread, as well as the weak demand, led to mild decrease of interest rates on loans despite of stagnation (on fx) or increase in deposit interest rates (on kuna, +18 b.p. at annual level) and the growing costs of banks. Interest rate at newly placed loans in 2012 on average amounted to 7.0% on loans with a currency clause (-32 b.p. year on year), i.e. 9.5% (-20 b.p.) on kuna loans. In climate of low demand and lower incomes of corporate and retail, interest rates on loans (especially corporate) did not, however, mark a significant drop due to several reasons as follows a) increase of bad loans in banks' balances increased aversion of banks towards risk, b) lack of a significant drop in costs of funds and c) regulatory costs. In that respect, mere membership in the EU shall not bring major changes, which could take place only when economic activity recovers and when domestic macro-economic imbalances are reduced (that shall decrease costs of funding and client risk), as well as in case of the regulatory changes.

Kuna depreciated

The increased demand of the corporate sector for foreign currency for repayment of foreign debt, combined with lower income from exports and foreign borrowing of government and private sector, resulted in increase of depreciation pressures on kuna in 2012. Average rate reached HRK 7.52 to the euro (2011: 7.43), and in 2013 we expect it will stand at current balanced level about 7.5 kuna to the euro.

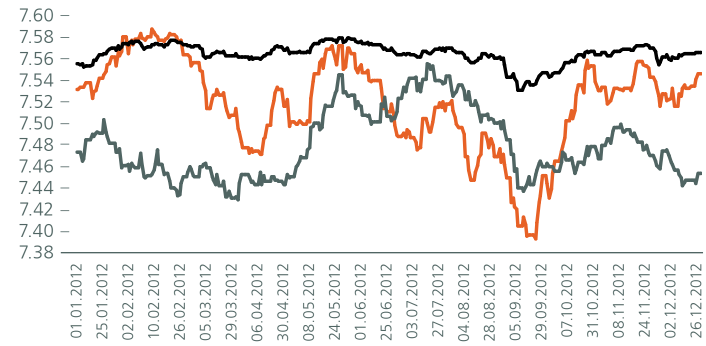
In 2012, kuna depreciated to dollar and Swiss franc (due to appreciation of dollar and franc to euro at world foreign currency markets) and the average exchange rate reached 5.85 kuna to dollar (2011: 5.34), i.e. 6.24 kuna to franc (2011: 6.04).

With the exception of occasional short disruptions at money market eased by regulatory changes and/ or foreign currency interventions, liquidity remains favourable for the most part of 2012, and the interest rates remain low. Thus, the average interest rate on overnight loans amounted to about 1%, as in the previous two years. The most significant regulatory changes took place in the first quarter when the currency pressures were the strongest and the central bank tried to defend the kuna exchange rate in the standard manner, by narrowing liquidity. Thus, in January reserve requirement rate increased from 14 to 15%, with the implementation of additional reserves calculation, and with that the first quarter saw three fx interventions. In May, the rate was decreased to 13.5% where it remained until year end.



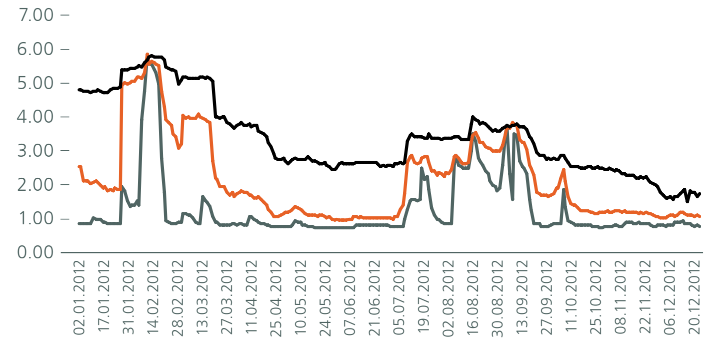
5Y CDS spread, basis points

source: BLOOMBERG



HRK middle exchange rate

source: CNB



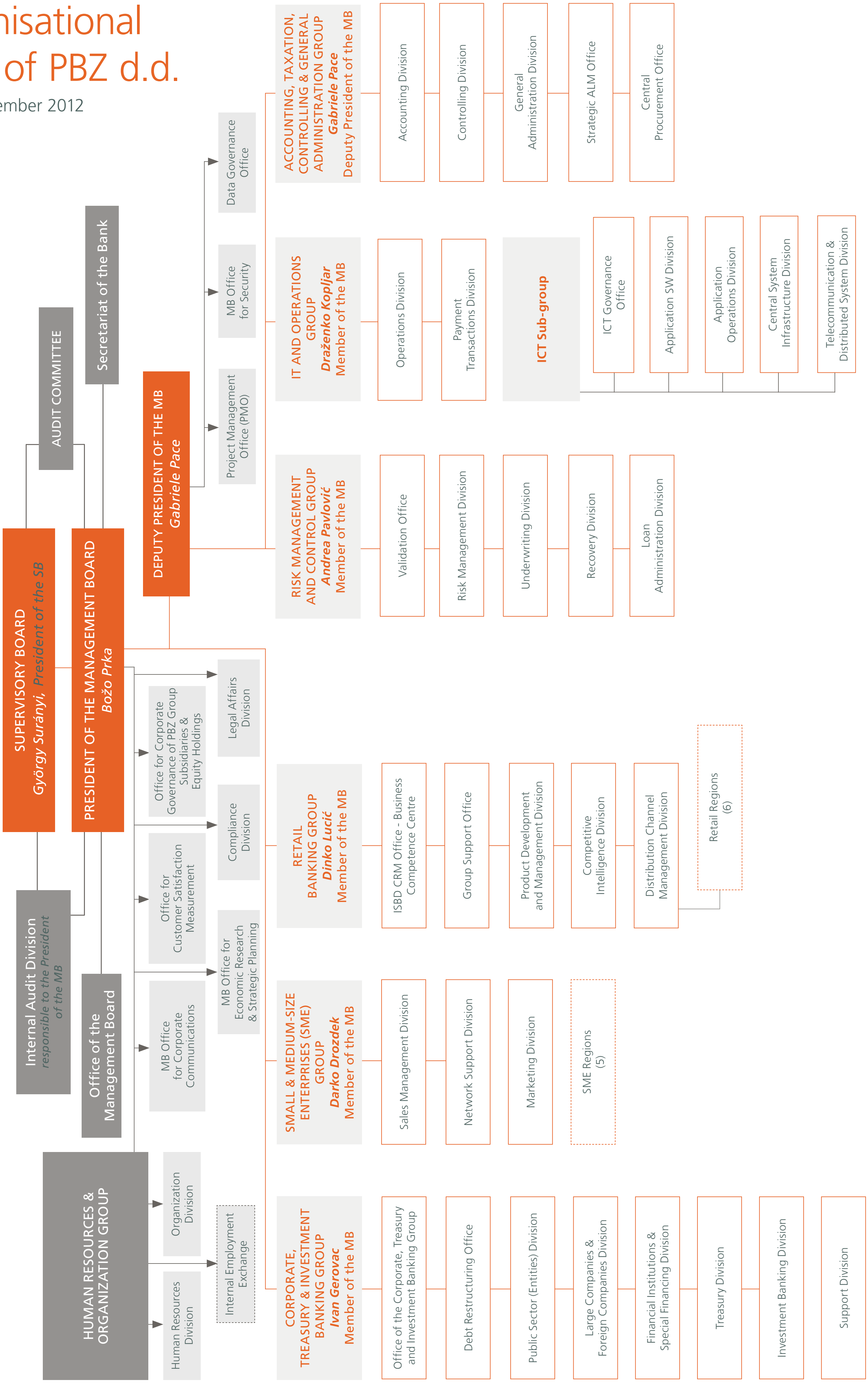
Zibor, %

source: REUTERS

Cavtat

Organisational chart of PBZ d.d.

as of 1 December 2012




Biokovo

Business description of the Bank

Privredna banka Zagreb (PBZ) was founded in 1966 and has consistently been a leading financial institution in the Croatian market, with an established business base and a highly recognized national brand name.
During all periods of its history, PBZ supported the largest investment programs in tourism, agriculture, industrialisation, shipbuilding, electrification and road construction. PBZ has become a synonym for economic vitality, continuity and the Croatian identity.
Privredna banka Zagreb today is a modern and dynamic financial institution, which has actively sought and won the role of market leader on the financial markets in Croatia. It is a fully licensed bank with nationwide branch network. With its nationwide network of branches and outlets, as well as a broad group of banking and non-banking subsidiaries, PBZ is one of the universal banks that cover the whole territory of the Republic of Croatia.

Organisational Structure and Business Activities

Nowadays, PBZ is the leading bank in Croatia in terms of subscribed share capital and the second bank in terms of total assets. It has consistently been a leading financial institution on the Croatian market with an established business base and recognised national brand name.
Upon successful privatisation in December 1999, PBZ became a member of Gruppo Intesa Sanpaolo – the largest Italian banking group and one of the most significant financial institutions in Europe. With this partnership, supported by the EBRD through its non-controlling shareholding stake, PBZ has retained its business strategy aimed at modern forms of banking and new products, confirming its image of a dynamic and modern European bank, which meets the demands of the market and its clients. The benefits of strategic partnership are clearly visible in the continuously improving financial results of the Bank, as well as of the PBZ Group.
Along with the adoption of the business and corporate governance standards set by its parent bank, Privredna banka Zagreb has maintained the strategic development orientation of a modern, client oriented, technically innovative universal financial institution. PBZ is focused on the continued advancement of its economic performance well into the future, as well as strengthening its position as a product leader in offering the most progressive banking products, through the optimal mix of traditional and modern distribution channels. This ensures that PBZ will continue to be able to set standards of the highest quality for product innovations and services offered to both its domestic and international clients. This commitment to quality and advanced banking practices is clearly seen by the fact that Privredna banka Zagreb received the Best Bank in Croatia award from Euromoney in 2001, 2002, 2004, 2005, 2007, 2008 and 2009. During 2006 PBZ received The Best Debt House in Croatia award by Euromoney. In 2012 PBZ won award for the Best Private Banking Service in Croatia. PBZ also received The Banker's Award for the Croatian Bank of the Year in 2005 and 2011. Additionally, PBZ's quality was confirmed by Global Finance's magazine in 2003, 2004, 2005, 2006, 2007, 2008, 2009, 2010 and 2011 when it received the Award for the Best Bank in Croatia, while in 2012 it was recognised as the Best Internet Bank in Croatia in the category Best Internet Banks in Croatia and Eastern Europe. In 2003, 2004, 2005 and in 2006 PBZ received the domestic prestige awards – the Golden Share Award for the Best Banking Share in the country, and the Golden Kuna Award in 2004, 2005 and 2010 for the previous year. Bank also received acknowledgement from Central European, Finance Central Europe, Adria Zeitung and others.
In addition, Privredna banka was listed among the world's top 500 financial brands for 2007 by Global 500 Financial Brands Index. This report, initially published in 2006, was the first publicly available table analysing the financial value of the world's leading banking brands.
Privredna banka Zagreb currently employs some 3,779 employees and provides a full range of specialized services in the areas of retail, corporate and investment banking services. The business activities of the Bank are organized into three principal client-oriented business groups.

Retail Banking Group

With respect to the retail banking segment, PBZ holds a comparative advantage over its competitors given its wide spread branch network in Croatia, consisting of more than 230 organisational units in 6 regions which cover the entire territory of the country.
In accordance with its business philosophy of focusing on client needs and demands, the Bank introduced the package of products (named Innovation) with which it rewards its clients who use several groups of products (up to 8), giving them a discount on certain forms of fees and awarding them an incentive interest rate, in addition to restructuring and repositioning the traditional distribution channels of the business network, PBZ also continues to develop and improve its direct banking distribution channels. It has extended the network of ATMs that accept Maestro, MasterCard, Visa and Visa Electron as well as American Express cards (a total of 670 ATMs have been installed). The number of EFT POS's (point of sale) has exceeded 28,000.
As a leader in modern technologies, PBZ has also expanded its distribution channels and products by applying the most advanced technology in order to implement its PBZ 365 services: the PBZ365TEL telephone banking service and the PBZ365SMS service. With Internet Banking - PBZ365NET and PBZ365WAP services - clients can access their accounts 24 hours a day, seven days a week, from any location in the world with Internet access. Four years ago PBZ introduced mPay - a system of payment through mobile phones, as the first bank in Croatia offering such a service. Last year PBZ introduced mPBZ, a full range of banking services over the mobile phone, such as paying bills, checking account balances, forex, etc. These achievements have firmly established PBZ as the Croatian market

leader in electronic banking, as well as the technological leader on Croatia's financial market. PBZ is the first bank in Croatia to implement secure e-commerce based on 3D Secure technology (Verified by Visa) and CAP/DPA technology for user authentication. Most recently, PBZ introduced a new innovative service – an Internet channel for distribution of investment banking services, now brokerage services on the domestic stock exchange and as well as custody accounts. In the area of retail product development, PBZ is constantly modifying and supplementing its wide range of products and services. Thus it has introduced several types of new loans on the basis of credit scoring - besides consumer and cash loans for PBZ American Express card holders, the Bank launched several very successful tranches of "quick loans" over the past years. Recently, new tranches of innovative loan products were introduced and placed through sophisticated direct marketing campaigns.

Overall in the period from 2000 until mid 2010, PBZ established itself as the market leader in retail loans with nearly a 20% share in the loan market on the Group level. In the area of savings, the PBZ Group has significantly increased its deposits, to HRK 32.4 billion to date, keeping 20.74% of all retail deposits in Croatia.

Retail operations in Privredna banka Zagreb comprise the following divisions: ISBD CRM Office – Business Competence Centre, Office for Group Support, Distribution Channel Management Division, Product Development Division, Competitive Intelligence Division, Analysis and Client Relationship Development Division and 6 Retail Regions.

Distribution Channel Management Division

This Division is responsible for defining, structuring, implementing and monitoring different distribution channels of the Bank for the delivery of retail products and services (the branch network, ATM network, PBZ 365 services - Internet banking, telephone banking, SMS banking, WAP banking, mPay). It prepares and co-ordinates a budget and staff education, and supervises the realization of all its goals for all distribution channels. The Division takes special care of the segment for affluent banking and the segment for regular banking, as well as private banking, which includes developing, improving, monitoring and controlling these three segments, setting up and improving business processes, organizing training courses for personal bankers, and following and reviewing market trends. Other very important tasks are negotiations and co-operation with corporate clients (favourable loans conditions for bank clients) and firms (the bank prepares special proposals for a firm's employees), development and improvement of utility business, training, co-ordination and budgeting of financial advisors.

It chooses the appropriate distribution channels for finished products intended for a specific targeted client group. In coordination with the Division for Product Development and the Competitive Intelligence Division it chooses the right moment for the launch of a new product/service and is responsible for informing Distribution Channels of all pursuant marketing activities which will have an effect on them.

Product Development and Management Division

This Division is responsible for developing products and services for clients of the Bank in the field of retail operations and monitoring their implementation in sales. It sets guidelines for developing products based on clients' needs and determined goals of the Bank and carries out a permanent analysis and monitoring of client demands as well as competitive deposit and credit products. Drawing on conducted analyses, it develops and implements new products and modifies existing products, and it also ensures the technological support of deposit and credit products.

Its area of activity also includes cooperation with other members of the PBZ Group (PBZ Card, PBZ Invest and PBZ Stambena štedionica) in the field of developing deposit and credit products, as well as cooperation with strategic partners in the field of bank insurance.

Competitive Intelligence Division

The activities of this division include the selection and co-ordination of appropriate communication and marketing campaigns and development of ideas for promotion and sales for the Bank's retail and SME products and services. It defines, organizes and implements marketing campaigns, (direct marketing, promotion, advertising), in cooperation with the Bank's Marketing Agency. This Division is also responsible for the selection of the most suitable communication channels for a defined market segment, and media planning, in cooperation with the Bank's Media Agency. It prepares proposals for the marketing budget and tracks it throughout the year. It continuously monitors the Bank's and competing bank's new and existing products and services and competing bank's communication and marketing campaigns.

Analysis and Client Relationship Development Division

This Division is responsible for analysing and developing models of supervision and implementation of measurement of key indicators used for assessment of the distribution network and retail products. Activities related to the analysis and client relationship development entail monitoring the profitability of segmented client data bases, analysing existing products and services intended for certain client segments and their requirements, developing models of measurement of client service quality through Mystery shopping, structured market research, monitoring clients' complaints and general level of our clients' satisfaction to predict various events in client relations with the Bank, the development of support for better relationship management with clients and calculation of key indicators of success in managing relations between the client and the Bank.

This Division expands its activities to other members of PBZ Group with the purpose of analysing and developing CRM activities related to the clients of Group members and other organisational parts.

Corporate, Treasury and Investment Banking Group

Privredna banka Zagreb d.d. is one of the leading Croatian banks when it comes to corporate banking. With a wide range of products and services offered to its corporate clients, both locally and internationally, it is hard to find a major company in Croatia today that does not bank with Privredna banka Zagreb d.d.. Supported by powerful electronic distribution channels, our network of well-organised branches is the key driving force in serving our clients effectively. We strive to create additional value by providing integrated financial solutions to meet the individual requirements of our clients.

PBZ has thoroughly developed a platform for supporting classic cash and non-cash transactions for corporate clients within the Bank's network. Due to it's wide network of correspondent banks, Privredna banka Zagreb d.d. offers it's clients fast and affordable services in the area of international payments. Also, PBZ has significantly changed the process of handling domestic payments. The Bank directly participates in the Croatian RTGS system (HSVP) and in the national clearing system (NKS) and thus has the ability to process any payment through the most appropriate channel. Improved with the new functionality, Internet banking for corporate clients – PBZ COM@NET service – is available for both domestic and international payments.

In terms of finance banking, Privredna banka Zagreb d.d. is a dominant participant on the Croatian market. PBZ has originated many contemporary products and has largely initiated the development of the financial market in the country. Consequently, PBZ, with its active role in the foreign exchange market, money market and primary and secondary capital market, has earned the title of market leader. We are determined to be recognized as the best financial services institution in the region. We have achieved this recognition from our clients through our ability to deliver the best quality in everything we do.

Following the adoption of the new organisation of Privredna banka Zagreb d.d., the Corporate Banking Group and the Finance Banking Group created the Corporate, Treasury and Investment Banking Group with particular emphasis on banking with large companies, financial institutions and the Government institutions and agencies.

Corporate, Treasury and Investment Banking Group consist of the following divisions: Office of the Corporate, Treasury and Investment Banking Group, Public Sector (Entities) Division, Large Companies and Foreign Companies Division, Financial Institutions and Special Financing Division, Treasury Division, Investment Banking Division and Support Division.

Public Sector (Entities) Division

Public Sector (Entities) Division is responsible for managing the entire business relationship with the central state and state-owned companies. The Sector is also responsible for running and monitoring the entire business relationship with major private enterprises whose business relationship with the Bank is exceptionally complex and structured, which implies the multiple interweaving of the products and services they use.

Recognising and taking into account the requirements of its clients for banking products and services, the Division offers all types and forms of short-term and long-term financing, purchase of receivables, B/E discounting, factoring, letters of guarantees, letters of credit, and renders services involving the opening of business accounts, cash pooling, contracting Internet banking, multi-purpose facilities, providing financial support to export businesses, active participation in the conclusion of deals of its clients abroad, as well as different models of deposit transactions and other innovative solutions adjusted to the requirements of each single client. Apart from the operations mentioned, it is also important to highlight the services in agency business – transactions performed on behalf and for the account of the ordering party, and commission business – deals made in its own name and for the account of the ordering party.

We particularly wish to bring into focus our financial advising services, applicable to whatever line of business/branch a legal entity is associated with, and the creation of the best possible solution for the respective entity.

In coordination with other units of the Bank, we participate in cross selling of all the PBZ Group products. By managing the overall business relationship between the Bank and the client, through a synergic effect we strive for the creation of new supplementary value for our clients.

Appreciating the diversity of its clients' business activities, employees of the Public Sector (Entities) Division, through their individual approach to each client, as well as in team work, provide support to clients in all aspects of their business activities by affording them the use of a wide range of the Bank's services and products, thus developing long-term business relations and partnerships.

In every segment of its business activities, operations and service rendering, the Division endeavours to promote the highest quality banking standards, first and foremost in being professionally and flexibly oriented, both to its present, and to its potential clients.

Large Companies and Foreign Companies Division

The Large Companies and Foreign Companies Division are responsible for business transactions with large domestic companies, companies in foreign ownership, as well as with foreign legal entities – non-residents. The Division offers all types of banking products and services rendered in cooperation with other Bank's organisation units – opening business accounts, offering Internet banking accounts, approving loan facilities, purchase of receivables, B/E discounting, issuing of letters of guarantees and opening of letters of credit, cash handling services (organising, transporting, collecting and transferring cash, cash pooling, global cash management), card operations, leasing, retail products and many other.

Major domestic clients are developing companies (building construction and civil engineering), companies engaged in tourism, companies engaged in the pharmaceutical industry, companies engaged in food

production, and large trading companies. To companies engaged in the construction of residential and business premises intended for sale we offer complete project implementation service – from the control of project documentation and building supervision to the financing of construction and sale of real estate to final buyers.
In view of the well-developed business network of Privredna banka Zagreb d.d., with as many as 204 branches and branch offices, we have successfully organised the complete conduct and management of cash transactions for some of our clients, who are also some of the largest chain stores, and companies engaged in tourism.
The International Desk forms part of the Division, and is in charge of performing transactions with domestic companies in foreign ownership and of coordinating activities of Privredna banka Zagreb d.d. and it's parent bank – Intesa Sanpaolo. All banking and advisory services are provided by the International Desk to Intesa Sanpaolo Group clients present on the Croatian market, as well as to other companies in foreign ownership. Apart from conducting business relations, this unit also assists foreign investors in the process of starting up a new company in Croatia, provides advisory services and general information on business terms and conditions in Croatia, contacts clients and puts them in touch with institutions exigent in the performance of regular business activities.
The non resident department is responsible for establishing and developing co-operation with foreign entities (foreign companies and private individuals engaged in business activities, foreign diplomatic and consular representative offices and representative offices of foreign legal entities, foreign associations, foundations and other non-profit organisations, international missions). Co-operation includes opening and managing of accounts, depositing funds, providing the clients with all necessary information required for conducting business in Croatia, which requires the constant monitoring of all national currency regulations (close co-operation with the CNB and Ministry of Finance-Foreign Exchange Inspectorate in money laundry prevention issues).

Financial Institutions and Special Financing Division

The key responsibilities of this Division are establishing, monitoring and promoting a complete range of business relations between the Bank and more than 1,800 domestic and international banks and financial institutions. In order to provide better services to PBZ clients and fully utilize its internal synergies, the Documentary Business (i.e. Guarantees and Documentary Credits) became part of the Financial Institutions and Special Financing Division in 2006.
As part of the special financing services, this Division offers all the Bank's clients tailor made financing solutions including trade and project financing, credit and special arrangements with financial institutions (both domestic and international) as well as with supranational organizations (e.g. EBRD, etc.), buyer's credits for the promotion of Croatian exports, open lines of credit guaranteed by state export agencies, commodity loans for export and import financing. One of the most notable financial services provided by this Division has been arranging and participating in syndicated loan facilities on behalf of the Bank and its clients (PBZ is the market leader in Croatia in arranging syndicated loans). Through this Division PBZ is an active participant in the secondary loan market and forfeiting transactions.
The PBZ's Group funding has also been a part of this Division's responsibilities.

Treasury Division

The Treasury Division is an important, and among the top players on the Croatian market with a broad spectrum of financial solutions for large corporate and institutional investors. The Treasury Division offers a comprehensive range of services, involving transactions on the international and domestic money markets, capital markets, and foreign currency markets and also manages the liquidity of the Bank. The PBZ Treasury Division is a reliable financial partner and has an active role in trading securities issued by the Ministry of Finance, currency and short-term cash derivatives on the money market.
The Treasury Division consists of three sections: Trading, Sales and Money Market. Trading Department consists of two subunits: securities and foreign exchange. The securities subunit operates with short, medium and long-term debt and owners' financial instruments. The foreign exchange subunit performs transactions with foreign currencies on spot and forward, with options and banknotes. The banknotes segment covers delivering, dispatching, processing and warehousing various shipments of foreign currencies. Privredna banka Zagreb acts on the domestic market as one of the leading banks in this particular banking area.
The money market section is involved in short-term securities, domestic and international T-bills, repo arrangements and deposits. In the foreign exchange section the most important segment of the activities is covered by the Corporate desk. It is mainly oriented towards corporate clients and fulfilling their needs, requirements and demands. It offers best quotations of all treasury products, plus information about exchange rates, interest rates and bond prices.
We are recognised as the market maker in securities, commercial papers, government, municipal and corporate bonds issued on domestic and foreign markets. Considering the above, we can most proudly conclude that as well as participating domestically, as a priority we are focused and open towards the global markets.

Investment Banking Division

As a leader in the Croatian investment banking industry, the Bank's Investment Banking Division provides institutional and private clients with a wide spectrum of investment banking products and services through capital market activities, financial advisory and structured finance services, research, as well as brokerage and custody services. In cooperation with Intesa Sanpaolo and its affiliates in Hungary (CIB), Slovakia (VUB), Bosnia & Herzegovina (ISP BiH) and Serbia (Banca Intesa Beograd), services to our clients are extended across South Eastern Europe.
With an outstanding reputation for innovative financial solutions, the Bank has

been consistently recognized as the leading Arranger of debt issues in the Republic of Croatia. The Bank has specialized origination, syndication and sales desks that deal with different type of debt or equity issues. Over the past decade, we have been second to none player in the field of IPO, sovereign, municipal or corporate bond issues, or commercial papers issues on domestic market both in terms of issued amounts, but also in terms of number of companies that have chosen us as their Issue Agent.
Structured finance department performs activities related to structured transactions, such as: designing and executing structured finance transactions, providing support to its clients during creation of optimal financial structure of a project, preparing financial projections of planned projects, identifying risks within the structured transactions and suggesting measures to mitigate those risks, participating in organisation and management of due diligence processes in order to prepare and execute structured transactions and participating in organisation and management of gathering financial sources needed for structured transactions.
PBZ's financial advisory services team provides advisory services related to capital structure, business strategies and mergers and acquisitions transactions. Our primary goal is to help our clients in various corporate activities aimed at creating added value and positioning our clients ahead of their competitors. Main areas of our expertise include advising on creating and executing corporate activities, such as: mergers and acquisitions, divestments, privatisations, employee share ownership programs (ESOP), MBO/LBO transactions, takeover defence, valuation exercises / fairness opinions, business strategies, financial restructuring.
The Research department closely cooperates with other departments of the Investment banking division and provides a wide spectrum of services connected to preparation and execution of various M&A (including buy-side and sell-side deals, privatisations, mergers, acquisitions, LBOs, MBOs etc.), capital markets transactions (issue of debt and equity securities), project finance etc.

In addition to the purchase and sale of securities on domestic and foreign stock exchanges, the Bank's brokerage services consist of providing detailed information on trading activities, supply and demand readily available through electronic trading systems and prompt reporting of securities transactions.
Privredna banka Zagreb d.d. is the leading Croatian custody banks offering high quality custody services for investment in domestic and foreign securities. In-dept market knowledge and expertise of our team as well as exellence in quality and services is why global custodians, other financial institutions and corporations turn to Privredna banka Zagreb d.d. Global Custodian survey of the clients of the agent banks in emerging markets gives Privredna banka Zagreb d.d. the highest accolade a provider can win in the survey – a top rated status from the Leading Clients.
Our dedicated staff in the Investment Banking Division, focused know-how and experience, combined with the ability to access local and regional markets effectively, provides our clients with top quality products and services and the assurance required in successfully accomplishing all their business goals.

Debt restructuring office

The Debt Restructuring Office is a newly established organizational unit in charge of providing support to Corporate and SME sales force in problem loan management, offering strategies of portfolio restructuring and monitor their execution

Support Division

This division offers full business support to all organisational units of the Corporate, Treasury and Investment Banking Group. In order to improve communication and relations with clients, the Support Division has established an Information Centre where clients can obtain all relevant information pertaining to the products and services of the Corporate, Treasury and Investment Banking Group.

Small and Medium-size Enterprises (SME) Group

Privredna Banka Zagreb, as one of the leading corporate banks, established the SME Group in 2006, with a clear focus on small & medium-size enterprises. The SME Group, with more than 250 employees, has been committed to developing new and improving existing products, implementing state-of-the-art technologies and IT applications, optimising processes and organisation in order to provide a more efficient service to more than 80 thousand customers - trades, crafts and businesses.
The SME Group has a nation wide network of 5 Regions, 14 Business/ SME Banking Centres and 60 SME Desks branded under the label "PBZ SINERGIJA" which is intended to develop a strong connection and communication with our customers.
Customers can use the largest network of ATMs (Cash-In/Cash-Out), night safes, EFT POS terminals and counters (branch offices for payments). In addition, the use of 2D barcodes (utility bills payment), mobile banking and text message services have turned us into one of the leading providers of payment services.
PBZ is a technological leader and has a pioneering role in terms of introducing the Internet banking services to the domestic market, which are currently available under labels PBZ COM@NET and PBZ@365 (for trades and crafts). An increasing number of users as well as more frequent use of direct distribution channels are the best indicators of our adequate strategy and quality of services. The use of VISA Electron debit cards linked to business accounts, a wide range of American Express business cards, and the largest network of EFT POS terminals are available with the support of PBZ CARD (subsidiary). Also, there is a special PBZ AGRO card that has been introduced to support financing of agricultural production. In cooperation with the Croatian Bank for Reconstruction and Development, EU development institutions, local self-government units and ministries of the

Republic of Croatia, the Group offers the most extensive range of (long-term) development credit lines in the Croatian market, intended to finance production, energy export and other development projects. We particularly emphasise the quality of cooperation and products available through EU pre accession funds (PHARE, ISPA, SAPARD, CARDS, TEMPUS, LIFE, INTERREG III, IPA MED). Our so-called International Desk provides a broad range of services designed to assist international companies that have decided to set up or improve their business in Croatia.
Since October 2010, we have introduced new scoring systems for micro-enterprises and trades, simultaneously optimising the related process (allowing faster decision-making), which is a significant step forward in terms of lending to this segment of clients in the Croatian market. The Group is centrally supported and managed by the Marketing Division, Sales Management Division and Network Support Division. The Factoring Department, as an integral part of the SME Group, provides the highest level of service in domestic and export factoring, as well as other transactions concerning the purchase of receivables available in the SME Group network. As far as social responsibility in the SME area is concerned, our goal lies primarily in the guidance, development, improving business quality and education of entrepreneurs in Croatia, as well as continuous (day-to-day) involvement in successful growth of this market segment.
The SME Group consists of Sales Management Division, Network Support Division, Marketing Division and 5 SME Regions.

Sales Management Division

The key responsibilities of this Division are business monitoring on a regional and segment level, sale support, initiating the development of new products and services, improving business processes and sale promotion of various products. Additionally, within this Division is the Factoring Department whose role is organising and sale of factoring products.

Network Support Division

This Division is responsible for providing administrative support to the SME network, development and maintenance of business applications and processes, support in development of new products and services developed with other SME Divisions and assisting SME customers in using products and services of the Bank. With the aim of running these operations adequately the Division is supported by the following Departments: Product Development Department and Customers Contact Service.

Marketing Division

The role of the Marketing Division is to establish an integrated management of business relationships with SME clients by supporting SME development processes within the SME domain. Division is responsible for monitoring of revenues, expenses and profitability of certain business units, budgeting and calculating key profitability indicators. Also, within it's domain are Customer Relationship Management, campaign management and all SME communication with customers.

SME - Region

The SME Group is also present in the Bank's network. Its presence is grouped in 5 regional centres including: Zagreb, Central Croatia, Dalmatia, Istra-Rijeka-Lika and Slavonia. Activities and responsibilities of SME Region centres include offering and sales of Bank's products to clients, consulting SME clients in matters of financing and cooperation with other Divisions of the Bank and subsidiaries. We also provide financing, guarantees, letters of credit, bills, factoring, deposit collection and payment services and other services.

Logistics areas

Business areas focusing on client requirements can only fully exploit their potential if they are provided with a reliable and efficient infrastructure.
The Accounting, Taxation, Controlling and General Administration Group led by the Deputy President of the Management Board, provide skilful and in-depth support with regard to all financial monitoring and reporting matters, financial planning and budgeting as well as administrative assistance to the business groups.
The IT and Operations Group represents a key part of the organisation that serves the entire Bank by providing IT and communications assistance, supporting distribution channels and feeding the system with financial information.
Risk management and control is a crucial part of our commitment to providing consistent, high-quality returns for our shareholders. It is our belief that delivery of superior shareholder returns greatly depends on achieving the appropriate balance between risk and return. In this context, we established the Risk Management and Control Group to protect the Bank from the risk of severe loss as a result of unlikely events arising from any of the material risks we face and to limit the scope of materially adverse implications to shareholder returns. Within the same Group there is a Recovery Division established with the goal of helping clients, who are unable to meet their financial obligations, to accomplish economic recovery through restructuring.
The Internal Audit Division, Office of the Management Board, Secretariat of the Bank, Human Resources and Organization Group, Legal Affairs Division, Compliance Division, Management Board Office for Corporate Communications, Management Board Office for Economic Research and Strategic Planning, Office for Customer Satisfaction Measurement, Office for Corporate Governance of PBZ Group Subsidiaries and Equity Holdings, Project Management Office as well as the Management Board Office for Security and Data Governance Office are integral elements of the overall logistics and support of the business groups and the management.

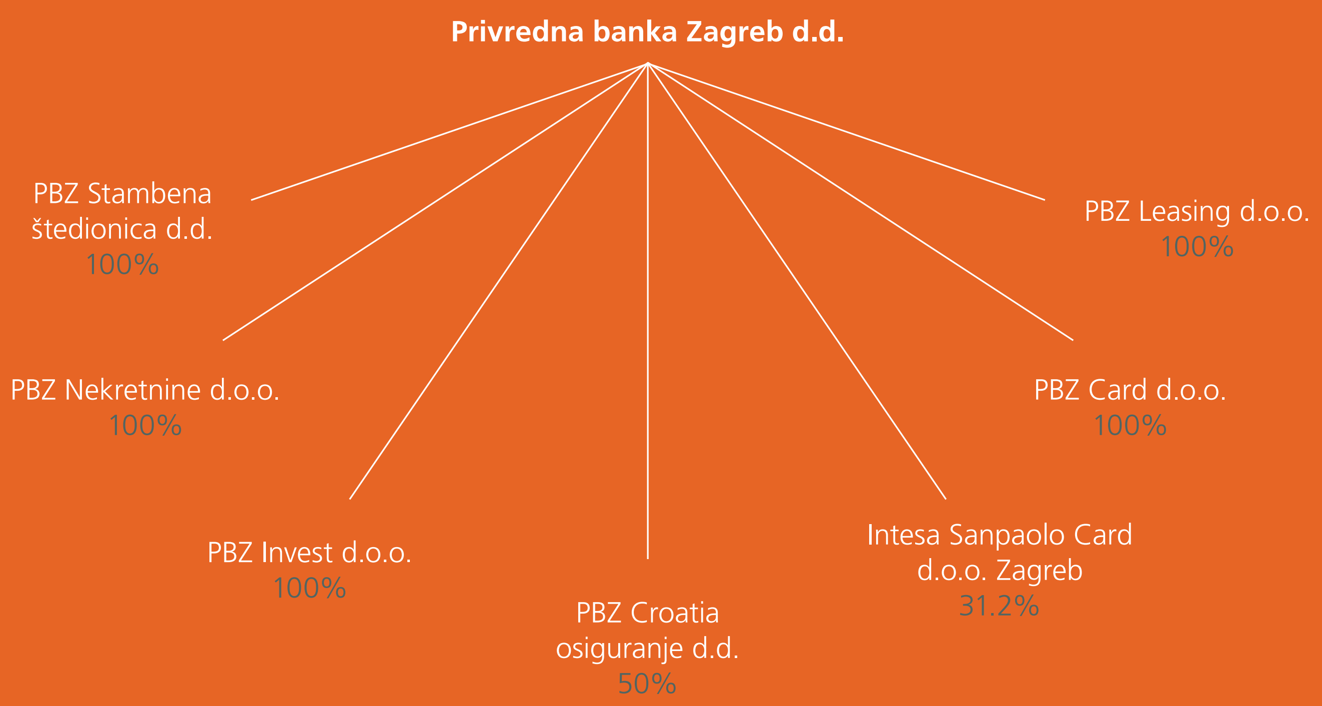
Velebit

The Group

The Privredna banka Zagreb Group is a Croatian based financial services group which provides a full range of retail and corporate banking services to customers in Croatia. The Group employs some 4,158 employees and serves nearly 1.6 million both private and corporate clients in the country. PBZ Group today is a well-organised institution whose market share in the overall banking system stands at 17.2 percent.

On 31 December 2012 the Group consisted of Privredna banka Zagreb and 5 subsidiaries and 2 associates.

The composition of the Group and a brief description of each subsidiary are set out below.



PBZ Card

PBZ Card is the leading card institution in Croatia. The Company specialises in issuing charge, credit and debit cards and is the only card organization responsible for charged with issuing and accepting American Express cards. It also offers a service of acceptance and building the sales network of MasterCard and Visa cards for the Croatian market. As the leading card organisation, PBZ Card today has a portfolio of more than 2 million active cards issued under the brands American Express, MasterCard, Maestro, Visa and Visa Electron and its developed sales network has approximately 60 thousand service establishments countrywide.

The operations of PBZ Card are founded on the wealth of knowledge and experience built up over more than 40 years of the presence of American Express on the Croatian market, the importance of the MasterCard and Visa brands and the strong position built up by Privredna banka Zagreb as the leading bank in introducing new technologies and products into card operations. The company strives to maintain the leading position and continues its market penetration that will further strengthen PBZ's position in card operations.

In 2012, the Company has celebrated forty years of American Express presence on the Croatian market, organising different activities for its card members and business partners. Likewise, it continued enhancing its portfolio with new products, such as Metro American Express Card, the first business co-brand card in the PBZ Card portfolio, and American Express Gift Card, improved services and benefits for its card users and partners through upgrading the special benefits including payment in instalments, savings programs Membership Rewards and My Card loyalty programs and many others. In addition, the Company has been very active on the social networks by following contemporary communication and marketing trends.

The Company also continues its distinguished social responsibility program particularly through its humanitarian card the American Express Card with a Heart donating notable funds to the Croatian Ministry of Health's project "Monitoring Children with Neurorisks".

Continuous portfolio and service improvements have been recognised by receiving several awards. Among others, the Company won the prestigious Global Network Services American Express Award for the launch of Membership Rewards® card.

PBZ Stambena štedionica

PBZ Stambena štedionica was founded by Privredna banka Zagreb in 2003. Given the large number of our clients interested in housing savings, the company offers four types of savings: Prima, Basic, Golden and Golden Children's savings. At present we have nearly 117 thousand savings contracts which amount to nearly HRK 1.3 billion. Prima and Basic types are aimed at clients whose goal is to make use of a housing loan with exceptionally favourable interest rates. Golden savings are designed for clients whose first intention is long-term saving. Golden Children's saving is aimed at children under 10. These forms of saving are run with a foreign currency clause in euro whilst deposits are insured in accordance with the Credit institutions act. There is also the possibility of changing the type of savings account whilst saving. Clients have the opportunity to manage their own savings accounts from their own home by means of Internet banking through PBZ365@NET services.

PBZ Invest d.o.o.

PBZ Invest d.o.o. was founded by Privredna banka Zagreb in 1998 as an asset management company in order to establish and manage mutual funds.

PBZ Invest d.o.o. seeks to offer clients a wide-range of investment funds and investment strategies. Our goal is to meet and exceed the needs of investors with varied preferences and investment goals. Our focus ranges from conservative investors - who prefer safety and liquidity, to those clients that are not averse to risk and want to see their investment value grow over a mid or long-term period.

Since its establishment in 1998, PBZ Invest has had 8 Mutual funds, of which four are Money market mutual funds - PBZ Novcani, PBZ Kunski novcani, PBZ Euro and PBZ Dollar, one bond fund - PBZ Bond, one balanced fund - PBZ Global, and two equity funds - PBZ Equity and PBZ I-Stock Fund. Due to changes on the market in July 2007, PBZ Invest decided to merge the PBZ Kunski novcani Fond with PBZ Novcani. So, since July PBZ Invest has been managing 7 Mutual Funds.

PBZ Novčani fond, the money market fund, is an open-ended investment fund with a conservative investment philosophy, focusing on low risk investments and high liquidity. The goal of the fund is to offer an alternative to kuna cash bank accounts. Purchasing stakes in the Fund enables investors to earn higher returns on their investment compared to a usual savings account. It represents a low-risk investment, an uninterrupted and unconditional liquidity option, and competitive return on investment by market standards.

PBZ Euro Novčani fond, the money market fund denominated in EUR. It is intended for investors seeking to hedge their funds denominated in HRK from exchange rate risk. This way the fund offers protection against the depreciation of the HRK/EUR exchange rate. PBZ Euro Novcani fond primarily invests in low risk short-term securities denominated in EUR.

