HRVATSKA POŠTANSKA BANKA

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• ANNUAL REPORT 2006 •

CONTENTS

Introduction

The annual report comprises the summary of financial information, description of operation and the audited financial statements, including Independent auditors' report for the year ended 31 December 2006, in Croatian and English.

Legal form

The annual report comprises the annual financial statements prepared in accordance with accounting regulations applicable to banks in the Republic of Croatia and audited in accordance with International Standards on Auditing.

The annual report is prepared in compliance with the Accounting Law and the Companies Act, which prescribe reporting of the Management Board to the shareholders at the General Assembly.

Abbreviations

In the annual financial statements, Hrvatska poštanska banka d.d. is referred to as "the Bank" or "HPB", the Croatian National Bank as "the CNB", the Republic of Croatia as "RH" and the Croatian Bank for Construction and Development as "HBOR".

Exchange rates

The following CNB exchange rates were used for translation of foreign currencies into Croatian kuna:

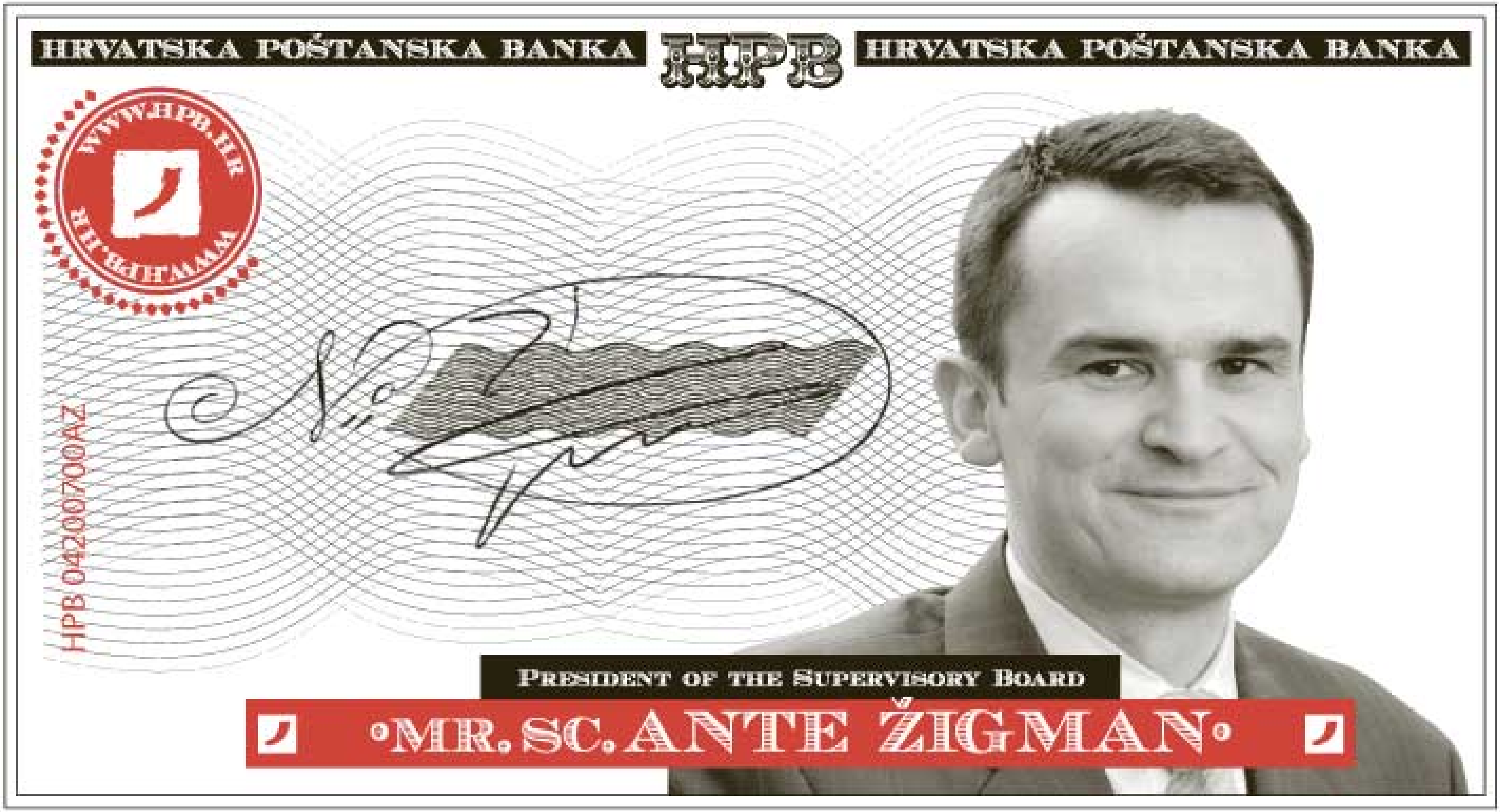
31 December 2006	EUR 1 = HRK 7.345081	USD 1 = HRK 5.578401
31 December 2005	EUR 1 = HRK 7.375626	USD 1 = HRK 6.233626

Summary of Operation and Key Financial Indicators

in HRK million	2006	2005	restated 2004	2003[1]	2002[1]
Key indicators					
Net profit for the year	101	90	60	84	71
Total assets	11,278	7,283	5,556	5,417	5,541
Loans and advances to customers	5,998	2,943	2,575	2,436	2,036
Deposits	8,651	5,056	4,365	4,369	4,611
Equity	840	749	656	590	506
Other indicators					
Return on share capital	17.29%	15.42%	10.30%	14.43%	12.16%
Return on assets	0.90%	1.24%	1.08%	1.56%	1.28%
Operating expenses[2]/operating income ratio	70.27%	60.93%	48.62%	51.35%	43.26%
Guarantee capital	866	682	619	535	465
Capital adequacy	11.45%	16.45%	24.32%	25.65%	22.58%

[1] figures not restated

[2] general and administrative expenses and depreciation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PRESIDENT OF THE SUPERVISORY BOARD
MR. SC. ANTE ŽIGMAN

Statement of the President of the Supervisory Board

Dear shareholders,

I am proud to present the Annual Report of the Bank for the year ended 31 December 2006.

In 2006, Hrvatska poštanska banka continued realising its adopted strategic plans which improved the quality of the Bank's operation, which is also witnessed by the best operating results realised since the Bank's foundation. According to 2006 operating results, on the dynamic and competitive Croatian banking market, the Bank increased its market share to 3.7% share in total assets of the banks. The operating results confirm the continuation of the Bank's and the Group's exceptional performance commenced two years ago. This is also confirmed by the confidence given to the Group's management and all its employees who, with their professional approach to work and their commitment, further strengthen the image of the Bank and the Group.

Among the most successful achievements was the increase in the Bank's assets by 54.9%, which in 2006 amounted to HRK 11.3 billion. Net loans to customers increased by 103.8% or HRK 3.1 billion, and deposits from customers by 62.9% or HRK 3.1 billion. Profit after tax amounted to HRK 101.1 million, and return on share capital amounted to 17.3%. A significant increase in the Bank's assets resulted in a decrease in the capital adequacy rate which, at 2006 year end, amounted to 11.5%. Because of this and because of its intensive investment in the development of its network and operation in general, the Bank already commenced a number of activities aimed at increasing capital. I must emphasize that Hrvatska poštanska banka is the largest domestic bank, and that there is a clear vision and desire of the Supervisory Board that the Bank retains Croatian ownership in the future.

Except by the realisation of the financial goals, 2006 was also marked by further improvement of the quality of services and products which put the Bank and the Group ahead of their competitors. Namely, a very active development of the financial market influenced on the fast development of all the segments of operation of the Group, primarily the investment funds. Other Group members also significantly contributed to the last year's result and the improvement in the quality of services and the overall offer of the innovative solutions to customers.

Hrvatska poštanska banka continued to offer competitive and distinctive products in a way that a number of products were adjusted to comply with different customer needs. We improved operation in all aspects of activities that comprise customer's interaction with the Bank. This includes the extension of the network of branches and other channels of distribution and continuation of cooperation with the strategic partner - Croatian post. The Bank succeeded to attract a significant number of customers on regional level and the level of towns, and succeeded to intensify the area of deposits in almost all regions in Croatia.

Among a number of successfully conducted projects, I must stress the independent performance of the domestic payment transactions, introduction of retail and corporate internet banking and a successful organisation of payment of the first two instalments of debt to Umirovljenički fond members. The Bank continued its project of introducing a new integral banking information system which will allow improvement of the quality of customer services and a faster and simplified introduction of new banking products and services. Furthermore, the HPB Group was extended by the foundation of HPB Stambena štedionica, and the results of the funds managed by HPB Invest, made them ones of the leading investment funds in RH.

In terms of corporate operation and transactions on the share capital market, in 2006 the Bank successfully kept pace with customer needs by improving its existing and introducing new products, with always a stronger emphasis on advisory and capital transactions for clients.

I am proud that Hrvatska poštanska banka celebrated its 15th anniversary as a successful, modern and competitive bank, which, on the current dynamic financial market, is continuously improving the quality of its operation and continues to grow. I must emphasize that good and open cooperation between the Supervisory Board and the Management of the Bank was continued, and that on their regular meetings, the Management Board regularly reported all the plans, decisions and achievements to the Supervisory Board.

Based on its core values of being a secure, profitable and dynamic domestic Bank, Hrvatska poštanska banka will continue to be the leader on the market in the next period, and its management will continue to focus on improving the Bank's market position, continuous improvement of the quality of services and development of a quality relationship with its customers, primarily taking into consideration their expectations in accordance with their needs and capabilities. Such a relationship with its customers will differ the Bank from all other banks on the Croatian, very competitive market.

On behalf of the Supervisory Board of Hrvatska poštanska banka, I would like to thank to all our clients and business partners for their confidence during the previous year. I would also like to thank to all the employees of the Bank for their high quality and professional performance, to all the Supervisory Board members for their cooperation and to the Management Board of Hrvatska poštanska banka for the professional and successful management of the Bank.

mr.sc. Ante Žigman

President of the Supervisory Board


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President of the Management Board
JOSIP PROTEGA

Statement of the President of the Management Board

Dear shareholders, business partners, customers,

On behalf of the Management Board, I am proud to present the Annual Report of the Bank for the year ended 31 December 2006.

Hrvatska poštanska banka closed its 2006 operation with a great success. In 2006, the Bank celebrated its 15th anniversary of operation and existence, which was the opportunity to remind ourselves of the goals and visions set at the Bank's foundation - to become a prominent domestic financial institution which focuses the strength of national economy on cash flows. We believe that a large number of those goals were realised during the past 15 years. Exceptional financial results, a number of realised strategic projects, further strengthening of customer relationship throughout Croatia and an enhanced offer of products and services, especially those focused on small and medium entrepreneurship, witness that 2006 was the best year in the operation of Hrvatska poštanska banka since its foundation.

Last year, the Bank achieved strong growth, in accordance with its strategy and its detailed, accepted business plans. The 2006 increase in the Bank's balance sheet by more than 50% as compared to 2005, is the result of the balanced, continuous and planned growth in different field of banking operation.

The 2006 financial results recorded growth and the realisation of a significant profit compared to the past period. The Bank's assets amount to HRK 11.3 billion, representing a 54.9% increase compared to 2005. Profit after tax increased by 12.2% compared to 2005, amounting to HRK 101.1 million. In the field of corporate finance, the Bank continued to significantly increase loans to commercial companies, while simultaneously decreasing the share of loans to state units. Gross retail loans increased by 81.7%, amounting to HRK 1.7 billion at year end.

Total deposits at year end amounted to HRK 8.7 billion, representing a 71.1% increase, whereby it should be noted that, within the total deposits structure, term deposits increased by 194.8%.

In 2006, the Bank intensively worked on its organic growth, increasing the quality of services and developing and modernizing the offer of financial products of the Bank and the HPB Group.

In the same period, the Bank also extended the palette of its retail and corporate loans, savings and credit-card products, thus offering VISA Business and MasterCard Gold cards to its customers, as well as retail and corporate Internet banking services and payment transaction services in the country and abroad for all its corporate customers.

Strategically focused on operation with small and medium enterprises and entrepreneurs, we offered them new products, such as micro and fast loans, which belong to the microfinancing group within the sector of small and medium entrepreneurship. I can proudly say that Hrvatska poštanska banka is the first business bank in Croatia which contracted a deal with the European Bank for Reconstruction and Development for a EUR 10 million worth credit line designed for long-term financing of entrepreneurs, especially the micro and small enterprises. Besides this, in terms of the support and development of a quality entrepreneurship, the Bank also entered into cooperation with the Croatian Chamber of Commerce and the Guarantee Agency for Sustainable Development of the Small Entrepreneurship of the Varazdin Region. Furthermore, the Bank made a significant step forward towards the development of cooperation with the local authorities by offering to the town of Makarska, besides financial services and banking products, the knowledge and experience of their banking experts whom it provided as an advisory and business support.

In order to make ourselves more accessible to our customers and thus improve customer satisfaction, we continued extending our operation throughout the Republic of Croatia. We have thus, in cooperation with our strategic partner, Croatian Post, opened six new outlets (in Makarska, Poreč, Split, Zadar, Zaprešić and Zagreb) and are now operating in sixteen outlets, five branches and two representative offices and have a wide network of other distribution channels throughout Croatia.

In 2006, the investment banking sector of Hrvatska poštanska banka developed into an important business segment of the Bank specialised in modern ways of financing, investment and cash management, which was recognised by our customers. During the last year, our investment bankers participated in significant events on the Croatian capital market. The Bank arranged the issue and organised inscription of the successfully conducted re-capitalisation of Viro sugar plant from Virovitica, for which we were also awarded the Golden Share for the contribution to the development of the Croatian capital market.

With HPB Invest and HPB Nekretnine, the first domestic banking group was further strengthened by the foundation of HPB Stambena štedionica. I must point out that HPB Invest continued its successful management of Umirovljenički fond and, in 2006; it conducted a complex process of organisational and technical preparation for payment of the first and the second instalment of amounts to Umirovljenički fond members. Besides, during the last year, HPB Invest founded two new funds - HPB Alpha fond, the first open investment fund with private offer and HPB Dynamic, balanced investment fund - confirming thus the reputation of the company which is outstanding not only in terms of realised results and the quality of asset management, but also in terms of innovation and attractiveness in creation of funds.

We were also simultaneously working on other projects with which we increased the level and the quality of operation. Hrvatska poštanska banka is the first bank from Croatia which became a member of the World Savings Banks Institute (WSBI).

Being aware of the importance of human resources in management and realisation of business activities, together with modern and stable organisational structure which was created at the beginning of the year, we introduced a special system for planning and grading of employee performance. Furthermore, we began introduction of the Balanced Scorecard and implemented Multi-level incentive scheme system.

We will remain truthful to values and goals that we set and started realising during the last two years, being innovation, reliability, high effectiveness and professionalism. The dynamic development of the Croatian market requires daily setup of new and more demanding criteria to which we will aspire, all in scope of fulfilment of the needs of our owners, business partners and customers.

On my own behalf and on behalf of the Management Board and my closest team of colleagues, I would like to thank to our clients and business partners for their confidence and professional relationship, and would like to thank to all employees of Hrvatska poštanska banka on their committed work and diligence with which they contributed to the Bank's success. I would especially like to thank to shareholders and the Supervisory Board members on their cooperation, support and trust.

Josip Protega

President of the Management Board

Macroeconomic movements in the Republic of Croatia in 2006

Macroeconomic stability and economic growth, decrease in growth of public and foreign debt, fiscal consolidation, decrease in unemployment rate, and continuation of negotiations for EU accession, were all the goals of the Croatian economic policy in 2006.

According to projections of the quarterly GDP, the economic growth additionally increased in 2006, compared to 2005 when it amounted to 4.3%. The economic growth was most significant in the first quarter of 2006 when the quarterly rate of increase represented 6.0% compared to the same period in 2005. Total industrial production in 2006 increased by 4.5% compared to 2005. Total nominal retail turnover increased by 4.8% at the end of 2006 (realistically 2.1%) compared to 2005, and individually the largest relative increase in turnover of 16.9% was noted in retail trade in textiles, clothing, footwear and leather products.

Total export of the Republic of Croatia in 2006, according to preliminary information, amounted to USD 10,376 million, and import amounted to USD 21,488 million. Foreign trade deficit amounted to USD 11,112 million while import/export coverage ratio amounted to 48.3%. Direct foreign investments in the Republic of Croatia during the first three quarters of 2006 increased by significant EUR 1.8 billion, i.e. 23.5%, amounting at the end of September to EUR 13.2 billion. Prices of goods and services for personal consumption, measured by consumer prices index, approximately increased by 3.2% in 2006, compared to 2005.

At 2006 year-end, there were 1,426.6 thousand employed and 293.2 thousand unemployed citizens, and the unemployment rate amounted to 17.0%. An average nominal net salary for the first eleven months of 2006 amounted to HRK 4,591, realistically representing an increase of 1.8% compared to the same period last year.

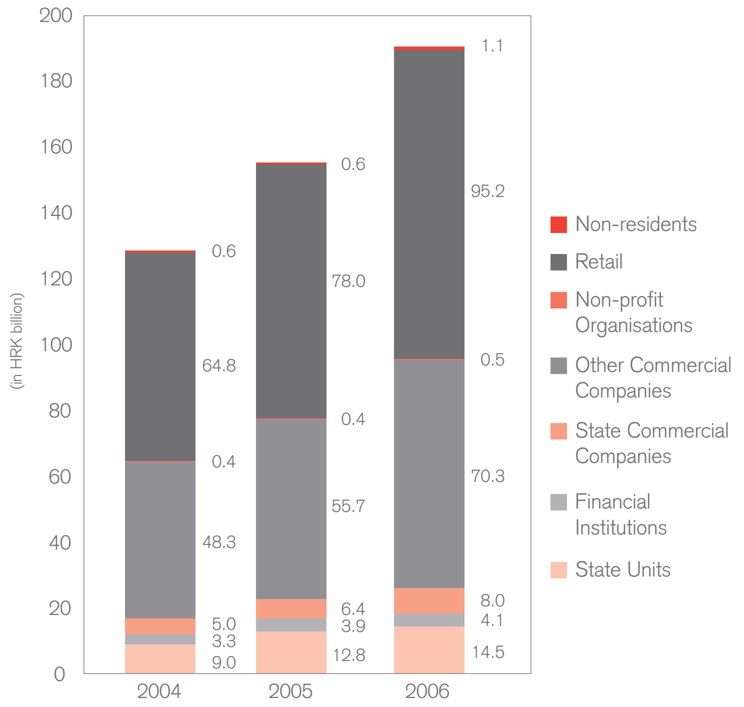
At 2006 year-end, the domestic currency was by 0.41% weaker in relation to EUR, compared to previous year.

In the first 11 months of 2006, the foreign debt increased by EUR 2.76 billion, amounting to EUR 28.3 billion. The increase primarily resulted from the direct indebtedness based on loans provided to other domestic sectors (commercial companies) from abroad.

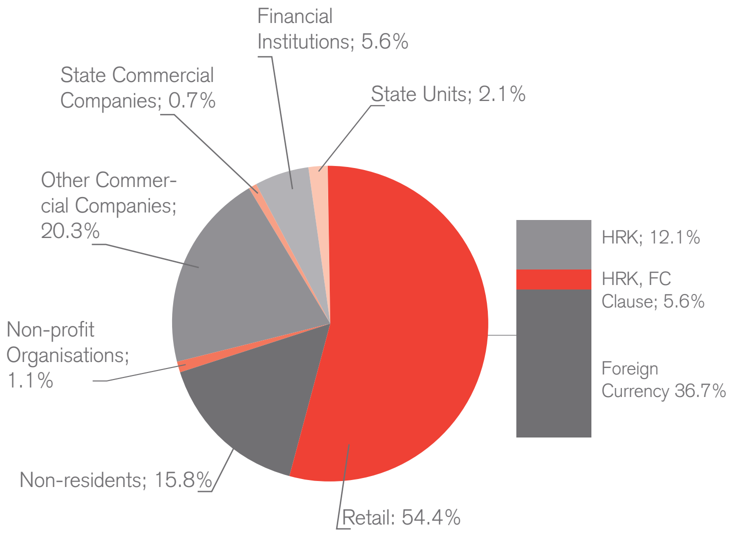
In 2006, Croatian National Bank continued its restrictive monetary policy in scope of limiting the growth of placements and de-stimulating further foreign indebtedness of banks. The main instrument used was the obligatory marginal reserve and a special obligatory reserve on issued securities, according to which 55% of amounts of funds collected from issued securities should be placed on CNB accounts. However, the operation of banks was highly influenced by several amendments of creditworthiness measures. Placements increased by HRK 34.2 billion, i.e. 22.93% compared to 2005, while total liquid assets (M4) increased by HRK 27.8 billion, i.e. 17.98%, in the same period.