PBZ Dollar fond, the money market fund denominated in USD, is intended for investors seeking to hedge their funds denominated in HRK from exchange rate risk. This way the fund offers protection against the depreciation of the HRK/USD exchange rate. Assets are invested in low risk short-term Government Securities, primarily issued by Croatia and denominated in USD. Like the money market fund, it is suitable for conservative investors who are more inclined to invest in US Dollars.

PBZ Bond fond, the bond fund, also an open-ended investment fund, aims to enable both private and institutional investors to earn additional income by investing in first-class domestic and global bonds issued by governments, local governments and the most stable domestic and global corporations, primarily denominated in EUR.

PBZ Global fond, the balanced fund, is an open-ended investment fund aimed at investors with moderate risk aversion and willingness to expose assets to the capital market, for the long term, or at least three years. The assets of the fund are invested in a combination of equity and bonds, traded locally, regionally and globally. The optimal combination should provide significant yield without compromising the security of the investment.
PBZ Equity fond, the equity fund, is an open-ended investment fund aimed at investors willing to expose their assets to the risks of the capital market over the long term, or at least from three to five years. The assets of the fund are mostly invested in equity traded locally and regionally, with exposure to emerging and global markets. Regional diversification helps us diversify risk and provide the possibility to earn a significant yield.
PBZ I-Stock fond, the equity fund, is an open-ended investment fund aimed at investors willing to expose their assets to the risks of the capital markets in the emerging economies. Risk exposure is the highest in this fund out of the entire PBZ Invest fund portfolio. The time horizon is also longer, or at least from three to five years. The assets of the fund are mostly invested in equity traded on the emerging and local markets. This fund is the best choice for individual investors interested in a high return at significant risk.
In 2005, in cooperation with Privredna banka Zagreb, PBZ Invest d.o.o. launched 2 tranches of a structured product - PBZ Protecto. This PBZ structured product is a combination of investment funds and classic savings in a bank, with a guarantee on the money invested.
In 2009, PBZ Invest introduced another new product – portfolio asset management for private individuals as an addition to Fund Management.
PBZ Invest d.o.o. is confident that there is a prosperous future for the investment fund industry on the Croatian financial market. Despite the significant shrinkage of assets under management since 2008, due to the global financial crisis, in 2012 the investment fund industry continued to stabilize assets under management. Money market funds remain a stable and trusted base for investors and therefore represent the leader in the rebuilding of assets under management. PBZ Invest is managing to maintain and increase its market share in the Croatian investment fund industry, it is holding a market share of 18% at the end of 2012.
PBZ Invest d.o.o. is an active member of the Croatian Chamber of Commerce, as well as a member of the Croatian Employers' Association, the Financial Services Association and ACI Croatia. PBZ Invest d.o.o. as an asset management company has received several awards for excellence in managing different types of mutual funds.

PBZ Leasing

PBZ Leasing is wholly owned by Privredna banka Zagreb. It was founded in 1991 under the name of PBZ Stan. In the beginning it dealt with property appraisals and restructuring of the public housing fund. From 1995 until 2004, the company commenced granting car purchase loans by placing funds of Privredna banka Zagreb.
From 2004, leasing has become core business activity of the company. Through finance and operating leases, the company engaged in financing of real estates, personal and commercial vehicles, vessels, machinery and equipment. In the last year the company made new leasing placement in amount of almost HRK 0.66 billlion.
By the end of 2012, PBZ Leasing made over 5.6 thousand lease arrangements with customers, which in financial terms reached almost HRK 1.3 billion.

PBZ Nekretnine

PBZ Nekretnine is a wholly owned subsidiary of Privredna banka Zagreb which engages in property transaction services, construction management and real estate valuation. Privredna banka Zagreb established PBZ Nekretnine with the goal of providing its clients with a complete range of services relating to property and investment in business projects. PBZ Nekretnine offers apartments, houses, business premises, construction sites and other properties for sale.
The activities of PBZ Nekretnine involve property transactions, property transaction services, property renting, construction, planning, construction supervision, construction evaluation, appraisal of property value, preparation of feasibility studies for investments, as well as legal supervision of works. PBZ Nekretnine has a professional team capable of answering all its clients' complex requests. The company provides all kinds of services related to the activities mentioned, no matter how specific and complicated the clients' demands are. PBZ Nekretnine employs highly trained employees, five of which are court experts in the field of construction. The company has been operating successfully within the Group since it was founded at the beginning of 1999. For the needs of its clients, PBZ Nekretnine has developed a network of associates and at the moment collaborates with over 70 associates.

PBZ Croatia osiguranje

PBZ Croatia osiguranje is a joint stock company for compulsory pension fund management. The company was incorporated on 26 July 2001 in accordance with the new changes in Croatian pension legislation and it is a mutual project of both Privredna banka Zagreb d.d. and Croatia osiguranje d.d. with ownership in the company of 50 percent belonging to each shareholder.

The principal activities of PBZ Croatia osiguranje include establishing and management of the compulsory pension fund. After the process of the initial stages of gathering members, PBZ Croatia osiguranje fund became one of the three largest compulsory funds in the country. Despite fierce competition on the market, the company's pension fund continued to operate successfully during 2012. In the successful management of its funds, PBZ Croatia osiguranje relies on its positive experience in managing investment funds and association with Gruppo Intesa Sanpaolo asset management.

At this point, the fund has over 295 thousand members and net assets in personal accounts exceeding HRK 8.3 billion, which represents a sound base for the long-term stable and profitable operation of the company.

Intesa Sanpaolo Card d.o.o. Zagreb

Intesa Sanpaolo Card was established in April 2009 by Intesa Sanpaolo Holding International S.A., Privredna banka Zagreb and Banka Koper. As of 31 December 2012, PBZ held 31.2 percent share of ownership, which was result of the demerger of processing unit in PBZ Card and direct capital investments.

The foundation of the company is based on complementary strengths of the two strongest cards businesses within the Intesa Sanpaolo Group, Banka Koper and Privredna banka Zagreb, and their transition from local companies into a fully international organization. Both centres of excellence were recognized based on long-term experience in card business in home markets (Croatia and Slovenia) which are, by many parameters, more advanced than some of the West-European markets. Both centres have the best practice not only at the level of Intesa Sanpaolo Group but also at the level of the entire Central-Eastern Europe.

Intesa Sanpaolo Card delivers a wide range of services to meet business needs of its clients. All services and solutions are tailored to meet regional, local market or individual client requirements:

- Issuing solutions - the Company and the Group offer a range of services across all stages of customer lifecycle. The Company card processing platform supports a comprehensive portfolio of products including a broad range of payment card types (consumer and commercial cards, debit, prepaid, credit, co-brand and affinity cards) and brands (American Express, MasterCard, Visa, private label). Services provided - Card management system, Credit management, Transaction processing, Authorization processing, Card personalisation and distribution.
- Acquiring solutions – the Group card processing platform offers a wide range of services which help company’s partners to build profitable card acquiring business. Services provided – Merchant administration, authorisation and transaction processing, POS and ATM terminal management, E-commerce solutions.
- Value added services - in addition to standard services and solutions, the Group provides a wide range of value-added services, giving innovative and technologically advanced solutions to company’s partners helping them to retain their current customers and attract new ones (loyalty programs, dispute and chargeback management, fraud and risk management, value added services at ATMs and POS terminals).

Dinara

Overview of the activities within the Corporate Social Responsibility programme of PBZ

Appendix to the Annual Report

Introduction

Ever since its establishment Privredna banka Zagreb has been at the very top of the Croatian banking sector and for a series of years has been playing a significant role and producing impact on our society's economic and social development. Nowadays, being a member of a large international banking group – Intesa Sanpaolo, we stand for a dynamic and modern European bank that keeps its finger on the pulse of the market and its customers. Boosting trust and improving the relationship with all parts of society that interact with the Bank represents the condition of a continuous improvement of our business. With our actions we aim to meet the needs and rise up to the expectations of all participants, from caring for the needs of our customers, employees, developing the local communities in which we are a part of, caring for the environment to creating new value for shareholders. Below is an overview of some of the more significant activities carried out in 2012.

1. Education and professional development

- we have been investing continuously in development of corporate knowledge via the 'PBZ business school' project – in 2012 the 6th generation of students enrolled and the programme counted 255 active attendees
- the 1st generation of IT academy ITAKA (internal training programme aimed at specialising employees) enrolled; 50 employees working in IT successfully completed the programme
- measures have been taken to upgrade the e-learning platform – three new e-learning programmes have been designed and introduced and additional licences have been procured thus allowing all PBZ group employees to access LMS
- the on-line library with about 30 thousand recent publications pertaining to finance, IT and management has been introduced
- we are actively engaged in the enforcement of active employment measures and, in cooperation with the Croatian Employment Service (HZZ), 50 persons were accepted into the PBZ Card system for participation in the programme of professional training for work without employment
- professional practice for students was set up within the Bank and PBZ group members; a total of 69 students coming from various faculties and colleges completed the internship programme within PBZ group
- cooperation has been established with domestic and international universities for the purpose of promoting, co-designing and running education programmes in the field of finance and banking; here we would particularly like to single out our cooperation with Libertas Business College and University College for Applied Computer Engineering

2. Care for employees

- the process of centralising the human resources function at PBZ group level has been fully completed and has established a single HR platform at group level (advantages: standardization of business processes and operating methods at PBZ group level; easier coordination, faster decision-making and more efficient control of staff functions)
- throughout 2012 we continued to upgrade eHR portal by implementing new functionalities: a more advanced search engine (allowing selection as per chosen parameters), creating CVs of all employees on personal eHR portal, electronic printing of calculation slips and tax cards, automatic creation of default reports for internal users
- aiming to continuously keep track of the potential and development needs of PBZ group employees, additional evaluation programmes have been set up and employees can now get feedback regarding their potential and development possibilities;
- in 2012 the internal rotation process has been rendered simpler and at strategic level we made a decision to encourage and facilitate internal schedules and rotations for the purpose of enabling internal development and improving employees' duties and by extension boosting their motivation and satisfaction
- the organisational climate was measured, which means that we have been keeping up the trend of uninterrupted continuous evaluation of important aspects: satisfaction, dissatisfaction and motivational factors and activities taken in response to the results
- within the scope of regular socioeconomic activities, solidarity was shown by helping destitute employees and their families, children of employees who passed away, we arranged that two orphans receive a scholarship; grants were made to employees with school age children so that they may procure school books; as part of our on-going cooperation with our colleagues from Intesa Sanpaolo we made arrangements that children be sent to the Children's village Follonica, Italy for a summer vacation;
- we care about the financial burden of our employees and educate and advise them via our Personal finance management programme on the way of balancing their income and expenses, we participate in putting forward proposals on debt rescheduling with a view to regaining financial stability
- as part of our employee healthcare programme, we organised regular full check-ups for both our employees and trainees, control check-ups for the employees who suffer from the ailments of the skeletal system with physical therapy as part of the treatment and preventive flu vaccination
- membership in the association PBZ Standard as of 2012 covered all the employees within PBZ group by which the number of members has increased to approximately 2,520; the range of activities has been expanded to the subsidiaries that had none and for the first time sports activities have been introduced for the children of employees of PBZ group
- in 2012 PBZ Standard subsidized participation of member employees in the humanitarian tournament where the money was collected for fit-out of a vehicle that daily transports disabled students

- the monthly bulletin PBZ Express, issued for the purpose of keeping employees up to date with novelties, also organised a humanitarian campaign called „Let's donate together" in which employees were involved in the campaign of collecting toys for the orphans living in the Children's home Lipik (over 200 packages were received) and a humanitarian campaign for the Children's home in Vinkovci; in addition to the 250 packages, the children's home also received two laptops and an LCD television set

In September 2012 we opened PBZ kindergarten Čigra – corporate day care centre for the employees of Privredna banka Zagreb, currently attended by 71 children. The children are organised into three nursery and one kindergarten group, and in addition to the full equipment of both internal and external area, the day care centre offers various additional options such as sports, foreign language learning, organising theatre plays and drama workshops. By opening the corporate day care centre PBZ is building an image of an employer focused on family as the most important value in life and on its employees as its most important resource. In such a way employees' satisfaction grows and allows them to reconcile their family and business affairs more easily.

4. New initiatives

PBZ Business Club – initiative involves organizing informative and educational meeting's with clients organized with the aim of informing them about PBZ financing programs developed in collaboration with EU development banks, Croatian Agency for SMEs and Investment, EU funds etc. These meetings are held in all major Croatian cities with PBZ's Chief economist providing macroeconomic outlook presentations.

5. Donations and sponsorships

Privredna banka Zagreb aims to contribute and show its responsibility towards the larger community by sponsoring events and giving donations. In 2012 almost HRK 26 million in total was appropriated for sponsorships and donations, by which we supported many cultural and other events, sports events, science and education, numerous associations and individuals. By its long standing participation in the social life through donations and sponsorships, PBZ aims to contribute to the development and in general to a better quality of life in the Republic of Croatia.

5.1. Donations

Donations in 2012	
Science and education	1.150.100 HRK
Sports	1.259.660 HRK
Culture	799.450 HRK
Social solidarity	9.820.840 HRK
Other	2.434.550 HRK
Total	**15,464,600 HRK**

PBZ actively participates in a series of socially useful projects and supports financially a great number of humanitarian and social institutions. Among the donations given in 2012 we would like to single out the following ones:

- Caritas campaign titled "For a thousand joys". For the 10th year in a row we were part of the great Caritas campaign raising funds for the foundation "For a thousand joys". The purpose of the campaign is to raise funds for Croatian families with low income. This year, under the slogan "Believe it or not – you can change the World" the action is specifically focused on public awareness of the difficulties faced by many families who are struggling with debt
- Donation to Ana Rukavina Foundation – a Registry of voluntary hematopoietic stem cell donors

Substantial funds were donated to raise the level of healthcare in numerous health institutions throughout the Republic of Croatia. In 2012, a two major donations were given to Children's Hospital Srebrnjak and the Clinical Hospital Dubrava.

- Children's Hospital Srebrnjak received the donation for the full equipment of the Clinical Research Ward – the first such Ward in Croatia and fully in accordance with EU standards that should revolutionize the development dosage for children's medications using the extensive research and testing, in accordance with strict norms, to confirm the effectiveness and safety of medications for children.
- Clinical Hospital Dubrava were donated the new CT device that should contribute to the quality of healthcare for seriously ill patients. At the Clinical Hospital Dubrava, besides inhabitants of Zagreb, many other citizens from the whole of Croatia are treated and CT scans are made for over 15,000 patients a year.

We would also like to emphasize the donation in the area of "restoration of cultural monuments and heritage" to the restoration of St. Frances (sv. Franjo Ksaverski) parish church which is a first category monument of cultural heritage from the baroque period.

5.2. Sponsorships

Sponsorships in 2012	
Science and education	HRK 597,215
Sports	HRK 7,346,457
Culture	HRK 1,671,855
Other	HRK 402,715
Total:	**10,018,242**

With its sponsorship policy as well as the promotion of its brand, PBZ aims to provide financial support and incentive to a great number of projects pertaining to culture, sports and science and thus contribute to the development of the Croatian society. In 2012 we would like to put an emphasis on cultural sponsorships by supporting various cultural events and institutions:

- Sponsorship of the Croatian National Theater in Zagreb – oldest (over 150 years) national theater institution that includes three large artistic ensembles (Drama, Opera and Ballet) - PBZ is a general sponsor of the season
- Sponshorship of the Modern Gallery Zagreb with its permanent exhibition of the top works of the Croatian artists of the 19th, 20th and the 21st century. All those works represent master pieces of landscape art, figurative art and abstract art as well as of portrait and animalistic sculpting. Being the main patron of the Modern Gallery, over the past years PBZ helped purchase new master pieces, painting and sculptures alike
- Sponsorship of one of the most renowned cultural events in Croatia – **Sinjska alka**, a tournament being organised for almost as long as three centuries, respecting the old customs. It has been taking place without interruption ever since 1715, and this unique spectacle has been recognised by Unesco as cultural world heritage.
- Support of various cultural programs and institutions included Croatian National Theatres in Zagreb Osijek and Varaždin, traditional ethnological manifestation "Rapska fjera", cultural event "Vinkovačke jeseni" and many others…

6. Impact on the environment

We have continuously been keeping track of our energy consumption and with various activities aim to reduce the consumption, while raising awareness of our employees on the importance of caring for the environment. On a regular basis we have been sending our employees personalised e-mails so as to remind them about mandatory shutting down of their PCs after office hours, turning off their-conditioning and heating over the weekend, separating used paper from other waste for recycling purposes.
Paper waste and plastics is gathered separately and collected by a contracted company that recycles it. Hazardous waste as cartridges are also separately sorted and collected by a contracted company which does business in compliance with laws and regulations.
Double sided copying of documents, which we introduced as our standard setting, reusable envelopes and other activities in that direction have resulted in a continues decrease in the consumption of paper, which is presented in the table below:

PAPER CONSUMPTION

2008	579,854 kg
2009	518,849 kg
2010	503,525 kg
2011	445,471 kg
2012	444,560 kg

Also, since June 01 2012, all the envelopes used in the Bank are made of recycled paper as well as A4 paper for automatic letter folding which resulted in a substantial increase in recycled paper usage. Total usage of recycle paper for 2012 was **105,699 kg** while in 2011 was **6,505 kg**.
Installing energy efficient light bulbs and electronic ballast in order to cut energy consumption for lighting is a common practice. Upon replacement of worn-out equipment, attention is paid to having such equipment replaced with one of optimal characteristics (classic light bulbs are replaced with energy efficient bulbs, air-conditioning devices with inverter technology and of higher energy efficiency degree are installed, the material and elements of good insulation properties are used in construction, LED lighting is used in advertising signs and also, heat recovery ventilation is installed.
As a result of our efforts in that direction ?, we have finished the process of the GreenLight certification of our branch offices in 2012 and on January 15 2013 we have received the welcome letter from the EC Joint Research Centre recognizing us as an official Partner **in GreenLight Program**.

GREENLIGHT

Electricity CONSUMPTION (KWH 000)

2009	18,617
2010	18,725
2011	17,529
2012	16,892

Biokovo

Corporate governance

In accordance with the Companies Law, Credit Institutions Act and its Article of Association, the Bank has a Supervisory Board and a Management Board. Above mentioned acts regulate the duties and responsibilities of members of the Management Board and the Supervisory Board. The two boards are separate and no individual may be a member of both boards.

Supervisory Board

The Supervisory Board consists of seven members. The Board meets quarterly and oversees the Management Board. The members of the Bank's Supervisory Board are appointed on a three year mandate. Members of the Supervisory Board are the following:

György Surányi, (President of the Supervisory Board, Intesa Sanpaolo) – mandate from 31 January 2010

Ivan Šramko, (Deputy President of the Supervisory Board, Intesa Sanpaolo) – mandate from 29 March 2011

Massimo Pierdicchi, (Member of the Supervisory Board, Intesa Sanpaolo) - mandate from 31 January 2010

Beata Kissné Földi, (Member of the Supervisory Board, Intesa Sanpaolo) – mandate from 9 April 2012

Giampiero Trevisan, (Member of the Supervisory Board, Intesa Sanpaolo) – mandate from 1 March 2010

Nóra Kocsis, (Member of the Supervisory Board, EBRD) - mandate from 2 July 2010

Branko Jeren, (Member of the Supervisory Board, independent - mandate from 19 April 2010)

Audit Committee

Pursuant to the Articles of Association of Privredna banka Zagreb, the Supervisory Board on its 15th meeting held at 10 December 2002 established the Audit Committee and adopted the Audit Committee Charter.

The Committee contributes to the work of Supervisory Board by monitoring various important processes such as the financial reporting, effectiveness of internal audit, risk management and compliance with laws. Among the above mentioned, during 2012 the Audit Committee discussed the annual work plans and reports (quarterly, semi-annual and annual) of control functions and significant issues relating to this area and overseeing the auditing of annual unconsolidated and consolidated financial statements and gave the recommendation of the assembly of shareholders on the selection of audit companies.

The Audit Committee may have at least three members.

Members of the Audit Committee in 2012 are the following:

Giovanni Bergamini, (President of the Audit Committee)

Beata Kissné Földi, (Member of the Audit Committee)

Guido Gioncada, (Member of the Audit Committee)

Dean Quinn, representative of Chief risk officer of Intesa Sanpaolo is present on meetings of the Audit committee as associate member

Executive Committee

Pursuant to the Articles of Association of Privredna banka Zagreb, the Supervisory Board on its 15th meeting held at 10 December 2002 established the Executive Committee as a auxiliary body and adopted the rules of procedure for the board.

The Executive Committee has three members (chairman and two members of the Supervisory Board of the Bank) and gives consent to the Decisions of the competent bodies of the Bank. Committee contributed to the Supervisory Board by rapid and effective resolution of issues that are mostly related to the Bank's exposure to credit risk for retail and corporate clients and organisational changes in the Bank.

Members of the Executive Committee in 2012 are the following:

György Surányi (President of the Executive Committee)

Massimo Pierdicchi (Member of the Executive Committee)

Beata Kissné Földi (Member of the Executive Committee)

Statement on the implementation of the Code of Corporate Governance at Privredna banka Zagreb

Management Board

The Management Board conducts business operations of the Bank. The Board consists of seven members and on three-year mandates, each is allocated a specific area of responsibility. The Management Board meets at least twice a month to discuss and determine the operating policies of the Bank.

Members of the Management Board are the following:

Božo Prka, President of the Management Board – new mandate from 9 February 2012

Gabriele Pace, (Deputy President of the Management Board responsible for Project Management office, MB Office for Security, Data Governance Office, Risk management and control Group, IT and Operations Group, Accounting, Taxation, Controlling and General administration Group) – mandate from 17 July 2010

Darko Drozdek, Member of the Management Board responsible for the SME Banking Group – mandate from 21 October 2010

Ivan Gerovac, Member of the Management Board responsible for the Corporate, Treasury and Investment Banking Group – mandate from 9 February 2012

Draženko Kopljar, Member of the Management Board responsible for the Information Technology and Operations Group – new mandate from 9 February 2012

Dinko Lucić, Member of the Management Board responsible for the Retail Banking Group – new mandate from 9 February 2012

Andrea Pavlović, (Member of the Management Board responsible for the Risk Management and Control Group) – mandate from 12 May 2010

Statement on the implementation of the Code of Corporate Governance at Privredna banka Zagreb

Pursuant to the provisions of Article 272.p of the Companies Act, the Management Board of Privredna banka Zagreb d.d. hereby declares that the Bank voluntarily implements the Code of Corporate Governance prepared jointly by the Croatian Agency for Supervision of Financial Services (HANFA) and the Zagreb Stock Exchange (ZSE).

The Annual questionnaire for the business year 2012, which makes a constituent part of this Statement (available also on the Bank's web site), reveals the Bank's corporate governance status and practices in view of the recommendations given in the Code of Corporate Governance, and provides explanations of certain departures. Namely, the Bank's corporate governance is not based solely on full satisfaction of regulatory requirements, but also on ingrained corporate culture and personal integrity of its management and employees.

General features of the conduct of internal supervision and risk management in terms of financial reporting are described in this Annual report, as well as data on the Bank's shareholders (as at 31 December 2012) are provided in this Annual report.

Rules on the appointment and recalling of members of the Management Board are laid down in the Bank's Articles of Association.

The number of members of the Management Board of the Bank is determined by decision of the Supervisory Board. Accordingly, the Management Board is composed of seven members. The Supervisory Board brings a decision to nominate candidates for President and members of the Management Board, who need to meet the conditions prescribed by the law governing banking operation and other relevant regulations. After obtaining the prior consent of the central bank, the Supervisory Board appoints the president and members of the Management Board for a three-year term of office, with the possibility of re-appointment. The Supervisory Board may revoke its decision on the appointment of a member or the president of the Management Board provided that there are substantial grounds therefore pursuant to the law in force.

Authorities of the Management Board are set out in the Bank's Articles of Association, while a special decision was adopted, with the consent of the Supervisory Board, to lay down the distribution of authority among the president, deputy president, and other members of the Management Board of the Bank.

Data of the composition and activities of the Management Board and the Supervisory Board of the Bank and their supporting bodies are presented in the enclosed Annual questionnaire.

Rules for making amendments to the Articles of Association of the Bank are laid down in the Articles of Association. The Decision on the amendments to the Articles of Association is adopted at the General Meeting of the Bank, in accordance with the law and the Articles of Association, by a ¾ majority of the voting share capital represented at the General Meeting on adoption of the decision. Amendments to the Articles of Association are proposed by the Supervisory Board, the Management Board, and the Bank's shareholders. The Supervisory Board is authorized to amend the Articles of Association only if it is a matter of harmonisation of the wording or of establishing the final version of the Articles of Association.

With a view to protect the interests of all investors, shareholders, customers, employees, and other interested parties, the Bank has set high corporate governance standards.

All questions contained in this Questionnaire relate to the period of one year for which annual financial statements are prepared.

1. **Does the Company have its own website?**
   Yes. The Bank's website address is www.pbz.hr

2. **Are the annual, semi-annual and quarterly financial statements available to the shareholders?**
   - At the Company's headquarters?
     Yes.
   - On the Company's website?
     Yes. The annual financial statements for 2012 with the external auditors' report are available on the Bank's website. Semi-annual and quarterly reports (TFI-KI form) for 2012 are published on the Bank's and Zagreb Stock Exchange website.
   - In English?
     Yes. The annual financial statements for 2012 with the external auditors' report are prepared and available in English on the Bank's website. Semi-annual and quarterly reports are also available on Bank's website.

3. **Has the Company prepared a calendar of important events? (If not, why not?) If yes,**
   - Has the calendar of important events been published on the Company's website? (If not, why not?)
   - Has the calendar of important events been updated regularly and in good time? (If not, why not?)
     Yes, the Bank has published a calendar of important events on its website and it is updated with each change.

4. **Is there a cross-ownership relationship between the Company and another Company/other Companies?**
   No.

5. **Are data on securities issued by the Company and held by the Supervisory Board members or Management Board members presented in the annual financial statements?**
   Yes. The number of Bank shares held by the Management Board and Supervisory Board member as of 31 December 2012 is published in the Annual Report for 2012. There were no changes (increase/decrease in number of shares owned) during 2012 by Supervisory Board and Management Board members.

6. **Are data on financial instruments issued by the Company and held by Supervisory Board members or Management Board members published on the Company's website and regularly updated (on a 24-hour basis)? If not, why not?**
   No. Data are published on the Zagreb Stock Exchange and HANFA website within the legally prescribed period and contents.

7. **Does the Company identify and publicly disclose risk factors? (If not, why not?)**
   Yes. Bank's risk factors are disclosed within the Annual report which is prepared in accordance with the International Financial Reporting Standards.

8. **Has the Company established mechanisms to ensure:**
   - That clarifications in respect of privileged information, its nature and importance, as well as the restrictions on its use, are supplied to persons to whom such information is made available? (If not, why not?)
     Yes.
   - Supervision of the flow of information and its possible misuse? (If not, why not?)
     Yes.

9. **Does each share of the Company carry the right of one vote?**
   Yes.

10. **Are the nominations, including relevant CVs, for all candidates for Supervisory Board or Management Board membership to be elected or appointed at the General Meeting, announced on the Company's website? (If not, why not?)**
    Yes. The Bank always discloses proposed decisions to both General and Extraordinary meetings of shareholders. These materials also include proposals for changes in the membership of the Supervisory Board with relevant CVs of the candidates and are posted on the Bank's website.

11. **Does the Company treat all shareholders in the same manner?**
    Yes.

12. **Did the Company issue new shares?**
    No.

13. **Did the Company acquire or release its own (treasury) shares?**
    No. During 2012 Bank did not acquire or release its own shares.

14. **Is the process of proxy issue for the General Meeting simplified and free of strict formal requirements?**
    Yes.

15. **Did the Company provide proxies for shareholders, who are for some reason prevented from voting at the General Meeting, who are obliged to vote in compliance to the shareholders' instructions, at no extra cost? (If not, why not?)**
    No. There were no such initiatives by the shareholders but the Bank is prepared to provide proxies for the shareholders if such an initiative occurs.

16. **Did the Management Board of the Company, up on convocation of the General Meeting, determine the date when the status in the share register would be established for the purpose of granting voting rights at the General Meeting of the Company in the manner that the date falls no more than six days**

before the General Meeting? (If not, why not?)
Yes.

17. Does the Decision on dividend payment or dividend advance stipulate the date when shareholders are to acquire the right to dividend payment and the date of dividend payment or period? (If not, why not?)
Yes.

18. Is the date on which the shareholders acquire the appropriate dividend payment or dividend advance payment at most 30 days after the adoption date of passing the respective Decision? (If not, why not?)
Yes, but from the day of gaining the right to claim for the payment of dividends, in accordance with the provisions of the Companies Act.

19. Is the decision on payment of dividend or advance which is determined by the aforementioned dates announced and submitted to the stock exchange no later than 2 days after the adoption?
Yes.

20. Did certain shareholders enjoy privileged treatment during dividend payments or advance dividend payments? (If yes, why yes?)
No.

21. Were the Agenda of the General Meeting, relevant information and documents with explanations relating to the Agenda published on the Company's website, and made available to the shareholders at the Company's headquarters as of date of the first public announcement of the Agenda? (If not, why not?)
Yes.

22. Were the Agenda of the General Meeting, relevant information and documents also published on the Company's website in English? (If not, why not?)
Yes.

23. Were any requirements set for participation at the General Meeting and exercising voting rights (irrespective of whether such requirements are prescribed by the law or the Articles of Association) such as announcing one's participation in advance, certifying letters of proxy, and the like? (If yes, why yes?)
No.

24. Apart from the contents prescribed by the law, does the report submitted by the Supervisory Board to the General Meeting contain an assessment of the Company's overall business performance, the performance of its Management Board and a separate commentary on its co-operation with the Management Board? (If not, why not?)
Yes

25. Is it possible for the shareholders to participate and, in particular, to vote at the Company's General Meeting by means of modern communication technology? (If not, why not?)
No. There were no such initiatives by the shareholders.

26. Did the Company's Management Board publish the decisions by the General Meeting and also information on possible law suits contesting such decisions? (If not, why not?)
Yes. (Note: there were no law suits contesting Decisions by the General Meeting)

27. Did the Supervisory Board make a decision on the tentative work plan which includes a schedule of its regular meetings and reports that should be made available to the Supervisory Board members on a regular and timely basis? (If not, why not?)
Yes. The schedule of the Supervisory Board meetings for the current year was determined and published on Bank's website. Reports that are regularly and timely put at the disposal of Supervisory Board members are defined by the individual decisions of the Supervisory Board and by law.

28. Did the Supervisory Board adopt Rules of Procedure? (If not, why not?)
Yes.

29. State the names of the Supervisory Board's members.
György Surányi, President;
Ivan Šramko, Deputy President;
Massimo Pierdicchi, Member;
Beata Kissné Földi, Member;
Giampiero Trevisan, Member;
Nóra Kocsis, Member;
Branko Jeren, Member.

30. For each Supervisory Board member, state the names of the companies of which he/she is a member of the Supervisory Board or the Management Board. If any of these companies is to be considered a competitor to your Company, indicate it.

György Surányi is a President of the Supervisory Board of the following companies:
CIB – Budapest, Hungary
VUB – Bratislava, Slovakia

Ivan Šramko is a member of the Supervisory Board of the following companies:
Intesa Sanpaolo Bank – Sarajevo, Bosnia and Herzegovina
Banka Koper – Koper, Slovenia
Banca Intesa Beograd – Belgrade, Serbia
CIB – Budapest, Hungary

Massimo Pierdicchi is a President of the Supervisory Board of the following companies:
Banca Intesa Beograd – Belgrade, Serbia
Intesa Sanpaolo Bank Albania – Tirana, Albania

And a member of the Supervisory Board of the following companies:

Massimo Pierdicchi *is a member of the Supervisory Board of the following companies:*
Intesa Sanpaolo Bank – Sarajevo, Bosnia and Herzegovina
ISP Romania – Bucharest, Romania

Beata Kissné Földi *is a member of the Supervisory Board of the following companies:*
Banca Intesa Beograd – Belgrade, Serbia
Intesa Sanpaolo Bank – Sarajevo, Bosnia and Herzegovina

Nóra Kocsis *is a member of the Supervisory Board of the following companies:*
Volksbank A.D. – Belgrade, Serbia

Giampiero Trevisan *is a member of the Supervisory Board of the following companies:*
CIB – Budapest, Hungary
Intesa Sanpaolo Bank – Bucharest, Romania

31. Is the Company's Supervisory Board mostly composed of independent members? (If not, why not?)

No. The Supervisory Board have one independent member as required by provisions of Credit Institutions Act.

32. State independent Supervisory Board members?

Branko Jeren.

33. Is there a long-term succession plan in place in the Company? (If not, why not?)

Yes.

34. Is the remuneration of the Supervisory Board members entirely or partly determined according to their contribution to the Company's performance? (If not, why not?)

Yes.

35. Is the remuneration of the Supervisory Board members:

- Determined by the Decision of the General Meeting?
  Yes.
- Determined in the Articles of Association of the Company?
  Yes, although most of the members of the Supervisory Board do not receive any kind of the remuneration.
- Determined in some other manner? (If yes, in which?)
  No.

36. Are detailed data on all types of remuneration and other receipts paid by the Company and its related persons to each member of the Company's Supervisory Board, including the structure of such remuneration, publicly announced? (If not, why not?) (If yes, where?)

Yes. Data on all remunerations are published in the decisions of the General Meeting. Also, total remunerations paid to the members of the Supervisory Board, Management Board, key management employees and Bank's related persons are disclosed in the Annual Report which is prepared in accordance with the International Financial Reporting Standards. The Annual report is available on the Bank's website.

37. Is each Supervisory Board member required to report to the Company on all changes in respect of his/her Company's share ownership on the following business day after such change has occurred? (If not, why not?)

This requirement is not set because Supervisory Board members do not own Bank shares.

38. State all the transactions involving Supervisory Board members or their related/associated persons, on the one hand, and the Company or its related/associated persons, on the other hand.

The Bank has not performed specific commercial transactions with the Supervisory Board members. The Bank has commercial (deposits-loans) transactions with the members of Intesa Sanpaolo Group which has a representative on the Supervisory Board. All transactions are market-based in terms and conditions. In the Annual Report, the Bank discloses a separate note on related party transactions which is prepared in accordance with the International Financial Reporting Standards. The Annual Report is available on the Bank's website.

39. Were all the transactions involving Supervisory Board members or their related/associated persons, on the one hand, and the Company or its related/associated persons, on the other hand:

- Concluded on the basis of market conditions (especially as regard to deadlines, interests rates, guarantees and similar)? (If not, why not and which?)
- Clearly stated in the Company's reports? (If not, why not and which?)
- Confirmed by the assessment of experts, independent in respect to the participants in the respective transactions? (If not, why and which?)

Refer to 38.

40. Are there contracts and agreements between the Supervisory Board members and the Company?

No.

41. Did the Supervisory Board establish an Appointment Committee? (If not, why not?)

Yes, the Executive Committee as an auxiliary body participates in appointments and dismissals of Management Board members.
If yes,

- Did the Committee estimate the composition, size, membership and work quality of the Supervisory Board and the Management Board members and make a draft of corresponding

recommendations for the Supervisory Board? (If not, why not?)
Yes.

- Did the Committee make an evaluation of the knowledge, skills and experience of the Supervisory Board members and inform the Supervisory Board thereof? (If not, why not?)
  Yes.
- Did the Committee make plans for the Supervisory Board's and Management Board's continuity? (If not, why not?)
  Yes.
- Did the Committee make an analysis of Management Board policy regarding key management employment? (If not, why not?)
  No. Management Board Policy regarding the employment is considered by Supervisory Board as part of a strategy for human resource management.

42. Did the Supervisory Board establish a Remuneration Committee?

Yes. The Executive Committee as an auxiliary body participates in the calculation of salaries for the Bank's Management Board members, which includes the fixed annual salary and the variable part (bonus).
If yes,

- Are the majority of Committee members independent members of the Supervisory Board? (If not, why not?)
  No. Refer to 31.
- Did the remuneration committee propose a remuneration policy to the Supervisory Board for Management Board members which has to include all types of remuneration, and in particular: the fixed component, the variable component depending on business performance, as well as the pension scheme and severance pay? (If not, why not?)
  Yes.
- With regard to the variable remuneration component determined by business performance, does the remuneration committee's proposal contain recommendations as to the objective performance assessment criteria? (If not, why not?)
  Yes.
- Did the remuneration committee propose remuneration for individual members of the Management Board to the Supervisory Board in accordance with the Company's remuneration policy and assessment of their individual performance? (If not, why not?)
  Yes.
- Did the committee propose to the Supervisory Board the appropriate format and content for contract of service for the Management Board members? (If not, why not?)
  No. This was not within the competence of the Executive Committee.
- Did the remuneration committee monitor the amount and structure of remuneration for key managers and give the Management Board recommendations in that regard? If not, why not?)
  Yes.
- Did the remuneration committee review a general policy of incentives for Management Board members, when those include share options or other arrangements based on share acquisition? Did it propose adequate solutions to the Supervisory Board and review the relevant information released in the annual report prior to publication? (If not, why not?)
  Yes.

43. Did the Supervisory Board establish an Audit Committee? (If not, why not?)

Yes.
If yes,

- Are the majority of the committee members independent members of the Supervisory Board? (If no, why?)
  No. Refer to 31.
- Did the committee monitor the integrity of the Company's financial information, and in particular the correctness and consistency of the accounting methods applied by the Company and the Group of which it is part, including also the criteria for consolidation of financial reports of the companies within its Group? (If not, why not?)
  Yes.
- Did the committee assess the quality of the internal control and risk management systems in place with the objective of ensuring that the main risks to which the Company is exposed (also including compliance risks) are adequately identified and disclosed, and properly managed? (If not, why not?)
  Yes.
- Did the committee undertake measures to ensure the efficiency of the internal audit system, in particular by giving recommendations concerning the selection, appointment, re-appointment and dismissal of the head of internal audit and also concerning the resources available to him/her, and by assessing action taken by the management following the findings and recommendations of the internal audit? (If not why?)
  Yes.
- If there is no internal audits function within the Company, did the committee assess the need to establish such a function? (If not, why not?)
  No. The internal audit function is established within the Bank.
- Did the committee make recommendations to the Supervisory Board regarding the selection, appointment, re-appointment or replacement of the external auditors, and also concerning the terms of engagement of the external auditors? (If not, why not?)
  Yes.
- Did the committee monitor the independence and objectivity of the external auditors, in particular as regard the rotation of chartered auditors within the audit firm and the fees paid by the Company for external audit services? (If not, why not?)
  Yes.

- Did the committee monitor the nature and amount of services other than audits provided to the Company by the external auditors or their related persons? (If not, why not?)
  Yes.
- Did the committee prepare rules regarding the services which may not be provided by external auditors or their related persons, services which may only be provided subject to ex-ante approval of the committee, and services which may be provided even without the committee's ex-ante approval? (If not, why not?)
  No. Such rules are regulated by law.
- Did the committee consider the efficiency of the external audit and the action undertaken by key management following the external auditor's recommendations? (If not, why not?)
  Yes.
- Did the committee examine the circumstances leading to the dismissal of the external auditor and give appropriate recommendations to the Supervisory Board (if the external auditors were dismissed)? (If not, why not?)
  No. Such an event did not occur.
- Does the committee have open and restriction-free communication with the Management Board and the Supervisory Board? (If not, why not?)
  Yes.
- To whom is the committee accountable?
  The Audit Committee is accountable to the Bank's Supervisory Board.
- Does the committee have open and restriction-free communication with the internal and external auditors? (If not, why not?)
  Yes.
- Did the Management Board submit to the Audit Committee:

- Timely and periodic information on financial statements and related documents prior to their public release (If not, why not?)
  Yes.

- Information on changes in accounting principles and criteria (If not, why not?)
  Yes.
- Accounting procedures adopted and applicable to the majority of transactions (If not, why not?)
  Yes.
- Information on all major differences between book and face values by individual items (If not, why not?)
  No. Such differences did not occur.
- Its entire correspondence with the internal audit department and external auditors (If not, why not?)
  Yes.

- Did the Management Board advise the Audit Committee on methods used in accounting for major and non-standard transactions and business events when they can be accounted for in different ways? (If not, why not?)
  Yes.
- Did the Audit Committee discuss with the independent auditor the issues related to:

- Changes to the existing accounting principles and criteria, (If not, why not?)
  Yes.
- Changes in the application of regulations (If not, why not?)
  Yes.
- Important estimates and conclusions in preparing financial statements (If not, why not?)
  Yes.
- Risk assessment methods and results (If not, why not?)
  Yes.
- High-risk areas of business (If not, why not?)
  Yes.
- Major deficiencies and significant weaknesses found in internal control system (If not, why)
  Yes.
- Impact of external factors (economic, legal and industrial) on financial statements and audit proce-dures? (If not, why not?)
  Yes.

- Did the Audit Committee provide high quality information by subsidiaries and affiliated companies, as also third parties (such as professional advisors)? (If not, why not?)
  Yes.

44. Was the documentation relevant for the work of the Supervisory Board submitted on time to all members? (If not, why not?)

Yes.

45. Were all decisions made at the Supervisory Board's meetings recorded in the minutes, together with voting results, also stating how individual member voted? (If not, why not?)

Yes.

46. Did the Supervisory Board prepare an assessment of its work in the preceding period including the assessment of its contribution and the competence of individual Supervisory Board members, as well as the activities of the committees and achievements compared to the target goals of the Company?

Yes.

47. State the names of the Management Board members.

Božo Prka, President;
Gabriele Pace, Deputy President;
Darko Drozdek, Member;
Ivan Gerovac, Member;
Draženko Kopljar, Member;
Dinko Lucić, Member;
Andrea Pavlović, Member.

48. Are there rules of procedure for the Management Board governing the following issues:

- Scope of activities and goals?
  Yes.
- Rules of procedure?
  Yes.
- Rules for resolving conflicts of interest?
  Yes.

- The Management Board secretariat?
  Yes.
- Meetings, adoption of decisions, agenda, preparation and content of the minutes and submission of documents?
  Yes.
- Co-operation with the Supervisory Board?
  Yes.

49. Did the company issue a statement of remuneration policy for the Management Board and the Supervisory Board as part of the annual report? (If not, why not?)

No. Although there is no formal statement concerning the Remuneration policy of Management Board and Supervisory Board, the Bank discloses aggregated information about related parties transactions as well as the amount of accrued and paid remunerations to the Bank's management in the Annual report which is prepared in accordance with the International Financial Reporting Standards. The Annual report is available on the Bank's website.

50. If there is a statement of remuneration policy does it contain the following:

- Major changes to the remuneration policy compared to previous year? (If not, why not?)
- Explanation of the relative share and importance of the fixed and variable remuneration components? (If not, why not?)
- Sufficient information on the performance criteria whose fulfilment gives the right to share options, shares or other forms of variable remuneration components? (If not, why not?)
- Sufficient information on the correlation between the remuneration amount and individual performance (If not, why not?)
- Main indicators and reasons for awarding annual bonus payments or benefits other than cash (If not, why not?)
- A brief summary of contracts of service for the members of the Management Board including information on the term of contracts, notice periods and severance pay. Any form of remuneration for the members of the management and Supervisory Boards involving share options or other rights to share acquisition, or if their remuneration is otherwise based on the Company's share price, has to be approved by the General Meeting before it becomes effective. The approval refers to the remuneration principles in general, and not to individual remuneration for the members of the management and Supervisory Boards. (If not, why not?).

51. Is the statement of remuneration policy permanently available on the Company's website? (If not, why not?)

52. Is detailed information on all types of remuneration and compensation paid to individual Management Board member disclosed in the Company's annual report? (If not, why not?)

53. Are all types of remuneration to the Management Board and the Supervisory Board members, including share options and other benefits clearly disclosed in the Company's annual report and broken down by item and person? (If not, why not?)

54. Does the statement of remunerations for the Management Board members contain the following elements for each member of the Management Board who performed the office during the year to which the statement relates:

- Total amount of monthly salary, irrespective of whether it has actually been paid or not? (If not, why not?)
- Remunerations or benefits received from associated companies? (If not, why not?)
- Remuneration in the form of profit-sharing or bonus schemes and the reasons it was paid? (If not, why not?)
- Any other additional remuneration paid to members of the Management Board for services performed by them beyond their scope of duties as management board members? (If not, why not?)
- Any compensation paid or which should have been paid to a former member of the Management Board upon termination of his/her term of office during the year to which the statement refers, (If not, why not?)
- Total estimated value of non-cash benefits considered as remuneration, not included under the above points (If not, why not?)
- When remuneration is paid in the form of shares or share options or other forms of remuneration based on share ownership: the number of options or shares awarded by the Company in the year to which the statement refers and requirements that need to be met in order to benefit from such schemes (If not, why not?)
- Number of share options exercised in the year to which the statement refers, and for each option, the number of shares and the price at which it was exercised, or the price of to be awarded to the Management Board members at year-end (If not, why not?)
  - Number of options not exercised at the end of the year, the price and date at which they can be exercised, and the main conditions pertaining to the exercise (If not, why not?)
- Each change related to the change of conditions for exercise of the existing options which occurred in the company in the year to which the statement relates (If not, why not?)
- Any loan (including outstanding debt and interest), advance payments or guarantees granted to Management Board members by subsidiaries/affiliated companies subject to consolidation. (If not, why not?)
  Refer to 49.

55. Did each member of the Management Board advise the Supervisory Board about all changes to his/her ownership of the Company's shares no later than next working day after the change occurred, with the Company's obligation to disclosure such changes as soon as possible? (If not, why not?)

No. There were no such changes during the year.

56. State all transaction which involved members of the Management Board or their related persons, on the one hand, and the Company or its related persons/entities on the other hand.

The Bank has had no specific commercial transactions with the Management Board members. The Bank has commercial (deposits-loans) transactions with the related companies through membership on the Supervisory Board of the Bank's Management Board members and key management employees. All transactions with these companies are market-based. The Bank discloses a note on related parties' transactions in the Annual Report which is prepared in accordance with the International Financial Reporting Standards. The Annual Report is available on the Bank's web site.

57. Were all transactions involving members of the Management Board or their related persons on the one hand, and the Company or its related persons, on the other hand:

- On a market basis (especially with regard to terms, interests, guarantees and similar)? (If not, why not and which?)
- Clearly stated in the Company's reports? (If not, why not and which?)
- Approved by the independent assessment of experts who are independent in relation to parties in the transaction concerned? (If not, why not and which?)

  Refer to 56.

58. Do the members of the Management Board hold a significant share in other companies which might be considered as the Company's competition? (If yes, which, where and how many?)

No.

59. Are the members of the Management Board also members of the Supervisory Boards of other companies? (If yes, state the names of these members of the Management Board, the companies in which they are the members of the Supervisory Boards, and their position in those Supervisory Boards).

Božo Prka *is a member of the Supervisory Board in the following company:*
Intesa Sanpaolo Card d.o.o. Zagreb – Zagreb, Croatia

Ivan Gerovac *is a President of the Supervisory Board in the following company:*
Unijapapir d.d. – Zagreb, Croatia

Draženko Kopljar *is a member of the Supervisory Board in the following companies:*
PBZ Card d.o.o. – Zagreb, Croatia

Dinko Lucić *is a President of the Supervisory Board in the following company:*
PBZ Stambena štedionica d.d. – Zagreb, Croatia
a Deputy President of the Supervisory Board in the following company:
PBZ Card d.o.o. – Zagreb, Croatia
and a member of the Supervisory Board in the following company:
Intesa Sanpaolo Card d.o.o. Zagreb – Zagreb, Croatia
Intesa Sanpaolo Card d.o.o. Ljubljana – Ljubljana, Slovenia

Andrea Pavlović *is a Deputy President of the Supervisory Board in the following company:*
PBZ Invest d.o.o. – Zagreb, Croatia
and a member of the Supervisory Board in the following company:
PBZ Stambena štedionica d.d. – Zagreb, Croatia

Darko Drozdek *is a President of the Supervisory Board in the following company:*
Luka Ploče d.d. – Ploče, Croatia

60. Does the Company have an external auditor (If not, why not?)

Yes.

61. Is the external auditor of the company:

- Connected with the Company in terms of ownership or interest? (If yes, state in which manner)

  No.
- Does it provide other services to the Company, either by itself or through its associated companies? (If yes, state which and how much it costs the company)

  No.

62. Do the external auditors directly inform the Company on the following (If not, why?):

- Discussion on the main accounting policy?

  Yes.
- Major weaknesses and deficiencies of the internal control system?

  Yes. The independent auditor informs the Audit Committee of the main characteristics of financial statement audit and their recommendations. During the year there were no significant weaknesses in the Bank's internal control system.
- Alternative accounting procedures?

  No, there was no need to consider alternative accounting policies.
- Non-compliance with the Management Board, risk assessment?

  No. There were no disagreements with the Management Board.
- Risk assessment, and

  Yes
- Potential analyses of fraud and/or misuse?

  Yes. The independent auditor informs

the Audit Committee of recommendations in internal controls. The independent auditor also (in line with ISA 240) obtains an understanding of how those charged with governance exercise oversight of management's processes for identifying and responding to the risks of fraud in the entity and the internal control that management has established to mitigate these risks. The auditor also makes inquiries of those charged with governance to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity.

63. Did the Company disclose the remuneration paid to the external auditors for audit and other services performed? (If not, why not?)
No. The external auditors only carried out an audit of annual financial statements at a contracted price.

64. Does the Company have an internal auditor function and internal control system? (If not, why not?)
Yes.

65. Can investors request in writing and obtain in good time all relevant information from the Management Board or from a person within the Company responsible for investor relations (If not, why not)?
Yes.

66. How many meetings did the Company's Management Board hold with investors?
The Bank has a stable shareholders structure and as a result there was no need for additional meetings with the shareholders (investors) except the General Meeting.

67. Did anybody suffer negative consequences because they reported deficiencies to the competent bodies within or outside the Company in applying the relevant regulations or ethical norms within the Company (If yes, why)?
No.

68. Do all members of the Management Board and Supervisory Board agree that, to the best of their knowledge, the answers given in this questionnaire are completely true? (If not, which Management Board members and/or Supervisory Board members disagree, why?)
Yes.


Omiš

Responsibilities of the Management and Supervisory Boards for the preparation and approval of the annual financial statements

The Management Board of the Bank is required to prepare separate and consolidated financial statements for each financial year which give a true and fair view of the financial position of the Bank and Group and of the results of their operations and cash flows, in accordance with applicable accounting standards, and is responsible for maintaining proper accounting records to enable the preparation of such financial statements at any time. It has a general responsibility for taking such steps as are reasonably available to it to safeguard the assets of the Bank and the Group and to prevent and detect fraud and other irregularities.

The Management Board is responsible for selecting suitable accounting policies to conform with applicable accounting standards and then apply them consistently; making judgements and estimates that are reasonable and prudent; and preparing the financial statements on a going concern basis unless it is inappropriate to presume that the Bank and the Group will continue in business.

The Management Board is responsible for the submission to the Supervisory Board of its annual report on the Bank and the Group together with the annual financial statements for acceptance.

If the Supervisory Board approves the annual financial statements they are deemed confirmed by the Management Board and Supervisory Board.

The separate and consolidated financial statements set out on pages 68 to 167, which have been prepared in accordance with International Financial Reporting Standards, as well as the schedules on pages 168 to 184 prepared in accordance with the Decision of the Croatian National Bank on the Structure and Content of the Annual Financial Statements of Banks, dated 30 May 2008 (Official Gazette 62/08), were authorised by the Management Board on 14 February 2013 for issue to the Supervisory Board and are signed below to signify this.

For and on behalf of Privredna banka Zagreb d.d.

Božo Prka, M.S.
President of the Management Board

Gabriele Pace
Vice President of the Management Board

26 March 2013

Independent auditors' report

Independent auditors' report to the shareholders of Privredna banka Zagreb d.d.

We have audited the accompanying separate financial statements of Privredna banka Zagreb d.d. ("the Bank") and consolidated financial statements of Privredna banka Zagreb Group ("the Group"), which comprise the statements of financial position as at 31 December 2012, the income statements, statements of comprehensive income, statements of changes in equity and statements of cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Separate and Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these separate and consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of separate and consolidated 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 separate and consolidated 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 separate and consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the separate and consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the separate and consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Bank's and Group's preparation and fair presentation of the separate and consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's and Group'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 separate and consolidated financial statements.

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

KPMG

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Bank and the Group as at 31 December 2012 and of their financial performance and their cash flows for the year then ended in accordance with International Financial Reporting Standards.

Other legal and regulatory requirements

Pursuant to the Decision of the Croatian National Bank on the Structure and Content of the Annual Financial Statements of Banks, dated 30 May 2008 (Official Gazette 62/08), the Management Board of the Bank has prepared the schedules set out on pages 168 to 184 ("the Schedules"), which comprise an alternative presentation of the statements of financial position as of 31 December 2012, and of the income statements, statements of changes in equity and statements of cash flows for the year then ended, and a reconciliation ("the Reconciliation") of the Schedules with the financial statements as presented on pages 168 to 184. The Management Board of the Bank is responsible for the Schedules and the Reconciliation. The financial information in the Schedules is derived from the financial statements of the Bank and the Group set out on pages 68 to 167 on which we have expressed an opinion as set out above.

Other Matter

The separate and consolidated financial statements of the Bank and the Group as at and for the year ended 31 December 2011 were audited by other auditors whose report dated 26 March 2012 expressed an unmodified opinion on those financial statements.

For and on behalf of KPMG Croatia d.o.o. za reviziju: Zagreb, 26 March 2013

KPMG Croatia
d.o.o. za reviziju
Eurotower, 17. kat
Ivana Lučića 2a, 10000 Zagreb

Goran Horvat
Director, Croatian Certified Auditor

KPMG *Croatia d.o.o. za reviziju*
Croatian Certified Auditors
Eurotower, 17th floor
Ivana Lučića 2a
10000 Zagreb
Croatia

Financial statements of the Bank and the Group

Income statement

	NOTES		GROUP		BANK
For the year ended 31 December		2012	2011	2012	2011
(in HRK million)					
Interest income	5	3,850	3,935	3,550	3,599
Interest expense	5	(1,444)	(1,455)	(1,337)	(1,331)
Net interest income		**2,406**	**2,480**	**2,213**	**2,268**
Fee and commission income	6a	1,353	1,352	623	624
Fee and commission expense	6b	(263)	(240)	(117)	(114)
Net fee and commission income		**1,090**	**1,112**	**506**	**510**
Dividend income	7	3	4	143	179
Net trading income and net loss on translation of monetary assets and liabilities	8	143	146	136	144
Other operating income	9	119	132	37	45
Revenue		**3,761**	**3,874**	**3,035**	**3,146**
Personnel expenses	10a	(724)	(770)	(610)	(655)
Impairment losses on loans and advances to customers	19c	(543)	(316)	(560)	(296)
Other impairment losses and provisions	11	(46)	(53)	(43)	(57)
Depreciation and amortisation	12	(191)	(213)	(124)	(141)
Other operating expenses	10b	(1,001)	(959)	(670)	(621)
Share of profits from associates	22	16	18	-	-
Profit before income tax		**1,272**	**1,581**	**1,028**	**1,376**
Income tax expense	13	(258)	(313)	(182)	(240)
Profit for the year		**1,014**	**1,268**	**846**	**1,136**
Attributable to:					
Equity holders of the parent		1,014	1,268	846	1,136
		1,014	**1,268**	**846**	**1,136**
		in HRK			
Basic and diluted earnings per share	49	53.3	66.7		

The accompanying accounting policies and notes on pages 76 to 167 are an integral part of these financial statements.

Statement of comprehensive income

	GROUP		BANK	
For the year ended 31 December	2012	2011	2012	2011
(in HRK million)				
Profit for the year	**1,014**	**1,268**	**846**	**1,136**
Other comprehensive income				
Net change in fair value on available-for-sale financial assets	3	(19)	(8)	(14)
Net amount transferred to the income statement	23	46	13	30
	26	**27**	**5**	**16**
Deferred tax on available-for-sale financial assets (Note 13d)	(5)	(6)	(1)	(3)
Other comprehensive income for the year, net of tax	**21**	**21**	**4**	**13**
Total comprehensive income for the year, net of tax	**1,035**	**1,289**	**850**	**1,149**
Attributable to:				
Equity holders of the parent	1,035	1,289	850	1,149
	1,035	**1,289**	**850**	**1,149**

The accompanying accounting policies and notes on pages 76 to 167 are an integral part of these financial statements.

Statement of financial position

	NOTES		GROUP		BANK
As at 31 December		2012	2011	2012	2011
Assets (in HRK million)					
Cash and current accounts with banks	14	4,171	2,647	4,168	2,465
Balances with the Croatian National Bank	15	5,657	6,989	5,657	6,757
Financial assets at fair value through profit or loss	16	3,986	2,497	3,927	2,497
Derivative financial assets	17	4	11	4	11
Loans and advances to banks	18	6,250	7,036	6,236	7,231
Loans and advances to customers	19	49,960	51,398	46,918	46,691
Financial assets available for sale	20	91	985	81	189
Held-to-maturity investments	21	208	391	-	124
Investments in subsidiaries and associates	22	151	135	220	389
Intangible assets	23	162	157	103	83
Property and equipment	24	1,254	1,204	700	683
Investment property	25	9	12	9	9
Non-current assets held for sale	26	-	30	-	30
Deferred tax assets	13c	177	171	132	118
Other assets	27	474	491	256	204
Total assets		**72,554**	**74,154**	**68,411**	**67,481**

The accompanying accounting policies and notes on pages 76 to 167 are an integral part of these financial statements.

Statement of financial position / continued

	NOTES	GROUP		BANK	
As at 31 December		2012	2011	2012	2011
Liabilities (in HRK million)					
Current accounts and deposits from banks	28	727	2,994	1,108	3,423
Current accounts and deposits from customers	29	48,143	47,431	46,973	44,081
Derivative financial liabilities	17	4	9	4	9
Interest-bearing borrowings	30	8,936	9,311	7,918	7,990
Other liabilities	31	1,518	1,633	394	461
Accrued expenses and deferred income	32	201	194	81	74
Provisions for liabilities and charges	33	204	191	204	186
Current tax liability		33	69	3	63
Total liabilities		**59,766**	**61,832**	**56,685**	**56,287**
Equity attributable to equity holders of the parent					
Share capital	35a	1,907	1,907	1,907	1,907
Share premium	35b	1,570	1,570	1,570	1,570
Treasury shares	35c	(76)	(76)	(76)	(76)
Other reserves	35d	375	375	308	300
Fair value reserve	35e	(27)	(48)	(8)	(11)
Retained earnings	35f	9,039	8,594	8,025	7,504
Total equity		**12,788**	**12,322**	**11,726**	**11,194**
Total liabilities and equity		**72,554**	**74,154**	**68,411**	**67,481**

The accompanying accounting policies and notes on pages 76 to 167 are an integral part of these financial statements.

Statement of cash flows

For the year ended 31 December	NOTES	GROUP 2012	GROUP 2011	BANK 2012	BANK 2011
(in HRK million)					
Cash flows from operating activities					
Profit before income tax		1,272	1,581	1,028	1,376
Impairment losses on loans and advances to customers	19c	543	316	560	296
Other impairment losses and provisions	11	46	53	43	57
Gain on disposal of property and equipment	9	(5)	(17)	(1)	(15)
Depreciation and amortisation	12	191	213	124	141
Net losses/(gains) from securities initially designated at fair value through profit or loss	8	54	(2)	56	(2)
Share of profits from associates	22	(16)	(18)	-	-
Net interest income	5	(2,406)	(2,480)	(2,213)	(2,268)
Dividend income	7	(3)	(4)	(143)	(179)
		(324)	**(358)**	**(546)**	**(594)**
Decrease/(increase) in operating assets					
Balances with the Croatian National Bank		322	398	715	(387)
Loans and advances to banks		(635)	(94)	(131)	(382)
Loans and advances to customers		1,210	(3,056)	617	(2,556)
Financial assets held for trading and financial assets available for sale		(655)	838	(1,398)	920
Other assets		44	(102)	36	(33)
Decrease/(increase) in operating assets		*286*	*(2,016)*	*(161)*	*(2,438)*
Increase/(decrease) in operating liabilities					
Current accounts and deposits from banks		(2,267)	(1,157)	(2,319)	(773)
Current accounts and deposits from customers		780	621	615	565
Other liabilities		(120)	166	(100)	25
Decrease in operating liabilities		*(1,607)*	*(370)*	*(1,804)*	*(183)*
Interest received		3,536	3,833	3,409	3,687
Interest paid		(1,512)	(1,699)	(1,412)	(1,417)
Dividends received		3	4	143	179
Net cash inflow/(outflow) from operating activities before income taxes paid		**382**	**(606)**	**(371)**	**(766)**
Income tax paid		(305)	(288)	(254)	(188)
Net cash from/(used in) operating activities		**77**	**(894)**	**(625)**	**(954)**

The accompanying accounting policies and notes on pages 76 to 167 are an integral part of these financial statements.

Statement of cash flows / continued

	NOTES	GROUP		BANK	
For the year ended 31 December		2012	2011	2012	2011
(in HRK million)					
Cash flows from investing activities					
Purchase of property and equipment and intangible assets	23, 24	(411)	(303)	(124)	(88)
Disposal of property and equipment and intangible assets		173	89	2	17
Redemption of held-to-maturity investments		183	256	124	257
Net cash (used in)/from investing activities		**(55)**	**42**	**2**	**186**
Cash flows from financing activities					
Dividends paid to equity holders of the parent		(569)	(301)	(569)	(301)
Decrease in interest-bearing borrowings		(375)	(578)	(180)	(441)
Net cash used in financing activities		**(944)**	**(879)**	**(749)**	**(742)**
Cash and cash equivalents acquired on merger of Međimurska banka		-	-	894	-
Net decrease in cash and cash equivalents		**(922)**	**(1,731)**	**(478)**	**(1,510)**
Cash and cash equivalents as at 1 January	36	11,024	12,779	10,588	12,122
Effect of exchange rate fluctuations on cash held		5	(24)	5	(24)
Cash and cash equivalents as at 31 December	**36**	**10,107**	**11,024**	**10,115**	**10,588**

The accompanying accounting policies and notes on pages 76 to 167 are an integral part of these financial statements.

Statement of changes in equity

(in HRK million)	Share capital	Share premium	Treasury shares	Other reserves	Fair value reserve	Retained earnings	Total
Group							
Balance as at 1 January 2012	**1,907**	**1,570**	**(76)**	**375**	**(48)**	**8,594**	**12,322**
Other comprehensive income							
Net change in fair value on available-for-sale financial assets	-	-	-	-	3	-	**3**
Net amount transferred to the income statement	-	-	-	-	23	-	**23**
Deferred tax on available-for-sale financial assets (Note 13d)	-	-	-	-	(5)	-	**(5)**
Total other comprehensive income	-	-	-	-	**21**	-	**21**
Profit for the year	-	-	-	-	-	1,014	**1,014**
Total comprehensive income for the year	-	-	-	-	**21**	**1,014**	**1,035**
Dividends paid	-	-	-	-		(569)	(569)
Transactions with owners, recorded directly in equity	**-**	**-**	**-**	**-**		**(569)**	**(569)**
Balance as at 31 December 2012	**1,907**	**1,570**	**(76)**	**375**	**(27)**	**9,039**	**12,788**
Balance as at 1 January 2011	**1,907**	**1,570**	**(76)**	**373**	**(69)**	**7,629**	**11,334**
Other comprehensive income							
Net change in fair value on available-for-sale financial assets	-	-	-	-	(19)	-	(19)
Net amount transferred to the income statement	-	-	-	-	46	-	46
Deferred tax on available-for-sale financial assets (Note 13d)	-	-	-	-	(6)	-	(6)
Total other comprehensive income	**-**	**-**	**-**	**-**	**21**	**-**	**21**
Profit for the year	-	-	-	-	-	1,268	**1,268**
Total comprehensive income for the year	**-**	**-**	**-**	**-**	**21**	**1,268**	**1,289**
Dividends paid	-	-	-	-	-	(301)	**(301)**
Other movements	-	-	-	2	-	(2)	-
Transactions with owners, recorded directly in equity	-	-	-	**2**	-	**(303)**	**(301)**
Balance as at 31 December 2011	**1,907**	**1,570**	**(76)**	**375**	**(48)**	**8,594**	**12,322**

The accompanying accounting policies and notes on pages 76 to 167 are an integral part of these financial statements.

Statement of changes in equity / continued

(in HRK million)	Share capital	Share premium	Treasury shares	Other reserves	Fair value reserve	Retained earnings	Total
Bank							
Balance as at 1 January 2012	**1,907**	**1,570**	**(76)**	**300**	**(11)**	**7,504**	**11,194**
Acquired on merger with Međimurska banka (Note 22)	-	-	-	8	(1)	244	**251**
Other comprehensive income							
Net change in fair value on available-for-sale financial assets	-	-	-	-	(8)	-	**(8)**
Net amount transferred to the income statement	-	-	-	-	13	-	**13**
Deferred tax on available-for-sale financial assets (Note 13d)	-	-	-	-	(1)	-	**(1)**
Total other comprehensive income	**-**	**-**	**-**	**-**	**4**	**-**	**4**
Profit for the year	-	-	-	-	-	846	**846**
Total comprehensive income for the year	**-**	**-**	**-**	**-**	**4**	**846**	**850**
Dividends paid	-	-	-	-	-	(569)	**(569)**
Transactions with owners, recorded directly in equity	**-**	**-**	**-**	**-**	**-**	**(569)**	**(569)**
Balance as at 31 December 2012	**1,907**	**1,570**	**(76)**	**308**	**(8)**	**8,025**	**11,726**
Balance as at 1 January 2011	**1,907**	**1,570**	**(76)**	**300**	**(24)**	**6,669**	**10,346**
Other comprehensive income							
Net change in fair value on available-for-sale financial assets	-	-	-	-	(14)	-	**(14)**
Net amount transferred to the income statement	-	-	-	-	30	-	**30**
Deferred tax on available-for-sale financial assets (Note 13d)	-	-	-	-	(3)	-	**(3)**
Total other comprehensive income	**-**	**-**	**-**	**-**	**13**	**-**	**13**
Profit for the year	-	-	-	-	-	1,136	**1,136**
Total comprehensive income for the year	**-**	**-**	**-**	**-**	**13**	**1,136**	**1,149**
Dividends paid	-	-	-	-	-	(301)	**(301)**
Transactions with owners, recorded directly in equity	**-**	**-**	**-**	**-**	**-**	**(301)**	**(301)**
Balance as at 31 December 2011	**1,907**	**1,570**	**(76)**	**300**	**(11)**	**7,504**	**11,194**

The accompanying accounting policies and notes on pages 76 to 167 are an integral part of these financial statements.

Notes to the financial statements

1 | Reporting entity

Privredna banka Zagreb d.d. ("the Bank") is a joint stock company incorporated and domiciled in the Republic of Croatia. The registered office is at Račkoga 6, Zagreb. The Bank is the parent of the Privredna banka Zagreb Group ("the Group"), which has operations in the Republic of Croatia. The Group provides a full range of retail and corporate banking services, as well as treasury, investment banking, asset management and leasing services.

These financial statements comprise both the separate and the consolidated financial statements of the Bank as defined in International Accounting Standard 27 Consolidated and Separate Financial Statements.

A summary of the Group's principal accounting policies are set out below.

2 | Basis of preparation

a) Statement of compliance

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

These separate and consolidated financial statements were authorised for issue by the Management Board on 14 February 2013 for approval by the Supervisory Board.

b) Basis of measurement

The separate and consolidated financial statements are prepared on the fair value basis for financial assets and liabilities at fair value through profit or loss and financial assets available for sale, except those for which a reliable measure of fair value is not available. Other financial assets and liabilities, and non-financial assets and liabilities, are stated at amortised or historical cost.

c) Functional and presentation currency

The separate and consolidated financial statements are presented in Croatian kuna ("HRK") which is the functional and presentation currency of the Bank and the Group. Amounts are rounded to the nearest million, unless otherwise stated.

The exchange rates used for translation at 31 December 2012 amounted to EUR 1 = HRK 7.546, CHF 1= HRK 6.245 and USD 1 = HRK 5.727 (31 December 2011: EUR 1 = HRK 7.530, CHF 1= HRK 6.195 and USD 1 = HRK 5.820).

d) Use of estimates and judgements

The preparation of financial statements in conformity with International Financial Reporting Standards requires management to make judgments, estimates and assumptions that affect the application of accounting policies and reported amounts of assets, liabilities and disclosure of commitments and contingencies at the reporting date, as well as amounts of income and expense for the period and other comprehensive income. Actual results may differ from these estimates.

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

Information about judgments made by management in the application of IFRS that have a significant effect on the financial statements and information about estimates with a significant risk of resulting in a material adjustment in the next financial year are included in Note 4.

e) Legal merger of Međimurska banka

The structure of the Group was changed following a Group reorganisation effective from 1 December 2012 whereby Međimurska banka (100% owned by Privredna banka Zagreb d.d.) was legally merged into the Bank and ceased to exist as a separate legal and operational entity. The Bank's income statement for 2012 does not include the results of Međimurska banka prior to the merger nor has the comparative information been restated to include Međimurska banka.

The assets and liabilities acquired as a result of the merger are recognised at the carrying amounts recognised immediately before the merger in the financial statements of Međimurska banka. The assets, liabilities and equity assumed on the merger are summarised in Note 22.

f) Financial crisis impact

The situation in global financial markets and impact on Croatia

The recession that began in 2007-2008 continued to have a strong impact on economic and financial variables in 2012 on global markets including Croatia. The crisis was especially strong in Europe where the sovereign debt crisis together with problems in the banking system forced European policymakers to introduce new measures which included: creation of the European Stability Mechanism, development of the banking union, the European Central Bank's ("ECB") second long-term refinancing operation (which injected much needed liquidity into European banks) and introduction of outright monetary transactions as part of ECB's policies. A number of other measures were also introduced which led to lower perception of risk for the Eurozone by the year-end in comparison to the first part of 2012. Although, the uncertainties entailing the Eurozone started to recede in the second part of the year, they have not been completely dismissed.

This financial turmoil had an impact on the Croatian economy and financial system. Risk premium for Croatia decreased towards the end of the year, but so did banks' statements of financial position. The process of deleveraging by parent companies occurred in Croatia but was not prominent. During 2012, deleveraging by parent companies did not hinder loan growth because demand for loans subsided and domestic deposits continued to grow, which was mostly influenced by retail deposits. Both corporate and retail demand for loans was at a low level, which was not surprising given the long lasting crisis in Croatia and the negative impact on economic subjects in the country. Deleveraging by parent companies did not have a negative impact on the liquidity of the Group, which was very high throughout the year. All this resulted in significantly low interest rates on money market and Government T-bills. Again, this was due to low credit activity among banks.

Households deleveraged as well, with total debt towards banks decreasing for the first time since 2009. The total debt of all sectors, as a share of GDP, continued to decline, which was supported by a fall in GDP by 1.8% in real terms. High unemployment, falling real wages, together with negative forecasts for Croatia and Europe resulted in lower consumer confidence indexes and consequently virtually no demand for new loans, especially mortgages and other types of long-term loans (apart from cash loans).

Corporate demand for loans was somewhat better, but the international and domestic crisis left its impact on this sector as well. The corporate sector decreased its international debt exposure while domestic funding increased slightly. As a result, total debt of the corporate sector as a share in GDP stagnated.

Non-performing loans continued to increase in 2012, which was expected given the long lasting crisis and effectively no increase in loan growth. The Group pays significant attention to the management of credit risk and the ratio of impairment allowances. As a result, a decrease in lending interest rates was either smaller than could have otherwise been expected or nonexistent (regardless of the falling costs of borrowing abroad).

Croatia has a number of problems and it is difficult to expect a strong rebound in the economy as long as the international financial crisis (especially in the EU and eurozone) continues to influence the economy and financial system.

3 | Significant accounting policies

a) Basis of consolidation

i) Business combinations
Business combinations are accounted for using the acquisition method as at the acquisition date, which is the date on which control is transferred to the Group. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, the Group takes into consideration potential voting rights that are currently exercisable.

Acquisitions on or after 1 January 2010

The Group measures goodwill at the acquisition date as:
- the fair value of the consideration transferred; plus
- the recognised amount of any non-controlling interests in the acquiree; plus
- if the business combination is achieved in stages, the fair value of the pre-existing equity interest in the acquiree; less
- the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed.

When the total is negative, a bargain purchase gain is recognised immediately in profit or loss.
The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognised in profit or loss.
Transaction costs related to the acquisition, other than those associated with the issue of debt or equity securities, that the Group incurs in connection with a business combination are expensed as incurred.
Any contingent consideration payable is recognised at fair value at the acquisition date. If the contingent consideration is classified as equity, it is not remeasured and settlement is accounted for within equity. Otherwise, subsequent changes to the fair value of the contingent consideration are recognised in the income statement.

Notes to the financial statements

Acquisitions prior to 1 January 2010

For acquisitions prior to 1 January 2010, goodwill represents the excess of the cost of the acquisition over the Group's interest in the recognised amount (generally fair value) of the identifiable assets, liabilities and contingent liabilities of the acquiree. When the excess was negative, a bargain purchase gain was recognised immediately in the income statement.
Transaction costs, other than those associated with the issue of debt or equity securities, that the Group incurred in connection with business combinations were capitalised as part of the cost of the acquisitions.

ii) Non-controlling interests
Non-controlling interests in the net assets (excluding goodwill) of the consolidated subsidiaries are identified separately from the Group's equity therein. For each business combination, the Group elects to measure any non-controlling interests in the acquiree either at fair value or at their proportionate share of the acquiree's identifiable net assets, which are generally at fair value.
Changes in the Group's interest in a subsidiary that do not result in a loss of control are accounted for as transactions with owners in their capacity as owners. Adjustments to non-controlling interests are based on a proportionate amount of the net assets of the subsidiary. No adjustments are made to goodwill and no gain is recognised in the income statement.

iii) Subsidiaries
Financial statements are prepared for the Bank and the Group. Financial statements of the Group include consolidated financial statements of the Bank and its entities under control (subsidiaries). In the Bank's separate financial statements investments in subsidiaries are accounted for at cost less impairment.
Subsidiaries are consolidated from the date on which effective control is transferred to the Group and are no longer consolidated from the date of disposal. All intercompany transactions, balances and unrealised surpluses and deficits on transactions between group companies have been eliminated. Where necessary, the accounting policies used by subsidiaries have been changed to ensure consistency with the policies adopted by the Group.
Losses applicable to the non-controlling interests in a subsidiary are allocated to the non-controlling interests even if doing so causes the non-controlling interests to have a deficit balance.

iv) Associates
Associates are entities over which the Group has significant influence but no control. Investments in associates are accounted for using the equity method of accounting in the consolidated financial statements and are initially recognised at cost. The Group's investments in associates include goodwill (net of any accumulated impairment loss) identified on acquisition. In the Bank's separate financial statements investments in associates are accounted at cost less impairment.
The Group's share of its associates' post-acquisition gains or losses is recognised in the income statement and its share of their post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise any further losses, unless it has incurred obligations or made payments on behalf of the associate.
Dividends received from associates are treated as a decrease of investment in associate in the Group's consolidated statement of financial position and as a dividend income in the Bank's unconsolidated income statement.
Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associate. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the assets transferred. The accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

v) Acquisition of entities under common control
Business combinations arising from transfers of interests in entities that are under the control of the shareholder that ultimately controls the Group are accounted for using book value accounting at the date of acquisition, the income statement does not include the results prior to the merger and the comparatives are not restated. The assets and liabilities acquired are recognised at the carrying amounts recognised previously in the financial statements of the acquired entities. The components of equity of the acquired entities are added to the same components within Group equity except for issued capital and pre-acquisition profits of the acquired entities.

vi) Loss of control
Upon the loss of control, the Group derecognises the assets and liabilities of the subsidiary, any non-controlling interest and other components of equity related to the subsidiary. Any surplus or deficit arising on the loss of control is recognised in the income statement. If the Group retains any interest in the previous subsidiary, then such interest is measured at fair value at the date that control is lost. Subsequently it is accounted for as an equity-accounted investee or in accordance with the Group's accounting policy for financial instruments (refer to accounting policy 3 l Financial instruments) depending on the level of influence retained.

vii) Transactions eliminated on consolidation
Intra-group balances, and income and expenses (except for foreign currency transaction gains or losses) arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

viii) Fund management
The Group manages and administers assets held in mutual funds on behalf of investors. The financial statements of these entities are not included in these consolidated financial statements except when the Group controls the entity (there were no such cases at the reporting date). Information about the Group's fund management activities is set out in Note 37.

b) Foreign currency translation
Transactions in foreign currencies are translated into the respective functional currencies of the operations at the spot exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated into the functional currency at the mid market exchange rate of the Croatian National Bank. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated into the functional currency at the spot exchange rate at the date that the fair value was determined.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Foreign currency differences arising on translation are recognised in the income statement, except for differences arising on the translation of available-for-sale equity instruments, which are recognised in other comprehensive income.

Changes in the fair value of securities denominated in foreign currency classified as available for sale are analysed between translation differences resulting from changes in the amortised cost of the security and other changes in the carrying amount of the security. Translation differences on monetary securities available for sale are recognised in profit or loss, and other changes in carrying amount are recognised in other comprehensive income. Translation differences on non-monetary securities denominated in foreign currency classified as available for sale are recognised directly in other comprehensive income along with other changes, net of deferred tax. The Group does not have qualifying cash flow hedges and qualifying net investment hedges as defined in International Accounting Standard 39 *Financial Instruments: Measurement and Recognition* ("IAS 39").

The Group has receivables and liabilities originating in HRK, which are linked to foreign currencies with a one-way currency clause (disclosed as other embedded derivatives in Note 17). Due to this clause, the Group has an option to revalue the asset by the higher of the foreign exchange rate valid as of the date of repayments of the receivables by the debtors, or the foreign exchange rate valid as of the date of origination of the financial instrument. In case of a liability linked to this clause, the counterparty has this option. Due to the specific conditions of the market in the Republic of Croatia, the fair value of this option cannot be calculated given forward rates for Croatian kuna for periods over 9 months are generally not available. As such, the Group revalues its receivables and liabilities linked to this clause by the agreed reference rate valid at the reporting date or foreign exchange rate agreed through the option (rate valid at origination), whichever is higher.

c) Interest income and expense
Interest income and expense are recognised in the income statement as they occur for all interest-bearing financial instruments, including those measured at amortised cost and those available for sale, using the effective interest rate method. The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that discounts estimated future cash payments or receipts over the expected life of the financial instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate for its assets, the Group does not consider future credit losses. The calculation includes all fees and percentage points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts. Such income and expense is presented as interest income or interest expense in the income statement.

Interest income and expense also include fee and commission income and expense in respect of loans and advances to customers and banks, interest-bearing borrowings, finance and operating leases, premium or discount amortisation as well as other differences between the initial carrying amount of an interest-bearing financial instrument and its value at maturity, recognised on an effective interest basis.
Interest income on debt securities at fair value through profit or loss is recognised using the nominal coupon rate and included in interest income.

d) Fee and commission income and expense
Loan commitment fees for loans and advances that are likely to be drawn down are deferred and recognised as an adjustment to the effective interest rate on the loan. Commitment fees in relation to facilities that are not likely to be drawn down are recognised over the term of the commitment.

Fee and commission income and expense mainly comprise fees and commissions related to domestic and foreign payments, the issue of guarantees and letters of credit, credit card business and asset management, and are recognised in the income statement upon performance of the relevant service, unless they have been included in the effective interest calculation.
Loan syndication fees are recognised as revenue when the syndication has been completed and the Group has retained no part for itself, or has retained a part at the same effective interest rate as the other participants. Portfolio and other management advisory

and service fees are recognised based on the applicable service contracts. Asset management fees related to investment fund management are recognised on an accruals basis over the period in which the service is provided. The same principle is applied for custody services that are continuously provided over an extended period of time.

e) Net trading income and net loss on translation of monetary assets and liabilities

Net trading income and net loss on translation of monetary assets and liabilities include foreign exchange trading gains, realised and unrealised gains on securities at fair value through profit or loss and net loss from the translation of monetary assets and liabilities denominated in foreign currency.

f) Other operating income

Other operating income includes net gains on securities classified as assets available for sale, net gains on disposal of property and equipment, rental income from investment property and assets under operating lease and other income.
Rental income from operating leases is recognised on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased assets and recognised on a straight-line basis over the lease term.

g) Employee benefits

Employee entitlements to annual leave are recognised when they accrue. A provision is made for the estimated liability for annual leave as a result of services rendered by employees up to the reporting date.

i) Personnel social contributions

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

	from 1 May 2012	up to 1 May 2012
Contributions to the Pension Fund	20.00%	20.00%
Contributions to the State Health Care Fund	13.00%	15.00%
Contributions to the Unemployment Fund	1.70%	1.70%
Injuries at work	0.50%	0.50%

The Group is also obliged to withhold contributions from the gross salary on behalf of the employee for the same funds. The Group has no further payment obligations once the contributions have been paid. The contributions are recognised as employee benefits in the income statement as they accrue.

ii) Termination benefits

Termination benefits are recognised as an expense when the Group is committed demonstrably, without realistic possibility of withdrawal, to a formal detailed plan either to terminate employment before the normal retirement date, or to provide termination benefits as a result of an offer made to encourage voluntary redundancy. Termination benefits for voluntary redundancies are recognised if the Group has made an offer of voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably. If benefits are payable more than 12 months after the reporting date, then they are discounted to their present value.

iii) Short-term employee benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

iv) Share-based payment transactions

The Group has a share-based payment agreement which entitle the key employees to receive the cash payment, based on price of the equity instrument (cash-settled transactions). The liability is initially measured by reference to the fair value of equity instruments at the grant date and remeasured until settlement. The fair value is determined as the market value of shares. The cost of cash-settled transactions is recognised over the period in which the performance and/or service conditions are fulfilled (refer to Note 39).

h) Direct acquisition costs related to housing savings

Direct acquisition expenses related to housing savings contracts are deferred, to the extent that they are estimated to be recoverable, and amortised to the income statement on a straight-line basis over the life of the related contracts.

i) Dividend income

Dividend income on equity securities is credited to the income statement when the right to receive the dividend is established except for dividend income from associates which is on consolidation credited to the carrying values of investments in associates in the Group's statement of financial position.

j) Income tax

The income tax charge comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in other comprehensive income, in which case it is recognised in other comprehensive income.

i) Current income tax
Current tax is the expected tax payable on the taxable income for the year, using the tax rates enacted or substantially enacted at the reporting date, and any adjustments to tax payable in respect of previous years.

ii) Deferred income tax
Deferred taxes are calculated by using the balance sheet liability method. Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The measurement of deferred tax assets and liabilities reflects the tax consequences that would follow from the manner in which the enterprise expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities, based on tax rates enacted or substantially enacted at the reporting date.
Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.
Deferred tax assets and liabilities are not discounted and are classified as non-current and/or long-term assets in the statement of financial position. Deferred tax assets are recognised only to the extent that it is probable that sufficient taxable profits will be available against which the deferred tax assets can be utilised. At each reporting date, the Group reassesses unrecognised potential deferred tax assets and the carrying amount of recognised deferred tax assets.
Additional income taxes that arise from the distribution of dividends are recognised at the same time as the liability to pay the related dividend.

k) Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise balances with remaining maturity of less than 90 days, including cash and current accounts with banks and loans and advances to banks up to 90 days.

l) Financial instruments

i) Recognition
The Group initially recognises loans and advances and other financial liabilities on the date at which they are originated, i.e. advanced to borrowers or received from lenders.
Regular way transactions with financial instruments are recognised at the date when they are transferred (settlement date). Under settlement date accounting, while the underlying asset or liability is not recognised until the settlement date, changes in fair value of the underlying asset or liability are recognised starting from the trade date. All other financial assets and liabilities (derivatives) are recognised on the trade date at which the Group becomes a party to the contractual provisions of the instrument.

ii) Classification
Financial instruments are classified in categories depending on the purpose for which the Group initially acquired the financial instrument or upon reclassification and in accordance with the Group's investment strategy. Financial assets and financial liabilities are classified in the following portfolios: "at fair value through profit or loss"; "held to maturity"; "available for sale"; or "loans and receivables" and "other financial liabilities". The main difference between the portfolios relates to the measurement of financial assets and the recognition of their fair values in the financial statements as described below.