The banking system of the Republic of Croatia was stable, liquid and profitable in 2006. According to preliminary information published by the CNB, at 31 December 2006, total assets of banks amounted to HRK 305.1 billion, representing a HRK 44.8 billion, i.e. 17.2% increase compared to 2005. As in the previous year, the increase of the banks' assets mostly resulted from the increase in retail loans in the amount of HRK 17.1 billion and loans to commercial sector in the amount of HRK 16.2 billion. At 2006 year-end, the banking gross loan portfolio comprised 49.2% of retail loans and 36.3% of loans to private commercial companies.

Total gross loan portfolio structure per sectors



Total deposits structure per sectors as at 31/12/2006



The increase in assets of banks was primarily financed from deposits, which increased by HRK 31.2 billion (among which majority were retail term deposits with foreign currency clause), then from balance sheet capital, which increased by HRK 8.1 billion (primarily related to a HRK 5.3 billion or 45.8% increase in share capital of banks), an HRK 4.8 billion increase in borrowings (completely from foreign majority shareholders of the banks) and other.

Total assets of savings institutions at the end of 2006 amounted to HRK 6.2 billion, representing an HRK 308.0 million or 5.3% increase. Housing loans to customers of the savings institutions increased by HRK 720.5 million or 125.2% compared to the previous year, while savings simultaneously increased by HRK 288.9 million or 5.2% (of which 84.2% was collected in December).

Description of the Bank's operation

Hrvatska poštanska banka d.d., Zagreb, was founded and registered as a joint stock company in accordance with applicable regulations of the Republic of Croatia, and is authorised to perform banking activities in the Republic of Croatia. The Bank's Management Board is in Jurišićeva 4, in Zagreb. At 31 December 2006, the Bank operated through two representative offices, five branches and sixteen outlets.

The Bank's main activity is operation in all kinds of deposit and loan activities for corporate and retail customers in domestic and foreign currency, performance of domestic and foreign payment transaction activities, issue of guarantees, sureties and other forms of guarantees, trade in foreign currency and securities and other banking activities.

Hrvatska poštanska banka is recognised as a dominant financial mechanism offered to citizens throughout RH, available through its own network of outlets and post offices, and as a support to Croatian economy, especially in the segment of small and medium entrepreneurship.

As a domestic bank, HPB is in the group of leading banks in the Republic of Croatia, which, with its assets in the amount of HRK 11.3 billion and its share capital, is ranked seventh among 33 banks altogether.

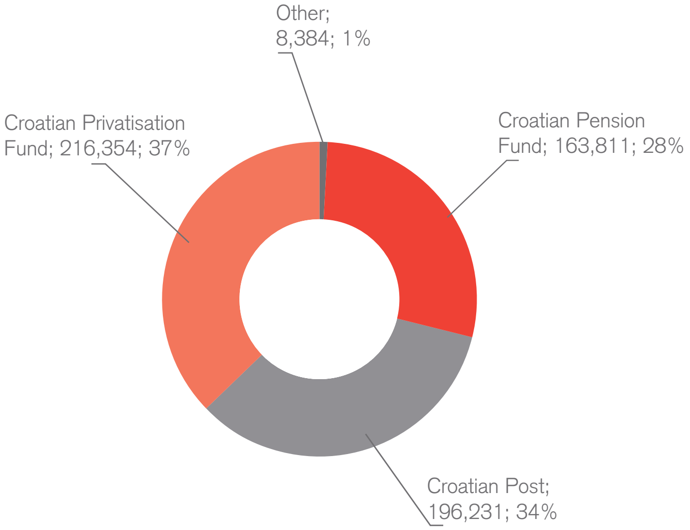
According to currently applicable Payment Transaction Law, Croatian Post is no longer the main payment system distribution channel, but is authorised to perform cash payment transactions on behalf and for Hrvatska poštanska banka, which makes her a participant in cash payment transactions.

In April 2006, the Bank founded HPB Stambena štedionica d.d. which, along with earlier founded HPB Invest d.o.o., the investment fund management company, and HPB Nekretnine d.o.o., the company for real estate and construction, form the HPB Group. All the three companies are fully owned by Hrvatska poštanska banka.

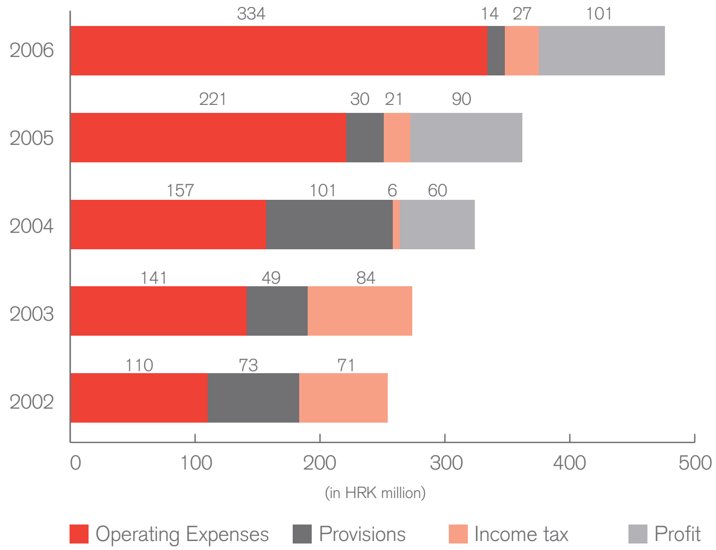
At 31 December 2006, HPB Invest managed six investment funds: HPB Money Market Fund, HPB Bond Fund, HPB Equity Fund, HPB Global Fund, HPB Alpha Fund and HPB Dynamic Fund.

In 2006, the Bank realised HRK 475.7 million profit from operation. The largest part of the income distribution structure were operating expenses (70%) and profit (21%). Operating expenses increased by 52% compared to 2005, while total impairment losses on loans and advances to customers, other assets and provisions for liabilities and charges in 2006 decreased by 54% compared to 2005.

Shareholder structure as at 31 December 2006



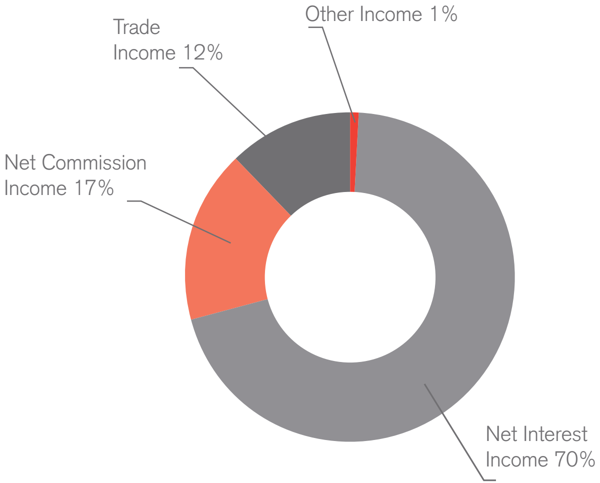
Allocation of Operating Income



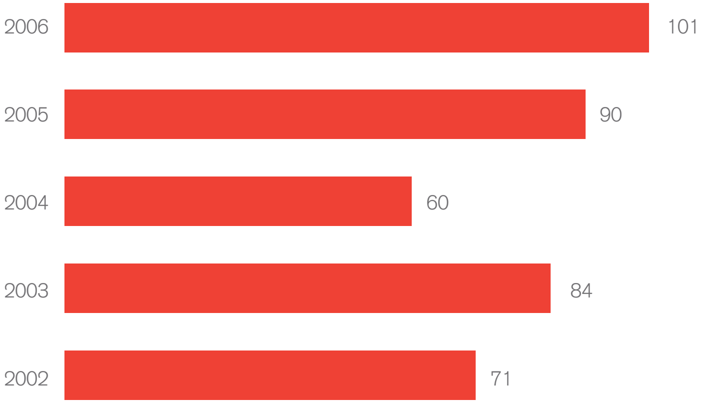
Total operating income increased by 31% compared to 2005. The most significant part of operating income is net interest income, representing 70% of total income.

In 2006 profit for the year amounted to HRK 101.1 million, representing an increase of HRK 11.0 million compared to 2005.

Structure of Operating Income for the Period from 1 January 2006 - 31 December 2006



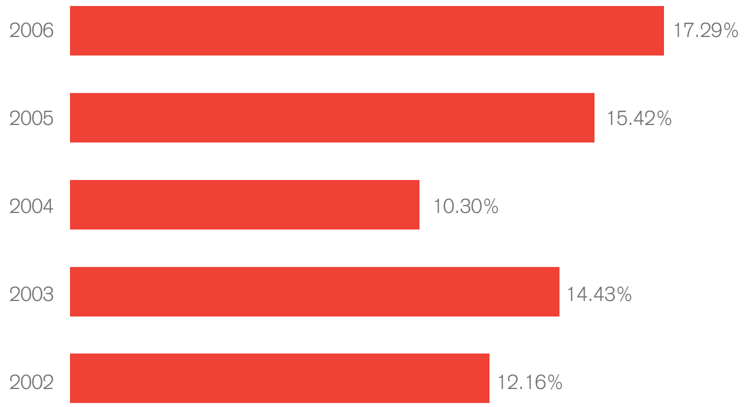
Net Income



(in HRK million)

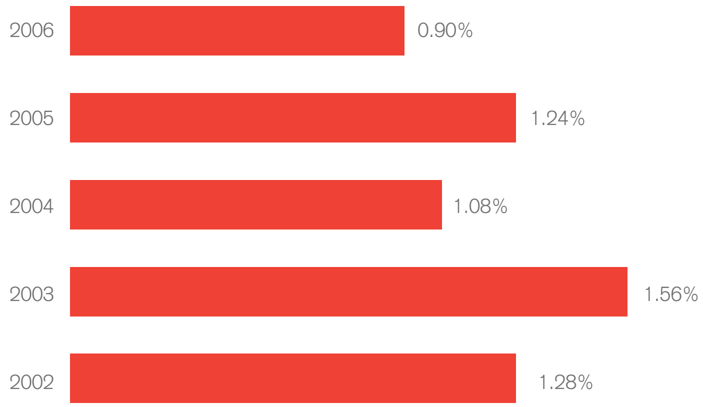
Movement in return on share capital (ROE) and return on assets (ROA) for the period from 2002 to 2006 is presented below.

Return on Share Capital

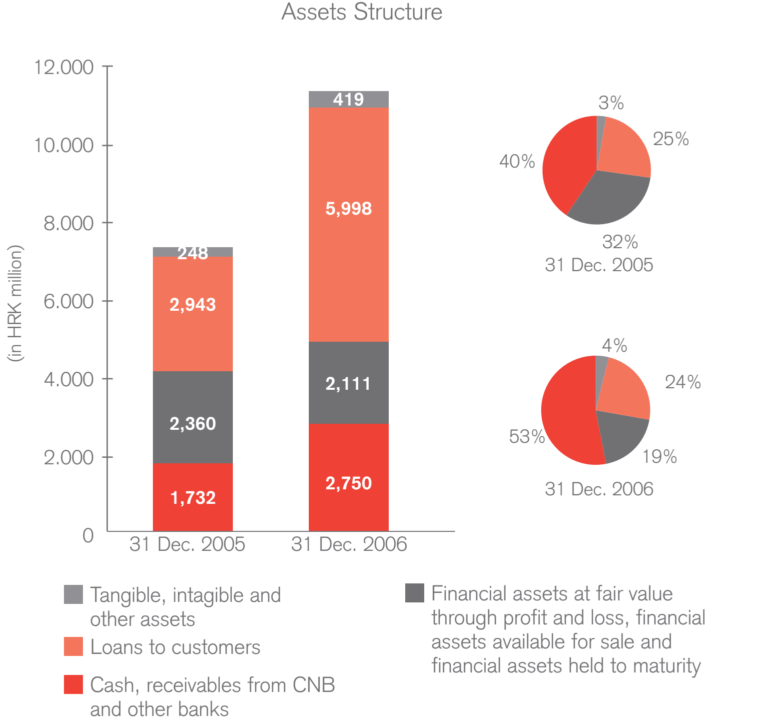


At 2006 year-end, the Bank's assets amounted to HRK 11,278 million, representing an HRK 3,995 million or 55% increase compared to 2005. The most signi-

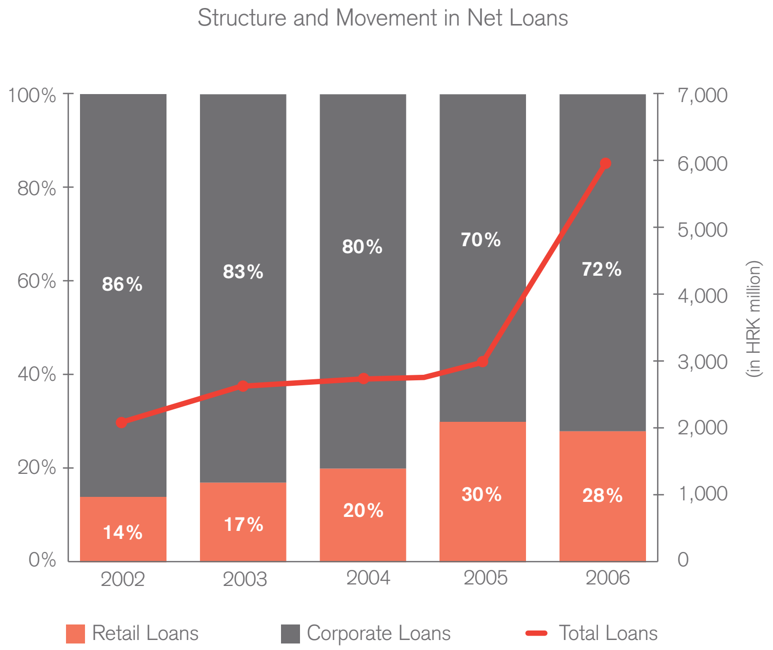
Return on Assets



ficant part within assets structure are loans and advances to customers (53%), financial assets at fair value through profit or loss, placements with and from other banks and the CNB obligatory reserve (35%).



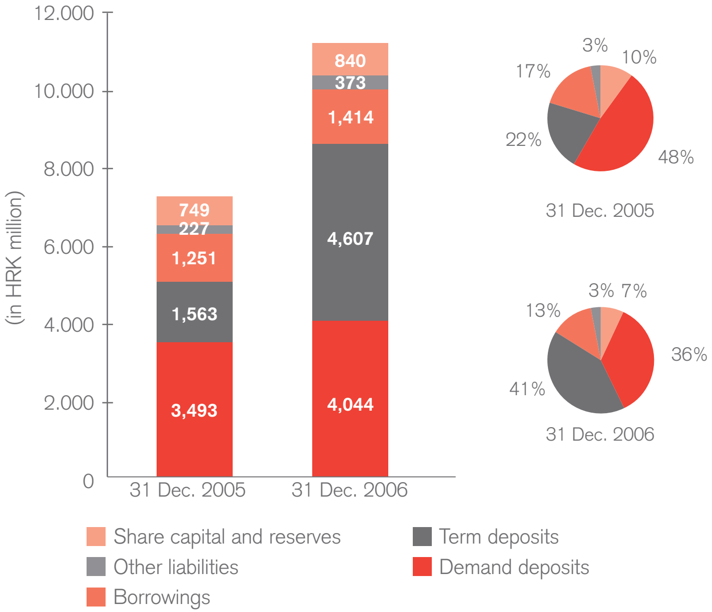
At 31 December 2006, total loans amounted to HRK 5,998 million, representing a 104% increase compared to 2005. The loan portfolio structure comprises 72% of corporate loans and 28% of retail loans.



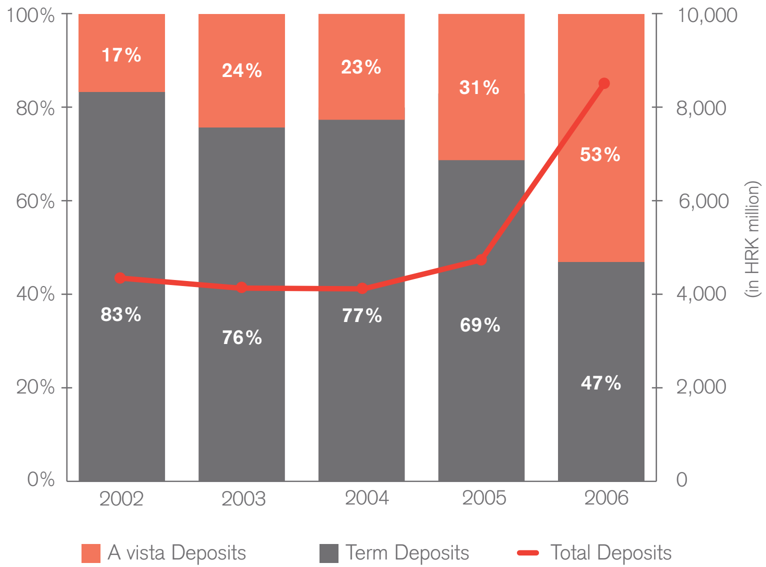
The most significant part within liabilities are term deposits (41%) and demand deposits (36%).

At 2006 year-end, deposits from customers and banks increased by 71% compared to 2005. The structure of deposits is dominated by term deposits (53%), compared to demand deposits (47%). In 2006, term deposits increased by 195%, and their share within the structure of total deposits increased from 31% to 53%. The Bank will continue its activities aimed at increasing deposits and improving maturity and foreign currency structure of term deposits, in scope of increasing long-term and foreign currency deposits.

Liabilities Structure



Structure and Movement in Deposits



Retail operation

HPB performs retail operation through it own business network which comprises 5 branches and 16 outlets, and through more than 1,100 post offices throughout the territory of the Republic of Croatia.

In accordance with its development strategy aimed at better acquainting customers with its products and services, in 2006, besides its existing 10 outlets, the Bank opened new outlets in Makarska, Poreč, Split, Zadar, Zaprešić and Zagreb and a representative office in Zadar.

Besides its outlet network expansion, HPB continued to develop and improve direct banking distribution channels and installed 28 new ATMs and 134 EFTPOS terminals. At the end of 2006, the Bank had its own network of 165 ATMs and 1.049 EFTPOS terminals, and contracted use of 372 EFTPOS terminals in the Financial Agency.

In scope of developing and improving the relationship with its retail customers, in 2006 the Bank expanded its palette of loans, savings and credit card products and offered Internet banking services.

Retail deposits represent 38.7% of the total deposit structure, representing an increase of 49.8% in 2006 and amounting to HRK 3.3 billion at 31 December 2006. Demand deposits amounted to HRK 2.0 billion, representing an increase of 37.7%, and term deposits amounted to HRK 1.3 billion, representing an increase of 71.5%. Higher growth in term deposits as compared to a vista deposits results from the expansion of the Bank's business network, improvement of business co-operation with Croatian Post, and a stimulative interest rate policy for longer term and foreign currency savings.

In 2006, total gross retail loan portfolio increased by 81.7%, amounting to HRK 1.7 billion at 31 December 2006. In 2006, 22,189 retail loans totalling HRK 890 million were granted. Retail loans represented 27.6% of total gross loans portfolio. The largest part of total retail loan portfolio are non-purpose loans, followed by used frame facilities on current accounts.

Among other activities within retail operation we point out the continuation of the improvement of business cooperation with Croatian Post, Financial Agency and other state institutions, especially in the field of payment of various fees, incentives from state budget and approval of loans on the basis of operation for and on behalf of third parties.

Corporate operation

In 2006, the Bank primarily focused its credit activity on loans to commercial companies. Consequently, gross loans to commercial companies increased by 77.5% or HRK 1.7 billion. The structure of loans is dominated by long-term loans which represent 40.4% of total placements.

The structure of loans for operation for and on behalf of third parties amounts to HRK 194.1 million, and activities were performed for 22 third parties.