Financial assets and financial liabilities at fair value through profit or loss
This category has two sub-categories: financial instruments held for trading (including derivatives), and those designated by management as at fair value through profit or loss at inception. A financial instrument is classified in this category if it is acquired or incurred principally for the purpose of selling or repurchasing it in the short term, for the purpose of short-term profit-taking, or designated as such by management.

The Group designates financial assets and liabilities at fair value through profit or loss when:

- the assets or liabilities are managed, evaluated and reported internally on a fair value basis;
- the designation eliminates or significantly reduces an accounting mismatch which would otherwise arise; or
- the asset or liability contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

Financial instruments at fair value through profit or loss include debt and equity securities and units in investment funds, as well as derivatives.

Held-to-maturity investments
Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Group has the positive intention and ability to hold to maturity. Held-to-maturity investments comprise debt securities.

Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market other than:
(a) those that the Group intends to sell immediately or in the near term, which shall be classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss;
(b) those that the Group upon initial recognition designates as available for sale; or
(c) those for which the Group may not recover substantially all of the initial investment, other than because of credit deterioration, which shall be classified as available for sale.

Loans and receivables include loans and advances to banks, loans and advances to customers, finance lease receivables, receivables from operating leases, obligatory reserve with the Croatian National Bank and trade and other receivables.

Available-for-sale financial assets
Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. Financial assets designated as available for sale are intended to be held for an indefinite period of time, but may be sold in response to needs for liquidity or changes in interest rates, foreign exchange rates, or equity prices. Available-for-sale financial assets include debt and equity securities.

Other financial liabilities
Other financial liabilities comprise all financial liabilities which are not held for trading or designated at fair value through profit or loss.

iii) Derecognition
The Group derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Group neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. Any interest in transferred financial assets, that qualify for derecognition that is created or retained by the Group is recognised as a separate asset or liability in the statement of financial position. On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset transferred), and consideration received (including any new asset obtained less any new liability assumed) is recognised in the income statement. In addition, any cumulative gain or loss that had been recognised in other comprehensive income is also recognised in the income statement.
In transactions in which the Group neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset and it retains control over the asset, the Group continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset. If transfer does not result in derecognition because the Group retained all or substantially all risks and rewards of ownership, the assets are not derecognised and liabilities secured with collateral are recognised in the amount of consideration received.
The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or expire. If the terms of a financial liability are significantly modified, the Group will cease recognising that liability and will instantaneously recognise a new financial liability, with new terms and conditions.
Realised gains and losses from the disposal of financial instruments are calculated using the weighted average cost method.

iv) Reclassification
No transfers of derivatives and financial instruments initially designated as at fair value through profit and loss are allowed to other portfolios. Financial assets held for trading may be reclassified from this category in the case when both of the following two conditions are met: a change in the intended purpose of the assets and an extraordinary event. In such case, the fair value at the reclassification date becomes the new cost/amortised cost. Reclassification is possible to the available-for-sale portfolio, the held-to-maturity portfolio and the loans and receivables portfolio.
Transfers from other portfolios to the portfolio at fair value through profit and loss are not possible.

v) Offsetting of financial instruments
Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.
Income and expenses are presented on a net basis only when permitted by the accounting regulations, or for gains and losses arising from a group of similar transactions such as in the Group's trading activity.

vi) Initial and subsequent measurement
When a financial asset or financial liability is recognised initially, the Group measures it at its fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs which are directly attributable to the acquisition or issue of the financial asset or financial liability. Financial assets at fair value through profit or loss are initially recognised at fair value, and transaction costs are immediately charged to the income statement.
After initial recognition, the Group measures financial instruments at fair value through profit or loss and available for sale at their fair value, without any deduction for selling costs. Equity instruments classified as available for sale that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are stated at cost less impairment.
Loans and receivables, held-to-maturity investments and other financial liabilities are measured at amortised cost (less any impairment for the assets) using the effective interest method.

vii) Gains and losses
Gains and losses arising from a change in the fair value of financial assets or financial liabilities at fair value through profit or loss are recognised in the income statement.
Gains and losses from a change in the fair value of available-for-sale financial assets are recognised directly in a fair value reserve in other comprehensive income, net of deferred tax, and are disclosed in the statement of changes in equity. Impairment losses, foreign exchange gains and losses, interest income and amortisation of premium or discount using the effective interest method on available-for-sale monetary assets are recognised in the income statement. Impairment losses on non-monetary available-for-sale assets are also recognised in the income statement. Foreign exchange differences on non-monetary financial assets available for sale are recognised in other comprehensive income, net of deferred tax. Dividend income is recognised in the income statement.
Upon sale or other derecognition of available-for-sale financial assets, any cumulative gains or losses are transferred from other comprehensive income to the income statement.
Gains and losses on financial instruments carried at amortised cost may also arise, and are recognised in the income statement, when a financial instrument is derecognised or when its value is impaired.

viii) Amortised cost measurement
The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

ix) Fair value measurement principles
Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm’s length transaction on the measurement date.
When available, the Group measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm’s length basis.
If a market for financial instruments, which are measured at cost less impairment is not active, or if for any reason, fair value cannot be reasonably measured by market price, then the Group establishes fair value using a valuation technique (except for certain unquoted equity securities). Valuation techniques include using recent arm’s length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analyses and option pricing models. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to the Group, incorporates all factors that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument. The Group calibrates valuation techniques and tests them for validity using prices from observable current market transactions in the same instrument or based on other available observable market data.
Fair values reflect the credit risk of the instrument and include adjustments to take account of the credit risk of the Group entity and the counterparty where appropriate.
The fair values of quoted investments are based on current closing bid prices.
The fair value of non-exchange-traded derivatives is estimated at the amount that the Group would receive or pay to terminate the contract at the reporting date taking into account current market conditions and the current creditworthiness of the counterparties.

x) Impairment of financial assets

Impairment of financial assets identified as impaired

a) Financial assets carried at amortised cost
The Group assesses at each reporting date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset
(a “loss event”) and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group

of financial assets that can be reliably estimated. Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the Group about the following loss events:

i) significant financial difficulty of the borrower;

ii) a breach of contract, such as a default or delinquency in interest or principal payments;

iii) the Group granting to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, a concession that it would not otherwise consider;

iv) significant restructuring due to financial difficulty or expected bankruptcy;

v) the disappearance of an active market for the financial asset because of financial difficulties;

vi) observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified for the individual financial assets in the group.

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity investments carried at amortised cost has incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.
If in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.
When possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of the new loan conditions. Once the terms have been renegotiated any impairment is measured using the original effective interest rate as calculated before the modification of terms and the loan is no longer considered past due. Management continually reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective assessment, calculated using the loan's original effective interest rate.
Individually significant financial assets are tested for impairment on an individual basis. Those individually significant assets which are not identified as impaired are subsequently included in the basis for collective impairment assessment. For the purpose of collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (i.e. on the basis of the Group's internal rating system that considers asset type, collateral type, past-due status and other relevant factors). Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

b) Financial assets carried at fair value
The Group assesses at each reporting date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity investments classified as available for sale, a significant or prolonged decline in the fair value of the investment below its cost is considered in determining whether the assets are impaired. In general, the Group considers a decline of 20% to be significant and a period of nine months to be prolonged. However, in specific circumstances a smaller decline or a shorter period may be appropriate. If any such evidence exists for available-for-sale financial assets, the cumulative loss, measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss, is removed from equity and recognised in the income statement. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the income statement. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is subsequently recognised in equity.

c) Financial assets carried at cost
These include equity securities classified as available for sale for which there is no reliable fair value. The Group assesses at each reporting date whether there is objective evidence that a financial asset or a group of financial assets is impaired.
An impairment loss is calculated as the difference between the carrying amount of the financial asset and the present value of expected future cash receipts discounted by the current market interest rate for similar financial assets.
Impairment losses on such instruments, recognised in the income statement, are not subsequently reversed through the income statement.

Impairment of financial assets not identified as impaired
If no objective evidence of impairment exists for a financial asset, whether significant or not, the Group includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment that has been incurred but not reported ("IBNR"). Assets that are assessed for specific impairment on individual or collective basis, and for which an impairment loss is or continues to be recognised, are not included in the collective assessment of IBNR impairment.
In assessing collective impairment for IBNR, financial assets are grouped on the basis of similar credit risk characteristics (i.e., on the basis of the Group's internal rating system, which considers asset type, counter party type, and other relevant factors). In assessing IBNR impairment the Group uses statistical modelling of historical trends of the probability of default, timing of recoveries, and the amount of loss incurred, adjusted for management's judgment and current economic conditions. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure they remain appropriate.

m) Derivative financial instruments
Derivative financial instruments are initially recognised in the statement of financial position in accordance with the policy for initial recognition of financial instruments and subsequently remeasured at their fair value. Fair values are obtained from quoted market prices, dealer price quotations, discounted cash flow models and options pricing models, as appropriate.

All derivatives are carried as assets when their fair value is positive and as liabilities when negative. Changes in the fair value of derivatives and gains and losses on derivatives based on securities are included in the income statement under "Net trading gains from forward foreign exchange contracts and swaps". All derivatives are classified as held for trading.

Some hybrid contracts contain both a derivative and a non-derivative component. In such cases, the derivative component is termed an embedded derivative. When the economic characteristics and risks of embedded derivatives are not closely related to those of the host contract and when the hybrid contract is not itself carried at fair value through profit or loss, the embedded derivative is treated as a separate derivative and classified at fair value through profit or loss with all unrealised and realised gains and losses recognised in the income statement, unless there is no reliable measure of their fair value.
Derivative financial instruments include foreign exchange forward contracts, foreign exchange swaps and embedded derivatives with a one-way currency clause.

n) Sale and repurchase agreements
The Group enters into purchases and sales of securities under agreements to resell or repurchase substantially identical securities at a certain date in the future at a fixed price. Investments purchased subject to such commitments to resell them at future dates are not recognised in the statement of financial position. The amounts paid are recognised as loans and advances to either banks or customers. The receivables are presented as collateralised by the underlying security. Securities sold under repurchase agreements continue to be recognised in the statement of financial position and are measured in accordance with the accounting policy for the relevant financial asset at amortised cost or at fair value as appropriate. The proceeds from the sale of the securities are reported as collateralised liabilities to either banks or customers.

The difference between the sale and repurchase consideration is recognised on an accrual basis over the period of the transaction and is included in interest income or expense.

o) Investments in subsidiaries and associates
Investments in subsidiaries and associates are accounted at cost less impairment in the separate financial statements of the Bank. Investments in subsidiaries are fully consolidated in the consolidated financial statements whilst investments in associates are accounted for under the equity method.

p) Interest-bearing borrowings
Interest-bearing borrowings are initially recognised at their fair value, less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between proceeds (net of transaction costs) and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis.

q) Current accounts and deposits from banks and customers
Current accounts and deposits are initially measured at fair value plus transaction costs, and subsequently stated at their amortised cost using the effective interest method.

r) Leases
Finance - Group as lessor
Leases where the Group, as lessor, transfers substantially all the risks and rewards incidental to ownership of an asset to the lessee are classified as finance leases. When assets are leased under finance lease arrangements, the present value of the lease payments is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is recognised as

unearned finance income. Initial direct costs, such as commissions, legal fees and internal costs that are incremental and directly attributable to negotiating and arranging a lease are included in the initial measurement of the finance lease receivable and reduce the amount of income recognised over the lease term. Finance lease receivables are included in the statement of financial position within Loans and advances to customers.

Operating - Group as lessor
The Group, as lessor, classifies all other leases other than finance leases as operating leases. Operating leases are included in the statement of financial position within property and equipment at cost net of accumulated depreciation. Such assets are depreciated over their expected useful lives which are based on the lease term (refer to the accounting policy for property and equipment). Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Operating lease receivables are included in loans and advances to customers.

Operating - Group as lessee
Leases of assets under which the risks and rewards of ownership are effectively retained with the lessor are classified as operating lease arrangements. Lease payments under operating lease are recognised as expenses on a straight-line basis over the lease term and included in other operating expenses.

s) Property and equipment
Property and equipment are stated at historical cost or deemed cost less accumulated depreciation and impairment losses. Historical cost includes its purchase price, including import duties and non-refundable purchase taxes and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

Property and equipment are tangible items that are held for use in the provision of services, for rental or other administrative purposes.

Subsequent cost is included in the asset's carrying amount or is recognised as a separate asset as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the period in which they have incurred.

Assets not yet brought into use are not depreciated until the relevant assets are completed and put into operational use and reclassified to the appropriate category of property and equipment.

Depreciation is provided on all assets except land and assets not yet brought into use on a straight-line basis at prescribed rates designed to write-off the cost over the estimated useful life of the asset. The estimated useful lives are as follows:

	2012	2011
Buildings	40 years	40 years
Office furniture	5 years	5 years
Computers	4 years	4 years
Motor vehicles	5 years	5 years
Equipment and other assets	2 to 10 years	2 to 10 years

The assets' residual values, useful lives and depreciation methods are reviewed, and adjusted if appropriate, at each reporting date. The carrying values of property and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.
When the use of property changes from owner-occupied to rented, the property is reclassified to investment property.
When assets are sold or retired, their cost and accumulated depreciation are eliminated and any gain or loss resulting from their disposal is included in the income statement.

t) Intangible assets

Intangible assets
Intangible assets are measured initially at cost. Intangible assets are recognised if it is probable that the future economic benefits attributable to the asset will flow to the enterprise and the cost of the asset can be measured reliably.

Subsequently, intangible assets are measured at cost less accumulated amortisation and any accumulated impairment losses. Intangible assets are amortised on a straight line basis over their estimated useful lives, which is 4 years.

The useful lives, residual values and depreciation methods are reviewed, and adjusted if appropriate, at each reporting date.

Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates.

Goodwill

According to IFRS 3 "Business Combinations", any excess of the cost of the acquisition over the acquirer's interest in the fair value of the identifiable assets and liabilities acquired on the date of the acquisition is presented as goodwill and recognised as an asset. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses.

Goodwill is reviewed for impairment at least annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (or the group of cash-generating units) to which the goodwill relates. Where the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then pro-rata to the other assets of the unit on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent period.

Upon the legal merger of the Bank's former subsidiary, Međimurska banka, goodwill formerly arising on consolidation was transformed into purchased goodwill recognised in the Bank's separate statement of financial position. Goodwill on acquisition of subsidiaries and purchased goodwill is included in intangible assets. Goodwill on acquisition of associates is included within investments in associates.

u) Investment property

Investment property is property held by the Group to earn rentals or for capital appreciation or for both, but not for sale in the ordinary course of business or for administrative purposes.

Investment property is measured initially at its cost, including transaction costs. Subsequently, investment property is stated at cost less accumulated depreciation and any impairment loss.

Investment property is depreciated on a straight-line basis over a period of 40 years.

Investment property is derecognised when either it has been disposed of or permanently withdrawn from use and no future economic benefits are expected from its disposal. Any gains or losses on the retirement or disposal of investment property are recognised in the income statement in the year of retirement or disposal.

v) Non-current assets and disposal groups classified as held for sale

The Group classifies a non-current asset as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition. Management must be committed to the sale and the sale should be expected to be completed within one year from the date of classification.

Immediately before classification as held for sale, the assets (or components of a disposal group) are remeasured in accordance with the Group's accounting policies. Thereafter, the assets (or disposal group of assets and liabilities) are measured at the lower of their carrying amount and fair value less cost to sell.

A non-current asset classified as held for sale is no longer depreciated.

Impairment losses on initial classification as held for sale are included in the income statement, as well as gains and losses on subsequent measurement.

w) Impairment of non-financial assets

Assets that have an indefinite useful life, such as goodwill, are not subject to amortisation and are tested for impairment whenever there are indications that these may be impaired or at least annually. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Intangible assets that are not yet available for use are assessed at each reporting date. An impairment loss is recognised whenever the carrying amount of an asset exceeds its recoverable amount. Impairment losses are recognised in the income statement.

The recoverable amount of property and equipment, investment property and intangible assets is the higher of the asset's fair value less costs to sell and value in use. For the purpose of assessing impairment, assets are grouped at the lowest level for which there are separately identifiable cash flows (cash-generating units). In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or cash-generating unit.

Other previously impaired non-financial assets, other than goodwill, are reviewed for possible reversal of the impairment at each reporting date. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

x) Provisions

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

Provisions for liabilities and charges are maintained at the level that the Group's management considers sufficient for absorption of losses. The management determines the sufficiency of provisions on the basis of insight into specific items, current economic circumstances, risk characteristics of certain transaction categories, as well as other relevant factors.

A provision for restructuring is recognised when the Group has approved a detailed and formal restructuring plan, and the restructuring either has commenced or has been announced publicly. Future operating losses are not provided for.

A provision for onerous contracts is recognised when the expected benefits to be derived by the Group from a contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing the contract. Before a provision is established, the Group recognises any impairment loss on the assets associated with the contract.

Provisions are released only for expenditure for which provisions are recognised at inception. If the outflow of economic benefits to settle the obligations is no longer probable, the provision is reversed.

y) Issued share capital

Issued share capital represents the nominal value of paid-in ordinary shares and is denominated in HRK.
Dividends are recognised as a liability in the period in which they are declared.

z) Treasury shares

When any Group company purchases the Bank's equity share capital (treasury shares), the consideration paid is deducted from equity attributable to the Bank's equity holders and classified as treasury shares until the shares are cancelled, reissued or disposed of. When such shares are subsequently sold or reissued, any consideration received, net of transaction costs, is included in equity attributable to the Bank's equity holders.

aa) Retained earnings

Any profit for the year retained after appropriations is classified within retained earnings.

bb) Off-balance-sheet commitments and contingent liabilities

In the ordinary course of business, the Group enters into credit-related commitments which are recorded in off-balance-sheet accounts and primarily comprise guarantees, letters of credit, undrawn loan commitments and credit-card limits. Such financial commitments are recorded in the Group's statement of financial position if and when they become payable.
Financial guarantees are contracts that require the Group to make specified payments to reimburse the holder for a loss incurred because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

Financial guarantee liabilities are initially recognised at their fair value, being the premium received, and the initial fair value is amortised over the life of the financial guarantee. The guarantee liability is subsequently carried at the higher of this amortised amount and the present value of any expected payment (when a payment under the guarantee becomes probable). Financial guarantees are included within Other liabilities.

cc) Managed funds for and on behalf of third parties

The Group manages funds for and on behalf of corporate and retail customers, banks and other institutions. These amounts do not represent the Group's assets and are excluded from the statement of financial position. For the services rendered the Group charges a fee. For details please refer to Note 37.

dd) Segment reporting

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components, whose operating results are reviewed regularly by the Management Board of the Bank (being the chief operating decision maker) to make decisions about resources allocated to each segment and assess its performance, and for which discrete financial information is available.

For management purposes, the Bank is organised into three primary operating segments: Retail, Corporate and Finance banking. Furthermore, the management of the Bank monitors performance of its subsidiaries on an individual basis. However, for the purpose of presentation of the operating segments for the Group, with the exception of PBZ Card, all subsidiaries have been grouped into one segment. The primary segmental information is based on the internal reporting structure of business segments. Segmental results are measured by applying internal prices (Note 42).

ee) Earnings per share

The Group presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS are calculated by dividing the profit or loss attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the period. Diluted EPS are determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares.

ff) Foreclosed assets

The Group occasionally acquires real estate in settlement of certain loans and advances. Real estate is stated at the lower of the cost of the related loans and advances and the current fair value of such assets. The Group's intention is mainly to sell such assets, which, however, in certain limited cases may end up being used by the Group.
Gains or losses on disposal are recognised in the income statement.

gg) Standards, interpretations and amendments to published standards that are not yet effective and were not used in preparation of these financial statements

Several new and altered Standards and Interpretations have been issued by the International Accounting Standards Board ("IASB") and its International Financial Reporting Interpretations Committee, but are not applicable to entities reporting under IFRS for the year ended 31 December 2012, and have not been applied in preparation of these financial statements. The majority of the new and altered Standards and Interpretations are not relevant to the Group's business and hence will not affect its financial statements except as follows:

IFRS 9 Financial instruments

IFRS 9 Financial instruments (the complete version of this standard has not yet been adopted and the IASB currently has an active project to make limited amendments to the classification and measurement requirements of IFRS 9 and to add new requirements to address the impairment of financial assets and hedge accounting), which replaces IAS 39 "Financial instruments: Recognition and Measurement". IFRS 9 is obligatory for the financial statements for the periods beginning 1 January 2015 with earlier adoption permitted. The standard introduces significant changes in terms of the classification and measurement of financial assets. The Group has not yet determined the date of the first adoption of IFRS 9 nor has it fully analysed the effects of its adoption.

IFRS 13 Fair value measurement

IFRS 13 is mandatory for financial statements for periods from 1 January 2013, with possible usage in earlier periods. It provides a single source of guidance on how fair value is measured, and replaces the fair value measurement guidance that is currently dispersed throughout IFRS. Subject to limited exceptions, IFRS 13 is applied when fair value measurements or disclosures are required or permitted by other IFRSs. The Group will apply IFRS 13 beginning from 1 January 2013, and considers that no significant changes will occur.

IFRS 10 Consolidated Financial Statements

IFRS 10 is effective for annual periods beginning on or after 1 January 2013 and provides a single model to be applied in the control analysis for all investees, which may lead to changes in current accounting for these investees. IFRS 10 introduces new requirements to assess control that are different from the existing requirements in IAS 27 (2008). The Group will apply IFRS 10 beginning from 1 January 2013, and considers that no significant changes will occur.

IFRS 12 Disclosure of Interests in Other Entities

IFRS 12 requires additional disclosures relating to significant judgements and assumptions made in determining the nature of interests in an entity or arrangement, interests in subsidiaries, joint arrangements and associates and unconsolidated structured entities. It is expected that the new Standard, when initially applied from 1 January 2013 will have impact on the level of disclosure in the financial statements. However, the Group is not able to prepare an analysis of the impact this will have on the financial statements until the date of initial application.

4 | Accounting estimates and judgments in applying accounting policies

The Group makes estimates and assumptions about uncertain events, including estimates and assumptions about the future. Such accounting assumptions and estimates are regularly evaluated, and are based on historical experience and other factors such as the expected flow of future events that can be rationally assumed in the existing circumstances, but nevertheless necessarily represent sources of estimation uncertainty. The estimation of impairment losses in the Group's credit risk portfolio and, as part of this, the estimation of the fair value of real estate collateral represents the major source of estimation uncertainty. This and other key sources of estimation uncertainty, that have a significant risk of causing a possible material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below.

Notes to the financial statements

a) Impairment losses on loans and advances
The Group reviews its portfolios of non-current loans and advances to assess whether there is objective evidence of impairment on an ongoing basis.

The Group first assesses whether objective evidence of impairment exists individually for assets that are individually significant (corporate exposures) and collectively for assets that are not individually significant (retail). Those assets which are not identified as specifically impaired are subsequently included in the basis for collective impairment assessment, on the basis of similar credit risk characteristics.

The Group uses its judgement to estimate the amount of any impairment loss in cases where a borrower is in financial difficulties and there is limited historical data relating to similar borrowers. Similarly, the Group estimates changes in future cash flows based on observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or based on national or local economic conditions that correlate with defaults on assets in the group. The Group uses estimates based on historical loss experience for assets with similar credit risk characteristics and objective evidence of impairment similar to those in the group of loans and advances. The Group uses its judgement to adjust observable data for groups of loans or advances to reflect current circumstances.

In addition to losses on an individual basis, the Group continuously monitors and recognises impairments which are known to exist at the reporting date, but which have not yet been identified. In estimating unidentified impairment losses for collectively assessed portfolios, the Group seeks to collect reliable data on appropriate loss rates based on historical experience related to and adjusted for current conditions, and the emergence period for the identification of these impairment losses.

b) Impairment of available-for-sale equity investments
The Group determines that available-for-sale equity investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgement.

In making this judgement, the Group evaluates among other factors, the nominal volatility in share price. In addition, impairment may be appropriate when there is evidence of deterioration in the financial health of the investee, industry and sector performance, changes in technology, and operational and financing cash flows.

c) Held-to-maturity investments
The Group follows the guidance of International Accounting Standard 39 Financial Instruments: Recognition and Measurement on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held to maturity. This classification requires significant judgement. In making this judgement, the Group evaluates its intention and ability to hold such investments to maturity.

d) Classification of lease contracts
The Group acts as a lessor in operating and finance leases. Where the Group, as a lessor, transfers substantially all the risks and rewards incidental to ownership to the lessee, the leases are classified as finance leases. All other leases are classified as operating and related assets are included in property and equipment under operating leases at cost net of accumulated depreciation. In determining whether leases should be classified as operating or finance, the Company considers the requirements of International Accounting Standard 17 Leases.

e) Impairment of goodwill
The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows.

f) Fair value of financial instruments
If a market for a financial instrument is not active, or, if for any reason, fair value cannot be reasonably measured by market price, the Group establishes fair value using a valuation technique (except for certain unquoted equity securities). Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analyses and option pricing models. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to the Group, incorporates all factors that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument. The Group calibrates valuation techniques and tests them for validity using prices from observable current market transactions in the same instrument or based on other available observable market data. The chosen valuation techniques are periodically reviewed by an independent expert who has not participated in their formation. All models are certified before use.

g) Reclassification of financial instruments
The Group identified that the market conditions for Croatian government bonds no longer demonstrated active trading during the first half of 2009. In general, the fixed income market in Croatia was adversely impacted by the global recession which led to a standstill in trading, interrupted only by occasional forced transactions. In such circumstanc-es, the Group could not actively trade these instruments and there were no observable elements on which the Group could reliably determine the fair value. In that context, in April and May 2009 the Group decided to reclassify the aforementioned financial instruments from the portfolio of financial instruments at fair value through profit and loss and available-for-sale portfolio to the loans and receivables portfolio. Overall, the Group has the intention and ability to hold the reclassified financial instruments for the foreseeable future. For more details refer to Note 41.

h) Taxation
The Group provides for tax liabilities in accordance with the tax laws of the Republic of Croatia. Tax returns are subject to the approval of the tax authorities who are entitled to carry out subsequent inspections of taxpayers' records.

i) Regulatory requirements
The Croatian National Bank and the Croatian Financial Services Agency are entitled to carry out regulatory inspections of the Group's operations and to request changes to the carrying values of assets and liabilities, in accordance with the underlying regulations.

j) Litigation and claims
The Group makes an individual assessment of all court cases. The assessment is made by the Legal Department of the Bank or its relevant subsidiaries and in certain cases external lawyers are engaged. As stated in Note 33 the Group and the Bank provided HRK 36 million (2011: HRK 34 million) and HRK 33 million (2011: HRK 30 million) respectively for principal and interest in respect of liabilities for court cases, which the management estimates as sufficient. It is not practicable for management to estimate the financial impact of changes to the assumptions based on which management assesses the need for provisions.

k) Fair value of property and equipment and investment property
The Group uses the cost model for property and equipment and investment property. Carrying values are reviewed for impairment at least annually. The management considers that there are no indications of impairment at the reporting date based on these analyses.

l) Foreclosed assets
The Group occasionally acquires real estate in settlement of certain loans and advances. Real estate is stated at the lower of the cost of the related loans and advances and the current fair value of such assets. Gains or losses on disposal are recognised in the income statement.

m) Law on Financial Transactions and Pre-bankruptcy Settlement
A new Law on Financial Transactions and Pre-bankruptcy Settlement came into force on 1 October 2012. The Law sets out criteria for the determination when the management has an obligation to commence the process of pre-bankruptcy settlement. In accordance with the Law an application for pre-bankruptcy settlement has to include a restructuring plan and should be filed with the Financial Agency. The Law was designed to help debtors that are in financial difficulties to restructure its operations, thus allowing them to continue with their business activities. During the period of the pre-bankruptcy process, the company is protected from its creditors, who during this period are unable to block bank accounts or take steps to push the debtor into bankruptcy or otherwise seek to realise collateral. The implementation of a restructuring plan is subject to approval by certain majorities of creditors in various classes. At the same time, creditors are now in an improved position for the collection of their receivables than would otherwise be the case had they initiated bankruptcy proceedings against the debtor.

As explained in Note 50 Subsequent events, the main effect of the new legislation started to be felt after the reporting date. Up to the end of February 2013, 88 applications have been filed with the Agency, which were debtors of the Bank at 31 December 2012, with total balance and off-balance sheet exposure of HRK 270 million as at 31 December 2012, net of impairment allowance. The impairment allowance accounts for 40% of the gross total value of those exposures.

The Group has set up the function which closely monitors the clients that have filed for pre-bankruptcy settlement and assists these borrowers in developing and implementing a restructuring plan in order to facilitate the collection of the Group's assets. At the same time, although a majority of debtors that have filled for pre-bankruptcy settlement have been already identified by the Group as non-performing, the Group is reassessing the adequacy of their provisions.

The management is unable to determine the effect of the pre-bankruptcy settlement process on the realisable value of its credit-risk exposures, but believes that the new Law will accelerate the credit default rate within the domestic economy. However, the consequences of the application of the new Law have yet to be determined in practice.

5 | Net interest income (in HRK million)

a) Interest income – analysis by source

	GROUP		BANK	
	2012	2011	2012	2011
Retail	2,063	2,108	1,924	1,958
Corporate	1,036	1,043	952	940
Public sector and other institutions	701	707	626	613
Banks	50	77	48	88
	3,850	**3,935**	**3,550**	**3,599**

b) Interest income – analysis by product

	GROUP		BANK	
	2012	2011	2012	2011
Loans and advances to customers	3,391	3,476	3,175	3,225
Debt securities classified as loans and receivables	192	202	142	141
Financial assets initially designated at fair value through profit or loss	152	106	152	106
Loans and advances to banks	47	65	45	76
Financial assets held for trading	31	20	31	20
Financial assets available for sale	25	32	2	9
Held-to-maturity investments	10	28	1	16
Balances with the Croatian National Bank	2	6	2	6
	3,850	**3,935**	**3,550**	**3,599**

Interest income includes interest income from previously impaired loans of the Group of HRK 263 million (2011: HRK 262 million) and of the Bank of HRK 211 million (2011: HRK 221 million).

5 | Net interest income / continued (in HRK million)

c) Interest expense – analysis by source

	GROUP		BANK	
	2012	2011	2012	2011
Retail	1,054	1,059	973	976
Banks	256	258	218	223
Public sector and other institutions	84	77	90	78
Corporate	50	61	56	54
	1,444	**1,455**	**1,337**	**1,331**

d) Interest expense – analysis by product

	GROUP		BANK	
	2012	2011	2012	2011
Current accounts and deposits from retail customers	1,054	1,059	973	976
Interest-bearing borrowings	202	222	182	188
Current accounts and deposits from corporate customers and public sector	127	123	121	116
Current accounts and deposits from banks	61	51	61	51
	1,444	**1,455**	**1,337**	**1,331**

6 | Net fee and commission income (in HRK million)

a) Fee and commission income

	GROUP 2012	GROUP 2011	BANK 2012	BANK 2011
Credit cards	778	757	91	89
Payment transactions	276	287	298	287
Customer services	72	71	69	68
Investment management, brokerage and consultancy	54	68	37	46
Customer loans	48	56	48	55
Guarantees	43	46	42	45
Other	82	67	38	34
	1,353	**1,352**	**623**	**624**

b) Fee and commission expense

	GROUP 2012	GROUP 2011	BANK 2012	BANK 2011
Credit cards	187	156	65	54
Payment transactions	40	47	35	46
Bank charges	9	12	9	9
Other	27	25	8	5
	263	**240**	**117**	**114**

7 | Dividend income (in HRK million)

	GROUP 2012	GROUP 2011	BANK 2012	BANK 2011
Dividends from associates	-	-	-	11
Dividends from subsidiaries	-	-	140	164
Dividends from other equity securities	3	4	3	4
	3	**4**	**143**	**179**

8 | Net trading income and net loss on translation of monetary assets and liabilities (in HRK million)

	GROUP 2012	GROUP 2011	BANK 2012	BANK 2011
Net trading income from forward foreign exchange contracts and swaps	154	60	154	60
Net loss from translation of monetary assets and liabilities denominated in foreign currency	(50)	(22)	(49)	(18)
Foreign exchange spot trading	94	107	88	101
Net losses on securities at fair value held for trading	(1)	(1)	(1)	(1)
Net (losses)/gains from securities initially designated at fair value through profit or loss	(54)	2	(56)	2
	143	**146**	**136**	**144**

9 | Other operating income (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Rental income from investment property and assets under operating lease	62	70	3	2
Net gain on disposal of available-for-sale securities	8	6	2	3
Gain on disposal of property and equipment	5	17	1	15
Gain on disposal of non-current assets held for sale	5	-	5	-
Other income	39	39	26	25
	119	**132**	**37**	**45**

10 | a) Personnel expenses (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Net salaries	399	393	336	329
Contributions for pension insurance	111	108	96	92
Taxes and surtaxes	100	95	85	80
Contributions for health insurance	84	89	70	75
Other personnel expenses	30	85	23	79
	724	**770**	**610**	**655**

Other personnel expenses include accrued expenses for bonuses payable to the members of the Management Board, other key management personnel, and all other employees of the Bank in the gross amount of HRK 12 million (2011: HRK 42 million). During the year the average number of employees within the Group was 4,170 (2011: 3,933) of which the Bank accounted for 3,413 employees (2011: 3,353).

b) Other operating expenses (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Materials and services	489	467	341	326
Deposit insurance premium	95	92	86	84
Operating leases	64	68	76	64
Indirect and other taxes	19	21	16	18
Other expenses	334	311	151	129
	1,001	**959**	**670**	**621**

11 | Other impairment losses and provisions

(in HRK million)	NOTES	GROUP 2012	GROUP 2011	BANK 2012	BANK 2011
(Release of)/impairment loss on loans and advances to banks	18b	(10)	14	(11)	13
Impairment loss on financial assets available for sale		26	30	26	30
Provisions for off-balance-sheet items	33	15	1	13	6
Provisions for court cases	33	6	(5)	6	(5)
Provisions for other items	33	9	13	9	13
		46	**53**	**43**	**57**

The impairment loss on financial assets available for sale in the amount of HRK 26 million (2011: HRK 30 million) includes HRK 12 million (2011: HRK 30 million) in respect of financial assets which first became impaired in the current year, while the remaining amount of HRK 14 million (2011: nil) relates to financial assets which were already impaired in prior years.

12 | Depreciation and amortisation (in HRK million)

	GROUP 2012	GROUP 2011	BANK 2012	BANK 2011
Depreciation of property and equipment	149	171	86	106
Amortisation of intangible assets	41	41	37	34
Depreciation of investment property	1	1	1	1
	191	**213**	**124**	**141**

Depreciation and amortisation of intangible assets for 2011 include the write-off of goodwill in the amount of HRK 3 million. Depreciation of property and equipment includes HRK 53 million of depreciation of assets under operating lease (2011: HRK 57 million).

13 | Income tax expense

a) Income tax expense recognised in the income statement

(in HRK million)	GROUP 2012	GROUP 2011	BANK 2012	BANK 2011
Current income tax charge	269	270	194	220
Net deferred tax (credit)/charge	(11)	43	(12)	20
Income tax expense recognised in the income statement	**258**	**313**	**182**	**240**

13 | Income tax expense / continued

b) Reconciliation of income tax expense (in HRK million)

The reconciliation between the accounting profit and income tax expense at 20% is set out below:

	GROUP		BANK	
	2012	2011	2012	2011
Accounting profit before tax	1,272	1,581	1,028	1,376
Tax calculated at rate of 20% (2011: 20%)	254	316	206	275
Tax effects of:				
Non-deductible expenses	12	6	8	3
Tax exempt income	(29)	(36)	(29)	(36)
Tax incentives for education expenses	(1)	(1)	(1)	(1)
Expenses included directly in income tax expense	(2)	(1)	(2)	(1)
Consolidation adjustments	24	29	-	-
Total income tax expense	**258**	**313**	**182**	**240**
Effective income tax rate	**20.3%**	**19.8%**	**17.7%**	**17.4%**

c) Deferred tax assets

(in HRK million)	GROUP		BANK	
	2012	2011	2012	2011
Timing differences				
On deferred fees	57	62	52	56
On impairment of real estate	7	6	7	6
On unrealised losses on financial assets at fair value through profit or loss	66	49	66	49
On unrealised losses on available-for-sale financial assets	6	11	2	3
On other items	3	7	5	4
On impairment of loans	38	36	-	-
Deferred tax assets	**177**	**171**	**132**	**118**

13 | Income tax expense / continued (in HRK million)

d) Movement in deferred tax assets

	Total	Deferred fees	Impairment of real estate	Unrealised losses on financial assets at fair value through profit or loss	Unrealised losses on available for-sale financial assets	Other items	Impairment of loans
Group							
Balance as at 1 January 2012	**171**	**62**	**6**	**49**	**11**	**7**	**36**
Increase credited to income statement	*55*	*19*	*1*	*28*	-	*4*	*3*
Utilisation charged to income statement	*(44)*	*(24)*	-	*(11)*	-	*(8)*	*(1)*
Net amount credited to income statement	11	(5)	1	17	-	(4)	2
Decrease in other comprehensive income	(5)	-	-	-	(5)	-	-
Balance as at 31 December 2012	**177**	**57**	**7**	**66**	**6**	**3**	**38**
Balance as at 1 January 2011	**220**	**69**	**6**	**59**	**17**	**12**	**57**
Increase credited to income statement	*39*	*21*	-	*11*	-	*3*	*4*
Utilisation charged to income statement	*(82)*	*(28)*	-	*(21)*	-	*(8)*	*(25)*
Net amount charged to income statement	(43)	(7)	-	(10)	-	(5)	(21)
Decrease in other comprehensive income	(6)	-	-	-	(6)	-	-
Balance as at 31 December 2011	**171**	**62**	**6**	**49**	**11**	**7**	**36**

13 | Income tax expense / continued (in HRK million)

d) Movement in deferred tax assets / continued

	Total	Deferred fees	Impairment of real estate	Unrealised losses on financial assets at fair value through profit or loss	Unrealised losses on available for-sale financial assets	Other items
Bank						
Balance as at 1 January 2012	**118**	**56**	**6**	**49**	**3**	**4**
Acquired on merger with Međimurska banka (Note 22)	3	2	-	-	-	1
Increase credited to income statement	*53*	*19*	*1*	*28*	-	*5*
Utilisation charged to income statement	*(41)*	*(25)*	-	*(11)*	-	*(5)*
Net amount credited to income statement	12	(6)	1	17	-	-
Decrease in other comprehensive income	(1)	-	-	-	(1)	-
Balance as at 31 December 2012	**132**	**52**	**7**	**66**	**2**	**5**
Balance as at 1 January 2011	**141**	**62**	**6**	**59**	**6**	**8**
Increase credited to income statement	*35*	*21*	-	*11*	-	*3*
Utilisation charged to income statement	*(55)*	*(27)*	-	*(21)*	-	*(7)*
Net amount charged to income statement	(20)	(6)	-	(10)	-	(4)
Decrease in other comprehensive income	(3)	-	-	-	(3)	-
Balance as at 31 December 2011	**118**	**56**	**6**	**49**	**3**	**4**

14 | Cash and current accounts with banks (in HRK million)

		GROUP		**BANK**
	2012	2011	2012	2011
Cash in hand	1,395	1,324	1,395	1,241
Current accounts with the CNB	1,709	1,204	1,709	1,120
Current accounts with foreign banks	1,034	97	1,034	88
Current accounts with domestic banks	27	19	27	13
Other cash items	6	3	3	3
	4,171	**2,647**	**4,168**	**2,465**

15 | Balances with the Croatian National Bank (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Obligatory reserve	4,857	5,179	4,857	4,957
Other deposits with the CNB	800	1,810	800	1,800
	5,657	**6,989**	**5,657**	**6,757**

The CNB determines the requirement for banks to calculate an obligatory reserve, which is required to be deposited with the CNB and held in the form of other liquid receivables.
The obligatory reserve requirement as at 31 December 2012 amounted to 13.5% (2011: 14%) of kuna and foreign currency deposits and borrowings.
As at 31 December 2012, the required rate for the part of the obligatory reserve calculated based on kuna liabilities to be deposited with the CNB amounted to 70% (2011: 70%), while the remaining 30% (2011: 30%) had to be held in the form of other liquid receivables. This includes the part of foreign currency obligatory reserve required to be held in HRK.
At least 60% (2011: 60%) of the part of the obligatory reserve based on foreign currency liabilities must be deposited with the CNB, while the remaining 40% (2011: 40%) (or less to the extent that the amount deposited with the CNB exceeds 60%) must be held in the form of other liquid receivables, after adjusting for the obligatory reserve requirement arising from foreign currency funds from non-residents and related parties (which is required to be held in full with the CNB). 75% of the part of the obligatory reserve calculated based on foreign currency liabilities is required to be held in kuna and is added to the kuna part of the obligatory reserve.
From March 2011 the obligatory reserve does not earn any interest.

16 | Financial assets at fair value through profit or loss (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Financial assets held for trading				
Equity securities - listed	18	27	18	27
	18	**27**	**18**	**27**
Financial assets initially designated at fair value through profit or loss				
Ministry of Finance treasury bills	3,472	2,037	3,424	2,037
Other sovereign treasury bills	151	-	151	-
Bonds issued by domestic corporate issuers	143	276	143	276
Municipal bonds	82	82	82	82
Units in investment funds	10	-	-	-
Equity securities	4	-	4	-
Domestic commercial bills	-	23	-	23
Accrued interest	106	52	105	52
	3,968	**2,470**	**3,909**	**2,470**
Listed securities	496	433	485	433
Unlisted securities	3,472	2,037	3,424	2,037
	3,968	**2,470**	**3,909**	**2,470**
Financial assets at fair value through profit or loss	**3,986**	**2,497**	**3,927**	**2,497**

17 | Derivative financial assets and liabilities (in HRK million)

	GROUP		BANK	
Assets	2012	2011	2012	2011
Fair value:				
Forward foreign exchange contracts and swaps	4	11	4	11
	4	**11**	**4**	**11**
Notional amount:				
Forward foreign exchange contracts and swaps	1,598	3,818	1,598	3,818
Other embedded derivatives	38	81	38	81
	1,636	**3,899**	**1,636**	**3,899**
Liabilities				
Fair value:				
Forward foreign exchange contracts and swaps	4	9	4	9
	4	**9**	**4**	**9**
Notional amount:				
Forward foreign exchange contracts and swaps	1,597	3,811	1,597	3,811
Other embedded derivatives	17	60	17	60
	1,614	**3,871**	**1,614**	**3,871**

The Group uses foreign currency forward and swap contracts to manage its exposure to foreign currency risk. Other embedded derivatives relate to loans with one-way currency clause.
The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised on the statement of financial position but do not necessarily indicate the amounts of future cash flows involved or the current fair value of instruments and, therefore, do not indicate the Group's exposure to credit or price risks.

18 | Loans and advances to banks (in HRK million)

	GROUP		BANK	
a) Analysis by type of product	2012	2011	2012	2011
Term deposits	5,133	6,155	5,107	5,884
Loans	1,149	920	1,160	1,386
Debt securities	-	3	-	3
	6,282	**7,078**	**6,267**	**7,273**
Impairment allowance	(32)	(42)	(31)	(42)
	6,250	**7,036**	**6,236**	**7,231**

Term deposits mainly relate to short-term deposits (up to one month) with local and foreign banks bearing an average annual interest rate of between 1.2% and 3.2% (2011: between 1.7% and 3.5%).

18 | Loans and advances to banks / continued (in HRK million)

b) Movement in impairment allowance	GROUP 2012	GROUP 2011	BANK 2012	BANK 2011
Balance at 1 January	**42**	**28**	**42**	**29**
Net (release) / charge for the year	(10)	14	(11)	13
Balance at 31 December	**32**	**42**	**31**	**42**

c) Geographical analysis	GROUP 2012	GROUP 2011	BANK 2012	BANK 2011
Republic of Croatia	1,307	1,001	1,293	1,439
France	976	759	976	759
Germany	768	931	768	908
Italy	735	2,793	735	2,756
Great Britain	682	208	682	178
Belgium	520	414	520	373
Austria	437	376	437	362
Switzerland	144	17	144	-
Other countries	713	579	712	498
	6,282	**7,078**	**6,267**	**7,273**
Impairment allowance	(32)	(42)	(31)	(42)
	6,250	**7,036**	**6,236**	**7,231**

As at 31 December 2011 loans and advances to banks included reverse repurchase agreements in the amount of HRK 531 million, including HRK 11 million of accrued interest. Such agreements were secured with government bonds and treasury bills. There are no reverse repurchase agreements with banks as at 31 December 2012.

19 | Loans and advances to customers (in HRK million)

a) Analysis by type of customer	GROUP 2012	GROUP 2011	BANK 2012	BANK 2011
Retail customers	27,664	27,703	25,341	24,574
Corporate customers	16,289	16,897	15,518	15,840
Public sector and other institutions	6,934	6,963	7,242	6,968
Debt securities	3,088	3,422	2,319	2,163
	53,975	**54,985**	**50,420**	**49,545**
Impairment allowance	(3,680)	(3,225)	(3,171)	(2,515)
Deferred interest and fees recognised as an adjustment to the effective yield	(335)	(362)	(331)	(339)
	49,960	**51,398**	**46,918**	**46,691**

Debt securities of the Group include HRK 923 million (2011: HRK 1,358 million) and HRK 170 million (2011: HRK 182 million) of the Bank representing Croatian corporate and government bonds reclassified from available-for-sale financial assets in 2009, as described in Notes 20(a) and 41.

b) Analysis by sector	GROUP 2012	GROUP 2011	BANK 2012	BANK 2011
Individuals	27,664	27,703	25,341	24,574
Public administration and defence, compulsory social security	5,456	6,057	5,456	6,004
Construction	5,222	4,668	5,002	4,543
Wholesale and retail trade	3,797	3,164	3,563	2,741
Manufacturing	2,731	2,713	2,723	2,697
Professional, scientific and technical services	1,416	1,352	1,416	1,352
Transport and communication	1,369	1,429	1,322	1,367
Energy products and water supplies	965	1,022	960	1,015
Real estate, renting and business services	907	1,073	883	1,028
Hotels and restaurants	871	808	830	765
Agriculture, forestry and fishing	601	1,266	579	1,221
Other	2,976	3,730	2,345	2,238
	53,975	**54,985**	**50,420**	**49,545**
Impairment allowance	(3,680)	(3,225)	(3,171)	(2,515)
Deferred interest and fees recognised as an adjustment to the effective yield	(335)	(362)	(331)	(339)
	49,960	**51,398**	**46,918**	**46,691**

Loans and advances to customers also include finance lease receivables. For detailed analysis of finance lease receivables please refer to Note 38 Leases.

19 | Loans and advances to customers / continued (in HRK million)

c) Movement in impairment allowance on loans and advances to customers

	Retail		Corporate		Public sector and other institutions		Total
	Specific	IBNR	Specific	IBNR	Specific	IBNR	
Group							
Balance at 1 January 2012	**1,575**	**177**	**1,067**	**343**	**35**	**28**	**3,225**
Amounts collected/reversed	(859)	(15)	(501)	(23)	(3)	-	**(1,401)**
Provisions charged	1,007	20	877	34	3	3	**1,944**
Charge in the income statement	**148**	**5**	**376**	**11**	**-**	**3**	**543**
Amounts written off	(18)	-	(75)	-	-	-	**(93)**
Foreign exchange loss	4	-	1	-	-	-	**5**
Balance at 31 December 2012	**1,709**	**182**	**1,369**	**354**	**35**	**31**	**3,680**
Balance at 1 January 2011	**1,447**	**345**	**861**	**228**	**34**	**2**	**2,917**
Amounts collected/reversed	(733)	(214)	(288)	(35)	(23)	(1)	**(1,294)**
Provisions charged	854	28	524	153	24	27	**1,610**
Charge in the income statement	**121**	**(186)**	**236**	**118**	**1**	**26**	**316**
Amounts written off	(8)	-	(39)	(3)	-	-	**(50)**
Foreign exchange loss	15	18	9	-	-	-	**42**
Balance at 31 December 2011	**1,575**	**177**	**1,067**	**343**	**35**	**28**	**3,225**

19 | Loans and advances to customers / continued (in HRK million)

c) Movement in impairment allowance on loans and advances to customers / continued

	Retail		Corporate		Public sector and other institutions		Total
	Specific	IBNR	Specific	IBNR	Specific	IBNR	
Bank							
Balance at 1 January 2012	**1,071**	**137**	**919**	**328**	**34**	**26**	**2,515**
Acquired on merger of Međimurska banka	87	10	76	13	-	-	**186**
Amounts collected/reversed	(772)	(12)	(477)	(23)	(2)	-	**(1,286)**
Provisions charged	951	9	852	28	3	3	**1,846**
Charge in the income statement	**179**	**(3)**	**375**	**5**	**1**	**3**	**560**
Amounts written off	(15)	-	(78)	-	-	-	**(93)**
Foreign exchange loss	2	-	1	-	-	-	**3**
Balance at 31 December 2012	**1,324**	**144**	**1,293**	**346**	**35**	**29**	**3,171**
Balance at 1 January 2011	**940**	**327**	**713**	**212**	**33**	**-**	**2,225**
Amounts collected/reversed	(663)	(213)	(274)	(31)	(23)	-	**(1,204)**
Provisions charged	782	23	498	147	24	26	**1,500**
Charge in the income statement	**119**	**(190)**	**224**	**116**	**1**	**26**	**296**
Amounts written off	(2)	-	(26)	-	-	-	**(28)**
Foreign exchange loss	14	-	8	-	-	-	**22**
Balance at 31 December 2011	**1,071**	**137**	**919**	**328**	**34**	**26**	**2,515**

19 Loans and advances to customers / continued

d) Loans and contingencies under guarantee

The state budget includes support for certain key industries in the Republic of Croatia. The repayment of loans and advances to qualifying customers in such industries is provided for by the state budget. In addition, the Republic of Croatia has issued guarantees for a certain number of the Bank's loans and off-balance-sheet credit risks.
The support and guarantee of the Republic of Croatia was taken into consideration when determining the level of provisions required against loans and off-balance-sheet credit risk exposure to certain legal entities.
Total Group loans and off-balance-sheet credit risks guaranteed by the Republic of Croatia or repayable from the state budget amount to HRK 5,654 million (2011: HRK 4,293 million).

e) Collateral repossessed

During the year, the Group and Bank foreclosed on real estate previously charged to them as collateral, and thereby recognised assets with a carrying value of HRK 4.7 million and HRK 2.8 million respectively (2011: HRK 5.6 million and HRK 3 million respectively). The repossessed collateral, which the Group is in the process of selling, is disclosed as foreclosed assets within Other assets (Note 27). In general, the Group does not occupy repossessed properties for business use.
During 2012 the Group sold repossessed collateral with a total fair value of HRK 2.3 million (2011: HRK 3 million).

f) Sale and repurchase agreement

Sale and repurchase agreements are transactions in which the Group sells a security and simultaneously agrees to repurchase it at a fixed price on a future date. The Group continues to recognise the securities in their entirety in the statement of financial position because it retains substantially all the risks and rewards of ownership. The cash consideration received is recognised as a financial assets and a financial liability is recognised for the obligation to pay a repurchase price (please refer to Note 30 interest-bearing borrowings).
The carrying amount of securities sold under repurchase agreements at 31 December 2012 was HRK 906 million (2011: HRK 1,001 million). Those securities are classified in the loans and receivables portfolio and financial assets initially designated at fair value through profit or loss portfolio (Note 16).
Reverse sale and repurchase agreements are transactions in which the Group purchases a security and simultaneously agrees to sell it at a fixed price on a future date. The Group holds collateral in the form of marketable securities in respect of loans given. Loans under reverse repurchase agreements amount to HRK 1 million (2011: HRK 5 million).

20 | Financial assets available for sale (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Debt securities	31	812	21	101
Equity securities	60	173	60	88
	91	**985**	**81**	**189**

	GROUP		BANK	
a) Available-for-sale debt securities	2012	2011	2012	2011
Corporate debt securities	20	22	20	22
Ministry of Finance treasury bills	10	637	-	-
Republic of Croatia bonds	-	120	-	65
Other securities issued by domestic issuers	-	18	-	-
Bonds issued by EU member state governments	-	11	-	11
	30	**808**	**20**	**98**
Accrued interest	1	4	1	3
	31	**812**	**21**	**101**
Listed securities	21	175	21	101
Unlisted securities	10	637	-	-
	31	**812**	**21**	**101**

	GROUP		BANK	
b) Available-for-sale equity securities	2012	2011	2012	2011
Listed securities	17	116	17	31
Unlisted securities	43	57	43	57
	60	**173**	**60**	**88**

20 | Financial assets available for sale / continued

Following the on set of the global financial crisis, the Group considered, during 2009, that market conditions for Croatian corporate and government bonds no longer enabled active trading.
As the Group had the ability and intention to hold these assets to maturity and they satisfied the definition of loans and receivables at the time, the Group decided to reclassify these securities from the available-for-sale portfolio to loans and receivables.
For details, please refer to Note 41 Fair values of financial assets and liabilities - reclassification of financial assets. There were no further reclassifications after 2009.
The following table summarises the Bank's and Group's holdings in unquoted equity investments classified as available for sale.

EQUITY INVESTMENTS	COUNTRY	NATURE OF BUSINESS	2012	2011
			holding %	
Quaestus Private Equity Kapital	Croatia	investment finance	29	29
Quaestus Private Equity Kapital II otvoreni investicijski fond	Croatia	investment finance	4	4
Europay Hrvatska d.o.o.	Croatia	card services	13	13
Hrvatski registar obveza po kreditima d.o.o.	Croatia	financial services	15	15
Tehnološko inovacijski centar d.o.o.	Croatia	manufacturing	11	11
Agromeđimurje d.d.	Croatia	agriculture	10	10
Tržište novca i kratkoročnih vrijednosnica d.d.	Croatia	financial services	8	8
Međimurske novine d.o.o.	Croatia	newspaper	7	7
Brodogradilište Viktor Lenac	Croatia	shipbuilding	-	2
Zagrebačka burza d.d.	Croatia	financial services	3	3
Bioinstitut d.o.o.	Croatia	manufacturing	2	2
Središnje klirinško depozitarno društvo d.d.	Croatia	financial services	1	1
Elan d.d.	Slovenia	manufacturing	1	1

The Group holds 29% (2011: 29%) of the ordinary issued share capital of Quaestus Private Equity Kapital, a private equity investment fund ("the Fund"). The Group does not consider itself to have a significant influence over the Fund because the Group does not have the power to participate in the Fund's financial and operating policy decisions.

21 | Held-to-maturity investments (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Republic of Croatia bonds	204	263	-	-
Recapitalisation bonds	-	78	-	78
Rehabilitation bonds	-	42	-	42
Accrued interest	4	8	-	4
	208	**391**	**-**	**124**

Republic of Croatia bonds relate to bonds issued by the Ministry of Finance of the Republic of Croatia. They are denominated in EUR, bear interest rates from 4.25% to 6.875% and mature from 2012 to 2019.

Recapitalisation bonds and rehabilitation bonds were issued by the State Agency for Bank Rehabilitation and Deposit Insurance (DAB). These bonds were denominated in HRK, with an interest rate of 5% and were payable semi annually and matured in 2011.

22 | Investments in subsidiaries and associates (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Consolidated subsidiaries	-	-	182	351
Associates accounted for under the equity method by the Group and at cost by the Bank	151	135	38	38
	151	**135**	**220**	**389**
Movements				
Balance at 1 January	**135**	**128**	**389**	**392**
Share of profits from associates	16	18	-	-
Receipt of dividend	-	(11)	-	-
Effect of merger with Međimurska banka	-	-	(169)	-
Impairment	-	-	-	(3)
Balance at 31 December	**151**	**135**	**220**	**389**

22 | Investments in subsidiaries and associates / continued

The principal investments in subsidiaries and associates as at 31 December are as follows:

CONSOLIDATED SUBSIDIARIES	COUNTRY	NATURE OF BUSINESS	2012 holding %	2011 holding %
Međimurska banka d.d.	Croatia	banking	*	100
PBZ Card d.o.o.	Croatia	card services	100	100
PBZ Leasing d.o.o.	Croatia	leasing	100	100
PBZ Invest d.o.o.	Croatia	asset management	100	100
PBZ Nekretnine d.o.o.	Croatia	real estate agency	100	100
PBZ Stambena štedionica d.d.	Croatia	housing savings bank	100	100
ASSOCIATES				
PBZ Croatia osiguranje d.d.	Croatia	pension management	50	50
Intesa Sanpaolo Card Zagreb d.o.o.	Croatia	card services	31	31

*As disclosed later in this Note, as at 1 December 2012 Međimurska banka was legally merged into the Bank.

The Group considers that its 50% investment in PBZ Croatia osiguranje d.d. represents an investment in an associate, as the Group does not have control over PBZ Croatia osiguranje d.d.. Consequently, PBZ Croatia osiguranje d.d. and Intesa Sanpaolo Card d.o.o. Zagreb are accounted for using the equity method in the consolidated financial statements. The following table illustrates summarised financial information of the Group's investment in associates:

(in HRK million)	2012	2011
Share of the associates' statement of financial position		
Current assets	116	113
Non-current assets	50	49
Current liabilities	(9)	(21)
Non-current liabilities	(6)	(6)
Bank's share in net assets of associates	**151**	**135**
Share of profit or loss from associates		
Revenue	117	113
Expenses	(101)	(95)
Profit	**16**	**18**

22 | Investments in subsidiaries and associates / continued

Merger of Međimurska banka

As of 1 December 2012 Međimurska banka was legally merged into the Bank, whereby Međimurska banka ceased to exist as a separate legal and operational financial institution. The assets and liabilities acquired by the Bank as a result of the merger are recognised at the carrying amounts recognised immediately prior to the merger in the financial statements of Međimurska banka. The components of equity of Međimurska banka were added to the same components within the Bank's equity except for issued capital and pre-acquisition earnings which were eliminated on merger.

The carrying values of assets and liabilities of Međimurska banka as at 30 November 2012, the date that preceded the merger were as follows:

(in HRK million)	**30 November 2012**
Cash and current accounts with Privredna banka Zagreb	339
Cash and current accounts held outside Privredna banka Zagreb	382
Balances with the Croatian National Bank	615
Loans and advances to banks	217
Financial assets available for sale	6
Loans and advances to customers	1,269
Property and equipment	23
Investment property	2
Deferred tax assets	3
Other assets	43
Current accounts and deposits from banks	(4)
Current accounts and deposits from customers	(2,353)
Interest-bearing borrowings	(108)
Provisions for liabilities and charges	(4)
Other liabilities	(24)
Net identifiable assets of Međimurska banka	**406**
Goodwill previously recognised on consolidation and subsequently recognised as purchased goodwill upon the merger of Međimurska banka into the Bank	14
	420
Less: carrying value of the investment in the subsidiary	(169)
Net identifiable assets added to the Bank	**251**
Merger of subsidiary - increase in reserves of the Bank	
Other reserves	8
Fair value reserve	(1)
Post-acquisition retained earnings	244
	251

23 | Intangible assets (in HRK million)

	Goodwill	Software	Other intangible assets	Assets acquired but not brought into use	Total
Group					
Acquisition cost					
Balance at 1 January 2011	**72**	**324**	**5**	**3**	**404**
Additions	-	-	-	53	**53**
Impairment loss	(3)	-	-	-	**(3)**
Disposals	-	(1)	-	-	**(1)**
Transfer in use	-	47	-	(47)	**-**
Balance at 31 December 2011	**69**	**370**	**5**	**9**	**453**
Additions	-	-	-	46	**46**
Transfer in use	-	50	-	(50)	**-**
Balance at 31 December 2012	**69**	**420**	**5**	**5**	**499**
Accumulated amortisation					
Balance at 1 January 2011	**-**	**256**	**2**	**-**	**258**
Charge for the year	-	37	1	-	**38**
Balance at 31 December 2011	**-**	**293**	**3**	**-**	**296**
Charge for the year	-	40	1	-	**41**
Balance at 31 December 2012	**-**	**333**	**4**	-	**337**
Carrying value					
Balance at 31 December 2011	**69**	**77**	**2**	**9**	**157**
Balance at 31 December 2012	**69**	**87**	**1**	**5**	**162**

At 31 December 2011, goodwill represents goodwill arising on consolidation. At 31 December 2012, following the merger of the Bank with its subsidiary, Međimurska banka, the goodwill previously arising on consolidation with that subsidiary has been recognised as purchased goodwill by the Group and Bank. Consequently, goodwill at 31 December 2012 recognised by the Group comprises goodwill arising on consolidation of HRK 55 million and purchased goodwill of HRK 14 million.

23 | Intangible assets / continued (in HRK million)

	Goodwill	Software	Assets acquired but not brought into use	Total
Bank				
Acquisition cost				
Balance at 1 January 2011	**-**	**294**	**3**	**297**
Additions	-	-	50	50
Transfer in use	-	44	(44)	-
Balance at 31 December 2011	**-**	**338**	**9**	**347**
Acquired on merger with Međimurska banka	14	-	-	**14**
Additions	-	-	43	**43**
Transfer in use	-	50	(50)	-
Balance at 31 December 2012	**14**	**388**	**2**	**404**
Accumulated amortisation				
Balance at 1 January 2011	**-**	**230**	**-**	**230**
Charge for the year	-	34	-	34
Balance at 31 December 2011	**-**	**264**	**-**	**264**
Charge for the year	-	37	-	**37**
Balance at 31 December 2012	**-**	**301**	**-**	**301**
Carrying value				
Balance at 31 December 2011	**-**	**74**	**9**	**83**
Balance at 31 December 2012	**14**	**87**	**2**	**103**

Following the legal merger of Međimurska banka into the Bank as at 1 December 2012, the goodwill formerly arising on consolidation of Međimurska banka was transformed into purchased goodwill and recognised in the Bank's separate statement of financial position.

24 | Property and equipment (in HRK million)

Group	Land and buildings	Furniture and other equipment	Motor vehicles	Computer equipment	Leasehold improve-ments	Asset acquired but not brought into use	Total
Acquisition cost							
Balance at 1 January 2011	**1,080**	**429**	**307**	**565**	**226**	**7**	**2,614**
Additions	-	-	-	1	-	249	**250**
Transfer to non-current assets held for sale	(54)	(4)	-	-	-	-	**(58)**
Disposals	(18)	(10)	(114)	(28)	(1)	-	**(171)**
Transfer into use	19	26	78	21	6	(150)	-
Balance at 31 December 2011	**1,027**	**441**	**271**	**559**	**231**	**106**	**2,635**
Additions	-	-	-	-	-	365	**365**
Transfer from investment property	2	-	-	-	-	-	**2**
Transfer from non-current asset held for sale	-	1	-	-	-	-	**1**
Disposals	(131)	(28)	(90)	(188)	(5)	(2)	**(444)**
Transfer into use	296	46	52	38	6	(438)	-
Balance at 31 December 2012	**1,194**	**460**	**233**	**409**	**232**	**31**	**2,559**
Accumulated depreciation							
Balance at 1 January 2011	**278**	**334**	**131**	**468**	**177**	**-**	**1,388**
Charge for the year	30	40	46	36	19	-	**171**
Transfer to non-current assets held for sale	(25)	(3)	-	-	-	-	**(28)**
Disposals	(6)	(10)	(56)	(28)	-	-	**(100)**
Balance at 31 December 2011	**277**	**361**	**121**	**476**	**196**	**-**	**1,431**
Charge for the year	29	34	40	28	18	-	**149**
Transfer from non-current assets held for sale	-	1	-	-	-	-	**1**
Disposals	(29)	(25)	(52)	(165)	(5)	-	**(276)**
Balance at 31 December 2012	**277**	**371**	**109**	**339**	**209**	**-**	**1,305**
Carrying value							
Balance at 31 December 2011	**750**	**80**	**150**	**83**	**35**	**106**	**1,204**
Balance at 31 December 2012	**917**	**89**	**124**	**70**	**23**	**31**	**1,254**

Real estate, furniture and other equipment and motor vehicles of the Group include assets leased under operating leases with a carrying value of HRK 450.9 million (2011: HRK 271.7 million).

24 | Property and equipment / continued (in HRK million)

Bank	Land and buildings	Furniture and other equipment	Motor vehicles	Computer equipment	Leasehold improve-ments	Asset acquired but not brought into use	Total
Acquisition cost							
Balance at 1 January 2011	**826**	**376**	**11**	**320**	**224**	**8**	**1,765**
Additions	-	-	-	-	-	38	**38**
Transfer to non-current assets held for sale	(54)	(4)	-	-	-	-	**(58)**
Disposals	(9)	(7)	(2)	(19)	(1)	-	**(38)**
Transfer in use	9	12	-	17	6	(44)	**-**
Balance at 31 December 2011	**772**	**377**	**9**	**318**	**229**	**2**	**1,707**
Acquired on merger with Međimurska banka	37	19	1	13	1	-	**71**
Additions	-	-	-	-	6	75	**81**
Transfer from non-current assets held for sale	-	1	-	-	-	-	**1**
Disposals	-	(21)	-	(35)	(5)	-	**(61)**
Transfer in use	17	19	-	37	-	(73)	-
Balance at 31 December 2012	**826**	**395**	**10**	**333**	**231**	**4**	**1,799**
Accumulated depreciation							
Balance at 1 January 2011	**236**	**304**	**6**	**261**	**175**	**-**	**982**
Charge for the year	24	31	2	30	19	-	**106**
Transfer to non-current assets held for sale	(25)	(3)	-	-	-	-	**(28)**
Disposals	(6)	(8)	(2)	(19)	(1)	-	**(36)**
Balance at 31 December 2011	**229**	**324**	**6**	**272**	**193**	**-**	**1,024**
Acquired on merger with Međimurska banka	16	17	1	13	1	-	**48**
Charge for the year	20	25	1	23	17	-	**86**
Transfer from non-current assets held for sale	-	1	-	-	-	-	**1**
Disposals	-	(21)	-	(35)	(4)	-	**(60)**
Balance at 31 December 2012	**265**	**346**	**8**	**273**	**207**	**-**	**1,099**
Carrying value							
Balance at 31 December 2011	**543**	**53**	**3**	**46**	**36**	**2**	**683**
Balance at 31 December 2012	**561**	**49**	**2**	**60**	**24**	**4**	**700**

25 | Investment property (in HRK million)

	GROUP	BANK
Acquisition cost		
Balance at 1 January 2011	**31**	**26**
Additions	-	-
Balance at 31 December 2011	**31**	**26**
Acquired on merger with Međimurska banka	-	2
Disposal	(3)	(2)
Transfer to property and equipment	(2)	-
Balance at 31 December 2012	**26**	**26**
Accumulated depreciation		
Balance at 1 January 2011	**18**	**16**
Charge for the year	1	1
Balance at 31 December 2011	**19**	**17**
Charge for the year	1	1
Disposal	(3)	(1)
Balance at 31 December 2012	**17**	**17**
Carrying value		
Balance at 31 December 2011	**12**	**9**
Balance at 31 December 2012	**9**	**9**

The estimated fair value of investment property held by the Group as at 31 December 2012 amounted to HRK 17 million (2011: HRK 30 million) and for the Bank HRK 17 million (2011: HRK 27 million). The fair value was estimated by PBZ Nekretnine, a wholly owned subsidiary of the Bank, engaged in real estate management and by an independent appraiser.
The property rental income earned by the Group and Bank from its investment property, all of which was leased out under operating leases, amounted to HRK 2.5 million (2011: HRK 2.4 million), and was presented within other operating income (Note 9).

26| Non-current assets held for sale (in HRK million)

In 2011, the Bank's management resolved to dispose of two office buildings together with related fixtures and fittings and signed the contracts with respective buyers. The assets were therefore reclassified as non-current assets held for sale and presented separately in the statement of financial position.
The transactions were closed in 2012 and the Bank as at 31 December 2011 realised profit on disposal of HRK 5 million (Note 9). Since furniture and equipment were not sold with the premises, the Group reclassified them as property and equipment in accordance with their change in use.

	GROUP		BANK	
	2012	2011	2012	2011
Land and buildings	-	29	-	29
Furniture and other equipment	-	1	-	1
	-	**30**	**-**	**30**

27| Other assets (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Receivables from card business	208	184	95	28
Receivables from debtors	57	55	1	1
Foreclosed assets	37	34	37	24
Accrued fees	30	32	39	42
Advance payments	28	26	27	25
Prepaid expenses	27	20	21	13
Receivables in course of collection	18	9	12	5
Receivables from Tax Authorities	6	35	-	-
Other assets	63	96	24	66
	474	**491**	**256**	**204**

28| Current accounts and deposits from banks (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Term deposits	522	2,665	898	3,079
Demand deposits	205	329	210	344
	727	**2,994**	**1,108**	**3,423**

29 | Current accounts and deposits from customers (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
a) Analysis by term				
Term deposits	32,623	32,420	31,476	30,021
Demand deposits	15,520	15,011	15,497	14,060
	48,143	**47,431**	**46,973**	**44,081**
b) Analysis by source				
Retail deposits	38,252	36,813	36,969	33,674
Corporate deposits	5,682	5,975	5,796	5,798
Public sector and other institutions	4,209	4,643	4,208	4,609
	48,143	**47,431**	**46,973**	**44,081**

30 | Interest-bearing borrowings (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Domestic borrowings	2,351	2,444	2,351	2,363
Foreign borrowings	6,582	6,864	5,564	5,624
Refinanced debt	3	3	3	3
	8,936	**9,311**	**7,918**	**7,990**

a) Domestic borrowings
Domestic borrowings of the Group mainly consist of loans received from the Croatian Bank for Reconstruction and Development ("HBOR") in the amount of HRK 1.5 billion (2011: HRK 1.2 billion) out of which payables under repurchase agreements with HBOR amounted to HRK 738 million (2011: HRK 839 million).
In accordance with the overall agreement, borrowings from HBOR are used to fund loans to customers for eligible construction and development projects at preferential interest rates.

b) Foreign borrowings
Foreign borrowings of the Group include short-term and long-term loans received from foreign banks and non-financial institutions denominated mostly in EUR and CHF and with floating interest rates.

31 | Other liabilities (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Payables to suppliers	1,166	1,154	73	49
Items in the course of settlement and other liabilities	264	350	245	305
Salaries and other personnel costs	88	129	76	107
	1,518	**1,633**	**394**	**461**

32 | Accrued expenses and deferred income (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Accrued expenses	114	110	62	59
Deferred income	87	84	19	15
	201	**194**	**81**	**74**

33 | Provisions for liabilities and charges (in HRK million)

GROUP	Total	Provisions for off-balance sheet items	Provisions for court cases	Provisions for other items
Balance as at 1 January 2012	**191**	**146**	**34**	**11**
Net charge in the income statement	30	15	6	9
Provisions used during the year	(18)	(3)	(4)	(11)
Foreign exchange loss	1	1	-	-
Balance as at 31 December 2012	**204**	**159**	**36**	**9**
Balance as at 1 January 2011	**214**	**142**	**57**	**15**
Net charge/(release) in the income statement	9	1	(5)	13
Provisions used during the year	(35)	-	(18)	(17)
Foreign exchange loss	3	3	-	-
Balance as at 31 December 2011	**191**	**146**	**34**	**11**

33 | Provisions for liabilities and charges / continued (in HRK million)

Bank	Total	Provisions for off-balance sheet items	Provisions for court cases	Provisions for other items
Balance as at 1 January 2012	**186**	**145**	**30**	**11**
Acquired on merger of Međimurska banka	4	3	1	-
Net charge in the income statement	28	13	6	9
Provisions used during the year	(15)	-	(4)	(11)
Foreign exchange loss	1	1	-	-
Balance as at 31 December 2012	**204**	**162**	**33**	**9**
Balance as at 1 January 2011	**206**	**139**	**52**	**15**
Net charge/(release) in the income statement	14	6	(5)	13
Provisions used during the year	(34)	-	(17)	(17)
Balance as at 31 December 2011	**186**	**145**	**30**	**11**

Provisions for off-balance sheet items, court cases and other items are recognised in other impairment losses and provisions in the income statement (Note 11).
As at 31 December 2012 there were several litigation cases taken against the Group. In the opinion of management, there is a probability that the Group may lose certain cases, in respect of which management has recognised provisions for court cases as at 31 December 2012 in the amount of HRK 36 million (2011: HRK 34 million) and HRK 33 million (2011: HRK 30 million), for the Group and the Bank, respectively.

34 | Contingent liabilities and commitments (in HRK million)

Credit related contingencies and commitments

Credit-related contingencies and commitments arise from various banking products, the primary purpose of which is to ensure that funds are available to a customer when required. Guarantees and standby letters of credit, which represent irrevocable assurances that the Group will make payments in the event that customers cannot meet their obligations to third parties, carry the same credit risk as loans and advances. Documentary and commercial letters of credit, which are written undertakings by the Group on behalf of a customer authorising a third party to draw funds on the Group up to a stipulated amount under specific terms and conditions, are collateralised by the underlying shipments of goods to which they relate and therefore have significantly lower risk. Management has assessed that a provision of HRK 159 million for the Group and HRK 162 million for the Bank is sufficient to cover risks due to the default of the respective counterparties (refer to Note 33).

34 | Contingent liabilities and commitments / continued (in HRK million)

The aggregate amounts of outstanding guarantees, letters of credit and other commitments at the end of the year were as follows:

	GROUP		BANK	
	2012	2011	2012	2011
Undrawn lending commitments	8,417	9,668	8,480	9,422
Performance guarantees	1,858	1,842	1,858	1,819
HRK guarantees	333	483	335	452
Foreign currency guarantees	478	334	478	331
Foreign currency letters of credit	176	310	176	310
Factoring and forfaiting	40	27	40	27
Other contingent liabilities	20	20	18	20
	11,322	**12,684**	**11,385**	**12,381**

On 31 December 2012 the Group and the Bank had long-term commitments as lessees in respect of rent for business premises and equipment lease agreements expiring between 2013 and 2017. The future minimum commitments for each of the next five years are presented below:

	2012	2013	2014	2015	2016	2017	Total
GROUP							
Premises	46	49	49	50	50	51	**295**
	46	**49**	**49**	**50**	**50**	**51**	**295**
BANK							
Premises	67	75	75	76	76	77	**446**
Equipment	9	9	9	9	9	9	**54**
	76	**84**	**84**	**85**	**85**	**86**	**500**

35 | Share capital (in HRK million)

a) Issued share capital
Issued share capital as at 31 December 2012 amounted to HRK 1,907 million (31 December 2011: HRK 1,907 million). The total number of authorised registered shares at 31 December 2012 was 19,074,769 (2011: 19,074,769) with a nominal value of HRK 100 per share (2011: HRK 100 per share). The parent company of the Bank is Intesa Sanpaolo Holding International and the ultimate controlling party is Intesa Sanpaolo S.p.A.
The ownership structure as at 31 December 2012 and 31 December 2011 was as follows:

	REGISTERED SHARES			
	31 December 2012		31 December 2011	
	Number of shares	Percentage of ownership	Number of shares	Percentage of ownership
Intesa Sanpaolo Holding International	14,609,532	76.6%	14,609,532	76.6%
EBRD	3,981,990	20.9%	3,981,990	20.9%
Non-controlling shareholders	418,574	2.2%	418,574	2.2%
Treasury shares	64,673	0.3%	64,673	0.3%
	19,074,769	**100.0%**	**19,074,769**	**100.0%**

The Bank's shares are listed on the Zagreb Stock Exchange. As at 31 December 2012 the share price of the Bank's ordinary shares quoted on the Zagreb Stock Exchange was HRK 510 (31 December 2011: HRK 475).

On 31 December 2012, the President of the Management Board Mr Božo Prka held 361 shares of Privredna banka Zagreb, and of the other members of the Management Board, Mr Ivan Gerovac held 120 shares and Mr Draženko Kopljar held 108 shares.

b) Share premium
The Bank recognises share premium in an amount of HRK 1,570 million (31 December 2011: HRK 1,570 million) representing the excess of the paid-in amount over the nominal value of the issued shares.

c) Treasury shares
During 2011 and 2012 there were no movements in treasury shares.

d) Other reserves
Other reserves comprise legal reserve, capital gains, treasury share reserve.

Legal reserve
As required by the Companies Act, companies in Croatia are required to appropriate 5% of their annual net profit into legal reserves until they, together with capital reserves, reach 5% of issued share capital.

Capital gains
Capital gain is a result of transactions with treasury shares of the Bank in previous periods.

Treasury share reserve
During 2012 the Bank did not purchase any treasury shares on the open market for its own purposes.

e) Fair value reserve
Fair value reserve includes unrealised gains and losses on changes in the fair value of financial assets available for sale, net of income tax. As at 31 December 2012 the accumulated loss on fair value reserve amounted to HRK 27 million (31 December 2011: accumulated loss of HRK 48 million) and HRK 8 million (31 December 2011: accumulated loss of HRK 11 million) for the Group and the Bank, respectively.

35 | Share capital / continued (in HRK million)

f) Retained earnings
Retained profits are generally available to shareholders, subject to their approval.
The amount of dividends distributable to equity holders during 2012 in respect of 2011 is HRK 29.90 (2011 in respect of 2010: HRK 15.85) per share.

g) Non-distributable reserves
Management considers that the fair value reserve and other reserves may not be distributed to shareholders. As at 31 December 2012 non-distributable reserves amount to HRK 348 million for the Group (31 December 2011: HRK 327 million) and HRK 300 million for the Bank (31 December 2011: HRK 289 million).

36 | Cash and cash equivalents (in HRK million)

The table below presents an analysis of cash and cash equivalents for the purposes of the cash flows statement:

	NOTES	GROUP		BANK	
		2012	2011	2012	2011
Cash and current accounts with banks	14	4,171	2,647	4,168	2,465
Loans and advances to banks with maturity of up to 90 days		5,136	6,567	5,147	6,323
Other deposits with the CNB	15	800	1,810	800	1,800
		10,107	**11,024**	**10,115**	**10,588**

37 | Managed funds for and on behalf of third parties (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Assets under custody	5,370	5,448	5,370	5,448
Assets under custody - investment funds	890	1,092	890	1,092
Assets under portfolio management	981	875	981	875
	7,241	**7,415**	**7,241**	**7,415**

Assets under portfolio management managed by the Group represent funds for and on behalf of third parties. These assets are accounted for separately from those of the Group and kept off balance sheet. Income and expenses arising from these funds are credited and charged to the corresponding sources and no liability falls on the Group in connection with these transactions. The Group is compensated for its services by fees chargeable to the clients.
Moreover, the Group also manages funds of its clients in terms of mutual investment funds and an obligatory pension fund. In that context, funds under management in mutual investment funds as at 31 December 2012 amounted to HRK 2,271 million (2011: HRK 1,980 million), out of which, HRK 890 million are assets under custody of the Bank (2011: HRK 1,092 million), while the remainder are held by custodians outside the Group.
Funds under management in the obligatory pension fund managed by the Bank's associate PBZ Croatia osiguranje d.d. amount to HRK 8,353 million as at 31 December 2012 (2011: HRK 6,851 million). These funds are held by a custody bank which is not a member of the Group.