During 2006, loans to large enterprises were dominated by loans to export oriented industry, civil engineering, housing construction in urban centres, shipbuilding with state guarantees and loans to small and medium entrepreneurship. In granting long-term loans, HBOR resources and own long-term resources were used.

The Bank significantly increased its loan granting activities to small and medium entrepreneurship, offering, among other things, two new products - micro and fast loans - which will be financed from the borrowing granted by the European Bank for the Reconstruction and Development. Except financing, this arrangement also includes introduction of the best banking practice in granting loans to small and medium entrepreneurship, which will additionally improve the quality of service and allow the entrepreneurs to save time and money. The Bank also continued its cooperation with institutions providing support to small and medium entrepreneurship (HAMAG, USAID), the Croatian Bank for Reconstruction and Development, the Ministry of Economy, Labour and Entrepreneurship, the Ministry of Sea, Tourism, Traffic and Development and towns, municipalities and counties in the Republic of Croatia. It all influenced on the increase in the share of loans to small and medium entrepreneurship within total loans portfolio.

The improvement of customer relationship and increase in corporate business activities was significantly influenced by the introduction of Internet banking.

At 31 December 2006, total corporate deposits amounted to HRK 4.8 billion, representing an HRK 2.0 billion or 73.5% increase compared to the previous year, whereby term deposits increased by 283.0%.

Investment banking

During 2006, the Investment Banking Division significantly extended the scope of its operation as an agent in trade of securities on the domestic as well as on regional financial markets. Among other things, the Bank offered services of trading securities on the financial market of Bosnia and Herzegovina. Last year, the Bank extended its business cooperation related to use of margin loans by contracting business with eight new brokers. Consequently, margin loans can be used by the clients of 13 leading brokers in Croatia and the clients of the Bank. The stated activities resulted in HRK 173.8 million of granted margin loans.

The Bank's realised annual turnover on both the domestic stock markets amounted to HRK 986.8 million, while the annual turnover on regional financial markets (Monte Negro, Macedonia and Bosnia and Herzegovina) amounted to HRK 238.8 million.

Business activities of the Investment Banking Sector, besides securities operation, are more frequently focused on strategic advisory regarding mergers and takeovers, organised employee shareholding, re-investment of dividends, bonus issue of shares, squeeze-out procedures, etc.

In 2006, the project of issue of shares based on initial public offer of Viro d.d., a sugar plant from Virovitica and the first joint stock company in Croatia that issued its shares by a public offer through Zagrebačka burza. Total value of the issue of shares amounted to HRK 125.6 million, sold in a record 18 seconds. For that project, HPB was awarded the Golden Share for its contribution to the development of the Croatian share capital market.

Treasury operation

In 2006, the Bank intensified its active role on the money market, increasing the volume and the number of transactions with domestic and foreign financial institutions.

The Bank's membership in the group of banks that form ZIBOR strengthened the position of the Croatian market maker. The number of repurchase transactions and short term securities transactions, especially with investment funds, was significantly increased.

Even in 2006, the Bank was one of the leaders according to total number of underwritten treasury bills of the Ministry of Finance of the RH.

The Bank intensified its operation in long-term debt securities and derivatives in scope of hedging the fixed income portfolio, and increased the portfolio of state and corporate bonds by daily quotation of price for bonds quoted on Croatian market. The Bank arranged the issue of the RH Croatian Ministry of Finance bonds during 2006.

The Treasury division successfully ensured the liquidity required for the continuing operation of the Bank and their customers and continued improving the Bank's liquidity risk management by implementing new internal acts and retaining the necessary liquidity reserves in accordance with regulations and the Bank's internal acts.

By forming the Treasury Products Sales Department, the Treasury division enabled a higher quality and faster contracting of foreign currency and money market transactions to the Bank's clients.

The Bank continued improving existing operation policies and procedures regulating the Treasury division operation, which enabled the formation of a trading portfolio of securities and the development of new products.

Risk management

The Bank's willingness to take the risk in daily operation represents a necessary precondition to the realisation of a positive financial result. Within Hrvatska poštanska banka, risk management represents the function that comprises evaluation and measurement of risk exposure, quantification of risk appetite through the system of limits, reporting and supervision of limit utilisation and corrective activities, all in scope of reducing the positions within prescribed limits.

Strategic risk management guidance and the definition of the limit of acceptable risk is achieved through the Management Board, Credit Committee and Asset and Liabilities Management Committee operation.

The Risk Management Division is responsible for independent assessment and measurement of risk exposure which is a precondition to quantification of acceptable risk exposure through the system of limits. In their operation, the Bank's business divisions implement risk management decisions of the authorised bodies and maintain positions within prescribed limits.

In scope of realising a positive business result, the Bank creates exposure to credit risks, market risks and structure risks (liquidity risk and interest rate risk in the balance sheet part which is not stated at fair value) and, as a consequence, an exposure to operating risk is created.

Credit risks

The Bank estimates recoverability, that is, a potential loss on each placement, before approval of placements, and periodically (quarterly) during the period of the business relationship. A conservative approach to credit risk management is characterised by strict obedience of regulatory requirements, impairments made against losses arising from credit risk and maintenance of a capital adequacy rate higher than the prescribed minimum (10%).

Market risks

The Bank is exposed to market risks on positions which are stated at fair value - financial assets at fair value through profit or loss and foreign currency position. In managing market risks, the Bank is fully compliant with regulatory requirements and Croatian National Bank decisions. The Bank develops a market risk management system which is based on Value at Risk principles, i.e. exposure to market risks is disclosed in terms of a potential loss (for a certain time period, with a certain statistical reliability).

The Bank's balance sheet structure risks

In managing structure risks, the Bank pays special attention to liquidity risk and interest rate risk in the part of the balance sheet which is not measured at fair value.

Liquidity risk management is based on maintenance of necessary liquidity reserves, compliance with structure limits and prescribed steps in case of occurrence of liquidity crisis.

In managing interest rate risk, the Bank determines the acceptable exposure in terms of sensitivity of net interest income (income perspective) and sensitivity of economic value of capital (economic value perspective).

Operating risks

The Bank determines its operating risk exposure in compliance with regulatory requirements and Croatian National Bank decisions and guidance of the New Basel Accord on Capital Adequacy (Basel II). In managing operating risk, the Bank implements quantitative and qualitative measures that are based on the collection of information on losses arising from operating risk, independent risk assessment and the control system.

Future activities

Future activities in the field of risk management development will be focused on adjustment with provision of the European Union Directive on Capital Requirements, that is, on the formation of a management function which will ensure that the total risk exposure be in accordance with available capital.

Internal controls system and internal audit

The Bank's internal acts comprise internal control system principles. Internal controls are the responsibility of management and individuals in charge of internal control.

All employees are responsible for implementation of internal controls, and implementation procedures are provided in the descriptions of tasks, procedures and guidance.

An adequate implementation of the internal control system hedges the Bank's exposure to risks and ensures timely information through an early warning on increased risk exposure system.

The internal control system is based on four principles:

- clear definition of responsibilities
- separation of duties and activities
- integrated control proceedings
- effective internal audit

In accordance with internal control principles, the internal audit was organised as an independent function which directly reports to the Management and Supervisory Boards of the Bank.

In 2006, the Bank's and the Group members' audit committees were formed.

The audit of all the organisational parts and functions of the Bank and the Group members is performed on the basis on the annual operating programme and quarterly operating plans.

The audit is performed in accordance with general internal audit standards and regulatory requirements, in four following steps:

- planning
- research
- reporting
- results monitoring

Report on audit results, which contains conclusions and recommendations, is submitted to the Bank's Management Board, Audit Committees and the Supervisory Board.

Management of the Bank

In accordance with the Companies' Act and the Bank's statute, the management of the Bank comprises the Supervisory Board and the Management Board.

The Supervisory Board

The Supervisory Board supervises the operation of the Bank's Management Board. The Supervisory Board consists of seven members which are elected at the General Assembly by a regular majority of the total number of votes. The members have a four year mandate and can be re-elected. The Supervisory Board decisions are passed by the majority of the total number of votes, of which each Supervisory Board member has one vote.

The Supervisory Board reports to the General Assembly on the performed supervision of business management in which it specifically states: if the Bank operates in accordance with laws, the company's acts and the Bank's General Assembly decision; if the annual financial statements have been prepared in compliance with information disclosed in the Bank's records and if they give a true financial and operating position of the Bank, and the opinion on the Management Board's proposal related to allocation of profit and coverage of loss.

In accordance with the law, the Supervisory Board members receive fees for their work, in the amount determined at the General Assembly of the Bank, for the business year in which fees will be paid.

The President of the General Assembly is mr. sc. Ante Žigman.

The Supervisory Board members in 2006 were:

mr.sc. Ante Žigman	President	
prof.dr.sc. Dragan Kovačević	Vice President	
dr.sc. Zoran Bubaš	Member	until 12/05/2006
Jadranko Mijalić	Member	
dr.sc. Miro Kovač	Member	from 30/10/2006
mr.sc. Grga Ivezić	Member	
Vera Babić	Member	
prof.dr.sc. Drago Jakovčević	Member	

The Management Board

The Management Board is responsible for the successful operation of the Bank. It consists of two members responsible for individual business areas.

The Management Board represents the Bank and it is responsible and authorised to initiate all actions of representation in court or with other state authorities.

Individuals who are appointed candidates for the position of the president and members of the Management Board must fulfil all requirements prescribed by law and other regulations. Upon each appointment of the president or the members of the Management Board, the Supervisory Board must request a prior consent form the Croatian National Bank. The Management Board members are appointed by the Supervisory Board for the five-year period, with a possibility of re-election.

The Bank's Management Board members in 2006 were:

Josip Protega	President
Ivan Sladonja	Member

SUPERVISORY BOARD

MANAGEMENT BOARD

President of the Management Board
Josip Protega

Member of the Management Board
Ivan Sladonja

INTERNAL AUDIT OFFICE
Executive Director
Miroslav Marić

- Executive Committee
- Credit Committee
- Assets and Liabilities Management Committee
- Amendments and Adjustments Management Committee
- Strategy Implementation Committee
- Profession Committee

OFFICE OF THE CHIEF FINANCIAL OFFICER
Chief Financial Officer
Marijo Kirinić

MANAGMENT BOARD OFFICE
Head of Office
Vinko Hrkać

- Investment Funds Management Company
- Housing Savings Bank
- Real Estate Management Company

STRATEGY OFFICE
Senior Executive Director
Ana Klarić

CORPORATE COMMUNICATIONS OFFICE
Director
Ivana Koludrović

PROJECT MANAGEMENT OFFICE
Senior Executive Director
Saša Stanković

REGULATORY LEGAL AFFAIRS OFFICE
Executive Director
Mladen Šunjić

CORPORATE SECURITY OFFICE
Director
Đuro Črnjak

HUMAN RESOURCES MANAGEMENT OFFICE
Executive Director
Predrag Grubišić

RISK MANAGEMENT DIVISION
Executive Director
Zoran Sikora

ACCOUNTING AND FINANCIAL CONTROLLING DIVISION
Executive Director
Zlatko Držanić

DEPARTMENT OF ECONOMIC ANALYSIS AND RESEARCH
Director
Mladen Mirko Tepuš

MONEY LAUDERING PREVENTION DEPARTMENT
Director
Snježana Rajaković-Vignjević

MIDDLE OFFICE
Director
Marko Reljić

LEGAL AFFAIRS DIVISION
Executive Director
Bosiljka Grbašić

INFORMATION TECHNOLOGY DIVISION
Executive Director
Darko Maljić

PROCUREMENT AND GENERAL SERVICES DIVISION
Executive Director
Gordan Milinić

OPERATIONAL AFFAIRS DIVISION
Senior Executive Director
Josip Ivančić

DIRECT BANKING DIVISION

BANK GROUP COORDINATION DEPARTMENT

MARKETING AND SALES DIVISION
Executive Director
Franjo Sinković

BUSINESS NETWORK MANAGEMENT DIVISION
Executive Director
Igor Lukačić

RETAIL BANKING DIVISION
Senior Executive Director
Mato Filipović

CORPORATE BANKING DIVISION
Senior Executive Director
Zdenko Perković

INVESTMENT BANKING DIVISION
Executive Director
Marinko Papuga

TREASURY DIVISION
Executive Director
Dubravka Kolarić

HRVATSKA POŠTANSKA BANKA **HPB** HRVATSKA POŠTANSKA BANKA

WWW.HPB.HR

Hrvatska poštanska banka d.d. (Croatian Post Bank) Zagreb was established in October 1991 as a bank organization for conducting of all types of banking operations in the country and abroad. Until the beginning of the year of 2001 the founder and majority owner was HPT, later Hrvatska pošta d.d. which, starting from good business practice of post banks in Europe, has continued through the newly established bank, the mission of the traditional post post-office savings banks founded in Croatia in 1883. Since the beginning of 2001 the Republic of Croatia has been, through funds and companies owned by the state, the majority owner of the shares of Hrvatska poštanska banka.

• JURIŠIĆEVA 4, ZAGREB •

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ANNUAL REPORT 2006

CONTENTS

Financial statements and Independent Auditors' Report

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

The Management Board is required to prepare consolidated and unconsolidated financial statements for each financial year which give a true and fair view of the financial position of the Bank and of the results of its 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 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; make judgements and estimates that are reasonable and prudent; and prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Bank will continue in business.

The Management Board is responsible for the submission to the Supervisory Board of its annual report on the Bank together with the annual financial statements, following which the Supervisory Board is required to approve the annual financial statements for submission to the General Assembly of Shareholders for adoption.

The unconsolidated financial statements set out on pages 40 to 144 were authorised by the Management Board on 28 February 2007 for issue to the Supervisory Board and are signed below to signify this.

On behalf of Hrvatska poštanska banka d.d.

Josip Protega	Ivan Sladonja
President of the Management Board	Member of the Management Board

Independent Auditors' Report to the Shareholders of Hrvatska poštanska banka d.d.

We have audited the accompanying unconsolidated financial statements of Hrvatska poštanska banka d.d. ("the Bank"), which comprise the balance sheet as at 31 December 2006 and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the unconsolidated financial statements give a true and fair view of the financial position of the Bank as at 31 December 2006, and of its financial performance and its cash flows for the year then ended in accordance with the statutory accounting requirements for banks in Croatia.

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

28 February 2007

For and on behalf of KPMG Croatia d.o.o. za reviziju:

Ismet Kamal
Director

Ivana Matovina
Croatian Certified Auditor

Unconsolidated balance sheet
As at 31 December 2006

ASSETS	Notes	2006 HRK '000	2005 HRK '000
Cash and receivables from banks	5	579,714	388,689
Obligatory reserve with Croatian National Bank	6	1,026,742	685,366
Placements with and loans to other banks	7	1,143,336	657,465
Financial assets at fair value through profit or loss	8	1,810,616	1,438,500
Financial assets available for sale	9	299,674	921,660
Financial assets held to maturity	10	150	-
Loans and advances to customers	11	5,998,224	2,942,889
Investments in subsidiaries	12	35,050	5,050
Property, plant and equipment	13	172,288	157,331
Intangible assets	14	71,783	19,837
Net deferred tax asset	15	9,669	2,694
Other assets	16	130,607	63,445
TOTAL ASSETS		**11,277,853**	**7,282,926**

LIABILITIES	Notes	2006 HRK '000	2005 HRK '000
Financial liabilities at fair value through profit and loss	17	583	-
Deposits from banks	18	496,658	50,940
Deposits from customers	19	8,153,941	5,004,946
Borrowings	20	1,413,682	1,250,444
Provisions for liabilities and charges	21	26,030	22,791
Other liabilities	22	334,708	182,690
Current tax liability		12,169	21,688
TOTAL LIABILITIES		**10,437,771**	**6,533,499**
EQUITY			
Share capital	34	584,780	584,780
Treasury shares	34	(874)	(874)
Statutory reserve	34	12,776	7,720
General banking reserve	34	91,072	31,609
Fair value reserve		(222)	10,248
Retained earnings		152,550	115,944
TOTAL EQUITY		**840,082**	**749,427**
TOTAL LIABILITIES AND EQUITY		**11,277,853**	**7,282,926**

The significant accounting policies and other notes on pages 51 to 144 form an integral part of these unconsolidated financial statements.

Unconsolidated income statement
For the year ended 31 December 2006

	Notes	2006 HRK '000	2005 HRK '000
Interest and similar income	23	513,336	351,397
Interest expense and similar charges	24	(180,562)	(102,924)
Net interest income		**332,774**	**248,473**
Fee and commission income	25	554,655	558,805
Fee and commission charges	26	(473,731)	(498,033)
Net fee and commission income		**80,924**	**60,772**
Gains less losses arising from dealing securities	27	25,043	16,728
Gains less losses arising from investment securities	28	12,603	9,462
Gains less losses arising from dealing in foreign currencies		20,460	18,230
Other operating income	29	3,877	8,296
Dealing and other income		**61,983**	**52,716**
Operating income		**475,681**	**361,961**

	Notes	2006 HRK '000	2005 HRK '000
General and administrative expenses	30	(300,100)	(196,102)
Depreciation and amortisation	13, 14	(34,144)	(24,455)
Impairment losses on loans and advances to customers and other assets	31	(10,631)	(19,331)
Provisions for liabilities and charges	21	(3,316)	(11,195)
Operating expenses		**(348,191)**	**(251,083)**
PROFIT BEFORE TAX		**127,490**	**110,878**
Income tax expense	32	(26,365)	(20,716)
PROFIT FOR THE YEAR		**101,125**	**90,162**
Earnings per share (in HRK)	33	**190.51**	**169.85**

The significant accounting policies and other notes on pages 51 to 144 form an integral part of these unconsolidated financial statements.

Unconsolidated statement of changes in equity
For the year ended 31 December 2006

	Share capital HRK '000	Treasury shares HRK '000	Statutory reserve HRK '000	General banking reserve HRK '000	Fair value reserve HRK '000	Retained earnings HRK '000	Total HRK '000
Balance at 1 January 2005 (restated)	**584,780**	**(874)**	**3,212**	**-**	**7,036**	**61,899**	**656,053**
Unrealised gains on financial assets available for sale	-	-	-	-	13,477	-	13,477
Realised gains on financial assets available for sale	-	-	-	-	(9,462)	-	(9,462)
Deferred tax	-	-	-	-	(803)	-	(803)
Net gains not recognised in the income statement	-	-	-	-	*3,212*	-	*3,212*
Profit for the year	-	-	-	-	-	90,162	90,162
Total recognised income for 2005	-	-	-	-	*3,212*	*90,162*	*93,374*
Transfer to statutory reserve	-	-	4,508	-	-	(4,508)	-
Transfer to general banking reserve	-	-	-	31,609	-	(31,609)	-
Balance at 31 December 2005	**584,780**	**(874)**	**7,720**	**31,609**	**10,248**	**115,944**	**749,427**
Balance at 1 January 2006	**584,780**	**(874)**	**7,720**	**31,609**	**10,248**	**115,944**	**749,427**

	Share capital HRK '000	Treasury shares HRK '000	Statutory reserve HRK '000	General banking reserve HRK '000	Fair value reserve HRK '000	Retained earnings HRK '000	Total HRK '000
Unrealised loss on financial assets available for sale	-	-	-	-	(484)	-	(484)
Realised gains on financial assets available for sale	-	-	-	-	(12,603)	-	(12,603)
Deferred tax	-	-	-	-	2,617	-	2,617
Net losses not recognised in the income statement	-	-	-	-	*(10,470)*	-	*(10,470)*
Profit for the year	-	-	-	-	-	101,125	101,125
Total recognised income for 2006	-	-	-	-	*(10,470)*	*101,125*	*90,655*
Transfer to statutory reserve	-	-	5,056	-	-	(5,056)	-
Transfer to general banking reserve	-	-	-	59,463	-	(59,463)	-
Balance at 31 December 2006	**584,780**	**(874)**	**12,776**	**91,072**	**(222)**	**152,550**	**840,082**

The significant accounting policies and other notes on pages 51 to 144 form an integral part of these unconsolidated financial statements.

Unconsolidated statement of cash flows
For the year ended 31 December 2006

	Notes	2006 HRK '000	2005 HRK '000
Cash flows from operating activities			
Profit before tax		127,490	110,878
Adjustment for:			
- Depreciation and amortisation	13, 14	34,144	24,455
- Disposal of property, plant and equipment	13	-	11
- Foreign exchange losses/(gains)	30, 29	6,554	(266)
- Impairment losses on loans and advances to customers and other assets	31	10,631	19,331
- Impairment losses on provisions for liabilities and charges	21	3,316	11,195
- Net gains on financial assets at fair value through profit or loss	27	(21,179)	(9,000)
Changes in operating assets and liabilities			
Increase in placements and loans to other banks		(64,975)	(131,254)
Increase in financial assets at fair value through profit or loss		(351,711)	(1,312,832)
Net increase in loans and advances to customers		(3,082,219)	(385,891)
Net increase in other assets		(58,955)	(20,126)
Net increase in deposits from banks		454,610	5,114
Net increase in deposits from customers		3,269,558	775,188
Net increase in other liabilities		124,893	17,478
Net cash inflow/(outflow) from operating activities before tax		**452,157**	**(895,719)**

	Notes	2006 HRK ‘000	2005 HRK ‘000
Interest paid		(112,279)	(70,849)
Income tax paid		(18,554)	(3,932)
Net cash inflow/(outflow) from operating activities		**321,324**	**(970,500)**
Cash flow from investing activities			
Interest received		35,135	44,172
Investment in subsidiaries		(30,000)	(5,050)
Purchase of property, plant and equipment and intangible assets		(101,047)	(49,725)
Disposal of financial assets available for sale		817,028	1,234,608
Acquisition of financial assets available for sale		(231,000)	(970,788)
Acquisition of financial assets held to maturity		(160)	-
Net cash inflow/(outflow) from investing activities		**489,956**	**253,217**
Cash flow from financing activities			
Interest paid		(31,462)	(14,367)
Increase in borrowings		5,258,122	11,635,118
Repayment of borrowings		(5,062,372)	(10,718,942)
Net cash inflow from financing activities		**164,288**	**901,809**
Effect of foreign exchange differences on cash and cash equivalents		(7,566)	(7,662)
Net increase in cash and cash equivalents		**968,002**	**176,864**
Cash and cash equivalents at the beginning of the year	36	**1,602,127**	**1,425,263**
Cash and cash equivalents at the end of the year	36	**2,570,129**	**1,602,127**

The significant accounting policies and other notes on pages 51 to 144 form an integral part of these unconsolidated financial statements.

Notes to the unconsolidated financial statements

1. SIGNIFICANT ACCOUNTING POLICIES

Hrvatska poštanska banka d.d. Zagreb ("the Bank") is a joint stock company incorporated and domiciled in Croatia. The address of the Bank's registrated office is Jurišićeva 4, Zagreb. The Bank is involved in corporate, retail, treasury and investment banking operations. These financial statements are the separate financial statements of the Bank as defined in International Accounting Standard 27 "Consolidated and separate financial statements". The Bank is the parent of the HPB Group and also publishes, as a separate document, consolidated financial statements comprising the Bank and its subsidiaries.

These financial statements were authorised for issue by the Management Board on 28 February 2007 for approval by the Supervisory Board.

The principal accounting policies applied in the preparation of these financial statements are summarised below. Where specific accounting policies are aligned with accounting principles set out in International Financial Reporting Standards, reference may be made to certain Standards in describing the accounting policies of the Bank; unless otherwise stated, these references are to Standards applicable at 31 December 2006.

a) Statement of compliance

The financial statements have been prepared in accordance with statutory accounting requirements for banks in Croatia. The Bank's operations are subject to the Banking Law, in accordance with which the Bank's financial reporting is regulated by Croatian National Bank ("the CNB") which is the central monitoring institution of the banking system in Croatia. These financial statements have been prepared in accordance with these banking regulations.

The accounting regulations of the CNB are based on International Financial Reporting Standards. The principal differences between the accounting regulations of the CNB and recognition and measurement requirements of International Financial Reporting Standards are as follows:

- The CNB requires banks to recognise impairment losses, in income, on assets not identified as impaired (including sovereign risk assets) at prescribed rates (excluding assets carried at fair value). The Bank has made portfolio based provisions of HRK 103,281 thousand (2005: HRK 64,524 thousand) in compliance with these regulations and has recognised a charge against income in respect of such provisions of HRK 38,757 thousand as an expense within the charge for impairment losses for the year (2005: income of HRK 1,052 thousand). Although, in accordance with International Financial Reporting Standards, such provisions should more properly be presented as an appropriation within equity, the Bank continues to recognise such provisions in income as a substitute for unidentified impairment losses calculated in accordance with the requirements of International Financial Reporting Standards. In the absence of reliable historical data on the extent of unidentified losses existing in its credit portfolios and the emergence period over which these losses come to light, the Bank is not yet able to estimate provisions for unidentified losses existing at the balance sheet date on the basis required by International Financial Reporting Standards.

- Although the Bank calculates impairment losses on corporate lending as the present value of the expected future cash flows, discounted at the instrument's original effective interest rate, in accordance with International Financial Reporting Standards, the CNB requires the amortization of the discount calculated to be presented in the income statement within the movement on impairment losses on loans and advances to customers and other assets, rather than as interest income, as required by International Financial Reporting Standards.
- In addition, the CNB prescribes minimum levels of provisions against certain specifically identified impaired exposures which may be different from the impairment loss required to be recognised in accordance with International Financial Reporting Standards. At 31 December 2006 there were no such placements.

b) Basis of preparation

The financial statements are prepared on the fair value basis for derivative financial instruments, financial assets and liabilities at fair value through profit or loss, and 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.

The financial statements have been prepared in a format generally adopted and internationally recognised by banks.

In preparing the financial statements, management has made judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities and disclosure of commitments and contingencies at the balance sheet date, as well as amounts of income and expense for the period. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances and information available at the date of the preparation of the financial statements, the result of which form the basis of making the judgements about carrying amounts of assets and liabilities that are not readily apparent from other sources. 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.

Judgements made by management in the application of applicable standards that have significant effects on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in Note 3.

The accounting policies have been consistently applied to all periods presented in these financial statements.

c) Standards, interpretations and amendments to published standards that are not yet effective

Certain regulations have been issued by the CNB as of the date on which these financial statements were authorised for issue, which were not effective at the balance sheet date, but which will be mandatory for accounting periods beginning on or after 1 January 2007. The Bank considers that the following regulation may have a significant impact on the financial statements or otherwise have a significant financial impact on its operations.

- In order to regulate the growth of banking assets, the CNB has issued a decision which requires banks to acquire mandatory CNB treasury bills should they report growth in customer credit risk exposures (on- and off- balance-sheet) in 2007 of more than 12% per annum, measured from the position at 31 December 2006. The CNB treasury bills will be required to be purchased at an amount equivalent to 50% of the excess over the threshold. Such bills have a maturity of 360 days and earn interest at the rate payable on kuna obligatory reserves, which was 0.75% per annum as at 31 December 2006. The decision became effective from 28 February 2007.

The Bank also expects that, in the ordinary course of updating its accounting regulations, the CNB may have regard to the following Standards and Interpretations issued by the International Accounting Standards Board and its International Financial Reporting Interpretations Committee, which were in issue as of the date at which these financial statements have been authorised for issue, but which are applicable to entities reporting under IFRS in periods commencing after 31 December 2006, and which may have an impact on the Bank, if adopted:

- IFRS 7, Financial Instruments: Disclosures, and a complementary amendment to IAS 1, Presentation of Financial Statements - Capital Disclosures (effective from 1 January 2007). IFRS 7 introduces new disclosures to improve the information about financial instruments. It requires the disclosure of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk, including sensitivity analysis to market risk. It replaces IAS 30, Disclosures in the Financial Statements of Banks and Similar Financial Institutions, and disclosure requirements in IAS 32, Financial Instruments: Disclosure and Presentation. It is applicable to all entities that report under IFRS. The amendment to IAS 1 introduces disclosures about the level of an entity's capital and how it manages capital. Management is currently assessing the impact of IFRS 7 and amendment to IAS 1 on the Bank operations.

- IFRS 8, Operating Segments (effective from 1 January 2009). The Standard requires segment disclosure based on the components of the entity that management monitors in making decisions about operating matters. Operating segments are components of an entity about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. Management is currently assessing the impact of IFRS 8 on the presentation and disclosure of its operating segments.

- IFRIC 9, Reassessment of Embedded Derivatives (effective for annual periods beginning on or after 1 June 2006). The Interpretation requires that a reassessment of whether an embedded derivative should be separated from the underlying host contract should be made only when there are changes in the terms of the contract that significantly modify the cash flows that otherwise would be required under the contract. The Bank has not yet completed its analysis of the impact of the new Interpretation.

- IFRIC 10, Interim Financial Reporting and Impairment (effective for annual periods beginning on or after 1 November 2006). The Interpretation prohibits the reversal of an impairment loss recognised in a previous interim period in respect of goodwill, investments in equity instruments or financial assets carried at cost. The Bank does not expect the Interpretation to have any impact on the financial statements.
- IFRIC 11, IFRS 2 - Bank and Treasury Share Transactions (effective for annual periods beginning on or after 1 March 2007). The Interpretation requires a share-based payment arrangement in which an entity receives goods or services as consideration for its own equity-instruments to be accounted for as an equity-settled share-based payment transaction, regardless of how the equity instruments needed are obtained. It also provides guidance on whether share-based payment arrangements, in which suppliers of goods or services of an entity are provided with equity instruments of the entity's parent, should be accounted for as cash-settled or equity-settled in the entity's financial statements. The Bank has not yet completed its analysis of the impact of the new Interpretation.

d) Functional and presentation currency

The Bank's financial statements are presented in Croatian kuna (HRK), which is the functional currency. Amounts are rounded to the nearest thousand (unless otherwise stated).

The exchange rate as at 31 December 2006 was HRK 7.3451 to EUR 1 (2005: HRK 7.3756) and HRK 5.5784 to USD 1 (2005: HRK 6.2336).

e) Changes in presentation or classification of the items in the financial statements

Where necessary, comparative information has been reclassified to achieve consistency with current financial year amounts and other disclosures.

f) Interest income and expense

Interest income and expense are recognised in the income statement as they accrue for all interest bearing financial instruments, including those measured at amortised cost, at fair value through profit or loss and available for sale, using the linear interest rate method. Such income and expense is presented as interest and similar income or interest expense and similar charges in the income statement. Interest income and expense also includes fee and commission income and expense in respect of loans provided to customers or borrowings from other banks, premium or discount amortisation, and other differences between the initial carrying amount of an interest bearing financial instrument and its value at maturity, recognised on an linear basis. Interest income and expense on all trading assets and liabilities are presented as interest income or expense.

g) Fee and commission income and expense

Fee and commission income and expense mainly comprises fees related to domestic and foreign payments, the issue of guarantees and letters of credit, and credit card business. Fees and commissions are generally recognised on an accruals basis where the service has been provided, unless they have been included, as indicated above, in the calculation of interest income or expense. Portfolio and other management advisory and service fees are recognised based on the applicable service contracts. Asset management fees are recognised over the period in which the service is provided. Fees for the issue of guarantees and letters of credit are recognised over the period over which the service is provided.

h) Dividend income

Dividend income from equity securities is recognised in the income statement when the rights to receive the dividend are established.

i) Gains less losses from dealing and investment securities

Gains less losses from dealing securities include unrealised and realised gains and losses arising from derivative financial instruments, trading debt securities and other financial instruments designated at fair value through profit or loss.

Gains less losses arising from investment securities comprise realised gains from financial instruments available for sale.

j) Gains less losses arising from dealing in foreign currencies

Gains less losses from dealing in foreign currencies include unrealised and realised gains and losses arising from spot dealings in foreign currencies.

k) Foreign currencies

Transactions in foreign currencies are translated into HRK at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated into HRK at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement. Non-monetary assets and liabilities denominated in foreign currency that are stated at fair value are translated in HRK at the foreign exchange rates ruling at the dates when the fair values were determined. Non-monetary assets and items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction and are not retranslated at balance sheet date.

Changes in the fair value of monetary 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. The translation differences are recognised in the income statement as part of the foreign exchange gains or losses on the revaluation of monetary assets and liabilities presented within general and administrative expenses (2005: other operating income) in the income statement. Translation differences on non-monetary financial assets, such as equity instruments classified as available for sale, are included in the fair value reserve in equity.

l) Financial instruments
Classification

The Bank classifies its financial instruments in the following categories: at fair value through profit or loss, loans and receivables, available for sale, held to maturity or financial liabilities. The classification depends on the purpose for which the financial instruments were acquired. The management determines the classification of financial instruments upon initial recognition.

Financial assets and financial liabilities at fair value through profit or loss

This category comprises: financial instruments held for trading (including derivatives), and those designated by management as at fair value through profit or loss at inception. The Bank 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.

Loans and receivables

This category comprises non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Bank provides money to a debtor with no intention of trading with the receivable and include purchased loans and receivables.

Financial instruments held to maturity

This category comprises non-derivative financial assets with fixed or determinable payments and fixed maturities that the Bank has the positive intention and ability to hold to maturity.

Financial assets available for sale

This category comprises non-derivative financial assets which are not included in loans and receivables or held-to-maturity investments, or classified as financial assets at fair value through profit or loss. Financial assets 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 designated at fair value through profit or loss.

Recognition and derecognition

Purchases and sales of financial assets and financial liabilities at fair value through profit or loss, and financial assets held to maturity and available for sale, are recognised on the settlement date which is the date when the financial instrument is delivered to or transferred from the Bank. Loans and receivables and financial liabilities at amortised cost are recognised when advanced to borrowers or received from lenders.

The Bank derecognises financial instruments (in full or part) when the rights to receive cash flows from the financial instrument have expired or when it loses control over the contractual rights over financial assets. It occurs when the Bank transfers substantially all the risks and rewards of ownership to another business entity or when the rights are realised, surrendered or have expired. The Bank derecognises financial liabilities only when the financial liability ceases to exist, ie when it is discharged, cancelled or has expired. If the terms of a financial liability change, the Bank 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 by using the weighted average cost method.

Initial and subsequent measurement

Financial assets and liabilities are recognised initially at their fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

After initial recognition, the Bank measures financial instruments at fair value through profit or loss and available for sale at their fair value, without any deduction for transaction costs. Equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are measured at cost less impairment.

Loans and receivables and held-to-maturity investments and financial liabilities not designated at fair value through profit or loss are measured at amortised cost.

Gains and losses

Gains or 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 or losses from a change in the fair value of available-for-sale monetary assets are recognised directly in a fair value reserve within equity 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 on available-for-sale monetary assets are recognised in the income statement. Foreign exchange differences on equity instruments are part of the fair value of these instruments and are recognised in equity.

Dividend income is recognised in the income statement. Upon sale or other derecognition of available-for-sale assets, any cumulative gains or losses on the instrument are transferred to the income statement.

Gains or losses arising from financial assets and financial liabilities carried at amortised cost are recognised as interest in the income statement over the period of amortisation. Gains or losses may also be recognised in the income statement when a financial instrument is derecognised or when its value is impaired.

Determination of fair value of financial instruments

The fair value of quoted financial assets in an active market is based on their current bid prices. If there is no active market for the financial instrument, or if, due to any other reason, the fair value cannot be reliably measured by the market price, the Bank uses an internal evaluation model for fair value estimation. Such models include the use of prices achieved in a recent transactions, reference to similar financial instruments, and discounted cash flow analysis, making maximum use of market inputs and relying as little as possible on entity-specific inputs. Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimate and the discount rate is a market rate.

The fair value of non-exchange-traded derivatives is estimated at the amount that the Bank would receive or pay to terminate the contract on the balance sheet date taking into account current market conditions and the current creditworthiness of the counterparties.

Impairment of financial assets

Impairment of assets identified as impaired

Financial assets are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such indication exists, the asset's recoverable amount is estimated.

The Bank estimates and performs impairment of all financial assets, except financial assets at fair value through profit or loss.

The recoverable amount of financial instruments measured at amortised cost is calculated as the present value of the expected future cash flows, discounted at the instrument's original interest rate. Short-term balances are not discounted.

Allowances for uncollectibility are made against the carrying amount of loans and advances that are identified as being impaired based on regular reviews of outstanding balances to reduce these loans and advances to their recoverable amounts (or lower amount if required by applicable CNB regulations). Increases in the impairment allowance account are recognised in the income statement. When a loan is known to be uncollectable, all the necessary legal procedures have been completed, and the final loss has been determined, the loan is written off directly. If in a subsequent period the amount of an impairment loss decreases and the decrease can be linked objectively to an event occurring after the write-down, the write-down or impairment loss is reversed through the income statement.

Impairment of assets not identified as impaired

In addition impairment losses on assets identified as impaired, the Bank recognises impairment losses, in income, on on- and off-balance-sheet credit risk exposures not identified as impaired at rates from 0.85-1.20%, in accordance with the accounting regulations of the CNB. Debt securities carried at fair value were excluded from the basis of such calculation at the balance sheet date.

m) Specific instruments

Cash and cash equivalents

Cash and cash equivalents comprise cash and balances with the Croatian National Bank, placements with other banks with original maturity of up to 90 days, and items in the course of collection.

Derivative financial instruments

The Bank uses derivative financial instruments to hedge economically its exposure to currency risk and interest rate risk arising from operating, financing and investing activities. In accordance with its investment policies, the Bank does not hold or issue derivative financial instruments for the purpose of speculative trading. No derivative instruments are as accounted for hedging instruments. All derivative agreements are classified as financial instruments at fair value through profit or loss.

Derivative financial instruments include foreign currency agreements, forward agreements, futures and other financial derivatives and are initially recognised at fair value which is the value of consideration paid to acquire the instrument less transaction costs. Subsequent to initial recognition, derivatives are measured at fair value. The fair value is determined based on the quoted market price or, if more appropriate, based on the discounted cash flow. All derivative instruments are presented as assets if their fair value is positive and as liabilities if their fair value is negative.

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 gains and losses recognised in the income statement, unless there is no reliable measure of their fair value.

Changes in the fair value of derivatives are included in gains less losses arising from dealing securities.

Treasury bills and debt securities

Treasury bills and debt securities that the Bank holds for the purpose of short-term profit taking are classified as at fair value through profit or loss or as available-for-sale assets, and are carried at fair value. Treasury bills and debt securities that the Bank has the intent and ability to hold to maturity are classified as held-to-maturity assets.

Equity securities and investments in open ended investment funds

Equity securities and investments in open ended investment funds are classified as at fair value through profit or loss or as available-for-sale assets.

Placements with banks

Placements with banks are classified as loans and receivables and are carried at amortised cost less impairment losses.

Loans and advances to customers

Loans and advances are presented net of impairment losses. Purchased loans that the Bank has the intent and ability to hold to maturity are classified as held-to-maturity assets.

In accordance with CNB requirements, the amortisation of any discounts included within impairment losses is presented in impairment losses.

Borrowings

Interest-bearing borrowings are recognised initially at 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 as interest.

Repurchase agreements

The Bank enters into purchases/(sales) of investments under agreements to resell (repurchase) substantially identical investments 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. The amounts paid are recognised in loans and advances to either banks or customers. The receivables are shown as collateralised by the underlying security. Investments sold under repurchase agreements continue to be recognised in the balance sheet 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 investments are reported as 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.

n) Investments in subsidiaries

In the Bank's separate financial statements investments in subsidiaries are accounted for at cost less impairment losses. Investments in subsidiaries are fully consolidated in the consolidated financial statements.

Investments in associates in the consolidated financial statements of the Bank are accounted for under the equity method of accounting, reduced for impairment losses. In the Bank's separate financial statements such investments are accounted for at cost less impairment losses.

Other equity securities are classified as at fair value through profit and loss or available-for-sale assets and measured at fair value.

o) Income tax

The income tax charge is based on taxable profit for the year and 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 equity, in which case it is recognised in equity. Current tax is the expected tax payable on the taxable income for the year, using the tax rates enacted or substantially enacted at the balance sheet date, and any adjustments to tax payable in respect of previous years.

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. Deferred tax assets and liabilities are measured by using the tax rates expected to apply to taxable profit in the years in which those temporary differences are expected to be recovered or settled based on tax rates enacted or substantially enacted at the balance sheet date.

The measurement of deferred tax liabilities and deferred tax assets reflects the tax consequences that would follow from the manner in which the enterprise expects, at the balance sheet date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are not discounted and are classified as non-current assets and/or liabilities in the balance sheet. 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 balance sheet date, the Bank reassesses unrecognised potential deferred tax assets and the carrying amount of recognised deferred tax assets.

p) Property, plant and equipment

Items of property, plant and equipment are shown at cost or deemed cost, less accumulated depreciation and impairment losses.