38 | **Leases** (in HRK million)

PBZ Leasing d.o.o., a company wholly-owned by the Bank, is engaged in providing finance and operating lease arrangements to its clients of various items of vehicles, vessels, real estate and equipment. Net investment in finance leases as at 31 December 2012 amounted to HRK 836.6 million (31 December 2011: HRK 791.1 million) which is included within loans and advances to customers (Note 19) in the Group financial statements. The carrying value of leased property and equipment under operating lease as at 31 December 2012 amounted to HRK 450.9 million (31 December 2011: HRK 271.7 million) and are classified within property and equipment (Note 24).
Future minimum lease payments under finance leases together with the present value of the net minimum lease payments are set out below:

	Minimum payments 2012	Present value of payments 2012	Minimum payments 2011	Present value of payments 2011
Less than one year	250	201	256	214
Between one and five years	491	374	502	396
More than five years	441	360	322	268
Gross investment in finance lease	**1,182**	**935**	**1,080**	**878**
Unearned finance income	(247)	-	(202)	-
	935	**935**	**878**	**878**
Less: Impairment allowance	(98)	(98)	(87)	(87)
Net investment in finance lease	**837**	**837**	**791**	**791**

Future minimum lease payments at undiscounted amounts under non-cancellable operating leases where the Group is the lessor are as follows:

	2012	2011
Less than one year	183	64
Between one and five years	140	116
More than five years	114	59
	437	**239**

39 | Related party transactions

The parent company of Privredna banka Zagreb d.d. and its subsidiaries is Intesa Sanpaolo Holding International which holds 76.6% of the Bank's share capital as at 31 December 2012. The ultimate controlling party is Intesa Sanpaolo S.p.A., a bank incorporated in Italy. The remaining shareholders are the European Bank for Reconstruction and Development (20.9%) and publicly held shareholders (2.2%).
The Bank considers that it has an immediate related party relationship with its ultimate parent and its affiliates, with other key shareholders and their affiliates; its subsidiaries and associates, the investment funds managed by one of its subsidiaries, PBZ Invest d.o.o.; the pension fund managed by its associate, PBZ Croatia osiguranje d.d., Supervisory Board members, Management Board members and other executive management (together "key management personnel") and close family members of key management personnel, in accordance with the International Accounting standard 24 "Related party Disclosures" ("IAS 24").
The Bank grants loans to or places deposits with related parties in the ordinary course of business.
The volumes of related party transactions during the year and outstanding balances at the year-end were as follows:

(in HRK million)	Key management personnel	Ultimate controlling party - Intesa Sanpaolo S.p.A	Associates	Other shareholders and their affiliates and affiliates of ultimate controlling party
Group				
Deposits and loans given				
Balance at 1 January 2012	**16**	**405**	**-**	**209**
Changes during the year	(2)	330	-	(208)
Balance at 31 December 2012	**14**	**735**	**-**	**1**
Interest income for the year ended 31 December 2012	**1**	**4**	**-**	**5**
Interest income for the year ended 31 December 2011	1	13	-	1
Deposits and loans received				
Balance at 1 January 2012	**38**	**112**	**61**	**5,701**
Changes during the year	3	(8)	(3)	10
Balance at 31 December 2012	**41**	**104**	**58**	**5,711**
Interest expense for the year ended 31 December 2012	**(1)**	**(11)**	**(2)**	**(158)**
Interest expense for the year ended 31 December 2011	(1)	(23)	(2)	(140)
Contingent liabilities and commitments at 31 December 2012	**2**	**1**	**16**	**15**
Contingent liabilities and commitments at 31 December 2011	2	1	20	15
Fees and other income for the year ended 31 December 2012	**-**	**11**	**2**	**12**
Fees and other income for the year ended 31 December 2011	-	-	12	10
Fees and other expense for the year ended 31 December 2012	**(1)**	**1**	**(44)**	**(2)**
Fees and other expense for the year ended 31 December 2011	(6)	(1)	(39)	(2)

39 | Related party transactions / continued

(in HRK million)	Key management personnel	The Bank's subsidiaries	Ultimate controlling party - Intesa Sanpaolo S.p.A	Associates	Other shareholders and their affiliates and affiliates of ultimate controlling party
Bank					
Deposits and loans given					
Balance at 1 January 2012	**14**	**686**	**405**	**-**	**14**
Changes during the year	(2)	(351)	330	-	(14)
Balance at 31 December 2012	**12**	**335**	**735**	**-**	**-**
Interest income for the year ended 31 December 2012	1	15	4	-	-
Interest income for the year ended 31 December 2011	1	24	13	-	1
Deposits and loans received					
Balance at 1 January 2012	**30**	**650**	**112**	**61**	**4,466**
Changes during the year	3	(131)	(8)	(3)	34
Balance at 31 December 2012	**33**	**519**	**104**	**58**	**4,500**
Interest expense for the year ended 31 December 2012	(1)	(17)	(11)	(2)	(114)
Interest expense for the year ended 31 December 2011	(1)	(9)	(23)	(2)	(102)
Contingent liabilities and commitments at 31 December 2012	**2**	**65**	**1**	**16**	**15**
Contingent liabilities and commitments at 31 December 2011	2	121	1	20	15
Lease expense for the year ended 31 December 2012	**-**	**(17)**	**-**	**-**	**-**
Lease expense for the year ended 31 December 2011	-	(13)	-	-	-
Fees and other income for the year ended 31 December 2012	**-**	**188**	**11**	**2**	**12**
Fees and other income for the year ended 31 December 2011	-	214	-	12	10
Fees and other expense for the year ended 31 December 2012	**(1)**	**(54)**	**1**	**(44)**	**(2)**
Fees and other expense for the year ended 31 December 2011	-	(50)	(1)	(39)	(2)

No provisions were recognised in respect of deposits and loans given to related parties (2011: nil).

39| Related party transactions / continued

Annual key management remuneration:

	GROUP		BANK	
(in HRK million)	2012	2011	2012	2011
Personnel compensation (gross)	41	38	32	26
Bonuses	18	21	14	16
Contributions to pension insurance	4	5	3	3
	63	**64**	**49**	**45**

Key management personnel include Management Board and Supervisory Board members, as well as senior executive directors or executive directors responsible for areas of strategic relevance. The total number of key management personnel of the Group and the Bank as at 31 December 2012 was 37 (31 December 2011: 38) and 23 (31 December 2011: 26), respectively.

All bonuses in 2012 and 2011 were paid in cash, while for two executives in 2012 bonus also included share allocation on deferred basis.

Share-based payments

In July 2012, the Board of Directors of Intesa Sanpaolo S.p.A. launched a new long-term scheme, in favour of 2 executives holding key positions in the Group, aimed at achieving business plan objectives and increasing the value of the Intesa Sanpaolo Group.
This scheme entitles the key executives to a cash payment, based on the price of Intesa Sanpaolo S.p.A. shares, if certain performance conditions are fulfilled. The fair value of services received from key executives is measured by reference to the fair value of the instrument granted which is based on the quoted market prices of Intesa Sanpaolo S.p.A. shares.

	Number of instruments granted (in units)	The carrying amount of liabilities for cash-settled (in HRK million)
Awards granted during the period	338,451	3

40| Capital

The Bank maintains an actively managed capital base to cover risks in the business. The adequacy of the Bank’s capital is monitored using, among other measures, the rules and ratios established by the Croatian National Bank in supervising the Bank.

Capital management

The primary objectives of the Bank's capital management are to ensure that the Bank complies with externally imposed capital requirements and that the Bank maintains strong credit ratings and healthy capital ratios in order to support its business and to maximise shareholders' value.

The Bank manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payments to shareholders, return capital to shareholders or issue capital securities. No changes were made in the objectives, policies and processes from the previous year.

Regulatory capital and capital adequacy ratio according to CNB requirements, calculated for the Bank only (as of the date of issuance of these financial statements information on risk-weighted assets is unaudited), are as follows:

40 Capital / continued

Regulatory capital

	BANK	
(in HRK million)	**2012**	**2011**
Tier 1 capital		
Issued share capital	1,907	1,907
Share premium	1,570	1,570
Treasury shares	(76)	(76)
Retained earnings (excluding profit for the period)	7,179	6,368
Profit for the period, decreased by proposed dividend	2	568
Other reserves (adjusted)	291	287
Deductions in accordance with CNB regulations	(140)	(31)
Total qualifying Tier 1 capital	**10,733**	**10,593**
Total qualifying Tier 2 capital	-	-
Deductions	(219)	(371)
Total regulatory capital	**10,514**	**10,222**
Risk weighted assets and other risk elements (unaudited)	**48,230**	**47,424**
Tier 1 capital ratio	**22.25%**	**22.34%**
Capital adequacy ratio	**21.80%**	**21.55%**

Regulatory capital consists of Tier 1 capital, which comprises share capital, share premium, and retained earnings including current year profit, but excluding proposed dividends and adjusted other reserves.

The minimum regulatory ratio on capital adequacy is 12% at the end of both observed periods.

41 | Fair values of financial assets and liabilities

Fair value represents the amount at which an asset could be exchanged or a liability settled on an arm's length basis. Financial assets and financial liabilities at fair value through profit or loss are measured at fair value. Loans and advances to customers and held-to-maturity investments are measured at amortised cost less impairment. Available-for-sale instruments are generally measured at fair value with the exception of some equity investments which are carried at cost less impairment given the lack of quoted market prices in an active market or whose fair value cannot be reliably measured.
The following methods and assumptions have been made in estimating the fair value of financial instruments:

- Loans and advances to banks and customers are presented net of specific and collective provisions. The estimated fair value of loans and advances represents the discounted amount of the estimated future cash flows expected to be received. Expected future cash flows are estimated considering credit risk of counterparty and any indication of impairment. As the Group has a limited portfolio of loans and advances with fixed interest rates and longer-term maturities, the Group estimates that the fair value of loans and advances is not significantly different from their carrying value;
- Financial assets and liabilities at fair value through profit or loss and financial assets available for sale are carried at fair value which is based on their market prices. Where a quoted market price is not available, the fair value is estimated using valuation techniques, described later in this Note. The amount of equity investments carried at cost less impairment is not significant;
- The fair value of securities held to maturity for the Group is estimated to be HRK 212 million (2011: HRK 381 million) and for the Bank HRK nil (2011: HRK 124 million) with carrying values of HRK 208 million (2011: HRK 391 million) and HRK nil (2011: HRK 124 million) for the Group and the Bank respectively;
- For demand deposits and deposits with no defined maturities, the fair value is determined to be the amount payable on demand at the reporting date;
- Most of the Group's long-term deposits and interest-bearing borrowings bear floating interest rates which are linked to market and reprice regularly. As such, the management believes that the carrying value of the long-term deposits and borrowings approximates their fair value;

The Group estimates that there are no significant differences between the carrying values and the fair values of financial assets and liabilities.

Determination of fair value and fair value hierarchy

The determination of fair value of financial assets and liabilities for which there is no observable market price requires the use of valuation techniques. For financial instruments that trade infrequently and have little price transparency, fair value is less objective, and for this reason, when calculating the fair value of a financial asset or liability all material risks that affect them must be identified and taken into consideration.
When measuring fair values the Bank takes into account the IFRS fair value hierarchy that reflects the significance of the inputs used in making the measurement. Each instrument is individually evaluated. The levels are determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety.
The financial instruments carried at fair value have been categorised under the three levels of the IFRS fair value hierarchy as follows:

Level 1: Instruments value using quoted (unadjusted) prices in active markets for identical assets or liabilities; These are instruments where the fair value can be determined directly from prices which are quoted in active, liquid markets.

- These instruments include: liquid debt and equity securities traded on liquid markets.

Level 2: Instruments valued with valuation techniques using observable market data. These are instruments where the fair value can be determined by reference to similar instruments trading in active markets, or where a technique is used to derive the valuation but where all inputs to that technique are observable.

- These instruments include: less-liquid debt and equity securities valued by a model which uses Level 1 inputs.

41 | Fair values of financial assets and liabilities / continued

Determination of fair value and fair value hierarchy / continued

Level 3: Instruments valued with a valuation techniques using market data which is not directly observable: these are instruments where the fair value cannot be determined directly by reference to market-observable information, and some other pricing technique must be employed. Instruments classified in this category have an element which is unobservable and which has a significant impact on the fair value.
These instruments include: illiquid debt securities and illiquid equity securities.

The following table presents an analysis of financial instruments carried at fair value by the level of hierarchy:

(in HRK million)

Group				2012				2011
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Derivative financial assets	-	4	-	**4**	-	11	-	**11**
Financial assets held for trading	18	-	-	**18**	27	-	-	**27**
Financial assets initially designated at fair value through profit or loss	-	3,637	225	**3,862**	-	2,060	358	**2,418**
Financial assets available for sale	17	10	63	**90**	243	659	79	**981**
Financial assets	**35**	**3,651**	**288**	**3,974**	**270**	**2,730**	**437**	**3,437**
Derivative financial liabilities	-	4	-	**4**	-	9	-	**9**
Financial liabilities	**-**	**4**	**-**	**4**	**-**	**9**	**-**	**9**

(in HRK million)

Bank				2012				2011
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Derivative financial assets	-	4	-	**4**	-	11	-	**11**
Financial assets held for trading	18	-	-	**18**	27	-	-	**27**
Financial assets initially designated at fair value through profit or loss	-	3,579	225	**3,804**	-	2,060	358	**2,418**
Financial assets available for sale	17	-	63	**80**	31	76	79	**186**
Financial assets	**35**	**3,583**	**288**	**3,906**	**58**	**2,147**	**437**	**2,642**
Derivative financial liabilities	-	4	-	**4**	-	9	-	**9**
Financial liabilities	**-**	**4**	**-**	**4**	**-**	**9**	**-**	**9**

The existence of published prices quotations in an active market is the best evidence of fair value and these quoted prices (Effective Market Quotes) shall therefore be used as the primary method for measuring financial assets and liabilities in the trading portfolio. If the market for a financial instrument is not active, the Group determines the fair value by using a valuation technique. Valuation techniques include:

- using market values which are indirectly connected to the instrument being measured, deriving from products with similar risk characteristics (Comparable Approach);
- valuations conducted using – even only in part – inputs not deriving from parameters observable on the market, for which estimates and assumptions formulated by the assessor are used (Mark-to-Model).

41 | Fair values of financial assets and liabilities / continued

Given the uncertainties of the domestic market, primarily characterised by low liquidity where market conditions do not show active trading but rather inactive, the Group primarily uses valuation techniques based on the following principles:

- Used yield curves are created from interest rate quotations observed on the market;
- An appropriate yield curve (the one that is associated with the same currency in which the security, whose price is modelled, is denominated) is used in discounting of all the security's cash flows in order to determine its present value;
- In determining the fair value of bonds issued by corporate issuers and municipality bonds, the Group additionally uses the spreads associated with the internal credit rating of the issuer, which is then added to the yield curve for valuation thus capturing credit risk and various other counterparty related risks.

During 2012 and 2011 there were no significant transfers of financial assets between hierarchy levels.

Reclassification of financial assets

2009 was characterised by substantial deterioration in global market conditions, including a severe shortage of liquidity and credit availability. These conditions led to a reduction in the level of market activity for many assets and the inability to sell assets other than at substantially lower prices.
In October 2008, the International Accounting Standards Board ("IASB") issued amendments to IAS 39 "Financial Instruments: Recognition and Measurement" and IFRS 7 "Financial instruments: Disclosures". Pursuant to these amendments, in 2009 the Group decided to reclassify Croatian Government bonds and commercial papers from the portfolio of financial instruments at fair value through profit or loss (held for trading) and the available-for-sale portfolio to the loans and receivables portfolio. For the reclassified assets the Group has the intention and ability to hold the reclassified financial instruments for the foreseeable future or until maturity. Following reclassification, the fair values of those assets are derived using the model as described above.
Upon reclassification of financial assets to loans and receivables category, the fair value of the financial assets immediately prior to the reclassification becomes the new amortised cost. Following reclassification of a financial asset available for sale with a fixed maturity, any gain or loss previously recognised in other comprehensive income, and the difference between the newly established cost and the maturity amount are both amortised over the remaining term of the financial asset using the effective interest method. For a financial asset available for sale with no stated maturity, any gain or loss previously recognised in other comprehensive income is reclassified from other comprehensive income to profit or loss when the financial asset is disposed of or impaired.
The following tables present the carrying amount and fair value of financial assets reclassified from "Held-for-Trading" and from "Available-for-Sale" to the "Loans and Receivables" category, at the reporting date.
All transfers occurred on 30 April 2009. There were no other reclassifications prior or after 30 April 2009.

(in HRK million)

	GROUP			BANK		
31 December 2012	Amounts reclassified	Carrying amount	Fair value	Amounts reclassified	Carrying amount	Fair value
Financial assets reclassified from held for trading to loans and receivables	1,903	1,958	2,014	1,903	1,958	2,014
Financial assets reclassified from available for sale to loans and receivables	1,418	923	968	213	170	180
31 December 2011						
Financial assets reclassified from held for trading to loans and receivables	1,903	1,940	1,929	1,903	1,940	1,929
Financial assets reclassified from available for sale to loans and receivables	1,418	1,353	1,365	213	182	185

41 | Fair values of financial assets and liabilities / continued (in HRK million)

Reclassification of financial assets / continued

The following table presents gains and losses recognised in the income statement in 2012 and 2011 on assets reclassified to the loans and receivables category:

	GROUP		BANK	
	2012	2011	2012	2011
Financial assets reclassified from held for trading to loans and receivables				
Interest income	92	93	92	93
Amortisation of discount	34	34	34	34
Net impairment loss on reclassified financial assets	-	-	-	-
Financial assets reclassified from available for sale to loans and receivables				
Interest income	51	82	9	12
Amortisation of discount	16	14	4	6
Amortisation of fair value reserve	(19)	(22)	(3)	(3)
Net impairment loss on reclassified financial assets	-	-	-	-

The following table presents the fair value gains or losses that would have been recognised in the income statement or in other comprehensive income during the year if the Group had not reclassified financial assets from "Held-for-Trading" and "Available-for-Sale" to the "Loans and Receivables" category.
This disclosure is provided for information purposes only and does not reflect what has actually been recorded in the financial statements of the Group.

	GROUP		BANK	
	2012	2011	2012	2011
Financial assets reclassified from held for trading to loans and receivables				
Fair value gains and losses which would have been recognised in net trading income and net loss on translation of monetary assets and liabilities	101	(13)	101	(13)
Financial assets reclassified from available for sale to loans and receivables				
Fair value gains and losses which would have been recognised in other comprehensive income	47	(54)	8	(4)

42 | Financial information by segment

The following tables present information on the Group’s result of each reportable business segment.
The segment reporting format is based on business segments as the Group's risks and rates of return are affected predominantly by differences in the products and services produced.
The operating businesses are organised and managed separately according to the nature of the products and services provided, with each segment representing a strategic segment unit that offers different products and serve different markets. Since the Group operates predominantly in Croatia, there are no secondary (geographical) segments. Intersegment income and expenses are based on current market prices.
For management purposes, the Bank is organised into 3 operating segments based on products and services accompanied with a central supporting structure. This segmentation follows the organisational structure as reflected in internal management reporting systems, which are the basis for assessing the financial performance of the business segments and for allocating resources to the business segments.

Retail banking:	Individual customers' savings and deposits, current accounts and overdrafts, all types of consumer loans, credit cards facilities and other facilities to individual customers
Corporate banking:	Loans and other credit facilities as well as deposit and current accounts for corporate and institutional customers including medium-term funding, public sector, government agencies and municipalities as well as small and medium sized enterprises
Finance banking:	Treasury operations as well as investment banking services including corporate finance, merger and acquisition services and trading
Central structure:	All other residual activities

Furthermore, the management of the Bank monitors performance of its subsidiaries on an individual basis. However, for the purpose of presentation of the operating segments, with the exception of PBZ Card, subsidiaries have been grouped into one segment. In that context, the following tables present overall financial information for the Bank and the Group by segment.

Items of the income statement in the presented tables on segment information for the Bank and the Group are generally in the format and of classification criteria suited for management reporting purposes. Therefore, disclosed segments have been reconciled to the financial statements prepared in accordance with the International Financial Reporting Standards. This reconciliation also includes consolidation adjustments in the Group segment report. Segment assets and segment liabilities for management reporting purpose are stated gross of provisions and other allowances unlike the disclosure criteria in the financial statements where assets and liabilities are presented net of provisions, deferred fees and other tax and non-tax allowances. In that context, reconciliation to the financial statements has reflected such offsetting.
In 2012 the Bank changed the methodology of allocation of segmental income and expense. The information for 2011 has also been changed to allow the comparison.

42 | Financial information by segment / continued

GROUP

As of and for the year ended 31 December 2012 (in HRK million)	Corporate banking	Retail banking	Finance banking	Central Structure	PBZ Card	Other subsidiaries	Reconciliation to financial statements	Financial statements
Net interest income	618	954	468	173	66	116	11	2,406
Net commission income/(expense)	234	248	24	-	538	59	(13)	1,090
Net profit/(loss) from trading and other operating income	(9)	125	25	7	(178)	101	210	281
Operating income	**843**	**1,327**	**517**	**180**	**426**	**276**	**208**	**3,777**
Operating expenses	(316)	(852)	(90)	57	(155)	(158)	(402)	(1,916)
Operating profit	**527**	**475**	**427**	**237**	**271**	**118**	**(194)**	**1,861**
Impairments	(398)	(184)	(26)	(30)	5	(13)	57	(589)
Profit before tax	**129**	**291**	**401**	**207**	**276**	**105**	**(137)**	**1,272**
Income tax expense	(36)	(27)	(79)	(40)	(56)	(20)	-	(258)
Profit after tax	**93**	**264**	**322**	**167**	**220**	**85**	**(137)**	**1,014**
Segment assets	25,727	26,553	19,058	2,136	2,211	5,818	(9,100)	72,403
Investments in associates	-	-	-	151	-	-	-	151
Total segment assets	**25,727**	**26,553**	**19,058**	**2,287**	**2,211**	**5,818**	**(9,100)**	**72,554**
Total segment liabilities	**20,481**	**39,267**	**2,373**	**614**	**1,424**	**5,100**	**(9,493)**	**59,766**
Capital expenditure	2	17	-	105	3	284	-	411

42| Financial information by segment / continued

Group

As of and for the year ended 31 December 2011 (in HRK million)	Corporate banking	Retail banking	Finance banking	Central Structure	PBZ Card	Other subsidiaries	Reconciliation to financial statements	Financial statements
Net interest income	757	808	498	205	66	139	7	2,480
Net commission income/(expense)	234	248	30	(2)	549	68	(15)	1,112
Net profit/(loss) from trading and other operating income	(3)	162	37	11	(166)	95	164	300
Operating income	**988**	**1,218**	**565**	**214**	**449**	**302**	**156**	**3,892**
Operating expenses	(322)	(835)	(96)	-	(157)	(168)	(364)	(1,942)
Operating profit	**666**	**383**	**469**	**214**	**292**	**134**	**(208)**	**1,950**
Impairments	(384)	96	(72)	4	(14)	(32)	33	(369)
Profit before tax	**282**	**479**	**397**	**218**	**278**	**102**	**(175)**	**1,581**
Income tax expense	(49)	(84)	(69)	(38)	(57)	(16)	-	(313)
Profit after tax	**233**	**395**	**328**	**180**	**221**	**86**	**(175)**	**1,268**
Segment assets	24,134	25,599	19,924	2,107	2,211	5,818	(5,774)	74,019
Investments in associates	-	-	-	135	-	-	-	135
Total segment assets	**24,134**	**25,599**	**19,924**	**2,242**	**2,211**	**5,818**	**(5,774)**	**74,154**
Total segment liabilities	**20,190**	**36,065**	**5,051**	**523**	**1,424**	**5,100**	**(6,521)**	**61,832**
Capital expenditure	1	15	-	72	4	211	-	303

42 | Financial information by segment / continued

Bank

As of and for the year 31 December 2012 (in HRK million)	Corporate banking	Retail banking	Finance banking	Central Structure	Reconciliation to financial statements	Financial statements
Net interest income	618	954	468	173	-	2,213
Net commission income	234	248	24	-	-	506
Net profit/(loss) from trading and other operating income	(9)	125	25	7	168	316
Operating income	**843**	**1,327**	**517**	**180**	**168**	**3,035**
Operating expenses	(316)	(852)	(90)	57	(203)	(1,404)
Operating profit	**527**	**475**	**427**	**237**	**(35)**	**1,631**
Impairments	(398)	(184)	(26)	(30)	35	(603)
Profit before tax	**129**	**291**	**401**	**207**	**-**	**1,028**
Income tax expense	(36)	(27)	(79)	(40)	-	(182)
Profit after tax	**93**	**264**	**322**	**167**	**-**	**846**
Total segment assets	**25,727**	**26,553**	**19,058**	**2,287**	**(5,214)**	**68,411**
Total segment liabilities	**20,481**	**39,267**	**2,373**	**614**	**(6,050)**	**56,685**
Capital expenditure	2	17	-	105	-	124

Bank

As of and for the year ended 31 December 2011 (in HRK million)	Corporate banking	Retail banking	Finance banking	Central Structure	Reconciliation to financial statements	Financial statements
Net interest income	757	808	498	205	-	2,268
Net commission income/(expense)	234	248	30	(2)	-	510
Net profit/(loss) from trading and other operating income	(3)	162	37	11	161	368
Operating income	**988**	**1,218**	**565**	**214**	**161**	**3,146**
Operating expenses	(322)	(835)	(96)	-	(164)	(1,417)
Operating profit	**666**	**383**	**469**	**214**	**(3)**	**1,729**
Impairments	(384)	96	(72)	4	3	(353)
Profit before tax	**282**	**479**	**397**	**218**	**-**	**1,376**
Income tax expense	(49)	(84)	(69)	(38)	-	(240)
Profit after tax	**233**	**395**	**328**	**180**	**-**	**1,136**
Total segment assets	**24,134**	**25,599**	**19,924**	**2,242**	**(4,418)**	**67,481**
Total segment liabilities	**20,190**	**36,065**	**5,051**	**523**	**(5,542)**	**56,287**
Capital expenditure	1	15	-	72	-	88

43 | Financial risk management policies

This section provides details of the Group's exposure to risks and describes the methods used by the management to identify, measure and manage risks. The most important types of financial risks to which the Group is exposed are credit risk, liquidity risk, market risk and operational risk. Market risk includes currency risk, interest rate risk and equity price risk.
An integrated system of risk management has been established at the Group level by introducing a set of policies and procedures, determining the limits of risk levels acceptable to the Group and monitoring its implementation. Additionally, the Group sets limits for annual potential loss measured by Value-at-Risk techniques for interest rate, exchange rate and equity price risk. The limits are set according to the amount of regulatory capital and apply to all types of risk. A methodology and models for managing operational risk have been developed.
Accepted management principles of risk management have been implemented in all subsidiaries.

a) Credit risk

The Group is subject to credit risk through its trading, lending and investing activities and in cases where it acts as an intermediary on behalf of customers or other third parties or issues guarantees. The risk that counterparties to both derivative and other instruments might default on their obligations is monitored on an ongoing basis. To manage the level of credit risk, the Group deals with counterparties of good credit standing, and when appropriate, obtain collateral.
The Group's primary exposure to credit risk arises through its loans and advances to customers. The amount of credit exposure in this regard is represented by the carrying amounts of the assets on the statement of financial position. In addition, the Group is exposed to off-balance sheet credit risk through commitments to extend credit and guarantees issued – as disclosed in Note 34.
Lending commitments including those based on guarantees issued by the Group that are contingent upon customers maintaining specific standards (including the solvency position of customers not worsening) represent liabilities that can be revoked. Irrevocable liabilities are based on undrawn but approved loans and approved overdrafts because these liabilities are the result of terms determined by loan contracts.
Guarantees and approved letters of credit that commit the Group to make payments on behalf of customers in the event of a specific act carry the same credit risk as loans. Standby letters of credit, which represent written guarantees of the Group in a clients' name such that a third party can withdraw funds up to the preapproved limit, are covered by collateral, being the goods for which they were issued. The credit risk for this type of product is significantly lower than for direct loans.
Exposure to credit risk has been managed in accordance with the Group's policies and with the regulatory requirements of the Croatian National Bank. Credit exposures to portfolios and individual group exposures are reviewed on a regular basis against the limits set. Breaches are reported to the appropriate bodies and personnel within the Bank authorised to approve them. Any substantial increases in credit exposure are authorised by the Credit Committee. The Assets Quality Committee monitors changes in the credit-worthiness of credit exposures and reviews them for any proposed impairment losses. Credit risk assessment is continuously monitored and reported, thus enabling an early identification of impairment in the credit portfolio. The Group continually applies prudent methods and models used in the process of credit risk assessment.
The Group is also continuous in developing internal models compliant with internal ratings-based approach ("IRB"), as prescribed by the CNB Decision on the capital adequacy of credit institutions requirements for calculation of capital adequacy, in order to quantify:

- default risk expressed in terms of internal rating which is periodically assigned to corporate and retail customers and quantified as probability of default (PD models);
- loss given default as an estimate of potential losses in the event of default, given the characteristics of transaction and present collateral (LGD models).

Internal models are deeply embedded into credit processes and underwriting policies where they determine characteristics of the transaction such as lending limit, required collateral and price as well as appropriate decision level within internal scheme of delegation of powers. Furthermore, internal models are also used for calculation of adequate level of internal capital (ICAAP) and within stress testing framework.

43 | Financial risk management policies / continued

a) Credit risk / continued

Maximum exposure to credit risk
The table below presents the maximum exposure to credit risk for the components of the statement of financial position. The maximum exposure is presented gross, before the effect of mitigation through collateral agreements.

	NOTES	GROUP		BANK	
(in HRK million)		2012	2011	2012	2011
Cash and current accounts with banks (excluding cash in hand)	14	2,776	1,323	2,773	1,224
Balances with the Croatian National bank	15	5,657	6,989	5,657	6,757
Debt securities at fair value through profit or loss	16	3,954	2,470	3,905	2,470
Derivative financial assets	17	4	11	4	11
Loans and advances to banks	18	6,250	7,036	6,236	7,231
Loans and advances to customers	19	49,960	51,398	46,918	46,691
Financial assets available for sale	20	91	985	81	189
Held-to-maturity investments	21	208	391	-	124
Other assets (excluding foreclosed assets and prepaid expenses)	27	410	437	198	167
Total		**69,310**	**71,040**	**65,772**	**64,864**
Contingent liabilities and commitments	34	11,322	12,684	11,385	12,381
Total credit risk exposure		**80,632**	**83,724**	**77,157**	**77,245**

Where financial instruments are recorded at fair value, the amounts shown above represent the credit risk exposure at the reporting date but not the maximum risk exposure that could arise in the future as a result of changes in fair values.
The maximum credit exposure to individual client or counterparty (excluding the Republic of Croatia and the Croatian National Bank) as of 31 December 2012 was HRK 1,435 million (2011: HRK 1,983 million) before taking account of collateral or other credit enhancements.

Collaterals held and other credit enhancements
In terms of credit risk mitigation the Group's policy is to require suitable collateral to be provided by certain customers prior to the disbursement of approved loans. As a rule, the Group approves a facility if there are two independent and viable repayment sources – cash flows generated by the borrower's activity and security instruments/collateral. The main types of collateral obtained are as follows:

- cash deposit for which the agreement stipulates that the Bank shall have the right to use the cash deposit for debt recovery and that the depositor may not use this deposit until the final settlement of all obligations under the approved facility;
- guarantee of the Government of the Republic of Croatia;
- pledge of securities issued by the Republic of Croatia or the Croatian National Bank;
- irrevocable guarantee or super guarantee issued by a domestic or foreign bank with adequate credit rating with the conditions of "payable on first demand" or "without objections" or similar;
- credit insurance policy issued by the Croatian Bank for Reconstruction and Development;
- credit insurance policy issued by an appropriate insurance company in accordance with the internal regulations of the Bank;
- pledge of units in investment funds managed by PBZ Invest;
- mortgage/lien/fiduciary transfer of ownership of property, movable property or securities of other issuers.

43 | Financial risk management policies / continued

a) Credit risk / continued

Collaterals held and other credit enhancements / continued

In general, a quality security instrument is an instrument with characteristics that provide a reasonable estimate of the Bank's ability to recover its receivables secured by that instrument (in case of its activation), through market or court mechanisms, within a reasonable period of time. Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained during its regular review of the adequacy of the allowance for impairment losses.

The majority of housing loans are secured by mortgages over residential property. A significant part of the corporate portfolio is secured by mortgages over different types of property. The Croatian real estate market, commercial and residential alike, has been illiquid since the end of 2007 and there are currently a limited number of transactions, despite significant decrease in prices in the second half of 2009 and more moderate decreases in subsequent years. The decrease in prices and illiquidity of the real estate market have an adverse effect on the recoverability of assets and the timing thereof in cases when the borrower experiences financial difficulty and the Bank relies on collateral to collect the asset.

Rescheduled and restructured receivables

Loan restructuring is done for clients where the focus of the business relationship shifted from making profit to mitigating losses on lending exposure at a stage when legal action for mitigating losses is not yet needed. The goal is timely identification of clients where restructuring would enable them to continue in business and to mitigate or prevent further losses for the Group.

Restructuring activities are based on cooperation with other organisational parts of the Group, which identify clients/exposures that are the subject of restructuring and include; supporting of sales staff in defining the appropriate restructuring strategy, analysing restructuring applications, suggesting measures and making recommendations for restructuring, monitoring progress, monitoring the portfolio, assessing the level of impairment and the Group's proposing measures that would improve collateral coverage in order to strengthen position in the collection of receivables.

Compared to the end of 2011, the restructured corporate portfolio has grown in volume by 24% in 2012, amounting to HRK 993 million (2011: HRK 798 million). The restructured portfolio provisions coverage as of 31 December 2012 was 35.6% (2011: 24%). The restructured individuals portfolio has grown in volume by 64% in 2012, amounting to HRK 842 million (2011: HRK 514 million), with the portfolio provisions coverage of 38.6%.

The Group is also continuously improving collection and workout processes (problem loan management framework) by introducing new application support boosting process efficiency and developing novel collection strategies in form of tailor made products and offers to retail customers, restructuring standards and support for corporate clients, and finally sale of assets where further collection is deemed immaterial and therefore not appropriate/efficient to be executed within the Group.

43 | Financial risk management policies / continued

a) Credit risk / continued

Loans and advances to customers: analysis by performance

(in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Loans and advances to customers				
Neither past due nor impaired	32,010	31,941	29,430	28,067
Past due but not impaired	15,924	17,773	15,339	16,777
Impaired	6,041	5,271	5,651	4,701
Gross	**53,975**	**54,985**	**50,420**	**49,545**
Specific impairment allowance	(3,113)	(2,677)	(2,652)	(2,024)
IBNR	(567)	(548)	(519)	(491)
Net of impairment allowance	**50,295**	**51,760**	**47,249**	**47,030**

Loans and advances to customers past due but not impaired

Past due but not impaired loans and advances to customers are those for which contractual interest or principal payments are past due, but the Group believes that impairment is not appropriate on the level of security, collateral available and/or the stage of collection of amounts owed to the Group.

An ageing analysis of loans and advances to customers past due but not impaired is shown below. The exposures below include due and not due portion of the loan. The table below provides an aggregated analysis of financial assets for the banking segment of the Bank, as the main segment of the consolidated statement of financial position.

43 | a) Credit risk / continued

Loans and advances to customers past due but not impaired / continued

(in HRK million)

Bank 2012	Up to 15 days	16 to 30 days	31 to 90 days	91 to 180 days	more than 180 days	Total
Loans and advances to corporate customers						
Government and municipalities	697	-	50	-	-	**747**
Corporate customers	7,037	30	772	7	1	**7,847**
SME	346	-	49	3	-	**398**
Others	351	-	13	1	-	**365**
Total	**8,431**	**30**	**884**	**11**	**1**	**9,357**

(in HRK million)

	Up to 15 days	16 to 30 days	31 to 90 days	91 to 180 days	more than 180 days	Total
Loans and advances to retail customers						
Car loans	82	6	43	1	-	**132**
Housing loans	2,234	147	741	47	10	**3,179**
Mortgage loans	192	15	97	9	1	**314**
Non-purpose loans	1,225	110	263	27	1	**1,626**
Overdrafts	24	2	17	2	-	**45**
Quick loans	358	5	58	5	-	**426**
Refinancing	135	14	61	16	2	**228**
Others	15	1	7	5	4	**32**
Total	**4,265**	**300**	**1,287**	**112**	**18**	**5,982**

43 | Financial risk management policies / continued

a) Credit risk / continued

Loans and advances to customers past due but not impaired / continued

(in HRK million)

Bank 2011	Up to 15 days	16 to 30 days	31 to 90 days	91 to 180 days	more than 180 days	Total
Loans and advances to corporate customers						
Government and municipalities	1,028	-	21	11	-	**1,060**
Corporate customers	8,479	43	457	13	-	**8,992**
SME	342	1	58	7	-	**408**
Others	350	-	35	4	-	**389**
Total	**10,199**	**44**	**571**	**35**	**-**	**10,849**

(in HRK million)

	Up to 15 days	16 to 30 days	31 to 90 days	91 to 180 days	more than 180 days	Total
Loans and advances to retail customers						
Car loans	166	9	71	3	-	**249**
Housing loans	2,309	129	633	39	3	**3,113**
Mortgage loans	215	13	102	8	1	**339**
Non-purpose loans	1,183	68	217	24	1	**1,493**
Overdrafts	9	1	8	2	1	**21**
Quick loans	482	2	69	8	1	**562**
Refinancing	84	9	30	9	1	**133**
Others	14	-	4	-	-	**18**
Total	**4,462**	**231**	**1,134**	**93**	**8**	**5,928**

The delinquencies up to 30 days are of a technical nature and are frequently of low value and represent an insignificant part of the aggregate outstanding amount of the borrower. The management believes that these exposures are fully recoverable. The exposure is presented gross, before the effect of mitigation through collateral agreements.

43 | Financial risk management policies / continued

a) Credit risk / continued

Loans and advances to customers that are neither past due nor impaired

For loans and advances to corporate customers that are neither past due nor impaired the Bank adopts special monitoring for clients with occasional defaults in repayment of loan. Special monitoring graded clients are analysed in detail for a short period of time after which the Group decides either to transfer the exposures to standard monitoring or to individually impaired category.

BANK (in HRK million)	2012	2011
Loans and advances to corporate customers		
Standard monitoring	9,784	10,895
Special monitoring	3,148	944
Loans and advances to retail customers		
Standard monitoring	16,498	16,228
Total	**29,430**	**28,067**

Loans and advances to customers that are past due and impaired

The Group determines that loans and advances to customers are impaired when there is objective evidence that a loss event has occurred since initial recognition and such loss event has an impact on future estimated cash flows from the asset. Impaired loans and advances to customers are set out below:

BANK / in HRK million	2012	2011
Loans and advances to corporate customers		
Government and municipalities	7	4
Corporate customers	3,213	2,639
SME	183	185
Others	68	106
Loans and advances to retail customers		
Car loans	79	92
Housing loans	713	549
Mortgage loans	183	179
Non-purpose loans	421	356
Overdrafts	148	131
Quick loans	147	137
Refinancing	463	299
Others	26	24
Total gross amount	**5,651**	**4,701**
Specific impairment allowance	(2,652)	(2,024)
Net amount	**2,999**	**2,677**

The fair value of collateral that the Group holds in respect of loans individually determined to be impaired as of 31 December 2012 amounts to HRK 7,343 million (31 December 2011: HRK 7,785 million).

43 | Financial risk management policies / continued

a) Credit risk / continued

Loans and advances to customers per CNB risk grades

Group (in HRK million)	2012		2011	
	Loans and advances to customers	Impairment allowance	Loans and advances to customers	Impairment allowance
A	47,795	567	49,455	548
B1	1,371	273	1,586	248
B2	2,932	1,199	2,056	785
B3	208	154	230	183
C	1,369	1,369	1,345	1,345
	53,675	**3,562**	**54,672**	**3,109**

Bank (in HRK million)	2012		2011	
	Loans and advances to customers	Impairment allowance	Loans and advances to customers	Impairment allowance
A	44,675	519	44,732	491
B1	1,343	262	1,506	226
B2	2,932	1,198	1,960	744
B3	186	147	201	160
C	998	998	856	856
	50,134	**3,124**	**49,255**	**2,477**

Impairment allowance for A graded loans relates to IBNR for loans and advances to customers.

Impairment allowance as a percentage of gross loans and advances to customers amounted to 6.6% (2011: 5.7%) for the Group and 6.2% (2011: 5.0%) for the Bank. The increase in the rate of impairment allowance in 2012 reflects the effect of the continued difficult economic environment.

The difference between net credit risk exposure for loans and advances to customers as shown in the tables above and as shown in the statement of financial position relates to accrued interest, which per the CNB Decision on the Structure and Content of Annual Financial Statements (Appendix 1) is shown within other assets and hence, is not included in the tables above, while in the statement of financial position it is included within loans and advances to customers. Accrued interest as at 31 December 2012 amounted to HRK 300 million (31 December 2011: HRK 313 million) for the Group and HRK 286 million (31 December 2011: HRK 290 million) for the Bank.

The difference between impairment allowance as shown in the tables above and as shown in this financial statements (Note 19 a) relates to impairment allowance on accrued interest. Impairment allowance on accrued interest as at 31 December 2012 amounted to HRK 118 million (31 December 2011: HRK 116 million) for the Group and HRK 47 million (31 December 2011: HRK 38 million) for the Bank.

43 | Financial risk management policies / continued

b) Liquidity risk

Liquidity risk arises in the general funding of the Group's activities and in the management of positions. It includes both the risk of being unable to fund assets at the appropriate maturities and rates and the risk of being unable to liquidate an asset at a reasonable price and in an appropriate time frame.

The Group has access to a diverse funding base. Funds are raised using a broad range of instruments including deposits, interest-bearing borrowings and share capital. This enhances funding flexibility, limits dependence on any one source of funds and generally lowers the cost of funding. The Group continually assesses liquidity risk by identifying and monitoring changes in funding required to meet business goals and targets set in terms of the overall Group strategy. In addition, the Group holds a portfolio of liquid assets as part of its liquidity risk management.