The Bank recognises in the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if it is probable that future economic benefits embodied with the item will flow to the Bank and the cost of the item can be measured reliably. All other expenditure on repairs and maintenance is expensed as incurred.

Depreciation is provided on a straight-line basis to allocate the cost of assets to their residual values over their estimated economic useful life. Land and assets under construction or development are not depreciated. The estimated useful lives are as follows:

	2006	2005
Buildings	40 years	40 years
Computers	3 years	3 years
Furniture and equipment	3-4 years	3-4 years
Motor vehicles	5 years	5 years
Other assets	10 years	10 years

The assets' residual values, depreciation method and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. 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. Gains and losses on disposals are determined by comparing proceeds with carrying amount, and are included in the income statement.

q) Intangible assets

Intangible assets are stated at cost less accumulated amortisation and impairment losses. Expenditure on development activities are capitalised if all of the features required by IAS 38 "Intangible assets" are satisfied. Amortisation is provided on a straight-line basis over the estimated useful lives of intangible assets.

Intangible assets are amortised on a straight-line basis over their estimated useful economic lives as follows:

	2006	2005
Leasehold improvements	4 years	4 years
Software	3-7 years	3 years
Other intangible assets	3-7 years	4 years

In 2006 the Bank changed the estimate of useful lives for certain software types and some categories of other intangible assets. These changes resulted in the reduction of amortisation expense by HRK 175 thousand, compared with amortisation rates used in 2005.

r) Non-current assets held for sale

Initially, non-current assets held for sale are recognised at the lower of carrying amount and fair value less costs to sell.

The Bank discontinues to classify assets as held for sale if the sale is no longer highly probable. The Bank measures non-current assets that cease to be classified as held for sale at the lower of the asset's carrying amount before the asset was classified as held for sale, adjusted for any depreciation, amortisation or revaluations and its recoverable amount at the date of subsequent decision not to sell. Any gain or loss from disposal or reclassification of non-current assets held for sale is recognised in the income statement as incurred.

s) Impairment of non-financial assets

The recoverable amount of property, plant and equipment 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. Non-financial assets that have suffered impairment 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 and to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no impairment loss had been recognised.

t) Provisions for liabilities and charges

The Bank recognises a provision when it has a present obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the obligation.

Provision for liabilities and charges are maintained at a level which management believes is adequate to absorb probable future losses. The management determines the adequacy of the provision based upon reviews of individual items, recent loss experience, current economic conditions, the risk characteristics of the various categories of transactions and other pertinent factors.

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

u) Employee benefits

Defined pension contributions

The Bank pays contributions to insurance plans on a mandatory, contractual basis. The Bank has no further payment obligations once the contributions have been paid. The contributions are recognised as employee benefit expense when they are due.

Provisions for severance payments and jubilee awards

In calculating provisions for severance payments and jubilee awards, the Bank discounts expected future cash flows in respect of the liabilities, using discount rates that, in opinion of the Bank's management, best represent the time value of money.

v) Retained earnings

Any profit for the year after appropriations is transferred to reserves, in accordance with General Assembly decisions.

w) Share capital and reserves

Share capital is stated in HRK at nominal value. The amount of consideration paid on repurchase of share capital, including directly attributable costs, is recognised as a deduction from equity and classified as treasury shares.

Dividends are recognised as a liability in the period in which they are declared.

The Bank recognises a reserve for general banking risks, which represents a reserve for potential losses in excess of those expected and provided for through recognised impairment losses. The reserve is calculated in accordance with applicable regulations which require that a certain percentage of net profit for the year be set aside as a reserve within equity if the growth of risk assets on an annual basis exceeds a specific level. The reserve for general banking risk cannot be transferred to retained earnings or other reserves or be otherwise distributed until the expiry of a consecutive three year period in which the Bank has recorded annual growth not exceeding 20%.

x) Earnings per share

The Bank presents earnings per share (EPS) data for its ordinary shares. EPS is 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.

y) Off-balance-sheet commitments and contingent liabilities

In the ordinary course of business, the Bank enters into credit related commitments which are recorded in off-balance-sheet accounts and primarily comprise guarantees, letters of credit and undrawn loan commitments. Such financial commitments are recorded in the Bank's balance sheet if and when they become payable.

z) Managed funds for and on behalf of third parties

The Bank manages funds for and on behalf of corporate and retail customers. These amounts do not represent the Bank's assets and are excluded from the balance sheet. For the services rendered, the Bank charges a fee which is recognised in the income statement on an accruals basis.

aa) Segment reporting

A segment is a distinguishable component of the Bank that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments. The Bank's current operations are in the segment of retail, corporate, treasury and investment banking (business segments) and its operations, total assets and the majority of its clients are located in Croatia (geographical segment).

2. CHANGES IN ACCOUNTING POLICIES

In June 2006 the CNB revised the mandatory chart of accounts which requires the recognition and derecognition of financial assets on the settlement date, which is the date that a financial instrument is delivered to or transferred from the Bank and not at trade date, which is the date on which the Bank commits to purchase or sell the instrument.

Consequently, the Bank changed its accounting policy from trade date accounting to settlement date accounting during the year for financial assets and liabilities at fair value through profit and loss. The policy was applied retrospectively. However, as at 31 December 2005 the Bank did not have any unsettled transactions in respect of sold or acquired financial assets or liabilities that were previously recognised on a trade date, no effects from the change of this policy were recognised retrospectively.

3. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS

The Bank 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 reasonably assumed in existing circumstances, but nevertheless necessarily represent sources of estimation uncertainty. The estimation of impairment losses in the Bank's credit risk portfolio represents the major source of estimation uncertainty. This and other key sources of estimation uncertainty, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below. Significant judgements made in determining the most appropriate methodology for estimating the fair value of financial instruments carried at fair value are also described below.

Impairment losses on loans and receivables

The Bank monitors the creditworthiness of its customers on an ongoing basis. In accordance with CNB regulations, the need for impairment of the Bank's on- and off-balance-sheet credit risk exposure is assessed at least quarterly. Impairment losses are made mainly against the carrying value of loans and advances to corporate and retail customers (summarised in Note 11), and as provisions for liabilities and charges arising from off-balance-sheet risk exposure to customers, mainly in the form of guarantees, documentary credits and undrawn loan commitments (summarised in Notes 21 and 37). Impairment losses are also considered for credit risk exposures to banks, and for other assets not carried at fair value, where the primary risk of impairment is not credit risk.

	Notes	2006 HRK '000	2005 HRK '000
Summary of impairment losses for customers			
Impairment losses on loans and advances to customers	11	201,265	271,172
Provisions for off-balance-sheet exposure	21	16,875	13,734
Total		**218,140**	**284,906**

Financial assets carried at amortised cost

The Bank first assesses whether objective evidence of impairment exists individually for assets that are individually significant (mainly corporate exposures) and collectively for assets that are not individually significant (mainly retail exposures). However, assets assessed individually as unimpaired are then included in groups of assets with similar credit risk characteristics. These portfolios are then assessed collectively for impairment.

The Bank estimates impairment losses in cases where it judges that the observable data indicates the likelihood of a measurable decrease in the estimated future cash flows of the asset or portfolio of assets. Such evidence includes delinquency in payments or other indications of financial difficulty of borrowers; and adverse changes in the economic conditions in which borrowers operate or in the value or enforceability of security, where these changes can be correlated with defaults.

The Bank takes into consideration the combined effect of several events when assessing impairment and uses its experienced judgement in cases where the observable data required to estimate impairment is limited. In estimating impairment losses on items individually or collectively assessed as impaired, the Bank has regard to the ranges of impairment loss prescribed by the CNB based on the age of overdue amounts.

At the year end, the gross value of specifically impaired loans and advances, and the rate of impairment loss recognised, was as follows:

	2006 HRK'000			2005 HRK'000		
	Corporate	**Retail**	**Total**	**Corporate**	**Retail**	**Total**
Gross value of exposure	177,372	44,804	222,176	247,985	37,294	285,279
Impairment rate	43%	84%	52%	76%	87%	77%

Each additional increase of one percentage point in the impairment rate on the gross portfolio at 31 December 2006 would lead to the recognition of an additional impairment loss of HRK 2,222 thousand (2005: HRK 2,853 thousand).

The Bank also seeks to recognise impairment losses which are known to exist at the balance sheet date, but which have not yet been specifically identified. In estimating unidentified impairment losses existing in collectively assessed portfolios, and in the absence of reliable data on historical loss rates and the emergence period for the identification of these impairment losses, the Bank has regard to the range of impairment loss rates of 0.85% to 1.20% prescribed by the CNB to be calculated on all credit risk exposures except those carried at fair value, including off-balance-sheet amounts (including undrawn lending and credit card commitments) and Croatian sovereign risk. Amounts assessed as impaired on an individual basis are excluded from this calculation.

The amount of impairment losses at 31 December 2006 estimated on a portfolio basis amounted to HRK 103,281 thousand (2005: HRK 64,524 thousand) of the relevant on- and off-balance-sheet exposure. The total of these portfolio based impairment losses amounted to 1.74% of loans and advances to customers (2005: 2.22%) and to 1% (2005: 1%) of on- and off-balance-sheet exposure, in both cases net of amounts individually assessed as impaired.

At the minimum rate prescribed by the CNB, portfolio based impairment allowances would be HRK 15,492 thousand (2005: HRK 9,678 thousand) lower than the amount recognised by the Bank. At the maximum rate prescribed by the CNB, portfolio based impairment allowances would be HRK 20,656 thousand (2005: HRK 12,905 thousand) higher than the amount recognised by the Bank.

Fair value of derivatives

The fair value of OTC derivatives are determined by using valuation techniques. Where valuation techniques (for example, models) are used to determine fair values, they are validated and periodically reviewed by qualified personnel independent of the area that created them. All models are certified before they are used, and models are calibrated to ensure that outputs reflect actual data and comparative market prices.

Fair value of treasury bills

The Bank determines the fair value of treasury bills issued by the Ministry of Finance of the Republic of Croatia, by reference to the market price of the last auction, and adjusted to the yield to maturity, using an internal model which considers their remaining maturity and the latest available auction prices of equivalent instruments. As at 31 December 2006, the carrying amount of treasury bills classified as financial assets at fair value through profit or loss or financial assets available for sale was to HRK 1,431,695 thousand (2005: HRK 1,607,617 thousand).

Fair value of the financial instruments quoted in an active market

In estimating the fair value of quoted financial instruments, the Bank does not use closing prices at the date of estimation, but applies average prices which are based on the individual transaction volumes of the specified instruments during the day of estimation. In the opinion of the Bank's management, this method provides a more realistic indication of the real price of the instrument, and decreases the risk of inadequate or inappropriate estimation of fair value which may result from limited trading in the instrument just before the end of the trading period, at a price which significantly differs from the daily average. The application of this policy resulted in financial assets at fair value through profit or loss of HRK 329,717 thousand (2005: HRK 265,853 thousand) being carried at amounts HRK 134 thousand higher (2005: HRK 188 thousand higher), and financial assets available for sale of HRK 97,313 thousand (2005: HRK 257,433 thousand) being carried at amounts HRK 21 thousand higher (2005: HRK 432 thousand lower), than had closing prices been applied.

Provisions for court cases initiated against the Bank

In calculating provisions for court expenses, severance payments and jubilee awards, the Bank discounts expected future cash flows in respect of the liabilities, using discount rates that, in the opinion of the Bank's management, best represent the time value of money.

Taxation

The Bank 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.

4. SEGMENT REPORTING

Limited segment information is presented in respect of the Bank's business segments. The primary format, business segments, is based on the Bank's management and internal reporting structure. However, as the Bank is unable to allocate overhead expenses and equity to segments, segment profitability is not reported.

Business segments

The Bank comprises the following main business segments:

- Corporate Banking — Includes loans, deposits and other transactions and balances with corporate customers
- Retail Banking — Includes loans, deposits and other transactions and balances with retail customers
- Central Treasury — Undertakes the Bank's funding and centralised risk management activities through borrowings, issues of debt securities, use of derivatives for risk management purposes and investing in liquid assets such as short-term placements and corporate and government debt securities
- Investment Banking — Includes the Bank's corporate and retail finance activities

	Corporate	Retail	Treasury	Investment banking	Unallocated	Total
						2006 HRK'000
Net interest income	208,732	60,447	53,954	9,641	-	332,774
Net fee and commission income	37	67,122	-	11,788	1,977	80,924
Dealing income	-	-	58,106	-	-	58,106
Other income	1,393	643	6	3	1,832	3,877
Operating income	**210,162**	**128,212**	**112,066**	**21,432**	**3,809**	**475,681**
General and administrative expenses	-	-	-	-	(300,100)	(300,100)
Depreciation and amortisation	-	-	-	-	(34,144)	(34,144)
Impairment losses on loans and advances to customers and other assets	26,744	(1,244)	(516)	-	(35,615)	(10,631)
Provisions for liabilities and charges	-	-	-	-	(3,316)	(3,316)
Operating expenses	**26,744**	**(1,244)**	**(516)**	**-**	**(373,175)**	**(348,191)**
Profit before tax	**-**	**-**	**-**	**-**		**127,490**
Income tax expense	-	-	-	-	(26,365)	(26,365)
Profit for the year	**-**	**-**	**-**	**-**	**-**	**101,125**
Segment assets	4,617,930	1,729,195	4,391,731	141,200	-	10,880,056
Unallocated assets	-	-	-	-	397,797	397,797
Total assets	**4,617,930**	**1,729,195**	**4,391,731**	**141,200**	**397,797**	**11,277,853**
Segment liabilities	4,846,848	3,342,771	1,861,226	13,436	-	10,064,281
Unallocated equity and liabilities	-	-	-	-	1,213,572	1,213,572
Total equity and liabilities	**4,846,848**	**3,342,771**	**1,861,226**	**13,436**	**1,213,572**	**11,277,853**

	Corporate	Retail	Treasury	Investment banking	Unallocated	Total
						2005 HRK'000
Net interest income	109,238	29,525	107,874	1,836	-	248,473
Net fee and commission income	(37)	59,069	-	1,740	-	60,772
Dealing income	-	-	44,420	-	-	44,420
Other income	94	6,369	33	1	1,799	8,296
Operating income	**109,295**	**94,963**	**152,327**	**3,577**	**1,799**	**361,961**
General and administrative expenses	-	-	-	-	(196,102)	(196,102)
Depreciation and amortisation	-	-	-	-	(24,455)	(24,455)
Impairment losses on loans and advances to customers and other assets	(26,824)	(167)	-	-	7,660	(19,331)
Provisions for liabilities and charges	-	-	-	-	(11,195)	(11,195)
Operating expenses	**(26,824)**	**(167)**	**-**	**-**	**(224,092)**	**(251,083)**
Profit before tax	**-**	**-**	**-**	**-**	**-**	**110,878**
Income tax expense	-	-	-	-	(20,716)	(20,716)
Profit for the year	**-**	**-**	**-**	**-**	**-**	**90,162**
Segment assets	2,270,552	1,061,792	3,690,638	38,558	-	7,061,540
Unallocated assets	-	-	-	-	221,386	221,386
Total assets	**2,270,552**	**1,061,792**	**3,690,638**	**38,558**	**221,386**	**7,282,926**
Segment liabilities	2,931,314	2,231,409	1,140,279	3,328	-	6,306,330
Unallocated equity and liabilities	-	-	-	-	976,596	976,596
Total equity and liabilities	**2,931,314**	**2,231,409**	**1,140,279**	**3,328**	**976,596**	**7,282,926**

5. CASH AND RECEIVABLES FROM BANKS

	2006 HRK '000			2005 HRK '000		
	In HRK	In foreign currency	Total	In HRK	In foreign currency	Total
Cash in hand						
Held by the Bank	96,088	22,137	118,225	37,670	12,883	50,553
Held by other parties	150,768	-	150,768	170,686	-	170,686
Cheques in the course of collection	-	2	2	-	3	3
	246,856	**22,139**	**268,995**	**208,356**	**12,886**	**221,242**
Receivables from banks						
Current accounts with domestic banks	-	9,046	9,046	-	2,674	2,674
Current accounts with foreign banks	-	31,571	31,571	-	18,610	18,610
Giro account with the CNB	270,102	-	270,102	146,163	-	146,163
	270,102	**40,617**	**310,719**	**146,163**	**21,284**	**167,447**
Total	**516,958**	**62,756**	**579,714**	**354,519**	**34,170**	**388,689**

6. OBLIGATORY RESERVE WITH CROATIAN NATIONAL BANK

	2006 HRK '000			2005 HRK '000		
	In HRK	In foreign currency	Total	In HRK	In foreign currency	Total
Obligatory reserve	912,815	80,575	993,390	611,571	53,842	665,413
Marginal obligatory reserve	-	32,708	32,708	-	19,531	19,531
Interest receivable - due	567	-	567	388	-	388
Interest receivable - not due	22	55	77	12	22	34
Total	**913,404**	**113,338**	**1,026,742**	**611,971**	**73,395**	**685,366**

The obligatory reserve represents amounts required to be deposited with the CNB.

At 31 December 2006, the obligatory reserve requirement amounted to 17% (2005: 18%) of kuna and foreign currency deposits, borrowings and issued debt securities.

At 31 December 2006, the required minimum rate of maintenance of the kuna obligatory reserve with the CNB amounted to 70% (2005: 70%), while the remaining 30% (2005: 30%) could be held in the form of other liquid receivables. This includes the part of foreign currency obligatory reserve required to be held in HRK (see below). In 2006, the annual interest rate on the kuna obligatory reserve payable by the CNB was 0.75% (2005: 0.75%).

60% of the foreign currency obligatory reserve (2005: 60%) is required to be held with the CNB, while the remaining 40% (2005: 40%) may 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). 50% (2005: 42%) of the foreign currency obligatory reserve is required to be held in HRK and is added to the kuna obligatory reserve (see above). At 31 December 2006, the annual interest rate on the foreign currency obligatory reserve payable by the CNB was 1.75% (2005: 1.13%).

In 2006, the marginal obligatory reserve requirement, whereby banks have to maintain funds on a non-interest earning account with the CNB, amounted to 55% (2005: 40%) of the net increase in liabilities to non-residents and related parties, from June 2004, when this requirement was introduced, and later dates from when, in 2006, the CNB broadened the basis for calculation of this reserve.

7. PLACEMENTS WITH AND LOANS TO OTHER BANKS

	2006 HRK '000	2005 HRK '000
Short-term placements with domestic banks	182,000	237,820
Short-term placements with foreign banks	782,257	310,851
Total short-term placements and loans	**964,257**	**548,671**
Guarantee deposits with foreign banks	1,229	89,254
Long-term placements with domestic banks	173,000	17,000
Total long-term placements and loans	**174,229**	**106,254**
Interest receivable - not due	4,850	2,540
Total interest receivable	**4,850**	**2,540**
Total	**1,143,336**	**657,465**

Long-term placements with domestic banks include an amount of HRK 100,000 thousand (2005: HRK 88,508 thousand held at foreign banks), pledged as collateral for the repayment of long-term borrowings repayable in 17 instalments from 14 September 2007 to 14 September 2015. Guarantee deposits mainly relate to deposits for card operations.

8. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

	2006 HRK '000	2005 HRK '000
Financial assets designated at fair value through profit or loss		
Ministry of Finance treasury bills	1,431,695	1,126,878
Croatian Bank for Reconstruction and Development bonds	30,420	32,025
Bonds issued by banks	9,750	-
Ministry of Finance bonds	213,906	199,759
Corporate bonds and commercial paper	34,746	25,670
Debt securities, traded or quoted on active markets	1,720,517	1,384,332
Investments in investment funds, quoted on active markets	42,636	35,341
Equity securities, traded or quoted on active markets	40,895	13,182
	1,804,048	**1,432,855**
Trading instruments		
Positive fair value of foreign exchange derivatives		
- forward contracts, OTC	233	-
- futures, quoted on active markets	1,496	-
	1,729	**-**
Interest receivable - not due	4,839	5,645
Total	**1,810,616**	**1,438,500**

9. FINANCIAL ASSETS AVAILABLE FOR SALE

	2006 HRK '000	2005 HRK '000
Debt securities, traded or quoted on active markets		
Ministry of Finance treasury bills	-	480,739
Ministry of Finance bonds	97,313	257,433
Bills of exchange	197,884	179,800
	295,197	**917,972**
Equity securities, non quoted on active markets		
- corporate	790	790
- non-banking financial institutions	1,513	84
	2,303	**874**
Interest receivable - not due	2,431	2,814
Impairment loss on bills of exchange	**(257)**	**-**
Total	**299,674**	**921,660**

Movement in impairment losses

The movement in the impairment losses on bills of exchange, recognised in the income statement, is as follows:

	2006 HRK '000	2005 HRK '000
Balance as at 1 January	-	189
Increase/(release) in impairment loss of financial assets available for sale	257	(189)
Balance as at 31 December	**257**	**-**

10. FINANCIAL ASSETS HELD TO MATURITY

	2006 HRK ‘000	2005 HRK ‘000
Bills of exchange	150	-
Total	**150**	**-**

11. LOANS AND ADVANCES TO CUSTOMERS

	2006 HRK '000	2005 HRK '000
Short-term loans		
Corporate	1,956,006	1,423,731
Retail	560,456	331,497
Total short-term loans	**2,516,462**	**1,755,228**
Long-term loans		
Corporate	2,487,156	831,942
Retail	1,149,192	610,570
Total long-term loans	**3,636,348**	**1,442,512**
Interest receivable - due	40,502	15,190
Interest receivable - not due	6,177	1,131
Total gross amounts	**6,199,489**	**3,214,061**
Impairment losses	**(201,265)**	**(271,172)**
Total	**5,998,224**	**2,942,889**

Loans and advances to customers include loans revalued in accordance with one-way currency clauses in the amount of HRK 341 thousand (2005: HRK 3,789 thousand) calculated as the difference between the mid CNB rate and the contractual rate of the clauses.

Movement in impairment losses for loans and advances to customers

The movement in impairment losses on loans and advances to customers is presented as follows:

	2006 HRK'000			2005 HRK'000		
	Identified losses	Unidentified losses	Total	Identified losses	Unidentified losses	Total
At 1 January	**220,380**	**50,792**	**271,172**	**194,150**	**58,261**	**252,411**
(Decrease)/increase in impairment losses	(14,857)	35,615	20,758	26,420	(7,469)	18,951
Amounts recovered during the year	(9,906)	-	(9,906)	(2,136)	-	(2,136)
Net foreign exchange (gain)/loss	(450)	-	(450)	1,946	-	1,946
Usage	(80,309)	-	(80,309)	-	-	-
At 31 December	**114,858**	**86,407**	**201,265**	**220,380**	**50,792**	**271,172**

Concentration of credit risk by industry

Commercial lending is concentrated on companies and individuals domiciled in Croatia. An analysis of the concentration of credit risk by industry of loans and advances to companies is presented below:

	2006 HRK '000	2005 HRK '000
Agriculture and forestry	95,844	51,780
Industry	1,448,039	846,749
Construction	439,645	527,305
Transport, storage and communications	283,140	98,842
Trade	876,677	380,046
Tourism	164,107	96,532
Services	357,143	88,349
Ministry of Finance	578,420	78,285
Other	200,147	87,785
Total gross loans and advances to companies	**4,443,162**	**2,255,673**
Loans and advances to individuals (gross)	1,709,648	942,067
Interest receivable	46,679	16,321
Allowance for impairment losses	(201,265)	(271,172)
Total	**5,998,224**	**2,942,889**

12. INVESTMENTS IN SUBSIDIARIES

	2006 HRK '000	2005 HRK '000
HPB Invest d.o.o.	5,000	5,000
HPB Nekretnine d.o.o.	50	50
HPB Stambena štedionica d.o.o.	30,000	-
Total investments in subsidiaries	**35,050**	**5,050**

In 2006, the Bank established HPB Stambena štedionica d.o.o., a savings bank (2005: HPB Invest d.o.o., an investment fund management company and HPB Nekretnine d.o.o., a real estate company). All subsidiaries are 100% owned by the Bank and are domiciled in Croatia.

13. PROPERTY, PLANT AND EQUIPMENT

2006	Buildings HRK '000	Computers, equipment and motor vehicles HRK '000	Assets in the course of construction HRK '000	Total HRK '000
Gross carrying amount				
Balance at 1 January 2006	125,004	107,199	22,492	254,695
Additions	-	-	42,133	42,133
Write-offs	-	(10,390)	-	(10,390)
Transfers	1,085	45,495	(46,580)	-
Balance at 31 December 2006	**126,089**	**142,304**	**18,045**	**286,438**
Accumulated depreciation				
Balance at 1 January 2006	(34,225)	(63,139)	-	(97,364)
Charge for the year	(3,139)	(23,998)	-	(27,137)
Write-offs	-	10,351	-	10,351
Balance at 31 December 2006	**(37,364)**	**(76,786)**	**-**	**(114,150)**
Carrying amount				
Balance at 31 December 2006	**88,725**	**65,518**	**18,045**	**172,288**
Balance at 1 January 2006	90,779	44,060	22,492	157,331

2005	Buildings HRK '000	Computers, equipment and motor vehicles HRK '000	Assets in the course of construction HRK '000	Total HRK '000
Gross carrying amount				
Balance at 1 January 2005	123,710	74,959	19,665	218,334
Additions	24	-	36,348	36,372
Disposals	-	(11)	-	(11)
Transfers	1,270	32,251	(33,521)	-
Balance at 31 December 2005	**125,004**	**107,199**	**22,492**	**254,695**
Accumulated depreciation				
Balance at 1 January 2005	(31,130)	(45,227)	-	(76,357)
Charge for the year	(3,095)	(17,912)	-	(21,007)
Balance at 31 December 2005	**(34,225)**	**(63,139)**	**-**	**(97,364)**
Carrying amount				
Balance at 31 December 2005	**90,779**	**44,060**	**22,492**	**157,331**
Balance at 1 January 2005	92,580	29,732	19,665	141,977

Assets in the course of construction comprise equipment at cost of HRK 18,045 thousand (2005: HRK 22,492 thousand).

14. INTANGIBLE ASSETS

2006	Software HRK '000	Leasehold improvements HRK '000	Licences HRK '000	Assets in the course of construction HRK '000	Total HRK '000
Gross carrying amount					
Balance at 1 January 2006	12,019	7,239	8,848	5,080	33,186
Additions	-	-	-	58,953	58,953
Transfers	6,204	16,627	3,102	(25,933)	-
Balance at 31 December 2006	**18,223**	**23,866**	**11,950**	**38,100**	**92,139**
Accumulated depreciation					
Balance at 1 January 2006	(8,791)	(1,103)	(3,455)	-	(13,349)
Charge for the year	(2,276)	(2,927)	(1,804)	-	(7,007)
Balance at 31 December 2006	**(11,067)**	**(4,030)**	**(5,259)**	**-**	**(20,356)**
Carrying amount					
Balance at 31 December 2006	**7,156**	**19,836**	**6,691**	**38,100**	**71,783**
Balance at 1 January 2006	3,228	6,136	5,393	5,080	19,837

2005	Software HRK '000	Leasehold improvements HRK '000	Licences HRK '000	Assets in the course of construction HRK '000	Total HRK '000
Gross carrying amount					
Balance at 1 January 2005	9,931	1,044	4,297	4,561	19,833
Additions	-	-	-	13,353	13,353
Transfers	2,088	6,195	4,551	(12,834)	-
Balance at 31 December 2005	**12,019**	**7,239**	**8,848**	**5,080**	**33,186**
Accumulated depreciation					
Balance at 1 January 2005	(6,813)	(402)	(2,686)	-	(9,901)
Charge for the year	(1,978)	(701)	(769)	-	(3,448)
Balance at 31 December 2005	**(8,791)**	**(1,103)**	**(3,455)**	**-**	**(13,349)**
Carrying amount					
Balance at 31 December 2005	**3,228**	**6,136**	**5,393**	**5,080**	**19,837**
Balance at 1 January 2005	3,118	642	1,611	4,561	9,932

Assets in the course of construction comprise application software and licences at cost of HRK 36,983 thousand (2005: HRK 5,080 thousand) and leasehold improvements at cost of HRK 1,117 thousand (2005: nil), which are being prepared for the use by the Bank.

15. NET DEFERRED TAX ASSET

a) Recognised deferred tax assets and liabilities -2006

Movements in temporary differences and components of deferred tax assets and deferred tax liabilities are as follows:

	2006 HRK '000	Credited/(charged) to income statement HRK '000	Credited/(charged) to equity HRK '000	Restated 2005 HRK '000
Deferred tax assets				
Loans and advances to customers	6,316	3,899	-	2,417
Other provisions	2,565	(71)	-	2,636
Financial assets	1,420	699	-	721
Fair value reserve	55	-	55	-
Deferred tax liabilities				
Borrowings	(687)	(169)	-	(518)
Fair value reserve	-	-	2,562	(2,562)
Net deferred tax asset/(liability)	**9,669**	**4,358**	**2,617**	**2,694**

b) Recognised deferred tax assets and liabilities - 2005

Movements in temporary differences and components of deferred tax assets and deferred tax liabilities are as follows:

	2005 HRK '000	Credited/(charged) to income statement HRK '000	Credited/(charged) to equity HRK '000	Restated 2004 HRK '000
Deferred tax assets				
Loans and advances to customers	2,417	2,417	-	-
Other provisions	2,636	2,636	-	-
Financial assets	721	369	-	352
Deferred tax liabilities				
Borrowings	(518)	(518)	-	-
Fair value reserve	(2,562)	-	(803)	(1,759)
Net deferred tax asset/(liability)	**2,694**	**4,904**	**(803)**	**(1,407)**

16. OTHER ASSETS

	2006 HRK '000	2005 HRK '000
Fees receivable	47,870	51,521
Assets held for sale	46,405	1,376
Items in course of collection	16,566	1,861
Deferred fee expense	3,434	2,595
Prepaid expenses	5,347	4,843
Other receivables	14,213	5,566
Total gross amounts	**133,835**	**67,762**
Allowance for impairment losses	(3,228)	(4,317)
Total	**130,607**	**63,445**

Assets held for sale comprise non-current assets acquired in lieu of uncollectible receivables. The market value of assets held for sale, which is the amount the Bank expects to realise during 2007, exceeds the carrying amount by HRK 7 million.

Movement in allowance for impairment losses

The movement in the allowance for impairment of other assets is presented below:

	2006 HRK '000	2005 HRK '000
Balance at 1 January	4,317	1,612
Increase in impairment losses	-	2,705
Amounts recovered during the year	(478)	-
Usage of impairment losses	(611)	-
Balance at 31 December	**3,228**	**4,317**

17. FINANCIAL LIABILITIES AT FAIR VALUE THROUGH PROFIT AND LOSS

	2006 HRK ‘000	2005 HRK ‘000
Negative fair value of forward foreign exchange contracts	345	-
Negative fair value of cross currency swaps	238	-
Balance at 31 December	**583**	**-**

18. DEPOSITS FROM BANKS

	2006 HRK '000			2005 HRK '000		
	In HRK	In foreign currency	Total	In HRK	In foreign currency	Total
Demand deposits	2,461	9,261	11,722	4,561	351	4,912
Term deposits	448,537	36,145	484,682	46,000	-	46,000
Interest payable - not due	225	29	254	28	-	28
Total	**451,223**	**45,435**	**496,658**	**50,589**	**351**	**50,940**

19. DEPOSITS FROM CUSTOMERS

	2006 HRK '000			2005 HRK '000		
	In HRK	In foreign currency	Total	In HRK	In foreign currency	Total
Demand deposits						
Retail	1,860,656	112,653	1,973,309	1,355,119	77,665	1,432,784
Corporate	1,039,248	254,932	1,294,180	1,138,856	207,249	1,346,105
Restricted deposits						
Retail	3,571	126	3,697	2,975	-	2,975
Corporate	680,895	76,748	757,643	671,364	29,834	701,198
	3,584,370	**444,459**	**4,028,829**	**3,168,314**	**314,748**	**3,483,062**
Term deposits						
Retail	682,507	683,258	1,365,765	348,243	447,407	795,650
Corporate	2,245,534	485,569	2,731,103	544,056	169,009	713,065
	2,928,041	**1,168,827**	**4,096,868**	**892,299**	**616,416**	**1,508,715**
Interest payable - due	20,876	534	21,410	10,517	-	10,517
Interest payable - not due	3,087	3,747	6,834	1,863	789	2,652
Total	**6,536,374**	**1,617,567**	**8,153,941**	**4,072,993**	**931,953**	**5,004,946**

Deposits denominated in HRK include HRK 391,518 thousand linked to foreign currency by revaluation clauses (2005: HRK 245,977 thousand). Restricted deposits mainly relate to client deposits which are predetermined for special purposes, such as those based on Court orders.

20. BORROWINGS

	2006 HRK '000			2005 HRK '000		
	In HRK	In foreign currency	Total	In HRK	In foreign currency	Total
Short-term borrowings from other financial institutions	3,673	-	3,673	4,425	-	4,425
Short-term borrowings from domestic banks	476,000	-	476,000	589,000	-	589,000
Long-term borrowings from banks	-	246,060	246,060	-	254,459	254,459
Long-term borrowing from HBOR (kuna and foreign currency clause)	680,012	-	680,012	398,037	-	398,037
Other long-term liabilities - leasing	-	-	-	124	-	124
Interest payable due	1,507	5,097	6,604	1,928	1,902	3,830
Interest payable - not due	1,333	-	1,333	490	79	569
	1,162,525	**251,157**	**1,413,682**	**994,004**	**256,440**	**1,250,444**

In accordance with their terms, borrowings from the Croatian Bank for Reconstruction and Development ("HBOR") are used to fund loans to customers for eligible construction and development projects at preferential interest rates, and mostly include a one-way foreign currency clause which gives HBOR the option to revalue the borrowing at the current foreign exchange rate. This represents an embedded derivative which the Bank has not separated and has not stated at fair value. As a result of the application of these clauses, borrowings are carried at amounts HRK 346 thousand (2005: HRK 562 thousand) greater than had they been translated into HRK at the year end exchange rate disclosed in Note 1(d).

21. PROVISIONS FOR LIABILITIES AND CHARGES

	2006 HRK '000	2005 HRK '000
Provisions for court cases initiated against the Bank	8,035	7,860
Provisions for potential and other liabilities	1,120	1,197
Portfolio based provisions for off-balance-sheet risks	16,875	13,734
Balance at 31 December	**26,030**	**22,791**

Movement in provisions for liabilities and charges

The movement in provisions for liabilities and charges is as follows:

	2006 HRK '000	2005 HRK '000
Balance at 1 January	22,791	11,596
Increase in impairment losses	3,316	11,195
Usage	(77)	-
Balance at 31 December	**26,030**	**22,791**

22. OTHER LIABILITIES

	2006 HRK '000	2005 HRK '000
Suppliers	47,649	40,279
Salaries, deductions from salaries, taxes and contributions	17,681	16,105
Liabilities for retirement, severance payments and other liabilities	9,834	7,604
Fees payable	36,305	35,654
Items in the course of settlement	165,881	46,143
Deferred fee income	31,580	12,087
Other liabilities	7,436	4,572
Liabilities under called upon guarantees issued in favour of customers	18,342	20,246
Balance at 31 December	**334,708**	**182,690**

Liabilities in the course of settlement mainly relate to a liability for repayment of pensions on behalf of the Croatian Pension Fund in the amount of HRK 87 million (2005: nil) and liabilities for transfer of cash inflows from the Bank's account to non-Bank retail clients in the amount of HRK 39 million (2005: HRK 33 million).

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In the beginning of 2005 the HPB repositioning has commenced under the guidance of the new, young management. The development strategy of the Bank for the period to 2010 was adopted and the new values, vision and mission of the Bank were determined. The new corporate identity was followed by the entirely refreshed visual identity: the red square and stylized white trumpet symbolizing the Bank's modernization and growth and connecting it with the Croatian Post – the Bank's the strategic partner and with the Croatian national identity. The slogan "My bank" reflects loyalty and emotional relationship with the clients and accessibility throughout the country.

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23. INTEREST AND SIMILAR INCOME

a) Analysis by product

	2006 HRK '000	2005 HRK '000
Loans and advances to customers		
Corporate	269,988	136,672
Retail	120,617	68,260
	390,605	204,932
Placements with and loans to banks	27,970	23,647
Debt securities	72,251	98,579
Bills of exchange	16,254	17,242
Obligatory reserve with the Croatian National Bank	6,256	6,997
Total	**513,336**	**351,397**

b) Analysis by source

	2006 HRK '000	2005 HRK '000
Companies	238,639	118,387
Individuals	120,617	68,260
State and the public sector	113,342	131,531
Banks and other financial institutions	39,299	32,968
Other organisations	1,439	251
	513,336	**351,397**

24. INTEREST EXPENSE AND SIMILAR CHARGES

a) Analysis by product

	2006 HRK '000	2005 HRK '000
Borrowings	39,400	18,767
Deposits from customers		
Corporate	82,070	46,573
Retail	49,806	36,336
	131,876	82,909
Deposits from banks	8,902	1,138
Other	384	110
Total	**180,562**	**102,924**

b) Analysis by recipient

	2006 HRK '000	2005 HRK '000
Companies	44,921	25,160
Individuals	49,806	36,336
State and public sector	9,230	11,720
Banks and other financial institutions	75,657	29,257
Other organisations	948	451
	180,562	**102,924**

25. FEE AND COMMISSION INCOME

	2006 HRK '000	2005 HRK '000
Commissions from cash based payment transactions	434,877	465,674
Commissions from non-cash-based payment transactions	34,688	36,778
Commissions from retail and credit card business	52,228	41,938
Commissions from letters of credit, guarantees and foreign currency payment transactions	14,718	9,492
Other commissions	18,144	4,923
Total	**554,655**	**558,805**

26. FEE AND COMMISSION CHARGES

	2006 HRK '000	2005 HRK '000
Commissions on cash based payment transactions	394,733	427,544
Commissions on non-cash-based payment transactions	51,464	49,245
Commissions on credit card transactions	13,339	7,624
Other commissions	14,195	13,620
Total	**473,731**	**498,033**

27. GAINS LESS LOSSES ARISING FROM DEALING SECURITIES

	2006 HRK '000	2005 HRK '000
Gains less losses from financial assets at fair value through profit or loss		
Realised (loss)/gain on disposal of debt securities	(7,733)	7,469
Realised gain on disposal of equity securities	6,205	-
Realised gains on derivative instruments (classified as held for trading)	5,392	259
	3,864	**7,728**
Unrealised gains/(losses)		
- Debt securities	(4,131)	5,645
- Investment funds	7,334	420
- Equity securities	16,831	2,935
- Futures	(585)	-
- Forward foreign exchange contracts - OTC	1,730	-
	21,179	**9,000**
Total	**25,043**	**16,728**

28. GAINS LESS LOSSES ARISING FROM INVESTMENT SECURITIES

	2006 HRK '000	2005 HRK '000
Gains less losses arising from available-for-sale securities		
Realised gains on disposal of debt securities	10,430	9,462
Realised gains on disposal of equity securities	2,173	-
Total	**12,603**	**9,462**

29. OTHER OPERATING INCOME

	2006 HRK '000	2005 HRK '000
Dividend income	473	277
Exchange rate differences from the revaluation of monetary assets and liabilities, net	-	266
Derecognition of liabilities on dormant customer accounts	113	6,145
Other income	3,291	1,608
Total	**3,877**	**8,296**

30. GENERAL AND ADMINISTRATIVE EXPENSES

	2006 HRK '000	2005 HRK '000
Materials and services	86,457	48,623
Administration and marketing	36,866	15,928
Post and telecommunications	29,966	24,816
Personnel expenses	118,323	89,629
Deposit insurance expenses	10,871	9,014
Other general and administrative costs	11,063	8,092
Net foreign exchange loss from translation of monetary assets and liabilities	6,554	-
Total	**300,100**	**196,102**

a) Personnel expenses

	2006 HRK '000	2005 HRK '000
Net salaries	56,978	42,761
Taxes and contributions (including employer's contributions)	55,034	42,301
Retirement, severance payments and other expenses	2,230	1,640
Other payments to employees	3,635	2,433
Fees to Supervisory Board members	446	494
Total	**118,323**	**89,629**

Contributions are paid or payable into obligatory pension plans. Contributions are calculated as a percentage of employees' gross salaries. At 31 December 2006, the Bank had 581 employees (2005: 446).