The Group adjusts its business activities to manage liquidity risk according to regulatory and internal policies for the maintenance of liquidity reserves, matching of liabilities and assets, control of limits, preferred liquidity ratios and contingency planning procedures. Needs for short-term liquidity are planned every month for a period of one month and controlled and maintained daily. The Treasury department manages liquidity reserves daily, ensuring also the fulfilment of all customer needs.

Apart from external requirements that include regulatory limits prescribed by the CNB (obligatory reserve with the CNB, minimum required amount of foreign currency claims, minimum liquidity coefficient and others), the Bank defined a set of internal limits for measuring and monitoring liquidity risk exposure. Thus, the process of liquidity monitoring and control is defined through the following activities and indicators:

- monitoring of liquidity reserve levels;
- short-term mismatches;
- stressed short-term mismatches;
- monitoring and control of Bank's structural liquidity ratios (medium and long-term “MLT” structural indicator) and analysis of the Bank's funding structure (core deposits modelling, MLT funding projection);
- money market debt exposure towards overall deposit base and other funding concentration ratios;
- cash flow projections;
- liquidity contingency plan indicators.

For the purpose of the Group's liquidity risk exposure reporting, the following three types of signals are defined:

- *Hard limit* - breach of a prescribed limit demands action in accordance with the Banks Liquidity risk management policy;
- *Threshold of attention* – breach of a threshold acts as an early warning signal, demanding additional attention and action if decided by responsible persons;
- *Information on various measures and indicators* - serving as information to the relevant decision-making bodies.

In accordance with the CNB Decision on the minimum foreign currency claims, the Bank is obliged to maintain a minimum of 17% (2011: 17%) of foreign currency liabilities in short-term assets. The actual figures were as follows:

2012	%	2011	%
"17% ratio" (at year end)	21.37	"17% ratio" (at year end)	19.55
Average	19.35	Average	18.61
Maximum	24.44	Maximum	21.92
Minimum	17.43	Minimum	17.44

Maturity analysis of financial liabilities according to the remaining contractual maturity as well as analysis of financial assets and financial liabilities according to their expected maturities are presented in Note 47 to these financial statements.
As part of management of liquidity risk arising from financial liabilities, the Group holds liquid assets comprising cash and cash equivalents and debt securities for which there is an active and liquid market so that they can be readily sold to meet liquidity requirements. In addition, the Group maintains agreed lines of credit with banks and holds unencumbered assets eligible for use as collateral.

43 | Financial risk management policies / continued

c) Market risk

All trading instruments are subject to market risk, which is the risk that changes in market prices, such as interest rates, equity securities prices, foreign exchange rates and credit spreads (not relating to changes in the obligator's/issuer's credit standing) will affect the Group's income or the value of its holdings of financial instruments. The Group manages and controls market risk exposures within acceptable parameters to ensure the Group's solvency while optimising the return on risk.
Market risk limits are defined based on the Group strategy and requirements, in accordance with senior management risk policy indicators.

Market risk measurement techniques
Exposure to market risk is formally managed by risk limits which are approved by senior management and revised at least annually. The Group applies the following market risk management techniques: VaR ("Value at Risk"), issuer limits, positional (nominal) exposure, PV01 (the present value of the impact of 1 bps movement in interest rate) and stop loss limits. The exposure figures and limit utilisations are delivered daily to the senior management and lower management levels within the Treasury Division, which enables informed decision-making at all management and operational levels.

The Group follows market risk measurement and management principles set in cooperation with the Intesa Sanpaolo Group. In 2004, the Group introduced VaR methodology as a basis for top management reporting on the Group's market risk exposure. In 2007, the Group began to use historical simulation (as the Group standard VaR methodology) and RiskWatch (as a Group wide VaR calculation engine), and other supporting activities (pricing, back-testing, stress testing) to ensure compliance with Intesa Sanpaolo Group standards.

The major elements of the market risk management framework include:
- VaR Methodology and Backtesting;
- Sensitivity;
- Fair Value Measurement;
- Level measurements (nominal amount, open position, market value etc.);
- Profit and loss indicators (P&L);
- Stress testing and scenario analysis;
- Monitoring and measurement of counterparty and delivery risk exposure.

VaR
The principal tool used to measure and control market risk exposure within the Group's trading portfolio is value-at-risk (VaR). VaR of a trading portfolio is the estimated loss that will arise on the portfolio over a specified period of time (holding period) given an adverse movement with a specified probability (confidence level). The model used by the Group is based upon a 99% confidence level and assumes a 1 day holding period. The use of a 99% confidence level means that losses exceeding the VaR figure should occur, on average, not more than once every one hundred days.

The Group uses VaR to measure the following market risks:
- general interest rate risk in the trading book;
- equity risk in trading book;
- foreign exchange risk on the statement of financial position level (both trading and banking book).

Since the majority of the trading book relates to the Bank, VaR is calculated at the Bank's level only.

43 | Financial risk management policies / continued

c) Market risk / continued

Bank

in HRK thousand	Equity VaR	Interest rate VaR	Foreign exchange VaR	Effects of correlation	Total
2012 – 2 January	586	4,230	1,916	(2,375)	**4,357**
2012 – 31 December	359	60	1,770	(721)	**1,468**
2012 – Average daily	573	2,146	2,181	(1,324)	**3,576**
2012 – Lowest	359	38	205	(152)	**450**
2012 – Highest	811	6,747	6,047	(6,605)	**7,000**

Note: historical simulation used for VaR calculations

in HRK thousand	Equity VaR	Interest rate VaR	Foreign exchange VaR	Effects of correlation	Total
2011 – 3 January	667	128	661	(655)	**801**
2011 – 30 December	582	4,343	2,448	(2,355)	**5,018**
2011 – Average daily	837	1,147	1,785	(1,266)	**2,503**
2011 – Lowest	397	42	116	58	**613**
2011 – Highest	1,408	5,465	4,541	(5,193)	**6,221**

Note: historical simulation used for VaR calculations

Although VaR is an important tool for measuring market risk, the assumptions on which the model is based gives rise to some limitations:

- a one day holding period assumes that it is possible to hedge or dispose of positions within that period. This may not be the case for illiquid assets or in situations in which there is severe market illiquidity;
- a 99% confidence level does not reflect losses that may occur beyond this level;
- the use of historical data as a basis for determining the possible range of future outcomes may not cover all possible scenarios, especially those of an exceptional nature;
- the VaR measure is dependent upon the Group's position and the volatility of market prices.

To determine the reliability of the VaR models, actual outcomes are monitored regularly to test the validity of the assumptions and the parameters used in the VaR calculation. As part of the validation process, the potential weaknesses of the models are analysed using statistical techniques, such as back-testing.

Currency risk
The Group is exposed to currency risk through transactions in foreign currencies. Foreign currency exposure arises from credit, deposit-taking, investment and trading activities. It is monitored daily in accordance with regulations and internally set limits, for each currency and for the total assets and liabilities denominated in or linked to foreign currency.
The currency risk exposure is monitored at the overall statement of financial position level by calculating the foreign exchange open position as prescribed by the regulatory provisions and daily through internal limits based on market risk models (foreign exchange VaR). The management of foreign exchange currency risk is supported by monitoring the sensitivity of the Group's financial assets and liabilities to fluctuation in foreign currencies.

43 | Financial risk management policies / continued

c) Market risk / continued

Currency risk / continued
The tables below indicate the currencies to which the Group and the Bank had significant exposure at 31 December 2012 and 31 December 2011. The analysis calculates the effect of a reasonably possible movement of the currencies against the kuna, with all other variables held constant on the income statement. A negative amount in the table reflects a potential net reduction in the income statement, while a positive amount reflects a net potential increase.

Group	Scenario 2012			Scenario 2011		
Currency	FX Open position 2012	10% Move Up	10% Move Down	FX Open position 2011	10% Move Up	10% Move Down
EUR	**507**	51	(51)	**475**	47	(47)
CHF	**(23)**	(2)	2	**(81)**	(8)	8
USD	**8**	1	(1)	**3**	-	-

Bank	Scenario 2012			Scenario 2011		
Currency	FX Open position 2012	10% Move Up	10% Move Down	FX Open position 2011	10% Move Up	10% Move Down
EUR	**270**	27	(27)	**531**	53	(53)
CHF	**(24)**	(2)	2	**(81)**	(8)	8
USD	**7**	1	(1)	**1**	-	-

Currency risk is further analysed in Note 46.

Interest rate risk
Interest rate risk represents the risk of decrease in asset values caused by adverse interest rate changes. Interest rate changes affect the net present value of future cash flows and consequently net interest income.

The sources of interest rate risk are:
- repricing risk - resulting from unfavourable changes in the fair value of assets and liabilities in the remaining period until the next interest rate change;
- yield curve risk - as the risk of changes in shape and slope of yield curve; and
- basis risk - as the risk of different base rates of corresponding asset and liabilities (e.g. EURIBOR vs LIBOR).

Asset-liability risk management activities are conducted to manage the Group's sensitivity to interest rate changes. Exposure to interest rate risk is monitored and measured using repricing gap analysis, net interest income and the economic value of capital. Risk management activities are aimed at optimising net interest income and the economic value of capital, in accordance with the Group's business strategies and given market interest rate levels.

The following table demonstrates the sensitivity to a reasonable possible change in interest rates of the Bank's income statement, with all other variables held constant. The sensitivity of the income statement is the effect of the assumed changes in interest rates on the net interest income for one year, based on the floating rate non-trading financial assets and financial liabilities held at 31 December 2012.

43 | Financial risk management policies / continued

c) Market risk / continued
Interest rate risk / continued

Group / in HRK million

Increase in basis points 2012	Change at 31 December 2012 interest income	interest expenses	net interest income	Change during the year ended 31 December 2012 net interest income *lowest*	net interest income *highest*	net interest income *average*
+25	99.2	76.1	23.1	10.5	23.1	16.3
+50	198.6	152.3	46.3	20.9	46.3	32.6

A decrease in basis points would have an opposite effect on the Group's net interest in the same amount. It is not practicable for the Group to present sensitivity analysis of net interest income for 2011.

Bank / in HRK million

Increase in basis points 2012	Change at 31 December 2012 interest income	interest expenses	net interest income	Change during the year ended 31 December 2012 net interest income *lowest*	net interest income *highest*	net interest income *average*
+25	96.2	73.1	23.1	9.7	23.1	15.8
+50	192.5	146.2	46.3	19.4	46.3	31.7

Increase in basis points 2011	Change at 31 December 2012 interest income	interest expenses	net interest income
+25	94.7	77.0	17.7
+50	189.3	153.9	35.4

A decrease in basis points would have an opposite effect on the Group's net interest in the same amount. It is not practicable for the Bank to present lowest, highest and average sensitivity of net interest income for 2011.
Interest rate risk management is further analysed in Note 44.

43 | Financial risk management policies / continued

c) Market risk / continued

Equity price risk
Equity price risk is the possibility that equity prices will fluctuate affecting the fair value of equity investments and other instruments that derive their value from a particular equity investment. The primary exposure to equity prices arises from equity securities held for trading and available for sale, which is not significant.

Derivative financial instruments
The Group enters into derivative financial instruments primarily to satisfy the needs and requirements of customers. Derivative financial instruments used by the Group include foreign exchange swaps and forwards. Derivatives are contracts which are individually negotiated over-the-counter.

d) Operational risk
Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. This definition includes legal risk but excludes strategic and reputation risk. In order to efficiently measure and manage operational risk exposure at the Group level, the Group applies an internal model for operational risk exposure management in line with the prescribed Basel II framework.

The internal model for calculation of the regulatory capital requirement for operational risk is based on Advanced Measurement Approach (AMA) and contains the following components: Loss Distribution Approach – LDA based on measure of historical losses or ex-post measured exposure (backward looking) and integrated self-diagnosis process (scenario analysis and business environment evaluation) based on subjective estimation of possible future operational losses (forward looking measure).

The AMA model has been used only for the calculation of the capital requirement for the Bank and the Bank applies the AMA approach since 31 March 2011. For all other Group members the Standardised Approach (TSA) has been used, which calculates capital requirement as a risk weighted indicator for all regulatory business lines.

44| Interest rate risk

The following tables present the Group's and the Bank's assets and liabilities analysed according to repricing periods determined as the earlier of the remaining contractual maturity and the contractual repricing. A significant amount of the Group's and the Bank's assets and liabilities are contracted with a discretionary right to reprice, although this right is infrequently used. All such instruments are included in the shortest time frame available (up to 1 month).

(in HRK million)

Group As at 31 December 2012	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	Over 1 year	Non-interest bearing	Total
Assets						
Cash and current accounts with banks	2,770	-	-	-	1,401	**4,171**
Balances with the Croatian National Bank	800	-	-	-	4,857	**5,657**
Financial assets at fair value through profit or loss	42	1,026	2,639	141	138	**3,986**
Derivative financial assets	-	-	-	-	4	**4**
Loans and advances to banks	4,386	610	340	776	138	**6,250**
Loans and advances to customers	19,816	13,258	8,789	6,037	2,060	**49,960**
Financial assets available for sale	-	-	30	-	61	**91**
Held-to-maturity investments	-	-	-	204	4	**208**
Investments in subsidiaries and associates	-	-	-	-	151	**151**
Intangible assets	-	-	-	-	162	**162**
Property and equipment	304	147	-	-	803	**1,254**
Investment property	-	-	-	-	9	**9**
Deferred tax assets	-	-	-	-	177	**177**
Other assets	3	-	-	-	471	**474**
Total assets	**28,121**	**15,041**	**11,798**	**7,158**	**10,436**	**72,554**
Liabilities						
Current accounts and deposits from banks	555	96	62	13	1	**727**
Current accounts and deposits from customers	22,809	1,997	20,706	2,178	453	**48,143**
Derivative financial liabilities	-	-	-	-	4	**4**
Interest-bearing borrowings	3,793	3,470	561	1,085	27	**8,936**
Other liabilities	-	-	-	-	1,518	**1,518**
Accrued expenses and deferred income	-	-	-	-	201	**201**
Provisions for liabilities and charges	-	-	-	-	204	**204**
Current tax liability	-	-	-	-	33	**33**
Total liabilities	**27,157**	**5,563**	**21,329**	**3,276**	**2,441**	**59,766**
Interest sensitivity gap	**964**	**9,478**	**(9,531)**	**3,882**	**7,995**	**12,788**

44 | Interest rate risk / continued (in HRK million)

Group **As at 31 December 2011**	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	Over 1 year	Non-interest bearing	Total
Assets						
Cash and current accounts with banks	1,135	-	-	-	1,512	**2,647**
Balances with the Croatian National Bank	1,810	-	-	-	5,179	**6,989**
Financial assets at fair value through profit or loss	-	1,242	824	352	79	**2,497**
Derivative financial assets	-	-	-	-	11	**11**
Loans and advances to banks	6,031	54	295	638	18	**7,036**
Loans and advances to customers	20,546	14,297	6,997	7,689	1,869	**51,398**
Financial assets available for sale	4	128	430	246	177	**985**
Held-to-maturity investments	-	120	60	203	8	**391**
Investments in subsidiaries and associates	-	-	-	-	135	**135**
Intangible assets	-	-	-	-	157	**157**
Property and equipment	109	163	-	-	932	**1,204**
Investment property	-	-	-	-	12	**12**
Non-current assets held for sale	-	-	-	-	30	**30**
Deferred tax assets	-	-	-	-	171	**171**
Other assets	23	5	21	-	442	**491**
Total assets	**29,658**	**16,009**	**8,627**	**9,128**	**10,732**	**74,154**
Liabilities						
Current accounts and deposits from banks	2,873	69	-	52	-	**2,994**
Current accounts and deposits from customers	24,202	1,955	18,793	2,055	426	**47,431**
Derivative financial liabilities	-	-	-	-	9	**9**
Interest-bearing borrowings	1,179	1,448	489	6,157	38	**9,311**
Other liabilities	1	-	-	-	1,632	**1,633**
Accrued expenses and deferred income	-	-	-	-	194	**194**
Provisions for liabilities and charges	-	-	-	-	191	**191**
Current tax liability	-	-	-	-	69	**69**
Total liabilities	**28,255**	**3,472**	**19,282**	**8,264**	**2,559**	**61,832**
Interest sensitivity gap	**1,403**	**12,537**	**(10,655)**	**864**	**8,173**	**12,322**

44| Interest rate risk / continued (in HRK million)

Bank As at 31 December 2012	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	Over 1 year	Non-interest bearing	Total
Assets						
Cash and current accounts with banks	2,770	-	-	-	1,398	**4,168**
Balances with the Croatian National Bank	800	-	-	-	4,857	**5,657**
Financial assets at fair value through profit or loss	42	1,026	2,591	141	127	**3,927**
Derivative financial assets	-	-	-	-	4	**4**
Loans and advances to banks	4,531	584	311	806	4	**6,236**
Loans and advances to customers	20,118	12,465	8,789	5,260	286	**46,918**
Financial assets available for sale	-	-	20	-	61	**81**
Investments in subsidiaries and associates	-	-	-	-	220	**220**
Intangible assets	-	-	-	-	103	**103**
Property and equipment	-	-	-	-	700	**700**
Investment property	-	-	-	-	9	**9**
Deferred tax assets	-	-	-	-	132	**132**
Other assets	-	-	-	-	256	**256**
Total assets	**28,261**	**14,075**	**11,711**	**6,207**	**8,157**	**68,411**
Liabilities						
Current accounts and deposits from banks	601	96	62	346	3	**1,108**
Current accounts and deposits from customers	22,707	1,957	20,381	1,475	453	**46,973**
Derivative financial liabilities	-	-	-	-	4	**4**
Interest-bearing borrowings	3,600	2,564	633	1,098	23	**7,918**
Other liabilities	-	-	-	-	394	**394**
Accrued expenses and deferred income	-	-	-	-	81	**81**
Provisions for liabilities and charges	-	-	-	-	204	**204**
Current tax liability	-	-	-	-	3	**3**
Total liabilities	**26,908**	**4,617**	**21,076**	**2,919**	**1,165**	**56,685**
Interest sensitivity gap	**1,353**	**9,458**	**(9,365)**	**3,288**	**6,992**	**11,726**

44 | Interest rate risk / continued (in HRK million)

Bank **As at 31 December 2011**	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	Over 1 year	Non-interest bearing	Total
Assets						
Cash and current accounts with banks	1,120	-	-	-	1,345	**2,465**
Balances with the Croatian National Bank	1,800	-	-	-	4,957	**6,757**
Financial assets at fair value through profit or loss	-	1,242	824	352	79	**2,497**
Derivative financial assets	-	-	-	-	11	**11**
Loans and advances to banks	6,259	34	295	626	17	**7,231**
Loans and advances to customers	19,265	13,549	6,769	6,818	290	**46,691**
Financial assets available for sale	-	-	-	98	91	**189**
Held-to-maturity investments	-	120	-	-	4	**124**
Investments in subsidiaries and associates	-	-	-	-	389	**389**
Intangible assets	-	-	-	-	83	**83**
Property and equipment	-	-	-	-	683	**683**
Investment property	-	-	-	-	9	**9**
Non-current assets held for sale	-	-	-	-	30	**30**
Deferred tax assets	-	-	-	-	118	**118**
Other assets	-	-	-	-	204	**204**
Total assets	**28,444**	**14,945**	**7,888**	**7,894**	**8,310**	**67,481**
Liabilities						
Current accounts and deposits from banks	2,995	368	-	52	8	**3,423**
Current accounts and deposits from customers	21,898	2,075	18,369	1,315	424	**44,081**
Derivative financial liabilities	-	-	-	-	9	**9**
Interest-bearing borrowings	1,152	205	471	6,129	33	**7,990**
Other liabilities	-	-	-	-	461	**461**
Accrued expenses and deferred income	-	-	-	-	74	**74**
Provisions for liabilities and charges	-	-	-	-	186	**186**
Current tax liability	-	-	-	-	63	**63**
Total liabilities	**26,045**	**2,648**	**18,840**	**7,496**	**1,258**	**56,287**
Interest sensitivity gap	**2,399**	**12,297**	**(10,952)**	**398**	**7,052**	**11,194**

45| Weighted average interest rates

The average effective interest rates for interest-earning financial assets and interest-bearing financial liabilities during the year are calculated on average balances at the end of each month for the Group and average monthly balances for the Bank.
The weighted average interest rates at the year-end are as follows:

	GROUP		BANK	
	2012	2011	2012	2011
	%	%	%	%
Current accounts with banks	0.05	0.02	0.05	0.02
Balances with the Croatian National Bank	-	0.05	-	0.05
Financial assets at fair value through profit or loss	4.64	3.53	4.64	3.50
Loans and advances to banks	0.56	0.81	0.60	0.86
Loans and advances to customers	6.47	6.64	6.69	6.84
Public debt due from the Republic of Croatia	-	5.00	-	5.00
Current accounts and deposits from customers	2.58	2.58	2.58	2.57
Current accounts and deposits from banks and interest-bearing borrowings	2.20	2.08	2.17	2.02

46 | Currency risk (in HRK million)

The Group manages its exposure to currency risk through a variety of measures including the use of revaluation clauses, which have the same effect as denominating HRK assets in other currencies, and foreign currency deals bought and sold forward.
The Group's open FX position is mitigated through the use of derivative financial instruments which are not shown in the tables below.

Group **As at 31 December 2012**	EUR and EUR linked	CHF and CHF linked	USD and USD linked	Other currencies	HRK	Total
Assets						
Cash and current accounts with banks	384	966	80	115	2,626	**4,171**
Balances with the Croatian National Bank	871	-	-	-	4,786	**5,657**
Financial assets at fair value through profit or loss	1,499	-	-	-	2,487	**3,986**
Derivative financial assets	-	-	-	-	4	**4**
Loans and advances to banks	2,187	-	2,292	513	1,258	**6,250**
Loans and advances to customers	29,868	3,840	393	-	15,859	**49,960**
Financial assets available for sale	-	-	-	-	91	**91**
Held-to-maturity investments	208	-	-	-	-	**208**
Investments in subsidiaries and associates	-	-	-	-	151	**151**
Intangible assets	-	-	-	-	162	**162**
Property and equipment	293	-	-	-	961	**1,254**
Investment property	-	-	-	-	9	**9**
Deferred tax assets	-	-	-	-	177	**177**
Other assets	15	2	-	-	457	**474**
Total assets	**35,325**	**4,808**	**2,765**	**628**	**29,028**	**72,554**
Liabilities						
Current accounts and deposits from banks	326	56	49	34	262	**727**
Current accounts and deposits from customers	30,799	727	2,718	552	13,347	**48,143**
Derivative financial liabilities	-	-	-	-	4	**4**
Interest-bearing borrowings	3,463	4,043	3	-	1,427	**8,936**
Other liabilities	63	5	37	1	1,412	**1,518**
Accrued expenses and deferred income	6	-	-	-	195	**201**
Provisions for liabilities and charges	8	-	12	1	183	**204**
Current tax liability	-	-	-	-	33	**33**
Total liabilities	**34,665**	**4,831**	**2,819**	**588**	**16,863**	**59,766**
Net position	**660**	**(23)**	**(54)**	**40**	**12,165**	**12,788**

46 | Currency risk / continued (in HRK million)

Group As at 31 December 2011	EUR and EUR linked	CHF and CHF linked	USD and USD linked	Other currencies	HRK	Total
Assets						
Cash and current accounts with banks	370	136	56	67	2,018	**2,647**
Balances with the Croatian National Bank	958	-	-	-	6,031	**6,989**
Financial assets at fair value through profit or loss	640	-	-	-	1,857	**2,497**
Derivative financial assets	-	-	-	-	11	**11**
Loans and advances to banks	3,810	26	2,117	461	622	**7,036**
Loans and advances to customers	31,817	4,309	270	-	15,002	**51,398**
Financial assets available for sale	367	-	12	-	606	**985**
Held-to-maturity investments	391	-	-	-	-	**391**
Investments in subsidiaries and associates	-	-	-	-	135	**135**
Intangible assets	-	-	-	-	157	**157**
Property and equipment	269	-	-	-	935	**1,204**
Investment property	-	-	-	-	12	**12**
Non-current assets held for sale	-	-	-	-	30	**30**
Deferred tax assets	-	-	-	-	171	**171**
Other assets	38	2	2	1	448	**491**
Total assets	**38,660**	**4,473**	**2,457**	**529**	**28,035**	**74,154**
Liabilities						
Current accounts and deposits from banks	580	44	26	25	2,319	**2,994**
Current accounts and deposits from customers	30,094	646	2,941	494	13,256	**47,431**
Derivative financial liabilities	-	-	-	-	9	**9**
Interest-bearing borrowings	3,944	4,010	3	-	1,354	**9,311**
Other liabilities	796	5	35	2	795	**1,633**
Accrued expenses and deferred income	4	-	-	-	190	**194**
Provisions for liabilities and charges	13	-	12	1	165	**191**
Current tax liability	-	-	-	-	69	**69**
Total liabilities	**35,431**	**4,705**	**3,017**	**522**	**18,157**	**61,832**
Net position	**3,229**	**(232)**	**(560)**	**7**	**9,878**	**12,322**

46 | Currency risk / continued

Bank (in HRK million) **As at 31 December 2012**	EUR and EUR linked	CHF and CHF linked	USD and USD linked	Other currencies	HRK	Total
Assets						
Cash and current accounts with banks	384	966	80	115	2,623	**4,168**
Balances with the Croatian National Bank	871	-	-	-	4,786	**5,657**
Financial assets at fair value through profit or loss	1,499	-	-	-	2,428	**3,927**
Derivative financial assets	-	-	-	-	4	**4**
Loans and advances to banks	2,187	-	2,292	513	1,244	**6,236**
Loans and advances to customers	28,403	3,840	393	-	14,282	**46,918**
Financial assets available for sale	-	-	-	-	81	**81**
Investments in subsidiaries and associates	-	-	-	-	220	**220**
Intangible assets	-	-	-	-	103	**103**
Property and equipment	-	-	-	-	700	**700**
Investment property	-	-	-	-	9	**9**
Deferred tax assets	-	-	-	-	132	**132**
Other assets	12	1	-	-	243	**256**
Total assets	**33,356**	**4,807**	**2,765**	**628**	**26,855**	**68,411**
Current accounts and deposits from banks	413	56	65	35	539	**1,108**
Current accounts and deposits from customers	29,695	727	2,702	551	13,298	**46,973**
Derivative financial liabilities	-	-	-	-	4	**4**
Interest-bearing borrowings	2,444	4,043	3	-	1,428	**7,918**
Other liabilities	45	5	22	1	321	**394**
Accrued expenses and deferred income	6	-	-	-	75	**81**
Provisions for liabilities and charges	8	-	12	1	183	**204**
Current tax liability	-	-	-	-	3	**3**
Total liabilities	**32,611**	**4,831**	**2,804**	**588**	**15,851**	**56,685**
Net position	**745**	**(24)**	**(39)**	**40**	**11,004**	**11,726**

46 | Currency risk / continued

Bank (in HRK million) **As at 31 December 2011**	EUR and EUR linked	CHF and CHF linked	USD and USD linked	Other currencies	HRK	Total
Assets						
Cash and current accounts with banks	332	128	52	61	1,892	**2,465**
Balances with the Croatian National Bank	925	-	-	-	5,832	**6,757**
Financial assets at fair value through profit or loss	640	-	-	-	1,857	**2,497**
Derivative financial assets	-	-	-	-	11	**11**
Loans and advances to banks	3,887	-	2,109	458	777	**7,231**
Loans and advances to customers	28,839	4,280	270	-	13,302	**46,691**
Financial assets available for sale	78	-	12	-	99	**189**
Held-to-maturity investments	124	-	-	-	-	**124**
Investments in subsidiaries and associates	-	-	-	-	389	**389**
Intangible assets	-	-	-	-	83	**83**
Property and equipment	-	-	-	-	683	**683**
Investment property	-	-	-	-	9	**9**
Non-current assets held for sale	-	-	-	-	30	**30**
Deferred tax assets	-	-	-	-	118	**118**
Other assets	35	2	1	1	165	**204**
Total assets	**34,860**	**4,410**	**2,444**	**520**	**25,247**	**67,481**
Liabilities						
Current accounts and deposits from banks	976	44	26	25	2,352	**3,423**
Current accounts and deposits from customers	27,547	584	2,929	486	12,535	**44,081**
Derivative financial liabilities	-	-	-	-	9	**9**
Interest-bearing borrowings	2,669	4,010	3	-	1,308	**7,990**
Other liabilities	54	5	25	2	375	**461**
Accrued expenses and deferred income	3	-	-	-	71	**74**
Provisions for liabilities and charges	13	-	12	1	160	**186**
Current tax liability	-	-	-	-	63	**63**
Total liabilities	**31,262**	**4,643**	**2,995**	**514**	**16,873**	**56,287**
Net position	**3,598**	**(233)**	**(551)**	**6**	**8,374**	**11,194**

47 | Liquidity risk (in HRK million)

Analysis of financial liabilities by remaining contractual maturities

The tables below set out the remaining contractual maturity of the Group's and Bank's financial liabilities as at 31 December 2012 and 31 December 2011.

Group As at 31 December 2012	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	Total
Liabilities						
Current accounts and deposits from banks	527	95	65	59	9	**755**
Current accounts and deposits from customers	20,420	7,239	16,805	4,474	127	**49,065**
Derivative financial liabilities	1	1	2	-	-	**4**
Interest-bearing borrowings	532	276	931	7,154	569	**9,462**
Other liabilities*	634	1,123	36	12	151	**1,956**
Total undiscounted financial liabilities	**22,114**	**8,734**	**17,839**	**11,699**	**856**	**61,242**
Off-balance sheet contingent liabilities and commitments						
Undrawn lending commitments	1,573	427	3,096	1,224	2,097	**8,417**
Other contingent liabilities	681	678	1,186	312	48	**2,905**
Total undiscounted off-balance sheet contingent liabilities and commitments	**2,254**	**1,105**	**4,282**	**1,536**	**2,145**	**11,322**

As at 31 December 2011	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	Total
Liabilities						
Current accounts and deposits from banks	2,571	376	-	46	10	**3,003**
Current accounts and deposits from customers	20,467	7,115	16,162	4,266	107	**48,117**
Derivative financial liabilities	4	1	4	-	-	**9**
Interest-bearing borrowings	517	232	1,433	5,160	2,755	**10,097**
Other liabilities*	745	1,151	25	32	134	**2,087**
Total undiscounted financial liabilities	**24,304**	**8,875**	**17,624**	**9,504**	**3,006**	**63,313**
Off-balance sheet contingent liabilities and commitments						
Undrawn lending commitments	4,287	617	1,718	161	2,885	**9,668**
Other contingent liabilities	926	596	1,011	429	54	**3,016**
Total undiscounted off-balance sheet contingent liabilities and commitments	**5,213**	**1,213**	**2,729**	**590**	**2,939**	**12,684**

* Other liabilities include other liabilities, accrued expenses and deferred income, provisions for liabilities and charges and current tax liability.

47 | Liquidity risk / continued (in HRK million)

Analysis of financial liabilities by remaining contractual maturities / continued

Bank As at 31 December 2012	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	Total
Liabilities						
Current accounts and deposits from banks	604	95	65	364	9	**1,137**
Current accounts and deposits from customers	20,344	7,198	16,470	3,680	128	**47,820**
Derivative financial liabilities	1	1	2	-	-	**4**
Interest-bearing borrowings	839	271	601	6,101	569	**8,381**
Other liabilities*	509	5	12	5	151	**682**
Total undiscounted financial liabilities	**22,297**	**7,570**	**17,150**	**10,150**	**857**	**58,024**
Off-balance sheet contingent liabilities and commitments						
Undrawn lending commitments	1,636	427	3,096	1,224	2,097	**8,480**
Other contingent liabilities	218	305	1,403	800	179	**2,905**
Total undiscounted off-balance sheet contingent liabilities and commitments	**1,854**	**732**	**4,499**	**2,024**	**2,276**	**11,385**

Bank As at 31 December 2011	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	Total
Liabilities						
Current accounts and deposits from banks	3,001	376	-	46	10	**3,433**
Current accounts and deposits from customers	19,508	6,764	15,154	3,198	89	**44,713**
Derivative financial liabilities	4	1	4	-	-	**9**
Interest-bearing borrowings	1,171	221	573	3,976	2,738	**8,679**
Other liabilities*	629	3	14	4	134	**784**
Total undiscounted financial liabilities	**24,313**	**7,365**	**15,745**	**7,224**	**2,971**	**57,618**
Off-balance sheet contingent liabilities and commitments						
Undrawn lending commitments	4,041	617	1,718	161	2,885	**9,422**
Other contingent liabilities	870	596	1,010	429	54	**2,959**
Total undiscounted off-balance sheet contingent liabilities and commitments	**4,911**	**1,213**	**2,728**	**590**	**2,939**	**12,381**

* Other liabilities include other liabilities, accrued expenses and deferred income, provisions for liabilities and charges and current tax liability.

47 | Liquidity risk / continued

Maturity analysis of assets and liabilities

The tables below present analyses of assets and liabilities of the Group and Bank according to their expected maturities at 31 December 2012 and 31 December 2011. The Group's expected cash flows on some financial assets and liabilities vary significantly from the contractual cash flows. For example, demand deposits from customers are expected to maintain a stable balance and are not all expected to be drawn immediately.

The Group and the Bank made certain assumptions in producing maturity analyses set out below. The assumptions, applied for loans and advances to customers were mostly based on contractual maturities, whilst overdraft, revolving and other facilities without precise amortisation plans were assumed to be recoverable within 12 months. Moreover, expected maturities for current accounts and deposits from customers and to some extent non-performing loans were based on statistical behaviour model of past experience. All other items of the Group and the Bank were mostly based on contractual maturities.

Group (in HRK million) **As at 31 December 2012**	Less than 12 months	Over 12 months	Total
Assets			
Cash and current accounts with banks	4,171	-	**4,171**
Balances with the Croatian National Bank	800	4,857	**5,657**
Financial assets at fair value through profit or loss	3,835	151	**3,986**
Derivative financial assets	4	-	**4**
Loans and advances to banks	5,443	807	**6,250**
Loans and advances to customers	18,655	31,305	**49,960**
Financial assets available for sale	71	20	**91**
Held-to-maturity investments	4	204	**208**
Investments in subsidiaries and associates	-	151	**151**
Intangible assets	-	162	**162**
Property and equipment	202	1,052	**1,254**
Investment property	-	9	**9**
Deferred tax assets	-	177	**177**
Other assets	428	46	**474**
Total assets	**33,613**	**38,941**	**72,554**
Liabilities			
Current accounts and deposits from banks	687	40	**727**
Current accounts and deposits from customers	9,038	39,105	**48,143**
Derivative financial liabilities	4	-	**4**
Interest-bearing borrowings	1,569	7,367	**8,936**
Other liabilities	1,518	-	**1,518**
Accrued expenses and deferred income	188	13	**201**
Provisions for liabilities and charges	54	150	**204**
Current tax liability	33	-	**33**
Total liabilities	**13,091**	**46,675**	**59,766**
Net expected maturity gap	**20,522**	**(7,734)**	**12,788**

47| Liquidity risk / continued (in HRK million)

Maturity analysis of assets and liabilities / continued

Group As at 31 December 2011	Less than 12 months	Over 12 months	Total
Assets			
Cash and current accounts with banks	2,647	-	**2,647**
Balances with the Croatian National Bank	1,851	5,138	**6,989**
Financial assets at fair value through profit or loss	2,145	352	**2,497**
Derivative financial assets	11	-	**11**
Loans and advances to banks	6,281	755	**7,036**
Loans and advances to customers	16,608	34,790	**51,398**
Financial assets available for sale	744	241	**985**
Held-to-maturity investments	186	205	**391**
Investments in subsidiaries and associates	-	135	**135**
Intangible assets	-	157	**157**
Property and equipment	81	1,123	**1,204**
Investment property	-	12	**12**
Non-current assets held for sale	-	30	**30**
Deferred tax assets	-	171	**171**
Other assets	459	32	**491**
Total assets	**31,013**	**43,141**	**74,154**
Liabilities			
Current accounts and deposits from banks	2,942	52	**2,994**
Current accounts and deposits from customers	11,954	35,477	**47,431**
Derivative financial liabilities	9	-	**9**
Interest-bearing borrowings	2,013	7,298	**9,311**
Other liabilities	1,633	-	**1,633**
Accrued expenses and deferred income	181	13	**194**
Provisions for liabilities and charges	38	153	**191**
Current tax liability	69	-	**69**
Total liabilities	**18,839**	**42,993**	**61,832**
Net expected maturity gap	**12,174**	**148**	**12,322**

47 | Liquidity risk / continued (in HRK million)

Maturity analysis of assets and liabilities / continued

Bank As at 31 December 2012	Less than 12 months	Over 12 months	Total
Assets			
Cash and current accounts with banks	4,168	-	**4,168**
Balances with the Croatian National Bank	800	4,857	**5,657**
Financial assets at fair value through profit or loss	3,776	151	**3,927**
Derivative financial assets	4	-	**4**
Loans and advances to banks	5,399	837	**6,236**
Loans and advances to customers	17,069	29,849	**46,918**
Financial assets available for sale	61	20	**81**
Investments in subsidiaries and associates	-	220	**220**
Intangible assets	-	103	**103**
Property and equipment	-	700	**700**
Investment property	-	9	**9**
Deferred tax assets	-	132	**132**
Other assets	211	45	**256**
Total assets	**31,488**	**36,923**	**68,411**
Liabilities			
Current accounts and deposits from banks	763	345	**1,108**
Current accounts and deposits from customers	7,868	39,105	**46,973**
Derivative financial liabilities	4	-	**4**
Interest-bearing borrowings	1,565	6,353	**7,918**
Other liabilities	394	-	**394**
Accrued expenses and deferred income	68	13	**81**
Provisions for liabilities and charges	61	143	**204**
Current tax liability	3	-	**3**
Total liabilities	**10,726**	**45,959**	**56,685**
Net expected maturity gap	**20,762**	**(9,036)**	**11,726**

47 | Liquidity risk / continued (in HRK million)

Maturity analysis of assets and liabilities / continued

Bank **As at 31 December 2011**	Less than 12 months	Over 12 months	Total
Assets			
Cash and current accounts with banks	2,465	-	**2,465**
Balances with the Croatian National Bank	1,800	4,957	**6,757**
Financial assets at fair value through profit or loss	2,145	352	**2,497**
Derivative financial assets	11	-	**11**
Loans and advances to banks	6,490	741	**7,231**
Loans and advances to customers	14,133	32,558	**46,691**
Financial assets available for sale	91	98	**189**
Held-to-maturity investments	124	-	**124**
Investments in subsidiaries and associates	-	389	**389**
Intangible assets	-	83	**83**
Property and equipment	-	683	**683**
Investment property	-	9	**9**
Non-current assets held for sale	-	30	**30**
Deferred tax assets	-	118	**118**
Other assets	172	32	**204**
Total assets	**27,431**	**40,050**	**67,481**
Liabilities			
Current accounts and deposits from banks	3,371	52	**3,423**
Current accounts and deposits from customers	11,317	32,764	**44,081**
Derivative financial liabilities	9	-	**9**
Interest-bearing borrowings	1,832	6,158	**7,990**
Other liabilities	461	-	**461**
Accrued expenses and deferred income	61	13	**74**
Provisions for liabilities and charges	61	125	**186**
Current tax liability	63	-	**63**
Total liabilities	**17,175**	**39,112**	**56,287**
Net expected maturity gap	**10,256**	**938**	**11,194**

48 | Concentration of assets and liabilities

Concentration of risk is managed by client/counterparty, by geographical region and by industry sector. The Bank's and the Group's assets and liabilities can be analysed by the following geographical regions and industry sector:

	GROUP			BANK		
(in HRK million)	Assets	Liabilities	Off balance sheet liabilities	Assets	Liabilities	Off balance sheet liabilities
As at 31 December 2012						
Geographic region						
Republic of Croatia	65,591	39,473	10,763	61,448	37,425	10,826
European Union	2,939	7,311	411	2,938	6,279	411
Other countries	4,024	12,982	148	4,025	12,981	148
	72,554	**59,766**	**11,322**	**68,411**	**56,685**	**11,385**
Industry sector						
Citizens	27,664	38,164	5,039	25,341	36,969	5,104
Finance	14,413	9,687	98	11,893	9,023	97
Government	9,924	1,968	83	8,867	1,932	83
Commerce	3,576	995	737	3,335	990	737
Tourism	916	244	30	862	242	30
Agriculture	681	152	95	658	152	95
Other sectors	15,380	8,556	5,240	17,455	7,377	5,239
	72,554	**59,766**	**11,322**	**68,411**	**56,685**	**11,385**
(in HRK million)						
As at 31 December 2011						
Geographic region						
Republic of Croatia	69,737	49,386	12,071	63,319	43,892	11,769
European Union	3,926	10,004	481	3,694	9,958	481
Other countries	491	2,442	132	468	2,437	131
	74,154	**61,832**	**12,684**	**67,481**	**56,287**	**12,381**
Industry sector						
Citizens	27,703	36,813	5,718	24,574	33,674	5,568
Finance	14,025	12,303	159	13,988	11,410	155
Government	11,047	2,706	664	8,925	2,693	634
Commerce	3,024	1,112	709	2,601	1,032	683
Tourism	865	201	78	822	188	78
Agriculture	1,348	211	79	1,303	206	79
Other sectors	16,142	8,486	5,277	15,268	7,084	5,184
	74,154	**61,832**	**12,684**	**67,481**	**56,287**	**12,381**

49| Earnings per share

For the purpose of calculating earnings per share, earnings represent the net profit after tax. The number of ordinary shares is the weighted average number of ordinary shares outstanding during the year after deducting the number of ordinary treasury shares. The weighted average number of ordinary shares used for basic earnings per share was 19,010,096 (2011: 19,010,096). There is no potential dilution effect from any instruments and hence the basic earnings per share are the same as diluted earnings per share.