31. IMPAIRMENT LOSSES ON LOANS AND ADVANCES TO CUSTOMERS AND OTHER ASSETS

	Notes	2006 HRK '000	2005 HRK '000
Identified losses			
Loans and advances to customers	11	24,763	(24,284)
Financial assets available for sale	9	(257)	189
Other assets	16	478	(2,705)
Total release/(charge)		**24,984**	**(26,800)**
Unidentified losses			
Loans and advances to customers	11	(35,615)	7,469
Financial assets available for sale		-	-
Other assets		-	-
Total (charge)/release		**(35,615)**	**7,469**
Loans and advances to customers		(10,852)	(16,815)
Financial assets available for sale		(257)	189
Other assets		478	(2,705)
Total charge		**(10,631)**	**(19,331)**

32. INCOME TAX EXPENSE

Total recognised income tax expense calculated at the income tax rate of 20%, comprises income tax expense recognised in the income statement and movements in income tax liabilities recognised directly in equity, as follows:

Income tax expense recognised in the income statement

	2006 HRK '000	2005 HRK '000
Current income tax expense	(30,723)	(25,620)
Deferred tax income relating to the origination and reversal of temporary differences	4,358	4,904
Total income tax expense in income statement	**(26,365)**	**(20,716)**

Movement in income tax liabilities recognised directly in equity

	2006 HRK '000	2005 HRK '000
Deferred tax income/(charges) relating to unrealised gains on available-for-sale investments recognised in fair value reserve	**2,617**	**(803)**

Reconciliation of income tax expense

The reconciliation between tax expense and accounting profit is shown as follows:

	2006 HRK '000	2005 HRK '000
Profit before tax	127,490	110,878
Income tax at 20%	(25,498)	(22,176)
Expenses not deductible for tax purposes	(5,196)	(553)
Income not subject to tax	4,329	2,013
	(26,365)	**(20,716)**
Effective income tax rate	20.7%	18.7%

33. EARNINGS PER SHARE

	2006 HRK '000	2005 HRK '000
Profit for the year attributable to ordinary shareholders	101,125	90,162
Average number of ordinary shares in issue (excluding treasury shares)	530,823	530,823
Earnings per share (in HRK)	**190.51**	**169.85**

34. EQUITY

a) Share capital

As at 31 December 2006 and 2005, authorised, issued and fully paid ordinary share capital amounted to HRK 584,779,800 and comprised 531,618 approved ordinary shares with a nominal value of HRK 1,100 each. The holders of the ordinary shares are entitled to receive dividends as declared at the General Assembly of Shareholders and are entitled to one vote per share. As of 31 December 2006, the Bank had 795 treasury shares (2005: 795) in the total amount of HRK 874 thousand (2005: HRK 874 thousand).

The shareholder structure is as follows:

	2006		2005	
	Paid capital HRK'000	**Ownership %**	**Paid capital HRK'000**	**Ownership %**
Croatian Privatisation Fund	216,354	37.00%	216,354	37.00%
Croatian Post	196,231	33.56%	196,231	33.56%
Croatian Pension Fund	163,811	28.01%	163,811	28.01%
Other	8,384	1.43%	8,384	1.43%
Total	**584,780**	**100.00%**	**584,780**	**100.00%**

b) Statutory reserve

The Bank is required to build a statutory reserve by appropriating 5% of net profit for the year until the reserve reaches 5% of share capital. Following a transfer from retained earnings of HRK 5,056 thousand, representing 5% of the profit for the year, the balance on the statutory reserve at 31 December 2006 amounted to HRK 12,776 thousand (2005: HRK 7,720 thousand), or 2.18% (2005: 1.32%) of share capital. No adjustment to the statutory reserve has been made in respect of the amounts by which profits for prior years have been restated nor has any transfer been made for amounts of total recognised income for the year and for prior years not recognised in the income statement. The statutory reserve may be used to cover prior period losses if the losses are not covered by current year profits or if other reserves are not available.

c) General banking reserve

In accordance with CNB regulations, the Bank is required to create and maintain provisions for general banking risks, as a result of the rapid growth of the Bank's balance sheet and off-balance-sheet exposure and increased exposure to risks. As a result of an increase in certain categories of risk exposure by more than 25% from 31 December 2005 to 2006, the Bank has recognised an increase in the reserve for general banking risks in the amount of HRK 59,463 thousand (2005: HRK 31,609 thousand) as an appropriation within equity from retained earnings.

d) Fair value reserve

The fair value reserve includes unrealised gains and losses on changes in the fair value of financial assets available for sale, net of tax.

e) Proposed dividends

Dividends payable are not accounted for until they have been ratified at the General Assembly of Shareholders. Management will not propose any dividend payment for the year ended 31 December 2006 (2005: Nil).

35. CONCENTRATION OF ASSETS AND LIABILITIES

The assets and liabilities of the Bank are significantly concentrated on amounts directly due from and to the Republic of Croatia. The amounts at year end, including off-balance-sheet exposure, are as follows:

	Notes	2006 HRK '000	2005 HRK '000
Giro account with the CNB	5	270,102	146,163
Obligatory reserve with the CNB	6	1,026,742	685,366
Bonds issued by the Republic of Croatia		317,778	464,641
Ministry of Finance treasury bills	8, 9	1,431,695	1,607,617
Loans and advances to the Republic of Croatia		583,368	84,251
Deposits from the Republic of Croatia		(901,976)	(924,045)
Repurchase agreements with the CNB		(476,366)	(589,229)
Undrawn lending commitments		-	400,000
Total		**2,251,343**	**1,874,764**

The Bank's exposure towards local government and state institutions not directly funded by the State Budget (excluding state owned companies) is presented below:

	2006 HRK '000	2005 HRK '000
Loans and advances	2,635	2,309
Deposits	(440,381)	(325,958)
Total	**(437,746)**	**(323,649)**

36. CASH AND CASH EQUIVALENTS

	Notes	2006 HRK '000	2005 HRK '000
Cash and receivables from banks	5	579,714	388,689
Obligatory reserve with Croatian National Bank	6	1,026,742	685,366
Placements to banks with original maturity up to 90 days		947,107	526,211
Items in course of collection	16	16,566	1,861
Total		**2,570,129**	**1,602,127**

37. COMMITMENTS AND CONTINGENCIES

	2006 HRK '000	2005 HRK '000
Guarantees denominated in HRK	396,734	186,765
Guarantees denominated in foreign currencies	19,607	6,305
Letters of credit	70,426	55,507
Accepted bills of exchange	24,285	-
Undrawn lending commitments	1,174,757	1,122,533
Other-off-balance-sheet items	1,642	2,250
Total	**1,687,451**	**1,373,360**

At 31 December 2006, the Bank recognised portfolio based provisions for off-balance-sheet risks arising from the issue of guarantees, letters of credit and undrawn lending commitments, in the amount of HRK 16,875 thousand, which are included in provisions for liabilities and charges (2005: HRK 13,734 thousand) (see Note 21).

38. DERIVATIVE INSTRUMENTS AND DEALINGS IN FOREIGN CURRENCIES

The Bank had the following derivative contracts, accounted for as trading instruments, open at year-end.

	Notional amount, remaining life					Fair values	
2006	**Up to 3 months HRK '000**	**3 - 12 months HRK '000**	**1 - 5 years HRK '000**	**Over 5 years HRK '000**	**Total HRK '000**	**Assets HRK '000**	**Liabilities HRK '000**
Forward foreign exchange contracts - OTC							
EUR	41,132	36,725	-	-	77,857	233	345
Cross currency swaps - OTC	9,940	-	-	-	9,940	-	238
Futures	94,017	-	-	-	94,017	1,496	-
	145,089	**36,725**	**-**	**-**	**181,814**	**1,729**	**583**

There were no outstanding derivative transactions as of 31 December 2005.

39. RELATED PARTY TRANSACTIONS

The Bank is the parent of the HPB Group. The key shareholders of the Bank and of the Group are the Croatian Privatisation Fund, Hrvatska pošta d.d. ("Croatian Post") and Hrvatski zavod za mirovinsko osiguranje ("HZMO") which together owned 98.57 % (2005: 98.57 %) of the Bank's shares at year end. The remaining 1.43% (2005: 1.43%) of the shares are publicly held. The Bank considers that it has an immediate related party relationship with its key shareholders; its subsidiaries and the investment funds managed by one of its subsidiaries, HPB Invest d.o.o.; the Supervisory and Management Board members and other executive management (together "key management personnel"); close family members of key management personnel; and entities controlled, jointly controlled or significantly influenced by key management personnel and their close family members, in accordance with the definitions contained in International Accounting Standard 24 "Related Party Disclosures" ("IAS 24").

a) Key transactions with immediate related parties

Croatian Post performs domestic payment transactions for and on behalf of the Bank. Risk exposure to Croatian Post mainly comprises fees receivable based on domestic payment transactions performed for and on behalf of the Bank. Liabilities towards Croatian Post are mainly in respect of demand and term deposits. Expenses include commission expense for services provided and interest expense payable on its deposits with the Bank.

Income from HZMO arises from services provided in respect of payment of pensions and other fees payable by HZMO. Liabilities comprise HZMO demand deposits in kuna.

Risk exposure to HPB Invest mainly comprises investments into investment funds managed by HPB Invest. The Bank processes payment transactions for its subsidiaries, for which it recognises income. Expenses payable to HPB Nekretnine are based on services for collateral evaluation provided by that subsidiary.

Key management personnel (directors of main organisational departments) held no ordinary shares at the year-end (2005: nil shares).

Included in loans and receivables are HRK 20,123 thousand (2005: HRK 13,765 thousand) in respect of loans and advances granted to key management personnel. During 2006 the Bank collected HRK 572 thousand (2005: HRK 247 thousand) of interest from these loans at interest rates of 4% - 10% (2005: 4% - 7.5%).

b) Amounts arising from transactions with immediate related parties

Assets and liabilities and off-balance-sheet exposure and income and expense as at and for the year ended 31 December 2006, arising from key transactions with related parties were as follows:

2006	Exposure* HRK'000	Liabilities HRK'000	Income HRK'000	Expense HRK'000
Key shareholders				
Croatian Post	62,852	157,033	2,300	331,199
HZMO	2,879	19,193	36,002	397
Subsidiaries				
HPB Invest	58,635	8,377	3,506	16
HPB Nekretnine	11,201	160	637	188
HPB Stambena stedionica	30,193	391	206	2
Key management personnel				
Short-term benefits				
(bonuses, salaries and fees)	4,273	1,627	7	24,564
Long-term benefits	15,850	1,701	565	53
Severance payments	-	-	-	8
Companies under significant influence	48,729	805	2,012	9
Total	**234,612**	**189,287**	**45,235**	**356,436**

Assets and liabilities and off-balance-sheet exposure and income and expense as at and for the year ended 31 December 2005, arising from key transactions with related parties were as follows:

2005	Exposure* HRK'000	Liabilities HRK'000	Income HRK'000	Expense HRK'000
Key shareholders				
Croatian Post	73,118	183,434	2,247	355,696
HZMO	2,986	33,024	35,257	273
Subsidiaries				
HPB Invest	42,515	534	5	7
HPB Nekretnine	550	108	1	363
Key management personnel				
Short-term benefits				
(bonuses, salaries and fees)	750	2,093	7	21,657
Long-term benefits	13,015	862	267	44
Severance payments	-	-	-	4
Companies under significant influence	46,342	5,310	758	24
Total	**179,276**	**225,365**	**38,542**	**378,068**

*Exposure comprises amounts advanced in cash or kind, commitments and contingencies, interest and other receivables, and includes HRK 32,960 thousand (2005: HRK 26,963 thousand) of off-balance-sheet receivables, whereof HRK 27,439 thousand (2005: HRK 26,350 thousand) relates to Croatian Post and key management personnel.

c) State owned companies

The three major shareholders of the Bank, who together own 98.57% of its shares, are state agencies or state owned companies, all mainly funded from the State Budget. Accordingly, transactions and balances with other state owned companies, including credit risk exposures guaranteed by the state, also represent related party relationships. The Bank has extensive banking relationships with such companies.

40. REPURCHASE AND RESALE AGREEMENTS

The Bank raises funds by selling financial instruments under agreements to repay the funds by repurchasing the instruments at future dates at the same price plus interest at a predetermined rate.

Repurchase agreements are commonly used as a tool for short-term financing of interest-bearing assets, depending on the prevailing interest rates. The financial instruments sold are not derecognised and the proceeds are accounted for as interest bearing borrowings. At 31 December 2006 assets sold under repurchase agreements were as follows:

	Fair value of underlying assets HRK'000	Carrying amount of corresponding liabilities HRK'000	Repurchase date	Repurchase price HRK'000
Debt securities at fair value through profit or loss				
2006	494,851	479,862	January and February 2007	480,016
2005	613,446	593,656	January 2006	593,889

The Bank also purchases financial instruments under agreements to resell them at future dates ("reverse repurchase agreements"). The seller commits to repurchase the same or similar instruments at an agreed future date. Reverse repurchase agreements are entered into as a facility to provide funds to customers and are accounted for as loans and advances to customers; the underlying financial instruments are not recognised. At 31 December 2006 assets purchased subject to agreements to resell them were as follows:

	Carrying amounts of receivable HRK'000	Fair value of assets held as collateral HRK'000	Repurchase date	Repurchase price HRK'000
Loans and advances to customers				
2006	80,807	81,549	January 2007	80,852
2005	7,525	8,023	February 2006	7,597

41. SUBSEQUENT EVENTS

Given that both the Bank's share capital exceeds HRK 30 million and that during the last quarter of 2006 at each month end, the Bank's share capital was held by more than 100 shareholders, the Bank qualified as a public company required to list its shares on the public companies quotation of the Zagreb Stock Exchange. The Bank is in the process of obtaining approval from the Croatian Agency for Supervision of Financial Services, upon which it will list its shares on the public companies quotation of the Zagreb Stock Exchange.

42. MANAGED FUNDS FOR AND ON BEHALF OF CORPORATE AND RETAIL CUSTOMERS

The Bank provides trust and custody services to companies, banks, individuals, and investment funds (Group investment funds) whereby it holds and manages assets or invests funds received in various financial instruments at the direction of the customer. The Bank receives fee income for providing these services. Trust assets are not assets of the Bank and are not recognised in the balance sheet of the Bank. The Bank is not exposed to any credit risk relating to such placements, as it does not guarantee these investments.

At 31 December 2006, the total assets under custody held by the Bank on behalf of customers were HRK 2 billion, including custody of HPB funds (2005: HRK 557 million).

In addition, at 31 December 2006, total assets of investment and pension funds to which the Bank is a depository bank, amounted to HRK 1.3 billion (2005: HRK 398 million).

Further, the Bank manages a number of loans on behalf of third parties as follows:

	2006 HRK '000	**2005 HRK '000**
Assets		
Corporate	194,131	194,610
Retail	453,921	406,943
Giro accounts	22,640	15,232
Total assets	**670,692**	**616,785**
Liabilities		
Croatian Employment Office	36,243	49,676
Counties	36,648	43,389
Government of the Republic of Croatia	479,326	428,689
HBOR	11,659	8,072
Development and Employment Fund	96,423	86,228
Other liabilities	10,393	731
Total liabilities	**670,692**	**616,785**

43. RISK MANAGEMENT POLICIES

Details of the Bank's exposure to risk and methods used by management to control risk are described below. The most important types of financial risk to which the Bank is exposed are credit risk, liquidity risk and market risk. Market risk includes currency risk, interest rate risk and equity price risk.

An integrated system of risk management was established by introducing policies and procedures, and determining the limits of risk levels acceptable to the Bank. The limits are set according to the amount of regulatory capital and apply to all types of risk. Methodologies and models for managing operational risk have been developed.

Credit risk

The Bank is subject to credit risk through its lending and investing activities and in cases where it acts as an intermediary on behalf of customers or other third parties. The risk that counterparties to financial instruments might default on their obligations is monitored on an ongoing basis. To manage the level of credit risk, the Bank deals with counterparties of good credit standing, and when appropriate, obtains collateral.

The Bank's primary exposure to credit risk arises through its loans and advances. The amount of credit exposure in this regard is represented by the carrying amounts of the assets. In addition the Bank is exposed to off-balance-sheet credit risk through commitments to extend credit and guarantees issued, which is presented in Note 37.

The Bank manages its credit risk exposure in accordance with its adopted policies. Credit exposures to portfolios and banks are reviewed on a regular basis taking into account limits set. Credit risk exposure by portfolio and to individual banks and customers is regularly checked, in accordance with existing limits. All breaches are reported to the relevant authorised decision making levels of the Bank.

The Credit Committee meets once a week or, if necessary, on a more frequent basis. Its members comprise the Chief Financial Officer, the Executive Director of the Corporate Division and the Executive Director of the Risk Management Division. The Credit Committee authorises each significant increase in credit exposure. The Credit Committee monitors changes in credit exposure and reviews impairment losses. The Bank applies prudent methods and models in evaluating credit risk. It is the Bank's policy to require adequate collateral from its customers before granting a loan. Collateral for loans, guarantees and letters of credit is usually in the form of charges over cash, stock, quoted securities, real estate and other assets.

Liquidity risk

Liquidity risk arises in the general funding of the Bank's activities and in the management of its positions. It includes both the risk of being unable to fund assets at appropriate maturities and rates and the risk of being unable to liquidate an asset at a reasonable price and in an appropriate timeframe. The Bank has access to a diverse funding base. Funds are raised using a broad range of instruments including deposits, borrowings and share capital. The Bank continually assesses liquidity risk by identifying and monitoring changes in the level of funding required to meet business goals and strategic targets. In addition the Bank holds a portfolio of liquid assets as part of its liquidity risk management.

The Bank adjusts its business activities in compliance with liquidity risk legislation and internal policies for the maintenance of liquidity reserves, matching of liabilities and assets, setting of position limits and achievement of preferred liquidity ratios. Treasury Division is responsible for both the management of the Bank's own liquidity and transactions on behalf of customers.

Market risk

All dealing instruments are subject to market risk, that is, the risk that future changes in market conditions may make an instrument less valuable or more onerous. Dealing financial instruments are recognised at fair value, and all changes in market conditions directly affect dealing income. The Bank manages its use of dealing instruments in response to changing market conditions. Exposure to market risk is formally managed in accordance with risk limits set by senior management by buying or selling instruments.

Currency risk

The Bank is exposed to currency risk through transactions in foreign currencies. Foreign currency exposure arises from credit, deposit-taking, investment and dealing activities. It is monitored daily in accordance to legislation and internally set limits, for each currency and for the total balance sheet denominated in or linked to foreign currency.

The Bank directs its business activities trying to minimise the gap between assets and liabilities denominated in or linked to foreign currency.

Interest rate risk

The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest-earning assets and interest-bearing liabilities mature or reprice at different times or in differing amounts. In the case of floating rate assets and liabilities the Bank is also exposed to basis risk, which is the difference in repricing characteristics of the various floating rate indices.

Risk management activities are aimed at optimising net interest income, given market interest rate levels consistent with the Bank's business strategies.

Asset-liability risk management activities are conducted in the context of the Bank's sensitivity to interest rate changes. Exposure to interest rate risk is monitored and measured using repricing maturity gap analysis.

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 available for sale.

Derivative financial instruments

The Bank enters into derivative financial instruments mostly for risk management purposes and on behalf of customers. Derivative financial instruments used by the Bank include swaps and forwards whose value changes in response to changes in interest rates and foreign exchange rates. Derivatives are either standardised contracts transacted through regulated exchanges or individually negotiated over-the-counter contracts.

Regulatory requirements

The Bank is required to comply with regulations of the Croatian National Bank which prescribe limits and other restrictions related to minimum capital adequacy, classification of loans and contingent liabilities in the off-balance-sheet records, as well as provisions to offset credit risk, liquidity risk, interest rate risk and risks related to foreign exchange position.

44. CURRENCY RISK

Assets and liabilities with foreign currency clause include HRK 687 thousand (2005: HRK 4,351 thousand) of loans and advances to customers and borrowings, which the Bank, and lenders of the Bank have the option to revalue in line with HRK movements against EUR, if HRK depreciates against to EUR beyond a certain level.

At 31 December 2006, the amounts of total assets and liabilities denominated in HRK and foreign currencies (amounts denominated in HRK but with foreign currency clauses, disclosed in the table below, are mainly linked to EUR) were as follows:

2006	**HRK HRK '000**	**HRK with foreign currency clause HRK '000**	**EUR HRK '000**	**Other foreign currencies HRK '000**	**Total HRK '000**
ASSETS					
Cash and receivables from banks	516,958	-	52,588	10,168	**579,714**
Obligatory reserve with Croatian National Bank	913,404	-	113,338	-	**1,026,742**
Placements with and loans to other banks	359,203	-	720,990	63,143	**1,143,336**
Financial assets at fair value through profit and loss	1,660,596	68,914	81,106	-	**1,810,616**
Financial assets available for sale	224,438	20,557	53,250	1,429	**299,674**
Financial assets held to maturity	150	-	-	-	**150**
Loans and advances to customers	4,238,804	1,525,387	59,463	174,570	**5,998,224**
Investments in subsidiaries	35,050	-	-	-	**35,050**
Property, plant and equipment	172,288	-	-	-	**172,288**
Intangible assets	71,783	-	-	-	**71,783**
Net deferred tax asset	9,669	-	-	-	**9,669**
Other assets	129,969	72	526	40	**130,607**
TOTAL ASSETS (1)	**8,332,312**	**1,614,930**	**1,081,261**	**249,350**	**11,277,853**

2006	HRK HRK '000	HRK with foreign currency clause HRK '000	EUR HRK '000	Other foreign currencies HRK '000	Total HRK '000
LIABILITIES					
Financial liabilities at fair value through profit or loss	344	-	-	239	**583**
Deposits from banks	451,223	-	32,665	12,770	**496,658**
Deposits from customers	6,144,856	391,518	1,436,415	181,152	**8,153,941**
Borrowings	705,930	456,595	251,157	-	**1,413,682**
Provisions for liabilities and charges	26,030	-	-	-	**26,030**
Other liabilities	315,061	18,365	1,255	27	**334,708**
Current tax liability	12,169	-	-	-	**12,169**
Total equity	840,082	-	-	-	**840,082**
TOTAL LIABILITIES AND EQUITY (2)	**8,495,695**	**866,478**	**1,721,492**	**194,188**	**11,277,853**
NET FOREIGN EXCHANGE POSITION (1) - (2)	**(163,383)**	**748,452**	**(640,231)**	**55,162**	**-**

44. CURRENCY RISK (CONTINUED)

At 31 December 2005, the amounts of total assets and liabilities denominated in HRK and foreign currencies (amounts denominated in HRK but with foreign currency clauses, disclosed in the table below, are mainly linked to EUR) were as follows:

2005	HRK HRK '000	HRK with foreign currency clause HRK '000	EUR HRK '000	Other foreign currencies HRK '000	Total HRK '000
ASSETS					
Cash and receivables from banks	354,519	-	25,873	8,297	**388,689**
Obligatory reserve with Croatian National Bank	611,971	-	73,395	-	**685,366**
Placements with and loans to other banks	129,300	-	450,359	77,806	**657,465**
Financial assets at fair value through profit and loss	1,222,285	117,120	99,095	-	**1,438,500**
Financial assets available for sale	822,214	42,981	56,465	-	**921,660**
Loans and advances to customers	2,005,032	858,426	26,549	52,882	**2,942,889**
Investments in subsidiaries	5,050	-	-	-	**5,050**
Property, plant and equipment	157,331	-	-	-	**157,331**
Intangible assets	19,837	-	-	-	**19,837**
Net deferred tax asset	2,694	-	-	-	**2,694**
Other assets	63,150	49	232	14	**63,445**
TOTAL ASSETS (1)	**5,393,383**	**1,018,576**	**731,968**	**138,999**	**7,282,926**

2005	HRK HRK '000	HRK with foreign currency clause HRK '000	EUR HRK '000	Other foreign currencies HRK '000	Total HRK '000
LIABILITIES					
Deposits from banks	50,589	-	226	125	**50,940**
Deposits from customers	3,827,016	245,977	798,731	133,222	**5,004,946**
Borrowings	651,624	342,380	256,440	-	**1,250,444**
Provisions for liabilities and charges	22,791	-	-	-	**22,791**
Other liabilities	162,128	21	16,972	3,569	**182,690**
Current tax liability	21,688	-	-	-	**21,688**
Total equity	749,427	-	-	-	**749,427**
TOTAL LIABILITIES AND EQUITY (2)	**5,485,263**	**588,378**	**1,072,369**	**136,916**	**7,282,926**
NET FOREIGN EXCHANGE POSITION (1) - (2)	**(91,880)**	**430,198**	**(340,401)**	**2,083**	**-**

45. MATURITY ANALYSIS

A maturity analysis of assets and liabilities, based on their remaining contractual maturity, except for financial assets at fair value through profit and loss which are analysed as current based on their classification and the Bank's trading intention, as at 31 December 2006 is presented below:

2006	0-30 days HRK '000	31-90 days HRK '000	91-360 days HRK '000	1 to 3 years HRK '000	More than 3 years HRK '000	Total HRK '000
ASSETS						
Cash and receivables from banks	579,714	-	-	-	-	**579,714**
Obligatory reserve with Croatian National Bank	1,026,742	-	-	-	-	**1,026,742**
Placements with and loans to other banks	942,799	26,850	73,000	-	100,687	**1,143,336**
Financial assets at fair value through profit and loss	1,805,777	4,839	-	-	-	**1,810,616**
Financial assets available for sale	53,877	54,899	91,282	-	99,616	**299,674**
Financial assets held to maturity	150	-	-	-	-	**150**
Loans and advances to customers	802,064	1,196,026	1,493,200	1,141,477	1,365,457	**5,998,224**
Investments in subsidiaries	-	-	-	-	35,050	**35,050**
Property, plant and equipment	-	-	-	-	172,288	**172,288**
Intangible assets	-	-	-	-	71,783	**71,783**
Net deferred tax asset	-	-	-	-	9,669	**9,669**
Other assets	127,227	109	492	1,283	1,496	**130,607**
TOTAL ASSETS (1)	**5,338,350**	**1,282,723**	**1,657,974**	**1,142,760**	**1,856,046**	**11,277,853**

2006	0-30 days HRK ‘000	31-90 days HRK ‘000	91-360 days HRK ‘000	1 to 3 years HRK ‘000	More than 3 years HRK ‘000	Total HRK ’000
LIABILITIES						
Financial liabilities at fair value through profit or loss	583	-	-	-	-	**583**
Deposits from banks	141,934	62,786	291,938	-	-	**496,658**
Deposits from customers	5,124,046	930,044	1,711,961	383,180	4,710	**8,153,941**
Borrowings	487,648	11,203	122,770	296,315	495,746	**1,413,682**
Provisions for liabilities and charges	-	-	-	-	26,030	**26,030**
Other liabilities	283,323	2,124	9,499	12,879	26,883	**334,708**
Current tax liability	-	-	12,169	-	-	**12,169**
Total equity	-	-	-	-	840,082	**840,082**
TOTAL LIABILITIES AND EQUITY (2)	**6,037,534**	**1,006,157**	**2,148,337**	**692,374**	**1,393,451**	**11,277,853**
MATURITY GAP (1) - (2)	**(699,184)**	**276,566**	**(490,363)**	**450,386**	**462,595**	**-**
CUMULATIVE MATURITY GAP	**(699,184)**	**(422,618)**	**(912,981)**	**(462,595)**	**-**	**-**

45. MATURITY ANALYSIS (CONTINUED)

A maturity analysis of assets and liabilities, based on their remaining contractual maturity, except for financial assets at fair value through profit and loss which are analysed as current based on their classification and the Bank's trading intention, as at 31 December 2005 is presented below:

2005	0-30 days HRK '000	31-90 days HRK '000	91-360 days HRK '000	1 to 3 years HRK '000	More than 3 years HRK '000	Total HRK '000
ASSETS						
Cash and receivables from banks	388,689	-	-	-	-	**388,689**
Obligatory reserve with Croatian National Bank	685,366	-	-	-	-	**685,366**
Placements with and loans to other banks	513,671	126,794	-	-	17,000	**657,465**
Financial assets at fair value through profit and loss	1,432,855	5,645	-	-	-	**1,438,500**
Financial assets available for sale	68,816	39,779	554,757	8,095	250,213	**921,660**
Loans and advances to customers	311,748	437,361	1,300,211	485,284	408,285	**2,942,889**
Investments in subsidiaries	-	-	-	-	5,050	**5,050**
Property, plant and equipment	-	-	-	-	157,331	**157,331**
Intangible assets	-	-	-	-	19,837	**19,837**
Net deferred tax asset	-	-	-	-	2,694	**2,694**
Other assets	59,500	52	234	599	3,060	**63,445**
TOTAL ASSETS (1)	**3,460,645**	**609,631**	**1,855,202**	**493,978**	**863,470**	**7,282,926**

2005	0-30 days HRK '000	31-90 days HRK '000	91-360 days HRK '000	1 to 3 years HRK '000	More than 3 years HRK '000	Total HRK '000
LIABILITIES						
Deposits from banks	50,912	28	-	-	-	**50,940**
Deposits from customers	3,888,290	243,836	640,416	207,259	25,145	**5,004,946**
Borrowings	623,734	4,152	29,703	167,899	424,956	**1,250,444**
Provisions for liabilities and charges	-	-	-	-	22,791	**22,791**
Other liabilities	150,321	551	5,669	11,387	14,762	**182,690**
Current tax liability	-	-	21,688	-	-	**21,688**
Total equity	-	-	-	-	749,427	**749,427**
TOTAL LIABILITIES AND EQUITY (2)	**4,713,257**	**248,567**	**697,476**	**386,545**	**1,237,081**	**7,282,926**
MATURITY GAP (1) - (2)	**(1,252,612)**	**361,064**	**1,157,726**	**107,433**	**(373,611)**	**-**
CUMULATIVE MATURITY GAP	**(1,252,612)**	**(891,548)**	**266,178**	**373,611**	**-**	

46. INTEREST RATE GAP ANALYSIS

The following tables present the Bank's assets and liabilities and equity analysed according to repricing periods determined as the earlier of remaining contractual maturity and contractual repricing.

The tables are management's estimate of the interest rate risk for the Bank as at 31 December 2006 and are not necessarily indicative of the positions at other times but provide some indication of the sensitivities of the Bank's earnings to movements in interest rates. Earnings will also be affected by the currency of the assets and liabilities and equity. The Bank has a significant proportion of interest-earning assets and interest-bearing liabilities in foreign currency.

The period of interest rate repricing, analysis of interest rate risk and amounts subject to fixed interest rates as at 31 December 2006 are presented below:

2006 HRK '000	**0-30 days**	**31-90 days**	**91-360 days**	**1 to 3 years**	**More than 3 years**	**Without interest**	**Total**	**Fixed interest**
ASSETS								
Cash and receivables from banks	310,719	-	-	-	-	268,995	**579,714**	-
Obligatory reserve with Croatian National Bank	993,390	-	-	-	-	33,352	**1,026,742**	-
Placements with and loans to other banks	1,048,486	17,000	73,000	-	-	4,850	**1,143,336**	1,037,257
Financial assets at fair value through profit and loss	1,720,517	-	-	-	-	90,099	**1,810,616**	1,720,517
Financial assets available for sale	53,877	52,468	91,282	-	97,313	4,734	**299,674**	294,940
Financial assets held to maturity	150	-	-	-	-	-	**150**	150
Loans and advances to customers	5,147,322	502,065	82,924	13,339	205,895	46,679	**5,998,224**	810,175
Investments in subsidiaries	-	-	-	-	-	35,050	**35,050**	-
Property, plant and equipment	-	-	-	-	-	172,288	**172,288**	-
Intangible assets	-	-	-	-	-	71,783	**71,783**	-

2006 HRK '000	0-30 days	31-90 days	91-360 days	1 to 3 years	More than 3 years	Without interest	Total	Fixed interest
Net deferred tax asset	-	-	-	-	-	9,669	**9,669**	-
Other assets	-	-	-	-	-	130,607	**130,607**	-
TOTAL ASSETS (1)	**9,274,461**	**571,533**	**247,206**	**13,339**	**303,208**	**868,106**	**11,277,853**	**3,863,039**
LIABILITIES								
Financial liabilities at fair value through profit or loss	-	-	-	-	-	583	**583**	-
Deposits from banks	141,934	62,532	291,938	-	-	254	**496,658**	484,683
Deposits from customers	6,097,743	531,319	1,366,779	127,339	2,517	28,244	**8,153,941**	2,432,879
Borrowings	1,402,072	3,673	-	-	-	7,937	**1,413,682**	479,673
Provisions for liabilities and charges	-	-	-	-	-	26,030	**26,030**	-
Other liabilities	-	-	-	-	-	334,708	**334,708**	-
Current tax liability	-	-	-	-	-	12,169	**12,169**	-
Total equity	-	-	-	-	-	840,082	**840,082**	-
TOTAL LIABILITIES AND EQUITY (2)	**7,641,749**	**597,524**	**1,658,717**	**127,339**	**2,517**	**1,250,007**	**11,277,853**	**3,397,235**
INTEREST RATE GAP (1) - (2)	**1,632,712**	**(25,991)**	**(1,411,511)**	**(114,000)**	**300,691**	**(381,901)**	**-**	**465,804**

46. INTEREST RATE GAP ANALYSIS (CONTINUED)

The period of interest rate repricing, analysis of interest rate risk and amounts subject to fixed interest rates as at 31 December 2005 are presented below:

2005 HRK '000	**0-30 days**	**31-90 days**	**91-360 days**	**1 to 3 years**	**More than 3 years**	**Without interest**	**Total**	**Fixed interest**
ASSETS								
Cash and receivables from banks	167,447	-	-	-	-	221,242	**388,689**	-
Obligatory reserve with Croatian National Bank	684,944	-	-	-	-	422	**685,366**	-
Placements with and loans to other banks	602,925	35,000	-	-	17,000	2,540	**657,465**	573,671
Financial assets at fair value through profit and loss	1,419,673	-	-	-	-	18,827	**1,438,500**	1,419,673
Financial assets available for sale	68,816	36,965	554,757	8,095	249,339	3,688	**921,660**	917,972
Loans and advances to customers	2,782,552	9,919	89,135	21,377	23,585	16,321	**2,942,889**	141,956
Investments in subsidiaries	-	-	-	-	-	5,050	**5,050**	-
Property, plant and equipment	-	-	-	-	-	157,331	**157,331**	-
Intangible assets	-	-	-	-	-	19,837	**19,837**	-
Net deferred tax asset	-	-	-	-	-	2,694	**2,694**	-
Other assets	-	-	-	-	-	63,445	**63,445**	-
TOTAL ASSETS (1)	**5,726,357**	**81,884**	**643,892**	**29,472**	**289,924**	**511,397**	**7,282,926**	**3,053,272**

2005 HRK '000	0-30 days	31-90 days	91-360 days	1 to 3 years	More than 3 years	Without interest	Total	Fixed interest
LIABILITIES								
Deposits from banks	50,912	-	-	-	-	28	**50,940**	47,914
Deposits from customers	4,668,502	2,290	284,266	33,867	2,852	13,169	**5,004,946**	360,367
Borrowings	1,245,951	60	34	-	-	4,399	**1,250,444**	593,549
Provisions for liabilities and charges	-	-	-	-	-	22,791	**22,791**	-
Other liabilities	-	-	-	-	-	182,690	**182,690**	-
Current tax liability	-	-	-	-	-	21,688	**21,688**	-
Total equity	-	-	-	-	-	749,427	**749,427**	-
TOTAL LIABILITIES AND EQUITY (2)	**5,965,365**	**2,350**	**284,300**	**33,867**	**2,852**	**994,192**	**7,282,926**	**1,001,830**
INTEREST RATE GAP (1) - (2)	**(239,008)**	**79,534**	**359,592**	**(4,395)**	**287,072**	**(482,795)**	**-**	**2,051,442**

47. AVERAGE INTEREST RATES

At 31 December 2006, average interest rates calculated as the weighted average of each category of interest-earning asset and interest-bearing liability, are presented below:

Assets	**Average interest rates 2006**	**Average interest rates 2005**
Cash and receivables from banks	0.50%	0.50%
Obligatory reserve with Croatian National Bank	0.83%	0.78%
Placements with and loans to other banks	3.68%	3.12%
Financial assets at fair value through profit and loss	4.15%	5.14%
Financial assets available for sale	6.92%	5.65%
Financial assets held to maturity	9.00%	-
Loans and advances to customers	7.30%	7.60%
Liabilities		
Deposits from banks	4.03%	3.21%
Deposits from customers	2.54%	1.80%
Borrowings	3.07%	3.08%

48. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value represents the amount at which an asset could be exchanged or a liability settled on an arm's length basis.

Financial assets at fair value through profit or loss and available for sale are measured at fair value. Originated loans and receivables and held-to-maturity assets are measured at amortised cost less impairment.

The following summarises the major methods and assumptions used in estimating the fair values of financial instruments.

Loans and advances

The fair value of loans and advances is calculated based on discounted expected future cash flows. Loan repayments are assumed to occur at contractual repayment dates. For loans that do not have fixed repayment dates or that are subject to prepayment risk, repayments are estimated based on experience in previous periods when interest rates were at levels similar to current levels, adjusted for any differences in interest rate outlook. Expected future cash flows are estimated considering credit risk and any indication of impairment including the portfolio based impairment allowances for performing loans calculated at rates prescribed by the CNB. Expected future cash flows for homogeneous categories of loans, such as residential mortgage loans, are estimated on a portfolio basis and discounted at current rates offered for similar loans to new borrowers with similar credit profiles. The estimated fair values of loans reflect changes in credit status since the loans were made and changes in interest rates in the case of fixed rate loans. As the Bank has a very limited portfolio of loans and advances with fixed rates and longer-term maturity, the fair value of loans and advances is not significantly different from their carrying value. Differences between the fair value of future losses from currently performing loans in the portfolio and the effect of the portfolio based provisions recognised in accordance with CNB rules, are not taken into account.

Bank and customer deposits

For demand deposits and deposits with no defined maturities, fair value is taken to be the amount payable on demand at the balance sheet date. The estimated fair value of fixed-maturity deposits is based on discounted cash flows using rates currently offered for deposits of similar remaining maturities. The value of long-term relationships with depositors is not taken into account in estimating fair values. As most of the Bank's deposits are given with variable rate, being the market rate, there is no significant difference between the fair value of these deposits and their carrying value.

Borrowings

Most of the Bank's long-term debt has no quoted market prices and fair value is estimated as the present value of future cash flows, discounted at interest rates available at the balance sheet date to the Bank for new debt of similar type and remaining maturity. Again, as the Bank's long-term debt is with variable interest there is no significant difference between the carrying and fair value.

The following table represents the Bank's estimate of the fair value of financial instruments as of 31 December 2006 and 31 December 2005.

	2006 HRK '000			2005 HRK '000		
	Carrying amount	Fair value	Unrecognised gains/ (losses)	Carrying amount	Fair value	Unrecognised gains/ (losses)
Cash and receivables from banks	579,714	579,714	-	388,689	388,689	-
Obligatory reserve with the Croatian National Bank	1,026,742	1,026,742	-	685,366	685,366	-
Placements with and loans to other banks	1,143,336	1,141,233	(2,103)	657,465	655,348	(2,117)
Financial assets at fair value through profit and loss	1,810,616	1,810,616	-	1,438,500	1,438,500	-
Financial assets available for sale	299,674	299,674	-	921,660	921,660	-
Financial assets held to maturity	150	130	(20)	-	-	-
Loans and advances to customers	5,998,224	5,947,397	(50,827)	2,942,889	2,933,660	(9,229)
Financial liabilities at fair value through profit and loss	583	583	-	-	-	-
Deposits from banks	496,658	490,620	6,038	50,940	50,940	-
Deposits from customers	8,153,941	8,110,147	43,794	5,004,946	4,996,475	8,471
Borrowings	1,413,682	1,413,667	15	1,250,444	1,250,444	-
Total			**(3,103)**			**(2,875)**

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HRVATSKA POŠTANSKA BANKA HPB HRVATSKA POŠTANSKA BANKA

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Today, Hrvatska poštanska banka is the largest domestic bank and, according to its business results and total assets amounting to more than HRK 11,3 billion, it ranks seventh in the Republic of Croatia. The Bank's business strategy is focused on intensive development of its business network and distribution channels, strenghtening of its investment banking and SME position, development of retail products and services and creation of an image of a modern, highly efficient and the most accessible business bank in the Republic of Croatia.

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