GROUP	2012	2011
Profit attributable to equity holders of the Bank (in HRK million)	1,014	1,268
Weighted average number of ordinary shares	19,010,096	19,010,096
Basic and diluted earnings per share (in HRK per share)	53.3	66.7

50| Subsequent events

a) New Law on Financial Transactions and Pre-bankruptcy Settlement
As described in Note 4 Accounting estimates and judgments in applying accounting policies, new legislation on pre-bankruptcy settlement process was introduced with effect from 1 October 2012. Consequently, the main impact of the new legislation on the Bank arising from applications from its borrowing customers for pre-bankruptcy settlement under the new Law started and continues to be felt in 2013. Up to the end of February 2013, 88 applications have been filed with the Agency, which were debtors of the Bank at 31 December 2012, with total balance and off-balance sheet exposure of HRK 270 million as at 31 December 2012, net of impairment allowance. The impairment allowance account for 40% of the gross total value of those exposures.

b) Proposed dividends
At its meeting held on 14 February 2013, the Management Board of the Bank proposed a dividend of HRK 44.40 per share. The total amount to be distributed to the shareholders amounts to HRK 844 million. The Supervisory Board gave its consent to the proposed distribution, which should be approved on the following General Assembly meeting.

Appendix 1 - Supplementary forms required by local regulation

Supplementary financial statements of the Group and the Bank prepared in accordance with the framework for reporting set out in the Decision of the Croatian National Bank on the Structure and Content of Annual Financial Statements (Official Gazette 62/08) are presented below:

Form "Balance sheet" (in HRK million)		**GROUP**		**BANK**
	31 December 2012	31 December 2011	31 December 2012	31 December 2011
Assets				
Cash and deposits with the Croatian National Bank	8,767	9,520	8,764	9,121
Cash	*1,401*	*1,327*	*1,398*	*1,244*
Deposits with the Croatian National Bank	*7,366*	*8,193*	*7,366*	*7,877*
Deposits with banking institutions	6,193	6,271	6,167	5,984
Ministry of Finance treasury bills and the Croatian National Bank bills	3,482	2,675	3,424	2,038
Securities and other financial instruments held for trading	18	27	18	27
Securities and other financial instruments available for sale	91	344	81	186
Securities and other financial instruments held to maturity	204	384	-	120
Securities and other financial instruments at fair value in profit or loss and not traded	380	380	380	380
Derivative financial assets	4	11	4	11
Loans to financial institutions	1,112	877	1,125	1,330
Loans to other clients	49,780	51,200	46,680	46,440
Investments in subsidiaries, associates and joint ventures	151	135	234	389
Foreclosed assets	37	34	37	24
Tangible assets (net of depreciation)	1,254	1,204	700	683
Interest, fees and other assets	1,081	1,092	797	748
Total assets	**72,554**	**74,154**	**68,411**	**67,481**

Form "Balance sheet" / continued (in HRK million)		**GROUP**		**BANK**
	31 December 2012	31 December 2011	31 December 2012	31 December 2011
Liabilities				
Loans from financial institutions	8,910	9,273	7,895	7,957
Short-term loans	*954*	*1,298*	*951*	*1,298*
Long-term loans	*7,956*	*7,975*	*6,944*	*6,659*
Deposits	48,415	49,998	47,624	47,074
Giro account and current account deposits	*8,271*	*8,688*	*8,413*	*8,351*
Savings deposits	*7,451*	*6,647*	*7,291*	*6,050*
Time deposits	*32,693*	*34,663*	*31,920*	*32,673*
Other loans	-	-	-	-
Short-term loans	-	-	-	-
Long-term loans	-	-	-	-
Derivative financial liabilities and other financial liabilities held for trading	4	9	4	9
Debt securities issued	-	-	-	-
Short-term debt securities issued	-	-	-	-
Long-term debt securities issued	-	-	-	-
Subordinated instruments issued	-	-	-	-
Hybrid instruments issued	-	-	-	-
Interest, fees and other liabilities	2,437	2,552	1,162	1,247
Total liabilities	**59,766**	**61,832**	**56,685**	**56,287**
Equity				
Share capital	1,907	1,907	1,907	1,907
Current year profit (loss)	1,014	1,268	846	1,136
Retained earnings (loss)	8,025	7,326	7,180	6,368
Legal reserves	137	136	134	130
Statutory reserves and other capital reserves	1,732	1,733	1,667	1,665
Unrealised gains/losses on value adjustments of financial assets available for sale	(27)	(48)	(8)	(12)
Total equity	**12,788**	**12,322**	**11,726**	**11,194**
Total liabilities and equity	**72,554**	**74,154**	**68,411**	**67,481**

The balance sheet form is prepared in accordance with the CNB Decision on the Structure and Content of Annual Financial Statements for Banks.

Appendix 1 - Supplementary forms required by local regulation

The following tables provide reconciliation between statutory financial statements and supplementary schedules for CNB.

Balance sheet reconciliation as at 31 December 2012 (in HRK million)

	GROUP			BANK		
	CNB schedules	per IFRS	Differences	CNB schedules	per IFRS	Differences
Assets						
Cash and deposits with the Croatian National Bank	8,767	-	8,767	8,764	-	8,764
Cash	*1,401*	-	*1,401*	*1,398*	-	*1,398*
Deposits with the Croatian National Bank	*7,366*	-	*7,366*	*7,366*	-	*7,366*
Cash and current accounts with banks	-	4,171	(4,171)	-	4,168	(4,168)
Balances with the Croatian National Bank	-	5,657	(5,657)	-	5,657	(5,657)
Deposits with banking institutions	6,193	-	6,193	6,167	-	6,167
Loans and advances to banks	-	6,250	(6,250)	-	6,236	(6,236)
Ministry of Finance treasury bills and the Croatian National Bank bills	3,482	-	3,482	3,424	-	3,424
Financial assets at fair value through profit or loss	-	3,986	(3,986)	-	3,927	(3,927)
Securities and other financial instruments held for trading	18	-	18	18	-	18
Securities and other financial instruments available for sale	91	91	-	81	81	-
Securities and other financial instruments held to maturity	204	208	(4)	-	-	-
Securities and other financial instruments at fair value in profit or loss and not traded	380	-	380	380	-	380
Derivative financial assets	4	4	-	4	4	-
Loans to financial institutions	1,112	-	1,112	1,125	-	1,125
Loans to other clients	49,780	49,960	(180)	46,680	46,918	(238)
Investments in subsidiaries, associates and joint ventures	151	151	-	234	220	14
Foreclosed assets	37	-	37	37	-	37
Intangible assets	-	162	(162)	-	103	(103)
Investment property	-	9	(9)	-	9	(9)
Tangible assets (net of depreciation)	1,254	1,254	-	700	700	-
Deferred tax assets	-	177	(177)	-	132	(132)
Interest, fees and other assets	1,081	-	1,081	797	-	797
Other assets	-	474	(474)	-	256	(256)
Total assets	**72,554**	**72,554**	**-**	**68,411**	**68,411**	**-**

Balance sheet reconciliation as at 31 December 2012 (in HRK million)

	GROUP			BANK		
	CNB schedules	per IFRS	Differences	CNB schedules	per IFRS	Differences
Liabilities						
Loans from financial institutions	8,910	-	8,910	7,895	-	7,895
Short-term loans	*954*	-	*954*	*951*	-	*951*
Long-term loans	*7,956*	-	*7,956*	*6,944*	-	*6,944*
Interest-bearing borrowings	-	8,936	(8,936)	-	7,918	(7,918)
Deposits	48,415	-	48,415	47,624	-	47,624
Giro account and current account deposits	*8,271*	-	*8,271*	*8,413*	-	*8,413*
Savings deposits	*7,451*	-	*7,451*	*7,291*	-	*7,291*
Time deposits	*32,693*	-	*32,693*	*31,920*	-	*31,920*
Current accounts and deposits from banks	-	727	(727)	-	1,108	(1,108)
Current accounts and deposits from customers	-	48,143	(48,143)	-	46,973	(46,973)
Other loans	-	-	-	-	-	-
Short-term loans	-	-	-	-	-	-
Long-term loans	-	-	-	-	-	-
Derivative financial liabilities and other financial liabilities held for trading	4	4	-	4	4	-
Interest, fees and other liabilities	2,437	-	2,437	1,162	-	1,162
Accrued expenses and deferred income	-	201	(201)	-	81	(81)
Provisions for liabilities and charges	-	204	(204)	-	204	(204)
Other liabilities	-	1,518	(1,518)	-	394	(394)
Current tax liability	-	33	(33)	-	3	(3)
Total liabilities	**59,766**	**59,766**	**-**	**56,685**	**56,685**	**-**
Equity						
Share capital	1,907	1,907	-	1,907	1,907	-
Current year profit (loss)	1,014	-	1,014	846	-	846
Share premium	-	1,570	(1,570)	-	1,570	(1,570)
Treasury shares	-	(76)	76	-	(76)	76
Retained earnings (loss)	8,025	-	8,025	7,180	-	7,180
Legal reserves	137	-	137	134	-	134
Statutory reserves and other capital reserves	1,732	-	1,732	1,667	-	1,667
Other reserves	-	375	(375)	-	308	(308)
Unrealised gains/(losses) on value adjustments of financial assets available for sale	(27)	(27)	-	(8)	(8)	-
Retained earnings	-	9,039	(9,039)	-	8,025	(8,025)
Total equity	**12,788**	**12,788**	**-**	**11,726**	**11,726**	**-**
Total liabilities and equity	**72,554**	**72,554**	**-**	**68,411**	**68,411**	**-**

Appendix 1 - Supplementary forms required by local regulation

Balance sheet reconciliation as at 31 December 2012 / continued (in HRK million)

Differences between the captions and amounts disclosed in the statement of financial position in the statutory financial statements and balance sheet positions reported in accordance with CNB Decision are as follows:

Assets
Cash and deposits with the Croatian National Bank are presented separately in the CNB schedule, while in the statutory financial statements they are included within Cash and current accounts with banks and Balances with the Croatian National Bank.
Deposits with banking institutions and Loans to financial institutions are presented separately in the CNB schedule, while in the statutory financial statements they are included within Loans and advances to banks and Cash and current accounts with foreign and domestic banks.
Ministry of Finance treasury bills and CNB bills are presented separately in the CNB schedule, while in the statutory financial statements these securities are included within Financial assets at fair value through profit or loss and Financial assets available for sale.
Securities and other financial instruments held for trading and Securities and other financial instruments at fair value through profit or loss which are not actively traded but are designated at fair value through profit or loss are presented separately in the CNB schedule, while in the statutory financial statements they are included within Financial assets at fair value through profit or loss.
Foreclosed assets are presented separately in the CNB schedule, while in the statutory financial statements they are presented within Other assets.
Interest, fees and other assets in the CNB schedule include Intangible assets, Investment property and Deferred tax assets, while in the statutory financial statements these items are presented separately. In addition, this position includes all interest receivables, which are presented as part of respective assets in the statutory financial statements.

Liabilities
Loans from financial institutions and Other loans and disclosed separately in the CNB schedule while in the statutory financial statements they are included within Interest-bearing borrowings.
Deposits on giro and current accounts, Savings deposits and Term deposits are presented separately in the CNB schedule, while in the financial statements they are presented within Current accounts and deposits from banks and Current accounts and deposits from customers.
Interest, fees and other liabilities in the CNB schedule include Other liabilities, Accrued expenses and deferred income, Provisions for liabilities and charges and Current tax liability, while in the statutory financial statements these items are presented separately. In addition, this position includes all interest payable, which are presented as part of respective liabilities in the statutory financial statements.

Equity
Current year profit (loss) and Retained earnings (loss) are disclosed separately in the CNB schedule, while in the statutory financial statements they are presented jointly within Retained earnings. Other reserves from the statutory financial statements in the amount of HRK 375 million include Legal reserves in the amount of HRK 137 million and HRK 134 million for the Group and Bank, respectively and Other reserves in the amount of HRK 238 million and HRK 174 million for the Group and Bank, respectively. In the CNB schedule Legal reserves are shown separately, while the remaining Other reserves are included within Statutory reserves and other capital reserves. In addition, Statutory reserves and other capital reserves in the CNB schedule include Share premium and Treasury shares which are shown separately in the statutory financial statements.

Form "Income statement" (in HRK million)	GROUP		BANK	
	2012	2011	2012	2011
Interest income	3,850	3,935	3,550	3,599
(Interest expenses)	(1,444)	(1,455)	(1,337)	(1,331)
Net interest income	**2,406**	**2,480**	**2,213**	**2,268**
Income from fees and commissions	1,353	1,352	623	624
(Expenses on fees and commissions)	(263)	(240)	(117)	(114)
Net income from fees and commissions	**1,090**	**1,112**	**506**	**510**
Gains/(losses) from investments in subsidiaries, associates and joint ventures	16	18	-	-
Gains/(losses) from trading activities	(1)	(1)	(1)	(1)
Gains/(losses) from embedded derivatives	-	-	-	-
Gains/(losses) from financial assets at fair value through profit or loss and not traded	(54)	2	(56)	2
Gains/(losses) from activities related to assets available for sale	8	6	2	3
Gains/(losses) from activities related to assets held to maturity	-	-	-	-
Gains/(losses) from hedging transactions	-	-	-	-
Income from equity investments in subsidiaries, associates and joint ventures	-	-		-
Income from other equity investments	3	4	143	179
Gains/(losses) from exchange differences	198	145	193	143
Other income	111	126	35	42
Other expenses	(493)	(472)	(313)	(278)
General administrative expenses and depreciation	(1,423)	(1,470)	(1,091)	(1,139)
Net operating income before value adjustments and loss provisions	**1,861**	**1,950**	**1,631**	**1,729**
Impairment expenses	(589)	(369)	(603)	(353)
Income (loss) before taxes	**1,272**	**1,581**	**1,028**	**1,376**
Income tax	(258)	(313)	(182)	(240)
Current year profit (loss)	**1,014**	**1,268**	**846**	**1,136**

The income statement form is prepared in accordance with the CNB Decision on the Structure and Content of Annual Financial Statements for Banks.

Appendix 1 - Supplementary forms required by local regulation

Income statement reconciliation for the year ended 31 December 2012 (in HRK million)

	GROUP			BANK		
	CNB schedules	per IFRS	Differences	CNB schedules	per IFRS	Differences
Interest income	3,850	3,850	-	3,550	3,550	-
(Interest expenses)	(1,444)	(1,444)	-	(1,337)	(1,337)	-
Net interest income	**2,406**	**2,406**	**-**	**2,213**	**2,213**	**-**
Income from fees and commissions	1,353	1,353	-	623	623	-
(Expenses on fees and commissions)	(263)	(263)	-	(117)	(117)	-
Net income from fees and commissions	**1,090**	**1,090**	**-**	**506**	**506**	**-**
Gains/(losses) from investments in subsidiaries, associates and joint ventures	16	16	-	-	-	-
Gains/(losses) from trading activities	(1)	-	(1)	(1)	-	(1)
Gains/(losses) from embedded derivatives	-	-	-	-	-	-
Gains/(losses) from financial assets at fair value through profit or loss and not traded	(54)	-	(54)	(56)	-	(56)
Net trading income and net loss on translation of monetary assets and liabilities	-	143	(143)	-	136	(136)
Gains/(losses) from activities related to assets available for sale	8	-	8	2	-	2
Gains/(losses) from activities related to assets held to maturity	-	-	-	-	-	-
Gains/(losses) from hedging transactions	-	-	-	-	-	-
Income from equity investments in subsidiaries, associates and joint ventures	-	-	-	-	-	-
Income from other equity investments	3	3	-	143	143	-
Gains/(losses) from exchange differences	198	-	198	193	-	193
Other income	111	-	111	35	-	35
Other operating income	-	119	(119)	-	37	(37)
Other expenses	(493)	-	(493)	(313)	-	(313)
Personnel expenses	-	(724)	724	-	(610)	610
Other operating expenses	-	(1,001)	1,001	-	(670)	670
General administrative expenses and depreciation	(1,423)	-	(1,423)	(1,091)	-	(1,091)
Depreciation and amortisation	-	(191)	191	-	(124)	124
Net operating income before value adjustments and loss provisions	**1,861**	**1,861**	**-**	**1,631**	**1,631**	-
Impairment expenses	(589)	-	(589)	(603)	-	(603)
Impairment losses on loans and advances to customers	-	(543)	543	-	(560)	560
Other impairment losses and provisions	-	(46)	46	-	(43)	43
Income (loss) before taxes	**1,272**	**1,272**	**-**	**1,028**	**1,028**	**-**
Income tax	(258)	(258)	-	(182)	(182)	-
Current year profit (loss)	**1,014**	**1,014**	**-**	**846**	**846**	**-**

Income statement reconciliation for the year ended 31 December 2012 / continued

Differences between the income statement positions disclosed in the statutory financial statements, and those prescribed by the CNB Decision relate to the following categories:

Gains/(losses) from trading activities, Gains/(losses) from financial assets at fair value through profit or loss and not traded and Gains/(losses) from exchange differences are disclosed separately in the CNB schedules while in the statutory financial statements they are shown within Net trading income and net loss on translation of monetary assets and liabilities.
Gains/(losses) from investments in subsidiaries, associates and joint ventures, Gains/(losses) from activities related to assets available for sale and Other income in the CNB schedule are presented separately while in the statutory financial statements they are included within Other operating income.
Depreciation and amortisation is disclosed separately in the statutory financial statements, while in the CNB schedule they are included within General administrative expenses and depreciation. This position also includes Personnel expenses and Other operating expenses from the statutory financial statements except for deposit insurance premiums, Operating leases and Other operating expenses which are included within Other expenses in the CNB schedule.
Impairment expenses in the CNB schedule include Impairment losses on loans and advances to customers and Other impairment losses and provisions while in the statutory financial statements these items are presented separately.

Appendix 1 - Supplementary forms required by local regulation

Form "Cash flow statement" (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Cash flow from operating activities				
Gains (losses) before tax	1,272	1,581	1,028	1,376
Impairment	589	369	603	353
Depreciation	191	213	124	141
(Gains) losses from sale of tangible assets	(5)	(90)	(1)	(15)
Other (gains) losses	(10)	(17)	(146)	(265)
Cash flow from operating activities before changes in operating assets	**2,037**	**2,056**	**1,608**	**1,590**
(Increase) decrease in operating assets				
Deposits with the Croatian National Bank	322	(397)	314	(390)
Ministry of Finance treasury bills and Croatian National Bank bills	(808)	206	(1,387)	322
Deposits with banking institutions and loans to financial institutions	(619)	(133)	(145)	(370)
Loans to other clients	879	(2,246)	500	(2,398)
Securities and other financial instruments held for trading	5	(1)	5	(1)
Securities and other financial instruments available for sale	247	615	89	559
Securities and other financial instruments at fair value in profit or loss and not traded	12	3	10	3
Other operating assets	-	(195)	582	74
Net (increase)/decrease in operating assets	**38**	**(2,148)**	**(32)**	**(2,201)**
Increase (decrease) in operating liabilities				
Demand deposits	(418)	692	447	318
Savings and time deposits	(1,165)	(1,464)	(2,252)	(611)
Derivative financial liabilities and other liabilities held for trading	-	-	-	-
Other liabilities	(163)	189	(337)	(111)
Net increase (decrease) in operating liabilities	**(1,746)**	**(583)**	**(2,142)**	**(404)**
Net cash flow from operating activities	**329**	**(675)**	**(566)**	**(1,015)**
(Profit tax paid)	(305)	(288)	(254)	(188)
Net inflow (outflow) of cash from operating activities	**24**	**(963)**	**(820)**	**(1,203)**

Form "Cash flow statement" / continued (in HRK million)

	GROUP		BANK	
	2012	2011	2012	2011
Investing activities				
Cash receipts from (payments to acquire) tangible and intangible assets	(197)	(136)	(81)	10
Cash receipts from the disposal of (payments for the investment in) subsidiaries, associates and joint ventures	-	-	899	3
Cash receipts from sales of (cash payments to acquire) securities and other financial instruments held until maturity	180	249	120	250
Dividends received	3	4	143	179
Other receipts from (payments for) investments	-	-	-	-
Net cash flow from investing activities	**(14)**	**117**	**1,081**	**442**
Financing activities				
Net increase (decrease) in received loans	(363)	(584)	(170)	(448)
Net increase (decrease) in issued debt securities	-	-	-	-
Net increase (decrease) in subordinated and hybrid instruments	-	-	-	-
Proceeds from issue of share capital	-	-	-	-
(Dividends paid)	(569)	(301)	(569)	(301)
Other proceeds (payments) from financing activities	-	-	-	-
Net cash flow from financing activities	**(932)**	**(885)**	**(739)**	**(749)**
Net increase (decrease) in cash and cash equivalents	**(922)**	**(1,731)**	**(478)**	**(1,510)**
Effect of exchange differences on cash and cash equivalents	5	(24)	5	(24)
Net increase (decrease) in cash and cash equivalents	**(917)**	**(1,755)**	**(473)**	**(1,534)**
Cash and cash equivalents at the beginning of the year	11,024	12,779	10,588	12,122
Cash and cash equivalents at the end of the year	**10,107**	**11,024**	**10,115**	**10,588**

Appendix 1 - Supplementary forms required by local regulation

Cash flow statement reconciliation for the year ended 31 December 2012 (in HRK million)

	GROUP			BANK		
	CNB schedules	per IFRS	Differences	CNB schedules	per IFRS	Differences
Cash flow from operating activities						
Gains (losses) before tax	1,272	1,272	-	1,028	1,028	-
Impairment	589	-	589	603	-	603
Impairment losses on loans and advances to customers	-	543	(543)	-	560	(560)
Other impairment losses and provisions	-	46	(46)	-	43	(43)
Depreciation	191	191	-	124	124	-
(Gains) losses from sale of tangible assets	(5)	(5)	-	(1)	(1)	-
Other (gains) losses	(10)	-	(10)	(146)	-	(146)
Net losses/(gains) from securities initially designated at fair value through profit or loss	-	54	(54)	-	56	(56)
Share of profit from associates	-	(16)	16	-	-	-
Net interest income	-	(2,406)	2,406	-	(2,213)	2,213
Dividend income	-	(3)	3	-	(143)	143
Cash flow from operating activities before changes in operating assets	**2,037**	**(324)**	**2,361**	**1,608**	**(546)**	**2,154**
(Increase) decrease in operating assets						
Deposits with the Croatian National Bank	322	322	-	314	715	(401)
Ministry of Finance treasury bills and Croatian National Bank bills	(808)	-	(808)	(1,387)	-	(1,387)
Deposits with banking institutions and loans to financial institutions	(619)	(635)	16	(145)	(131)	(14)
Loans to other clients	879	1,210	(331)	500	617	(117)
Securities and other financial instruments held for trading	5	-	5	5	-	5
Securities and other financial instruments available for sale	247	-	247	89	-	89
Securities and other financial instruments at fair value in profit or loss and not traded	12	-	12	10	-	10
Financial assets held for trading and financial assets available for sale	-	(655)	655	-	(1,398)	1,398
Other operating assets	-	-	-	582	-	582
Other assets	-	44	(44)	-	36	(36)
Net (increase)/decrease in operating assets	**38**	**286**	**(248)**	**(32)**	**(161)**	**129**
Increase (decrease) in operating liabilities						
Demand deposits	(418)	-	(418)	447	-	447
Savings and time deposits	(1,165)	-	(1,165)	(2,252)	-	(2,252)
Current accounts and deposits from banks	-	(2,267)	2,267	-	(2,319)	2,319
Current accounts and deposits from customers	-	780	(780)	-	615	(615)
Derivative financial liabilities and other liabilities held for trading	-	-	-	-	-	-
Other liabilities	(163)	(120)	(43)	(337)	(100)	(237)
Net increase (decrease) in operating liabilities	**(1,746)**	**(1,607)**	**(139)**	**(2,142)**	**(1,804)**	**(338)**

Cash flow statement reconciliation for the year ended 31 December 2012 / continued (in HRK million)

	GROUP			BANK		
	CNB schedules	per IFRS	Differences	CNB schedules	per IFRS	Differences
Interest received	-	3,536	(3,536)	-	3,409	(3,409)
Interest paid	-	(1,512)	1,512	-	(1,412)	1,412
Dividends received	-	3	(3)	-	143	(143)
Net cash flow from operating activities	**329**	**382**	**(53)**	**(566)**	**(371)**	**(195)**
(Profit tax paid)	(305)	(305)	-	(254)	(254)	-
Net inflow (outflow) of cash from operating activities	**24**	**77**	**(53)**	**(820)**	**(625)**	**(195)**
Investing activities						
Cash receipts from (payments to acquire) tangible and intangible assets	(197)	-	(197)	(81)	-	(81)
Purchase of property and equipment and intangible assets	-	(411)	411	-	(124)	124
Cash receipts from the disposal of (payments for the investment in) subsidiaries, associates and joint ventures	-	-	-	899	-	899
Disposal of property and equipment and intangible assets	-	173	(173)	-	2	(2)
Cash receipts from sales of (cash payments to acquire) securities and other financial instruments held until maturity	180	183	(3)	120	124	(4)
Dividends received	3	-	3	143	-	143
Other receipts from (payments for) investments	-	-	-	-	-	-
Net cash flow from investing activities	**(14)**	**(55)**	**41**	**1,081**	**2**	**1,079**
Financing activities						
Net increase (decrease) in received loans	(363)	(375)	12	(170)	(180)	10
Net increase (decrease) in issued debt securities	-	-	-	-	-	-
Net increase (decrease) in subordinated and hybrid instruments	-	-	-	-	-	-
Proceeds from issue of share capital	-	-	-	-	-	-
(Dividends paid)	(569)	(569)	-	(569)	(569)	-
Other proceeds (payments) from financing activities	-	-	-	-	-	-
Net cash flow from financing activities	**(932)**	**(944)**	**12**	**(739)**	**(749)**	**10**
Cash and cash equivalents acquired on merger of Međimurska banka	-	-	-	-	894	(894)
Net increase (decrease) in cash and cash equivalents	**(922)**	**(922)**	**-**	**(478)**	**(478)**	**-**
Effect of exchange differences on cash and cash equivalents	5	5	-	5	5	-
Net increase/(decrease) in cash and cash equivalents	**(917)**	**(917)**	**-**	**(473)**	**(473)**	**-**
Cash and cash equivalents at the beginning of the year	11,024	11,024	-	10,588	10,588	-
Cash and cash equivalents at the end of the year	**10,107**	**10,107**	**-**	**10,115**	**10,115**	**-**

Appendix 1 - Supplementary forms required by local regulation

Cash flow statement reconciliation for the year ended 31 December 2012 / continued

Differences between the cash flows positions disclosed in the statutory financial statements, and those prescribed by the CNB Decision relate to the following categories:
Net interest income, interest received and interest paid are disclosed separately in the statutory financial statements while in the CNB schedule they are included as part of the increase/decrease in operative assets and liabilities.
Dividends received are treated as cash flow from Operating activities in the statutory financial statements, while in the CNB schedule they are included within Investing activities.
Impairment losses on loans and advances to customers and Other impairment losses and provisions are disclosed separately in the statutory financial statements while in the CNB schedule they are included within Impairment.
Other (gains) losses in the CNB schedule include Net (gains)/losses from securities initially designated at fair value through profit or loss and Dividend income which are disclosed separately in the statutory financial statements.
Share of profit from associates is presented separately in the statutory financial statements while in the CNB schedule it is included within Other operating assets.
Net change in Ministry of Finance treasury bills and Croatian National Bank bills, Securities and other financial instruments held for trading, Securities and other financial instruments available for sale and Securities and other financial instruments at fair value in profit or loss and not traded are presented separately in the CNB schedule while in the statutory financial statements they are included within the position Financial assets held for trading and financial assets available for sale.
Cash receipts from (payments to acquire) tangible and intangible assets in the CNB schedule include net proceeds from purchase/sale of tangible and intangible assets and foreclosed assets. In the statutory financial statements purchase and disposal of property and equipment and intangible assets are disclosed separately within cash flows from investing activities and net proceeds from foreclosed assets are shown within Other assets.
Cash and cash equivalents acquired on merger of Međimurska banka are disclosed as a separate line item in the statutory financial statements while in the CNB schedule this position is included as part of Cash receipts from the disposal of (payments for the investment in) subsidiaries, associates and joint ventures.

Form "Statement of changes in equity " (in HRK million)

	Share capital	Treasury shares	Legal, statutory and other reserves	Retained earnings/ (loss)	Current year profit/loss	Unrealised gains/ (losses) on value adjustments of financial assets available for sale	Minority interest	Total equity and reserves
Group								
Balance as at 1 January 2012	**1,907**	**(76)**	**1,945**	**7,326**	**1,268**	**(48)**	**-**	**12,322**
Changes in accounting policies and correction of errors	-	-	-	-	-	-	-	-
Closing balance as at 1 January 2012	**1,907**	**(76)**	**1,945**	**7,326**	**1,268**	**(48)**	**-**	**12,322**
Sale of available-for-sale financial assets	-	-	-	-	-	(8)	-	(8)
Changes in fair value of the portfolio of available-for sale financial assets	-	-	-	-	-	3	-	3
Tax on items recognised directly or transferred from equity and reserves	-	-	-	-	-	(5)	-	(5)
Other gains and losses recognised directly in equity and reserves	-	-	-	-	-	31	-	31
Net gains (losses) recognised directly in equity and reserves	**-**	**-**	**-**	**-**	**-**	**21**	**-**	**21**
Current year profit/loss	-	-	-	-	1,014	-	-	1,014
Total current year income and expenses	**-**	**-**	**-**	**-**	**1,014**	**21**	**-**	**1,035**
Increase/(decrease) of share capital	-	-	-	-	-	-	-	-
(Purchase)/sale of treasury shares	-	-	-	-	-	-	-	-
Other changes	-	-	-	-	-	-	-	-
Transfer to reserves	-	-	-	699	(699)	-	-	-
Dividend payments	-	-	-	-	(569)	-	-	(569)
Profit distribution	**-**	**-**	**-**	**699**	**(1,268)**	**-**	**-**	**(569)**
Closing balance as at 31 December 2012	**1,907**	**(76)**	**1,945**	**8,025**	**1,014**	**(27)**	**-**	**12,788**

Appendix 1 - Supplementary forms required by local regulation

Form "Statement of changes in equity " / continued (in HRK million)

	Share capital	Treasury shares	Legal, statutory and other reserves	Retained earnings/ (loss)	Current year profit/loss	Unrealised gains/ (losses) on value adjustments of financial assets available for sale	Minority interest	Total equity and reserves
Group								
Balance as at 1 January 2011	**1,907**	**(76)**	**1,943**	**6,607**	**1,022**	**(69)**	**-**	**11,334**
Changes in accounting policies and correction of errors	-	-	-	-	-	-	-	-
Closing balance as at 1 January 2011	**1,907**	**(76)**	**1,943**	**6,607**	**1,022**	**(69)**	**-**	**11,334**
Sale of available-for-sale financial assets	-	-	-	-	-	(6)	-	(6)
Changes in fair value of the portfolio of available-for-sale financial assets	-	-	-	-	-	(19)	-	(19)
Tax on items recognised directly or transferred from equity and reserves	-	-	-	-	-	(6)	-	(6)
Other gains and losses recognised directly in equity and reserves	-	-	-	-	-	52	-	52
Net gains (losses) recognised directly in equity and reserves	**-**	**-**	**-**	**-**	**-**	**21**	**-**	**21**
Current year profit/loss	-	-	-	-	1,268	-	-	1,268
Total current year income and expenses	**-**	**-**	**-**	**-**	**1,268**	**21**	**-**	**1,289**
Increase/(decrease) of share capital	-	-	-	-	-	-	-	-
(Purchase)/sale of treasury shares	-	-	-	-	-	-	-	-
Other changes	-	-	-	-	-	-	-	-
Transfer to reserves	-	-	2	719	(721)	-	-	-
Dividend payments	-	-	-	-	(301)	-	-	(301)
Profit distribution	**-**	**-**	**2**	**719**	**(1,022)**	**-**	**-**	**(301)**
Closing balance as at 31 December 2011	**1,907**	**(76)**	**1,945**	**7,326**	**1,268**	**(48)**	**-**	**12,322**

Form "Statement of changes in equity " / continued (in HRK million)

	Share capital	Treasury shares	Legal, statutory and other reserves	Retained earnings/ (loss)	Current year profit/loss	Unrealised gains/ (losses) on value adjustments of financial assets available for sale	Total equity and reserves
Bank							
Balance as at 1 January 2012	**1,907**	**(76)**	**1,870**	**6,368**	**1,136**	**(11)**	**11,194**
Changes in accounting policies and correction of errors	-	-	-	-	-	-	-
Closing balance as at 1 January 2012	**1,907**	**(76)**	**1,870**	**6,368**	**1,136**	**(11)**	**11,194**
Sale of available-for-sale financial assets	-	-	-	-	-	(2)	(2)
Changes in fair value of the portfolio of available-for sale financial assets	-	-	-	-	-	(8)	(8)
Tax on items recognised directly or transferred from equity and reserves	-	-	-	-	-	(1)	(1)
Other gains and losses recognised directly in equity and reserves	-	-	-	-	-	15	15
Net gains (losses) recognised directly in equity and reserves	**-**	**-**	**-**	**-**	**-**	**4**	**4**
Current year profit/loss	-	-	-	-	846	-	846
Total current year income and expenses	**-**	**-**	**-**	**-**	**846**	**4**	**850**
Increase/(decrease) of share capital	-	-	-	-	-	-	-
(Purchase)/sale of treasury shares	-	-	-	-	-	-	-
Other changes	-	-	8	244	-	(1)	251
Transfer to reserves	-	-	-	567	(567)	-	-
Dividend payments	-	-	-	-	(569)	-	(569)
Profit distribution	**-**	**-**	**-**	**567**	**(1,136)**	**-**	**(569)**
Closing balance as at 31 December 2012	**1,907**	**(76)**	**1,878**	**7,179**	**846**	**(8)**	**11,726**

Appendix 1 - Supplementary forms required by local regulation

Form "Statement of changes in equity " / continued (in HRK million)

	Share capital	Treasury shares	Legal, statutory and other reserves	Retained earnings/ (loss)	Current year profit/loss	Unrealised gains/ (losses) on value adjustments of financial assets available for sale	Total equity and reserves
Bank							
Balance as at 1 January 2011	**1,907**	**(76)**	**1,870**	**5,809**	**860**	**(24)**	**10,346**
Changes in accounting policies and correction of errors	-	-	-	-	-	-	-
Closing balance as at 1 January 2011	**1,907**	**(76)**	**1,870**	**5,809**	**860**	**(24)**	**10,346**
Sale of available-for-sale financial assets	-	-	-	-	-	(3)	(3)
Changes in fair value of the portfolio of available-for sale financial assets	-	-	-	-	-	(14)	(14)
Tax on items recognised directly or transferred from equity and reserves	-	-	-	-	-	(3)	(3)
Other gains and losses recognised directly in equity and reserves	-	-	-	-	-	33	33
Net gains (losses) recognised directly in equity and reserves	**-**	**-**	**-**	**-**	**-**	**13**	**13**
Current year profit/loss	-	-	-	-	1,136	-	1,136
Total current year income and expenses	**-**	**-**	**-**	**-**	**1,136**	**13**	**1,149**
Increase/(decrease) of share capital	-	-	-	-	-	-	-
(Purchase)/sale of treasury shares	-	-	-	-	-	-	-
Other changes	-	-	-	-	-	-	-
Transfer to reserves	-	-	-	559	(559)	-	-
Dividend payments	-	-	-	-	(301)	-	(301)
Profit distribution	**-**	**-**	**-**	**559**	**(860)**	**-**	**(301)**
Closing balance as at 31 December 2011	**1,907**	**(76)**	**1,870**	**6,368**	**1,136**	**(11)**	**11,194**

Statement of changes in equity reconciliation
The statement of changes in equity form is prepared in accordance with the CNB Decision on the Structure and Content of Annual Financial Statements for Banks.
Legal, statutory and other reserves in the CNB schedule include Share premium and Other reserves which are presented separately in the statutory financial statements.
Retained earnings and Profit for the year are presented separately in the CNB schedule while in the statutory financial statements they are included within Retained earnings.
Sale of available-for-sale financial assets and Other gains and losses recognised directly in equity and reserves are shown separately in the CNB schedule while in the statutory financial statements they are shown within Net amount transferred to the income statement.
Other changes in the CNB schedule for the year ended 31 December 2012 for the Bank relate to balances acquired on merger with Međimurska banka as disclosed in the statutory financial statements.

Appendix 2 - Supplementary financial statements in EUR (unaudited)

Income statement

	GROUP		BANK	
(in EUR million)	2012	2011	2012	2011
Interest income	511	529	472	484
Interest expense	(192)	(196)	(178)	(179)
Net interest income	**319**	**333**	**294**	**305**
Fee and commission income	180	182	83	84
Fee and commission expense	(35)	(32)	(16)	(15)
Net fee and commission income	**145**	**150**	**67**	**69**
Dividend income	-	1	19	24
Net trading income and net loss on translation of monetary assets and liabilities	19	20	18	19
Other operating income	16	18	5	6
Revenue	**499**	**522**	**403**	**423**
Personnel expenses	(96)	(104)	(81)	(88)
Impairment losses on loans and advances to customers	(72)	(42)	(74)	(40)
Other impairment losses and provisions	(6)	(7)	(6)	(8)
Depreciation and amortisation	(25)	(29)	(16)	(19)
Other operating expenses	(133)	(129)	(89)	(83)
Share of profits from associates	2	2	-	-
Profit before income tax	**169**	**213**	**137**	**185**
Income tax expense	(34)	(42)	(24)	(32)
Profit for the year	**135**	**171**	**113**	**153**
Attributable to:				
Equity holders of the parent	135	171	113	153
	135	**171**	**113**	**153**

The income statement items were translated from the measurement currency (HRK) to the Euro at the average exchange rate in 2012 (1 EUR = 7.517340 HRK) and in 2011 (1 EUR = 7.434204 HRK).

Appendix 2 - Supplementary financial statements in EUR (unaudited)

Statement of financial position

As at 31 December (in EUR million)	GROUP 2012	GROUP 2011	BANK 2012	BANK 2011
Assets				
Cash and current accounts with banks	553	351	552	327
Balances with the Croatian National Bank	750	928	750	897
Financial assets at fair value through profit or loss	528	332	520	332
Derivative financial assets	1	1	1	1
Loans and advances to banks	828	934	826	960
Loans and advances to customers	6,621	6,825	6,218	6,200
Financial assets available for sale	12	131	11	25
Held-to-maturity investments	28	52	-	17
Investments in subsidiaries and associates	20	18	29	52
Intangible assets	21	21	14	11
Property and equipment	166	160	93	91
Investment property	1	2	1	1
Non-current assets held for sale	-	4	-	4
Deferred tax assets	23	23	17	16
Other assets	63	65	34	27
Total assets	**9,615**	**9,847**	**9,066**	**8,961**

The items of the statement of financial position were translated from the measurement currency (HRK) to the Euro at the closing exchange rates as at 31 December 2012 (1 EUR = 7.545624 HRK) and as at 31 December 2011 (1 EUR = 7.53042 HRK).

Statement of financial position / continued

As at 31 December (in EUR million)	GROUP 2012	GROUP 2011	BANK 2012	BANK 2011
Liabilities				
Current accounts and deposits from banks	96	398	147	455
Current accounts and deposits from customers	6,380	6,299	6,225	5,854
Derivative financial liabilities	1	1	1	1
Interest-bearing borrowings	1,184	1,236	1,049	1,061
Other liabilities	202	217	52	61
Accrued expenses and deferred income	27	26	11	10
Provisions for liabilities and charges	27	25	27	25
Current tax liability	4	9	-	8
Total liabilities	**7,921**	**8,211**	**7,512**	**7,475**
Equity attributable to equity holders of the parent				
Share capital	253	253	253	253
Share premium	208	208	208	208
Treasury shares	(10)	(10)	(10)	(10)
Other reserves	50	50	41	40
Fair value reserve	(4)	(6)	(1)	(1)
Retained earnings	1,197	1,141	1,063	996
Total equity	**1,694**	**1,636**	**1,554**	**1,486**
Total liabilities and equity	**9,615**	**9,847**	**9,066**	**8,961**

The items of the statement of financial position were translated from the measurement currency (HRK) to the Euro at the closing exchange rates as at 31 December 2012 (1 EUR = 7.545624 HRK) and as at 31 December 2011 (1 EUR = 7.53042 HRK).

Publisher **Privredna banka Zagreb d.d.**
Design & Production **Havas Worldwide Zagreb, a member of Unex Group**
Photography **Ivo Pervan**
Printing **Intergrafika** • Edition **400**

Annual Report 2012 in pdf version is available for download on
www.pbz.hr